

Exhibit No.:

Issues: MEPPH Capacity
Contract & Off-System
Sales

Witness: Stephen L. Ferry

Sponsoring Party: Missouri Public
Service

Case No.: ER-2001-672

Before the Public Service Commission
of the State of Missouri

FILED²

JAN 22 2002

Surrebuttal Testimony

Missouri Public
Service Commission

of

Stephen L. Ferry

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**BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI
SURREBUTTAL TESTIMONY OF STEPHEN L. FERRY
ON BEHALF OF MISSOURI PUBLIC SERVICE,
A DIVISION OF UTILICORP UNITED INC.
CASE NO. ER-2001-672**

1 Q. Please state your name and business address.

2 A. My name is Stephen L. Ferry. My business address is 10750 East 350 Highway, Kansas
3 City, Missouri.

4 Q. Are you the same Stephen L. Ferry who submitted direct and rebuttal testimonies in this
5 case?

6 A. Yes.

7 Q. What is the purpose of your surrebuttal testimony?

8 A. The purpose of this testimony is to rebut testimony in this case of Missouri Public
9 Service Commission Staff ("Staff") witness Cary G. Featherstone on the issue of off-
10 system sales; and Staff witnesses Featherstone and Mark B. Oligschlaeger on the issue of
11 the capacity purchase from MEP Pleasant Hill ("MEPPH").

12 Q. How is your surrebuttal testimony organized?

13 A. My surrebuttal testimony is organized as follows:

14 I. Off-System Sales

15 II. MEP Pleasant Hill Unit Participation Purchase

I. OFF-SYSTEM SALES

Q. Regarding Mr. Featherstone's rebuttal testimony on off-system sales, what issues will you be addressing in this surrebuttal testimony?

A. I will address margin sharing, and the true-up of off-system sales expense and revenue in this case.

Q. At page 4, lines 15 – 17 of his rebuttal testimony in this case, Mr. Featherstone states, "By reducing the level of off-system sales levels by half – a 50% sharing to the shareholders – the Company is increasing the overall revenue requirement in this case by a corresponding amount." Does sharing the margins associated with off-system sales between the ratepayer and the Company increase overall revenue requirement, and thereby increase rates?

A. Not in the long run. While it's true that sharing margins will have the short-term effect of raising revenue requirement, it will have the long-term effect of lowering revenue requirement.

Q. Why?

A. Retaining a portion of the margins associated with off-system sales motivates the Company to be more aggressive in pursuing off-system sales, and therefore increases total margins. The Company believes that the corresponding increase in margins will overcome any short-term increase in revenue requirement brought about by margin sharing. These additional margins would be included in the next rate case, and thereby

1 lower rates.

2 Q. Does any other jurisdiction permit sharing of off-system sales margins?

3 A. Yes. MPS became aware, on January 16, 2002, that Oklahoma permits a 50% sharing of
4 margins associated with off-system sales. The sharing is addressed in a January 2, 1997,
5 stipulation and settlement agreement between the Corporation Commission of the State of
6 Oklahoma and Okalahoma Gas and Electric Company. A copy of the stipulation and
7 settlement agreement is attached to this surrebuttal testimony as Schedule SLF-3.

8 Q. At page 7, line 24 through page 8, line 2 of his rebuttal testimony, Mr. Featherstone
9 states, "To the extent that off-system sales increase over time, the shareholders get the
10 direct benefit of any levels above those rates. Thus, under the traditional approach of
11 including all off-system sales margins in the revenue requirement determination, both
12 customers and shareholders benefit." Do you agree with Mr. Featherstone's statement?

13 A. Partial agreement only. It's true that regulatory lag allows the Company to retain margins
14 above the levels set in rates, but in order for that to happen the margins must exceed the
15 levels imputed to rates. And for that (i.e., margins exceeding the levels set in the rates) to
16 happen, market conditions, after rates are set, must be more favorable than the conditions
17 that were assumed for rate-making purposes. Based on the current trend of declining off-
18 system sales revenues cited in my rebuttal testimony in this case, the wholesale energy
19 market, from the seller's perspective, is now in decline. Thus, to base rates in this case
20 by giving all margins to the ratepayer will most likely result in MPS under-recovering its

1 costs.

