

**BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI**

In the Matter of)
Kansas City Power & Light Company's)
Request for Authority to Implement)
A General Rate Increase for Electric Service)

File No. ER-2012-0174

INITIAL BRIEF

OF

SOUTHERN UNION COMPANY

D/B/A MISSOURI GAS ENERGY

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Table of Contents

I. THE PROBLEM.....	3
II. THE PROPOSALS.....	4
III. DISCUSSION AND ANALYSIS	6
A. ISSUES LIST.....	6
B. RESIDENTIAL RATE BACKGROUND.....	6
C. RESIDENTIAL REVENUE-NEUTRAL RATE ADJUSTMENTS.....	9
D. PRIMARY RECOMMENDATION: ELIMINATE AVAILABILITY OF SPECIALLY- PRICED SPACE HEAT RATES.....	16
E. ALTERNATE RECOMMENDATION: FREEZE AVAILABILITY OF SPECIALLY- PRICED SPACE HEAT RATES.....	18
F. RESIDENTIAL RATE DESIGN	19
G. RESIDENTIAL BILL IMPACTS	21
IV. SUMMARY.....	23

I. THE PROBLEM

Seventy-Nine percent (79%) of KCPL's Residential customers are subsidizing specially-priced, discounted rates that encourage the increased use of electricity. For eight months of the year, a Residential General Use customer who does not have electric space heating equipment pays more for electricity than a neighbor who installs electric heating equipment under KCPL's discounted Residential Space Heat rates. These rates are a product of a different era and are at odds with current energy policy priorities which should encourage energy conservation and strive for cost-based rates. No other investor-owned electric utility in Missouri has these specially-priced Residential rates for customers who space heat with electricity.

Electric Space Heat rates are the primary growth area in KCPL's Residential customer base. While overall numbers of KCPL's General Use Residential customers have declined, Residential Space Heat customers have increased - presumably attracted, through false price signals, to this discounted rate. Accordingly, this subsidized rate is unsustainable in the long term - with increasingly fewer numbers of Residential General Use customers supporting discounted rates of increasing numbers of Residential Space Heat customers. The Commission should act now to freeze or eliminate the availability of these rates.

KCPL's existing discounted Residential Space Heat rates are not cost-based and result in the subsidization of Residential winter service by summer service and the subsidization of Residential Space Heat customers by all other Residential customers in the winter. We know this because KCPL's own class cost of service (CCOS) study shows that:

- A. The KCPL winter Residential rate of return is lower than the summer Residential rate of return; and,

B. The KCPL winter Residential Space Heat rate of return is lower than the winter rate of return for Residential General Use and the Residential class as a whole.¹

Importantly, the Staff agrees that winter Residential Space Heat customers' rates must be increased by an amount higher than the system average increase awarded by the Commission in this case in order to move those rates closer to the cost of providing that service.² The Office of the Public Counsel, while not providing testimony on this issue, supports Staff's position. While Staff moves in the right direction, its proposal does not adequately address the problem.³

II. THE PROPOSALS

The following proposals to address the identified problem have been made by the parties in this case:

A. **KCPL** – KCPL has ignored the problem and recommends an across-the-board increase for all rate elements⁴;

B. **Staff** – Acknowledging the existence of the problem, Staff proposes to increase winter Residential Space Heat rates on a revenue neutral basis prior to assignment of any increase awarded in this case⁵; and,

C. **MGE** –MGE proposes that the Commission adjust current KCPL Residential rates on a revenue-neutral basis to remove 100% of the existing seasonal inequities in the collection of revenue in relation to cost, as well as the inequities in the collection of winter revenue among

¹ Exh. 38, Normand Direct, page 23, Table 3.

² Exh. 212, Scheperle Direct, page 3, lines 11-15.

³ Exh. 626, Cummings Rebuttal, page 3, lines 1-16 and Rebuttal Schedule FJC- 1.

⁴ Exh. 41-NP, Rush Direct, page 9, lines 18-20 and Exh. 43-NP, Rush Surrebuttal, page 13, lines 14-16.

⁵ Exh. 212, Scheperle Direct, page 3, lines 11-15.

customers taking service on different rate schedules.⁶ This adjustment would occur whether the availability of Space Heat rates is either frozen or eliminated. MGE recommends that any Residential rate increase that may be awarded in this case should be assigned to Residential rates in a way that preserves the movement to cost-based rates within the Residential class.⁷

After making these adjustments, MGE has two alternate proposals. As its primary proposal, MGE recommends that the Commission eliminate the availability of KCPL's Residential Space Heat rates as a separate rate schedule.⁸ If the availability of Space Heat rates is eliminated, KCPL's current Space Heat winter block rate structure should be used to develop a consolidated General Use rate on which both current General Use and Space Heat customers would take service.⁹ In the alternative, MGE recommends that the Commission indicate its intent to eliminate Residential Space Heat rates in a subsequent rate case, freeze the availability of these rates, and require tariff language to ensure the effectiveness of freezing the availability of the rate schedules.¹⁰ Rates that would result from both elimination and freezing the availability of Space Heat rates on a revenue-neutral basis are illustrated on p. 20 below.

