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Witness:	*Cary G. Featherstone*
Sponsoring Party:	*MoPSC Staff*
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MISSOURI PUBLIC SERVICE COMMISSION

UTILITY SERVICES DIVISION

SURREBUTTAL TESTIMONY

OF

CARY G. FEATHERSTONE

Great Plains Energy Corporation
GREATER MISSOURI OPERATIONS COMPANY
MPS AND L&P ELECTRIC OPERATIONS

CASE NO. ER-2009-0090

Jefferson City, Missouri
April 2009

****Denotes Highly Confidential Information****

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GREATER MISSOURI OPERATIONS COMPANY
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Q. Please state your name and business address.

A. Cary G. Featherstone, Fletcher Daniels State Office Building, 615 East 13th Street, Kansas City, Missouri.

Q. By whom are you employed and in what capacity?

A. I am a Regulatory Auditor with the Missouri Public Service Commission (Commission).

Q. Are you the same Cary G. Featherstone who filed direct testimony in this proceeding?

A. Yes, I am. I, with Curt Wells, filed direct testimony in this case on February 13, 2009 sponsoring Staff's cost of service report (Staff Report) for KCP&L Greater Missouri Operations Company's (GMO or Company) rate case filed on September 5, 2008. I filed direct testimony in GMO's pending steam rate case, Case No. HR-2009-0092, on February 13, 2009. I also filed direct on February 11, 2009, rebuttal on March 11, 2009 and surrebuttal on April 7, 2009 in Kansas City Power & Light Company's (KCPL's) concurrently pending rate case, Case No. ER-2009-0089.

Q. What is the purpose of your surrebuttal testimony?

A. I respond to the rebuttal testimonies of several GMO witnesses regarding the incomplete construction audits of several plant additions that have been, made or will be, added to the plant in service balances of GMO and KCPL. These plant additions for GMO and KCPL relate to the current construction projects at Iatan 1 for environmental equipment and upgrades to the steam turbine (L&P), the completed construction projects of environmental equipment at Jeffrey Energy Center, Units 1 and 3 (MPS), of which GMO has an 8% ownership share and the environmental upgrades for the Sibley generating facility, Unit 3, (MPS) of which GMO has a 100% ownership share.

An additional purpose of this surrebuttal testimony is to address the rebuttal testimony filed on behalf of GMO by GMO witness Burton L. Crawford, Manager, Energy Resource Management, relating to the area of capacity planning and peaking turbines. Mr. Crawford supports inclusion of a new generating facility of GMO in the form of four combustion turbines totaling 300 megawatts of capacity originally installed in 2002 in Clarksdale, Mississippi, designated as Crossroads Energy Center (Crossroads). These generating units were built as a non-regulated facility by Aquila Merchant Services Inc. (Aquila Merchant), an affiliate of GMO when GMO was named Aquila, Inc.

Q. How will you refer to GMO in this surrebuttal testimony?

A. Because GMO has two areas in its service territory that have different electric rates based on differing rate bases and costs of service, when referring to the operations and area that was most recently referred to as being served by Aquila as Aquila Networks-MPS (the old Missouri Public Service Company (MoPub) service area) I will simply use the designation of GMO MPS or MPS. When referring to the operations and area that was most

recently referred to as being served by Aquila as Aquila Networks-L&P (the former St. Joseph Light & Power Company service area) I will simply use the designation of GMO L&P or L&P. GMO merged with St. Joseph Light & Power Company in 2000 when it was named UtiliCorp United, Inc.. At various places in this surrebuttal testimony when I discuss historical aspects of GMO capacity planning I will use the name GMO was using at the time-Aquila (Aquila, Inc.) during the period early 2002 to mid 2008 and UtiliCorp (UtiliCorp United, Inc.) before early 2002. I refer to the former operating divisions of Aquila-Aquila Networks-MPS and Aquila Networks-L&P, as MPS and L&P, respectively, when discussing GMO when it was named Aquila, i.e., before it was acquired by Great Plains Energy Corporation (GPE) on July 14, 2008.

EXECUTIVE SUMMARY

Q. Would you please summarize your surrebuttal testimony on the issue of construction costs?

A. Staff's review of the Iatan 1, Sibley and Jeffrey Energy Center construction costs are not complete and as such, Staff has proposed to either, (1) to the extent the costs of that project exceed KCPL's and GMO's definitive estimates, make that portion of GMO's rates interim subject to refund, or (2) expressly state in its Report and Order in this case that the Commission is not deciding for the purpose of setting rates in this case the issue whether the construction costs of the Iatan 1, Sibley and Jeffrey Energy Center projects were prudently incurred, and that it will take up the matter of the prudency of those costs in a future cases, if a party properly raises the issue before the Commission in those cases.

GMO has misinterpreted Staff's recommendation concerning the completion of construction cost review, commonly referred to as a construction audit. GMO infers that it

believes Staff's position is to exclude prudently incurred Iatan 1, Sibley and Jeffrey Energy Center costs from the current case. That is not correct. Under the first option, GMO would be permitted by the Commission to collect in permanent rates the construction costs of Iatan 1, Sibley and Jeffrey Energy Center environmental enhancements up to the total of the definitive estimates for the costs of these improvements and the remainder of the construction costs interim subject to refund. Under the second option, GMO would be permitted by the Commission to collect in permanent rates all of the construction costs of Iatan 1, Sibley and Jeffrey Energy Center environmental enhancements, but the Commission would specifically state in its Report and Order that the Commission has not decided the issue of whether the construction costs of Iatan 1, Sibley and Jeffrey Energy Center were prudently incurred and, if raised b a party in the next GMO and KCPL rate cases, would take up that issue at that time.

Q. Would you please summarize your surrebuttal testimony on the area of the capacity planning of Aquila and the related costs of combustion turbines?

A. The following summarizes my testimony on this topic.

GMO presents in its rebuttal testimony what it believes is justification for its inclusion of Crossroads in its rate base for MPS in this filing. GMO believes that Crossroads is the lowest cost generation planning and, therefore, represents the best option that the Company had in the 2007 and 2008 time period to meet its system load requirements. Staff does not agree with this assessment. Staff has examined the capacity issue at GMO (Aquila) since 1999 and has concluded that the replacement of a major purchased power agreement that terminated in May 2005 has never been completely addressed by GMO (Aquila) until 2008, when the Company moved Crossroads from an unregulated affiliate into its regulated plant

investment. Staff opposes the inclusion of the cost of Crossroads in rate base for MPS as it was not a least cost planning decision and the plant is located in the state of Mississippi several hundred miles from GMO's service territory.

The least cost planning decision for ratemaking in this case should be focused on the events surrounding the time period of 2004 and 2005 when GMO (Aquila) was deciding how to replace the full 500 megawatt capacity needs it had that it was meeting with a purchased power agreement that expired before the summer of 2005. GMO is misdirecting the Commission to the wrong time horizon.

In lieu of GMO's 315 megawatt South Harper facility and GMO's Crossroads facility, Staff proposed to include what it has described as the MPS facility. The MPS facility is a 525 megawatt facility based on the costs Aquila prudently incurred in building its South Harper facility plus the costs of two additional 105 megawatt combustion turbines. Since the legal issues surrounding the South Harper facility are now resolved with the March 28, 2009 effective date of the Commission's Report and Order in Case No. EA-2009-0118, the MPS facility is now the South Harper facility plus two additional 105 megawatt combustion turbines. This position is addressed at pages 85 to 93 in the Staff Cost of Service Report, and rebuttal and surrebuttal testimonies of Staff witnesses Lena M. Mantle and Charles R. Hyneman. This testimony supports that GMO (Aquila) should have built its own generation to meet its growing electric needs and should have been doing so since at least the late 1990s. The South Harper facility is the first Commission-regulated generating capacity that GMO (Aquila) has built since 1983. Between 1983 and 2005 GMO relied on purchased power agreements to meet the growing demand for electricity in its MPS service territory. Staff was put into the position of imputing

the MPS facility to GMO because GMO (Aquila) did not build generating assets for MPS, or L&P, for a substantial period of years.

Unlike the costs of a six combustion turbine site with three installed 105 megawatt combustion turbines, which were based on Aquila's costs for South Harper facility as built in 2005, Staff did not have such a basis for the costs to acquire and build the two additional combustion turbines to value the two additional turbines referred to as Turbines 4 and 5 in this case (as well as the last two MPS rate cases - Case ER-2005-0436 and Case No. ER-2007-0004). This is because Aquila did not adequately plan and pursue building generating assets to meet its system load requirements. GMO (Aquila) did, with Calpine, build the Aries Combined Cycle Generating Station (Aries), a 585- megawatt power plant. That station went into service in early 2002. At that time, GMO, then known as UtiliCorp United, Inc., had a corporate policy not to build generating assets for its regulated utility operations. The Aries station was conceived, planned, designed, engineered and costs determined by GMO, but GMO turned the project over to its unregulated subsidiary Aquila Merchant Inc. (Aquila Merchant) to build. GMO (Aquila) signed a five-year purchased power agreement with Aquila Merchant for MPS' operations that ended May 31, 2005, (the Aries Agreement). Before it began imputing generating assets, Staff took the position in GMO's prior rate cases that the Aries Agreement was not an arms' length transaction, and made adjustments in each of those cases to exclude the full value of the capacity agreements between MPS and its affiliate, Aquila Merchant.

Planning for the expiration of the May 31, 2005, Aries Agreement, MPS developed a least cost plan in early 2004 to meet MPS' capacity needs for the summer of 2005. This capacity plan was that the least cost plan was to build five (5) turbines having a total

capacity of 525 megawatts. However, in the summer of 2005 Aquila MPS installed only three combustion turbines totaling 315 megawatts at its South Harper site designed for six such combustion turbines, following what it referred to as its "preferred plan." The remaining capacity to replace Aries was to be met by power from purchased power agreements. South Harper was the subject of extensive litigation. Originally, the three turbines GMO (Aquila) installed at South Harper were held in storage from 2002 to 2005 after GMO (Aquila) no longer planned for them to be used by GMO's non-regulated subsidiary, Aquila Merchant, who had planned to install them at its then owned Aries generating site, as Aries II. GMO (Aquila) unsuccessfully attempted to sell these turbines before storing them long term. Rather than building additional capacity, GMO (Aquila) subjected itself to the volatile market conditions of the energy power markets. After the installation of the combustion turbines at South Harper in 2005, GMO (Aquila) continued to rely on short-term purchased power agreements for the remaining capacity necessary for it to meet its system load requirements year-after-year. GMO (Aquila) did so until the decision by GMO (Aquila) to transfer Crossroads from its non-regulated affiliate Aquila Merchant to MPS in August 2008.

Up until January 2004, GMO (Aquila's) resource planning analyses only considered capacity agreements. Since January 2004, GMO (Aquila) performed resource planning analyses year-after-year, identifying a need to build generating units to make up for the Aries capacity. Other than South Harper, GMO (Aquila) never built any of these units. Even though GMO (Aquila) expressed to Staff in the past several years an intent to build generating facilities, it failed to do so. GMO (Aquila) made no plans to build future generating plant, other than its participation in the Iatan 2 coal-fired project.

The value of Crossroads is substantially overstated because the four combustion turbines installed at that facility were purchased at a time when turbine manufactures were selling those units in sellers' market with very high prices. GMO (Aquila) had many opportunities to acquire turbine capacity for installation in and around its load center at greatly reduced prices relative to the prices paid for the turbines installed at the Crossroads facility. If the Commission allows Crossroads in rate base, it should do so at a substantially reduced amount compared to what GMO is requesting in this case.

The four Crossroads turbine are book valued at approximately ** ___ ** million each, or a total of ** ____ ** million. Based on GMO's imprudency in not acquiring that owned capacity in 2004-2005, Staff believes those values should be significantly reduced in the range of ** _____ ** million each or total range of ** _____ ** million based on sales and offers to other utilities for the same turbine model.

In addition to the turbine values being over stated, the costs of the transmission plant at Crossroads is higher than it would be if GMO (Aquila) would have installed the turbines at an existing site such as South Harper. Staff believes that the there was a ** ___ ** million amount that was estimated for transmission upgrades at the Aries site where those three South Harper turbines were originally planned to be installed. Crossroads transmission is substantially higher than this transmission upgrade estimate.

Staff believes that the annual transmission expenses will be higher for the Crossroads units because of where they are located. If the turbines would have been installed in the Kansas City area the transmission costs would be dramatically less.

Staff believes that the natural gas costs will be higher at Crossroads than it would be if the capacity was located in the Kansas City area.

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COST REVIEW OF CONSTRUCTION PROJECTS

Q. Did GMO address any concerns regarding Staff's review of the Iatan construction project?

A. Yes. Several Company witnesses responded to Staff's recommendation made at page 33 of my direct testimony relating to the review of the construction costs of Iatan 1 for environmental equipment currently being installed and tested - the Air Quality Control System (AQCS) equipment.

While several Company witnesses identify similar concerns regarding Staff's position on review of the construction costs for several construction projects completed or soon to be completed, GMO witness Chris Giles states the general position regarding Staff's proposal for the review of construction costs for the Iatan 1 environmental equipment. Mr. Giles states the following at page 10 (starting at line 20) of his rebuttal testimony:

> By suggesting that it might be appropriate for the Commission only to reflect in the Company's rates the definitive estimate for the AQCS projects, Mr. Featherstone implies that costs incurred over and above those estimates were not prudently incurred. However, he does not provide any evidence, much less create serious doubt about the Company's prudence.

Q. Has GMO accurately portrayed Staff's recommendation?

A. No. Staff is not recommending the Commission exclude all Iatan 1, Sibley Unit 3 and Jeffrey Energy Center Units 1 and 3 costs from cost of service, unless the equipment and generating units are not fully operational and used for service by the true-up cut-off date established in this case. It is my understanding, that the only generating unit that is in question regarding the in-service criteria is the Iatan 1 AQCS, which is the most significant of these construction projects. The Iatan 1 construction affects GMO L&P's rates as well as KCPL's rates.

