BEFORE THE STATE CORPORATION COMMISSION
OF THE STATE OF KANSAS

In the Matter of the Joint Application of Sunflower Electric Power Corporation and Mid-Kansas Electric Company, Inc. for an Order Approving the Merger of Mid-Kansas Electric Company, Inc. into Sunflower Electric Power Corporation.	))))))	Docket No. 19-SEPE-054-MER

PREFILED DIRECT TESTIMONY OF

H. DAVIS ROONEY

VICE PRESIDENT AND CHIEF FINANCIAL OFFICER

ON BEHALF OF

SUNFLOWER ELECTRIC POWER CORPORATION

and

MID-KANSAS ELECTRIC COMPANY, INC.

AUGUST 3, 2018

Q. Please state your name.

A. My name is H. Davis Rooney.

Q. By whom are you employed and what is your business address?

A. I am employed by Sunflower Electric Power Corporation ("Sunflower"). My business address is 301 W. 13th Street, Hays, Kansas.

Q. What are your present positions at Sunflower and Mid-Kansas Electric Company, Inc. ("Mid-Kansas") and how long have you held the current positions?

A. I am Vice President and Chief Financial Officer of both Mid-Kansas and Sunflower. I assumed these positions on October 22, 2008.

Q. What prior positions have you held?

A. Prior to joining Sunflower, I held positions at Kansas City Power & Light Company ("KCP&L"), Aquila, Inc. ("Aquila"), and Arthur Andersen.

Q. Please describe your education, experience, and employment history.

A. I graduated from the University of Kansas. I received a B.A. with distinction in mathematics, and a B.S. with distinction in business, with majors in accounting and business administration and a concentration in computer science. I obtained my certified public accountant certificate in 1983 and practiced in public accounting from 1983 to 1992. In 1992, I joined Aquila as controller of its WestPlains Energy division. This division was later reorganized into WestPlains Energy – Colorado and WestPlains Energy – Kansas ("WPEK"). At Aquila I held several positions focused on financial management and analysis, including director of accounting and finance for the Missouri Electric divisions of Aquila

Networks. My last position at Aquila was as director of resource planning and commodity analysis. At KCP&L I held the position of manager, CEP business operations. My responsibilities included business planning and analysis concerning infrastructure investment projects for KCP&L, and Aquila d/b/a KCP&L Greater Missouri Operations Company.

Q. What is the purpose of your testimony?

A. The purpose of my testimony is to support the merger of Sunflower and Mid-Kansas regarding specific benefits of approving the Agreement and Plan of Merger ("Merger Agreement"). The benefits arise in five primary ways: (1) strengthening the financial condition of the two companies; (2) improving the credit profile to lower the cost of debt service; (3) stabilizing wholesale rates through scale and mitigation of impacts from load variations; (4) diversifying our generation; and (5) savings associated with merging the two companies. Each of these improves the credit profile of Mid-Kansas and lowers the cost of financing. Lower financing costs directly benefit our Members and their retail customers, as well as wholesale transmission customers. Additionally, diversifying the generation resources mitigates energy cost fluctuations due to market fluctuations in fuel costs. I will also testify to the treatment of the Member's equity interests pursuant to the Merger Agreement, treatment of Member's capital accounts and capital credit allocation after merger, and the wholesale rate variance between the two companies.

Q. How does your testimony relate to the merger standards?

A. I will provide testimony in support of the Agreement and Plan of Merger ("Merger Agreement"). I will provide support for Merger Standards (a)(i), (a)(ii), (a)(iii), (a)(iv), (d), (e), and (g). More specifically I will discuss:

- The merged company has greater credit strength than the individual companies. This supports merger standard (a)(i) impact on financial condition.
- Greater credit strength will lead to lower costs through lower interest rates on borrowings. This supports merger standards (a)(ii) reasonableness of purchase price (however, there is no purchase price) in light of savings, (a)(iii) benefits for ratepayers, (a)(iv) operational synergies to justify an acquisition premium (however, there is no acquisition premium), and (g) reduction of economic waste.
- Merger related savings resulting from elimination of duplicative efforts and reduced cost allocation complexities. This supports merger standards (a)(ii) reasonableness of purchase price in light of savings, (a)(iii) benefits for ratepayers, (a)(iv) operational synergies to justify an acquisition premium, (d) preservation of the commission's jurisdiction, and (g) reduction of economic waste.
- Improved rate stabilization from increased scale and greater diversification of generation resources. This supports merger standards (a)(i) impact on financial condition, (a)(ii) reasonableness of purchase price in light of savings,

(a)(iii) benefits for ratepayers, (a)(iv) operational synergies to justify an acquisition premium, and (g) reduction of economic waste.

- Preservation of the Commission's jurisdiction and capacity to regulate, while reducing the number of regulatory filings. This supports merger standards (a)(ii) reasonableness of purchase price in light of savings, (a)(iii) benefits for ratepayers, (a)(iv) operational synergies to justify an acquisition premium, (d) preservation of the Commission's jurisdiction, and (g) reduction of economic waste.
- The impact of the merger on Sunflower and Mid-Kansas Members and wholesale customers.

Overview

Q. Please provide an overview of the transaction from a financial perspective.

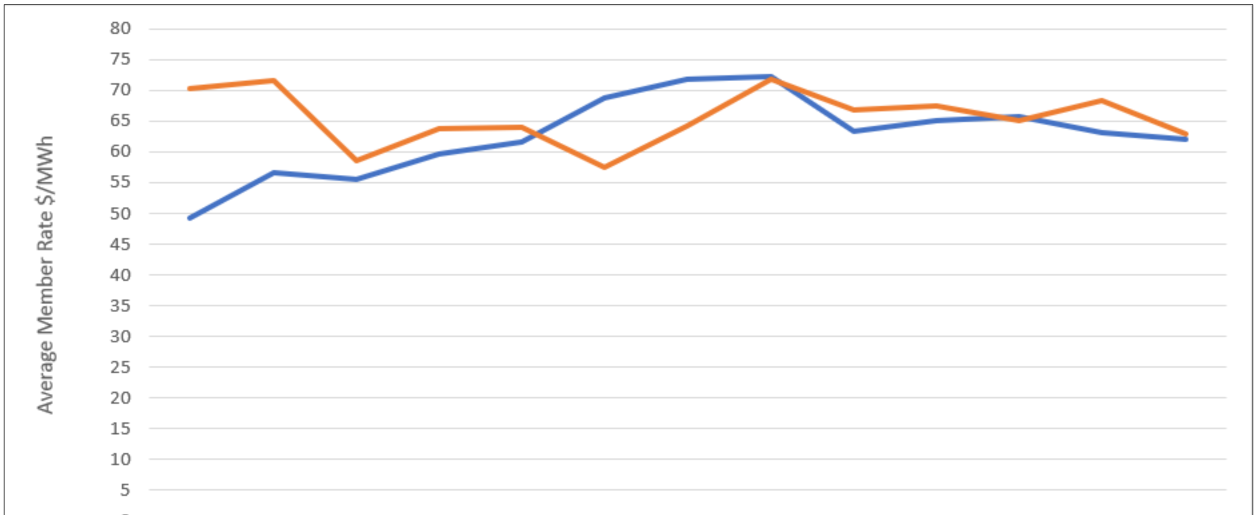
A. The transaction is structured as a merger of equals. Practically speaking, the six Member distribution retail cooperatives own both Sunflower and Mid-Kansas. In some ways this merger is like the Westar/Great Plains Energy merger (Docket 18-KCPE-095- MER). There is no cash being exchanged, and no acquisition premium being paid. The Members combine their equity in Mid-Kansas with their equity in Sunflower. There will be no change in the equity ownership by Member. There will be no new long-term debt issued to support the merger and no change in the book value of utility assets. Unlike Westar/Great Plains, there will be no goodwill booked and we will not be maintaining separate rate areas or legal entities. In fact, one of the key objectives of the Members since the acquisition of the WestPlains system of Aquila, Inc. ("Aquila-WPK") by the Mid-Kansas

Members was to establish an integrated electric system between Sunflower and Mid-Kansas to facilitate a consolidated rate for the two service territories. In this way, the Sunflower and Mid-Kansas merger is similar to the rate convergence of Westar North and Westar South (Docket 09-WSEE-641-GIE or “09-641 Docket”).

