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Witness: Chris B. Giles
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Sponsoring Party: Kansas City Power & Light Company
Case No.: ER-2006-____
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MISSOURI PUBLIC SERVICE COMMISSION

CASE NO. ER-2006-____

DIRECT TESTIMONY

OF

CHRIS B. GILES

ON BEHALF OF

KANSAS CITY POWER & LIGHT COMPANY

Kansas City, Missouri
January 2006

"[redacted]**" Designates that "Proprietary" Information has been Removed Pursuant to the Standard Protective Order.**

DIRECT TESTIMONY

OF

CHRIS B. GILES

CASE NO. ER-2006-____

Q: Please state your name and business address.

A: My name is Chris B. Giles. My business address is 1201 Walnut, Kansas City, Missouri 64106-2124.

Q: By whom and in what capacity are you employed?

A: I am employed by Kansas City Power & Light Company ("KCPL") as Vice President, Regulatory Affairs.

Q: What are your responsibilities?

A: My responsibilities include all aspects of regulatory activities including cost of service, rate design, revenue requirements, and tariff administration.

Q: Please describe your education, experience and employment history.

A: I graduated from the University of Missouri at Kansas City in 1974 with a Bachelor of Arts degree in Economics and in 1981 with a Master of Business Administration degree with concentrations in accounting and quantitative analysis. I was first employed at KCPL in 1975 as an Economic Research Analyst in the Rates and Regulation Department. I held positions as supervisor and manager of various rate functions until 1988 when I was promoted to Director of Marketing. In January 1993, I returned to the rate area as Director, Regulatory Affairs. In March of 2005, I was promoted to Vice President, Regulatory Affairs.

Q: Have you previously testified in a proceeding at the Missouri Public Service Commission ("MPSC") or before any other utility regulatory agency?

A: I have previously testified before both the MPSC and the Kansas Corporation Commission ("KCC") on numerous issues regarding utility rates and regulation.

Q: What is the purpose of your testimony?

A: The purpose of my testimony is to provide a summary and overview of this case. I will do so by describing the background leading up to the Stipulation and Agreement concerning KCPL's Regulatory Plan, which the MPSC approved in Case No. EO-2005-0329 ("Regulatory Plan Stipulation and Agreement"), identify the planned investment, provide a description of the rate cases associated with implementation of and completion of the investments set out in the Regulatory Plan Stipulation and Agreement, explain the status of those investments, describe the major drivers of and how the proposed rate increase was determined. As part of my testimony, I will also identify Company witnesses that will provide additional support and detail regarding this summary and overview. A list of topics and supporting witnesses is contained in the direct testimony of KCPL witness Don A. Frerking as Schedule DAF-3.

Q: Please provide background leading up to the Regulatory Plan Stipulation and Agreement?

A: On May 6, 2004, KCPL filed in Case No. EO-2004-0577 its "Application To Establish Investigatory Docket And Workshop Process Regarding Kansas City Power & Light Company." In its Application, KCPL requested that the MPSC issue an Order (a) opening an investigatory docket regarding the future supply and pricing of the electric service provided by KCPL; and (b) authorizing the use of the MPSC's workshop process to address certain issues related to the future supply and pricing of electricity for KCPL and its customers, and any other issues impacting KCPL that may arise from discussion among the interested participants.

Q: How did the MPSC respond?

A: On May 25, 2004, the MPSC issued an Order Directing Notice And Setting Intervention Deadline in Case No. EO-2004-0577.

Q: Did other parties file applications for intervention?

A: Yes. The Missouri Department of Natural Resources ("MDNR"); Aquila, Inc. ("Aquila"); The Empire Electric District Company ("Empire"); the City of Kansas City, Missouri; the Concerned Citizens of Platte County; Praxair, Inc.; the Missouri Industrial Energy Customers; and the Missouri Joint Municipal Electric Utility Commission ("MJMEUC") filed applications to intervene in Case No. EO-2004-0577. Subsequently, the Missouri Energy Group, the Sierra Club, Union Electric Company, d/b/a AmerenUE, and Jackson County, Missouri participated in the workshops conducted in Case No. EW-2004-0596, which is discussed below.

Q: What action did the MPSC take?

A: On June 3, 2004, the MPSC issued an Order Establishing Case, which granted KCPL's Application to Establish Investigatory Docket and Workshop Process Regarding Kansas City Power & Light Company, and established an informal, investigatory proceeding designated as Case No. EW-2004-0596. In the June 9, 2004 Notice of Participants, the MPSC made the parties who intervened in Case No. EO-2004-0577 participants in Case No. EW-2004-0596. On July 1, 2004, the MPSC issued its Notice Closing Case in Case No. EO-2004-0577, which formally closed that proceeding.

Q: How did Case No. EW-2004-0596 proceed?

A: A prehearing conference was held in Case No. EW-2004-0596 on June 30, 2004. A series of presentations and workshops were held on June 21, June 30, July 21, July 30, August 10-11, August 19, August 24-26, September 7, September 15, September 29, and October 29, 2004. During this period KCPL conducted numerous informal meetings with interested groups and individuals to discuss the many issues raised by this proceeding.

Q: How was the workshop organized?

