BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

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

POST-HEARING REPLY BRIEF OF INTERVENOR AG PROCESSING INC

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COMES NOW Intervenor Ag Processing Inc. a Cooperative (AGP) and submits its Reply Brief in this proceeding. Most of the Joint Applicants' arguments were anticipated in our Initial Brief. Some few deserve further response, which here follows.

I. INTRODUCTION.

A. The Difference Between Approval of a "Clean" Merger Application and a Complicated "Regulatory Plan" Must Be Distinguished.

The basic error of both Applicants' Initial Briefs, and their error in the case itself, concerns what the Commission is supposed to review and evaluate and the standard applicable to its actions. There seems little dispute that the standard of review applicable to approval of a **merger** is whether there is public detriment. The Applicants appear to miss the point of this entire case, namely that their efforts should have been concentrated on demonstrating that the **merger** did not result in public detriment rather than attempting to validate a regulatory plan that shifts the cost of the acquisition to the backs of the St. Joseph Light & Power Company (SJLP) ratepayers. This failure to distinguish between the **merger** and the **regulatory plan** permeates both Joint Applicants' Initial Briefs.

The cases cited by Applicants deal essentially with "clean" merger applications. Utility "A" agrees to merge with Utility "B" and seeks Commission approval. No complex "innovative" regulatory plan is proposed, no extra-jurisdictional relief is sought from the Commission. The shareholders of the acquiring company approve (if appropriate, through its Board of Directors) and the shareholders of the acquired utility approve and the merger transaction proposed stands or falls on its own business merit. Any economies of scale that are gained (and which should be the motivator for the transaction) result in reduced operating costs which, in turn, result in reduced rates. That is, assuredly, **not** this case.

B. This Case Presents Not a "Clean" Merger, Rather An Attempt By Two Monopolies to Use Their Monopoly Power and Captive Customers to Improve Their Position in Competitive Markets.

Here are two monopoly companies, one of whom is smaller and complains that it "cannot compete" because of its size. Yet representatives of both testified that there was no competition in the SJLP service area for distributors of electric energy and no plan or view to have such service become competitive. These monopolies want to become stronger "competitors" in areas and in aspects of their business in which they face competition and want the ratepayers of both companies to fund the transaction through the so-called "regulatory plan." More properly, it should be called the "acquisition premium recovery scheme."

C. SJLP's Initial Brief.

Several statements in SJLP's Initial Brief are revealing and deserve further analysis.

1. SJLP Faces No Threat From Competition for Its Distribution Or Monopoly Business.

First, at page 5, SJLP states that "[i]nstead, smaller utilities must evaluate whether they can continue to offer quality services in a climate of customer choice." The "climate of customer choice" to which SJLP refers is not currently a reality in Missouri and, indeed was argued to be so uncertain and so far in the future that market power studies were unnecessary. Ironically, SJLP urges a presently non-existent "climate of customer choice" as justification for the merger but resisted the market power implications of that "climate" contending that those were matters that were beyond the scope of the Commission's consideration. Sauce for the goose becomes sauce for the gander. If the "climate of customer choice" is irrelevant for market power studies, it is also irrelevant as justification for the merger.

But that minor point aside, SJLP's statement needs analysis as to the "climate of customer choice" that so threatens

SJLP. The "climate" referred to concerns **only** the potential for a retail customer to choose a generation supply. The "wires" or the distribution system currently owned and maintained by SJLP would be unaffected.[1] The Commission would set distribution rates and SJLP would remain as the monopoly provider for those distribution services **without which customer "choice" as to generation would be meaningless**. Thus, the only "threat," if threat it be, from "customer choice" is to SJLP's monopoly position as the sole source of generation supply for its customers.

2. SJLP Would Continue to Be A Low Cost Supplier -- and Its Low Cost Generation Is Why UCU Is Willing to Pay An Acquisition Premium.

Further analyzed, even that "threat" evaporates when it is realized that SJLP will be a low cost supplier of such generation resources in a market-based "climate of customer choice." SJLP's principal generation resources are Lake Road and Iatan, both low cost base load sources. The only fears that SJLP should have from a "climate of customer choice" is that customers would seek to purchase supplies of energy from other providers. Unless

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[1] SJLP appears to acknowledge this on the next page of its Initial Brief where in discussing Mr. Ferry's testimony, it states:

> SJLP is reacting to the change ***in which wholesale generation is deregulated***. [Mr. Ferry] testified that ***it is now a competitive service*** while retail service is regulated.

