

**BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI**



In the Matter of Kansas City Power & Light)	<u>File No. ER-2014-0370 et al.</u>
Company's Request for Authority to Implement a)	YE-2015-0194
General Rate Increase for Electric Service)	YE-2015-0195

REPORT AND ORDER

Issue Date: September 2, 2015

Effective Date: September 15, 2015

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REPORT AND ORDER

I. Procedural History

A. Tariff Filings, Notice, and Intervention

On October 30, 2014, Kansas City Power & Light Company (“KCPL”) filed tariff sheets designed to implement a general rate increase for utility service. The tariff sheets bore an effective date of November 29, 2014. In order to allow sufficient time to study the effect of the tariff sheets and to determine if the rates established by those sheets are just, reasonable, and in the public interest, the tariff sheets were suspended until September 29, 2015. The Commission directed notice of the filings and set an intervention deadline. The Commission granted intervention requests from the following entities: the Missouri Department of Economic Development- Division of Energy, Midwest Energy Consumers Group, Missouri Industrial Energy Consumers, Brightergy, LLC, Sierra Club, Consumers Council of Missouri, U.S. Department of Energy and Federal Executive Agencies, Union Electric Company d/b/a Ameren Missouri, Missouri Gas Energy, the City of Kansas City, Missouri, and the International Brotherhood of Electrical Workers Local Unions No. 412, 1464, and 1613. On January 30, 2015, the Commission consolidated this case with a related matter in File No. EU-2015-0094.

B. Test Year and True-Up

The test year is a central component in the ratemaking process. Rates are usually established based upon a historical test year which focuses on four factors: (1) the rate of return the utility has an opportunity to earn; (2) the rate base upon which a return may be earned; (3) the depreciation costs of plant and equipment; and (4) allowable operating

expenses.¹ From these four factors is calculated the “revenue requirement,” which, in the context of rate setting, is the amount of revenue ratepayers must generate to pay the costs of producing the utility service they receive while yielding a reasonable rate of return to the investors.² A historical test year is used because the past expenses of a utility can be used as a basis for determining what rate is reasonable to be charged in the future.³

The parties agreed to, and the Commission adopted, a test year of twelve months ending on March 31, 2014, updated through December 31, 2014. The Commission also established the true-up period to run through May 31, 2015, to reflect any significant and material impacts on KCPL’s revenue requirement. The use of a true-up audit and hearing in ratemaking is a compromise between the use of a historical test year and the use of a projected or future test year.⁴ It involves adjustment of the historical test year figures for known and measurable subsequent or future changes.⁵ However, the true-up is generally limited to only those accounts necessarily affected by some significant known and measurable change, such as a new labor contract, a new tax rate, or the completion of a new capital asset. The true-up is a device employed to reduce regulatory lag, which is “the lapse of time between a change in revenue requirement and the reflection of that change in rates.”⁶

C. Local Public Hearings

On December 3, 2014, some of the parties filed a *Joint Proposed Procedural Schedule*, which included a recommendation for the dates and locations for local public

¹ *State ex rel. Union Electric Company v. Public Service Comm’n*, 765 S.W.2d 618, 622 (Mo. App. 1988).

² *State ex rel. Capital City Water Co. v. Public Service Comm’n*, 850 S.W.2d 903, 916 n. 1 (Mo. App. 1993).

³ *See State ex rel. Utility Consumers’ Council of Missouri, Inc. v. Public Service Comm’n*, 585 S.W.2d 41, 59 (Mo. banc 1979).

⁴ *St. ex rel. Missouri Public Service Comm’n v. Fraas*, 627 S.W.2d 882, 887-888 (Mo. App. 1981).

⁵ *Id.* at 888.

⁶ *In the Matter of St. Louis County Water Company*, Case No. WR-96-263 (*Report & Order*, issued December 31, 1996), at p. 8; 5 Mo. P.S.C. 3d 341, 346.

hearings to give KCPL's customers an opportunity to respond to the requested rate increase. The Commission conducted local public hearings in Kansas City, Belton, Marshall, and Gladstone.⁷

D. Stipulations and Agreements

On June 26, 2015, some of the parties filed a *Non-Unanimous Stipulation and Agreement Regarding Pension and Other Post-Employment Benefits*. On July 1, 2015, some of the parties filed a *Partial Non-Unanimous Stipulation and Agreement as to Certain Issues* and a *Partial Non-unanimous Stipulation and Agreement as to True Up, Depreciation and Other Miscellaneous Issues*. Although these stipulations and agreements were not signed by all parties, they became unanimous stipulations and agreements because no party filed a timely objection.⁸ These stipulations and agreements resolved a number of the issues in dispute between the parties. The Commission found the stipulations and agreements to be reasonable and approved them on July 17, 2015. The issues resolved in these three partial stipulations and agreements will not be addressed further in this report and order, except as they may relate to any unresolved issues.

On June 16, 2015, some of the parties filed a *Non-Unanimous Stipulation and Agreement on Certain Issues* ("Rate Design Agreement"), which addressed issues relating to class cost of service, rate design, and tariffs. On August 3, 2015, Staff and KCPL filed a *Non-Unanimous Stipulation and Agreement Regarding Class Kilowatt-Hours, Revenues and Billing Determinants, and Rate Switcher Revenue Adjustments* ("True-Up Agreement"), which attempted to 1) resolve all issues relating to weather normalization, rate revenues, and the resulting class billing determinants used in developing rates for all rate classes, and 2) assign a revenue shortfall of \$500,000 for rate switchers in the LGS and LP rate

⁷ Transcript, Vols 3, 4, 6-8.

⁸ Commission Rule 4 CSR 240-2.115(2).

classes in order to account for any of those customers migrating to a different rate schedule to receive more advantageous pricing as a result of the Rate Design Agreement. KCPL objected to the Rate Design Agreement and the Office of Public Counsel objected to the True-Up Agreement, so those two stipulations and agreements became joint position statements of the signatory parties, and all the issues addressed in the Rate Design Agreement and True-Up Agreement remain for determination after hearing.⁹

E. Evidentiary Hearing

The evidentiary hearing was held on June 15-19, 29 and 30, 2015, and July 1, 2015.¹⁰ A true-up hearing was held on July 20, 2015.¹¹ During the hearings, the parties presented evidence relating to the unresolved issues previously identified by the parties.

F. Case Submission

During the evidentiary hearing and true-up hearing held at the Commission's offices in Jefferson City, Missouri, the Commission admitted the testimony of 61 witnesses, received 179 exhibits into evidence, and took official notice of certain matters.¹² Post-hearing briefs were filed according to the post-hearing procedural schedule. The final post-hearing briefs were filed on August 3, 2015, and the case was deemed submitted for the Commission's decision on that date.¹³

⁹ Commission Rule 4 CSR 240-2.115(2)(D).

¹⁰ Transcript, Vols 9-20.

¹¹ Transcript, Vols 21 and 22.

¹² At the hearing, the regulatory law judge took official notice of the following: 1) Commission's Report & Order in File No. TO-97-397, 2) Commission's Report & Order in File No. ER-2014-0258, 3) Commission's Report & Order in File No. ER-2014-0351, 4) Commission's Report & Order in File No. ER-2010-0356, and 5) the legislative history of Senate Bill 179 contained in Exhibit 152.

¹³ "The record of a case shall stand submitted for consideration by the commission after the recording of all evidence or, if applicable, after the filing of briefs or the presentation of oral argument." Commission Rule 4 CSR 240-2.150(1).

II. General Matters

A. General Findings of Fact

1. Kansas City Power & Light Company (“KCPL”), founded in 1882, is a wholly-owned subsidiary of Great Plains Energy Incorporated, both of which are headquartered in Kansas City, Missouri.¹⁴ KCPL is a vertically-integrated, regulated electric utility that provides generation, transmission, and distribution service as part of its sale of electricity to retail and wholesale customers in Missouri and Kansas.¹⁵

2. The Office of the Public Counsel (“Public Counsel”) is a party to this case pursuant to Section 386.710(2), RSMo¹⁶, and by Commission Rule 4 CSR 240-2.010(10).

3. The Staff of the Missouri Public Service Commission (“Staff”) is a party to this case pursuant to Section 386.071, RSMo, and Commission Rule 4 CSR 240-2.010(10).

4. KCPL provides electric service to approximately 519,000 customers, including approximately 457,700 residences, 59,300 commercial firms, and 2,100 industrials, municipalities, and other electric utilities, in the Kansas City metropolitan area and surrounding cities.¹⁷

5. KCPL’s base load generating capacity consists of ownership in four large coal-fired generating stations, the Wolf Creek nuclear power generating station, 2,200 megawatts (MW) of natural gas and oil-fired peaking capacity, and 149 MW of wind generating capacity. In 2011 and 2013, KCPL negotiated long-term power purchase agreements for additional wind and hydro generation. KCPL operates and maintains

¹⁴ Ex. 114, Heidtbrink Direct, p. 3.

¹⁵ Ex. 210, Featherstone Direct, p. 11.

¹⁶ Unless otherwise stated, all statutory citations are to the Revised Statutes of Missouri, as codified in the year 2000 and subsequently revised or supplemented.

¹⁷ Ex. 114, Heidtbrink Direct, p. 3.

approximately 12,000 miles of distribution lines and 1,800 miles of transmission lines to serve its customers.¹⁸

6. The proposed tariffs filed by KCPL in this case were designed to generate an aggregate revenue increase of approximately \$120.9 million, or 15.75%, based on a current Missouri jurisdictional base retail revenue of \$767.4 million.¹⁹

7. In order to determine the appropriate level of utility rates, the Commission must calculate a revenue requirement for KCPL, which is the increase or decrease in revenue KCPL needs in order to provide safe and reliable service, as measured using KCPL's existing rates and cost of service.²⁰

8. The revenue requirement calculation can be identified by a formula as follows:²¹ $RR = O + (V - D) R$ where,

- RR = Revenue Requirement;
- O = Operating Costs; (such as fuel, payroll, maintenance, etc., Depreciation and Taxes);
- V = Gross Valuation of Property Used for Providing Service;
- D = Accumulated Depreciation Representing the Capital Recovery of Gross Property Investment.
- $(V - D)$ = Rate Base (Gross Property Investment less Accumulated Depreciation = Net Property Investment)
- R = Overall Rate of Return or Weighted Cost of Capital
- $(V - D) R$ = Return Allowed on Net Property Investment

9. A test year is a historical year used as the starting point for determining the basis for adjustments that are necessary to reflect annual revenues and operating costs in calculating any shortfall or excess of earnings by the utility. Adjustments, such as annualization and normalization adjustments, are made to the test year results when the

¹⁸ *Id.* at p. 3-4.

¹⁹ *Id.* at p. 12.

²⁰ Ex. 210, Featherstone Direct, p. 26.

²¹ *Id.* at p. 26-27.

unadjusted results do not fairly represent the utility's most current annual level of existing revenue and operating costs.²²

10. The test year for this case is the twelve months ending March 31, 2014, updated to December 31, 2014.²³

11. The Commission also selected a true-up period ending May 31, 2015, in order to account for any significant changes in KCPL's cost of service that occurred after the end of the test year period but prior to the tariff operation of law date.²⁴

12. A normalization adjustment is an adjustment made to reflect normal, on-going operations of the utility. Revenues or costs that were incurred in the test year that are determined to be atypical or abnormal will get specific rate treatment and generally require some type of adjustment to reflect normal or typical operations. The normalization process removes abnormal or unusual events from the cost of service calculations and replaces those events with normal levels of revenues or costs.²⁵

13. An annualization adjustment is made to a cost or revenue shown on the utility's books to reflect a full year's impact of that cost or revenue.²⁶

14. The calculated total revenue requirement is then compared to net income available from existing rates to determine the incremental change in KCPL's rate revenues required to cover its operating costs and provide a fair return on investment used in providing utility service.²⁷

15. The Commission finds that any given witness's qualifications and overall credibility are not dispositive as to each and every portion of that witness's testimony. The

²² *Id.* at p. 18.

²³ *Id.* at p. 20.

²⁴ *Id.* at p. 20-21.

²⁵ *Id.* at p. 23-24.

²⁶ *Id.* at p. 22.

²⁷ *Id.* at p. 27.

Commission gives each item or portion of a witness's testimony individual weight based upon the detail, depth, knowledge, expertise, and credibility demonstrated with regard to that specific testimony. Consequently, the Commission will make additional specific weight and credibility decisions throughout this order as to specific items of testimony as is necessary.²⁸

16. Any finding of fact reflecting that the Commission has made a determination between conflicting evidence is indicative that the Commission attributed greater weight to that evidence and found the source of that evidence more credible and more persuasive than that of the conflicting evidence.²⁹

B. General Conclusions of Law

KCPL is an "electrical corporation" and a "public utility" as defined in Sections 386.020(15) and 386.020(43), RSMo, respectively, and as such is subject to the personal jurisdiction, supervision, control and regulation of the Commission under Chapters 386 and 393 of the Missouri Revised Statutes. The Commission's subject matter jurisdiction over KCPL's rate increase request is established under Section 393.150, RSMo.

Sections 393.130 and 393.140, RSMo, mandate that the Commission ensure that all utilities are providing safe and adequate service and that all rates set by the Commission are just and reasonable. Section 393.150.2, RSMo, makes clear that at any hearing involving a requested rate increase the burden of proof to show the proposed increase is just and reasonable rests on the corporation seeking the rate increase. As the party

²⁸ Witness credibility is solely a matter for the fact-finder, "which is free to believe none, part, or all of the testimony". *State ex rel. Public Counsel v. Missouri Public Service Comm'n*, 289 S.W.3d 240, 247 (Mo. App. 2009).

²⁹ An administrative agency, as fact finder, also receives deference when choosing between conflicting evidence. *State ex rel. Missouri Office of Public Counsel v. Public Service Comm'n of State*, 293 S.W.3d 63, 80 (Mo. App. 2009)

requesting the rate increase, KCPL bears the burden of proving that its proposed rate increase is just and reasonable. In order to carry its burden of proof, KCPL must meet the preponderance of the evidence standard.³⁰ In order to meet this standard, KCPL must convince the Commission it is “more likely than not” that KCPL’s proposed rate increase is just and reasonable.³¹

In determining whether the rates proposed by KCPL are just and reasonable, the Commission must balance the interests of the investor and the consumer.³² In discussing the need for a regulatory body to institute just and reasonable rates, the United States Supreme Court has held as follows:

Rates which are not sufficient to yield a reasonable return on the value of the property used at the time it is being used to render the services are unjust, unreasonable and confiscatory, and their enforcement deprives the public utility company of its property in violation of the Fourteenth Amendment.³³

In the same case, the Supreme Court provided the following guidance on what is a just and reasonable rate:

What annual rate will constitute just compensation depends upon many circumstances and must be determined by the exercise of a fair and enlightened judgment, having regard to all relevant facts. A public utility is entitled to such rates as will permit it to earn a return on the value of the property which it employs for the convenience of the public equal to that generally being made at the same time and in the same general part of the country on investments in other business undertakings which are attended by corresponding risks and uncertainties; but it has no constitutional right to profits such as are realized or anticipated in highly profitable enterprises or speculative ventures. The return should be reasonably sufficient to assure confidence in the financial soundness of the utility and should be adequate,

³⁰ *Bonney v. Environmental Engineering, Inc.*, 224 S.W.3d 109, 120 (Mo. App. 2007); *State ex rel. Amrine v. Roper*, 102 S.W.3d 541, 548 (Mo. banc 2003); *Rodriguez v. Suzuki Motor Corp.*, 936 S.W.2d 104, 110 (Mo. banc 1996), citing to, *Addington v. Texas*, 441 U.S. 418, 423, 99 S.Ct. 1804, 1808, 60 L.Ed.2d 323, 329 (1979).

³¹ *Holt v. Director of Revenue, State of Mo.*, 3 S.W.3d 427, 430 (Mo. App. 1999); *McNear v. Rhoades*, 992 S.W.2d 877, 885 (Mo. App. 1999); *Rodriguez v. Suzuki Motor Corp.*, 936 S.W.2d 104, 109-111 (Mo. banc 1996); *Wollen v. DePaul Health Center*, 828 S.W.2d 681, 685 (Mo. banc 1992).

³² *Federal Power Commission v. Hope Natural Gas Co.*, 320 U.S. 591, 603, (1944).

³³ *Bluefield Water Works & Improvement Co. v. Public Service Commission of the State of West Virginia*, 262 U.S. 679, 690 (1923).

under efficient and economical management, to maintain and support its credit and enable it to raise the money necessary for the proper discharge of its public duties. A rate of return may be reasonable at one time and become too high or too low by changes affecting opportunities for investment, the money market and business conditions generally.³⁴

The Supreme Court has further indicated:

‘[R]egulation does not insure that the business shall produce net revenues.’ But such considerations aside, the investor interest has a legitimate concern with the financial integrity of the company whose rates are being regulated. From the investor or company point of view it is important that there be enough revenue not only for operating expenses but also for the capital costs of the business. These include service on the debt and dividends on the stock. By that standard the return to the equity owner should be commensurate with returns on investments in other enterprises having corresponding risks. That return, moreover, should be sufficient to assure confidence in the financial integrity of the enterprise, so as to maintain its credit and to attract capital.³⁵

In undertaking the balancing required by the Constitution, the Commission is not bound to apply any particular formula or combination of formulas. Instead, the Supreme Court has said:

Agencies to whom this legislative power has been delegated are free, within the ambit of their statutory authority, to make the pragmatic adjustments which may be called for by particular circumstances.³⁶

Furthermore, in quoting the United States Supreme Court in *Hope Natural Gas*, the Missouri Court of Appeals said:

[T]he Commission [is] not bound to the use of any single formula or combination of formulae in determining rates. Its rate-making function, moreover, involves the making of ‘pragmatic adjustments.’ ... Under the statutory standard of ‘just and reasonable’ it is the result reached, not the method employed which is controlling. It is not theory but the impact of the rate order which counts.³⁷

³⁴ *Bluefield*, at 692-93.

³⁵ *Federal Power Commission v. Hope Natural Gas Co.*, 320 U.S. 591, 603 (1944) (citations omitted).

³⁶ *Federal Power Commission v. Natural Gas Pipeline Co.* 315 U.S. 575, 586 (1942).

³⁷ *State ex rel. Associated Natural Gas Co. v. Pub. Serv. Comm’n*, 706 S.W. 2d 870, 873 (Mo. App. W.D. 1985).

III. Disputed Issues

A. Cost of capital

Findings of Fact

17. Four financial analysts offered recommendations regarding an appropriate cost of capital in this case. Robert B. Hevert testified on behalf of KCPL. Hevert is Managing Partner of Sussex Economic Advisors, LLC. He holds a Bachelor of Science degree in Finance from the University of Delaware and a Master of Business Administration with a concentration in finance from the University of Massachusetts. He also holds the Chartered Financial Analyst designation.³⁸ He recommends the Commission allow KCPL a return on equity of 10.3 percent, within a range of 10.0 percent to 10.6 percent.³⁹

18. Michael Gorman testified on behalf of Missouri Industrial Energy Consumers (“MIEC”) and Midwest Energy Consumers Group (“MECG”). Gorman is a consultant in the field of public utility regulation and is a managing principal of Brubaker & Associates. He holds a Bachelor of Science degree in Electrical Engineering from Southern Illinois University and a Master’s Degree in Business Administration with a concentration in Finance from the University of Illinois at Springfield.⁴⁰ Gorman recommends the Commission allow KCPL a return on equity of 9.10 percent, within a recommended range of 8.80 percent to 9.40 percent.⁴¹

19. Maureen L. Reno testified on behalf of the U.S. Department of Energy and the Federal Executive Agencies. Reno holds a Bachelor of Arts in Economics from the University of Maine at Orono, Maine and a Master of Arts in Economics from the University of New Hampshire in Durham, New Hampshire. She is employed as an independent

³⁸ Ex. 115, Hevert Direct, p. 1; Attachment A.

³⁹ Ex. 116, Hevert Rebuttal, p. 2.

⁴⁰ Ex. 550, Gorman Direct, p. 1; Attachment A.

⁴¹ *Id.* at p. 2.

consultant.⁴² Reno recommends the Commission allow KCPL a return on equity of 9.0 percent, within a recommended range of 8.2 percent to 9.6 percent.⁴³

20. Zephania Marevangepo testified on behalf of Staff. Marevangepo is employed by the Commission as a Utility Regulatory Auditor III in the Financial Analysis Unit. Marevangepo holds a Bachelor of Science degree in Business Administration from Columbia College in Columbia, Missouri and a Masters of Business Administration from Lincoln University in Jefferson City, Missouri.⁴⁴ Marevangepo recommends a return on equity of 9.25 percent, within a range of 9.00 percent to 9.50 percent.⁴⁵

21. An essential ingredient of the cost-of-service ratemaking formula is the rate of return, which is premised on the goal of allowing a utility the opportunity to recover the costs required to secure debt and equity financing. If the allowed rate of return is based on the costs to acquire capital, then it is synonymous with the utility's weighted average cost of capital, which is calculated by multiplying each component ratio of the appropriate capital structure by its cost and then summing the results. In order to arrive at a rate of return, the Commission must examine an appropriate ratemaking capital structure, KCPL's embedded cost of debt, and KCPL's cost of common equity, or return on equity.⁴⁶

22. The actual capital structure of Great Plains Energy Incorporated ("GPE") as of May 31, 2015, was 50.090 percent common equity, .552 percent preferred stock, and 49.358 percent long-term debt.⁴⁷ This capital structure is consistent with the capital structure of utility operating companies held by proxy companies.⁴⁸

⁴² Ex. 700, Reno Direct, p. 1.

⁴³ *Id.* at p. 4.

⁴⁴ Ex. 200, Staff Report- Revenue Requirement Cost of Service, Appendix 1, p. 75.

