BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

In The Matter Of The Construction Audit and Prudence Review Of Environmental Upgrades To Iatan 1 Generating Plant, and Iatan Common Plant, and the Iatan 2 Generating Plant, Including All Additions Necessary For These Facilities To Operate	)))))	File No. EO-2010-0259

REPLY BRIEF OF THE STAFF OF THE MISSOURI PUBLIC SERVICE COMMISSION

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Table Of Contents

I. KCPL/GMO Are Inappropriately Requesting That The Commission Make Ratemaking Decisions Outside The Context Of A Rate Case

At page 8 of their Initial Brief, KCPL/GMO admit that the Commission in the past has not made ratemaking decisions outside the context of a rate case:

> . . . the Commission Staff conducted its investigation and made its recommendations to the Commission in the context of those rate cases. And in those cases, the Commission made its determinations of prudence and determined the appropriate amount of investment that should be included in rate base within the context of those rate cases.

KCPL/GMO variously argue in their Initial Brief that the Commission should make ratemaking decisions in the context of the non-contested proceedings of the instant File No. EO-2010-0259:

> (1) The Companies are requesting that the Commission clarify that the prudence audit of the Staff has now ended, as of the filing of the December 31 Reports. (p. 4, first full paragraph, fourth sentence). . . . new prudence issues related to Iatan 1 and common plant may not be proposed by Staff in the upcoming rate cases. [p. 4, first full paragraph, last sentence].
>
> (2) The Commission should find that the prudence review of the Iatan 1 and Common Plant ended as of December 31, 2009, and no additional prudence disallowances should be permitted to be proposed by Staff in the upcoming KCP&L and GMO rate cases. [p. 34, second full paragraph, second sentence].
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> (3) . . . the Companies request that the Commission issue an order in this proceeding:
>
> > (1) clarifying the status of the Staff's audit and confirm that the Staff's prudence review of Iatan 1 and the common plant needed to operate Iatan 1 ended with the filing of the Staff's Reports on December 31, 2009; [p. 41, "Conclusion" section; *See also* p. 3, second paragraph, last sentence].
> >
> > (2) precluding Staff from proposing additional prudence disallowances in the next rate cases in addition to those eighteen (18) disallowances for KCP&L and twelve (12) disallowances for GMO that are already contained in its Staff's Report Regarding Construction Audit and Prudence Review of Environmental Upgrades to Iatan 1 and Iatan Common Plant filed in Case Nos. ER-2009-0089 and ER-2009-0090 on

December 31, 2009 ("December 31, 2009 Reports") [p. 41, "Conclusion" section; *See also* pp. 2-3, last paragraph bottom of page 2, first paragraph top of page 3].

(4) The Companies believe that the Commission should make the following findings based upon the evidence in the record:

a) The Companies have not engaged in any dilatory or unreasonable practices in responding to discovery during the construction audit and prudence review. [p. 3, "Relief Requested '2'" section].

b) The Companies' cost control system adequately tracks the costs of the projects, and is consistent with accepted industry standards. [p. 3, "Relief Requested '2'" section].

(5) The Companies' cost control system adequately tracks the costs of the projects, and is consistent with accepted industry standards. [p. 25, Heading "A.2."].

(6) As explained by Mr. Giles, KCP&L agreed in the Regulatory Plan Stipulation in Case No. EO-2005-0329 that the Company would develop and implement a cost control system that allowed the Company to identify "cost over-runs" above the definitive estimates and explain any cost increases above that estimate. [p. 26, first paragraph, second sentence].

(7) Based upon the competent and substantial evidence in the record, it is clear that KCP&L has developed a cost control system that adequately tracks the costs associated with Iatan 1 and 2, and is consistent with the best practices in the industry. [p. 28, third paragraph, first sentence].

(8) the Companies request that the Commission issue an order that finds:

(a) The Companies have not engaged in any dilatory or unreasonable practices in responding to discovery during the construction audit and prudence review; [p. 42, "Conclusion" section].

(b) The Companies' cost control system adequately tracks the costs of the projects, and is consistent with accepted industry standards; [p. 42, "Conclusion" section].

(9) The Companies have not engaged in any dilatory or unreasonable practices in responding to discovery during the construction audit and prudence review. [p. 18, Heading "A.1."].

(10) Based upon the competent and substantial evidence in the record, the Commission should find that KCP&L and GMO have acted lawfully with regard to discovery requests and have not engaged in any dilatory or unreasonable practices in responding to discovery during the prudence and construction audit. [pp. 24-25, last paragraph bottom of page 24, first paragraph top of page 25].

At pages 10-12 of their Initial Brief in their section entitled "Settlement Of The KCP&L And GMO Rate Cases" KCPL/GMO ignore the essential language in the applicable June 10, 2009 Commission Orders Approving Non-Unanimous Stipulations and Agreements And Authorizing Tariff Filings in Case No. ER-2009-0089 and Case No. ER-2009-0090 which clearly state that the Commission has approved in entirety the revenue requirement/global agreement Stipulation and Agreements. Instead, KCPL/GMO focus at pages 12-14 of their Initial Brief, in their section entitled "June 10th 2009 Order Regarding Joint Motion To Extend Filing Date," on the other June 10, 2009 Commission Orders keeping the June 19, 2009 date for the filing of a Staff prudence review/construction audit report, although changed to a preliminary report, and setting December 31, 2009 for the filing of the Staff's prudence review/construction audit report.

The ratemaking that KCPL/GMO are seeking is in direct conflict with the Western District Court of Appeal's holding in the first accounting authority ("AAO") decision, *State ex rel. Public Counsel v. Public Serv. Comm'n*, 858 S.W.2d 806 (Mo.App. W.D. 1993). In that case Public Counsel argued, among other things, that the Commission's approval of AAOs constituted single-issue ratemaking in violation of Section 393.270. The Commission did not grant rate relief to the Missouri Public Service division of UtiliCorp United, Inc. but determined that the costs of two construction projects were extraordinary and may be deferred. The Commission stated that "'[a]ll other issues would still remain, including, but not limited to, the prudency of any expenditures, the amount of recovery, if any, whether carrying costs should be

recovered, and if there are any offsets to recovery.'" *Id*. at 812. The amount of the deferred costs to be recovered and all other ratemaking issues, including prudency, were to be determined in a later rate case. *Id*.

The Western District Court of Appeals related that no Missouri court decisions have determined whether deferring extraordinary expenses constitutes single-issue ratemaking, but the Illinois Court of Appeals had considered the issue and found it not to constitute single-issue ratemaking:

> . . . In *Business & Professional People for the Pub. Interest v. Illinois Commerce Comm'n,* 205 Ill.App.3d 891, 150 Ill.Dec. 750, 563 N.E.2d 877 (1990), the court considered whether the order of the Illinois Commerce Commission (ICC) which granted Commonwealth Edison Company, an electrical power producing company, authority to adjust accounting procedures of financing costs and to defer depreciation at its nuclear power plant constituted illegal single-issue and retroactive ratemaking. *Id.* 150 Ill.Dec. at 753-54, 563 N.E.2d at 880-81. The court concluded that the ICC order affected account procedures, was not a ratemaking decision, and was legal. *Id.* 150 Ill.Dec. at 754, 563 N.E.2d at 881. The court recognized that the order did not foreclose any discussion or presentation of evidence that would normally occur when the ICC conducts the ratemaking hearing for the nuclear power plant. *Id.*

858 S.W.2d at 813. Contrary to order sought by Commonwealth Edison Company from the Illinois Commerce Commission, the Order being sought by KCPL/GMO from this Commission would foreclose discussion and the presentation of evidence that would normally occur when this Commission conducts the ratemaking hearing for Iatan 1 AQCS and Iatan 1 common plant. Also, unlike the situation in *State ex rel. AG Processing, Inc. v. Public Serv. Comm'n*, 120 S.W.3d 732 (Mo. Banc 2003)("*AG Processing*"), i.e., the merger of UtiliCorp United, Inc. ("UtiliCorp") and St. Joseph Light & Power Co. ("SJLP"), there is no matter pending before the Commission regarding KCPL's construction of Iatan 1 AQCS or Iatan 1 common plant or the Staff's prudence review/construction audit of same that is required by law to be addressed now by the Commission. In the *AG Processing* case, the Court held that the Commission by law had

to rule on the reasonableness of the SJLP acquisition premium to be incurred by UtiliCorp and whether the acquisition premium made the proposed merger detrimental to the public, if the acquisition premium were to be recovered from the ratepayers, rather than from the shareholders of UtiliCorp. *Id*. at 736.

The procedure adopted by the Commission for the hearings on April 28-29, 2010 was abbreviated compared to the procedures in a rate case. Although there was a hearing there was no prefiled direct, rebuttal and surrebuttal testimony as there would be in a rate case where ratemaking determinations are being made. KCPL/GMO never sought to treat the proceedings with the same formality as a rate case proceeding.

The Staff in its Initial Brief refers to KCPL, Public Counsel, and the Staff as parties in File No. EO-2010-0259. There is actually a question whether KCPL, Public Counsel, and the Staff in File No. EO-2010-0259 are participants rather than parties because File No. EO-2010-0259 is a non-contested case.

