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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

APPELLANT'S SUBSTITUTE REPLY BRIEF

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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.

This reply brief responds to the Substitute Briefs filed by the Missouri Public Service Commission ("PSC") and Liberty Energy (Midstates) Corp. d/b/a Liberty Utilities ("Liberty") on January 26, 2015.

1. Interpreting Legislative Intent by the Plain and Ordinary Meaning

Public Counsel argued in its Substitute Brief that the plain and ordinary meaning of the relevant statute, § 393.1009(5)(a), is clear from the language used, which limits eligible infrastructure replacements to:

> 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.[1]

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

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The PSC's brief correctly states that "[o]nly the projects that fall under subsection (a) are at issue in this case" (PSC Brief, p. 15). Accordingly, this appeal seeks an opinion from the Court interpreting the language of § 393.1009(5)(a), which limits eligible replacements to "existing facilities that have worn out or are in deteriorated condition."

The PSC argues that if the legislature intended to limit the eligible replacements to exclude infrastructure destroyed by human conduct, "it could have simply used the phrase "worn out" instead of "worn out or deteriorated" (PSC Brief, p. 18). Liberty made a similar argument in its brief (Liberty Brief, pp. 15-16). Both terms, "worn out" and "in deteriorated condition," however, are necessary to effectuate the purpose of the statute in that they address different infrastructure conditions. Pipe that is worn out is no longer usable,[2] whereas, pipe that is in deteriorated[3] condition may still be usable, but the deterioration has weakened the integrity of the pipe and created a potential safety concern. Every word in a statute has meaning. *Mo. Prosecuting Attys. v. Barton County*, 311 S.W.3d 737, 742 (Mo. 2010). Public Counsel's arguments have not rendered any word within § 393.1009(5)(a) "superfluous" as claimed by the PSC and Liberty, rather, the plain and ordinary meaning of "worn out" and "deteriorated" have the meaning addressed in Appellant's Substitute Brief and do not need to be repeated here.

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[2] *American Heritage Dictionary* defines "worn-out" as, "Worn or used until no longer usable or effective." *American Heritage Dictionary*, 1983 (4th ed. 2009).

[3] *Webster's* defines "deteriorate" as either, "to make inferior in quality or value: impair," or "to grow worse." *Webster's Third New International Dictionary*, 616 (3rd ed. 1993).

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Liberty further states that "there are many undertakings" required of gas companies in the PSC's safety rules that are ISRS-eligible, and cites to the "General" subsection of the PSC's "Maintenance" rules for gas companies found in 4 CSR 240-40.030(13)(B)(2), which states, "Each segment of pipeline that becomes unsafe must be replaced, repaired, or removed from service" (Liberty Brief, p. 19). Public Counsel agrees that when a pipeline becomes unsafe, the gas company must replace, repair, or remove the pipe from service. 4 CSR 240-40.030(13)(B)(2). But not all safety-related replacements qualify for ISRS eligibility – the statute specifically limits ISRS eligibility to pipeline replacements for "existing facilities that have worn out or are in deteriorated condition." § 393.1009(5)(a).

Had the legislature intended to expand ISRS-eligible replacements to include all safety-related pipeline replacements as suggested by the PSC and Liberty, the legislature would simply have ended § 393.1009(5)(a) after the word "facilities," and the subsection would state that eligible gas utility plant projects include:

> 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~~.

What is the purpose of the language stricken above if not to limit the eligible replacements in some way? The limiting language was included because worn out and deteriorated infrastructure is precisely what the replacement programs require gas

companies to locate and replace because infrastructure in this weakened condition creates the safety concern remedied by the replacement programs. 4 CSR 240-40.030(15).

