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Kansas Corporation Commission
/S/ Patrice Petersen-Klein

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BEFORE THE CORPORATION COMMISSION

OF THE STATE OF KANSAS

IN THE MATTER OF THE APPLICATION OF MID-KANSAS ELECTRIC COMPANY, LLC FOR APPROVAL TO MAKE CERTAIN CHANGES IN ITS CHARGES FOR ELECTRIC SERVICES IN THE GEOGRAPHIC SERVICE TERRITORY SERVED BY LANE SCOTT ELECTRIC COOPERATIVE, INC.	]	KCC Docket No. 12-MKEE-410-RTS

CROSS ANSWERING TESTIMONY OF

ANDREA C. CRANE

ON BEHALF OF

THE CITIZENS' UTILITY RATEPAYER BOARD

December 10, 2012

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A. Introduction

Q. Please state your name and business address.

A. My name is Andrea C. Crane and my business address is 90 Grove Street, Suite 211, Ridgefield, Connecticut 06877. (Mailing Address: PO Box 810, Georgetown, Connecticut 06829.)

Q. Did you previously file testimony in this proceeding?

A. Yes, I filed Direct Testimony in this case on November 30, 2012. In my Direct Testimony, I addressed two issues relating to the Rate Application filed on April 2, 2012 by the Mid-Kansas Electric Company ("MKEC") for customers served in the Lane Scott portion of its service territory ("Lane Scott Division" or "Company"). In that Rate Application, the Lane Scott Division sought a rate increase of $510,915 or approximately 13.34%, based on a rate base/rate of return methodology. In my Direct Testimony, I recommended that the KCC adjust the Company's rate base claim to reflect the actual amount paid for the Aquila assets by the Lane Scott Division. In addition, I also provided recommendations regarding the Lane Scott Division's financial and managerial relationship to Lane Scott Electric Cooperative, Inc., which owns the native system and the assets of the Lane Scott Division. Direct Testimony on behalf of CURB was also filed by Stacey Harden and Benjamin D. Cotton.

Q. What is the purpose of your Cross-Answering Testimony?

A. My Cross-Answering Testimony is being filed in response to Direct Testimony filed by the

KCC Staff. Specifically, my Cross-Answering Testimony will address four aspects of Staff's testimony:

1. Staff's proposal to update the Test Year to reflect actual results through September 30, 2012;
2. Staff's proposal to set rates based on a Times Interest Earned Ratio ("TIER") of 2.0;
3. Staff's alternative rate base/rate of return proposal that reflects a cost of equity of 14.25%;
4. A recommendation that any margin awarded the Lane Scott Division should be retained within the Lane Scott Division.

B. Test Year Concept

Q. What Test Year did the Company utilize in its Rate Application?

A. In its filing, the Lane Scott Division utilized the Test Year ending December 31, 2010.

Q. What Test Year did Staff utilize to develop its revenue requirement recommendations?

A. Staff updated certain aspects of the Company's filing to September 30, 2012. Specifically, Staff updated the Company's rate base components to September 30, 2012. In addition, it updated the Company's payroll expense and depreciation expense claims to September 31, 2012 and updated the Company's rate case expense claim to reflect costs at November 10, 2012. Other adjustments made by Staff to dues, donations, lobbying , advertising, and non-recurring costs were based on the 2010 Test Year expenses.

Q. Do you believe that Staff's adjustments to update certain components of the Test Year to September 30, 2012 are appropriate?

A. No, I do not. The Lane Scott Division chose to file this case based on the 2010 Test Year. Moreover, in that filing, the Company had the opportunity to propose adjustments based on known and measurable changes to the Test Year. Staff's attempt to update much of the filing with actual results that are almost two years beyond the end of the Test Year violates the Test Year concept. One of the purposes of requiring utilities to file a Test Year, which is based on historic results, is that it provides the other parties with a framework on which to evaluate the utility's filing within the 240-day time constraint imposed by statute. Updating for actual results as the case progresses requires parties such as CURB to continually chase after a moving target. While the KCC has historically permitted known and measurable changes to the Test Year, these proposed known and measurable changes should be included as part of a utility's initial filing so that the parties have a reasonable opportunity to review any known and measurable changes during the discovery process. The ratemaking process should not be based on a floating test year that simply updates each month with actual results.

Moreover, the Company had the opportunity to file its case based on a more recent Test Year. It chose not to do so. In this case, it is Staff that has taken upon itself to propose extending the Test Year to September 30, 2012. Staff has proposed similar extensions in other cases even if, as here, such extensions have not been proposed by the utility. If Staff is permitted to extend the Test Year in its Direct Testimony filed in response to utility rate applications, then CURB will have no way of knowing what Test Year will be utilized to set rates until Staff actually files its Direct Testimony in any given case. This not only places an unreasonable burden on CURB but it also violates the Test Year principle. As noted, Staff has updated rate base and a few operating expenses, but revenues and many other expenses are based on the 2010 Test Year, resulting in a mixed presentation. Staff's propensity to update portions of the Test Year is even more curious in this case, since Staff found that, at least through December 31, 2011, "Lane-Scott's revenue, expense, and plant values had not changed significantly from those values contained in the test year."[1]

Q. What do you recommend?

A. Given that a) the Lane Scott Division proposed to utilize calendar year 2010 as its Test Year, b) there has been little change in operations since the 2010 Test Year, and c) other parties in this case should not be put in the position of chasing a moving test year target, I recommend that the KCC base the Company's revenue requirement on actual results for the twelve months ending December 31, 2010, adjusted for known and measurable changes at the time of the Company's filing. This recommendation is consistent with the revenue requirement presented in Ms. Harden's Direct Testimony in this case.

