

Iatan 2: Audit Purpose Used To Develop Audit Scope

The purpose of this Audit is to determine whether the Iatan Project segments not addressed in the Commission-ordered audits of Iatan 1 Air Quality Control System (“AQCS”) and Common Plant needed to operate Iatan 1 segments of the Iatan Project contain: 1) inappropriate/unreasonable charges or 2) cost overruns resulting from imprudent/unreasonable KCPL actions. The Audit will now be structured to comply with the Commission’s July 7, 2010 directive to cease all audit activities by January 30, 2011. The Audit is being used to assist the Commission in determining the amount of costs of the Iatan Project related to the Iatan 2 and Common Plant segments that should be allocated to Kansas City Power & Light Company’s (“KCPL”) Missouri retail customers to establish the rates that these customers will be charged for electrical service.

▪ ***Factors impacting Audit Scope*** - Existing facts and conditions that should be considered in the further development of the scope for this Audit.

1) Engineering Review - Members of the Commission’s Utility Operations Division conduct site visits and document reviews. As part of a Staff construction audit, engineers in the Engineering Analysis Section of the Energy Department, Utility Operations Division, monitor the progress of the project during construction by making periodic field visits to the site. Field visits begin at the on-set of the construction and continue until a project is determined to meet criteria to be considered fully operational and used for service. During a field visit, engineering Staff meet with construction and KCPL personnel to review the

overall progress of construction, review documents related to changes including changes in the schedule and costs, and receive updates of safety related aspects of the project. The Staff engineers also review the change orders associated with the project. Change order reviews include the evaluation, from an engineering perspective, of the need for, scope and cost of the change order. If it is determined that there are engineering concerns with a change order, the Staff engineers would share this information with the auditing Staff and consult with Staff management to determine the appropriate response. In addition, the Staff engineers work with auditing Staff on specific issues that are raised during the course of the Staff's construction audit to ensure that both an engineering and an auditing perspective are provided. The work performed by the Staff engineers is sometimes referred to as a construction audit (although it is only a part of the Staff's construction audit), but is referred to and considered by Utility Operations Division as an engineering review.

2) KCC Staff Audit Results – The Staff of the Kansas Corporation Commission (“KCC Staff”) has completed its evaluation of the Iatan 2 construction. In its recent filing the KCC Staff proposed Staff Adjustment No. 8 (RB-8) which decreases KCPL's pro forma test year plant in service by \$55,929,184 (total company amount is \$224,000,000). KCC Staff's adjustment is the disallowance of certain Iatan 2 plant in service costs. KCC Staff consultant Walter P. Drabinski, Vantage Consulting, Inc., is the source of this adjustment.

3) Project Cost Overruns and Schedule Delays – Iatan 2 has incurred continuing cost overruns over its definitive estimate/control budget estimate and has not been completed by its initial scheduled completion date.

4) Prior Audit Results Regarding Inappropriate/Unreasonable Charges –

Prior Staff audit activity addressed in the Staff’s Iatan 1 AQCS and Iatan 1 Common Plant December 31, 2009 Reports found inappropriate/unreasonable charges to the Iatan 2 segment of the Iatan Project.

5) Commission’s July 7, 2010 Order –

The Commission’s July 7, 2010 establishes a deadline of completion for all audit activity, of any type, involved with the Iatan 2 generating facility, including common plant shared between Iatan 1 and Iatan 2 of January 30, 2011.

Audit Scope

Audit scope is being defined by the Staff as the range of activities and the time period that will be utilized by the Staff in its audit examination. The areas selected to be included in this scope are based on at least one of three categories. These categories are dollar amount, area subject to error and mistake, and problem areas noted in a prior audit(s). The audit scope will include a review of the recent Kansas Corporation Commission (“KCC”) Staff filing proposing significant ratemaking adjustments to the Iatan Project. The Staff has included in its Motion For Clarification filed on July 14, 2010 a question regarding the Vantage Consulting, Inc. testimony before the KCC. Technical Staff and Staff Counsel Office attorneys are considering attending at least some of the KCC hearings in Topeka, Kansas on the Iatan Project to assist in Staff’s evaluation of the Iatan issues.

