**STATE OF MISSOURI**
**PUBLIC SERVICE COMMISSION**
**JEFFERSON CITY**
**December 28, 2000**

**CASE NO: EM-2000-369**

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**Enclosed find certified copy of REPORT AND ORDER the above-numbered case(s).**

**Sincerely,**

Dale Hardy Roberts

**Dale Hardy Roberts**
**Secretary/Chief Regulatory Law Judge**

# BEFORE THE PUBLIC SERVICE COMMISSION

# OF THE STATE OF MISSOURI

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| In the Matter of the Joint Application of UtiliCorp United Inc. and The Empire District Electric Company for Authority to Merge The Empire District Electric Company with and into UtiliCorp United Inc., and, in Connection Therewith, Certain Other Related Transactions | ) ) ) ) ) ) ) | Case No. EM-2000-369 |

## REPORT AND ORDER

**Issue Date: December 28, 2000**

**Effective Date: January 7, 2001**

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## APPEARANCES

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**and**

**Leslie Jackson Parrette, Jr.**, Attorney at Law, UtiliCorp United Inc., 20 West 9th Street, Kansas City, Missouri 66209, for UtiliCorp United Inc. and The Empire District Electric Company.

**Stuart W. Conrad**, Attorney at Law, Finnegan, Conrad & Peterson, L.C., 3100 Broadway, Suite 1209, Kansas City, Missouri 64111, for ICI Explosives USA and Praxair Inc.

**Shelley Woods**, Assistant Attorney General, Office of the Attorney General, Supreme Court Building, Post Office Box 899, Jefferson City, Missouri 65102, for the Missouri Department of Natural Resources.

**Jeffrey A Keevil**, Attorney at Law, Stewart & Keevil, 1001 Cherry Street, Suite 302, Columbia, Missouri 65201, for the City of Springfield, Missouri, through the Board of Public Utilities.

**William A. Jolley**, Attorney at Law, Jolley, Walsh, Hurley & Raisher, 204 West Linwood Boulevard, Kansas City, Missouri 64111, for the International Brotherhood of Electrical Workers, Local 1474.

**James B. Deutsch**, Attorney at Law, Blitz, Bardgett & Deutsch, 308 East High Street, Suite 302, Jefferson City, Missouri 65101, for Albert Fuchs, George Dorsey, Jack De Graffenreid, Richard Vanwinkle, Jack Wilson, Vernon Corkle, Verl Alumbaugh, Donald Crayne, Bill Athey and Glenn D. Rhoads (collectively referred to as the Empire Retirees).

**Douglas E. Micheel**, Senior Public Counsel, **John B. Coffman**, Deputy Public Counsel, Post Office Box 7800, Jefferson City, Missouri 65102-7800, for the Office of the Public Counsel and the public.

**Dana K. Joyce**, General Counsel, **Steven Dottheim**, Chief Deputy General Counsel, **Keith R. Krueger**, Deputy General Counsel, **Nathan Williams**, Senior General Counsel, **Dennis L. Frey**, Associate General Counsel, and **Bruce H. Bates**, Assistant General Counsel, Missouri Public Service Commission, Post Office Box 360, Jefferson City, Missouri 65102, for the Staff of the Missouri Public Service Commission.

**REGULATORY LAW JUDGE: Morris L. Woodruff.**

# REPORT AND ORDER

## PROCEDURAL HISTORY

On December 15, 1999, UtiliCorp United Inc. (UtiliCorp) and The Empire District Electric Company (Empire) filed a Joint Application seeking authority to merge Empire with and into UtiliCorp. The Commission, on December 16, 1999, issued an Order and Notice that provided notice of the filing of the application and notified interested parties that if they wished to intervene they should file an application with the Commission on or before January 14, 2000. Timely applications to intervene were received from the City of Springfield, Missouri, through the Board of Public Utilities (Springfield), Union Electric Company, d/b/a AmerenUE (AmerenUE), the Missouri Department of Natural Resources (MDNR), Praxair, Inc. (Praxair), ICI Explosives USA, Inc., and International Brotherhood of Electrical Workers, Local Union No. 1474 (IBEW No. 1474). On January 19, 2000, the Commission granted the applications to intervene of IBEW No. 1474, MDNR, AmerenUE[1], Springfield, Praxair and ICI.

After the filing by various parties of competing proposed procedural schedules, the Commission, on February 10, 2000, issued an order adopting a procedural schedule that set this case for hearing on September 11 through September 15, 2000. In that same order, the Commission denied separate motions filed by the Office of the Public

[1] Although AmerenUE was admitted as a party it did not appear for the hearing.

Counsel (Public Counsel) and MDNR that would have consolidated this case with Case No. EM-2000-292, the case established for consideration of UtiliCorp's proposed merger with St. Joseph Light & Power Company (SJLP).

On June 16, 2000, Albert Fuchs, George Dorsey, Jack De Graffenreid, Richard V. Vanwinkle, Jack Wilson, Vernon Corkle, Verl Alumbaugh, Donald Crayne, Bill Athey and Glenn D. Rhoads filed an Application to Intervene. The named individuals are retired former employees of Empire. On July 6, 2000, the Commission issued an order that permitted the named individuals to intervene out of time for good cause shown. The named individuals intervened as individuals and not as a class or a formal group; however, for purposes of convenience, this report and order will refer to them collectively as "the Empire Retirees."

The various parties prefiled testimony and an evidentiary hearing was held beginning on September 11 and continuing through September 15, 2000. Post-hearing briefs were filed on October 31, 2000, with reply briefs filed on November 21, 2000.

## Stipulations and Agreements

### Empire Retirees, UtiliCorp and Empire

On October 18, 2000, the Empire Retirees, UtiliCorp and Empire filed a stipulation and agreement that purported to resolve all the issues between them. The stipulation and agreement specifies the plan of retirement benefits for retired Empire employees as further clarification of Section 6.13 of the Agreement and Plan of Merger. On October 25, 2000, Staff filed a request for hearing on that stipulation and agreement. However, following a conference held on November 14, 2000, the Staff, on November 16, 2000, withdrew its request for hearing on the stipulation and agreement.

The stipulation and agreement was entered into only by the Empire Retirees, UtiliCorp and Empire. It was not signed by any other party and is therefore a non-unanimous stipulation. Commission rule 4 CSR 240-2.115(1) provides that if no party requests a hearing regarding a non-unanimous stipulation and agreement, the Commission may treat the stipulation and agreement as a unanimous stipulation and agreement. 4 CSR 240-2.115(3) provides that each party shall have seven days from the filing of the non-unanimous stipulation and agreement to file a request for a hearing. Failure to file a timely request for hearing shall constitute a full waiver of that party's right to a hearing. No party has requested a hearing regarding the stipulation and agreement between the Empire Retirees, UtiliCorp and Empire. Therefore, the stipulation and agreement will be treated as a unanimous stipulation and agreement.

The Commission has the legal authority to accept a stipulation and agreement as offered by the parties as a resolution of issues raised by the Empire Retirees in this case, pursuant to Section 536.060, RSMo Supp. 1999. After considering the matter, the Commission concludes that the stipulation and agreement filed by the Empire Retirees, UtiliCorp and Empire should be approved.

**UtiliCorp, Empire and Staff**

On November 30, 2000, UtiliCorp, Empire and Staff filed a stipulation and agreement that purported to resolve certain issues between them. Staff filed written suggestions in support of the stipulation and agreement on December 5, 2000. No other party has filed a response to the stipulation and agreement.

The stipulation and agreement was entered into only by UtiliCorp, Empire and Staff. It was not signed by any other party and is therefore a non-unanimous stipulation. Commission rule 4 CSR 240-2.115(1) provides that if no party requests a hearing regarding a non-unanimous stipulation

and agreement, the Commission may treat the stipulation and agreement as a unanimous stipulation and agreement. 4 CSR 240-2.115(3) provides that each party shall have seven days from the filing of the non-unanimous stipulation and agreement to file a request for a hearing. Failure to file a timely request for a hearing shall constitute a full waiver of that party's right to a hearing. No party has requested a hearing regarding the stipulation and agreement between UtiliCorp, Empire and Staff. Therefore, the stipulation and agreement will be treated as a unanimous stipulation and agreement.

The stipulation and agreement indicates that Staff, UtiliCorp and Empire have negotiated agreements on certain matters that were identified as issues in the List of Issues and Statements of Positions filed prior to the hearing in this case. Staff, UtiliCorp and Empire have reached agreement regarding the following issues:

**Pension Funds Condition:**

UtiliCorp, Empire and Staff agree that in post-merger cases involving UtiliCorp's Empire operating division, UtiliCorp will maintain the pre-merger funded status of the Empire pension fund by accounting for it separately. UtiliCorp will, however, be allowed to combine the assets. The accounting on a going-forward basis will start with a market value of asset evaluation performed by Empire's actuarial firm at the time of merger closing. On a going-forward basis the net rate of return (actual earned return income earned on the assets during the year less benefits paid) on UtiliCorp's combined pension assets will be used to increase (decrease) the market value of pre-merger funded status for the Empire operating division.

**Income Taxes Condition:**

UtiliCorp, Empire and Staff agree that if the merger is determined to be a taxable event and deferred taxes of Empire are thereby lost, UtiliCorp will be required to include an amount equal to those deferred

taxes in existence at merger closing in future Empire rate proceedings as an offset to rate base.

