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Witness: Mark A. Foltz
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MISSOURI PUBLIC SERVICE COMMISSION

CASE NO.: ER-2012-0174

REBUTTAL TESTIMONY

OF

MARK A. FOLTZ

ON BEHALF OF

KANSAS CITY POWER & LIGHT COMPANY

**Kansas City, Missouri
September 2012**

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Case No. ER-2012-0174

1 **Q: Please state your name and business address.**

2 A: My name is Mark A. Foltz. My business address is 1200 Main, Kansas City, Missouri
3 64105.

4 **Q: By whom and in what capacity are you employed?**

5 A: I am employed by Kansas City Power & Light Company (“KCP&L” or “Company”) as
6 Senior Project Director.

7 **Q: What are your responsibilities?**

8 A: I am currently assigned as finance functional lead to the program management office in a
9 project to re-implement the Company’s major accounting, budgeting and enterprise
10 reporting systems. I also continue to hold responsibility for benefit plan financial
11 administration and am involved in benefit plan accounting, reporting and rate-making
12 matters.

13 **Q: Please describe your education, experience and employment history.**

14 A: I received a Bachelor of Science in Business Administration with a major in accounting
15 in 1980 and a Masters of Arts in Accountancy in 1981 from the University of Missouri-
16 Columbia. I passed the Certified Public Accounting examination in May 1981 and
17 received a permit to practice in 1983. I was employed with Arthur Andersen & Company
18 in Kansas City, Missouri, from 1981 through 1987 with assignments primarily in the
19 regulated industries practice. I was employed with Mark VII, Inc., a publicly-held long-

1 haul, truckload carrier and logistics company headquartered in St. Joseph, Missouri from
2 1987 through 1995 leaving as Assistant Vice President of Finance. I was employed as
3 Vice President of Finance and Corporate Secretary with TransFinancial Holdings, Inc., a
4 publicly-held company headquartered in Lenexa, Kansas with ownership of a regional,
5 less-than-truckload carrier and insurance premium finance company from 1995 through
6 2000. In 2000, I joined Aquila, Inc. as Manager of External Reporting and Corporate
7 Accounting and progressed to the role of Vice President & Controller at the time of the
8 merger with Great Plains Energy Incorporated in July 2008. Subsequent to the merger I
9 served as Assistant Controller for the Company and am currently serving in the role of
10 Senior Project Director. I am a member of the American Institute of Certified Public
11 Accountants and hold the designation as a Certified Global Management Accountant. I
12 have substantial experience throughout my career in accounting, external reporting,
13 employee benefit plan accounting and administration and income tax compliance.

14 **Q: Have you previously testified in a proceeding before the Missouri Public Service**
15 **Commission (“Commission” or “MPSC”) or before any other utility regulatory**
16 **agency?**

17 A: No.

18 **Q: What is the purpose of your Rebuttal Testimony?**

19 A: I will rebut positions in the Direct Testimony of Charles R. Hyneman of the Missouri
20 Public Service Commission Staff (“Staff”) (contained in the Staff’s Revenue
21 Requirement/Cost of Service report) related to qualified pension costs, Supplemental
22 Executive Retirement Plan (“SERP”) costs and other post-employment benefit (“OPEB”)
23 plan costs for the Wolf Creek Generating Station.

1 Qualified Pension Costs

2 **Q: What position did Mr. Hyneman take regarding the Company’s salary escalation**
3 **assumptions used to calculate the Company’s pension cost?**

4 A: Mr. Hyneman has proposed an adjustment to the Company’s pension cost to lower the
5 salary escalation assumption, based on a comparison of KCP&L’s salary assumption to
6 that of other Missouri utilities.

7 **Q: What does the salary escalation assumption represent?**

8 A: The Company is required under Generally Accepted Accounting Principles (“GAAP”) to
9 use its best estimate of the salary escalation assumption, which represents the overall rate
10 of increase in compensation for the Company’s eligible employees over their expected
11 service period. Financial Accounting Standards Board (“FASB”) Accounting Standards
12 Codification 715, formerly identified as Statement of Financial Accounting Standards
13 No. 87 (“FAS 87”), states that *“Assumed compensation levels shall reflect an estimate of*
14 *the actual future compensation levels of the individual employees involved, including*
15 *future changes attributed to general price levels, productivity, seniority, promotion, and*
16 *other factors.”* While the current economic environment should be taken into
17 consideration, this estimate is to be reflective of the Company’s best estimate of future
18 compensation levels over the long-term.

