BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

In the Matter of the Application of Kansas City Power and Light Company for Approval to Make Certain Changes in its Charges for Electric Service to Begin the Implementation of Its Regulatory Plan.	)))))	**Case No. ER-2006-0314**

PREHEARING BRIEF OF
KANSAS CITY POWER & LIGHT COMPANY

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Kansas City Power & Light Company ("KCPL" or "Company") respectfully submits its Prehearing Brief in accordance with the Commission's Order Setting Procedural Schedule issued on March 29, 2006. Pursuant to the March 29, 2006 Order, KCPL will address the list of issues filed by the parties on October 6, 2006.

I. STATEMENT OF THE CASE

Fulfilling the commitments that it made in the Regulatory Plan approved by the Commission as part of the 2005 Stipulation and Agreement ("Stipulation"),[1] Kansas City Power & Light Co. ("KCPL" or "Company") has embarked upon a series of infrastructure and customer enhancement projects valued at $1.3 billion. In this first of a series of four rate cases provided for by the Stipulation, KCPL seeks a Commission decision that appropriately reflects the risks that the Company has undertaken in this endeavor, grants necessary increases in revenue, and sets a rate of return that will permit KCPL to remain financially healthy.

The critical task of the Commission is to fashion an order that correctly balances the risks with the benefits as they affect customers, shareholders and creditors. Two major factors, unique to KCPL among Missouri electric utilities, must be weighed by the Commission: (1) The Company's multi-million dollar construction projects, including the coal-fired Iatan 2 unit, new

[1] Report and Order, In re Proposed Regulatory Plan of Kansas City Power & Light Co., No. EO-2005-0329 (Mo. P.S.C., July 28, 2005).

wind generation, and numerous environmental upgrades, which will require KCPL to generate sufficient cash earnings to meet credit ratios; and (2) the risk and uncertainty of Off-System Sales which in recent years have accounted for approximately 50% of KCPL's earnings included in determining retail rates.

These two factors pose major risks to the Company. If not properly assessed by the Commission in this rate case, the sure result will be a financial downgrade to the Company which will trigger more uncertainty and greater costs, all to the detriment of customers. Given KCPL's exemplary record of performance over the past decade, the Company seeks a Return of Equity ("ROE") of 11.50% so that its history of top-of-the-industry productivity can continue.

The ROE should be set at this level to generate the necessary cash earnings for the Company, independent of other mechanisms like the Additional Amortizations permitted by the Stipulation. The Additional Amortizations (which act like accelerated depreciation, and therefore, an eventual off-set to rate base) are intended to be used as a last resort to maintain KCPL's credit ratios in the event that its earnings, as determined in general rate cases like this proceeding, fail to satisfy certain financial rations. See Stipulation, § III.B.1.i at 19.

Proper consideration of these facts and use of the tools provided in the Stipulation will lead to a decision that sets just and reasonable rates for the next twelve months, and that balances the risks of construction and the Off-System Sales market with the benefits to be gained from the Regulatory Plan.

II. ISSUES TO BE ADDRESSED

A. Revenue Requirement

1. Incentive Compensation

a. What amount, if any, of incentive compensation should be included in rates?

KCPL witness David Cross demonstrates that the use of incentive compensation is a powerful tool to ensure operational efficiency, which clearly serves the interests of utility customers. The use of financial measures is a very effective way to reflect performance on a broad range of customer service measures.

Staff witness Harris disallows performance base incentive compensation that is awarded on the basis of achieving financial goals that tie to earnings per share (EPS). KCPL believes that incentive compensation that is based on the financial goals tied to EPS is appropriate because a financially sound and stable company provides a direct benefit to all stakeholders including employees, customers, shareholders and the community in which it operates. In a regulated environment, growth in EPS is only achieved by managing costs which benefits the ratepayers and the shareholders.

Moreover, Staff ignored the fact that KCPL's incentive plan for 2006 has changed. EPS will continue to fund the non-officers' plan, but EPS has been eliminated as a specific score and plan goal. Using EPS as the funding mechanism simply means that KCPL must be profitable in order to pay an incentive. The scorecard goals focus on operational excellence, reliability, customer satisfaction and a commitment to KCPL's strategic intent.

2. <u>Pensions</u>

a. How should the expense and contributions relating to pension benefits for (1) Joint Partners and (2) the Supplemental Executive Retirement Plan (SERP) be accounted for in the tracking of the regulatory asset required by the Stipulation and Agreement in Case No. EO-2005-0329?

b. Should FAS 88 pension expenses be treated consistently with the KCPL application in this proceeding and its application for an AAO in Case No. EU-2006-0560?

KCPL understands that issues (a) and (b) no longer need to be resolved by the Commission as KCPL and Staff intend to file a stipulation and agreement that will address these issues.

3. <u>Hawthorn 5</u>

a. Should the insurance recoveries and lawsuit settlements related to the Hawthorn 5 explosion in 1999 have been accounted for differently?

As related in the rebuttal testimony of KCPL witness Lori Wright, KCPL is required to adopt the Federal Energy Regulatory Commission (FERC) Uniform System of Accounts (USofA). KCPL was required pursuant to US of A to treat insurance recoveries related to Hawthorn 5 property damage as salvage and record the recoveries to FERC Account 108, Accumulated Provision for Depreciation of Electric Utility Plant. Recording these recoveries as a reduction to gross plant, as advocated by Staff witness Williams, would have meant that KCPL would have been in violation of the USofA.

b. Is the AFUDC amount overstated as a result of the way that KCPL accounted for the insurance recoveries and lawsuit settlements related to the Hawthorn 5 explosion?

KCPL does not agree that AFUDC was overstated due to KCPL recording insurance proceeds in accordance with the USofA. The base used to calculate AFUDC represents the cost to construct the assets and that base is not overstated because the insurance recoveries were recorded in FERC account 108, Accumulated Provision for Depreciation of Electric Utility Plant as directed by the USofA. Had the insurance recoveries been recorded as a credit against the cost of construction as Staff asserts, the Company would have been in violation of a FERC directive.

c. Is the gross plant value of Hawthorne 5 overstated as a result of the way that KCPL accounted for the insurance recoveries and lawsuit settlements related to the Hawthorn 5 explosion?

No. As discussed in Wright's rebuttal testimony, the value of the assets placed in service related to the Hawthorn 5 rebuild represents the cost to construct those assets. The insurance recoveries were recorded in accordance with the USofA.

d. Should an adjustment be made to KCPL's books and records regarding the amount for AFUDC to fund the Hawthorn 5 reconstruction?

No. As explained earlier, the base used by KCPL to calculate AFUDC is consistent with the USofA as prescribed by FERC, so there is no need for such an adjustment.

4. Ice Storm Costs

a. What amount of the amortization of the costs associated with the 2002 ice storm should be included in rates?

KCPL believes the rates established in this proceeding should reflect an amortization expense related to the 2002 ice storm. KCPL was granted an AAO by the Commission to defer the ice storm costs ratably over the period September 2002 through January 2007.

5. EEI Dues

a. What amount of EEI dues should be included in rates?

KCPL is a dues paying member of many trade organizations, including the Edison Electric Institute (EEI). While a portion of the dues paid to EEI go to fund lobbying activities of EEI, KCPL as explained in the rebuttal testimony of KCPL witness Lori Wright, removed the lobbying portion of the dues from the amount it is seeking to recover in its cost of service. Staff's witness Williams adjustment does not recognize this fact.

6. Severance Costs

a. What amount, if any, of severance costs should be included in rates?

