Exhibit No.:	
Issue:	
Witness:	Gary L. Clemens
Type of Exhibit:	Direct Testimony
Sponsoring Party:	KCP&L Greater Missouri Operations Company
Case No.:	HC-2010-0235
Date Testimony Prepared:	October 22, 2010

MISSOURI PUBLIC SERVICE COMMISSION

CASE NO.: HC-2010-0235

DIRECT TESTIMONY

OF

GARY L. CLEMENS

ON BEHALF OF

KCP&L GREATER MISSOURI OPERATIONS COMPANY

Kansas City, Missouri
October 2010

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.	)	

AFFIDAVIT OF GARY L. CLEMENS

STATE OF MISSOURI)
) ss
COUNTY OF JACKSON)

Gary L. Clemens, being first duly sworn on his oath, states:

1. My name is Gary L. Clemens. I work in Kansas City, Missouri, and I am self-employed as a utility consultant.

2. Attached hereto and made a part hereof for all purposes is my Direct Testimony on behalf of KCP&L Greater Missouri Operations Company consisting of nine (9) pages, having been prepared in written form for introduction into evidence in the above-captioned docket.

3. I have knowledge of the matters set forth therein. I hereby swear and affirm that my answers contained in the attached testimony to the questions therein propounded, including any attachments thereto, are true and accurate to the best of my knowledge, information and belief.

Gary L Clemens
Gary L. Clemens

Subscribed and sworn before me this 21st day of October 2010.

Nicole A. Wehry
Notary Public

My commission expires: Feb. 4, 2011

" NOTARY SEAL "
Nicole A. Wehry, Notary Public
Jackson County, State of Missouri
My Commission Expires 2/4/2011
Commission Number 07391200

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DIRECT TESTIMONY

OF

Gary L. Clemens

Case No. HC-2010-0235

Q: Please state your name and business address.

A: My name is Gary L. Clemens, and my business address is 6805 N. Hardesty Avenue, Kansas City, Missouri 64119.

Q: By whom are you employed, what is your job title, and what are your job responsibilities?

A: I am a self-employed utility consultant.

Q: Please briefly describe your education and work experience.

A: I attended Northwest Missouri State University, Maryville, Missouri, from which I was awarded a Bachelor of Science Degree in Business Administration with a major in Accounting. After graduation in 1980, I joined Aquila, Inc. (Missouri Public Service at that time) as a Staff Accountant in Regulatory Services. From 1980 through July 2008, I held various positions in the Accounting and Regulatory Services departments with my final position being Senior Director of Regulatory Services.

Q. Have you previously testified in a proceeding at the Missouri Public Service Commission or before any other utility regulatory body?

A. Yes, I have testified on numerous occasions before the Missouri Public Service Commission as well as the Federal Energy Regulatory Commission.

Q: On whose behalf are you testifying?

A: I am testifying on behalf of KCP&L Greater Missouri Operations Company, formerly known as Aquila, Inc. (generally referred to as "Aquila" or "Company" below).

Q: What subjects are addressed in your testimony?

A: I will discuss the inclusion of natural gas hedging costs in the Nonunanimous Stipulation and Agreement reached in Aquila's 2005 steam rate case, Case No. HR-2005-0450 ("2005 Steam Rate Case") in which the first Quarterly Cost Adjustment ("QCA") was implemented. I will also discuss: (a) the participation of Ag Processing, Inc. ("AGP") and its representatives as a party in the 2005 Steam Rate Case, specifically in the development of the QCA; (b) the agreement and understanding by all parties to the 2005 Steam Rate Case that Aquila's natural gas hedging program would be included in the QCA; and, (c) subsequent events and discussions in 2007 and 2008.

Q: In the Direct Testimony of AGP witness Donald Johnstone at pages 5 and 31, Mr. Johnstone suggests that the Company did not discuss the hedging program with the steam customers prior to implementing the program. Is this true?

A: No. I was heavily involved in Aquila's 2005 Steam Rate Case and have personal knowledge of the involvement of AGP and its representatives in the course of that case and in its ultimate resolution. I can state without qualification that AGP played an integral part in the development of the QCA in that case, which was designed to include a program for natural gas hedging. AGP was also a party to Aquila's 2005 electric rate case, Case No. ER-2005-0436 ("2005 Electric Rate Case") where issues regarding the Company's natural gas hedging program were prominent.

Q: What was AGP's involvement in the 2005 Steam Rate Case?

A: AGP was fully engaged in the negotiations and drafting of the nonunanimous stipulations and agreements in both the 2005 Steam Rate Case and 2005 Electric Rate Case. AGP was a signatory to each of the stipulations that resolved these cases.

