Exhibit No.:	______________
Issue(s):	Fuel Adjustment Clause
Witness/Type of Exhibit:	Mantle/Rebuttal
Sponsoring Party:	Public Counsel
Case No.:	ER-2016-0023

REBUTTAL TESTIMONY

OF

LENA M. MANTLE

Submitted on Behalf of the Office of the Public Counsel

EMPIRE DISTRICT ELECTRIC COMPANY

CASE NO. ER-2016-0023

** **

Denotes Highly Confidential Information that has been redacted

May 2, 2016

NP

BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

In the Matter of The Empire District Electric Company's Request for Authority to Implement a General Rate Increase for Electric Service	))))	Case No. ER-2016-0023

AFFIDAVIT OF LENA M. MANTLE

STATE OF MISSOURI)) ss COUNTY OF COLE)

Lena M. Mantle, of lawful age and being first duly sworn, deposes and states:

1. My name is Lena M. Mantle. I am a Senior Analyst for the Office of the Public Counsel.

2. Attached hereto and made a part hereof for all purposes is my rebuttal testimony.

3. I hereby swear and affirm that my statements contained in the attached testimony are true and correct to the best of my knowledge and belief.

Lena M Mantle

Lena M. Mantle
Senior Analyst

Subscribed and sworn to me this 27th day of April 2016.

NOTARY PUBLIC NOTARY SEAL STATE OF MISSOURI

JERENE A. BUCKMAN
My Commission Expires
August 23, 2017
Cole County
Commission #13754037

Jerene A. Buckman

Jerene A. Buckman
Notary Public

My Commission expires August 23, 2017.

INDEX

Purpose	1
Fairness of FAC	2
Off-System Sales and Purchased Power Definitions	12
Addition to Empire’s Monthly FAC Submission	17

REBUTTAL TESTIMONY

OF

LENA M. MANTLE

THE EMPIRE DISTRICT ELECTRIC COMPANY

CASE NO. ER-2016-0023

Q. Please state your name and business address.

A. My name is Lena M. Mantle and my business address is P.O. Box 2230, Jefferson City, Missouri 65102.

Q. Are you the same Lena M. Mantle that provided direct testimony in this case?

A. Yes.

<u>PURPOSE</u>

Q. What is the purpose of your rebuttal testimony?

A. In this rebuttal testimony, I respond to two points in the direct testimony of the Empire District Company ("Empire") witness Todd W. Tarter with respect to the fuel adjustment clause ("FAC") and specifically:

1. The "fairness" of an FAC to all sides as described by Mr. Tarter's testimony; and

2. Definition of off-system sales and purchased power.

In addition, Office of Public Counsel ("OPC") is requesting the Commission add an additional information requirement for Empire to be included in its monthly FAC report submissions if the Commission does not agree to OPC's recommendation to discontinue Empire's FAC.[1] OPC requests the Commission require Empire to include in its monthly FAC submission the FAC costs and revenues by the major and minor accounts for that month and the twelve months ending that month.

FAIRNESS OF FAC

Q. Does the FAC process produce a result that is "fair to all sides" as Mr. Tarter asserts on page 9 of his direct testimony?

A. While there could be benefits to both Empire and its customers, the FAC is not equally "fair" to all sides. Fairness, as defined by Merriam-Webster, is the "lack of favoritism toward one side or another."[2]

Q. Would you please explain?

A. An FAC provides greater benefits to the electric utility than it does to its customers. With the FAC proposed by Empire, the risk to it of non-recovery of increased costs or decreased revenues included in the FAC ("FAC costs") is minimal.

---

[1] *Staff's Rate Design And Class Cost-Of-Service Report*, page 40
[2] http://www.merriam-webster.com/thesaurus/fairness

Q. Empire is proposing continuation of the FAC 95%//5% sharing mechanism. With this sharing mechanism, is Empire taking on some of the risk of increasing costs?

A. If fuel costs are correctly set in this rate case, the risk to Empire of not recovering its FAC cost is minimal. Its 5% of the sharing mechanism is actually 5% of the difference between the FAC costs included in base rates and what it actually incurs. As described in the whitepaper attached to my direct testimony as Schedule LMM-3,[3] with the sharing mechanism proposed by Empire, if the actual costs were 10% higher than what was included in base rates, Empire would recover 99.5% of its FAC costs. Even under the very unlikely circumstance actual costs would be more than 150% of the FAC costs included in base rates, Empire would still bill its customers 98.3% of its FAC costs. The FAC as proposed by Empire is a guaranteed recovery of almost all of the increases in FAC costs without taking into account decreases in non-FAC costs.