Q. How are Sunflower and Mid-Kansas similar to the Westar North and Westar South rate consolidation considered in the 09-641 Docket?

A. Like Westar South, Mid-Kansas has no direct employees. Sunflower employees operate the Mid-Kansas assets and costs are allocated to Mid-Kansas. Like Westar North and South, Sunflower and Mid-Kansas are operated on an integrated basis with a single dispatch authority to meet the needs of both companies. In 2014, that single dispatch authority was transferred to the Southwest Power Pool (“SPP”). Like the Westar North and South areas, Sunflower and Mid-Kansas have two rate areas operated under common operational control and planning. Greater levels of integration have been achieved year after year. This high level of existing integration has already achieved many of the usual opportunities for savings from merger. Since the acquisition of Aquila-WPK, the Boards of Sunflower and Mid-Kansas have taken actions to decrease the rate differential that existed at the time of the acquisition. Our rates to our Members are currently close together and, given the integrated planning and operation, it makes more sense to merge the two companies and move to a single rate than to preserve a distinction that is less and less meaningful each year. Below is a chart showing the Member rates from the time of acquisition to the current budget year[1]. If merger is approved, the merged company will have a single rate for all Members.

Comparison of Sunflower and Mid-Kansas Average Member Rates



	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018P	2019P
SEPC	49.32	56.68	55.56	59.67	61.66	68.75	71.92	72.18	63.41	65.19	65.80	63.15	62.14
MKEC	70.28	71.65	58.47	63.83	64.1	57.47	64.21	71.81	66.74	67.54	65.13	68.26	62.91

Unlike, Westar North and South, separate debt is held by Mid-Kansas and by Sunflower. This makes joint rate setting among the separate companies complex and better accomplished by merger.

Q. How will wholesale customers (non-members) be impacted?

A. Some wholesale customers take power supply from Sunflower or Mid-Kansas at rates tied to the Member rate. These customers will be impacted similarly to the Members. Some wholesale customers have contracted rates. If they have contracted rates, they will remain at the rates and terms in their contracts. Some

[1] Sunflower and Mid-Kansas are currently in the 2019 budget preparation process and the projected rates could change once the final budget numbers are set by the respective boards. However, the current expectation is that the difference in the two rates will be similar to those as represented in the graph. The rate in 2020, after merger, would be a single rate.

wholesale customers take only transmission service. Currently, in 2018, the transmission rates for both the Mid-Kansas zone and the Sunflower zone are also very close to each other, within 2% of the combined average rate. We expect the post-merger transmission rate impact on the transmission only customers to also be minimal. Our intent is to have a single transmission formula rate for the merged company.

Q. Does the Commission prefer reducing rate disparities in merged entities?

A. Yes, I believe so. Much of the history and Commission policy is discussed in the 09-641 Docket.[2] The Commission notes both a history of utilities converging their rates and a preference by the Commission for this to occur. Sunflower and Mid-Kansas believe they are pursuing prudent policies consistent with the Commission by implementing rate convergence actions.

<u>Financial Condition and Credit Profile</u>

Q. How will the financial condition of the merged entity compare to the standalone entities?

A. Because there is not a purchase price and not an acquisition premium, there is not the increase in debt that normally accompanies a merger. The financial condition of both entities will be improved by the merger. The combined entity credit strength will be stronger than the simple sum of the two standalone entities.

[2] "The Commission notes that the gradual move toward equal rate treatment for WN and WS customers is consistent with its policy for other merged utilities." Order Approving Rate Consolidation, 09-641 Docket, page 16, para. 35.

