Additional Public Counsel Comments
Environmental Cost Recovery Mechanism Rules
Case No. EX-2008-0105
January 17, 2008

I am Russell Trippensee. I am the chief utility accountant for the Missouri Office of the Public Counsel. On January 2 of this year, the office filed comments on the Commission's proposed rules published in the Missouri Register on December 3, 2007. The Commission's proposed rules address environmental costs incurred by electric utilities providing retail service in Missouri. These rules are a result of the passage of Senate Bill 179 during the 2006 legislative session. My testimony today is intended to respond to comments filed by various parties to this docket on or after January 2. These comments are not intended to change or supplement the comments OPC filed with one exception; however I would be happy to answer any questions the Commissioners might have regarding those comments.

First, let me thank the Commission for the workshop process that allowed all stakeholders the opportunity to provide input into the Commission's process of drafting these rules. While all the stakeholders could not reach agreement on how the rules should reflect the intent of SB 179, that process was beneficial to all who participated. Public Counsel's comments indicate its belief that the draft rules could be improved in order to meet the goal of regulation, which is to provide safe and adequate service at just and reasonable rates to the customers. Public Counsel believes the comments of the non-utility parties to this case provide other reasonable recommendations for moving closer to that goal. Specifically Public Counsel would echo AARP comments regarding the 2 ½% annual cap and that the appropriateness of inclusion of deferrals in rates be addressed in the subsequent rate case. Public Counsel also would state that this is a hard annual cap and further believes the rules should reflect that this annual cap should not be allowed to accumulate if not used in any year during the four-year duration of an ECRM. That is, if no changes in ECRM eligible costs occur during the first two years of an ECRM, the allowable revenue increase in year three is 2 ½ % and not 7 ½%.

The exception I referenced with regard to Public Counsel's filed comments is that Public Counsel would recommend the paragraph 4 CSR 240-3.162 (2) (O) be deleted in its entirety if the Commission accepts Public Counsel's recommended paragraph 4 CSR 240-3.162 (2) (P). This paragraph contains information contained in Public Counsel's recommended addition of what is labeled paragraph 4 CSR 240-3.162 (2) (P).

My testimony today will focus on the comments filed by the utility parties to this case, specifically the comments filed by the Missouri Energy Development Association and Union Electric Company d/b/a AmerenUE and by inference the concurrence of Kansas City Power & Light Company with the MEDA comments. If implemented, the recommendations of the utility stakeholders would result in a rule that would allow utilities to manage earnings so that excess earnings would be assured, transfer wealth from current and future generations of ratepayers to utilities without any cost of service justification, and ignore the specific language of SB 179. My testimony will also point out that this Commission should question the MEDA representative regarding the ten instances where its comments failed to identify new additions or deletions. MEDA's attempt to insert or delete language without identification could be overlooked if it was an isolated event, but ten separate instances that are contained in six separate sections is at best sloppy and at worst misleading.

OPC Exhibit No. 4
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The comments of MEDA and AmerenUE can be summarized as:

1. The language of SB 179 is difficult to implement so ignore it.
2. The purpose of SB 179 as it relates to environmental costs was to address more than environmental costs.
3. The ECRM should be implemented in a manner consistent with the ISRS (Infrastructure System Replacement Surcharge)
4. Excess Earnings at the expense of ratepayers is authorized by SB 179

The Commission's proposed rules set out a process that develops an environmental cost of service as determined in a rate case. Subsequently, if these costs change, the utility would have the opportunity to request an ECRM adjustment consistent with the language from SB 179 that states a periodic rate adjustment (ECRM) will reflect; "increases or decreases in its prudently incurred costs, whether capital or expense, to comply with any federal, state, or local environmental law, regulation, or rule." In order to measure change, this Commission must have a base from which to measure. The measurement of change is a basic mathematical concept that is embodied in the language of SB 179 requiring that the rate change "reflect increases and decreases". The comments of MEDA and AmerenUE would have this Commission ignore this basic mathematical fact by eliminating from the Commission's proposed rule the requirement to determine the base capital costs in the general rate case.

MEDA's comments propose a new cost definition entitled Base Environmental Expenses to substitute throughout the proposed rule as the base which is subtracted from the new environmental costs (both capital and expense) in order to determine the revenues to collect from ratepayers through the ECRM. MEDA's new cost definition completely excludes capital cost from the determination of its Base Environmental Expense determination. (MEDA page 4, new section (1)(F) The result is that MEDA would have this Commission compare capital costs and expense to MEDA's proposed Base Environmental Expense that excludes capital costs. MEDA justifies this exclusion by stating that determining an environmental and a non-environmental rate base would be "an extremely unwieldy and unreasonable exercise." While I will address the fallacy of this claim which AmerenUE's comments expand on, suffice it to say the Public Counsel does not believe that this Commission should ignore the requirements of SB179 just because some party alleges they will be difficult to comply with.
(MEDA page 5)

MEDA uses the terms "environmental rate base and non-environmental rate base" to distinguish rate base items that are used to comply with environmental rules and rate base components that are not affected by environmental rules. MEDA's comments lists all types of equipment that allegedly would need to be identified as pertaining to environmental compliance and even asserts the Commission would need to get down to a level of detail that looks at items that cost less than $100. AmerenUE's comments exaggerate MEDA's already-exaggerated concerns with a discussion of allocation of items that serve dual purposes. One must even assume that since AmerenUE states that "every single item in a utility's rate base would have to be reviewed and categorized", that AmerenUE would propose to allocate the proverbial president's desk.