2 Q. Why is the wholesale energy market declining?

3 A. Primarily due to increased supply over what has been available since 1998 and

4 transmission constraints. I provide more detail on this in my response to Mr.

5 Featherstone's Data Request No. MPSC-0606. I have included a copy of MPS' response

6 to that Data Request in this surrebuttal testimony as Schedule SLF-1.

7 Q. Did the Staff and MPS agree to true-up off-system sales in this case?

8 A. Yes. The agreement was acknowledged by Mr. Featherstone at page 11, lines 1 – 8 of his
9 rebuttal testimony.

10 Q. What is Staff's position on a true-up of off-system sales?

11 A. Staff's position is given on page 11, lines 9 – 18 of Mr. Featherstone's rebuttal testimony.

12 I interpret what he says to mean Staff agreed to true-up off-system sales, but since no

13 specific methodology was agreed to, Staff is obligated to only review actual operating

14 data at January 31, 2002, but not necessarily use it in the annualization of expenses and

15 revenues in this case.

16 Q. Is there any special methodology required to true-up off-system sales expenses and
17 revenues?

18 A. Not to my knowledge. I understand true-up to mean updating expenses and revenues to a
19 certain point in time; in this case January 31, 2002.

20 Q. Is it appropriate to true-up off-system sales revenues and expenses to the twelve months

1 ending January 31, 2002?

2 A. Yes. As I stated in my rebuttal testimony, truing-up off-system sales revenues and
3 expenses to January 31, 2002 would make off-system sales consistent with the other fuel
4 and purchased power items in the true-up.

5 Q. Why do off-system sales need to be consistent with the other fuel and purchased power
6 items in the true-up?

7 A. The expenses and revenues associated with off-system sales are dependent on the
8 wholesale market, which I previously discussed in this surrebuttal testimony, and on the
9 cost to produce the energy associated with the sales. Those costs include the cost for fuel
10 and purchased power. A change in the cost of fuel and purchased power will change the
11 expense associated with providing energy for off-system sales, which changes the price,
12 and the resulting revenue. Thus, truing-up fuel and purchased power costs without
13 truing-up expenses and revenues associated with off-system sales creates an apples and
14 oranges situation.

15 Q. Are there any other reasons for truing-up off-system sales to January 31, 2002?

16 A. Yes. In the event that the Commission decides to base fuel and purchased energy in this
17 case on Staff's joint dispatch of the MPS/SJLP systems, then off-system sales need to be
18 consistent with the joint dispatch approach.

19 Q. Please explain.

20 A. In its direct-filed case, the Company developed its annualized fuel and purchased energy

1 expense using a production cost model of the MPS stand-alone system. Sales associated
2 with the twelve months ending December 31, 2000 were consistent with that fuel model,
3 because MPS did not begin joint dispatch of the MPS/SJLP systems until August 2001.
4 In developing its fuel and purchased energy expense, Staff used a production cost model
5 of the jointly-dispatched MPS/SJLP system. Jointly dispatching the MPS and SJLP
6 systems reduces expenses from those that would have been experienced from operating
7 the systems on a stand-alone basis. For example, using the Staff's fuel model results as
8 reported in Schedule 2 of Staff witness David W. Elliott's rebuttal testimony in this case,
9 the savings associated with the joint dispatch of MPS and SJLP were estimated to be \$6.5
10 million, \$5.1 million of which were allocated by Staff to MPS. The majority of these
11 savings occur because energy that is surplus in one of the systems is transferred at cost to
12 the other system and is used to replace higher cost energy that would have been generated
13 or purchased. While transferring the surplus energy to the other system reduces expenses
14 in the other system, it also reduces the opportunity to market that same energy on the
15 wholesale market, and therefore reduces the opportunity for off-system sales. As a result,
16 if Staff's joint dispatch approach is used to set rates in this case, then the level of off-
17 system sales needs to be adjusted from the level occurring in the twelve months ending
18 December 31, 2000.

19 Q. What is an appropriate level of off-system sales to be included in this case?

20 A. If the Commission decides to base fuel and purchased energy expense in this case on

1 Staff's joint dispatch of the MPS/SJLP systems, I recommend that off-system sales
2 revenue and expense be trued-up to reflect actual MPS sales for the twelve-month period
3 ending January 31, 2002. In the event that the Commission should decide to not true-up
4 off-system sales, then fuel and purchased energy expense in this case should be based on
5 a stand-alone MPS system. Using Staff's MPS stand-alone fuel run with fuel prices
6 trued-up through January 31, 2002 (estimated), annualized fuel and purchased energy
7 expense for the stand-alone MPS system would be \$76,007,370.

