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MISSOURI PUBLIC SERVICE COMMISSION

REGULATORY REVIEW DIVISION

UTILITY SERVICES - AUDITING

REBUTTAL TESTIMONY

OF

KEITH MAJORS

KANSAS CITY POWER & LIGHT COMPANY

CASE NO. EU-2014-0255

Jefferson City, Missouri
November 14, 2014

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KEITH MAJORS
KANSAS CITY POWER & LIGHT COMPANY
CASE NO. EU-2014-0255**

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OF

KEITH MAJORS

KANSAS CITY POWER & LIGHT COMPANY

CASE NO. EU-2014-0255

Q. Please state your name and business address.

A. Keith Majors, Fletcher Daniels Office Building, 615 East 13th Street, Room G8, Kansas City, Missouri, 64106.

Q. Please describe your educational background and work experience.

A. I attended Truman State University in Kirksville, Missouri, and earned a Bachelor of Science degree in Accounting in 2007. I have been employed by the Missouri Public Service Commission (“Commission”) since June 2007 within the Auditing Unit.

Q. What is your current position with the Commission?

A. In 2010, I was promoted to my current position of Utility Regulatory Auditor IV within the Auditing Unit, within the Audits, Depreciation, and Financial Analysis Department, Regulatory Review Division, of the Commission.

Q. Have you previously filed testimony before this Commission?

A. Yes. A listing of the cases in which I have previously testified, or authored a Staff recommendation or memorandum, and the issues I have addressed in those filings, is attached as Schedule KM-1 to this rebuttal testimony.

Q. What knowledge, skills, experience, training and education do you have in the areas of which you are testifying as an expert witness?

Rebuttal Testimony of
Keith Majors

A. I have been employed by the Commission as Regulatory Auditor for 7 years, and have submitted testimony on ratemaking matters several times before the Commission. I have participated in in-house and outside training, and attended seminars on technical and general ratemaking matters while I have been employed by the Commission.

I have been assigned to several Kansas City Power & Light Company (“KCPL”) and KCP&L Greater Missouri Operations Company (“GMO”) rate case matters during my employment at the Commission:

<u>Utility</u>	<u>Case No.</u>
KCPL – Electric	ER-2009-0089
GMO – MPS and L&P Electric	ER-2009-0090
GMO – L&P Steam	HR-2009-0092
KCPL – Electric	ER-2010-0355
GMO – MPS and L&P Electric	ER-2010-0356
KCPL – Electric	ER-2012-0174
GMO – MPS and L&P Electric	ER-2012-0175
KCPL – Electric	ER-2014-0370
KCPL – Electric	EU-2015-0094

GMO is an affiliate of KCPL.

Q. What caused the need to file this rebuttal testimony?

A. On June 12, 2014 KCPL filed an application for an Accounting Authority Order (AAO) to defer certain costs related to the accounting treatment used for construction of the environmental upgrades at its LaCygne Generating Station (“LaCygne”). The effect of what KCPL proposes is, first, to defer the impact on its books of recording depreciation expense associated with the LaCygne project from the time construction is completed to when the Company starts to recover the LaCygne project’s capital costs in rates in the rate case filed on October 30, 2014, designated as Case No. ER-2014-0370—the 2015 rate case. Second, KCPL is proposing to defer the impact of inclusion of the LaCygne project in KCPL’s rate base once the project is in-service by recording carrying charges on the LaCygne project

1 investment from the time construction is completed to when the Company starts to recover the
2 LaCygne project's capital costs in rates in the 2015 rate case. KCPL seeks authority to accrue
3 these deferred costs as a regulatory asset on its books and records. This accrual is referred to as
4 "continuation of construction accounting," or, further abbreviated, "construction accounting."

5 While KCPL's request is not a typical deferral of costs the Commission generally
6 sees, in order to achieve this accounting the Commission would have to in effect authorize
7 an AAO.

8 Q. What is the purpose of your rebuttal testimony?

9 A. I am, along with Staff witness Mark Oligschlaeger, responding to KCPL
10 witness Ronald Klote who filed direct testimony on June 12, 2014 with the application
11 wherein KCPL requested the use of construction accounting for the LaCygne environmental
12 upgrades. Witness Klote provides an overview of KCPL's request in his direct testimony.

13 Q. Have you participated in the Commission Staff's ("Staff") audit of KCPL
14 concerning its request to defer certain costs relating to the completion of the environmental
15 upgrades being installed at for an AAO in this proceeding?

16 A. Yes, I have, with the assistance of other members of Staff.

17 Q. Are you participating in a case presently pending before the Commission that
18 involves KCPL and issues similar to those in KCPL's request in this case?

19 A. Yes. On October 9, 2014, Staff filed a petition at the Commission requesting it
20 to order KCPL to record to a new subaccount, **FERC Account 254—Other regulatory**
21 **liabilities** labeled **KCPL—MO DOE fees regulatory liability** in the amount of \$7,019
22 for each day after May 15, 2014, for the amount KCPL is recovering in Missouri retail
23 customer rates for the one-tenth of a cent for each kWh of net nuclear generation from

1 Wolf Creek delivered and sold by KCPL that KCPL was incurring to the DOE for
2 spent nuclear fuel storage fees until May 15, 2014, when the DOE reduced the quarterly fee to
3 zero effective May 16, 2014, and thereafter. Staff's petition has been designated as Case
4 No. EU-2015-0094.

5 Q. How are the issues in that case similar to the issues in this case?

6 A. In both cases, KCPL and Staff are asking for relief on the basis of a change in
7 circumstances affecting the Company's cost of service that they assert was not one of the "all
8 relevant factors" the Commission considered when it established KCPL's current rates.

9 Q. How are you participating in Case No. EU-2015-0094?

10 A. I prepared direct testimony that was filed with the petition, as did Mark
11 Oligschlaeger, Manager of the Auditing Unit of the Commission.

12 **EXECUTIVE SUMMARY**

13 Q. Please summarize your rebuttal testimony in this proceeding.

14 A. As described in its Application, as well as in the direct testimony of KCPL
15 witness Ronald A. Klote, KCPL is requesting that the Commission authorize it to defer
16 certain costs relating to the KCPL's environmental upgrade currently being installed at
17 LaCygne. KCPL has requested an AAO to allow it to accrue a regulatory asset on its books
18 and records equal to the depreciation expense and carrying costs for the Missouri
19 jurisdictional portion of its investment in the LaCygne environmental plant additions for the
20 period after the new investment is in-service but prior to when the new investment will be
21 included in KCPL's rate base in its next general rate proceeding. This accrual is referred to as
22 construction accounting.

1 Staff recommends the Commission reject KCPL's Application in this case for several
2 reasons. First, while KCPL has filed its 2015 rate case, Staff's audit has just started. Staff
3 has not been able to substantiate the need for the construction accounting treatment requested
4 by KCPL for the LaCygne environmental upgrades. The Company does not need a decision
5 for its Application for construction accounting until sometime during the later stages of the
6 rate case because the in-service date for the LaCygne project and its resulting financial
7 impacts will not occur until the first and second quarters of 2015. As result, it is premature at
8 this time to decide if KCPL needs construction accounting for its LaCygne plant additions.

9 Second, the LaCygne environmental construction project does not rise to the level of
10 other KCPL construction projects that have received construction accounting treatment in the
11 past. Staff does not believe KCPL's request meets the Commission's prior standard for
12 AAOs being associated with events that are extraordinary, unusual, and infrequent.

13 Third, if the Commission authorizes KCPL's requested AAO, then Staff recommends
14 several modifications to the amounts calculated as well as reductions for offsetting cost
15 decreases related to Staff's petition in Case No. EU-2015-0094 and other matters.

16 **ACCOUNTING AUTHORITY ORDERS AND BACKGROUND**

17 Q. What is an AAO?

18 A. An AAO is an authorization by the Commission for a utility to account for a
19 particular cost in a different manner than is normally prescribed in the Federal Energy
20 Regulatory Commission (FERC) Uniform System of Accounts (USOA), which the
21 Commission has adopted for accounting purposes, for use by the electric utilities it regulates.
22 The Commission may authorize utilities to defer certain costs resulting from unusual or
23 extraordinary events that occur during the course of utility operations. The USOA has

1 provisions that allow deferrals to be identified on the books of utility companies for future
2 determination in a rate case to see if these deferred costs – increases or decreases to costs –
3 are considered for rate making treatment. An AAO is a vehicle that can reduce or mitigate the
4 impacts of regulatory lag. Regulatory lag is the period of time that elapses between the time
5 of an event and its related consequences occur and the time the event and its related
6 consequences are reflected in the utility's rates. AAO's are most often proposed by utilities to
7 offset regulatory lag that otherwise would disadvantage their shareholders.

8 The most common examples of AAOs in this jurisdiction are orders from the
9 Commission allowing a company to defer on its books remediation and repair costs associated
10 with "extraordinary events," such as weather related natural disasters (or "acts of God") like
11 ice storms, tornados, floods and hurricanes. Other AAOs over time have addressed the
12 accounting for other post-employment benefits (OPEB) and retiree medical expenses,
13 manufactured gas plant (MGP) expenses, costs associated with the implementation of new
14 Commission rules, extraordinary mechanical failure not involving operator negligence, and
15 "Year-2000" (Y2K) expenses.

16 Q. Does the Commission only grant authority to defer costs in a separate AAO
17 application?

18 A. No. Expense deferrals have been frequently authorized by the Commission
19 within the context of a general rate case. For example, in KCPL's 2012 rate case, Case No.
20 ER-2012-0174, the Commission authorized a 5-year deferral and amortization of non-wage
21 O&M expenses related to the 2011 Missouri River flooding and a 3-year deferral and
22 amortization of certain 2010 rate case expenses.

1 Ongoing expense deferrals are also a result of the pension expense and other tracking
2 mechanisms authorized for the major utilities in the state. These tracking mechanisms are
3 commonly authorized by the Commission after parties have agreed to their terms and
4 technical calculations in stipulations and agreements.

5 Q. Are deferral mechanisms limited to expenses?

6 A. No. Revenues or a reduction in expense can also be deferred and amortized
7 through the cost of service. A recent example is the return of property tax refunds to Ameren
8 Missouri customers in Case No. ER-2012-0166, thereby creating a *regulatory liability*.

9 Q. What are “regulatory assets” and “regulatory liabilities”?

10 A. This definition is found in the USOA, Code of Federal Regulations, Part 101,
11 Definition 30 (April 1, 2004 Edition):

12 31. Regulatory Assets and Liabilities are assets and liabilities
13 that result from rate actions of regulatory agencies. Regulatory
14 assets and liabilities arise from specific revenues, expenses, gains,
15 or losses that would have been included in net income
16 determination in one period under the general requirements of the
17 Uniform System of Accounts but for it being probable:

18 A. that such items will be included in a different period(s) for
19 purposes of developing the rates the utility is authorized to charge
20 for its utility services; or

21 B. in the case of regulatory liabilities, that refunds to
22 customers, not provided for in other accounts, will be required.

23 Q. Is it the Commission’s general practice to allow a utility to preserve deferrals
24 on its balance sheet until an amortization can be included in the utility’s rates?

