

Exhibit No : 901
Witness: James T. Selecky
Type of Exhibit: Direct Testimony
Issues: Cost of Service and
Revenue Allocation
Sponsoring Parties: Wal-Mart Stores East, LP
Case No : ER-2006-0314

BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

FILED

AUG 22 2006

In the Matter of the Application of
Kansas City Power & Light Company
for Approval to Make Certain Changes
in its Charges for Electric Service to
Begin the Implementation of Its
Regulatory Plan

Missouri Public
Service Commission

Case No. ER-2006-0314

Direct Testimony and Schedules of

James T. Selecky
on Cost of Service
and Revenue Allocation

FILED

NOV 13 2006

On Behalf of

Missouri Public
Service Commission

Wal-Mart Stores East, LP

August 22, 2006



BRUBAKER & ASSOCIATES, INC.
St. Louis, MO 63141-2000

Project 8627

Exhibit No. 901
Case No(s) ER-2006-0314
Date 10-16-06 Rptr KF

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STATE OF MISSOURI)

SS

COUNTY OF ST. LOUIS)

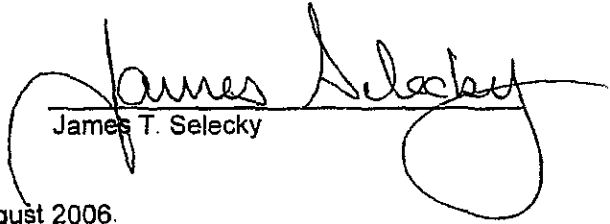
Affidavit of James T. Selecky

James T. Selecky, being first duly sworn, on his oath states:

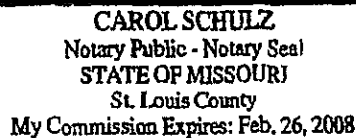
1. My name is James T. Selecky. I am a consultant with Brubaker & Associates, Inc., having its principal place of business at 1215 Fern Ridge Parkway, Suite 208, St. Louis, Missouri 63141-2000. We have been retained by Wal-Mart Stores East, LP in this proceeding on their behalf.

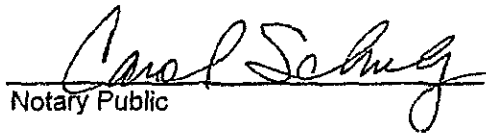
2 Attached hereto and made a part hereof for all purposes is my direct testimony on cost of service and revenue allocation issues which was prepared in written form for introduction into evidence in Missouri Public Service Commission Case No ER-2006-0314.

3. I hereby swear and affirm that the testimony is true and correct and that it shows the matters and things it purports to show.


James T. Selecky

Subscribed and sworn to before this 21st day of August 2006.




Notary Public

My Commission Expires February 26, 2008.

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

**In the Matter of the Application of
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Case No. ER-2006-0314

Direct Testimony of James T. Selecky

1 Q **PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.**

2 A James T. Selecky; 1215 Fern Ridge Parkway, Suite 208; St. Louis, MO 63141-2000.

3 Q **WHAT IS YOUR OCCUPATION AND BY WHOM ARE YOU EMPLOYED?**

4 A I am a consultant in the field of public utility regulation and a principal in the firm of
5 Brubaker & Associates, Inc., energy, economic and regulatory consultants.

6 Q **PLEASE SUMMARIZE YOUR EDUCATIONAL BACKGROUND AND
7 EXPERIENCE.**

8 A These are set forth in Appendix A to my testimony.

9 Q **ON WHOSE BEHALF ARE YOU TESTIFYING IN THIS PROCEEDING?**

10 A I am testifying on behalf of Wal-Mart Stores East, LP (Wal-Mart). Wal-Mart
11 purchases electricity from Kansas City Power & Light Company (KCPL or Company)
12 primarily on Rate Schedule 14.

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1 Q WHAT IS THE PURPOSE OF YOUR TESTIMONY?

2 A The purpose of my testimony is to discuss the results of KCPL's cost of service study
3 and the allocation of any rate increase that the Missouri Public Service Commission
4 (Commission) may grant. The fact that an issue is not addressed should not be
5 construed as an endorsement of KCPL's position.

6 Q PLEASE SUMMARIZE YOUR CONCLUSIONS AND RECOMMENDATIONS.

7 A A summary of my conclusions and recommendations is as follows:

- 8 1. The Commission should utilize the results of a cost of service study for purposes
9 of allocating any increase in this proceeding.
- 10 2. The Commission should reject KCPL's proposal to use the average and peak
11 method for purposes of allocating production and transmission fixed cost to
12 KCPL's rate classes.
- 13 3. The Commission should utilize the results of a cost of service study that utilizes
14 either the coincident peak method, or the average and excess demand method for
15 purposes of allocating production and transmission fixed cost to the rate classes.
- 16 4. The average and peak method is inappropriate because it does not truly reflect
17 cost causation, double counts the energy consumption or average demand
18 component, and fails to recognize the appropriate trade offs between capital and
19 operating costs.
- 20 5. The revenue allocation proposed by KCPL moves rates further away from cost of
21 service when comparing the revenue responsibility of each rate class with the
22 cost to serve that rate class.
- 23 6. If the Commission determines that KCPL's overall revenue requirement is less
24 than the amount requested, the reduction to the revenue requirement should be
25 allocated to those classes that have revenues in excess of the cost of service.
26 That is, any reduction in the revenue requirement from the level requested by
27 KCPL should be allocated to those rate classes based on cost of service.

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1 **Cost of Service Overview**

2 Q HAS KCPL FILED A CLASS COST OF SERVICE STUDY (CCOSS) IN THIS
3 PROCEEDING?

4 A Yes. KCPL has filed an embedded CCOSS study in this case. A CCOSS is used to
5 determine the cost that KCPL incurs to serve the various customer classes.

6 Q WHAT INFORMATION IS CONTAINED IN A CCOSS?

7 A A CCOSS compares the cost that each customer class imposes on the system to the
8 revenues each class contributes. This relationship is generally presented by
9 comparing the rate of return that a class is providing with the utility's overall
10 *jurisdictional rate of return.*

11 For example, when a customer class produces the same rate of return as the
12 total utility rate of return, the customer class is paying revenue to the utility just
13 sufficient to cover the costs that the utility incurs to serve that class. If a class
14 produces a below-average rate of return, it may be concluded that the revenue
15 provided by the class is insufficient to cover all relevant costs to serve that class. On
16 the other hand, if a class produces a rate of return above the system average, it is not
17 only paying revenues sufficient to cover the cost attributable to it, but in addition, it is
18 paying part of the cost attributable to other classes who produce below system
19 average rates of return.

