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Witness: Chris B. Giles
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Sponsoring Party: Kansas City Power & Light Company
Case No.: ER-2006-0314
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MISSOURI PUBLIC SERVICE COMMISSION

CASE NO.: ER-2006-0314

SURREBUTTAL TESTIMONY

OF

CHRIS B. GILES

ON BEHALF OF

KANSAS CITY POWER & LIGHT COMPANY

**Kansas City, Missouri
October 2006**

***** [REDACTED] *** Designates that "Highly Confidential" Information has been
Removed Pursuant to the Standard Protective Order.**

SURREBUTTAL TESTIMONY

OF

CHRIS B. GILES

Case No. ER-2006-0314

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

2 A. My name is Chris B. Giles. My business address is 1201 Walnut, Kansas City, Missouri
3 64106.

4 **Q. By whom and in what capacity are you employed?**

5 A. I am employed by Kansas City Power & Light Company ("KCPL") as Vice President,
6 Regulatory.

7 **Q. Are you the same Chris B. Giles who pre-filed direct and rebuttal testimony in this**
8 **proceeding?**

9 A. Yes, I am.

10 **Q. What is the purpose of your testimony?**

11 A. The purpose of my testimony is to clarify for the Commission that KCPL's position in this
12 case regarding off-system sales margins is not inconsistent with or in violation of the
13 Stipulation and Agreement in Case No. EO-2005-0329 as alleged in the rebuttal testimony
14 of Staff witnesses Mr. Traxler and Mr. Featherstone, and Office of Public Counsel witness
15 Mr. Kind. In addition, I will demonstrate based on recent market changes, why it is
16 necessary to evaluate the off-system sales market on a forward basis contrary to Staff's and
17 OPC's position that historical data should be utilized.

1 **Q. Please explain why KCPL agreed to the provision in the Stipulation and Agreement in**
2 **Case No. EO-2005-0329, that it would not propose any adjustment that would remove**
3 **any portion of its off-system sales from its revenue requirement determination in any**
4 **rate case.**

5 **A.** At the time KCPL and other parties to the case negotiated the Stipulation and Agreement it
6 was KCPL's position, and it is KCPL's position today, that a utility has no inherent right to
7 retain off-system sales profit or margin as long as the fixed costs of the generation assets
8 utilized to supply power to the off-system market are in rate base and those costs are
9 included in retail rates. It was KCPL's perception that other parties to the agreement desired
10 to commit KCPL to this position during the term of the regulatory plan and KCPL agreed to
11 do so. Based upon this agreement, KCPL could not propose a sharing of off-system sales
12 profit. KCPL has not proposed a sharing of profit in this case. Contrary to testimony of
13 Staff and OPC, KCPL is not inconsistent with or in violation of the Stipulation and
14 Agreement. Staff and OPC take a very limited view of KCPL's agreement to this provision
15 in the Stipulation and Agreement. They refuse to acknowledge the risk of the off-system
16 sales market, and they continue to complain without merit that KCPL's proposal to
17 recognize the risk of this market is inconsistent with the terms of the Stipulation and
18 Agreement.

19 **Q. What was the basis of KCPL's proposal to use projected off-system sales margins for**
20 **calendar year 2007?**

21 **A.** I have covered this extensively in my rebuttal testimony. A summary of KCPL's position is
22 that historical data related to off-system sales margins is absolutely meaningless when
23 setting retail rates, particularly when approximately 50 percent of the earnings included in
24 determining those retail rates are based upon an off-system sales market that is volatile. The

1 market is based on market prices for electric energy largely driven by natural gas prices,
2 generation unit availability, and retail sales levels. KCPL witness Mr. Michael Schnitzer
3 updates the most recent projections of this market for calendar year 2007 and discusses the
4 risk of the market in his surrebuttal testimony. The volatility of this market can be no more
5 apparent than changes in the market in just the past three months or even the past thirty
6 days. Since KCPL supplied its update (supported by Mr. Schnitzer) to the parties in this
7 case in July of 2006, the median value of off-system sales margins KCPL expects for the
8 year 2007 have declined from **[REDACTED]** on a total Company basis to a median value
9 in the range of **[REDACTED]**. The 25 percent point on the curve, the
10 point KCPL proposes to set its off-system sales margin in this case, will also decline. As
11 stated in the surrebuttal testimony of Mr. Schnitzer, these results are preliminary and will be
12 updated in the True-Up. The updated distribution of KCPL's contribution margins as of
13 September 30, 2006 has shifted to the left from the distribution prepared and referenced in
14 the rebuttal testimony of Mr. Schnitzer. There can be no better evidence of the risk of this
15 market when establishing retail rates than what has occurred in the past three months. Retail
16 customers receive the benefit of this market but absent a return on equity adjustment (as
17 described in my rebuttal testimony) or selection of a point on the curve that provides a
18 realistic opportunity for the Company to earn the return allowed during the first and only
19 year these rates will be in effect, the Company will not likely have sufficient cash flow to
20 meet its credit requirements even with amortization.

21 **Q. Does Staff, OPC, or any other party take issue with Mr. Schnitzer's analysis?**

22 A. No. To date, no party to this proceeding has taken issue with Mr. Schnitzer's analysis. Staff
23 and OPC appear to believe if they ignore the potential of this market in 2007 and hide
24 behind their test year adjustments and limited view of the Stipulation and Agreement in Case

1 No. EO-2005-0329, then the necessity for the Commission to recognize the impact of this
2 market in this case, and the very significant and substantial impact of not recognizing it on
3 the ability of the Company to maintain its stock price and credit quality, will just go away.

