Missouri Public Service Commission

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May 10, 2000

Mr. Dale Hardy Roberts
Secretary/Chief Regulatory Law Judge
Missouri Public Service Commission
P. O. Box 360
Jefferson City, MO 65102

RE: Case No. GM-2000-637

Dear Mr. Roberts:

Enclosed for filing in the above-captioned case are an original and eight (8) conformed copies of a **STAFF RECOMMENDATION.**

This filing has been mailed or hand-delivered this date to all counsel of record.

Thank you for your attention to this matter.

Sincerely yours,

Cliff E. Snodgrass

Cliff E. Snodgrass
Senior Counsel
(573) 751-3966
(573) 751-9285 (Fax)

CES:sw
Enclosure
cc: Counsel of Record

BEFORE THE PUBLIC SERVICE COMMISSION

OF THE STATE OF MISSOURI

FILED[2]

MAY 1 0 2000

Missouri Public Service Commission

In the Matter of the Application of UtiliCorp United Inc. for Authority to Acquire, Indirectly, an Ownership Interest in AlintaGas Limited, and to Take all Other Actions Reasonably Necessary to Effectuate Said Transaction	)	Case No. GM-2000-637

STAFF RECOMMENDATION

COMES NOW the Staff of the Missouri Public Service Commission (Staff) by and through one of its attorneys, and for its Recommendation in this case, states as follows:

1. On April 11, 2000 Utilicorp United Inc. (Company) filed an Application seeking Commission approval to acquire a 45% equity interest in the securities of AlintaGas Limited (AlintaGas), an Australian corporation.

2. Staff has researched the above Application filed pursuant to §393.190 RSMO. 1994 and 4 CSR 240-2.060(9), which is now 4 CSR 240-2.060(12).

3. The standard for approval of a stock acquisition is "not detrimental to the public interest". This standard was enunciated by the Missouri Supreme Court in City of St. Louis v. Public Service Commission, 73 S.W.2d 393 (Mo. banc 1934) and was echoed by the Commission in The Matter of Missouri Gas Company, et al., 3 Mo. P.S.C. 3d 216, 221 (Case No. GM-94-252) (October 12, 1994).

4. Staff's review of the Company's Application for Commission approval of the transaction indicates that the purchase transaction complies with the standard described above.

5. In the attached Memorandum, which is labeled Appendix A, the Staff recommends that the Commission issue an Order which approves the Company's Application with the following conditions:

   A. That nothing in the Commission's Order shall be considered a finding by the Commission of the value of this transaction for rate making purposes, and that the Commission reserves the right to consider the rate making treatment to be afforded these financing transactions in any subsequent proceeding.

   B. That the Commission's Order shall not be deemed precedent for any future financing, even with similar facts.

   C. That any adverse financial effects of this acquisition shall be borne by the Company's stockholders and not by Missouri ratepayers.

   D. That all records pertaining to this transaction be maintained at the Company's headquarters and shall be made available to the Staff as the Staff deems necessary.

   E. That the Company shall be obligated to provide documentation of proper cost allocations to non-regulated entities.

F. That the Company shall include any costs borne by Missouri Public Service related to these non-regulated subsidiaries in the monthly surveillance reports sent to the Staff.

Respectfully submitted,

DANA K. JOYCE
General Counsel

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Senior Counsel
Illinois Bar No. 3123645

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Certificate of Service

I hereby certify that copies of the foregoing have been mailed or hand-delivered to all counsel of record as shown on the attached service list this 10th day of May, 2000.

Cliff Snodgrass

MEMORANDUM

To: Missouri Public Service Commission's Official Case File
Case No. **GM-2000-637**, UtiliCorp United Inc.

From: Ron Bible, Manager - Financial Analysis Department RB
John Kiebel, Financial Analysis Department (1-2664) JK

Subject: Staff's Recommendation Regarding the Application of UtiliCorp United Inc. for authority to indirectly acquire up to 45% of the capital stock of AlintaGas Limited, a natural gas utility located in western Australia.

Date: May 9, 2000

Approved by: Ronald L. Bible 5/9/00 — Project Coordinator / Date
Thomas R. Schwarz Jr. 5-10-2000 — General Counsel's Office / Date

CES 5-9-2000

UtiliCorp United Inc.

