**BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI**

In the Matter of the Joint Application of Great Plains Energy Incorporated, Kansas City Power & Light Company, and Aquila, Inc. for Approval of the Merger of Aquila, Inc. with a Subsidiary of Great Plains Energy Incorporated and for Other Related Relief	))))))	Case No. EM-2007-0374

**CITY OF KANSAS CITY'S PROPOSED FINDINGS OF FACT
AND CONCLUSIONS OF LAW**

Comes now the City of Kansas City, Missouri and submits its Proposed Findings of Fact and Conclusions of Law on the list of issues submitted by the parties in this case on April 16, 2008. The City has limited its Proposed Findings of Fact and Conclusions of Law to the issues on which it has taken a position or on which it has filed and presented testimony.

FINDINGS OF FACT

Issue VII – Municipal Franchise

1. Should Commission approval of the Joint Application be conditioned upon the negotiation of a single, unitary franchise between KCPL/Aquila and the City of Kansas City within nine (9) months of the Commission's approval of the merger?

Throughout this case, the City of Kansas City ("Kansas City") has advised the Commission that it generally favors the proposed merger, but it has also adamantly asserted that to avoid detriment to the public interest the Commission order approving the merger should include several conditions, one of which is a condition whereby Kansas City Power & Light ("KCPL") and Aquila, Inc. ("Aquila") would be required to negotiate a unitary franchise agreement with the City within nine months of merger approval.

There are several persuasive reasons for Kansas City's request. The applicants' service territories are largely contiguous and in some cases overlapping within the city limits of Kansas City. <u>See</u> Tr. p. 42, lns 14-16. The applicants' proposed merger between Aquila and Great Plains Energy, Inc. ("GPE") will significantly integrate operations between Aquila and KCPL within City limits, and the greater Kansas City metropolitan area will be managed as a single district. Ex. 17, Herdegan Supplemental Direct, p. 11, ln 10.

A fundamental reason for Kansas City's request is that KCPL and Aquila currently provide service to Kansas City under separate electric franchise agreements. The franchise agreement between KCPL and Kansas City was executed in 1881 and is less than two pages long. The franchise agreement between Kansas City and Aquila expired on December 31, 2006 and the parties have agreed to operate under the terms and obligations of the expired franchise agreement until January 2009. Tr. p. 2158. The Aquila franchise, a term-limited franchise that is subject to periodic renegotiation, can be revised to accommodate the operational changes resulting from the merger.

There is ample evidence that Kansas City has experienced material difficulties operating under separate franchise agreements with KCPL and Aquila. Kansas City's problems with Aquila have included operational matters such as relocations, communications with personnel, and obtaining service extensions. <u>See</u> Ex. 400, Cauthen Rebuttal, pp. 4-5. Kansas City's issues with KCPL include subordination of rights in the public right-of-way, facility relocation, transparency in operations, and undergrounding. It is not surprising that none of these topics is addressed in the two pages of the KCPL franchise. <u>See</u> Ex. 400, Cauthen Rebuttal, pp. 7-9. KCPL's argument that its franchise provides significant benefits to its customers is found wanting in light of the problems experienced by one of KCPL's largest customers - Kansas City. Ex. 22, Marshall Surrebuttal, p. 14, ln. 2.

KCPL and Kansas City engaged in an effort to modernize their working relationship in 1996, but this effort failed ostensibly because KCPL refused to execute the negotiated operating agreement. Yet during the course of this proceeding, KCPL and Aquila have offered to enter into an operating agreement to address difficulties that might arise in combining their own operations. Ex. 39, Giles Additional Supplemental Direct, p. 3, lns 4-10. KCPL also has requested the Commission to issue any additional orders to ensure that the purposes of the merger be achieved. Opp. of GPE and KCPL to Second Motion in Limine of Indicated Industrials, p. 7. These overtures aside, an operating agreement between Kansas City and KCPL/Aquila that does not contemplate the impact of combined operations on the public is insufficient. Kansas City uniquely lies within the boundaries of each utility's service territory and facilitates the public interest through its role as a steward of the public rights-of-way. In order to prevent detriment to the public, any meaningful attempt to modernize and coordinate activities in the public rights-of-way must start at the legal source: the franchise.

KCPL has argued that the Commission cannot impair KCPL's contractual rights under its existing franchise agreement with Kansas City, or, in the alternative, that consideration of a consolidated franchise in this proceeding would be premature because GPE intends to maintain two separate legal entities for the foreseeable future. Ex. 22, Marshall Surrebuttal, p. 14, lns 2-6; p. 16, lns 22-23. These arguments are rejected.