The Staff will review each adjustment contained in its December 31, 2009 Iatan 1 AQCS and Iatan 1 Common Plant Staff Reports in Case No. ER-2009-0089 and Case No.

ER-2009-0090 and in its August 6, 2010 Iatan 1 Staff Reports in File No. ER-2010-0355 and File No. ER-2010-0356 for their applicability to Iatan 2. These adjustments follow below and will be treated as separate areas in the Iatan 2 Reports, if applicable to Iatan 2. Each audit area in the Staff's Iatan 2 Report will contain a description of the area, Staff finding regarding the area relevant to the costs of Iatan 2 and Common Plant, the name of the Staff person responsible for the Staff's finding, and description of the information supporting the finding.

The following table lists the Staff proposed adjustments respecting Iatan 1 AQCS and Iatan 1 Common Plant, without any summary information related to each Staff adjustment. The Staff's proposed adjustments for Iatan 2, if any, will be separate areas in Staff's Iatan 2 Report and will be prepared by the same individuals that prepared the Staff's adjustments in the December 31, 2009 and the August 6, 2010 Reports on Iatan 1 AQCS and Common Plant. An explanation and support for the adjustment is presently contained in the Detailed Findings sections of the Staff's December 31, 2009 Iatan 1 AQCS and Iatan 1 Common Plant Reports.

<u>Adj.</u>	<u>Adjustment Description</u>	<u>Total Project</u>	<u>AFUDC-KCPL</u>	<u>Total</u>
1	May 23, 2008 Crane Accident Adjustment	**\$_____**	**\$_____**	**\$_____**
2	Employee Mileage Charge Adjustment	**\$_____**	**\$_____**	**\$_____**
3	Schiff Hardin Out-of-Pocket Expense Adjustment	**\$_____**	**\$_____**	**\$_____**
4	Schiff Hardin Hourly Rate Adjustment	**\$_____**	**\$_____**	**\$_____**
5	Schiff Hardin Work Scope Adjustment	**\$_____**	**\$_____**	**\$_____**
6	Alstom July 18, 2008 Settlement	**\$_____**	**\$_____**	**\$_____**
7	JLG Incident Alstom Settlement	**\$_____**	**\$_____**	**\$_____**
8	JLG Surfacing Alstom Settlement	**\$_____**	**\$_____**	**\$_____**
9	Campus Relocation for Unit 2 Turbine Bldg	**\$_____**	**\$_____**	**\$_____**
10	AFUDC Accrual From Turbine Start Up Failure	**\$_____**	**\$_____**	**\$_____**
11	Unregulated Affiliate and KCPL Only Charges	**\$_____**	**\$_____**	**\$_____**
#12	AFUDC For Reduction in Equity Rate	**\$_____**	**\$_____**	**\$_____**
#13	Severance Adjustment	**\$_____**	**\$_____**	**\$_____**
#14	Property Tax to Common Plant	**\$_____**	**\$_____**	**\$_____**
#15	Remove Excess Iatan 1 Common Plant AFUDC	**\$_____**	**\$_____**	**\$_____**
#16	Remove Excess Iatan 1 Common Indirects AFUDC	**\$_____**	**\$_____**	**\$_____**
17	Project Development Costs Transferred to Unit 2	**\$_____**	**\$_____**	**\$_____**
#18	AFUDC For GPE Acquisition of Aquila	**\$_____**	**\$_____**	**\$_____**
	Total	\$26,631,529	\$3,101,927	\$29,733,456

Staff adjustment respecting KCPL, not respecting GMO.

