BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

In the Matter of Kansas City Power & Light Company's Request for Authority to Implement a General Rate Increase for Electric Service	))))	Case No. ER-2014-0370

TRUE-UP / REPLY POSTHEARING BRIEF

OF

MIDWEST ENERGY CONSUMERS GROUP

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BEFORE THE PUBLIC SERVICE COMMISSION
<u>OF THE STATE OF MISSOURI</u>

In the Matter of Kansas City	)	
Power & Light Company's Request	)	Case No. ER-2014-0370
for Authority to Implement a General	)	
Rate Increase for Electric Service	)	

INITIAL POST-HEARING BRIEF OF
MIDWEST ENERGY CONSUMERS' GROUP

COME NOW the Midwest Energy Consumers' Group (collectively referred to herein as "MECG") by and through the undersigned counsel, pursuant to the Commission's December 12, 2014 *Order Setting Procedural Schedule and Establishing Test Year and Other Procedural Requirements*, and provides its True-Up / Reply Post-hearing Brief. In this brief, MECG will address the following issues: (1) Cost of Capital (Issue I); (2) Fuel Adjustment Clause (Issue II); (3) Transmission Tracker (Issue III); (4) Property Tax Tracker (Issue IV); (5) Critical Infrastructure Protection ("CIP") / Cyber-Security Tracker (Issue V); (6) Management Audit (Issue XVII); (7) Income Tax-Related Issues (Issue XIX); (8) Class Cost of Service / Rate Design (Issue XXV) and (9) True-Up Issues.

I. INTRODUCTION

In its Initial Brief, MECG encouraged the Commission "to avoid deciding issues in a vacuum."[1] Instead, MECG asserts that the Commission "should view each issue in this case with recognition of the overall status of the case."[2] In this way, the Commission should, in its consideration of each issue, be cognizant of the rapid increase in KCPL's rates over the last 9 years. Specifically, since January 1, 2007, KCPL has received the following rate increases.[3]

• ER-2006-0314:	$50.6 million	10.46% increase
• ER-2007-0291:	$35.3 million	6.50% increase
• ER-2009-0089:	$95.0 million	16.16% increase
• ER-2010-0355:	$34.8 million	5.25% increase
• ER-2012-0174:	$67.4 million	9.64% increase
	$283.1 million	57.69% increase

The 57.69% increase is exacerbated by the fact that KCPL is virtually guaranteed another double digit rate increase. As detailed in cross-examination, KCPL's quantification of its current revenue requirement is $125.7 million (14.68%).[4] On the other hand, despite its exceptional work in this proceeding, Staff's revenue requirement details a revenue deficiency of $87.3 million (11.37%).[5] ***As such, under any scenario, KCPL's rates will have increased 75.68% - 80.83% in less than less than 8 ½ years***.

MECG asserts, therefore, that the Commission should be aware that, when it considers KCPL's request for an inflated return on equity, that KCPL's rates have already

[1] MECG Initial Brief, page 5.
[2] *Id.*
[3] Exhibit 200, Staff Cost of Service Report, page 11.
[4] Tr. 2029.
[5] *Id.*

increased 80% in less than 9 years. Similarly, when the Commission contemplates KCPL's request to include cost increases occurring after the true-up date, it should be acutely familiar with the fact that KCPL's ratepayers have suffered greatly with KCPL's inability to control costs. Additionally, the Commission should be the conscious of KCPL's continued inability to control A&G costs when it debates whether a management audit is needed to protect ratepayers from KCPL's unfettered cost spending. Finally, when the Commission deliberates KCPL's request for numerous trackers and a fuel adjustment clause, the Commission should understand that such requests will serve to increase corporate earnings and inflate future rates over and above the 80% increase already imposed on ratepayers.

MECG is aware that, with KCPL's investment in capital projects, there is a limit to its ability to control KCPL's rate increase in this case. That said, MECG urges the Commission to exercise its discretion where available to demonstrate that it empathizes with the fate of KCPL's customers and has taken steps to ensure that rates are no more than is necessary.

II. RETURN ON COMMON EQUITY

In its Initial Brief (pages 21-37), MECG provided evidentiary support for its recommendation that the Commission authorize KCPL a return on equity between 8.80% - 9.40% (midpoint = 9.10%). MECG further noted that, consistent with the testimony of Mr. Gorman, this return on equity is based upon KCPL's current risk profile. To the extent that the Commission approves any extraordinary ratemaking mechanisms (fuel adjustment clause or trackers), the Commission needs to consider the change in prospective reduction in KCPL's risk by reducing the authorized return on equity to the low end of Mr. Gorman's range. Furthermore, MECG detailed for the Commission that in numerous cases over the last 10 years, the Commission has accepted Mr. Gorman's recommendations as the most reasoned and credible.

Faced with the Commission's long-term reliance on Mr. Gorman's methodology and recommendations, KCPL makes several arguments in its Initial Brief designed to convince the Commission to award it a return on equity above the 9.53% recently awarded to Ameren.[6] As this reply brief indicates, KCPL's arguments are misplaced. Given the continued decline in capital costs since the consideration of the Ameren case as well as the Commission's historical perception that KCPL is less risky than Ameren, the Commission should award KCPL a return on equity that is below the 9.53% recently awarded to Ameren.

A. KCPL's MODIFIED RECOMMENDATION

Reflecting the need to disallow significant amounts of rate case expense, KCPL appears to abandon its recommended return on equity of 10.3% and now seeks to

[6] KCPL Initial Brief, pages 1-19.

negotiate a return on equity that is simply above that recommended by all the other parties to this case.

> In the pending case, KCP&L's expert Robert Hevert recommends an ROE of 10.3%, based on a range of 10.0-10.6%. The average of the recommendations at the top of the range of the three opposing witnesses is 9.5%. When averaged with the low range of KCPL's recommendation (10%), the result is 9.75%. This is consistent with the ROE of 9.75% that was recently authorized by the West Virginia Commission for Appalachian Power Co.[7]

Recognizing KCPL's willingness to now accept a 9.75% return on equity, one must necessarily wonder why ratepayers should be expected to pay the significant consultant and outside counsel costs associated with KCPL's now abandoned attempt to justify a 10.3% return on equity.

Issues with KCPL's rate case expense set aside, there are at least two fundamental problems with adopting KCPL's tangled averaging methodology. ***First***, utilizing the KCPL averaging methodology will simply entice utilities to seek a higher return on equity in the future. For instance, faced with this averaging methodology, KCPL will undoubtedly offer a return on equity in the next case with a low end of 10.5%. When averaged with the other three recommendations, KCPL will see its averaged return now increase from 9.75% to 10.0%. Similarly faced with such an approach, customers will necessarily have to recommend a deflated return on equity simply to offset the utility's obviously inflated recommendation. KCPL's suggested approach would make a mockery of Missouri regulation.

Second, KCPL's averaging methodology is decidedly one-sided. Specifically, KCPL seeks to average its return on equity with the results of the other three analyses. This methodology provides triple weighting to KCPL's results. For instance, assume that

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[7] KCPL Initial Brief at page 2.

the same approach was taken towards MECG's recommendation of 9.10%. When averaged with the average result of the other three analyses (9.52%),[8] the Commission would then reach a return on equity of 9.31%. If the Commission were going to engage in averaging, it should provide equal weighting and simply average the results of all four recommendations to arrive at a return on equity of 9.41%.

B. ECONOMIC CONDITIONS ARE INCLUDED IN RECOMMENDATIONS

In its Initial Brief, KCPL makes several references to improving economic conditions.[9] KCPL then posits that, given this alleged improvement in the economy and rising interest rates, capital costs are increasing. Consistent with its continued abandonment of its 10.3% recommended return on equity, KCPL then implies that its authorized return must be above the "9.53% awarded to Ameren Missouri."[10] KCPL's strained logic must necessarily fail.

It is inappropriate for the Commission to make long-term predictions of economic growth based simply on short-term fluctuations in the economy. As detailed in MECG's Initial Brief, this case has seen signs of both economic regression as well as economic growth.

> While Treasury Bond (T-bond) yields did increase at the time of the June hearing (approximately 3.1%), from those that were noticed when Staff and intervenors filed their direct testimony in early April, they still represent a decline from the 3.2% bond yields in existence at the time that KCPL filed its direct testimony in October 2014. The real point is that, while there are bound to be minor fluctuations up and down over short

[8] Staff midpoint return on equity = 9.25%. KCPL midpoint return on equity = 10.3%, DOE midpoint return on equity = 9.0%. Average of these three recommendations = 9.52%

[9] KCPL Initial Brief, page 2 ("Given the clear evidence of growth in the economy, rising interest rates, and lower unemployment); *Id.* at page 14 ("Given Mr. Gorman's recognition of recent growth in the conomy, the increase in utility bond yields, and the decline in utility stock prices.") *Id.* at pages 20-21 ("reflective of improvements in the economy and higher interest rates.")

[10] *Id.* at page 20.

periods of time, there is not yet a clear upward trend in those bond yields.[11]

Contrary to KCPL's immediate pleas, it is foolhardy to ignore the short-term signs of regression in favor of KCPL's preferred signs of economic improvement.

Secondly, it is important to recognize that predictions of some economic improvement are already reflected in the recommendations in this case. As Mr. Gorman notes, the GDP outlook did project accelerated economic activity over the next five years, but projected that it would later slow over the following five years. Given that Mr. Gorman considered such GDP outlooks in his sustainable growth and multi-stage DCF calculation, he clearly reflected such predictions in the context of his overall recommendation.[12]

Third, the Company's predictions of economic improvement have not been considered with any consistency where KCPL references stagnant load growth as a problem justifying the many piecemeal cost trackers in this case. The Company should not be allowed to have it both ways, arguing that economic improvement cannot help future energy sales to grow, to help "pay for" increasing transmission, property taxes, fuel costs and cybersecurity spending, while economic improvement is cited as a basis to speculate about higher interest rates.

Recognizing the misplaced nature of KCPL's economic argument, the Commission should reject KCPL's invitation and refrain from making any *ex-post* adjustments to the recommendations. Instead the Commission should continue to recognize the credible nature of Mr. Gorman's recommendation.

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[11] MECG Initial Brief at page 33.
[12] Exhibit 550, Gorman Direct, page 18.

C. MR. HEVERT'S INFLATED GROWTH RATES

As noted in MECG's Initial Brief, the Commission has repeatedly rejected Mr. Hevert's return on equity recommendation and criticized his continued use of growth rates that are "too high". The following reference to the Commission's recent decision in the Ameren rate case is reflective of a string of similar opinions concerning Mr. Hevert's recommendations.

> Ameren Missouri's expert witness, Robert Hevert, supports an increased ROE at 10.4 percent. The Commission finds that such an ROE would be excessive. ***In large part, Hevert's ROE estimate is high because he based his multi-stage DCF analysis calculations on an optimistic nominal long-term GDP growth rate outlook of 5.71 percent. As Gorman explains, that growth rate is substantially higher than consensus economists' forward-looking real GDP growth outlooks***. Adjusting Hevert's optimistic growth rate outlook to the consensus economist level reduces his multi-stage growth DCF return from 10.02 percent to 8.80 percent for his proxy group.[13]

In its Initial Brief, KCPL simply ignores the 800 pound gorilla that is Mr. Hevert's credibility. Turning a blind eye to the Commission's previous findings of Mr. Hevert's use of inflated growth rates, KCPL simply glosses over the growth rates employed by its witness.[14]

In its Initial Brief, MECG pointed out that Mr. Hevert ignored the Commission's past criticism and continued to utilize inflated growth rates. Specifically, MECG pointed out that, in his constant-growth DCF analysis, Mr. Hevert utilized a growth rate of 6.81%

[13] Case No. ER-2014-0258, *Report and Order*, issued April 29, 2015, at page 66 (emphasis added).
[14] KCPL Initial Brief at page 7 ("Utilizing earnings growth estimates provided by Zacks, First Call, and Value Line, Mr. Hevert employed an average earnings growth rate of 5.64%."); *Id.* at page 8 ("He [Mr. Hevert] chose a long-term growth rate of 5.65%, which was based on the real grow domestic production ("GDP") growth rate of 3.27% from 1929 through 2013, and an inflation rate of 2.31%.");

that is substantially higher than consensus economists' forward-looking real GDP growth outlooks [4.4% to 4.7%] for that period.[15]

Similarly, in his multi-stage DCF analysis, Mr. Hevert employed a long-term sustainable growth rate based on a nominal GDP growth rate that is "considerably higher" than consensus analysts' projections. Specifically, while Mr. Hevert uses a long-term nominal GDP growth rate of 5.65%, consensus economists' estimates of GDP growth over the next five to 10 year period range from 4.45% to 4.65%.[16] Similar problems were pointed out associated with Mr. Hevert's CAPM analysis and risk premium analysis.[17]

Given the well documented nature of flaws in Mr. Hevert's analysis as well as his refusal to correct his analysis for the criticisms leveled by this Commission, the Commission should once again summarily reject Mr. Hevert's recommendation.[18]

D. MR. GORMAN'S ANALYSIS

Given the Commission's long-standing acceptance of Mr. Gorman's return on equity recommendations, KCPL attempts to attack his methodology and analysis. As the evidence indicates, however, Mr. Gorman's methodology and approach are consistent with those previously accepted by this Commission.

First, KCPL erroneously argues Mr. Gorman's recommendation "is well below the returns authorized by even the least supportive regulatory commissions."[19] KCPL fails to recognize that its comparison suffers from a fundamental timing difference.

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[15] MECG Initial Brief at pages 26-27 (citing to Exhibit 551, Gorman Rebuttal, pages 9-11).
[16] MECG Initial Brief at pages 27-28 (citing to Exhibit 551, Gorman Rebuttal, pages 11-13).
[17] Exhibit 551, Gorman Rebuttal, pages 17-22.
[18] Of course, as pointed out previously in this reply brief, it appears that KCPL has already abandoned Mr. Hevert's recommendation in favor of its modified averaging approach which results in a return on equity of 9.75%..
[19] KCPL Initial Brief, page 14.

Specifically, recognizing the regulatory lag of which KCPL constantly bemoans, commission return on equity decisions provided during 2014 were likely based upon financial information existing in late 2013. On the other hand, Mr. Gorman's analysis is based upon financial data from the first quarter of 2015.[20] As such, KCPL is improperly comparing Commission decisions that relied upon 2013 data with Mr. Gorman's analysis that relies upon 2015 data. Certainly, in a declining capital market, one would necessarily expect that such a delay would result in a return on equity that is below those authorized by public utility commissions.

Second, KCPL seeks to impugn Mr. Gorman's credibility by claiming that "[w]hile returns on equity and the calculations that support them require the employment of judgment and discretion, ***it is apparent that over the past six years Mr. Gorman has exercised his judgment to continuously lower his ROE recommendations***."[21] KCPL's allegations are laughable. Specifically, Mr. Gorman's "continuously lower" return on equity recommendations over the "past six years" are directly supported by the declining cost of capital reflected in the return on equity decisions of all state utility commissions.

Year	Authorized Electric Return
2009	10.48%
2010	10.24%
2011	10.07%
2012	10.01%
2013	9.79%
2014	9.76%

Source, Exhibit 550, Gorman Direct, Schedule MPG-11

Certainly given this demonstrated decline in authorized electric returns over the last six years, it is apparent that KCPL suffers from paranoid delusions when it claims that Mr. Gorman has "exercised his judgment to continuously lower his ROE recommendations."

[20] Exhibit 550, Gorman Direct, pages 15-16.
[21] KCPL Initial Brief, page 16 (emphasis added).

Simply, Mr. Gorman's judgment is supported by the continuing decline in return on equity decisions handed out by utility commissions across the country.

E. PUBLIC UTILITY COMMISSION DECISIONS

Consistent with its newly requested 9.75% ROE recommendation, KCPL offers its interpretation of recent public utility commission decisions. Specifically, relying on information outside of the record, KCPL wrongfully implies that public utility commission decisions on ROE have started to increase.[22] Like KCPL's faulty argument that interest rates have risen based upon a short-term fluctuation, KCPL wrongly implies that ROE decisions have increased based upon a small sample size (3 decisions).

Reflecting the problem with parties reaching outside the record, KCPL fails to provide the underlying data and instead interprets that data in a self-serving fashion. As the following indicates, KCPL's self-serving interpretation is patently wrong. According to SNL Financial, after including several more data points, it is apparent that return on equity decisions have continued to decline, not increase as suggested by KCPL.

Year	Decisions	Average ROE
2012	51	10.01
2013	38	9.79
2014	33	9.76
2015	**10**	**9.57**

Source: SNL Financial LC, June 30, 2015.