II. *State ex rel. Sierra Club and Concerned Citizens of Platte County v. Public Serv. Comm'n and Kansas City Power & Light Co.*, Cause No. SC88530, WD66893, 05ACCC00917 (2007)

The Staff believes that *State ex rel. Sierra Club v. Public Serv. Comm'n* offers a cautionary tale for the Commission regarding addressing substantive rights in a non-contested proceeding. *State ex rel. Sierra Club v. Public Serv. Comm'n* was the judicial review of the KCPL Experimental Alternative Regulatory Plan Stipulation And Agreement. KCPL ultimately executed a Collaborative Agreement[1] with Sierra Club/Concerned Citizens, resolving litigation,

[1] The Collaboration Agreement between KCPL, the Sierra Club, and the Concerned Citizens of Platte County, executed March 19, 2007, is Exhibit No. 2 (EFIS, Item No. 54, in Case No. EO-2007-0008) in the April 4, 2007 "hearing and question and answer session" held by the Commission regarding the Stipulation And Agreement in Case No. EO-2007-0008, In the Matter of the Resource Plan of Kansas City Power & Light Co. Pursuant to 4 CSR 240-22, Case No. EO-2007-0008.

after the Western District Court of Appeals reversed the Commission's approval of the Stipulation And Agreement constituting the KCPL Experimental Alternative Regulatory Plan. As part of the Collaborative Agreement between Sierra Club/Concerned Citizens and KCPL, Sierra Club/Concerned Citizens agreed to seek remand of their appeal, and if remand were denied, dismissal of their appeal. Sierra Club/Concerned Citizens also agreed that they would not, in any subsequent case, file any opposition to the Commission's approval of the KCPL Experimental Alternative Regulatory Plan.

In addition to dismissal of the appeal, KCPL and the Commission were interested in the Western District Court of Appeals vacating its decision reversing the Commission's approval of the KCPL Experimental Alternative Regulatory Plan. The Western District Court of Appeals denied KCPL's and Sierra Club/Concerned Citizens' request to dispose of the appeal and KCPL's and the Commission's Motions For Rehearing and Applications For Transfer to the Missouri Supreme Court.

The Statement Of Facts in the Notice Of Application For Transfer filed by the Commission in the Supreme Court Of Missouri in SC88530 (WD66893 / 05AC-CC00917) was as follows:

> On May 6, 2004, KCPL filed an Application to open an investigatory docket to provide notice and establish a workshop to address certain issues related to the future supply, delivery and pricing of electricity by KCPL to its customers. In particular, the workshop addressed the possible construction of Iatan generating unit 2, an 800-900 megawatt (MW), coal burning, baseload generating unit at the Iatan generating station near Weston, Missouri. The Commission created Case No. EO-2004-0577 to consider the application. The Commission issued a notice of the case and set an intervention deadline. Several entities filed to intervene.

Exhibit No. 1 (EFIS, Item No. 53, in Case No. EO-2007-0008) in the April 4, 2007 "hearing and question and answer session" held by the Commission regarding the Stipulation And Agreement in Case No. EO-2007-0008 is the Joint Motion To Dismiss Appeal filed by the Sierra Club, the Concerned Citizens of Platte County, and KCPL in the Western District Court of Appeals, Case No. WD66893, regarding the Sierra Club's and the Concerned Citizens of Platte County's review of the Commission's approval of the Stipulation And Agreement in Case No. EO-2005-0329.

The Commission established an investigatory workshop designated as EW-2004-0596. Case No. EO-2004-0577 was closed by the Commission.

The Commission's presiding officer, the regulatory law judge, advised the parties that an investigatory workshop is not a contested case, rather it is an information gathering and exchange proceeding in which there is participation and not intervention. Sierra Club and Concerned Citizens of Platte County (SC/CCPC) participated in EW-2004-0596 with many other entities. The Commission issued a Protective Order to facilitate discovery of "highly confidential information" from KCPL. Meetings and presentations were also held. One participant filed a Motion to Terminate the workshop proceeding prompting several other parties, including SC/CCPC, to seek a similar result. On February 18, 2005, the Commission closed Case No. EW-2004-0596 stating that if KCPL develops a regulatory plan for which it wants Commission approval, it can request approval in a new case.

On March 28, 2005, most participants to the EW-2004-0596 case filed a Stipulation and Agreement (S&A), which comprises KCPL's regulatory plan. The Commission established Case No. EO-2005-0329, a contested case, to consider KCPL's regulatory plan embodied in the S&A. The S&A reflects that KCPL would consider: The Empire District Electric Co. and Aquila, Inc., as potential partners of at least a 30% share of Iatan 2; the Missouri Joint Municipal Electric [Utility] Commission as a potential partner of at least 100 MWs of Iatan 2; and KCPL reserving the right to discuss with other entities potential participation in Iatan 2. SC/CCPC opposed the S&A and the case followed contested case procedures including the Commission issuing notice and setting an intervention deadline. The Commission held local public hearings in Kansas City and Platte City on May 24, 2005, and evidentiary hearings in Jefferson City on June 23-24, 27, and July 12, 2005, ultimately issuing a Report and Order approving the regulatory plan on July 28, 2005.

SC/CCPC filed a Petition for Writ of Review in the Cole County Circuit Court on September 22, 2005. The Court entered Judgment for the Commission and this appeal followed.

On February 27, 2007, the Court of Appeals concluded that the Commission was without jurisdiction to consider KCPL's regulatory plan because a contested case may not be initiated by a stipulation and agreement. On March 14, 2007, the Commission and KCPL filed Motions for Rehearing and Applications to Transfer. While the motions were pending, SC/CCPC and KCPL executed a Collaboration Agreement dated March 19, 2007, comprising a global settlement addressing this appeal and other litigation in State and Federal Courts and agencies. On April 3, 2007, while the Motions for Rehearing or Transfer were still pending, SC/CCPC and KCPL filed a Joint Motion to Dismiss the Appeal and withdraw the February 27, 2007 Opinion. The Commission filed a Notice that it did not oppose the dismissal and withdrawal of the opinion. On May 1, 2007, the Court of Appeals

denied the Joint Motion to Dismiss and overruled the Motions for Rehearing and Transfer.

On June 26, 2007, the Missouri Supreme Court granted transfer, thereby vacating and setting aside the decision of the Western District Court of Appeals which reversed the Commission's approval of the KCPL Experimental Alternative Regulatory Plan. On July 11, 2007 a Joint Motion To Dismiss And Suggestions In Support of KCPL, Sierra Club/Concerned Citizens, and the Commission was filed with the Missouri Supreme Court. On that very same day, the Court sustained the Joint Motion and closed the cause. The parties were advised of the Court's action by a letter from the Clerk of the Court, by the Deputy Clerk, Court en Banc, dated July 11, 2007.

In the vacated decision of the Western District Court of Appeals, the Court related that the Commission asserted that while there was no explicit statutory authority allowing a contested case to be initiated by the filing of a stipulation and agreement, such authority is implied. (Slip Opinion, p. 12). The Western District Court of Appeals held that "the procedures set forth in the statutes provide the mechanism for prosecuting substantive rights and must be followed, and the Commission is without statutory authority to initiate a contested case via the filing of the Stipulation and Agreement." (Slip Opinion, p. 14). The Court held that as a consequence, the Commission lacked jurisdiction to enter its Report And Order. (Slip Opinion, p. 6).

The Western District Court of appeals related in its vacated opinion that the Commission argued that any failure to comply with any statutory requirements was minimal and technical and the Commission cited Sections 386.410.1, 386.410.2, and 386.610 for the proposition that the Commission is not bound by the technical rules of evidence, no formality in any proceeding shall invalidate any order or decision of the Commission, substantial compliance with the provisions of this chapter shall be sufficient, and the provisions of this chapter shall be liberally construed.

The Court responded that: "As the Commission lacked authority to initiate a contested case through the filing of the Stipulation and Agreement, a contested case was never initiated. Thus, there was nothing to which these statutory provisions applied." (Slip Opinion, p. 15).

As the Commissioners are aware, a "contested case" is "a proceeding before an agency in which legal rights, duties or privileges of specific parties are required by law to be determined after hearing." Section 536.010(4) RSMo. Cum. Supp. 2009. The Western District Court of Appeals commenting on the hearing provided by the Commission significantly held in its vacated opinion: "Whether the hearing provided by the Commission was thorough and fair and whether the Commission's decision is supported by the evidence presented by the hearing is irrelevant. The nature of a subsequent hearing cannot serve to confer jurisdiction on the Commission." (Slip Opinion, p. 18).

III. KCPL's/GMO's Non-Response To Staff's Legal Arguments

KCPL/GMO, at hearing on April 28-29, 2010 and in its Initial Brief starting at the last paragraph on page 35, suggest that the Commission should ignore certain of the Staff's legal arguments because KCPL/GMO asserts that they are belatedly raised by the Staff. Significantly, on page 36 of KCPL's/GMO's Initial Brief, second paragraph, last two sentences, KCPL/GMO contend that the Commission should wait until some party other than the Staff raises the issues that the Staff has raised and the Commission should in essence decide the legal issues raised by the Staff on the basis that the Commission intended that the Staff's prudence audit be completed as of December 31, 2009.

The Commission should hear and seriously address these arguments now. Among the reasons that the Staff has raised them is that the Staff believes that if these arguments are raised by some entity before, for example, the Cole County Circuit Court and the Western District

Court of Appeals, these arguments will not be ignored by those Courts, and certainly not on the basis of at what point they were raised before the Commission by the Staff or some other entity.

