PUBLIC VERSION

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-2010-0356

Initial Post-Hearing Brief of Issues Related Only to KCP&L Greater Missouri Operations Company

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Pursuant to the Commission's March 7, 2011 Order, KCP&L Greater Missouri Operations Company ("GMO" or "Company") submits its initial brief on GMO only issues.

1. Capacity Planning

a. Introduction

The disagreement between GMO and Staff concerning GMO's capacity planning boils down to two decisions made by the Company:

(1) The 2004 decision to pursue the construction of three 105 MW combustion turbines (CTs) at South Harper and pursue a 200 MW system-participation based purchased power agreement (PPA); and

(2) The decision to add the Crossroads generating facility to the MPS generation fleet.

The prudence of each of these independent decisions needs to be considered separately. As the Company's case demonstrates, both decisions were prudent.

In response to meeting GMO's future capacity needs, the Company decided after considerable analysis in 2004 to pursue the construction of three 105 MW CTs at South Harper and pursue a long-term 200 MW system-participation based PPA. This decision resulted in the construction of three combustion turbines at South Harper and a capacity agreement for some

very favorably priced base load energy, both occurring in 2005. This decision was consistent with the opinion expressed by Staff in 2004 that an optimal long-term mix of generation must include base load generation. However, Staff contends that GMO should have pursued construction of five CTs in 2005 instead of the plan GMO pursued. Staff has maintained that position since the first rate case after the three CTs were built. In this case, Staff has imputed to the Company the cost of two non-existent CTs, hence Phantom Turbines. Staff's conclusion is based on the same analysis as that developed and used by the Company in deciding to pursue the three CT/system-participation PPA. There have been no questions raised concerning the validity of the analysis, just the conclusion.

Three years later with the South Harper site and long-term PPA in place, the company had a decision to make regarding adding additional resources to the GMO supply portfolio. In response to this need, GMO issued an RFP as well as developed self-supply options for consideration. A thorough analysis of the available options demonstrated that the addition of the 300 MW Crossroads Energy Center was the lowest cost option for meeting GMO's requirements.

The Company maintains that diversifying its fuel mix, as directed by Staff, was both reasonable and prudent, therefore Staff's attempts to disallow recovery of its used and useful, in-service generating resources should be rejected.

b. Staff's Phantom Turbines

As stated above, Staff contends that GMO should have built five 105 MW CTs at South Harper by the summer of 2005. Because GMO built three 105 MW CTs instead of the five as preferred by Staff, Staff has imputed to GMO the cost of two additional 105 MW CTs. Exhibit GMO-11, Crawford Rebuttal at 1. Staff argues: "Aquila should have built five 105 MW CTs at the South Harper site, rather than the three it actually built, given the information that was

available to GMO (then known as Aquila, Inc.) through its resource planning process at the time GMO was deciding how it was replacing the power it was getting from the Aries plant (now the Dogwood plant) through a capacity contract." Hearing Exhibit GMO-210, Staff Cost of Service Report at 91. Staff has maintained this position for the past three GMO rate cases, arguing in the 2007 case, "Aquila identified five (5) 105 MW CTs as the least cost way to meet its resource needs at the time. Even so, Aquila chose to build only three (3) 105 MW CTs at its South Harper site and entered into short-term purchased power agreements for its remaining capacity needs." Hearing Exhibit GMO-11, Crawford Rebuttal at 2, citing Mantle Direct, Case No. ER-2007-0004, at 8. Staff argues in the current case that its adjustments "reflect the continuation of Staff's position that GMO should have prudently addressed its capacity needs for MPS to replace the Aires PPA when it expired on May 31, 2005." Hearing Exhibit GMO-210, Staff Cost of Service Report at 103. Staff has conducted no analysis to support its position that GMO should have built five CTs, instead relying on an analysis prepared by GMO that compared the 20-year net present value of revenue requirements (NPVRR) for 12 different resource plans. "[T]he lowest cost plan under base natural gas price assumptions was to build five 105-MW CTs." Of particular note, "[t]he second lowest cost plan was to build three 105-MW CTs and enter into a 200-MW system participation-based purchased power contract (which included base load capacity)." Hearing Exhibit GMO-11, Crawford Rebuttal at 2-3.

GMO elected not to build five CTs, in favor of three CTs and a purchased power agreement that included base load capacity, in order to diversify its resource portfolio additions. "GMO concluded that it would be prudent to spread the execution and operating risks from the resource additions between building CTs and adding a PPA that contained some level of base load capacity." Id. at 4. Not only would this reduce the Company's dependence on any one fuel

source, but would also ensure that the additional capacity would include both base load and peaking capacity. Id.

As referenced above, Staff recognized in 2004 - one year prior to constructing the three CTs and entering into a purchased power agreement with base load capacity - that "Aquila needed to be looking at base-load generation because Aquila should not become overly dependent upon short-term PPAs." Id., citing Schedule LLM-1, p. 2. In addition, Staff stated in this case, "if MPS were a standalone utility, it would be very beneficial for MPS to diversity its generation portfolio with base load capacity." Hearing Exhibit GMO-210, Staff Cost of Service Report at 99. The Commission, too, has recognized GMO's need for base load generation. In his dissenting opinion in Case No. ER-2005-0436, Commissioner Gaw stated, "the MPS territory relies too heavily on gas generation." Hearing Exhibit GMO-11, Crawford Rebuttal at 4. Further, in his concurring opinion, Commissioner Clayton stated, "[l]astly, this case represents another example of why utilities should not be reliant on natural gas for power generation for significant amounts of its portfolio." Id. Staff has apparently chosen to ignore both its own directives to the Company to add base load generation to its resource portfolio, as well as statements by the Commission, in its rate case adjustments. Given Staff's testimony, GMO is confused by the inconsistent - and punitive - adjustments Staff persists in making to GMO's recovery of prudently incurred generation resources.

In making its adjustment, Staff appears to rely solely on the 2004 five CT plan which had the lowest NPVRR under the base natural gas price assumption. However, it did not have the lowest NPVRR under the high natural gas price assumption. The plan selected by the Company performed better than the five CT plan under the high natural gas assumption. Id. at 5. This analysis demonstrates the risks that the Company, the Commission and even Staff recognized in relying solely on natural gas generation when considering resource additions. Further, because

of these risks (e.g., fluctuations in natural gas prices), it is important to analyze the performance of plans under several scenarios. In other words, it may be prudent to select a preferred plan that does not result in the lowest NPVRR when another plan reduces the risks associated with future uncertainties. Id. In this case, "[t]he Company's preferred plan reduced the risks associated with natural gas prices." Id. Not only did it reduce the risks associated with natural gas uncertainty, it did so at a reasonable cost.

The difference between Staff's preferred five CT plan and the Company's three CT/system-participation PPA plan is minimal. See Hearing Exhibit GMO-217, Featherstone Surrebuttal, Schedule 119. When this difference in plan costs was presented to Staff witness Lena Mantle, she stated that she did not believe the cost difference between the Company's preferred plan and Staff's five CT option over 20 years was significant (Hearing Tr. at 4090), and further that she did not find the Company's decision based on this difference to be imprudent. Id. at 4091. GMO whole-heartily agrees with this assessment. It is important to note that this is the very analysis that Staff points to as demonstrating why the Company's preferred plan to pursue the three CT/system-participation PPA was imprudent. If this difference in plan costs is neither significant nor imprudent, Staff has presented no evidence to support its disallowance of GMO's supply resources.

Analyzing the risks associated with future uncertainties in an effort to minimize the cost of a preferred plan is not only prudent, but standard practice at the Commission. The Commission's rules on electric utility planning specifically require this risk analysis in order to ensure that the preferred plan is in the public interest. See 4 CSR 240-22. The Company performed this analysis and selected the second lowest cost plan as its preferred plan in order to limit gas price exposure. Hearing Exhibit GMO-11, Crawford Rebuttal at 6.

Ultimately, the Company did not implement precisely its preferred plan. Based on the 2004 analysis, the preferred plan called for three 105 MW CTs and a 200 MW system participation contract. The three CTs were completed in the summer of 2005, but the Company was unable to complete the system participation contract. Instead, the Company entered into a 9-year 75 MW base load contract with the Nebraska Public Power District (NPPD). This revision was presented to Staff in July 2004. Id. In later cases, Staff opined that "Aquila had found a very good 75 MW contract with Nebraska Public Power District." Id. at 6-7, citing Mantle Direct, Case No. ER-2005-0436, at 6. Staff further indicated that the contract with NPPD was a "very favorable" base load contract. Id. at 6, citing Featherstone Surrebuttal, Case No. ER-2007-0004, at 89. In the current case, Staff repeated that "Aquila had found a very good 75 MW PPA with Nebraska Public Power District." Id. at 7, citing Schedule LMM-1, p. 3.