Q. What is Staff's recommendation regarding the construction costs for the environmental plant additions for Iatan 1, Sibley Unit 3 and Jeffrey Energy Center Units 1 and 3?

A. Staff recommended the following in its direct case at page 33 of my direct testimony:

> Staff recommends the Commission either, (1) to the extent the costs of that project exceed KCPL's and GMO's definitive estimate, make that portion of GMO's rates interim subject to refund or (2) expressly state in its Report and Order in this case that it is not deciding for the purpose of setting rates in this case the issue whether the construction costs of the Iatan 1, Sibley and Jeffrey Energy Center projects were prudently incurred and that it will take up the matter of the prudency of those costs in a future cases, if a party properly raises the issue before the Commission in those cases.

Q. Is Staff proposing to exclude construction costs relating to the Iatan 1, Sibley or Jeffrey Energy Center environmental plant additions in this case?

A. No. Staff is proposing, in particular with option 2, that the Commission simply state in its Order issued in this rate case that "…it is not deciding for the purpose of setting rates in this case the issue whether the construction costs of the Iatan 1, Sibley Unit 3 and Jeffrey Energy Center Units 1 and 3 projects were prudently incurred and that it [the Commission] will take up the matter of the prudency of those costs in a future cases, if a party properly raises the issue before the Commission in those cases." This means that the rates in this case would not exclude recovery for the Iatan 1 environmental plant additions for GMO L&P and Sibley Unit 3 and Jeffrey Energy Center Units 1 and 3 for GMO MPS. It would mean however, that the parties would have an opportunity to review the final completed and actual costs relating to the Iatan 1, Sibley Unit 1 and Jeffrey Energy Center Units 1 and 3 projects of GMO MPS and L&P.

At no time did Staff expressly state, imply or infer that rates in this case would not include completed Iatan 1 costs for GMO MPS and Sibley Unit 3 and Jeffrey Energy Center Units 1 and 3 for GMO L&P, assuming that these units are fully operational and used for service.

Q. Has GMO discussed with the Staff the proposal outlined in your direct testimony for the treatment for plant additions?

A. No. At no time has GMO, Great Plains Energy, or KCPL, made any attempt to discuss with Staff, Staff's proposal to address the prudency of the Iatan 1 environmental costs even to assure itself that it understood Staff's proposal. The Company did not engage in any discovery to assure itself that it understood Staff's position on this matter. The Company misunderstood Staff's position and then devoted significant time and resources to dispute its misunderstanding.

Q. When does KCPL anticipate the construction of the Iatan 1 environmental equipment to be completed?

A. KCPL is working on finalizing and testing the newly installed environmental equipment and presently anticipates the testing for the in-service criteria agreed to by the Company and Staff to be completed sometime in April 2009.

Q. What is KCPL's estimate of the final construction costs for Iatan 1?

A. In KCPL witness Brent C. Davis direct testimony, KCPL identifies the Iatan 1 environmental cost estimates as follows:

$ in millions	Control Budget Estimate	Estimate at Completion	Increase (Decrease)
Base Estimate	** _____ **	** _____ **	** _____ **
Project Contingency	** ___ **	** ___ **	** ___ **
Reserve Contingency	** ___ **	** __ **	** __ **
Total	** _____ **	** _____ **	** _____ **

[Source: Highly Confidential Schedule BCD-1 Davis' KCPL direct testimony filed in Case NO. ER-2009-0089]

Q. What are Iatan common costs?

A. Common costs are those plant systems, equipment and facilities that provide operational function to both units at Iatan, the original Unit 1 and the new Iatan 2. An example of Iatan common costs is the emissions stack or chimney. This single chimney facility has separate liners within it for the two generating units at Iatan. Buildings used for equipment storage and shops may be common to both units. Water treatment facilities and equipment are examples of common plant costs.

Q. What is the value of the Iatan common costs?

A. Not only have the common costs significantly changed a number of times but the methodology for determining the common costs has changed.

The Iatan common costs as quantified by the Company can be summarized below:

Iatan Unit 1 AQCS Project Costs

	KCPL Share	GMO L&P Share
January 21, 2009	** _____ **	** _____ **
February 6, 2009	** _____ **	** _____ **
March 26, 2009	** _____ **	** _____ **

[Source: E-mail transmittals from KCPL to Staff]

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Q. Did GMO and KCPL recently provide support for Iatan common costs?

A. Yes. Staff just received support for the most recent March 26th version of the common costs on March 30, 2009. Staff will further examine common costs for the Iatan facility.

Q. Are there issues with the Iatan common costs?

A. At this point it is not possible to know if there are going to be differences on approaches of including common costs in rate base in this case. One element of concern involves the chimney that is going to be used for both Iatan 1 and Iatan 2. In KCPL witness Steven Jones rebuttal testimony filed in Case No. ER-2009-0089 at page 20, line 22, he states "even though the Iatan Unit 2 chimney liner will not be utilized until 2010, the entire chimney stack must be put into service in order to facilitate start-up and operations of Iatan 1 Unit AQCS." In KCPL witness Brent Davis' direct testimony, page 13, line 21 filed in Case No. ER-2009-0089 he states "…it is appropriate to include a portion of the cost of the new chimney in rates associated with the Iatan 1 projects and to allocate a portion to be in rates associated with Iatan 2." This apparent difference in position with the Company will have to be resolved in order to determine the proper level of common costs that should be included in plant-in-service for the true-up portion of this case if Iatan 1 AQCS is fully operational and used for service by the close of the true-up period.

Q. Will the common costs for Iatan 1 be included as part of the true-up audit?

A. Yes. Staff will have discussions and perform discovery on the common costs for the Iatan 1 and 2 construction projects. Not only will the actual costs be considered during the true-up review but also the allocation and assignment of these costs between the two Iatan units. Costs associated with Iatan 1 will be included in the plant-in-service. I am under

the impression that GMO and KCPL will be seeking an Accounting Authority Order (AAO) for a portion of the common costs, i.e., those common costs associated with Iatan 2. Staff will review any AAO proposal when and if GMO and KCPL provide such a proposal.

Q. Has GMO proposed to reduce its common costs by any reimbursements from the Iatan 2 partners?

A. No. This is another item Staff must address to determine the amount of these costs that should be recovered from GMO's customers.

Q. When does GMO anticipate the construction of the Sibley Unit 3 and Jeffrey Energy Center Units 1 and 3 environmental equipment to be completed?

A. Sibley Unit 3 met its in-service criteria in the first quarter of 2009. The Jeffrey Energy Center Units 1 and 3 environmental equipment were in service in 2008, and the Jeffrey Energy Center Unit 2 is expected to be completed in second quarter 2009.

A. KCPL is working on finalizing and testing the newly installed environmental equipment and presently anticipates

Q. Has Staff proposed similar treatment in this case that it has proposed in past cases?

A. Yes. In KCPL's 2006 rate case, Staff did not complete the construction audit regarding the Hawthorn 5 re-build which resulted from a boiler explosion that occurred in February 1999. The unit was out of service until June 2001. Staff reviewed construction costs for several combustion turbines installed at various times from May 1997 through 2003. Staff did not complete its review of the Hawthorn 5 generating facility in the 2006 rate case. Staff identified the units that it had completed its review and stated that it was unable to finish

the work to make a recommendation regarding the prudence of the Hawthorn 5 re-build. I addressed this at page 25 of my direct testimony filed in Case No. ER-2006-0314.

> Q. Was Staff able to go through the same review process for Hawthorn 5 construction costs as it did for the combustion turbine generators?
>
> A. No. Unfortunately, with time constraints of the filing deadline, Staff was not able to follow the same approach for Hawthorn 5 that was used for the combustion turbine generators. As an example, after the initial discussion with personnel regarding each of the combustion turbine generators construction, Staff submitted follow-up questions, and reviewed additional documentation. Follow-up discussion with KCPL construction personnel took place with further review of documentation and questions. With respect to the West Gardner and Osawatomie generating units, Staff talked to the KCPL project engineer three separate times. Staff has not had the chance to complete the review process of the Hawthorn 5 construction costs using the same information gathering approach it has used for the combustion turbine generators.
>
> Q. Is the Hawthorn 5 construction project larger than the combustion turbine projects?
>
> A. Yes, substantially. . . .
>
> * * * *
>
> . . . Staff has only started the review of these files within the last couple weeks of the audit. It is unlikely, with the press of the remaining schedule for the KCPL case, including the construction audit of the wind turbines during the true-up portion of the case, that Staff will be able to complete the document review. Staff will not be able to complete the follow-up interview process with Hawthorn 5 personnel. In fact, Staff has questions that are outstanding regarding interviewing KCPL construction management that Staff wants to complete. For these reasons, Staff will continue the Hawthorn 5 construction cost review in the next rate case filed by KCPL, which is currently scheduled to be filed February 1, 2007, according to the KCPL Experimental Regulatory Plan.

Q. Did KCPL express any concerns regarding the delay of Staff's review of construction costs regarding the re-build of Hawthorn 5?

A. No. KCPL did not express any concerns at all either in discussions it had with Staff or did it provide responsive testimony on this subject. Staff's alternative proposal to defer the issue of the prudence of the Iatan 1 environmental costs until a future case without the rates being interim subject to refund is the same as the position taken in KCPL's 2006 rate case referenced above regarding the review of the re-build of Hawthorn 5.

CROSSROADS ENERGY CENTER GENERATING UNIT

Q. GMO witness Mr. Crawford states, at page 9 of his rebuttal testimony, that GMO "concluded that the Crossroads Energy Center would result in the lowest 20-year NPVRR, including the cost of transmission service." Does Staff agree that this is the lowest cost generation that GMO should have considered?

A. No. GMO proposes to include a new generating unit in its rate base. The history and decision regarding including Crossroads in rate base is discussed in the direct and rebuttal testimonies of Staff witnesses Mantle and Hyneman. My surrebuttal testimony focuses on the history and decision of GMO (Aquila) during the period 1999 to 2005 when the Company needed generating capacity as result of its load growth.

Q. Why does Staff not agree that Crossroads does not represent GMO's least cost option?

A. Staff believes that the time period of 2007 that GMO is relying on to evaluate the costs of this generating capacity is misplaced and well past the time when this capacity was needed by the Company. The time that is relevant to the evaluation of least cost capacity planning for GMO is the time period of 2004 when the Company had to make decisions

regarding its replacement of the 500 megawatt Aries purchased power agreement that expired May 31, 2005. This agreement was originally with an affiliate of Aquila who owned and built Aries with its partner, Calpine. GMO (Aquila) signed a five-year purchased power agreement with Aquila Merchant for MPS.

Upon termination of the 500 megawatt Aries purchased power agreement, GMO (Aquila) committed to replacing part of its capacity shortfall with three combustion turbines that an Aquila affiliate had in storage - the combustion turbines it installed at South Harper. In January 2004, Aquila informed Staff that it was going to use these combustion turbines to partially replace the 500 megawatts of capacity it had been obtaining from the Aries station in order to meet its capacity needs during the summer of 2005 peak season. At the time, Staff questioned GMO (Aquila) why it was only installing three combustion turbines, when the Company's own analysis showed the least costs planning to replace the 500 megawatt Aries PPA was to install five combustion turbines. In 2004, GMO explained that it only had three combustion turbines to install and it also thought there were attractive short-term purchased power agreements available for the summer of 2006 which was the summer after the South Harper units were to become operational.

Q. Did Staff accept this explanation by GMO (Aquila)?

A. No. Staff continued to express its concerns it had previously communicated to GMO (Aquila) many times that Staff believed the best approach for the Company was to pursue the installation of three combustion turbines that were eventually installed at South Harper and to build additional generating capacity making up the shortfall. Staff expected GMO (Aquila) to build five combustion turbines making up approximately

525 megawatts of capacity which would have more than adequate to replace Aries 500 megawatts of capacity.

Q. Did GMO (Aquila) ever have an opportunity to purchase Aries after its unregulated affiliate sold its interest to Calpine?

A. Yes. In late 2006, GMO (Aquila) informed Staff that it had planned to bid on Aries unit that was put up for sale by its former partner, Calpine. Aquila bid for this generating facility on December 4, 2006, but was not the successful bidder.

Q. Would you briefly describe the Aries and Iatan 2?

A. Yes. Aries is a 585 megawatt combined cycle facility and would have more than met MPS' system load requirements for 2007 and beyond, possibly through 2010 when Aquila's share of Iatan 2 Generating facility is expected to go into service. Iatan 2 is a coal-fired generating plant which is currently being built by Kansas City Power & Light Company (KCPL) and, in which Aquila has an 18 percent ownership share.

Q. Did Calpine's sale of Aries in 2006 influence GMO (Aquila's) decision to build new capacity?

A. Yes. Because GMO (Aquila) did not need peaking capacity in addition to the 585-megawatt Aries combined cycle facility, it would not commit to building combustion turbines before Calpine sold Aries.

Staff believes that GMO (Aquila's) decision to build Aries as merchant plant caused the problems with its capacity planning. Aries was previously owned by GMO (Aquila) as a non-regulated unit. GMO (Aquila) sold a 50% share of Aries in late 1999 to Calpine. If GMO (Aquila) had built this plant as a regulated facility, there would not be the capacity issues that have plagued GMO (Aquila) over the past several years. With ownership and

control of the Aries capacity, GMO (Aquila) would not be subjected to the capacity market year after year.

Q. Since GMO (Aquila) did not acquire the Aries Unit how did it meet its capacity needs during the summers of 2007 and 2008 to meet system loads?