**Surveillance Condition:**

UtiliCorp, Empire and Staff agree that UtiliCorp will be required to continue to submit to the Commission's Financial Analysis Department, on a monthly basis, separate surveillance reports for UtiliCorp, on a total company basis; UtiliCorp's Missouri Public Service (MPS) operating division, on a stand-alone basis; and UtiliCorp's Empire operating division, on a stand-alone basis, following the closing of the merger.

**Fuel Energy Cost Information Condition:**

UtiliCorp, Empire and Staff agree that after the closing of the merger, UtiliCorp will be required to provide Staff with historical actual hourly generation, energy purchases and sales data, and other information required by Commission Rule 4 CSR 240-20.080 in electronic format accessible by a spreadsheet program for MPS and Empire. UtiliCorp will also provide access to such additional documents as may be necessary for the Staff to analyze fuel and energy costs.

**Tariff Conditions:**

UtiliCorp, Empire and Staff agree that after the closing of the merger, UtiliCorp will be required to file with the Commission an adoption notice in Empire's electric and water tariffs as follows:

**ADOPTION NOTICE**

> Effective [month, day, year], The Empire District Electric Company (EDE), a Kansas corporation, has merged with and into UtiliCorp United Inc. (UtiliCorp), a Delaware corporation, as authorized by the Missouri Public Service Commission in Case No. EM-2000-369. UtiliCorp is the surviving entity.
> Pursuant to the Commission's Report and Order issued [month, day, year], in said case, UtiliCorp hereby adopts, ratifies and makes its own in every respect, as if the same had been originally filed by it, all tariffs, schedules and rules and regulations of EDE filed with and approved by the Commission before [month, day, year].

UtiliCorp will operate in the area formerly served by EDE using the name "[insert name here]."

The Commission has the legal authority to accept a stipulation and agreement as offered by the parties as a resolution of certain issues raised by the Staff in this case, pursuant to Section 536.060, RSMo Supp. 1999. After considering the matter, the Commission concludes that the stipulation and agreement filed by the Staff, UtiliCorp and Empire should be approved.

## FINDINGS OF FACT

The Missouri Public Service Commission has considered all of the competent and substantial evidence upon the whole record in order to make the following findings of fact. The Commission has also considered the positions and arguments of all the parties in making these findings. Failure to specifically address a particular item offered into evidence or a position or argument made by a party does not indicate that the Commission has not considered it. Rather the omitted material was not dispositive of the issues before the Commission.

UtiliCorp is a Delaware corporation with its principal office and place of business located in Kansas City, Missouri. UtiliCorp is authorized to conduct business in Missouri through its MPS operating division and, as such, is engaged in providing electrical and natural gas utility service in Missouri to customers in its service areas. UtiliCorp has regulated energy operations in seven other states. UtiliCorp also operates in New Zealand, Australia and Canada.

Empire is a Kansas corporation with its principal office and place of business located in Joplin, Missouri. Empire is engaged in the business of providing electrical and water utility services in Missouri to customers in its service areas.

## A. Approval of Merger:

UtiliCorp and Empire argued that their proposed merger would not be detrimental to the public and would, in fact, be beneficial for the ratepayers of both companies. Myron McKinney, President and Chief Executive Officer of Empire, explained the benefits of the merger as follows:

> We believe that the merger will provide opportunities for our customers, employees, and shareholders to achieve benefits that would not be available if Empire were to remain an independent company and that the merger will result in a combined company that will be well positioned to succeed in the increasingly competitive energy marketplace. Specifically, the combined enterprise can more effectively participate in the increasingly competitive market for the generation of power. Through the elimination of duplicate activities there will be reductions in operating and maintenance expenses. The inherent increase in scale and market diversification will provide increased financial stability and strength, which could not be achieved without the combination of the companies.
> M. McKinney Direct, Ex. 1, at p. 4

The merger of Empire with UtiliCorp will permit Empire's customers to be served by a substantially larger utility better able to compete in the wholesale energy market.

**Costs of Merger Exceed Benefits:**

Several parties argued that the proposed merger would be detrimental to the ratepayers of both Empire and UtiliCorp and for that reason it should not be approved by the Commission. In particular, Staff, joined by other parties, contended that the costs associated with the merger would exceed the savings attributable to the merger.

Staff bases its arguments about increased cost of service on various adjustments it has made to the estimates of merger savings set forth by UtiliCorp and Empire. Staff challenges the estimates of merger savings in three areas. First, Staff argues that most of the savings in the area of projected energy cost savings from the joint dispatch of the

power supply of the merging companies that UtiliCorp and Empire claim as a benefit of the merger could, in fact, be achieved by Empire as a stand-alone company even if there is no merger. Second, Staff argues that UtiliCorp's and Empire's assumption about the inflation rate for UtiliCorp's overhead costs results in a significant overstatement of the possible savings to be expected from the merger. Third, Staff alleges that labor reductions claimed as merger savings by UtiliCorp might also occur without a merger.

Staff's arguments are not convincing for several reasons. First, with regard to the projected savings from joint dispatch, Staff overestimates the extent to which Empire, as a stand-alone company, could take advantage of increased sales opportunities in the wholesale generation market. UtiliCorp's and Empire's savings assumptions are based on the premise that, absent a merger, UtiliCorp and Empire would continue to generate approximately the same level of normalized wholesale volumes and margins over the ten-year study period as those generated in recent years. UtiliCorp and Empire assumed that after the merger the combined company would make all wholesale market sales at market rates and that the combined company would be able to increase its wholesale market penetration. Under this scenario the merger would result in both an increase in the volume of wholesale sales and an increase in profitability due to use of market-based rates.

Staff's argument assumes that Empire, even without the merger, could make the same power sales on the wholesale market. Thus, according to Staff, the increased profit from those potential sales should not be attributed to the merger. Staff's assumption appears to overstate Empire's ability to compete in the wholesale market. Empire has not been and is not now active in the wholesale market. Empire does not currently have a wholesale marketing group dedicated to pursuing the wholesale market and

does not have plans to create such a group. Even if it wished to develop such a marketing group, Empire's size and limited resource mix could make it costly to develop and sustain an effective wholesale marketing group. Furthermore, Empire elected not to separate its transmission and generation functions due to cost. Thus, it does not have FERC approval to sell energy at market-based rates and must sell its excess energy at cost-based rates. UtiliCorp's MPS division, on the other hand, has been an effective player in the wholesale market since 1996. It has separated its generation and transmission functions and can sell energy at market-based rates. MPS maintains a fully staffed wholesale marketing group to pursue opportunities in the wholesale market.

It is not reasonable to assume that Empire could effectively and efficiently create the marketing knowledge and resources needed to operate in the wholesale market and obtain the same results as those that could be obtained after a merger with UtiliCorp. The evidence does not indicate precisely how much merger savings could be obtained through increased activity in the wholesale market, but it is reasonable to conclude that there could be savings.

Second, Staff's argument about the inflation rate for UtiliCorp's overhead costs is also unpersuasive. In calculating the expected cost of future UtiliCorp corporate allocations that are to be charged to the Empire operating division after the merger, UtiliCorp assumed that the corporate allocations would increase each year by an inflation rate of two-and-a-half percent. Staff argued that an inflation factor of five percent was more appropriate given the much larger annual increases in corporate overhead costs allocated by UtiliCorp to its MPS operating division in previous years. If an inflation factor of five percent is used, then the level of estimated savings resulting from the merger will be reduced.

UtiliCorp responded by pointing out that Staff's review of corporate overhead costs was overstated by Staff's failure to take into account that the large annual increases in corporate allocations to MPS experienced in previous years could be attributed to the increased operational cost of reengineering initiatives that were implemented in 1997, 1998 and 1999 over the entire UtiliCorp system.

The Commission does not need to determine an appropriate inflation factor for corporate allocations in order to decide this case. In any future rate case, the cost of UtiliCorp's corporate allocations will be a known factor. If, in that future rate case, those allocations are shown to be excessive, then the Commission will be able to consider that fact when setting the rates for UtiliCorp's Empire operating division. Higher rates for Empire's customers cannot result from this merger unless the Commission approves those rates in a future rate case.

Third, the same considerations apply to Staff's argument about possible labor reductions in the absence of a merger as well as to all of Staff's arguments about possible increased costs of service resulting from the merger. As Staff repeatedly testified, it is very difficult to speculate about what Empire's cost of service might be in five or ten years. Staff used that fact to argue that merger savings could not be reliably established at this time. However, the same difficulty applies to Staff's argument about the costs of the merger exceeding the benefits. If UtiliCorp's and Empire's representations of merger savings are speculative, then Staff's representations of excessive merger costs could also be characterized as speculative. Such speculations are not a valid reason for refusing to allow UtiliCorp and Empire to complete the proposed merger.

**Increased Financial Risk for Empire Ratepayers:**

Public Counsel points out that Empire's long-term debt bears a credit rating of A-. On the other hand, UtiliCorp's long-term debt bears a

credit rating of BBB. After the merger the credit rating of the combined UtiliCorp/Empire will likely be the BBB rating of UtiliCorp. Public Counsel argues that the downgraded credit rating will increase the cost of debt for Empire's ratepayers above the cost of debt for Empire absent the merger. Public Counsel argues that this will lead to higher rates for Empire's ratepayers and constitutes a detriment that should lead to the rejection of the merger.

