IN THE SUPREME COURT OF MISSOURI

SPIRE MISSOURI INC., f/k/a LACLEDE GAS COMPANY,
Appellant,

v.

PUBLIC SERVICE COMMISSION OF THE STATE OF MISSOURI,
Respondent,

and

OFFICE OF PUBLIC COUNSEL, Intervenor.

APPEAL NO. SC 97834

SUBSTITUTE REPLY BRIEF OF APPELLANT SPIRE MISSOURI INC., f/k/a LACLEDE GAS COMPANY

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INTRODUCTION

In this appeal, Appellant Spire Missouri Inc. ("Spire") challenges three decisions made by the PSC in its March 7, 2018 Amended Report and Order ("Amended Order") in rate cases for Spire East and West.[1] The three issues are (i) the PSC's denial of half of Spire's rate case expense[2]; (ii) the PSC's use of relocation proceeds from a sale of property prior to the test year to reduce rates in Spire East's rate case; and (iii) the PSC's denial of a prepaid pension asset that Spire has carried on its books since the 1990s.

STANDARD OF REVIEW

The overarching issue in this case is what standard of review should the courts adopt in reviewing PSC decisions. The Missouri Constitution directs the courts to review all of the evidence on a given point on appeal, and to determine whether there is sufficient competent and substantial evidence on the whole record to support the PSC's decision. On findings of fact, PSC orders must be reasonable, which means they must be supported by competent and substantial evidence on the whole record, and must not be arbitrary and

[1] Spire would note that the Amended Order is 150 pages and covers dozens of decisions, many of which were adverse to Spire. The three issues in this case are the only PSC decisions that Spire has chosen to raise in this appeal.

[2] Not including the expenses required to conduct a depreciation study and send customer notices, both of which are non-litigation expenses that Spire is required to perform pursuant to either PSC rule or order.

capricious, or an abuse of discretion. As the PSC acknowledges, on conclusions of law, it is given no deference; legal issues are reviewed de novo.

The Court must look to the whole record of an agency's decision, and not just the evidence supporting the decision. The Court reviews the whole record objectively, and not in the light most favorable to the PSC's decision. ***Hampton v. Big Boy Steel Erection***, 121 S.W.3d 220, 223 (Mo. banc 2003). The Court should confirm that this standard applies to PSC cases, and consider removing the reference that agency decisions should be overturned only in "rare" cases, for fear that it serves as an artificial safety net, encouraging agencies to push the boundaries of propriety. (PSC Br., p. 28).

A court reviews the evidence not to determine whether it agrees with the agency's finding, but whether, given all the evidence, the agency could have reasonably arrived at that finding. There is no strict mathematical formula for this review. The court does not "weigh" evidence to see which side had the better of the argument. Evidence is weighed only to determine whether the scales are so heavily tipped against the agency's decision that such decision is unreasonable.

The PSC Brief acknowledges that courts should review the competent and substantial evidence on the whole record. However, the PSC's arguments in this case encourages a review that would fail to meet the required standard. The PSC invites the Court to forego its constitutionally mandated role in assuring that the PSC has acted reasonably. Like the Wizard of Oz, the PSC does not want this Court to look behind the curtain, but wants the court to afford the PSC discretion so broad as to effectively eviscerate judicial review.

There is ample proof of the PSC's efforts to avoid having the Court look behind its decisions at the evidence. First, the PSC's Section 1 Argument cites ***State ex rel. KCP&L Greater Mo. Operations Co. v. Pub. Serv. Comm'n***, 406 (sic)[3] S.W.3d 153, 162 (Mo. App. W.D. 2013), for the proposition that "the standard for the adequacy of the Commission's factual findings is a flexible one." (PSC Br., p. 28). The PSC proceeds to use this case to conclude that the "facts are adequate if they are 'sufficiently definite and certain . . . to enable the court to review the decision intelligently and ascertain if the facts afford a reasonable basis for the order *without resorting to the evidence*.'" (*Id.* (emphasis added)). The PSC adds that "[i]t is not necessary for the Commission's order to go into evidentiary detail to be valid. ***Mo. Gas Energy***, 186 S.W.3d at 382." (*Id.* at 29). The PSC's citation to these cases to support its argument for a watered-down standard of review is misguided. One need only read these cases to understand that the points being made therein refer only to whether a finding is written clearly enough so that a court can understand the meaning of the finding and whether it supports the agency's decision. The cited language does not describe the review necessary to determine whether a finding is supported by competent and substantial evidence on the whole record. Since Spire raises no issues on appeal regarding the written clarity or adequacy of the findings in the Amended Order, the PSC's argument based on its misguided citation to ***State ex rel. KCP&L Greater Mo. Operations Co.*** and ***Mo. Gas Energy*** has no relevance to the issues raised in this appeal.