Q. Is there a measure of how much Empire is willing to pay for this reduction in its risk?

A. Yes. Under traditional ratemaking without an FAC, any decrease in fuel costs or increases in fuel related revenues would result in an increase in earnings for Empire. Therefore, a measure of how much Empire is willing to pay for this

[3] Page 11

reduction in its risk can be measured by the amount of decrease in the FAC costs Empire is willing to return to its customers.

Q. Do you have a measure of that amount for Empire?

A. Empire is willing to return at least $7.4 million to its customers to reduce its risk of recovery of increased fuel costs.

Q. Would you please explain?

A. For the two FAC accumulation periods[4] ending just prior to Empire filing its requested increase in this case,[5] Empire's FAC costs for its Missouri customers were $7.8 million less than the FAC costs included in its base rates set in the last case. The FAC approved by the Commission in the last case requires Empire to return 95% of that savings ($7.4 million) to its customers. Under traditional ratemaking without an FAC, this decrease in FAC costs would have resulted in an increase in Empire's earnings. Despite having to return $7.4 million of revenue, Empire chose to request continuation of its FAC in this case. This demonstrates Empire values the reduction in risk provided by an FAC by at least $7.4 million.

Q. Does the reduction in risk to Empire with respect to FAC costs bring any benefits to the customers?

A. Yes. Investor rating agencies view an FAC as a positive in determining Empire's ratings outlook and, in turn, may reduce Empire's cost of credit and therefore

[4] Accumulation period 13 and 14 encompassing the twelve months ending August 31, 2015
[5] October 16, 2015

reduce costs to Empire's customers. However, it is just one consideration of many in determining Empire's ratings outlook.

Q. Is there a measure of the benefit to customers of this positive impact of an FAC on Empire's investor ratings outlook?

A. No. Because of the complexity of determining a rating and the numerous variables involved, there is no measure of the benefit of the impact of an FAC on a utility's investor rating or the utility's credit. Therefore, there is no way to measure this benefit to the customer.

Q. Does this reduction in Empire's risk result in any detriment to its customers?

A. Yes. Customers lose their ability to control their electric bill. With traditional ratemaking, the customer can, within a billing season,[6] manage their bill by controlling how they use electricity. If they use the same amount of electricity in two different billing periods in the season, their bills will be the same. If they used less electricity in a billing season, their bill will be lower. With an FAC, customers lose that control. Their bills for the same amount of electricity usage in different billing months in a season may not be the same because of changes to the FAC rates. If the FAC rate does change in the billing season, the customer's bill may actually increase even if they use less electricity.

While customers do appreciate lower bills when FAC costs are declining, the impact of increasing customer bills during times of increasing costs creates uncertainty regarding the amount of the bill and can put a strain on customers' budgets.

Q. Can this detriment be measured?

A. Yes, but it is different for each customer. For customers with some discretionary income, the detriment is likely to be minimal. However, for customers with little to no discretionary income, the detriment is measured in food and medicine that cannot be purchased as an example.

Q. Is Mr. Tarter's statement[7] that "the FAC conveys a more accurate cost of electric energy to Empire's customers" accurate?

A. No, it is not. Empire's FAC is designed to accumulate FAC costs for comparison to the costs included in base rates over a six month time period. It then takes three months to get the FAC rate changed to reflect the difference between the costs included in base rates and the actual incurred costs during those six months. Those FAC rates, which reflect the fuel costs from the prior nine months, are charged for the next six months. By the time that the customers are billed the FAC rate, it is not an accurate measure of fuel cost at the time that the customers receive their bills. In fact, there are times the FAC sends the wrong price signal.

[6] Billing seasons for Empire are Summer (June through September) and Other (October through May)
[7] Direct testimony, page 9

Q. Would you give an example of when this has occurred?

A. Yes, I will. This occurred recently with Empire's FAC where its FAC costs for the accumulation period of March 2014 through August 2014[8] were above the costs included in base rates resulting in positive FAC rates. These positive FAC rates resulted in higher bills for Empire's customers in the recovery period of December 2014 through May 2015. This FAC rate sent a signal to Empire's customers that fuel and purchased power costs were increasing. However, the FAC costs that Empire was incurring for this same time period of December 2014 through May 2015 were actually decreasing. The positive FAC rate a price signal to Empire's customers that costs were increasing at a time costs, were actually decreasing.

Q. Mr. Tarter states that "[t]he fixed energy pricing system that Missouri used prior to the FAC tended to shield the customer from the true cost of electric energy, which may hamper the customers' adoption of or participation in energy efficiency programs." Do you agree with Mr. Tarter?