⁴⁵ Ex. 200, Staff Report- Revenue Requirement Cost of Service, p. 19.

⁴⁶ Ex. 200, Staff Report- Revenue Requirement Cost of Service, p. 18, 37.

⁴⁷ Ex. 166, Klote True-Up Rebuttal, p. 2.

⁴⁸ Ex. 115, Hevert Direct, p. 54-55.

23. In KCPL's last rate case, File No. ER-2012-0174, the Commission used a consolidated capital structure and embedded cost of debt for KCPL consistent with that of GPE, KCPL's parent company.⁴⁹

24. In KCPL's most recent retail rate case in Kansas, the Kansas Corporation Commission approved the use of a capital structure based on the GPE consolidated capital structure.⁵⁰

25. All of the expert witnesses on this issue recommended using the GPE capital structure for KCPL, except for witness Maureen Reno.⁵¹ Ms. Reno used KCPL's actual capital structure as of December 31, 2014, which included short-term debt.⁵²

26. The consolidated cost of long-term debt of GPE as of May 31, 2015, was 5.557 percent.⁵³ KCPL's weighted average coupon rate for KCPL's debt instruments is consistent with the prevailing market conditions at the time of issuance.⁵⁴

27. Excluding short-term debt from the capital structure is consistent with the Federal Energy Regulatory Commission ("FERC") Order 561, which set forth the formula for calculating the allowance for funds used during construction. Since short-term debt is first used to fund construction work in progress, that same debt cannot be included in the regulatory capital structure without double-counting that debt.⁵⁵

28. A utility's cost of common equity is the return investors require on an investment in that company. Investors expect to achieve their return by receiving dividends and through stock price appreciation. To comply with standards established by the United States Supreme Court, the Commission must authorize a return on equity sufficient to

⁴⁹ Ex. 200, Staff Report- Revenue Requirement Cost of Service. p. 37; Ex. 115, Hevert Direct, p. 53.

⁵⁰ Ex. 116, Hevert Rebuttal, p. 64; Transcript, Vol. 9, p. 235.

⁵¹ Transcript, Vol. 9, p. 234-35.

⁵² Ex. 700, Reno Direct, p. 10.

⁵³ Ex. 166, Klote True-Up Rebuttal, p. 2.

⁵⁴ Ex. 700, Reno Direct, p. 52.

⁵⁵ Ex. 116, Hevert Rebuttal, p. 64.

maintain financial integrity, attract capital under reasonable terms, and be commensurate with returns investors could earn by investing in other enterprises of comparable risk.⁵⁶

29. Financial analysts use variations on three generally accepted methods to estimate a company's fair rate of return on equity. The Discounted Cash Flow ("DCF") method is based on a theory that a stock's current price represents the present value of all expected future cash flows. In its simplest form, the Constant Growth DCF model expresses the cost of equity as the discount rate that sets the current price equal to expected cash flows.⁵⁷ The analysts also use variations of the DCF model including the multi-stage growth DCF and the sustainable growth DCF.⁵⁸ The Risk Premium method is based on the principle that investors require a higher return to assume a greater risk. Common equity investments have greater risk than bonds because bonds have more security of payment in bankruptcy proceedings than common equity and the coupon payments on bonds represent contractual obligations.⁵⁹ The Capital Asset Pricing Method ("CAPM") assumes the investor's required rate of return on equity is equal to a risk-free rate of interest plus the product of a company-specific risk factor, beta, and the expected risk premium on the market portfolio.⁶⁰ No one method is any more correct than any other method in all circumstances. Analysts balance their use of all three methods to reach a recommended return on equity.

30. State public utility commissions in the country are reducing authorized returns on equity to follow the significant decline in capital market costs. A comparison of industry authorized returns on equity indicates that they have been steadily declining over the last

⁵⁶ Ex. 550, Gorman Direct, p. 11.

⁵⁷ Ex. 115, Hevert Direct, p. 15.

⁵⁸ Ex. 550, Gorman Direct, p. 11.

⁵⁹ *Id.* at p. 27.

⁶⁰ *Id.* at p. 33.

several years. In calendar year 2014, the industry authorized return on equity for fully litigated cases was 9.63 percent. In the first quarter of 2015, the industry authorized return on equity for fully litigated cases was 9.57 percent.⁶¹ Witness Gorman states credibly that based on returns awarded by other commissions, a reasonable finding for a return on equity in this case is conservatively at 9.5 percent or less.⁶²

31. The Commission mentions the industry authorized return on equity because KCPL must compete with other utilities all over the country for the same capital. Therefore, the industry authorized return on equity provides a reasonableness test for the recommendations offered by the return on equity experts.

32. In its decision regarding KCPL's last rate case, the Commission established a return on equity of 9.7 percent.⁶³ Over the last four years, the market capital costs for Missouri electric utilities are significantly lower, due to increases in utility stock prices and decreases in bond yields and utility dividend yields.⁶⁴

33. KCPL's expert witness, Robert Hevert, supports an increased return on equity at 10.3 percent. The Commission finds that such a return on equity would be excessive. Hevert's return on equity estimate is high because 1) his constant growth DCF results are based on excessive and unsustainable long-term growth rates, 2) his multi-stage DCF is based on a flawed accelerated dividend cash flow timing and an inflated gross domestic product growth estimate as a proxy for long-term sustainable growth, 3) his CAPM is based

⁶¹ Ex. 552, Gorman Surrebuttal, p. 3, Schedule MPG-SR-1.

⁶² Ex. 552, Gorman Surrebuttal, p. 4.

⁶³ Report and Order, *In the Matter of Kansas City Power & Light Company's Request for Auth. to Implement A Gen. Rate Increase for Elec. Serv. & in the Matter of KCP&L Greater Missouri Operations Company's Request for Auth. to Implement A Gen. Rate Increase for Elec. Serv.*, ER-2012-0174, 2013 WL 299322 (Jan. 9, 2013).

⁶⁴ Transcript, Vol. 9, p. 265, 279-80.

on inflated market risk premiums, and 4) his bond yield plus risk premium is based on inflated utility equity risk premiums.⁶⁵

34. If a fuel adjustment clause is implemented in this case, it will reduce KCPL's prospective investment risk, and this risk reduction should be considered in establishing a reasonable return on equity for KCPL.⁶⁶

35. Since April 2015, some capital market and general economic indicators have changed, indicating expanding macroeconomic growth and increased required returns.⁶⁷

36. The return on equity recommendations of witnesses Gorman, Marevangepo, and Reno are all reasonable and an accurate estimate of the current market cost of capital for KCPL, as those recommendations rely on verifiable and independent market data and accepted market-based rate of return models. Gorman testified credibly that these return on equity recommendations demonstrate that KCPL's current cost of equity is 9.5 percent or less.⁶⁸

Conclusions of Law and Decision

In determining the rate of return, the Commission must first consider KCPL's capital structure and cost of debt. This Commission has historically used the actual capital structure of GPE in determining the capital structure of KCPL, as has the Kansas Corporation Commission when setting KCPL's rates in that state. It is appropriate to use a consistent capital structure across all regulatory jurisdictions to avoid disagreements about one operating company's capital structure having more or less equity than another operating company. Ms. Reno's testimony was not persuasive that short-term debt should be included in the capital structure. The Commission concludes that in calculating KCPL's

⁶⁵ Ex. 551, Gorman Rebuttal, p. 6-7, 9-24.

⁶⁶ Ex. 552, Gorman Surrebuttal, p. 13.

⁶⁷ Ex. 117, Hevert Surrebuttal, p. 46-47.

⁶⁸ Ex. 552, Gorman Surrebuttal, p. 2.

cost of capital, the correct capital structure to use is the actual capital structure of GPE as of May 31, 2015, which was 50.090 percent common equity, .552 percent preferred stock, and 49.358 percent long-term debt. The use of short-term debt is not appropriate, so the correct cost of debt for KCPL is its actual cost of long-term debt as of May 31, 2015, which was 5.557%.

In order to set a fair rate of return for KCPL, the Commission must determine the weighted cost of each component of the utility's capital structure. One component at issue in this case is the estimated cost of common equity, or the return on equity. Estimating the cost of common equity capital is a difficult task, as academic commentators have recognized.⁶⁹ Determining a rate of return on equity is imprecise and involves balancing a utility's need to compensate investors against its need to keep prices low for consumers.⁷⁰

Missouri court decisions recognize that the Commission has flexibility in fixing the rate of return, subject to existing economic conditions.⁷¹ "The cases also recognize that the fixing of rates is a matter largely of prophecy and because of this commissions, in carrying out their functions, necessarily deal in what are called 'zones of reasonableness', the result of which is that they have some latitude in exercising this most difficult function."⁷² Moreover, the United States Supreme Court has instructed the judiciary not to interfere when the Commission's rate is within the zone of reasonableness.⁷³

⁶⁹ See Phillips, *The Regulation of Public Utilities*, Public Utilities Reports, Inc., p. 394 (1993).

⁷⁰ *State ex rel. Pub. Counsel v. Pub. Serv. Comm'n*, 274 S.W.3d 569, 574 (Mo. Ct. App. 2009).

⁷¹ *State ex rel. Laclede Gas Co. v. Public Service Commission*, 535 S.W.2d 561, 570-571 (Mo. App. 1976).

⁷² *State ex rel. Laclede Gas Co. v. Public Service Commission*, 535 S.W.2d 561, 570-571 (Mo. App. 1976).

In fact, for a court to find that the present rate results in confiscation of the company's private property, that court would have to make a finding based on evidence that the present rate is outside of the zone of reasonableness, and that its effects would be such that the company would suffer financial disarray. *Id.*

⁷³ *State ex rel. Public Counsel v. Public Service Commission*, 274 S.W.3d 569, 574 (Mo. App. 2009). See, *In re Permian Basin Area Rate Cases*, 390 U.S. 747, 767, 88 S.Ct. 1344, 20 L.Ed.2d 312 (1968) ("courts are without authority to set aside any rate selected by the Commission [that] is within a 'zone of reasonableness'").

The evidence shows that return on equity recommendations of witnesses Gorman, Marevangepe, and Reno are all reasonable and an accurate estimate of the current market cost of capital for KCPL. The ranges of those recommendations overlap, and the upper end of those ranges is between 9.4 percent and 9.6 percent. The Commission finds that witness Gorman testified credibly and persuasively that KCPL's current cost of equity is 9.5 percent or less. The Commission has considered other factors, such as recent indicators of growth that may suggest an increased return, and the reduction of investment risk to KCPL by approving a fuel adjustment clause, which suggests a reduced return. However, based on the competent and substantial evidence in the record, on its analysis of the expert testimony offered by the parties, and on its balancing of the interests of the company's ratepayers and shareholders, the Commission concludes that 9.5 percent is a fair and reasonable return on equity for KCPL. This rate of return will allow KCPL to compete in the capital market for the funds needed to maintain its financial health.

B. Fuel adjustment clause

2005 stipulation and agreement

Findings of Fact

37. A fuel adjustment clause ("FAC") is a mechanism established in a general rate case that allows periodic rate adjustments, outside a general rate proceeding, to reflect increases and decreases in an electric utility's prudently incurred fuel and purchased power costs.⁷⁴

38. While the three other investor-owned electric utilities in Missouri have FACs in place, KCPL does not have an FAC.⁷⁵ In File No. EO-2005-0329, the Commission approved

⁷⁴ Commission Rule 4 CSR 240-20.090(1)(C).

⁷⁵ Ex. 134, Rush Direct, p. 9.

a stipulation and agreement which included an Experimental Regulatory Plan (“2005 Stipulation”). That 2005 Stipulation included a provision that stated:

KCPL agrees that, prior to June 1, 2015, it will not seek to utilize any mechanism authorized in current legislation known as “SB 179” or other change in state law that would allow riders or surcharges or changes in rates outside of a general rate case based upon a consideration of less than all relevant factors. In exchange for this commitment, the Signatory Parties agree that if KCPL proposes an Interim Energy Charge (“IEC”) in a general rate case filed before June 1, 2015 in accordance with the following parameters, they will not assert that such proposal constitutes retroactive ratemaking or fails to consider all relevant factors:...⁷⁶ (emphasis added)

39. The 2005 Stipulation, including the above provision, was approved by the Commission in its Report and Order issued on July 28, 2005. The Report and Order directed that the signatory parties, including KCPL, shall abide by all of the terms and requirements in the 2005 Stipulation.⁷⁷

40. Senate Bill 179 was passed by the Missouri General Assembly, signed by the Governor, and became effective on January 1, 2006. This bill became section 386.266, RSMo, which authorizes electrical corporations to apply to the Commission for an FAC.⁷⁸

41. In Missouri, public utilities must file tariff sheets with the Commission with a specific effective date that determines when rates can first be charged or programs contained on those tariff sheets can be implemented.⁷⁹ The tariff sheets KCPL filed in this case for an FAC cannot be used by KCPL until the Commission approves an FAC tariff.⁸⁰

⁷⁶ Ex. 200, Staff Report, Revenue Requirement Cost of Service, p. 189-90; Ex. 153.

⁷⁷ Report and Order, EO-2005-0329, *In Re Kansas City Power & Light Co.*, 13 Mo. P.S.C. 3d 568, 242 P.U.R.4th 492 (July 28, 2005).

⁷⁸ Ex. 152.

⁷⁹ Transcript, Vol. 18, p. 1652.

⁸⁰ *Id.* at p. 1653-54.

42. Since KCPL's last rate increase went into effect on January 26, 2013, KCPL's costs related to fuel, purchased power, and transmission have all increased substantially, while actual revenues have decreased. KCPL had to absorb these increased costs.⁸¹

43. While the Commission authorized a return on equity of 9.7% for KCPL's Missouri operations, KCPL was only able to earn a return on equity of 6.5% in 2013, primarily as a result of increases in fuel, purchased power and transmission costs.⁸²

44. Without an adequate mechanism to timely recover these cost increases, KCPL will not have a reasonable opportunity to earn its authorized return on equity in the foreseeable future.⁸³ Because of regulatory lag, it is unlikely that these cost increases could be recovered through a normal rate case.⁸⁴

45. KCPL competes for credit with other vertically-integrated electric utilities in the Midwest and throughout the country, the vast majority of which already have FACs. KCPL's inability to recover its costs, over time, could undermine its financial health and compromise cash flows, which would jeopardize its ability to compete for capital, maintain service levels, and invest in its system. The resulting increased capital costs could potentially lead to increased costs to customers.⁸⁵

46. On June 10, 2015, Missouri Industrial Energy Consumers and the Office of the Public Counsel filed a Motion to Strike Pleadings, Reject Tariff Sheets, and Strike Testimony, to remove from the record portions of KCPL's evidence and reject tariff sheets in support of its request for an FAC, based on the allegation that KCPL violated the 2005 Stipulation and the Commission's Report and Order in EO-2005-0329. At the

⁸¹ Ex. 134, Rush Direct, p. 6, 12.

⁸² *Id.* at p. 12.

⁸³ *Id.* at p. 7.

⁸⁴ *Id.* at p. 14.

⁸⁵ *Id.* at p. 8.

evidentiary hearing, the regulatory law judge deferred a ruling on the motion and took the motion with the case.⁸⁶

Conclusions of Law and Decision

All parties other than KCPL have expressed the position that KCPL has violated the terms of the 2005 Stipulation provision stated above that prohibits KCPL from seeking to utilize a mechanism such as an FAC prior to June 1, 2015. They argue that by filing the rate case and tariff sheets requesting approval of an FAC before June 1, 2015, KCPL is improperly seeking to utilize an FAC before that date. KCPL argues that it has complied with the 2005 Stipulation because if the Commission authorizes an FAC for KCPL, any tariff approving the use of that FAC will not become effective until after June 1, 2015.

The Commission is a body of limited jurisdiction and has only such powers as are expressly conferred upon it by the statutes and powers reasonably incidental thereto.⁸⁷ The Commission cannot enforce, construe or annul contracts,⁸⁸ nor can it declare or enforce principles of law or equity.⁸⁹ However, the “Commission is entitled to interpret its own orders and to ascribe to them a proper meaning and, in so doing, the Commission does not act judicially but as a fact-finding agency”.⁹⁰ The Commission’s Report and Order in EO-2005-0329 approved the 2005 Stipulation and ordered the signatory parties, including KCPL, to abide by its terms. In determining whether KCPL has complied with that Commission order to abide by the terms of the 2005 Stipulation, the Commission has the authority to interpret the meaning of the provision of the 2005 Stipulation in dispute.

⁸⁶ Transcript, Vol. 9, p. 19.

⁸⁷ *State ex rel. & to Use of Kansas City Power & Light Co. v. Buzard*, 350 Mo. 763, 766, 168 S.W.2d 1044, 1046 (1943).

⁸⁸ *Wilshire Const. Co. v. Union Elec. Co.*, 463 S.W.2d 903, 905 (Mo. 1971).

⁸⁹ *State ex rel. Cass County v. Pub. Serv. Comm'n*, 259 S.W.3d 544, 547 (Mo. App. 2008).

⁹⁰ *State ex rel. Beaufort Transfer Co. v. Public Service Commission of Missouri*, 610 S.W.2d 96, 100 (Mo. App. 1980).

The 2005 Stipulation was a settlement agreement, and Missouri courts generally treat settlement agreements as contracts.⁹¹ “The primary rule in the interpretation of a contract is to ascertain the intent of the parties and to give effect to that intent.”⁹² “Where there is no ambiguity in the contract, the intent of the parties is to be gathered from it alone, and the court will not resort to construction where the intent of the parties is expressed in clear and unambiguous language as there is nothing to construe. The intent of the parties shall be determined from the instrument alone.”⁹³ “Contract language is ambiguous when there is uncertainty as to its meaning and it is fairly susceptible to more than one meaning so that reasonable persons may fairly and honestly differ on construction of its terms.”⁹⁴ “Words are not ambiguous merely because their meaning and application confound the parties.”⁹⁵

KCPL argues that “seek to utilize” is not ambiguous, and that under the plain and ordinary meaning of those words, it means in the context of a rate case that KCPL is prohibited from having an FAC go into effect prior to June 1, 2015, regardless of when the request is filed. The other parties argue that KCPL’s interpretation is incorrect, and that by filing its rate case on October 30, 2014, KCPL was improperly seeking to utilize an FAC in violation of the 2005 Stipulation. The dictionary is a good source for finding the plain and ordinary meaning of contract language, but it is important to consider the contract’s context in applying the appropriate definition.⁹⁶ The dictionary defines “seek” as “to make an

⁹¹ *State ex rel. Missouri Cable Telecommunications Ass’n v. Missouri Pub. Serv. Comm’n*, 929 S.W.2d 768, 774 (Mo. Ct. App. 1996).

⁹² *Speedie Food Mart, Inc. v. Taylor*, 809 S.W.2d 126, 129 (Mo.App.1991).

⁹³ *Marshall v. Pyramid Dev. Corp.*, 855 S.W.2d 403, 406 (Mo. Ct. App. 1993), citing *Wickham v. Wickham*, 750 S.W.2d 544, 546 (Mo.App.1988) and *Republic Nat. Life Ins. Co. v. Missouri State Bank & Trust Co.*, 661 S.W.2d 803, 808 (Mo.App.1983).

⁹⁴ *DCW Enterprises, Inc. v. Terre du Lac Ass’n, Inc.*, 953 S.W.2d 127, 130 (Mo. App. 1997), citing *Clampit v. Cambridge Phase II Corp.*, 884 S.W.2d 340 (Mo.App.1994).

⁹⁵ *Bailey v. Federated Mut. Ins. Co.*, 152 S.W.3d 355, 357 (Mo. App. 2004).

⁹⁶ *Id.*

attempt: TRY – used with an infinitive⁹⁷, and “utilize” is defined as “to make useful ... make use of”.⁹⁸ So, under those definitions, seeking to utilize an FAC means to “try to make use of” an FAC. In the context of a rate case, it is clear that KCPL cannot try to make use of an FAC until the Commission has approved tariffs authorizing that mechanism. If the Commission issues a report and order authorizing an FAC, KCPL will file tariffs in compliance with that order to implement the FAC. Those compliance tariffs would both be requested and have an effective date after June 1, 2015.

The Commission finds that terms of the 2005 Stipulation are not ambiguous, so there is no need to apply the rules of contract construction. Using the plain and ordinary meaning of the words in the 2005 Stipulation provision at issue, the filing of KCPL’s rate case on October 30, 2014, did not seek to utilize an FAC prior to June 1, 2015. Therefore, the Commission concludes that KCPL did not violate the terms of the 2005 Stipulation, and it has not violated the Commission’s Report and Order approving that agreement. As a result of this conclusion, the Commission will deny the Motion to Strike Pleadings, Reject Tariff Sheets, and Strike Testimony filed by Missouri Industrial Energy Consumers and the Office of the Public Counsel.

Even assuming for the sake of argument that KCPL violated the 2005 Stipulation, the Commission is not a signatory to that agreement and is not bound by its terms. The Commission may determine for reasons of public policy and public interest that KCPL should be granted an FAC even if it did violate the 2005 Stipulation. The evidence shows that KCPL’s costs related to fuel, purchased power, and transmission have all increased substantially while actual revenues have decreased, resulting in KCPL’s inability to earn its authorized return on equity. KCPL’s inability to recover its costs, over time, could

⁹⁷ Webster’s Third New International Dictionary-Unabridged, 2055 (1986).

⁹⁸ *Id.* at p. 2525.

undermine its financial health and compromise cash flows, which would jeopardize its ability to compete for capital, maintain service levels, and invest in its system. The resulting increased capital costs could potentially lead to increased costs to customers. Since an FAC is a mechanism that would help KCPL to timely recover its increased costs for fuel, purchased power and transmission and to avoid the negative consequences of regulatory lag, the Commission concludes that, for reasons of public policy, if KCPL meets the criteria for an FAC it should be granted such authority.

