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October 3, 2000

Dale Hardy Roberts
Missouri Public Service Commission
P.O. Box 360
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FILED[2]
OCT 3 2000
Missouri Public Service Commission

Re: Case No. EM-2000-292

Dear Mr. Roberts:

Enclosed for filing on behalf of UtiliCorp United Inc., please find an original and eight (8) copies of UtiliCorp's Reply Brief.

Copies of this filing will be provided to all parties of record.

Would you please see that this filing is brought to the attention of the appropriate Commission personnel.

I thank you in advance for your cooperation in this matter.

Sincerely yours,

James C. Swearengen

James C. Swearengen

JCS/lar
Enclosure
cc: All Parties of Record

FILED[2]
OCT 3 2000
Missouri Public Service Commission

BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

In the Matter of the Joint Application of UtiliCorp United Inc. and St. Joseph Light & Power Company for authority to merge St. Joseph Light & Power Company with and into UtiliCorp United Inc. and, in connection therewith, certain other related transactions	)))))))	Case No. EM-2000-292

REPLY BRIEF OF UTILICORP UNITED INC.

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I. INTRODUCTION AND OVERVIEW

This Reply Brief is submitted in response to the Initial Briefs of the Staff of the Missouri Public Service Commission ("Staff"), the Office of the Public Counsel ("Public Counsel"), the City of Springfield ("Springfield"), the Missouri Department of Natural Resources ("DNR"), and AG Processing Inc. ("AGP").

In deciding this case, the Commission is faced with two fundamental and overriding issues. The first is whether the proposed merger between UtiliCorp and SJLP should be approved under the "not detrimental to the public interest" legal standard. The second is what conditions, if any, should be placed on the transaction.

UtiliCorp respectfully submits that the merger meets the legal standard and must be approved on that basis. UtiliCorp also submits that the conditions which should attach to the approval are those set out in its Proposed Regulatory Plan - - conditions which are designed to make the transaction economically feasible to UtiliCorp's shareholders who bear the risk of the transaction.

Once again, it is important to remember that UtiliCorp's shareholders will invest approximately $270 million to acquire the ownership of SJLP. This equates to a $23 per share purchase price which is approximately 36% above SJLP's stock trading value just before the merger was announced (Ex. 2, p. 6). This 36% amount equals an estimated $92 million and is referred to as the "acquisition premium." (Ex. 4, p. 4). <u>The transaction would not take place absent this premium which is a precondition to the merger and the unlocking of the potential merger savings</u>. (Ex. 2, p. 11). It is the payment of this premium by UtiliCorp's shareholders, however, which creates the risk which necessitates a plan which will allow these shareholders a reasonable opportunity to recover their investment. UtiliCorp entered into this transaction with the expectation that, based upon prior actions of this Commission, it would have a <u>reasonable opportunity</u> for premium recovery - - and that is what the Regulatory Plan is designed to accomplish. (Ex. 2, p. 11).

II. ARGUMENT

The Staff's Initial Brief presents several arguments as to why the Commission should reject the merger as "detrimental to the public interest." (See Initial Brief of Staff at 38-40.) By responding to these arguments raised by the Staff, UtiliCorp will address essentially the substance of all the issues raised in the initial briefs of the other parties. In this regard, it should be noted that while the Staff's Initial Brief is some 200 pages in length, nowhere in that document does the Staff attempt to apply the applicable legal standard to the involved facts. Given the Staff's opposition to this transaction, the reason for this failure is readily apparent. An application of the legal standard to the facts shows that the merger must be approved.

The Applicable Legal Standard

Because of the failure of the Staff to apply the legal standard to the facts, it is worthwhile to revisit that standard. In determining whether to authorize a merger under § 393.190 RSMo, the Commission is required by law to determine whether the transaction is "detrimental to the public," the standard established by the Missouri Supreme Court in *State ex rel. City of St. Louis v. Public Service Commission*, 73 S.W.2d 393 (Mo. 1934). In that case, the Missouri Supreme Court stated:

> To prevent injury to the public, in the clashing of private interest with public good in the operation of public utilities, is one of the most important functions of Public Service Commissions. <u>It is not their province to insist that the public shall be</u>

> *benefited*, as a condition to change of ownership, but their duty is to see that no such change shall be made as would work to the public *detriment*. "In the public interest," in such cases, can reasonably mean no more than "not detrimental to the public." (Italics supplied.)

Id. at 400.

In its decision emphasizing that a regulatory commission must not affirmatively find that a change in ownership of a utility is in the public interest, the Missouri Supreme Court said:

> "[t]he owners of this stock should have something to say as to whether they can sell it or not. To deny them that right would be to deny to them an incident important to ownership of property . . . A property owner should be allowed to sell his property unless it would be detrimental to the public." (Emphasis added: Citations omitted.)

Id.

The judicially established "not detrimental to the public" standard is the test which this Commission has always applied in merger and acquisition cases.[1] While the standard is not an issue in this proceeding, the failure of the Staff to recognize and properly apply it is a fatal flaw to their arguments.

Not only is the legal standard not at issue, there is also no issue in this case as to what is meant by the term "detrimental to the public." "Detriment" means "higher rates and/or a deterioration in the level of customer service." *See Laclede Gas Company* Case No. 17, 267, 92 P.U.R. 3rd 426. The Staff agrees as indicated by the testimony of its witness Steve M. Traxler (Ex. 718, p. 7 Tr. 388). Moreover, "the public" involved in considering whether there is detriment is the "consuming public" or "ratepayers." *See In the matter of the application of*

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[1]See Appendix A of Initial Brief of UtiliCorp

Continental Water Company 19 Mo. P.S.C. (N.S.) 192; Re GTE Corporation 121 P.U.R. 4th 54; Re Kansas Power & Light Company, 126 P.U.R. 4th 385, 1 Mo. P.S.C. 3d 150; *City of St. Louis*, 73 S.W.2d 400. The Staff concedes that this is the proper definition of "the public" as indicated by the testimony of its witness Cary G. Featherstone (Ex. 704 pp. 17-18).

Consistently throughout its 200 page brief, the Staff complains of aspects of the proposed Regulatory Plan, the plan under which UtiliCorp will operate the acquired properties, that are too beneficial for UtiliCorp; are not beneficial enough for the former SJLP customers; are not beneficial enough for UtiliCorp's existing Missouri Public Service ("MPS") customers; or transfer too little benefit to the Missouri customers as a whole. These arguments underscore the Staff's failure to come to grips with the appropriate legal standard and therefore must fall on deaf ears before the Commission. As the Missouri Supreme Court has held, it is not the Commission's duty to ensure that the public benefits from a merger. *City of St. Louis*, 73 S.W.2d at 400. The Commission's only duty is to make certain the merger does not prove detrimental to the public. Moreover, and perhaps more incredible is that fact that these arguments raised in the Staff's Initial Brief run counter to the testimony of its own witness, Steve M. Traxler, who admitted at page 7 of his direct testimony that UtiliCorp and SJLP <u>did not have to demonstrate net benefits or improved customer service</u>. (Ex. 718, p. 7). In other words, the Staff concedes the principle that the status quo for the consuming public satisfies the legal standard for merger approval. Unfortunately in its brief the Staff ignores the applicable legal standard and its own evidence and by doing so, wastes the Commission's time by submitting 200 pages of essentially irrelevant argument.

