

**BEFORE THE STATE CORPORATION COMMISSION
OF THE STATE OF KANSAS**

REBUTTAL TESTIMONY OF

CHRIS B. GILES

**ON BEHALF OF
KANSAS CITY POWER & LIGHT COMPANY**

**IN THE MATTER OF THE APPLICATION OF
KANSAS CITY POWER & LIGHT COMPANY
TO MODIFY ITS TARIFFS TO CONTINUE THE
IMPLEMENTATION OF ITS REGULATORY PLAN**

DOCKET NO. 07-KCPE-905-RTS

1 **Q: Are you the same Chris B. Giles who submitted Direct Testimony in this**
2 **proceeding?**

3 **A:** Yes, I am.

4 **Q: What is the purpose of your Rebuttal Testimony?**

5 **A:** The purpose of my testimony is to rebut certain positions taken by Kansas
6 Corporation Commission (“Commission”) Staff and the Citizens’ Utility Ratepayer
7 Board (“CURB”) in their Direct Testimony in this proceeding. Specifically, I address
8 (i) CURB’s proposal to reopen the Regulatory Plan; (ii) contribution in aid of
9 construction (“CIAC”) and its relationship with return on equity (“ROE”);
10 (iii) elements of the energy cost adjustment (“ECA”); (iv) Commission policy
11 regarding customer programs, including demand response and energy efficiency; (v)
12 CURB’s recommended disallowance of Iatan 2 related litigation costs; (vi) Kansas
13 City Power & Light Company’s (“KCPL” or the “Company”) investment in wind

1 generation; (vii) Staff’s recommended treatment of the Wolf Creek Department of
2 Energy Settlement; and (viii) off-system sales (“OSS”) margins.

3 **Q: Please provide background on the critical elements of this rate case.**

4 A: KCPL is engaged in an investment program in excess of \$1 billion over the next five
5 years. This program of work, referred to by KCPL as its comprehensive energy plan,
6 was developed in a collaborative process that culminated in a stipulation and
7 agreement (“Regulatory Plan”) signed by several parties, including the Staff, in
8 Docket No. 04-KCPE-1025-GIE (“1025 Docket”). As described in my Direct
9 Testimony, this current rate case is the second rate case contemplated in the
10 agreement, and was prepared consistent with the 2006 Rate Case Stipulation and
11 Agreement reached in Docket No. 06-KCPE-828-RTS (“2006 Rate Case”), as well as
12 the Stipulation and Agreement in the 1025 Docket.

13 **REGULATORY PLAN**

14 **Q: Has anyone in this current rate case requested the agreement reached in the**
15 **1025 Docket to be reopened?**

16 A: Yes, CURB’s witness Andrea Crane at page 8, numbered paragraph 8 states

17 “The KCC should reopen the Regulatory Plan to reexamine the Company’s
18 generation resource plan in view of new developments, such as the lower-
19 than-projected wind capacity factor, the Company’s recent Settlement
20 Agreement in Missouri with the Sierra Club and other parties, and the
21 Company’s proposed acquisition of Aquila. The KCC should also reexamine
22 its approval of a cash flow mechanism that effectively cedes control over
23 Kansas jurisdictional rates to credit rating agencies.”
24

25 **Q: Do you believe the new developments at KCPL as described by Ms. Crane**
26 **provide any reason to reopen the Regulatory Plan?**

1 A: No, I do not. The developments described by Ms. Crane do not affect the Regulatory
2 Plan, or any provision contained in it, as set forth in the 1025 Docket. The Sierra
3 Club agreement Ms. Crane references has served to facilitate the construction of
4 Iatan 2. KCPL and the Sierra Club have worked together to find common ground that
5 allows the Company to move forward with the construction of Iatan 2 without the
6 distraction and potential risks associated with protracted litigation. Additionally, the
7 Sierra Club agreement covers a time frame beyond that contemplated in the
8 Regulatory Plan. It does not alter the Regulatory Plan, but instead facilitates its
9 implementation. All significant elements of the Sierra Club agreement are contingent
10 on Commission approval. KCPL is currently developing its resource plan applicable
11 to the period beyond 2010, when its current Regulatory Plan expires. A resource plan
12 will be submitted to the Commission for approval at an appropriate time. This
13 resource plan will be a collaborative effort including all stakeholders and will not be
14 completed until late 2008.

