BEFORE THE PUBLIC SERVICE COMMISSION
STATE OF MISSOURI

In the Matter of the Application of Kansas City Power & Light Company for Approval to Make Certain Changes in its Charges for Electric Service to Implement its Regulatory Plan.	))))	**Case No. ER-2012-0174** Tariff No YE-2012-0404
In the Matter of the Application of KCP&L Greater Missouri Operations Company for Approval to Make Certain Changes in its Charges for Electric Service.	))))	**Case No. ER-2012-0175** Tariff No. YE-2012-0405

STAFF'S REPLY BRIEF

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STAFF'S REPLY BRIEF

COMES NOW the Staff of the Missouri Public Service Commission, by and through counsel, and for its Reply Brief, states:

INTRODUCTION

Each having initiated these cases by filing a new schedule of rates which the Commission suspended, Kansas City Power & Light Company ("KCPL") and KCP&L Greater Missouri Operations Company ("GMO") each has the burden of proof,[1] which includes not only the burden of production—adducing evidence to support its new schedule of rates, but also the burden of persuasion—convincing the Commission the new schedule is just and reasonable.[2]

In their joint initial post-hearing brief KCPL and GMO have made arguments on several issues to which Staff is replying in this brief. Likewise Staff is responding to argument the group calling themselves Midwest Energy Consumers' Group make in their initial brief in the GMO rate case. That Staff does not address any particular statement or matter contained in the joint initial brief of KCPL and GMO, MECG or any other party, should not be construed as agreement or acquiescence by Staff, unless Staff explicitly states its agreement or acquiescence. Furthermore, unless Staff explicitly states otherwise, the initial briefs of the other parties have not caused Staff to deviate from the positions and recommendations it presented to the Commission in its initial brief on any issue, and Staff continues to urge the Commission to adopt Staff's

[1] § 393.150.2, RSMo. 2000; see e.g., *State ex rel. Noranda Aluminum, Inc. v. Public Service Commission*, 356 S.W.2d 293 (Mo. App. 2011).
[2] See *Kinzenbaw v. Director of Revenue*, 62 S.W.3d 49, 53-55 (Mo. Banc 2001).

positions and recommendations on the issues in this case for the reasons set forth in detail in both this and Staff's initial brief.

Although the Energy Independence and Security Act of 2007 ("EISA") (Section 111(d)(16), (17), (18), and (19) Public Utility Regulatory Policies Act ("PURPA")) electric standards are not a contested issue, the Commission should consider and determine whether or not it is appropriate to implement such standards and address these matters in its report and order as described in Staff's initial brief.

Staff notes, as it did during the true-up hearing,[3] that its true-up accounting schedules for GMO include future program funding of $150,000 per year for low-income weatherization that, with the Commission's approval of the stipulation and agreement in GMO's MEEIA case,[4] no longer is to be included in GMO's rate base, it instead is being funded through part of the $18.73 million annual revenue requirement attributable to the MEEIA agreement.

COST OF CAPITAL

Return on Common Equity

What return on common equity should be used for determining rate of return*?*

In its initial post-hearing brief, Staff recommended that the Commission authorize a return on common equity ("ROE") in the range of 9.0 to 9.92, midpoint 9.46, rounded up to 9.50.[5] The bottom of this range is based on Mr. Murray's recommendation of 9.0,

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[3] Vol. 21, Tr. 1118.
[4] *In the Matter of KCP&L Greater Missouri Operations Company's Application for Approval of Demand-Side Programs and for Authority to Establish a Demand-Side Programs Investment Mechanism*, Case No. EO-2012-0009, (Nov. 15, 2012, *Order Approving Non-Unanimous Stipulation and Agreement Resolving KCP&L Greater Missouri Operations Company's MEEIA Filing*).
[5] *Staff's Initial Post-Hearing Brief,* p. 16.

the Lowest Reasonable Rate, and the top is set national average of awarded ROEs for the first three months of 2012 at 9.92.[6] The midpoint, rounded up to 9.50 from 9.45, is identical to Mr. Kahal's recommendation of 9.50 and just above Mr. Gorman's recommendation of 9.40.[7] Staff made this recommendation based on a consideration of the relevant factors, including the testimony and recommendations of the four expert cost-of-capital witnesses, the generally reduced cost of capital since the Great Plains operating companies' last general rate cases,[8] and the recent downward trend in awarded ROEs for electric utilities.[9]

The Great Plains operating companies urge the Commission to "reject Mr. Murray's analysis and recommendations, as it has in the past."[10] The Companies invite the Commission to set the ROE within 100 basis points above or below the national average in a return to its former "Zone of Reasonableness" analysis.[11] Company witness Dr. Samuel Hadaway finds himself well out of the mainstream in these cases, insisting on a ROE much higher than the other experts' recommendations, higher than the national average of awarded ROEs, and higher than the Great Plains operating companies' last awarded ROE, in a declining cost-of-capital environment. Dr. Hadaway insists on a ROE for the Companies that is *higher* than they were awarded in their last general rate case.[12] Staff's recommended range of 9.0 to 9.92 largely overlaps the ranges proposed by expert witnesses Matthew Kahal and

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[6] Tr. 17:423.
[7] Kahal: Tr. 17:543-544; Gorman: Tr. 17:536.
[8] *Staff's Initial Post-Hearing Brief,* pp. 12-14; Tr. 17:544-545.
[9] Tr.: 17:422-423.
[10] *KCPL & GMO Initial Post-Hearing Brief,* p. 15.
[11] *Id.,* p. 17.
[12] *KCPL and GMO Initial Post-Hearing Brief,* p. 14.

Michael Gorman, 8.80 to 9.80 and 9.10 to 9.50, respectively.[13] A review of the analytical results of the four experts shows that Messrs. Murray, Kahal and Gorman overlap in the band between 6.7 and 9.6.[14] Only Mr. Kahal reports a result that, at 9.8, is as high as Dr. Hadaway's lowest result.[15] The experts thus naturally sort into two groups, the non-company experts and the company expert. The weight of the evidence thus suggests a ROE of 9.6 or below.

Logic tells us that the Companies, of course, want the *highest* ROE they can get. This is reflected in Dr. Hadaway's range of 9.8 to 10.3 and his point recommendation of 10.3 at the high end of his range. Dr. Hadaway's low end is close to the national average, while his high end is even higher than the Companies were awarded in their last rate cases. Logic also tells us that customers want the *lowest* ROE they can get, which is reflected in the recommendations of the other three experts at 9.0, 9.4 and 9.5. Staff's position, which takes the high end of Mr. Murray's range as its low end and the national average as its high end, embraces the recommendations and most of the ranges of both Mr. Kahal and Mr. Gorman.

Dr. Hadaway's range and recommendation are simply too high and are, frankly, contrary to the weight of the credible evidence as reflected by the testimony of Messrs. Murray, Kahal and Gorman. In particular, they are based on outlandishly high growth rates.[16] Even a cursory glance at Table 2 in Staff's *Initial Post-Hearing Brief* reveals that Dr. Hadaway used higher growth rates than did Messrs. Murray, Kahal and

[13] Tr. 17:536, 543-544.

