

THE STATE CORPORATION COMMISSION  
OF THE STATE OF KANSAS

Before Commissioners: Chairman Mark Sievers  
Commissioner Ward Loyd  
Commissioner Thomas E. Wright

In the Matter of the Petition of Kansas City )  
Power & Light Company (KCP&L) for )  
Determination of the Ratemaking Principles )  
and Treatment That Will Apply to the ) Docket No. 11-KCPE-581-PRE  
Recovery in Rates of the Cost to be Incurred )  
by KCP&L for Certain Electric Generation )  
Facilities Under K.S.A. 66-1239. )

ORDER GRANTING KCP&L PETITION FOR PREDETERMINATION  
OF RATE-MAKING PRINCIPLES AND TREATMENT

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The above-captioned matter comes before the State Corporation Commission of the State of Kansas (Commission) for consideration and decision. Having reviewed the files and being fully advised of all matters of record, the Commission summarizes the arguments of the parties and finds and concludes as follows:

## I. Executive Summary

1. On February 23, 2011, Kansas City Power & Light Company (KCP&L) filed a Petition for Predetermination pursuant to K.S.A. 2010 Supp. 66-1239 (Petition) asking the Commission to determine rate-making principles and treatment to recover in rates the cost to make environmental upgrades to La Cygne Unit 1 and La Cygne Unit 2 (the La Cygne Project). KCP&L proposed the La Cygne Project to comply with environmental rules that are anticipated to become effective in the future and with the Regional Haze Agreement, which KCP&L entered into with the Kansas Department of Health and Environment (KDHE) as part of the State Implementation Plan currently pending approval by the Environmental Protection Agency (EPA).<sup>1</sup> Kansas Gas and Electric Company (KG&E), a wholly-owned subsidiary of Westar Energy, Inc. (collectively Westar), has a 50% interest in La Cygne and receives 50% of the power generated by the plant to meet the needs of Westar customers for electricity.<sup>2</sup>

2. The Commission must rule on the rate-making principles and treatment proposed by KCP&L within 180 days of the filing of its Application or the rate-making principles and treatment proposed by the utility “will be deemed to have been approved by the commission and shall be binding for rate-making purposes during the useful life of the generating facility[.]”<sup>3</sup> In this proceeding, KCP&L asked the Commission to make five specific rulings to address rate-making principles and treatment. The Commission in this Order makes the following rulings on these five requests:

- (1) The Commission finds the plan selected by KCP&L to retrofit La Cygne Units 1 and 2, as set forth in the La Cygne Project identified in this proceeding and reflected in

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<sup>1</sup> Petition, ¶ 4.

<sup>2</sup> Direct Testimony of Dick F. Rohlf, filed April 15, 2011, pages 2-3 (Rohlf Direct, pp 2-3).

<sup>3</sup> K.S.A. 2010 Supp. 66-1239(d).

KCP&L Exhibit 5, is reasonable, reliable and efficient under K.S.A. 2010 Supp. 66-1239(c)(3).

(2) The Commission finds the estimated cost of \$1.23 billion excluding AFUDC and property tax, as listed by component in KCP&L Staff Exhibit 5, is reasonable and constitutes an “original cost estimate” that is a “definitive estimate” for purposes of examining prudence under K.S.A. 66-128g(b).

(3) The Commission finds that, if the overall cost of the La Cygne Project goes over the “definitive estimate” of \$1.23 billion excluding Allowance for Funds Used During Construction (AFUDC) and property tax, and if KCP&L seeks to recover any excess over the defined estimate from ratepayers, then KCP&L bears the burden of proof to show the amount it seeks to recover from ratepayers is just and reasonable.

(4) The Commission denies KCP&L’s request to implement an environmental cost recovery rider (ECRR) for costs of the La Cygne Project. Furthermore, the Commission finds that Westar will not be allowed to recover costs of the La Cygne Project through its ECRR.

(5) The Commission determines that KCP&L’s cost of capital and rate of return for the La Cygne Project will be the same as that established generally for KCP&L’s overall rate base.

3. Within one year from the effective date of this decision, KCP&L must notify the Commission whether it will proceed with the La Cygne Project.<sup>4</sup>

## **II. Summary of Administrative Proceedings**

### **A. Application under K.S.A. 2010 Supp. 66-1239**

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<sup>4</sup> K.S.A. 2010 Supp. 66-1239(d).

4. A public utility, before undertaking a proposed construction project that can include improvements to an existing generation facility, can ask the Commission to determine rate-making principles and treatment that will apply to recovery in wholesale or retail rates of the cost incurred by the utility. In filing its request, the utility must provide information that includes (A) a description of its conservation measure, (B) a description of its demand side management efforts, (C) its ten-year generation and load forecasts, and (D) a description of “all power supply alternatives considered to meet the public utility’s load requirements.”<sup>5</sup>

5. The Commission must issue an Order setting forth rate-making principles and treatment that will apply to the utility’s stake in the generating facility, which here is the La Cygne Project, “in all rate-making proceedings on and after such time as the generating facility is placed in service[.]”<sup>6</sup> In all subsequent proceedings in which the Commission considers the cost of the utility’s stake in the generating facility, the Commission is required to use the rate-making principles and treatment applicable to the generating facility.<sup>7</sup> The Commission must issue a decision within 180 days of the filing of the petition for predetermination or the rate-making principles and treatment proposed by the utility in its petition will be deemed to have been approved and will be binding for rate-making purposes during the useful life of the generating facility.<sup>8</sup> The deadline for the Commission to file an Order in this proceeding is August 22, 2011. The utility has one year from the effective date of the Order to notify the Commission whether it will construct the generating facility.<sup>9</sup>

6. As described in its Petition and in testimony of its witnesses, KCP&L is preparing to install wet scrubbers, baghouses, and a common dual-flue chimney for La Cygne Units 1 and 2,

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<sup>5</sup> K.S.A. 2010 Supp. 66-1239(c)(2).

<sup>6</sup> K.S.A. 2010 Supp. 66-1239(c)(4).

<sup>7</sup> K.S.A. 2010 Supp. 66-1239(c)(5).

<sup>8</sup> K.S.A. 2010 Supp. 66-1239(c)(6).

as well as a selective catalytic reduction (SCR) system, low-nitrogen oxide (NOx) burners (LNBS) and an over-fire air (OFA) system for La Cygne Unit 2.<sup>10</sup> Necessity of the La Cygne Project is not driven by current environmental rules, regulations and compliance requirements, but by future requirements that will take effect over the next few years; at this time, La Cygne Units 1 and 2 comply with current environmental rules and regulations. Tr. Vol. 4, 1289-96(Ling). KCP&L noted that a timely decision is needed to allow it to begin construction to enable KCP&L to meet its obligations under its Regional Haze Agreement with KDHE and the Collaborative Agreement with the Sierra Club by June 15, 2015<sup>11</sup> and to comply with expected environmental rules and regulations affecting the La Cygne units. KCP&L asserted that a Commission decision that provides certainty about recovery of costs for the La Cygne Project “will significantly improve KCP&L’s ability to attract capital on reasonable terms.”<sup>12</sup> KCP&L presented a brief summary of the facility upgrades and noted those witnesses providing more detailed information in direct testimony submitted with the Petition.<sup>13</sup>

7. KCP&L asked the Commission to make the following five determinations of rate-making principles and treatment in this Order: (1) KCP&L’s decision to construct and install the La Cygne Project is “reasonable, reliable, efficient and, therefore, prudent”; (2) the estimate of \$1.23 billion excluding AFUDC and property taxes (\$281 million KCP&L Kansas jurisdictional share) “is reasonable, reliable and prudent”; (3) amounts in excess of \$1.23 billion (excluding AFUDC and property taxes) if any “will be recoverable subject to further prudence review during

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<sup>9</sup> K.S.A. 2010 Supp. 66-1239(d)-(f).

<sup>10</sup> Heidtbrink Direct, pp 3, 6-10.

<sup>11</sup> The Regional Haze Agreement states the retrofits must be installed “no later than 5 years after approval of the SIP or June 1, 2015, whichever date occurs first.” Because the EPA has not approved the Regional Haze Agreement SIP, June 1, 2015, will come before 5 years after approval of the SIP, making it the deadline for KCP&L to comply with this agreement. Regional Haze Agreement, ¶ 23.E. The Regional Haze Agreement incorporated emission rates, which were slightly lower than the required presumptive level, from the Collaboration Agreement KCP&L reached with Concerned Citizens of Platte County and the Sierra Club. Tr. Vol. 3, 805-06 (Gross).

<sup>12</sup> Petition, ¶ 4.

a future rate proceeding”; (4) use of an environmental cost recovery rider (ECRR) to recover KCP&L’s costs associated with the La Cygne Project “is reasonable and efficient”; and (5) KCP&L’s cost of capital and rate of return, including return on equity (ROE), that is applied to the La Cygne Project will be the same established generally for KCP&L’s overall rate base.<sup>14</sup> The Commission will discuss and rule on each request in this Order.

8. The Commission’s staff (Staff) participated throughout this proceeding. Several parties were allowed to intervene, as follows: Westar Energy and Kansas Gas and Electric Company (Westar), the Citizens Utility Ratepayer Board (CURB), Sierra Club, and Great Plains Alliance for Clean Energy (GPACE) were allowed to intervene without limitations. Kansas Industrial Consumers, Inc. (KIC) was allowed to intervene to the extent it represented interests of its members intervening separately in this docket, which were Spirit AeroSystems, Inc. (Spirit), Goodyear Tire & Rubber Company (Goodyear), Cargill, Incorporated (Cargill), and Hawker Beechcraft Corporation (Hawker Beechcraft).

9. The Commission designated Martha J. Coffman, Advisory Counsel, to serve as the Prehearing Officer in this proceeding.<sup>15</sup> A Prehearing Conference, with Prehearing Officer Coffman presiding, was conducted on March 9, 2011, to establish a procedural schedule. In an Order issued on May 9, 2011, the Commission adopted a procedural schedule and ordered two public hearings be conducted as follows: for KCP&L customers on May 5, 2011, in Overland Park, Kansas, and for Westar customers on May 10, 2011, in Topeka, Kansas.<sup>16</sup> A Prehearing Conference, with Prehearing Officer Coffman presiding, was conducted on July 7, 2011, just prior to the evidentiary hearing to address prehearing matters.

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<sup>13</sup> Petition, ¶¶ 8-10.

<sup>14</sup> KCP&L Post-Hearing Brief, pp 2-3.

<sup>15</sup> Order issued March 2, 2011, ¶ 3.

<sup>16</sup> May 9, 2011 Order, ¶¶ 6, 8.

## **B. Evidentiary Hearing**

10. An evidentiary hearing, with the Commission presiding, was conducted from July 11 through 15, 2011. Staff reported that notice of the evidentiary hearing was contained in the Prehearing Officer's Order Approving Joint Stipulation and Modifying the Procedural Schedule, issued June 3, 2011. Absent objections, the Commission found notice was proper and jurisdiction existed over the parties and the subject matter of this proceeding.<sup>17</sup>

11. Counsel for the parties entered their appearances as follows: Glenda Cafer, Terri Pemberton, Frank A. Caro, Jr., Heather A. Humphrey for Kansas City Power & Light; Robert V. Eye, Holly Bressett, and Douglas Hayes for the Sierra Club; James A. Roth and Cheryl Vaught for GPACE, James P. Zakoura for Kansas Industrial Consumers and certain retail electric service customers; C. Steven Rarrick for Citizens' Utility Ratepayer Board; Martin J. Bregman and Cathryn J. Dinger for Westar Energy, Inc., and Kansas Gas and Electric Company; and Patrick Smith and Andrew Schulte on behalf of the Commission Staff and the public generally.<sup>18</sup>

12. Witnesses testifying live at the hearing were as follows: on behalf of KCP&L Chris B. Giles, Michael W. Cline, Robert N. Bell, Scott H. Heidtbrink, Kevin E. Bryant, George M. McCollister, Wm. Edward Blunk, Burton L. Crawford, and Paul M. Ling; on behalf of Westar John T. Bridson, Bruce Akin, James Haines, and Dick F. Rohlf; on behalf of the Sierra Club William Steinhurst, Jeremy I. Fisher, and Ezra D. Hausman; on behalf of GPACE David A. Schlissel; on behalf of CURB Michael J. Majoros, Jr., Karl Richard Pavlovic, and Andrea C. Crane; and members of the Commission's Utilities Staff Jeffrey D. McClanahan, Adam Gatewood, Michael Deupree, and Robert H. Glass. Thomas Gross, KDHE Bureau of Air, testified at the request of the Commission. Prefiled testimony of two witnesses, KCP&L Witness

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<sup>17</sup> Transcript of Proceedings, taken July 11 to 15, 2011 (Tr.), Volume 1, page 9 (Tr. Vol. 1, 9).

<sup>18</sup> Tr. Vol. 1, pp 2-4, 7-9.

Forrest Archibald and Staff Utilities Witness Michael Wegner, was accepted into the record without objection, but by agreement of the parties these witnesses did not appear for cross-examination.

13. In addition, Staff contracted with Bates White, LLC, an economic and utilities regulatory consulting firm. Four witnesses, Collin Cain, J. Nicholas Puga, Kenneth J. Slater, and Hal. W. Taylor, prefiled testimony, including a report that was a result of their analysis, and also testified as a panel at the hearing. These four witnesses verified a prefiled joint report that had been submitted with the Direct Testimony of one of the Bates White witnesses, but sponsored and adopted by all four witnesses. The Bates White Report constituted individual opinions of each of these four witnesses and acted as their testimony.<sup>19</sup> Also, Staff provided a list identifying which witness was responsible for each part of the Bates White Report.<sup>20</sup> CURB objected to submission of the Bates White Report in lieu of separate testimony by each witness.<sup>21</sup> GPACE and the Sierra Club joined in CURB's objection.<sup>22</sup> CURB also objected to admission of the Report due to errors and unreliability of data upon which it is based, and was allowed to *voir dire* the Bates White witnesses regarding the underlying basis for alternative modeling reflected in the Report.<sup>23</sup> The Commission denied CURB's objections.<sup>24</sup> The Commission reaffirms its decisions. Parties were given an opportunity to cross-examine the four individual witnesses whose opinions and conclusions were stated in the Bates White Report. During cross-examination, parties could direct questions to a specific individual witness or ask questions of the panel as a whole to permit response by the witness most capable of answering the question posed. The Commission finds

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<sup>19</sup> Tr. Vol. 5, 1322-24, 1338 (Cain); 1325-26, 1338 (Puga); 1326-28, 1338 (Slater); 1328-29, 1339 (Taylor).