A. No, I do not. As discussed above, FAC rates do not necessarily send proper price signals. If Empire's customers made a decision regarding the purchase of a higher efficiency air-source heat pump based on their bills in December 2014 through May 2015, the decision was made on inaccurate information.

[8] Accumulation period 12

Empire's FAC rates change every six months. Therefore, the payback of the energy efficiency measure will change every six months if the FAC rate is included in determining participation of energy efficiency programs. Long-term decisions regarding the adoption of or participation in energy efficiency programs should be made using the base rates of the utility and should not include the FAC rates.

Q. Is there an aspect of fairness that Mr. Tarter did not discuss?

A. Yes. An FAC removes an aspect of fairness to the customers that occurs under traditional ratemaking with no FAC. The number of decisions made by the electric utility affecting FAC costs are substantial. There are big decisions like what type of generation should be built and small decisions like when to do maintenance on a piece of equipment in a power plant. Under traditional ratemaking, imprudence in electric utility decision-making regarding fuel and purchased power, both the small and large decisions, directly impacts the utility. Any financial impact of imprudence reduces earnings automatically. Likewise, the financial impact of efficient and prudent decisions increase the earnings of the electric utility. This method is fair because the party making the decisions, the utility, bears the consequences of its decisions.

However, with an FAC, this fairness aspect of traditional ratemaking is removed. The cost of an imprudent action is passed on to the customer until Staff or an intervenor discovers wrong-doing and the Commission finds the utility to be imprudent. This is unfair to the customers who must rely on the discovery of imprudence and then imprudence wait for that imprudence to be proved by parties whose source of information regarding imprudence is the utility.

In practice, Staff and intervenors bear the burden of reviewing thousands of decisions, finding imprudence, and proving any imprudent fuel and purchased-power cost decisions by utility management had a financial impact on customers. The utility makes all of the fuel and purchase power cost decisions and determines what and how to document these decisions complicating the ability to find and prove imprudence by other parties.

In addition to these difficulties, the amount of time that passes between the occurrence of imprudence and the return to the customers of any increase in cost due to imprudence, is a detriment to customers. For example, the last FAC audit[9] conducted by Staff on Empire's FAC was initiated on March 5, 2015 for the time period of March 1, 2013 through February 28, 2015. Staff filed its report[10] finding no imprudence on August 31, 2015 and the Commission issued an order approving the Staff report and recommendation on September 16, 2015. In this case, where no imprudence was found, the time period between when Empire

[9] Case No. EO-2015-0214
[10] *Fifth Prudence Review of Costs Related to the Fuel Adjustment Clause for the Electric Operations of The Empire District Electric Company*, EFIS item no. 4

began incurring FAC costs and the Commission's order[11] was more than thirty months.

Q. Has the Commission found that Empire has been imprudent in any of its FAC cost and revenue actions?

A. No, it has not.

Q. Does this mean that all of Empire's FAC cost decisions have been prudent?

A. Not necessarily. As Staff states in its most recent Empire FAC prudence review report[12] "[b]ased on its review, Staff *found no evidence* of imprudence by Empire *for the items it examined* for the period of March 1, 2013 through February 28, 2015." (Emphasis added) The sheer volume of FAC cost decisions along with the complexities of conducting an FAC audit discussed above leaves doubt in my mind that every decision was reviewed and found prudent.

Q. Are you aware of any imprudence by Empire with respect to FAC costs and revenues?

A. No, I am not. But as described in OPC witness John Riley's rebuttal testimony in this case, OPC is investigating Empire's natural gas hedging practices and policies. At this time OPC does not have enough information to determine imprudence but is concerned about the magnitude of Empire's hedging costs given the current low and stable natural gas market.

[11] *Order Approving Staff's Prudence Audit Report and Recommendation*, EFIS item no. 5
[12] *Fifth Prudence Review of Costs Related to the Fuel Adjustment Clause for the Electric Operations of The Empire District Electric Company*, EFIS item no. 4, page 1

Q. Is there any detriment to an electric utility of having an FAC?

A. Yes, there is a detriment to an electric utility when FAC costs are decreasing. Under traditional ratemaking without an FAC, the utility passes on all of the cost savings to its shareholders. With the FAC currently proposed by Empire, the utility is required to return 95% to its customers and only pass on 5% of the cost savings to its shareholders.

However, the FAC statute allows Empire to request the establishment, modification, and *discontinuation* of its FAC. Therefore, Empire should, each time it files a general rate increase, evaluate whether or not it is in its best interest to request the continuation, modification or discontinuation of its FAC. If the Commission approves an FAC for an electric utility, the customers must pay the FAC charge or face disconnection of service.