Public Counsel would submit that the Commission's proposed definition of environmental cost that refers to "directly related to compliance" clearly indicates that the costs to be considered in the calculation of the costs to be included in base rates are much more narrowly defined than the utility stakeholders have asserted. Public Counsel concurs with the environmental revenue requirement approach in the Commission's proposed rule and believes that investments or costs requiring allocation should not be required to be included in the calculation of environmental costs. Public Counsel recommends that if the investment is recorded as a unit of property in a manner consistent with the Commission's rules on continuing property records and its predominant purpose is directly related to compliance with an environmental rule or law, then that property unit should be included in the ECRM calculation. As example, a power plant may require a pollution control device housed in a structure. In turn that structure might also house ancillary functions not directly related to the pollution control device such as storage. The predominant purpose of the structure is to house the pollution control device, therefore it would be included in the
ECRM calculation.

A second point that must be made pertains to the review of plant investments would be made in the initial case in which a utility files for an ECRM. Once this task is completed and the Commission approves the findings, that work will not need to be performed again as the base line will already be set. Only new investments will need to be reviewed.

It also is critical to point out that the purpose of the ECRM is to address major new environmental investments as are outlined in MEDA's comments. In the next decade, over $4 billion is expected to be invested by Missouri utilities including the co-ops. This Commission is well aware of KCPL's regulatory plan that included over $100 million in environmental upgrades. These levels of investments are easily identifiable as are the property units that they replace if a pre-existing system was installed. The Commission proposed rules recognize that it has discretion to determine which portion of prudently incurred environmental costs should be recovered in an ECRM and what portion should be recovered in base rates. The Commission should recognize that materiality of the investment and the resulting effect on earnings are important factors to consider. Misleading comments that raise red herring issues like identifying and tracking valves costing less than $100 should be ignored.

The utility stakeholders' attempt to get this Commission to ignore environmental capital costs included in base rates when calculating the ECRM is nothing more than a variant on the age old practice of double dipping in which a utility tries to get the Commission to include both a historic cost that has been replaced by another cost along with the new cost. Exclusion of capital costs in base rates from the ECRM calculation would result in double dipping as even assets that had been retired would still be in the total rates being paid by the ratepayers. That clearly is bad public policy.

Public Counsel finds it very enlightening that AmerenUE argues that other parties, specifically mentioning OPC, would argue that an ECRM should address regulatory lag for customers. This is a straw man argument as OPC is not making such an argument. Public Counsel does believe that regulatory lag can certainly provide incentives for a utility to operate in an efficient manner

and that single issue rate mechanisms create distortions in those incentives. It is more telling to read the rest of the sentence where AmerenUE makes the previously mentioned assertion. AmerenUE goes on to indicate that "the proposed environmental rate base fails to recognize that even with an ECRM, a utility will still experience significant regulatory lag for huge costs." AmerenUE concludes the paragraph by talking about all the other increases in operating costs that electric utilities are allegedly experiencing. By ignoring the clear language of SB 179 that requires measurement of the **change** in environmental costs, the utility stakeholders are attempting to use the ECRM to address regulatory lag associated with other costs by having a ECRM calculation that will always result in an overstatement of the change in environmental costs.
(Page 4 of AmerenUE comments)

MEDA and AmerenUE recommend that the Commission look to the Infrastructure System Replacement Surcharge (ISRS) when developing rules for the ECRM. (MEDA page 4, & AmerenUE pages 1, 2, & 6) The utility stakeholders assert that the ECRM should treat capital costs like they are treated in the ISRS. What the utility stakeholders ignore is that the statute enacting the ISRS is completely different than the statute enacting the ECRM. The utility stakeholders also ignore that neither the ISRS or the Fuel Adjustment statutes or rules provide for cap in revenue changes and a deferral of revenues that the utility would receive absent the revenue change being greater than the cap. The deferrals under an ECRM are separate and distinct from the change in the environmental revenue requirement and create the opportunity for the utility to over-earn. This very real possibility is why Public Counsel proposes the Commission look at earnings during the period of any deferral prior to allowing the recovery of any deferred amounts in a subsequent rate case. This review of earnings would not occur in relation to any calculations of the net change in eligible environmental costs and resulting environmental revenue requirement changes subject to the cap.

