No. SC94470

In the

Supreme Court of Missouri

OFFICE OF THE PUBLIC COUNSEL,

Appellant,

v.

PUBLIC SERVICE COMMISSION,

Respondent.

Appeal from the
Missouri Public Service Commission

SUBSTITUTE BRIEF OF APPELLANT OFFICE OF THE PUBLIC COUNSEL

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JURISDICTIONAL STATEMENT

The Office of the Public Counsel ("OPC" or "Public Counsel") is a state agency which represents utility ratepayers. § 386.710, RSMo Supp. 2013.[1] OPC challenges the lawfulness and reasonableness of the October 16, 2013, Report and Order of the Missouri Public Service Commission ("Commission" or "PSC") issued in PSC Case No. GO-2014-0006.[2] This review is brought pursuant to §§ 386.510 and 386.540.

After the Western District of the Court of Appeals issued its opinion affirming the Commission's Report and Order, OPC moved the Court either to rehear the matter or transfer it to this Court. The Western District Court of Appeals denied both motions.

On September 17, 2014, OPC sought transfer pursuant to Rule 83.04 of the Missouri Supreme Court Rules. On November 25, 2014, this Court granted transfer.

STATEMENT OF FACTS

On July 2, 2013, Liberty Energy (Midstates) Corp. d/b/a Liberty Utilities ("Liberty") filed an application with the PSC requesting an increase to its Infrastructure System Replacement Surcharge (ISRS) for eligible infrastructure costs incurred between June 1, 2012, and May 31, 2013 (Legal File (L.F.) at p. 4). The ISRS is a surcharge, separate and in addition to general rates, that gas companies are authorized to establish and periodically raise outside of a general rate review for the purpose of recovering costs

[1] All statutory references are to RSMo Supp. 2013.

[2] *See* Appendix for a copy of the Report and Order.

incurred complying with certain government-mandated infrastructure replacements, improvements, and relocations. §§ 393.1009, 393.1012 and 393.1015.

Public Counsel opposed Liberty's proposal to include in the ISRS costs incurred replacing infrastructure that was damaged or destroyed due to human conduct or other reason, and argued that such costs do not satisfy the ISRS eligibility requirements for pipeline replacement costs (L.F. p. 197, 305).

The PSC's October 16, 2013 Report and Order approved Liberty's ISRS increase, and included costs incurred replacing and repairing damaged and destroyed facilities (L.F. p. 250). The PSC concluded that replacements of such facilities are eligible ISRS costs as replacements of pipeline system components that are "worn out or are in deteriorated condition" under § 393.1009(5)(a) (L.F. p. 250).

A. Background

The events giving rise to the ISRS statutes began between 1987 and 1989 when a series of natural gas explosions in Missouri raised concerns over the safety of Missouri's aging gas distribution infrastructure (Transcript (Tr.) pp.6-7). These included a gas leak that ignited an office building and adjacent buildings in Jefferson City, and tragic accidents in Kansas City, Fulton, and Oak Grove, including the deaths of an elderly couple in Oak Grove. *Id.* In 1988 alone, "the number of breaks in cast iron mains nearly doubled from 38 to 70." *The Staff of the Public Service Commission v. The Kansas Power and Light Company;* 30 Mo. P.S.C. (N.S.) 123 (1990).

According to Liberty, "These accidents resulted in unprecedented actions by [the] Commission, including the promulgation of an emergency rule requiring all natural gas

companies in Missouri to conduct emergency leak surveys over all steel service lines and yard lines not protected against corrosion and to make immediate and necessary repairs." (Tr. pp. 6-7). The PSC's "summary and analysis of the results of its emergency leak survey" supported the "need for a more stringent gas safety program." Mo. Reg., Vol.14, No. 23, p. 1583 (December 1, 1989).[3] "Over fifty percent (50%) of all leaks found in the emergency survey…were classified as hazardous or potentially hazardous" and "[o]ver eight hundred (800) hazardous or potentially hazardous leaks which could have caused explosions or fires" were detected. *Id.*

In response to this problem of an aging and unprotected infrastructure, the PSC promulgated rules in 1989 requiring Missouri's regulated gas companies to establish long-term facility replacement programs for the systematic inspection and replacement of unsafe facilities, such as cast iron lines and unprotected steel lines. 4 CSR 240-40.030(15); Mo. Reg., Vol.14, No. 23, p. 1581-1602 (December 1, 1989). The PSC's rules, titled "Replacement Programs," required gas companies to file: (1) leak detection and replacements programs for unprotected steel service lines and yard lines; (2) programs to replace cast iron pipe; and (3) programs to identify and cathodically protect or replace unprotected steel transmission lines, feeder lines and mains. 4 CSR 240-40.030(15)(C), (D), and (E). These rules addressed problems associated with corrosion that occurs on cast iron and unprotected steel lines and mains over time. The PSC's Order of Rulemaking concluded that "the number of natural gas incidents in the last

[3] *See* Appendix for a copy of the Order of Rulemaking.

