BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

In the Matter of Union Electric Company d/b/a AmerenUE for Authority to File Tariffs Increasing Rates for Electric Service Provided to Customers in the Company's Missouri Service Area.	)))))	**Case No. ER-2010-0036**

PUBLIC COUNSEL'S BRIEF ON INTERIM RATE REQUEST

Introduction

AmerenUE would have this Commission believe that the Commission has an implied power to grant interim increases at the Commission's discretion. A more accurate reading of the relevant cases reveals that the Commission has an implied power to deal with utility emergencies, and that granting interim rate relief to deal with emergencies is within the Commission's discretionary exercise of this implied power. In other words, the implied power derives from the existence of an emergency (or a situation very close to an emergency). If there is no emergency, there is no power to exercise. The Commission has no inherent powers; it has only those powers expressly granted to it by statute and those powers necessarily implied by the express grant.

AmerenUE argues that what it now considers to be "excessive regulatory lag" (and which it was very happy to deal with for most of the last twenty-five years) creates a disincentive to invest in its system. But AmerenUE does not ever give a single example of a better investment that would offer it a better long-term return than investing in rate-regulated property in Missouri. The "disincentive to invest" argument is a red herring. Of course there are ways the Commission

could make it an even better investment, but investing in Missouri rate-regulated property already is an extremely attractive proposition. AmerenUE has been investing and will continue to invest in its Missouri system (TR 542-543), and it proudly trumpets this fact to investors, despite the different story it is telling to the Commission here.

AmerenUE does not argue that it is facing anything other than a routine shortfall in earnings. It does not argue that any specific harm will befall ratepayers if the interim increase is not granted. It does not argue that any specific benefit will accrue to ratepayers if the interim increase is granted. It did not present evidence that any specific capital projects have been canceled because of what it considers excessive regulatory lag. It did not present evidence that any specific capital projects will be undertaken if the interim increase is granted. It did not present evidence that it has taken significant steps to control costs and achieve efficiencies. In short, the only sure result – if the Commission abandons 60 years of precedent and grants the interim increase – is that AmerenUE's profits will increase. Moreover, every utility that can make a *prima facie* showing that it is missing its authorized return on equity by a few percentage points will argue that it deserves a similar profit boost. The Commission has given AmerenUE more than an adequate opportunity to prove that there are good reasons other than increased profits to award an interim increase, and AmerenUE has wholly failed to do so.

Public Counsel has filed three lengthy pleadings in this case arguing against awarding interim relief. In this brief, Public Counsel will generally not repeat the arguments raised in those pleadings (incorporated herein by reference), but instead will focus on the following four points:

1) the implied power of the Commission to deal with emergencies does not allow it to grant interim increases merely to increase profits;

2) regulatory lag must be properly defined and understood;

3) even if the Commission could award an interim increase in the absence of an emergency, AmerenUE has not shown that one is warranted in the current situation; and

4) no Public Service Commission in Missouri's history has granted an interim increase simply to increase a utility's profits.

1. The Commission cannot grant an interim increase absent an emergency or near-emergency

The general rule is that when a statute expressly authorizes an agency to do something in a certain way, the statute necessarily precludes any implied authority to do it some other way:

> Where the statute (Section 8548) "limits the doing of a particular thing in a prescribed manner, it necessarily includes in the power granted the negative that it cannot be otherwise done." Keane v. Strodtman, 323 Mo. 161, 18 S.W. (2d) 896. See, also, Dougherty v. Excelsior Springs, 110 Mo. App. 623, 85 S.W. 112; Taylor v. Dimmitt, 326 Mo. 330, 78 S.W. (2d) 841. **In other words, there can never be an implied power given a county or other public corporation when there is an express power.**[1]

The courts are generally circumspect in finding implied powers, and find such powers only if clearly implied by statute or necessary to carry out the express powers granted:

> "If such power existed at all, it must be looked for among the powers which can be implied only as being **essential** to effectuate the purpose manifested in an express power or duty, conferred, or imposed upon the County Court by Statute." King v. Maries County, 297 Mo. 488, 249 S.W. 418, 420. In this case no implied powers to regulate or control are essential to effectuate the purpose manifested in the express powers granted the County Courts under Sec. 311.220, supra.[2]

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[1] Lancaster v. County of Atchison, 352 Mo. 1039, 1046 (Mo. 1944); emphasis added.