25 A. No. In most cases, utilities have agreed, or the Commission has ordered, that
26 deferred costs begin to be amortized to expense immediately or a short time after the
27 extraordinary event triggering the deferral has occurred, even if the utility does not have a

1 general rate case filed. However, there is still a benefit to the utility from the deferral and
2 amortization of expenses in that circumstance because the financial impact of the event is
3 spread across multiple accounting reporting periods (years) rather than reflecting the entire
4 impact in the year the extraordinary event occurred. Absent the deferral treatment authorized
5 by the Commission, the utility would have to charge the costs as current expenses in the year
6 costs were incurred.

7 An example of this scenario is the AAO authorized in Case No. EU-2002-1048 for
8 KCPL's expenditures related to the 2002 ice storm impacting the majority of its distribution
9 system. The Commission ordered amortization of KCPL's deferral to begin September 2002
10 and end January 2007. KCPL did not file a general rate case from the mid-1980s until
11 February 1, 2006. In the interim between authorization of this AAO and early 2006, KCPL
12 amortized the regulatory asset to expense and determined that earnings were adequate and that
13 no rate relief was necessary during the amortization period. In that case, the Commission's
14 grant of an AAO functioned in practice more as a tool to "smooth" earnings over several
15 accounting periods rather than to provide rate recovery of extraordinary costs.

16 Q. What standard has the Commission used to determine whether it should
17 authorize a utility to deviate from normal USOA accounting rules?

18 A. Generally, the Commission in prior cases has said that the standards for
19 granting the authority to a utility to defer costs incurred outside of a test year as a regulatory
20 asset are: 1) the costs relate to an event that is extraordinary, unusual, and infrequent, and
21 2) the costs associated with the event are material.

22 In Case Nos. EO-91-358 and EO-91-360 (consolidated, "the Sibley Case"),
23 the Commission determined its policy regarding the use of AAOs to defer costs normally

1 charged to income as they are incurred. Page 7 of the Commission's *Report and Order* in that
2 case stated:

3 Under historical test year ratemaking, costs are rarely considered
4 from earlier than the test year to determine what is a reasonable
5 revenue requirement for the future. Deferral of costs from one
6 period to a subsequent rate case causes this consideration and
7 should be allowed only on a limited basis.

8 This limited basis is when events occur during a period which are
9 extraordinary, unusual, and unique, and not recurring. These types
10 of events generate costs which require special consideration.
11 These types of costs have traditionally been associated with
12 extraordinary losses due to storm damage or outages, conversions,
13 or cancellations. *UE* at 618. The Commission in the past has also
14 allowed accrual of Allowance for Funds Used During Construction
15 (AFUDC) and nuclear fuel leases. These were allowed because of
16 the size of the investments to be deferred. The USOA recognizes
17 that only extraordinary items should be deferred. The definition
18 cited earlier states the intent of the USOA that net income shall
19 reflect all items of profit and loss during the period and exceptions
20 are only for those items which are of significant effect, not
21 expected to recur frequently, and which are not considered in the
22 evaluation of ordinary business operations.

23 Later in the Sibley Case *Report and Order* on page 8, the Commission determined the
24 following regarding materiality of costs for which deferral treatment is requested:

25 Staff's first criterion, which requires the event to be extraordinary,
26 is, as stated above, the most significant inquiry in a deferral case.
27 As MPS points out, the crux of the criterion is, what is an
28 extraordinary event? This, of course, will be the primary focus of
29 the Commission in any case involving a request for an AAO. The
30 issues of whether the event has a material or substantial effect on a
31 utility's earnings is also important, but not a primary concern. The
32 company, under the USOA, is required to seek Commission
33 approval if the costs to be deferred are less than five percent of the
34 company's income computed before the extraordinary event. This
35 five percent standard is thus relevant to materiality and whether the
36 event is extraordinary but is not case-dispositive.

1 The Commission commented on the effect of regulatory lag in reference to requests for
2 deferral on page 10 of the Sibley Case *Report and Order*:

3 Lessening the effect of regulatory lag by deferring costs is
4 beneficial to a company but not particularly beneficial to
5 ratepayers. Companies do not propose to defer profits to
6 subsequent rate cases to lessen the effects of regulatory lag, but
7 insist it is a benefit to defer costs. Regulatory lag is a part of the
8 regulatory process and can be a benefit as well as a detriment.
9 Lessening regulatory lag by deferring costs is not a reasonable goal
10 unless the costs are associated with an extraordinary event.

11 Most recently, the Commission affirmed its standard of review of AAO requests in Case No.
12 EU-2014-0077, KCPL and GMO's request for a transmission expense tracker.
13 The Commission denied this request in its *Report and Order* dated August 29, 2014, on the
14 basis that the transmission costs were not extraordinary, unusual, and infrequent.

15 Q. Has the Commission made ratemaking findings in the context of AAO
16 applications?

17 A. No. The Commission has traditionally held that AAO applications are for the
18 sole purpose of determining the accounting treatment for certain costs. The decision
19 regarding rate recovery of deferred costs – the length of the amortization and whether or not
20 the unamortized balances receives rate base treatment – has always been reserved by the
21 Commission for subsequent general rate proceedings.

22 **KCPL'S REQUEST FOR DEFERRAL**

23 Q. Briefly describe LaCygne and the LaCygne environmental project.

24 A. LaCygne is an electric generating station located in Kansas comprised of
25 two coal-fired units. Unit 1 went into service in 1973 and has a net generating capacity of
26 736 megawatts (MW), and Unit 2 went into service in 1977 and has a net generating capacity

1 of 682 MW. KCPL owns 50% of LaCygne, and Kansas Gas and Electric Company; a wholly
2 owned subsidiary of Westar Energy, Inc. (Westar) owns 50% of LaCygne Unit 1 and leases
3 the other 50% of LaCygne Unit 2. KCPL is the operating partner for both units.

4 The LaCygne environmental project is the construction of wet scrubbers to control
5 sulfur dioxide (“SO₂”), baghouses to control particulates, and a common dual flue chimney
6 for both Unit 1 and Unit 2. KCPL is constructing selective catalytic reduction (SCR)
7 equipment, low-nitrogen oxide (“NO_x”) burners, and an over-fire air (OFA) system for
8 Unit 2 to control NO_x emissions. (Unit 1’s SCR was installed in 2007.) The cost estimate at
9 completion of the project is \$1.23 billion. KCPL has identified the amount of Missouri
10 jurisdictional rate base impact of the LaCygne environmental project to be \$336 million prior
11 to the impact of AFUDC.

12 The LaCygne environmental project is required to be completed by its owners on or
13 before June 1, 2015. This date resulted from a 2007 agreement between KCPL and the
14 Kansas Department of Health and Environment (“KDHE”) to install best available retrofit
15 technology (“BART”) equipment on or before the deadline. If the LaCygne units are not in
16 compliance with the agreement on or before June 1, 2015, KCPL is required to cease
17 operating the units at LaCygne until the units are in compliance with the requirements of
18 the agreement.

19 Q. What is KCPL requesting in its Application in Case No. EU-2014-0255?

20 A. The Company requests that the Commission authorize it to use construction
21 accounting beginning on the in-service date of each of the units for the LaCygne
22 environmental project until new rates that include the cost of the LaCygne environmental
23 project become effective. “Specifically, for that period of time the Company seeks to record

1 as a regulatory asset 1) carrying costs on the LaCygne environmental project which will be
2 calculated by applying on a monthly basis a carrying cost rate to LaCygne environmental
3 project plant additions placed in-service. The carrying costs will be deferred to regulatory
4 asset account 182.3 from the date the plant additions are placed in service until the date the
5 plant additions are included in rates; and 2) depreciation expense on the LaCygne
6 environmental project will be deferred to regulatory asset account 182.3 from the date
7 the LaCygne environmental project plant additions are placed in-service to the date
8 the plant additions are included in rates.” (*Application*, Case No. EU-2014-0255
9 (“Application”), pp. 4-5). The reference to account 182.3 is to the FERC USOA
10 Account 182.3, “Other regulatory assets.”

11 Q. When will the construction of the LaCygne environmental upgrades be
12 completed?

13 A. The LaCygne Unit 2 environmental upgrade is expected to be completed
14 sometime in the early second quarter of 2015 and LaCygne Unit 1 environmental upgrade is
15 expected to be completed by June 1, 2105. Under KCPL’s proposal, LaCygne Unit 2 deferral
16 would start when the environmental construction is completed and continue until the
17 point when rates change as a result of KCPL’s 2015 rate case; i.e., no later than late
18 September 2015. Unit 1’s deferral would start when its environmental upgrades are
19 completed as of June 1, 2015 until the point when rates change.

20 Q. Has KCPL filed a general rate case in Missouri since it has filed this
21 AAO application?

22 A. Yes. KCPL filed its *Notice of Intended Case Filing* on June 25, 2014,
23 notifying the Commission of its intent to file a general rate case no earlier than 60 days after

1 that date. KCPL then filed its *Application* for a general rate increase on October 30, 2014
2 which was assigned as Case No. ER-2014-0370.

3 **PRINCIPLES OF CONSTRUCTION ACCOUNTING**

4 Q. What is AFUDC?

5 A. Beginning at the inception of a construction project, an electric utility is
6 allowed to accrue carrying costs, or interest, in FERC Account 107 – Construction Work In
7 Progress (generally, “CWIP”) according to a specified formula enumerated in the USOA,
8 Electric Plant Instructions, Paragraph 17. The carrying costs are referred to as AFUDC and
9 are based on a formula that considers the capital structure using the utilities’ amount of
10 outstanding CWIP, short-term and long-term debt, and equity. The cost of debt and equity is
11 also part of this calculation. The resulting carrying costs from this formula are capitalized to
12 the account and added to the CWIP balance as any other cost of construction. The purpose of
13 AFUDC is to compensate the utility for its cost of money, obtained from both debt holders
14 and shareholders, while an asset is being constructed. AFUDC is a deferred return of
15 construction costs while the project is under construction. Utilities are allowed to accrue for
16 AFUDC until the time the plant addition goes into service and recover those costs over the
17 life of the plant like all other costs relating to the construction project.

18 Q. Generally, how does the use of construction accounting, benefit a utility?

19 A. Upon completion and dedication to utility service of an asset, AFUDC ceases
20 to be accrued, the entire cost of the construction project is transferred to FERC Account 101 –
21 Electric Plant in Service and depreciation begins to accrue on that amount for financial and
22 regulatory accounting purposes.

1 A utilities' cost of service related to plant-in-service consists of two parts: a return *of*
2 investment (depreciation), and a return *on* investment (Return on Investment, or Return on
3 Equity). Due to the regulatory process, there is a period of time between the completion of
4 construction of an asset and the recovery of the return of and return on utility plant in service.
5 All other things being equal, the utility will realize an earnings shortfall related to the specific
6 asset in this time period. The use of construction accounting, or more correctly *continuation*
7 *of* construction accounting, attempts to "bridge the gap" in that time period after construction
8 is complete but before construction costs are reflected in the cost of service through new rates,
9 and eliminates the earnings shortfall described above.

10 Once an asset's construction is completed, the utility is required to depreciate that
11 asset to account for the ongoing reduction of useful life and return the plant investment to
12 investors and shareholders. Under continuation of construction accounting, the utility is
13 allowed to accrue a regulatory asset for the exact amount of the depreciation. The utility also
14 accrues a carrying cost on the balance of the asset as a regulatory asset, typically at the same
15 rate as AFUDC. Both of these accruals cease on the effective date of new rates that reflect the
16 return of and return on (depreciation and return on investment) the plant-in-service in
17 question. The net result to the utility is the exact matching of the financial impact of CWIP
18 transferring to plant to the recovery in rates of that plant. If KCPL could time its rate case
19 perfectly with the in-service dates of its major construction projects, there would not ever be a
20 need for construction accounting. KCPL's application is essentially intended to make the
21 Company whole for this imperfect timing.