Public Counsel's argument is not persuasive. First, UtiliCorp's credit rating of BBB, while lower than Empire's current rating, is still considered to be investment grade. There is no evidence to support an assertion that UtiliCorp is financially unstable or that the merger with UtiliCorp will put Empire's ratepayers at any great risk. Second, no evidence was presented that would quantify the amount by which the cost of debt attributable to Empire would increase because of the merger. Indeed, there is no way to reliably quantify such an amount. Certainly there is no guarantee that Empire's credit rating would remain at A- if the merger does not proceed. Third, the cost of debt is just one factor the Commission will consider when setting future rates for UtiliCorp's Empire unit. If the company's cost of debt is unreasonable, appropriate adjustments can be made to protect the ratepayers. Finally, even if it is assumed that the merger will result in an increased cost of debt for Empire's ratepayers, that fact alone does not require the Commission to reject the merger. The risk of an increased cost of debt is just one more factor for the Commission to weigh when deciding whether or not to approve the merger.

After considering all the evidence and the arguments of the parties, the Commission concludes that the merger between UtiliCorp and Empire will not be detrimental to the public and should be approved. In addition to approving the merger itself, UtiliCorp and Empire ask that the

Commission approve what they refer to as a Regulatory Plan. The Commission will not do so for reasons fully explained in its Conclusions of Law.

### B. Proposed Conditions on Approval:

Several parties identified what they believe to be particular problems with the merger as proposed. They ask that various conditions be imposed upon the Commission's approval of the merger so that the alleged problems will not create a detriment to ratepayers. Those various conditions will be addressed in turn.

**Stranded Costs Condition:**

Staff defines stranded costs as those costs presently charged by electric utilities in rates that may not be recoverable when and if electric utilities must set their prices based upon a competitive market. Obviously such a competitive market and resulting stranded costs will not occur unless the Missouri legislature or the United States Congress acts to deregulate the electric industry. Staff does not believe that Empire is currently facing possible stranded costs because it appears that its electric generating assets are worth more in an unregulated marketplace than under continued regulation. However, Staff is concerned that:

> if electric restructuring occurs, it is possible that the Joint Applicants in the future may argue that any failure to recover UtiliCorp's valuation of Empire's assets (i.e., the portion of the acquisition adjustment allocable to generation operations) would constitute a 'stranded cost'. Oligschlaeger Rebuttal, Ex. 712, at 68-69.

Staff asserts that this possibility constitutes a detriment to the customers of Empire and asks that the Commission require that UtiliCorp and Empire commit not to seek recovery of such stranded costs in any future Missouri regulatory proceeding. Staff further recommends that that UtiliCorp and Empire be required to commit not to seek or endorse

legislation in Missouri that would mandate the recovery of all or a portion of the acquisition adjustment as part of claimed stranded costs.

The Commission will not impose the condition requested by Staff. If UtiliCorp ever attempts to recover stranded costs for its Empire unit, it will presumably have to do so before the Commission. If it asks for an inappropriate recovery, the Commission will deal with such a request at the time that it is made. Therefore, there is no need to impose a condition that would limit, in advance, UtiliCorp's ability to make an argument before the Commission.

Staff indicates that UtiliCorp may attempt an end-run around the Commission by seeking relief before the legislature. Thus, the second part of Staff's condition would have the Commission attempt to limit UtiliCorp's right to lobby the legislature to enact legislation regarding stranded costs. Staff does not indicate where the Commission would find the authority to forbid a utility from communicating with the legislature. The Commission will not impose the condition requested by Staff.

**Access to Books and Records Condition:**

Public Counsel argues that the proposed merger will result in increased size, scope and complexity of transactions between UtiliCorp and its affiliates. Public Counsel recommends that, as a condition to its approval of the merger, the Commission require UtiliCorp to agree to provide Public Counsel and Staff access to the books, records, employees and officers of all corporate entities for which UtiliCorp or its wholly owned subsidiaries have an ownership interest of ten percent or more. UtiliCorp replies that the access sought by Public Counsel is already mandated by Commission rule and that it is not necessary to require it to pledge to comply with a rule that it is already legally obligated to obey.

The Commission has promulgated extensive rules to govern transactions between utilities and their affiliates. For electric utilities the affiliate transaction rule is found at 4 CSR 240-20.015. That rule addresses the concerns raised by Public Counsel. So long as the affiliate transaction rule is in effect there is no reason to extract a promise from UtiliCorp that it will comply with the regulation. Its compliance is already expected and required. The requested condition regarding access to books and records will not be imposed.

**Affiliate Transaction Condition:**

Public Counsel proposed that, as a condition to its approval of the merger, the Commission require UtiliCorp to agree to comply with the Commission's affiliate transaction rule. In its initial brief, Public Counsel asks that the Commission state in any order approving the merger that the Commission will "commit to close scrutiny of the merged entity with regard to compliance with the terms of the Commission's affiliate transaction rules." (Initial Brief of the Office of the Public Counsel at p. 48)[2] UtiliCorp replies that it will, of course, comply with all the Commission's regulations.

As previously indicated with regard to the books and records condition, there is no reason to extract a promise from UtiliCorp that it will comply with the regulations of the Commission. The Commission will continue to scrutinize UtiliCorp for compliance with the affiliate

[2] Public Counsel's initial brief also recommends that the Commission require as a condition of the merger that UtiliCorp never propose to charge the Empire division customers for access to the Empire fiber optic system, because Empire's non-regulated operations have never provided any compensation whatsoever to the regulated operations for the use of its right of way, poles, ducts and underground conduit. This recommendation was never identified as an issue by the parties and no evidence was presented regarding such a condition other than a brief, conclusory statement in the rebuttal testimony of Ryan Kind, Exhibit 201, p. 7. In any event, the requested condition is unnecessary because the Commission will exercise its authority to review any future request by UtiliCorp to revise its charges to its customers. The condition requested by Public Counsel will not be imposed.

transaction rules, as it does all other utilities in this state that are required to comply with those rules. The Commission will not impose the requested affiliate transaction condition.

**Customer Service Indicators Condition**:

Staff is concerned that the pressures and dislocations associated with the merger might lead to a decrease in the quality of service that UtiliCorp would provide to the former customers of Empire. In order to protect Empire's customers, Staff proposed that UtiliCorp be required to adopt several changes to its customer service program. Specifically, Staff asked the Commission to require UtiliCorp to:

1. Continue to track and monitor the level of customer complaints separately for the MPS and Empire divisions after the merger;

2. Continue Empire's support program designed for its elderly and handicapped customers entitled Empire's Action to Support the Elderly (EASE);

3. Continue Empire's policy of permitting flexible payment due dates for Empire customers who sign up for the average payment plan;

4. Continue to perform formalized customer satisfaction surveys;

5. Provide actual monthly performance indicators to Staff on a calendar year quarterly basis following the effective date of the merger. Such reports to Staff would include data regarding Call Center Abandoned Call Rate (ACR), Call Center Average Speed of Answer (ASA), Distribution Reliability Customer Average Interruption Duration (CAIDI), Distribution Reliability System Average Interruption Frequency Index (SAIFI), and Distribution

Reliability System Average Interruption Duration Index (SAIDI). Staff also recommends that UtiliCorp be required to provide information regarding staffing level at Customer Call Centers and that UtiliCorp be required to spend reasonable and appropriate amounts within the next year to improve customer service relating to any performance indicator that did not meet expectations;

6. Establish specified objectives that UtiliCorp would be required to meet for its ACR and ASA indicators; and

7. Maintain the SAIFI, SAIDI and CAIDI reliability measures separately for the MPS and Empire divisions.

UtiliCorp replies to Staff's proposed requirements by pointing out that UtiliCorp has provided quality service in Missouri for more than 80 years. UtiliCorp argues that there is no reason to believe that it will not continue to provide quality service after the merger and that it would be unfair to require it to comply with remedial measures and reporting requirements that are not required of every other utility in Missouri.

UtiliCorp has a history of providing quality service to its Missouri customers. The evidence presented by Staff indicated that the service provided by UtiliCorp to the customers of its MPS division differed somewhat from that provided by Empire to its customers. The Commission finds that the customer service currently provided by MPS is not substantially inferior to that provided by Empire. Therefore, the Commission will not impose extensive special customer service conditions that are not applicable to the other utilities in this state.

Certainly the Commission expects that its Staff will continue to monitor the level of customer service provided by UtiliCorp in both its MPS and Empire divisions. If Staff notes problems with the level of service provided by UtiliCorp, it has the responsibility to bring those problems to

the attention of the Commission through all appropriate means. However, with one exception, the Commission will not impose the conditions on the merger requested by Staff.

The only customer service condition that the Commission will impose is a requirement that UtiliCorp provide Staff with monthly reports for one year following the merger.[3] It is certainly possible that the merger process could cause disruptions in the level of service that both UtiliCorp and Staff expect to be provided to UtiliCorp's customers. While Staff could obtain the information it needs to monitor customer service levels by performing repeated audits on UtiliCorp, the regular reporting of information by UtiliCorp is the most efficient and effective method by which Staff can fulfill its responsibility to monitor the quality of service UtiliCorp is providing to its customers.

