**BEFORE THE STATE CORPORATION COMMISSION
OF THE STATE OF KANSAS**

In the Matter of the Application of Kansas Power	**)**	
Pool for a Certificate of Convenience and Authority	**)**	
to Transact the Business of an Electric Public Utility in the State	**)**	**Docket No. 18-KPPE-343-COC**
of Kansas for Transmission Rights Only	**)**	
to Cross Service Territory of Southern Pioneer Electric	**)**	
Company and Ninnescah Rural Electric Company	**)**	

CROSS-ANSWERING TESTIMONY

PREPARED BY

JUSTIN T. GRADY

UTILITIES DIVISION

KANSAS CORPORATION COMMISSION

July 16, 2018

Contents

I. Introduction, Purpose of Testimony, Areas of Testimony Response

Q. Please state your name and business address.

A. My name is Justin T. Grady and my business address is 1500 Southwest Arrowhead Road, Topeka, Kansas, 66604.

Q. Are you the same Justin T. Grady that filed Direct Testimony in this matter on July 9, 2018?

A. Yes.

Q. What is the purpose of your testimony in this matter?

A. In the testimony that follows, I will respond to the testimony of H. Davis Rooney and Corey W. Linville, filed on behalf of Southern Pioneer and Mid-Kansas Electric Company (MKEC) in this Docket. Both of these witnesses filed testimony addressing the same subject as my Direct Testimony in this Docket, that is, the economic analysis of the Kingman Direct Connection (KDC) performed by Larry Holloway on behalf of KPP. In several areas, these witnesses drew different conclusions than I did when I reviewed Mr. Holloway's analysis. In the testimony that follows, I will address and respond to those differences of opinion for clarity of the record and to aid the Commission in its decision making in this Docket.

Q. What issues are you responding to in these witnesses Direct Testimony?

A. First, I will respond to the portions of Mr. Rooney's testimony pertaining to the proper recognition of financing costs and capital investment outlay in a traditional Net Present Value (NPV) analysis. Then, I will address Mr. Rooney's arguments that KPP's avoidance of Southern Pioneer's Local Access Delivery Charge (LAC or LADS) should not be considered in the analysis. Third, I will address Mr. Rooney's use of different capital, O&M cost, and metering loss estimates. Lastly, I will address Mr. Linville's testimony regarding the estimated value of capacity sales from Kingman's generating units in Mr. Holloway's economic analysis.

II. Response to Mr. Rooney's Direct Testimony

A. Recognition of Financing Costs in NPV Analysis

Q. Please recap Mr. Rooney's testimony regarding the recognition of financing costs in the economic analysis.

A. On pages 15 through 17, Mr. Rooney discusses Mr. Holloway's economic analysis of the KDC. In this testimony, Mr. Rooney criticizes Mr. Holloway's inclusion of financing costs and his exclusion of capital investment costs, in the economic evaluation of the KDC. Additionally, Mr. Rooney disagrees with the discount rate chosen by Mr. Holloway for the analysis.

Q. When you reviewed Mr. Holloway's economic analysis of the KDC, did you have the same criticisms of the analysis?

A. I did not disagree with Mr. Holloway's inclusion of financing costs in the economic analysis instead of the capital cost outlay of the investment. However, I did present testimony disagreeing with Mr. Holloway's choice of discount rates for the analysis.

Q. Since you did not present the same criticism of Mr. Holloway's analysis as Mr. Rooney, do you disagree with Mr. Rooney's testimony?

A. Not entirely. Much of Mr. Rooney's testimony discusses the traditional corporate finance perspective on the proper treatment of financing costs when performing a traditional cost benefit analysis using the NPV methodology. That is, the proper way to include the impact of financing costs in an NPV analysis is to reflect the cost of financing indirectly in the determination of the discount rate applied to discount future cash flows, as opposed to directly including forecasted cash flows associated with the financing in the analysis.