⁶ Exh. 625 Cummings Direct, page 9, line 16 - page 13, line 12; page 18, lines 4-14; page 23, line 3 - page 24, line 18; and Schedules FJC-3 and FJC-8.

⁷ Exh. 625, Cummings Direct, page 26, line 3 - page 27, line 3 and Schedule FJC-9.

⁸ Exh. 625, Cummings Direct, page 19, line 3 - page 21, line 2; Exh. 627, Cummings Surrebuttal, page 10, line 6 - page 13, line 7 and Surrebuttal Schedule FJC-1.

⁹ Exh. 625, Cummings Direct, page 23, line 9 - page 24, line 5 and Schedule FJC-8. As explained in this testimony, the frozen Space Heat-Two Meters rate is not eliminated because KCPL did not provide the necessary billing determinants to include these customers in the consolidated General Use rate.

¹⁰ Exh. 625, Cummings Direct, page 21, line 4 - page 22, line 21.

III. DISCUSSION AND ANALYSIS

A. *ISSUES LIST*

The specific issue of KCPL's specially-discounted rates is represented in the Issues List as a part of KCPL issue 6, as follows:

6. f. Residential rate adjustments:

- i. Should current residential rates be adjusted to reflect a revenue neutral shift seasonally and among residential rate schedules in the winter based on KCPL's class cost of service study?
- ii. How should any residential rate increase be assigned to rate elements?

6. g. Residential Space Heat services:

- i. Should KCPL's Residential Space Heat services be eliminated?
- ii. In the alternative, should KCPL's Residential Space Heat services be scheduled for elimination in a subsequent rate case by freezing their availability in this case?
- iii. Should the Commission adopt Staff's proposal to increase by 5% the first block of the residential space heating rates?

B. *RESIDENTIAL RATE BACKGROUND*

To understand the underlying issues with these discounted rates, it is important to understand how the majority of KCPL's customers pay more for electric service for eight months of the year. The following table shows the portion of KCPL Residential customers now served under each current Residential rate schedule:¹¹

General Use	79%
Space Heat - One Meter	16%
Space Heat - Two Meters (frozen)	5%

KCPL's General Use customer base has steadily declined for a number of years while at the same time its Residential Space Heat customer base has continually grown.¹² This imbalanced growth within KCPL's Residential class has resulted from discounted pricing for

¹¹ Exh. 625, Cummings Direct, page 5, footnote 3. KCPL also has 41 Time of Day customers (0.02%) and 5 Other Use customers (less than 0.01%).

¹² Exh. 625, Cummings Direct, page 16, lines 10-17 and Schedule FJC-6. Even Space Heat - 2 Meters has added some customers since the Commission froze the schedule in 2007.

Space Heat services compared to General Use services, that MGE has shown are neither cost justified nor supported by other valid ratemaking or policy considerations.

As indicated above, the availability of Space Heat – Two Meters rate was previously frozen by this Commission – for many of the same policy, ratemaking, and equity considerations that MGE is arguing in this case. In Case No. ER-2007-0291, the Commission addressed separate all-electric space and separately-metered space heating services provided to KCPL general service customers. In that case, the Commission froze the availability of these services to existing customers' locations and reduced the price advantage of these services over the general service schedules, with findings and decisions that included:

- Waiting until anywhere from 2009 to 2012 to address the rate disparities that the separately-metered space heating and all-electric tariff customers pay compared to the general service tariff customers is waiting too long.
- Trigen's and Staff's argument that increasing all class' rates the same percentage would effectively increase the size of the general service-space heating discounts, and exacerbate the current problem, is compelling.
- In a future rate case, the Commission might be willing to consider eliminating the discounts altogether. Allowing even more customers to use those discounts flies in the face of a possible move, supported by Staff, towards eliminating them entirely.¹³

MGE believes that the Commission should make similar findings regarding KCPL's Residential Space Heat rate based on the record evidence in this case.

KCPL Residential rates are further broken down seasonally into summer and winter rates. Summer rates (a flat rate energy charge) apply to electricity used from May 16 through September 15 (four months). Winter rates (declining block energy charges) apply to electricity used from September 16 through May 15 (eight months).

¹³ Report and Order, Case No. ER-2007-0291, issued December 6, 2007, pages 77, 78, and 82. The Commission also froze Residential General Use and Space Heat - 2 Meters in this case.

The current summer energy charge is the same for the General Use and Space Heat customer sub-classes, and this summer energy charge is higher than current winter energy charges.¹⁴ In the winter, both General Use and Space Heat - One Meter have declining block energy charges, meaning that customers pay less for electricity in the winter as they use more of it. General Use customers have higher energy charges than customers who sign up for KCPL's specially-discounted Space Heat – One Meter rate, a rate that applies to all usage, not just space heat usage. Average winter energy prices are lower for Space Heat - One Meter than for General Use.¹⁵ The non-heat portion of a customer's usage on frozen Space Heat - 2 Meters is priced the same as General Use in the winter; however, the space heat usage on the separate meter for the Space Heat - 2 Meters schedule is priced significantly below General Use.