As with most large employers, KCPL incurs severance costs every year. KCPL is continually positioning its employees to better serve the company's needs, and as such, severance costs will continue in the future. KCPL believes a reasonable amount of severance costs should be included in its costs of service as it is an ongoing cost of providing service at an economical price. KCPL recommends a three-year average of certain severance costs to be included in its cost of service. This three-year average severance amount is representative of an ongoing level of severance costs. Staff witness Hyneman proposed to disallow all severance costs. Although KCPL's information demonstrates that it has incurred severance annually since 2001, Staff asserts severance costs are incurred on an irregular basis. Staff's adjustment does not recognize the ongoing nature of severance costs. Severance pay is a management tool and therefore KCPL believes an ongoing amount of severance costs should be included in rates.

7. Bad Debts

a. Should the bad debt percentage be applied to reflect the total revenues, including any rate increase in Missouri jurisdictional retail revenues awarded in this proceeding?

Yes. As explained by KCPL witness Lori Wright, KCPL determined its annualized bad debt expense by applying a bad debt write-off factor to test period revenue. See Wright Direct Testimony at 13. The bad debt write-off factor should be applied to the Missouri jurisdictional revenues awarded in this proceeding. Because bad debt is calculated as a percentage of revenue, any change in KCPL's revenue requirement will result in a corresponding change to KCPL's annualized bad debt expense. As summarized by KCPL witness Don A. Frerking, "the omission of bad debt expense corresponding to the pro forma revenue increase inappropriately understates the pro forma revenue requirement." See Frerking Surrebuttal Testimony at 15.

8. Fuel & Purchased Power Expense

a. What is the appropriate level of on-system fuel and purchased power expense that KCPL should be allowed to recover in its rates?

KCPL witness Burton L. Crawford described the method used by KCPL for normalizing the test year fuel and purchase power expense in this proceeding. See Direct Testimony of Burton L. Crawford at 12-16. As explained by Mr. Crawford, the proper method for normalizing the test year fuel and purchased power expense is to normalize and annualize the system peak and energy, the market price of purchased power, the prices paid for fuel, generating system maintenance and forced outages, and available generating resources. After determining the appropriate normalized and annualized values, an accurate production cost computer modeling tool is used to develop the appropriate generation and purchase power levels and resulting fuel and purchased power expenses. KCPL used the MIDAS™ model for its production cost model. Id. at 12.

The Staff used a similar process for developing its fuel and purchase power expenses. Staff witness Charles R. Hyneman describes in his Direct Testimony how the Staff calculated the fuel and purchased power expense that should be included in KCPL's revenue requirement. The Staff computed the fuel expense using prices and quantities incurred by KCPL through June 30, 2006. This process included using fuel prices for nuclear, coal, including freight, natural gas, including natural gas transportation costs and oil. See Direct Testimony of Charles R. Hyneman at 3-20. The Staff's fuel prices were provided to Staff witness Leon Bender as inputs for the Staff's fuel models. Staff witness Curt Wells of the Energy Department, and Staff witness Kimberly K. Bolin of the Auditing Department, developed normalized and annualized sales through June 30, 2006. Other Staff witnesses developed the Staff's annualized net system load, including a line loss percentage and a Company-use level.

After reviewing Staff's calculations related to fuel and purchase power expense, KCPL has accepted the Staff's position in this proceeding, subject to true-up through September 30, 2006. As a result, there is no issue between KCPL and Staff to be resolved by the Commission related to fuel and purchased power expense at this time.

At this stage of the proceeding, KCPL is unclear whether there are any remaining issues related to fuel and purchase power expense that are being sponsored by Public Counsel or intervenors. Apparently, Public Counsel or an intervenor suggested that the List of Issues filed on October 6, 2006, include the above-referenced issues related to fuel and purchased power expense. Public Counsel witness Ralph C. Smith asserted that "[p]rices for natural gas used by

KCPL should be updated to reflect a known and measurable change as of June 30, 2006. The June 30, 2006, NYMEX price should be substituted for the six-day average from December 27, 2005 through January 3, 2006 that was used by KCPL." See Direct Testimony of Ralph C. Smith (HC) at 33.

b. What level of natural gas fuel price should be used in the production cost modeling that is used, along with appropriate fuel adders, to quantify the level of on-system fuel and purchased power expense that KCPL should be allowed to recover in its rates?

As explained by Staff witness Hyneman, the Staff methodology used a weighted average natural gas price that was based upon KCPL's actual gas purchases over the 18-month period from January 2005 through June 2006. See Direct Testimony of Charles R. Hyneman at 13-14. As mentioned above, KCPL expects that the price of natural gas will be part of the fuel and purchased power expenses that will be considered in the true-up proceeding in this case. KCPL respectfully suggests that the true-up process should resolve this issue. However, to the extent that any party continues to have an issue in the area of fuel and purchased power expense, the hearing should clarify the status of this issue.

9. Surface Transportation Board Litigation

a. Should the deferred expenses associated with the Surface Transportation Board rail rate complaint case that were incurred through June 30, 2006, be included in rate base?

This issue relates to the accounting treatment of the litigation costs associated with a rate complaint that KCPL initiated on October 12, 2005, with the Surface Transportation Board (STB) against the Union Pacific (UP) railroad, KCPL's sole source of rail service from Southern Powder River Basin in Wyoming to KCPL's Montrose Station. In that rate complaint, KCPL charged that UP's rates for the movement of coal from origins in the Powder River Basin of Wyoming to KCPL's Montrose Generating Station were unreasonably high. The STB is the exclusive forum available for contesting rates for railroad services.

KCPL estimated that potential freight cost savings could be substantial if it were successful in the STB Complaint proceeding. See Rebuttal Testimony (HC) of Wm. Ed Blunk at 3. Staff also believes that KCPL's efforts to pursue this complaint case and keep fuel costs as low as possible are in the best interests of KCPL's customers. See Direct Testimony of Charles R. Hyneman at 22-23. However, since these litigation costs are not considered normal and recurring expenses by Staff, Staff recommends that they be deferred and amortized over a period of years. KCPL accepts Staff's recommendation on this issue. See Blunk Rebuttal Testimony (HC) at 3.

Both KCPL witness Ed Blunk and Staff witness Charles Hyneman now recommend that the Commission treat the litigation costs related to the STB case as a regulatory asset. Those costs would then be amortized to expense over five years beginning in January 2007, the month when new electric rates will go into effect. If KCPL's Complaint case results in a refund, any refund received by KCPL would first offset any existing balance of STB case costs in the regulatory asset, with the remainder of the refund offsetting fuel costs as determined in a future proceeding. See Hyneman Direct Testimony (HC) at 22-23; Blunk Rebuttal Testimony (HC) at 3-4.

Public Counsel witness Ralph C. Smith, on the other hand, recommends that the Commission should deny recovery on any of these litigation costs. However, as an alternative position, Mr. Smith also recommends that if the Commission decides to include the costs in the Company revenue requirement, "at minimum the costs of the STB complaint should be spread over a representative period, such as five years or longer, that reflects the relative infrequency of such cases and the future period benefited from the expenditure." See Direct Testimony (HC) of Ralph C. Smith at 24.

KCPL respectfully requests that the Commission accept the KCPL/Staff position (and Public Counsel's alternative position) and treat these litigation costs as a regulatory asset and spread the costs over five years. Any refund received by KCPL as a result of this litigation would first offset any existing balance of STB case costs in the regulatory asset, with the remainder of the refund offsetting fuel costs as determined in a future proceeding.

10. <u>SO2 Premiums</u>

a. How should SO2 premiums related to lower-sulfur coal be recorded for book and ratemaking purposes?

b. What parameters does the Commission-approved Stipulation & Agreement in Case No. EO-2005-0329 impose on the treatment of SO2 premiums in this case?