15 Ms. Crane also suggests that the acquisition of Aquila by Great Plains Energy
16 Incorporated (“Great Plains Energy”) somehow justifies reopening the Regulatory
17 Plan. It does not. Great Plains Energy’s plan to purchase the Missouri Aquila
18 electric properties in no way changes the need to provide for the future needs of
19 KCPL’s Kansas customers. Aquila and KCPL generation resources will not be
20 jointly dispatched. Joint dispatch and joint planning of generation resources will
21 require approval of this Commission in a future proceeding. The Aquila acquisition
22 has no impact on KCPL’s generation resource planning and will not have an impact

1 until such time as the Commission approves an application by the Company to joint
2 dispatch and plan generation resources.

3 **Q: Did the Commission address CURB's concern regarding CIAC and credit**
4 **ratings in the 1025 Docket?**

5 A: Yes, this issue was raised in that Docket, and addressed by the Commission.

6 **Q: Has anything that you are aware of changed that would give the Commission**
7 **reason to reexamine the findings in that docket?**

8 A: No, there is nothing I am aware of. The Commission must balance the interest of all
9 stakeholders in determining just and reasonable rates. Credit ratings have a
10 significant effect on both the amount of capital available to the utility as well as the
11 cost of that capital. The CIAC mechanism provides a means to maintain KCPL's
12 credit rating at investment grade. Absent CIAC during this period of substantial
13 capital investment, KCPL's credit rating would fall below investment grade and
14 increase its cost of debt, the cost of which would ultimately be borne by KCPL's
15 customers.

16 **CONTRIBUTION IN AID OF CONSTRUCTION**

17 **Q: Although Ms. Crane suggests that the Commission also reexamine its approval**
18 **of a cash flow mechanism, did she consider the use of CIAC in this case?**

19 A: Yes, she did. In the case prepared for CURB, Ms. Crane includes a CIAC in the
20 amount of \$16,436,781.

21 **Q: Was CURB a signatory party to the Stipulation and Agreement reached in**
22 **KCPL's 2006 Rate Case?**

23 A: Yes, CURB was a signatory party in that case.

1 **Q: Did KCPL receive a portion of its rate increase in the 2006 Rate Case in the**
2 **form of a CIAC?**

3 A: Yes, it did. Four million dollars of the awarded rate increase was in the form of
4 CIAC. In the 2006 Rate Case Stipulation and Agreement, this amount was described
5 as a “pre-tax payment on plant on behalf of customers.”

6 **Q: Did Ms. Crane make any recommendations regarding the 50 basis points KCPL**
7 **included in its cost of equity recommendation to address construction risk?**

8 A: Yes, she did. Ms. Crane believes KCPL should not be awarded additional
9 consideration to address construction risk, as she believes the use of the CIAC
10 mechanism mitigates this risk.

11 **Q: Do you agree with Ms. Crane’s assessment?**

12 A: No, I do not. It is important to recognize that the provision of CIAC does not
13 eliminate the requirement for a risk adder for construction as proposed by KCPL
14 witness Dr. Sam Hadaway. Ms. Crane somehow equates investor risk with credit
15 risk. As explained in the Rebuttal Testimony of KCPL witness Michael Cline, CIAC
16 only reduces risk for creditors. It does nothing to reduce the risk faced by equity
17 holders. These are two different risks.

18 **ENERGY COST ADJUSTMENT**

19 **Q: Did KCPL file an ECA in this case?**

20 A: Yes, consistent with the Stipulation and Agreement in the 2006 Rate Case, KCPL
21 filed an ECA.

22 **Q: What process did KCPL use to design the ECA proposed?**

1 A: As discussed in the Direct Testimony of Company witness Tim M. Rush, the
2 Company met several times with the signatory parties of the 2006 Rate Case to
3 discuss the specifics of the ECA mechanism in order to attempt to reach a consensus
4 on the issue. KCPL considered the individual concerns of the parties and attempted
5 to construct an ECA that addresses as many of the issues as possible.

6 **Q: Have any of the parties in this current rate case raised issues with KCPL's**
7 **proposed ECA?**

8 A: Yes, several of the parties have. I would like to address several of the issues raised
9 by CURB witness Andrea Crane, and Staff witnesses Larry Holloway and Dr. John
10 Cita. Company witness Tim M. Rush also discusses the ECA in his Rebuttal
11 Testimony.

