EXHIBIT

~~GMO~~-261

Exhibit No.:
Issues: Rate of Return, Capital Structure
Witness: David Murray
Sponsoring Party: MoPSC Staff
Type of Exhibit: True-Up Rebuttal Testimony
File No.: ER-2010-0356
Date Testimony Prepared: February 28, 2011

MISSOURI PUBLIC SERVICE COMMISSION

UTILITY SERVICES DIVISION

TRUE-UP REBUTTAL TESTIMONY

OF

DAVID MURRAY

Great Plains Energy, Incorporated
KCP&L GREATER MISSOURI OPERATIONS COMPANY

FILE NO. ER-2010-0356

Jefferson City, Missouri
February, 2011

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Staff Exhibit No. ~~GMO261~~
Date 3/3/11 Reporter SmB
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Q. Please state your name.

A. My name is David Murray.

Q. Are you the same David Murray who earlier filed rebuttal, surrebuttal, and true-up direct testimony in this proceeding on behalf of the Staff of the Missouri Public Service Commission ("Staff") and, in addition, was responsible for the section of the Staff's Cost of Service Report ("COS Report") filed November 17, 2010, concerning cost of capital issues?

A. Yes, I am.

Q. What is the purpose of your True-up Rebuttal Testimony?

A. The purpose of my True-up Rebuttal Testimony is to respond to KCP&L Greater Missouri Operations Company ("GMO" or "Company") witness Michael W. Cline's True-up Direct Testimony. Mr. Cline provided testimony regarding GMO's updated capital structure and embedded costs of capital through the period ending December 31, 2010.

CAPITAL STRUCTURE

Q. Do you have any concerns regarding Mr. Cline's proposed capital structure as of the true-up period in this case?

A. Only as it relates to his inclusion of Kansas City Power & Light Company ("KCPL") preferred stock in the capital structure. Otherwise, the balances of the other capital components appear to be accurate.

EMBEDDED COST OF LONG-TERM DEBT

Q. Do you have any concerns about the ramifications of Mr. Cline's updated GMO embedded cost of debt as of December 31, 2010?

A. Yes. Mr. Cline assigns $250 million of 3-year, 2.75 percent Great Plains Energy, Incorporated ("GPE") debt ("2.75 percent debt") to GMO for purposes of his embedded cost of debt recommendation. GPE issued this debt on August 13, 2010. This assignment causes GMO's embedded cost of debt to drop to 6.42 percent from GMO's previous assigned overall embedded cost of debt of 7.07 percent as of June 30, 2010. This compares to the 6.82 percent cost of debt Mr. Cline recommends for KCPL in his True-up Direct Testimony in File No. ER-2010-0355 and KCPL's assigned embedded cost of debt of 6.82 percent as of June 30, 2010.

Q. If GMO is financially weaker than KCPL, why is GMO's embedded cost of debt now lower than KCPL's embedded cost of debt?

A. Internal financing decisions and credit support from GPE. As Staff explained in its True-Up Direct Testimony in the KCPL case, File No. ER-2010-0356, both KCPL and GMO had short-term debt balances of $297 million and $267 million as of June 30, 2010, respectively. As of September 30, 2010, KCPL and GMO had short-term debt balances of $209 million and $0, respectively. Consequently, it appears that most of the $250 million of debt proceeds were used to eliminate the balance on GMO's credit facility.

Q. Considering GMO's weak stand-alone financial condition, how was GMO able to procure debt proceeds at a coupon rate of 2.75 percent?

A. GPE's credit support, which has been rated investment grade by the major rating agencies before and after it acquired the GMO properties. GMO's credit metrics on a stand-alone basis are more consistent with below investment-grade credit ratings. In fact, GPE guarantees all of GMO's debt, which directly supports the creditworthiness of GMO's debt that would otherwise be considered by the rating agencies as "junk" quality if GMO were a stand-alone company.

Q. How has GPE been able to maintain its investment-grade credit rating?

A. The credit support it receives from its KCPL operations as these are the only other assets that GPE owns.

Q. Does the need for GMO to have support for its debt come at a cost to KCPL?

A. Yes. If GPE is issuing debt on behalf of GMO, then this holding company debt would reduce KCPL's total credit capacity and increase the cost of the remaining credit capacity.

Q. Should this cost be borne by KCPL ratepayers?

A. No.

Q. Do you believe KCPL's ratepayers will be negatively impacted if the Missouri Public Service Commission ("Commission") accepts Mr. Cline's proposal to assign the entire amount of the 2.75 percent debt to GMO?

A. Yes. The acceptance of this proposal would allow GPE's internal financing decisions to not only negatively impact KCPL ratepayers in terms of a higher cost of debt compared to GMO in this case, but possibly in future rate cases if this assignment process is construed to be endorsed by the Commission in this case.