19 **Q: Does the salary assumption encompass much more than just annual salary increases**
20 **due to merit?**

21 A: Yes. An annual salary increase due to merit is only one factor that impacts the salary
22 assumption. There are other factors that also influence the degree of salary changes
23 throughout an employee’s career. Employees also receive salary increases due to

1 promotions within their department or transfers to more highly compensated jobs
2 elsewhere in the corporation. In addition, other factors come into play such as the
3 employee's level of seniority and placement within an employee's job salary range.
4 These other factors make it difficult to compare one company's salary assumption with
5 that of another company.

6 **Q: How is the salary assumption used to calculate pension cost?**

7 A: The Company's qualified pension plans are "final-pay plans" which means that the level
8 of pension benefits under the plans are determined based on the level of compensation of
9 employees over specified periods immediately preceding their retirement or separation
10 from the Company. FAS 87 states that "The service cost component of net periodic
11 pension cost and the projected benefit obligation shall reflect future compensation levels
12 to the extent that the pension benefit formula defines pension benefits wholly or partially
13 as a function of future compensation levels (that is, for a final-pay plan or a career-
14 average-pay plan)." The salary escalation assumption is one of many assumptions used
15 to calculate current pension cost but does not impact the ultimate value or cost of an
16 employee's pension benefit which is determined on actual compensation and service.

17 **Q: What was the Company's estimate of the salary escalation assumption based on?**

18 A: The Company considers the actual demographics of employees participating in the plans,
19 past experience in the plans and the Company's best judgment of expected future
20 compensation changes. With regard to past actual salary escalation experience in the
21 plans, the Company's actuary computes average total pay increases for continuing active
22 employees as the change in base salary year over year for those employees at the end of

1 each plan year that were participants in the plans at the beginning of the plan year. For
2 the Company's non-union pension plan the recent increases were as follows:

For valuation 10/1/YYYY	2011	2010	2009	2008	2007
Continuing Active Salary Increase	3.43%	4.52%	4.77%	5.51%	5.12%

3 For the Company's union pension plan the recent increases were as follows:

For valuation 10/1/YYYY	2011	2010	2009	2008
Continuing Active Salary Increase	4.66%	4.77%	5.27%	7.23%

4
5 **Q: How do the current Company assumptions compare to the historical actual salary**
6 **escalations provided in the table above?**

7 A: The current salary escalation assumptions are lower than historical averages in all but one
8 year of the historical tables provided above.

9 **Q: How has the salary escalation assumption changed over recent years?**

10 A: The Company reviews the salary escalation assumption and other assumptions each year
11 in connection with the annual actuarial valuation. In 2010, the Company decreased the
12 salary escalation assumption for the management pension plan from 4.25% to 4.00%
13 based on the decreasing trend of historical increases and its view of future increases. The
14 Company will continue to review these assumptions each year.

15 **Q: Why is it inappropriate to base the Company's salary escalation assumption on the**
16 **assumptions used by other companies?**

17 A: The determination of assumptions to be used in calculating the Company's pension cost
18 should be based on the Company's specific facts and circumstances and as required by
19 FAS 87 "shall reflect an estimate of the actual future compensation levels of the
20 individual employees involved". The Company does not have knowledge of the other
21 companies' demographics or insight as to how other companies view future

1 compensation increases. Using other companies' assumptions is clearly not consistent
2 with GAAP and, therefore, it is inappropriate to base assumptions regarding the
3 Company's pension plans on the assumptions used by other companies, especially when
4 actual historic company amounts have been higher than the current assumptions being
5 used. Also, as discussed above, many factors influence salary adjustments other than
6 merit increase, and those factors can vary widely among companies, rendering company
7 comparisons of dubious value.

8 **Q: What is the value of this issue?**

9 A: Mr. Hyneman's reduction of the salary assumption reduced the Missouri jurisdictional
10 revenue requirement by \$1.1 million.

11 **Supplemental Executive Retirement Plan Pension Costs**

12 **Q: What is the purpose of this portion of your testimony?**

13 A: I will rebut Mr. Hyneman's position which denied any recovery of SERP costs paid as
14 lump-sum payments.

15 **Q: Why is it necessary for Staff and the Company to make an adjustment for SERP
16 separately from the adjustment for other pension costs?**

17 A: Pension costs, including SERP, are calculated by the Company's actuaries based on the
18 provisions of GAAP as codified in FASB Accounting Standards Codification 715,
19 formerly identified as Statement of Financial Accounting Standards No. 87. Staff
20 believes it is more correct to exclude SERP costs from the current period pension costs
21 calculated by the actuaries because, unlike qualified pension costs which are funded to a
22 pension trust, SERP costs are not funded until time of benefit payment.