FAC criteria

Findings of Fact

47. Fuel used by KCPL to generate electricity is comprised mainly of coal, nuclear, natural gas and oil, and its costs for fuel and transportation alone are of such a magnitude that they would materially impact the utility.⁹⁹

48. The price of coal, natural gas, nuclear fuel, and oil, as well as the associated transportation costs, are established by national or international markets, so KCPL does not have control over commodity prices.¹⁰⁰ KCPL cannot control the fundamentals that drive the short and long-term fuel markets, so fuel costs are beyond the control of KCPL's management.¹⁰¹

49. Since January 2004, the price for natural gas has ranged from \$1.91/million British thermal units ("MMBtu") to \$15.38, which is a range of seven times the lowest price. In April 2012, natural gas prices were as low as \$1.91/MMBtu, but by February 2014 those

⁹⁹ Ex. 200, Staff Report-Revenue Requirement Cost of Service, p. 197.

¹⁰⁰ *Id.*

¹⁰¹ Ex. 103, Blunk Direct, p. 23-24.

prices had more than tripled to \$6.15. In the six months from February to August of 2015 the price for natural gas dropped almost 40%.¹⁰²

50. Coal prices experienced price changes similar to natural gas. In June 2012, coal prices were \$.40/MMBtu. In fewer than two years, the price had almost doubled to \$.76/MMBtu. Just a few months after reaching that high in April 2014, the price had dropped 17% to \$.63/MMBtu.¹⁰³

51. KCPL's hedging program can manage some of the short-term volatility in coal prices, but this does not protect against long-term market shifts or trends.¹⁰⁴

52. For the period of 2016 through 2019, the approximate time that an FAC would operate, only a fraction of KCPL's coal requirements are currently under contract.¹⁰⁵

53. KCPL's net energy costs were more volatile than 13 of the 14 companies in the proxy group used in KCPL's cost of capital analysis, and more volatile than Missouri's three other electric utilities that have FACs.¹⁰⁶

Conclusions of Law and Decision

Section 386.266.1, RSMo, allows the Commission to establish an FAC for KCPL.

Commission Rule 4 CSR 240-20.090(2)(C) states, in part, that:

In determining which cost components to include in a RAM¹⁰⁷, the commission will consider, but is not limited to only considering, the magnitude of the costs, the ability of the utility to manage the costs, the volatility of the cost component and the incentive provided to the utility as a result of the inclusion or exclusion of the cost component.

The evidence shows that KCPL's fuel and transportation costs are of such a magnitude that they would materially impact the utility, that those fuel costs are beyond the

¹⁰² *Id.* at p. 21-22.

¹⁰³ *Id.* at p. 22.

¹⁰⁴ *Id.*

¹⁰⁵ Ex. 104, Blunk Rebuttal, p. 9-10.

¹⁰⁶ *Id.* at 23-24.

¹⁰⁷ A "RAM" is a rate adjustment mechanism.

control of KCPL's management, and that its fuel costs are volatile. In addition, Section 386.266.4, RSMo, provides that an FAC must be "reasonably designed to provide the utility with a sufficient opportunity to earn a fair return on equity". Permitting KCPL to establish an FAC will assist the company in earning its authorized return on equity. The Commission concludes that KCPL has met the criteria for the Commission to authorize an FAC and, therefore, KCPL should be allowed to establish a fuel adjustment clause.

FAC tariff provisions

- 1. What percentage (customers/company) of changes in costs and revenues should the Commission find appropriate to flow through the fuel adjustment clause?**

Findings of Fact

54. KCPL is requesting 100% recovery of the costs included in its proposed FAC.¹⁰⁸

55. Staff is recommending 95%/5% sharing, where customers would be responsible for, or receive the benefit of, 95% of any deviation in fuel and purchased power costs as defined in the FAC tariff from the base amount included in rates.¹⁰⁹

56. The other three regulated electric utilities in Missouri have FACs that provide for 95%/5% sharing from the customers of those companies.¹¹⁰

57. Customers are the parties with the least amount of control over the cost of acquisition and supply of fuel used to generate electricity. KCPL's requested 100% recovery of costs might act as a disincentive to manage its fuel expense properly.¹¹¹

¹⁰⁸ Ex. 208, Eaves Rebuttal, p. 8.

¹⁰⁹ *Id.*

¹¹⁰ *Id.*

¹¹¹ *Id.*

Conclusions of Law and Decision

Under Missouri law, the Commission is authorized to approve rate schedules for an FAC and may include “features designed to provide the electrical corporation with incentives to improve the efficiency and cost-effectiveness of its fuel and purchased-power procurement activities”.¹¹² The Commission finds that allowing KCPL to have 100% recovery of its costs in an FAC would act as a disincentive for KCPL to control those costs. A 95%/5% sharing mechanism, where customers would be responsible for, or receive the benefit of, 95% of any deviation in fuel and purchased power costs would provide KCPL a sufficient opportunity to earn a fair return on equity while protecting KCPL’s customers by providing the company an incentive to control costs. KCPL’s FAC shall include an incentive clause providing that 95% of any deviation in fuel and purchased power costs from the base level shall be passed to customers and 5% shall be retained by KCPL.

- 2. Should the costs and revenues that are to be included in the FAC be approved by the Commission and explicitly identified along with the FERC account, subaccount and the resource code in which KCPL will record the actual cost/revenue? If so, what costs and revenues should be included and what are their corresponding FERC accounts, subaccounts and resource codes?**
- 3. Should the FAC tariff sheets reflect the accounts, subaccounts, resource codes, and the cost/revenue description?**

Findings of Fact

58. No additional findings of fact are necessary, as this is essentially a policy question for Commission determination.

Conclusions of Law and Decision

No party disagrees that the Commission should approve costs and revenues to be included in the FAC. The Commission determines that the FAC tariff sheets should identify

¹¹² Section 386.266.1, RSMo.

costs and revenues by FERC account and subaccount, but that the use of corporate resource codes is not necessary.

4. Should Southwest Power Pool (“SPP”) and other regional transmission organization/independent system operator transmission fees be included in the FAC, and at what level?

Findings of Fact

59. KCPL is a member of SPP, a regional transmission organization (“RTO”). As of March 1, 2014, SPP implemented its Integrated Marketplace (“IM”), in which SPP is responsible for the market operations of its participants and generating resources.¹¹³

60. KCPL buys back energy from SPP to meet the needs of its customers. The price at which KCPL purchases energy from the market will be at a rate set by SPP that reflects a market price.¹¹⁴

61. On a daily basis, KCPL sells all of the power it generates into the SPP market and purchases from SPP 100% of the electricity it sells to its retail customers.¹¹⁵

62. KCPL requests that transmission costs associated with the charges and revenues from SPP billings, and transmission costs to buy and sell energy, be recovered in rates through the FAC mechanism. KCPL is proposing that standard point-to-point transmission charges and base plan funding in FERC account 565 be included.¹¹⁶

63. KCPL is proposing to place all of its wholesale transmission expenses and revenues into its FAC, not just those that are for the transportation of purchased power.¹¹⁷

¹¹³ Ex. 200, Staff Report-Revenue Requirement Cost of Service, p. 198.

¹¹⁴ *Id.*

¹¹⁵ Ex. 107, Carlson Rebuttal, p. 9.

¹¹⁶ Ex. 134, Rush Direct, p. 17, 22.

¹¹⁷ Ex. 557, Dauphinais Rebuttal, p. 7-8.

64. The only transportation costs for purchased power that KCPL incurs are its wholesale transmission expenses that are incurred to transmit power it has purchased from SPP or other third parties.¹¹⁸

65. KCPL's wholesale transmission expenses incurred to transmit power from its own generation resources to its own load are not incurred for transportation of fuel or purchased power.¹¹⁹

66. KCPL generally does not incur wholesale transmission expenses to make off-system sales to SPP or to any third party located within SPP. Pursuant to the SPP tariff, KCPL generally only incurs wholesale transmission expenses for off-system sales when those sales are to third parties located outside of SPP.¹²⁰

67. Only approximately 7.3% of KCPL's total SPP wholesale transmission expenses can be reasonably classified as being for transportation of fuel or purchased power.¹²¹

68. KCPL's transmission costs have been rising, and projections show that these expenses will continue to increase at a significant rate from 2014 through 2019.¹²²

69. While KCPL's transmission costs are increasing, those costs are known, measurable, and not unpredictable, so the costs are not volatile.¹²³

Conclusions of Law and Decision

Section 386.266.1, RSMo, allows an electric utility to make periodic rate adjustments only to "reflect increases and decreases in its prudently incurred fuel and purchased-power costs, including transportation". This limits the costs that can be flowed through an FAC for

¹¹⁸ *Id.* at p.8.

¹¹⁹ *Id.*

¹²⁰ *Id.* at p. 10.

¹²¹ *Id.* at p.12.

¹²² Ex. 134, Rush, Direct, p. 20.

¹²³ *Id.* at p. 11, line 2; Ex. 200, Staff Report-Revenue Requirement Cost of Service, p. 199; Eaves Rebuttal, p. 208; Ex. 209, Eaves Surrebuttal, p. 1-5..

recovery. Transportation costs have been determined to include transmission costs, but limited only to those connected to purchased power costs.¹²⁴

KCPL argues that all of its SPP transmission fees should be included in the FAC because those fees are mandatory, increasing in amount, and volatile. In addition, KCPL states that since all of its power generation is sold into the SPP market and purchased from that market, all SPP expenses and revenues related to those individual sales and purchases of transmission service must be included in the FAC.

The Commission has addressed this issue in recent rate cases. In the Report and Order issued in File No. ER-2014-0258 for Ameren Missouri, the Commission stated:

The evidence demonstrated that for purposes of operation of the MISO tariff, Ameren Missouri sells all the power it generates into the MISO market and buys back whatever power it needs to serve its native load. From that fact, Ameren Missouri leaps to its conclusion that since it sells all its power to MISO and buys all that power back, all such transactions are off-system sales and purchased power within the meaning of the FAC statute. The Commission does not accept this point of view.

The drafters of the FAC statute likely did not envision a situation where a utility would consider all its generation purchased power or off-system sales. In fact, the policy underlying the FAC statute is clear on its face. The statute is meant to insulate the utility from unexpected and uncontrollable fluctuations in transportation costs of purchased power. At the time the statute was drafted, and even in our more complex present-day system, the costs of transporting energy in addition to the energy generated by the utility or energy in excess of what the utility needs to serve its load are the costs that are unexpected and out of the utility's control to such an extent that a deviation from traditional rate making is justified.

Therefore, of the three reasons Ameren Missouri incurs transmission costs cited earlier, the costs that should be included in the FAC are 1) costs to transmit electric power it did not generate to its own load (true purchased power) and 2) costs to transmit excess electric power it is selling to third parties to locations outside of MISO (off-system sales). Any other interpretation would expand the reach of the FAC beyond its intent.¹²⁵

¹²⁴ *In re Union Elec. Co.*, 422 S.W.3d 358, 367 (Mo. App. 2013).

¹²⁵ Report and Order, ER-2014-0258, *In the Matter of Union Elec. Co., d/b/a Ameren Missouri's Tariff to Increase Its Revenues for Elec. Serv.*, 320 P.U.R.4th 330 (Apr. 29, 2015).

Similarly, in a subsequent rate case for The Empire District Electric Company, which is also a member of SPP, the Commission concluded:

Furthermore, as has been the case since the FAC statute was created, the costs of transporting energy in addition to the energy generated by the utility or energy in excess of what the utility needs to serve its load are the costs that are unexpected and out of the utility's control to such an extent that a deviation from traditional rate making is justified. Therefore, the costs Empire incurs related to transmission that are appropriate for the FAC, from a policy perspective and by statute, are: 1) Costs to transmit electric power it did not generate to its own load ("true purchased power"); or 2) Costs to transmit excess electric power it is selling to third parties to locations outside of its RTO ("Off-system sales").¹²⁶

The evidence shows in this case that on a daily basis, KCPL sells all of the power it generates into the SPP market and purchases from SPP 100% of the electricity it sells to its retail customers. However, based on the Commission's analysis in the two cases cited above, it would not be lawful for KCPL to recover all of its SPP transmission fees through the FAC. In addition, while KCPL's transmission costs are increasing, those costs are known, measurable, and not unpredictable, so the costs are not volatile. The Commission concludes that the appropriate transmission costs to be included in the FAC are 1) costs to transmit electric power it did not generate to its own load (true purchased power); and 2) costs to transmit excess electric power it is selling to third parties to locations outside of SPP (off-system sales).

5. Should SPP and FERC Administrative fees (SPP Schedule 1-A and 12) be included in the FAC?

Findings of Fact

70. SPP Schedule 1-A fees are for SPP expenses associated with administering its Open Access Transmission Tariff. These expenses cover regional scheduling, planning,

¹²⁶ Report and Order, ER-2014-0351, *In the Matter of the Empire Dist. Elec. Co. for Auth. to File Tariffs Increasing Rates for Elec. Serv. Provided to Customers in the Company's Missouri Serv. Area*, ER-2014-0351, 2015 WL 4036220 (June 24, 2015)

and market-monitoring services provided to facilitate the transportation of energy on the transmission system.¹²⁷

71. SPP Schedule 12 fees are an assessment charged by FERC related to KCPL's membership in SPP.¹²⁸

72. Schedule 1-A and 12 fees are administrative in nature and not directly linked to fuel and purchased power costs. These fees support the operation of SPP and are not needed for KCPL to buy and sell energy to meet the needs of its customers.¹²⁹

73. RTO administrative fees, such as Schedule 1-A and 12 fees, are not included in the FACs of other regulated utilities in Missouri.¹³⁰

74. Schedule 1-A and 12 fees are variable, but not volatile in nature.¹³¹

Conclusions of Law and Decision

KCPL has requested that SPP Schedule 1-A and 12 fees be included in its FAC. The Commission finds that these fees are administrative in nature and not directly linked to fuel and purchased power costs. These fees support the operation of SPP and are not needed for KCPL to buy and sell energy to meet the needs of its customers. These fees are neither fuel and purchased power expenses nor transportation expenses incurred to deliver fuel or purchased power. The Commission concludes that including such fees would be unlawful under Section 386.266.1, RSMo, and, therefore, Schedule 1-A and 12 fees should not be included in the FAC. These fees are appropriate for recovery in base rates.

¹²⁷ Ex. 107, Carlson Rebuttal, p. 10.

¹²⁸ Ex. 106, Bresette Surrebuttal, p. 6.

¹²⁹ Ex. 208, Eaves Rebuttal, p. 9-10.

¹³⁰ *Id.*

¹³¹ *Id.*

6. Should all realized gains and losses from KCPL's hedging and/or cross hedging practices be included in the FAC?

Findings of Fact

75. KCPL has a hedging program to manage the price risk of coal and natural gas. The coal price hedging program involves a strategy of laddering into a portfolio of forward contracts for coal. Laddering refers to purchasing multiple products with different maturity dates. The natural gas hedging program involves the purchase of futures contracts to lock in a future price.¹³²

76. KCPL's hedging programs for both of these fuels has helped to avoid much of the volatility in the coal market, as well as exposure to natural gas market price risk.¹³³

77. An example of cross-hedging is the use of natural gas futures contracts to hedge electricity prices, since there is not a good market for electricity hedging instruments and the price of each have a strong relationship and move in tandem.¹³⁴

78. Cross-hedges are the best means for hedging power purchases or sales.¹³⁵

79. KCPL has used cross-hedging to achieve a balance in its hedging programs to reduce risk and volatility but does not do so at this time.¹³⁶

Conclusions of Law and Decision

KCPL has requested that its realized gains and losses from its hedging programs be included in the FAC. Hedging programs help to avoid volatility in the coal market and limit exposure to natural gas market price risk. Staff does not object to hedging, but opposes cross-hedging power transactions with natural gas because KCPL does not currently utilize cross-hedges. KCPL is persuasive that having the option of using both hedging and cross-

¹³² Ex. 103, Blunk Direct, p. 24-32.

¹³³ *Id.* at p. 25, 31.

¹³⁴ Transcript, Vol. 18, p. 1600.

¹³⁵ Ex. 104, Blunk Rebuttal, p. 34.

¹³⁶ Transcript, Vol. 18. P. 1601-2.

hedging would be valuable to reduce risk and volatility. The Commission concludes that all realized gains and losses from KCPL's hedging and/or cross-hedging practices should be included in the FAC.

7. Should SO₂ amortizations, bio fuels, propane, accessorial charges, broker commissions, fees and margins, be included in the FAC?

Findings of Fact

80. Accessorial charges are a necessary part of transporting coal by rail, including switching and the release and pick-up of locomotive power. This type of charge is included in railroad tariffs.¹³⁷

81. KCPL does not have unique account numbers or resource codes for these costs, so excluding them would increase the administrative and audit burden of the company.¹³⁸

82. SO₂ amortizations are collected in FERC account 509.¹³⁹

Conclusions of Law and Decision

KCPL has requested that charges for SO₂ amortizations, bio fuels, propane, accessorial charges, broker commissions, fees, and margins should be included in the FAC. Staff objects that these terms are not adequately defined, which KCPL has agreed to do. Including an appropriate description of these terms would enable KCPL to operate and Staff to audit the FAC correctly. Since accessorial charges are included in railroad tariffs and SO₂ amortizations are collected in FERC account 509, the Commission finds that SO₂ amortizations, bio fuels, propane, accessorial charges, broker commissions, fees, and margins should be included in the FAC, but should also be specifically defined within the FAC tariff.

¹³⁷ Ex. 104, Blunk Rebuttal, p. 34.

¹³⁸ *Id.*

¹³⁹ Ex. 135, Rush Rebuttal, p. 26, responding to Ex. 309, Mantle Direct, p. 30.

8. Should the FAC include costs and revenues that KCPL is not currently incurring or receiving other than insurance recoveries, subrogation recoveries and settlement proceeds related to costs and revenues included in the FAC?

Findings of Fact

83. Allowing new costs and revenues to flow through an FAC would be a modification to the FAC that the Commission approved.¹⁴⁰

84. Including a cost or revenue in the FAC that KCPL does not currently incur or record clouds the transparency of the FAC and unnecessarily complicates it.¹⁴¹

85. Insurance recoveries, subrogation recoveries and settlement proceeds related to costs and revenues included in the FAC are revenues typically related to an unexpected incident or accident. If these types of revenues do occur, it is likely that at some point in time, prior to the receipt of the recovery or settlement, there were increased costs or reduced revenues due to that circumstance that have been included in the fuel adjustment rates paid by customers.¹⁴²

Conclusions of Law and Decision

KCPL argues that the FAC should include all costs and revenues relating to net fuel and purchased power costs, whether or not they are currently being incurred. However, allowing a new cost or revenue to flow through an FAC is a modification to that FAC, which under Section 386.266, RSMo, only the Commission has the authority to modify. It is the Commission that should make the determination as to what costs or revenues should flow through the FAC, not the electric utility. An exception to this would be insurance recoveries, subrogation recoveries and settlement proceeds related to costs and revenues included in the FAC because such revenue increases are likely the result of circumstances that already

¹⁴⁰ Ex. 309, Mantle Direct, p. 33.

¹⁴¹ *Id.* at p. 34.

¹⁴² *Id.*

caused additional costs or reduced revenues in the FAC. The Commission concludes that the FAC should not include costs and revenues that KCPL is not currently incurring or receiving, other than insurance recoveries, subrogation recoveries and settlement proceeds related to costs and revenues included in the FAC.

9. Does the FAC need to have exclusionary language added to insure that NERC and FERC penalties are not included?

Findings of Fact

86. Staff proposed a change to KCPL's exemplar tariff sheet for an FAC to include a statement that all penalties related to NERC and FERC compliance standards shall be excluded.¹⁴³

87. The FERC Uniform System of Accounts ("USoA") provides guidance that such charges should be recorded in account 557, which is not includible in the FAC, so there could be no recovery of such penalties even if the language proposed by Staff were not included.¹⁴⁴

Conclusions of Law and Decision

Staff and OPC take the position that it would be preferable to include language to exclude NERC and FERC penalties from the FAC to make that completely clear. The Commission concludes that it is not necessary to include this language because the FERC USoA specifically provides that these penalties are not to be included. The proposed language should not be included in the FAC.

¹⁴³ Ex. 135, Rush Rebuttal, p. 18-19.

¹⁴⁴ *Id.*

10. Should the phrase “miscellaneous SPP IM charges, including but not limited to,” be included in KCPL’s FAC tariff?

Findings of Fact

88. KCPL has proposed including in the FAC the phrase “miscellaneous SPP IM charges, including but not limited to,” to account for any changes to SPP IM market charge types directed by SPP. The inclusion of the word “miscellaneous” referring to charges is vague.¹⁴⁵

89. The Commission takes administrative notice of the FAC tariff for Union Electric Company d/b/a Ameren Missouri, which tariff sheets are titled MO. P.S.C. Schedule No. 6, Original Sheet No. 70.1 through Original Sheet No. 73.11 and filed with the Commission.

Conclusions of Law and Decision

The Commission finds that the language proposed by KCPL, which includes the phrase “miscellaneous SPP IM charges, including but not limited to,” in the FAC tariff, is too vague and open-ended. The Commission concludes that the FAC tariff for KCPL should include language regarding changes in the SPP IM market charge types substantially similar to the FAC tariff language on that subject found in the FAC tariff for Ameren Missouri in MO. P.S.C. Schedule No. 6, Original Sheet No. 70.1 through Original Sheet No. 73.11.

11. How should OSSR be defined?

Findings of Fact

90. KCPL has proposed a definition of revenues from off-system sales (“OSSR”), as follows:

¹⁴⁵ Ex. 209, Eaves Surrebuttal, p. 9.

