

BEFORE THE STATE CORPORATION COMMISSION  
STATE OF KANSAS

STATE CORPORATION COMMISSION

APR 17 2009

In the Matter of the General Investigation )  
into Commission Policy Regarding )  
Pension and Retirement Costs for )  
Investor-Owned Utilities. )

07-GIMX-1041-GIV

 Docket Room

**Comments of CURB**

The Citizens' Utility Ratepayer Board submits its Comments in response to the Report and Recommendation ("Report") filed by the Staff of the Kansas Corporation Commission ("KCC") in the above-referenced docket on March 18, 2009.

**1. Introduction**

The KCC opened this generic investigation on March 29, 2007 to examine two requests made collectively by several utility companies in a previous docket that relate to the treatment of pension, postretirement and post-employment costs for regulatory purposes.<sup>1</sup> Specifically, the companies requested KCC authorization to:

Establish a regulatory asset or regulatory liability to track the difference between the amounts recognized in rates and the pension, postretirement and post employment expenses recorded according to Generally Accepted Accounting Principles ("GAAP") as defined in the Statements of Financial Accounting Standards ("SFAS") Nos. 87, 88, 106, 112, 132(R).

Recognize for rate making purposes the companies' contributions to their pension, postretirement, and post employment plans in excess of pension, postretirement, and post employment plan expense recorded in compliance with SFAS Nos. 87, 88, 106, 112, 132(R), 158.

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<sup>1</sup> The companies filing the original Application (Docket No. 07-ATMG-387-ACT) were Atmos Energy Corporation, Aquila, Inc. d/b/a Aquila Networks KGO, Aquila Networks, The Empire District Electric Company, Kansas City Power & Light Company, Westar Energy, Inc., and Kansas Gas and Electric Company.

The KCC had previously approved a request by the companies to recognize, for rate making purposes, any charges recorded against equity in compliance with SFAS No. 158 and SFAS Nos. 87, 88, 106, and 132(R) as amended through either the establishment of a regulatory asset or an adjustment to the equity percentage in the utility's capital structure. The KCC approved that request on January 24, 2007.

## **2. Staff Report and Recommendations**

Staff filed its Report and Recommendations on March 18, 2009. The Staff Report recommended that the KCC permit the companies to establish a regulatory asset or regulatory liability to track the difference between the amounts recognized in rates and the pension, postretirement and post employment expenses recorded according to GAAP as defined in SFAS Nos. 87, 88, 106, 112, 132(R). However, the Report also recommended that if the Commission approves this request, then the companies should be required to fund these costs, based on the pension, postretirement and post employment expenses recovered annually in utility rates.

The Report recommended that the KCC deny the companies' request to recognize, for rate making purposes, their contributions to their pension, postretirement, and post employment plans in excess of pension, postretirement, and post employment plan expense recorded in compliance with SFAS Nos. 87, 88, 106, 112, 132(R), 158.

CURB recommends that the KCC decline to adopt these recommendations, for the reasons detailed below. However, in the event that the KCC accepts the Report's recommendation to permit the companies to establish a regulatory asset or regulatory liability to track the difference between the amounts recognized in rates and pension,

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postretirement, and post employment costs booked pursuant to GAAP, then CURB recommends that the Commission require funding for the amounts recovered in rates, consistent with Staff's recommendation.

**3. The KCC should reject all further requests for reimbursement ratemaking**

Staff's Report recommends that the KCC approve a request of the companies to record a regulatory asset or regulatory liability for the difference between pension, postretirement, and postemployment costs included in rates and the amounts booked by the companies for financial reporting purposes pursuant to GAAP. CURB disagrees with the Report's recommendation and recommends instead that the Commission decline to adopt this method of reimbursement ratemaking for these costs.

The Report's proposal effectively provides a true-up between amounts collected in rates and actual costs that are incurred between base rate cases pursuant to GAAP. Since base rates are only changed periodically, but pension, postretirement and postemployment costs fluctuate each year, usually there are annual differences between the amounts collected in rates and the costs booked for financial reporting purposes. The Report's recommendation would result in a true-up of these differences, with amortization of the regulatory asset or regulatory liability over a period of five years.