20 Q WHY IS A CCOSS OF IMPORTANCE?

21 A A CCOSS shows the costs that a utility incurs to serve each class. It is a widely held
22 principle that costs should be shared among customer classes on the basis of cost-

1 causation. That principle is perhaps the most universally accepted principle of
2 regulatory cost determination.

3 **Q DO YOU SUPPORT THAT PREMISE?**

4 A Yes. Cost-based rates are not only fair and reasonable, but further the cause of
5 stability, conservation and efficiency. When consumers are presented with price
6 signals that convey the consequences of their consumption decisions, i.e. how much
7 energy to consume, at what rate, and when, they tend to take actions which not only
8 minimize their own costs, but those of the utility as well.

9 Although factors such as simplicity, gradualism, economic development and
10 ease of administration may also be appropriate for consideration when determining
11 the spread of the revenue requirement among classes, the fundamental starting point
12 and guideline should be the actual cost of serving each customer class.

13 **Q HOW ARE COST-BASED RATES DETERMINED?**

14 A The appropriate mechanism to develop cost-based rates is a fully allocated
15 embedded CCOSS. It follows, however, that the objective of cost-based rates cannot
16 be attained unless the CCOSS is developed using cost-causation principles
17 consistently.

18 **Q WHAT ARE THE MAJOR STEPS IN A COST OF SERVICE STUDY?**

19 A The first step in a CCOSS is known as functionalization. This simply refers to the
20 process by which the Company's investments and expenses are reviewed and put
21 into different categories of cost. The primary functions utilized are production,

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1 transmission and distribution. Of course, each broad function may have several
2 subcategories to provide for a more refined determination of cost of service.

3 The second major step is known as classification. In the classification step,
4 the functionalized costs are separated into the categories of demand-related, energy-
5 related and customer-related costs.

6 Demand or capacity-related costs are those costs that vary with the amount of
7 demand placed on the system. A traditional example of capacity-related costs is the
8 investment associated with generating stations, transmission lines and a portion of
9 the distribution system. Once the utility makes an investment in these facilities, the
10 costs continue to be incurred, irrespective of the number of kilowatthours generated
11 and sold.

12 Energy-related costs are those costs that vary in proportion to the number of
13 kilowatthours sold. Thus, the fuel expense is almost directly proportional to the
14 amount of kilowatthours generated by the utility system.

15 Customer-related costs are those costs that vary in proportion with the
16 number of customers served. Primary examples of customer-related costs are
17 investments in the distribution system, meters and service lines, and such accounting
18 functions as meter reading, bill preparation and revenue accounting.

19 The final step in the CCOSS is the allocation of each category of costs to the
20 various customer classes. Demand-related costs are allocated on the basis which
21 gives recognition to each class's responsibility for the company's need to build plant
22 to serve demands imposed on the system. Energy-related costs are generally
23 allocated on the basis of energy use by each customer class. Customer-related costs

1 are generally allocated based upon the number of customers in each class, weighted
2 to account for the complexity of servicing the different classes of customers.

3 **Q WHAT CUSTOMER CLASSES DID KCPL INCLUDE IN ITS CCOSS STUDY?**

4 A KCPL developed a CCOSS for Residential, Small General Service, Medium General
5 Service, Large General Service, Large Power Service, and Lighting. These classes
6 generally conform to KCPL's current electric tariffs. Finally, the test year that was
7 used for the CCOSS was the 12-month period ending September 2005.

8 **Q WHY IS IT IMPORTANT TO ADHERE TO BASIC COST OF SERVICE PRINCIPLES**
9 **IN THE RATEMAKING PROCESS?**

10 A The basic reasons for using cost of service as the primary factor in the revenue
11 allocation/rate design process are equity, cost causation, appropriate price signals,
12 conservation and revenue stability.

13 **Q HOW IS THE EQUITY PRINCIPLE ACHIEVED BY BASING RATES ON COSTS?**

14 A To the extent practical, when rates are based on cost, each customer pays what it
15 costs the utility to serve them, no more and no less. If rates are not based on cost of
16 service, then some customers contribute disproportionately to the utility's revenue
17 requirement and provide contributions to the cost to serve other customers. This is
18 inherently inequitable.

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1 **Q HOW DO COST-BASED RATES PROVIDE APPROPRIATE PRICE SIGNALS TO**
2 **CUSTOMERS?**

3 A Rate design is the step that follows the allocation of costs to classes, so it is important
4 that the proper amounts and types of costs be allocated to the customer classes so
5 that they may ultimately be reflected in the rates.

6 When the rates are designed so that the demand costs, energy costs, and
7 customer costs are properly reflected in the demand, energy and customer
8 components of the rate schedules, respectively, customers are provided with the
9 proper incentives to manage their loads appropriately. This, in turn, provides the
10 correct signal to the utility (and other competitive power suppliers if applicable) about
11 the need for new investment. When customers impose a certain level of demand on
12 the system, they should pay for the prudent cost that the utility incurs to supply that
13 demand and the energy charge that they pay should reflect the cost of providing that
14 energy.

15 From a rate design perspective, overpricing the energy portion of the rate and
16 under pricing the fixed components of the rate, such as customer and demand
17 charges, will result in a disproportionate share of revenues being collected from high
18 load factor customers and send erroneous price signals to all customers.

19 **Q HOW DO COST-BASED RATES FURTHER THE GOAL OF CONSERVATION?**

20 A Conservation occurs when wasteful or inefficient uses of electricity are discouraged or
21 minimized. Only when rates are based on actual costs do customers receive an
22 accurate and appropriate price signal against which to make their consumption

1 decisions. If rates are not based on costs, then customers may be induced to use
2 electricity inefficiently in response to the distorted price signals.

3 **Q PLEASE DISCUSS THE REVENUE STABILITY CONSIDERATION.**

4 **A** When rates are closely tied to costs, the impact on the utility's earnings due to
5 changes in customer use patterns will be minimized. Rates that are designed to track
6 changes in the level of costs result in revenue changes that mirror cost changes.
7 Thus, cost-based rates provide an important enhancement to a utility's earnings
8 stability, reducing its need to file for rate increases.