heating season indicates a need for expedited action on the part of the commission." Mo. Reg., Vol.14, No. 23, p. 1583 (December 1, 1989). The PSC's Order of Rulemaking also concluded, "the commission finds that unprotected steel is, by its very nature, subject to corrosion over time." *Id.*, p. 1598. Accordingly, the "programs are to provide for cathodic protection or replacement" of steel lines, and "if necessary, the eventual replacement of unsafe cast iron piping." *Id.*

Missouri's largest gas utilities at the time included Associated Natural Gas, Laclede Gas Company ("Laclede") and Union Electric Company, and all three opposed the proposed rules. *Id.*, pp. 1581-1602. They argued that the rules would be too costly. *Id.* Laclede argued that it was already "systematically replacing bare, unprotected steel mains and services since the early 1950s," and the new rules would "result in additional capital expenditures of up to thirty million dollars ($30,000,000) per year and increased operating costs by eight million dollars ($8,000,000) to ten million dollars ($10,000,000)" for a total estimate of up to forty million dollars ($40,000,000) per year. *Id.*, pp. 1581-1582. Laclede characterized this amount as "more than Laclede's total past level of construction costs for all purposes." *Id.*, p. 1582. Despite these objections, the PSC adopted the rules and in its Order of Rulemaking explained that recent "natural gas explosions, ignitions and fires which occurred in the past heating season" were the reasons for the rules. *Id.*

The new rules became effective on December 15, 1989. *Id.*, p. 1581. Following the rules, gas companies filed replacement programs for PSC approval. For example, in the main replacement program approved for Union Electric Company, the PSC explained

that the parameters considered to rate the pipe being evaluated were: "a. Age; b. Working pressure; c. Total number of leaks in the section; d. Leak history in the most recent two years; e. Type of material; and f. Diameter." *In the Matter of the Review and Approval of the Cast Iron Main and Unprotected Steel Main Programs for Union Electric Company,* 1993 Mo. PSC LEXIS 74 (1993). The PSC made no mention of damaged or destroyed pipe as a parameter for inclusion in the program. *Id.*

As predicted, the replacement programs caused the gas companies to incur substantial costs between rate cases that they were unable to recoup from ratepayers until rates were reset in the next general rate review. *In the Matter of Missouri Gas Energy's Tariff Sheets Designed to Increase Rates for Gas Service in the Company's Missouri Service Area.; In the Matter of Missouri Gas Energy's Proposed Modifications to its Facilities Extension Policy,* 7 Mo. P.S.C. 3d 394 (1998); *See also, In the Matter of the Application of Missouri Public Service for the Issuance of an Accounting Authority Order Relating to its Gas Operations,* 1 Mo. P.S.C. 3d 220 (1992), wherein the PSC stated, "Company states that its accelerated compliance with the Commission's gas safety rule and order has caused Company to incur out-of-period gas line replacement and carrying cost expenses."

To help the utility address this regulatory lag issue, the PSC authorized gas companies to utilize an Accounting Authority Order ("AAO") to defer program compliance costs to a later period when the deferred amounts would be included in rates following a general rate review. *Id.* In a case where Laclede Gas Company sought an AAO for replacement costs, the PSC stated:

> **Gas Safety AAO**: The parties agree that Laclede should be granted accounting authorization to continue to defer and book to Account 182.3 costs incurred to comply with the Commission's gas safety requirements including costs: (1) to replace Company service and yard lines and to move and reset and/or replace meters; (2) to replace cast iron mains and transfer services from the old main to the new main; (3) to replace and/or cathodically protect unprotected steel mains and transfer services from the old main to the new main; and, (4) to survey buried fuel lines for leaks. The costs described above will be incurred in order to comply with Commission regulations. They constitute substantial costs that will be nonrecurring. The Commission finds it is reasonable to defer the costs by means of an AAO.

In the matter of Laclede Gas Company's Proposed Tariff Sheets Designed to Increase Rates For Gas Service Provided to Customers in the Missouri Service Area of the Company, and the Company's Proposed Experimental Incentive Ratemaking Plan, 5 Mo. P.S.C. 3d 108 (1996).

In another case where Missouri Gas Energy (MGE) sought an AAO for mandated replacement costs, the PSC explained:

> This issue relates to the costs that MGE incurs by deferring the costs of improvements that MGE has made through its safety line replacement program (SLRP) by replacing mains and services lines pursuant to Commission Rule 4 CSR 240-40.030 (1995). The carrying costs of construction could be recovered immediately through a price increase if the

> Company were not a regulated industry required to obtain the approval of the Commission prior to any increase in rates. The Commission established the use of the accounting authority order (AAO) to allow MGE to book, in addition to the actual costs of the improvements, the carrying costs of those investments until the next rate case is filed with the Commission. The AAO has no guaranteed ratemaking treatment. The company is required to request ratemaking treatment of the amounts booked under the AAO in the next rate case the Company files. Under certain circumstances, companies regulated by the Commission are allowed to suspend normal accounting procedures through the use of an AAO.
>
> …
>
> These SLRP related costs have been considered "extraordinary items" since the gas safety rules issued by the Commission have required the companies to replace main and service lines within their service areas. As the majority of the SLRP project is almost complete, the Commission finds that MGE's position is just and reasonable and there is competent and substantial evidence to support MGE's request for an AAO. The Commission shall issue an AAO authorizing MGE to defer and book costs relating to SLRP deferral carrying costs, property taxes and depreciation expenses.

