

MEMORANDUM

FILED

JUL 27 1999

TO: Missouri Public Service Commission Official Case File,  
Case No. EF-2000-8, Kansas City Power & Light Company

FROM: David P. Broadwater, Financial Analysis Department

SUBJECT: Staff's Recommendation for Approval of the Application of Kansas City  
Power & Light Company for Authority to enter into Interest Management  
Products

DATE: July 26, 1999

REVIEWED BY:

*R.E. Schellberg* 7-26-99  
Director - Utility Services Division / Date

*Steven D. [Signature]* 7/26/99  
General Counsel's Office / Date

By Order dated April 1, 1988 in Case No. EF-88-213, the Commission authorized the Kansas City Power & Light Company (KCPL or Applicant) to fix the interest rate on up to \$150 million of its variable rate debt by entering into interest rate "swap" and/or interest rate "cap" and/or interest rate "collar" agreements (interest rate management products). On June 20, 1989, in Case No. EF-89-229, the Commission extended the authority to enter into interest rate management products for an additional twenty-four months at an effective cost of eleven percent (11%) or less per transaction. On June 19, 1991, in Case No. EF-91-383, the Commission extended the authority to enter into interest rate management products for an additional twenty-four months at an effective cost of eleven percent (11%) or less per transaction. On June 10, 1993, in Case No. EF-93-328, the Commission extended the authority to enter into interest rate management products for an additional thirty-six months at an effective cost of ten percent (10%) or less per transaction. On June 30, 1995, in Case No. EF-95-397, the Commission extended the authority to enter into interest rate management products for an additional thirty-six months at an effective cost of ten percent (10%) or less per transaction. On July 2, 1999 KCPL filed an Application with the Commission seeking to extend its authorization an additional thirty-six months. Specifically, KCPL is seeking authority to enter into interest rate management products "[f]or a period of three additional years, . . . to have outstanding at any one time \$250 million of interest rate management products with an effective interest rate of 10% or less on fixed rate transactions and an initial interest rate of not more than 10% on variable rate transactions." This request also includes the authority to enter into all documents necessary for the above-described transactions.

The Application states that:

The Applicant's objective is to maintain a low cost of debt while managing the interest rate risk on portions of its variable rate debt. Applicant's goal is to have approximately 15% to 30% of its debt in a variable interest rate mode, depending on market conditions. Interest rate management techniques allow the Applicant to

economically manage its percentage of variable rate debt within this range. With \$30 million of interest rate management products currently in place, the percent of long-term variable rate debt to total long-term debt is about 31%.

Due to the transitory nature of interest rate management products, KCPL must be able to execute a transaction when the opportunity arises to obtain the most competitive pricing. If KCPL were required to seek regulatory approval of each transaction, the opportunity would likely be lost due to time constraints inherent in the approval process. KCPL proposes to continue to account for all payments or receipts and administrative costs incurred due to these transactions as an increase or decrease in interest expense for book purposes. The Applicant will also "... continue to notify the Commission's Office of Financial Analysis [currently referred to as the Financial Analysis Department] of terms and conditions of interest rate management products entered into and will continue to submit quarterly reports regarding the performance of such interest rate management products." Staff deems this to be acceptable.

KCPL has successfully used interest rate management products over the last ten years. According to KCPL, its average cost of long-term debt in 1998 was 5.5% down from 8.2% in 1988, when it started using interest rate management products. It should be noted that all of this reduction in interest cost is not attributable to interest rate management products. Over that same time period the interest rate on "A" rated public utility bonds has decreased from 10.06% in December of 1988 to 8.27% in December of 1998. KCPL's Application states that "it is in the public interest to manage the interest on its debt through the use of interest rate management techniques." Staff concurs with this statement, and therefore recommends that the Commission approve Kansas City Power & Light Company's Application in Case No. EF-2000-8.

The Commission should state that nothing in the order granting approval of this application shall be considered as a finding by the Commission that would preclude the right to consider the ratemaking treatment to be afforded these or any future expenditures by the Company in any later proceeding.

Copies:      Director - Utility Operations Division  
                 Director - Utility Service Division  
                 General Counsel  
                 Manager - Financial Analysis Department  
                 Manager - Procurement Analysis Department  
                 Manager - Energy Department  
                 Office of the Public Counsel