SJLP Initial Brief, p. 6 (emphasis added) they were able to beat SJLP's low cost generation in the market place, it is unlikely that a competitor would be chosen as a source of supply over SJLP. But even if they were, SJLP would still be the monopoly distributor within its assigned service territory at rates that would reflect the cost of service of that distribution system.

3. Market Price Fluctuations Are Not the Problem.

SJLP complains that the deregulated wholesale power market fluctuates. AGP is not impressed. Try soybeans! Other companies have for years dealt with market conditions and fluctuations. Utilities have proven to be skilled at "risk avoidance" by being in a cost-plus business, shifting their business risk to captive ratepayers and simultaneously whining about how they should be allowed a 15% plus rate of return because of their "risk." The concept of "risk management" is obviously foreign to utilities, but countless companies engage in it and work successfully in competitive markets every day, both for raw materials and for their finished goods. Tools exist to manage business risk.

4. Joint Applicants Seek to Enhance Their Competitive Position at the Expense of Their Captive Customers.

Nothing has been demonstrated in this record that supports any concern that SJLP would not be able to offer quality services in a "climate of customer choice." Indeed, it would be **protected** in its monopoly service territory as to the provision of such services in a "climate of customer choice." Accordingly, it is only SJLP concerns that by reason of its size it cannot compete **effectively** in competitive markets and areas in which it is not regulated by this Commission (or by any other regulatory authority). It is only SJLP concerns that by reason of its size it cannot compete in areas in which SJLP would hotly oppose regulatory recognition of profits that drive this merger. Building a more competitive company or business is certainly a SJLP shareholder/Board decision, but it should not be financed by SJLP ratepayers. Instead it should be financed by success in the competitive market which the combination activity is designed to assure. Several times, representatives of UtiliCorp United (UCU) asserted that if the recovery of the acquisition premium were not guaranteed by the Commission, the deal was in trouble. Our response is simple: if the deal's economics depend on shifting the acquisition premium to the ratepayers, then it should be rejected. The real question, which the Joint Applicants' Initial Briefs do not answer, is whether the merger, apart from the regulatory plan, has been shown not detrimental to the public interest.

There is a reason that both Initial Briefs are silent on this issue: it is a hurdle they cannot jump.

5. **The Merger, Even Without the Regulatory Plan, Is Detrimental to the Ratepayers.**

Apart from the proposed regulatory plan, the merger itself is detrimental. Neither Joint Applicant does anything in their Initial Briefs to explain away these demonstrated flaws.

The supposed cure-all is the rate moratorium. AGP and others demonstrated in our respective initial briefs that the Commission cannot impose upon itself, its Staff or upon non-consenting customers any such rate moratorium. Indeed, it cannot even deny the utility access to the regulatory forum. But beyond that, the evidence demonstrates that the effect of the moratorium is to deny the ratepayers what would otherwise be reductions in their rates by forcing them to shoulder the burden of the acquisition premium. If the claims of synergies have any substance, then the ratepayers should have commensurate reductions. To do otherwise forces them to pay the acquisition premium, which should be the responsibility of shareholders.

Joint Applicants' argument then asserts that without acquisition premium recovery from ratepayers there would be no utility mergers. Were that argument true, then unregulated companies would never merge nor be acquired. The simple difference is whether the **merger** makes economic sense for the acquiring or surviving company. Unregulated companies, by definition, have no "regulatory plan" to shift risks to their captive customers. If the merger synergies do not result in lower costs or improved market position, an unregulated merger will not meet even the "sniff" test. If the **unregulated** marketplace will not justify the merger, then it does not happen.