A: The workshop was organized into two teams. Team A reviewed issues concerning Integrated Resource Planning, including load forecasting, generation planning, demand side management, environmental issues, and distribution and transmission technologies. A sub-team within Team A reviewed affordability, efficiency, and demand response programs. Team B reviewed the financial issues associated with KCPL's various plans, including maintaining KCPL's current investment grade credit rating. Representatives from KCPL and the MPSC staff ("Staff") led these Teams jointly. Meetings also occurred on dates subsequent to October 29, 2004. On January 18, 2005, the MPSC held an on-the-record conference. On February 18, 2005, the MPSC issued its Order Closing Case in Case No. EW-2004-0596.

Q: Why was this collaborative workshop process necessary?

A: The issues presented by KCPL in this proceeding included the following:

1. The need for additional generating capacity in the KCPL service territory;
2. The mix of new generation investments that would result in a reliable and cost efficient service for Missouri customers;

3. The desirability of proactively addressing environmental concerns with respect to new generation and existing generating facilities;

4. Investment in a highly reliable transmission and distribution infrastructure;

5. Establishment of customer efficiency and affordability programs and development of new technologies and applications for demand response programs; and

6. Adoption of a regulatory plan that would adequately address the comprehensive undertakings being considered by KCPL, and will recognize the importance of timely cost recovery and the financial considerations of such significant investments.

KCPL believed that the informal workshop process utilized by the MPSC in the past would be well suited to the consideration of the wide range of issues necessary for the development of KCPL's Regulatory Plan. KCPL also believed that conducting these discussions in the context of informal MPSC workshops would give all stakeholders the opportunity to agree upon a regulatory plan that addressed these dynamic issues on a prospective basis for KCPL. That plan would then be presented to the MPSC for its consideration and approval.

Q: How did KCPL solicit this input?

A: Throughout 2004, KCPL conducted numerous workshops, public forums, and strategic planning seminars, involving employees, customers, energy experts, financial experts, the general public, consumer groups, manufacturers, industrial and trade groups, environmental organizations, and other utility companies, as well as government and community leaders to solicit comment regarding its planning process. Meetings with the

Staff, the Missouri Office of Public Counsel ("OPC"), and other parties to the workshop docket were also conducted at which KCPL made presentations and answered questions.

Q: How does this collaborative approach compare to the traditional process used by utilities to undertake major initiatives?

A: Traditionally, utilities conducted their planning and project work in a "near vacuum." The utility would conduct its studies, determine the best alternative, secure financing, seek approvals where necessary, and at the end of the project seek approval to adjust rates as necessary to recognize major investments.

Q: Why did KCPL choose not to use the traditional model?

A: The traditional model often focuses upon historic information rather than looking forward five to ten years--something a utility must now do to plan and develop a strategy to continue to provide reliable reasonably priced service for its customers. In addition, the traditional model does not provide a convenient forum for informally discussing different perspectives on public utility issues, and as a result, it does not take advantage of the "collective wisdom" of other parties. KCPL believed that the traditional model was therefore not the best approach for developing and implementing a comprehensive, multi-year regulatory plan when a more collaborative, informal approach was available.

Q: Please explain.

A: In the traditional model, the utility does not spend much if any effort to gain acceptance from the interested parties for its plan. While this can save time at the beginning of the process, it can lead to contentious and time-consuming disputes concerning the prudence of its decisions after the investments are made. The public utility must defend its actions and runs the risk that it will not be awarded full recovery of its investments.

Q: Why were these issues of particular concern to KCPL?

A: KCPL recognized that during the planning horizon, it would require additional generation to meet the needs of its customers. KCPL also believed that the construction of a base load coal plant was necessary. At the same time, environmental concerns needed to be addressed along with investments in distribution assets to maintain reliability, and customer programs for managing electricity use. In order to meet these needs, KCPL needed a plan that would facilitate attracting capital at a low cost. Investors needed some assurance that KCPL would be allowed to recover its investment, and continue to be an attractive component of the investors' investment portfolio. KCPL needed a plan that the parties could agree to in order to reduce risk and move ahead with implementation of a collaborative strategy. For these reasons, KCPL chose to pursue the collaborative approach described earlier.

Q: What are the key benefits to be realized with the implementation of the plan outlined in the Regulatory Plan Stipulation and Agreement?

A: The key benefits are as follows:

1. KCPL can meet the growing demand in its service area for years to come;
2. KCPL will meet this need and avoid increasing its reliance on high cost and volatile natural gas as a fuel source, providing less volatile and more predictable long-term rates;
3. The environmental investments included in the plan will substantially reduce emissions from KCPL's fossil fuel fleet, even with the addition of a new, efficient coal unit at the Iatan plant site;
4. KCPL will add renewable wind energy to its generation portfolio;

5. Customers will be offered a broad set of customer-focused demand response, efficiency and affordability programs;

6. KCPL will maintain top-tier reliability for its customers;

7. Temporary and permanent jobs will be created in the Kansas City metropolitan area; and

8. KCPL will have regulatory authority to support the investment plan and will be able to maintain key credit ratios through future rate increases and the treatment of certain revenue and expense items, including the cost of fuel and purchased power.

Q: Please describe the key investments set out in the Regulatory Plan.