22 The resulting regulatory asset is usually amortized to expense in the cost of service
23 over a period of time to be recovered in rates ratably, generally over the life of the asset.

1 However, this mitigation does not come without a cost to customers; under
2 continuation of construction accounting, each day the implementation of new rates is delayed
3 additional depreciation and carrying costs will be accrued and potentially recovered through
4 rates. In other words, while it may appear that the delay of a rate increase would benefit
5 customers; in fact, those same customers will be financing the delay.

6 Q. Has Staff agreed to construction accounting on the terms KCPL is proposing?

7 A. No. Staff has agreed to construction accounting in the context of stipulations
8 and agreements under different circumstances and under different terms and conditions than
9 what KCPL is proposing in this application.

10 **KCPL REGULATORY PLAN CONSTRUCTION ACCOUNTING**

11 Q. At page 8 of his testimony, Mr. Klote indicates that the Commission has
12 previously allowed construction accounting or other similar accounting treatment for KCPL's
13 construction of environmental improvements at Iatan 1 as well as the construction of Iatan 2.
14 Do you have any comments on this assertion?

15 A. Yes. In both cases accounting treatment was provided for through a stipulation
16 and agreement reached among the parties to a regulatory proceeding. As with most
17 settlements, there was "give and take" and concessions made by both sides. For example, in
18 return for construction accounting for Iatan 2 capital costs, as well as other regulatory items,
19 the terms of the Stipulation and Agreement in Case No. EO-2005-0329, the KCPL "regulatory
20 plan" case, provided for the following:

- 21 • KCPL's voluntary agreement to forego a fuel adjustment clause
- 22 for nearly 10 years,
- 23 • Authorization of construction of Iatan 2, a new coal-fired
- 24 baseload unit; environmental equipment at LaCygne 1; and
- 25 100MW of wind generation,

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- Parties to the agreement would not question the need for Iatan 2, referred to as decisional prudence,
- Establishment of Demand Response, Efficiency, and Affordability Programs,
- A reduced AFUDC rate for Iatan 2 during construction and for construction accounting,
- A rate moratorium through December 31, 2006

In this case, of course, KCPL's construction accounting proposal stands alone with no "mitigating" aspects.

Q. Are the circumstances underlying the construction accounting agreed to by the parties in 2005 different than they are today?

A. Yes. At the time the parties reached the settlement in 2005 providing for construction accounting for Iatan 2, KCPL had gone approximately 20 years without a rate case. Construction accounting for Iatan 1 was provided for in the stipulation and agreement in the 2009 Rate Case, Case No. ER-2009-0089. Since 2006, KCPL has completed five rate cases and now has filed a sixth rate case.

Q. How do the rates now compare to the rates that were in existence in 2006?

A. According to the KCPL information filed as part of its minimum filing requirements in the 2006 rate case, ER-2006-0314, KCPL average rate in 2006 was 5.677 cents per kWh.¹ Today, KCPL's average rate in 2014 is 8.907 cents per kWh.² Thus, to date, KCPL's rates have increased by 56.9% in 8 years. Moreover, KCPL has proposed in its pending case (ER-2014-0370) to increase rates by 15.75%. Therefore, the average rate would be 10.301 cents per kWh if the full amount of its rate request is granted.³ As such, under KCPL's proposal in the pending rate case, average rates will have increased 81.45%.

¹ ER-2006-0314 Minimum Filing Requirements page 1 of 2 -- 5.677 cents Average Price per kWh.

² ER-2014-0370 Minimum Filing Requirements 8.907 cents Average Price per kWh.

³ ER-2014-0370 Minimum Filing Requirements 10.301 cents Average Proposed Price per kWh.

1 Certainly, circumstances have changed since the 2006 timeframe after 20 years of stable rates
2 than they are today.

3 Q. How does the increase in KCPL's rates since 2006 compare to the increase in
4 regional and national electric rates?

5 A. The following chart shows that KCPL's rates have increased much more than
6 the state, regional (Iowa, Kansas, Minnesota, Missouri, South Dakota and North Dakota) and
7 national average rates according to the most recent Edison Electric Institute (EEI) rate
8 comparison—Typical Bills and Average Rates Report Summer 2014⁴:

9

Rates as of July 1, 2014	2006	2014	Increase
KCPL	5.66 ¢ / kWh	8.79 ¢ / kWh	55.3%
Missouri	5.74 ¢ / kWh	8.53 ¢ / kWh	48.6%
Regional	6.38 ¢ / kWh	8.64 ¢ / kWh	35.4%
National	8.89 ¢ / kWh	10.53 ¢ / kWh	18.5%

10

11 Thus, KCPL's average rate has increased almost three times as fast as the national average
12 electric rate over this period. Further, while KCPL's total average rate in 2006 was 11.3%
13 below the regional average rate, the current 2014 average rate now exceeds the regional
14 average rate. All of these figures are based upon KCPL's current rates. As mentioned, KCPL
15 has currently proposed to increase its existing rates in Missouri by 15.75%. As such, the
16 difference between KCPL's rates and the current regional and national rates is likely to be
17 even greater following the completion of the rate case. A summary of this data is attached as
18 Schedule KM 2.

19 Q. Has the increase in KCPL's rates been seen throughout all rate classes?

⁴ Edison Electric Institute – Typical Bills and Average Rates Report Summer 2014 – rates as of July 1, 2014.

1 A. Yes. All rate classes have experienced rate increases that range from 50.1% to
2 57.1%. Where KCPL residential rates were 13.6% below the regional average residential rate
3 in 2006, in 2014 the gap has narrowed to almost the same as the regional average residential
4 rate to within 0.5%. On the other hand, while KCPL's industrial rate was 11.6% below the
5 regional average industrial rate; it now exceeds the regional average industrial rate. Again,
6 these figures are based upon KCPL's current rates and do not consider KCPL's proposed
7 15.75% rate increase.

8 Q. What is your conclusion regarding Mr. Klote's comparison to the construction
9 accounting provided for Iatan 1 and Iatan 2?

10 A. Clearly, the comparison is not applicable. As mentioned, construction
11 accounting was provided in those situations as a result of a settlement between all parties and
12 involved certain concessions by KCPL. To date, KCPL has not proposed any offsets or
13 comparable beneficial terms and conditions with regard to its request for construction
14 accounting for the LaCygne project that would be comparable to the terms agreed to in prior
15 requests for construction accounting. Also, customers in 2006 had seen stable rates for a
16 period of 20 years. In contrast, today's customers have seen rates increase by 55% in eight
17 years with an additional proposed increase of 15.75% pending. The circumstances are clearly
18 different than it was when the agreement was reached in 2005 for construction accounting
19 Iatan 2 and later for Iatan 1.

20 **PRIOR USES OF CONSTRUCTION ACCOUNTING**

21 Q. Has the Commission authorized the use of construction accounting in the past?

A. Yes. The table below is a non-exhaustive list of cases in which the Commission authorized the use of construction accounting:

Company	Case No.	Generating Unit
Union Electric	EO-85-17 & ER-85-160	Callaway
Ameren Missouri	ER-2010-0036	Sioux Environmental
KCPL	EO-85-185 & ER-85-128	Wolf Creek
KCPL	ER-2009-0089	Iatan 1 & Common Environmental
KCPL GMO - SJLP	ER-2009-0090	Iatan 1 & Common Environmental
KCPL	EO-2005-0329	Iatan 2 & Common
KCPL GMO - MPS	EU-2011-0034	Iatan 2 & Common
KCPL GMO - SJLP	EU-2011-0034	Iatan 2 & Common
Empire	EO-2005-0263	Iatan 1 & Common Environmental
Empire	EO-2005-0263	Iatan 2 & Common
Empire	EO-2010-0262	Plum Point

A detailed list of these plants including the constructed amounts and respective portions of rate base is attached to this testimony as Schedule KM-3. It is my understanding that all of these previous authorizations for electric utilities to use construction accounting were in the context of negotiated stipulations and agreements.

Q. Briefly describe Wolf Creek and Callaway generating units.

A. Wolf Creek and Callaway are both nuclear power facilities completed in the mid-1980's. Wolf Creek, 47% of which is owned by KCPL, was completed at \$2.98 billion (1985 dollars), \$1.95 billion over the definitive estimate and 29 months after the original estimated date of commercial operation. The completion of Wolf Creek was so substantial that the Commission noted in its *Report and Order* in Case Nos. EO-85-185 and ER-85-128 [Cases Combined], "[E]lectric users are being burdened with the largest electric rate base addition in KCPL's history." At the time of inclusion in electric rates, Wolf Creek represented an 82% increase in KCPL's Missouri Jurisdictional rate base.

1 Callaway, wholly owned by Ameren Missouri (then, Union Electric Company), was
2 completed at \$2.98 billion (1985 dollars), \$1.89 billion over the definitive estimate and
3 33 months after the original estimated date of commercial operation. At the time of inclusion
4 in electric rates, Callaway represented a 60% increase of Ameren Missouri's (then Union
5 Electric) Missouri Jurisdictional rate base.

6 Due to the substantial delays, the uncertainty of completion, and the size of the
7 investments for both Wolf Creek and Callaway, both of these plants received continuation of
8 construction accounting treatment, through agreement between the parties to those rate
9 proceedings. Essentially, so the cases could be delayed past the normal 11 month time period
10 for setting rates after tariffs are filed, it is my understanding that Staff agreed to allow
11 construction accounting for these sizable plant additions in the rate cases in which the nuclear
12 units received rate base treatment.

13 Q. Briefly describe the Iatan 1 environmental project and the use of continuation
14 of construction accounting for that project.

15 A. The Iatan 1 environmental project included the construction of wet scrubbers
16 to control SO₂, and SCR to control NO_x emissions, and a baghouse to control particulate
17 emissions. Iatan 1 is owned 70% by KCPL, 18% by GMO – L&P, and 12% by The Empire
18 District Electric Company ("Empire"). This project was quite similar in nature to the current
19 LaCygne 2 project as the Iatan 1 and LaCygne 2 are similar base-load coal units. At the time
20 of the completion of construction, the Iatan 1 environmental upgrades, with Iatan 1 Common
21 totaled \$496.8 million, \$267.6 million of which was KCPL's Missouri jurisdictional share,
22 and these upgrades were an increase of 21% of its existing rate base. GMO-L&P's 18% share
23 of the Iatan 1 upgrades was an increase of 49% of its existing rate base.

1 The continuation of construction accounting for the Iatan 1 environmental upgrades
2 was authorized through the Commission's approval of the *Non-Unanimous Stipulation and*
3 *Agreement* in Case No. ER-2009-0089 for KCPL and Case No. ER-2009-0090 for GMO-
4 L&P. For these upgrades the continuation of construction accounting was calculated on the
5 amount not already included in the cost of service in the respective cases, which is slightly
6 different than what KCPL is requesting in this case, but the principle is generally the same. In
7 that instance of construction accounting, depreciation and carrying costs accrued on the
8 amount greater than the amount included in rates until the effective date of rates in the next
9 succeeding rate case.