In the Matter of Missouri Gas Energy's Tariff Sheets Designed to Increase Rates for Gas Service in the Company's Missouri Service Area.; In the Matter of Missouri Gas Energy's

Proposed Modifications to its Facilities Extension Policy, 7 Mo. P.S.C. 3d 394 (1998). Accordingly, the replacement program costs were allowed to be deferred for recovery in a future rate case because they were considered *extraordinary* items.

In 2002, a year before the ISRS statutes were enacted, the PSC approved an AAO for Laclede Gas Company that was limited to replacement costs only:

> Laclede will be permitted to defer certain expenses related to the Commission-mandated replacement of plant, including: the replacement of unprotected, bare steel service and yard lines and the associated resetting of meters; the replacement or protection of steel mains and the associated transfer of services from old mains to new mains; the replacement of cast iron mains and associated transfer of services; and the replacement, renewal or relaying of direct buried copper service lines.

In the Matter of Laclede Gas Company's Tariff to Revise Natural Gas Rate Schedules, 11 Mo. P.S.C. 3d 538 (2002). Accordingly, under the AAO deferral mechanism used immediately prior to the ISRS statutes, the gas utilities did not receive PSC authorization to defer costs incurred repairing or replacing pipe destroyed due to human conduct. *Id.* The AAO deferrals were specifically limited to costs incurred complying with the company's replacement programs, that is, the replacement or cathodic protection of unprotected steel, the replacement of cast iron pipe if necessary, and the replacement, renewal or relaying of direct buried copper service lines. *Id.*

Until the ISRS statutes, the AAO was the method used to address the regulatory lag that existed between when the utility incurred costs complying with the PSC-

mandated line replacement programs and when the utility began recovering program costs in rates. The AAOs addressed this regulatory lag by authorizing the gas utilities to defer amortization to the next rate case to allow the full cost of the replacement to be recovered through rates. But the AAOs did not address the timing issue of the lag that existed between when the utility incurred the costs and when it recovered those costs in rates following a general rate case review. Nor could it, because without express legislative authority, an immediate rate increase to recover just these costs would have been unlawful under § 393.270, which prohibits single-issue ratemaking, that is, raising rates between rate cases to address a single cost category without considering all costs. *State ex rel. Utility Consumers Council of Missouri, Inc. v. P.S.C.*, 585 S.W.2d 41, 56 (Mo. banc 1979) (*UCC*).

Both the regulatory lag issue and the single-issue ratemaking issue were addressed by the ISRS statutes, which "permit the gas company to make single-issue rate increases between general rate cases in order to timely recover its costs for certain government-mandated infrastructure projects without the time and expense required to prepare and file a general rate case." *Office of the Public Counsel v. P.S.C.*, 417 S.W.3d 815, 821 (Mo. App. W.D. 2014).

The ISRS statutes attempted to resolve the problems created by the combination of the material of pipe (steel, cast iron, and copper), and corrosion that occurs on these materials underground over time. As explained above, the PSC concluded that the replacement programs addressed infrastructure that was subject to "corrosion over time."

Mo. Reg., Vol.14, No. 23, p. 1598 (December 1, 1989). Liberty Utilities itself referred to the ISRS as addressing the problem of an "aging infrastructure" (Tr. pp.6-7).

The ISRS statute replaced the AAO as a cost recovery mechanism and permitted quicker recovery of these replacement program costs by providing for an exception to the prohibition against single-issue ratemaking. Following the enactment of the ISRS statutes, there are no PSC cases where a gas company sought an AAO to recover the plant investments mandated by 4 CSR 240-40.030(15).

B. Liberty's ISRS Petition

Liberty initiated the present case before the PSC on July 2, 2013, when Liberty requested authority from the PSC to increase its ISRS surcharge (L.F. p. 4). Liberty sought to increase the surcharge to generate a total annual incremental revenue increase of $650,670 (Tr. p.10). Public Counsel opposed the request on procedural and substantive grounds and requested an evidentiary hearing (L.F. p.59). The PSC held an evidentiary hearing on September 26, 2013 (Tr. pp.1-99).

During the evidentiary hearing, Liberty's President, Mr. David Swain, testified on behalf of the company's requested ISRS rate increase (Tr. p.35). Mr. Swain testified that Liberty's requested ISRS amount includes costs resulting from damage to Liberty's facilities caused by a contractor or other third party (Tr. pp.41-42). Mr. Swain further testified that Liberty included in its ISRS practically all costs incurred extending the life of the system and practically all costs "that deal with replacements" (Tr. p.45). Mr. Swain made no mention of the specific limitations imposed on eligible replacements by §

393.1009(5)(a), which authorizes only those existing facilities that are "worn out or are in deteriorated condition." *Id.*

The PSC approved the ISRS increase and concluded that "damaged" infrastructure is synonymous with "deteriorated" infrastructure, as that term is used in § 393.1009 (L.F. p.250). The Order further concluded, "A pipe damaged by a third party is in a deteriorated condition and, therefore, an eligible project because it has been lowered in quality, character, or value, although that deterioration has occurred quicker than what happens normally through the passage of time" (L.F. p.250).