6. Interrelationship of This Case and the AAO Application [EO-2000-845].

As regards the interrelationship of this docket and the AAO docket, EM-2000-845, on the eve of this filing Staff filed motions pertaining to both cases and raising questions about the consistency of positions. We also have observed the financial news on the transaction and note the same inconsistency. That inconsistency is very apparent in SJLP's Initial Brief which, at pages 16-17 which demonstrate that the "write off" would simply result in increasing the burden on ratepayers. Although this is not the AAO docket, AGP notes that the cost of purchased power is a part of the fuel costs of the electric generator and a fuel adjustment clause or any substitute therefor was ruled unlawful by the Missouri Supreme Court. Certainly, SJLP may file all the rate cases it wishes, so that threat is vacuous.

D. UCU's Initial Brief.

There are some specific issues in UCU's Initial Brief that also need to be addressed.

1. The Burden of Proof Remains on the Joint Applicants.

UCU states in its Initial Brief, at page 3, that the merger must be approved "unless it can be shown by competent and substantial evidence on the record that the merger would be detrimental to the public interest." *State ex rel. St. Louis v.*

Public Service Commission, 73 S.W.2d 393, 400 (Mo. *en banc* 1934), is cited for the proposition.

The proposition is not supported by the *St. Louis* case or by any other. The burden of showing that the proposed merger is not detrimental remains at all times on UCU. But there is a more subtle point: As noted above, Joint Applicants seek to confuse the approval of the **merger** with the approval of the **regulatory plan**. While neither should be approved, note the subtle change in wording below which occurs on only the next page of UCU's Initial Brief: "Based on this standard established by the Courts and followed by the Commission, it is clear that the ***transaction*** should be approved." (Emphasis added). The merger, which is subject to the "not detrimental" standard, has been transmuted to a "transaction" obviously intended to include the regulatory plan. As noted earlier, that is the basic error of this entire package.

2. Merger Savings Do Not Exceed Merger Costs.

UCU's Initial Brief simply ignores the evidence. Exhibits 502 and 503 showed that merger savings did not exceed merger costs. Detriments are shown in parentheticals on this exhibit. UCU boldly denies (p. 57) the demonstration that costs exceed benefits for the steam and gas customers. These exhibits were from the Joint Applicants' own workpapers. Ignoring facts does not make them go away. Thus, on a **stand-alone basis** the merger should be rejected -- even without consideration of the adverse effects of the "regulatory plan."

3. Risk of the Transaction is Placed Squarely on the Ratepayers.

UCU repeatedly characterizes its shareholders have having accepted the risk of the transaction. If so, then why are "guarantees" from the Commission the apparent *sine qua non* for the transaction? At page 8 of its Initial Brief, UCU states that the "Regulatory Plan is designed to make the merger transaction economically feasible from UtiliCorp's standpoint . . . ." UCU has it backwards. If the combination of the companies is not economically feasible without the regulatory plan, it simply should not be done. To the contrary, UCU now asserts that approval of the regulatory plan is now "absolutely essential to eh financial viability and thus the completion of this merger." UCU Initial Brief, p. 12 (emphasis in original).

UCU asserts that all it wants is a return "on" its investment (UCU Initial Brief, p. 12), and a return "of" its investment (UCU Initial Brief, p. 15). Of course, the ratepayers both of SJLP and of MoPub would pay this return "on" and return "of" the "investment." If that is so, and UCU seeks guarantees from the Commission, then where has the risk gone?

This is about as clear a case of a monopolist seeking to have the regulated side of its business finance and support the competitive side as can be imagined. If UCU shareholders really want the risk of this transaction, the Commission can assign it to them. To the contrary, however, the guarantees from the Commission, to the detriment of ratepayers, are now "absolutely essential" to the viability of this deal. Instead, the deal needs to be seen as overcooked and should be discarded.

4. UCU Provides No Authority to Show that the Commission Can Lawfully Order a Moratorium Nor Preclude Staff from its Obligations.

UCU's insistence on a "rate freeze" or "moratorium" has now changed. Apparently realizing that AGP and other parties cannot be bound to an agreement that they wish not to make, UCU now has retreated from its position that the Commission could preclude these parties and the Public Counsel from seeking to reduce rates. The Commission will recall during the hearing how tenaciously UCU personnel held to the view that all parties could be bound. Once again, the view has changed. Still, however, no authority is provided to substantiate the view that the Commission can bind itself or its unwilling Staff.

