

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

Ag Processing, Inc.,)	
)	
Complainant,)	
)	
v.)	Case No. HC-2012-0259
)	
KCP&L Greater Missouri Operations)	
Company,)	
)	
Respondent.)	

**RESPONSE OF
KCP&L GREATER MISSOURI OPERATIONS COMPANY
TO STAFF’S REPORT AND RECOMMENDATION**

KCP&L Greater Missouri Operations Company (“GMO” or “Respondent”) hereby responds to Staff’s August 21, 2012 Report and Recommendation (“Report and Recommendation”), pursuant to the Commission’s April 5, 2012 Order Setting Procedural Schedule.

I. Introduction.

On August 21, 2012 Staff filed its Report and Recommendation, which set forth seven conclusions and recommendations for the Commission’s consideration. See Report and Recommendation ¶ 3 at 1-3. Concurrently with its Report and Recommendation, Staff filed Rebuttal Testimony of witness Cary G. Featherstone, which repeated those seven conclusions and recommendations. See Featherstone Rebuttal at 2-4.

Staff’s conclusions and recommendations are testament to its confusion as to the hedging costs at issue in this case, the purpose of hedging programs, who bears the ultimate responsibility to make hedging program management decisions, the contents of GMO’s Quarterly Cost Adjustment (“QCA”) tariff, and what damages are appropriate. This Response addresses Staff’s

confusion, made apparent in its Report and Recommendation, as well as in Mr. Featherstone's Rebuttal Testimony.

II. This complaint case concerns natural gas hedging costs in 2009.

The Complaint¹ filed by Ag Processing, Inc. ("AGP") asks this Commission to review a natural gas hedging program for GMO's steam operations at the Lake Road Plant in St. Joseph, Missouri ("steam hedging program") that Aquila, Inc. ("Aquila"), now known as GMO, implemented in February 2006 pursuant to the Nonunanimous Stipulation and Agreement ("Stipulation") that resolved Aquila's 2005 Steam Rate Case, Case No. HR-2005-0450. AGP alleges that Aquila's use of its steam hedging program to mitigate natural gas price volatility for its steam operations was imprudent during the 2009 QCA period covered by those proceedings.

Without due attention to the facts presented in the pending case, Staff's first conclusion in its Report and Recommendation is that GMO allegedly was imprudent in managing its steam hedging program because it made hedge purchases "based unreasonably on estimates of steam loads supplied by the steam customers that consistently were overstated." See Report and Recommendation ¶ 3 (1) at 1-2. This conclusion is indistinguishable from that drawn by the Commission in its September 28, 2011 Report and Order ("Report and Order") in AGP's first complaint case, No. HC-2010-0235 ("first complaint case"), which related to the hedging practices of GMO's predecessor Aquila, Inc. that occurred in *2006 and 2007*. Yet the facts in the present case, particularly those relating to the forecasts of GMO's customers concerning the year *2009*, are vastly different from those years.

In the case addressing GMO's steam hedging costs in 2006 and 2007, the Commission found that GMO was not imprudent in adopting a natural gas hedging program for its steam

¹ AGP filed a Prudence Challenge in the form of a Complaint in Case No. HR-2010-0028 on January 29, 2012. Subsequently, the Commission severed the complaint from this case and filed the Complaint in the subject docket, Case No. HC-2012-0259, on January 30, 2012.

service and that the program was not imprudently designed. See Report and Order at 10-11. However, the Commission did find that Aquila failed to prove that it operated the steam hedging program in a prudent manner, finding that Aquila relied on its customers' inaccurate forecasts of their use. Id. at 14-16.² While AGP "offered Aquila reasonably accurate estimates of its steam usage" for 2006 and 2007, the subject years of AGP's first complaint case, the Commission found that other steam customers' forecasts were unreliable, and that it was GMO's responsibility to determine the reasonableness of those forecasts. Id. at 15-16.³

The facts are quite different for the year 2009, the subject year of the present Complaint. As shown in Schedule TMN-3, attached to the Rebuttal Testimony of GMO witness Timothy M. Nelson, AGP's budget variance in 2009 accounts for the majority of the variance between budgeted and actual burn for that year. See Nelson Rebuttal at Schedule TMN-3. Schedules TMN-4A and TMN-4B provide further evidence that AGP is the primary contributor to the swings in steam demand. See Nelson Rebuttal at Schedules TMN-4A and TMN-4B.

