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Witness:	*Charles R. Hyneman*
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MISSOURI PUBLIC SERVICE COMMISSION

UTILITY SERVICES DIVISION

SUREBUTTAL TESTIMONY

OF

CHARLES R. HYNEMAN

Great Plains Energy, Inc.
GREATER MISSOURI OPERATIONS COMPANY
GMO-MPS AND GMO-L&P ELECTRIC

CASE NO. ER-2009-0090

Jefferson City, Missouri
April 9, 2009

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

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EXECUTIVE SUMMARY

Q. What is the purpose of this testimony?

A. The purpose of this testimony is to respond to the rebuttal testimonies of several GMO witnesses on the issues noted above on the Table of Contents page of this testimony.

TRANSITION COSTS

Q. Please provide a summary of your surrebuttal testimony on the transition cost recovery issue.

A. The Staff is proposing the regulatory lag recovery method instead of the direct rate recovery method for Great Plains Energy's (GPE) transition costs in this case. GPE is the parent company of GMO and KCPL and is seeking direct rate recovery of transition costs for its utility subsidiaries. The basis of Staff's position is that GPE, Aquila, and KCPL, (the Joint Applicants in GPE's July 14, 2008 acquisition of Aquila, Inc.), have not lived up to the commitments made to the Commission and relied upon by the Commission to approve GPE's acquisition of Aquila in Case No. EM-2007-0374 (the Acquisition Order).

1 Specifically, the Joint Applicants failed to implement a synergy savings tracking mechanism
2 with a 2006 base year as ordered by the Commission.

3 Q. How did the transition cost recovery issue developed?

4 A. On April 4, 2007, the Joint Applicants filed an application with the
5 Commission seeking authority for a series of transactions whereby Aquila's Missouri electric
6 operating divisions of Aquila Networks-MPS (MPS) and Aquila Networks-L&P (the former
7 Saint Joseph Light & Power Company) would become a direct, wholly-owned subsidiary of
8 GPE. On July 1, 2008, the Commission approved the acquisition (the Acquisition case).

9 In the Commission's Acquisition Order, the Commission concluded that it is not a
10 detriment to the public interest to allow recovery of transition costs of the acquisition.
11 In paragraph 6c. of the Ordered Section of the Acquisition Order, the Commission directed
12 the Joint Applicants to implement a synergy savings tracking mechanism using a base year
13 of 2006.

14 The Staff's position is that through the language of Paragraph 6c of the
15 Acquisition Order, the Commission ordered GPE to create this synergy savings tracking
16 mechanism to prove that the overall costs of operating the <u>combined</u> KCPL and GMO
17 (the former Aquila electric operations of MPS and L&P) was less than the cost of operating
18 KCPL and Aquila on a pre-acquisition stand alone basis and that net integration synergies
19 would be realized by both KCPL and GMO.

20 The Staff also believes that by ordering GPE to produce this document the
21 Commission is also requiring GPE to provide this document as evidence to support its current
22 and subsequent transition cost rate recovery proposals.

1 Staff contends that the Joint Applicants proposed and the Commission adopted the
2 provision that the burden of showing that the GPE acquisition of Aquila has resulted in a
3 reduced level of operating costs, and this reduced level of expense is greater than the amount
4 of transition costs that the Joint Applicants would seek to recover in future rate cases.

5 Contrary to the Staff's understanding of the Acquisition Order, GMO, through the
6 rebuttal testimony of Mr. Darrin Ives, has taken the position that the Commission required no
7 such synergy savings tracking mechanism be produced to support rate recovery of its
8 transition costs in this rate case or any future rate case.

9 The Staff is requesting that the Commission find that the failure to produce the
10 required documentation is evidence that GMO has not met the burden of proof standard that it
11 committed to in the Acquisition Case. This standard was adopted by the Commission and
12 was to be met by GMO prior to charging its customers for the transition costs.

13 In the Acquisition Order, the Commission agreed that there was the potential for
14 significant savings as a result of the acquisition and was supportive of the recovering of costs
15 incurred in combining the operations of KCPL and Aquila (transition costs). While the
16 Commission was supportive of recovery of the transition costs in general, the Commission did
17 not specify any method in which this recovery is to be accomplished.

18 In fact, its Ordered paragraphs 13 of the Acquisition Order, the Commission stated
19 that "nothing in this order shall be considered a finding by the Commission of the value for
20 ratemaking purposes of the transactions herein involved." And in paragraph 14 it said that the
21 Commission "reserves the right to consider any ratemaking treatment to be afforded the
22 transactions herein involved in a later proceeding."

1 Because it has not met the standard required for direct rate recovery, the Staff
2 recommends that the Commission order GMO to recover its transition costs by using the same
3 method as GMO proposed that it be allowed to recover its integration
4 synergies – natural regulatory lag.

5 Q. Does GPE in general support the use of natural regulatory lag as a
6 cost recovery mechanism?

7 A. Yes. GPE, for reasons that are not clearly supported or explained, supports the
8 use of regulatory lag to recover the benefits of the acquisition – integration synergies,
9 but rejects the use of regulatory lag to recover the costs to achieve the synergies – transition
10 costs. The Staff believes that GPE's proposal is inconsistent, is not adequately supported in
11 testimony, and is not supported by the evidence in which the Commission ordered it to
12 produce.

13 Q. What is the basis of the Staff's position that transition costs should be
14 recovered by GMO through natural regulatory lag?

15 A. As described above, the Staff's position is based on the fact that GPE has not
16 produced the synergy savings tracking mechanism so ordered by the Commission.
17 The synergy savings tracking mechanism was a Joint Applicant proposal that was adopted by
18 the Commission as a requirement to show net acquisition benefits have been realized before
19 direct rate recovery would be allowed.

20 Q. Are there other reasons why the natural regulatory lag method is the preferred
21 method for transition cost recovery in this case?

22 A. Yes. As noted by GPE itself, any attempt to accurately track integration
23 savings is difficult in the best of conditions. This is position also supported by Staff.

1 GPE, however, by its management deciding to file four separate rate cases in less than
2 two months following the closing date of the acquisition, has created the worst conditions
3 under which any analysis of acquisition synergies can take place.

4 The GPE management decision to file rate cases so soon after the acquisition closing
5 has forced GMO into a position where it physically cannot produce any actual evidence of the
6 existence of actual net acquisition synergies. The appropriate course of action for the
7 Commission to take is to allow GMO the opportunity to recover its transition costs in the
8 same manner GMO proposes it be allowed to recover integration synergies, through natural
9 regulatory lag.

10 Q. Since GPE did not implement the synergy tracker ordered by the Commission
11 in Case No EM-2007-0374, does actual financial information for GMO show that the level of
12 non-fuel operations and maintenance expense (NFOM) GMO is incurring today in
13 a post-acquisition environment is less than the level it incurred in the 2006 base year, as a
14 stand alone entity?

15 A. No. In 2006 Aquila filed for a rate increase for its MPS and L&P operating
16 divisions. That case, Case No. ER-2007-0004, was based on a 2005 test year updated for
17 known and measurable changes through September 2006, with a true-up date of December
18 2006. A comparison of the Staff's Accounting Schedules' updated NFOM levels in that case
19 compared to the Staff's current NFOM levels in this rate case shows an increase of $19
20 million, or 18% for GMO-MPS, and an increase of $5.3 million, or 12% for GMO-L&P
21 electric. There is no indication that the combined post-acquisition NFOM expenses for either
22 GMO-MPS or GMO-L&P have decreased from pre-acquisition levels.

1 This data is reflected in the chart below and is included as Schedule 1 to this
2 testimony:

		MPS Staff EMS ER-2007-0004 "Base Year" NFOM	MPS Staff EMS ER-2009-0090 "Current" NFOM
O&M	Acct	$318,989,653	$338,592,960
Fuel	501	($65,882,708)	($86,842,102)
Fuel	547	($15,693,210)	($26,284,993)
Purch Pwr	555	($79,123,271)	($70,255,970)
Purch Pwr	555	($7,485,922)	($26,881,690)
Purch Pwr	555	($42,139,995)	($598,049)
NFOM		**$108,664,547**	**$127,730,156**
Increase			**$19,065,609**
Increase %			**18%**

		L&P Staff EMS ER-2007-0004 "Base Year" NFOM	L&P Staff EMS ER-2009-0090 "Current" NFOM
O&M	Acct	$101,762,675	$101,488,550
Fuel	501	($17,313,510)	($21,737,163)
Fuel	547	($1,485,134)	($4,438,929)
Purch Pwr	555	($19,637,113)	($26,359,604)
Purch Pwr	555	($9,492,000)	$0
Purch Pwr	555	($10,239,841)	$0
NFOM		**$43,595,077**	**$48,952,854**
Increase			**$5,357,777**
Increase %			**12%**

3

4 GMO's NFOM expense levels are not decreasing as promised in the Acquisition Case,
5 but significantly increasing. Even if a 3 percent across the board inflation rate is assumed for
6 each dollar of NFOM expense for 2007 and 2008, the NFOM increase is still $12.5 million
7 for GMO-MPS or 11 percent increase, and an increase of $2.7 million for GMO-L&P or 6 %
8 increase.

9 While GMO can point to isolated examples of cost reductions, such a method is
10 deficient in that it fails to examine areas of the operations that may have increased expenses
11 as a result of the GPE acquisition. The Joint Applicants proposed and the Commission
12 accepted a 2006 tracker to be able to calculate when synergies existed. The Commission's

1 approach was to protect consumers from paying transition costs from a flawed acquisition by
2 accepting the Joint Applicants' proposal to only seek recovery of these costs when and if the
3 acquisition produced actual net synergies, not estimated or budgeted synergies.

4 GMO and KCPL have failed to produce the required documentation to prove the
5 existence of net synergies and the Staff is holding the Joint Applicants to the commitment
6 made in the Acquisition case.

7 Q. Did the Joint Applicants promise to achieve a significant level of integration
8 synergies?

9 A. Yes. At paragraph 34 of its Joint Application of Great Plains Energy
10 Incorporated, Kansas City Power & Light Company and Aquila, Inc., in Case No.
11 EM-2007-0374, the Joint Applicants stated "that the Merger will result in significant
12 synergies, economies of scale, and efficiencies from the elimination of duplicate corporate
13 and administrative services, all of which will ultimately result in a lower cost of operations.
14 In its Acquisition Order (paragraph 273), the Commission said that "the range
15 of 7-10% is a reasonable general expectation for total nonfuel synergy savings."

16 Q. Has there been any evidence in this case or any evidence at all put forth by
17 KCPL that the acquisition has yet resulted in a lower cost of operations?

18 A. No. GMO has not produced any document which shows that the total
19 NFOM expenses of operating GMO after the acquisition is lower than its pre acquisition
20 NFOM expense. The only evidence in this rate case that is based on the actual costs of
21 providing utility service, the analysis shown above, shows, not a decrease, but a significant
22 increase in NFOM expense.

1 Q. Does the GMO witness Ives appear to agree that the Commission was not
2 making any finding on the subsequent ratemaking treatment of transition costs in its
3 Acquisition Order?

4 A. He apparently does, although his rebuttal testimony at page 2 is not clear.
5 Here Mr. Ives tries to explain that he knows why the Commission attached a footnote to
6 language at page 241 of its Acquisition Order and that the Commission did this to "align"
7 ordered paragraphs 13 and 4 described above with language it included at page 241 of its
8 Acquisition Order.

9 The Staff does not understand the point Mr. Ives is trying to make here or how he
10 came to know the reasons why, when the Commission was drafting the Acquisition Order,
11 it attached a specific footnote to a particular paragraph to "align" it with subsequent ordered
12 paragraphs. However, while the point Mr. Ives was attempting to make is unclear, what is
13 absolutely clear is the fact that the Commission ordered no finding of ratemaking treatment of
14 transition costs in its Acquisition Order.