The following revenues or costs reflected in FERC Account Number 447: all revenues from off-system sales. This includes charges and credits related to the SPP Integrated Marketplace including, energy, make whole and out of merit payments and distributions, Over collected losses payments and distributions, TCR and ARR settlements, virtual energy costs, revenues and related fees where the virtual energy transaction is a hedge in support of physical operations related to a generating resource or load, generation/export charges, ancillary services including non- performance and distribution payments and charges and other miscellaneous SPP Integrated Market charges including, but not limited to, uplift charges or credits. It does not include sales for resale – private utilities or sales for resale – municipalities.¹⁴⁶

91. Staff has proposed a different definition of OSSR, as follows:

OSSR = Revenues from Off-System Sales:

The following revenues or costs reflected in FERC Account Number 447: all revenues from off-system sales. This includes charges and credits related to the SPP Integrated Marketplace including, energy, ancillary services, revenue sufficiency and neutrality payments and distributions, Over collected losses payments and distributions, TCR and ARR settlements, demand reductions, virtual energy costs, revenues and related fees where the virtual energy transaction is a hedge in support of physical operations related to a generating resource or load, generation/export charges, ancillary services including non- performance and distribution payments and SPP uplift revenues or credits. Off-system sales revenues from full and partial requirements sales to municipalities that are served through bilateral contracts in excess of one year shall be excluded from OSSR component.¹⁴⁷

92. Staff’s definition of OSSR struck “make whole and out of merit payments and distributions”, but added ancillary services, revenue sufficiency, and neutrality.¹⁴⁸

93. Staff’s terminology more accurately describes the type of revenue that should be included in an FAC.¹⁴⁹

¹⁴⁶ Ex. 134, Rush Direct, Schedule TMR-4.

¹⁴⁷ Ex. 202, Staff Rate Design & Class Cost of Service Report and erratum, Schedule DEE-1-3.

¹⁴⁸ Ex. 135, Rush Rebuttal, p. 20.

¹⁴⁹ Ex. 209, Eaves Surrebuttal, p. 10.

Conclusions of Law and Decision

The Commission finds that Staff's definition of OSSR more accurately and specifically describes the type of revenue that should be included in an FAC. The Commission concludes that KCPL's FAC tariff should include Staff's definition of OSSR.

12. How should the "J" component be defined, i.e., how should "Net System Input" be defined for KCPL's operations?

Findings of Fact

94. The "J" component refers to the definition of KCPL's jurisdictional allocation calculation. KCPL proposes that the "J" component be defined as: $J = \text{Missouri Retail Energy Ration} = \text{Missouri Retail kWh Sales} / \text{Total Retail kWh Sales (KS and MO)} + \text{Sales for Resale (Account 447.100 – Municipals)}$.¹⁵⁰

95. Staff proposes that the "J" component be defined as: $\text{Missouri Retail Energy Ration} = \text{Missouri Retail kWh sales} / \text{Total Net System Input (NSI)}$, where NSI is defined as $[\text{Retail Sales (KS+MO)} + \text{Sales for Resale} + \text{Border Customers} + \text{Firm Wholesale} + \text{Losses}]$.¹⁵¹

96. KCPL's Kansas customers are mostly residential and Missouri customers include more commercial and industrial customers. Typically, a service area composed of residential customers will experience higher line loss percentage than that of a system with a mixture of residential, commercial and industrial customers, such as the Missouri service territory.¹⁵²

Conclusion of Law and Decision

KCPL's recommendation would be appropriate if line losses are proportional to kWh sales, but line losses between Missouri and Kansas are not proportional based on the

¹⁵⁰ Ex. 135, Rush Rebuttal, p. 20.

¹⁵¹ *Id.*; Ex. 209, Eaves Surrebuttal, p. 10-11.

¹⁵² Ex. 209, Eaves Surrebuttal, p. 10-11.

current customer mix (residential v. commercial/ industrial). The Commission concludes that Staff's proposed definition of the "J" component is more appropriate and should be included in KCPL's FAC tariff.

13. Should the rate schedules implementing the FAC have an amount for the Base Factor when the Commission initially approves them, or not until after the end of the first FAC accumulation period?

Findings of Fact

97. Both KCPL and Staff agree that an FAC Base Factor must be set in this case and that the Base Factor must be stated in the FAC tariff.¹⁵³

98. Staff recommends that the Base Factor be included both in the body of the FAC tariff and on the "formula" sheet.¹⁵⁴

99. The actual calculation of the Base Factor will need to be modified to reflect the Commission's final decision in this case.¹⁵⁵

Conclusion of Law and Decision

The Commission concludes that the Base Factor, as modified to reflect the Commission's decision in this case, shall be included both in the body of the FAC tariff and on the "formula" sheet.

14. How many different voltage levels of service should be recognized for purposes of applying loss factors?

Findings of Fact

100. KCPL provided to Staff a loss study dated October 29, 2014, which contains system loss calculations and determinations based on data collected during calendar year 2013.¹⁵⁶

¹⁵³ Ex. 209, Eaves Surrebuttal, p. 11; Transcript, Vol. 18, p. 1630-31.

¹⁵⁴ Ex. 202, Staff Rate Design & Class Cost of Service Report and erratum, Schedule DEE-1-6.

¹⁵⁵ Ex. 209, Eaves Surrebuttal, p. 11.

¹⁵⁶ Ex. 200, Staff Report-Revenue Requirement Cost of Service, p. 200.

101. Staff used the information in this loss study in developing its recommended two primary and secondary voltage level adjustment factors.¹⁵⁷

102. Midwest Energy Consumers Group proposes that KCPL's FAC include four voltage levels, primary, secondary, substation, and transmission.¹⁵⁸

103. KCPL's loss study does not contain applicable data for losses at the substation level, which is one of the voltage level distinctions recommended by MECG, so that recommendation is not based on the data in the loss study.¹⁵⁹

Conclusion of Law and Decision

Commission Rule 4 CSR 240-20.090(9) requires an electric utility that desires to implement a rate adjustment mechanism, such as an FAC, to complete a jurisdictional system loss study of the corresponding energy losses experienced in its delivery of electricity. This study must be conducted within 24 months prior to the general rate case in which it requests its rate adjustment mechanism. KCPL's line loss study, required by this Commission rule, does not contain applicable data for losses experienced at the substation level, so recognition of more than two voltage levels is not currently supported by a necessary study. The Commission concludes that for this rate case two different voltage levels of service should be recognized for purposes of applying loss factors.

KCPL is directed to include in its line loss study for its next general rate case the information necessary to allow the parties to consider and evaluate if any additional voltage level adjustment factors should be incorporated into the design of the FAC tariff in KCPL's next rate case.

¹⁵⁷ *Id.* at p. 200-201.

¹⁵⁸ Ex. 554, Brubaker Direct, p. 7-9.

¹⁵⁹ Ex. 204, Bax Rebuttal, p. 2-3 and Schedule ABJ-1.

15. What are the appropriate recovery periods and corresponding accumulation periods for the FAC?

Findings of Fact

104. KCPL has proposed recovery periods of October through September and April through March with the corresponding accumulation periods of January through June and July through December.¹⁶⁰ KCPL has indicated that neither Staff nor OPC have any objections to this proposal.

Conclusion of Law and Decision

The parties that expressed a position on this issue have agreed that recovery periods of October through September and April through March with the corresponding accumulation periods of January through June and July through December should be included in the FAC. The Commission agrees that these recovery periods and accumulation periods are reasonable and should be included in the FAC.

16. Should FAC costs and revenues be allocated in the accumulation period's actual net energy cost in a manner consistent with the allocation methodology utilized to set permanent rates in this case?

Findings of Fact

105. KCPL, Staff and OPC agree that FAC costs and revenues should be allocated consistently with the allocation methodology used to set permanent rates.¹⁶¹

Conclusion of Law and Decision

All parties have agreed that costs and revenues should be allocated consistently with the allocation methodology used to set permanent rates in this case. The Commission concludes that FAC costs and revenues should be allocated in the accumulation period's

¹⁶⁰ Ex. 135, Rush Rebuttal, p. 27.

¹⁶¹ KCPL initial brief at p. 58; Staff initial brief at p. 58; OPC initial brief at p. 41-42.

actual net energy cost in a manner consistent with the allocation methodology used to set permanent rates in this case.

17. If the Commission authorizes KCPL to have a fuel adjustment clause, what FAC-related reporting requirements should it order KCPL to comply with?

Findings of Fact

106. Staff has proposed that the following information be provided due to the accelerated Staff review process necessary with FAC adjustment filings:

- As part of the information KCPL submits when it files a tariff modification to change its Fuel and Purchased Power Adjustment rate, include KCPL's calculation of the interest included in the proposed rate;
- Maintain at KCPL's corporate headquarters or at some other mutually-agreed-upon place and make available within a mutually-agreed-upon time for review, a copy of each and every coal and coal transportation, natural gas, fuel oil and nuclear fuel contract KCPL has that is in or was in effect for the previous four years;
- Within 30 days of the effective date of each and every coal and coal transportation, natural gas, fuel oil and nuclear fuel contract KCPL enters into, provide both notice to the Staff of the contract and opportunity to review the contract at KCPL's corporate headquarters or at some other mutually-agreed-upon place;
- Provide a copy of each and every KCPL hedging policy that is in effect at the time the tariff changes ordered by the Commission in this rate case go into effect for Staff to retain;
- Within 30 days of any change in a KCPL hedging policy, provide a copy of the changed hedging policy for Staff to retain;
- Provide a copy of KCPL's internal policy for participating in the Southwest Power Pool's Integrated Market;
- Maintain at KCPL's corporate headquarters or at some other mutually-agreed-upon place and make available within a mutually-agreed-upon time for review, a copy of each and every bilateral energy or demand sales/purchase contract;
- If KCPL revises any internal policy for participating in the Southwest Power Pool, within 30 days of that revision, provide a copy of the revised policy with the revisions identified for Staff to retain; and
- The monthly as-burned fuel report supplied by KCPL required by 4 CSR 240-3.190(1)(B) shall explicitly designate fixed and variable components of the average cost per unit burned including commodity, transportation, emission, tax, fuel blend, and any additional fixed or variable costs

associated with the average cost per unit reported (Staff is willing to work with KCPL on the electronic format of this report).¹⁶²

107. KCPL has agreed to provide this information to Staff.¹⁶³

Conclusion of Law and Decision

Since KCPL does not object to providing the reporting requirements recommended by Staff and listed above, the Commission determines that KCPL shall comply with those reporting requirements.

18. If the Commission authorizes KCPL to have an FAC, should KCPL be allowed to add cost and revenue types to its FAC between rate cases?

Findings of Fact

108. Allowing new cost and revenues types to flow through an FAC would be a modification to the FAC that the Commission approved.¹⁶⁴

109. Staff has proposed the following FAC tariff language that would permit changes to cost and revenue types:

Should FERC require any item covered by components FC, E, PP, TC, OSSR or R to be recorded in an account different than the FERC accounts listed in such components, such items shall nevertheless be included in component FC, E, PP, TC, OSSR or R. In the month that the Company begins to record items in a different account, the Company will file with the Commission the previous account number, the new account number and what costs or revenues that flow through the Rider FAC are to be recorded in the account.¹⁶⁵

Conclusion of Law and Decision

KCPL should not be able to add cost and revenue types to its FAC between rate cases unless the FAC tariff provides for those changes. The Commission concludes that

¹⁶² Ex. 202, Staff Rate Design & Class Cost of Service Report, p. 42-43.

¹⁶³ Ex. 135, Rush Rebuttal, p. 17; Transcript, Vol. 18, p. 1700-01.

¹⁶⁴ Ex. 309, Mantle Direct, p. 33.

¹⁶⁵ Ex. 202, Staff Rate Design & Class Cost of Service Report, p. 37 and erratum, Schedule DEE-1.

the tariff provision proposed by Staff above is reasonable and should be included in KCPL's FAC tariff.

19. If the Commission authorizes KCPL to have a FAC, should KCPL be required to clearly differentiate itself from GMO on customer bills?

Findings of Fact

110. When KCPL and KCP&L Greater Missouri Operations Company ("GMO") were brought under GPE, that company decided to use a single brand, KCPL, for both. At this time, GMO bills only indicate the KCPL brand name.¹⁶⁶

111. The customer's rate code is present on the bill and would serve to direct the customer to the correct tariffs for each individual company. Customer service employees are available to help customers identify the applicable tariff sheets.¹⁶⁷

112. Changing the bill language and presentation would not be a trivial undertaking, as space on the bill is limited and can impact various systemic billing processes.¹⁶⁸

113. There is no evidence in the evidentiary record that demonstrates customer confusion regarding which company provides service.

Conclusion of Law and Decision

The evidence shows that although bills for GMO customers do not have that company name on them, there is other information on the bill that would direct a customer to the correct tariff for that company. In addition, customer service employees are available to provide that information, and changing the bills would cause hardship to KCPL. Since there is no evidence of customer confusion, the Commission concludes that KCPL should not be required to clearly differentiate itself from GMO on customer bills.

¹⁶⁶ Transcript, Vol. 18, p. 1632-33.

¹⁶⁷ Ex. 135, Rush Rebuttal, p. 64.

¹⁶⁸ *Id.*

C. Transmission fee expense

Findings of Fact

114. In Missouri, rates are usually established based upon a historical test year where the company's expenses and the rate base necessary to produce the revenue requirement are synchronized. The deferral of costs from a prior period results in costs associated with the production of revenues in one period being charged against the revenues in a different period, which violates the "matching principle" required by Generally Accepted Accounting Principles (GAAP) and the Uniform System of Accounts approved by the Commission. The matching principle is a fundamental concept of accrual basis accounting, which provides that in measuring net income for an accounting period, the costs incurred in that period should be matched against the revenue generated in the same period. Such matching creates consistency in income statements and balance sheets by preventing distortions of financial statements which present an unfair representation of the financial position of the business. One type of deferral accounting, a "tracker", has the effect of either increasing or decreasing a utility's earnings for a prior period by increasing or decreasing revenues in future periods, which violates the matching principle.¹⁶⁹

115. A tracker is a rate mechanism under which the amount of a particular cost of service item actually incurred by a utility is tracked and compared to the amount of that item currently included in a utility's rate levels. Any over-recovery or under-recovery of the item in rates compared to the actual expenditures made by a utility is then booked to a regulatory asset or liability account and would be eligible to be included in the utility's rates in its next general rate proceeding through an amortization to expense.¹⁷⁰

¹⁶⁹ Ex. 312, Robertson Surrebuttal, p. 5-6.

¹⁷⁰ Ex. 235, Oligschlaeger Rebuttal, p. 3.

116. The broad use of trackers should be limited because they violate the matching principle, tend to unreasonably skew ratemaking results, and dull the incentives a utility has to operate efficiently and productively under the rate regulation approach employed in Missouri.¹⁷¹

117. KCPL requested a tracker for transmission fees it incurs to send and receive power (“transmission”) through the territory of RTOs such as the Southwest Power Pool (“SPP”).¹⁷²

118. KCPL’s transmission costs have increased over the past several years, but administrative fees charged by SPP are projected to decrease in the future.¹⁷³

119. KCPL’s transmission costs are normal, ordinary and recurring operating costs, and not extraordinary.¹⁷⁴

120. KCPL’s correct annualized levels of transmission expense and revenue to recognize in its revenue requirement on a Missouri jurisdictional basis are the highly confidential amounts stated in Ex. 256 HC, Lyons True-Up Rebuttal, p. 14, lines 13-14. These amounts do not include any transmission costs charged to KCPL by reason of Independence Power & Light becoming a member of SPP.

121. In surrebuttal testimony, KCPL requested for the first time that for SPP transmission fees not included in an FAC or afforded tracker treatment, \$5 million of annual estimated Missouri jurisdiction SPP transmission fees expense should be added to the revenue requirement above the base amount of Missouri jurisdiction SPP transmission fees. If the forecast amount recognized in revenue requirement exceeds actual SPP

¹⁷¹ Ex. 235, Oligschlaeger Rebuttal, p. 7.

¹⁷² Ex. 135, Rush Rebuttal, p. 11

¹⁷³ Ex. 223, Lyons Surrebuttal, p. 6

¹⁷⁴ Ex. 223, Lyons Surrebuttal, p. 9.

transmission fee expense during the period rates are in effect, such amounts should be credited to customers in a subsequent rate case.¹⁷⁵

Conclusions of Law and Decision

The Commission has the statutory authority to prescribe methods for electrical corporations to keep their accounts, records and books.¹⁷⁶ The Commission has set forth such proper methods in Commission Rule 4 CSR 240-20.030, which requires every electrical corporation to keep all accounts in conformity with the Uniform System of Accounts (“USoA”) as prescribed by FERC and published at 18 CFR Part 101 (2013). In the USoA, Accounts 182.3 and 254, other regulatory assets and liabilities, describe accounts for recording an item outside the year of occurrence (“deferral”) for determination in a later action.¹⁷⁷ The USoA allows deferral for “extraordinary items”, which are defined as:

Those items related to the effects of events and transactions which have occurred during the current period and which are of unusual nature and infrequent occurrence shall be considered extraordinary items. Accordingly, they will be events and transactions of significant effect which are abnormal and significantly different from the ordinary and typical activities of the company, and which would not reasonably be expected to recur in the foreseeable future.¹⁷⁸

¹⁷⁵ Ex. 136, Rush Surrebuttal, p. 9.

¹⁷⁶ Section 393.140(4), RSMo.

¹⁷⁷ 18 C.F.R. § Pt. 101, Definition 31. Regulatory Assets and Liabilities are assets and liabilities that result from rate actions of regulatory agencies. Regulatory assets and liabilities arise from specific revenues, expenses, gains, or losses that would have been included in net income determination in one period under the general requirements of the Uniform System of Accounts but for it being probable:

A. that such items will be included in a different period(s) for purposes of developing the rates the utility is authorized to charge for its utility services; or

B. in the case of regulatory liabilities, that refunds to customers, not provided for in other accounts, will be required.

¹⁷⁸ 18 C.F.R. § Pt. 101, General Instruction No. 7; See also, Report and Order, ER-2012-0174, *In the Matter of Kansas City Power & Light Company’s Request for Auth. to Implement A Gen. Rate Increase for Elec. Serv. & in the Matter of KCP&L Greater Missouri Operations Company’s Request for Auth. to Implement A Gen. Rate Increase for Elec. Serv.*, 2013 WL 299322 (Jan. 9, 2013); Report and Order, *In the Matter of the Application of S. Union Co. for the Issuance of an Accounting Auth. Order Relating to Its Natural Gas Operations & for A Contingent Waiver of the Notice Requirement of 4 CSR 240-4.020(2)*, GU-2011-0392, 2012 WL 363727 (Jan. 25, 2012).

KCPL has requested that the Commission approve the use of a particular deferral accounting method, a tracker. This type of deferral accounting to defer costs which may be incurred in the future is similar to an accounting authority order that defers expenses incurred as a result of a past event, in that neither constitute ratemaking. Missouri courts have stated that the granting of an accounting authority order is not ratemaking and creates no expectation of recovery.¹⁷⁹ For example, in a recent rate case, the Commission refused to allow recovery of amounts deferred under a previous accounting authority order.¹⁸⁰ Like an accounting authority order, a tracker simply defers a cost for determination in a future rate case where the Commission may determine whether that cost should be recovered in rates after considering all relevant factors.¹⁸¹

KCPL also requested a transmission tracker in its most recent rate case, ER-2012-0174, under a very similar fact situation. That Commission denied that requested tracker, finding that KCPL had failed to demonstrate that the projected cost increases were extraordinary:

“Rare” does not describe cost increases in the utility business generally. Specifically, Applicants’ evidence shows the following as to transmission. Transmission is an ordinary and typical, not an abnormal and significantly different, part of Applicants’ activities. Also, Applicants showed that paying more for transmission than in the previous year is a foreseeably recurring event, not an unusual and infrequent event. Thus, “items related to the effects of” transmission cost increases are not rare and, therefore, are not extraordinary.¹⁸²

¹⁷⁹ *State ex rel. Missouri Gas Energy v. Public Serv. Com’n*, 210 S.W.3d 330, 336 (Mo. App. W.D. 2006); *Missouri Gas Energy v. Public Serv. Com’n*, 978 S.W.2d 434, 438 (Mo. App. W.D. 1998). See also, Commission Rule 4 CSR 240-20.030(4), which states, in part, that “[i]n prescribing this system of accounts, the commission does not commit itself to the approval or acceptance of any item set out in any account for the purpose of fixing rates or in determining other matters before the commission.”

¹⁸⁰ Report and Order, ER-2014-0258, *In the Matter of Union Elec. Co., d/b/a Ameren Missouri’s Tariff to Increase Its Revenues for Elec. Serv.*, 320 P.U.R.4th 330 (Apr. 29, 2015).

¹⁸¹ Commission Rule 4 CSR 240-20.030(5) does allow the Commission to waive or grant a variance from the provisions of the USoA for good cause shown, but KCPL did not request such a waiver or variance.

¹⁸² Report and Order, ER-2012-0174, *In the Matter of Kansas City Power & Light Company’s Request for Auth. to Implement A Gen. Rate Increase for Elec. Serv. & in the Matter of KCP&L Greater Missouri*

The evidence presented in this case showed that KCPL's transmission costs, while having increased in recent years, are normal, ordinary and recurring operation costs. These recurring costs are not abnormal or significantly different from the ordinary and typical activities of the company, so they are not extraordinary and, therefore, not subject to deferral under the USoA. The Commission concludes that KCPL has not met its burden of proof to demonstrate that projected transmission cost increases are extraordinary, so its request for a transmission tracker will be denied.