In other words, AGP's forecasts of its steam needs were not "consistently" overstated. However, they were overstated for the budget year 2009. See Nelson Rebuttal at 8-9, 12-13. Nevertheless, Staff argues in its Report and Recommendation that GMO imprudently made its hedging purchases based on the "consistent" overstatements of steam requirements by GMO's customers. See Report and Recommendation ¶ 3 (1) at 1-2. While the Commission determined that such was the case with regard to GMO's 2006 and 2007 hedge costs, this certainly is not the case with regard to GMO's 2009 hedge costs. In that year, formerly "reasonably accurate" AGP

² Subsequent to the denial of rehearing, GMO appealed the case to the Missouri Court of Appeals for the Western District, where it is currently pending as Case WD74601. The appeal has been fully briefed, and oral argument is scheduled to occur on Wednesday, September 19, 2012.

³ The Commission's determination on this issue is a point GMO raises on appeal. GMO maintains that such findings set an unreasonable and dangerous standard. Not only are a utility's industrial customers in the best position to forecast their volume requirements, as they possess all of the knowledge and expertise to make such a forecast, but a utility simply is not in the business of second guessing sophisticated industrial customers' volume estimations. A utility's business is quite the opposite, as a utility is obligated to provide adequate service. See MO. REV. STAT. § 393.130.1.

accounted for the majority of the variance between budgeted and actual burn. See Nelson Rebuttal at 8-9, 12-13.

In other words, the “consistently” overstated forecasts of GMO’s other steam customers were not the problem in 2009. Rather, AGP, which historically provided “reasonably accurate estimates of its steam usage,” is the customer that Staff presumably would find GMO “unreasonably” relied upon in 2009. GMO’s reliance on a historically “reasonably accurate” customer cannot amount to imprudence for 2009 steam hedging costs. Staff cannot fall back on the Commission’s determinations with regard to 2006 and 2007 steam hedging costs for a conclusion of imprudence for the year 2009. Issues with usage forecasted for 2006 or 2007 have no bearing on 2009 hedging program costs. See Rebuttal Testimony of Wm. Edward Blunk at 30.

III. Hedging programs such as GMO’s are not designed to make a profit.

In its second conclusion in its Report and Recommendation, Staff alleges that GMO was imprudent for failing to liquidate or unwind hedge positions entered into prior to the November 1, 2007 suspension of the steam hedging program. See Report and Recommendation ¶ 3 (2) at 2. Failure to liquidate or unwind positions in 2008, Staff alleges, prevented GMO from realizing gains on those hedges. Id.; Featherstone Rebuttal at 18-21. In drawing this conclusion, however, Staff fails to understand that the goal of Aquila’s steam hedging program was to mitigate price volatility -- not make a profit -- regardless of whether prices rose or fell. See Blunk Rebuttal at 12-15.

It is, therefore, important to understand how a hedging program mitigates upward price volatility, and that a prudent hedging program does not always result in savings to net fuel costs, as the Commission and its Staff have previously recognized. See Order Finding Necessity For Rulemaking, In re Proposed Rulemaking Concerning Mitigation of Natural Gas Price Volatility,

Case No. GX-2002-478 (Apr. 16, 2002); 4 CSR 240-40.018(1)(A) & (C); Joint Report on Natural Gas Market Conditions, PGA Rates, Customer Bills & Hedging Efforts of Missouri's Natural Gas Local Distribution Companies, In re Investigation into Status of Missouri's Natural Gas Local Distribution Companies' Compliance with 4 CSR 240-40.018, Case No. GW-2006-0110 (Feb. 24, 2006) ("Joint Report").

Indeed, the Joint Report stated that the "goal of hedging is not to 'beat the market' but rather to mitigate upward price volatility." See Joint Report at 8. The Commission further determined in its Report and Order in AGP's first complaint that "the point of a hedging program is to decrease volatility, not to speculate on windfall profits or losses." See Report and Order at 14.