15 Q. At page 3 of his rebuttal testimony Mr. Ives quotes from the Conclusions
16 of Law – Final Conclusions Regarding Projected Synergy Savings section on pages 237 and
17 238 of the Commission's Acquisition Order:

> 18 The Commission further determines that substantial and
> 19 competent evidence in the record as a whole supports the
> 20 conclusions that … (3) the synergies exceed transaction and
> 21 transition costs and the method proposed for recovery of
> 22 transaction and transition costs does not place the ratepayers at
> 23 risk … and (4) because the Applicant's have agreed to recover
> 24 any merger savings through 'regulatory lag' as part of the
> 25 traditional ratemaking process there is no net detriment to
> 26 customers….

1 Q. Please comment on this portion of Mr. Ives' rebuttal testimony.

2 A. It appears Mr. Ives is quoting this language to support his conclusion that the
3 Commission's intent is that integration synergies should be recovered through regulatory lag,
4 but not the associated transition costs that were incurred to achieve the integration synergies.
5 According to Mr. Ives, the Commission intended that the transition costs to achieve the
6 integration synergies should receive special treatment by receiving direct rate recovery.
7 Mr. Ives' conclusion is contradicted by the language contained in the Commission's order.

8 Q. How does Mr. Ives' conclusion conflict with the language in the
9 Commission order?

10 A. At paragraph 14, page 284 of the Ordered Section of the
11 Commission's Acquisition Order, the Commission ordered that it reserves the right to
12 consider any ratemaking treatment to be afforded the transactions herein involved in a later
13 proceeding. The Staff interprets this language to mean that the Commission would consider
14 the Staff's proposed method of recovery of transition costs, which can be described as
15 the indirect, or "natural regulatory lag" method as well as the Company's proposed method of
16 transition cost recovery, the direct rate recovery method. In addition, the Commission would
17 consider any proposed recovery method put forth by any party to this rate proceeding.

18 Q. Explain further how GPE has not complied with the Commission's Acquisition
19 Order concerning a demonstration that integration savings are greater than its transition costs?

20 A. At paragraph 6c, page 282 of the Ordered Section of the Commission's
21 Acquisition Order, the Commission ordered that the parties shall implement a synergy savings
22 tracking mechanism as described Applicants, and in the body of this order, utilizing a base
23 year of 2006.

1 GPE's acquisition of Aquila closed on July 14, 2008. Over eight months have passed
2 since this transaction closed and GPE has yet to produce any synergy savings tracking
3 mechanism that shows actual net synergies actually exist. As stated in Paragraph 1 of the
4 Ordered Section on pages 282 and 283, the transaction was approved subject to the conditions
5 in ordered paragraphs 2 through 15. GMO has failed to comply with paragraph 6c shown
6 below:

7 6. Authorization of the transactions described in Ordered
8 Paragraphs Number One through Five are subject to the
9 following conditions:

10 c. Great Plains Energy, Incorporated, Kansas City Power
11 & Light Company, and Aquila, Inc., shall, upon closure
12 of the authorized transactions, implement a synergy
13 savings tracking mechanism as described by the
14 Applicants, and in the body of this order, utilizing a base
15 year of 2006.

16 Q. Did Staff request and receive a synergy savings tracking mechanism tracking
17 actual costs incurred with a base year of 2006?

18 A. No. GMO filed this rate case in September 2008, over seven months ago.
19 Throughout its cost of service audit the Staff repeatedly requested that it be provided with a
20 copy of the synergy savings tracking mechanism using a base year of 2006 that the
21 Commission ordered GMO and KCPL to implement in Case No. EM-2007-0374.

22 GMO responded that no such tracking mechanism was implemented to support
23 transition cost recovery in this rate case. Upon prodding by the Staff, GMO began to make an
24 effort to produce this document. Finally, on Thursday, April 2 2009, the Staff received this
25 document, four business days prior to filing this surrebuttal testimony.
26 Because of the time commitments of this surrebuttal testimony, both in writing testimony and
27 reviewing the surrebuttal testimony of other Staff auditors, I have not yet started an analysis

1 and audit of the data provided. I just began my review of this data on April 7, 2009.
2 As I noted in my direct testimony in the Staff's Cost of Service Report, there is no possible
3 way for this document to be adequately analyzed, audited and conclusions reached prior to the
4 conclusion of this rate case.

5 Q. What does your preliminary review of the summary document of this study
6 show?

7 A. GPE used a 2006 base year NFOM expense level for KCPL and GMO.
8 Added to this amount was $48 million of inflation dollars, which represents an inflation
9 increase of 3.1 percent for 2007, 2008 and 2009. Also added to these inflated base year
10 expenses was an additional $86 million in baseline adjustments for a total adjustment to 2006
11 baseline expenses of $134 million, or a 27 percent increase.

12 To calculate its expected synergies, GPE did not use any actual incurred costs, but
13 2009 budgeted NFOM costs. The Staff understands that part of the delay in the Staff receiving
14 this study is that GPE's Board of Directors had to approve the 2009 budget.
15 GPE's conclusion was that its 2009 budgeted NFOM expense levels for GMO and KCPL
16 is $40 million less than the 2006 base year NFOM expense level after including
17 the $134 million of additional costs. Just from the summary page of this document the Staff
18 has serious concerns about the current levels of inflation assumed and the amount of
19 additional expenses added to 2006 base year NFOM expenses.

20 Q. Does the Staff have an opinion as to what needs to be included in the tracker
21 that implements a synergy savings tracking mechanism which is in compliance with the
22 Commission's Acquisition Order?

1 A. Yes. The Staff recommends that any inflation rate included in the tracker be
2 based on actual incurred inflation rates in the event that reasonable and necessary known and
3 measurable adjustments are made and approved to the 2006 base year. Further, any inflation
4 factor needs to be adjusted to the known and measurable amount of the changes and the
5 timing of when these known and measurable changes result in incurred costs. Finally, any
6 inflation factor must be offset by a productivity factor that is inherent in the operations of
7 most businesses. Productivity factors reflect expense savings and/or productivity
8 improvements that occur over time. If no inflation factor is used in the tracker, then a
9 productivity factor would not be needed. In this case, any inflation increase would be
10 assumed offset by the productivity increase.

11 Q. At page 5 of his rebuttal testimony Mr. Ives describes how your testimony in
12 the Staff's Cost of Service Report indicated that GMO has already enjoyed the benefits of
13 synergy savings through regulatory lag. Is he correct?

14 A. Yes. In the Staff's Cost of Service Report, I provided an example of how,
15 under GPE's belief as to the level of current synergies being realized, GMO has already
16 recovered and is currently recovering, through natural regulatory lag, a significant portion of
17 its transition costs

18 Q. Has GPE indicated by its testimony in the Acquisition Case that it believes,
19 by September 2009, it will have received integration synergy revenues in an amount sufficient
20 to pay for all of the transition costs it has incurred to date?

21 A. Yes. In the Supplemental Direct Testimony provided by Terry Bassham in
22 Case No. EM-2007-0374 at page 3, he stated that on a Missouri jurisdictional basis total
23 synergies are equal to $222 million over the first five years. Using Mr. Bassham's own

1 calculations and assuming the savings are realized ratably, GPE will have already recovered
2 22 percent of the $222 million five year synergies, or $48 million by the time the rates are
3 changed in this case in September 2009. This $48 million of transition costs that according to
4 GPE will be recovered by September 2009 exceeds the $42.8 million Missouri portion of the
5 total transition costs that GPE will incur in the first five years. This amount is shows at page
6 5 of Mr. Bassham's Supplemental Direct Testimony.

7 Q. Has GPE already publicly announced that it has realized significant integration
8 synergies due to natural regulatory lag?

9 A. Yes. William Downey, President and COO, GPE and KCPL
10 in a EEI Conference Webcast on November 11, 2008 stated that GPE has already achieved a
11 net $23 million of operating synergies that accrued to GPE's shareholders in just the
12 four-month period from July 15, 2008 through November 11, 2008, or almost 40 percent of its
13 anticipated total company transition costs.

14 Q. Is it normal practice for a utility or for any company to first use revenues
15 received to pay expenses and then allocate any remaining revenues to profit?

16 A. Yes, it is.

17 Q. Is that how GMO is planning to treat its synergy savings revenues?

18 A. No. GPE is planning to allocate all of the additional synergy savings revenues
19 that it has realized from August 2008 to September 2009 to profit and not allocate one dollar
20 of this estimated $48 million in revenues to the transition costs of the acquisition.
21 This proposal makes no sense from either an accounting or a ratemaking standpoint and is
22 directly contrary to accounting and ratemaking principle of matching, which requires that

1 there be recognition in the same period of the revenues received and the expenses incurred to
2 generate those revenues.

3 In contrast to GPE, the Staff is proposing that GMO, through natural regulatory
4 lag, would recover these integration synergies and apply them to pay down the deferred
5 transition costs. All the remaining synergies it achieves in between rate cases can be assigned
6 as profit to its shareholders. This natural regulatory lag as proposed by the Staff is simple and
7 straightforward. If GPE is correct that the synergies have occurred, are occurring today and
8 will continue to occur over the next ten years, this method is an easily achievable way for
9 GMO to recover all of its transition costs.

10 Q. Has GMO attempted to match any of the additional integration synergy
11 revenues that it has realized and is currently receiving with the transition cost expenses that
12 were necessary to generate the additional revenues?

13 A. No. In its original Application to the Commission in the Acquisition Case,
14 GMO proposed that it be allowed to defer as a regulatory asset its transition costs and
15 amortize these costs over five years beginning the month following the July 2008 closing.
16 This would mean that the amortization would have started in August 2008, which is a logical
17 and appropriate start date. However, GPE changed this proposal from starting the
18 amortization the month following closing of the transaction to starting the amortization when
19 rates from the current rate cases become effective, currently estimated to be September 2009.

20 If GMO actually began its amortization in August 2008, then there would be a
21 matching of the additional revenues (integration synergies) being realized currently with the
22 costs incurred to generate these additional revenues. Because GMO is not currently
23 amortizing its transition costs against current integration synergy revenues, all of the

1 integration synergies realized from August 2008 until September 2009 will be enjoyed as
2 profit by GPE's shareholders.

3 Q. By delaying its amortization of transition costs until September 2009 when,
4 according to GPE, the incurred transition costs started to produce integration synergy benefits
5 much earlier in August 2008, is GMO improperly matching its additional integration synergy
6 revenues with the expenses it incurred to generate these revenues?

7 A. Yes. GMO is improperly applying the accounting and ratemaking matching
8 principle that says costs should be matched with the revenues generated from the incurrence
9 of the costs, or stated another way, the costs should be matched over the period in which the
10 associated benefits are received.

11 According to GMO, significant integration synergy revenues (benefits) are currently
12 being received, yet no matching of the additional revenues is being made with the costs that
13 were incurred to generate these benefits. This is a failure on the part of GMO to properly
14 apply the requirements of the matching principle.

15 Q. When did GPE change its proposal from the correct amortization start date of
16 August 2008 (the month following the acquisition closing) to its revised and incorrect
17 September 2009 start date?

18 A. In the Supplemental Direct Testimony provided by Terry Bassham in Case No.
19 EM-2007-0374 at page 5, Mr. Bassham changed the Joint Applicants request for the date to
20 start the amortization from the month following the transaction closing date, which is August
21 2008 to the date the rates change in this rate case, which is estimated to be September 2009.