The April 24, 2009 and May 22, 2009 revenue requirement/global agreement Stipulation And Agreements in Case No. ER-2009-0089 and Case No. ER-2009-0090, respectively, provided for the Staff continuing its Iatan 1 prudence review/construction audits into the Iatan 2 rate cases of KCPL and GMO, and on May 28, 2009 the Staff and KCPL/GMO jointly filed a motion requesting the Commission extend the deadline in the Commission's April 15, 2009 Order for the Staff filing its prudence review/construction audit of the environmental upgrades at Iatan 1, including all additions necessary for these facilities to operate, until the Staff filed its direct case in the next KCPL and GMO general rate cases. As late as KCP&L's And GMO's Initial Response To Staff Report Of The Construction Audit/Prudence Review Of Environmental Upgrades To Iatan 1 And Iatan Common Plant, filed by KCPL/GMO on February 16, 2010, KCPL/GMO were not requesting a two-day hearing: "Although the Companies strongly disagree with the substantive findings of the Construction Audit Report, those findings will be addressed through testimony in the Companies' next rate cases. . . . The construction audit and prudence review concerning Iatan 1 and common plant has been completed and should not be permitted to continue." It is only after the Commission scheduled a hearing on its own motion for April 6, 2010 that KCPL/GMO requested a two-day hearing.

The Commission should make note that KCPL/GMO have been subtly telling the Commission for some time that the Commission did not understand what it was doing if it was asking for a final construction audit report from the Staff on December 31, 2009. KCPL/GMO have been telling the Commission that the ratemaking audit / financial audit / construction audit of Iatan 1 can and should continue beyond December 31, 2009 since there are invoices

respecting Iatan 1 costs that could not be included in the Staff's December 31, 2009 Reports. In their Initial Brief at page 4, first full paragraph, fourth and sixth sentences, KCPL/GMO state:

> . . . The Companies are requesting that the Commission clarify that the prudence audit of the Staff has now ended, as of the filing of the December 31 Reports. . . . Other rate case issues (e.g. AFUDC calculations, allocation issues between Iatan I and Iatan 2, and construction audit issues) may be continued to be reviewed. (Tr. 150-51). . . .

The Staff's request is that the Commission leave open not only what KCPL/GMO are calling the ratemaking audit / financial audit / construction audit, but also what KCPL/GMO call the prudence review.

KCPL/GMO assert in the second paragraph on page 36 of their Initial Brief that the Staff's arguments about the voiding of the Stipulation And Agreements in Case No. EO-2005-0329, Case No. ER-2009-0089, and Case No. ER-2009-0090 are a "red herring." Based on the record in this proceeding, undersigned counsel assumes KCPL/GMO are referring to a seafood entre at The Capital Grille – Kansas City Country Club Plaza, which would require a good wine, such as a Layer Cake Cabernet Sauvignon, which does not overwhelm the red herrings' delicate scent, and that if such a lunch/dinner of red herring had been mistakenly charged by a KCPL individual to utility operating expense or the Iatan 2 project, it would be corrected by KCPL the very next day, after the Staff impudently brought the matter to KCPL's attention by the Staff addressing such an inconsequential matter with an excessive utilization of Commission resources and ratepayers' dollars.

IV. Iatan 1 Costs In 2010

Commissioner Kenney engaged KCPL/GMO witness Mr. Blanc in a colloquy that KCPL through December 31, 2009 had engaged in 92% of the actual expenditures for the Iatan 1

project and that was adequate for making all prudence determinations respecting the Iatan 1 project:

> [BY COMMISSIONER KENNEY] Q. I'm going to discuss the percentages that we were discussing before.
>
> [MR. BLANC] A. Okay.
>
> Q. And just with respect to the number that's in the blue shaded box, you said that's **8 percent of the overall project**?
>
> A. Correct.
>
> Q. So to put it conversely, 92 percent of the project is complete?
>
> A. I guess to try and put it as --
>
> Q. 92 percent of the expenses have been --
>
> A. That's exactly the distinction I was going to make. As of December 31st, 92 percent of the -- and these are actual costs, so costs would have been paid.
>
> Q. And there is a witness that will testify for KCP&L that at that stage, the 92 percent of these expenses that have been booked, that that is enough information to conclude or complete a prudence audit?
>
> A. Yes. That would be Dr. Kris Nielsen.

(Tr., Vol. 1, pp. 189-90).

Eight percent outstanding for the "half billion dollars" identified by Mr. Giles for Iatan 1 AQCS equals $40 million remaining for 2010. Highly Confidential KCPL/GMO Exhibit No. 1, Kansas City Power & Light Company, Strategic Infrastructure Investment Status Report, Fourth Quarter 2009, February 12, 2010, Case No. EO-2005-0329, KCP&L Strategic Infrastructure Initiatives - Quarterly Status Update indicates that the table/chart on page 41 for Iatan 1 shows actual expenditures for Iatan 1 through December 31, 2009. The number in the blue shaded box on page 41of Highly Confidential KCPL/GMO Exhibit No. 1 can basically be calculated from

what is in the public record because in addition to Mr. Giles' reference to Iatan 1 AQCS being a half billion dollar project, which is in the public record, KCPL's/GMO's Initial Brief states at the bottom of page 4 that "by September 2009 over 90% of the costs had been incurred and were able to be audited by the end of 2009 (Ex. 1, p. 41)."

The Commission should be clear regarding what KCPL/GMO are saying. KCPL/GMO are saying that the Commission should rule in the present proceeding that the Staff can make no prudence disallowance proposals regarding $40 million of Iatan 1 costs, based on KCPL's/GMO's definitions of prudence review and ratemaking audit / financial audit / construction audit.

V. Staff Has Not Asserted That It Was Unable To Complete Its Prudence Review/Construction Audit Because of KCPL's/GMO's Discovery Practices And Cost Control System

At page 18, first full paragraph, first sentence, KCPL/GMO contend that the Staff has "assert[ed] that it has been unable to complete its prudence review and construction audit because of the Company's discovery practices and cost control system . . ." The Staff has noted the problems that it has encountered with KCPL's discovery practices and cost control system, but the Staff has testified at hearing and related in its Initial Brief and this Reply Brief that it believes that it has complied with the Commission's Orders.

VI. Staff's Preliminary Report Filed On June 19, 2009 Accurately Indicated On June 19, 2009 The Nature Of The Staff Reports That The Staff Would File On December 31, 2009 – For Example, Staff Review Of KCPL Officer Expense Reports And Staff Review Not Limited To Invoices

Throughout KCPL's/GMO's Initial Brief, in citations to the transcript and in particular at page 7, first full paragraph, second sentence, KCPL/GMO seek to give the impression that the Staff's approach in its prudence review/construction audit, which resulted in the Staff Reports filed on December 31, 2009 in Case No. ER-2009-0089 and Case No. ER-2009-0090, were

revelations to KCPL/GMO. The Staff's approach was made clear in the June 19, 2009 Preliminary Report Of The Staff Respecting Its Construction Audit / Prudence Review Of Environmental Upgrades To Iatan 1 And Iatan Common Plant filed in Case No. ER-2009-0089 and Case No.ER-2009-0090. Any concerns regarding the Staff's approach could have been expressed well in advance of the Staff Reports filed on December 31, 2009. The December 31, 2009 Staff Reports in Case No. ER-2009-0089 and Case No. ER-2009-0090 track what the Staff indicated in its June 19, 2009 Preliminary Report that it would file on December 31, 2009.

At page 3 of the June 19, 2009 Preliminary Staff Report in Case Nos. ER-2009-0089 and ER-2009-0090 in the "Preliminary Analysis" section appear two tables identifying areas of Staff analysis. These areas of Staff analysis, including "AFDC on personal expenses of KCPL Executives" and "Excessive KCPL Executive's charges," are shown as follows in the tables in the Staff's June 19, 2009 Preliminary Report:

> The areas of analysis for Iatan 1 air quality control system (AQCS) are contained in the following table. . . .

Identification Number	Description	Dollar Amount
Iatan 1 #1	Edited Schiff Hardin Invoices remove all description of the work paid for	
Iatan 1 #2	AFUDC on costs recorded before invoice is received or paid	
Iatan 1 #3	AFDC on personal expenses of KCPL Executives	
Iatan 1 #4	Costs related to duplicate payments made to KCPL Executives for mileage for trips to Iatan site.	
Iatan 1 #5	Crane Incident	
Iatan 1 #6	Payment for vendor expenses not in compliance with KCPL policies	

> . . . Examples of common costs analysis are contained in the following table. . . .

Identification Number	Description	Dollar Amount

Iatan Common Plant #1	Edited Schiff Hardin Invoices remove all description of work being paid for	
Iatan Common Plant #2	Great Plains Power, a former KCPL affiliate, costs charged to common costs	
Iatan Common Plant #3	Excessive KCPL Executive's charges	

(EFIS, Item Nos. 29 and 32, Case No. EO-2010-0259, June 19, 2009 Staff Preliminary Report, p. 3). The "Audit Scope And Approach" section at pages 13-14 identifies as one of the examples of the specific audit activities that have been performed and will continue to be performed until the completion of the task is: "g. Review KCPL officer expense reports and evaluate the effectiveness of KCPL's officer expense report process internal controls."