On April 4, 2000, UtiliCorp United Inc. (UtiliCorp, Company) filed pursuant to Section 393.190 RSMo 1994 and 4 CSR 240-2.060 (9), an application requesting authority to indirectly acquire up to 45% of the capital stock of AlintaGas Limited (Alinta). As part of the Application, UtiliCorp has requested that the Public Service Commission (Commission) act on its application by June 8, 2000 due to the bidding timetable for this transaction.

The State of Western Australia (State) is committed to an energy reform and development agenda that is expected to foster the development of new energy sources and enhance competition between existing energy sources. The government's ongoing effort to privatize its natural gas industry is expected to encourage a competitive and integrated energy market in western Australia. The anticipated restructuring is likely to lead to enhanced service standards to both residential and commercial users, as all natural gas customers will be able to select the supplier of their choice by July 2002.

Alinta is a commercial natural gas distribution, retail and marketing business that serves more than 400,000 retail natural gas customers throughout western Australia. It is a direct, wholly owned subsidiary of the Gas Corporation, a statutory corporation owned and operated by the State. Alinta is the only major Australian natural gas utility remaining in State ownership.

The State is in the process of accepting bids for stapled securities of Alinta as part of a two-tiered sale. In the first tier, 45% of the shares will be sold to a successful bidder. This will be followed by a public float for the remaining 55% of the shares. UtiliCorp is seeking approval to acquire only the initial 45% of the shares. The Company was one of four finalists given the opportunity to undertake a comprehensive due diligence inquiry. If UtiliCorp's binding bid is accepted, the

Appendix A

Company's Australian subsidiary (United Energy) will operate Alinta pursuant to a management contract and appoint three of seven members to Alinta's Board of Directors.

According to the Company's Application, UtiliCorp's aggregate direct investment in Alinta will not exceed the sum of $125 million (U.S.) assuming an exchange rate of $.60/$1 U.S. at the time of closing. The funding of this proposed acquisition is expected to come from the issuance of $75 million in long-term debt and the sale of $50 million in common stock. It is likely that UtiliCorp will be required to directly or indirectly guarantee the financing of its subsidiary's stake in Alinta. The proposed ownership structure is depicted in Attachment C.

The Company stated that this acquisition is similar to the bidding process that resulted in its present ownership of United Energy, an Australian electric distribution company, and MultiNet/Ikon, a natural gas distribution business located in the suburbs of Melbourne, Australia. The Commission approved these investments in the context of Case Nos. EM-95-303 and GM-98-531, respectively.

According to Standard & Poor's (S & P) June 1999 Utilities Rating Service, the Company's Commercial Paper was rated A-2, its Senior Secured Debt and Senior Unsecured Debt were both rated BBB, and its Subordinated Debt and Preference Stock were both rated BBB-. The BBB rating is the lowest rating still considered "investment grade."

Based on current and pro forma financial statements submitted with the Application, the Company's capital structure as of December 31, 1999, consisted of 51.38% long-term debt, 5.70% short-term debt, 8.01% preferred stock, and 34.91% common equity. On a pro forma basis showing the full effect of the additional $75 million in long-term debt and the additional $50 million in common equity, the Company's capital structure would consist of 51.62% long-term debt, 5.54% short-term debt, 7.79% preferred stock, and 35.05% common equity (see Attachment A).

The Company's proposed 60% debt/40% common stock transaction would increase its percentage of total debt to total capital by eight basis points, from 57.08% to 57.16%. Although this debt ratio is within acceptable range limits, the percentage of debt is more than 400 basis points higher than both the mean and the median for similarly rated electric utilities. As a result, the Staff does have a concern about the Company's future credit rating and its ability to attract capital.

The Staff has also reviewed other pro forma financial data submitted by the Company (see Attachment B). The pro forma pre-tax interest coverage of 2.21x is within the acceptable range for similarly rated electric utilities. It is the Staff's opinion that the Company's pro forma pre-tax interest coverage ratio would remain reasonable for attracting additional capital. The pro forma funds from operations to total debt ratio of 14.82% is within the acceptable range.

S & P's January 2000 Utility Credit Report for UtiliCorp considered the Company's credit rating outlook to be "stable," but expressed concerns about its high-risk business profile. S & P stated that this conclusion "...reflects moderate utility spending needs and sound utility operations, offset by the company's need to strengthen financial measures in response to a changing business profile that includes higher-risk, nonregulated ventures, like energy marketing and trading. As the nonregulated businesses continue to grow more quickly than the utility operations, UtiliCorp's financial profile will have to strengthen to compensate for the increased business risk."