[14] *See* Table 2 at p. 31, *Staff's Initial Brief*. Mr. Murray's results range from 5.96 to 9.60; Mr. Gorman's from 7.98 to 9.73; and Mr. Kahal's from 6.7 to 9.8. Dr. Hadaway's results range from 9.8 to 10.3.

[15] *Id*.

[16] Tr. 17:556 (Kahal): "All I know is that 5.7 percent is way out of line with the consensus of expert forecasters. It's way too high."

Gorman.[17] Mr. Kahal noted that the growth rate used by Dr. Hadaway, 5.7%, includes a 3% inflation expectation, whereas "the blue chip consensus is for long-term inflation outlook of 2.1 percent for the GDP deflator."[18]

The purpose of ROE testimony is to describe investor expectations. It's just that simple. What is the average return that investors expect on the stocks of the proxy group selected for analysis? The evidence of record does not support Dr. Hadaway's depiction of those expectations; nor should the Commission ignore his manipulation of his proxy group in his updated analysis. Instead, the similar testimony and broadly congruent recommendations of the other experts, Messrs. Murray, Gorman and Kahal, provide a reliable, bench-tested picture of investor expectations.

Staff's recommended range of 9.0 to 9.92, particularly where it overlaps the recommendations of Mr. Kahal at 9.5 and Mr. Gorman at 9.4, is well-supported by the record. Staff urges the Commission to select a ROE in this range, preferably in the zone formed by Mr. Murray's recommendation of 9.0 and the high end of the previously described zone of expert agreement at 9.6. Within this zone, Staff believes 9.5 would be an appropriate number.

<u>Capital Structure</u>

What capital structure should be used for determining rate of return?

The appropriate capital structure for determining the allowed rate of return is GPE's consolidated capital structure, exclusive of short-term debt, as of the true-up date, August 31, 2012.

[17] Dr. Hadaway used 5.48 and 5.7; Mr. Murray used 3.0 to 5.5, Mr. Gorman used 4.85 to 5.14; and Mr. Kahal used 4.5 to 5.5. *See* Table 2, p. 31, *Staff's Initial Post-Hearing Brief.*

[18] Tr. 17:558.

<u>Cost of Debt</u>

Should GPE's consolidated cost of debt be assigned to KCPL and GMO or should the cost of debt be subsidiary specific?

Staff's position is that GPE's consolidated cost of debt should be assigned to KCPL and GMO.

In either case, should adjustments be made to holding company debt issued subsequent to GPE's acquisition of GMO?

Yes.

Should any adjustments be made to certain debt issuances? Should the cost of debt be a consolidated cost of debt of 6.425%?

Yes, adjustments should be made to certain debt issuances. The following GPE debt issuances should be adjusted downward anywhere within the ranges supported in Staff's testimony with Staff recommending point adjustments in its surrebuttal testimony:

- GPE's $250 million, 3-year, 2.75% Note: 60 to 75 basis points; point estimate of 65 basis points;
- GPE's $350 million, 10-year, 4.85% Note: 60 to 85 basis points; point estimate of 65 basis points;
- GPE's $287.5 million, 10-year, 5.292% Note: 110 to 120 basis points; point estimate 115 basis points.

No, the cost of debt should not be 6.425%. After the aforementioned adjustments are made, the appropriate consolidated cost of debt should be 6.187%.

As Staff argued in its *Initial Post-Hearing Brief,* adjustments must be made to protect GMO's ratepayers from the continuing ill effects of Aquila's legacy debt.[19] GPE's financial guarantee has allowed GMO to have an investment grade credit rating, but this rating is still below the level at which Aquila committed to assess hypothetical

[19] *Staff's Initial Post-Hearing Brief,* pp. 42-44.

costs to Missouri ratepayers. Although all of that Aquila debt has now been retired, "GMO's debt costs are still not free from the effects of the creative financing techniques required to finance GMO's Missouri utility assets."[20] These techniques were necessary only because of Aquila's failed unregulated ventures.[21] GMO's assets are high-quality and low-risk; but for the lingering taint of Aquila, Staff believes that GMO would be rated "BBB" just like KCPL.[22] For this reason, Staff's proposed downward adjustments are required to protect GMO's ratepayers. The size of the adjustments are based on cost-of-debt spreads obtained by the GPE companies from their underwriters and obtained in turn by Staff through discovery. The adjustments are neither unreasonable nor arbitrary, but are rather equitable and thoughtful.

Kevin A. Thompson

CROSSROADS

As stated in the introduction, GMO has the burden of proof in its case, which includes the burden of production and the burden of persuasion, i.e., GMO use not only adduce evidence to support its positions, it must also convince the Commission of them.

<u>What should be the value of Crossroads included in rate base?</u>

In its initial brief GMO argues that the net cost it has recorded on its books and records ("net book cost")—which does not reflect the Commission's valuation of Crossroads in GMO's last general electric rate case—is the "net original cost" of Crossroads and that it is the only party who offered competent evidence of the value of Crossroads. Both arguments are wrong.

[20] *Id.*
[21] *Id.*
[22] *Id.*

Although GMO has the burdens of production and of persuasion, GMO's evidence of the "net book value" of Crossroads as of August 31, 2012 (the end of the ordered true-up period), is nonexistent as far as Staff can tell, and its evidence of "net book value" is thin otherwise. Staff found the following evidence in the record: In direct testimony GMO witness Rush testifies that GMO included for its rate base for its MPS rate district "the full plant balances and depreciation reserves and expenses for Crossroads based on the jurisdictional plant balance," which is the same position it took in its last general electric rate case.[23] In rebuttal testimony GMO witness Crawford, as GMO notes in its brief, testifies, "As of March 31, 2012, GMO valued Crossroads at ***approximately*** (Emphasis added.) $82.7 million." That is the extent of GMO's evidence Staff could find in the evidentiary record of GMO's "net book value" for Crossroads.

However, Staff, when it filed rebuttal testimony, based on GMO responses to Staff data requests, pegged GMO's net book value for Crossroads in direct at $91.3 million ($132.7 million plant in service, including transmission plant, less $41.4 million depreciation reserve for a net of $91.3 million).[24] Notably, GMO does not cite in its brief where its "net book value" for Crossroads as of August 31, 2012, may be found, nor does its cite where the components that make up net book value—the full plant balances and depreciation reserves and expenses that GMO witness Rush refers to in his direct testimony—may be found.

In contrast, Staff's valuation of Crossroads as of August 31, 2012, if GMO recovers no Crossroads transmission expense ($62,609,430), appears on line 102 of page three of five of Staff Accounting Schedule 3 for GMO's MPS rate district, admitted

[23] Ex. GMO-134, GMO witness Rush Direct, p. 8.
[24] Ex. Staff-272, Featherstone GMO Rebuttal, p. 23.

into evidence on November 19, 2012.[25] The associated accumulated depreciation reserve as of the same date is $10,033,437 as shown on line 102 of page three of five of Staff Accounting Schedule 6 for GMO's MPS rate district.[26] The associated accumulated deferred income tax, also of that same date is $4, 333,301.[27] Therefore, the impact on GMO's rate base for its MPS rate district is $62,609,430 less $10,033,437 = $52,575,993, offset by $4,333,301 = $48,242,692.