12 **Q: What are the issues raised by Ms. Crane?**

13 A: Generally, Ms. Crane opposes any ECA. Ms. Crane states (i) an "ECA results in
14 single-issue ratemaking;" (ii) an "ECA mechanism results in reimbursement
15 ratemaking;" (iii) an "ECA mechanism provides a disincentive to a utility to engage
16 in hedging activities or to adopt good management practices in order to control
17 costs;" (iv) an "ECA mechanism results in rate uncertainty for ratepayers;" (v) "it is
18 very difficult for the KCC Staff and/or CURB to undertake a thorough and
19 comprehensive review of the purchasing decisions made by KCPL as part of each
20 ECA review;" (vi) the "KCC has not examined the impact of the ECA on the
21 Company's overall return requirements;" and (vii) an "ECA puts the KCC in the
22 position of approving rate increases without any idea of the potential magnitude of
23 those increases."

1 **Q: Do you agree with any of the issues raised by CURB?**

2 A: Yes, I agree that an ECA is single-issue ratemaking and that it results in
3 reimbursement ratemaking. In fact, an ECA is designed to do both of those things.
4 The purpose of an ECA is to flow through dollar for dollar the cost of fuel to
5 customers outside the context of a general rate proceeding. In doing this, the
6 customer pays their true cost, and the Company is reimbursed its true expenses.

7 **Q: Is an ECA a new concept for Kansas electric consumers?**

8 A: No, the use of an ECA is not a new concept. According to CURB's web-site,
9 Midwest Energy, Westar, and Empire all have ECAs. In addition, KCPL had an ECA
10 in Kansas during the 1970s.

11 **Q: Do you believe an ECA provides a disincentive to hedge fuel costs or adopt good
12 management practices in order to control costs?**

13 A: No, I do not. The ECA provides neither a disincentive nor an incentive to engage in
14 these activities. As originally proposed by KCPL, the ECA allowed recovery of
15 hedging costs. Under the originally proposed ECA, KCPL's fuel procurement
16 processes and results are subject to an annual review. Presuming the Commission
17 and CURB believe hedging and cost control is appropriate, KCPL has every incentive
18 to hedge its fuel prices and use good management practices to control costs.
19 Company witness Wm. Ed Blunk further discusses KCPL's hedging in his Rebuttal
20 Testimony, and responds to Dr. Cita's hedging-related Direct Testimony.

21 **Q: Does an ECA result in rate uncertainty for ratepayers?**

22 A: Yes, to some extent it does. Ratepayers will pay a different amount monthly
23 dependent on changes in the various components of the ECA.

1 **Q: Does the ECA proposed by KCPL address this idea of volatility for ratepayers?**

2 A: Yes, it does. In meeting with the signatory parties to KCPL's 2006 Rate Case
3 settlement, regarding the design of the ECA, it was apparent one of the concerns was
4 the volatility imposed on customers by an ECA. This led KCPL to propose that the
5 monthly ECA be based on forecasted fuel costs and OSS a year in advance. OSS
6 margins are a credit to the cost of fuels, and reduce the cost to customers. In using
7 this year-ahead-look, customers could estimate what their costs would be looking
8 forward. The ECA proposed by the Company allows for changes to these monthly
9 values should it become apparent the forecasted values have not tracked closely to
10 actuals and/or the forecast for the remainder of the ECA year has changed such that
11 year-end projected ECA revenues as compared to year-end projected costs less off-
12 system sales margins are expected to be significantly different.

13 **Q: Is there anything else in the ECA proposed by KCPL that addresses volatility?**

14 A: Yes, KCPL proposes to spread its forecast of OSS margins evenly on a per kWh basis
15 back to customers rather than applying the monthly forecast of OSS margins to the
16 ECA.

17 **Q: How does this address volatility?**

18 A: The ECA would vary substantially month-to-month due to the volatility of OSS
19 margins because KCPL's OSS margins vary considerably from month to month.
20 Should the Company include its estimate of margins as they are expected to occur
21 monthly, the ECA would vary to reflect the volatility of those sales. KCPL's
22 proposal smoothes this effect.