A: KCPL has committed to investing over $1.3 billion over the course of the Regulatory Plan. This investment includes the completion or substantial progress on the following projects:

- 800-900 MW of new coal-fired generation capacity, Iatan Unit 2, located at the Iatan site near Weston, Missouri, of which KCPL will own approximately 500 MW. This will be regulated generation capacity excepting that interest that may be owned by a municipality or joint municipal utility commission.
- Environmental investments related to Iatan Unit 1 and LaCygne Unit 1 for accelerated compliance with environmental regulations; the Iatan Unit 1 and LaCygne Unit 1 environmental equipment will provide significant reductions in site emissions of sulfur dioxide ("SO_2"), nitrous oxides ("NOx"), particulate matter and mercury, and will pre-position the units to meet compliance requirements set forth in the Clean Air Interstate Rule, which was recently

promulgated by the U.S. Environmental Protection Agency ("EPA"). With the addition of Iatan Unit 2 at this site, the environmental upgrades on Iatan Unit 1 will ensure that total site emissions after completion of Iatan Unit 2 will be less than the current site emissions from Iatan Unit 1 and will help address the environmental concerns of citizens living in the area around the Iatan plant site. In addition, the early installation of a selective catalytic reduction ("SCR") facility at LaCygne Unit 1 is designed to help maintain attainment of the 8-Hour Ozone standard within the metropolitan Kansas City region. Installation of this SCR before the 2007 Ozone season is considered a significant component of the region's proposed Ozone mitigation plan by the Mid-America Regional Council, regional EPA officials, Kansas Department of Health & Environment and MDNR. With respect to any of the expenditures anticipated for environmental compliance, KCPL will continue to assess the environmental laws to ensure that its expenditures will comply with existing or expected environmental regulations.

- 100 MW of new wind generation facilities to be installed in 2006. An additional 100 MW of new wind generation facilities will be installed in 2008 if a detailed evaluation (made with input from interested parties to the Regulatory Plan Stipulation and Agreement ("Signatory Parties") supports such an action to proceed with its construction. KCPL's detailed evaluation will include Missouri-specific wind assessment information. As discussed in the direct testimony of KCPL witness John Grimwade, KCPL is participating in a Missouri wind study being undertaken by MDNR and the University of Missouri – Columbia. The detailed evaluation will utilize the wind assessment information (and other

Missouri-specific information, if available) to analyze the cost effectiveness of wind generation in Missouri before installing the second 100 MW of wind generation in any state other than Missouri. The initial report analyzing the first 12 months of Missouri wind assessment data will be completed by March 31, 2007. The final report analyzing the first 18 to 21 months of data will be completed by December 31, 2007.

- KCPL has committed to implement a number of customer programs including demand response, efficiency and affordability programs throughout the period of the Regulatory Plan. The initially budgeted expenditures for the five (5) year period for Missouri are $13.8 million for Demand Response Programs, $2.5 million for Affordability Programs, and $12.7 million for Efficiency Programs.
- KCPL will make investments totaling $42.4 million over the period of the Regulatory Plan in transmission and distribution infrastructure to ensure a highly reliable transmission and distribution system.

Q: Please describe the rate cases contemplated to be filed in the Regulatory Plan Stipulation and Agreement.

A: KCPL committed to file rate schedules on February 1, 2006 with an effective date of January 1, 2007 ("2006 Rate Case"). This case fulfills the commitment to file the first of four potential rate cases related to the Regulatory Plan. This 2006 Rate Case includes estimated expenditures related to 100 megawatts of wind generation, and the additions to transmission and distribution infrastructure as set out in the Regulatory Plan that are planned to be in service prior to the agreed upon true-up date of the rates approved in this case. The 2006 Rate Case, as filed, does not include any amortization expense, related to KCPL's credit ratio metrics, although the Regulatory Plan Stipulation and Agreement contemplates that KCPL could have proposed up to $17 million of such amortization on a Missouri jurisdictional basis, and additional amount in subsequent rate cases during the period of implementing the Regulatory Plan. I will explain the basis for such potential amortization amounts later in my testimony. The 2006 Rate Case also includes an amortization of $ 348,668 related to the Demand Response, Efficiency and Affordability Programs, as set out in the Regulatory Plan Stipulation and Agreement.

Q: Did KCPL file a Class Cost of Service Study in this 2006 Rate Case?

A: Yes. KCPL agreed that the 2006 Rate Case would include the filing of a Class Cost of Service Study. This filing contains both a Missouri jurisdictional revenue requirement cost of service study and a Missouri jurisdictional customer class cost of service study covering the twelve (12) months ended September 30, 2005. The class cost of service study and rate design is discussed in the direct testimony of KCPL witness Tim M. Rush.

Q: What other rate case filings are anticipated?

A: Over the course of the Regulatory Plan, four rate cases may be filed, however, only two are mandatory: (1) This case, the 2006 Rate Case, and (2) the 2009 Rate Case. The other two rate cases are optional. If KCPL chooses to file the second rate case, rate schedules with an effective date of January 1, 2008 will be filed with the MPSC on February 1, 2007. This 2007 Rate Case will include prudent expenditures for the installation of an SCR facility at LaCygne Unit 1, and the additions to transmission and distribution infrastructure as set out in the Regulatory Plan Stipulation and Agreement that are in service prior to the agreed upon true-up date. The 2007 Rate Case will include an amortization expense that is expected to be $17 million on a Missouri jurisdictional basis, as may be adjusted upward or downward. The 2007 Rate Case will also include the amortization related to the Demand Response, Efficiency and Affordability Programs, as more fully described in the Regulatory Plan Stipulation and Agreement.

Q: If KCPL chooses to file the third rate case, when would that happen?

