

Exhibit No. \_\_\_\_\_

Issue: \_\_\_\_\_

Witness: Steven C. Carver

Sponsoring Party: GST

Type of Exhibit: Surrebuttal Testimony

Case No. EC-99-553

**BEFORE THE PUBLIC SERVICE COMMISSION**

**STATE OF MISSOURI**

**SURREBUTTAL TESTIMONY**

**OF**

**STEVEN C. CARVER**

**FILED**

APR 6 2000

Missouri Public  
Service Commission

Jefferson City, Missouri  
April 6, 2000

**SURREBUTTAL TESTIMONY OF  
STEVEN C. CARVER  
ON BEHALF OF GST STEEL COMPANY  
CASE NO. EC-99-553**

1 Q. Please state your name and business address.

2 A. My name is Steven C. Carver. My business address is 740 North Blue Parkway, Suite 204,  
3 Lee's Summit, Missouri 64086.

4 Q. Are you the same Steven C. Carver whose prepared direct testimony has been previously  
5 filed in this proceeding?

6 A. Yes, I am.

7 Q. On whose behalf are you appearing in this proceeding?

8 A. As indicated in my direct testimony, Utilitech was retained by GST Steel Company  
9 (hereinafter "GST") to assist in its evaluation of the rates charged by the Kansas City Power  
10 & Light Company ("KCPL" or "Company") pursuant to the Amended and Restated Power  
11 Supply Agreement ("Power Supply Agreement" or "Special Contract") executed by the  
12 parties on August 12, 1994.

13 Q. Please summarize the purpose and content of your surrebuttal testimony in this proceeding.

14 A. On behalf of GST, I will respond to portions of the rebuttal testimonies of Staff witness Dr.  
15 Michael S. Proctor and Company witness Mr. Chris B. Giles. In summary, the prices paid  
16 by GST do make a contribution to KCPL's fixed costs including property insurance, GST  
17 has paid higher costs for replacement power as a result of the Hawthorn explosion and GST  
18 should receive the benefit of the replacement power insurance proceeds as an offset to the  
19 higher costs incurred.

20 **Response to Staff Rebuttal Testimony**

1 Q. At pages 3 through 7 of his rebuttal testimony, Dr. Proctor provides certain background  
2 information regarding the GST/KCPL Special Contract and offers certain views regarding  
3 the options available to the contracting parties to resolve differences which might arise in the  
4 administration of such contract. Do you have any general comments applicable to this  
5 portion of the Staff's rebuttal testimony?

6 A. Yes. On March 17, 2000, the Commission Staff, KCPL and GST filed separate comments  
7 with the Commission to address certain questions raised by the Commission's February 17,  
8 2000, Order Concerning Show Cause Hearing. As addressed by the following excerpts from  
9 the respective comments, KCPL and GST have effectively waived the arbitration provisions  
10 of the contract and have presented their disagreement to the Commission for resolution:

11 Commission Staff

12 Since the effect of the contract provisions on the parties to the  
13 contract may be dependent on the intent of the parties, whether or not the  
14 arbitration provision is binding on the parties is something that the parties to  
15 the contract should probably address first, and to which the Staff may  
16 respond.

17 However, Staff would suggest that generally the right to arbitrate  
18 given by a contract may be waived, and that such waiver may be express or  
19 implied from conduct. [footnote omitted] Since neither party has acted to  
20 enforce the dispute resolution provisions of the contract, Staff might assume  
21 that both parties by their conduct have acted to waive the provision and  
22 proceed with the case at the Commission.

23 [Staff Memorandum dated March 17, 2000; p. 6]

24 KCPL

25 18. In light of the history of this proceeding before the Commission, it is  
26 very likely that a court would rule that both parties have waived their right  
27 to arbitrate the matters currently before the Commission.

28 In summary, the Special Contract explicitly provides that its arbitration  
29 provision does not divest the Commission of jurisdiction over the matters  
30 involved in this proceeding. Further, arbitration is a right of the parties to the  
31 contract. They may exercise this right as they see fit. In the instant case,  
32 they have chosen not to seek arbitration. Finally, it is likely the parties have  
33 waived their right to arbitration by progressing so far before the Commission.  
34 Under the foregoing circumstances, it appears that the arbitration provision  
35 of the Special Contract does not divest the Commission of its jurisdiction  
36 over the matters relating to the instant controversy between KCPL and GST.

