

**Exhibit No.:**

**Issue(s):**

Regulatory Plan Amortization

**Witness/Type of Exhibit:**

Trippensee

Surrebuttal

**Sponsoring Party:**

Public Counsel

**Case No.:**

ER-2006-0314

**SURREBUTTAL TESTIMONY**

**OF**

**RUSSELL W. TRIPPENSEE**

Submitted on Behalf of the Office of the Public Counsel

**KANSAS CITY POWER & LIGHT COMPANY**

CASE NO. ER-2006-0314

October 6, 2006

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

In the Matter of the Application of Kansas )  
City Power & Light Company for )  
Approval to Make Certain Changes in its ) **ER-2006-0314**  
Charges for Electric Service to Begin the )  
Implementation of Its Regulatory Plan )

**AFFIDAVIT OF RUSSELL W. TRIPPENSEE**

**STATE OF MISSOURI** )  
 ) ss  
**COUNTY OF COLE** )

Russell W. Trippensee, of lawful age and being first duly sworn, deposes and states:


1. My name is Russell Trippensee. I am Chief Public Utility Accountant for the Office of the Public Counsel.
2. Attached hereto and made a part hereof for all purposes is my surrebuttal testimony consisting of 14 pages.
3. I hereby swear and affirm that my statements contained in the attached testimony are true and correct to the best of my knowledge and belief.

  
Russell W. Trippensee

Subscribed and sworn to me this 6<sup>th</sup> day of October 2006.



JERENE A. BUCKMAN  
My Commission Expires  
August 10, 2009  
Cole County  
Commission #05754036

  
Jerene A. Buckman  
Notary Public

My Commission expires August 10, 2009.

**SUREEBUTTAL TESTIMONY**

**OF**

**RUSSELL W. TRIPPENSEE**

**KANSAS CITY POWER & LIGHT COMPANY  
CASE NO. ER-2006-0314**

**Q. PLEASE STATE YOUR NAME AND ADDRESS.**

A. Russell W. Trippensee. I reside at 1020 Satinwood Court, Jefferson City, Missouri 65109, and my business address is P.O. Box 2230, Jefferson City, Missouri 65102.

**Q. BY WHOM ARE YOU EMPLOYED AND IN WHAT CAPACITY?**

A. I am the Chief Utility Accountant for the Missouri Office of the Public Counsel (OPC or Public Counsel).

**Q. ARE YOU THE SAME RUSSELL W. TRIPPENSEE WHO HAS FILED REBUTTAL TESTIMONY IN THIS CASE?**

A. Yes.

**Q. WHAT IS THE PURPOSE OF YOUR SURREBUTTAL TESTIMONY?**

A. To address the Additional Amortization (RPAA) calculation that was provided for in the Stipulation and Agreement (Regulatory Plan) that was approved by the Missouri Public Service Commission (MPSC or Commission) in Case No. EO-2005-0329 involving Kansas City Power & Light Company (KCPL or Company). I will clarify Public Counsel's position on how the calculation of the RPAA should be performed after the Commission determines the revenue requirement using traditional regulatory procedures. The revenue requirement should be determined prior to consideration of the financial metrics set out in the Regulatory Plan.

I will address the rebuttal testimony of Company witnesses Chris Giles and Michael Cline. Mr. Giles discusses the purpose of the Regulatory Plan and the RPAA. Mr. Giles along with Mr. Cline also

1 state that the RPAA creates increased costs to the customer as compared to the MPSC authorizing  
2 increased earnings to provide additional cash flow necessary. While neither of these witnesses  
3 specifically requests a higher return to meet the financial metrics, the clear inference is that if the  
4 financial metrics set out in the Regulatory Plan are not met, a higher rate of return on equity (i.e.  
5 increased earnings) should be granted in lieu of all or at least a portion of the RPAA.

