proposed amendment, so it is not reprinted here. This proposed amendment becomes effective thirty (30) days after publication in the *Code of State Regulations*.

SUMMARY OF COMMENTS: No comments were received.

Title 3—DEPARTMENT OF CONSERVATION
Division 10—Conservation Commission
Chapter 12—Wildlife Code: Special Regulations for Areas Owned by Other Entities

ORDER OF RULEMAKING

By the authority vested in the Conservation Commission under sections 40 and 45 of Art. IV, Mo. Const., the commission amends a rule as follows:

3 CSR 10-12.140 Fishing, Daily and Possession Limits **is amended.**

A notice of proposed rulemaking containing the text of the proposed amendment was published in the *Missouri Register* on May 1, 2009 (34 MoReg 841). No changes have been made in the text of the proposed amendment, so it is not reprinted here. This proposed amendment becomes effective thirty (30) days after publication in the *Code of State Regulations.*

SUMMARY OF COMMENTS: No comments were received.

Title 3—DEPARTMENT OF CONSERVATION
Division 10—Conservation Commission
Chapter 12—Wildlife Code: Special Regulations for Areas Owned by Other Entities

ORDER OF RULEMAKING

By the authority vested in the Conservation Commission under sections 40 and 45 of Art. IV, Mo. Const., the commission amends a rule as follows:

3 CSR 10-12.145 Fishing, Length Limits **is amended.**

A notice of proposed rulemaking containing the text of the proposed amendment was published in the *Missouri Register* on May 1, 2009 (34 MoReg 841–842). No changes have been made in the text of the proposed amendment, so it is not reprinted here. This proposed amendment becomes effective thirty (30) days after publication in the *Code of State Regulations.*

SUMMARY OF COMMENTS: No comments were received.

Title 4—DEPARTMENT OF ECONOMIC DEVELOPMENT
Division 240—Public Service Commission
Chapter 3—Filing and Reporting Requirements

ORDER OF RULEMAKING

By the authority vested in the Public Service Commission under sections 386.250, 386.266, and 393.140, RSMo 2000, the commission adopts a rule as follows:

4 CSR 240-3.162 is adopted.

A notice of proposed rulemaking containing the text of the proposed rule was published in the *Missouri Register* on February 3, 2009 (34 MoReg 187–196). A second notice of proposed rulemaking containing the text of the proposed rule was published in the *Missouri Register* on March 16, 2009 (34 MoReg 595–605). Relevant portions of those sections with changes are reprinted here. This proposed rule becomes effective thirty (30) days after publication in the *Code of State Regulations.*

SUMMARY OF COMMENTS: The first public comment period ended March 4, 2009, and a public hearing on the proposed rule was held March 4, 2009. The second public comment period ended April 15, 2009, and a second public hearing was held the same day. Timely written comments were received from Union Electric Company d/b/a AmerenUE, the Missouri Industrial Energy Consumers (MIEC), the Public Counsel (OPC), and the staff of the Missouri Public Service Commission. In addition, Lena Mantle and Mark Oligschlaeger on behalf of the staff, Ryan Kind on behalf of OPC, and Mark C. Birk on behalf of AmerenUE testified at the hearing on March 4, 2009, and counsel to the commenters made substantive verbal comments at the hearing. Counsel for the Missouri Industrial Energy Consumers and for AmerenUE also offered comments at the April 15 hearing. The testimony and comments both opposed and supported the adoption of the rule, and both opponents and supporters of the rule made specific recommendations for changes in the language and operation of the rule. Consumers and consumer groups opposed the rule; electric companies and the commission staff supported the rule.

COMMENT #1 (Public Interest): AmerenUE agrees with the commission's finding that these rules are necessary and with the commission's statement that, in the current economic climate, these rules are necessary. Timely recovery of investment capital will be essential to financing environmental upgrades to existing power plants and hastening compliance with government mandates designed to improve the quality of the environment for all Missourians. With the exception of AmerenUE's technical correction to the proposed rule, it finds the rule as proposed to be acceptable.

Staff believes that the presence of an Environmental Cost Recovery Mechanism (ECRM) is consistent with the public interest, because one presumes that the state legislature acts in the broad public interest. Staff takes the position that the presence of an ECRM is neutral to ratepayers. However, if used properly, it may operate to improve capital flows or certainly cash flow, which could be translated into a benefit in ratemaking terms. It is possible to track or monitor a benefit to ratepayers of an ECRM, but staff notes that it would be very difficult to do.

In response to questions, staff commented that it supported adoption of the rule although the commission already allows a surcharge for infrastructure replacement. Staff opines that those procedures are not adequate to address the issues dealt with in an ECRM, in that the infrastructure replacement rules do not apply to both increases and decreases, and deal only with capital expenditures.

MIEC notes that section 386.266, RSMo Supp. 2008, provides the authority for the commission to promulgate regulations to implement, and that are consistent with, that section. The legislature could have simply authorized utilities to implement an ECRM but instead granted the commission discretion, under specific parameters, to authorize or withhold an ECRM.

OPC believes that, as presently proposed by the commission, the rule is not consistent with the public interest.

RESPONSE: The commission remains convinced that these rules are in the public interest. Other filings made by Missouri electric utilities to this commission indicate that those utilities are in the process of spending hundreds of millions, possibly billions, of dollars to comply with new and proposed federal regulations. These regulations are a tool that can be used by the commission to help the company install new environmental upgrades while maintaining access to the capital markets to fund other necessary or desirable infrastructure investments and to do so in a manner that could ultimately lower costs to the ratepayer. Accordingly, with the exception of specific proposed changes, which are dealt with elsewhere in this order, these comments do not necessitate any change.

COMMENT #2 (Overearning): Staff believes that the rule creates a potential for a utility to earn more than its authorized rate of return. Staff does not believe that the ECRM creates any greater potential for overearning than another type of surcharge, such as a fuel adjustment clause. Absent the surcharge, the utility has to manage all of its costs and all of its revenues. To isolate a portion of operations and allow rate increases, if that portion's expenses increase, removes down-side risk. Therefore, the possibility to overearn is enhanced. However, staff notes that the inclusion of capital expenditure in an ECRM will not necessarily mean that a utility is overearning, even without any sharing mechanism, because to determine whether a utility is overearning, the commission must review all the operations, all its costs with a return on investment, taxes, and all operating expenses and compare that with revenues to determine whether operations generate an appropriate return. The commission will do this in a general rate proceeding in which an ECRM is sought. Although staff believes this review is precluded between the rate cases, staff believes that the surveillance data will significantly assist in its monitoring and reviewing process and notes that the cap of two and one-half percent (2.5%) would serve to limit any overearnings, if they exist. Staff notes that it still is able to file a complaint if it believes a company is overearning.

OPC responds that a significant short-coming of the complaint process is the statutory limitation of potential complainants. Complainants face a resource-intensive undertaking and must begin it with limited information to predict the success of its efforts. Only staff has sufficient resources to mount an earnings complaint. Workload considerations can prevent or delay a complaint and limit the investigation. The surveillance provisions of the rule may help determine when a complaint may be justified, but will not supply sufficient data and other resources necessary to successfully prosecute a complaint. Moreover, if the ECRM does lead to overearning, the utility will keep excess earnings generated between the time the overearning is discovered and the complaint is resolved. Further, there is no statutory time limit in which to decide a complaint case, so this creates an incentive to delay. In such a situation, customers bear both the risk of increasing and volatile costs and the risk of funding excess earnings without the possibility of refund.

MIEC asserts that the statute was intended to strike a balance between the interests of utilities and of consumers. MIEC agrees with both OPC and staff that the legislature did not intend to create a mechanism for utilities to overearn. However, MIEC believes the proposed rules tip the scale in favor of utilities. In MIEC's view, it is possible under the rules that an overearning utility will receive additional revenues under an ECRM, contrary to legislative intent. MIEC's proposed changes are designed to allow utilities to receive additional revenues for environmental costs only when necessary to achieve the authorized rate of return.

OPC also asserts that SB 179's creators clearly contemplated that the commission would protect consumers in its ECRM rules. While the law enhances a utility's ability to increase revenues, it does not alter fundamental "rate of return" regulation. The proposed rule allows the utility to protect and enhance its interests by deferring costs during a period of over-earning to a subsequent period. The proposed rules would allow utilities to manipulate their earnings to the detriment of the public. The utility has too much control over the timing of rate cases, filings under the rule, placing plant in service, and other matters. The proposed rules fail to safeguard consumers to the detriment of the public, without any cost of service justification.

Although AmerenUE conceded that it is possible for a utility to earn more than its authorized rate of return while an ECRM is in place, given the magnitude of the environmental investments that utilities face, along with other cost and revenue issues that are tracked closely by this commission, it is highly unlikely. AmerenUE noted that the statute's purpose is to give a utility an opportunity to earn a fair return. At any given snapshot in time, the utility may earn more or less than that. The fact that a utility at a moment in time earns over its authorized return does not mean its rates are unjust and unreasonable or that it is overearning. The statute does not attempt to prevent any circumstance where the utility at a given point could earn less or more than its authorized return. True overearning is systemic earnings so much in excess of the utility's cost of capital (which can change from the time of the rate case) from what was authorized, based on normalized conditions, that rates become unjust and unreasonable. It is not earning greater than the authorized return at a given moment.