8 Q. Since joint dispatch of the MPS/SJLP systems didn't occur until August 2001, doesn't
9 truing-up sales to the twelve months ending January 31, 2002 still include sales based on
10 MPS stand-alone operation for the months of February 2001 through July 2001?

11 A. Yes. MPS recognizes that sales trued-up through January 31, 2002 will still result in
12 annualized sales being higher than those that would have occurred if joint dispatch of the
13 MPS/SJLP systems had been implemented in February 2001. However, MPS is willing
14 to accept the higher but unrepresentative level of sales in the case solely in the interest of
15 resolving this issue.

16 **II. MEP Pleasant Hill Unit Participation Purchase**

17 Q. Regarding Staff's testimony on the MEPPH purchase, what issues will you be addressing
18 in this surrebuttal testimony?

19 A. I will address Mr. Featherstone's rebuttal testimony pertaining to in-service criteria.

20 Q. Beginning at page 15, line 15 and continuing to page 16, line 22, Mr. Featherstone

1 discusses the need for MPS to demonstrate that the Aries plant has met Staff's in-service
2 criteria before the MEPPH purchase contract expenses can be included in MPS' rates. Do
3 you agree with Mr. Featherstone's position?

4 A. No. The in-service criteria referenced by Mr. Featherstone was intended to be applied to
5 a generating unit placed in-service by Empire District Electric Company ("Empire").
6 That unit was a rate-based facility. MPS did not build the Aries facility, nor does it own
7 it. The Aries plant is a merchant plant, it is not a rate-based facility. MPS purchases
8 power from the plant under the terms of a purchased power agreement.

9 Q. Has Staff provided MPS with a copy of the in-service criteria for the Aries plant?

10 A. No. Staff has not provided such document to MPS.

11 Q. Has Staff provided MPS with a copy of the in-service criteria for the MEPPH purchase?

12 A. No. Staff has not provided such document to MPS.

13 Q. Does Mr. Featherstone identify any examples in his rebuttal testimony where the Staff's
14 in-service criteria for the Empire unit was applied to a purchase power agreement?

15 A. No. The Empire unit he references is a rate-based facility.

16 Q. Should Staff's in-service criteria for the Empire unit be applied to the MEPPH purchase?

17 A. No.

18 Q. Why not?

19 A. MPS' responsibility under the MEPPH purchase is to pay for power it (MPS) buys from
20 MEPPH. MEPPH's responsibility is to provide that power. MEPPH intends to use the

1 Aries plant to provide this power, but it (MEPPH) may, at its option, provide the power
2 from an alternate source.

3 Q. Has MEPPH acknowledged its obligation to provide power and energy under the
4 contract?

5 A. Yes. This acknowledgement is contained in the January 7, 2002, letter from MEPPH to
6 MPS. I have attached a copy of that letter to this surrebuttal testimony as Schedule SLF-
7 2. As long as MEPPH provides the power for which it contracted with MPS to sell,
8 regardless of whether it is sourced from Aries or not, MEPPH satisfies its obligations
9 under the contract. And since MPS receives the power for which it contracted, its
10 requirements under the contract are satisfied. As a result, Staff's in-service criteria for
11 the Empire unit, which does not address receipt of power under a purchase power
12 agreement, isn't applicable to the MEPPH purchase.

13 **Summary**

14 Q. Please summarize your recommendations regarding off-system sales.

15 A. Regarding margin sharing, the Company believes that sharing the margins associated
16 with off-system sales between the ratepayer and the Company, rather than imputing all
17 margins to the ratepayer, provides an incentive to the Company to be more aggressive in
18 pursuing off-system sales, and ultimately will benefit the customer. Staff's contention
19 that regulatory lag alone provides this incentive is untrue, especially in a declining
20 wholesale market.