9 From the perspective of the customer, cost-based rates provide a more
10 reliable means of determining future levels of power costs. If rates are based on
11 factors other than the cost to serve, it becomes much more difficult for customers to
12 translate expected utility-wide cost changes, such as expected increases in overall
13 revenue requirements, into changes in the rates charged to particular customer
14 classes and to customers within the class. This situation reduces the attractiveness
15 of expansion, as well as continued operations, in the utility's service territory because
16 of the limited ability to plan and budget for future power cost.

17 **KCPL's CCOSS**

18 **Q PLEASE COMMENT ON KCPL'S MISSOURI JURISDICTIONAL CCOSS.**

19 **A** First, KCPL's proposed allocation method utilized to allocate the production and
20 transmission fixed costs is inappropriate and over allocates costs to high load factor
21 customers. As indicated in the testimony of KCPL witness Lois Liechti on page 8, the
22 Company used an allocation method called the Average and Peak method to allocate

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1 production and transmission fixed costs. Second, the Company allocated certain
2 Administrative and General (A&G) costs on an energy allocator. These costs should
3 have been allocated on a Salary/Wages allocator. I have not performed a thorough
4 review of the allocation of all cost components. Therefore, expect for the items
5 specifically identified, I have utilized the Company's allocation method to develop the
6 CCROSS that I will discuss later. The fact that I have used a Company proposed
7 allocation of revenues or costs should not be construed as an endorsement.

8 **Q DOES THE COMPANY PROVIDE SUPPORT FOR UTILIZING THE AVERAGE AND**
9 **PEAK METHOD TO ALLOCATE PRODUCTION AND TRANSMISSION PLANT?**

10 A No. The Company simply states in its testimony that it has utilized the Average and
11 Peak method for purposes of allocating production and transmission plant investment
12 because it gives classes recognition for both usage and contribution to peak load.

13 **Q WHAT IS THE BASIC REASONING FOR UTILIZING THE AVERAGE AND PEAK**
14 **(A&P) METHOD FOR ALLOCATING PRODUCTION AND TRANSMISSION**
15 **PLANT?**

16 A Generally, those who endorse the A&P method argue that it reflects resource
17 planning because it accounts for both the coincident peak and the average demand.
18 Typically, the reason for using the A&P method is because this method assumes the
19 electric utility will invest in more expensive types of generating capacity solely
20 because of lower fuel costs associated with that capacity. As a result, this assumes a
21 substitution of capital investment for fuel cost.

1 **Q WHAT ARE THE FLAWS WITH THE A&P METHOD?**

2 **A The basic flaws with utilizing the A&P method are:**

- 3 1. Energy consumption or average demand is double counted.
- 4 2. The A&P method, if viewed as a capital substitution method, fails to
- 5 appropriately recognize the trade-offs between capital and operating costs.
- 6 This is sometimes referred to as a fuel symmetry problem.
- 7 3. The A&P method is an oversimplification of the utility planning process.

8 **Q WHY DO YOU SAY THAT THE A&P METHOD DOUBLE COUNTS AVERAGE**

9 **DEMAND OR ENERGY?**

10 **A Double counting occurs because the average demand, which is equivalent to the year**

11 round energy consumption divided by 8,760 hours, is also a component of the

12 coincident peak demand. By allocating some capital costs relative to average

13 demand, and some relative to coincident peak demand, energy is counted twice –

14 once by itself and the second time as a subset of the coincident peak. If the year-

15 around energy is analogous to base load units which supply capacity on a continuing

16 basis throughout the year, then it follows that the only time when intermediate and

17 peaking units would be needed to meet the system demands when they are in excess

18 of the average year demand. The A&P improperly allocates the cost of this additional

19 capacity relative to the total coincident demand, rather than the excess demand. As

20 a result, the double counting substantially penalizes high load factor customers by

21 assigning them a disproportionate share of costs.

1 **Q TURNING TO YOUR SECOND CRITICISM, HOW DOES THE A&P METHOD, AS A**
2 **CAPITAL SUBSTITUTION METHOD, FAIL TO PROVIDE A SYMMETRICAL**
3 **ALLOCATION OF BOTH CAPITAL AND OPERATING COSTS?**

4 A The A&P method focuses on the allocation of production fixed costs. For example,
5 the A&P method allocates more production plant to high load factor classes than
6 either the coincident peak or an average and excess allocation methods. These
7 methods will be discussed later in my testimony. This result is claimed to be fair by
8 A&P proponents because high load factor customers require more base load capacity
9 and because the capital cost of base load units tend to be higher than peaking plants.
10 However, the A&P method, as applied, makes no attempt to recognize the other side
11 of the capital cost/operating cost trade-off. Base load plants may have above
12 average capital costs, but they usually have below average operating costs relative to
13 peaking units. To ignore the fuel cost differential creates a mismatch between the
14 theory and application.

15 If system planning principles are to be applied in determining the allocation of
16 production plant, it is also logical and consistent to apply the same principles to the
17 allocation of fuel expense. However, this is not done in KCPL's CCOSS. Average
18 fuel expense is allocated to each rate class. That is, each class is allocated the same
19 per unit fuel cost.

20 **Q WHAT WOULD YOU ESTIMATE THE OUTCOME TO BE OF AN ANALYSIS THAT**
21 **WOULD CORRECT THE FUEL SYMMETRY PROBLEM?**

22 A Such an analysis would confirm that there is a symmetrical relationship between the
23 allocation of plant and fuel costs. A low load factor class, which is allocated below

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1 average plant investment, would be allocated above average fuel cost. High load
2 factor customers, by contrast, who are allocated above average plant investment,
3 would be allocated below average fuel cost. By failing to recognize this symmetrical
4 relationship, the A&P method is flawed and is obviously grossly unfair to high load
5 factor customers.