At best, Staff's adjustments are inconsistent with its prior statements and opinions on the Company's preferred resource plan. At worst, Staff's adjustments are insupportably punitive. Not only is it impossible to meet GMO customers' real capacity needs with non-existent turbines, the 210 MW imputed is insufficient to meet the current needs. In previous rate cases Staff recommended imputing a 100 MW PPA in addition to the 210 MW Phantom Turbines. In this case they did not do so, leaving the Company short of capacity even after assuming one could get real capacity from the Phantom Turbines. The Commission should therefore reject Staff's Phantom Turbine adjustments and allow GMO to fully recover the costs associated with its preferred resource plan, the construction of three 105 MW CTs and a purchased power agreement that includes base load generation.

c. Staff's Phantom Turbines Adjustment Is Legally Flawed

Staff's case is contrary to the prohibition set forth in § 393.135, RSMo 2000 which precludes a party from including in the rates of an electrical corporation any charge for property

before it is "fully operational and used in service." Staff's two CTs are entirely imaginary and, therefore, are not, and cannot be, used in providing service to GMO's customers. The Staff adjustment is unlawful on its face and should be rejected. Beyond that, Staff's recommendation, if adopted, would exceed the Commission's statutory authority in that it is an attempt to manage the Company's operations.

The Commission is an administrative body of limited powers, created by state law. Accordingly, it has only such powers as are expressly conferred upon it by the statutes and reasonably incidental thereto. State ex rel. and to the Use of Kansas City Power and Light Co. v. Buzard, 315 Mo. 763, 168 S.W.2d 1044, 1046 (1943); State ex rel. City of West Plains v. Public Service Commission, 310 S.W.2d 925, 928 (Mo. banc 1958). Although the Act is remedial in nature, and should be construed liberally, neither convenience, expediency nor necessity are proper matters for consideration in the determination of whether or not an act of the Commission is authorized by statute. State ex rel. Kansas City v. Public Service Commission, 301 Mo. 179, 257 S.W. 462 (Mo. banc 1923); State ex rel. Utility Consumers Counsel of Missouri Inc. v. Public Service Commission, 585 S.W.2d 41, 49 (Mo. banc 1979).

So long as the Company conducts its power resource planning in a manner consistent with its obligations under the Commission's IRP rules, the consequent power procurement activities by the Company is not a matter that can be directed or determined by the Commission or by its Staff. The law on this topic is clear and unambiguous. The Commission's authority to regulate certain aspects of a public utility's operations and practices does not include the right to dictate the manner in which the company conducts its business. State ex rel. City of St. Joseph v. Public Service Commission, 30 S.W.2d 8 (Mo. banc 1930).

Similarly, in State ex rel. Harline v. Public Service Commission, 343 S.W.2d 177 (Mo. App. 1960), the Court observed that the Commission's powers are "purely regulatory." Id. at

181. Further, the Public Service Commission Act provides "regulation which seeks to correct the abuse of any property right of a public utility, not to direct its use." Id. The Court of Appeals elaborated on this important principle:

> The utility's ownership of its business and property includes the right to control and management, subject, necessarily to state regulation through the Public Service Commission. The powers of regulation delegated to the Commission are comprehensive and extend to every conceivable source of corporate malfeasance. Those powers do not, however, clothe the Commission with the general power of management incident to ownership. The utility retains the lawful right to manage its affairs and conduct its business as it may chose, as long as it performs its legal duty, complies with lawful regulation and does no harm to the public welfare.

Thus, the commission may regulate GMO's operations, but it has no authority to manage the Company's business or to substitute its business judgment for that of GMO, so long as GMO is meeting its public service obligation to provide safe and adequate service to its patrons. In this regard, Staff fails to allege that the Company has not determined its resource needs through valid resource planning practices or that its implementation of those plans has resulted in inadequate service to its customers. Absent any such plausible showing, Staff's attempt to place two make-believe CTs in GMO's portfolio of owned power generation must be rejected.

d. Crossroads Energy Center

i. Staff's Disallowance of Crossroads is Unsupported

In addition to imputing the cost of two phantom CTs to GMO, Staff has removed the Crossroads Energy Center (Crossroads) from its cost of service. Staff presents four reasons for excluding the capacity and associated costs of Crossroads:

- Affiliate transaction concerns;
- Opinion that the delivered price of natural gas to Crossroads has been historically higher than the price of gas to South Harper;
- The cost of transmission to move energy from Crossroads to GMO's service territory; and

- The ability of GMO to provide proper management oversight to the Crossroads plant.

Hearing Exhibit GMO-210, Staff Cost of Service Report at 92.

GMO disagrees with Staff's rationale. First, Crossroads was initially held by Aquila's unregulated merchant subsidiary. The plant was transferred by the unregulated subsidiary to the parent, Aquila, Inc. Aquila, Inc. later transferred Crossroads to the regulated utility, Missouri Public Service. Great Plains Energy assumed the contract as part of its acquisition of Aquila, Inc.

Missouri's affiliate transaction rules are intended to prevent regulated utilities from subsidizing their non-regulated operations. In addition, these rules also address the financial and evidentiary standards applicable to Missouri utilities that participate in transactions with an affiliated entity. Hearing Exhibit GMO-11, Crawford Rebuttal at 11; and see 4 CSR 240-20.015. The financial standard states, in relevant part:

> A regulated electrical corporation shall not provide a financial advantage to an affiliated entity. For purposes of this rule, a regulated electrical corporation shall be deemed to provide a financial advantage if -
>
> 1 It compensates an affiliated entity for goods or services above the lesser of -
>
> A. The fair market price; or
>
> B. The fully distributed cost to the regulated electrical corporation to provide the goods or services for itself; ...

4 CSR 240-20.015(2)(A).

The evidentiary standard states, in relevant part:

> (A) When a regulated electrical corporation purchases information, assets, goods or services from an affiliated entity, the regulated electrical corporation shall either obtain competitive bids for such information, assets, goods or services or demonstrate why competitive bids were neither necessary nor appropriate.
>
> (B) In transactions that either involve the purchase or receipt of information, assets, goods or services by a regulated electrical corporation from an affiliated entity, the regulated electrical corporation shall document both the fair market price of such information, assets, goods and services and

> the FDC [fully distributed cost] to the regulated electrical corporation to produce the information, assets, goods or services for itself.

4 CSR 240-20.015(3).

The regulated utility determines fair market value by obtaining competitive bids for the service or asset it seeks to acquire for itself. "The purpose of seeking competitive bids is to identify other supply options available to the regulated utility, not other customers or buyers for the non-regulated affiliate." Hearing Exhibit GMO-11, Crawford Rebuttal at 12. Hence, the non-regulated affiliate is not required to obtain a bid to sell itself or its services to others in order to determinate fair market value. GMO, in fact, issued a request for proposals (RFP) in March 2007 seeking long-term capacity and energy. Id. This resulted in two non-affiliated entities offering long-term capacity and energy options. "Crossroads was determined to be the lowest cost option. Therefore, the cost of Crossroads is not greater than the fair market value of other available options." Id. GMO also received an offer from a non-affiliated entity "for four GE 7EA CTs, the same number of GE 7EA CTs as installed at Crossroads. Id. The installed cost from the non-affiliated offer was higher than the Crossroads offer, and didn't include the cost for land, water, transmission interconnection, step-up transformer, among other items. The lower Crossroads offer included all costs. Id. at 13. GMO also considered and documented a self-build option. Crossroads again was determined to be a lower cost option. Id.

To the extent that the transfer of Crossroads to the regulated utility falls under the affiliate transaction rules, GMO has fully complied with the rules. "GMO obtained competitive bids to determine the fair market value of long-term capacity and energy. GMO documented the cost to provide long-term capacity and energy for itself. GMO's analysis shows that the cost of acquiring Crossroads is less than the fair market value of available alternatives and less than the cost of the regulated utility providing the capacity and energy for itself." Id. at 14.

Next, Staff suggests that the delivered price of natural gas to Crossroads has been historically higher than the price of gas to South Harper. In determining the price of natural gas, there are several components to consider: the wellhead price of natural gas, reservation charges, commodity charges, fuel retention, FERC's Annual Charge Adjustment, balancing fees and other tariff charges. Hearing Exhibit GMO-8, Blunk Rebuttal at 2. According to KCPL's witness Wm. Edward Blunk, in the first 10 months of 2010, the average commodity cost for natural gas shipped to Crossroads was less than gas shipped on Panhandle Eastern Pipeline to South Harper. Moreover, the average delivered cost of natural gas to Crossroads was about half the average delivered cost of natural gas to South Harper. Id. The Company acknowledges that the price of natural gas available to Crossroads is not always less than the price of natural gas available to South Harper. Id. at 3. However, the viable shipping options to move more gas to South Harper, as would be required by Staff's adjustment to impute two additional CTs at South Harper to the Company, require paying pipeline capacity or reservation charges. Southern Star Central Gas Pipeline, Inc. and Panhandle Eastern Pipeline, the two natural gas pipelines serving South Harper, are both fully subscribed. As a result, transportation is not always available. Id. at 3-4 and 6.