The Two Key Questions

As indicated at the outset of this brief, there are really only two overriding issues in this case. The first is whether the merger should be approved and the second is under what conditions.

A. The Merger Should Be Approved

The Staff and Public Counsel argue that the costs of the merger will outweigh its benefits, and therefore, the merger is "detrimental to the public interest" and should not be approved. (Initial Brief of Staff at 1, 55; Initial Brief of Public Counsel at 26.) The arguments are premised on the notion that the estimated merger savings exceed the estimated merger costs and that when "appropriate" adjustments are made to UtiliCorp's estimates of merger savings and costs to "incorporate more reasonable assumptions," the savings will not exceed the costs. As a consequence these parties urge that the transaction be denied.

In response, it must be emphasized that first, it is the position of UtiliCorp that merger savings will exceed merger costs and accordingly the arguments of the Staff, Public Counsel and others on this point must fail. Second, the question is not relevant to approval of the merger because, under the proposed Regulatory Plan, UtiliCorp will bear the responsibility and risk of generating merger synergies, quantifying them properly and providing that information to the Commission in future rate proceedings. If UtiliCorp cannot create savings and prove to the Commission that these savings have resulted from the merger, then UtiliCorp will not be permitted to achieve any premium recovery through rates. Regardless, however, under the Regulatory Plan, customers of the SJLP operating unit are guaranteed a $1.6 million in reduction of cost of service.

A brief review of the evidence demonstrates that UtiliCorp's position on this point is correct. First, under the Regulatory Plan, a five year rate moratorium will be put in place upon the closing of the merger.[2] (Ex. 4, pp. 7-8). As a consequence, there will be no rate impact on customers during this five year rate freeze regardless of whether costs exceed benefits during this time. In other words, the public cannot possibly suffer a detriment from a rate standpoint for the initial five year period after the merger as the status quo will be preserved.[3] Thereafter, if none of UtiliCorp's projected merger synergies result, no premium costs will be included in rates at the end of the moratorium. However, customers of the SJLP unit will still receive a benefit because the Regulatory Plan guarantees an annual $1.6 million cost of service reduction in years 6-10 after the merger is closed.

As a part of its argument on this point, the Public Counsel claims that because UtiliCorp has more long term debt than SJLP, its risk is greater, and therefore, the customers of the SJLP unit will be subject to higher rates in the future. (Initial Brief of Public Counsel at 18). This argument fails on two points. First, it assumes that the Commission, in some future rate case, will act unlawfully or unreasonably and pass on inappropriate costs to customers. Second, the argument ignores the fact that it is anticipated that these customers will be the beneficiaries of lower rates based on economies of scale and other merger savings which have been articulated by UtiliCorp throughout this proceeding and will be demonstrated in any future rate cases. Simply

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[2]The proposed moratorium is described at page 13 of UtiliCorp's Initial Brief. It prevents UtiliCorp and the Staff from taking action, but does not prohibit other proper parties from bringing a complaint against UtiliCorp's rates. (Tr. 426, 427, 435, 459)

[3]Contrary to the claim of AGP, the status quo is not a detriment. (See Re Laclede Gas Company 92 P.U.R. 3rd 426).

stated, the Public Counsel cannot now show with any degree of certainty that this difference in long term debt will have any impact on future rates; and therefore cannot show any detriment to the public.

Finally, this overall argument, that the costs of the transaction will exceed the benefits, and thus, the merger will necessarily result in higher rates for customers of the SJLP unit, was in essence abandoned by the Staff when its witness testified that if the merger were approved, any after-the-fact effort to show in a subsequent rate case five years in the future that SJLP rates would have been lower if the merger had not occurred would involve "an exercise in speculation." (Tr. 594).

Given that the argument of the Staff and Public Counsel on this point is grounded in guesswork and speculation, the Commission must find that the proposed merger meets the "no detriment" test and approve it. Furthermore, it is clear that reasonably anticipated benefits to customers will exceed costs; that under the proposed Regulatory Plan the customers will benefit through a cost of service reduction regardless; and that customers are ultimately protected, in any event, by the fact that rates for the SJLP unit cannot increase without the Commission's authorization.

B. **The Conditions of the Merger -- The Proposed Regulatory Plan**

The Staff, Public Counsel and AGP assert that the proposed Regulatory Plan has deficiencies that make the merger detrimental to the public. However, the laundry list of reasons the Staff presents to the Commission in its Initial Brief, which essentially cover all of the points raised by the parties, has been refuted by the evidence presented in this case and the arguments set out in UtiliCorp's Initial Brief. In addition, many of the assertions by the Staff and other parties regarding the Regulatory Plan are irrelevant to this merger proceeding.

These arguments, as summarized by the Staff at pages 38-40 of its Initial Brief, are as follows:

- the requested rate treatment for the acquisition premium unfairly assigns costs to customers instead of to UtiliCorp's shareholders;
- the Regulatory Plan will result in UtiliCorp receiving more than 50% of the acquisition premium;
- the Regulatory Plan will require customers to pay for merger transition costs;
- the frozen stand-alone SJLP capital structure will deny customers any benefit of savings from the merger;
- the Regulatory Plan bases its merger benefit on tracking merger savings;
- the plan will result in an insignificant portion of the merger savings to flowing Missouri customers;
- the Regulatory Plan will increase administrative and general costs that would be borne by SJLP customers and is not related to service;
- the Regulatory Plan will result in a disproportionate amount of savings being assigned to SJLP customers at the expense of MPS customers; and
- 89% of the joint dispatch savings can be achieved by SJLP on a "stand-alone" basis. (Initial Brief of Staff at 38-40.)

UtiliCorp's reply to these arguments and others follows:

1. **The Acquisition Adjustment**

The impetus for the challenge of the Staff and Public Counsel to the proposed merger is the treatment requested for the acquisition premium as set out in the Regulatory Plan. This requested treatment has given rise to an emotional response apparently because this Commission has never previously authorized the direct rate recovery of premium although it has allowed indirect recovery of such costs. The Staff, Public Counsel, AGP and others, however, fail to present any compelling argument, based on sound regulatory principles, as to why this Commission should not grant the request to give UtiliCorp a reasonable opportunity to make the economics of the proposed transaction work.

Once again, the Commission should remember that it is UtiliCorp's shareholders who have agreed to pay the premium which will make this merger and its related synergies possible and that these shareholders bear all of the risk of the transaction. UtiliCorp's shareholders simply want a reasonable opportunity to have favorable ratemaking treatment of fifty percent (50%) of the unamortized premium, ("the Assigned Premium") if the synergies from the merger are developed and proven.

In this regard, as indicated, under its Regulatory Plan UtiliCorp is requesting first that the Commission approve the amortization of the acquisition adjustment above the line beginning at the closing of the merger. Then, after five years of this amortization, in the sixth year after the merger is closed, in the context of the Post-Moratorium rate case, the Assigned Premium will be included in the rate base of the SJLP operating unit and the amortization of the premium will be included in the cost of service, provided that UtiliCorp meets its burden of proof in that rate case by showing that the merger savings created by this transaction meet or exceed the cost of the

Assigned Premium. (Ex. 4, p. 7.). If UtiliCorp cannot prove to the Commission that the incremental value created from the merger is at least equal to the Assigned Premium, UtiliCorp shareholders will bear the difference. If, however, in the Post-Moratorium rate case UtiliCorp is able to demonstrate that synergies resulting from the merger meet or exceed the Assigned Premium, the requested ratemaking treatment for the Assigned Premium should be granted. Customers of the SJLP unit will receive a $1.6 million cost of service reduction in any event. Clearly, under its proposal, UtiliCorp's shareholders have the entire financial risk for this transaction.