6 **REGULATORY PLAN ADDITIONAL AMORTIZATION CALCULATION**

7 **Q. DOES PUBLIC COUNSEL BELIEVE THAT CERTAIN CHANGES TO THE**  
8 **CALCULATION OF THE ADDITIONAL AMORTIZATION HAVE BEEN AGREED**  
9 **TO BY THE STAFF, THE COMPANY, AND PUBLIC COUNSEL?**

10 A. Yes. In order to make the calculation consistent with the stipulation and agreement, certain changes  
11 to the calculation as contained in Staff's direct testimony were determined to be necessary. It should  
12 be noted that Staff's initial calculation was consistent with Appendix D to the Regulatory Plan.  
13 However, I believe the Company and Staff will acknowledge that Appendix D was illustrative in  
14 nature and was not completely consistent with the language of the Regulatory Plan.

15 It is OPC's understanding that these changes will be reflected in the additional amortization  
16 calculation that Staff files as part of its surrebuttal testimony. OPC has not had an opportunity to  
17 review that testimony as all parties' testimony is to be concurrently filed.

18 **Q. PLEASE EXPLAIN THE CHANGES THAT OPC ANTICIPATES WILL BE PART**  
19 **OF THE ADDITIONAL AMORTIZATION CALCULATION.**

20 A. OPC expects the calculation to reflect an increase in the amount of the RPAA resulting from a change  
21 to the calculation to recognize the decreased cash flow available due to reduction of deferred income  
22 tax expense resulting from the treatment of the RPAA as additional book depreciation expense. This

1 reduction in cash flow creates a need for an increase in the RPAA (to be treated as additional book  
2 depreciation expense) in order to provide sufficient cash flow to meet the financial metrics set out in  
3 the Regulatory Plan. Public Counsel agrees with this change.

4 OPC also expects the calculation to reflect a revision to the format of the calculation to set out the  
5 capital structure percentages so that the investment in Missouri jurisdictional retail electric operations  
6 is properly synchronized with the capital structure. This synchronization is required so that the  
7 RPAA does not provide cash flow to support debt costs that are used to support company operations  
8 other than Missouri retail electric operations as determined by this Commission. Public Counsel  
9 agrees with this change.

10 **Q. DOES PUBLIC COUNSEL ANTICIPATE A CHANGE WILL BE MADE TO**  
11 **STAFF'S INITIAL CALCULATION TO REFLECT ADDITIONAL INVESTMENT**  
12 **IN EXCESS OF RATE BASE?**

13 A. Yes. The illustrative calculation of the additional amortization found in Appendix D to the  
14 Regulatory Plan included Rate Base but did not include other investments related to Missouri electric  
15 operations, specifically construction work in progress (CWIP). The Regulatory Plan specifically  
16 states:

17 The Signatory Parties agree to support an additional amortization amount added to  
18 KCPL's electric cost of service in a rate case when the projected cash flows resulting  
19 from KCPL's Missouri jurisdictional electric operations, as determined by the  
20 Commission, fail to meet or exceed the Missouri electric portion of the lower end of  
21 the top third of the BBB range shown in Appendix E, for the Funds from Operations  
22 Interest Coverage ratio and the Funds from Operations as Percentage of Average  
23 Total Debt ratio.

24 (emphasis added)

25 (Case No. ER-2005-0329, Stipulation & Agreement, page 20)

1 The primary investment related to Missouri electric operations that is not contained in rate base is  
2 CWIP. Therefore OPC believes that it is appropriate to add CWIP to the Commission determined  
3 rate base prior to synchronizing the Missouri electric operations investment with the capital structure  
4 as was previously discussed. It is critical to point out that the CWIP balance to be added to rate base  
5 for the purposes of calculating the additional amortization should be reduced by the amount of short  
6 term debt used in the additional amortization calculation in the section labeled Additional Financial  
7 Information Needed for the Calculation of Ratios. Based on information provided to OPC by the  
8 Staff, the net amount of investment to be added to rate base would be \$219,619,000 of CWIP less the  
9 amount of short term debt used in the RPAA calculation in the section Additional Financial  
10 Information needed for the Calculation of Ratios. The CWIP amount is a total company amount and  
11 will have to be allocated to Missouri jurisdictional electric operations prior to inclusion in the RPAA  
12 calculation.