[3] The correct cite is ***408*** S.W.3d 153.

Second, the PSC's brief primarily cites only to its own evidence and avoids looking at the record as a whole, as the standard requires. Including the PSC's discussion of the standard of review and its arguments, the PSC states 14 times in its brief that the standard of review requires a review of the record as a whole. However, the PSC's "statement of facts" goes on for 17 pages citing all of the PSC's findings of facts and evidence, and only the PSC's findings, as if those are the only facts and evidence that exist. (*See id.* at 7-24). Most of the PSC's arguments are merely recitations of its own findings, sometimes without supporting evidence for those findings, and other times with support based only on the evidence chosen by the PSC. As explained below, the PSC often ignores evidentiary insufficiencies that would become clear when one considers the record as a whole.

In focusing only on its own findings, the PSC is advocating a standard that denies Spire and other litigants the opportunity to show that such findings are not supported by competent and substantial evidence on the whole record. The PSC relies on §393.270.4, RSMo. to support its purported broad discretion in setting rates (*Id.* at 26, 35). Notably, courts have interpreted §393.270.4 to mean that the Commission must consider all relevant factors in setting utility rates. ***State ex rel. Util. Consumers' Council of Mo., Inc. v. Pub. Serv. Comm'n***., 585 S.W.2d 41 (Mo. banc 1979) ("***UCCM***"). The PSC argues that §393.270.4 provides it virtually unfettered discretion to deny Spire any expense item. In fact, ***UCCM*** stands for precisely the opposite proposition. In ***UCCM***, this Court struck down an electric utility fuel adjustment clause (FAC), finding that adjusting fuel rates outside of a rate case was prohibited single-issue ratemaking. The Court acknowledged that not every item of expense had to be treated alike; for example, a tax adjustment clause for gross receipts taxes was justified because the nature of these taxes was such that adjusting them did not affect the underlying rates. ***UCCM***, 585 S.W.2d at 51-53. However, the Court considered gross receipt taxes to be a rare exception to the rule. *Id*. at 56-57. The Court found that the FAC was not different enough from other expense items to justify allowing it to be adjusted outside of a rate case. *Id*. at 53.

Rather than affording the PSC wide discretion, ***UCCM*** actually *limits* the PSC's discretion by requiring it to take into account all relevant factors, and not permitting the PSC to treat fuel expenses differently. The ***UCCM*** court agreed that gross receipt taxes could be treated differently from other expenses, but declined to go further down a slippery slope and permit the same discretion to fuel expenses. *Id*. at 57. In this case, the PSC is also trying to distinguish an expense (i.e., rate case expense) and treat it differently than other operating expenses. As set forth below, the stated distinctions are either false or meaningless. The PSC is attempting to slide down a slippery slope by inaccurately claiming it has the discretion to separate rate case operating expense from other operating expenses.

REPLY ARGUMENT

Rate Case Expense

Point I: The PSC cannot simply disallow normal utility operating expenses without violating the utility's right to just and reasonable rates. The Amended Report and Order decision denying Spire nearly half of its rate case operating expenses was unlawful. (Replies to Respondent's Point 2)

Utilities are entitled to just and reasonable rates in order to meet their obligation to provide safe and adequate service. §393.130, RSMo. It is well established that the PSC is required to approve rates sufficient to cover a utility's operating expenses (as well as the capital costs of the business). ***State ex rel. Mo. Water Co. v. Pub. Serv. Comm'n***, 308 S.W.2d 704, 714-15 (Mo. 1957); ***State ex rel. Associated Nat. Gas Co. v. Pub. Serv. Comm'n of Mo.***, 706 S.W.2d 870, 873 (Mo. App. W.D. 1985).

While the PSC has some discretion in determining what costs are not properly recoverable (e.g., charitable donations or political lobbying expenses, both of which are unrelated to the provision of utility service), it cannot deny normal utility operating costs without running afoul of the utility's right to just and reasonable rates.

Certainly, the costs to bill and collect from customers is a normal operating cost. The PSC cannot find that shareholders should share these costs simply because collecting revenues benefits shareholders. Nor could the PSC force shareholders to share debt costs, even though the utility uses those revenues to pay creditors, which benefits equity holders. The PSC cannot force shareholders to assume a share of these costs without violating the utility's constitutional rights.

Rate case expense is also a necessary and normal operating expense that a utility must incur. A utility is generally prohibited from raising its rates without a rate case, so utilities must file such cases to keep up with inflation and other cost increases. In order to survive, utilities must be able to recover required operating expenses, such as normal rate case operating expense. The fact that the ISRS Statute required Spire to file a rate case or lose the right to collect millions of dollars in ISRS revenues only strengthens that position, especially since the rate case filing requirement is a consumer protection intended for the utility to justify its ISRS charges every 3-4 years. (§393.1012, RSMo.; Exs. Vol. 11, p. 1751).