In addition, one of the benefits of Crossroads over the two Phantom Turbines at South Harper "is that natural gas shipped to Crossroads typically comes from a different supply region than natural gas shipped to South Harper. This allows the Company to take advantage of short-term pricing disparities." Id. at 4-5. With Crossroads in the portfolio, however, "the Company can choose to generate electricity from the region with the lower priced natural gas." Id. at 5.

Further, during those times when the Company needs generation from both Crossroads and the existing South Harper units in order to serve the Company's summer peak load, Crossroads offers an important benefit to the Company that the Phantom Turbines do not -- that

is, supply diversity. Id. at 5-6. When weather patterns affect GMO's service territory or the west central part of Missouri, those same weather patterns are also affecting the other electric utilities in the region, requiring all the utilities to utilize their peaking resources. Id. at 6. Without firm transportation, there is no assurance that natural gas could be transported to South Harper. Id. Because Southern Star and Panhandle are both fully subscribed, it is unlikely either of those carriers could provide transport service to South Harper. In contrast, "[i]t is unlikely that the weather pattern driving the peak load in west central Missouri will simultaneously be pushing load in Mississippi to the same magnitude." Id. In other words, while the other electric utilities in our region are competing for the limited pipeline resources, "Crossroads is on a different pipeline and sufficiently removed from the local weather pattern that it would not be affected." Id. Crossroads offers GMO the ability to choose between pricing regions, adds supply and transportation diversity and increases system reliability. Id. The Phantom Turbines at South Harper do not provide these same benefits.

Third, Staff argues that the cost of transmission to move energy from Crossroads in Mississippi to GMO's service territory justifies, in part, removing Crossroads from GMO's cost of service. It is true that GMO has transmission costs to move energy from Crossroads to its service territory. GMO receives firm transmission service from Entergy until the power interconnects with the Southwest Power Pool, Inc. (SPP), at which point transmission is taken under SPP's network transmission service tariff. However, the Company has demonstrated that the cost of transmission is offset by the lower gas reservation costs. In other words, it costs as much to bring natural gas to GMO's service territory to run a local plant as it does to acquire firm transmission to get the power from the Crossroads plant to GMO's service territory.

In addition, the cost of transmission service for Crossroads was included in the 2007 analysis that demonstrated that Crossroads was the lowest cost solution in meeting the additional

GMO resource needs. Hearing Exhibit GMO-11, Crawford Rebuttal at 10. Singling out one cost component, like transmission costs, that is higher than what it may be with other resource alternatives should not be grounds for disallowing the entire facility particularly when the all-in costs of the facility result in minimizing the NPVRR over 20 years when compared to the available alternatives.

Finally, Staff expressed concern with GMO's ability to provide appropriate management oversight of a plant located in Mississippi. As explained by Company witness Marvin L. Rollison, the plant is operated by the Clarksdale Public Utilities Commission. According to the Generation Agreement between the Clarksdale Public Utilities Commission and GMO, GMO receives "the output of the plant in exchange for payments that cover fixed and variable costs to produce the electrical output, as well as to maintain and operate the facility." Hearing Exhibit GMO-31, Rollison Rebuttal at 2-3. The agreement also provides that "GMO has the right to review and approve the annual Operating Plan which constitutes a comprehensive and detailed plan for operating the facility for [the] coming two-year period." Id. at 3. In turn, the Operating Plan "covers projected routine maintenance, projected heat rate, and staffing plans to execute the Plan." Id. In addition, GMO has the authority to review and approve the annual plant budget, among other rights and authorities related to the plant Id. Mr. Rollison further testified that he, along with other Company personnel, have made several trips to the plant. Id. at 4. There are also financial incentives tied to the Clarksdale Public Utility Commission's efficient operation of the plant. Id. at 3-4. To suggest that GMO should not be allowed to recover the costs associated with Crossroads because of its location ignores the rights and responsibilities the Company has and exercises over the plant, and further ignores the reality of the Company's other remotely located generation facilities. For example, the Company does not provide employees or provide on-site management oversight to either the Jeffrey Energy Center or the Wolf Creek Nuclear

Power Plant, yet Staff has not made a similar disallowance of the Company's interests in those facilities. The Crossroads facility is no different.

Staff has offered no proof that any inappropriate management oversight of Crossroads has occurred. It would be improper to disallow costs due to speculation that oversight will be a problem. Should such inappropriate management occur in the future, the Commission could certainly take this into consideration in any future rate case, just as it could with any GMO resource.

Further, despite Staff's direct testimony which indicates its concern with long-distance management oversight of Crossroads as a reason for disallowing ratemaking treatment of the plant, Staff's rebuttal testimony states the opposite. Staff's revised opinion states that: "Staff does not oppose including the book value of the Crossroads in MPS's rate base because Crossroads is far away in Mississippi and has more capacity than MPS needs in the short term." Hearing Exhibit GMO-232, Mantle Rebuttal at 2. Based on the testimony of Company witness Rollison and Staff's revised position, the Commission should reject the location of Crossroads as a justification to disallow recovery of the plant in the Company's cost of service.

ii. The Addition of Crossroads was Prudent

In March 2007, GMO issued a Request for Proposals (RFP) for supply resources. According to GMO's witness Burton L. Crawford: "The RFP was very broad, seeking renewable resources, conventional peaking, base load, and intermediate capacity and energy. In addition the RFP requested a variety of proposal types including equity participation, EPC (engineering, procurement and construction), generating equipment only and PPAs (purchased power agreements)." Hearing Exhibit GMO-11, Crawford Rebuttal at 8. GMO received several responses to its RFP "representing a range of options from non-affiliated entities as well as self-build options." Id. After reviewing and analyzing the responses, GMO conducted a 20-year

analysis to determine a preferred plan. The analysis showed that Crossroads would result in the lowest 20-year NPVRR. The Company presented its analysis and preferred plan determination to Staff in October 2007. Id.

In addition to the results of the analysis presented to Staff in October 2007, GMO performed an additional analysis on capacity requirements options in compliance with the Non-Unanimous Stipulation and Agreement in Case No. ER-2009-0090. This analysis evaluated several different capacity options over 42 scenarios with varied assumptions such as natural gas prices and retail load forecast. This analysis was completed in April 2010. Consistent with its earlier 2007 evaluation, the inclusion of Crossroads resulted in the lowest cost to retail customers over a 20-year period. Id. at 9.

iii. The Company's Valuation of Crossroads is Appropriate

GMO has included the cost of Crossroads at the net book value of $104 million. Hearing Exhibit GMO-12, Crawford Surrebuttal at 3. "The net book value reflects the value of the plant as it was offered in response to GMO's 2007 request for proposals (RFP) for capacity to meet GMO's resource needs at that time." Id. at 1-2. As stated above, GMO's evaluation of the 2007 RFP responses demonstrated that Crossroads was the most cost effective alternative for meeting GMO's resource needs at that time. Id. at 2. Although Staff's primary recommendation is that Crossroads should be disallowed in its entirety (Hearing Exhibit GMO-210, Staff Cost of Service Report at 92), it argues alternatively that if the Commission decides to allow Crossroads in GMO's cost of service, then the value of Crossroads for ratemaking purposes is $51.6 million. Hearing Exhibit GMO-216, Featherstone Rebuttal at 3; see also Exhibit GMO-25, Ives Surrebuttal at 12-13. Staff's valuation is based on a preliminary S-4 filing the Company made with the Security and Exchange Commission (SEC) which recognized a conservative, "worst case scenario" estimate of dismantling and selling the plant. To explain, during the Aquila

acquisition process, Great Plains Energy was required to produce a fair value disclosure as part of its S-4 filing at the SEC. In preparing the May 2007 S-4 disclosure statement, Great Plains Energy, among other things, performed a high level analysis of different alternatives for the Crossroads facility. In order to reflect the uncertainty regarding whether any of the alternatives was achievable, the Company opted to disclose the value of the plant based on dismantling it and selling the turbines and other equipment for salvage. According to that S-4 filing, the salvage value of Crossroads is $51.6 million. Hearing Exhibit GMO-12, Crawford Surrebuttal at 3; see also Hearing Exhibit GMO-25, Ives Surrebuttal at 12-15, Hearing Exhibit GMO-47 at p. 2 and Hearing Tr. at 4103.

Staff's valuation ignores the reality that the plant was not dismantled and sold, but rather is fully operational. It further ignores the valuation of Crossroads at the time of acquisition, which was performed by an independent, third party valuation. This valuation appeared in GMO's September 2008 rate case in Case No. ER-2009-0090. Hearing Exhibit GMO-25, Ives Surrebuttal at 12-14. According to the alternative that the plant remained operational and GMO was able to obtain transmission from Crossroads to GMO, the value of the plant was $94.75 million, assuming that $20 million in transmission upgrades would be required. GMO was ultimately able to obtain transmission service with only a minimal transmission investment of $145,000, bringing the estimated value of Crossroads to $114.60 million. Hearing Exhibit GMO-12, Crawford Surrebuttal at 3. This value is even more than the $104 million GMO has requested for ratemaking treatment in this case and highlights how unrealistic Staff's proposed salvage value of $51.6 million is.

iv. Dogwood Energy, LLC

Dogwood Energy, LLC (Dogwood) presented testimony in this case which described its interests as both a retail power customer of GMO and a wholesale power supplier to GMO.

