BEFORE THE PUBLIC SERVICE COMMISSION
STATE OF MISSOURI

In the Matter of the Application of Kansas City Power & Light Company and KCP&L Greater Missouri Operations Company for the Issuance of an Accounting Authority Order Relating to their Electrical Operations and for a Contingent Waiver of the Notice Requirement of 4 CSR 240-4.020(2).	)))))))	**Case No. EU-2014-0077**

STAFF'S BRIEF

COMES NOW the Staff of the Missouri Public Service Commission, by and through counsel, and for its *Brief* states as follows:

INTRODUCTION

What is the issue in this case?

This case is about accounting. Stated briefly, the Applicants[1] seek an Accounting Authority Order ("AAO") from the Commission authorizing them to deviate from the accounting rules they must otherwise follow.[2] If they are successful, the AAO will permit the Applicants to defer certain costs and carry them as a regulatory asset rather than expensing them in the period in which they were incurred.[3] The Applicants' ultimate goal, of course, is to recover those costs in rates.

What are those costs? They are the portion of Applicants' transmission costs

[1] The Applicants are Kansas City Power & Light Company ("KCP&L") and KCP&L Greater Missouri Operations Company ("GMO"), both of which are regulated electric utilities owned by Great Plains Energy, Inc.

[2] *Oligschlaeger Rebuttal,* p. 4.

[3] *Oligschlaeger Rebuttal,* p. 5. Applicants want relief that is both retrospective and prospective in that they desire to defer excess transmission costs starting January 26, 2013, until their next rate cases, whenever those will be. Tr. 187 (Ives). NOTE: All transcript references are to Transcript Volume 2.

that exceeds the amount allowed in base rates at the Applicants' last rate cases.[4] The Applicants contend that transmission costs are rising by 16% each year and that they will continue to do so until at least 2022 and probably longer.[5] Without the requested AAO, the excess portion of those costs will simply be lost.[6]

Specifically, the costs that the Applicants seek to defer through an AAO are transmission customer costs, including charges from SPP for base plan funding and also some fees for services, as well as charges related to transmission obtained from other Regional Transmission Organizations ("RTOs")[7] such as MISO[8] and from other utilities.[9] Additionally, they include SPP administrative costs and FERC assessment fees.[10] The main driver appears to be SPP Schedule 11 charges.[11] SPP Schedule 11,

[4] The Commission has not granted a deferral for these sorts of costs in the past. Tr. 286-287 (Oligschlaeger).

[5] Tr. 124-125 (Bresette): The Applicants plan for transmission costs on a five-year forward horizon, based on projections supplied by the Southwest Power Pool ("SPP"). Tr. 3:131-132 (Carlson): Transmission costs should eventually return to 2011-2012 levels, but not until 2030 or 2040 because of the amortization of the costs of SPP's current build-out. Tr. 162 (Ives): 16% average annual increase between now and 2022.

[6] Ameren Missouri recovers transmission costs in excess of base rates through its Fuel Adjustment Clause ("FAC"). Tr. 151-152 (Ives); Tr. 249 (Oligschlaeger). However, Applicant KCP&L is barred from seeking a FAC prior to June 1, 2015. Tr. 152-153 (Ives); Tr. 247 (Oligschlaeger). KCP&L will likely seek a FAC as soon as it is free to do so. Tr. 172 (Ives).

[7] *Oligschlaeger Rebuttal,* p. 8: "RTOs are transmission providers that administer transmission service over a defined region generally comprising the service territories of its transmission owning members. KCPL and GMO belong to the SPP RTO. SPP administers transmission service over an eight-state region including parts of Missouri. KCPL and GMO, as well as other entities belonging to SPP, have transferred functional control over their transmission assets to SPP. The transmission service paid by the Companies for transmission service within the SPP region is provided under the terms of SPP's Open Access Transmission Tariff (OATT)."

[8] "MISO" is the Mid-continent Independent System Operator, an RTO.

[9] Tr. 158 (Ives).

[10] Tr. 158-159 (Ives). "FERC" is the Federal Energy Regulatory Commission.

[11] *Stahlman Rebuttal,* p. 5.

Base Plan Zonal Charge and Region-wide Charge, consists of the point-to-point and network charges that compensate transmission owners for construction of Base Plan, Balanced Portfolio, Priority, or Integrated Transmission Planning ("ITP") projects.[12] Schedules JRC-1 and JRC-2 attached to the testimony of Applicants' witness John Carlson contain projections of future increases to Schedule 11 charges.[13]

Public Utility Accounting:

The control of public utility accounting is a fundamental aspect of the Commission's regulatory responsibility. To that end, the General Assembly has equipped the Commission with plenary authority to prescribe the accounting system that electric utilities must use.[14] Pursuant to that authority, the Commission has promulgated its Rule 4 CSR 240-20.030, *Uniform System of Accounts – Electrical Corporations,* which provides:

> (1) Beginning January 1, 1994, every electrical corporation subject to the commission's jurisdiction shall keep all accounts in conformity with the Uniform System of Accounts Prescribed for Public Utilities and Licensees subject to the provisions of the Federal Power Act, as prescribed by the Federal Energy Regulatory Commission (FERC) and published at 18 CFR Part 101 (1992) and 1 FERC Stat. & Regs. paragraph 15,001 and following (1992), except as otherwise provided in this rule. This uniform system of accounts provides instruction for recording financial information about electric utilities. It contains definitions, general instructions, electric plant instructions, operating

[12] *Stahlman Rebuttal,* p. 6.

[13] *Id.*

[14] Section 393.140(4), RSMo.: "[The commission shall h]ave power, in its discretion, to prescribe uniform methods of keeping accounts, records and books, to be observed by gas corporations, electrical corporations, water corporations and sewer corporations engaged in the manufacture, sale or distribution of gas and electricity for light, heat or power, or in the distribution and sale of water for any purpose whatsoever, or in the collection, carriage, treatment and disposal of sewage for municipal, domestic or other necessary beneficial purpose. * * *"

> expense instructions, and accounts that comprise the balance sheet, electric plant, income, operating revenues, and operation and maintenance expenses.

Rule 4 CSR 240-40.030 also provides that "(5) The commission may waive or grant a variance from the provisions of this rule, in whole or in part, for good cause shown, upon a utility's written application."

The General Assembly has also granted to the Commission specific authority, after hearing, to direct the accounting treatment of any particular transaction.[15] Pursuant to that authority, and the authority at Rule 4 CSR 240-40.030(5) set out above, the Commission has from time-to-time granted AAOs that permit an electric utility to account for some transaction in a manner not otherwise permitted by the Uniform System of Accounts ("USOA") or by other mandatory accounting rules.[16] Mr. Oligschlaeger testified:

> The most common example of AAOs in this jurisdiction are orders from the Commission allowing a company to defer on its books costs associated with "extraordinary events," such as natural disasters (or so-called "acts of God") or other extraordinary events involving utility infrastructure.[17]

The ultimate issue for decision in this case is the Applicants' request for an AAO permitting them to treat a portion of their transmission expenses as a regulatory asset and thus to preserve these expenses for consideration in their next general rate case.

[15] Section 393.140(8), RSMo.: "[The commission shall] * * * have power, after hearing, to prescribe by order the accounts in which particular outlays and receipts shall be entered, charged or credited."

[16] *Oligschlaeger Rebuttal,* p. 4. Staff expert Mark Oligschlaeger explained that, for example, AAOs were used to permit utilities to continue their traditional accounting practices for pensions and other post-employment benefits ("OPEBs") despite changes in applicable financial accounting standards. Tr. 250-252.

