BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

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.	))))	**File No. ER-2010-0356**

STAFF'S INITIAL BRIEF OF ISSUES SPECIFIC TO KCP&L GREATER MISSOURI OPERATIONS COMPANY

Respectfully submitted,

Nathan Williams
Deputy Counsel, Missouri Bar No. 35512
Attorney for the Staff of the
Missouri Public Service Commission
P. O. Box 360
Jefferson City, MO 65102
(573) 751-8702 (Telephone)
(573) 751-9285 (Fax)
nathan.williams@psc.mo.gov

March 25, 2011

NP

Table of Contents

BEFORE THE PUBLIC SERVICE COMMISSION
STATE OF MISSOURI

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.	))))	**File No. ER-2010-0356**

Staff's Initial Brief of Issues Specific to KCP&L Greater Missouri Operations Company

COMES NOW the Staff of the Missouri Public Service Commission, by and through counsel, and for its Initial Brief of Issues Specific to KCP&L Greater Missouri Operations Company, states as follows:

The KCP&L Greater Missouri Operations Company Specific Issues are:

1) KCP&L Greater Missouri Operations Company's ("GMO") fuel adjustment clause (the "fuel adjustment clause" issues), including the following: a) continuation of a fuel adjustment clause, b) the appropriate net base fuel cost, c) the level of changed net costs at risk in the clause—characterized as a "sharing" mechanism, d) whether transmission costs should be included in the clause, e) a clarification of the definition of forecasted retail net system input ("RNSI"), f) a clarification of the definition of OSSR, g) adding a factor to exclude fuel costs attributable to GMO's Crossroads generating station and h) other miscellaneous changes;

2) For determining the respective costs of service of MPS and L&P, the allocation between MPS and L&P of GMO's investment in, and the capacity and energy from Iatan 2, including the related impacts on fuel costs and off-system sales margins (the "Iatan 2 allocation" issue);

3) The level of investment, capacity, fuel, transmission, and related costs that should be included in MPS's cost of service for setting rates (the "Crossroads" issue)—for which Staff imputes costs based on two 105 MW combustion turbines built in 2005, and for which GMO relies on the costs of its Crossroads generating facility as a resource it owns which it dedicated to serving its retail load in August of 2008; and

4) The level of costs incurred for the Jeffrey Energy Center Flue Gas Desulphurization Rebuild Project that should be treated as investment and included as rate base in MPS's cost of service used for setting rates in this case (the "Jeffrey FGD Rebuild Project" issue).

In organizing this brief, as it did in its Initial Brief, Staff has restated the issues as GMO characterized them, followed by Staff's statements of the issues, position statements and argument. Unlike its Initial Brief, here there is no focus on the maxim, "*falsus in uno, falsus in omnibus.*" Because prudence was thoroughly discussed in its Initial Brief, in this brief Staff limits its discussions of prudence here to showing GMO's imprudence in the "Crossroads" and the "Jeffrey FGD rebuild project" issues.

Missouri courts have long recognized the purpose of the Public Service Commission Law is to protect consumers against the natural monopolies of the public utilities while permitting the utilities to recover just and reasonable returns.[1] In doing so the courts have stated the legislative purpose of the Public Service Commission Law is to replace competition inadequate to protect the public and avoid economic waste of competition between public

[1] See *State ex rel. Utility Consumers Council of Missouri, Inc. v. Public Serv.* Comm'n, 585 S.W.2d 41, 47 (Mo. Banc 1979).

utilities.[2] Further, the courts have said, ". . . such regulation, to command respect from patron or utility owner, must be in the name of the overlord, the state, and to be effective must possess the power of intelligent visitation and the plenary supervision of every business feature to be finally (however invisibly) reflected in rates and quality of service."[3]

The officers of GMO have fiduciary obligations to GMO's shareholder.[4] In carrying out those obligations GMO's officers constructed the MPS and L&P cases they filed with a goal of maximizing the revenues this Commission would allow GMO to be entitled to get from its retail customers. By proposing net base fuel costs in its fuel adjustment clause significantly below the net fuel-related costs included in the costs of service of MPS and L&P, and by their allocation of Iatan 2 between MPS and L&P, GMO's officers managed to propose virtually the same percentage increases to the rates of KCPL, MPS and L&P customers—13.8%, 14.4% and 13.9%, respectively, in the tariff sheets they filed on June 4, 2010. Further, by proposing the net base fuel costs in GMO's fuel adjustment clause remain at their current levels, which are significantly below the annualized, normalized, trued-up test year net fuel-related costs for MPS and L&P, based on Staff's true-up case, GMO's officers are proposing to recover from its MPS and L&P customers through its fuel adjustment clause 95 percent of $3.4 million and $11.4 million, respectively. While not changing the bases does delay GMO's recovery of 95% of its net fuel costs it does not recover in its general rates, and GMO's customers pay that 95%, not 100%, GMO gets interest on that 95% which offsets most, if not all, of the 5% GMO is not explicitly

---

[2] *Id.*

[3] *Id.* (quoting *May Department Stores v. Union Electric Power and Light Co.*, 341 Mo. 299, 107 S.W.2d 41, 48, quoting *State ex rel. City of Sedalia v. Public Service Commission*, 275 Mo. 291, 204 S.W.497, 498 (Mo. 1918) appeal dismissed 251 U.S. 547, S.Ct. 342, 64 L.Ed. 408 (1920)).

[4] *See Waters v. G&B Feeds, Inc.*, 306 S.W.3d 138, 146-47 (Mo. App. 2010).

recovering through its fuel adjustment clause as a net fuel cost. If those costs are instead collected through GMO's general rates, they would increase current rates by approximately 0.7% and 8.0% for MPS and L&P retail customers, respectively, and send timelier fuel cost signals to retail customers. All of these actions are the result of the attempts of GMO's officers to maximize the revenues GMO receives from its retail customers as a result of new rates in this case, not because of any ratemaking principle, or principles.

FUEL ADJUSTMENT CLAUSE ISSUES

GMO's statements of the fuel adjustment clause issues follow:

> **IV. GMO Only Issues**
>
> **5.** Transmission Costs: Should transmission costs be included in the FAC as recommended by the Company? If not, should a tracker be established for recovery of transmission costs? If either case, should changes in wholesale transmission revenue be used to offset transmission expense as proposed by Staff?
>
> **6.** Rebasing: Should the Company be required to rebase its fuel and purchase power expenses, net of off system sales, in excess of such amounts built into base rates?
>
> **7.** FAC sharing mechanism: Should the FAC sharing mechanism be changed from 95/5 to 75/25 as proposed by Staff?

Staff's statements of the fuel adjustment clause issues with its responsive position statements follow:

> **90. Fuel Adjustment Clause continuation**:
>
> Should GMO's Fuel Adjustment Clause (FAC) be modified, continued, or discontinued?
>
> Staff's position: GMO's FAC should be continued with modifications.
>
> **91. Sharing Mechanism**:
>
> What should be the level of sharing in GMO's Fuel Adjustment Clause sharing mechanism?
>
> Staff's position: The sharing mechanism should be 75% customers/25% GMO.

92. Base Energy Cost:

Should GMO's Fuel Adjustment Clause be modified to require the base energy cost in the Fuel Adjustment Clause equal the base energy cost in the test year total revenue requirement used for setting rates in the rate case?

Staff's position: Yes.

93. Should transmission expenses be included in GMO's Fuel Adjustment Clause?

Staff's position: No.

Should two FERC accounts now in the definition of Purchased Power Cost be deleted since these FERC accounts are for transmission expenses and, therefore, are not consistent with the definition of fuel and purchased power cost in 4 CSR 240-20.090(1)(B).

Staff's position: Yes.

94. Should factor RNSI (forecasted retail net system input) be redefined in GMO's Fuel Adjustment Clause as RNSI = Forecasted recovery period net system input, at the generator, for the calculation of the CAF (cost adjustment factor)?

Staff's position: Yes.

95. Should the definition of OSSR be changed to clarify that only sales to Missouri municipalities are excluded from OSSR.

Staff's position: Yes.

96. Should GMO's Fuel Adjustment Clause include a new factor to exclude GMO's fuel costs for its Crossroads generating plant from GMO's Fuel Adjustment Clause?

Staff's position: Yes.

97. Should GMO's Fuel Adjustment Clause tariff sheets follow the example tariff sheet filed with the surrebuttal testimony of Staff witness John Rogers or the example tariff sheet filed with the testimony of GMO witness Tim Rush?

Staff's position: The exemplar tariff sheets as filed with the surrebuttal testimony of John Rogers.

Section 386.266.5, RSMo. Supp. 2009, provides that after the Commission approves a fuel adjustment clause, "it shall remain in effect until the commission authorizes the modification, extension, or discontinuance of the mechanism in a general rate case or complaint proceeding." Staff recommends the Commission authorize certain modifications to GMO's fuel adjustment clause, but opposes others. In considering these fuel adjustment clause issues, the Commission should keep in mind that the purpose of a fuel adjustment clause is to protect a utility from the regulatory lag associated with recovery through retail rates of increasing fuel-related costs and its customers from the regulatory lag associated with reductions in retail rates due to decreasing fuel-related costs.

REBASING

First, Staff recommends the Commission authorize and require modification of GMO's fuel adjustment clause so that, for both MPS and L&P, respectively, the base energy cost in its fuel adjustment clause equal the base energy cost in the test year total revenue requirement used for setting rates in this case. To accomplish the purpose of a fuel adjustment clause—to protect utilities and their customers from delay in recognizing changes in the costs of fuel and purchased power—the net base fuel cost in GMO's fuel adjustment clause should match with the base energy cost in the test year total revenue requirement used for setting rates in this case. This is referred to as "re-basing." It is important to recognize that even GMO does not to propose to collect all of its fuel and purchased power costs through its fuel adjustment clause in this case, only a portion of them. Therefore, GMO is proposing to collect part of its fuel and purchased power costs through its general rates, to collect another part of its fuel and purchased power costs

through its fuel adjustment clause, and account for variations in its fuel and purchased power costs through its fuel adjustment clause.

