MISSOURI PUBLIC SERVICE COMMISSION

STAFF'S

RATE DESIGN

AND

CLASS COST-OF-SERVICE

REPORT

VEOLIA ENERGY KANSAS CITY, INC.

FILE NO. HR-2011-0241

Jefferson City, Missouri
September 2, 2011

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

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I. Executive Summary

Missouri Public Service Commission Staff (Staff) conducted a Class Cost-of-Service (CCOS) Study in this case and allocated costs to the customer rate classes of Veolia Energy Kansas City, Inc. (Veolia Kansas City or Company). Staff recommends no shift of cost between the classes.

Staff's rate design proposal includes the use of Veolia Kansas City's current rate design. Staff is recommending a percentage increase for all of Veolia Kansas City's customer classes based on the Staff's CCOS Study.

Staff is recommending a change to Veolia Kansas City's computation of its billing demand for its demand charges. Staff recommends that the computation of billing demand should be over a yearly period.

Staff Expert: Thomas M. Imhoff

II. Fundamental concepts of steam Class Cost-of-Service

Cost of Service: total costs, prudently incurred by a utility in providing services to its customers in a particular jurisdiction.

Cost-of-Service Study: a study that analyzes total company costs, adjusts them in accordance with regulatory principles (annualizations and normalizations), allocates these costs to the relevant jurisdiction, and compares the allocated costs to the revenues the utility is generating from its retail rates and other revenues. The results of a cost-of-service study are expressed in terms of additional revenue required for the utility to recover its cost of service.

CCOS Study: a quantitative analysis of the costs incurred by a utility to serve its various classes of customers. A Staff CCOS Study consists of these steps: a) costs are categorized (functionalized) based upon the specific role they play in the operations of a local distribution company (LDC); b) costs are classified by whether they are customer related, demand related, or energy related; and, c) functionalized/classified costs are allocated to customer classes. The sum of all allocated costs to a customer class is called the cost to serve that class.

The cost of service of each customer class is compared to the annualized, normalized revenues the utility collects from each class through its rates, plus each class' allocated share of revenues from other revenues, such as miscellaneous revenues. The results of a CCOS Study are expressed in terms of additional revenue required from each class for the utility to recover its cost of serving that class.

Relationship between Cost of Service and CCOS: conceptually, class cost of service is a breakdown of cost of service. A cost-of-service study determines what portion of total company costs is attributable to the retail jurisdiction; a CCOS Study determines what portion of retail costs is attributable to each customer class.

Cost Allocation: a procedure by which common or joint costs are apportioned among customers or classes of customers.

Cost Functionalization: the grouping of rate base and expense accounts according to the specific function they play in the operations of an LDC. The most aggregated functional categories are production, distribution, and revenue related.

Customer Class: a group of customers with similar characteristics (usage patterns, conditions of service, usage levels, etc.) that are identified for the purpose of setting rates for gas service.

Rate Design: (1) a process used to determine the rates for a gas utility once total cost of service is known; (2) characteristics such as rate structure, rate values and availability that define a rate schedule and provide the instructions necessary to calculate a customer's gas bill.

Rate Schedule: one or more tariff sheets that describe the availability requirements and prices applicable to a particular type of retail gas service. A customer class used in a CCOS Study may consist of one or more rate schedules.

Rate Values (Rates): the per-unit prices the utility charges to provide service to its customers. Rates are expressed as dollars per unit of volume (Mlbs) or per unit of energy (MMBtu, therm), etc.

Tariff: a document filed by a regulated entity with either a federal or state commission, it lists the rates (prices) the regulated entity will charge to provide service to its customers as well as the terms and conditions that it will follow in providing service.

Units of Measurement:

Btu: British thermal unit.

MMBtu: one million Btus. One MMBtu is approximately the amount of energy contained in 1,000 Cf (or 1 Mcf) of natural gas, 83.3 pounds of coal, 10.917 gallons of propane, 8 gallons of gasoline, or 293.083 kWh of electricity.

Cf: a unit of volume of one cubic foot of natural gas, which contains approximately 1,000 Btus of energy.

Therm: 100,000 Btus of energy, approximately equal to the energy contained in 100 Cfs of natural gas.

Mlbs: 1,000 pounds of steam.