22 Also at page 4 of the Supplemental Direct Testimony of GPE witness Chris B. Giles
23 he states that "we propose to allocate the merger integration costs over a period of five years

1 (beginning with the effective date of rates ordered by the Commission in the first rate case
2 after the close of the merger)." This change in GPE's proposal is also shown at page 3 line 26
3 through page 4 line 4 of Mr. Ives' rebuttal testimony.

4 Q. What is the effect of GPE changing its transition cost amortization start date?

5 A. The effect of this changed proposal is that GPE, according to its own estimates
6 will reap the benefits of $48 million in integration savings by charging its regulated
7 KCPL and GMO customers rates that are based on recovering $48 million in expenses that no
8 longer exist.

9 The transition costs that are currently being recovered by GMO and KCPL are being
10 recovered through regulatory lag. The net result is that by delaying the start date of the
11 transition cost amortization, 100 percent of the benefits of the savings that GMO and KCPL
12 have enjoyed and will enjoy through natural regulatory lag until rates are changed in the
13 current rate cases, in which Mr. Bassham estimates to be $48 million, flows directly to net
14 profit for GPE's shareholders.

15 Q. Do the 13 months that will have elapsed between the time the transaction
16 closed in July 2008 and the date that rates will change in this rate case, September 2009 have
17 the same effect as a rate moratorium period?

18 A. Yes, it does. This time period between rate cases is an example where
19 natural regulatory lag allows for the merged entities to enjoy any cost savings from
20 lower combined expenses that, according to GPE, are currently being incurred
21 (such as reduced payroll, medical insurance and other benefits) over the higher level of
22 expenses that are embedded in current rates.

Q. Does GMO anywhere in its testimony in this case address how it is proposing to treat this $48 million in additional revenues that it will receive through natural regulatory lag?

A. No. GMO is silent on the issue of associating any current integration synergies with the costs incurred to obtain the synergies. However, if GPE kept to its original proposal in the Acquisition Case it would have been amortizing 1/60th of its transition cost deferral to expense each month beginning in August 2008. When rates change as a result of this rate case GPE's books and records would have recognized that it had already recovered 22 percent of its transition cost deferral (13 months divided by the total amortization period of 60 months).

Q. You've been describing how GMO is already recovering transition costs through natural regulatory lag. If the Commission ordered GMO to continue this method of transition cost recovery, instead of starting the amortization process over again beginning in September 2009 through direct rate recovery, in your opinion would it prevent a lot of rate case issues and litigation that is likely to arise over the accuracy of any integration tracking study in future rate cases?

A. Yes. In its Acquisition Order, based on GPE testimony, the Commission agreed that it would be very difficult to track synergy savings with any degree of accuracy. The following is a finding of fact from page 97 of the Commission's Acquisition Order:

> 244. Tracking synergy savings with any degree of accuracy is problematic at best. Business operations are not conducted in a static environment, but rather under constant change, including customer growth, technological improvements, etc. Tracking will become more difficult each successive year after the merger. 353
>
> 353. (GPE/KCPL Exhibit 29, Wright Direct p. 5; GPE/KCPL Exhibit 1, Bassham Direct, p.10).

Q. At page 4 line 31 of his rebuttal testimony, Mr. Ives begins a description of how Staff has addressed transition cost recovery in previous merger and acquisition cases before the Commission. Were you involved in all of these cases?

A. Yes. In addition, I have participated in the following merger or acquisition cases before the Commission:

EM-96-149	Union Electric/CIPSCO, Inc.
EM-97-515	Western Resources, Inc. /Kansas City Power & Light Co.
GM-2000-312	Amos Energy Corp/Associated Natural Gas Company
EM-2000-369	UtiliCorp United Inc./Empire District Electric Company
EM-2000-292	UtiliCorp United Inc./St. Joseph Light & Power Company
GM-2000-502	Southern Union Company/Valley Resources, Inc.
GM-2000-0043	Southern Union Company/Pennsylvania Enterprises, Inc.
GM-2000-500	Southern Union Company/Providence Energy Corporation
GM-2000-503	Southern Union Company/Fall River Gas Company
GM-2003-238	Southern Union Company / Panhandle Eastern Pipeline Projects

Q. Do you agree with Mr. Ives' characterization of the Staff's general position on recovery of transition costs?

A. Yes. As noted in Mr. Ives' rebuttal testimony, the Staff has been supportive of transition cost recovery in rates over a reasonable period of time, which in the past the Staff has found to be ten years. However, the facts and circumstances surrounding the merger and acquisition cases cited in Mr. Ives' rebuttal testimony are quite different from the facts and circumstances that are unique to this transaction.

Q. Please explain.

A. Mr. Ives, at page five of his rebuttal testimony quotes my testimony in Case No. ER-2005-0436. In that case the Staff independently calculated fuel and purchase power savings (integration savings) from the joint dispatch of SJLP's and MPS' generation units to be in excess of the total $4.9 million in transition costs that Staff and Aquila agreed should be recovered.

1 In the transaction where Aquila acquired SJLP, Staff was able to make its proposal on
2 the appropriate transition cost recovery method based upon a showing that the actual net
3 integration synergies did exist and the amount of net synergies were well in excess of the total
4 approximately $5 million in transition costs that Aquila agreed to be recovered in rates.

5 The joint dispatch integration savings from Aquila's acquisition of SJLP in just one
6 year exceeded the total amount of transition costs in which it was seeking to recover
7 over 10 years. This fact lessened the concern that the combined costs of the post acquisition
8 Aquila and SJLP were greater than the costs of the pre-acquisition stand alone utilities.
9 These facts and circumstances are totally different from those now presented
10 by GPE's acquisition of Aquila.

11 Q. How were they different?

12 A. Unlike the evidence of the existence of a significant amount of net integration
13 synergies with Aquila's acquisition of SJLP, GMO has failed to provide until April 2, 2009
14 documentation of a synergy savings tracking mechanism on which the Staff and other parties
15 to this case could start an analysis of whether or not any net integration synergies actually
16 have occurred. The Staff notes that this recently received documentation is deficient and
17 does not meet the Commission's standard because it is based on estimated future costs, not
18 actual incurred costs.

19 The main facts in this case is that GMO's NFOM expenses have increased not
20 decreased, over the level of costs contained in the 2006 base year in the Commission's Order
21 in the Acquisition Case and GMO has not provided any evidence to the contrary.

22 Finally, Aquila agreed to seek recovery of less than $5 million in transition costs over
23 ten years. The potential harm from incorrectly concluding the actual existence of net

1 acquisition benefits in the Aquila – SJLP acquisition, which was $5 million over ten years is
2 significantly less than the risk in these rate cases where GPE will seek recovery on an
3 unspecified amount of transition costs possibly exceeding $50 million and is seeking to
4 recover these costs over a very short and unsupported five-year amortization period.

5 Q. Earlier you stated that the Staff has found ten years to be an appropriate
6 amortization period for transition costs. Does the Staff consider GMO's proposed five-year
7 amortization or recovery period to be excessively short?

8 A. Yes. If GMO wanted to amortize the transition costs on its books and records
9 for five years without seeking direct rate recovery, that would not be an issue. However, by
10 seeking direct rate recovery of the transition costs, as described above under the matching
11 principle, GMO is obligated to match the expense side of its income statement (amortization
12 of transition costs) with the revenue side (realization of integration synergy revenues).
13 Since GPE estimates that it will be able to achieve integration synergies over at least ten years
14 (GPE/KCPL Exh.37, Bassham Additional Supp. Direct p.3) then it should match its
15 amortization of transition costs over a minimum of a ten year period as well.
16 GMO's proposed five-year amortization period results in a significant mismatch between
17 anticipated savings and expenses.

18 Q. At page 6 of his rebuttal testimony, Mr. Ives list four reasons why he does not
19 agree with the indirect or natural regulatory lag recovery method proposed by Staff.
20 Please comment on each Mr. Ives' four concerns.

21 A. Mr. Ives' first concern is that reliance on regulatory lag to generate sufficient
22 revenues to cover transition costs "would in effect shift the burden for all of the costs to
23 achieve synergies (i.e. transition costs) to shareholders."

1 While I agree that the burden of transition cost recovery should be squarely placed on
2 GPE's shareholders until the existence of net acquisition benefits in rates is demonstrated to a
3 level satisfactory to the Commission, I disagree that this is what has occurred.
4 Mr. Ives' conclusion that GPE's shareholders would bear the entire burden of transition cost
5 recovery is wrong.

6 As noted above, if actual synergies are being realized, GMO and KCPL ratepayers are
7 paying dollars in current rates for a level of NFOM expenses that no longer exist and are
8 lower due to integration synergies. In actuality, these customers are bearing the burden of
9 paying higher utility bills based on higher costs than is actually being incurred by
10 GMO and KCPL in the hopes that eventually this prepayment of higher rates will lead to
11 future lower rates when the synergy savings are reflected in rates. Contrary to the concern
12 raised by Mr. Ives, it is not GPE's shareholder, but GMO and KCPL ratepayers who are
13 bearing 100 percent of the burden of transition cost recovery to the extent of an estimated
14 $48 million.

15 Q. Please continue with Mr. Ives' second concern that he believes the Staff's
16 position in this case is inconsistent with its position in other merger proceedings and rate
17 cases in which the Staff has provided testimony on transition cost recovery.

18 A. At page five of his rebuttal testimony Mr. Ives' describes Staff testimony in
19 two rate cases, Case Nos. ER-2005-0436 and ER-2001-672 and one merger case,
20 EM-2000-292. All three cases related to the recovery of transition costs incurred by Aquila
21 during the period it was integrating Saint Joseph Light & Power Company (SJLP) with its
22 MPS electric utility operations.

As described above, there was a strong indication of significant integration savings that resulted from Aquila's acquisition of SJLP in the area of fuel expense and purchased power expense. Significant cost savings were expected to be achieved as a result of the joint dispatch of Aquila's and SJLP's generation units. Fuel and purchased power savings in one year alone under joint dispatch was sufficient to cover the total amount of transition costs agreed upon by Staff and Aquila in Case No. ER-2005-0436.

As it relates to GPE's acquisition of Aquila, there is no joint dispatch of generation units and therefore no joint dispatch synergies. This is a potentially significant level of synergies that is not available to GMO's customers as it was to Aquila's customers.

This clear indication of potentially significant integration synergies was the reason why the Staff ultimately agreed to direct rate recovery of transition costs in the Aquila – SJLP acquisition. The fact for KCPL is that it has experienced significant cost increases not decreases since the acquisition. The total lack of evidence of any integration synergies in this case, and the absence of any potentially significant joint dispatch synergies, form the basis for the Staff's proposed regulatory lag recovery method for GPE to recover any integration synergies, if these synergies do, in fact, exist.

Unlike the portrayal by Mr. Ives in his rebuttal testimony, there is no inconsistency on the part of Staff on its position on transition cost recovery. Like most issues, the Staff makes its ratemaking recommendations to the Commission based on the facts and circumstances of each case.

Q. Explain why you believe that the Staff position on this issue as outlined in the testimony cited by Mr. Ives at page 5 of his rebuttal testimony and the Staff position in this case are consistent?

1 A. In my rebuttal testimony in Case No. ER-2001-0672 at page 33 I state that
2 transition costs are incurred after the merger in an attempt to run the combined utility more
3 efficiently. I also state, "If attained, these efficiencies should be reflected in a lower cost of
4 providing utility service, thereby providing a potential benefit to utility customers".
5 The Staff position taken in my rebuttal testimony in Case No. ER-2001-0672 concerning
6 recovery of transition costs contemplates the fact that actual integration savings have been
7 attained. I would certainly never recommend, and I do not believe the Staff would ever
8 recommend, rate recovery of transition costs in a utility rate case when there was not
9 convincing evidence that actual integration synergies have been achieved.