1 Regarding the true-up of off-system sales, revenues and expenses associated with off-
2 system sales in this case should be trued-up to the twelve months ending January 31,
3 2002. This true-up would make off-system sales consistent with the true-up of other fuel
4 and purchased power items in this case; it would also make off-system sales consistent
5 with Staff's proposal to base fuel and purchased energy expense on a jointly dispatched
6 MPS/SJLP system. If the Commission should decide not to true-up off-system sales,
7 then fuel and purchased energy expense in this case should be based on a stand-alone
8 MPS system.

9 Q. Please summarize your recommendations regarding the MEPPH Pleasant Hill Unit
10 Participation Purchase.

11 A. MPS purchases power from MEPPH under the MEPPH purchase agreement. MEPPH
12 may provide this power from the Aries plant or an alternate source. The in-service
13 criteria for the Empire unit does not address receipt of power under a purchase power
14 agreement. Staff's proposal to apply its in-service criteria for the Empire rate-based unit
15 to the Aries merchant plant is inappropriate.

16 Q. Do you have any other concluding remarks regarding the MEPPH purchase?

17 A. Yes. Throughout its testimony in this case, Staff has attempted to paint the picture that
18 the MEPPH purchase is somehow improper; this in spite of Staff's support of the
19 purchase in Case No. EM-99-369. In that case, the Staff's Michael S. Proctor concluded
20 that the MEPPH purchase:

1. Would benefit Missouri customers;
2. Did not violate any state law;
3. Would not provide MEPPH any unfair competitive advantage by virtue of its affiliation or association with UtiliCorp;
4. Is in the public interest.

Contrary to what Staff would have the Commission think, MPS played by the rules in arriving at the MEPPH contract:

1. MPS properly identified the need for the capacity using Missouri's Integrated Resource Planning process;
2. MPS issued an RFP for the capacity;
3. Staff and Office of Public Counsel ("OPC") reviewed the RFP before it was issued;
4. Staff and OPC reviewed the bids that were returned under the RFP;
5. Aquila's proposal to supply capacity and energy under a purchase power agreement ("PPA") was the low bid;
6. Aquila elected to provide the capacity and energy associated with its bid from the Aries project; but under the contract could also provide the power and energy from an alternate source;
7. The power contract was determined to be an EWG contract which required regulatory approval from the Federal Energy Regulatory Commission

1 ("FERC") and the Missouri Commission. These approvals were obtained.

2 8. The PPA became effective June 1, 2001 for 320 MW;

3 9. The PPA became effective January 1, 2002 for 200 MW for twelve
4 months a year plus an additional 300 MW for the months of April through
5 September.

6 I agree with Dr. Proctor's assessment that the MEPPH agreement 1) benefits Missouri
7 customers; 2) does not violate any state law; 3) does not provide MEPPH unfair
8 competitive advantage; and 4) is in the public interest.

9 Q. Does this conclude your testimony at this time?

10 A. Yes.

UTILICORP UNITED
CASE NO. ER-01-672
DATA REQUEST NO. MPSC-606

DATE OF REQUEST: January 14, 2002
DATE RECEIVED: January 15, 2002
DATE DUE: January 22, 2002
REQUESTOR: Cary Featherstone

QUESTION:

With respect to UtiliCorp witness Ferry's rebuttal testimony, page 12, lines 3 and 4, wherein it is stated that "the projected revenue in 2001 is only \$6 million", please provide the following:

1. Identify and describe all reasons why there is expected to be a significant reduction to off-system sales revenues in 2001 from the levels achieved in the 12-months ending June 30, 2001, and calendar years 2000, 1999, 1998, 1997, 1996.
2. Provide all support for the reasons of this projected reduction in off-system sales from those that have been achieved from previous years.

RESPONSE:

1. Please refer to MPS' response to Data Request No. MPSC-0602 in this case. The projected revenues of \$6 million given in Ferry's rebuttal are now actual revenues of \$6.4 million.