While I agree with Mr. Rooney's portrayal of corporate finance theory in discussing the proper method of recognizing investment outlays and financing costs when performing an NPV calculation, I don't agree that the strict corporate finance perspective is the only appropriate way to conduct a cost/benefit analysis in a regulatory proceeding such as this. As Mr. Rooney discusses in his testimony, financing costs are often considered directly in regulatory cost/benefit analyses when net present value revenue requirement calculations are performed.

I would also point out that much of corporate finance theory and application that Mr. Rooney refers to pertains to for-profit corporations, with observed costs of debt and estimated costs of equity (based on the required level of economic profit necessary to induce investment in the for profit enterprise). It goes without saying that neither Kingman nor KPP is a for-profit entity with a purely defined capital structure or cost of equity.

For these reasons, I did not object to Mr. Holloway's direct inclusion of financing costs in his economic analysis of the KDC. Additionally, as long as the discount rate used in the NPV analysis is the same as the cost of financing used to derive the annuity (bond) payments, the resulting impact to the NPV analysis is the same whether you reflect the cost of the investment outlay at the beginning of the project or you forecast future cash flows associated with financing and then discount them to the present day values.

B. Recognition of Avoided LAC Charges in the Economic Analysis

Q. What is Mr. Rooney's position on the inclusion of avoided LAC charges being included in the economic analysis?

A. Mr. Rooney states on page 25 of his Direct Testimony that he "removed the LADS charges shifted from KPP customers to SPEC customers….because they are reallocations of costs among members of the public, not incremental cost reductions benefitting the public as a whole." Later on pages 36 and 37, Mr. Rooney testifies that "The Kingman Direct Connection only produces a net benefit to KPP by being able to shift the LADS charges to other ratepayers." Mr. Rooney goes on, "Even without uplift to the zone, by building a more expensive project than necessary, KPP will shift the cost of its LADS charges to other customers."

Q. Do you agree that the Commission should not consider the impact of KPP's ability to avoid paying Southern Pioneer's LADS charge in the economic evaluation of KPP's KDC?

A. No. I believe that is appropriate to consider KPP's ability to avoid the LADS charge from Southern Pioneer by completing the KDC. Additionally, I do not agree with the testimony that describes this cost avoidance by KPP as a "cost shift" to other customers. While I agree that the result will be that Southern Pioneer's other customers will pay more if KPP leaves the Southern Pioneer 34.5 kV system, I do not agree with the premise that the resulting rate increases to those customers will be a detriment to the public interest that exactly offsets any benefit to the public by KPP avoiding the LAC charges.

Q. If KPP leaves the 34.5 kV system and Southern Pioneer's rates go up, why is that not a detriment to the public interest that exactly offsets the public interest gain achieved by KPP avoiding the LAC charges?

A. KPP leaving the Southern Pioneer 34.5 kV system to serve the Kingman load would simply be reverting back to the state of affairs that existed prior to 2005 when KPP built 26 miles of 34.5 kV line to connect to the Cunningham substation. In other words, by taking service over Southern Pioneer's 34.5 kV system today (and paying the LAC charge), KPP is contributing credits to the cost of service that Southern Pioneer doesn't have to recover from other retail and wholesale customers of Southern Pioneer, which is a benefit to those customers, no doubt. But, if KPP never voluntarily elected to take service from Southern Pioneer, the costs of the 34.5 kV system would still exist, and they would be recovered from other Southern Pioneer customers. KPP's decision to leave the 34.5 kV system does not cost Southern Pioneer customers "more", it simply returns them to the status quo from thirteen years ago. It cannot, therefore, be considered a detriment to the public interest for Southern Pioneer's customers to pay for the costs of a system that serves them. It is however, in the public interest for KPP's customers to avoid having to pay for the costs of a system that they no longer desire to use.

C. Capital Cost, O&M, and Metering Loss Assumptions

Q. Does Mr. Rooney's analysis refer to different estimates of the capital investment costs of the different projects being considered?

A. Yes. While Mr. Rooney refers to different capital investment cost estimates of the KDC and Southern Pioneer project, he ultimately uses similar estimated capital investment costs to those Mr. Holloway used in his analysis. As I mentioned in my Direct Testimony, I do not object to using the most recent or reliable estimated investment costs of the projects in the economic evaluation. While this is a material consideration in the economic evaluation, it pales in comparison to the question of whether the avoided LAC charge should be included in the benefits to the public associated with the request to build the line.