Presently, the Staff's Iatan 2 Audit is being based on the actual costs of the Iatan 2 and Iatan Project Common Plant segments of the Iatan Project as of April 30, 2010. This

data is the most current information on the Iatan Project costs that KCPL has made available to the Staff. Among other things, this information is being used by the Staff to identify the areas that will be included in the Staff's Iatan 2 Audit. The Staff will continue to rely upon its data request to KCPL for the provision of monthly invoices, as they become available, which is generally forty-five (45) days after the end of a given month. The Commission has scheduled true-up hearings in File Nos. ER-2010-0355 and ER-2010-0356 for mid-February 2011. The Staff will monitor each KCPL update to determine if additional areas need to be added to the Staff's Reports through the October 31, 2010 update, which should be provided to the Staff by KCPL by approximately December 15, 2010. The October 31, 2010 update is the last update that the Staff will be able to consider with a January 30, 2011 deadline for final completion for all audit activity, of any type, involved with the Iatan 2 generating facility, including any common plant shared between Iatan 1 and Iatan 2.

Other areas that presently will be part of the scope of the Iatan 2 segment of the Staff's case in File Nos. ER-2010-0355 and ER-2010-0356 will be Internal Control, Cost Control, Common Plant, Major Decisions, Cost Overruns, KCC Staff Adjustments, Experience of the Project Management Team, as well as the final version of the Audit Scope and Risk Assessment as modified by information found by future audit activities.

The direct testimony of KCPL witnesses regarding Iatan 1 AQCS, Iatan 2, and Iatan Common Plant will be compared to Staff Iatan Project information and to obtain additional Iatan Project information of which Staff was not aware. All of this information including the information Staff obtains as a result of reviewing the Iatan

Project proceedings before the KCC will be used by Staff in developing the positions that Staff will take in its Reports and testimony.

The scope of the Staff's audit is influenced by results of preliminary tests, risk assessments, and internal control evaluation. It is impractical to examine, develop, or follow every possible line or avenue relative to an endeavor as large as the Iatan 2 segment of the Iatan Project.

KCPL will not close the Iatan 2 segment of the Iatan Project by January 30, 2011. KCPL will incur in the tens of millions of dollars after Staff's audit of Iatan 2 is "completed" for the purposes of File No. ER-2010-0355 and File No. ER-2010-0356. The Staff estimates that **\$_____** of costs before consideration of AFUDC will be beyond the January 30, 2011 audit cutoff date.

Assigned members of the Staff will meet with the Executive Director early the week of July 18, 2011 to finalize Staff assignments for all projected areas in the Staff's Iatan 2 Reports. The information needed to address the audit areas specified in the Staff's audit scope will be obtained through various audit activities. Some examples of these specific audit activities are as follows:

- a. KCPL employee interviews
- b. Project manager interviews
- c. Review minutes of periodic CEP Oversight Committee minutes
- d. Confer with other regulatory personnel charged with reviewing the appropriateness, reasonableness, and prudence of the Iatan construction projects.
- e. Review testimony related to the Iatan construction projects of other regulatory personnel charged with reviewing the

appropriateness, reasonableness, and prudence of the Iatan construction projects and KCPL's response to such testimony.

f. Investigate apparent discrepancies in KCPL responses and incomplete KCPL responses to different jurisdictions.

g. Review KCPL officer expense reports and evaluate the effectiveness of KCPL's officer expense report process internal controls

h. Review a significant number, but not all, of construction contractor and vendor invoices. Issue follow-up data requests as needed.

i. Review GPE and KCPL Board of Director Minutes regarding any matters relating to the construction projects.

j. Visit the construction work site, among other things, to interview appropriate work site personnel to determine fully operational and used for service status and examine construction activities.

k. Meet with project management personnel at KCPL's Kansas City headquarters building to review project status and costs.

l. Iatan Project contract evaluation respecting relevant provisions affecting project costs and schedule.

