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MISSOURI PUBLIC SERVICE COMMISSION

UTILITY SERVICES DEPARTMENT

REBUTTAL TESTIMONY

OF

ZEPHANIA MAREVANGEPO

KCP&L GREATER MISSOURI OPERATIONS COMPANY

FILE NO. EO-2012-0009

Jefferson City, Missouri
March 2012

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

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2	OF	
3	ZEPHANIA MAREVANGEPO	
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5	FILE NO. EO-2012-0009	
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1 This designation is awarded based upon experience and successful completion of a written
2 examination, which I completed during my attendance at a SURFA conference in April of 2008.

3 Q. Have you filed testimony in other cases before this Commission?

4 A. Yes. Please see Schedule 1.

5 Q. Have you made recommendations in any other cases before this Commission?

6 A. Yes, I have made recommendations on finance cases, acquisition cases, small
7 water and sewer rate cases, and telephone certificate cases before this Commission.

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

9 A. To respond to portions of the direct testimony of Tim M. Rush and
10 Kevin E. Bryant, witnesses for KCP&L Greater Missouri Operations Company (“GMO”).
11 Specifically, I address the testimony of each witness regarding the (1) projected impact of the
12 incentive component of the demand-side investment mechanism (DSIM) GMO proposes on
13 certain credit ratios, (2) a general discussion of the projected impact of the utility incentive
14 component of the DSIM programs on business risk for purposes of setting the Company’s
15 allowed return on equity (ROE) in the current and/ or future rate cases and (3) a quantification of
16 GMO’s proposed performance incentive component of the DSIM; and Staff’s proposed
17 performance incentive component of the DSIM, as sponsored in the rebuttal testimony of Staff
18 expert witness John A. Rogers, in terms of basis points of an allowed ROE in GMO’s last
19 rate case, Case No. ER-2010-0356.

20 **DSIM DEFINITION AND PORTIONS OF THE INCENTIVE COMPONENT OF THE DSIM**

21 Q. What is your understanding of a DSIM?

22 A. Rule 4 CSR 240-3.163(1)(F) defines DSIM as:

(F) Demand-side programs investment mechanism, or DSIM, means a mechanism approved by the commission in a utility's filing for demand-side program approval to encourage investments in demand-side programs. The DSIM may include, in combination and without limitation:

1. Cost recovery of demand-side program costs through capitalization of investments in demand-side programs;
2. Cost recovery of demand-side program costs through a demand-side program cost tracker;
3. Accelerated depreciation on demand-side investments;
4. Recovery of lost revenues; and
5. Utility incentive based on the achieved performance level of approved demand-side programs;

Q. What is your understanding of a "utility incentive" as contemplated under Rule 4 CSR 240-3.163(1) (F)?

A. Utility incentive is one of the five components of a DSIM, which the Commission may approve, in combination and without limitation, designed to encourage investments in demand-side programs. It is based on the achieved performance level of approved demand-side programs.¹

Q. What is the incentive component of GMO's proposed DSIM?

A. On page 16, lines 9-10, of Tim Rush's direct testimony, he indicates that the incentive mechanism of GMO's proposed DSIM is comprised of two portions: (1) a portion of annual shared benefits (12 percent of benefits to be recovered over the first three years)² and (2) a performance award (performance bonus).³

Q. Did Mr. Rush provide information concerning the impact of GMO's DSIM proposal upon the Company's credit metrics?

¹ Code of State Regulations, 4 CSR 240-3.163 (1) (F)5.

² Tim Rush's direct testimony, page 17, lines 4-6 [12%*present value of (energy + capacity benefits)].

³ Tim Rush's direct testimony, page 20, the performance incentive table at lines 1-5

1 A. Yes, Mr. Rush provided this information under several scenarios at
2 Schedule TMR-5 attached to his direct testimony.

3 Q. Did Mr. Rush provide a scenario that considers the entire incentive component
4 of GMO's proposed DSIM when analyzing its potential impact on GMO's projected key
5 credit metrics?

6 A. No. Mr. Rush's "with an incentive" scenario does not include the performance
7 bonus because he only addressed the first three years of the DSM programs. The performance
8 bonus would not be received until the fourth year. Staff understands that beginning in the
9 fourth year under its proposed DSIM, GMO can receive up to an additional \$4 million from
10 ratepayers after it has already received the 12 percent of shared benefits component of the DSIM.
11 Although Mr. Rush only provided three years of data, this additional cash flow would obviously
12 boost GMO's cash flows and earnings in the fourth year and beyond.

13 Q. What are the "key credit metrics" Mr. Rush refers to on page 25, lines 9-12, of his
14 direct testimony?

15 A. The "key credit metrics," Mr. Rush refers to in his direct testimony, are financial
16 ratios that are routinely assessed by rating agencies (in this case, specifically Standard & Poor's)
17 when evaluating or assigning credit ratings. They include, but are not limited to, the following:
18 (1) Debt to Total Capitalization, (2) Funds From Operations (FFO) to Total Debt and (3) FFO to
19 Interest Coverage.