<sup>20</sup> Tr. Vol. 5, 1331-36 (Smith).

<sup>21</sup> Tr. Vol. 5, 1336-67, 1339 (Rarrick).

<sup>22</sup> Tr. Vol. 5, 1340.

<sup>23</sup> Tr. Vol. 5, 1340-48 (Rarrick).

<sup>24</sup> Tr. Vol., 1340, 1348 (Sievers).



that use of a panel to address these four expert witnesses was particularly helpful, effective, and efficient in conducting this proceeding.

### **C. Administrative Record**

14. The contents of the administrative record in this proceeding are established under the Kansas Administrative Procedure Act (KAPA).<sup>25</sup> All prefiled testimony submitted by witnesses was admitted into the administrative record.<sup>26</sup> Prefiled Direct Testimony was filed on February 23, 2011 by Chris B. Giles, Michael W. Cline, Robert N. Bell, Scott H. Heidtbrink, Kevin E. Bryant, George M. McCollister, Ph. D., Wm. Edward Blunk, Burton L. Crawford, Paul M. Ling, and Forrest Archibald; Rebuttal Testimony was filed on June 24, 2011, by Giles, Cline, Bryant, Blunk, Crawford, and Ling; and Supplemental Rebuttal Testimony on June 30, 2011, by Giles, Crawford, and Paul M. Ling. Prefiled Testimony submitted on behalf of Westar included Directed Testimony filed April 15, 2011, by John T. Bridson, Bruce Akin, James Haines, and Dick R. Rohlf; and Rebuttal Testimony filed on June 24, 2011, by Haines and Rohlf. Prefiled Direct Testimony was filed on June 3, 2011, by witnesses for Intervenors as follows: for the Sierra Club, William Steinhurst, Jeremy I. Fischer, and Ezra D. Hausman; for GPACE, David A. Schlissel; and for CURB, Michael J. Majoros, Jr., Karl Richard Pavlovic, and Andrea C. Crane. Prefiled Cross-Answering Testimony was filed on June 17, 2011, on behalf of Intervenors as follows: for the Sierra Club, Fisher and Hausman; and for CURB, Pavlovic and Crane. Prefiled Direct Testimony was filed on June 3, 2011, by witnesses on behalf of Staff as follows: Jeffrey D. McClanahan, Adam Gatewood, Michael Deupree, Robert H. Glass, J. Nicholas Puga, Collin Cain, Kenneth J. Slater, Hal W. Taylor, and Michael Wegner. Prefiled Supplemental Direct Testimony was filed on June 10, 2011, on behalf of Staff by the following witnesses: Gatewood, Glass,

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<sup>25</sup> K.S.A. 2010 Supp. 77-532.

<sup>26</sup> K.A.R. 82-1-229.

Puga, Cain, Slater, and Taylor. Prefiled Cross Answering Testimony was filed on June 17, 2011, on behalf of Staff by the following witnesses: Gatewood and Deupree. Prefiled Direct Testimony was filed at the request of the Commission on July 12, 2011, by Thomas Gross, KDHE Bureau of Air.<sup>27</sup> In addition, the transcript of the evidentiary hearing is included in the record and will also be cited in this Order.

15. At the conclusion of the evidentiary hearing, the record was left open to receive a document from KCP&L that reflected components and respective costs for the La Cygne Project, which are the basis for the definitive cost estimate of \$1.23 billion. KCP&L submitted Confidential KCP&L Exhibit 5 on July 18, 2011, and adopts this as the original cost estimate, which constitutes a “definitive estimate” for the La Cygne Project.<sup>28</sup> The Commission admits Confidential KCP&L Exhibit 5 into the official administrative record and hereby incorporates KCP&L Exhibit 5 and its contents into this Order. See Attachment A. All parties filed Post-Hearing Briefs and Proposed Findings of Fact and Conclusions of Law on July 25, 2011.

16. The Commission may take official notice of matters that could be judicially noticed in Kansas courts, the record of other proceedings before the Commission, and technical or scientific matters within the Commission’s specialized knowledge.<sup>29</sup> During the evidentiary hearing, the Commission took administrative notice of several documents (all of which were available to the parties), which are listed below.

(a) Regional Haze Agreement between KCP&L and KDHE, signed November 19, 2007, by KCP&L and effective December 5, 2007, after signature of the Secretary of KDHE<sup>30</sup>;

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<sup>27</sup> Tr. Vol. 3, 571 (Gross).

<sup>28</sup> K.S.A. 66-158g(b)(1).

<sup>29</sup> K.S.A. 77-524(f); K.S.A. 60-409; K.A.R. 82-1-230(h).

<sup>30</sup> Tr. Vol. 1, 15.

(b) Environmental Protection Agency's Regional Haze Rule, which requires the state to develop a SIP<sup>31</sup>;

(c) State of Kansas Air Quality State Implementation Plan, Regional Haze, October 26, 2009 (Kansas SIP)<sup>32</sup>;

(d) Order issued November 22, 2010, in Docket 10-KCPE0415-RTS<sup>33</sup>;

(e) Order issued January 5, 2011, in Docket 10-KCPE-415-RTS<sup>34</sup>;

(f) 2011 EIA Annual Energy Outlook 2011, with Projections to 2035, U.S. Energy Information Administration, DOE/EIA-0383 (2011), April 2011<sup>35</sup>;

(g) Kansas Corporation Commission Electric and Natural Gas Billing Standards, effective July 24, 2007, specifically II.B.<sup>36</sup>;

(h) EPA Cross-State Air Pollution Rule, published July 6, 2011 (CSAPR), and the Ozone Season Supplemental Proposal, published July 11, 2011 (OSS Proposal).

17. In addition to the Commission taking official notice of documents, the parties have stipulated that the Collaboration Agreement, executed March 19, 2007, by and between KCP&L, the Sierra Club, and the Concerned Citizens of Platte County, Inc. is relevant and will be admitted into the administrative record of this proceeding.<sup>37</sup>

#### **D. Legal Principles**

18. This proceeding was conducted pursuant to the Kansas Administrative Procedure Act (KAPA).<sup>38</sup> If judicial review of this decision is sought, it will be pursuant to the Kansas

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<sup>31</sup> Tr. Vol. 1, 15.

<sup>32</sup> Tr. Vol. 1, 15.

<sup>33</sup> Tr. Vol.1, 16.

<sup>34</sup> Tr. Vol. 1, 16.

<sup>35</sup> Tr. Vol. 2, 350, Westar Exhibit 1.

<sup>36</sup> Tr. Vol. 4, 874-75.

<sup>37</sup> Tr. Vol. 1, p. 17.

<sup>38</sup> K.S.A. 77-501, *et seq.*

Judicial Review Act (KJRA).<sup>39</sup> The Commission must separately state findings of fact, conclusions of law, and policy reasons for its decision. Any findings of fact must be based exclusively upon evidence in the record and matters officially noticed in this proceeding.<sup>40</sup>

19. The Commission must base any determination of fact upon evidence supported by the appropriate standard of proof that is substantial when viewed in light of the record as a whole.<sup>41</sup> "Substantial, competent evidence" is "evidence which possesses something of substantial and relevant consequence and which furnishes a substantial basis of fact from which the issues tendered can reasonably be resolved."<sup>42</sup> By statute the phrase "in light of the record as a whole" means that the adequacy of evidence in the record to support a particular finding of fact will be judged "in light of all the relevant evidence in the record cited by any party that detracts from such finding as well as all of the relevant evidence in the record compiled pursuant to K.S.A. 77-620, and amendments thereto, cited by any party that supports such finding, including any determinations of veracity by the presiding officer who personally observed the demeanor of the witness and the agency's explanation of why the relevant evidence in the record supports its material findings of fact."<sup>43</sup>

20. In discussing these recent amendments, including adopting K.S.A. 77-621(d) defining "in light of the record as a whole," the Kansas Supreme Court concluded new subsection (d) alters an appellate court's analysis in three ways: "(1) It requires review of the evidence both supporting and contradicting the [agency's] findings; (2) it requires an examination of the presiding officer's credibility determination, if any; and (3) it requires review

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<sup>39</sup> K.S.A. 77-601, *et seq.*

<sup>40</sup> K.S.A. 77-526(c) & (d).

<sup>41</sup> K.S.A. 2010 Supp. 77-621(c)(7).

<sup>42</sup> *Jones v. Kansas Gas & Elec. Co.*, 222 Kan. 390, 397, (1977); *see also Williams Natural Gas Co. v. Kansas Corp. Comm'n*, 22 Kan. App. 2d 326, 334-35 (1996) (review denied).

<sup>43</sup> K.S.A. 2010 Supp. 77-621(d).

of the agency's explanation as to why the evidence supports its findings."<sup>44</sup> The Commission has taken this decision into account in analyzing whether substantial evidence exists in the record as a whole to support its decision on KCP&L's Petition.

21. Under the Kansas rules of evidence, the term "burden of proof" is considered synonymous with "burden of persuasion."<sup>45</sup> The burden of persuasion means a party has an obligation to meet the requirements of a rule of law that the fact to be established must be proven by a requisite degree of belief.<sup>46</sup> In civil cases, the degree of proof is by a preponderance of the evidence, which is the greater weight of evidence, in view of all facts and circumstances of the case.<sup>47</sup> Generally, the burden of proof falls upon the party asserting a point; that party must prove the allegations of its petition by a preponderance of the evidence.<sup>48</sup> The burden of going forward with the evidence is the duty of a party to a case to refute or to explain a particular point, such as the need to make a *prima facie* showing. Finally, the burden of producing evidence is the obligation of a party to introduce evidence sufficient to avoid a ruling against the party on the issue. Under traditional theory, the burden of persuasion does not shift at any stage of the proceeding while the burden of coming forward with the evidence may shift back and forth as the case progresses.<sup>49</sup>

22. The Commission acted as the presiding officer during all evidentiary proceedings.<sup>50</sup> During this week-long evidentiary hearing, 29 witnesses testified in person through cross-examination and answering the Commissioners' questions. Prefiled testimony of two additional witnesses was accepted into the record. Throughout the hearing, the Commission

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<sup>44</sup> *Redd v. Kansas Truck Center*, 291 Kan. 176, 182-83, 239 P.3d 66, 72 (2010).

<sup>45</sup> K.S.A. 60-401(d).

<sup>46</sup> K.S.A. 60-401(d).

<sup>47</sup> *In re Estate of Robinson*, 236 Kan. 431, 439, 690 P.2d 1383 (1984).

<sup>48</sup> 236 Kan. at 439.

<sup>49</sup> Black's Law Dictionary, WEST PUBLISHING CO., 5<sup>th</sup> Ed., p. 178.

<sup>50</sup> K.A.R. 82-1-228.

observed the demeanor of each witness, considered the credibility of testimony on disputed issues presented by each witness, and questioned many of the witnesses directly. This personal observation greatly assisted the Commission in performing its quasi-judicial functions that include judging the relevance and value of testimony and evidence, observing the demeanor and evaluating the credibility of each witness, and weighing and balancing the evidence contained in the record as a whole, both the evidence that supports and that detracts from the positions of the parties on each issue.<sup>51</sup> Use of prefiled testimony allowed an opportunity to understand complex issues involving environmental retrofits and to give thoughtful review and careful analysis to statements by specialized experts before cross-examination.

23. Several witnesses present expert opinion testimony. In hearings before the agency, admission of expert testimony lies within the discretion of the Commission.<sup>52</sup> Facts relied upon by an expert for an opinion should afford a reasonably accurate basis for the conclusion as distinguished from mere guess or conjecture. Expert witnesses generally must confine their opinions to relevant matters that are certain or probable, not those which are merely possible.<sup>53</sup> Evidence regarding expert testimony in the form of opinions or inferences must be limited to opinions that are not only within the scope of the expert's special knowledge, skill, experience, or training, but also must be based on facts or data perceived by or personally known to the witness to be sure an expert has a factual basis for an opinion and can separate opinion from mere speculation.<sup>54</sup>

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<sup>51</sup> *Mobil Exploration & Producing U.S. Inc. v. Kansas Corporation Comm'n*, 258 Kan. 796, 821, 908 P.2d 1276 (1995)(Commission acts in quasi-judicial capacity when weighing evidence and exercising discretion); *In re Tax Appeal of Trickett*, 27 Kan. App. 2d 651, 655-56, 8 P.3d 18 (2000)(discussing quasi-judicial functions of agency). See Black's Law Dictionary, 1121 (5<sup>th</sup> Ed. 1979).

<sup>52</sup> *Kansas Gas & Electric Co. v. Kansas Corp. Comm'n*, 14 Kan. App. 2d 527, Syl. 3, 538, 794 P.2d 1165 (1990).

<sup>53</sup> *State v. Struzik*, 269 Kan. 95, 99, 5 P.3d 502 (2000).

<sup>54</sup> *Kuxhausen v. Tillman*, 291 Kan. 314, 241 P.3d 75, 79 (2010); *State v. Papen*, 274 Kan. 149, 259, 50 P.3d 37 (2002), citing K.S.A. 60-456(b)(1)

24. The Commission must interpret and apply K.S.A. 2010 Supp. 66-1239 and 66-128g in deciding the issues presented in this docket. The fundamental rule of statutory construction, to which all other rules are subordinate, is that the intent of the legislature as expressed in the plain language of the statute controls.<sup>55</sup> If a statute is plain and unambiguous, the Commission will not speculate about the legislative intent behind it and will not read the statute to add something not readily found in it. Only if the statute's language is unclear or ambiguous does the Commission turn to applying canons of construction or rely on legislative history construing the statute to effect the legislature's intent.<sup>56</sup>

### **III. Findings and Conclusions Regarding KCP&L's Application and Requests**

25. At a high level, the Commission is being asked to approve the decision to make environmental upgrades to La Cygne Units 1 and 2 and to pay for the cost of such upgrades to comply with environmental requirements set forth in the Regional Haze Agreement between KCP&L and the Kansas Department of Health and Environment (KDHE) executed on December 5, 2007<sup>57</sup> and other environmental rules and regulations KCP&L expects to affect future operations of the La Cygne units. If pollution limits established in the KDHE agreement are not met by June 1, 2015,<sup>58</sup> KCP&L Witness Heidtbrink testified he must make the call to shut down the La Cygne units and would be personally subject to going to prison or to fines and penalties if the units continued to run.<sup>59</sup>

26. To a large extent, the obligation to retrofit the La Cygne units and reduce emissions is a contractual obligation assumed by KCP&L with the KDHE and the Sierra Club

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<sup>55</sup> *Williamson v. City of Hays*, 275 Kan. 300, 305, 64 P.3d 2003 (2003).