A: If KCPL chooses to file the third rate case, then rate schedules with an effective date of January 1, 2009 will be filed with the MPSC on February 1, 2008. This 2008 Rate Case will include prudent expenditures for the installation of an SCR facility, a Flue Gas Desulphurization ("FGD") unit and a Baghouse at Iatan Unit 1; possibly 100 MW of wind generation; and the additions to transmission and distribution infrastructure as set out in the Regulatory Plan Stipulation and Agreement that are in service prior to the agreed upon true-up date. The 2008 Rate Case will include an amortization expense expected to be $17 million on a Missouri jurisdiction basis, as may be adjusted upward or downward. The 2008 Rate Case will also include the amortization related to the Demand Response, Efficiency and Affordability Programs, as more fully described in the Regulatory Plan Stipulation and Agreement.

Q: When would the fourth mandatory rate case be filed?

A: Rate schedules with an effective date of September 1, 2010, will be filed with the MPSC on October 1, 2009, or eight (8) months prior to the commercial in-service operation date of Iatan Unit 2. This 2009 Rate Case will include prudent expenditures for Iatan Unit 2; the FGD unit and the Baghouse at LaCygne Unit 1; and the additions to transmission and distribution infrastructure as set out in the Regulatory Plan Stipulation and Agreement. The 2009 Rate Case will also include the amortization related to the Demand Response, Efficiency and Affordability Programs, as more fully described in the Regulatory Plan Stipulation and Agreement.

Q: Please describe the status of the investments in power supply infrastructure.

A: KCPL has executed a contract with enXco, Inc. ("enXco"), a leading developer of wind generation, to construct, operate and maintain approximately 100 MW of wind generation at a site near Spearville, Kansas. enXco will operate and maintain the wind generation for a period of five years. enXco will utilize General Electric wind turbines. Construction is expected to begin in February of 2006.

A contract has been executed with Babcock and Wilcox to engineer, procure, and construct the SCR at the LaCygne Unit 1 generating plant. The SCR is scheduled to be in operation prior to the summer of 2007.

Burns and McDonald, a local engineering firm recognized worldwide, is the owner's engineer for the Iatan Unit 2 project. Bid packages for the turbine and boiler were released in the fall of 2005 and bids are due to be received in February and March 2006, respectively. John Grimwade, Senior Director, Construction, is managing the generation infrastructure projects. Additional information is contained in his direct testimony in this case.

Q: Please describe the status of securing partners for the Iatan Unit 2 generation plant.

A: Although final agreement on contract language is not yet complete, KCPL does not believe that any substantive issues exist with potential partners. The partners in the project and their respective ownership shares, based upon a total of 850 MW, are as follows: KCPL - 465 MW, Empire - 102 MW, Aquila – 153 MW, MJMEUC – 100 MW, and Kansas Electric Power Cooperative – 30 MW. These ownership shares may change slightly depending on the ultimate size of the plant; however, pursuant to the Regulatory Plan Stipulation and Agreement, Aquila and Empire will be given the opportunity to own 30% of the total jointly and MJMEUC will be given the opportunity to own 100 MW.

Q: Please describe the status of the transmission and distribution infrastructure investments.

A: The Regulatory Plan Stipulation and Agreement was approved in the summer of 2005. Since that time, KCPL's transmission and distribution engineers have conducted a pilot program to assess the overhead distribution system and developed a plan of work. In addition, a full distribution system assessment is scheduled to be completed by the end of the year 2008. Similarly, a plan of work for the transmission system and for distribution automation has been completed. The objectives of the asset management and distribution automation infrastructure investments include the following: 1) to mitigate risks of major outage events to customers, 2) to minimize the System Average Interruption Duration Index ("SAIDI"), and 3) to minimize the number of customers with multiple interruptions; each objective to be met at the most optimal cost. A detailed description of the status and scope of work for asset management and distribution automation is contained in the direct testimony of KCPL witness John R. Marshall. In addition, past performance metrics, strategic objectives, and initiatives for Delivery are included in the Delivery Business Plan attached to his testimony.

Q: Please describe the status of customer programs.

A. The Regulatory Plan Stipulation and Agreement established an advisory group, Customer Programs Advisory Group ("CPAG"), consisting of representatives of signatories to the Agreement. CPAG had two key objectives: perform pre-implementation evaluation of energy efficiency programs, and review program design, implementation and evaluation plans for all programs. It is not a governmental body and makes no recommendations on government policy. CPAG met on several occasions and, as a result, tariffs have been filed and approved by the MPSC for some programs. Other programs have tariffs filed and are in final review by the Staff, and yet others are soon to be filed. A more detailed description of the status of customer programs is contained in the direct testimony of KCPL witness Susan K. Nathan.

Q: How long has it been since KCPL requested a rate increase?

A: It has been twenty years since KCPL last filed a request to increase rates. The last rate increase resulting from that case became effective in 1988. Four rate decreases, in the years 1991, 1994, 1996/1997, and 1999 have been implemented since the last increase. Each of these decreases resulted from stipulation and agreements with the Staff, OPC and other parties. The MPSC approved each agreement.

Q: Please describe in general terms the conditions that led to increases or decreases or lack of change in rates during the period 1988 through 2005.

A: The increase in the year 1988 was the last increase related to placing the Wolf Creek generation plant into rate base. Subsequent to the filing of the last rate increase request, interest rates declined from historic high levels during the construction of and at the time Wolf Creek was placed into rate base. In addition, tax law revisions in 1987 reduced the corporate income tax rate. Depreciation of the investment in the Wolf Creek generation plant offset, to a large extent, additions to rate base from on-going capitalized maintenance and new infrastructure investments. Also, fuel costs were beginning to stabilize and actually declined in cents per mmbtu during the late 1980s and early 1990s.