In fact, demonstrating the continued decline in return on equity decisions, on June 17, 2015, the New York Public Service Commission issued decisions in the pending Central Hudson Gas & Electric as well as the Consolidated Edison Co. of New York rate cases authorizing a return on equity of 9.00%. Clearly then, MECG's recommended 9.10% return on equity is justified by the continuing decline in capital costs.

[22] KCPL Initial Brief, page 20.

I. FUEL ADJUSTMENT CLAUSE

A. KCPL GENERAL ARGUMENTS

1. KCPL Willingness to Ignore Statutory Directives

At page 31, KCPL seeks to focus on one portion of Section 386.266 while ignoring all other provisions. Specifically, KCPL argues that the "purpose of the FAC. . . is to be reasonably designed to provide the utility with a sufficient opportunity to earn a fair return on equity."[23] KCPL claims that this singular provision, contained in subsection 4, "should guide the Commission on the appropriateness and design of the FAC."[24] In focusing on this singular provision, KCPL asks that the Commission ignore at least three other critical provisions contained in the statute.

For instance, in its rush to get to the return on equity provision contained in subsection 4, KCPL has completely ignored the customer protection contained in subsection 1. Specifically, KCPL claims that the sharing incentive contained in every fuel adjustment clause since 2005 is an "arbitrary disallowance." Meanwhile, KCPL conveniently ignores that subsection 1 specifically provides for such a sharing mechanism.

> The commission may, in accordance with existing law, include in such rate schedules features designed to provide the electrical corporation with ***incentives to improve the efficiency and cost-effectiveness of its fuel and purchased-power procurement activities***.[25]

The sharing mechanism is not an "arbitrary disallowance" as suggested by KCPL. Rather, as suggested by the General Assembly and repeatedly adopted by the Commission, the sharing mechanism is designed to recognize the inadequacy of prudence

[23] KCPL Initial Brief, page31.
[24] *Id.*
[25] Section 386.266.1.

reviews[26] and replace the incentives that are otherwise lost through the implementation of deferral accounting.

> The Commission also finds after-the-fact prudence reviews alone are insufficient to assure Aquila will continue to take reasonable steps to keep its fuel and purchased power costs down, and ***the easiest way to ensure a utility retains the incentive to keep fuel and purchased power costs down is to not allow a 100% pass through of those costs***.
>
> The Commission finds allowing Aquila to pass 95% of its prudently incurred fuel and purchased power costs, above those included in its base rates, through its fuel adjustment clause is appropriate. With a 95% pass-through, the Commission finds Aquila will be protected from extreme fluctuations in fuel and purchased power cost, yet ***retain a significant incentive to take all reasonable actions to keep its fuel and purchased power costs as low as possible, and still have an opportunity to earn a fair return on its investment***.[27]

Similarly, while arguing that its return on equity should not be reduced in recognition of the reduction in prospective risk resulting from the implementation of a fuel adjustment clause,[28] KCPL conveniently fails to recognize the statutory provision calling on the Commission to consider this reduction in risk.

> The commission may take into account any ***change in business risk to the corporation resulting from implementation of the adjustment mechanism*** in setting the corporation's allowed return in any rate proceeding, in addition to any other changes in business risk experienced by the corporation.[29]

Finally, while claiming that the Commission should allow for the inclusion of "all transmission costs" in the FAC,[30] KCPL asks the Commission to ignore the statutory

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[26] KCPL relies heavily on these prudence reviews. ("Of course, the only way to provide evidence that such an economic incentive either does or does not exist would be for the Commission to allow for full recovery and then analyze whether or not the FAC without an arbitrary disallowance had an effect on fuel procurement strategies or other management behavior.") (KCPL Initial Brief, page 32). Of course, such an analysis would be done through prudence reviews that the Commission has repeatedly found to be "insufficient."
[27] Case No. ER-2007-0004, *Report and Order*, issued May 17, 2007, page 54.
[28] Exhibit 129, Overcast Rebuttal, page 4. *See also*, Tr. 1351.
[29] Section 386.266.7.
[30] KCPL Initial Brief, pages 34, 50-52.

requirement that all costs included in the fuel adjustment clause be related to "fuel and purchased power costs."[31] Given this requirement, the Commission has in two recent cases found that transmission costs should be allowed in the fuel adjustment clause to the extent that they are related to off-system sales or the purchase of power from third-parties. As such, transmission costs associated with transmitting energy from KCPL's generators to its load is not related to fuel and purchased power and should not be included in the FAC.[32]

Clearly, as it regards its implementation of extraordinary mechanisms, KCPL takes a myopic view. . . focusing only on those provisions that can assist corporate profits while ignoring those provisions that are focused on customer protection. The Commission should reject KCPL's invitation to ignore these critical statutory provisions and should instead apply the statute in total.

2. KCPL Willingness to Ignore Commission Regulations

Similar to KCPL's willingness to ignore key provisions of the FAC statute, KCPL also seeks to ignore key provisions of the Commission's FAC rule. Undoubtedly in recognition of the fact that it has not met the Commission's stated criteria, KCPL argues that the Commission should still authorize it to implement a fuel adjustment clause.

> While 4 CSR 240-20.090(2)(C) provides factors that the Commission will consider, the regulation certainly does not and cannot impose determinative factors which would prohibit an FAC's authorization without a particular finding. ***Here again, the Commission should not be duped into believing it is hamstrung by a prescriptive list of determinative factors offered by opponents.***[33]

[31] Section 386.266.1.
[32] See, Case No. ER-2014-0258, *Report and Order*, issued April 29, 2015, pages 115-116; Case No. ER-2014-0351, *Report and Order*, issued June 24, 2015, pages 27-30.
[33] KCPL Initial Brief, page 33.

Notice that KCPL's fails to provide any legal citation for its argument that the Commission is not bound by list of determinative factors contained in its regulation.

4 CSR 240-20.090(2)(C) explicitly provides that the Commission "will consider" certain criteria. As such, while the Commission may consider additional criteria, the criteria contained in the rule do appear to be prescriptive. Contrary to KCPL's current suggestion, the Commission cannot simply ignore those criteria simply in the desire to grant KCPL's its fuel adjustment clause.

Additionally, KCPL argues that the application of the Commission's prescribed criteria to individual cost components is "inappropriate."[34] 4 CSR 240-20.090(2)(C) expressly provides that the individual criteria will be applied specifically to each cost component.

> ***In determining which cost components to include in a RAM***, the commission will consider, but is not limited to only considering, the magnitude of the costs, the ability of the utility to manage the costs, the volatility of the cost component and the incentive provided to the utility as a result of the inclusion or exclusion of the cost component.

Again, KCPL provides no legal authority for its suggestion that the Commission can simply ignore its regulation simply in its desire to grant KCPL its fuel adjustment clause.

Much as with KCPL's pleas to ignore certain provision of the FAC statute, the Commission should also reject KCPL's pleas to ignore certain provisions of the Commission FAC regulations.

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[34] *Id.* ("So an analysis of KCP&L's coal contracts or other fuel procurement strategies in isolation is inappropriate.").

B. DOES KCPL'S FUEL ADJUSTMENT CLAUSE REQUEST VIOLATE THE STIPULATION AND AGREEMENT FROM CASE NO. EO-2005-0329? IF SO, SHOULD IT BE REJECTED? (ISSUE II(A))

After reading 37 pages of KCPL's brief, MECG has finally identified an item on which it agrees with KCPL. . . "there is no ambiguity" in the 2005 Regulatory Plan.[35] At pages 38-42 of its Initial Brief, MECG pointed out that when the entire provision is read in total, there is no ambiguity. Specifically, when the first key sentence is read in conjunction with the second sentence, the provision becomes abundantly clear. As Staff, the only objective party to this proceeding, and a key participant in the negotiations that lead to the Regulatory Plan notes: "[T]the first sentence must mean that KCPL is not permitted to request a FAC or any other SB 179 mechanism before June 1, 2015, while the second creates an exception to that broad prohibition by allowing KCPL to request an IEC (but not a FAC) before June 1, 2015."[36]

Supporting Staff's clear understanding of this provision, MECG provided instances in which KCPL has previously expressed the identical interpretation. Specifically, when asked to swear to its interpretation of this provision, KCPL's understanding was significantly different at that time than is now portrayed in its Initial Brief. For instance, in previous sworn testimony before the Public Service Commission:

> Q: Does the Company have a Fuel Adjustment Clause ("FAC")?
>
> A: No, it does not. Per the Stipulation and Agreement ("Stipulation") approved in 2005 by the Commission in KCP&L's Experimental Regulatory Plan ("Regulatory Plan") docket, Case No. EO-2005-0329, the Company agreed that it **will not seek a FAC prior to June 1, 2015**. However, the Company is not prohibited from requesting an IEC.[37]

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[35] *Id.* at page 37.
[36] Exhibit 200, Staff Cost of Service Report, page 192 (emphasis added).
[37] *Id.* at pages 192-193 (citing to Direct Testimony of Tim M. Rush. Case No. ER-2012-0174. Page 10, lines 4-8).

Still again, in a sworn filing with the SEC, KCPL recognized that its current fuel adjustment clause request is premature. Specifically, by placing the June 1, 2015 date in the same clause as the word "seek", and separating it apart from the word "utilize," KCPL recognized that the June 1, 2015 prohibition applies to the act of seeking a fuel adjustment clause.

> ***KCPL will not seek prior to June 1, 2015***, to utilize any mechanism authorized in pending legislation or other change in state law that would allow riders, surcharges or changes in rates outside of a general rate case based upon a consideration of less than all relevant factors.[38]

Clearly, when the first sentence of the Regulatory Plan provision is read in conjunction with the second sentence, it is apparent that the Regulatory Plan prohibition precludes KCPL from seeking a fuel adjustment clause prior to June 1, 2015. More importantly, despite its current claims, KCPL's own sworn testimony and SEC filings demonstrate that KCPL held this same interpretation of this key provision.

In its Initial Brief, KCPL attempts to portray a different picture from that previously expressed in its sworn statements to the Commission and the SEC. Specifically, while recognizing that the intent of the parties needs to be determined "from the four corners of the contract,"[39] KCPL seeks to ignore the four corners of the document and, instead, focus entirely on three words from the provision.

> There is no ambiguity in the language "seek to utilize" in the CEP Stipulation. A reasonable and average person with a modicum of knowledge about Missouri utility law would understand this language within the context of a rate case. Within the context of a rate case the Company is prohibited from having an FAC tariff go into effect prior to June 1, 2015.[40]

[38] Exhibit 507.
[39] KCPL Initial Brief, page 37 (citing to *Eisenberg v. Redd*, 38 S.W.3d 409, 411 (Mo. banc 2001).
[40] KCPL Initial Brief, page 37.

Repeatedly throughout its brief, KCPL focuses on these three words ("seek to utilize") separate and apart from the remainder of this provision or other words within the four corners of the document.[41] **<u>Not once does KCPL attempt to interpret these three words in the context of the entire Regulatory Plan provision</u>**. As Staff notes, read in context, the phrase is abundantly clear.

> To provide meaning to the applicability of the June 1, 2015, date, both the first and the second sentences of the Regulatory Plan quoted above should be read together. It is significant that the date in both sentences – June 1, 2015 – is the same. The second sentence qualifies the first sentence by allowing KCPL to do something it could not under the first sentence. If the first sentence means that KCPL could request [seek] a SB 179 mechanism in a rate case filed before June 1, 2015, as long as that mechanism did not become effective until after June 1, 2015, then the date in the second sentence would be meaningless. ***<u>Therefore, the first sentence must mean that KCPL is not permitted to request a FAC or any other SB 179 mechanism before June 1, 2015, while the second creates an exception to that broad prohibition by allowing KCPL to request an IEC (but not a FAC) before June 1, 2015.</u>***[42]

Next, KCPL argues that "seek to utilize" cannot mean "to file" because that term ("to file") has a clear meaning. As such, "seek to utilize" must mean something entirely different. In this regard, knowing then what we know now, MECG agrees that the provision would have been clearer if the phrase "to file" at been used instead. That said, as KCPL fails to recognize, since SB179 had not yet been passed, no one knew that the initiation of a fuel adjustment clause request would involve an act of filing. As Lena Mantle, a key participant in the negotiation of this Regulatory Plan provision points out:

> I believe now that we know the process of an FAC, we know what the legislation is, to utilize is not as important as the seek. As I explained yesterday, not knowing -- every state has different legislation and different ways that an FAC can -- can happen for a utility. Now that we have 20/20 hindsight, you know, we can -- we read it with our 20/20 hindsight. At that time, we did not know whether the Commission was going to be allowed

[41] *Id.* at pages 38-39.
[42] Exhibit 200, Staff Cost of Service Report, page 192 (emphasis added).

> to grant it, if it was going to be just automatically given, how things were going to happen. So I would -- you know, when I wrote this, of course it is OPC's position and my position that it was to seek and that's why I wrote that that way.[43]

The Commission should not condone KCPL's hyper-critical wordsmithing in its attempt to renege on its previous commitment. Specifically, the Commission should reject KCPL's invitation to focus on three simple words to the exclusion of the remainder of the provision. Read in context, the Commission will reach the same conclusion that Staff, OPC, MECG, MIEC and, prior to this case, even KCPL have reached. Specifically, using KCPL's own words, "[p]er the Stipulation and Agreement ("Stipulation") approved in 2005 by the Commission in KCP&L's Experimental Regulatory Plan ("Regulatory Plan") docket, Case No. EO-2005-0329, the Company agreed that it **will not seek a FAC prior to June 1, 2015**."[44]

C. HAS KCPL MET THE CRITERIA FOR THE COMMISSION TO AUTHORIZE IT TO HAVE A FUEL ADJUSTMENT CLAUSE? (ISSUE II(B))

In less than three pages, KCPL attempts to argue that its request for a fuel adjustment clause, and its request for the cost components in that FAC, meets the Commission's prescribed criteria.[45] As mentioned previous (pages 15-19), KCPL's alleges that it meets this criteria by ignoring several key components of the Commission's rule and previous Commission decisions. For instance, contrary to the express direction contained in 4 CSR 240-20.090(2)(C), KCPL fails to apply the Commission's criteria to each specific cost component to be included in the FAC.[46]

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[43] Tr. 1742-1743.

[44] *Id.* at pages 192-193 (citing to Direct Testimony of Tim M. Rush. Case No. ER-2012-0174. Page 10, lines 4-8).

[45] KCPL Initial Brief, pages 43-46.

[46] It is amazing that, when interpreting the Regulatory Plan provision, KCPL argues that the "plain and ordinary" meaning of the words "seek to utilize." (KCPL Initial Brief, page 38). Here, when faced with a Commission regulation containing unquestioned clarity, KCPL fails to follow its clear direction. Again,

> ***<u>In determining which cost components to include in a RAM</u>***, the commission will consider, but is not limited to only considering, the magnitude of the costs, the ability of the utility to manage the costs, the volatility of the cost component and the incentive provided to the utility as a result of the inclusion or exclusion of the cost component.

Similarly, KCPL claims its requested fuel adjustment clause meets the Commission's volatility standard by refusing to apply previous Commission orders. Specifically, claiming that the term "volatility" is "not defined in the Commission's regulations," KCPL urges the Commission to simply apply a dictionary definition.

Contrary to KCPL's argument, however, the Commission has previously defined the term "volatility." Rejecting KCPL's current hyperbole, the Commission has never defined volatility as "extreme or violent changes."[47] Rather, the Commission has simply stated that volatility does not simply include costs that are expected to increase. Rather, "volatile prices tend to go up and down in an unpredictable manner."[48]

> ***<u>Thus AmerenUE's fuel costs, while certainly rising, cannot be said to be volatile.</u>***
>
> ***<u>Markets in which prices are volatile tend to go up and down in an unpredictable manner</u>***. When a utility's fuel and purchased power costs are swinging in that way, the time consuming ratemaking process cannot possibly keep up with the swings. As a result, in those circumstances, a fuel adjustment clause may be needed to protect both the utility and its ratepayers from inappropriately low or high rates. Because AmerenUE's costs are simply rising, that sort of protection is not needed.[49]

Recently, the Commission expanded on this definition of volatility.

> The projected five year SPP related transmission expansion costs are expected to increase, but do not demonstrate volatility. Empire's Missouri

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KCPL's willingness to insist on certain provisions contained in statutes, rules, and orders, while simultaneously ignoring other provisions, seemingly knows no limits.

[47] KCPL Initial Brief, page 45.

[48] Exhibit 503, Brosch Direct (Rate Design), page 7.

[49] Case No. ER-2007-0002, *Report and Order*, issued May 22, 2007, pages 17-19.