KCPL's correct annualized levels of transmission expense and revenue to recognize in its revenue requirement on a Missouri jurisdictional basis are the amounts stated in Ex. 256 HC, Lyons True-Up Rebuttal, p. 14, lines 13-14. These amounts do not include any transmission costs charged to KCPL by reason of Independence Power & Light becoming a member of SPP. KCPL has also requested that the Commission add to this amount an additional amount of \$5 million, which it claims is an estimate of its increased transmission costs, subject to refund in a future rate case. Since this request was first submitted in surrebuttal testimony, it violates Commission Rule 4 CSR 240-2.130(7)(A), which requires that "[d]irect testimony shall include all testimony and exhibits asserting and explaining that party's entire case-in-chief." By submitting the request for the first time in surrebuttal, KCPL has prevented other parties from having a sufficient opportunity to conduct discovery or provide testimony on that matter. The Commission also finds that KCPL failed to adequately explain how it arrived at its estimate and how the Commission has the legal authority to grant such relief. For all these reasons, the Commission concludes that KCPL's request for an additional \$5 million added to the approved base amount of revenue requirement should be denied.

Operations Company's Request for Auth. to Implement A Gen. Rate Increase for Elec. Serv., 2013 WL 299322 (Jan. 9, 2013).

D. Property tax expense

Findings of Fact

122. KCPL requests that the Commission authorize a tracker mechanism for its expenses related to property taxes determined by Missouri state assessors. Those expenses would be deferred for consideration by the Commission to include in rates in KCPL's next rate case.¹⁸³

123. A property tax tracker, as with other types of trackers, would create an inconsistent matching over time of investments, revenues and expenses.¹⁸⁴

124. KCPL's property tax expenses have been increasing for the last five years, and may continue to increase in the future.¹⁸⁵

125. Property taxes are normal operating costs that will continue to occur every year, and an annualized level of such expenses to include in rates can be reasonably calculated. KCPL's property taxes are not rare or unusual.¹⁸⁶

126. KCPL's correct level of property tax expense to recognize in its revenue requirement on a total company basis is \$91,616,599.¹⁸⁷

127. In surrebuttal testimony, KCPL requested for the first time that for property tax expenses not afforded tracker treatment, \$5.6 million of annual estimated Missouri jurisdiction property tax expense should be added to the revenue requirement above the base amount of Missouri jurisdiction property taxes. If the forecast amount recognized in revenue requirement exceeds actual property tax expenses during the period rates are in effect, such amounts should be credited to customers in a subsequent rate case.¹⁸⁸

¹⁸³ Ex. 134, Rush Direct, p. 28-29.

¹⁸⁴ Ex. 222, Lyons Rebuttal, p. 8.

¹⁸⁵ Ex. 124, Klote Direct, p. 75.

¹⁸⁶ Ex. 223, Lyons Surrebuttal, p. 23-24.

¹⁸⁷ Ex. 259, Revised True-Up Accounting Schedules, Income Statement Detail, p. 7.

¹⁸⁸ Ex. 136, Rush Surrebuttal, p. 16-17.

Conclusions of Law and Decision

KCPL has requested that the Commission approval the same type of deferral mechanism for property tax expenses that it requested for transmission fee expenses. For that reason, the Commission incorporates herein the analysis contained in the conclusions of law and decision section from the transmission fee expense issue discussed above. The Commission concludes that KCPL has not met its burden of proof to demonstrate that projected property tax increases are extraordinary, so its request for a property tax tracker will be denied.

KCPL's correct level of property tax expense to recognize in its revenue requirement on a total company basis is \$91,616,599. KCPL has also requested that the Commission add to this amount an additional amount of \$5.6 million, which it claims is an estimate of its increased property tax costs, subject to refund in a future rate case. Since this request was first submitted in surrebuttal testimony, it violates Commission Rule 4 CSR 240-2.130(7)(A), which requires that "[d]irect testimony shall include all testimony and exhibits asserting and explaining that party's entire case-in-chief". By submitting the request for the first time in surrebuttal, KCPL has prevented other parties from having a sufficient opportunity to conduct discovery or provide testimony on that matter. The Commission also finds that KCPL failed to adequately explain how it arrived at its estimate and how the Commission has the legal authority to grant such relief. For all these reasons, the Commission concludes that the KCPL's request for an additional \$5.6 million added to the approved base amount of revenue requirement should be denied.

E. CIP/cyber-security expense

Findings of Fact

128. In 2007, the FERC designated the North American Regulatory Commission (“NERC”) as the electric reliability organization under the Federal Power Act and subsequently approved NERC’s reliability standards, which include the Critical Infrastructure Protection (“CIP”) standards. CIP addresses the security of cyber assets essential to the reliable operation of the electric grid and is continuously evolving due to the fluid nature of security threats to critical infrastructure. CIP has recently been updated with Version 5, which includes new standards. KCPL is subject to these CIP standards.¹⁸⁹

129. KCPL is requesting that the Commission authorize a tracker for the costs related to compliance with CIP and other cyber-security efforts. Those expenses would be deferred for consideration by the Commission to include in rates in KCPL’s next rate case.¹⁹⁰

130. A cyber-security tracker, as with other types of trackers, would create an inconsistent matching over time of investments, revenues and expenses.¹⁹¹

131. KCPL’s CIP/cyber-security costs are projected to increase as a result of the addition of new employees and capital additions, primarily in 2015. Thereafter, those costs will decrease for the next two years.¹⁹²

132. Compliance with CIP and cyber-security standards will be an ongoing cost for KCPL for the foreseeable future.¹⁹³

¹⁸⁹ Ex. 118, Ives Direct, p. 27-28.

¹⁹⁰ Ex. 134, Rush Direct, p. 34.

¹⁹¹ Ex. 222, Lyons Rebuttal, p. 28.

¹⁹² Ex. 222, Lyons Rebuttal, p. 27.

¹⁹³ Transcript, Vol. 18, p. 1855.

133. KCPL's correct level of CIP/cyber-security expense to recognize in its revenue requirement on a Missouri jurisdictional basis are the highly confidential amounts stated in Ex. 256 HC, Lyons True-Up Rebuttal, p. 16, lines 1-2.

134. In surrebuttal testimony, KCPL requested for the first time that for CIP/cyber-security costs not afforded tracker treatment, \$3.5 million of annual estimated Missouri jurisdiction CIP/cyber-security expense should be added to the revenue requirement above the base amount of Missouri jurisdiction CIP/cyber-security expense. If the forecast amount recognized in revenue requirement exceeds actual CIP/cyber-security expense during the period rates are in effect, such amounts should be credited to customers in a subsequent rate case.¹⁹⁴

Conclusions of Law and Decision

KCPL has requested that the Commission approval the same type of deferral mechanism for CIP/cyber-security expenses that it requested for transmission fee expenses. For that reason, the Commission incorporates herein the analysis contained in the conclusions of law and decision section from the transmission fee expense issue discussed above. The Commission concludes that KCPL has not met its burden of proof to demonstrate that projected CIP/cyber-security increases are extraordinary, so its request for a tracker will be denied.

KCPL's correct annualized levels of transmission expense and revenue to recognize in its revenue requirement on a Missouri jurisdictional basis are the amounts stated in Ex. 256 HC, Lyons True-Up Rebuttal, p. 16, lines 1-2. KCPL has also requested that the Commission add to this amount an additional amount of \$3.5 million, which it claims is an estimate of its increased CIP/cyber-security costs, subject to refund in a future rate case.

¹⁹⁴ Ex. 136, Rush Surrebuttal, p. 15-16.

Since this request was first submitted in surrebuttal testimony, it violates Commission Rule 4 CSR 240-2.130(7)(A), which requires that “[d]irect testimony shall include all testimony and exhibits asserting and explaining that party’s entire case-in-chief”. By submitting the request for the first time in surrebuttal, KCPL has prevented other parties from having a sufficient opportunity to conduct discovery or provide testimony on that matter. The Commission also finds that KCPL failed to adequately explain how it arrived at its estimate and how the Commission has the legal authority to grant such relief. For all these reasons, the Commission concludes that KCPL’s request for an additional \$3.5 million added to the approved base amount of revenue requirement should be denied.

F. La Cygne environmental retrofit project

Findings of Fact

135. The La Cygne generating station is comprised of two coal-fired units, Unit 1 and Unit 2. KCPL owns 50% of La Cygne, and Kansas Gas and Electric Company, a wholly-owned subsidiary of Westar Energy, Inc., owns the other 50% share. Pursuant to the ownership agreement, KCPL is responsible for operating both La Cygne units.¹⁹⁵

136. KCPL installed emission control equipment to reduce emissions from La Cygne by June 1, 2015, in order to comply with the Regional Haze Agreement that KCPL entered with the Kansas Department of Health and Environment. The emission control equipment is also required for compliance with the Mercury and Air Toxics Rule, the Cross-State Air Pollution Rule, and the National Ambient Air Quality Standards.¹⁹⁶

137. The emissions control equipment that was installed at La Cygne included limestone-based, wet scrubber flue gas desulfurization systems, fabric filters, mercury

¹⁹⁵ Ex. 102, Bell Direct, p. 7.

¹⁹⁶ Ex. 127, Ling Direct, p. 2-3.

control systems on both Units 1 and 2, and low NO_x burners, over-fired air, and selective catalytic reduction system on Unit 2.¹⁹⁷

138. KCPL successfully achieved the in-service criteria for La Cygne. As of March 24, 2015, Unit 2 was in-service, and as of April 30, 2015, Unit 1 was in-service.¹⁹⁸

139. The projected cost of the entire retrofit project was \$1.23 billion. While the final project costs are not yet determined, there is an indication that the project will be completed at some level below the estimated cost. Commission's Staff conducted a construction audit and prudence review of the project, and concluded that no adjustments should be proposed regarding the costs KCPL is requesting to be included in rates in this case. Staff determined that the prudently incurred costs to include in KCPL's Missouri rate base for the La Cygne project were \$292,620,121.¹⁹⁹

140. Before making the decision to proceed with the La Cygne environmental retrofit project, in 2010 KCPL conducted a multi-faceted analysis of a series of alternative long-term resource plans to assess the risk associated with various critical factors, such as natural gas prices, retail customer load growth, and carbon dioxide costs. The end result of this process resulted in an expected 25-year net present value of revenue requirement ("NPVRR") that evaluates the risks associated with uncertain factors in the electric utility industry.²⁰⁰

141. The results of this analysis completed in early 2011 demonstrated that the most cost-effective solution was the retrofitting of La Cygne Units 1 and 2.²⁰¹ KCPL's decision to retrofit La Cygne was supported by its determination that retiring the La Cygne

¹⁹⁷ Ex. 102, Bell Direct, p. 9.

¹⁹⁸ Ex. 162, Bell True-Up Direct, p. 1-2.

¹⁹⁹ Ex. 252, Hyneman True-Up Direct, p. 5-21.

²⁰⁰ Ex. 109, Crawford Direct, p. 17, 20.

²⁰¹ Ex. 109, Crawford Direct, p. 24-25; Transcript, Vol. 12, p. 792-93.

units and replacing them with combined-cycle natural gas generation would have resulted in a significant reliance on the relatively more volatile natural gas market.²⁰²

142. KCPL submitted its analysis of whether to retire or retrofit La Cygne to the Kansas Corporation Commission on February 23, 2011, as part of a petition for predetermination, which sought authorization to recover expenditures on the La Cygne retrofits.²⁰³ The Kansas commission granted KCPL's petition on August 19, 2011.²⁰⁴

143. Sierra Club's witness Rachel Wilson alleges that KCPL was imprudent in 1) failing to consider missing elements in its calculations that would have raised the costs to retrofit La Cygne, and 2) deciding to continue with the retrofit project in 2011 and 2012. She argues that while natural gas prices were declining during this period of time, KCPL should have re-evaluated its analysis using 2011 and 2012 forecasts from the Energy Information Administration's Annual Energy Outlook ("AEO"). Wilson alleges that using this AEO forecast would have revealed that retirement of La Cygne units would have been the more economic choice.²⁰⁵

144. KCPL did not fail to consider a reasonable level of cost-effective energy efficiency or a full range of options for addressing regulations such as non-gas supply options. The net benefits in KCPL's original analysis significantly exceeded other alternative plans considered. KCPL did not consider the conversion from a wet to a dry bottom ash system for Unit 2, but the projected costs would not have meaningfully changed the results.²⁰⁶

²⁰² Ex. 109, Crawford Direct, p. 22-24; Ex 110, Crawford Rebuttal, p. 2.

²⁰³ Ex. 402, Wilson Direct, p. 6.

²⁰⁴ *Id.* at p. 27.

²⁰⁵ Ex. 402, Wilson Direct, p. 3-5.

²⁰⁶ Ex. 110, Crawford Rebuttal, p. 3-5.

145. In KCPL's original analysis, it utilized several long-term forecasts regarding gas prices, which produces better results over time than using a single forecast.²⁰⁷ KCPL did not use the single AEO forecast alone because that forecast does not take into account future regulations that can produce upward pressure on gas prices.²⁰⁸

146. KCPL re-evaluated whether it was appropriate to retrofit the La Cygne units on four occasions, once each in 2012, 2013, 2014 and 2015, as part of KCPL's integrated resource planning ("IRP") process. The 2012 IRP planning work started in the summer of 2011, included the 2012 AEO forecast, and assumed that no project costs had been committed.²⁰⁹

147. Witness Burton Crawford testified credibly that the results of each re-evaluation of the La Cygne analysis during the IRP processes demonstrated that continuing with the retrofit project resulted in lower overall costs than resource plans that included retiring those units.²¹⁰

Conclusions of Law and Decision

In rate cases, there is initially a presumption that a utility's expenditures incurred in providing utility service, which are one component of its revenue requirement, are prudent.²¹¹ This presumption can be rebutted upon a showing of serious doubt as to the prudence of the expenditure, at which point the utility must dispel this doubt and prove the questioned expenditure is prudent.²¹² The Commission has interpreted this process as follows:

²⁰⁷ *Id.* at p. 6.

²⁰⁸ *Id.* at p.9-10.

²⁰⁹ *Id.* at p. 7; Transcript, Vol. 12, p. 783-84.

²¹⁰ *Id.*; Transcript, Vol. 12, p. 777.

²¹¹ *State ex rel. Public Counsel v. Public Service Comm'n*, 274 S.W.3d 569, 586 (Mo. App. 2009).

²¹² *Id.*; *State ex rel. Associated Natural Gas Company v. Public Service Commission of the State of Missouri*, 954 S.W.2d 520, 528 (Mo.App.1997); *In the Matter of Union Electric Company*, 27 Mo.P.S.C. (N.S.) 183, 193

In the context of a rate case, the parties challenging the conduct, decision, transaction, or expenditures of a utility have the initial burden of showing inefficiency or improvidence, thereby defeating the presumption of prudence accorded the utility. The utility then has the burden of showing that the challenged items were indeed prudent. Prudence is measured by the standard of reasonable care requiring due diligence, based on the circumstances that existed at the time the challenged item occurred, including what the utility's management knew or should have known. In making this analysis, the Commission is mindful that "[t]he company has a lawful right to manage its own affairs and conduct its business in any way it may choose, provided that in so doing it does not injuriously affect the public."²¹³

Testimony on behalf of Sierra Club from Ms. Wilson raised a serious doubt about KCPL's decision to proceed with the La Cygne retrofit project following authorization of the project by the Kansas Corporation Commission. Natural gas prices did fall shortly after KCPL completed its original analysis showing that the retrofit project was a lower-cost option than retirement of the units, and that original analysis did not take into account an AEO forecast showing those lower gas prices. Ms. Wilson alleges that KCPL waited too long to re-evaluate its original decision, and if it had done so it would have found that retirement was actually the lower-cost option after considering the lower gas prices.

KCPL's witnesses testified credibly, however, that the 2012 re-evaluation process was started just a few months after the release of the 2012 AEO forecast, that they included that forecast, in addition to several other more reliable forecasts, in their planning process, and that the result of the 2012 IRP process yielded the same result as the original KCPL analysis that was approved in Kansas. When the retrofit project was re-evaluated each year in 2012-2015, those studies showed that the retrofit project resulted in lower overall costs than resource plans that included retiring those units. In addition, the evidence

(1985) (quoting *Anaheim, Riverside, etc. v. Federal Energy Regulatory Commission*, 669 F.2d 779, (D.C. Cir. 1981)).

²¹³ *State ex rel. City of St. Joseph v. Public Service Commission*, 30 S.W.2d 8, 14 (Mo. banc 1930); In the Matter of Missouri-American Water Company's Tariff Sheets, *Report and Order*, Case No. WR-2000-281 (August 31, 2000), 9 Mo. P.S.C. 3d 254.

shows that KCPL did not fail to consider missing elements in its calculations that would have raised the costs to retrofit La Cygne.

The Commission concludes that KCPL has met its burden of proof to demonstrate that, based on the circumstances that existed at the time, KCPL was prudent in choosing to proceed with the La Cygne environmental retrofit project. The correct and prudently incurred costs to include in KCPL's Missouri rate base for the La Cygne project are \$292,620,121.

G. Rate case expense

Findings of Fact

148. Rate case expense can be defined as all incremental costs incurred by a utility directly related to an application to change its general rate levels.²¹⁴

149. KCPL's total rate case expense as of August 12, 2015, is \$1,024,304.²¹⁵

150. Rate case expense can benefit both utility shareholders and customers, though often in different ways. A utility and its shareholders directly benefit from this expense because generally these costs are incurred in order to increase a utility's revenues and, ultimately, its profitability. Customers benefit generally from being served by financially healthy utilities, which is bolstered in part by the ability of a utility to periodically seek increased rates to recover increasing expenses and earn a return on investments in their systems.²¹⁶

151. The rate case process can be adversarial in nature, with the utility and ratepayers on opposing sides.²¹⁷

²¹⁴ Ex. 243, p. 1.

²¹⁵ Ex. 169 and 216. OPC's rate case expense amount in Ex. 319 differed from that of both KCPL and Staff, and so is found to be less credible.

²¹⁶ Ex. 243, p. 11.

²¹⁷ Transcript, Vol. 13, p. 1022.

152. KCPL engaged several outside experts and consultants in this case. Witness Spanos performed the depreciation study required by Commission rules. Mr. Hevert performed a cost of capital/capital structure analysis using industry-wide data. Witness Rogers did a highly-specialized study to determine the cost of dismantling non-nuclear generating units. Mr. Overcast testified on the topic of regulatory mechanisms. These types of testimonies and studies are generally performed by outside experts in rate cases in Missouri.²¹⁸

153. Staff and OPC propose that the expenses of KCPL witness Overcast be disallowed as duplicative of testimony given by other witnesses.²¹⁹

154. KCPL retained the services of witness Overcast to respond to other parties opposed to KCPL's requests for a fuel adjustment clause and trackers. Mr. Overcast was hired to provide a nationwide view of how other jurisdictions have approached such alternative regulatory mechanisms.²²⁰

155. KCPL was represented in this case by both in-house and external legal counsel. KCPL used two in-house attorneys and employed two outside attorneys. The two outside attorneys have represented KCPL in numerous rate cases and other Commission proceedings in the past to supplement the in-house legal team.²²¹

156. OPC witness Addo proposed adjustments to rate case expenses, including reducing the hourly rates of KCPL outside attorneys to \$200/hour, based on the rates one attorney charged Ameren Missouri and the results of a 2013 survey of hourly rates by the Missouri Bar.²²²

²¹⁸ Ex. 120, Ives Rebuttal, p. 25.

²¹⁹ Ex. 226, Majors Surrebuttal, p. 62-63; Ex. 308, Addo Surrebuttal, p. 27-28.

²²⁰ Transcript, Vol. 13, p. 970-71.

²²¹ Ex. 120, Ives Rebuttal, p. 26.

²²² Ex. 308, Addo Surrebuttal, p. 26-30.

157. Mr. Addo did not compare the background and experience of the KCPL attorneys with that of the Ameren Missouri attorney, and he did not calculate the number of hours or examine the tasks that Ameren Missouri's counsel performed on a prior rate case.²²³

158. In Missouri, almost all utilities hire witnesses to sponsor their rate of return/return on equity positions in rate cases and often hire consultants to handle other issues, as well.²²⁴

159. In a rate case, a utility chooses how many and what type of consultants it will engage, what issues to pursue, and what legal strategies it will employ, and therefore, the extent of rate case expense is largely at KCPL's discretion.²²⁵

160. The expenses in this case are driven primarily by issues raised by KCPL, which has complete control over the content and methodologies proposed in its rate cases. For example, KCPL has requested several trackers, two of which have never been requested before in Missouri and two of which were first presented in rebuttal testimony²²⁶, and has requested recovery in rates of the expenses from the Clean Charge Network.

161. KCPL has requested that all costs and expenses associated with legal representation, consultants, and expert witnesses be included in its increased revenue requirement.²²⁷

162. All consumer groups were represented by hired counsel in this case, and some also engaged expert witnesses. While KCPL is able to recoup the costs of its legal counsel and expenses through utility service rates, OPC, the entity representing

²²³ Transcript, Vol. 13, p. 1068-72.

²²⁴ Ex. 243, p. 1-2.

²²⁵ Transcript, Vol. 13, p. 1062; Ex. 226, Majors Surrebuttal, p. 57-58.

²²⁶ Ex. 226, Majors Surrebuttal, p. 60-61.