The term "original cost" is defined in Commission Rule 4 CSR 240-20.030, which incorporates the 1992 version of the FERC Uniform System of Accounts, as follows: "*Original cost,* as applied to electric plant, means the cost of such property to the person ***first devoting it to public service***."[28] (Emphasis added). "Book cost" and "cost" are also defined in that rule. "Book cost" means "the amount at which property is recorded in these accounts without deduction of related provisions for accrued depreciation, amortization, or for other purposes." Cost" means "the amount of money actually paid for property or services. When the consideration given is other than cash in a purchase and sale transaction, as distinguished from a transaction involving the issuance of common stock in a merger or a pooling of interest, the value of such consideration shall be determined on a cash basis."

As Staff witness Featherstone testifies, paragraph 15,052 of the FERC USOA provides, "All amounts included in the accounts for electric plant acquired as an operating unit or system, except as otherwise provided in the texts of the intangible

[25] Ex. Staff-384.
[26] *Id*.
[27] Ex. GMO-119, GMO witness Hardesty Surrebuttal, p. 9; Ex. Staff-384, GMO True-up Accting Sch. 2, p. 1 of 2, l. 37; Ex. GMO-149, GMO witness Rush True-up Rebuttal, pp. 1-2.
[28] Commission Rule 4 CSR 240-20.030(1) incorporates the 1992 versions of FERC Uniform System of Accounts published at 18 CFR Part 101 and FERC Stat. & Regs. Paras. 15,001 *et seq.*, and original cost is defined there.

plant accounts, shall be stated ***at the cost incurred by the person who first devoted the property to utility service***."[29] (Emphasis added). After quoting that FERC USOA paragraph, Staff witness Featherstone explains, "Depreciation and amortization of the utility property from the previous owner must be deducted from the original cost, which results in a net original cost figure to be recorded on the purchaser's books and records. The acquired property is valued at the same value the seller placed on it, hence the "original cost when first devoted to public service," adjusted for depreciation and amortization, concept."[30] The significance of the foregoing is that "original cost" is the value of the property ***when*** it is first devoted to public utility service.

GMO argues "net original cost" for Crossroads is approximately $82.7 million,[31] which is based off of an assertion the original cost (net booked cost as of July 14, 2008) of Crossroads is about $116 million—booked cost of about $140.7 million less booked depreciation reserve of $24.3 million.[32] That booked cost is based on what GMO's unregulated affiliate (Aquila Merchant Services, Inc.) and Aquila had invested in Crossroads before it was first devoted to public service, primarily 2002 construction costs.[33]

The Commission has before it in evidence a number of values for Crossroads offered to support and undermine two principal bases for the original cost of Crossroads—GMO's net booked cost basis and Staff's comparable sales basis. GMO relies on a $121 million valuation of Crossroads as of July 14, 2008,

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[29] Ex. Staff-272, Staff witness Featherstone GMO Rebuttal, p. 28.
[30] *Id*.
[31] GMO initial brief, p. 59, para. 157.
[32] Ex. Staff-272, Staff witness Featherstone GMO Rebuttal, pp. 24-25. (Based on plant balances as of September 30, 2008.)
[33] *Id*. at 25-27.

PricewaterhouseCoopers provided to Great Plains Energy in a November 8, 2008, report.[34] That report is not in the evidentiary record, but it was created, after the July 14, 2008, purchase for purposes of a purchase accounting valuation.[35] Staff witness Featherstone testified it should not be relied on for determining the original cost of Crossroads for multiple reasons: (1) it was done to satisfy a requirement to determine the values of acquired assets for purposes of determining impairments and goodwill, (2) it was performed after Great Plains Energy acquired Aquila and after the decision was made to include Crossroads in GMO's rate base, and (3) PricewaterhouseCoopers assumed Crossroads would be included in GMO's rate base at net book value (its analysis would have been different had GMO been planning to scrap Crossroads or otherwise not include it in rate base.[36]

As it did in its last general electric rate case, GMO also relies on a response to a request for proposals for capacity that its affiliate made in March 2007 at net book value, first presented in this case in the rebuttal testimony of GMO witness Crawford for a valuation of $117.9 million.[37] It is also mentioned in a GMO document Staff presented as Schedule CGF-REB-4 to the rebuttal testimony of Staff witness Featherstone in this case. In that document the $117.9 million is identified as the net book value of Crossroads on the affiliate's books which was bid for supplying long-term power to Aquila in response to an Aquila request for proposals issued March 19, 2007. The document also discloses that Crossroads was transferred to Aquila on March 31, 2007,

[34] Ex. GMO-211, GMO witness Crawford Rebuttal, p. 2; Ex. GMO-125, GMO witness Ives Surrebuttal, pp. 37-38.
[35] Ex. Staff-272, Staff witness Featherstone GMO Rebuttal, Sch. CGF-REB-4, p. 2 of 4; Ex. Staff-294, Staff witness Featherstone GMO Surrebuttal, pp. 73-75.
[36] Ex. Staff-272, Staff witness Featherstone GMO Rebuttal, Sch. CGF-REB-4, p. 2 of 4; Ex. Staff-294, Staff witness Featherstone GMO Surrebuttal, pp. 73-75; Vol. 19, Tr. 936-38, Staff witness Featherstone.
[37] Ex. GMO-111, GMO witness Crawford Rebuttal, Sch. BLC-9, slide 18.

at net book value, although Aquila did not book Crossroads in the rate base of its MPS rate district until August 31, 2008, after Great Plains bought Aquila and renamed it GMO.[38] Given the timing of these events and the close relationship between these affiliates, this response to the March 19, 2007, request for proposals is not reliable for the actual value of Crossroads.

The best evidence of what a willing buyer would pay a willing seller is when there is a sale between non-affiliated entities. What GMO has presented is (1) a valuation based on a post-sale analysis by PricewaterhouseCoopers, without presenting the analysis itself and without any foundation for its expertise to conduct that analysis, (2) a valuation based on a response to a request for proposals made by an affiliate, without the response itself, and (3) internal bookkeeping entries to move Crossroads from nonregulated to regulated operations, without the books themselves.

The Commission has before it evidence of several transactions between willing buyers and sellers, transactions where Aquila was the seller and a third party was the buyer—when it sold Goose Creek and Raccoon Creek to AmerenUE, when it sold a combustion turbine to a utility in Colorado and when it sold two combustion turbines to a utility in Nebraska. In contrast to the evidence in the record that would support GMO's valuation for Crossroads, Staff put into the record during its direct case the values at which Aquila actually sold Goose Creek and Raccoon Creek to AmerenUE in 2006, "The final sale price was $175 million and included all the generating equipment, substation and transmission costs. Since the total capacity of these two generating stations is 850 megawatts, the resulting installed capacity cost was $205.88 per kilowatt ($175 million divided by 850,000 kilowatts) [source: Aquila's SEC Form 8-K filed

[38] Ex. Staff-272, Staff witness Featherstone GMO Rebuttal, Sch. CGF-REB-4, pp. 1-3 of 4.