10 Empire's 12% share of the expenditures related to the Iatan 1 environmental upgrades
11 received continuation of construction treatment authorized by Commission approval of the
12 *Stipulation and Agreement* in Case No. EO-2005-0263, more commonly referred to as
13 Empire's "Experimental Regulatory Plan" docket. Empire's share of the Iatan 1 upgrades
14 was an increase of 7% of its existing rate base. However, in the same time frame that these
15 upgrades were being constructed, Empire was participating in the construction of Iatan 2 and
16 Plum Point, as discussed later in this testimony. These three investments in combination
17 represented \$363.5 million Missouri jurisdictional investment, increasing Empire's rate base
18 from Case No. ER-2010-0130 by 50%.

19 Q. Briefly describe Iatan 2 and the use of continuation of construction accounting
20 for that project.

21 A. Iatan 2 is a 850 MW supercritical coal-fired baseload unit completed in
22 August 2010. Iatan 2 is owned 54.71% by KCPL, 18% by GMO, 12% by Empire, with the
23 remainder owned a power cooperative and a municipal entity. This was the first baseload unit

1 constructed by KCPL since Wolf Creek and was completed at a cost of approximately
2 \$2 billion, \$525.6 million of which was KCPL's Missouri jurisdictional share, and this new
3 unit represented an increase of 34% of existing rate base for that Company.

4 The continuation of construction accounting for Iatan 2 was authorized through the
5 Commission's approval of the *Stipulation and Agreement* in Case No. EO-2005-0329, more
6 commonly referred to as KCPL's "Experimental Regulatory Plan" docket, for KCPL's
7 ownership share. The use of construction accounting for KCPL's share of Iatan 2 was based
8 on a negotiated settlement reached between the signatory parties to Case No. EO-2005-0329,
9 including KCPL and Staff. Essentially, each party received some type of value from the
10 settlement which included allowing KCPL to use construction accounting for this project.
11 Other parties received benefits from other aspects of the settlement.

12 For GMO's share of Iatan 2, the Parties to Case No. ER-2010-0356 agreed in the
13 *Stipulation and Agreement / Proposed Procedural Schedules* that GMO would file an
14 application for an AAO requesting continuation of construction accounting, and that the non-
15 utility Signatory Parties would not oppose the AAO. The Commission authorized GMO's
16 AAO, Case No. EU-2011-0034, effective October 8, 2010. GMO's share of Iatan 2
17 represented an increase of 18% and 36% of GMO-MPS and GMO-L&P rate base,
18 respectively.

19 Empire's 12% share of the expenditures related to Iatan 2 received continuation of
20 construction accounting treatment authorized by Commission approval of the *Stipulation and*
21 *Agreement* in Case No. EO-2005-0263, more commonly referred to as Empire's
22 "Experimental Regulatory Plan" docket. Empire's share of Iatan 2 represented an increase of
23 34% of its Missouri jurisdictional rate base.

1 Q. Briefly describe Plum Point and the use of continuation of construction
2 accounting for that project.

3 A. Plum Point is a 665 MW coal-fired baseload generating unit located in
4 Osceola, Arkansas completed in August 2010. Empire owns 50 MW of the unit and leases an
5 additional 50 MW portion. Empire's share of Plum Point was completed at a cost of \$105
6 million, \$87.5 million of which was Empire's Missouri Jurisdictional share, and this new unit
7 represented an increase of 13% of existing rate base.

8 For Empire's share of Plum Point, the Parties to Case No. ER-2010-0130 agreed in the
9 *Stipulation and Agreement* that Empire would file an application for an AAO requesting
10 continuation of construction accounting, and that the non-utility Signatory Parties would not
11 oppose the AAO. The Commission authorized Empire's AAO, Case No. EO-2010-0262,
12 effective May 15, 2010.

13 Q. Briefly describe the Sioux environmental upgrade project and the use of
14 continuation of construction accounting for that project.

15 A. Sioux is a two-unit coal-fired generating station wholly owned by Ameren
16 Missouri (Ameren). Ameren constructed scrubbers on both units for reduction of SO2
17 completed at a cost of \$574 million, Ameren's Missouri Jurisdictional share, and this
18 construction project represented an increase of 9% of existing rate base.

19 The continuation of construction accounting for the Sioux environmental upgrades
20 was authorized through the Commission's approval of the *First Non-Unanimous Stipulation*
21 *and Agreement* in Case No. ER-2010-0036.

22 Q. How much is the LaCygne environmental project in total, compared to
23 KCPL's existing rate base?

1 A. The LaCygne environmental project's budget is \$1.23 billion. Using KCPL's
2 \$336 million figure from witness Klote's direct testimony, the LaCygne investment is 16% of
3 the same rate base. LaCygne represents a relative portion of existing rate base lower than
4 KCPL's share of Iatan 1 environmental upgrades and Iatan 2.

5 Q. What can be surmised concerning the historical use of the continuation of
6 construction accounting?

7 A. In every instance of the authorization of construction accounting in recent
8 memory, the Commission approved a stipulation and agreement in which the parties, through
9 negotiation, arrived at an agreement to not oppose, if not affirmatively recommend the use of
10 construction accounting. Implicit in every Stipulation and Agreement before the Commission
11 is a compromise of some sort between the parties to the agreement. The basic nature of a
12 compromise is that the parties saw value in terms of the agreement that may or may not have
13 been the original position of the parties, but that by agreeing to the terms they were mitigating
14 items that would cause the parties to reject the overall agreement.

15 Also in every recent instance of the authorization of construction accounting, the
16 recommendation to the Commission or stipulation and agreement by the parties was made
17 concurrently with general rate case proceedings often with the investment in question being
18 sought for inclusion in the cost of service. In general rate case proceedings, all relevant factors
19 are subject to consideration. Every general rate case normally reflects additional investment
20 in plant-in-service by the utility, as well as additional accumulated depreciation calculated on
21 existing plant-in-service from the prior rate case. Plant construction projects are routinely
22 included in rate base investment to establish the cost of service; the magnitude of KCPL's
23 investment aside, the LaCygne project is no different than any other construction project.

1 In this case, KCPL has requested the construction accounting treatment outside the
2 rate case process, which to Staff's knowledge has not been requested since the 1991 Sibley
3 cases. Staff believes KCPL's request in this case is premature as there is a pending rate case,
4 but no procedural schedule has been ordered and, therefore, Staff does not know for certain
5 what the final cost of the LaCygne project will be, when it will be considered to be in-service,
6 the date of new rates KCPL will receive as a result of its pending general rate case, and how
7 material the financial impact of any deferral will be in light of KCPL's Missouri earnings
8 levels. Staff will need to complete the rate case audit to determine whether construction
9 accounting is truly needed and, if so, what terms and conditions should be applied to it.
10 At this time, KCPL's request for construction accounting only identifies an estimate for the
11 financial impact of the proposed LaCygne project deferral. KCPL has also made no attempt
12 to consider any offsets that may be appropriate to determine the proper construction
13 accounting costs, if construction accounting is even considered necessary.

14 Q. How is KCPL's application different from traditional AAO applications?

15 A. KCPL's application is based on costs that will be incurred in the future, far
16 different than any AAO application in recent memory. The LaCygne environmental project is
17 scheduled to become used and useful and in-service sometime in the first and second quarters
18 of 2015. Traditional AAO applications, such as those for "act of God" weather events, are
19 after the fact applications when the event and the related costs are actual and known and
20 measurable to a high degree of accuracy.

21 KCPL is requesting continuation of construction accounting on assets which will be
22 in-service and assumedly included in the new rates that result in KCPL's filed rate Case No.
23 ER-2014-0370. The true-up date and the effective date of rates, which have yet to be

determined, will have a significant impact on the amount of the deferral. Using KCPL's calculations, each additional month of deferral through the effective date of new rates will add \$1.9 million to the deferral.

COMMISSION STANDARDS FOR DEFERRAL

Q. Can you identify the historical standards for deferral this Commission has held?

A. The Commission standards for deferral of expenses originate from the Sibley Order. These are the two standards:

- 1) The costs relate to an event that is extraordinary, unusual and unique, and not recurring, and
- 2) The costs associated with the event are material.

Q. How does the USOA define "extraordinary"?

A. Extraordinary, as defined by FERC USOA General Instruction 7 is as follows:

7. Extraordinary Items

It is the intent that net income shall reflect all items of profit and loss during the period with the exception of prior period adjustments as described in paragraph 7.1 and long-term debt as described in paragraph 17 below. Those items related to the effects of events and transactions which have occurred during the current period and which are of unusual nature and infrequent occurrence shall be considered extraordinary items. Accordingly, they will be events and transactions of significant effect which are abnormal and significantly different from the ordinary and typical activities of the company, and which would not reasonably be expected to recur in the foreseeable future. (In determining significance, items should be considered individually and not in the aggregate. However, the effects of a series of related transactions arising from a single specific and identifiable event or plan of action should be considered in the aggregate.) To be considered as extraordinary under the above guidelines, an item should

1 be more than approximately 5 percent of income, computed
2 before extraordinary items. Commission approval must be
3 obtained to treat an item of less than 5 percent, as
4 extraordinary. (See accounts 434 and 435.)

5 Q. USOA General Instruction 7 identifies a materiality standard for extraordinary
6 items as being more than 5% of net income. Can KCPL's application be judged to be
7 extraordinary by this standard?

8 A. No. The USOA standard for extraordinary treatment is a *historical cost*
9 standard. That is, if a utility believes an extraordinary event has occurred it would compute
10 net income before the impact of the item. Because KCPL has filed this AAO *before* any of
11 the actual expenses have been incurred, no one can judge what KCPL's net income will be in
12 the future, what the construction accounting amounts will be and whether or not these
13 expenses would be 5% of that amount.

14 Q. Has the Commission used this standard to determine if an AAO is appropriate?

15 A. While the 5% test in General Instruction 7 can be one factor, the Commission,
16 as noted in the Sibley Order, determined the materiality of the expenses is "also important, but
17 not a primary concern." The Commission has in the past required that costs be extraordinary
18 in nature to be eligible for deferral, with the materiality of the amount to be deferred as a
19 secondary consideration for deferral.

20 Extraordinary relates to the nature of the event in which a cost was incurred.
21 Materiality relates to the overall magnitude of the cost. Costs can be extraordinary but not
22 material, material but not extraordinary, or both, or neither. In this case, the fact that a large
23 investment will be declared in-service before rates reflect the return on and return of that
24 investment might be material but is not relevant to a determination of whether the costs can be
25 reasonably determined to be extraordinary in nature.

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Q. Are the costs KCPL seeks to defer unusual and unique?

A. No. As an electric utility, KCPL is continually building new plant, retiring and replacing old plant, and making capital improvements in all aspects of generation, transmission, and distribution as a vertically integrated utility. KCPL has had a long history of making significant capital additions as a regulated utility. Staff has identified several major investments KCPL has made without the use of construction accounting and in some cases without immediate rate relief:

Generating Unit	Year Completed	Missouri Jurisdictional Plant Amount, ER-2006- 0314
West Gardner Units 1-4	2003	\$ 63,567,824
Osawatomie	2003	\$ 16,833,624
Hawthorn 6	1997	\$ 23,396,286
Hawthorn 9	2000	\$ 39,174,555
Hawthorn 7 & 8	2000	\$ 27,997,459
Total		\$ 170,969,748
True-up Rate Base, ER-2006-0314		\$ 1,250,250,731
Percentage of Construction to Rate Base		13.7%
Spearville Wind	2006	\$ 84,759,931
Percentage of Construction to Rate Base with Spearville Wind		20.5%

The table above is a list of the investments Staff included in KCPL's rate base in the true up of Case No. ER-2006-0314 ("2006 Rate Case"). The 2006 Rate Case was KCPL's first rate case since 1985. In the interim, KCPL completed construction of several combustion turbines and a combined cycle unit, Hawthorn 9. KCPL did not receive direct rate relief for the assets until January 1, 2007, the date of rates in the 2006 Rate Case; several years after the assets were constructed and dedicated to utility service. The investments represented 13% of KCPL's Missouri jurisdictional rate base in the 2006 Rate Case. In addition to these assets,

KCPL completed the Spearville 1 wind farm and it was also included in the 2006 Rate Case. Combined, these assets represented 20% of KCPL's Missouri jurisdictional rate base in the 2006 Rate Case. Yet, KCPL never requested nor did it receive construction accounting on any of these investments. This rate case was completed at a time when KCPL was in a significant construction cycle with large retrofit projects at LaCygne 1 and Iatan 1, and the construction of Iatan 2.