Hearing Exhibit GMO-3601, Janssen Rebuttal at 3. As a customer, Dogwood supported Staff's disallowance of Crossroads and imputation of two Phantom Turbines in order "to protect GMO's retail customers, including Dogwood, against exorbitant rates." Id. at 4. However, as demonstrated above, both GMO's preferred resource plan to build three CTs and enter into a PPA, instead of building five CTs, and its decision to include the capacity of Crossroads in its generation mix, result in the lowest cost to retail customers. With regard to its interest as a wholesale supplier to GMO, Dogwood suggests that the Commission discourage GMO from using the Crossroads facility and instead replace it with a local unit -- such as Dogwood's combined cycle facility. Id. Dogwood's interest is admittedly self serving, stating "Dogwood wants to assure it has a fair and competitive opportunity to supply power to GMO." Id. at 6. Dogwood further stated that it has extended power supply and plant purchase offers to GMO in recent years. Id. at 12. Dogwood indicated it has responded to all of GMO's long-term and short-term RFPs issued during the past few years of which it was aware, and also provided GMO unsolicited offers between the issuance of its RFPs. Id. at 14. As stated above, in response to its issued RFPs, GMO has always selected the least cost resource option. Clearly, Dogwood's responses were not the most economical option for the Company or it would have selected Dogwood. At a minimum, Dogwood believes its proposals were more cost-effective than Crossroads. Id. at 15. Dogwood asks the Commission to consider offers made by Dogwood, in addition to Staff's Phantom Turbines, when setting GMO's rates. Id. at 20. The Commission should reject Dogwood's proposal because the Company has demonstrated that Crossroads is, in fact, a more cost-effective resource option than Dogwood and, as a result, results in a lower cost for ratepayers.

Dogwood presented testimony to address the Company's assertion that Crossroads provided the lowest 20-year NPVRR, including the cost of transmission, from other alternatives

reviewed and analyzed. <u>See</u> Hearing Exhibit GMO-3603, Rose Surrebuttal. Dogwood's witness Judah Rose believes that the Dogwood option is actually lower cost than Crossroads; however, Dogwood's analysis contains several errors which, when corrected, demonstrate that its 20-year NPVRR is much higher than Crossroads. <u>See</u> Hearing Exhibit GMO-3603, Rose Surrebuttal at 60.

The most egregious error in Dogwood's analysis is the input used for Crossroads' transmission cost is significantly overstated. <u>Id.</u> GMO takes firm point-to-point transmission service from Entergy at a rate of $1,380 per MW/month. <u>See</u> Hearing Exhibit GMO-49. This is less than one-third the amount Dogwood used in its analysis. Correcting for this error alone causes Crossroads to have a lower net cost than Dogwood.

Another error in Dogwood's analysis is that the capacity factor used for Dogwood is overstated. Hearing Exhibit GMO-3603, Rose Surrebuttal at 60. The capacity factor assumed in Dogwood's analysis fails to reflect the plant's actual historical generation. If the number of MWh generated in Dogwood's model were lower to reflect a more typical level of actual generation, the analysis would show a lower net energy margin. Hearing Tr. at 4130-31 Using an accurate capacity factor alone makes Crossroads a better proposition. Using an accurate capacity factor *and* using the correct transmission charge makes Crossroads the clearly superior option.

e. Conclusion

Adoption of the Staff's Crossroads and phantom turbine adjustments by the Commission would lead to the unjust result of GMO being short nearly 100 MW in its capacity needs since the Staff's 210 MW imputation from the non-existent turbines does not cover the 300 MW currently being provided by Crossroads. More importantly, since the phantom turbines do not exist, it is impossible for GMO to meet its real capacity needs under Staff's position and

therefore will have to purchase capacity in the open market rather than relying on its own production assets at Crossroads.

Should the Commission reject the phantom turbine adjustment, but accept Staff's lower capital price for Crossroads, then the Company will not recover its capital investment at Crossroads nor its operating costs. Because Staff does not include operating costs for Crossroads, adoption of Staff's alternative position would result in GMO not being able to recover the operating costs, including operating and maintenance production and transmission costs. This result is not appropriate regulation as it does not reflect GMO's cost to serve its customers.

The Company's 2004 decision to pursue the construction of three 105 MW CTs at South Harper and pursue a 200 MW system-participation based purchased power agreement (PPA), and the Company's decision to add the Crossroads generating facility to the MPS generation fleet were both prudent. The Commission should therefore reject Staff's Phantom Turbine adjustments and allow GMO to fully recover the costs associated with its preferred resource plan, the construction of three 105 MW CTs and a purchased power agreement that includes base load generation and should reject Staff's adjustment to disallow the recovery of Crossroads in the Company's cost of service.

2. <u>Jeffrey Energy Center FGD Rebuild Project</u>

a. Should the Jeffrey Rate Base Additions be included in rate base in this proceeding?

Based upon the competent and substantial evidence in the record, the Commission should include the prudently incurred Jeffrey Energy Center (JEC) Additions in rate base in this proceeding. JEC environmental equipment includes cold-side electrostatic precipitators for particulate removal and limestone-based wet flue gas

desulfurization (FGD) systems or scrubbers. (Hearing Exhibit GMO-210 (NP), p. 42, COS Report)

Westar Energy is the primary owner and constructor of this project. GMO owns 8% of the plant. Monthly status reports and cost reports provided by Westar were reviewed and monitored by GMO for prudence and reasonableness. The Staff Engineers, Mr. David Elliott and Mr. Shawn Lange, found there were no engineering issues that needed to be addressed. (Hearing Exhibit GMO-210 (NP), pp. 59-60, COS Report; GMO-21 (NP), pp. 1-6, Hedrick Rebuttal) In addition, the Kansas Corporation Commission found that the Jeffrey Rate Base Additions should be included in rates without any disallowances. (Hearing Exhibit GMO-21 (NP), p. 6, Hedrick Rebuttal) The Missouri Staff engineers, Mr. David Elliott and Shawn Lange, have evaluated all three units and found no engineering concerns with any of the Jeffrey Energy Center FGD project change orders. Staff concluded that the scrubbers have successfully met all of the in-service criteria and are "fully operational and used for service." (Hearing Exhibit GMO-210 (NP), pp. 62-63, COS Report)

b. Should Staff's proposed disallowance related to the Jeffrey Energy Center FGD Rebuild Project be adopted?

No. In this proceeding, Staff witness Keith Majors is sponsoring a proposed adjustment to the Jeffrey Energy Center FGD Rebuild Project. Mr. Majors is proposing an adjustment of **[redacted]** (Hearing Exhibit GMO-210 (NP), pp. 42-

47, COS Report; GMO-21 (HC), p. 3, Hedrick Rebuttal). For the reasons stated herein, this Staff adjustment should be rejected.

As an 8% minority owner of the Jeffrey Energy Center, GMO's involvement in the project was limited. (Hearing Tr. p. 4267) Monthly FGD status and cost reports were provided by Westar and reviewed and monitored by GMO for prudence and reasonableness. Several construction site visits were also conducted during the project by GMO staff. (Hearing Exhibit GMO-21 (HC), p. 3, Hedrick Rebuttal)

Mr. Terry S. Hedrick, KCP&L's Director of Supply Engineering, explained the reasons why Westar and GMO did not require ** **
as follows:

** **

**

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** (Hearing Exhibit GMO-21 (HC), pp. 3-4, Hedrick Rebuttal; Hearing Tr. p. 4268)

Mr. Leonard R. Ruzicka, an expert in construction law, was retained by GMO to review documents and interview individuals as necessary to determine the appropriateness of the awarding of a contract to PMSI for the general construction work on the rebuild of the scrubber systems on the three units of the Jeffrey Energy Center coal-fired generating station. Mr. Ruzicka is a partner in the law firm of Stinson Morrison Hecker LLP, and previously had 20 years experience as a Senior Vice President and General Counsel for Fru-Con Corporation, a large international company engaged in construction, engineering and real estate development. (Hearing Exhibit GMO-36 (NP), p. 1, Ruzicka Rebuttal; Hearing Tr. p. 4271-72, 4341) He was also retained to review the testimony of Mr. Keith Majors and give his assessment of the opinions expressed by Mr. Majors in that testimony.