[17] *Oligschlaeger Rebuttal,* p. 4.

The rate case paradigm:

The Applicants' request for an AAO cannot be fully understood except in the context of cost-of-service ratemaking. Utility rates are based upon the actual results of a historical test year, which are updated, annualized and normalized to produce an ideal or *pro forma* year that is predictive of the costs of the utility's future operations.[18] Based on this ideal year, rates are designed to recover the actual cost of serving the utility's customers, plus a reasonable profit. AAOs figure into the ratemaking paradigm in this way: costs incurred outside of the test year are nonetheless brought forward for consideration and possible inclusion in the revenue requirement.[19] An AAO, therefore, is both a deviation from normal accounting rules and a deviation from normal ratemaking rules. It is a deviation from normal accounting rules because an AAO allows costs to be recorded in a period other than that in which they were actually incurred.[20] It is a deviation from normal ratemaking rules because an AAO allows costs from outside the test year to be considered for recovery in the revenue requirement.

Another bite of the apple:

This is not the first time that the Applicants have requested special accounting treatment for their transmission costs. In their last rate cases, referred to above, they

[18] *See* Lowell E. Alt, Jr., ***Energy Utility Rate Setting: A Practical Guide to the Retail Rate-Setting Process for Regulated Electric and Natural Gas Utilities*** (Lulu, 2006).

[19] Utility rates are made in a two-step process, the first of which is the determination of the revenue requirement, that is, the amount of revenue necessary to cover the cost of service plus a fair return or profit. The second step is designing rate schedules that will produce the required revenue given the historical billing determinants, that is, volume of usage, number of customers, number of customer classes, number of bills, percentage of uncollectibles, and so forth. Alt, *supra,* 19-20.

[20] The effect is that net income increases because a portion of the offsetting expenses are instead deferred and carried on the balance sheet as an asset. Tr. 179 (Ives).

requested a "transmission tracker."[21] The Commission denied the request, pointing out that excess transmission costs are not eligible for deferred accounting because they are not extraordinary:

> Applicants have not proved that the transmission cost increases meet that standard. The projected transmission cost increases are not "extraordinary" within the legal definition because they are not rare or current.
>
> "Rare" does not describe cost increases in the utility business generally. Specifically, Applicants' evidence shows the following as to transmission. Transmission is an ordinary and typical, not an abnormal and significantly different, part of Applicants' activities. Also, Applicants showed that paying more for transmission than in the previous year is a foreseeably recurring event, not an unusual and infrequent event. Thus, "items related to the effects of" transmission cost increases are not rare and, therefore, are not extraordinary.[22]

The Commission appropriately denied the Applicants' request for a Transmission Tracker in their last rate cases because transmission expenses are ordinary, everyday operating costs for an electric utility.[23] They are in no way extraordinary and thus do not qualify for extraordinary accounting treatment. In this case, Staff urges the Commission to again deny Applicants' request.

[21] A "tracker" is a sort of rolling AAO, as its description in the list of issues in Case Nos. ER-2012-0174 and ER-2012-0175 makes clear: "Should the Commission authorize KCP&L and GMO to compare their actual transmission expenses with the levels used for setting permanent rates in these cases, and to accrue and defer the difference into a regulatory asset?" Amounts deferred by a tracker mechanism are recorded in the same accounts as amounts deferred via AAO. Tr. 125-127 (Bresette).

[22] Case Nos. ER-2012-0174 and ER-2012-0175, *Report and Order* issued January 9, 2013, p. 31.

[23] Tr. 3:135: "Q. (Ch. Kenney) So there's nothing peculiar about transmission costs generally, it's just the nature and extent of the most recent projects that SPP has approved. A. (Carlson) That's correct."

ARGUMENT

Issue 1: What standards and/or factors should be considered in granting or denying an AAO in this proceeding?

Staff's position is that an AAO should be granted only to defer costs that are (1) extraordinary, unusual and unique, and not recurring; and (2) material.[24]

One purpose of accounting is to reliably report the results of business operations over a given period of time. The Commission has previously stated, "[c]osts incurred by the utility during a period are offset against revenues from that same period in determining a company's profitability."[25] Consequently, the USOA requires that transactions generally be recorded during the period in which they occurred.[26] To that end, USOA General Instruction No. 4 provides, "Each utility shall keep its books on a monthly basis so that for each month all transactions applicable thereto, as nearly as can be ascertained, shall be entered in the books of the utility."[27] USOA General Instruction No. 7 provides, "[i]t is the intent that net income shall reflect all items of profit and loss during the period . . . ."[28] This fundamental accounting principle is often referred to as the "Matching Principle" in that revenues and expenses from the same period are matched to provide an accurate picture of the results of operations. A deviation from this rule, therefore, must be justified by significant considerations.

---

[24] *Oligschlaeger Rebuttal,* p. 6.

[25] ***In the Matter of Missouri Public Service Co.,*** 1 Mo.P.S.C.3d 200, 203 (Dec. 20, 1991) ("Sibley").

[26] Tr. 118.

[27] 18 C.F.R. Part 101, General Instruction No. 4, *Accounting Period.*

[28] *Id.,* General Instruction No. 7, *Extraordinary Items.*

Section 393.140(8), RSMo., does not include an explicit standard. However, it ***does*** expressly require a hearing, that is, the presentation of evidence, the making of a record, and a fair opportunity for stakeholders to be heard.[29] This accords with Rule 4 CSR 240-40.030(5), which permits a variance "for good cause shown," for it is at a hearing that the applicant must make the required showing of good cause. Both of these provisions thus relate to the "reasonableness" standard by which the Commission's contested case decisions are measured:

> "Pursuant to section 386.510, the appellate standard of review of a [PSC] order is two-pronged: 'first, the reviewing court must determine whether the [PSC]'s order is lawful; and **second, the court must determine whether the order is reasonable.'"** * * * The lawfulness of an order is determined "by whether statutory authority for its issuance exists, and all legal issues are reviewed de novo." **"The decision of the [PSC] is reasonable where the order is supported by substantial, competent evidence on the whole record; the decision is not arbitrary or capricious or where the [PSC] has not abused its discretion."**[30]

The Missouri Court of Appeals recently explained that, in the context of administrative action, the test for "arbitrary and capricious" is whether or not the action in question "bears 'a rational relationship to a legitimate state interest.' If so, it is neither arbitrary, capricious, nor unreasonable."[31] Likewise, in an earlier case, the court stated:

> Generally "capriciousness" concerns whether the trial court's

---

[29] By "fair," Staff means a hearing convened on satisfactory notice to interested parties. *See* ***Damon v. City of Kansas City,*** 2013 WL 6170565, 8 (Mo. App., W.D. 2013), *citing* ***Mullane v. Central Hanover Bank & Trust Co.,*** 339 U.S. 306, 314, 70 S.Ct. 652, 94 L.Ed. 865 (1950).

[30] ***Office of Public Counsel v. Missouri Public Service Com'n,*** 409 S.W.3d 371, 375 (Mo. banc 2013) (emphasis added; internal citations removed).

[31] ***Psychiatric Healthcare Corp. of Missouri v. Department of Social Services,*** 100 S.W.3d 891, 900 (Mo. App., W.D. 2003), citing ***Massage Therapy Training Inst., LLC v. Mo. State Bd. of Therapeutic Massage,*** 65 S.W.3d 601, 608 (Mo. App., W.D. 2002) (internal citations omitted).