This is the central feature of the Regulatory Plan. UtiliCorp is asking the Commission, in this case, to reaffirm its policy on premium recovery AND to state that if UtiliCorp meets its burden of proof of demonstrating merger savings in the future rate case, the requested rate treatment of the Assigned Premium and related amortization will be authorized. (Ex. 5, p. 11).

Historically, this Commission has included in rates those expenditures which bring about cost efficiencies in cost of service. Such ratemaking treatment is appropriate and reasonable because savings from the efficiencies are flowed through to customers. Likewise, the requested ratemaking treatment for the Assigned Premium should be viewed in the same manner as other utility cost saving initiatives. (Ex. 4, p. 16).

In considering this issue, the Commission should not automatically assume that the proposed treatment of the Assigned Premium will result in increased rates. Such an assumption is particularly inappropriate in this case because it fails to take into account the cost savings which will result from the merger. In other words, the cost savings resulting from merger synergies should be considered and measured against the cost of the Assigned Premium. If UtiliCorp can meet its burden of proof and demonstrate that the incremental value created and realized by the merger exceeds the Assigned Premium, the rates of the SJLP unit will actually be lower than they would have been otherwise. (Ex. 4, pp. 16-17).

The Staff argues that including the Assigned Premium in utility rates is improper because it will provide incentives for negotiating utilities to settle on a higher purchase price for a transaction. This argument, however, ignores the fact that under the Regulatory Plan in this case, the ratemaking treatment of the Assigned Premium is to be judged for its reasonableness based on the value of aggregate merger benefits. Under these circumstances, UtiliCorp, or any other purchasing utility, clearly has an incentive to minimize the amount of any premium paid because it cannot reasonably expect to receive full cost of service recognition for the premium if synergies do not support the full cost. (Ex. 4, p. 17).

The Staff's argument on this point is also without merit because when a utility realizes that any premium will be evaluated by this Commission for reasonableness based on the synergies produced, the utility accepts the risk of not recovering the premium in rates. (Ex. 4, p. 17-18). Based on its prior pronouncements, this Commission has indicated that it will, in fact, evaluate the ratemaking treatment of a merger premium or acquisition adjustment on a case by case basis. In this proceeding, UtiliCorp is simply asking for a continuation of the present policy, but with assurances on the front end in this case that if the appropriate evidentiary standards are met, the requested rate treatment of the Assigned Premium will be authorized in the Post-Moratorium rate case five years in the future.

By evaluating the reasonableness of UtiliCorp's request, this Commission will be fulfilling its responsibility to set just and reasonable rates. The review process for the rate recovery of the Assigned Premium should be viewed no differently than the process which this Commission undertakes in a rate case for the consideration of the reasonableness of investments and expenses generally. Obviously, it is common practice for this Commission to pass cost savings on to customers through the ratemaking process. And in so doing, the Commission usually allows rate treatment for the investments and expenses used to develop savings. In this regard, this Commission should consider the premium in this transaction as simply an "investment" to develop merger savings. When seen in this light, the premium, in this case the Assigned Premium will deserve rate recognition if synergies meet or exceed the cost of the Assigned Premium and net synergies are passed on to customers. (Ex. 4, p. 18).

Determining the reasonableness of a premium does not mean that the Commission needs to be a part of merger negotiations. Rather, the Commission should simply exercise its duty to determine the reasonableness of the premium just as it determines the reasonableness of other investments and expenses incurred by utilities. (Ex. 4, p. 19).

In this case, the evidence demonstrates that the $23 per share price which UtiliCorp will pay for the SJLP stock is fair and reasonable. It resulted from an arm's length negotiation, competitive bidding process, and is comparable to industry norms. (Ex. 3, pp. 11-12). In connection with this, as indicated previously, UtiliCorp must know now whether the entire $92 million premium will be considered as the basis for determining rate recovery of the Assigned Premium in the Post-Moratorium rate case.

Once again, it must be emphasized that this Commission has previously stated its policy that it is not opposed to the consideration of acquisition adjustment for ratemaking purposes. *See Re Missouri American Water Co.*, Case No. WR-95-205, 4 Mo. P.S.C. 3d 205. This Commission has said that it is not opposed to the concept of a savings sharing plan (as part of an acquisition adjustment request) provided that only merger-related savings are shared. *Id. See also Re Kansas Power & Light Company*, Case No. EM-91-213, 126 P.U.R. 4th 385, 1 Mo. P.S.C. 3d 150 (September 24, 1991). This Commission has also said that it does not wish to prevent companies from producing economies of scale and savings which can benefit ratepayers and shareholders alike. *Id.*

The Commission's policy finds support in Missouri case law. In *State ex rel Martigney Creek Sewer Company v. PSC* 537 S.W.2d 388 (Mo. 1976), the Missouri Supreme Court, <u>in discussing the transfer of utility assets under §393.190, RSMo</u>, discussed the Commission's duty to value a utility's property <u>for ratemaking purposes</u>. The Court, quoting from Priest, "Principles of Public Utility Regulation" said:

> "When public utility property is acquired by another public service company, should any cost of acquisition in excess of 'the cost of such property to the person first devoting it to public service' be included in an original-cost rate base? Regulatory agencies which have said 'No' constitute a majority, <u>but there is much respectable authority to the contrary</u>. If the transaction was at arm's-length, if it resulted in operating efficiencies, if it received regulatory approval as having been in the public interest, if it made possible a desirable integration of facilities, the 'excess' over original cost was capital dedicated to the public service. And that capital would seem entitled to amortization out of operating expenses, rather than 'below the line,' or out of income. <u>That burden of proof may be onerous, but it has been met</u>." (emphasis added). *Id.* at 399.

Clearly, UtiliCorp's request is not a radical departure from established norms. In fact, in the past, this Commission has evaluated each merger on its own merits and has concluded that different circumstances have necessitated different approaches and solutions. In one case, an earnings sharing grid was approved with target returns set high enough to allow for full or partial recovery of the premium or acquisition adjustment. *Re Union Electric Company*, Case No. EM-96-149, 176 P.U.R. 4th 201, 6 Mo. P.S.C. 3d 28. In another case, a rate freeze was established for a period of time that allowed for a full or partial recovery of the acquisition adjustment. *Re Western Resources Inc.*, Case No. EM-97-515, (September 2, 1999). Once again in this case, UtiliCorp urges the Commission to continue its policy of considering rate recovery of premium on a case by case basis and to approve the proposed Regulatory Plan, or some other plan or procedure which will give UtiliCorp a reasonable opportunity for premium recovery.

The Staff would have the Commission believe that it does not have the authority to determine this issue in a merger case and the Public Counsel contends that there is nothing in § 393.190 RSMo specifically authorizing any ratemaking determinations in a merger case. (Initial Brief of Public Counsel at 4). The statute, however, clearly does not prohibit such a determination. In fact, the Commission in the recent past ruled on a "rate-case" issue in a non-rate case proceeding. (*See Re UtiliCorp United Inc.*, Case No. GA-94-325 (1994). There are other instances in which the Commission has established depreciation rates outside the context of a rate case, which depreciation rates were later reflected in cost of service.