After an extensive review of the relevant documents and interviews with individuals involved on the Jeffrey project, Mr. Ruzicka concluded that Westar/GMO had **

** (Hearing Exhibit GMO-36 (NP), p. 2-5, Ruzicka Rebuttal). Mr. Ruzicka explained the reasons why it was appropriate to award the contract as Westar/GMO did:

> When the spread between low and second low bidder is substantial, it would be appropriate and reasonable to consider waiving the bonding requirement but only after conducting the same type of due diligence that is conducted by the sureties. **
>
> ** In accepting that recommendation, Westar/GMO acted appropriately and reasonably and

consistent with what a prudent owner would do in similar circumstances. (Id. at 3)

In addition, Mr. Ruzicka explained that ** [redacted] ** As a result, there was no basis for a claim of liquidated damages under a performance bond. (Hearing Tr. pp. 4349-52; See also Hearing Tr. p. 4266; 4356-57) Typically, a principal will be found in default under a construction contract for failure to timely perform; or for performing the work defectively and refusing to cure the defect; or a combination of both. ** [redacted] ** (Hearing Exhibit GMO-36 (NP), p. 6, Ruzicka Rebuttal).

Assuming Staff's theory regarding the performance bond was correct (which it is not), the competent and substantial evidence also shows that Staff's calculation of the proposed adjustment is incorrect. ** [redacted] ** (Hearing Exhibit GMO-36 (NP), p. 5, Ruzicka Rebuttal)

For the foregoing reasons, the Commission should reject the Staff's adjustment related to the Jeffrey Energy Center FGD Rebuild. The competent and substantial evidence in the whole

record supports a finding that Westar/GMO acted prudently in managing the Jeffrey Energy Center Project, including awarding the contract to PMSI as discussed herein.

3. Allocation of Iatan 2 Between L&P and MPS Service Areas

From GMO's perspective, the Iatan 2 Allocation issue is more akin to a rate design issue since it determines the relative amount of the rate increase that will be received by both the MPS and the L&P service areas rather than the overall revenue requirement impact of Iatan 2. (Tr. p. 3821)

GMO has allocated 41 MW of Iatan 2 to the L&P service area, and the remaining 112 MW to the MPS service area, based upon the balancing of the respective baseload capacity needs of L&P and the MPS service areas, as well as the resulting rate impacts upon its customers. (Hearing Exhibits GMO-33, pp. 10-12, Rush Rebuttal; GMO-5, pp. 7-10, Blanc Rebuttal; GMO-11, pp. 14-16, Crawford Rebuttal)

GMO's proposed allocation of Iatan 2 results in 60% of L&P's 2011 projected peak demand to be met with base load capacity, and 61% of MPS's projected peak to be met with base load capacity—So both service areas would have nearly identical percentages of base capacity, using the GMO's allocation proposal for Iatan 2. (Hearing Exhibit GMO-11, pp. 15-16, Crawford Rebuttal) GMO's proposal also recognizes that Iatan 2 is jointly dispatched between both the L&P and MPS service areas, based upon economics rather than previous corporate history. (Tr. p. 3847)

The Staff is recommending that a substantially larger share of Iatan 2 be allocated to the L&P service area than what GMO has requested. Staff proposes to allocate 100 MW of Iatan 2 to the L&P rate jurisdiction which is about 240% more of Iatan 2 than what GMO proposed. (Tr. p. 3853) Only 53 MWs would be allocated to MPS under Staff's proposal.

Staff's proposal would have 73% of L&P's peak met with base load capacity, and only 57% of MPS's peak would be met with base load capacity. (Tr. p. 3844) (Hearing Exhibit GMO-11, pp. 15-16, Crawford Rebuttal) Staff witness Mantle testified that Staff primarily based its position on St. Joseph Light & Power Company's resources when it merged with Aquila more than a decade ago. (Tr. p. 3845) (Hearing Exhibit, GMO-210 (NP), p. 94, COS Report) Staff looked back about a decade to make its determination about the proper allocation of Iatan 2 for the future.

As GMO witness Rush explained, Staff's proposed allocation will have adverse effects on the customers in the L&P service area, GMO's Fuel Adjustment Clause mechanism, and the appropriate amount of fuel and purchased power assigned to each of the service areas since base load, intermediate and peaking capacity have relatively different fuel costs. (Tr. pp. 3820-21)

Staff's proposal would increase the revenue requirement for the L&P service area by approximately $20 million above GMO's request. (Tr. p. 3820) GMO requested a $22 million total increase for the L&P area after considering all of the other cost drivers in the case. By adding another $20 Million to account for Staff's proposed allocation of Iatan 2, it will have an adverse impact upon GMO's customers that live in the St. Joseph and other L&P service areas. (Tr. p. 3820)

Staff acknowledges that its proposed allocation of 100 MW of Iatan 2 "will potentially cause the rates increase to L&P customers to be almost four times the rate increase to MPS customers." (Hearing Exhibit GMO-210 (NP), p. 102, COS Report) The Staff's Report also states: "Staff realizes that economic conditions are tough and the rate impact of adding 100 MW of Iatan 2 investment and costs in L&P's revenue requirement will not be easy for many of its customers." (Hearing Exhibit GMO-210 (NP), p. 95, COS Report) In support of its proposed allocation, despite the severe impact upon L&P customers, the Staff simply speculates that the

L&P service area may benefit in the long term and that L&P might have ended up with a similar result had it not been acquired by Aquila in the Year 2000. (Hearing Exhibit GMO-210 (NP), p. 103, COS Report)

Staff recognized that there might be more than one allocation scenario for allocating Iatan 2 that would be reasonable. (Tr. p. 3851). In fact, Staff analyzed five (5) different scenarios in the Cost of Service Report.

Ms. Mantle concluded that Scenarios 1, 2 and 3 were reasonable for GMO if the only consideration was L&P's needs as a stand alone company. (Scenario 2 represents the Staff's preferred allocation methodology). Scenario 5 allocated all of Iatan 2 to MPS, and would be most appropriate if the only consideration was MPS's needs as a stand alone utility. (Tr. p. 3851)

But, even Staff acknowledges that St. Joseph Light & Power Company was acquired by Aquila Inc. more than a decade ago, and MPS and L&P are not stand alone companies anymore. (Tr. p. 3851)

Scenario 4 (which is the scenario recommended by GMO) is the only scenario analyzed by Staff which finds some common ground and balances the interests of both MPS and L&P customers. (Tr. p. 3857):

[Fischer]: Q. There's—at Line 12 it says scenarios 1, 2 and 3 are reasonable for GMO if the only consideration is L&Ps needs as a stand alone utility. Is that right?

[Mantle]: A. That's what it says, yes.

Q. Okay. Then if we go up to Line 4, it says scenario 5 above, all of Iatan 2 allocated MPS would be the most appropriate scenario if the only consideration is MPS's needs as a stand alone utility; is that right?

A. That's right.

* * *

Q. But I believe you said that it—they are not really stand alone companies. Correct?

A. That is correct.

Q. Is there another scenario in between those two that would balance those interests?

A. I believe scenario 4 . . . more closely meet MPS's needs that Light and Power as a stand alone, it would be more beneficial to MPS.

* * *

Q. Wouldn't you agree that scenario 4 does find some common ground between those scenarios?

A. Yes.

(Tr. pp. 3851-52)

It makes little sense, from GMO's perspective, to analyze the issue of the proper allocation of Iatan 2--based upon an assumption that St. Joseph Light & Power Company was still in existence as a stand alone company. The corporate world has changed, and the Commission has much more flexibility to properly balance the interests of all customers as a result. Instead, the Commission should analyze the issue based upon the electricity needs of the customers in the two service areas.

For all of the foregoing reasons, GMO respectfully requests that the Commission equitably balance the interests of its MPS and L&P customers, and adopt GMO's proposed allocation of Iatan 2 in this proceeding.

4. <u>Rebasing: GMO Should Not be Required to Rebase its Base Energy Costs Above the Costs that are Proposed for GMO's Base Rates</u>

The Company did not request an increase in base rates for fuel and purchased power expenses (net of off-system sales) in excess of the amounts that are currently proposed for

GMO's rates in this case. Contrary to Staff's recommendation, the Company should not be compelled to rebase its Base Energy Costs in this regard. If the Commission were to adopt Staff's position, it would unnecessarily increase rates to customers.

Company witness Tim Rush explained that GMO decided to maintain the current base amount for both the MPS Division ($0.02348/KWh net system input) and the L&P Division ($0.01642/KWh net system input) in order to keep its overall rate request to as low an amount as reasonable, yet still allow for a reasonable recovery of fuel-related costs and a fair return to investors. See Rush Rebuttal (Cost of Service) at 3; Rush Rebuttal (Rate Design) at 26. Because GMO has not rebased these fuel and purchase power expenses (and, thus, not adjusted the Fuel Adjustment Clause [FAC] to reflect such rebasing), GMO has agreed to forego 5% of the increase in its future fuel and purchased power expenses under the current FAC that allows recovery of 95% of its prudently incurred costs.

As Mr. Rush testified in his pre-filed testimony, during the 2009 rate case GMO did propose to rebase its fuel costs, but encountered strenuous objections from other parties. See Rush Rebuttal (cost of service) at 3; Rush Rebuttal (rate design) at 26-27. Consequently, the Company adopted its current position which actually mitigates the proposed increase by over 11%, compared to what it would have been had GMO decided to seek a rebasing of its fuel costs. See Rush Rebuttal (Rate Design) at 27. Consequently, the Company's decision not to rebase its fuel costs should be viewed favorably by the Commission, given that GMO has agreed to recover only 95% of its prudent costs under the current FAC. Id. at 28.