10 Significant portions of the transition costs at issue in this case were incurred before
11 GPE acquired Aquila. This is unusual. Prior to the transaction, these costs are normally
12 defined as transaction costs. Transition costs addressed by the Staff in other cases were
13 primarily incurred after the transaction closed and are directly related to the operation of the
14 entities after the transaction has been completed. The Staff found evidence that
15 savings existed as a result of the Aquila-SJLP acquisition in 2000, and as a result, the Staff
16 did recommend rate recovery of the transition costs to achieve these savings in rates in
17 Case No. ER-2005-0436.

18 Q. Please continue with Mr. Ives' third concern with the natural regulatory lag
19 approach the Staff is recommending for transition cost recovery in this case, that it was the
20 Commission's intention to allow the Company to defer transition costs and amortize these
21 costs over five years.

22 A. The Staff does not disagree that the Commission authorized a deferral of
23 transition costs to be amortized over a five year period in its Report and Order in

1 Case No. EM-2007-0354. However, the Staff disagrees with any interpretation of this
2 Report and Order that assumes, contradictory to express language in the ordered section of the
3 Report and Order, that the Commission authorized any type of ratemaking treatment.
4 The Commission's Report and Order specifically disproves Mr. Ives testimony.

5 Mr. Ives should recognize that the authorization of a deferral of transition costs
6 and a set amortization period was provided by the Commission so that the transition costs
7 could be deferred on GPE's books and records and the process of amortization could begin.
8 Once the transition costs were deferred, parties in subsequent rate cases would have the
9 opportunity to recommend the appropriate recovery methods for these costs. GPE entered into
10 the transaction to acquire Aquila with no assurance of any rate recovery of these costs unless
11 it could prove that the acquisition had produced savings to justify such recovery.

12 If GMO is not able to defer these costs on its books and records, it would have to
13 charge these expenses to income in the period in which they are incurred. The Commission
14 authorizes this same type of deferral authority all the time in accounting authority order
15 ("AAO") cases without authorizing any type of ratemaking treatment. AAOs granted in the
16 past to GMO and KCPL provided no guarantee of cost recovery from customers.
17 AAOs provide utilities with an opportunity to seek future rate recovery from customers and
18 nothing more. The Commission's exact same deferral authority granted in its
19 Acquisition Order granted an opportunity for KCPL to seek rate recovery of transition costs in
20 future rate cases, and nothing more.

21 Q. Please comment on Mr. Ives' fourth and final concern about the Staff's
22 proposed regulatory lag method of transition cost recovery.

1 A. Mr. Ives states that he believes the Commission acknowledged the "regulatory
2 lag" approach proposed by the Applicants was intended to provide the shareholders with an
3 ability to share in synergy savings before new rates are in place.

4 The Staff does not disagree at all with Mr. Ives' understanding of GMO's position and
5 how this position was characterized in the Commission's Acquisition Order. In fact, the Staff
6 is supportive of GMO's position as described by Mr. Ives, with just one exception.

7 Q. What is that one exception?

8 A. The Staff's proposal is that all of the benefits of the acquisition that have
9 accrued to GMO to date, all of the benefits that will accrue to GMO to September 2009, and
10 all future integration synergies that are achieved in between rate cases should be kept by
11 GPE's shareholders. It will be the responsibility of GPE's shareholders through
12 their representation by GPE's Board of Directors to encourage GPE management to attain a
13 level of integration synergies that first pays off the transition costs and then provides a
14 satisfactory level of profit to the shareholders.

15 The Staff's proposal is very similar to GMO's proposal except that it corrects
16 GMO's proposal by reassigning to GMO's shareholders the responsibility to pay down the
17 transition costs before they can enjoy the fruits of the acquisition. As I described earlier, a
18 business must pay expenses first before it can record profits.

19 The Staff agrees with Mr. Ives that it wasn't the Commission's predetermined intent
20 to use regulatory lag to recover transition costs because the Commission did not addresses any
21 appropriate ratemaking treatment in its Acquisition Order. The Commission did not say
22 whether regulatory lag was an appropriate mechanism or an inappropriate mechanism to
23 recover transition cost because it did not even address the appropriate ratemaking treatment

1 for recovery of transition costs. The Commission, appropriately so, left it to the parties in
2 future rate cases to put forth their proposal on transition cost recovery. That is what the Staff
3 is doing in this case.

4 Q. At pages 7-10 of his rebuttal testimony, Mr. Ives describes GMO's new
5 synergy savings tracking mechanism or the "Project Charter Synergy Tracking Mechanism."
6 Was this the synergy savings tracking process described by Mr. Ives in his direct testimony in
7 the case?

8 A. No. This is a completely new and different process. Mr. Ives' direct testimony
9 never mentioned the terms "Project Charter" and never addressed the new Phase 1 and Phase
10 2 tracking process he describes in his rebuttal testimony.

11 Q. Does the Staff have an opinion on the merits of the new tracking process?

12 A. Not at this point. The first time the Staff learned about this process was in
13 Mr. Ives' rebuttal testimony. However, the Staff will agree with Mr. Ives statements
14 at page 7 lines 8 and page 9 line 2 of his rebuttal testimony that because of the acquisition
15 closing in July 2008 it would be impossible to calculate any actual integration synergies
16 achieved in 2008 to compare to a base year 2006. This problem was created
17 by GPE's management in its decision to file four rate cases in Missouri less than two months
18 after the acquisition close date.

19 Q. Did GPE, GMO, or KCPL seek any waiver or variance regarding the
20 Commission's order in Case No. EM-2007-0374 respecting the requirement to implement a
21 synergy tracking system using a 2006 base year?

1 A. No. GMO just failed to comply with the Acquisition Order and decided to
2 substitute a different approach without consultation with the parties or Commission approval
3 to do so.

4 Q. At page 8 of his rebuttal testimony, Mr. Ives states that the new tracker
5 compares actual results to the 2006 base year, adjusted for known and measurable changes,
6 including inflation. Has KCPL ever provided to Staff any synergy savings tracking reports
7 that compare actual costs incurred with 2006 base year costs?

8 A. No. Staff, despite several attempts to obtain this data, has never been provided
9 any synergy savings tracking report that compares base year 2006 results with actual incurred
10 costs.

11 As noted in my rebuttal testimony on this issue, because of the number of assumptions
12 made to increase 2006 base year costs and the sheer volume of data required to be reviewed
13 and analyzed, it would take two Staff auditors approximately 45 to 60 audit work days
14 working solely on this issue to reach a conclusion about whether or not it was likely that any
15 actual integration synergies have been realized and provide an estimate of the approximate
16 size of the integration synergies if it was concluded that, any were in fact, realized.

17 Q. Above you reference where the Commission ordered GPE to implement a
18 synergy savings tracking mechanism as described by the Applicants and as described in the
19 body of the Commission Acquisition Order. How did the Applicants describe the synergy
20 savings tracking mechanism and did they commit to doing one?

21 A. In the Supplemental Direct Testimony provided by Terry Bassham in Case No.
22 EM-2007-0374 at pages 6 and 7, he committed to the Commission that Great Plains Energy
23 would track synergy savings that have actually been achieved. On pages 6 and 7, he stated:

1 If the Commission so desires, Great Plains Energy is willing to
2 track synergy savings achieved. The synergies achieved can be
3 compared to the transaction and transition cost amortization and
4 to the extent the synergies do not cover the amortization, the
5 cost would continue to be deferred until such time that the
6 demonstrated savings from the merger exceeds the related cost.

7 Q. How does GPE define "synergy savings" as it relates to the GPE-Aquila
8 acquisition?

9 A. At page 3 of his direct testimony Mr. Ives defines synergies as "a reduction in
10 costs, and avoided costs, as a result of the operational integration of utility operations
11 of GMO and KCPL as compared to the combined costs of the entities operating standing
12 alone absent the operational integration.

13 Q. At page 10 of his rebuttal testimony Mr. Ives makes the statement
14 that GPE does not believe that the 2006 baseline tracking mechanism was intended to
15 specifically provide the value of synergy savings to be flowed through to customers in the
16 ratemaking process. Do you agree?

17 A. No. The portions of the Commission's Acquisition Order cited in his
18 testimony to support this belief do not even reference a synergy savings tracking mechanism.
19 The Staff believes the more appropriate references in the Commission's Acquisition Order
20 which support its position that GPE must prove the existence of actual synergies achieved
21 using the tracking mechanism and the 2006 base year as follows:

> 245. If the Commission requires synergy tracking, the Applicants suggest a simple approach, noting that additional complexity does not improve accuracy. The Applicants suggest establishing base period costs and then comparing each subsequent year's actual costs to the base year costs, as adjusted for inflation. The net decrease in expense would be considered synergy savings. (Emphasis added; Footnote omitted).
>
> 247. Applicants recommend 2006 as the base year for synergy savings tracking because that year represents the last full year of operations unaffected by the merger. It is also the test period for Aquila's most recent rate case, Case No. ER-2007-0004, and the test period of KCPL's most recent rate case, Case No. ER-2007-0291. Consequently, the base year of 2006 provides a good test period for both Aquila and KCPL to evaluate synergy savings to be accomplished as a result of the merger. (Footnote omitted).
>
> IT IS ORDERED THAT:
>
> 6. Authorization of the transactions described in Ordered Paragraphs Number One through Five are subject to the following conditions:
>
> c. Great Plains Energy, Incorporated, Kansas City Power & Light Company, and Aquila, Inc., shall, upon closure of the authorized transactions, implement a synergy savings tracking mechanism as described by the Applicants, and in the body of this order, utilizing a base year of 2006. (Emphasis added)

The Staff believes that a correct interpretation of the Commission's Acquisition Order is that the Commission ordered GPE to implement a synergy savings tracking mechanism and use 2006 to establish a base year level of expenses. As GPE incurs actual costs in subsequent years, it is required to compare the actual costs incurred to the 2006 base year level to determine if any integration synergies exist, and if they exist, do they exceed the level of transition costs proposed to be passed on to ratepayers.

If and when GMO demonstrates through this Commission-mandated tracker that actual synergies, the net decrease in NFOM expenses comparing a year's actual cost to the

1 base year costs, exceed transition costs, then GMO can propose rate treatment for the
2 transition costs in a rate case. This is the basis on which the Commission determined that if
3 the synergies did not exceed the transition costs, GPE committed to not seek recovery of the
4 transition costs and thus no ratepayer detriment would occur.

5 Q. At pages 12 of his rebuttal testimony Mr. Ives tries to justify the reasons why
6 KCPL is increasing its 2006 base year expenses by $93 million. Please comment on this
7 adjustment.

8 A. As stated earlier, when GPE eventually completes its 2006 base year synergy
9 savings tracking mechanism, this $93 million adjustment in one of the reasons why an audit
10 of GPE's tracking mechanism will require so much time. This Staff has been advised that this
11 $93 million has adjusted to $86 million.

12 Q. While the Staff may have concerns about what costs and factors are included in
13 the $93 million that GPE is proposing be added to the 2006 base year costs, does it also have
14 concerns with what GPE excluded from its $93 million adjustment?

15 A. Yes. What is of serious concern to the Staff at this point is that GPE has not
16 included in its analysis any efficiency gains or other cost savings measures that have occurred
17 by the stand alone GMO and by the stand alone KCPL. The Companies' analysis concludes
18 that no efficiency gains of any type would have been realized by the stand alone entities.
19 Such an omission in the calculation of the $93 million adjustment does not speak well of the
20 management efficiency of GPE, GMO, or KCPL.