Also on point is a Report and Order issued by the Commission on November 13, 1973 in Case No. 17,873, a proceeding involving an application by Laclede Gas Company for an order determining the amounts of certain acquisition adjustments and permitting the transfer of those amounts from certain accounts and further permitting the amortization of those accounts over 40 years as an operating expense. (In this regard, Laclede's request was much more aggressive than

UtiliCorp's in this case. Laclede asked for a specific ratemaking determination. UtiliCorp only seeks a reasonable opportunity to obtain a favorable ratemaking determination at a later date.) In its Report and Order, the Commission determined the amounts of the acquisition adjustments in question, approved the transfer of the total acquisition adjustment from account 186 to account 114, and approved a 40 year amortization of the acquisition adjustment. Laclede's request for authority to charge the amortization against operating expenses, a "rate case" type issue, was contested and the Commission found against Laclede on the grounds that no showing had been made which would justify the inclusion of the acquisition adjustment in the operating expenses of the company.

In other words in the Laclede case, the Commission made a decision on the ratemaking treatment to be afforded an acquisition adjustment outside the context of a rate case. This is clearly additional precedent for the proposition that the Commission does have this authority and has in fact in the past made "rate case" type decisions outside the context of a rate proceeding. The concept is neither novel nor unlawful.

In the event UtiliCorp meets its burden of proof in the Post-Moratorium rate case and the Commission allows rate recovery of the Assigned Premium, this Commission will be acting in a manner consistent with the regulatory principles discussed by the Missouri Supreme Court in the Martigney Creek case, <u>supra</u>. The Commission would also be acting in a manner consistent with other states which have, in fact, permitted rate recovery of a portion or all of the cost of acquisitions.

The Massachusetts Department of Public Utilities determined that where potential benefits for customers exist, it is not in the interest of those customers, the shareholders of the utility, or the state to maintain a barrier against mergers. *Re Guidelines and Standards for Acquisitions and Mergers of Utilities*, 155 P.U.R. 4th 320.

The Oklahoma Corporation Commission, in *Re Oklahoma Gas and Electric Co.*, 150 P.U.R. 4th 33 (Okla. Feb. 25, 1994) established the following criteria in determining whether to allow rate recovery of an acquisition premium:

1) The public interest must be considered.
2) The purchase price must be reasonable.
3) The benefits to ratepayers must equal or exceed the cost of the acquisition premium.
4) The transaction must be conducted at arm's length.

(Ex. 4, p. 23).

Rate base treatment and/or cost of service treatment for acquisition premiums has been allowed by regulatory commissions under various circumstances, including:

1) when acquisitions represent an essential or desirable part of an integration of facilities program devoted to serving the public better;

2) when acquisitions are clearly in the public interest, because operating efficiencies offset the excess price over net original cost; and

3) when acquisitions are determined to involve arm's-length bargaining.

(Ex. 4, p. 24).

The Tennessee Public Service Commission allowed both rate base and cost of service treatment for acquisition adjustments of a telephone company where the acquisitions were found to be in the best interest of the public and not for the purpose of inflating the rate base. (79 P.U.R. 3rd 499, Tenn. 1969). *Re United Inter-Mountain Telephone Company.*

In a 1955 Virginia Supreme Court of Appeals decision, the Court ruled that the Virginia State Corporation Commission had properly allowed both rate base and cost of service treatment for an amount paid at arm's length bargaining in excess of original cost. (8 P.U.R. 3rd 120, Va. 1955). *Board of Supervisors of Arlington County v. Virginia Electric and Power Company.*

In 1946, the Louisiana Public Service Commission allowed rate base and cost of service treatment for an acquisition adjustments. *Louisiana Public Service Commission v. Louisiana Power & Light Company* (65 P.U.R. (NS) 18, La. 1946). In that case, the Louisiana Commission stated:

> The owners of a public utility are entitled to earn and receive a fair rate of return upon the money prudently invested in property used and useful in rendering public service. Money is prudently invested, even though it is in excess of the original cost of the property purchased, if the excess of purchase price over original cost was paid as the result of arm's-length bargaining between nonassociated buyer and seller, if the excess was necessary for the integration of the property into a larger and more efficient system, and if the purchase necessitating the excess did or reasonably should have resulted in public benefit by improvement of service to customers or in lowered rates or both better service and lowered rates. This integration cost or excess of purchase price over original cost termed in prescribed system of accounts as 'Utility Plant Acquisition Adjustments' should remain a part of the prudent investment during the life of the physical property to which it was applied, and its extinguishment from the investment when and if required by the Commission, should be accomplished by amortization through annual charges to Operating Revenue Deductions during the life of the property remaining after the date of the purchase which created the excess. (65 P.U.R. (NS) 23).

In 1991, the Kansas Corporation Commission in *Re Kansas Power & Light Co.*, 127 P.U.R.4th 201, established a policy with regard to acquisition adjustments which in essence provides that to the extent that savings can be shown, the acquisition premium will receive ratemaking treatment in a future rate case. In that case, the Kansas Commission stated:

> The Commission cannot ensure the recovery of the AP. The Commission can only ensure the opportunity to recover the AP. The Commission believes the appropriate regulatory treatment of the AP is to tie the potential recovery of the AP to benefits that will be realized by ratepayers as a result of the merger. In this case, the amount of the AP to be included in rates shall be tied to the savings

> reasonably projected to be generated by the merger. Applicants in future merger cases will have the burden of quantifying benefits that will accrue to ratepayers as a result of the merger. The Commission will not necessarily limit benefits to operating cost savings but will look at a variety of factors in determining ratepayer benefits. For example, Utility A is acquired by Utility B and Utility B is able to bring financial strength to make improvements to Utility A; Utility B may be allowed to include in its rates an AP commensurate with the improvements it was able to effect through its financial strength.
>
> In this case where ratepayer benefits are tied to synergies that can be generated from cost cutting measures and synergies resulting from the overlapping service territories, to identify and quantify savings becomes a critical component of Applicants' burden of proof. The savings to be generated by the acquisition must be reasonably identified and capable of quantification, otherwise the Commission has no reasonable way to assess whether there are benefits for ratepayers.

(Ex. 4, p. 26).

More recently, in *Re UtiliCorp United Inc. dba West Plains Energy Kansas* 198 P.U.R. 4th 397 the Kansas Corporation Commission allowed UtiliCorp to recover in rates $2.35 million of some $5 million of the annual cost of the acquisition premium in connection with UtiliCorp's acquisition of electric assets from Centel Corporation. The burden of proof was on UtiliCorp in that case to demonstrate that the claimed savings would not have been created except for the Centel acquisition, the same burden of proof which UtiliCorp will be expected to meet under its proposed Regulatory Plan in this case. The issue was not so complex that the Kansas Commission could not deal with it, the fear expressed by the Staff in this case.

The point of all this is that there is sound Missouri authority and ample precedent from other jurisdictions to allow premium recovery. UtiliCorp urges the Commission to continue its policy of considering premium recovery on a case by case basis. UtiliCorp simply wants a <u>reasonable opportunity</u> through an indication from the Commission that if UtiliCorp meets its burden, the requested rate treatment will be authorized.