III. General Description of the CCOS Study filed in HR-2011-0241

The purpose of the Staff's CCOS Study is to provide the Missouri Public Service Commission (Commission) with a measure of relative class cost responsibility for the overall revenue requirements of Veolia Kansas City. For individual items of cost, the responsibility of a certain class of customers to pay that cost can be either directly assigned or allocated to customer classes using reasonable methods for determining the class responsibility for that item of cost. The results are then summarized so that they can be compared to revenues being collected from each class on current rates. The difference between a particular customer class' costs responsibility and the revenues generated by that customer class is the amount that class is either paying in excess of its costs (revenues greater than costs) or the amount other classes are paying in excess of their respective costs.

The annualized usage levels and customer bill counts for the Standard Commercial Service, Large Commercial Service, Interruptible Heating Service, and Process Steam classes were provided by Staff witness Karen Lyons. The class peak demand levels were provided by Staff witness Daniel I. Beck and were based on data provided by the Company. All accounting information was developed using costs produced by the Auditing Department, the costs are based upon a test year ending December 31, 2010, updated for known and measurable changes through June 30, 2011.

IV. Customer Classes

Staff analyzed the costs and revenues of the following customer classes:

Standard Commercial Service (SCS)
Large Commercial Service (LCS)
Interruptible Heating Service (IHS)
Process Steam (PS)

These classes correspond to Veolia Kansas City current customer classes, except that the PS customers are not served from any tariff and are not regulated.

The SCS class is available to all customers using 5,000 Mlbs, or less, of total annual steam. The LCS class is comprised of those customers with an annual usage of more than 5,000 Mlbs (unless their demand cannot reasonably or accurately be measured with a demand meter). The IHS class is available to certain customers with less than 100,000 Mlbs of annual steam consumption who have the ability to space heat all of their space without the Company's service.

The Company's costs were first categorized into functional areas that are to be allocated by their function (Production, Distribution, etc.). This is referred to as cost functionalization. The rate base and expense accounts are assigned to one of the following functional categories: Production, Distribution Mains, Distribution Measuring and Regulating, Distribution Meters, Distribution Services, Billing, Meter Reading, and Revenue Related.

Those costs which cannot be directly assigned into any of these specific functional categories, are divided among several functions based upon some relational factor. For example, it is reasonable to assume that property taxes are related to gross plant costs and can therefore be functionalized in the same manner as gross plant costs.

The allocation factor for Distribution Mains, as well as those for Distribution Meters, and Distribution Service Lines were developed by using the allocation factors developed by Staff witness Daniel I. Beck. Meter Reading costs were allocated using weighted customer numbers. Revenue Related costs were allocated based upon the Staff's annualized margin revenues.

The results of the Staff's CCOS Study for the Company are shown on Schedule 2. The CCOS Study is presented in terms of revenue requirements before any increase in the Company's respective revenue requirements. These results show that Standard Commercial Service, Large Commercial Service, and Interruptible Heating Service classes' revenues are insufficient to cover their costs, while the Process Steam class' revenues are in excess of their costs.

Staff Experts/Witnesses: *Thomas A. Solt*
Daniel I. Beck

V. Billing Demand

Veolia Kansas City currently computes its billing demand charge using the time period from December 31 th rough March 31. This tim e period fails to tak e into account those customers who are summer peaking. Staff pr oposes the billing dem and language should be changed to an annual tim e frame. By com puting the billing dem and on an annual basis, all customers who should be paying a billing demand charge will be charged for the service. The billing demand for a custom er is based on their highest hourly peak cons umption of steam in any 60-minute interval in the two immediately preceding, completed time frames.

Staff expert: Thomas M. Imhoff

VI. Rate Design

A. Overview

Veolia Kansas City's steam operations provide service to approxim ately 62 commercial and industrial custom ers located in the downtown Kans as City area. Subsequent to the previous rate case, Case No. HR-2008- 0300, Veolia Kansas City operated as Trigen Kansas City Energy Corporation (Trigen). In Case No. HN-2011-0286, at the request of the Company, the Commission authorized the Compa ny name change from Trigen to Veolia. Prior to 1990 the Company's steam operation was part of Kansas City Powe r & Light Company. In Case No. HM-90-4, the Commission authorized the sale of those assets from Kansas City Power & Light to Trigen and authorized the Company to provide steam service in the designated Kansas City area.