4 **Q. Is there any reason why the Commission could not adopt the Company's position on**
5 **this issue?**

6 A. No. Test year adjustments, and normalizations are utilized in an effort to mirror ongoing
7 operations of the Company, particularly during the year that the increased rates are in effect.
8 As Mr. Kind states in his rebuttal testimony, various means may be used to determine the
9 most reliable estimate of ongoing operations. There is not a Commission rule or statute or
10 any other provision that I am aware of that would prevent the Commission from utilizing a
11 detailed uncontroverted probabilistic analysis of off-system sales margins to determine the
12 appropriate level of off-system sales margins to include in determination of revenue
13 requirement in this case. In fact, I believe this is a method that should be utilized in future
14 cases to recognize the risk of this market. As I stated in my rebuttal testimony, the
15 Commission should award KCPL a basis point adder for this market risk or conversely
16 adopt KCPL's recommended level of off-system sales margins that will be provided in the
17 True Up. Contrary to the allegations of Staff and OPC, adjusting return on equity for the
18 risk of this market is not inconsistent with or in violation of the Stipulation and Agreement
19 in Case No.2005-0329.

20 **Q. Are there any other issues related to off-system sales margins?**

21 A. Yes, Staff witnesses Mr. Traxler and Mr. Featherstone, and DOE witness Mr. Dittmer
22 oppose KCPL's allocation of off-system sales margins based on unused energy. KCPL
23 witness Mr. Don Frerking provides direct and surrebuttal testimony regarding the details of
24 the calculation. However, Mr. Featherstone indicates KCPL has not provided a basis for use

1 of this allocation method and in addition questions why this allocation has not previously
2 been utilized. I will clarify KCPL's position on this issue.

3 **Q. Please continue.**

4 A. I am not aware of any case where off-system sales margins have been allocated between
5 jurisdictions. I know for a fact that it has never been done in a KCPL case. Thus, the
6 allegation that KCPL is not following prior allocation methodology is incorrect. This also
7 highlights the aversion the Staff's witnesses have to addressing significant new issues that
8 arise from this relatively new off-system sales market. They ignore the risk of this market
9 and fail to utilize an appropriate method to directly allocate off-system sales margins
10 between jurisdictions. Instead, they rely on an outdated and inappropriate method of
11 allocation based upon a jurisdictional retail energy ratio. Off-system sales margins may be
12 defined as the amount of revenue received in excess of the fuel cost attributable to the sale
13 of the energy. In each of KCPL's prior cases, margin was never separately identified. Total
14 revenue received from the sale of energy was allocated to KCPL's Missouri and Kansas
15 jurisdictions based upon a jurisdictional energy ratio because most of the revenue was
16 simply offsetting the fuel cost. Total revenue was small and margin averaged \$3 to
17 \$6 dollars per mwh compared to current average margins of \$30 to \$40 per mwh. Revenue
18 in excess of fuel costs was not enough to attempt to separate the margin from fuel cost for
19 allocation purposes during prior rate cases, thus total revenue was allocated on a mwh ratio.
20 The ability to sell into the off-system sales market is predicated on first meeting retail load
21 requirements. Only unused energy of retail customers is available to sell into this market. It
22 is logical and equitable to allocate off-system sales margin between KCPL's Missouri and
23 Kansas retail jurisdictions based on the unused energy of each jurisdiction. KCPL utilized
24 this allocation methodology because it is the right thing to do. The result of this method

1 compared with an energy mwh ratio is to allocate slightly more margin to KCPL's Kansas
2 jurisdiction because the Company's Kansas jurisdiction has a lower load factor than its
3 Missouri jurisdiction. The Commission's Staff ignores this reality and argues that it is
4 appropriate to allocate margin to Missouri in a manner that is neither logical nor equitable.
5 Unlike previous cases, margins are now identifiable, and thus should be allocated separately
6 from fuel cost. Staff did not propose a means of allocation but instead refuses to address
7 changes in the cost of service related to this market. This approach is similar to Staff's
8 decision to ignore the risk of the off-system sales market in determining KCPL's revenue
9 requirement. In addition, Staff spent an entire day deposing KCPL witness Mr. Frerking
10 regarding the impetus behind KCPL's allocation of the off-system sales margin in this case.
11 Staff made it clear to KCPL that they suspected some sort of collusion or conspiracy with
12 the Kansas Staff as the impetus for KCPL to pursue this allocation method. In fact, Kansas
13 Staff was unaware of KCPL's allocation method until KCPL filed its rate cases in both
14 states. Unused energy is the most equitable and appropriate allocation methodology.
15 Unfortunately, the Commission's Staff does not appear to be interested in what is most
16 equitable and appropriate. Instead, they prefer to rely on flawed historical calculations just
17 because such calculations favor Missouri over Kansas.

18 **Q. Does this conclude your testimony?**

19 **A.** Yes, it does.

NICOLE A. WEHRY
Notary Public - Notary Seal
STATE OF MISSOURI
Jackson County
My Commission Expires: Feb. 4, 2007