21 Q. Please explain what you mean by efficiency gains.

22 A. By efficiency gains I am referring to reduction in expenses caused by things
23 such as improvements in technology, design of more efficient work processes, and more

1 effective and efficient employment of human capital. For example, in recent years Aquila put
2 a very strong emphasis on process improvement and cost reductions through its Six Sigma
3 Program.

4 Six Sigma is a management philosophy developed by Motorola that emphasizes
5 setting extremely high objectives, collecting data, and analyzing results to a fine degree as a
6 way to reduce defects in products and services. The Staff became aware in recent Aquila rate
7 cases and the acquisition case that Aquila was expecting significant cost savings in future
8 years as a result of changes that will be put in place by the Six Sigma Program.

9 These costs savings that Aquila was creating and planned to create in the future as a
10 stand alone entity were completely ignored by GPE's calculations of adjustment to 2006 base
11 year costs. Further, GPE, GMO and KCPL do not use Six Sigma and instead use an informal,
12 unspecified internal process to attempt to introduce productivity into its operations.
13 The abandonment of Aquila's formal Six Sigma Program is likely to lead to higher, not lower
14 costs than Aquila could achieve on a stand-alone basis.

15 Q. What is the effect of not including efficiency gains in the adjustments
16 to 2006 base year stand alone costs of GMO and KCPL?

17 A. The effect is that without appropriate adjustments to help offset some of the
18 $93 million in cost increases GPE is adding to its 2006 base year level of stand alone costs,
19 any calculation of integration synergies will be overstated. .

20 Q. Why is it critical to any attempt to calculate integration synergies that actual
21 costs incurred post-acquisition, which represents the costs of the combined entity,
22 be compared with pre-acquisition costs?

1 A. Assuming that integration synergies can be tracked with any degree of
2 accuracy, which is a highly debatable assumption, the only way to track synergies is to
3 compare total costs of a combined company with previously established costs of the two stand
4 alone companies. This comparison has to be done on a total, not a piecemeal basis to obtain
5 any meaningful results.

6 GMO has to date failed to complete a comprehensive total cost analysis and has
7 instead relied on a completely inadequate piecemeal process of calculating integration
8 synergies. Mr. Ives, who is sponsoring GMO's integration savings adjustment in this case has
9 admitted in his rebuttal testimony that an actual costs savings calculation cannot be done.
10 What he has chosen to do instead is to look at specific and isolated purported costs reductions,
11 such as reduced employee levels salaries and benefits, reduced insurance premiums and
12 reduced facilities ownership costs. What he has failed to include in this assessment is any
13 analysis comparing GMO and KCPL on items such as procurement policies, employee and
14 officer expense account policies, salary levels, employee benefits, medical insurance, other
15 postretirement benefits, supplemental pension benefits and a host of other costs. All of these
16 items, the effect of which would be reflected in an analysis of actual 2006 base year costs
17 compared to actual post-acquisition costs, are not being considered in Mr. Ives' piecemeal
18 approach to calculating integration synergies.

19 Q. Does the Staff believe integration synergies can be accurately tracked?

20 A. No. My experience has shown that there is no effective method for tracking
21 acquisition/merger-related synergy savings and thus comparing those savings
22 to merger-related transition costs is a contrived process at best. GPE's testimony in the
23 Acquisition Case and the Commission's Acquisition Order acknowledges the same fact.

1 I do believe that under the right circumstances a methodology for tracking
2 acquisition-related synergy savings can be accepted by parties impacted by a transaction
3 based upon unique and specific facts and circumstances.

4 The primary reason I have rejected the notion of tracking acquisition synergy savings
5 is that GPE has failed to comply with the Commission's Acquisition Order and produce
6 documentation that shows the existence of actual integration synergies. GPE, GMO and
7 KCPL have made no effort to engage in collaborative processes to attempt to build a
8 consensus of agreement regarding how this synergy savings tracking mechanism could be
9 employed. It is my experience that the former Aquila Regulatory Department employees
10 would have sought input from the parties before it attempted such an endeavor. As described
11 above, this failure on the part of GPE is a direct result of the fact that it filed four Missouri
12 rate cases within two months of the closing date of the acquisition.

13 Because of its timing of the filing of this rate case, which was completely at the
14 discretion of GPE, GPE was unable to produce any document that even purports to show that
15 lower costs actually exists and was the result of GPE's acquisition of Aquila. The Staff has
16 explained in detail why natural regulatory lag is the best option for the Commission to allow
17 recovery of transition costs in this case.

18 **SJLP SUPPLEMENTAL EXECUTIVE RETIREMENT PLAN (SERP)**

19 Q. At page 5 of her rebuttal testimony KCPL witness Barbara Curry states that a
20 SERP is designed to make individuals whole whose compensation is in excess of federal tax
21 law limits. Does GMO have a history of using its SERP to pay executive bonuses and other
22 executive perquisites?

1 A. Yes. GMO's executive SERP bonus payments and credits and other change in
2 control accelerated SERP benefits have been contested issues in prior GMO rate cases,
3 including its most recent rate case, No. ER-2007-0004.
4 Q. At page 6 of her rebuttal testimony Ms. Curry states that she agrees with your
5 SERP rate case adjustment for GMO-MPS, but not for GMO-L&P. Why does she agree with
6 your GMO-MPS SERP adjustment?
7 A. She agrees because I included GMO-MPS's annualized test year level
8 of SERP expense. This SERP expense meets the Staff's requirements of inclusion in cost of
9 service.
10 Q. What are the Staff's requirements for inclusion of SERP expense in cost of
11 service?
12 A. The Staff's requirements have been, and continue to be, that it will recommend
13 SERP costs be included in a utility's cost of service if 1) they are not significant, 2) they are
14 reasonable and only include the amount that would have been accrued by the employee as
15 pension credits absent the IRS compensation limitations, and 3) the expenses can be
16 quantified under the known and measurable standard.
17 The first requirement is that SERP costs should not be significant. It is an additional
18 benefit plan, not a primary benefit plan. Second, the SERP payment must be reasonable,
19 which means that it should include only a dollar benefit that would exist and be paid under the
20 normal pension plan absent the Internal Revenue Service (IRS) compensation limits.
21 Third, SERP payments must also meet the known and measurable standard, which means they
22 must be normal, recurring costs that are known to occur and be capable of being measured
23 with a high degree of accuracy.

Q. Why does Ms. Curry not agree with your SERP adjustment for GMO-L&P?

A. At page 6 line 14 of her rebuttal testimony she states that I offer no support for my contention that there are sufficient assets to satisfy GMO's SERP obligations to former executive officers of Saint Joseph Light & Power Company (SJLP). In 2000, GMO, then known as UtiliCorp United, Inc., acquired SJLP and severed, with the payment of very lucrative compensation packages, SJLP's executive officers.

Q. Would you please describe the origination of this L&P executive SERP fund?

A. GMO, when named UtiliCorp United, Inc., filed a joint proxy statement/prospectus, Form S-4 with the Securities and Exchange Commission (SEC) on May 4, 1999. In this document SJLP and GMO explained the terms and conditions of the acquisition of SJLP by UtiliCorp. In the section below, the joint parties explained that SJLP would contribute approximately $2 million to a trust to meet its (SJLP's) obligations to its executive officers who were about to be unemployed when the merger closed. The pertinent part of that joint proxy statement/prospectus, Form S-4 follows:

> **ST. JOSEPH'S LONG-TERM INCENTIVE PLANS AND SUPPLEMENTAL EXECUTIVE RETIREMENT PLAN.**
>
> Messrs. Steinbecker, Stoll, Myers, Stuart and Svuba are participants in St. Joseph's 1994 Long-Term Incentive Plan (the "1994 Plan"), St. Joseph's 1998 Long-Term Incentive Plan (the "1998 Plan") and St. Joseph's Supplemental Executive Retirement Plan (the "SERP").
>
> Under the 1994 and 1998 Plans, the executives can earn certain performance-based restricted stock awards. Upon a shareholder vote approving a change of control of St. Joseph, the executive is entitled to receive all awards available to him under the 1994 Plan, whether or not earned (computed based on St. Joseph's actual performance through the date of the shareholders' vote), all vesting requirements are immediately accelerated and all restrictions on the awards are eliminated.

> Upon the closing of a transaction involving a change of control of St. Joseph, each executive is entitled to receive all awards available to him under the 1998 Plan, whether or not earned (computed as though St. Joseph's performance was at the maximum potential level), all vesting requirements are immediately accelerated and all restrictions on the awards are eliminated.
>
> On or prior to the completion of the merger, St. Joseph will contribute approximately $2 million to trusts to meet its obligations to the executives under the SERP. Under each of the 1994 Plan, the 1998 Plan and the SERP, the merger will constitute a change of control of St. Joseph. (Emphasis added)

Q. How would you characterize this $2 million funding of the SERP fund by SJLP prior to the closing of the merger, as an obligation of SJLP or of GMO?

A. I would characterize this funding as an obligation of SJLP. This was a pre-merger obligation of SJLP, and not an obligation of GMO. GMO made and make SERP payments to the former SJLP executives out of the fund that SJLP paid for before the merger of SJLP and GMO.

Q. What is the Staff's position on GMO's inclusion of these SERP payments in GMO's revenue requirement for L&P?

A. It is Staff's position that since the obligation to pay future SERP expenses to the former SJLP executives was satisfied by SJLP before its merged with GMO, this obligation has never been an obligation of GMO.

Q. If GMO were obligated to fund and distribute to former SJLP executives these SJLP severance SERP payments, would the Staff support rate recovery of these payments?

A. No. If that were the case, which it is not, the Staff asserts that SJLP ratepayers already contributed the funds used to make these SERP payments and until these funds are exhausted, there should be no additional recovery of these SERP payments from GMO ratepayers.

1 Q. What annual level of SERP expense is GMO seeking to include in cost of
2 service for L&P?
3 A. This amount is $303,780.
4 Q. Is MPS a significantly larger utility than L&P?
5 A. Yes.
6 Q. Then is it noteworthy that GMO is proposing to recover from L&P ratepayers
7 SERP expense of $303,780 which is over seven times greater than
8 the $39,751 GMO is proposing to recover from MPS ratepayers?
9 A. Yes, Staff finds it unusual.

10 **ACQUISITION DETRIMENT-PREMATURE RETIREMENTS**

11 Q. At page 5 of his rebuttal testimony GMO witness Ron Klote describes the
12 Staff's position on plant retirement accounting for plant that was retired as a result
13 of GPE's acquisition of GMO. GMO witness Ives also addresses this issue in his rebuttal
14 testimony and stated that the Staff did not fully explain Staff's rationale for this adjustment in
15 direct testimony. Please explain this issue and address Mr. Ives' concern by explaining the
16 rationale for the Staff's position.
17 A. In my testimony in the Staff's Cost of Service Report, I explained how the
18 Staff takes issue with MPS' accounting for certain assets that were retired as a result of its
19 acquisition by Great Plains Energy. As a result of integrating the operations
20 of GMO and KCPL, GMO used normal plant retirement accounting to retire computer
21 software and hardware plant that has not been fully depreciated.
22 Q. Should normal plant retirement accounting be used for plant that was
23 prematurely retired as a consequence of GPE's acquisition of Aquila?

1 A. No. Under normal plant retirement accounting, the original cost of the plant is
2 removed from the plant accounts and the same dollar amount (original cost of the plant
3 retired) is removed from the associated plant reserve account. However, the plant retirement
4 that is in question was not a normal retirement. It was a premature, extraordinary retirement
5 that was made as a direct consequence of GMO being acquired by GPE.

6 The loss in the case of GMO's premature retirement of GMO's computer software and
7 hardware plant is a loss created by the acquisition and needs to be treated as an acquisition
8 detriment. The appropriate ratemaking treatment is for GMO to only remove the actual
9 amount of depreciation expense on this plant that was charged to the reserve. This loss on
10 premature retirement of plant can be treated below-the-line for ratemaking purposes.