The PSC has effectively conceded that rate case expense is a normal expense, because it "normalized" the expense over the usual amount of time between Spire rate cases (four years). (L.F. Vol. 12, p. 4285; PSC Br., pp. 11, 14). The PSC itself defined a normalization adjustment as an "adjustment made to reflect normal, ongoing operations of the utility." (L.F. Vol. 12, p. 4242). By normalizing rate case expense recovery, the PSC acknowledged that rate case expense is a normal operating expense. As such, the PSC cannot deny this prudently incurred expense without running afoul of Spire's right to just and reasonable rates.

Nevertheless, the PSC improperly decided that it could lawfully separate rate case expense from other operating expenses. (L.F. Vol. 12, pp. 4282-85). The PSC relied on four arguments to support its denial of rate case expense: 1) the rate case process is adversarial in nature, with the utility on one side and its customers on the other; 2) rate case expense produces some direct benefits to shareholders that are not shared with customers, such as seeking a higher return on equity; 3) requiring all rate case expense to be paid by ratepayers provides the utility with an inequitable financial advantage over other case participants; and 4) full reimbursement of all rate case expense does nothing to encourage reasonable levels of cost containment. (L.F. Vol. 12, p. 4060).

None of these reasons excuse the PSC from its obligation to treat rate case expense like other operating expenses.[4] The flaws in these reasons were discussed at length in Appellant's brief. In addition, the PSC cannot lawfully justify separating rate case expense from other operating costs when it routinely approves the expenses of full-time employees who perform most of the work in rate cases. There is no legal distinction between rate case expense incurred by Spire employees and those incurred by outside contractors. In fact, to the extent outside contractors specialize in rate case issues, such as class cost of service studies and rate design, such contractors could be more effective and efficient than Spire employees.

Spire understands and supports the concept that it is not entitled to recover expenses that are imprudently incurred, including those expenses found to be excessive or unreasonable. The PSC wrongly believes that its discretion is so broad that it may disallow any expense, whether or not the expense is prudent. In this case, the PSC made no finding of imprudence. (L.F. Vol. 12, p. 4284).

But even if the Court were to decide that the PSC could disallow rate case expense for the specific reasons given in the Amended Order to justify such a disallowance, the Amended Order completely fails to link any rate case expense actually incurred to any of those reasons. The PSC cannot lawfully identify certain reasons that it believes justifies a

[4] The allegedly adversarial rate case process was established by the legislature in the PSC Statutes, which provide for substantial justice between customers and utilities. §386.610, RSMo. As described herein, Spire's proposals were primarily designed to be mutually beneficial to the utility and its customers.

disallowance and then simply shed half of Spire's rate case expense without any tie between the reasons and the amount of disallowance, other than Spire happened to raise half the issues in its own rate case. Doing so deprives the utility of its right to just and reasonable rates.

Point II: The Amended Order was unreasonable because it denied nearly half of Spire's rate case expense based on reasons that were arbitrary and capricious, unsupported by competent and substantial evidence or were an abuse of discretion. (Replies to Respondent's Point 2)

In addition to being unlawful, the Amended Order's denial of rate case expense was unreasonable. A brief review of the record evidence demonstrates that the PSC acted unreasonably in denying rate case expense based upon the number of issues Spire raised. The unreasonableness of the PSC's approach is underscored by its failure to deny any of Spire's rate case expense as imprudent.

PSC's Failure to Link Tracking Issues to Rate Case Expense

The PSC failed to link any particular rate case expense to the matters supporting its decision. The Amended Order states that one of the reasons supporting rate case expense disallowance was Spire's proposing three new tracking mechanisms. Spire did propose tracking mechanisms at the beginning of the case, but withdrew two of the three prior to hearing. (Exs. Vol. 5, pp. 1112-13). The remaining tracker was for environmental costs, which is specifically authorized by the legislature. (*See* §386.266.2, RSMo.; L.F. Vol. 11, pp. 3529-31). Moreover, the matter was handled by in-house employees whose cost do not even qualify as rate case expense. Hence, the submission of these proposals did not drive any rate case expense.

PSC's Failure to Consider the Whole Record in Denying Expenses

The PSC's arbitrary and capricious decision to deny Spire half of its rate case expense based on a one-sided view of the evidence presented below is exactly what the Missouri Constitution sought to avoid in directing courts of law to review the decisions of administrative agencies by looking at the evidence on the whole record.[5] In addition to the proposed tracking mechanisms, the PSC identified four other matters brought by Spire that provided a basis for denying Spire's rate case expense. (L.F. Vol. 12, p. 4283). The four matters are: 1) the revenue stabilization mechanism (RSM); 2) return on equity (ROE); 3) earnings-based incentive compensation; and 4) the alleged padding of revenue requirement.