Staff recommends matching the base energy costs in fuel adjustment clauses to the base energy cost in the test year total revenue requirement used for setting general rates because doing so ensures that retail customers get the correct price signal through fixed rates for the utility's cost to serve them as soon as possible, and the utility's retail customers will avoid paying interest on fuel and purchased power costs that would be collected later through its fuel adjustment clause. When the base energy cost in a fuel adjustment clause matches the base energy cost in the test year total revenue requirement used for setting general rates, in an environment where the cost variations trend neither up nor down, the risk to the utility of billing or issuing credits occurs as intended; however, if the base energy cost in a fuel adjustment clause is less than the base energy cost in the test year total revenue requirement used for setting rates, in an environment where the cost variations trend neither up nor down, or where they are increasing, the utility will bill its customers through its fuel adjustment clause for fuel costs that are already included in the permanent rates they are paying, *i.e.*, GMO's retail customers will be billed ***twice*** for the same fuel costs.[5]

GMO's mismatch proposal not to rebase—not to match the net base fuel cost in its proposed fuel adjustment clause with the base energy cost in its test year total revenue requirement it proposes be used for setting rates in this case—is driven by GMO's goal of maximizing the revenues it will get from its retail customers as a result of this case, while minimizing the stated rate increase. GMO expressly stated this is the "primary reason" why it

[5] Ex. GMO—210, Staff Revenue Requirement Cost of Service Report, pp. 199-201; Ex. GMO—240, Rebuttal Testimony of John A. Rogers, pp. 7-10; Ex. GMO—241, Surrebuttal Testimony of John A. Rogers, pp. 6-9.

chose not to rebase.[6] GMO's mismatch proposal seems contrary to the spirit of the first sentence of the enabling language of Section 386.266.1, RSMo. Supp. 2009, 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.) Moreover, given that in its last general rate increase case, Case No. ER-2009-0090, when GMO's original filing matched the base energy cost in its fuel adjustment clause with the base energy cost in its proposed test year total revenue requirements used for the rates it proposed for MPS and L&P, GMO did not include the amount of the increase in its general rates attributable to fuel and purchased power costs it would otherwise collect through its fuel adjustment clause when describing its proposed rate increases. In this case, GMO stridently refused to reflect in its customer notice what its rate increases for MPS and L&P would be if GMO did not have a fuel adjustment clause arguing it had not filed its case for such an increase. It is patent that when it filed this case, GMO's goal was to avoid telling its customers with any accuracy what GMO views it costs GMO to serve them, including the impacts on their bills when the impacts of prospective general rate increases mesh with retrospective fuel adjustment clause rate increases.[7]

During the evidentiary hearing GMO witness Rush testified on cross-examination as follows:

---

[6] Ex. GMO—34, Rebuttal Testimony of Tim M. Rush, p. 26.

[7] Ex. GMO—32, Direct Testimony of Tim M. Rush, p. 6; Ex. GMO—33, Rebuttal Testimony of Tim M. Rush, pp. 3-4.

> If we increase the base fuel cost in comparison to recovering it through the fuel adjustment clause, the only thing that the Company would obtain to its benefit would be the 5 percent that we currently absorb in the 95-5 sharing mechanism that exists in the FAC. So, for example, if the costs went up a dollar for fuel and you rolled that in to the base rates, the Company would only receive five cents' contribution to that fuel cost because it's already receiving 95 percent in the fuel adjustment mechanism.[8]

In response to the question, "Why in this case did the Company believe it was not in the best interest of itself and its customers to rebase the fuel costs in the fuel adjustment clause?", he further testified:

> The Company was putting in the most significant increased investment that the Company has made in many, many years with the Iatan project, and the rate increase, the Company felt, was going to be significant.
>
> In evaluating all of the things that we looked at, we tried to determine what things we should ask for, what things we needed to ask for, and what things we were willing to absorb as a company to mitigate the needs to help address the issue of the consumer.
>
> One of the things that we considered is trying to rebase -- whether we rebase the fuel cost or not. In my testimony I demonstrated that if we would have rebased, it would've put a significant increase to the consumer on an immediate basis, and we felt that spreading that out over a longer period of time after we get through the hurdles of a significant increase in our rates would be much better to the consumer, and the Company was willing to absorb that.[9]

The "that" GMO was willing to "absorb" is the five percent it loses through the existing fuel adjustment clause "sharing mechanism."

[8] Tr. Vol. 42, p. 4427.

[9] Tr. Vol. 42, pp. 4432-33.

GMO witness Rush's statements in his rebuttal and surrebuttal testimony that in GMO's last rate case the parties agreed not to rebase GMO's fuel adjustment clause are erroneous.[10] As Mr. Rush finally admitted after forcing Public Counsel to repeat the same question several times during cross-examination, the base energy costs in GMO's fuel adjustment clause were changed in its last rate case, Case No. ER-2009-0090,[11] and, further, that case was resolved by a commission-approved "black box" stipulation and agreement—**NON-UNANIMOUS STIPULATION AND AGREEMENT**[12]**—**signed by GMO and filed May 22, 2009, and which includes the following provisions:

> **19**. This 2009 GMO Stipulation is being entered into solely for the purpose of disposing of Case No. ER-2009-0090. Except as expressly and specifically addressed otherwise in this 2009 GMO Stipulation, no Signatory to this 2009 GMO Stipulation shall be deemed to have approved, accepted, agreed, consented, or acquiesced in, including without limitation, any procedural principle, question of Commission authority, accounting authority order principle, cost of capital principle or methodology, capital structure principle or methodology, decommissioning methodology, ratemaking principle, valuation methodology, cost of service methodology or determination, depreciation principle or method, rate design methodology, cost allocation principle or methodology, cost recovery principle or methodology, or prudence question that may underlie this 2009 GMO Stipulation, or for which provision is made in this 2009 GMO Stipulation.
>
> **20.** This 2009 GMO Stipulation represents a negotiated settlement. Except as specified herein, the Signatories to this 2009 GMO Stipulation shall not be prejudiced, bound by, or in any way affected by the terms of this 2009 GMO Stipulation: (a) in any future proceeding; (b) in any proceeding currently pending under a separate docket; (c) in any pending judicial review and/or appeal

[10] Ex. GMO—33, Rebuttal Testimony of Tim M. Rush, p. 3; Ex. GMO—35, Ex. GMO—34, Rate Design Rebuttal Testimony of Tim M. Rush, pp. 26-27;Ex. GMO—35, Surrebuttal Testimony of Tim M. Rush, p. 3.

[11] Tr. Vol. 42, pp. 4443-4446.

[12] Ex. GMO-50.

> including, but not limited to, those arising from Commission Case Nos. ER-2007-0004, EO-2008-0216, EO-2008-0415, EO-2009-0254 and EM-2007-0374; and/or (d) in this proceeding should the Commission decide not to approve this 2009 GMO Stipulation, or in any way condition its approval of same.
>
> * * * *
>
> **22.** If approved and adopted by the Commission, this 2009 GMO Stipulation shall constitute a binding agreement among the Signatories. The Signatories shall cooperate in defending the validity and enforceability of this 2009 GMO Stipulation and the operation of this 2009 GMO Stipulation according to its terms.

Moreover, in its June 10, 2009, *Order Approving Non-Unanimous Stipulations and Agreements and Authorizing Tariff Filing*, with which the Commission approved the stipulation and agreement where the foregoing terms appear, the Commission, in ordered paragraph 2, ordered, "The Signatories to the Non-Unanimous Stipulation and Agreement are ordered to comply with the terms of the Agreement."[13] As stated above, GMO is a signatory to that agreement. Once again GMO has demonstrated a flagrant disregard of the agreements it enters into when they do not suit its purposes.

Based on information known as of December 31, 2010, matching the base energy costs in GMO's fuel adjustment clause to match the base energy costs in the test year total revenue requirements Staff recommends be used for setting rates has the impact of increasing GMO's fuel adjustment clause base energy cost for MPS and L&P by 2.3% and 30.1%, respectively.

[13] Ex. GMO--52.

"SHARING" MECHANISM

Second, Staff recommends the Commission authorize and require modification of GMO's fuel adjustment clause so that GMO's retail customers are responsible for 75% rather than 95% of the variations in total energy costs (GMO FAC factor "TEC") from base energy costs (GMO FAC factor "B") and a newly proposed Crossroads generation plant (GMO FAC factor "CGP") factor.

Primarily because the 95%/5% sharing mechanism currently in place is not sufficient incentive to cause KCP&L Greater Missouri Operations Company to file to reset the base energy cost in the fuel adjustment clause to match the base energy cost used to set rates in the rate case, the sharing mechanism should be changed to a 75%/25% sharing.

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 25% 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 and, at the same time, manage the risk of losing supplies of its energy. Further, it would provide a sufficient risk of revenue loss that GMO would not "absorb" that loss in order to obtain a larger increase in its general rates, *i.e.*, GMO would not have been willing to forego 25% of the portion

of its fuel costs it anticipates collecting through its fuel adjustment clause, as it is willing to do when it is seeking to forego only five percent.[14]

Rather than accepting the premise the utilities promote—that they are entitled to recover all their fuel and purchased power costs—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 powers costs embedded in general 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 on revenues because the variations should be much less than the level in excess of the base fuel and purchased power costs included in its general rates that GMO is proposing to recover through its fuel adjustment clause. If the level of risk proves too great, GMO may file a general rate case in which it seeks to reduce that risk level.

GMO's suggestions Staff is seeking to penalize it by recommending the "sharing" mechanism be changed from 95%/5% to 75%/25% are untrue. Section 386.266.1, RSMo. Supp. 2009, 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 willingness to forego five percent of a portion of historically based expected fuel and purchased power costs demonstrate a 95%/5% sharing simply is not very meaningful to it.

Another demonstration that the 95%/5% sharing is not very meaningful to GMO is that GMO has stopped accepting and processing new applications for its large customer MPower

[14] Ex, GMO—210, Staff Revenue Requirement Cost of Service Report, pp. 196-199; Ex. GMO—240, Rebuttal Testimony of John A. Rogers, p. 10; Ex. GMO—241, Surrebuttal Testimony of John A. Rogers, p. 12.

demand-response program now that it has the low-cost capacity of Iatan 2 available to it, even though the program proved to be a very effective way to reduce load on its system during times when market prices for energy are very high. Apparently the five percent of revenue that GMO would get to keep for any sales made possible from demand reductions due to the MPower program is not meaningful enough for GMO to pursue these available demand-response resources.

Since the Commission first authorized GMO's fuel adjustment clause—with a 95%/5% "sharing" mechanism—natural gas prices—a commodity upon which GMO is very dependent—have become and are expected to remain relatively stable in the future due to the very large potential of shale gas plays.