11 Q. When a plant is prematurely retired, does it create a loss and cause a plant
12 reserve deficiency?

13 A. Yes. For example, if a plant with an original cost of $1,000 and an
14 accumulated depreciation reserve balance of $700 was retired prematurely, the journal entry
15 to record this event would be

Line	Account	Debit	Credit
16	Plant Depreciation Reserve	700	
17	Loss on Plant Retirement	300	
18	Plant in Service		1,000

19

20 The loss, and reserve deficiency created as a result of GMO's premature retirement of
21 computer software and hardware plant is a loss created by the GPE acquisition and has to be
22 treated as an acquisition detriment. The Staff believes the appropriate ratemaking treatment
23 would be for GMO to only remove the actual amount of depreciation expense on this plant
24 ($700 in this example) that was charged to the reserve. This loss on retirement and reserve
25 deficiency can be treated below-the-line for ratemaking purposes.

1 Q. How would the journal entry to record the event be made under GMO's
2 proposed treatment?
3 A. The journal entry would not result in a gain or loss, because the same dollar
4 amount is being removed from both the plant and reserve accounts. The journal entry would
5 be:

6 Plant Reserve	1,000	
7 Plant in Service		1,000

8
9 This entry results in an acquisition detriment in this rate case since the plant reserve,
10 which represents past recoveries of plant investment through depreciation expense,
11 is prematurely reduced due to GPE's acquisition of Aquila. If more accrued depreciation
12 expense is removed from the reserve account than justified by normal utility plant retirements,
13 then the rate base is artificially inflated and customers have to pay more than they otherwise
14 would be required under normal, not premature accounting.
15 Q. Does the FERC USOA provide various options for GMO to record costs
16 incurred as a result of its being acquired by GPE?
17 A. Yes. These costs are not normal costs and must be segregated from normal
18 costs. The FERC USOA, as well as generally accepted accounting principles have specific
19 rules for costs incurred in a merger or acquisition. For example, a cost incurred as a result of
20 a merger or acquisition could be recorded in plant acquisition adjustment accounts,
21 or extraordinary retirement accounts, or general category accounts, such as will be described
22 below.
23 Q. How does the FERC USOA provide guidance for utilities to account for
24 unrecovered costs (which can be defined here as the amount of the plant removed from the

1 plant accounts less the amount of depreciation reserve that was accrued on this plant and
2 reflected in the reserve account) plant costs that have been prematurely retired?

3 A. The FERC USOA required that these costs be recorded in FERC account
4 182.3, Unrecovered plant and regulatory study costs. The FERC USOA definition of this
5 account is:

6 **182.2 Unrecovered plant and regulatory study costs.**

7

8 A. This account shall include: (1) Nonrecurring costs of
9 studies and analyses mandated by regulatory bodies
10 related to plants in service, transferred from account
11 183, Preliminary Survey and Investigation Charges,
12 and not resulting in construction; and (2) when
13 authorized by the Commission, significant unrecovered
14 costs of plant facilities where construction has been
15 cancelled **or which have been prematurely retired.**
16 (Emphasis added)

17

18 B. This account shall be credited and account 407,
19 Amortization of Property Losses, Unrecovered Plant
20 and Regulatory Study Costs, shall be debited over the
21 period specified by the Commission.

22

23 C. Any additional costs incurred, relative to the
24 cancellation or premature retirement may be included
25 in this account and amortized over the remaining period
26 of the original amortization period. Should any gains or
27 recoveries be realized relative to the cancelled or
28 prematurely retired plant, such amounts shall be used to
29 reduce the unamortized amount of the costs recorded
30 herein.

31

32 D. In the event that the recovery of costs included herein is
33 disallowed in the rate proceedings, the disallowed costs
34 shall be charged to account 426.5, Other Deductions, or
35 account 435, Extraordinary Deductions, in the year of
36 such disallowance.

37 Q. At page 5 of his rebuttal testimony GMO witness Mr. Klote states that the cost
38 to be recovered from ratepayers as a result of the Company's accounting for the retirements is

1 the same as the cost that would have been recovered from ratepayers had the acquisition not
2 occurred and the assets not retired. Please comment.

3 A. Mr. Klote does not explain why he believes this statement to be true but he
4 does refer to the rebuttal testimony of GMO witness Mr. Ives. At page 16 of his rebuttal
5 testimony, Mr. Ives states that the net reduction in the reserve account is the same as the
6 remaining depreciable value of the plant at retirement. This statement does not appear to be
7 consistent with his description of how the accounting journal entry to record this event should
8 be made, which, as I explained in my example above, removes the historical cost of the plant
9 from both the plant account and the reserve account. The method he proposes at page 17 line
10 5 does not decrease the reserve account by the net depreciable value, but by the full original
11 cost of the plant. Basically Mr. Ives recognizes that a reserve deficiency will be created by
12 this retirement transaction, but his solution is that it can be fixed in future years when a new
13 depreciation study is done. However, this will be too late. If GMO prevails on this issue,
14 rates in this case will reflect a inappropriately lower depreciation reserve and therefore a
15 higher rate base. The Staff thinks the correction should be made now.

16 **ACQUISITION DETRIMENT-DEPRECIATION RATES**

17 Q. At page 2 of this rebuttal testimony, GMO witness Mr. Klote, supports no
18 change in depreciation rates until completion of the significant capital project of the building
19 of Iatan 2 coal fired generation facility and that the Company perform a Great Plains Energy
20 system-wide depreciation study conducted on all KCPL and GMO assets. Mr. Klote takes
21 this position despite the fact the Staff, through the depreciation study of Rosella Schad,
22 and GMO's own depreciation witness, Ron White, has found that GMO's current depreciation
23 rates are too high. Please comment.

1 A. It appears that the delay in the implementation of appropriate depreciation rates
2 for GMO plant accounts is being driven by GPE's acquisition of GMO. Since absent the
3 acquisition GMO would not be able to support a delay in the implementation of new
4 depreciation rates, GMO's ratepayers could be harmed because of the acquisition if
5 implementation of the appropriate depreciation rates is delayed. If GMO prevails on the
6 depreciation issue in this case, this will result in an acquisition detriment.

7 Q. What would be an appropriate way to address this acquisition detriment?

8 A. The Staff recommends that if the Commission adopts GMO's position on this
9 issue, that the difference in utility rates paid by GMO's ratepayers as a result of the delay in
10 implementing appropriate depreciation rates verses what those utility rates would be if
11 appropriate depreciation rates were implemented in this rate case, be applied as a reduction to
12 any acquisition synergy calculation made by GMO, if the Commission approves any
13 acquisition synergy calculation in this case. Since the acquisition will result in higher costs
14 through higher depreciation expense, it would be appropriate to offset this increased expense
15 by the same dollar amount of any acquisition synergies, should the Commission find that any
16 synergies have been measured and tracked appropriately.

17 **CAPACITY – CROSSROADS ENERGY CENTER**

18 Q. At page 4 of his rebuttal testimony, GMO witness Burton Crawford states that
19 the Staff did not conduct its own analysis that demonstrates GMO should have built 5 CTs.
20 Please comment.

21 A. It is not the responsibility of the Staff to do a utility's resource planning
22 analysis. This responsibility falls on the management of the company. The Staff does review
23 these resource planning documents and has discussions with utility management of these

planning documents, but it does not create them. The analysis that was performed for GMO's capacity needs in 2005 was made by GMO management. GMO's management determined in 2004 or earlier that it was the least cost option of providing capacity to its customers by 2005, but acted in an imprudent manner by not following through on this least cost plan. The end result of this imprudent decision is that GMO is now trying to force higher capacity costs on to its customers. The Staff, in its testimonies in this case, is explaining to the Commission how these higher imprudent costs were incurred and why these costs of imprudent management decisions should not be charged to customers.

Q. Also at page 4 of his rebuttal testimony Mr. Crawford states that the Commission never ruled on this capacity planning issue. Please comment on this statement.

A. The only reason the Commission has never specifically ruled on this issue in a rate case order is that is that GMO's last two rate cases settled. One reason they settled on an overall revenue requirement is that the Staff's position of imputing the cost of Prudent CTs #4 and #5 which increased GMO's revenue requirement by a significant amount in comparison to the purchased power agreements GMO included in its revenue requirement.

Q. At pages 5 and 6 of his rebuttal testimony GMO witness Mr. Crawford says that the basis of the GMO's management decision not to select the lowest cost resource plan was because it was trying to limit its exposure to potentially future high natural gas prices. Please comment.

A. GMO did not rely on the least cost planning option based on expected natural gas prices. Instead, according to Mr. Crawford, it decided to forego the least cost planning option for capacity on the chance that its natural gas price forecasts were too low. If this was in fact the basis for GMO's decision, the Staff does not believe is was a prudent and

1 reasonable decision. There are other ways GMO could have mitigated the risk of future
2 higher natural gas prices through the myriad of natural gas hedging options available in the
3 marketplace. With all these options available, the decision to incur certain higher capacity
4 costs due to the potential for higher natural gas prices is not prudent. Staff witness
5 Lena Mantle describes in her surrebuttal testimony how GMO's decision to incur higher
6 capacity costs did not result is less exposure to natural gas price changes.

7 Q. At page 8 of his rebuttal testimony Mr. Crawford describes why he believes
8 that the 100MW capacity contract included in the Staff's revenue requirement is not
9 reasonable. Is he correct?

10 A. No. To cover its short-term capacity needs until the Iatan 2 plant comes on
11 line next year, the Staff included in its revenue requirement the pro rata share
12 (100 MW/308 MW) of the actual contract price that GMO paid for this capacity in the test
13 year.

14 If GMO's management had acted prudently and actually implemented its least cost
15 capacity plan in 2005, it would currently have a need for a short-term 100 MW capacity
16 contract. To meet this requirement, the Staff used the prices of a capacity contract in effect
17 for GMO in the test year. If GMO did not think the cost of this capacity included in the Staff
18 revenue requirement was sufficient, it has not made Staff aware of this fact. The Staff
19 included GMO's actual test year capacity cost for this 100 MW of capacity.

20 Q. At page 9 of his rebuttal testimony GMO witness Mr. Crawford states
21 "The Staff has been critical of the Company's reliance on purchased power agreements for
22 several years, but yet they impute a 100 MW capacity contract even though the Company has
23 demonstrated that the Crossroads Energy Center is projected to be the lowest cost ownership

1 from a NPVRR perspective while meeting the Company's capacity needs." Please comment
2 on this statement.

3 A. This statement includes two points that need to be addressed. First, the Staff has
4 said in testimony that it believes that at certain times the use of short-term capacity contracts
5 is appropriate. They are an appropriate tool for a utility to use to meet its long-term
6 least-cost capacity plans. The problem the Staff has had with GMO management for several
7 years is not the appropriate use of short term capacity contracts, but GMO's continued
8 reliance on these short-term capacity contracts to meet its capacity needs.

9 This refusal by GMO to put regulated plant "steel in the ground" in Missouri to meet
10 its capacity needs on the lowest long-term cost to its customers is the issue. By its continued
11 reliance on short-term capacity contracts, which are more costly in the long-run than adding
12 plant in service to rate base, GMO has unnecessarily and imprudently increased its cost of
13 providing utility service. The portion of this cost of service that is imprudent should not be
14 passed on to customers, but retained by GMO's shareholders.

15 The second point raided by Mr. Crawford is that the Crossroads Energy Center was
16 projected to be the least cost capacity for GMO in 2008. This point is totally irrelevant to this
17 issue. This issue is not about what GMO's least cost option is in 2008, but what the least cost
18 option was in 2004. If the Staff agreed with Mr. Crawford and accepted GMO's least cost
19 option in 2008, it would be agreeing to force GMO's regulated Missouri customers to absorb
20 millions of dollars of imprudently incurred costs. The Staff will not do so.