In this case, KCPL has determined the LaCygne environmental project is projected to equal 16% of the rate base in the 2012 Rate Case. KCPL has in the past completed construction with an approximate magnitude of its current investment in LaCygne without the use of construction accounting.

Q. What amount of construction investment has KCPL made in the recent past and what are the budgeted amounts for future construction?

A. The responses to Staff Data Requests Nos. 6, 6.1, and 6.2 detailed the actual and budgeted amounts of KCPL construction expenditures from 2007-2018:

Year	KCPL Construction Budget in Millions	Actual/Budget
2007	** _____ **	Actual
2008	** _____ **	Actual
2009	** _____ **	Actual
2010	** _____ **	Actual
2011	** _____ **	Actual
2012	** _____ **	Actual
2013	** _____ **	Actual

Year	KCPL Construction Budget in Millions	Actual/Budget
2014	** _____ **	Budget
2015	** _____ **	Budget
2016	** _____ **	Budget
2017	** _____ **	Budget
2018	** _____ **	Budget

1
2 This data, which includes the timeframe for construction of the LaCygne project, shows no
3 discernable trend in KCPL's construction expenditures and no overall upward trend. The data
4 does show that KCPL is a utility that will have significant ongoing investment in the near
5 future and that the LaCygne environmental project should not be viewed as unusual or unique.

6 Q. Are the costs KCPL seeks to defer non-recurring?

7 A. No. Again, as a vertically integrated utility, KCPL is constantly constructing
8 new assets and replacing old assets. While it can be argued that the specific environmental
9 project being constructed at LaCygne is non-recurring in its own right, this assertion does not
10 make the in-service of this equipment a unique, non-recurring, or extraordinary event worthy
11 of AAO treatment.

12 The costs for which KCPL is requesting deferral treatment result from basic operating
13 decisions made by KCPL in response to the need to build and maintain sufficient generating
14 capacity to service its customers with an adequate reserve. All electric utilities in this state
15 are faced with the same fundamental issue of capacity planning that is basic to providing
16 electric service to the public. KCPL is not at all unique in Missouri in considering and
17 carrying out unit environmental retrofits. In fact, Empire is currently completing a large

1 environmental construction project at its Asbury generating station, but has not requested and
2 is not receiving construction accounting treatment for that asset. Empire completed several
3 major plant additions for its State Line Combustion Turbine and State Line Combined Cycle
4 units completed in the late 1990s and 2001, yet received no construction accounting.
5 Empire has also added plant at its Energy Center and Riverton stations, again with no
6 construction accounting.

7 In regards to environmental compliance, KCPL is no stranger to capital investment to
8 meet the requirements of governmental mandates. Iatan 1 has been retrofitted and KCPL
9 completed an SCR upgrade at LaCygne 1 in 2007. Hawthorn 5 was retrofitted during its
10 reconstruction from the February 1999 explosion, but did not receive construction accounting.
11 KCPL's affiliate, KCP&L GMO has made several investments to comply with environmental
12 rules at Sibley 3 and Jeffrey Energy Center without the need for construction accounting.
13 These types of investments and the resulting expenses of committing them to service are
14 clearly not non-recurring.

15 Another way to evaluate whether expenses are non-recurring is if they can be planned
16 ahead of time by a utility and considered in the appropriate time a utility would file for rate
17 relief. The LaCygne environmental project was contemplated by KCPL since late 2007 and
18 has been under construction since mid-2011. This contrasts with typical "act of God"
19 extraordinary events such as major ice storms, floods, and other weather events which can be
20 prepared for, but cannot be predicted or controlled. KCPL has planned the LaCygne
21 environmental project, knows with some degree of accuracy when it will be dedicated to the
22 provision of utility service, and has filed a rate case before the Commission to include the
23 expenses related to the project in its cost of service. There is nothing unpredictable about

1 these events and KCPL has complete control of when it will file rate cases and complete
2 control of the management of the LaCygne environmental project.

3 Q. Are the costs KCPL seeks to defer material?

4 A. In the Sibley Case, the Commission referenced USOA General Instruction 7
5 which sets out a materiality standard that events that have an impact on net income of more
6 than 5% are presumed to be subject to special accounting treatment as extraordinary events,
7 with specific Commission authorization needed if a utility seeks to treat as extraordinary a
8 cost amounting to less than 5% of net income. However, any specific materiality test relating
9 to a LaCygne project deferral would not be strictly applicable at this time as the costs in
10 question have yet to occur. Generally speaking, adding large generating assets to a
11 company's rate base, and their resulting expenses such as depreciation, are material to a
12 utility's cost structure. But major plant additions do not by themselves create the need to
13 change rates as can be seen by the period before the 2006 Rate Case when KCPL completed
14 \$170 million of plant (Missouri jurisdictional) not only without construction accounting but
15 also without immediate rate relief—in fact did not have rate relief for some of these units for
16 several years after the units were completed.

17 At the time KCPL filed its request for this AAO in June, current rates had been in
18 effect for a year and a half, with no pending rate case. A premise of utility regulation is that,
19 until the point when a utility files for a rate increase, it must be presumed that it is covering all
20 of its current costs through its ongoing rate levels and therefore, rates are adequate. If a utility
21 determined it was consistently earning below its authorized rate of return, logic would dictate
22 that the utility should file for a rate increase. KCPL has determined that its current revenue
23 levels do not support its cost of service and has filed a rate case to recover the very expenses

1 for which it is requesting for deferral in this case, among other items. In fact, a central
2 element of KCPL's filed rate case is the inclusion of the LaCygne environmental project in
3 the cost of service when it is dedicated to utility service. While the audit is underway, Staff
4 has yet to make the determination if KCPL's revenues adequately support its cost of service
5 and will do so in KCPL's current filed case.

6 Q. Did KCPL address materiality in its direct testimony filed in this case?

7 A. No. However, in a filing before the Commission in Case No. EU-2015-0094,
8 Staff's petition concerning the DOE fees, KCPL stated its belief that \$2.36 million in annual
9 expense does not meet the Commission's materiality threshold. Staff disputes not only
10 KCPL's quantification of the amount of the fees, but also KCPL's assessment of materiality.
11 Staff's calculations at this time result in an estimate of the LaCygne construction accounting
12 deferral to be approximately \$5.8 million. Staff has identified \$3.5 million of savings related
13 to the DOE fees that are no longer being paid. Based on prior Commission guidance that
14 the 5% materiality standard is not to be strictly applied, Staff believes the materiality of
15 both items is large enough to potentially justify deferral treatment if the costs associated
16 with the events would otherwise qualify for deferral. Staff believes KCPL's contention in
17 EU-2015-0094 has no merit and is opposite of its position in this AAO Application.

18 **STAFF RECOMMENDATION**

19 Q. Given the facts and evidence in this testimony, what is Staff's recommendation
20 regarding KCPL's request for construction accounting?

21 A. Staff recommends the Commission reject KCPL's request for construction
22 accounting for the following reasons:

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- 1) The expenses KCPL seeks to defer do not meet the Commission's standards for deferral. The expenses are not extraordinary, unique and unusual, and are not non-recurring;
- 2) The expenses KCPL seeks to defer have not actually occurred, and will not occur until the second quarter of 2015, therefore the materiality of the requested deferral cannot be accurately evaluated;
- 3) KCPL has had levels of investment similar to the amount of the LaCygne environmental project in the recent past without the use of construction accounting;
- 4) The LaCygne environmental project does not rise to the level of most other investments that have been granted construction accounting by the Commission; and
- 5) The construction accounting costs for the LaCygne environmental project have not been adequately determined by KCPL in its proposal filed in this case. There are several offsets that should be considered reducing KCPL's calculations.

However, if the Commission approves KCPL's application for construction accounting, Staff recommends several modifications be made to KCPL's calculations and that several offsets be ordered to the amount of the deferral.

STAFF'S RECOMMENDED MODIFICATIONS AND OFFSETS

Q. If the Commission approves KCPL's application, does Staff recommend any modifications to KCPL's proposed construction accounting calculations or offsets to the amount of the deferral?

A. If the Commission approves KCPL's application, Staff recommends the following modifications be ordered to KCPL's construction accounting calculations:

- 1) Offset the base on which carrying costs are calculated by the additional non-environmental LaCygne depreciation reserve from the true-up date through the effective date of rates.

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- 2) Offset the base on which carrying costs are calculated by the monthly depreciation expense deferral recorded to the regulatory asset.
- 3) Offset the base on which carrying costs are calculated by the accumulated deferred income taxes created by the LaCygne environmental plant.
- 4) Offset the base on which carrying costs are calculated by the accumulated deferred income taxes created by the monthly regulatory asset deferral.
- 5) Use actual depreciation and carrying costs based on the actual unadjusted AFUDC rate, less Staff's adjustment to the equity rate, with an estimate based on actuals for amounts calculated after the true-up in Case No. ER-2014-0370.
- 6) For the calculation of AFUDC rate, a 250 basis point (2.50%) reduction should be assumed in the cost rate of common equity component of the AFUDC rate.
- 7) No additions to the base on which carrying costs or depreciation are calculated after the true-up in Case No. ER-2014-0370.
- 8) No additional deferrals after the effective date of rates in Case No. ER-2014-0370.

Staff would also recommend offsetting the amount of the deferral by the following items:

- 1) The amount of over collected expired and / or expiring amortizations of other regulatory assets, and
- 2) The amount currently collected in rates for the Department of Energy (DOE) Nuclear Waste Fund fees, which have been reduced to \$0 addressed in Case No. EU-2015-0094.

Each of these modifications will be discussed further in this testimony.

ADDITIONAL DEPRECIATION RESERVE – ADJUSTMENTS 1 AND 2

Q. How should additional depreciation reserve offset the base on which carrying costs are calculated, Adjustment 1 recommended by Staff?

1 A. The next KCPL rate case will presumably include a true-up of costs as of a
2 certain cutoff date which will include an amount of accumulated depreciation reserve on all
3 KCPL plant investment, likely at May 31, 2015. The continuation of construction accounting
4 provides earnings protection for a utility through the effective date of rates. Generally
5 speaking, the amount of accumulated reserve would increase between the true-up cutoff and
6 the effective date of rates, reducing rate base and consequently the revenue requirement.

7 To most accurately reflect the actual investment and financial impact of construction
8 accounting, the additional depreciation reserve on all plant investment at LaCygne should
9 be included as an offset to the base on which carrying costs should be accrued. As the
10 actual depreciation amounts will not be known until the update and true-up periods in Case
11 No. ER-2014-0370, Staff does not know the actual amount of the offset. An approximation
12 of this amount could be determined at the time of the true-up similar to what KCPL
13 proposal contemplates for the construction accounting costs through the effective date of
14 rates. The amount would offset the carrying cost base for the months between the true-up and
15 effective date of rates.