According to Liberty's President, Mr. David Swain, the *only* pipeline or other facility replacement that Liberty excluded from its ISRS are those associated with growth (Transcript (Tr.) 37, 43-45).[4] This constitutes an unlawful abuse of the single-issue ratemaking privilege afforded Liberty by the ISRS statute. In effect, Liberty is following the modified § 393.1009(5)(a) shown above, and the PSC's Order authorized this unlawful interpretation of the ISRS. All pipe will need to be replaced at some point, but the ISRS provides an accelerated cost recovery for only a limited number of replacements – those replacements made complying with the replacement programs required by the PSC's rules. 4 CSR 240-40.030(15).

Liberty also argues that the *condition* of the infrastructure is the controlling factor, not the *cause* of the condition (Liberty Brief, p. 16). Public Counsel agrees that the condition is the controlling factor under § 393.1009(5)(a), but the condition of the pipe can be significantly influenced by the cause that creates the condition itself, which the statute recognizes. A pipe that has been deteriorating for the past thirty (30) years is in a much different condition than a pipe that has been torn open by a backhoe or even one

[4] The interpretation of § 393.1009(5)(a) followed by the PSC and Liberty would even authorize Liberty to raise rates for replacements caused by third-party damages regardless of whether such replacements will be paid for by the liable third-party or by the gas company's insurer.

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that has worn out. Under the PSC's interpretation, a replacement would be eligible for the ISRS even where the utility installs a brand new polyethylene pipe and accidentally destroys the pipe the very next day while excavating, thus necessitating a replacement. Such a result is totally inconsistent with the plain and ordinary meaning of the phrase "worn out or in deteriorated condition."

Liberty argues that a family at risk due to an unsafe condition of a pipe does not care whether such condition occurs naturally or due to human intervention, rather, they are most concerned about their safety (Liberty Brief, p. 16). This argument misses the point that the ISRS statutes in no way encourage more or less replacements, rather, they simply provide a recovery mechanism for replacements that are already required by law. § 393.1009(5). Liberty's argument suggests that a family at risk due to a pipe torn open by human conduct would be better off by including such replacement costs through the ISRS. However, there is no evidence suggesting that Liberty would replace the torn pipe any less quickly if the pipe replacement was ineligible under the ISRS. Liberty is obligated immediately to replace, repair or remove any unsafe pipe. 4 CSR 240-40.030(13)(B)2. Accordingly, the ISRS does not provide either an incentive or a disincentive to a gas utility to replace, repair or remove an accidentally ruptured main line. The obligation to remedy exists irrespective of the ISRS statutes.

Liberty argues that the PSC is given authority to interpret statutes and that such interpretation is afforded great weight by the Court. (Liberty Brief, p. 13). However, there is no presumption in favor of the PSC's resolution of legal issues, and the Court is to decide legal points anew. *State ex rel. Atmos Energy Corp. v. P.S.C.*, 103 S.W.3d 753,

759 (Mo. banc 2003). Where a state agency's decision is based upon an interpretation, application, or conclusion of law, the decision is reviewed de novo. *Klein v. Missouri Dept. of Health and Senior Services,* 226 S.W.3d 162, 164 (Mo. banc 2007).

2. Interpreting Legislative Intent by the Purpose of the Statute

A significant misperception regarding the ISRS, made by Liberty in its brief, is that the purpose of the ISRS is to eliminate disincentives that the gas company may have to make needed investments in infrastructure (Liberty Brief, p. 10). This is a misperception because it assumes that replacements eligible for ISRS recovery are incurred only at the discretion of the gas company. However, plant projects under the ISRS are eligible only if the project is *mandated* by state or federal government. § 393.1009(5). Under subpart (a) of § 393.1009(5), infrastructure replacements are eligible only if "installed to comply with state or federal safety requirements." Under subpart (b) of § 393.1009(5), infrastructure projects to extend the life of existing infrastructure are eligible only if "undertaken to comply with state and federal safety requirements." Lastly, under subpart (c) of § 393.1009(5), facility relocations are only eligible if "required" by a government entity or other entity with the power of eminent domain. All three categories of eligibility share one thing in common – they involve costs incurred by the gas company that are not discretionary. Therefore, the language of the ISRS statute refutes Liberty's assertion that the purpose of the ISRS is to provide an incentive for the gas company to make improvements. Those improvements are required irrespective of the ISRS statute. Any "disincentive" the gas companies may have had to make necessary improvements was removed when the PSC mandated the replacement programs required

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by 4 CSR 240-40.030(15). The ISRS statutes merely provide a faster form of recovery of compliance costs from ratepayers than what existed before the ISRS statutes.