December 16, 2006].”[39] It also put into the record during its direct case the highly confidential values at which Aquila actually sold uninstalled combustion turbines in 2003 to unaffiliated utilities in Beatrice, Nebraska and in Colorado that were the same model combustion turbines as those it installed at Crossroads.[40] Each of those values is a fact, not an opinion; GMO disputes none of them.

In testimony during its direct case GMO admitted the Commission valued Crossroads based on an average of Aquila’s sales of two plants in Illinois as follows: “The Commission ruled in the last case, Case No. ER-2010-0356, that for purposes of setting rates Crossroads’ plant value be reduced from $104 million to $61.8 million, based on the average price of two plants in Illinois previously owned by Aquila that were sold in 2006.”[41] Like the values at which Staff witness Featherstone testified Aquila sold Goose Creek and Raccoon Creek to AmerenUE in 2006 and combustion turbines to utilities in Nebraska and Colorado in 2003, it is fact, not opinion, that the Commission used “the average installed dollar per kilowatt basis AmerenUE paid for the combustion turbines at Raccoon Creek and Goose Creek” to value Crossroads in GMO’s rate base at $61.8 million in GMO’s preceding general electric rate case.[42]

In addition to what AmerenUE paid to Aquila for Goose Creek and Raccoon Creek being a superior basis for valuing Crossroads because they are actual sales consummated between a willing seller and an unrelated willing buyer, they are also a superior basis because they occurred nearer in time to when GMO needed

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[39] Ex. Staff-259, Staff GMO Cost of Service Report, p. 77.
[40] Ex. Stafff-259, Staff GMO Cost of Service Report, pp. 79-80.
[41] Ex. GMO-134, GMO witness Rush, p. 7.
[42] *In the Matter of the Application of KCP&L Greater Missouri Operations Company for Approval to Make Certain Changes in its Charges for Electric Service*, Case No. ER-2010-0356, Report and Order, p. 99.

additional capacity, but relied on purchased power—often acquired from Crossroads—instead of owned capacity. This time was when utilities such as AmerenUE were buying additional capacity in a buyers' market, even though they already had sufficient capacity to meet their short-term needs.[43]

One basis upon which GMO challenges Staff witness Featherstone's opinion of the rate base value of Crossroads is an assertion that the foundation for his opinion is deficient. GMO relies on *Board of Healing Arts v. McDonagh*, 123 S.W.3d, 146 (Mo. Banc 2003), which holds the requirements of § 490.065, RSMo. 2000, apply to administrative proceedings. *McDonagh* and § 490.065, RSMo. 2000 require the following: "The facts or data in a particular case upon which an expert bases an opinion or inference may be those perceived by or made known to him at or before the hearing and must be of a type reasonably relied upon by experts in the field in forming opinions or inferences upon the subject and must be otherwise reasonably reliable." As stated above, in the direct testimony of GMO witness Tim Rush GMO admitted the Commission valued Crossroads based on an average of Aquila's sales of two plants in Illinois. The requisite foundation is in the record in this case since the Commission is a body of experts who reasonably relied on the very same facts and data in GMO's last general electric rate increase case for valuing Crossroads. Even if a sufficient foundation had not been laid, the Commission could base its valuation of Crossroads on the facts before it, not on expert opinion, and it should.

GMO cites *State ex rel. Missouri Water Co. v. Public Service Commission*, 308 S.W.2d 74 (Mo. 1958), on page 60 of its initial brief for the proposition that original cost is a "floor" and fair value a "ceiling," implying the Commission cannot value

[43] Staff's Initial Brief, p. 52; Ex. Staff-294, Staff witness Featherstone GMO Surrebuttal, pp. 78-84.

Crossroads at less than net book value, since GMO equates "original cost" with "net book value." In that case the Court held it was error for the Commission to not consider fair value as one of the all relevant factors when setting new rates, relying instead on original cost less depreciation in the interest of expediency, economy and the difficulty in determining fair value with any accuracy. [44] The "bracket" the Court cited with approval was not necessarily a "floor" of original cost and a "ceiling" of fair value, it was a range bounded by them, where "fair value" could be less than "original cost."[45]

Despite GMO's arguments to the contrary, Staff has adduced competent and substantial evidence upon which the Commission may value Crossroads in GMO's rate base for its MPS rate district at $62,609,430 for purposes of setting rates for that rate district.

GMO ignores the Commission's affiliate transaction rule. As the Commission determined in GMO's last general electric rate case, and as Staff discusses at page 50 of its initial brief and in testimony, because Crossroads was transferred from GMO's affiliate, the Commission's affiliate transaction rule applies. That rule provides a cap on transfers between a utility and its affiliate measured by the lesser of the fair market price or the "fully distributed costs to the regulated electrical corporation to provide the goods or services for itself."[46] As Staff discusses above and in its initial brief, the lesser of the two is fair market price. So long as GMO recovers no transmission expense for Crossroads, that fair market price is the $205.88 per kilowatt AmerenUE paid Aquila for Goose Creek and Raccoon Creek.

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[44] *Id*. at 719.
[45] *Id*. at 718.
[46] Rule 4 CSR 240-20.015.

<u>What amount of accumulated deferred taxes associated with Crossroads should offset the value of Crossroads in rate base?</u>

As addressed on pages 57-60 of its initial brief, Staff is in agreement with GMO on this issue only if the Commission values Crossroads in this case at $62,609,430 as of August 31, 2012. If it does so, then Staff and GMO agree the associated deferred income taxes accumulated through August 31, 2012, are $4,333,301. However, despite GMO's assertions in its initial brief that Staff and GMO agree as to the methodology for calculating the accumulated deferred income taxes associated with Crossroads, that is only true if the Commission values Crossroads at $62,609,430 as of August 31, 2012. If the Commission adopts GMO's position and values Crossroads at or close to net book value as of August 31, 2012, then, as Staff stated in its initial brief, the associated deferred income tax offset should be the deferred income taxes that have accumulated from the date Crossroads was completed in 2002—$14.8 million as of August 31, 2012—because, if the Commission grants GMO a variance from the Commission's affiliate transaction rule—4 CSR 240-20.015—and requires GMO's retail customers in its MPS rate district to pay rates that are based on the costs Aquila's merchant operations incurred for Crossroads, those customers should get the benefit of all the timing differences between tax depreciation accounting and ratemaking depreciation accounting from the date Aquila Merchant built Crossroads in 2002.

Staff disagrees with MECG that the Commission understood and intended in GMO's last general electric rate case to get to a particular overall rate base impact for Crossroads. As Staff stated in its initial brief, it is Staff's view the Commission simply did not have in the evidence before it in that case the appropriate amount of the accumulated deferred income taxes associated with Crossroads based on the

$61.8 million valuation as of July 14, 2008, the Commission determined. Instead, it had GMO's argument there should be no accumulated deferred income tax reserve offset to rate base and evidence from Staff that deferred income taxes of $15 million had accumulated since Crossroads was built in 2002. Here, it has before it what the accumulated deferred income tax reserve offset to rate base is as of August 31, 2012, based on an original cost valuation of Crossroads of $61.8 million as of July 14, 2008—$4,333,301.