<sup>56</sup> *Double M Construction*, 288 Kan. 268, 271, 202 P.3d 7 (2009).

<sup>57</sup> Regional Haze Agreement, p. 8, ¶ 34. During round one, *i.e.*, the first 10-year period of regulations under the Regional Haze SIP, or until 2018, KCP&L and Westar are the only two companies subject to the emission limits. Under the Regional Haze Agreement KDHE reached with Westar, the emission limits will become effective January 1, 2014. Additional companies may be subject to emission limits under the second round of the Regional Haze SIP. Tr., Vol. 3, 597-99 (Gross).

<sup>58</sup> Regional Haze Agreement, p. 5, ¶ 23.E.

<sup>59</sup> Tr. Vol. 1, 226-27 (Heidtbrink). See Tr. Vol. 3, pp 811-12 (Gross) (KDHE and EPA have authority to shut down La Cygne if emission standards are not met, but it is not clear what actions KDHE will take in the event of noncompliance); Tr. Vol. 4, pp 1205-07 (Ling) (Potential penalty is \$25,000 per day per violation).

and the environmental rules and regulations that will affect the operations of the La Cygne units. The La Cygne units currently meet all of the EPA emissions standards, but the contractual commitments made by KCP&L in both agreements exceed the current EPA emissions standards for such coal-fired units or, in the case of particulate matter in total (PM<sub>10</sub>) create a contractual emission standard that is not currently measured by the EPA.<sup>60</sup> KCP&L Witness Ling testified that, in his opinion, the control equipment being installed at La Cygne will satisfy all the rule makings being anticipated at this time.<sup>61</sup> Also, EPA's release of the Cross-State Air Pollution Rule (CSAPR) makes the need to move with the retrofit project more urgent.<sup>62</sup>

27. The Commission was not presented with nor did it review and/or approve either agreement prior to their execution in 2007. K.S.A. 66-136 states that "No franchise or certificate of convenience and necessity granted a common carrier or public utility governed by the provision of the act shall be assigned, transferred or leased, nor shall any contract or agreement with reference to or affecting such franchise or certificate of convenience and necessity or right there under be valid or of any force or effect whatsoever, unless the assignment, transfer, lease, contract or agreement shall have been approved by the Commission." Certainly, the Commission does not wish to review and approve all contracts and agreements, but this statute was enacted a century ago and is focused on contracts dealing with transfer of utility contracts that affect the utility's franchise, and thus has a purpose. Here there were two contracts -- one with KDHE and the other with the Sierra Club -- one subjecting KCP&L to government enforcement actions (the KDHE contract) and the other to civil penalties (the Sierra Club contract). A contract involving a \$1.23 billion upgrade to a major base-load generating facility where the utility asserts it would have to shut down the plant if it failed to meet the contractual deadline seems to fall into the category of contracts that affect KCP&L franchise or certificate of convenience and necessity. Likewise, the extensive discussion of the environmental upgrades in

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<sup>60</sup> Tr. Vol. 4, 1289-1297 (Ling).

<sup>61</sup> Tr. Vol. 4, 1215, 1230-31, 1233 (Ling).

<sup>62</sup> Tr. Vol. 4, 1216 (Ling).



financial analysts' assessment of KCP&L's financial matters also indicates that the contract is material and affects KCP&L's franchise or certificate of convenience and necessity.<sup>63</sup> The Commission rejects arguments that KCP&L's petition for predetermination should be denied because these agreements were not previously presented to the Commission. Going forward, the Commission concludes contracts that significantly affect a utility's franchise or certificate of convenience and necessity, such as the agreements at issue here, are the type that should be presented to the Commission, not just its Staff. For this reason, the Commission directs Staff to develop a proposal regarding a procedure to be followed to enable review and approval of the type of material contracts entered into by public utilities we regulate.

28. The consequences of breaching or voiding these agreements are unclear. Several KCP&L and Westar witnesses testified unequivocally that the La Cygne units would have to be shut down if KCP&L failed to deploy the Best Available Retrofit Technology (BART) by the contractual due date of June 1, 2015.<sup>64</sup> However, Thomas Gross from KDHE testified that while KDHE has broad enforcement powers, whether KDHE would shut down the La Cygne facility or not remained to be determined.<sup>65</sup> Mr. Gross also testified that the Regional Haze Agreement could be modified.<sup>66</sup> But if the Regional Haze Agreement is modified, Mr. Gross testified the component of the Kansas State Implementation Plan (SIP) associated with this agreement would need to be withdrawn and, because the agreement is such a major component of the SIP, the process for SIP approval would likely start over.<sup>67</sup>

29. The record indicates that the Regional Haze Agreement was entered into by KCP&L and KDHE in order to facilitate KDHE's completion of the SIP to comply with the EPA's federal Regional Haze Rule. The federal Regional Haze Rule is a collection of environmental requirements designed to reduce haze in national parks and wilderness areas.

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<sup>63</sup> Cline Direct, Schedule MWC2011-1, p. 1; Tr. Vol. 2, 314-19 (Cline).

<sup>64</sup> See, e.g., Tr. Vol. 4, 1299-1300 (Ling); Rolfs Direct, p. 7.

<sup>65</sup> Tr. Vol. 3, 652-654 (Gross).

<sup>66</sup> Gross Direct, pp 2-3.

<sup>67</sup> Gross Direct, p. 2; Tr. Vol. 4, 580-81, 638-39 (Gross).

None of the national parks or wilderness areas identified in the Kansas SIP is in Kansas.<sup>68</sup> The Kansas (SIP) has not yet been approved by the EPA.<sup>69</sup> If the Kansas SIP is rejected by the EPA or otherwise found to be wanting, a possible penalty is the EPA imposing a presumably more stringent federal implementation plan (FIP).<sup>70</sup>

30. The Collaboration Agreement with the Sierra Club appears to be an agreement entered into by KCP&L to settle claims alleged in civil lawsuits. Gross testified that the emissions requirements committed to by KCP&L in the Collaboration Agreement were incorporated into the Regional Haze Agreement that KCP&L reached with KDHE.<sup>71</sup> The penalties to be imposed for breaching the Collaboration Agreement and not meeting the proposed emissions limits by the June 1, 2015 due date are unclear.

31. Both the KDHE Regional Haze Agreement and the Sierra Club Collaboration agreements describe Best Available Retrofit Technology (BART) retrofits to the La Cygne units to reduce emissions levels. Neither agreement appears to envision shutting the units down or replacing them with alternative fuels (*e.g.*, natural gas).

32. Along with the Regional Haze Agreement and the Collaboration Agreement, the table below summarizes the environmental rules and regulations KCP&L identified as potentially affecting future operations of the La Cygne facility:

**Environmental Requirements Affecting the La Cygne Station Units**

(Sources: KCP&L Exhibit 1; Bates White Report, p. 54)

Environmental Rule or Contractual Obligation	Description	Final Rule or Action Expected by:	Compliance Date (if any)
KDHE Regional Haze Agreement	Agreement between KCP&L and KDHE to reduce emissions for: (1) Nitrogen Oxides (NO <sub>x</sub> ); (2) Sulfur Dioxides (SO <sub>2</sub> ); and (3) Particulate Matter (PM <sub>10</sub> filterable and PM <sub>10</sub> total). Agreement also requires construction for emissions reductions commence by December 31,	Agreement fully executed on December 5, 2007.	June 1, 2015

<sup>68</sup> Tr. Vol. 3, 654-55 (Gross).

<sup>69</sup> Gross Direct pp. 2-3.

<sup>70</sup> Tr. Vol. 3, 639-40 (Gross).

<sup>71</sup> Tr. Vol. 3, 806 (Gross).

<b>Environmental Rule or Contractual Obligation</b>	<b>Description</b>	<b>Final Rule or Action Expected by:</b>	<b>Compliance Date (if any)</b>
	2011 and Best Available Retrofit Technology (BART) be deployed by June 1, 2015		
Sierra Club Collaboration Agreement	Agreement between KCP&L and the Sierra Club and the Concerned Citizens of Platte County to reduce emissions for: (1) Nitrogen Oxides ( $NO_x$ ); (2) Sulfur Dioxides ( $SO_2$ ); and (3) Particulate Matter ( $PM_{10}$ filterable and $PM_{10}$ total). Agreement also requires construction for emissions reductions commence by December 31, 2011 and Best Available Retrofit Technology (BART) be deployed by June 1, 2015	Agreement executed in March 2007	June 1, 2015
Cross State Air Pollution Rule	$SO_2$ and $NO_x$ reduction for compliance with the National Ambient Air Quality Standards (NAAQS). Creates allowance for certain emissions. Requires installation of baghouse, scrubbers, low $NO_x$ burners, over-fired air and selective catalytic reduction equipment to address expected allowance shortfalls	July 2011	Phase I – 2012 Phase II – 2014
2010 $SO_2$ Standard	Requires reduction in $SO_2$ levels for compliance with NAAQS	June 2010	2017
Industrial Boiler Maximum Achievable Control Technology (MACT)	Requires reduction in hazardous air pollutants	April 2012	2015
Power Plant Mercury and Air Toxics Standards	Requires reduction in hazardous air pollutants	November 2011	2016-2018
2011 Ozone Standard	$NO_x$ reduction for compliance with the NAAQS	July 2011	2017
Clean Water Act Effluent Guidelines	Affects cooling water intake, fish impingement and entrainment	July 2012	2016-2020
Coal Combustion Residuals rule	Disposal and beneficial use of coal combustion residuals	2012	2013-2019

33. Irrespective of contractual obligations to the KDHE and the Sierra Club, KCP&L is still subject to all of the environmental rules and regulations cited by KCP&L, many still being developed. The testimony and evidence in the record was consistent that more, not less, environmental requirements are likely to be enacted that will adversely affect the current

operations of the La Cygne units. Indeed, no witness testified that the environmental rules and regulations would likely be lessened over the next several decades

34. To evaluate alternatives to meet these requirements, KCP&L compared the capital and operating costs of various alternatives for compliance (*e.g.*, retrofit the La Cygne units to reduce emissions, convert La Cygne to a combined cycle plant, etc.) by projecting various future costs of critical components of constructing (retrofit or conversion) and operating the La Cygne units (*e.g.*, coal price, natural gas price, CO<sub>2</sub> cost, financing costs, and retail customer load growth<sup>72</sup>) over more than 20 years and used a simulation model to convert the expected value of those future costs to a present value figure. Using the retrofit alternative as an example, the simulation model used by KCP&L estimated the future costs of operating a retrofitted La Cygne unit by assuming cost projections for critical inputs with differing probabilities. For example, the low projection for future CO<sub>2</sub> prices was assigned a 25% probability, whereas the high price projection for financing costs was assigned a 33% probability and the medium price projection for coal costs was assigned a probability of 50%. Using that analytical process, KCP&L concluded that retrofitting the La Cygne units was the least cost (most efficient) alternative.<sup>73</sup>

35. KCP&L's determination that retrofitting the La Cygne units, with the Best Available Retrofit Technology (BART), was also supported by independent analyses performed by Westar and Bates-White using different analytical approaches. No other party presented comparable analysis or other evidence that showed any alternative configuration being a lower cost alternative to retrofitting the La Cygne units.

36. Thus, in addition to estimating the cost of satisfying the Regional Haze Rule, this matter involves a projection by KCP&L about future environmental rules and regulations and numerous very long term projections about future prices of critical components of the future operating costs of the La Cygne units in different configurations. It is not unreasonable to expect experts to disagree about the price path of any of the critical components, to disagree with the

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<sup>72</sup> Tr. Vol. 4, 980 (Crawford).

<sup>73</sup> Tr. Vol. 4, 1151 (Crawford).

technical details of how they are combined in a complex simulation model, and to disagree about future environmental regulations. At its core, this effort is fraught with unknowns and uncertainty. As Westar witness Haines testified “There is no business decision of any consequence that I am aware of that is ever made with complete information. There's always incomplete information.”<sup>74</sup> Likewise GPACE’s witness Schlissel testified, “... a long term forecast is basically unreliable once you’ve said it.”<sup>75</sup> The complaints raised by the parties about the decision-making process used by KCP&L boiled down to:

- Was the future price projection for various components reasonable (*e.g.*, was the price series of natural gas used in the model too high and, thus, unreasonable because it was biased against alternatives that relied on natural gas)?
- Was the probability assigned to a particular future price projection of a critical component reasonable (*e.g.*, was the 25% probability assigned to the low price of future CO<sub>2</sub> prices (equal to zero) too high a probability)?
- Was the range of alternatives considered and modeled by KCP&L reasonable (*e.g.*, was the modeling effort unreasonable because KCP&L did not consider simply shutting down the plants and making up generation needs entirely through demand side management and purchased power)?
- Was the modeling used by KCP&L technically unreasonable because it did not account for interdependencies between the future prices of critical components (*e.g.*, if the price of natural gas and the price of CO<sub>2</sub> are correlated, then should the model select these price paths to reflect the correlation and not assume they are independent)?

37. Westar used two different approaches to evaluate the La Cygne decision. The first approach investigated the impact on the present value of revenue requirement (PVRR) and the impact on the retail energy cost adjustment (RECA).<sup>76</sup> Westar estimated PVRR using a financial

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<sup>74</sup> Tr. Vol. 4, 1044 (Haines).

<sup>75</sup> Tr. Vol. 2, 507 (Schlissel).

<sup>76</sup> Akin Direct, p. 3.

model, while the RECA analysis, because it incorporates asset-based off-system sales, required the use of a dispatch model. On a levelized basis, Westar concluded that the PVRR analysis shows that retrofitting La Cygne is the least cost option.<sup>77</sup> Similarly, the RECA analysis shows the operational costs of running La Cygne are less than the operational costs of a generic combined cycle.<sup>78</sup> Thus, the PVRR/RECA analysis shows that, for the Westar Service Area, retrofitting La Cygne is the least cost decision.

