EXHIBIT

Exhibit No.:
Issue(s): Management Expense Reports/ Policy Changes/ Customer Service/ Expense Trackers in Rate Base/ Transmission Revenues/ KCPL's Supplemental Executive Retirement Plan ("SERP")
Witness/Type of Exhibit: Hyneman/Rebuttal
Sponsoring Party: Public Counsel
Case No.: ER-2016-0285

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REBUTTAL TESTIMONY

OF

CHARLES R. HYNEMAN

Submitted on Behalf of the Office of the Public Counsel

KANSAS CITY POWER & LIGHT COMPANY

CASE NO. ER-2016-0285

December 30, 2016

OPC Exhibit No. 303
Date 2.7.17 Reporter MB
File No. ER-2016-0285

BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

In the Matter of Kansas City Power & Light Company's Request for Authority to Implement A General Rate Increase for Electric Service	))))	Case No. ER-2016-0285

AFFIDAVIT OF CHARLES R. HYNEMAN

STATE OF MISSOURI)
) ss
COUNTY OF COLE)

Charles R. Hyneman, of lawful age and being first duly sworn, deposes and states:

1. My name is Charles R. Hyneman. I am the Chief Public Utility Accountant for the Office of the Public Counsel.

2. Attached hereto and made a part hereof for all purposes is my rebuttal testimony.

3. I hereby swear and affirm that my statements contained in the attached testimony are true and correct to the best of my knowledge and belief.

CRH

Charles R. Hyneman, C.P.A.
Chief Public Utility Accountant

Subscribed and sworn to me this 30th day of December 2016.

NOTARY PUBLIC NOTARY SEAL STATE OF MISSOURI
JERENE A. BUCKMAN
My Commission Expires
August 23, 2017
Cole County
Commission #13754037

Jerene A. Buckman

Jerene A. Buckman
Notary Public

My Commission expires August 23, 2017.

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REBUTTAL TESTIMONY

OF

CHARLES R. HYNEMAN

KANSAS CITY POWER & LIGHT COMPANY

FILENO. ER-2016-0285

INTRODUCTION

Q. Please state your name and business address.

A. Charles R. Hyneman, PO Box 2230, Jefferson City, Missouri 65102.

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

A. I am employed by the Missouri Office of the Public Counsel ("OPC") as the Chief Public Utility Accountant.

Q. Are you the same Charles R. Hyneman who filed direct testimony in this case?

A. Yes, I am

Q. What is the purpose of your rebuttal testimony?

A. The purpose of this testimony is to address some of the statements made and positions taken in direct testimonies of the following Kansas City Power & Light Company ("KCPL") and Commission Staff ("Staff") rate case witnesses:

1	Darrin Ives (KCPL)
2	Scott Heidtbink (KCPL)
3	Charles Caisley
4	Ron Klote (KCPL)
5	Tim Rush (KCPL)
6	Robert Hevert
7	Keith Majors (Staff)

Q. Should the fact that you do not address a particular issue in this rebuttal testimony be interpreted as approval or agreement with any other comments made or

positions taken by KCPL, Staff or any other party in their respective direct testimony filings?

A. No, it should not.

Q. Please summarize your rebuttal of Mr. Ives' direct testimony.

A. Mr. Ives identified the following five cost driver issues in this case:

1. Increased depreciation, property taxes and capital costs for plant placed in service from June 1, 2015 (end of true-up period in KCPL's 2014 rate case, ER-2014-0370) to December 31, 2016, the end of the true-up period in this rate case;
2. Rising Transmission Expenses - KCPL seeks to include transmission expenses in a FAC. In lieu of a FAC, KCPL seeks forecasted Transmission expenses.
3. Increases in property tax expense – KCPL seeks projected 2017 and 2018 property tax expense included in its cost of service in this case with a one-way tracker to track any potential over-recovery.
4. Declining customer usage;
5. Requested changes in its fuel adjustment clause ("FAC")

In my rebuttal testimony, I address Mr. Ives' 2nd issue, transmission expense, and his 3rd issue, property tax expense. OPC witness Lena Mantle will address issue No. 5, KCPL's requested changes to its FAC.

Mr. Ives also includes a discussion of his views of regulatory lag. I will provide additional information and viewpoints on regulatory lag. Finally, Mr. Ives presents a misleading and inaccurate picture of Missouri's regulatory environment. In this testimony I correct his direct testimony on this issue.

<u>REGULATORY ENVIRONMENT</u>

Q. Starting with your last point, how does Mr. Ives provide a misleading characterization of Missouri's regulatory environment?

A. Mr. Ives makes the following assertions of the regulatory ratemaking environment in Missouri:

1. Page 17 lines 1-5. Here Mr. Ives asserts KCPL has underperformed financially and places the blame for the company financial performance on the Commission, instead of itself. He asserts that KCPL's less than satisfactory earnings is caused by the Commission failing to keep up with the changing environment for electric utilities. Mr. Ives specifically criticizes the Commission's use of a "historical test year regulatory model".

2. Page 17 lines 20-22 to Page 18 lines 1-2. Mr. Ives tells the Commission it should recognize what he thinks is a "disconnect" between changing conditions and the Commission's ratemaking policies and procedures. He states the Commission must adopt KCPL's proposal of forecasted expenses, (a proposal that is not consistent with any Commission regulatory policies and procedures) if KCPL is to have a reasonable opportunity to earn its authorized return.

3. Page 19 line 5. Mr. Ives refers to the direct testimony of Mr. Robert Hevert. Mr. Hevert is a utility consultant who often supports cost of equity proposals for regulated utility companies in rate case proceedings and is a KCPL witness in this rate case. Mr. Hebert addresses in his testimony in this case a 2014 document from a rating agency that ranks the regulatory climate and regulatory commissions in the U.S. Mr. Ives also references this outdated evaluation and mischaracterizes the results of this evaluation.

Q. What evidence did Mr. Ives provide in his direct testimony to support these three assertions about Missouri's regulatory climate?

A. I can see no substantive evidence at all to support his conclusions. The only evidence he provides is a chart that shows that KCPL has performed poorly over the past few years. Instinctively, one would look at the skill of utility management first when assessing the cause of poor financial performance. Once poor management performance is ruled out, other factors can then be considered. Mr. Ives skips the review and consideration of poor KCPL management as a potential reason for KCPL's poor performance.

The evidence I present below shows it is very likely that it is KCPL management that is wholly or substantially responsible for its poor financial performance. Missouri electric utilities with the exception of KCPL seem to be performing well in the Missouri regulatory environment. All these utilities operate in the same regulatory environment but it is only KCPL that consistently underperforms. I think the answer and solution to KCPL's woes lie with KCPL management, not with the Commission and its regulatory practices.

Q. Describe the 2014 rating agency evaluation referenced by Mr. Ives?

A. In Standard & Poor's ("S&P") January 2014 "Utility Regulatory Assessments For U.S. Investor Owned Utilities Report" ("S&P 2014 Report"), S&P ranked the Missouri regulatory environment as "Strong/Adequate." From a utility bondholder perspective S&P ranked the Missouri regulatory environment at its second highest possible rating. S&P's rating categories include:

1. Strong
2. Strong/Adequate
3. Adequate
4. Adequate/Weak
5. Weak

Q. Does Mr. Ives try to portray S&P's ranking of Missouri's regulatory climate of "Strong/Adequate" as a negative rating and attempt use this to explain KCPL's poor financial performance?

A. Yes, he does. S&P gave Missouri's regulatory environment and the Commission its second highest rating. This rating shows that the Commission and its practices are more than fair and responsive to utility investors. The report cited by Mr. Ives provides additional evidence, as will be explained later, that the Commission and its regulatory policies are not the cause of KCPL's financial woes.

Q. Even though the 2014 S&P Report does show the Commission to be supportive of utility investors, do you consider this report to be outdated and stale?

A. Yes, but that does not indicate Missouri's regulatory environment has deteriorated since the report was issued in 2014. The industry standard source for statistics in rate cases and regulatory matters in general is the Regulatory Research Associates ("RRA"). Utilities including KCPL consistently cite to the RRA in testimony and portray the RRA as a source that is accurate and reliable. KCPL witness Mr. Hevert, in his direct testimony, often cites RRA as an authoritative source. The RRA, however, portrays a different picture of the Missouri regulatory environment from the picture painted by Mr. Ives in his direct testimony.

RRA maintains three principal rating categories, Above Average, Average, and Below Average. Above Average indicates a relatively more constructive, lower-risk regulatory environment from an investor viewpoint, and Below Average indicates a less-constructive, higher-risk regulatory climate from an investor viewpoint. Within the three principal rating categories, the numbers 1, 2, and 3 indicate relative position with the number 1 indicating least risk.

The following table shows that RRA ranks the Missouri Commission and the regulatory environment in Missouri right in the middle of all the state commissions. Of the 53 commissions ranked by RRA in its July 21, 2016 ranking, 18 commissions or 34%, are ranked more shareholder-friendly than the Missouri Commission and 20 commissions or 38% are rated as more ratepayer friendly than the Missouri Commission.

RRA rates the Missouri Commission as Average/2 which is the rating assigned to the largest group of state regulatory commissions in the Unites States. RRA affirmed its ranking of the Missouri Commission and the Missouri regulatory climate as recently as October 16, 2016.

RRA Rankings from Shareholder Perspective July 21, 2016	No. of State Commissions Ranked by RRA
Above Average / 2	3
Above Average / 3	5
Average / 1	10
Average / 2 (Missouri PSC)	15
Average / 3	12
Below Average / 1	6
Below Average / 2	2
Total	53

Q. Has Regulatory Research Associates recently performed a specific evaluation of the Missouri PSC and Missouri's regulatory climate?

A. Yes. Regulatory Research Associates published its findings in a report entitled *Missouri Regulatory Review-October 6, 2016*. In this document, RRA directly contradicts Mr. Ives' opinion of the Missouri Commission and Missouri's regulatory environment. The report finds that from an investor perspective and from a historical perspective, Missouri regulation has been relatively balanced. By its re-affirming the Missouri Commission's rating, RRA finds that the Missouri Commission continues to be balanced from an investor perspective.

The following is from the page 1 evaluation o the Missouri Commission:

> <u>Historically, Missouri regulation has been relatively balanced from an investor perspective.</u> ROEs adopted by the PSC over the past year or so were slightly below prevailing industry averages at the time established. All of the large electric utilities have fuel adjustment clauses, or FACs, in place that allocate a portion of fuel and purchased power-related cost variations to shareholders. However, in three electric rate proceedings decided in 2015, and one case decided in 2016, the PSC prohibited the companies from prospectively recovering a portion of their transmission costs through their FACs.
>
> In the gas arena, the state's local gas distribution companies are permitted to adjust rates to reflect changes in gas commodity costs on a timely basis, and the commission has approved the use of surcharges for recovery of infrastructure improvement costs between base rate cases.

> RRA recently affirmed its Average/2 ranking of the jurisdiction, but noted that it is mindful of the fact that the 2016 legislative session concluded without action being taken on a bill that would have altered the state's ratemaking framework to address concerns regarding "regulatory lag." The issue is of particular concern to Missouri's electric utilities, and the matter is now being considered both by an interim legislative committee and the PSC in a working docket.
>
> Although the utilities are generally supportive of potential changes to the regulatory paradigm, recent comments from the public counsel were dismissive of regulatory lag concerns. Separately, the staff has suggested that the commission should exercise authority over Great Plains Energy's proposed acquisition of Westar Energy, despite the companies' public assurances that PSC approval is not required for the transaction to be consummated. Should the legislature or PSC fail to take action to address regulatory lag concerns, or if the Great Plains/Westar deal ultimately comes before the PSC in a contentious proceeding, a reduction in RRA's ranking may be justified. (Section updated 10/6/16) (emphasis added).

Q. Mr. Ives states that the current regulatory model in Missouri has not kept pace with the changing operating environment faced by KCPL. Do you agree?

