

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

In the Matter of the Application of Aquila,)
Inc., for Authority to Acquire, Sell and Lease)
Back Three Natural Gas-Fired Combustion)
Turbine Power Generation Units and) Case No. EO-2005-0156
Related Improvements to be Installed and)
Operated in the City of Peculiar, Missouri)

REPLY TO RESPONSES OF PUBLIC COUNSEL AND STAFF

COMES NOW Applicant Aquila, Inc. ("Aquila") and for its reply to the responses of Public Counsel and Staff to Missouri Public Service Commission's ("Commission") September 29, 2005 Order Directing Filing, states the following:

1. While considering the responses filed by Staff and Public Counsel on October 14, 2005 (collectively, the "Responses" or individually, the "Response" as applicable), the Commission should bear in mind the current procedural posture of this case. Before the Commission for consideration and approval is a Stipulation and Agreement signed by representatives of Aquila, Staff and Public Counsel, filed on September 1, 2005 (the "Agreement"). That Agreement proposes a comprehensive resolution of the two principal issues which are pending before the Commission for decision. The issue of valuation of the combustion turbines and auxiliary equipment (the "CTs") remains unaffected by the matters alleged in Public Counsel's Motion to Stay and subsequent Responses. The agreement of the parties that the tax-advantaged Chapter 100 financing is not detrimental to the public interest also appears to remain

unchanged. In fact, a principal objective of this type of financing is to benefit customers through a lower cost of service than otherwise would be the case.

Valuation of the CTs

2. Of critical significance is the fact that neither Staff or Public Counsel contend that § II of the Agreement, which address the issue of the valuation of the CTs, should not be approved. To the contrary, Staff's Response states that the questions surrounding the closing of the Chapter 100 financing in December 2004 "has no effect on Staff's agreement to the appropriate value for the three combustion turbines for regulatory purposes addressed in the" Agreement. Public Counsel's Response is silent on this topic and can only reasonably be construed as continued support for the agreed-to valuation of the CTs. Consequently, the Commission should proceed and decide the valuation issue based on the Agreement.

No Party has Requested Termination of any Aspect of the Agreement

3. As to that part of the Agreement addressing the requested approval of the Chapter 100 RSMo tax-advantaged financing package (§ III), the Responses appear to be at odds. Staff suggests the Commission issue an order approving the Agreement. Public Counsel, on the other hand, requests that the Commission issue an order "declaring each and every transaction or action

entered into or performed by Aquila...to be void as a matter of law.”¹ Public Counsel also requests that the Commission direct its General Counsel to seek civil and criminal penalties against Aquila for alleged misleading statements.

4. Public Counsel’s request, that the Chapter 100 financing transactions be declared void as a matter of law, is not consistent with the terms of the Agreement. The relevant language of the Agreement provides as follows:

The Signatory Parties enter into this Agreement in reliance upon information provided to them by Aquila. In the event that the Commission finds that Aquila failed to provide the Signatory Parties with material and relevant information in its possession, or which should have been available to Aquila through reasonable investigation, or in the event that the Commission finds that Aquila misrepresented facts relevant to this Agreement, this Agreement shall be terminated.

In this regard, Public Counsel has not made a showing that justifies the conclusion that Aquila failed to provide Public Counsel with material and relevant information in its possession, that Aquila misrepresented facts relevant to the Agreement or that Public Counsel was not otherwise fully informed of the facts concerning the Chapter 100 RSMo financing. As explained below, the opposite is true. Consequently, there is no basis for invalidating or terminating the Agreement as it relates to the Chapter 100 financing.

¹ Staff’s Response contains a statement of its belief the transactions are void but provides no reasoning that explains the factual, legal or public policy basis for this conclusion. See, ¶ 8. Nevertheless, Staff has recommended approval of the terms of the Agreement.

**Public Counsel has not Presented Circumstances which Justify
Termination of the Agreement**

5. It is significant that Public Counsel has not requested that the Agreement be terminated. Consequently, the Response it has filed does not present a recommendation that is relevant to the Agreement that is before the Commission for approval.

6. Public Counsel's claim that it was not informed the Chapter 100 RSMo financing was closed in December of 2004 is contradicted by the fact that it was supplied on March 23, 2005, with a copy of Aquila's response to Staff's Data Request No. MPSC0033. Attachment A hereto demonstrates that a copy of that data request response was sent to Public Counsel's witness Ted Robertson by Mark Reed of Aquila. The very first part of Aquila's response contains the following explicit statement:

Current legal title to this equipment is held by the City of Peculiar in accordance with the Chapter 100 arrangement. Title was transferred December 30, 2004.