Staff's proposal to rebase rates would raise MPS rates above existing levels by 6.5%, and by 21.2% for the L&P Division. See Rogers Surrebuttal at 8. Staff's recommendation to rebase fuel costs and raise rates beyond GMO's proposal appears to be premised upon both an economic theory and a legal theory. The economic theory is that rebasing rates "in each general

rate case assures that customers receive the correct price signal through fixed rates as soon as possible." Id. at 7. Staff witness Rogers additionally observed that customers would not be subjected to paying "unnecessarily additional interest which can occur if the FAC is not rebased" in each rate case. Id. However, he failed to calculate or otherwise analyze what the difference would be between any additional interest costs under the existing FAC and the increase in fixed rates proposed by Staff. Tr. 4484-85.

Under the existing FAC where GMO is permitted to recover 95% of its prudently incurred costs, customers surely receive sufficiently accurate price signals, based on the increase or decrease in fuel costs incurred by GMO. It is ironic that in other aspects of its case Staff ignores current economic realities (such as in its return on equity recommendations), but here seeks to make the customers pay more than what the utility asks to recover.

Staff also bases its recommendation to rebase fuel costs and rates on its subjective legal or regulatory view of "a good FAC and a good FAC sharing mechanism." See Rogers Rebuttal at 8. However, the Commission's Fuel Adjustment Clause rules do not require a rebasing of Base Energy Costs in an FAC every time a utility files a general rate case that requests that its rate adjustment mechanism be continued. See 4 CSR 240-3.161(3); 4 CSR 240-20.090. Although a voluminous amount of information is required when a utility proposes to continue an FAC, the twenty subsections of (A) through (T) of Rule 3.161(3) do not in any way address the rebasing of the fuel component of base rates. This is not surprising because there is nothing in Section 386.266 (the codification of Senate Bill 179) that concerns rebasing rates in general rate cases subsequent to the proceeding where an FAC is approved.

On cross-examination, Staff witness Rogers agreed that neither Section 386.266 nor the Commission's rules require rebasing. Tr. 4478. Additionally, given Mr. Rogers' retraction of his testimony in rebuttal regarding GMO's 2009 rate case and the rebasing issue (Tr. 4465-66,

4477), the only evidence in the record regarding this matter is Mr. Rush's testimony that there was no rebasing in the 2009 case, as a result of the positions taken by the parties, and that the Company's proposal in this case not to rebase Base Energy Costs is consistent with the resolution of the prior rate case. See Tr. 4443-44.

Given that neither Section 386.266 nor the Commission's rules relating to Fuel Adjustment Clauses require the rebasing of Base Energy Costs, there is no reason for the Commission to add to the rate increase requested by GMO and to set rates even higher -- 6.5% for the MPS Division and 21.2% for the L&P Division -- when it has not been requested by the Company.

5. Fuel Adjustment Clause Sharing Mechanism: The Commission Should Continue to Set the Sharing Mechanism at a 95% to 5% Ratio

GMO proposes to continue the current policy whereby it is permitted to pass 95% of its fuel costs above fuel costs built into base rates, with the remaining 5% of such costs being borne by the Company itself. The uncontroverted evidence in the record shows that there has been no investigation or even a suggestion that GMO is not properly accounting for its fuel costs or otherwise not competently procuring fuel. Given that the majority of other electric utilities in the Midwest recover 100% of their fuel costs (either in base rates or through a fuel adjustment mechanism), there is no reason to accept Staff's extreme proposal to quintuple the fuel costs that GMO must absorb by shifting the sharing mechanism to a 75/25 percent ratio.

GMO's Fuel Adjustment Clause was established and approved in the final rate case of its predecessor Aquila, where the Commission set forth the current 95/5 sharing mechanism in order to provide the Company an incentive to manage its fuel and purchased power costs efficiently. See In re Aquila, Inc., Report and Order, Case No. ER-2007-0004 (May 17, 2007) at 54. Since the FAC was established, Aquila/GMO have made six cost adjustment factor (CAF) filings which in total Staff estimated (and GMO agrees) under-collected $121 million over a 3-year

period. See GMO Staff Report at 196-97. Of this amount, approximately $6 million was absorbed by the Company pursuant to the 95/5 sharing mechanism. Id. at 197.

Staff now recommends, in essence, that an additional $24 million be added to this figure under its proposed 75/25 sharing mechanism. This would only serve to penalize GMO by prohibiting it from recovering more of the fuel costs that it incurs to serve its customers. See Rush Rebuttal (Cost of Service) at 5-7; Blanc Surrebuttal at 2. Such a recommendation is particularly at odds with Staff's admission that it "found no evidence of imprudent decisions by the Company's management related to procurement of fuel for generation, purchased power and off-system sales." See Staff Report at 193. At the evidentiary hearing, Mr. Rogers confirmed that this was Staff's finding. Tr. 4476-77.

Moreover, Staff's Report and Mr. Rogers's Surrebuttal Testimony confirm that prior to the inception of the FAC, Aquila had under-collected $116 million during 2004-06 "for which GMO's customers were responsible for paying $0." See Rogers Surrebuttal at 17. Mr. Rogers conceded on cross-examination that those losses contributed to Aquila's financial problems at the time. Tr. 4486 ["I'm sure it did."].

It is ironic then that Staff's recommended 75/25 ratio would return the Commission and GMO to those financially troubled times of the past, as the following exchange demonstrates:

> Q. ... so Staff would like to go back to the days of at least greater under-collections that would not be recovered by the Company. Is that a fair statement?
>
> A. Yes. [Tr. 4487]

Although Mr. Rogers was not familiar with Senate Bill 179, now Section 386.266 (Tr. 4487), that legislation passed by the General Assembly in 2005 firmly established the policy that cost recovery for prudently incurred fuel expenses should occur through the use of "periodic" or "interim" adjustments to rates. Since Staff's thorough reviews of GMO's fuel procurement

practices have uncovered no imprudence, Staff's recommendation is contrary to and undermines Missouri law and public policy.

Staff appears to have devised its recommendation in order to punish GMO for refusing to rebase its Base Energy Costs. Mr. Rogers conceded that while Staff had "not found any imprudence in its reviews, the Company's reluctance to reset the Base Energy Cost indicates that the 5% that GMO does not recover <u>is not large enough to mean much to GMO</u>." <u>See</u> Rogers Surrebuttal at 12 [emphasis added]. Mr. Rush aptly noted that the "true purpose" of Staff's proposal is "to discipline the Company for its position." <u>See</u> Rush Surrebuttal at 4. As Mr. Rush observed, rather than "a fundamental element of a 'good FAC mechanism' contemplated in advance," Staff's proposal seems to be "a punitive measure developed late in the case." <u>Id.</u>

If the Commission were to abandon the 95/5 sharing ratio, it would have profound consequences for this Company, compared with other electric utilities in the Midwest. It would send a disturbing message to the financial markets.

GMO Exhibit 51 summarizes the sharing mechanisms applicable to Fuel Adjustment Clauses in eleven other Midwestern states. While all of the utilities surveyed except one has a Fuel Adjustment Clause, none of the companies with FACs have a sharing mechanism like the one under which GMO operates. The sharing mechanisms that are utilized by other Midwestern utilities relate to off-system sales margins and provide a meaningful incentive, rather than a penalty. <u>See</u> GMO Exhibit 51 (reformatted version attached); Tr. 4449-50 (Rush: "GMO's current FAC states: 'We're going to make you absorb 5 percent rather than we're going to incentivize you to do something that you could also have a benefit from.' ").

GMO witness Gary M. Rygh, a Managing Director of Barclays Capital Inc., testified that the potential adverse effects of altering the 95/5 sharing mechanism to a 75/25 ratio would

"represent a major adverse modification to the FAC and make it even more challenging for GMO to earn the return on equity granted by the Commission ...." See Rygh Surrebuttal at 13.

Mr. Rygh stated that it would be "a far worse 'signaling' event to the investors whose capital is needed to ensure the continued safe and reliable operations of GMO." Id. He noted that given today's economic outlook and volatile commodity markets, investors would wonder why the Commission was "willing to significantly degrade the existing FAC and pass-through mechanism despite GMO's positive operational track record," in light of the fact that there was no evidence that GMO had not competently managed its largest operating expense. Id. at 11, 14. Given that 90% of integrated electric utilities in the United States "operate with a FAC and the vast majority of those have no sharing mechanism at all," investors would be concerned that GMO was at risk and held "in very little regard by the Commission." Id. at 14-15.

Mr. Rygh concluded:

> Investors expect and rely on the Commission to hold GMO accountable when it does not perform or does not act prudently. However, from an investor perspective, it is my opinion that making a significant adjustment to the sharing mechanism of the FAC in the absence of any performance issues would be viewed as lacking sufficient cause and doing so would create a much less favorable environment in which to consider deploying capital to GMO. [Id. at 16.]