The Commission agrees with Kansas City that opting into a "unitary franchise" condition on the merger would be strictly voluntary on the part of the applicants. This condition would neither abrogate existing contracts, nor would it order the utilities into a new one; rather, it gives the applicants the choice to honor the precondition. In the absence of a unified agreement, the applicants' proposal to combine operations creates the risk that Kansas City will be exposed to a significant disruption in its ability to effectively manage its rights-of-way. This scenario also would result in a perverse set of circumstances whereby Kansas City would be compelled to renegotiate the expired Aquila franchise with KCPL representatives. Tr. at p. 2208, lns 3-19. As a result of these negotiations, the activities of KCPL employees in the Aquila territory would be governed by a modern franchise agreement, while the activities of KCPL employees in the KCPL territory would be governed by the 1881 agreement. This arrangement would not make sense.

The Commission possesses broad authority to "[override] all contracts, privileges, franchises, charters or city ordinances" in order to preserve and maintain the public welfare. See May Dep't Stores Co. v. Union Elec. Light & Power Co., 107 S.W.2d 41, 48 (Mo. 1937). The Commission's jurisdiction extends to the supervision of franchise agreements. Section 393.170, RSMo, provides that before a certificate of convenience and necessity shall be issued to an electrical corporation by the Commission, the corporation must file municipal franchises with the Commission "showing that it has received the required consent of the proper municipal authorities."

The Joint Applicants' reliance on XO Missouri, Inc. v. City of Maryland Heights, 256 F. Supp. 2d 966 (E.D. Mo. 2002) ("XO Missouri"), and the internal citation therein to State ex rel. City of St. Louis v. Laclede Gaslight Co., 14 S.W. 974 (Mo. 1890) ("Laclede") is misplaced. Neither decision contemplated the Commission's authority to condition approval of merger transactions to avoid detriment to the public interest. Indeed, application of the XO Missouri case as interpreted by the Joint Applicants would virtually bar the Commission from applying *any* merger conditions that directly or indirectly affect existing agreements. The United States Supreme Court has cautioned against an overbroad reading of the "Contracts Clause," stating that it is "well settled that the prohibition against impairing the obligation of contracts is not to be read literally." See Keystone Bituminous Coal Ass'n v. DeBenedictis, 480 U.S. 470, 502 (1987) (Stevens, J.) citing W.B. Worthen Co. v. Thomas, 292 U.S. 426 (1934). Moreover, blanket application of the Laclede decision offered by the Joint Applicants in p. 36 of their prehearing brief has been expressly overridden by the Missouri Supreme Court. See City of Fulton v. Pub. Serv. Comm'n, 204 S.W. 386, 386 (Mo. 1918).

More recently, the Missouri Court of Appeals held that contractual impairment arguments do not apply to franchise agreements subject to Commission authority. See Missouri ex rel. Union Elec. Co. v. Pub. Serv. Comm'n, 770 S.W.2d 283, 286 (Mo. Ct. App. 1989). There, the court held:

> A franchise under these constraints and limitations [*i.e.*, municipal and Commission approval pursuant to Section 393.170 RSMo] cannot be transfigured into a contract subject to impairment as Union Electric argues. Only in Commission dicta explaining its holding in Re Union Electric Company, 3 Mo. PSC (N.S.) 157 (1951) does the notion of contract rights get mistakenly introduced and tied to the franchise concept. A franchise is not truly a contract but merely a license for a term of years. As a license it promotes civic responsibility and exemplary corporate conduct on the part of the utility.

Id. at 286 (parenthetical added). It is noteworthy that the Court's statement that a franchise is a license *for a term of years* is made in the context of evaluating a *perpetual* franchise, suggesting that whether or not KCPL has a perpetual franchise has no bearing on this analysis.

KCPL defends the obvious limitations of its 19th century crafted franchise by suggesting that Kansas City's operational needs are covered by Commission-approved tariffs. Tr. p. 2212. With regard to relocation, KCPL states that "if the City or any other municipality asks KCPL to relocate its facilities that are located in a private easement, the City pays the relocation costs. If the facilities are located on public rights of way, any changes are done at KCPL's expense." Joint Applicants' Prehearing Br. at 48. In so doing, KCPL references two tariffs: (1) Section 15.08, Changes and Removal, Municipal Lighting Service, KCPL General Rules and Regulations, P.S.C. Mo. No. 2 (Tariff Sheets 1.51-52); and (2) Section 10.03(e)(v) Underground Distribution System in Residential Subdivisions. A review of these tariffs demonstrates that KCPL misinterprets the factors of cost allocation and overstates the applicability of current tariffs. [1]