Public Counsel filed its Application for Rehearing on October 24, 2014, wherein Public Counsel raised several points of error, including procedural rule violations and several substantive statute violations (L.F. p.305). Public Counsel's Application for Rehearing argued that the Report and Order was unlawful and unreasonable (L.F. p.305). The PSC denied Public Counsel's Application for Rehearing (L.F. p.329).

Public Counsel appealed the PSC's Order to the Court of Appeals for the Western District (L.F. p.353). Public Counsel argued that the PSC's Order was unlawful in that it violated §§ 393.1009, 393.1012 and 393.1015 by authorizing the ISRS to include costs incurred replacing infrastructure that was damaged or destroyed, and that was not incurred as a result of a state or federally mandated replacement program. *Liberty Energy (Midstates) Corp. v. Office of Pub. Counsel*, 2014 Mo. App. LEXIS 811 (Mo. App. W.D. July 29, 2014). The Court of Appeals affirmed the Order. *Id.*

STANDARD OF REVIEW

The standard of review applied by Courts reviewing a PSC decision under § 386.510, is a two-pronged analysis. *State ex rel. AG Processing, Inc. v. P.S.C.*, 120 S.W.3d 732, 734 (Mo. banc 2003). First, the Court must determine whether the PSC's order was lawful. *Id.* Second, the Court must determine whether the order is reasonable. *Id.* The lawfulness of an order is determined "by whether statutory authority for its issuance exists, and all legal issues are reviewed de novo." *Id.* In determining whether the PSC's order is lawful, the court must exercise "unrestricted, independent judgment" and "correct erroneous interpretations" of the law. *State ex rel. Riverside Pipeline Co., L.P. v. PSC of Mo.*, 215 S.W.3d 76, 84 (Mo. banc 2007). The reasonableness of the order is determined by whether the order is supported by competent and substantial evidence on the whole record, and whether the decision is arbitrary, capricious, or constitutes an abuse of the PSC's discretion. *State ex rel. Praxair, Inc. v. P.S.C.*, 344 S.W.3d 178, 184 (Mo. banc 2011). Additionally, the Court must review the PSC's decision in light of the fundamental principle that the purpose of public utility law is "to protect the consumer against the natural monopoly of a public utility, as provider of a public necessity." *UCC*, 585 S.W.2d at 56.

POINTS RELIED ON

POINT 1

THE PSC ERRED IN ITS ORDER APPROVING AN INCREASE TO LIBERTY UTILITIES' INFRASTRUCTURE SYSTEM REPLACEMENT SURCHARGE, BECAUSE THE ORDER IS UNLAWFUL AND UNREASONABLE AND SUBJECT TO REVIEW UNDER § 386.510, RSMO SUPP. 2013, IN THAT THE PSC AUTHORIZED LIBERTY TO INCLUDE EXPENSES IN THE SURCHARGE THAT ARE NOT AUTHORIZED BY §§ 393.1009, 393.1012 OR 393.1015, RSMO SUPP. 2013.

Authorities:

§ 393.1009, RSMo Supp. 2013.

§ 393.270, RSMo Supp. 2013.

Utility Consumers Council of Missouri, Inc. v. P.S.C., 585 S.W.2d 41 (Mo. banc 1979).

ARGUMENT

POINT 1

THE PSC ERRED IN ITS ORDER APPROVING AN INCREASE TO LIBERTY UTILITIES' INFRASTRUCTURE SYSTEM REPLACEMENT SURCHARGE, BECAUSE THE ORDER IS UNLAWFUL AND UNREASONABLE AND SUBJECT TO REVIEW UNDER § 386.510, RSMO SUPP. 2013, IN THAT THE PSC AUTHORIZED LIBERTY TO INCLUDE EXPENSES IN THE SURCHARGE THAT ARE NOT AUTHORIZED BY §§ 393.1009, 393.1012 OR 393.1015, RSMO SUPP. 2013.

The PSC's Order should be reversed and the case remanded back to the PSC because the Order unlawfully misinterprets and misapplies §§ 393.1009, 393.1012 and 393.1015, RSMo Supp. 2013, ("ISRS statutes") in that the Order authorizes Liberty to recover costs through the ISRS surcharge that are not authorized by law. Specifically, the Order authorizes Liberty to recover costs incurred replacing infrastructure regardless of whether the replacement was due to a rupture caused by human conduct, which is contrary to both the plain language of the ISRS statutes and the legislative intent behind the ISRS statutes.