1 [KCPL's Suggestions dated March 17, 2000; p. 10]

2 GST

3 The second provision in the Special Contract relevant to the  
4 Commission's inquiry is set forth in Section 7.2. That Section provides as  
5 follows:

6 Commission Authority. This agreement is in all respects made  
7 subject to the jurisdiction and authority of the Commission.  
8 Notwithstanding any other provisions of this agreement, nothing in  
9 this agreement shall be construed as divesting or attempting to divest  
10 the Commission or other regulatory agency or body or any party  
11 hereto of any of its rights, jurisdiction, power or authority vested in  
12 it by law or provided in any governmental regulatory act or law.

13 The plain language of this Section evidences the parties intent not to waive any of  
14 their rights or disturb in any way the Commission's authority over the Contract or the  
15 parties. Further, it expressly supersedes any other provision in the Contract. It must,  
16 therefore, be concluded that the Commission's jurisdiction has been properly invoked  
17 in this case.

18 [GST's Memorandum of Law dated March 17, 2000; p.17]

19 Q. At pages 8 through 11 of his rebuttal testimony, Dr. Proctor disagrees with your testimony  
20 indicating, in part, that GST's payments to KCPL under the terms of the Special Contract do  
21 not include any provision for or contribution to the cost of property insurance. Do you care  
22 to comment on this subject?

23 A. Yes. I do concur with the Staff that, under the pricing terms of the Special Contract, GST  
24 does not pay \*\* \*\*\*. I have not contended otherwise. However, I  
25 disagree with his apparent conclusion that GST has not provided any contribution to the  
26 fixed, joint and common costs incurred by KCPL – which would include the cost of property  
27 insurance. As discussed below, GST does make a contribution to the KCPL's fixed costs  
28 under the terms of the Special Contract.

29 At page 3 of his rebuttal testimony, Dr. Proctor briefly discusses his involvement in the  
30 Staff's review and recommendation for approval of the Special Contract in October 1994.

1 The following excerpts appear in the highly confidential Staff Recommendation that is  
2 attached as Appendix B to GST's original petition filed on May 11, 1999.

3 • \*\*

8 \*\*

9 [Staff Memorandum dated October 21, 1994; p. 2]

10 • \*\*

19 \*\*

20 [Staff Memorandum dated October 21, 1994; p. 2]

21 • \*\*

27 \*\*

28 [Staff Memorandum dated October 21, 1994; p. 4]

29 • \*\*

37 \*\*

38 [Staff Memorandum dated October 21, 1994; p. 4]

1 The Special Contract does include a \*\* \*\*\*. Dr. Proctor's  
2 rebuttal testimony appears to be inconsistent with the Staff's October 1994 memorandum.

3 Q. Please continue.

4 A. At page 4 of his rebuttal testimony, Dr. Proctor states: \*\*  
5  
6  
7

8 \*\* Again, I do not disagree with this statement.

9 However, I do not concur with Dr. Proctor's implied ability to "trace" cash. In other words,  
10 Dr. Proctor has alleged that, because the rates paid by GST pursuant to the Special Contract  
11 are not based on \*\* \*\*, GST does not provide KCPL with any  
12 contribution to cover fixed, joint and common costs such as property insurance.  
13 Nevertheless, the October 1994 Staff memorandum (co-authored by Dr. Proctor) clearly  
14 expresses Staff's opinion that the Special Contract would cover KCPL's \*\*  
15

\*\*.

16 Further, no evidence has been presented to suggest the specific costs or profit elements that  
17 may have been included in or excluded from the \*\*

18 \*\*\_. However remote, it is possible that the \*\*  
19

20 \*\*.

21 As a regulatory auditor, I believe that it is virtually impossible to determine which unique  
22 cost elements such a \*\* \*\* does or does not cover. I certainly can not quantify  
23 how much of a \*\* \*\* GST has made to the cost of property insurance. But, I  
24 do believe that Dr. Proctor is incorrect in his apparent conclusion that GST has not

1 historically provided any funds whatsoever toward the cost of such insurance, just because  
2 the pricing terms of the Special Contract are not based on \*\* \*\*.