21 Q. The difference in revenue requirement between including the capacity through
22 Prudent CTs 4 and 5 plus a 100 MW purchased power agreement and the Crossroads Energy
23 Center is about $12 million on an annual basis, excluding the impact of capital structure and

1 equity cost differences between GMO and the Staff. What some of the reasons why the cost
2 of the Crossroads plant is so much higher than the cost of including Prudent CTs 4 and 5 in
3 GMO's rate base?

4 A. This $12 million represents the annual cost of the former GMO management's
5 imprudent capacity planning decisions that current GMO management is trying to charge to
6 its regulated customers. Staff witness Cary Featherstone will address the differences in the
7 cost of the combustion turbines in his surrebuttal testimony in this case. The CT valuation
8 difference is the most significant portion of this $12 million. In addition to the significant
9 differences in the cost of the combustion turbines, because the Crossroads Energy Center is
10 located in Mississippi, it requires approximately $20 million additional transmission plant
11 than Prudent CTs #4 and #5, located in Cass County, Missouri. Not only does the plant's
12 location in Mississippi require an additional $20 million in additional plant, but the
13 requirement to get the electricity generated in Mississippi to Missouri requires an additional
14 $3.8 million in annual transmission expense.

15 Another factor contributing to the $12 million difference in revenue requirement
16 between GMO and the Staff is the fact that, although it has recorded accumulated deferred
17 income taxes on the Crossroads Energy Center since GMO built the facility in 2002,
18 GMO is only willing to include a small portion of these deferred taxes in GMO's rate base.
19 I will address this issue later in my surrebuttal testimony.

20 Q. At page 10 of his rebuttal testimony Mr. Crawford discusses the Commission's
21 Affiliate Transaction Rule. He quotes 4 CSR 240-20.015(2)(A) which describes the
22 prohibition against utilities providing a financial advantage to an affiliated entity. The rules
23 requires that a utility shall not compensate an affiliate for goods and services above the lesser

1 of the fair market price or the fully distributed cost to the utility to provide the goods or
2 services for itself. Did GMO transfer the Crossroads Energy Center from an affiliated
3 company to the regulated utility at a price above the fair market value, in apparent violation of
4 the Commission's affiliate transaction rule?

5 A. Yes, it did. A history of the ownership of the Crossroads Energy Facility is
6 included as Schedule 2 to this testimony. As I explained in detail in my rebuttal testimony in
7 this case, strong support exists that the fair market value of the Crossroads Energy Center was
8 significantly lower than its recorded net book value. GPE management's conclusion when it
9 placed a $51.6 million value on the Crossroads Energy Center prior to its acquisition of this
10 asset confirmed the validity of this support. Despite the support that the net book value of the
11 Crossroads Energy Center was significantly overstated, it remained on Aquila's balance sheet
12 at net book value. GPE management, however, reported to its stockholders and the Securities
13 and Exchange Commission in 2007 that it would likely have to write down the value of
14 Crossroads Energy Center from its net book value of $117.9 million to a fair market value of
15 $51.6 million.

16 Based on the support I describe above and the support in my rebuttal testimony, there
17 is a concern that GMO violated the Commission's Affiliate Transaction Rules by transferring
18 the Crossroads Energy Center from its unregulated affiliate to MPS at net book value.

19 Q. At page 13 of his rebuttal testimony GMO witness Mr. Crawford describes
20 how Great Plains Energy hired an outside accounting firm, Pricewaterhousecoopers (PwC)
21 to do determine the value for financial statement purposes of the Crossroads Energy Center.
22 This study was performed in accordance with the requirements of Financial Accounting

1 Standards No. 141, Business Combinations, (FAS 141). Have you reviewed this study as it
2 pertains to the Crossroads Energy Center?
3 A. Yes, I have. In addition I have reviewed the workpapers provided in response
4 to data request No. 179 that support this study.
5 Q. What is your opinion as to the results of this study?
6 A. The purpose of this study was not to determine the historical cost to
7 Great Plains Energy of the Crossroads Energy Center, but simply what value to assign to this
8 asset, as a regulated rate base asset, for financial reporting purposes. The study tries to
9 appropriately allocate the total price Great Plains Energy paid to acquire Aquila's assets to the
10 specific tangible and intangible assets acquired in accordance with generally accepted
11 accounting principles (GAAP), primarily FAS 141. The historical cost of Crossroads Energy
12 Center was previously determined by Great Plains Energy's management in its due diligence
13 review of the Aquila assets it was purchasing. In determining how much money it would pay
14 to Aquila to purchase Aquila's assets, including the Crossroads Energy Center, Great Plains
15 Energy's management determined that the fair value of the Crossroads Energy Center was
16 $51.6 million. This PwC valuation was not performed until after Great Plains Energy
17 acquired Aquila and after the fact that Great Plains Energy decided to include the Crossroads
18 Energy Center in rate base in this case.
19 Q. Was the fact that Great Plains Energy's management told PwC that it intended
20 to put the Crossroads Energy Center in GMO's rate base in this rate case influence,
21 to a significant degree, the value that PwC placed on the Crossroads Energy Center?
22 A. Yes. This is the reason why PwC placed the value it did on the Crossroads
23 Energy Center. Therefore, the PwC valuation cannot be used as support for the appropriate

1 historical cost amount to place on the Crossroads Energy Center to include in GMO's rate
2 base. It is nothing more than an "after the fact" valuation influenced by the fact that, since the
3 plant was going to be included in a regulated rate base, a certain amount of revenues to
4 recover the plant's costs will be guaranteed.

5 Q. Is the PwC study on the value of the Crossroads Energy Center a
6 comprehensive study?

7 A. No. The fact that Great Plains Energy advised PwC that it intended to include
8 the Crossroads Energy Center in a regulated rate base, it limited the type of work PwC was
9 required to do to determine a financial statement fair value. The study may be perfectly
10 adequate for its intended purpose; however it is not a comprehensive study on the fair market
11 value of the Crossroads Energy Center. The valuation portion of the study primarily consists
12 of a simple mathematical calculation. PwC just took the ** recorded construction cost of the
13 plant, grossed up this construction cost for inflation and decreased this calculated amount by
14 an estimated amount of depreciation expense. ** This PwC analysis is attached
15 as a Highly Confidential Schedule 3 to this testimony, and the supporting workpapers are
16 attached as Highly Confidential Schedule 4.

17 Q. Please address the rebuttal testimony of GMO witness Melissa Hardesty
18 concerning the reasons why GMO is withholding approximately $12 million of the
19 total $13.4 million of the accumulated deferred income taxes that are directly assignable to the
20 Crossroads Energy Center.

21 A. At page 3 of her rebuttal testimony she states: "The deferred taxes related to
22 these units prior to the transfer to GMO-MPS were never a prepayment of income taxes by
23 GMO-MPS's customers or any other customer in a regulated environment.

NP

1 Therefore, the Company does not believe that it is appropriate to reduce its rate base for these
2 deferred taxes."

3 The statement that the deferred taxes related to the transfer were never a prepayment
4 of income taxes by GMO's customers is a correct factual statement. Her statement that this is
5 an appropriate reason to exclude these deferred taxes from GMO's rate base is totally
6 inconsistent with GMO's position on including the net book value of the Crossroads Energy
7 Center in GMO's rate base. This position is not only inconsistent with GMO's overall
8 position on including the net book value of this plant in rate base, but is also reflects a bias on
9 the part of GMO to favor its shareholders to the detriment of its ratepayers.

10 Q. What do you mean when you say GMO is inconsistent and unfair?

11 A. As noted above, if the Crossroad Energy Center is included in GMO's rate
12 base at net book value, such an action would result in GMO's customers paying
13 approximately $12 million annually for imprudent GMO management decisions. Further, if
14 the Crossroad Energy Center is included in GMO's rate base at net book value, then it would
15 be unfair and inconsistent to not include the current book value of the deferred taxes in
16 determining the revenue requirement of MPS.

17 GMO is proposing to increase GMO's rate base by approximately $117 million.
18 This is the net book value (original cost of the plant less accumulated depreciation expense
19 taken on the plant). This net book value, however, does not represent GMO's net investment
20 in the plant. Its net investment in this plant is the $117 million less $13.4 million of
21 accumulated deferred income taxes, for a net investment, of $103.6 million.

1 If the Commission determined that the Crossroads Energy Facility should be included
2 in GMO's rate base at net book value, then the appropriate net book or net investment value
3 would be $103.6 million.

4 GMO's position is inconsistent in that it proposes to reflect the accumulated
5 depreciation recorded on its books for the Crossroads Energy Center. This accumulated
6 amount of depreciation expense since the plant was constructed was "never a payment of
7 depreciation expense by GMO-MPS's customers or any other customer in a regulated
8 environment" as Ms Hardesty notes for the deferred taxes, yet GMO proposes to reflect the
9 total amount of the depreciation reserve in GMO-MPS' rate base.

10 If this position is appropriate for accumulated depreciation expense, it is also
11 appropriate for accumulated deferred income taxes, which are directly associated with and
12 directly the result of the depreciation taken on this plant. The deferred taxes represent the tax
13 effect of depreciation expense taken for book purposes and for income tax purposes. It is a
14 benefit provided by United States income tax laws that GMO has taken advantage of to the
15 benefit of its shareholders, yet refuses to pass the effect of this decreased investment cost to
16 the detriment of its regulated customers.

17 Q. Does this end your surrebuttal testimony?

18 A. Yes, it does.

BEFORE THE PUBLIC SERVICE COMMISSION

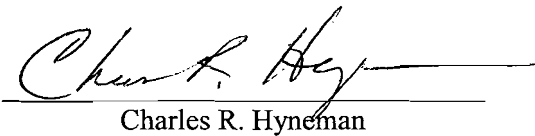
OF THE STATE OF MISSOURI

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

AFFIDAVIT OF CHARLES R. HYNEMAN

STATE OF MISSOURI)
) ss.
COUNTY OF COLE)

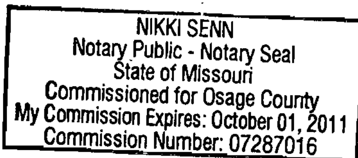
Charles R. Hyneman, of lawful age, on his oath states: that he has participated in the preparation of the foregoing Surrebuttal Testimony in question and answer form, consisting of 51 pages to be presented in the above case; that the answers in the foregoing Surrebuttal Testimony were given by him; that he has knowledge of the matters set forth in such answers; and that such matters are true and correct to the best of his knowledge and belief.



