MISSOURI PUBLIC SERVICE COMMISSION STAFF

MANAGEMENT AUDIT REPORT

KANSAS CITY POWER & LIGHT COMPANY

CASE NO. EO-2016-0124

EXECUTIVE SUMMARY

The Staff has completed its Management Audit of Kansas City Power & Light Company ("KCPL" or the "Company") that addressed two areas directed by the Missouri Public Service Commission ("Commission") in Case No. EO-2016-0124[1]. Specifically, the Staff reviewed the Company's administrative and general expenses ("A&G") as well as conducted an analysis of additional opportunities for synergy savings as a result of merging KCPL and KCP&L Greater Missouri Operations Company ("GMO"). The following are the findings and conclusions Staff derived upon the completion of its audit as well as the recommendations it makes to KCPL management:

MANAGEMENT AUDIT FINDINGS AND CONCLUSIONS:

1) Few if any synergies remain to be achieved from the 2008 acquisition of Aquila, Inc. ("Aquila') if GMO and KCPL were merged. Some negative consequences may arise from the merger of GMO and KCPL in the form of property tax restructuring.
2) KCPL A&G expenses are high in numerous comparisons, driven primarily by Pension Expense. The Company has taken actions to better control pension expense and while the benefit of those actions will not be realized in the near term, they are anticipated to eventually lower A~~-~~&~~-~~G costs.
3) No comprehensive internal audit has been performed of the Company's A&G expenses.

Comment [HR1]: See comment HR12 on p. 52.

[1] Case No. EO-2016-0124 – In the Matter of a Management Audit of Kansas City Power & Light Company.

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4) While the Company has taken positive action to address various expense account weak internal controls identified by Staff in past rate cases as well as has performed various focused Internal Audit examinations of aspects of its expense process, opportunities for improvement still exist. The Company's expense account definition for reimbursement for travel and entertainment is written overly broadly and the Company's internal control over its expense account process, while improved, has not been consistently effective, particularly in light of the Company's public and well documented concerns regarding its inability to earn its ROE.

5) There is no tracking mechanism in place to record the expense accounts that are moved from below-the-line to above-the-line by Company executives.

6) Significant Company alcohol expenditures are sometimes an above-the-line regulated account expenditure.

MANAGEMENT AUDIT RECOMMENDATIONS:

Staff recommends that KCPL management:

Track and Monitor the Cost-Savings Benefits of the Company's Changes to its Pension Benefits.

Analyze and Monitor A & G Expenses on a Continual Basis to Determine Opportunities to Reduce Such Expenses.

Direct the Performance of a Comprehensive Internal Audit of A & G Expenses Within the Next 12 months.

Revise the Current Expense Account Policy to Require that Entertainment Expenses Promote the Business Purposes of the Company when Regulated Accounts are Booked with Such Expenditures.

Develop a Tracking Mechanism to Monitor the Movement of Executive Expenses to "Above-the-Line" or Missouri Regulated Utility Accounts.

Develop and Adhere to a Policy that Defines and Prohibits Material Alcohol Expenses From Being Booked "Above-the-Line" to Missouri Regulated Utility Accounts.

INTRODUCTION AND HISTORY

On December 2, 2015, the Missouri Public Service Commission issued an order directing its Staff to conduct an audit of the administrative and general costs of Kansas City Power & Light to identify possible cost savings and efficiencies and report its audit findings and recommendations to the Commission. The impetus for the audit originated with the Report and Order issued September 2, 2015 by the Commission relating to the 2014 KCPL rate case identified as Case No. ER-2014-0370 ("2014 Rate Case"). The Midwest Energy Consumers' Group ("MECG"), an intervenor in the 2014 rate case, along with the Office of the Public Counsel ("Public Counsel" or "OPC"), sponsored a joint witness who submitted testimony regarding the level of operation and maintenance ("O&M") and A&G expenses incurred by KCPL. The witness noted that KCPL's A&G expense metrics consistently exceeded that of other utilities in the region. He recommended the Commission order a management audit to be conducted by an independent auditor for the "purpose of identifying cost savings and efficiencies" and to particularly focus on concerns related to KCPL's excessive A&G costs. [2]

In its December 2, 2015 Commission order, the Commission indicated that the evidence in the preceding rate case showed that KCPL's A&G's expenses were higher than other utilities in the region and directed Staff to conduct the audit and KCPL to cooperate. The Commission's order further directed Staff to examine if potential merger savings could be identified if KCPL and its affiliate entity, GMO, were merged. The possible cost savings and efficiencies from such a KCPL and GMO merger were to be reported in the findings and recommendations to the Commission. After the Missouri Commission approved its acquisition of Aquila on July 14, 2008 in Case No. EM-2007-0374, Great Plains Energy Inc. ("Great Plains" or "GPE") renamed Aquila as

[2] Direct Testimony of Lane Kollen who testified on behalf of the Midwest Energy Consumers' Group ("MECG") and the Missouri Office of the Public Counsel (OPC) in Kansas City Power & Light Company's 2014 rate case, Case No. ER-2014-0370.

GMO. Staff did not take a position in the 2014 Rate Case regarding the Public Counsel's and MECG's management audit recommendation.

The Commission's December 2, 2015 order also instructed Staff to file a pleading stating when it anticipated filing its final report in the matter. On December 16, 2015, Staff indicated in a filing to the Commission that its anticipated report would be filed by December 31, 2016 and that it would file its proposed audit scope no later than February 1, 2016. On March 9, 2016 the Commission approved Staff's proposed audit scope, attached as Schedule 1, which was filed on February 1, 2016. Staff's audit scope included specific activities it committed to perform in the context of the management audit relating specifically to the A & G expenses area and potential savings resulting from a merger of KCPL and GMO.

STAFF'S AUDIT ACTIVITIES

On December 18, 2015, Staff submitted three (3) data requests to KCPL to acquire initial information from the Company regarding its A & G costs and the Company's analysis and review of potential cost savings from a merger of KCPL and GMO. Since that time and at the time of this writing, the Staff has submitted a total of 54 data requests in the current case as well as analyzed the Federal Energy Regulatory Commission ("FERC") Form 1 expense information ("FERC Form 1") for KCPL, GMO and a variety of other Midwest utilities. Staff also considered various data request responses provided in KCPL's current rate case, Case No. ER-2016-0285 (KCPL's 2016 rate case) as well as selected responses to data requests in GMO's most recent rate case, Case No. ER-2016-0156 (GMO's 2016 rate case). Additionally, Staff conducted various interviews with KCPL personnel. A table below presents the dates of the in-person interviews, topics addressed, as well as personnel names and position titles of those interviewed. Interviews typically lasted no longer than two hours.

Staff's audit activities included a review of a number of Board of Director's Minutes from 2014 going forward as well as the review of external audit work papers of Deloitte Touche Tohmatsu LLP, the Company's external audit firm. Staff also reviewed specific internal audit reports conducted by Great Plains' Internal Audit personnel and the overall independence of the Company's Internal Audit Department including such things as reporting relationships (The Institute of Internal Audit recommends a direct reporting relationship to the Audit Committee of a Board of Directors, which direct reporting relationship is true for Great Plains Energy's Internal Audit department), the Great Plains Energy's Annual Report to Shareholders and GPE's and KCPL's Annual Form 10 K filings made with the U.S. Securities Exchange Commission ("SEC"), SEC proxy statements, rate case stipulations and agreements, Commission Reports and Orders and rate case testimony on pension issues. Staff examined various control processes the Company uses respecting its operational, non-fuel expenses and KCPL and GMO budgets.

Staff performed analysis to identify costs and conducted various comparisons of available information. Staff reviewed source material including documents respecting executive pensions, expense accounts, and salaries and benefits. Staff reviewed cost savings opportunities that may be present by combining KCPL with GMO including the Company's internal synergy analysis.

During the course of the review of KCPL's and GMO's operations, Staff conducted rate case audits of both GPE subsidiaries for KCPL's 2016 rate case and GMO's 2016 rate case. As such, information from these two rate cases was invaluable in understanding the overall operations of KCPL and GMO and their cost structure. Staff also had recently conducted a rate case audit for KCPL in 2014 in Case No. ER-2014-0370, which provided information for this management review.

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SCHEDULE OF IN PERSON INTERVIEWS CONDUCTED BY STAFF

Interview	Job Title	Topic	Date of Interview
Steven P. Busser Maria R. Jenks	Vice President – Risk Management and Controller Vice President – Supply Chain	Internal Control of Administrative and General Expense, Expense Account Process	September 29, 2016
Ellen E. Fairchild	Vice President, Chief Compliance Officer and Corporate Secretary	Internal Control of Administrative and General Expense	September 29, 2016
Darrin R. Ives Bryan Weiss	Vice President – Regulatory Affairs Manager of Corporate Accounting	Merger Synergies	September 29, 2016
Tony Jackson	Senior Director ~~Internal~~ Audit Services	Internal Control of Administrative and General Expense, Expense Account Process	October 12, 2016
Kelly Murphy Joyce Swope Mark Foltz	Senior Director Human Resources ~~Analyst~~Lead Analyst in Regulatory Accounting Senior Project Director	Pension Process	October 12, 2016
Terry Bassham	Chairman of the Board, President and Chief Executive Officer	Internal Control	October 12, 2016

ADDITIONAL POTENTIAL SYNERGY SAVINGS FROM MERGING KCPL AND GMO

As referenced in the December 2nd Order, the Commission ordered Staff to identify any potential cost savings related to a merger between KCPL and GMO. On April 4, 2007, Great Plains, KCPL and Aquila sought authority for a series of transactions whereby Aquila would become a direct, wholly-owned subsidiary of Great Plains. On July 1, 2008, in Case No. EM-2007-0374 ("Acquisition Case"), the Commission granted that authority. On July 14, 2008, Great Plains completed the acquisition and closed on Aquila.

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Combining Missouri electric operations of Aquila, Great Plains created a separate wholly-owned subsidiary called GMO. Great Plains operates GMO through an operating agreement with KCPL dated October 10, 2008. All employees, including the former Aquila employees, are presently part of the KCPL organization (GMO has no employees of its own) and KCPL provides all management and operational oversight of GMO.[3]

The 2008 Aquila acquisition created cost savings through the consolidation of work functions and processes such as those in the areas of accounting, treasury activities, corporate taxes, system engineering, construction and maintenance operations, and senior level corporate management oversight.

The Commission, in its Order issued in KCPL's 2015 rate case, specifically ordered the review of any further merger savings between KCPL and GMO resulting from the merger of these two entities in the current management audit docket.[4]

In an interview conducted with KCPL's Vice President of Regulatory Affairs, Mr. Darrin R. Ives, which occurred on September 29, 2016, Mr. Ives indicated all Aquila acquisition savings were achieved three to four years after the completion of the July 2008 acquisition. The Company's response to Staff Data Request No. 45 in the present management audit docket further indicates that:

> Virtually all of the synergy savings related to the Aquila acquisition were identified by the end of 2011. However, savings related to these identified synergies continue to accrue, even if they are not currently being tracked. For instance, reduced headcount, facilities savings and procurement savings continue to provide on-going benefits to the companies.[5]

[3] Joint Operating Agreement Between Kansas City Power & Light Company and Aquila, Inc. dba KCP&L Greater Missouri Operations Company, Case No. EM-2007-0374 on October 10, 2008.
[4] Case No. EO-2016-0124, Commission Order Requiring a Management Audit of Kansas City Power & Light Company, December 2, 2015.
[5] Response to Staff Data Request No. 45 in Case No. EO-2016-0124 is attached as Schedule 2 to this Report..

