BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

Ag Processing, Inc., a Cooperative,	)	
	)	
Complainant,	)	
	)	
v.	)	Case No. HC-2010-0235
	)	
KCP&L Greater Missouri Operations Company,	)	
	)	
Respondent.	)	

REPLY TO AG PROCESSING'S RESPONSE IN OPPOSITION

KCP&L Greater Missouri Operations Company, formerly known as Aquila, Inc. ("GMO" or "Company"),[1] hereby replies to the Response in Opposition to Application for Rehearing of Ag Processing, Inc., a Cooperative ("AGP").

I. GMO's Application for Rehearing is Proper.

1. AGP mischaracterizes or entirely misunderstands GMO's Application for Rehearing. GMO does not re-argue its position in its post-hearing brief, as AGP alleges (AGP Response at 2), but rather lays out various errors that render the Report and Order unreasonable and unlawful. GMO's arguments have merit and do indeed form the basis for rehearing, contrary to AGP's contention. (AGP Response at 2).

2. GMO argues in its Application for Rehearing that the Commission's conclusory finding that Aquila knew that its customer estimates were not reliable, and its resultant finding of imprudence (Report and Order ¶¶ 44-48 at 14-16), is inadequate and unreasonable. Furthermore, GMO argues that the Commission's finding of imprudence is contrary to its "just and reasonable" prudence standard, whereby the prudence of a utility's costs

[1] The Company will frequently be referred to as "Aquila" in this pleading since the subject matter of this proceeding relates to the steam hedging program implemented by Aquila in 2006 and 2007.

is not based upon 20/20 hindsight. For these reasons, the Report and Order is unreasonable and rehearing is warranted.

3. GMO also argues in its Application for Rehearing that the Commission erroneously found that Aquila failed to meet its burden of dispelling purported doubts raised by the complainant, and erroneously sustained the objection to proper rebuttal testimony. Because there is no proper basis in the record for the Commission's finding that Aquila failed to meet its burden of proof, and because the Commission excluded evidence regarding Aquila's prudent administration of its steam hedging program, the Report and Order is unjust, unreasonable, arbitrary, capricious, unlawful, not supported by substantial and competent evidence of record, and not supported by adequate findings of fact and conclusions of law. Accordingly, rehearing should be granted.

4. Finally, GMO argues in its Application for Rehearing that the Commission improperly calculated the measure of damages, improperly and unlawfully expanded the scope of the Complaint to other steam customers in violation of the Quarterly Cost Adjustment Rider, and improperly failed to grant the Company's Motion to Dismiss. As a result, the Report and Order is unlawful, unreasonable, arbitrary, capricious, not supported by substantial and competent evidence of record, and not supported by adequate findings of fact. Consequently, rehearing should be granted.

II. <u>The Commission Found that Aquila's One-Third Strategy Is Prudent.</u>

5. Accusing GMO of "bootstrapping" justification for a hedging program into justification for imprudent implementation of a hedging program, AGP itself bootstraps its responsive brief regarding a rehearing application into a general attack on Aquila's hedging strategy. (AGP Response at 5-9). AGP criticizes Aquila for "locking in gas prices" and "leaving

GMO with no means of protecting the customers if gas prices dropped." (AGP Response at 6, 9).

6. Little room in this Reply needs to be spent to remind the Commission that it found Aquila was prudent in adopting a natural gas hedging program (Report and Order ¶ 25 at 9-10), and that Aquila's hedging program was prudently designed (Report and Order ¶ 31 at 11). AGP's arguments that Aquila did not follow its One-Third Strategy is the true "rabbit trail" of which AGP complains.

III. AGP Misunderstands GMO's Arguments Regarding the Burden of Proof.

7. Furthermore, AGP would have the Commission believe that GMO seeks rehearing because "Aquila should not have had the burden of proof." (AGP Response at 2). This is patently untrue. GMO has repeatedly acknowledged in its pleadings that the standard of review in this proceeding is a modified prudence standard. In criticizing GMO for "struggling" with the fact that the complaint procedure is to be used in this proceeding, AGP itself completely misunderstands GMO's arguments regarding the burden of proof. (AGP Response at 11-13).