The winter price advantage of Space Heat has increased over time through a series of KCPL rate increases that generally resulted from stipulations and across-the-board increases, or equal percentage increases for all rate elements.¹⁶ By once again proposing to increase all rate elements by an equal percentage across the board, KCPL proposes to further enlarge this Space Heat winter price discount.¹⁷

While KCPL alleges, without explanation or reference to any record evidence, that its CCOS supports the discounted winter price for Space Heat compared to General Use, quite the

¹⁴ KCPL's current Residential rates are described in Exh. 625, Cummings Direct, page 6, lines 1-12 and shown in Schedule FJC-1.

¹⁵ Both the non-heat portion of a customer's usage on the Space Heat - One Meter rate and the space heat usage are priced significantly below the General Use rate.

¹⁶ Exh. 625, Cummings Direct, page 7, lines 8-19 and Schedule FJC-2.

¹⁷ Exh. 625, Cummings Direct, page 6, line 14 - page 7, line 3; page 7, lines 13-14; page 7, lines 18-19; and Schedule FJC-2.

opposite is, in fact, the case.¹⁸ According to KCPL's own CCOS, discussed more fully below, Space Heat winter rates would have to increase relative to General Use winter rates in order to equalize the winter rates of return among the various Residential rate schedules.¹⁹ These rates are not cost-based and KCPL's own CCOS shows this. KCPL has simply provided no evidence to support the current discounted Space Heat winter rate, much less justify an increase in that discount.

KCPL's Residential Space Heat discounts are unique among Missouri electric utilities regulated by this Commission. Neither of the other investor-owned Missouri electric utilities has separate all-electric or space heat rates.²⁰ The standard Residential services of Ameren Missouri and The Empire District Electric Company have declining block winter energy charges, but neither has a special, discounted space heat rate. KCPL already has a strong potential to add winter load through its current General Use schedule with its more-sharply declining winter energy prices than Ameren Missouri's or Empire District's rates, without the need for separate, significantly lower-priced Space Heat schedules.²¹ KCPL also has a greater summer/winter differential than do Ameren Missouri or Empire District.

C. RESIDENTIAL REVENUE-NEUTRAL RATE ADJUSTMENTS

Equity considerations suggest that each customer rate class should pay the cost to serve the class.²² Achieving full equity results in identical rates of return for each class, which is based on the revenue produced from rates and the cost to serve each class. If the equity objective is not

¹⁸ Exh. 625, Cummings Direct, page 8, line 3 - page 9, line 14 and footnote 8.

¹⁹ Exh. 625, Cummings Direct, page 12, line 14 - page 13, line 12 and Schedule FJC-3.

²⁰ Exh. 625, Cummings Direct, page 13, lines 16-19 and Schedule FJC-4.

²¹ Exh. 625, Cummings Direct, page 14, lines 1-17.

²² Different rate customer classes should be broadly interpreted to include different rate schedules.

met, a portion of the cost to serve one or more classes is necessarily borne by other class(es).²³ That is, the cost to serve the customer class (or sub-class) with a lower-than-system-average rate of return is being subsidized by the customer class (or sub-class) with a higher-than-system-average rate of return.

The following example illustrates the inequities in revenue collection among a hypothetical Residential rate schedules with differing rates of return. Suppose a utility serves its Residential customer class through two rate schedules, A and B. The first row in the table below shows Current Revenue for each rate schedule and for the Residential class as a whole. The second row provides Operating Expenses for each schedule determined in a class cost of service (CCOS) study. The third row, Net Operating Income, is the difference between Current Revenue and Operating Expenses. This row is the dollar amount available to provide a return on investment, or Rate Base. Each rate schedule's Rate Base, shown in the fourth line, is developed in the CCOS. The Rate of Return in line 5 is Net Operating Income divided by Rate Base.

<u>Line</u>		<u>Rate Schedule</u>		<u>Residential</u>
		<u>A</u>	<u>B</u>	<u>Total</u>
1	Current Revenue	10,000	5,000	15,000
2	Operating Expenses	7,000	4,000	11,000
3	Net Operating Income	3,000	1,000	4,000
4	Rate Base	50,000	30,000	80,000
5	Rate of Return	6.00%	3.33%	5.00%
6	Cost of Service to Meet <u>Current Class Rate of Return</u>			
7	Operating Expenses	7,000	4,000	11,000
8	Return at 5%	2,500	1,500	4,000
9	Total Current Cost of Service	9,500	5,500	15,000
10	Current Revenue Less Total Current Cost of Service (at 5%)	500	(500)	-

²³ Exh. 625, Cummings Direct, page 9, line 16 - page 10, line 3.

In this example, with current Residential rates and resulting Current Revenue, Rate Schedule A earns a 6.00% return and Rate Schedule B earns a 3.33% return, while the Residential class as a whole provides a 5.00% return at current rates. If each rate schedule were to provide the class total 5.00% return, Rate Schedule A rates would have to be reduced to produce \$500 less revenue and Rate Schedule B rates must be increased to collect \$500 more revenue, as shown on line 10. Alternatively stated, at current rates, customers on Rate Schedule A provide revenue that covers not only their own cost of service of \$9,500, but also subsidizes \$500 of the cost to serve Rate Schedule B customers' \$5,500.