23 **Q: Was price volatility viewed as a negative by all the signatory parties?**

1 A: No, it was not. Price volatility can be synonymous with price signal. While it was
2 not the desire of any party to subject customers to substantial swings in pricing, there
3 was some concern that customers should be made aware of the actual prices of fuel,
4 and the periods of higher fuel prices. Generally, the Company experiences higher
5 fuel prices during periods of higher demand. There was some desire to construct an
6 ECA that made this apparent to customers.

7 **Q: What is your response to the fifth, sixth, and seventh issues raised by Ms.
8 Crane?**

9 A: These issues raised by Ms. Crane relate to (i) the difficulty the Commission and
10 CURB will face in reviewing KCPL's purchasing decisions; (ii) impact of the ECA
11 on the Company's return; and (iii) the approval of rate increases in light of an ECA.

12 **Q: Are these issues described by Ms. Crane of concern if KCPL has an ECA?**

13 A: No, the Commission and CURB are faced with reviewing the prudence of KCPL's
14 purchasing decisions, the impact of fuel costs and OSS on the Company's return, and
15 the rate increases awarded in light of fuel costs and OSS whenever KCPL has made a
16 rate increase request.

17 **Q: On pages 77 and 78 of Ms. Crane's testimony, Ms. Crane states, "If, however,
18 the KCC adopts the ECA mechanism, then 100% of the off-system sales should
19 be flowed through that mechanism in order to provide ratepayers, who are
20 paying 100% of the fuel and purchased power costs, with 100% of the benefit
21 from such sales." Do you agree with Ms. Crane's position?**

22 A: Yes, KCPL's proposal flows back to Kansas customers 100% of the Kansas portion
23 of OSS margins. The monthly projected ECA is trued up at the end of the year to

1 reflect actual fuel costs and actual OSS margins. Flowing back 100% of Kansas OSS
2 margins on a monthly basis would require monthly estimates of OSS margins and
3 increase the volatility of the ECA factor.

4 **Q: You mentioned earlier that there were ECA issues raised by Staff witnesses**
5 **Larry Holloway and Dr. John Cita. What are the issues you would like to**
6 **address?**

7 A: Mr. Holloway raises two issues concerning the ECA proposed by KCPL. The first
8 issue I would like to address is Mr. Holloway's recommended adjustment for coal
9 inventory.

10 **Q: What is Mr. Holloway's recommendation?**

11 A: While Mr. Holloway supports KCPL's approach to determining target fuel
12 inventories, he believes the ECA true-up should be used to make adjustments related
13 to higher fuel costs as a result of KCPL carrying coal inventory levels lower than
14 target.

15 **Q: Do you agree with Mr. Holloway's position?**

16 A: No, I do not. Like many issues considered in a rate case, the fuel inventory is
17 "normalized" for rate making purposes. Mr. Holloway supports KCPL's
18 normalization based on target inventories, so the level of the normalized fuel
19 inventory is not at issue. The reason for normalization is to obtain representative
20 amounts for setting rates. Fuel inventory is a rate base item. Attempting to do some
21 sort of true-up through the ECA, which has no bearing on rate base, would at best be
22 difficult. Too many factors that are often beyond the Company's control affect fuel
23 inventories. The ECA review is intended to examine the prudence of KCPL's fuel

1 procurement practices. As long as there is no finding by the Commission of
2 imprudent procurement practices, it would be inappropriate to attempt to quantify and
3 then adjust the ECA based on fuel inventories. This issue is more fully discussed in
4 the Rebuttal Testimony of Company witnesses Tim M. Rush.

5 **Q: What is the second issue Mr. Holloway raises that you would like to address.**

6 A: Mr. Holloway, as well as Staff witness Justin Grady, advocates the use of an Unused
7 Energy allocator (“UE1”) to allocate OSS margins to KCPL’s Kansas customers.

8 **Q: Why do you take issue with this recommendation? Didn’t KCPL advocate the**
9 **use of this allocator in its last case?**

10 A: Yes, the Company did. However, KCPL’s proposal was unique and to my
11 knowledge, not utilized anywhere else in the country. It was not KCPL’s intent to
12 create yet another allocation issue between the states of Missouri and Kansas.
13 Obviously, changing allocation methods results in more or less benefit or cost
14 allocated to one state or the other. This could result in unrecovered costs or benefits
15 greater than actual. Because this approach has never been utilized by Missouri or
16 Kansas, KCPL believes it is appropriate to continue the same allocation as has been
17 used by both states for at least the past 40 years. Company witness Tim M. Rush
18 discusses the details of this issue in his Rebuttal Testimony.