In summary, there is no credible basis for Staff's recommendation to abandon the 95/5 sharing mechanism. There have been no findings of imprudence by GMO in its fuel procurement practices. There have been no irregularities cited in any of the Company's informational filings required by the Commission's regulations. No complaint case has been filed against GMO for irregularities in its fuel procurement practices. Nonetheless, with a vague reference to putting "more skin in the game" and displeasure with GMO's failure to rebase its Base Energy Costs or make more off-system sales during the worst recession since the Great

Depression,[1] Staff recommends that the Commission abandon the current practice which has worked well.

This is not the time to place greater financial burdens on the Company, particularly given uncertainty in the energy markets stemming from turmoil in the Middle East and the continued volatility in natural gas and other commodity markets. Any change in the 95/5 sharing mechanism will bring uncertainty to the minds of investors and raise unnecessary questions for a Company with a good operating record and, since its acquisition by Great Plains Energy, an improved financial outlook.

6. Off-System Sales Should Be Set on a Normalized Basis using Test Year 2009 MIDAS™ data, Not on 2007-08 Levels of Such Sales

GMO used 2009 normalized test-year data produced through the use of the MIDAS™ model to set off-system sales. This process was also used to normalize test-year fuel and purchased power costs. See Crawford Direct at 5-9. Staff, however, proposes to set off-system sales on stale and irrelevant historical data from 2007-08, which ignores recent economic facts and trends pertaining to the test year, as well as off-system sales policy set forth by the Federal Energy Regulatory Commission regarding wholesale electricity sales.

Staff witness V. William Harris reviewed off-system sales revenues and margin from 2002 to the present, noting the downward trend for both the MPS and L&P Divisions of GMO. See Staff Report at 77-78; Harris Rebuttal at 2-4. Without any particular reason, apart from what

[1] Staff's recommendations concerning fuel and energy related issues when analyzed together pose serious risks to GMO. Staff seeks to reset the Base Energy Costs, which GMO didn't ask for and customers will be shocked at. Additionally, Staff seeks to rejigger the FAC sharing mechanism to 75/25, increasing the burden of the Company to absorb more fuel costs, and causing investors to raise questions about its performance. Finally, it seeks to set rates based on off-system sales from 2007-08, and not the test year of 2009. These three positions of Staff, combined with its recommendation of a return on equity over 130 basis points below the national average of 10.33%, pose serious obstacles to achieving the Company's goals of operational and financial stability.

Mr. Harris judged to be a puzzling decline in sales, he arbitrarily chose to take data from 2007-08 to set rates. However, as Mr. Crawford pointed out, Staff's use of old historical off-system sales data -- some of it over four years old -- is flawed because it fails to consider the substantial changes in wholesale electricity market prices from 2007-08 to mid-2011 when GMO's rates will go into effect, as opposed to 2009 test-year data.

Staff's departure from using 2009 data is inconsistent with long-held concepts of utility regulation. "The test period construct is commonly, if not universally, followed in utility rate regulation." See L. Goodman, The Process of Ratemaking (1998) at 141. In Illinois the Commission has adopted an administrative rule requiring utilities to file rate cases with a proposed one-year test year. Citizens Utility Board v. Illinois Commerce Commission, 651 N.E. 2d 1089, 1103 (Ill. 1995). The purpose of a test year is to provide a period for which complete data is available in order to permit review by Staff and others, as well as to provide the Commission with a basis for estimation in future revenue requirements. See C. Phillips, The Regulation of Public Utilities (1993) at 196. While additional information to the "strict test year" concept is permitted, such new data typically reflects "a change that actually took place during or after the test period" or "a forward-looking test year." Id.

Missouri has also embraced the concept of test year and has not lightly departed from it, except to account for future developments or to normalize a level of revenue or expense that will be "more representative of future expenses." In re Union Elec. Co., Report and Order at 53, Case No. ER-2010-0035 (May 28, 2010) ("AmerenUE 2010 Rate Case") at 50. See State ex rel. Missouri Power & Light Co. v. PSC, 699 S.W.2d 941, 945 (Mo. App. W.D. 1984); State ex rel. Missouri Public Serv. Co. v. Fraas, 627 S.W.2d 882, 889 (Mo. W.D. 1981).

In AmerenUE's 2010 rate case the Commission reviewed data concerning coal plant maintenance expense, finding that the test year data should be normalized with data from outside

the test year. It did so carefully, with an eye toward "whether a proposed normalized test year expense is reasonably related to anticipated future expenses." See AmerenUE 2010 Rate Case at 53.

In this case the parties agreed to use 2009 as the test year, with a true-up as of December 31, 2010, with only certain exceptions not applicable to setting GMO's off-system sales. See Order Approving Nonunanimous Stipulation & Agreement, Setting Procedural Schedule, and Clarifying Order Regarding Construction & Prudence Audit at 2, ¶ 3 (Aug. 18, 2010).

Given the abrupt fall in energy prices from 2007-08, it would be unreasonable to focus only on those two years as Staff recommends, and to ignore data from 2009 as trued-up through 2010. The average market price during 2007-08 was approximately $50/MWh. Since 2009, the average price has dropped to around $30/MWh. See Crawford Rebuttal at 16. The data supplied by Company witness Michael Schnitzer of the NorthBridge Group, in response to a request from Commissioner Davis to provide the Commission with SPP-North spot market prices, confirms that electricity was bought and sold at much higher rates in 2007-08 than in the past two years. See KCP&L Ex. 122. Staff's proposal to utilize historical prices form 2007-08 to set off-system sales in rates must be rejected.

Additionally, the generating cost of the units from which excess generation is sold in the off-system wholesale market has risen since 2007-08. With higher expenses and lower market prices, margins naturally decrease. See Crawford Rebuttal at 16. With the expiration of GMO's purchased power contract with the Nebraska Public Power District and the addition of 153 MW from GMO's share of Iatan 2, off-system sales in 2011, even based on a test year of 2009, will not bear any relevance to the 2007-08 historical levels utilized by Staff. Id. at 17. Therefore, the data generated for 2009 using the MIDAS™ model should be used as proposed by the Company.

Finally, as both Mr. Crawford and Mr. Blanc testified at the evidentiary hearing, FERC has clarified that it is not appropriate for a utility to use network transmission service to facilitate purchases of energy for resale at a profit. See MidAmerican Energy Co., 112 FERC ¶ 61, 346, 2005 WL 2430182 (2005). In this case FERC made it clear that utilities are not to use network service to advance their own off-system sales. Network transmission service is to be used only to satisfy a utility's native load. In MidAmerican the audit conducted by FERC Staff uncovered a variety of irregularities, which the utility settled by agreeing to construct $9.2 million of previously unplanned transmission upgrades, and to forego recovery of all costs associated with these projects for six years from the time the assets are placed in-service. Id. at 3.

As Mr. Crawford noted, Aquila and KCP&L had "a different interpretation" of what was permissible under their respective tariffs, and the Company determined "what's permissible under that tariff and elected not to continue those ... transactions." Tr. 4221-22.

Staff's recommendation is based on 2007-08 data, without any analysis or research concerning energy prices in the SPP-North region since that time. Tr. 4228-29 (Harris). Mr. Harris additionally did not conduct any research regarding the use of network transmission service to facilitate off-system sales, and was not familiar with FERC policy that governs this subject. Tr. 4230-31. Mr. Harris's questions about GMO's recent off-system sales revenue and margins, given his lack of research and analysis, is mere speculation and not credible evidence.

Staff's proposal to set off-system sales based upon data that does not reflect test-year data from 2009 and the drop in energy prices since 2007-08 should be rejected. The Commission should adopt GMO's proposal to use 2009 normalized data, as set forth in Mr. Crawford's testimony which is consistent with the test year established in the case.

CONCLUSION

For all the reasons expressed above, GMO requests that the Commission adopt its position on the issues discussed in this brief.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I do hereby certify that a true and correct copy of the foregoing document has been hand delivered, emailed or mailed, postage prepaid, this 25th day of March, 2011, to all counsel of record.