3 Because the cost of property insurance has been fully reflected in the rates charged to  
4 KCPL's customers (i.e., there have not been any regulatory disallowances of such costs), the  
5 Company's shareholders have not contributed any funds toward the cost of the property  
6 insurance. Accordingly, the Company's shareholders should not retain the benefit of such  
7 insurance proceeds.

8 Q. At rebuttal testimony page 9, Dr. Proctor states that "if Missouri ratepayers were subject to  
9 a fuel adjustment clause, which they are not, I would argue that KCPL's regular ratepayers  
10 would be entitled to the full amount of the insurance compensation, and special contract  
11 customers would not be entitled to share in this benefit unless \*\*

12 \*\* and their contracts include a specific provision for such  
13 sharing." Do you have any reply?

14 A. Yes. I agree that the existence of a fuel adjustment clause would be a compelling factor in  
15 determining which customers should benefit from any "extra expense - replacement energy"  
16 insurance proceeds received by KCPL. If all of KCPL's customers were absorbing the  
17 increased cost of fuel and purchased power resulting from the Hawthorn 5 explosion, it  
18 would be reasonable to develop an equitable apportionment process to allocate any insurance  
19 benefits.

20 Nevertheless, it is even more compelling that no fuel adjustment clause has been in effect  
21 during the term of this contract. As a consequence, GST is one, if not the only, KCPL  
22 customer whose energy charge has fluctuated with the change in fuel costs. KCPL's full-  
23 tariff customers have not been required to pay any of the increased cost of replacement  
24 power. Essentially, this portion of Dr. Proctor's testimony fails to adequately discuss or  
25 portray the actual fact circumstances in which KCPL currently operates in the State of  
26 Missouri.

1 Q. At page 10 (line 15) through page 11 (line 3), Dr. Proctor implies that only customers who  
2 pay rates subject to the "traditional" regulatory treatment of costs should derive any benefit  
3 from items such as the replacement power insurance proceeds. Are any of KCPL's existing  
4 full-tariff customers receiving any direct benefit from such insurance proceeds?

5 A. No. There are only two basic "traditional" mechanisms through which such benefits could  
6 be conveyed to the Company's full-tariff customers. Those mechanisms are: a fuel  
7 adjustment clause and a pending rate case (through which these proceeds are used to either  
8 reduce current tariff rates or decrease a proposed rate increase). Neither of these "traditional"  
9 mechanisms are presently in existence. So, GST is not seeking to deny any benefits  
10 otherwise due the Company's full-tariff customers.

11 Instead, GST is seeking a portion of the replacement power insurance proceeds as a  
12 reduction, or offset, to the increased costs, or detriment, that it has actually experienced – due  
13 to the unavailability of Hawthorn 5. Other ratepayers are simply not eligible to receive the  
14 benefit of these "extra-expense" insurance proceeds since they have not been required to  
15 incur the increased energy costs and there is no established mechanism to return such funds  
16 to those customers.

17 Q. Beginning at rebuttal testimony page 11, line 14, Dr. Proctor discusses the general  
18 relationship between the risks assumed by the seller/buyer and the price of the services  
19 rendered/received. Dr. Proctor concludes that the application of this principle "...makes it  
20 clear that GST Steel is not entitled to benefits that are not included as terms and conditions  
21 of its contract." Do you have any thoughts on this testimony?

22 A. Yes. Both KCPL and GST have bargained for certain risks and rewards. Even the Staff  
23 recognized this risk/ reward trade-off, as indicated in a previously quoted excerpt from the  
24 October 1994 Staff Memorandum recommending approval of the Special Contract,:

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9 [Staff Memorandum dated October 21, 1994; p. 2]

..\*\*

10 As indicated previously, there is no fuel adjustment clause nor a rate case pending in which  
11 the disposition of these insurance benefits will be considered by the Commission. Even  
12 KCPL acknowledges that GST has experienced increased energy costs pursuant to the terms  
13 of the Special Contract approved by this Commission. [See rebuttal testimony of Company  
14 witness Giles.] Under currently existing circumstances, the adoption of the  
15 recommendations set forth in Dr. Proctor's rebuttal testimony would inequitably benefit  
16 KCPL at the cost of GST.