19 **Q: You said you intended to address an issue raised by Dr. Cita. Can you describe**
20 **the issue?**

21 A: Generally, Dr. Cita recommends reporting that is inconsistent with the ECA tariff
22 proposed by the Company, and supported by Commission witness Larry Holloway.

1 Company witness Tim M. Rush addresses the details of the inconsistency in his
2 Rebuttal Testimony.

3 **Q: Are you opposed to periodic reporting to the Commission in conjunction with**
4 **the ECA?**

5 A: No, not at all. The Company understands the need to submit reports to the
6 Commission regarding the ECA, and the true-up associated with the ECA. The
7 problem is the reporting described by Dr. Cita is contradictory to the tariff, in that it
8 would replace KCPL’s proposed quarterly reporting and correction methodology with
9 a monthly calculation of the ECA factor. The proposed tariff allows for monthly
10 ECA factors that are prepared once a year, and only updated if necessary throughout
11 the year. KCPL believes the reporting should support and follow the intent of the
12 tariff.

13 **CUSTOMER PROGRAMS**

14 **Q: There was a large focus on Energy Efficiency/Demand Response (“EE/DR”)**
15 **measures in developing the Regulatory Plan. Are there any issues in this case**
16 **related to EE/DR?**

17 A: Yes, both Staff and CURB have recommendations regarding the cost of these
18 initiatives. Staff witness Justin Grady eliminates the EE/DR-related operating
19 expenses and rate base additions proposed by KCPL, and suggests these costs be
20 recovered through an Energy Efficiency Rider (“EER”) instead, as recommended by
21 Staff in Docket No. 07-GIMX-247-GIV. Ms. Crane, CURB’s witness, makes similar
22 adjustments.

23 **Q: Why does this concern you?**

1 A: My primary concern is the message this recommendation sends to utilities. EE/DR is
2 a cornerstone of KCPL's Regulatory Plan developed with the input of many parties.
3 Fundamentally, unless EE/DR investments receive regulatory treatment on the same
4 or similar basis as generation investment, utilities may have less incentive to make
5 EE/DR investments.

6 Additionally, Mr. Grady suggests KCPL recover these cost through an EER as
7 suggested by Staff in Docket No. 07-GIMX-247-GIV. This docket is still open. The
8 Commission has not ruled, and has not accepted Staff's recommendation. Even if
9 this were an acceptable alternative for KCPL, it is premature to mandate it at this
10 time.

11 **LITIGATION DISALLOWANCE**

12 **Q: Are there any other disallowance recommendations made you would like to**
13 **address?**

14 A: Yes, CURB witness Ms. Crane recommends the disallowance of costs related to what
15 she characterizes as "Missouri" litigation. Her issue is the Company's allocation to
16 Kansas of a share of the costs associated with litigation in Missouri in defense of
17 legal appeals filed by the Sierra Club and others. She does not believe this is a cost
18 that should be borne by Kansas ratepayers.

19 **Q: What did the appeals pertain to?**

20 A: The appeals were filed by the Sierra Club and others, and involved an appeal of the
21 decision by the Missouri Department of Natural Resources, which issued a permit to
22 KCPL related to Iatan 2, and the Missouri Public Service Commission's order

1 approving KCPL's Regulatory Plan. The resolution of both of these appeals was
2 critical to KCPL's construction of Iatan 2.

3 **Q: Will Iatan 2 serve Kansas customers?**

4 A: Yes, it will, and the costs associated with the appeals are directly related to the
5 construction of Iatan 2. Iatan 2 will serve Kansas customers as well as Missouri
6 customers. There is no reason to exclude these costs from Kansas rates, just because
7 the appeals were filed in Missouri.

8 **Q: Has KCPL sought to recover costs associated with the settlement agreement in
9 this case?**

10 A: No, it has not. The agreement covers a period beyond that contemplated in the
11 current Regulatory Plan. The Company is not seeking any recovery related to the
12 agreement.