6 To give an analogy, suppose that two different customers are required to rent
7 a fleet of cars. The fleet consists of two types of cars. One type has a high fixed
8 charge per day, and gets better mileage per gallon of gasoline, while the other type
9 has a low fixed charge per day and gets poor mileage. The first type of vehicle is
10 analogous to a base load plant, while the second vehicle is analogous to a peaking
11 plant. The A&P method argues that the customer who drives his/her car a few miles
12 per day should be allocated more gas guzzlers and few of the more efficient cars,
13 with the opposite type of allocation for the customer that will drive many miles per
14 day. While recognizing that the lower load factor customer would pay a lower daily
15 charge for his/her car than the higher load factor customer, the A&P method fails to
16 recognize the lower load factor customer should accordingly pay a higher mileage
17 charge than the higher load factor customer to recognize the higher fuel cost of a gas
18 guzzler. In other words, the A&P method suffers from the fuel symmetry problem.

19 **Q DO UTILITY PLANNERS CONSTRUCT MORE CAPITAL-INTENSIVE CAPACITY**
20 **FOR THE SOLE PURPOSE OF REDUCING FUEL COSTS?**

21 **A** No. This belief is based on an oversimplification of the planning process. In reality,
22 planners are faced with the decision of providing reliable service and minimizing total
23 costs.

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1 Cost minimization is a requirement that the utility provide service at the lowest
2 overall cost. The utility strives to install a mix of generating capacity that, along with
3 its existing generation, yields the lowest total cost. In other words, the economic
4 choice between a base load plant and a peaking plant must consider both capital
5 costs and operating costs.

6 The utility's investment decisions can also be affected by existing generation
7 mix, the availability of a suitable site for the plant, environmental restrictions and fuel
8 diversification, just to mention a few

9 Q IS THE A&P METHOD APPROPRIATE FOR ALLOCATING PRODUCTION AND
10 TRANSMISSION PLANT?

11 A No. It is inappropriate for allocating production plant for the reasons I have previously
12 stated.

13 **Results of KCPL's Cost of Service Study**

14 Q HAVE YOU REVIEWED THE RESULTS OF KCPL'S CCOSS?

15 A Yes. I reviewed the results of KCPL's CCOSS. The results of the CCOSS are
16 summarized on Schedule JTS-1.

17 Q WHAT DO THE RESULTS OF THE CCOSS SHOW?

18 A Schedule JTS-1 shows the results of the Company's CCOSS at both the current and
19 the proposed rates. The CCOSS results include the rate of return, the index of
20 return, and the revenue under and over-collection. A revenue under-collection means

1 a class is providing revenues below its cost of service. An over-collection means that
2 a class is providing revenues in excess of its cost to serve.

3 The results of KCPL's CCOSS show that the residential and lighting classes
4 are currently paying rates that are less than the cost of serving the customers in
5 those classes. All other rate classes are paying rates in excess of cost of service.

6 Q DOES KCPL'S PROPOSED REVENUE ALLOCATION REDUCE THE OVER AND
7 UNDER COLLECTIONS?

8 A No. As shown on **Schedule JTS-1**, KCPL's proposed allocation of the rate increase
9 moves rates further away from cost of service as measured by the differences
10 between the revenues and the cost of providing that service. For example, the Large
11 Power Service class over-collection increases from \$2,705,000 to \$4,757,000 under
12 KCPL's proposed revenue allocation.

13 Q HOW DID KCPL ALLOCATE THE INCREASE IN THIS CASE?

14 A As indicated in the testimony of KCPL witness Tim Rush, the Company is
15 recommending an equal percentage increase to all customer classes with minimal
16 changes to rate design.

17 **Revised Allocation of Production and Transmission Costs**

18 Q WHAT METHOD DO YOU PROPOSE FOR ALLOCATING KCPL'S PRODUCTION
19 AND TRANSMISSION COSTS?

20 A I would support an allocation of fixed production and transmission costs using either
21 the coincident peak method, or the average and excess demand (A&E) method.

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1 **Q PLEASE DESCRIBE THE COINCIDENT PEAK METHOD.**

2 A The coincident peak method uses each customer class coincident peak demand to
3 allocate the production and transmission fixed costs.

4 **Q WHY DO YOU BELIEVE THE COINCIDENT PEAK METHOD IS APPROPRIATE**
5 **FOR ALLOCATING PRODUCTION AND TRANSMISSION COSTS?**

6 A The method used to allocate production and transmission cost should be consistent
7 with the principles of cost causation. The allocation method should reflect the
8 contribution of each customer class to the demands that cause utilities to incur
9 demand or capacity-related costs.

10 Production and transmission investments are sized to meet the maximum
11 simultaneous demands of all customers on the system. Production units and
12 transmission lines are normally rated by their maximum demands in MW. Typically,
13 these types of investments are not rated by average demand, or the amount of
14 energy that is consumed during the year, divided by 8,760 hours.

15 **Q WHEN UTILIZING A COINCIDENT PEAK DEMAND, WHAT FACTORS SHOULD**
16 **BE CONSIDERED IN ALLOCATING THE PRODUCTION AND TRANSMISSION**
17 **COSTS?**

18 A The selection of the coincident peak allocation factor should properly reflect the
19 operating characteristics of the loads that are served by the utility. If a utility has a
20 higher summer peak relative to the demands during the other times during the year,
21 then the production and transmission fixed cost should be allocated based on each
22 customer's contribution to the summer peak. If a utility has predominant peaks in

1 both the summer and winter months, then the allocation of the production and
2 transmission fixed cost should be based on both the summer and winter peak
3 periods

4 **Q WHAT MONTHS DID YOU UTILIZE TO DEVELOP YOUR COINCIDENT PEAK**
5 **ALLOCATOR?**

6 **A** For KCPL, the production and transmission costs should be allocated based on each
7 customer classes' peak demand during the summer months (June through
8 September). The energy costs would be allocated based on energy usage as
9 proposed by KCPL.

10 **Q WHY DID YOU CHOOSE THE MONTHS OF JUNE THROUGH SEPTEMBER?**

11 **A** **Schedule JTS-2** is an analysis of the monthly loads of KCPL's system for the historic
12 period 1996 through 2005. A review of this load data indicates a dominance of the
13 summer peaks of June, July, August and September on KCPL's system. The peak
14 loads during these months do not go below 80% of the highest peak, except for
15 September 2003. This clearly indicates that KCPL's demand peaks during these four
16 months. These four summer peaks are the primary driver for determining the amount
17 of capacity that KCPL needs to adequately provide service to its customers. It is
18 these peaks that cause KCPL to incur additional cost that must be passed on to their
19 ratepayers. Therefore, it is critical that customers receive proper price signals as to
20 what is causing their rates to increase. To send the appropriate price signals to
21 customers, it is appropriate to allocate their fixed production and transmission costs
22 based on a four-month coincident peak allocator.