> jurisdictional RTO transmission costs are reasonably projected and thus not volatile.[50]

Thus, according to these two Commission orders, volatility is characterized by prices going up and down in and unpredictable manner, not simply rising costs. In a similar manner, since they go up and down in an "unpredictable manner," volatile costs are not "reasonably projected."

Given its inability, or refusal, to apply the necessary criteria, including the appropriate definitions, to the individual cost components which it seeks to include in the fuel adjustment clause, KCPL is able to gloss over the Commission's directives and reach its ultimate conclusion that "KCP&L has met the Commission's criteria."[51]

Contrary to KCPL's current assertion, other parties that sought to properly apply the Commission's criteria have each concluded that KCPL has failed to meet the Commission's criteria. For instance, claiming that KCPL has failed to show that its fuel and purchased power costs are not volatile and not reasonably managed by management,[52] "Staff recommends the Commission ***not*** grant KCPL's request for the implementation of a FAC as it has not met all of the three criteria for determining whether an electric utility should be allowed to implement a FAC."[53]

Similarly, OPC concludes that KCPL has failed to meet the Commission's criteria.

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[50] Case No. ER-2014-0351, *Report and Order*, issued June 24, 2015, page 25.

[51] KCPL Initial Brief, page 43.

[52] Contrary to the clear direction of 4 CSR 240-20.090(2)(C), the Staff failed to apply the individual Commission criteria to the individual cost components to be contained in the fuel adjustment clause. As Staff concludes, however, even when viewed in the aggregate, KCPL's fuel and purchased power costs do not meet the Commission's criteria.

[53] Exhibit 200, Staff Revenue Requirement Cost of Service Report, page 194.

Q. DOES KPCL'S FILING AND PROPOSED FAC MEET THE CRITERIA TO BE GRANTED AN FAC?

A. No, it does not. For this reason, if the Commission finds that KPCL has not violated the Regulatory Plan agreement, OPC recommends that the Commission deny KCPL's request for an FAC.[54]

Most importantly, recognizing that he developed the criteria adopted by the Commission and contained within its FAC rules, MECG witness Brosch concludes that KCPL has failed to meet the Commission's criteria. "I recommend, for all the reasons stated herein and in my previously filed revenue requirement testimony, that the Company does not need and should not be granted a fuel adjustment clause."[55]

Despite its failure to apply appropriate criteria and definitions to the individual cost components to be included in the fuel adjustment clause, KCPL makes some conclusory, and erroneous, statements in its Initial Brief that should be rebutted.

►Beyond the Control of Management: In one paragraph, and without any analysis, KCPL makes the conclusory claim that coal costs are beyond the control of its management.[56] The analysis presented by Mr. Brosch, however, finds that KCPL has exerted tremendous control over its exposure to both coal and freight costs.

First, KCPL controls its exposure to coal prices changes through the use of coal price hedging program relying on a "strategy of laddering into a portfolio of forward contracts with staggered terms so that a portion of the portfolio will roll over each year."[57] In this way, KCPL signs multi-year coal contracts such that coal requirements in the near term are largely covered and KCPL has limited exposure to market price changes. For instance, KCPL may sign a coal contract in 2012 which may cover 30% of

[54] Exhibit 309, Mantle Direct, page 18.
[55] Exhibit 503, Brosch Direct (Rate Design), page 54.
[56] KCPL Initial Brief, pages 44-45.
[57] Exhibit 103, Blunk Direct, pages 24-25.

KCPL's coal needs for 2013-2015. In addition, KCPL may sign another coal contract in 2013 which meets 30% of KCPL's coal needs for 2014-2016. Finally, KCPL may sign a third coal contract which meets 30% of KCPL's coal needs for 2015-2017. The practical effect is that these laddered contracts provide relatively fixed costs for 90% of KCPL's coal needs in 2015. Thus, KCPL has invested significant time and resources in order to limit the Company's exposure to any fluctuations in the market price of coal.

Second, KCPL management controls its exposure to the delivered price of coal through the use of long-term rail freight contracts. As Mr. Brosch explains, "More than **___** of the per ton delivered cost of PRB coal is rail freight. . . . KCPL's primary rail freight contracts with **____________________** are for terms of **_______________ ______**" and at per-ton prices that are largely fixed.[58]

The practical effect of KCPL's use of laddered coal contracts and long-term freight contracts is that KCPL experiences stable prices for the delivered cost of coal. Specifically, KCPL's cost for coal in 2014 was **______** per ton, and is projected to decline to **______** in 2015 and **______** in 2016.[59]

►Volatility: At paragraph 125 of its Initial Brief, KCPL attempts to provide an appearance of volatility by resorting to coal market spot prices. KCPL ignores, however, that it has virtually no exposure to these spot prices. Rather, given its use of laddered, long-term, coal contracts, KCPL buys very little coal on the spot market. Specifically, recognizing that KCPL had approximately 95% of its 2015 coal requirements under contract at year-end 2014,[60] KCPL has little exposure to changes in the market price of coal. In fact, KCPL reported to its investors that "a hypothetical 10% increase in the

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[58] Exhibit 503, Brosch Direct (Rate Design), page 21.
[59] *Id.* at pages 21-22.
[60] *Id.* at page 17 (citing to Great Plains Energy SEC Form 10K, at page 46.).

market price of coal would result in an approximately $2.1 million increase in fuel expense for 2015."[61] Given its total operating cost portfolio, "a $2.1 million increase in fuel expense represents only about 0.15 percent of overall expenses."[62] Clearly, KCPL's reliance on spot market coal prices as a proxy for its coal cost volatility is misplaced.

The best evidence of KCPL's exposure to coal cost volatility is its historical cost of coal. In this regard, coal and freight costs have been very stable.

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Source: Exhibit 504, Brosch Surrebuttal, page 52. **

Given this thorough analysis, and contrary to KCPL's conclusory findings, coal and freight costs should not be included in a fuel adjustment clause.

D. IF THE COMMISSION AUTHORIZES KCPL TO HAVE A FUEL ADJUSTMENT CLAUSE, HOW SHOULD IT BE STRUCTURED?

Demonstrating the inherent complexity and foretelling the obvious future litigation over KCPL's proposed fuel adjustment clause, KCPL spends 46 paragraphs

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[61] *Id.*
[62] *Id.* at page 18.

addressing individual issues regarding the structure of a fuel adjustment clause.[63] Reflecting KCPL's desire to expand the FAC and include as many costs as possible, KCPL uses these paragraphs in an attempt to convince the Commission that: (1) it should ignore the express directive contained in Section 386.266.1 and forego the inclusion of a sharing mechanism in the context of any fuel adjustment clause[64] as well as allow the inclusion of all transmission costs;[65] (2) it should not provide additional definition regarding the identity of the costs to be included in the FAC;[66] and (3) KCPL should be allowed to unilaterally include additional items in the FAC in the future;[67] As with the Initial Brief, MECG will use this Reply Brief to address certain structural issues.

1. Percentage Flow Through

Amazingly, after not having a fuel adjustment clause for 36 years, and reflecting its greedy posture towards virtually every issue in this case,[68] KCPL now gripes that the implementation of a 95/5 sharing is tantamount to a "disallowance." Furthermore, given that other "regional utilities" have an FAC that allegedly include 100% of costs, KCPL argues that it will be at a competitive disadvantage when it attempts to raise capital.[69] KCPL's arguments are misplaced.

As indicated, Section 386.266.1 expressly allows the Commission to provide a sharing of FAC costs in an effort to replace the incentives that are lost through the implementation of a fuel adjustment clause. Recognizing that it has repeatedly found that

[63] KCPL Initial Brief, pages 47 (paragraph 132) through 60 (paragraph 178).
[64] *Id* at pages 47-48.
[65] *Id.* at pages 50-53.
[66] *Id.* at pages 48-49.
[67] *Id.* at page 55-56.
[68] KCPL asks for an inflated return on equity. KCPL asks for the inclusion of costs to be incurred months after the true-up date. KCPL asks for the unilateral ability to include costs in the fuel adjustment clause. KCPL asks for the inclusion of excessive rate case expense associated with unnecessary consultants and outside counsel. KCPL asks for the implementation of trackers never seen for other Missouri utilities.
[69] KCPL Initial Brief, pages 47-48.

prudence reviews are insufficient, the Commission has provided for a 95/5 sharing of costs in the fuel adjustment clauses for Ameren, Empire and KCPL-GMO. While each of these utilities made the same arguments as KCPL, none of them felt strongly enough that it would challenge the Commission's decision to implement such a sharing provision.

Furthermore, while KCPL argues that it would be at a competitive disadvantage in raising capital, it is apparent that, the inclusion of 100% of fuel costs in the FAC would place KCPL at a competitive advantage relative to the other Missouri utilities. KCPL's arguments ring hollow and should be rejected. KCPL provides no evidence of any historical difficulty raising capital with a zero-percent FAC, so approval of a 50 percent or 95 percent sharing FAC can only fairly be viewed as narrowing any specious claim of competition in accessing capital markets. In fact, without a FAC, KCPL has raised capital for all its construction projects going back to the installation of its wind farm at Spearville in 2006, the completion of Iatan 1 environmental upgrade, the in-service of Iatan 2, right up through the completion of the La Cygne environmental project in this case. KCPL has not complained about any difficulty in raising capital costs.

2. Inclusion of Transmission Costs

At pages 50-53, KCPL essentially argues that, given their alleged materiality, volatility and lack of management control, the Commission should expand the scope of the FAC statute and disregard recent Commission orders to allow for the inclusion of all transmission costs. KCPL fails to understand that the Commission is a creature of statute. Simply, the Commission acts in conformance with the authority provided by the General Assembly. To the extent that KCPL is unhappy with the limited inclusion of

transmission costs in the fuel adjustment clause, their recourse is to seek modification in the General Assembly.

In past cases, the Commission has rightfully held that transmission costs associated with transmitting electricity from utility generators to utility load are not related to "fuel and purchased power." As such, given the express dictates in Section 386.266.1, such costs are not properly included in a fuel adjustment clause. As with the 95/5 sharing mechanism, KCPL now asks that the Commission reject its findings with respect to Ameren and Empire and allow it a more expansive version of a fuel adjustment clause. KCPL's cries about the limitations of the fuel adjustment clause statute are misplaced and should be directed across the street at the Capitol.

3. Line Loss Voltage Levels

In its Initial Brief (pages 62-64), MECG pointed out that line losses increase every time electric voltage is transformed. Given the increased line losses, the energy charges in KCPL's Large Power rate schedule recognize four different voltage levels: (1) Transmission; (2) Substation; (3) Primary and (4) Secondary. Given that line losses are a fact and understanding that KCPL already calculates line losses for four different voltage levels, MECG argues that this data should be utilized in the context of KCPL's fuel adjustment clause.

In its Initial Brief, KCPL provides **one** sentence in support of its argument that it should only recognize two voltage levels. Simply, KCPL argues that "the two voltage levels identified in KCP&L's proposed FAC are sufficient."[70] Noticeably, KCPL does not dispute that line losses vary with different voltage levels. Nor does KCPL argue that it already tracks this line loss data for four voltage levels. Finally, KCPL does not argue

[70] KCPL Initial Brief, page 58.

that it utilizes these four voltage levels in the context of its Large Power rate schedule. Simply, in what can only be argued as blatant laziness, KCPL asserts that two voltage levels are "sufficient."

MECG urges the Commission to recognize the data that already exists. The use of proper line losses by voltage level is proper ratemaking and prevents the creation of subsidies within the Large Power rate schedule. Clearly, contrary to KCPL's lazy assertions, two voltage levels are not sufficient and should be rejected.

4. Distinction Between KCPL & GMO Customer Bills

At pages 64-66 of its Initial Brief, MECG argued that there is significant customer confusion as a result of KCPL-GMO's marketing itself as KCPL. Specifically, KCPL-GMO markets itself as KCPL. For all customer contact purposes, KCPL-GMO markets itself as KCPL. Recognizing that their electric bills contain no mention of GMO, these customers understandably believe that they are served by KCPL at KCPL rate levels. Contrary to the express purpose of the tariff publication requirement in Section 393.140(11), GMO customers, not realizing that GMO even exists, are incapable of locating their rates or the underlying tariffs. Certainly, to the extent that GMO misbills these customers, the GMO customers will be incapable of identifying such problems. Recognizing that the fuel adjustment clause line item is now virtually the only point of distinction between these two utilities, this distinction will be eliminated if KCPL is granted a fuel adjustment clause. As such, MECG urges the Commission to require KCPL to distinguish itself from GMO on GMO bills.

In its Initial Brief, KCPL argues that the Commission has already decided this issue. Specifically, based upon Staff's failure to provide evidence of customer confusion

in 2009, the Commission refused to hear Staff's complaint. KCPL fails to see that customer confusion is a fact and was prominently presented in this case. Specifically, Commissioner Kenney, a GMO customer and knowledgeable of the difference between KCPL and GMO, could not even assess whether he was a KCPL or a GMO customer.

> COMMISSIONER KENNEY: I will tell you I've been a GMO customer, Aquila customer, and ***I had to ask my staff to look up and see whether I was KCP&L or GMO.***
>
> * * * * *
>
> Well, the reason I checked into it is because when we had the public hearings, there were no public hearings in my -- you know, the cities of Lee's Summit and Blue Springs.
>
> MR. WOODSMALL: Confusing, yes.[71]

Certainly, if a Commissioner, knowledgeable about the difference between KCPL and GMO, is incapable of determining whether he is a KCPL or GMO customer, then it is unquestionable that the remaining GMO customers may also be incapable of accurately determining their electric provider.

In his testimony, KCPL's Chief Operating Officer expressly stated that, if KCPL's actions to market GMO as KCPL are causing customer confusion, then he is committed to correcting such confusing practices.

> **Mr. Woodsmall**: If I told you hypothetically that there is customer confusion, that GMO customers do not believe -- do not understand that their service provider is GMO, do you think that's something that you should clarify and correct?
> **Mr. Heidtbrink**: I would think that if it is causing a problem for customers, ***yes, we need to correct it***.[72]

Certainly, recognizing the admitted confusion of a public service commissioner, customer confusion for GMO customers is not a hypothetical, it is a fact. Recognizing,

[71] Tr. 1587.
[72] Tr. 1310.

the Commission's customer protection mandates and KCPL's commitment to correct customer confusion, the Commission should order KCPL to distinguish its bills from GMO.

Finally, it should be pointed out that a requirement that GMO bills be distinguished from KCPL bills should not cause additional cost. Specifically, at the time that it purchased Aquila, KCPL also acquired all of the underlying billing systems. Recognizing that those systems were capable of properly distinguishing those customer bills, and in light of the fact that KCPL acquired those billing systems, it should be able to meet such a requirement with a minimum of expense and effort.

III. PROPOSED TRACKERS

A. LACK OF STATUTORY AUTHORITY[73]

During the evidentiary hearing in this case, MECG repeatedly pointed out that, absent "extraordinary" costs, the Commission lacked statutory authority to implement KCPL's proposed trackers. In its Initial Brief, MECG noted that, in a review proceeding, the appellate court will seek specific statutory authority in order to determine if the Commission's decision is lawful.

> Since it is purely a creature of statute, ***the Public Service Commission's powers are limited to those conferred by the above statutes, either expressly, or by clear implication as necessary to carry out the powers specifically granted***. Thus, while these statutes are remedial in nature, and should be liberally construed in order to effectuate the purpose for which they were enacted, "neither convenience, expediency or necessity are proper matters for consideration in the determination of" whether or not an act of the commission is authorized by the statute.[74]

In its Initial Brief, KCPL attempts to rebut MECG's claims. Relying on the general powers conferred under Sections 393.140(4) and 393.140(8), KCPL argues that the Commission "has statutory authority to grant each of the trackers proposed by KCP&L."[75] Noticeably, however, KCPL fails to provide any case law extending this general power to the specific relief now requested by KCPL.

KCPL failure to provide any specific authority, statutory or otherwise, is not surprising given the fact that such authority does not exist. Specifically, while KCPL references Sections 393.140(4) and 393.140(8) as statutory authority, the limited case law interpreting these provisions indicate either: (1) that the general authority conveyed in

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[73] KCPL Initial Brief, pages 24-27.
[74] *Id.* at page 49 (citations omitted, emphasis added).
[75] KCPL Initial Brief, at page 24.

these statutes do not provide for any specific statutory powers[76] or (2) that this statutory authority provides the power to defer costs, but only for an "extraordinary" event.[77]

In 1979, the Missouri Supreme Court considered the Commission's utilization of deferral accounting through the implementation of a fuel adjustment clause. In fulfilling its review of the Commission's decision, the Court sought to determine if the Commission had specific statutory authority for approving the deferral accounting represented by the fuel adjustment clause. In response to the Court's inquiry, the Commission, like KCPL today, pointed to Section 393.140 as authority for the fuel adjustment clause. Dealing a crushing blow to the Commission's argument then, and to KCPL's current argument, the Supreme Court found that Section 393.140 only provides general authority and does not provide any specific authority.