13 **WIND INVESTMENT**

14 **Q: Has CURB recommended any other disallowances in this case?**

15 A: Yes, Ms. Crane recommends that the Commission limit recovery of the capital costs
16 associated with wind generation to the amount contained in the Regulatory Plan. This
17 amount according to Ms. Crane is \$130.8 million (excluding AFUDC) vs. \$166
18 million (excluding AFUDC) in the Company's 2006 Rate Case. Company witness
19 John P. Weisensee also addresses the dollar values associated with this proposed
20 disallowance in his Rebuttal Testimony.

21 **Q: Was the wind generation in service and included in the 2006 Rate Case?**

22 A: Yes, it was.

1 **Q: Was the rate base value of the wind generation determined in the 2006 Rate**
2 **Case?**

3 A: Yes, it was.

4 **Q: What was the resolution of the 2006 Rate Case?**

5 A: The parties reached a non-unanimous settlement agreement, and the Commission
6 approved it.

7 **Q: Is it your belief the rates established in the 2006 Rate Case included the full rate**
8 **base value of the wind project?**

9 A: Yes, it is.

10 **Q: Was CURB a signatory party to the agreement?**

11 A: Yes, it was. In my opinion, this issue was covered in the 2006 Rate Case. The
12 Spearville wind generation facility is currently reflected in rate base at the full value,
13 and any adjustment at this point in time is inappropriate.

14 **Q: As the Company received bids for its wind generation project, did the Company**
15 **keep the parties informed as to the costs reflected in the bids?**

16 A: Yes, it did. The Company met with the parties and provided new estimates and
17 updated analysis that showed the wind investment to be economical even with the
18 higher costs reflected in the bids. The original estimate reflected in the Regulatory
19 Plan was based on surveys of potential developers prior to solicitation of bids. Ms.
20 Crane provides no evidence of cost overruns or imprudence. In fact, the project came
21 in on budget and on time, once the bid was accepted. If utilities are held to such
22 preliminary estimates, prior to solicitation of bids, nothing may be built.

23 **Q: Why did the cost increase from the original estimate?**

1 A: The Federal government extended the Production Tax Credit ("PTC"). As a result,
2 wind turbine suppliers and wind project developers increased their prices due to the
3 greater demand for wind turbines caused by the PTC.

4 **Q: Ms. Crane voices concern with the performance of the Spearville wind facility in**
5 **relation to the Company's estimate of the capacity factor. Has the Spearville**
6 **facility been in operation long enough to determine the capacity factor for the**
7 **site?**

8 No, it has not. Ms. Crane suggests that the brief operations history of KCPL's
9 Spearville wind generation facility somehow justifies reopening the Regulatory Plan.
10 It does not. As Staff witness Mr. Glass testifies, the capacity factor of the Spearville
11 wind generation facility has been impacted by an ice storm transmission constraints,
12 which have since been remedied, and normal start-up limitations. In addition, wind
13 measurement must be accumulated over many, or at least several years, prior to
14 determination of capacity factor.

15 **WOLF CREEK-DEPARTMENT OF ENERGY SETTLEMENT**

16 **Q: Staff's witness Laura Bowman has proposed a three-year amortization for the**
17 **Wolf Creek Department of Energy Settlement. Do you believe this is**
18 **appropriate?**

19 A: No, I do not. Ms. Bowman points out that the refund KCPL received is an unusual
20 event that was recorded in the test years, but related to services purchased during
21 prior years. This in and of itself supports KCPL's position that this refund is not a
22 normal occurrence, and should not be reflected in the current case. Ms. Bowman
23 further states "KCPL customers already paid for the uranium enrichment services

1 through fuel expenses during fiscal years 1986-1993. Ratepayers are entitled to any
2 refunds related to these services.” KCPL did not have an ECA in place during 2006.
3 There is no ECA mechanism to flow this refund through. Furthermore, reaching back
4 to prior years outside the test period, in order to apply a “refund” going forward
5 constitutes retroactive ratemaking, and is not appropriate. The Commission is setting
6 rates for future years. It is no more appropriate to reach back beyond the test year as
7 Ms. Bowman proposes, than it is for the Company to reach back for rate increases
8 foregone during this period. KCPL did not have a change in rates during this entire
9 period.