<u>Should depreciation expense be based upon the authorized gross plant value for Crossroads?</u>

It appears the parties are in agreement that depreciation expense for Crossroads should be based on the value the Commission determines for Crossroads in GMO's rate base for its MPS district.

<u>What transmission costs for energy from Crossroads should be included in revenue requirement?</u>

As Staff indicated in its initial brief, disallowance of transmission costs for energy from Crossroads is integral to the rate base value of Crossroads. If the Commission allows GMO to recover any such transmission costs, then it must take that into account when valuing Crossroads—transmission costs lower the value. Staff joins with Dogwood Energy, LLC's attorney Carl Lumley in saying that the Commission can disallow these transmission costs without running afoul of federal preemption as set out in *Nantahala Power and Light Co. v. Thornburg*, 476 U.S. 953 (1986) cited by GMO. If the Commission makes the disallowance because of where Crossroads is, then it is not making the disallowance because of the transmission rates, *i.e.*, the disallowance would be because of what GMO did, not because of a disagreement with what the FERC did.[47]

Rather than rehashing here the points it made in its initial brief that respond to GMO's arguments, Staff refers the Commission to pages 61-69 of that brief where Staff explains the deficiencies in GMO's arguments in detail. Among those deficiencies are that GMO has never used Crossroads at any time other than in the summer when it has run no more than half the time to meet peak load, GMO has used high estimates for firm natural cost to the South Harper site for Crossroads if it were located there, the relevant firm gas transportation costs for the comparable sales of Raccoon Creek and Goose Creek are those of the buyer—AmerenUE—not for delivery to GMO in GMO's service area, and that GMO has ignored the cost of the natural gas itself, which is cheaper around Kansas City, Missouri, than it is around Clarksdale, Mississippi.

Nathan Williams

FUEL ADJUSTMENT CLAUSE

<u>What should GMO's FAC sharing be?</u>

GMO begins this section of its initial brief by mischaracterizing the fuel adjustment clause ("FAC") sharing mechanism, claiming that the "sharing mechanism calls for 95% of its prudently incurred fuel and purchased power costs be paid by customers, with 5% to be absorbed by the utility." However, as described in more detail in Staff's initial brief, the sharing mechanism applies to the *difference between* (a) GMO's actual, prudently incurred fuel and purchased power costs net of off-system sales revenues and (b) the billed base fuel and purchased power costs net of off-system

[47] Vol. 19, Tr. 876-77.

sales revenues based on GMO's base energy rates per kWh. This is further reflected in the first sentence of the enabling language of Section 386.266.1 RSMo., which follows: "Subject to the requirements of this section, any electrical corporation may make an application to the commission to approve rate schedules authorizing an interim energy charge, or periodic rate adjustments outside of general rate proceedings *to reflect increases and decreases in its prudently incurred fuel and purchased-power costs*, including transportation." (Emphasis added.) In other words, the Commission should view the fuel adjustment clause from the premise that it is intended to allow the recovery of *variances* from the fuel and purchased power costs embedded in general (base) rates. When viewed from that perspective, the fuel adjustment clause is a vehicle for recovering *changes* in fuel and purchased power costs, not for recovery *of* fuel and purchased power costs. When limited to those variations, a greater risk on the utility is of lesser impact.

GMO's initial brief next mischaracterizes the Commission order which first approved GMO's FAC in 2007, by implying that the 2007 order found after-the-fact prudence reviews to be a sufficient safeguard; however, as set forth in Staff's initial brief, that order specifically found that "after-the-fact prudence reviews alone are insufficient to assure Aquila [now GMO] will continue to take reasonable steps to keep its fuel and purchased power costs down."[48] While the Commission did adopt a sharing mechanism of 95%/5% in 2007, since that time the evidence (described in detail in Staff's initial brief) has continued to mount that the 95%/5% sharing mechanism, which places only 5% of the risk of increases in the cost of fuel and purchased power on GMO, is an insufficient incentive.

[48] Case No. ER-2007-004, *Report and Order* issued May 17, 2007, p. 54.

GMO's repeated mantra that Staff is seeking to penalize it by recommending the sharing mechanism be changed from 95%/5% to 85%/15% is simply untrue. Section 386.266.1 RSMo., allows the Commission to provide electric utilities with incentives to improve the efficiency and cost effectiveness of their fuel and purchased power procurement activities; however, GMO's actions and statements since the sharing mechanism was first adopted by the Commission in 2007 which are detailed in Staff's initial brief demonstrate a 95%/5% sharing simply is not very meaningful to GMO. The Commission has stated its purpose for sharing mechanisms in fuel adjustment clauses is to incent the utility to "keep its fuel and purchased power costs down." Staff recommends the Commission change the sharing mechanism of GMO's fuel adjustment clause from GMO bearing five percent of the risk of increases in fuel and purchased power costs to being at risk for 15% of them. To do so would provide a greater incentive for GMO to develop and manage an effective energy procurement process which minimizes energy costs.

GMO's claim on page 79 of its initial brief that if the historical sharing mechanism had been 85%/15% its earnings would have been reduced by $16.5 million misses the point of an "incentive." If the sharing mechanism had been set at a level which was truly meaningful to GMO and which gave GMO a real incentive to keep its fuel and purchased power costs down (or to increase its off-system sales), there is no way to know with specificity what GMO's fuel and purchased power costs would have been in the past periods relied upon by GMO.[49] Furthermore, as discussed in Staff's initial brief, although GMO focuses solely on periods of increasing costs, under Staff's proposal any decrease in fuel and purchased power costs net of off-system sales revenues

[49] Tr. 835.

(compared to those embedded in base rates) will benefit GMO because it will get to keep 15% of any such decrease instead of only keeping 5% under the current sharing mechanism. In fact, in the most recent GMO FAC accumulation period case, its actual total energy costs were lower than base energy costs billed to customers and GMO was allowed to retain 5% of the difference.[50] Given a more appropriate incentive, there is no reason to believe this should not become the norm.

On pages 80-81 of its initial brief GMO attempts to spin the testimony of its witness, Mr. Blunk, in Case No. EO-2011-0390 to explain away GMO's clear indifference to its actual amount of fuel cost and purchased power costs net of off-system sales revenues under the current 95%/5% sharing mechanism. In its brief GMO attempts to couch the testimony of Mr. Blunk as being that they (*i.e.*, GMO) are indifferent because they are hedged; however, such explanation completely ignores several of Mr. Blunk's more telling statements. For example, GMO's reconstruction fails to address Mr. Blunk's statements that GMO only hedges for the customers' benefit and that there is no benefit to the company of a hedge program when the company has a fuel adjustment clause in place.[51] GMO also fails to address Mr. Blunk's testimony in *this* case that "the Company's exposure to market price risk is managed by having a fuel adjustment clause ("FAC") in place, but without a hedge program, the ratepayer's risk would not be managed."[52] In other words, as stated in Staff's initial brief, by merely having a FAC with a 95%/5% sharing mechanism in place, GMO considers *itself* protected from the risk of higher prices and is indifferent about whether or not it hedges its fuel price risk—unlike ratepayers, who are not protected without a hedging program.