Both lower gas prices and customer participation in its MPower program enhance GMO's opportunities for increased off-system sales, which would provide GMO with a greater benefit with a 75%/25% "sharing" than with the current 95%/5% "sharing."[15]

CROSSROADS GENERATING STATION FACTOR

Third, if the Commission accepts Staff's position on fuel costs in the Crossroads issue, Staff recommends the Commission authorize and require modification of GMO's fuel adjustment clause to include a new factor that would exclude an increment of GMO's fuel costs for its Crossroads generating station from Fuel and Purchased Power Adjustments (GMO FAC "FPAs"). Consistent with its position that GMO's ratepayers should pay costs based on two 105 megawatt combustion turbines built in 2005 and located at the South Harper site, GMO's fuel clause should be modified so that its customers do not bear the

[15] Ex. GMO—241, Surrebuttal Testimony of John A. Rogers, pp. 15-18.

incremental costs associated with higher gas prices and transmission costs of the Crossroads Energy Center which is located near Clarksdale, Mississippi.

GMO has not responded to Staff's proposal presented in its *Rate Design and Class Cost-of-Service Report*; however, given the contention between Staff and GMO on the Crossroads issue, Staff is confident GMO opposes inclusion of a "CPG" factor in its fuel adjustment clause to remove from total energy costs for MPS the additional fuel costs attributable to Crossroads, a factor Staff proposes be $740,071 annually; $370,035 for each six-month accumulation period. Staff proposes this factor consistent with its position fuel costs for Crossroads are higher than they would be had GMO built two additional 105MW combustion turbines at South Harper in 2005.[16]

FORECASTED RETAIL NET SYSTEM INPUT DEFINITION

Fourth, Staff recommends the Commission authorize and require modification of GMO's fuel adjustment clause so that the factor RNSI (forecasted retail net system input) in GMO's fuel adjustment clause be redefined to clarify that it is based on net system input *at the generator*.[17] This change should have no substantive effect. Because GMO has not responded to this proposal, Staff believes it is uncontested.

[16] Ex. GMO—211, Staff Rate Design and Class Cost-of-Service Report, p. 34, Sch. JAR-2-14; Ex. GMO—241, Surrebuttal Testimony of John A. Rogers, Sch. JAR-2-14 Revised.

[17] Ex. GMO—211, Staff Rate Design and Class Cost-of-Service Report, p. 33, Sch. JAR-2-16.

ONLY SALES TO MISSOURI MUNICIPALITIES EXCLUDED FROM OFF-SYSTEM SALES REVENUES

Fifth, Staff recommends the Commission authorize and require modification of GMO's fuel adjustment clause to clarify that only sales to Missouri municipalities are excluded from off-system sales revenues (GMO FAC factor "OSSR").[18] This change should have no substantive effect. Because GMO has not responded to this proposal, Staff believes it is uncontested.

CLARIFICATIONS

Sixth, Staff recommends the Commission authorize and require certain other modifications to GMO's fuel adjustment clause tariff sheets to clarify and improve them as shown in the example tariff sheets attached to Staff's Rate Design and Class Cost-of-Service Report, as revised in schedules attached to the surrebuttal testimony of Staff witness John A. Rogers.[19] Staff believes GMO agrees to these modifications only to the extent that Staff's proposed changes match changes proposed by GMO witness Tim Rush.[20]

TRANSMISSION EXPENSES

Finally, Staff opposes GMO's proposed modification to include transmission expenses and, in that same vein, proposes GMO's fuel adjustment clause be modified to remove from the

---

[18] Ex. GMO—211, Staff Rate Design and Class Cost-of-Service Report, p. 34, Sch. JAR-2-15; Ex. GMO—241, Surrebuttal Testimony of John A. Rogers, Sch. JAR-2-15 Revised.

[19] Ex. GMO—211, Staff Rate Design and Class Cost-of-Service Report, Schs. JAR-1 and JAR-2; Ex. GMO—241, Surrebuttal Testimony of John A. Rogers, Schs. JAR-1-10 Revised, JAR-2-14 Revised and JAR-2-15 Revised

[20] Ex. GMO—32, Sch. TMR2010-3.

definition of Purchased Power Cost in the clause two FERC accounts—FERC account numbers 565 and 575.[21] GMO hangs its proposal to include transmission expenses in its fuel adjustment clause on its faulty interpretation that "transportation" costs as used in 4 CSR 240-20.090(1)(B) and therefore, section 386.266.1, RSMo. Supp. 2009, includes transmission costs.[22] That GMO witness Tim Rush actually believes this interpretation is questionable since he draws a distinction between "transportation" and "transmission" costs in his direct testimony, "The increasing prices for natural gas, coal, coal *transportation* and *transmission* costs are not costs that can be controlled by the Company, nor are they costs that can be absorbed by reducing other costs."[23] (Emphasis added.) Further, in the original Public Service Commission Act, the Legislature recognized "transportation" is distinct from "transmission,"

> The pendency of a writ of review shall not of itself stay or suspend the operation of the order or decision of the commission, but during the pendency of such writ, the circuit court in its discretion may stay or suspend, in whole or in part, the operation of the commission's order or decision. No order so staying or suspending an order or decision of the commission shall be made by any circuit court otherwise than on three days' notice and after hearing, and if the order or decision of the commission is suspended the same shall contain a specific finding based upon evidence submitted to the court and identified by reference thereto, that great or irreparable damage would otherwise result to the petitioner and specifying the nature of the damage. In case the order or decision of the commission is stayed or suspended, the order or judgment of the court shall not become effective until a suspending bond shall first have been executed and filed with, and approved by, the circuit court, payable to the state of Missouri, and sufficient in amount and security to secure the prompt payment, by the party petitioning for the review, of all damages caused by the delay in the enforcement of the order or decision of the commission, and of all moneys which any person or corporation may be compelled to pay, pending the review proceedings, for ***transportation***, ***transmission***, product, commodity or service in excess of the

[21] Ex. GMO—211, Staff Rate Design and Class Cost-of-Service Report, Sch. JAR-2-15; Ex. GMO—241, Surrebuttal Testimony of John A. Rogers, Sch. JAR-2-15 Revised.

[22] Ex. GMO—35, Surrebuttal Testimony of Tim M. Rush, p. 2.

[23] Ex. GMO—32, Direct Testimony of Tim M. Rush, p. 6.

charges fixed by the order or decision of the commission, in case such order or decision is sustained.[24] (Emphasis added.)

Additionally, the common definitions of transportation and transmission differ:

trans·por·ta·tion–noun

1. the act of transporting.
2. the state of being transported.
3. the means of transport or conveyance.
4. the business of conveying people, goods, etc.
5. price of travel or transport by public conveyance; fare.
6. tickets or permits for transport or travel.
7. banishment, as of a criminal to a penal colony; deportation.
8. (*initial capital letter*) Also called Transportation Department. *Informal*. The Department of Transportation.

trans·mis·sion–*noun*
1. the act or process of transmitting.
2. the fact of being transmitted.
3. something that is transmitted.
4. *Machinery* .
a. transference of force between machines or mechanisms, often with changes of torque and speed.
b. a compact, enclosed unit of gears or the like for this purpose, as in an automobile.
5. *Radio and Television*. the broadcasting of electromagnetic waves from one location to another, as from a transmitter to a receiver.
6. *Physics*. transmittance.

For all the foregoing reasons transmission costs should not be included in GMO's adjustment clause because they are not included in section 386.266, RSMo. Supp. 2009, as a type of cost to be recovered through a fuel adjustment clause, they are inconsistent with the definitions of fuel and purchased power cost in 4 CSR 240-20.090(1)(B), and elsewhere, and they do not vary in a direct relationship with fuel or purchased power. For these same reasons two FERC accounts which track transmission costs that are now included in the

[24] § 386.520.1, RSMo. 2000.

definition of "purchased power cost" in GMO's fuel adjustment clause should be removed from that definition—FERC account numbers 565 and 575.

IATAN 2 ALLOCATION

GMO's statements of the Iatan 2 allocation issue follows:

> **IV. GMO Only Issues**
>
> **3**. Iatan 2 allocation (MPS vs. L&P): What is the appropriate allocation of Iatan 2 and associated common plant between MPS and L&P?

Staff's statement of the Iatan 2 allocation issue with its responsive position statement follows:

> 77. **Iatan Unit 2 and Iatan Common Costs**:
>
> a. How should GMO's portion of the costs of Iatan 2 and associated Iatan Common Plant be allocated to the rate bases of L&P and MPS, respectively?
>
> Staff's Position: They should be allocated based on L&P having 100 MW and MPS having 53 MW, i.e., the cost allocators should be 0.6536 for allocation L&P and 0.3464 for allocation to MPS.

This issue is about how to fairly assign and apportion between GMO's two rate districts—MPS and L&P—the impacts of GMO's investment in Iatan 2 on rate base, fuel costs, off-system sales margins, etc. In other words, the issue is between the two rate districts, what should MPS and L&P customers pay for their electricity due to Iatan 2?[25] Staff recommends the Commission treat L&P as getting 100 MW of Iatan 2 and MPS as getting 53 MW.[26] With this approach the impacts of Iatan 2 on GMO's cost of service would

[25] Lena M. Mantle, Tr. Vol.36, p. 3892.

[26] Ex. GMO-210, Staff Revenue Requirement Cost of Service Report, p. 85; Ex. GMO—232, Rebuttal Testimony of Lena Mantle, p. 4.

then be assigned or allocated to cost of service for MPS and cost of service for L&P based on the following: 100/153 (0.654 or 65.4%) for L&P and 53/153 (0.346 or 34.6%) for MPS. When compared to GMO's proposal of 41/153 (0.268 or 26.8%) for L&P and 112/153 (0.732 or 73.2%) for MPS,[27] Staff's proposal shifts about $18 million of revenue responsibility from MPS to L&P, *i.e.*, considering just the issue of the Iatan 2 assignment to MPS and L&P, this shift results in Staff's cost of service for L&P being about $18 million higher than GMO's and, at the same time, Staff's cost of service for MPS is about $18 million less that GMO's.

This about $18 million shift between MPS and L&P takes into account not only the difference in capital costs assigned to MPS and L&P, but also the impact on fuel costs. Iatan 2 is expected to be GMO's lowest cost generation unit.[28] As a result, with the addition of Iatan 2 GMO's more expensive to run natural gas-fired units will be used less, resulting in lowered MPS fuel costs. While L&P will reap the same benefit, the beneficial impact on L&P's fuel costs will be less since power from Iatan 2 will replace low-cost energy L&P has been getting through a 100 MW purchased power agreement that ends in May of 2011. Further, for each incremental MW less than 100 MW of Iatan 2 that is allocated to L&P (the capacity of the expiring purchased power agreement), L&P's fuel costs will greatly increase because, in each hour, the low-cost Iatan 2 energy L&P would have gotten will be replaced by energy from MPS's highest operating cost unit that is running. Therefore, Staff's recommendation of allocating 100 MW to L&P results in the lower fuel costs for L&P than MPS's recommended allocation of 41 MW to L&P.[29]

---

[27] Ex. GMO—232, Rebuttal Testimony of Lena M. Mantle, p. 4.