Q. Did KCPL's ratepayers pay higher rates than traditional cost of service ratemaking during the period of KCPL's Experimental Alternative Regulatory Plan ("Regulatory Plan")?

A. Yes.

Q. Why was this allowed?

A. Signatory parties to KCPL's Experimental Plan, which was approved by the Commission in Case No. EO-2005-0329, had the understanding that this consideration would be used to target benchmark credit metrics consistent with a 'BBB+' credit rating.

Q. Did the higher rates paid by KCPL's ratepayers also support GPE's credit rating?

A. Yes.

Q. How can the Commission ensure fair and equitable treatment to KCPL ratepayers for the higher rates they paid to allow GPE the ability issue lower cost of debt on behalf of GMO?

A. Some of the 2.75 percent debt should be assigned to KCPL for purposes of its cost of debt. This would have the effect of lowering KCPL's embedded cost of debt and increasing GMO's embedded cost of debt.

Q. If it appears that most of the funds from the 2.75 percent debt were used to pay down GMO's credit facility, then why is this appropriate?

A. GPE could have just as easily used proceeds from the 2.75 percent debt to reduce KCPL's short-term debt balances in order to create more short-term debt capacity for KCPL. If GPE had made this decision, then KCPL would have had the entire 2.75 percent debt issuance assigned to KCPL's embedded cost of debt and GMO would have continued to have a higher embedded cost of debt.

Q. Does GPE have a financial incentive to consistently carry short-term debt at KCPL rather than at GMO?

A. Yes. KCPL has access to the commercial paper markets, whereas GMO does not. The cost of commercial paper is usually lower than that of direct borrowings on credit facilities. For example, as of June 30, 2010, KCPL had a weighted-average interest rate on its commercial paper outstanding of 0.44 percent, whereas GMO had a weighted-average interest rate of 1.625 percent on its direct borrowings from its credit facility.

Q. Why is Staff concerned about GPE's decision to refinance the higher cost short-term debt if this a financially responsible decision for GPE?

A. Because it demonstrates that GPE's focus is on maximization of wealth of GPE's shareholders. It does not appear that financial decisions are being made for the best interests of the individual subsidiaries. I believe it is important for Staff to ensure that the setting of a fair and reasonable rate of return, including the cost of debt in this situation, should not be driven by processes and procedures of a debt assignment process, but based on the fairness of the end-result. In this situation, the end-result, i.e., using KCPL's credit capacity and creditworthiness to allow GPE to lower the embedded cost debt for only GMO, is not fair.

Q. How can the Commission ensure fairness in this situation?

A. As discussed previously, assign at least part of the 2.75 percent debt to KCPL.

Q. Why didn't you recommend doing this in your True-up Direct Testimony in the KCPL case?

A. Because I did not recommend inclusion of the 2.75 percent debt for either KCPL or GMO. I recommended using The Empire District Electric Company's ("Empire") embedded cost of debt for GMO. However, if the Commission were to adopt GPE's decision to assign the entire amount of the 2.75 percent debt to GMO's cost of debt, then this may be construed as the Commission's preferred approach. In Staff's opinion, this would be inherently unfair and detrimental to KCPL's customers.

Q. If the Commission accepts the inclusion of the 2.75 percent debt for purposes of the true-up, how can this cost be assigned to both KCPL and GMO?

A. Simply use a GPE consolidated cost of debt for both GMO's and KCPL's rate of return ("ROR").

Q. Did you not indicate in your True-Up Direct Testimony in the KCPL rate case that if GPE's credit metrics were more consistent with that of KCPL's credit metrics that GPE's 3-year bonds could have been issued at an even lower coupon rate than 2.75 percent?

A. Yes. During the period of the Regulatory Plan, KCPL was allowed to charge higher rates in order to directly target credit metrics consistent with benchmarks for a 'BBB+' credit rating. Because KCPL has been affiliated with companies with either a weaker business or financial risk profile over the period of the Regulatory Plan, it is difficult to know with certainty whether KCPL and/or GPE would have been rated at the targeted level. However, if KCPL would have been able to achieve a 'BBB+' credit rating, then GPE's unsecured debt rating would have likely been one notch lower at 'BBB' due to structural subordination. According to utility bond yield data from Bloomberg that GMO provided in response to Staff Data Request No. 379, 3-year utility bonds rated 'BBB' and 'BBB+' had yields that averaged 2.21 percent and 1.87 percent, respectively, during the month of August 2010 (the month in which GPE issued the 2.75 percent debt). Staff will use a 2-percent coupon for purposes of the embedded cost of debt it recommends the Commission use if it were to include the 2.75 percent debt in the embedded cost of debt for purposes of the true-up in this case.