Section 393.1012 authorizes gas companies to petition the PSC to establish or change an ISRS to "allow for the adjustment of the gas corporation's rates and charges to provide for the recovery of costs for eligible infrastructure system replacements." *Eligible* infrastructure replacements are defined as "gas utility plant projects that: (a) Do

not increase revenues by directly connecting the infrastructure replacement to new customers; (b) Are in service and used and useful; (c) Were not included in the gas corporation's rate base in its most recent general rate case; and (d) Replace or extend the useful life of an existing infrastructure." § 393.1009.

What qualifies as a *gas utility plant project* is further limited to: (a) eligible replacements; (b) eligible projects that extend the useful life or enhance the integrity of the pipeline; and (c) eligible facility relocations. § 393.1009(5)(a)(b) and (c). The ISRS statutes limit eligible replacements under § 393.1009(5)(a) to the following:

> (a) Mains, valves, service lines, regulator stations, vaults, and other pipeline system components installed to comply with state or federal safety requirements as replacements for existing facilities that have worn out or are in deteriorated condition;

This case involves only the first category of gas utility plant projects – replacements, and Liberty's practice of including in its ISRS costs which exceed the scope of the statute, including pipeline damaged or destroyed by third party excavators or others, as would occur, for example, if a backhoe or drill ruptured a main line during excavation or boring activities.

A. PSC Interpretation is Inconsistent with the Plain and Ordinary Meaning of "Worn Out or are in Deteriorated Condition"

The key elements to eligibility for the ISRS under § 393.1009(5)(a) are that the replacement must be: (1) performed to comply with state or federal safety requirements, and (2) that the existing facilities that are being replaced must be "worn out or are in

deteriorated condition." § 393.1009(5)(a). A pipe that has been ruptured due to an accident, negligence or even through intentional harm to the facility, does not satisfy this second element of eligibility because such facilities are not "worn out" or "in deteriorated condition" as those terms are understood by their plain and ordinary meaning.

"When interpreting a statute, the primary goal is to give effect to legislative intent as reflected in the plain language of the statute." *State v. Moore*, 303 S.W.3d 515, 520 (Mo. banc 2010). The primary question presented by this case is whether infrastructure, such as a main line ruptured by way of an accident, satisfies the statutory limitation that ISRS-eligible replacements only include infrastructure that is "worn out or are in deteriorated condition." § 393.1009(5)(a).

The plain language of this phrase contemplates two separate qualifications for replacements: "worn out" facilities, or facilities that "are in deteriorated condition." Neither "worn out" or "deteriorated" is defined by the statute. "In the absence of a statutory definition, words will be given their plain and ordinary meaning as derived from the dictionary." *State ex rel. Mogas Pipeline LLC v. P.S.C.*, 366 S.W.3d 493, 498 (Mo. banc 2012).

The *American Heritage Dictionary* defines "deteriorate" as a transitive verb to mean, "To diminish or impair in quality, character, or value: *Time and neglect had deteriorated the property.*" *American Heritage Dictionary*, 494 (4th ed. 2009). As an intransitive verb, deteriorate is defined as, "To grow worse; degenerate: *The weather deteriorated overnight"*, and, "To weaken or disintegrate; decay: *The nation's highways are deteriorating at a rapid pace." Id.* These definitions and the sample sentences

provided for context all apply a meaning that does not contemplate an immediate event, as would occur if an excavation crew were to bore through a gas main. They all require a more gradual process.

These definitions are also consistent with the *Webster's* definition, which defines "deteriorate" as either, "to make inferior in quality or value: impair," or "to grow worse (*the weather had deteriorated during the night*)." *Webster's Third New International Dictionary*, 616 (3rd ed. 1993). *Webster's* also defines "deterioration" as "the action or process of deteriorating or state of having deteriorated; gradual impairment," which again suggests a gradual occurrence rather than a sudden event, as would happen if a main is ruptured during excavation. *Id.*

The *American Heritage Dictionary* defines "worn-out" as, "Worn or used until no longer usable or effective." *American Heritage Dictionary*, 1983 (4th ed. 2009). "Worn out," therefore, implies an infrastructure that has been rendered non-functional through wear, whereas "deteriorated" implies an infrastructure that may still be functional (it is not worn *out*), but is in a condition that weakens the integrity of the infrastructure and renders it unsafe. When gas infrastructure wears out or deteriorates, it does so due to forces of nature, usage, and time, whereas damaged or destroyed infrastructure typically occurs instantly as the result of human conduct or other event. This interpretation is consistent with *Black's Law Dictionary*, which defines "deterioration," "with respect to a commodity" as "a constitutional hurt or impairment, involving some degeneration in the substance of the thing, such as that arising from decay, corrosion, or disintegration." *Black's Law Dictionary*, 450 (6th ed. 1990).

In using the phrase "worn out or are in deteriorated condition," the legislature limits replacements eligible for the ISRS to infrastructure that over time has weakened and is potentially hazardous. This limitation eliminates from eligibility typical maintenance costs incurred replacing pipe for reasons other than the wear and deterioration that occurs due to age. Without the limiting phrase "worn out or are in deteriorated condition", *all* replacements would be eligible for the ISRS, regardless of the reason for the replacement or the condition of the pipe. The interpretation applied by the PSC below all but writes out that limiting phrase from the law.