KCPL and Staff are in agreement that KCPL should be required to charge all of its coal SO_2 (i.e., sulfur) premiums against the regulatory liability in Account 254, Regulatory Liability, after January 1, 2007. KCPL believes that this accounting treatment is consistent with the following provision contained in the Stipulation And Agreement approved in Case No. EO-2005-0329:

KCPL currently purchases coal from vendors under contracts that indicated nominal sulfur content. To the extent that coal supplied has a lower sulfur content than specified in the contract, KCPL may pay a premium over the contract price. The opportunity to burn coal with lower sulfur content is both advantageous to the environment and reduces the number of SO_2 emission allowances that must be used. To the extent that KCPL pays premiums for lower sulfur coal up until January 1, 2007, it will determine the portion of such premiums that apply to retail sales and will record the proportionate cost of such premiums in Account 254. But in no event will the charges to the Missouri jurisdictional portion of Account 254 for these premiums exceed $400,000 annually. The portion of premiums applicable to retail will be determined monthly based on the system-wide percentage of MWh's from coal generation used for retail sales versus wholesale sales as computed by the hourly energy costing model. This system-wide percentage will be applied to premiums invoiced during the same period. See Stipulation at 9-10, Case No. EO-2005-0329.

Public Counsel witness Ryan Kind seems to have a different position on this issue, however. According to his Rebuttal Testimony, he believes that the coal sulfur premium provision of the Stipulation referenced above extends through the end of 2007. This interpretation of the Stipulation, however, is incorrect.

The Stipulation states: "To the extent that KCPL pays premiums for lower sulfur coal up until January 1, 2007, it will determine the portion of such premiums that apply to retail sales and will record the proportional cost of such premiums in Account 254." See Stipulation, § III.B.1.d at 10 (emphasis added).

By its own terms, this provision of the Stipulation expires at midnight on January 1, 2007. It is simply not applicable to coal premiums incurred in 2007. As a result, the Commission should reject the position of the Public Counsel on this issue.

Secondly, while Public Counsel agrees that it is appropriate to adjust Account 254 for coal sulfur premiums, Public Counsel assumes that the $400,000 annual limit should be spread over twelve months commencing with the effective date of the Order approving the Stipulation. According to Public Counsel's interpretation, the $400,000 annual limit is effectively twelve consecutive monthly limits of $33,333.33. KCPL must respectfully disagree.

The Stipulation states: "The portion of premiums applicable to retail will be determined monthly based on the system-wide percentage of MWh's from coal generation used for retail sales versus wholesale sales as computed by the hourly energy costing model. This system-wide percentage will be applied to premiums invoiced during the same period." See Stipulation, § III.B.1.d at 10 (emphasis added). This provision does not state, as Public Counsel asserts, that the \$400,000 annual limit will be apportioned on a monthly basis. Public Counsel's interpretation is also inconsistent with the manner in which the \$400,000 annual limit has been treated by KCPL in the past.

Beginning in August 2005, KCPL has determined the portion of coal generation associated with the retail sales and recorded that portion of coal sulfur premiums in Account 254. According to the Surrebuttal Testimony of Ed Blunk, KCPL reached the annual limit the following month. Beginning in January, 2006, KCPL again determined the portion of coal generation associated with retail sales and recorded that portion of coal sulfur premiums in Account 254. The annual limit of \$400,000 was again reached the following month, February, 2006. <u>See</u> Blunk Surrebuttal Testimony at 2-4.

Unlike Public Counsel, Staff is proposing that KCPL be required to charge all of its coal SO_2 premiums against the regulatory liability after January 1, 2007. <u>See</u> Hyneman Direct Testimony at 11-12. KCPL believes Staff interpretation is consistent with the Stipulation and consistent with the correct interpretation that "annually" does not imply pro-rata distribution over twelve months.

For the foregoing reasons, the Commission should reject the adjustment proposed by Public Counsel, and instead adopt the position of the Staff and KCPL on this issue.

11. <u>Injuries and Damages</u>

a. What is the appropriate amount of injuries and damages expense to include in rates?

As indicated in KCPL rebuttal witness Lori Wright's testimony, KCPL uses the accrual method of accounting. Staff also uses the accrual method for insurance and related premiums. However, Staff makes an adjustment to reflect the remainder of injuries and damages using a three year average of cash payments. KCPL believes that using the accrual method for all injuries and damages results in the most appropriate amount to include in its cost of service. In the event the Commission finds Staff's recommendation is appropriate, the cash working capital study should be revised to reflect recovery of injuries and damages on a cost basis.

12. <u>Rate Case Expense</u>

a. What amount of rate case expense should be included in rates?

As set forth in the rebuttal testimony of Lori Wright, KCPL believes it is appropriate to defer reasonable rate case expenses through the duration of the case.

b. Should rate case expense be normalized or deferred and amortized? If the latter, then what is the appropriate amortization period for the deferred rate case expense?

KCPL believes the appropriate amortization period of the deferred rate case expense is two years.

c. Should the costs deferred for future amortization be included in rate base?

Yes, as these are cash costs.

13. <u>Corporate Projects and Strategic Initiatives</u>

a. Should the costs of the LED-LDI and CORPDP-KCPL projects, which are being deferred and amortized over 5 years, be included in rate base?

Yes. These costs are cash expenditures and therefore KCPL believes the nonpayroll cost to be deferred and amortized should be included in rate base. These projects are necessary to enable KCPL to implement its Strategic Intent vision in which it will demonstrate leadership in the supply and delivery of electricity and provide innovative energy solutions to meet the needs of its customers now and for years to come. Staff witness Hyneman maintains that these costs do not meet the test for rate base inclusion as they do not provide "probable future benefits." KCPL asserts that these projects were necessary as part of its ongoing improvement process.

14. **Payroll, Including A&G Salaries**

a. How should annualized payroll costs of Great Plains Energy Services (GPES) employees be allocated to KCPL?

KCPL and Staff both use the GPES billing percentage to KCPL as of the true-up date of September 30, 2006 to determine the GPES allocation of payroll costs to KCPL.

b. What is the proper method to be used in determining the allocation or assignment of A&G salaries to be capitalized or expensed?

KCPL understands that issue (b) no longer needs to be resolved by the Commission as KCPL and Staff intend to file a stipulation and agreement that will address this issue.

15. **Other Benefits**

a. What amount of other benefits should be included in rates?

KCPL is recommending in the testimony of Lori Wright the use of six months actual (through June 30, 2006) and six months projected (through December 31, 2006) for Other Benefit costs. Staff witness Bolin only reflects Other Benefits as of the end of test year period and will update those amounts through September 30. KCPL's approach is more reflective of increasing healthcare costs which are expected to rise due to inflation in the healthcare sector.

16. **Maintenance Expense**

a. Should an adjustment be made to normalize test year maintenance for production and distribution expenses? If so, how?

Staff witness William Harris sponsors adjustments regarding the normalization of maintenance expense for both production and distribution. Mr. Harris recommends adjusting the 2005 test year level of maintenance expense to represent a normalized level of maintenance based upon an historical analysis of actual costs. He originally used a six-year average of actual maintenance expenses for years 2000 through 2005 to reflect production and distribution costs.[2]

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[2] In his Surrebuttal Testimony, Mr. Harris revised his maintenance normalization analysis which is contained in Schedule 1 to his Surrebuttal. With his revised adjustment, he analyzed each functional plant group separately and

For the reasons stated below, Mr. Harris's adjustments should not be accepted.

Production Expense

Since the filing of his original direct testimony, Mr. Harris has proposed the use of a two-year average for steam production maintenance normalization. Unfortunately, this adjustment appears to state actual non-labor operations and maintenance as "In-Year$'s" and does not express costs as a common value. As explained by KCPL witness Dana Crawford, 2004 costs should be escalated to like-year dollars to match the test year and take into account the impacts of market inflation/escalation to indicate all figures in "test-year dollars," (i.e., 2005 dollars). In contrast, KCPL's approach applied historic cost escalations based on the Handy-Whitman Index, which is a nation-wide database, recognized throughout the United States as an industry standard for documenting changes in historic costs. According to the Handy-Whitman Index, price increases for bulk materials, labor and other costs associated with maintenance of industrial equipment have increased between 2004 and 2005. For non-labor O & M, these increases have been 5.08 percent. <u>See</u> Rebuttal Testimony of Dana Crawford at 2-3.

Because KCPL sees this trend continuing with no apparent reduction in demand over the foreseeable future, KCPL requests that the Commission view historic costs on the basis of today's costs. Using Mr. Harris' two-year average for steam production adjusted to 2005 dollars, results in a positive adjustment of $626,656.

Distribution Expenses

Mr. Harris recommends a reduction of $1,877,784 in distribution maintenance expenses based upon the use of a six-year average of actual maintenance expenses for the years 2000 through 2005.

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determined what methodology to use for normalizing maintenance expense. His revised approach, however, contains the same flaws as his original adjustment, and should therefore be rejected by the Commission.

For the same reasons that his analysis of production expenses is flawed, the Commission should reject his adjustment on distribution expenses. As explained in the Rebuttal Testimony of John R. Marshall, Mr. Harris' analysis does not take into account the time value of money, and the escalation in maintenance for distribution equipment that has occurred. Mr. Marshall recommends that the normalized adjustment should be calculated by utilizing the Handy-Whitman index to the test year dollars. This results in an increased normalized adjustment above Mr. Harris' calculation of $1,150,331 for distribution maintenance expense.

In addition, KCPL will be absorbing an additional operations and maintenance impact ("O & M") impact of approximately $2 million a year resulting from the Asset Management Inventory and System Assessment Project discussed by Mr. Marshall. A reduction in the distribution maintenance expenses could make it more difficult for KCPL to implement the Inventory and System Assessment Project, as well as the other projects associated with the Asset Management Plan.

For these reasons, KCPL respectfully requests that the Commission decline to accept Mr. Harris' normalization of maintenance expenses for production and distribution expenses, and instead adopt the recommendations of KCPL witnesses Crawford and Marshall.

17. <u>Property Taxes</u>

a. Should property taxes be adjusted to reflect changes in tax jurisdiction assessment values, levy rates, in plant additions, and other factors during the test period, including both the update period and true-up period?

Yes. Property taxes should be adjusted to reflect changes in tax jurisdiction assessment values, levy rates, in plant additions, and other factors during the test period, including both the update period and true-up period.

Staff witness Phil Williams sponsored an adjustment which increases the actual test year property taxes expensed of $54,284,956 by $1,684,275 to annualize the property tax amount based upon December 2005 plant balances.

As explained in the Rebuttal Testimony of KCPL witness Shannon Green, Jr., KCPL appreciates Staff's efforts to adjust test year 2005 property tax expense to an annualized level. However, Staff's adjustment does not reasonably reflect the increased property tax expense that KCPL will incur in 2006 and thereafter. In particular, Staff's adjustment does not reflect known and measurable changes to the property taxes that will be paid by KCPL in 2006, nor does it reflect the additional property taxes due to the applicable plant additions during 2006.

Staff's adjustment does not fully reflect the following known and measurable changes:

1. KCPL's property assessments in 2006 have increased. An adjustment is needed to reflect the increased property assessments by county;

2. The tax levy rates in 2006 are increasing. An adjustment is needed to reflect the 2006 increases in the actual 2005 tax levy rates[3];

3. Payments In Lieu of Property Taxes (PILOTs) will be paid on the Wind Generation Facility. An adjustment is needed to reflect the PILOTs on the Wind Generation Facility.

KCPL respectfully requests the Commission to allow recovery of known and measurable increases in its property tax expense amounting to $4,689,563. This annualized adjustment to KCPL's 2005 test year property tax expense exceeds Staff's recommended adjustment of $1,684,275 by $3,005,288.

The following adjustments should be included in the Company's revenue requirement in this proceeding:

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[3] For example, on August 14, 2006, the Board of Education of USD #244 approved a 2.5 mill levy increase for 2006, raising KCPL's 2006 projected property taxes by $500,316. Other tax levy increases will be known by the true-up proceeding, and are expected to be approximately $660,293 based upon a three-year historical trending factor of levy rate increases for total KCPL property of 1.18%.

			Adjustments
1)	Use of Actual 2006 Assessed Property Values		$1,890,810
2)	Use of Increased 2006 Tax Levies		1,159,227
3)	Annualized property taxes on 2006 Plant Additions		
	a) Estimated plant additions (January 1 to September 30, 2006, excluding wind generation facility)	$1,309,526	
	b) Payments In Lieu of Property Taxes	330,000	
			1,639,526
	Known and Measurable Increases in Property Taxes		$ 4,689,563
	Minus Staff Annualization Adjustment		$1,684,275
	Requested Adjustment to Staff case		$3,005,288

In his Surrebuttal Testimony, Staff witness Phillip K. Williams argues that such changes are not "known and measurable" since tax levy rates may decrease at the same time that property assessed values increase. He suggests that: "Staff has seen in the past when reviewing historical property tax data at other utilities that many times when the assessed values are increased the corresponding tax levy rates are adjusted downward to keep the property tax levels revenue neutral." See Surrebuttal of Phillip K. Williams at 26-27. He also argues that the Commission should ignore the property taxes and PILOTs on the wind generation facility since "KCPL's proposed level of property tax expense violates the test year and the true-up period in this case." Id. at 31.

Apparently, Staff would have the Commission ignore known and measurable changes in property assessments and tax levies in the hope that tax authorities will lower tax levies in the future "to keep the property tax levels revenue neutral." Id. at 25. The Commission should reject this approach. KCPL respectfully requests that the Commission incorporate into the revenue requirement in this proceeding the known and measurable changes in property assessments and tax levies, based upon the information known at this time, as updated in the true-up proceeding. In the event that tax levies are lowered at some future date, those future tax levies may be incorporated into the revenue requirement in KCPL's next rate case.

Secondly, KCPL would disagree with Staff that KCPL's proposed adjustments should exclude the property taxes and PILOTs on the wind generation facility that has been recently completed. The true-up proceeding will incorporate the addition of the wind generation facility into KCPL's revenue requirement. It would be unreasonable to incorporate the plant in service related to the wind generation facility, but refuse to recognize the property tax impact of that same investment.

In summary, KCPL respectfully requests that the Commission adopt its proposed adjustments to Staff's property tax annualization and thereby reflect the known and measurable changes in tax jurisdiction assessment values, levy rates, in plant additions, and other factors during the test period, including both the update period and true-up period.

18. Decommissioning Expense

a. Should decommissioning expense be reduced to reflect the amount of annual accruals expected under a 60-year license?

The Wolf Creek Nuclear Operating Corporation submitted an application to the U.S. Nuclear Regulatory Commission ("NRC") on October 4, 2006, requesting that the NRC grant a 20-year extension to the license to operate the Wolf Creek Generating Station. The current annual accruals are based upon the plant's existing 40-year operating license. If the NRC grants the requested license extension, the assumed plant life will increase to 60 years. There is no indication from the NRC or from the unit's operating history that would suggest that the license extension will not be granted. Consequently, the annual accrual should reflect the longer expected life of the unit. KCPL recommends that the decommissioning accrual schedule included in the direct testimony of KCPL witness Don A. Frerking be approved by the Commission in this proceeding.

19. <u>True-up</u>

a. What elements of Cost of Service and Rate Base should be updated in the September True Up?

In the Stipulation And Agreement approved in Case No. EO-2005-0329, p. 30, the Signatory Parties agreed to the following provision related to the true-up in this case:

> **a. RATE FILING # 1 (2006 RATE CASE)**
> (i) <u>Schedule.</u> Rate schedules with an effective date of January 1, 2007 will be filed with the Commission on February 1, 2006. The test year will be based upon a historic test year ending December 31, 2005, (initially filed with nine (9) months actual and three (3) months budget data), with updates for known and measurable changes, as of June 30, 2006, and with a true-up through September 30, 2006. <u>On or about October 21, 2006, KCPL will file in a true-up proceeding a reconciliation as of September 30, 2006. The specific list of items to be included in the true-up proceeding shall be mutually agreed upon between KCPL and the Signatory Parties, or ordered by the Commission during the course of the rate case. However, the Signatory Parties anticipate that the true-up items will include, but not necessarily be limited to, revenues including off-system sales, fuel prices and purchased power costs, payroll and payroll related benefits, plant-in-service, property taxes, depreciation and other items typically included in true-up proceedings before the Commission.</u> (emphasis added)

At this stage of the proceeding, there has been no agreement between KCPL and the other parties regarding a specific list of items to be included in the true-up proceeding. However, KCPL continues to believe that the list should include the following items: "off-system sales, fuel prices and purchased power costs, payroll and payroll related benefits, plant-in-service, property taxes, depreciation and other items typically included in true-up proceedings before the Commission." KCPL intends to discuss with other parties in the course of this proceeding a more specific list of true-up items that should be included in the reconciliation to be filed on October 21, 2006. Hopefully these discussions will resolve this issue without the need for a decision by the Commission. To the extent that the Commission wishes to address this issue during the hearing, KCPL witness Tim Rush will be available to address this topic.

20. Regulatory Plan Additional Amortizations

a. What amount of Regulatory Plan additional amortizations should be allowed to maintain KCPL's credit rating? Should a "gross up" for taxes be added to this amount? If so, what amount is appropriate?

KCPL has presented evidence justifying a rate increase of approximately 11.5% ($55.8 million) and an ROE of 11.50% based upon a capital structure of 53.81% equity. If the Commission's decision reflects the position of the Company, there is no need for Additional Amortizations (as permitted by the Stipulation) to be set by the Commission.

The use of the Additional Amortizations mechanism will result in an addition to KCPL's cost of service in a rate case when the projected cash flows resulting from the Company's Missouri jurisdictional operations, as determined by the Commission, fail to meet the low end of the top third of the BBB range. See Appendix E-1, Stipulation. That is the only circumstance in which the Amortizations come into play. Because KCPL's proposal in this case is premised on cash flow that will be adequate to achieve the thresholds for the two key credit metrics in Appendix E-1, there should be no need for Additional Amortizations, as explained in the Direct Testimony of Michael Cline at 5-6, KCPL's Treasurer.

Further, as Mr. Cline explained in rebuttal and surrebuttal, because the Amortizations ensure that KCPL maintains target levels for certain key credit metrics, they primarily benefit bondholders and other creditors. They do not address the concerns of equity investors who focus on KCPL's ability to generate earnings over time. See Cline Rebuttal at 3-4.

Gross-Up of Additional Amortizations for Income Tax Purposes

KCPL believes that Staff and Public Counsel are in general agreement with the Company that the Additional Amortizations related to the Regulatory Plan should include an amount reflecting a gross-up for income tax purposes. See Traxler Surrebuttal Testimony at 13-14; Trippensee Surrebuttal Testimony at 2-3.[4]

As explained in the Rebuttal and Surrebuttal Testimony of Robert W. Hrisko, a tax managing director in the Chicago office of PricewaterhouseCoopers LLP, it is essential to KCPL that the Commission recognize the implications of the tax effects of the Additional Amortizations. Otherwise, the cash flow benefits of the amortizations in the Stipulation will not be realized.

For book purposes, the Amortizations are included in gross revenues with an offsetting accelerated depreciation/amortization expense. This results in no change to KCPL's net operating income. For tax purposes, however, the Amortizations are includable in gross taxable income under Internal Revenue Code Section 61. However, there will be no offsetting tax deduction.

This results in an increase in current taxes payable that is equal to KCPL's current federal and state tax rate times the total Amortizations allowed. In order to receive the proper amount of cash to meet the credit ratios, KCPL must be allowed to gross-up for income taxes any Additional Amortizations cash-flows that are allowed. For example, if additional cash flows of $1,000 were required to meet the ratios, KCPL should collect $1,538 from ratepayers as a result of the income tax (assuming a 35% corporate federal income tax rate) that would be due. This Additional Amortization would permit KCPL to increase its cash flow by $1,000. See Hriszko Rebuttal at 3-4.

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[4] Staff initially took a different position on this issue at the time of the filing their direct testimony in this matter. See Direct Testimony of Steve Traxler (HC) at 20. However, after further discussions in the context of this case and in the pending Empire Rate Case, Case No. ER-2006-0315, it is KCPL's understanding that Staff and Public Counsel have modified their position on this issue, and now support the position of KCPL and Empire that the Additional Amortization should be grossed-up to provide the public utilities with sufficient cash flow to meet the financial metrics contained in their respective Regulatory Plans.

The actual amount of the gross-up for income taxes will be directly related to any Additional Amortizations approved by the Commission. As explained by KCPL witness Chris Giles, this will be determined at the conclusion of the case when the Commission establishes the level of the Company's revenue requirement, including Return on Common Equity.

b. What risk factor should be used in calculating the Regulatory Plan additional amortizations for off-balance sheet purchased power agreements?

c. Over what period of time should the Regulatory Plan additional amortizations be treated as an offset to rate base?

d. Should the capital structure be synchronized with the investment in Missouri jurisdictional electric operations? How should that be accomplished?

e. Should an amount be added to Missouri jurisdictional rate base to reflect additional investments related to Missouri jurisdictional electric operations?

KCPL understands that issues (b) through (e) no longer need to be resolved by the Commission as KCPL, Staff and Public Counsel intend to file a stipulation and agreement that will address and resolve the mechanics of implementing any Additional Amortizations in this case.

21. <u>Weather Normalization/Customer Growth</u>

a. What methodology should be used to compute Large Power class kWh sales and revenues?

As set forth in the rebuttal testimony of Dr. George M. McCollister, the large power (LP) class is weather sensitive. KCPL adjusts revenues to the weather normalized level in its direct case. This weather adjustment was also used to calculate weather normalized fuel costs in the Company's direct case. Staff witness Lange believes that the LP class billing data should not be weather normalized. Staff's position ignores the fact that the large power class load shows a weather sensitivity since many of these companies have substantial air conditioning loads which would vary with outdoor temperature. Dr. McCollister performed a statistical test of the weather sensitivity of the LP customers to confirm that the LP customers are weather sensitive.

22. Jurisdictional Allocations

a. What is the appropriate method (4 CP vs. 12 CP) to use for allocating generation and transmission costs among jurisdictions?

As explained by KCPL witness Don A. Frerking, KCPL recommends allocating generation and transmission costs among jurisdictions on a 12-month average coincident peak demand allocation ("12 CP") basis. See Frerking Direct Testimony at 11. Staff witness Erin L. Maloney and Praxair/MIEC witness Maurice Brubaker recommend using a 4-month average coincident peak demand allocation ("4 CP"). The 12 CP methodology is more appropriate for allocating KCPL's plant and other fixed costs associated with production and transmission assets.