Liberty briefly addressed Public Counsel's explanation that the ISRS was meant to replace the Accounting Authority Order (AAO) mechanism for recovering replacement program costs. Liberty does not dispute Public Counsel's recitation of these historic facts, and states only, "Public Counsel's purported "legislative history" and its strained analysis is actually based on regulatory history, about which the Commission itself would be most familiar" (Liberty Brief p. 17). Similarly, the PSC does not dispute Public Counsel's recitation of the historic facts regarding the link between the AAO rate recovery mechanism and the ISRS rate recovery mechanism. Accordingly, the legislative history of the ISRS statute shows that it was enacted to permit gas utilities to expeditiously recoup increased costs created by government-mandated pipeline replacement programs, which were required as a response to unprecedented pipeline accidents caused by an aging infrastructure that was in great need of inspection, and where worn out or deteriorated, subject to replacement.

3. Evidence That the Approved ISRS Included Ineligible Costs

The PSC and Liberty assert that Public Counsel did not present evidence that the ISRS calculations were incorrect or provide Public Counsel's own calculations (Liberty Brief, p. 5; PSC Brief, pp. 5-6). These assertions assume that calculations showing each and every instance of an ineligible project are the only evidence available to show that the ISRS includes ineligible projects. However, testimonial evidence from Liberty's State President, Mr. David Swain, during cross-examination, is sufficient testimony to

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show that Liberty's ISRS includes costs incurred that resulted from damage caused by a contractor or other third party. Mr. Swain testified as follows:

Q. Do all leaking gas mains and service lines need to be replaced or are there some leaking mains or service lines that can be repaired instead of replaced?

A. A leaking gas – a leaking main or service or any type of facility has to either be replaced or repaired as you say, yes.

Q. Can you please describe how those facilities are repaired?

A. Traditionally they're repaired by replacing, and in some instances a repair could be made by applying a repair fitting on that facility that would encapsulate that leak and render it safe.

Q. And are those type of expenses you believe eligible for ISRS recovery?

A. Yes, I do.

Q. If a third-party contractor accidentally strikes a Liberty main or service line while digging, is it your opinion that Liberty's costs to repair that main or service line are eligible for ISRS?

A. Yes. We – obviously a damaged – a damage that's done by a third party causes that line to leak, and so my previous answer is the same.

Q. And did any of the expenses that Liberty seeks to include in this ISRS petition result from damage to Liberty's facilities caused by a contractor or contractors or other third parties?

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A. It would have.

(Tr. pp. 41-42). The PSC's Chairman followed up on this question when examining Mr. Swain:

Q. I just want to clarify. So if there is a main leak caused by a contractor, your testimony is that that would be ISRS eligible?

A. Yes, it is.

(Tr. p. 43). The PSC's Order relied upon this testimony when it found, "Some expenses Liberty included in the Petition resulted from damage to Liberty's facilities caused by a contractor or other third party" (Legal File (L.F.) 257). When the Order approved the petition and allowed Liberty to increase the surcharge, the PSC knowingly allowed a single-issue rate increase for replacement costs that included third party damages.

This evidence provides sufficient support to reach the conclusion that Liberty included in its ISRS costs incurred as a result of damages caused by contractors and other third parties. And while the total costs for projects included in Liberty's ISRS that involved the replacement of pipe due to ruptures caused by human conduct or other events is not known by Public Counsel, those details can be determined upon remand.