[2] State ex rel. Floyd v. Philpot, 364 Mo. 735, 744-745 (Mo. 1954); emphasis added. Indeed, most Missouri cases discussing powers derived by implication as opposed to express statutory

And even if an entity is found to possess certain implied powers, those powers are held to be only as broad as necessary and no more. In a unanimous decision of the Missouri Supreme Court in a case examining the extent of the implied authority of a state agency, the Court found it obvious that an agency's implied authority is severely limited:

> The Judicial Finance Commission has specific authority to make factual determinations regarding the reasonableness of the circuit court's budget. That duty includes the discretion to determine the reasonableness of part or all of any particular budget item, as well as the reasonableness of the total amount budgeted. Incidental and necessary to the proper discharge of the Commission's function is a mechanism for avoiding disruption of critical government services while the reasonableness of the circuit court's budget estimates are being resolved. Thus, the Judicial Finance Commission has implied authority to order the effective date of the appropriation of the new budget delayed until the Commission has had an opportunity to conduct its review of the facts. **Naturally, that implied authority should be exercised with great restraint and only when it clearly appears that failure to grant temporary relief will result in the disruption of vital public services** and the party seeking relief has been diligent in obtaining review.[3]

Thus, when the Laclede[4] court found that the Commission had an implied power to deal (by awarding an interim increase) with an emergency situation that could have lead to a utility financial crisis or the impairment of safe and adequate service, it was because such an implied power was essential to the Commission's *raison d'etre*. The Commission exists to ensure that the public is provided with continuing safe and adequate utility services; if such provision is threatened, the Commission must necessarily have the power to deal with the threat even if such

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authority use such terms as "necessary implication" (*e.g.*, In re Estate of Moore, 354 Mo. 240 (Mo. 1945) or "clearly implied" (*e.g.*, State ex rel. Spink v. Kemp, 365 Mo. 368, 399 (Mo. 1955)).

[3] State ex rel. Twenty-Second Judicial Circuit v. Jones, 823 S.W.2d 471 (Mo. 1992); emphasis added.

[4] State ex rel. Laclede Gas Co. v. Public Service Commission, 535 S.W.2d 561 (Mo. App. 1976)

power is not explicitly set out in the statutes. The same cannot be said for a non-emergency situation in which a utility believes it is earning a somewhat inadequate profit.[5] The Commission has express authority to remedy inadequate returns by raising rates after considering all relevant factors in a general rate case, and the Commission cannot claim an implied power when it has an express power.

Cases dating back to the very beginning of utility regulation in the early 1900s recognized that public utility commissions were designed to have limited powers:

> Furthermore, the Public Service Commission, being a creature of the statute, can only exercise such powers as are expressly conferred on it; and the statute conferring such powers, to authorize action thereunder, should clearly define their limits. Nothing should be left to inference **or seek refuge in implication or the exercise of a discretion.** The language of the New York Court of Appeals in People ex rel. v. Willcox, 200 N.Y. 431, 94 N. E. 215, is apposite in this connection; that: "**The public service commissions were given extensive powers; but they should not be extended by implication beyond what may be necessary** for their just and reasonable execution. They are not without limits, when directed against the management, or the operations, of railroads, and the commissions cannot enforce a provision of law, unless the authority to do so can be found in the statute. . . . Nor should they reach out for dominion over matters not clearly within the statute."[6]

Other cases have reiterated the concept that implied powers only exist to the extent necessary to allow an entity to effectively use its express powers:

> In Love 1979, however, the purchase of the steam plant and loop Bi-State was an intermediate step necessary to achieve the mandate of the statute. Implied powers

[5] AmerenUE, in some of its testimony, appears to argue that it is not making a profit unless it earns in excess of its authorized return on equity. Mr. Baxter, for example, testified that return on equity – profit – is a cost (see, *e.g.* Exhibit C, Baxter Surrebuttal on interim rates, page 4; TR page 329), and that AmerenUE is not covering its costs (*i.e.*, is unprofitable) unless it earns at least its authorized return on equity. Such sophistry aside, if AmerenUE covers its costs and earns at least some return on equity, it is operating profitably even if not as profitably as it desires.