The Staff explained at pages 3-4 of the June 19, 2009 Staff Preliminary Report that the Staff's review/audit was not limited to invoices:

> The Staff used its best efforts to comply with the literal interpretation of the Commission's order consistent with the realities of the task ordered by the Commission. In its current audit and review the Staff is examining the actual cost incurred for the Iatan 1 projects and the Iatan common plant projects and did not limit itself to only a review of construction invoices. Invoices do not represent the only type of costs included the amounts the utility seeks to recover from its customers. The Iatan 1 project costs included Allowance For Funds Used During Construction (AFUDC), Kansas City Power & Light Company (KCPL) also charges the project for its payroll and payroll benefits, employee expenses. These items reflect project costs not supported directly by an invoice. . . .

In addition, the Staff's Preliminary Report filed on June 19, 2009 relates on page 4: "The Engineering Staff of the Commission's Electric Department reviews project change orders to determine, in particular, if KCPL made prudent engineering decisions when significant changes are made to the Iatan 1 construction project. . . . To review the change orders and observe the construction process, the Engineering Staff of the Commission's Electric Department has made ten visits of one or two days to the Iatan project construction site."

KCPL/GMO did not complain to the Commission of the Staff's approach to the project until KCPL/GMO filed their March 22, 2010 Kansas City Power & Light Company's And GMO's (1) Response To Order Establishing Investigatory Docket And Setting On-The-Record Proceeding; And (2) Response To Staff Motion To Open Construction Audit And Prudence Review Investigation Case and their March 25, 2010 Kansas City Power & Light Company's And GMO's Response To Clarify Relief Being Requested From The On-The-Record Proceeding.

VII. KCPL's/GMO's Self-Serving Naming And Characterization Of "The Bucket Excuse" And The Incorrect Implication By KCPL/GMO That The Staff Does Not Intend To Properly Perform And Present A Prudence Review/Construction Audit Of Iatan 2 In The Context Of KCPL's And GMO's Impending Iatan 2 Rate Cases

At page 37 of KCPL's/GMO's Initial Brief, KCPL/GMO coins the phrase "The Bucket Excuse" and asserts:

> . . . Staff elaborated on another excuse during the on the record proceeding. Staff witness Schallenberg explained that he approached the prudence review as having different "buckets" and that a proper review would wait until all of the buckets were complete so that the Commission could see costs moving from bucket to bucket. (Tr. 482) Schallenberg did not explain why he did not bring this matter to the attention of the Commission any sooner. . . .

The Staff related in its Initial Brief that Mr. Schallenberg, in responding to Commissioner Davis at the on the record presentation on June 8, 2009 in Case Nos. ER-2009-0090 and HR-2009-0092, explained that even if the Commission ordered the Staff to perform a prudence review/construction audit of Iatan 1 AQCS by December 31, 2009 that prudence review/construction audit would not be complete even though Iatan I AQCS was fully operational and used for service. That situation does not prevent a less than truly "complete" prudence review/construction audit of Iatan 1 AQCS from being performed:

> [Mr. Schallenberg]: . . . In Iatan 1's case, Iatan 1 is interrelated with Iatan 2, and as we finish or as we finish Iatan 1, there's going to be an overlap between that

> and Iatan 2. There's going to be costs that should be in one or the other. And then we still have that common plant deal.
>
> So when you're saying Iatan 1, Iatan 1 will still have some overhang until Iatan 2 is finished, and I -- we're still talking to the company. We get those updates as to when Iatan 2 will be finished because that dictates when the next rate case will take place.
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> * * * *
>
> And I think we're looking at some schedules that go through the rest of this year of payments that are projected to be made that haven't been made. So the -- that is an issue as to what the construction audit at December 31st would address because it can only address what -- what has actually been paid because audits are done on what's paid, not what was projected.

(File No. EO-2010-0259, Tr. Vol. 1, pp. 59-61; Case Nos. ER-2009-0090 and HR-2009-0092, Tr. Vol. 12, pp. 180-82, June 8, 2009).

KCPL/GMO assert at pages 38-41 of their Initial Brief that the Commission should require the Staff to complete its prudence review of Iatan 2 and file any proposed prudence disallowance at the time the Staff files its direct testimony in the impending KCPL and GMO Iatan 2 rate cases. KCPL/GMO further request that the prudence issues should be ordered to be addressed in the main hearing of the impending KCPL and GMO Iatan 2 rate cases. (*See* last complete sentence at the bottom of page 40 of KCPL/GMO Initial Brief).

The Commissioners should take particular note of the next two sentences in KCPL's/GMO's Initial Brief at the bottom of page 40 and the top of page 41:

> . . . **The Commission should further order that the cut-off date for the construction (financial audit) of invoices should be four months prior to the true-up date of KCP&L and GMO's next rate case (in-service date of Iatan 2). Any additional invoices after that date would be subject to review in the next rate case.** . . .

(Emphasis added). In KCPL's/GMO's own idiom, they are saying that the "construction audit" cannot be completed in the context of the impending KCPL and GMO Iatan 2 rate cases.

KCPL/GMO are recommending that the construction audit be completed in the rate cases after the impending KCPL and GMO Iatan 2 rate cases.

In response to questions from Chairman Clayton, Mr. Schallenberg indicated that in the impending rate cases of KCPL and GMO the Commission can expect from the Staff analysis of most, but not all, of the costs of Iatan 2 because not all of the costs of Iatan 2 will be known:

> [CHAIRMAN CLAYTON] Q. . . . In the next rate case, should we anticipate that all Iatan 1 and 2 numbers will be completed and ready for analysis or be ready for a decision of whether they go into rate base, whether they're prudent or not?
>
> [MR. SCHALLENBERG] A. It would be -- when you say all, I am not sure -- well, I'm pretty confident not all of the Iatan 2 costs will be known at the time that we have a true-up or a cutoff for Iatan 2 given that at least all indications are we will still have Iatan 1 expenditures throughout 2010, but I will say that seems to be related to an auxiliary boiler, which right now I can tell you the Staff's position is that belongs in common and it shouldn't be in the Iatan 1 numbers anyway. So I can tell you we'll be making that adjustment as soon as those dollars start showing up. So I think Iatan 1 will be known, and if it's anything outstanding, it will not be big, in the next case. There probably will be a significant amount of expenditures still outstanding from Iatan 2 in the next case, and I think all the common costs will be -- well, by the way they're measured, the common cost estimates aren't actual dollars anyway, so the common cost numbers will be known in the next case. So there's three buckets at the Iatan project. So I would tell you Iatan 1, if anything is outstanding in the next case, it's going to be minor. Common, should be -- should be known. Maybe a little bit of an estimate if we're still doing any indirects from Iatan 2. And the Iatan 2 number will be the most significant amounts of outstanding expenditures.
>
> Q. Following the last rate case, the Commission issued an Order directing the Staff conduct a construction audit. From Staff's perspective, do you believe the Staff has complied with the Commission's Order that came after the rate case?
>
> A. Yes. But in your question you said they issued an Order after the case?
>
> Q. Was it after or during? I can't remember. I thought it was after the stip, but –

(Tr., Vol. 3, pp. 481-83).

* * * *

A. . . . I look at the order -- excuse me -- the construction audit prudence review was ordered on April 15th. The timetables for filing the results of that construction audit were modified on June 10th of 2009.

Q. So do you think Staff complied with that Order?

A. Yes, I do.

Q. Even though the report doesn't reach a conclusion, a full conclusion on the Iatan 1 upgrade?

A. I think it reaches a conclusion consistent with what the Commission requested us to do on April 15th.

Q. What in your -- what do you see the Commission asking to do on April 15th?

A. On April 15th, the Commission asked us to do construction audit/prudence review based on the information that the Staff had under its control on April 15th. At the same time, the Commission also ordered the company to provide the Staff invoices through a true-up date, I believe, of June 8th. So I -- I viewed that the Commission had ordered a prudence audit to be based on information that we had in our house under our control April 15th, 2009. And there is some debate. What I will say is I perceive that those invoices were also supposed to be used as a part to conduct that construction audit/prudence review through June 8th.

(Tr., Vol. 3, pp. 484-85).

VIII. KCPL's/GMO's List Of Comparison Cases Regarding "Prudence Reviews"

At page 8, first paragraph of KCPL's/GMO's Initial Brief, KCPL/GMO argue that respecting the Callaway, Wolf Creek and Grand Gulf nuclear power plants, the Staff conducted its prudence audits and made its recommendations to the Commission within the context of the rate case in which each of the plants was included in rates. The Staff will not repeat the procedural explanation it has provided regarding the Wolf Creek case in the Staff's Initial Brief. However, contrary to KCPL's/GMO's citation to the Arkansas Power & Light Company ("APL") Grand Gulf nuclear generating station, that case does not support KCPL's/GMO's

position. *Re Arkansas Power & Light Co.*, Case No. ER-85-265, Report And Order, 28 Mo.P.S.C.(N.S.) 435 (1986).