B. Existing Rate Design

Veolia Kansas City pre sently has three st eam rate s chedules: SCS tariff, LCS, and IHS. Staff has evaluated these schedules and normalized and annualized the billing units to more accurately dep ict Veolia Kan sas City's steam costs and revenue on a going-forward

basis. For more detailed information on the adjustments to steam sales and rate revenue included in Staff's case, please see the "Income Statement" section of the Cost of Service Report authored by Staff witness Karen Lyons. Consistent with the revenue requirement determination, Staff developed billing units for the proposed rates on a weather-normalized and annualized basis for the test year customers.

C. Veolia Kansas City's Proposed Rate Design

Veolia Kansas City is proposing to maintain its' current customer classes, SCS, LCS, and IHS. In the current classes, customers are well differentiated based on usage. The current structure divides firm customers (SCS and LSC) based on usage (greater or less than 5,000 Mlbs/year), and provides demand metering for the larger customer class (IHS). Staff finds these classes acceptable in that rate structures that reflect fixed and variable costs have been found to be an appropriate means of cost recovery. Further measuring demand to better determine load provides both Veolia Kansas City and its customers more visibility into their usage patterns.

D. Staff's Analysis of Veolia's Proposed Rate Changes

Staff weather-normalized and annualized usage for each individual customer as Veolia Kansas City did. However, Staff adjusted its starting point to reflect the Class Cost of Service (CCOS) analysis. As a result, the percentage increase needed to reach CCOS revenue requirement was approximately 15.0%, rather than the 19.1% proposed by Veolia. Staff applied this CCOS percentage increase to Staff's adjusted current revenue for each rate class to determine that class's revenue target.

Veolia Kansas City's rate structure includes Demand or Capacity charges for the larger customers. Due to Staff's adjustments for weather normalization, annualization of the

number of customers, and differences in peak data, Staff's revenue calculation for each class differed from that calculated by Veolia Kansas City.

Staff used the class target revenues as calculated above to make adjustments to Veolia Kansas City's proposed rates. Veolia Kansas City's proposed rate structure includes the same usage charge across all rates (implicit in the SCS class as part of its Steam Charge), a blocked Demand or Capacity charge, and a meter charge. When making the rate adjustments, the usage charge and meter charges were held constant. In Staff's analysis, for the SCS class, each block of the Steam Charge was adjusted by an equal percentage toward the target class revenue. For the LCS and IHS classes, Staff adjusted the rate for each block of the Demand and Capacity Charges, respectively, by toward the combined target revenue. Proposed class billing units, rates, and revenue are at Appendix II, Schedules HW 1-1.

Staff Expert: Henry Warren

BEFORE THE PUBLIC SERVICE COMMISSION

OF THE STATE OF MISSOURI

In the Matter of Veolia Energy Kansas City, Inc's. Tariffs to Increase Rates	))	File No. HR-2011-0241

AFFIDAVIT OF THOMAS M. IMHOFF

STATE OF MISSOURI)
) **ss**
COUNTY OF COLE)

Thomas M. Imhoff, employee of the Staff of the Missouri Public Service Commission, being of lawful age and after being duly sworn, states that he has participated in the preparation of the accompanying Staff Report on pages 1 + 5, and the facts therein are true and correct to the best of his knowledge and belief.

Thomas M. Imhoff

Subscribed and sworn to before me this 2nd day of September, 2011.

Notary Public

SUSAN L. SUNDERMEYER
Notary Public - Notary Seal
State of Missouri
Commissioned for Callaway County
My Commission Expires: October 03, 2014
Commission Number: 10942086

BEFORE THE PUBLIC SERVICE COMMISSION

OF THE STATE OF MISSOURI

In the Matter of Veolia Energy Kansas City, Inc's. Tariffs to Increase Rates	))	File No. HR-2011-0241

AFFIDAVIT OF THOMAS A. SOLT

STATE OF MISSOURI)
) **ss**
COUNTY OF COLE)

Thomas A. Solt, employee of the Staff of the Missouri Public Service Commission, being of lawful age and after being duly sworn, states that he has participated in the preparation of the accompanying Staff Report on pages 1-4, and the facts therein are true and correct to the best of his knowledge and belief.