/s/ Roger W. Steiner

Roger W. Steiner
Attorney for KCP&L Greater Missouri Operations Company

Sharing Mechanisms for Utilities in Missouri-Comparable States

(Neighboring and Other Non-Restructured Midwestern States)[1]

State	Major Investor-Owned-Utility	Fuel Adjustment Clause?	Sharing of Total Net Fuel & Purchased Power Expenses?	Separate Sharing of Off-System Sales Margins?	Historical or Projected Costs?	Historical
AR	Entergy Arkansas Inc	Yes	No	No	Projected	0
AR	Oklahoma Gas & Electric Co	Yes	No	No	Projected	0
AR	Southwestern Electric Power Co (AEP)	Yes	No	Yes, the minimum OSS margin, which would be fully credited to retail customers, was $583,539 (pre-merger) and $758,600 (post-merger). Both pre- and post-merger, 85% of OSS margins between $758,600 and $1,167,078 was credited to retail customers, and only 50% of OSS margins above $1,167,078 was credited to customers.	Projected	0
IA	Interstate Power & Light Co	Yes	No	No	Projected	0
IA	MidAmerican Energy Co	No	No	No	n/a	0
IN	Duke Energy Indiana	Yes	No	Yes, only 50% of OSS margin above base level is credited to ratepayers during summer periods	Projected	0
IN	Indiana Michigan Power Co (AEP)	Yes	No	Yes, only 50% of OSS margins above $37.5 million is credited to ratepayers	Projected	0
IN	Indianapolis Power & Light	Yes	No	No	Projected	0
IN	Northern Indiana Public Service Co	Yes	No	No	Projected	0
IN	Southern Indiana Gas & Electric Co	Yes	No	Yes, only 50% of OSS margins above $10.5 million is credited to ratepayers	Projected	0
KS	Kansas City Power & Light Co	Yes	No	No	Projected	0
KS	Kansas Gas & Electric Co	Yes	No	No	Projected	0
KS	Westar Energy Inc	Yes	No	No	Projected	0
KY	Duke Energy Kentucky	Yes	No	Yes, 50% of Margins > $1 million credited to ratepayers	Historical	1
KY	Kentucky Power Co (AEP)	Yes	No	No	Historical	1
KY	Kentucky Utilities Co	Yes	No	No	Historical	1
KY	Louisville Gas & Electric Co	Yes	No	No	Historical	1
MN	Allete Inc	Yes	No	No	Historical	1
MN	Interstate Power & Light Co	Yes	No	No	Projected	0
MN	Northern States Power Co (Minnesota)	Yes	No	Yes - 100% of asset-based energy sales, and 25% of non-asset based energy sales are credited to ratepayers	Projected	0
MN	Otter Tail Power Co	Yes	No	No	Historical	1
ND	MDU Resources Group Inc	Yes	No	No	Historical	1
ND	Northern States Power Co (Minnesota)	Yes	No	Yes - 85% of asset-based energy sales, and 50% of non-asset based energy sales are credited to ratepayers	Historical	1
ND	Otter Tail Power Co	Yes	No	Yes, 85% of asset-based sales margins credited to ratepayers	Historical	1
OK	Oklahoma Gas & Electric Co	Yes	No	Yes - 80% pass-through to ratepayers	Historical	1
OK	Public Service Co of Oklahoma (AEP)	Yes	No	Yes, 75% of OSS margin credited to ratepayers	Historical	1
SD	Black Hills Power Inc	Yes	No	Yes, 65% of pretax Power Marketing Operating Income credited to ratepayers, not to fall below $2 million per year	Historical	1
SD	Northern States Power Co (Minnesota)	Yes	No	Yes - 100% of asset-based energy sales, and 25% of non-asset based energy sales are credited to ratepayers	Historical	1
SD	NorthWestern Corp	Yes	No	No	Historical	1
TN	Kingsport Power Co (AEP)	Yes	No	No	Historical	1
WI	Consolidated Water Power Co	Yes	No	No	Historical	1
WI	Madison Gas & Electric Co	Yes	No, although there is a threshold to trigger review	No	Projected	0
WI	Northern States Power Co (Wisconsin)	Yes	No, although there is a threshold to trigger review	No	Projected	0
WI	Superior Water Light & Power Co	Yes	No	No	Historical	1
WI	Wisconsin Electric Power Co	Yes	No, although there is a threshold to trigger review	No	Projected	0
WI	Wisconsin Power & Light Co	Yes	No, although there is a threshold to trigger review	No	Projected	0
WI	Wisconsin Public Service Corp	Yes	No, although there is a threshold to trigger review	No	Projected	0
Total	37	**36**	**0**	**12**		
% of Total		**97%**	**0%**	**32%**		

[1]: Sample reflects Major Investor-Owned-Utilities in non-restructured states either bordering Missouri, or within the Midwest (defined as states within Census Bureaus of West North Central and East North Central). Major Investor-Owned-Utility defined using a threshold of at least 500 GWh of retail sales in 2006.

GMO Exh. 51
(Reformatted)

Sharing Mechanisms for Utilities in Missouri-Comparable States

(Neighboring and Other Non-Restructured Midwestern States)[1]

Projected	Frequency of Adjustment	Backup documentation	Monthly	Monthly And Historical
1	Annually	http://www.entergy-arkansas.com/content/price/tariffs/eai_ecr.pdf	0	0
1	Annually	http://www.oge.com/Documents/ARK/Energy%20Cost%20Recovery%20Rider%20(Rider%20ECR).pdf	0	0
1	Annually	https://www.swepco.com/global/utilities/lib/docs/ratesandtariffs/Arkansas/Arkansas2_12-01-2009.pdf	0	0
1	Monthly	http://www.alliantenergy.com/UtilityServices/UtilityRatesFacts/ssLINK/015433	1	0
0	n/a	http://www.midamericanenergy.com/include/pdf/rates/rates_main.pdf#page=4	0	0
1	Quarterly	http://www.duke-energy.com/rates/indiana/tariff.asp	0	0
1	Quarterly	https://www.indianamichiganpower.com/global/utilities/lib/docs/ratesandtariffs/Indiana/IM-IN-TB-10-01-10.pdf	0	0
1	Quarterly	http://www.iplpower.com/library/IPL/website%2011.30.10/FAC%2089%2011-30-10.pdf	0	0
1	Quarterly	http://www.nipsco.com/Libraries/Electric_Tariffs/electricgrr.sflb.ashx	0	0
1	Quarterly	http://www.snl.com/irweblinkx/file.aspx?IID=4057065&FID=9163208&O=3&OSID=9	0	0
1	Annually, with quarterly updates and rate adjustments	http://www.kcpl.com/about/KSRates/Sched2.pdf	0	0
1	Quarterly	http://www.westarenergy.com/wcm.nsf/publishedtariffs/E3A44B382C2185B08625770C00676248/$file/RECA	0	0
1	Quarterly	http://www.westarenergy.com/wcm.nsf/publishedtariffs/6C8B8128BC9366938625770C00676235/$file/RECA.	0	0
0	Monthly	http://www.duke-energy.com/pdfs/DE-KY-rider-psm_3.01.10.pdf, http://www.duke-energy.com/pdfs/Sheet_Nc	1	1
0	Monthly	https://www.kentuckypower.com/global/utilities/lib/docs/ratesandtariffs/kentucky/KYTAR12-30-2009.pdf	1	1
0	Monthly	http://www.eon-us.com/rsc/ku/kuelecrates.pdf	1	1
0	Monthly	http://www.eon-us.com/rsc/lge/lgereselectric.pdf	1	1
0	Monthly	http://www.mnpower.com/regulatory_matters/documents/ratebook_internet.pdf	1	1
1	Monthly	http://www.alliantenergy.com/UtilityServices/UtilityRatesFacts/ssLINK/015433	1	0
1	Monthly	http://www.xcelenergy.com/SiteCollectionDocuments/docs/Me_Section_5.pdf	1	0
0	Monthly	http://www.otpco.com/ElectricRates/PDF/MN/MN_13.01.pdf	1	1
0	Monthly	http://www.montana-dakota.com/RatesTariffs/NDElectric58.pdf	1	1
0	Monthly	http://www.xcelenergy.com/SiteCollectionDocuments/docs/Ne_Section_05.pdf	1	1
0	Monthly	http://www.otpco.com/ElectricRates/PDF/ND/ND_13.01.pdf	1	1
0	No more than quarterly	http://www.oge.com/residential-customers/billing-and-payment/Pages/RateInfo.aspx	0	0
0	Varies	https://www.psoklahoma.com/global/utilities/lib/docs/ratesandtariffs/Oklahoma/RidersMiscSchedules10-2010.	0	0
0	Annually	http://www.blackhillspower.com/pdf/SDTariff.pdf	0	0
0	Monthly	http://www.xcelenergy.com/SiteCollectionDocuments/docs/Se_Section_5.pdf	1	1
0	Quarterly	http://puc.sd.gov/commission/tariffs/Electric/NOrthwestern/section3.pdf	0	0
0	Monthly	https://www.appalachianpower.com/global/utilities/lib/docs/ratesandtariffs/Tennessee/kgtariff03-10.pdf	1	1
0	Monthly	http://psc.wi.gov/pdffiles/tariffs/elc/1330.pdf	1	1
1	Varies	http://www.legis.state.wi.us/rsb/code/psc/psc116.pdf	0	0
1	Varies	http://www.legis.state.wi.us/rsb/code/psc/psc116.pdf	0	0
0	Monthly	http://www.swlp.com/customer_service/rates/doc/swlp_ratebook.pdf	1	1
1	Varies	http://www.legis.state.wi.us/rsb/code/psc/psc116.pdf	0	0
1	Varies	http://www.legis.state.wi.us/rsb/code/psc/psc116.pdf	0	0
1	Varies	http://www.legis.state.wi.us/rsb/code/psc/psc116.pdf	0	0