16 Q. In reference to Staff Adjustment 2, why should the amount of depreciation
17 included in the construction accounting deferral be removed from the amount on which
18 carrying costs are calculated?

19 A. Depreciation is the recovery of the investment in an asset or group of assets.
20 Carrying costs are determined by applying a carrying cost rate to the unrecovered investment.
21 The unrecovered investment is determined by reducing the investment by accumulated
22 depreciation. Depreciation does not begin to be calculated until an asset is completed and
23 included in plant in service; no depreciation is calculated for Construction Work In Progress

1 (CWIP). Therefore, CWIP carrying costs (AFUDC) are calculated on the dollars invested in
2 CWIP without regard to depreciation.

3 KCPL has calculated carrying costs based on the gross investment in the LaCygne
4 environmental project without consideration of depreciation. However, KCPL has also added
5 depreciation expense to the total cost of the AAO deferral. It would be appropriate to
6 calculate carrying costs without consideration of depreciation if KCPL did not add
7 depreciation expense to the deferral. If depreciation expense is to be added to the deferral
8 then KCPL should not also receive carrying costs on the depreciation expense. In other
9 words, carrying costs should be calculated only on the unrecovered investment: gross
10 investment less depreciation expense.

11 **ACCUMULATED DEFERRED INCOME TAXES – ADJUSTMENTS 3 AND 4**

12 Q. What are accumulated deferred income taxes (ADIT)?

13 A. ADIT are assets or liabilities that represent the cumulative amount of
14 additional income taxes owed to or previously paid to the Internal Revenue Service (IRS), in a
15 different period in which the financial impact of the income taxes is reported in the utilities'
16 financial statements according to Generally Accepted Accounting Principles (GAAP). The
17 Internal Revenue Code (IRC) governs the methods of determining taxable income which
18 often differ from GAAP, creating timing differences between taxes actually paid and income
19 tax expense for financial reporting purposes. For regulated utilities the largest and most
20 common category of timing differences occur when depreciating property, plant, and
21 equipment which result in a difference between the tax deduction and book deduction
22 amounts for depreciation. The IRS contains provisions for accelerated depreciation which
23 creates a larger deduction resulting in a lower income tax cost paid to the IRS and subsequent

1 current income tax liability than the amount of income taxes determined for book depreciation
2 and regulatory purposes. Utility rates reflect the tax deduction for book depreciation resulting
3 in a larger income tax expense for regulatory purposes compared to the actual amount paid to
4 the IRS using the higher accelerated depreciation deduction. The difference between the
5 actual amounts paid the IRS using the higher accelerated depreciation and the amount of the
6 income taxes for book purposes determined using the lower depreciation on straight line
7 method is referred as tax timing difference. This tax timing difference results in deferred
8 income taxes—treated as a deferred liability on the utility’s books. The deferred income tax
9 is a cumulative liability and represents a net prepayment of income taxes by KCPL’s
10 customers in rates before the actual payment of the income taxes to the IRS. This prepayment
11 is a cost-free source of capital to KCPL and is therefore not included in the net investment
12 upon which KCPL earns a return when establishing rates, also referred to as a “rate base
13 offset.” Deferred taxes are included as a reduction to rate base in every case Staff calculates a
14 revenue requirement.

15 This immediate benefit is to the utility when it takes the higher tax deduction than
16 what is allowed in rates. But ratepayers do benefit from the deferred taxes as it does generate
17 a source of cost-free capital that reduces the capital requirement in the cost of service and is
18 therefore reflected as a rate base offset. While the benefit is temporary for each individual
19 asset, an electric utility normally replaces capital assets on a continual basis, creating
20 additional deferred tax benefits each year.

21 Q. Are there other items that produce book-tax timing differences?

22 A. Yes. Other timing differences create deferred tax assets or liabilities
23 depending on the difference between deductibility for tax purposes and determining book

1 income. One of these differences relates to regulatory assets or liabilities created by an order
2 by the Commission.

3 For example, the Commission has in the past authorized utilities to record a regulatory
4 asset for the amount of rate case expenses incurred with an amortization period of several
5 years. For this timing difference, there is no special treatment for tax purposes and the entire
6 amount was deducted in the year incurred, but for financial reporting purposes the amount is
7 reported pursuant to the amortization period.

8 Missouri utilities usually have a myriad of regulatory assets and liabilities which in
9 turn produce deferred tax timing differences.

10 Q. How and why should deferred income taxes offset the amount of the base on
11 which carrying costs are calculated, Adjustments 3 and 4 recommended by Staff?

12 A. There are two categories of deferred taxes that should be considered.

13 The first category of deferred taxes is the deferred taxes accrued on the LaCygne
14 environmental equipment from the date of in-service through the effective date of rates. Once
15 an asset is declared in-service and used in the production of electricity, depreciation is
16 charged to income. As explained above, accelerated tax depreciation in excess of book
17 depreciation creates ADIT which is a source of cost-free capital to the utility. Although the
18 actual income taxes may not be paid until some point in the future, the financial impact of the
19 deferred tax accumulation should be considered as an offset to the accrual of carrying costs, in
20 this case the reduction of the proposed construction accounting.

21 KCPL has not proposed to reduce the LaCygne environmental construction accounting
22 in its application for the amount of deferred taxes. Staff believes this is a deficiency in
23 KCPL's proposal.

1 The second category of deferred taxes is the deferred taxes accrued on the deferral of
2 the regulatory asset, comprised of depreciation and carrying costs. For each month these
3 expenses are deferred, ADIT is accrued on the amount. For income tax purposes, the
4 expenses charged to the deferral are deductible in the year incurred; there is no special
5 treatment for tax purposes. For financial reporting purposes, the deferral would be charged to
6 income (expensed) over the amortization period; in this case, for the remaining service life of
7 LaCygne. Since there is a higher tax deduction in the first year, the Company reduces its
8 income tax expense for tax purposes but does not do this for ratemaking purposes. This
9 difference between tax treatment and book treatment creates the ADIT balance, similar to
10 accelerated depreciation, and should be considered in the calculation of the carrying costs.

11 **CARRYING COST RATE AND EQUITY RATE ADJUSTMENT – ADJUSTMENT 5**

12 Q. If the Commission approves KCPL's application, what carrying cost rate does
13 Staff recommend be used to calculate carrying costs?

14 A. Staff recommends the actual AFUDC rate be used as the starting point in
15 calculation of the carrying costs instead of an estimate as KCPL proposes. This rate is
16 calculated monthly based on a specific formula found in the USOA. Staff is proposing to
17 employ the same calculation for carrying costs that is used by KCPL to accrue AFUDC on the
18 LaCygne environmental project during its construction period.

19 The LaCygne construction accounting deferral is unique in that rate recovery of the
20 deferral would occur immediately after the asset is created. If the construction accounting
21 deferral receives rate recovery in the current rate Case No. ER-2014-0370, the most current
22 data would be based on the AFUDC rate and carrying cost base as of the true-up. Because the
23 ultimate amount of the deferral must be determined at the time of the true-up for

determination of KCPL's cost of service, even before the actual deferral is made, the actual carrying cost rate after the true-up would not be known. Staff would recommend the Commission use an average of the AFUDC rate used for the months prior to the true-up for the carrying cost rate after the true-up to calculate the deferral.

Q. What carrying cost rate does KCPL recommend for the deferral?

A. KCPL has recommended an estimated rate of 4.67%. Staff believes this rate is substantially higher than the actual AFUDC rate for KCPL that will be in effect after the LaCygne environmental project is completed. While Staff believes the LaCygne environmental costs should not receive construction accounting, if the Commission allows KCPL such treatment, Staff believes the actual, and likely lower AFUDC be used to determine the deferral.

CARRYING COST RATE AND EQUITY RATE ADJUSTMENT – ADJUSTMENT 6

Q. Are there any adjustments to the AFUDC rate that should be made?

A. Yes. The AFUDC rate is calculated using several component rates contained within the overall cost of capital calculation: short-term debt, customer deposits, long-term debt, and equity rates. Staff recommends a 250 basis point (2.50%) reduction be assumed in the cost rate of common equity component of the AFUDC rate. The USOA defines the cost of equity rate used in the overall AFUDC calculation as follows:

The cost rate for common equity shall be the rate granted common equity shall be the rate granted common equity in the last rate proceeding before the ratemaking body having primary rate jurisdictions. If such cost rate is not available, the average rate actually earned during the preceding three years shall be used.

(FERC USOA Paragraph 18, Subpart (b))

1 The return on equity rate currently being used in KCPL's AFUDC calculation is 9.7%, the
2 return on equity authorized for KCPL in Case No. ER-2012-0174. Generally, the return on
3 equity compensates shareholders for the risks inherent in owning equity in a utility. Part of
4 that risk is regulatory lag, both positive and negative. If the Commission authorizes the
5 continuation of construction accounting for the LaCygne environmental project, a substantial
6 amount of risk to shareholders will be removed. To reflect this reduction in risk a
7 complementary reduction in the equity rate used to calculate for construction accounting
8 carrying costs should be used.

9 Q. Has the equity rate been reduced in prior instances when continuation of
10 construction accounting was authorized?

11 A. Yes. The continuation of construction accounting authorized by the
12 Commission for Iatan 2 included a reduction in the equity rate for carrying costs for
13 both the AFUDC accrued during construction and the carrying costs for the deferral.
14 This was included as part of the Regulatory Plan authorized by the Commission in Case No.
15 EO-2005-0329. This reduction was 250 basis points (2.50%), the same reduction Staff
16 recommends for this deferral, if the Commission approves KCPL's application.

17 For Staff's estimated calculation of the LaCygne deferral, Staff used the actual
18 average AFUDC rate for January through June 2014, reduced by the amount of LaCygne
19 CWIP, and with Staff's recommended 2.5% equity rate adjustment. While these calculations
20 are estimates, they are a better approximation of the actual AFUDC rate than KCPL's
21 recommended rate.

22 **LIMITS TO THE DEFERRALS – ADJUSTMENTS 7 AND 8**

23 Q. Please explain adjustments 7 and 8.

1 A. These can be described more as conditions than adjustments.

2 Staff recommends the base on which carrying costs are calculated does not increase
3 after the amount determined at the true-up. Any additional plant becoming in-service after the
4 true-up would not receive construction accounting deferral treatment as the amounts would be
5 based on estimates.

6 Staff also recommends no additional deferrals after the effective date of rates. This is
7 the same methodology as the construction accounting authorized for KCPL's portion of
8 Iatan 2. The rate case true-up process captures the relationship between investment, expenses
9 and revenue at a certain point in time to determine KCPL's cost of service. The rates
10 established in the next case will assumedly reflect the investment in LaCygne at the time of
11 the true-up, as well as the amortization of deferred depreciation and carrying cost, if the
12 Commission authorizes KCPL's application. These rates will accurately reflect KCPL's cost
13 of service, therefore there would be no justification to defer additional amounts when rates
14 already reflect these expenses.

15 **EXPIRING AMORIZATIONS OF OTHER REGULATORY ASSETS –**
16 **ADJUSTMENT 9**

17 Q. What are the amortizations that should offset the amount of the deferral for the
18 continuation of construction accounting, if it is approved?