The combination of these conditions has acted to offset other cost increases and has led to stable or declining electricity prices. Within two months of the Stipulation and Agreement to reduce rates in 1999, and before the MPSC had actually approved the Agreement, a boiler explosion occurred at the Hawthorn Unit 5 generating plant. The plant was out of service for about two and one half years to rebuild the boiler and other facilities destroyed during the explosion. During this outage, additional environmental equipment consisting of a scrubber, bag-house, and SCR were installed at Hawthorn Unit 5.

Q: Did KCPL file for a rate increase as a result of the Hawthorn Unit 5 boiler explosion, and related two and one half year outage?

A: No, even though KCPL had to purchase replacement power, occasionally at exorbitant prices during this 1999-2002 period, the Company did not request a rate increase. As a consequence, earnings were reduced during the period of the outage.

Q: Why didn't the Company request an increase to recover the costs of replacement power during the outage of Hawthorn Unit 5?

A: KCPL agreed to a moratorium on rate changes in the 1999 Stipulation and Agreement for a period of two years. Although, the Agreement providing the moratorium could be waived for major changes in circumstance such as a two and one half year plant outage, KCPL believed it was important to demonstrate its commitment to achieve the rate reduction that it had negotiated in good faith, and chose not to reopen those discussions or subsequently file a rate increase request during the moratorium.

Q: Why did KCPL choose not to request a rate increase after the moratorium expired?

A: Beginning in late 2002, after Hawthorn Unit 5 returned to service, and continuing through 2005, KCPL has been able to utilize its generation assets to sell power to other utilities or marketers (off-system sales) primarily from its base-load coal units during those hours not required to serve retail customer load. The margin (revenue less fuel and variable cost) on these sales has increased during the last three years, and the volume of sales has increased over that same time frame. The margin or profit from these sales has offset the cost increases in other areas of the business during this period, and permitted KCPL to meet its revenue requirement, despite increases in rate base from capitalized maintenance and infrastructure investments. In addition, KCPL has reduced costs in other areas as it strives to either reach or maintain an efficiency ranking within the top 25% of benchmarked utility companies. Based on the budget for 2007, the first year rates from this case would be in effect, the off-system sales margin is expected to result in nearly **[redacted]** of KCPL's total earnings and return on equity. The magnitude of the profit from a volatile, competitive, off-system sales market compared with the amount of profit from off-system sales at the last time KCPL filed a request for a rate increase or even since the last rate decrease in 1999, compels the MPSC and all parties to this case to examine and take account of the participation in this new profit market, in terms of the benefits as well as the additional risks, for customers and shareholders. One simply cannot compare utilities with nearly **[redacted]** of earnings from an unregulated volatile market with utilities having 90% to 100% of earnings source from retail customers whose prices are regulated, using the same return on equity or cost of capital metrics. I will discuss this further later in my testimony.

Q: Hasn't KCPL always had the opportunity to sell power not required for retail load into the off-system sales market?

A: Yes. However, until the wholesale power market was deregulated as a result of the Energy Policy Act of 1992, utilities could only sell into this market at cost plus ten percent. Beginning in the late 1990s, activity in regional wholesale power market increased dramatically and power was sold at market clearing prices where the prices were generally determined by market forces. KCPL was limited in its opportunity to participate in this unregulated off-system sales market until the return to service of its Hawthorn Unit 5 generating plant. Since that time KCPL has focused on selling every MWh it can generate to other utilities or marketers in the off-system sales market when the price it can charge is greater than the variable cost of generating the MWh. This strategy benefited and continues to benefit customers. For example, during the period following the return of Hawthorn Unit 5 to service, the off-system sales margin largely covered the cost increases related to on-going operations and revenue requirement related to capitalized maintenance and infrastructure investments. KCPL was able to forego rate increase requests as a result of the off-system sale activity. The Company also benefited to the extent that the off-system sales market provided additional opportunities for increased earnings. KCPL has continued to squeeze the gap between capacity factor (the total amount of power that the capacity would allow to be generated from the plant compared to how much is actually generated) and availability factor of its base-load coal units as a result of this market. Operations and maintenance personnel and management of the Company continue to focus on maintaining the availability of the base-load coal fleet as high as possible without negatively impacting the life of the equipment or length of potential outages. Detailed production operations objectives, past performance, and strategic initiatives are contained in the Supply Business Plan attached to the direct testimony of KCPL witness Dana Crawford.

Q: Has KCPL added additional generation capacity in the past ten years?

A: Yes, KCPL added Hawthorn Unit 6, a Siemens gas turbine and Siemens air-cooled generator in May 1997. In July 2000, a heat recovery steam generator ("HRSG"), and a re-powered steam turbine with supplemental natural gas duct firing were added and combined with Hawthorn Unit 6. The combination is identified as Hawthorn Unit 6/9. In fired conditions, *i.e.*, combined-cycle with supplemental duct firing, Unit 6 is rated at 132 MW, and Unit 9, 137 MW. Hawthorn Units 7 and 8 were installed in May 2000. Each unit is rated 77 MW at peak capacity. Hawthorn Unit 5 was rebuilt after the boiler explosion, and was placed back into service in June 2001. The current capacity of the unit is 565 MW. West Gardner Units 1 through 4 are simple cycle combustion turbines that were added in May 2003. Each unit is rated 77 MW at peak capacity. Osawatomie Unit 1, a simple cycle gas-fired turbine was added in June 2003. The unit is rated 77 MW at peak capacity. KCPL has added over 800 MW of gas-fired peaking capacity and an additional 75 MW of coal capacity without a rate increase. Additional detail regarding these additions, and in-service criteria is contained in the direct testimony of Dana Crawford.