[5] The Amended Order determined that Spire share "most of the rate case expenses." (L.F. Vol. 12, p. 4282). The $1.3 million amount on pages 34-35 of the PSC's brief was incurred by September 30, 2017, prior to any of the three sets of hearings in these cases. (L.F. Vol 12, p. at 4277 & n.159). The total rate case expense came to roughly two million dollars total for both cases, so the actual sharing percentage was closer to 40%, if one includes the non-litigation expenses that Spire is required by the PSC to incur to perform a depreciation study and send customers individual notices of public hearings.

The RSM is Mutually Beneficial and was Approved in Concept

The RSM is an adjustment device that provides for customers to receive refunds after they incur high charges in unusually cold winters, and to be surcharged when they have underpaid expenses in unusually warm winters. (Exs. Vol. 5, pp. 1037-38). Although the evidence clearly showed that the RSM is a tool that reduces risks and provides benefits for both the utility and its customers, the PSC characterized it as only a shareholder-focused tool that insulates shareholders from risk. (L.F. Vol. 12, pp. 4279, 4283). The PSC used this characterization to justify assigning rate case expense to Spire, even though the characterization is untrue, and even though the PSC found the proposal to have enough merit that it actually *approved* a form of an RSM tariff known as a Weather Normalization Adjustment Rider (WNAR). (L.F. Vol. 12, pp. 4311, 4315). Such a characterization is even more specious given the fact that the General Assembly has explicitly authorized the PSC to approve customer usage adjustment mechanisms that will provide the utility no more and no less than "a sufficient opportunity to earn a fair return on equity." §386.266.5(1), RSMo. The General Assembly further instructed the PSC to "take into account any change in business risk . . . in setting the corporation's allowed return" in a rate case. §386.266.8, RSMo. Hence, the PSC's assertion that Spire's proposed RSM was designed to reduce Spire's risk or provide a financial benefit to Spire at the expense of its customers is simply incorrect. In its brief, the PSC ignores Spire's points and merely restates its findings, as if neither Spire nor the Court is entitled to an explanation. (PSC Br., p. 32).

<u>Spire's Proposed ROE was Reasonable and Litigation Expense was Inevitable</u>

In the Amended Order, the PSC was critical of Spire's proposed ROE of 10.35%. (L.F. Vol. 12, pp. 4279, 4283). In its Appellant's brief, Spire pointed to evidence showing that the 10.35% proposal was as close or closer than the other parties to the final ordered ROE of 9.8%. In response, the PSC brief does not address the evidence, but only repeats its findings, consistent with its approach that the Court should not apply the required standard and look at the whole record. (*See* PSC Br., pp. 31-33; 36-37). Instead, the PSC declares its decision lawful and reasonable based on its citation to only selectively curated record evidence. (*Id*. at 33). The PSC's claim that a proposed ROE of 10.35% is egregious is simply not supported by the competent and substantial evidence on the record. And once again, this statement establishes no nexus between Spire's request for a higher ROE than that approved by the PSC and the amount of rate case expense incurred. Because Spire had to submit ROE testimony in any event, and because neither the 10.35% requested by Spire nor the 9.8% approved by the PSC were deemed acceptable by the other parties,[6] Spire had to litigate this issue no matter what. Given these circumstances, any suggestion that there were additional litigation costs because Spire initially proposed a slightly higher ROE is completely unsupported. The denial of rate case expense threatens the necessary give and take on these vital matters that the legislature intended.

[6] Witnesses for the other parties advocated ROEs of 9.20%-9.25%. (L.F. Vol. 12, pp. 3871, 4258-59).

<u>Spire's Earning-Based Incentive Compensation Proposal was Mutually Beneficial</u>

The evidence showed that Spire proposed earnings-based incentive compensation as a win-win for the utility and its customers, because if Spire could share in increased earnings, it is motivated to lower costs and increase revenues, either of which can lengthen the time between rate cases or reduce the amount of a future rate increase. (Exs. Vol. 19, pp. 2893-94). In effect, customers would be incentivizing the utility just like management incentivizes employees. The PSC's criticism of this proposal was flawed for two reasons. First, since this issue was handled entirely by in-house staff, there was absolutely no rate case expense associated with this proposal. (Exs. Vol. 19, pp. 2887-89; Tr. Vol. 3, pp. 2754-55).[7] Second, the PSC misrepresented the status of earnings-based incentive compensation in the Amended Order, so it could use the issue to justify rate case expense sharing. Although earnings-based incentive compensation is considered politically controversial, its practical merit is obvious. In its most recent decision on the subject, in 2009, the PSC actually *approved* a form of earnings-based incentive compensation. ***In re of Union Elec. Co., d/b/a AmerenUE's Tariffs to Increase Its Annual Revenues for Elec. Serv.***, 271 P.U.R.4th 475, No. ER-2008-0318 (Jan. 27, 2009); (Exs. Vol. 44, pp. 7029, 7119-7121). The PSC failed to mention this fact in finding that "earnings-based incentive compensation . . . has been consistently denied" by the PSC. (L.F. Vol. 12, p. 4283). The courts should not be required to defer to the PSC when it makes such misrepresentations.