A. Based on the evidence I provide below, I do not. Other Missouri electric utilities face the same operating environment as KCPL. These electric utilities are performing well in the same operating environment where KCPL is underperforming. Instead of the Missouri Commission and Missouri regulatory environment being the cause of KCPL's not meeting its earnings expectation, KCPL should look at the possibility that its current management has not kept pace with the change in business conditions and how to perform well in those conditions.

Q. How did you test the assertions made by Mr. Ives?

A. As described above, the first test was to determine if there was more recent published evidence giving an objective view of the Missouri Commission and Missouri's regulatory environment. I found that there was and described the RRA analysis above. While the RRA rankings themselves are from a shareholder perspective, they provide much more current and more accurate evidence of the Missouri regulatory environment than the 2014 stale document cited by Mr. Ives.

The second test of Mr. Ives' assertions is to determine how other electric utility companies operating in the current Missouri regulatory environment have fared under the Commission's regulatory model over the past few years. I find that other Missouri electric utilities have performed well under the Commission's ratemaking and regulatory policies and procedures.

Q. Describe how KCPL's sister utility, KCPL Greater Missouri Operations ("GMO") has fared over the past few years under this Commission's policies and procedures.

A. GMO has apparently fared very well over the past several years and it appears the Commission's regulatory model has kept pace with the environment faced by GMO.

Since the acquisition of GMO in 2008, KCPL and GMO have traditionally filed simultaneous rate cases. KCPL and GMO both filed rate cases as recently as 2012. In 2014, however, GMO did not join KCPL in filing a rate case. Logically, if GMO was not earning at or above its authorized rate of return in 2014 it would have filed with KCPL to increase its rates.

GMO did file a rate case in 2016 as File No. ER-2016-0156 ("2016 rate case"). However, GMO represented that it filed this rate case because it was required to file a rate case in order to maintain its FAC. After completing a thorough rate case audit of GMO's revenue requirement, the Commission's Staff found that GMO was earning in excess of a reasonable return on equity in an amount of $31.3 million. The Staff calculated this amount as its midpoint rate of return (Staff Accounting Schedules Exhibit 1, Schedule1 page 1, sponsored by Staff witness Cary Featherstone in Case No. ER-2016-0156).

Although GMO sought a rate increase of $59.3 million in its 2016 rate case, the case was settled for an increase of $3 million. These facts provide strong evidence that GMO has been earning at or above its authorized rate of return since at least 2014, when it chose not to file for a rate increase with KCPL.

Q. What do the facts you cited about GMO indicate?

A. These facts provide evidence that it just may be the skill in how KCPL manages its utility operations, rather than the Commission's regulatory model, that is to blame for KCPL's failure to earn its authorized rate of return.

Q. Is there additional evidence that the Commission's regulatory model has kept pace with the requirements of regulated utilities?

A. Yes. The Empire District Electric Company ("Empire") is being acquired by a large non-Missouri utility company. If the Commission's regularly model was as bad as Mr. Ives portrays, it is highly doubtful that a large and sophisticated utility company would invest in such a business venture. The regulatory environment in which Empire operates was certainly a focus of any due diligence of an acquiring utility. It appears the Missouri Commission and the Missouri regulatory environment passed this test.

Q. Finally, is there additional evidence that the Missouri regulatory model is working well and that Mr. Ives' testimony to the contrary is inaccurate?

A. Yes. Union Electric Company d/b/a/ Ameren Missouri ("Ameren Missouri") is Missouri's largest electric utility. Ameren Missouri, like KCPL, reports its own financial results in its annual report to the Securities and Exchange Commission ("SEC").

I calculated the following actual earned returns on equity ("ROE") from Ameren Missouri's and KCPL's Form 10-K SEC Annual Reports. The ratio I used to calculate the actual earned ROEs was net income as the numerator divided by average common equity as the denominator. While other measures may be used for the denominator and may be preferable, these ROE calculations were calculated using average equity (beginning balance + ending balance divided by two).

Year	Amern MO ROE	KCPL ROE
2004	12.4%	14.8%
2005	11.7%	12.3%
2006	11.1%	11.4%
2007	9.9%	10.9%
2008	6.8%	8.1%
2009	6.8%	7.3%
2010	8.9%	8.3%
2011	7.0%	6.7%
2012	10.3%	6.8%
2013	9.8%	7.9%
2014	9.9%	7.3%
2015	8.7%	6.5%

Q. **What is most significant from this chart?**

A. This chart reflects two vertically-integrated utilities operating during the same time period. Ameren Missouri operates 100 percent under the Missouri regulatory model and its average four-year ROE is 9.7%. KCPL operates roughly equally under both a Kansas and a Missouri regulatory model. KCPL's actual earned ROE over the past four years is 7.1%.

	Amern MO ROE	KCPL ROE
Avg 2012-2015	9.7%	7.1%

Q. **Are both KCPL and Ameren Missouri subject to the exact same ratemaking and regulatory policies and procedures of the Missouri Commission?**

A. Yes, they are. KCPL, as noted above, does also operate in the Kansas regulatory jurisdiction.

Q. Based on your review of how well other Missouri electric utilities are performing, what conclusions do you reach as it relates to KCPL's performance?

A. My conclusion is that any difficulties in reaching its authorized rate of return are likely due to the fault of KCPL management. It is likely KCPL's failure to skillfully and prudently operate the utility that is the cause of its performance and not the policies of the Missouri Public Service Commission.

<u>KCPL'S TRANSMISSION EXPENSES</u>

Q. In his direct testimony KCPL witness John R. Carlson provides an overview of the different types of KCPL's transmission expenses. Do you agree in general with his descriptions?

A. Yes, I do. Mr. Carlson testifies in his direct testimony in this current KCPL rate case that KCPL anticipates that one segment of its transmission expenses, SPP regionally-allocated transmission plant charges will increase until 2018. He also testifies that the other segments of KCPL's transmission expense, SPP Schedule 1A Administrative Fees (Admin fees) are decreasing and the FERC Assessment assessed through the SPP ("FERC assessment) has remained very steady.

Q. Did Mr. Carlson provide rebuttal testimony on SPP Transmission Fees in KCPL rate case ER-2014-0370 ("2014 rate case")?

A. Yes, he did. That rebuttal testimony was marked as Exhibit 107 in that case. In his 2014 KCPL rebuttal testimony Mr. Carlson stated that the SPP provides annual projections of base plan funding expenses, and these are only projections which have no bearing on actual expenses. Mr. Carlson then pointed to a chart at page 8 of his 2014 rebuttal testimony and stated:

> Staff pointed to the Direct Testimony of Tim M. Rush in which he provided a calculation of the "projected" annualized increases in Schedule 11 charges for 2013-2022. Staff somehow mischaracterized these "projected" Schedule 11 charges as known

> and measurable. Such costs are more accurately described as "expected and projected".
>
> While SPP provides annual projections of base plan funding expenses, these are only <u>projections and have no bearing on actual expenses.</u>
>
> <u>The following chart shows how SPP projections vary drastically from projection to projection. Projections for calendar year 2013 vary by approximately $7.0 million when comparing the projection from July 10, 2012 to the projection from July 8, 2013. Similarly, projections for calendar year 2015 vary by approximately $8.0 million dollars between the various projections.</u> (emphasis added)

Q. At page 9 of his direct testimony Mr. Ives states that SPP regional transmission upgrade projects are being planned, constructed, and billed to SPP members in order to expand and enhance the ability for the SPP transmission footprint. He also states that as these projects are placed in service, KCPL is continuing to receive its share of the costs of the expansion. What is a main cause of KCPL's increased transmission charges from the SPP?

A. KCPL's transmission cost increases are, to a significant extent, a direct result of the high number of SPP regional transmission projects that have been and are being constructed by utilities and other entities in the SPP footprint.

A number of these projects include increased costs due to higher FERC-allowed equity returns and incentives as well as other extraordinary ratemaking mechanisms granted by FERC. For example, FERC allowed a 50 basis point ROE adder solely for an entity being a member of a Regional Transmission Organization, such as the SPP.

Q. How does KCPL propose to treat transmission expenses for ratemaking purposes in this case?

A. Mr. Ives describes KCPL's primary proposal at page 9 line 18 of his direct testimony that an average of 2017 and 2018 forecasted levels of KCPL transmission expense be included in KCPL's FAC. Mr. Ives states that if the Commission does not agree to include transmission expenses in KCPL's FAC, it should instead authorize the use of a transmission tracker and set the cost of service transmission expense at the average of forecasted future expenses.

Q. Does OPC support including transmission expenses in a fuel and purchased power FAC tracker?

A. No. OPC's position on KCPL's proposal to include transmission expenses in KCPL's fuel and purchased power FAC is addressed in the rebuttal testimony of OPC witness Lena Mantle.

Q. Does OPC have any concerns about KCPL's proposal to obtain special ratemaking treatment (forecasted expense levels) for transmission costs in this case?

A. Yes. While there are potentially additional problems with this KCPL proposal, OPC has three primary concerns with KCPL's proposal to use projected future transmission expenses. Based on these concerns, OPC recommends the Commission reject KCPL's projected transmission expense ratemaking methodology.

Q. What is OPC's first concern about KCPL's proposal for special ratemaking treatment for its transmission expenses?

A. The first concern is that the Commission only allows recovery of expenses in a utility's cost of service that are "known and measurable". The known and measurable standard is a ratemaking standard long applied and enforced by the Commission. Basically, this standard requires that a cost or revenue in a rate case be known to exist and, if it is known to exist, the cost or revenue must be measurable with a high degree of accuracy.

Clearly, "projected" or estimated future transmission expenses for KCPL are not known and measurable. I am only aware of one time when projected costs were considered an option in setting rates and that was during the 1970s when fuel costs were rising significantly and were extremely volatile. My understanding is that projected fuel costs were considered in lieu of a fuel adjustment clause. I am not aware of any of time when projected future costs were seriously considered in a Missouri rate case proceeding.

For the Commission to abandon its known and measurable standard, I believe KCPL would have to provide significant evidence that - due to this one expense - it is experiencing significant financial problems. KCPL has not done that in this rate case.

Q. What is OPC's second concern about KCPL's proposal to set electric utility rates in this case based on estimated or projected future transmission expenses?

A. The second concern is related to the accuracy of projecting future costs and events. OPC does not believe this can be done with any reasonable degree of accuracy. In addition, KCPL's own witness on SPP transmission expense in this rate case, Mr. John Carlson, testified before this Commission in KCPL's 2014 rate case to the same effect. KCPL witness Carlson testified that SPP cost projections are not reliable and SPP cost projections "vary drastically" from projection to projection.

Simply stated, future year projections of actual costs are not accurate and are not reliable. Setting rates on inaccurate and unreliable costs projections is not something that the Commission should agree to do in this rate case.

Q. Describe OPC's third concern about KCPL's transmission expense proposal.

A. KCPL's purported need for forecasted transmission expense will soon end as the year-to-year increase in the regionally-allocated portion of transmission costs will soon end. KCPL witness Carlson states at page 8 (lines 7-11) of his direct testimony in this case that Base Plan Funding expense will continue to increase through 2018 and peak in 2018.

It is reasonable to assume given the mechanics of plant-in-service ratemaking, that the cost of these regionally-allocated projects will begin to decrease after their peak in 2018. Rates from this rate case will go into effect in approximately May 2017, which means that in the worst case scenario, KCPL will only face increases in this one expense for about 1.5 years. Regulatory lag allows for any decrease in these regionally-allocated costs from SPP to KCPL after the 2018 peak to act as a reimbursement mechanism for KCPL. Given that rates in this case will likely include a higher level of regionally-allocated SPP expenses that incurred by KCPL post-2018, regulatory lag should compensate KCPL for any potential under-recoveries until this expense starts to decrease.

Q. Is that method you just described the way regulatory lag is supposed to work?

A. Yes. There are times when a utility experiences higher expenses than the level of expenses directly included in rates for that individual expense. At times, just the opposite is true, and a utility's rates were set on a level of expense that is higher than the actual level incurred. This is how ratemaking which is based on regulatory lag works and works well to balance the interests of Company and ratepayers.