17 **Response to KCPL Rebuttal Testimony**

18 Q. Beginning at line 19 of rebuttal page 13, Company witness Giles states:

19 "Based on Mr. Carver's testimony, one is to presume that GST has paid  
20 insurance premiums for replacement power. This rationale is absurd. One  
21 could just as well presume that included in the demand charge, the delivery  
22 system charge, or the adder to incremental cost are the fully embedded costs  
23 that are built into the tariff rate schedules of all other customers. . . . No  
24 specific costs can be attributed to the Special Contract's fixed prices that are  
25 based on total system costs, such as those included in the tariff rate  
26 schedule."

27 Do you have any comments regarding Mr. Giles' characterization of your testimony?

28 A. Yes. In order to support this position, Mr. Giles must disagree with the Staff's 1994  
29 memorandum recommending adoption of the Special Contract and/or he must claim an  
30 ability to "trace" cash.

1 If the Company is now contending that the Special Contract does not \*\*  
2 \*\*, KCPL has not offered any evidence  
3 to support such an implication. On the other hand, if the Company concurs that the Special  
4 Contract does \*\* \*\*,  
5 Mr. Giles must be able to trace the specific \*\*  
6 \*\* in order to contend that GST's payments for service contain  
7 no \*\* \*\* to the cost of insurance premiums for replacement power.

8 Interestingly, at page 13, line 12, of his rebuttal testimony, Mr. Giles states: "These [Special  
9 Contract] charges do not represent any particular item or component of the total system cost  
10 of service used to develop regulated tariff rate schedules." This passage is slightly reworded  
11 at page 14, line 3, where Mr. Giles states: "No specific costs can be attributed to the Special  
12 Contract's fixed prices that are based on total system costs, such as those included in the  
13 tariff rate schedule." Based on these statements and the responses to GST Data Request Nos.  
14 15.18, 15.19 and 15.20, it would appear that Mr. Giles has effectively admitted that he, too,  
15 can not "trace" cash.

16 So, as long as total utility revenues cover total utility costs and the prices charged GST  
17 pursuant to the Special Contract \*\*  
18 \*\*, I have no choice but to respectfully disagree with Mr. Giles's  
19 characterization of my direct testimony in this regard.

- 20 Q. Have you alleged that the special contract reflects the same fully embedded costs that are  
21 built into KCPL's general rates and tariffs?
- 22 A. No. I have not made such an allegation. However, it is my contention that any revenues  
23 collected from GST pursuant to the provisions of the Special Contract that are \*\*  
24 \*\*, including  
25 the cost of property insurance.

1 Q. At page 14, line 6, Mr. Giles indicates that GST would not be entitled to any portion of the  
2 insurance collections even if a portion of the premiums are included in the fixed portion of  
3 the Special Contract charges. Do you have any comments?

4 A. Yes. GST knows that KCPL has incurred and will continue to incur significant replacement  
5 power costs in excess of \$5 million. As indicated by the calculations presented by GST  
6 witness Smith, GST is painfully aware of the fact that KCPL has incurred and continues to  
7 incur significant replacement power costs – a portion of which has been directly passed on  
8 to and paid by GST. GST's point is that it should receive the benefit of a portion of those  
9 insurance proceeds as an offset to the higher replacement power costs that it has been  
10 charged.

11 Q. Also at rebuttal page 14, Mr. Giles explains that the block pricing mechanism meets all retail  
12 and firm wholesale customer loads first, such that any benefit from the insurance proceeds  
13 would flow through those customer blocks long before it impacted the incremental price  
14 charged to GST. His rebuttal testimony continues by offering a quantification of the portion  
15 of the \$5 million of insurance that GST could expect to benefit if shared proportionately with  
16 other customers. Do you concur with Mr. Giles's position?