It is this goal that distinguishes hedging from speculation. As described by GMO witness Wm. Edward Blunk, hedgers take positions to protect against adverse price movements in future periods. See Blunk Rebuttal at 11. Closing positions prematurely removes that protection. Id. Speculators, on the other hand, attempt to time the market and remove positions to take a profit. Id. Mr. Featherstone appears to agree, stating that "Staff fully expected there would be losses along with gains to smooth out the volatility of natural gas." See Featherstone Rebuttal at 26. However, GMO suspended its steam hedging program in 2007 at the request of AGP, preventing it from potentially realizing any gains that Staff would expect to occur "at some point." Id.

Nevertheless, Staff now criticizes GMO for failing to liquidate or unwind its hedging positions and, as a result, not realizing a profit from its steam hedging program in 2008. See Report and Recommendation ¶ 3 (2) at 2. Staff believes that GMO should have liquidated positions when the market turned in 2008 so as to realize economic gains at that time. See Featherstone Rebuttal at 16, 21. Mr. Featherstone advocates that "Aquila should have taken advantage of the market condition and captured any gain." Id. at 16.

Such action by GMO would amount to speculation, the purpose of which is to profit from betting on the direction in which a market will be moving. See Blunk Rebuttal at 28. Hedgers like GMO that do not engage in speculation intentionally and prudently allow positions to simply run their course. Id. at 11.

Mr. Featherstone also makes much of the fact that AGP requested that GMO suspend its steam hedging program on November 1, 2007, believing this fact to bolster his conclusion that GMO should have engaged in speculation and liquidated or unwound its remaining hedge positions in 2008. See Featherstone Rebuttal at 15-16, 20. However, the email Mr. Featherstone quotes at page 15 of his Rebuttal Testimony, from AGP witness Mr. Johnstone to GMO confirming suspension of the program, clearly shows that AGP did not request that GMO liquidate or unwind existing hedge positions; it shows that AGP understood GMO to be merely “suspending” its hedging program. Id. at 15 (quoting Clemens Rebuttal at Schedule GLC-6).

Contrary to Mr. Featherstone’s belief that this email is an indication that AGP “did not want to absorb the risk of any hedging program” (see Featherstone Rebuttal at 16), Mr. Johnstone’s email goes on to state that he understands that GMO plans to “meet with your steam customers in the near future before making a decision regarding the future of the hedging program.” Id. at 15. Clearly, AGP contemplated that the steam hedging program would continue to run its course after suspension and that GMO would take no action with regard to remaining hedge positions without first consulting its steam customers. Liquidating or unwinding hedge positions without first consulting AGP would be contrary to Mr. Johnstone’s email.

This fact is bolstered, not weakened, by the emails attached to GMO witness Gary L. Gottsch’s Rebuttal Testimony that Mr. Featherstone quotes at pages 19-20 of his Rebuttal Testimony. Not only did Mr. Gottsch adjust hedge purchases to meet the new budgeted volumes

updated in 2006 and 2007, but it was GMO's regular course of action to unwind excess hedges when volume information was updated. See Gottsch Rebuttal at 14-15, Schedules GLG-2 and GLG-3. As demonstrated by the emails Mr. Featherstone quotes, GMO prudently unwound excess hedges, but did not unwind all hedges as such would amount to speculation. Id.

Furthermore, as discussed by Mr. Gottsch and Mr. Clemens in their Rebuttal Testimony, GMO allowed its existing hedge positions to run their course at the instruction of Mr. Johnstone and Mr. Conrad, counsel for AGP. See Gottsch Rebuttal at 16-17; Clemens Rebuttal at 11. Mr. Gottsch recalls such instruction occurring at a May 2008 meeting attended by Mr. Johnstone, Mr. Conrad, numerous GMO representatives, and Mr. Featherstone. See Gottsch Rebuttal at 16. Mr. Clemens recalls the meeting as occurring at some point in the Spring of 2008. See Clemens Rebuttal at 11. Mr. Featherstone's testimony about an April, 22 2008 meeting at the Lake Road Plant is beside the point, as Mr. Gottsch recalls the meeting as occurring in May and his name does not appear on Mr. Featherstone's attendance sheet for the April meeting. See Featherstone Rebuttal at Schedule CGF-4.