7. In addition, then-Public Counsel, John Coffman, was present at the public hearing in Harrisonville, Missouri on March 15, 2005, chaired by Commissioners Davis, Appling and Gaw in the proceedings in Case No. EA-2005-0248 concerning the South Harper peaking power station, at which time the mayor of the City of Peculiar, George Lewis, testified to the fact that the Chapter 100 financing closed in late December of 2004.

8. Also, Public Counsel acknowledges in ¶8 of its Response that it received from Aquila execution copies of the Economic Development Agreement

(the “EDA”), the Deed of Trust and Security Agreement, the Bill of Sale, the Special Warranty Deed, the Lease, the Bond Purchase Agreement and the Bond in response to OPC Data Request Nos. 2, 3 and 4. Each of the documents supplied were dated as of December 30, 2004. Public Counsel’s contention that the “execution copies” supplied did not bear signatures, overlooks the significance of the documentation with which it was provided. Execution copies, in this context, refer to agreements and related documentation that have been generated and circulated for the specific purpose of obtaining party signatures.

9. These facts refute any implication that Aquila failed to provide Public Counsel with material and relevant information concerning the status of the financing. More to the point, there is no validity to Public Counsel’s unjustified claim that Aquila has “perpetrated . . . a deception” on the Commission.² To the contrary, the fact of the closing had been a matter of public record for many months prior to the Commission’s hearing on September 21, 2005.

**The Financing Agreements are Subject to
Obtaining Required Approvals**

10. Ultimately, Public Counsel’s allegations are a case study in being distracted by the trees and missing the forest. As Aquila has previously pointed out, the Chapter 100 financing arrangements are expressly subject to a regulatory contingency set forth in Section 4.01 of the EDA. That section provides in pertinent part:

² Response, ¶20.

The Bonds issued by the City may be redeemed by Aquila (acting in its sole discretion) if Aquila does not receive any approval required to (a) consummate the Project, [or] (b) perform its obligations under this Agreement, the Lease or the Bond Documents...

The practical effect of this language is that the Chapter 100 financing arrangement which is the subject of § III of the Agreement is no different than any other transaction or arrangement evidenced by a signed agreement which is subject to a regulatory approval contingency. Unsupported statements by Staff³ and Public Counsel⁴ that the Commission cannot “ratify” the financing miss the point by exalting form over substance. Whether regulatory approval is a condition precedent or subsequent, the requirement of regulatory approval expressly is accommodated in the EDA. Moreover, under the indenture, Aquila has the right to redeem the bonds at any time for any reason, which would include the Commission’s lawful exercise of jurisdiction over the Chapter 100 financing and denial thereof were it to find that the financing is detrimental to the public interest. To the extent the Commission has statutory authority over the sale and leaseback arrangement⁵, that authority has not been impaired.

The Tax-Advantaged Financing is in the Public Interest

11. Public Counsel’s pleading also misses the practical bottom line that the tax-advantaged Chapter 100 financing is in the public interest. It will reduce Aquila’s cost of service because the tax savings which are anticipated to be approximately \$18 million over the life of the Bond(s) are expected to be a flow-

³ Response, ¶8.

⁴ Response, ¶19.

⁵ See, paragraphs 12 and 13, *supra*.

through item in rates. The cost benefits of the tax-advantaged financing put in place by Aquila will be immediate in that the savings are being reflected in test year tax expense in Aquila's pending electric general rate increase case, Case No. ER-2005-0436. The property tax expense associated with the South Harper power station is based on this year's PILOT thus flowing through any Chapter 100 savings to the customer. This would not have been the case but for the actions taken by Aquila at year-end 2004. Additionally, the PILOT payments will benefit the local community. The Agreement expressly states that the actions contemplated by the financing "are not detrimental to the public interest" subject to the agreed-to conditions set forth therein. This is the applicable standard for approval.⁶ Nothing in Public Counsel's Response refutes this element of the Agreement. In essence, Public Counsel's Response purports to induce the Commission to declare void a transaction the principal purpose of which has been to keep the cost of electric service to the general public as low as possible. This simply makes no common sense.