Adoption of this recommendation would establish yet another milestone in the continuing (and very successful) campaign of the utilities to transform the regulatory process into a system of dollar-for-dollar reimbursement of their costs. The Commission has approved numerous surcharges and true-up mechanisms. CURB also notes that the legislature has been instrumental in this process as well, depriving the KCC of its discretion to deny the utilities' requests for certain types of surcharge mechanisms so

long as they meet the statutory application requirements. Each time another surcharge or true-up mechanism is approved, the approval represents a distinct, deliberate action to eliminate regulatory risk for the utilities and to eliminate the protections from monopolies that the regulatory process was supposed to provide ratepayers.

The regulatory process is *supposed* to provide a substitute for competition in a monopolistic regime, not ensure that utility companies are made whole every year for cost differences that occur between base rate cases. Utility rates are *supposed* to be established in a base rate case based on *pro forma* levels of investment, revenues, and expenses. Regulators are *supposed* to keep this regulatory triad in balance to protect the interests of the utilities and the ratepayers. The rates are *supposed* to be set at a level that provides the utility an opportunity to earn an appropriate level of profit, not a guarantee. This system is *supposed* to provide the utility an incentive to operate more efficiently and reduce its costs. The system, when it works right, is *supposed* to produce a balanced result of fair earnings to the utility—especially if it is efficient and good at cutting costs—and fair rates for the ratepayers, who can't choose to do business with a competing utility if their current utility's rates aren't fair.

But single-issue ratemaking undoes all that. It provides the utility reimbursement whenever one type of cost exceeds expectations. (While it can be argued that it also provides credit to ratepayers when costs turn out to be lower than expected, utilities generally don't seek true-up mechanisms for costs they anticipate will decrease, as discussed further below.) Single-issue ratemaking destroys the utility's incentive to be efficient and prudent. It destroys the protection from monopoly that regulation is supposed to provide the ratepayers.

Furthermore, the introduction of true-up clauses without regard for overall earnings can result in increased costs to ratepayers, even if a utility is still earning its authorized rate of return. Between base rate cases, all components of the regulatory triad will change, *i.e.*, some costs will go up, some will go down, but it is generally up to the utility to decide whether, given these variations, it's time to file a request for a rate increase. It is a fact of life that utilities don't seek accounting orders and surcharges for expenses that they expect to decrease. The balance of the regulatory triad is upset when the utility is granted regular true-ups of the types of costs that are likely to increase, but there is no corresponding true-up of the types of costs that are likely to remain stable or decrease during the same period since these costs are often left in base rates. As a result, even if the utility's overall costs haven't increased enough to deprive the utility of its authorized rate of return, the ratepayers are nevertheless forced to provide the utility additional periodic bumps in rates. That is the primary reason, but not the only one, for why surcharges, accounting orders and other true-up mechanisms are bad for ratepayers.

Another reason for rejecting these mechanisms is that the proliferation of true-up clauses has weakened the regulatory process. While providing less incentive for the utilities to control costs, true-up clauses also make it more difficult for the KCC to scrutinize the costs being recovered from ratepayers. One reason is that there are likely to be fewer parties in these cases, and the participating parties generally have more limited resources than in a base rate case. Thus, discrepancies in the company's filing are less likely to be challenged. Even if the Commission Staff's review is relatively thorough, the practical fact is that the data isn't given the level of scrutiny (such as on-site audits) that is usually given to expense components that are reviewed as part of the

base rate case process, and no one but the ratepayers have incentive to protest.

Furthermore, with deadlines for decisions being imposed by the legislature in some circumstances, the KCC simply has less time for review of the rates resulting from true-up clauses than they do for review in a base rate case. All of these factors contribute to the fact that the Commission rarely orders disallowances in proceedings involving true-up mechanisms.