The email chain between AGP and GMO in the Spring of 2008 that Mr. Featherstone attaches as Schedule CGF-6 to his Rebuttal Testimony also indicates that there was a meeting between the parties later than that held on April 22, 2008. On April 24, 2008, AGP witness Mr. Johnstone emailed GMO that he understood "some work has been done by Aquila in regard to the suggestions made on behalf of the customer group." See Featherstone Rebuttal at Schedule CGF-6 at 2. Mr. Johnstone requested a conference to bring AGP up to speed on this strategy. Id. There is a large gap between the May 9, 2008 email from GMO to AGP regarding scheduling a meeting to discuss "work" done by Aquila on a steam hedging strategy and the June 5, 2008 email from GMO to AGP regarding meeting to discuss a steam audit. Id. at 1-2. On June 27, 2008, AGP circulated a draft steam hedging strategy, indicating that the parties had

met between the time of AGP's April 24, 2008 email to GMO to discuss such strategy and June 24, 2008 email containing AGP's revisions to that strategy. Id. at 1.

Thus, not only did GMO prudently allow its hedge positions to run their course after the November 1, 2007 suspension of its steam hedging program -- as liquidating or unwinding such positions would amount to speculation and the goal of Aquila's steam hedging program was to mitigate price volatility, not make a profit -- but it did so because it had agreed to consult with AGP "before making a decision regarding the future of the hedging program." See Featherstone Rebuttal at 15. The parties disagree as to whether AGP ever instructed GMO to allow its existing hedge positions to run their course. Whether such instruction ever occurred is an extraneous point, however, as Mr. Johnstone's email confirms that GMO was to take no action with regard to the steam hedging program without first meeting with its steam customers. GMO, like any other hedger seeking to mitigate price volatility, normally and prudently allowed its positions to simply run their course. See Blunk Rebuttal at 11. No party has offered any evidence of instruction to act in what would be a clear deviation from normal hedging practice.

IV. GMO prudently administered its steam hedging program in the best interest of its customers and with their input.

In Staff's third, sixth, and seventh conclusions in its Report and Recommendation, Staff makes contradictory, and somewhat demeaning, points about the responsibilities of GMO and its customers with regard to the management of its steam hedging program. See Report and Recommendation ¶ 3 (3), (6), and (7) at 2-3; Featherstone Rebuttal at 18, 34. Staff first states that "GMO had the obligation to operate and make prudent decisions in what is the best interest of its customers and the Company's financial condition regardless of the desires of its customers." Id. ¶ 3 (3) at 2. Apparently (and illogically) believing that, much like children, GMO's sophisticated industrial steam customers' "desires" might not align with their "best

interests,” Staff asserts that GMO ultimately has the responsibility to operate its business. Id. Staff goes on to state, however, that because AGP “was and is such a significant steam customer, it should have some level of influence of [sic] the GMO steam operations.” See Featherstone Rebuttal at 34; Report and Recommendation ¶ 3 (6)-(7) at 2-3.

Staff’s conclusions that GMO must act in loco parentis, acting in the best interests of its customers as it sees fit (Id. ¶ 3 (3) at 2), but also that prudent management involves coordinated action with its sophisticated industrial customers (Id. ¶ 3 (6)-(7) at 2-3), contradict each other. The fact is that GMO has prudently administered its steam hedging program in the best interest of its customers with their input since its inception in 2006.

The Commission found in AGP’s first complaint that GMO was prudent in adopting a steam hedging program (Report and Order at 9-10), and that GMO’s hedging program was prudently designed (Report and Order at 11). GMO prudently administered its One-Third Strategy by hedging to the most accurate volumes possible, based on information received directly from steam customers who continued to assure GMO that their operations would require such levels of service. See Rebuttal Testimony of Joseph G. Fangman at 4-9. Those customers are in the best position to determine their steam load requirements, and GMO has a duty to them to ensure reliable steam service based on those customers’ anticipated needs. Id. at 9. GMO adjusted its forecasts and hedge purchases in light of customer requirements. See Gottsch Rebuttal at 14-15.