KCPL does not believe there are any material additional merger savings to be achieved from the Aquila consolidation[6] since most of the savings of the Aquila acquisition resulted in combining the work force of the former Aquila entity into the KCPL organization, which occurred on "day one", of the July 2008 acquisition.[7] There are no longer any Aquila (GMO) employees and all employees who have GMO responsibilities are employed by KCPL. The two utility companies (KCPL and GMO), share one organizational structure including one set of executive management that is responsible for both companies' generation operations, financial management, corporate services, human resources and legal counsel, corporate secretary and compliance, marketing and public affairs, and regulatory affairs activities.

At this time the acquisition of Aquila occurred over eight years ago and the process of combining organizational functions to extract the most significant savings has been completed. The Company indicates that some small savings could be achieved if the two companies, KCPL and GMO, were combined regarding "administrative efficiencies including internal reporting, journal entries, compliance reporting and other administrative process improvement initiatives that could be realized and be a benefit with the combination into one entity."[8] Such savings of a combined KCPL and GMO may encompass the reduction of separate legal filings both companies make on the federal level, such as filings with ~~the SEC,~~ the FERC, the Internal Revenue Service ("IRS"), etc., and regulatory filings, made at the state level, for matters such as rate cases.

Comment [HR2]: GMO does not make SEC fiings.

The Company's response to Staff Data Request No. 45 also points to concerns with operating KCPL on an "integrated basis in two state jurisdictions," such as property tax issues including the "potential significant reallocation of property taxes between counties and between

[6] Darrin Ives Interview September 29, 2016.
[7] Darrin Ives Interview September 29, 2016.
[8] Response to Staff Data Request No. 45 in Case No. EO-2016-0124.

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rate jurisdiction territories included in KCP&L and GMO's territories." The Company also raised the matter of joint ownership of generating plants in light of the recently proposed acquisition of Westar[9] as an additional concern arising from a merger of KCPL and GMO. While this combination has not received the necessary regulatory approvals and is still pending, consolidation of these two entities will likely result in changes to the corporate structure, which could affect KCPL and GMO operations and the cost allocation process.

Based upon the Company's response to Staff inquiries and Staff's analysis, Staff concludes that the likelihood of any further opportunities for meaningful dollar savings to be realized and passed on to Missouri ratepayers, were KCPL and GMO to merge, are significantly limited and perhaps may be outweighed by potential detriments associated with such a merger.

SYNERGY SAVINGS TRACKING AND TRANSITION COSTS RELATED TO THE AQUILA, INC. ACQUISITION

In the Commission's Report and Order in Case No. EM-2007-0374, at page 282 of the Slip Opinion, in ordered paragraph 6(c), the Commission included the following condition:

> 6c. Great Plains Energy, Incorporated, Kansas City Power & Light Company and Aquila, Inc., shall, upon closure of the authorized transactions, implement a synergy savings tracking mechanism as described by the Applicants, and in the body of this order, utilizing a base year of 2006;

Re Great Plains Energy Inc., et al., Case No. EM-2007-0374, Report and Order, 17 Mo.P.S.C.3d 338, 581 (2008).

The Commission found potential for significant savings from the acquisition, and supported Great Plains, KCPL and Aquila recovering the costs incurred in combining the operations of KCPL and Aquila. These costs are referred to as "transition costs" and include non-executive severance costs for employees terminated, facilities' integration costs, and incremental third-party

[9] *Ibid*.

and other non-labor expenses incurred as a result of the acquisition. The Commission also addressed transaction costs, such as investment banking fees and legal costs for preparing documents to complete the acquisition. In the Case No. EM-2007-0374 Report and Order where it presented its "Final Conclusions Regarding Transaction and Transition Cost Recovery," on page 241 of the Slip Opinion, the Commission stated:

> Substantial and competent evidence in the record as a whole supports the conclusions that: (1) the Applicants' calculation of transaction and transition costs are accurate and reasonable; (2) in this instance, establishing a mechanism to allow recovery of the transaction costs of the merger would have the same effect of artificially inflating rate base in the same way as allowing recovery of an acquisition premium; and (3) the uncontested recovery of transition costs is appropriate and justified. The Commission further concludes that it is not a detriment to the public interest to deny recovery of the transaction costs associated with the merger and not a detriment to the public interest to allow recovery of transition costs of the merger.
>
> If the Commission determines that it will approve the merger when it performs its balancing test…, the Commission will authorize KCPL and Aquila to defer transition costs to be amortized over five years.[930]
>
> --------------------
>
> [930] The Commission will give consideration to their [transition costs] recovery in future rate cases making an evaluation as to their reasonableness and prudence. At that time, the Commission will expect that KCPL and Aquila demonstrate that the synergy savings exceed the level of the amortized transition costs included in the test year cost of service expenses in future rate cases.
>
> 17 Mo.P.S.C.3d at 548.

In KCPL's 2010 Rate Case (Re Kansas City Power & Light Co., File No. ER-2010-355, Report and Order (2010), the Commission determined the appropriate amount of acquisition transition costs to include in KCPL's rates. The Commission ordered recovery of the transition costs over five years beginning with the effective date of rates in the 2010 Rate Case. KCPL and GMO have not deferred any additional transition costs after December 31, 2010. Below are the total transition costs for all jurisdictions:

Total EM-2007-0374 Acquisition Transition Costs[10]	
KCPL – Missouri	$19,344,018
GMO – Missouri Public Service	$17,727,367
GMO – St. Joseph Light & Power	$4,452,471
GMO – St. Joseph Light & Power Steam	$244,067
KCPL – Kansas	$15,633,625
Total Transition Costs	$58,111,084

To demonstrate to the Commission the merits of the recovery of transition costs, the Company's synergy savings tracking model, as ordered by the Commission in Case No. EM-2007-0374,[11] compared the adjusted base year of non-fuel operations and maintenance (non-fuel O&M) of standalone KCPL and Aquila operations in 2006 to the combined KCPL and GMO operations of 2009[12] and to other 12 month periods in future test years.

To understand KCPL's true savings from the acquisition, one must examine the synergies from the Company's perspective. In addition to creating and maintaining a tracking model to compare the adjusted 2006 base year to 2009 as ordered by the Commission, KCPL prepared and maintained a specific "synergy charter tracking data base" to track synergy savings, including those in and beyond the savings identified in the tracking model. KCPL has a cumulative database of these synergy charters by the quarter in which they occurred, total by year, and by individual charter. A synergy "charter" is a document that specifically identifies and tracks a

[10] Response to Staff Data Request No. 146, Case No. ER-2010-0355.
[11] Commission Report and Order, Case No. EM-2007-0374, page. 282, ordered paragraph 6.c.
[12] Case No. ER-2010-0355.

category of savings that can be directly attributed to the acquisition. The table below summarizes the cumulative synergy savings as they appear in the charter database.

Cumulative Synergy Savings from Synergy Charter Tracking Database[13]		
Period	Regulated Savings	Corporate Savings
2008 (3rd and 4th Quarters)	$20,614,613	$48,950,489
2009	$64,561,991	$78,001,774
2010	$83,023,990	$81,679,059
2011	$83,073,379	$80,087,134
2012	$75,532,276	$70,165,888
2013 (1st and 2nd Quarters)	$40,703,068	$34,272,223
Total Cumulative Synergies	$367,509,317	$393,156,567

"Regulated Savings" identified in the above table represent those acquisition savings that occurred from the consolidation of operations of Aquila into KCPL. As the two organizations were "combined" within one KCPL entity (all employees operate as part of KCPL), operations and processes were consolidated resulting in cost savings. Examples of cost savings were the consolidation of work force for the accounting and treasury functions, information technology systems, purchasing and procurement activities, and maintenance crews for power plant, transmission and distribution operations. The Board of Directors and senior management functions were combined causing operational savings.

The column labeled "Corporate Savings" are corporate retained synergies that KCPL has identified that are not included in the synergy savings tracking model the Commission ordered,

[13] Response to Staff Data Request No. 230 – Case No. ER-2014-0370.

and have not been and will not be flowed to ratepayers. These savings include reduced interest expense from the upgrade of Aquila's debt post-acquisition, line of credit fees, and corporate redundant expenditures, and are referred to as "non-regulated" savings.

There are synergy savings that took place after the acquisition was announced but before GPE acquired Aquila. In its response to Staff Data Request No. 460 in Case No. ER-2010-0355, KCPL stated, "[We] have not tracked or evaluated synergy savings for any period prior to the completion of the acquisition on July 14, 2008." If there were any synergy savings before GPE acquired Aquila, the companies would have retained the additional synergies in 2008, before flowing them through rates. It is typical for companies to lose employees (and not fill vacated positions), resulting in a reduction of payroll costs, during the course of a merger or acquisition. Many employees, fearing loss of jobs, will leave the merging companies to seek employment elsewhere before the merger is fully authorized or closed.

IDENTIFICATION OF SYNERGY SAVINGS FROM THE ACQUISITION OF AQUILA

The following synergies have been achieved resulting from the acquisition of Aquila and are quantified in the table on the previous page:

- 20 West 9th Headquarters – capital costs of former Aquila Headquarters that was subsequently sold
- Nebraska Facilities – capital costs of Nebraska property that was subsequently sold
- ~~Blue Springs Service Center – capital costs of Blue Springs Service Center that was subsequently sold~~
- Liberty Service Center – capital costs of Liberty Service Center that was consolidated with the Northland Service Center that was subsequently sold
- Platte City Property – capital costs of Platte City Property that was subsequently sold
    - Elimination of Aquila board of director fees and associated non-employee director stock plans
    - Elimination of travel and meals expense of Aquila Extended Leadership Team
    - Headcount Reduction of former Aquila employees
    - Redundant Spending in the following categories:
        a. Human Resources and Temporary Labor
        b. Central Services (collections, customer identification, credit reporting)
        c. Contracted Engineering Services

Comment [HR3]: Blue Springs Service Center was not sold.