Thomas A. Solt

Subscribed and sworn to before me this 2nd day of September, 2011.

SUSAN L. SUNDERMEYER
Notary Public - Notary Seal
State of Missouri
Commissioned for Callaway County
My Commission Expires: October 03, 2014
Commission Number: 10942086

Notary Public

BEFORE THE PUBLIC SERVICE COMMISSION

OF THE STATE OF MISSOURI

In the Matter of Veolia Energy Kansas City, Inc's. Tariffs to Increase Rates	))	File No. HR-2011-0241

AFFIDAVIT OF HENRY E. WARREN

STATE OF MISSOURI)
) **ss**
COUNTY OF COLE)

Henry E. Warren, employee of the Staff of the Missouri Public Service Commission, being of lawful age and after being duly sworn, states that he has participated in the preparation of the accompanying Staff Report on pages 5-7, and the facts therein are true and correct to the best of his knowledge and belief.

Henry E. Warren

Subscribed and sworn to before me this 2nd day of September, 2011.

SUSAN L. SUNDERMEYER
Notary Public - Notary Seal
State of Missouri
Commissioned for Callaway County
My Commission Expires: October 03, 2014
Commission Number: 10942086

Notary Public

Thomas A. Solt

Present Position:

I am an auditor in the Gas Rates and Tariffs Section of the Energy Department, Operations Division of the Missouri Public Service Commission.

Educational Background and Work Experience:

I have a Bachelor of Science degree in Business Administration from the University of Missouri—St. Louis, and a Master's degree in Public Administration from the University of Missouri--Columbia. I am a licensed certified public accountant, hold other professional certifications, and have been employed by the Missouri Public Service Commission since May, 1992, except for approximately four months in late 1997 and early 1998.

Thomas A. Solt

Education

Master's Degree in Public Administration
University of Missouri—Columbia, 1999

Bachelor of Science Degree in Business Administration
University of Missouri—St. Louis, 1987

Professional Certifications

Certified Government Financial Manager, November 1996
Certified Internal Auditor, August 1995
Certified Public Accountant, August 1988
Commercial Pilot, Single-engine Land and Sea, Multi-engine Land, Glider
Certified Flight Instructor—Instrument, Single- and Multi-engine, Airplane

Professional Experience

Missouri Public Service Commission, Jefferson City, MO
2004-Present, Auditor, Energy Department
1999-2004, Auditor, Telecom Department
1998-1999, Auditor, Gas Department
1996-1997, Policy Analyst, Federal Telecom Department
1994-1996, Energy Department
1992-1994, Auditor, Accounting Department,

Schedule 1
Thomas A. Solt

Company Case	Number	Issue
St. Joseph Light & Power Co. GR-93-42	ER-93-41 &	Payroll, payroll taxes, management incentive plan, 401(k) plan, advertising
Western Resources, Inc.	GR-93-240	Plant-in-service, depreciation reserve, depreciation expense, materials & supplies, prepayments, customer advances, customer deposits, property taxes, and property insurance
The Empire District Electric Co.	ER-94-174	Tariff issues
Missouri Gas Energy	GR-95-33	Recovery of FERC transition costs
Missouri Gas Energy	GR-98-140	Tariff issues
Missouri Universal Service Fund	TO-98-329	USF surcharge
Southwestern Bell Telephone Co.	TT-2000-258	Local Plus availability, ordering, and tariff approval
Southwestern Bell Telephone Co.	TT-2000-667	Local Plus
Ozark Telephone Co. TC-2001-402	TT-2001-117 &	Rate design
Relay Missouri Proceeding	TO-2003-0171	Relay surcharge
Fidelity Telephone Company	IR-2004-0272	Rate design
Atmos Energy Corporation	GR-2006-0387	Overview
Missouri Gas Energy	GR-2006-0422	Class cost of service
Union Electric Co. d/b/a AmerenUE	GR-2007-0003	Class cost of service
Laclede Gas Company	GR-2007-0208	Overview
Missouri Gas Utility	GR-2008-0060	Class cost of service

Laclede Gas Company	GT-2008-0026	Bad debts though PGA
Missouri Gas Energy	GR-2009-0355	Class cost of service
Empire District Gas Company	GR-2009-0434	Overview
Laclede Gas Company	GR-2010-0171	Miscellaneous Tariff Issues
Southern Missouri Natural Gas	GR-2010-0347	Overview
AmerenUE	GR-2010-0363	Miscellaneous Tariff Issues
Southern Missouri Natural Gas	GR-2010-0347	Rate Design, Tariff Issues