> Respondents, however, state that the statutes as a whole do support their power to utilize a fuel adjustment clause. *Section 393.130* generally sets out basic rules governing the giving of safe and adequate service by the utility, and prevents preferential rates being given one customer. ***Section 393.140 sets out the general powers of the commission***. While this statute gives the PSC general supervisory power over electric utilities, as discussed *supra*, it gives the PSC broad discretion only *within* the circumference of the powers conferred on it by the legislature; ***the provision cannot in itself give the PSC authority to change the rate making scheme set up by the legislature***.[78]

Thus, the Missouri Supreme Court has found that, contrary to KCPL's current claims, Section 393.140 fails to provide any specific statutory authority.[79]

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[76] *State ex rel. Utility Consumers Council of Missouri v. Public Service Commission*, 585 S.W.2d 41 (Mo. banc 1979) ("*UCCM*")

[77] *State ex rel. Office of the Public Counsel v. Public Service Commission*, 858 S.W.2d 806 (Mo.App. 1993) ("*Sibley*").

[78] *UCCM* at pages 55-56.

[79] Interestingly, KCPL recognizes that "[b]ut for this law being passed in 2005 [Section 386.266], a FAC would be unlawful." (KCPL Initial Brief, page 30). It is interesting that KCPL recognizes that, because of the lack of specific statutory authority, an FAC would be otherwise unlawful in Missouri. For the same reason, MECG asserts that, because KCPL cannot provide specific statutory authority for its recommended trackers, those trackers must also be unlawful. Just as Section 393.140 could not provide the statutory

In 1993, the Missouri Court of Appeals considered the Commission's decision to allow for the limited use of deferral accounting for "extraordinary" events. There the Commission held that the deferral of depreciation and carrying cost did not constitute retroactive ratemaking, as defined by UCCM court, because the costs were associated with an extraordinary event and were outside the current "match of revenues and expenses." As such, the Commission opined that deferral accounting for this "extraordinary" event was appropriate.

> The Commission does not consider the granting of the deferrals of extraordinary items either single-issue or retroactive ratemaking as argued by Public Counsel. Retroactive ratemaking occurs when rates are set to recover for past deficiencies or to refund past excesses. . . ***The deferrals approved in Case No. EO-91-358 do not constitute retroactive ratemaking since they involve items which have been found to be extraordinary and therefore outside the current period match of revenues and expenses***.[80]

On appeal, the Court of Appeals, interpreting both Sections 393.140(4) and 393.140(8), agreed that deferral accounting was appropriate, but only for an "extraordinary event."

> The Commission's decision to grant authority to defer the costs associated with the Sibley reconstruction and coal conversion projects by recording the costs in Account No. 186 was the result of the Commission's determination that the construction projects were unusual and nonrecurring, and therefore, extraordinary. . . . Because rates are set to recover continuing operating expenses plus a reasonable return on investment, only ***an extraordinary event*** should be permitted to adjust the balance to permit costs to be deferred for consideration in a later period.[81]

As such, contrary to KCPL's claims that the Commission has broad authority to implement its requested trackers, such authority is either: (1) non-existent (Supreme

authority for deferral accounting for a fuel adjustment clause in 1979, that same statute cannot be the basis for deferral accounting for KCPL's trackers in 2015.

[80] Case No. EO-91-358, *Report and Order*, issued December 20, 1991, 1 Mo.PSC 3d 200, 212-213.

[81] *Sibley* at page 811.

Court's *UCCM* decision) or (2) exists only for an "extraordinary event" (Missouri Court of Appeals' *Sibley* decision).

Despite the pivotal nature of the *Sibley* decision, KCPL only pays fleeting attention to its holding. In an effort to avoid the *Sibley* holding, KCPL wrongfully claims that the *Sibley* court "did not explicitly limit deferral accounting to only extraordinary items." At best, KCPL's statement represents its incomplete understanding of the law. At worst, it represents an attempt to mislead this tribunal. There, the Court of Appeals held, in direct contradiction of KCPL's current claim, that deferral accounting is limited solely to an extraordinary item.

> Because rates are set to recover continuing operating expenses plus a reasonable return on investment, ***only an extraordinary event*** should be permitted to adjust the balance to permit costs to be deferred for consideration in a later period.[82]

Clearly then, there is no legal support for KCPL's claim that the *Sibley* court "did not explicitly limit deferral accounting to only extraordinary items. Rather, the *Sibley* Court did provide such a limitation.

Next, KCPL argues that the *Sibley* decision is distinguishable from the immediate proceeding because the *Sibley* decision was limited to an AAO. In contrast, KCPL is requesting a tracker mechanism.[83] As indicated in MECG's Initial Brief, KCPL's attempt to distinguish its unlawful request for trackers from the limited authority provided by the *Sibley* court is regulatory semantics.

> The mechanism that creates the deferral accounting (adjustment mechanism, tracker mechanism or accounting authority order) is simply a matter of regulatory semantics. This lack of distinction between the various adjustment mechanisms is best seen by the fact that, in Case No. EU-2014-0077, KCPL asked the Commission for authority to implement

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[82] *Sibley* at page 811.
[83] KCPL Initial Brief, page 25.

> either a transmission tracker or an accounting authority order. ("The Companies therefore respectfully request that the Commission give them the authorization to defer these transmission expenses until the next rate case ***through an AAO or a transmission tracker***."). As Mr. Dauphinais points out, "they [trackers and AAOs] essentially do the same thing" Putting semantics aside, each of these regulatory tools suffers from the same infirmities as discussed herein.[84]

Still again, finally appearing to recognizing the dispositive nature of the *Sibley* decision, KCPL makes a weak attempt at fulfilling its "extraordinary" standard. KCPL claims that "[t]he regulatory mechanisms proposed by KCP&L are designed to preserve the result of Commission decisions in ***extraordinary*** times."[85] Noticeably, KCPL fails to provide any true definition for what causes this to be an "extraordinary" time. KCPL appears to imply that this is an extraordinary time simply because in recent years it has "filed frequent and successive rate case."[86]

Certainly, the fact that KCPL has filed several rate cases in succession cannot be indicative of "extraordinary" times now or in the future. In the past 9 ½ years, KCPL has filed 6 rate cases.[87] Interestingly, in less than 8 years between April 1978 and April 1986, KCPL filed and completed six rates cases.[88] Similarly, Ameren, Empire and Missouri Public Service all experienced similar stretches of successive rate cases. In each situation, those cases were completed and the financial health of the utilities secured without the tracker mechanisms that KCPL now seeks. Both time frames of rate cases had substantial construction activity—in the earlier period all the utilities were building additional generating facilities such as Iatan 1 and Wolf Creek for KCPL and again in the

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[84] MECG Initial Brief, page 67, footnote 178 (citing to Exhibit 504, Brosch Surrebuttal, page 23 and Tr. 1751-1752.

[85] KCPL Initial Brief, page 26.

[86] *Id* at pages 26-27.

[87] See, Case Nos. ER-2006-0314, ER-2007-0291, ER-2009-0089, ER-2010-0355, ER-2012-0174 and ER-2014-0370.

[88] See, Case Nos. ER-78-252, ER-80-48, ER-81-42, ER-82-66, ER-83-49 and ER-85-128.

last ten years, base load generation was built by KCPL, GMO and Empire (Iatan 2) and all the utilities completed significant capital additions for environmental compliance. Certainly, given that such stretches of rates cases are ordinary, KCPL cannot point to them as basis for its claim that these are "extraordinary" times. Additionally, the accounting deferrals KCPL now seeks would function prospectively and the Company has made no showing that extraordinary conditions will exist in future years.

Finally, KCPL attempts to divert the Commission's attention away from the limitations in the *Sibley* decision and instead claims that, since the Courts have approved the use of the purchased gas adjustment ("PGA") for gas utilities, their requested tracker mechanisms must also be lawful.[89] In support of this claim, KCPL references *State ex rel. Midwest Gas Users' Ass'n v. PSC*.[90] Noticeably, KCPL fails to fully inform the Commission that, given more recent pronouncements from the Supreme Court, the deferral accounting in the PGA clause is also on shaky legal ground. Specifically, in a 2013 decision, the Supreme Court questioned the lawfulness of the PGA because it was implemented without any "specific statutory directive." As with MECG's argument here, the Supreme Court explicitly pointed to the *UCCM* decision as support for the requirement that Commission action must be pursuant to specific statutory authority.

> The PSC adopted the PGA/ACA rate mechanism pursuant to its broad power to regulate gas utilities, rather than pursuant to a specific statutory directive. This Court has not addressed the authority of the PSC to utilize the PGA/ACA mechanism as part of its regulation of gas utilities, although one court of appeals decision has done so. *See State ex rel. Midwest Gas Users' Ass'n v. Pub. Serv. Comm'n or State, 976 S.W.2d 470 (Mo. App. 1998)* (discussing implied authorization for use of PGA/ACA mechanism when certain procedural protections are in place). Here, as neither party challenges the use of the PGA/ACA mechanism, this Court still does not reach that issue. *Cf. State ex rel. Util. Consumers' Council of*

[89] KCPL Initial Brief, pages 24-25.
[90] 976 S.W.2d 470 (Mo.App. 1998).

> *Missouri, Inc. v. Pub. Serv. Comm'n, 585 S.W.2d 41, 46 (Mo. banc 1979)* (disapproving *electric* utility's use of a fuel adjustment clause, which is similar to a PGA mechanism, because automatic adjustment clauses were unlawful under statutory scheme then in place).[91]

Clearly then, KCPL's claim that, the existence of the PGA clause implies legal authority for its newly proposed trackers, is very shaky.

Based upon the clear directives of the *UCCM* and *Sibley* decisions, and given KCPL's failure to provide any other legal support for its requested trackers, the Commission should reject KCPL's trackers on the basis that they do not meet the "extraordinary" standard. Indeed, less than 12 months ago, the Commission held that transmission costs, since they are an ordinary expense, do not meet the Court's "extraordinary" standard.

> In Missouri, rates are normally established based off of a historic test year. The courts have stated than an AAO allows the deferral of a final decision on current *extraordinary* costs until a rate case and therefore is not retroactive ratemaking. Consistent with the language in General Instruction No. 7, the Commission has evaluated the transmission costs for which Companies seek an AAO to determine if they are an unusual and infrequent occurrence. The Commission concludes they are not.
>
> Companies began incurring transmission expenses when they began providing retail electric service. Transmission costs are part of the ordinary and normal costs of providing electric service and are expected to continue in the foreseeable future. Furthermore, while the transmission costs at issue may have a significant effect on Companies, they are not "abnormal and significantly different from the ordinary and typical activities" of the Companies. The increase in transmission costs was anticipated and is indeed the norm for all electric utility members of SPP. ***Therefore, the transmission costs are not extraordinary***.[92]

The Commission should make a similar determination regarding KCPL's proposed trackers in this case.

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[91] *State ex rel. Office of the Public Counsel v. Public Service Commission*, 409 S.W.3d 371 (Mo. 2013).
[92] Case No. EU-2014-0077, *Report and Order*, issued July 30, 2014, at page 10.

B. KCPL'S GENERAL CLAIMS[93]

1. Failure to Apply Extraordinary Standard to Proposed Trackers

At pages 27-30 of its Initial Brief, KCPL makes several generic claims, usually without any citation to the record, regarding its proposed tracker mechanisms. As primary matter, it is important to recognize that, at no time, does KCPL attempt to apply the "extraordinary" standard as set forth by the *Sibley* court. This obviously reflects the fact that KCPL, like the Commission in its Report and Order in Case No. EU-2014-0077, cannot find that such costs are "extraordinary." Given its inability to make such a claim, KCPL instead seeks to simply ignore the "extraordinary" criteria in favor of its more preferred criteria - a criteria specifically designed to support KCPL's desired goal of convincing the Commission to authorize a variety of trackers.

2. Outside of KCPL Control

On page 27 of its Initial Brief, KCPL mistakenly claims, without citation to the record, that "[t]here is no serious dispute that these costs are largely outside the control of the Company." Again, KCPL is flat wrong. In his Direct Testimony, Mr. Brosch points out repeatedly that each of the costs are, to a large degree, within the control of KCPL's management. For instance, Mr. Brosch explained that there are a number of actions that KCPL's management can take to control property taxes.[94] Given the virtually guaranteed recovery of costs provided under a tracker mechanism, Mr. Brosch questions whether KCPL's management would take such steps in the future. "One would question whether KCPL would be willing to take such steps it if was guaranteed recovery of all property

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[93] KCPL Initial Brief, pages 27-30.

[94] Exhibit 502, Brosch Direct (Revenue Requirement), page 21.

tax increases."[95] Similarly, Mr. Brosch points out that, since cyber-security costs are largely labor related, they are largely within the control of KCPL's management. "[U]tility management has responsibility and control over decisions regarding the hiring, testing, training, new capital investments and security modifications to facilities and automated systems that are made in order to achieve and maintain compliance."[96] In fact, while KCPL subsequently withdrew its request for a vegetation management tracker, KCPL's management also exerted significant control over those costs as well. "Utility management has considerable control and discretion over vegetation management spending and can favorably impact such costs through efficient scheduling of work and the development of enhanced vegetation management programs."[97]

3. KCPL Claims that It Will Lose Money on these Costs

Next, through its failure to recognize the proper ratemaking paradigm, KCPL wrongly claims that it is "a given that the Company will lose money on these costs starting day one without a tracker."[98] Contrary to KCPL's implicit claim that individual costs should be isolated and considered in a vacuum when they are included in rates, Missouri courts have found that it is the overall "relationship of investment, revenues and expenses" that is to be considered.

> The accepted way in which to establish future rates is to select a test year upon the basis of which past costs and revenues can be ascertained as a starting point for future projection." ***A test year is a tool used to find the relationship between investment, revenues, and expenses***.[99]

[95] *Id* at page 22.
[96] *Id.* at page 34.
[97] *Id.* at page 27.
[98] KCPL Initial Brief, page 27.
[99] *State ex rel. GTE North, Inc. v. Public Service Commission*, 835 S.W.2d 356 (Mo.App. 1992).

Given that it is the relationship of costs, revenues and rate base and not the level of individual costs that is the critical inquiry, KCPL's claim that it "will lose money on these costs" is the wrong consideration. For instance, while KCPL claims that "it is a given" that it will lose money on these costs, it is also a "given" that KCPL will make money on other items. As an example, Staff is aware of a capacity agreement that became effective shortly after the true-up date. It is a "given" that KCPL will make money as a result of that item.[100] There are undoubtedly several other items that would decrease KCPL's revenue requirement, but, since they are not within the test year / true-up, they were not included in this case.[101]

This "given", that there are other items on which KCPL will make money, is a fact of life. The existence of such items following recent KCPL cases is significant. For instance, following the completion of a case, KCPL made money associated with: (1) reduced rate base resulting from depreciation; (2) increased off-system sales revenues; (3) reduced payroll and benefit costs associated with downsizing; (4) reductions in fuel and freight costs; (5) reduced inventory costs; (6) reduced debt costs; (7) reduction in income taxes; (8) reduced equity costs; and (9) increase customer revenues.[102]

The existence of offsetting costs is the exact point underlying the test year concept. As the Court of Appeals points out, it is test year "relationship between investment, revenues, and expenses" that is critical. There are bound to be some costs that will increase. Similarly, there are bound to be other costs that will decrease or

[100] Tr. 2057.
[101] Tr. 2057-2058.
[102] Exhibit 212, Featherstone Surrebuttal, page 26. *See also,* Exhibit 502, Brosch Direct (Revenue Requirement), page 12) indicating considerable cost savings associated with refinancing of long-term debt both in the past and in the expected future as well as cost savings associated with supply chain transformation projects and inventory optimization.

revenues that will increase. Either way, the test year relationship is maintained. Noticeably, while KCPL proposes trackers for the items on which it claims that it "will lose money", it does not seek to track these offsetting items on which it "will make money." Such a one-sided approach to trackers demonstrates the utility's ultimate desire to destroy the test year matching and "game" the ratemaking process.