[6] State ex rel. United R. Co. v. Public Service Com., 270 Mo. 429, 442-443 (Mo. 1917); emphasis added.

> are powers not expressed but necessary to render effective the power that is expressed. Reilly v. Sugar Creek Township of Harrison County, 139 S.W.2d 525, 526 (Mo. 1940). In the present case, providing an insurance package is a way to provide insurance at less cost to the members and is not an intermediate step in providing insurance. Provision of liability insurance is not dependent on provision of other types of coverage. The uncontradicted evidence shows that liability insurance for the members may be more difficult to obtain and more expensive but that it would not be impossible to obtain or purchase. While inclusion of other forms of insurance coverage would certainly be to the benefit of the municipalities, such coverage is not necessary to achieve the mandate of the statute.[7]

Here, while an interim rate increase, granted without an examination of all relevant factors, would certainly be to the benefit of AmerenUE's shareholders, it is equally certainly not necessary to achieve the mandate of the statute.

The Fischer case, because it follows and cites both Laclede and UCCM, can be viewed as the definitive statement on the derivation and extent of the Commission's power to grant interim rate increases:

> The inquiry is properly begun by reviewing the origins of the Commission's power to grant interim rate increases. While no express statutory provision exists as to such authority, this court held in State ex rel. Laclede Gas Co. v. Public Service Commission, 535 S.W.2d 561 (Mo. App. 1976), that the Commission has the authority to grant interim rate increases implied from the "file and suspend" sections, §§ 393.140 and 393.150. This court held that the Commission's authority to grant an interim rate increase is **necessarily implied from the statutory authority granted to enable it to deal with a company in which immediate rate relief is required to maintain the economic life of the company** so that it might continue to serve the public. The court, citing Laclede, recognized the Commission's power to grant interim rate increases in State ex rel. Utility Consumers Council of Missouri, Inc., v. Public Service Commission, 585 S.W.2d 41, 48[4] (Mo. Banc 1979).[8]

2. Regulatory lag defined and defended

[7] Crist v. Missouri Intergovernmental Risk Management Asso., 1988 Mo. App. LEXIS 203, 8-9 (Mo. Ct. App. 1988)

[8] State ex rel. Fischer v. Public Service Com., 670 S.W.2d 24, 26 (Mo. Ct. App. 1984); emphasis added.

The rationale that AmerenUE uses to justify the granting of an interim increase is that regulatory lag in Missouri is excessive. AmerenUE defines regulatory lag as the time it takes the regulatory system to adjust rates to reflect changes in specific costs or investments from the time those costs are incurred or those investments made. (Exhibit A, Baxter Direct, page 2) Counsel for AmerenUE reiterated this definition at the evidentiary hearing. (TR 615)

A more accurate definition of regulatory lag is the period of time from when it is determined that earnings level of a utility has become either too high or too low relative to current market conditions and when rates can be readjusted to reflect the rate change necessary to eliminate the under/over earnings situation. (TR 623-624). In other words, regulatory lag is not the period of time it takes to reflect a certain specific investment or cost in rates, but rather the time it takes to adjust rates once it is known that an adjustment may be warranted.

Of course, lag is not unique to regulated companies. Few, if any, businesses operate in an environment that allows them to immediately adjust the prices of their products to account for changes in their costs or investments. As Missouri Industrial Energy Consumers witness Gorman noted:

> [T]he lag in changing prices to reflect -- to reflect increased or decreased costs is not unique to regulated utility enterprises. Competitive companies may have contractual lags or may have limitations on market pricing to change prices to reflect changes in their cost structure. So it's not unique to a utility company. (TR 537)

The regulatory process used in Missouri is referred to as "Rate of Return Regulation" and is consistent with the standards set out in the seminal cases of Hope and Bluefield[9] where the focus of the process is on the earnings of a utility and the resulting ability to attract capital

[9] Federal Power Commission v. Hope Natural Gas, 320 US 591 (1942) and Bluefield Water Works and Improvement Company v. Public Service Commission of West Virginia, 262 US 679 (1923)

investment. In order to understand the relationship of the regulatory process of setting rates and the evaluation of whether or not a rate change is necessary, one must understand the revenue requirement formula. The basic revenue requirement formula is:

Revenue Requirement = Operating Expenses + Depreciation Expense + Taxes + Cost of Capital. (TR 608) Another way to express the formula is:

*Revenue Requirement = Operating Expenses + Depreciation Expense + Taxes + Interest Expense + ROE% * Rate Base*

The regulatory process calculates the Revenue Requirement necessary and compares those revenues to the level of revenues generated by current rates, (i.e. current revenues). If a difference exists between the Revenue Requirement and Current Revenues, rates are changed so that the needed level of revenues can be generated. It must be recognized that the revenue requirement formula is solving for the total revenues needed. The use of current revenues in the process is only necessary so that the "change" in revenues can be determined and communicated to the public or other interested parties. The current level of revenues is not necessary to determine the revenue requirement, but only to determine revenue shortfall or excess.

Once rates are set in a rate case, a continuing analysis determines whether or not the utility's earnings are adequate using rate of return as the basis for this determination. If the return is not equal to the current level of capital market equity costs, a rate change may be warranted. A more detailed evaluation must be made to ensure that the actual results from the period reviewed do not require adjustment to eliminate events or other factors that would not be considered or be adjusted in the regulatory process. It is the entire rate of return analysis that

determines whether a utility's rates are adequate, inadequate or excessive. One cannot look simply at an increase in rate base and conclude that a utility's rates must be inadequate.

Once regulatory lag has been properly defined, the next question is whether it needs to be reduced or eliminated. Even AmerenUE concedes that some regulatory lag can be a good thing. (Exhibit A, Baxter Direct, page 8) Public Counsel witness Trippensee noted the testimony of a witness in a Southwestern Bell case about the beneficial effects of regulatory lag:

> The incentives for regulated entities to achieve efficiencies are virtually the same as for firms in the unregulated sectors. For utilities, once service rates have been set, realized earnings will depend upon actual revenues and costs going forward. To the extent the utility can improve its efficiency and reduce costs, it will enjoy a return greater than that authorized, other things remaining constant. When another rate case occurs, tariffs are revised to conform to the utility's new cost structure. Any economic rents are eliminated, and the benefits of improved efficiency are passed on to customers in the prices charged for utility service.
>
> This outcome of the regulatory process is no different than markets provide under perfect competition. Just as the competitive firm introducing efficiencies enjoys greater returns during the transition period when competing firms are attempting to achieve the same improvements, regulated utilities have the incentive to increase the efficiency of their usage of all resources -- labor, capital, and technology -- in order to earn transitory profits above the authorized rate of return between rate cases.[10]

The academic literature on utility regulation similarly recognizes that it is beneficial. Alfred E. Kahn notes:

> The regulatory lag – the inevitable delay that regulation imposes in the downward adjustment of rate levels that produce excessive rates of return and in the upward adjustments ordinarily called for if profits are too low – is thus to be regarded not as a deplorable imperfection of regulation but as a positive advantage.[11]

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[10] Exhibit N, Trippensee Rebuttal, page 13; citing the Rebuttal Testimony of William Avera in Case No. TC-89-14, page 62 – 63.

[11] Alfred E. Kahn, The Economics of Regulation, Principles and Institutions, MIT Press, 1989, Volume 2, page 48.

And Bonbright *et al.* similarly pronounce "Quite aside from the recognized undesirability of too frequent rate revisions, commissions recognize the regulatory lag as a practical means of reducing the tendency of a fixed-profit standard to discourage efficient management."[12]

3. AmerenUE's current situation does not warrant an interim increase, even if the Commission had the power to grant one

As discussed above, the Commission has neither express nor implied authority to award an interim increase except to alleviate or avert an emergency. No such emergency exists, so the Commission would be exceeding its statutory authority if it were to grant an interim increase. But even if the Commission disagrees and believes that it has the implied power to grant an interim increase purely to increase profits, the record in this case does not demonstrate any compelling reason to do so.