**Market Power Conditions:**

Several parties expressed concerns about whether the merger would result in UtiliCorp acquiring greater horizontal or vertical retail market power. Before this issue can be discussed, it is important to understand the meanings of the terms, horizontal and vertical market power. The testimony of Ryan Kind, Public Counsel's witness, presents definitions of these terms developed by this Commission's Education Working Group to the Task Force on Retail Electric Competition, established in Case No. EW-97-245. Those definitions are as follows:

> Market Power is the ability of a firm, alone or in concert with other firms to profitably maintain the price of a product above the competitive market level for an extended period of time. Suppliers with vertical or horizontal market power could charge unfair prices and realize excessive profits.

[3] Staff asks for monthly data to be provided in quarterly reports. However, the Commission imposed a monthly reporting requirement on UtiliCorp in the merger between UtiliCorp and St. Joseph Light & Power Company, Case No. EM-2000-292. The Commission will impose the same requirement in this case.

> *Vertical* market power involves the ability of a firm to control an essential element in the vertical production chain and, through that control, cause competitors to be at a disadvantage through either restricted access or higher costs for the products or services required to produce and deliver the specific product.
> *Horizontal* market power exists when a single firm or small group of firms have the ability to affect the price of a product. In the case of a single firm, horizontal market power is present when a firm dominates a market where entry barriers protect it from competition. In the case of a small group of firms, horizontal market power can occur through explicit collusive behavior or through strategies that jointly maximize the self-interest of each of the firms.

Kind Rebuttal, Ex. 201, p. 62-63

Staff, Public Counsel and Springfield argue that the merger will permit UtiliCorp to exercise greater vertical and horizontal retail[4] market power to the possible future detriment of the public.[5] In order to deal with these possible detriments, various parties asked the Commission to impose various conditions on its approval of the merger.

1. Staff proposed that UtiliCorp and Empire be required to join the same regional transmission entity that meets the eleven ISO principles enumerated in FERC Order No. 888 before the October 15, 2000 deadline imposed by FERC Order No. 2000. UtiliCorp replied that it would meet the FERC deadline for joining a regional transmission entity and indicated that it did not believe that it should be required to announce its intentions any sooner than any other utility. It is unclear as to whether Staff meant that UtiliCorp and Empire should join the same regional transmission entity before the deadline or simply that it should be required to comply with the deadline. However, the October 15, 2000 deadline is now past and this

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[4] The merger may also affect wholesale market power. However, wholesale market power is an area that is subject to regulation by FERC and will not be addressed in this Report and Order.

[5] Retail market power could become a detriment only if retail electric competition is authorized in Missouri. Currently, Empire and UtiliCorp are subject to cost-based regulation and that status will continue after the merger.

proposed condition is moot. The Commission finds that conditioning the approval of the merger upon joining the same regional transmission entity is not necessary. Therefore, the Commission will not impose the requested condition.

2. Staff is concerned that harmful horizontal market power could develop in load pockets following the advent of retail electric competition. Load pockets are geographic areas within the service territories where the transmission system will not allow competitive generation to provide services to a significant percentage of end-use customer loads on a year-round basis. Staff proposed that UtiliCorp should be required to agree to submit a study showing what percentage of load can be served from competitive generation sources throughout their merged service territory. Staff would require UtiliCorp to prepare and present this study at the time that retail competition is approved in Missouri. UtiliCorp replied that it would be willing to perform such a study if ordered to do so at the time that retail electric competition is instituted but that it should not be ordered to perform such a study at this time.

Staff and other parties request that the Commission order UtiliCorp to perform market power studies at some future time when retail electric competition may become a reality in Missouri. However, no one can possibly know when, or if, that competition will arrive. Neither can anyone predict what form that competition may take. None of the parties have provided a satisfactory explanation of why the Commission should order the completion of these studies now, in this Report and Order, rather than waiting until the circumstances of retail electric competition become more clear. Under these circumstances the Commission will not impose the condition sought by Staff. If, at the time that retail electric competition becomes a reality, the Commission finds that a market power study is needed, the Commission will exercise its authority to order the completion of any needed studies.

3. Public Counsel suggests that UtiliCorp should be compelled to agree to the same market power conditions that were approved by the Commission in the KCPL/Western Resources merger case, Case No. EM-97-515. Those conditions would require UtiliCorp to do the following:

a. Agree to perform a horizontal market power study that meets specified conditions. The market power study would be performed at the time that retail electric competition is commenced in Missouri;

b. Address vertical market power concerns by agreeing to become a member of a Regional Transmission Organization;

c. Agree to various restrictions on its retail market power including restrictions on the use of the name of Empire for marketing of unregulated products and services provided by UtiliCorp or its affiliates; and

d. Agree that it will not propose or otherwise support legislation in Missouri designed to prohibit or substantially limit the Commission from addressing market power issues.

UtiliCorp replies that the KCPL/Western Resources merger was a different case with different circumstances and there is no reason to impose those conditions upon UtiliCorp in this merger case.

The KCPL/Western Resources merger was different from this merger in that it was resolved through the filing of a stipulation and agreement. That means that the merging parties agreed to the imposition of those conditions. The lack of agreement in this case most clearly impacts the proposed condition that would limit UtiliCorp's right to propose or support legislation. While a party can certainly agree not to propose or support certain legislation, the Commission has no authority to order a utility to refrain from exercising its right to petition the legislature and the Commission will not attempt to do so.

With regard to the other proposed conditions, the Commission has previously indicated that it will not now order the performance of market power studies. UtiliCorp is already obligated to become a member of an RTO by FERC order 2000. Finally, any necessary restrictions on UtiliCorp's retail market power may be imposed at such time as it is no longer subject to cost-based regulation. Public Counsel's proposed conditions will not be imposed upon UtiliCorp.

4. Springfield argued that the merger of Empire and UtiliCorp would create a detriment to the public in that it would give the resulting entity the opportunity, ability and incentive to utilize scarce electrical transmission resources for its own use, leaving other utilities no economic alternatives for delivery of needed power supplies. Springfield suggests several conditions that should be imposed to avoid these detriments. Those conditions are closely related to Springfield's concerns about transmission access and reliability and will be discussed along with those issues in the Conclusions of Law.

**Load Research Condition**:

Staff raised an issue regarding the Load Research programs maintained by UtiliCorp and Empire. Load Research refers to a program designed to provide hourly electric load data for use in calculating hourly class loads. A load research program helps the utility understand how its customers use energy. The cost of generating electricity varies by the hour or even shorter intervals. However, electrical use for most customers is measured by the month because monthly data is used for billing. A load research program permits the utility to more closely measure how certain classes of customers actually use electricity during the month and during the day so that appropriate rates can be established.

Staff is pleased with Empire's current load research program and is less pleased with UtiliCorp's current load research program for its MPS

division. Staff would like to see MPS's program brought up to the level of Empire's program and to that end has proposed that UtiliCorp be required to agree to:

1. Continue to treat the Empire service territory separately from the MPS service territory for load research purposes;

2. Maintain Empire's load research program at its current standard of timeliness and quality;

3. Provide hourly class load data, selected individual customer hourly load research data for the Empire service territory and the checks and balances performed on that data to the Staff on an on-going basis;

4. Improve MPS' current load research program to match the current Empire standard of timeliness and quality; and

5. Provide hourly class load data, selected individual customer hourly load research data and checks and balances performed on that data for the MPS service territory to the Staff on an on-going basis.

UtiliCorp replied that it does intend to treat MPS and Empire separately for load research purposes for as long as they have separate rate structures. UtiliCorp indicates that it is taking steps to improve the load research program for MPS. However, UtiliCorp disagrees with Staff's other proposed conditions regarding its load research program. UtiliCorp argues that it would be unfair to hold its load research program to a higher standard than is applied to other similar utilities. UtiliCorp suggests that if Staff believes that higher standards are needed it should determine those standards through consultation with the industry as a whole. UtiliCorp also argues that it should not be required to periodically report its research data to Staff because such a requirement would be unnecessarily costly.

The Commission expects that UtiliCorp will continue to provide high quality load research for both its Empire and MPS divisions. While

Staff indicates that Empire's load research program is superior to that of UtiliCorp, it did not present any evidence to indicate that UtiliCorp's current program, or the program it plans to use after the merger, fails to comply with any statute, regulation or industry standard. The Commission will not attempt to micromanage UtiliCorp's business by ordering that it hire a certain number of workers for its load research program. Neither will it attempt to establish any firm standards for UtiliCorp to meet. If Staff believes that such standards are necessary, it should use the rulemaking process to establish those standards for all similarly situated utilities. UtiliCorp will not be singled out for special scrutiny. For these reasons, the Load Research Conditions suggested by Staff will not be imposed upon UtiliCorp.