13 Public Counsel is not aware of any other item recorded on the Company's financial records that is not  
14 considered in the Commission's determination of rate base. If a prudent investment is recorded on  
15 the Company's records in the future that relates to Missouri electric operations but is not included in  
16 the Commission's determination of rate base, that item should be examined and a determination made  
17 as to the appropriateness of including it in the additional amortization calculation.

18 **Q. DOES PUBLIC COUNSEL EXPECT STAFF TO MAKE AN ADJUSTMENT TO**  
19 **RECOGNIZE ADDITIONAL INVESTMENT RELATED TO MISSOURI ELECTRIC**  
20 **OPERATIONS THAT ARE NOT INCLUDED IN RATE BASE?**

21 **A.** Yes. It is Public Counsel's understanding that Staff has performed a calculation that uses the  
22 Company's balance sheet and eliminates items that Staff believes are already specifically identified as

1 a component of rate base. The remaining balance sheet assets are reduced by the remaining liabilities  
2 and the net amount is then added to the rate base prior to the synchronization of the capital structure.

3 **Q. PLEASE EXPLAIN WHY OPC BELIEVES STAFF'S ADDITIONAL AMOUNT IS**  
4 **INAPPROPRIATELY CALCULATED.**

5 A. The Regulatory Plan clearly sets out that the additional amortization is to provide the necessary cash  
6 flows based on Missouri jurisdictional electric operations as determined by this Commission. Rate  
7 Base as determined by this Commission is the net investment used to provide electric jurisdictional  
8 service. Similarly, a balance sheet represents the net investment of a company but is in fact the  
9 accumulation of all assets and liabilities of the Company, both jurisdictional and non-jurisdictional,  
10 and thus the resulting net investment does not represent Missouri jurisdictional electric operations.  
11 The balance sheet also reflects the assets and liabilities at a point in time whereas rate base often  
12 includes investments that reflect averages over a period. Material and supplies along with fuel  
13 inventories would be illustrative of these types of investments that are measured differently for rate  
14 base versus a balance sheet that is prepared for financial reporting purposes. Rate base includes  
15 certain measurements of assets and liabilities in a manner distinctly different from the balance sheet.  
16 As example, accounts payable and accounts receivable are shown on the balance sheet as a number at  
17 a specific point in time whereas a lead lag study is used to measure payment of monies and receipt of  
18 monies on an annual basis and the result is reflected in cash working capital component of rate base.  
19 To the extent that Staff's analysis will not eliminate or identify these concerns, OPC believes the  
20 result should not be added to rate base to determine the net investment applicable to Missouri electric  
21 retail operations that ratepayers should provide monies via an additional amortization.

22 **REGULATORY PLAN ADDITIONAL AMORTIZATION POLICY**

1 **Q. WHAT CONCERNS DOES PUBLIC COUNSEL HAVE WITH THE REBUTTAL**  
2 **TESTIMONY OF THE COMPANY REGARDING THE RPAA?**

3 A. The rebuttal testimony of Mr. Giles and Mr. Cline contain several inaccurate statements regarding the  
4 RPAA development and calculation. In addition, the testimony appears to imply that providing  
5 additional earnings through the traditional regulatory process in order to meet the financial metrics  
6 required under the Regulatory Plans is appropriate and also less costly to the ratepayers. My  
7 surrebuttal testimony will address these statements and provide the MPSC with the accurate  
8 information.

9 **Q. MR. GILES AND MR. CLINE BOTH ASSERT THAT RPAA "IS NOT LESS**  
10 **COSTLY TO CUSTOMERS" AND IN FACT MR. CLINE PRESENTS AN**  
11 **ANALYSIS THAT PURPORTS TO SHOW THAT THE RPAA IS IN FACT MORE**  
12 **EXPENSIVE TO RATEPAYERS IN THE SHORT-RUN. PLEASE COMMENT ON**  
13 **MR. CLINE'S ASSERTION.**

14 A. At best, Mr. Cline's testimony (Cline Rebuttal, page 4, line 23 – page 5, line 12) asserting that the  
15 RPAA is more costly to ratepayers in the short-run reveals a fundamental lack of understanding of the  
16 regulatory process.