Q. How will Mid-Kansas' financial position be improved?

A. Mid-Kansas will benefit from Sunflower's stronger equity position, from greater fuel diversity, and greater economy of scale gained from the merger as opposed to a standalone entity. At the end of 2017, Sunflower had equity as a percent of capitalization of approximately 55% while Mid-Kansas had equity as a percent of capitalization of about 13%. By merging the two, the surviving company, Sunflower, will have an equity position of about 30% which is viewed as a very favorable G&T equity position from a creditor's perspective. Beginning in 2019, Mid-Kansas will be dependent on only natural gas for dispatchable generation. Mid-Kansas will gain fuel diversity by gaining access to Sunflower's coal generation. Both Mid-Kansas and Sunflower will benefit from increased economy of scale that will help with greater stabilization of rates.

Q. How will Sunflower's financial condition be improved?

A. Because of Sunflower's historical borrowing constraints under RUS, Sunflower has not directly developed the lender relationships Mid-Kansas has. Mid-Kansas has a multi-bank $100 million syndicated line of credit. Mid-Kansas has developed relationships through its private placement with lenders in the insurance industry. Sunflower will benefit from this lender diversity. Sunflower, like Mid-Kansas, will benefit from fuel diversity. Sunflower's generation is largely coal. Sunflower will gain fuel diversity by gaining access to Mid-Kansas' natural gas, wind, and solar generation. Both Mid-Kansas and Sunflower will benefit from increased scale that will help with greater stabilization of rates.

Q. How do Sunflower and Mid-Kansas measure their credit strength?

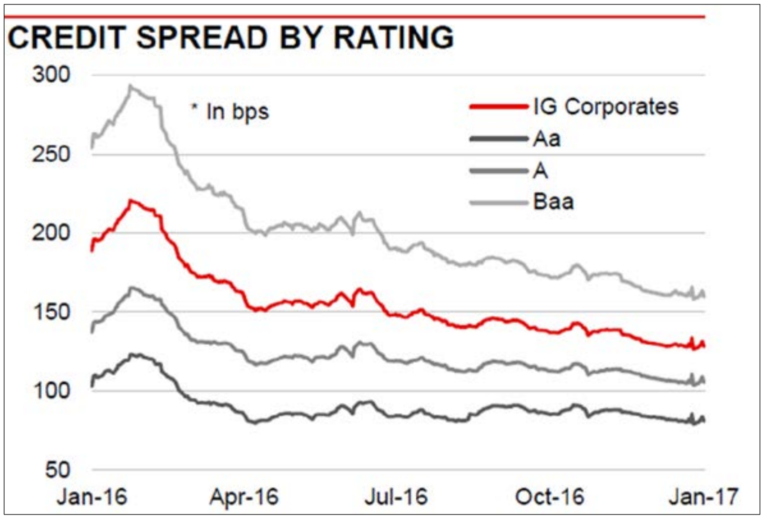
A. Neither Sunflower nor Mid-Kansas have undertaken to be rated by any credit rating agencies. The most objective measure is through Moody's which publishes a credit rating matrix for Cooperative G&T's that we can use as guidance.

Q. How have you assessed the credit of the proposed merged entity?

A. Using the Moody's credit rating matrix, I have evaluated the standalone entities and the combined entity. As expected, the credit of the merged entity is between the credit of the individual companies. However, as Mid-Kansas has the lower standalone credit but the greater historical borrowing needs, the credit of new borrowings in the merged entity will be better than the credit achieved by the standalone entities.

Q. How will the better credit affect Mid-Kansas borrowings?

A. We believe Mid-Kansas is an investment grade (Baa) entity. The merged entity, we believe will be an A-rated entity. The credit spread (premium to government grade investments) is higher for Baa-rated than for A-rated entities. This spread can vary over time. As can be seen in the illustration below, for the period January 2016 to January 2017 the difference ranged from 0.50% to 1.30% (50 to 130 basis points).



Source: MUFG Capital Markets Weekly IG Market Update 20 January 2017

Q. How much would stronger credit be worth?

A. As the chart above shows, spreads can vary greatly and at times become relatively large. At the low end, we expect we could save 0.125% (12.5 bps), at the high end perhaps 0.50% (50 bps).