²²⁷ Ex. 169HC; Ex. 261HC.

ratepayers, operates within a tight annual budget, and interveners pay their own legal expenses.²²⁸

163. Prudency reviews, by their nature, are not a strong incentive to control costs. The utility holds all the information a challenging party needs to prove imprudence, and it is not likely a challenging party could identify all instances of imprudence, even when engaged in a conscientious prudence review.²²⁹

164. Awarding a utility all of its incurred rate case expenses could provide that utility with a significant financial advantage over other participants in the rate case process, who may be constrained by budgetary and other financial restrictions. Such a practice does not encourage reasonable levels of cost containment in the utility's rate case expense decisions.²³⁰

165. An incentive for a utility to limit its rate case expense is to tie a utility's percentage recovery of rate case expense to the percentage of its rate increase request that the Commission finds just and reasonable. Use of this approach would directly tie a utility's recovery of rate case expense to both the reasonableness of its issue positions and the dollar value sought from customers in a rate case.²³¹

166. KCPL previously filed rate cases in 2006, 2007, 2009, 2010, and 2012.²³² In recent rate cases, KCPL has incurred rate case expenses substantially higher than historical levels and higher than other utilities in Missouri.²³³

²²⁸ Ex. 200, Staff Report- Revenue Requirement Cost of Service, p. 132-33.

²²⁹ Transcript, Vol. 18, p. 1745-46; Transcript, Vol. 16, p. 1520-21.

²³⁰ Ex. 243, p. 11-12.

²³¹ *Id.* at p. 14; Ex. 236, Oligschlaeger Surrebuttal, p. 9-11; Transcript, Vol. 13, p. 1056-58.

²³² Ex. 200, Staff Report- Revenue Requirement Cost of Service, p. 3-4.

²³³ Transcript, Vol. 13, p. 1063; Ex. 243, p. 6-8.

167. Prudence is not the only consideration in determining what costs should be included in rates; the benefit to customers must also be considered when deciding what costs are reasonable for customer rates.²³⁴

168. KCPL has pursued issues in this case that benefit only the shareholders, such as La Cygne construction accounting and some elements of the rate of return recommendation.²³⁵ Utility expenses that are highly discretionary and do not benefit customers, such as charitable donations, political lobbying expenses, and incentive compensation tied to earnings per share, are typically allocated entirely to shareholders.²³⁶

169. Staff and OPC recommend that the Commission require shareholders and ratepayers to share the rate case expense costs equally.²³⁷ Staff also proposes, as an alternative to equal sharing of expenses, that KCPL receive rate recovery of rate case expenses in proportion to the amount of rate relief it is granted compared to the amount of its original rate increase request.²³⁸

Conclusion of Law and Decision

In a rate case, the Commission has broad discretion to determine which expenses a utility may recover from ratepayers. The Missouri Supreme Court has stated that the Commission's statutory power and authority to set rates "necessarily includes the power and authority to determine what items are properly includable in a utility's operating expenses and to determine and decide what treatment should be accorded such expense

²³⁴ Transcript, Vol. 13, p. 1050.

²³⁵ Transcript, Vol. 13, p. 1033-34.

²³⁶ Ex. 200, Staff Report- Revenue Requirement Cost of Service, p. 133-34; Ex. 226, Majors Surrebuttal, p. 57-58.

²³⁷ Ex. 226, Majors Surrebuttal, p. 55; Ex. 307, Addo Rebuttal, p. 46.

²³⁸ Ex. 236, Oligschlaeger Surrebuttal, p. 10-11.

items.”²³⁹ The Commission’s authority extends to allocating an expense between certain classes or groups of ratepayers²⁴⁰ and to requiring company shareholders to bear expenses the Commission finds to be unreasonable or unnecessary.²⁴¹

As stated above, there is initially a presumption that a utility’s expenditures incurred in providing utility service, which are one component of its revenue requirement, are prudent.²⁴² This presumption can be rebutted upon a showing of serious doubt as to the prudence of the expenditure, at which point the utility must dispel this doubt and prove the questioned expenditure is prudent.²⁴³

Staff and OPC allege that the expenses of witness Overcast should be disallowed because his testimony was duplicative and those expenses were imprudent. Similarly, OPC and MECG argue that the fees of KCPL’s outside attorneys were imprudent and should be reduced to \$200/hour or disallowed entirely. These expenses for experts, consultants, and attorneys do not lend themselves to review for prudence. Unlike industry standards for pipe size or transmission line capacity, there is no accessible appropriate standard for determining whether one consultant’s analysis was truly unnecessary or if one attorney’s expertise is worth more than another’s. The evidence does not reveal a bright line solution to this problem, and the Commission will not disallow these or any other rate case expenses in this case.

²³⁹ *State ex rel. City of W. Plains v. Pub. Serv. Comm’n*, 310 S.W.2d 925, 928 (Mo. 1958). See also, *State ex rel. KCP & L Greater Missouri Operations Co. v. Missouri Pub. Serv. Comm’n*, 408 S.W.3d 153, 166 (Mo. App. 2013).

²⁴⁰ *State ex rel. City of W. Plains v. Pub. Serv. Comm’n*, 310 S.W.2d at 934.

²⁴¹ *State ex rel. KCP & L Greater Missouri Operations Co. v. Missouri Pub. Serv. Comm’n*, 408 S.W.3d at 164-165.

²⁴² *State ex rel. Public Counsel v. Public Service Comm’n*, 274 S.W.3d 569, 586 (Mo. App. 2009).

²⁴³ *Id.*; *State ex rel. Associated Natural Gas Company v. Public Service Commission of the State of Missouri*, 954 S.W.2d 520, 528 (Mo.App.1997); *In the Matter of Union Electric Company*, 27 Mo.P.S.C. (N.S.) 183, 193 (1985) (*quoting Anaheim, Riverside, etc. v. Federal Energy Regulatory Commission*, 669 F.2d 779, (D.C. Cir. 1981)).

Instead, the Commission will consider whether it is reasonable that KCPL shareholders cover a portion of KCPL's rate case expense. In one sense, rate case expense is like other common operational expenses that a utility must incur to provide utility services to customers. Since customers benefit from having just and reasonable rates, it is appropriate for customers to bear some portion of the utility's cost of prosecuting a rate case.

However, rate case expense is also different from most other types of utility operational expenses, in that 1) the rate case process is adversarial in nature, with the utility on one side and its customers on the other; 2) rate case expense produces some direct benefits to shareholders that are not shared with customers, such as seeking a higher return on equity; 3) requiring all rate case expense to be paid by ratepayers provides the utility with an inequitable financial advantage over other case participants; and 4) full reimbursement of all rate case expense does nothing to encourage reasonable levels of cost containment.

The Commission has the legal authority to apportion rate case expense between ratepayers and shareholders. Under Missouri law, the Commission must set just and reasonable rates²⁴⁴, and rates that include all of the utility's rate case expense, for the reasons set forth above, may not be just or reasonable.²⁴⁵ Moreover, this Commission has already found rate case expense sharing to be just and reasonable in at least one prior case. In a 1986 decision, *In the Matter of Arkansas Power and Light Company*, the Commission "adopted Public Counsel's proposed disallowance of one-half of rate case

²⁴⁴ Section 393.130.1, RSMo, "...All charges made or demanded by any...electrical corporation ... shall be just and reasonable and not more than allowed by law or by order or decision of the commission..."

²⁴⁵ There are rate cases where the utility does not have the means to absorb a portion of rate case expense and requiring it to do so would ultimately harm customers. In such circumstances, it would appear just and reasonable that rates include the entire amount of rate case expense.

expense.”²⁴⁶ It is also important to note that there are a number of other cases where the Commission acknowledged it has this authority.²⁴⁷

KCPL argues that it would be unlawful for the Commission to adopt a new policy related to the recovery of rate case expense without conducting a rulemaking proceeding under Chapter 536, RSMo. The Commission agrees that it cannot prospectively change its statement of general applicability that implements, interprets or prescribes law or policy, or that describes the organization, procedure, or practice requirements before this agency.²⁴⁸ Agencies cannot engage in this type of rulemaking by an adjudicated order.²⁴⁹ However, the Commission is not announcing a general change in policy regarding rate case expense for all utilities in this Report and Order. Rather, the Commission is setting just and reasonable rates under the particular facts of this case, so the Commission is not engaging in improper rulemaking.

The evidence shows that the expenses in this case are driven primarily by issues raised by KCPL, which has complete control over the content and methodologies proposed when it files its rate cases. In this case, KCPL has requested three new trackers, two of which have never been requested before in Missouri. KCPL has also requested recovery in rates of the expenses from the Clean Charge Network, which is a type of expense that has never been raised in a rate case before this Commission. Each of these issues are unique to KCPL, and while KCPL always has the opportunity to pursue new and unique issues in a

²⁴⁶ Report and Order, File No. ER-85-265, 28 Mo. P.S.C. (N.S.) 435, 447 (1986),

²⁴⁷ See, *In the Matter of Kansas City Power & Light Company*, Report and Order, File Nos. EO-85-185 and EO-85-224, 28 Mo. P.S.C. (N.S.) 229, 263 (1986), and *in the Matter of Missouri Gas Energy*, Report and Order, File No. GR-2009-0355, 19 Mo. P.S.C. 3d 245, 303 (2010).

²⁴⁸ Section 536.010(6) defines a rule as “each agency statement of general applicability that implements, interprets, or prescribes law or policy.” In other words, a rule is “[a]n agency statement of policy or interpretation of law of future effect which acts on unnamed and unspecified persons or facts.” *Missourians for Separation of Church and State v. Robertson*, 592 S.W.2d 825, 841 (Mo.App.1979). *HTH Companies, Inc. v. Missouri Dept. of Labor and Indus. Relations*, 157 S.W.3d 224, 228 -229 (Mo. App. 2004); *Greenbriar Hills Country Club v. Director of Revenue*, 47 S.W.3d 346, 357 (Mo. banc 2001).

²⁴⁹ *Greenbriar Hills Country Club v. Director of Revenue*, 47 S.W.3d 346, 357 (Mo. banc 2001).

rate case, the decision to do so is entirely with KCPL's power. In addition, KCPL has pursued some issues that only directly benefit shareholders, such as the La Cygne accounting authority and, of course, a higher ROE. In recent rate cases, KCPL has incurred rate case expenses substantially higher than historical levels and higher than other utilities in Missouri.

The Commission finds that in order to set just and reasonable rates under the facts in this case, the Commission will require KCPL shareholders to cover a portion of KCPL's rate case expense. One method to encourage KCPL to limit its rate case expenditures would be to link KCPL's percentage recovery of rate case expense to the percentage of its rate increase request the Commission finds just and reasonable.²⁵⁰ The Commission determines that this approach would directly link KCPL's recovery of rate case expense to both the reasonableness of its issue positions and the dollar value sought from customers in this rate case.²⁵¹

The Commission concludes that KCPL should receive rate recovery of its rate case expenses in proportion to the amount of revenue requirement it is granted as a result of this Report and Order, compared to the amount of its revenue requirement rate increase originally requested. This amount should be normalized over three years. The Commission also finds that it is appropriate to require a full allocation to ratepayers of the expenses for KCPL's depreciation study, recovered over five years, because this study is required under Commission rules to be conducted every five years.

²⁵⁰ This method can be expressed as: $(\text{Revenue Requirement Approved} / \text{Original Revenue Requirement Requested}) \times 100 = \text{allowable percentage of rate case expense}$.

²⁵¹ It is understood that some of the issues litigated in this case do not directly affect the overall revenue requirement granted by the Commission; but it is also clear that the vast majority of the litigated issues do have a direct or indirect impact on the revenue requirement. Accordingly, percentage sharing is a reasonable approach to correlating recovery of rate case expense to the relationship between the amount of litigation that benefited both ratepayers and shareholders and that which benefited only shareholders.

H. Management audit

Findings of Fact

170. KCPL's Administrative & General ("A&G") costs from 2011 through 2013 were higher than three other utilities operating in this region. While the reasons for this are unknown, it may be due to a structural problem.²⁵²

171. Staff's analysis of KCPL's A&G expenses, which examined the peer group utilities that KCPL used to determine executive compensation, credibly demonstrated that KCPL has some of the highest A&G expenses of its national peers and Missouri utilities. Of the group examined, KCPL has the highest A&G costs per customer, per dollar of revenue, and compared to its operations and maintenance expense, and the third highest A&G expense per megawatt hour of electricity sold.²⁵³

172. A management audit focused on identifying and achieving efficiencies and cost reductions should benefit both KCPL's customers and shareholders.²⁵⁴

Conclusions of Law and Decision

MECG and MIEC witness Kollen has recommended that the Commission direct KCPL to undergo a management audit by an independent auditor to identify cost savings and efficiencies. The evidence showed that KCPL's A&G expenses are significantly higher than its peers, but that the cause for this discrepancy is unknown. The Commission finds that it would benefit both customers and shareholders to find efficiencies and reduce costs, so a management audit is a reasonable mechanism to accomplish this result. However, rather than charge the costs of such an audit to KCPL's customers or shareholders, such an audit could be performed by the Commission's Staff. The Commission will initiate a

²⁵² Ex. 500, Kollen Direct, p. 8-15.

²⁵³ Ex. 226, Majors Surrebuttal, p. 40-54.

²⁵⁴ Ex. 501, Kollen Surrebuttal, p. 12.

separate case after this case is concluded that directs the Commission's Staff²⁵⁵ to audit KCPL's A&G expenses.

I. Clean Charge Network

Findings of Fact

173. On January 26, 2015, KCPL publicly announced that it had launched a joint initiative ("Clean Charge Network") with KCP&L Greater Operations Company to install and operate more than 1,000 electric vehicle charging stations throughout the greater Kansas City region. The charging stations would be capable of supporting more than 10,000 electric vehicles and upon completion would be the largest such utility-owned installation in the United States.²⁵⁶

174. During a two-year pilot period, the Clean Charge Network would offer free charging on every station to all electric vehicle drivers. Any electricity costs for charging station usage would be paid by partnering organizations during the pilot period.²⁵⁷

175. KCPL has initiated the Clean Charge Network to promote environmental sustainability, reduce carbon emissions, and help the Kansas City region attain EPA regional ozone standards.²⁵⁸

176. KCPL has requested that the charging stations placed in service in its Missouri service territory as of May 31, 2015, be included in rate base as a part of the revenue requirement for this case.²⁵⁹ As of that date, KCPL has invested \$732,559 in its Clean Charge Network in Missouri, but plans to invest a total of \$7-8 million.²⁶⁰

²⁵⁵ The Commission's Staff includes a unit that specializes in management services and that has conducted management audits of varying scope in the past at the Commission's discretion.

²⁵⁶ Ex. 119, Ives Supplemental Direct, p. 1-2.

²⁵⁷ *Id.* at p. 2.

²⁵⁸ *Id.* at p. 3.

²⁵⁹ *Id.* at p. 5.

²⁶⁰ Transcript, Vol. 11, p. 567, 600.

177. KCPL developed the Clean Charge Network project without soliciting input from any of the parties to this case, including those parties representing customers who would bear the costs of the project if the Commission includes those costs in KCPL's revenue requirement.²⁶¹

178. KCPL has not established any criteria by which it proposes to measure the success of the Clean Charge Network, and has not conducted studies concerning the five areas of alleged public benefit – beneficial electrification, environmental benefits, economic development, customer programs, and cost and efficiency benefits.²⁶²

179. Important program details relating to ratepayer subsidies, program goals, income distribution, public participation, tariffs, program design, scope of the investment, risk shifting, cost-benefit analysis, participating organizations, host sites, free electricity offerings, anti-competitive subsidies, and proper performance-based measures to determine effectiveness are all missing from KCPL's proposal and would be best addressed in a separate working case.²⁶³

180. A KCPL witness agreed that a working case would be a good place to address long-term policy issues relating to the Clean Charge Network, including potential impacts on both customers and the company.²⁶⁴

Conclusions of Law and Decision

KCPL's proposed Clean Charge Network is an important first step in creating an infrastructure to serve the increasing number of customers who choose to purchase electric vehicles, and the Commission commends KCPL for its efforts to anticipate this future demand and for its commitment to environmental sustainability. However, this issue was

²⁶¹ *Id.* at p. 626-27.

²⁶² *Id.* at p. 577-83.

²⁶³ Ex. 304, Dismukes Rebuttal, p. 11-39.

²⁶⁴ Transcript, Vol. 11, p. 577.

raised for the first time more than three months after KCPL first filed this case and without seeking input from this Commission or other parties to the case. The proposal currently lacks important information that is critical to designing and implementing a program unlike any other existing in the state. While the Commission believes that it would be beneficial to move forward with the Clean Charge Network, it is premature to require KCPL's customers to bear the costs of the program. The Commission concludes that KCPL has failed to meet its burden of proof to demonstrate that the charging stations placed in service in its Missouri service territory as of May 31, 2015, should be included in rate base as a part of the revenue requirement for this case, so that request will be denied. The Commission will establish a working case in order to address the legal and long-term policy issues relating to the Clean Charge Network.

J. Income tax issues

CWIP-related ADIT

Findings of Fact

181. Accumulated deferred income taxes ("ADIT") are assets or liabilities that represent the cumulative amounts of additional income taxes that are estimated to become receivable or payable in future periods. Future income taxes are impacted by tax returns filed today because of differences between book accounting and income tax accounting regarding the timing of revenue or expense recognition.²⁶⁵

182. Specific provisions within GAAP require recognition of income tax impacts from these book/tax timing differences, by recording ADIT assets or liabilities. ADIT assets generally occur when revenue taxation occurs prior to book recognition of the revenues or when the tax deductibility for expenses is subsequent to the book recognition of the

²⁶⁵ Ex. 502, Brosch Direct-Revenue Requirement, p. 46.

expense. ADIT liabilities, on the other hand, represent delayed taxation of revenues or advance deduction of expenses, in relation to the timing of the same transactions on the books. ADIT balances exist to recognize that certain tax expenses are determinable today, but actually become payable in the future whenever book/tax timing differences ultimately reverse.²⁶⁶

183. From a ratemaking perspective, a utility's persistently large credit ADIT balances caused by the deferred payment of recorded tax expenses represent a significant source of capital to the utility. ADIT balances represent a form of zero-cost capital to the utility created by the income tax savings permitted under tax laws and regulations that are not immediately "flowed through" to ratepayers and would benefit only shareholders unless properly recognized as a rate base reduction. ADIT balances are normally included in rate base as reductions by regulators, so as to limit the utility to only a return on the net amount of investor-supplied capital to support rate base assets.²⁶⁷

184. KCPL records ADIT that is associated with Construction Work in Progress ("CWIP") reflected on its books and records. This ADIT represents a free source of capital funds available for use by the utility before the construction project is completed and included in plant-in-service. CWIP is excluded from the rate base on which KCPL earns a return in the ratemaking process. Although CWIP is not included in rate base, KCPL is allowed to earn an Allowance for Funds Used During Construction ("AFUDC") before the property under construction is added to rate base. AFUDC is accrued during the construction of the asset and included in rate base when the plant is placed into service. The amount of AFUDC is included in depreciation and rate base over the life of the plant. For the calculation of AFUDC, there is no consideration for ADIT as a reduction to the base

²⁶⁶ *Id.* at p. 47.

²⁶⁷ *Id.* at p. 48.

on which it is calculated; the AFUDC is calculated on the “gross” amount, with no consideration of ADIT.²⁶⁸

185. Because ADIT is not considered in the calculation of AFUDC, the benefit must be accounted for by an offset to rate base for ADIT associated with CWIP balances.²⁶⁹

186. KCPL ratepayers provide fully-normalized income taxes in the cost of service regardless of the actual amount paid to the IRS. Even if KCPL is not realizing all the benefits of accelerated depreciation due to a net operating loss position, it does not invalidate the fact that ratepayers are providing several million dollars in cash income taxes.²⁷⁰

Conclusions of Law and Decision

KCPL excluded the ADIT liability related to CWIP since the capital expenditures have not been included in rate base. KCPL argues that since CWIP cannot be included in rates in Missouri, KCPL’s shareholders, not its customers, are paying the costs associated with plant under construction. KCPL states that it is unfair to include the ADIT offset to rate base when the CWIP itself may not be included.

The Commission considered this issue recently in another rate case. In reaching the conclusion that it is appropriate to reduce rate base for CWIP-related ADIT balances, that Commission stated that:

CWIP related ADIT balances must be accounted for in rate base because AFUDC is applied to Ameren Missouri’s gross investment in CWIP, with no recognition given to the CWIP-related ADIT amounts that serve to reduce the company’s actual net capital requirements for CWIP... In other words, failure to recognize the CWIP-related ADIT balance in the company’s rate base will overstate the companies AFUDC costs and future rate base, essentially

²⁶⁸ Ex. 200, Staff Report-Revenue Requirement Cost of Service, p. 178.

²⁶⁹ Ex. 226, Majors Surrebuttal, p. 64.

²⁷⁰ Ex. 226, Majors Surrebuttal, p. 64-65.

allowing the company to earn AFUDC and a return on capital supplied by ratepayers.²⁷¹

KCPL asserts that its situation is different than that of the utility at issue in File No. ER-2012-0166 because KCPL has a net operating loss and, as a consequence, KCPL has more deductions than it has revenues during the applicable period, so it has not and will not receive a cash tax benefit. However, KCPL ratepayers provide fully-normalized income taxes in cost of service regardless of whether KCPL pays those taxes concurrently to the IRS. Even if KCPL is not realizing all the benefits of accelerated depreciation due to a net operating loss position, it does not invalidate the fact that ratepayers are providing several million dollars in cash income taxes. The Commission concludes that the amount of ADIT related to CWIP should be an additional reduction to KCPL's rate base.

1KC Place lease ADIT

Findings of Fact

187. KCPL occupies leased office space in downtown Kansas City in a building known as 1 KC Place and has received certain lease abatement benefits in connection with its lease agreement. On its books, KCPL has recorded a significant liability balance to recognize the delayed obligation to make additional lease payments. In connection with this liability balance, a large and offsetting deferred tax asset was recorded to recognize that accrued but unpaid future lease costs are not currently deductible for income tax purposes. KCPL proposes to include in rate base the debit ADIT item to increase rate base, but not the corresponding accrued lease liability balance that would reduce rate base if recognized.²⁷²

²⁷¹ Report and Order, *In the Matter of Union Elec. Co., d/b/a Ameren Missouri's Tariff to Increase Its Annual Revenues for Elec. Serv.*, ER-2012-0166, 2012 WL 6643105 (Dec. 12, 2012).