[7] Both witness Mispagel and counsel Zucker were Spire employees.

The competent and substantial evidence on the whole record does not justify the PSC's false claim that this issue benefits only shareholders.

<u>Spire Did Not Pad Its Revenue Requirement</u>

With respect to the alleged padding of revenue requirement, Spire went to great lengths in its Appellant's brief to show how the PSC misrepresented the record. Spire will not belabor the point, other than to note in its long experience with such cases every party, including the PSC Staff and OPC, has routinely proposed more aggressive positions than what they will settle for, or what the PSC will approve. The PSC's focus on this routine and nearly universal feature of the litigation process provides no justification for reducing Spire's ability to recover its rate case expense, while, as discussed below, Staff and OPC recover all of their expenses through Spire and without any prudence review.

More examples exist. Spire proposed performance metrics, under which Spire could earn credits for meeting certain criteria above and beyond normal utility performance and could suffer losses if it failed to meet certain minimum standards. (Exs. Vol. 5, pp. 1044-47, 1113-15). Again, this issue was handled entirely by in-house staff; there were no rate case expense. (Tr. Vol. 2, pp. 687-88). This proposal is another example of forward-thinking incentive management. The PSC characterized it as an expense that does not benefit customers. (L.F. Vol. 12, pp. 4279-80). Given the two-way nature of the proposal, such a characterization is patently false and does not make sense as a reason to force Spire to absorb rate case operating expenses. The PSC disallows rate case expense because it deems the rate case process adversarial, while at the same time misrepresenting Spire's cooperative, win-win proposals to justify the disallowance. The Court should be able to look behind the curtain far enough to consider whether the PSC's decision to punish Spire for thoughtful and creative business solutions is arbitrary and capricious, or is an abuse of discretion.

The PSC also determined that disallowing half of Spire's rate case expense would lead to cost containment. This kind of flawed reasoning should be a red flag for the courts. A cost containment incentive does not justify disallowing an otherwise prudent operating expense. Using that criteria, the PSC could disallow a portion of any expense as a "cost containment incentive."

The PSC also determined that requiring all rate case expense to be paid by ratepayers provides the utility with an inequitable financial advantage over other case participants. This is a particularly tortured argument given the reality that Spire and other utilities already pay 100% of the litigation expenses of the PSC Staff and the OPC through assessments levied by the PSC. *See* §386.370, RSMo.; ***In re the Assessment Against the Pub. Util. in the State of Mo. for the Expenses of the Comm'n for the Fiscal Year Commencing July 1, 2018***, No. AO-2018-0379, 2018 WL 3208896 (June 20, 2018). The PSC Staff and OPC are the utilities' primary opponents in a rate case. As a consequence, under the PSC's treatment of rate case expense, Spire is required to pay all of the litigation expenses of these opponents, who are not subject to a prudence standard, while absorbing a significant portion of its own litigation expense for countering their claims in the ratemaking process.[8] Given this circumstance, the Amended Order's finding that recovery of prudent rate case expense affords Spire an inequitable financial advantage is arbitrary and capricious, and an abuse of the PSC's discretion.

The PSC sets a dangerous precedent by finding that utilities should share expenses that benefit both utilities and customers. Natural gas utilities provide gas service to customers, who pay for the costs of the service. Utility shareholders do not share in the benefits provided by natural gas, nor should such shareholders assume a share of the prudent costs to provide such service. The Court should draw a line that prohibits the PSC from requiring shareholders to absorb prudent utility operating expenses.

<u>Retroactive Ratemaking (Forest Park Property Sale)</u>

Point III: The Amended Report and Order's use of $3.6 million in relocation proceeds, which Spire received in connection with the sale of its Forest Park facility, to reduce current and future rates is unlawful retroactive ratemaking. (Replies to Respondent's Point 3)

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[8] In fact, the PSC's assessment billed to Spire in 2018 to pay for Staff and OPC litigation expenses significantly exceeded the amounts embedded in base rates in the rate case. The PSC denied Spire's request to defer such excess amount, conclusively demonstrating that no financial advantage favors the utility. *See* ***In re the Application of Spire Mo. Inc. for an Accounting Auth. Order Concerning its Comm'n Assessment for the 2019 Fiscal Year***, No. GU-2019-0011, 2019 WL 1354074 (Mar. 20, 2019).