A. With short-term purchased power agreements for capacity from Crossroads.

Q. Why is the time frame of the Aries contract which ended in 2005 relevant to the discussion of Crossroads?

A. Since GMO has taken the position through Mr. Crawford's rebuttal testimony that Crossroads is the most economical capacity generation available to the Company, it is essential to any assessment of the Crossroads facility to understand that it is GMO's actions that positioned so that it appears on the surface this rate base decision looks good in 2007. Staff believes, however, that the relevant time period is when the Aries contract ended in 2005, not two years later in 2007. The costs of combustion turbine acquisition and installation in 2005 are substantially different than in the 2007 and 2008 time period. For capacity replacement to have occurred by May 2005, GMO (Aquila) would have had to have purchased the turbine equipment by 2004. The combustion turbine market in 2004 was completely different than the market during 2007 and 2008 when GMO made its analysis and concluded that Crossroads was the least cost decision.

Q. How did GMO base its decision that Crossroads was its least cost capacity decision in 2007 and 2008?

A. GMO witness Mr. Crawford generally describes the process GMO (Aquila) went through to determine that Crossroads was the best decision for the Company at page 9 of his rebuttal testimony. GMO (Aquila) received responses from a request for proposal (RFP)

for purchased power agreements and self-build options. The self-build options contained prices for turbines and equipment priced at 2007 costs. These costs would have significantly increased compared to when GMO (Aquila) should have evaluated the capacity addition in 2004. To suggest that Crossroads is an economic decision as GMO indicates in Mr. Crawford's rebuttal testimony is simply wrong.

Q. GMO witness Crawford states at page 12 of his rebuttal testimony that GMO considered self-build options but "Crossroads was determined to be a lower cost option than self-building." Does Staff agree that Crossroads is a low cost option for GMO to meet its generating needs?

A. No. The comparison that GMO (Aquila) made prior to the acquisition was based on the wrong time period. Aquila examined the costs in 2007 but that was three years after the analysis should have been done. By 2007, the combustion turbine had increased substantially causing Aquila to make the wrong decision on the costs of Crossroads. The analysis that was done used inflated turbine costs over those that the Company could have received had they pursued the self-build option in 2004 as opposed to 2008. More important, Aquila likely would have never considered adding a power plant located in Mississippi to its generating fleet unless the costs were substantially lower than any other option. Since having a power plant several hundred miles from the Company's load center presents logistic problem for operations and maintenance and, in particular, substantial costs to transport the power back to GMO's customers. Clearly, it is beneficial to have the generating fleet close to where the electricity is going to be used.

Had KCPL or GMO ever seriously suggested to consider the Crossroads facility Staff would have wanted to know the magnitude of the additional costs that would be involved in

managing the plant facility and the substantial costs relation to the transmission of the power. Those are costs that are incurred as long as the plant is needed for system load requirements.

GMO (AQUILA) 2004 LEAST COST PLANNING DECISION

Q. Mr. Crawford states at page 4 of his rebuttal testimony that "Staff relied on analysis conducted by the Company." Is this correct?

A. Yes. As part of GMO's (Aquila) commitment to the resource planning process, it presented findings from its least cost planning study in 2004. This analysis was based on responses GMO (Aquila) had received from RFP's (similar to the REF process GMO used to support its Crossroads decision in 2007). The 2004 analysis concluded that the least cost plan to replace the Aries purchased power agreement was the construction and installation of five combustion turbines, with each unit sized at 105 megawatts, totaling 525 megawatts of capacity. Staff expressed to the Company that it thought the least cost plan was the best course for GMO (Aquila) to follow. Attached as Highly Confidential Surrebuttal Schedule 1 is the 2004 integrated resource planning presentation regarding its Resource Planning dated February 9, 2004.

The RFP process that GMO wants to ignore from the 2004 time period is the same RFP process used by GMO in 2007 that it now embraces to support its view that Crossroads is the most economic decision. While there is nothing wrong with the 2007 RFP process that GMO conducted to determined its future capacity planning needs this analysis just is not the one that would address GMO's (Aquila) earlier capacity needs in the 2005 time frame. The actual decision needed to be made in 2004 because of the May 2005 expiration of the Aries 500 megawatt purchased power agreement. GMO used the right analysis, just at the wrong time.

Q. Did Staff rely on GMO's (Aquila) least cost plan approach in previous GMO (Aquila) rate cases?

A. Yes. After the completion of the Aries capacity agreement, GMO (Aquila) constructed three combustion turbines at its South Harper facility. This facility was originally sized to accommodate up to six combustion turbines with at least the size of the Siemens model 501 D, each having 105 megawatts of capacity. The three installed combustion turbines total 315 megawatts. Staff supported the use of the cost of these units in rate base in the 2005 rate case. However, the South Harper site was subject to significant legal challenges resulting in the Commission to have to rule on GMO's authority tp construct South Harper and these units three separate times. Therefore, Staff used the costs of South Harper as a surrogate, or proxy, in GMO's (Aquila) 2005 (Case No. ER-2005-0436) and 2007 (Case No. ER-2007-0004) rate cases. In addition to the three combustion turbines, Staff included the capacity for two more combustion turbines of the same size, 105 megawatts.

Q. Has Staff included the South Harper Generating Facility in the rate base of MPS?

A. When Staff had to file its direct testimony in this case on February 13, 2009, the legal process had not been fully completed. Since that time, it is my understanding that the legal issues surrounding the South Harper facility are now resolved with the March 28, 2009 effective date of the Commission's Report and Order in Case No. EA-2009-0118. Staff now considers the South Harper facility to be in rate base in this case. In addition to South Harper generation Staff continues to support the two additional 105 megawatt combustion turbines addressed at pages 85 to 93 in the Staff Cost of Service Report,

and rebuttal and surrebuttal testimonies of Staff witnesses Lena M. Mantle and Charles R. Hyneman.

GMO (AQUILA'S) CAPACITY PLANNING AND ADDITIONAL PEAKING TURBINES

Q. At page 4 of GMO witness Mr. Crawford's rebuttal testimony, he identifies the February 2004 meeting where the least cost plan was provided to Staff. Did you attend meetings between GMO (Aquila) and Staff regarding GMO (Aquila's) decision to build South Harper?

A. Yes. On January 27, 2004, Staff met with several GMO (Aquila) personnel, including Mr. Richard C. Green, then GMO (Aquila's) Chairman, Chief Executive Officer and President. During that meeting GMO (Aquila), based on its 2004 resource plan, committed to install three combustion turbines by June 2005. GMO (Aquila) had these units in storage at its Ralph Green plant located at Pleasant Hill, Missouri. Within the next couple of weeks, in early February 9, 2004, GMO (Aquila) held a second meeting with Staff and Public Counsel at GMO (Aquila's) 6-month Integrated Resource Planning (IRP) presentation to provide the results of GMO (Aquila's) review of its capacity needs. At this meeting GMO (Aquila) provided its analyses of its least cost and preferred plans. Staff questioned GMO (Aquila) about it's analysis of the Preferred Plan, but Staff did express its concerns with GMO (Aquila's) capacity planning effort, and Staff took strong exception with GMO (Aquila) as to why GMO (Aquila) was not pursuing the building of more generating assets, particularly if that was GMO (Aquila's) "least cost" plan.

Q. Did GMO (Aquila) only evaluate its preferred plan?

A. No. When GMO (Aquila) developed its capacity plan and presented it to Staff in January 2004, GMO (Aquila) determined that its least cost plan was to install five combustion turbines, not three. At the February 9, 2004, IRP meeting, GMO (Aquila's) lowest cost plan on a net present value revenue requirements over a 20-year period identified replacing the Aries Agreement by constructing five combustion turbines totaling 535 megawatts, instead of the three totaling 315 megawatts that they installed at the South Harper facility.

Staff asked GMO (Aquila) why it was not pursuing its least cost plan, instead of installing three turbines. GMO (Aquila) indicated that it only had three combustion turbines in storage at the time and planned to use them in its preferred plan. With its preferred plan, GMO (Aquila) would make up the capacity shortfall resulting from the expiration of the Aries Agreement with purchased power agreements.

Q. When did GMO (Aquila) begin planning to replace the power it was taking under the Aries Agreement?

A. Power from the Aries Agreement ended May 31, 2005. So GMO (Aquila) needed to have replacement capacity by that date. GMO (Aquila) started planning to replace the Aries agreement by issuing Request for Proposals (RFPs) as early as the spring of 2001. In response to Data Request No. 166 (Case ER-2005-0436) concerning the Aries replacement power (attached as Highly Confidential Schedule 2) Aquila provided a history of its capacity planning process, with much emphasis on replacing the Aries agreement in 2005.

From the time GMO (Aquila) signed the Aries agreement in February 1999, GMO (Aquila) started considering replacing the Aries capacity, but only with purchased

power agreements. Even though the combustion turbines that are presently installed at the South Harper facility had been in storage since beginning August 2002, it was not until the January 2004 meeting that GMO (Aquila) committed to building a generating plant.

Q. How did GMO (Aquila) meet its capacity requirements after the summer of 2005 when South Harper was complete?

A. Since GMO (Aquila) did not build its least cost plan of five combustion turbines, it relied on short term agreements in each of the years from 2006 to 2008.

Q. Does Staff believe that GMO (Aquila's) capacity planning was prudent?

A. No. Staff has been very critical of GMO (Aquila) approach to addressing its capacity needs for its system. Examples of GMO (Aquila's) decision making:

- Having a corporate policy not to build regulated generation evidenced by not having built generation since 1983, except for South Harper in 2005 which effects the regulated operations to this day.
- In 1997 attempted to move all generating assets to an Exempt Wholesale Generator (EWG), Case No. EM-97-395.
- MPS Resource planning in 1992 determined need for a combined cycle unit by 2000 for MPS yet Aquila's corporate decision made to build unit as a non-regulated merchant plant (Aries) after regulated operations did most of the preliminary work for the development of the project.
- MPS purchased power agreement from 2001 to 2005 from a non-regulated GMO (Aquila) affiliate (Aries Agreement).
- GMO (Aquila) sold its 50% share of Aries giving its partner ** _____ _____ ** to take unit over.
- GMO (Aquila) attempts unsuccessfully to re-acquire Aries in 2006.
- Despite having a known certain date to replace the Aries Agreement by June 2005, GMO (Aquila) did not timely plan for the replacement of this capacity. Until January 2004, did not seriously consider building generation instead looking at another purchased power agreement from an affiliate (Aries II).

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- GMO (Aquila) attempts to sell at steep discounts three turbines which were to be installed at Aries as Aries II in 2002. Units were placed in storage. While units were for sale, at no time were the units ever considered or offered to MPS to meet its growing capacity needs before 2004. In January 2004 GMO (Aquila) made decision to replace Aries Capacity Agreement with three combustion turbines it had left over from its merchant business. These units had been in storage since 2002 during which the units' warranty expired. Units were eventually installed at the South Harper facility.

- South Harper legal issues caused by having to move forward on project to get units in service by June 2005 to replace Aries Agreement. Since GMO (Aquila) already had possession of units since 2002, appropriate planning could have taken place much earlier than it did providing ample time to get necessary community support.

- GMO (Aquila) had many combustion turbines, three of which were new units, in its asset portfolio that it sold at distressed values resulting in hundreds of millions of dollars of impairment charge losses that the Company did not consider to use for its regulated operations despite MPS' need to for capacity. (Raccoon Creek, Goose Creek and General Electric 7 EAs combustion turbines).

- In 2000 Aquila re-acquired MPS' four combustion turbines at Greenwood which it had built starting in 1975 and sold under a sale lease back which had a provision where the Company could acquire the units at the end of the lease at the existing market value. Aquila re-acquired the units at greater than the original purchase price even though the units were 25 years old. The units were reacquired by a Aquila non-regulated MPS affiliate with a corporate decision that MPS entered into a 15-year purchased power agreement. This agreement was ultimately terminated and the units were moved back in the regulated operations of MPS. The 25-year old units are now in rate base at a greater amount than what they were originally purchased for. Customers will have in essence paid for these units twice- once through the lease and now in rate base.

The foregoing demonstrates that Aquila has not had appropriate and effective decision-making regarding its resource plans or its resource planning process. These events and circumstances are not the actions of a typical utility this Commission regulations.

SOUTH HARPER COMBUSTION TURBINE VALUES

Q. What value is Staff using for the South Harper site and three combustion turbines, and which Staff used for its cost of the MPS facility and what it referred to in earlier testimony as Turbines 1 through 3 of the MPS facility?

A. In Case No. EO-2005-0156, GMO (Aquila), Office of Public Counsel and Staff agreed to a value of $66.76 million for the combustion turbines, or $22.25 million per turbine. The cost for these turbines is $211.9 per kilowatt ($66.76 million divided by 315,000 kilowatts). GMO (Aquila) wrote down the turbines to the agreed upon amount and has reflected that amount on its books and records. Both GMO (Aquila) and Staff have included the written down value of $66.76 million for the three turbines in this case.

Q. Was the amount for the turbines agreed to in Case No. EO-2005-0156 the level supported by Staff?

A. Yes. Staff filed extensive testimony in that case supporting the amount that was finally agreed to by GMO (Aquila), the Office of Public Counsel and Staff.

Q. Would you quantify each of the write-downs?

A. GMO (Aquila) made a write-down of over $10 million in November 2004 to reflect, what it believed was a fair value for the three turbines installed at South Harper. Additionally, GMO (Aquila) agreed to an almost $4 million additional write-down when it agreed to value the turbines at the $66.76 million.

Q. Does Staff have market value information for valuing the South Harper combustion turbines?

A. Staff filed testimony in Case No. EO-2005-0156 to support a valuation of $66.76 million for the three South Harper turbines, including related equipment. At one time

GMO (Aquila) offered to sell the turbines for $69 million including a warranty, to KCPL. That offer formed the basis for the Staff's valuation. Attached as Highly Confidential Schedule 3 are documents relating to GMO's (Aquila's) offer to KCPL provided in Data Request No. 38 in Case No. EO-2005-0156. Also, Schedule 4 is a table identifying the various values Staff considered for these units (Data Request No. 5 in Case No. EO-2005-0156).

Q. How did Staff arrive at a valuation of $66.76 million?

A. Because the warranty for the combustion turbines expired while they were in storage, the $69 million was adjusted downward by $2.240 million to reflect the estimated value of the warranty. This estimate of $2.240 million originated from GMO (Aquila) and was the result of discussions it had with the turbine manufacturer and a consultant (R.W. Beck) hired to assist in developing a fair value of the units.