OPC proposes that to guard against earnings in excess of the authorized rate of return, the commission should implement an "earnings test." According to OPC, any ECRM that would pass through environmental costs to ratepayers while the utility earns in excess of its authorized rate would abrogate the commission's obligations to ratepayers. The proposed rule requires the commission to find that an ECRM provides the opportunity to earn a fair rate of return whenever it decides to continue or modify an ECRM the utility has requested be discontinued. This same determination is just as necessary when the commission decides to implement an ECRM in the first place, but it is not required in the rule. Effectively, ratepayers have less ability to challenge the implementation of an ECRM than to challenge a commission decision to modify or continue an ECRM.

AmerenUE notes that staff has said that there will be a study of a company's earnings in the general rate proceeding that establishes an ECRM, but that staff is precluded from doing such a study between rate cases. AmerenUE asserts that this is the same conclusion reached by the commission in refusing to include similar earnings tests proposed by OPC and others in the fuel adjustment clause (FAC) rulemaking proceedings.

RESPONSE: Use of the ECRM must be authorized by the commission inside a rate case where the commission reviews all revenue and expenses. In the event the commission authorizes an ECRM, the commission has the ability to track all of those revenues and expenses, and to take action accordingly. Therefore, the commission finds that the proposed rules do not necessarily cause utilities to overearn, and if a utility does overearn, there are sufficient remedies available. With the exception of specific proposed changes, which are dealt with elsewhere in this order, these comments do not necessitate any change.

COMMENT #3 (Effect on Environmental Projects): AmerenUE does not believe that the presence of an ECRM will necessarily accelerate the completion of environmental projects. Environmental projects to be completed are regulatory requirements imposed on the utilities. The ECRM will allow utilities to meet those environmental requirements and still have access to necessary capital to invest in and maintain other plant assets over and above the environmental assets. The rule is designed to allow utilities to most effectively install environmental projects that are required. Without the rule, the environmental projects will be installed, but access to additional capital to perform other needed maintenance and equipment upgrades on the other plant will not exist. Other potential projects that will enhance reliability on existing generating that are not mandated will suffer.

AmerenUE notes that while the rule is not necessary to enforce environmental obligations, not having it may lead to higher costs to install environmental projects. If a utility is required to install environmental equipment, ultimately those costs will be passed on to ratepayers. Being able to recover those costs more quickly can lead to a lower overall cost for the installation of mandated equipment.

As to the timely completion of environmental projects, although staff does not believe that more will be completed, some may be completed earlier than they would have otherwise. If an ECRM is approved, it could be used as a tool by the utilities if they determine that early implementation is a benefit to both the consumers and the company. In some cases, based on available labor, steel prices, etc., it may be beneficial for environmental equipment to be added early.

OPC has no reason to believe that the rule will accelerate the completion of environmental projects or that the rule will encourage more environmental projects than would otherwise occur.

RESPONSE: The commission finds that it is not necessary for the rule to operate in a way that will accelerate or enhance the completion of environmental projects. It is enough that this rule has the ability to assist companies faced with large capital spending programs and lower the cost of financing projects of this nature, which will be of benefit to the company and the ratepayers. No change will be made as a result of this comment.

COMMENT #4 (Consumer Safeguards): Staff commented at length on the process of roundtables and other group efforts that created the draft ECRM rules and how the proposed ECRM relates to other rate adjustment mechanisms. As to safeguards in the rule, staff noted that electric utilities will only be permitted to request an ECRM in a general rate proceeding where all relevant expenses, revenues, and rate base items are considered. Parties to that proceeding can propose variations or alternative methodologies/mechanisms or can oppose the ECRM. The commission may approve, modify, or reject any proposed ECRM. An ECRM cannot remain in effect for longer than four (4) years without a new general rate proceeding and modification or extension of the ECRM.

OPC believes the proposed rules do not contain adequate consumer protections and do not adequately ensure that utilities will act prudently with respect to environmental expenditures. It is reasonable to assume the legislature would only have granted the commission authority to allow an ECRM in the belief that the commission's rules would protect ratepayers. Regulatory procedures should address the needs of both ratepayers and utilities (safe and adequate service at just and reasonable rates that provide a utility an opportunity to earn a fair rate of return). The rules should apply incentives to the utility, so it makes necessary environmental investments economically and so it operates those facilities reasonably. Timelines should be set out in the rule to ensure ratepayers are not faced with unreasonably large rate increases.

OPC opines that an ECRM shifts the risk of changes in the cost of environmental compliance from the utility to its customers and that this shift removes incentives for utilities to exercise due diligence and to develop and implement prudent environmental compliance strategies. This greatly changes the regulatory paradigm in Missouri, which has fostered low rates while maintaining reasonable returns for investors. Adequate consumer protections must be added to the proposed rules to compensate for the shifting risk, if the commission is to adequately perform its statutory duties. The allowance of an ECRM is not mandatory, but the proposed rules do not provide any guidance for determining whether an ECRM is appropriate. A "threshold test" of the necessity of an ECRM for the utility to earn its authorized return is needed, and should assess the likelihood the ECRM would cause it to overearn. The utility must be required to submit adequate financial data, accessible to all parties in the rate case, as part of its application.

MIEC agrees that it is crucial that consumer protections be included in the rule, rather than being left to rate cases. Key principles should be included in the rules, because industrial consumers must be allowed to plan for their impact. Providing protections in the rules ensures predictability for consumers and utilities alike and leads to fair application of the rules.

MIEC asserts that although section 386.266, RSMo, does authorize the commission to grant ECRMs, the statute is replete with consumer protections, such as the prudence requirement, the two and one-half percent (2.5%) annual cap, the ECRM creation rate case requirement, the "fair return" finding, the annual true-up, the no longer than four (4)-year rate case cycle, and regular prudence reviews. Failure to adhere to these consumer protections could render such an ECRM unlawful.

AmerenUE and staff are of the opinion that the consumer protections contained in SB 179 are already in the proposed rules.

RESPONSE: The commission finds that the necessary consumer protections, including the several consumer protections reflected in section 386.266, RSMo, are already contained in the rule and are sufficient. No change will be made as a result of this comment.

COMMENT #5 (Sharing Mechanisms): OPC advocates for a process to align the interests of ratepayers and shareholders. OPC would change language to allow approval of an ECRM that allows recovery of "some or all" of the costs, to provide an incentive mechanism in which the utility could only collect, ninety or ninety-five percent (90 or 95%) of the change in environmental costs. In addition, OPC would include a new section that specifically aligns the interests of ratepayers and shareholders, similar to performance-based language in the fuel adjustment clause rules. OPC remains skeptical that an ECRM could ever benefit ratepayers. For there to be a benefit, positive aspects would need to overcome the large detriment created by a flow-through mechanism for cost recoveries. The proposed rule, without the additional consumer protections OPC proposes, would be detrimental to ratepayers.

OPC believes that a financial incentive (gains or losses) is a critical consumer protection. To pass through one hundred percent (100%) of the cost significantly diminishes any incentive to prudently manage the annual cost of environmental compliance and to minimize long-run costs. Regulators cannot review transactions in real time, as the utility does. The utility should have to justify recovery of environmental compliance costs in a prudence review subsequently, using information gleaned during the recovery period. The electric industry is highly complex. A "fix" in one area can cascade through the rest of the system. A regulatory model that does not recognize this fact is inferior.

Staff counters that section 386.266, RSMo, allows incentives for rate adjustment mechanism, but there is no similar statutory provision for incentives for ECRMs. Section 386.266, RSMo, restricts the annual amount of revenue collected by an ECRM to not more than two and one-half percent (2.5%) of the revenues of the electric utility but allows the electric utility to defer costs not recovered as a result of this restriction. The language in the rule mirrors the language in the statute.

RESPONSE: The commission finds that staff is correct, in that subsection 1 of section 386.266, RSMo, which deals with rate adjustment mechanisms for fuel and purchased power costs, contains language permitting incentive plans, but subsection 2, pertaining to environmental cost recovery, does not. Subsection 8, cited by OPC in its comments, does not provide authority for incentive mechanisms; rather it states in part, "This subsection shall not be construed to authorize or prohibit any incentive- or performance-based plan." No change will be made as a result of this comment.

COMMENT #6 (Eligible Costs): Staff envisions that both capital expenditures and associated items that are normally expensed would be recoverable through an ECRM, the larger portion of which would be the capital expenditures. As to truly one (1)-time expenses, if the expense qualified for the adjustment, it would be put in then come out in subsequent true-up periods.

Staff has not compiled a list of items to be included or not included in an ECRM and does not recommend that the rule further define "federal, state, or local environmental law, regulation, or rule." The commission should determine in the proceeding in which an ECRM is established or modified exactly what costs are prudently incurred to comply with a "federal, state, or local environmental law, regulation, or rule" and should be recovered in an ECRM. This issue was discussed at length in the workshops on the rule, but the participants found it difficult to define without being either too broad or too restrictive. Staff concludes that it is best left to the discretion of the commission. For example, a utility might purchase a higher-priced coal to meet environmental requirements, but not have a fuel adjustment clause. There may be an argument that the higher-priced coal should not be in an environmental cost mechanism but would be more properly reflected in a fuel adjustment clause. It also is possible that the commission might find that a utility does not qualify for a fuel adjustment clause and then would have to address whether an increase in coal expense for compliance purposes should be included in the ECRM.

OPC comments that as the commission exercises its discretion in determining what types of costs are eligible for recovery, it should look at the volatility of the costs to be included and the extent to which the costs are directly related to compliance with environmental regulations.