2. **Previous Merger Cases**

A theme throughout the Staff's Initial Brief is that this merger case is somehow "different" than other merger cases presented to this Commission and that this "difference" requires the Commission to reject the merger proposal. This argument is less than compelling, without logic, and ignores the law. Once again, in Missouri the law is that if the transaction is not detrimental to the public, it should be approved.

The Staff maintains on several different occasions in its 200 page document that it knows of no other Missouri case in which the applicants did not project that savings from the merger would exceed the merger costs. Even assuming that the Staff is correct in its assertion with respect to this case, which UtiliCorp denies, the point is totally irrelevant. Nowhere in its Initial Brief does the Staff even attempt to argue that the proposal is contrary to established Missouri law. Nowhere does the Staff present a case from another jurisdiction where a <u>claim</u> that anticipated costs exceed anticipated benefits automatically invalidates a merger attempt.

What is clear from all of this is that the real problem with this case, from the standpoint of the Staff and Public Counsel, is the fact that UtiliCorp continues to press for the <u>opportunity</u> to recover some premium costs directly through rates, and has been unwilling to drop this request as a condition of merger approval. As has been explained previously, UtiliCorp cannot give in to this demand. The proposed Regulatory Plan, with its <u>opportunity</u> for premium recovery, or some other approach which will give UtiliCorp a reasonable opportunity to obtain a return on its investment, is <u>absolutely essential</u> to the financial viability of this transaction. (Ex. 3, p. 10). In this regard, UtiliCorp really seeks a result no different than this Commission afforded Union Electric Company when it approved its merger with CIPSCO and at the same time authorized an extension of a "sharing plan" <u>designed to allow UE to earn and keep up to 12.6% return on equity.</u> (*See Re Union Electric Company*, <u>supra</u>).

3. **Costs to Achieve**

The Staff claims that customers will bear the brunt of the involved transition costs, or "costs to achieve" the merger. This assertion is an overstatement. While it is true the Regulatory Plan will allow UtiliCorp to recover some of its costs in rates, the savings in synergies will far outweigh those costs and the customers will experience a net reduction in cost of service. Public Counsel also argues that it is inappropriate for ratepayers to pay for transition costs. (Initial Brief of Public Counsel at 32.) This argument, however, fails because it has nothing to do with the legal standard the Commission is required to apply to this merger. Once again, ratepayers will experience no detriment from the merger if they pay some of the transition costs, because under the Regulatory Plan this will only happen if merger synergies exceed the Assigned Premium and costs to achieve, resulting in a net benefit to ratepayers.

Under its proposal, UtiliCorp will recover in rates the costs to achieve the transaction such as those costs associated with executive severance payments. Specifically, executive severance payments approximating three years of salaries will be incurred in order to realize the synergies from eliminating the salaries of those executives over the ten years of the Regulatory Plan. To reflect in cost of service the synergies from the elimination of ten years of executive salaries, while at the same time not reflecting the executive severance costs needed to achieve those savings, would not be fair. Moreover, actual rate recovery of executive severance costs is projected to be less than half the actual costs due to time value of the recovery and the shortfall of synergies during the five year moratorium period. (Ex. 8, pp. 15-16).

In addition, UtiliCorp should recover in rates the costs of the Advisory Board. The Advisory Board is provided for in the merger agreement and is necessary to accomplish the transaction. The cost of three years of the Advisory Board replaces the cost of ten years of the SJLP Board of Directors. Again, not to recognize the merger-required costs of the Advisory Board, while at the same time passing on the related synergies to customers, would clearly not be fair. Also with respect to this item, actual cost recovery is projected to be less than half the actual costs due to time value of the recovery and the shortfall of synergies during the moratorium. (Ex. 8, pp. 15-16).

Further, UtiliCorp should recover in rates the costs associated with full funding of SJLP's Supplemental Executive Retirement Plan. The funding of the Supplemental Executive Retirement Plan is included in current cost of service for SJLP as a stand-alone company. The elimination of annual funding of these costs will be included as a synergy over ten years because the full funding to be paid at closing will eliminate the annual funding requirement. To reflect the synergies over the ten years, but to disallow the funding costs that eliminated the annual costs would clearly not be fair. Again, cost recovery for this item is projected to be less than half the actual costs due to time value of the recovery and the shortfall of synergies during the moratorium. (Ex. 8, p. 15).

UtiliCorp intends to track those "costs to achieve" that are deemed eligible for rate treatment to ensure rate recovery. While the Staff is technically correct in suggesting that the customers will pay for some of these costs, these same customers will receive a net gain because of the merger. In the final consideration, there is no detriment to the public resulting from UtiliCorp's proposal for "costs to achieve."

4. **Frozen Capital Structure**

The Staff argues that the frozen capital structure proposal contained in the Regulatory Plan will deny customers any of the benefits which result from the merger. This assertion is incorrect and reflects a basic misunderstanding of the proposal. First, customers of the SJLP operating unit will benefit from the merger through the guaranteed $1.6 million in reduction of cost of service in any event. Further, the applicable standard is whether the merger is detrimental to the public interest, not whether customers get a benefit. In this regard, the Staff does not assert that the frozen capital structure proposal will be a detriment; only that it will not result in a benefit. Again, the Staff and others miss the point. Missouri is a "no detriment" state. The status quo is acceptable. The frozen capital structure will accomplish this.

The rates for the SJLP unit in Years 6-10 post-merger should be calculated using the stand-alone SJLP capital structure advocated by the Staff in Case No. ER-99-247 - - that is 47% debt, 53% equity. The reason for this structure is that, absent the merger, the capital structure for SJLP as a continued stand-alone company would not change appreciably and as a consequence using this 47% debt, 53% equity capital structure will result in no "new" cost for the SJLP customers. (Ex. 4, p. 28). In addition, because UtiliCorp will be converting 100% of SJLP existing equity to UtiliCorp equity, no decrease in the equity investment actually occurs. (Ex. 2, pp. 5-6). Because no new or increased costs will be passed on to SJLP customers, this aspect of the Regulatory Plan is clearly not detrimental to the public interest.

5. **Tracking Merger Savings**

The heart of the challenge of the Staff and Public Counsel to the Regulatory Plan is a claim that the guaranteed $1.6 million in savings is a "fiction" because the savings tracking methods are speculative. The Staff claims "the problem with merger savings tracking is not the degree of sophistication of accounting systems, but the inherent lack of knowledge people have of the effect of events and actions that did not occur." (Initial Brief of Staff at 39.)

The Staff misses the point. Even if UtiliCorp is unable to meet its burden of proof in the Post-Moratorium rate case either because of a lack of synergies or an inability to track and prove them, customers of the SJLP unit still obtain a $1.6 million reduction in cost of service. <u>And because the Staff admits that in that Post-Moratorium rate case it will be impossible for the Staff to prove that rates for the SJLP unit would have been lower absent the merger, it really doesn't matter whether or not savings can be tracked.</u> UtiliCorp accepts the burden of proving synergies, and if it cannot do so effectively, it will not obtain rate recovery of the Assigned Premium. A savings of $1.6 million, however, is still guaranteed.