[28] Tim M. Rush, Tr. Vol. 36, p. 3815.

[29] Ex. GMO—232, Rebuttal Testimony of Lena M. Mantle, p. 5.

This issue originates with the merger of UtiliCorp United, Inc., and St. Joseph Light & Power Company in 2000. In obtaining approval from this Commission for that merger, UtiliCorp United, Inc., now named GMO, committed to not changing the rates of the former St. Joseph Light and Power Company customers due to the merger. Since that time GMO has had two rate districts, one in and about St. Joseph, Missouri—the L&P rate district—and one for the remainder of its service area—the MPS rate district. Since that merger in 2000, the premerger ownership of assets has been used as the basis for assigning and allocating costs and revenues for determining rates for these two districts. [30] This is a matter of fairness.

Many of the generating units GMO and St. Joseph Light & Power Company owned and used to serve their retail customers were costly to build and resulted in initially higher rates that over time have become more cost effective relative to other sources of electricity, sources such as purchased power.[31] Those customers who initially paid higher rates for generating facilities still being used to serve them—primarily Iatan 1—should get the benefit of the now relatively lower cost of those units to generate electricity. When GMO and St. Joseph Light & Power Company merged, St. Joseph Light & Power Company had more than enough generation resources to serve its load, including growth, for many years, and GMO needed significant additional capacity to replace its 500 MW purchased power contract that ended in May of 2005.[32] Because St. Joseph Light & Power Company had an 18% ownership of the entire Iatan station before Iatan 2 was built, Iatan 2 could not be built without affecting

[30] Ex. GMO-210, Staff Revenue Requirement Cost of Service Report, pp. 94-95 and Appendix 5, Sch. LMM-3.

[31] Ex. GMO-210, Staff Revenue Requirement Cost of Service Report, pp. 103, 108.

[32] Ex. GMO-210, Staff Revenue Requirement Cost of Service Report, p. 91; Ex. GMO—233, Surebuttal Testimony of Lena M. Mantle, p. 4.

St. Joseph Light & Power Company's ownership interest in the Iatan station.[33] GMO, then known as Aquila, particularly due to its poor financial condition, only had the opportunity to be a part owner of Iatan 2 because it had acquired St. Joseph Light & Power Company's ownership in the Iatan station when it acquired and merged with St. Joseph Light & Power Company.[34] These are the reasons Staff has used the premerger ownership of assets as the basis for assigning and allocating costs and revenues for setting rates for MPS and L&P customers.

Because it was the MPS rate district that needed additional capacity to serve its retail customers, the costs of South Harper were assigned to MPS.[35] The issue now is how to assign and allocate the impacts GMO's ownership share of Iatan 2 between MPS and L&P. Following the precedent of using the pre-2000 merger ownership of assets as a basis for assigning and allocating costs related to generating units for determining rates for MPS and L&P, Staff has relied on the following to shape its recommendation: 1) It was St. Joseph Light and Power Company that had an ownership interest in the Iatan station before the construction of Iatan 2; 2) it was St. Joseph Light and Power Company that entered into a long-term purchased power contract with Nebraska Public Power District for 100 MW of baseload capacity that expires in May 2011, while MPS does not have a similar agreement that will expire as imminently[36]; and 3) the impacts on MPS and L&P rates of different allocations of Iatan 2 impacts.[37] Based on

---

[33] Ex. GMO-210, Staff Revenue Requirement Cost of Service Report, p. 94..

[34] Ex. GMO-210, Staff Revenue Requirement Cost of Service Report, p. 99; Ex. GMO—217, Surrebuttal Testimony of Cary G. Featherstone, pp. 45-48.

[35] Ex. GMO-210, Staff Revenue Requirement Cost of Service Report, pp. 85, 95, 105-106.

[36] MPS has a 75 MW purchased power agreement with NPPD, but it does not expire until 2014. Ex. GMO—11, Rebutal Testimony of Burton L. Crawford, pp. 6-7; Ex. GMO—33, Rebuttal Testimony of Tim M. Rush, p. 11, Tim M. Rush, Tr. Vol. 36, p. 3880; Mantle Tr. Vo. 36, pp. 3867-68.

[37] Ex. GMO—233, Surrebuttal Testimony of Lena M. Mantle, p. 8.

these considerations and the precedent of looking at the capacity needs of each district, rather than proposing all of the impacts of Iatan 2 be assigned and allocated to L&P, Staff conservatively is proposing that the impacts of Iatan 2 be assigned and allocated to MPS based on 53 of 153 MW and to L&P based on 100 of 153 MW.[38] Staff's proposal more correctly matches the proper level of Iatan 2 costs to customers who originally supported the Iatan plant facility and who need replacement of the base load purchased power capacity that has expired. Without this amount of capacity, L&P, if it was a stand-alone utility, would not have sufficient capacity to meet the energy requirements of its customers.[39] Staff, who believes MPS should have additional base load capacity, has assigned the remainder of GMO's share of Iatan 2 to MPS.

Staff opposes GMO's proposal that Iatan 2 be placed in a separate corporation, and that in this and each following rate case the costs of Iatan 2 be allocated between MPS and L&P for setting the rates applicable in each. As was done with South Harper—all costs and rate impacts as if MPS owned South Harper were assigned to MPS—it is Staff's view that between MPS and L&P the rate impacts of Iatan 2 be fixed as if ownership were assigned to L&P and MPS.[40] Further, GMO's proposal to place most of the baseload generation of Iatan 2 with MPS and shift from MPS to L&P peaking generation to result in similar mixes of baseload and peaking generation for each is based on the unsupported premise that both should have a similar mix.

---

[38] Ex. GMO-210, Staff Revenue Requirement Cost of Service Report, pp. 94-103; Ex. GMO—232,Rebuttal Testimony of Lena M. Mantle, pp. 4-6; Ex. GMO—233, Surrebuttal Testimony of Lena M. Mantle, p. 8.

[39] Ex. GMO-210, Staff Revenue Requirement Cost of Service Report, p. 99; Rebuttal Testimony of Lena M. Mantle, p. 8; Ex. GMO—233.

[40] Ex. GMO—232, Rebuttal Testimony of Lena M. Mantle, pp. 5, 8.

GMO's methodology, which results in a similar mix of base/non-base generation, is not supported by the load requirements of MPS and L&P. L&P's winter heating load is of nearly the same magnitude as its summer cooling load, signifying a high saturation of electric heating whereas MPS load showed little response to winter. As a percentage of load, L&P has more industrial load than MPS and MPS has more weather-sensitive commercial load than L&P. All of which means L&P can more efficiently use additional baseload capacity such as Iatan 2 than MPS.[41] L&P has more baseload energy needs than MPS and, therefore, should be allocated more of Iatan 2. As a result, it is appropriate it have more baseload generation in L&P's mix than MPS's.

As stated early in this brief, GMO's proposal for Iatan 2 is an attempt by GMO's officers to maximize the revenues GMO receives from its retail customers as a result of new rates in this case, not because of any ratemaking principle, or principles.

After it obtained rights to Iatan 2 GMO initially proposed to treat Iatan 2 as being "owned" by MPS, as South Harper is treated. Staff and other stakeholders voiced their concerns and GMO stated it would work with them on an appropriate sharing of Iatan 2 between MPS and L&P, before and after GPE acquired GMO in 2008. That never occurred, and Staff did not know of GMO's proposal to treat MPS as having 112 MW and L&P as having 41 MW until it reviewed GMO's June 4, 2010, filing that initiated this case.[42]

Although GMO has not expressly stated it, like its goal for not rebasing its fuel adjustment clause—to maximize revenues while limiting the rate increase,[43] the primary goal of

---

[41] Ex. GMO—233, Surrebuttal Testimony of Lena M. Mantle, pp. 10-11.

[42] Ex. GMO-210, Staff Revenue Requirement Cost of Service Report, pp. 96-98.

[43] Ex. GMO—34, Rebuttal Testimony of Tim M. Rush, p. 26.

GMO's proposal for Iatan 2 is to limit the impact of Iatan 2 on the rates of its L&P retail customers, while still recovering all of its Iatan 2 costs—through MPS rates.[44] As noted earlier, KCPL and GMO proposed virtually the same percentage increases to the rates of KCPL, MPS and L&P retail customers—13.8%, 14.4% and 13.9%, respectively, in the tariff sheets they filed on June 4, 2010. With GMO's proposal, because MPS has nearly three times the customer base as L&P, the same increase in cost of service has a much lesser rate impact on its MPS customers than on its L&P customers.[45] GMO witness Rush quantified for L&P customers the difference between GMO's proposal and Staff's recommendation to be approximately an additional 12% increase in rates above GMO's 13.9% request, i.e., a total increase of approximately 26%.[46]

Although of less significance and not a basis for Staff's recommendation, Staff notes that GMO jointly dispatches its generating units to serve load in both the MPS and L&P, and has stated since it acquired St. Joseph Light and Power Company it has a long-term goal of having a uniform tariff, including uniform rates throughout its service territory.[47] GMO's proposal would have the impact of widening the gap between MPS and L&P rates;[48] Staff's would not.

GMO's retail rates for MPS and L&P not only differ significantly, they have differed significantly for many years. The following table not only shows, for residential customers, how much they differ now, it also shows how they have compared in the past to each other and to all of the electric utilities this Commission rate regulates.[49]

---

[44] Ex. GMO—33, Rebuttal Testimony of Tim M. Rush, pp. 11-12; Tr. Vol. 36, pp. 3802, 3809, 3819-20.

[45] Tr. Vol. 36, p. 3812.

[46] Tr. Vol. 36, pp. 3808-09.

[47] Ex. GMO-210, Staff Revenue Requirement Cost of Service Report, p. 95.

[48] Ex. GMO—232, Rebuttal Testimony of Lena M. Mantle, p. 6.