Q. Who manufactured the three combustion turbines?

A. These combustion turbines were manufactured by Siemens and are identified as 501D5A with a capacity rating of 105 megawatts each, resulting in 315 megawatts of total station capacity.

Q. Did GMO (Aquila) purchase these units for its MPS system?

A. No. The units were originally purchased by an GMO (Aquila) affiliate, Aquila Merchant in 2002 under an agreement signed in September 2001. Originally, the units were to be installed at the Aries Generating Facility and called Aries II. Those plans were cancelled in July 2002 during the period of the collapse of the merchant business that affected Aquila Merchant especially hard. The Company started taking delivery of the units in

August 2002 and stored them at GMO's (Aquila's) regulated plant, Ralph Green Generating Facility until they were moved in March 2005 to South Harper.

Q. How did GMO (Aquila) originally intend to use these three combustion turbines?

A. GMO (Aquila) intended to install them at its Aries site and sell power from them to MPS. It was expected that once Aries II went into service, MPS would enter into a purchased power agreement between an GMO (Aquila) affiliate, Aquila Merchant and MPS. The term for the agreement was to be for 15 years starting June 1, 2005, to coincide with the expiration of the Aries agreement May 31, 2005. The expected return on investment for this Aquila Merchant project was between ** ——————— ** [source: Data Request No. 58 in Case No.EO-2005-0156, Highly Confidential Schedule 5-5].

Q. When did GMO (Aquila) decide to use the combustion turbines for its regulated operations, and to include their costs in rate base?

A. Staff was informed of this decision on January 27, 2004, in a meeting with GMO (Aquila's) then Chief Executive Officer, Richard Green. At this meeting, Mr. Green committed that the three turbines in storage would be deployed for the regulated electric operations in Missouri.

These units were installed at South Harper and were declared commercial by GMO (Aquila) on June 30, July 1, and July 14, 2005.

Q. Why do you believe GMO (Aquila) built South Harper?

A. GMO (Aquila) had the three combustion turbines in storage. While GMO (Aquila's) MPS regulated operations needed the capacity, GMO (Aquila) attempted

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unsuccessfully to sell these combustion turbines to unaffiliated entities. GMO (Aquila) finally committed to installing these units for MPS in January 2004.

Absent having the three combustion turbines left over from GMO (Aquila's) merchant business, Staff believes GMO (Aquila) would not have built any peaking capacity. Staff has seen no evidence that indicates GMO (Aquila) had any intention of using the combustion three turbines for MPS' operations. To the contrary, the documentation indicates just the opposite-- that GMO (Aquila) made every attempt to sell the combustion turbines.

Q. When did GMO's then Aquila Networks-MPS operating division learn of the three combustion turbines it installed at South Harper?

A. At the summer 2002 IRP meeting, MPS identified the need for capacity to replace the Aries agreement that was expiring May 31, 2005. Staff indicated to MPS' Resource Planning Group that three combustion turbines existed within GMO (Aquila's) organization; and inquired if they would be considered to replace the Aries capacity. The GMO (Aquila) personnel attending the meeting stated they were unaware of the existence of these combustion turbines. At the summer of 2003 IRP meeting MPS' Resource Planning Group personnel indicated that they were still unaware of the existence of these combustion turbines and, therefore, could not model them. At that time, GMO (Aquila) was considering only purchased power agreements for replacing the Aries capacity. At this 2003 meeting, Staff made it clear that it knew GMO (Aquila) had the combustion turbines in storage, and inquired why GMO (Aquila's) Resource Planning Group was not considering those combustion turbines to meet MPS' capacity requirements in lieu of purchased power agreements. MPS responded that it could only consider what it knew was available, and those combustion turbines were not available for MPS' capacity requirements.

Q. Did GMO (Aquila) ever consider the three combustion turbines for meeting MPS' capacity requirements?

A. Yes. When Aquila Merchant planned on installing these combustion turbines at the Aries facility as a non-regulated merchant plant, GMO (Aquila) was negotiating with itself (its affiliated company), Aquila Merchant, to enter into a 15-year purchased power agreement with MPS. Highly Confidential Schedule 5 is a presentation made by GMO (Aquila's) Capital Deployment Group entitled "Aries II - Peaking Power Facility" dated March 5, 2002, identifies that these combustion turbines were to provide capacity to MPS through 2020.

After GMO (Aquila's) merchant business collapsed in mid-2002, GMO (Aquila) decided in July 2002 not to deploy the three combustion turbines at the Aries site. At this point, these three combustion turbines were no longer considered for meeting MPS' capacity needs. GMO (Aquila) finally decided in January 2004 to use this capacity for MPS, after no other home was found for the three combustion turbines.

Q. When did GMO (Aquila) last consider a self-build option to meet its capacity requirements?

A. GMO witness Mr. Crawford indicates in his rebuttal testimony at page 9 that GMO (Aquila) considered self-build options in 2007. Also, GMO (Aquila's) Generation Group submitted on February 20, 2006, a response to GMO (Aquila's) January 17, 2006, request for proposal. This proposal included several different options for different combustion turbines at a variety of locations. One of the proposed options was ** _____ _____ **.

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This proposal was not pursued by GMO (Aquila). Instead GMO (Aquila) relied on purchased power agreements to meet each peak summer's requirement from 2006 to 2008.

Prior to this response, GMO (Aquila's) Generation Group, on November 22, 2004, submitted a response to GMO (Aquila's) October 15, 2004, request for proposal for capacity year 2007 [Data Request No. 166, in Case No. ER-2005-436]. However, GMO (Aquila) made no attempt to consider meeting MPS' capacity needs by purchasing any combustion turbines. GMO (Aquila) did not contact combustion turbine manufactures for bids nor did it attempt to negotiate a contract with any combustion turbine supplier. Consequently, GMO (Aquila) was not in any position to seriously consider installing more generating assets. GMO (Aquila) did not consider meeting its system load requirements by any means other than purchasing the capacity.

Prior to early 2006, GMO (Aquila) did not consider several options that other utilities have pursued, options such as: 1) seeking from combustion turbine manufactures new combustion turbine sale offers; 2) requesting offers from combustion turbine manufacturers for new equipment that has been released by the original buyer before delivery, which vendor manufacturers discount; 3) pursuing the gray market for combustion turbines from non-turbine manufactures; and 4) examining access to existing facilities Aquila owned and ultimately sold to third party non-affiliates, such as AmerenUE.

COSTS VALUATION OF CROSSROADS

Q. GMO witness Mr. Crawford states at page 11 of his rebuttal testimony that since the Company received offers for long-term capacity and energy options from two non-affiliates that supported Crossroads being "determined to be the lowest cost option." Do you agree with this assertion?

A. No. As stated previously, GMO conclusions are faulty because they examined and compared the market prices for capacity, in particular, the self-build option during the wrong time frame. The decision to replace the Aries capacity was in 2004 for installation by summer of 2005. The March 19, 2007 GMO request for proposal was three years too late. Any analysis that would need to be done to make cost determinations for Crossroads would have had to use turbine pricing well before the 2007 time frame. Combustion turbine costs have increased significantly since 2003 and 2004.

Q. Are the turbine costs at Crossroads overstated?

A. Yes. The value of Crossroads is substantially overstated because the four combustion turbine installed at that facility were purchased at a time when turbine manufactures were selling those units in sellers' market during very high prices. GMO (Aquila) had many opportunities to acquire turbine capacity for installation in and around its load center at greatly reduced prices compared to those for the Crossroads facility. If the Commission allows Crossroads in rate base it should do so at a substantially reduced amount than what GMO is requesting in this case.

The four Crossroads turbine are book valued at approximately ** ____ ** million each, or a total of ** ____ _ ** million. Staff believes those values should be significantly reduced in the range of ** _____ ** million each or total range of ** _____ ** million for inclusion in rate base based on sales and offers to other utilities made by GMO (Aquila). This would reduce the increased costs of operating a plant facility that has higher annual transmission costs, natural gas fuel costs, and transmission investment over and above the levels that would have existed if GMO (Aquila) would have installed capacity at existing plant sites such as South Harper.

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In addition to the turbine values being over stated, the costs of the transmission plant at Crossroads is higher than it would be if GMO (Aquila) would have installed the turbines at an existing site such as South Harper. Staff believes that the there was a ** ___ ** million amount that was estimated for transmission upgrades at the Aries site where those three South Harper turbines were originally planned to be installed. Crossroads transmission is substantially higher than this transmission upgrade estimate.

Staff believes that the annual transmission expenses will be higher for the Crossroads units because of where they are located. If the turbines would have been installed in the Kansas City area the transmission costs would be dramatically less.

Staff believes that the natural gas costs will be higher at Crossroads than it would be if the capacity was located in the Kansas City area.

COMBUSTION TURBINE COSTS

Q. What is your basis for asserting combustion turbine prices have gone up since the time that GMO should have made decision in 2004 to replace the 2005 Aries capacity agreement?

A. In every case since the 2005 rate case Staff has reviewed pricing of combustion turbines. Like previous GMO rate cases, Staff reviewed the industry publication of *Gas Turbine World* for the publication years 2007-2008 and 2009. In the 2007-2008 GTW Handbook, *Gas Turbine World* reports that turbine prices increased 20 to 30 percent over 2006 levels. At page 29 of this industry publication the following appears:

> **Seeing dramatic increase in prices**
>
> During the past 18 months we have seen power plant equipment prices increase by as much as 20-30 percent over pre-2006

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> levels. Meanwhile delivery schedules have stretched out to 16-18 months from 12 months or less, as growing demand puts strain on available manufacturing capacity.
>
> Special orders that require additional engineering can add seven months of lead time.
> The rise in equipment price levels since 2006 has been driven by a worldwide increase in cost of materials, higher manufacturing costs, and growing market demand.
>
> Over the last few years, copper has more than tripled to $3.40 per pound from around $1, molybdenum six-fold to $31 per pound from around $5, aluminum almost doubled to $2,800 per ton from $1,500, and nickel almost quadrupled to $31,000 per ton form $8,000.

Staff's review of the Gas Turbine World identified that General Electric's new model that replaced the 7 EA model that is installed at Crossroads is valued at $19.5 million in the 2007-2008 GTW Handbook and $25.9 million in the 2009 GTW Handbook. This indicates that prices in the 2007 and 2008 time period shows substantial increases over the time that GMO (Aquila) should have installed turbines to meet the capacity needs of its customers back in 2005.

Q. Were the General Electric 7 EA model combustion turbines valued less in the 2004 time period?

A. Yes. At a time GMO (Aquila) should of added capacity the General Electric 7EA models were significantly less than the Crossroads of 2001. *Gas Turbine World* reported in its 2004-2005 Handbook that these units were selling for $14.8 million. The 2003 price was $16.6 million and the 2000-2001price was $21 million. This compares to the actual Crossroads book value of ** ____ ** million each. The volatility of the natural gas market contributed to the decline in sales of gas-fired generation on top of a market decline caused by the implosion of the merchant energy market during the 2002 to 2005 time period.

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This would have been an ideal time to purchase capacity if a utility needed generation, which GMO (Aquila) did.

In 2006, the price for the General Electric 7 EA (new model PG7121(EA)) had gone up to $19.2 million according to the 2006 Handbook.

The South Harper Siemens 501D5A units saw prices follow the same pattern going from high at the start of the decade to significant price reductions during 2003 and 2004 time frame. In the "2004-05 GTW Handout, published by *Gas Turbine World*, the price of Siemens 501D5A was quoted at $18.7 million. In the 2003 Handbook, the value was $19.9 million and the 2000-2001 Handbook had 5015DA priced out at $25.5 million. Based on the information, the market cost of these units has been trending downward during the time Aquila would have been needed the five turbines to replace the Aries Agreement.

However, recently the 2006 Handbook identified a significant price increase for the Siemens 501D5A (new model SGT6-3000E) to $22.8 million per unit.

Q. Is the $18.7 million amount for the Siemens 501D5A solely for the cost of the turbine, or does it include related costs?

A. *Gas Turbine World* does surveys of the industry and contacts turbine manufactures to determine its pricing information. Some of its data is for actual purchases made by companies - regulated utilities and merchant companies alike. While there may be added costs for these turbine prices because a utility may want specific features based on individual needs like duel fuel source burning capability and fast-start capability, typically these are prices what the industry relies on to trend costs of turbine equipment.

Q. What information, other than the $69 million offer to KCPL for the South Harper turbines, is Staff aware of bearing on the valuation of the three combustion turbines GMO (Aquila) installed at the South Harper Facility?

A. GMO (Aquila) has made offers to sell turbines to third parties and has sold or given up rights to several turbines over the past several years. Staff has reviewed documents relating to these offers and sale transactions which identified the pricing of turbines from 2002 to present.

1) GMO (Aquila) had four General Electric model 7EA natural gas-fired 75 megawatt turbines that it sold in 2003.

2) GMO (Aquila) sold to AmerenUE its Goose Creek and Raccoon Creek Generating Facilities in 2006.

3) GMO (Aquila) had an offer from Rolls-Royce Power Company to sell two Siemens 501 D5A natural gas-fired combustion turbines.

4) Staff has seen offers made by turbine manufacturers to another Missouri utility in the range identified in the *Gas Turbine World*.

GENERAL ELECTRIC 7 EAS

Q. At what price did GMO's (Aquila's) affiliate sell its General Electric combustion turbines?

A. Aquila Merchant sold three turbines with rated capacity of 75 megawatts each, to two non-affiliates for ** ___ ** million or ** ___ ** million each and a third turbine was sold for ** ___ ** million. All three turbines were sold substantially below the original purchase price of ** ___ ** million [Data Request No. 77 in Case No. EO-2005-0156]. The average price entities in 2003. Two were sold that Aquila Merchant sold these three units was ** ___ ** million [** ___ ** million plus ** ___ **

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million divided by three]. Using this average price, GMO (Aquila) would have had a far better price at which to deploy these three General Electric turbines to meet its regulated system requirements and greater megawatt capacity. These prices compare with the Crossroads turbine values of ** ___ ** million per unit price for the same GE 7 EA model that GMO is expecting to put into rate base in this case.