This same inequity exists in KCPL's current Residential rate schedules. KCPL's own CCOS results show that winter revenue produced from current Residential rates - and the resulting winter rates of return for Space Heat relative to General Use - do not support the discounted winter Space Heat rates.²⁴ Specifically, at current rates, the KCPL CCOS shows the following winter rates of return:

General Use	5.174%
Space Heat - One Meter	2.922%
Space Heat - 2 Meters	2.284%
Residential Class Total	4.498% ²⁵

Furthermore, at current rates, this winter Residential rate of return of 4.498% is less than the summer Residential rate of return of 6.509%.²⁶

As illustrated in KCPL's own CCOS, General Use customers – the majority of KCPL's customers- are subsidizing a portion of the cost to serve Space Heat customers in the winter. This inequity is inconsistent with the Commission's obligation to establish rates that are not

²⁴ Exh. 625, Cummings Direct, page 9, lines 10-14; page 10, line 5 - page 11, line 9; Exh. 627, Cummings Surrebuttal, page 5, line 13 - page 6, line 8.

²⁵ Exh. 625, Cummings Direct, Schedule FJC-3, line 11.

²⁶ Exh. 625, Cummings Direct, Schedule FJC-3, line 4.

unduly discriminatory. “Under Section 393.130.3, [public utilities] are forbidden from granting undue preference or advantage to any ratepayer, just as they may not unduly or unreasonably prejudice or disadvantage any ratepayer in the provision of services.” *State ex rel City of Joplin v. PSC*, 186 S.W.3d 290, 296 (Mo.App.W.D. 2005).

In addition, KCPL’s CCOS shows that for the Residential class as a whole, current rates and the resulting revenue produce a lower rate of return in the winter than in the summer. These inequities within the Residential schedules both seasonally (i.e., between the summer and winter rates) and in the winter (between Space Heat and General Use rates) have persisted since at least KCPL’s last rate case, when KCPL’s own CCOS showed similar inequities.²⁷ Furthermore, KCPL’s proposal to apply any revenue increase awarded by the Commission in this case across-the-board to the various Residential schedules in this case not only ignores KCPL’s own CCOS, but also exacerbates the current inequities shown above.²⁸

For example, application of a ten percent increase for illustrative purposes to rates in equal percentages causes the rate of return difference between General Use and Space Heat - One Meter to increase from 2.252% to 2.551%, thus, enlarging the discount provided to the Space Heat customers.²⁹ Given KCPL’s position in this case, this disparity will continue to grow with successive rate cases until it is no longer sustainable and until the customer impact will only be greater. The Commission should act now to freeze or eliminate these discounted Space Heat rates.

Based on KCPL’s CCOS, MGE recommends a revenue shift and resulting energy charge adjustments to eliminate the seasonal inequities in KCPL’s current Residential rates and resulting

²⁷ Exh. 625, Cummings Direct, page 11, line 11 - page 12, line 12.

²⁸ Exh. 625, Cummings Direct, page 17, line 16 - page 17, line 2 and Schedule FJC-7.

²⁹ *Id.*

revenue collection and to correct the current relative under pricing of the discounted Space Heat services in the winter.³⁰ Residential revenue in total is unchanged with these rate adjustments, but additional revenue is collected in the winter that is offset by reduced revenue collected in the summer. While rates on all schedules are increased in the winter, Space Heat rates are increased more than General Use rates.

No party has questioned the accuracy of MGE’s recommended revenue shift.³¹ KCPL’s argument that discounted winter Space Heat prices are justified based on the Staff CCOS and the Department of Energy (“DOE”) CCOS is misplaced.³² The KCPL argument is based solely on annual CCOS results for the Residential rate schedules, not seasonal results from its own study. The Staff’s annual CCOS results mask both the seasonal inequities within the Residential class and the inequities among Residential customers taking service on different rate schedules in the winter.³³ The DOE’s CCOS does not provide seasonal results by Residential rate schedule.³⁴

³⁰ The required Residential shift requires a \$6,325,326 increase in winter revenue offset by a corresponding decrease of \$6,325,326 in summer revenue. The increased winter revenue must be assigned to the Residential rates schedules as follows in order to equalize the winter rates of return on all schedules:

<u>General Use</u>	<u>Space Heat-One Meter</u>	<u>Space Heat-2Meters</u>	<u>Time of Day</u>	<u>Other Use</u>
\$ 1,254,583	\$ 3,549,712	\$ 1,518,75	\$ 2,752	\$ 4

Exh. 625, Cummings Direct, page 3, lines 9-16; page 17, lines 5-14; page 18, lines 4-14; page 23, lines 3-7; page 24, lines 14-18; Schedule FJC-3; and Schedule FJC-8, lines 1 and 2; and Exh. 627, Cummings Surrebuttal, page 7, lines 1-14 and page 8, lines 1-9.

³¹ KCPL mischaracterized MGE’s revenue shift in indicating that it solely equalizes seasonal rates of return for the Residential class. Exh. 627, Cummings Surrebuttal, page 2, line 19 - page 3, line 11.

³² Exh. 43-NP, Rush Surrebuttal, page 6, lines 7-9 and page 7, lines 9-12 with table that follows.