49 Ex. GMO—215, Direct Testimony of Cary G. Featherstone, p. 37.

Residential rate (¢/kWh)	2009	2008	2007	2006	2005
KCPL- Kansas	9.07	8.43	7.43	6.92	6.88
KCPL-Missouri	8.51	8.14	7.61	6.90	6.88
MPS	**9.67**	**9.10**	**8.64**	**8.08**	**7.45**
L&P	**7.43**	**7.03**	**6.78**	**6.31**	**5.97**
Ameren Missouri	7.03	6.53	6.60	6.60	6.52
Empire	9.75	9.19	9.10	8.35	7.98
Missouri Average	7.77	7.27	5.93	6.96	6.77
USA Average	11.72	11.52	10.95	10.62	9.60

As this table shows, current MPS residential rates exceed the average of Missouri residential rates of rate regulated utilities (9.67 ¢/kWh vs. 7.77 ¢/kWh) and current L&P residential rates are the average of Missouri residential rates of rate regulated utilities (7.43 ¢/kWh vs. 7.77 ¢/kWh).

CROSSROADS

GMO's statements of the Crossroads issues follow:

IV. GMO Only Issues

1. Crossroads:

   a. Should Crossroads be included in rate base at depreciated net book value in this proceeding? What is the appropriate valuation of Crossroads?

   b. If Crossroads is included in rate base, should the accumulated deferred taxes associated with Crossroads be used as an offset to rate base?

   c. Was a variance from the Commission's Affiliated Transaction Rule required to move Crossroads into GMO's rate base?

   d. Should the GMO cost of service include the hypothetical costs for 2 additional non-existing combustion turbines at South Harper?

Staff's statements of the fuel adjustment clause issues with its responsive position statements follow:

78. <u>Prudence of MPS Generating Capacity Additions</u> <u>(MPS only):</u>

b. Was the decision of MPS to wait to add the approximately 300 MW of capacity GMO is obtaining from Crossroads prudent?

Staff's position: No. Two additional 105 MW combustion turbines should have been installed in 2005 at a GMO site that would permit the building of six such combustion turbines.

c. If the Commission determines the addition of the approximately 300 MW of capacity from Crossroads was prudent, for purposes of setting rates for MPS, should the revenue requirement for the approximately 300 MW of capacity GMO is obtaining from Crossroads be based on the depreciated net book value of Crossroads on MPS's books and included in MPS's rate base?

Staff's position: No, it should be based on the costs of CTs installed in 2005 at a GMO site that would permit the building of six such combustion turbines because GMO

was imprudent by not acquiring the capacity of those two additional combustion turbines in 2005.

d. If the Commission determines the addition of the approximately 300 MW of capacity from Crossroads was prudent, for purposes of setting rates for MPS, should the revenue requirement for the approximately 300 MW of capacity GMO is obtaining from Crossroads be based on the present cost of two additional 105 MW combustion turbines installed in 2005 at a GMO site that would permit the building of six such combustion turbines (rate base) because GMO was imprudent by not acquiring the capacity of those two additional combustion turbines in 2005?

Staff's position: If the Commission determines the addition of the approximately 300 MW of capacity from Crossroads was prudent, the revenue requirement for the approximately 300 MW of capacity GMO is obtaining from Crossroads should be based on the present cost of two additional 105 MW combustion turbines installed in 2005 at a GMO site that would permit the building of six such combustion turbines (rate base) because GMO was imprudent by not acquiring the capacity of those two additional combustion turbines in 2005.

e. If the Commission determines the addition of the approximately 300 MW of capacity from Crossroads was prudent, should the accumulated deferred taxes associated with Crossroads be used as an offset to rate base?

Staff's position: Yes.

f. Was the transfer on GMO's books of Crossroads from non-regulated operations to the regulated operations of MPS at cost permitted by the Commission's Affiliated Transaction Rule without a variance from the Commission?

Staff's position: No.

g. If a value of Crossroads is included in rate base, should the transmission expense to get the energy from Crossroads to MPS's territory be included in expenses? If so, should the Commission reflect any transmission cost savings to the Company resulting in its future participation in SPP as a network service customer related to the Crossroads plant?

Staff's position: No, transmission expense to get energy from Crossroads to MPS territory should not be included in cost of service, but if the Commission disagrees, any cost savings from future participation in SPP as a network service customer related to the Crossroads plant should be an offset.

h. Would GMO be prudent to delay building additional combustion turbine capacity in order to utilize the power and asset sales offers by Dogwood in response to GMO's RFPs?

Staff's position: Staff has no position on this issue.

These issues have their genesis from GMO's anticipation in the late 1990's and early 2000's of the deregulation and decoupling of generation from regulated electric utility operations in Missouri and its forays into the energy market in Missouri and other states through a subsidiary, Aquila Merchant Services, Inc. As part of its merchant generation activities, in 2000, Aquila Merchant, with Calpine, built a natural gas-fired, 585 MW, combined-cycle, intermediate generating facility within GMO's service area using a five-year purchased power agreement with GMO that expired in May 2005 as an anchor for building the facility.[50] Aquila Merchant also

[50] Ex. GMO-210, Staff Revenue Requirement Cost of Service Report, p. 91.

purchased eighteen 75 MW model 7EA combustion turbines from General Electric and, in 2002, at least three 105 MW model 501D combustion turbines from Siemens-Westinghouse.[51]

Aquila Merchant used four of the 75 MW combustion turbines at the facility it built near Clarksdale, Mississippi in 2002—Crossroads Energy Center ("Crossroads").[52] Aquila Merchant sold, at substantial discounts from its cost, three of the 75 MW combustion turbines to nonaffiliates in 2003. Aquila Merchant released one of the 75 MW combustion turbines back to the manufacturer, and in 2003 installed six of them at the Goose Creek Energy Center and the other four at the Raccoon Creek Energy Center, both in Illinois.[53] Aquila Merchant kept the three 105 MW Siemens-Westinghouse combustion turbines it purchased in 2002 intending to install them at the 585 MW, combined-cycle generating facility for a purchased power agreement with GMO after the 5-year purchased power agreement with GMO expired in May 2005. When it could not sell them, they were stored until 2005 when they were installed as regulated MPS units at South Harper.[54] Aquila Merchant sold both its Goose Creek Energy Center and its Raccoon Creek Energy Center to Union Electric Company d/b/a AmerenUE (now d/b/a Ameren Missouri) at substantially below book value in 2006.[55] The table that follows shows the installed cost per kilowatt of 17 of the combustion turbines Aquila Merchant bought and took delivery of, and the price per kilowatt it received when it disposed of them:[56]

---

[51] Ex. GMO—215, Direct Testimony of Cary G. Featherstone, pp. 39, 48.

[52] Ex. GMO—216, Rebuttal Testimony of Cary G. Featherstone, p. 4.

[53] Ex. GMO—215, Direct Testimony of Cary G. Featherstone, pp. 47-51.

[54] *Id*. at pp. 39-40.

[55] *Id*. at p. 47.

[56] Ex. GMO--215, p. 51; Ex. GMO—262 Staff MPS Accounting Schedules 3-1, 3-2, 6-1 and 6-2.

Installed site	No. of Turbines	Date Installation / Sold	Cost	Capacity	Price per kilowatt
Raccoon Creek **Goose Creek**	4 6	2003 installed 2006 sold to Ameren	$175 million	850,000 kW	**$205.88**
South Harper	3	2001 Purchased 2005 installed	At Dec 31, 2010 Plant $120.4 million Reserve $24.4 Net $95.9	315,000 kW	**$382.16**
Crossroads	4	2002 installed 2008 transferred to MPS regulated	At Dec 31, 2010 Plant $119.2 million Reserve 32.1 Net $87.1 million Transmission upgrades (intangibles) Plant $22.5 million Reserve 4.4 Net $18.1 million Total Plant $141.7 million Reserve 36.5 Net $105.2 million	300,000 kW	**$427.46**

From early in the 1980's until it built South Harper in 2005, GMO exclusively relied on purchased power to meet its retail customers' increasing demands for electricity instead of building new generating units. Although every other investor-owned electric utility in Missouri built generation, GMO had a corporate policy not to build regulated generating units that it followed until it built South Harper in 2005.[57] As stated above, in doing so, in 2000, GMO entered into a five-year purchased power agreement to take power from a natural gas-fired, 585 MW, combined-cycle, intermediate generating facility within GMO's service area

[57] Ex. GMO—217, Surrebuttal Testimony of Cary G. Featherstone, pp. 34 and 39.

that ended in May of 2005. That agreement provided for 500 MW of capacity in the summer and 320 MW in the winter.[58]

GMO knew in 2000 when it began taking power under the five-year purchased power agreement that it would have to replace that capacity by June of 2005. GMO began exploring in 2001 what options might be available in 2005 to replace that needed 500 MW of capacity. It did so by issuing a request for proposals in the spring of 2001 for delivery of energy beginning in June of 2005. Because of changes in the industry, GMO reissued that request for proposals in early 2003.[59]

Staff has criticized and challenged GMO's capacity planning in rate cases over the past decade. It did so in Case Nos. ER-2001-672 and ER-2004-0034, criticizing GMO for entering into a five-year purchased power agreement for power from a 585 MW natural gas-fired combined cycle generating unit built by Calpine and GMO's affiliate Aquila Merchant Services, Inc., instead of building generation it owned. It did so in Case No. ER-2005-0436, challenging the prudency of how GMO built South Harper in the face of opposition to the siting of that facility and its decision to only install three 105 MW combustion turbines instead of five. And it did so in Case Nos. ER-2007-0004 and ER-2009-0090, again taking issue with the prudency of GMO installing three 105 MW combustion turbines in 2005 instead of five.

At GMO's June 26, 2003, resource planning update meeting with Staff and the Office of the Public Counsel, GMO presented the results of its analysis of the proposals it received. With the exception of one proposal, the proposals were for purchased power agreements, with

---

[58] Ex. GMO-210, Staff Revenue Requirement Cost of Service Report, p. 91; Ex. GMO—233, Surrebuttal Testimony of Lena M. Mantle, p. 4.