RESPONSE: The commission finds that examining whether the costs are directly related to environmental compliance is inconsistent with the statutory standard set forth in the statute of "prudently incurred costs, whether capital or expense, to comply with [environmental requirements]." The commission finds the inclusion of the volatility of the costs into its consideration to be irrelevant. The ECRM is limited to two and one-half percent (2.5%) of a utility's Missouri gross jurisdictional revenues. This will serve to mitigate such volatility as may exist. Further, the commission may include a consideration of volatility, and is not precluding such a review by failing to include it here. Inclusion would require the commission to always consider volatility, even in those instances in which it is irrelevant. The commission agrees that a listing of eligible costs would be counter-productive, in that any attempt at such a list would likely be either too narrow or too broad. No change will be made as a result of this comment.

COMMENT #7 (4 CSR 240-3.162(1)(F)1. and 2.): AmerenUE notes a drafting problem with the segregation of each utility's pre-existing revenue requirement into "environmental" and "non-environmental" components so that changes in the environmental revenue requirement can be tracked through the ECRM. The proposed rules remain ambiguous.

Since depreciation and taxes associated with capital projects are expensed under standard accounting practices, the language in the proposed rules arguably suggests that depreciation and taxes fall under paragraph (1)(F)1., which in turn may lead some to argue that depreciation and taxes for all capital projects, not just major projects whose primary purpose is to comply with environmental standards, must be included in the existing "environmental revenue requirement." This would mean that depreciation and taxes associated with every environmental capital item, no matter how minor, would have to be identified, calculated, and included in the environmental revenue requirement, which would be difficult if not impossible. Given the commission's adoption of the major project/primary purpose concept, it appears that the intent is to include in the environmental revenue requirement only those capital-related costs associated with major items whose primary purpose is environmental compliance.

There are three (3) costs associated with environmental capital projects: the cost of capital (return); depreciation; and taxes. The commission need only modify the proposed rules as follows:

1. All expensed environmental costs (other than taxes and depreciation associated with capital projects) that are included in the electric utility's revenue requirement in the general rate proceeding in which the ECRM is established; and

2. The costs (i.e., the return, taxes, and depreciation) of any major capital projects whose primary purpose is to permit the electric utility to comply with any federal, state, or local environmental law, regulation, or rule. Representative examples of such capital projects to be included (as of the date of adoption of this rule) are electrostatic precipitators, fabric filters, nitrous oxide emissions control equipment, and flue gas desulfurization equipment. The costs of such capital projects shall be those identified on the electric utility's books and records as of the last day of the test year, as updated, utilized in the general rate proceeding in which the ECRM is established.

Staff supports AmerenUE's changes. No commenters opposed them or provided alternative language.

RESPONSE AND EXPLANATION OF CHANGE: The commission finds the rule as written is unclear and it will make the changes proposed by AmerenUE and supported by staff as noted in the comment and as fully set forth below.

COMMENT #8 (4 CSR 240-3.162(2)(E)): MIEC and OPC propose a similar modification to subsection (2)(E). OPC proposes the following language: A complete explanation of how the proposed ECRM is reasonably designed to provide the electric utility a sufficient opportunity to earn a fair return on equity but not in excess of a fair return on equity. MIEC proposes slightly different language: A complete explanation of how the proposed ECRM is reasonably designed to provide the electric utility a sufficient opportunity to earn a fair return on equity, but not by use of the ECRM in excess of a fair rate of return on equity.

AmerenUE responds that this additional language is not consistent with SB 179, for all the reasons set forth above in comment #2. The addition of such a requirement would be impracticable and essentially disable the use of the mechanism. The enabling statute does not contain such a requirement, rather it requires only that the mechanism needs to be reasonably designed to provide a fair opportunity to earn a reasonable return. There is nothing about earnings tests between rate cases. An ECRM is established only in a rate case and reviewed in a subsequent rate case. If excess earnings are suspected between rate cases upon review of the extensive surveillance and reporting, a complaint can be filed.

OPC responds that the inclusion of this language does not pertain to earnings reviews between cases. This provision pertains only to establishment of an ECRM. This language insertion really has nothing to do with periodic adjustments.

RESPONSE: The commission finds that the language change is not necessary. The language proposed by OPC and MIEC, on its face, seems to question the validity of an ECRM if the utility earns in excess of its authorized rate of return at any point in time, which is not consistent with the statute. If the language is inserted only to remind the commission of its duty to balance the interests of ratepayers and shareholders, then it is redundant. No change will be made as a result of this comment.

COMMENT #9 (4 CSR 240-3.162(2)(P)and (Q)): As discussed in comment #2 above, MIEC believes the proposed rules favor utilities. An overearning utility could receive additional revenues under an ECRM, contrary to legislative intent. OPC also asserts that the proposed rule allows a utility to protect and enhance its interests by deferring costs during a period of overearning to a subsequent period and would allow utilities to manipulate their earnings to the detriment of the public. The utility has such control over the timing of rate cases, filings under the rule, placing plant in service, and other matters that it allows the utility to "manage" its earnings. The proposed rule fails to reflect that fact and fails to safeguard consumers. Therefore, MIEC and OPC propose the inclusion of the following subsections in section (2):

(P) A five (5)-year annual history in electronic spreadsheet format of the rate base, capitalization, income statement, jurisdictional allocations and out-of-period adjustment items in a format consistent with the Surveillance Monitoring Report set out in section (6) of this regulation; and

(Q) A forecast of the annual jurisdictional revenue requirements and supporting workpapers including capital budget data. The forecast period shall be of a length to fully include four (4) years of operation of the proposed ECRM. The forecast shall quantify any rate increases necessary to preserve the rate of return requested by the utility, under each of the following alternative assumptions:

1. ECRM as proposed by the utility; and
2. No ECRM.

AmerenUE responds that the language in subsection (2)(P) essentially asks for data on a backwards-looking basis. In a rate case subsequent to the case that established the ECRM, in which the utility seeks to continue the ECRM or recover deferrals in excess of the cap, this language would enable a party to look at a revenue requirement in each year of the ECRM's duration, in addition to the test year in the rate case. This language is inconsistent with the commission's use of a normalized test year, for all the same reasons stated by AmerenUE in comments #2 and #8 above. The commission is not empowered to apply an earnings test each year to adjustments under the ECRM.

AmerenUE adds that the forecast in subsection (2)(Q) attempts to look forward over a four (4)- or five (5)-year period and impose an earnings test at the front end. Forecasts over such a period of time become less reliable as circumstances change quickly. This goes beyond the "reasonably designed to allow a fair opportunity to earn a fair return on equity." The rules cannot go beyond the statute.

Finally, AmerenUE notes that nothing in SB 179 requires the commission to reconstruct earnings or discern what earnings might be in the future. OPC proposes to require an examination of the revenue requirement in the historic test year and in any year in which there is a deferral. The language proposed by OPC and MIEC should not be adopted.

RESPONSE: The commission finds that the language change is not necessary. As noted above, an ECRM is not to be rendered invalid if the utility earns in excess of its authorized rate of return at any point in time, because that would be inconsistent with the statute. The rule already requires the submission of extensive reports and surveillance information; requiring this additional information would burden both the utilities and the staff.

COMMENT #10 (4 CSR 240-3.162(3)(E)): MIEC and OPC propose a similar modification to subsection (3)(E): OPC proposes the following language: A complete explanation of how the proposed ECRM is reasonably designed to provide the electric utility a sufficient opportunity to earn a fair return on equity but not in excess of a fair return on equity. MIEC proposes slightly different language: A complete explanation of how the proposed ECRM is reasonably designed to provide the electric utility a sufficient opportunity to earn a fair return on equity, but not by use of the ECRM in excess of a fair rate of return on equity.

This proposed change is identical to that discussed in comment #8. All the same comments apply.

RESPONSE: For the reasons discussed in comment #8, no change will be made as a result of this comment.

COMMENT #11 (4 CSR 240-3.162(3)(P)and (Q)): OPC proposes the insertion of subsection (3)(P), and both MIEC and OPC propose the insertion of subsection (3)(Q):

(P) A five (5)-year annual history in electronic spreadsheet format of the rate base, capitalization, income statement, jurisdictional allocations, and out-of-period adjustment items in a format consistent with the Surveillance Monitoring Report set out in section (6) of this report;

(Q) A forecast of the annual jurisdictional revenue requirements and supporting workpapers including capital budget data. The forecast period shall be of a length to fully include four (4) years of operation of the proposed ECRM. The forecast shall quantify any rate increases necessary to preserve the rate of return requested by the utility, under each of the following alternative assumptions:

1. ECRM as proposed by the utility;
2. No ECRM; and

This proposed change is identical to that discussed in comment #9. All the same comments apply.

RESPONSE: For the reasons discussed in comment #9, no change will be made as a result of this comment.

COMMENT #12 (4 CSR 240-3.162(4)(C)): MIEC and OPC propose a similar modification to subsection (4)(C): OPC proposes the following language: A complete explanation of how the proposed ECRM is reasonably designed to provide the electric utility a sufficient opportunity to earn a fair return on equity but not in excess of a fair return on equity. MIEC proposes slightly different language: A complete explanation of how the proposed ECRM is reasonably designed to provide the electric utility a sufficient opportunity to earn a fair return on equity, but not by use of the ECRM in excess of a fair rate of return on equity.

This proposed change is identical to that discussed in comment #8. All the same comments apply.

RESPONSE: For the reasons discussed in comment #8, no change will be made as a result of this comment.

COMMENT #13 (4 CSR 240-3.162(5) and (6)): Staff supports the language of these sections, noting that a utility using an ECRM is required to comply with monthly and quarterly reporting requirements. Care was taken in the drafting of the reporting requirements of the proposed ECRM rules to make them consistent, as much as possible, with the reporting requirements of the rate adjustment mechanism (RAM) rules. As required by SB 179, and consistent with the RAM rules, the ECRM rules require true-ups at least every twelve (12) months, prudence reviews at least every eighteen (18) months, and separate identification of the ECRM on customers' bills.

The staff supports the surveillance reporting requirements, as this will provide sufficient data for the staff to evaluate the earnings of a utility with an ECRM and determine whether it has cause to file a complaint that the utility is overearning. Staff notes that it reviews both net increases and decreases. This allows staff to consider such factors as decreases in depreciation or property tax. Netting the costs could benefit consumers.

RESPONSE: These comments do not necessitate any change.

4 CSR 240-3.162 Electric Utility Environmental Cost Recovery Mechanisms Filing and Submission Requirements

(1) As used in this rule, the following terms mean:

(F) The environmental revenue requirement shall be comprised of the following:

1. All expensed environmental costs (other than taxes and depreciation associated with capital projects) that are included in the electric utility's revenue requirement in the general rate proceeding in which the ECRM is established; and

2. The costs (i.e., the return, taxes, and depreciation) of any major capital projects whose primary purpose is to permit the electric utility to comply with any federal, state, or local environmental law, regulation, or rule. Representative examples of such capital projects to be included (as of the date of adoption of this rule) are electrostatic precipitators, fabric filters, nitrous oxide emissions control equipment, and flue gas desulfurization equipment. The costs of such capital projects shall be those identified on the electric utility's books and records as of the last day of the test year, as updated, utilized in the general rate proceeding in which the ECRM is established;

Title 4—DEPARTMENT OF ECONOMIC DEVELOPMENT
Division 240—Public Service Commission
Chapter 20—Electric Utilities

ORDER OF RULEMAKING

By the authority vested in the Public Service Commission under sections 386.250, 386.266, and 393.140, RSMo 2000, the commission adopts a rule as follows:

4 CSR 240-20.091 is adopted.

A notice of proposed rulemaking containing the text of the proposed rule was published in the *Missouri Register* on February 3, 2009 (34 MoReg 196-199). A second notice of proposed rulemaking containing the text of the proposed rule was published in the *Missouri*

Register on March 16, 2009 (34 MoReg 605–608). Relevant portions of those sections with changes are reprinted here. This proposed rule becomes effective thirty (30) days after publication in the *Code of State Regulations*.

SUMMARY OF COMMENTS: The first public comment period ended March 4, 2009, and a public hearing on the proposed rule was held March 4, 2009. The second public comment period ended April 15, 2009, and a second public hearing was held the same day. Timely written comments were received from Union Electric Company d/b/a AmerenUE, the Missouri Industrial Energy Consumers (MIEC), the Public Counsel (OPC), and the staff of the Missouri Public Service Commission. In addition, Lena Mantle and Mark Oligschlaeger on behalf of the staff, Ryan Kind on behalf of OPC, and Mark C. Birk on behalf of AmerenUE testified at the hearing on March 4, 2009, and counsel to the commenters made substantive verbal comments at the hearing. Counsel for the Missouri Industrial Energy Consumers and for AmerenUE also offered comments at the April 15 hearing. The testimony and comments both opposed and supported the adoption of the rule, and both opponents and supporters of the rule made specific recommendations for changes in the language and operation of the rule. Consumers and consumer groups opposed the rule; electric companies and the commission staff supported the rule.

COMMENT #1 (Public Interest): AmerenUE agrees with the commission's finding that these rules are necessary and with the commission's statement that, in the current economic climate, these rules are necessary. Timely recovery of investment capital will be essential to financing environmental upgrades to existing power plants and hastening compliance with government mandates designed to improve the quality of the environment for all Missourians. With the exception of AmerenUE's technical correction to the proposed rule, it finds the rule as proposed to be acceptable.

Staff believes that the presence of an Environmental Cost Recovery Mechanism (ECRM) is consistent with the public interest, because one presumes that the state legislature acts in the broad public interest. Staff takes the position that the presence of an ECRM is neutral to ratepayers. However, if used properly, it may operate to improve capital flows or certainly cash flow, which could be translated into a benefit in ratemaking terms. It is possible to track or monitor a benefit to ratepayers of an ECRM, but staff notes that it would be very difficult to do.

In response to questions, staff commented that it supported adoption of the rule although the commission already allows a surcharge for infrastructure replacement. Staff opines that those procedures are not adequate to address the issues dealt with in an ECRM, in that the infrastructure replacement rules do not apply to both increases and decreases, and deal only with capital expenditures.

MIEC notes that section 386.266, RSMo Supp. 2008, provides the authority for the commission to promulgate regulations to implement, and that are consistent with, that section. The legislature could have simply authorized utilities to implement an ECRM but instead granted the commission discretion, under specific parameters, to authorize or withhold an ECRM.

OPC believes that, as presently proposed by the commission, the rule is not consistent with the public interest.

RESPONSE: The commission remains convinced that these rules are in the public interest. Other filings made by Missouri electric utilities to this commission indicate that those utilities are in the process of spending hundreds of millions, possibly billions, of dollars to comply with new and proposed federal regulations. These regulations are a tool that can be used by the commission to help the company install new environmental upgrades while maintaining access to the capital markets to fund other necessary or desirable infrastructure investments and to do so in a manner that could ultimately lower costs to the ratepayer. Accordingly, with the exception of specific proposed changes, which are dealt with elsewhere in this order, these comments do not necessitate any change.

COMMENT #2 (Overearning): Staff believes that the rule creates a potential for a utility to earn more than its authorized rate of return. Staff does not believe that the ECRM creates any greater potential for overearning than another type of surcharge, such as a fuel adjustment clause. Absent the surcharge, the utility has to manage all of its costs and all of its revenues. To isolate a portion of operations and allow rate increases, if that portion's expenses increase, removes down-side risk. Therefore, the possibility to overearn is enhanced. However, staff notes that the inclusion of capital expenditure in an ECRM will not necessarily mean that a utility is overearning, even without any sharing mechanism, because to determine whether a utility is overearning, the commission must review all the operations, all its costs with a return on investment, taxes, and all operating expenses and compare that with revenues to determine whether operations generate an appropriate return. The commission will do this in a general rate proceeding in which an ECRM is sought. Although staff believes this review is precluded between the rate cases, Staff believes that the surveillance data will significantly assist in its monitoring and reviewing process and notes that the cap of two and one-half percent (2.5%) would serve to limit any overearnings, if they exist. Staff notes that it still is able to file a complaint if it believes a company is overearning.

OPC responds that a significant short-coming of the complaint process is the statutory limitation of potential complainants. Complainants face a resource-intensive undertaking and must begin it with limited information to predict the success of its efforts. Only staff has sufficient resources to mount an earnings complaint. Workload considerations can prevent or delay a complaint and limit the investigation. The surveillance provisions of the rule may help determine when a complaint may be justified, but will not supply sufficient data and other resources necessary to successfully prosecute a complaint. Moreover, if the ECRM does lead to overearning, the utility will keep excess earnings generated between the time the overearning is discovered and the complaint is resolved. Further, there is no statutory time limit in which to decide a complaint case, so this creates an incentive to delay. In such a situation, customers bear both the risk of increasing and volatile costs and the risk of funding excess earnings without the possibility of refund.

MIEC asserts that the statute was intended to strike a balance between the interests of utilities and of consumers. MIEC agrees with both OPC and staff that the legislature did not intend to create a mechanism for utilities to overearn. However, MIEC believes the proposed rules tip the scale in favor of utilities. In MIEC's view, it is possible under the rules that an overearning utility will receive additional revenues under an ECRM, contrary to legislative intent. MIEC's proposed changes are designed to allow utilities to receive additional revenues for environmental costs only when necessary to achieve the authorized rate of return.

OPC also asserts that SB 179's creators clearly contemplated that the commission would protect consumers in its ECRM rules. While the law enhances a utility's ability to increase revenues, it does not alter fundamental "rate of return" regulation. The proposed rule allows the utility to protect and enhance its interests by deferring costs during a period of over-earning to a subsequent period. The proposed rules would allow utilities to manipulate their earnings to the detriment of the public. The utility has too much control over the timing of rate cases, filings under the rule, placing plant in service, and other matters. The proposed rules fail to safeguard consumers to the detriment of the public, without any cost of service justification.

Although AmerenUE conceded that it is possible for a utility to earn more than its authorized rate of return while an ECRM is in place, given the magnitude of the environmental investments that utilities face, along with other cost and revenue issues that are tracked closely by this commission, it is highly unlikely. AmerenUE noted that the statute's purpose is to give a utility an opportunity to earn a fair return. At any given snapshot in time, the utility may earn more or less than that. The fact that a utility at a moment in time earns over its authorized return does not mean its rates are unjust and unreasonable or that it is overearning. The statute does not attempt to prevent any circumstance where the utility at a given point could earn less or more than its authorized return. True overearning is systemic earnings so much in excess of the utility's cost of capital (which can change from the time of the rate case) from what was authorized, based on normalized conditions, that rates become unjust and unreasonable. It is not earning greater than the authorized return at a given moment.

OPC proposes that to guard against earnings in excess of the authorized rate of return, the commission should implement an "earnings test." According to OPC, any ECRM that would pass through environmental costs to ratepayers while the utility earns in excess of its authorized rate would abrogate the commission's obligations to ratepayers. The proposed rule requires the commission to find that an ECRM provides the opportunity to earn a fair rate of return whenever it decides to continue or modify an ECRM the utility has requested be discontinued. This same determination is just as necessary when the commission decides to implement an ECRM in the first place, but it is not required in the rule. Effectively, ratepayers have less ability to challenge the implementation of an ECRM than to challenge a commission decision to modify or continue an ECRM.

AmerenUE notes that staff has said that there will be a study of a company's earnings in the general rate proceeding that establishes an ECRM, but that staff is precluded from doing such a study between rate cases. AmerenUE asserts that this is the same conclusion reached by the commission in refusing to include similar earnings tests proposed by OPC and others in the fuel adjustment clause (FAC) rulemaking proceedings.

RESPONSE: Use of the ECRM must be authorized by the commission inside a rate case where the commission reviews all revenue and expenses. In the event the commission authorizes an ECRM, the commission has the ability to track all of those revenues and expenses, and to take action accordingly. Therefore, the commission finds that the proposed rules do not necessarily cause utilities to overearn, and if a utility does overearn, there are sufficient remedies available. With the exception of specific proposed changes, which are dealt with elsewhere in this order, these comments do not necessitate any change.

COMMENT #3 (Effect on Environmental Projects): AmerenUE does not believe that the presence of an ECRM will necessarily accelerate the completion of environmental projects. Environmental projects to be completed are regulatory requirements imposed on the utilities. The ECRM will allow utilities to meet those environmental requirements and still have access to necessary capital to invest in and maintain other plant assets over and above the environmental assets. The rule is designed to allow utilities to most effectively install environmental projects that are required. Without the rule, the environmental projects will be installed, but access to additional capital to perform other needed maintenance and equipment upgrades on the other plant will not exist. Other potential projects that will enhance reliability on existing generating that are not mandated will suffer.

AmerenUE notes that while the rule is not necessary to enforce environmental obligations, not having it may lead to higher costs to install environmental projects. If a utility is required to install environmental equipment, ultimately those costs will be passed on to ratepayers. Being able to recover those costs more quickly can lead to a lower overall cost for the installation of mandated equipment.

As to the timely completion of environmental projects, although staff does not believe that more will be completed, some may be completed earlier than they would have otherwise. If an ECRM is approved, it could be used as a tool by the utilities if they determine that early implementation is a benefit to both the consumers and the company. In some cases, based on available labor, steel prices, etc., it may be beneficial for environmental equipment to be added early.

OPC has no reason to believe that the rule will accelerate the completion of environmental projects or that the rule will encourage more environmental projects than would otherwise occur.

RESPONSE: The commission finds that it is not necessary for the rule to operate in a way that will accelerate or enhance the completion of environmental projects. It is enough that this rule has the ability to assist companies faced with large capital spending programs and lower the cost of financing projects of this nature, which will be of benefit to the company and the ratepayers. No change will be made as a result of this comment.

COMMENT #4 (Consumer Safeguards): Staff commented at length on the process of roundtables and other group efforts that created the draft ECRM rules and how the proposed ECRM relates to other rate adjustment mechanisms. As to safeguards in the rule, staff noted that electric utilities will only be permitted to request an ECRM in a general rate proceeding where all relevant expenses, revenues, and rate base items are considered. Parties to that proceeding can propose variations or alternative methodologies/mechanisms or can oppose the ECRM. The commission may approve, modify, or reject any proposed ECRM. An ECRM cannot remain in effect for longer than four (4) years without a new general rate proceeding and modification or extension of the ECRM.

OPC believes the proposed rules do not contain adequate consumer protections and do not adequately ensure that utilities will act prudently with respect to environmental expenditures. It is reasonable to assume the legislature would only have granted the commission authority to allow an ECRM in the belief that the commission's rules would protect ratepayers. Regulatory procedures should address the needs of both ratepayers and utilities (safe and adequate service at just and reasonable rates that provide a utility an opportunity to earn a fair rate of return). The rules should apply incentives to the utility, so it makes necessary environmental investments economically and so it operates those facilities reasonably. Timelines should be set out in the rule to ensure ratepayers are not faced with unreasonably large rate increases.

OPC opines that an ECRM shifts the risk of changes in the cost of environmental compliance from the utility to its customers and that this shift removes incentives for utilities to exercise due diligence and to develop and implement prudent environmental compliance strategies. This greatly changes the regulatory paradigm in Missouri, which has fostered low rates while maintaining reasonable returns for investors. Adequate consumer protections must be added to the proposed rules to compensate for the shifting risk, if the commission is to adequately perform its statutory duties. The allowance of an ECRM is not mandatory, but the proposed rules do not provide any guidance for determining whether an ECRM is appropriate. A "threshold test" of the necessity of an ECRM for the utility to earn its authorized return is needed, and should assess the likelihood the ECRM would cause it to overearn. The utility must be required to submit adequate financial data, accessible to all parties in the rate case, as part of its application.

MIEC agrees that it is crucial that consumer protections be included in the rule, rather than being left to rate cases. Key principles should be included in the rules, because industrial consumers must be allowed to plan for their impact. Providing protections in the rules ensures predictability for consumers and utilities alike and leads to fair application of the rules.

MIEC asserts that although section 386.266, RSMo, does authorize the commission to grant ECRMs, the statute is replete with consumer protections, such as the prudence requirement, the two and one-half percent (2.5%) annual cap, the ECRM creation rate case requirement, the "fair return" finding, the annual true-up, the no longer than four (4)-year rate case cycle, and regular prudence reviews. Failure to adhere to these consumer protections could render such an ECRM unlawful.

AmerenUE and staff are of the opinion that the consumer protections contained in SB 179 are already in the proposed rules.

RESPONSE: The commission finds that the necessary consumer protections, including the several consumer protections reflected in section 386.266, RSMo, are already contained in the rule and are sufficient. No change will be made as a result of this comment.

COMMENT #5 (Sharing Mechanisms): OPC advocates for a process to align the interests of ratepayers and shareholders. OPC would change language to allow approval of an ECRM that allows recovery of "some or all" of the costs, to provide an incentive mechanism in which the utility could only collect, ninety or ninety-five percent (90 or 95%) of the change in environmental costs. In addition, OPC would include a new section that specifically aligns the interests of ratepayers and shareholders, similar to performance-based language in the fuel adjustment clause rules. OPC remains skeptical that an ECRM could ever benefit ratepayers. For there to be a benefit, positive aspects would need to overcome the large detriment created by a flow-through mechanism for cost recoveries. The proposed rule, without the additional consumer protections OPC proposes, would be detrimental to ratepayers.

OPC believes that a financial incentive (gains or losses) is a critical consumer protection. To pass through one hundred percent (100%) of the cost significantly diminishes any incentive to prudently manage the annual cost of environmental compliance and to minimize long-run costs. Regulators cannot review transactions in real time, as the utility does. The utility should have to justify recovery of environmental compliance costs in a prudence review subsequently, using information gleaned during the recovery period. The electric industry is highly complex. A "fix" in one area can cascade through the rest of the system. A regulatory model that does not recognize this fact is inferior.

Staff counters that section 386.266, RSMo, allows incentives for rate adjustment mechanism, but there is no similar statutory provision for incentives for ECRMs. Section 386.266, RSMo, restricts the annual amount of revenue collected by an ECRM to not more than two and one-half percent (2.5%) of the revenues of the electric utility but allows the electric utility to defer costs not recovered as a result of this restriction. The language in the rule mirrors the language in the statute.

RESPONSE: The commission finds that staff is correct, in that subsection 1 of section 386.266, RSMo, which deals with rate adjustment mechanisms for fuel and purchased power costs, contains language permitting incentive plans, but subsection 2, pertaining to environmental cost recovery, does not. Subsection 8, cited by OPC in its comments, does not provide authority for incentive mechanisms; rather it states in part, "This subsection shall not be construed to authorize or prohibit any incentive- or performance-based plan." No change will be made as a result of this comment.

COMMENT #6 (Eligible Costs): Staff envisions that both capital expenditures and associated items that are normally expensed would be recoverable through an ECRM, the larger portion of which would be the capital expenditures. As to truly one (1)-time expenses, if the expense qualified for the adjustment, it would be put in then come out in subsequent true-up periods.

Staff has not compiled a list of items to be included or not included in an ECRM and does not recommend that the rule further define "federal, state, or local environmental law, regulation, or rule." The commission should determine in the proceeding in which an ECRM is established or modified exactly what costs are prudently incurred to comply with a "federal, state, or local environmental law, regulation, or rule" and should be recovered in an ECRM. This issue was discussed at length in the workshops on the rule, but the participants found it difficult to define without being either too broad or too restrictive. Staff concludes that it is best left to the discretion of the commission. For example, a utility might purchase a higher-priced coal to meet environmental requirements, but not have a fuel adjustment clause. There may be an argument that the higher-priced coal should not be in an environmental cost mechanism but would be more properly reflected in a fuel adjustment clause. It also is possible that the commission might find that a utility does not qualify for a fuel adjustment clause and then would have to address whether an increase in coal expense for compliance purposes should be included in the ECRM.

OPC comments that as the commission exercises its discretion in determining what types of costs are eligible for recovery, it should look at the volatility of the costs to be included and the extent to which the costs are directly related to compliance with environmental regulations.

RESPONSE: The commission finds that examining whether the costs are directly related to environmental compliance is inconsistent with the statutory standard set forth in the statute of "prudently incurred costs, whether capital or expense, to comply with [environmental requirements]." The commission finds the inclusion of the volatility of the costs into its consideration to be irrelevant. The ECRM is limited to two and one-half percent (2.5%) of a utility's Missouri gross jurisdictional revenues. This will serve to mitigate such volatility as may exist. Further, the commission may include a consideration of volatility, and is not precluding such a review by failing to include it here. Inclusion would require the commission to always consider volatility, even in those instances in which it is irrelevant. The commission agrees that a listing of eligible costs would be counter-productive, in that any attempt at such a list would likely be either too narrow or too broad. No change will be made as a result of this comment.

COMMENT #7 (4 CSR 240-20.091(1)(B) and (4)(B)): OPC commented that risk provides a powerful incentive to a utility to plan and operate its system in the most prudent manner. Increased earnings resulting from critical operational decisions provide immediate and effective feedback to those making the critical decisions. In contrast, regulatory oversight under the proposed rule is after the fact. The commission must attempt to recreate situations to envision the options available to a "reasonable person." Much of the information necessary to evaluate reasonableness is not always available to OPC or the commission. OPC proposes several changes in the attached rule to address this incentive concern. Inclusion of the phrase "some or all" in several sections explicitly recognizes the commission's discretion to approve an ECRM that permits only a portion of the changes in costs allowable to be included and recovered in the ECRM.

AmerenUE notes that it is entirely within the commission's discretion to not approve an ECRM. However, if the commission does approve one, the statute says that utility will be able to propose tariffs that would reflect changes in their environmental cost. In the ECRM context sharing or incentive mechanisms are not authorized. Section 386.266, RSMo, has two (2) subsections. Subsection 1 specifically indicates that the commission can incorporate incentive mechanisms in rate adjustment mechanisms for fuel and purchased power. Subsection 2, which deals with environmental costs, does not have any language of that nature. Therefore, the "some or all" language should not be inserted into this rule. If the government mandates an environmental cost and the utility incurs it, the utility ought to be able to pass that cost through.

RESPONSE: As discussed in response to comment #5 above, the commission finds that subsection 1 of section 386.266, RSMo, which deals with rate adjustment mechanisms for fuel and purchased power costs, contains language permitting incentive plans, but subsection 2, pertaining to environmental cost recovery, does not. No change will be made as a result of this comment.

COMMENT #8 (4 CSR 240-20.091(1)(D)1. and 2.): AmerenUE notes a drafting problem with the segregation of each utility's preexisting revenue requirement into "environmental" and "non-environmental" components so that changes in the environmental revenue requirement can be tracked through the ECRM. The proposed rules remain ambiguous.

Since depreciation and taxes associated with capital projects are expensed under standard accounting practices, the language in the proposed rules arguably suggests that depreciation and taxes fall under paragraph (1)(D)1., which in turn may lead some to argue that depreciation and taxes for all capital projects, not just major projects whose primary purpose is to comply with environmental standards, must be included in the existing "environmental revenue requirement." This would mean that depreciation and taxes associated with every environmental capital item, no matter how minor, would have to be identified, calculated, and included in the environmental revenue requirement, which would be difficult if not impossible. Given the commission's adoption of the major project/primary purpose concept, it appears that the intent is to include in the environmental revenue requirement only those capital-related costs associated with major items whose primary purpose is environmental compliance.

There are three (3) costs associated with environmental capital projects: the cost of capital (return); depreciation; and taxes. The commission need only modify the proposed rules as follows:

1. All expensed environmental costs (other than taxes and depreciation associated with capital projects) that are included in the electric utility's revenue requirement in the general rate proceeding in which the ECRM is established; and

2. The costs (i.e., the return, taxes, and depreciation) of any major capital projects whose primary purpose is to permit the electric utility to comply with any federal, state, or local environmental law, regulation, or rule. Representative examples of such capital projects to be included (as of the date of adoption of this rule) are electrostatic precipitators, fabric filters, nitrous oxide emissions control equipment, and flue gas desulfurization equipment. The costs of such capital projects shall be those identified on the electric utility's books and records as of the last day of the test year, as updated, utilized in the general rate proceeding in which the ECRM is established.

Staff supports AmerenUE's changes. No commenters opposed them or provided alternative language.
RESPONSE AND EXPLANATION OF CHANGE: The commission finds the rule as written is unclear. It will make the changes proposed by AmerenUE and supported by staff as noted in the comment and as fully set forth below.

COMMENT #9 (4 CSR 240-20.091(1)(F)): Staff, in support of the proposed rule, notes that the ECRM rules do not address voltage levels. Voltage levels and line losses pertain to fuel and purchased power costs but are not relevant to environmental compliance costs. Most environmental costs will be large capital plant investments. This equipment is required regardless of how much energy the plant generates and does not correspond to the amount of energy usage of any customer or any customer class. The ECRM rules are silent on the rate design of the ECRM. Parties to the general rate case setting the ECRM can propose cost allocation methodologies and rate design proposals to the commission. The rules, as proposed, leave to the commission the determination of allocation method, including methods that take voltage levels into account.
RESPONSE: No language change is necessitated by these comments.

COMMENT #10 (4 CSR 240-20.091(2)(A)): As discussed in comment #2 above, MIEC believes the proposed rules favor utilities. An overearning utility could receive additional revenues under an ECRM, contrary to legislative intent. OPC proposes the following additional language in subsection (2)(A):

> The commission may approve the establishment, continuation, or modification of an ECRM and rate schedules implementing an ECRM provided that it finds that the ECRM it approves is necessary and reasonably designed to provide the electric utility with a sufficient opportunity to earn a fair return on equity, but no greater than a fair return on equity. Any rate schedule approved to implement an ECRM must conform to the ECRM approved by the commission.

MIEC proposed similar language, which states:

> The commission may approve the establishment, continuation, or modification of an ECRM and rate schedules implementing an ECRM provided that it finds that the ECRM it approves is necessary and reasonably designed to provide the electric utility with a sufficient opportunity to earn a fair return on equity, but not by use of the ECRM in excess of a fair return on equity. Any rate schedule approved to implement an ECRM must conform to the ECRM approved by the commission.

As to the inclusion of the word "necessary," OPC comments that this change was proposed to give guidance to the commission on its exercise of the discretion under this new law, to decide whether an ECRM is appropriate. AmerenUE notes that the proposed language is inconsistent with section 386.266.4.1, RSMo, which requires that the commission find that the mechanism is reasonably designed to provide the utility with a sufficient opportunity to earn a fair return on equity. This is a substantively different standard than "necessary."

As to the inclusion of the phrase "but no greater than a fair return on equity," AmerenUE responds that this additional language is not consistent with SB 179, for all the reasons set forth above in comment #2. The addition of such a requirement would be impracticable and essentially disable the use of the mechanism entirely. The enabling statute does not contain such a requirement, rather it requires only that the mechanism needs to be reasonably designed to provide a fair opportunity to earn a reasonable return. There is nothing in the statute about having earnings tests between rate cases, except to the extent they will be applied when an ECRM adjustment is made. An ECRM is established only in a rate case and reviewed in a subsequent rate case. If excess earnings are suspected between rate cases upon review of the extensive surveillance and reporting, a complaint can be filed.

As to the inclusion of the sentence, "Any rate schedule approved to implement an ECRM must conform to the ECRM approved by the commission," no party objected to the inclusion. AmerenUE noted that it found the requirement to be unnecessary, as every compliance tariff filed after a rate case must conform to the order of the commission. However, AmerenUE stated it had no objection.
RESPONSE AND EXPLANATION OF CHANGE: The commission finds that the first two (2) language changes are not necessary. The "necessary" language imposes a standard not found in the statute, which restricts the scope of this rule and precludes inclusion. The second language change, which calls into question the validity of an ECRM if the utility earns in excess of its authorized rate of return at any point in time, is not consistent with the statute. No change will be made as a result of these comments.

As to the language concerning compliance tariffs, the commission finds that, although it restates a current requirement, it properly articulates that standard and is reasonable to include, as set forth fully below.

COMMENT #11 (4 CSR 240-20.091(2)(B) and (3)(B)): OPC and MIEC propose to change the word "may" to "shall" in subsection (B) of sections (2) and (3). MIEC notes that although the statute uses the word "may," both OPC and MIEC have suggested that the commission require consideration in establishing an appropriate rate of return whether utility has an ECRM. The statute uses the term may, but this commission has the right to exercise its discretion to require it in every case, and MIEC suggests that the commission do that. AmerenUE comments that changing the word "may" to "shall" is another attempt to change the statute itself, which reads, the commission "may take into account any change in business risk..." The rules cannot lawfully require when the legislation specifically provides that the commissions may, but is not required to, consider this factor.
RESPONSE: The commission agrees that the rule appropriately mirrors the language in the statute. No change will be made as a result of this comment.

COMMENT #12 (4 CSR 240-20.091(2)(C)): OPC suggests additional considerations for the commission to address in determining the appropriateness of recovery through an ECRM. OPC asserts that insertion of the word "directly" does not impose a new standard because the concept already appears in the definitions of environmental cost in both Chapter 20 and Chapter 3. The Chapter 20 definition says, "Environmental costs mean prudently incurred costs, both capital and expense, directly related to compliance with any federal, state or local environmental law, regulation or rule." OPC suggests making this subsection consistent with the provisions in the rule that define environmental cost. OPC also proposes to include volatility in the criteria for evaluating whether a particular cost should be included in an ECRM.

MIEC and OPC propose to make insertions in subsection (2)(C) as follows:

In determining which environmental cost components to include in an ECRM, the commission will consider, but is not limited to only considering, the magnitude of the costs, the ability of the utility to manage the costs, the volatility of the cost, the incentive provided to the utility as a result of the inclusion or exclusion of the cost, and whether the cost is directly related to environmental compliance.

AmerenUE notes that volatility is just a factor the commission reviews in connection with fuel adjustment clauses. It is not required by the statute. Moreover, consideration of volatility does not dictate a certain outcome as to inclusion in a fuel adjustment cause. In any event, environmental costs are driven by compliance with statutes or regulations that are imposed by the government. The ECRM provisions were designed to be a tool to address the prospect of huge expenditures to control pollution. Installation of a $500 million scrubber every couple years may not be "volatile" in the sense intended by OPC, but an item mandated by law and beyond the utility's control will certainly inject volatility into utility earnings.

AmerenUE opposes the inclusion of "directly" as it appears to preclude the utility from passing through an environmental cost that is indirectly caused by environmental regulation. If a law imposes indirect costs, then those costs should be recovered. If a company put in a scrubber earlier than required because it would be cheaper at that point, it might be argued that, because it was not required at that moment, it was only indirectly caused by the regulations, although it was prudent and wise to do. Therefore, the proposed change is inappropriate and unwise.

RESPONSE: As the commission discussed in its response to comment #6 above, examining whether the costs are directly related to environmental compliance is inconsistent with the statutory standard of "prudently incurred costs, whether capital or expense, to comply with [environmental requirements]." Although OPC correctly points out that the definition of environmental costs includes the word "directly," its inclusion here is inappropriate. The commission finds the inclusion of the volatility of the costs into its consideration to be irrelevant. The ECRM is limited to two and one-half percent (2.5%) of a utility's Missouri gross jurisdictional revenues. This will serve to mitigate such volatility as may exist. Further, the commission may, in its discretion, consider volatility and is not precluding it by not including it here. Inclusion would require the commission to always consider volatility, even in those instances in which it is irrelevant. No change will be made as a result of this comment.

COMMENT #13 (4 CSR 240-20.091(2)(H) and(4)(C)): MIEC proposes a limitation on deferrals of ECRM costs. Ratepayers need protection against deferrals of excessive ECRM costs resulting in unreasonable rates. The proposed rule should specify the commission's authority to limit deferrals to protect ratepayers. The rule should specify that deferred costs cannot be recovered when the utility earned in excess of its authorized return during the period in which the deferred costs were incurred, and specify that allowed deferred costs be collected over the life of the capital addition that gave rise to the cost deferral.

OPC proposes changes to reduce the utility's ability to earn in excess of its authorized return. Specifically, OPC and MIEC propose the following standard to determine whether deferred costs can be included in either an ECRM or rate case proceeding in subsection (4)(C):

4. The recovery of any deferred costs and related carrying costs shall be limited to those deferrals that, absent deferral, would have resulted in the utility earning less than its authorized rate of return on equity during the periods from which the costs were deferred.

5. The recovery period for which deferred costs are eligible for recovery shall be equal to the life of the asset if the cost would have been a capital cost or related to a capital cost in the period incurred absent its deferral.

6. The recovery period for which deferred costs are eligible for recovery shall be not less than five (5) years but not greater than ten (10) years if the cost would have been an expense in the period incurred absent its deferral.

7. The recovery period shall be determined by the commission at the time the recovery of the deferred costs begins.

8. Deferred costs that are eligible for recovery shall not be considered part of Rate Base in subsequent general rate proceedings.

OPC's proposed earnings test applies only to the deferral and not to the ECRM periodic adjustment. If the ECRM adjustment is less than two and one-half percent (2.5%), there would be no subsequent earnings test. The earnings test would only apply when the utility defers revenues, and would determine whether, absent the deferral, earnings would have been adequate. The analysis would be performed only in the required rate case at the end of the ECRM period. OPC notes that a deferral in years one (1), two (2), or three (3) of an ECRM does not preclude an ECRM adjustment in a subsequent year to reflect a change in environmental revenue requirement. The ECRM calculation would be made just as it was in the initial year. Environmental compliance expenses and capital investments will be recorded as they occur. Costs, not revenues, determine the overall cost of service.

AmerenUE comments that language to limit recovery of deferred costs when the utility has earned in excess of its authorized return at any point within the duration of an ECRM is not authorized, is unwise, and should not be adopted. Limiting the recovery period to the life of the capital asset to which the deferred cost relates appears to modify the two and one-half percent (2.5%) cap and deferral provisions in SB 179. The last sentence of section 386.266.2, RSMo, says that any costs not recovered as a result of the annual two and one-half percent (2.5%) limitation may be deferred at a carrying cost each month equal to the utility's net of tax cost of capital for recovery in a subsequent year or in the corporation's next general rate case or complaint proceeding. Therefore, the proposed language is contrary to the statute and for that reason should not be adopted.

Staff commented that the statute limits the ECRM to two and one-half percent (2.5%) of a utility's Missouri gross jurisdictional revenues in first year; in the second year, an additional two and one-half percent (2.5%) is permitted and so forth for all four (4) years. The most the rates could increase would be ten percent (10%), based on the statutory language "shall not exceed an annual amount," meaning that each year's maximum ECRM amount cannot exceed two and one-half percent (2.5%). Staff does not support any restriction on the amounts of the deferral of increases above the cap, which carries over to the next rate case, in which recovery may be sought. Safeguards tie large deferrals to capital investments that track to an environmental compliance plan. The commission can determine in the rate case whether a cost is a fuel/purchased power or an environmental cost. Some stakeholders feared that utilities may identify an environmental cost as a fuel or purchased power cost to circumvent the two and one-half percent (2.5%) annual limit. However, no suitable language to address this concern could be agreed upon. The proposed rules do state that environmental costs do not include fuel and purchased power costs. The parties to the rate case can present their positions as which cost items should be collected in a rate adjustment mechanism and which should be collected in an ECRM. The commission will then have the opportunity to ensure that environmental costs are not improperly classified.

RESPONSE: The commission finds that the language change is not necessary. As discussed in comment #2 above, limiting recovery because there are earnings in excess of an authorized rate of return at a point in time would be inconsistent with the statute. In the event that a utility has environmental costs in excess of the cap, it shall, as staff noted, seek to recover all of those costs in the subsequent rate case. Attempting, in that subsequent rate case, to determine whether a utility overearned for any period of time or at a point in time would unduly burden a rate case proceeding in which the established parameters of test year and normalized conditions protect both utilities and ratepayers. No change will be made as a result of this comment.

COMMENT #14 (4 CSR 240-20.091(2)(K)): MIEC asserts that the rules need to protect against utility overearnings. Absent a mechanism to adjust rates if earnings are above the authorized return, there is a strong potential that utilities will overearn and rates will be too high. Section 386.266, RSMo, requires that an ECRM be "reasonably designed to provide the utility with a sufficient opportunity to earn a fair return on equity," not that utilities "earn at least a fair return on equity." Moreover, the commission's statutory obligation is to establish "just and reasonable rates." After rates are set, elements of the revenue requirement equation will change. The combined effect of changes alters the utility's return on equity. To the extent that particular costs are singled out for separate recovery, such as the ECRM, there is a high likelihood that the utility will over-earn, because environmental compliance cost increases may be passed through without any offsetting decreases in other costs. Accordingly, the commission must implement a mechanism that enables it to limit the pass-through of environmental costs if other costs decrease. MIEC asserts that Missouri utilities have earned returns in excess of "reasonable" returns and have made refunds and reduced rates. Utilities may argue this is not likely to be repeated. If that is the case, the utilities should be unconcerned with MIEC's proposals. MIEC believes the potential for overearning still exists and that consumers are entitled to protection, especially when adjustment clauses are added to tariffs. Such mechanisms, left unchecked, allow utilities to isolate and recover costs, without considering all other costs and revenues. Completion of major construction will result in declining rate base, resulting in increasing returns. MIEC proposes to add the following language as new subsection (2)(K):

> In establishing, continuing, or modifying the ECRM, the commission shall consider whether the presence of the ECRM is likely to allow the utility to earn in excess of its authorized return on equity. If the commission finds this to be the case, it may include in the ECRM procedures designed to periodically examine the utility's earnings (on a regulatory basis), and appropriately limit the collection of costs under the ECRM to the extent necessary to prevent the utility from earning in excess of its authorized return on equity as a result of revenues received through the ECRM.

AmerenUE responds that MIEC's proposed language is an earnings test; a cap on ECRM adjustments based on whether a utility is earning above its authorized return, without consideration of other factors, at some particular point in time. It would improperly preclude consideration of a change in the utility's cost of equity. Whether a utility's rates are just and reasonable cannot be determined at a point in time by "examining the utility's earnings (on a regulatory basis)." This is what the periodic rate cases required by SB 179 are for.