GMO certainly agrees that it will consult with its steam customers before reinstituting a steam hedging program, as it has done since the program’s suspension in 2007. See Clemens Rebuttal at 11-12. GMO also agrees that it bears the responsibility to procure natural gas and any other commodity necessary for the safe and reliable operations of steam service. See Report and Recommendation ¶ 3 (7) at 3. However, GMO cannot stress enough that it necessarily

depended upon the forecasts of its five steam customers when setting the budget upon which hedge purchases were made. See Fangman Rebuttal at 4-9, Nelson Rebuttal at 3-5, and Gottsch Rebuttal at 11-12. Those customers are in the best position to determine their steam load requirements. See Fangman at 9.

As of July 27, 2006, the day the first hedge was placed for 2009 according to GMO's prudently designed steam hedging program, GMO had no way of knowing that customer load in 2009 was going to be lower than its steam customers had projected. See Blunk Rebuttal at 30-31. As the budget was updated, however, Mr. Gottsch adjusted volumes and hedge plans accordingly, liquidating hedge positions to get hedges down to levels that were in sync with the amounts set forth in the One-Third Strategy. See Gottsch Rebuttal at 14, Schedule GLG-2 at 4-6. GMO thus did "operate and make prudent decisions in what is the best interest of its customers and the Company's financial condition." See Report and Recommendation ¶ 3 (3) at 2.

V. Staff never conducted a Step Two prudence review and never, until this point, issued a report alleging imprudence.

While Mr. Featherstone insists that he is familiar with GMO's Quarterly Cost Adjustment ("QCA") mechanism, he nevertheless plainly misunderstands it. See Featherstone Rebuttal at 1, 2, 9, 11, 12, 17, 21, 24-27, 31-34. Mr. Featherstone states that he "reviewed and monitored the QCA filings made by GMO and the related costs relating to the steam operations made as part of these filings starting with the first year of the QCA the 2006 partial year and each subsequent year for 2007 through 2011." Id. at 11. He "was personally involved in the prudency phase of the QCA process." Id. at 2.

Nevertheless, Mr. Featherstone is unclear about when he first learned of GMO's steam hedging program, which used a One-Third Strategy nearly identical to that used for its electric

operations. See Blunk Rebuttal at 13, Schedule WEB-2. Indeed, Mr. Featherstone admits that Staff was “not making a distinction between the two operations.” See Featherstone Rebuttal at 25. Oddly, Mr. Featherstone denies any transparency in the implementation of GMO’s steam hedging program, despite consistently referring to GMO’s One-Third Strategy, used for both its steam and electric operations, as “the” hedging program. Id. at 22-27.

As the Commission is aware, Mr. Nathan Williams and Mr. Steven Dottheim, counsel for Staff, as well as Mr. Conrad, counsel for AGP, were present at the February 27, 2006 on-the-record presentation before the Commission in the 2005 Steam Rate Case where Aquila’s One-Third Strategy hedging program for its steam operations was specifically discussed. See Rebuttal Testimony of Gary L. Clemens at 7-8. The Stipulation that resolved the case had no requirement that GMO obtain prior approval from any signatory party before it made any hedge purchases or with regard to any particular purchases that it made. See Case No. HC-2010-0235 Tr. [Johnstone] at 65. Indeed, Aquila would not have implemented a gas hedging program for its steam operations if AGP had not requested that it do so. See Rebuttal Testimony of Gary L. Clemens at 5, 7-8.

What is truly surprising and what warrants significant attention in this Response is Mr. Featherstone’s ignorance of the terms of GMO’s QCA tariff, with which he claims to be familiar. See Featherstone Rebuttal at 1, 2, 9, 11, 12, 17, 21, 24-27. When asked about the QCA review process or the “two (2) step approach” that is contained on Tariff Sheet 6.4 (attached as Exhibit B to AGP’s Complaint), Mr. Featherstone misconstrues the tariff and stops short of any discussion of Staff’s Step Two full prudence review. See Featherstone Rebuttal at 31-32.