This Court has affirmed the canon of construction that the express mention of one thing in a statute implies exclusion of another. *Harrison v. MFA Mut. Ins. Co,* 607 S.W.2d 137, 146 (Mo. banc 1980). In the context of the ISRS statutes, the express mention of "worn out or are in deteriorated condition" as being eligible infrastructure implies that the statute excludes all other infrastructure replacement from eligibility, including ruptures caused by human conduct or other events. Interpreting § 393.1009(5)(a) to allow facility replacements due to ruptures caused by human conduct or other events is, therefore, inconsistent with the plain and ordinary meaning of "worn out or are in deteriorated condition." Accordingly, the PSC erred when it authorized Liberty to include amounts in its ISRS that were incurred replacing infrastructure that was not worn out or in a deteriorated condition.

B. PSC Interpretation is Inconsistent with Legislative Intent

When the plain language of a statute does not answer a reasonable dispute as to its meaning, the statute is ambiguous. *Allen v. Cont'l Western Ins. Co*., 436 S.W.3d 548, 554

(Mo. banc 2014); *Derousse v. State Farm Mut. Auto. Ins. Co.*, 298 S.W.3d 891, 895 (Mo. banc 2009). The ISRS statute is not ambiguous because the plain and ordinary meaning of "worn out or are in deteriorated condition" does not include damaged or destroyed infrastructure associated with human conduct or other events. However, should this Court conclude that the ISRS language at issue here is subject to more than one conflicting interpretation and, therefore, ambiguous, the Court should resolve the ambiguity consistent with the intent of the legislature. *Reichert v. The Board of Education of the City of St. Louis*, 217 S.W.3d 301, 305 (Mo. banc 2007). This is accomplished through the application of the rules of statutory construction. *Id.*

"The seminal rule of statutory construction directs this Court to determine the true intent of the legislature, giving reasonable interpretation in light of the legislative objective." *Williams v. Nat'l Gas. Co.*, 132 S.W.3d 244, 249 (Mo. banc 2004). "All canons of statutory construction are subordinate to the requirement that the court ascertain and apply a statute in a manner consistent with the legislative intent." *Id.* In evaluating the intent of the legislature in enacting a law, consideration must be given to the "circumstances and the usages of the time." *Playboy Club, Inc. v. Myers*, 431 S.W.2d 228, 232 (Mo. 1968). That is to say, where there is ambiguity in the four corners of the law as written, intent should be gathered from the entirety, history and purpose of the statute. *Rust v. Missouri Dental Board*, 155 S.W.2d 80, 83 (Mo. 1941). In construing a statute to determine legislative intent, it is appropriate to consider its history, the presumption that the legislature had knowledge of the law, the surrounding

circumstances, and the purpose and object to be accomplished. *Person v. Scullin Steel Co.*, 523 S.W.2d 801, 803 (Mo. banc 1975).

The legislative intent with the ISRS statutes was to permit gas utilities to recoup expeditiously increased costs created by government-mandated replacement programs.[4] The replacement programs were an unprecedented response to an unprecedented problem. According to one gas company, the replacement programs resulted in the largest expense ever encountered by gas companies in Missouri. Mo. Reg., Vol.14, No. 23, p. 1582 (December 1, 1989). The focus of these unprecedented programs was and is to seek out existing safety issues that otherwise would not be remedied without the mandated replacements. There is nothing unprecedented about human conduct damaging or destroying gas pipe and the resulting need to replace that pipe. Gas utilities have been

[4] Liberty itself acknowledged this purpose during the evidentiary hearing when Liberty "set the stage for this matter" by discussing the natural gas accidents that occurred between 1987-1989, leading to the ISRS rules, which Liberty states were to "encourage the gas utilities to replace and maintain their aging infrastructure to protect against threats to public safety." (Tr. pp. 6-9). Liberty next states that "the purpose of the legislation is to address the single issue of relief for natural gas utilities from regulatory lag attributable to safety-related infrastructure investments." *Id.*

dealing with damaged and destroyed pipe since well before the PSC was established in 1913, and long before the ISRS statute was adopted in 2004.[5]

The purpose of the replacement programs was explained in the PSC's Order of Rulemaking where the PSC concluded that the replacement programs target the material used because of the tendency of steel to corrode, and cast iron to crack, as a result of the materials themselves and the *natural* pressures placed upon these materials due to their location within the ground. Mo. Reg., Vol. 14, No. 23, p. 1598 (December 1, 1989). This reading is also supported by Liberty's own recognition that the ISRS was to address a problem of an *aging infrastructure* (Tr. p.7). Replacing pipe destroyed due to human conduct or other force that was not the result of wear or deterioration is inconsistent with the ISRS statute because the costs incurred replacing damaged infrastructure were not incurred as the result of the government-mandated safety-related replacement programs.