1 **Q: Do you concur with this practice?**

2 A: The Company has not challenged this position.

3 **Q: What position did Mr. Hyneman take?**

4 A: Mr. Hyneman included in Cost of Service only an annualized level of actual monthly-
5 recurring SERP payments made by KCP&L to its former executives and other highly
6 compensated former employees.

7 **Q: Do you consider the Mr. Hyneman's SERP adjustment to be appropriate?**

8 A: No, I do not because it disallows recovery of all lump-sum SERP payments. Although
9 Mr. Hyneman did not discuss it in the Cost of Service Report, his adjustment allows
10 recovery only of the monthly annuity SERP payments, thereby excluding a significant
11 portion of the SERP benefit payments. If recovery of SERP is on a cash basis, then total
12 payments should be allowed regardless of payment method.

13 **Q: How is the form of benefit payment determined?**

14 A: Under the plan design, employees becoming eligible to participate in the SERP plan are
15 required to make an election as to the form of payment of their future benefit, annuity or
16 lump-sum.

17 **Q: How does the form of benefit payment affect the overall cost of the SERP to the
18 Company?**

19 A: The form of benefit payment, annuity or lump-sum, is not intended to impact the cost of
20 the SERP benefit to the Company as the lump-sum payment is determined as a
21 discounted value of annuity benefit calculated based on the years of service and
22 compensation benefit formula. Therefore, Staff's position to allow recovery of SERP

1 annuity payments but not lump-sum payments is inconsistent and unreasonable. SERP
2 payments should be recoverable, regardless of the employee's payment election.

3 **Q: What makes this particularly significant?**

4 A: Between 2002 and 2012 all but three SERP-eligible retiring employees elected lump-sum
5 payments. In 2011, three eligible employees elected an annuity. All but one current
6 eligible employee has elected to receive their future benefit payments as a lump-sum.
7 Consequently, there must be a basis for systematic recovery of lump-sum payments.

8 **Q: What alternate position is more appropriate for SERP costs?**

9 A: The Company proposes recovery of an annualized amount that includes monthly annuity
10 payments and a normalized level of lump-sum payments. The Company has proposed
11 use of a three-year average to recover lump-sum SERP payments. We believe that this
12 averaging method has the same effect as the use of a monthly annuity by spreading costs
13 over time. As indicated previously, all but three employees eligible to begin SERP
14 payments during the period 2002 through 2012 elected a lump-sum payout. The three-
15 year normalization period averages the lump sum payments over a 3 year period and
16 recognizes that there will routinely be employees becoming eligible for SERP payments
17 over a three year period. By averaging the payments, the lump sum payments take the
18 form of a monthly annuity payment during this time period. The monthly annuity
19 payments have been recognized by Staff in previous rate case requests.

20 **Q: How were SERP costs included in the last cases?**

21 A: Staff and the Company have never come to an agreement about how to properly include
22 lump-sum payments in cost of service. Instead, they have been included as part of the
23 settlements of miscellaneous issues.

1 **Q: What is the value of this issue?**

2 A: At the time of Staff's direct filing, Staff reduced the Company's revenue requirement by
3 approximately \$230,000 based on activity through March 2012. Because additional
4 lump-sum payments are scheduled to be made prior to the August 31, 2012 true-up date,
5 the issue value will increase to about \$300,000.

6 **Q: Is there any other issue regarding SERP that you would like to address?**

7 A: Yes. In this case for the first time, Mr. Hyneman also removed from the pension
8 calculation all SERP costs related to the Wolf Creek Nuclear Operating Corporation
9 ("WCNOC"), in which KCP&L is a 47% owner. Although Mr. Hyneman removed the
10 actuarially computed costs from annualized pension costs, he did not include them in
11 Staff's calculation of annualized SERP costs. WCNOC has seven individual SERP
12 agreements, of which all participants are retired and being paid monthly. KCP&L's
13 annual share of the monthly payments is \$242,800 for 2011 and 2012. Staff has been
14 informed of this omission and has indicated that it is willing to include \$92,500.

15 **Q: Why has Mr. Hyneman reduced its allowed amount from the \$242,800 annual
16 payment amount?**

17 A: Mr. Hyneman made two adjustments. First, he set a maximum annual payment amount
18 of \$50,000 per individual and eliminated all amounts greater than the maximum. Next,
19 he eliminated 100% of the SERP payments for employees who had not been employed by
20 WCNOC for at least five years.