Q. Does Mr. Rooney's analysis use different estimates of operating and maintenance costs of the different projects being considered?

A. Yes. Beginning on page 19 of Mr. Rooney's testimony, he addresses his difference of opinion regarding the proper O&M expense amount for the competing projects, expressed as a percentage of net plant. Mr. Rooney criticizes Mr. Holloway's estimated O&M as a percentage of net plant (3%) for the following reasons:

1. It is based on a comparison of the costs that other utilities report on 345 kV transmission facilities, not 34.5 kV facilities; and
2. It is based on facilities that are of newer construction vintage and, thus, doesn't properly reflect the fact the escalation of O&M expenses over the life of the plant.

Accordingly, Mr. Rooney recommends using 6% of Net Plant for the amount of O&M expenses. Mr. Rooney arrives at this number by comparing the O&M percentage used in setting the revenue requirement for the City of Winfield's transmission revenue requirement in Docket No. 12-KPPE-630-MIS and the current rate of Southern Pioneer's O&M as a percentage of net plant.

Q. Do you agree with Mr. Rooney's analysis of this issue?

A. Not entirely. First, Mr. Rooney fails to mention that the actual O&M as a percentage of net plant calculated when Mr. Holloway reviewed other transmission formula rates was 1.79%. Mr. Holloway used 3% in his analysis. So, the near doubling of the O&M expenses used in the analysis compared to the proxy group does account for some of Mr. Rooney's criticisms regarding the comparison of 345 kV and 34.5 kV O&M cost rates.

Second, the ratio being calculated here is O&M expense divided by net plant. Therefore, as the plant in question ages, the net plant decreases as additional accumulated depreciation is recorded over time. This has the effect of increasing the O&M as a percentage of net plant, regardless of whether the actual O&M amount is increasing. This is relevant because Mr. Rooney's estimated O&M percentages were all derived from plant that is at least ten years old (half the time horizon used in Mr. Holloway's analysis). Mr. Holloway's estimated O&M expense rate is applied to the first year of the investment and then inflated at 2% for the life of the project. Because the O&M expense rate is applied to a larger plant balance (before any depreciation expense has accumulated), the resulting O&M expense might not be as unreasonable as Mr. Rooney presents. Ultimately, this issue is not that material as it does not sway the determination that the KDC is economical from KPP's perspective.

Q. Does Mr. Rooney's analysis use different estimates of the electrical losses that will be experienced as a result of the KDC or the Southern Pioneer project?

A. Yes. On pages 22 and 23, Mr. Rooney describes his differences of opinion with Mr. Holloway regarding the metering losses that Kingman will save as a result of avoiding losses on the Southern Pioneer 34.5 kV system. Mr. Rooney's estimated loss calculation relies on a loss study performed by Mid-Kansas and sponsored by Dr. Ala Tamimi. The loss study in Dr. Tamimi's testimony estimates losses to the system as a whole, as opposed to just the losses that the City of Kingman will save on the billing from KPP. I can see the perspective of both KPP and MKEC on this issue, so I don't have a specific recommendation for the Commission as to which losses amount to use. Ultimately, in terms of materiality, this issue pales in comparison to the issue of whether it is appropriate to consider in the economic analysis KPP's ability to avoid paying Southern Pioneer's LAC charge by taking transmission service directly from SPP over MKEC's transmission facilities.

III. Response to Mr. Linville's Direct Testimony

Q. Please describe the testimony of Mr. Linville that you are responding to.

A. I am responding to the portions of Mr. Linville's testimony that pertains to KPP's projected capacity sales revenue from the generating units in Kingman. Mr. Linville raises two points of contention regarding the possibility of capacity sale revenue from the Kingman generating units. First, Mr. Linville points out that KPP is capacity deficient after 2022 if we assume the current capacity contract with Westar expires as written. Second, Mr. Linville points out that KPP is currently pooling its available capacity (including the Kingman generator units) in order to sell excess capacity to third parties in SPP. Therefore, Mr. Linville argues that there is no incremental benefit to KPP or the City of Kingman associated with KPP bypassing Southern Pioneer's LAC system.