Mr. Featherstone discusses only Step One, apparently confusing the two elements of Step One with the two separate steps to Staff’s review process. Id. The Step One process, which is set forth in Section 6 of Sheet No. 6.4, calls for Staff to “ascertain” (a) that “the concept of

aligning of Company and customer interests is working as intended” and (b) “that no significant level of imprudent costs is apparent.” As GMO witness Tim Rush stated in his Rebuttal Testimony, Staff has submitted and the Company has responded to numerous requests investigating all aspects of the QCA. See Rush Rebuttal at 18. While Mr Featherstone notes that Staff has issued periodic reports regarding the QCA reviews (see Featherstone Rebuttal at 32), Staff has never, until its current Report and Recommendation, submitted any reports to the Commission alleging imprudence with regard to the QCA or any other irregularity. See Rush Rebuttal at 18.

Nor has Staff ever issued a report addressing the Step Two prudence review, which is set forth in Section 7 of Sheet No. 6.4, as correctly noted by Mr. Rush. Id. at 19. Pursuant to the QCA tariff, “Staff may proceed with Step Two, a full prudence review, if deemed necessary.” See Sheet No. 6.4, Section 7. The QCA tariff goes on to require that such full prudence review, if pursued, “shall be complete no later than 225 days after the end of each year. Such full prudence review shall be conducted no more often than once every twelve (12) months and shall concern the prior twelve (12) month period or calendar year only.” Id.

When asked why Staff never completed a Step Two full prudence review within the 225 day framework of the QCA, Mr. Featherstone merely stated that he was unaware of this threshold until the fall of 2008. See Featherstone Rebuttal at 33. This admission is startling, given that the QCA was first initiated in March of 2006 as an outcome of Aquila’s 2005 steam rate proceeding, regarding which Mr. Featherstone was “one of two case coordinators.” Id. at 21. Furthermore, Staff had the opportunity in 2010 (well after Mr. Featherstone claims to have learned of the threshold) to proceed with a Step Two full prudence review of the 2009 steam hedging costs that are at issue in the present Complaint, but chose not to.

Staff's ignorance of the terms of GMO's tariff is surprising, particularly because Mr. Featherstone "reviewed and monitored the QCA filings made by GMO" from 2006 through 2011. Id. at 11. Regardless, Staff felt no need to conduct a Step Two full prudence review, as it believed "sufficient progress was being made on the hedging concerns and other issues to not file a report within the 225 day window for either the years 2006 or 2007." Id. at 33.

Oddly, however, Staff now concludes that GMO was imprudent with regard to its steam hedging program costs for 2009 -- a program whose adoption, design, and administration has not changed since 2006. This inconsistency aside, Staff's conclusion of imprudence in its Report and Recommendation and Mr. Featherstone's Rebuttal Testimony clearly fall well beyond the 225 day threshold contained in the QCA tariff.

VI. A refund to all steam customers upon a finding of imprudence is inappropriate.

In its fifth conclusion in its Report and Recommendation, Staff states that the Commission should order a refund of hedging costs to all steam customers, to be consistent with AGP's first complaint case. See Report and Recommendation ¶ 3 (5) at 2. First and foremost, the instant case and Case No. HC-2010-0235 are two separate matters with distinct facts concerning customer forecasts. A blind damages award, simply ordered in the name of "consistency," amounts to a denial of due process. Due process is violated if a proceeding "offends some principle of justice so rooted in the traditions and conscience of our people as to be ranked as fundamental." Snyder v. Massachusetts, 291 U.S. 97, 105 (1934). Because the facts of AGP's two hedging complaint cases are distinct and because an identical damages award for consistency's sake would be fundamentally unfair, Staff's conclusion should be disregarded.

In AGP's first complaint case, the Commission admitted that Aquila's steam customers other than AGP "significantly overestimated the amount of steam they would use," while "AGP offered Aquila reasonably accurate estimates of its steam usage." See Report and Order at 15.