To help the gas utilities with quicker recovery of their costs of complying with the mandated replacement programs, the PSC authorized an Accounting Authority Order (AAO) to allow the companies to defer program costs to the next general rate case. However, even with an AAO giving some assurance of cost recovery, it does not extinguish the regulatory lag. Accordingly, the General Assembly passed the ISRS statutes to enable gas companies to recoup their costs from customers more quickly. And

[5] For example, *Sedalia Gaslight Co. v. Mercer*, 48 Mo. App. 644, 648 (Mo. App. K.C. 1892) is an 1892 case that involved damages sustained to a gas main while a third party was digging a ditch to install a sewer system.

so, as a practical matter, the ISRS statutes replaced the AAO mechanism for recovering replacement program costs.[6]

There is nothing in the plain language of the ISRS statute to suggest that the ISRS was intended to do anything other than replace the AAO. Moreover, there is nothing from the history of the ISRS statutes to suggest that the legislature intended to expand or restrict in any way the scope of the costs that were eligible under the earlier recovery mechanism. And so, by replacing the AAO mechanism as the method of allowing gas utilities quicker recovery of costs incurred complying with government-mandated replacement programs, the legislature intended the ISRS to apply to the same types of replacements that were qualifying for deferral under the AAO – that is, only those costs

[6] While this Court has not specifically addressed the lawfulness of the AAO mechanism, the Western District of the Court of Appeals previously determined in a 1993 case that AAOs are lawful, and do not constitute a single-issue ratemaking violation of § 393.270. *State ex rel. Office of Pub. Counsel v. P.S.C.*, 858 S.W.2d 806, 812 (Mo. App. W.D. 1993). The use of the AAO as a cost-deferral mechanism was upheld by the Missouri Court of Appeals as not in violation of single-issue ratemaking because it addressed an extraordinary cost increase. *Id*. "Because rates are set to recover continuing operating expenses plus a reasonable return on investment, only an extraordinary event should be permitted to adjust the balance to permit costs to be deferred for consideration in a later period." *Id.* Public Counsel does not concede the ultimate lawfulness of AAOs, but it is not an issue in this appeal.

incurred complying with the replacement programs. *Person*, 523 S.W.2d at 803 (Mo. banc 1975) (*Stating*, knowledge of the law and surrounding circumstances are relevant to ascertain the legislator's intent).

"To discern legislative intent, the Court may…examine the whole act to discern its evident purpose, or consider the problem that the statute was enacted to remedy." *United Pharmacal Co. of Mo., Inc. v. Mo. Bd. of Pharm.*, 208 S.W.3d 907, 911 (Mo. banc 2006). The ISRS statutes as a whole show that the purpose was to allow the surcharge to recover only extraordinary expenses caused by government-mandated replacement program costs (§393.1009(5)(a)), government-mandated improvements (§393.1009(5)(b)), and government-mandated relocations (§393.1009(5)(c)). All share the same characteristics in that they are large government-mandated expenses. Ordinary expenses, such as projects to replace or repair pipe that was destroyed or damaged, do not fit these characteristics of eligible projects. The replacement programs were not necessary to require a gas utility to repair or replace a pipeline that was ruptured during excavation – the gas companies were already performing those functions because such repairs and replacements were necessary, and have always been necessary for gas companies to continue providing service. What the gas companies were *not* doing is performing comprehensive system-wide inspections and replacements to rid their distribution systems of hazardous conditions due to age. Once the PSC ordered such infrastructure inspections, and the gas companies experienced the associated expenses and the resulting regulatory lag issues that followed, the ISRS statutes were enacted to address this issue. There is no similar history associated with costs incurred replacing damaged or destroyed

infrastructure, and, therefore, there is no history suggesting that the legislature intended damaged or destroyed pipe caused by human conduct or other event to be recovered through the ISRS statutes.

"Since it is purely a creature of statute, the Public Service Commission's powers are limited to those conferred by the above statutes, either expressly, or by clear implication as necessary to carry out the powers specifically granted." *UCC*, 585 S.W.2d at 56. The PSC's Order unlawfully expanded the scope of the ISRS by authorizing costs not authorized by the ISRS statute. Under either the plain and ordinary meaning of the ISRS statutes from the language used, or from a statutory interpretation that looks at the purpose of the ISRS statute and its history, the result is the same – the ISRS statutes were meant to allow for the recovery between rate cases of the extraordinary expense caused by the PSC's pipeline replacement programs. For these reasons, the Order is unlawful and should be remanded back to the PSC so that the unlawful costs associated with replacing damaged and destroyed facilities can be removed.

C. Exceptions to Single Issue Ratemaking Should be Strictly Construed

This Court has held that, "Exceptions in a statute should be strictly construed." *Florida Realty, Inc. v. Kirkpatrick*, 509 S.W.2d 114, 121 (Mo. 1974). The ISRS is an exception to the prohibition against single issue ratemaking. *Public Counsel*, 417 S.W.3d at 821. The general rule, as provided for in § 393.270, and as interpreted in *UCC*, is that rate increases that do not consider all costs and revenues in a general rate case constitute unlawful single-issue ratemaking. *UCC*, 585 S.W.2d at 56. The ISRS exception to the general rule, therefore, should be construed strictly. *Florida Realty*, 509 S.W.2d at 121.