**4. Staff's recommendation is not supported by facts or sound reasoning.**

The Staff Report's recommendation to adopt this mechanism is not supported by facts or a rational explanation for adopting it. The Report states that "[a]ny change in the utilities' pension, postretirement and post employment expenses between rate cases is absorbed by the utilities."<sup>2</sup> This statement fails to acknowledge that these changes can be decreases in costs between rate cases, which the utility also "absorbs", a situation that actually benefits utilities under the current regulatory scheme. At least the Report acknowledges that approving this request would absolve the utilities "of any risk in recovering the pension, postretirement, and postemployment costs. The company will have shifted all risk onto the consumer who will bear the entire responsibility of the pension, postretirement, and post employment costs."<sup>3</sup> Thus, the Report acknowledges that approval of this request will shift the entire risk of these costs onto ratepayers, but fails to provide a rationale for approving this shift.

What is also missing in the Report is an explanation of why pension, postretirement, and post employment costs deserve this treatment, and why they should

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<sup>2</sup> Staff Report, pages 2-3.

<sup>3</sup> Staff Report, page 3.

be treated differently from all the other costs that are currently recovered in base rates. There's no discussion of the impact on the utilities' cost of capital of shifting this risk. There's no provision for reducing the utilities' cost of capital to reflect this lower risk. In fact, the Report provides no rationale whatsoever for why the Commission should adopt this proposal to establish a regulatory asset/liability. There is no discussion of the full impact on ratepayers, no discussion of why ratepayers should bear these risks, and no discussion of why ratepayers should guarantee recovery of these costs while continuing to provide the utilities the same return as before. In recommending approval of this true-up mechanism without addressing these issues, the Report provides insufficient evidence to support a Commission finding that this proposal is the interest of "the public generally."

Given the fact that the proposed accounting treatment would constitute single-issue ratemaking, would provide a disincentive for the companies to control these costs, would weaken regulatory oversight, would shift risk from the companies completely to ratepayers, and has not been justified by Staff, CURB recommends that the KCC deny the companies' request to establish a regulatory asset or regulatory liability for the difference between the amounts collected in rates and the amounts booked pursuant to GAAP.

**5. If the KCC adopts the recommendation to establish a regulatory asset/liability, then it should also impose the funding conditions recommended by Staff .**

If, in spite of CURB's recommendation, the KCC adopts the policy of allowing utilities to establish a regulatory asset or regulatory liability for the difference between

the amounts collected in rates and the amounts booked pursuant to GAAP, then CURB supports Staff's recommendation that the Commission require the companies to fund these costs. Specifically, Staff's proposal in its Report would require funding of the amount included in rates. As the Report noted, "...the inclusion of pension, postretirement and post employment costs in the company's cost of service does not automatically result in a cash outlay."<sup>4</sup> It goes on to note that, "[i]n the past, it has been a common occurrence for a company to have no cash outlay for pension, postretirement, and post employment costs but experience a cash inflow from ratepayers for recovery through the cost of service."<sup>5</sup>

Thus, in order to ensure that amounts collected from ratepayers will be used for the purposes intended, the Report recommends "minimum mandatory funding with third party trustees of all monies collected from rate payers for pension, postretirement and post employment benefits."<sup>6</sup> CURB supports this requirement.

While CURB opposes establishing yet another regulatory asset or regulatory liability, for the reasons stated above, if the KCC approves the companies' request to establish a regulatory asset/liability, then it should at least ensure that the amounts collected from ratepayers are used for the purpose intended. This can be accomplished by requiring funding of these costs, based on the amounts included in utility rates. Moreover, these amounts should be contributed to a third-party trust fund, to ensure that the funds will be available when needed. Otherwise, there is no assurance that the funds collected from ratepayers will be used for their intended purpose and ratepayers could be required to pay twice for these employee benefit costs.

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<sup>4</sup> Staff Report, page 3.

<sup>5</sup> Id.

<sup>6</sup> Id.



Accordingly, if the KCC approves the companies' request to establish a regulatory asset/ liability, then the KCC should also require them to place the money collected from ratepayers in the appropriate trust fund, as recommended in Staff's Report.