The total costs for the three General Electric turbines sold to third parties would be ** ___ ** million with a total capacity of 225 megawatts, or ** ___ ** per kilowatts, far below the three Siemens turbine costs used at South Harper. Two 501D5A turbines are 210 megawatts of capacity compared to the 225 megawatts of capacity of three General Electric 7EA turbines would have been retained by Aquila and installed at South Harper, or another existing site. It would have been more cost effective to install the three General Electric 7EAs having greater capacity than the two Siemens units. Staff, in pricing of two additional turbines, chose to include the higher costs of the Siemens turbines to be conservative in its costing of these units.

Q. Where were the purchasers of these combustion turbines located?

A. Two turbines were sold to a utility in Beatrice, Nebraska, and the third turbine was sold to a utility in Colorado (Data Request No. 43 in Case No. EO-2005-0156).

Q. Did Aquila Merchant have any other General Electric combustion turbines?

A. Yes. Aquila Merchant originally purchased 18 General Electric 7 EAs, taking delivery and deploying 10 turbines at two different site locations in Illinois (these turbines will be discussed later). Four other turbines were deployed at the Crossroads Energy Center located in Mississippi.

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As noted above, three of the General Electric turbines were sold to Colorado and Nebraska entities and a fourth turbine was release back to the manufacture, with GMO (Aquila) losing the reservation (option) payments it had made to General Electric.

Q. Were there any offers made by GMO (Aquila) regarding the four General Electric combustion turbines before execution of the contracts under which they were sold?

A. Yes. Like the Siemens turbines installed at South Harper, GMO (Aquila) offered the General Electric turbines to other entities including KCPL.

Q. Did GMO (Aquila's) MPS or L&P divisions have an opportunity to acquire any of these four General Electric 7 EAs combustion turbines?

A. No. GMO (Aquila) never considered using these turbines for its regulated operations, even though MPS needed to replace the Aries agreement by June 2005. GMO (Aquila) indicated that these turbines were sold in 2003, in advance of decision to install turbines at South Harper. (Data Request No. 43, Case No. EO-2005-0156).

SALE OF NATURAL GAS-FIRED COMBUSTION TURBINES AT RACCOON CREEK AND GOOSE CREEK

Q. Did GMO (Aquila) have generating facilities located outside of its service territories?

A. Yes. Aquila Merchant built two generating facilities in Illinois, Raccoon Creek and Goose Creek.

Q. Would you describe these facilities?

A. Aquila Merchant installed ten General Electric 7EAs, 75 megawatt turbines at two locations in Illinois. Six 7EAs were installed at Goose Creek Energy Center having a combined capacity of 510 megawatts. Four 7EAs were installed at Raccoon Creek Energy

Center having a combined capacity of 340 megawatts. GMO (Aquila) responded to an RFP to supply turbine capacity issued by AmerenUE in the summer of 2005. GMO (Aquila) disclosed to the Staff it had offered in August 2005 to sell them to AmerenUE in response to Data Request No. 464 (Case ER-2005-0436).

Q. What were the terms of GMO (Aquila's) original offer?

A. GMO (Aquila) offered to sell both facilities (ten installed turbines) to AmerenUE on the following terms.

** _____
_____
_____
_____ ___ _____
_____
_____
_____
_____
_____ **

[Data Request No. 464 in ER-2005-0436; Highly Confidential Schedule 13-4]

Q. Has the sale been completed?

A. Yes. On December 16, 2005, GMO (Aquila) entered into an asset purchase and sale agreement with the final sale transaction completed in early 2006.

Q. Do you know if negotiations between the two parties changed the initial terms of the offer?

A. Yes, it did. The final sell price for both Raccoon Creek and Goose Creek was $175 million for all the generating equipment, substation and transmission costs.

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The total capacity of these two generating stations equal 850 megawatts resulting in an installed capacity of $205.88 per kilowatt ($175 million divided by 850,000 kilowatts) [source: Aquila's SEC Form 8-K filed December 16, 2006].

Q. Based on the original offer, what would the price be on a installed kilowatt basis?

A. The installed kilowatt for Aquila's initial offer would be between ** _____ _____ **. The final price paid for both facilities of $175 million resulted in the installed kilowatt would be $233 per kilowatt [$175 million dividend by 750,000 kilowatts of installed capacity].

Q. Did GMO (Aquila) lose money on the sale of these units?

A. Yes. Because of the distressed nature of the merchant business at the time, GMO (Aquila) incurred a pre-tax non-cash impairment charge of approximately $93.6 million for Goose Creek and $65.9 million for Raccoon Creek, or a total after-tax loss of $99.7 million ($58.5 million and $41.2 million) [source: Aquila's SEC Form 8-K filed December 16, 2006].

Q. Are the Raccoon Creek and Goose Creek facilities both fully operational generating plants?

A. Yes. Both of these facilities are fully operating generating stations. They were installed in 2003.

Q. Did GMO (Aquila's) MPS or L&P divisions have an opportunity to acquire these facilities?

NP

A. No. GMO (Aquila's) position is that the units are located in Illinois and there was not sufficient transmission path to get the power from those units to the MPS and L&P systems.

Q. Could the combustion turbine units at these facilities be moved?

A. Yes. The turbines presently at South Harper were moved from the Ralph Green Generating Facility where they were in storage. While these units were not installed at Ralph Green, the units, with considerable effort, were moved to the South Harper facility. Turbines, generators and related equipment are heavy pieces of machinery requiring special transportation and hauling, but they are moved from the manufacturer and from different locations. Moving such equipment in the electric utility industry is not particularly unique. Indeed the Greenwood Generating Facility, which has four combustion turbines, initially had a lease agreement that required GMO (Aquila) to move, at its expense, the generating units at the end of the lease to a destination designated by the Greenwood owners. Since the Greenwood Units were reacquired by GMO (Aquila) in 2000, the units were not moved.

Q. Would the sale of the Raccoon Creek or Goose Creek facilities have any impact on the Staff's estimate of the cost to GMO (Aquila) of additional combustion turbines capable of generating about 210 megawatts?

A. Staff's estimate would not change as result of this sale transaction. But the sale price on a cost per kilowatt identified above supports the conservative nature of Staff's installed kilowatt costs identified in Mr. Hyneman's direct testimony. The installed cost for Turbines 4 and 5 of $304 per kilowatt is significantly higher than the final selling price of $205.88 per kilowatt costs for Raccoon Creek and Goose Creek facilities.

Initially, in the last case, Staff relied on the Aquila offer made to AmerenUE for Raccoon Creek and Goose Creek facilities as a conservative estimate for Turbine 4 and 5 costs. Since the final price for these units were not finalized at the time of the direct filing in the 2005 case, Staff used a $275 kilowatt amount for 210,000 kilowatts compared to the ** ———— ** per kilowatt offer price. Since added additional conservative nature to the costs for Turbines 4 and 5 by taking another approach identifying the costs of the turbines and construction costs resulting in even higher costs of $304 per kilowatt. At the same time the final costs to for the Raccoon Creek and Goose Creek facilities decreased to $205.88 per kilowatt resulting in almost a $100 per kilowatt higher amount for the two additional combustion turbines referred to as Turbines 4 and 5.

Q. Are the Raccoon Creek and Goose Creek installed costs paid by AmerenUE lower than the installed costs of Crossroads?

A. Mr. Crawford identifies the installed costs of Crossroads at ** —— ** per kilowatt while the Raccoon Creek and Goose Creek installed cost is $205 per kilowatt.

Q. Have there other generating facilities sold recently?

A. Yes. On January 10, 2007, it was announced that Public Service Enterprise Group sold to American Electric Power, a relatively new natural gas-fired 1,096 megawatt combined cycle power plant located in Lawrenceburg, Indiana. The selling price was $325 million resulting in a $296.53 per kilowatt value, lower than the South Harper installed costs of $454.17 per kilowatt and the Turbines 4 and 5 installed costs of $304.12 per kilowatt.

On January 16, 2007, it was announced by independent generator Mirant Corporation that it was selling to LS Power six natural gas-fired plants, with total capacity of 3,619 megawatts for $1.407 billion resulting in a cost of $388.78 per kilowatt. These plants,

the 903 megawatt Zeeland plant in Michigan, the 613 megawatt West Georgia plant in Georgia, the 469 megawatt Shady Hills plant in Florida, the 561 megawatt Sugar Creek and the 546 megawatt Bosque plants in Indiana and the 527 megawatt Apex plant in Nevada, all were included in the $1.407 price paid to Mirant.

ROLLS-ROYCE POWER VENTURES OFFER

Q. Is the Staff aware of any other offers for sale of combustion turbines involving GMO (Aquila)?

A. Yes. During the audit in Case No. EO-2005-0156, GMO (Aquila) provided supporting information on the appraisals per the South Harper valuation issue (Data Request No. 5 in Case No. EO-2005-0156). In material supplied by GMO (Aquila), the Staff learned that on September 23, 2004, Rolls-Royce Power Ventures (Rolls-Royce) offered to sell GMO (Aquila) two new Siemens 501D5A natural gas-fired turbines that were manufactured in 2001 and placed in storage in Houston and Germany (Schedule 14). Both units were offered for $43 million, or $21.5 million each. This initial price was less than the South Harper turbines but, for comparison purposes, several adjustments to the price needed to be added, such as transportation costs and Siemens Technical Field Assistance. Also, the warranty had expired similar to the South Harper turbines and was estimated that would increase both unit costs by total of $2.240 million, the same as the warranty estimate for the South Harper turbines—GMO (Aquila) ultimately opted not to re-purchase the warranty from Siemens for the South Harper turbines. Another major expense would be converting the combustion system for approximating $5 million. Adding all the costs to the initial offer of $43 million did not make these units attractive to GMO (Aquila).

But it is noteworthy that while the Rolls-Royce offer was high in relation to the other turbine information Staff reviewed, it does represent the only tangible evidence that GMO (Aquila) had regarding its review of the actual turbine market for its regulated operations. No other information has been brought to Staff's attention that would indicate that (Aquila) actually pursued the acquisition of turbines for either of its MPS or L&P divisions with the exception of South Harper during the 2003 and 2005 time frame.

OTHER UTILITY OFFERS

Q. Does Staff have experience with equipment supply agreements in the course of performing its duties for the Commission?

A. Yes. Over the course of many years Staff has seen numerous contracts for actual purchases of equipment. Staff has seen numerous bids or quotes for proposed purchases of equipment. Without detailing the specifics, turbine costs have generally declined during the period from early in the decade to the period of 2004 and 2005, at time when GMO (Aquila) should have made the decision to install additional capacity over the levels it did at South Harper. Now the turbine prices have gone back up. GMO is using the higher priced turbines to justify its decision to rely on Crossroads-- a plant that has overstated turbine costs, has high transmission costs and is located in Mississippi that has higher natural gas costs. Turbine prices started to increase as the turbine market stabilizes from the fallout of the collapse of the merchant market.

Q. Has Staff reviewed bids and offers for generating equipment?

A. Yes. At various times, in rate cases, construction audits, development of regulatory plans or as part of the Commission's Chapter 22 resource planning process,

Staff has had opportunities to review request for proposals, offers and bids for generating equipment, including turbine offers.

While this information on other utilities is confidential, the offers we have seen over the past several years substantiate the general decline in the turbine market during the time GMO (Aquila) needed to make decision to replace the Aries capacity agreement. Specifically, during the time frame of 2003 and 2004, there were very attractive pricing for turbine equipment. Other companies have been benefiting from this "buyers'" market, but GMO (Aquila) chose not to make the proper decisions. Consequently, GMO was faced with need for capacity in 2008 and made decision to use a unit located in Mississippi that is poorly situated to meet system load requirements in its service territory.

COMBUSTION TURBINES HAVE EXPERIENCED A SIGNIFICANT DECLINE IN VALUES

Q. When did Aquila Merchant and Siemens negotiate for the three combustion turbines that Aquila installed at the South Harper Facility?

A. In late 2000 through out summer 2001. The turbine contract between Siemens and Aquila Merchant was signed September 2001 for an in service date of June 2003. Aquila Merchant planned to have a purchased power agreement with MPS for 15 years starting in June 2005.

Q. Was the combustion turbine market different in 2000 and 2001 than in 2003 and 2004 when (GMO) Aquila should have been planning for replacement of the power it was taking under the Aries capacity agreement?

A. Yes. In 2000 and 2001, when Aquila Merchant negotiated for the South Harper turbines, the power equipment industry was experiencing a sellers' market.

Purchasers were paying premiums to reserve manufacturer's slots to place orders and negotiate contract terms. During an interview David Kreimer, GMO (Aquila) former Director of Engineering, indicated "that during the time Aquila Merchant was negotiating with Siemens for the three combustion turbines it was a brutal sellers market for all forms of generation." He stated "that it was the most brutal sellers' [market] that he experienced in the 30 years that he had been working in the industry at the time of the negotiations and when Aquila Merchant entered into the agreement to purchase these combustion turbines." Mr. Kreimer stated that "the sellers' market peaked around August 2002 and pricing for the large F frame machines began to decline quickly….the sellers' market for the larger [Siemens] F model combustion turbines started losing value first before the values for the smaller Siemens 501D5a's and General Electric 7EA combustion turbine[s] started to decline—the smaller combustion turbine's market value lasted longer" [Source: Data Request No. 56.1 in Case No. EO-2005-0156, April 29, 2005 Kreimer interview].