[50] Ex. Staff-259, Staff Cost of Service Report, pp. 265, 267.
[51] Ex. Staff-397, pp. 124-125; Ex. Staff-259, Staff GMO Cost of Service Report, pp. 273-274.
[52] Ex. GMO-104, Surrebuttal Testimony of GMO witness Wm. Edward Blunk, pp. 7-8.

Therefore, the current 95%/5% sharing mechanism is providing insufficient incentive to GMO to keep its fuel and purchased power price down, as GMO believes it is sufficiently protected from the risk of higher prices by simply having a FAC with a 95%/5% sharing mechanism.

In its initial brief GMO also places undue emphasis on the absence of an imprudence finding by Staff in GMO's Third Prudence Review. Regardless of the structure of the sharing mechanism – or even in the absence of a sharing mechanism – a prudence review procedure is statutorily required for any electric fuel adjustment clause pursuant to Section 386.266.4(4) RSMo., which authorizes electric fuel adjustment clauses. It was against this statutory backdrop that the Commission found, as stated above, that after-the-fact prudence reviews are insufficient to assure that GMO takes reasonable steps to keep its fuel and purchased power costs down.[53] GMO's continued reliance on the absence of an imprudence finding does not mean that the current sharing mechanism provides a sufficient incentive, particularly in light of the evidence to the contrary.

Section 386.266.1, RSMo. provides:

> Subject to the requirements of this section, any electrical corporation may make an application to the commission to approve rate schedules authorizing an interim energy charge, or periodic rate adjustments outside of general rate proceedings to reflect increases and decreases in its prudently incurred fuel and purchased-power costs, including transportation. The commission may, in accordance with existing law, include in such rate schedules features designed to provide the electrical corporation with incentives to improve the efficiency and cost-effectiveness of its fuel and purchased-power procurement activities.

The link the Legislature has forged between incentives and fuel and purchased-power procurement is that the Commission may include "features designed

[53] Case No. ER-2007-004, *Report and Order* issued May 17, 2007, p. 54.

to provide the electrical corporation with incentives to improve the efficiency and cost-effectiveness of its fuel and purchased-power procurement activities," not that if no imprudence is found pursuant to the prudence review procedure required by Section 386.266.4(4) RSMo. the sharing mechanism should not be changed. The current 95%/5% sharing mechanism is such a feature the Commission designed to provide GMO with an incentive to improve the efficiency and cost-effectiveness of its fuel and purchased power procurement activities.

Staff believes changing the current 95%/5% sharing mechanism to 85%/15% would better incent GMO to "improve the efficiency and cost-effectiveness of its fuel and purchased-power procurement activities." While GMO dwells on the potential impact based on its past experience—where Staff believes it was inadequately incented—it ignores the potential benefits from the retention of 15% of a decrease in fuel and purchased power costs net of off-system sales revenues (compared to those embedded in base rates) it would get under Staff's proposal, a benefit Staff believes better incents GMO to "improve the efficiency and cost-effectiveness of its fuel and purchased-power procurement activities." Staff believes that changing the sharing mechanism to 85%/15% will give GMO a strong incentive to move from the current negative net off-system sales margins to positive net off-system sales margins in the future and give GMO a strong incentive to reduce its future fuel and purchased power costs.

At the bottom of page 82 of its initial brief GMO cites to Exhibit No. KCPL-8, Bresette Rebuttal at 13-14, as the only record support for its argument regarding GMO's purchases from KCPL during 2011. However, as the Commission will recall, the FAC issue is a "GMO-only" issue – an issue in the GMO case but not in the KCPL case –

and **this particular piece of testimony is not an Exhibit in the record of the GMO case** (ER-2012-0175); it was only an Exhibit in the KCPL case (ER-2012-0174) on the issue of “2011 Missouri River Flooding.” There is no corresponding piece of testimony in the record of the GMO case, thus denying Staff the opportunity to respond to the testimony. Since the cases were only consolidated for hearing but not for evidentiary purposes, this Exhibit cannot be relied upon by GMO in its brief or by the Commission when it decides this case. Furthermore, Bresette Rebuttal in the KCPL case is only four pages in length, and the cite in GMO’s initial brief is to pages 13 and 14; therefore, not only is the testimony not in the record of the GMO rate case, but the testimony does not even support the proposition for which it is cited. Finally, the only piece of testimony in the record of either case which Staff counsel could find and which comes even close to supporting the proposition stated at the bottom of page 82 of GMO’s initial brief is another piece of testimony which is only in the record of the KCPL case – not the GMO case – and which *specifically excludes the Dogwood contract* (*i.e.*, the contract at the centerpiece of Staff’s testimony regarding GMO’s energy purchases from KCPL during the summer of 2011; *see* Staff’s Initial Brief, pages 74-75) from the price calculation which is referenced in GMO’s initial brief. Therefore, there is absolutely no record evidence whatsoever to support GMO’s initial brief argument regarding GMO’s energy purchases from KCPL during 2011.

Although not downright wrong like the bottom of page 82, the discussion on page 83 of GMO’s initial brief regarding GMO’s under-collected amounts related to fuel and purchased power over the past four and a half years could certainly be misleading to the Commission if not read carefully. The $165 million figure referenced by GMO is the amount under-collected during accumulation periods 2 through 10[54], *not* the amount absorbed by GMO pursuant to the FAC sharing mechanism. Of the $165 million amount, GMO was only required to absorb 5%, for a total of approximately $8.3 million over nine accumulation periods, for an average of approximately $919,000 per accumulation period.[55] Considering the average accumulation period total under-collected amount of approximately $18.4 million, Staff believes that the average accumulation period amount of $919,000 for which GMO has been responsible under the current sharing mechanism has proven to be an insufficient incentive for GMO.[56] Had Staff's recommended sharing mechanism been in place during these nine accumulation periods, and had GMO's fuel and purchased power costs net of off-system sales been unchanged despite the change in sharing mechanism, GMO would have been responsible for an average accumulation period amount of approximately $2.8 million rather than $919,000; GMO would thus have had a true incentive to keep its fuel and purchased power costs down, and to minimize fuel and purchased power costs less off-system sales revenues while managing risk of loss of energy supply.[57]

Furthermore, the Commission should keep in mind that with a change in the sharing mechanism, *i.e.*, an increased incentive, there is no reason to believe that GMO cannot do better than it has done in the past (for example, negative off-system sales). As discussed above, GMO's continued focus on how much it would have had to absorb in past periods under Staff's proposal misses the point of an "incentive." If the sharing

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[54] Ex. Staff-259, Staff GMO Cost of Service Report, pp. 269-270.
[55] *Id.* at 269-272.
[56] *Id.* at 272.
[57] *Id.*

mechanism had been set at a level which was truly meaningful to GMO and which gave GMO a real incentive to keep its fuel and purchased power costs down (or to increase its off-system sales), there is no way to know with specificity what GMO's fuel and purchased power costs would have been in the past periods relied upon by GMO.