17 There are only two sources of funds available through traditional regulation that will provide  
18 additional Funds from Operations (FFO). Those two sources are additional return on equity  
19 (earnings) or non-cash expenses such as depreciation or amortizations.

20 The inclusion of an additional dollar of earnings in the revenue requirement will result in an  
21 additional dollar of FFO if and only if revenues are increased to reflect the resulting additional  
22 income taxes. Based on the Staff's direct testimony, the additional dollar of earnings must be



1 multiplied by 1.633 in order to provide sufficient income taxes so that the Company would retain a  
2 dollar of earnings to provide for cash flow. If the RPAA is calculated in a manner consistent with that  
3 discussed earlier in this testimony, the result will be that, in order for the RPAA to provide an  
4 additional dollar of net cash flow, the RPAA will have to be set at a level that mathematically  
5 calculated as \$1.633. Therefore in the short-run, the effect increasing earnings or implementing an  
6 RPAA is exactly equal.

7 **Q. DOES NOT MR. CLINE ATTACH TO HIS REBUTTAL TESTIMONY SCHEDULE**  
8 **MWC-3 THAT PURPORTS TO SHOW THAT FOR THE PURPOSES OF**  
9 **PROVIDING ADDITIONAL CASH FLOW THE RPAA WOULD BE MORE COSTLY**  
10 **THAN EARNINGS?**

11 A. Yes such a schedule does purport to make that representation. Unfortunately Schedule MWC-3 is not  
12 representative of the regulatory process used to set rates. It must also be pointed out that the starting  
13 points used in the respective examples are not consistent thus could best be characterized as a  
14 comparison of apples and beef. Finally the financing examples used in the comparison are not even  
15 representative of the capital structure of KCPL.

16 **Q. PLEASE EXPLAIN WHY SCHEUDULE MWC-3 IS NOT REPRESENTATIVE OF**  
17 **THE REGULATORY PROCESS USED TO SET RATES UNDER THE REGULATORY**  
18 **PLAN OR TRADITIONAL RATE OF RETURN REGULATION FOR THAT**  
19 **MATTER.**

20 A. This schedule addresses "financing for a \$1 million dollar capital expenditure". Simply put, rates are  
21 set in Missouri to provide the level of revenues equal to the cost of service. The following formula  
22 highlights this.

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1 column labeled Debt Financing using a completely different capital structure. Thus any resulting  
2 difference in the cost of his two methods is meaningless.

3 I would also point out that a utility investment financed entirely by debt as Mr. Cline proposes in his  
4 cost comparison would not a prudent course of action by utility management. A completely  
5 leveraged utility would not be investment grade.

6 **Q. YOU INDICATED THE EXAMPLES ARE NOT EVEN REPRESENTATIVE OF THE**  
7 **CAPITAL STRUCTURE OF KCPL. PLEASE EXPLAIN.**

8 A. KCPL has a capital structure that consists of approximately 45% debt and 55% equity according to  
9 the Company witness, Samuel Hadaway (direct testimony, page 7, lines 7 -11). Mr. Cline's example  
10 uses a capital structure of 31.5% debt and 68.5% equity for determining the cost of his "earnings"  
11 method and a capital structure of 100% debt and 0.0% equity for determining the cost of his  
12 "amortization" method. These divergent capital structures highlight the inconsistencies in his analysis  
13 in addition to the lack of relevance to KCPL's actual situation.

14 **Q. DOES THE RPAA RESULT IN SAVINGS TO THE RATEPAYER OVER A**  
15 **LONGER PERIOD OF TIME AS COMPARED TO SIMPLY INCREASING**  
16 **EARNINGS ABOVE A JUST AND REASONABLE LEVEL AS KCPL PROPOSES**  
17 **SHOULD BE DONE?**

18 A. Yes.

19 **Q. PLEASE EXPLAIN?**

20 A. As previously discussed the initial cost to the ratepayers will be equal under either an RPAA method  
21 or an "increased earnings" method. However, the RPAA will be recorded on the financial records as  
22 an amortization expense (debit) and accumulated reserve account (credit) in a manner consistent with

1 the procedures used to record normal depreciation expense. That is because like depreciation  
2 expense, the RPAA is the "return of" the capital investment of the Company included in rate base.  
3 Therefore, upon the "return of" the capital investment to the Company the ratepayer will no long be  
4 required to pay a "return on" that investment to the Company. This will have the effect of reducing  
5 future revenue requirements related to those capital investments, all things else being equal.