APL was an investor-owned Arkansas corporation engaged in the generation, transmission, and distribution of electric energy in Arkansas and previously in southeastern Missouri, until it sold its operations to Union Electric Company. APL was a wholly owned subsidiary of Middle South Utilities, Inc. (now Entergy Corporation), a public utility holding company, registered under the Public Utility Holding Company Act of 1935. The section of the Commission's 1986 Report And Order that KCPL/GMO cite in footnote 7 at page 8 of their Initial Brief is the "Excess Capacity" issue. Excess Capacity is the principal "decisional analysis" / "prudence" issue that the non-utility Signatory Parties to the Case No. EO-2005-0329 KCPL Experimental Alternative Regulatory Plan Stipulation And Agreement agreed they would not raise so long as certain conditions were met. The Case No. EO-2005-0329 KCPL Experimental Alternative Regulatory Plan Stipulation and Agreement addresses decisional analysis as indicated below at pages 31, 36, 39, and 42-43. Although it would appear that KCPL/GMO would assert that the Commission should only be concerned about the second sentence in each paragraph below, and actually not even then, if some Case No. EO-2005-0329 non-utility Signatory Party raises the matter in the future. The Staff suggests that the Commission that should take note of the second sentence in each subsection below in respect to a possible voiding of the Case No. EO-2005-0329 Stipulation And Agreement:

> **III.B.3.a. Rate Filing # 1 (2006 Rate Case)**
>
> *** * * ***
>
> (v) Infrastructure. . . . The Signatory Parties agree that they will not take the position that these investments should be excluded from KCPL's rate base on the ground that the projects were not necessary or timely, or that alternative technologies or fuels should have been used by KCPL, so long as KCPL proceeds to implement the Resource Plan described herein (or a modified version of the Resource Plan where the modified plan has been approved by the

Commission) and KCPL is in compliance with Paragraph III.B.1(o) "Resource Plan Monitoring." Nothing in this Agreement shall be construed to limit any of the Signatory Parties' ability to inquire regarding the prudence of KCPL's expenditures, or to assert that the appropriate amount to include in KCPL's rate base or its cost of service for these investments is a different amount (e.g., due to imprudent project management) than that proposed by KCPL.

* * * *

III.B.3.b. Rate Filing # 2 (2007 Rate Case)

*** * * ***

(v) Infrastructure. . . . The Signatory Parties agree that they will not take the position that these investments should be excluded from KCPL's rate base on the ground that the projects were not necessary or timely, or that alternative technologies or fuels should have been used by KCPL, so long as KCPL proceeds to implement the Resource Plan described herein (or a modified version of the Resource Plan where the modified plan has been approved by the Commission) and KCPL is in compliance with Paragraph III.B.1(o) "Resource Plan Monitoring." Nothing in this Agreement shall be construed to limit any of the Signatory Parties' ability to inquire regarding the prudence of KCPL's expenditures, or to assert that the appropriate amount to include in KCPL's rate base or its cost of service for these investments is a different amount (e.g., due to imprudent project management) than that proposed by KCPL.

* * * *

III.B.3.c. Rate Filing #3 (2008 Rate Case)

*** * * ***

(v) Infrastructure. . . . The Signatory Parties agree that they will not take the position that these investments should be excluded from KCPL's rate base on the ground that the projects were not necessary or timely, or that alternative technologies or fuels should have been used by KCPL, so long as KCPL proceeds to implement the Resource Plan described herein (or a modified version of the Resource Plan where the modified plan has been approved by the Commission) and KCPL is in compliance with Paragraph III.B.1(o) "Resource Plan Monitoring." Nothing in this Agreement shall be construed to limit any of the Signatory Parties' ability to inquire regarding the prudence of KCPL's expenditures, or to assert that the appropriate amount to include in KCPL's rate base or its cost of service for these investments is a different amount (e.g., due to imprudent project management) than that proposed by KCPL.

* * * *

III.B.3.d. Rate Filing # 4 (2009 Rate Case)

*** * * ***

(v) Infrastructure. . . . The Signatory Parties agree that they will not take the position that these investments should be excluded from KCPL's rate base on the ground that the projects were not necessary or timely, or that alternative technologies or fuels should have been used by KCPL, so long as KCPL proceeds to implement the Resource Plan described herein (or a modified version of the Resource Plan where the modified plan has been approved by the Commission) and KCPL is in compliance with Paragraph III.B.1(o) "Resource

> Plan Monitoring." Nothing in this Agreement shall be construed to limit any of the Signatory Parties' ability to inquire regarding the prudence of KCPL's expenditures, or to assert that the appropriate amount to include in KCPL's rate base or its cost of service for these investments is a different amount (e.g., due to imprudent project management) than that proposed by KCPL.

(Case No. EO-2005-0329, KCPL Experimental Alternative Regulatory Plan Stipulation And Agreement).

The Staff made note of the particular sentence quoted above, in paragraph 21, page 15 of its March 29, 2010 filing with the Commission in File No. EO-2010-0259 entitled Staff's Reply To Kansas City Power & Light Company's And KCP&L GMO's March 22, 2010 Response to Staff And Kansas City Power & Light Company's And KCP&L GMO's Response To Commission's March 24, 2010 Agenda Session.

The "prudence" issues at issue in File No. EO-2010-0259 and at issue in the Wolf Creek and Callaway cases[2] were not the prudence issues at issue in the Grand Gulf case cited by KCPL/GMO in its Initial Brief. A perusal of the Commission's May 4, 1986 Report And Order in Case No. ER-85-265 reveals that the Staff did not perform a similar type of prudence review / construction audit in Case No. ER-85-265, and how very different the Commission's "regulation" of the Grand Gulf costs were because of the Middle South System:

> Company seeks inclusion in its rates of the costs assessed by FERC Opinion No. 234 issued on June 13, 1985, which allocated 36 percent of the power and associated costs of a nuclear generating station known as Grand Gulf Unit No. 1 to the Company. The Commission Staff, Public Counsel, and intervenors, propose a disallowance of those costs.

28 Mo.P.S.C.(N.S.) at 473-74.

* * * *

> . . . The ultimate agreement of significance was a Reallocation Agreement executed on July 28, 1981, by Company and the other operating companies of MSU. Under that agreement APL was to take no power from either of the Grand

[2] *Re Kansas City Power & Light Co.*, Case Nos. EO-85-185 and EO-85-224, *Report And Order*, 28 Mo.P.S.C.(N.S.) 228 (1986)(Wolf Creek *Report And Order*) and *Re Union Electric Company*, Case Nos. EO-85-17 and ER-85-160, *Report And Order*, 27 Mo.P.S.C.(N.S.) 183 (1985)(Callaway *Report and Order*).

> Gulf units, with the three other operating companies taking all of the power in varying percentages.
>
> The FERC Opinion No. 234 rejected the agreement of the operating companies and allocated 36 percent of the power and associated costs of Grand Gulf to the Company. . . . On February 4, 1986, the Company filed an action in the United States District Court for the Western District of Missouri, Central Division, in response to this Commission's denial of the Grand Gulf costs on an interim basis in Case No. ER-85-265. The Commission was ordered to allow the Grand Gulf costs on an interim basis in Arkansas Power & Light Company v. Missouri Public Service Commission, Docket No. 86-4067-CV-C-5 (March 10, 1986). Grand Gulf costs included in rates for the Missouri portion of the Company's service area are presently $10,598,000 annually, subject to refund. Because of the manner in which we have disposed of the allocation issues in this case, the Grand Gulf costs at issue are $9,033,000 on an annual basis.

Id. at 474.

* * * *

> The Grand Gulf costs at issue in the permanent case are the same costs at issue in the interim case. By subsequent order issued in Cause No. 86-4067-CV-C-5, the United States District Court for the Western District of Missouri modified its Order, but only to the extent of stating that it was not determining the Missouri portion of the Grand Gulf costs being incurred or the procedure by which the costs should be recovered. We are actively pursuing reversal of Order No. 234 as well as District Court Order in Docket No. 86-4067-CV-C-5. Absent those reversals, we are of the opinion we must pass through the Grand Gulf costs.

Id. at 477.

In the second paragraph on page 8 of their Initial Brief and in opening statement on April 28, 2010, KCPL/GMO specifically identified a number of generating units for which KCPL/GMO assert that the Staff conducted its prudence investigation and made its recommendation in the associated rate cases and the Commission made determinations of prudence and the appropriate amount of investment that should be included in rates. Only one of the cases cited by KCPL/GMO involved the environmental enhancement of an existing generating unit. Also a Staff witness disputed the accuracy of the inclusion of one of the units in the list by KCPL/GMO, i.e., Empire's State Line Combined Cycle Plant. Staff Auditor Cary Featherstone testified that he and another accountant were the principal Staff witnesses

addressing prudency in the Empire rate case regarding the State Line Combined Cycle Plant and not all of the costs of that unit could be audited for inclusion for consideration in the rate case after that unit was first fully operational and used for service. (Tr., Vol. 1, p. 111-12). Furthermore, KCPL/GMO did not make note of the rebuild of the Hawthorn 5 baseload generating unit after the catastrophic boiler explosion which destroyed that unit in 1999. Mr. Featherstone testified that the Staff did not complete its prudence review/construction audit until the next rate case after the 2006 rate case in which the rebuilt Hawthorn 5 was fully operational and used for service and was placed in rate base. (Tr., Vol. 1, p. 112-13).