Comment [HR4]: Bullets and indentation from here on imply that all of these items are sub-parts (i.e., related to the Platte City Property) when that is not the case; suggest using the larger bullet indicator for each of these items.

d. Contracted Environmental Services
e. Contracted Security Services
f. Finance and Banking Services
g. Contracted Finance and Accounting Services
h. Insurance
i. General Management Expenses (customer research, load forecasting, tax research)
j. Office Supplies (Printing, copier leases)
k. Safety Expenses
l. Legal and Litigation Services
m. Miscellaneous Non-recurring expenses

- Elimination of Six Sigma Program Office
- Employee meals and travel related to headcount reductions
- Employer portion of payroll taxes related to reduced headcount
- Elimination of Letter of Credit Fees
- Reduction of Interest Savings
- Truck Fleet Reductions
- Combined Street Light Maintenance Contract
- Transmission and Substations Contract Labor Resources
- Reduced Transmission Expense resulting from Aquila joining the Southwest Power Pool
- Transfer of write-offs (Bad Debts) to second agency
- Savings from repairing, reclaiming, and recycling select transmission and distribution assets
- Savings from combined capacitor purchase contract
- Savings from repair, fabrication, and maintenance performed in-house that would otherwise have been contracted
- Savings from centralized negotiation management of temporary labor contracts
- Savings from consolidation of corporate purchasing cards
- Employee benefits savings from headcount reductions
- Various Synergies related to information technology consolidation projects
- Savings from consolidation of contracted transmission and distribution construction
- Savings from consolidation of contracted line locates
- Savings from consolidation of materials and supplies vendors
- Savings from consolidation of OATI WebTrader Software
- Savings from elimination of duplicative software subscriptions
- Savings from consolidation of relay department
- Savings from consolidation of contracted vegetation management
- Savings from consolidation of wood pole contracts
- Savings from consolidation of energy optimizer program contracted services
- Savings from consolidation of transmission and distribution contracted freight
- Savings from consolidation of transmission and distribution maintenance and elimination of contracted maintenance
- Savings from eliminating Residential Customer Purchase Plan
- Savings from reduction of contracted Sarbanes-Oxley services

Savings from transfer of some maintenance projects previously charged to expense to capital projects

- Savings from increase in demand side energy efficiency programs
- Savings from replacement of inaccurate meters

ADMINISTRATIVE AND GENERAL EXPENSES

The FERC has specific accounting and reporting requirements for public utilities and licensees operating under its jurisdiction that includes the uniform system of accounts (“USOA”). The USOA specifies how utility operational expenditures, property, income and other activities are to be accounted. The 920 to 935 series of FERC accounts includes utility A&G expenses which are specific costs not directly associated with generating, transmitting or delivering power to customers. Specific USOA account numbers and a brief description of the expense to be recorded in each account are below.

ADMINISTRATIVE AND GENERAL EXPENSE
FERC ACCOUNTS 920 THROUGH 935

ACCOUNT NUMBER	ACCOUNT DESCRIPTION
920	Administrative and General Salaries
921	Office Supplies and Expenses
922	Administrative Expenses Transferred – Credit
923	Outside Services Employed
924	Property Insurance
925	Injuries and Damages
926	Employee Pensions and Benefits
927	Franchise Requirements
928	Regulatory Commission Expenses
929	Duplicate Charges – Credit
930.1	General Advertising Expenses
930.2	Miscellaneous ~~and~~ General Expenses
931	Rents

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933 Transportation Expenses (Nonmajor Only)

935 Maintenance of General Plant

It is, in part, KCPL's and GMO's historically high A&G expense compared to other regulated Missouri utilities and Westar Energy Company, which prompted the request by MECG and Public Counsel witness, Mr. Lane Kollen, to recommend the Commission approve a management audit of the A & G expenses of KCPL. Mr. Kollen's initial request, which was made in his Direct Testimony in KCPL's 2014 rate case, included the recommendation for an audit of all of KCPL's operation and maintenance activities as well, not only A&G costs. The Commission's December 2, 2015 order directing the management audit focused on the Company's A&G expenses instead of Mr. Kollen's original broader recommendation. The Direct Testimony of Staff witness, Keith Majors, in the Company's 2014 rate case, also provided significant analysis and discussion of KCPL's high A&G expense relative to its electric utility peers.

KCPL's A&G expense was analyzed and compared in a variety of manners during the 2014 rate case by both Staff and the OPC and MECG witnesses. Specifically, these expenses were compared in the following manner: 1) A&G expense per customer, 2) A&G expense per megawatt hour sold and 3) A&G expense per electric operating revenue for the calendar year 2014 and in a five-year historical comparison or from 2009 to 2014 for the following companies: The Empire District Electric Company, Union Electric Company d/b/a Ameren Missouri, Westar Energy Company, KCPL- Greater Missouri Operations Company and Kansas City Power & Light Company. Staff witness Keith Majors' Direct Testimony, page 237 of the Staff COS Report[14] in Case No. ER-2014-0370 provided a succinct summary of Staff's analysis for the comparisons:

[14] Staff Cost of Service Report – Direct filing made April 2015; EFIS #361, Exhibit 200 in Case No. ER-2014-0370

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> In comparison to The Empire District Electric Company ("Empire"), Union Electric Company d/b/a Ameren Missouri ("Ameren Missouri"), and Westar , KCPL and GMO combined have the highest A&G cost per customer, the third highest A&G cost per megawatt hour sold (GMO has the highest), and the highest A&G cost per dollar of electric revenue.

The Company took exception to the use of the FERC Form 1 data that served as the basis for Staff and OPC and MECG's witnesses' analyses and argued that the recording of A&G expenses by utilities is "very subjective" and open to interpretation under the FERC Uniform System of Accounts.[15] Specifically, the Company argued that not every cost is recorded to the same FERC account for every utility and further that the FERC Form 1 comparison does not recognize that utilities engage in different activities that may require additional administrative support, which could be reflected in higher A&G expense. The Company gave the specific example of KCPL's energy efficiency programs that require administrative support to manage the programs; another example provided was the Company's provision of solar rebates, which requires additional administrative effort to support.

The Company indicated that Westar Energy and The Empire District Electric Company would record little or no costs in the A&G expense area. Further example was provided by the Company with costs to comply with the Nuclear Regulatory Commission ("NRC") regulations in that utilities with no ownership of nuclear generation will not require any cost support. In further disagreement with the Staff and OPC and MECG witnesses' utilization of FERC Form 1 information to compare A&G costs among various utilities, the Company indicated that the FERC USOA provides an "outline of accounts to be used for expenses" and it is not possible for FERC to have a policy for every situation as to where to record expenses to allow for a good comparison between utilities.

[15] Case No. ER-2014-0370, Rebuttal Testimony of Ryan A. Bresette, page 3 line 11 through page 4 line 13.

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While Staff does not discount the factors identified by the Company addressed above concerning some of the limitations of FERC Form 1 information, it is Staff's opinion that the FERC Form 1 data is valuable when used as an "initial barometer" by which to gauge the costs of one utility as compared to that of another. The usefulness of the FERC Form 1 data for such comparisons increases when costs, such as A & G, are analyzed in variety of manners such as by 1) costs per customer, 2) costs per megawatt hour sold, 3) costs per operating revenue, and 4) costs per total company costs.

Regardless of the underlying impetus for the management audit (high A&G costs), Staff's audit scope indicated it would specifically review and determine the company's internal control processes it uses to manage it's A&G expenses. A system of effective internal control is critical in the management of any process or practice and controlling expenses requires effective management decision-making and effective controls regardless of how the company's costs may compare to other companies.

The Company's A&G costs 1) per customer, 2) per megawatt hour sold, 3) per electric operating revenue and 4) compared to overall O&M costs compared to other Missouri utilities and Westar Energy is presented below using the FERC Form 1 information:

Administrative and General Expense Per Customer

	2009	2010	2011	2012	2013	2014	2015
Empire	$170.09	$194.16	$222.05	$251.10	$265.94	$270.78	$272.87
Ameren Missouri	$211.03	$201.85	$231.17	$198.47	$210.39	$232.25	$219.87
Westar	$ 257.00	$281.25	$290.14	$305.20	$292.30	$298.72	$317.04
GMO	$214.65	$198.10	$225.46	$240.43	$236.67	$235.68	$250.44
KCPL	**$278.43**	**$298.54**	**$339.18**	**$298.63**	**$302.53**	**$311.95**	**$306.30**
Combined KCPL & GMO	$254.23	$260.45	$296.07	$276.55	$277.54	$283.05	$285.22

Administrative and General Expense Per Megawatt Hour Sold

	2009	2010	2011	2012	2013	2014	2015
Empire	$5.28	$5.46	$6.35	$7.47	$7.95	$8.89	$9.35
Ameren Missouri	$5.11	$4.98	$5.72	$5.38	$5.84	$6.45	$6.12
Westar	$6.27	$6.59	$6.85~~0~~	$7.42	$7.03	$6.94	$7.74
GMO	$8.26	$7.02	$8.27	$8.99	$8.86	$8.77	$9.50
KCPL	**$7.08**	**$7.10**	**$8.53**	**$6.97**	**$7.18**	**$7.20**	**$7.73**
Combined KCPL and GMO	$7.42	$7.07	$8.45	$7.53	$7.65	$7.63	$8.24

Administrative and General Cost Per Dollar of Revenue

	2009	2010	2011	2012	2013	2014	2015
Empire	$0.0660	$0.0678	$0.0706	$0.0825	$0.0837	$0.0773	$0.0836
Ameren Missouri	$0.0926	$0.0793	$0.0853	$0.0757	$0.0743	$0.0821	$0.0762
Westar	$0.0931	$0.0925	$0.0904	$0.0919	$0.0841	$0.0792	$0.0896
GMO	$0.1035	$0.0838	$0.0928	$0.0992	$0.0931	$0.0878	$0.1010
KCPL	**$0.1079**	**$0.1007**	**$0.1115**	**$0.0969**	**$0.0932**	**$0.0935**	**$0.0938**
Combined KCPL and GMO	$0.1064	$0.0952	$0.1054	$0.0977	$0.0932	$0.0916	$0.0961

A&G Expenses Compared to Total Operations & Maintenance Expense

	2009	2010	2011	2012	2013	2014	2015
Empire	10.31%	10.66%	11.54%	13.82%	14.40%	12.56%	14.32%
Ameren MO	15.65%	14.17%	14.66%	14.93%	13.56%	14.99%	13.58%

Attachment A

Westar	14.52%	14.79%	14.37%	15.13%	13.83%	13.09%	15.62%
GMO	14.84%	13.14%	14.50%	17.13%	16.42%	14.34%	16.92%
KCPL	**19.41%**	**19.08%**	**19.42%**	**17.17%**	**16.39%**	**16.17%**	**17.07%**
Combined KCPL & GMO	17.67%	16.88%	17.69%	17.16%	16.40%	15.54%	17.02%

Staff performed the same analysis above, comparing KCPL to a broader group of utilities, including: Alliant Energy Corporation, Avista Corporation, Black Hills Corporation, Cleco Corporation, IdaCorp, Inc., OGE Energy Corporation, Pinnacle West Capital Corporation, PNM Resources, Inc., Portland General Electric Company, TECO Energy Inc., UNS Energy Corporation, Westar Energy, Inc and Wisconsin Energy Corporation. These peer utilities were identified in the GPE 2014 Annual Report Proxy statement for purposes of determining executive compensation. The peer utilities were selected by Mercer, GPE's compensation consultant, for their size and business mix similar to GPE's using three criteria: annual revenues, market value and percentage of total revenues from regulated electric operations. Compared to each of these companies KCPL had the second to highest A & G costs per customer for 2015 (second only to Westar Energy). In other words, from highest cost utility to lowest cost utility, with 18 representing the highest cost utility, KCPL ranked 17th out of 18.