**Energy Conditions:**

The Missouri Department of Natural Resources alleged that the merger between UtiliCorp and Empire would have a detrimental impact on the low-income customers of UtiliCorp and Empire. It also alleged that the merger would have a detrimental impact on energy efficiency and the use of renewable energy resources. MDNR proposed that the Commission impose numerous conditions upon the merger in order to alleviate these alleged harms. MDNR proposed that UtiliCorp be required to:

1. Enter into a partnership with MDNR and other interested parties to market and leverage funds for the development of energy efficiency programs;

2. Develop or retain low-income service packages to meet customer needs, reduce energy costs and provide a return to UtiliCorp;

3. Join with MDNR and a broad range of stakeholders to assess the state's renewable and alternative resources and develop demonstration projects, review and implement policy and market options and put the questions to customers in a deliberative poll;

4. Target outreach to customers that are income eligible and encourage them to take advantage of the opportunity to reduce energy consumption and to improve home affordability;

5. Amend the cooperative agreement between UtiliCorp and Kansas City, Missouri, to permit averaging unit cost within the agreement to maximize the opportunity to assist customers;

6. Eliminate tying the dollar amount to specific measures to maximize the energy conservation measures installed in each home and permit any energy efficient measure that is deemed cost-effective as a result of computer analysis, as stated in the agreement between UtiliCorp and Kansas City, Missouri;

7. Permit energy-efficiency assistance to all eligible households and allow funds to be spent on non-electric appliances;

8. Implement a 25-site Benefit Outreach and Screening Software (BOSS) pilot project, and expand the program, as appropriate, if found to successfully deliver benefits to low-income customers;

9. Implement a base load and space heating electric energy efficiency program directed toward high use payment-troubled, low-income customers;

10. Implement a pilot solar energy program directed toward high use low-income customers;

11. Implement a periodic survey process through which the merged company will take pro-active efforts to identify which of its payment-troubled customers represent low-income households;

12. Implement an Outcome-based Performance Reporting System (OPRS) through which the customer service outcomes to low-income customers can be systematically tracked over time.

UtiliCorp replied that it opposed making acceptance of any of MDNR's proposals a condition upon approval of the merger. UtiliCorp

indicated that it is willing to discuss with MDNR and other parties options for additional or different types of programs related to energy and low-income weatherization or assistance as long as discussions also involve methods of recovery of increased costs for these programs. UtiliCorp indicated that it intends to continue to participate in low-income and energy efficiency programs and supports a number of them currently through funding and other measures.

MDNR argues that the Commission must impose the conditions it has listed in order to avoid possible detriment to UtiliCorp's low-income customers. MDNR suggests that the Commission must ensure that the benefits of the merger are appropriately 'passed-on' to UtiliCorp's low-income customers. MDNR argues that the low-income customers currently served by Empire and UtiliCorp are a separate market that will be harmed because the benefits of the merger will not be distributed fairly to all customers.

MDNR's framework for analyzing this merger is based on that used by federal courts in evaluating mergers under federal anti-trust laws. Obviously, this is not an anti-trust case and this Commission is not obligated to follow federal precedent established for the application of anti-trust laws. Nevertheless, the Commission agrees that it should consider the possible impact of the merger on all the customers of Empire and UtiliCorp when making its determination of whether or not the proposed merger is detrimental to the public. However, it is not clear that low-income customers can properly be considered as a separate class when considering the impact of the merger.

Low-income customers have not previously been accorded status as a separate class of consumer when utility rates are designed. Standard rate design treatment attempts to match revenue requirement determination with cost causation by class. In other words, the class of consumers that

causes a cost to a utility should be required to pay those costs through rates. The evidence presented by MDNR suggests that low-income consumers have special problems that UtiliCorp should address through additional programs. Those programs, of course, bear a cost. Thus, if the Commission were to require UtiliCorp to institute new programs to better serve its low-income consumers, without subsidization from other classes of consumers, it might be necessary to increase the rates charged to the class of low-income consumers in order to pay for those programs. Obviously, such a result would not be practical or desirable from the standpoint of the low-income consumers. But neither would it be fair and reasonable for the Commission to order UtiliCorp to institute such programs without giving it an opportunity to recover the cost of those programs through rates. As previously indicated, this case is not about establishing rates. It also is not about adjusting UtiliCorp's class cost of service.

MDNR suggests that such programs could be paid for through the passing on of the synergy benefits of the merger to the consumers. However, absent a rate or complaint case, UtiliCorp is under no obligation to pass any merger savings on to consumers. MDNR's proposed conditions will not be imposed upon UtiliCorp.

MDNR also argues that the Commission should impose conditions on the merger to require UtiliCorp to institute additional energy efficiency and renewable energy programs. It suggests that the flow of money out of Missouri to pay for non-renewable sources of energy is a detriment to the public and suggests that UtiliCorp be required to make a commitment to renewable energy sources. While energy efficiency and the increased use of renewable energy may be a laudable goal, MDNR has not made a showing that would link energy efficiency and renewable energy to this merger. The fact that UtiliCorp is seeking to merge with Empire will not increase the reliance of the resulting company on non-renewable energy, nor will it

affect the efficiency of use of energy by the customers of the companies. There is no evidence that this merger will cause any detriment with regard to energy efficiency and the use of renewable energy sources. MDNR's proposed conditions will not be imposed upon UtiliCorp.

**Labor Protective Provisions Condition:**

The IBEW raises concerns about the impact of the proposed merger on the benefits and terms of employment of its members employed by Empire. The IBEW also argues that the possible elimination of some of Empire's bargaining unit employees by UtiliCorp after the merger would have a detrimental impact on the safety and reliability of the electrical service provided by Empire. The concerns raised by the IBEW will be addressed in turn.

First, the IBEW is concerned that after the merger, UtiliCorp will make changes to the medical insurance and retirement benefits currently received by the bargaining unit employees. In particular, UtiliCorp is expected to require the former employees of Empire to pay a larger percentage of the cost of their medical insurance premiums. The IBEW asks that, as a condition for approval of the merger, the Commission require UtiliCorp to continue to maintain medical insurance coverage for bargaining unit employees with no increase in the percentage of employee contributions that is currently required. The IBEW also asks that the Commission require that UtiliCorp not terminate or adversely change the retirement plan, retirement funding or retirement benefits affecting bargaining unit members.

UtiliCorp employees currently pay a greater percentage of the cost of their health insurance than do employees of Empire. UtiliCorp indicates that following the merger it intends to put into effect for Empire employees the same overall healthcare package that exists now for UtiliCorp employees, meaning that the Empire employees will pay more for their health

insurance coverage. Thus, the IBEW argues that its proposed condition preventing an increase in the cost of health insurance should be imposed because otherwise the merger will be detrimental to the bargaining unit employees. There was no persuasive evidence or argument to demonstrate that increasing the cost of health insurance for the bargaining unit employees would be detrimental to the public at large.

The IBEW's argument is not persuasive. The terms of employment under which the IBEW's union members will work for Empire or UtiliCorp are subject to negotiation between employer and employee. Such terms are currently embodied in a collective bargaining agreement between Empire and IBEW. UtiliCorp has indicated that it intends to assume that collective bargaining agreement after the merger. Aside from any possible preclusive effect of the National Labor Relations Act, it is clear that under state law the PSC is an agency of limited jurisdiction and has only such powers as are conferred upon it by statute. *Inter-City Beverage Co., Inc. v. Kansas City Power & Light*, 889 S.W.2d 875, 877, (Mo. App. W.D. 1994). There is no provision in Missouri's statutes that would justify the Commission's intervention in a collective bargaining agreement in a merger case. Indeed, in Section 386.315.1, RSMo 1994, there is a specific legislative prohibition against such interference with a collective bargaining agreement in the context of establishing the rates to be charged by a utility. Clearly, the Commission has no authority to step into the negotiations between UtiliCorp and the IBEW to impose a particular term favorable either to the employees or to the employer.

The IBEW's second concern regards the safety and reliability of the electrical service that will be provided by UtiliCorp in the area currently served by Empire. UtiliCorp has indicated its intent to eliminate some fifty bargaining unit positions. Some of the positions to be eliminated may include linemen and electricians responsible for

maintaining and repairing the electrical service lines in the Empire service territory.[6]

IBEW states that the elimination of these fifty bargaining unit positions may compromise the safety and reliability of the electrical service delivered by UtiliCorp after the merger. It is possible that the safety of the employees could be endangered if too few linemen are available to do the work currently performed by Empire's linemen. Similarly, the reliability of the transmission system could be adversely affected if there are too few workers available to make needed repairs to the electric lines. This could be a particular problem in a widespread outage, such as could result from a major ice storm. In such a situation, UtiliCorp conceded that a reduced crew of linemen would not be able to restore power as quickly. It is also troubling that UtiliCorp has not conducted any specific studies to determine the impact that substantially reducing the number of bargaining unit employees would have on the safe and reliable delivery of service in the Empire service area.

The IBEW suggests that the Commission should deal with its concerns by mandating, as a condition on its approval of the merger, that UtiliCorp not eliminate any bargaining unit positions as a result of the merger. The assertion by IBEW that elimination of bargaining unit positions would have a negative effect on safety or reliability is not supported by sufficient evidence to cause the Commission to conclude that IBEW's proposed condition is warranted. The Commission will not impose such a condition.

Section 386.310, RSMo 1994, gives the Commission the power to require every public utility to maintain and operate its system in such

[6] The positions that UtiliCorp is considering eliminating may be found in UtiliCorp's Response to Data Request No. IBEW-6, which is attached as an appendix to the cross-surrebuttal testimony of Bill Courtney, Exhibit No. 100.

a manner as to "promote and safeguard the health and safety of its employees, customers, and the public." The Commission is always concerned about the safe and reliable delivery of electrical service. In order to ensure that the health and safety of UtiliCorp's employees, customers and the public are protected after the merger, the Commission will establish, by a separate order, a case to investigate these safety issues.