In addition, it is CURB's understanding that under Staff's proposal, the resulting regulatory asset or regulatory liability will not be included in a company's rate base during the period over which it is being amortized. Since the funding of the pension trust will match amounts collected in cost of service, the establishment of a regulatory asset or regulatory liability will not impact the company's funding requirement for ratemaking purposes. Therefore, there would be no rationale for including any unamortized balances in rate base.

**6. CURB supports Staff's recommendation to deny a return on excess contributions.**

In the previous docket, the companies had requested that the KCC permit them to establish a mechanism to track, between rate cases, contributions in excess of pension, postretirement, and post employment expenses calculated and recorded pursuant to GAAP, and also requested authorization to include these excess contributions in rate base claims as part of their base rate cases. Staff recommended in its Report that the Commission deny these requests. CURB concurs with the Report's recommendation.

As noted by Staff in its Report, the utilities have significant discretion in determining the annual contributions to the retirement trust funds. Funding decisions can be influenced by many factors that have no direct relationship to regulated cost of

service, such as tax considerations and the availability of alternative investments. While the companies have discretion regarding these funding decisions, there is no rationale for making ratepayers pay a return on excess contributions. As discussed above, Staff's recommendation is that the companies be required to fund pension, postretirement, and post employment costs based on the amounts collected from ratepayers. To the extent that the companies decide to make additional contributions to a trust fund, ratepayers should not be required to provide a return to shareholders. Thus, CURB supports Staff's position on this issue.

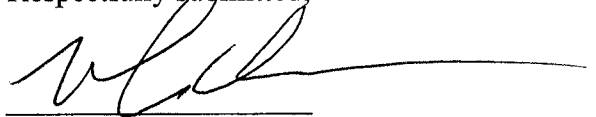
## **7. Summary of Recommendations**

CURB recommends that the KCC decline to adopt the recommendations contained in the Staff Report and not establish a regulatory asset or regulatory liability for the difference between the amounts collected in rates and the amounts booked pursuant to GAAP. Permitting the establishment of a regulatory asset or regulatory liability would constitute single-issue ratemaking, would provide a disincentive for the companies to control these costs, would weaken regulatory oversight, would shift risk from the companies completely to ratepayers, and has not been justified by Staff.

If, in spite of CURB's recommendation, the KCC accepts the Staff Report and permits the companies to establish a regulatory asset or regulatory liability for the difference between the amounts collected in rates and the amounts booked pursuant to GAAP, then CURB supports Staff's recommendation that the companies be required to fund these costs. CURB also supports Staff's position that the unamortized regulatory asset or regulatory liability would not be included in rate base.

Finally, CURB supports Staff's recommendation that the KCC deny the companies' request to establish a mechanism to track, between rate cases, contributions in excess of pension, postretirement, and post employment expenses calculated and recorded pursuant to GAAP. Funding decisions can be influenced by many factors that have no direct relationship to regulated cost of service. To the extent that the companies decide to make additional contributions to a trust fund, ratepayers should not be required to provide a return to shareholders.

Respectfully submitted,



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VERIFICATION

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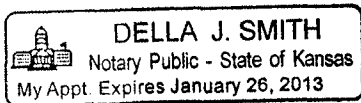
I, Niki Christopher, of lawful age, being first duly sworn upon her oath states:

That she is an attorney for the Citizens' Utility Ratepayer Board, that she has read the above and foregoing document, and, upon information and belief, states that the matters therein appearing are true and correct.



Niki Christopher

SUBSCRIBED AND SWORN to before me this 17<sup>th</sup> day of April, 2009.

  
Notary Public

My Commission expires: 01-26-2013.

**CERTIFICATE OF SERVICE**

07-GIMX-1041-GIV

I, the undersigned, hereby certify that a true and correct copy of the above and foregoing document was placed in the United States mail, postage prepaid, e-mailed, or hand-delivered this 17th day of April, 2009, to the following:

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Della Smith

\* Denotes those receiving the Confidential version