KCPL's Municipal Lighting Service tariff states that KCPL will perform the relocation of municipal lighting facilities at Kansas City's request, and must be reimbursed costs unless the facilities are in a public right of way *and* if the relocation will service a public improvement paid for by public funds. KCPL's Residential Undergrounding tariff requires the party requesting the relocation of underground distributions systems in residential neighborhoods to pay the estimated relocation costs to the company, without any mention of public or private rights-of-way, or of public improvements. Both tariffs suggest that KCPL will not assume relocation costs for facilities solely by virtue of their location on the public rights of way, but will also evaluate whether projects are "public" or "private." Furthermore, KCPL's tariffs apply specifically to traffic control systems and undergrounded facilities in residential neighborhoods - there are numerous other utility facilities not addressed by these tariffs. [2]

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[1] The Commission is authorized to take official notice of the matters which courts of this state may judicially notice. The Commission may take official notice of its own records and may do so on its own motion. At this time, the Commission takes official notice of KCPL's approved tariffs which it has identified.

[2] The Commission identified one additional KCPL tariff specifically addressing relocation: Section 16.08, Changes and Removals of Traffic Control System, KCPL Rules and Regulations. Section 16.08 requires a municipality to notify KCPL in writing to remove, change or discontinue traffic control facilities. KCPL will perform the change as soon as reasonably practical. The municipality must pay costs including labor, transportation and materials, applicable overheads, insurance and taxes. Additional costs depend on whether KCPL facilities will be restored or replaced by municipal-owned facilities. This rule is also limited to traffic control systems and apparently assigns costs to the affected municipality irrespective of facility location in a public easement.

Missouri common law establishes that utilities must remove or relocate facilities sited in public rights of way, and pay for such removal or relocation, when required by public necessity. Missouri case law has restricted this general rule when the removal or relocation is required during a municipality's proprietary, rather than governmental, activity. See, e.g., Bridgeton v. Missouri American Water Co., 219 S.W.3d 226, (Mo. 2007); Union Elec. Co. v. Land Clearance for Redevelopment Auth. of St. Louis, 555 S.W.2d 29, 31-32 (Mo. 1977); Homebuilders Assoc. of Greater St. Louis v. St. Louis County Water Co., 784 S.W.2d 287, 290-91 (Mo. Ct. App. 1989); Kansas City v. Kansas City Power & Light Co., 2006 WL 1210206 (Mo. P.S.C. 2006) ("KCMO v. KCPL").

Uncertainties regarding the responsibility of costs, as well as the utility-generated reimbursement calculations for relocations, have resulted in disputes and litigation. The Commission resolved a dispute between Kansas City and KCPL about relocations and undergrounding in the 2006 KCMO v. KCPL case. See Case No. EC-2006-0332, Report and Order (Apr. 2006). Because existing tariffs and regulations appeared to be insufficient to address the factual circumstances of that case, the Commission suggested it would order Staff to review whether a new tariff governing utility facilities relocation was feasible, and whether rulemaking requiring KCPL to submit its objective formula for calculating line extension and relocation costs was appropriate. Id. at 8, 10. The Commission finds that the current franchise agreements and tariffs are inadequate to prevent disputes and litigation, and there is a risk of public detriment by permitting two "separate" legal entities to significantly integrate operations without recalibrating the parties' working relationship. In short, there is a clear nexus between the City's existing franchise agreements and the public interest.

In light of the combined operations that will result from this merger, the appropriate time for the Commission to consider Kansas City's request for a unified franchise agreement is now. Despite its projections of synergies resulting from the integration and consolidation of KCPL and Aquila operations, KCPL is asking the Commission to ignore the practical effect of the transaction on Kansas City's management of its rights-of-way. KCPL cannot have it both ways. If KCPL and Aquila can take advantage of synergies from more unitary operations, so too should their customers.

The Commission concludes that it possesses the jurisdiction to condition this merger approval on the negotiation of a unified franchise agreement. Accordingly, the Commission hereby orders that, to avoid detriment to the public interest, and to promote the very synergies touted by the applicants, KCPL and Aquila must negotiate a unified franchise with Kansas City within nine months of the closing date of the merger.

<u>Issue VIII – Quality of Service Plan and Earnings Sharing Mechanism</u>

1. Should Commission approval of the Joint Application be conditioned upon requiring KCPL/Aquila to file an application for a Quality of Service Plan within 90 days of the Commission's final decision in this proceeding?