KCPL also ranked 10 out of 18 for A & G costs per megawatt sold in this group of companies (KCPL total O & M expense ranking as compared to the group was 2) and ranked 14 out of 18 for A & G costs per electric operating revenue, again with the ranking of 18 as the highest cost. The Company ranked 16 out of 18 for its A & G expense compared to total O & M costs. Its A & G is ranked 1 (lowest cost) compared to operating revenue in the grouping. Schedule 3 demonstrates these rankings for each of the utilities in this comparison grouping and their costs.

On page 2 of Staff's Proposed Audit Scope, Staff identified that KCPL and GMO's A~~-~~&~~-~~G costs would be analyzed using 2007 as a base period. This period was selected because it was the last year KCPL and GMO (at that time Aquila, Inc.) operated as separated entities. Staff also included 2005 and 2006 FERC Form 1 information and the results of Staff's analysis are below:

Calendar Year 2005	**Empire**	**Ameren Missouri**	**Westar**	**GMO**	**KCPL**	**Combined KCPL and GMO**
A&G Cost per Customer	$172.98	$206.19	$208.42	$173.52	$245.03	$218.25
Ranking (1, is lowest)	1	3	4	2	6	5
A&G Cost per Megawatt Hour Sold	$5.27	$4.58	$4.86	$5.90	$6.25	$6.14
Ranking (1, is lowest)	3	1	2	4	6	5
A&G Cost Per Electric Revenue Dollar	$0.08	$0.09	$0.09	$0.10	$0.11	$0.10
Ranking (1, is lowest)	1	3	2	4	6	5
A&G as a % of Total O&M	12%	15%	13%	13%	19%	17%
Ranking (1, is lowest)	1	4	3	2	6	5

Calendar Year 2006	**Empire**	**Ameren Missouri**	**Westar**	**GMO**	**KCPL**	**Combined KCPL and GMO**
A&G Cost per Customer	$163.61	$209.51	$212.62	$222.58	$257.52	$244.36
Ranking (1, is lowest)	1	2	3	4	6	5
A&G Cost per Megawatt Hour Sold	$5.02	$4.84	$5.12	$6.90	$6.57	$6.68
Ranking (1, is lowest)	2	1	3	6	4	5
A&G Cost Per Electric Revenue Dollar	$0.07	$0.09	$0.09	$0.11	$0.11	$0.11
Ranking (1, is lowest)	1	3	2	4	6	5
A&G as a % of Total O&M	11%	16%	13%	14%	21%	18%
Ranking (1, is lowest)	1	4	2	3	6	5

Calendar Year 2007	**Empire**	**Ameren Missouri**	**Westar**	**GMO**	**KCPL**	**Combined KCPL and GMO**

Attachment A

A&G Cost per Customer	$180.44	$224.63	$231.79	$207.41	$277.80	$251.17
Ranking (1, is lowest)	1	3	4	2	6	5
A&G Cost per Megawatt Hour Sold	$5.39	$5.25	$5.05	$6.82	$6.63	$6.69
Ranking (1, is lowest)	3	2	1	6	4	5
A&G Cost Per Electric Revenue Dollar	$0.07	$0.09	$0.09	$0.09	$0.11	$0.10
Ranking (1, is lowest)	1	4	2	3	6	5
A&G as a % of Total O&M	11%	16%	13%	13%	20%	17%
Ranking (1, is lowest)	1	4	3	2	6	5

As can be seen from the above metrics and rankings, KCPL, GMO, and Combined KCPL and GMO had comparatively high A&G costs prior to the acquisition of Aquila, Inc., and they continue to have comparatively high A&G costs subsequent to the acquisition.

EMPLOYEE PENSIONS AND BENEFITS – ACCOUNT 926

A number of acronyms are used in this section and a brief index may be helpful to the reader:

OPEB: Other Post Employment Benefits
SERP: Supplemental Executive Retirement Plan
DB: Defined Benefit Plan~~ension~~
PBO: Projected Benefit Obligation
DC: Defined Contribution Plan
ERISA: ~~Federal~~ Employee Retirement Income Security Act
PPA: Pension Protection Act

Staff's Audit Scope document listed pension expense as a part of Item 1 on page 3. By far the most significant portion of A&G expense is Account 926 – Employee Pensions and Benefits. Staff reviewed pension expense in the context of A~~-~~&~~-~~G expenses for Missouri utilities and the peer group utilities used for Staff's A&G analysis.

The Staff also reviewed other pertinent documents such as GPE and the peer group utilities' annual shareholder reports, FERC Form 1 information related to pension expense, SEC

Form 10-K's, SEC proxy statements, rate case stipulations and agreements, and rate case testimony on pension issues. Staff reviewed the annual actuary reports created by KCPL's and GMO's compensation experts and consultants. Finally, Staff reviewed the Board of Directors' Compensation Subcommittee which specifically has responsibility to oversee KCPL's and GMO's compensation and benefits.

In addition to obtaining company-specific information, the Staff researched current issues concerning pension plans in the utility industry and non-utility industry. The Staff obtained a copy of Deloitte LLP's ("Deloitte") 2015 Study of Economic Assumptions and 2016 Study of Economic Assumptions. In these studies, Deloitte compiled information disclosed by many of the Fortune 500 companies in their most recent annual reports. Deloitte focused on 267 companies that sponsor pension or other postretirement benefits and that have calendar fiscal years. Deloitte noted on page 3 of its 2016 Study that, although the selection of pension plan assumptions should be specific to the individual plan, plan sponsors, as well as regulators, often compare their discount rate and other assumptions to those of other plan sponsors.

In addition to the Deloitte Study, Staff also obtained and reviewed a copy of the PricewaterhouseCoopers ("PwC") Pension/OPEB 2015 Assumption and Disclosure Survey and Pension/OPEB 2016 Assumption and Disclosure Survey. The PwC Survey presents an analysis of 100 companies comprising the Fortune 100 and other large and established companies with a December 31 measurement date. PwC reviewed the public annual reports for the companies selected for financial information regarding pension and other postemployment benefit ("OPEB") plans.

PwC provided the survey so that companies can benchmark the assumptions used in its pension and OPEB plans against the survey results. In its review, Staff used the results of the

Deloitte Study and the PwC Survey to benchmark Missouri utilities'~~y's~~ 2014 and 2015 pension plan assumptions for reasonableness and as a possible indication of the focus of utility management on controlling pension expense. The economic assumptions referenced in the Deloitte and PwC surveys are the discount rate, expected rate of return, and salary increase assumptions. Also reported in the surveys is the funded status of the surveyed pension plans.

Pension costs are impacted by actual employee demographics (including age, life expectancies, compensation levels and employment periods), earnings on plan assets, the level of employer contributions made to the plan, and plan amendments. Pension costs are also affected by changes in key actuarial assumptions, including anticipated rates of return on plan assets, salary increase projections and the discount rates used in determining the projected benefit obligation and pension costs. The assumptions used in the calculation of pension costs are subjective in that they are nothing more than estimates of the impact of future events.

All of the larger Missouri electric, gas and water utilities operate under "pension tracker" mechanisms. Pension trackers work through a continuous comparison of the amount of pension costs funded by a utility to the amount of pension costs collected in customer rates. Any under- or over-recovery of pension costs in rates compared to the amount of cash placed in the utility's external fund(s) is allowed to be recovered (if the costs are prudently incurred) in the utility's next rate case, with the over-collection or under-collection of pension costs amortized over a five-year period. A review of the Stipulations and Agreements establishing the pension trackers reveals that the trackers are designed in theory to ensure that the utility or its customers are made whole for every dollar of expense related to pensions (and pension settlements) in addition to receiving a financial return (at its overall cost of capital) by inclusion of pension regulatory assets/liabilities in rate base. The use of pension trackers in Missouri has eliminated the effect of regulatory lag from this major utility compensation expense.

In a traditional DB plan, an employee receives a set monthly amount at retirement. The amount the retiree receives is based upon the employee's salary and length of service with the company. In contrast to traditional DB plans where the amount of the benefit is defined in advance, many employees today participate in defined contribution plans like 401(k) plans. DC plans get their name because they are the amount of the contribution that is defined instead of the benefit. Employees contribute a portion of their salary into a retirement account where it can be invested in stocks, bonds, mutual funds, etc. Some companies, like KCPL, make a matching contribution to the employees' accounts up to a certain percentage. The account grows through contributions and investment earnings until retirement. Separate and distinct from, and in addition to, their DB pension plans, some Missouri utilities provide additional pension benefits. Costs of 401(k) plans, although significant, and a direct cost of providing retirement benefits, have not been considered and included in pension costs subject to pension trackers in Missouri. KCPL's DC is offered to all employees as a tax-qualified retirement savings plan.

In addition to Defined Benefit and Defined Contribution plans, all Missouri utilities offer upper-level executive employees additional pension benefits in their Supplemental Executive Retirement Plans ("SERP"). These are generally unfunded plans, that is, contributions are not paid to a trust but are instead made on a "pay as you go" basis.

Staff calculated an average of each of the pension assumptions for Missouri and Westar electric utilities included in this review and compared this result to the assumptions selected by KCPL and GMO. Any significant discrepancies between the assumptions used by the utilities and those used by their Missouri and Westar peer group are noted. Staff calculated an average of the pension assumptions for the peer utility group identified in the A&G cost comparison. Staff's analysis in presented in later in the report.

In this management audit report, Staff is also presenting data concerning the funded status of each plan in calendar years 2014 and 2015. The funded status of each plan was calculated as a comparison of the value of the plan assets as of December 31 of each year to the PBO of each plan at the same point in time. The PBO is the cash flow discounted amount of pension benefits owed by each plan at a point in time based upon current and future salary levels of covered employees. A funded status of 100% signifies that the utility's pension fund has sufficient current assets to pay all current and future owed pension benefits to its employees. The funded status in this calculation is according to Generally Accepted Accounting Principles ("GAAP"). Pension and OPEB plans are governed in part by the ~~Federal~~ ERISA and the ~~Federal~~ PPA. ERISA and PPA have calculations and valuation standards that differ from GAAP and consequently the funded status as calculated by ERISA and PPA differs from GAAP and can be higher or lower than the funded status as reported in the tables below. It should be noted that the financial crisis that struck the U.S. economy starting in 2008 had a significant negative impact on pension fund earnings for both regulated and non-regulated businesses, and that having a funded percentage of less than 100% in the current environment is not unusual.

KCPL manages two DB pension plans, the ~~Management~~Non-Union Pension Plan and the Joint Trusteed ~~Pension~~Retirement Plan, and participates in the Wolf Creek Nuclear Operating Corporation ("Wolf Creek" or "WCNOC") Retirement Plan. KCPL also manages two DB OPEB plans, the ~~Management OPEB~~Non-Union Health & Welfare ~~p~~Plan and the Joint Trusteed ~~OPEB~~Health & Welfare Plan, and participates in the WCNOC OPEB Plan.