**Public Counsel's Regulatory Plan Condition:**

Public Counsel proposes that the Commission adopt an alternative to the regulatory plan proposed by UtiliCorp. Public Counsel suggests that UtiliCorp should be required to file a rate case for each of its Missouri operating divisions within one year of the approval of both the merger between UtiliCorp and St. Joseph Light & Power and the merger between UtiliCorp and Empire. UtiliCorp opposed this condition.

Public Counsel's proposed condition is unnecessary. UtiliCorp can decide for itself when it wishes to propose rate adjustments for its Missouri operations. If Public Counsel believes that UtiliCorp is over-earning, it is free to bring an appropriate complaint. The Commission will not upset that balance by arbitrarily ordering UtiliCorp to institute a rate case at a particular time.

## CONCLUSIONS OF LAW

The Missouri Public Service Commission has reached the following conclusions of law:

## A. Requirements for Approval of the Merger:

UtiliCorp and Empire have asked the Commission to approve their merger pursuant to the provisions of Section 393.190.1, RSMo 1994.[7] In interpreting the requirements of this statute, the Commission and the courts that have reviewed its decisions, have consistently held that a proposed utility merger must be approved if such approval is in the public interest. This does not mean that the public must receive a benefit from the proposed merger. Instead, the Missouri Supreme Court has established a standard that holds that the requirement that the merger be "in the public interest" can mean no more than that the merger is "not detrimental to the public." *State ex rel. City of St. Louis v. Public Service Commission*, 335 Mo. 448, 459, 73 S.W.2d 393, 400 (Mo. banc 1934). Therefore, the Commission is required to approve this merger if it can be shown that the merger is not detrimental to the public.

What then does it mean for the Commission to find that the proposed merger is "not detrimental to the public"? Furthermore, who is the public that is to be protected from detriment? Several parties suggest that the public that the Commission is obligated to protect is the ratepayers and the detriments from which they are to be protected are higher rates or a deterioration in the level of customer service. Certainly the Commission has utilized those definitions in past cases. *See, e.g.*, *Laclede Gas Company*, 16 Mo P.S.C. (N.S.) 328 (1971). There does

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[7] Section 393.190.1, RSMo 1994, provides in relevant part as follows:

> No gas corporation, electrical corporation, water corporation or sewer corporation shall hereafter sell, assign, lease, transfer, mortgage or otherwise dispose of or encumber the whole or any part of its franchise, works or system, necessary or useful in the performance of its duties to the public, nor by any means, direct or indirect, merge or consolidate such works or system, or any franchises, or any part thereof, with any other corporation, person or public utility, without having first secured from the commission an order authorizing it so to do.

not, however, appear to be any controlling authority that would firmly limit the Commission to those definitions. Nevertheless, the Commission will generally adhere to those definitions in this decision.

### B. Burden of Proof:

Who then has the burden of proving that this merger is not detrimental to the public? The Missouri Supreme Court has stated that "the relevant inquiry in determining which party has the burden of proof is to identify who, as is disclosed from the pleadings, asserts the affirmative of an issue. Generally that party has the burden of proof." *Anchor Centre Partners, Ltd. v. Mercantile Bank, N.A.*, 803 S.W.2d 23, 30 (Mo. banc 1991); *see also Dycus v. Cross*, 869 S.W.2d 745 (Mo. banc 1994). The joint applicants, UtiliCorp and Empire, are asserting that their merger will not be detrimental to the public. Therefore, they have the burden of proving that assertion. However, simply assigning the general burden of proof on UtiliCorp and Empire does not resolve all questions about burden of proof.

UtiliCorp and Empire must prove that their proposed merger is not detrimental to the public. However, other parties have asserted that the merger is detrimental in one or more specific areas. It is not enough for a party to assert that a detriment exists and demand that UtiliCorp and Empire prove them wrong.

While the burden of proof never shifts throughout a trial, the burden of going forward with evidence may shift if a prima facie case is made. *Anchor Centre Partners* at 30. Therefore, the parties asserting that the merger is detrimental to the public in a particular way have the burden of going forward by presenting sufficient evidence to support their particular assertions.

## C. The Regulatory Plan:

The details of UtiliCorp's proposed regulatory plan are set forth in paragraph 15 of its joint application and may be summarized as follows:

1. A five year rate moratorium for the Empire retail electric energy distribution unit will be put in place on the effective date of the revised rates resulting from the electric rate case which Empire will file in the second half of 2000 (Pre-Moratorium Rate Case)[8] (Rate Freeze);
2. UtiliCorp asks that several determinations regarding the Pre-Moratorium Rate Case be ordered now in this merger case, including test year, update and true-up periods, in-service criteria for Empire's State Line Combined Cycle plant (SLCC), which is anticipated to be in service on or about June 1, 2001, a list of the categories that would be adjusted in revenues, rate base, and expense, an agreement that the return on equity would be based on Empire as a stand-alone entity, and an agreement that all open positions in existence because of the merger be built into the cost of service. (Predetermination of Rate Case Issues);
3. During the fifth year of the rate moratorium, UtiliCorp will initiate a general rate case for the electric operations of the Empire unit (the Post-Moratorium Rate Case) with the new rates to take effect at the end of the moratorium period. This rate filing will specifically set out an accounting of the synergies realized as a result of merger and the balance of the acquisition premium not covered by said synergies (Post-Moratorium Rate Case);
4. In the context of the Post-Moratorium Rate Case and for ratemaking purposes, fifty percent (50%) of the unamortized balance of the premium will be included in the rate base of the Empire unit's electric operations and the annual amortization of the premium will be included in the expenses allowed for recovery in cost of service (Partial Recovery of Premium in Rates);
5. In the context of the Post-Moratorium Rate Case, and for ratemaking purposes, the return allowed on the premium portion of the rate base will be based on a UtiliCorp capital structure of 60% debt and 40% equity. The return allowed on the balance of the rate base will be based on an Empire unit capital structure as found in the Pre-Moratorium rate case (Frozen Capital Structure); and
6. The allocation of UtiliCorp's corporate and intra-business unit costs to MPS shall exclude for ratemaking purposes the Empire factors from the

[8] The Pre-Moratorium Rate Case was filed on November 3, 2000, and was assigned case number ER-2001-299.

methodology for the period covered by the regulatory plan (MPS Allocations).

UtiliCorp asserts that approval of this regulatory plan is necessary to allow its shareholders the opportunity to recover the $850-900 million investment, including a premium of approximately $280 million, required to acquire the ownership of Empire. Every element of the regulatory plan drew sharp opposition from the other parties.

**The Five-Year Rate Moratorium:**

UtiliCorp proposed that after completion of the merger and the Pre-Moratorium Rate Case, the rates for the Empire division would be frozen for a period of five years. UtiliCorp would be bound to not request a rate increase during those five years barring certain unforeseen catastrophic circumstances that might justify a rate increase. In return, UtiliCorp asks that the Commission order that its rates not be decreased during the same five years. Such a rate freeze would allow UtiliCorp to recover at least a portion of its investment through the effect of regulatory lag. In other words, UtiliCorp anticipates that its cost of service will go down because of the savings resulting from the merger. It wants assurance that the Commission will not reduce its rates until UtiliCorp's shareholders have had a chance to benefit from that decreased cost of service.

The Commission has approved a rate freeze as part of other merger cases. However, in each case the rate freeze was a part of a stipulation and agreement submitted for the Commission's approval by all the parties. In this case, UtiliCorp is asking that the Commission impose a rate freeze on unwilling parties. For a number of reasons, UtiliCorp's request cannot be granted.

First, the imposition of a five-year rate freeze would be contrary to the Commission's statutory obligation to provide continuous regulation of the public utilities of this state. In describing the authority and

responsibility of the Public Service Commission, the Missouri Supreme Court has stated that the Commission is:

> a fact finding body, exclusively entrusted and charged by the legislature to deal with and determine the specialized problems arising out of the operation of public utilities. . . . Its supervision of the public utilities of this state is a continuing one and its orders and directives with regard to any phase of the operation of any utility are always subject to change to meet changing conditions, as the commission, in its discretion, may deem to be in the public interest.

*State ex rel. Chicago, R. I. & P. R. Co. v. Public Service Commission*, 312 S.W.2d 791, 796 (Mo. 1958). In rejecting a proposed stipulation and agreement that would have limited the Commission's ability to entertain complaints against a Missouri utility, the Commission stated as follows:

> The Commission cannot agree to relinquish its statutory duties as proposed by the parties. The Commission is essentially a creation of the Legislature and, as such, is empowered by statute to carry out certain functions. Among the various statutory responsibilities incumbent on the Commission to perform are the setting of rates (Section 393.150, RSMo), the provision of safe and adequate service (Section 393.130, RSMo), the proper litigation of complaints (Section 386.400, RSMo) and other general powers (Section 393.150). The Commission cannot proceed in a manner contrary to the terms of a statute and may not follow a practice which results in nullifying the express will of the Legislature.