<u>Merger Savings</u>

Q. Have you assessed the potential for merger related savings?

A. Yes. In addition to the potential interest savings noted above, there are is also some potential for labor and outside service cost savings.

Q. Please describe the potential labor savings.

A. Because we already serve both companies with a single Sunflower workforce, and we already jointly dispatch, operate and plan both systems, most savings will come from the elimination of doing things twice. For example, we will only need one audit, one tax return, one budget, one annual transmission formula rate filing, one monthly board meeting, one monthly board report, one KCC annual report – instead of two of each. We have identified approximately 125 to 200 duplicate processes that will be eliminated post-merger. Particularly in the financial services area, we expect to reduce workload annually by about 1,200 hours. We are likely to see benefits from increased productivity rather than reduction of annual salaries. Likewise, we will see a general reduction in work complexity as accounting codes are reduced from two companies to one, and cost assignments and allocations can be simplified or eliminated with the elimination of one company.

Q. Will any employee positions be eliminated as a result of the merger?

A No.

Q. Will there be any outside service savings?

A. Yes. We do incur duplicate costs to perform two annual financial audits and make various company filings for both companies, and utilize consultants to support the separate companies in, for example, load forecasts and rate design. Some of these occur annually, like financial audits, load forecasts, and formula rate filings. Other studies like rate design and depreciation studies, typically occur every three to five years. We estimate savings of about $500,000 per year.

Q. Are there other savings to consider?

A. Yes, but we have not fully quantified these. As noted above, we expect the credit strength of the merged company to be better than the standalone companies. This is expected to lower borrowing costs (interest rates). In part, this is because we believe added scale (size) will improve our rate stability and lower exposure to rate shocks, a factor considered by rating agencies. Additionally, while we currently maintain two indentures and two lines of credit for the two companies, we will be able to eliminate one.

Q. How will these savings be shared with customers?

A. In a cooperative business model, our customers are our owners. Whether the benefits go directly to the retail customers or to our Members, the savings eventually benefit the retail customers. Practically speaking, we set our Member rates annually through our budget process. Cost savings will be reflected in the budgets and in the resulting rates. Amounts that are retained in net income become capital credit allocations to our Members that may be redeemed in future years for cash.

<u>Rate Stability and Generation Diversity</u>

Q. Please explain further the impact of the merger on rate stability.

A. The merger will stabilize rates against short-term and long-term potential rate shocks. This increased stabilization is the result of both the increased scale of the merged company and the combined generation resources.

Q. How does scale stabilize rates against short-term and long-term rate shocks?

A. Short-term rate shocks can include events such as unexpected customer load changes. In a given year, such events are more likely to impact one standalone company, rather than both. In some years, the impact will be on the Sunflower side, in other years the impact will be on the Mid-Kansas side. Long-term rate shocks can result from the need for rapid capital investment or changing technology or regulation. Sharing the impact of these types of events across both companies' loads will halve the rate impact of such events.

Q. How will the combined generation resources help stabilize rates?

A. By merging, the customers of both companies will experience greater fuel diversity, reducing the potential impact on rates due to a significant increase in a specific fuel-type. In some ways, the two companies already benefit from their combined resources. For example, Mid-Kansas and Sunflower utilize their combined resources to meet SPP capacity requirement rules. Additionally, Mid-Kansas and Sunflower report their renewable resources together to the Commission. In other ways, the resources are not combined. Although the generation resources were jointly dispatched by Sunflower from April 2007 until March 2014, and, since March 2014, the resources have been jointly dispatched by SPP, the generation resource revenues and costs have been identified to the standalone companies. Since Sunflower's resources are heavily weighted to coal, and Mid-Kansas' resources are heavily weighted to natural gas, the two companies' standalone generation costs vary differently because of their different resource mixes. Absent action by the two boards, these resource mix differences will increase in 2019, when the Mid-Kansas purchase power agreement ("PPA") with the Westar Jeffrey Energy Center coal resource ends. Mid-Kansas will become even more natural gas dependent compared to Sunflower. Merging the two companies equalizes their mix of resources. Mid-Kansas gains fuel diversity with coal while Sunflower gains fuels diversity with greater natural gas, wind and solar. The merged entity has one-third less coal than the standalone entities had from 2007 to 2018.