> decision was whimsical, impulsive or unpredictable. In a related way the idea of "arbitrariness" focuses on whether a rational basis for the trial court's decision exists.[32]

The remaining standard, "abuse of discretion," is simply a synonym for "arbitrary and capricious":

> On the face of it one might reasonably assume that the legislature, in employing varied nomenclature, meant something of significance, that "abuse of discretion" is indeed distinct from "arbitrary," and for that matter both are separate from "capricious," and so on. The implication then seems that an administrative act might be "arbitrary," but not rise to the level of "abuse of discretion," or vice versa. Distinctions of this subtlety are difficult to justify and impossible to find in the case law. Rather the various formulations are often used synonymously, interchangeably, and often collectively as expressions of administrative action that goes too far. Understanding just why the thresholds have been crossed is less a function of abstract formulation and more one of appreciation of the facts of the particular case.[33]

One measure of unacceptable administrative action is treating "similarly situated parties differently for no apparent reason."[34] To avoid that sort of capriciousness with respect to AAOs, this Commission has consistently applied a standard based upon General Instruction No. 7 of the USOA, which provides:

> 7. *Extraordinary Items.*
>
> It is the intent that net income shall reflect all items of profit and loss during the period with the exception of prior period adjustments as described in paragraph 7.1 and long-term debt as described in paragraph 17 below. Those items related to the effects of events and transactions which have occurred during the current period and which are of unusual nature and infrequent occurrence shall be considered extraordinary items.

---

[32] ***State ex rel. Div. of Transp. v. Sure-Way Transp., Inc.,*** 948 S.W.2d 651, 655 n. 4 (Mo. App., W.D. 1997) (internal citations omitted).

[33] Alfred S. Neely, 20A ***Missouri Practice: Administrative Practice and Procedure,*** § 12.49 (West: St. Paul, MN, 2001) (footnotes omitted).

[34] *Id.,* § 12.48.

> Accordingly, they will be events and transactions of significant effect which are abnormal and significantly different from the ordinary and typical activities of the company, and which would not reasonably be expected to recur in the forseeable [*sic*] future. (In determining significance, items should be considered individually and not in the aggregate. However, the effects of a series of related transactions arising from a single specific and identifiable event or plan of action should be considered in the aggregate. To be considered as extraordinary under the above guidelines, an item should be more than approximately 5 percent of income, computed before extraordinary items. Commission approval must be obtained to treat an item of less than 5 percent, as extraordinary. (See accounts 434 and 435.)[35]

The Commission has incorporated the USOA, including its General Instruction No. 7, into its regulations.[36] "The rules of a state administrative agency duly promulgated pursuant to properly delegated authority have the force and effect of law and are binding upon the agency adopting them."[37] Thus, the standard stated by General Instruction No. 7 is mandatory and must be applied.

The Commission applied General Instruction No. 7 in a case concerning a large construction project at the Sibley Generating Station.[38] GMO, then called UtiliCorp United, sought an AAO in order to defer the costs associated with the Sibley project to its next rate case. Mindful of the deviation from the normal ratemaking paradigm implicit in an AAO, the Commission stated:

> Under historical test year ratemaking, costs are rarely considered from earlier than the test year to determine what is a reasonable

[35] 18 C.F.R. Part 101.

[36] Rule 4 CSR 240-40.030(1); *see* ***Report and Order,*** Case Nos. Case Nos. ER-2012-0174 and ER-2012-0175, issued January 9, 2013, at p. 29.

[37] ***State ex rel. Martin-Erb v. Missouri Com'n on Human Rights,*** 77 S.W.3d 600, 607 (Mo. banc 2002).

[38] ***In the Matter of Missouri Public Service Co.,*** 1 Mo.P.S.C.3d 200, 203 (Dec. 20, 1991) **(*"Sibley"*)**.

> revenue requirement for the future. Deferral of costs from one period to a subsequent rate case causes this consideration and should be allowed only on a limited basis. This limited basis is when events occur during a period which are extraordinary, unusual and unique, and not recurring. These types of events generate costs which require special consideration.[39]

The Commission emphasized in ***Sibley*** that the extraordinary event is the "primary focus" in any request for an AAO: "The decision to defer costs associated with an event turns on whether the event is in fact extraordinary and nonrecurring."[40] Virtually quoting General Instruction No. 7, the Commission stated that "[e]xtraordinary means unusual and nonrecurring."[41] For this reason, the Commission has refused to grant AAOs in cases in which it determined that the costs in question were recurring costs.[42] Mr. Oligschlaeger explained:

> The Commission has in the past required that costs be extraordinary in nature to be eligible for deferral, with the materiality of amount to be deferred as a secondary consideration for deferral. The words "extraordinary" and "material" do not mean the same thing; the concept of "extraordinary" relates to the circumstances under which a particular cost was incurred, and the concept of "material" relates to the overall magnitude of the cost. A cost can be extraordinary but not material, or material but not extraordinary.[43]

The ***Sibley*** Commission noted that "whether the event has a material or substantial effect on a utility's earnings" is also relevant to the decision to grant an AAO[44]

---

[39] *Id.,* at 205 (original paragraph formatting altered).

[40] *Id.,* at 205, 206.

[41] *Id.,* at 207.

[42] Tr. 288 (Oligschlaeger).

[43] *Oligschlaeger Rebuttal,* pp. 13-14.

[44] ***Sibley*** at 206.

On the other hand, the Commission rejected as irrelevant such factors as mitigation of regulatory lag and maintaining the financial integrity of the utility.[45]

The standard adopted by the Commission in its ***Sibley*** decision was affirmed by the Missouri Court of Appeals:

> The Commission's decision to grant authority to defer the costs associated with the Sibley reconstruction and coal conversion projects by recording the costs in Account No. 186 was the result of the Commission's determination that the construction projects were unusual and nonrecurring, and therefore, extraordinary. The Commission determined the projects to be unusual because of their size and substantial cost. The Commission expressed that deferral of costs just to support the current financial status distorts the balancing process utilized by the Commission to establish just and reasonable rates. Because rates are set to recover continuing operating expenses plus a reasonable return on investment, only an extraordinary event should be permitted to adjust the balance to permit costs to be deferred for consideration in a later period.[46]

The Applicants argue that General Instruction No. 7 has no bearing on deferral

---

[45] *Id.,* at 206-207.