IX. The Yellow Book - Generally Accepted Government Auditing Standards ("GAGAS")

At page 33 of KCPL's/GMO's Initial Brief, KCPL/GMO assert that the appropriate standards for prudence audits is prescribed by the Comptroller General of the United States, United States Government Accountability Office, Government Auditing Standards, July 2007 Revision – GAO-07-731G (a/k/a the "Yellow Book"). Dr. Nielsen testified that the term Generally Accepted Government Auditing Standards, abbreviated "GAGAS," is generally referred to as the "Yellow Book." (Tr., Vol. 1, p. 249). The Missouri Public Service Commission has adopted the FERC Uniform System of Accounts ("USOA"), 4 CSR 240-20.030, for recordkeeping purposes, but not for ratemaking purposes - 4 CSR 240-20.030(4). The Missouri Public Service Commission has not adopted the Yellow Book. The Yellow Book was not a factor in either the Callaway prudence review/construction audit case, *Re Union Electric Co.*, Report And Order, Case Nos. EO-85-17 and EO-85-160, 27 Mo.P.S.C.(N.S.) 183 (1985) or the Wolf Creek prudence review/construction audit case, *Re Kansas City Power & Light Co.*, Report And Order, Case Nos. EO-85-185 and EO-85-224, 28 Mo.P.S.C.(N.S.) 228 (1986).

Mr. Giles related that he had been employed by KCPL for 34 years before he retired in June 2009. His last position was Vice President of Regulatory Affairs. He said that as Vice President of Regulatory Affairs he was involved in all aspects of regulatory work, revenue requirement, rate cases, cost of service, and the KCPL Experimental Alternative Regulatory Plan. (Tr., Vol. 1, pp. 268-69). He testified that he had never performed a prudence review nor a construction audit, he did not know what the term GAGAS was or how it is used, he did not know whether any of the prudence reviews that he had been involved in used the Yellow Book, and he did not know whether KCPL internal audits followed the Yellow Book:

> [MR. HATFIELD] Q. Now, have you previously been involved in either construction audits or prudence reviews?
>
> [MR. GILES] A. I have, as I indicated, been employed by KCP&L since 1975. During that timeframe, I have not conducted a prudence review. I have been involved in them with the LaCygne 2 coal generation unit, Iatan 1 initial construction, which was in service in 1980, Wolf Creek 1986, the rebuild of Hawthorn 5, and various other rate cases and plant expansions during that timeframe.

(Tr. Vol., p. 269).

> [MR. DOTTHEIM] Q. Earlier this evening you indicated that you have not performed a prudence audit, I believe. Did I hear that correctly?
>
> [MR. GILES] A. Yes.
>
> Q. You haven't performed a construction audit, have you?
>
> A. I have not performed a construction or a prudence review. I must say, the difference between this project and the ones I referred to earlier, the LaCygne 2, Iatan 1 and Wolf Creek –
>
> Q. Was the answer to my question no?
>
> A. It was no, yes.
>
> Q. Okay. Thank you. Do you know whether the prudence reviews that you were involved with followed GAGAS?

A. I don't have any idea what the term is and how it's used.

Q. Were you here -- well, do you know whether the prudence reviews that you were involved with followed the Yellow Book?

A. I don't know.

(Tr. Vol. 1, pp. 293-94).

[MR. DOTTHEIM] Q. . . . Mr. Giles, can you identify who is Maria Jinks?

[MR. GILES] A. Maria Jinks was the -- I don't recall what her title is, but basically Maria Jinks was the head of internal audit for Kansas City Power & Light. She is no longer in that position, but that's what her previous job was. She is now head of procurement.

Q. Okay. So if I understand correctly, she had a role in relation to the audit reports that are Staff Exhibits 5 through 8?

A. Yes.

Q. Okay. Staff met with Maria Jinks regarding the audit reports, did they not?

A. I don't know. I would assume they did, but I wasn't in those meetings.

Q. Do you know whether the KCPL audit reports followed the Yellow Book?

A. I don't know.

(Tr., Vol. 1, pp. 294-95).

X. $405 Lunch/Dinner – Significant Issue – Why?

KCPL/GMO in its Initial Brief at pages 22-23 takes the Staff to task for its concern respecting a $405 lunch/dinner charged to the Iatan construction project. The Staff's Data Request No. 270.3 was submitted on February 8, 2009. KCPL responded over three months later, on May 12, 2009, after first objecting to the Staff Data Request on the basis that cost was being charged to Iatan 2, not Iatan 1 AQCS or Iatan common plant (EFIS, Item No. 30, File No.

EO-2010-0259, Staff Report December 31, 2009 In Case No. ER-2009-0089, p. 80; EFIS, Item No. 33, File No. EO-2010-0259, Staff Report December 31, 2009 In Case No. ER-2009-0090, p. 74):

> Staff Data Request No. 270.3:
>
> Question:
> Please provide the receipts for Mr. William H Downey's local business meal at the Capital Grill of $405.26 on February 13, 2007.
>
> Response: [Objection]
>
> 02/11/09 Because KCPL has not included this amount in its cost of service and therefore is not seeking to recover this amount from ratepayers, KCPL objects to this data request as it calls for information which is irrelevant, immaterial and inadmissible and whose discovery is not reasonably calculated to lead to the production of relevant and admissible evidence.
>
> Response: [5/12/09]
>
> Attached please find the requested receipt for Mr. Downey's February 13, 2007 local business meal. The expense report indicates that the expense was for lunch. As indicated on the receipt, however, it was for dinner. In addition, the amount was inadvertently billed to the Iatan construction project. However, once the meal expense was identified, the Company immediately withdrew it from the case. Supporting documentation demonstrating its removal from the Iatan construction project and the related credit to the joint owners is also attached. In addition, Mr. Downey personally reimbursed the Company for the expense. A copy of that check and confirmation that it was deposited in the Company's accounts is included in the reimbursement documentation.

KCPL's desire to be precise that the $405 expense was actually for dinner, and not for lunch, may be because a portion of the charges were for spirits. (Staff Ex. 1, KCPL Response to Staff DR No. 270.3HC).

KCPL sought to make Staff's attention to the $405 Downey/Roberts lunch/dinner and Staff's pursuit of the records relating to the $405 Downey/Roberts lunch/dinner some sort of ignominy on the part of the Staff. As indicated by the data request response, KCPL was personally reimbursed the day after the Staff Data Request was submitted but the records were

not submitted to the Staff until over 90 days later. On cross-examination Staff auditor Hyneman responded to counsel for KCPL that Staff was not dissuaded by KCPL's effort to put off the Staff in the then pending KCPL rate case, Case No. ER-2009-0089, by KCPL's assertion that KCPL was not seeking recovery of the expense in the rate case for the charge was made to the Iatan 2 construction project, not the pending KCPL rate case, Case No. ER-2009-0089. Mr. Hyneman explained that the Staff's interest became that the $405 Downey/Roberts lunch/dinner charge was made to Iatan 2, but a piece of which is attributable to common plant, which is assigned to Iatan 1. Mr. Hyneman further testified that Staff's concern is that this item may be indicative of a tone that is being set and a breakdown of internal controls, which requires auditors to perform additional work to attempt to determine whether there are other instances of this tone and lack of internal control, or something even more pervasive:

> [MS. VAN GELDER] Q. Okay. We've dealt with this for so many times here, but let's go with it. During the rate case audit this Staff found a $405 lunch. Why in December after this is -- in a prudence audit, in a construction audit, a prudence review, why are we still talking about a charge in the rate audit?
>
> [MR. HYNEMAN] A. First of all, it was not a charge in the rate audit. That charge was made to Iatan 2, which a piece of that cost goes into the common plant, which is assigned to Iatan 1.
>
> Q. Right.
>
> A. So that's the reason why we pursued it in the construction audit, and when we pursued it, KCPL said, well, this charge, we're not seeking recovery of that charge. Well, we're understanding that's a false statement because they're seeking recovery of that common plant in that rate case. Now, we came to find out subsequently that the individual reimbursed KCPL for that charge, and then that may be the basis of why they said they're not seeking recovery, but KCPL refused to provide that information for us for I think three months, and we had to fight and fight and fight just to get an understanding of what they were doing on that.
>
> Q. So you had a three-month fight –
>
> A. Right.

Q. -- to get receipts for a $405 lunch, correct?

A. Yes.

* * * *

BY MS. VAN GELDER: Q. So let's go this way. I think we can do that. So you spent three months to get information for a $405 lunch, of which 21 percent of the lunch charge is going to be charged to the Iatan project common plant?

[MR. HYNEMAN] A. The dollar amount is not important to me. What is important to me is what taking that action -- and it's just not a simple mistake as KCPL characterizes it. For that charge –

Q. It's not a simple mistake as KCPL characterized it?

A. Correct.

Q. So you don't believe their answer?

A. They may believe it's a mistake, but here's what has to happen for that mistake to take place: This individual has to incur that meal, that charge, and I don't want to get into the specifics about it, but take that receipt, fill out an expense report, charge that cost to Iatan 2, submit that expense report, get that expense report approved by the CEO of the company and get reimbursed for that expense. That to me is not a definition of a mistake. That's an intentional action.

Q. It's a conspiracy.

A. It's an intentional action which raises questions in the mind of an auditor, who can't dismiss it as a simple mistake. And what does, because of the individual who took that action, they set the tone at KCPL. It's the tone at the top, and when you have a tone and a breakdown of internal controls, that creates a lot of work on the auditors where it increases the amount of work they have to do to make sure that that lack of internal control is not pervasive throughout the company. So that is why that charge is very important to us.

Q. Okay. When we talked, you could not tell me with any certainty that that charge was actually coded and imported by the officer that you're saying made the intentional act to put in a personal expense?