One of AmerenUE's constant refrains is that it is "chronically" unable to earn its authorized return. (See, *e.g.*, Exhibit C, Baxter Surrebuttal, page 6). Yet Mr. Baxter frankly admitted that the term chronic would not be accurate if one looked a period going back more than the last several years. (TR 331). In the normal cycles of business for a regulated utility, several years does not make for a "chronic" condition. In fact, as noted in previous Public Counsel pleadings, AmerenUE had – until the last several years – gone twenty years with flat or declining rates. If there is any kind of a chronic condition with respect to AmerenUE's earnings, history demonstrates that AmerenUE chronically exceeds its authorized rate of return. In fact, over the last twenty-five years, regulatory lag has worked in AmerenUE's favor about ten times

[12] Bonbright, Danielson, and Kamershen, Principles of Public Utility Rates, Second Edition, 1988, page 198

as long as it has worked to AmerenUE's detriment. Truly, AmerenUE is crying crocodile tears over the "chronic" effects of regulatory lag.

The main issue with granting interim rate increases is that the parties are not able to investigate and the Commission is not able to address all relevant factors that may be affecting a utility's financial results. MIEC witness Gorman summed it up concisely: "It would not have been possible to adequately review all the relevant factors to determine whether or not a rate increase of any sort is needed on an interim basis in [the two months since the Commission issued its October 7th order scheduling the evidentiary hearing.]" Even AmerenUE admitted that there are "many other[]" factors affecting its results that have not been addressed in this proceeding. (TR 380). And the record reveals that there are many relevant cost factors that are declining. MIEC witness Gorman listed some of them (and apparently would have listed more had he not been stopped by AmerenUE counsel):

> [C]ommodity costs have come down substantially relative to last year. Fuel costs over long periods of time, if they haven't been hedged, eventually will come down. It's my understanding that steel, copper, aluminum prices have come down substantially this year relative to last year. I understand AmerenUE has undertaken a voluntary and mandatory employee reduction program that will reduce their labor and benefits expenses. Cost of capital has come down in this case relative to the last case. Single A rated utility bond yield in this case is lower than it was at the time of Ameren's last rate filing. Moody's has increased Ameren's senior secured bond rating in this case which would lower its cost of capital. Ameren's capital structure even with the equity infusion that took place at the end of September of this year has a lower percentage of common equity than the capital structure used to set rates. That will lower its cost of capital. (TR 519-520)

AmerenUE asserts that the Commission should grant an interim increase to take a step to reduce what it considers to be "excessive regulatory lag." The record in this case demonstrates that by the most relevant objective measure – credit ratings – AmerenUE is faring quite well under

Missouri's regulatory framework. MIEC witness Gorman testified, and AmerenUE does not dispute, that AmerenUE's credit ratings "are very strong for an integrated electric utility, both in comparison to other Ameren affiliates and around the country." (TR 535)

4. No Commission in Missouri's history has granted an interim increase merely to increase profits

AmerenUE has only been able to cite to three cases in Missouri – ever – that do not explicitly apply the emergency or near-emergency standard, and only two of these actually granted an interim increase. The first of these, in which the Commission declined to award interim relief, is a 1997 Empire case. But in Empire's next interim increase request (in 2001), the Commission noted that it had briefly flirted with applying a "good cause" standard in that 1997 case, and it **clearly rejected** that "good cause" standard in its order in the 2001 case:

> As Empire notes in its pleadings, the Commission did partially develop a "good cause" standard for interim relief in In Re The Empire District Electric Company, 6 MoPSC 3rd 17 (Case No. ER-97-82). However, in that case the Commission based its denial of Empire's request on its conclusion that: "There is no showing by the Company [Empire] that its financial integrity will be threatened or that its ability to render safe and adequate service will be jeopardized if this request is not granted." The differences, if any, between this good cause standard and the historically applied emergency or near emergency standard were not clearly annunciated, and the Commission now returns to its historic emergency or near emergency standard.[13]

[13] In the Matter of Tariff Revisions of The Empire District Electric Company Designed to Increase Rates on an Interim Basis for Electric Service to Customers in its Missouri Service Area, Case No. ER-2001-452, Order issued March 8, 2001, Mo. P.S.C. 3D 124, 2001 Mo. PSC LEXIS 578

The other two cases are even less convincing. In the Timber Creek Sewer case,[14] the Commission applied what appears to be a "near emergency" standard even though it did not use that phrase:

> Thus, it is reasonable to conclude that as of the time of the true-up, September 30, 2007, Timber Creek will be earning $115,310 per year less than necessary to meet its revenue requirement. In addition, **$115,310 per year for a small company like Timber Creek is a significant amount that if forgone could quickly threaten the company's financial integrity and even its ability to provide safe and adequate service**. The company originally indicated its need for a revenue increase in March. Suspending the general rate increase while waiting an additional 6-11 months for a decision regarding the connection fee could be detrimental to the company's operations.

