BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

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

CITY OF KANSAS CITY'S PREHEARING BRIEF

Comes now the City of Kansas City, Missouri (City) and submits its prehearing brief on the issues submitted by the parties in this case on November 21, 2007. The City has limited its brief to the issues on which it has taken some position or on which it has filed testimony. With respect to the remaining issues identified by the parties on November 21, 2007, the City takes no separate position, without impairment of its right to brief and argue these issues to the Commission as the evidence unfolds at hearing.

At the outset, the City states that it is generally in favor of the merger proposed in the application. Nonetheless, while the City does not oppose the merger, it must emphasize that to avoid any detriment to the public interest a Commission order approving the merger should include the conditions described below.

Issue IX – Municipal Franchise and Energy Audit

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

To date, Kansas City Power & Light ("KCPL") and Aquila, Inc. ("Aquila") have provided service to the City of Kansas City under separate electric franchise agreements. Because the proposed merger will effectively unite KCPL and Aquila as affiliated entities, with significant integration of operations between the two, simple logic necessitates the conclusion that the City should be able to deal with the affiliated entities under a single franchise agreement.

By way of background, the City's electric franchise agreement with Aquila expired on December 31, 2006. Although the City recently commenced negotiations for a new franchise with Aquila, these negotiations were delayed once the transaction between Aquila and Great Plains Energy was announced. As a result, the City and Aquila continue to operate under the terms and obligations of the expired agreement.

The City's electric franchise agreement with KCPL was granted in 1881 and does not contain a term limit. The KCPL agreement, which is less than two pages in length, contains almost no information on how the parties intend to operate and is truly antiquated. While the City and KCPL negotiated an ordinance in 1996 that would have served as an operational agreement between the parties, KCPL failed to execute that agreement. Accordingly, the original franchise agreement still controls the relationship between the parties. This arrangement stands in stark contrast with municipal-utility relations under modern franchise agreements. Modern franchise agreements, which are no longer executed for indefinite periods of time, include terms and conditions that assure the quality and reliability of electrical service, as well as the provision of customer service through simplified billing and prompt outage restoration. Modern franchise agreements provide clear definitions, timeframes and procedures that reduce the potential for confusion or disagreement, and promote efficient and timely service, thereby reducing costs to consumers. Finally, modern franchise agreements typically incorporate requirements for municipalities and utilities to implement renewable energy programs, establish basic commitments to community development, and include other related provisions that reflect issues important to utilities, local governments, and consumers alike.

The existence of two utilities acting under separate franchise agreements forces the City to expend additional resources and taxpayer money in order to manage its rights-of-way. City departments and personnel must work to meet two separate sets of differing obligations and responsibilities, and must duplicate efforts to monitor and manage two entities providing the exact same type of service to customers. The cost of monitoring and coordination - not to mention confusion - is likely to increase if there are two "separate" legal entities with significantly integrated operations. Thus, a unitary franchise is a common sense solution that will ameliorate these issues for the City *and* the utility.

As KCPL witness John Marshall has explained, "from a community and communication perspective, since the majority of [KCPL] customers live in the same metropolitan area, the merger enables more effective interaction with them, and a more coordinated role in supporting the needs of our community."[1] These observations should apply with equal force to the utility's relationship with the City as well. Nevertheless, KCPL has argued that the Commission cannot impair KCPL's contractual rights under its existing franchise agreement with the City,[2] or, in the alternative, that consideration of a consolidated franchise in this proceeding would be premature because Great Plains Energy intends to maintain two separate legal entities for the foreseeable future.[3] Neither argument is persuasive.

As an initial matter, to the extent that this Commission imposes a "unitary franchise" condition on the merger, opting into such a condition would be strictly voluntary on the part of the merging entities. Irrespective of this observation, it is well-established under Missouri law that the Commission possesses broad authority to "[override] all contracts, privileges, franchises, charters or city ordinances" in order to preserve and maintain the public welfare. *See May Dep't*

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[1] Supplemental Direct Testimony of John R. Marshall at 4, Lines 13-16.
[2] Surrebuttal Testimony of John R. Marshall at 14, Lines 2-6.
[3] *Id.* at 16, Lines 22-23.