The rating agency stated that the Company's "...acquisition strategy and focus on unregulated opportunities, the unpredictability of future acquisitions, and the capital requirements associated with these acquisitions impair credit quality. Furthermore, the credit profile of unregulated operations are weaker than the utility's core business." The rating agency also stated that "...energy trading and marketing activities have been slightly negative for credit quality with its high-risk business profile."

S & P had other concerns about the Company's capital structure, such as "Management's aggressive attitude regarding debt leverage and off-balance-sheet obligations appears in the balance sheet ratios, where total debt to capital approaches 60% and is projected to decrease only moderately in the future." The rating agency also stated that "...S & P believes that management's historic affinity for the use of leverage is still present and will limit credit quality in the future."

Another rating agency, Duff & Phelps Credit Rating Company (D & P), considered the Company's credit rating outlook to be "stable" in November 1999. D & P stated that "...interest coverages remain stable reflecting the Company's core domestic utility operations. Expected further slight improvement...would reflect pending utility acquisitions, its growing low business risk international portfolio, improved midstream gas market conditions, and continued growth in its profitable energy trading and marketing operations. Internal cash flow is expected to continue to be sufficient to support a moderate capital expenditure budget."

The Company's Director of Corporate Finance, who formerly was an analyst with S & P, stated that the rating agency's relationship with management is such that the Company would take whatever actions necessary to assure credit quality. According to the Director of Corporate Finance, the Company is committed to maintaining a capital structure of approximately 55% debt and 45% equity in each issuance. The Company stated that its capital structure is expected to stabilize through periodic common equity issuances used to partially refinance debt incurred with acquisitions.

In conclusion, the Staff believes that the transactions described in UtiliCorp's Application will not be detrimental to the ratepayers of its Missouri Public Service division. The Staff recommends that the Commission approve UtiliCorp's Application, with the following conditions applicable to proposed transaction:

1. That nothing in the Commission's order shall be considered a finding by the Commission of the value of this transaction for rate making purposes, and that the Commission reserves the right to consider the rate making treatment to be afforded these financing transactions in any subsequent proceeding.

2. That the Commission's order shall not be deemed to be precedent for any future financing even if the facts may be similar.

3. That any adverse financial effects of this acquisition be borne by UtiliCorp's stockholders and not by Missouri ratepayers.

4. That all records pertaining to these transactions be maintained at UtiliCorp's headquarters and made available to the Staff as the Staff deems necessary.

5. That UtiliCorp be prepared to provide documentation of proper cost allocations to non-regulated entities.

6. That UtiliCorp include any costs borne by Missouri Public Service related to these non-regulated subsidiaries in the monthly surveillance reports sent to the Staff.

Attachments:
A - Pro Forma Capital Structure as of December 31, 1999
B - Selected Pro Forma Financial Ratios
C - Proposed Ownership Structure

ATTACHMENT: A
MO PSC CASE NO. GM-2000-637

Pro Forma Capitalization as of December 31, 1999
for UtiliCorp United Inc.

Capital Component	Percentage of Capital	Capital Dollars	Pro Forma Adjustments	Pro Forma Capital Dollars	Pro Forma Percentage of Capital
Common Equity	34.91%	$1,525,400,000	$50,000,000	$1,575,400,000	35.05%
Preferred Stock	8.01%	350,000,000	0	350,000,000	7.79%
Long-Term Debt	51.38%	2,245,100,000	75,000,000	2,320,100,000	51.62%
Short-Term Debt	5.70%	248,900,000	0	248,900,000	5.54%
Total	100.00%	$4,369,400,000	$125,000,000	$4,494,400,000	100.00%

Financial Ratio Benchmarks
Total Debt / Total Capital

		AA	A	BBB
Standard & Poor's Corporation's Utilities Rating Service, Financial Statistics Electric Utilities June 30, 1999	Range %	38.01-53.16	40.98-55.70	44.70-60.30
	Median %	44.75	48.25	53.00
	Mean %	45.47	48.25	52.99

Note: LT debt includes $42.8 million representing the current portion of LT debt. JK

ATTACHMENT: B
MO PSC CASE NO. GM-2000-637

Selected Pro Forma Financial Ratios for Utilicorp United Inc.