³³ Staff witness Schepelerle’s testimony illustrates why these annual CCOS results mask the inequities that MGE’s recommendation addresses. He indicated that the Staff CCOS annual results referenced by KCPL (based on an assumed overall revenue increase of \$33.7 million – an increase of 4.86%) requires Space Heat - One Meter annual revenue to increase by 14.80%, while winter revenue must increase by 29.53%; and, Space Heat - 2 Meters annual revenue must increase by 24.66%, while winter revenue must increase by 35.55%. Transcript, Volume 19, page 1068, line 10 - page 1069, line 7 and Exh. No. 631.

³⁴ Exh. 501, Goins Direct, Schedules DWG-1 through DWG-4.

Neither the Staff CCOS nor the DOE CCOS can be used to develop the revenue shifts required to cure the inequities in the collection of current Residential revenue.³⁵ This is because, first, the Staff CCOS is based on its then-recommended revenue requirement, not current revenues and, second, the study is structured in a manner that does not identify operating expenses and rate base by season and rate schedules. This expense and rate base information is required to develop the appropriate revenue-neutral shift. Similarly, the DOE CCOS does not provide results by season for each Residential rate schedule.³⁶

In contrast to the Staff and DOE CCOS, the KCPL CCOS results in this case provide an appropriate basis for correcting Residential revenue collection inequities. For reference, the same CCOS approach by KCPL was adopted by the Kansas Corporation Commission (KCC) in KCPL's 2010 rate case.³⁷ Based on the KCPL CCOS results, the KCC designed Residential rates based on a shift in revenue collection away from General Use customers toward Space Heat customers.

It is very important to note that Staff recognizes that KCPL Residential Space Heat services are underpriced and, therefore, are being subsidized by General Use rates.³⁸ That conclusion has caused Staff to recommend that the first block of the Residential Space Heat rates be increased by 5%.³⁹ However, Staff's recommended revenue shift does not go far enough to

³⁵ In addition to KCPL, Staff, and DOE, the Missouri Industrial Energy Users' Association and Midwest Energy Consumer's Group ("Industrials") filed a CCOS. The Industrials CCOS results are provided only for the Residential class as a whole on an annual basis. Residential results by season and rate schedule are not available in the Industrials CCOS.

³⁶ Exh. 501, Goins Direct, Schedules DWG-1 through DWG-4.

³⁷ Exh 627, Cummings Surrebuttal, page 14, lines 5-8 and footnote 37; Exh. 39, Normand Rebuttal, page 11, lines 8-12.

³⁸ Exh. 212, Scheperle Direct, page 3, line 1-15.

³⁹ *Id.*

address the current inequities in the collection of winter revenue from Residential customers served on different schedules and does not correct the seasonal inequity in the collection of current Residential revenue.⁴⁰ As can be seen from MGE’s testimony, a \$4.5 M increase to the Space Heat – One Meter and Space Heat – Two Meters rates is required to eliminate the inequities resulting from the current discount. However, the Staff’s proposal would only increase those rates by a total of \$1.1 M.⁴¹ If cost-based rates are appropriate, as Staff indicates, the proper approach is to eliminate or freeze the availability of these rates in a way that removes all of the existing inequities as recommended by MGE. The Staff proposal, while directionally correct, is simply insufficient.

Moreover, it should also be noted that under Staff’s proposal, a portion of that shift would immediately be negated if any revenue increase was spread across rates on an equal percentage basis. The following table illustrates how even a 5% “across-the-board” increase will diminish the impact of Staff’s shift and begin to again increase the discount for Space Heat rates:

	Current - Before <u>Staff 5% Shift</u>	<u>After Staff 5% Shift</u>	Assuming a 5% <u>Increase</u>
General Use - first block winter rate	\$ 0.09914	\$ 0.09914	\$ 0.10410
Space Heat-One Meter first block winter rate	\$ 0.07382	\$ 0.07751	\$ 0.08139
Difference between first block winter rates	\$ 0.02532	\$ 0.02163	\$ 0.02271

MGE’s recommended current Residential rate adjustment is consistent with sound ratemaking concepts, is fully supported by the record evidence, and should be adopted by the Commission in this case.

⁴⁰ Exh. 626, Cummings Rebuttal, page 3, line 1- page 4, line 8 and Rebuttal Schedule FJC-1.

⁴¹ Exh. 626, Cummings Rebuttal, Rebuttal Schedule FJC-1.

***D. PRIMARY RECOMMENDATION: ELIMINATE AVAILABILITY OF
SPECIALLY-PRICED SPACE HEAT RATES***

In the 1970s, rising natural gas demand and declining production along with supply availability concerns provided public policy support for favoring the use of electricity over natural gas, including offering special space heat rates to encourage the installation of electric space heating equipment. Energy market conditions today no longer provide this public policy basis for preferential treatment of electricity for space heating purposes. Instead, today's energy-related public policy focuses on promoting end-user energy conservation, limiting environmental impacts related to energy production and delivery, and encouraging efficiency in energy consumption.⁴² Consistent with today's energy policy considerations, a number of electric utilities nationally have discontinued or closed the availability of specially-priced Residential Space Heat services, including utilities in Arkansas, California, Connecticut, Massachusetts, Nebraska, New Jersey, North Carolina, Ohio, Pennsylvania, and Wisconsin.⁴³ No other investor-owned electric utility in Missouri makes specially-discounted Residential Space Heat rates available.⁴⁴

Policy considerations dictating elimination of KCPL's discounted Residential Space Heat services include:

1. The current KCPL General Use winter declining block rate structure encourages winter load additions. By offering an even lower-priced Space Heat service, customers are not incented to conserve electricity used for both heating and non-heating purposes.⁴⁵

⁴² Exh. 625, Cummings Direct, page 19, lines 11-23.