Q. What actions have the Sunflower and Mid-Kansas Boards of Directors taken regarding fuel diversity?

A. Sunflower's Power Supply department worked extensively with both the Mid-Kansas and the Sunflower Boards of Directors. After consideration, both Boards concluded that over-dependence on one fuel type is undesirable and fuel diversity, including some coal, is desirable. Additionally, as noted above, although combined loads and resources are presented to SPP, the standalone loads and resources are separately accounted for in the two companies. One company may be longer in total resources and one shorter, with each company paying the cost or getting the benefit of their standalone long or short position. The solution for 2019 was a resource rebalance – essentially an adjustment to the allocation of costs between the two companies under the operating agreement. Sunflower, which was long with coal resources, would allocate a block of coal to Mid-Kansas which was short on coal resources, and Mid-Kansas which was long on natural gas, would allocate a block of natural gas resources to Sunflower which was short natural gas. The two companies have been operated as an integrated electric system. Consistent with that operation, both boards desired that the rebalance be executed in a manner that would result in a prudent mix of resources for both companies and in a manner that would continue to support rate convergence.

Q. What is the long-term solution?

A. Rather than having a cost allocation between the two companies, merging the two companies and having a single Member rate achieves a simpler and more permanent solution to rate convergence and resource mix for 2020 and the following years.

<u>Debt Plan</u>

Q. You mentioned Sunflower and Mid-Kansas have separate borrowings. How will the debt be handled in the merged entity?

A. In 2012, when Mid-Kansas issued its private placement debt, we included provisions in the indenture for the potential merger of Mid-Kansas and Sunflower. The existing debt of Mid-Kansas was rolled under an indenture and the private placement debt was issued under the indenture. The Mid-Kansas indenture provides that the Mid-Kansas debt can be transferred to Sunflower if Mid-Kansas merges with Sunflower, provided that Sunflower has an indenture substantially the same as Mid-Kansas'. At the end of 2016, when Sunflower made its final payments on the RUS secured debt, we put a Sunflower indenture in place for all Sunflower secured debt. This Sunflower indenture, although not identical to Mid-Kansas', has limited differences. During these transactions and in discussions with our lenders, it has been the expectation to roll the Mid-Kansas debt under the Sunflower indenture upon merger.

Regulation

Q. Will the merger impact the Commission's jurisdiction and capacity to regulate the surviving entity?

A The Commission's jurisdiction and capacity to regulate the merged company will remain the same as its capacity to regulate the two companies.

The merger will reduce the KCC annual report filing to one. Often both Mid-Kansas and Sunflower are parties to dockets. After merger there will be only one company to participate in dockets. We will have only one transmission formula rate, instead of two. Included with the savings previously mentioned are annual regulatory cost savings of about $250,000. The merger will reduce the number of regulatory filings, streamlining the existing regulatory process and reducing costs borne by our customers.