RATIO ANALYSIS	Ratios as of 6-30-99 (1)	Pro-Forma Ratios	S&P Guidelines "AA" Rating (1)	S&P Guidelines "A" Rating (1)	S&P Guidelines "BBB" Rating (1)
Pre-Tax Interest Coverage:	2.23 x	2.21 x	3.77-4.74 x	3.17-4.44 x	2.04-3.44 x
Funds From Operations Interest Coverage:	1.87 x	1.87 x	4.91-6.09 x	3.93-5.22 x	3.04-4.29 x
Funds from Operations to Total Debt:	13.87 %	13.91 %	22.98-34.35 %	19.03-28.00 %	13.10-20.70 %
Total Debt to Total Capital:	57.08 %	57.16 %	42.03-49.85 %	44.90-52.65 %	49.60-57.80 %

Notes:

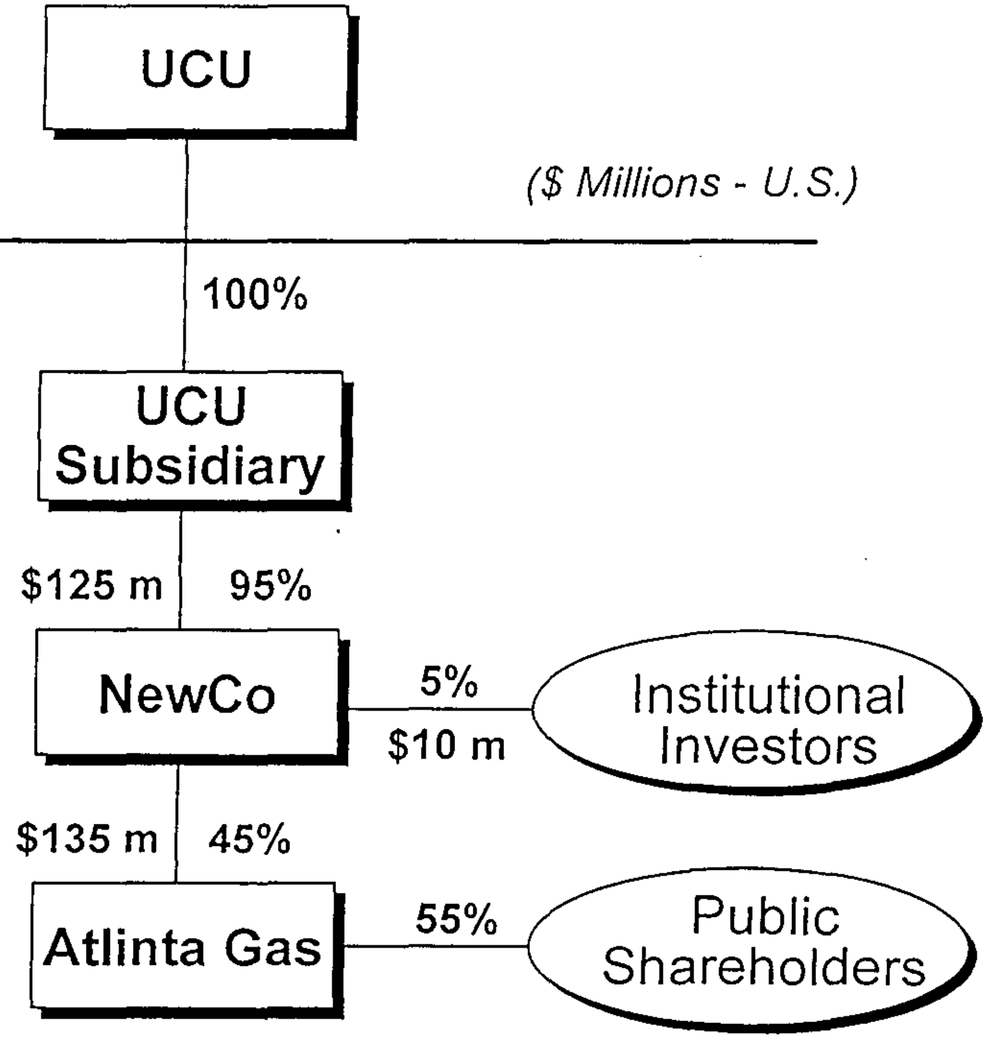
(1) Standard & Poor's Utilities Rating Service, Financial Statistics, June 30, 1999

Structure Diagram

($ Millions - U.S.)

USA

Australia



UCU Acquisition Funding

L.T. Debt	$ 75 m
UCU Equity issuance	50 m
Total	$ 125 m

* *Exchange Ratio U$0.60 / A$1.00*

ATTACHMENT: C
- MO PSC CASE NO. GM-2000-637

Service List for
Case No. GM-2000-637
May 10, 2000

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