8. GMO has never stated that it should not have the burden of proof, assuming that AGP created a serious doubt as to the prudence of the hedging program whereby the presumption of prudence would be overcome. Rather, GMO argues that (a) the burden was either improperly shifted or (b) once shifted, GMO met its burden or was not permitted to explain why it met its burden.

9. GMO's argument regarding the burden of proof in its Application for Rehearing has four elements: (1) the Commission erroneously shifted the burden of proof to Aquila by finding Aquila to be negligent in listening to its customers; (2) the Commission erroneously shifted the burden of proof to Aquila by engaging in improper 20/20 hindsight when it reviewed Aquila's hedging program for prudence; (3) even if the Commission did not

erroneously shift the burden of proof, Aquila met that burden; and (4) even if the Commission did not erroneously shift the burden of proof, the Commission improperly sustained AGP's objection to proper rebuttal testimony that would have allowed Aquila to meet its burden of proof.

A. The Commission Improperly Excluded GMO's Proper Rebuttal Testimony.

10. Importantly, if Aquila did bear the burden of dispelling any doubt created by AGP (as AGP claims), the Commission improperly prevented Aquila from dispelling the doubt created by AGP witness Donald Johnstone's Rebuttal testimony. It did so by excluding Aquila's offer of rebutting and clarifying testimony from GMO witness W. Edward Blunk and documentary evidence he was prepared to explain at the hearing. (Tr. at 335-338). While counsel for GMO did state that this testimony and evidence was "clarification," it was unquestionably proper rebuttal. Mr. Blunk advised the Commission, prior to AGP counsel's objection, that he had prepared a different chart that reflected his effort to "figure out what happened and come to grips myself with [whether] Aquila's actions [were] prudent or reasonable …." (Tr. at 335). In response to the objection, GMO counsel stated that the refinement of the chart in Exhibit 109 was offered to "enlighten the Commission" regarding Mr. Blunk's evaluation of the One-Third Strategy "just as Mr. Johnston [AGP's expert witness] did." (Tr. at 336).

11. Nevertheless, because the Commission improperly sustained AGP's objection to proper rebuttal testimony, Mr. Blunk was not given a chance to explain his chart or undergo cross-examination or Commissioner questions regarding it. Although the hearing Judge permitted GMO to put this rebuttal in its brief, argument in a brief is not evidence.

12. Mr. Blunk's chart, attached to GMO's Initial Brief as Exhibit A, demonstrates that Aquila's steam hedge program performed quite well in protecting its steam

customers from upward volatility of the price of natural gas ***while managing the variance between the steam customers' projected load requirements and actual usage***. See Exhibit A. This chart rebuts Mr. Johnstone's Chart Reb-2, upon which the Commission relied in making its finding that "Aquila's forecasted/budgeted natural gas usage far exceeded the actual amounts burned for steam production." (Report and Order ¶ 44 at 14, citing Johnstone Rebuttal, Ex. 2, Page 22, Chart Reb-2). The Commission's finding was the foundation for its determination that AGP "demonstrate[d] serious doubt" sufficient to overcome the presumption of prudence, shifting the burden of proof to GMO. (Report and Order ¶ 44 at 15). Thus, Mr. Blunk's chart and any related testimony not only is proper rebuttal, but also is directly relevant to the Commission's finding of imprudence.

13. Contrary to AGP's argument, GMO's failure to make a permissive offer of proof does not waive an objection or render the sustaining of the objection proper. As the Commission rule states: "Formal exceptions to rulings shall be unnecessary and need not be taken." See 4 CSR 240-2.130(3).

14. If this action truly "took on the character of a prudence review rather than a complaint" (Report and Order ¶ I at 18), the law requires that Aquila be afforded the procedural protections of such a review. Thus, exclusion of this rebuttal testimony and evidence was prejudicial error.

B. The Commission Improperly Determined This Proceeding to be a Full Prudence Review.

15. AGP's misunderstanding of GMO's arguments regarding the burden of proof may stem from its failure to grasp the difference between a prudence review, which GMO acknowledges is the proper standard for this proceeding, and a ***full*** prudence review, which is not the proper standard for this proceeding but which the Commission adopted as its standard.