38. Nonetheless, Westar points out that “the PVRR and RECA analysis do not take into account the impacts of fuel price volatility and assume that the relationship among the inputs remains constant.”<sup>79</sup> Therefore, the second approach used by Westar, the Real Options Analysis, takes historical fuel data and estimates fuel price volatility, and then estimates the impact on customers of this fuel price volatility in either the retrofit La Cygne case or the replace La Cygne with a combined cycle case. The results show overwhelmingly that the retrofit option is the best for Westar consumers when fuel price volatility is taken into account.<sup>80</sup>

39. Bates White used a production cost and dispatch model to independently evaluate the La Cygne retrofit proposal.<sup>81</sup> Based on its analysis, Bates White concluded that CO<sub>2</sub> is the dominant risk affecting the retrofit decision.<sup>82</sup> Using PROMOD IV power system analysis software, Bates White simulated the Eastern Interconnection and conducted sensitivity analysis to assess the impact of CO<sub>2</sub> prices on economic viability of retrofitting La Cygne.<sup>83</sup> Like KCP&L and Westar, Bates White concluded that the La Cygne retrofit is the least-cost option.<sup>84</sup>

40. The Commission concludes that, based on the evidence presented in this matter, KCP&L’s modeling effort and conclusion to retrofit the La Cygne units is reasonable, reliable and efficient. While concerns were expressed regarding some assumptions made in KCP&L’s

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<sup>77</sup> Akin Direct, p. 12, Table 3.

<sup>78</sup> Akin Direct, p. 13, Table 4.

<sup>79</sup> Akin Direct, p. 14.

<sup>80</sup> Akin Direct, pp. 14-16, and especially p. 16, Table 5.

<sup>81</sup> Bates White Report, pp 43-43, Exhibit BW-1.

<sup>82</sup> Bates White Report, p. 65.

<sup>83</sup> Bates White Report, ¶ 4, Exhibit BW-1S.

<sup>84</sup> Bates White Report, pp 640-68, Exhibit BW-1, and ¶¶ 40-41, Exhibit BW-1S, ¶¶ 40-41.

modeling for the La Cygne Project, witnesses during the hearing discussed in detail the planning process that went into the modeling. KCP&L's management is not required to be perfect, just prudent. The Commission concludes that none of the challenges made to KCP&L's proposed project rose to a level that would invalidate the decision reached by KCP&L, namely that a retrofit of the La Cygne units was the least cost (*i.e.*, efficient) alternative. Indeed, KCP&L's retrofit conclusion was validated by Westar and Bates-White, which used different simulation models and different price projections, but nevertheless concluded that a retrofit was the least cost alternative.

#### **A. Filing Requirements for a Predetermination Petition**

41. A public utility is allowed to petition the Commission before undertaking construction of a "generating facility" for a determination of rate-making principles and treatment as proposed by the utility "that will apply to recovery in wholesale or retail rates of the cost to be incurred" by the utility to acquire the utility's stake in the generating facility "during the expected useful life of the generating facility[.]"<sup>85</sup> The statute applies to the proposed environmental upgrades proposed for La Cygne under the definition of "generating facility" that includes any improvement to an existing generation facility.<sup>86</sup> When a utility requests a predetermination of rate-making principles and treatment, certain information must be submitted as part of its filing.<sup>87</sup> The Commission will examine whether KCP&L met these filing requirements.

42. Conservation measures and demand side management (DSM) efforts, K.S.A. 2010 Supp. 66-1239(c)(2)(A) & (B): When filing a predetermination request, the utility must submit a description of its conservation measures, K.S.A. 2010 Supp. 66-1239(c)(2)(A), and its demand side management (DSM) efforts.<sup>88</sup> KCP&L Witness Kevin Bryant addressed these issues in testimony filed with the Petition.<sup>89</sup> Sierra Club witnesses William Steinhurst and Ezra D. Hausman asserted that KCP&L did not adequately consider additional investment in demand-side

<sup>85</sup> K.S.A. 2010 Supp. 66-1239(c)(1).

<sup>86</sup> K.S.A. 2010 Supp. 66-1239(a)(3).

<sup>87</sup> K.S.A. 2010 Supp. 66-1239(c)(2).

<sup>88</sup> K.S.A. 2010 Supp. 66-1239(c)(2)(B).

<sup>89</sup> Bryant Direct, pp 3-27; Bryant Rebuttal, pp 2-8.

resources as a low-cost, low-risk option to match supply with demand and suggested KCP&L rejected DSM as an alternative to the La Cygne retrofits without examining and modeling possible DSM resources.<sup>90</sup> KCP&L Witness Burton L. Crawford countered Hausman's suggestion, stating that KCP&L analyzed a reasonable range of DSM levels in its analysis that included a level of DSM that would be nearly sufficient to replace one La Cygne unit. Even with this aggressive level of DSM, the outcome in those scenarios still pointed to retrofitting La Cygne as the least cost alternative.<sup>91</sup>

43. The Sierra Club's witness, Dr. Hausman testified that while he has been involved in many utility cases, he was aware of no state where a large coal-fired plant was retired due to DSM efforts. He also testified that an aggressive DSM plan reduces demand by, at best, only one or two percent annually.<sup>92</sup> Based on his experience with other commissions, the Commission finds Dr. Hausman's testimony to be credible on this issue and concludes that the potential savings from DSM programs to be *de minimus* relative to the capacity associated with the La Cygne units.

44. Staff Witness Michael Deupree reviewed KCP&L's conservation and DSM, noting the statute merely requires a utility to describe its conservation measures and DSM efforts in its filings and no Commission action is necessary.<sup>93</sup> Regarding Sierra Club's proposal to use DSM in lieu of retrofitting La Cygne, even if KCP&L has pursued all economical DSM potential, the effects would have been minimal and "[c]ertainly not enough to assuage a decision affecting two base-load coal unit[s] with a combined capacity of 1,418 MWs."<sup>94</sup>

45. The Commission finds that KCP&L complied with the requirements of the statute by submitting a description of its conservation measures and DSM efforts. The Commission has considered this information in deciding the utility's requests. The Commission rejects the Sierra

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<sup>90</sup> Tr. Vol. 2, 540-42, 547-48, 550-53 (Steinhurst); Hausman Direct, 17; Tr. Vol. 2, 425-31, 434 (Hausman).

<sup>91</sup> Crawford Rebuttal, pp 2-4. See Bryant Rebuttal, pp 2-3 (KCP&L analyzed a reasonable range of DSM levels and retrofit was still the least cost alternative with more aggressive DSM).

<sup>92</sup> Tr. Vol. 2, 447-450 (Hausman).

<sup>93</sup> Deupree Direct, pages 7-8, 11-15.

<sup>94</sup> Deupree Cross-Answering, pages 2-3.



Club's argument that KCP&L's analysis of the La Cygne Project should be rejected for not adequately considering more aggressive DSM efforts in part because this is not a valid reading of the statute and the obligation imposed on an applicant and in part because the Sierra Club presented no credible evidence of aggressive DSM efforts that could be used to offset the loss of the 1,418 MW of base-load generation provided by La Cygne.<sup>95</sup> Also, the Sierra Club did not address the impact this would have on Westar customers given Westar's contractual terms involving the La Cygne units.<sup>96</sup>

46. KCP&L's ten-year generation and load forecasts, K.S.A. 2010 Supp. 66-1239(c)(2)(C): KCP&L Witness George M. McCollister presented KCP&L's 10-year load forecast used in this case to determine the need for generation resources to meet future load growth. He explained a forecast is developed for each class of customers in Kansas and in Missouri.<sup>97</sup> The forecast of annual net system input and peak demand for KCP&L customers in each state from 2010 through 2020 is shown in Schedule GMM2011-1, attached to his testimony.<sup>98</sup> No party contested this matter. The Commission finds KCP&L complied with the requirement to present the utility's ten-year generation and load forecasts.

47. All power supply alternatives considered to meet the utility's load requirements, K.S.A. 2010 Supp. 66-1239(c)(2)(D): With its predetermination filing, a utility must include a description of all power supply alternatives considered to meet the utility's load requirements. KCP&L Witness Crawford provided this information, explaining that the process used to evaluate KCP&L's long-term resource plan alternatives is based on the electric integrated resource plan (IRP) procedures required by Missouri. Initially a number of preliminary options for environmental compliance, system generation and DSM/energy efficiency programs are screened, which reduces the options included in evaluating the expected cost of alternative resource plans. These plans are evaluated in a production cost model called MIDAS™ to calculate each plan's

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<sup>95</sup> Tr. Vol. 4, 1135-39 (Crawford).

<sup>96</sup> Rohlfs Direct, pp 3-9.

<sup>97</sup> McCollister Direct, pages 2-3.

<sup>98</sup> McCollister Direct, page 5.

expected total revenue requirement over a number of years. Calculations are performed for each alternative resource plan under a variety of potential scenarios to determine the level of risk each alternative plan faces. Here the modeling devised 64 scenarios to gauge the risk associated with identified critical uncertain factors. The result is a series of alternative long-term resource plans with an expected 25-year net present value of revenue requirements (NPVRR) that takes into account the risk associated with critical uncertainty factors in the industry.<sup>99</sup> In his testimony, Crawford describes the screening process and the MIDAS™ model in detail, including major assumptions used in the model.<sup>100</sup> Fourteen alternative resource plans were considered with four additional sensitivity scenarios.<sup>101</sup>

48. It is important to note that K.S.A. 2010 Supp. 66-1239(c)(2)(D) does not require a utility to consider all possible power supply alternatives, but simply to provide a description of “all power supply alternatives considered to meet the public utility’s load requirements.” In this matter, given the modeling approach applied, KCP&L examined 18 different resource plans with 64 scenarios even though more plans and scenarios were theoretically possible. As CURB notes in its brief, the differences between the NPVRR produced by the scenarios was often small.<sup>102</sup> But other than rejecting KCP&L’s application outright – and subjecting the public to the consequences (and costs) of non-compliance with the host of environmental rules and regulations described in this proceeding – CURB and its witnesses (none of whom described any significant experience in power plant retirement or retrofit cases) does not offer better credible alternatives than the approach taken by KCP&L and Bates White in analyzing the retrofit decision presented in this case.

49. Several parties contested the adequacy of the analysis conducted by KCP&L in determining the extent and number of power supply alternatives to consider in evaluating the question of whether to retrofit the La Cygne units.<sup>103</sup> The Commission will discuss some of those

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<sup>99</sup> Crawford Direct, pp 4-5, and Confidential Schedule BLC2011-10.

<sup>100</sup> Crawford Direct, pp 6-8.

<sup>101</sup> Crawford Direct, p. 9, and Confidential Schedule BLC2011-13.

<sup>102</sup> CURB Post-Hearing Brief, p. 18.

<sup>103</sup> Tr. Vol. 2, 497 (Schlissel) (KCP&L should have looked at a wider range of alternatives).

criticisms in evaluating the strength of the evidence addressing whether KCP&L's proposed plan to retrofit La Cygne is reasonable, reliable, and efficient. Here, the Commission finds KCP&L complied with the requirement to submit with its Petition a description of "all power supply alternatives considered to meet the public utility's load requirements."<sup>104</sup> Thus, the Commission finds KCP&L met all initial filing requirements.<sup>105</sup>

50. Before examining each determination requested by KCP&L, the Commission notes that KCP&L has argued that, if its petition is denied, this will be a rejection of its proposal and will cause KCP&L to reject or abandon the La Cygne Retrofit Project.<sup>106</sup> Inasmuch as KCP&L and Westar have determined by their respective models that this Project is the least cost alternative available to make the environmental improvements required under KCP&L's Haze Agreement with KDHE, and both companies have made it abundantly clear throughout this hearing that neither can afford to go without the capacity and energy provided by La Cygne, the Commission finds this position disingenuous. Depending upon the reasons for denial, more probably these utilities would retrofit La Cygne as proposed here and request, after completion of the retrofit and in the context of a new rate case, that the retrofit costs be included in rate base.

#### **B. KCP&L's Proposed Plan to Retrofit La Cygne**

51. The predetermination statute provides that, in considering a public utility's supply plan, the Commission "may consider if the public utility issued a request for proposal from a wide audience of participants willing and able to meet the needs identified under the public utility's generating supply plan, and if the plan selected by the public utility is reasonable, reliable and efficient."<sup>107</sup> The Sierra Club argued KCP&L should have reviewed additional alternatives beyond the plan KCP&L selected.<sup>108</sup> Staff disagreed with the Sierra Club, noting subsection (c)(2)(D) uses the term "power supply alternatives" to differentiate the plan being proposed by the

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<sup>104</sup> K.S.A. 2010 Supp. 66-1239(c)(2)(D).

<sup>105</sup> K.S.A. 2010 Supp. 66-1239(c)(2).

<sup>106</sup> Giles Reb., p. 4; Tr. Vol. 1, 148-49 (Giles).

<sup>107</sup> K.S.A. 2010 Supp. 66-1239(c)(3).

<sup>108</sup> Tr. Vol. 2, 528-29 (Steinhurst).

utility in seeking predetermination under the statute.<sup>109</sup> KCP&L asserted the evidence established that its decision to undertake the plan to retrofit La Cygne Units 1 and 2 was reasonable, reliable and efficient, and thus was prudent.<sup>110</sup>

52. The predetermination statute refers to “power supply alternatives” in subsection (c)(2), to “public utility’s supply plan,” “public utility’s generating supply plan,” and “the plan selected by the public utility” in subsection (c)(3), and to an “alternative supply plan” in subsection (f). Although defining several other terms in K.S.A. 2010 Supp. 66-1239(a), these terms are not defined. Because the plain meaning of the statute cannot be understood on its face, the Commission has turned to the legislative history to seek an understanding of the Legislature’s intent in enacting this statute.<sup>111</sup> When this bill was pending before the Senate Utilities Committee, testimony was submitted by several proponents. L. Earl Watkins, Executive Vice President and General Counsel to Sunflower Electric Power Corporation, which proposed the bill, stated the bill was intended to “improve the electric power supply and delivery systems in Kansas” and “to provide a level of comfort to the credit ratings agencies, the capital markets, and the utility, all before a firm commitment is made by a utility to a project.”<sup>112</sup> Bruce Graham, Vice President of Kansas Electric Power Cooperative, Inc. (KEPCo), noted, “The power supply market is changing very quickly and dramatically” and “this bill simply sends a message to the markets that the project is necessary and asks the KCC to state what they [sic] will expect from the utility in order to recover the cost of the project from ratepayers.”<sup>113</sup> On behalf of KCP&L, Tim Rush, Director, Regulatory Affairs, testified the statute “is about ensuring electric utilities can get the

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<sup>109</sup> Staff Proposed Findings of Fact, ¶¶ 9-10.

<sup>110</sup> KCP&L Post-hearing Brief, pp 6-7.

<sup>111</sup> 288 Kan. at 271.

