BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

In the Matter of the Application of Kansas City Power and Light Company for Approval to Make Certain Changes in its Charges for Electric Service to Implement Its Regulatory Plan.	**)))))**	**Case No. ER-2007-0291**

REPLY AND TRUE-UP BRIEF OF KANSAS CITY POWER & LIGHT COMPANY

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Kansas City Power & Light Company ("KCPL" or "Company") respectfully submits its Reply and True-Up Brief in accordance with the Commission's Order Setting Briefing Schedule issued on October 18, 2007, as modified by the Regulatory Law Judge on November 9, 2007. KCPL will discuss the issues addressed by the parties in their Post-Hearing Briefs filed on November 5, 2007, and considered during the True-Up Hearing held on November 9.

In light of the Missouri Supreme Court's recent decision in State ex rel. Office of the Public Counsel v. Public Service Commission, Case No. SC88390 (Mo., Oct. 30, 2007), KCPL respectfully requests that the Commission issue its Report & Order in this matter with sufficient time to allow for the preparation and review of the compliance tariffs by all parties. KCPL believes that if the Commission issued its decision by December 10, 2007, it would give the parties the necessary time to prepare and review the tariffs. The effective date of the tariffs would be January 1, 2008, as contemplated by the 2005 Regulatory Plan Stipulation.

The Company also respectfully requests that the Commission approve the Non-Unanimous Stipulation and Agreement Regarding Pensions between KCPL and Staff which was filed on November 13, 2007.

ISSUES IN THE CASE

A. Rate of Return

1. An 11.50% Return on Common Equity, consisting of a 10.75% Base ROE and a 50 Basis Point Adder, should be set by the Commission.

> **a. The Commission's approval of the Regulatory Plan in Case No. EO-2005-0329 does not justify a reduction in the ROE awarded in this case.**
>
> **b. KCPL's increased risk due to its large construction program justifies a 50 Basis Point Adder to the ROE.**

Neither Staff, OPC nor the Department of Energy ("DOE") offer any persuasive reason why the analysis of KCPL's expert witness Dr. Hadaway should be rejected. His recommendation was that a base ROE of 10.75% be adopted by the Commission, with a 50 basis point adder for construction risks, resulting in a total ROE of 11.25%.

The main objection that these three parties raise is that adopting such a recommendation would place KCPL's return on equity at the top of all ROEs, according to national surveys. However, if there is any candidate to receive an ROE that ranks high in the nation, it should be a medium-sized, well-performing utility like KCPL that faces financial challenges in these times of uncertain markets while it is in the midst of a billion-dollar construction program. As explained by Dr. Hadaway, KCPL in 2006 began the largest construction program in the United States compared with its existing asset base. In 2007 it dropped to third place in the nation, given that aspects of the program had gone into rate base. See Ex. 30. Because KCPL is in the middle of one of the largest construction projects in the nation, it deserves favorable consideration for one of the highest ROEs in the nation.

In its Post-Hearing Brief, Staff has conceded that both its and OPC's recommendations advocate below-average ROEs for the Company, with Staff coming in at the bottom. See Staff Post-Hearing Brief at 10. Instead of analyzing the reasons why KCPL should be awarded an above-average ROE, Staff instead engages in name-calling, arguing that "KCPL seeks a windfall" ROE that would represent "free money" and "no strings and no obligations" attached to its request. Id. at 16. Given the turmoil in the financial markets as KCPL continues its ambitious construction program endorsed by Staff in the 2005 Regulatory Plan Stipulation, these allegations ring hollow. Staff's reference in its brief to the Commission's denial of AmerenUE's request for an adder (id. at 13) is irrelevant to KCPL's request which is based on different facts applicable to a different utility with a different operational and performance record.

OPC attacks Dr. Hadaway's use of a 6.6% growth rate, arguing that it is unduly weighted toward historical trends. OPC also criticizes his risk premium analysis as "flawed." See OPC Initial Brief at 8. However, when given the opportunity to cross-examine Dr. Hadaway at the hearing on these and other points, OPC asked no questions. See Tr. 224-25. In his testimony Dr. Hadaway explained, contrary to OPC's view, that the 6.6% is actually weighted more toward recent history. See Ex. 11, Hadaway Direct at 35. See also Ex. 13, Hadaway Surrebuttal at 10-11. As he explained at the hearing in response to DOE's questions: "The 20-year average is included five times. And so we gave more weight to that more recent slightly lower inflation-influenced GDP. That weighted average, then, is the bottom line in there, the 6.6% forecast." See Tr. 228-29.

As the record demonstrates, OPC's expert witness Mr. Gorman used the extraordinarily low growth rate of 5.1%, far below even the rates used by Staff's Mr. Barnes, which ranged from 5.34% to 6.50%. See Ex. 201, Gorman Direct at 21; Ex. 105, Barnes Direct at 18 and Sched. 15.

Regarding the OPC criticism of the risk premium analysis, Dr. Hadaway testified that his risk premium of 4.25% was far more realistic than Mr. Gorman's 3.1%. As Hadaway noted:

"The flaw in Mr. Gorman's position is that there has not been a risk premium as low as 3.1% since 1994, when interest rates were much higher." See Ex. 13, Hadaway Surrebuttal at 11-12.

The parties opposing KCPL's ROE request have not only disputed the need for a construction adder, but actually argue that the ROE should be reduced because of the 2005 Regulatory Plan Stipulation. As explained by Dr. Hadaway during the hearing, while there is a reduction in risk to the Company's bondholders, any risk reduction to shareholders is *de minimis*. See Tr. 273-78.

OPC's hypothetical question to Mr. Gorman about a regulatory "blessing" of a $100 million power plant that experiences a $10 million overrun has no bearing to KCPL's situation. See OPC Initial Brief at 10. Although the 2005 Regulatory Plan Stipulation endorsed the construction of coal and wind generation, there was no pre-approval of any amount for any of the several infrastructure projects covered by the agreement. As Mr. Gorman himself admitted, there was no approval of any construction amounts or even a budget. See Tr. 340. See also Ex. 29, 2005 Regulatory Plan Stipulation at 36, 52.

The idea of awarding KCPL a below-average ROE, in light of its construction program, is simply irresponsible. New wind and coal generation, environmental retrofits, and extensive demand response, energy efficiency and customer assistance programs require at minimum an above-average return on equity. The Commission should continue the course that it set in 2006 by awarding an ROE that is above average with an adder to account for the unprecedented construction risks that KCPL faces at this time.

2. Capital Structure: What capital structure should be used for determining KCPL's rate of return?

KCPL and Staff agree that the capital structure that should be adopted by the Commission for purposes of setting rates in this case is the structure that reflects the actual capital structure of KCPL as of September 30, 2007.

That structure calls for 57.62% in equity, 40.93% in long-term debt, and 1.45% in preferred stock. See Ex. 36, Cline True-Up Direct at 1-2; Ex. 125, Barnes True-Up Direct at 2.

However, the Office of the Public Counsel ("OPC") proposes a hypothetical capital structure based upon KCPL's summer of 2007 projection of what it estimated its capital structure would be at the end of September, 2007. See Ex. 210, Gorman True-Up Direct Rebuttal at 3; Tr. 1164-65.