> The many diverse elements of electric utility revenue requirements are constantly changing between test years. Some utility costs increase while others decline. . . . Any attempt to isolate and track selected costs that are expected to increase, while ignoring the other continuous changes in the utility's revenue requirement elsewhere that may offset such cost increases opens the regulatory system up to gaming and excessive rates. The isolation of only cost increases for regulatory tracking and future recovery creates a problem of "piecemeal ratemaking" that destroys the essential balance and "matching" of costs and revenues that is performed by measuring all of the elements of the test year revenue requirement at the same point in time and in a balanced manner in formal rate cases.[103]

Recognizing that offsetting cost reductions / revenue increases are a given and that KCPL's tracker proposal obliterates the fundamental relationship created through the test year, the Commission should reject KCPL's tracking proposals.

4. Need for Future Rate Cases

At pages 26-27 of its Initial Brief, KCPL bemoans its continued filing of rate cases. Ever willing to grasp an opportunity, KCPL implies that the implementation of trackers would have reduced the need for these past rate cases as well as future rate cases. KCPL's implicit claims are misplaced. Also missing from KCPL's argument is any enforceable commitment to file either fewer or smaller future rate cases, if its tracker and FAC proposals are granted, which reveals the Company's opportunistic approach that seeks unbalanced regulation to maximize revenues and profits.

[103] Exhibit 502, Brosch Direct (Revenue Requirement), pages 11-12.

First, contrary to KCPL's implication, the 6 rate cases filed over the past 9 years were not the result of increases in vegetation management, property taxes, cyber-security or transmission costs. Rather, as KCPL is undoubtedly aware, but conveniently fails to recognize, those cases were a direct result of KCPL's capital investment in Iatan 1, Iatan 2 and La Cygne.[104] The existence of the proposed trackers would not have alleviated the need for such prior rate cases. This fact is best demonstrated by the fact that, despite its multitude of trackers, KCPL filed an equal number of rate cases in Kansas, its other jurisdiction. Tracker mechanisms in prior years simply would not have reduced the number of recent KCPL rate cases.

Next, given the continued requirement to meet increasing environmental regulations, it is likely that KCPL will continue to have occasional future rate cases to reflect increased investment in rates. As such, the existence of trackers will not eliminate the need for these future cases. In fact, recognizing that a tracker simply defers increases in costs until a future case, a necessary part of a tracker is that there is a future case to collect the costs that are deferred on a piecemeal basis after the test year. Therefore, contrary to KCPL's implicit promise, the Commission's implementation of trackers will not eliminate the need for future rate cases, but by their very nature, force the need for a future case. In fact, it is noticeable that KCPL's request for trackers did not include its commitment to forego future rate cases. Clearly, KCPL seeks to have the best of both worlds. . . a sweetened regulatory framework now while simultaneously preserving its unilateral ability to file future rate cases when motivated by corporate profits.

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[104] See, Regulatory Plan, Case No. EO-2005-0329.

5. Purpose of Trackers

At page 27 of its Initial Brief, KCPL attempts to hide its true motivation for the proposed trackers and claims:

> T]he purpose of a tracker mechanism is to bring *transparency* to the amount of money lost or gained by the Company on these expenses and give the Company or consumers an opportunity with a future rate case to recover the loss. A tracker gives the Commission and regulators more information, not less. It operates as a feedback-mechanism, giving the Commission a comparison between rate-setting process and the reality of the rate-year. Nothing about the operation of a tracker diminishes the general rate case as the process by which rates are set and all relevant factors are considered.[105]

KCPL's claim underlying the purpose of trackers raises two important points.

First, trackers are not about transparency. In the event that the Commission desires to see an isolated break-down of specific costs and a comparison between the amount included in rates and the amount experienced following the rate case, that information already exists. KCPL certainly has this information and can provide this information. Staff and other parties have requested, and KCPL has provided, very detailed information about its specific costs in rate cases. The Commission does not need to create a tracker, destroy the test-year matching concept and ruin all management incentive to control such costs in order to gain such "transparency."

In reality, the purpose of a tracker is about shifting risk and increasing revenues. Specifically, by implementing a tracker, a utility seeks to shift the risk that certain costs will increase from the utility to the ratepayer. The utility seeks to shift this specific risk component while simultaneously preserving the possibility that it will see and keep increased profits associated with revenues that are increased or other costs that are decreasing. Through this mechanism of shifting some costs and risks and preserving

[105] KCPL Initial Brief, pages 27-28.

other opportunities, future rates and profits are increased.[106] Clearly then, a tracker is not about transparency.

Second, contrary to KCPL's self-serving claims, a tracker does diminish "the general rate case as the process by which rates are set." As indicated, the Court of Appeals has previously indicated that a fundamental aspect of ratemaking is the test year concept and the creation of a relationship between investment, revenues and expenses. This sentiment was reflected in the testimony of Mr. Brosch.

> Traditional regulation of energy utilities involves the conduct of formal rate cases, in which the utility selects a test year and presents a calculation of its desired revenue requirement, including operating expenses, depreciation and taxes, plus a rate of return applied to a rate base measure of invested capital. The key characteristics of traditional rate case regulation include:
>
> •A **test year**, in which all of the components of the revenue requirement are holistically analyzed and quantified in a balanced and internally consistent manner with appropriate "matching" of costs and revenues.
>
> •Utilization of regulatory lag as an **efficiency incentive** which financially rewards the utility for achieved cost reductions, by allowing it to keep those savings until the next case, and punishes the utility, through reduced earnings, when costs increase more rapidly than revenues between test years.[107]

Through its tracker proposal, and under the alleged guise of "transparency," KCPL seeks to destroy both of these critical aspects of the general rate case process. Specifically, by tracking one cost component and deferring any changes in that cost for recovery in a future case, a tracker mechanism precludes the opportunity for consideration of offsetting changes in other costs and revenues. This deferral of changes in a single cost item, without consideration of changes in other costs and revenues,

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[106] Exhibit 502, Brosch Direct (Revenue Requirement), page 9.
[107] *Id.* at page 13.

destroys the test year and matching of costs and revenues to be used in the future rate case.

Next, by allowing for deferral of any changes in a specific cost item, the tracker mechanism destroys the efficiency incentive that is inherent in the current general rate case process.

> A tracking mechanism for a specific cost eliminates the regulated lag incentive that would normally serve to encourage efficiency and cost control between rate cases. If every dollar of a tracked type of cost is eligible for deferral and future rate recovery, management can afford to be less concerned about efficiency and the aggressive pursuit of cost containment for that type of cost and can be expected to focus attention on other areas of the business where earnings will be impacted by cost changes. In fact, if the pursuit of new efficiencies in connection with a tracked cost involves any significant risks or the incurrence of other costs that are not tracked, rational business behavior would discourage the pursuit of such efficiencies.[108]

As can be seen then, KCPL's is attempting to downplay the purpose and impact of a tracker. Contrary to KCPL's suggestion, a tracker is not about transparency. That transparency, to the extent that it is desired by the Commission, is available without opening the Pandora's box that is associated with tracking mechanisms. Next, contrary to KCPL's claims, a tracker mechanism does diminish the general rate case process by obliterating the test year matching concept and destroying the incentive the current exists to minimize costs.

6. Impact of UCCM

In its Initial Brief, KCPL wrongly claims that "UCCM is about the FAC prior to the passage of Section 386.266."[109] Again, KCPL either misunderstands the point of this seminal decision or else it seeks to mislead the Commission about the implications of this

[108] *Id.* at page 15.
[109] KCPL Initial Brief, page 28.

decision. Certainly, *UCCM* did address the legality of an FAC prior to the passage of Section 386.266. In this regard, much like MECG is currently claiming, the Court found that the Commission had no specific statutory authority to implement an FAC. The remainder of the *UCCM* decision is equally important however. Recognizing that the utilities sought to collect a surcharge of money previously uncollected under the FAC, the Court addressed this surcharge. Furthermore, the Court addressed its available remedies and clarified the doctrine against retroactive ratemaking. There, the Court said:

> The utilities take the risk that rates filed by them will be inadequate, or excessive, each time they seek rate approval. To permit them to collect additional amounts simply because they had additional past expenses not covered by either clause is ***retroactive rate making***, i.e., the setting of rates which permit a utility to recover past losses or which require it to refund past excess profits collected under a rate that did not perfectly match expenses plus rate-of-return with the rate actually established. Past expenses are used as a basis for determining what rate is reasonable to be charged in the future in order to avoid further excess profits or future losses, but under the prospective language of the statutes, *§§ 393.270(3)* and 393.140(5) they cannot be used to set future rates to recover for past losses due to imperfect matching of rates with expenses.[110]

Clearly then and now, contrary to KCPL's attempts to minimize the importance of the *UCCM* decision, that decision indicates that, without specific statutory authority, it is retroactive rate making for the commission to allow a utility "to collect additional amounts" simply because a rate "did not perfectly match expenses plus rate-of-return with the rate actually established." Similarly, past expenses "cannot be used to set future rates to recover for past losses due to imperfect matching of rates with expenses." Given that KCPL's proposed trackers seek to violate both of these fundamental concepts, without any specific statutory authority, they are clearly unlawful.

[110] *UCCM* at page 59.

7. <u>MECG's Alleged Use of "Multi-Factor Tests"</u>

At page 29 of its Initial Brief, KCPL accuses MECG of constructing "multi-factor tests out of whole cloth for assessing the appropriateness of using a tracker mechanism." KCPL's depiction is inaccurate. In reality, it is KCPL that seeks to use this cloth to hide itself from the multi-factor test that is <u>required</u> by court decisions (i.e., *UCCM* and *Sibley*) as well as previous Commission orders. Specifically, as a result of the *Sibley* court's limiting authorization for deferral accounting specifically to "extraordinary" events, MECG urges the Commission to apply the extraordinary standard to KCPL's proposed tracking mechanisms. Next, consistent with the Commission's criteria applicable to the use of deferred accounting in the context of a fuel adjustment clause, MECG encourages the Commission to also apply the following criteria:

1. Substantial enough to have a material impact upon revenue requirements and the financial performance of the business between rate cases.

2. Beyond the control of management, where utility management has little influence over experienced revenue or cost levels.

3. Volatile in amount, causing significant swings upward and downward in income and cash flows if not tracked.

4. Straightforward and simple to administer, readily audited and verified through expedited regulatory reviews.

5. Balanced, such that any known factors that mitigate cost impacts are accounted for in a manner that preserves test year matching principles.[111]

Recognizing that MECG's criteria are based upon the *Sibley* limited authority for the use of deferral accounting as well as the Commission's established criteria, KCPL's claims that this multi-factor test being developed out of "whole cloth" is absurd. The first

[111] Exhibit 502, Brosch Direct (Revenue Requirement), page 18.

three of these criteria have also been acknowledged by the Commission for consideration whenever an FAC is requested and criteria 4 and 5 represent essential and practical considerations for any tracker mechanism. Undoubtedly, KCPL makes such an accusation out of its inability to meet these common sense criteria and its desire to implement a more relaxed standard whenever piecemeal cost tracking would be profitable.

V. TRANSMISSION EXPENSES AND TRACKER

At pages 60-63 of its Initial Brief, KCPL asks for several unprecedented approaches associated with its ongoing transmission costs. First, KCPL asks that the Commission allow it to implement a tracker to defer and recover changes in transmission costs over and above that included in rates. Related to this request, KCPL greedily asks that the Commission allow it to include any balance in rate base (i.e., earn a return on the balance). Second, in the event that the Commission rejects KCPL's tracker proposal, KCPL asks that the Commission include an arbitrary, inflated amount of transmission expenses in rates in this case.

As this brief demonstrates, the Commission should reject both of KCPL's requests. ***First***, as previously demonstrated, transmission costs are not "extraordinary". In its holding less than 12 months ago, the Commission explicitly found that such costs were not "extraordinary" and, therefore, not eligible for deferral accounting. Similarly, in the event that the Commission allows for the implementation of such a tracker, it should not allow rate base treatment of any tracker balances. ***Second***, the Commission should reject KCPL's fallback request to include an arbitrarily inflated amount of transmission costs in rates.

A. TRANSMISSION TRACKER

At pages 34-41, MECG pointed out that, outside of a fuel adjustment clause or MEEIA costs, the Commission does not have specific statutory authority for the implementation of trackers. Rather, any authority for the deferral of such costs is contained in the Court of Appeal's finding in the *Sibley* case. Consistent with that decision, any deferral of costs is limited solely to ***extraordinary*** events.

Less than 12 months ago, the Commission considered an identical request to that currently advanced by KCPL in this case. In that case, the Commission explicitly applied the "extraordinary" standard and held that KCPL's request for a tracker was inappropriate.

> In Missouri, rates are normally established based off of a historic test year. The courts have stated than an AAO allows the deferral of a final decision on current *extraordinary* costs until a rate case and therefore is not retroactive ratemaking. Consistent with the language in General Instruction No. 7, the Commission has evaluated the transmission costs for which Companies seek an AAO to determine if they are an unusual and infrequent occurrence. The Commission concludes they are not.
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> Companies began incurring transmission expenses when they began providing retail electric service. Transmission costs are part of the ordinary and normal costs of providing electric service and are expected to continue in the foreseeable future. Furthermore, while the transmission costs at issue may have a significant effect on Companies, they are not "abnormal and significantly different from the ordinary and typical activities" of the Companies. The increase in transmission costs was anticipated and is indeed the norm for all electric utility members of SPP. Therefore, the transmission costs are not extraordinary.[112]

Given the clarity of the *Sibley* decision and recognizing the fact that transmission costs are not extraordinary, the Commission should once again reject KCPL's request.[113]

Never willing to accept a negative decision from the Commission, KCPL again ignores the "extraordinary" standard and, instead pretends to apply the criteria for a fuel adjustment clause (sufficient magnitude, volatility, and outside the control of management).[114] Burying its head in the sand, KCPL postulates that, if it is good enough for the fuel adjustment clause, it must be good enough for the requested trackers.[115]

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[112] Case No. EU-2014-0077, *Report and Order*, issued July 30, 2014, at page 10.
[113] Similar to other issues, the Commission should consider rejecting rate case expense for burdening this case with a request that is identical to that litigated less than a year ago.
[114] In its Initial Brief, MECG has already pointed out that KCPL's transmission costs do not meet the criteria advanced by KCPL. (See, MECG Initial Brief, pages 81-82).
[115] KCPL Initial Brief, pages 61-62.

While KCPL has proposed multiple tracker mechanisms, its request for a transmission tracker is most egregious. Specifically, as part of the FAC legislation passed in 2005, the General Assembly allowed for the deferral and later recovery of a limited amount of transmission costs through the FAC. It defies credulity to think that, while expressly allowing for the deferral of a limited amount of transmission costs in the fuel adjustment clause, the General Assembly had already implicitly allowed for the deferral of all transmission costs. If such implicit authority already existed, why did the General Assembly deem it appropriate to include a redundant provision for the deferral of a limited amount of such costs? Such an interpretation makes this portion of the FAC legislation redundant. Given that the General Assembly has expressly limited the Commission's authority to defer transmission costs to those associated with purchased power costs, the Commission should reject KCPL's invitation to defer all transmission costs through backdoor, allegedly implied, authority.

In the event that the Commission deems it appropriate to reach beyond its statutory authority and allows KCPL to implement a transmission tracker, it should not allow for rate base treatment of any under-recovered tracker balance. Rate base treatment of costs is generally limited to capital investment. In contrast, KCPL's transmission costs proposed for tracking are not capital investments. Rather, these costs are recorded as expenses and should not be provided capitalized (rate base) treatment.

B. TRANSMISSION EXPENSE

Undoubtedly in recognition of the fact that the Commission lacks statutory authority to defer ordinary and recurring costs like transmission expenses, KCPL seeks another way to guarantee full recovery of such costs. While agreeing that the annualized

level of transmission expense for the test year should be $54,027,871,[116] KCPL asks that the Commission arbitrarily include an additional $5 million of "forecast" transmission expense if those costs are not included in either the FAC or tracker.[117] KCPL's request to arbitrarily inflate transmission costs is particularly egregious given that customer rates have already increased 57% since 2006 and 82% if the rates from this case are reflected.[118] Notably, KCPL does not propose to reach forward for estimated reductions in other expenses, even though declining expenses are expected in the future.

KCPL's request is also problematic in that it violates the fundamental matching principle inherent in the historical test year concept. In the ratemaking process, Section 393.270.4 requires that the Commission consider costs "actually expended." As a result of the focus on costs that were "actually expended", Missouri has always been a historical test year jurisdiction.

As Mr. Brosch points out, one of the key characteristics of Missouri rate case regulation is the reliance on a historical test year and the matching principal contained therein.[119] Through its request to include an additional $5 million of forecasted transmission expense, KCPL seeks to violate the historical focus of Section 393.270.4 as well as the matching principal inherent in historical test year regulation. Such a request opens the proverbial Pandora's box. Specifically, if the Commission were to include an

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[116] Exhibit 166, Klote True-Up Rebuttal, page 2 ("KCP&L and Staff have reached agreement that $54,027,871 (KCP&L Total Company) represents the level of annualized transmission expense as of the May 31, 2015 true-up period before other adjustments).