The operating and capacity planning realities of the KCPL's generation portfolio support the use of the 12-CP methodology. KCPL's capacity planning process takes into account all the hours of the year, not just the peak hour or any seasonal peaks. In addition, KCPL utilizes periods of the year, typically in the spring and fall, with lower retail and FERC jurisdictional wholesale peak loads to perform necessary maintenance on its generating facilities and to pursue off-system sales while still maintaining adequate reserve margins. All of these operating and capacity planning realities indicate that the 12-CP methodology is more appropriate than simply relying on the summer month peaks. See Frerking Surrebuttal Testimony at 3-4; Frerking Rebuttal Testimony at 5-7.

Moreover, KCPL uses the 12 CP methodology in its FERC and KCC jurisdictions. If consistent allocation methodologies are not utilized in KCPL's various jurisdictions, the result will likely be an over or under recovery of KCPL's costs.

b. How should A&G expenses be allocated to the Missouri retail, Kansas retail and FERC wholesale jurisdictions?

As explained by KCPL witness Don A. Frerking, KCPL recommends allocating A&G costs among jurisdictions using a number of methods depending on the cause of the costs. See Frerking Direct Testimony at 10. Specifically, KCPL recommends allocating salaries, employee benefit, and injuries and damages expenses based on the ratio of the allocated sum of the labor portion of the production, transmission, distribution, customer, and sales expenses described previously. KCPL recommends directly assigning the regulatory expenses to the jurisdiction of their origin. KCPL recommends allocating property insurance expenses based on the allocation of total plant. KCPL recommends allocating general plant maintenance and fleet expenses based on the allocation of the plant with which they are associated. KCPL recommends allocating general advertising expenses using the Customer allocator. KCPL recommends allocating the remainder of the A&G expenses using the Energy allocator.

23. Off-System Sales

a. What level of off-system sales margin should be included in determining KCPL's cost of service?

Given the risk and volatility of the competitive wholesale power markets, a probabilistic determination of expected margins from Off-System Sales ("OSS") should be included in KCPL's cost of service for the year in which the rates set by this case will be in effect. KCPL recommends that the Commission set the level of margins at the point where there is a 75% chance that the Company will be able to achieve such OSS margins (i.e., the 25% point on the probability distribution of OSS). Alternatively, the Commission should increase the return on equity 9.57 basis points for each $1 million of OSS margin included in the test year revenue requirement above the 25% point of expected sales.

The Company's recommendation is based on the study conducted by Michael M. Schnitzer, co-founder of the NorthBridge Group which provides economic and strategic advice to energy companies. He describes in detail why the three key drivers of OSS margins — natural gas prices, the market heat rate, and the quantity sold — are uncertain and cannot be forecast with precision. Given the NorthBridge analysis, which none of the parties disagrees with, KCPL proposes to place this risk with shareholders, but, in exchange, establish a level of OSS margins where there is a 25% chance that the margins will be below such level and a 75% chance that they will be above. Alternatively, the Commission should increase the ROE by 9.57 basis points for each $1 million of OSS margin included in test year revenue above the 25% point. As noted in the testimony of Chris B. Giles, rate of return witnesses do not directly account for the risk of this market in their evidence.

Establishing a realistic level of expected margins is critical. The prospective calculation of margin has declined significantly in the past three months, as noted in Mr. Schnitzer's Surrebuttal Testimony. Moreover, the risks facing KCPL in the future cannot be measured by historical sales which, although favorable, demonstrate the highly volatile nature of the market. As Mr. Schnitzer stated: Past performance is no guarantee of future results.

b. How should the off-system sales margin be allocated to the Missouri retail, Kansas retail and FERC wholesale jurisdictions?

KCPL favors allocating OSS margins between Missouri and Kansas based upon "Unused Energy."

Because KCPL can only sell into the wholesale market if it first meets its retail load requirements, it is the Unused Energy of retail customers that is available for such sales. Since its Kansas jurisdiction has a lower load factor than Missouri, KCPL proposes to allocate slightly more margin to Kansas customers. Because OSS margins can be specifically identified, Unused

Energy is the most logical and equitable basis to allocate such margins, as noted in the testimony of Chris B. Giles and Don Frerking.

c. What parameters does the Commission-approved Stipulation & Agreement in Case No. EO-2005-0329 impose on the treatment of off-system sales revenue in this case?

The Stipulation does not bar or otherwise restrict the Commission from setting OSS revenues for ratemaking purposes on the basis of the testimony of Mr. Schnitzer and Mr. Giles.

The Stipulation states that OSS will "continue to be treated above the line for ratemaking purposes." KCPL's proposal does not change that. The Company agreed not to propose "any adjustment that would remove any portion" of OSS from its revenue requirement determination in a rate case, and agreed not to argue that OSS revenues and expenses should be excluded from the ratemaking process. See Stipulation, § III.B.1.j at 22. KCPL's proposal is consistent with each of those pledges.

KCPL asks the Commission to determine the appropriate level of OSS margins to include in the revenue requirement, based upon the NorthBridge probabilistic analysis of OSS margins which is uncontroverted. While the Commission could award KCPL a basis-point adder to mitigate the risks of the competitive wholesale market, the Company believes that its recommended level of OSS margins, as adjusted at the True-Up proceeding, is the best solution. It is a lawful element of the Company's Experimental Regulatory Plan approved in the Stipulation, and is supported by long-standing Missouri case law which has upheld experimental ratemaking provisions. See Union Elec. Co. v. PSC, 136 S.W.3d 146, 152 (Mo. App. 2004); State ex rel. Laclede Gas Co. v. PSC, 535 S.W.2d 561, 567 (Mo. App. 1976).

d. Should KCPL's customers receive the benefit of all margins of off-system sales or should it be shared between customers and shareholders? Should a mechanism be adopted to ensure that the benefit is received by the appropriate party or parties? If so, what mechanism?

KCPL does not propose sharing OSS margins with customers, which would be contrary to the intent and spirit of the Stipulation's Section III.B.1.j at 22.

The mechanism proposed by the Company, described above and detailed at length in the testimony of Chris B. Giles, calls for the Commission to eliminate 25% of the risk of OSS margins from the volatile competitive wholesale electric markets.

24. Depreciation

a. What are the appropriate depreciation rates to be used in establishing rates in this proceeding?

As explained by KCPL witness Don A. Frerking, KCPL maintains that the Commission should reject Staff's proposal to decrease KCPL's depreciation expense. See Frerking Rebuttal Testimony at 15. KCPL did not submit a depreciation study in this case because it believed that it was the intent of the parties to the Stipulation and Agreement in Case No. EO-2005-3029 to use the depreciation rates listed in Appendix G of that agreement in this case. KCPL's most recent depreciation study, which it submitted on March 31, 2005 in compliance with 4 CSR 240-20.030, suggests changes that, if implemented, would have increased KCPL's overall depreciation expense.

KCPL maintains that it does not make sense to change depreciation rates in this case, because the credit ratio amortization mechanism established in the Regulatory Plan Stipulation and Agreement provides for additional amortization expense, if necessary, to provide cash to maintain adequate credit metrics during the term of the Regulatory Plan. From a practical standpoint any adjustment to depreciation rates would necessitate an equal and offsetting adjustment to amortization expense to maintain equivalent cash flow. The Regulatory Plan Stipulation and Agreement contemplates that the accumulated amortization can be re-directed to specific plant accounts to be determined at a later time. KCPL believes that it would be more appropriate to defer any revision to depreciation rates until the conclusion of the Regulatory Plan when the total accumulated amortization related to the Regulatory Plan is known.

The Commission's Staff filed a depreciation study in this case that appears to suggest that a decrease in KCPL's depreciation expense is warranted. As explained by KCPL witness Don A. Frerking, KCPL disagrees with this conclusion and argues that the appearance of a need for a decrease is the result of significant flaws in Staff's study. See Frerking Rebuttal Testimony at 16-20. First, the Staff's study appears to contain significant flaws with regard to the lifespan analysis and the related interim retirements for the generation accounts. Second, the retirement curve matching for a number of the transmission, distribution, and general plant accounts is questionable. And third, the approach the Staff used to calculate net salvage rates is mathematically and analytically incorrect.

The Commission should disregard Staff's depreciation study as flawed and refrain from revising the depreciation rates of KCPL's assets until the conclusion of the Regulatory Plan.

25. Cost of Capital

a. What is the appropriate capital structure?

The capital structure requested by KCPL is described in the Direct Testimony of Dr. Samuel Hadaway, founder and principal of FINANCO, Inc., Austin, Texas, and formerly Director of the Economic Research Division at the Texas Public Utility Commission. Its components are as follows:

KCPL Requested Capital Structure

Debt	44.67%
Preferred Stock	1.52%
Common Equity	53.81%
Total	100.00%

Since Staff corrected its August 8, 2006 direct testimony to reflect KCPL's capital structure as of June 30, 2006, including the issuance of $150 million in common equity, Staff's recommendations are comparable to that of the Company.

Staff Recommended Capital Structure

Debt	45.22%
Preferred Stock	1.54%
Common Equity	53.24%
Total	100.00%

OPC and DOE, the only other parties offering testimony on the subject, have accepted the Company's capital structure request.

b. What is the appropriate return on common equity (ROE)?

Based on Dr. Hadaway's testimony, KCPL requests an ROE of 11.50%.

The key factor in analyzing what should be a fair rate of return for KCPL is its large capital expenditure program. Over the next five years, it is expected to equal 95% of the Company's current net plant. In comparing KCPL to a "reference group" of other investment grade electric utilities, Dr. Hadaway stated that their spending averaged only 56% of current net plant. While he estimated the average cost of equity for these companies at 11.0%, KCPL's risk profile justifies an increase of 50 basis points.

This recommendation is based upon the reference group's DCF (discounted cash flow) analysis range of 10.6% to 11.3%, as well as a risk premium analysis that indicated an ROE range of 10.9% to 11.8%. Considering the ongoing risks that exist in the electric utility industry, and the specific risks that KCPL faces in its construction program and its Off-System Sales margins, an 11.50% ROE is a reasonable estimate of the fair cost of equity capital to the Company.

c. Should ROE be adjusted either upwards or downwards to reflect increased or decreased risk or company performance? If so, what adjustment should be made?

The ROE set by this Commission should reflect the environment in which KCPL will operate until the next rate case is filed. Its $1.3 billion construction poses risks that simply cannot be eliminated through careful planning and competent management. KCPL's recent experience with Off-System Sales margins providing almost half of its earnings is not likely to continue. These are the most relevant factors that the Commission is required by law to consider.

Furthermore, it would be appropriate for the Commission to consider KCPL's recent record of excellent performance, as described in the testimony of Mr. Robert Camfield, a Vice President of Christensen Associates Energy Consulting, LLC, Madison, Wisconsin, and a former staff member of the Michigan and New Hampshire Public Service Commissions. He reviewed four metrics: (1) Overall Retail Prices; (2) Total Factor Productivity; (3) Cost Diagnostics of utility operations; and (4) Scorecard Metrics related to customer satisfaction.

Based upon his study, Mr. Camfield concluded:

- Since 1994, KCPL's retail prices have declined 1.5% faster than the industry and 1.75% faster than its peer group.

- KCPL's Total Productivity Factor increased at an average annual rate of 2.4% (1994-2004), surpassing the 1.0% annual rate achieved by neighboring utilities. The industry as a whole realized only a 0.6% increase, while KCPL's peer group experienced no change.

- KCPL reduced customer service operations and maintenance costs substantially, and sharply outperformed industry and comparison groups. Measuring the total of KCPL's resources employed in both capital and O&M expenses, the Company demonstrated substantial gains in resource utilization and productivity.

- Scorecard Metrics also revealed KCPL has satisfied its target levels for customer satisfaction, and has increased its performance in metrics measuring percentage of customers returned to service in two hours and response times to calls for service.

See Camfield Direct Testimony at 14-20.

Based upon these findings, Mr. Camfield concluded that from 1994 to 2004, KCPL "has achieved on of the highest levels of productivity improvement in the U.S. electric industry." See Camfield Direct Testimony at 20 (lines 15-16). He estimated that KCPL's performance translated into net value gains to retail consumers of $116.9 million to $144.6 million. He recommended that the Commission establish a Performance Allowance of 50 to 100 basis points within the authorized ROE. This would equate to incremental revenues in a range of $5.6 - $11.1 million. See Camfield Surrebuttal at 6-7. In recent years commissions in Iowa, Virginia, Ohio and Pennsylvania have adopted similar proposals that recognized the quality of a utility's performance and management. See Leonard S. Goodman, The Process of Ratemaking 644-45 (1998).

Mechanisms to promote efficiency and productivity are not new, and have been embraced by this Commission in various experimental regulatory plans. See Union Elec. Co. v. PSC, 136 S.W.3d 146, 152 (Mo. App. 2004). See also Charles F. Phillips, Jr., The Regulation of Public Utilities 401-12 (3d. ed., 1993). Performance-based ratemaking is not a new concept to encourage efficiencies and maintain earnings. Id., 401-02. As Phillips has observed, "failure to maintain the financial integrity of utilities is against the interests of consumers, as well as investors." Id. at 412. An adjustment to KCPL's ROE to encourage continued excellent performance should be seriously considered in this case.

B. Class Cost-of-Service and Rate Design

1. Class Cost-of-Service

a. On what basis should distribution costs be allocated to classes? Should the allocation of primary distribution costs include any customer-related component? What type of demand should be used to allocate the cost of distribution substations and distribution lines?

KCPL witness Lois J. Liechti sponsors KCPL's Class Cost of Service Study ("CCOS") in this proceeding. In her Direct Testimony, she explains that the purpose of the CCOS study is to determine the contribution that each customer class makes toward the Company's overall rate of return. The CCOS analysis strives to attribute costs in relationship to the cost-causing factors of demand, energy and customers.

As explained by Ms. Liechti, KCPL used its load research data to develop distribution plant allocators based on customers' non-coincident loads within each class. See Liechti Direct Testimony at 8. The demand portion of the distribution plant and related expense was allocated on two types of non-coincident demands ("NCD"). Substation related equipment and expense were allocated on class NCD allocators, while delivery equipment and expense were allocated on customer NCD allocators. The customer portion of the distribution plant and related expense was allocated based on the weighted number of customers. General and intangible plant was allocated based on the sum of combinations of production, transmission and distribution plant accounts.

b. On what basis should production capacity and transmission costs be allocated to classes?

The Company used an allocation method called the Average and Peak method to allocate production and transmission plant. This method gives classes recognition for both usage and contribution to peak load.

c. What is the appropriate method to use for allocating margins on off-system sales among Missouri retail customer classes? (MIEC)

KCPL does not believe that the issue of the allocation of off system sales margins among the retail classes is properly considered a class cost of service or rate design issue. The allocation of off system sales margins should be consistent with the revenue requirement allocation of off-system sales, which has been addressed in other sections of this brief.

d. Do KCP&L's computation of coincident peak demands and class peak demands properly recognize line losses?

As explained by Ms. Liechti, consideration of system losses, unaccounted for and sampling error was taken into account in determining the class demands in KCPL's CCOS. KCPL witness George M. McCollister describes this process in his direct testimony.

e. To what extent, if any, are current rates for each customer class generating revenues that are greater or less than the cost of service for that customer class?

The results of KCPL's CCOS study indicate that the residential class is not providing a comparable return on rate base in comparison to all other major classes of customers. The results of the CCOS show a return in the residential class that is 74% of the overall average. Small General Service is 11% above the overall average rate of return. Large General Service is 21% above the overall average and Large Power Service is 12% above the average. The Lighting Class showed a rate of return that was 39% of the overall average. See Rush Direct Testimony at 4-5.

The individual classes' rates of return at current rates vary, and are shown in the following table:

Residential	Small GS	Medium GS	Large GS	Large Power	Other Lighting
5.5%	8.3%	10.4%	9.0%	8.3%	2.9%

If rates were changed so that KCPL earned the same rate of return from each customer class then each class's rate would have to change as follows:

Residential	Small GS	Medium GS	Large GS	Large Power	Other Lighting
7.5%	-3.0%	-9.0%	-4.6%	-2.3%	10.3%

f. What is the appropriate basis for allocating Administrative and General Expense Account Numbers 920, 922, 923, 930.2, and 931 among Missouri retail customer classes?

KCPL witness Lois Liechti addresses the appropriate allocation factors in KCPL's Class Cost of Service study and workpapers.

2. Rate Design

a. Should revenue adjustments among classes be implemented in order to better align class revenues to class cost-of-service? If so, what percentage increase or decrease should be assigned to each customer class?

b. Should class revenue adjustments be implemented even if no increase or decrease in revenue requirement is granted?

c. Should revenue adjustments be phased-in over multiple years?

d. Should revenue adjustments among the non-residential classes be applied uniformly or non-uniformly?

e. How should any increase in the revenue requirement be implemented?

f. Should a comprehensive analysis of KCPL's class cost-of-service issues and rate design be conducted after the conclusion of the regulatory plan and the in-service date of Iatan 2? Should the cost-basis of general service all-electric rates be included in this analysis?

As explained by KCPL witness Timothy M. Rush, KCPL does not propose to change the current relationship of customer class returns to the average jurisdictional return. The Company is recommending an equal percentage increase be ordered for all customer classes with minimal changes in rate design. It is the Company's position that any additional shift in revenue requirement among classes for the purpose of achieving equal returns of all classes is more appropriately addressed in a future rate design case. KCPL does not believe it is appropriate to increase any class of customer rates higher than the average in this case. KCPL believes that the appropriate time to move toward equal rate of return for all customer classes is after the completion of the Regulatory Plan and the in-service of Iatan 2. Subsequent to that case it may be appropriate to file another rate design case based upon revenue neutral jurisdictional revenue requirement that would result in minimizing a one-time impact on any particular customer or class of customer.

KCPL is proposing to maintain the current relationship of rate design within the residential class, except to increase the service charge by a larger percentage than the other rate components. The reason for increasing the service charge is to more closely approximate the cost of providing service. KCPL is proposing to delete customer service charges where the Company does not have customers or the customer usage characteristics would be such as they should be on another rate schedule.

3. Availability of General Service Space-Heating Rate Discounts

a. In this case, should the qualification provision of the existing general service all-electric rate schedules be expanded as proposed by KCPL, and the all-electric winter energy rate increased an additional 5%, to make rate discounts available to existing and future customers who are not all-electric customers?

KCPL is proposing to increase the all-electric winter energy rate by 5%, while expanding the qualifications provision to establish electric heating as the primary heating sources, rather than the requirement that the customer qualification is all-electric. KCPL is proposing this change to tailor its tariffs to meet customer needs. For example, KCPL's current tariff requires a customer to be all-electric in order to qualify. This means that all of the customer's energy consuming equipment, including water heating and space heating, must be all electric. As explained by Tim Rush, this precludes customers that wish to install solar equipment or other supplemental heating energy sources from qualifying. It also precludes customer from having natural gas cooking, water heating or other minor energy sources. KCPL believes that expansion of the tariff will give customers more choice and a better means for equipment utilization. See Rush Rebuttal Testimony at 4-5.

b. Should KCPL's proposed changes to the General Service customer charge be implemented?

Yes. KCPL has service charges within each rate schedule that vary based on the size of the customer. KCPL recommends that those service charges be deleted where KCPL does not have customers or where the customer usage characteristics are such that they should be on another rate schedule. These latter two changes are essentially clean-up and simplication changes from the rate design case in 1996.

c. Should the existing general service all-electric rate schedules and the separately metered space heating provisions of KCPL's standard general service tariffs be (1) eliminated; or (2) restricted to existing customers only until there is a comprehensive class cost of service study and/or cost-effectiveness study which analyzes and supports such tariffs and provisions as well as KCPL's Affordability, Energy Efficiency and Demand Response programs?

No. KCPL's general service rate design been in place for many years with the approval of the Commission. KCPL participated in an extensive CCOS study and rate design case in 1996. At that time, rates were established based on the CCOS, and rate design changes were made that changed the overall price structure. The rates maintained the price differential between customers with electric heating that were in place prior to the rate design case. It would be inappropriate and unreasonable to eliminate or otherwise restrict the existing KCPL general service all-electric rate schedules as suggested by Trigen in this proceeding.

C. Customer Programs

1. Weatherization Program

a. Should the weatherization program be modified so that KCPL's Call Center will refer customers to the program?

As explained by KCPL witness Sue Nathan, this issue was discussed during a meeting of KCPL's Customer Program Advisory Group ("CPAG") that was held on September 20, 2006. At that time, the participants discussed the various ways KCPL could refer customers to this program. KCPL agreed to develop a list of its customers who receive third-party assistance in paying their bills and who met KCPL's usage and customer eligibility guidelines. KCPL agreed to inform those customers of the availability of the program. See Nathan Surrebuttal Testimony at 8-9. KCPL believes that there are no longer any disputes concerning this issue.

b. Should LIHEAP recipients be directed to the weatherization program and be required to participate in it?

LIHEAP is administered through the Missouri Department of Social Services. Therefore, that agency would be responsible for any changes in the current referral procedures. KCPL would support having the Department of Social Services and other providers modify their rules to improve referrals to weatherization. KCPL maintains, however, that such an initiative should be a statewide issue and is outside the purview of this rate case. See Nathan Surretbuttal Testimony at 9. KCPL believes that there are no longer any disputes concerning this issue.

c. Should KCPL participate in an "Energy Conservation Program" that will provide consultation, weatherization materials and installation?[5] If so, should the cost of the program to be underwritten by KCPL and charged to the customer?

KCPL witness Sue Nathan responds to Mr. Bill Dias's request for the Commission to require KCPL to implement an "Energy Conservation Program" in her Surrebuttal Testimony at 4-5. Although the details of what Mr. Dias wants the Commission to require of KCPL are unclear, KCPL understands that he requests the Commission to compel KCPL to utilize a service he or his company is providing. The Commission should not require KCPL to participate in this kind of an "Energy Conservation Program." KCPL works collaboratively with other parties through the CPAG to consider and evaluate energy conservation and other customer programs. KCPL sees no merit in circumventing the CPAG process to give Mr. Dias and his company preferential treatment.

WHEREFORE, for the reasons stated herein, Kansas City Power & Light Company respectfully requests that the Commission order that adopts its recommendations in this case.

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[5] The Missouri Department of Natural Resources and the City of Kansas City object to the inclusion of this issue and assert that it is not properly before the Commission in this case.

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Respectfully submitted,

/s/ James M. Fischer
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CERTIFICATE OF SERVICE

I do hereby certify that a true and correct copy of the foregoing document has been hand delivered, emailed or mailed, postage prepaid, this 12th day of October, 2006, to all counsel of record.

/s/ James M. Fischer
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