The reverse is true in the present case. As noted above, in this case it is AGP's budget variance that accounted for the majority of the variance between budgeted and actual burn for the year at issue, and AGP was the primary contributor to the swings in steam demand. See Nelson Rebuttal at Schedules TMN-3, TMN-4A, and TMN-4B. Hence, while GMO's other steam customers may have a valid claim against GMO (though only one other customer has actually joined in this Complaint), AGP has a much weaker case.

Furthermore, a refund of steam hedging costs to all of GMO's steam customers is inconsistent with the QCA tariff. For this reason, among others, the Commission's erroneous order in AGP's first complaint case that GMO refund that portion of the cost of the hedging program borne by all of its steam customers during the two relevant years currently is on appeal.⁴ Of note in the present case is that the Commission's misplaced rationale with regard to its ability to order a refund to all customers, even though only two have complained, persists in Staff's Report and Recommendation and Mr. Featherstone's Rebuttal Testimony.

Despite the clear QCA tariff provisions for a full prudence review by Staff, Mr. Featherstone believes that "it was primarily the responsibility of the entities who developed the QCA, Aquila (GMO) and Ag Processing," to address any issues with the steam hedging program. See Featherstone Rebuttal at 34. Mr. Featherstone correctly notes that Staff's failure to conduct a full prudence review does not preclude a customer from initiating a complaint for the purpose of pursuing a prudence review. Id. Nevertheless, such a complaint is not a "full prudence review" and any refund ordered by the Commission therefore does not apply to customers other than those who complain.

Significantly, the Commission stated in AGP's first complaint that a full prudence review and a complaint plainly are not the same thing.

⁴ See note 2, supra.

The tariff contemplates that a “full prudence review” is one that is conducted by Staff. The tariff goes on to state that any customer may initiate a complaint to pursue “a prudence review” and that the customer will not be prejudiced by the lack of a “full prudence review.” The Commission interprets these provisions as clearly setting out two different types of prudence reviews. One that may be initiated by Staff within 225 days of the end of the year; and one that may be initiated by a customer through the complaint process without a specific time limitation and without prejudice by Staff having not conducted a “full prudence review.” [Order Denying Motion to Dismiss at 4, Case No. HC-2010-0235 (July 21, 2010) (emphasis added)].

It is, therefore, startling that Staff would suggest the Commission reward customers (a) who never filed a complaint and (b) who never resorted to the complaint procedures offered by the QCA Rider. Because AGP’s Complaint is not a “full prudence review,” a refund to all GMO industrial steam customers, as recommended by Staff, is inappropriate.

VII. Conclusion.

Staff’s conclusion of imprudence and recommendations regarding prudent hedging program management are muddled at best and reveal its uncertainty as to the facts of this case and the QCA tariff that controls it. Staff’s conclusion of imprudence also is untimely, as it falls well outside the 225 day threshold for a Step Two full prudence review, which is set forth in Section 7 of Sheet No. 6.4. Finally, Staff’s conclusion of imprudence is inconsistent with its belief that “sufficient progress was being made on the hedging concerns and other issues to not file a report within the 225 day window for either the years 2006 or 2007.” See Featherstone Rebuttal at 33. Indeed, GMO’s steam hedging program has not changed since 2006.

Staff has never, until its current Report and Recommendation, submitted any reports to the Commission alleging imprudence with regard to the QCA and has never issued a report addressing the Step Two full prudence review. More than two years have passed since the closing of the 225 day window within which Staff could have proceeded with a Step Two full prudence review of 2009 steam hedging program costs, had Staff deemed such review necessary.

Nonetheless, and quite incongruously, Staff now criticizes GMO's management of its steam hedging program, rather than defend its decision not to proceed with a Step Two full prudence review.

Based on the circumstances that existed when GMO's steam hedging program was in effect -- including what GMO knew or should have known about the volatile price of natural gas, as well as the anticipated increase in load from GMO's steam customers -- the steam hedging program was prudently adopted, designed, and administered. As a result, there is no credible, factual basis for second-guessing the operation of GMO's steam hedging program.

Respectfully submitted,

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Certificate of Service

A copy of the foregoing was emailed this 18th day of September 2012 to all counsel of record.

/s/ Karl Zobrist

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