19 A. If the Commission approves KCPL's application, Staff recommends the total
20 amount of the deferral should be offset by over-collections of the amortization of other
21 regulatory asset deferrals currently being recovered in rates by KCPL. These regulatory
22 assets have been established in prior cases and amortized and recovered in the cost of service.
23 Once a regulatory asset has been fully amortized, a utility will begin to over-collect that

1 regulatory asset and its earnings will increase, all other things being equal. Staff has in prior
2 circumstances reflected over-collections of regulatory assets as an offset to recovery of other
3 regulatory assets. KCPL's rate case expense regulatory assets have been offset in this manner
4 by expired amortizations of prior rate case expense regulatory assets.

5 Over collections of tracker deferral amortizations are also considered in the calculation
6 of pensions and OPEBs in rate cases.

7 Staff has calculated a \$2.3 million over-collection of the amortization expense
8 associated with these regulatory assets through the projected effective date of new rates
9 resulting from KCPL's current rate case, Case No. ER-2014-0370. This over-collection total
10 is related to the items listed below:

- 11 • R&D Consulting Fees – The deferred consulting fees for research
12 and development (R&D) tax credits from the 2007 Rate Case,
13 Case No. ER-2007-0291, an annual amortization of \$78,845. The
14 last month of the amortization period was August 2014 and results
15 in an over-collection of \$85,635.
- 16 • Missouri Rate Case – The deferred rate case expenses from the
17 2010 KCPL Rate Case, Case No. ER-2010-0355, an annual
18 amortization of \$1.29 million. The last month of the amortization
19 period was April 2014 and results in an over-collection of \$1.83
20 million.
- 21 • Economic Relief Pilot Program Vintage 1 – The deferred expenses
22 for KCPL's Economic Relief Pilot Program established in Case
23 No. ER-2009-0089, an annual amortization of \$85,642. The last
24 month of the amortization period was April 2014 and results in an
25 over-collection of \$121,564.
- 26 • Wolf Creek Refuel Outage #16 – The deferred expenses for Wolf
27 Creek Outage 16 established in Case No. ER-2009-0089, an
28 annual amortization of \$314,116. The last month of the
29 amortization period was August 2014 and results in an over-
30 collection of \$340,292.

1 Q. Why should these over collections offset the continuation of construction
2 accounting deferral?

3 A. These over collections represent amounts ratepayers have paid over and above
4 the amounts of the actual deferred assets agreed to be recovered in rates. KCPL in essence
5 has either currently over-collected the amounts from its customers or will do so before the
6 rates are changed in the pending 2015 rate case filed by KCPL. If the Commission orders
7 deferred treatment for the LaCygne construction accounting, the amount should be offset by
8 these over collections of other deferrals authorized by the Commission. Utilities should not
9 be allowed to unjustly gain as a result of extraordinary rate treatment through over-collection
10 of a deferred amount; the deferred asset should be collected, no more no less.

11 If the Commission does not authorize KCPL's AAO, Staff will address the appropriate
12 rate treatment of the Company's over-collections of regulatory asset amortizations in Case
13 No. ER-2014-0370. In any case, Staff does not believe utilities should be allowed to absorb
14 to the benefit of its shareholders over collections of AAO's, or any deferred amounts.

15 **DEPARTMENT OF ENERGY NUCLEAR WASTE FUND FEES – ADJUSTMENT 10**

16 Q. What are the Department of Energy (DOE) Nuclear Waste Fund Fees?

17 A. The Nuclear Waste Policy Act of 1982 authorized the DOE to enter into
18 contracts for the collection and disposal of spent nuclear fuel and high level waste. KCPL,
19 who owns 47% of Wolf Creek, was required to pay to the Nuclear Waste Fund 1 (one) "mil"
20 (1/10 of one cent, or 1/1000 of one dollar) per kilowatt-hour (kWh) of electricity produced at
21 Wolf Creek. In exchange, DOE would begin to dispose of spent nuclear fuel and high level
22 waste not later than January 31, 1998.

1 The DOE failed to meet its 1998 obligation and has not accepted any nuclear materials
2 for permanent storage. The fee was challenged in the courts and in late 2013, the United
3 States Court of Appeals issued its decision in *National Association of Regulatory Utility*
4 *Commissioners (NARUC) v. United States Department of Energy*, where it ordered the
5 Secretary of the DOE submit to the United States Congress a proposal to change the fee to \$0.
6 The DOE reduced the fee to the current level of \$0 (zero dollars) effective May 16, 2014.
7 Despite being reflected in utility rates which customers continue to pay, KCPL is no longer
8 incurring this fee resulting in a cost savings to KCPL.

9 Q. Provide a brief overview of Staff's petition to the Commission in Case No.
10 EU-2015-0094.

11 A. On October 9, 2014, Staff filed a Petition with the Commission to order KCPL
12 to record a regulatory liability based on the amount currently being paid in the Missouri
13 jurisdictional cost of service for the DOE Nuclear Waste Fund Fees which, as of May 16,
14 2014, are no longer being paid by KCPL. Mark Oligschlaeger, Manager of the Auditing Unit
15 and I filed direct testimony supporting this petition. Staff's Petition functions similarly to an
16 AAO. Staff believes the abrupt elimination of the fee customers have paid for 29 years to be
17 an extraordinary event and meets the Commission's prior standards for deferral. If ordered by
18 the Commission, KCPL would be required to establish a regulatory liability for the Missouri
19 Jurisdictional portion of the DOE fees currently being paid by customers during the period
20 May 16, 2014, the date the fee was reduced to \$0, through the effective date of rates in the
21 pending Case No. ER-2014-0370 when the reduced fee is reflected in the cost of service.
22 Staff has calculated this amount to be \$3.5 million, Missouri jurisdictional.

1 Q. If the Commission authorizes Staff's petition in that case, how might the
2 Commission treat any amounts deferred in future rate case?

3 A. In his direct testimony in Case No. EU-2015-0094, Mr. Oligschlaeger listed a
4 number of alternative ways the Commission might choose to reflect these deferrals in future
5 KCPL rate proceedings, including:

- 6 1) The deferred amount could be returned directly to customers over
7 a period of time through an amortization reducing KCPL's cost of
8 service in the 2015 general rate case;
- 9 2) The deferred amount could offset (reduce) future nuclear fuel
10 expenses charged to Account 518 that would otherwise be
11 included in KCPL's cost of service in a future general rate case;
- 12 3) The deferred amount could offset (reduce) a regulatory asset that
13 would otherwise be included in KCPL's cost of service in the 2015
14 general rate case; or
- 15 4) The deferred amount could be preserved on the books as a
16 regulatory liability to offset (reduce) future costs (expense or
17 capital investment) related to the storage of spent nuclear fuel and
18 high level waste.

19 This is not an exhaustive list and, again, the Commission has traditionally reserved any
20 ratemaking treatment for deferred amounts to a general rate proceeding.

21 Q. Should Staff's proposed accounting treatment for the DOE fees and KCPL's
22 AAO for LaCygne construction accounting be evaluated together?

23 A. While the applications relate to separate events, for a balanced approach the
24 applications could stand or fall together. Staff supports combining or consolidating these two
25 cases. In any event, Staff recommends that the two cases should be considered at the same
26 time according to the procedural schedule ordered for Case No. EU-2014-0255.

27 If the Commission authorizes construction accounting for the LaCygne environmental
28 project, Staff recommends the Commission also order that deferral to be offset (reduced) by

1 the amount Staff has requested to be returned to customers in Case No. EU-2015-0094.
2 KCPL Witness Klote stated that KCPL would be requesting recovery of the deferral of the
3 LaCygne project construction accounting costs in Case No. ER-2014-0370, and its direct filed
4 workpapers assume the Commission will approve its request and reflect recovery of the
5 amortization of KCPL's calculation of the LaCygne deferral. Offsetting the LaCygne deferral
6 by the DOE fee amount would be analogous to Option 3 as described above.

7 Staff's recommendation to offset the LaCygne environmental project construction
8 accounting deferral by the amounts paid for the DOE fees is based upon fundamental fairness,
9 and the need to maintain consistency and symmetry in the ratemaking process by recognizing
10 that cost reductions due to extraordinary events are just as important as cost increases due to
11 extraordinary events.

12 Q. Does KCPL indicate it needs Commission authority for its construction
13 accounting proposal before its 2014 books are closed?

14 A. Yes. KCPL has stated it needs authorization for its proposal regarding
15 construction accounting before its books are closed for calendar year 2014. Staff does not
16 believe this is necessary since the LaCygne environmental project is not planned for
17 completion until sometime in the 2nd quarter of 2015, and no deferral would be booked by the
18 Company until that time. However, because the DOE fees were eliminated March 2104, the
19 Commission needs to order KCPL to defer the impact those reduced costs prior to the close of
20 the calendar year 2014 books. In reality, there is a greater need for immediate Commission
21 action in Case No. EU-2015-0094 than in this case.

SUMMARY OF ADJUSTMENTS AND OFFSETS

Q. Can you provide a reconciliation of the Company's pro-forma deferral amounts and Staff's adjustments and offsets?

A. Below is a summary of the pro-forma deferrals and Staff's adjustments and offsets. It is important to note that due to the way KCPL has chosen to request its AAO, before the expenses in question have been incurred, the amounts are estimates but are believed by Staff to be reliable for purposes of determining if KCPL's petition should be approved or denied:

KCPL Calculation of the LaCygne Deferral	\$10,162,555
Staff Adjustments for Deferred Taxes & AFUDC Rate (Adjustments 1-5)	\$(4,359,963)
Staff Calculated LaCygne Deferral	\$5,802,592
Adjustment 8 – Expired Amortizations	\$(2,385,146)
Adjustment 9 – DOE Fees, Case No. EU-2015-0094	\$(3,530,553)
Net Total	\$(113,107)

Detailed calculations of Staff's estimated LaCygne deferral are attached as Schedule KM-4.

With Staff's adjustments to the LaCygne deferral, the amount should be \$5.8 million, as opposed to KCPL's calculated \$10.1 million. Staff's Petition in Case No. EU-2015-0094 identified a \$3.5 million regulatory liability that could offset that amount, to a net total of \$2.3 million. Taking KCPL's over collections of other deferral amortizations into account, there would be no expenses to defer as shown in the table above. Staff recommends that the

1 expired amortizations be considered as an offset to the LaCygne deferral, but alternatively,
2 they could be considered to offset other deferrals in the forthcoming rate case.

3 **OTHER MITIGATING COST DECREASES**

4 Q. On page 6 of KCPL witness Klote's Direct testimony, he discusses regulatory
5 lag. Is there a specific example related to KCPL that shows that regulatory lag can benefit
6 KCPL shareholders?

7 A. Yes. KCPL has reduced its employee headcount after its last rate case,
8 Case No. ER-2012-0174, by a net of ** ____ ** employees. The annual salaries, wages,
9 and benefits (0.6 adder) related to these employees are an annual savings to KCPL of
10 ** ____ **, approximately ** ____ ** Missouri jurisdictional. ** ____

11 _____
12 _____
13 ____ ** The savings related to this program is ** ____ **, total company.
14 Rates were set in KCPL's 2012 rate case, which went into effect January 2013, which were
15 based on including in KCPL's cost of service the higher costs for the higher level of employee
16 headcount and the ** ____ **.

17 These two cost reductions are examples of regulatory lag providing benefits to a utility
18 that offset against increases in other expenses and decreases in revenues.