⁴³ Exh. 627, Cummings Surrebuttal, page 8, line 14 - page 10, line 2.

⁴⁴ Exh. 625, Cummings Direct, page 13, lines 16-19.

⁴⁵ Exh. 625, Cummings Direct, page 20, lines 7-10.

2. The additional electricity production and delivery caused by discounted Space Heat services results in adverse environmental impacts, another point unrebutted by KCPL in testimony.⁴⁶
3. Encouraging the use of electricity through discounted Space Heat services ignores the fact that natural gas is more efficient than electricity for space heating purposes, which was also unrebutted by KCPL in testimony.⁴⁷
4. Space heating with natural gas is less expensive than heating with electricity from KCPL, another point unrebutted by KCPL in testimony.⁴⁸
5. KCPL's Residential General Use schedule has more-sharply declining winter energy prices than Ameren Missouri's and Empire District's Residential rates. Through these price signals, KCPL's has a stronger potential to encourage winter usage through its General Use schedule than does Ameren Missouri and Empire District through their Residential rates - rates that do not offer discounts for Space Heating. KCPL's discounted Space Heat services are not needed for winter-load building.⁴⁹
6. Customers choose electricity rather than natural gas for space heating simply because they receive winter price breaks not only for space heating purposes but also for lighting their homes, operating their televisions and refrigerators, and using other electric appliances. Aside from promoting false price signals, these rates are not sustainable in the long term.⁵⁰
7. Elimination of Space Heating services is consistent with factors that KCPL articulates as being important in assessing rate design proposals.⁵¹

⁴⁶ Exh. 625, Cummings Direct, page 19, line 23 - page 20, line 2; page 20, lines 10-13; Exh. 627, Cummings Surrebuttal, page 10, line 14 - page 11, line 4 and Surrebuttal Schedule FJC-1.

⁴⁷ Based on U.S. Department of Energy efficiency standards for residential furnaces and heat pumps, the consumption efficiency, i.e., combined appliance and fuel cycle efficiency, for a natural gas furnace is 74-82 percent while the consumption efficiency is 50 percent for an electric heat pump and 23 percent for an electric furnace. Exh. 625, Cummings Direct, page 20, line 15 - page 21, line 2. Also, see Exh. 627, Cummings Surrebuttal, page 10, line 6 - page 12, line 13 and Surrebuttal Schedule FJC-1.

⁴⁸ Exh. 625, Cummings Direct, page 14, line 19 - page 15, line 9 and Schedule FJC-5.

⁴⁹ Exh. 625, Cummings Direct, page 14, lines 1-17.

⁵⁰ Exh. 625, Cummings Direct, page 15, line 11 - page 16, line 8. There would typically be many days in the long, eight-month period when KCPL's winter rates are in effect in which Space Heat customers do not operate their space heating equipment and yet they pay less for electricity than electric customers who choose an alternative energy source for space heating. General Use customers, 79% of the Residential class, are being treated unfairly due to the availability of the specially-priced Space Heat service.

⁵¹ Exh. 42 NP, Rush Rebuttal, page 11, line 1 - page 12, line 14; and Exh. 627, Cummings Surrebuttal, page 15, line 3 - page 22, line 14.

Sound ratemaking and policy considerations support the elimination of KCPL's discounted winter Space Heat services.⁵² The only question is whether these specially-priced services should be eliminated in this case or a subsequent rate case.⁵³ MGE recommends that these services be eliminated in this case. The resulting rates are shown on the table below on page 20.

E. ALTERNATE RECOMMENDATION: FREEZE AVAILABILITY OF SPECIALLY-PRICED SPACE HEAT RATES

However, if the Commission prefers a more gradual approach, MGE recommends in the alternative that the Commission indicate its intent to eliminate these services in a subsequent rate case, adopt the recommended Residential revenue neutral shift in this case, freeze the availability of these specially-priced services, and require tariff language to ensure the effectiveness of freezing the schedules and to simplify their future elimination.⁵⁴

⁵² However, while ratemaking and policy considerations support MGE's recommendation to eliminate the Space Heat schedules, MGE's recommendation does not preclude Residential customers from choosing electricity for space heat purposes. Exh. 627, Cummings Surrebuttal, page 12, line 15 - page 13, line 7.

⁵³ Exh. 625, Cummings Direct, page 4, lines 4-10.