On page 85 of its initial brief GMO misstates the testimony of Mr. Rush regarding GMO's survey of utilities in other states which GMO conducted, or had conducted, for its prior rate case and introduced as an exhibit in this case. On page 85 of its initial brief GMO claims Mr. Rush testified at the hearing in this case that "nothing had changed since that 2011 survey." However, a review of the transcript reveals that what Mr. Rush actually said was "we're not aware of anything that has changed since that point;"[58] a significant difference from the affirmative statement that "nothing has changed." That Mr. Rush is "not aware" of any change since the survey was conducted for GMO's previous rate case does not mean that nothing has in fact changed; perhaps neither Mr. Rush nor anyone else representing GMO has even checked to see whether anything has or has not changed.

Should both the revenues and the costs associated with Renewable Energy Certificates flow through GMO's FAC?

In this section of its initial brief GMO states that "Assuming that Staff's recommendation is that REC revenue be used to off-set REC costs, GMO agrees to this recommendation." However, as GMO is well aware, this has never (at least in this case) been Staff's recommendation. As stated in Staff's initial brief, its recommendation is that the Commission order GMO's FAC tariff be modified to provide that revenues from the sale of Renewable Energy Certificates ("RECs") which are not needed for

[58] Tr. 802.

GMO to meet the Renewable Energy Standard[59] law ("RES") be flowed through GMO's FAC as an offset to the other costs which are flowed through the FAC.[60] However, costs associated with RECs, if any, should not flow through the FAC for several reason which are discussed in detail in Staff's initial brief.[61]

GMO's initial brief provides no support or analysis whatsoever justifying flowing REC costs through the FAC. Staff's initial brief, on the other hand, provides several reasons why REC revenues, but not REC costs, should flow through GMO's FAC.

Should GMO's FAC tariff be clarified to specify that the only transmission costs included in it are those that GMO incurs for purchased power and off-system sales, excluding the transmission costs related to the Crossroads Energy Center?

As stated in Staff's initial brief, Staff recommends that the Commission order GMO's FAC tariff be modified to specifically state that the only transmission costs included in GMO's FAC are those transmission costs which are necessary for GMO to receive purchased power to serve its native load and transmission costs which are necessary for GMO to make off-system sales that are included in FERC Account Number 565, except for costs related to GMO's Crossroads Energy Center.[62] Staff explained why its recommendation should be adopted on pages 81-82 of its initial brief.

As the Commission is aware, the issue of recovery of Crossroads transmission costs is a separate contested issue in this case; in its initial brief Staff addressed why GMO's revenue requirement should not include transmission costs for energy from

[59] See § 393.1030 RSMo and 4 CSR 240-20.100.
[60] Ex. Staff-259, Staff GMO Cost of Service Report, p. 278.
[61] See Staff's Initial Brief pages 79-81; Ex. Staff-290, GMO Surrebuttal Testimony of Matthew J. Barnes, p. 7.
[62] Ex. Staff-259, Staff GMO Cost of Service Report, p. 279; Ex. Staff-267, Staff GMO Rate Design and Class Cost-of-Service Report, p. 32 and Sch. MJB-2-3; Ex. Staff-290, GMO Surrebuttal Testimony of Matthew J. Barnes, Sch. MJB-1-3.

Crossroads beginning on page 61. The instant issue is a separate issue concerning GMO's FAC, although GMO confuses the two issues in its brief. Rather than argue that Crossroads transmission costs should flow through its FAC, GMO's initial brief on this issue simply reargues why GMO believes it should be allowed to recover Crossroads transmission costs at all – the separate Crossroads transmission cost issue. In fact, GMO's initial brief on this issue states that "GMO does not contend that such costs must be recovered in the FAC." For the reasons set forth in Staff's initial brief, even if the Commission does not adopt Staff's position on the separate Crossroads transmission cost issue, transmission costs related to Crossroads still should not be allowed to flow through GMO's FAC; GMO's initial brief sets forth no reason they should.

Should GMO be ordered to provide or make available the additional information and documents requested by Staff to aid Staff in performing FAC tariff, prudence and true-up reviews?

Near the beginning of this section of its initial brief GMO states that "Staff does not claim that it has encountered any problems in conducting these reviews [*i.e.*, FAC tariff, prudence and true-up reviews]," and then almost immediately thereafter admits that it (GMO) has already been providing such information to Staff. The absence of any documented problems is not surprising given that the information has been provided.

Staff takes issue with GMO's characterization at the top of page 88 of its initial brief that "*Contrary to Staff's implication*, GMO has supplied such information to Staff for the past three years." (Emphasis added). Staff has not implied otherwise; in fact, a review of the transcript reveals that Staff counsel, in his opening statement, stated "that it is my understanding that GMO is already supplying this information or at least most of it. However, since GMO is requesting to continue its FAC, Staff felt it was prudent to request in this case that GMO be ordered to continue to supply this information to Staff."[63] How GMO could claim in its initial brief that Staff implied that GMO was not providing the information is simply beyond understanding. Since GMO admits to already supplying the requested information, it can provide no good reason why it should not be ordered to continue providing the information, and the Commission should so order for the reasons set forth in Staff's initial brief.

<u>Changes to FAC Tariff Sheet Terminology</u>

GMO did not address Staff's recommended changes to the FAC tariff sheet terminology in its initial brief; therefore, Staff will not reargue them here.

Jeff Keevil

TRANSMISSION TRACKERS

<u>Should the Commission authorize KCPL and GMO to compare their actual transmission expenses with the levels used for setting permanent rates in these cases, and to accrue and defer the difference for potential recovery in future rate cases, i.e., to employ a "tracker"?</u>

KCPL's statement in its Initial Brief that Staff supported a Transmission Tracker in the last KCPL and GMO rate cases, Case Nos. ER-2010-0355 and ER-2010-0356, is highly misleading. In those cases Staff supported a transmission expense **and revenue** tracker.[64] As discussed in the Surrebuttal Testimony of Daniel Beck in these cases, Case Nos. ER-2012-0174 and ER-2012-0175, the Staff witness who made the recommendation in support of a transmission expense and revenue tracker in Case Nos. ER-2010-0355 and ER-2010-0356, KCPL and GMO's situations regarding transmission expense and revenues have changed since the time Staff made that

[63] Tr. 781.
[64] Exhibit KCPL-59 at 150; Exhibit GMO-145 at 161.

recommendation. The development and implementation of the SPP Day-Ahead market and the pursuit by GPE of non-regulated transmission ownership are important factors in Staff's decision to no longer recommend a transmission expense and revenue tracker.

That the term "Transmission Tracker" is a misnomer becomes evident upon review of KCPL's brief. KCPL and GMO are requesting tracking of the expense of belonging to the SPP. Nothing more, and nothing less. Therefore, it would appear that reference to an SPP Expense Tracker would be less confusing, although at this late date it would likely be more confusing to change the referenced term. Staff does not raise this point as an idle aside however. KCPL's attempt in its Initial Brief to frame the issue as expenses it incurs to put electrons on KCPL and GMO's wires for their customers is simply inaccurate, and it is important to consider the nature of the implicated expenses and revenues when considering authorization of any extraordinary accounting treatment, such as the requested tracker or Staff's attempt to lessen the harm implicit in the tracker's design through the application of conditions.

KCPL's Initial Brief attempts to obfuscate the fact that the companies are recovering a level of SPP expenses through their base rates, and no party is attempting to adjust those expenses out of base recovery. KCPL's Initial Brief also conflates a right to recovery in base rates with a right to authorization of extraordinary accounting authority. Simply put, a tracker is a preemptive accounting authority order. The Initial Briefs of various parties discussed the previously-applied Commission criteria for implementation of trackers, so Staff will not recite those criteria here. However, Staff will raise the simple fact that if KCPL's projections outlined in its Initial Brief as to the costs it and GMO will be charged by the SPP do pan out, KCPL is highly capable of filing requests for an Accounting Authority Order for itself and GMO, as it has done many times.

KCPL's conflation of a right to recovery with a right to authorization of extraordinary accounting authority is most evident in its discussion of Staff's fourth condition. Staff's fourth condition is:

> That KCPL must impute into its tracker mechanism, the level of transmission revenues earned by any transmission company affiliate related to facilities in KCPL's Missouri jurisdictional service territory into its tracker mechanism to the extent necessary to ensure that no additional revenue requirement resulting from any decision by Great Plains Energy, Inc. (GPE) to transfer responsibility for transmission construction activity from KCPL's regulated business is passed on to KCPL's Missouri retail customers through the tracker.

KCPL and GMO have no right to extraordinary accounting authority regarding SPP expense. If the utilities want that authority, the Commission may condition its grant. Accordingly, while the Commission cannot disallow lawful costs approved by the FERC, the Commission is under no compulsion to provide extraordinary ratemaking treatment for those costs, as requested by KCPL and GMO in the form of the requested transmission tracker. In *Arkansas Power & Light Company v Missouri Public Service Commission*, 829 F2d 1444, the United States Court of Appeals, Eighth Circuit, decided that a Missouri-regulated utility had no right under Federal Preemption to an immediate rate increase to reflect an increase in a FERC-regulated expense. The court held that "the ordinary state-law process of suspension and investigation is not preempted, under the circumstances of this case, by the Federal Power Act." That case involved costs that were unexpectedly assessed to Arkansas Power & Light, which are unlike the ostensibly predictable costs detailed in the charts provided in KCPL and GMO's testimonies and briefs.

Simply put, regarding the requested transmission expense-only tracker, KCPL and GMO do not have to accept Commission conditions they do not like – they can simply not accept the conditioned tracker. The utilities do not have to accept a conditioned expense and revenues tracker – and they have no right to an unconditioned expense-only tracker.

Also regarding Staff's fourth condition, KCPL's argument at page 54 mischaracterizes Staff's condition. Staff's fourth condition is intended to apply only to transmission facilities owned by a KCPL or GMO affiliate that are physically located in KCPL's or GMO's service territories. The intent of Staff's fourth condition to guard against potential detriment associated with transfer of jurisdiction from Missouri to FERC for projects constructed in KCPL's or GMO's service territories by a GPE transmission affiliate. It is not intended to impute the profits earned by that affiliate into KCPL or GMO's revenue requirement.[65]

The absurdity of KCPL's position on Staff's first condition is self-evident in KCPL's argument against it. Staff's first condition is:

> That the tracker reflects both transmission revenues and expenses, and thereby operate as a two-way mechanism (i.e., tracking both under and over collections of net transmission costs).

KCPL argues that KCPL and GMO bear cost responsibility for only 12% of SPP-regionally allocated costs. KCPL then argues that because KCPL and GMO only bear responsibility for 12% of those costs, that the companies should retain 100% of associated revenues. The theory underpinning KCPL and GMO's request for the

[65] Trans v 18 pp. 733-4.

tracker in the first place is that SPP costs are escalating and are out of their control. KCPL's response is that the companies should get to hold onto the revenues that are similarly escalating and are not related to costs incurred by KCPL and GMO. The "mismatch" here that KCPL alleges in Staff's first condition is the purpose for the condition, not an unintended defect. KCPL and GMO expect to see increases in SPP revenues. To the extent KCPL and GMO want the extraordinary accounting authority to track increases in their SPP expenses, it is imperative to track the similar revenues.

At pages 52 – 53 of its Initial Brief, KCPL makes a claim that there is "mismatch" if all SPP transmission revenues are included in the tracker. However, the essence of a tracker is to provide accounting authority to allow a utility to deviate from a strict application of the matching principle. Staff's condition mitigates the mismatch that KCPL and GMO have requested – that mismatch that is requested being to capture SPP expenses incurred after this case and charge them to ratepayers in a future case. Staff's first condition is appropriate because it is proper in the context of a transmission tracker to require inclusion of all SPP related transmission expenses and all SPP related transmission revenues, as you need to incorporate both to calculate an accurate revenue requirement associated with SPP membership.[66]

Finally, because KCPL currently does not produce any quarterly FAC surveillance reports, Staff is willing to discuss with KCPL the possibility of modifying their current surveillance reporting process to allow for the quarterly reporting that would be required under Staff's Sixth Condition.[67] Staff agrees that adoption of its sixth condition would not result in a perfect measurement of KCPL's or GMO's actual ongoing

[66] Ex. Staff 252, Surrebuttal Testimony of Mark Oligschlaeger, pp. 8 - 9; Ex. Staff 3008, Surrebuttal Testimony of Mark Oligschlaeger, p. 5.
[67] Trans v 18 p. 736.

earnings for purposes of “turning on/turning off” tracker deferrals. But, imposition of Staff’s suggested condition is superior to not attempting to measure KCPL’s ongoing earnings at all, and allowing it to book under or over recoveries of net transmission expenses without any concern as to whether KCPL is earning above or below its overall ROE. Conditioning a grant of the extraordinary accounting authority of a tracker mechanism on a reasonable limitation of KCPL’s and GMO’s ability to book tracker deferrals irrespective of its actual earnings is appropriate, given that the Commission is not required to allow the Companies to use a tracker mechanism at all and that tracking authority is extraordinary accounting authority, even for costs under FERC jurisdiction.[68] Staff does not concur in other arguments raised by KCPL in its Initial Brief, but Staff’s argument is adequately presented in its Initial Brief and those of other parties.

Sarah Kliethermes

CONCLUSION

WHEREFORE, Staff continues to request the Commission to adopt the Staff’s position on each and every issue before the Commission in these cases.

[68] *Arkansas Power & Light Company v Missouri Public Service Commission*, 829 F2d 1444

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 electronic mail to all counsel of record this 11th day of December, 2012.

/s/ Nathan Williams