

**BEFORE THE PUBLIC SERVICE COMMISSION  
OF THE STATE OF MISSOURI**

In the Matter of The Empire District Electric	)	
Company's Application for Certificate of Public	)	
Convenience and Necessity and Approval of	)	<b><u>Case No. EO-2005-0263</u></b>
An Experimental Regulatory Plan Related to	)	
Generation Plant	)	

**OPINION OF COMMISSIONER STEVE GAW CONCURRING IN PART AND  
DISSENTING IN PART**

I concur in part and dissent in part with the Commission's decision approving the Stipulation and Agreement in this case. It is apparent that Empire needs to add baseload generation to its system in light of its current heavy dependence on natural gas-fired generation. As such, adding capacity from the Iatan 2 generating facility is a move in the right direction. Despite this positive aspect, what is disturbing is that, instead of resulting in an increase in the percentage of baseload capacity for Empire, the regulatory plan envisions a best case scenario that actually produces a baseload capacity percentage decrease.

The reason underlying the declining baseload capacity percentage is easily understood. Empire's need for baseload generation has been documented for over 12 years. In early 1993, Empire was contacted by Ahlstrom Development Corporation with a proposal by which Ahlstrom would build a small power production facility which would utilize unreclaimed waste coal and petroleum coke as fuel.<sup>1</sup> Projected to be completed in the year 2000, Empire would purchase either 160 or 260 MWs of power for a period of 25 years and would then be given the option of assuming ownership of the facility. Evidence in that case indicates that, despite its need for baseload capacity, Empire would not even engage in meaningful negotiations.<sup>2</sup>

In its testimony, Empire asserted that the purchased power costs of the Ahlstrom project

---

<sup>1</sup> *Ahlstrom Development Corporation, and Cottonwood Energy Partners, L.P. v. The Empire District Electric Corporation*, 4 Mo.P.S.C. 3d 187 (1995).

<sup>2</sup> *Id.* at 192.

were too expensive relative to other available baseload capacity options. Instead, Empire claimed that it had recently entered into a 10 year agreement to purchase 162 MWs of capacity from Western Resources (WRI). Empire maintained, and the Commission ultimately agreed, that the WRI agreement represented a lower cost alternative and that Empire should not be required to execute an agreement with Ahlstrom.

While the WRI contract may have been a cheaper alternative in the short run, it did not represent a permanent solution. Instead the WRI agreement only provided for baseload capacity and energy for a period of 10 years. As envisioned by the Order, however, it was the Commission's belief that Empire's management would use the intervening time period to identify, finance, and construct a baseload facility to be available upon the expiration of the WRI agreement.<sup>3</sup> Clearly, Empire has not used that intervening time period as envisioned by the Commission. Rather than seeking the baseload capacity, Empire engaged in a strategy of heavy investment in natural gas-fired intermediate and peaking facilities.<sup>4</sup> It is this decision of Empire's management to invest in natural gas generation that is now haunting Empire ratepayers, has led to a succession of Empire rate increases, and should be the subject of future Commission scrutiny.

Staff Witness Wood testified that, even using Staff's conservative load growth predictions, the addition of the Iatan 2 generation will leave Empire far below an optimal generation mix with an over-dependence on expensive gas-fired intermediate and peaking generation facilities. With the recent passage of SB 179, Empire shareholders and management bear less accountability for the utility's decision to become increasingly dependent on natural gas

---

<sup>3</sup> The Commission specifically found that the most appropriate determination of Empire's avoided cost was based upon the WRI 10 year power purchase agreement combined with a 160 MW baseload unit to be available immediately upon the expiration of the WRI contract. Based upon the 45 year costs for the combined power purchase agreement & baseload addition, the Commission found that "Empire's 45-year avoided is substantially less than the costs associated with either Ahlstrom proposal".

<sup>4</sup> Information provided in recent rate proceedings indicates that Empire added: (1) a 90 MW gas-fired State Line Unit 1, (2) 2-50 MW gas-fired Energy Center jet engines, and (3) a 300 MW gas-fired State Line Unit 2 combined cycle.

generation. Whereas the utility would have once bore the volatility risk of investing heavily in a particular source of electric generation, SB 179 now shifts that volatility risk and the high fuel costs associated with running gas turbines to the consumers.

Perhaps foreshadowing the current generation situation faced by Empire, the Commission, in its Ahlstrom decision, specifically warned Empire that its generation procurement decisions should be subject to future prudence determinations.

The Commission's finding as to Empire's avoided cost should not be construed as a limitation upon the ability of parties to attack the prudence of the WRI agreement or later 2 charges in connection with future electric rate cases of Empire or other electric utilities. In particular, in all likelihood Empire's revenue requirement will be affected by the WRI agreement in future Empire rate proceedings. The Commission's finding in the instant proceeding with respect to Empire's avoided costs does not limit the ability of any party to attack the prudence of costs incurred under the WRI agreement in the context of future Empire rate proceedings.<sup>5</sup>

It is this Commissioner's belief that the Empire generation procurement decisions, based upon a heavy dependence on natural gas and peaking facilities should finally be scrutinized. Empire's failure to arrange for baseload capacity to be available upon the expiration of the WRI purchase power agreement has likely resulted in higher rates to the Empire ratepayers. The rationale underlying Empire's: (1) failure to arrange for baseload capacity and (2) decision to continue to invest in natural gas-fired peaking and intermediate facilities should be subjected to some test of reasonableness.

Along these lines and perhaps most troubling is that this Stipulation seems to approve the construction of an additional gas-fired peaking facility to the Empire system. As mentioned, Empire is already heavily dependent on natural gas. Recognizing the current natural gas prices, I cannot vote for an Order that continues to dig a deeper hole for Empire's customers.

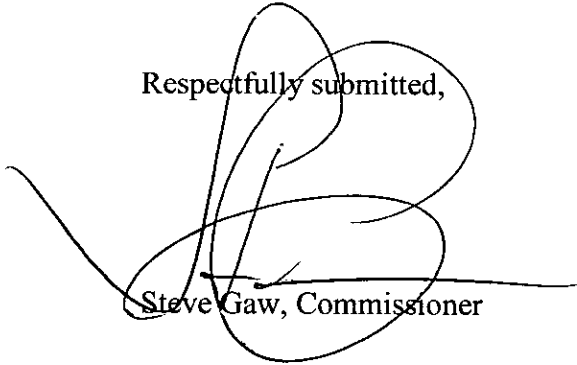
The Office of the Public Counsel and Staff seem to have attempted to preserve an argument on the prudence of Empire decisions on fuel mix while allowing the gas turbine to be a

---

<sup>5</sup> *Id.* at 197.

part of the Regulatory Plan. This creates the potential for confusion in a rate case where the gas-fired turbine is challenged as a part of Empire's choice of generation mix. Empire seems to acknowledge some preservation of this argument in future rate cases. However, it would seem much cleaner to have simply omitted the gas turbine from the regulatory plan approved in the Stipulation in this case.

Respectfully submitted,



Steve Gaw, Commissioner

Dated at Jefferson City, Missouri,  
on this 30<sup>th</sup> day of September, 2005.