Q. Do you agree with Mr. Linvilles's testimony?

A. I agree that Mr. Linville raises some valid points. Based on the evidence that Mr. Linville presented regarding KPP's Resource Adequacy Workbook that is submitted to SPP, it does appear that KPP will only have excess capacity to sell until 2022, assuming the Westar contract expires as written. Also, Mr. Linville presents a cogent argument that KPP is already receiving value from its Kingman units as part of a pooled capacity arrangement which makes it possible for KPP to have excess capacity to sell. However, I'm also aware of a real and relatively recent example in which a capacity contract between KMEA and KPP selling capacity from the Kingman generation units was terminated early because KMEA was assessed Southern Pioneer's LAC charge. The history and facts specific to that situation can be found in Docket No. 15-MKEE-461-TAR. So, while I agree that in theory these units could be "pooled" to produce excess capacity, in the event that these units were specifically designated as providing capacity sales outside of the MKEC 34.5 kV footprint, there would be a Southern Pioneer LAC assessed, which would make capacity sales from these units uneconomical.

Q. Should the Commission include the value of capacity sales from Kingman's generating units as part of the economic analysis of the KDC?

A. Before I make that recommendation, I would prefer to read the rebuttal testimony of Mr. Holloway in response to Mr. Linville's statements. Specifically, whether KPP plans to have excess capacity to sell after 2022 and whether there is anything that prohibits KPP from "pooling" the capacity associated with the Kingman units to make capacity sales today, without the KDC.

Q. Does that conclude your testimony?

A. Yes.

STATE OF KANSAS)
) ss.
COUNTY OF SHAWNEE)

VERIFICATION

Justin T. Grady, being duly sworn upon his oath deposes and says that he is Chief-Accounting and Finance, Utilities Division, of the State Corporation Commission of the State of Kansas, that he has read and is familiar with the foregoing *Cross-Answering Testimony* and that the statements contained therein are true and correct to the best of his knowledge, information and belief.

Justin T. Grady
Chief-Accounting and Finance, Utilities Division
State Corporation Commission of the
State of Kansas

Subscribed and sworn to before me this 16th day of July, 2018.

PAMELA J. GRIFFETH
Notary Public - State of Kansas
My Appt. Expires 08-17-2019

Notary Public

My Appointment Expires: August 17, 2019

CERTIFICATE OF SERVICE

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I, the undersigned, certify that a true and correct copy of the above and foregoing Cross-Answering Testimony was served by electronic service on this 16th day of July, 2018, to the following:

GLENDA CAFER, ATTORNEY
CAFER PEMBERTON LLC
3321 SW 6TH ST
TOPEKA, KS 66606
Fax: 785-233-3040
glenda@caferlaw.com

TERRI PEMBERTON, ATTORNEY
CAFER PEMBERTON LLC
3321 SW 6TH ST
TOPEKA, KS 66606
Fax: 785-233-3040
terri@caferlaw.com

BRIAN G. FEDOTIN, DEPUTY GENERAL COUNSEL
KANSAS CORPORATION COMMISSION
1500 SW ARROWHEAD RD
TOPEKA, KS 66604
Fax: 785-271-3354
b.fedotin@kcc.ks.gov

MICHAEL NEELEY, LITIGATION COUNSEL
KANSAS CORPORATION COMMISSION
1500 SW ARROWHEAD RD
TOPEKA, KS 66604
Fax: 785-271-3167
m.neeley@kcc.ks.gov

ROBERT VINCENT, LITIGATION COUNSEL
KANSAS CORPORATION COMMISSION
1500 SW ARROWHEAD RD
TOPEKA, KS 66604
Fax: 785-271-3354
r.vincent@kcc.ks.gov