[59] Ex. GMO-210, Staff Revenue Requirement Cost of Service Report, Appendix 5, Sch. LMM-1,p. 1.

the source of the capacity and energy varying among wind, coal, combustion turbines and combined-cycle units. GMO also disclosed then that a bid for 600 MW of capacity which would be more than sufficient for its needs and that GMO considered to be "excellent" had been made to it. On September 10, 2003, Staff learned the bid had been withdrawn and not replaced.[60]

On January 27, 2004, only sixteen months before its 500 MW capacity agreement would expire, GMO met with and informed Staff of GMO's power acquisition process for the following five years. In that meeting GMO presented its preferred/proposed resource plan was to build what became South Harper, and enter into three-to-five year purchased power agreements for the balance of its resource needs based on the responses to the spring 2003 request for proposals. Staff responded it was concerned with the shortsightedness of the plan and that it viewed that GMO needed to be evaluating adding baseload generation because GMO should not become overly dependent on short-term purchased power agreements.[61]

At its next resource planning update, on February 9, 2004, GMO, based on a twenty-year planning period, disclosed that its least cost resource plan was to build five 105 MW combustion turbines in 2005 and buy a small amount of capacity from the market in 2005, meet load growth with additional market purchases until 2009, when it would build an additional 105 MW combustion turbine in 2009 and a second in 2010, as well as pursue adding baseload capacity for 2010. ***Therefore, in February of 2004, about sixteen months before its five-year 500 MW purchased power agreement expired, GMO's least cost resource plan included building five 105 MW combustion turbines in 2005***.[62]

---

[60] *Id*. at pp. 1-2.

[61] *Id*. at p. 2.

[62] *Id*. at p. 3.

At its following semi-annual update to Staff and the Office of the Public Counsel, held on July 9, 2004, eleven months before its five-year purchased power agreement ended, GMO disclosed it had entered into an agreement to purchase 75 MW of power from NPPD, but that its least cost plan still included building five 105 MW combustion turbines in 2005, although its preferred plan still was to build three 105 MW combustion turbines in 2005 and rely on purchased power for the balance of its needs. ***Therefore, in July of 2004 GMO's, about eleven months before its five-year 100 MW purchased power agreement expired, its least cost resource plan included building five 105 MW combustion turbines in 2005***.[63]

After prudently exploring and planning its capacity needs following the expiration of its five-year 500 MW purchased power agreement in May of 2005, rather than following its 2004 least cost resource plans to build five 105 MW combustion turbines, GMO instead built three 105 MW combustion turbines at South Harper, a site designed for up to six 105 MW combustion turbines. This decision not to build two more 105 MW combustion turbines was, for a regulated utility, imprudent. Ironically, GMO now says that transferring to its regulated operations at book value in 2008 300 MW of combustion turbine generation located in Mississippi that its unregulated affiliate Aquila Merchant unsuccessfully tried to sell in at least 2001 and 2005 is its least cost and preferred resource option.[64] Further, as Staff explained in some detail in the initial note on prudence section of its initial brief filed in this case, and the companion File No. ER-2010-0355 case, on March 10, 2011, GMO's imprudence continued in how it went about constructing South Harper. The construction of South Harper led to three final appellate

[63] *Id*.

[64] Ex. GMO—11, Rebuttal Testmony of Burton L. Crawford, pp.8-10.

court decisions,[65] at least two cases before this Commission[66] and enactment of legislation with a one year sunset.[67] It was also part of the focus of a Staff management audit of GMO.[68]

These three combustion turbines only replaced 315 MW of the 500 MW of generating capacity GMO needed in the summers. GMO entered a capacity agreement for 75 MW of power from NPPD and purchased power from Crossroads short-term for the remaining 200 MW.[69]

Since 2005, Staff has consistently taken the position it was imprudent for GMO to build only the three combustion turbines and rely on purchased power agreements for the balance of its power needs. And since 2005, Staff has included in its cost of service for GMO the costs of additional combustion turbines rather than the costs of the purchased power agreements GMO relied on to supply that power.[70] As stated above, ironically, with Crossroads, GMO now is seeking to include additional combustion turbine capacity for MPS, albeit located in Mississippi and based on booked values transferred in August of 2008, on the basis that doing so is both the least cost and its preferred resource.[71] Staff disputes GMO's claim that Crossroads is the least cost solution to GMO's capacity needs.

If the Commission agrees with Staff that two 105 MW combustion turbines built at South Harper should be imputed to the cost of service for MPS in lieu of Crossroads, Staff recommends the Commission value them together at $37.4 million as of May 31, 2005, less accumulated

---

[65] ***StopAquila.Org v. Aquila, Inc.,*** 180 S.W.3d 24 (Mo. App., W.D. 2005); ***StopAquila.Org v. City of Peculiar,*** 208 S.W.3d 895 (Mo. banc 2006); ***State ex rel. Cass County v. Public Service Commission,*** 259 S.W.3d 544 (Mo. App., W.D. 2008).

[66] Case Nos. EA-2005-0248 and EA-2006-0309.

[67] § 393.171, RSMo. 2000

[68] Case No. EO-2006-0356.

[69] Ex. GMO-210, Staff Revenue Requirement Cost of Service Report, Appendix 5, Sch. LMM-1, pp. 1 and 3.

[70] *Id*. at pp. 3-6.

[71] Ex. GMO—11, Rebutal Testimony of Burton L. Crawford, pp. 8-10.

depreciation through December 31, 2010.[72] The $37.4 million valuation as of May 31, 2005, is supported in the direct testimony of Staff witness Cary G. Featherstone. When depreciation and transmission, construction costs, common plant and allowance for funds used during construction, all unchallenged by GMO, are included with to the $37.4 million, the total impact on cost of service due to these two combustion turbines as of December 31, 2010, is $62.2 million.[73] Because Staff has included two 105 MW combustion turbines and GMO has included Crossroads, which has 300 MW of capacity, Staff's and GMO's cases differ by 95 MW of capacity.

Aside from the above prudency issue of when GMO should have added capacity, *i.e.*, that GMO should have built an additional 210 MW of capacity in 2005 instead of acquiring 300 MW in 2008, Staff has a number of concerns with including Crossroads in cost of service for MPS. Those concerns are 1) relying on book value when Crossroads was acquired from an affiliate;

2) the delivered price of natural gas to Crossroads has historically been higher than the delivered price of natural gas to South Harper; 3) the cost of transmission to move energy from Crossroads to MPS is substantially higher; 4) the special protection scheme in SPP for transmission of energy from Crossroads to MPS adds cost; and 5) the ability of GMO to properly provide managerial oversight to the plant.[74]

---

[72] Ex. GMO—215, Direct Testimony of Cary G. Featherstone, p. 42.

[73] Ex. GMO—267, Revised True-up Direct Cost of Service Staff Accounting Schedules, Sch. 3, p. 2.

[74] Ex. GMO—233, Surebuttal Testimony of Lena M. Mantle, p. 7.

VALUATION OF CROSSROADS

If the Commission rejects Staff's recommendation that it impute two additional 105 MW combustion turbines built at South Harper to the cost of service for MPS in lieu of Crossroads, then the Commission should not rely on the GMO's plant book value for Crossroads—$119.2 million as of December 31, 2010.[75] At December 31, 2010, the plant and transmission facilities values for Crossroads are:[76]

Plant in Service	$119.1 million
Depreciation Reserve	$ 32.1 million
Net Plant	$ 87.0 million
Transmission Rights -- Intangible)	$ 22.5 million
Reserve	$ 4.4 million
Net Transmission	$ 18.1 million
Total Crossroads Plant	$141.7 million
Reserve	$36.5 million
Net Plant	$105.2 million

GMO attempted to sell Crossroads at least ** [redacted] **[77] It follows that, absent a write-down which GMO has not taken, the market value of Crossroads is less than its booked value. Further, under the Commission's affiliate transactions rule, 4 CSR 240-20.015, when an asset is transferred to operations this Commission regulates, the asset is to be accounted for on the regulated books at the lower of cost or market value.

[75] Ex. GMO—267, Revised True-up Direct Cost of Service Staff Accounting Schedules, Sch. 3, p. 2.

[76] Ex. GMO—262 Staff MPS Accounting Schedules 3-1, 3-2, 6-1 and 6-2.

[77] Ex. GMO—216, Rebuttal Testimony of Cary G. Featherstone, p. 13.

In SEC filings made in connection with GPE's acquisition of Aquila, both GPE and GMO valued Crossroads at $51.6 million, for both production and transmission facilities; therefore, this is the market value of Crossroads as of July 14, 2008, and Staff recommends the Commission rely on this publicly stated valuation made by both GPE and GMO as the value, less depreciation accumulated since then, at which to value Crossroads in this case.[78]

While GPE did not pay book value for Crossroads, GMO is seeking Commission authorization and approval to charge its customers in rates as though GPE, and GMO, paid the full value of Crossroads stated on the non-regulated books of Aquila Merchant. When conducting its due diligence review of Aquila's assets for determining its offer price for Aquila, GPE would have considered the transmission constraints and other problems associated with Crossroads.[79] It is incomprehensible that GPE would pay book value for generating facilities in Mississippi to serve retail customers in and about Kansas City, Missouri. It is a virtual certainty GPE management was able to negotiate a price for Aquila that considered the distressed nature of Crossroads as a merchant plant which Aquila Merchant had tried for years to sell, but was unable to sell. Further, it is equally likely that GPE was in as good a position to negotiate a price for Crossroads as AmerenUE was when it negotiated the purchases of Raccoon Creek and Goose Creek, both located in Illinois, from Aquila Merchant in 2006.

Alternatively, only if the Commission disagrees with using $51.6 million as of January 14, 2008, as the basis for valuing Crossroads, Staff recommends the Commission instead rely on the values of the ten 75 MW General Electric model 7EA combustion turbines Aquila Merchant sold to AmerenUE in 2006. These are ten of the same eighteen 75 MW

[78] Ex. GMO—216, Rebuttal Testimony of Cary G. Featherstone, pp. 3 and 8.

[79] Ex. GMO—216, Rebuttal Testimony of Cary G. Featherstone, p. 7.

General Electric model 7EA combustion turbines Aquila Merchant bought at the same time, four of which it installed at Crossroads. The ten 75 MW General Electric model 7EA combustion turbines Aquila Merchant sold to AmerenUE are located at Goose Creek and at Raccoon Creek. They sold at an average installed cost of $205.88 per kW.[80] Based on that average installed cost of $205.88 per kW, the 300 MW of combustion turbines at Crossroads would have an installed cost of $61.8 million.

As stated above at the beginning of Staff's discussion of the Crossroads issues, in 2001, Aquila Merchant purchased a total of 21 combustion turbines. It offered three of them at below its cost to several entities, including KCPL, in 2002 before it stored them. These turbines were eventually installed at South Harper and are in MPS's rate base at a discount from what Aquila Merchant paid for them. Aquila merchant also sold thirteen other combustion turbines below its cost to buy them as follows:[81]

- Goose Creek—6 General Electric turbines sold to AmerenUE in 2006
- Raccoon Creek—4 General Electric turbines sold to AmerenUE in 2006
- Utility in Beatrice, Nebraska – 2 General Electric turbines sold in 2002
- Utility in Colorado – 1 General Electric turbines sold in 2002

All the above generating assets are now serving customers at prices consistent with the turbine market after the Enron collapse. Even GMO wrote-down from what Aquila Merchant paid for them the combustion turbines it installed at South Harper to comply with the Commission's affiliated transaction rule. Yet, in this case GMO is seeking to include the full

[80] Ex. GMO—215, Direct Testimony of Cary G. Featherstone, pp. 50-51.