Stores Co. v. Union Elec. Light & Power Co., 107 S.W.2d 41, 48 (Mo. 1937). Moreover, since a franchise "is not truly a contract but merely a license for a term of years," contractual impairment of a franchise agreement by the Commission under similar circumstances is not even a legally cognizable claim. *See Missouri ex rel. Union Elec. Co. v. Pub. Serv. Comm. of Missouri*, 770 S.W.2d 283, 286 (Mo. Ct. App. 1989).

In light of the proposed transaction, the appropriate time for the Commission to consider this merger condition is now. Despite its projections of hundreds of millions of dollars in synergies resulting from the integration and consolidation of KCPL and Aquila operations,[4] KCPL is asking the Commission to ignore the practical effect of the transaction on the City's management of its rights-of-way. KCPL cannot have it both ways. The franchise relationship between the utilities and the City must change to properly reflect KCPL's plans for a single experience for all customers. Accordingly, the Commission should condition its approval of this merger on KCPL/Aquila negotiating a single, unitary franchise with the City within nine months of Commission approval.

2. Should Commission approval of the Joint Application be conditioned upon requiring KCPL/Aquila to fund a comprehensive energy audit by a third party to evaluate the City of Kansas City's opportunities for lower costs, increased efficiency, consolidated purchasing and cooperative siting or cogeneration with the utility.

[4] *See*, *e.g.*, Supplemental Direct Testimony of Terry Basham at 1, Lines 15-16 ("The customers of Aquila and KCPL will benefit from the significant synergy savings that the combination of these two companies will produce); *Id.* at 2, Lines 8-10 ("Individual customers, and the community as a whole, will benefit from a larger, stronger regional utility that can be a better corporate citizen and provide low-cost reliable service."); Direct Testimony of William Downey at 4, Lines 13-15 (explaining that "significant savings opportunities are available soon after the close of the Merger through synergy savings related to combined operations of many functions within KCPL and Aquila."); Surrebuttal Testimony of Chris B. Giles at 3, Lines 9-10 ("It is true that much of the benefit to KCPL and Aquila customers from this transaction comes from integrating various KCPL and Aquila functions and activities."); Supplemental Direct Testimony of John R. Marshall at 3, Lines 7-11 ("[U]nderstanding the logic of this deal is as simple as looking at the map of service territories for the two companies," since "[c]onsolidating adjacent operations will enable the two companies to more efficiently cover the same area.").

The City views the Great Plains/Aquila merger as providing an opportunity for the City and the merged utility to reduce the City's energy use by ensuring that City departments are on the appropriate tariffs. KCPL has stated that it intends to realize energy efficiency through the offering of its Affordability, Energy Efficiency and Demand Response programs within Aquila's service territory and augmenting this customer service program with additional Aquila offerings as appropriate. The City is also extremely interested in achieving a greater level of energy efficiency that has not been possible for the City in the past given its service from two providers.

As one of the utilities' largest customers, it will be critical for the City to ensure that it is acquiring and utilizing energy as efficiently as possible in the event that the merger is approved. The City should have the opportunity to receive an aggregate rate for all of its uses, or at the very least take adequate advantage of its consolidated purchasing power. A comprehensive energy audit would address the City's concerns and allow for the City and the newly merged utility to begin from a "clean slate" with regard to the City's energy profile. Ultimately, an energy audit will result in a reduction in taxpayer burden, and increase the City's role as a green citizen of the environment.

KCPL has argued that there are already a number of programs that the City could avail itself of, and that it should not receive an audit at the expense of KCPL's other customers.[5] This argument proves too much. Such a condition will inure to the benefit of *all* of KCPL's customers because, by reducing the City's aggregate demand and identifying opportunities for load shifting, the energy audit will benefit all ratepayers of the merged entity. Furthermore, *any* demand side management or efficiency program can be assailed as benefiting some customers at the expense of others. The whole idea of demand side management – and of this requested audit – is to affect aggregate demand and increase efficiency so that the system as a whole benefits.

[5] Surrebuttal Testimony of John R. Marshall at 17, Lines 17-22.

That is all the City is asking for here—assistance to be a better consumer and assistance to make the entire system more efficient.

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

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

The Joint Applicants' proposal currently lacks specificity regarding rate integration, system integration, customer service integration, and a meaningful commitment to compensate customers if certain service quality standards aren't maintained or improved as a result of the merger.