1 **Q PLEASE DESCRIBE SCHEDULE JTS-2.**

2 **A As previously stated, Schedule JTS-2 is an analysis of KCPL's monthly peak**
3 **demands. Page 1 of Schedule JTS-2 shows KCPL's average monthly peak**
4 **demands for the period 1996 through 2005. Page 2 of Schedule JTS-2 shows each**
5 **year's peak demand as a percentage of the maximum peak demand in any year. As**
6 **page 2 shows, the months of June through September are the dominant months in**
7 **determining KCPL's capacity needs.**

8 **Q HAVE YOU PERFORMED A CCROSS ALLOCATING THE PRODUCTION COST**
9 **AND TRANSMISSION FIXED COSTS ON A FOUR COINCIDENT PEAK**
10 **ALLOCATOR?**

11 **A Yes. Schedule JTS-3 is a result of my CCROSS study at present rates for Missouri**
12 **customers utilizing the four coincident peak allocation method for fixed production**
13 **and transmission cost.**

14 **Q PLEASE BRIEFLY DESCRIBE SCHEDULE JTS-3.**

15 **A Schedule JTS-3 shows the results of the CCOS study utilizing the four-month**
16 **coincident peak allocator. Schedule JTS-3 shows the relative rates of return, the**
17 **indices of return, and the change in revenues that would be needed to produce**
18 **equalized rates of return. As Schedule JTS-3 shows, the Residential class is**
19 **providing revenues below their cost of service. All other classes are providing**
20 **revenues in excess of their class cost of service.**

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1 Q HAVE YOU MADE ANY OTHER REVISIONS TO THE CCOSS?

2 A Yes. As I previously indicated, KCPL has allocated certain A&G costs utilizing an
3 energy allocation factor. The energy allocation factor was used for the following A&G
4 expenses:

- 5 1. Account 921 – Office Expense.
- 6 2. Account 922 – Administrative Expense Transfer-Credits.
- 7 3. Account 923 – Outside Services.
- 8 4. Account 930.2 – Miscellaneous General Expenses – Others.
- 9 5. Account 931 – Rents.

10 I revised this allocation factor and utilized a Salary/Wages allocator. It should be
11 noted that KCPL utilized Salary/Wages to allocate some of their A&G expenses in
12 their CCOSS. Finally, the use of Salary/Wages to allocate these costs is consistent
13 with the allocation method supported by the National Association of Regulatory
14 Commissioners in their Electric Utility Cost Allocation Manual.

15 Q HAVE YOU ALSO PERFORMED A CCOSS UTILIZING THE AVERAGE AND
16 EXCESS DEMAND METHOD?

17 A Yes. The results of that CCOSS are summarized on Schedule JTS-4.

18 Q BEFORE YOU DISCUSS THE RESULTS OF THE A&E CCOSS, PLEASE BRIEFLY
19 DESCRIBE THE A&E METHOD.

20 A The A&E method allocates cost to the rate classes utilizing an average demand
21 component and an excess demand component. This theory allocates plants
22 recognizing that utility plant capacity serves a dual purpose.

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1 The average demand component is simply the total kWh usage by rate class,
2 divided by the total number hours in the year. This essentially represents the amount
3 of capacity that would be needed to produce energy if the same demand were taken
4 at the same rate each hour of the year. Under this allocation method, it essentially
5 assumes that each class uses energy at a constant 100% load factor.

6 The second component of each classes' allocation factor is the excess
7 demand factor. It is the demand that is in excess of the average demand. This
8 component provides for the allocation of cost that represents each class's peak
9 usage or contribution to peak in excess of average demand.

10 **Q PLEASE EXPLAIN WHY THE A&E METHOD MAY BE APPROPRIATE FOR**
11 **ALLOCATING PRODUCTION AND TRANSMISSION COSTS.**

12 **A**Assume that you have two rate classes that have different usage patterns and both
13 classes utilize the same amount of energy. In addition, assume Class A has a 100%
14 load factor, while Class B's load factor is less, but has a dominant peak period.
15 Figure 1 below shows the different usage patterns.

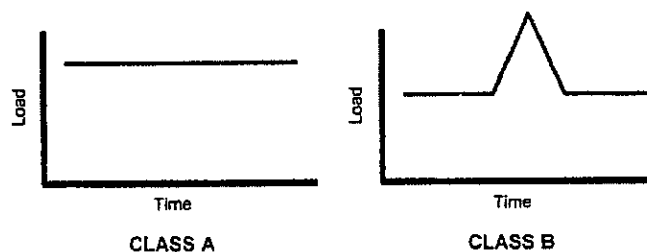


Figure 1

16 Because both classes use the same total amount of energy, both classes
17 have the same average demand. However, a greater maximum demand is imposed

1 on the system by Class B. A greater maximum demand imposes greater costs on the
2 utility that must be passed on to ratepayers. This is because the utility must have
3 sufficient capacity to meet the maximum demands of all of its customers. In addition,
4 there may also be higher costs incurred by the utility because of the variation in
5 usage patterns from one class to another.

6 The A&E method provides a way to allocate the additional production capacity
7 cost of the system in proportion to the peaks that each customer class imposes that
8 are in excess of their average demand.

9 Q HAVE YOU PROVIDED THE RESULTS OF THE CCROSS USING THE A&E
10 ALLOCATOR?

11 A Yes. Schedule JTS-4 shows the results of the cost of service study using the A&E
12 factor to allocate fixed production and transmission costs. Schedule JTS-4 shows
13 the rates of return, the indices of return, and the change in revenues needed to
14 equalize the rate of return for all rate classes.

15 As Schedule JTS-4 shows, the Residential class is providing revenues less
16 than their cost of service. The Small General Service Class is almost providing
17 revenues equal to its cost of service. The Medium General Service, Large General
18 Service, Large Power Service, and Lighting classes are providing revenues in excess
19 of their cost of service. Therefore, these classes would need to see rate decreases in
20 excess of 9% to bring their rates to cost of service.

1 Q DID YOU MAKE ANY OTHER REVISIONS TO THE COST OF SERVICE STUDY
2 THAT USES THE A&E METHOD, OTHER THAN THE CHANGE IN THE
3 PRODUCTION AND TRANSMISSION ALLOCATION FACTORS?