Revenues have declined because of declining spot-market volatility and prices. For example, in January of 2000 the summer prices per MWH for the Cinergy and Entergy hubs were approximately \$136 and \$132 respectively. Summer 2002 today is at \$49 and \$44.25. The declines in volatility and prices have been brought about by:

- a. Increasing Supply. Cambridge Energy Research Associates ("CERA") reported in its December 2001 report titled "Recession Deepens Down Phase in Power Markets", that since 1998, 5,823 MW of generating capacity has been added in SPP with 4,552 MW currently under construction; 9,448 MW added in MAIN with 6,759 MW more under construction; and 10,732 MW added in ECAR with 8,739 MW additional under construction; and 1,702 MW added in MAPP with 128 MW under construction. These capacity additions have raised capacity margins in the named regions in 2002 and 2003 respectively to: SPP at 28% and 29%, MAIN at 27% and 28%, ECAR at 24% and 24%, and MAPP at 23% and 22%. Historically, 1996 - 2000, capacity margins have been 12% to 20%.
- b. Transmission Constraints. For the summer of 2001, MPS was unable to buy monthly firm transmission from any control area located in SPP to deliver to MPS. MPS was also unable to procure transmission from WPEK to Entergy. Additionally, MPS was unable to obtain access across Ameren in either direction

for summer 01, 02 and 03. All of these transmission constraints have reduced MPS ability to make sales.

2. Please see response to part 2 above.

ATTACHMENTS:

ANSWERED BY: Steve Ferry



MEP PLEASANT HILL, LLC ARIES POWER PROJECT

25111 E. 175TH STREET
P.O. Box 110
PLEASANT HILL, MO 64080
TEL 816 • 540 • 2800
FAX 816 • 540 • 3058

January 7, 2002

Mr. Steve Pella
Missouri Public Service
10700 E. 350 Highway
Kansas City, Missouri 64138

Re: Power Sales Agreement dated February 22, 1999

Dear Mr. Pella:

Pursuant to the above-referenced Power Sales Agreement (PSA) between MPS and MEPPH, MEPPH has declared to MPS that MEPPH is ready to provide service under the PSA effective as of January 1, 2002, all as provided for in Sections 1.4 and 3.1 of the PSA. MEPPH is prepared to provide such equivalent service to MPS from alternative resources in accordance with the terms and conditions of the PSA upon MPS providing scheduling instructions pursuant to Section 6.1 of the PSA and the scheduling arrangements that were in place while the Missouri Generator was in simple cycle operation last year. MPS has advised Aquila that MPS has adequate capacity to receive this firm energy at the proposed alternate delivery point. Please do not hesitate to contact me if I may be of further service in regard to this matter.

Sincerely,

Barry O'Brien
Chairman, Management Committee
MEP Pleasant Hill, LLC

cc: PSA Operating Committee

"ATTACHMENT A"

BEFORE THE CORPORATION COMMISSION OF THE STATE OF OKLAHOMA

IN THE MATTER OF THE APPLICATION OF)
 OKLAHOMA GAS AND ELECTRIC COMPANY)
 FOR AN ORDER OF THE COMMISSION)
 AUTHORIZING APPLICANT TO MODIFY ITS)
 RATES, CHARGES AND TARIFFS FOR RETAIL)
 ELECTRIC SERVICE IN OKLAHOMA)

Cause No. PUD 960000116

FILED
 JAN 02 1997

JOINT STIPULATION AND SETTLEMENT AGREEMENT COURT CLERK'S OFFICE - OKC
 CORPORATION COMMISSION
 OF OKLAHOMA

COME NOW the undersigned parties to the above entitled cause and pursuant to 17 O.S. §282 present the following Joint Stipulation and Settlement Agreement for the Commission's review and approval as their compromise and resolution of all issues between the parties to this Joint Stipulation ("Stipulating Parties"). The Stipulating Parties represent to the Commission that this Joint Stipulation represents a fair, just and reasonable settlement of these issues, that the terms and conditions of the Joint Stipulation are in the public interest, and the Stipulating Parties urge the Commission to issue an Order in this Cause which adopts and approves this Joint Stipulation.

It is hereby stipulated and agreed by and between the Stipulating Parties as follows:

Terms of the Joint Stipulation and Settlement Agreement

1. **Jurisdictional Rates.** The Stipulating Parties represent and agree that Oklahoma Gas & Electric Company (hereinafter "Company", "OG&E", or "Applicant") shall file tariffs designed to produce Oklahoma jurisdictional operating revenues of \$976,082,881 based upon the test year billing units reflected in Section M of the Company's Application Package, all as set forth in paragraph 2 of this Joint Stipulation and Settlement Agreement. In conjunction with the Company's rate schedules authorized to be filed effective with the first billing period in the Month of March, 1997, OG&E will be authorized to file a Rider for Off-System Sales of Electricity and a Performance Based Rider for Generation Efficiency, each of which are described in the next succeeding subparagraphs.