A. I know he put it on his expense report, he charged it to Iatan 2, he signed it, he had his CEO sign it and he recovered the fund.

Q. And you're saying on expense account he said Iatan 2?

A. Yes. I have a copy if you'd like to see it.

Q. Yes.

A. Here I've highlighted for you.

Q. All right.

A. And it goes down and it filters in to here, which is 520123, which is the Iatan 2 project.

Q. Now, we've got some markings in here, and it was signed, but I asked you before and I'm going to ask you again, how do you know his secretary didn't fill this out?

A. She very -- or he may have, but I don't know how she would get the receipts without him giving it to her.

Q. Getting a receipt and coding it to the wrong project are two different things, aren't they?

A. Well, he signed a document.

Q. He did. He did. And yes, you are, you're assuming that he signed a document and he read the document when his secretary gave him that, but you're also assuming that he intentionally tried to game the rate-holders.

A. No, I'm not. I don't know if it was a mistake on his part. What I'm saying is there's a breakdown of internal control to let that cost be charged to the company and Missouri ratepayers. Whether he did it a mistake or not, that may be. The lack of internal control or the breakdown of internal control is what is important to me in the scope of this audit.

(Tr., Vol. 3, pp. 662-66; *See* EFIS, Item No. 30, File No. EO-2010-0259, Staff Report December 31, 2009 In Case No. ER-2009-0089, pp. 79-83; EFIS, Item No. 33, File No. EO-2010-0259, Staff Report December 31, 2009 In Case No. ER-2009-0090, p. 73-76).

XI. KCPL's/GMO's Issue Respecting Staff's "Funeral" Data Request

At page 31 of their Initial Brief, KCPL/GMO state:

. . . In one request, the Staff even questioned whether the trip of Mr. Churchman, KCP&L Vice-President of Construction, to the funeral of the gentleman that died in the crane accident should be considered as a personal or a business-related trip. (DR No. 780)

Counsel for KCPL/GMO utilized the above sentence almost verbatim in an apparent feigned tearful voice in his opening statement for KCPL/GMO on April 28, 2010. This mischaracterization of Staff Data Request No. 780 is indicative of how KCPL/GMO have attempted to tar the Staff's audit with unwarranted accusations and innuendos. KCPL/GMO in its opening statement and Initial Brief have only noted the second sentence of Staff Data Request No. 780. The first sentence of Staff Data Request No. 780 identifies that KCPL/GMO mistakenly booked the expense for this trip to Iatan 2 rather than to Iatan 1. The first sentence of Staff Data Request No. 780 states as follows: "Please provide the rationale for charging Iatan 2 for a portion of Mr. Churchman's 5/29/08 business mileage to Chillicothe, Mo on his 9/18/08 Expense Report to attend funeral of crane incident victim." (EFIS, Item No. 44, KCPL/GMO March 22, 2010 Filing in Case No. ER-2010-0259, Attachment 2, p. 12). The KCPL/GMO response to Staff Data Request No. 780 is as follows:

> Since the mileage expense was incurred as a result of the crane incident KCP&L will create a journal entry to transfer the expense from Iatan 2 to Iatan 1.
>
> Mr. Churchman attended the funeral as a representative of KCP&L.

The basis for the Staff's second question, the only Staff question which KCPL/GMO made note of, was to verify that the expense was being charged to the Iatan project.

XII. KCPL's Invitation To Staff To Participate In Reforecast Of Iatan Project Cost And Schedule

KCPL/GMO state at page 28 of their Initial Brief that "Staff was also invited to observe the actual development of the re-forecasted budget estimate in an effort to be transparent, but Staff declined to **participate** with Company personnel in the reforecast process" (Emphasis added):

> [MR. HATFIELD] Q. And so I think we finished this story, but did they ever participate, did the Staff ever **participate** in the reforecast process?

[MR. GILES] A. No.

(Tr. Vol. 1, p. 283; Emphasis added). In fact, Mr. Giles thought it was noteworthy that Mr. Wess Henderson and perhaps even Mr. Dottheim contacted him after the offer was made by KCPL/GMO. (Tr. Vol. 1, p. 281). Staff counsel cross-examined Mr. Giles on this matter but Mr. Giles' recollection on this matter as on other matters about which Staff counsel asked him was not good:

> [MR. DOTTHEIM] Q. Okay. Mr. Giles, do you know whether Mr. Downey contacted Wes Henderson about Staff **participation** in the reforecast that occurred in 2008?
>
> [MR. GILES] A. I don't know if he did or not. He may have. He and I were in discussions. We were both -- in other words, it was a mutual agreement between Mr. Downey and myself that we should offer this. So he very well could have called Mr. Henderson.
>
> Q. Did the KCC staff **participate** in the Iatan 1 reforecast in 2008?
>
> A. No. We did not offer.

(Tr., Vol. 1, pp. 295-96; Emphasis added).

The KCPL/GMO choice of the word "**participate**" should not go unnoticed and will not go uncommented on by the Staff. The Utility Services Division of the Staff of the Commission is ever attuned to concerns of the appearance of cooptation, let alone attuned to concerns of actual cooptation. For this reason, among others, the Utility Services Division of the Staff of the Commission utilizes data requests to obtain information from KCPL/GMO rather than proceeding informally.

KCPL's/GMO's Initial Brief at page 28 identifies Forrest Archibald as KCPL's "cost control manager." KCPL did not present any testimony of Mr. Archibald. Instead it presented the review of Dr. Nielsen. KCPL's/GMO's Initial Brief at page 28 states that "[i]f the [Staff's]

criticism [of the KCPL cost tracking system] had been raised earlier, Mr. Giles testified that he would have 'insisted that the Staff spend enough time with our cost control manager, Forest Archibald, to walk through however many examples were required to give them the ability to track the costs. We did that with Dr. Nielsen and we did that with the Kansas Staff.'" Staff counsel asked Mr. Giles at the April 28, 2010 hearing, whether he recalled that Mr. Archibald made a presentation to the Staff a year earlier, and he responded that he did not recall the date or number of presentations:

> [MR. DOTTHEIM] Q. Mr. Giles, are you aware that Forrest Archibald and his Staff made a presentation to the Missouri Staff or members of the Missouri Staff on April 28th, 2009?
>
> [MR. GILES] A. I know Mr. Archibald made presentations to Staff. I'm not sure of the date. There may have been more than one.

(Tr. Vol. 1, p. 295).

XIII. $733 Million Project, A Half A Billion Dollar Investment, $484 Million – Is There A Relevant Or Correct Number For Iatan 1 AQCS And Iatan 1 Common Plant?

After reading KCPL's/GMO's Initial Brief, the Staff believes that it would be beneficial if the Staff sorted through the numbers that have been bandied about in the record.

At page 23 of KCPL's/GMO's Initial Brief appears the statement "[m]ore specifically, it is particularly difficult to understand how a $405 receipt for any expenditure would be considered essential to completing the prudence review and construction audit of a $733 million project." The Case No. ER-2009-0089 revenue requirement/global agreement Stipulation And Agreement reads in part at page 4, paragraph "5. Prudence and In-Service Timing of Iatan 1": "KCP&L represents that Iatan 1 and Iatan common costs will not exceed $733 million on a total project basis." The Case No. ER-2009-0090 revenue requirement/global agreement Stipulation And Agreement reads in part at page 3, paragraph "5. Prudence and In-Service Timing of Iatan

1": "GMO acknowledges Kansas City Power & Light Company has represented that Iatan 1 and Iatan common costs will not exceed $733 million on a total project basis."

Mr. Giles in testimony at hearing on April 28, 2010 referred to "a half billion dollar investment":

> [MR. GILES] . . . Rather than first focussing on prudence and large contracts and a **half a billion dollar investment**, Staff has spent an unusual amount of time tracking mileage, tracking expense reports.

(Tr., Vol. 3, p. 302).

Mr. Rush identified $353 million as the initial quantification of the cost of the Iatan 1 AQCS, and $484 million as the quantification of the cost of Iatan 1 AQCS announced in May 2008 as the result of the 2008 reforecast of the cost of Iatan 1 AQCS, which process was addressed and number was treated as Highly Confidential in the April 2008 hearings in Case No. EM-2007-0374. (*See* July 1, 2008, Report And Order in Case No. EM-2008-0374; Tr., Vol. 3, pp. 412-13, 421). Mr. Rush related that of the $484 million, $370 million is Iatan 1 AQCS, and $114 million is Iatan 1 common plant. (Tr., Vol. 3, p. 415). He further stated that Iatan 1 and Iatan 2 common plant combined amounted to $363 million. Thus, he explained that the $733 million number is the $370 million Iatan 1 AQCS plus the $363 million Iatan 1 and Iatan 2 common plant combined. (Tr., Vol. 3, p. 416). These numbers reflect total project. To derive the Missouri jurisdictional numbers for Iatan 1, Mr. Rush testified that the numbers are multiplied by 70% to get KCPL's Iatan share and then multiplied by approximately 55% to allocate to the Missouri retail jurisdiction. (Tr., Vol. 3, p. 418).

Mr. Giles was also asked about these numbers and provided testimony, but he indicated that since he had retired Mr. Rush was a good person for questions about these numbers to be

directed to. (Tr., Vol., 1, pp. 310-12, 313, 348-49). Mr. Giles indicated that these numbers did not include AFUDC. (Tr., Vol., 1, p. 348).