Ratemaking can only work efficiently if regulatory lag is allowed to create the pressures on utility management to continually focus on reducing costs to meet earnings targets. When that management pressure is removed, ratemaking fails and unnecessarily higher costs will undoubtedly be forced on ratepayers. Also, when this management pressure is removed, the Commission, who is tasked to make sure that a utility faces these competitive price pressures, is unable to perform its main role, which is to protect ratepayers.

Q. As an example, did the competitive pressures of regulatory lag work effectively with one segment of KCPL's transmission expense, Schedule 1A Admin Fees?

A. Yes, it did. KCPL witness Carlson describes on page 9 (lines 14-19) of his direct testimony that a portion of KCPL's transmission expenses as (Schedule 1-A SPP Administrative fees) have been decreasing. He states that for 2016 the administrative charge is $0.37/MWh, which is a decrease from the 2014 level of $0.381/MWh and the 2015 level of $0.39/MWh.

Whether KCPL's current transmission expenses were set on the 2014 level or the 2015 level of Schedule 1A fees, KCPL is now recovering in rates more for this transmission expense than it is being charged by the SPP for this expense. Regulatory lag is working for this segment of KCPL's transmission expenses just as it will work for the other segments.

Q. Does KCPL management have an ability to control SPP Administrative fees?

A. To a great extent, it does. This is yet another example of how regulatory lag has performed its "competitive pressure" function well and worked in favor of KCPL and other SPP members.

Over the past several years SPP members have pressured the SPP leadership to control and reduce its Administration fees. This pressure from SPP members like KCPL was likely the result of increased Schedule 1A expenses that may not have been fully and directly recovered in the utility rates of the SPP members. This cost pressure caused SPP members to focus on cost increases and take action to reduce costs. Is this situation, the existence of regulatory lag that has caused the decrease in SPP's Schedule 1 Administration Fees.

Removing this regulatory lag cost pressure by placing transmission expenses in a FAC or placing them under a tracker is bad ratemaking policy and will result in unnecessarily higher costs, unreasonable rates and removes the opportunity for regulatory lag that would benefit KCPL.

Q. In addition to the fact that KCPL's transmission expense proposal is 1) not capable of being known and measurable, 2) may soon not be a cost issue, and 3) eliminates essential management cost control pressures, does OPC have a final concern with this KCPL proposal?

A. Yes. OPC supports the use expense trackers under certain conditions and for short time periods. One primary condition for this support is that the utility act prudently and take all available actions to minimize that cost. That condition does not exist with KCPL. KCPL's management is taking an imprudent position on this cost issue by excluding utility transmission revenues from its cost of service. Mr. Ives and KCPL witness Mr. Ron Klote are proposing revenue adjustment R-80 that removes from regulated utility operations the regulated utility revenues KCPL receives by providing transmission service to other members of the SPP.

Q. Do KCPL's transmission revenues provide an opportunity for KCPL to mitigate any negative earnings impact from increased regionally-allocated transmission project costs?

A. Yes. KCPL management has imprudently decided not to take advantage of this opportunity and instead took specific actions that increase its cost of service.

The ability to increase transmission revenues, when netted against transmission expenses, results in lower net transmission expense. KCPL had an opportunity to significantly increase its transmission revenues and thus reduce its transmission expense but decided to transfer this opportunity and these utility revenues to its non-utility parent company, Great Plains Energy ("GPE") and GPE's nonregulated ventures.

REGULATORY LAG

Q. What is your overall concern with Mr. Ives' description of regulatory lag in his direct testimony?

A. In his direct testimony, Mr. Ives provides the Commission with an incomplete and narrowly-focused discussion of regulatory lag. For example, nowhere in his testimony does he address the very significant benefits to a utility from regulatory lag, the very benefits that have allowed KCPL's shareholders to enjoy past actual returns on equity that were higher than its actual cost of equity.

In addition, Mr. Ives does not address the very real and potentially very serious side-effects of trackers and other single-issue ratemaking mechanisms. Trackers and other single-issue ratemaking mechanisms work as a disincentive to utility management to control costs. That is just a simple fact that KCPL refuses to recognize and address.

The position of trackers being a disincentive to utility cost control is not only supported by OPC, Staff, and the Commission's past orders, but by highly recognized industry experts.

Q. Do you have significant experience working with the issue of trackers and other single-issue ratemaking mechanisms?

A. Yes. I have been involved in numerous cases involving the issue of regulatory lag and mechanisms designed to address regulatory lag, such as accounting authority orders (AAOs), and both natural gas and water utility Infrastructure System Replacement Charge ("ISRS") cases. I have also testified before the Commission in GMO's FAC Case EO-2011-0390.

Q. Have you previously filed expert witness testimony before the Commission on the issue of regulatory lag?

A. Yes, on several occasions. I filed extensive testimony on regulatory lag in KCPL's 2014 rate case ER-2014-0370.

Q. Please describe regulatory lag.

A. Regulatory lag explained simply is the time between the incurrence of a cost or revenue by a utility and the direct reflection of that cost or revenue in rates established in a rate case. A better and more descriptive definition is provided by Alfred E. Kahn in his book *The Economics of Regulation: Principles and Institutions.* in which he refers to regulatory lag as a "positive advantage" of cost of service rate regulation. Professor Kahn, a former Chairman of the New York Public Service Commission, is likely the most widely recognized and often-cited expert on the economics of regulation. He provides this definition of regulatory lag:

> The regulatory lag - the inevitable delay that regulation imposes in the downward adjustment of rate levels that produce excessive rates of return and in the upward adjustments ordinarily called for if profits are too low - is thus to be regarded not as a deplorable

> imperfection of regulation but as a positive advantage. [Kahn, A.E., The Economics of Regulation: Principles and Institutions (New York: John Wiley & Sons, 1970, Chapter 2, p.48).]

Q. What did Mr. Kahn believe about the role of regulatory lag in the ratemaking process?

A. Professor Kahn believed regulatory lag can be used by a regulatory body to incent positive utility management behavior. In The Economics of Regulation: Principles and Institutions (chapter 2, page 48) he states that "freezing rates for the period of the lag imposes penalties for inefficiency, excessive conservatism, and wrong guesses, and offers rewards for their opposites: companies can for a time keep the higher profits they reap from a superior performance and have to suffer the losses from a poor one." In essence, Professor Kahn describes the use of regulatory lag in the rate-setting process is the way a state utility commission can fulfill its calling to be a surrogate for competition in a monopolistic environment.

Q. What is your understanding of when the benefits of regulatory lag were first discussed?

A. William Baumol, a respected professor at New York and Princeton Universities first explained the benefits of regulatory lag in the 1960s.

> The idea of using "regulatory lag", the delay between rate cases, for incentive benefits came from Baumol (1968). He argued that the regulated firm would have incentive to control its costs while it was stuck with unchanging prices between rate cases, the fixed prices essentially serving as a stick. So he proposed a specific time period between rate cases, such as three years or five years, when prices would remain fixed. [Review of Network Economics Vol.2, Issue 4 – December 2003]

Q. What is your view of regulatory lag?

A. Regulatory lag is the primary tool available to a rate-setting body to incent the management of a monopoly to act efficiently under similar competitive pressures as experienced by management of competitive firms. Regulatory lag is the cornerstone of cost of service regulation and attempts to manipulate regulatory lag with more than minor and temporary adjustments risks breaking down the very fundamental basis of rate regulation that has served Missouri utilities and the Missouri Commission so well over so many years.

Q. Do you believe that regulatory lag is a necessary, if not critical, component of utility cost of service regulation?

A. Yes. Regulatory lag creates a type of "competitive environment" for utilities, in some ways somewhat similar to the environment in which competitive firms operate. Because of regulatory lag, regulated firms such as KCPL have a strong incentive to keep costs low once rates are set in order to achieve reasonable profits for shareholders.

Regulatory lag is best and most efficient when it is allowed to operate freely and without restrictions. Freely operating regulatory lag creates an environment similar to the environment experienced by competitive firms that cannot immediately increase prices due to rising costs.

In the competitive world there are periods when demand for the product will not support higher prices in a declining and changing economic environment. When this occurs, management is tasked to minimize any reduction in profits by taking cost reducing actions and operate the company at a very efficient level. In such an environment, utilities are better protected than competitive firms as they can raise prices by showing proof of rising costs. However, that price adjustments are not immediate. During the period between rate changes is when utility management is called to act and manage the utility skillfully by maintaining profit levels during periods between rate cases and potentially delaying rate cases.

Q. Does regulatory lag, when allowed to work as designed, affect regulated utilities like KCPL in a symmetrical or balanced manner, providing benefits to shareholders through higher earned ROEs in good economic times and lower earned ROEs in bad economic times?

A. Yes. That symmetry represents the inherent equity or fairness that is embedded in regulatory lag. It is that symmetry, the ability to respond to major economic factors in an unbiased fashion, that is exactly what needs to be protected about regulatory lag. This inherent quality, the ability to operate without bias, is so embedded in regulatory lag that it is inextricable, that is, not able to be separated without causing negative outcomes.

Q. Is this inherent equity quality, which is embedded in regulatory lag, mentioned anywhere in Mr. Ives's testimony to this Commission?

A. No, it is not. In his testimony, Mr. Ives only presents the Commission with his view that regulatory lag is only negative and has no positive aspects for KCPL. Yes, utilities like KCPL do experience some short-term negative consequences of regulatory lag when expenses grow faster than normal and revenues or other technological advances are not, at that time, sufficient to compensate for these changes. However, utilities like KCPL are protected to the extent that they control the effect of regulatory lag, and most importantly, this effect of regulatory lag is limited.

While they may be time consuming and require the incurrence of additional costs, utilities have total control over when they file for rate increases to offset any negative effects of regulatory lag. On the other side of the regulatory lag equation, ratepayers have little defense and are almost completely powerless to mitigate when regulatory lag works to the utilities' advantage for an extended period with higher than authorized profit levels.

Q. Did many utilities including KCPL enjoy very high profit levels in the years prior to the recession in 2008?

A. Yes. KCPL enjoyed very high profit levels during this period.

Q. Did KCPL take any action to lower these high profit levels caused by regulatory lag?

A. No, it did not. Regulatory lag has a symmetrical nature and KCPL has experiences both sides of that symmetrical nature. KCPL's reaction to regulatory lag, however, has not been symmetrical. KCPL has taken a one-sided narrow approach to try to eliminate the part of regulatory lag that forces its management to work hard to focus cost control and absorb less than the authorized maximum profit levels.

Q. Did KCPL express any concern that its operating profits during prior periods were too high and propose changes to the Missouri regulatory environment to reduce its profits to a reasonable level?

A. No, it did not. The benefit of regulatory lag is that it is symmetrical over time and is free from bias. The same cannot be said of KCPL. When regulatory lag benefits shareholders over customers the company takes no steps to change the process. When regulatory lag benefits customers over shareholders the company has sought ways to change the process to benefit shareholders.

KCPL's Property Tax Expense

Q. Describe Mr. Ives' proposal to treat KCPL's property tax expense in this rate case?

A. At page 10 line 6 of his direct testimony Mr. Ives proposes that test year property tax expense be adjusted to a level that is based on the average of projected property taxes in 2017 and 2018. This expense will then be tracked on a going-forward basis.

Q. Does OPC support KCPL's proposed ratemaking treatment of property taxes?

A. No. As noted above, OPC will only support special ratemaking mechanisms, such as trackers, when the utility is actually trying to keep its costs as low as possible for its customers and not abusing the single-issue ratemaking mechanism privileges that have already been granted to the utility. KCPL is not doing that.

While there are several, in this testimony I point out just two ways KCPL management is not trying to keep utility costs as low as possible. Above I noted that KCPL management is seeking to transfer dollars of transmission revenues from ratepayers to shareholders. KCPL has absolutely no logical or reasonable reason to do this, yet it does. In my direct testimony and in the testimony of OPC witness Amanda Conner, OPC addressed the continuing problem of KCPL's excessive management expense report charges. If KCPL cannot clean up this problem and be trusted to spend ratepayer revenues wisely at this level, it certainly cannot be trusted with additional single-issue ratemaking mechanisms such as a property tax tracker based on projected costs.