17 A. No. I find it particularly interesting that the process described would assign virtually all of  
18 the replacement power proceeds to all retail and firm wholesale customer loads – loads that  
19 have not been charged any of the increased cost of the replacement power. Certainly, such  
20 an assignment of the replacement power insurance proceeds would be necessary if the retail  
21 and firm wholesale customers were being required to pay the significantly higher costs  
22 incurred by KCPL. As I indicated previously, there is no fuel adjustment clause in Missouri  
23 and KCPL has stated that it will not seek rate changes to recover the higher cost of the  
24 replacement power from its retail and firm wholesale customers. GST is one of the few  
25 customers, if not the only customer, of KCPL that has experienced the detrimental impact  
26 of the higher replacement power costs.

1 Further, Mr. Giles has quantified a portion of the insurance proceeds (i.e., \$225,000) that  
2 would be incremental to GST, if the \$5 million were shared proportionately. Although this  
3 amount was subsequently revised to \$252,000 in KCPL's response to GST Data Request No.  
4 15.21, Mr. Giles has not suggested that KCPL would offset even this small amount against  
5 the significant increase in KCPL's purchased power costs billed to and paid by GST.

6 Q. At page 15 of his rebuttal testimony, Mr. Giles states that the reduction in O&M costs due  
7 to the Hawthorn outage are solely related to fixed O&M costs to which GST is not entitled  
8 to participate. Do you care to comment on this statement?

9 A. Yes. Although I have not conducted a detailed historical analysis of KCPL's O&M costs for  
10 Hawthorn 5 or any other Company generating unit, my direct testimony does not state that  
11 the O&M savings should be flowed through to GST. Instead, I have identified the existence  
12 of such savings and have questioned whether any such savings are properly considered  
13 within the framework of the O&M cost provisions of the Special Contract.

14 In response to GST Data Request No. 11.6, KCPL provided a breakdown of the estimated  
15 \$11.5 million reduction in O&M costs by generating station. This response (attached hereto  
16 as Surrebuttal Schedule 1) shows that KCPL reduced its O&M budget for the Hawthorn  
17 facility by \$7,342,000 (or about 48.6%) and for Iatan by \$2,910,000 (or 26.5%). At page 15  
18 of his rebuttal testimony, Mr. Giles indicates that the Hawthorn outage only impacts fixed  
19 O&M costs. I would expect that the devastating loss of a generating unit would eliminate  
20 all normal O&M costs, including both fixed and variable costs, for the "lost" unit. So, if the  
21 entire reduction in Hawthorn O&M is solely attributable to fixed O&M costs, it would seem  
22 to follow that the Hawthorn unit does not have any variable O&M or any O&M incremental  
23 to serving GST – as the loss of a generating facility should substantially eliminate all of the  
24 O&M costs (both fixed and variable) associated with that unit.

25 If GST has somehow been historically charged for incremental O&M costs attributable to  
26 the Hawthorn facility, it would then seem to follow that the amounts billed to GST

1 subsequent to the explosion should automatically reflect a reduction for the decrease in any  
2 incremental O&M costs related to Hawthorn 5. In any event, GST should no longer be  
3 charged for nor be required to pay any variable O&M associated with Hawthorn 5.

4 Q. At page 16 of his rebuttal testimony, Mr. Giles addresses your discussion of KCPL's double  
5 recovery of the cost of replacement power. Do you agree with Mr. Giles?

6 A. No. At page 20 of my direct testimony, I identify how KCPL would double recover a  
7 portion of the increased cost of replacement power:

8 First, KCPL would recover a portion of the higher cost of replacement  
9 [power] through the prices charged to GST and any other similarly situated  
10 customers. Second, KCPL would recover a portion of the higher cost of  
11 replacement [power] through collection of insurance proceeds.  
12 [Emphasis added, Carver Direct Testimony, page 20, lines 13-16]

13 At no time did I allege or intend to represent that KCPL would double recover all of its  
14 increased cost of replacement power. My testimony clearly states that KCPL would be able  
15 to recover a portion of such higher costs through the prices charged GST and through the  
16 insurance proceeds.