4 A Yes. I made a change to the allocation of certain A&G expenses that were previously
5 discussed. That is, I revised the allocation factors utilized to allocate certain A&G
6 expenses from an energy allocator to a Salary/Wages allocator.

7 Q WHAT IS YOUR PROPOSAL REGARDING WHICH CCROSS THE COMMISSION
8 SHOULD ADOPT FOR DETERMINING THE RATE REVENUE RESPONSIBILITY
9 OF EACH RATE CLASS?

10 A Although I prefer the coincident peak method, I recommend the Commission utilize
11 the results of the A&E method cost of service study for purposes of establishing each
12 rate class's revenue responsibility.

13 It should be noted that KCPL indicates the Company intends to file annual rate
14 cases for the next few years. Given that customers may be seeing annual base rate
15 increases, it is critical that the Commission adopt a cost of service method that is
16 reflective of cost causation. Therefore, I recommend that the Commission require
17 KCPL in its future rate proceedings file a cost of service study utilizing the A&E
18 method for allocating production and transmission costs for purposes of determining
19 each rate class's revenue responsibility.

1 **Revenue Allocation**

2 Q HOW DOES THE COMPANY PROPOSE TO ALLOCATE ANY RATE INCREASE
3 THAT THE COMMISSION MAY GRANT IN THIS PROCEEDING?

4 A KCPL is recommending an equal percentage increase to all customer classes. As a
5 result, the Company has allocated its overall increase of 11.5% to all customer
6 classes. My preference is to move all rates to cost of service.

7 Q IF THE COMMISSION DETERMINES THAT KCPL'S OVERALL REVENUE
8 INCREASE SHOULD BE LESS THAN ITS \$55.8 MILLION REQUESTED, HOW
9 SHOULD THE INCREASE BE ALLOCATED?

10 A If the Commission determines the total increase should be less than KCPL's
11 requested amount, I recommend that any reduction from the requested amount
12 should be allocated to those classes whose rates are above cost of service or have a
13 *rate of return in excess of the overall rate of return that KCPL is proposing*. Under
14 this scenario, rates would move closer to cost of service. The results of the average
15 and excess CCROSS should be used to allocate any amount that is less than the level
16 requested.

17 Q HAVE YOU PREPARED A SCHEDULE THAT SHOWS HOW YOU WOULD
18 ALLOCATE ANY RATE REDUCTION FROM THE AMOUNT REQUESTED BY
19 KCPL?

20 A Yes. **Schedule JTS-5** provides an example of how a reduction of \$20 million from
21 the amount that KCPL is requesting in this case would be allocated to customer
22 classes based on my recommendation.

James T. Selecky
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1 The allocation of a \$20 million reduction from KCPL's requested amount
2 would be based on the cost of service results as shown on **Schedule JTS-4**. The
3 reduction in the revenue requirement would be used to reduce KCPL's proposed
4 revenue for those rate classes that are above cost of service, while maintaining
5 KCPL's recommended revenue responsibility for those rate classes that are below
6 cost of service.

7 **Q WHAT IS YOUR RECOMMENDATION IF THE DECREASE IN KCPL'S PROPOSED**
8 **REVENUE REQUIREMENT IS SUFFICIENT TO BRING ALL RATES TO COST OF**
9 **SERVICE?**

10 **A If the reduction to KCPL's requested revenue requirement is sufficient to bring all rate**
11 **classes to cost of service, then any additional reduction should be allocated based on**
12 **rate base to all classes.**

13 **Q DOES THIS CONCLUDE YOUR DIRECT TESTIMONY AT THIS TIME?**

14 **A Yes, it does.**

Appendix A

Qualifications of James T. Selecky

1 **Q PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.**

2 **A James T. Selecky. My business address is 1215 Fern Ridge Parkway, Suite 208,**
3 **St. Louis, Missouri 63141.**

4 **Q PLEASE STATE YOUR OCCUPATION.**

5 **A I am a consultant in the field of public utility regulation and am a principal with the firm**
6 **of Brubaker & Associates, Inc. (BAI), energy, economic and regulatory consultants.**

7 **Q PLEASE STATE YOUR EDUCATIONAL BACKGROUND AND PROFESSIONAL**
8 **EMPLOYMENT EXPERIENCE.**

9 **A I graduated from Oakland University in 1969 with a Bachelor of Science degree with a**
10 **major in Engineering. In 1978, I received the degree of Master of Business Admin-**
11 **istration with a major in Finance from Wayne State University.**

12 I was employed by The Detroit Edison Company (DECo) in April of 1969 in its
13 Professional Development Program. My initial assignments were in the engineering
14 and operations divisions where my responsibilities included evaluation of equipment
15 for use on the distribution and transmission system; equipment performance testing
16 under field and laboratory conditions; and troubleshooting and equipment testing at
17 various power plants throughout the DECo system. I also worked on system design
18 and planning for system expansion.

19 In May of 1975, I transferred to the Rate and Revenue Requirement area of
20 DECo. From that time, and until my departure from DECo in June 1984, I held
21 various positions which included economic analyst, senior financial analyst,

1 supervisor of the Rate Research Division, supervisor of the Cost-of-Service Division
2 and director of the Revenue Requirement Department. In these positions, I was
3 responsible for overseeing and performing economic and financial studies and book
4 depreciation studies; developing fixed charge rates and parameters and procedures
5 used in economic studies; providing a financial analysis consulting service to all
6 areas of DECo; developing and designing rate structure for electrical and steam
7 service; analyzing profitability of various classes of service and recommending
8 changes therein; determining fuel and purchased power adjustments; and all aspects
9 of determining revenue requirements for ratemaking purposes.

10 In June of 1984, I joined the firm of Drazen-Brubaker & Associates, Inc
11 (DBA). In April 1995 the firm of Brubaker & Associates, Inc. (BAI) was formed. It
12 includes most of the former DBA principals and staff. At DBA and BAI I have testified
13 in electric, gas and water proceedings involving almost all aspects of regulation. I
14 have also performed economic analyses for clients related to energy cost issues.

15 In addition to our main office in St. Louis, the firm also has branch offices in
16 Phoenix, Arizona; Corpus Christi, Texas; and Plano, Texas.