Finally, it is OPC's position as expressed in the direct and rebuttal testimony of OPC witness Lena Mantle that KCPL is taking advantage of the privilege granted to KCPL by the Commission in the form of a fuel adjustment clause. OPC will not support any additional single-issue ratemaking mechanism for KCPL until it fixes the problems OPC identified with its FAC and begins to treat the FAC as a privilege and not a right.

REBUTTAL OF KCPL WITNESS HEIDTBRINK

Q. Mr. Heidtbrink's direct testimony discusses customer service and the company's cost control measures. At page 5 line 4 of his direct Mr. Heidtbrink states that KCPL "has been, and remains, focused on meeting its customers' needs." Do you agree with this statement?

A. No. KCPL management may have a focus on meeting some customer needs such as reliability of electric service, and Mr. Heidtbrink provides some examples of this in his direct testimony. However, KCPL management ignores other significant customer needs and cost control measures.

Q. What particular customers needs are ignored by KCPL management?

A. Customers need to be able to afford the utility service. KCPL management ignores this need when KCPL management fails to act reasonably and prudently when incurring costs. As shown in my direct testimony, and in the direct testimony of OPC witness Amanda Conner, KCPL management fails to provide an important cost control measure when it comes to meeting the customer need for affordability when KCPL management unreasonably and imprudently charges ratepayers for excessive monthly management expenses.

Q. In your direct testimony you identified major concerns with KCPL management's continued imprudence associated with managing its management expense report policies and procedures and costs. Is Mr. Heidtbrink primarily responsible for KCPL's continued problems in this area?

A. Yes. Mr. Heidtbrink, as KCPL's Chief Operating Officer, is responsible for setting the tone for KCPL's corporate culture regarding management expenses. Problems in this area have been raised on numerous occasions by Commission Staff rate case auditors as well as KCPL's own internal audit department auditors. Mr. Heidtbrink, as Chief Operating Officer, is primarily responsible for the failure to address this problem.

Mr. Heidtbrink is KCPL's highest ranking officer who is not also an officer of KCPL's nonregulated parent company. Therefore, unlike other KCPL officers, his loyalty to KCPL's customers and responsibility to these customers should undivided. At page 1 of his testimony Mr. Heidtbrink explains that he is "responsible for all aspects of KCP&L's utility operations, including Generation, Transmission and Delivery Operations, Customer Service, major construction and Critical Infrastructure Protection Standards ("CIPS"), including KCP&L Greater Missouri Operations Company ("GMO")."

Q. Have you reviewed Mr. Heidtbrink's test year expense report charges?

A. Yes, I have.

Q. Based on this review do Mr. Heidtbrink's actions reflect a focus on meeting KCPL's customers' needs for KCPL to act prudently in the incurrence of monthly expense report charges?

A. No. Similar to other KCPL officers Mr. Heidtbrink charges KCPL for excessive expenses on his monthly expense reports related to food, travel, and entertainment and miscellaneous purchases.

In addition, my review indicates that Mr. Heidtbrink charges KCPL ratepayers for an excessive number of lunch meal costs in the Kansas City, Missouri local area. In the test year Mr. Heidtbrink charged KCPL ratepayers for lunches in downtown Kansas City on 36 separate occasions for a total cost of $1,739.

Q. Do other KCPL officers also charge Missouri ratepayers for local meals, costs that most people have to pay out of their own pocket?

A. Yes. Other members of KCPL management exceed Mr. Heidtbrink's expenditures. However, Mr. Heidtbrink is a significant contributor to KCPL's excessive management expense report spending especially because he is in a position to curb such excessive and imprudent spending

Q. What is Mr. Heidtbrink's annual compensation?

A. Mr. Heidtbrink's 2015 annual base salary was $503,000 (based on KCPL's 2015 FERC Form 1 page 104). With the addition of employee benefits such as pension costs, Mr. Heidtbrink is compensated a minimum of $800,000 annually by KCPL ratepayers.

Q. If other KCPL management employees charged ratepayers for Kansas City area lunch meals in the same frequency and magnitude as Mr. Heidtbrink what would be the annual dollar impact?

A. The annual cost to ratepayers of being forced to pay for KCPL management's lunches under this assumption would be between $1 million and $2 million annually.

Q. How long have you audited and raised concerns to the Commission concerning KCPL's excessive and imprudent management spending?

A. I have raised concerns in this area with KCPL and the Commission since KCPL's 2006 rate case, ER-2006-0314. I have addressed in testimony KCPL's excessive and imprudent management spending in most, if not all of KCPL's rate cases since 2006.

Q. Describe the corporate culture KCPL management has developed with respect to management spending.

A. KCPL's corporate culture as it relates to management spending for meals, travel and miscellaneous purchases is extremely permissive and allows management to regularly incur excessive and imprudent charges. KCPL management places no spending limit or reasonableness evaluation when reimbursing management expenses. For example, it is unreasonable for a highly paid executive to charge the company for local meals in Kansas City but this occurs regularly at KCPL. If these amounts are charged to ratepayers, it unnecessarily increases the cost of service and can impact the affordability of rates. If these amounts are recorded below-the-line, then shareholders suffer reduced earnings. These expenses are excessive and imprudent whether charged to ratepayers or shareholders.

KCPL's corporate culture has permitted excessive and imprudent management spending for the past ten years. It is evident that nothing will change this corporate culture except strong Commission admonishment. Commission action on this issue can protect both ratepayers and shareholders.

Q. How can the Commission communicate its concern to KCPL in this area?

A. First, the Commission can order the low-end of a range of reasonableness in its ordered return on equity rate in this rate case. Second, the Commission can and should include consideration of this management behavior in evaluating and denying KCPL's requested proposed shareholder-risk reducing rate mechanisms such as its proposed transmission expense and property tax expense trackers. The Commission should require KCPL to demonstrate it has established and complies with a reasonable and prudent management expense policy.

Q. Please summarize your rebuttal testimony as it pertains to KCPL's imprudent management expenses.

A. KCPL's customers expect reliable utility service. Customers also expect that KCPL management will incur no more costs than is necessary to run the utility in a cost efficient and reliable manner to keep rates affordable. Failure to meet this customer expectation can be as detrimental to a customer's experience as getting customer's bills wrong or taking too long to answer a customer calls for assistance.

Mr. Heidtbrink, as COO, sets the tone at the top for management spending and should resolve to correct the excessive and imprudent management expenditures. Furthermore, the Commission should take strong action to help convince KCPL management that it needs to address this problem. KCPL management is incapable of fixing this problem on its own as it has demonstrated this lack of capability for the past ten years.

Q. Has OPC proposed an adjustment in its direct filing in this case that is intended to protect ratepayers from KCPL's excessive expense report charges?

A. Yes. While this adjustment is designed to protect ratepayers from these excessive charges, the point I am making here addresses and responds to KCPL's testimony that it is focused on customer needs. The management expense policies and practices of KCPL and KCPL's top management reflects a lack of concern about utility customers. The absence of reasonable and prudent cost control measures related to management expenses also indicates a lack of concern about running the utility operations of KCPL efficiently to benefit both ratepayers and shareholders.

Q. In addition to an expectation of prudence and reasonableness as it relates to incurring utility costs do customers also expect to be treated with courtesy and respect?

A. Yes, they do.

Q. Has KCPL management taken specific actions which demonstrate that it has little or no concern with this customer service factor?

A. Yes. Around 2005 KCPL associated itself with a high-pressure marketing company Allconnect, Inc. ("Allconnect"). When KCPL customers called in to relocate or start new service, KCPL gave the customer an option to be transferred to Allconnect to hear Allconnect's sales pitch for services unrelated to utility service. Most of KCPL customers declined this option. Given the strong desire of KCPL's customers not to be transferred to Allconnect, KCPL had to end its relationship with the marketing company.

However, more recently in 2013, KCPL re-started the Allconnect program under the direction of KCPL witness Charles Caisley. Under the revamped program, KCPL decided not to respect the wishes of its customers and chose call center scripts designed to mislead its customers into being transferred to Allconnect. This led to the Commission's Staff filing a complaint, EC-2015-0309, against KCPL and GMO.

Q. What was the result of that complaint case?

A. The Commission found the company had violated Commission Rule 4 CSR 240-20.015(2)(C) by transferring customer information and calls to Allconnect in exchange for a fee.

Q. Did the Commission order KCPL to obtain informed customer consent before transferring customer information to Allconnect if it wished to continue the program?

A. Yes. In fact, issued an order indicating the script that the company must use if it wished to continue transferring customer information and calls to Allconnect.

Q. Did KCPL ignore that Commission order?

A. It appears so. KCPL management chose to ignore the Commission's Report and Order in EC-2015-0309 to stop violating Commission Rule 4 CSR 240-20.015(2)(C) by transferring customer information without consent. KCPL refused to comply with this Commission Order as evidenced by the Company's Notice of Termination of Transferring Missouri Customer Calls to Allconnect filed on December 9, 2016. After learning that KCPL and GMO were still transferring customer information and calls to Allconnect without using the

Commission-approved script, OPC filed a complaint, EC-2017-0175, on December 13, 2016.

Q. Is Mr. Heidtbrink responsible for KCPL ignoring the Commission order and directive on Allconnect?

A. Yes. Mr. Heidtbrink as the leader of KCPL was responsible for allowing KCPL to restart the Allconnect marketing program that was appropriately abandoned in 2005. Mr. Heidtbrink is responsible for the way KCPL treated its customers through its association with Allconnect and Mr. Heidtbrink is responsible for the significant maltreatment of its customers by transferring customer information to a high-pressure marketing company in violation of the Commission's affiliate transaction rule.

Q. Does KCPL's treatment of customer information related to Allconnect raise other concerns about the information collected by the company?

A. Yes. In Mr. Heidtbrink's direct testimony, at page 9, he discusses Meter Data Management for KCPL's new AMI meters explaining the company plans to collect "centralized customer data that can be used to assess and improve operational efficiency in a number of areas, including billing revenue protection, outage management and customer service." The Commission should be very concerned about KCPL's management's past actions in the Allconnect case may be repeated with the customer information collected for Meter Data Management.

<u>REBUTTAL TO THE DIRECT TESTIMONY OF KCPL WITNESS CHARLES CAISLEY</u>

Q. Does Mr. Caisley describe his expertise in the area of customer service in his direct testimony?

A. Yes. Mr. Caisley is primarily a marketing executive and his description of his experience confirms that assessment. Mr. Caisley has little or no traditional utility customer experience, such as working with and supervising utility customer service employees and customer call center employees. Mr. Caisley's primary focus and attention, however, appears to be the marketing of KCPL's brand name and raising the image of KCPL in the minds of KCPL customers. Mr. Caisley states in his testimony that for most of his professional career he has been involved in marketing activities such as drafting, fielding, and analyzing of telephone and online polls, focus groups and other survey instruments. Mr. Caisley states that he has drafted and analyzed more than 400 telephone polls since 1999.

Q. Do you view the type of "customer service" activities in which Mr. Caisley focuses his time and attention as being necessary for a utility to provide safe and adequate service and good customer service?

A. No. While Mr. Caisley may focus on some activities that can be considered customer service, building KCPL's image in the minds of its customers and charging customers for these efforts is not only unnecessary, it is inappropriate.

In fact, since the company began to focus on these "image building" activities, KCPL's customer service ratings, relative to its peer utilities, have dropped dramatically. KCPL used to be a top performer and score well in JD Power residential customer service surveys. However, since the focus on these activities under Mr. Caisley's direction KCPL consistently performs at below-average to average levels in these surveys.

Q. At page 3 of his direct testimony Mr. Caisley states he has been serving on the J.D. Power and Associates ("JD Power") Utility Customer Executive Advisory Board on Customer Experience since 2012. Have you measured KCPL's JD Power residential customer survey results over the past several years?