KCPL has pension trackers that have been developed in each of its four rate cases since the Stipulation and Agreement approved by the Commission in its Report and Order in Case No. EO-2005-0329 (Case Nos. ER-2006-0314, ER-2007-0291, ER-2009-0089, and ER-2010-0355) and the two most recently completed rate cases in 2013 (Case No. ER-2012-0174) and 2014 (Case No. ER-2014-0370). Pension issues in these rate cases have been settled through stipulation and agreements.

KCPL made some changes to its pension plan for employees hired after September 1, 2007, and made these pension plan changes available to employees hired before that date. This change was referred to by KCPL as "GPE Retirement Choice" and is described by KCPL as follows:

> In 2007, non-union employees of Great Plains Energy and KCP&L, including the NEO's [Named Executive Officers] were given a one-time election to remain in their existing Pension Plan and 401(k) Plan (''Old Retirement Plan''), or choose a new retirement program that includes a slightly reduced benefit accrual formula under the Pension Plan paired with an enhanced benefit under the 401(k) Plan (''Current Retirement Plan'')[16].

In addition, for union employees hired after October 1, 2013, the DB pension benefits are derived from a cash balance account formula. Effective January 1, 2014, the "Current Retirement Plan" management Defined Benefit plan was closed to all future employees including all future executive officers and senior management.

REASONABLENESS OF PENSION ASSUMPTIONS

Staff calculated an average of each of the pension assumptions for Missouri utilities (and Westar), and for the peer utility group included in this review, and compared this result to KCPL's assumptions. In addition to comparing the pension assumptions used by KCPL to other large Missouri utilities, the Staff also compared KCPL assumptions to industry-average pension

[16] 2015 GPE Annual Report Proxy Statement, page 42.

assumptions as found by pension consulting companies Deloitte and PWC. The individual pension assumptions are identified and discussed below. In summary, KCPL's pension assumptions appear to be reasonable compared to the Deloitte, PwC, and peer utility metrics.

DISCOUNT RATE

The discount rate is used for valuation of the PBO and for the periodic benefit cost calculation. The computation of these items use separate discount rates in most cases. For this review, Staff used the discount rate for computation of periodic cost as that amount would affect pension expense as opposed to the PBO, a balance sheet item. The discount rate computes the value of future cash flows for pension payments to account for the time value of money. Discount rates are usually based on high quality corporate bond yields and are developed by management and reviewed by KCPL's external auditors. Discount rates have an inverse relationship with determination of the PBO and consequently overall funded status. As discount rates increase, the PBO decreases as the present value of future pension benefits decrease. For net periodic costs, higher discount rates result in higher periodic costs as the discount rate is used to calculate interest expense on the PBO. Staff's discount rate comparison is in the table below:

Discount Rate - For Net Costs	Missouri & Westar Averages	Peer Utility Averages	PWC Survey Averages	Deloitte Survey Averages	KCPL & GMO
Pension 2014	4.96%	4.85%	3.96%	3.97%	5.03%
Pension 2015	4.11%	4.19%	4.30%	4.35%	4.22%
OPEB 2014	4.83%	4.65%	3.87%	N/A	4.92%
OPEB 2015	4.04%	4.07%	4.20%	N/A	4.14%

Comment [HR5]: These figures (3.96% and 3.97%) appear to be outliers; they should be checked to ensure apples-to-apples comparison.

The KCPL and GMO to industry-average comparison shows that KCPL and GMO estimates for the discount rate are generally in-line with Missouri electric utilities and Westar, and the peer utility group.

RATE OF FUTURE COMPENSATION INCREASE

The rate of future compensation increase is an assumption concerning the future earnings of employees included in the pension plan. This assumption is developed by management and is based on historical compensation increases and on expectations of future increases in salaries and wages. As the assumption of the rate of future compensation increases so does the PBO and net periodic cost. Increases in compensation over time will increase benefit payments. OPEB plans do not always include rates of compensation increase, but instead they can include rate of increase of health care costs.

Future Compensation Increase	Missouri & Westar Averages	Peer Utility Averages	PWC Survey Averages	Deloitte Survey Averages	KCPL & GMO
Pension 2014	3.75%	3.90%	3.85%	3.75%	3.69%
Pension 2015	3.75%	3.92%	3.78%	3.74%	3.62%
OPEB 2014	3.67%	4.07%	N/A	N/A	3.50%
OPEB 2015	3.67%	4.11%	N/A	N/A	3.50%

The KCPL to industry-average comparison shows that KCPL's estimates for the rate of future compensation increases are generally in-line with Missouri electric utilities and Westar, and the peer utility group.

EXPECTED RETURN ON ASSETS

The expected return on assets is management's assumption of the overall rate of return on the pension and OPEB plan assets. This assumption is developed by management and is based on historical rates of return and expectations of future rates of return on plan assets. The expected return can vary with the demographics of the employee population, management's approach to plan investment, and the overall state of financial markets. Some OPEB plans are unfunded, "pay as you go" plans and do not have any assets in a trust. Staff's expected rate of return comparison is in the table below:

Expected Return	Missouri & Westar Averages	Peer Utility Averages	PWC Survey Averages	Deloitte Survey Averages	KCPL & GMO
Pension 2014	7.25%	7.16%	7.21%	7.10%	7.24%
Pension 2015	7.25%	6.99%	7.06%	6.99%	7.14%
OPEB 2014	6.51%	6.28%	N/A	N/A	2.70%
OPEB 2015	6.51%	5.87%	N/A	N/A	2.81%

The KCPL and GMO to industry-average comparison shows that KCPL and GMO estimates for the rate of future compensation increases are generally in-line with Missouri electric utilities and Westar, and the peer utility group. The low expected rate of return for OPEB is due to KCPL's and GMO's OPEB expected rate of return listed as after tax.

ACTUAL RETURN ON ASSETS

The actual return on assets is not a management assumption but rather the earned return on the pension and OPEB assets during the year. Staff used the actual returns on the fair value of assets at January 1 of 2014 and 2015. The actual earned return can vary with the demographics of the employee population, management's approach to plan investment, and the overall state of financial markets. The Deloitte and PwC pension and OPEB surveys did not include metrics on the actual return on assets. Staff's actual rate of return comparison is in the table below:

Actual Return on Assets	Missouri & Westar Averages	Peer Utility Averages	KCPL & GMO
Pension 2014	9.32%	9.26%	6.71%
Pension 2015	-1.26%	-1.93%	-2.23%
OPEB 2014	4.79%	5.28%	4.05%
OPEB 2015	-0.49%	-1.68%	-0.09%

Comment [HR6]: What is the source of the data for this entire table?

Attachment A

The KCPL and GMO to industry-average comparison shows that KCPL and GMO's actual rate of return is generally lower compared to other Missouri electric utilities and Westar, and the peer utility group. This can be attributed to the impacts of the financial downturn of 2008 and the asset mix utilized by the peer utilities.

FUNDED STATUS

The funded status of pension and OPEB plans is the PBO compared to the fair value of the assets in the pension trust. Pursuant to the PPA, and as modified, the target funding to KCPL's DB plan is 100% over seven years. The Accumulated Benefit Obligation ("ABO") is comparable to the PBO but without any future benefit obligations and represents all future costs as if the pension plans were "frozen" at the salary level at present. Staff did not list the ABO because none of the plans in Staff's review were "frozen". Staff's funded status comparison is in the table below:

Funded Status (End of Period)	Missouri & Westar Averages	Peer Utility Averages	PWC Survey Averages	Deloitte Survey Averages	KCPL & GMO
Pension 2014	71.48%	82.73%	81%	81%	61.51%
Pension 2015	72.60%	81.28%	81%	81%	62.69%
OPEB 2014	84.71%	52.13%	N/A	N/A	66.95%
OPEB 2015	91.15%	52.91%	N/A	N/A	83.13%

The KCPL and GMO to industry-average comparison shows that KCPL's funded status is generally in-line with Missouri electric utilities and Westar, and the peer utility group. It should be noted that while KCPL and GMO's funded status is less than the averages listed, there are other gauges of funded status, such as those calculated under ERISA or PPA that results in a higher funded status. Additionally, most of the peer utility pension and OPEB plans are closed to new members and have been so for several years. Closing pension and OPEB plans to new members reduces future benefits and reduces the increase to the PBO. Closed plans will have higher funded statuses over time with no change in contributions. KCPL and GMO only recently closed their ~~Management~~Non-Union Pension Plan to new members and while pension costs will decrease over time there is no immediate reduction in expense.

PENSION COST MITIGATION

During the review, Staff submitted several data requests relating to pension and OPEBs costs. These cost elements have been increasing significantly over the last several years. Both KCPL and GMO have received special tracker rate treatment for these costs because of their increases and volatility.

In an October 12, 2016 interview, conducted specifically to address employee benefit costs, several reasons were identified by KCPL personnel (Kelly Murphy, Senior Director, Human Resources, Joyce Swope, a~~n~~ Lead Analyst in Regulatory Accounting, and Mark Foltz, Senior Project Director) regarding pension and OPEBs cost increases:

- Discount Rate— the lower the discount rate the larger the PBO, and consequently the lower the funded status. In 2009, the discount rate used by KCPL was 6.1%; the discount rate as of December 31, 2014 was 4.2%, resulting in higher pension costs.
- Mortality Rates have decreased for individuals causing the assumption for life expectancy to increase resulting in higher pension costs— In 2014 the Society of Actuaries Retirement Plans Experience Committee ("RPEC") issued a new mortality table (Retirement Plan ("RP"~~)~~-2014) and mortality improvement scale (MP-2014) ~~mortality rates issued by actuaries~~which substantially increased life expectancies. KCPL ~~used 75%~~adopted ~~of the~~ RP 2014 but modified the improvement scale grading over 10 years to a long-term improvement rate of 0.75% for ages up to 85 declining to 0.00% at age 95 (as compared to 1.00% used in MP-2014 declining to

Attachment A

0.00% at age 115). The RPEC has subsequently issued RP 2015/MP-2015 which has decreased life expectancies closer to the level used by KCPL ~~used~~.

- Investment returns experienced from the pension assets declined causing increased pension costs. The pension assets have not earned as great a return on assets, resulting in less actual returns and an increase in pension costs.
- Increased Funding – PBO funding is currently in the mid- to upper 60% level, up from the upper 50% level in the past. KCPL's and GMO's pension funding is over 100% of the ERISA minimum requirement.

Employee benefit costs have increased substantially over the last several years driving up the A&G costs. In addition to pension and OPEB cost increases, medical insurance costs have increased as well putting further pressure on A&G costs.

As previously noted in this report, while KCPL and GMO's funded status is less than the averages listed, there are other gauges of funded status, such as those calculated under ERISA or PPA that results in a higher funded status. Funded status per ERISA is used to base future contributions, and is consequently the guiding factor in determining the viability of a pension or funded OPEB plan.