Kansas City proposes a condition that would require the applicants to initiate a docket and file an application with the Commission for a Quality of Service Plan ("QSP") within ninety days of the final decision in this proceeding. Kansas City does not insist on the specific details of a QSP at this time, and proposes the Joint Applicants devise a framework in cooperation with the Commission. The City acknowledges the Commission's recently adopted reliability monitoring and reporting rules will contribute towards setting a foundation for reporting and establishing metrics, but contends that utility-specific metrics with some type of consequences are required in the context of this merger. See Kansas City Post-Hearing Br. p. 7-8.

KCPL argues that a QSP is not necessary because previous Staff reviews of five years of KCPL's performance measures for System Average Interruption Frequency Index ("SAIFI"), System Average Interruption Duration Index ("SAIDI"), Customer Average Interruption Frequency Index ("CAIDI") and Momentary Average Interruption Frequency Index ("MAIFI") found no long term trends of concern. KCPL Post-Hearing Br. p. 33-34. KCPL advises the Commission that it is dedicating sufficient resources to its customer service operations to ensure that quality of service does not deteriorate. Tr. p. 2295.

The Commission finds that there is a heightened risk of service quality degradation when utility operations and functions are integrated. Tr. p. 1877-78. When a utility has an incentive to cut capital expenditures to improve its earnings picture – which occurs frequently in merger situations – it is the Commission's duty to ensure that merger savings do not come at the expense of service quality. KCPL has represented to this Commission that "all stakeholders" bear a "shared risk" of service quality degradation if the merger is approved. See Tr. p. 327-28. This should not, and need not, be the case. The current rates that customers pay reflect a certain level of service. Reparations or bill credits for past periods of poor performance are not penalties, but return money to customers that have already paid for an expected level of performance. See generally Tr. p. 2173. The Commission's reliability rules do not address the specific service quality concerns stemming from this merger application. In order to prevent the merger from being detrimental to the public interest, the Commission concludes that KCPL and Aquila must initiate a docket and file an application with the Commission for a Quality of Service Plan within ninety days of the final decision in this proceeding.

2. Should Commission approval of the Joint Application be conditioned upon establishment of an Earnings Sharing Mechanism that returns to customers excess earnings of KCPL/Aquila above an authorized level.

Kansas City proposes that the Commission condition its merger approval upon KCPL/Aquila filing for an Earnings Sharing Mechanism ("ESM") that returns a portion of excess earnings above the Commission's authorized rate of return to customers. Ex. 401, Hix Rebuttal, p. 6. Kansas City proposes that the applicants would file financial data with the Commission annually, and Commission Staff and other interested parties would have an opportunity to review and validate the figures supplied. Kansas City asserts it is likely that the parties to the proceeding would come to an understanding of appropriate costs and revenues and establish the amounts subject to distribution to customers and the utility, after which the Commission would issue a decision ordering the merged entity to return the proper portion of excess earnings to customers. Kansas City acknowledges that the applicants are making significant investments in Missouri, but asserts there is an expectation that additional investments should yield additional revenues. See Kansas City Post-Hearing Br., p. 9.

The applicants reject this proposal by arguing that ESMs are not appropriate when costs of service are increasing. The applicants predict that current construction projects and rising fuel costs will increase overall costs in an amount to exceed the total estimated synergies of the merger. As a result, the applicants contemplate a rate increase that would nullify the value of an ESM. Furthermore, the applicants argue, and Kansas City concedes, that the Commission does not have the authority to unilaterally impose an alternative regulatory plan. See KCPL Pre-Hearing Br., p. 33, Kansas City Pre-Hearing Br., p. 10.

At the outset, the Commission would note that while it may not unilaterally impose an alternative regulation plan, the Commission does have the necessary authority to approve a reasonably structured alternative regulation. See Staff of the Missouri Public Service

Commission v. Southwestern Bell Tel. Co., Case Nos. TC-93-224 / TO-93-192, 1994 WL 323583 (Mo. P.S.C. 1994). In this application, KCPL has made a number of assertions regarding its cost picture that may or may not be true. See Ex. 15, Giles Surrebuttal, pp. 13-14. Presumably, one of the motivations for GPE in proposing this merger is the opportunity to realize more profit; however, the applicants continue to ignore the possibility of increased revenues as a result of an improved cost structure. See Ex. 15, Giles Surrebuttal, p. 13. As a general proposition, the amounts of synergies and costs associated with the merger have been debated and altered since the application was filed. The Commission finds that if excess revenues do not occur in the future, this does not imply that an ESM would be a waste of Commission resources. While excess earnings may occur and would be distributed in other years, the opportunity for Staff and other parties to validate the utility's costs and revenues following the annual filing provides an additional regulatory benefit that is more efficient than the Joint Applicants' proposal to share synergies with customers through regulatory lag. See KCPL Post-Hearing Br., p. 32.