JANET BUCHANAN, DIRECTOR- REGULATORY AFFAIRS
KANSAS GAS SERVICE, A DIVISION OF ONE GAS, INC.
7421 W 129TH ST
OVERLAND PARK, KS 66213-2713
Fax: 913-319-8622
janet.buchanan@onegas.com

TERESA MILLER, GEN. MANAGER
NINNESCAH RURAL ELECTRIC COOPERATIVE ASSN., INC.
275 NE 20th ST
PO BOX 967
PRATT, KS 67124-0967
Fax: 620-672-6852
tmiller@ninnescah.com

MARY KAY MILLER, VICE PRES, REGULATORY & GOV AFFAIRS
NORTHERN NATURAL GAS
1111 S 103RD STREET (68124)
PO BOX 3330
OMAHA, NE 68103-0330
Fax: 402-398-7006
mary.kay.miller@nngco.com

LINDSAY CAMPBELL, EXECUTIVE VP - GENERAL COUNSEL
SOUTHERN PIONEER ELECTRIC COMPANY
1850 W OKLAHOMA
PO BOX 403
ULYSSES, KS 67880-0430
Fax: 620-356-4306
lcampbell@pioneerelectric.coop

STEPHEN J. EPPERSON, CHIEF EXECTUTIVE OFFICER
SOUTHERN PIONEER ELECTRIC COMPANY
1850 W OKLAHOMA
PO BOX 403
ULYSSES, KS 67880-0430
Fax: 620-356-4306
sepperson@pioneerelectric.coop

CERTIFICATE OF SERVICE

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RANDY MAGNISON, EXEC VP & ASST CEO
SOUTHERN PIONEER ELECTRIC COMPANY
1850 W OKLAHOMA
PO BOX 403
ULYSSES, KS 67880-0430
Fax: 620-356-4306
rmagnison@pioneerelectric.coop

RENEE BRAUN, CORPORATE PARALEGAL, SUPERVISOR
SUNFLOWER ELECTRIC POWER CORPORATION
301 W. 13TH
PO BOX 1020 (67601-1020)
HAYS, KS 67601
Fax: 785-623-3395
rbraun@sunflower.net

JAMES BRUNGARDT, MANAGER, REGULATORY RELATIONS
SUNFLOWER ELECTRIC POWER CORPORATION
301 W. 13TH
PO BOX 1020 (67601-1020)
HAYS, KS 67601
Fax: 785-623-3395
jbrungardt@sunflower.net

DAVIS ROONEY, VICE PRESIDENT AND CFO
SUNFLOWER ELECTRIC POWER CORPORATION
301 W. 13TH
PO BOX 1020 (67601-1020)
HAYS, KS 67601
Fax: 785-623-3395
hrooney@sunflower.net

AL TAMIMI, VICE PRESIDENT, TRANSMISSION PLANNING AND POLICY
SUNFLOWER ELECTRIC POWER CORPORATION
301 W. 13TH
PO BOX 1020 (67601-1020)
HAYS, KS 67601
Fax: 785-623-3395
atamimi@sunflower.net

AMY FELLOWS CLINE, ATTORNEY
TRIPLETT, WOOLF & GARRETSON, LLC
2959 N ROCK RD STE 300
WICHITA, KS 67226
Fax: 316-630-8101
amycline@twgfirm.com

TIMOTHY E. MCKEE, ATTORNEY
TRIPLETT, WOOLF & GARRETSON, LLC
2959 N ROCK RD STE 300
WICHITA, KS 67226
Fax: 316-630-8101
temckee@twgfirm.com

MARK D. CALCARA, ATTORNEY
WATKINS CALCARA CHTD.
1321 MAIN ST STE 300
PO DRAWER 1110
GREAT BEND, KS 67530
Fax: 620-792-2775
mcalcara@wcrf.com

TAYLOR P. CALCARA, ATTORNEY
WATKINS CALCARA CHTD.
1321 MAIN ST STE 300
PO DRAWER 1110
GREAT BEND, KS 67530
Fax: 620-792-2775
tcalcara@wcrf.com

Pamela Griffeth

Pamela Griffeth
Administrative Specialist