(a) **Rider for Off-System Sales of Electricity.** The Company will be permitted to file a Rider for Off-System Sales of Electricity, by the terms of which OG&E will share, on a 50%-50% basis with its customers, profits associated with its non-jurisdictionally allocated firm sales and its spot-market off-system sales of electricity, with profits derived therefrom

EXHIBIT 320

Joint Stipulation and Settlement Agreement

Cause No. PUD 960000116

to be the difference between the sales price of the electricity and the costs associated with such sales of such electricity excluding variable operation and maintenance costs.

(b) **Performance Based Rider for Generation Efficiency.** The Company will be permitted to file a Performance Based Rider for Generation Efficiency. By its terms, OG&E's actual (fossil) fuel costs (as reported on FERC Form 1,¹ consistent with KRZ-3 notes 1 and 2) will be compared to the following standard. The standard is the actual Weighted Average Cost of (fossil) Fuel (WACOF) for the Specified Investor Owned Utilities (hereinafter referred to as the "SPP WACOF"), as listed on Page 2 of Exhibit KRZ-3 dated October 21, 1996, including notes 1 and 2, all as reflected on Appendix 1 to this Joint Stipulation and Settlement Agreement which is made a part hereof. The formulae for the Performance Based Rider for Generation Efficiency are:

- 1) If OG&E's actual cost of fossil fuel is greater than 103.739 percent of the SPP WACOF ($1.03739 \times \text{SPP WACOF}$), then the rider shall be

$$\frac{(\text{SPP WACOF} \times 1.03739) - \text{OG\&E's WACOF}}{3}$$

or

- 2) If OG&E's actual cost of fossil fuel is less than 96.261 percent of the SPP WACOF ($.96261 \times \text{SPP WACOF}$), then the rider shall be

$$\frac{(\text{SPP WACOF} \times .96261) - \text{OG\&E's WACOF}}{3}$$

or

- 3) If OG&E's actual cost of fossil fuel is equal to or less than $1.03739 \times \text{SPP WACOF}$ and equal to or greater than $.96261 \times \text{SPP WACOF}$ then the dollar per kilowatthour value of the Rider is zero.

¹As currently reported on

Page 401 (lines 3 and 7) Sources of Energy -
STEAM megawatt hours and Sources of
ENERGY - Other megawatt hours, and
Page 320 (line 5) Steam Power Generation -
Fuel (Account 501) and page 321 (line 63)
Other Power Generation Fuel (Account 547)

**BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI**

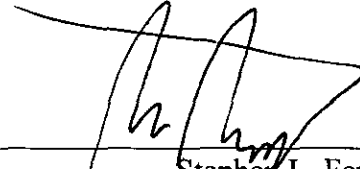
In the matter of Missouri Public Service)
of Kansas City, Missouri, for authority)
to file tariffs increasing electric rates)
for service provided to customers in the)
Missouri Public Service area)

Case No. ER-2001-672

County of Jackson)
) ss
State of Missouri)

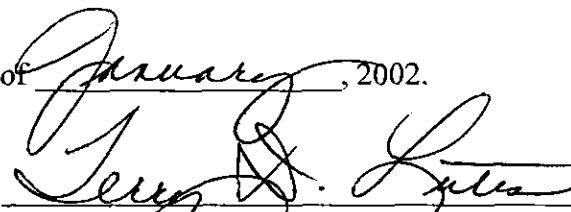
AFFIDAVIT OF STEPHEN L. FERRY

Stephen L. Ferry, being first duly sworn, deposes and says that he is the witness who sponsors the accompanying testimony entitled "Surrebuttal Testimony of Stephen L. Ferry;" that said testimony was prepared by him and under his direction and supervision; that if inquiries were made as to the facts in said testimony and schedules, he would respond as therein set forth; and that the aforesaid testimony and schedules are true and correct to the best of his knowledge, information, and belief.



Stephen L. Ferry

Subscribed and sworn to before me this 21st day of January, 2002.



Notary Public

My Commission expires:

8-20-2004