Q. What is the size of the l F frame combustion turbines that Mr. Kreimer referred to in his interview?

A. The F frame units are Siemens 501FD combustion turbines and are the range of 150 to 160 megawatts in size. The Aries Combined Cycle Unit has two F frame combustion turbines. The Siemens 501D5A combustion turbines GMO (Aquila) installed at the South Harper Facility are 105 megawatts and the smaller General Electric 7EA combustion turbines are the units at Crossroads, Raccoon Creek and Goose Creek. These are nominally rated at 75 to 80 megawatts. [Source: Data Request No. 56.1, April 29, 2005 Kreimer interview]

Q. Was Mr. Kreimer involved in Aquila Merchant's purchase of the three Siemens turbines from Siemens Westinghouse?

A. Yes. When GMO (Aquila) negotiated for and bought these units, Mr. Kreimer was employed by Aquila Merchant. He was directly involved in the discussions between Siemens Westinghouse and GMO (Aquila) regarding these combustion turbines. Mr. Kreimer also was involved in the negotiations of a 1999 contract to purchase two Siemens 501F EconoPacs installed at the Aries facility near Mount Pleasant, Missouri to create the combined-cycle unit.

Q. Why is the nature of the combustion turbine market that was occurring in 2000 and 2001, described as a brutal sellers' market, important now?

A. Combustion turbine prices declined after the 2001-2002 timeframe ending the sellers' market in this country. The power equipment market was substantially impacted as result of the collapse of the merchant power market and the utility industry's building of natural gas-fired generation.

During this sellers market is when the Crossroads units were originally purchased by Aquila Merchant. The values that GMO is requesting be included in rate base in this case are the book values of the original purchased price made in the very high sellers' turbine market. Therefore, the GMO recommended rate base amount in this case is higher than it should be if GMO (Aquila) would have purchased the Aries replacement power at the time when the turbine market collapsed during the 2003 and 2004 time period.

ADVANTAGES OF UTIIITY OWNING GENERATING ASSETS

Q. What are the advantages of regulated utilities building, owning and operating their own generating facilities?

A. Utilities are able to control the operations of the generating facilities if they own and operate those assets. Utilities will not be subjected to the volatility of the market place with cost increases related to purchased power if they operate their own generating assets. Also, utilities are able to provide a much more reliable source of energy when the regulated company has its generation under its authority. The regulated entity can operate the unit in a prudent and economic manner and can maintain and make capital improvements to prolong the life of this valuable asset.

Q. Are there advantages for regulated utilities to own generating facilities?

A. The control of generating facilities by utilities is considered very important. Companies can better manage costs for maintenance and reliability of units if they own them. In essence, by controlling the generating unit, the Company is much more in charge of its own destiny. In an interview with Staff on November 14, 2003, Mr. Terry Hedrick, GMO (Aquila's) Generation Services Manager and the Project Manager of South Harper he indicated that he believed there were "significant advantages in both owning and operating the generation equipment in developing maintenance expertise. If you control / own the equipment, he believes that there are advantages in the areas of costs, manpower and staffing and dispatch flexibility." (Data Request No. 616.1 in Case No. ER-2004-0034)

Q. Are there advantages to customers if regulated utilities own their generating assets?

A. Yes. Generally, the costs (revenue requirements) are higher in the early years of ownership. The capital costs of the plant investment require a return (return on investment) and the utility is entitled to a recovery of the investment (return of investment). As the plant investment is recovered through depreciation - the return of investment - the rate base return

required - return on the investment - decreases. At some point in the future, especially if the plant lives are longer than expected, such as in the case of Aquila's Sibley generating units, the customers will have the benefit of the plant while the rate base investment is very low. The return on investment declines which causes the revenue requirements to decline dramatically.

Q. Is GMO (Aquila) in a position to reap these advantages?

A. No. GMO (Aquila), by deciding not to build regulated generation for a period of over 20 years since 1983 put its customers at risk because there is a substantial amount of capacity that it is having to replace - at least 500 megawatts - since the Aries purchased power agreement expired in May 2005. GMO (Aquila) made no commitment to build regulated generation for over 20 years, unlike every other major electric utility that operates in this state, and now faces the challenge of replacing the Aries capacity in large block of power, at least 500 megawatts. It has met part a good part of this capacity with South Harper.

Q. Did Aquila Merchant recognize the advantages of owning generating facilities?

A. Yes. Aquila Merchant acquired several generating assets during the 2000 and 2001 time frame including Aries. GMO (Aquila) believed that the forecast for power costs would be increasing over time, made decisions to "lock in" the cost of owning its own generation, so it could take advantage of the increasing market for power costs. In an October 29, 2003, interview Mr. Max Sherman, a former Aquila Merchant employee and Project Manager during the early development and construction phase of the Aries plant and Crossroads, he discussed the need for generating units:

> Aquila Merchant committed to purchase 12 or more combustion turbines during this period (starting in 2000) to build unregulated peakers to take advantage of the wholesale marketplace (this was after the Aries construction decision had

> been made and the plant was under construction). The reason for Aquila Merchant's acquisition of the combustion turbines was its belief that**, given expected future power market conditions, it would be less expensive to produce power from generating units you control than to have to buy power in the marketplace.** Mr. Sherman indicated that the last place a merchant company wanted to be was to have to supply power through long-term contracts and be at the mercy of a volatile power market and have to buy power to supply those contracts….
>
> [Data Request No. 549 in Case No. ER-2004-0034; emphasis added]

Non-regulated merchant companies would want their own generation so they would not be at the mercy of power pricing "spikes." This was especially important if power had to be delivered through contracts to third parties.

If the regulated entity that did not build and operate its own generating units believed that power costs were going to increase, it would have to enter into purchased power agreements priced at market-based rates. The non-regulated merchant company who negotiated to deliver power to the regulated entity at the escalating market-based contracts benefit if they own and operate their generation assets. In some cases the non-regulated merchant may supply power by either generating or acquiring power through a purchase from another party. The profitability of the non-regulated merchant will depend on the ability to acquire or generate the power at a cost that would be below that which it would receive in revenues. Since GMO (Aquila) believed there was going to be a significant rise in the power market costs, the non-regulated subsidiary built and acquired generating assets to engage in the open market for power.

Q. Would the same concern in a rising energy cost market favor regulated entities owning generating assets?

A. Yes. The approach that Aquila Merchant pursued could also have been followed by the regulated MPS division. For the exact reasons that Aquila Merchant believed it was necessary to own the generating assets, MPS should have built and operated its own generation. This was especially important when you take into consideration that the Company believed that the power market costs were going to rise significantly over time. The decision by GMO (Aquila) to allow the Aquila Merchant organization to build and acquire generating assets and sell that power through the open market through purchased power agreements like those entered into between the Aries partners and MPS resulted in the situation where (Aquila's) regulated operations were subjected to the volatility of the market for power costs. It is clear that Aquila Merchant believed that it could not enter into long-term agreements and be subjected to the whims of the market place in supplying that power, thus causing them to reach a decision to own the generating assets in order to supply those power needs to their non-regulated customers. It should be just as clear that the regulated entity, MPS, would also want to own generating assets in this same situation.

Q. Do know of any non-regulated merchant company that builds it own generating facilities?

A. Yes. In a meeting with Calpine in the spring 2005, Staff asked Calpine if it supplied electricity to its customers on a long-term basis using purchased power agreements. Calpine indicated that it was in the business of owning and operating its generating facilities and would not meet long-term power commitments to customers by purchasing the power.

Q. Are there advantages to the utility in owning and operating generating facilities as regulated assets?

A. Yes. Regulated assets are typically put in rate base which, when the units are completed and declared in service, are included in rates allowing the utility a reasonable return on the investment and a recovery over the life of the generating asset through depreciation expense. Thus, a utility is provided some reasonable assurance that the investment in the regulated asset will be fully recovered from its retail electric customers. This provides some reasonable assurance to investors that their asset will be protected through the regulatory process by rate basing the asset. Utility customers benefit by being insulated from rising costs for power during a time when those costs are expected to significantly increase. The customers and the utility owners gain substantial advantages when a company builds and places in service, generating facilities in its regulated operations.

Q. Are there also disadvantages in placing generating assets in the regulated operations?

A. Yes. If there are rising power market costs, a company owning both regulated and non-regulated entities would be at a relative disadvantage if it put the generating facilities in its regulated operations, because it would not be able to shield the profits obtained from the regulated entity. While the regulated entity would have an opportunity to sell the generating capacity in the open market during the period of expected rising power costs, the profits from these transactions are typically included in the ratemaking process. For as long as the regulated entity can stay out of a rate case, the company will benefit from the increased sales. However, when the regulated entity files for rate relief, the power sales would be considered in the rate process. The decision to put generating assets in a regulated entity of a company would cause the non-regulated entity to miss opportunities for profit making in the increased power cost market. Assets that are in the regulated operations would be held to a typical

regulated return which would likely be less than those that would be received by non-regulated entities engaging in profit taking from a rising power market. GMO (Aquila) believed that it could receive greater returns on its investment dollars by having a non-regulated entity, Aquila Merchant, own the generating facilities and selling the power through purchased power agreements to entities like MPS in the open market through market-based pricing. As the market reflected the increased power costs, the non-regulated entity would also receive the increased revenues resulting in greater-than-regulated returns.

Q. Do you know of an example where GMO (Aquila) has been subjected to increasing costs through market-based pricing?

A. Yes. In the 1970s, GMO (Aquila), then operating as Missouri Public Service Company, built four combustion turbines at its Greenwood Generating Station. Upon completion, the Company sold at book value to financial institutions, all four of the combustion turbines, and received the capacity power through a 25-year lease for each of the generating units. The lease did not allow for any residual value to be passed to the utility entity that originally owned the generating units. Upon expiration of the lease, GMO (Aquila) reacquired those four combustion turbines at an existing market-based price. In essence, the Company has purchased the same asset twice. The cost to reacquire the assets at the current market is very close to the original purchase price paid for the assets when they were new. Thus, GMO (Aquila) bought 25-year-old generators and paid close to what the original investment was back in the mid-1970s. Customers paid for 25 years lease payments which in large part covered the fixed costs of the units with MPS having the responsibility for all operating and maintenance costs along with any capital additions. MPS customers are now

paying in rates for the units which have a greater value than when they were new-- in essence paying a second time for the units.

EFFECTS OF GMO (AQUIILA'S) DECISION NOT TO TREAT ARIES AS A REGULATED GENERATING FACILITY

Q. Did GMO (Aquila) ever consider building Aries as part of its regulated operations?

A. Yes. In 1998, prior to the decision to build Aries by the non-regulated side of GMO (Aquila), the regulated operations of MPS considered building a 500-megawatt combined cycle unit on the same land that Aries is now on. Because of GMO (Aquila's), then corporate policy to not build regulated generating units, GMO (Aquila) decided this unit would be a non-regulated non-rate based EWG operating within MPSs service area, with MPS regulated operations bidding on the capacity.

In the summer of 1998, at the time of the initial evaluations of the request for proposals (RFP) for capacity for MPS, which were issued on May 22, 1998, the regulated operations of GMO (Aquila) responded to its own RFP with a "build" proposal. This build option to supply capacity and energy to MPS from a combined cycle unit operated by the EWG was the low cost option at the time of the initial review phase of the RFP.

Q. Why didn't the regulated side of GMO (Aquila (MPS)) build the combined cycle unit as an EWG?

A. The MPS regulated operations of GMO (Aquila) presented its proposal to Robert K. Green, then Aquila President, who made the decision that the regulated side of its operations would not build Aries. The material covered two different dates: 1) October 8, 1998, - Financial Analysis of Supply Options, and 2) October 28, 1998, - Updated Analysis of

Supply Options. The presentation material was provided to Staff in response to Data Request No. 301 (Case No. ER-2004-0034) and is attached to this testimony as Highly Confidential Surrebuttal Schedules 6 and 7.

Q. How did Staff learn of the process GMO (Aquila) used to determine who would build Aries?

A. This was discussed with former GMO (Aquila) personnel who were involved in not only the issuance and review of the RFP, but also as one of the bidders to the RFP to supply capacity to MPS through the EWG. Staff conducted an interview with the individuals who were directly involved in the issuance and review of the RFP and also in making the decision to submit a bid to build a combined cycle unit to supply power to MPS as an EWG.

Q. How did the interview with the former Aquila personnel come about?

A. Staff indicated to GMO (Aquila) that it wanted to discuss the RFP process and aspects of how MPS came to agree to purchase power from the Aries partners. GMO (Aquila) contacted two individuals who were directly involved in these decisions and provided them for an interview with Staff.

Q. Is it Staff's view that GMO (Aquila) should have given more consideration to building Aries as a regulated unit?

A. Yes. Staff believes that had GMO (Aquila) built Aries as a regulated generating station and rate based it in the traditional manner, GMO (Aquila's) likely would not have the capacity problems it has today. Staff has had issues with GMO (Aquila's) decision making regarding building generating units since GMO (Aquila's) 2001 rate case, Case No. ER-2001-672. In each case since, Case Nos. ER-2004-0034, ER-2005-0436 and

ER-2007-0004, Staff expressed its concerns on Aquila's decision not to build generation units and proposed adjustments relating GMO (Aquila's) purchase power agreements.

Q. Had GMO (Aquila) examined building a combined cycle unit as a regulated asset in the past?

A. Yes. In its 1992 Integrated Resource Plan dated February 1992, GMO (Aquila) identified that its recommendation was to build ** _____ _____ ** for MPS.

[February 3, 1992 Integrated Resource Plan-Executive Summary, Item 6.]

Q. Did the regulated MPS develop the Aries project?

A. Yes. MPS throughout the late 1990s developed the 500 MW combined-cycle unit that ultimately became the Aries Combined Cycle Generating Facility. The site for Aries was land that was previously owned by Missouri Public Service Company, the predecessor to UtiliCorp.

Q. Did MPS incur costs to develop the Aries site?

A. During the early and mid-1990's, the regulated MPS expended funds to continue to study and develop the preliminary work that was necessary to prepare for construction of this project. Ultimately, GMO (Aquila) corporate management determined that the regulated MPS would not be permitted to build the Aries facility but rather its non-regulated Aquila Merchant would develop this project. Aquila Merchant took over the Aries project in the summer of 1998.