There is a discussion, including costs and facilities, among other things, of common plant needed to operate Iatan 1, which includes both Iatan 1 common plant and Iatan 2 common plant, in the December 31, 2009 Staff Reports, beginning on page 12 in both the Staff Report for Case No. ER-2009-0089 (KCPL) and the Staff Report for Case No. ER-2009-0090 (GMO).

XIV. The Empire District Electric Company Procedural Schedule Settlement In Case No. ER-2010-0130 Respecting Iatan 1 AQCS and Iatan 1 Common Plant

At page 39 of their Initial Brief, KCPL/GMO relate that "Mr. Michael Cline, KCPL's Vice-President of Investor Relations and Treasurer, testified about the expected adverse reactions of investors to the uncertainty surrounding a failure to resolve the Iatan 1 and common plant prudence issues . . ." and "[h]e explained that the uncertainty around such prudence issues can be expected to put downward pressure on bond ratings and the price of stock." KCPL/GMO entered with the Staff into a Joint Motion Of Staff, KCP&L And GMO To Extend The Filing Date Of Staff's Construction Audit And Prudence Review Reports And The Filing Date Of Responses Or Rebuttal Testimony To KCP&L's And GMO's Next General Rate Cases, which was filed on May 28, 2009 in Case Nos. ER-2009-0089 and ER-2009-0090. KCPL/GMO and the Staff stated at page 5, paragraph 6 in said Joint Motion that extending the Staff's filing date to the date of the filing of the Staff's direct testimony in the next general rate cases of KCPL and GMO "will not prejudice any party to these cases . . ."

Additionally, KCPL/GMO and The Empire District Electric Company ("Empire") could have tried the Iatan 1 ACQS and Iatan 1 common plant issues in the now settled rate increase case of Empire, Case No. ER-2010-0130. However, on January 25, 2010, when the procedural schedule in Empire's rate case, Case No. ER-2010-0130, was still in dispute and the Staff was

proposing to try the Iatan 1 AQCS and Iatan common plant in the then pending Empire rate case, KCPL filed the Response Of Kansas City Power & Light Company To Staff's And Empire's Proposed Procedural Schedules, And To Staff's Motion To Delay The Adoption Of Procedural Schedule. KCPL argued for delay in the hearing of the Iatan 1 AQCS and common plant issues that could have been heard as part of Empire's rate increase case. KCPL's pleading in Empire's rate increase case reads, in part, as follows at paragraph 4, on page 2:

> . . . KCP&L has a different concern with the proposed schedules that pertains to the Iatan 1 AQCS and the Iatan common plant included in Empire's case. In particular, KCP&L is very concerned that the procedural schedule being proposed by Staff may result in any prudence issues related to the completion of the Iatan 1 AQCS and the Iatan common plant being litigated in the context of the pending Empire rate case rather than in the context of the next KCP&L rate case which is anticipated to be filed this Spring.[1] KCP&L strongly believes it would be preferable to wait to litigate such prudence issues until the next KCP&L rate case since KCP&L, rather than Empire, is the majority owner, constructor, and operator of the Iatan Generating Station. Litigating prudence first in the case of a minority owner will likely create both logistical and due process issues. KCP&L, however, also expects that the discussions among the parties may address and resolve this concern. . . .
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> ---
>
> [1] In Staff's Proposed Procedural Schedule And Other Proposed Procedures, Staff stated at page 3: "The Staff's direct case filing on February 26, 2010 will include the Staff's Iatan 1 AQCS and Iatan 1 common plant construction audit and prudence review filed by Staff on December 31, 2009, in Case No. ER-2009-0089 and Case No. ER-2009-0089, which is based on invoices booked and paid by KCPL through May 31, 2009." KCP&L, as opposed to Empire, is in a better position to substantively respond to the issues raised in those reports.

The Non-Unanimous Stipulation and Agreement filed on February 25, 2010 and approved by the Commission on March 3, 2010 in Case No. ER-2010-0130 provides for prudence issues related to the completion of the Iatan 1 AQCS and the related Iatan common plant being litigated in the context of Empire's next succeeding rate case to Case No. ER-2010-0130. (EFIS, File No. EO-2010-0259, Item No. 48, filed March 29, 2010, Staff's Reply To Kansas City Power & Light Company's And KCP&L GMO's March 22, 2010 Response To Staff And Kansas City Power & Light Company's And KCP&L GMO'S Response To Commission's March 24, 2010 Agenda Session, pp. 10-12). Thus, both KCPL and Empire had

no objection to the processing of Empire's just concluded rate case in which Empire was seeking recovery of its share of the costs of the Iatan 1 AQCS and Iatan 1 common plant investment without trying any Iatan 1 construction audit / prudence review issues until the KCPL/GMO Iatan 2 rate cases.

Although the Staff and the other non-KCPL signatories to the April 24, 2009 Non-Unanimous Stipulation And Agreement in Case No. ER-2009-0089 and the Staff and the other non-GMO signatories to the May 22, 2009 Non-Unanimous Stipulation And Agreement in Case No. ER-2009-0090 agreed to a cap on disallowances respecting KCPL's and GMO's ownership share of Iatan 1, there is no such cap respecting Empire's ownership share. By not trying Iatan 1 AQCS and Iatan common plant disallowances in the Empire rate increase case, this strategy permitted KCPL/GMO to avoid having to try Iatan 1 AQCS and Iatan 1 common plant in rate cases without disallowance caps. (EFIS, File No. EO-2010-0259, Item No. 48, filed March 29, 2010, Staff's Reply To Kansas City Power & Light Company's And KCP&L GMO's March 22, 2010 Response To Staff And Kansas City Power & Light Company's And KCP&L GMO'S Response To Commission's March 24, 2010 Agenda Session, pp. 10-12). The Staff should note that the disallowances that it has proposed in its December 31, 2009 Staff Reports are not near the caps of $30 million for KCPL and $15 million for GMO established in the revenue requirement/global agreement Stipulation And Agreements in Case No. ER-2009-0089 and Case No. ER-2009-0090.

XV. Case No. EM-96-149 Delay Of Commission Report And Order For Market Power Testimony

As previously noted, KCPL/GMO relate at page 39 of their Initial Brief that Mr. Cline of KCPL/GMO testified about the "expected adverse reactions of investors" and "expected . . . downward pressure on bond ratings and the price of stock" that the uncertainty surrounding a

failure to resolve the Iatan 1 and common plant prudence issues" as KCPL/GMO are proposing would have. It nearly goes without saying that when Commissioners have before them a significant case or issue they should take as much time as they deem necessary given the bounds of any statutory limits and propriety. In 1996-1997, when Union Electric Company was before the Commission seeking approval of a proposed merger with Central Illinois Public Service Company, after the parties appeared before the Commissioners for an on the record presentation of a Stipulation And Agreement resolving all issues among the parties, or at least there was no party opposed to the Stipulation And Agreement, the Commissioners took almost an additional six (6) months to consider the Stipulation And Agreement because of market power questions that they wanted addressed. Regardless of the financial consequences of the Commission's action to the utilities involved, the Commission issued a September 25, 1996 *Order Requesting Additional Information* stating: "the Commission requests the parties to submit additional testimony, either individually or jointly, regarding the market power which will be created in Ameren Corporation, the proposed new holding company which will own Union Electric Company (UE), Central Illinois Public Service Co., and a non-utility investment company if the merger is approved." *Re Union Electric Co*., 5 Mo.P.S.C.3d 157, 158 (1996). The Commission identified the various points of analysis it desired the parties to address in additional testimony. The Staff utilized the State of Missouri's request for proposal process to obtain a market power consultant after the Commission's September 25, 1996 *Order Requesting Additional Information*. Additional testimony was submitted by the Staff, Public Counsel, and Union Electric Company. The Commission approved the proposed Stipulation And Agreement in a Report And Order issued on February 21, 1997.[3] The Staff raises this matter only to suggest that

[3] A.G. Processing ("AGP") in *State ex rel. A.G. Processing v. Public Serv. Comm'n*, 120 S.W.3d 732, 735-36 (Mo. banc 2003) argued, among other issues, that the Commission impermissibly shifted the burden of proof of §393.150

there never should be a pell-mell rush to judgment, either in reality or in perception. One of the present counsel for KCPL/GMO was Chairman of the Commission in 1996-97.

XVI. Conclusion

For the reasons stated in the Staff's Initial Brief filed on May 21, 2010 and for the reasons related above, the Commission should deny KCPL's/GMO's request for any substantive or procedural relief or rulings relating to the prudence review / construction audit of Iatan 1 AQCS and Iatan common plant outside of the context of the full contested case hearings in the impending KCPL and GMO Iatan 2 rate cases.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that copies of the foregoing have been mailed, hand-delivered, transmitted by facsimile or emailed to all counsel of record this 5th day of June, 2010.

/s/ Steven Dottheim

from the applicants in the merger case of UtiliCorp and SJLP to the intervenors by failing to require UtiliCorp and SJLP to submit a market power study. The Missouri Supreme Court held that the §393.150.2 burden of proof pertains to rate cases and not mergers; the Commission, as an administrative agency, is not bound by *stare decisis*, nor are Commission decisions binding on the judiciary; and AGP failed in its burden to show by clear and satisfactory evidence that applicants in a merger proceeding were required to submit a market power study.