Q. Is there a benefit of the FAC to customers when FAC costs are declining?

A. Yes. The bills of customers with an FAC should be lower when FAC costs are declining. However, if an electric utility believes that FAC costs over the next four years are going to decrease, it may request its FAC be discontinued that would also discontinue this benefit to customers.

OFF-SYSTEM SALES AND PURCHASED POWER DEFINITIONS

Q. Mr. Tarter states in several places[13] in his direct testimony that Empire's native load is supplied by the Southwest Power Pool ("SPP") integrated market ("IM"). Does this mean that the SPP generates and provides electricity to Empire to meet the energy requirements of Empire's customers?

A. No, it does not. In his direct testimony, Mr. Tarter explains Empire's resource planning process and how it is responsible for providing capacity and energy to meet its customers' needs at the lowest possible cost.[14] Empire's native load requirement is supplied by its own generation resources and long-term purchased-power contracts supplemented by spot purchases of energy from other members of SPP when the SPP IM market price is below Empire's cost to provide the electricity needed for its customers.

Q. What is Mr. Tarter referring to when he states that the SPP IM "supplies" the energy for Empire's native load?

A. The electricity provided through Empire's generation and purchased power contracts does not flow to an SPP site and then back to Empire's customers. It behaves according to the laws of physics and flows to the closest draw just as it did before the SPP IM. However, the SPP does determine the dispatch of its

[13] Page 11, page 18, and page 20
[14] Page 12

member's resources, including Empire's resources, based on bids placed by the members in its IM. SPP provides a payment to its members for the energy it generates based on this dispatch. Because SPP is providing revenue for the generation it is dispatching, it also charges its members based on their load requirements. When Mr. Tarter states that Empire's native load is "supplied" from the SPP he is referring to the financial transaction Empire enters into with SPP, for the energy that Empire's native load requires. This cost to Empire is offset by the revenue it receives from SPP for Empire's generation resources SPP dispatches.

Very simplistically, if SPP would dispatch Empire's generation resources at exactly the amount of electricity required by Empire's customers, the revenue provided for Empire's generation in the SPP IM would be exactly the same as the cost SPP charged for Empire's native load. The revenue and costs would net to zero.

Q. Why is it important to understand this distinction?

A. It is important because the payment provided to the SPP is sometimes referred to as "purchased power" and the revenue received from SPP is referred to as "off-system sales."

However, this is different from the definitions of purchased power and off-system sales at the time Missouri's FAC statute[15] was passed. Purchased power costs and off-system sales are defined on the Commission's Fuel Adjustment Charge fact sheet on its web site[16] attached to this testimony as Schedule LMM-R-1. On this fact sheet, the Commission describes purchased power costs as "costs the company incurs if it has to buy power, either through a contract with another electric utility or on the spot market to meet its customers' needs" and not as all the energy necessary to meet its customers' need. Instead it is based on long-term contract purchases and short-term market purchases to meet the utility's customers' needs.

Q. Does the Commission's fact sheet include a definition of off-system sales?

A. Yes, it does. Off-system sales are defined on the Commission's FAC Fact Sheet as "a term used to describe sales of excess power on the open market by the electric company". Off-system sales as defined on the Commission's FAC fact sheet, is not the power needed for the electric utility's own customers' needs plus any excess generated but the excess generated above the customers 'needs that is sold on the market.

[15] Section 386.266 RSMo
[16] http://psc.mo.gov/CMSInternetData/ConsumerInformation/FAC_.pdf

Q. Why is this important?

A. For FACs in Missouri, it is important to understand there is now more than one definition of purchased-power and off-system sales. Care should be taken, especially in light of the FAC statute, how fuel and purchased power costs, including transportation[17] may be included in an FAC. While the FAC statute is silent with respect to off-system sales revenues, the Commission rules contemplate the inclusion of off-system sales revenues in FACs.[18] Therefore it is important to have a correct understanding of what purchased power and off-system sales mean in each context to get a clear understanding of those costs.

Q. Would you provide an example where it may be confusing?

A. Schedule DCR-d1, attached to Staff's Rate Design and Class Cost-of-Service Report shows Empire estimated normalized off-system sales revenue of $152 million and Staff estimation of $150 million. However, this off-system sales revenue is actually the amount of revenue each party estimated Empire would receive from SPP for dispatch of its resources. It is both the revenue generated for energy generated to meet Empire's load and off-system sales revenues as defined on the Commission's FAC fact sheet.

[17] Section 386.266.1
[18] 4 CSR 240-20.090(1)(B)

Q. Does either Staff or Empire provide an off-system sales revenue estimate for off-system sales as defined as revenue from the sale of electricity above the native load requirements?