19 **SUMMARY**

20 Q. Please summarize your rebuttal testimony.

21 A. Staff recommends the Commission reject KCPL's AAO application. The
22 expenses in question have not occurred and do not meet the Commission's standard of
23 extraordinary. The expenses are not unique and unusual, or non-recurring. The LaCygne

Rebuttal Testimony of
Keith Majors

1 environmental project does not rise to the level of other more substantial construction projects
2 that have been authorized for construction accounting. Therefore, KCPL's request to defer
3 costs relating to the LaCygne's environmental project and treated as construction accounting
4 should be denied.

5 If the Commission approves KCPL's application, Staff believes KCPL's calculation
6 for construction accounting is improper and should be adjusted for the effects of accumulated
7 depreciation, accumulated deferred income taxes and reduced AFUDC. Staff also
8 recommends the Commission should offset (reduce) the LaCygne deferral by the amount of
9 DOE fees identified in Case No. EU-2015-0094 and the amounts of over collected
10 amortizations paid by Missouri ratepayers.

11 Q. Does that conclude your rebuttal testimony?

12 A. Yes, it does.

BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

In the Matter of the Application of Kansas City)
Power & Light Company for the Issuance of an) Case No. EU-2014-0255
Order Authorizing Construction Accounting)
relating to its Electrical Operations)

AFFIDAVIT OF KEITH MAJORS

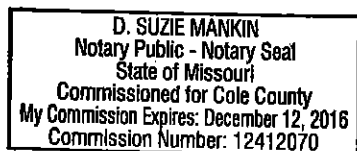
STATE OF MISSOURI)
)
COUNTY OF COLE) ss.

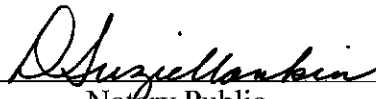
Keith Majors, of lawful age, on his oath states: that he has participated in the preparation of the foregoing Rebuttal Testimony in question and answer form, consisting of 51 pages to be presented in the above case; that the answers in the foregoing Rebuttal Testimony were given by him; that he has knowledge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



Keith Majors

Subscribed and sworn to before me this 14th day of November, 2014.





Notary Public

Keith Majors

Educational and Employment Background and Credentials

I am currently employed as a Utility Regulatory Auditor IV for the Missouri Public Service Commission (Commission). I was employed by the Commission in June 2007. I earned a Bachelor of Science degree in Accounting from Truman State University in May 2007.

As a Utility Regulatory Auditor, I perform rate audits and prepare miscellaneous filings as ordered by the Commission. In addition, I review all exhibits and testimony on assigned issues, develop accounting adjustments and issue positions which are supported by workpapers and written testimony. For cases that do not require prepared testimony, I prepare Staff Recommendation Memorandums.

Prior Case Assignments:

Case Name	Case Number	Issues	Exhibit
KCP&L	EU-2015-0094	DOE Nuclear Waste Fund Fees	Direct Testimony
KCP&L	EU-2014-0255	Construction Accounting	Rebuttal Testimony
Veolia Kansas City	HR-2014-0066	Income Taxes, Revenues, Corporate Allocations	Staff Report
Missouri Gas Energy	GR-2014-0007	Corporate Allocations, Pension & OPEB, Incentive Compensation, Income Taxes	Staff Report, Rebuttal, Surrebuttal
Missouri Gas Energy ISRS	GO-2013-0391		Staff Memorandum
KCP&L & KCP&L GMO	ER-2012-0174 & ER-2012-0175	Acquisition Transition Costs, Fuel, Legal and Rate Case Expense	Staff Report, Rebuttal, Surrebuttal
Missouri Gas Energy ISRS	GO-2011-0269		Staff Memorandum
Noel Water Sale Case	WO-2011-0328		Staff Recommendation
KCP&L & KCP&L GMO	ER-2010-0355 & ER-2010-0356	Acquisition Transition Costs, Rate Case Expense	Staff Report, Rebuttal, Surrebuttal
KCP&L Construction Audit & Prudence Review	EO-2010-0259	AFUDC, Property Taxes	Staff Report
KCP&L, KCP&L GMO, & KCP&L GMO – Steam	ER-2009-0089, ER-2009-0090, & HR-2009-0092	Payroll, Employee Benefits, Incentive Compensation	Staff Report, Rebuttal, Surrebuttal
Trigen Kansas City	HR-2008-0300	Fuel Inventories, Rate Base Items, Rate Case Expense, Maintenance	Staff Report
Spokane Highlands Water Company	WR-2008-0314	Plant, CIAC	Staff Recommendation
Missouri Gas Energy ISRS	GO-2008-0113		Staff Memorandum

Electric Rates Comparison

All figures are cents per kilowatt hour (kWh)

<u>Total Retail Rates</u>	<u>Year 2006 as of 1/1/06</u>	<u>EEI Reference</u>	<u>Year 2014 as of 7/1/14</u>	<u>EEI Reference</u>	<u>percentage change</u>
KCPL	5.66	page 180	8.79	page 178	55.3%
Missouri Average	5.74	page 180	8.53	page 178	48.6%
West North Central Region	6.38		8.64	page 180	35.4%
National Average	8.89		10.53	page 195	18.4%
 <u>Residential Rates</u>					
KCPL	6.90	page 214	10.84	page 212	57.1%
Missouri Average	6.96	page 214	10.43	page 212	49.9%
West North Central Region	7.99		10.90	page 213	36.4%
National Average	10.62		12.56	page 228	18.3%
 <u>Commercial Rates</u>					
KCPL	5.49	page 247	8.41	page 244	53.2%
Missouri Average	5.56	page 247	8.16	page 244	46.8%
West North Central Region	6.38		8.70	page 245	36.4%
National Average	9.33		10.71	page 260	14.8%
 <u>Industrial Rates</u>					
KCPL	4.21	page 280	6.32	page 276	50.1%
Missouri Average	4.14	page 280	5.81	page 276	40.3%
West North Central Region	4.76		6.16	page 277	29.4%
National Average	6.00		7.10	page 292	18.3%

Comparative Construction Analysis									
Prepared by Keith Majors, Case No. EU-2014-0255									
Company	Construction Accounting Case No.	Construction Project	Total Company Share Constructed Plant in Service	Source	Missouri Jurisdictional Constructed Plant in Service	Source	Missouri Jurisdictional Net Rate Base Excluding Construction Project	Source	Construction Project % of Net Rate Base
Union Electric	EO-85-17 & ER-85-160	Callaway	2,978,248,000	Commission Reports, Volume 27, p.189	2,442,300,000	Commission Reports, Volume 27, p.189	4,055,088,934	Commission Reports, Volume 27, p. 270	60.23%
Ameren Missouri	ER-2010-0036	Sioux Environmental	574,098,132	Gary Weiss True-Up Direct, ER-2011-0028	574,098,132	Gary Weiss True-Up Direct, ER-2011-0028	6,135,560,194	Gary Weiss True-Up Direct, ER-2011-0028	9.36%
KCPL	EO-85-185 & ER-85-128	Wolf Creek	1,366,496,000	Commission Reports, Volume 28, p. 279	924,812,000	Commission Reports, Volume 28, p. 279	1,126,914,700	Commission Reports, Volume 28, p. 415	82.07%
KCPL	ER-2009-0089	Iatan 1 & Common Environmental	496,841,343	DR 193, Case No. ER-2012-0174	267,648,432	DR 193, Case No. ER-2012-0174	1,269,458,884	Staff Direct Accounting Schedules, ER-2009-0089	21.08%
KCPL GMO - L&P	ER-2009-0090	Iatan 1 & Common Environmental	94,684,505	DR 141, Case No. ER-2012-0175	94,684,505	DR 141, Case No. ER-2012-0175	190,475,404	Staff Direct Accounting Schedules, ER-2009-0090	49.71%
KCPL	EO-2005-0329	Iatan 2 & Common	982,476,091	DR 193, Case No. ER-2012-0174	525,673,764	DR 193, Case No. ER-2012-0174	1,524,610,061	Staff Revised True-Up Accounting Schedules, ER-2010-0355	34.48%
KCPL GMO - MPS	EU-2011-0034	Iatan 2 & Common	206,289,001	DR 141, Case No. ER-2012-0175	205,257,556	DR 141, Case No. ER-2012-0175	1,108,183,457	Staff Revised True-Up Accounting Schedules, ER-2010-0356	18.52%
KCPL GMO - L&P	EU-2011-0034	Iatan 2 & Common	109,333,171	DR 141, Case No. ER-2012-0175	109,333,171	DR 141, Case No. ER-2012-0175	300,554,763	Staff Revised True-Up Accounting Schedules, ER-2010-0356	36.38%
Empire	EO-2005-0263	Iatan 1 & Common Environmental	62,209,942	Mertens Direct, ER-2011-0004	51,835,750	Mertens Direct, ER-2011-0004	717,938,940	Staff Direct Accounting Schedules, ER-2010-0130	7.22%
Empire	EO-2005-0263	Iatan 2 & Common	269,059,140	Mertens Direct, ER-2011-0004	224,190,569	Mertens Direct, ER-2011-0004	641,697,501	Staff Direct Accounting Schedules, ER-2011-0004	34.94%
Empire	EO-2010-0262	Plum Point	105,097,322	Mertens Direct, ER-2011-0004	87,571,187	Mertens Direct, ER-2011-0004	641,697,501	Staff Direct Accounting Schedules, ER-2011-0004	13.65%

Case No. ER-2014-0255

Summary of Estimated Staff Deferral

Year	Period	Missouri Jurisdiction Depreciation Deferral	Missouri Jurisdiction Carrying Costs	Less: Impact of Deferral ADIT	Total Estimated Regulatory Asset
	2015 April	297,118	151,140	(210)	448,048
	2015 May	659,968	335,480	(675)	994,773
	2015 June	725,699	367,923	(1,186)	1,092,435
	2015 July	725,699	366,771	(1,697)	1,090,773
	2015 August	725,699	365,620	(2,208)	1,089,112
	2015 September	725,699	364,469	(2,717)	1,087,450
Total		3,859,882	1,951,403	(8,693)	5,802,592

**SCHEDULE KM-4,
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HAS BEEN DEEMED

HIGHLY CONFIDENTIAL

IN ITS ENTIRETY

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HAS BEEN DEEMED

HIGHLY CONFIDENTIAL

IN ITS ENTIRETY

AFUDC January 2014-June 2014									
Source: Report 73, DR 7, Case No. EU-2014-0255									
	KCPL UNADJUSTED					WITH STAFF ADJUSTMENTS			
			Annual	Monthly				Annual	Monthly
Month	Debt	Equity	AFUDC Rate	AFUDC Rate		Debt	Equity	AFUDC Rate	AFUDC Rate
Jan-14	2.72%	3.84%	6.56%	0.55%		2.00%	0.00%	2.00%	0.16667%
Feb-14	2.64%	3.86%	6.50%	0.54%		1.68%	0.16%	1.84%	0.15333%
Mar-14	2.61%	3.76%	6.37%	0.53%		1.56%	0.01%	1.57%	0.13083%
Apr-14	2.46%	3.52%	5.98%	0.50%		1.27%	0.00%	1.27%	0.10583%
May-14	2.34%	3.27%	5.61%	0.47%		1.13%	0.00%	1.13%	0.09417%
Jun-14	1.98%	2.51%	4.49%	0.37%		0.96%	0.00%	0.96%	0.08000%
				6 Month Average				1.46%	