HENRY WARREN, PHD

REGULATORY ECONOMIST
UTILITY OPERATIONS DIVISION
ENERGY DEPARTMENT

EDUCATION AND EXPERIENCE

I received my Bachelor of Arts and my Master of Arts in Economics from the University of Missouri-Columbia, and a Doctor of Philosophy (PhD) in Economics from Texas A&M University. Prior to joining the PSC Staff (Staff), I was an Economist with the U.S. National Oceanic and Atmospheric Administration (NOAA). At NOAA I conducted research on the economic impact of climate and weather. I began my employment at the Commission on October 1, 1992 as a Research Economist in the Economic Analysis Department. My duties consisted of calculating adjustments to test-year energy use based on test-year weather and normal weather, and I also assisted in the review of Electric Resource Plans for investor owned utilities in Missouri. From December 1, 1997, until May 2001, I was a Regulatory Economist II in the Commission's Gas Department, where my duties included analysis of issues in natural gas rate cases and were expanded to include reviewing tariff filings, applications and various other matters relating to jurisdictional gas utilities in Missouri. On June 1, 2001 the Commission organized an Energy Department and I was assigned to the Tariff/Rate Design Section of the Energy Department. My duties in the Energy Department include analysis of issues in rate cases of natural gas and electric utilities, tariff filings, applications, and various other matters relating to jurisdictional gas and electric utilities in Missouri, including review of Electric Resource Plans and Regulatory Plans for investor owned electric utilities in Missouri. I have also served on various task forces, collaboratives, and working groups dealing with issues relating to jurisdictional natural gas and electric utilities.

MISSOURI PUBLIC SERVICE COMMISSION

CASES IN WHICH PREPARED TESTIMONY,

REPORT, OR REVIEW WAS SUBMITTED BY:

HENRY E. WARREN, PHD

COMPANY NAME	CASE NUMBER
St. Joseph Light and Power Company	GR-93-042[1]
Laclede Gas Co.	GR-93-149
Missouri Public Service	GR-93-172[1]
Western Resources	GR-93-240[1]
Laclede Gas Co.	GR-94-220[1]
Kansas City Power & Light Co.	EO-94-3601[2]
United Cities Gas Co.	GR-95-160[1]
UtiliCorp United, Inc.	EO-95-187[2]
The Empire District Electric Co.	ER-95-279[1]
The Empire District Electric Co.	EO-96-56[2]
St. Joseph Light and Power Company	EO-96-198[2]
Laclede Gas Co.	GR-96-193[1]
Missouri Gas Energy	GR-96-285[1]
The Empire District Electric Co.	ER-97-081[1]
Union Electric Co.	GR-97-393[1]
Missouri Gas Energy	GR-98-140[1]
Laclede Gas Co.	GR-98-374[1]
St. Joseph Light & Power Company	GR-99-246[1]
Laclede Gas Co.	GR-99-315[1]
Union Electric Company (d/b/a AmerenUE)	GR-2000-512[1]
Missouri Gas Energy	GR-2001-292[1]
Laclede Gas Co.	GR-2001-629[1]

[1]Testimony includes computations to adjust test year volumes, therms, or kWh to normal weather.

[2]Staff Report or Review

MISSOURI PUBLIC SERVICE COMMISSION

CASES IN WHICH PREPARED TESTIMONY,

REPORT OR REVIEW WAS SUBMITTED BY:

HENRY E. WARREN, PHD

(CONTINUED)