17 Mr. Giles also states on page 16 of his rebuttal testimony that: "At any time replacement  
18 power costs are recovered from tariff rate schedule customers these costs would be offset by  
19 the applicable insurance proceeds as Mr. Carver indicates is standard regulatory accounting  
20 procedures." In the absence of a fuel adjustment clause or processing of a general rate case,  
21 KCPL's tariff rate schedule customers will not be charged the higher replacement power  
22 costs nor participate in the applicable insurance proceeds. The Company would then retain  
23 100% of those proceeds, even though GST has paid for a portion of the increased cost of  
24 replacement power.

1 Q. Are you aware of any intention by KCPL to prepare and submit an application for a general  
2 rate increase to recover the higher cost of replacement power from the Company's tariff rate  
3 schedule customers?

4 A. No. I discuss this very topic at page 15 of my direct testimony. Beginning at page 5 (line  
5 19) of his rebuttal testimony, Mr. Giles refers to the material adverse effect clause of the  
6 Stipulation and Agreement in Case No. ER-99-313 and indicates that KCPL has not  
7 requested any regulatory relief as a result of the explosion, even though earnings have  
8 declined as a result of the loss of Hawthorn 5.

9 GST Data Request No. 15.7 sought information concerning whether the Company considers  
10 the explosion to qualify as a material adverse effect and inquired why KCPL has not sought  
11 any change in its tariff rate schedules. In response, KCPL simply stated: "A final  
12 determination has not been made in this regard." This discovery request also questioned  
13 whether KCPL had prepared any studies or analyses to evaluate whether material changes  
14 have resulted in the Company's total system cost of service, subsequent to the explosion.  
15 KCPL responded with: "No."

16 Based on the available information, it does not appear that KCPL's tariff rate schedule  
17 customers are likely to experience the increased cost of replacement power – as has GST.

18 Q. Beginning at page 16, line 14 of Mr. Giles' rebuttal testimony, the Company claims that it  
19 is GST that has proposed a double recovery by seeking "lower prices as though H-5 was still  
20 operating and also receive insurance proceeds paid to KCPL because of the H-5 outage."  
21 Has Mr. Giles properly characterized GST's request?

22 A. No. GST is not seeking the benefit of the insurance proceeds and also have its costs restated  
23 as if the Hawthorn 5 explosion had not occurred. If the charges billed to and paid by GST  
24 were historically restated to reflect the continued operation of Hawthorn 5, GST would not  
25 request any benefit of the replacement power insurance proceeds. However, if recognition  
26 of the continued operation of Hawthorn 5 is denied or only implemented on a prospective

1 basis, GST would contend that it should still receive the benefit of the insurance proceeds  
2 – because GST has previously been charged for the higher cost of replacement power.

3 **Correction to Direct Testimony**

4 Q. Do you have any clarifications of or corrections to your direct testimony as a result of the  
5 rebuttal testimonies filed by the Staff and KCPL?

6 A. Yes. Referring to page 12 of my direct testimony, I address two sources of information  
7 concerning KCPL's accounting for the insurance proceeds that appeared to be somewhat  
8 contradictory. These data sources were KCPL's response to GST Data Request No. 1.5(c)  
9 and KCPL's SEC Form 10-Q, for the third quarter of 1999. Based on this information, I  
10 concluded that KCPL had not credited any of the insurance proceeds to expense.

11 The apparent purpose of the rebuttal testimony of Company witness Christine Davidson is  
12 to present the Company's actual accounting for the \$85 million of insurance proceeds  
13 received by KCPL. As stated at page 2 of Ms. Davidson's rebuttal testimony, the Company  
14 did record a five million dollar (\$5 million) credit to Account 401555 (purchased power  
15 expense) as a reduction to the cost of replacement power. Based on this additional  
16 information, the referenced portion of my direct testimony reached an incorrect conclusion.

17 Q. Since KCPL did record a \$5 million credit to Account 401555 to reduce the cost of  
18 replacement power expense, did KCPL similarly consider this \$5 million credit in  
19 quantifying the variable cost of purchased power used as an input into the production cost  
20 model underlying the energy costs billed to GST?

21 A. No. [See KCPL response to GST Data Request No. 11.4(e).]

22 Q. Does this conclude your surrebuttal testimony?

23 A. Yes, it does.