<sup>112</sup> Testimony Submitted to the Kansas Senate Utilities Committee in support of Senate Bill 104, by L. Earl Watkins, Executive Vice President and General Counsel, Sunflower Electric Power Corporation, February 17, 2003, pages 1, 4 (Watkins Testimony, pp 1, 4.).

<sup>113</sup> Testimony on Senate Bill 104, Senate Utilities Committee -- February 17, 2003, by Bruce Graham, Vice President of Member Services and External Affairs, Kansas Electric Power Cooperative, Inc. (KEPCO), page 1 (Graham Testimony, p. 1).

lowest possible interest rates on the financing required to construct or improve utility generation[.]”<sup>114</sup>

53. After taking into account the stated purpose of the predetermination statute by proponents presented to the Kansas Legislature, the Commission concludes the requirement in subsection (c)(2)(D), for the utility to include in its petition for predetermination a “description of all power supply alternatives considered to meet the public utility’s load requirements,” is unrelated to the references to a “plan” in subsection (c)(3).<sup>115</sup> Subsection (c)(3) states what the Commission “may consider” regarding a utility’s chosen supply plan; thus, subsection (c)(3) does not relate to all other power supply alternatives presented under subsection (c)(2)(D). With this understanding of the predetermination statute in mind, the Commission will first consider evidence in the record as a whole to decide if KCP&L’s proposal is reasonable, reliable and efficient under K.S.A. 66-1239(c)(3). Then the Commission will address the issue of prudence.

54. *Reasonable.* In determining whether KCP&L’s proposed plan is reasonable, the Commission should consider whether the plan is fair, proper, or moderate under the circumstances or “is according to reason.”<sup>116</sup> The Commission is aware that at least three significant bodies of regulations currently affect La Cygne, including the Regional Haze Rule, the National Ambient Air Quality Standards (NAAQS) and the Acid Rain Program.<sup>117</sup> The Regional Haze Agreement that KCP&L entered with KDHE was included as part of the State Implementation Plan (SIP) that KDHE submitted to the Environmental Protection Agency (EPA); this SIP is waiting for EPA approval.<sup>118</sup> KDHE elected to negotiate agreements with KCP&L and Westar as a preferable method by which to draft a SIP, inasmuch as it would be based upon the

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<sup>114</sup> Testimony before the Senate Committee on Utilities In General Support of Senate Bill No. 104, by Tim M. Rush, Director, Regulatory Affairs, Kansas City Power & Light Company, February 17, 2003, page 1 (Rush Testimony, p. 1).

<sup>115</sup> Staff Post-Hearing Brief, pp 1-2.

<sup>116</sup> Blacks’ Law Dictionary, 8<sup>th</sup> Ed., p. 1293; Tr. Vol. 1, p. 186 (Sievers); Tr. Vol. 2, 529-30 (Steinhurst) (“reasonable” includes a decision by a utility manager diligently fulfilling his responsibility to provide a public service under sound and economical management based on what is known at the time).

<sup>117</sup> Ling Direct, p. 4.

<sup>118</sup> Gross Direct, at 2.

individual needs of the company.<sup>119</sup> When approved by the EPA, the SIP will be enforceable law that the KDHE may enforce with fines, injunctive relief, and criminal prosecution.<sup>120</sup> Thus, under the Regional Haze Agreement, KCP&L is obligated to meet environmental requirements for La Cygne Units 1 and 2 by June 1, 2015, or it faces the possibility of penalties being imposed.<sup>121</sup>

55. KCP&L Witness Giles acknowledged that the utility planning process is fraught with uncertainty, but Giles testified, “Today sitting where we sit, [retrofitting La Cygne] appears to be [] the least cost alternative given all the assumptions.”<sup>122</sup> KCP&L’s decision to retrofit La Cygne was subjected to extensive analysis by KCP&L,<sup>123</sup> by Westar,<sup>124</sup> and by Staff through the Bates White Report.<sup>125</sup> The analysis by each of these entities reached the same conclusion -- that KCP&L’s decision to retrofit La Cygne as proposed in this proceeding was the least cost option to comply with environmental obligations and to meet KCP&L’s and Westar’s supply obligations. Based upon Commission review and consideration of the modeling undertaken by KCP&L, Westar, and Bates White, the Commission finds evidence in the record as a whole establishes that KCP&L’s plan to retrofit La Cygne Units 1 and 2 is reasonable.

56. Reliable. KCP&L argued the crux of the reliability determination in this proceeding is how to reliably address future risk.<sup>126</sup> Staff defined reliability differently by reference to the North American Electric Reliability Corporation (NERC) mandates which define “reliability” in terms of “adequacy” and “security.” Under NERC’s definitions, adequacy means the ability to supply the aggregate electrical demand and energy requirements of the customers at

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<sup>119</sup> Tr. Vol. 3, 598-603 (Gross). Mr. Gross made clear his opinion that if KDHE had not drafted and submitted a SIP for EPA approval, the EPA would have imposed a Federal Improvement Plan (FIP) upon the state. A subsequent review of the CSAPR reflects that the rules as issued, including the Ozone Season Supplemental Proposal that is to be deemed finalized by October 31, 2011, are in fact a FIP imposed upon Kansas notwithstanding any provisions in the referenced SIP that may appear to be to the contrary. See Tr. Vol. 3, 639-40 (Gross).

<sup>120</sup> Tr. Vol. 3, 652-53, 811-12 (Gross).

<sup>121</sup> Tr. Vol. 3, 576-77 (Gross).

<sup>122</sup> Tr. Vol. 1, 193 (Giles).

<sup>123</sup> Crawford Direct, pp 4-14 (cost analysis of 15 different resource plan alternatives, with an additional 4 sensitivity plans, running numerous scenarios for each plan under various assumptions regarding future reasonably possible events). *Infra*, ¶¶ 34-36.

<sup>124</sup> Akin Direct, pp 2-3, 17 (Westar’s analysis corroborates KCP&L’s analysis by using a different approach resulting in the same conclusions); Tr. Vol. 1, p. 1; Bridson Direct, p. 9. *Infra*, ¶¶ 37-38.

<sup>125</sup> Bates White Report, pp 42-43. *Infra*, ¶ 39.

<sup>126</sup> KCP&L Post-Hearing Brief, ¶ 17, *citing* Tr. Vol. 2, 507 (Schlissel).

all times; security means the ability to withstand sudden disturbances, such as electric short circuits or unanticipated loss of system elements.<sup>127</sup>

57. Both KCP&L and Westar rely upon the energy produced at La Cygne to meet their obligations to service customers in Kansas.<sup>128</sup> In explaining why KCP&L's proposal to retrofit the La Cygne Units should be considered reliable, KCP&L Witness Giles noted these two 700-megawatt coal units produce power 80 percent of the time. Because they are always running, power from these units is available to use for customers or to sell on the wholesale market, which also benefits customers.<sup>129</sup> The Sierra Club argued that KCP&L did not adequately consider the possibility of using wind power as an alternative resource.<sup>130</sup> The Commission is aware that wind is an intermittent resource that cannot be considered a reliable substitute for the energy and capacity produced by La Cygne.<sup>131</sup> For this reason, the Commission finds no credibility to the suggestion that any renewable energy, given current technology availability, is a reasonable substitution for base-load generation.

58. GPACE criticized KCP&L for not adequately taking into account low natural gas prices when analyzing whether natural gas turbines could be a reliable alternative resource to retrofitting La Cygne and for not rerunning its model using more current, and even lower, natural gas prices.<sup>132</sup> Although currently the price of natural gas is low, the Commission notes that historically the price of natural gas has proven to be very volatile.<sup>133</sup> GPACE Witness Schlissel expressed his opinion that domestic and international demand for Powder River Basin (PRB) coal could increase dramatically, causing its price to increase.<sup>134</sup>

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<sup>127</sup> Staff Post-Hearing Brief, ¶ 16, *citing* <http://22.nerc.com/page.php?cid-1/15/123>.

<sup>128</sup> Heidtbrink Dir., p. 4 (La Cygne units provide 27% of KCP&L entire coal fleet MWh generation); Bridson Dir., p. 3 (Westar needs La Cygne capacity to meet the need of Westar customers and maintain capacity margins required by SPP); Glass Dir., pp 3-4. See Tr. Vol. 4, 878 (Povlavic) (agrees KCP&L needs amount of capacity and energy provided by La Cygne).

<sup>129</sup> Tr. Vol. 1, 187 (Giles).

<sup>130</sup> Sierra Club Post-Hearing Brief, p. 6; Tr. Vol. 4, 1135-39 (Crawford).

<sup>131</sup> Tr. Vol. 1, 187 & 205 (Giles); Tr. Vol. 5, 1469 (Slater); Tr. Vol. 5, 1512-13 (Akin).

<sup>132</sup> Tr. Vol. 2, 472 (Schlissel). See, Tr. Vol. 2, 455 (Hausman) (natural gas prices is a major uncertainty factor).

<sup>133</sup> Tr. Vol. 1, 187 (Giles); Blunk Direct, pp 7-10 (natural gas prices are volatile and uncertain).

<sup>134</sup> Schlissel Direct, p. 21; Tr. Vol. 2, 472-74, 495 (Schlissel).

59. KCP&L pointed out that another risk factor is the uncertainty surrounding future CO<sub>2</sub> costs. Numerous witnesses discussed this issue.<sup>135</sup> The variety of views reflected in the record regarding future CO<sub>2</sub> costs illustrate any predictions or forecasts of future CO<sub>2</sub> prices rely upon speculation about what Congressional legislation might be enacted regarding CO<sub>2</sub>.<sup>136</sup> The Commission cannot speculate about what Congress may do or what the law may become, and we refuse to do so. Instead, our obligation is to apply the law as it exists before us in deciding the Application pending before us.

60. In considering whether KCP&L's plan to retrofit La Cygne Units 1 and 2 is reliable, the Commission has taken into account the uncertainty surrounding future CO<sub>2</sub> prices, the historical volatility of natural gas prices, the need for "always on" electric power generating facilities, and the intermittent nature of wind. The Commission has also reviewed modeling of different scenarios by KCP&L, Westar, and Bates White. The Commission concludes KCP&L's plan to retrofit La Cygne is reliable.

61. *Efficient.* KCP&L argued that efficiency relates to "productive efficiency" or "technical efficiency" that involves finding the best set of resources and operational configuration to meet specified constraints. KCP&L also pointed out that regulated utilities must make forward-looking supply decisions without perfect knowledge of future conditions. Thus, an efficient choice would be "the option that is the least cost alternative from a range of alternatives under consideration, assuming the options assessed all of the constraints and the associated uncertainty."<sup>137</sup> Staff added that "societal efficiency" also plays a role and arises when societal benefits to both public and private interests are greater than the overall societal costs. According to Staff, the EPA quantifies societal costs by setting emission standards that cause costs to meet

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<sup>135</sup> Tr. Vol. 2, 454 (Hausman) (carbon regulation will be intended to actually reduce emissions); Tr. Vol. 2, 484-87 (Schlissel) (no evidence imposition of a CO<sub>2</sub> regime would have an impact on natural gas prices); Tr. Vol. 3, 666-68, 704-07 (Blunk) (discussing correlation between natural gas and coal and between natural gas and CO<sub>2</sub> costs); Crawford Direct, pp 12-13 (best to model natural gas and CO<sub>2</sub> prices independently).

<sup>136</sup> Tr. Vol. 4, 889 (Pavlovic).

<sup>137</sup> KCP&L Post-Hearing Brief, p. 10, *citing* Tr. Vol. 1, 188 (Giles).



those standards, which are reflected in the modeling that found retrofitting La Cygne to be productively efficient as the least cost alternative.<sup>138</sup>

62. KCP&L argued the result of its modeling demonstrated that the La Cygne Project is the most efficient option available for KCP&L and Westar to meet their legal obligations. KCP&L modeled 18 different alternative resource plans, each with 64 scenarios that factored in various levels of uncertainty. The conclusion reached was the La Cygne Project was the least cost and, therefore, efficient.<sup>139</sup> Staff pointed out that its consultant Bates White relied upon its own independent analysis of the modeling and projections needed to determine if retrofitting La Cygne Units 1 and 2 was the least cost alternative. Like KCP&L, Bates White concluded the plan to retrofit La Cygne was the least cost alternative.<sup>140</sup> Westar applied a different method of modeling and used different assumptions in analyzing potential alternatives to retrofit La Cygne Units 1 and 2. The modeling by Westar also found the least cost option was KCP&L's plan to retrofit La Cygne.<sup>141</sup> The Commission finds KCP&L's plan to retrofit La Cygne Units 1 and 2 is efficient. Thus, the Commission concludes KCP&L's La Cygne Plan is reasonable, reliable and efficient under K.S.A. 66-1239(c)(3).

63. Prudence. KCP&L argued that, if the La Cygne Project is reasonable, reliable, and efficient under K.S.A. 66-1239(c)(3), the Commission will necessarily find the La Cygne Project is prudent.<sup>142</sup> KCP&L asked the Commission "to determine the prudence of both: (1) the decision to move forward with this project, *i.e.*, the reasonableness of the project itself, and (2) the cost of the project."<sup>143</sup> As support, KCP&L cites the prudence statute at K.S.A. 66-128g, which outlines 12 factors for the Commission to consider "in determining the reasonable value of electric generating property." As KCP&L recognized, most of the factors listed contemplate an evaluation made after a project is complete,<sup>144</sup> and some are not relevant at all.<sup>145</sup> KCP&L

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<sup>138</sup> Staff Post-Hearing Brief, ¶ 6 (pp 4-5), *citing* Tr. Vol. 1, 188 (Sievers).

<sup>139</sup> Tr. Vol. 1, 189 (Giles) (the La Cygne Project is efficient).

<sup>140</sup> Bates White Report, pp 67-68.

<sup>141</sup> Bridson Direct, pp 11-12.

<sup>142</sup> KCP&L Post-Hearing Brief, ¶¶ 5-6, 10.

<sup>143</sup> KCP&L Post-Hearing Brief, ¶ 5.

<sup>144</sup> K.S.A. 66-128g(a)(3), (4), (6), (8), (10), & (11).

asserted only factor (12) applies in this predetermination proceeding. Factor (12) refers to “any other fact, factor or relationship which may indicate prudence or lack thereof as that term is commonly used.”<sup>146</sup> According to KCP&L’s reasoning, K.S.A. 2010 Supp. 66-1239 and K.S.A. 66-128g should be read in harmony in evaluating whether its decision is prudent. Thus, a finding here that the La Cygne Plan is “reasonable, reliable and efficient” under K.S.A. 2010 Supp. 66-1239(c)(3) supports a finding that KCP&L’s decision is prudent under K.S.A. 66-128g(a)(12).