Q: How was the rate case test year data and resultant rate increase amount determined?

A: Pursuant to the Regulatory Plan Stipulation and Agreement, the test year is 2005, updated through June 2006, and trued-up through September 2006. Nine (9) months actual and three (3) months projected data were used for calendar year 2005. The data were restated to a Missouri jurisdictional basis, annualized, and normalized, as appropriate. The rate case data are then, adjusted to projected month-end September 2006, and allocated between FERC, Missouri and Kansas jurisdictions. The production allocation was made on the basis of twelve coincident monthly peaks (12 CP). A list of adjustments and witnesses sponsoring those adjustments is contained in Schedule DAF- 3, which is attached to the direct testimony of KCPL witness Don A. Frerking. The cost of service and revenue requirement determination is contained in Schedule DAF-1 and is supported by the direct testimony of KCPL witness Don A. Frerking.

Q: What is the amount of rate increase requested in this case?

A: The amount of the rate increase is approximately 11.5% or $55.8 million dollars based on test year revenue of approximately $487 million.

Q: Does this amount include amortization expense to meet credit ratios?

A: The amortization required to meet credit ratios in this case is zero ($0) and is described in detail in the direct testimony of Michael Cline.

Q: Do the additional amortization provisions in the Regulatory Plan Stipulation and Agreement in any way limit the ability of the Signatory Parties to recommend a specific capital structure or rate of return for ratemaking purposes?

A: No, it does not. The agreement allows the Signatory Parties to propose a return on equity and capital structure in rate cases utilized to determine rates. Although KCPL is not seeking any amortization in this case to help KCPL meet the credit ratio metrics, any such amortization would result in an offset to rate base under the Regulatory Plan

Stipulation and Agreement, which would result in lower rates, attributable to the amortization offset to rate base, in future rate proceedings of KCPL.

Q: What is the return on equity KCPL is requesting in this case?

A: KCPL is requesting a minimum return on equity of 11.5% based upon the 53.81% equity capital structure of KCPL's parent holding company Great Plains Energy, Inc. ("GPE").

Q: What is the basis of an 11.5% return on equity?

A: The rate of return recommendation of 11.5% accounts for the baseline cost of equity capital, and recognizes investor risks associated with construction. An authorized rate of return of 11.5% on common equity is the minimum level appropriate, when combined with sharing of off-system sales risk, as discussed later in my testimony. KCPL witness Samuel Hadaway presents his cost of capital study results and recommendations in support of an 11.5% rate of return. Dr. Hadaway has utilized a traditional approach to estimate the underlying cost of equity capital for a group of electric utility companies. However, the utility companies used for comparison by Dr. Hadaway, have, in total, significantly smaller construction activity than KCPL. Consequently, the traditional approach and sample does not fully account for KCPL's higher investment risks, as perceived by investors currently, in the cost of capital estimate. Dr. Hadaway indicates that the risk premium associated with KCPL's high level of construction increase the cost of capital to the Company by about 50 basis points.

Q: What other factors support an 11.5% return on equity?

A: A return level greater than the baseline 11.0% is also justified by KCPL's utility performance, which has added substantial value to customers. Over a number of years, KCPL has provided retail customers with a very high level of utility performance. The

Company's performance has been subjected to an independent benchmarking study and review, as conducted by Christensen Associates Energy Consulting ("CA Energy Consulting"). KCPL witness Robert J. Camfield of CA Energy Consulting reviews the study of KCPL performance, and suggests ample evidence exists to support a performance allowance and demonstrates why an allowance is in the interests of retail customers and investors. Mr. Camfield's testimony also discusses the underlying reasons why investors face higher risks associated with the electric industry as a whole. He also explains why KCPL's high level of performance has resulted in lower prices, efficient productivity and resource utilization, and superior service. In summary, the Company's performance has created value and savings for retail customers and the State of Missouri, particularly in recent years. Accordingly, the Company respectfully requests that the MPSC and parties to the current proceeding give consideration to KCPL's performance when recommending a rate of return on equity in this proceeding.

Q: Did KCPL calculate its rate increase request based upon a performance allowance?

A: No. As I mention above, a rate of return on equity level of 11.5% is requested. KCPL believes that given the combined risks of the extensive, fast-paced construction program coupled with KCPL's exceptional performance and cost reduction efforts, a minimum of 11.5% return on equity is sufficient to sustain the Company and fairly compensate investors. Anything less, would leave the Company in danger of not satisfying the expectations and requirements of the investment community as a whole. The construction program is vital to the region served by KCPL, and ready access to outside capital is absolutely necessary for the timely completion of the construction. Acquiring outside capital on reasonable terms, in turn, requires that GPE continue to maintain the value of its common stock. To this end, a return level of at least 11.5% on equity is necessary. GPE must issue a substantial amount of equity during the five-year regulatory plan. An equity return level of less than 11.5%, however, is costly to the Company because it does not compensate shareholders for investment risks that they assume, and it does not provide sufficient flexibility to manage business risks under the condition of an on-going high level of construction.