Q. When was the Aries capacity agreement signed with MPS?

A. MPS entered into this purchased power agreement with its affiliate, Aquila Merchant, in February 1999.

NP

Q. Did MPS prepare cost estimates for the Aries project?

A. Yes. In an interview with David Kreimer, he indicated that he spent a substantial amount of his time during the winter and spring months of 1998 developing preliminary cost data and studying the estimates for the 500 MW combined cycle unit that ultimately became Aries.

Q. Were these cost estimates and studies provided to Aquila Merchant assisting in building the Aries facility?

A. Yes. The regulated MPS did much of the preliminary work to get Aries project to the construction stage.

Q. How did the Aries purchased power agreement come about?

A. In the spring of 1998, MPS issued a request for proposal (RFP) for its power needs in the early years of this decade. It received responses in July 1998 offering to provide MPS power needs through a variety of options from several different entities. As part of this evaluation by MPS, it also examined the option of building and owning itself a 500 megawatt combined cycle unit with a projected in-service date in 2001.

In August 1998, through MPS analysis as well as the independent analysis of Burns & McDonnell, an engineering consulting firm, MPS determined that the least cost option for it was to build the 500 megawatt combined cycle unit.

Q. Did MPS pursue building the 500 megawatt combined cycle unit?

A. Yes. However, GMO (Aquila), at some point, assigned the construction project away from GMO (Aquila's) regulated MPS operations and transferred it to Aquila Power Corporation, GMO (Aquila's) non-regulated operations later known as Aquila Merchant.

Initially, the regulated operations of MPS pursued building the Aries Combined Cycle Unit as an unregulated EWG. The studies and analyses performed by personnel of the regulated operations ultimately led to the conclusion that the 500 megawatt combined cycle unit was the least cost option to meet the capacity needs of MPS starting in 2001. This was confirmed by the independent engineering firm, Burns & McDonnell in an August 1998 report to the Company.

In an August 24, 1998 study entitled "UtiliCorp United Inc. Missouri Public Service 1998-2003 Preliminary Energy Supply Plan," the Company independently determined that the construction of a 500 megawatt combined cycle unit was the least cost plan for MPS. Under the Executive Summary Section 1, "Conclusions," the following appears:

> **Conclusions**
>
> **Based on the 1998-2003 supply-side analysis, the least cost plan for MPS consists of executing short term purchase contacts to meet MPS capacity needs through the year 2000, and the construction of a gas-fired 500 MW combined cycle unit to meet all of MPS' capacity needs in 2001-2003 time frame and a majority of its needs thereafter.**
>
> **The above supply provides the least cost means to meet the MPS capacity and energy needs even though MPS' has a low annual load factor of <50% and an abundant supply of low-cost energy supplied by its existing resource base which is 64% coal-fired base load generating capacity.**
>
> **The ability of combined cycle units to complete in the regional energy market place enables these resources to provide sufficient revenue to offset their higher capital cost.**
>
> **1.5 Recommended Action Plan**
>
> **As a result of the analysis outlined in this report, it is recommended that UCU [(Aquila/UtiliCorp)]:**
>
> **Negotiate extension of the existing lease agreements on the Greenwood combustion turbines.**

Secure short term capacity to meet MPS' capacity needs thru 2000.

Pursue the construction of a 500 MW combined cycle unit proposed with an in service date of June 1, 2001.

[Source: Data Request No. 607 in ER-2004-0034—1998-2003 Preliminary Energy Supply Plan]

Q. Did GMO then operating as UtiliCorp, ever examine the option of MPS building and owning the Aries Combined Cycle Unit as part of its regulated operations?

A. No. At no time during the 1998 time period, did GMO (Aquila) or MPS ever consider this as an option. Staff is aware of numerous examples, in the last two MPS electric cases (Case Nos. ER-2001-672 and ER-2004-0034) where GMO (Aquila) readily admitted that at no time did it consider allowing the regulated operations of MPS to own or control generating units as regulated plant. While the EWG option was pursued by MPS regulated operations, the combined cycle unit was never planned to be part of the traditional regulated operations of MPS, and GMO (Aquila) never planned for the unit to be included in rate base.

Q. Does Staff consider this a fatal flaw in the Company's analysis to meet the capacity needs of its Missouri retail electric customers?

A. Yes. To not have even considered the option of building regulated generating assets held by MPS to meet the capacity needs of GMO (Aquila's) Missouri regulated operations is a failure on the GMO (Aquila's) part and constitutes imprudence. This decision by GMO (Aquila) resulted in GMO (Aquila's) regulated Missouri operations being at the mercy of purchased power agreements priced at market-based rates through May 31, 2005, when the Aries agreement terminated. GMO (Aquila) continued to be subjected to market-based rates for the power used by its Missouri regulated operations right up to acquisition by GPE in July 2008.

Q. What was the effect of GMO (Aquila's) strategy to not build regulated generating assets until recently?

A. GMO (Aquila) subjected its MPS and now, L&P operations, to purchased power agreements priced at market-based rates. The market rates for purchased power during the period of most of this decade has increased significantly over what they were in the late 1990s when GMO (Aquila) entered into the Aries purchased power agreement.

Q. What is the basis for the Staff's belief that GMO (Aquila) did not consider building regulated generation to meet its capacity needs in Missouri and, instead, committed to building unregulated generation?

A. GMO (Aquila) freely admitted that it never considered building regulated generating facilities to meet the capacity needs of its regulated utility operations in the state of Missouri. Mr. DeBacker (page 9, line 9 DeBacker rebuttal) and Mr. Stamm (page 12, line 18 Stamm rebuttal) both admit in their rebuttal testimonies filed in Case No. ER-2004-0034, that this option was never considered by GMO (Aquila's) regulated operations. In Case No. ER-2001-672, GMO (Aquila) provided response to Data Request No. 365 where it stated that "the Company believes that the current regulatory climate does not warrant the business risks associated with constructing and owning ratebased generating plants."

Also, in an interview with Mr. DeBacker and Mr. Robert Holzwarth (Vice-President and General Manager of UtiliCorp Power Services (UPS)) held on October 28, 2003, Mr. DeBacker stated that it was Aquila's corporate policy not to consider building regulated generating assets. Mr. DeBacker indicated in the interview that "MPS did not intend to build and include in rate base generating units to supply its power needs. Thus, Aquila (UtiliCorp) through its regulated

MPS division never considered building generating capacity as a regulated unit" [Data Request No. 548 in Case No. ER-2004-0034).

Q. Did Aquila provide a reason for why it never entertained the option of building a regulated power plant?

A. Yes. During the aforementioned interview with Mr. DeBacker and Mr. Holzwarth, they indicated there was a corporate policy at GMO (Aquila) that no new generation would be built as a regulated unit subject to rate basing. The following accurately characterizes the information provided at the October 28, 2003 interviews on this topic of corporate policy:

> **The philosophy of "buy/not build" in regard to power supply, taken in response to perceived electric industry uncertainty, was an Aquila (UtiliCorp) corporate strategy in place by 1998; it wasn't just Mr. DeBacker's and Mr. Holzwarth's belief at that time. The Aquila (UtiliCorp) philosophy was consistent with MPS' strategy in 1998. MPS took the position to depend on purchased power for short-term power needs, no construction of regulated power plants. The Aquila (UtiliCorp) divisions in Colorado and Kansas followed this same approach. Bob Green, Jim Miller and Harvey Padawer communicated the "buy/not build" strategy for the regulated entities. This strategy is not set down in writing, to DeBacker's and Holzwarth's knowledge, but was no secret within Aquila. Mr. Holzwarth was present at one meeting where Bob Green expressed the "buy/not build" philosophy. Among senior officers still with Aquila, Rick Green, currently Chairman, President and Chief Executive Officer could address this philosophy if necessary.**
>
> **Both Mr. DeBacker and Mr. Holzwarth indicated that UtiliCorp was concerned about the future of retail competition / retail access and was concerned about the "stranded costs" relating to loss of customers to completion from "customer choice". The Company wanted to "stay short in the market" (stay in market 3 to 5 years only). The decision to "stay short" in the market was made by UtiliCorp in 1996/1997 time frame. Mr. Holzwarth said, "what would happen if you build big units (generating**

> **units) and half your customers went away?" When asked if either of them knew of any system (electric system) where half the customers "went away" neither Mr. DeBacker nor Mr. Holzwarth knew where this had occurred. Mr. Holzwarth cited the competition that was occurring in other states such as Pennsylvania, New Jersey, New York and Illinois.**
>
> **[October 28, 2003 interview with DeBacker and Holzwarth, Data Request No. 548 in Case No. ER-2004-0034]**

The least cost option that MPS developed for meeting the capacity needs of (Aquila's) Missouri regulated utility operations was to build the Combined Cycle Unit as an EWG as part of the regulated operations of the Company (Mr. DeBacker's rebuttal testimony in Case No. ER-2004-0034).

Mr. DeBacker indicated in the fall of 1998, the Company decided to create another unregulated corporate entity under its Aquila Merchant subsidiary to build and own generating assets such as the Aries Combined Cycle Unit (page 19 of DeBacker Rebuttal Testimony filed in Case No. ER-2004-0034). While MPS, a regulated division of GMO (Aquila), had performed the work required to determine the size and scope of the generating asset needed for the capacity needs of GMO (Aquila's) Missouri regulated operations, (October 28, 2003 DeBacker interview, Data Request No. 548, in ER-2004-0034), (Aquila's) upper management transferred that function to the non-regulated operations of Aquila Merchant.

It is interesting to note that the regulated operations of the Company continued to examine the EWG option as late as October 1998. A presentation made on October 8, 1998, entitled "Financial Analysis of Supply Options" and another presentation made on October 28, 1998, entitled "Updated Analysis of Supply Options." both of presentations were made by GMO (Aquila's) regulated operations presented the EWG option of building and owning the

500 megawatt combined cycle unit. As late as the end of October 1998, the regulated operations of UtiliCorp were still pursuing the generation option that would later become the Aries Project.

However, the option of the regulated operations building the 500 megawatt combined cycle unit was rejected by Aquila's upper management. Other than the statements made in the interview with Mr. DeBacker and Mr. Holzwarth that the Company believed it would be difficult to have the regulated operations build and own the Aries Combined Cycle Unit, the Staff has not seen nor been provided any documentation that would identify the specific reasons why this option was not agreed to by the Company's upper management. In the October 28, 2003, interview, Mr. Holzwarth indicated that upper management decided that it would be too difficult to have the regulated operations create the non-regulated function of building and owning the Aries Unit. The following interview notes, reviewed by the interviewees, accurately describe this:

> **In 1998, the only economic analysis performed to assess MPS' power options for the first years of the next century were for a three-to-five year period only. Building plants for MPS' rate base was not considered as an option, but Holzwarth's group did consider building a generating plant as an unregulated Exempt Wholesale Generator (EWG) within MPS. Building a unit as part of an EWG was viewed as superior to including a regulated unit in rate base because there was less risk to Aquila of stranded costs if retail access was allowed in Missouri. Plus, the EWG proposal allowed MPS to better control costs and to "control its own destiny" in regard to power supply, and also allowed MPS the opportunity to profit on a non-regulated basis in the wholesale marketplace through the sale of energy as off-system sales. The analysis performed by UtiliCorp for the EWG never assumed MPS to be a customer of the MPS EWG unit beyond the original five-year power supply proposal in the RFP. Mr. Holzwarth stated that the MPS EWG option was presented at a meeting attended by Bob Green, then UtiliCorp President, and Harvey Padawer (maybe Jim Miller as well). The MPS EWG option was rejected because of questions raised at the**

> **meeting the risk of a massive EWG operating failure when taking into consideration MPS' relatively small size; how to obtain generating economies of scale, since a separate organization within MPS would have to be responsible for the EWG unit; MPS' lack of familiarity with the combined-cycle technology; and regulatory scrutiny of possible cross-subsidies between MPS' regulated and non-regulated sides. Mr. Holzwarth said some of the questions posed at this meeting where he recommended that MPS (through UPS) build non-regulated EWG generating unit were: How can MPS operating people manage the EWG also? What would be the "risk" to cash? Where would you get economies of scale from a regulated operation running a non-regulated EWG operation? Mr. Holzwarth stated he did not have answers to these questions.**
>
> **[Source: October 28, 2003 interview with Mr. DeBacker and Mr. Holzwarth]**

The decision was made to obtain power from other sources. Mr. DeBacker and Mr. Holzwarth indicated that they were not aware of any records documenting the reasons for the MPS EWG option rejection by Aquila's upper management.

> **Mr. Holzwarth stated that the ultimate decision would have been made by Bob Green and/or Harvey Padawer; however, the consensus opinion of senior management was that a regulated power plant with its potential stranded cost issues was not desirable. Mr. Holzwarth indicated he did not make the decision; he only made the presentation recommending that his group UtiliCorp Power Supply build a generating unit as a non-regulated EWG.**
>
> **[Source: October 28, 2003 interview with Mr. DeBacker and Mr. Holzwarth,]**

Q. Did Staff ask who made the decision not to build regulated generating units?

A. Yes. Staff submitted a data request asking the following:

> **1. Why was the decision made by Aquila (formerly UtiliCorp United) not to build and operate Aries Combined Cycle Unit as a "regulated" power plant to be included in rate base? Include in your response all reasons and rationales why this decision was made.**

Response: Uncertainty surrounding the deregulation of the electric power industry and the possibility of incurring unrecoverable "stranded costs". Avoiding long term power supply commitments was viewed as a means to effectively mitigate potential "stranded costs" arising from potential retail generation choice.

2. Provide all supporting documentation relating to and relied on upon in making this decision, including but not limited to reports, analyses, studies, etc.

Response: Compliance with MPS Joint Agreement with MPSC [Missouri Public Service Commission] and Office of Pubic Counsel—approved by PSC in Case No. EO-98-316 on 6/25/98.