COMPANY NAME	CASE NUMBER
Laclede Gas Company	GC-2002-0110[2]
Laclede Gas Company	GR-2002-0356[1]
Aquila, Inc.	GC-2003-0131[2]
Laclede Gas Company	GC-2003-0212[2]
Laclede Gas Company	GT-2003-0117
Aquila, Inc., (d/b/a Aquila Networks MPS and L&P)	GR-2004-0072[1]
Missouri Gas Energy	GR-2004-0209
Laclede Gas Company	GC-2004-0240[2]
Kansas City Power & Light Company	EO-2005-0329[2]
Union Electric Company (d/b/a AmerenUE)	EO-2006-0240[2]
The Empire District Electric Company	ER-2006-0315
The Atmos Energy Corporation	GR-2006-0387[1]
Missouri Gas Energy	GR-2006-0422[1]
Union Electric Company (d/b/a AmerenUE)	GR-2007-0003[1]
Kansas City Power & Light Company	EO-2007-0008[2]
Aquila, Inc., (d/b/a Aquila Networks MPS and L&P)	EO-2007-0298[2]
Laclede Gas Company	GR-2007-0208[2]
Missouri Gas Energy – The Empire District Gas Company	GA-2007-0289, et al
Union Electric Company (d/b/a AmerenUE)	EO-2007-0409[2]

[1]Testimony includes computations to adjust test year volumes, therms, or kWh to normal weather.

[2]Staff Report or Review

MISSOURI PUBLIC SERVICE COMMISSION

CASES IN WHICH PREPARED TESTIMONY,

REPORT OR REVIEW WAS SUBMITTED BY:

HENRY E. WARREN, PHD

(CONTINUED)

The Empire District Electric Company	EO-2008-0069[2]
Union Electric Company (d/b/a AmerenUE)	ER-2008-0318
Missouri Gas Energy	GR-2009-0355[1]
The Empire District Gas Company	GR-2009-0434
The Empire District Electric Company	ER-2010-0130
Laclede Gas Company	GR-2010-0171[2]
Atmos Energy Corporation	GR-2010-0192
Chairman's Request for Status Report Regarding Energy Efficiency …	AO-2011-0035[2]
Kansas City Power & Light	ER-2010-0355[2]
Kansas City Power & Light (Surrebuttal)	ER-2010-0355
KCP&L - Greater Missouri Operations	ER-2010-0356[2]
KCP&L - Greater Missouri Operations (Surrebuttal)	ER-2010-0356
Union Electric Company (d/b/a Ameren Missouri)	GR-2010-0363[2]
Union Electric Company (d/b/a Ameren Missouri) (Rebuttal)	GR-2010-0363
Union Electric Company (d/b/a Ameren Missouri)	ER-2011-0028[2]
Empire District Electric Company	ER-2011-0004[2]

[1]Testimony includes computations to adjust test year volumes, therms, or kWh to normal weather.

[2]Staff Report or Review

Veolia Energy Kansas City
CASE NO. HR-2011-0241
TEST YEAR ENDED December 31, 2010
C-O-S RESULTS

	TOTAL	Standard Commercial Service	Large Commercial Service	Interruptible Heating Service	Process Steam
RATE BASE	$16,791,316	$669,685	$6,073,186	$2,306,846	$7,741,600
REQUESTED RETURN	7.31%	7.31%	7.31%	7.31%	7.31%
RETURN ON RATE BASE	$1,227,781	$48,967	$444,071	$168,677	$566,066
O & M EXPENSES	$19,054,589	$840,655	$6,669,227	$2,611,490	$8,933,217
DEPRECIATION EXPENSE	$796,293	$35,317	$286,655	$110,035	$364,286
TAXES OTHER THAN INCOME	$639,208	$27,155	$225,482	$87,413	$299,159
INCOME TAXES	($1,111,917)	($44,346)	($402,165)	($152,759)	($512,647)
TOTAL EXPENSES	$19,378,173	$858,780	$6,779,199	$2,656,180	$9,084,014
TOTAL C-O-S	$20,605,954	$907,747	$7,223,270	$2,824,856	$9,650,080
OTHER REVENUES	$229,222	$10,098	$80,352	$31,424	$107,348
REQUIRED MARGIN REVENUE	$20,376,732	$897,649	$7,142,918	$2,793,432	$9,542,732
CURRENT MARGIN REVENUES	$19,320,598	$565,003	$5,701,109	$795,030	$12,259,456
	$1,056,134	$332,646	$1,441,809	$1,998,402	($2,716,724)
ZERO REVENUE INCREASE PLUG	($1,056,134)	($46,526)	($370,220)	($144,785)	($494,604)
C-O-S MARGIN REVENUES @ 0%	$19,320,598	$851,124	$6,772,698	$2,648,648	$9,048,128

Appendix II – Schedule HW-1

Is Deemed

Highly Confidential

In Its Entirety