21 **Q: Do you believe this is appropriate?**

22 A: No. Mr. Hyneman has applied a \$50,000 annual maximum to four individuals, each of
23 whom held the position of Chief Executive Officer for some period during the life of

1 Wolf Creek, beginning in 1986. The SERP contracts were established as a necessary
2 component of overall compensation to attract and retain the in-depth nuclear industry
3 experience necessary for this position. Because all but one of these CEO's were hired
4 directly into the position of CEO or Vice President after obtaining extensive industry
5 experience elsewhere, it is not unexpected that they would have both 1) high annual
6 salaries and SERP payments and 2) a shorter tenure at WCNOG before retirement than
7 would an individual who started at a lower level in the organization.

8 Other Post-Employment Benefit Costs

9 **Q: What is the purpose of this portion of your testimony?**

10 A: The purpose of this portion of my testimony is to rebut Mr. Hyneman's positions in a
11 number of areas related to OPEB costs, as follows: 1) that the Company is not in
12 compliance with the funding requirements of Section 386.315 RSMo, due to the
13 WCNOG plan 2) that it is likely that KCP&L has been significantly over-collecting its
14 WCNOG OPEB costs for several years and 3) that the proper amount of WCNOG OPEB
15 costs to include in cost of service should be only the amount that KCP&L remits to
16 WCNOG on a pay-as-you-go basis.

17 **Q: Briefly describe Mr. Hyneman's position.**

18 A: Mr. Hyneman believes that the funding criteria of Section 386.315 RSMo must be
19 applied individually to each of KCP&L's three OPEB plans-the management plan, the
20 bargaining plan and the WCNOG plan. Since WCNOG's policy is to fund payments in
21 excess of participant contributions, Mr. Hyneman believes that KCP&L may have been
22 over-collecting in rates regardless of the amount of KCP&L's contributions to the plans
23 in total.

1 **Q: Please explain the Company’s position.**

2 A: From a regulatory perspective, the Company believes that it has appropriately recorded
3 OPEB costs based on FAS 106 as it has been allowed rate recovery and is required to
4 make contributions for OPEB costs based on jurisdictional funding requirements for the
5 plans in total. KCP&L manages a Voluntary Employees’ Beneficiary Association
6 (“VEBA”) trust for its management employees and jointly manages with union trustees a
7 VEBA trust for its bargaining unit employees. KCP&L does not manage the trust used
8 by WCNOG for its employees and is not able to make contributions directly into it. If
9 KCP&L were to make additional OPEB payments to WCNOG over their requested
10 amount, any excess would apply to all WCNOG partners and KCP&L would only receive
11 their ownership share of future benefits from the extra payments.

12 **Q: Why is Mr. Hyneman’s position inappropriate?**

13 A: There is nothing in Section 386.315 RSMo that requires funding by individual plan, only
14 that the amounts collected in rates be funded to an independent external funding
15 mechanism in order to use amounts calculated pursuant to GAAP as codified by FASB in
16 Accounting Standards Codification 715, formerly referred to as Statement of Financial
17 Accounting Standards No. 106 (“FAS 106”) for ratemaking. From a cost of service
18 perspective it is generally irrelevant which plan is funded since the plan contributions
19 increase plan assets which earn a return and lower the Company’s future FAS 106 costs
20 which directly benefits the Company’s customers. We believe the statute allows for
21 funding criteria to be applied to the Company plans in total which are based on a FAS
22 106 calculation for the entire Company including WCNOG.

1 **Q: What are the funding requirements for OPEB's?**

2 A: There are two sources of funding requirements; 1) statutory funding requirements as
3 required by Section 386.315 RSMo effective in 1994 and 2) regulatory funding
4 requirements established in the Non-unanimous Stipulation and Agreement Regarding
5 Pensions and Other Post-Employment Benefits ("OPEB S&A") approved by the
6 Commission in Case No. ER-2010-0355 for rates effective May 4, 2011. KCP&L must
7 also comply with the funding requirements approved by the Kansas Corporation
8 Commission in early 2011 for OPEB costs effective December 1, 2010.