The ISRS statute is very prescriptive and it is mandatory that the Commission authorize an ISRS in the manner prescribed in the statute if the utility makes qualifying investments as defined in the statute. This is just what happened in Case No WO-2004-0116 when the Commission approved an ISRS increasing rates by over $3.5 million on January 1, 2004 for Missouri American Water. Then less than four months later, the company stipulated to a general rate decrease effective April 19, 2004. The effect of these cases was that ratepayers paid ISRS charges when the utility was experiencing excess earnings. Although such an outcome is allowed – and arguably required – under the ISRS statutes, it is not required by SB 179 and should not be allowed by the Commission's rules implementing SB 179.

The prescriptive nature of the ISRS statute mandated that a rate increase occur despite the fact that the utility was over-earning. The ISRS statute specifically defines the investments to be used in the calculating the ISRS. This prescriptive nature resulted in ratepayers paying for excessive earnings the very first time the ISRS was used. In contrast, the ECRM statute does not provide for mandated rate changes and instructs the Commission to develop rules to implement an ECRM if it finds it appropriate. While Public Counsel or anyone else cannot be absolutely sure, it would be appear that the legislature learned from the ISRS experience. The ECRM statute would seem to reflect that, since the legislature approved an ECRM statute that gave the

Commission a tool it could evaluate and decide how and when to use. The utility stakeholders' assertions that the ECRM should mirror the ISRS is not supported by statutory language, actual ratemaking experience, nor is it good public policy to write a rule for ECRM that is based on conforming to another unrelated statute.

AmerenUE also contends that allowing only two ECRM changes per year is detrimental the utility. The material costs that would flow through an ECRM are the large investments that are summarized on page 2 of the MEDA comments. As this Commission is aware, these types of projects have specific in-service dates. Since the utility will have intimate knowledge of the in-service date and have control of the timing of ECRM filing, these can obviously be managed to minimize any time lag. Also the implied assertion is that these type projects happen more often than twice a year. The Commission only need look at the KCPL Regulatory Plan documents to find that major construction projects are spread out over several years and are known with some precision well in advance of actual occurrence. In contrast, the ISRS projects are part of on-going construction programs consisting of small individual projects that become in-service after short construction schedules often without Allowance for Funds Used During Construction even being appropriate. These projects are closed to plant-in-service each and every month. Some of the replacement programs involved in the ISRS will take upwards of 40 years to complete.

Public Counsel's comments on the Commission's proposed ECRM rules were provided under the belief that the purpose of those rules is to implement SB 179 and maintain the Commission's obligation to ensure that ratepayers receive safe and adequate service at just and reasonable rates. In contrast the utility stakeholders appear to have multiple other goals in their comments that are not supported by either SB 179 or the Commission's obligation to ratepayers as found in case law cited in Public Counsel's filed comments in this docket. As mentioned earlier, the utility stakeholders believe the ECRM should ignore capital costs in base rates in order to increase the ECRM revenues to address regulatory lag with other non-related costs. (AmerenUE page 4 & 7) AmerenUE further argues that the ECRM will not only be "useful to utilities", but also that it will "encourage these investments". SB 179 does not have a purpose section and does not address either of these alleged benefits. However, SB 179 does set out the standard that the costs must be incurred "to comply with any federal, state, or local environmental law, regulation, or rule. Public Counsel fails to see any justification to charge ratepayers excessive revenues in order to incent the utilities to comply with laws regulation or rules properly enacted by government bodies. The incurrence of environmental compliance costs should result from implementing a utility's environmental compliance plan. This plan should be based on prudent planning, not reliance on single issue cost recovery mechanisms to provide an incentive. Nothing in SB 179 suggests that it was intended to incent a utility to prefer certain environmental investments over others or to encourage a utility to make any particular environmental investments sooner than would otherwise be appropriate.

In conclusion, the Commission is charged with protecting the public. The ECRM tilts the ratemaking process toward utility interests. The Commission must create rules implementing an ECRM that does not diminish its ability to ensure that rates are just and reasonable and that excess earnings are not a result of the process. The utility stakeholders assert that there are multiple consumer protections in SB 179 and in the proposed Commission rules. Their characterization is that these protections are adequate for the ratepayer's interest. However, the ratepayer's interest is measured by the goal of safe and adequate service at just and reasonable rates. The so-called protections touted by the utility stakeholders and included in the Commission's proposed rule are only tools, not the actual protection provided by the Commission. Absent the additional language proposed by Public Counsel, these so-called consumer protection tools may be used but they will not result in just and reasonable rates. Absent use of consumer protection tools as modified by the non-utility commenter's to determine or ensure rates are just and reasonable, ratepayers will not be protected by the very Commission charged with that responsibility.

Adopting the changes proposed by utility stakeholders would severely limit the Commission's ability to fulfill its obligation of providing protection to consumers by establishing just and reasonable rates.