²⁷² Ex. 502, Brosch Direct-Revenue Requirement, p. 55.

188. The accrued liability for the deferred rent payments on the 1KC Place lease has not been included in rate base, but this accrued liability is being amortized as a reduction to rent expense.²⁷³

189. This reduced rent expense is included in the cash voucher line within the expense lead day calculations of KCP&L's lead lag study. Although there has not been a separate lead lag computation on the 1KC Lease directly, the reduction in rent expense is included in the overall cash working capital computations and in the rent expense included in cost of service.²⁷⁴

Conclusions of Law and Decision

A proposed adjustment concerns the ADIT asset related to the 1KC Place lease. This ADIT increases rate base, unlike the ADIT related to CWIP. Because the deduction for the 1KC Place lease has not been taken on a tax return, but has been taken for financial and regulatory purposes, the ADIT asset represents tax benefits that the ratepayers have received in computing income tax expense but that KCPL has not received on its tax returns.

KCPL has not included the accrued liability for the deferred rent payments on the 1KC Place lease in rate base. This exclusion is appropriate because the accrued liability is being amortized monthly as a reduction to rent expense in cost of service. This reduced rent expense is also included in KCPL's lead lag computation of cash working capital. The Commission concludes that the impact of this liability has been included in the case, and the ADIT asset related to this liability should be included in rate base, so no adjustment should be made.

²⁷³ Ex. 112, Hardesty Rebuttal, p. 6.

²⁷⁴ *Id.* at p. 6-7.

Employee compensation ADIT

Findings of Fact

190. Certain elements of employee compensation are paid much later than they are earned, requiring the Company to recognize an accrued liability for such deferred compensation and bonus pay that is owed to its employees.²⁷⁵

191. The accrued liability for the employee compensation and bonus pay has not been included in rate base.²⁷⁶

192. This accrued liability is for two different items. One item is the ADIT asset for the deferred compensation, where certain executives have elected to defer the payout of a portion of their salary and incentive compensation to a future period. The second item is the ADIT asset for the incentive compensation (bonus pay) that is accrued during the year, but is not paid out in cash until March 15 of the following year. For both of these items, the salary and incentive compensation is included in cost of service expense and in the total payroll or cash voucher line on the lead day calculations of KCP&L's lead lag study. Although there has not been a separate lead lag computation on these liabilities directly, the salary and incentive compensation is included in the overall cash working capital computations and in the payroll expense included in cost of service.²⁷⁷

Conclusions of Law and Decision

The proposed adjustment to exclude the ADIT asset related to employee compensation and bonus pay from rate base would also decrease the revenue requirement. The proposed adjustment, which is similar to the proposal for the 1KC Place lease, is based on an argument that the liability for the accrued employee compensation

²⁷⁵ Ex. 502, Brosch Direct-Revenue Requirement, p. 56.

²⁷⁶ Ex. 112, Hardesty Rebuttal, p. 7.

²⁷⁷ *Id.* at p. 6-7.

and bonus pay is not in rate base so the ADIT asset related to this tax timing difference should also be excluded. However, both deferred compensation and bonus pay are included in the overall cash working capital computations, and the payroll expense is included in cost of service. Therefore, since the impact of this liability has been included in this case, the Commission concludes that the ADIT asset related to this liability should be included in rate base and no adjustment should be made.

Net operating tax losses

Findings of Fact

193. KCPL files its taxes as part of a consolidated group, consisting of GPE and its affiliated companies. Consolidated filing benefits the entire group, but it is the nature of a consolidated filing that any given member may be better off in some years and worse off in other years as a result of consolidated filing.²⁷⁸

194. A net operating loss (“NOL”) is created when, in any year, a taxpayer reports more deductions than it has taxable income. Under the generally applicable tax rules, an NOL can be carried back two years or forward 20 years. In the year in which it is carried to, an NOL is treated like an additional deduction, reducing the taxable income otherwise produced in that year. When an NOL must be carried forward, a portion of the deductions claimed by the taxpayer in the year that the NOL is created will not offset taxable income and not reduce the taxpayer’s tax liability – thus, no cost-free capital was received for the amount of NOL that did not reduce the tax liability.²⁷⁹

195. In KCPL’s rate case application, it reflected the impact of its NOL carryforward for tax purposes as an ADIT asset (a deferred tax asset) of approximately \$37.8 million.

²⁷⁸ Ex. 112, Hardesty Rebuttal, p. 9, 16.

²⁷⁹ *Id.* at p. 11-12.

This had the effect of increasing rate base by that amount (by decreasing the overall ADIT balance which reduces rate base).²⁸⁰

196. KCPL reduces its rate base by its net ADIT liability balance (sum of deferred tax assets and deferred tax liabilities) as a result of timing differences between deductions for tax purposes and financial statement purposes. The net deferred tax liability is used to reduce rate base because it represents a source of cost-free capital (a reduction in the amount of cash paid for tax purposes) that KCPL has received as a consequence of claiming certain tax deductions. In a year that KCPL generates a net operating loss for tax purposes that is carried forward, the NOL carryforward reduces the amount of cost-free capital it received. Therefore, KCPL has reflected in its rate base computation the actual impact its NOL has had on the amount of cost-free capital it received using the method prescribed under the Internal Revenue Service regulations to allocate losses to companies within a consolidated group.²⁸¹

197. KCPL computes the amount of NOLs allocated to each subsidiary based on when and how the NOLs are used by the consolidated group in accordance with the Tax Allocation Agreement Among Great Plains Energy Incorporated and Affiliates (“Tax Allocation Agreement”). The Tax Allocation Agreement was put in place to ensure that each subsidiary received benefit for all tax attributes when used by the consolidated group and to ensure that all subsidiaries paid any tax liabilities it incurred or got benefit for any tax credits or NOLs it generated, but only when incurred or used by the consolidated group. This method most accurately represents the economics and the cash flow that actually occurs when a consolidated return is filed.²⁸²

²⁸⁰ *Id.* at p.8.

²⁸¹ *Id.* at p. 8-9.

²⁸² *Id.* at p. 16.

198. In its calculations, KCPL has used the actual amount of cost-free capital it actually received; it has used the amounts reflected on its financial records. These amounts reflect the actual cash that KCPL has received in connection with the claiming of its tax deductions.²⁸³

199. MEGC proposes to reduce the NOL carryforward ADIT asset by computing the NOL amounts on a KCPL “stand-alone” basis instead of using the amounts computed under the Tax Allocation Agreement. This proposed adjustment would involve imputing an additional amount of cost-free capital equal to the additional amount that would have been received as of the end of the true-up period had KCPL filed in this stand-alone basis. This approach would produce more cost-free capital than KCPL actually received, thereby reducing the amount of deferred tax asset included in rate base.²⁸⁴

Conclusions of Law and Decision

MEGC has proposed an adjustment that would reduce KCPL’s rate base amount as a result of reducing the NOL carryforward ADIT asset by computing the NOL amounts on a KCPL “stand-alone” basis instead of using the amounts computed under the Tax Allocation Agreement. MEGC suggests that the Commission’s affiliate transaction rule may be used to justify a change in the way the NOL deferred tax assets are computed for KCPL.

Commission Rule 4 CSR 240-20.015(2) states:

(2) Standards.

(A) A regulated electrical corporation shall not provide a financial advantage to an affiliated entity. For the purposes of this rule, a regulated electrical corporation shall be deemed to provide a financial advantage to an affiliated entity if –

²⁸³ *Id.* at p. 14

²⁸⁴ *Id.*

1. It compensates an affiliated entity for good or services above the lesser of –
 - A. The fair market price; or
 - B. The fully distributed cost to the regulated electrical corporation to provide the goods or services for itself; or
2. It transfers information, assets, goods or services of any kind to an affiliated entity below the greater of –
 - A. The fair market price; or
 - B. The fully distributed cost to the regulated electrical corporation.

Section 4 CSR 240-20.015(1)(B) defines affiliate transaction as:

B. Affiliate transaction means any transaction for the provision, purchase or sale of any information, asset, product or service, or portion of any product or service, between a regulated electrical corporation and an affiliated entity, ...

The Commission has ruled on this issue in a recent case with a very similar fact situation. In that case, the Commission stated that “[t]he Commission’s affiliate transaction rules do not apply in this situation because there is no transaction involved. The affiliate transaction rules are intended to control transfers of goods or services between regulated utilities and their affiliates... where there is no transaction, the restrictions of the rule have no meaning.”²⁸⁵ The Commission finds that the affiliate transaction rule does not apply to this situation.

In that prior case, where Ameren Missouri used the consolidated NOL as allocated to the utility under a tax allocation agreement between the subsidiaries of a consolidated group, the Commission stated that:

Ameren Missouri proposes to use the NOLC [net operating loss carryforward] it has actually accumulated rather than a hypothetical NOLC proposed by MIEC and supported by Staff, MIEC advocates a policy that arrangements between affiliates should always be interpreted in a manner that benefits ratepayers, even if that results in a detriment to the utility. There is no basis in law or fact for such a policy. The Commission must balance the interests of ratepayers and shareholders to set just and reasonable rates. Ameren Missouri’s position is fair and will be adopted.

²⁸⁵ Report and Order, ER-2014-0258, *In the Matter of Union Elec. Co., d/b/a Ameren Missouri’s Tariff to Increase Its Revenues for Elec. Serv.*, 320 P.U.R.4th 330 (Apr. 29, 2015).

MECG attempts to distinguish the prior case by alleging that the Tax Allocation Agreement to which KCPL is obligated does not benefit KCPL or its ratepayers. Even if no benefits have accrued to KCPL in the recent past, that does not mean that KCPL and its ratepayers will not benefit in the future. There is no evidence in the record showing that KCPL has attempted to manipulate its tax obligations to take advantage of ratepayers, and the Commission will not question management decisions made by the company with regard to its tax filings under such a tax allocation agreement. The Commission concludes the proposed adjustment to the computation of ADIT assets related to net operating losses should be rejected.

K. Class cost of service, rate design, and tariff rules

- 1. Class cost of service-production plant- What methodology should the Commission use to allocate fixed production plant costs among customer classes?**
- 2. Rate design**
 - a. What methodology is most reasonable for allocating net cost of service among the customer classes in this case?**
 - b. How should any revenue increase be allocated among rate schedules?**
 - c. What, if any, interclass shift in revenue responsibilities should the Commission make?**

Findings of Fact

200. A class cost of service study is a method by which utility costs and revenues are reconciled across different customer classes. In general, utilities incur three categories of costs: 1) customer-related costs, which are costs associated with connecting customers to the distribution system, metering usage and other customer support functions; 2) energy-related costs, which are costs that tend to change with the amount of electricity sold; and 3) demand-related costs, which are costs associated with meeting maximum electricity demands.²⁸⁶

²⁸⁶ Ex. 303, Dismukes Direct, p. 4-6.

201. KCPL has invested almost \$8.7 billion in its various production, transmission and distribution facilities. Of this, over 63 percent is associated with KCPL's investment in its various methods of generating electricity.²⁸⁷

202. Separate class cost of service studies were provided by KCPL, Staff, OPC, MEGG/MIEC, and the U.S. Department of Energy.²⁸⁸

203. The Commission benefits from the presentation of alternative class cost of service studies, but those study results should only be used as a guide.²⁸⁹

204. On June 16, 2015, some of the parties filed a *Non-Unanimous Stipulation and Agreement on Certain Issues* ("Rate Design Agreement"), which addressed issues relating to class cost of service, rate design, and tariffs. That Rate Design Agreement stated, in part, that:

Class Cost of Service, Production Plant: The Signatories agree that the Commission should allocate any increase to revenue requirement resulting from this case as an equal percentage increase to all the classes. Given that an equal percent revenue allocation is consistent with some party recommendations contained on the record, the Signatories do not believe that the Commission needs to make specific findings as to the appropriate methodology for allocating production plant costs among the customer classes.

Rate Design: The Signatories agree that the appropriate methodology, in this case, for most reasonably allocating net cost of service among the customer classes, for allocating revenue increase among rate schedules, and for interclass shifts in revenue responsibilities, should be an equal percentage increase to all customer classes.

The Rate Design Agreement is attached hereto as Attachment A and incorporated herein.

KCPL objected to the Rate Design Agreement.

²⁸⁷ Ex. 201, Staff Accounting Schedules, Schedule 2, p. 6-7.

²⁸⁸ Ex. 135, Rush Rebuttal, p. 45.

²⁸⁹ Ex. 220, S. Kliethermes Surrebuttal, p. 1.

Conclusions of Law and Decision

Based on the evidence in this case, the Commission finds that acceptance of the provisions of the Rate Design Agreement on these issues is a fair and reasonable resolution of these issues, since an equal percent revenue allocation is consistent with some party recommendations. The Commission adopts the provisions of the Rate Design Agreement stated above.

3. Residential customer charge- At what level should the Commission set KCPL's residential customer charge?

Findings of Fact

205. The residential customer charge is designed to include those costs necessary to make electric service available to the customer, regardless of the level of electric service utilized. Examples of such costs include monthly meter reading, billing, postage, customer accounting service expenses, a portion of costs associated with meter investment, and the service line.²⁹⁰

206. KCPL proposes to increase the customer charge for the residential class from \$9.00 to \$25.00, an increase of approximately 178 percent for those customers.²⁹¹

207. KCPL's residential customer-related costs are \$11.88 per month, which is based on the results of Staff's class cost of service study.²⁹²

208. KCPL requests that the Commission include as part of the customer charge additional costs for local facility equipment, which are costs for the secondary distribution system and line transformers.²⁹³

²⁹⁰ Ex. 202, Staff Rate Design and Class Cost of Service Report, p. 34.

²⁹¹ Ex. 303, Dismukes Direct, p. 14.

²⁹² Ex. 247, Affidavit of R. Kliethermes to correct testimony.

²⁹³ Ex. 135, Rush Rebuttal, p. 20-22.

209. KCPL's proposal to include local facility equipment costs in the residential customer charge is inconsistent with its own class cost of service study. That study defines local facility equipment as demand-related, and those types of costs are typically recovered through a demand charge for those customers that are demand-metered. However, residential customers are not demand-metered, so their demand-related costs are usually recovered through energy charges, not monthly customer charges.²⁹⁴

210. The signatory parties to the Rate Design Agreement recommended that the Commission decline to increase the current customer charge of \$9.00 per month.

Conclusions of Law and Decision

Customer-related costs are generally recovered through the customer charge, which serves to prevent higher usage customers from subsidizing lower usage customers, sends all customers more accurate energy pricing signals, and provides more stable and predictable funding for utilities' fixed costs. Other costs are recovered through volumetric rates that vary with the amount of electricity used. Staff's class cost of service study determined that the costs related to residential customers are \$11.88 per month. While KCPL requests that additional costs related to local facility equipment be included in the customer charge, the Commission finds that inclusion of those additional costs would be inappropriate because that request is inconsistent with KCPL's own class cost of service study.

Determining an appropriate customer charge is a question of rate design, not a question of the company's revenue requirement. Any increase in the company's customer charge should be accompanied by a decrease in volumetric rates so that, in theory, the company recovers the same amount of revenue. The Commission considers that an

²⁹⁴ Ex. 305, Dismukes Surrebuttal, p. 8, See also, Ex. 218, R. Kliethermes Surrebuttal, p. 2-4.

important goal of rate design is to recover costs from those who cause the costs to be incurred. Therefore, the Commission concludes that the appropriate residential customer charge is \$11.88 per month, based on Staff's cost of service study.

4. Residential energy charge- At what level should the Commission set KCPL's residential energy charges?

Findings of Fact

211. In KCPL's rate design proposal for the residential class, the company has made a number of adjustments, particularly to the winter rate block structures. In KCPL's last rate case, off-peak winter rate schedules were providing less than their cost of service. The Commission ordered that certain rates blocks within the class should be increased by an additional five percent.²⁹⁵

212. In this case, KCPL is proposing to decrease some of the very rates that the Commission previously ordered to increase. Because a class cost of service study shows that the off-peak winter rate schedules are providing a higher return than the on-peak summer rate schedules, decreasing the rates at this time may have unintended results.²⁹⁶

213. In the Rate Design Agreement, the signatory parties agreed that, "[w]ith regard to the residential energy charge, the Signatories agree that after accounting for the continuation of the existing customer charges, the residential energy charges will be increased by the same percentages to achieve required revenues."

Conclusions of Law and Decision

The Commission finds that KCPL's proposed adjustments regarding the residential energy charges are inappropriate due to possible unintended results. The Commission finds that acceptance of the provisions of the Rate Design Agreement on this issue is a fair

²⁹⁵ Ex. 303, Dismukes Direct, p. 40.

²⁹⁶ *Id.* at p. 41.

and reasonable resolution of the issue. Since the Commission has decided to increase the residential customer charge, that provision will need to be modified slightly. The Commission concludes that after accounting for the increase in the existing customer charges, the residential energy charges will be increased by the same percentages to achieve required revenues.

5. **Time of day – should the time of day rate be frozen from the addition of future customers (KCPL proposal) or should KCPL be required to file modified time of day tariff provisions in its next rate case?**
6. **Special rates-two-part time-of-use- Should the two-part time of use rate be eliminated from the addition of future customers (KCPL proposal) or should KCPL file a modified two-part time of use tariff provisions in its next rate case?**
7. **Real time pricing tariffs – should the real time pricing rate be frozen from the addition of future customers or should KCPL file modified real time pricing tariff provisions in its next rate case?**

Findings of Fact

214. KCPL proposes to freeze availability of the residential time-of-use rate because it only has 38 customers and does not perform as it should.²⁹⁷ KCPL also proposes to freeze two special rates, the two-part time-of-use and real time pricing tariffs, because they are not used or no longer functional.²⁹⁸

215. KCPL opposes imposing a new time-of-use rate because it is beginning two projects that will fundamentally impact a time-of-use design, the AMI metering roll-out and the implementation of a new billing system. KCPL cannot commit to a schedule for a new time-of-use tariff because it needs more information about these new system projects and possible impacts to integrated resource planning and MEEIA programs.²⁹⁹

²⁹⁷ Ex. 134, Rush Direct, p. 66.

²⁹⁸ *Id.* at p. 59.

²⁹⁹ Ex. 135, Rush Rebuttal, p. 61.

216. The Division of Energy proposes that two-part time-of-use and real time pricing tariffs remain available and that KCPL be required to submit revised tariffs and supporting documentation in its next rate case.³⁰⁰

217. In the Rate Design Agreement, the signatory parties agreed that:

Regarding time of day rates, the Signatories agree that current residential and other special two-part time-of-day or real time pricing tariffs remain available, and the Signatories would request that the Commission order Kansas City Power & Light Company to complete a study regarding these issues within 2 years in which no party is obligated to support the findings of that study or any proposed tariff design as a result of that study.

Conclusions of Law and Decision

KCPL has requested that the Commission freeze the residential time-of-use rates, two-part time-of-use, and real time pricing tariffs in this proceeding and not require KCPL to file new tariffs in its next rate case. The Commission agrees that these rates should be frozen from the addition of future customers for the present time. However, it is clear that all of these rates need to be redesigned, and at least the time-of-use tariff is far too important in meeting the goals of MEEIA and providing customer choices for energy efficiency and bill savings to redesign at an unknown time in the future. The Commission concludes that KCPL should complete a study regarding all of these issues within two years of the effective date of this order.

8. Should the ResB rate structure be changed to make it consistent with ResA and ResC rate structures?

Findings of Fact

218. The residential class has three main sub-class rate classifications – general use (ResA), one meter general use and space heat (ResB), and two meter rate with general use on one meter and a separate meter for space heating (ResC).³⁰¹

³⁰⁰ Ex. Hyman Rebuttal, p. 32.

219. Staff has recommended a rate structure change to ResB to make it consistent with ResA and ResC rate structures, to which KCPL agrees.³⁰²

220. In the Rate Design Agreement, the signatory parties stated that “[t]he Signatories agree to allow modification to the structure of the ResB rate to add an intermediate block rate which will be set equal to the first block rate to make it consistent with the ResA and ResC rate structures.”

Conclusions of Law and Decision

Based on the evidence in this case, the Commission finds that acceptance of the provisions of the Rate Design Agreement on this issue is a fair and reasonable resolution of the issue. The Commission adopts the provisions of the Rate Design Agreement stated above.

9. Commercial and industrial –

- a. SG, MG, LP and LGS energy charges – at what level should the Commission set KCPL’s SG, MG, LP and LGS energy charges?**
- b. SG, MG, LP and LGS separate meter space heating energy charges and the first energy block rate for the winter rates – at what level should these energy charges be set?**
- c. Should the Commission adopt MIEC/MECG’s rate design proposal for the LGS and LP rate classes, or some a variant of it?**

Findings of Fact

221. KCPL’s Large General Service (“LGS”) and Large Power Service (“LP”) tariffs consist of a series of charges differentiated by voltage level. There are separate charges for service at secondary voltage, service at primary voltage, service at substation voltage, and service at transmission voltage. The rates charged at the higher voltage levels are

³⁰¹ Ex. 202, Staff Rate Design and Class Cost of Service Report, p. 3.