C. Times Interest Earned Ratio ("TIER")

Q. What concerns do you have about the TIER of 2.0 recommended by Staff?

A. If the KCC adopts Staff's recommendation to utilize a TIER approach to set rates for the

[1] Testimony of Mr. Bell, page 5.

Lane Scott Division, then I believe that the TIER of 2.0 recommended by Staff is excessive. As noted by Staff witness John Bell on page 29 of his Direct Testimony, the Rural Utilities Service ("RUS"),which provides financing to cooperative utilities, requires a TIER of 1.25. Thus, Staff's recommendation provides a "cushion" of 60% over the RUS requirement. I believe that this cushion is excessive, especially in this case where there is no actual outstanding debt.

In prior MKEC cases, Staff has generally recommended a TIER in the range of 2.0. However, in those cases, the cooperative utilities actually had outstanding debt and were required to achieve certain TIER requirements through their bond covenants. There is no such requirement in this case, since the Lane Scott Division has no outstanding debt. Therefore, there is no need to award a TIER that is any higher than the RUS requirement.

Q. What do you recommend?

A. If the KCC utilizes a TIER approach to set rates in this case, then I recommend that a TIER of 1.25 be used to determine the Company's required net margin. This recommendation would reduce Staff's proposed increase by approximately $95,500. In addition, since the Lane Scott Division does not actually have any outstanding debt, the entire margin is available to build up the Company's equity. Assuming imputed interest expense of $127,327 as calculated by Staff, a TIER of 1.25 would provide $159,159 (1.5 X $127,327) in margin that the utility could utilize to improve its equity position. This is a reasonable result if the KCC elects to utilize the TIER methodology.

D. Return on Equity

Q. How did Staff determine the recommended return on equity utilized in its alternative rate base/rate of return analysis?

A. Staff utilized a modified form of the Goodwin Model, which seeks to increase a utility's entity to a target level within a specified period of time. Staff's model assumes a current equity level of 18.80%, a target equity level of 27.00%, and a period of 12 years in which to achieve the targeted equity level. This methodology resulted in a return on equity of 14.25%.

Q. Do you believe that a return on equity of 14.25% is appropriate?

A. No, I do not. If the KCC decides to utilize a rate base/rate of return methodology to set rates, then it should reject Staff's recommended 14.25% and instead utilize the 8.72% return on equity requested by the Lane Scott Division. Not only is 14.25% well above the return on equity requested by the Company, but it is also well above the equity returns being awarded to utilities today. While I understand that Staff's recommendation is based on an accepted form of the modified Goodwin Model, Staff's recommendation is based on actual equity at Lane Scott Electric Cooperative, Inc., an unregulated entity. As an unregulated entity, the management of Lane Scott Electric Cooperative, Inc. may have made financing decisions that would be inappropriate for a regulated utility. It is therefore inappropriate to assume, as Staff has done, that those financing decisions should be utilized as the foundation for the inputs utilized in the modified Goodwin Model to determine the Lane Scott Division's return on equity in this case.

Q. What do you recommend?

A. If the KCC utilizes the rate base/rate of return methodology to set rates, then it should utilize the 8.72% cost of equity requested by the Lane Scott Division. This recommendation is also consistent with the cost of equity recommendations made by CURB in other recent cases and is more in line with current equity awards than the 14.25% proposed by Staff.

E. Use of Net Margins

Q. Do you have any other concerns about the net margins recommended by Staff?

A. Yes, I do. As discussed on page 20 of Mr. Bell's Direct Testimony, at least part of Staff's rationale for imputing interest expense to the Lane Scott Division was that it considers the Company's negative cash balance to be an actual liability of the Lane Scott Division. The Company has repeatedly said that it does not consider this negative cash balance to be a liability and it has never formalized any kind of liability or repayment schedule with Lane Scott Electric Cooperative, Inc.

Regardless of whether the KCC decides to set rates base on the rate base/rate of return approach proposed by the Company or on the TIER approach recommended by Staff, ratepayers should be assured that all future margins are utilized for the benefit of the Lane Scott Division. Thus, the KCC should require any margins authorized in this case to be retained within the Lane Scott Division and should specifically preclude the Company from using any of these margins to "repay" any liability that Lane Scott Electric Cooperative, Inc. may claim in the future relating to the current negative cash balance. In addition, as recommended in my Direct Testimony, any future liabilities between the Lane Scott Division and Lane Scott Electric Cooperative, Inc. should be formalized so that the KCC can ensure that there is no cross-subsidization between regulated and unregulated utilities.

Q. Does this complete your testimony?

A. Yes, it does.

VERIFICATION

STATE OF CONNECTICUT)

COUNTY OF FAIRFIELD) ss:

Andrea C. Crane, being duly sworn upon her oath, deposes and states that she is a consultant for the Citizens' Utility Ratepayer Board, that she has read and is familiar with the foregoing testimony, and that the statements made herein are true to the best of her knowledge, information and belief

Andrea C. Crane

Andrea C. Crane

Subscribed and sworn before me this 8th day of December 2012.

Notary Public

SANDRA QUARFORD
Notary Public
My Commission Expires: My Commission Expires 08/31/2013

CERTIFICATE OF SERVICE

12-MKEE-410-RTS

I, the undersigned, hereby certify that a true and correct copy of the above and foregoing document was served by electronic service this 10th day of December, 2012, to the following parties who have waived receipt of follow-up hard copies:

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