RESPONSE: The commission finds that the proposed language would allow for the modification of an ECRM between rate cases, which is specifically precluded by section 386.266.4., RSMo. That section requires that the "commission shall have the power to ... modify ... adjustment mechanisms ... only after providing ... a general rate proceeding." No change will be made as a result of this comment.

COMMENT #15 (4 CSR 240-20.091(3)(A)): Both OPC and MIEC propose language be added to the rule that would allow those who oppose the discontinuation of an ECRM to be able to do so on the grounds that granting an ECRM is a detriment to the public interest, by inserting as a grounds for opposition to the discontinuation of an ECRM "or on any other grounds that would result in a detriment to the public interest." OPC notes that although this language is not in the statute, neither is the other language in the proposed rule concerning a basis for opposing discontinuation of an ECRM. If opposing the discontinuance on the basis of declining costs is appropriate, OPC asserts that opposing the discontinuance on the basis of public detriment is appropriate as well.

AmerenUE responds that a "public interest" standard is not found anywhere in SB 179 and would cause the ECRM rules to vary from the FAC rule provisions on the same subject. The obvious purpose of this discontinuation provision is to preclude the utility from opportunistically ending an ECRM mechanism if its environmental costs were going down. It was not to prevent the utility from deciding it did not want to file a tariff in a later rate case to continue an ECRM based upon the amorphous "public interest" language proposed by OPC and MIEC. Utilities are the only parties who can file tariffs to propose an ECRM in the first place. Unless the utility is opportunistically seeking to end an ECRM to deprive ratepayers of environmental cost decreases, the utility should be free to discontinue an ECRM for other reasons.

RESPONSE AND EXPLANATION OF CHANGE: As has been noted above, the FAC rules and the ECRM rules should and do differ in material respects. Because the commission has determined that it will not include any incentive or sharing mechanisms, there is less incentive for companies to "opportunistically" discontinue an ECRM. However, to the extent that parties in a general rate case may seek to oppose the discontinuance of an ECRM on the grounds that doing so would be a detriment to the public is perfectly reasonable. Therefore, the commission will insert the requested language in subsection (3)(A) as fully set forth below.

COMMENT #16 (4 CSR 240-20.091(3)(A)): In support of the rule, staff notes that adjustments to the ECRM will be usually based on large capital investments which will be depreciated. The proposed rules require that the ECRM reflect both the net increases and decreases in an electric utility's environmental costs, including the depreciation that accumulates as a reduction to rate base over time. These will also capture changes in environmental costs from the general rate case that are replaced with another type of environmental cost.

RESPONSE: No language change is necessitated by these comments.

COMMENT #17 (4 CSR 240-20.091(4)): In support of the rule, staff asserts that tracking costs to calculate net increases and decreases will not be burdensome. An electric utility could identify a limited number of specific environmental cost and revenue items on its books and records that would be considered in adjusting its ECRM.

RESPONSE: No language change is necessitated by these comments.

COMMENT #18 (4 CSR 240-20.091(4)(D)): In support of the rule, staff commented that, as to the number of filings to be made each year, two (2) filings each year (one (1) true-up and one (1) at the utility's discretion) are sufficient. Two (2) filings within the year should be able to capture those additional capital investments to meet the compliance rules. Environmental costs are not likely to fluctuate greatly in a short period of time. Before any of them are allowed in rates, the commission must determine that the equipment is "fully operational and used for service." Fewer adjustments will reduce the volatility of customer bills. The rate adjustment limit provision of SB 179 is annual and cumulative for each year.

RESPONSE: No language change is necessitated by these comments.

COMMENT #19 (4 CSR 240-20.091(5)(D)): In support of the rule, staff commented that the language in the ECRM rule provides for monthly application of interest, equal to the utility's average monthly short-term debt cost, to a utility's cumulative under- or over-recovery of ECRM costs. Important to managing environmental costs is a

long-term environmental compliance plan that is consistent with the electric utility's long-term resource plan.
RESPONSE: No language change is necessitated by these comments.

COMMENT #20 (4 CSR 240-20.091(11)): MIEC and OPC seek to insert a new section entitled "Incentive Mechanism or Performance-Based Program," which they assert is consistent with 4 CSR 240-20.090(11) (the fuel adjustment clause rule) and prior commission decisions, as follows:

(11) Incentive Mechanism or Performance-Based Program. During a general rate proceeding in which an electric utility has proposed establishment or modification of an ECRM, or in which an ECRM may be allowed to continue in effect, any party may propose for the commission's consideration incentive mechanisms or performance-based programs to improve the efficiency and cost effectiveness of the electric utility's environmental compliance planning and implementation activities.

(A) The incentive mechanisms or performance-based programs may or may not include some or all components of environmental costs, designed to provide the electric utility with incentives to improve the efficiency and cost-effectiveness of its environmental compliance planning and implementation activities.

(B) Any incentive mechanism or performance-based program shall be structured to align the interests of the electric utility's customers and shareholders. The anticipated benefits to the electric utility's customers from the incentive or performance-based program shall equal or exceed the anticipated costs of the mechanism or program to the electric utility's customers. For this purpose, the cost of an incentive mechanism or performance-based program shall include any increase in expense or reduction in revenue credit that increases rates to customers in any time period above what they would be without the incentive mechanism or performance-based program.

(C) If the commission approves an incentive mechanism or performance-based program, such incentive mechanism or performance-based program shall be binding on the commission for the entire term of the incentive mechanism or performance-based program. If the commission approves an incentive mechanism or performance-based program, such incentive mechanism or performance-based program shall be binding on the electric utility for the entire term of the incentive mechanism or performance-based program unless otherwise ordered or conditioned by the commission.

AmerenUE notes that the proposed language appears to be copied from the fuel adjustment clause rules into the ECRM rules. The problem is there is specific language in the fuel adjustment clause provisions of section 368.266, RSMo, that authorizes incentives. There is no such language in the environmental provisions of section 386.266, RSMo, and therefore, under very basic principles of statutory construction, the absence of that language precludes these types of incentive mechanisms. In addition, eligible costs are mandated by environmental regulation. They do not produce revenue, and many will reduce generating capability, thereby reducing revenues. For these reasons, incentive mechanisms for ECRMs are not only unlawful, but unfair and unwise.
RESPONSE: As discussed at length above in response to comments #5 and #7 and elsewhere, the commission remains convinced that, although subsection 1 of section 386.266, RSMo, pertaining to rate adjustment mechanisms for fuel and purchased power costs, includes language permitting incentive plans, subsection 2, pertaining to environmental cost recovery, does not. The commission is without authority to authorize any incentive- or performance-based plan in environmental cost recovery mechanisms. No change will be made as a result of this comment.

4 CSR 240-20.091 Electric Utility Environmental Cost Recovery Mechanisms

(1) Definitions. As used in this rule, the following terms mean as follows:

(D) The environmental revenue requirement shall be comprised of the following:

1. All expensed environmental costs (other than taxes and depreciation associated with capital projects) that are included in the electric utility's revenue requirement in the general rate proceeding in which the ECRM is established; and

2. The costs (i.e., the return, taxes, and depreciation) of any major capital projects whose primary purpose is to permit the electric utility to comply with any federal, state, or local environmental law, regulation, or rule. Representative examples of such capital projects to be included (as of the date of adoption of this rule) are electrostatic precipitators, fabric filters, nitrous oxide emissions control equipment, and flue gas desulfurization equipment. The costs of such capital projects shall be those identified on the electric utility's books and records as of the last day of the test year, as updated, utilized in the general rate proceeding in which the ECRM is established;

(2) Applications to Establish, Continue, or Modify an ECRM. Pursuant to the provisions of this rule, 4 CSR 240-2.060, and section 386.266, RSMo, only an electric utility in a general rate proceeding may file an application with the commission to establish, continue, or modify an ECRM by filing tariff schedules. Any party in a general rate proceeding in which an ECRM is in effect or proposed may seek to continue, modify, or oppose the ECRM. The commission shall approve, modify, or reject such applications to establish an ECRM only after providing the opportunity for a full hearing in a general rate proceeding. The commission shall consider all relevant factors that may affect the costs or overall rates and charges of the petitioning electric utility.

(A) The commission may approve the establishment, continuation, or modification of an ECRM and rate schedules implementing an ECRM provided that it finds that the ECRM it approves is reasonably designed to provide the electric utility with a sufficient opportunity to earn a fair return on equity. Any rate schedule approved to implement an ECRM must conform to the ECRM approved by the commission.

(3) Application for Discontinuation of an ECRM. The commission shall allow or require the rate schedules that define and implement an ECRM to be discontinued and withdrawn only after providing the opportunity for a full hearing in a general rate proceeding. The commission shall consider all relevant factors that affect the cost or overall rates and charges of the petitioning electric utility.

(A) Any party to the general rate proceeding may oppose the discontinuation of an ECRM on the grounds that the electric utility is currently experiencing, or in the next four (4) years is likely to experience, declining costs or on any other grounds that would result in a detriment to the public interest. If the commission finds that the electric utility is seeking to discontinue the ECRM under these circumstances, the commission shall not permit the ECRM to be discontinued, and shall order its continuation or modification. To continue or modify the ECRM under such circumstances, the commission must find that it provides the electric utility with a sufficient opportunity to earn a fair rate of return on equity.