PENSION AND BENEFIT EXPENSE COMPARED TO OTHER UTILITIES

Staff compared the portion of A&G costs in Account 926 – Employee Pensions and Benefits to the overall A&G costs identified in Staff's study. This comparison included Account 926 – Employee Pensions and Benefits as a percentage of Total A&G expense, and as a percentage of Total O&M Expense:

2013 Peer Utility FERC Form 1 Pension Comparison	**GMO**	**KCPL**	**Combined KCPL and GMO**
Account 926 Pensions and Benefits	$ 29,593,080	$ 69,852,014	$ 99,445,094
Account 926 as a % of A&G Expense	39.70%	44.85%	43.18%

Ranking (1, is lowest)	8	14	13
Account 926 as a % of Total O&M	6.52%	7.35%	7.08%
Ranking (1, is lowest)	14	17	16

2014 Peer Utility FERC Form 1 Pension Comparison	**GMO**	**KCPL**	**Combined KCPL and GMO**
Account 926 Pensions and Benefits	$ 29,989,590	$ 76,625,030	$ 106,614,620
Account 926 as a % of A&G Expense	40.19%	47.33%	45.08%
Ranking (1, is lowest)	14	18	16
Account 926 as a % of Total O&M	5.76%	7.65%	7.01%
Ranking (1, is lowest)	15	18	16

2015 Peer Utility FERC Form 1 Pension Comparison	**GMO**	**KCPL**	**Combined KCPL and GMO**
Account 926 Pensions and Benefits	$ 28,787,691	$ 81,157,597	$ 109,945,288
Account 926 as a % of A&G Expense	36.13%	50.47%	45.72%
Ranking (1, is lowest)	12	17	15
Account 926 as a % of Total O&M	6.11%	8.62%	7.78%
Ranking (1, is lowest)	15	18	17

As can be seen from the comparison, KCPL and GMO rank among the highest, out of 18 utilities, for pension expense as a portion of A&G expenses and as a portion of total O&M expenses. KCPL and GMO's comparatively high pension expenses as a portion of A&G expenses are reflected in the metrics Staff used in the overall A&G comparison: A&G per customer, revenue, megawatt hour sold, and compared to O&M. Consequently, high pension and benefit expenses is a key driver of KCPL and GMO's high A&G expenses in Staff's comparison of Missouri electric utilities, Westar, and the utility peer group.

The key drivers of pension expense are lower discount rates, lower mortality rates (longer employee lives), lower rates of return, and higher contributions. KCPL has made recent changes to their offered pension benefits, namely elimination of pension benefits for future management hires and cash balance pension plan offerings to future union hires. These changes will decrease pension expense over time but reductions will not be observed in the immediate or near future as pension costs continue to be incurred and recognized on employees hired before these changes were instituted. Staff did note that several of the peer utilities instituted these or similar changes and did so during the last decade. The savings resulting from these changes would be at a more advanced state the earlier a utility instituted the changes, which would result in a lower overall pension expense.

EMPLOYEE EXPENSE ACCOUNT PROCESS

The expense accounts process is a component of A&G although employee expenses may be booked to any number of "above-the-line" accounts including the 500 through 935 series of the USOA. Above-the-line accounts are classified on the Company's records as those costs to be funded by rate payers. Employee expenses may also be booked "below-the-line" in account numbers 417 through 426. Such below-the-line accounts are to be funded by the Company's shareholders and not expected to be recouped in regulated customer rates.

In addition, KCPL and GMO charge certain costs to non-regulated business units of Great Plains Energy. While the Company identifies the costs to these non-regulated entities as "above-the-line" accounts, because the costs are booked on non-regulated business units, those costs have the effect of "below-the-line" treatment as those costs are not included in regulated KCPL or GMO customer rates.

KCPL's expense account process and various expense account charges have drawn extensive rate case audit attention and some press attention for a number of years, since approximately 2009. Some recounting of the history on this topic is necessary to understand at least a portion of the context in which the expense account process has been examined in the management audit.

A. BRIEF HISTORY OF THE KCPL EXPENSE ACCOUNT ISSUE

On February 5, 2009, a Kansas City Star article criticized KCPL for expense account expenditures such as $200,000 for World's of Fun tickets, $188,000 for golfing fees, tickets to the Kansas City Chiefs and Royals games, various expenses for flowers, movie tickets, gift cards, banquet fees, etc. In Case No. ER-2009-0089[17], Staff witness Charles R. Hyneman addressed the issue of KCPL and GPE officer expense accounts and made an adjustment in KCPL's 2009 rate case for what Staff concluded to be excessive and inappropriate charges included in the KCPL cost of service. Staff further found fault with the Company's lack of sufficient internal controls on the officer expense account process which allowed inappropriate expenditures to flow to customer rates. The Non-Unanimous Stipulation and Agreement filed in the case specifically included the following language:

17. <u>Miscellaneous Costs Not Included in Rates</u>

> The Signatory Parties agree that the following costs are not included in the rate levels contained in this agreement: Sporting events, golf events, Worlds of Fun tickets, dues and donations, lobbying, image or institutional advertising, spousal travel, local meal expenses, officer expense reports, and catering expense. The Signatory Parties reserve the right to seek inclusion or oppose inclusion of these costs in a future rate case.[18]

The Commission approved the Non-Unanimous Stipulation and Agreement on June 10, 2009 with an effective date of June 23, 2009 and found the stipulated revenue requirement to be "just and reasonable" and "fair to both the utility and its customers."

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[17] Case No. ER-2009-0089, Direct Testimony in Staff's Cost of Service Report by Charles R. Hyneman, pp. 127-130.
[18] Non-Unanimous Stipulation and Agreement, Case No. ER-2008[sic]-0089, page 9, filed April 24, 2009.

In Case No. ER-2010-0355, KCPL's accounting witness John P. Wiesensee[19] made an adjustment for certain expense report charges while stating "We believe the costs were ordinary and reasonable business expenses; however, we do not believe such costs should be borne by rate payers." Company witness Curtis D. Blanc[20] also wrote direct testimony on this matter in GMO's 2010 rate case (Case No. ER-2010-0356) stating that the officer expense account process had been a "distraction" from more significant issues and that GMO had removed all officer expense charges incurred during the test year for that rate case. The Company's expense account process and various charges also drew attention from the Staff in the Company's 2012 and 2014 rate cases, Case Nos. ER-2012-0174 and ER-2014-0370.

Specifically in Case No. ER-2014-0370 Staff witness Charles R. Hyneman provided this testimony, in part, about officer expense reports:

> . . . In several previous KCPL rate cases Staff has also found problems with the prudence, excessiveness and reasonableness of KCPL and Great Plains officer expense report charges. Staff is aware of attempts by KCPL to mitigate the detriment to its customers from these types of expenses, including in a previous rate case, KCPL making rate case adjustments to remove all officer expense report charges. In response to Staff's concerns in these prior cases KCPL appeared to implement internal control procedures designed to reduce the risk of unreasonable, imprudent and excessive officer expenses from being charged to KCPL ratepayers. It seems KCPL has either failed to continue with these internal control measures or the measures are ineffectively administered.[21]

Mr. Hyneman further went on to list several KCPL officer expense account charges that were of concern to Staff. The "Partial Non-Unanimous Stipulation and Agreement as to True Up, Depreciation and Other Miscellaneous Issues," filed July 1, 2015 included the following provision and commitment by KCPL toward resolving Staff concerns with the Company's expense account process:

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[19] Case No. ER-2010-0355, Direct Testimony of John P. Wisensee page 42, lines 16 through 18, and Schedule JPW2010-2.
[20] Case No. ER-2010-0356, Direct Testimony of Curtis D. Blanc page 7, lines 7 through 15.
[21] Case No. ER-2014-0370, Direct Testimony in Staff's Cost of Service Report by Charles R. Hyneman, pages 159-161, 159.

G. EXPENSE ACCOUNT IMPLEMENTATION PLAN

> KCP&L will submit to Staff and interested parties to this case an implementation plan 180 days after the date rates are effective in this case regarding the actions, if any, it will implement to address expense account issues, such as proper account charging, reporting and other issues noted by the Staff in this case.

On March 24, 2016 KCPL e-mailed Staff, Public Counsel and MECG its approximate two-page plan to tighten internal controls around its expense account process. A copy of the Company's original e-mail and its expense account implementation plan are attached as Schedule 4. A summary of the key activities the Company identified to address the expense account issues includes:

- Defaulting officer expense accounts to be set to "below-the-line."
- ~~Additional review by Wells Fargo to ensure Company credit card policy compliance and accurate accounting coding.~~The Wells Fargo company credit card program administrator (a KCPL employee) is reviewing various samples of company credit card business transactions each month to ensure company credit card policy compliance as well as accurate accounting code block coding is followed.
- Job Aids for Executive Administrative Assistants were reviewed to ensure accuracy of coding and accounting and training of the Assistants was conducted.
- Wells Fargo (the Company's credit card provider) has been provided a shortened list of account block code values to reduce the list from which employees can choose for credit card purchases.
- Default accounting code values were reviewed and resulted in employee education on the proper use of codes.
- Default accounting codes are now reviewed on a quarterly basis.
- Changes were made to the General Allocator

B. COMPANY INTERNAL AUDIT ACTIVITIES REGARDING EXPENSE ACCOUNT PROCESS

Comment [HR7]: This is not accurate as Wells Fargo does not provide any review.

Staff interviewed the Company's Senior Director of Audit Services, Mr. Tony Jackson, on October 12, 2016. Mr. Jackson discussed with Staff that his internal audit team produces Continuous Assurance Program ("CAP") audits every year. These audits reexamine various operational aspects on a regular or periodic basis such as yearly. Other select audits are driven by identified risks to the organization. Audit planning begins in the fall prior to the next year the audits will be performed. Internal Audit prepares the Audit Plan based on a risk assessment driven from a number of sources, including participation in Risk Summits conducted as part of the Company's Enterprise Risk Management program, to prioritize where audit resources are utilized. The Audit Plan is recommended to the Audit Committee of the Board of Directors annually~~in December~~ and once approved, an audit schedule is developed and updated throughout the year. ~~Risk Summits are conducted every three to four years and they review all aspects of the completed audits and what risks to the organization may have increased the greatest to determine what may require future auditing resources.~~ There have been no comprehensive internal audits of A & G costs specifically but Audit Services indicates that they have audited particular accounts that impact A & G costs.[22] The following represents a sample of past Audit Services issues, opportunities and assessments in relation to the Company's expense account process that the Company provided in response to Staff Data Requests Nos. 9 and 16:

- ** ____________________ **
- ** ____________________ **
- ** ____________________ **
- ** ____________________ **

[22] Interview with the Director of Audit Services, Mr. Tony Jackson, on October 12, 2016.

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Attachment A

- ** ____________________ **
- ** ____________________ **
- ** ____________________ **
- ** ____________________ **[25]
- ** ____________________ **
- ** ____________________ **
- ** ____________________ **[27]

~~The Company indicates that all past internal audits include "action plans."~~ In some cases, a determination may have included that even though an action was found to have been against

Comment [HR8]: All of these audit findings are HC ** ____________________ **

Comment [HR9]: This is not accurate and should be struck or re-written What is the source?