A. They do not provide an estimate in their testimony. However, Staff's workpapers show its fuel model estimated normalized spot sales of ** ** million.

Q. Does either Staff or Empire provide an estimated cost of spot purchase power for Empire?

A. According to its direct filing workpapers, Empire did not include any spot market purchases in its calculation of the FAC base rate. Staff included spot purchased power in Schedule DCR-d1 "<u>PURCHASED POWER ENERGY CHARGES</u>" along with the costs of Empire long-term purchased power agreements. Staff's workpapers show its fuel model estimated a normalized ** ** million of spot market purchases.

Q. Are purchased power and off-system sales as defined on the Commission's fact sheet included in Empire and Staff's calculation of the FAC base factor?

A. I have reviewed Staff's fuel modeling workpapers and believe, even though purchased power and off-system sales as defined on the FAC fact sheet are not specifically identified in the costs and revenues used to estimate the FAC base factor, they are included in the calculation of the FAC fact sheet. I cannot discern from Empire's workpapers whether or not they have been included in the calculation of Empire's FAC base factor.

ADDITION TO EMPIRE'S MONTHLY FAC SUBMISSION

Q. If the Commission approves the continuation of Empire's FAC, what is OPC recommending be added to Empire's monthly FAC submission?

A. If they do this, the Commission should order Empire to include in its monthly FAC submissions, by general ledger account, the FAC costs in each of the general ledger accounts Mr. Tarter provides in Schedule TWT-5 of his direct testimony.

Q. Why is this important?

A. This additional information, provided on a monthly basis, would provide more transparency regarding the costs and revenues Empire is including in the FAC.

Q. Does Empire report these costs and revenues in its current monthly submissions?

A. I believe it does. However, it does not report all the costs and revenues by general ledger accounts shown in Schedule TWT-5. However, Empire does provide the costs in FERC account 555 by general ledger account in its monthly FAC submissions.

Q. Does this conclude your rebuttal testimony?

A. Yes.

Fuel Adjustment Charge

A Publication Of The Missouri Public Service Commission

Some electric companies in Missouri have a Fuel Adjustment Charge (FAC) which appears on the monthly electric bill as a separate line-item.

Background

The Fuel Adjustment Charge is not new. In fact, some customers have had an FAC charge on their electric bills since 2007. The charge was created after legislation (Senate Bill 179) was passed in 2006. The FAC is designed to address fuel and purchased power cost volatility, as well as, company off-system sales revenues. Those costs tend to change -- up and down -- quite frequently. The FAC attempts to capture those costs in a more timely fashion so that the company recoups cost increases closer to when those costs occur and consumers benefit faster, in lower rates, when those costs go down.

What Are Fuel And Purchased Power Costs?

Fuel costs are costs the electric company incurs to purchase fuel such as coal, natural gas, uranium, or oil. Those fuels are used to run the power plants that produce the electricity that goes to your home. Purchased power costs are costs the company incurs if it has to buy power, either through a contract with another electric utility or on the spot market, to meet its customers' needs.

What Are "Off-System Sales"?

Off-system sales is a term often used to describe sales of excess power on the open market by the electric company because the price that it receives for the sale is greater than the price to generate power. The revenue from those sales goes toward reducing the overall fuel costs to serve customers.

Does The FAC Ever Change?

Yes. When an electric company seeks to change its FAC, it is required to make a filing with the Missouri Public Service Commission. Under PSC rules, the Commission has 60 days after the filing to make a decision. After the filing is made, it is thoroughly reviewed by the PSC staff. The PSC staff then makes a recommendation to the Commission on whether the filing should be approved. If the filing complies with state law, PSC rules, is mathematically correct and receives PSC staff support, the Commission allows the change.

How Is The FAC Calculated?

The fuel adjustment charge is calculated using actual fuel costs and predicted customer usage. As part of the FAC process, a "true-up" is conducted to make sure what the company paid in fuel costs is what it billed its customers through the FAC charge. An annual true-up is necessary to reflect actual customer usage for that period of time reflected in the FAC charge. Predicted versus actual usage could vary based upon factors such as the weather and economic conditions. If an over-collection or under-collection has occurred, it is ultimately reflected in the customer FAC charges.

For more information

Created in 1913, the Missouri Public Service Commission (PSC) regulates investor-owned telecommunications, water and sewer, natural gas, electric and steam utilities. The PSC works to ensure that Missouri citizens receive safe, reliable and reasonably priced utility services. If you have an inquiry, billing question or service-related problem that your utility provider cannot answer, please call the PSC at **1-800-392-4211** or visit our website at **www.psc.mo.gov**