A. Yes. I performed an analysis of how KCPL scored in relation to peer group electric utilities in the JD Power residential customer surveys from 2006 through 2016. From 2009 through 2011, KCPL ranked no lower than 3rd in the group of 16 utilities. In the last three years, KCPL has scored no higher than 9th out of 16 electric utilities in the peer group.

Q. Did Mr. Caisley address KCPL's JD Power residential customer service survey scores in his direct testimony?

A. Yes. At page 12 he states that KCPL uses JD Power as a benchmark against other utilities to see at a high level how well KCPL is providing customer service. At page 4 line 15 Mr. Caisley states that KCPL's goal is to be top quartile among utilities nationwide.

Q. Is KCPL close to its goal of being in the top quartile nationwide?

A. No. As the JD Power chart below shows, KCPL has not even finished in the top quartile of the 16 Midwest utility peer group of electric utilities since 2011.

JD Power Residential Customer Survey	KCPL Score	Midwest Large Utility Avg	Number in Peer Group	KCPL Rank in Peer Group	KCPL Points Above (below) Peer Avg Points
2006	679	663	15	8	16
2007	697	651	17	5	46
2008	667	623	12	4	44
2009	646	609	16	2	37
2010	655	624	16	3	31
2011	644	621	16	3	23
2012	625	617	16	7	8
2013	640	631	16	6	9
2014	641	644	16	9	(3)
2015	660	661	16	11	(1)
2016	678	678	16	9	0

Q. Has KCPL's JD Power residential survey ranking among the peer group utilities only been decreasing over the last couple of years?

A. No. This decrease in ranking among its peers in the residential customer service survey has occurred over the last five years, starting in the year 2011 to 2012 and continuing through 2016.

Q. Has KCPL considered it important to look at the relative rankings of the individual companies in a JD Power survey and compare the ranking with the other electric utilities in the peer group?

A. Yes. In Case No. ER-2010-0355 Jimmy Alberts, KCPL's former Vice President of Customer Service stated in his rebuttal testimony at pages 9-10:

> Q: Looking beyond the errors in Staff's interpretation of the business studies, do you have concerns regarding Staff's interpretation of the JD Power residential data?
>
> A: Yes. Staff makes reference to our good performance in the 2010 JD Power Residential study but fails to mention KCP&L's residential satisfaction scores rank among the best in the Midwest Large utilities categories in previous years.
>
> Even beyond the scores, **<u>I believe it is important to look at the ranking of the Company among its peers.</u>**
>
> For example, just prior to the Aquila acquisition, the 2008 JD Power Residential study was completed. KCP&L was ranked among the top four Midwest utilities and Aquila was ranked as one of the bottom four utilities. Since the acquisition, the combined company results are consistently ranked among the top four Midwest Large utilities.
>
> This would seem to indicate a grand improvement for Aquila/KCPL customers and a continuing excellent customer experience for KCP&L customers. (emphasis added)

Q. In his rebuttal testimony in Case No. ER-2010-0355 did Mr. Alberts, who was KCPL's senior customer service representative, provide a list of events outside of a utility's control that may impact a JD Power customer satisfaction score?

A. Yes. He said that some of the "factors that can impact utility index scores include, but are not limited to: Temperature differences from year to year; significant disruption to operations, like storms; upheaval and uncertainty in economic security, like that experienced during the past two-and-a-half years; rate cases; media coverage; and, public communication channels like blogs."

Q. Did Mr. Caisley state in his direct testimony at page 13 line 22 what he believes are the reasons why KCPL's JD Power scores have decreased relative to its peer group electric utilities?

A. Yes. He attributes this decline to the high number of KCPL rate cases, which he states are more than almost of all the Company's regional peers. He also attributes the decline in

KCPL's customer service rankings to the fact that KCPL spends significantly less on advertising "the KCP&L brand" relative to other utilities in the peer group.

Q. Is your experience that when the Company's JD Power scores are high, like they were prior to 2012, the Company attributes the high scores and high ranking among its peers to its management's activities to improve customer service?

A. Yes. When KCPL's JD Power scores are high, KCPL management takes the credit for the high scores and has, in the past, used these scores to increase management compensation.

Q. Is your experience that, when KCPL's JD Power scores decrease relative to its peers, like they have since 2012, the Company attributes the decrease in peer rankings to elements outside the control of utility management?

A. Yes. While KCPL often praises themselves for high scores and high peer rankings in JD Power surveys, they then disavow any responsibility for lower scores and low peer rankings.

This attitude of taking credit for the good but not taking responsibility for the bad significantly decreases the value of any JD Power survey results to the Commission. This attitude on the part of KCPL management only allows for misleading and "less than transparent" customer service measurement information being presented to the Commission.

Q. Other than Mr. Caisley's direct testimony in this case, what is the most recent document filed with the Commission where KCPL disavows any responsibility for decreased JD Power scores or peer rankings?

A. KCPL discussed the lower JD Power peer rankings at the bottom of page 7 KCPL's February 25, 2016 Reply Brief in Case No. EC-2015-0309, Staff's Allconnect Complaint Case against KCPL and GMO ("Allconnect Complaint"). Mr. Caisley was the KCPL witness on this issue in that complaint case.

In attempting to absolve KCPL management from any responsibility for the JD Power decreased peer group rankings, counsel for KCPL advised the Commission to ignore the actual survey results or relative peer group rankings. KCPL argued that, despite the decline in peer group rankings, there has been no slippage in customer service and the Commission should ignore the slippage in peer group rankings. KCPL indicated the Commission should focus only on the raw scores as the peer group rankings are affected solely by events and circumstances KCPL cannot control:

> It is possible that Public Counsel or Staff will argue that JD Power results show that the Company's customer satisfaction has slipped recently. These arguments are wrong, and should therefore be ignored, for a number of reasons.
>
> Despite higher raw scores in nearly all areas of the JD Power residential customer satisfaction index, our rank has fallen relative to peer utilities in the last couple of years.
>
> For the calendar year of 2015, in the JD Power Residential Customer Study, KCP&L scored just below the median in eleventh place out of sixteen large Midwestern utilities. (Ex. 115)
>
> We believe that there are a number of drivers behind our drop relative to other utilities. Chief among them is a high number of rate cases in recent years, more than almost all of our regional peers, as well as spending significantly less on advertising the KCP&L brand relative to other utilities in our peer group. (Tr. 485- 87)
>
> That said, we are seeing improvement in our ranking over the last two quarters and our customer satisfaction ranking is now ranked above the average for large utilities in the Midwest. (Ex. 117)

Q. In his rebuttal testimony in Case No. ER-2010-0355 did Mr. Alberts, who was KCPL's senior customer service officer at the time, indicate that utility image advertising had any impact on JD Power survey scores?

A. No. The list of events that may affect customer service scores included in his testimony, while not all inclusive, did not include a relative spending on image advertising as suggested by Mr. Caisley.

Q. Does OPC believe that JD Power surveys are a good indicator of a utility's actual level of customer service?

A. No. There are just too many variables that can affect a given utility's score in a given year even with the assumption that the number of customers contacted in the survey is statistically significant. However, it appears that KCPL and other utilities in Missouri believe JD Power survey results are relevant to customer service performance. Therefore, I have included an analysis of KCPL's JD Power survey results in this testimony.

Q. In your experience, does the Commission Staff put much value in JD Power scores?

A. No. Staff, correctly so, has taken the position that JD Power scores are not strongly correlated with an individual utility's actual customer service performance.

Staff witness Lisa Kremer stated in her rebuttal testimony in Case No. ER-2010-0355, Kansas City Power & Light Company, Staff's position on the value it places on JD Power surveys:

> Q. What value does the Staff attribute to KCPL/KCPL's participation in JD Power to the extent the Company pays for detailed reporting, the opportunity to ask additional survey questions, receive recognition in the form of trophies and other aspects of JD Power?
> A. In the Staff's opinion, the value of customer surveys to utilities and to the customers they serve is when they are used by the utility as a tool to identify deficiencies, take corrective action to address these deficiencies, and measure the Company's progress by developing benchmarks for improvement. While Staff is opposed to customer survey results being used as a justification for an increased ROE, Staff does recognize such surveys can be beneficial to the Company in improving its operations.

Q. Do you agree with this prior Staff testimony?

A. Yes. OPC supports KCPL doing customer surveys that are highly efficient, low cost, and specifically targeted to identify customer service problems as Staff suggests. OPC is concerned about the significant level of expenses KCPL is incurring (and charging to ratepayers) to have its consultants and marketing companies perform numerous customer surveys with little or marginal benefit.

Q. Do you believe KCPL use the JD Power surveys result in the manner suggested by Staff, that is, to identify and improve specific customer service issues?

A. No. It has been my experience that KCPL only uses JD Power survey results to promote itself and seek higher utility rates from ratepayers.

Q. When did KCPL seek to increase utility rates to its customers as a result of its JD Power customer survey results?

A. In his surrebuttal testimony in KCPL's 2010 rate case, No. ER-2010-0355, KCPL's Customer Service witness Alberts made the following statement seeking higher utility rates based on JD Power survey results:

> What is missing from Staff's analysis? Not only did KCP&L perform well within the Midwest Region for large utilities, third highest of sixteen, but KCP&L's performance was consistent across all large utilities within the United States.
>
> KCP&L's score was superior to 49 of the 58 other large utilities. This demonstrates KCP&L not only ranks in the top quartile within the Midwest, but ranks in the top quartile across all large utilities surveyed by JD Power. See LAK Schedules 3-4, 3-6, 3-8 and 3-10.
>
> <u>KCP&L believes that the Staff and Commission should recognize the outstanding performance by KCP&L by awarding an ROE above the mid- point range offered by the Company.</u> (emphasis added)

Q. Did KCPL witness Alberts state in his surrebuttal testimony in Case No. ER-2010-0355 that KCPL has no incentive to provide excellent service without receiving benefits like a higher return on equity in a rate case?

A. Yes. Mr. Alberts, in a moment of insightful candor, revealed the likely true motivation behind KCPL's efforts to promote itself with JD Power survey results. At page 3 line 3 of his surrebuttal testimony in Case No. ER-2010-0355, KCPL's highest ranking customer service management employee at that time stated:

> Without a hope of receiving any benefit-like a higher ROE-for excellent customer service, there is little incentive to offer but just enough customer service to avoid a formal complaint.

Q. If JD Power customer survey results are reflective of actual customer service, as KCPL believes they are, what do the historical results of KCPL's JD Power residential customer survey responses indicate?

A. They survey responses indicate that prior to 2014 KCPL provided <u>above</u> average residential customer service. For the years 2014 and 2015, KCPL provided <u>below</u> average customer service and for 2016, KCPL provided <u>average</u> customer service compared to its peers.

Q. At page 4 line 9, Mr. Caisley states that KCPL continually strives to improve customer service scores and metrics. As it relates to JD Power results, has KCPL failed in this area?

A. Yes, when you view the JD Power survey results as a benchmarking tool and evaluate how KCPL has scored relative to the other 15 utilities in the peer group.

Q. Given this failure on the part of KCPL, does that mean OPC believes that KCPL is not providing adequate or reasonable customer service?

A. No. As noted above, OPC does not accept JD Power results as a valid and reliable measure of customer service performance. With the exception of KCPL's poor treatment of certain customers related to its relationship with Allconnect and excessive management spending, I am not aware of any current concerns about the overall level of customer service provided by KCPL.

Q. At page 12 line 20 Mr. Caisley concludes that KCPL has provided a solid residential customer experience. Do you agree with this statement?

A. Yes I do. It has been my personal and professional experience that with the exception of the Allconnect issue, and with the exception of its ability to manage costs, two very major customer service issues, KCPL has provided solid customer service.

Given this solid track record, OPC does not see the need or the prudence in KCPL continuing to spend year after year thousands of dollars on consultants doing continuous surveys. These "customer service" consultant companies, such as WPA Research, appear to act more like marketing companies than objective customer survey consultants.

OPC also does not see the need for KCPL to promote itself through image-building advertising and charging these costs to ratepayers. KCPL must remember that they are regulated monopolies and not competitive companies that have to compete for customer dollars.

Q. Do you believe KCPL's customer service consultant surveys require a thorough review?

A. Yes. OPC is aware that KCPL's consultants are conducting surveys of KCPL's regulated electric utility customers asking them very pointed and specific questions about their political affiliation and political preferences. This is an absurd action on the part of a regulated electric utility and is not only a waste of ratepayer's money, but also borders on customer harassment.

Q. As an electric utility customer, would you personally be concerned if you were contacted by a polling company acting on behalf of the electric utility asking you about your personal political preferences?

A. Yes I would and I would question the pollster why are they asking me this question. I would even be more offended and disappointed if I found out that the utility was charging me in utility rates for the expense of this polling or surveying consultant. OPC intends to look closely into KCPL's marketing/customer service surveys in the near future and take action to prevent this type of utility behavior from recurring, or at a minimum, for the costs to be recovered in utility rates.

Q. Mr. Caisley states that KCPL takes customer experience very seriously. Do you believe that to be a true statement?

A. No. As a KCPL or GPE officer, Mr. Caisley was involved in Case No. EC-2015-0309, the Allconnect complaint case filed by the Commission Staff. I was also a participant and an expert witness in that Staff complaint case as a member of the Commission Staff and subsequently as a member of the OPC.

There is substantial evidence in the record in that complaint case to support a conclusion that not only does KCPL not take the "customer experience" seriously, KCPL management intentionally violated the Commission's electric affiliate transaction rule by releasing customer information without the customer's consent.

KCPL even took intentional actions to continue to violate the affiliate transaction rule after the Commission found KCPL in violation in its Report and Order in that case. OPC has filed a complaint with the Commission against KCPL on this issue.

KCPL's treatment of its customers through its relationship with the high-pressure marketing firm Allconnect has been inappropriate and does not reflect a concern for the customers' experience.

Q. Has KCPL recently announced that it has terminated its relationship with Allconnect?

A. Yes, but its notice indicated it would continue transferring calls until the end of the year rather than immediately comply with the commission's order and the affiliate transaction rules. KCPL's notice, attempted to place blame on the Commission Staff for this termination. However, "blame" is an inappropriate word to use in this circumstance. The Staff should be commended for its efforts to protect customers and ensure compliance with the Commission's Order in the KCPL/Allconnect complaint case. I am personally aware of the Staff's intensive work devoted to this issue to protect KCPL and GMO's customers from abusive treatment by the utility. OPC is thankful and appreciative of the very strong and very successful efforts put forth by certain members of the Commission's Staff on this issue.

Q. Explain how KCPL management intentionally disregarded the clear orders of the Commission in the KCPL/Allconnect complaint case.

A. OPC has outlined the details in its complaint against KCPL. KCPL's notice in this case admits the company's failure to comply with the Commission directives on the script ordered by the Commission. KCPL has continued to transfer customer calls and information to Allconnect in exchange for a fee without getting customer consent. In my experience I have never seen such a bold and defiant reaction to a Commission directive by a Missouri regulated utility.

Q. In its relationship with Allconnect Inc., how could KCPL have acted like it had an interest in the "customer experience"?

A. First, it could have provided its customers with a basic courtesy of not being transferred Allconnect, a high-pressure marketing company. Without any say in the matter, KCPL customers were transferred to a high-pressure marketing company when all the customer wanted was help with their electric service. No one familiar with this issue could realistically say a utility that treated its customers in this manner actually values its "customer experience".

Secondly, KCPL could have obtained its customer's permission, as required by the Commission's affiliate transaction rule (and required by the Commission's order), before it released customer information to Allconnect. KCPL not only ignored the clear meaning of the affiliate transaction rule but continued to violate this rule after the Commission ordered them in violation. This, again, does not indicate KCPL cares about its "customer experience" or even complying with governing regulations.

Q. Can you provide further evidence as to this assertion?

A. In the Allconnect complaint case, I listened to several audio recordings of telephone calls between KCPL and KCPL regulated utility customers and Allconnect marketing representatives where Allconnect personnel treated KCPL customers badly and offensively.

KCPL was aware of this behavior, or reasonably should have been aware of this behavior, and took no decisive action to stop this behavior from recurring.

In my opinion, a utility that cared about its customer's experience would never put its customers through such an abusive experience by transferring them to a high-pressure marketing company, especially without consent.

Q. Do you have evidence, in addition to the Allconnect issue, why you do not believe KCPL management cares about its customer's experience?

A. Yes. In addition to Allconnect, I have personally found that KCPL officers, such as Mr. Caisley, continue to incur expense report type charges that are imprudent, excessive, unreasonable and detrimental to customers and their experience.

OPC believes that, if what Mr. Caisley says in his testimony about the "customer experience" is true, KCPL would have ceased its imprudent, excessive, and unreasonable expense account spending habits in 2006 when the issue of excessive expense account spending was first raised by the Staff. The issue of excessive management expense report expenses has been raised in many, if not all, KCPL rate cases since 2006, yet the same irresponsible behavior by KCPL management continues.

If KCPL is concerned about its customers, management would stop charging its customers for excessive management expense report charges. Since it will not stop this behavior, the only conclusion that a reasonable person can make is that KCPL has no real concern about the well being of its customers.

REBUTTAL TO THE DIRECT TESTIMONY OF KCPL WITNESS RON KLOTE

Q. KCPL witness Ronald Klote discusses KCPL's proposed revenue adjustment R-80-Transmission Revenue ROE at page 32 line 7 of his direct testimony. Do you have any comments on this testimony?

A. Yes. KCPL Adjustment R-80 removes regulated utility transmission test year revenues recorded in KCPL's books and records. Removing these revenues from cost of service will increase KCPL's cost of service without any reasonable justification.

In his direct testimony KCPL witness Klote provides no reasonable logic or rationale why a regulated utility such as KCPL should exclude regulated utility revenues from its cost of service. As will be explained below, OPC finds KCPL's proposed revenue adjustment R-80 reaches a special level of unreasonableness.

Q. What is Mr. Klote's stated reason in his direct testimony why he believes KCPL's cost of service should be increased by assigning the utility's Missouri transmission revenues to non-utility, non-regulated operations?

A. The only reason put forth by Mr. Klote is that these transmission revenues are charged by KCPL to other entities in the Southwest Power Pool ("SPP") under KCPL's FERC Formula rate. FERC's formula rate currently includes a higher return of equity (11.1%) on transmission plant than KCPL is proposing in this case (9.9%). In explaining why this adjustment is necessary, Mr. Klote states at page 31 line 5:

> Absent this adjustment, the effective ROE included in retail rates for transmission assets would be less than that authorized by the MPSC.

Q. Could this statement by Mr. Klote be true?

A. No. This statement cannot be true. The effective return on equity dollars for KCPL in this rate case will be the return on equity authorized by the Commission multiplied times KCPL's approved net rate base. The regulated utility revenues KCPL receives, whether they are revenues received from Missouri retail customers or transmission revenues received from other entities in the SPP, have no impact on the return on equity dollars ordered by the Commission in this rate case. The authorized return on equity for KCPL's net utility assets will be set by the Commission in this rate case and is not affected by the inclusion or exclusion of any KCPL revenue or expense.

Q. In your experience have you ever heard of any party to any rate case or the Commission use the term "ROE included in retail rates for transmission assets"?

A. No. To my knowledge, only KCPL management has used this term. I have never seen any such calculation nor have I ever heard that term used in any rate case I have been involved with in Missouri since 2003. I conclude that KCPL must have crated that term and statistic to seek to create a reason to support this adjustment.

Q. Have you recently asked representatives of Ameren Missouri if they have ever proposed to remove regulated utility revenues from Ameren Missouri's cost of service as KCPL is proposing in this case?

A. Yes, I have. Representatives from Ameren Missouri stated they do not make any such adjustment and acted quite surprised when I advised them of KCPL's proposed adjustment.

Q. How would acceptance of Adjustment R-80 by the Commission impact rates for KCPL's customers?

A. If the Commission accepts this adjustment, it would be increasing KCPL's cost of service and imposing higher rates on KCPL's customers without any justification. The Commission should not support KCPL's attempt to take from its customers regulated utility rate revenues that act to reduce KCPL's cost of service.

Q. What is the inherent inequity in Mr. Klote's proposal to remove actual utility-earned transmission revenue from its cost of service in this case?

A. At page 41 of his direct testimony, Mr. Klote describes KCPL adjustment CS-45 *Transmission of Electricity By Others*. In this adjustment, Mr. Klote (and other KCPL witnesses) seeks special ratemaking treatment in the form of budgeted or projected future transmission expenses. Included in these future projected transmission expenses is the same higher FERC equity return charged by other SPP members to KCPL and passed on by KCPL to its ratepayers.

Therefore, as a part of KCPL's proposed special ratemaking treatment, it is asking the Commission for its permission to charge its customers for future estimated transmission payments to other SPP entities based on the same FERC return on equity cost that is embedded in the transmission revenues that it is seeking to exclude from its cost of service with its proposed adjustment R-80. To reiterate, no person who understands what KCPL is attempting to do through this adjustment would ever agree that KCPL is interested in its customers' well being.

Q. Should the Commission reject KCPL's proposed R-80 revenue adjustment?

A. Yes. The Commission should note the inherent inequity in such an adjustment and reject it from being included in KCPL's cost of service in this rate case.

Q. If the Commission accepts KCPL's revenue adjustment R-80, should the Commission, for consistency purposes, make a similar adjustment to KCPL's account 565 *Transmission of Electricity by Others*?

A. Yes. If the Commission accepts the methodology proposed by KCPL for transmission revenues (adjusting from a FERC revenue requirement to a Missouri revenue requirement basis), then it must apply this same methodology to transmission expenses. Symmetrical treatment is required for these ratemaking components because they reflect both sides of the exact same transaction.

In this case, the "flip-side" adjustment to Adjustment R-80 that would be necessary for the Commission to make is a downward adjustment to KCPL's transmission expense proposal in this case in CS-45. The Commission should order that KCPL's transmission expense recovery request in this rate case be lowered appropriately using the same methodology proposed by Mr. Klote for transmission revenues.

If the Commission accepts KCPL's proposed R-80 adjustment, this OPC-proposed responsive adjustment to KCPL's transmission expense would be fair and reasonable as it reflect the same ratemaking treatment proposed by KCPL for the exact same revenue requirement components – regionally-allocated transmission revenues and regionally-allocated transmission expenses.

Q. Please summarize OPC's position on Mr. Klote's proposed revenue adjustment R-80?

A. Mr. Klote's proposed R-80 adjustment is creative. However, it is not reasonable and simply makes no sense from a regulated utility ratemaking point of view. Revenues received by the utility from employing its own assets and from the provision of utility management services belong to the utility and not its affiliates. Any attempt to remove utility revenues from a utility's cost of service shows a lack of concern for the well being of the utility's customers.

<u>REBUTTAL TO THE DIRECT TESTIMONY OF KCPL WITNESS TIM RUSH</u>

Q. At page 3 line 11 of his direct testimony Mr. Rush states that rate case procedures normally used in Missouri do not provide a sufficient mechanism for KCPL to recover costs and still earn a fair return on equity. Does Mr. Rush provide any evidence to support this statement?

A. No, he provides no evidentiary support for this statement. In fact, as described above, there is significant evidence to the contrary including the fact that evidence indicates that KCPL's sister utility, KCPL - Greater Missouri Operations Company ("GMO") has been earning a fair return on equity over the past several years under Missouri rate case procedures.

Q. What evidence is there that GMO, who operates under the same identical rate case procedures as KCPL, has been earning a fair rate of return the last few years?

A. First, GMO last filed its rate case in 2012. KCPL also filed a rate case in 2012 and again in 2014. If GMO was not recovering all of its costs and still earning a fair return on equity then why did GMO not file for a rate increase in 2014 with KCPL? The strong presumption is that GMO was recovering all of its costs and earning a fair return on equity during the period 2012 through 2016.

Additionally, as I described in my rebuttal testimony to KCPL witness Mr. Ives' direct testimony, the Staff, in its 2016 rate case audit of GMO found that instead of GMO not earning a reasonable rate of return, it was earning significantly in excess of a reasonable rate of return. Staff found that GMO's current excess earnings are in the range of $30 million.

Mr. Rush and KCPL make general statements about Missouri's ratemaking procedures and how Missouri has a bad regulatory environment for utility investors. However, for the Commission to accept KCPL's assertions, KCPL must provide convincing evidence that it is the Commission and not KCPL that is to blame for KCPL's financial performance. It has not. There is no evidence in this case that the Commission or Missouri's regulatory environment is to blame for KCPL's purported lack of earnings but there is substantial evidence that KCPL is the party who deserves the blame, if there is blame, to be assessed.

Q. In your testimony in this rate case do you provide evidence why it is likely that KCPL management's skill in running the utility is likely the reason for KCPL failing to meet its profit level expectations?

A. Yes. In my rebuttal testimony I provide strong evidence that the regulatory environment in Missouri is in fact very fair to utility investors. I show that KCPL's recent history of not earning at its authorized return on equity over the past few years is very likely caused by KCPL management's skill and decisions made in running the utility.

Q. What are some examples that show KCPL management is likely responsible for its failure to meet expected profit levels?

A. KCPL management does not apply any reasonable standards to its spending. I have proven that this statement is a fact. Instead of focusing on cost control and efficiency improvements, KCPL's management has spent what I estimate to be hundreds of hours on its relationship with a high-pressure marketing firm, Allconnect.

KCPL senior management has spent and continues to spend significant time highly focused on non-Missouri utility operations. In 2016 much of KCPL's senior management devoted most of their time significantly devoted to spending billions of dollars in acquiring other out-of-state utility companies instead of focusing on KCPL's Missouri regulated customers. These are just a few of potentially dozens of examples that go a long way in explaining why KCPL's management performance, and not anything to do with the Commission, has led to less than expected profit levels.

Q. Is Mr. Rush KCPL's primary witness on its Fuel Adjustment Clause ("FAC")?

A. Yes, he is.

Q. Does OPC have several concerns with KCPL's proposed FAC and its accounting for purchased power costs?

A. Yes, it does. OPC witness Lena Mantle addresses OPC's concerns with KCPL's FAC and its proposed changes to its FAC. OPC witness John Riley explains to the Commission OPC's concern that KCPL is not filing its FAC documentation consistent with the FERC Uniform System of Accounts ("USOA"), specifically FERC Order 668, when it provides information related to purchased power costs in FERC USOA account 555, Purchased Power. OPC witness John Robinett explains how KCPL failed to meet the Commission's FAC filing requirement regarding heat rate testing and the importance of heat rate testing to fuel costs. He also provides testimony regarding KCPL's attempt to include unit train depreciation in its FAC.

Q. In general, what are some of the concerns with KCPL's proposed FAC?

A. The FAC proposed by KCPL is designed to liberally include any cost that is arguably related to fuel. OPC believes the company's approach is unreasonable. The FAC was created to address volatile fuel costs and purchased power, including transportation. It was not created so utilities can directly recover any expense that can be remotely associated with fuel and purchased power through the FAC thus eliminating any risk of non-recovery and eliminating any chance of a reasonable audit and review of those costs.

Q. What is one reason why utilities like KCPL try to include as many costs as possible into an FAC?

A. It is my opinion based on my experience that Missouri utilities know that it is very difficult for any party to overcome the Commission's burden of proof standard to exclude any actually incurred cost (regardless of its reasonableness) in a non-general rate case proceeding.

Q. Can you provide an example of the types of non-fuel costs Mr. Rush attempts to include in KCPL's FAC?

A. Yes. The essential characteristic of fuel is that it produces energy. Fuel such as coal, natural gas and uranium are converted into energy. Fuel adders, such as limestone, do not produce energy. Fuel additives are a cost of operating the plant that burns the fuel to produce energy. Fuel handling does not produce energy and includes a myriad of costs including airline fees and meal reimbursements. Many SPP cost do not result in energy being provided to KCPL. They provide support for generation but are not fuel costs. KCPL wants to even include some depreciation expenses in its FAC. These types of costs are not fuel and should not be included in a special ratemaking mechanism that was designed to mitigate the price volatility of fuel.

Q. Did you review Mr. Rush's Schedule TMR-4, the FAC base calculation?

A. Yes, I did. The specifics of this schedule are addressed in Ms. Mantle's testimony. However I did want to express a concern about Mr. Rush's attempt to include transmission expense in KCPL's FAC.

Q. Please continue.

A. Utility costs are made up of several large "buckets" or types of costs. For example there are debt costs, equity costs, labor costs, fuel costs, maintenance costs, depreciation costs, purchased power costs, taxes, transmission costs and miscellaneous operation and maintenance ("O&M") costs. These costs can be further classified into generation, transmission and distribution costs.

These are general utility costs that are separate and distinct and can be separately identified. KCPL has a fuel adjustment clause which was designed to allow recovery of fuel and purchase power costs. It was not designed to allow inclusion of the many other buckets of utility costs, such as depreciation, maintenance, labor, and transmission. Mr. Rush's attempt to force non-FAC costs in KCPL's FAC reflects badly on KCPL's treatment of the FAC privilege granted to KCPL by the Commission just a few years ago.

Q. In addition to the costs that you described are you aware of one of these types of cost that KCPL is asking to include in its FAC?

A. Yes. KCPL has included unit train depreciation to the steam FERC account in an attempt to recover this depreciation through the FAC. OPC witness John Robinett addresses this in his rebuttal testimony.

Q. Has the Commission ruled that transmission expenses do not belong in a FAC?

A. Yes, it has. It has issued Report and Orders for Ameren Missouri, the Empire District Electric Company and KCPL stating that the only transmission costs that can be included in the FAC are the costs to transmit true purchased power and off-system sales.

Q. Have other Missouri electric utilities accepted this Commission order and no longer seeking transmission costs in its FAC?

A. Yes. In its direct filing in its current rate case, Ameren Missouri has advised the Commission it is no longer seeking to include transmission expenses in its FAC. In addition, GMO, in its last rate case asked for all transmission costs to be included in its FAC but agreed to settle the case with only the transmission costs as the Commission ordered Ameren Missouri and Empire District Electric to include in their FACs.

Q. Has Mr. Rush or any other KCPL witness in this case provided any reason for the Commission to change its position on transmission expenses in a FAC?

A. No. KCPL has provided no new evidence why the Commission should change its position. Without any new evidence, there is little reason for the Commission to seriously consider KCPL's FAC proposal.

<u>REBUTTAL OF KCPL WITNESS HEVERT</u>

Q. At page 44 of his direct testimony one of KCPL's cost of equity witnesses Robert Hevert cites to a 2014 Standards and Poor's ("S&P") document which he purports is critical of the work of the Missouri Commission. Have you read this S&P document?

A. Yes. This document is attached to my rebuttal testimony as Schedule CRH-R-1.

Q. How did S&P assess the Missouri Public Service Commission, or the state of Missouri's regulatory environment in this document cited by Mr. Hevert?

A. In its July 7, 2014 "Utility Regulatory Assessments For U.S. Investor Owned Utilities," S&P ranked the Missouri jurisdiction as "Strong/Adequate." From a utility bondholder perspective S&P ranked the Missouri regulatory environment at its second highest possible rating. S&P's rating categories include:

1. Strong (the most bondholder friendly)
2. Strong/Adequate
3. Adequate
4. Adequate/Weak
5. Weak

Q. The document referenced by Mr. Hevert shows that the Missouri Commission created a strong and/or adequate regulatory environment for utility investors in 2013 and years prior to 2013. Is this document relevant to the regulatory environment that exists in Missouri today?

A. No. Only three of the five members of the Commission were on the Commission at in 2013 and Chairman Daniel Hall did not join the Commission until late in 2013, likely too late to have any impact on the S&P report published in January 2014. Four of the five current Commissioners were not on the Commission in 2012. Therefore, while the regulatory environment created by the Commission in 2013 and in years prior may have indeed been fair to utility investors as portrayed in the S&P report cited by KCPL witnesses Hevert and Ives, that does not necessarily mean that it is the same today. A 2014 S&P report that reflects a regulatory environment in 2013 and prior provides no meaningful evidence on any issue in this current 2016 KCPL rate case.

Q. Is there a more current assessment of the Missouri regulatory climate available?

A. Yes. The industry standard about statistics in rate cases and regulatory matters from a utility investor perspective, and in general, is the Regulatory Research Associates ("RRA"). RRA rates the Missouri Commission as Average/2 which is the rating assigned to the largest group of regulatory commissions in the 2016 RRA study. RRA affirmed its ranking of the Missouri Commission and the Missouri regulatory climate as recently as October 16, 2016.

Mr. Hevert consistently cites to the RRA as an authoritative and reliable source in his direct testimony. Of the 53 commissions ranked by RRA in its July 21, 2016 ranking, 18 commissions are ranked more shareholder-friendly than the Missouri Commission and 20 commissions are ranked less shareholder-friendly. The Missouri Commission is ranked in the middle of this group along with 14 other regulatory commissions.

Q. To the extent Mr. Hevert based his range of reasonable ROEs for KCPL based on an outdated and wrongly interpreted Missouri regulatory environment, is his cost of equity recommendation for KCPL overstated?

A. Yes, it is.

<u>CAPITALIZATION OF SERP EXPENSES STAFF WITNESS MAJORS</u>

Q. In his direct testimony did Staff witness Keith Majors explain why his proposed Supplemental Executive Retirement Plan ("SERP") adjustment reflects an allocation (or capitalization) of a portion of SERP expenses to plant construction accounts?

A. Yes. He states that Staff capitalizes SERP costs because KCPL capitalizes SERP costs. He provided no reason why it is appropriate for Staff to do so from an accounting or ratemaking standpoint. Mr. Majors states:

> KCPL and GMO currently charge a portion of SERP costs to plant accounts, also known as capitalizing these costs. In the response to Staff Data Request 229.1, KCPL identified that a portion of SERP has been capitalized for "a number of years" and there has been no change in that policy. The cumulative portion of capitalized SERP is included in the plant in service balances in Staff Accounting Schedule 3 as a portion of construction costs. <u>Because KCPL capitalizes SERP costs, Staff has included a reduction in SERP expense commensurate with the capitalization rate used in Staff's payroll adjustment in this case. (emphasis added)</u>

Q. Did KCPL management have a policy in 2016 that SERP costs should not be capitalized?

A. Yes, it did.

Q. Did Staff in the past have a policy that SERP costs should not be capitalized?

A. Yes, it did.

Q. Has either KCPL or Staff provided any reason why it changed from a non-capitalization policy to a capitalization policy for SERP?

A. Yes. As noted above, Mr. Majors stated that Staff changed its policy because KCPL changed its policy. However, KCPL has not explained why it changed its policy on SERP.

Q. Have you ever noted an instance when Staff changed a ratemaking policy simply because the utility changed its ratemaking policy?

A. No. If Staff wants to change a ratemaking approach to a specific cost in a rate case, I believe Staff owes it to the parties and the Commission to explain the theoretical rationale, from an accounting and ratemaking standpoint, why it changed its position. Staff stating that it changed its position because KCPL changed its position is not sufficient.

Q. Did a KCPL corporate officer previously testify before this Commission that it agreed that SERP expenses should not be charged to current construction projects?