64. In addressing the issue of prudence, Staff agreed the Commission could decide KCP&L’s proposal to move forward with retrofitting La Cygne is a prudent decision, but opposed any decision that the definitive estimate of \$1.23 billion constituted a prudent decision on costs for purposes of K.S.A. 66-128g. Staff pointed out that all parties, including KCP&L, agreed the \$1.23 billion estimate was considered an “original cost estimate” and “definitive estimate” under K.S.A. 66-128g(b) and (b)(1). But, Staff argued, such estimates only serve as a component of future prudence review under K.S.A. 66-128g, making this the estimate against which the final costs are tracked and compared.<sup>147</sup>

65. The Commission will address cost issues, including the original cost estimate, more fully below. Here, the Commission focuses on KCP&L’s decision to propose retrofitting La Cygne Units 1 and 2. As used in K.S.A. 66-128g, the term “prudence” is to be given its common meaning of “carefulness, precaution, attentiveness and good judgment.”<sup>148</sup> The factors listed in K.S.A. 66-128g provide guidelines for determining prudence, obviating the need for a definition of the term in the statute itself.<sup>149</sup> The Commission does not agree with KCP&L that a finding under the predetermination statute that a utility’s proposed is reasonable, reliable and efficient under K.S.A. 2010 Supp. 66-1239(c)(3) necessarily constitutes a finding of prudence under K.S.A. 66-128g(12).

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<sup>145</sup> *E.g.*, K.S.A. 66-128g(a)(5) (applies to new construction, not retrofitting existing generation) & (7) (applies to nuclear facilities).

<sup>146</sup> K.S.A. 66-128g(a)(12).

<sup>147</sup> Staff Post-Hearing Brief, ¶¶ 12-13.

<sup>148</sup> *Kansas Gas & Electric Co. v. Kansas Corporation Comm.*, 239 Kan. 483, 495, 720 P.2d 1063 (1986).

<sup>149</sup> 239 Kan. at 503.

66. The Commission concludes that evidence here shows KCP&L was careful in evaluating alternative resources, took caution in running numerous scenarios, was attentive in evaluating its impact, and used good judgment in making its decision to move forward with a plan to retrofit La Cygne Units 1 and 2, including among many considerations the regulatory and marketplace uncertainties inherent in planning such investments over a plant that will likely have a remaining useful life of more than two decades. Relying on this evidence, the Commission finds that KCP&L's decision to propose the La Cygne Project was prudent at the time the determination was made as reflected in the record. But the Commission cautions that it recognizes events change. Many witnesses have discussed changing scenarios in this proceeding that may impact the validity of this decision over the course of the implementation of the La Cygne Project. For example, witnesses discussed the historical volatility of the cost of natural gas as well as changing requirements related to protecting the environment. The week before the evidentiary hearing, on July 6, 2011, the EPA issued its long-awaited decision on Cross-State Air Pollution Rule (CSAPR) imposing additional requirements.<sup>150</sup> Also, Westar Witness Haines urged that the Commission should hold a company accountable if a project receiving predetermination treatment failed to perform up to expectations presented during the predetermination proceeding.<sup>151</sup> Thus, the issue of prudence does not end with a finding by this Commission that, at the time its determination was made, KCP&L made a prudent decision that the La Cygne Project was the least cost option. While implementing the La Cygne Project, KCP&L will need to continue to be careful, use caution, be attentive, and use good judgment in addressing ongoing changes that arise and in making decisions regarding the La Cygne Project to be sure its decision remains prudent.

### **C. Estimated Cost of the La Cygne Project**

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<sup>150</sup> As we subsequently learned, on July 11, 2011, which was during the course of the evidentiary hearing, the EPA issued a new Ozone Season Supplemental (OSS) Proposal to be finalized by October 31, 2011, and effective May 1, 2012. The difficulty in the implementation of these new rules is that, while the Regional Haze Rule has been effective and applicable before now to a number of states, particularly in the Northeast, these rules did not previously apply in Kansas.

<sup>151</sup> Tr. Vol. 4, 1054-55, 1068 (Haines).

67. KCP&L has asked the Commission to find that the estimated cost to construct the La Cygne Plan of \$1.23 billion excluding AFUDC and property taxes (\$281 million KCP&L Kansas jurisdictional share<sup>152</sup>) is reasonable and prudent.<sup>153</sup> According to KCP&L, by approving its Petition “the Commission will be acknowledging that it is prudent for the Company to proceed with the project at the estimated cost of \$1.23 billion.” KCP&L Witness Archibald described how KCP&L developed its cost estimate.<sup>154</sup> A request for proposals (RFP) process was used for selection of the Owner’s Engineer, chimney vendor, and the engineer, procure, and construct (EPC) contractor for the La Cygne Project.<sup>155</sup> KCP&L Witness Giles testified a lull currently existed in the construction market and costs for the La Cygne Project could escalate significantly in the near future if the EPA continued to promulgate and issue rules increasing demand for this type of equipment, such as the Cross-State Air Pollution Rule (CSAPR) issued the prior week and supplemented by the Ozone Season Supplemental (OSS) Proposal the following week.<sup>156</sup> Giles stated that if the Commission approved KCP&L’s predetermination request, the EPC contract would likely be signed within a week of the Order because that contract is void if not signed by September 1, 2011.<sup>157</sup>

68. Giles testified that if the Commission denied KCP&L’s request for predetermination, costs would be higher because the cost of capital will go up and the cost to finance the Project will increase.<sup>158</sup> According to Giles, “[t]he credit and investment markets will penalize the Company” if it goes forward with the La Cygne Project without a predetermination ruling.<sup>159</sup> If the Commission rejects the predetermination request, KCP&L will perceive that

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<sup>152</sup> Giles testified that 75% of the cost of the La Cygne Project is Kansas jurisdictional and approximately 25% is Missouri jurisdictional. As a result, KCP&L was “placing a great deal of emphasis on this Commission’s decision[.]” Tr. Vol. 1, 150 (Giles). See Tr. Vol. 2, 296 (Cline) (Missouri jurisdictional amount reflects one-half of KCP&L’s 50% ownership in La Cygne).

<sup>153</sup> KCP&L Post-Hearing Brief, ¶¶ 6, 8-9; Tr. Vol. 1, 132 (Giles).

<sup>154</sup> Archibald Direct, pp. 3-8.

<sup>155</sup> Bell Direct, pp. 7-8 (chimney vendor RFP), 9 (Owner Engineer RFP), and 9-14 (EPC RFP).

<sup>156</sup> Tr. Vol. 1, 85-86, 117-19 (Giles).

<sup>157</sup> Tr. Vol. 1, 141 (Giles).

<sup>158</sup> Tr. Vol. 1, 122, 149 (Giles).

<sup>159</sup> Tr. Vol. 1, 153 (Giles). See Tr. Vol. 1, 267 (Cline); Cline Direct, p. 8 (financial community would deem it imprudent for KCP&L to proceed with the La Cygne Project without preapproval); Tr. Vol. 2, 298 (Cline).

decision as notice that this agency does not agree with taking the approach proposed in the La Cygne Project.<sup>160</sup> Giles explained that, if this predetermination request is approved and a rate case is filed after completion of the La Cygne Project without including construction work in progress (CWIP) in rate base through an earlier rate case, the average KCP&L customer would be expected to pay \$8.25 per month gradually decreasing to \$4.80 per month.<sup>161</sup>

69. Westar concurred with KCP&L's estimate of the project costs.<sup>162</sup> For Staff, Michael Wegner concluded the RFP process was fair.<sup>163</sup> Bates White independently determined the estimated construction costs for a plant like the one proposed and under consideration here would be \$1.211 billion<sup>164</sup> and confirmed the cost estimate provided by KCP&L was reasonable.<sup>165</sup> No evidence challenged KCP&L's original cost estimate of \$1.23 billion as reasonable, reliable and efficient. Parties differed, however, on the significance of such a finding.

70. Westar Witness Jim Haines testified that, if the estimate was approved, the Commission would be bound by the estimate unless the utility was not prudent in managing the construction project causing increased costs or poor performance due to its mismanagement.<sup>166</sup> Regarding the factors listed in K.S.A. 66-128g, Haines noted some factors would be appropriate to consider at this point, but others could not be considered until the upgrades at La Cygne are completed.<sup>167</sup> Staff argued that any decision regarding prudence of the value of the final costs of the retrofit facilities and how these costs were incurred should be withheld until after the project is completed.<sup>168</sup>

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<sup>160</sup> Tr., Vol. 1, 157 (Giles). See Tr. Vol. 1, 183 (Giles discusses likely action KCP&L would take if predetermination is denied).

<sup>161</sup> Giles Direct, p. 17; Tr. Vol. 1, 96-97 (Giles). See Tr. Vol. 1, 180 (Giles) (In a rate case filed after the La Cygne Project is complete, for a customer it is "about 8/10<sup>th</sup> of a cent per kilowatt hour in 2016 and that drops over time to about 3/10<sup>th</sup> of a cent.").

<sup>162</sup> Bridson Direct, pp 7-9.

<sup>163</sup> Wegner Direct, p. 10.

<sup>164</sup> Bates White Report, p. 39.

<sup>165</sup> Bates White Report, p. 41.

<sup>166</sup> Tr., Vol. 4, 1057, 1071.

<sup>167</sup> Tr. Vol. 4, 1019-20.

<sup>168</sup> Staff Post-Hearing Brief, ¶ 14.

71. The Commission concludes that evidence in the record as a whole supports a finding that the cost estimate for the La Cygne retrofit proposal of \$1.23 billion (\$281 million KCP&L Kansas jurisdictional share), excluding AFUDC and property taxes, is reasonable, reliable, and efficient.<sup>169</sup> KCP&L confirmed that this is a “definitive estimate” under K.S.A. 66-128(b)(1), as set forth in Confidential KCP&L Exhibit 5. In deciding this issue, the Commission has relied upon KCP&L’s representation that Exhibit 5 sets out projected costs for the components included in the definitive estimate. As KCP&L Witness Archibald explained, the engineer, procure, and construct (EPC) contract comprises the bulk of the definitive cost estimate.<sup>170</sup> The Bates White Report noted that, after the initial filing, KCP&L decided to proceed with Activated Carbon Injection (ACI) for mercury control within the EPC contract.<sup>171</sup> The Commission considers the costs of both ACI and cooling towers to be included within the definitive estimate contained in KCP&L’s Exhibit 5. The “Remaining Direct Costs Component” of the definitive estimate includes costs required for the chimney, site development, security, plant communications, and other direct project costs not included in the EPC contract.<sup>172</sup> The “Indirect Cost Component” includes such costs as construction management, oversight, legal services, and start-up costs.<sup>173</sup> The definitive estimate also includes a significant reserve under the “Contingency Cost Component” that is an allowance for items, conditions, or events “for which the occurrence is uncertain but experience dictates that it will likely result in additional costs.”<sup>174</sup> In its modeling, although KCP&L took into account operational and age-related maintenance that may be required due to the age of the units to be sure its modeling captured all

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<sup>169</sup> K.S.A. 2010 Supp. 66-1239(c)(3).

<sup>170</sup> Archibald Dir., p. 3.

<sup>171</sup> Bates White Report, ¶ 93, and n. 29. Bates White also recognized that KCP&L has discussed installation of new cooling towers as part of the retrofit for La Cygne. Crawford Dir., p. 12; Bates White Report, ¶ 100, n. 36.

<sup>172</sup> Archibald Dir., p. 6. The Remaining Direct Cost component includes a separate contract for the chimney and site development work. Archibald Dir., p. 6.

<sup>173</sup> Archibald Dir., p. 6. Archibald explained the Indirect Cost Component represent costs of the Owners (KCP&L and Westar) and Black & Veatch, the engineer that developed the bid specification and helped analyze and categorize vendors that bid for the engineer, procure, and construct (EPC) contract. Archibald Dir., p. 6.

<sup>174</sup> Archibald Dir., p. 7. Examples of such events included, but were not limited to, “design maturation, planning and estimating errors or omissions, pricing volatility, constructability or equipment interfacing issues, environmental conditions or schedule impacts.” Archibald Dir., p. 7.

the costs, KCP&L does not request, and the Commission in deciding this issue does not approve, any maintenance, capital costs, or operating expense of the La Cygne unit.<sup>175</sup> If KCP&L completes construction of the La Cygne Project within this definitive estimate of \$1.23 billion, excluding AFUDC and property taxes, and KCP&L does not, in a subsequent proceeding, request recovery for any amount exceeding this estimate, absent a showing of fraud or other intentional imprudence in the construction project, the Commission would not address prudence issues regarding the reasonable value of the La Cygne Project retrofits.

#### **D. Amounts Exceeding the Original Cost Estimate of \$1.23 billion**

72. In addition to asking that its Original Cost Estimate be found reasonable, KCP&L requests the Commission to allow recovery of amounts in excess of this amount “subject to further prudence review during a future rate proceeding.”<sup>176</sup> KCP&L recognized that setting the Original Cost Estimate has established a definitive estimate by which it will be judged in future proceedings. KCP&L then asserted, “Consequently, in a future rate proceeding when these costs are put into rate base, K.S.A. 128g(b) provides that the completed project costs will be presumed prudent unless they exceed 200% of the definitive estimate.”<sup>177</sup> The Commission disagrees with KCP&L’s reading of K.S.A. 66-128g(b). The first sentence of subsection (b) states: “The portion of the cost of a plant of facility which exceeds 200% of the ‘original cost estimate’ thereon shall be presumed to have been incurred due to a lack of prudence.”<sup>178</sup> This sentence does not state any amount exceeding a definitive estimate up to 200% is presumed prudent; instead the sentence makes clear any excess amount over 200% is deemed *imprudent*. But even in those situations, the statute gives the Commission discretion to include the amount deemed imprudent, i.e. over 200% of the original cost estimate, in determining the reasonable value of the electric generating property if the utility satisfies the Commission by a preponderance of the evidence that these excess costs were prudently incurred.<sup>179</sup>

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<sup>175</sup> Tr. Vol. 1, 101-02 (Giles).

<sup>176</sup> KCP&L Post-Hearing Brief, ¶ 6.

<sup>177</sup> KCP&L Post-Hearing Brief, ¶ 32.

<sup>178</sup> K.S.A. 66-128g(b).

<sup>179</sup> K.S.A. 66-128g(b).