20 **PROJECTED IMPACT OF THE INCENTIVE COMPONENT OF THE DSIM ON CREDIT**
21 **METRICS**

22 Q. What did you analyze in order to assess the projected impact of the incentive
23 component of GMO's proposed DSIM on GMO's credit metrics?

1 A. I evaluated scenarios in Schedule TMR-5 attached to Mr. Rush's direct testimony.
2 The schedule presents scenarios that show the impact of GMO's proposed DSIM with the
3 proposed incentive,⁴ and GMO's proposed DSIM without the proposed incentive on the
4 "key credit metrics."

5 Q. Did you independently investigate the reasonableness of the operational and
6 financial inputs (e.g., projected sales growth before and after DSM programs) of the credit
7 metrics discussed in Mr. Rush's testimony?

8 A. No. I did not independently verify the reasonableness of the inputs used to
9 compute the figures shown in the credit metric calculations in Mr. Rush's Schedule TMR-5.
10 Although Staff has not adjusted any financial figures in the credit metric calculations,
11 Staff considers Mr. Rush's interest rate assumption of ** ** per year to be
12 unreasonable, given the prevailing low interest rate environment. Staff also notes, in Scenario 2
13 ("without incentive"), Mr. Rush assumes GMO will issue debt to make itself whole for the
14 "lost margins," which is illogical as capital is usually issued for capital investment rather than to
15 make up for reduced cash flows.

16 Q. Regardless of the assumption of issuing any capital to make up for lost margins, is
17 it appropriate to assume that only debt would be issued if the purpose of these calculations is to
18 show the possible impact of recovery of lost margins on the "key credit metrics"?

19 A. No. For purposes of this illustration, the Company should assume maintaining a
20 balanced capital structure in the long-term, which requires the assumption that equity would be
21 issued in proportion to its current capital structure. However, given the *de minimis* amount
22 _____

⁴ GMO's DSIM proposal requests recovery of shared benefits contemporaneously based on projections, whereas the Staff proposes recovery of shared benefits retrospectively. The proposed recovery mechanism is fully discussed in Staff expert witness' testimony – Mark L. Oligschlaeger.

of debt Mr. Rush assumed under Scenario 2, GMO's illogical assumption is not of major concern to Staff.

Q. What are the scenarios Mr. Rush presented in Schedule TMR-5 attached to his direct testimony?

A. The first two tables (*Scenarios 1 and 2*) below, obtained from Schedule TMR-5, show the quantitative impact of the incentive component of the DSIM on GMO's key credit metrics. The third table only shows Standard & Poor's (S&P) description of GMO's current financial risk profile⁵.

**

Scenario 1 (With an incentive)

[illegible]

Scenario 2 (Without an incentive)

[illegible]

S&P Financial Benchmarks⁶

_____ _____		
_____	_____	_____
_____	_____	_____

**

⁵ Source: S&P credit portal – S&P rating service bases its rating on GMO on the consolidated credit profile its parent company, Great Plains Energy Inc.

⁶ May 27, 2009, Table 2, S&P, Criteria Methodology: Business Risk/ Financial Risk Matrix Expanded

1 Q. Would you please explain the impact on GMO's credit metrics as represented by
2 the ratios in the tables above?

3 A. Yes.

4 In Scenario 1 (With an incentive): There is no impact.

5 Mr. Rush assumes GMO invests in DSM programs and recovers costs based on its proposed
6 DSIM. While Staff is not taking issue with the percentage of benefits GMO proposes to recover
7 from ratepayers, Staff does take issue with GMO's request for contemporaneous recovery of
8 projected benefits. Staff witness Mark L. Oligschlaeger presents Staff's position on this issue in
9 his rebuttal testimony.

10 In Scenario 2 (Without an incentive): Impact is insignificant.

11 Mr. Rush assumes that GMO invests in DSM programs, but does not receive any portion of the
12 projected benefits. Based on the three-year projections provided, the impact is not significant
13 enough to cause Great Plains Energy's (GPE, GMO's parent company) FFO to Debt ratio to fall
14 outside the benchmarks for S&P's Credit Descriptor of "Aggressive." GPE's Debt to Total
15 Capital ratio also currently falls within the benchmark for the "Aggressive" Credit Descriptor.
16 This would not change even with Mr. Rush's assumption that debt is issued to fund lost margins.

17 **IMPACT ON CREDIT QUALITY AND BUSINESS RISK**

18 Q. What is business risk?

19 A. Business risk is the uncertainty in the expected return caused by a firm's industry-
20 specific factors, as well as company-specific factors.

21 Q. Do lower credit metrics imply additional business risk?

22 A. Not necessarily.

23 Q. What would imply additional business risk?

1 A. Business risk is a combination of quantitative and qualitative factors some of
2 which may vary from one company to another. Rating agencies, such as S&P and Moody's, do
3 not depend on the absolute value of credit metrics when assessing a company's business risk.
4 For instance, the categories underlying S&P's business risk assessment are: (1) Country risk,
5 (2) Industry risk, (3) Competitive risk and (4) Profitability/ Peer group comparisons. Moody's
6 overall analysis of electric and gas utilities focuses on the following factors: (1) Regulatory
7 Framework, (2) Ability to Recover Costs and Returns, (3) Diversification and (4) Financial
8 Strength and Liquidity. All of these factors affect the volatility of the cash flow available for
9 payment of fixed obligations. If there is less volatility, there is less business risk.

10 Q. Does the financial information Staff obtained from GMO allow Staff to quantify
11 the long-term potential change in business risk caused by GMO's proposed DSIM?

12 A. No. The business risk of a company is embedded in the volatility of its cash
13 flows, assuming constant financial risk. Therefore, to provide a logical opinion of the potential
14 impact of proposed DSIM, Staff would need to evaluate GMO's cash flows, under both
15 scenarios, "with an incentive" and "without an incentive," for the 15-year period GMO used to
16 evaluate proposed DSM programs. GMO did not provide this information. The information
17 provided is limited to three years.

18 Q. Did Staff request this information from the Company?

19 A. Yes. In its response to Staff Data Request No. 17 GMO indicates that the
20 Missouri Energy Efficiency Investment Act (MEEIA) filing requirements do not specifically
21 require it to provide such financial projections, that GMO has not conducted the analysis and that
22 GMO does not have information available to do so.

1 Furthermore, Mr. Rush represented during a technical conference on March 8, 2012, that
2 a 15-year “without an incentive” scenario would not be as simple as eliminating cash flows
3 anticipated in the “with an incentive” scenario. He indicated that certain complex and uncertain
4 assumptions and adjustments would need to be made to account for different ratemaking
5 treatment than what is contemplated under its DSIM proposal.

6 Q. Has GMO provided Staff any qualitative information that indicates other possible
7 factors that may impact the Company’s “key credit metrics” and business risk?

8 A. Yes. On page 5, lines 7-10, of his direct testimony, Mr. Bryant states that the
9 current mechanism takes a “rearview mirror approach,” which delays recovery of DSM costs and
10 then only allows recovery of program costs; and on page 7, lines 19-20, Mr. Bryant states that
11 the current mechanism has a negative impact on the company’s “key credit metrics” such as FFO
12 to debt. In paragraph three (3) of the Company’s response to Staff Data Request No. 15, the
13 Company states that the “rearview mirror approach” increases business risk.

14 Q. On page 8, lines 11-15, of his direct testimony, Mr. Bryant indicates that the
15 current recovery mechanism discourages investors “causing investors to discount the Company’s
16 stock price and raising the cost of equity.” Did the company quantify the amount by which the
17 Company’s stock price has been discounted?

18 A. No. In response to Staff Data Request No. 19, the Company stated that it is not
19 possible to quantify the specific impact.

20 Q. Then it did not quantify the impact on its cost of equity either, did it?

21 A. It did not.

1 Q. Do you agree from a conceptual perspective that, if anything, GMO's proposed
2 prospective recovery of the incentive component would more likely be viewed as a slight
3 reduction in business risk and cost of equity?

4 A. Yes.

5 Q. What cost recovery mechanism, for the incentive component of the DSIM, is
6 contemplated by the MEEIA rules?

7 A. Retrospective cost recovery approach. Rule 4 CSR 240-20.093(2) (H) 3 states:

8 Any utility incentive component of a DSIM shall be
9 implemented on a retrospective basis and all energy and
10 demand savings used to determine a DSIM utility incentive
11 revenue requirement must be measured and verified
12 through EM&V.

13 Q. Did the Commission order the retrospective cost recovery approach in GMO's
14 last rate case, Case No. ER-2010-0356?

15 A. Yes.

16 Q. Did the Commission make any specific adjustments to GMO's allowed ROE for
17 the retrospective cost recovery approach in this most recent rate case?

18 A. No.

19 Q. Then what does this imply about any consideration the Commission should give
20 to GMO's allowed ROE if the Commission approves GMO's proposed DSIM?

21 A. Although the Staff is not proposing any specific reduction at this time, if
22 anything, GMO's allowed ROE should be lowered.

23 Q. Business risk aside, does the proposed incentive mechanism have enough of
24 an impact on the credit metrics over the next three years to cause GMO's credit rating to
25 be downgraded?

A. No. Most importantly, Staff concludes that GMO's 3-year projected credit metrics are at adequate levels and that the modest cash outflow impacts associated with GMO's proposed DSM programs will not threaten GMO's parent company's (Great Plain Energy) credit status.