[117] KCPL Initial Brief, page 60 ("If SPP transmission fees are not included in either the FAC or a tracker, $5 million of annual forecast SPP transmission fees expense (Missouri jurisdictional) ***should be added to the revenue requirement above the base amount of SPP transmission fees***." (emphasis added).

[118] MECG Initial Brief, page 6.

[119] Exhibit 502, Brosch Direct (Revenue Requirement), page 13 ("The key characteristics of traditional rate case regulation include: a test year, in which all of the components of the revenue requirement are holistically analyzed and quantified in a balanced and internally consistent manner with appropriate 'matching' of costs and revenues.)"

additional "forecast" amount of transmission expense, it should also include an additional "forecast" amount of wholesale and retail revenues. Certainly, it is not appropriate for KCPL to utilize forecasted amounts only for those items that serve to inflate revenue requirement.

Given the questionable nature of KCPL's request to include an additional $5 million of forecast transmission expense, the Commission should reject KCPL's request. Instead, the Commission should include $54,027,821 of annualized transmission expense as agreed upon by Staff[120] and KCPL.[121]

[120] Exhibit 256, Lyons True-Up Rebuttal, page 3.
[121] Exhibit 166, Klote True-Up Rebuttal, page 2.

VI. PROPERTY TAX EXPENSES AND TRACKER

Much like its two prong approach for transmission costs, KCPL takes a similarly novel approach with regards to property taxes. First, at pages 65-69 of its Initial Brief, KCPL asks that the Commission allow it to implement a property tax tracker to defer and recover any changes in property taxes from that amount included in rates. As with its requested transmission tracker, KCPL asks for rate base treatment of any tracker balance. Second, at pages 69-70 of its Initial Brief, KCPL asks that the Commission disregard the historical test year approach suggested by Section 393.270.4 and, instead, adopt a forecasted level of property taxes if its one-sided tracker proposal is not accepted.

As this brief demonstrates, the Commission should reject both of KCPL's requests. ***First***, as previously demonstrated, property tax expenses are not "extraordinary". Rather, as with all other utilities, KCPL has always incurred property taxes and historically incurred tax levels have not been volatile. Moreover, such taxes are projected to continue indefinitely into the future. ***Second***, recognizing its use of historical test years and the matching of costs, revenues and investment, the Commission should reject KCPL's fallback request to include an arbitrarily inflated amount of property taxes in rates.

A. PROPERTY TAX TRACKER

As previously indicated, there is no specific statutory authority for the implementation of a property tax tracker. Rather, any authority to implement such a tracker is necessarily contained with the *Sibley* decision limiting deferral accounting to "extraordinary" costs.

Specific statutory authority for such a tracker could be easily constructed by the General Assembly. For instance, in 1997, the Kansas Legislature provided specific statutory authority for the Kansas Corporation Commission to implement a property tax tracker.

> K.S.A. 66-117(f): Whenever, after the effective date of this act, an electric public utility, a natural gas public utility or a combination thereof, files tariffs reflecting a surcharge on the utility's bills for utility service designed to collect the annual increase in expense charged on its books and records for ad valorem taxes, such utility shall report annually to the state corporation commission the changes in expense charged for ad valorem taxes. For purposes of this section, such amounts charged to expense on the books and records of the utility may be estimated once the total property tax payment is known. If found necessary by the commission or the utility, the utility shall file tariffs which reflect the change as a revision to the surcharge. Upon a showing that the surcharge is applied to bills in a reasonable manner and is calculated to substantially collect the increase in ad valorem tax expense charged on the books and records of the utility, or reduce any existing surcharge based upon a decrease in ad valorem tax expense incurred on the books and records of the utility, the commission shall approve such tariffs within 30 days of the filing. Any over or under collection of the actual ad valorem tax increase charged to expense on the books of the utility shall be either credited or collected through the surcharge in subsequent periods. The establishment of a surcharge under this section shall not be deemed to be a rate increase for purposes of this act. The net effect of any surcharges established under this section shall be included by the commission in the establishment of base rates in any subsequent rate case filed by the utility.

Clearly, KCPL is incapable of pointing to similar authority for the implementation of a property tax tracker in Missouri. Given its inability to direct the Commission to specific statutory authority as well as its continued refusal to attempt to apply the *Sibley* court's "extraordinary" standard, KCPL instead seeks to adopt a single portion of the Commission's fuel adjustment clause criteria (beyond management control) and apply it in isolation to its property tax tracker request. Specifically, in its brief, KCPL alleges that, because property taxes are beyond management control, this supports the

implementation of a tracker mechanism.[122] Noticeably, despite urging for the use of such liberal criteria,[123] KCPL never argues that property taxes are volatile or materially significant.

In its Initial Brief, MECG noted that property taxes do not meet the "extraordinary" standard. Similarly, MECG asserted that, a thorough application of even KCPL's own criteria leads to the undeniable conclusion that a property tax tracker is not appropriate. Specifically, MECG demonstrated, through the expert testimony of Mr. Brosch, that property taxes are not significant,[124] are not volatile,[125] and are not entirely outside the control of KCPL's management.[126]

Recognizing that property taxes are not "extraordinary" as well as the fact that KCPL has not even alleged that such costs are volatile[127] or significantly material, the Commission should reject KCPL's request to implement a property tax tracker.

In the event that the Commission deems it appropriate to reach beyond its statutory authority and allow KCPL to implement a property tax tracker, it should not allow for rate base treatment of any deferred cost balance. Rate base treatment of costs is generally limited to capital investment. In contrast, KCPL's property taxes expenses proposed for tracking are not capital related. Rather, these costs are recorded as expenses and should not be provided capitalized (rate base) treatment.

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[122] KCPL Initial Brief, pages 68-69.
[123] KCPL Initial Brief, page 33.
[124] MECG Initial Brief, pages 82-83 (citing to Exhibit 502, Brosch Direct (Revenue Requirement), page 19).
[125] *Id.* at page 83 (citing to Exhibit 502, Brosch Direct (Revenue Requirement), page 21).
[126] *Id.* at pages 83-84 (citing to Exhibit 502, Brosch Direct (Revenue Requirement), pages 21-22).
[127] In fact, in its Initial Brief, KCPL admits that, because they are largely based upon net operating income, property taxes are not likely to increase until "2017 or later." (KCPL Initial Brief, page 66).

B. PROPERTY TAX EXPENSE

While KCPL spends a great deal of time criticizing Staff's approach for calculating test year property tax expense,[128] it is important to recognize that KCPL agrees with Staff's property tax expense calculation.[129] Specifically, Staff and KCPL both agree that property taxes for the test year should be $91 million.[130] Nevertheless, in the event that the Commission rejects KCPL's request for a property tax tracker, KCPL proposes that the Commission include an additional, arbitrary, "forecast" amount of property taxes of $5.6 million over the annualized $91 million level.

As with KCPL's request to include an inflated, forecast amount of transmission costs in rates, KCPL's request to include an additional, forecast amount of property taxes is also problematic. Specifically, the use of a forecast amount of property taxes violates the fundamental matching principle inherent in the historical test year concept. In the ratemaking process, Section 393.270.4 requires that the Commission consider costs "actually expended." As a result of the focus on costs that were "actually expended", Missouri has always been a historical test year jurisdiction.

As Mr. Brosch points out, one of the key characteristics of Missouri rate case regulation is the reliance on a historical test year and the matching principal contained therein.[131] Through its request to include an additional $5.6 million of forecasted property taxes, KCPL seeks to violate the historical focus of Section 393.270.4 as well as

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[128] KCPL Initial Brief, page 66 ("Staff's backwards-looking approach); page 66 ("a method which does not give the Company a reasonable opportunity to recover its prudently incurred property tax expense"); page 66 ("the reason why Staff's methodology is out of date is easy to understand.").
[129] Exhibit 112, Hardesty Rebuttal, page 24.
[130] KCPL Initial Brief, page 64.
[131] Exhibit 502, Brosch Direct (Revenue Requirement), page 13 ("The key characteristics of traditional rate case regulation include: a test year, in which all of the components of the revenue requirement are holistically analyzed and quantified in a balanced and internally consistent manner with appropriate 'matching' of costs and revenues.)"

the matching principal inherent in historical test year regulation. Such a request opens the proverbial Pandora's box. Specifically, if the Commission were to include an additional "forecast" amount of property taxes, it should also include an additional "forecast" amount of wholesale and retail revenues. Certainly, it is not appropriate for KCPL to utilize forecasted amounts only for those items that serve to inflate revenue requirement.

Given the questionable nature of KCPL's request to include an additional $5.6 million of forecast property taxes, the Commission should reject KCPL's request. Instead, the Commission should include $91 million of annualized property taxes as agreed upon by Staff and KCPL.

VII. CIP / CYBER-SECURITY EXPENSES AND TRACKER

Much like its two prong approach for transmission costs and property taxes, KCPL takes a similar approach with regards to Critical Infrastructure Protection ("CIP") / Cyber-Security costs. First, at pages 73-75 of its Initial Brief, KCPL asks that the Commission allow it to implement a cyber-security tracker to defer and recover any changes in costs from that amount included in rates. Like its other tracker requests, KCPL also asks for rate base treatment of any tracker deferred cost balance.[132] Second, at pages 71 and 78 of its Initial Brief, KCPL asks that the Commission disregard the historical test year approach suggested by Section 393.270.4 and, instead, adopted a forecasted level of cyber-security costs.

As this brief demonstrates, the Commission should reject both of KCPL's requests. ***First***, as previously demonstrated, there is no specific statutory authority for the creation of a cyber-security tracker. Rather, the creation of such a tracker must be pursuant to the *Sibley* court's approval of deferral accounting associated with "extraordinary" events. Certainly, cyber-security costs are not "extraordinary". Rather, as with all other utilities, KCPL has always incurred security costs. Moreover, such costs are projected to continue indefinitely into the future. ***Second***, recognizing its use of historical test years and the matching of costs, revenues and investment, the Commission should reject KCPL's fallback request to include an arbitrarily inflated amount of cyber-security costs in rates.

A. CIP / CYBER-SECURITY TRACKER

As previously indicated in connection with KCPL's other piecemeal tracking proposals, there is no specific statutory authority for the implementation of a cyber-

[132] KCPL Initial Brief, page 80.

security expense tracker. Rather, any authority to implement such a tracker is necessarily contained with the *Sibley* decision limiting deferral accounting to "extraordinary" costs. Clearly KCPL has not and is incapable of demonstrating that cyber-security expenses are "extraordinary." Given this obvious shortcoming, KCPL instead seeks to adopt a single portion of the Commission's fuel adjustment clause criteria (beyond management control)[133] and apply in isolation it to its cyber-security tracker request. Specifically, in its brief, KCPL alleges that, because cyber-security costs are beyond management control, this supports the implementation of a tracker mechanism.[134] Noticeably, despite urging for the use of such liberal criteria,[135] KCPL never argues that cyber-security costs are volatile or materially significant.

In its Initial Brief, MECG noted that cyber-security costs do not meet the "extraordinary" standard. Similarly, MECG asserted that, a thorough application of even KCPL's own criteria leads to the undeniable conclusion that a cyber-security expense tracker is not appropriate. Specifically, MECG demonstrated, through the expert testimony of Mr. Brosch, that cyber-security costs are not significant,[136] are not volatile,[137] and are not entirely outside the control of KCPL's management.[138]

Recognizing that cyber-security expenses are not "extraordinary" as well as the fact that KCPL has not even alleged that such costs are volatile or significantly material, the Commission should reject KCPL's request to implement a cyber-security tracker.

[133] KCPL Initial Brief, page 75 ("the Company has only limited ability to control" cyber-security costs");
[134] KCPL Initial Brief, page 75.
[135] KCPL Initial Brief, page 33.
[136] Exhibit 502, Brosch Direct (Revenue Requirement), page 33.
[137] *Id.* at page 34.
[138] *Id.*

Another reason for the denial of a cyber-security tracker is found in the fact that, after nine months of this case, KCPL has still yet to define such cyber-security programs and costs with any specificity. As Mr. Brosch points out:

> The proposed tracking mechanism is open ended and Mr. Rush simply states, "[t]he cost to comply is undefined at this time, but will be substantial" and that "KCP&L is working diligently to develop an overall plan….[t]he plan is to establish an amount reflecting personnel hired directly attributable to the CIP in the true-up and also include any defined costs that may have already been incurred.[139]

Ultimately, Staff agrees with Mr. Brosch's conclusion.[140] In fact, in its Initial Brief, KCPL admits that such programs and costs are uncertain. "KCP&L agrees that CIP/cyber-security standards continue to evolve and that this brings an element of uncertainty to both implementation plans and cost estimates."[141] Commission-approved tracking for vaguely defined cyber-security expenses would invite potential overstatement of any deferred costs and frustrate the ability of Staff to effectively audit such deferrals.

In a recent decision, the West Virginia Public Service Commission rejected a utility request for a cyber-security tracker as a result of the uncertainty of such costs and programs.

> The Commission is aware of the increased security dangers presented in the modern world, particularly to the electric utility system. We know that extraordinary steps will become necessary (and may become common), but the Commission concludes that in the absence of concrete plans to implement specific security measures, projected costs, or new regulatory requirements, the proposal of the Companies to implement a Security Rider is premature.[142]

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[139] *Id.* at page 30.
[140] Exhibit 235, Oligschlaeger Rebuttal, page 12.
[141] KCPL Initial Brief, page 76.
[142] See, Case No. 14-1152-E-42T, *Commission Order on the Tariff Filing of Appalachian Power Company and Wheeling Power Company to Increase Rates, and Petition to Change Depreciation Rates*, issued May 26, 2015, at page 95.

Similarly, the Maryland Public Service Commission[143] and Indiana Utility Regulatory Commission[144] have rejected a tracker proposal associated with cyber-security costs.

In the event that the Commission deems it appropriate to reach beyond its statutory authority and allow KCPL to implement a cyber-security tracker, it should not allow for rate base treatment of any balance. Rate base treatment of costs is generally limited to capital investment. In contrast, KCPL's cyber-security expenses are not capital investments. Rather, these costs are recorded as expenses and deferrals of such expenses should not be provided capitalized (rate base) treatment.

B. CIP / CYBER-SECURITY EXPENSE

KCPL has agreed that an appropriate annualized (total-company) amount of CIP / cyber-security expenses is $4,150,012 associated with cyber-security costs and $4,766,126 associated with Critical Infrastructure Protection ("CIP") costs.[145] Despite this agreement, KCPL suggests that the Commission should include an additional forecasted amount $3.5 million in the event that the Commission rejects KCPL's proposed tracker.[146] The egregious nature of KCPL's request to include an additional amount of CIP / cyber-security costs is demonstrated by the fact that KCPL's estimates that such costs will decrease dramatically in the near future. In fact, KCPL is so used to

[143] Re: Baltimore Gas and Electric, Maryland Public Service Commission, Case No. 9208, issued June 21, 2010.

[144] Re: Indianapolis Power & Light Company, Indiana Utility Regulatory Commission, Case No. 43960, issued November 22, 2011.

[145] Exhibit 166, Klote True-Up Rebuttal, page 3.

[146] KCPL Initial Brief, page 71. *See also*, KCPL Initial Brief, page 79 ("The second approach proposed by KCP&L is to base the rate allowance on a forward-looking estimate of CIP / cyber-security O&M expenses.").

complaining about increasing costs that it fails to recognize that such costs are expected to actually decrease.[147]

Table 3: KCPL Projected Critical Infrastructure Protection / Cybersecurity Costs

Forecasted Costs:	2015	2016	2017
Non-Labor O&M	$ 8,541,288	$ 8,295,878	$ 6,752,557
Labor O&M	3,152,125	4,603,025	4,929,085
Capital Investment	12,932,083	5,129,262	6,205,815
Total Estimate	$ 24,625,495	$ 18,028,166	$ 17,887,458

Source: Exhibit 502, Brosch Direct (Revenue Requirement), page 32.

As previously explained, the use of a forecast amount of cyber-security expenses violates the fundamental matching principle inherent in the historical test year concept. In the ratemaking process, Section 393.270.4 requires that the Commission consider costs "actually expended." As a result of the focus on costs that were "actually expended", Missouri has always been a historical test year jurisdiction.