It has been well established that single-issue ratemaking is unreasonable because it increases the chances that the regulated utility will earn more than its authorized return. *UCC*, 585 S.W.2d at 56. This could occur if the PSC were to raise rates based upon one factor without considering all other relevant cost factors. *Id*. At the time the concept of single-issue ratemaking was defined by the courts, gas utilities incurred ordinary costs replacing or repairing damaged pipeline just as they do today. Nothing with respect to damaged facilities has changed. The only relevant change has been recognition of the weakening of an aging gas infrastructure and the need, for public safety purposes, to mandate systematic inspection and replacement programs. To allow routine and ordinary maintenance costs incurred replacing or repairing damaged pipe outside of a general rate case is contrary to the prohibition against single-issue ratemaking and the purpose of the ISRS statutes. *UCC,* 585 S.W.2d at 56; § 393.270.

Strictly construing exceptions to the prohibition against single-issue ratemaking is also consistent with "[t]he dominant thought and purpose of the [public utility law] policy [which] is the protection of the public while the protection given the utility is merely incidental." *State ex rel. Crown Coach Co. v. Public Service Commission,* 179 S.W.2d 123, 126 (Mo. App. K.C. 1944). In *UCC,* this court held:

> The first Public Service Commission law was enacted in 1913, S.B. 1, 1913 Mo.Laws, §§ 1-140, at 556. This court has previously recognized that its purpose was to protect the consumer against the natural monopoly of a public utility, as provider of a public necessity, *May Dep't Stores Co. v. Union Electric Light & Power Co., 341 Mo. 299, 107 S.W.2d 41, 48 (1937),*

> while at the same time permitting a recovery by the utility of a just and reasonable return.

UCC, 585 S.W.2d at 47. Protecting consumers against the harms of single-issue ratemaking is consistent with the PSC's and the Court's primary objective when interpreting public utility law. The PSC's Order, on the other hand, is inconsistent with *UCC*, *Crown Coach*, and *Florida Realty* in that it interprets the ISRS statutes broadly and in a manner that allows for greater single-issue rate increases, which increases the potential for rates that are unjust and unreasonable. *Crown Coach,* 179 S.W.2d at 126; *UCC*, 585 S.W.2d at 47. Accordingly, allowing the ISRS to include costs incurred replacing damaged or destroyed facilities is unlawful under § 393.1009(5)(a).

SUMMARY OF ARGUMENT

Appellant Public Counsel first urges the Court to reverse the Commission's Report and Order because it misinterprets and misapplies the plain and ordinary meaning of the ISRS statutes, §§ 393.1009, 393.1012, and 393.1015. Section 393.1009(5)(a) authorizes the PSC to approve ISRS rate increases for a narrowly defined set of costs incurred replacing infrastructure that is "worn out or are in deteriorated condition." The PSC incorrectly interpreted this language to allow costs incurred replacing infrastructure that was damaged or destroyed due to human conduct, such as when a pipe is accidentally ruptured during excavation or boring activities. This interpretation is contrary to the legislative intent as determined by a plain and ordinary reading of the language used –

damaged or destroyed pipe is not the same as pipe that is worn out or deteriorated, and therefore, damaged or destroyed pipe does not qualify for the ISRS.

To the extent the Court concludes that the phrase "worn or are in deteriorated condition" is subject to more than one conflicting interpretation, the statute is ambiguous and the legislative intent can be determined from the purposes that the ISRS statutes were meant to address. The purpose of § 393.1009(5)(a) was to allow for a more timely recovery of costs incurred complying with the Commission's mandated pipeline replacement programs. This purpose had nothing to do with repairing or replacing pipe that was damaged or destroyed by the gas company or a third party. The intent of the ISRS statutes has always been to remedy unsafe pipeline infrastructure that occurs naturally, not avoidable problems created by human conduct.

Lastly, PSC statutes should be interpreted in a manner that recognizes the primary purpose of the public utility law, that is, the protection of the public. Accordingly, statutory exceptions to traditional ratemaking principles must be narrowly construed to protect the public, and the ISRS statute should be narrowly construed to protect against single-issue ratemaking.

CONCLUSION

The court should reverse the Commission's order because it is unlawful, unreasonable, arbitrary and capricious and an abuse of discretion, and remand the case back to the PSC.

Respectfully submitted,

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Certificate of Service

I hereby certify that this brief and accompanying appendix was filed through the Court's electronic filing system, and notice of this filing, along with an electronic copy of this filing, was provided to the following counsel this 6th day of January 2015.

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CERTIFICATE OF COMPLIANCE

The undersigned certifies that this brief complies with the requirements contained in Rule 84.06. According to the word count of the word-processing system used to prepare the Brief (excepting there from the cover, certificate of service, this certificate, and the signature block and the appendix), contains 7,884 words.

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