While UtiliCorp has presented a thorough method of tracking savings, the approval of a specific tracking system, however, is not critical to approval of the merger. As indicated, under its proposed Regulatory Plan, UtiliCorp will have the burden to show in the Post-Moratorium rate case that it has been able to both track and quantify merger savings. UtiliCorp believes that it will be able to meet this burden. For a complete discussion on the methods UtiliCorp plans on implementing to track merger savings, and the benchmark values, see Initial Brief of UtiliCorp, at 39-46.

Finally on this point, UtiliCorp has recently been successful in demonstrating to the Kansas Corporation Commission merger savings sufficient to allow direct rate recovery of a portion of an acquisition premium. (*See In Re UtiliCorp United Inc. dba West Plains Energy Kansas*, supra). If nothing else, the recent Kansas case indicates that merger savings are real and demonstrable and not a "fiction" as alleged by the Staff.

6. **Savings to Missouri Customers**

The Staff asserts that the merger savings realized by customers will be insignificant. Simply put, this claim is irrelevant. While UtiliCorp disagrees with the merits of Staff's argument on this point, given that the forecasted savings have been detailed at every step in this process, the argument does not matter. The applicable standard is whether the merger is detrimental to the public interest. In other words, even assuming the Staff is correct, the public will not experience a detriment which is the lawful standard. Under Missouri law, the merger is not required to benefit customers.

7. **More Savings to SJLP Customers than MPS Customers**

Although the Staff apparently does not believe the savings are significant, it argues that SJLP customers will get a proportionally higher share of those savings than MPS customers and somehow this should result in the Commission rejecting the merger. AGP makes a similar argument claiming the proposed merger and Regulatory Plan are "out of balance". (AGP at 13). Again, these arguments ignore the no detriment to the public interest test. Furthermore, they ignore the sound rationale behind this aspect of the Regulatory Plan.

As previously indicated, one of the purposes of the Regulatory Plan is to ensure that savings are passed on to customers of the SJLP unit to offset the costs resulting from the transaction which are also assigned to that unit. In other words, no merger-related benefits are flowed to MPS customers because those customers are not being asked to pay any of the merger-related costs.

8. **Market Power Conditions**

The Staff and Public Counsel argue that the merger will increase the vertical, horizontal, and retail market power of UtiliCorp and that this will be a detriment to the public. Much of Public Counsel's argument on this claim is based on what it believes might happen in the future with respect to other mergers in other states involving UtiliCorp. (Initial Brief of Public Counsel at 21-22.) Not only are these assertions pure speculation, they have absolutely nothing to do with this case.

The Staff argues that UtiliCorp should be required to commit to join a single regional transmission organization ("RTO") before the October 15, 2000 deadline of FERC Order No. 2000. UtiliCorp opposes this request. As discussed by the FERC in its Order, approving this merger, UtiliCorp, as with other utilities, has several choices as to which RTO to join. UtiliCorp should be given the same latitude as all other public utilities under FERC Order 2000 regarding the timing of its statement of intentions with respect to the specific RTO it intends to join. No compelling reason exists to single out UtiliCorp and SJLP here and treat them differently than any other public utility subject to the same deadline. The FERC understands and agrees with this notion, as it said: "We accept Applicants' commitment to join an RTO ... and rely on it in approving these mergers." *Order Conditionally Authorizing Mergers*, FERC Dockets EC00-27-000 et al., p. 13 (July 26, 2000).

UtiliCorp also should not be subjected to market provisions decided in a previous case, as Public Counsel argues. Case No. EM-97-515 concerning Western Resources was a different case with a different set of conditions and circumstances and its provisions are not applicable here. UtiliCorp is subject to the requirements of the FERC in regard to joining an RTO, as noted above. Further, the FERC has found that special conditions argued for by intervenors are not appropriate in this regard. *Id.*, p. 13.

With regard to horizontal market power, the Staff contends that UtiliCorp should submit a study in anticipation of retail competition in Missouri. UtiliCorp opposes such a study as it is premature. UtiliCorp stated in its direct testimony that it will comply with requirements ordered by the Commission for studies at that future time. (Ex. 5, p. 8) At this point, it is only speculation as to when and if retail competition will occur. Further, UtiliCorp should not be expected to agree now to complete a study under conditions that may be contrary to conditions the Commission believes are appropriate at the appropriate future time when such a study is ordered. (Ex. 5, p. 8).

Springfield, in its brief, argues that the merger will allow UtiliCorp to take valuable, limited transmission capacity necessary for other Missouri utilities. (Springfield Brief at 4). This argument is speculative, at best. UtiliCorp is the third largest electric company in the state, and will remain so after the merger. Its position in the state regarding transmission capacity will not dramatically change because of this merger such that it will hinder other utilities. Given that Springfield's argument relies on speculation rather than facts, it should not sway the Commission.

Finally, these arguments raised by the other parties on this point do not show any detriment to the public or that the proposed Regulatory Plan is insufficient in any way.

9. **Transmission Access and Reliability**

This is an issue where there has been a lot of sound and fury (from Springfield) signifying nothing. No evidence was produced that the merger will actually bring about a detrimental effect on the transmission system or the ratepaying public. Indeed, exactly the opposite is true because a physical connection between UtiliCorp and SJLP via a new transmission line constructed after the merger (Lake Road to Nashua) can only *increase* the available transmission capacity in the area. (Ex. 13, p. 7)

Springfield made the most noise about this issue, but it really had no standing to be in this case in the first place. A merger between UtiliCorp and SJLP doesn't affect Springfield in the slightest given that Springfield is down in the southwest part of the state -- far away from any future physical interconnection between the transmission systems of UtiliCorp and SJLP in the *northwest* part of the state.

Springfield seems to be most concerned about the possible effect of the merger on a future capacity purchase it has made with KCPL out of KCPL's Montrose plant. Simply looking at a map shows that to get from the Montrose generating plant in Henry County (southeast of Kansas City) to Springfield in Greene County, you do not go through SJLP's territory in northwest Missouri, unless you are hopelessly lost. There was no evidence that any proposed power transactions or line construction between SJLP and UtiliCorp after the merger would have any negative impact whatsoever on Springfield on anyone else.

Springfield's witness claims the MPS system of UtiliCorp is "weak and unreliable." (Springfield Brief at 12) If that were really true, there undoubtedly would have been published reports of problems in the service territory during the last heat wave around Labor Day. (Springfield Brief at 11-12) There were none. That is because Springfield's witness is relying on the *hypothetical* results of a computer model which shows a potential problem on the Sibley to Duncan transmission line in a "worst-case" scenario. (Tr. 1289) Mr. Kreul of UtiliCorp explained that this was nothing of immediate significance. "UCU is aware that ... [the line] can become slightly overloaded during certain contingencies. UCU currently has an operating procedure in place to reduce the loading on these lines, should these contingencies occur." (Ex. 13, p. 3) Mr. Kreul added that this operating procedure, which is more economical than building new facilities, has been demonstrated to be effective on a number of previous occasions. (Id. at 3-4) Implementing the operating procedure, which involves changing the amount of generation at either the Sibley or Greenwood plants, eliminates the problem. (Tr. 1289) In short, there was no evidence that the Sibley to Duncan line has anything to do with a physical connection between UtiliCorp and SJLP post-merger and it does not prove that the UtiliCorp system is weak and unreliable.