Q: Does an 11.5% return on equity adequately address the substantial risk of KCPL's off-system sales?

A: No, it does not. The risk of the off-system sales market consists of several components, including market price, volumetric risk associated with generation variable cost, generation unit outages, coal supply availability, weather, and uncertainty of retail sales growth. A detailed risk analysis of the off-system sales market has been prepared by the Northbridge Group, Inc. ("Northbridge") and is contained in the testimony of Mr. Schnitzer of Northbridge. The risk of this market is too large for either the Company or its customers to bear entirely. Because these risks are so large, the Company believes that it would not be acceptable to retail consumers to incorporate the full costs of the risks to capital within the rate of return. Therefore, KCPL has decided not to request a rate of return above 11.5%, and proposes to share the off-system sales risk with customers and shareholders.

Q: How does KCPL propose to share the risk of off-system sales margins between customers and investors?

A: Based upon the analysis of Mr. Schnitzer, KCPL included approximately **[redacted]** of off-system sales margin in its test year revenue requirement. The expected level of off-system sales margin included in the budget for the year 2007, the first year increased rates would be in effect, is approximately **[redacted]**. At the time the budget was prepared (late summer/early fall 2005) it was estimated based upon MIDAS modeling that the Company has about a 50/50 chance of reaching this level of off-system sales margin. This amount of off-system sales margins is approximately the median of the distribution more recently developed by Mr. Schnitzer and shown in Schedule MMS-6 attached to his testimony.

Q: What was the actual off-system sales margin for the year 2005?

A: Model simulations indicate that the actual off-system sales margin for the year 2005 was approximately $100 million. This off-system sales margin represents revenue minus fuel cost consistent with the budgeted off-system sales margin of **[redacted]**.

Q: Why did the Company not use $100 million as the margin in the test year revenue requirement?

A: As I stated earlier in my testimony, and as further explained in the testimony of KCPL witnesses Burton Crawford and Michael Schnitzer a variety of factors will influence off-system sales margin in any given year. It is not appropriate to include such historical margins as a basis for determining the revenue requirement. As commonly recognized, off-system sales margins are highly uncertain, and, at a level that represents nearly **[redacted]** of KCPL's total earnings, cannot be equated with retail revenues that provide a continuous and dependable flow of returns to capital, for purposes of inclusion within test-year revenue requirement determination. This is particularly true when KCPL is in the first year of implementing a five-year $1.3 billion comprehensive energy plan.

Q: Is it appropriate to use historical data to estimate off-system sales margin when determining a test-year revenue requirement?

A: No, it is not. As I indicated previously, the only reasonable and responsible method to determine the appropriate amount of off-system sales margin to include in test year revenue is to project the amount of off-system sales margin expected during the first year that the increased rates would be in effect, calculate the risk of those off-system sales and share that risk between retail customers and the Company. This method provides the best balance of interests among customers, investors, and creditors, particularly in view of the scale of KCPL's construction program through the 2010 timeframe.

Q: How did KCPL determine the amount of projected 2007 off-system sales margins to include in determination of test-year revenue requirement?

A: Our estimate of the off-system sales margin included in test year revenue is based on Mr. Schnitzer's probability distribution shown in Schedule MMS-6 **(P)** of his testimony. Based on this analysis, it is 75 % likely that the Company will exceed **[redacted]** in off-system sales margin in 2007. However, this means a 25% chance exists that the off-system sales margin will be below this amount. Traditional return on equity determinations are based upon the assumption that retail revenue is the predominant contributor to return on equity. As stated previously, however, retail revenue and uncertain off-system margins should not be considered equal. KCPL selected the 75/25 point on the probability curve as a risk the Company would be able to accept given the return on equity, amortization, and other factors in the regulatory plan, *e.g.*, potential annual rate filings.

Q: Did KCPL consider a hedging strategy to reduce the risk of its off-system sales margins?

A: Yes, both Mr. Burton Crawford and Mr. Schnitzer are evaluating potential hedging strategies to reduce this risk. As described in Mr. Schnitzer's testimony, the opportunity to hedge spot market price risk by selling forward is limited. KCPL could construct a gas hedge by selling NYMEX gas contracts forward, or attempt to enter into bilateral contracts. Bilateral power sales are more highly correlated to the off-system contribution margin and thus are a more effective edge. However, the ability of the Company to enter into these bilateral sales is not certain. Mr. Schnitzer estimates a hedging strategy may reduce the probability of off-system sales margins falling below **[redacted]** in 2007 from 25% to 19% with a gas hedge that may cost around $3 million. As indicated previously, bilateral power sales are more highly correlated to the off-system sales contribution to margin. Mr. Schnitzer estimates a bilateral hedge strategy may reduce the probability of falling below **[redacted]** margin to 11%. However, it is unknown whether a hedge strategy based upon bilateral contracts would be possible. . Such a strategy is entirely dependent on finding buyers of the product. In addition, the cost of a bilateral hedge strategy is not known at this time and could be substantially higher than a gas hedge strategy. KCPL, in conjunction with Mr. Schnitzer and Northbridge Group, Inc., will continue to evaluate hedging strategies throughout the next several months and will provide additional information in the update of this proceeding. Given KCPL's risk sharing proposal for off-system sales margins in this proceeding, KCPL would not expect or propose that customers contribute to the cost of hedging at this time.

Q: Wouldn't a fuel adjustment clause eliminate the risk of off-system sales profit margin for KCPL?