A. Yes. In her 2010 rebuttal testimony witness Ellen E. Fairchild testified in Case No. ER-2010-0356 that she agreed with Staff's position that SERP payments should not be capitalized. Ms. Fairchild is currently Vice President, Chief Compliance Officer and Corporate Secretary, Great Plains Energy and KCPL. At page 3 of her rebuttal testimony in Case No. ER-2010-0356 Ms. Fairchild stated:

> While I do have a number of areas of disagreement, <u>I do agree with Mr. Hyneman's rational for not allocating any SERP expense to capital;</u> the reduction of monthly annuities by 20 percent to reflect that some SERP expense was based on bonus payments and incentive compensation which were not included in cost of service; and the exclusion of SERP for former L&P executives and certain former Aquila executives. (Emphasis added)

Q. Is the capitalization of SERP expense a reasonable accounting and ratemaking position?

A. No, it is not reasonable. This argument is contrary to current generally accepted accounting principles (GAAP) theory and is simply not sound ratemaking.

Q. Are you aware of any specific GAAP that provides general guidance on capitalization policies for self-constructed assets for an entity's own use, such as utility construction plant projects?

A. Yes. FASB Accounting Standards Codification ("ASC") is the source of authoritative generally GAAP recognized by the FASB to be applied to nongovernmental entities. FASB's ASC 360-10 ASC 360, Property, Plant, and Equipment, provides guidance on accounting for property, plant, and equipment.

ASC 360-10 states that:

> The basis of accounting for depreciable fixed assets is cost, and all normal expenditures of readying an asset for use are capitalized. However, unnecessary expenditures that do not add to the utility of the asset are charged to expense.

Q. Are the services provided by current utility employees necessary to ready utility construction projects for use in providing utility service?

A. Yes, they are, and therefore the costs of these services should be capitalized to the construction project.

Q. Are the services provided by retired former utility employees necessary to ready utility construction projects for use in providing utility service?

A. No, they are not. Therefore the current expenses for these past services should not be capitalized to current construction projects. This was the policy adopted by both Staff and KCPL in recent cases that, without any reasonable explanation from either party, was suddenly abandoned in this rate case.

Q. Has there been very recent discussions by the Financial Accounting Standards Board on this very issue - capitalization of pension costs?

A. Yes. On January 26, 2016 the FASB recently issued and Exposure Draft titled Proposed Accounting Standards Update, Compensation—Retirement Benefits (Topic 715): Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost (the "ED"). One of the questions for respondents proposed by the FASB was:

> FASB Questions for Respondents
>
> Question 1: Should the service cost component be reported in the income statement apart from the other components of net benefit cost as defined in paragraphs 715-30-35-4 and 715-60-35-9 and be the only component eligible to be capitalized in assets? Why or why not?

PricewaterhouseCoopers LLP's ("PwC") is a large international accounting firm. In its Appendix 1 to PwC's April 26, 2016 letter to the FASB responding to this ED, PwC expressed its agreement that capitalizing only the service cost component of pension expense is a reasonable interpretation of current generally accepted accounting principles on cost capitalization:

> We can understand a view that includes service cost as the only component eligible for capitalization in the cost of assets. Even if service cost is not presented separately in the income statement, we believe that a reasonable interpretation of the cost capitalization guidance in ASC 330 and ASC 360 could nonetheless be limited to the service cost component of net benefit cost.
>
> Asset capitalization guidance is not explicit as to the types of costs to include; the principle is the expenditures and charges incurred in bringing an article to its existing condition and location through current production (ASC 330-10-30-1) or the costs incurred to bring an asset to the condition and location necessary for its intended use (ASC 360-10-30-1).
>
> On balance, given the relatively broad principles-based cost capitalization guidance in ASC 330, Inventory, ASC 350-40, Internal use software, and ASC 360, Property, Plant and Equipment, we would be supportive of providing entities an accounting policy election to capitalize only the service cost component of net periodic benefit cost. [Comment Letter No. 22 File Reference No. 2016-200, April 25, 2016 PricewaterhouseCoopers LLP letter to FASB]

Q. How did Ernst & Young LLP ("EY"), another large accounting firm respond to the FASB's ED?

A. My understanding of EY's letter to the FASB supported the position that only employee service costs rendered in the current period should be capitalized to construction projects of the current period. Payments to former retirees for past services do not meet this standard:

> We support the FASB's objective to improve the reporting of net periodic pension cost and net periodic postretirement benefit cost (net benefit cost) in the financial statements. We agree that only the service cost component of net benefit cost should be eligible for capitalization in assets because this component is directly attributable to employee services rendered in the current period.
>
> [EY April 25, 2016 letter to FASB- Proposed Accounting Standards Update, Compensation — Retirement Benefits (Topic 715): Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost (File Reference No. 2016-200)] (Emphasis added).

Q. Please explain why capitalization of SERP payments is unsound ratemaking.

A. Not all expenses are capitalized to construction projects. Only expenses that provide value or benefit to the construction project should be charged to that project. For example, the cost of paying a SERP retiree in 2016 for utility services performed in 2005 should not be charged to a construction project underway in 2016. That project and the service provided to ratepayers from that current construction project benefits in no way from the payment to that SERP retiree for service rendered 10 years ago.

In addition to this basic ratemaking principle, another regulatory principle that has been recognized by this Commission is referred to as "intergenerational equity." This is a regulatory term used to describe the ratemaking principle that customer rates should be set to reflect an appropriate share of costs for the benefits received.

This ratemaking principle has often been associated with depreciation ratemaking and requires that the generation of customers for whom a particular asset was used to provide service should be the generation from whom the costs of removing that asset is collected. However, the ratemaking principle of intergenerational equity also applies to SERP ratemaking.

SERP cash payments are made to former employees for the service that was provided during the employment of these former employees, sometimes, many years ago. While SERP payments are a retiree compensation expense that must be reflected in the income statement as an expense. Under cash accounting (or pay-as-you-go accounting), that is the nature of the transaction and some intergenerational equity concerns are inevitable.

However, the issue is made worse by accounting treatment that is designed to charge ratepayers many years in the future (over the life of long-lived utility assets) for the employee service provided by utility employees that provided no value to the construction of that utility plant.

Q. How should the Commission address this issue?

A. The Commission should adopt a position that was a former Staff position and a former KCPL position that SERP expenses should not be capitalized to current construction projects for the reasons cited above. The Commission should base this decision based on good accounting methods reflected in GAAP and supported by the FASB and major accounting firms. The Commission should also base its decision on this issue on the ratemaking equity considerations discussed above.

Q. Does this conclude your rebuttal testimony?

A. Yes, it does.

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Utility Regulatory Assessments For U.S. Investor-Owned Utilities

Primary Credit Analyst:
Todd A Shipman, CFA, New York (1) 212-438-7676; todd.shipman@standardandpoors.com

Secondary Contacts:
Barbara A Eiseman, New York (1) 212-438-7666; barbara.eiseman@standardandpoors.com
Gabe Grosberg, New York (1) 212-438-6043; gabe.grosberg@standardandpoors.com
Gerrit W Jepsen, CFA, New York (1) 212-438-2529; gerrit.jepsen@standardandpoors.com
Kyle M Loughlin, New York (1) 212-438-7804; kyle.loughlin@standardandpoors.com
Dimitri Nikas, New York (1) 212-438-7807; dimitri.nikas@standardandpoors.com
Ana M Olaya-Rotonti, New York (1) 212-438-8668; ana.olaya-rotonti@standardandpoors.com
Matthew L O'Neill, New York (1) 212-438-4295; matthew.oneill@standardandpoors.com

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Utility Regulatory Assessments For U.S. Investor-Owned Utilities

In Standard & Poor's Ratings Services' commentary "Assessing U.S. Investor-Owned Utility Regulatory Environments," published on Jan. 7, 2014, on RatingsDirect, we discussed our views on what constitutes a credit-supportive regulatory climate in the U.S.

We use those factors to create assessments of the regulatory environments in jurisdictions that regulate the electric, gas, and water utilities that we rate. We base the assessments on quantitative and qualitative factors, focusing on four main categories: the stability of the basic regulatory paradigm employed in the jurisdiction, tariff-setting procedures, financial stability, and the political independence of the regulator.

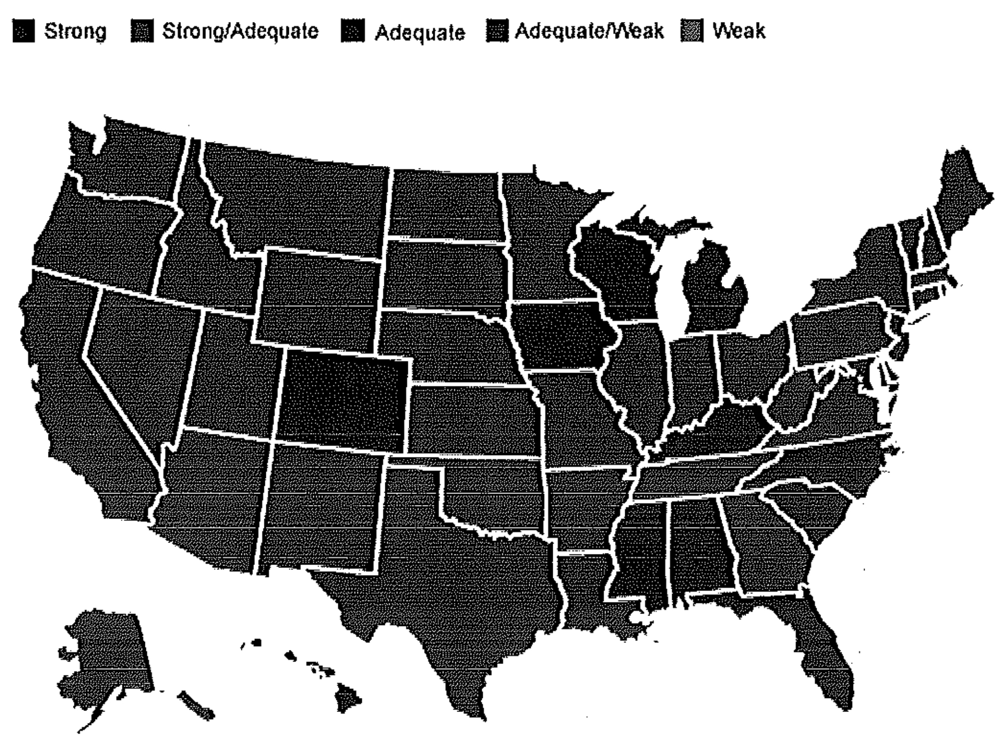
The following table, which lists the jurisdictions in rank order, and map show our updated assessments of regulatory jurisdictions. Since the scale is now global and the categories are different, comparisons to the previous assessments are not valid.

Regulatory Jurisdictions For Investor-Owned Utilities In The U.S.

Strong	Strong/Adequate	Adequate	Adequate/Weak	Weak
U.S. (federal)	California	Hawaii		
Wisconsin	Georgia	Mississippi		
Florida	Louisiana			
Michigan	Minnesota			
Alabama	Oklahoma			
Iowa	Texas (RR Comm.)			
South Carolina	Vermont			
North Carolina	Pennsylvania			
Kentucky	Virginia			
Colorado	Oregon			
	Kansas			
	Tennessee			
	Nevada			
	Maine			
	Utah			
	Wyoming			
	Indiana			
	Arkansas			
	South Dakota			
	Arizona			
	North Dakota			
	Idaho			
	Nebraska			
	New York			
	Illinois			

Regulatory Jurisdictions For Investor-Owned Utilities In The U.S. (cont.)
Ohio
Massachusetts
New Jersey
West Virginia
Rhode Island
Delaware
Alaska
Missouri
Texas (PUC)
Connecticut
District of Columbia
Maryland
Washington
New Mexico
New Hampshire
Montana

Utility Regulatory Assessments—U.S. Investor-Owned Utilities



U.S. (federal) is "Strong" and District of Columbia is "Strong/Adequate."

Related Criteria And Research

Related Criteria

- Criteria | Corporates | General: Corporate Methodology, Nov. 19, 2013
- Criteria | Corporates | Utilities: Key Credit Factors For The Regulated Utilities Industry, Nov. 19, 2013

Related Research

- Assessing U.S. Investor-Owned Utility Regulatory Environments, Jan. 7, 2014