10 **OFF-SYSTEM SALES MARGIN**

11 **Q: Are there any other issues you would like to address?**

12 A: Yes, there is one final issue raised by Ms. Crane. Ms. Crane generally opposes any
13 ECA. It is Ms. Crane’s position that absent an ECA, KCPL’s revenue requirement
14 should be set using OSS margins at the 50th percentile rather than the 25th percentile.
15 As in the 2006 Rate Case, it is the Company’s position that inclusion of OSS margins
16 at the 25th percentile is appropriate due to the inherent risk associated with those
17 margins. Should the Commission adopt an ECA mechanism for KCPL, this issue is
18 moot. KCPL’s proposed ECA flows back 100% of the Kansas portion of OSS
19 margins to Kansas customers.

20 **Q: What level of OSS margins is included in the Company’s traditional revenue**
21 **requirement in this case?**

22 A: KCPL included in the revenue requirement in this case and used as the OSS margin
23 projection for the ECA mechanism, the projections of Company witness Michael

1 Schnitzer at the 25th percentile, as described in my Direct Testimony and the Direct
2 Testimony of Mr. Schnitzer.

3 **Q: Why is KCPL proposing to use the 25th percentile for off-system sales margins**
4 **rather than the 50th percentile?**

5 A: As KCPL witness Michael Schnitzer described in his Direct Testimony, there is
6 significant risk associated with margins in the OSS market. The risk of the OSS
7 market consists of several components, including market price, volumetric risk
8 associated with generation variable cost, generation unit outages, coal supply
9 availability, weather, and uncertainty of retail sales growth. A detailed risk analysis
10 of the OSS market has been prepared by Mr. Schnitzer and is included in his Direct
11 Testimony.

12 As discussed in the 2006 Rate Case, the significant construction program,
13 which KCPL is currently implementing in compliance with the Regulatory Plan,
14 requires that KCPL maintain sufficient cash flow to maintain its credit ratings. If,
15 because of a change in the OSS market, KCPL's actual OSS margins for 2007 were
16 less than what is built into the revenue requirement, then the Company's cash flow
17 and credit metrics would be negatively affected resulting in higher costs for the
18 construction program and ultimately for customers. Significant changes have
19 occurred in the OSS market since the Company filed the 2006 Rate Case. These
20 changes in the market confirm that the Company's cash flow requirements in 2007
21 are at risk, and highlight the risk of including the 50th percentile of projected OSS
22 margins in the revenue requirement determination.

23 **Q: Please describe the changes in the market since the 2006 Rate Case process?**

1 A: When KCPL filed its original 2006 application, natural gas prices and the wholesale
2 energy market were at a relatively high level. Natural gas prices were around \$10 per
3 mcf, considerably higher than the \$2-\$5 range during years prior to that case. In the
4 2006 Rate Case, I testified that the Commission should look forward and take into
5 account the risk of the OSS market in determining the amount of OSS margin to
6 include in KCPL's revenue requirement. I noted that historical data should not be
7 used as indicative of potential future margins in this volatile market. By September
8 2006, natural gas prices had sharply declined. This resulted in a much lower
9 expectation of OSS margins for 2007. In fact, prices declined to the extent that the
10 expected 50th percentile point on the curve was approximately \$11 million lower than
11 originally filed in the case. The 25th percentile was approximately \$7 million lower
12 than originally included in the 2006 Rate Case.

13 **Q: What level of OSS margins did the Commission determine appropriate to**
14 **include in revenue requirement in the 2006 Rate Case?**

15 A: The 2006 Rate Case Stipulation and Agreement contained a "black box" settlement so
16 the level of OSS margin was not litigated and it was not specifically defined within
17 the Stipulation and Agreement.

18 **Q: What is the current expectation for off-system sales margins for 2007?**

19 A: Prices in the market have continued to decline. The Company's current 50th
20 percentile projection for 2007 is roughly equal to the 25th percentile of one year ago.

21 **Q: By setting the projected OSS margin at the 25th percentile, do Kansas customers**
22 **still receive the benefit of all (100%) of the Kansas OSS?**

1 A: Yes, even without an ECA, all Kansas OSS margins (100%) realized by the Company
2 will be credited back to Kansas customers in a future rate case, or refunded once the
3 actual results are known.

4 **Q: Why is it so important to set OSS margins at the 25th percentile?**

5 A: CIAC is impacted as well as cash flow. Setting margins at the 50th percentile
6 provides the Company only a 50/50 chance it will remain investment grade. This is
7 too risky. As last year has proven, had the OSS been set at the 50th percentile, KCPL
8 would be below investment grade today.

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

10 A: Yes, it does.