A: A fuel adjustment clause could certainly be designed to eliminate all risk of off-system sales margins for the Company. This type of fuel clause would automatically pass through actual monthly fuel costs, offset by any off-system sales margins. Under this type of clause, the Company bears no risk for outages, prices, volume, weather, or any other risk. However, under this arrangement, the risks of off-system sales margins and other factors are entirely borne by customers. KCPL does not have such a fuel clause available to it in Missouri. I should mention that it is possible that a similar sharing of risk, as proposed in this filing, could be accomplished with the Interim Energy Clause ("IEC") option contained in the Regulatory Plan Stipulation and Agreement. However, in our view, the provisions regarding annual true-ups and asymmetrical over-and under-recovery contained in the IEC simply compound the risk the Company already bears, so we have not proposed it.

Q: Is KCPL proposing an IEC in this case to recover projected fuel costs excluding off-system sales margins?

A: No, KCPL is not proposing to utilize an IEC in this case. KCPL currently anticipates that it will file rate cases annually during the five-year Regulatory Plan period. Although the cost of coal, both F.O.B. mine and transportation costs, are increasing, KCPL's cost of coal is largely locked in for 2007, other than transportation cost adjustments such as diesel fuel. Increases in natural gas costs will likely cause KCPL's total costs of generation to increase; however, such cost increases will likely be more than offset by increased margins of off-system sales should natural gas prices rise, because gas prices set the market price for electricity in many hours of the year.

Q: Does a significant upside exist for the Company from the off-system sales market?

A: Yes, the Company recognizes that the probability at the time the budget was prepared, of exceeding its projected off-system sales margin in 2007, was 50/50. More recent analysis by Mr. Schnitzer indicates **[redacted]** represents the median of his probability distribution. KCPL intends to account for this potential earnings increase in some manner in this proceeding, given the Company's proposed risk sharing of off-system sales. This case will be updated to the twelve months ended June 2006, and trued up to September 30, 2006. As time gets closer to the effective date of new rates, KCPL anticipates additional information will be valuable in determining different approaches to this issue. A number of alternatives exist in this proceeding to account for the potential upside to the Company of increased off-system sales margins. These alternatives may include, but are not limited to; return on equity sharing mechanisms, earmarking of additional earnings for future amortization requirements, adjustments to the risk sharing for off-system sales, and potential refunds to customers.

Q: Did the Regulatory Plan Stipulation and Agreement contain a provision regarding treatment of off-system ratemaking purposes?

A: Yes, it did. The provision in Section III(B)(1)(j) at page 22 reads as follows:

"KCPL agrees that off-system energy and capacity sales revenues and related costs will continue to be treated above the line for ratemaking purposes. KCPL will not propose any adjustment that would remove any portion of its off-system sales from its revenue requirement determination in any rate case, and KCPL agrees that it will not argue that these revenues and associated expenses should be excluded from the ratemaking process."

Q: **Does KCPL believe it has complied with this provision contained in the Regulatory Plan Stipulation and Agreement?**

A: Yes, KCPL is treating all off-system sales margins above the line for ratemaking purposes. KCPL's proposal represents a means to recognize significant benefits of the off-system sales markets in customer rates and, at the same time, share the risk of not achieving expected yet unknown benefits during the first year increased rates are in effect. This represents an effort to balance the interest of customers, investors, and creditors.

Q: **Has KCPL implemented its SO_2 allowance plan?**

A: Yes. KCPL witness Edward Blunk describes the initial plan, its implementation and the revised plan recently submitted to the MPSC Staff and Office of Public Counsel.

Q: **Are there other potential issues that may impact this case that may be better defined or known by the time of the update or true up in this proceeding?**

A: Yes, legislation is currently proposed in Congress to require Companies with employee pension plans to reach a specific level of funding of those pension plans over a five-year period. Should such legislation become law it may require additional cash funding of the employee pension plan. This will impact the cash requirements of the Company and may impact the amortization amount needed to maintain the financial ratios established in the Stipulation and Agreement.

Q: **Does that conclude your testimony?**

A: Yes, it does.

BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

In the Matter of the Application of Kansas City Power & Light Company to Modify Its Tariffs to Begin the Implementation of Its Regulatory Plan	)))	Case No. ER-2006-____

AFFIDAVIT OF CHRIS B. GILES

STATE OF MISSOURI)
) **ss**
COUNTY OF JACKSON)

Chris B. Giles, being first duly sworn on his oath, states:

1. My name is Chris B. Giles. I work in Kansas City, Missouri, and I am employed by Kansas City Power & Light Company as Vice President, Regulatory Affairs.

2. Attached hereto and made a part hereof for all purposes is my Direct Testimony on behalf of Kansas City Power & Light Company consisting of twenty-nine (29) pages, all of which having been prepared in written form for introduction into evidence in the above-captioned docket.

3. I have knowledge of the matters set forth therein. I hereby swear and affirm that my answers contained in the attached testimony to the questions therein propounded, including any attachments thereto, are true and accurate to the best of my knowledge, information and belief.

Chris B. Giles
Chris B. Giles

Subscribed and sworn before me this 30th day of January 2006.

Nicole A. Wehry
Notary Public

My commission expires: Feb. 4, 2007

NICOLE A. WEHRY
Notary Public - Notary Seal
STATE OF MISSOURI
Jackson County
My Commission Expires: Feb. 4, 2007