[23] Response to Staff Data Request No. 9 - Case No. EO-2016-0124, September 2011 Procurement Card Audit Report.
[24] Response to Staff Data Request No. 16 – Case No. EO-2016-0124 April 2014 Continuous Assurance Program Procurement and T&E Corporate Card Analytic Results- Q4 2013.
[25] Response to Staff Data Request No. 16 – Case No. EO-2016-0124, May 2014 Continuous Assurance Program Procurement and T&E Expense System Analytic results- Q4 2013.
[26] Response to Staff Data Request No. 16 – Case No. EO-2016-0124 December 2014 Continuous Assurance Program Procurement and T&E Corporate Card Analytic Results- Q1 and Q2 2014.
[27] Response to Staff Data Request No. 16 – Case No. EO-2016-0124 June 2015 Continuous Assurance Program, Travel and Entertainment Expenses.

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the expense account policy, risk indicators were ~~evaluated~~identified and analyzed, exceptions noted and a determination made that no additional follow-up was required.

In July 2016, an internal audit report entitled "Risk Area Detail For the Corporate Expense Reporting Audit" was completed. This report includes a review of the Commercial Credit Card Reporting ("CCER") system now being utilized as part of the Wells Fargo corporate card provider. The report includes both opportunities for improvement (for example: ** ____ **) as well as improvements generally from the new system compared to the prior system (for example: ** ____ **). Another issue that was identified was that ** ____ **[28] The HC Audit Report is attached in its entirety as Schedule 6.

Comment [HR10]: This is an HC audit finding

Comment [HR11]: This is an HC audit finding

Comment [HR12]: This is an HC audit finding

SIGNIFICANT CHANGES TO KCPL's EXPENSE ACCOUNT PROCESS

One significant change impacting the expense account process has been the combination of five travel, entertainment and procurement cards into one Company corporate credit card and a separate fleet card. The Company's prior credit card company would not comply with "chip" security technology which prompted the Company to eliminate all prior cards and move to the Wells Fargo vendor.[29] The Company's response to Staff Data Request No. 36 in Case No. EO-2016-0124 (attached as Schedule 5) addresses some of the specific changes

[28] HC July 2016 Corporate Expense Reporting Audit Report, provided in response to Staff Data Request No. 47 in File No. EO-2016-0124.
[29] Maria Jenks and Steve Busser Joint Interview – September 20, 2016.

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associated with the use of the Wells Fargo expense account system. Specifically, the Company's response states, in part:

> . . . When a purchase is made, default accounting codes are applied based on information provided by the company to Wells Fargo for each individual user and the type of purchase (determined by the merchant category code). The employee is then required to upload receipts electronically and to verify that the correct accounting codes have been applied. After the employee has reviewed and approved, a manager will review and give final approval. Out-of-pocket expenses, such as mileage, follow a similar process. In all cases, everything related to the expense accounts is completed online in the Wells Fargo system, so a cover sheet is not required to be utilized as was the case in the PeopleSoft system. . .

The Company revised its prior Expense Account Policy due to a determination that improvements were needed in the policy as well as changes with the Company's purchasing and travel card vendor. The new policy became effective January 1, 2016. One of the most significant changes is the requirement for receipts for all transactions except mileage. The revised expense account policy is attached as Schedule 7. ~~as well as~~In addition, a new management procedure was put in place providing that all officer expense accounts ~~to~~ default to below-the-line accounts. Officer expense accounts must be manually moved to accounts above-the-line. ~~The revised expense account policy is attached as Schedule 7.~~

ISSUES OF CONCERN WITH THE COMPANY'S EXPENSE ACCOUNT PROCESS

While the Company has made some positive improvements to tighten the internal control of its expense account process, in Staff's opinion the Company's current expense account policy has weakness. Staff found various expense accounts that appeared not to meet all of the requirements of the existing expense account process, for example some did not include receipts or had a complete list of meeting/event attendees (For expense account purposes, KCPL requires employees to identify specific meetings and events attended as well as those in attendance at such functions—in some cases the meeting/ event listings were not complete).

Attachment A

The expense account provision that is of concern to Staff for the protection of regulated retail customers and to ensure strong internal control is under the section of "Valid Business Expenses" and is the definition of "reimbursable" expenses. In the Company's current expense account policy, reimbursable entertainment expenses are defined as:

> Food, beverages and entertainment for employees and non-employee business guests where the business purposes of the Company **<u>can</u>** be advanced immediately, before, during or after the occasion.

It is the use of the word "can" that Staff considers excessively vague and creating an opportunity for the payment of food, beverages and entertainment for employees and non-employee business guests that "can," but is not required to be sought to be advanced as part of the business purposes of KCPL. If utility rate payers or shareholders are paying for travel, meals, entertainment, gifts etc., it would seem imperative that a firm line be drawn that such expenses must and without waver, advance the business purposes of the Company. The Company may argue that expenses are reviewed by employee supervisory personnel to ensure the business purpose is advanced but the policy clearly does not require it. Policies are written to direct employee actions and ensure appropriate internal control, which the above statement, in Staff's opinion, does not provide.

As have been addressed in prior rate cases, Staff found various officer expense accounts that drew its attention, including those booked both above and below-the-line. While those costs booked below-the-line are not flowed to rate payers, those costs do negatively impact the Company's ability to achieve its authorized return on equity ("ROE") which the Company has publicly stated it has not been successful doing for years. On September 13, 2016, the Company made a presentation during the Case No. EW-2016-0313 Electric Regulatory Reform workshop, held at the Governor Office Building, which included discussion and a slide in its presentation indicating it had not been successful for a decade regarding earning its authorized ROE. This slide included in Mr. Rob Hack's September 13th presentation is attached as Schedule 8. Direct testimony filed in the Company's current rate case, Case No. ER-2016-0285, by the Company's Vice President of Regulatory Affairs, Mr. Darrin R. Ives, provides extensive discussion of the Company's historical inability to achieve its authorized ROE beginning on page 7, line 12 through a chart at the top of page 12.

Examples of some expenditures incurred and booked by the Company below-the-line that appear questionable, particularly in spite of the Company's documented ROE concerns, are expenditures for such things labeled "customer" gifts ($888.47 for four Kansas City Royals field bases and a base display case incurred on January 21, 2016).

Further, the attendance at various professional sporting events such as two Royals games by KCPL executives on April 3, 2016 and April 5, 2016[30] also drew Staff's attention as Staff found no Company attendee list of who attended the second game (a violation of the Company's Expense Account Policy which requires a list of attendees for Meals and Entertainment expenditures) [31] and resulted in charges of $1,475.55[32] being submitted as an expense by a KCPL senior executive. Documentation for the first baseball game, occurring on April 3, 2016, included a list of eleven Company executives with a suite bill for, what appears to be, charges primarily for alcohol. The remaining portion of the bill included a significant gratuity, administrative charges etc. for a total expenditure of $837.31.

[30] Schedule 9 includes a receipt from Royals Authentics, Kauffman Stadium.
[31] Response to Staff Data Request No. 8 in Case No. EO-2016-0124, page 2 "Responsibility of the Approvers" section.
[32] Actual receipt includes an additional $40 cash gratuity which was not accounted for on the Company's books, according to the "Complete Line by Line Transaction Detail for all Credit Card Expenses and Out of Pocket Expenses for all KCP&L Executives for 2016 Year-to-Date" in response to Staff Data Request No. 36.1.

A receipt for a Royals vs. Tigers professional baseball game on September 3, 2016 while booked to an above-the-line account but a non-regulated operating unit, had the description of various purchased items "whited out" or deleted but the dollar amount was shown. In a follow-up inquiry, Staff requested the Company provide a copy of the receipt as it appeared originally with all dollar amount descriptions visible. The Company complied and all "whited-out" items were for alcohol purchases. Regardless of the altered receipt, Staff questions, how much the "business purposes of a regulated utility can be advanced" at a professional sporting event, a requirement in the Company's current Expense Account Policy.

Numerous other examples of expenditures booked below-the-line, but nonetheless drawing attention, have been observed including the attendance by various participants at a Kansas City Chief's game at Arrowhead Stadium with expenses on January 3, 2016 totaling $2,744.87. The total expenditure included approximately $550.00 worth of wine and beer.

A March 24, 2016 e-mail from Mr. Charles Caisley to the Company's Officer Team, began by saying:

"Attached is the FINAL schedule / assignments for the Royals this year. . ." The e-mail went on to state further in its body: "As a reminder, the following guidelines should be followed" and indicates in the fourth bullet that, "The company does not pay for alcohol at employee events" and that "We will not order alcohol to be in the suite when you arrive and we ask that employees not use T&E cards to purchase alcohol."[33] An examination of numerous receipts demonstrates the Company *does pay* a substantial expense for alcohol at employee events and such expenditures are booked both below and above-the-line, to regulated and non-regulated accounts.

[33] See Schedule 9.

It is the expenses booked above-the-line which draw Staff's greatest attention such as an expense for $1,799.82 incurred on October 27, 2015 for food and beverages (including alcohol) for World Series game 1 at the KCPL Suite at Kauffman Stadium for "Business Networking" purposes. Christmas gifts purchased for Company Officers in the amount of $532.48 were also booked above- the-line in December 2015.[34] As of this writing, Staff has not found Company direction regarding the specific purchase of holiday gifts in the Company's expense account policy but would consider either of these expenses to be questionable as expenses to be funded by rate payers, regardless of the amount. Staff found the purchase of IPad equipment booked above-the-line that appears to have been returned for a credit booked below-the-line.[35]

Pages 7, 12 and 33 of the 2015 Great Plains Energy Code of Ethical Business Conduct Training and Certification materials includes the following that, in Staff's opinion, should provide substantial guidance generally regarding the questionable expenditures set out above (See Schedule 10):

- Always be cost conscious
- Would it look good to others if it were published in the newspaper?
- We may participate in the accepted practice of giving and receiving occasional and modest gifts, meals, services or entertainment as a way to promote goodwill and help build positive business relationships.

  An example of a <u>modest</u> gift would be a promotional item, such as a pen or calendar with the company's name on it. These relatively inexpensive gifts should be given or received infrequently and must be customary, legal and of modest value.

Staff notes the definition of "modest gift" and the underlining of the word "modest" in the 2015 Great Plains Energy Code of Ethical Business Conduct Training and Certification.

[34] *Ibid.*
[35] Response to Staff Data Request Nos. 36 and 36.1 in Case No. EO-2016-0124.

For this management audit, Staff did not do an exhaustive audit of the Company's expense account process and purchases, as those have been examined extensively by Staff in prior KCPL and GMO rate cases. However, Staff has the opinion that the Company's expense account process required re-visitation to some modified extent in the present Management Audit as such expenditures are 1) a component of A & G and 2) the Company's expense account process has historically been a concern expressed by Staff in prior rate cases. While Staff attempts to make adjustments in rate cases for expense issues such as those identified above, in Staff's opinion, such adjustments do not entitle nor should they enable the Company to exercise anything less than vigilant internal control for all expenditures, but particularly for those such as those noted above that are booked above-the-line and to regulated accounts.

KCPL's AND GMO 's CURRENT AND HISTORICAL CUSTOMER RATES

On page 3 of Staff's Proposed Audit Scope, Staff listed a review and determination of KCPL's current and historical customer rates including adjustments made in A & G expenses.