Q: Did the Nonunanimous Stipulation and Agreement ("Stipulation") in the 2005 Steam Rate Case provide for a natural gas hedging program and the recovery of its costs?

A: Yes. Natural gas hedging programs were included in the Stipulation. Section 8.1 of the Stipulation provided: "The cost of gas in Account 501 will include the cost of physical gas deliveries and financial instruments, when settled, associated with gas delivered in the quarterly period." See Schedule GLC-1 at 5. The parties to the case discussed and understood the term "financial instruments" to mean the futures contracts and option contracts that had been used in Aquila's natural gas hedging program that Aquila had used for certain of its electric operations, and that would be used for its steam operations in St. Joseph.

Q: How did AGP and other parties become aware of the gas hedging program?

A: Aquila's response to Commission Staff's Data Request No. MPSC-0266 describes the gas hedging program and its procedures. See Schedule GLC-2 (relevant excerpts attached). This response is referenced in the Direct Testimony that Maurice Brubaker filed on October 14, 2005 in both the 2005 Steam Rate Case and the 2005 Electric Rate Case, which Mr. Brubaker filed on behalf of AGP.

On page 4 of his Direct Testimony in the 2005 Steam Rate Case, Mr. Brubaker stated that Aquila had a hedging program for its purchased energy requirements and that the program had been described in responses to the data requests. Mr. Brubaker stated:

"The purpose of a hedging program is to moderate the effects of rising and falling prices of the commodity being acquired." On page 4, line 19, he was asked: "In your view, would it be appropriate to reflect the effects of the hedging program?" In response Mr. Brubaker stated: "Yes. As noted above, the main purpose of the hedging program is to dampen the price swings in the market, and to otherwise protect consumers from increases in price. Unless the results of the hedging program are reflected in determining the prices to be charged to consumers, this objective will not be met. Rather, consumers would continue to be exposed to the effects of market volatility, and the hedging program would basically benefit stockholders, rather than consumers. Especially in light of the high and volatile gas prices currently being faced, it is appropriate for the effects of the hedging program to be reflected in determining the fuel and purchase power costs properly chargeable to consumers." See Schedule WEB-6 (attached to the Direct Testimony of Company Witness Wm. Edward Blunk).

Q: Did Aquila have a natural gas hedging program in place for its industrial steam production needs at the Lake Road Plant in St. Joseph before February 2006 when the Stipulation was signed?

A: No. Based upon the testimony filed by Staff and by AGP in the 2005 Steam Rate Case, as well as Aquila's discussions with the parties to the case, especially AGP, Aquila decided to take the gas hedging program that had been used in its electric operations side and that had been discussed with Staff and other parties, and implement it with respect to its steam operations in St. Joseph. Aquila would not have implemented a gas hedging program for its steam operations if AGP had not requested that it do so.

Q: Why did Aquila believe that the gas hedging program used for its electric operations was an acceptable program?

A: The program had been discussed on several occasions with Staff, AGP, and other parties, beginning in the summer of 2004. As shown in Aquila's August 10, 2005 response to Staff's Data Request No. MPSC-0266, Aquila provided an update to its hedging strategy in a memorandum entitled "Missouri Natural Gas & Purchase Power Hedge Strategy – Implementing the Market Neutral Approach – Update" which had been prepared on February 25, 2005. See Schedule GLC-2 at 2. The response to this Staff DR also provided AGP and other parties with the Resource Planning presentation made to Commission Staff and the Office of the Public Counsel on July 9, 2004, which described in detail Aquila's 2005-07 hedging strategy. See Schedule GLC-2 at 5–20. I was present at this meeting. Both of these documents set forth in detail the "One-Third Strategy" pursuant to which one-third of gas purchases would set by fixed-price futures contracts, one-third by options contracts, and one-third purchased on the open market. See Schedule GLC-2 at 3, 13–14.

No party to the 2005 Steam Rate Case, including AGP, raised any objections to the hedging strategy employed by Aquila or requested that Aquila enter into a different hedging program. The signatory parties to the Stipulation were Aquila, Commission Staff, AGP, and the City of St. Joseph. The Stipulation was approved by the Commission without change on February 28, 2006, effective March 6, 2006.

Q: In addition to the information on Aquila's hedging program that was distributed to the parties to the 2005 Steam Rate Case, how else was AGP made aware of and

involved in the decision to hedge natural gas for the industrial steam customers of the Lake Road Plant?