Secondary Concern

1. Inexperience in operating large F-frame combustion turbine generating units and uncertainty surrounding the actual maintenance costs of these machines.

[Data Request No. 302 in Case No. ER-2004-0034]

This project then became assigned to Aquila Merchant and the Aries project was developed as part of the merchant energy partners segment of that operation.

Q. Who at GMO (Aquila) made the decision to not to build regulated generating assets to meet MPS capacity requirements?

A. As indicated above cited in the October 28, 2003 interview, Mr. Holzwarth said Mr. Bob Green and Harvey Padawer made the decision not to build regulated generating assets. In response to the Data Request No. 302 in Case No. ER-2004-0034 the Company identified the following decision makers on that issue:

Bob Green-- Chief Operating Officer supervised by Rick Green

Jim Miller – Leader Business Segment UED (UtiliCorp Energy Delivery)

Harvey Padewar—Leader Business Segment UEG (UtiliCorp Energy Group)

In the October 28, 2003, Staff interview with Mr. DeBacker and Mr. Holzwarth, when asked about who made the decision to build Aries as a nonregulated plant, according to Staff notes of the interview reviewed by the interviewees, they stated:

> **Were Bob Green, Harvey Padawer and Jim Miller involved in meetings dealing with Aquila Merchant matters? DeBacker and Holzwarth said Padawer would have been; he was head of Aquila Merchant at the time and reported to Mr. [Bob] Green. They supposed Bob Green would have met with Aquila Merchant people; Bob Green as President of Aquila (UtiliCorp) was over Aquila Merchant as well as the regulated utility operations. Mr. DeBacker and Mr. Holzwarth were not sure about Mr. Miller, Senior Vice President of UtiliCorp Energy Delivery (UED) which was responsible for the transmission and distributions system (pipes and wires) of the regulated utilities.**
>
> **[Data Request No. 548 in Case No. ER-2004-0034]**

Q. Who was Mr. Bob Green?

A. Until October 2002, Mr. Green was the President and Chief Executive Officer of GMO (Aquila) and President of Aquila Merchant.

Q. Who is Mr. Harvey Padawer?

A. Mr. Padawer was head of Aquila Merchant at the time of the decision to build the Aries Project. Aquila Merchant was engaged in the marketing of natural gas and electricity to industrial and wholesale customers. During the time Mr. Padewar was in charge, Aquila Merchant was starting its merchant energy function, of which the Aries unit was intended to play a major part of that strategy.

Q. Who is Jim Miller?

A. Mr. Miller was head of GMO (Aquila's) regulated operations, known as the "pipes and wires" part of the business. He was in charge of UtiliCorp Energy Delivery, or the regulated transmission and distribution operations of the Company.

Q. Have other utilities followed a different course than Aquila to meet their power capacity needs since the mid to late 1990s?

A. Yes. As noted earlier, utilities such as Empire , KCPL and AmerenUE have all embarked on building generating assets, and owning and controlling those generating assets as part of their regulated operations. Staff supports this and has encouraged this practice by utilities through the IRP process, as well as various applications that have appeared before the Commission concerning restructuring and reorganizations of the various corporate entities.

In KCPL's application to restructure its corporate operations in Case No. EM-2001-464, a critical element of Staff's concern and, ultimately, the resolution of that application filed with the Commission, was the commitment for KCPL to continue to build and keep regulated generating assets as part of its regulated operations.

Q. Would there ever be an advantage to a utility not building its own generating units and relying on purchased power market pricing to serve its regulated customers?

A. Yes, to the extent that a company had both regulated and non-regulated entities and the non-regulated entity owned and operated generating facilities that could sell power to the regulated affiliated company. If the utility believed that the market pricing of power costs was going to rise over time, the utility could build and own non-regulated generating facilities and enter into purchased power agreements with regulated affiliated companies. There would be a direct benefit to the company if the costs could be passed on to regulated customers

through rates. The increased power costs would benefit the owner of the generation because they could raise the costs to the regulated entity through market-based rate contracts. This arrangement would benefit the parent company that owned both the regulated utility and the non-regulated generating affiliate because earnings to the parent company would increase. In essence, the forecast of increasing power costs justified the building of the generating facility by the non-regulated entity with the expectation that the increased pricing would be reflected in newly negotiated power contracts. This, of course, assumes that the Company is successful in passing the increase in costs to its regulated customers through purchased power agreements similar to the one that Aquila entered into with the Aries partners.

Q. Why is this important since GMO (Aquila) no longer has an affiliate company that is attempting to sell power to GMO (Aquila's) regulated companies?

A. While GMO (Aquila) does not have an affiliate selling it power, the aftermath of the Aries decision still affected the Company's decision making right up to 2008. Aries originally was owned by GMO (Aquila) exclusively until it sold 50% of its ownership interests to Calpine. In 2004, GMO (Aquila) sold its entire interest in Aries to Calpine. Not only did GMO (Aquila) lose a 585 megawatt combined cycle unit - a subject this Commission is still having to deal with in finding a replacement to this power - but it lost very valuable land rights. This facility was sized for additional generating units. In fact, the three turbines installed at South Harper were originally planned to be installed at Aries as Aries II. When GMO (Aquila) gave up its ownership interest in Aries, and going back even further when it decided to get a partner for Aries, has caused the Company great hardship in its capacity planning and meeting the energy needs of its customers.

As the Company has struggled with zoning and permitting issues at South Harper it is easy to understand the value of existing sites that already had zoning approvals.

Q. Did Cass County provide zoning and permitting authority to GMO (Aquila) to build Aries?

A. Yes. Aquila sought all the necessary zoning and permitting requirements in building Aries.

Q. How has the Company's inattention to the Missouri-regulated operations of the Company impacted those operations and its customers?

A. In every instance, the Staff knows about with regard to other Missouri utilities, the companies have pursued meeting their customers' long-term capacity needs through building and owning generating assets unless utilities obtain very favorable base load generation pricing such as the two NPPD capacity agreements like GMO (Aquila) has. Empire has a very favorable long-term base load agreement with a Kansas utility Westar Energy. But other utilities for the most part want to own and control their generating assets. GMO (Aquila) stands alone when they make year after year decisions to pursue purchase power agreements with market-based rates. The decision by GMO (Aquila's) management to embark on a non-regulated path to meet its capacity needs put the regulated operations "behind the curve" in the sense of ownership of power production facilities. Empire as a company, and Empire's customers, have enjoyed the benefits of the State Line Combined Cycle since it went into production of electricity in June 2001. Empire and its customers will have the benefit of that unit for many years to come. GMO (Aquila's) customers, however, will not have the same opportunities for those benefits and will pay more in the long-run by not building generation since 1983 with the exception of the South Harper facility.

Q. Will prudent ownership of generating assets produce the lowest overall cost?

A. Very likely. GMO (Aquila) produced a study for the January 2004 IRP analysis that concluded that building and owning five combustion turbines was the least cost scenario for replacing the Aries capacity agreement in June 2005.

CONCLUSIONS FOR CAPACITY PLANNING AND PEAKING TURBINES

Q. What are the conclusions that Staff has regarding the Company's building generation?

A. GMO (Aquila) made the decision to not build regulated generating assets as a corporate policy. During the IRP process, GMO (Aquila) never looked at building regulated assets in a meaningful way except South Harper. GMO (Aquila) continued the no build option right to current with the exception of its base load coal-fired Iatan 2 commitment. GMO (Aquila) did not submit any RFPs to turbine manufacturers to get turbine pricing so that it could do complete and thorough studies concerning the build vs. purchasing options until late 2005, well after the time for decision concerning the replacement of the Aries Agreement. GMO (Aquila) did not present any plans to build capacity for, even though it indicated that its system needs capacity during the period from 2005 to current. Staff has proposed what it believes is a conservative amount for the two additional turbines identified as Turbines 4 and 5. The turbines prices declined during the period that Aquila would have needed to place orders for the units with an in-service date by June 2005. There would have been economies of scale to building the five combustion turbines instead of three. GMO (Aquila's) IRP Plan presented in January 2004 concluded that the least costs plan for the 2005 replacement of the

Aries Agreement was the building of five combustion turbines instead of three combustion turbines.

Q. Does conclude your surrebuttal testimony?

A. Yes.

BEFORE THE PUBLIC SERVICE COMMISSION

OF THE STATE OF MISSOURI

In the Matter of the Application of KCP&L Greater Missouri Operations Company for Approval to Make Certain Changes in its Charges for Electric Service.	)))))	Case No. ER-2009-0090

AFFIDAVIT OF CARY G. FEATHERSTONE

STATE OF MISSOURI	)	
	)	ss.
COUNTY OF COLE	)	

Cary G. Featherstone, of lawful age, on his oath states: that he has participated in the preparation of the foregoing Surrebuttal Testimony in question and answer form, consisting of 12 pages to be presented in the above case; that the answers in the foregoing Surrebuttal Testimony were given by him; that he has knowledge of the matters set forth in such answers; and that such matters are true and correct to the best of his knowledge and belief.

Cary G. Featherstone

Subscribed and sworn to before me this 9th day of April, 2009.

NIKKI SENN
Notary Public - Notary Seal
State of Missouri
Commissioned for Osage County
My Commission Expires: October 01, 2011
Commission Number: 07287016

Notary Public

SCHEDULES 1 - 3

HAVE BEEN DEEMED

HIGHLY CONFIDENTIAL

IN THEIR ENTIRETY

AQUILA, INC.
AQUILA NETWORKS-MPS-INVESTOR (ELECTRIC)
CASE NO. EO-2005-0156
MISSOURI PUBLIC SERVICE COMMISSION
DATA REQUEST NO. MPSC-5

DATE OF REQUEST:	December 10, 2004
DATE RECEIVED:	December 10, 2004
DATE DUE:	December 29, 2004
REQUESTOR:	Phil Williams
BRIEF DISCRIPTION:	Please provide all appraisals of the plant site and the value of the combustion turbines.

QUESTION:

Please provide all workpapers that support the appraisals of the plant site and the value of the combustion turbines to be sold and then be leased back for the proposed plant at Peculiar, Missouri.

RESPONSE: See files on attached CD

ATTACHMENT: CD with 17 files

ANSWERED BY: Robert Brune

_____
SIGNATURE OF RESPONDENT

DATE: _____

SCHEDULE 4-1

Aquila CT Appraisal - Pricing Summary

Client No. 010144
W/O No. 02-01362-01000
Date 11/19/2004

	Original Cost	Replacement Cost	Aquila offer to sell to KCPL	Rolls Royce offer to sell to Aquila	SWPC offer to sell grey unit to Aquila	Penn Energy internet offer 1	Penn Energy internet offer 2	Utility Warehouse internet offer
CT								
qty	3	1	3	2	1	1	1	1
Cost	$76,137,869	$24,500,000	$69,000,000	$43,000,000	$19,000,000	$26,000,000	$33,000,000	$15,000,000
Adjustments								
Option Payment	($3,712,500)							
CO No. 1 (Exhaust Stacks)		($1,849,200)		($1,849,200)	($1,849,200)	($1,849,200)	($1,849,200)	
CO No. 1 (Other)								
Warranty	($2,240,000)	($2,240,000)	($2,240,000)		($2,240,000)			
Guarantees								
Prod Mods	($300,000)							
Rehabilitation	($600,000)							
TFA				$2,350,000	$2,350,000			$2,350,000
Mult Unit Purchase		($1,000,000)						
Change to DLN				$5,000,000	$5,000,000			$5,000,000
Transportation				$1,200,000	$1,200,000	$1,200,000	$1,200,000	$1,200,000
Internal Labor	($39,399)							
Total Adjustments	($6,891,899)	($5,089,200)	($2,240,000)	$6,700,800	$4,460,800	($649,200)	($649,200)	$8,550,000
CT Subtotal*	**$69,245,970**	**$68,410,800**	**$66,760,000**	**$71,200,800**	**$61,460,800**	**$77,350,800**	**$98,350,800**	**$53,550,000**
* adjusted for three units								
Transformers & Breakers								
Transformers								
qty	6	6		6	6	6	6	6
Cost	$1,686,150	$1,686,150		$1,686,150	$1,686,150	$1,686,150	$1,686,150	$1,686,150
Adjustments								
Storage	($15,500)	($15,500)		($15,500)	($15,500)	($15,500)	($15,500)	($15,500)
Retesting	($28,305)	($28,305)		($28,305)	($28,305)	($28,305)	($28,305)	($28,305)
Additional Retainage	($1,045)	($1,045)		($1,045)	($1,045)	($1,045)	($1,045)	($1,045)
Transformer Subtotal	$1,641,300	$1,641,300		$1,641,300	$1,641,300	$1,641,300	$1,641,300	$1,641,300
Breakers								
qty	3	3		3	3	3	3	3
Cost	$765,570	$765,570		$765,570	$765,570	$765,570	$765,570	$765,570
Adjustments								
Bond	($7,500)	($7,500)		($7,500)	($7,500)	($7,500)	($7,500)	($7,500)
Storage	($13,320)	($13,320)		($13,320)	($13,320)	($13,320)	($13,320)	($13,320)
Breakers Subtotal	$744,750	$744,750		$744,750	$744,750	$744,750	$744,750	$744,750
Procurement								
Cost	$126,644	$126,644		$126,644	$126,644	$126,644	$126,644	$126,644
Adjustment								
B&M Services	($126,644)	($126,644)		($126,644)	($126,644)	($126,644)	($126,644)	($126,644)
Procurement Subtotal	$0	$0		$0	$0	$0	$0	$0
$2,576,364								
Transformers & Breakers Subtotal	**$2,386,050**	**$2,386,050**		**$2,386,050**	**$2,386,050**	**$2,386,050**	**$2,386,050**	**$2,386,050**
Total	**$71,632,020**	**$70,796,850**	**$66,760,000**	**$73,586,850**	**$63,846,850**	**$79,736,850**	**$100,736,850**	**$55,936,050**

SCHEDULE 4-2

SCHEDULE 4-2

SCHEDULES 5 - 7

HAVE BEEN DEEMED

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