When regulated monopolies propose mergers that allege significant synergies and cost savings, it is incumbent on the Commission to ensure that service quality to captive customers does not deteriorate. The Joint Application fails to establish obligatory service quality standards that would put some teeth into requirements that the utility meet minimum service quality targets post-merger. Customers should be provided with safeguards to guarantee service quality, and in the event that these standards are not met, the utility should be obligated to provide compensation for the diminution of utility services.

The Commission should therefore require the company to file an application for a Quality of Service Plan, with the appropriate standards and customer remedies, within ninety days of its final decision in this proceeding. While the City is not suggesting that the Joint Applicants are doing anything wrong at this time, this measure is being proposed to avoid potential problems in the future. Regulatory guidelines with defined awards and penalties are best established when a utility has additional motivation for compliance, such as during a merger case that the utilities are strongly pursuing here.

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

In its application for merger approval, Great Plains asserts substantial benefits to itself, its shareholders, KCPL's customers and Aquila's customers. Included in this filing are requests for special regulatory treatment of certain costs and revenues. In this instance, a better approach is for customers to share in the improved cost structure of the merged entity through a mechanism that annually evaluates the earnings picture of the company, and if earnings are realized in excess of the Commission's authorized rate of return, then customers receive a portion of that excess. The Commission should therefore require KCPL/Aquila to commit to an "Earnings Sharing Mechanism" that timely returns excess earnings above an authorized level to customers.

An Earnings Sharing Mechanism would work as follows. On an annual basis, KCPL/Aquila would file financial data with the Commission, and Commission Staff and other interested parties would have an opportunity to review and validate the figures supplied. The procedure could be litigated, but the more likely outcome is that the parties to the proceeding would come to an understanding of appropriate costs and revenues and establish the amounts subject to distribution to customers and the utility. The Commission would then issue a decision ordering the merged entity to return the proper portion of excess earnings to customers.

The most successful Earnings Sharing Mechanism would include a "reverse taper" in determining rewards for customers and the utility. This methodology utilizes the authorized return on equity (ROE) as the threshold above which excess earnings are either retained by the utility or returned to customers. In light of the fact that the easiest earnings to achieve are the next several dollars above the authorized level, the reverse taper returns to customers a greater share of those dollars. After greater excess earnings are achieved, more is retained by the utility. By way of example, if KCPL's authorized ROE is 11.25%, any earnings above 11.25% and up to 12.25% receive a distribution of 65% to customers and 35% to KCPL. Excess earnings above 12.25% up to 14.25% are split 50% each to customers and KCPL. The next 1% of excess ROE is allocated 35% to customers and 65% to KCPL. Finally, all excess earnings over 15.25% are retained 100% by KCPL.

If the utility does not experience a period of excess earnings during a particular year, this should not imply that the Earnings Sharing Mechanism has no value as a regulatory tool. While excess earnings may occur and would be distributed in other years, the opportunity for Staff and other parties to validate the utility's costs and revenues following the annual filing provides an additional regulatory benefit.

<u>Issue XI – Future Rate Case</u>

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

While Great Plains has briefly alluded to the topic of rate integration in its testimony and responses to discovery, its proposal lacks details and discussions of timing, improved rate designs and improved collection of customer data. The company should be dealing now with notions of how this significant transformation can be achieved with the optimum result for the company and its customers.

Rate integration can be an important step toward a total company effort to improve electric system operations and enhanced utilization of generation and transmission resources. Great Plains has stated that it will file cases for the separate operations of its KCPL and Aquila affiliates following the merger, but the savings associated with rate integration should not be deferred to another day. The Commission should therefore order the company to file a proposal to integrate financial operations and electric system operations into a cost structure that can be comprehensively evaluated for efficiencies and improved operations. Following a brief period to track and evaluate data, the company should be obligated to file a comprehensive rate case for its merged operations within three years of the Commission's approval of the merger. The analysis of the new cost structure should lead to more equitable assignment or allocations of costs to the appropriate service territories and customer classes of the new entity. The Commission needn't mandate a uniform rate structure or design throughout the territories, as rationally justified differentials due to geographic or other system differences should be allowed.

Respectfully submitted,

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CERTIFICATE OF SERVICE

A true and correct copy of the foregoing was served via email upon the parties identified on the attached service list on this 27th day of November, 2007.

/s/ Mark W. Comley

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