6 In contrast, the "increased earnings" method will result only in an increase in the bottom line of the  
7 Company providing additional funds to either distribute to stockholders or be retained to invest in  
8 new rate base. There would be no increase in accumulated depreciation or any other account that  
9 would be used to reduce future rate bases.

10  
11 **Q. MR. CLINE CRITICIZED STAFF WITNESS TRAXLER ASSERTION THAT THE**  
12 **COMPANY HAD AN INCENTIVE TO MAXIMIZE THE EQUITY RETURN USED**  
13 **IN THE DETERMINATION OF RATE BASE. (CLINE REBUTTAL, PAGE 2,**  
14 **LINES 12 - 23) PLEASE COMMENT.**

15 **A.** Mr. Traxler's concern is very valid and Mr. Cline's attempt to dismiss it serves only to benefit the  
16 Company. If the Company is able to convince the MPSC to maximize its earnings and to the extent  
17 those increased incremental earnings (above a just and reasonable level absent cash flow concerns)  
18 are reinvested in the new investments, current ratepayers will not only effectively fund those new  
19 investments, future ratepayers will be required to pay a "return on" and a "return of" those same  
20 investments. Stated another way, the Company will have rate base upon which it receives a "return  
21 on" and a "return of" and for which the ratepayers actually provided the funding.

1 This possibility clearly represents a distinct financial incentive for KCPL to maximize its return on  
2 equity recommendation to this Commission in any manner possible. Mr. Cline's unfounded criticism  
3 ignores that the RPAA is calculated after the revenue requirement. Mr. Cline's position also ignores  
4 that in fact it is Company witness Dr. Hadaway that makes a 50 basis point adjustment to his study of  
5 the cost of equity. The result is that the Company's recommended return on equity is 20 basis points  
6 above the high end of his "Reasonable DCF Range" (Hadaway direct, page 35, line 11, 20, & 21).  
7 KCPL has also proposed to include less than the anticipated level of off-system sales margins in the  
8 revenue requirement determination in this case. This proposal would also increase earnings above a  
9 just and reasonable level 75% of the time base on the anticipated outcomes related to off-system sales.

10  
11 While it is readily apparent to the objective observer, I would will emphasize that the effect of the two  
12 KCPL recommendations regarding off-system sales and Dr. Hadaway's earnings basis point  
13 adjustment, both of which serve to increase earnings, use completely conflicting reasoning in support  
14 of the individual adjustment. KCPL advocates that the Commission should use the 25<sup>th</sup> percentile of  
15 expected probabilities for off-system sales in order to reduce the risk associated with the earnings  
16 from off-system sales. KCPL then sponsors Dr. Hadaway who recommends a 50 basis point adder to  
17 his "Reference Group Cost of Equity Estimate" to reflect "company-specific risks and uncertainty  
18 KCPL is currently facing" (Hadaway direct, page 36, lines 2 – 3).

19 **Q. MR. GILES ASSERTS THAT FUTURE CASH FLOWS WILL BE NEGATIVELY**  
20 **IMPACTED BY THE ADDITIONAL AMORTIZATION. (GILES REBUTTAL,**  
21 **PAGE 14, LINES 3 - 21) PLEASE COMMENT ON MR. GILES**  
22 **ASSERTION.**

1 A. Mr. Giles' assertion is premised on his belief that the any accumulated amortization will have to be  
2 assigned to specific plant accounts no later than the end of the regulatory plan and the result will be  
3 that future depreciation rates will be reduced. Mr. Giles' concerns are unfounded for two reasons. I  
4 am not aware that the Regulatory Plan requires the specific assignment to plant accounts. The parties  
5 may present such a proposal but there is no requirement.