To encourage efficiency after the merger, the most effective ESM would include a "reverse taper" in determining rewards for customers and the utility. This methodology utilizes the authorized return on equity (ROE) as the threshold above which excess earnings are either retained by the utility or returned to customers. In light of the fact that the easiest earnings to achieve are the next several dollars above the authorized level, the reverse taper returns to customers a greater share of those dollars. After greater excess earnings are achieved, more is retained by the utility. See Ex. 401, Hix Rebuttal, p. 7. To prevent detriment to the public interest, the Commission hereby conditions merger approval upon KCPL/Aquila filing for an ESM that returns a portion of excess earnings above the Commission's authorized rate of return to customers. This proposal should include a reverse taper calculation not unlike that proposed by Kansas City in this proceeding.

Issue IX – Future Rate Case

1. Should Commission approval of the Joint Application be conditioned upon requiring KCPL/Aquila to file a comprehensive rate case with respect to the merged operations within three (3) years of the Commission's approval of the merger?

Kansas City requests that the Commission order the Joint Applicants to track costs and organizational changes and file a comprehensive rate case for the approved merger within a reasonable period of time. Kansas City supports the Office of Public Counsel's recommendation that if the application is approved, both KCPL and Aquila should be required to file a consolidated rate case proceeding consistent with the timing required in the Regulatory Plan for KCPL, Case No. EO-2005-0329, with respect to Rate Filing #4. See Updated OPC Prehearing Br., p. 7.

KCPL replies that because KCPL and Aquila will not legally merge but retain separate Commission-approved tariffs and separate generation, transmission, and distribution systems, any Commission order requiring a comprehensive rate case is premature. KCPL adds that the timing of its rate cases is influenced by its commitments and activities under the Regulatory Plan Stipulation Case No. EO-2007-0329. See KCPL Posthearing Br., p. 34.

The Commission finds that rate integration is important to prevent detriment to the public interest and is an important step toward a total company effort to improve electric system operations and enhanced utilization of generation and transmission resources. GPE has stated that it will file cases for the separate operations of its KCPL and Aquila affiliates following the merger, but the savings associated with rate integration should be deferred to another day. The Commission disagrees, and hereby orders the company to file a proposal to integrate financial operations and electric system operations into a cost structure that can be comprehensively evaluated for efficiencies and improved operations. Following a brief period to track and evaluate data, the company is obligated to file a comprehensive rate case for its merged operations consistent with the timing required in the Regulatory Plan for KCPL, Case No. EO-2005-0329, with respect to Rate Filing #4. The analysis of the new cost structure should lead to more equitable assignment or allocations of costs to the appropriate service territories and customer classes of the new entity.

ORDERED SECTIONS

IT IS THEREFORE ORDERED:

1. That Great Plains Energy and Aquila are authorized to perform in accordance with the terms and provision of the Agreement and Plan of Merger, APA, PIPA, and all other transaction related instruments, and to take all other actions that may be reasonably necessary and incidental to the performance of the Merger, **SUBJECT HOWEVER**, to the following conditions:

A. KCPL and Aquila shall negotiate with the City of Kansas City on a unified franchise with Kansas City and shall have the franchise finalized within nine (9) months of the closing date of the merger.

B. Within ninety (90) days of the effective date of this Order, KCPL and Aquila must initiate a docket and file an application with the Commission for a Quality of Service Plan ; additionally KCPL/Aquila will file for Commission approval an Earnings Sharing Mechanism that returns a portion of excess earnings above the Commission's authorized rate of return to customers. This proposal should include a reverse taper calculation similar to that proposed by Kansas City in this proceeding.

C. KCPL and Aquila shall, consistent with the timing required in the Regulatory Plan for KCPL, Case No. EO-2005-0329, with respect to Rate Filing #4, but no later than within three (3) years of the effective date of this Order, file a proposal to integrate their financial operations and electric system operations into a cost structure that can be comprehensively evaluated for efficiencies and improved operations.

2. [the balance of other orders and relief] .

Respectfully submitted,

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CERTIFICATE OF SERVICE

A true and correct copy of the foregoing was served via email upon the parties identified on the attached service list on this 6th day of June, 2008.

/s/ Mark W. Comley

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