73. KCP&L offered to “explain thoroughly any cost above \$1.23 billion in any proceeding in a future rate case” but appears to deny that it would bear the burden of proof to justify such cost overruns.<sup>180</sup> In this Order, the Commission grants KCP&L’s request to find the costs for the La Cygne Project of \$1.23 billion, excluding AFUDC and property tax, and more particularly identified in Confidential KCP&L Exhibit 5, is reasonable. Having granted KCP&L’s request regarding this amount, the Commission further finds that KCP&L shall bear the burden of proving any costs exceeding this amount was prudently incurred and is reasonable to recover from its ratepayers.

74. K.S.A. 2010 Supp. 66-1239(c)(4) gives the Commission discretion to decide which rate-making principles and treatment will be established in ruling on a predetermination petition. To the extent any ambiguity exists regarding the Commission’s authority to decide this issue, the Commission points to testimony by Earl Watkins when he testified on behalf of Sunflower at the time the predetermination statute was proposed to the Legislature. Mr. Watkins stated his belief that “the Commission can fashion orders that would protect ratepayers. If costs rise during construction the utility is at risk.”<sup>181</sup>

75. Here, KCP&L has presented an Original Cost Estimate that will be treated as a definitive estimate under K.S.A. 66-128g(b)(1). If KCP&L completes construction of the La Cygne Project within this definitive estimate, absent a showing of fraud or other intentional imprudence in the construction project, the Commission will find this amount was prudently incurred and will not address prudence issues regarding the reasonable value of the La Cygne Plan retrofits under K.S.A. 66-128g. However, if costs exceed the definitive estimate of \$1.23 billion, excluding AFUDC and property taxes, and KCP&L seeks to recover this excess from ratepayers in a subsequent proceeding, then KCP&L will bear the burden to show that any amount over the definitive estimate of \$1.23 billion, excluding AFUDC and property taxes, was prudently incurred.

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<sup>180</sup> Tr. Vol. 1, 160-61, 209 (Giles).

<sup>181</sup> Watkins Testimony, p. 4.



### **E. Environmental Cost Recovery Rider**

76. KCP&L requested that, as a ratemaking principle, the Commission allow for recovery of the costs of the La Cygne retrofits through an Environmental Cost Recovery Rider (ECRR). As a preliminary matter, the Commission notes that an ECRR mechanism is not specifically provided for by statute, but has been implemented by the Commission in a past case involving Westar based on the specific circumstances of that case dealing with recovery of its mandated federal environmental compliance costs.<sup>182</sup> The Commission declined to allow KCP&L to recover its environmental costs for the La Cygne unit retrofits at issue in this proceeding through an ECRR in a previous proceeding.<sup>183</sup> Subsequent to the Westar case and this matter, the Kansas legislature enacted statutes that provided for recovery of Construction Work in Progress (CWIP).<sup>184</sup> Specifically, the relevant portions of K.S.A. 66-128 provide:

- (b) (1) For the purposes of this act, except as provided by subsection (b)(2), property of any public utility which has not been completed and dedicated to commercial service shall not be deemed to be used and required to be used in the public utility's service to the public.
- (2) Any public utility property described in (b)(1) shall be deemed to be completed and dedicated to commercial service if (A) Construction of the property will be commenced and completed in one year or less ...

In this matter, KCP&L seeks recovery of costs for a construction project that is expected to require four years to complete, so by statute, it would not be deemed to be completed and dedicated to public service during the construction phase. Likewise, K.S.A. 2010 Supp. 66-1239(c)(4), the provision under which KCP&L filed its application in this matter, states that "The commission shall issue an order setting forth rate-making principles and treatment that will be applicable on and after such time as the generating facility is placed in service."

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<sup>182</sup> In the Matter of the Applications of Westar Energy, Inc. and Kansas Gas and Electric Company for Approval to Make Certain Changes in Their Charges for Electric Service, Order on Rate Applications. Docket No. 05-WSEE-981-RTS at pp 26-30 (Dec. 28, 2005)

<sup>183</sup> In the Matter of the Application of Kansas City Power & Light Company to Modify its Tariffs to Continue the Implementation of its Regulatory Plan Order: 1) Addressing Prudence; 2) Approving Application, in Part; & 3) Ruling on Pending Requests Docket No. 10-KCPE-415-RTS, pp. 106-114 (Nov. 10, 2010).

<sup>184</sup> K.S.A. 2010 Supp. 66-128.

77. KCP&L requested an ECRR similar to the one previously approved for Westar. The Westar ECRR provides a return on and return of the capital deployed to build environmental upgrades, including related Operations and Maintenance (O&M) expenditures directly tied to environmental improvements. Under the Westar ECRR, an annual filing is made that includes the prior calendar year's costs, and the costs are reviewed by Staff in an abbreviated proceeding, and, if approved by the Commission, reflected in rates shortly afterwards. At the next rate case, these accumulated environmental costs are included in base revenue requirements.

78. As support for an ECRR, KCP&L argued the total cost to ratepayers for the La Cygne Project will be reduced using an ECRR and pointed out that KCP&L withdrew a request to include operations and maintenance expenses in its ECRR.<sup>185</sup> KCP&L claimed allowing use of an ECRR recognizes Construction Work in Progress (CWIP) in a timely way and minimizes “rate shock” by gradually recovering costs in rate base over the term of construction, rather than introducing one large rate increase when the project is complete as part of a rate case.<sup>186</sup> Also, KCP&L suggested that allowing an ECRR will significantly reduce AFUDC that would otherwise be incurred.<sup>187</sup> If financial markets should collapse, KCP&L could use available lines of credit to finance this Project or could stall or stop construction of the Project. But if an ECRR is in place, ratepayers will continue to pay costs until the Commission has an opportunity to rule on this decision.<sup>188</sup> KCP&L claimed that if an ECRR is approved, the number of costly rate cases filed will be minimized during the life of the La Cygne Project, but KCP&L refused to agree not to file a base rate case until after the La Cygne Project was completed. Giles asserted approving its ECRR will not obviate the need to file a rate case during the four years needed to complete the La Cygne Project,<sup>189</sup> stating “What [granting the ECRR] will do, it will provide an opportunity for KCPL to delay or postpone rate increase cases.”<sup>190</sup>

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<sup>185</sup> Giles Rebuttal, p. 22.

<sup>186</sup> Giles Rebuttal, pp 26-27.

<sup>187</sup> Giles Direct, p. 15; Tr., Vol. 5, 1569-74 (Rohlf).

<sup>188</sup> Tr. Vol. 2, 331-32, 237-38 (Cline).

<sup>189</sup> Tr. Vol. 1, 99 & 159 (Giles).

<sup>190</sup> Tr. Vol. 1, 70 (Giles).

79. Both KCP&L and Westar argued that another reason to approve an ECRR for the La Cygne Project is that a specific ECRR charge will appear on bills and alert customers to the costs needed to meet mandated environmental requirements.<sup>191</sup> KCP&L's ECRR will only be in effect during construction of the La Cygne Project and transparency for this Project will increase because KCP&L agreed to provide Staff and the Commission with monthly and quarterly reports on costs being incurred.<sup>192</sup> Additionally, KCP&L confirmed that it will calculate AFUDC allocations manually and update its software so these calculations can be performed mechanically by the end of 2011 to address the concern with allocation of costs between Kansas and Missouri (thereby admitting that KCP&L does not presently have software in place capable of providing these calculations).<sup>193</sup> KCP&L argued its proposed ECRR is a reasonable and efficient mechanism for funding its environmental obligations to retrofit La Cygne Units 1 and 2.

80. Westar noted that the Commission, in an Order issued May 27, 2011, in Docket No. 09-WSEE-737-TAR-CPL-1, approved other revisions to Westar's ECRR surcharge tariff but not Westar's recovery of costs associated with the La Cygne environmental retrofits until the investigation and analysis in this docket was completed. If predetermination is granted in this case, Westar saw no reason not to allow use of its ECRR to recover these costs. Although using an ECRR generally allows somewhat earlier recovery of costs than using a full rate case, Westar noted recovery using an ECRR is not immediate since Westar notifies Staff and CURB of a project at least 12 months in advance.<sup>194</sup> By using the ECRR process, parties can concentrate on reviewing a limited number of environmental projects rather than the 40 to 50 individual adjustments that must be dealt with in a traditional rate case proceeding. Tr., Vol. 5, p. 1528 (Rohlf's). Westar customers are notified through a bill insert when an adjustment is sought to its ECRR and its monthly energy bills have a separate charge identifying costs recovered through its ECRR. Rohlf's Rebuttal, pp 3-4.

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<sup>191</sup> Tr. Vol. 1, 183 (Giles); Rohlf's Direct, p. 10.

<sup>192</sup> Tr. Vol. 5, 1584-1585 (McClanahan) (confirmed reports from KCP&L will alleviate some review and analysis usually done in annual ECRR filings).

<sup>193</sup> Giles Direct, p. 13; Cline Reb., p. 2; Tr. Vol. 5, 1588-89 (McClanahan).

<sup>194</sup> See Rohlf's Rebuttal, p. 3 (describing ECRR process).

81. Staff and CURB opposed using an ECRR to recover costs for the La Cygne Project. Staff Witness McClanahan listed concerns the Commission expressed when denying KCP&L's request for an ECRR in Docket 10-415 and asserted that no new compelling evidence has caused Staff to reconsider this issue.<sup>195</sup> Staff pointed out benefits from using an ECRR will be reduced if KCP&L files rate cases during the life of the La Cygne Project,<sup>196</sup> Giles recognized this to be a possibility.<sup>197</sup> Staff further argued an ECRR for KCP&L and Westar were not equivalent, noting Westar's ECRR will include more projects than La Cygne and KCP&L's ECRR will require additional calculations to separate Kansas and Missouri jurisdictional costs.<sup>198</sup> Also, Staff was concerned that Kansas ratepayers will not realize the full benefit of an ECRR because KCP&L does not have an ECRR in Missouri. Furthermore, as a result of rate increases over the last four years, Staff noted that an ECRR would not provide the rate stability claimed by KCP&L, but would simply continue a trend of annual rate increases.<sup>199</sup>

82. CURB, like Staff, asserted reasons given for rejecting KCP&L's request for an ECRR in Docket 10-415 have not changed.<sup>200</sup> KCP&L's customers have had rate increases of \$138 million during the last 5 years (a 40% overall increase) in the four rate cases in KCP&L's Resource Plan from Docket 04-1025, and these rate increases will continue using an ECRR.<sup>201</sup> CURB also argued K.S.A. 2010 Supp. 66-1239(c)(4) precludes use of an ECRR by requiring the Commission to issue an order establishing rate-making principles and treatment "that will be applicable to the public utility's stake in the generating facility . . . in all rate-making proceedings on and after such time as the generating facility is placed in service." The ECRR is a Commission creation and directly conflicts with this explicit statutory language requiring any rate-making treatment be applied "on or after" the plant comes online.<sup>202</sup> In addition, CURB

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<sup>195</sup> McClanahan Direct, p. 5.

<sup>196</sup> Tr. Vol. 5, 1598-99 (McClanahan).

<sup>197</sup> Tr., Vol. 1, 70-71 (Giles).

<sup>198</sup> Tr. Vol. 5, 1588, 1602 (McClanahan).

<sup>199</sup> Tr. Vol. 5, 1590-91 (McClanahan).

<sup>200</sup> McClanahan Direct, p. 5, *citing* Docket 10-415, November 22, 2010 Order, p. 114.

<sup>201</sup> CURB Post-Hearing Brief, ¶ 60.

<sup>202</sup> CURB Post-Hearing Brief, ¶ 61. See KIC Post-Hearing Brief, ¶ 46 (ECRR cannot go into effect under K.S.A. 66-1239 until retrofits are in commercial operation and a depreciation schedule ordered).

noted Staff has no more than 45 days to review Westar's ECRR, and CURB has only 15 days, which is not adequate time to review prudence of a project or the specific expenditures. Westar's ECRR submission does not contain as much information as supplied in this predetermination docket, such as a supply plan model, load forecast data, demand response information, or data about alternatives.<sup>203</sup> Finally, CURB asserted that collecting costs annually from customers through an ECRR results in more total dollars to the utility on a net present value basis than if construction costs are placed in AFUDC and carried until the next utility rate case.<sup>204</sup>

83. In considering whether to approve use of an ECRR to recover costs for the La Cygne Project, the Commission has examined the positions of the parties, including the benefits KCP&L and Westar urge weigh in favor of adopting this rate-making principle as well as the concerns Staff and CURB argue weigh in favor of rejecting the ECRR here. The Commission sees many differences between the ECRR being considered here and the rate recovery proposal initially presented to the Commission by Westar in Docket 05-981.<sup>205</sup> The rider this Commission approved in Docket 05-981 almost six years ago allowed Westar to recover its costs for making specific environmental improvements on identified generation plants under EPA requirements imposed on Westar. No questions were raised then about whether the underlying generation plant should be retrofitted or closed. Tr. Vol. 4, 893 (Pavlovic) ("The issue of retrofit for environmental reasons is a relatively new one."). With this docket, the Commission finds itself in a new era with a different set of statutes and proposed environmental upgrades based on contractual commitments and, as yet, environmental rules and regulations that have not been fully implemented by the EPA. The consideration in this case involved a complex assessment of a broad range of alternatives that included major changes to the facility. Use of an ECRR is not appropriate for such circumstances.

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<sup>203</sup> Tr. Vol. 5, 1529-30 (Rohlf's).

<sup>204</sup> CURB Post-Hearing Brief, ¶¶ 65-69.

<sup>205</sup> *Order on Rate Applications*, Docket No. 05-WSEE-981-RTS, issued December 28, 2005, ¶¶ 53-65, *Kansas Industrial Consumers Group v. Kansas Corporation Comm'n*, 36 Kan. App. 2d 83, 138 P.3d 338, rev. denied 282 Kan. 790 (Nov. 8, 2006), *aff'd following remand in Kansas Industrial Consumers Group v. Kansas Corporation Comm'n*, No. 99,415, Unpublished Opinion filed February 11, 2008, 176 P.3d 250 (Kan. App. Ct 2008).