At the outset, it should be noted that much of the PSC's argument in this section is irrelevant, because it addresses an issue Spire did not pursue at the Southern District and is not pursuing in this Court. As the PSC noted in its brief, after Spire sold the Forest Park property in 2014, the property still had $1.8 million in undepreciated book value, on which customers would still be paying. (L.F. Vol. 12, p. 4251). In the Amended Order, the PSC directed that Spire apply a credit to its assets of $1.8 million to relieve customers of paying for those costs. Although that is not the usual and proper accounting treatment, Spire opted not to challenge that part of the Amended Order. Hence, the PSC's arguments on that point are not only irrelevant but confuse the issue and obfuscate the PSC's unlawful treatment of relocation proceeds. (PSC Br., pp. 41-45)

The Forest Park property was sold in 2014. As part of the sale, Spire received $5.7 million in relocation proceeds. The relocation proceeds were all spent on the various costs incurred in Spire's reorganization of its work locations. These costs were all credited against the proceeds, so none of these costs hit Spire's books as expenses, either in the test year or in the rate case. In other words, customer rates included none of the furniture purchased nor the expenses covered by these proceeds. The PSC gave Spire credit for about $2.1 million that was spent on furniture and costs specific to the move from Forest Park. It used the remaining $3.6 million to reduce Spire's rate base, specifically the rate base for the Manchester Road facility. (L.F. Vol. 12, p. 4255).

The rate case test year was calendar year 2016, updated through September 2017. The rate case was filed in April 2017, and was decided in March 2018, with new rates going into effect on April 19, 2018.

The PSC tries in vain to demonstrate that its use of relocation proceeds received in 2014 to reduce rates in 2018 was not retroactive ratemaking. First, the PSC tries to claim that retroactive ratemaking is only tied to previous *rates* and not to other sources of income that Spire received in the past. (PSC Br., p. 39). For this to be true, the Court would have to find that the PSC can use any money the utility received in the past to reduce future rates, so long as that money did not emanate from past rates. For example, §393.140(12), RSMo. authorizes utilities to engage in a separate business not regulated by the Commission. Certainly, it would be confiscatory for the PSC to use profits derived from such a business to reduce rates in the utility's next rate case. This concept is so clearly confiscatory that no previous Commission has dared do it, and the PSC can cite to no case on point. Moreover, it would be impossible in this case to separate the $3.6 million in relocation proceeds from other revenues derived from rates, since the $3.6 million was spent on various reorganization-related items.

The PSC cites ***State ex rel. GTE North v. Mo. Pub. Serv. Comm'n***, 835 S.W.2d 356, 368 (Mo. App. W.D. 1992) for the proposition that normalization adjustments are made in rate cases to eliminate non-recurring items of expenses or revenues. (PSC Br., p. 40). However, in the Amended Order, the PSC itself violated the normalization rule; it not only adjusted Spire's rate by using a non-recurring revenue item (the relocation proceeds), but it did so with a revenue received two years before the test year. There is simply no way to portray this as something other than retroactive ratemaking.

The PSC then cites ***GTE North*** as relevant case law supporting adjustments for events occurring outside the test year, but overlooks that ***GTE North*** dealt with adjustments based on *post*-test year events. (*Id.* (citing ***GTE North***, 835 S.W.2d at 368)). The relevant part states: "Adjustments are also made for events occurring outside the test year. The criteria used to determine whether a post-year event should be included in the analysis of the test year is whether the proposed adjustment is (1) 'known and measurable,' (2) promotes the proper relationship of investment, revenues and expenses, and (3) is representative of the conditions anticipated during the time the rates will be in effect." ***GTE North***, 835 S.W.2d at 368. These three criteria are all based on a forward-looking time frame, not a backward-looking time frame. The PSC's attempt to use the ***GTE North*** criteria to justify retroactive ratemaking fails and should be rejected.

The PSC tries to rely upon ***GTE North*** for a principle for which it is not intended: to look backward in order to grab past revenues and use them to reduce current and future rates. That the "known and measurable" test is forward looking is apparent from the fact that the past is always known and measurable, so no such test would be needed. The PSC would also fail to meet the second criteria, because reducing Spire's rates going forward based on $3.6 million in relocation proceeds that were received and spent in the past, in no way promotes the proper relationship of investment, revenues and expenses.

Finally, the PSC fails the third test, as reducing Spire's assets by $3.6 million from relocation proceeds received and spent prior to the test year is not representative of the conditions anticipated during 2018-2020, when the rates will be in effect, given the one-time nature of the sale of an 85-year-old property.