Hypothetical capital structures have generally not been favored by this Commission, except where the structure was viewed as inefficient and unreasonable, or when a utility's structure within a holding company system did not reflect the system's capital costs. See State ex rel. Missouri Gas Energy v. PSC, 186 S.W.3d 376, 389 (Mo. App. W.D. 2005)("MGE case"); State ex rel. Assoc. Natural Gas Co. v. PSC, 706 S.W.2d 870, 878-79 (Mo. App. W.D. 1985). The capital structure agreed to by KCPL and Staff reflects the capital structure of KCPL's owner Great Plains Energy (Ex. 36, Cline True-Up Direct at 1), so there is no question that it is a "real world" structure, such as the Commission endorsed in the MGE case. 186 S.W.3d at 389.

As Mr. Cline explained in response to questions from OPC and the bench, KCPL's capital structure does reflect the realities of the market. Although KCPL had planned to issue hybrid debt prior to the close of the third quarter, worldwide credit markets and the sub-prime mortgage crisis prevented the Company from accessing capital on attractive terms. Tr. 1151-54. Given the Company's prudent reaction to changed market conditions (Tr. 1160) and its need for a strong equity base during this period of intense infrastructure construction, there is no good reason to depart from reality and adopt a hypothetical capital structure.

B. Expense Issues

3. Hawthorn 5 Subrogation Proceeds: Should subrogation proceeds KCPL received in 2006 concerning the 1999 Hawthorn 5 boiler explosion litigation be included in cost-of-service for setting KCPL's rates?

Staff and OPC argue that the subrogation proceeds KCPL received in 2006 as a result of the 1999 Hawthorn 5 boiler explosion should be included in KCPL's cost of service in this case. Their argument is premised on the assertion that KCPL's customers paid the costs that the subrogation proceeds were intended to recover because KCPL appeared to be earning a reasonable rate of return during the 1999-2001 outage that resulted from the explosion. Staff's and OPC's arguments suffer from three fatal flaws.

First, for their argument to prevail, the Commission would have to determine whether KCPL did, in fact, earn a reasonable rate of return during the 1999-2001 outage. To base KCPL's prospective rates on earnings from 1999-2001 is the very definition of retroactive ratemaking. The Commission would have "to determine what a reasonable rate *would have been*" during the 1999-2001 outage and set KCPL's prospective rates accordingly. Utility Consumers Council of Missouri, Inc. v. PSC, 585 S.W.2d 41, 58 (Mo. 1979)(emphasis in original)("UCCM"). Such retroactive ratemaking is prohibited. It would be no more appropriate to include the subrogation proceeds in KCPL's cost of service in the present case than it would be for KCPL to attempt in this case to recover its outage-related expenses that were in excess of the Hawthorn 5 costs included in the Company's rates during the outage. In both cases, the request would constitute retroactive ratemaking. In UCCM, the Missouri Supreme Court defined retroactive ratemaking as "the setting of rates which permit a utility to recover past losses or which require it to refund past excess profits collected under a rate that did not perfectly match expenses plus rate-of-return with the rate actually established." 585 S.W.2d 41, 59 (Mo. 1979).

Second, assuming it would be appropriate to look to KCPL's earnings in 1999-2001, the only evidence in the record is the following testimony from Mr. Chris Giles: "The two years where we really struggled were '99, 2000 and part of 2001." Tr. 90, lines 21-22. Staff and OPC infer that KCPL's earnings must have been reasonable because KCPL agreed to a rate reduction in 1999 prior to the explosion and did not attempt to repudiate that agreement after the explosion occurred. Staff and OPC in essence seek to penalize KCPL for weathering the storm instead of seeking rate relief in 1999. If their position prevails, utilities will have little choice but to seek rate relief whenever a significant and unanticipated expense occurs.

Third, including the subrogation proceeds in KCPL's cost of service ignores the fact that neither the proceeds, nor the costs they were intended to recover, have anything to do with the test year in this case or with KCPL's continuing operations. KCPL filed suit in 2001, and judgment was entered in favor of KCPL in 2004. However, due to the length of the appellate judicial process, KCPL did not actually receive the proceeds until 2006. Tr. 131, lines 9-15. The timing of KCPL's receipt of the proceeds is happenstance.

For the foregoing reasons, the Commission should not include the Hawthorn 5 subrogation proceeds in KCPL's cost of service in this case.

a. If so, should the five-year amortization period proposed by Staff be adopted?

It is inappropriate to include the Hawthorn 5 subrogation proceeds in KCPL's cost of service in this case. As explained in KCPL's Post-Hearing Brief, doing so through an amortization does not change this result. Although amortizing the proceeds reduces the adverse impact on the Company, it does not address the fact that it is inappropriate to include the proceeds in KCPL's cost of service.

4. Long-Term Incentive Compensation Should the costs of KCPL's and GPE's long-term incentive compensation plans be included in cost-of-service for setting KCPL's rates?

See discussion below for Issue 5 which relates to both Long-term and Short-term Incentive Compensation.

5. Short-Term Executive Compensation: Should part of the costs of KCPL's and GPE's short-term executive compensation plans be excluded from cost-of-service for setting KCPL's rates?

In this proceeding, Staff and DOE have cited to previous Commission decisions which have disallowed incentive compensation programs principally upon the ground that such programs show no tangible benefits to Missouri ratepayers. (Staff Br. at 26; DOE Br. at 28). In this proceeding, KCPL is requesting that the Commission re-consider its past decisions in light of the competent and substantial evidence in this record that demonstrates that KCPL's short-term and long-term executive compensation plans have produced tangible benefits to KCPL's customers.

As explained in KCPL's Post-Hearing Brief at 22-23, KCPL witness Michael Halloran, a consultant with Mercer Human Resource Consulting, testified that the use of short-term and long-term incentives are powerful tools to benefit both customers and shareholders. The use of financial measures is a very effective way to reflect performance on a broad range of customer service measures. In particular, a program that focuses on the achievement of earnings per share ("EPS") is beneficial for customers and shareholders. Ex. 14, Halloran Rebuttal at 3-5.

EPS is a measure related to funds from operations ("FFO") and operating income. These are principal indices of performance for investor-owned entities like KCPL. Because KCPL is a regulated public utility, the organization is committed to its responsibility to achieve its EPS through the provision of efficient, clean, safe and affordable electricity. Therefore, EPS is an important measure of performance and productivity in areas related to product and service delivery. In addition, the Company's incentive plans are based upon individual performance factors relating to the specific employee's responsibilities and contribution to achieving divisional and overall performance objectives. Id. at 3.

Stronger financial performance through improvements in EPS provides additional cash, allowing the Company to invest in ongoing maintenance and upgrading of facilities, which ensures a steady, reliable, low cost supply of electricity to the customer. Contrary to the suggestion of Staff (Staff Br. at 24), EPS is vital to regulated utilities which are in a major construction program that is necessary to serve their customers. See Tr. 184. Staff witness Traxler conceded during cross-examination that public utilities must be able to attract capital if they are to continue to build new capacity such as Iatan 2, and that this capacity benefits customers. Tr. 183-84. Without sufficient retained earnings, it would be necessary for a public utility to finance its construction program using only outside sources of capital. See Tr. 184.

In addition, EPS is critical to public utilities such as KCPL which must expend funds for customer programs, such as the Vegetation Management Standards (4 CSR 240-23.030) which were recently adopted by the Commission. The costs of compliance with the Vegetation Management Standards rule are not being recovered in this case, and KCPL will need to retain earnings to fund its compliance efforts. See Ex. 40, Herdegan True-Up Direct at 2-3; Ex. 41, Rush True-Up Direct at 5. Another relevant example reflected in this case is the nearly $7 million of coal cost increases that are expected to occur in January 1, 2008, but which will not be recovered in rates in this proceeding. Ex. 41, Rush True-Up Direct at 5.

As Mr. Halloran testified, the use of incentive compensation to focus the management team on the achievement of EPS goals, as well as individual performance goals is a wise and appropriate investment in the business. KCPL believes that incentive compensation that is based on the financial goals tied to EPS is appropriate because a financially sound and stable company provides a direct benefit to all stakeholders, including employees, customers, shareholders and the community in which it operates. Ex. 14, Halloran Rebuttal at 3.

The record in this case is replete with evidence the KCPL has been providing "exemplary" service to its customers, and has been nationally recognized for its achievements in this regard. See Tr. 456, 468, 470-71, 502; Ex. 109, Hyneman Surrebuttal at 17; Ex. 101, Staff Cost of Service Report at 53-54. It is clear from the evidence that KCPL's overall record of providing safe, reliable and reasonably priced electric service to its customers is excellent. The Commission should recognize that proper incentives for KCPL's management team will promote the continuation of such important customer goals and achievements.

For these reasons, KCPL respectfully requests that the Commission reject the disallowances proposed by Staff and DOE related to short-term and long-term incentive compensation.

6. Talent Assessment Program Employee Severance Cost: Should the severance and other associated costs of KCPL employees terminated under KCPL's talent assessment program be included in cost-of-service for setting KCPL's rates?

In its Post-Hearing Brief, Staff is now taking the position that it "cannot support recovery through rates of expenses a utility incurs where there is no showing of any benefit to the utility's customers." See Staff Brief at 30. Unfortunately, Staff simply has chosen to ignore the competent and substantial evidence that KCPL's management is doing a good job of managing its workforce for the benefit of KCPL's customers. For example, Staff "did not rely on the J.D.

Powers & Associates customer survey" (Staff Brief at 32) which demonstrated KCPL has achieved Tier 1 status in overall residential customer satisfaction in comparison to other midwest utilities. Mr. Hyneman confirmed that KCPL's ranking among regional public utilities rose from 8th to 4th out of 16 public utilities surveyed by J.D. Powers and Associates from 2006 to 2007.[1] Ex. 109, Hyneman Surrebuttal, p. 17; Tr. 468. However, Staff quibbles with this clear evidence by suggesting that the "raw scores" of KCPL declined in the J.D. Power customer service surveys for these years. Staff witness Hyneman had not investigated whether the criteria for obtaining the raw scores had changed during this period. See Tr. 467. Instead, Staff has chosen to disregard the fact that KCPL's relative rankings among its peers have improved into the Top Quartile of midwestern public utilities.

In addition, Staff has apparently chosen to ignore the fact that KCPL was awarded the Edison Award ("Utility of the Year") in 2007 which is a prestigious industry commendation for public utilities that distinguish themselves in leadership, innovation and advancement of the industry (Tr. 435), particularly for commitments to operational excellence, reliability, and innovation in the generation and delivery of electricity to customers. See Tr. 470-71.

Staff witnesses Hyneman and Traxler both confirmed, however, that Staff has been monitoring KCPL's call center performance and its overall reliability indices, and Staff has not identified any long-term trends in this data that should cause concern for the Commission. See Tr. 456, 187. During his testimony at the hearings, Mr. Hyneman also conceded that KCPL has been "exemplary" and "performing well as a regulated utility." See Tr. 502. Yet, Staff has

[1] In 2007 a total of 29,042 telephone interviews were conducted by J.D. Powers measuring 48 satisfaction attributes within the following six components: Power Quality & Reliability; Company Image; Price & Value; Communications; Billing & Payment; and Customer Service. See Ex. 109, Hyneman Surrebuttal at 17. KCPL ranked 4th among the 16 public utilities surveyed in 2007.

mistakenly concluded that "there is no showing of any benefit to utility customers" from the Talent Assessment Program. The Commission should reject this conclusion.

Staff continues to use the fact that KCPL is already providing safe and adequate service, as a reason to deny recovery of the Talent Assessment Program costs. See Staff Brief at 31. As explained in KCPL's Post-Hearing Brief at 31, Staff's suggested approach is short-sighted, not in the interest of KCPL's customers, and should be rejected by the Commission. The Commission should not deny recovery of a management program that is intended to ensure that customer service is being provided at an "A" level instead of being satisfied with merely an average "C" grade of service.

Staff asserted that "any failure on the part of KCPL's management to fulfill its responsibility to hire and train its employees should not be borne by KCPL's customers." See Staff Brief at 31. KCPL agrees with Staff that management is responsible for hiring and training its employees, but it is incorrect to suggest, as Mr. Hyneman does, that the employees who were terminated under the Talent Assessment Program did not meet KCPL's performance expectations. Ex. 2, Cheatum Rebuttal at 5-6. The real issue was whether these employees would be able to meet KCPL's rising performance expectations in the future. Id. Such employees had the opportunity to demonstrate that they could and would meet future expectations or accept a voluntary separation and leave the Company. This program demonstrates that KCPL's management is taking full responsibility to manage its work force to continue to provide reliable energy at a reasonable cost. Id. at 6.

Finally, Staff points out that KCPL did not include the Talent Assessment Program costs when it calculated the earnings associated with its incentive compensation levels. See Staff Brief at 33. As KCPL explained in its Post-Hearing Brief at 24-28, the Company's treatment of this program in its incentive compensation plan has no bearing upon the legitimacy of this program to benefit the Company and its customers. Since the Talent Assessment Program was a one-time, non-recurring program, KCPL excluded its costs from its earnings calculation for purposes of its incentive compensation program. See Tr. 417.

KCPL believes that its Talent Assessment Program was a reasonable and prudent management tool for determining if its workforce had the skills, ability, and desire to assist the Company in reaching its strategic objectives in the future. KCPL's performance levels have improved and been recognized nationally. Nevertheless, the Company wants to continue to improve its service and reliability to its customers. The Talent Assessment Program is one fundamental management program that has provided tangible benefits to KCPL's customers. The Company respectfully requests that the costs of its Talent Assessment Program be included in cost-of-service in this proceeding.

a. If so, should the costs be recognized in cost-of-service using KCPL's proposed deferral and amortization to expense over five years?

Yes. Recognizing that the Talent Assessment Program is a special program designed to ensure that KCPL has skilled, productive, customer-focused employees in place for the future, the Company proposed that these costs be amortized over a five-year period to reflect the fact that there will be benefits that extend over several years, and that the program costs will not recur annually. KCPL respectfully renews its request that the Commission allow the recovery of the severance payments, out-placement services, and other payroll taxes related to the Talent Assessment Program, and amortize them over a 5-year period. Id. at 7.

7. Employee Severance Cost: Should the severance costs of KCPL employees terminated for reasons other than KCPL's talent assessment program be included in cost-of-service for setting KCPL's rates?