[81] Ex. GMO—216, Rebuttal Testimony of Cary G. Featherstone, pp. 47 and 49.

value of Crossroads on its books, without a write-down, in MPS's rate base. Crossroads has additional problems as an asset serving MPS: transmission costs and natural gas prices. Even if Crossroads was located within MPS or L&P instead over 525 miles away in Mississippi, it still would be appropriate to write-down the value of the four combustion turbines at that facility.

Aquila Merchant bought the combustion turbines installed at Crossroads in 2001 when the turbine market was a "brutal sellers market," and combustion turbines were selling at all time highs.[82] GMO is requesting the Commission value these turbines based on that overly high valuation and include the significantly higher transmission and natural gas costs it will incur over the life of Crossroads. At the very least the Commission should not agree with GMO. Instead, it should rely on the $51.6 million at which GPE and GMO valued it when GPE acquired Aquila in 2008 or, alternatively, at $61.8 million based on the average installed dollar kilowatt basis AmerenUE paid for the combustion turbines at Raccoon Creek and Goose Creek in 2006.

DELIVERED NATURAL GAS PRICES

Historically the prices of natural gas delivered to Crossroads (Clarksdale, Mississippi have been higher than the prices of natural gas delivered to South Harper (Peculiar, Missouri). The commodity prices of natural gas are higher at Crossroads than at South Harper. Adding the natural gas reservation payments to the commodity price for natural gas at South Harper results in a higher natural gas price than the natural gas price that was paid at Crossroads the past two years—2009 and 2010.[83] Typically there has been a significant difference in the natural gas prices paid at South Harper near Peculiar, Missouri Kansas City and those paid at Crossroads

[82] Ex. GMO—215, Direct Testimony of Cary G. Featherstone, p. 58; Ex. GMO—217, Surrebuttal Testimony of Cary G. Featherstone, p. 6.

[83] Ex. GMO—217, Surrebuttal Testimony of Cary G. Featherstone, p. 44.

near Clarksdale, Mississippi. This difference has not been great recently, but historically has been significantly different. In addition, the prices paid for natural gas for GMO's Greenwood facility in Missouri are significantly lower than the prices for natural gas for Crossroads.[84]

The lower natural gas prices at Crossroads are offset by much higher electric transmission costs, discussed below.[85]

TRANSMISSION COST

The cost of transmission to move energy from Crossroads to customers served by MPS is a very significant cost that is far greater than the transmission costs for power plants located in the MPS district. It exceeds $4.8 million per year.[86] This higher transmission cost is an ongoing cost that will be paid every year that Crossroads is operating to provide electricity to customers located in and about Kansas City, Missouri. GMO does incur any transmission costs for its other production facilities that are located in its MPS district that are used to serve its native load customers in that district. This ongoing transmission cost GMO incurs for Crossroads is a cost that it does not incur for South Harper, and is the cause of one of the biggest differences in the on-going operating costs between the two facilities.

SPECIAL PROTECTION SCHEME

Crossroads is subjected to a the special protection scheme to ramp down the output of one of its four combustion turbines if a particular one of the two transmission lines used to move energy from Crossroads to MPS becomes unavailable. This risk of capacity loss is one of the

---

[84] *Id.*

[85] *Id.*

[86] Tr. Vol. 38, p. 4050.

transmission-related risks of Crossroads. MPS retail customers should bear neither the costs nor risks associated with the transmission limitations in getting electricity from Crossroads to MPS.[87]

PLANT MANAGERIAL OVERSIGHT

The ability of GMO to properly provide managerial oversight to the plant is greatly hampered by the long distance location of the plant facilities. Crossroads is located near Clarksdale, Mississippi—over 9 hours and 525 miles from Kansas City, Missouri. [88] To reduce transmission losses and outages power plants are built close to where the electricity is needed—close to customers. GMO has contracted with the City of Clarksdale, Mississippi to operate Crossroads under an agreement with the Clarksdale Public Utilities Commission.[89] No KCPL employees operate Crossroads; although with the exceptions of the Wolf Creek nuclear plant (of which KCPL is a minority owner) and the Jeffrey Energy Center (of which GMO is a minority owner), KCPL employees operate all other KCPL and GMO plants.[90]

DEFERRED INCOME TAXES

The accumulated deferred taxes associated with Crossroads should be applied as an offset to MPS's rate base.[91] Since Crossroads became part of the non-regulated operations of Aquila Merchant in 2002, deferred income taxes accumulated. In all instances, KCPL and GMO use deferred income taxes relating to regulated investment assets as an offset (reduction) to rate

---

[87] Ex. GMO—233, Surrebuttal Testimony of Lena Mantle, pp. 5-6.

[88] *Id.* at 42.

[89] Ex. GMO—31, Rebuttal Testimony of Marvin L. Rollison, p. 2.

[90] Tr. Vol. 38, pp. 4054, 4075 and 4079.

[91] Ex. GMO—210, Staff Revenue Requirement Cost of Service Report, p. 110.

base, except now for Crossroads. It is GMO's position that since Crossroads was not part of its regulated operations when those deferred taxes were created, they should not be used as an offset to MPS's rate base now. If the Commission authorizes GMO to rate base Crossroads in this case, then it is Staff's position that all the accumulated deferred income taxes associated with Crossroads should be offset against MPS's rate base.

JEFFREY FGD REBUILD PROJECT

GMO's statements of the Jeffrey FGD Rebuild Project issues follow:

IV. GMO Only Issues

2. Jeffrey Energy Center:

   a. Should the Jeffrey Rate Base Additions be included in rate base in this proceeding?

   b. Should the Commission presume that the costs of the Jeffrey Rate Base Additions were prudently incurred until a serious doubt has been raised as to the prudence of the investment by a party to this proceeding?

   c. Has a serious doubt regarding the prudence of the Jeffrey Rate Base Additions been raised by any party in this proceeding?

   d. Should the Company's conduct be judged by asking whether the conduct was reasonable at the time, under all the circumstances, considering that the Company had to solve its problem prospectively rather than in reliance on hindsight? ("prudence standard")?

   e. Has GMO demonstrated that it properly managed these complex projects and properly managed matters within its control?

Staff's statements of the Jeffrey FGD Rebuild Project issues with its responsive position statements follow:

84. Jeffrey Energy Center (Jeffrey) Flue Gas Desulphurization (FGD) Rebuild Project:

a. Should the Jeffrey FGD rebuild project costs be included in rate base in this proceeding?

Staff's position: Yes, net of Staff's adjustment.

b. Has doubt regarding the prudence or reasonableness of the Jeffrey FGD rebuild project been raised by any party in this proceeding?

Staff's position: Yes.

c. What should be the appropriate prudence standard regarding the costs of Jeffrey FGD rebuild project?

Staff's position: See Staff's Report filed on November 3, 2010 on pages 8-11. The Commission is not limited to disallowing imprudent costs. For example, the Commission may disallow costs that are not of benefit to ratepayers, and there does not need to be a showing of bad faith or abuse of discretion for the Commission to disallow such costs. *State ex rel. Laclede Gas Co. v. Public Serv. Comm'n*, 600 S.W.2d 222, 228-29 (Mo.App. W.D. 1980), *appeal dismissed*, 449 U.S. 1072, 101 S.Ct. 848, 66 L.Ed.2d 795 (1981); *State ex rel. Southwestern Bell Tel. Co. v. Public Serv. Comm'n*, 645 S.W.2d 44, 55-56 (Mo.App. W.D. 1982).

d. Did GMO prudently manage the Jeffrey FGD rebuild project?

Staff's position: No, because Westar, the manager of the project and the majority owner of the plant did not prudently manage the project in which GMO is an 8% owner. The Staff has raised a serious doubt concerning the prudence, reasonableness and/or appropriateness of certain costs of the Jeffrey FGD.

e. Has GMO carried its burden of proving the costs of the Jeffrey FGD rebuild project?

Staff's position: No.

The Jeffrey Energy Center ("JEC") is a coal-fired electric generating facility consisting of three 720 MW units located in St. Marys, Kansas. [92] GMO owns 8% of the JEC facility for a total of 172.8 MW, which is assigned to MPS. Westar is the operating partner who owns the remaining 92%.[93] To comply with increased environmental regulations, Westar made a decision

[92] Ex. GMO-210, Staff Revenue Requirement Cost of Service Report, p. 42, ll. 11-12.

[93] Ex. GMO-210, Staff Revenue Requirement Cost of Service Report, p. 42, ll. 12-14.

to rebuild the flue gas desulfurization system, or "scrubbers" on all three JEC units. Westar failed to require the largest vendor on the project, Powerplant Maintenance Specialists, Inc., to obtain a performance bond, exposing GMO to financial risks. The choice to engage this contractor and not require a performance bond was imprudent, inappropriate, unreasonable and unnecessary.

The Commission should accept Staff's $4.5 million adjustment related to the Jeffrey Energy Center Flue Gas Desulphurization rebuild project ("Jeffrey FGD Rebuild Project"). As an eight percent owner of JEC, GMO has an obligation to ensure that the Jeffrey FGD Rebuild Project expenditures were prudent. However, Westar imprudently contracted with a vendor whose financial instability and poor performance report resulted in additional costs to the project. And GMO did nothing to protect itself from these imprudent costs. This imprudence did not benefit the ratepayers and, thus, should be removed from GMO's cost-of-service.

In 2004, the U.S. Environmental Protection Agency (EPA) served a Notice of Violation at the JEC, identifying the need for compliance with new environmental regulations.[94] To avoid civil penalties, Westar decided to rebuild the cold-side electrostatic precipitators for particulate removal and the limestone-based wet flue gas desulfurization (FGD) systems, or "scrubbers" on each unit.[95] GMO agreed with Westar's decision to rebuild the scrubbers on all three JEC units.[96]

---

[94] Ex. GMO-210, Staff Revenue Requirement Cost of Service Report, p. 42, ll. 20-22.

[95] Ex. GMO-210, Staff Revenue Requirement Cost of Service Report, p. 42, ll. 15-17, 21-22.