Member Impacts

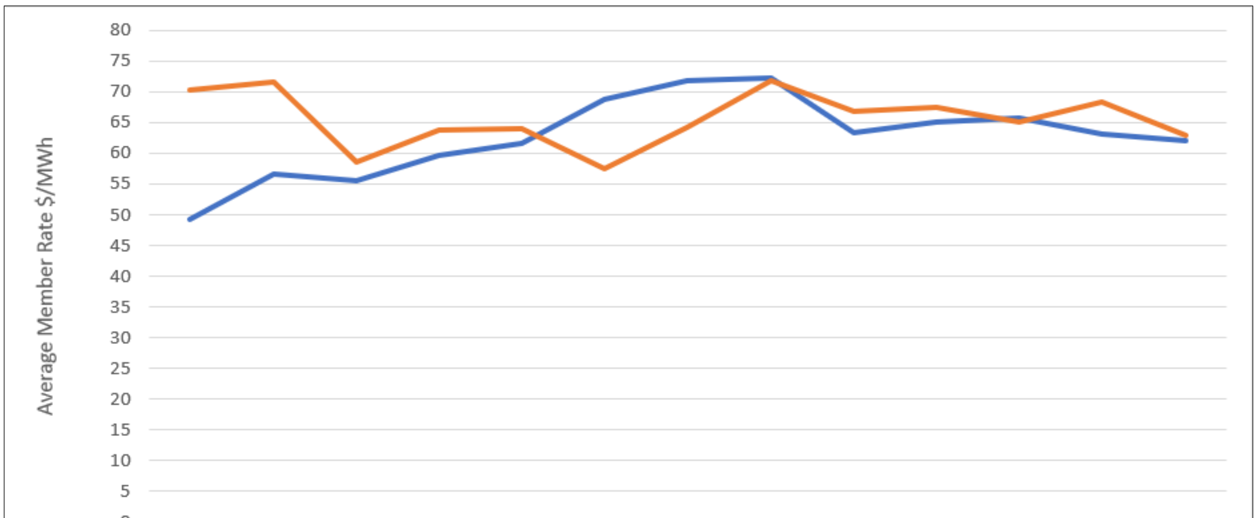
Q. What is the impact of the merger on the Members?

A. The primary impact is the ability to move from two companies under common operation and planning with separate resource mixes, equity levels, credit strengths and rates to a single company with common resources, equity, credit strength, and a single rate. Because the rates to our Members are close together now, the impact on the individual Members will be small. After merger, as Sunflower and Mid-Kansas do today, Sunflower will continue to manage costs and service in a way that provides reliable, affordable energy to the public we and our Members serve. The merger will not alter Sunflower's ongoing commitment to our Members to provide energy at the lowest cost possible while still providing reliable service.

Q. How will merging the rates of Mid-Kansas and Sunflower impact the Member rate?

A. The Mid-Kansas and Sunflower rates have been fairly close for a number of years. Sometimes the Mid-Kansas rate has been higher, sometimes the Sunflower rate has been higher. Below is a graph of the average Member rates for each company. As one can see, the 2019 rates are expected to be fairly close. If merger is approved, the merged company will have a single rate for all Members.

<u>Comparison of Sunflower and Mid-Kansas Average Member Rates</u>



	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018P	2019P
SEPC	49.32	56.68	55.56	59.67	61.66	68.75	71.92	72.18	63.41	65.19	65.80	63.15	62.14
MKEC	70.28	71.65	58.47	63.83	64.1	57.47	64.21	71.81	66.74	67.54	65.13	68.26	62.91

Q. How will Member equity be treated?

A. Each Member will retain the same total equity upon merger as it had in the individual companies. This will preserve their historical equity positions and preserve their relative capital credit positions. Each Member will continue to earn equity and capital credits after the merger essentially as before. At merger, Southern Pioneer will become a Class B member of Sunflower and enter into a wholesale power purchase agreement with Sunflower on the same terms and conditions as the other Sunflower Members. Southern Pioneer will earn capital credits based on usage in the same manner as the other Members. Pioneer and its wholly-owned subsidiary Southern Pioneer will, together, have one set of seats on the Sunflower Board. The treatment of Member equity is addressed in the Merger Agreement and Bylaws attached to the Merger Agreement (attached to the Joint Application as Exhibit JA-2) which all Members have approved.

Q. Does this conclude your testimony?

A. Yes.

VERIFICATION

STATE OF KANSAS)
) ss:
COUNTY OF Ellis)

H. Davis Rooney, being first duly sworn, deposes and says that he is the H. Davis Rooney referred to in the foregoing document entitled "PREFILED DIRECT TESTIMONY OF H. DAVIS ROONEY" before the State Corporation Commission of the State of Kansas and that the statements therein were prepared by him or under his direction and are true and correct to the best of his information, knowledge and belief.

H Davis Rooney
H. Davis Rooney

SUBSCRIBED AND SWORN to before me this 3rd day of August, 2018.

NOTARY PUBLIC - State of Kansas
Reneé K. Braun
My Appt. Expires 4/30/2022

Renee K. Braun
Notary Public

My Appointment Expires: