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Case No.: ER-2010-0355
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MISSOURI PUBLIC SERVICE COMMISSION

CASE NO.: ER-2010-0355

REBUTTAL TESTIMONY

OF

LARRY W. LOOS

ON BEHALF OF

KANSAS CITY POWER & LIGHT COMPANY

**Kansas City, Missouri
December 2010**

KCP&L Exhibit No. KCP&L40
Date 2/4/11 Reporter LMB
File No. ER-2010-0355

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REBUTTAL TESTIMONY

OF

LARRY W. LOOS

Case No. ER-2010-0355

INTRODUCTION

1 **Q: Please state your name and business address.**

2 A: Larry W. Loos, 11401 Lamar, Overland Park, KS, 66211.

3 **Q: Are you the same Larry W. Loos who prefiled Direct Testimony in this matter?**

4 A: Yes, I am.

5 **Q: What is the purpose of your rebuttal testimony?**

6 A: I will respond to the issue of the allocation of off-system sales margins raised in the Staff
7 Report and in the testimony of Mr. Greg Meyer on behalf of certain industrial customers.
8 In this regard, I sponsor Schedule LWL2010-13.

9 **Q: How does Staff recommend allocating off-system sales margins?**

10 A: Though not entirely clear, at Page 187 of the Staff Report, Staff suggests allocating off-
11 system sales based on annual sales. Staff does not make a definitive recommendation
12 regarding the allocation of off-system sales revenues, much less off-system sales margin.

13 **Q: How does Mr. Meyer recommend allocating off-system sales margins?**

14 A: At Page 13 of his direct testimony, Mr. Meyer recommends allocating off-system sales
15 margins based on the energy allocator.

16 **Q: Do you agree with Staff and Mr. Meyer's recommendation?**

17 A: No, I do not. As I discuss in detail beginning at Page 38 of my direct testimony, I
18 recommend the Commission reject an energy allocation of off-system sales margin. I

1 recommend allocating off-system sales margins based on the allocation of the fixed costs
2 associated with the generating resources used to generate energy sold off-system.¹

OFF-SYSTEM SALES VS. SALES REVENUES VS. SALES MARGINS

3 **Q: In your prior response, you indicate in response to the question of the allocation of**
4 **off-system sales margin that Staff suggests allocating off-system sales based on**
5 **energy. Do you mean to imply that off-system sales margin represents the same**
6 **thing as off-system sales?**

7 **A:** No, I do not. However, both Staff and Mr. Meyer would ignore this distinction. Off-
8 system sales (more properly off-system sales revenues) represent the dollar amount
9 KCP&L realizes from the sale of energy in bulk power supply markets outside of
10 KCP&L's control area. Off-system sales margin represents the contribution to fixed
11 costs provided by off-system sales. Off-system sales margin is equal to off-system sales
12 revenues less the incremental (out-of-pocket) costs incurred in generating (and/or
13 purchasing) the energy sold off-system.

14 The allocation (credit) of variable costs associated with off-system sales is not
15 really a material issue. The real issue is the allocation of the revenues in excess of the
16 out-of-pocket cost of making off-system sales (off-system sales margin). Mr. Meyer
17 recommends allocating that margin based on sales. Apparently Staff does as well. Since
18 this margin represents a contribution to power supply fixed costs, I recommend allocating
19 off-system sales margin based on the 4CP capacity allocation factor.

¹ Since in this case I recommend allocating fixed power supply costs based on capacity, I will subsequently refer to this as a capacity (4CP) allocation.

1 Q: Staff states at page 187 of its Report that the “costs of making these sales (off-
2 system) are generally variable in nature.” Do you agree with Staff’s assertion that
3 the costs of making these sales are generally variable?

4 A: Yes, I do. However, the fact that the cost of making such off-system sales tends to vary
5 with the level of off-system sales does not mean that off-system sales revenues (much
6 less off-system sales margins) can be considered variable.

7 Staff, Mr. Meyer, and I all seem to agree to allocate variable costs (power supply)
8 in proportion to energy sales. While we may not agree on the level of variable costs
9 associated with off-system sales, the implication of any difference is relatively minor.
10 The costs associated with generating energy sold off-system are included in total variable
11 costs. A proper allocation should result in each jurisdiction receiving a credit for the
12 variable costs allocated to that jurisdiction that are actually used to generate energy not
13 used by that jurisdiction but sold off-system. Staff and Mr. Meyer choose to make this
14 credit by allocating the costs of generating the energy sold off-system based on energy
15 sold in each jurisdiction.

16 I use a more precise method. Before allocating variable costs, I remove the out-
17 of-pocket costs associated with the energy sold off-system from total variable costs. As a
18 result, costs associated with generating energy sold off-system are not included in the
19 variable costs allocated to jurisdictions.

20 The issue is Staff’s and Mr. Meyer’s further recommendation to reduce variable
21 costs allocated to jurisdictions by the margin associated with off-system sales. However,
22 this margin is not related to variable cost. It represents a contribution to fixed costs and
23 should be allocated accordingly.

1 **Q: Have you prepared a schedule that demonstrates this difference?**

2 A: Yes, I have. Schedule LWL2010-13 shows the difference between the energy allocation
3 recommended by Staff and Mr. Meyer, with the allocation of margin that I recommend
4 based on capacity. The amounts I show in Schedule LWL2010-13 are the same that I use
5 in my other schedules. However, I have changed the format to demonstrate the
6 difference between the allocation methods.

7 In Lines 1 through 6 of Schedule LWL2010-13, I show an energy allocation of
8 off-system sales margins as recommended by Staff and Mr. Meyer. This allocation can
9 be shown as a credit to variable power supply costs of total revenues associated with off-
10 system sales. The net variable cost so determined is then allocated based on energy sales.
11 As I show in Line 2, the power supply gross revenue requirement amounts to \$216,327
12 per MW, plus \$12.58 per MWH based on total sales of 22,375,733 MWH. This sales
13 level includes 6,254,865 MWH sold off-system. Reducing total variable cost by total
14 revenues from off-system sales, unit variable cost allocated to jurisdictions amounts to
15 \$4.72 per MWH.

16 In Line 5, I show the allocation of power supply cost to the Missouri jurisdiction
17 by multiplying the unit cost I develop in Line 4 by the units of service associated with
18 service to Missouri jurisdictional customers. Note that the amount I show allocated to the
19 Missouri jurisdiction is identical to the amount I show in Schedule LWL2010-5, Sheet 2
20 of my Direct Testimony.

21 In Lines 7 through 12 of Schedule LWL2010-13, I show my recommended
22 allocation of off-system sales margins. As shown, I reduce total power supply variable
23 cost (\$281,378,082) by the out-of-pocket cost associated with making the off-system

1 sales (\$100,891,638). I reduce fixed power supply costs by the off-system sales margin
2 (\$104,451,915). The net variable cost so determined is then allocated based on energy
3 sales. As I show in Column H, total variable costs amount to \$12.58 per MWH, whereas
4 the cost associated with producing the energy sold off system amounts to \$16.13 per
5 MWH. The net variable cost applicable to native load amounts to \$11.20 per MWH.

6 Multiplying the unit costs that I show in Line 10 by the units of service associated
7 with the Missouri jurisdiction, I find total allocated costs applicable to Missouri of
8 \$446,971,473, which is identical to the amount I show in Schedule LWL2010-7.

9 **Q: Do you have any further observations concerning Schedule LWL2010-13?**

10 **A:** Yes, I do. Staff and Mr. Meyer propose to credit variable costs for costs that are not
11 there. They propose to credit variable cost for the variable costs associated with making
12 off-system sales. Variable costs associated with making off-system sales are indeed
13 included in total variable power supply costs. However, they go one-step further and
14 propose to credit variable costs for the fixed cost contribution of off-system sales. This is
15 a classic mixing of apples and oranges. They would subtract oranges (margin associated
16 with off-system sales) from apples (variable costs associated with service to native load
17 customers).

18 The Staff/Meyer proposal does not lead to a sound conclusion, as demonstrated
19 by the resulting unit variable costs applicable to native load customers. As I show in
20 Column H, Line 4, by reducing variable cost by total off-system sales revenues, the
21 resulting variable cost amounts to \$4.72 per MWH. This amount is only slightly higher
22 than the average fuel cost of generation from the Wolf Creek nuclear unit (\$4.57 per
23 MWH as shown in Schedule LWL2010-2, Sheet 1). They would allocate the benefit of

1 the higher fixed cost generating units (variable cost of \$4.72 per MWH) to the higher
2 load factor jurisdiction while saddling the lower load factor jurisdiction with a
3 disproportionate share of the fixed cost of the generation benefiting the higher load factor
4 jurisdiction.

5
ALLOCATIONS USED BY OTHER MISSOURI UTILITIES

6 **Q: At Page 187 of the Staff Report, Staff states that “traditionally, off-system sales have
7 been allocated using the energy allocation factor since these costs of making these
8 sales are generally variable in nature.” Do you agree?**

9 **A:** Although I don't necessarily agree that off-system sales have traditionally been allocated
10 using an energy allocation factor, I do agree that the costs of making off-system sales
11 tend to vary. Further, and more importantly, the costs of making off-system sales are
12 included in variable power supply costs.

13 **Q: Staff also notes on Page 187 that energy has been used to allocate off-system sales
14 revenues for the Empire District Electric Company and Aquila's MPS electric
15 operations for many rate cases. Is this relevant to KCP&L's situation?**

16 **A:** No. The fact that an energy allocation has been used for Empire and MPS does not mean
17 that it is reasonable for KCP&L. The magnitude of KCP&L's off-system sales far
18 exceeds that of either Empire or MPS. Moreover, the fact that an energy allocation is
19 used in a class cost of service does not mean that it should be used in a jurisdictional
20 allocation.