4. ISRS Safeguards Against Single-Issue Ratemaking Inapplicable

The PSC states that "[t]he ISRS statutes include appropriate safeguards against the potential issues associated with single-issue ratemaking" (PSC Brief, p. 24). These safeguards are inapplicable to the issues raised in this appeal. If the PSC authorizes ineligible cost increases on consumer rates through the surcharge, between rate cases, and

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without a consideration of all costs and revenues, the PSC has unlawfully allowed single-issue ratemaking. *State ex rel. Utility Consumers Council of Missouri, Inc. v. P.S.C.*, 585 S.W.2d 41, 56 (Mo. banc 1979)(*UCC*). There is no safeguard within the rule to protect consumers against such single-issue ratemaking, and the only safeguard at that point is the consumer's right to seek review of PSC orders. § 386.510.

The PSC points to the three-year rate case requirement as a single-issue ratemaking safeguard (PSC Brief, p. 24). But the three-year rate case filing requirement does not protect against single-issue ratemaking that occurs between rate cases, rather, it merely limits any over-earnings caused by the single-issue rate increase to a three-year period (or longer if the gas company files a general rate case at the end of the three-years, which would prolong the ISRS for another eleven (11) months). §393.1012.2. If ineligible costs are included in the ISRS, there is no safeguard to protect consumers against the unlawful single-issue rate increase, which would increase the chances of over-earnings caused by the ISRS.

5. Public Counsel's Argument is Consistent with its Application for Rehearing

The PSC argues that Public Counsel's argument in its Substitute Brief is different than the argument it raised in its Amended Application for Rehearing (PSC Brief, p. 23). The PSC states that the only issue raised in the Amended Application for Rehearing was the ISRS recovery of costs attributable to third-party damages. *Id.* However, the PSC confuses its own conclusion regarding third-party damages with the error claimed by

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Public Counsel. Public Counsel's Amended Application for Rehearing raised the argument now on appeal as follows:

> Rehearing is also appropriate because the Order unlawfully and unreasonably concludes, "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." This conclusion is unlawful in that it authorizes amounts to be included in the ISRS that are not authorized by Section 393.1009(5) RSMo. The Order recognizes that a destroyed or damaged pipe is different than a deteriorated pipe when the Order states that the "deterioration has occurred quicker than what happens normally through the passage of time." But the Order takes an unreasonable and unlawful leap when it concludes that the term "deteriorated" includes pipe that has been damaged. These are different terms with different meanings. A deteriorated pipe is one where the quality of the pipe has been gradually lowered; it is not a pipe that has been destroyed or damaged immediately. The Order weakens the protections provided by the rule because it opens up the door for infrastructure investments that are not the type contemplated by the statute.

(L.F. 307-308). While the PSC's conclusion was limited to third-party damages only, the error identified by Public Counsel was not so limited. *Id.* Public Counsel's claim of error, as it properly raised in its Amended Application for Rehearing, is in regard to all

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costs included in the ISRS that were incurred replacing infrastructure that does not satisfy the plain and ordinary meaning of the term "worn out or in deteriorated condition." *Id.* Even language that is "extremely general and imprecise…is sufficient" to be "preserved" for consideration under Section 386.500(2) RSMo. *State ex rel. Chicago, Rock Island and Pacific Railroad Co., v. P.S.C.*, 441 S.W.2d 742 (Mo. App. 1979).