⁵⁴ Exh. 625, Cummings Direct, page 4, line 12 - page 5, line 3 and page 21, line 4 - page 22, line 21. The required tariff language should clearly indicate that the frozen service is available to existing customers at existing premises on the date rates in this case become effective. A customer on the schedule cannot receive the service upon moving to a different location and the customer's former premise is not eligible to provide the service to a new customer

F. RESIDENTIAL RATE DESIGN

MGE provides rate design recommendations based on the elimination of Space Heat services and on the alternative of freezing the availability of these services.⁵⁵ If Space Heat services are eliminated, KCPL's current Space Heat winter block rate structure along with MGE's current revenue shift should be used to develop a consolidated General Use rate on which both current General Use and Space Heat customers would take service after this case. If Space Heat services are frozen, current Space Heat customer rates should be adjusted to reflect MGE's revenue shift.

The following table show current rates (from Exh. 625, Schedule FJC-1) and the rates associated with MGE's recommendations (from Exh. 625, Schedule FJC-8) for the alternatives of eliminating Space Heat and freezing Space Heat on a revenue-neutral basis. This table compares current rates with rates upon the elimination of Space Heat and with the alternative of

⁵⁵ Exh. 625, Cummings Direct, page 23, line 3 - page 24, line 18 and Schedule FJC-8. KCP&L incorrectly describes MGE's recommendations as "a series of scenarios to revise Residential rate blocking" (Exh. 627, Cummings Surrebuttal, page 3, line 16 - page 4, line 9) based on "modifications to the Company's billing determinates [sic]" (Cummings Surrebuttal, page 5, lines 4-8 and footnote 11).

freezing Space Heat:

	<u>Current</u>	<u>Space Heat Elimination</u>	<u>Space Heat Retained/Frozen</u>
Space Heat - One Meter			
Service Charge	9.00	9.00	9.00
Energy Charge			
Summer			
All kWh	0.11028	0.10416	0.10416
Winter			
First 1000 kWh	0.07382	0.08732	0.08403
Over 1000 kWh	0.04872	0.06222	0.05893
Space Heat - 2 Meters			
Service Charge	11.05	11.05	11.05
Energy Charge			
Summer			
All kWh	0.11028	0.10416	0.10416
Winter			
First 600 kWh	0.09914	0.10029	0.10029
Next 400 kWh	0.05945	0.06060	0.06060
Over 1000 kWh	0.04968	0.05083	0.05083
Separate Meter-All kWh	0.04747	0.06910	0.06910
General Use			
Service Charge	9.00	9.00	9.00
Energy Charge			
Summer			
All kWh	0.11028	0.10416	0.10416
Winter			
First 600 kWh	0.09914	0.08732	0.10029
Next 400 kWh	0.05945	0.08732	0.06060
Over 1000 kWh	0.04968	0.06222	0.05083

The rates in this table result from MGE’s revenue neutral rate adjustments before any Residential revenue increase approved by the Commission is implemented. MGE has provided recommendations regarding how these rates should be adjusted to incorporate any Residential increase approved by the Commission.⁵⁶ MGE’s recommendation ensures that the seasonal equity resulting from MGE’s recommended current Residential rate adjustments continues after implementation of any approved Residential revenue increase. By contrast, KCPL’s across-the-

⁵⁶ Exh. 625, Cummings Direct, page 5, lines 5-11; page 26, line 3 - page 27, line 3; and Schedule FJC-9.

board increase to all Residential rate schedules and rate elements would introduce additional seasonal inequities in the collection of Residential revenue.⁵⁷

In order to effectuate a less comprehensive Residential revenue shift than recommended by MGE, Staff recommends a rate design change that increases the winter price differential between the current Space Heat rate blocks.⁵⁸ Staff provides no support for continuing the historical pattern of an increasingly-pronounced winter declining block rate structure and the resulting additional encouragement of winter load additions.⁵⁹ By contrast, MGE recommends that the revenue shift be assigned to rate blocks to maintain the current rate block differentials, consistent with the policy considerations discussed above.

G. RESIDENTIAL BILL IMPACTS

Mindful that rate shifts should not take place in a vacuum, MGE examined and provided the customer bill impacts that would result from its recommendations.⁶⁰

MGE's recommendations result in annual bill reductions for current General Use customers prior to any overall increase in rates granted by the Commission in this case.⁶¹ A typical General Use annual bill will decrease by 5.6%, if Space Heat is eliminated, and by 1.9%, if Space Heat is frozen. These customers - who have been footing a part of the cost to serve specially-priced Space Heat customers - comprise 79% of KCPL's Residential class. On the

⁵⁷ Exh. 625, Cummings Direct, page 17, line 16 - page 18, line 2 and Schedule FJC-7; Exh. 43 NP, Rush Surrebuttal, page 12, lines 17-20.

⁵⁸ Exh. 212, Scheperle Direct, page 3, lines 11-15.

⁵⁹ Exh. 626, Cummings Rebuttal, page 4, line 12 - page 5, line 2.

⁶⁰ Exh. 627, Cummings Surrebuttal, page 21, line 7 - page 22, line 14 and Surrebuttal Schedule FJC-2.