As Mr. Brosch points out, one of the key characteristics of Missouri rate case regulation is the reliance on a historical test year and the matching principal contained therein.[148] Through its request to include an additional $3.5 million of forecasted CIP / Cyber-Security costs, KCPL seeks to violate the historical focus of Section 393.270.4 as well as the matching principal inherent in historical test year regulation. Such a request opens the proverbial Pandora's box. Specifically, if the Commission were to include an additional "forecast" amount of CIP / Cyber-Security costs, it should also include an

[147] KCPL Initial Brief, page 78 ("Even when confronted with overwhelming evidence of substantially increasing CIP / cyber-security O&M expenses after May 31, 2015."). *See also*, KCPL Initial Brief, page 79 ("Given the continued expansion of CIP / cyber-security requirements, it is beyond a doubt that KCP&L's CIP / cyber-security O&M expenses will continue to raise after May 31, 2015."); KCPL Initial Brief, page 72 ("What is not uncertain, however, is the fact that future costs will exceed historical CIP / cyber-security O&M expense allowance included in rates.").

[148] Exhibit 502, Brosch Direct (Revenue Requirement), page 13 ("The key characteristics of traditional rate case regulation include: a test year, in which all of the components of the revenue requirement are holistically analyzed and quantified in a balanced and internally consistent manner with appropriate 'matching' of costs and revenues.)"

additional "forecast" amount of wholesale and retail revenues. Certainly, it is not appropriate for KCPL to utilize forecasted amounts only for those items that serve to inflate revenue requirement.

Given the questionable nature of KCPL's request to include an additional $3.5 million of forecast CIP / Cyber-Security costs, the Commission should reject KCPL's request. Instead, the Commission should include that amount previously agreed upon by Staff and KCPL.

VIII. MANAGEMENT AUDIT

In its Initial Brief, MECG demonstrated that, as compared to other regional and peer group utilities, KCPL's Administrative & General ("A&G") are excessive. Specifically, on a per-customer basis, KCPL's A&G costs are higher than all the other peer group electric utilities.

2013 and 2014 A&G Per Customer

Peer Company	2013 A&G per Customer	2013 Ranking	2014 A&G per Customer	2014 Ranking
Alliant	$176	14	$181	13
Avista	$176	13	$185	12
Black Hills	$298	3	$289	4
Cleco	$190	10	$201	9
GMO	$237	7	$236	7
IdaCorp	$299	2	$305	2
KCPL	**$303**	**1**	**$312**	**1**
KCPL & GMO	$278	5	$283	5
OGE	$139	16	$146	16
Pinnacle	$186	12	$165	14
PNM	$266	6	$257	6
Portland	$189	11	$192	10
TECO	$209	8	$187	11
UNS	$209	9	$221	8
Westar	$292	4	$299	3
Wisconsin	$172	15	$147	15

Source: Exhibit 246, Majors Testimony (corrected), page 52.

Given that these metrics indicate excessive A&G costs at KCPL, and recognizing the structural problems underlying these excessive costs, MECG recommends that "the Commission direct KCP&L to undergo a management audit by an independent auditor for the purpose of identifying cost savings and efficiencies. This audit should encompass

all functional operation and maintenance activities and expenses as well as all administrative and general activities and expenses."[149]

In predictive fashion, given that the undeniable conclusion is that KCPL's A&G costs are excessive, KCPL finds fault with the use of utility-specific FERC Form 1's. KCPL incorrectly claims that "the recording of expenses to A&G by utilities is very subjective and open to interpretation under the FERC USOA."[150]

KCPL's criticism is misplaced. As. Mr. Kollen points out, given the common definitions and instructions, the FERC Form 1 data is inherently reliable.

> The data provided in an electric utility FERC Form 1 is compiled, segregated and assigned to specific accounts pursuant to detailed account definitions and instructions. These accounts, definitions and instructions are known as the FERC Uniform System of Accounts. Furthermore, the utility is required to attest that the data conforms to the Uniform System of Accounts. Finally, the FERC Form 1 is required to be signed by an independent auditor. As such, there is a heightened level of reliability underlying this data and, as a result of common accounts and definitions, an increased level of comparability between different utilities.[151]

In fact, in recent cases, KCPL has expressly relied upon an A&G analysis, relying upon FERC Form 1 data, for purposes of calculating its merger synergies following its acquisition of Aquila.

> Mr. Kemp [KCPL] testified that in order to compare KCPL's synergy estimates to the synergies in other utility mergers, he classified both the base 2006 costs and the estimated synergies into six major functional areas: Generation, Transmission, Distribution, Customer Service, Sales, and Administrative & General (A&G). These groupings correspond to the functional groups of accounts in FERC's Uniform System of Accounts.[152]

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[149] *Id.*
[150] KCPL Initial Brief, page 111.
[151] Exhibit 501, Kollen Surrebuttal, page 9.
[152] Case No. EM-2007-0374, *Report and Order,* issued July 1, 2008, at page 102.

Further, given the inherent reliability underlying FERC Form 1, KCPL expressly used this data in this case for its own purposes. Specifically, for purposes of comparing energy costs, KCPL relied upon FERC Form 1 data.

> Q. Do others use the FERC Form 1 data for comparing utilities' fuel and power costs?
>
> A. Yes. For example, it was a component of a study regarding electric utility automatic adjustment clauses prepared for Edison Electric Institute by the Brattle Group.[153]

Clearly, despite KCPL's concerns with FERC Form 1 data, KCPL routinely uses this data. This is not surprising given the common definitions and instructions contained in the Uniform System of Accounts and utilized in the FERC Form 1's. Recognizing KCPL's repeated and long-standing reliance on the FERC Form 1 data, the Commission should not give any credibility to KCPL's current self-serving concern with such data.

Based upon its sudden lack of confidence in the use of FERC Form 1 data, KCPL seeks to promote its own A&G analysis. Specifically, in its Rebuttal Testimony, KCPL provided an A&G analysis conducted by PA Consulting. Not surprisingly, given the undeniable conclusions that result from the FERC Form 1 analysis, the PA Consulting study provides KCPL the answer that it desperately needs, "KCPL's A&G costs are not excessive and are, in fact, below the median of the other utilities that participated in the benchmark study."[154] As the record indicates, however, there are fundamental problems with the KCPL benchmark study.

As Mr. Kollen points out, the benchmark analysis relied upon by KCPL "are not structured by FERC account in the same manner that test year costs are developed and

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[153] Exhibit 104, Blunk Rebuttal, page 22.
[154] Exhibit 105, Bresette Rebuttal, page 11.

presented."[155] Second, recognizing that the Company refused to provide the underlying cost data, the results could not be verified or evaluated.[156] Third, "the comparisons were not comprehensive, but were limited to specific functions / activities."[157] Fourth, unlike the analysis conducted based upon FERC Form 1 data, the KCPL study does not appear to be based upon common account definitions and instructions.[158]

Ultimately, it is illogical that KCPL rejects the idea of a management audit. As KCPL readily admits, audits of a lesser scope have been beneficial in the past.

> **Mr. Woodsmall:** Okay. So do you believe that these external -- these process reviews that have been conducted in the past that you talked about with Commissioner Hall, do you believe those have been beneficial?
>
> **Mr. Bresette:** Yes. Otherwise I don't think the Company would have made the decision to engage a third party for -- for review of processes. The Company only makes prudent business expenses.
>
> **Mr. Woodsmall:** Okay. So with regard to the first one, you agree that there are times that outside consultants can provide benefits to management outside their normal operations; is that true?
>
> **Mr. Bresette:** Generally I would agree.
>
> **Mr. Woodsmall:** Okay. And you would also agree that there are consultants out there that may be able to provide benefits beyond what have already been identified by the consultants that you have retained; is that true?
>
> **Mr. Bresette:** I -- I guess it's possible.[159]

Recognizing that regulatory lag would dictate that any savings inure to shareholders, KCPL would initially receive the entirety of all savings.

[155] Exhibit 501, Kollen Surrebuttal, page 8.
[156] *Id.* While KCPL was allowed to provide its own identity within the benchmark study it "is bound by a contractual obligation that we are not to reveal any of the participants in this study." (Tr. 1161). In fact, given the confidentiality problems, KCPL did not attempt to verify the accuracy of any of the underlying data. (Tr. 1164).
[157] *Id.* at pages 8-9.
[158] *Id.* at page 9
[159] Tr. 1169-1171,

> While KCP&L witnesses attempt to portray regulatory lag as a negative aspect of the current Missouri regulatory paradigm, there is no question that it can work to the benefit of utility shareholders. Specifically, in those situations where costs decrease between rate cases, those savings completely inure to the benefit of the utility shareholders until such time as another rate case is initiated and rates are rebased. Similarly, to the extent that a management audit identifies cost savings, KCP&L shareholders will retain the entirety of those cost savings until a subsequent rate case. As such, my recommended management audit may be beneficial to KCP&L shareholders.[160]

In the final analysis, it is undeniable that KCPL's A&G costs are excessive. The reasons for these excessive costs are structural and incapable of being adequately addressed in a rate case. Given this, MECG urges the Commission to fulfill its customer protect mission and order that KCPL undergo an audit for the purpose of process improvement and reducing these excessive costs.

[160] Exhibit 501, Kollen Surrebuttal, page 12.

IX. INCOME TAX RELATED ISSUES

In its Initial Brief, KCPL obfuscates these tax issues and, like so many other issues, refuses to accept the guidance of previous Commission decisions. KCPL hopes that confusion, rather than clarity, may result in a decision in its favor. KCPL fails to recognize, however, that the burden of proof dictates that if it is successful in confusing the Commission on these issues, that the Commission must reject KCPL's position for a higher revenue requirement and, instead, adopt MECG's adjustments. Specifically, Section 393.150(2) requires KCPL to show, by a preponderance of the evidence, the truth of its claim. As such, a strategy of confusion works contrary to KCPL's ultimate purpose.

MECG does not seek to rely solely on burden of proof. Rather, MECG provided significant discussion in its Initial Brief explaining these issues. Specifically, at pages 103-117 of its Initial Brief, MECG discussed the complicated income tax related issues. ***First***, MECG pointed out that Mr. Brosch is widely recognized as an expert on tax-related issues. In fact, admitting his expertise, KCPL acknowledged that it has made several mistakes in the calculation of income tax expenses. ***Second***, MECG provided a thorough discussion regarding the timing differences between financial accounting under General Accepted Accounting Principles ("GAAP") and accounting under the Internal Revenue Code. These timing differences lead to the creation of both Accumulated Deferred Income Tax ("ADIT") assets and liabilities. Given the potential inclusion of these assets and liabilities in rate base, these ADIT balances have the ability to significantly affect rate base and KCPL's revenue requirement. ***Finally***, MECG pointed out that KCPL's position with respect to: (1) Construction Work in Progress ("CWIP") -

related ADIT liability balance; (2) 1KC Place Lease ADIT asset balance; (3) accrued employee compensation ADIT asset balance; and (4) Net Operating Tax Losses is detrimental to ratepayers and is designed to inflate KCPL's revenue requirement.

A. CWIP-RELATED ADIT

In its Initial Brief, MECG explained that, since ratepayers provide a return on projects under construction, through the application of Allowance for Funds Used During Construction ("AFUDC"), the ADIT liability balance should be included in rate base.[161] While it is not a current cash return, the AFUDC return is capitalized into the overall cost of the construction project and KCPL is allowed to fully recover this deferred return once the construction project is completed. Since ratepayers are providing KCPL a return on these construction projects through AFUDC, they should also receive the benefits of the associated ADIT balances. By excluding these ADIT balances as an offset to rate base, KCPL is earning the return and keeping all of the benefits of accumulated depreciation (e.g., lower current income taxes).[162] In other words, customers have to pay KCPL a return, yet, under KCPL's approach, customers receive none of the benefits.

In its Initial Brief, KCPL refuses to recognize the return provided by ratepayers through the application of AFUDC. KCPL doggedly repeats its argument that it "has appropriately excluded the ADIT liability related to CWIP since the capital expenditures have not been included in rate base."[163] Through this position, KCPL takes the narrow position that a return on construction projects can only be received by placing the investment in rate base. KCPL refuses to acknowledge that a return on these construction projects is, in fact, being received through the application of AFUDC. As Mr. Brosch

[161] MECG Initial Brief, pages 106-108.
[162] Exhibit 502, Brosch Direct (Revenue Requirement), pages 51-52.
[163] KCPL Initial Brief, page 128.

explains, "the AFUDC return is fully compensatory to KCPL and obligates ratepayers to repay in cash the full amount of all AFUDC that is reasonably recorded."[164]

Given that ratepayers provide a return, through AFUDC, on construction projects, they should also receive the benefits of the CWIP-related ADIT liability balances. The failure to include the ADIT liability balances in rate base serves to inflate KCPL's revenue requirement.

> It is necessary to fully account for CWIP-related ADIT balances to avoid an inflated rate base and excessive utility rates. CWIP-related ADIT balances must be included in rate base because AFUDC is applied to KCPL's gross investment in CWIP work orders, with no recognition given to the CWIP-related ADIT amounts that serve to reduce the Company's actual net capital requirements for CWIP.[165]

This position, advanced by Mr. Brosch in a recent Ameren proceeding, was expressly adopted by the Commission.

> Even though Ameren Missouri cannot add CWIP to its rate base, and therefore cannot earn a return on that investment, until the property is fully operational and used for service, it is allowed to earn an Allowance for Funds Used for Construction (AFUDC) before the property under construction is added to rate base. AFUDC is accrued during the process of construction and is added to the balances of plant in service that is included in rate base when the plant is placed in service. It is then recovered from ratepayers over the remaining life of the property.
>
> ***CWIP related ADIT balances must be accounted for in rate base*** because AFUDC is applied to Ameren Missouri's gross investment in CWIP, with no recognition given to the CWIP-related ADIT amounts that serve to reduce the company's actual net capital requirements for CWIP. . . . In other words, ***failure to recognize the CWIP-related ADIT balance in the company's rate base will overstate the companies AFUDC costs and future rate base, essentially allowing the company to earn AFUDC and a return on capital supplied by ratepayers***.[166]

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[164]Exhibit 502, Brosch Direct (Revenue Requirement), page 51.
[165] *Id.* at page 52.
[166] *Id.* at pages 28-30 (emphasis added).

After refusing to accept the fact that ratepayers provide an AFUDC return on construction work in progress, KCPL also refuses to accept the clarity of the Commission's decision. Instead, in its attempt to obfuscate this issue, KCPL claims that the Ameren decision is not applicable because of the existence of a KCPL Net Operating Loss ("NOL").[167] KCPL surmises that, since the Ameren decision was silent as to a NOL for Ameren, KCPL is in a different position than Ameren. ***Sadly, KCPL knows that this position is not true and is simply attempting to mislead the Commission***.

In a data request, KCPL was asked to "[e]xplain Ms. Hardesty's understanding of whether or not Ameren Missouri was, in fact, in a NOL position in its 2012 rate case test year." In its response, and directly contrary to its current misrepresentations to the Commission, KCPL admitted that it "did understand that Ameren Missouri had NOL carryforward in its 2012 rate case."[168]

Further, Mr. Brosch points out that, based upon his own experience in that Ameren proceeding, Ameren had a NOL carryforward and was in an identical position to KCPL in this case.

> I can state from personal involvement in Case No. ER-2012-0166, that Ameren Missouri's rate base included significant Net Operating Loss deferred tax asset amounts, as an increase to rate base within the same test year the CWIP-related ADIT amounts were disputed. . . . It should be noted that, under essentially the same facts as those occurring in this case, Ameren Missouri's own witness did not argue Ms. Hardesty's view that Ameren Missouri NOL position had any bearing upon the proper rate base treatment of CWIP-related ADIT balances.[169]

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[167] KCPL Initial Brief, page 129 ("KCP&L generated a NOL during the period that the assets were in CWIP and it has not and will not receive a cash tax benefit related to the tax basis differences related to CWIP in this case.").
[168] Exhibit 504, Brosch Surrebuttal, page 6 (referring to Schedule MLB-24 (citing to Data Request 15-47a).
[169] *Id.* at page 6.

Putting aside KCPL's lack of candor with the Commission, it is apparent that the existence of KCPL's NOL makes it even more essential for the Commission to reflect the Company's CWIP-related ADIT liability balance in rate base. Specifically, contrary to KCPL's current claims, the amount of the Company's NOL is larger as a direct result of CWIP-related income tax deductions relate to the CWIP-related ADIT amounts that must, therefore, reduce KCPL's rate base.

> The Company's NOL is the result of its negative taxable income in certain prior tax years, after accounting for all of KCPL's current taxable revenues and deductions, including the deductions arising from self-constructed assets. Some of these assets were not yet in service and were recorded within CWIP accounts at test year-end. ***Thus, the recorded NOL deferred tax balance that has been included by KCPL to increase rate base is larger than it would be in the absence of the CWIP related income tax deductions that contributed to such tax losses***. To be consistent, if the Company intends to consider CWIP-related ADIT as not rate base includable, it would need to also reduce its NOL deferred tax asset that is included in rate base by an offsetting amount, to recognize and eliminate the impact of CWIP related tax deductions that contributed to the Company's tax losses. It is inequitable for KCPL to exclude these CWIP-ADIT balances at the same time the related CWIP-ADIT tax deductions have increased the NOL deferred tax asset that KCPL has included in rate base. This essential matching of tax deductions and their ADIT balances with NOL offsets is not accomplished under the Company's approach.[170]

In the final analysis, it is apparent that KCPL receives a return, through AFUDC, on its construction projects before they are completed and placed into service. Given this return, ratepayers are entitled to recognition of the CWIP-related ADIT asset balance in rate base. The Commission has previously adopted the logic of this position in a previous Ameren case. Contrary to KCPL's current misrepresentations, KCPL and Ameren were in identical positions regarding the existence of an NOL deferred tax asset. Given the

[170] *Id.* at page 4.

identical facts, the Commission should again apply the logic of its previous Ameren decision.

B. 1KC PLACE LEASE ADIT

Unlike the CWIP-related ADIT liability balance, in which KCPL seeks to exclude from rate base, in this issue KCPL seeks to include an ADIT assetbalance in rate base. Not surprisingly, in both instances, KCPL's position increases rate base and revenue requirement.

In its Initial Brief, MECG explained that, under its headquarters lease, certain rent payments are abated until some point in the future even though such deferred payment amounts must be accrued as expenses. The income tax deduction for rent is limited to amounts paid and this lower amount of currently deductible rent will result in a temporarily higher level of currently payable income taxes. On the other hand, KCPL will pay the higher amount of rent in the later years of the lease that is recognized as an accrued expense on the books. At that future point in time, this higher amount of rent will drive larger business expense deductions and a lower amount of currently payable income taxes. The timing difference that occurs when "tax deductibility for expenses is subsequent to the book recognition of the expense" results in an ADIT asset.[171]

In this situation, KCPL seeks to include the ADIT asset in rate base and inflate its revenue requirement. As MECG explains, however, while KCPL proposes to include the ADIT asset item in order to increase rate base, KCPL has failed to recognize the corresponding accrued lease liability balance that would reduce rate base if recognized.[172]

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[171] *Id.* at page 47.
[172] MECG Initial Brief, page 109.

In its Initial Brief, KCPL admits that it has included the ADIT asset balance in rate base and has failed to include the offsetting accrued liability for deferred rent payments.[173] KCPL erroneously suggests that its failure to include the offsetting accrued liability is appropriate "because the accrued liability is being amortized monthly as a reduction to rent expense in cost of service."[174] KCPL wrongly postulates that the amortization of the liability that is "included in KCP&L's lead lag computation of cash working capital"[175] somehow has the effect of rate base accounting for deferred rent liabilities.

MECG anticipated KCPL's misplaced argument.[176] ***First***, as MECG points out, and KCPL admits, the reflection of this accrued liability in rate base through cash working capital "is not financial [sic] equivalent to fully including the 1KC liability in rate base."[177]

Second, putting aside KCPL's admission that cash working capital recognition of the accrued liability would not be "financially equivalent" to including the liability in rate base, Mr. Brosch also points out that KCPL's contention is inherently illogical and produces a result entirely contrary to that suggested by KCPL. As Mr. Brosch points out, "the effect of including a reduced expense on the "Cash Vouchers" line of the Company's lead lag study would actually increase rate base, producing a result completely inconsistent with recognition of deferred lease payment liabilities that would reduce rate base if recognized."[178]

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[173] KCPL Initial Brief, page 131.
[174] *Id.*
[175] *Id*.
[176] MECG Initial Brief, pages 109-110.
[177] Exhibit 504, Brosch Surrebuttal, page 9.
[178] *Id.*

Recognizing that KCPL has not yet paid the abated rent associated with its lease of 1KC Place and has not reduced rate base to recognize the accrued liability for higher future rent payments, it should not be allowed to increase rate base associated with the ADIT asset balance that is created. Rather, any ADIT asset balance included in rate base should also include the accrued liability balance in order to maintain the proper matching and protect the ratepayers from inflated rates. As such, MECG urges the Commission to adopt Mr. Brosch's ADIT-1KC Place adjustment.

C. ACCRUED EMPLOYEE COMPENSATION ADIT

Like many companies, KCPL provides certain deferred compensation benefits to its employees. Accrual accounting under GAAP requires KCPL to recognize the liability for payment of this future compensation on its books. On the other hand, tax accounting does not recognize this accrued expense as tax deductible until the compensation is actually paid at a future date. Again, this situation where "tax deductibility for expenses is subsequent to the book recognition of the expense" resulting an ADIT asset balance.[179]

As with the 1KC Place ADIT asset balance, KCPL seeks to include the accrued employee compensation ADIT asset balance in rate base. Noticeably, however, KCPL does not include the offsetting accrued liability. As a result, KCPL's rate base is inflated and revenue requirement increased.

Again, KCPL erroneously attempts to justify its failure to include the offsetting accrued liability on the alleged basis that this liability is amortized and flowed through "the overall cash working capital computations."[180] As with the 1KC Place ADIT balance, MECG anticipated KCPL's misplaced argument already.

[179] *Id.* at page 47.
[180] KCPL Initial Brief, page 132.

In data request responses, KCPL admits that including this accrued liability in rate base through cash working capital "is not financially equivalent to fully including the bonus and deferred compensation liabilities in rate base."[181] As with the 1KC Place ADIT asset, KCPL's suggestion that it has recognized this liability through its cash working capital study is inherently illogical and produces a result entirely contrary to that suggested by KCPL.

Recognizing that KCPL has not yet paid the deferred compensation and has not reduced rate base to recognize the accrued liability for higher future compensation payments, it should not be allowed to increase rate base by including the corresponding ADIT asset balance that is created. Rather, any ADIT asset balance included in rate base should also include the accrued liability balance in order to maintain the proper matching and protect the ratepayers from inflated rates. As such, MECG urges the Commission to adopt Mr. Brosch's ADIT-accrued employee compensation adjustment.

D. NET OPERATING TAX LOSSES

In its Initial Brief, MECG pointed out that KCPL has executed a Tax Allocation Agreement ("TAA") with its affiliates that causes it, through the allocation of consolidated income tax Net Operating Losses, to pay an increased share of consolidated income taxes than it would otherwise pay absent the TAA. In complete candor, MECG pointed out that the Commission has recently ruled regarding the appropriateness of Ameren's Tax Allocation Agreement. There, the Commission approved rate case recognition of Ameren's TAA because: (1) there was no evidence to show that the Agreement was structured so as to be detrimental to Ameren Missouri and (2) Ameren Missouri ratepayers had previously benefited because of the Agreement.

[181] Exhibit 504, Brosch Surrebuttal, page 11.

> There is no evidence in this case to show that Ameren's Tax Allocation Agreement is structured in a way that would be detrimental to Ameren Missouri and its ratepayers. Instead, for several years, Ameren Missouri's ratepayers benefited from a lower rate base because of the Tax Allocation Agreement. The Tax Allocation Agreement has not changed, but in more recent years ratepayers have not benefitted from that agreement, although that may change again in the future. That fluctuation does not mean the agreement is unreasonable, and there is no evidence the fluctuation was intentionally created in order to change who benefits from the Tax Allocation Agreement.[182]

As MECG demonstrates, however, the circumstances that led to the Commission's acceptance of the Ameren Tax Allocation Agreement are not present in this case. Specifically, unlike the Ameren agreement, the Great Plains Energy TAA is inherently and persistently detrimental to KCPL and its ratepayers. Furthermore, unlike the previous Ameren case, KCPL ratepayers have never benefitted under the Great Plains Energy TAA and, given KCPL's own admissions and financial forecasts, are not anticipated to benefit from that affiliate agreement in future years. Given the persistent and detrimental nature of the Great Plains Tax Allocation Agreement, MECG urges the Commission to calculate KCPL's Net Operating Tax Losses on a stand-alone basis.

In its Initial Brief, KCPL attempts to divert the Commission's attention from the persistent and detrimental nature of the Great Plains Tax Allocation Agreement. Instead, holding out the false hope of future benefits to its ratepayers, KCPL claims that "it is the nature of a consolidated filing that any given member may be better off in some years as a result of consolidated filing and worse off in other years."[183] KCPL fails to inform the Commission that, as it has admitted in data request responses, KCPL ratepayers have never been "better off" under the Great Plains Tax Allocation Agreement.

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[182] Report and Order, Union Electric Company d/b/a Ameren Missouri, April 29, 2015, page 21.
[183] KCPL Initial Brief, page 133.

> In every prior year, KCPL has received no benefit from participation in the Great Plains Energy consolidated tax group under the TAA. This fact is conceded by Ms. Hardesty in her response to MECG data request 15-51. In responding to MECG Data Request 15-53, the Company again confirmed, "KCPL has not received any extra benefit by filing consolidated [returns] with Great Plains Energy since the GPE TAA was signed in 2008.[184]

In fact, contrary to KCPL's offer of false hope, KCPL ratepayers are not expected to benefit from that agreement in the future.

> This is a major distinction, in comparison to the Ameren Missouri situation, where the Ameren TAA over time has produced a mix of historical benefits in some years and detriments to Ameren Missouri in other years, with results that could switch back and forth in the future. In fact, in response to MECG Data Request 15-53(d), Ms. Hardesty stated, ***"[w]e only have financial projections for 2015-2019, and we do not expect KCPL to see a benefit by filing with the consolidated group during this period.***"[185]

Finally, MECG has shown, as requested by the Commission in its Ameren decision, that the Great Plains Tax Allocation Agreement is "inherently detrimental to KCPL and its ratepayers."

> The Great Plains TAA is structured to combine the tax attributes of Great Plain's **____**, with the utility businesses that have experienced tax losses only rarely historically and should remain profitable in future years if bonus depreciation is not extended past 2014, when it expired under current tax law. ***This structure causes the Great Plains utility businesses to systematically subsidize the holding company and non-utility businesses, by providing taxable income to accelerate the tax benefit realization of non-utility losses while any non-utility losses may displace or delay the realization of utility tax credits and utility NOLs***. In contrast, the Ameren TAA, that was addressed by the Commission in Case No. ER-2014-0258, was favorable to Ameren Missouri ratepayers in the years 2008 through 2012, when it served to accelerate the realization of utility NOL benefits by combining such utility losses with positive taxable income from Ameren Corporation's non-regulated generating and energy marketing businesses.[186]

[184] Exhibit 504, Brosch Surrebuttal, page 15 (citing to Schedule MLB-25).
[185] *Id.* at page 16 and Schedule MLB-25 (citing to KCPL Response to MECG question 15-53(d).
[186] Exhibit 504, Brosch Surrebuttal, page 17.

Given that KCPL ratepayers are harmed by the detrimental Great Plains Energy TAA, have never benefitted from that affiliate agreement and are not projected to benefit from that agreement, MECG urges the Commission to protect the ratepayers from the harms that befall them from this unreasonable affiliate agreement. Specifically, MECG urges the Commission to adopt the adjustment proposed by Mr. Brosch.

X. CLASS COST OF SERVICE / RATE DESIGN

In its Initial Brief, MECG noted that a Non-Unanimous Stipulation had been filed on June 16 that resolved Class Cost of Service, Revenue Allocation and the LP / LGS rate design issue. Shortly after the filing of the stipulation, KCPL objected on the basis that the LP / LGS rate design could lead to a revenue shortage as a result of potential customer migration. As indicated at the true-up hearing, KCPL and Staff reached a settlement designed to compensation for this potential lost revenue. A Non-Unanimous Stipulation addressing resolution was filed on August 3, 2015.[187] As KCPL has indicated, with the approval of that rate migration settlement, it no longer opposes the June 16 Class Cost of Service / Revenue Allocation and LP / LGS rate design issues. As such, MECG urges the Commission to approve the now Unanimous June 16 stipulation as well as the August 3 settlement. Specifically, consistent with the June 16 settlement, the Commission does not need to make specific findings regarding the appropriateness of a particular fixed production cost allocation methodology or the most reasonable class cost of service study. Instead, since it is consistent with the positions of multiple parties, the Commission may simply find that any revenue increase should be allocated on an equal percentage basis across all customer classes.

[187] Ideally, the rate migration settlement amount would have been included in the June 16, 2015 settlement. Inexplicably, despite being aware of the LP / LGS rate design proposal since April 16, 2015, KCPL never raised any concern regarding a concern with customer migration. Instead, KCPL waited until the evidentiary hearing to raise this concern. Had KCPL addressed issues in a timely fashion and not waited until the 11th hour to raise its concerns, then the resolution contained in the August 3 settlement could have been incorporated in the June 16 settlement.

XI. TRUE-UP ISSUES

In an effort to mitigate the regulatory lag faced by utilities, Staff and consumers agreed to the use of a true-up audit. Under this proposal, plant, revenues and costs are brought forward to a more recent date. Importantly, as required by the Court of Appeals, the audit is comprehensive in order to preserve the matching of investment, revenues and expenses.[188] In most instances, this reduces regulatory lag to about 4 months. For instance, in this case, several items were trued-up through May 31, 2015. Recognizing that rates are likely to go into effect simultaneous with the end of the suspension period of the original tariffs (September 29, 2015), regulatory lag is reduced to slightly less than 4 months.

Ever the opportunist (at the expense of their ratepayers), and not satisfied with an 83% rate increase over the course of nine years, KCPL seeks to violate the true-up process. Specifically, KCPL seeks to violate the matching process and make several isolated adjustments designed to further inflate its revenue requirement. Noticeably, while KCPL seeks to make isolated adjustments for bills not expected to be received until September 2015, KCPL ignores any offsetting adjustments. Specifically, KCPL seeks to include these isolated cost increases while failing to propose offsetting adjustments for retail and wholesale revenue growth.

This is not the first time that KCPL has made such proposals. In 2006, KCPL asked that it be allowed to include a payroll increase that was proposed to occur well after the true-up date. As here, KCPL failed to propose any offsetting adjustments to maintain the matching of investment, revenues and expenses. There, the Commission expressly rejected KCPL's one-sided adjustment.

[188] *State ex rel. GTE North, Inc. v. Public Service Commission*, 835 S.W.2d 356 (Mo.App. 1992).

> The Commission finds that the competent and substantial evidence supports Staff's position, and finds this issue in favor of Staff. The Commission agrees with Staff that it is important to match revenues and expenses as of a date certain. As Staff points out, should the Commission accept KCPL's 113 employees in cost of service, then the Commission would also need to insert additional revenue from customer growth occurring after the known and measurable date of June 30.
>
> If the Commission does not take a snapshot of a company's revenues and expenses as of the known and measurable date, the true-up date, or any date, for that matter, then what? KCPL's employee count, as well as a host of other revenues and expenses, has no doubt changed since the true-up hearing; the Commission will get yet another snapshot of those changes when KCPL files its next rate case. To set just and reasonable rates, the Commission simply must match revenues and expenses as of a certain date.[189]

In this case, Staff has performed a thorough true-up audit of KCPL's operations that include a proper matching of investment, revenues and expenses. In fact, recognizing the importance of the true-up date, Staff did not propose an adjustment to include the increased revenue associated with a capacity agreement that became effective in July.[190] Undoubtedly, there are further adjustments that would reduce revenue requirement, but given the sanctity of the true-up date, Staff did not consider such a review.[191]

The Commission should adopt the logic of its previous decision as well as that set forth by the Staff. Specifically the Commission should reject KCPL's attempts to violate the matching concept and the true-up date.

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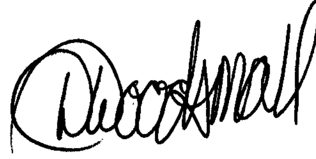
[189] Case No. ER-2006-0314, *Report and Order*, issued December 21, 2006, at pages 71-72.
[190] Tr. 2057.
[191] Tr. 2057-2058.

Respectfully submitted,

WOODSMALL LAW OFFICE



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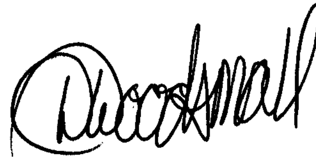
ATTORNEYS FOR MIDWEST ENERGY CONSUMERS GROUP

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that I have this day served the foregoing pleading by email, facsimile or First Class United States Mail to all parties by their attorneys of record as provided by the Secretary of the Commission.



David L. Woodsmall

Dated: August 3, 2015