³⁰² *Id.*

lower than the rates charged at the lower voltage levels in order to recognize differences in cost of service.³⁰³

222. In KCPL's LGS and LP rate schedules, the specific energy charges to be applied to a particular customer's usage decrease as the customer's load factor increases. Energy usage is charged in a sequential manner, so that energy is first billed at the initial 180 hour energy block; any usage in excess of this is billed at the second 180 hour energy block; and any remaining usage is billed at the tail block rate. In order to receive the benefit of the lower energy charges in the second energy block and the tail block, customers must first fill the preceding blocks and pay for energy at the associated higher energy rate.³⁰⁴

223. These tariffs collect revenue through, among others, a demand and energy charge, but KCPL is currently collecting a large portion of its fixed costs through LGS and LP energy charges, rather than just collecting its variable costs.³⁰⁵

224. In the Rate Design Agreement, the signatory parties agreed as follows:

Except as provided in the following paragraph, as rate design relates to Commercial and Industrial classes the Signatories agree with the following as it relates to section B(e)(1)-(3) and section (B)(f)(1) and (3) in the *Issues List*: the following rate components of each class be increased across-the-board for each class on an equal percentage basis after:

- Increasing the first winter energy block rate of the frozen All-Electric Service rate schedules for the SGS, MGS, and LGS rate classes increasing by an additional 5%;
- Changing the winter second and third SGS all electric block rates to match the winter second and third general service SGS block rates.

As explained in the pre-filed Direct Cost of Service and Rate Design testimony of Maurice Brubaker, at pages 32-33, the general service LGS and LP second block energy rates shall receive 75% of the applicable class percentage increases and there shall be no increase to the tail blocks of the general service LGS and LP energy rates. Any remaining increase in revenue requirement for these classes shall be collected through an equal percentage increase in the customer, demand and first energy blocks.

³⁰³ Ex. 554, Brubaker Direct-Rate Design, p. 28.

³⁰⁴ *Id.* at p. 29.

³⁰⁵ *Id.* at p. 30-31.

Conclusions of Law and Decision

Based on the evidence in this case, the Commission finds that acceptance of the provisions of the Rate Design Agreement on these issues is a fair and reasonable resolution of the issues. The Commission adopts the provisions of the Rate Design Agreement stated in paragraph 225 above.

10. Special interruptible – should the special interruptible rate be frozen from the addition of future customers?

Findings of Fact

225. KCPL has proposed to freeze or eliminate the special interruptible rate.³⁰⁶

226. In the Rate Design Agreement, the signatory parties state that “[t]he Signatories do not oppose Kansas City Power & Light Company’s request to eliminate the special interruptible rate.”

Conclusions of Law and Decision

Based on the evidence in this case, the Commission finds that acceptance of the provisions of the Rate Design Agreement on this issue is a fair and reasonable resolution of the issue. The Commission adopts the provisions of the Rate Design Agreement stated above, and the special interruptible rate is eliminated.

11. Tariff rules and regulations- Should the return check charge be applied to payment forms beyond checks (electronic payments)?

Findings of Fact

227. KCPL has a large number of customers who no longer use paper checks for payment, but instead use electronic payment methods.³⁰⁷

228. KCPL has proposed to revise its tariff to extend the return payment charge to all forms of payment received by the company in the event of insufficient funds.³⁰⁸

³⁰⁶ Ex. 134, Rush Direct, p. 59.

³⁰⁷ Ex. 135, Rush Rebuttal, p. 63.

229. Staff supports KCPL's proposal³⁰⁹, and no other party has provided testimony or evidence on this issue.

Conclusions of Law and Decision

KCPL's request to extend the return payment charge to all forms of payment received by the company in the event of insufficient funds is reasonable. The Commission concludes that KCPL's tariff should be revised such that the return check charge shall be applied to payment forms beyond checks.

12. Tariff rules and regulations- Should the collection charge be increased to reflect the cost of this service?

Findings of Fact

230. KCPL has proposed to revise its tariff to increase the collection charge from \$25 to \$30 for in-field payments to reflect the cost of the service and to make the charge consistent with the current GMO collection charge.³¹⁰

231. Staff supports KCPL's proposal³¹¹, and no other party has provided testimony or evidence on this issue.

Conclusions of Law and Decision

KCPL requests to increase the collection charge for in-field payments. KCPL argues that this increase is to reflect the cost of the service and to make the charge consistent with the current GMO collection charge. The Commission concludes that KCPL has not adequately explained the need for this increased charge, and so has failed to meet its burden of proof to demonstrate that the increase is necessary. The Commission denies the request to increase the collection charge, and it will remain at \$25.00.

³⁰⁸ *Id.*

³⁰⁹ Ex. 233, Murray Surrebuttal, p. 2.

³¹⁰ Ex. 135, Rush Rebuttal, p. 63.

³¹¹ Ex. 233, Murray Surrebuttal, p. 2.

13. Economic development rider/urban core development rider – Should the Commission approve the Division of Energy’s proposal to link MEEIA participation to receipt of EDR and UCD incentives?

Findings of Fact

232. KCPL’s economic development rider (“EDR”) is designed to encourage industrial and commercial business development in Missouri and retain existing load where possible. The urban core development rider (“UCD”) has the purpose of encouraging industrial and commercial business development within a specific section of KCPL’s service territory.³¹² Only four KCPL customers participate in the EDR rider.³¹³

233. Division of Energy proposes that KCPL’s EDR and UCD riders be changed to require that customers participate in applicable MEEIA programs to be eligible for taking service under the special EDR and UCD rates.³¹⁴ The Division of Energy altered its proposal to make it easier for customers to opt-out of MEEIA programs and still receive the special EDR and UCD rates.³¹⁵

234. The EDR was re-designed in October 2013 to make the rider more functional for customers.³¹⁶

235. The Division of Energy’s proposal would be nearly impossible to administer because the proposal requires participation in all cost-effective energy efficiency programs.³¹⁷

Conclusions of Law and Decision

The Division of Energy recommends that the Commission require KCPL to link MEEIA participation with the receipt of EDR and UCD incentives. The MEEIA statute,

³¹² Ex. 354, Lohraff Direct, p. 8-9.

³¹³ Ex. 555, Brubaker Rebuttal, p. 23.

³¹⁴ *Id.* at p. 4.

³¹⁵ Ex. 355, Lohraff Surrebuttal, p. 5.

³¹⁶ Ex. 136, Rush Surrebuttal, p. 30.

³¹⁷ Ex. 135, Rush Rebuttal, p. 65.

Section 393.1075.7, RSMo, allows certain large users of electricity to opt out of participation in MEEIA programs, and the Division of Energy has amended its proposal to make it easier for such customers to opt-out and still receive EDR and UCD rates. However, the evidence showed that this proposal would be difficult for KCPL to administer. The EDR and UCD programs do not have high participation at this time, and adding further restrictions to this recently re-designed program would be counter-productive. In a recent Ameren Missouri rate case, File No. ER-2014-0258, this Commission rejected a very similar proposal and instead decided to establish a collaborative to examine this issue more closely. The Commission concludes that this proposal should be rejected, as well.

14. Should KCPL be required to establish a working group to review its Standby Service Tariff to ensure that rates are cost-based and reflect best practices?

Findings of Fact

236. Properly designed standby rates can facilitate efficiency gains, energy independence and demand-side management opportunities associated with combined heat and power (“CHP”) technologies. Standby rates are a key factor in determining the cost-effectiveness of such CHP projects.³¹⁸

237. KCPL has a standby rate tariff, which went into effect in 1997 and was revised in 2013.³¹⁹

238. Standby rate tariffs for The Empire District Electric Company and Ameren Missouri are currently under review by stakeholders.³²⁰

239. In the Rate Design Agreement, the signatory parties agreed that “a working group should be formed to review KCP&L’s Standby Service Tariff for the purposes of 1) ensuring that the design of standby rates and the terms and conditions of service are

³¹⁸ Ex. 354, Lohraff Direct, p. 12.

³¹⁹ *Id.*

³²⁰ *Id.*

consistent with best practices and 2) to develop recommendations on cost-based rate levels. Signatories request that the Commission order KCP&L to file a new Standby Service Tariff in its next general rate case.”

Conclusions of Law and Decision

While the standby rate is important for CHP projects, there has been no adequate showing that the existing KCPL tariff is deficient. The Commission finds it is not mandatory that KCPL to file a new standby rate tariff in its next general rate case. The Commission will not adopt the provision above in the Rate Design Agreement. However, since the standby rate tariffs of other electric utilities are currently under review, the Commission concludes that KCPL should complete a study regarding this issue within two years of the effective date of this order.

L. Revenues

Findings of Fact

240. In Section K, subsection 9 above, the Commission adopted provisions of the Rate Design Agreement regarding rate design for the LGS and LP classes for commercial and industrial customers. This provision recovers the bulk of the LGS and LP class revenue increase from this case through the second block energy rates for those classes, but has no increase for the third block energy rates.

241. This provision creates the potential for some customers to benefit from switching to a different and more advantageous rate schedule.³²¹

242. KCPL should have the opportunity to earn its revenue requirement when customers are switching rates schedules due to rate design shifts.³²²

³²¹ Ex. 238, Scheperle Rebuttal, p. 14; Transcript, Vol. 10, p. 447-48.

³²² *Id.*

243. Staff estimated that an adjustment of no more than \$250,000 should be made for possible LGS customers switching rates.³²³

244. KCPL estimated that the company could lose revenues of approximately \$590,000 due to rate switching from the rate design provision in the Rate Design Agreement. KCPL's estimate is more credible than the Staff estimate because KCPL looked at all commercial and industrial customers who may switch rates, while Staff only looked at the Large Power Class.³²⁴

245. On August 3, 2015, Staff and KCPL filed a *Non-Unanimous Stipulation and Agreement Regarding Class Kilowatt-Hours, Revenues and Billing Determinants, and Rate Switcher Revenue Adjustments* ("True-Up Agreement"), which attempted to 1) resolve all issues relating to weather normalization, rate revenues, and the resulting class billing determinants used in developing rates for all rate classes, and 2) assign a revenue shortfall of \$500,000 for rate switchers in the LGS and LP rate classes in order to account for any of those customers migrating to a different rate schedule to receive more advantageous pricing as a result of the Rate Design Agreement. Since OPC objected to the True-Up Agreement, it is a joint position statement, but Staff and KCPL urge the Commission to adopt its terms. OPC only objected to the provision relating to rate switching. The True-up Agreement is attached hereto as Attachment B and incorporated herein by reference.

Conclusions of Law and Decision

KCPL's estimate was that it would lose revenues of approximately \$590,000 if certain customers switched to a rate with more advantageous pricing. The True-Up Agreement proposed an adjustment of \$500,000 to account for rate switching customers which is a more reasonable estimate, as not all customers would be likely to switch rates at

³²³ Ex. 253, R. Kliethermes True-Up Direct, p. 5.

³²⁴ Ex. 167, Rush True-Up Rebuttal, p. 2-3.

the same time. Based on the evidence in this case, the Commission finds that acceptance of all the provisions of the True-Up Agreement on the issues contained therein is a fair and reasonable resolution of those issues. The Commission adopts the provisions of the True-Up Agreement in their entirety as stated in Attachment A to this Report and Order.

M. Low income weatherization

Findings of Fact

246. The Commission has authorized KCPL to participate in a program to weatherize homes of low-income residents called the Income Eligible Weatherization Program (“Program”). KCPL operates the Program independently of a similar federal weatherization program and provides funding to community action agencies that deliver such services within KCPL’s service territory.³²⁵

247. In Missouri, only KCPL and GMO operate their weatherization programs under the Missouri Energy Efficiency Investment Act (“MEEIA”). Other regulated electric utilities fund their weatherization services through customer contributions in base rates. Base rate recovery is preferable to recovery through MEEIA because regulated electric utilities offer MEEIA on a voluntary basis, and there is no guarantee that weatherization programs will be offered if a utility does not participate in MEEIA.³²⁶

248. Ninety-nine percent of MEEIA weatherization funds go to single-family homes. Funding the Program through KCPL’s base rates would allow Program funds to be made available to multi-family homes.³²⁷

³²⁵ Ex. 350, Buchanan Direct, p. 9.

³²⁶ *Id.* at p. 10-11.

³²⁷ Transcript, Vol. 20, p. 1970-71.

249. Before collecting Program funds through MEEIA, KCPL collected Program funds through base rates. KCPL presently has a surplus of Program funds previously collected through base rates.³²⁸

Conclusions of Law and Decision

Since the Program is an important service that benefits low-income residents, the Commission considers continuity of the Program to be a valuable goal. To avoid any continuity problems in the future, the Commission finds that collecting Program funds through base rates to be preferable. This will also provide for consistency across the state, as most other regulated electric utilities collect weatherization funds through base rates. The Commission concludes that KCPL should resume recovery of low-income weatherization program costs in base rates following the conclusion of KCPL's MEEIA Cycle 1 and cease recovery of these costs in future MEEIA applications. With regard to any surplus Program funds recovered previously through base rates, the unexpended low-income weatherization program funds collected through KCPL's base rates should be used to offset any expenditures relating to the Program.

N. Economic Relief Pilot Program

Findings of Fact

250. KCPL originally established the Economic Relief Pilot Program ("ERPP") to deliver energy affordability benefits to KCPL's qualifying low-income customers. The ERPP currently provides up to \$50 in bill credit for up to 1,000 participants. One half of the funding for the ERPP comes from shareholders and the other half from ratepayers. Between

³²⁸ Ex. 200, Staff Report-Revenue Requirement Cost of Service, p. 138-39.

January 2013 and September 2014, the average number of monthly participants was approximately 949, and 20,355 customer bills received an ERPP credit.³²⁹

251. In this case, KCPL proposes to double the amount of ERPP funding to \$630,000 for shareholders and \$630,000 for ratepayers. KCPL is also proposing to raise the current limit of participants to 1,500 and increase the available monthly bill credit to \$65.³³⁰

252. Currently any unused ERPP funds are to be used to offset demand-side management programs. KCPL recently received approval to offer its demand-side management programs under MEEIA, so KCPL proposes to direct any future unused ERPP funds to its Dollar-Aide program, which helps families pay heating, cooling and water bills during difficult financial times.³³¹ Staff recommends that any unspent funds be made available for future ERPP expenditures.³³²

253. The current ERPP tariff makes the program available to customers with an annual household income no greater than 185 percent of the Federal Poverty Level. Due to the Federal Poverty Level increasing in 2009, Staff recommends that KCPL change the eligibility requirement to 200 percent of the Federal Poverty Level.³³³

254. KCPL does not oppose Staff's recommendations to expand the eligibility requirements and make unspent ERPP funds available for future ERPP expenditures.³³⁴

Conclusions of Law and Decision

The ERPP is an important and valuable program to assist low-income customers with bill affordability. KCPL should be commended for establishing this program and

³²⁹ Ex. 134, Rush Direct, p. 42-43.

³³⁰ *Id.*

³³¹ *Id.* at p. 44.

³³² Ex. 200, Staff Report- Revenue Requirement Cost of Service, p. 138.

³³³ Ex. 200, Staff Report- Revenue Requirement Cost of Service, p. 137.

³³⁴ Ex. 135, Rush Rebuttal, p. 6.

recommending that it be expanded. The Commission concludes that the ERPP should be expanded as proposed by KCPL by doubling the funding, increasing the number of participants, and increasing the available bill credit. The eligibility requirements should be changed to 200 percent of the Federal Poverty Level, and any unspent ERPP funds should be made available for future ERPP expenditures to ensure these funds are used as they were intended and not for some other purpose.

O. True-up issues

Findings of Fact

255. KCPL has proposed two adjustments to its revenue requirement for events that occur outside of the true-up period in this case: 1) KCPL has proposed to remove two capacity agreements that expire on September 30, 2015; and 2) KCPL has included the potential cost increases for transmission expenses from Independence Power & Light's membership in SPP.³³⁵

256. In this case, the true-up period ended on May 31, 2015. A true-up is used to include the impacts of known and measurable material events that occur after the update period and that are much closer to when rates are going to be in effect to be reflected in the determination of rates.³³⁶ The term "known and measurable" relates to items or events affecting a utility's cost of service that must have been realized (known) and must be calculable with a high degree of accuracy (measurable).³³⁷

257. On April 13, 2015, SPP filed with the FERC, on behalf of the City of Independence, Missouri, revisions to its Open Access Transmission Tariff to implement the annual transmission revenue requirement for Independence Power & Light ("IPL") to be

³³⁵ Ex. 251, Featherstone True-Up Rebuttal, p. 3.

³³⁶ *Id.* at p. 5, 7.

³³⁷ Ex. 256, Lyons True-Up Rebuttal, p. 11.

included in KCPL's transmission pricing zone. On June 12, 2015, FERC approved those tariff revisions, subject to refund, with an effective date of June 1, 2015.³³⁸

258. FERC has not yet determined if SPP's tariff will result in just and reasonable rates, which further decision is subject to additional hearing and settlement procedures.³³⁹

259. KCPL has protested the FERC decision and continues to argue in the ongoing FERC proceeding that it should not be required to pay any increased net transmission expenses resulting from IPL's membership in SPP. KCPL intends to challenge the assignment of IPL's costs to KCPL up to and including a final non-reviewable FERC order.³⁴⁰

260. KCPL has made estimates of the impact of this FERC decision on its transmission revenues and expenses, but KCPL has not received an invoice from SPP with specific costs related to the addition of IPL in KCPL's SPP pricing zone and does not expect to receive such an invoice until at least September 2015.³⁴¹

261. KCPL has two capacity sales agreements with the Kansas Municipal Energy Agency ("KMEA") that will expire on September 30, 2015. By these agreements, KCPL agreed to provide energy service to KMEA on a firm capacity basis.³⁴²

262. The net impact on KCPL's cost of service from these two contracts is \$1.453 million (total company basis).³⁴³

Conclusions of Law and Decision

KCPL has proposed that the Commission should include in its revenue requirement costs incurred from IPL's membership in SPP and exclude revenues from KCPL's

³³⁸ *Id.* at p. 6.

³³⁹ *Id.*

³⁴⁰ Ex. 164, Ives True-Up Rebuttal, p. 8, 10.

³⁴¹ Ex. 256, Lyons True-Up Rebuttal, p.7; Transcript, Vol. 21, p. 2030-31.

³⁴² Ex. 251, Featherstone True-Up Rebuttal, p. 12.

³⁴³ Ex. 163, Crawford True-Up Rebuttal, p. 7.

agreements with the KMEA. For such true-up adjustments, those costs and revenues must be known and measurable. The IPL costs imposed on KCPL are not yet known and measurable because KCPL is continuing to fight those costs in FERC's ongoing proceedings, and FERC has not yet provided KCPL with an invoice that specifies any cost increases. The revenues that KCPL will lose at the expiration of the KMEA contracts on September 30, 2015, are known and measurable because as of May 31, 2015 it was known that the contracts will expire on September 30, and the amount of revenues lost is measurable with accuracy. The Commission concludes that any increased costs KCPL may incur related to IPL's membership in SPP should be excluded from the revenue requirement and that the revenues from the expiration of the KMEA contracts should also be excluded.

Decision Summary

In making this decision as described above, the Commission has considered the positions and arguments of all of the parties. Failure to specifically address a piece of evidence, position or argument of any party does not indicate that the Commission has failed to consider relevant evidence, but indicates rather that the material was not dispositive of this decision.

Additionally, KCPL provides safe and adequate service, and the Commission concludes, based upon its independent review of the whole record, that the rates approved as a result of this order support the provision of safe and adequate service. The revenue increase approved by the Commission is no more than what is sufficient to keep KCPL's utility plants in proper repair for effective public service and provide to KCPL's investors an opportunity to earn a reasonable return upon funds invested.

By statute, orders of the Commission become effective in thirty days, unless the Commission establishes a different effective date.³⁴⁴ In order that this case can proceed expeditiously, the Commission will make this order effective on September 15, 2015.

THE COMMISSION ORDERS THAT:

1. The Motion to Strike Pleadings, Reject Tariff Sheets, and Strike Testimony filed by Missouri Industrial Energy Consumers and the Office of the Public Counsel on June 10, 2015, is denied.

2. The tariff sheets submitted on October 30, 2014, by Kansas City Power & Company, assigned Tariff Nos. YE-2015-0194 and YE-2015-0195, are rejected.

3. Kansas City Power & Light Company is authorized to file tariff sheets sufficient to recover revenues approved in compliance with this order. Kansas City Power & Light Company shall file its compliance tariff sheets no later than September 8, 2015.

4. Kansas City Power & Light Company shall file the information required by Section 393.275.1, RSMo 2000, and Commission Rule 4 CSR 240-10.060 no later than September 8, 2015.

5. The Staff of the Missouri Public Service Commission shall file its recommendation concerning approval of Kansas City Power & Light Company's compliance tariff sheets no later than September 14, 2015.

6. Any other party wishing to respond or comment regarding Kansas City Power & Light Company's compliance tariff sheets shall file the response or comment no later than September 14, 2015.

³⁴⁴ Section 386.490.3, RSMo.

7. The *Non-Unanimous Stipulation and Agreement on Certain Issues* filed by some of the parties on June 16, 2015, is attached hereto as Attachment A and incorporated herein by reference.

8. Staff and Kansas City Power & Light Company's *Non-Unanimous Stipulation and Agreement Regarding Class Kilowatt-Hours, Revenues and Billing Determinants, and Rate Switcher Revenue Adjustments* filed on August 3, 2015, is attached hereto as Attachment B and incorporated herein by reference.

9. This Report and Order shall become effective on September 15, 2015, except that Ordered Paragraphs 3, 4, 5 and 6 shall become effective upon issuance.

BY THE COMMISSION



A handwritten signature in black ink that reads "Morris L. Woodruff".

Morris L. Woodruff
Secretary

Hall, Chm., Stoll, Kenney, and Rupp, CC., concur and certify compliance with the provisions of Section 536.080, RSMo. Coleman, C., abstains.

Dated at Jefferson City, Missouri,
on this 2nd day of September, 2015