⁶¹ Exh. 627, Cummings Surrebuttal, page 22, lines 12-14 and Surrebuttal Schedule FJC-2, column (b). In addition, Footnote 2 of this Schedule shows the General Use customer bill impacts if KCP&L received a \$35.2 million Residential revenue increase, or one-third of its proposed increase. By comparison, KCP&L's recommendation would increase General Use typical annual bills by 5% with this revenue increase.

other side, if Space Heat is eliminated, the Space Heat - One Meter typical annual bill will increase by 6.1%. If Space Heat is frozen, the typical bill will increase by 4.0%. This information is summarized in the following table:

<u>Customer Type</u>	<u>Percentage of KCPL Customers</u>	<u>Bill Increase/(Decrease) If Space Heat – One Meter Rate Eliminated</u>	<u>Bill Increase/(Decrease) If Space Heat – One Meter Rate Frozen</u>
General Use	79%	(5.6%)	(1.9%)
Space Heat – One Meter	16%	6.1%	4.0%

For comparison purposes, KCPL’s recent experience in Kansas has value. The annual Space Heat bill impacts resulting from the KCC’s Order in KCPL’s 2010 rate case – 18.4% – were substantially larger than those resulting from MGE’s recommendations in this case – 6.1%, if the discounted rate is eliminated and 4.0%, if the discounted rate is frozen.⁶²

Moreover, it is important to recognize that the bill impacts provided by MGE are the only accurate bill impact information available to the Commission. During cross examination, Mr. Rush admitted to inaccuracies contained in his bill impact calculations and accordingly his calculations cannot be relied upon.⁶³ Staff witness Scheperle contends that MGE’s recommendation to eliminate Space Heat would result in rate shock.⁶³ However, Mr. Scheperle did not present any calculation of the typical Space Heat bill impact. Importantly, Mr. Scheperle did not analyze – or in any way rebut – potential rate impacts based on MGE’s proposal.⁶⁴ Mr. Scheperle simply calculated differences between bills based on *current* General Use rates and

⁶² Exh. 627, Cummings Surrebuttal, page 22, lines 1-7 and Surrebuttal Schedule FJC-2. Additional discussion of the KCPL-Kansas 2010 rate case is provided in Exh. 625, Cummings Direct, page 27, line 7 - page 29, line 18 and Exh. 627, Cummings Surrebuttal, page 13, line 11 – page 14, line 12.

⁶³ Exh. 255, Scheperle Surrebuttal, page 9, lines 3-4.

⁶⁴ Transcript, Volume 19, page 1059, line 23 - page 1060, line 12.

bills based on *current* Space Heat rates.⁶⁵ He did not analyze rate impact based on MGE's proposal, which, by first adjusting seasonal disparities and eliminating subsidization, actually results in a decrease in rates for the majority of KCPL's customers who have been overpaying for their electric service. Finally, neither KCPL nor Staff provided bill impact calculations associated with MGE's alternative recommendation to freeze the availability of Space Heat services.

IV. SUMMARY

KCPL's current Residential rates inappropriately promote and incentivize the use of electricity over other resources for space heating. KCPL's rates price electricity under the Residential Space Heat rate schedules below cost (at a discount) and require KCPL's other Residential customers to pay a share of the cost to serve these Space Heat customers.

Not correcting this situation and requiring an across the board equal percentage rate increase would cause Residential Space Heat rates to continue to move further away from the actual cost to serve these customers, would send misleading price signals to customers, and would represent a decision to inefficiently favor electricity over other space heating energy sources.

MGE has provided two recommendations in order to address this issue:

(1) MGE's first recommendation is that the Commission adjust current KCPL Residential rates on a revenue-neutral basis to remove the existing seasonal inequities in the collection of revenue in relation to cost and the inequities in the collection of winter revenue among customers taking service on different rate schedules. This recommendation results in *reduced* bills for Residential General Use customers (which represent 79% of KCPL's residential customer base) and increased bills for KCPL's Residential Space Heat customers through the

⁶⁵ Transcript, Volume. 19, page 1058, line 18 – page 1059, line 2.

elimination of this subsidy. Staff also recognizes that KCPL Residential Space Heat services are underpriced, but its Staff's revenue-neutral adjustment recommendation only partially corrects the inequities in the collection of current Residential revenue; and,

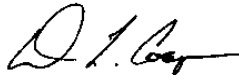
(2) After the removal of these inequities on a revenue-neutral basis, MGE recommends that the Residential Space Heat rates be eliminated. In the alternative, MGE recommends that the Commission freeze the availability of Space Heat rates using tariff language to simplify the future elimination of these rates. Moreover, MGE recommends that any Residential rate increase that may be awarded in this case should be assigned to Residential rates in a way that preserves the movement to cost-based rates.

It is important for the Commission to consider the impact of not acting. This is especially true given KCPL's recommendation to continue the historical pattern of moving Space Heat rates further and further away from the cost to serve these customers. While there are impacts associated with bringing the Space Heat rates in line with cost now, those impacts are less than they will be in the future, if nothing is done. "Kicking the can down the road" will only result in a larger and more painful customer impact in the future.

WHEREFORE, MGE respectfully requests that the Commission consider this Initial

Brief and, thereafter, issue such orders as it should find to be just and reasonable.

Respectfully submitted,



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CERTIFICATE OF SERVICE

I do hereby certify that a true and correct copy of the foregoing document has been sent by electronic mail this 28th day of November, 2012, to:

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