KCPL overall rates for Missouri have gone from 5.65 cents per kilowatt hour in 2005 to 9.34 cents per kilowatt hour on December 31, 2015, or a 65.3% increase.36

MPS overall retail rates in Missouri have gone from 6.45 cents per kilowatt hour in 2005 to 9.93 cents per kilowatt hour in 2015, or a 54% increase. L&P overall retail rates in Missouri have gone from a 5.20 cents per kilowatt hour in 2005 to 9.35 cents per kilowatt hour in 2015, or a 79.8% increase.37

As a result of the Commission's Order Approving Stipulations and Agreements, Rejecting Tariffs, Cancelling True-Up Hearing, and Ordering Filing of Compliance Tariffs dated September

[36] Using EEI Winter 2016 Report, page 178—KCPL's total average rates- 2015 of 9.34 cents per kWh compared to 2005 of 5.65 cents per kWh representing a 65.3% increase.
[37] Using EEI Winter 2016 Report, page 178-- MPS's total average rates- 2015 of 9.93 cents per kWh compared to 2005 of 6.45 cents per kWh representing a 54.0% increase and L&P's total average rates- 2015 of 9.35 cents per kWh compared to 2005 of 5.20 cents per kWh representing a 79.8% increase.

28, 2016 in Case No. ER-2016-0156, MPS and L&P rates will be consolidated at the effective date of rates of December 22, 2016. On a going-forward basis, there will not be separate MPS and L&P rates, there will be one GMO set of rates. For Staff's analysis, the data used include the historical MPS and L&P rates.

Staff made a comparison of KCPL's and GMO's electric rates broken out between KCPL and GMO's MPS territory and L&P territory with other electric utilities in Missouri and Kansas. Based on information compiled by the Edison Electric Institute ("EEI"), KCPL's and GMO's rates are higher than regional[38] and State of Missouri averages.

KCPL and GMO have experienced significant rate increases since the early 2000s and their rates have increased faster than the national average over that period. Below is a table that identifies KCPL's and GMO's overall rates with GMO's rates broken out for MPS and L&P which includes all classes of customers – residential, commercial and industrial, or large volume users. KCPL's and GMO's overall rates are below the national average during the period 2005 to 2015. But the national average rate increased 30.3%,[39] compared to KCPL's 65.3% increase, MPS' 54% increase and L&P's 79.8% increase over this period. The West North Central region, which includes GMO, experienced an overall increase of 46.3%. KCPL's and GMO's overall rates continue to be above the regional average and the State of Missouri average.

The following tables on retail customer rates are based on information from the Edison Electric Institute's Typical Bills and Average Rates Report Winter 2016 publication for Total Retail Average Rates:

[38] KCPL and GMO are in the West Central Region which includes Iowa, Kansas, Minnesota, Missouri, North Dakota and South Dakota.
[39] The 30.3% increase for the national average is determined comparing 2015 rate of 10.71 cents to 2005 rate of 8.22 cents (10.71 cents/8.22 cents). This same calculation is made for both MPS and L&P.

Attachment A

Utility Company	2015[40]	2014	2013	2012	2011	2010	2009	2008	2007	2006	2005
MISSOURI RETAIL AVERAGE RATES—CENTS PER KWH											
KCPL-Missouri	9.34 cents/ kwh Sept 2015 ER-2014-0370	8.89	8.78 Jan 26, 2013 ER-2012-0174	8.23	8.01 May 4, 2011 ER-2010-0355	7.69	6.88 Sept 1 ER-2009-0089	6.51 Feb 1 ER-2007-0291	6.14 Feb 1 ER-2006-0314	5.66	5.65
MPS	**9.93**	9.56	9.51	9.48	9.31	9.09	8.36	7.79	7.33	6.85	6.45
L&P	**9.35**	9.14	9.10	8.49	7.34	6.75	6.34	5.93	5.63	5.30	5.20
Ameren Missouri	8.53	8.02	8.12	7.36	7.16	6.48	5.95	5.43	5.46	5.43	5.49
Empire-Missouri	11.09	11.0 0	10.65	10.35	10.07	8.96	8.45	8.18	8.03	7.33	7.09
Missouri Average	**9.01**	**8.56**	**8.58**	**7.96**	**7.72**	**7.11**	**6.55**	**6.04**	**5.93**	**5.74**	**5.71**
KANSAS RETAIL AVERAGE RATES—CENTS PER KWH											
KCPL-Kansas	10.99	10.40	10.42	9.87	9.43	8.57	8.06	7.46	6.73	6.35	6.32
Empire - Kansas	10.76	10.39	10.15	10.48	10.11	9.25	8.41	8.69	8.61	8.06	6.54
Westar Energy -- KGE	9.43	9.54	8.87	8.42	7.90	7.46	7.13	6.32	5.73	6.04	6.03
Westar Energy -- KPL	10.06	10.17	9.42	8.99	8.28	8.15	7.82	6.92	6.06	6.25	5.58
Kansas Average	10.06	9.99	9.46	9.00	8.43	8.00	7.62	6.84	6.12	6.35	6.14
West North Central	**8.95**	**8.70**	**8.56**	**8.06**	**7.82**	**7.53**	**7.14**	**6.81**	**6.51**	**6.38**	**6.17**
United States Average	**10.71**	**10.73**	**10.37**	**10.09**	**10.09**	**9.97**	**9.83**	**9.77**	**9.21~~0~~**	**8.89**	**8.22**

Source: EEI Winter 2010 Report, page 180 provided response to Staff Data Request No. 380- ER-2010-0355

[40] The EEI rate amounts are average price per kWh billed to customers and do not represent tariff rates. These average rates for each period are the levels at December 31 year end.

Attachment A

EEI Winter 2012 Report, page 180 provided response to Staff Data Request No. 241- ER-2012-0174
EEI Winter 2014 Report, page 179; EEI Winter 2015 Report, page 178; EEI Winter 2016 Report, page 178

None of these increases include any impact of changes in rates that may result from the recently completed GMO case with effective date of rates on December 22, 2016 or the current KCPL with effective date of rates on May 28, 2017.

Staff also reviewed electric rates of the peer group utilities in Staff's A&G analysis. The following table identifies the utility, the state in which the utility operates and the utility's rates in cents per kilowatt hour for the period 2013 to 2015:

Holding Company	Utility	States	EEI Rate Book Region	2015	2014	2013
	KCPL-Missouri	**Missouri**	**West North Central**	**9.34 cents/kwh**	**8.89**	**8.78 Jan 26, 2013 ER-2012-0174 and ER-2012-0175**
	MPS	Missouri	West North Central	9.93	9.56	9.51
	L&P	Missouri	West North Central	9.35	9.14	9.10
Alliant						
	Interstate Power & Light	Iowa	West North Central	9.53	9.27	9.32
		Minnesota	West North Central	8.96	9.02	8.68

	Wisconsin Power & Light	Wisconsin	East North Central	9.37	9.71	9.63
Avista		Idaho	Mountain	7.80	7.52	7.07
		Washington	Pacific	8.14	8.63	8.42
Black Hills Corporation	Black Hills Power	Montana	Mountain	6.29	6.31	6.58
		South Dakota	West North Central	11.20	10.63	10.10
		Wyoming	Mountain	9.84	8.38	7.93
	Cheyenne Light Fuel and Power	Wyoming	Mountain	10.92	10.37	10.03
	Colorado Electric Utility Company (formerly Aquila Networks WPE)	Colorado	Mountain	9.69	8.97	11.54
Cleco Power LLC		Louisiana	West South Central	9.84	10.21	10.32
IdaCorp	Idaho Power Company	Idaho	Mountain	8.07	7.96	7.52
		Oregon	Pacific	8.00	8.07	7.92
OGE Company	Oklahoma Gas & Electric	Arkansas	West South Central	6.47	6.86	6.60
		Oklahoma	West South Central	7.52	8.05	7.80
Pinnacle	Arizona Public Service Company	Arizona	Mountain	11.76	11.60	11.51
Texas New Mexico	Public Service	New Mexico	Mountain	11.15	10.85	10.34

Power	Company of New Mexico					
Portland General Electric		Oregon	Pacific	9.58	9.51	9.79
Tampa Electric Company		Florida	South Atlantic	10.45	10.56	10.14
UNS	Tucson Electric Power Company	Arizona	Mountain	10.51	9.92	9.57
We Energies	Wisconsin Electric Power	Michigan	East North Central	7.29	13.26	12.76
		Wisconsin	East North Central	11.97	11.97	11.81

Source: EEI Winter 2014 Report, pages 161 to 196; EEI Winter 2015 Report, pages 161 to 195; EEI Winter 2016 Report, pages 161 to 195.

KCPL's and L&P's overall retail rates at the end of 2015 are higher than Arkansas, Idaho, Michigan, Minnesota, Montana, Oklahoma, Oregon and Washington. MPS' rates are higher than Arkansas, Idaho, Michigan, Minnesota, Montana, Oklahoma, Oregon, Washington and Wyoming.

MANAGEMENT AUDIT FINDINGS AND CONCLUSIONS:

1 Few if any synergies remain to be achieved from the 2008 acquisition of Aquila, Inc. if GMO and KCPL were merged. Some negative consequences may arise from the merger of GMO and KCPL in the form of property tax restructuring.

2) KCPL A&G expenses are high in numerous comparisons, driven primarily by Pension Expense. The Company has taken actions to better control pension expense and while the benefit of those actions will not be realized in the near term, they are anticipated to eventually lower A&G costs.

3) No comprehensive internal audit has been performed of the Company's A-&-G expenses.

Comment [HR13]: Note that, in addition to the many audits conducted by Internal Audit each year that touch elements of A&G expense, there is an annual review of the CCER system by all KCP&L department heads and executives identified as having system users. For 2016, this review was completed in Oct. 2016.

4) While the Company has taken positive action to address various expense account weak internal controls identified by Staff in past rate cases, opportunities for improvement still exist. The Company's expense account definition for reimbursement for travel and entertainment is written overly broadly and the Company's internal control over its expense account process, while improved, has not been consistently effective, particularly in light of the Company's public and well documented concerns regarding its inability to earn its ROE.

5) There is no tracking mechanism in place to record the expense accounts that are moved from below-the-line to above-the-line by Company executives.

6) Significant Company alcohol expenditures are sometimes an above-the-line – regulated account expenditure.

MANAGEMENT AUDIT RECOMMENDATIONS:

Staff recommends that KCPL management:

Track and Monitor the Cost-Savings Benefits of the Company's Changes to its Pension Benefits.

Analyze and Monitor A-&-G Expenses on a Continual Basis to Determine Opportunities to Reduce Such Expenses.

Direct the Performance of a Comprehensive Internal Audit of A-&-G Expenses Within the Next 12 months.

Revise the Current Expense Account Policy to Require that Entertainment Expenses Promote the Business Purposes of the Company when Regulated Accounts are Booked with Such Expenditures.

Develop a Tracking Mechanism to Monitor the Movement of Executive Expenses to "Above-the-Line" or Missouri Regulated Utility Accounts.

Attachment A

<u>Develop and Adhere to a Policy that Defines and Prohibits Material Alcohol Expenses From Being Booked "Above-the-Line" to Missouri Regulated Utility Accounts.</u>