Iatan 1 Continuing Audit Scope

The Commission directed in Ordered item 8 of its July 7 Order that “[a]ll audit activity, of any type, associated with the environmental upgrades to Iatan I, if not already filed, shall be completed and filed no later than August 6, 2010.” The Staff’s August 6, 2010 Iatan 1 Reports will be based on updating the Staff’s December 31, 2009 Reports through April 30, 2010 cost information. The Staff has issued data requests to KCPL designed to identify any Staff adjustments proposed in the December 31, 2009 Staff Iatan 1 AQCS and Iatan 1 Common Plant Reports that KCPL has recorded against the costs of Iatan 1 as of April 30, 2010. The Staff will inquire as to KCPL’s position / the status of KCPL’s position regarding items that the Staff identified as inappropriate charges. The Staff will request a meeting with KCPL to inquire regarding KCPL’s position / the status of KCPL’s position regarding all other content of the December 31, 2009 Staff Reports.

The Common Plant portion of the December 31, 2009 Staff Reports will be updated, transferred to, and addressed in the Staff’s Iatan 2 and Common Plant Audit Reports to be filed based on the procedural schedule in File No. ER-2010-0355 and File No. ER-2010-0356. The Staff will transfer any costs related to the auxiliary boiler matter from the Iatan 1 AQCS costs to the Iatan Project Common Plant segment.

The Staff has an outstanding data request to KCPL regarding the identification and explanation for the cost overruns for the Iatan 1 AQCS segment of the Iatan Project. KCPL’s response will be considered by the Staff conjunction with the Staff’s Iatan 1 AQCS audit and review to determine whether the cost overruns have been adequately identified and explained. Historically, the Staff has reflected cost overruns that have not

been adequately identified and explained as Staff adjustments and will likely continue to propose that such items be reflected as adjustments. At page 5 of both of its December 31, 2009 Staff Reports, the Staff stated \$60 million in Iatan 1 AQCS cost overruns would be examined in conjunction with Staff's audit of Iatan 2 cost overruns. The Staff's December 31, 2009 Reports state that while Staff was not at that time proposing a disallowance of the Iatan 1 AQCS cost overruns not identified or explained by the change management system, the Staff could not recommend inclusion of these amounts without identification, explanation, and review. Both December 31, 2009 Staff Reports further stated at page 5 that subsequent Staff audit work on Iatan 2 and the remaining Common Plant, with additional interaction with KCPL representatives, was expected to result in further refinement of this \$60 million number leading to an opinion by the Staff whether costs are justified or should be disallowed.

The KCC Staff in KCPL's currently pending Kansas rate case has proposed KCC Staff Adjustment No. 7 (RB-7) which decreases KCPL's pro forma test year plant in service by \$13,702,672 (total company amount is \$30,024,896). The KCC Staff's adjustment is the disallowance of Iatan 1 and Iatan Common Plant, plant in service costs, previously proposed by the KCC Staff in Docket No. 09-KCPE-246-RTS, KCPL's prior rate case before the KCC. The adjustment is based upon the testimony of Walter Drabinski, the KCC Staff consultant.

All Staff audit activity, of any type, associated with the environmental upgrades to Iatan 1, if not already filed, will be completed and filed no later than August 6, 2010. On August 7, 2010, the Iatan 1 AQCS project will not be closed by KCPL. The Staff expects tens of millions of dollars of Iatan 1 related activity to occur outside the scope of this

audit which pursuant to the Commission's Order is to be completed and filed by the Staff no later than August 6, 2010. At this stage of the audit, the Staff will compare the results to the cap terms in the overall revenue requirement Stipulation And Agreements in Case No. ER-2009-0089 and Case No. ER-2009-0090.

Assigned members of the Staff will meet with the Executive Director early the week of July 18, 2011 to finalize Staff assignments for all projected areas in the Staff's Iatan 1 Reports. It is anticipated that present members of the Staff will continue with their prior work assignments on Iatan 1 AQCS and Iatan Project Common Plant.