On a topic that at least had some relevance to the northwest part of the state, Springfield's witness raised concerns about a previously known problem with one of KCPL's lines (Lake Road to Nashua). UtiliCorp's witness, however, explained that KCPL is aware of its problem and it also has an operating procedure to open up the line when it comes close to an overload situation. (Ex. 13, p. 4) Springfield never explains how the existence of this pre-existing problem *on a KCPL-owned line* is a detriment to the merger of SJLP and UtiliCorp. In contrast, Mr. Kreul explained that if the merger is approved, UtiliCorp will construct a new and separate line from Lake Road to Nashua, and thus eliminate the current problem with the KCPL line and at the same time "increase the reliability at both Lake Road and Nashua." (Ex. 13, p. 6) The study performed by UtiliCorp estimated that constructing this new line after the merger will increase available transmission capacity in the region by roughly 700 MW. (Id.) Increasing available transmission capacity in the region is a clear benefit from the merger, not a detriment.

●Since Springfield could not demonstrate any actual negative effects from the merger, it tried hard to show *potential* negative effects so it could justify its proposed conditions. These hypothetical effects are briefly discussed here, but the Commission needs to ask three questions about these Springfield hypotheticals. The first is whether Springfield has demonstrated that they are likely to occur; the second is whether the Commission has subject matter jurisdiction to remedy the situation; and the third concerns the motive of Springfield in raising these arguments. Springfield claims there will be post-merger problems with power transfers between UtiliCorp and SJLP territories unless they are required by the Commission to be posted on the OASIS network. This is a trumped-up charge since UtiliCorp/SJLP transfers do not even come close to the Springfield area. The Staff's brief notes that the Southwest Power Pool (SPP) study does not conclusively show the validity of Springfield's concerns. (Staff Brief at 195) The merger will actually improve transmission capacity in that region because of a new line (Lake Road to Nashua) that would <u>only</u> be built if the merger occurs. By definition, native load does not have to be posted on OASIS. The FERC does not consider native load transfers to be of significance in this regard. If the Commission were to condition the merger on such a provision, it may actually harm UtiliCorp customers for the sole benefit of Springfield -- which is not even regulated by the Commission as to its electric operations. If Springfield wants a greater "firmness" and priority for its wholesale transactions with KCPL, Springfield ought to pay for that itself. **It is not the Commission's statutory role to protect Springfield from hypothetical problems by making UtiliCorp and SJLP ratepayers fund solutions.** OASIS is also a purely federal invention. Therefore, any order of the Commission in this regard would have to be scrutinized to see if it is preempted by federal regulation in this area and to determine if it meets the Missouri statutory criteria for the Commission to order operational changes. The Commission needs to remember that Springfield is obviously looking out for its own financial interests. The Commission should also ask itself why the people who actually own and operate transmission lines in the western part of the state (such as AmerenUE, KCPL, Associated Electric Cooperative, KAMO, and others) are not intervenors in this case raising the same concerns as Springfield. Perhaps it is because they do not think there are such problems.

• Springfield says its study was corroborated by the SPP study. (Springfield Brief at 13) The SPP study was performed under a set of assumptions. One was a "worst-case" scenario which is not likely to happen in the real world. (Tr. 1290-91) Another is that <u>none</u> of the proposed physical interconnections to be built after the merger were included. UtiliCorp asked SPP to perform a study for "network service" which is an alternative to UtiliCorp building physical connections between itself and SJLP and Empire. The transmission lines UtiliCorp says it will build after the merger are not included in the SPP study. UtiliCorp has since determined not to take network service from SPP due to its cost. UtiliCorp's study is a more accurate assessment of the impact of the merger on the region. It showed no loading violations and only one irrelevant voltage violation. (Ex 13, p. 2)

• Springfield claims at page 15 of its brief that UtiliCorp originally agreed to make upgrades shown in the SPP study but now has "backed away." No such commitment to build whatever SPP recommended ever existed. UtiliCorp was simply exploring different ways to connect the systems. Network service through SPP was one possibility. Building new transmission lines was another. The SPP study shows the need for expensive upgrades that would not particularly benefit UtiliCorp ratepayers. What is really going on here is that Springfield wants the Commission to order UtiliCorp to participate in SPP because that makes UtiliCorp pay for new facilities that ultimately benefit Springfield at the expense of UtiliCorp ratepayers.

- Springfield says it wants UtiliCorp to be required to join the SPP ISO/RTO (Springfield Brief at 20) That is impossible since SPP's proposal to become an ISO was rejected by the FERC in May 2000. This demand again reflects the nature of Springfield's interest in this case. Springfield would benefit from such an order at the expense of UtiliCorp ratepayers. The Staff recognized this when it said in its brief that it can not support the "SPP Proposal" because it requires UtiliCorp to pay the full incremental cost of an upgrade without revenue recovery. (Staff Brief at 193-194) That is another way of saying that UtiliCorp's ratepayers pay and Springfield gets the benefit. Finally, the Commission does not have to order UtiliCorp to join an ISO/RTO. As noted earlier, UtiliCorp has already committed to the FERC that it will signify its intent by October 15, 2000.

- Springfield claims UtiliCorp could "re-functionalize" its transmission facilities in anti-competitive ways. (Springfield Brief at 20) There is no evidence UtiliCorp intends to do this, so there is no evidence of an imminent detriment. Even if UtiliCorp were to do that in the future, and Springfield claims harm as a result, where is the proper forum for the resolution of that complaint? Surely the Commission realizes that the proper forum is FERC.

All of the above, and other concerns raised by Springfield that are not addressed specifically here because they are of the same unsubstantiated and hypothetical flavor, are simply Springfield's attempt to get something for nothing. If Springfield can convince the Commission to strap UtiliCorp with onerous and unnecessary conditions that ultimately benefit Springfield's ability to purchase wholesale power at a lower cost than otherwise, Springfield will be the winner and the UtiliCorp ratepayers, who have to pay for that, will be the long-term losers. Springfield has made all these same arguments to the FERC, who ultimately has jurisdiction over the transmission systems. The FERC was not impressed with the merits of the arguments. The Commission should similarly reject Springfield's arguments here for what they are – self-serving and motivated solely by financial concerns. Springfield already has a proper forum if it considers that it has been wronged by some future transmission situation. The FERC has the authority to remedy any harm it may find.

Load Flow Studies. The recommendation of the Staff for the production of further load flow studies before the Commission decides this case is simply overkill and justification for the Staff to further delay the merger. The essence of the Staff recommendation is to spread out the study over the entire year. The UtiliCorp and SPP studies already examine the region at peak load conditions, and show no problems of concern or significance. If there are no problems at the peak load conditions when everything is strained, logically there are not going to be problems when there is plenty of available capacity on the system during non-peak conditions. Requiring UtiliCorp to do the study the Staff recommends would be like requiring someone to test whether your car starts every day during the summer to determine if it will start on the coldest morning in the winter.

DNR / Energy Efficiency

The lengthy DNR brief presents a law-review type article on the law of mergers in other jurisdictions and in different circumstances than are present here. It would be a waste of time for UtiliCorp to respond to that here because it is irrelevant. The legal standard applicable here is not found in cases involving shoe stores, cellophane or banks. It is the "not detrimental to the public interest" standard found in *City of St. Louis*, supra. That case does not require the Commission to identify esoteric "markets." The DNR brief is incorrect (beginning on page 9) when it concludes that there must be a "passing on of benefits." The quotation, which deals with identifying benefits for another purpose, does not support the conclusion argued by DNR. (See the earlier discussion on the legal standard applicable here.)