A: AGP participated in numerous discussions during the course of the 2005 Steam Rate Case during which the parties exchanged documents regarding what became the QCA process. For example, AGP consultant and expert witness Mr. Johnstone circulated a proposal on January 16, 2006 which contained a proposed Section 4.1 that stated: "The cost of gas will include the cost of physical gas deliveries and financial instruments associated with gas delivered in the quarterly period." See Schedule GLC-3. This concept was eventually reflected in Section 8.1 of the Stipulation, quoted above, as well as in the QCA tariff sheets themselves. Numerous revisions were discussed during the settlement process, but the above referenced wording remained largely unchanged and was included in the final Stipulation as well as the tariff, with the minor addition that the cost of gas will include the cost of physical gas deliveries and financial instruments "when settled." See Schedule GLC-1 at 5.

Q: Mr. Johnstone states at pages 5 and 7 of his Direct Testimony that the Aquila hedging program was not needed for steam operations because the QCA mechanism mitigates the effect of fuel cost volatility and price spikes, and that Aquila ignored this effect. Was the QCA designed to be a hedging program?

A: No. First of all, the aspect of the QCA mechanism to which it appears Mr. Johnstone is referring is the 80/20 sharing formula described in Section 8 and Section 8.6 of the Stipulation. Under this formula, Aquila is responsible for 20% of the change in fuel costs and is only permitted to charge customers 80% of the change in fuel costs. Section 8.3

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additionally provides that any quarterly changes in costs will be collected over twelve months.

Second, his discussion of coal performance standards has nothing to do with price volatility and spikes in the natural gas markets. The purpose of these standards was to encourage the efficient operation of the coal-fired Boiler No. 5, as indicated in Section 8.2 and Appendix D to the Stipulation.

Finally, the parties to the Stipulation, particularly Aquila and AGP, contemplated that a program of financial instruments and hedging would be an integral part of the overall QCA mechanism. This is demonstrated by the Direct Testimony of AGP's witness Maurice Brubaker who, as noted above, recommended that the results of the hedging program used by Aquila be used to formulate rates charged to customers. Section 8.1 specified that the cost of natural gas "will include the cost of physical gas deliveries and financial instruments, when settled, associated with gas delivered in the quarterly period." See Schedule GLC-1 at 5.

Mr. Johnstone's remarks on page 11 of his Direct Testimony that no hedging program was needed and that Mr. Williams gave "fundamentally bad advice" in authorizing the gas hedging program are totally at odds with what actually occurred. Mr. Johnstone's testimony ignores the positions taken by AGP in the 2005 Steam Rate Case, including discussions in which I participated. It also is contrary to the plain language of Section 8.1 of the Stipulation. His comment about Mr. Williams is unfair and unwarranted.

Q. Was AGP kept informed of the impact that the hedging program for Aquila's steam operations in St. Joseph was having on natural gas costs?

A. Yes. Pursuant to the approved tariffs, a QCA filing is made quarterly through the Commission's electronic filing and information system (EFIS). For example, in Case No. HR-2007-0028, Aquila filed a steam tariff sheet with the current QCA data reflecting fuel costs and other data for the second quarter (April–June) of 2006. Under the heading "Fuel Costs - 2006" was the line item: "Hedging Costs - 2006." With Staff's favorable recommendation, the Commission approved the tariff on August 29, 2006. See Schedule GLC-4. AGP was a party to this proceeding. This process was also followed in the fall of 2006, of which AGP received notice. See Schedule GLC-5.

Each of these QCA filings included the calculation of the new QCA rate which specified gas hedging costs as a separate item within the accumulation of the quarterly fuel costs.

Q. After the QCA process and the hedging program for steam operations was implemented, did representatives of AGP comment on the results of the program?

A. Yes. On numerous occasions during 2007 and 2008 I and other Aquila representatives, particularly Dennis Williams and Davis Rooney, met with representatives of AGP, in particular Mr. Johnstone and AGP's counsel Stuart W. Conrad. The price of natural gas had fallen substantially in 2006 and 2007, and the estimates of steam usage provided by St. Joseph steam customers fell short. Consequently, the hedging program produced losses. Beginning in the fall of 2007, Aquila asked AGP for its feedback on the hedging program, including whether it should be changed or discontinued. In response to these requests and after some discussion, Mr. Johnstone sent me an email dated October 30, 2007 that confirmed AGP's request that Aquila suspend the gas hedging program as it related to the steam operation effective November 1, 2007. See Schedule GLC-6. Aquila complied with this request.

Q. Did Aquila continue to meet with AGP representatives with regard to the steam hedging program and hedging issues?

A: Yes. From the fall of 2007 into the summer of 2008 until the time that Aquila was acquired by Great Plains Energy Inc., I and other Aquila representatives met with Mr. Johnstone and Mr. Conrad about these issues.

Q: Does that conclude your testimony?

A: Yes, it does.