Q. Does Staff's consolidated embedded cost of debt estimate assume the Commission adopts the Company's proposed GMO cost of debt in the general rate case?

A. Yes. Staff is providing this estimate to the Commission based on this premise. If the Commission were to adopt the Staff's proposal to use Empire's cost of debt as a proxy for GMO's cost of debt, then this issue is moot.

Q. Is it possible that Staff may recommend an adjusted consolidated embedded cost of debt for KCPL and GMO, which includes the debt in question, in future rate cases?

A. Yes.

Q. Assuming the Commission adopts GMO's proposed cost of debt in the general rate case, what embedded cost of debt do you recommend the Commission adopt for GMO for purposes of the true-up?

A. 6.598 percent, which assumes that the Commission accepts Staff's adjustment to the coupon rate of the 2.75 percent debt.

Q. If you used a 6.598 percent embedded cost of debt for the Empire proxy cost of debt you used in your True-Up Direct Testimony, what is the indicated ROR range?

A. 7.75 percent to 8.21 percent, midpoint of 7.98 percent (see Schedule 1).

Q. What would the consolidated embedded cost of debt be if the Commission were to accept the actual coupon rate of 2.75 percent?

A. 6.659 percent.

Q. If you used a 6.659 percent embedded cost of debt for the Empire proxy cost of debt you used in your True-Up Direct Testimony, what is the indicated ROR range?

A. 7.78 percent to 8.24 percent, midpoint of 8.01 percent (see Schedule 2).

Q. Does this conclude your True-up Rebuttal 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	))))	File No. ER-2010-0356

AFFIDAVIT OF DAVID MURRAY

STATE OF MISSOURI)
) ss.
COUNTY OF COLE)

David Murray, of lawful age, on his oath states: that he has participated in the preparation of the foregoing True-Up Rebuttal Testimony in question and answer form, consisting of 8 pages to be presented in the above case; that the answers in the foregoing True-Up Rebuttal 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.

David Murray
David Murray

Subscribed and sworn to before me this 28th day of February, 2011.

D. SUZIE MANKIN
Notary Public - Notary Seal
State of Missouri
Commissioned for Cole County
My Commission Expires: December 08, 2012
Commission Number: 08412071

D Suzie Mankin
Notary Public

KCPL Greater Missouri Operations Company
File No. ER-2010-0356

Weighted Cost of Capital as of December 31, 2010 for KCP&L Greater Missouri Operations Company

Capital Component	Percentage of Capital	Embedded Cost		Weighted Cost of Capital Using Common Equity Return of: 8.50%	9.00%	9.50%
Common Stock Equity	46.58%	-----		3.96%	4.19%	4.43%
Preferred Stock	0.00%	0.000%		0.00%	0.00%	0.00%
Long-Term Debt	48.87%	6.598%	1,2	3.22%	3.22%	3.22%
Equity Units	4.55%	12.351%	1,3	0.56%	0.56%	0.56%
Total	**100.00%**			**7.75%**	**7.98%**	**8.21%**

Notes:

1. Data for Embedded Cost of Long-Term Debt, Embedded Cost of Preferred Stock and Embedded Cost of Equity Units Provided in Response to Staff Data Request No. 0159T in File No. ER-2010-0356.
2. Embedded cost of long-term debt is based on GPE's consolidated cost of debt using adjusted coupon of 2.00% on the 3-year debt.
3. Adjusted consistent with adjustment made in the general rate case for the period ending June 30, 2010.

SCHEDULE 1

Weighted Cost of Capital as of December 31, 2010 for KCP&L Greater Missouri Operations Company

Capital Component	Percentage of Capital	Embedded Cost		Weighted Cost of Capital Using Common Equity Return of: 8.50%	9.00%	9.50%
Common Stock Equity	46.58%	---		3.96%	4.19%	4.43%
Preferred Stock	0.00%	0.000%		0.00%	0.00%	0.00%
Long-Term Debt	48.87%	6.659%	1,2	3.25%	3.25%	3.25%
Equity Units	4.55%	12.351%	1,3	0.56%	0.56%	0.56%
Total	**100.00%**			**7.78%**	**8.01%**	**8.24%**

Notes:

1. Data for Embedded Cost of Long-Term Debt, Embedded Cost of Preferred Stock and Embedded Cost of Equity Units Provided in Response to Staff Data Request No. 0159T in File No. ER-2010-0356.
2. Embedded cost of long-term debt is based on GPE's consolidated cost of debt using actual coupon of 2.75% on the 3-year debt.
3. Adjusted consistent with adjustment made in the general rate case for the period ending June 30, 2010.

SCHEDULE 2