[96] Ex. GMO-210, Staff Revenue Requirement Cost of Service Report, p. 43, l. 1.

The initial budget for the environmental upgrades at JEC was ** [redacted] **; therefore, GMO's share was ** [redacted] **.[97] ** [redacted] **[98] In Commission general rate cases, Case Nos. ER-2009-0090 and HR-2009-0092, on April 15, 2009, the Commission stated the following regarding the *Construction and Prudence Audits of the Environmental Upgrades at Iatan, Jeffrey Energy Center and the Sibley Generating Facility*, "[A]t the motion hearing for Case Nos. ER-2009-0090 and HR-2009-0092, GMO's counsel represented that the improvements to the Sibley and Jeffrey facility were on time and on budget . . . ."[99] Further, during Case Nos. ER-2009-0090 and HR-2009-0092, counsel for GMO indicated that the Jeffrey FGD Rebuild Project was on time and generally on budget.[100]

GMO's representations in the ER-2009-0090 and HR-2009-0092 cases were inaccurate. As of February 2009, the total dollars expended on the Jeffrey FGD Rebuild Project were ** [redacted] ** (total), of which GMO's share was ** [redacted] ** over the budget, which included a contingency.[101]

Powerplant Maintenance Specialist, Inc. (PMSI) was the largest vendor on the Jeffrey FGD Rebuild Project; it was the general construction work contractor.[102] PMSI's initial

---

[97] Ex. GMO-210, Staff Revenue Requirement Cost of Service Report, p. 43, ll. 2-3.

[98] Ex. GMO-210, Staff Revenue Requirement Cost of Service Report, p. 43, ll. 4-5.

[99] Case Nos. ER-2009-0090 and HR-2009-0092, *Construction and Prudence Audits of the Environmental Upgrades at Iatan, Jeffrey Energy Center and the Sibley Generating Facility*, issued April 15, 2009, p. 3; Ex. GMO-210, *Cost of Service Report*, p. 43, ll. 14-16.

[100] Case Nos. ER-2009-0090 and HR-2009-0092, *Construction and Prudence Audits of the Environmental Upgrades at Iatan, Jeffrey Energy Center and the Sibley Generating Facility*, Tr. Vol. 10, p. 28, ll. 13-23; Ex. GMO-210, *Cost of Service Report*, p. 43, ll. 19-22.

[101] Ex. GMO-210, Staff Revenue Requirement Cost of Service Report, p. 44, ll. 1-6.

[102] Ex. GMO-210, Staff Revenue Requirement Cost of Service Report, p. 44, ll. 9-10.

contract was for ** [redacted] **.[103] Westar's contract with PMSI was originally a fixed price contract without a performance bond.[104] GMO's witness, Leonard Ruzicka testified on cross-examination that ** [redacted] **.[105] While Westar and GMO did not require PMSI to obtain a performance bond, they required other contractors on the Jeffrey FGD Rebuild Project to obtain a performance bond.[106]

Burns & McDonnell was hired as the owners' engineer for the Jeffrey FGD Rebuild Project.[107] Burns & McDonnell provided monthly status reports that addressed project concerns, scheduling, and budget.[108] Burns & McDonnell stated in its June 2008 Status Report:

** [redacted]

[redacted]

[103] Ex. GMO-210, Staff Revenue Requirement Cost of Service Report, p. 44, ll. 11-12.

[104] Tr. p. 4252, ll. 12-14.

[105] Tr. p. 4282, ll. 12-18.

[106] Ex. GMO-210, Staff Revenue Requirement Cost of Service Report, p. 45, ll. 30-31; *See* Ex. GMO-210, Staff Revenue Requirement Cost of Service Report, Appendix 3, Schs. 6, 7 and 8.

[107] Ex. GMO-230, Staff Revenue Requirement Cost of Service Report, p. 44, ll. 14-15.

[108] Ex. GMO-230, Staff Revenue Requirement Cost of Service Report, p. 44, ll. 15-16.

[redacted]s

[redacted]4. **[109]

In contract Specification 203 – General Construction in where Burns and McDonnell recommended PMSI, the following statement appears:

** [redacted]

**[110]

It was unreasonable of Westar and GMO not to require PMSI to obtain a performance bond, and this failure to require a performance bond exposed GMO to inappropriate,

[109] Ex. GMO-230, Staff Revenue Requirement Cost of Service Report, p. 45, ll. 1-16; Appendix 3, Schedule 4.

[110] Ex. GMO-230, Staff Revenue Requirement Cost of Service Report, p. 45, ll. 21-27; Appendix 3, Schedule 5.

unreasonable and unnecessary level of financial risk, risk that materialized.[111] Mr. Ruzika testified that cash flow issues, bankruptcy, liquidity issues and termination in the past are all reasons a contractor would not be able to obtain a performance bond or a letter of credit.[112]

In its "due diligence" of PSMI Westar relied upon a financial stability memorandum performed by Jefferson Wells after Westar had already contracted with PMSI.[113] ** [redacted] **[114] Yet, Westar selected PMSI because its bid was substantially lower than next lowest bidder. This financial stability analysis was performed a year and a half after Westar executed its contract with PMSI.[115]

Westar failed to conduct proper due diligence when evaluating PMSI as a potential contractor. According to Black's Law Dictionary, the definition of "due diligence" is:

> "1. The diligence reasonably expected from, and ordinarily exercised by, a person who seeks to satisfy a legal requirement or to discharge an obligation – Also termed reasonable diligence."[116] GMO witness, Leonard Ruzicka, testified that "[w]hen the difference between the low and second low bidder is substantial, it would be appropriate and reasonable to consider waiving the bonding requirement but only after conducting the same type of due diligence that is conducted by the sureties."[117]

Federal Acquisition Regulations require:

> [T]o be determined reasonable, a prospective contractor must (A) have adequate financial resources to perform the contract or the ability to obtain them; (B) be

---

[111] Ex. GMO-210, Staff Revenue Requirement Cost of Service Report, p. 46, ll. 6-8.

[112] Tr. p. 4328, l. 4 – p. 4329, l. 24.

[113] Ex. GMO-230, Surrebuttal Testimony of Keith Majors, Sch. 8.

[114] *Id.*

[115] Ex. GMO—230, Surrebuttal Testimony Keith Majors, p. 37, ll. 16-18.

[116] BLACK'S LAW DICTIONARY 468 (7th ed. 1999).

[117] Ex. GMO—36, Rebuttal Testimony of Leonard R. Ruzicka, Jr., p. 3, ll. 9-11.

> able to comply with the required or proposed delivery or performance schedule taking into consideration all existing commercial and governmental business commitments; (c) have satisfactory performance record. A prospective contractor shall not be determined reasonable or non-reasonable solely on the basis of lack of relevant performance history except as provided in 9.104-2; and (D) have a satisfactory record of integrity and business ethics.[118]

Mr. Ruzika testified that during his tenure at FruCon he let government contracts.[119] He also testified that under federal contracting there is no leeway regarding the Federal Acquisition Regulations.[120] While the private industry is not required to follow the strict language contained within the Federal Acquisition Regulations, Westar took "leeway" in awarding the general construction contract to PMSI without a performance bond, to the detriment of GMO, who is seeking to pass that detriment to its retail customers through their rates. Moreover, Mr. Ruzika did not follow any auditing standards when reviewing the work related to PMSI, thus creating serious concerns to the value of his opinion testimony.[121]

PMSI yet again began experiencing cash flow problems and Westar began looking for a replacement contractor for PMSI.[122] Mr. Ruzicka testified that PMSI could easily have been replaced.[123] However, Westar decided to indulge PMSI's financial difficulties by amending the terms of the original contract. The PMSI contract changed from an ** [redacted] **.[124] Not only did Westar give PSMI carte blanche to pass through costs to construct with no incentive to contain

---

[118] Ex. GMO-260, Federal Acquisition Regulations, § 9.104-1.

[119] Tr. p. 4274, ll. 3-5.

[120] Tr. p. 4276, ll. 2-9.

[121] Tr. p. 4336, ll. 21-22.

[122] Tr. p. 4253, ll. 2-3.

[123] Tr. p. 4278, ll. 18-19.

[124] Tr. pp. 6-16.

those costs, Westar also gave PSMI an ** [redacted] **[125] This contract addendum resulted in substantial increases to the overall Jeffrey FGD Rebuild project cost.

GMO admitted in its response to Staff Data Request No. 0346 that Westar's ** [redacted] **.[126] Further, GMO admitted that ** [redacted] **.[127] In the contract addendum, Westar ** [redacted] **.[128] Contrary to Westar's ** [redacted] **.[129]

Regardless that GMO was only an eight percent owner of JEC, it still had an obligation to ensure the costs of the Jeffrey FGD Rebuild Project were prudent.[130] Staff has provided the Commission with substantial evidence that ** [redacted] **.[131] Westar's lack of concern over a contractor's financial stability is alarming. Its lack of due diligence and

[125] Ex. GMO-230, Surrebuttal Testimony of Keith Majors.

[126] Tr. p. 4262, ll. 1-16; Ex. GMO-258, Response to Staff Data Request No. 0346.

[127] Tr. p. 4265-66, Ex. GMO-259, Response to Staff Data Request No. 0346.1.

[128] Tr. p. 4318, ll. 19-23.

[129] Ex. GMO-230, Surrebuttal Testimony of Keith Majors, p. 35, ll. 23-27.

[130] Tr. p. 4267, ll. 5-7.

[131] Ex. GMO-230, Surrebuttal Testimony of Keith Majors, p. 33, ll. 8-10, s*ee also* p. 33, l.. 16 to p. 35, l. 18.

willingness to continue working with a contractor who practically defaulted on its contract resulted in substantially higher project costs. These costs were imprudently incurred and would harm ratepayers if the Commission allows them into the cost of service for MPS. The Commission should accept Staff's $4.5 million adjustment related to the Jeffrey FGD Rebuild Project.

CONCLUSION

WHEREFORE, for the reasons set forth above, the Staff requests the Commission to adopt the Staff's position on each and every KCP&L Greater Missouri Operations Company specific issue that was presented in this case.

Respectfully submitted,

/s/ Nathan Williams
Nathan Williams
Deputy Counsel
Missouri Bar No. 35512

Attorney for the Staff of the
Missouri Public Service Commission
P. O. Box 360
Jefferson City, MO 65102
(573) 751-8702 (Telephone)
(573) 751-9285 (Fax)
nathan.williams@psc.mo.gov

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 25th day of March 2011.

/s/ Nathan Williams