PSC's Unreasonable Reliance on Manchester Facility Capital Cost

The PSC also argues that retroactive ratemaking is justified because the Manchester facility, built in late 2016, has a higher capital cost than Forest Park, which was built with 1935 pricing. Yet, the PSC admitted that the undisputed evidence establishes that the Manchester facility has lower operating expenses and is more cost efficient to operate than the Forest Park facility. (L.F. Vol. 12, p. 4250). The record as a whole demonstrates that the Manchester property saved customer's money compared to the Forest Park facility. (Exs. Vol. 17, pp. 2574-75). Regardless, the Manchester facility's capital cost is a red herring, because nothing in this cost comparison justifies retroactive ratemaking – that is, using past revenues to reduce current and future rates.

The PSC's statement of facts recites from its order that "Spire East did not seek Commission authorization prior to the sale of the Forest Park property. (LF 4252)."[9] PSC's statements of facts continues: "[a]t the time of the sale, the Forest Park property was necessary and useful to the provision of utility service. (LF 4252)"; "The Forest Park property was necessary for the provision of utility service. (LF 4254)"; "Spire East had to continue using the Forest Park buildings after the sale, and it was necessary to replace a portion of the Forest Park facilities with the more expensive Manchester Avenue facilities. (LF 4255)." (PSC Br., pp. 17-19).

[9] Spire explicitly notified the PSC of the sale in a public presentation in 2014. (Conf. Exs. Vol. 3, p. 471).

All of the statements above are findings that point toward an alleged violation of §393.190, RSMo. Nevertheless, in its argument, the PSC would have this Court believe that "there is nothing in the amended order to indicate that the reasons that the Commission enumerated for [using the relocation proceeds to reduce the Manchester asset] were punitive or retaliatory." (*Id.* at 46). Given the PSC's findings this is simply not a credible statement. The PSC used retroactive ratemaking to punish Spire while denying it the due process of notice, a complaint or a hearing. The PSC's decision should be reversed.

<u>The Prepaid Pension Asset</u>

Point IV: The Amended Report and Order's denial of the entire $28.8 million of Spire East's pension asset was arbitrary, unreasonable and unsupported by competent and substantial evidence on the whole record, because it directly conflicted with clear record evidence endorsed by the PSC demonstrating that a pension asset accrued as a result of the rates set in Spire East's 1990 and 1994 rate cases. (Replies to Respondent's Point 4)

The PSC's position on this issue would preclude a meaningful review of PSC decisions so long as those decisions are based on witness credibility. In the present case, the PSC asserts non-existent credibility issues to justify findings that have no basis in record evidence. The background on the argument between Spire and the PSC Staff is laid out in Appellant's initial brief on pages 67-71. As stated therein, Spire East's prepaid pension asset represents the difference between cash spent by Spire East to fund its pension versus the amount of pension expense Spire East charged to customers in rates. (L.F. Vol. 12, p. 4324; Supp. Exs., p. 5; Exs. Vol. 21, part 2 p. 3260; Tr. Vol. 3, p. 2074).

Since the amount of cash Spire East paid into its pension is well known, the issue in dispute is how much customers paid in rates for pension expense between 1990 and 1996. (L.F. Vol. 12, p. 4325). Customer rates were either based on Spire's annual cash contributions (the "cash method"), or on an accrual accounting method (the "accrual method") dictated by Financial Accounting Standards 87 and 88 ("FAS 87" and "FAS 88"). If customer rates were based on the cash method, no asset or liability would have accrued since the cash method matches Spire's cash contribution basis. However, if customer rates were based on the accrual method, an asset or liability accrues for the difference between customer rates and Spire's cash contributions.

The issue in this case arose out of the 1990, 1992 and 1994 rate cases. Spire asserted that a $28.8 million pension asset accrued from the rates in those cases. The PSC Staff disagreed. The matter was deferred for many years, but finally came to a head and was decided in the Amended Order.

The disagreement stems from the fact that in the early 1990s, Spire's cash contributions to its pension began to outpace the amount of pension expense calculated under the accrual method. Spire argued that customer rates in the 1990, 1992 and 1994 rate cases were all based on the accrual method, which resulted in a pension asset to account for the gap between the higher cash contributions made by the Company and the lower accrual method pension expense paid by customers.

The PSC Staff argued that customer rates in the 1990 and 1992 rate cases were based on the cash method, not the accrual method, so no asset accrued between 1990 and 1994. The Staff agreed that rates from the 1994 rate case were based on FAS 87 accruals, but argued that FAS 88 gains were not used to reduce pension expense until Spire East's 1996 rate case. Staff disputed Spire East's claim that a $9.0 million asset arose between 1994 and 1996 under FAS 88.

So, the issue boils down to whether pension costs in customer rates for the 1990, 1992 and 1994 rate cases were based on the cash method or the accrual method. (L.F. Vol. 12, p. 4325). With respect to the 1990 rate case, both Spire East and Staff witnesses proposed rates based on the accrual method. (Exs. Vol. 17, p. 2591; Exs. Vol. 31, p. 4673-74). This could not be more clear.