*Public Counsel v. Missouri Gas Energy* 6 Mo. P.S.C. 3d 464, 465 (1997). The views expressed by the Commission in that earlier case are still appropriate. Imposition of a five-year rate freeze would purport to deprive the Commission of the legislatively imposed duty to adjust UtiliCorp's rates to meet changing conditions. The Commission will not agree to relinquish its statutory duties.

Second, even if the Commission were willing to agree to a five-year rate moratorium, it is apparent that such a rate moratorium could not be effective to actually freeze UtiliCorp's rates. Section 386.390.1, RSMo 1996, permits the Commission, the Office of the Public Counsel, municipal and county officials, or a group of not less than twenty-five

ratepayers, to bring a complaint before the Commission seeking to challenge the reasonableness of the rates charged by an electrical corporation. The Commission clearly cannot prevent the Office of the Public Counsel, municipal or county officials or qualifying groups of ratepayers from bringing a rate complaint against UtiliCorp within the proposed five-year moratorium. Instead, UtiliCorp asks that the Commission bar its Staff from participating in or assisting in any complaint brought by another party. Essentially, then, UtiliCorp would have the Commission go through the motions of providing a fair hearing for a rate complaint brought during the five-year rate moratorium, but it would expect the Commission to have prejudged that complaint in favor of UtiliCorp. Obviously, such a practice would be both illegal and unethical.

The Commission cannot prevent appropriate parties from bringing a rate complaint during the five-year rate moratorium, nor can it prevent UtiliCorp or even a future Commission from ignoring such a moratorium. In a 1975 case, *State ex rel. Jackson County v. Public Service Commission*, 532 S.W.2d 20 (Mo. banc. 1975), the Missouri Supreme Court reversed a circuit court decision that would have prevented the Commission from granting a rate increase during a two-year moratorium established by the Commission in a previous rate case. The court held that "to rule otherwise would make section 393.270(3) of questionable constitutionality as it potentially could prevent alteration of rates confiscatory to the company or unreasonable to the consumers." *Jackson County* at 29-30. Therefore, UtiliCorp would be free to seek increased rates and the Commission would be free to establish revised rates despite the existence of a moratorium.

Third, even if all the legal barriers to an effective rate moratorium could be surmounted, a five-year rate moratorium would not be good public policy either from the perspective of UtiliCorp or its ratepayers. The electric utility marketplace has seen phenomenal change in

recent years. Certainly there is no reason to believe that the pace of change will diminish in the next five years. The cost of fuel might fluctuate significantly, plans for possible deregulation of the electric industry are under consideration in the legislature, and there is always the possibility of an unforeseen event. Attempting to lock in a rate now to remain in effect until 2006 simply is not fair to either UtiliCorp or its ratepayers and is not good public policy.

**Other Aspects of the Regulatory Plan:**

In addition to the proposed five-year rate freeze, UtiliCorp's proposed regulatory plan would have the Commission establish, in this case, several facts that would be used to establish UtiliCorp's rates in a both the Pre-Moratorium and Post-Moratorium Rate Cases. In particular, UtiliCorp would have the Commission decree that for the post-moratorium rate case, the return allowed on the assigned premium would be based on a UtiliCorp capital structure of sixty percent debt and forty percent equity. The return allowed on the balance of the rate base would be based on an Empire stand-alone unit capital structure as determined in the Pre-Moratorium Rate Case.

Empire's stand-alone capital structure is more reliant on equity and less reliant on long-term debt. UtiliCorp utilizes a more highly leveraged capital structure closer to forty percent equity and sixty percent debt. UtiliCorp's preference for a capital structure more reliant on long-term debt enables it to acquire capital at the relatively low rates that are available for debt financing, rather than the relatively high rates that are required for equity financing. By utilizing, for ratemaking purposes, a hypothetical capital structure that overstates the use of equity financing, UtiliCorp would receive a higher rate than it would otherwise receive and thus would be able to recover a portion of the acquisition premium. UtiliCorp argues that because Empire's capital

structure probably would not change absent the merger, the use of a hypothetical capital structure would merely maintain the status quo for Empire's ratepayers and thus would not be a detriment to them.

Similarly, UtiliCorp asks the Commission to declare that in post-moratorium rate cases the allocation of UtiliCorp's corporate and intra-business unit costs to UtiliCorp's MPS operating division would exclude the Empire factors. Thus, UtiliCorp asks the Commission to ignore the effect that the addition of the Empire division to UtiliCorp would have on the costs allocated to MPS. The fact that the Empire division had been added to the UtiliCorp corporate structure would tend to reduce the amount of corporate and intra-business unit costs that would be allocated to each of UtiliCorp's operating divisions. By ignoring the addition of the Empire division, UtiliCorp's plan would have the effect of preventing a decrease in the MPS division's cost of service and would keep the rates paid by MPS's ratepayers somewhat higher than they might otherwise be if the addition of the Empire division were allowed to be included. UtiliCorp argues that such a result is fair because those corporate allocations will not be reduced if the merger is not completed.

In addition, UtiliCorp asks the Commission to determine that it will be allowed to recover transaction costs and costs to achieve associated with the merger. Again, UtiliCorp argues that such costs are part of the costs that must be incurred to achieve the savings that will result from the merger.

Finally, UtiliCorp asks the Commission to establish, in this case, certain items, including the test year and in-service/commercial operation criteria for the State Line Combined Cycle plant, that are at issue in what it refers to as the Pre-Moratorium Rate Case.

Essentially, in each matter, UtiliCorp asks the Commission to state now how it will rule on certain issues in future rate cases. The

Commission will not do so. Section 393.270.4, RSMo 1994, provides that when the Commission determines the rate that can be charged by a utility, it:

> may consider all facts which in its judgment have any bearing upon a proper determination of the question . . . , with due regard, among other things, to a reasonable average return upon the value of the property actually used in the public service and to the necessity of making reservations out of income for surplus and contingencies.

The law is quite clear that when determining a rate the Commission is obligated to review and consider *all* relevant factors, rather than just a single factor. See *State ex rel. Missouri Water Co. v. Public Service Commission*, 308 S.W.2d 704 (Mo. 1957); *State ex rel. Utility Consumers' Council of Missouri, Inc. v. Public Service Commission*, 585 S.W.2d 41 (Mo banc 1979); and *Midwest Gas Users' Association v. Public Service Commission*, 976 S.W.2d 470 (Mo. App. W.D. 1998). To consider some costs in isolation might cause the Commission to allow a company to raise rates to cover increased costs in one area without realizing that there were counterbalancing savings in another area. Such a practice is justly condemned as single-issue ratemaking. *Midwest Gas Users' Association* at 480.

In order to avoid single-issue ratemaking, the Commission has avoided making decisions about rate case matters outside of the context of a rate case. In fact, the Commission typically includes language in non-ratemaking cases that specifically provides that the ratemaking treatment to be afforded a transaction will be considered in a later proceeding. The ratemaking factors that UtiliCorp asks the Commission to decide in this case can only be properly considered within the context of all relevant factors in a subsequent rate case. The Commission will not engage in single-issue ratemaking and will decline UtiliCorp's invitation

to prejudge certain factors that can only be properly considered in a future rate case.

**Recovery of the Acquisition Premium:**

UtiliCorp's proposed regulatory plan asks that the Commission find, in this case, that UtiliCorp should be allowed to include in the rate base of the Empire division's retail electric operations in a future rate case, up to fifty percent of the unamortized balance of the acquisition premium paid by UtiliCorp for Empire. UtiliCorp proposes that this recovery would be contingent upon UtiliCorp proving to the Commission that merger synergies are equal to fifty percent of the premium costs and other costs to achieve the synergies. In other words, UtiliCorp asks that it be allowed to recover from Empire's ratepayers, through its rates, the acquisition premium it paid to purchase Empire, to the extent that the ratepayers would benefit from the savings arising from the merger.

In asking the Commission to decide in this case how it will treat its request for recovery of its acquisition premium, UtiliCorp is asking the Commission to prejudge a ratemaking factor outside a ratemaking case. As previously indicated, the Commission will not do so. The Commission will give due consideration to a proposal to provide for recovery of a merger premium if that proposal is presented in a rate case.

The matter of the acquisition premium is not properly before the Commission. It is a matter for a rate case. Therefore, the Commission will not address the matter of the acquisition premium in this case.

## D. Transmission Access and Reliability Conditions:

Springfield raised numerous issues regarding the possible effects that the merger would have on the transmission of electricity within and between the service territories of UtiliCorp's MPS division and Empire, and on the transmission of electricity destined to other electric service

providers, such as Springfield. Springfield presented expert testimony that purported to show that the merger and the ensuing joint dispatch of the electricity resources of the merged companies could have negative effects upon the flow of electricity on the transmission system of the combined company and surrounding electric service providers. Springfield proposed several conditions that would require UtiliCorp to further study the flow of electricity and would require UtiliCorp to take steps to correct any problems identified by those studies. UtiliCorp replied that the FERC has exclusive jurisdiction over these issues and that they should not be addressed by this Commission.

The question of whether the Commission has jurisdiction over the transmission access and reliability issues raised by Springfield is answered through a review of applicable federal law. In 1935, Congress passed the Federal Power Act, which created Federal jurisdiction over the "transmission of electric energy in interstate commerce and the sale of such energy at wholesale in interstate commerce." 16 U.S.C. §824(a). That act also provides that the various states retain jurisdiction over "facilities used in local distribution or only for the transmission of electric energy in intrastate commerce." 16 U.S.C. §824(b) In 1996 the FERC issued Order No. 888, which interprets the Federal Power Act as leaving regulation of only bundled retail transmissions[9] to the various states. The FERC's order asserts federal jurisdiction over all unbundled retail transmissions as well as wholesale transmissions.