Staff argues that KCPL's severance payments are "made only to protect shareholders." See Staff Brief at 35. KCPL must respectfully disagree with this limited view of the purpose of severance payments. As explained by KCPL witness Cheatum, severance payments are a helpful and legitimate business tool to ensure that the Company has the human capital capable of delivering reliable service at reasonable prices. Such payments make the transition of employees to future employment smoother, and tend to promote employee morale for both the terminated employee and the remaining KCPL employees. These costs should be included in rates since they are necessary in order to hire and retain the employees to implement the Company's strategic goals and to continue to achieve Tier I level performance for cost, reliability and customer service. See Ex. 2, Cheatum Rebuttal, p. 11.

Staff suggests that severance payments made to decrease payroll would be of benefit to consumers, however. Staff Brief at 35; Tr. 506. The Staff's standard for including severance payments in rates is not appropriate for an expanding company such as KCPL that is in the midst of the $1.3 billion construction program contemplated by the Regulatory Plan. KCPL cannot be expected to "downsize" its future payroll costs under these circumstances, but should be permitted to utilize severance payments to better position the workforce for the expected tasks of the new undertakings envisioned in the Regulatory Plan. The Commission should not deny KCPL recovery of its severance payments merely because it is a growing company and not "downsizing" its payroll, as is apparently the standard being proposed by Staff.

a. If so, is it appropriate to include a three-year average of those costs?

KCPL is requesting that a three-year average of severance payment amounts be included in the revenue requirement as representative of its ongoing level of severance costs. These costs are a recurring, necessary cost of business that allows the Company to hire and retain employees to implement the Company's strategic goals and to achieve high levels of reliability and customer service. It is therefore appropriate that such severance payments be included in the Company's cost of service in this proceeding.

8. Cost-of-Removal Income Tax: Should the tax timing difference for cost-of-removal be reflected under normalization accounting or flow-through accounting for pre-1981 vintage property for purposes of determining income tax expense in KCPL's cost-of-service for this case?

This issue has been settled and is addressed in the Stipulation and Agreement filed on October 3, 2007 by Staff and KCPL.

9. Organization Membership Dues: What level of membership dues that KCPL paid to organizations should be included in cost-of-service for setting KCPL's rates?

This issue has been settled and is addressed in the Stipulation and Agreement filed on October 3, 2007 by Staff and KCPL.

10. Advertising Costs: What level of KCPL's advertising costs should be included in KCPL's cost-of-service for setting KCPL's rates?

As KCPL explained in its Post-Hearing Brief, the Company has accepted Staff's position on this issue, as set forth in the Surrebuttal Testimony of Staff witness Graham A. Vesely. No other party asserted a position concerning this issue. KCPL and Staff anticipate filing a Stipulation and Agreement for the Commission's consideration and approval that formally resolves this issue.

11. Washington Employee Costs: Should any level of costs associated with KCPL's Washington, D.C. employee who represents KCPL in federal matters be included in KCPL's cost-of-service for setting KCPL's rates?

This issue has been settled and is addressed in the Stipulation and Agreement filed on October 3, 2007 by Staff and KCPL.

12. KCPL Supplemental Executive Retirement Pension (SERP) costs: What level of SERP costs should be included in KCPL's cost-of-service for setting KCPL's rates?

This issue has been settled and is addressed in the Stipulation and Agreement filed on October 3, 2007 by Staff and KCPL.

13. Meal Expenses: What level of local meal expense should be included in KCPL's cost-of-service for setting KCPL's rates?

This issue has been settled and is addressed in the Stipulation and Agreement filed on October 3, 2007 by Staff and KCPL.

14. Off-System Sales Margin: Should KCPL's rates continue to be set at the 25th percentile of non-firm off-system sales margin as projected in this case for 2008 as proposed by KCPL and accepted by the Staff, or at the 40th percentile as proposed by Public Counsel?

a. KCPL's rates for non-firm off-system sales margin should continue to be set at the 25% Level as projected, not at the 40% level proposed by OPC.

KCPL and Staff agree that the Commission should continue to set rates for off-system sales ("OSS") margins at the 25% Level. See Ex. 39, Giles True-Up Direct at 1-2; Ex. 130, Traxler True-Up Direct at 9.

OPC is the only party contending that OSS rates should be set at the 40% Level. Its newest argument is that because sales in 2007 have declined, in part, because of forced outages, OSS rates should nevertheless be increased in an effort to "incent" KCPL to sell more power. See Ex. 211, Robertson Surrebuttal at 12. OPC makes this argument even though the risks associated with unit availability and outages were thoroughly discussed in both this case and the

2006 Rate Case. Such risks were an integral part of the probabilistic analysis conducted by KCPL witness Michael Schnitzer of the NorthBridge Group in both dockets.

As explained in the True-Up Rebuttal of KCPL's Burton Crawford, the major reason for reduced OSS margins in 2007 is not forced outages, but rather the drop in the price of electricity. See Ex. 38, Crawford True-Up Direct at 2. As noted in Mr. Crawford's highly confidential testimony, the projected price levels for 2007 were based on estimates made in 2006. The price of electricity in 2007, however, averaged over $10 per megawatt hour (MWh) less than in the prior year, mostly because of the drop in the price of natural gas. Id. at 2-3 and Sched. BLC-1; Tr. 1254-55.

The other reason for decreased sales in 2007 was lower MWh sales volumes. This was mainly caused by an increase in KCPL's native load and an increase in forced outages. See Ex. 38, Crawford True-Up Direct at 2-3. OPC's Ted Robertson argued that because the Commission's 2006 Report and Order mainly voiced concern over the risks of market volatility, the 25% Level should be raised to 40% to make KCPL responsible for any and all increases caused by unit unavailability and outages. See Ex. 211, Robertson True-Up Rebuttal at 3-5, 11-12. However, as Mr. Robertson conceded both in his written testimony and on the stand during the true-up hearing, the probabilistic analysis presented by KCPL witness Michael Schnitzer clearly advised the Commission that unit availability and forced outages must be taken into consideration as part of the risks that the Company faces in projecting its sales into the wholesale power markets. See id. at 5; Tr. 1271-72. Mr. Schnitzer advised the Commission of these facts, not only in his direct testimony in this case, but also in the 2006 Rate Case, of which administrative notice was taken. See Ex. 22, Schnitzer Direct at 7-8, 13. See also Ex. 30, Schnitzer Direct at 12-17, Case No. ER-2006-0314 (administrative notice taken at Tr. 1337).

Additionally, Mr. Robertson conceded that he had conducted no investigation of the forced outages that KCPL experienced in 2007, and that his word "abnormal" was, in fact, not based upon any study of what either "abnormal" or "normal" outage rates were at KCPL. See Tr. 1273-74. KCPL's Burton Crawford testified that, contrary to OPC's suggestion, the Company's available generating capacity during 2007 was consistent with national averages, based on data from the North American Electric Reliability Council. See Tr. 1264. Additionally, Mr. Crawford explained that KCPL's earlier inclusion of transactions related to Southwest Power Pool's Energy Imbalance Service market that went operational in 2007 was in error. As corrected, KCPL now anticipates an increase in OSS margins over what was projected earlier this year. See Ex. 38, Crawford True-Up Direct at 4-10. Compare Ex. 9, Giles Rebuttal at 12 with Ex. 39, Giles True-Up Direct at 2-3.

There is no evidence before the Commission that should cause it to set rates for off-system sales at any other level but the 25% Level. The arguments of OPC are not based on a proper or reasonable analysis of KCPL forced outage data. Mr. Robertson conceded that third parties are often responsible for the substantial costs of forced outages, admitting that KCPL has recovered over $20 million from third parties who bore responsibility for the 1999 Hawthorn 5 explosion. See Tr. 1273.

The Commission should continue to set OSS rates at the 25% Level, consistent with its decision in the 2006 Rate Case.

b. Interest should be calculated and flowed back to ratepayers on OSS margin that exceeds the 25% Level approved in the 2006 Rate Case.

Yes, as set forth in KCPL's Post-Hearing Brief at 34.

15. Department of Energy Nuclear Fuel Overcharge Refund: Should the Department of Energy Nuclear Fuel Overcharge Refunds for 1986 through 1993 that KCPL received during the test year in this case be included in KCPL's cost-of-service for setting KCPL's rates?

This issue is very similar to the Hawthorn 5 subrogation proceeds issue discussed above. Staff acknowledges this fact in its Post-Hearing Brief when it states: "For the same reasons presented in that part of this brief above addressing Issue No. 3 (Hawthorn 5 subrogation proceeds), the Commission should presume KCPL recovered from its customers in the rates KCPL charged from 1986 through 1993, the fuel enrichment overpayments KCPL made to the Department of Energy." See Staff Post-Hearing Brief at 38. KCPL agrees that the same logic dictates the outcome of both issues, but argues that such logic leads one to the conclusion that the refunds from the Department of Energy ("DOE"), like the Hawthorn 5 subrogation proceeds, are inappropriate for inclusion in KCPL's cost of service in this case. The same three flaws apply to Staff's position.

First, for their argument to prevail, the Commission would have to determine whether KCPL's earnings were reasonable from 1986-1993. To do so the Commission would have "to determine what a reasonable rate *would have been*" from 1986-1993 and set KCPL's prospective rates accordingly. UCCM, 585 S.W.2d 41, 58 (Mo. 1979)(emphasis in original). Such retroactive ratemaking is prohibited. It would be no more appropriate to include the DOE refund in the present case than it would be for KCPL to attempt to reach back to include the overcharges in rates had DOE not issued the refund. In either case, the inclusion would constitute retroactive ratemaking.

Second, assuming it would be appropriate to look to KCPL's earnings from 1986-1993, Staff relies on the circumstantial inference that because KCPL did not file a rate case during this timeframe, its earnings must have been reasonable. KCPL acknowledges that it did not file a rate case during the 1986-1993 timeframe, but notes that Staff did not file a complaint case alleging over-earning during that period either. Neither point speaks directly to the adequacy of KCPL's earnings. There is no evidence in the record to support Staff's position.

Third, including the DOE refund in KCPL's cost of service in this case ignores the fact that neither the refund, nor the costs it was intended to recover, have anything to do with the test year in this case. Moreover, the issue has nothing to do with KCPL's continuing operations. DOE overcharged KCPL for uranium enrichment services from 1986 until 1993. See Hyneman Surrebuttal Testimony, at 12; Tr. 655, lines 7-11. KCPL filed a lawsuit in 2004 against DOE to recover the amount KCPL was overcharged. The lawsuit ultimately settled and KCPL accrued $427,150 in 2006. Staff witness Charles Hyneman acknowledges that "the only tie to the test year in this case is that KCPL happened to receive the refund in 2006." Tr. 658, lines 17-19. Mr. Hyneman also concedes that if the matter had settled quickly and KCPL had received the DOE refund in 2004 when it filed the suit, he would not have proposed to include the refund in KCPL's rates in this case. Tr. 656, lines 9-13.

For the foregoing reasons, it would be inappropriate for the Commission to include in KCPL's cost of service in this case the refund it received from DOE for overcharges that occurred between 1986 and 1993.

a. If so, should the five-year amortization period proposed by Staff by adopted?

It is inappropriate to include the DOE refund in KCPL's cost of service in this case. As explained in KCPL's Post-Hearing Brief, doing so through an amortization does not change this result. Although amortizing the refund reduces the adverse impact on the Company, it does not address the fact that it is inappropriate to include the refund in KCPL's cost of service.

16. Research and Development Tax Credits: Should research and development tax credits related to amended income tax returns for years 2000 to 2004 be deferred and amortized in KCPL's cost-of-service for setting KCPL's rates if received in the future?

KCPL believes that this issue has been settled, subject to the Commission's approval of the October 3, 2007 Stipulation and Agreement filed by KCPL and Staff.

17. Bad Debt Expense: What bad debt expense factor should be applied to both adjusted and pro-forma revenues to determine the level of bad debt expense to be included in cost of service?

This issue has been settled and is addressed in the Stipulation and Agreement filed on October 3, 2007 by Staff and KCPL.

18. Wolf Creek Refueling Outage Costs: Should the Commission order KCPL to reflect Wolf Creek refueling outage costs under the defer-and-amortize method adopted by KCPL in 2006 in accordance with a new accounting pronouncement or order KCPL to maintain its accounting for regulatory purposes under the prior accrue-in advance method?

This issue has been settled and is addressed in the Stipulation and Agreement filed on October 3, 2007 by Staff and KCPL.

C. <u>Rate Base Issues</u>

19. Rate Case Expense: Should KCPL's rate case expense deferred for future amortization in accordance with the Commission's order in Case No. ER-2006-0314 be included in KCPL's rate base?

This issue has been settled and is addressed in the Stipulation and Agreement filed on October 3, 2007 by Staff and KCPL.

20. Surface Transportation Board Litigation Expenses: Should KCPL's Surface Transportation Board litigation expenses deferred for future amortization in accordance with the Commission's order in Case No. ER-2006-0314 be included in KCPL's rate base?

This issue has been settled and is addressed in the Stipulation and Agreement filed on October 3, 2007 by Staff and KCPL.

D. <u>Class Cost Of Service / Rate Design</u>

21. Effect of Case No. EO-2005-0329 Stipulation and Agreement on Inter-class Shifts: Does the Stipulation and Agreement incorporating the KCPL Experimental Regulatory Plan that the Commission approved in Case No. EO-2005-0329 allow the signatories to the Stipulation and Agreement to propose inter-class revenue shifts in this case?

KCPL has already discussed and rebutted most of the arguments presented on this issue in its Post-Hearing Brief at 44-49. However, a few additional comments are necessary to address some limited points raised by Staff and intervenors on the class cost of service/rate design issue.

First, Staff argues that if KCPL's interpretation of the 2005 Regulatory Plan Stipulation language is adopted, then "a simple rate increase by equal percentage would be prohibited, as customers might chose to switch from utility sourced electricity to customer-owned solar panels, customer-owned wind generation, chilled water or steam, or gas for all or some portion of their energy needs." See Staff Brief at 41. This is incorrect. KCPL believes that any change to the rates that will cause customers to re-evaluate the electric rates they have chosen represents a "rate structure" change. Ex. 20, Rush Rebuttal at 2. KCPL is not arguing that an across-the-board percentage increase would be a "rate structure" change since the relationships among the various customer classes and rate schedules within a customer class would be maintained. If an across-the-board percentage increase was adopted, there would be no need for electric customers to consider moving to another electric rate schedule since the rate relationships would be the same among the various customer classes and rate schedules.

Second, KCPL continues to be troubled by Staff's insistence on spreading on the record privileged settlement discussions. See Staff Brief at 40. The fact that Staff has filed this information as Highly Confidential does not mitigate the prejudicial impact of disclosure of this privileged information. The disclosure of such privileged material is intended to influence the Commission in its deliberations on the merits of the rate design issue. While filing the privileged information under seal protects the information from public disclosure, it does not mitigate the adverse impact of its disclosure to the decision-maker. The unilateral disclosure of such privileged information by the Staff, if accepted by the Commission, will have a chilling effect upon frank and candid exchanges of information, and will serve to compromise positions taken in the settlement process.

KCPL, therefore, renews its motion to strike the portion of Ms. Pyatte's Surrebuttal Testimony beginning at Page 10, Line 5 and continuing through Page 11, Line 12 since this testimony violates the prohibition contained in 4 CSR 240-2.090(7) against the unilateral disclosure of privileged settlement negotiations without the agreement of the other parties to the settlement discussions. In addition, the Commission should disregard the HC discussion in the Staff Brief related such settlement discussions. See Staff Brief at 40.

a. If so, should any inter-class revenue shifts be implemented in this case?

For the reasons stated in KCPL's Post-Hearing Brief at 37-49, KCPL continues to oppose such inter-class shifts in this case in this case. The Commission should maintain the *status quo* in this case, as contemplated by the Regulatory Plan Stipulation, and approve any increase in revenues on an equal percentage basis.

22. Large Power Service Rate Design: Does the Stipulation and Agreement incorporating the KCPL Experimental Regulatory Plan that the Commission approved in Case No. EO-2005-0329 allow the signatories to the Stipulation and Agreement to make rate design modifications within the Large Power Service Rate schedule?

KCPL has already adequately addressed the arguments of Staff, Praxair, Ford/MIEC, and DOE on this issue. See KCPL Post-Hearing Brief at 49-50.

a. If so, what are the appropriate demand and energy charges for the Large Power Service rate class?

KCPL opposes any changes in these charges, for the reasons noted in its Post-Hearing Brief at 49-50. Staff also agrees that no changes should be made to the relationship between the demand and energy charges for the Large Power Service (LPS) rate schedules. See Staff Brief at 44. In particular, Staff emphasized the customer impact of adopting the Praxair/Ford/MIEC proposal. Id. As Staff noted, 75 of KCPL's 89 LPS customers will experience increased bills, before any general rate increase is implemented. Tr. 739. Perhaps more importantly, 47 of KCPL's 89 LPS customers would benefit by taking service on a different rate schedule, but still would experience increased bills above the system average increase approved in this case. Tr. 741-42.

KCPL agrees with Staff regarding the customer impact concerns raised by the Praxair/Ford/MIEC proposal. The adoption of such a dramatic change in rates would certainly represent a "rate structure" change, from KCPL's perspective. Tr. 786. Mr. Rush also testified that the Praxair/Ford/MIEC proposal is excessive since it would reduce the tailblock rates for the LPS class to a level that is less the KCPL's parallel generation tariff. Tr. 787. KCPL's parallel generation tariff of 2.4 cents per KWh reflects KCPL's incremental cost of providing energy. See Ex. 20, Rush Rebuttal at 3. Therefore, no energy charges should be reduced below this rate level.

While KCPL is opposed to making any changes to the relationship between demand and energy charges for the LPS class in this case, Mr. Rush discussed during the hearings an alternative proposal acceptable to KCPL that would reduce the adverse consequences of the Praxair/Ford/MIEC proposal. While KCPL does not recommend this change, Mr. Rush suggested that the Commission could limit a reduction of the energy charges to no more than one-half of a cent for the first two energy blocks, with no decrease in the tailblock rate for the

LPS class. Most importantly, this alternative proposal would keep the LPS tailblock rate above KCPL's parallel generation tariff of 2.4 cents per KWh. Tr. 788. The reduction in energy charges under this proposal would need to be made up in increased demand charges for the LPS class.

23. General Service All-Electric Tariffs and General Service Separately-Metered Space-Heating Tariff Provisions:

a. Should KCPL's General Service All-Electric tariff rates and Separately-Metered Space Heating rates be increased more (*i.e.*, by a greater percentage) than KCPL's corresponding standard general application rates and, if so, by how much more?

No. The Company in the 2006 Rate Case did, in fact, increase the Space Heating rates by 5% above the system average increase. No further adjustments should be made until a cost of service study is completed. The Company believes that an across-the-board percentage increase to all customer classes, including the General Service All-Electric and Separately Metered Space Heating rates is appropriate. Until additional cost information is available, the Commission should change the rate relationships that currently exist among the various customer classes, including the General Service All-Electric and Separately-Metered Space Heating rates which have been approved for KCPL since the 1996 Rate Design proceeding, Case No. EO-94-199. As discussed below, both Trigen and Staff supported the Company's rate design at that time. The Commission should restrict their attempts to modify KCPL's rate structure in this proceeding, without any supporting evidence to justify the dramatic changes being proposed.

b. Should KCPL's General Service All-Electric tariffs and Separately-Metered Space Heating rates be phased-out and, if so, over what period?

No. The Company continues to oppose the recommendations of both Trigen and Staff to begin phasing-out the All-Electric tariffs and Separately-Metered Space Heating rates. Such dramatic changes in rate structure for these customers would clearly be inconsistent with the terms and conditions of the Regulatory Plan Stipulation where the Signatory Parties agreed: "Rate Design: The Signatory Parties agree not to file new or updated class COS studies or to propose changes to rate structures in Rate Filing #2." See Regulatory Plan Stipulation, Section III(B)(3)(b)(iv) at 35. Staff witness Janice Pyatte conceded that the elimination of a rate schedule would be a "rate structure" change. (Tr. 1030) Clearly, a phase-out of the All-Electric and Separately-Metered Space Heating schedules would also represent such a prohibited "rate structure" change. Ex. 21, Rush Surrebuttal at 8.

KCPL participated in an extensive class cost of service study and rate design case in 1996. At that time, rates were established based on that study, and rate design changes were made that changed the overall price structure. Trigen also "agree[d] to support and endorse before the Commission the Stipulation and Agreement filed by the signatory parties on May 29, 1996" which implemented the current rate structure. See Ex. 20, Rush Rebuttal at 10. As a signatory party to the Stipulation And Agreement in Case No. EO-94-199, Staff also supported the current rate structures.

The Commission should maintain the Company long-standing rate structure in this proceeding. If the Commission desires to modify the KCPL rate structure, however, it should only be done after a comprehensive review of all rates, and not just the General Service All-Electric and Space-heating rates.

For these reasons, Trigen's position on this issue should again be rejected by the Commission.

c. Should the availability of KCPL's general service all-electric tariffs and separately-metered space heating rates be restricted to those qualifying customers commercial and industrial physical locations being served under such all-electric tariffs or separately-metered space heating rates as of the date used for the billing determinants used in this case (or as an alternative, the operation of law date of this case) and should such rates only be available

to such customers for so long as they continuously remain on that rate schedule (*i.e.*, the all-electric or separately-metered space heating rate schedule they are on as of such date)?