However, the PSC decided that the testimony showed that "parties were using a cash contribution method, and not FAS 87 or FAS 88 accrual accounting prior to September 1, 1994," which was the effective date of rates in Spire East's 1994 rate case. (L.F. Vol. 12, p. 4331). The PSC's conclusion necessarily implies that customer rates in Spire's 1990 rate case were based on the cash method. The Amended Order gave no indication why pension expense in the 1990 case was not based on the accrual method, which would have justified a pension asset for the period of 1990-1992. The PSC failed to address the matter directly in the Amended Order, at the Southern District, or in its brief to this Court. (PSC Br., pp. 47-51).

With respect to the 1990 rate case, the PSC has nothing to support its arbitrary finding that Spire did not utilize the accrual method. Indeed, the PSC Staff witness in the 1990 rate case clearly states in his testimony that Staff based pension rates in the 1990 case on FAS 87. This is a textbook case of an agency decision that is simply not supported by the evidence on the whole record. The PSC has no competent and substantial evidence to support its finding regarding the 1990 rate case, and so it is left to simply repeat its conclusory statement that pension rates were based on cash contributions until 1994. (*Id.* at 50).

The PSC should not be permitted to portray a circumstance where the record evidence is clear as a credibility issue in order to shield its findings from judicial review. The PSC's main argument revolves around credibility. The PSC decided that it believed the witnesses who testified during the 1990s. (*Id.*; L.F. Vol. 12, p. 4331). The PSC correctly states that it is entitled to decide which witnesses it believes and which witnesses it does not believe. (PSC Br., pp. 47, 50). However, the PSC is not entitled to claim that it believes the witnesses from the 1990s, but then ignore their evidence when it conflicts with the PSC's desired outcome, i.e., when the evidence demonstrates that 1990 rates were based on FAS 87. The competent and substantial evidence on the whole record clearly shows that 1990 rates were based on accrual accounting.

The PSC is also not entitled to find that 1992 rates were based on cash contributions because both parties filed their cases on the cash method, and then, without explanation, refuse to apply that same criteria to the 1990 case, where both parties filed on the accrual method. It is classic arbitrary and capricious behavior for the PSC to do so, and this Court should not condone it.

Finally, the PSC states that Spire did not itemize a pension asset in the 1990, 1992 and 1994 rate cases. (*Id.* at 49; L.F. Vol. 12, p. 4326). Of course, all the citations in the PSC Brief are to the PSC's Amended Order. Spire did not itemize a pension asset in 1990, because no pension asset existed at the time of that rate case. The pension asset was formed by the use of FAS 87 accrual accounting to set pension rates in the 1990 rate case. The PSC's finding that Spire did not itemize a pension asset in the 1994 case is again contrary to the evidence. The undisputed evidence in the form of a schedule from the 1994 case lists a "Prepaid Pension Asset." (Exs. Vol. 20, p. 3086). Without a court to review that evidence, the PSC can say anything it wants without fear of contradiction.

CONCLUSION

Spire requests that, pursuant to §386.510, RSMo., the Court set aside and reverse the Amended Order on the issues argued herein and remand these matters to the PSC. Pursuant to §386.520.2(1) and (3), Spire further requests that the Court instruct the PSC, on remand, to provide temporary rate adjustments consistent with the Reconciliation approved by the PSC on April 25, 2018, for the Forest Park Relocation Proceeds and the Rate Case Expense Sharing. With respect to the Prepaid Pension Asset Disallowance, Spire requests that the Court instruct the PSC, on remand, to confirm the amount of the Company's regulatory pension asset consistent with the Court's decision and, pursuant to §386.520.2(3), to approve a temporary rate adjustment designed to allow Spire to recover from its customers the amounts it should have collected in rates for a return on that asset, beginning on April 19, 2018.

Dated: December 5, 2019

Respectfully submitted,

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CERTIFICATE OF COMPLIANCE WITH MISSOURI SUPREME COURT RULES 55.03 AND 84.06

This brief complies with the requirements of Rule 55.03. This brief complies with the type-volume limitations of Missouri Supreme Court Rule 84.06 because this brief contains 7,510 words, excluding parts of the brief exempted by Rule 84.06(b). This brief complies with the typeface and the type style requirements of Rule 84.06 because this brief has been prepared in a proportionally styled typeface using Microsoft Word in 13-point font size and Times New Roman type style.

CERTIFICATE OF SERVICE

I hereby certify that on December 5, 2019, a true and correct copy of the foregoing brief was served via the Court's electronic filing system to all counsel of record.

/s/ Jeremiah W. (Jay) Nixon