6 Paragraph III.B.1.i does not preclude KCPL, the Staff, Public Counsel, or any other  
7 party from requesting that this amortization be directed toward specific plant  
8 accounts or from requesting additional changes in depreciation rates that may result  
9 from depreciation studies.

10 (Regulatory Plan, page 40)

11 The second concern I have is that a reduction in depreciation rates based on such a transfer would  
12 effectively represent a shift in depreciation methodology from whole life depreciation rates to  
13 remaining life depreciation rates. This Commission has historically used whole life rates for electric  
14 companies. The result of a change such as Mr. Giles anticipates would transfer responsibility for a  
15 paying a return of investment from future ratepayers to current ratepayers.

16 **Q. MR. CLINE ADDRESSES THE BASIS FOR THE RPAA BEGINNING ON PAGE**  
17 **3 OF HIS REBUTTAL TESTIMONY. DO YOU HAVE ANY COMMENTS ON HIS**  
18 **VIEW POINT?**

19 A. Yes. Mr. Cline's understanding of the basis for the "compromise" that resulted in the RPAA may be  
20 KCPL's reasoning but I can say assuredly that it was not Public Counsel's. (Cline rebuttal, page 3,  
21 lines 12 – 16) While Public Counsel agrees that maintenance of credit quality is a desirable goal, it  
22 does not agree that "the sole purpose of the Additional Amortization mechanism is to **ensure** that  
23 KCPL maintains target levels for certain key credit metrics" (Cline rebuttal, page 3, lines 19 – 20,

1 emphasis added). The Regulatory Plan clearly sets out that the RPAA is designed to provide the  
2 **opportunity** for KCPL to meet certain financial metrics but that it is incumbent on KCPL to take  
3 prudent actions in order to try to actually achieve those metrics. A real concern to Public Counsel is  
4 that KCPL's parent company, Great Plains Energy Inc. (GPE), also owns Strategic Energy which  
5 Standard & Poors views as having a "much weaker business profile" in its August 1, 2006 Ratings  
6 Direct report. The RPAA is calculated on Missouri electric operations whereas S&P calculates its  
7 metrics on a GPE basis of actual results inclusive of Strategic Energy and other non-Missouri  
8 operations of GPE/KCPL. Clearly, the goal of the RPAA cannot be to "maintain" targets levels with  
9 regard to the credit metrics.

10 **Q. MR. CLINE ALSO ASSERTS THAT THE LEGAL FRAMEWORK REGARDING**  
11 **RETURN ON EQUITY WAS A PRIME DRIVER IN THE COMPROMISE**  
12 **RESULTING IN THE RPAA. DO YOU AGREE?**

13 **A.** No. It is true that KCPL floated the idea of a preset return on equity for the entire construction period  
14 of Iatan II but that was part of a package that included predetermined rate changes without any  
15 regulatory review during the same period based on forecasted construction costs and forecasted in-  
16 service dates. Mr. Cline does recognize that the proposal was illegal under Missouri law. How he  
17 can assert that by making a proposal that would not meet legal standards somehow influenced the  
18 other parties is curious. I can state emphatically that the proposal had no impact on Public Counsel's  
19 position in developing the RPAA.

20 Public Counsel recognizes that during periods of large construction projects with long lead times, the  
21 cash flow is an issue that the parties needed to address. Since the change in tax laws in 1986  
22 mandated the use of normalization treatment of tax timing differences for ratemaking purposes (the

1 Commission authorized flow-through treatment of tax-timing differences prior to 1986), the option  
2 previously used of increasing cash flow via the use of normalization treatment of tax timing  
3 differences was not available to the Commission. The only other two options to materially increase  
4 cash flow, and thus Funds From Operations, are accelerated depreciation or increased earnings. The  
5 RPAA was developed to provide additional funds via an amortization that is to be calculated based on  
6 specific criteria so that Missouri operations would have rates set based on certain credit metrics as  
7 part of the regulatory process.

8 **Q. DOES THIS CONCLUDE YOUR SURREBUTTAL TESTIMONY?**

9 **A. Yes.**