21 A class cost of service study represents a guide to develop cost-based rates. It
22 represents a split of the total jurisdictional revenue requirement among the customer

1 classes served in that jurisdiction. The implications of the allocation are thus limited to
2 the implications between the various customer classes. If different jurisdictions use
3 different allocation bases in class cost of service studies, the implications are limited to
4 customers within each jurisdiction.

5 By contrast, a jurisdictional allocation represents a determination of the revenue
6 requirement associated with serving each jurisdiction. If different allocation bases are
7 used by various jurisdictions, the company (as is the case with KCP&L) may not be
8 provided a reasonable opportunity to earn the rate of return allowed by the Commission.
9 The implications of different allocation bases in class cost of service do not usually
10 represent a material barrier to the utility earning the rate of return found reasonable. In
11 KCP&L's case, using different allocation bases in the jurisdictional allocation does
12 prevent KCP&L from earning its rate of return.

13 **Q: At Page 15 of his Direct Testimony, Mr. Meyer cites a recent Commission decision**
14 **in AmerenUE's Case No. ER-2010-0036, where the Commission adopted an energy**
15 **based allocation of "off-system sales to customer classes." Do you consider this**
16 **relevant?**

17 **A:** No, I do not. The AmerenUE situation does not appear comparable to KCP&L's in this
18 case. For example:

- 19 1) The finding by the Commission apparently relates to class cost of service,
20 whereas in this case it relates to the jurisdictional allocation.
- 21 2) The finding by the Commission apparently relates to the allocation of off-
22 system sales revenues, not to the allocation of off-system sales margins which is
23 the issue in this case.

1 Further, it appears that the evidence presented in the AmerenUE case was limited to an
2 energy allocation versus a capacity allocation of off-system sales revenues (variable cost
3 plus margin). In the instant case, the evidence I present relates to the allocation of off-
4 system sales margins.
5

IMPLICATIONS ON CLASS COST OF SERVICE

6 **Q: What are the implications of using energy to allocate off-system sales margins on**
7 **class cost of service?**

8 A: Based on the results I show in Schedule LWL2010-13, relative to a capacity allocation
9 (4CP) of off-system sales margins, an energy based allocation will decrease power supply
10 costs allocated to a 70 percent annual load factor class (such as large industrial) by nearly
11 4 percent (0.16 cents per kWh). Conversely, an energy allocation will increase power
12 supply costs applicable to a 30 percent annual load factor class (such as residential) by a
13 little over 6 percent (0.50 cents per kWh). This means, all other factors being equal, that
14 residential customers would have rates 0.50 cents per kWh higher, while industrial
15 customers would get a reduction of 0.16 cents.

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

17 A: Yes, it does.

Kansas City Power Light Company
Unit Power Supply Revenue Requirements
2008 Adjusted

Line No.	Function/Plant	Adjusted Power Supply Revenue Requirement			Units of Service		Unit Power Supply Revenue Requirement	
		Total	Fixed	Variable	Capacity	Energy	Fixed	Variable
		\$	\$	\$	MW	MWH	\$/MW	\$/MWH
1	Energy Allocation of Off-System Sales Margins							
2	Gross Revenue Requirements	1,032,827,902	751,449,820	281,378,082	3,474	22,375,733	216,327	12.58
3	Off-System Sales	205,343,553		205,343,553	-	6,254,865		32.83
4	Net Revenue Requirements	827,484,349	751,449,820	76,034,529	3,474	16,120,868	216,327	4.72
5	Allocation to Missouri Jurisdiction	442,975,739	399,630,926	43,344,812	1,847	9,189,983	216,327	4.72
6	Allocation to Kansas and FERC	384,508,610	351,818,894	32,689,717	1,626	6,930,886	216,327	4.72
7	Capacity Allocation of Off-System Sales Margins							
8	Gross Revenue Requirements	1,032,827,902	751,449,820	281,378,082	3,474	22,375,733	216,327	12.58
9	Off-System Sales	205,343,553	104,451,915	100,891,638	-	6,254,865		16.13
10	Net Revenue Requirements	827,484,349	646,997,905	180,486,444	3,474	16,120,868	186,258	11.20
11	Allocation to Missouri Jurisdiction	446,971,473	344,082,020	102,889,453	1,847	9,189,983	186,258	11.20
12	Allocation to Kansas and FERC	380,512,876	302,915,885	77,596,991	1,626	6,930,886	186,258	11.20
13	Reference							
14	Columns B, C, and D:							
15	Lines 2 through 4 and 8 through 10: Schedule LWL2010-4, Sheet 2							
16	Lines 5 and 11: Column E * G and Column F * H							
17	Lines 6 and 12: Line 4 minus 5 and Line 10 minus 11							
18	Column E: 4CP - Schedule LWL2010-5, Sheet 2							
19	Column F:							
20	Schedule LWL2010-5, Sheet 2, Line 34							
21	Lines 3 and 9: Workpapers							
22	Columns G and H:							
23	Column C / E and Column D / F							
24	Line 5 = Line 4							
25	Line 11 = Line 10							