Charles R. Hyneman

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

Notary Public



Non-Fuel O&M Comparison
Revenue Requirement - Case Nos ER-2007-0004 and ER-2009
GMO-MPS and GMO-L&P

		MPS Staff EMS ER-2007-0004 "Base Year" NFOM	MPS Staff EMS ER-2009-0090 "Current" NFOM
O&M	Acct	$318,989,653	$338,592,960
Fuel	501	($65,882,708)	($86,842,102)
Fuel	547	($15,693,210)	($26,284,993)
Purch Pwr	555	($79,123,271)	($70,255,970)
Purch Pwr	555	($7,485,922)	($26,881,690)
Purch Pwr	555	($42,139,995)	($598,049)
NFOM		**$108,664,547**	**$127,730,156**
Increase			**$19,065,609**
Increase %			**18%**

		L&P Staff EMS ER-2007-0004 "Base Year" NFOM	L&P Staff EMS ER-2009-0090 "Current" NFOM
O&M	Acct	$101,762,675	$101,488,550
Fuel	501	($17,313,510)	($21,737,163)
Fuel	547	($1,485,134)	($4,438,929)
Purch Pwr	555	($19,637,113)	($26,359,604)
Purch Pwr	555	($9,492,000)	$0
Purch Pwr	555	($10,239,841)	$0
NFOM		**$43,595,077**	**$48,952,854**
Increase			**$5,357,777**
Increase %			**12%**

SCHEDULE 1

DRAFT

To: **Files**

From: Ron Klote, Senior Manager Regulatory Accounting

CC: Darrin Ives

Date: October 31, 2008

Subject: Crossroads Energy Center Transfer to the KCP&L Greater Missouri Operations Company Regulated Jurisdiction's MOPUB Business Unit

Purpose:
To document the reason for and the timing of the property accounting move of the Crossroads Energy Center to the books and records of KCP&L Greater Missouri Operations Company's ("GMO") MOPUB business unit. In addition, documenting the recording of the Crossroads Energy Center as a capital lease and how the accumulated deferred income taxes ("ADIT") should be treated associated with the plant.

Relevant Guidance Researched:
Code of Federal Regulations Title 18 Part 101

Background:
The Crossroads Energy Center is an approximately 300MW combustion turbine power plant consisting of four General Electric 7EA units. It was built in 2002 by a non-regulated subsidiary of Aquila, Inc. titled Aquila Merchant Services. It is located in Mississippi and is owned by the City of Clarksdale for property tax abatement purposes. GMO holds a purchase option that provides the opportunity for GMO to purchase the plant from the City of Clarksdale at any time for $1,000. This purchase would eliminate the property tax abatement treatment of the plant. The Crossroads Energy Center is controlled by GMO through a long-term tolling agreement. The plant is recorded as a capital lease on the books and records of MOPUB.

The placement of the Crossroads Energy Center on the books and records of Aquila, Inc. was as follows. In October 2002, the Crossroads Energy Center was moved from business unit MEP (Merchant Energy Partners Investment LLC) CWIP account into business unit ACEC (Crossroads Energy Center) plant accounts. ACEC was a business unit under the non-regulated subsidiary of MEP. In March 2007, due to the wind down of Aquila's Merchant operations and their inability to effectively dispatch power from the Crossroads Energy Center, there was a negotiation of the rights and obligations of the plant to Aquila, Inc. This transfer was governed by a Master Transfer Agreement dated March 31, 2007. Aquila, Inc. paid $117.9 million to Aquila Merchant which was equivalent to the net book value of Crossroads at this time. Rather than pay a cash purchase price, the purchase price took the form of a credit that reduced the amount of indebtedness owed by Aquila Merchant to Aquila parent. On March 31, 2007, Crossroads Energy Center was recorded at Net Book Value to a nonregulated business unit CECAQ (Crossroads Energy Center Aquila) where it resided at the time of the acquisition of Aquila, Inc. by Great Plains Energy (GPE).

On March 19, 2007, the regulated jurisdictional operations of GMO issued a request for proposal for a long-term supply option. The Crossroads Energy Center was bid into the request for proposal at net book value to satisfy the long-term supply option. The candidates submitting bids for the long-term supply option were evaluated and the Crossroads Energy Center was selected as the least cost and preferred option for long-term supply. The evaluation process and selection of the Crossroads Energy Center as the preferred option was presented to the Missouri Public Service Commission Staff on October 31, 2007.

SCHEDULE 2-1

On approximately May 14, 2008 Aquila's management presented a review of the IRP process presented to Staff in October 2007 with GPE management. During this presentation, the Request for Proposal process was discussed with GPE management and Aquila's decision to select Crossroads as the least cost and preferred option was reviewed. At this meeting, GPE concurred with Aquila's recommendation to use Crossroads as a long-term supply option. (Note added by Tim Rush: Attendees, Todd Kobayashi, Kevin Bryant, Tim Rush, Scott Heidtbrink, Davis Rooney, Gail Allen, Gary Clemens, Denny Williams, Jeremy Morgan). As a note, in the initial evaluation of the acquisition of Aquila, GPE had not made a decision on how it would address the Crossroads facility.

On August 31, 2008 the Crossroads Energy Center was moved from GMO's business unit NREG, where it was recorded after the acquisition of Aquila, Inc. by Great Plains Energy on July 14, 2008, to MOPUB's books and records. MOPUB is the regulated business unit which previously served the territory known as Missouri Public Service. On September 5, 2008 GMO regulated jurisdictions filed a rate case including the Crossroads Energy Center in MPS's rate base at net book value.

Conclusion:

The following actions regarding the accounting of the Crossroads Energy Center are appropriate:

1. The Crossroads Energy Center should be recorded at net book value on the books and records of KCP&L Greater Missouri Operations Company's MOPUB business unit.
2. August 2008 was the appropriate time to move the Crossroads Energy Center to the MOPUB business unit.
3. The Crossroads Energy Center is appropriately recorded as a capital lease as part of the continuing property records.
4. The ADIT associated with the time period that the Crossroads Energy Center was recorded on the non-regulated subsidiary of Aquila, Inc. should be recorded on the non-regulated business unit AQP (GMO's non-regulated subisidiary). The ADIT balances from March 2007 when the Crossroads Energy Center was moved to a business unit under Aquila, Inc. parents books and records until the present should be recorded on the business unit MOPUB.

Support of Conclusion:

Recorded at Net Book Value on MOPUB's Books and Records

The support for the decision by GPE's management to record the Crossroads Energy Center at net book value can be directly linked to the Request for Proposal process by GMO. As discussed in the background section above, on March 19, 2007 the regulated jurisdictional operations of GMO sent out a Request for Proposal to evaluate and choose a long-term supply option. Aquila, Inc. bid the Crossroads Energy Center into the Request for Proposal process at net book value. All bids were accumulated and evaluated. The Crossroads Energy Center was selected as the least cost and most preferred option. This was presented to Missouri Public Service Commission Staff on October 31, 2007.

Additionally, with the acquisition of Aquila, Inc. by Great Plains Energy, PricewaterhouseCoopers was engaged to complete a Purchase Accounting Valuation. As part of this analysis, there was an assessment of the fair market value of the Crossroads Energy Center. This evaluation resulted in an amount that was in excess of the Net Book Value that was offered into the Request for Proposal process initiated by Aquila Inc. GPE's management made the decision to not record a fair market value adjustment on the Crossroads Energy Center, but instead record the plant at net book value and include the property as part of GMO's regulated jurisdiction. This amount is being requested to be part of rate base at net book value in GMO's current rate case filing, case number ER-2009-0090.

Recorded at August 2008 on Business Unit MOPUB

The support to move the Crossroads Energy Center to MOPUB's business unit in August 2008 can be linked to a series of events ultimately concluding in GPE management's decision to include the Crossroads Energy Center in the GMO's regulated jurisdiction rate base calculation in the September 5, 2008 rate case filing (ER-2009-0090). The series of events as discussed in the background section of this whitepaper are detailed below:

- On March 31, 2007, the non-regulated subsidiary Merchant Energy Partners negotiated an assignment of the rights and obligations of the Crossroads Energy Center to the Parent company Aquila, Inc.
- Subsequently, Aquila, Inc. bid the Crossroads Energy Center into a Request for Proposal by GMO's regulated jurisdiction for a long-term supply option.
- GMO's evaluation of the bids offered concluded that the Crossroads Energy Center was the least cost and preferred option for the long-term supply option.
- On October 31, 2007, a presentation was made to the Missouri Public Service Commission Staff communicating the results of the Request for Proposal process.
- Approximately May 14, 2008 Aquila's management reviewed the results of the IRP process and the results of the Request for Proposal process with GPE's management. GPE's management concurred with the decision that Crossroads was the least cost and preferred long-term supply option.
- On July 14, 2008 Great Plains Energy completed their acquisition of Aquila, Inc.
- August 2008, GPE's management decided to include the Crossroads Energy Center in rate base in its GMO regulated jurisdiction.
- On August 25, 2008, GPE's management met with Missouri Public Service Commission Staff and discussed GPE's decision to move the Crossroads Energy Center onto the books and records of GMO's regulated jurisdiction and include the net book value of the plant in rate base in the upcoming rate case filing.
- August 31, 2008 Crossroads Energy Center was transferred to GMO's regulated jurisdiction.
- September 5, 2008, GMO filed a rate case under the docket number ER-2009-0090 including the Crossroads Energy Center in rate base at net book value.

<u>*Recorded as a Capital Lease*</u>
The "General Instructions" number 19 of 18 CFR part 101 states the following:

> *If at the inception a lease meets one or more of the following criteria, the lease shall be classified as a capital lease. Otherwise, it shall be classified as an operating lease.*
> 1. *The lease transfers ownership of the property to the lessee by the end of the lease term.*
> 2. *The lease contains a bargain purchase option.*
> 3. *The lease term is equal to 75 percent or more of the estimated economic life of the leased property.*
> 4. *The present value at the beginning of the lease term of the minimum lese payments, excluding that portion of the payments representing executory costs such as insurance, maintenance and taxes to be paid by the lessor, including any profit theron, equals or exceeds 90 percent of the excess of the fair value of the leased property to the lessor at the inception of the lease over any related investment tax credit retained by the lessor and expected to be realized by the lessor.*

The Crossroads Energy Center has been recorded on the books and records since October 2002 as a capital lease. This is supported by the following:

- Criteria number 3 states that the lease term is equal to 75 percent or more of the estimated economic life of the leased property. The Crossroads Energy Center meets this criteria. The lease term agreed to with the City of Clarksdale was for an original term of 30 years and two 5 year extension options. The economic life of the plant is estimated at 40 years. This equates to 75 percent of the economic life when considering the original terms and 100 percent of the economic if the two 5 year extension periods are exercised. Both meet or exceed the 75 percent criteria discussed above.
- In addition, criteria number 2 states that the lease must contain a bargain purchase option. Effective March 28, 2008 GMO finalized a purchase option that allows it to purchase the Crossroads Energy Center from the City of Clarksdale at any time for $1,000. $1,000 would be considered a bargain purchase option as it is significantly less than the fair market value of the plant. Crossroads would meet this requirement.

Recording of ADIT Balances

ADIT balances to date associated with the Crossroads Energy Center can be grouped into two separate categories as follows:

- ADIT accumulated from original in service date during 2002 to the date the plant was transferred to Aquila, Inc.'s parents books CECAQ in March 2007.
- ADIT accumulated on Aquila, Inc.'s parents books from March 2007 to present.

The ADIT in the first grouping when the Crossroads Energy Center was recorded on Aquila's non-regulated subsidiary Merchant Energy Partner's with a business unit titled ACEC is attributable to the deferred intercompany gain from when the Plant was transferred to Aquila, Inc.'s parents books. The transfer of these ADIT balances to Parent would not be appropriate as the Parent or the future GMO jurisdiction has not received any benefits of the accelerated depreciation that was recognized on the non-regulated subsidiary books. As such, the ADIT associated with this time period is recorded presently on the non-regulated business unit AQP.

The ADIT associated with the time period of when the plant was recorded on Aquila Inc.'s parents books to the present is attributable to the tax effected difference between book and tax depreciation. Due to tax normalization rules, these amounts are required to follow the plant as it gets transferred to the GMO regulated jurisdiction of MOPUB. These ADIT amounts will be used as rate base offsets to the plants net book value that will be included in GMO's rate case filings.

SCHEDULE 3

HAS BEEN DEEMED

HIGHLY CONFIDENTIAL

IN ITS ENTIRETY

SCHEDULE 4

HAS BEEN DEEMED

HIGHLY CONFIDENTIAL

IN ITS ENTIRETY