[46] ***State ex rel. Office of the Public Counsel v. Public Service Commission of Missouri,*** 858 S.W.2d 806, 811 (Mo. App., W.D. 1993). *See also* ***State ex rel. Aquila, Inc. v. Public Service Commission,*** 326 S.W.3d 20, 27 (Mo. App., W.D. 2010) ("When a utility incurs extraordinary expenses (such as the construction of major capital improvements) outside of a "test year," those extraordinary expenses will not be reflected in rates (because the rates were established to allow the utility to recoup its ordinary expenses, as reflected in the "test year"). An accounting authority order or "AAO" permits a utility to capture those extraordinary expenses for (potential) recovery in the forward-looking rates to be established at a future rate case (even though the extraordinary expenses may occur outside the "test year" utilized in that future rate case)"); ***State ex rel. Office of the Public Counsel v. Missouri Public Service Commission,*** 301 S.W.3d 556, 567-70 (Mo. App., W.D. 2009) (AAO for costs of Cold Weather Rule compliance); ***State ex rel. Missouri Gas Energy v. Public Service Commission,*** 210 S.W.3d 330, 335-36 (Mo. App., W.D. 2006) ("The costs of the ECWR [Emergency Cold Weather Rule] are merely a deferment of extraordinary costs."); ***Missouri Gas Energy v. Public Service Commission,*** 978 S.W.2d 434 (Mo. App., W.D. 1998) ("The Commission has the regulatory authority to grant a form of relief to the utility in the form of an accounting technique, an Accounting Authority Order, (hereinafter called an "AAO") which allows the utility to defer and capitalize certain expenses until the time it files its next rate case. The AAO technique protects the utility from earnings shortfalls and softens the blow which results from extraordinary construction programs. However, AAOs are not a guarantee of an ultimate recovery of a certain amount by the utility.").

accounting.[47] Applicants' witness Ives testified, "I don't believe there's anything that you can read in the USOA that says that items have to be extraordinary or have to be greater than five percent to be deferred."[48] Staff expert Mark Oligschlaeger, by contrast, testified that "I believe this Commission has established over the long term a policy by which the criteria of extraordinary which is laid out and defined in generally [*sic*] instruction number 7 should generally guide whether deferrals should be allowed into account 182.3."[49]

In conclusion, Staff's position is that the Commission must apply the ***Sibley*** Test in determining the Applicants' request for an AAO. The ***Sibley*** Test is founded on the standard stated by General Instruction No. 7; that standard is mandatory because it has been incorporated into a promulgated rule. It has been approved by the Court of Appeals. Additionally, it meets the requirement that Commission actions be reasonable, that is, based upon the substantial evidence of record, not arbitrary or capricious, not an abuse of discretion, and bearing a rational relationship to a legitimate state interest.

Issue 2: Should KC&PL and GMO be authorized an AAO to defer and record in Account 182 of the Federal Energy Regulatory Commission ("FERC") Uniform System of Accounts ("USOA") certain incremental transmission costs charged to them by the Southwest Power Pool ("SPP") and other providers of transmission service above the level included in current base rates or defer and record in USOA Account 254 said transmission costs below the amount included in current

[47] Tr. 224 (Ives).

[48] Tr. 224 (Ives).

[49] Tr. 255 (Oligschlaeger). The transcript reads "128.3" but the correct account reference is "182.3."

base rates, with the calculation of the deferrals beginning with the effective date of rates in the Companies' last general rate case proceedings, which was January 26, 2013, as proposed by KCP&L and GMO?

No, the Applicants' request for an AAO for transmission costs in excess of the transmission costs since their last rate cases should be denied for the same reason that this Commission previously denied the Applicants' request for a tracker for these same costs.[50] That reason is that the costs in question are not extraordinary, unusual or non-recurring, but are instead the everyday, common costs of doing business for electric utilities such as Applicants.[51] As the Commission stated in the Applicants' rate cases:

> Transmission is an ordinary and typical, not an abnormal and significantly different, part of Applicants' activities. Also, Applicants showed that paying more for transmission than in the previous year is a foreseeably recurring event, not an unusual and infrequent event. Thus, "items related to the effects of" transmission cost increases are not rare and, therefore, are not extraordinary.[52]

General Instruction No. 7, which controls here, defines "extraordinary" as follows:

> Those items related to the effects of events and transactions which have occurred during the current period and which are of unusual nature and infrequent occurrence shall be considered extraordinary items. Accordingly, they will be events and transactions of significant effect which are abnormal and significantly different from the ordinary and typical activities of the company, and which would not reasonably be expected to recur in the forseeable [*sic*] future.[53]

The ***Sibley*** Test, based on General Instruction No. 7, allows deferral "only on a

[50] *See* page 4, above.

[51] *Oligschlaeger Rebuttal,* pp. 3, 10.

[52] Case Nos. ER-2012-0174 and ER-2012-0175, *Report and Order* issued January 9, 2013, p. 31.

[53] 18 C.F.R. Part 101.

limited basis" . . . "when events occur during a period which are extraordinary, unusual and unique, and not recurring."[54] Applying General Instruction No. 7 and the ***Sibley*** Test here, it is immediately apparent that excess transmission costs simply do not qualify for deferral:

- They are not of unusual nature, but are ordinary and common.[55]
- They are of frequent occurrence, not infrequent.[56]
- They are normal, not abnormal.[57]
- They are not significantly different from the ordinary and typical activities of the company; in fact, they *are* the ordinary and typical activities of the company.[58]
- They are recurring costs, not non-recurring.[59]

Pursuant to the standards stated in General Instruction No. 7 and the ***Sibley*** Test, transmission fees in excess of those in rates are not eligible for deferral via an AAO. It follows that, should the Commission nonetheless grant Applicants' request, the Commission's action would be vulnerable on appeal to a finding that it was unreasonable, contrary to the weight of the credible evidence, arbitrary and capricious, an abuse of discretion, and not bearing a rational relationship to a legitimate state

[54] *Id.,* at 205 (original paragraph formatting altered).

[55] *Oligschlaeger Rebuttal,* pp. 12-13.

[56] *Id.*

[57] *Id.*

[58] *Id.*

[59] *Id.*

interest.

Does that mean that Staff believes that these transmission costs in excess of those in rates should not be recovered? Not at all. They simply should not be recovered through the vehicle of an AAO or a tracker. The appropriate vehicle for the recovery of these costs is through base rates, as reset in a general rate case.[60] When everyday operating costs like these rise by an unacceptable degree, the appropriate response is to file a rate case.[61] Mr. Ives testified that Applicants have a revenue deficiency today, which would support a general rate case.[62] However, Mr. Ives also testified that, after performing an "all relevant factors" analysis, the Applicants elected to seek an AAO rather than file a rate case.[63] The necessary implication is that, when all relevant factors are considered, the Applicants are not actually under-earning, despite the fact that they are not recovering these excess transmission costs.[64]

The Applicants contend that deferrals have been allowed for events that were not

[60] Tr. 162 (Ives): "Based on our projections and the projections from SPP and the fact that we see, you know, according to Mr. Carlson's testimony a 16 percent annual rise on average between now and 2022 on transmission expenses we'll be asking for a solution. We can't sustain that as some parties have suggested by just filing traditional rate cases. Best case scenario even filing a traditional rate case there's going to be 11 months, on the day you got new effective rates there'd be 11 months until the next one, that's 11 months of lag with 16 percent analyzed growth rate, that's a problem for us and it's material to us so whether it's a continuation of a deferral, inclusion in a fuel adjustment clause like Ameren has we'll have to consider that as we're putting the case together but we'll need a solution."

[61] Tr. 268 (Oligschlaeger).

[62] Tr. 166 (Ives); *Ives Surrebuttal*, p. 11.

[63] Tr. 176 (Ives).

[64] Tr. 176, 227 (Ives). The Applicants filed this AAO action because they interpreted certain language in the *Report and Order* in Case Nos. ER-2012-0174 and ER-2012-0175 as an invitation to do so. ". . . there was also a sentence in the order that talked about the five percent greater than or less than and it said if the amounts were less then the Company certainly could come in and ask for an AAO. We know they're greater than but the Commission acknowledged an ability to come ask for an AAO . . . ."

extraordinary;[65] that AAOs have been granted for costs that are normal business expenses.[66] Mr. Ives said of these costs, "I think they're normal business expenses that the Commission has made a decision to handle accounting differently for."[67] AAOs have been granted for pension and other post-employment benefits ("OPEBs")[68] accounting, for service line replacement programs, for computer upgrades for Y2K, for renewable energy standards, changes in the property tax in Kansas, major construction projects, security costs, and infrastructure replacement programs.[69] However, contrary to the testimony of Mr. Ives, Mr. Oligschlaeger testified, "I believe in one way or the other the Commission found that they were extraordinary in nature but I would agree that they were not all the classical acts of God type situation."[70]

There is another reason why the requested AAO should be denied, and that reason is that it would be grossly unfair to the ratepayers given that there is evidence that the Applicants are currently overearning despite the effect of the excess transmission costs.[71] Rates must be just and reasonable and it would be neither just nor reasonable to grant extraordinary relief to the Applicants for the purpose of mitigating regulatory lag at a time when they are earning more profit than the

[65] Tr. 190 (Ives): "Q. What was the intent of the schedule? A. (Ives) To demonstrate that there were things that deferrals were allowed for other than acts of God extraordinary in nature and I think the subject line does that." See also Tr. 229 (Ives).

[66] Tr. 232 (Ives).

[67] Tr. 232 (Ives).

[68] I.e., retiree medical benefits. Tr. 260-261 (Oligschlaeger).

[69] Tr. 259-261 (Oligschlaeger).

[70] Tr. 262 (Oligschlaeger).

[71] Tr. 302 (Meyer).

Commission has authorized.[72] The current overearning situation is clear from analysis of GMO's quarterly surveillance reports and Data Request ("DR") responses obtained from KCP&L.[73] Expert witness Greg Meyer testified that this data shows that the Applicants are ***already*** recovering the excess transmission costs without any deferral mechanism.[74] Mr. Meyer commented on the testimony of Applicants' witness Darrin Ives as follows:

> Q. (Thompson): Did you hear Mr. Ives explain that the reason the Company did not file a general rate case was because of the results of an analysis of all relevant factors?
>
> A. (Meyer): I did hear that.
>
> Q. (Thompson): In your professional opinion do you take that to support the results of your analysis?
>
> A. (Meyer): What I take from that is he's done an analysis of their current operations and I think his surveillance data proves that and that he would be putting his excess earnings at risk for trying to attempt to increase his rates.

In conclusion, the requested deferral should be rejected because the circumstances do not support the grant of a deferral mechanism. The costs involved are ordinary, everyday costs of doing business; they are not unique, non-recurring or

[72] *Meyer Direct,* pp. 12-17 (HC).

[73] Tr. 299-304, 306 (Meyer).

[74] Tr. 306-307 (Meyer).

extraordinary. Additionally, the Applicants appear to be overearning and the grant of an extraordinary mechanism to protect earnings in the present circumstances would be an abuse of discretion.

Issue 2.a: Are there mitigating factors affecting the current operations and earnings levels of KCP&L and GMO that are relevant to the KCP&L and GMO request for AAOs?

Staff takes no position on Issue 2.a.

Issue 3: Should KCP&L and GMO be authorized to include carrying costs based on the Companies' latest approved weighted average cost of capital on the balances in this regulatory asset or regulatory liability of transmission costs as proposed by KCPL and GMO?

No. In a case involving the deferral of expenses involved in the Sibley rebuild, the Commission noted that rate base treatment "is the usual practice when ***capital costs*** are amortized."[75] The concept behind allowing rate base treatment of deferrals and allowing carrying costs related to the deferrals is similar. While rate base treatment has been granted to deferral amortizations in some circumstances to recognize the delay in recovery of capital-related costs once rate treatment of the item has begun, allowing accrual of carrying costs recognizes the delay in recovery of the deferred costs before any rate recovery has been authorized. The transmission costs that the Applicants seek to defer in this application are expense items, not capital

[75] ***In the Matter of Missouri Public Service,*** 30 Mo.P.S.C. (N.S.) 320, 341 (Oct. 5, 1990), quoted with approval by ***Aquila,*** *supra,* 326 S.W.3d at 30.

expenditures.[76]

Applicants assert that carrying costs are appropriate to reflect the time value of money.[77] However, Staff witness Oligschlaeger noted that it is true of every cost recovered by a utility that a delay occurs between the time the cost is incurred and when it is recovered.[78] While the mitigation of regulatory lag is an appropriate purpose of an AAO, its elimination is not.[79] In this way, responsibility for extraordinary items is shared by shareholders and ratepayers.[80] This policy has been implemented for many prior AAO deferrals through an immediate amortization of deferred amounts without rate-base treatment and without inclusion of carrying costs.[81]

There have been deferrals where the consensus opinion is that carrying costs are appropriate.[82] The Missouri Court of Appeals has approved granting rate base treatment to deferred expenses where the Commission's action was supported by testimony as to the sound public policy aspect of providing an incentive to the utility to undertake an expensive construction project (i.e., the Sibley rebuild).[83] Carrying costs have been allowed for deferrals of costs involved in complying with Commission

[76] Tr. 122 (Ives).

[77] Tr. 233 (Ives).

[78] Tr. 263 (Oligschlaeger).

[79] Tr. 264 (Oligschlaeger).

[80] Tr. 264-265 (Oligschlaeger).

[81] Tr. 266 (Oligschlaeger).

[82] Tr. 288 (Oligschlaeger).

[83] ***Aquila,*** *supra,* 326 S.W.3d at 29 and n. 12 ("In the cited findings the Commission found that Aquila had conferred a benefit on ratepayers by incurring the costs at issue, and chose to adopt the (identified) rationale offered by two witnesses as to why rate-base treatment of these unamortized costs furthered the public interest.").

mandates.[84] But, generally, deferrals do not include carrying costs.[85]

In conclusion, not only is there no good reason to include carrying costs if these expenses are deferred, there is no good reason to defer them at all.

Issue 4: Should KCP&L and GMO be authorized to defer such amounts in a separate regulatory asset or regulatory liability with the disposition to be determined in each Company's next general rate case?

No. It is often said that deferral, in and of itself, does not mean that any part of the amount deferred will ultimately be recovered.[86] However, this is too simplistic. Accounting standards require that, for a deferral to be recognized, its recovery must be probable (though not guaranteed).[87] For this reason, Applicants must have an order from the Commission specifically authorizing any deferral.[88] Mr. Ives further testified that he would not expect the Commission to deny the recovery of prudently incurred transmission expenses in a rate case and that the subsequent recovery of deferred transmission costs would thus indeed be likely.[89] Staff expert Mark Oligschlaeger testified:

> There's two different things we're talking [about] here. One is the accounting directives this Commission has in its scope governing the accounting of all the subject utilities. Number two is the jurisdiction of the

[84] Tr. 288 (Oligschlaeger).

[85] Tr. 288-289 (Oligschlaeger).

[86] *Oligschlaeger Rebuttal,* pp. 6-7.

[87] Tr. 174 (Ives): ACS 980 requires that recovery be probable in order to recognize the deferral at all.

[88] Tr. 228 (Ives), and see at 225: ". . . we just can't, without a specific Commission authority to defer we can't defer, our accountants won't agree with that and our external accountants won't agree with that."

[89] Tr. 232 (Ives). Staff witness Oligschlaeger agreed that "it's always been our policy to include prudent and necessary transmission expenses in the Company's cost of service." Tr. 268.

> financial accounting community over the Company's published financial reports. Obviously the external auditors don't govern what this Commission does in terms of accounting and this Commission can't govern what the external auditors decree in terms of the published financial reports. My point here is without explicit authorization from the Commission for a deferral it is unlikely a company's external auditors, their public accounting firm would allow them to book the deferral for purposes of their published financial reports. If they were not allowed to do that then at least some, much of the benefit that the company intends as part of the deferral process cannot be accomplished.[90]

Mr. Oligschlaeger further testified that, should the Commission decide to allow the Applicants to defer the excess transmission costs, then it should issue an order specifically permitting that treatment.[91] Mr. Oligschlaeger testified:

> Staff does not disagree with the overall conclusion made by Mr. Ives and Mr. Bresette that utilities may not be able to book deferrals of costs in certain circumstances for financial reporting purposes without an order from the Commission explicitly authorizing such a deferral. Therefore, in the event that it is the Commission's intent that the Companies be allowed to book a deferral of transmission costs as a result of this proceeding, Staff believes that the Commission should issue an order authorizing an AAO or tracker for that purpose.[92]

In summary, the application for a deferral mechanism should be denied. If it is nonetheless granted, it should be in the form of a written order specifying the costs that may be deferred and the governing conditions.

Issue 5: Should KCP&L and GMO be authorized trackers for their transmission costs in this proceeding rather than AAOs?

No. Staff expert witness Mark Oligschlaeger testified, "even if viewed as

[90] Tr. 256-257 (Oligschlaeger).

[91] Tr. 258 (Oligschlaeger).

[92] *Oligschlaeger Rebuttal,* p. 27.

equivalent to a request for a transmission expense tracker, the Company's Application still fails to meet appropriate criteria for such treatment . . . ."[93] Of course, the Applicants do not care what mechanism is used as long as they get their money.[94] Mr. Ives testified, "I don't see a distinction between trackers or AAOs or deferrals, I think they're all governed by the same rules for deferral under [USOA Account] 182."[95]

A tracker is a deferral mechanism that is similar in some respects to an AAO. Mr. Oligschlaeger explained:

> Trackers are similar in concept to AAOs, in that both mechanisms are intended to result in deferral of certain financial impacts on utility books, with the deferral amount eligible for recovery in subsequent rate proceedings. However, trackers are typically different from AAOs in that the associated costs are not extraordinary in nature, the amount of the deferral is tied to a comparison of the cost allowance for the item included in the utility's current rates, and trackers are usually established in general rate proceedings. Based upon the structure of the deferral sought by the Companies in this Application, Staff views this deferral request to be closer to prior requests for use of tracker mechanisms than what has been traditionally sought within AAO requests.[96]

Trackers have been granted for costs showing significant volatility over time and which are difficult to forecast accurately.[97] Examples include pensions and OPEB costs and some storm damage costs.[98] Trackers have also been granted for new costs where historical data is lacking and accurate estimation is difficult, such as Operating

[93] *Oligschlaeger Rebuttal,* p. 3.

[94] Tr. 161, 186 (Ives).

[95] Tr. 192 (Ives).

[96] *Oligschlaeger Rebuttal,* p. 24.

[97] *Oligschlaeger Rebuttal,* p. 25.

[98] *Id.*

and Maintenance ("O&M") costs for new generating stations.[99] Finally, trackers have been allowed for costs imposed upon utilities by Commission rules, such as vegetation management and infrastructure inspection costs.[100]

The excess transmission costs that are the subject of this proceeding do not qualify for a tracker:

- They are not volatile.[101]
- They are not difficult to estimate or forecast accurately.[102]
- Historical data is not lacking.[103]
- They are not imposed by Commission rule.[104]

Mr. Oligschlaeger commented:

> Fundamentally, Staff believes the primary reason KCPL and GMO seek this treatment of a portion of its transmission revenue requirement is to lessen its regulatory lag; or, stated a different way, to protect its earnings from the impact of a projected increasing level of ongoing and ordinary transmission costs. Staff asserts that this is not an appropriate or sufficient rationale for either issuance of an AAO or implementation of a tracker mechanism regarding these costs.[105]

This Commission has already rejected the Applicants request for a transmission tracker once, in the context of a general rate case in which all relevant factors were

[99] *Id.*

[100] *Id.*

[101] *Id.*

[102] *Id.*

[103] *Id.*

[104] *Id.*

[105] *Oligschlaeger Rebuttal,* pp. 25-26.

considered. It certainly should not change its mind and grant a tracker in this case in which only one, isolated cost has been considered.

Issue 6: If the Commission grants KCP&L and/or GMO AAOs or trackers, should it also adopt all or any of the following conditions proposed by Staff and addressed by one or more of the other Parties?

Yes. These conditions are necessary to protect the ratepayers in the event that a deferral mechanism is granted against Staff's advice.

Staff's Proposed Conditions:

1. That the deferral reflects both transmission revenues and expenses, and thereby be based upon the level of net transmission costs experienced by KCP&L and GMO.

The purpose of this condition is to require that both SPP-allocated-transmission expenses and SPP-allocated-transmission revenues be incorporated into any regulatory asset or liability granted to the Applicants.[106] The SPP transmission charges paid by the Applicants are intended to reimburse other SPP members for the Applicants' use of the transmission facilities belonging to those other SPP members.[107] In turn, the Applicants receive reimbursement through SPP for the use of their transmission facilities by all other SPP members.[108] It is inappropriate to exclude the transmission revenues while

[106] *Oligschlaeger Rebuttal,* p. 29.

[107] *Id.*

[108] *Id.*

deferring the transmission expenses.[109] Mr. Oligschlaeger testified:

> KCPL and GMO have structured their request in a skewed and inappropriate manner. The Companies' deferral request seeks earnings protection against increases in portions of their transmission revenue requirement, but would totally ignore concurrent and potentially offsetting changes in the levels of transmission revenues received by them, as well as expected cost savings and benefits associated with the projected increases in transmission expenses for which they seek deferral.[110]

For example, Ameren Missouri recovers excess transmission charges through its FAC, which also includes offsetting transmission revenues.[111]

The Applicants, however, strongly oppose the inclusion of transmission revenues in any deferral mechanism.[112] They contend that transmission revenues should be netted against the "ownership costs" of the transmission assets and not against the excess transmission charges.[113] The Applicants assert it would be a mismatch to offset revenues associated with their ownership of transmission assets against expenses associated with their use of transmission service obtained from other entities.[114]

Staff's position is that the Applicants are proposing a mismatch of revenues and expenses.[115] Staff's proposal would include all SPP expenses and

---

[109] *Id.*

[110] *Oligschlaeger Rebuttal,* p. 3; and see *Oligschlaeger Rebuttal,* p. 30.

[111] Tr. 151-152, 156 (Ives); Tr. 249 (Oligschlaeger).

[112] *Oligschlaeger Rebuttal,* pp. 17-18.

[113] Tr. 209-210, 220 (Ives).

[114] *Oligschlaeger Rebuttal,* p. 18.

[115] Tr. 280 (Oligschlaeger).

all SPP revenues in the deferral mechanism because this is the proper match of revenues and expenses – both are the result of using transmission systems not owned by the user.[116] As Mr. Oligschlaeger testified, "From a revenue requirement perspective, the financial impacts of SPP membership on KCPL's and GMO's financial situation are opposite sides of the same coin."[117] Mr. Oligschlaeger warned that adopting the Applicants' view could result in double recovery of the excess transmission costs – "a financial windfall for them."[118]

The "ownership costs" referred to by the Applicants are properly excluded from the deferral mechanism, as are the base rate revenues that pay them.[119] That, too, is a proper match of revenues and expenses -- the Applicants use their own transmission system to serve their native load and the ratepayers reimburse the associated costs through rates.[120]

2. That KCP&L and GMO provide to all parties in this case on a monthly basis copies of billings from SPP for all SPP rate schedules that contain charges and revenues that will be included in the deferral and report, per its general ledger, all expenses and revenues included in the deferral by month by FERC USOA account and KCP&L/GMO subaccount or minor account. KCP&L and GMO shall also provide, on no less than a

[116] Tr. 280 (Oligschlaeger); *Oligschlaeger Rebuttal,* pp. 9-10.

[117] *Oligschlaeger Rebuttal,* p. 18.

[118] *Oligschlaeger Rebuttal,* p. 19.

[119] Tr. 280-281 (Oligschlaeger); *Oligschlaeger Rebuttal,* pp. 8-9.

[120] Tr. 282 (Oligschlaeger).

quarterly basis, the internally generated reports it relies upon for management of its ongoing levels of transmission expenses and revenues. KCP&L and GMO shall also notify the Parties of any changes to its existing reporting or additional internal reporting instituted to manage its transmission revenues and expenses.

The purpose of Staff's second condition is to require the Applicants to provide ongoing reporting of the transmission costs and revenues flowing through the deferral mechanism.[121] This information will enable Staff to monitor the ongoing levels of costs being deferred, to investigate any unusual trends in the deferred amounts, and expedite its review of these costs in subsequent rate proceedings.[122] Staff wants to "keep the Applicants honest" by requiring them to provide monthly and quarterly information returns showing revenues and expenses pertinent to the deferral mechanism.[123]

3. That KCP&L and GMO maintain an ongoing analysis and quantification of all benefits and savings associated with participation in SPP not otherwise passed on to retail customers between general rate proceedings.

Staff proposes that the Applicants maintain an ongoing analysis and quantification of all benefits and savings associated with participation in SPP not

[121] *Oligschlaeger Rebuttal,* p. 30.

[122] *Id.*

[123] Tr. 282 (Oligschlaeger).

otherwise passed on to ratepayers in other general rate cases.[124] The purpose of this condition is to enable the Commission to have the ability to consider offsetting these benefits against the deferred transmission expenses in future rate proceedings where recovery of the deferred amounts is considered.[125]

What are these benefits? As part of the process of obtaining authorization from the Commission to continue participation in the SPP, the Applicants prepare and submit cost benefit studies showing that the benefits of participation outweigh the costs.[126] For example, an interim report submitted in 2011 stated that:

> For both companies together the projected annual net benefits of participating in SPP vary from approximately negative 4 million in a low case to positive 50 million in the high case yielding a mid-point net benefit of about 23 million per year. These numeric results do not capture the full range of benefits that are and can be achieved through SPP membership because many of the benefits are not readily quantifiable.[127]

The next such studies are scheduled to be produced in 2017.[128]

Applicants oppose this condition. They complain that these studies are costly and time-consuming to produce;[129] they are complex;[130] the benefits are

[124] Tr. 283 (Oligschlaeger).

[125] *Oligschlaeger Rebuttal,* p. 31.

[126] Tr. 147 (Ives), Tr. 283 (Oligschlaeger); *Oligschlaeger Rebuttal,* p. 20.

[127] Tr. 149 (Ives).

[128] Tr. 147, 150-151 (Ives); Tr. 284 (Oligschlaeger).

[129] Tr. 151, 237-238 (Ives).

[130] Tr. 283 (Oligschlaeger).

difficult to quantify.[131] Some are avoided costs while others, such as supporting the greater availability of renewable energy, are public policy objectives.[132] Nonetheless, the Applicants proclaimed these purported benefits to persuade the Commission to allow their continued participation in SPP.[133] It is only reasonable that these benefits also be taken into account if extraordinary treatment of increased transmission costs is authorized by the Commission.

4. That KCP&L and GMO maintain documentation of its efforts to minimize the level of costs deferred under any AAOs or trackers authorized for it.

Staff also proposes that, if a deferral mechanism is granted, then the Applicants should be required to maintain documentation of their efforts to minimize the level of deferred costs.[134] Mr. Oligschlaeger testified:

> Inherently, an authorization to book any increase in transmission expenses above the level already included in rates would weaken the Companies' incentive to control such expense increases to a minimum, as KCPL's and GMO's reported earnings would be insulated from increases in their transmission expenses above the level currently reflected in rates through the general rate case process.[135]

Staff's goal is to incentivize the Applicants to make every effort to maximize the benefits that accrue to both customers and shareholders from their

[131] Tr. 238 (Ives).

[132] Tr. 238 (Ives).

[133] Case Nos. EO-2012-0135 and EO-2012-0136.

[134] Tr. 284 (Oligschlaeger).

[135] *Oligschlaeger Rebuttal,* p. 17.

involvement with SPP.[136] Mr. Oligschlaeger testified that cost minimization is one aspect of maximizing those benefits.[137] In the absence of such an incentive, the Applicants could not be expected to act diligently to protect ratepayers from unnecessary and avoidable cost increases.

5. That all ratemaking considerations regarding transmission revenue and expense amounts deferred by the Company pursuant to Commission authorization be reserved to the next KCP&L and GMO rate proceedings, including examination of the prudence of the revenues and expenses.

The Applicants are willing to accept this condition.[138]

6. That an amortization to expense over a 60-month period of the amounts accumulated in any deferral commence on KCP&L's and GMO's books in the first full calendar month following Commission approval of the AAOs or trackers.

This condition is intended to prevent the Applicants from "hoarding" transmission expense recoveries over a long period of time in order to maximize their potential rate recovery of transmission costs.[139] Mr. Oligschlaeger testified:

It is neither appropriate regulatory policy nor appropriate application

[136] Tr. 284 (Oligschlaeger); *Oligschlaeger Rebuttal,* p. 31.

[137] Tr. 284 (Oligschlaeger).

[138] Tr. 286: "Q. (Fischer) And we agree, don't we, that if the Commission grants the AAO in this case that ratemaking consideration should be left for the next rate case? A. (Oligschlaeger) I believe the Company accepts that position."

[139] *Oligschlaeger Rebuttal,* p. 31.

> of accounting theory to allow a utility to defer recognition on its financial statements of incurred costs for a prolonged period of time simply to preserve the utility's ability to attempt to recover the entirety of the cost in question. An AAO or tracker, if granted in this circumstance, should only allow the utility to spread recognition of the deferred costs over a five-year period for financial reporting purposes, not to indefinitely delay any recognition of these costs at all, especially in time periods in which the related benefits to these expenditures are recognized in the Companies' income.[140]

In the past, the grant of an AAO has sometimes included a requirement that the company initiate a rate case within a certain interval or lose any chance of recovery in rates.[141] More recently, the mechanism of immediate amortization has been used for the same purpose.[142] As Mr. Oligschlaeger testified:

> The normal practice has been to allow rate recovery of deferred costs associated with a natural disaster over a multi-year amortization period (usually five years), but not to allow a rate base return on the unamortized portion of deferred costs. The practical effect of this approach is to "share" responsibility for the extraordinary expenses between the utility's shareholders and ratepayers. This demonstrates that the AAO mechanism has not been used in the past to entirely insulate utilities from the financial impact of the triggering events.[143]

The underlying reasoning is that if current earnings are such that the company does not need to seek immediate rate relief, then the deferred costs are considered to have been recovered through current revenues.[144]

Applicants oppose this condition because they contend that it necessarily

---

[140] *Id.*

[141] Tr. 289 (Oligschlaeger).

[142] Tr. 289 (Oligschlaeger).

[143] *Oligschlaeger Rebuttal,* p. 27.

[144] Tr. 289 (Oligschlaeger).

denies full recovery of the costs in question.[145] Staff, on the other hand, favors it as a way of sharing the responsibility for extraordinary items between ratepayers and shareholders.[146] It is Staff's position that while the mitigation of regulatory lag may be an appropriate purpose of an AAO, its elimination in entirety is not.[147] The risk and responsibility for extraordinary items should be shared by shareholders and ratepayers.[148] This policy is normally implemented by amortizing deferred amounts immediately without rate-base treatment and without allowing carrying costs.[149] Furthermore, Applicants' current earnings may be sufficient to absorb the excess transmission costs without rate relief.[150] In that case, for all practical purposes, they should be considered to have recovered those costs.[151]

7. That deferrals addressed by the AAOs or trackers cease when KCP&L or GMO report it is earning at or in excess of its authorized ROE on a twelve-month rolling forward average basis in quarterly earnings "surveillance" reporting on an overall basis. Deferrals addressed by the AAOs or trackers begin again when KCP&L or GMO report it is below its authorized ROE on a twelve-month rolling forward average basis in

[145] Tr. 234 (Ives).

[146] Tr. 266 (Oligschlaeger).

[147] Tr. 264 (Oligschlaeger).

[148] Tr. 264-265 (Oligschlaeger).

[149] Tr. 266 (Oligschlaeger).

[150] Tr. 267 (Oligschlaeger).

[151] Tr. 267 (Oligschlaeger).

quarterly earnings "surveillance" reporting on an overall basis.

Staff proposes that any deferral mechanism for excess transmission costs be automatically suspended any time that quarterly surveillance reports show that the Applicants are earning at their authorized return on equity ("ROE") or overearning.[152] This mechanism is intended as a "bright line" or automatic tripwire to protect ratepayers from being treated unreasonably by the Companies.[153] Given that the only legitimate purpose of a deferral mechanism for transmission costs in excess of those in base rates is to mitigate a situation in which the Applicants have no reasonable opportunity to earn their authorized return on equity, it is only fair that the mechanism not operate when the Applicants are earning at their authorized ROE or overearning.[154]

This braking mechanism would be triggered by the Actual Earned Return on Equity contained in the quarterly surveillance reports that GMO already prepares and submits.[155] KCP&L has indicated that it could do the same.[156] The deferral mechanisms authorized by the Commission in the past have operated, at least in part, as earnings protection mechanisms for both the utilities and their customers.[157] Therefore, there is no reason to defer the impact of under

[152] Tr. 269 (Oligschlaeger); *Oligschlaeger Rebuttal,* p. 3.

[153] Tr. 274 (Oligschlaeger).

[154] Tr. 274 (Oligschlaeger).

[155] Tr. 217 (Ives); Tr. 247, 249 (Oligschlaeger)..

[156] Tr. 170-171 (Ives).

[157] *Oligschlaeger Rebuttal,* p. 32.

collections in rates of one cost-of-service element when Applicants are earning in excess of their authorized ROEs on an overall basis.[158]

The Applicants object that the return on equity in the surveillance reports is not directly comparable to the return on equity authorized in a rate case. Staff agrees. In fact, Staff does not believe that the earned return on equity reported in surveillance reports is directly comparable to the return on equity authorized in a rate case; the latter reflects numerous normalizing adjustments.[159] As Mr. Oligschlaeger testified, "Surveillance reports are not detailed enough to justify changes in rates in and of themselves."[160] However, Staff does use the reported earned return on equity as an analytical starting point.[161]

Both Southwestern Bell Telephone Company and Ameren Missouri had earnings sharing plans in effect for several years in the 1990s based on the calculation of those utility's return on common equity for a 12 month period.[162] GMO has a FAC and thus prepares and submits regular surveillance reports.[163] KCP&L has indicated that it could do the same.[164] These surveillance reports

---

[158] *Id.*

[159] Tr. 271-272 (Oligschlaeger), and see Tr. 311 (Meyer). Note that Meyer testified that weather normalized sale figures would be ***higher*** than depicted in the surveillance reports, making the Actual Earned Return on Equity higher as well. Tr. 312.

[160] Tr. 273 (Oligschlaeger).

[161] Tr. 272 (Oligschlaeger).

[162] Tr. 156-157 (Ives).

[163] Tr. 217 (Ives); Tr. 247, 249 (Oligschlaeger)..

[164] Tr. 170-171 (Ives).

include Actual Earned Return on Equity.[165] This figure, like net income, would increase if some portion of expenses were deferred and carried as an asset.[166] According to Mr. Ives, this figure is directly comparable to the return on equity authorized by the Commission.[167]

CONCLUSION

Applicants seek extraordinary accounting and ratemaking treatment for what are merely the ordinary, day-to-day costs of doing business. If granted, the Commission will disorder and confuse the ratemaking and regulatory accounting paradigms carefully developed over more than a century. The Applicants' request, accordingly, should be denied.

Accounting rules exist so that financial accounting will produce fair and accurate reports of the results of business operations. A deferral mechanism breaks those rules and distorts those reports, making the results obtained look better than they actually were. This sort of accounting treatment should only be undertaken in the rare case in which it is absolutely necessary. Ratemaking rules exist so that just and reasonable rates can be set, rates that are fair to the shareholders and fair to the ratepayers. A deferral mechanism breaks those rules and shifts risks from the shareholders to the ratepayers. This sort of ratemaking treatment should only be undertaken in the rare

[165] Tr. 180-181 (Ives).

[166] Tr. 181 (Ives).

[167] Tr. 182 (Ives).

case in which it is absolutely necessary. This is not such a case.

Every business has its particular risks. For public utilities, one risk is that costs will rise after the conclusion of a rate case, putting a squeeze on profits. Perhaps that is what is happening here. We don't actually know – this case has examined only one cost, in isolation. Other costs may be holding steady or even declining. In fact, one party has presented evidence that, over all, the Applicants' cost of service is falling. One very persuasive piece of corroborating evidence is Mr. Ives' admission that an "all pertinent factors" analysis does not support rate relief right now, despite the increasing transmission costs.[168]

The Commission should deny the Application before it. The circumstances do not justify a deferral. Should the Applicants decide that they absolutely must recover the increasing excess transmission costs, they can file a rate case. That's how cost-of-service regulation works.

Respectfully submitted,

s/ Kevin A. Thompson
KEVIN A. THOMPSON
Missouri Bar Number 36288
Chief Staff Counsel

WHITNEY M. HAMPTON
Missouri Bar Number 64886
Assistant Staff Counsel

Missouri Public Service Commission
P.O. Box 360
Jefferson City, MO 65102

[168] Staff will monitor the Applicants' earnings to determine whether an overearnings complaint should be filed.

573-751-6514 (Voice)
573-526-6969 (Fax)
kevin.thompson@psc.mo.gov

Attorneys for the Staff of the
Missouri Public Service Commission.

Certificate of Service

I hereby certify that a true and correct copy of the foregoing was served, either electronically or by hand delivery or by First Class United States Mail, postage prepaid, on this **25th day of February, 2014,** to the parties of record as set out on the official Service List maintained by the Data Center of the Missouri Public Service Commission for this case.

s/ Kevin A. Thompson