17 **Q HAVE YOU PREVIOUSLY APPEARED BEFORE A REGULATORY COMMISSION?**

18 **A** Yes. I have testified on behalf of DECo in its steam heating and main electric cases.
19 In these cases I have testified to rate base, income statement adjustments, changes
20 in book depreciation rates, rate design, and interim and final revenue deficiencies.

21 In addition, I have testified before the regulatory commissions of the States of
22 Colorado, Connecticut, Georgia, Illinois, Indiana, Iowa, Kansas, Louisiana, Maryland,
23 Massachusetts, Missouri, New Hampshire, New Jersey, North Carolina, Ohio,
24 Oklahoma, Oregon, Tennessee, Texas, Utah, Washington, Wisconsin, and Wyoming,
25 and the Provinces of Alberta, Nova Scotia and Saskatchewan. I also have testified

Appendix A
James T. Selecky
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1 before the Federal Energy Regulatory Commission. In addition, I have filed testimony
2 in proceedings before the regulatory commissions in the States of Florida, Montana,
3 New York and Pennsylvania and the Province of British Columbia. My testimony has
4 addressed revenue requirement issues, cost of service, rate design, financial
5 integrity, accounting-related issues, merger-related issues, and performance
6 standards. The revenue requirement testimony has addressed book depreciation
7 rates, decommissioning expense, O&M expense levels, and rate base adjustments
8 for items such as plant held for future use, working capital, and post test year
9 adjustments. In addition, I have testified on deregulation issues such as stranded
10 cost estimates and rate design.

11 **Q ARE YOU A REGISTERED PROFESSIONAL ENGINEER?**

12 **A** Yes, I am a registered professional engineer in the State of Michigan.

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KANSAS CITY POWER & LIGHT COMPANY - MISSOURI

Rates of Return, Indexes and Subsidies Using the Company Filed Cost of Service Study (Dollars in Thousands)

Line	Rate Classes	Rate Base (1)	Operating Revenue (2)	Operating Expenses (3)	Net Operating Income (4)	Present Rates			Company Proposed Increase (8)	Proposed Operating Income (9)	KCPL Proposed Rates		
						Rate of Return (5)	Index (6)	(Under) Over Collections (7)			Rate of Return (10)	Index (11)	(Under) Over Collections (12)
1	Residential	\$ 508,385	\$ 214,112	\$ 186,167	\$ 27,945	5.50%	74	\$ (15,948)	\$ 19,913	\$ 40,130	7.89%	76	\$ (20,217)
2	Small General Service	90,679	41,685	34,197	7,488	8.26%	111	1,247	4,215	10,067	11.10%	108	1,149
3	Medium General Service	137,945	73,557	59,258	14,300	10.37%	140	6,650	7,182	18,694	13.55%	131	7,271
4	Large General Service	234,737	131,190	110,091	21,099	8.99%	121	6,030	12,587	28,801	12.27%	119	7,452
5	Large Power Service	190,988	118,207	102,387	15,819	8.28%	112	2,705	11,136	22,633	11.85%	115	4,757
6	Lighting	9,297	6,648	6,378	270	2.91%	39	(685)	716	708	7.62%	74	(411)
7	Total Missouri	\$ 1,172,031	\$ 585,399	\$ 498,477	\$ 86,922	7.42%	100	\$ 0	\$ 55,749	\$ 121,034	10.33%	100	\$ (0)
8	Tax Factor	1.634290											

KANSAS CITY POWER & LIGHT COMPANY

Monthly Peak Demands (MW)

<u>Month</u>	<u>1996</u>	<u>1997</u>	<u>1998</u>	<u>1999</u>	<u>2000</u>	<u>2001</u>	<u>2002</u>	<u>2003</u>	<u>2004</u>	<u>2005</u>	<u>Average</u>
Jan	1,916	2,002	1,914	2,171	2,026	2,233	2,105	2,268	2,335	2,313	2,128
Feb	1,956	1,812	1,778	1,954	1,937	2,147	2,095	2,165	2,235	2,186	2,027
Mar	1,820	1,703	1,940	1,859	1,776	1,981	2,036	2,095	1,858	2,003	1,907
Apr	1,608	1,662	1,628	1,778	1,885	1,988	2,131	2,011	1,895	2,042	1,863
May	2,328	1,723	2,734	1,910	2,936	2,579	2,779	2,556	2,734	2,615	2,489
Jun	2,795	2,816	2,987	2,766	2,958	2,858	3,083	3,109	3,009	3,338	2,972
Jul	2,987	3,044	3,136	3,251	3,230	3,304	3,335	3,426	3,384	3,512	3,261
Aug	2,803	2,929	3,175	3,084	3,374	3,352	3,333	3,610	3,376	3,426	3,246
Sep	2,489	2,761	2,993	2,961	3,269	2,722	3,139	2,617	2,874	3,007	2,883
Oct	1,810	2,405	1,849	1,963	2,352	1,920	2,665	2,018	1,977	2,754	2,171
Nov	1,846	1,761	1,763	1,812	2,045	1,988	1,957	1,994	2,129	2,209	1,950
Dec	2,012	1,933	2,117	2,085	2,382	1,934	2,055	2,186	2,376	2,563	2,164

KANSAS CITY POWER & LIGHT COMPANY

Monthly Peak Demands as a Percentage of Maximum Annual Peak

<u>Month</u>	<u>1996</u>	<u>1997</u>	<u>1998</u>	<u>1999</u>	<u>2000</u>	<u>2001</u>	<u>2002</u>	<u>2003</u>	<u>2004</u>	<u>2005</u>	<u>Average</u>
Jan	64.1%	65.8%	60.3%	66.8%	60.0%	66.6%	63.1%	62.8%	69.0%	65.9%	65.3%
Feb	65.5%	59.5%	56.0%	60.1%	57.4%	64.1%	62.8%	60.0%	66.0%	62.2%	62.1%
Mar	60.9%	55.9%	61.1%	57.2%	52.6%	59.1%	61.0%	58.0%	54.9%	57.0%	58.5%
Apr	53.8%	54.6%	51.3%	54.7%	55.9%	59.3%	63.9%	55.7%	56.0%	58.1%	57.1%
May	77.9%	56.6%	86.1%	58.8%	87.0%	76.9%	83.3%	70.8%	80.8%	74.5%	76.3%
Jun	93.6%	92.5%	94.1%	85.1%	87.7%	85.3%	92.4%	86.1%	88.9%	95.0%	91.1%
Jul	100.0%	100.0%	98.8%	100.0%	95.7%	98.6%	100.0%	94.9%	100.0%	100.0%	100.0%
Aug	93.8%	96.2%	100.0%	94.9%	100.0%	100.0%	99.9%	100.0%	99.8%	97.6%	99.5%
Sep	83.3%	90.7%	94.3%	91.1%	96.9%	81.2%	94.1%	72.5%	84.9%	85.6%	88.4%
Oct	60.6%	79.0%	58.2%	60.4%	69.7%	57.3%	79.9%	55.9%	58.4%	78.4%	66.6%
Nov	61.8%	57.9%	55.5%	55.7%	60.6%	59.3%	58.7%	55.2%	62.9%	62.9%	59.8%
Dec	67.4%	63.5%	66.7%	64.1%	70.6%	57.7%	61.6%	60.6%	70.2%	73.0%	66.4%