6. This Appeal is Not Moot

The PSC argues that the issue raised in this appeal has become moot due to the recent order issued by the PSC to resolve Liberty's 2014 rate case (PSC Brief, p. 10). "A cause of action is moot when the question presented for decision seeks a judgment upon some matter which, if the judgment was rendered, would not have any practical effect upon any then existing controversy." *State v. Reardon*, 41 S.W.3d 470, 473 (Mo. banc 2001). A judgment rendered in the present case will have a significant practical effect upon the controversy in question because the PSC's rate case order is, in part, predicated upon the outcome of this appeal. Liberty's Substitute Brief contains a reprint of a stipulated agreement between the parties that ties the outcome of that case to the outcome of the appeal in the present case (Liberty Brief, pp. 21-22). In that agreement, Liberty agreed to establish a regulatory liability account "to be used as a regulatory mechanism to preserve funds that could be used to credit the Company's ratepayers in the event that a court of competent jurisdiction reverses and remands the Commission's decision in the above-referenced case (referring to the present case)" *Id.* Accordingly, the point raised on appeal is not moot. It is highly inconsistent for the PSC to issue an order on August 20, 2014 ordering the outcome of the ISRS prudence review in the rate case to be

dependent upon the outcome of the present appeal,[5] and then, five months later, argue in its brief that the Court should determine the issue to be moot.

7. Public Counsel's Substitute Appellant's Brief Complied with Rule 84.04(c)

The PSC's brief and Liberty's brief assert that the "Background" portion of Appellant's Substitute Brief violates Rule 84.04(c) calling for a statement of facts without argument (PSC Brief, p. 1; Liberty Brief. p. 2). Neither party provides any explanation as to what "arguments" were made in Appellant's Statement of Facts, thereby providing no support for this claim. Contrary to their assertion, the background provided in Appellant's Substitute Brief provides the Court with an important understanding of the factual history that lead to the creation of the ISRS statute. This is the same background information that Liberty itself deemed important enough to raise in its opening statement during the PSC's evidentiary hearing (Tr. 6-7).

8. Public Counsel's Substitute Brief Appendix is Proper

The PSC states that Public Counsel's Appellant's Substitute Brief "relies heavily on material that is contained in its appendix but is outside of the record on appeal." However, Appellant's Substitute Brief complied with Supreme Court Rule 84.04(h),

[5] *In the Matter of Liberty Utilities (Midstates Natural Gas) Corp. d/b/a Liberty Utilities' Tariff Revisions Designed to Implement a General Rate Increase for Natural Gas Service in the Missouri Service Areas of the Company*, Case No. GR-2014-0152, Order Approving Partial Stipulation and Agreement, August 20, 2014.

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which states in part, that the appendix shall include, "The complete text of all statutes, ordinances, rules of court, or agency rules claimed to be controlling as to a point on appeal" and "matters pertinent to the issues discussed in the brief such as copies of exhibits, excerpts from the written record, and copies of new cases or other pertinent authorities." The Appendix to Appellant's Substitute Brief included no more than these documents authorized by Supreme Court Rule 84.04(h).

9. Exceptions to Single Issue Ratemaking Should be Strictly Construed

Public Counsel's Substitute Brief explained that the ISRS statute is an exception to the prohibition against single-issue ratemaking, and such exceptions should be strictly construed to protect consumers against the harms inherent in raising rates without considering all relevant factors (Appellant's Substitute Brief, pp. 30-32). This point was not contested in the Respondents' briefs. Accordingly, as the Court interprets the ISRS statute, it should strictly construe § 393.1009(5)(a) by recognizing that unless costs sought to be included in the ISRS are clearly authorized by the statute, those costs should be excluded from the ISRS to protect customers against increasing the likelihood that Liberty earns more than its authorized return on investment.

CONCLUSION

The plain and ordinary meaning of the ISRS statute, the legislative history behind the ISRS statute, and the protections afforded by the prohibition against single-issue ratemaking, all support a conclusion that the Commission unlawfully expanded the type of replacements eligible for ISRS recovery. Accordingly, the court should reverse the

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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 5th day of February 2015.

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Certificate Pursuant to Rule 84.06(c) and 84.06(g)

I hereby certify that the foregoing Brief of Appellant Office of the Public Counsel of Missouri complies with the limitations contained in Rule 84.06(b) and, 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 4,093 words.

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