16. As GMO explained in its Application for Rehearing, the Quarterly Cost Adjustment (QCA) Rider that governs steam service in this case provides a two-step approach to review prudence issues. In Step One, Commission Staff is to ascertain "that the concept of aligning of Company and customer interests is working as intended," and "that no significant level of imprudent costs is apparent." See Ex. 104, Schedule TMR-1 ("QCA Rider") at § 6.1. Staff "may proceed with Step Two, a full prudence review, if deemed necessary." See QCA Rider § 7 (emphasis added). This "full prudence review, if pursued, shall be complete[d] no later than 225 days after the end of each year." Id.

17. Staff's authorization to conduct a full prudence review is distinct from a customer's authorization to "initiate a complaint for the purpose of pursuing a prudence review by use of the existing complaint process." See QCA Rider § 8. There is nothing in Section 8 of the QCA Rider that creates a new breed of complaint or declares that a customer complaint is a "full prudence review," as contemplated in Section 7 when initiated by Staff. The Commission itself previously interpreted these provisions as "clearly setting out two different types of prudence reviews" -- a point that AGP notably fails to discuss in its Response. See Order Denying Motion to Dismiss at 4, Case No. HC-2010-0235 (July 21, 2010).

18. Nevertheless, without any factual or legal basis, the Commission found that this complaint case brought under the QCA Rider by AGP is "actually a full prudence review of Aquila's fuel purchasing decisions." (Report and Order ¶ E at 17, ¶ I at 18). Therefore, the Commission erroneously concluded: "Since this action is a full prudence review, it applies to all of Aquila's steam customers." See Report and Order ¶ J at 19 (emphasis added).

19. The decision of the Commission to award a refund to customers who never filed a complaint, based on its erroneous conclusion that this is a full prudence review, is neither lawful nor reasonable, is a denial of due process, and is unjust.

IV. AGP Misunderstands GMO's Arguments Regarding the Measurement of Damages.

20. Similarly, AGP mischaracterizes GMO's arguments regarding the Commission's improper calculation of the measure of damages as another "rabbit trail." (AGP Response at 2, 13). However, GMO's arguments regarding the measure of damages in its Application for Rehearing are sound.

21. First, as discussed above, because the Commission erroneously determined this proceeding to be a full prudence review, and therefore ordered GMO to refund that portion of the cost of the hedging program borne by all of its steam customers, the Report and Order is unlawful and unreasonable.

22. Second, the calculation of damages set forth by the Commission is flawed. Because there is (a) no evidence as to AGP's separate and discrete damages and (b) no evidence about what the costs of the program would have been had forecasts matched actual volumes or if the amount hedged had been within a "reasonable" variance to actual volumes, the measure of damages is woefully lacking support in the record. As a result, the Report and Order is not supported by substantial and competent evidence of record, is not supported by adequate findings of fact, and is, therefore, unreasonable.

23. Regarding damages point (a), in determining that "the relief ordered by the Commission should apply to all of Aquila's steam customers," the Commission failed to make any findings as to AGP's individual damages. If AGP is entitled to relief, there are no facts in the record to support any proper calculation of costs that were incurred solely by AGP as a result of Aquila's steam hedging program during 2006 and 2007.

24. As to damages point (b), the Commission erroneously ordered a refund of the entire net cost of Aquila's hedging program without any findings of fact or citations to the record that imprudence in the operation of the hedging program necessarily required a refund of

the entire cost of the program. The Commission reached this conclusion despite its candid acknowledgment that there would have been presumably proper and appropriate costs resulting from the operation of Aquila's hedging program even if the volume forecast had "been completely accurate." See Report and Order Decision at 19-20. Because there is no competent and substantial evidence in the record as to what the actual costs of the hedging program were, or as to the reasonable margin of error in hedging of volumes, the Commission's order that refunds the entire net cost of the program is unreasonable, arbitrary, and capricious.

V. Conclusion.

25. These Commission actions were unreasonable, arbitrary and capricious, and contrary to the letter and spirit of Section 386.266. As a result, the Report and Order is unjust, unreasonable, unlawful, not supported by substantial and competent evidence of record, and not supported by adequate findings of fact and conclusions of law.

Respectfully submitted,

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Certificate of Service

I hereby certify that on this 25th day of October, 2011 copies of the foregoing have been mailed, transmitted by facsimile, or emailed to all counsel of record.

/s/ Karl Zobrist
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