KANSAS CITY POWER & LIGHT COMPANY - MISSOURI

Class Cost of Service Study for Missouri Customers 4 Coincident Peak Scenario For the Test Year Ended September 30, 2005 (Dollars in Thousands)

<u>Line</u>	<u>Description</u>	<u>Missouri Retail (1)</u>	<u>Residential (2)</u>	<u>Small General Service (3)</u>	<u>Medium General Service (4)</u>	<u>Large General Service (5)</u>	<u>Large Power Service (6)</u>	<u>Lighting (7)</u>
1	Total Rate Base	\$ 1,172,031	\$ 560,673	\$ 88,903	\$ 135,506	\$ 218,276	\$ 162,989	\$ 5,684
	Operating Revenues:							
2	Adjusted Sales Revenues	\$ 483,656	\$ 171,390	\$ 36,586	\$ 62,431	\$ 108,729	\$ 98,464	\$ 6,057
3	Other Revenues	<u>101,743</u>	<u>43,863</u>	<u>5,062</u>	<u>11,089</u>	<u>22,105</u>	<u>19,116</u>	<u>508</u>
4	Total Operating Revenue	\$ 585,399	\$ 215,253	\$ 41,648	\$ 73,520	\$ 130,834	\$ 117,580	\$ 6,564
5	Total Operating Expenses	\$ 498,477	\$ 196,462	\$ 34,025	\$ 58,802	\$ 106,763	\$ 96,627	\$ 5,798
6	Operating Income	\$ 86,922	\$ 18,791	\$ 7,623	\$ 14,718	\$ 24,071	\$ 20,952	\$ 767
7	Rate of Return	7.42%	3.35%	8.57%	10.86%	11.03%	12.86%	13.49%
8	Index Rate of Return	100	45	116	146	149	173	182
9	Change Needed to Equalize ROR	\$ -	\$ 37,246	\$ (1,682)	\$ (7,629)	\$ (12,883)	\$ (14,487)	\$ (564)
10	Percent of Sales Revenue	0.00%	21.73%	-4.60%	-12.22%	-11.85%	-14.71%	-9.31%

KANSAS CITY POWER & LIGHT COMPANY - MISSOURI

Class Cost of Service Study for Missouri Customers Traditional Average and Excess Peak Scenario For the Test Year Ended September 30, 2005 (Dollars in Thousands)

Line	Description	Missouri Retail (1)	Residential (2)	Small General Service (3)	Medium General Service (4)	Large General Service (5)	Large Power Service (6)	Lighting (7)
1	Total Rate Base	\$ 1,172,031	\$ 555,970	\$ 92,822	\$ 138,141	\$ 216,606	\$ 162,807	\$ 5,684
	Operating Revenues:							
2	Adjusted Sales Revenues	\$ 483,656	\$ 171,390	\$ 36,586	\$ 62,431	\$ 108,729	\$ 98,464	\$ 6,057
3	Other Revenues	101,743	43,757	5,151	11,148	22,067	19,112	508
4	Total Operating Revenue	\$ 585,399	\$ 215,147	\$ 41,737	\$ 73,579	\$ 130,796	\$ 117,575	\$ 6,564
5	Total Operating Expenses	\$ 498,477	\$ 195,644	\$ 34,707	\$ 59,260	\$ 106,472	\$ 96,596	\$ 5,798
6	Operating Income	\$ 86,922	\$ 19,503	\$ 7,030	\$ 14,319	\$ 24,324	\$ 20,980	\$ 767
7	Rate of Return	7.42%	3.51%	7.57%	10.37%	11.23%	12.89%	13.49%
8	Index Rate of Return	100	47	102	140	151	174	182
9	Change Needed to Equalize ROR	\$ -	\$ 35,513	\$ (238)	\$ (6,658)	\$ (13,499)	\$ (14,554)	\$ (564)
10	Percent of Sales Revenue	0.00%	20.72%	-0.65%	-10.66%	-12.41%	-14.78%	-9.31%

KANSAS CITY POWER & LIGHT - MISSOURI

Allocation Of Reduction To KCPL Proposed Increase Based On Average and Excess COSS

<u>Line</u>	<u>Rate Class</u> (1)	<u>Revenue Deviation From CCOSS (Thousands)</u> (2)	<u>Revenue In Excess Of CCOSS (Thousands)</u> (3)	<u>Revenue In Excess Of CCOSS Allocation</u> (4)	<u>Revenue Reduction (Thousands)</u> (5)	<u>Rate Base (Thousands)</u> (6)	<u>Rate Base Allocation</u> (7)
1	Residential	\$35,513				\$555,970	47.44%
2	Small General	(\$238)	\$238	0.67%	\$134	\$92,822	7.92%
3	Medium General	(\$6,658)	\$6,658	18.75%	\$3,750	\$138,141	11.79%
4	Large General	(\$13,499)	\$13,499	38.01%	\$7,602	\$216,606	18.48%
5	Large Power	(\$14,554)	\$14,554	40.98%	\$8,196	\$162,807	13.89%
7	Lighting	<u>(\$564)</u>	<u>\$564</u>	1.59%	\$318	<u>\$5,684</u>	<u>0.48%</u>
8	Total	\$0	\$35,513	100.00%	\$20,000	\$1,172,030	100.00%

Note: Positive revenue deviation means that a class revenue is below cost of service.