What this contention, of course, raises is the very position of the Staff in this hierarchy. Either the Staff is an independent party, held to the same standards as any other party, or it is the arm of the Commission. The Commission can no more bind Staff by its order than it can bind itself or any other unwilling party. UCU cites no authority for its argument because none exists. Indeed, the authorities are to the contrary as discussed at pages ___ of Staff's Initial Brief.

UCU fails to apparently understand the critical difference between this case and cases in which parties have *agreed* to a rate moratorium. Here there is no such agreement, Staff certainly has not agreed to such a limitation and the Commission cannot, under the law, even bind itself.

5. If UCU Had An "Understanding" About the Commission's Decision, Such Understanding Was Misplaced.

At page 16 of its Initial Brief, UCU makes an interesting statement:

> UtiliCorp entered into the Merger Agreement ***with the understanding*** that based on past Commission decisions, it would have a reasonable opportunity for premium recovery through approval of its Regulatory Plan.

(Bolded emphasis added; underlining in original). Such an "understanding" was certainly misplaced. During cross-examination, Mr. Green seemed unable to clearly identify the basis of this understanding and on what it was based. Pressed, he identified "regulatory personnel" and outside counsel, but was able to identify no written document containing such legal opinion. AGP's attempt to seek disclosure of such information was rebuffed by the RLJ.

Absent such documentation, assertions about UCU's "understandings" should be given no weight whatsoever. As an aside, it should be considered as remarkable that a NYSE-listed company such as UCU would base such a critical "understanding" regarding a part of the Regulatory Plan that it now asserts is "absolutely essential" to only a verbal and unverifiable statement. Such an assertion lacks obvious credibility, but **if true** it sharply undercuts UCU's current assertion that such "understanding" was "absolutely essential" to the continuation of the merger.

6. The "Must Decide" Issue of Savings Tracking Can Be Decided Negatively.

UCU now asserts, at page 17 of its Initial Brief, that the Commission must decide whether tracking merger savings is possible and what the "benchmarks" would be. Absent such a decision, UCU "cannot determine whether the merger with SJLP will be economically feasible and should be closed." Not happy with shifting the risk of its deal to the SJLP and MoPub ratepayers, UCU now attempts to shift the blame for the deal's falling apart on the Commission.

The Commission is in the status of a judge. It is not a partner in this merger, a consultant to UCU, nor its scrivener. Throughout the entire course of the hearing, neither of the Joint Applicants could come forward with a coherent and accurate scheme to track merger savings nor a set of "benchmarks" that could be used. Apparently now that the hearing is over, and realizing its failure, UCU invites the Commission to fabricate a merger savings tracking mechanism that neither Joint Applicant could design.

What appears really to be the case is that UCU wants to try to jockey the Commission into the position of having a stake in the merger proceeding. This is, we believe, improper. If the evidence isn't there, the Commission cannot decide the issue, or should simply decide that it cannot on this record make a decision. Of course, a deal that was economically viable would not run aground on such a shoal.

II. CONCLUSION.

UCU and SJLP have given the Commission several bases to reject this package (if package it be) even in their own Initial Briefs. It is clear based even on their Initial Briefs that the only way in which this deal can be justified from UCU's perspective is if UCU is permitted to recover the costs of becoming a stronger competitor and acquiring low cost generating assets to do so from the regulated side of its business. This request represents an open and unlawful perversion of regulation. The merger **without** the regulatory plan is not economically viable according to UCU's own arguments and evidence. Indeed it is detrimental to the ratepayers. The effect of the regulatory plan is to shift the costs of the transaction premium to the ratepayers on the regulated side of the business who are the only source from which UCU shareholders can expect a return "of" and "on" their "investment."

It is a detriment to the ratepayers to continue to pay higher rates than current costs justify. If the merger must depend on such detriments to survive, it deserves to die.

WHEREFORE, Ag Processing Inc a Cooperative respectfully requests that the Commission reject both the Regulatory Plan and the proposed merger.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I HEREBY CERTIFY that I have this day served the foregoing pleading by U.S. mail, postage prepaid addressed to all parties by their attorneys of record as provided by the Secretary of the Commission and shown on the sheet following.

Stuart W. Conrad

Dated: October 3, 2000

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