No Factual, Legal or Public Policy Rationale has been Offered that Justifies a Summary Order Declaring the Chapter 100 Financing Void as a Matter of Law

12. As to Public Counsel's request that the Commission declare void the steps taken by Aquila to close the financing transaction that took place in December of 2004, Public Counsel in effect is requesting a partial summary disposition without having complied with the requirements of Commission rule 4

⁶ Staff's Response ratifies the conclusion of its suggestion in support of the Agreement "that it would not be detrimental to the public interest for Aquila to enter into the Chapter 100 financing arrangement with the City of Peculiar." (See, Response, ¶ 9)

CSR 240-2.117. The Response is therefore procedurally flawed and should be denied. Secondly, Public Counsel's request is premised on the assumption that the Commission has statutory authority to approve the sale and lease-back arrangement, an assumption that is tenuous at best as explained below. Finally, Public Counsel has provided no compelling legal or factual rationale for the Commission to issue such a summary ruling. As noted above, the financing arrangement is very much subject to the Commission's regulatory approval in the event that it is required so there is no principled basis for taking any action to void a transaction which by its express terms can be unwound if the Commission disapproves the relevant terms of the Agreement.

Public Counsel and Staff have not made a Showing that the Commission has Statutory Authority over the Sale and Lease-Back Arrangement by and between Aquila and the City of Peculiar

13. Any order by the Commission that the transactions entered into to facilitate the tax-advantaged financing are void necessarily must be grounded on express finding that the Commission has statutory authority over the transaction in the first instance. This is an extremely dubious conclusion in light of the Commission's January 23, 1981 Order in Case No. EO-81-216 that addressed nearly identical facts as those presented in this case. There, the Commission concluded that a sale and repurchase agreement entered into to facilitate tax-exempt financing did not constitute a "sale" or "transfer" within the meaning of

those terms as used in § 393.190.1 RSMo.⁷ The Commission pointed out the obvious fact that the transactions were entered into merely to finance additions and improvements to the electric utility system of Arkansas Power & Light Company (“AP&L”) and not to dispose of necessary or useful parts of its franchise works or system. It is not reasonable to suggest that the technical transfer of legal title to the CTs, the real estate and service structures in this case was calculated to impair, or has impaired, service to Aquila’s electric customers. To the contrary, the Agreement includes a clause setting forth how Aquila will depreciate the CTs which would not be pertinent but for the fact that the South Harper power station will be treated as being owned by Aquila.⁸ Additionally, the Commission has already noted the South Harper “facility will replace part of Aquila’s current capacity represented by a Power Purchase Agreement” that expired on May 31, 2005.⁹ It is anticipated by all parties that the South Harper power station is being treated as a regulated asset dedicated to regulated public service regardless of the fact that the City of Peculiar holds technical legal title. This cannot be reconciled with Public Counsel’s contention that Aquila has improperly disposed of property that is necessary and useful in the performance of its regulated electrical obligations.

14. In the 1981 AP&L case, the Commission also observed that even if transfer of legal title merely to facilitate a tax-exempt financing were to be viewed

⁷ “The obvious purpose of this provision is to ensure the continuation of adequate service to the public served by the utility.” *State ex rel. Fee Fee Trunk Sewer, Inc. v. Litz*, 596 S.W.2d 466, 468 (Mo. App. 1980).

⁸ See, II.B.

⁹ *Order Clarifying Prior Certificates of Convenience and Necessity*, dated April 7, 2005, Case No. EA-2005-0248, slip op. at p. 2.

as a true sale, the transaction had been entered into before the facilities had been put in service so the transaction did not involve a sale or transfer of any part of the franchise works or system which were necessary and useful in the performance of AP&L's duties to the public. In this case, the Public Counsel complains of a transaction that occurred in December of 2004, several months before the South Harper power station began generating electricity for the grid in the early Summer of 2005.

Summary of Reply to Responses

15. No party has requested additional hearings in this case. No party has requested that the Agreement be terminated or provided any justification for terminating the Agreement. It should, therefore, be approved without the necessity of further proceedings. Public Counsel's allegations that it has been deceived by Aquila about the timing of the closing of the Chapter 100 RSMo are not supported by the facts. To the contrary, as early as March of this year Public Counsel had actual notice the financing was closed in December of 2004. Public Counsel and Staff have offered no legal or factual analysis that would distinguish the present situation from identical circumstances examined by the Commission in 1981 in the AP&L case. As such, no procedural, legal or factual justification would justify a declaration that any of the elements of the Chapter 100 financing transaction are void as has been requested by Public Counsel. As to Public Counsel's request that the Commission direct its General Counsel to seek civil and criminal penalties against Aquila and/or its employees, there is no legal or

factual justification for doing so for the reasons set forth above. In any event, the request is beyond the scope of this proceeding.

WHEREFORE, the Commission should deny the relief requested in Public Counsel's Response and approve the terms of the Agreement without further proceedings or delay.

Respectfully submitted,

/s/ Paul A. Boudreau

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CERTIFICATE OF SERVICE

I hereby certify that a true and correct copy of the above and foregoing document was delivered by electronic mail, first class mail or by hand delivery, on this 24th day of October, 2005 to the following:

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