QUANTIFICATION OF GMO AND STAFF'S PROPOSED PERFORMANCE INCENTIVE

Q. Does GMO request an additional performance "bonus" in its DSIM?

A. Yes. Mr. Rush discusses this on page 19, line 3, through page 20, line 23 of his rebuttal testimony.

Q. Do you know how Mr. Rush determined that possible bonuses from \$0 to \$4 million are appropriate additional incentives for GMO's proposed DSIM?

A. No.

Q. What is the impact on GMO's allowed ROE of allowing a \$2 million, \$3 million and \$4 million performance incentive component?

A. Table 1 below shows GMO's performance incentive component impact on ROE.

Table 1

ROE Impact based on GMO's performance incentive component structure

Performance bonus impact on after-tax allowed ROE			
Bonus	% Impact on ROE	ROE before Bonus	ROE with Bonus
2 Million	0.15%	10.00%	10.15%
3 Million	0.23%	10.00%	10.23%
4 Million	0.30%	10.00%	10.30%

Source: 10% ROE is from GMO's last rate case, ER-2010-0356, Report and Order, 5-4-11

Q. Does Staff believe the Commission should adopt GMO's proposed structure for the performance incentive component of GMO's proposed DSIM?

A. No. On page 46, of Staff expert witness' John A. Rogers' rebuttal testimony, he presents Staff's proposed performance incentive component structure. On pages 43-47, Mr. Rogers explains why the Commission should adopt Staff's proposed performance incentive component structure and reject GMO's structure.

Q. Would you please present the projected impact on the after-tax allowed ROE if the Commission were to adopt Staff's proposed performance incentive component structure?

A. Yes. Please see Table 2 below:

Table 2

ROE impact based on Staff's performance incentive component structure

Performance bonus impact on after-tax allowed ROE			
Bonus	% Impact	ROE before Bonus	ROE after Bonus
\$1 million	0.08%	10.00%	10.08%
\$1.3 million	0.10%	10.00%	10.10%
\$1.6 million	0.12%	10.00%	10.12%
\$1.9 million	0.14%	10.00%	10.14%
\$2.2 million	0.17%	10.00%	10.17%
\$2.5 million	0.19%	10.00%	10.19%
\$3.3 million	0.25%	10.00%	10.25%

Although the performance incentive may allow GMO to earn an ROE that may ultimately be higher than an allowed ROE determined in a rate case, as explained by Staff witness Rogers, this consideration is consistent with the intent of the MEEIA rules to incentivize investment in demand-side programs.

Q. Does this conclude your rebuttal testimony?

A. Yes.

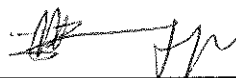
BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

In the Matter of KCP&L Greater Missouri)
Operations Company's Notice of Intent to) File No. EO-2012-0009
File an Application for Authority to)
Establish a Demand-Side Programs)
Investment Mechanism)

AFFIDAVIT OF ZEPHANIA MAREVANGEPO

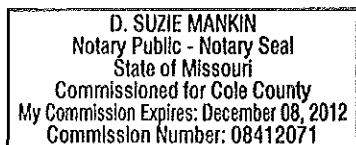
STATE OF MISSOURI)
) ss.
COUNTY OF COLE)

Zephania Marevangpo, of lawful age, on his oath states: that he has participated in the preparation of the foregoing Rebuttal Testimony in question and answer form, consisting of 12 pages to be presented in the above case; that the answers in the foregoing Rebuttal Testimony were given by him; that he has knowledge of the matters set forth in such answers; and that such matters are true and correct to the best of his knowledge and belief.



Zephania Marevangpo

Subscribed and sworn to before me this 20th day of March, 2012.




Notary Public

SUMMARY OF CASE PARTICIPATION

ZEPHANIA MAREVANGEPO

Date Filed	Issue	Case Number	Exhibit	Case Name
08/08/2011	Rate of Return	HR-2011-0241	Cost of Service Report	Veolia Energy Kansas City, Inc.
11/08/2010	Rate of Return	GR-2010-0363	Cost of Service Report	Union Electric Company d/b/a AmerenUE
07/20/2010	Rate of Return	GR-2010-0171	Surrebuttal	Laclede Gas Company
06/24/2010	Rate of Return	GR-2010-0171	Rebuttal	Laclede Gas Company
06/04/2010	Rate of Return/ Cost of Capital	GR-2010-0192	Cost of Service Report	Atmos Energy Corporation
05/24/2010	Rate of Return/ Cost of Capital	GR-2010-0171	Cost of Service Report	Laclede Gas Company
03/16/2010	Finance Case	GR-2009-0450	Rebuttal	Laclede Gas Company
02/23/2010	Finance Case	GR-2009-0450	Direct	Laclede Gas Company