DNR obviously has concerns about the plight of low-income residents of the state. So does UtiliCorp and SJLP, and so undoubtedly does the Commission. That topic, however, is much broader than a merger between two utility companies. Other than speculation by DNR's witnesses, there was no hard evidence that the merger of SJLP and UtiliCorp will detrimentally affect low-income customers in the SJLP territory. Unlike situations discussed by DNR where mergers might remove a vendor from the market, and thus reduce potential consumer choice, the customers after this merger will continue to receive at least the same level of electric and natural gas service, or better, than they received before. The electricity will flow through the same wires and the natural gas will flow through the same pipes, and the customers can contact the same local offices and personnel.

The facts are that UtiliCorp will offer the same assistance and programs to the type of customers targeted by DNR as SJLP does today. UtiliCorp will maintain the local office in St. Joseph with adequate staffing levels. (Ex. 10, p. 22) The level of customer service will actually increase as a result of the merger since the SJLP customers will have access to a round- the-clock call center, while SJLP only provides that service during normal working hours. (Ex. 9, p. 4) UtiliCorp is flexible in dealing with customers and is also less strict in collection policies than SJLP. (Ex. 10, pp. 22-23) The UtiliCorp service center employees have access to a computerized listing of agencies ("ATLAS") in the state that can provide assistance to customers needing it, or can put them into contact with a local representative. (Ex. 10, p. 22-23)

At page 23 of its brief, DNR contends that "low-income customers have certain rights under PSC regulations." That may be true, but it is not solely due to their level of income. UtiliCorp observes that the Commission's regulations do not purport to define what is a "low-income" customer. Neither do those regulations offer remedies only to "low-income" customers. The remedies and procedures available in 4 CSR 240-13 make no distinction regarding the customer's income. DNR is also mistaken when it implies on page 25 that the merger will somehow override the Commission's regulations. As the Commission well knows, no internal policy of UtiliCorp may take precedence over the Commission's rules. The Commission has already dealt with concerns in this area on a state-wide basis by adopting provisions such as 4 CSR 240-13. There is no justification or authority for the imposition of special requirements on certain utilities as advocated here by DNR.

Utility companies cannot be expected to transform low-income customers into middle-income customers as a result of a merger or to solve all their "payment troubles." The overall economy probably has more to do with the economic status of customers than anything else. The General Assembly makes the policy for the state and determines where and how tax revenues are spent. If it wants to triple the amount of funds it devotes to programs such as LIHEAP, it has the means and authority to do that. No law in this state, however, requires that a merger of two utility companies produce a benefit to an unidentified class of "low-income" customers or requires utility companies to enter into "pilot projects." UtiliCorp already voluntarily focuses a great deal of efforts in the area as explained in detail by Mr. Pella. (Ex. 10 pp. 24-28). It simply would be unreasonable and inappropriate for the Commission to impose the conditions DNR requests.

Other Arguments Raised in Opposition to the Merger and Regulatory Plan

Pooling v. Purchase Accounting. The Staff devotes ten pages of its 200 page brief on the differences between "pooling" and "purchase" accounting. (Initial Brief of Staff at 87-97.) Its main contention is that pooling accounting would lead to more benefits resulting from the merger. The Staff does not claim that by using the purchase method of accounting UtiliCorp's proposal is detrimental to the public. Therefore, the argument is not relevant. However, UtiliCorp has demonstrated through testimony that the pooling method is not even an option in this transaction. In fact, the Generally Accepted Accounting Principles mandate that, given the circumstances, UtiliCorp use the purchase accounting method in this case. The pooling method would have run afoul of the guidelines and would have placed the entire merger in jeopardy. (Ex. 26). That fact is not refuted by Staff.

Electric Allocations Agreement. Again, the Staff argues that MPS will not be allocated the same benefits as SJLP and again, this argument is not relevant. As described in the Initial

Brief of UtiliCorp, these costs and profits should flow to SJLP to offset the merger costs. This is of particular importance when it comes to profits from off-system sales which represent a significant portion of the anticipated merger savings.

As has been explained previously, energy costs and profits from off-system sales associated with the joint dispatch of both the MPS and the SJLP power supply resources should be allocated to the SJLP operating unit because these incremental margins would not be possible except for the addition of the SJLP power supply portfolio and transmission assets. Moreover, allocation of 100% of the incremental margins to SJLP places the benefits with the operating unit which has incurred the costs, including premium costs, necessary to combine the companies and bring about the synergies. (Ex. 20, p. 11). UtiliCorp's decision to concentrate both the merger benefits and the merger costs in the SJLP operating unit is appropriate and makes sense for the reasons indicated and will also simplify matters by avoiding issues concerning the allocation of premium and other costs to existing MPS customers.

Administrative and General Costs. The Staff contends that the Regulatory Plan will allow UtiliCorp to recover A&G costs at a much higher rate than would be recovered compared to SJLP's stand-alone A&G levels. This statement is patently false and ignores the fact that no costs can flow through rates without the Commission's consent. Furthermore, the Staff makes no real effort in its brief to support this assertion.

Affiliate Transactions Condition. UtiliCorp will comply with all lawfully promulgated and effective Commission rules.

Load Research Condition. UtiliCorp agrees to treat MPS and SJLP separately for load research purposes as long as they have a separate rate structures. UtiliCorp intends to in-source

MPS's load research program. UtiliCorp has improved MPS's load research program. UtiliCorp disagrees with Staff's recommendation regarding staffing levels and frequency and standards for load research data.

Public Counsel's Regulatory Plan Condition. This plan is unacceptable to UtiliCorp as it would render the proposed merger economically unfeasible.

Access to Books and Records Condition. There is no reason for the proposed condition because legally an agreement to comply with a lawful rule is redundant. UtiliCorp agrees to comply with all lawfully promulgated and effective Commission rules. (Ex. 5, p. 17).

Conclusion

This Reply Brief has demonstrated that this merger is not detrimental to the public interest, the standard that must drive the Commission's decision in this case. Opposing parties, especially the Staff, have simply attempted to confuse the issues in this case by arguing, again and again, that the merger is not beneficial enough or that the merger is different than other mergers. These arguments are absolutely irrelevant to the task at hand. The Commission must approve the merger if it finds that it is not detrimental to the public interest and no record evidence of such detriment exists. With respect to conditions, UtiliCorp respectfully submits that its Regulatory Plan, or some other comparable model that will create certainty by allowing UtiliCorp's shareholders a reasonable opportunity to obtain a return on their investment, is absolutely essential to the financial viability and thus, the completion of the transaction.

In the final consideration, the Commission should approve the merger between UtiliCorp and SJLP and the proposed Regulatory Plan. The "no public detriment" standard is clearly satisfied. The merger as proposed will benefit all stakeholders and the long term economic development of the State of Missouri.

Respectfully submitted,

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Certificate of Service

I hereby certify that a true and correct copy of the above and foregoing document was sent by U.S. Mail, postage prepaid, or hand-delivered, on this 3d day of October, 2000, to all parties of record.