84. Instead, the ECRR in this case appears to have become a mechanism for increasing a utility's annual revenues to satisfy demands for growth made by the financial community rather than a mechanism for dealing with environmental compliance costs. The report by J.P. Morgan is attached to KCP&L's witness Cline's Direct Testimony provided particular insight into how the financial community views environmental riders and predetermination. For example, the J.P. Morgan analysts concluded:

Beyond the Comprehensive Energy Plan, we anticipate environmental retrofits at GXP's existing coal plants to constitute the most meaningful rate base growth driver going forward. Their timing and magnitude, as well as GXP's ability to negotiate appropriate regulatory treatment that minimizes regulatory lag, however, will likely determine the ultimate earnings impact.<sup>206</sup>

85. Although the Commission has found the definitive estimate for the La Cygne Project is reasonable given anticipated compliance with environmental requirements, this large project will have a significant impact on ratepayers' bills. Recent downturns in the economy have placed stress upon many ratepayers of both KCP&L and Westar. Also, as described above, the Commission notes that many of the environmental improvements included in the La Cygne Project will meet requirements that have not yet been fully implemented, but instead are anticipated to take effect in the future. Significant questions have arisen regarding the modified cap and trade feature of the CSAPR, the availability of excess credits, the market that may develop for such credits, and the potential cost of credits. The potential future cost that utility companies will undoubtedly expect customers to bear is presently unforeseeable or speculative at best, but undoubtedly will be significant. The parties recognized many uncertainties exist regarding determinations the Commission must make in this proceeding. Predicting what Congress will do in the future is one of the biggest uncertainties, including decisions about the environment and the future of the EPA. Based upon its review of the entire record in this proceeding, the Commission denies KCP&L's request for an ECRR to pass through costs of the La Cygne Project to its ratepayers. Although Westar was not an applicant in this proceeding, it

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<sup>206</sup> Cline Direct, MWC2011-1, p. 1. See, Tr. Vol. 2, 314-319 (Cline).

participated throughout this administrative process as an intervenor. For that reason, the Commission further makes clear in this Order that costs of the La Cygne Project as described in this Order and identified as a definitive cost in KCP&L Exhibit 5, will not be passed through Westar's ECRR to its customers.

#### **F. Return on equity for costs associated with the La Cygne Project**

86. KCP&L does not seek a separate rate of return or consideration of capital costs for the La Cygne Project, instead asking the Commission to confirm the cost of capital and rate of return applied to the La Cygne Project will be consistent with what is established generally for KCP&L's Kansas jurisdictional operations.<sup>207</sup> KCP&L argued that traditionally return on equity is established during a rate case where the entire Company's revenues and expenses are considered in determining a reasonable return on equity.<sup>208</sup> Any modification to its authorized rate of return based upon perceived risks of the La Cygne Project "would be fundamentally improper and unsound practice."<sup>209</sup> KCP&L specifically denied implications that the La Cygne Project is being undertaken to grow its rate base. Although acknowledging rate base will grow to the extent capital must be raised and deployed, KCP&L argued the decision to propose the La Cygne Project was based on its need to satisfy its government-mandated environmental obligations and to use the least cost alternative to reliably and efficiently meet its obligation to serve load.<sup>210</sup>

87. Citing different reasons, Staff also recommended the Commission make no change in return on equity. Staff pointed out that the Commission in Docket 10-415 was persuaded by Staff Witness Gatewood's testimony regarding cost of capital theory in setting a 10% rate of return for KCP&L. No reason was given to adjust this decision here. Instead, the Commission should reserve a determination of KCP&L's return on equity for future full rate cases.<sup>211</sup>

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<sup>207</sup> Petition, ¶ 8; Giles Direct, p. 13; Cline Rebuttal, p. 2.

<sup>208</sup> KCP&L Post-Hearing Brief, ¶ 61, citing *Federal Power Comm'n v. Hope Natural Gas Co.*, 320 U.S. 591, 603 (1944).

<sup>209</sup> KCP&L Post-Hearing Brief, ¶ 61, citing Cline Direct, p. 9; Haines Direct, pp 6-22.

<sup>210</sup> KCP&L Post-Hearing Brief, ¶ 63.

<sup>211</sup> Gatewood Direct, p. 3; Tr. Vol. 4, 906-07, 911-15; Tr. Vol. 5, 1624-25.

88. CURB recommended a 100 basis point reduction of the return on equity be applied for the retrofit equipment if predetermination is granted because a predetermination proceeding is not a traditional rate-making approach and in effect reduces shareholder risk by shifting that risk to KCP&L's customers.<sup>212</sup> To recognize this shift in risk, CURB urged a 100 basis point reduction in shareholder return on equity in all future rate cases for the portion of rate base attributable to the La Cygne Project.<sup>213</sup> CURB noted that KCP&L Witness Cline, Treasurer of Great Plains Energy, recognized the risk to KCP&L, "in terms of access to and cost of capital, is the negative financial stakeholder response anticipated if the Commission were to reject the Company's request, thereby forcing KCP&L to follow the higher-risk traditional ratemaking model if it were to go forward with this very significant investment."<sup>214</sup> Risks shifted to ratepayers if KCP&L's predetermination request is approved include greater cost of the retrofits, retrofits not operating as anticipated, higher coal prices, higher CO2 prices, lower natural gas prices, higher plant operating costs, and/or retirement of La Cygne Units 1 or 2 before 2034.<sup>215</sup> CURB Witness Crane explained why she recommended a 100 basis point reduction for any costs associated with the La Cygne Project.<sup>216</sup>

89. The Commission notes that in proposing adoption of the predetermination statute, Earl Watkins stated that Sunflower met with the Commissioners, as well as the Commission's General Counsel and Chief of Operations, to discuss the proposed legislation. Watkins in testifying before the Senate Utilities Committee stated, "Naturally, a primary concern discussed with the Commission was 'shifting' risk from utilities to ratepayers." Watkins Testimony, page 6. Watkins pointed out Iowa had recently adopted legislation similar to that being proposed in Kansas, which allowed the Iowa Utilities Board to reduce "the utility's rate of return to reflect the lowering of risk for the utility."<sup>217</sup> Watkins continued, "The utility [under the Iowa statute] still

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<sup>212</sup> Crane Direct, p. 6.

<sup>213</sup> CURB Post-Hearing Brief, ¶ 9.

<sup>214</sup> Cline Direct, p. 13.

<sup>215</sup> CURB Post-Hearing Brief, ¶ 56, *citing* Schlissel Direct, p. 3.

<sup>216</sup> Crane Direct, pp 30-31.

<sup>217</sup> See FINAL DECISION AND ORDER, *In re: Midamerican Energy Company*, Iowa Utilities Board Docket No. RPU-2009-0003 (December 14, 2009), p. 2, *citing* Iowa Code 476.53 (upon request, Board shall specify ratemaking



has certainty; the ratepayers enjoy lower costs.” Watkins Testimony, page 6. The Kansas statute by which this Commission is bound contains no such provision, though the Legislature was certainly mindful of that option.

90. The Commission rejects CURB’s request to reduce KCP&L’s return on equity by 100 basis points for any costs associated with the La Cygne Project. The Commission has denied the request to pass through costs of the La Cygne Project using an ECRR. Having reached that decision, the Commission determines KCP&L’s cost of capital and return on equity for the La Cygne Project will be the same established generally for KCP&L’s overall rate base.

#### **IV. Conclusion**

91. In reviewing the Project Management of the La Cygne Project, Staff recommended that KCP&L use the Earned Value Management process for measuring the performance of the project work against what was planned. Earned Value Management takes a snap shot of the project at a specific moment in time and gathers data that includes the actual costs incurred as of that date, the planned value as of that date, and input from the construction management team regarding the percentage of completeness of the progress. Staff Witness Michael Wegner explained how Earned Value is calculated and recommended that this data be provided on a monthly basis, where data is captured one week prior to the report being filed. He noted such a reporting requirement provides KCP&L an opportunity to explain what its EPC contractor is doing to correct any issues. Staff recommended this information be reported for each of the 33 Scope of Work Element listed in the bid analysis of the La Cygne Project and for the Project as a whole.<sup>218</sup> Staff further recommended that the Commission include in its Order requirements for the retrofitted plant to perform to emission output levels defined in the Regional Haze Agreements, as shown in Exhibit MJW-1, p. 5, ¶ 23 A through E.<sup>219</sup>

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principles in advance that will apply when costs for constructing eligible new electric generation is included in rates), and pp 79-82 (Board approves return on equity component agreed to in settlement of rate-making principles).

<sup>218</sup> Wegner Direct, pp 14-16.

<sup>219</sup> Wegner Direct, p. 16.

92. Following receipt of Wegner's Direct Testimony, KCP&L and Staff agreed to reporting metrics KCP&L will use and provide to Staff on a regular basis throughout the life of the La Cygne Project.<sup>220</sup> This agreement is reflected in Schedule CBG2011-5, which is incorporated in this Order. See Attachment 2. KCP&L further agreed to use the Regional Haze emission requirements as the basis for in-service criteria for the La Cygne Environmental Project.<sup>221</sup>

93. The Commission approves the agreement reached between KCP&L and Staff regarding the filing of reporting metrics, as set forth in Attachment 2 but on a monthly basis, throughout the life of the La Cygne Project. The monthly reporting requirement will begin on the first day of October, 2011, and continue during the life of the La Cygne Project. Staff shall review the Reports as submitted by KCP&L and shall bring to the attention of the Commission any information reflecting a significant event or problem regarding implementation of the La Cygne Project. KCP&L will submit these monthly reports for Staff's review by filing them in a sub-docket of this proceeding using compliance Docket No. 11-KCPE-581-PRE-CPL-1. In addition, the Commission approves use of the Regional Haze Agreement emission requirements as the basis for in-service criteria for the La Cygne Project.

94. In closing this Order, the Commission notes this docket has been one of the more interesting, if not challenging, to be heard in recent years. The Commission acknowledges the skill and professionalism shown throughout this proceeding by the parties and their counsel. The Commission has decided many issues in this Order. To the extent an issue was raised by a party but not specifically addressed in this Order, the issue is denied. The Commission sought the advice of many experts throughout the evidentiary hearing. The Commission in particular recognizes the philosophy offered by Mr. Slater in discussing how a decision must be made when balancing current available information with future unknowns:

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<sup>220</sup> Giles Rebuttal, p. 31.

<sup>221</sup> Giles Rebuttal, p. 32.

If you make a decision on what you know rather than on what you don't know, . . . it has over time proven to be pretty good decision making. It's had its little ups and downs, but it's turned out well in the long term. We all have a good reliable supply of electricity because we've done our planning.<sup>222</sup>

The Commission grants KCP&L's request for predetermination as set forth in this Order.

IT IS, THEREFORE, BY THE COMMISSION ORDERED THAT:

(A) The Commission hereby grants KCP&L's Petition for predetermination of rate-making principles and treatment under K.S.A. 2010 Supp. 66-1239, as stated in this Order.

(B) The Commission denies KCP&L's request to approve use of an ECRR to recover costs for the La Cygne Project, as stated in this Order.

(C) Consistent with the decision stated above, the Commission orders that Westar is not allowed to use an ECRR to recover costs for the La Cygne Project, as stated in this Order.

(D) Parties have agreed to electronic service, with no hard copy follow-up. Parties have fifteen days from the date of service of this Order in which to petition the Commission for reconsideration of any matter decided herein. K.S.A. 66-118b; K.S.A. 2010 Supp. 77-529(a)(1).


(E) The Commission designates this Order as precedent under 2011 House Bill No. 2027, (b)(2)(A), *amending* K.S.A. 2010 Supp. 77-415, that may be relied upon in any subsequent adjudication.

(F) The Commission retains jurisdiction over the subject matter and parties for the purpose of entering such further order or orders as it may deem necessary.

BY THE COMMISSION IT IS SO ORDERED.

Sievers, Chmn; Loyd, Com.; Wright, Com.

Dated: AUG 19 2011

  
ORDER MAILED AUG 19 2011  
ELECTRONIC

Patrice Petersen-Klein  
Executive Director

mjc

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<sup>222</sup> Tr. Vol. 5, 1425 (Slater).

# **CONFIDENTIAL INFORMATION**

(Located in Docket Room)

In the Matter of the Petition of Kansas City Power & Light Company (“KCP&L”) for Determination of the Ratemaking Principles and Treatment that Will Apply to Recovery in Rates of the Cost to be Incurred by KCP&L for Certain Electric Generation Facilities Under K.S.A. 66-1239.

**Docket Number**

**11-KCPE-581-PRE**

Confidential Attachment A to Order Granting KCP&L Petition for Predetermination of Rate-Making Principles and Treatment

**FILE DATE**

**August 19, 2011**

**Kansas City Power & Light Company's**  
**Project Controls Reporting to KCC Staff**  
**for La Cygne Environmental Retrofit Project**

- On a quarterly basis, KCP&L will provide Staff with a project status update, including both Cost and Schedule status. In the interim, Staff will have monthly access to both Cost and Schedule metrics once they are generated and have completed the required approval process. The Cost Report, including the ancillary reports, will be generated after KCP&L's monthly closing process.
- KCP&L will report Earned Value metrics by scheduled area as defined within the EPC contractor's (LEP's) schedule. The areas will transition into systems during the start-up phase. The following Earned Value metrics will be reported for scheduled man-hours only:
  - Schedule Performance Index (SPI) / Schedule Variance (SV)
    - Measure of Schedule Performance
    - Formula = Earned Man-hours divided by Planned Man-hours
  - Cost Performance Index (CPI) / Cost Variance (CV)
    - Measure of Contractor's Cost Performance - This is an INDICATOR ONLY for whether or not the contractor is spending more or less man-hours than originally planned. This is not directly related to budget variances in an EPC contract, however, it is an indicator for the owner to be more cognizant of possible contractor initiated change orders/ safety/ owner caused delay claims.
    - Formula = Earned Man-hours/ Actual Man-hours
  - Payments to EPC Vendor
    - KCP&L will use Schedule of Values (SOV) for payment of the base contract.
    - KCP&L will convert the dollars associated with each SOV milestone to a unit price rate for each schedule man-hour associated with that SOV milestone. The unit price will encompass both labor and material and be inclusive of the contractor's indirects (*i.e.*, superintendents, management personnel, overheads, etc). The vendor will be paid based on percent complete of the SOV milestones. The percent complete will be reported weekly and validated by the KCP&L's construction team and agreed to by both KCP&L and LEP prior to execution of monthly payments.
- KCP&L will report project costs using a format similar to what was produced for the Iatan Project. The package will consist of the following:
  - Monthly Cost Report;
  - Contingency Log; and
  - Budget Transfer Log.

**CERTIFICATE OF SERVICE**

**AUG 19 2011**

11-KCPE-581-PRE

I, the undersigned, hereby certify that a true and correct copy of the above and foregoing Order Granting KCP&L Petition for Predetermination of Rate-Making Principles and Treatment was served by electronic mail this 19th day of August, 2011, to the following parties who have waived receipt of follow-up hard copies:

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