BEFORE THE PUBLIC SERVICE COMMISSION OF THE STATE OF MISSOURI

In the Matter of a Working Case to Consider Proposals to Create a Revenue Decoupling Mechanism for Utilities	)))	**File No. AW-2015-0282**

LEGALITY OF DECOUPLING FOR ELECTRIC UTILITIES

COME NOW Earth Island Institute d/b/a Renew Missouri ("Renew Missouri"), Sierra Club ("Sierra Club"), the Natural Resources Defense Council ("NRDC"), Great Rivers Environmental Law Center and Earthjustice, and offer this legal memorandum on behalf of their respective organizations. This legal memo is offered in response to Staff's July 30, 2015 Motion directing interested stakeholders to respond to questions from the Commission, specifically the question on whether revenue decoupling is legal under Missouri law (¶2.a). The analysis in this memorandum is limited specifically to the legality of decoupling for electric utilities.

Decoupling—a true-up of a utility's revenue requirement to prevent the erosion of revenue from lost sales caused by energy efficiency programs—is authorized under Missouri law for electric utilities by the language of MEEIA and by the decision of the Court of Appeals Western District upholding the Commission's MEEIA rules, *State ex rel. Public Counsel v. PSC,* 397 S.W.3d 441 (Mo.App. W.D. 2013).

The MEEIA statute makes it the policy of the State of Missouri to remove the "throughput disincentive." As a consequence of traditional ratemaking, a utility that reduces its sales (e.g. through demand-side energy efficiency programs) has a financial disincentive to encourage its customers to save energy and runs the risk of failing to recover its full fixed costs between rate cases. MEEIA therefore provides:

> 3. It shall be the policy of the state to value demand-side investments equal to traditional investments in supply and delivery infrastructure and allow recovery of all reasonable and prudent costs of delivering cost-effective demand-side programs. In support of this policy, the commission shall:
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> …
>
> (2) Ensure that utility financial incentives are aligned with helping customers use energy more efficiently and in a manner that sustains or enhances utility customers' incentives to use energy more efficiently…

§ 393.1075.3(2). MEEIA is more explicit in § 393.1075.5:

> 5. To comply with this section **the commission may develop cost recovery mechanisms to further encourage investments in demand-side programs including, in combination and without limitation:** capitalization of investments in and expenditures for demand-side programs, rate design modifications, accelerated depreciation on demand-side investments, and allowing the utility to retain a portion of the net benefits of a demand-side program for its shareholders. In setting rates the commission shall fairly apportion the costs and benefits of demand-side programs to each customer class except as provided for in subsection 6 of this section. Prior to approving a rate design modification associated with demand-side cost recovery, the commission shall conclude a docket studying the effects thereof and promulgate an appropriate rule.

MEEIA further provides, in § 393.1075.11:

> 11. The commission shall provide oversight and may adopt rules and procedures and approve corporation-specific settlements and tariff provisions, independent evaluation of demand-side programs, as necessary, to ensure that electric corporations can achieve the goals of this section.

The *UCCM* CASE

The leading case on rate adjustment mechanisms is *UCCM v. PSC,* 585 S.W.2d 41 (Mo. banc 1979), which struck down a FAC because it was a departure from traditional ratemaking, which requires that rates be fixed in a general rate case. Any departure from this fixed-rate rule requires authorization by the legislature "either expressly, or by clear implication as necessary to carry out the powers specifically granted" by statute. 585 S.W.2d at 49. In a general rate case, the Commission must consider "all relevant factors" in evaluating whether proposed rates are just and reasonable. 585 S.W.2d at 49.

The Court distinguished *Hotel Continental v. Burton,* 334 S.W.2d 75 (Mo. 1960), which allowed KCP&L to pass through to its customers local gross receipts taxes. In *Burton,* the tax could not affect the company's rate of return, nor could the amount of the tax be affected by any action of the company. The tax could therefore legitimately be treated differently from other items of expense. 585 S.W.2d at 52–3.

A revenue requirement true-up is different from both the FAC in *UCCM* and the tax in *Burton.* It does have this crucial similarity to *Burton*: it cannot affect the company's authorized rate of return or revenue requirement; on the contrary, the purpose of a decoupling mechanism is to ensure that the utility will collect no more and no less than the revenue requirement that was authorized in a general rate case after consideration of all relevant factors.

The immediate question, though, is whether MEEIA expressly or by necessary implication authorizes such a mechanism.

Public Counsel v. PSC

In *State ex rel. Public Counsel v. PSC,* 397 S.W.3d 441 (Mo.App. W.D. 2013), the Court turned back OPC's challenge to the Commission's rules on Demand Side Investment Mechanisms (DSIM) and the adjustment of DSIM rates outside a rate case. The court determined that MEEIA, §§ 393.1075.5 and 393.1075.11, gave the Commission "discretion to develop a cost-recovery mechanism that would encourage utilities to invest in demand-side programs despite the financial risk." 397 S.W.3d at 450. The Court reasoned that MEEIA, by implication at least, gave the PSC discretion to allow rate adjustments outside a general rate case. *Id.*

OPC also challenged the lost revenue recovery provision in the rules. The court held that lost revenue "can be construed as a cost of delivering demand-side programs in the context of

MEEIA," 397 S.W.3d at 452, and that "recovery of lost revenue is impliedly authorized under MEEIA," 397 S.W.3d at 453, specifically § 393.1075.3(2).

Decoupling is a different means of addressing this same lost revenue problem. The Commission has broad discretion under MEEIA to deal with this "cost" of DSM and to do so by adjustments to the revenue requirement that has already been determined in a rate case.

Rate design

MEEIA expressly permits "rate design modifications" subject to a requirement for a study docket and a rulemaking. § 393.1075.5. Decoupling is commonly regarded as a rate design. *See, e.g.*, *Ohio Consumers' Council v. PUCO,* 125 Ohio St.3d 57, 926 N.E.2d 261, 2010 Ohio 134, ¶ 3.

The Illinois Supreme Court recently upheld a decoupling rate design in the form of a rider for gas companies. *People ex rel. Madigan v. Illinois Commerce Commission,* 388 Ill. Dec. 895, 2015 IL 116005, 25 N.E.3d 587 (2015). Appellants challenged the rider as a violation of rate-of-return ratemaking principles. 25 N.E.3d at 596, ¶ 27. The court rejected the challenge: "So a rate design that allows a utility company to recover its revenue requirement does not guarantee a profit any more than the revenue requirement itself does," but the utility was entitled to its ROE. 25 N.E.2d at 597, ¶ 30. The rider "also guards customers against the negative effects of inevitably incorrect forecasting. Decoupling stabilizes both utility revenues and customer bills." 25 N.E.2d at 598, ¶ 33.

Conclusion

For the reasons set forth above, the Commission has authorization under MEEIA to implement decoupling for electric utilities through a working docket and a rulemaking under § 393.1075.5.

Respectfully submitted,

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