The FERC, in Order No. 888, adopted a seven-factor test to determine whether the activities of the facility in question are used for

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[9] "Vertically integrated utilities use their own facilities to generate, transmit, and distribute electricity to their customers. Traditionally the customer paid one combined rate for both the power and its delivery, thus the industry refers to such sales as 'bundled'." *Transmission Access Policy Study Group v. F.E.R.C.*, 225 F.3d 667, 691 (D.C. Cir. 2000)

local distribution and thus are subject to state jurisdiction. That seven-factor test is as follows:

(1) Local distribution facilities are normally in close proximity to retail customers.

(2) Local distribution facilities are primarily radial in character.

(3) Power flows into local distribution systems; it rarely, if ever, flows out.

(4) When power enters a local distribution system, it is not reconsigned or transported on to some other market.

(5) Power entering a local distribution system is consumed in a comparatively restricted geographical area.

(6) Meters are based at the transmission/local distribution interface to measure flows into the local distribution system.

(7) Local distribution systems will be of reduced voltage.

The FERC's interpretation of the Federal Power Act was recently upheld by the United States Court of Appeals for the District of Columbia Circuit in *Transmission Access Policy Study Group v. F.E.R.C.,* 225 F.3d 667 (D.C. Cir. 2000).

If the FERC's seven-factor test is applied to the issues raised by Springfield, it is apparent that Springfield's concerns do not relate to unbundled retail transmissions as they are defined by the FERC. Springfield's fundamental concern is that the merger will disrupt the flow of wholesale power that it receives through the service territories of UtiliCorp and Empire. The Commission will not attempt to determine the validity of Springfield's concerns and will instead defer to the jurisdiction of the FERC.

Springfield's issues regarding transmission access and reliability concern the transmission of power across service territories for purpose of

wholesale deliveries. They are properly regulated by the FERC and are not subject to regulation by this Commission. For that reason the conditions proposed by Springfield regarding transmission access and reliability will not be imposed.

### E. Jurisdiction

UtiliCorp is an "electrical corporation," a "gas corporation" and a public utility as those terms are defined in Section 386.020, RSMo Supp. 1999, and is subject to the jurisdiction of the Commission pursuant to Section 386.250, RSMo Supp. 1999. Empire is an "electrical corporation," a "water corporation," a "telecommunications company" and a "public utility" as those terms are defined in Section 386.020, RSMo Supp. 1999, and is subject to the jurisdiction of the Commission pursuant to Section 386.250, RSMo Supp. 1999.

Based upon the Commission's review of the applicable law and its findings of fact, the Commission concludes that the proposed merger between UtiliCorp and Empire is in the public interest because it is not detrimental to the public.

**IT IS THEREFORE ORDERED:**

1. That The Empire District Electric Company is authorized to merge with and into UtiliCorp United Inc. with UtiliCorp United Inc. being the surviving corporation, and to otherwise accomplish the merger, all as more particularly described in and pursuant to the terms of the Agreement and Plan of Merger.

2. That The Empire District Electric Company is authorized, through the merger, to transfer to UtiliCorp United Inc. all the properties, rights, privileges, immunities and obligations of The Empire District Electric Company, including, but not limited to, those under The Empire District Electric Company's certificates of public convenience and

necessity, works, systems and franchises, and all securities, evidences of indebtedness and guarantees, effective as of the date of the closing of the merger.

3. That UtiliCorp United Inc. is authorized to acquire and assume the stocks and bonds, other indebtedness and other obligations of The Empire District Electric Company, all as more particularly described in and pursuant to the terms of the Agreement and Plan of Merger.

4. That The Empire District Electric Company and UtiliCorp United Inc. are authorized to perform in accordance with the terms of the Agreement and Plan of Merger.

5. That The Empire District Electric Company is authorized to terminate its responsibilities as a public utility in the state of Missouri as of the effective date of the merger.

6. That UtiliCorp United Inc., the surviving corporation, is authorized to provide electric, water and telecommunications service in the current service territories of The Empire District Electric Company in accordance with the rules, regulations, rates and tariffs of The Empire District Electric Company as may be on file with and approved by the Commission as of the effective date of the merger, except as otherwise provided for herein or as otherwise ordered by the Commission. Further that the transfer of all The Empire District Electric Company's customers to UtiliCorp United Inc. is authorized as contemplated by Section 393.106, RSMo 1994.

7. That the Regulatory Plan proposed by UtiliCorp United Inc. is rejected.

8. That The Empire District Electric Company and UtiliCorp United Inc. are authorized to enter into, execute and perform in accordance with the terms of all other documents and to take any and all actions which may

be reasonably necessary and incidental to the performance of the Agreement and Plan of Merger.

9. That the stipulation and agreement between the Empire Retirees, UtiliCorp United Inc. and The Empire District Electric Company, filed on October 18, 2000, is approved.

10. That the stipulation and agreement between the Staff of the Commission, UtiliCorp United Inc. and The Empire District Electric Company, filed on November 30, 2000, is approved.

11. That the Commission's approval of the merger of The Empire District Electric Company with and into UtiliCorp United Inc. is subject to UtiliCorp United Inc.'s agreement to the following conditions:

a. That in post-merger cases involving UtiliCorp United Inc.'s Empire District Electric Company operating division, UtiliCorp United Inc. will maintain the pre-merger funded status of The Empire District Electric Company's pension fund by accounting for it separately.

b. That if the merger is determined to be a taxable event and deferred taxes of The Empire District Electric Company are thereby lost, UtiliCorp United Inc. shall include an amount equal to those deferred taxes in future rate proceedings for its Empire District Electric Company operating division as an offset to rate base.

c. That UtiliCorp United Inc. shall continue to file separate surveillance reports for its Missouri Public Service and Empire District Electric Company operating divisions following the closing of the merger.

d. That for one year following the closing of the merger, UtiliCorp United Inc. shall provide the Staff of the Commission with monthly reports regarding Call Center Abandoned Call Rate (ACR), Call Center Average Speed of Answer (ASA), Distribution Reliability Customer Average Interruption Duration (CAIDI), Distribution Reliability System

Average Interruption Frequency Index (SAIFI), and Distribution Reliability System Average Interruption Duration Index (SAIDI).

e. That UtiliCorp United Inc. shall provide historical actual hourly generation, energy purchases and sales data, and other information required by Commission Rule 4 CSR 240-20.080 in electronic format accessible by a spreadsheet program for both the Missouri Public Service and Empire District Electric Company operating divisions of UtiliCorp United Inc. UtiliCorp United Inc. shall also provide access to such additional documents as may be necessary for the Staff of the Commission to analyze fuel and energy costs.

f. That after the closing of the merger, UtiliCorp United Inc. shall file with the Commission an adoption notice in Empire's electric and water tariffs as follows:

**ADOPTION NOTICE**

> Effective [month, day, year], The Empire District Electric Company (EDE), a Kansas corporation, has merged with and into UtiliCorp United Inc. (UtiliCorp), a Delaware corporation, as authorized by the Missouri Public Service Commission in Case No. EM-2000-369. UtiliCorp is the surviving entity.
> Pursuant to the Commission's Report and Order issued [month, day, year], in said case, UtiliCorp hereby adopts, ratifies and makes its own in every respect, as if the same had been originally filed by it, all tariffs, schedules and rules and regulations of EDE filed with and approved by the Commission before [month, day, year]. UtiliCorp will operate in the area formerly served by EDE using the name "[insert name here]."

12. That any evidence the admission of which was not expressly ruled upon is admitted into evidence.

13. That any objection that was not expressly ruled upon is overruled.

14. That any motions not expressly ruled upon are denied.

15. That nothing in this order shall be considered a finding by the Commission of the value for ratemaking purposes of the transactions herein involved.

16. That the Commission reserves the right to consider any ratemaking treatment to be afforded the transactions herein involved in a later proceeding.

17. That this Report and Order shall become effective on January 7, 2001.

**BY THE COMMISSION**

**Dale Hardy Roberts**
**Secretary/Chief Regulatory Law Judge**

( S E A L )

Lumpe, Ch., Drainer, Murray, Schemenauer, and Simmons, CC., concur and certify compliance with the provisions of Section 536.080, RSMo 1994.

Dated at Jefferson City, Missouri, on the 28th day of December, 2000.

ALJ/Sec'y: Woodruff / Boyce

12-26
Date Circulated

EM-2000-369
CASE NO.

Lumpe, Chair

Drainer, Vice Chair

Murray, Commissioner

Schemenauer, Commissioner

Simmons, Commissioner

12-28
Agenda Date

Action taken: 5-0 AA

Must Vote Not Later Than

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

**I have compared the preceding copy with the original on file in this office and I do hereby certify the same to be a true copy therefrom and the whole thereof.**

**WITNESS my hand and seal of the Public Service Commission, at Jefferson City, Missouri, this 28th day of December 2000.**

Dale Hardy Roberts

**Dale Hardy Roberts**
**Secretary/Chief Regulatory Law Judge**