The last of the only two cases that AmerenUE cites to counter sixty years of precedent is a Citizens Electric case.[15] It is perhaps even more easily reconciled with the unbroken line of cases hewing to the emergency or near-emergency standard than the Timber Creek case. The Commission's order stated:

> Citizens stated that without the interim increase, it would suffer the loss of approximately $13,000 per day under the new contracted price for power.
> ...
> Citizens Electric Corporation is a uniquely situated entity. Like most of the utilities that come before the Commission, it is a corporation established under Chapter 351 RSMo. Unlike other corporate entities regulated by the Commission, however, Citizens is structured such that it operates on a business plan similar to a cooperative electric corporation. Citizens' stockholders are also the consumers of the power that Citizens sells. Citizens refers to these consumers as members. Under Citizens' business plan, all revenues in excess of costs are returned to its members in the form of capital credits. Because of its business plan, Citizens has many of the same characteristics of a rural electric cooperative.

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[14] In the Matter of Timber Creek Sewer Company, Inc.'s Tariff Designed to Increase Rates for Sewer Service, Case No. SR-2008-0080, Order issued October 30, 2007; emphasis added.

[15] In the Matter of the Application of Citizens Electric Corporation for Approval of Interim Rates, Subject to Refund, and for a Permanent Rate Increase, Case No. ER-2002-217, Order issued December 20, 2007, 11 Mo. P.S.C. 3D 30, 2001 Mo. PSC LEXIS 1817

> Citizens does not generate any power. Citizens purchases all of its power under contracts in the wholesale energy market. Citizens recently completed negotiations for a new purchased power agreement which will increase the costs of its wholesale power by 15 percent beginning January 1, 2002. Citizens has not requested a general rate increase since 1982.
> ...
> The Commission finds that the agreement is reasonable in that it provides for just and reasonable rates to be set in the ongoing permanent rate case and it allows Citizens to recover in the interim, subject to refund, the increased costs of its new purchased power agreement. **Therefore, Citizens will be able to provide safe, adequate and reliable service without incurring additional debt or impairing its financial stability.**
> Without the interim increase in rates, Citizens would be placed in the position of losing substantial income each day after January 1, 2002. This potential loss in income would cause Citizens difficulty borrowing money to maintain other operations and proceed with its construction contracts, **negatively impacting Citizens' ability to provide safe, adequate and reliable service to its members.** In addition, because of its unique business plan, the increased interest on borrowed money will ultimately be paid by the consumers themselves, by virtue of their positions as stockholders. **Citizens also indicated that financial problems could result in the elimination of services to the members.**
> ...
> **Because Citizens' organization is very similar to a rural electric cooperative, the Commission finds that it is differently situated than other electrical corporations regulated by the Commission. Therefore, the Commission concludes that it is appropriate to grant interim rate relief on a nonemergency standard in this instance** to permit interim rates....

AmerenUE explicitly denies that it will incur any financial problems or that it will have any difficulty continuing to provide safe and adequate service if the Commission declines to award an interim increase. Thus the instant case is very different from both the Timber Creek case and the Citizen's Electric case.

What is glaringly obvious, even viewing these two cases in the light most favorable to AmerenUE, is that neither granted interim relief simply to increase the utility's profit. Even though the Commissions deciding those cases did not use the term “emergency or near-

emergency," it is clear that the circumstances in both cases were threatening to service quality and financial integrity, unlike the circumstances in the instant case.

Conclusion

The Commission should reject AmerenUE's request for an interim rate increase for the reasons stated herein and in Public Counsel's prior pleadings.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing has been emailed to parties of record this 21st day of December 2009.

/s/ Lewis R. Mills, Jr.