9 **Q: How do these apply to the Company?**

10 A: Section 386.315 RSMo applies to all utilities in the state of Missouri who wish to include
11 OPEB costs based on FAS 106 in cost of service for ratemaking. Each utility is required
12 to fund amounts included in rates based on FAS 106 into a separate funding mechanism
13 to be used solely for payment of OPEB benefit costs. For purposes of this statute,
14 amounts included in rates would equal the Missouri jurisdictional portion of OPEB costs
15 included in cost of service. They do not include either the non-jurisdictional portion of
16 FAS 106 costs or the Missouri jurisdictional portion of amounts not included in rates, i.e.
17 amounts pertaining to other regulatory jurisdictions, amounts pertaining to joint partners
18 shares or amounts capitalized rather than expensed. The Missouri jurisdictional
19 allocation factor in the last several cases has been approximately 54%, and the expense
20 factor has been slightly less than 80%.

21 **Q: Please explain the requirements of the OPEB S&A approved by the Missouri Public
22 Service Commission in Case No. ER-2010-0355 for rates effective May 4, 2011.**

23 A: Paragraph 15 of the OPEB S&A included the following two provisions:

1 a. OPEB cost, as described for pensions in paragraph 7, will be calculated based on
2 FAS 106 requirements.

3 b. Funding requirements, as described for pensions in paragraph 12, are replaced
4 with a single requirement that current period OPEB cost will be funded.

5 **Q: Were funding requirements also established for the Company's Kansas**
6 **jurisdiction?**

7 A: Yes. As a result of the OPEB tracker established in conjunction with Docket No. 10-
8 KCPE-415-RTS, the Company was required to fund the Kansas jurisdictional portion of
9 OPEB costs included in rates beginning December 1, 2010. The costs included in rates
10 were the expense portion of OPEB costs based on the FAS 106 actuarial calculation.
11 There was no previous funding requirement.

12 **Q: Can you demonstrate that these requirements were met?**

13 A: Yes, the table below shows GPE's total 2010 and 2011 Section 386.315 RSMo and
14 regulatory funding requirements and GPE's contributions to the VEBA trusts for each
15 year. As shown the contributions exceed the statutory and regulatory funding
16 requirements for each year.

	<u>Total GPE Funding Requirement for FAS 106-OPEB⁽¹⁾</u>		<u>Contributions to the⁽²⁾</u> <u>Management & Bargaining</u> <u>VEBA</u>
	<u>Section 386.315 RSMo</u>	<u>Regulatory Funding Requirements</u>	
2011	\$7.3	\$10.2	\$15.9
2010	\$5.1	N/A ⁽³⁾	\$17.4

(1) Amounts are in millions.

(2) Contributions do not include FAS 158 regulatory funding.

(3) Mo. regulatory funding requirements were effective May 4, 2011 for KCP&L and June 25, 2011 for GMO.

1 **Q: Is it the Company's position that both statutory and regulatory funding**
2 **requirements from the OPEB S&A have been satisfied?**

3 A: Yes, as reflected in the table above, the Company has met the funding requirements under
4 Section 386.315 RSMo and the regulatory funding requirements.

5 **Q: Has KCP&L been significantly over-collecting its WCNOB OPEB costs for several**
6 **years?**

7 A: No, as shown in the table above, on a total company basis the Company exceeded the
8 regulatory and statutory funding requirements for the last two years. With the
9 Company's policy to annually fund 100% of the management and bargaining FAS 106
10 amounts, the Company has exceeded statutory requirements since the implementation of
11 Section 386.315 RSMo and the Company has not been over-collecting its OPEB costs.

12 **Q: What is the appropriate amount of OPEB costs to include for ratemaking in this**
13 **case?**

14 A: The appropriate amount of OPEB costs to be included in cost of service is the Missouri
15 jurisdictional expense portion of the FAS 106 OPEB costs determined by the actuarial
16 valuation which includes the FAS 106 OPEB costs associated with WCNOB

17 **Q: Is this consistent with how OPEB costs have been included in cost of service in the**
18 **four rate cases initiated under the Company's Regulatory Plan (Case No. EO-2005-**
19 **0329) that was approved in 2005?**

20 A: Yes, it is.

21 **Q: Was Staff aware of how funding of WCNOB OPEB costs was occurring?**

22 A: Yes, Staff was aware. As expressed to Staff in responses to various data requests over
23 the past years, most completely in Data Request No. 2-93 in Case No. ER-2006-0314,

1 KCP&L has reimbursed WCNOG for amounts paid for current OPEB costs. WCNOG
2 established a VEBA at beginning of 2011, but the Company cannot make contributions
3 directly into the WCNOG trust, as stated earlier, as these payments would go to pay
4 benefits for which the Company is only 47% responsible.

5 **Q: Does that conclude your testimony?**

6 **A:** Yes, it does.