No. Trigen recommends that the Commission restrict the availability of these tariffs to existing customers of KCPL who qualify for the rate at a location other than the physical location at the time of the true-up. This issue was addressed in the 2006 Rate Case, and the Commission ruled against Trigen. Although Trigen is appealing the Commission's decision on this issue, it has not yet been ruled on by the Cole County Circuit Court. KCPL disagrees with Trigen's position and believes that this issue should be addressed in the context of an overall study.

d.

(i) Should the Commission require KCPL, as soon as possible but not later than its next rate case, to present complete cost of service and/or cost-effectiveness studies and analyses of KCPL's general service all-electric tariffs and separately-metered space heating rates and, consistent with the findings of such studies and analyses, allow KCPL the opportunity at that time to present its preferred phase-out plan for the remaining commercial and industrial customers served under the all-electric tariffs and separately-metered space heating rates?

No. As discussed in KCPL's Post Hearing Brief at 53-54, this issue is clearly addressed by the Regulatory Plan Stipulation approved by the Commission. KCPL, Staff, OPC, and all the other signatory parties to the case have already agreed:

> "The Signatory Parties agree not to file new or updated class cost of service studies or to propose changes to rate structures in Rate Filing #3." See Stipulation, Section III(B)(3)(c)(iv) at 39.

In the 2006 Rate Case, the Commission ruled in favor of KCPL on this issue. The Company continues to support the Commission's decision, and believes that the time to conduct the cost studies is at the conclusion of the last rate case anticipated by the Regulatory Plan, when Iatan 2 comes on-line. KCPL believes any cost studies concerning the All-Electric tariff and the

Separately-Metered Space Heating rates should be part of a larger comprehensive rate design study. Ex. 20, Rush Rebuttal at 12.

Staff "supports providing KCPL an opportunity to present a complete cost-of-service study and/or cost-effectiveness study and analysis in its next rate case to justify any rate discounts for space heating and, if not justified, to allow KCPL the opportunity to present its preferred phase-out plan." See Staff Brief at 47. While KCPL believes that it is restricted by the agreements made in the Regulatory Plan Stipulation not to file any new or updated cost of service studies in the 2008 Rate Case, as explained above, if ordered to do so by the Commission, KCPL will present a cost-of-service study and/or cost analysis that will clearly justify its existing rate structure related to the General Service All-Electric and Space-Heating rates in the next rate case. KCPL strongly believes that this approach (i.e., reviewing additional cost of service results in the next rate case) is preferable to the proposals of Trigen and Staff in this case to increase these rates more than the system-wide average rates, or otherwise begin a phase-out of these Commission-approved rate structures related to these General Service customers' rates without sufficient cost study support.

The Company continues to support the Commission's decision in the last rate case, however, and believes that the time to conduct the cost studies is at the conclusion of the last rate case anticipated by the Regulatory Plan when Iatan 2 comes on-line. KCPL believes that any cost studies concerning the All-Electric tariff and the Separately-Metered Space Heating rates should be part of a larger comprehensive rate design study. See Ex. 20, Rush Rebuttal at 12.

(ii) In the event that KCPL does not file such cost of service and/or cost-effectiveness studies before or as part of its next rate case, should the Commission require KCPL to impute the revenues associated with the discounted rates in the all-electric general service tariffs and separately-metered space heating provisions of its tariffs and impute

revenues equal to KCPL's cost of administering these discounted rates as part of its next rate case?

As explained in KCPL's Post-Hearing Brief at 54, it would be improper and unlawful for the Commission to require the Company to impute a higher rate for these services than the rate lawfully approved by the Commission. <u>See also</u> Ex. 20, Rush Rebuttal at 12.

e. Should the Commission require KCPL to (a) investigate and determine whether the commercial and industrial customers currently served under the general service all-electric tariffs and the separately-metered space heating provisions of the standard General Service tariffs continue to meet the eligibility requirements for those discounted rates; (b) remove from the discounted rates those customers which KCPL's investigation determines are no longer eligible for such discounted rates; and (c) monitor and police the eligibility requirements of those customers receiving such discounted rates for reporting in KCPL's direct testimony in its next rate case filing?

No. Such "eligibility investigations" are currently addressed through the internal processes at the Company for placing customers on the appropriate rates. KCPL believes that it has the appropriate procedures and safeguards for correctly placing customers on the appropriate rates. No such further study is warranted. <u>See</u> Ex. 20, Rush Rebuttal at 12-13.

f. Should the Commission approve KCPL's proposal to rename its General Service "All-Electric" tariffs as "Space Heating" tariffs?

Yes. KCPL believes that it would be appropriate to rename its General Service "All-Electric" tariffs, to be known as "Space Heating" Tariffs.

E. <u>KCPL Experimental Regulatory Plan Additional Amortizations</u>

24. What, if any, Additional Amortizations are required by KCPL's Experimental Regulatory Plan approved by the Commission in Case NO. EO-2005-0329?

KCPL has calculated the Additional Amortizations that will be necessary pursuant to the 2005 Regulatory Plan Stipulation to permit the Company to achieve the necessary cash flows so that its investment grade credit rating is not jeopardized. KCPL's Michael Cline prepared these calculations in accord with the Stipulation and its Appendices E and F. See Ex. 36, Cline True-Up Direct at 3-4. The amount of the Additional Amortizations that KCPL requests is $14,155,968, and reflects calculations that account for KCPL's short-term debt. Id., Sched. MWC-9; Tr. 1178-80

While Staff has arrived at a different figure because of the positions it has taken on other issues, such as return on equity, Staff is aligned with KCPL on how the Additional Amortizations are to be calculated. Staff agrees that short-term debt and its expense should be reflected in the calculation. See Tr. 1196. Staff witness Steve Traxler agreed that the line in the calculation that represents short-term interest expense is found at Line 27b of both the Company's and the Staff's Additional Amortizations worksheet. See Tr. 1211-12 (Traxler); Ex. 214 (Staff's Worksheet with Line 27b) [authenticated by Mr. Traxler at Tr. 1211-12 and marked at Tr. 1216]; Ex. 36, Sched. MWC-9 to Cline True-Up Direct (KCPL Worksheet with Line 27b).

As Mr. Cline testified, short-term debt expense was erroneously omitted from previous calculations, in part, because the figure was not viewed as material. Tr. 1178-80. However, given the financial turmoil of recent months and KCPL's inability to fulfill its plan to issue a large amount of hybrid debt because of unfavorable market conditions, the amount of short-term debt -- $259 million -- was material and its costs were properly included in the Additional Amortizations calculation. Tr. 1179-80, 1193.[2]

Such calculations are entirely in accord with the 2005 Stipulation which explicitly embraced the use of Standard & Poor's credit ratios. The "Funds from Operations Interest Coverage" and others ratios set forth on page 20 of the 2005 Stipulation are taken directly from

[2] The exact amount of the short-term debt is $258,647,000, found on Line 37 of both KCPL's calculation in Cline Schedule MWC-9 and Staff's calculation in Ex. 214.

S&P's financial metrics definitions. See Schedule MWC-2 to Mr. Cline's Direct Testimony (Ex. 3). The numerator in the "FFO Interest Coverage" ratio is specifically defined as:

> Funds from operations (less the amortized portion of securitized debt and contributions to nuclear decommissioning trust funds, where applicable), plus cash interest paid (less the interest portions of nonrecourse debt and securitized debt, where applicable), capitalized interest and the debt portion of AFUDC, the dividends paid on hybrid preferred securities, and the interest computed for the off-balance-sheet debt items. [Page 2 of Sched. MWC-2, Cline Direct (Ex. 3). (emphasis added).]

Plainly, the cost of both short-term and long-term debt was to be included.

No party objects to this calculation except OPC. In an erroneous and hyper-technical interpretation of the 2005 Stipulation and its Appendices E and F, OPC's Russell Trippensee contends that the cash flow metrics were specifically designed to exclude short-term debt because it is not traditionally included in a utility's capital structure. See Ex. 212, Trippensee True-Up Rebuttal at 2-5. He additionally argues that because short-term debt is typically used to fund construction projects, it must be excluded from the Stipulation's analysis related to KCPL's funds derived from its operations and the cash flow analysis required by Appendices E and F. Id. at 5-7.

However, Mr. Trippensee misses the point. As explained below, the Additional Amortizations calculation is driven by cash-flow metrics as derived from KCPL's Missouri operations, not regulatory issues of what is or isn't included in rate base.

Mr. Trippensee acknowledged on cross-examination that there while there is no specific language in the 2005 Regulatory Plan Stipulation that prohibited the use of short-term debt in calculating the cash flow metrics, he argued that the phrase "Missouri jurisdictional revenue requirement" overruled all other considerations. Tr. 1226-27. He conceded that short-term debt is recognized on Lines 44-45 of Appendix F-3, which are incorporated in calculations of "adjusted interest expense" in Line 63 and in other lines that are used in the ratio calculations. See Tr. 1232; Ex. 44 at 4 (Attachment 1 to Appendix F). But, he chose to ignore the provision in the 2005 Stipulation that states: "The Signatory Parties agree to adopt an amortization level necessary to meet the Missouri jurisdictional portion of these financial ratios." See Ex. 43 at 20. He agreed that the Stipulation specifically excluded certain elements from cash flow measurements leading to Additional Amortizations, and that none of them required the exclusion of short-term debt or its costs. See Tr. 1229-30; Ex. 43 (pages 21-22 of 2005 Stipulation). Negative cash flow impacts related to special contracts are also excluded. See Ex. 43 at 21.

Mr. Trippensee's theory is that because the phrase "Missouri jurisdictional revenue requirement" is used on page 19 of the 2005 Stipulation, the cash flow analysis required by the Stipulation must exclude short-term debt. However, it is clear from reading the entire section relating to Additional Amortizations that the calculations were to be performed upon KCPL's projected cash flows resulting from its Missouri operations. In this regard, the Stipulation states:

> The Signatory Parties agree to support an additional amortization added to KCPL's cost of service in a rate case when the projected cash flows resulting from KCPL's Missouri jurisdictional operations, as determined by the Commission, fail to meet or exceed the Missouri jurisdictional portion of the lower end of the top third of the BBB range shown in Appendix E, for the Funds from Operations Interest Coverage Ratio and the Funds from Operations as a Percentage of Average Total Debt Ratio. [Ex. 43 at 20.]

The sentence following this provision emphatically states: "The Signatory Parties agree to adopt an amortization level necessary to meet the Missouri jurisdictional portion of these financial ratios." Ex. 43 at 20. Moreover, "KCPL also recognizes and agrees that its Missouri operations are only responsible for and will only provide cash flows for its Missouri operating share of the necessary cash flows as set out in this Paragraph III.B.1.i [the Additional Amortizations section of the 2005 Regulatory Plan Stipulation]. See Ex. 43 at 21.

A reading of the entire agreement makes clear, as Staff has stated, that cash flows are to be calculated based on the Missouri portion of KCPL's total company operations. All that phrase means is the Missouri percentage of KCPL's operations -- 52.7% -- which is noted at the top of both the Company and Staff calculations. See Sched. MWC-9; Ex. 214.

In defining the "funds from operations interest coverage," Appendix E includes gross interest expense, with no exclusion of short-term debt. See Ex. 44 at 1. The explanation of how the calculation is to work in Appendix F contains no mention of short-term debt being excluded from the calculation. See Ex. 44 (Appendices E and F). Clearly, interest expense relating to both short-term and long-term debt is permitted to be used in that calculation.

Mr. Cline conceded that the in the past KCPL had not taken into consideration short-term debt expense, in part, because it was not material. However, as he explained during the true-up hearing, given the volatility in the financial markets over the past few months, caused by the sub-prime mortgage crisis, short-term debt of $259 million is now a material element of KCPL's financial condition. See Tr. 1179-80, 1193. Therefore, it is essential that short-term debt be included in the calculation, both in this case and in future proceedings.

Finally, it is clear that as the Additional Amortizations calculations are performed, the parties will need to make adjustments from time to time. In this regard, it is significant that Attachment 1 to Appendix F -- the calculation worksheet -- is simply described on pages Appendix F-1 and F-2 as an "illustration" of the "method used to determine the adjustment to amortization amounts required for KCPL to meet investment grade credit guidelines." See Ex. 44.

Indeed, the "illustration" has already undergone modification as a result of issues noted by the parties. When OPC's Mr. Gorman pointed out in direct testimony that KCPL had failed to follow the methodology employed by Standard & Poor's to determine Funds from Operations by erroneously excluding amortization expense related to off-balance sheet debt equivalent for operating leases, KCPL's Michael Cline accepted the argument and "amended" (Mr. Gorman's word) the calculation. See Ex. 203, Gorman Surrebuttal at 7. Notably, this adjustment led to an increase in KCPL cash flows and a reduction in the amount of Additional Amortizations requested by the Company. See Ex. 201, Gorman Direct at 30-31; Ex. 202, Gorman Rebuttal at 17-21; Ex. 203, Gorman Surrebuttal at 7; Ex. 4; Cline Rebuttal at 4. Mr. Trippensee acknowledged this was the case. See Tr. 1236-37.

The Additional Amortizations calculation must be used as it was intended to be used, and that was as a means by which to achieve threshold metrics for KCPL's projected cash flows from its Missouri operations. Interest on KCPL's short-term debt, allocated appropriately to KCPL's Missouri operations, clearly meets this definition and is, therefore, necessary, relevant and appropriate to include. As Mr. Trippensee remarked: "Cash flows are not irrelevant." See Tr. 1229. However, accepting his view of how the cash-flow metrics work to calculate Additional Amortizations would make a critical element of the 2005 Stipulation both irrelevant and ineffective.

An erroneous or hyper-technical interpretation of this mechanism could lead to financial harm and will defeat the very purpose for which the Additional Amortizations concept was proposed and accepted by this Commission in the 2006 Rate Case. OPC's proposal, opposed by both the Company and Staff, must be rejected.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I do hereby certify that a true and correct copy of the foregoing document has been hand delivered, emailed or mailed, postage prepaid, this 16th day of November, 2007, to all counsel of record.

/s/ Karl Zobrist
Karl Zobrist