

STATE OF MISSOURI
PUBLIC SERVICE COMMISSION

At a Session of the Public Service
Commission held at its office
in Jefferson City on the 31st
day of May, 1991.

In the matter of the application of The Kansas)
Power and Light Company, a Kansas corporation,) CASE NO. GF-91-374
for authority to issue and sell additional)
Preference Stock.)

ORDER AUTHORIZING SALE OF PREFERENCE STOCK

By an application filed May 16, 1991, The Kansas Power and Light Company (KPL) seeks permission to issue in one or more public offerings, up to 1,500,000 shares of Preference Stock without par value for a cash price of \$100 per share. The transmittal letter accompanying the application asks that the Commission consider this filing and act upon it by May 22, 1991, or as soon as possible thereafter. The transmittal letter also states the Applicant believes that the Commission may act on the verified application and recommendation of the Commission Staff without a hearing.

The Commission, upon consideration of the verified application, the exhibits offered in support thereof, and the recommendation of its Staff, is of the opinion that a hearing is unnecessary to resolve the issues herein and finds and concludes as follows:

KPL is a corporation organized and existing under the laws of the State of Kansas with its principal office and place of business at 818 Kansas Avenue, Topeka, Kansas 66601. Its principal office in Missouri is located at 2460 Pershing Road, Kansas City, Missouri 64108, at which it does business as KPL Gas Service in the provision of natural gas service to approximately 400,000 customers in the State of Missouri. KPL is a gas utility subject to the jurisdiction, supervision, and control

of this Commission pursuant to Chapters 386 and 393, RSMo, 1986. The Commission's approval of the issuance contemplated by this application is required by Section 393.180 and 393.200, RSMo, 1986.

At March 31, 1991, KPL's capital structure consisted of common stock equity in the amount of \$641,252,000 (45.48 percent), preferred stock in the amount of \$31,491,000 (2.23 percent), long-term debt of \$612,240,000 (43.43 percent), and short-term debt in the amount of \$124,845,000 (8.86 percent).

KPL proposes to add the proceeds of the sale to its general funds to be used to repay short-term indebtedness, refinance certain long-term indebtedness, and reimburse the treasury of the Company for construction costs incurred within the past five years.

KPL proposes to issue and sell one or more series of Preference Stock, each with a maturity date of not less than 10 years nor more than 30 years, and an effective annual cost not to exceed 150 basis points above the yield on United States Treasury Securities of 30 years maturity as quoted in the actively traded secondary market on the date of the underwriting agreement relating to each series of stock. In no event will the Underwriter's commission for any series of stock exceed 7/8 of 1 percent of the principal amount of each series. The proposed stock is subject to a sinking fund which will vary according to the final maturity of each series.

After soliciting additional information from KPL the Commission Staff, on May 29, 1991, filed its recommendation of denial of the instant application. In the alternative, the Staff suggests an approval of the application with certain reservations.

The Staff has conducted extensive evaluations of the Company's financial condition both actual and pro forma. In addition, the Staff has analyzed market conditions and current security offerings of various types, including those similar to the issue herein contemplated.

One area of concern expressed by the Staff is the need for the issuance of permanent financing. KPL's current unsecured debt balance is approximately \$163 million. The Company currently has credit lines of \$185 million. Although the Staff indicates that the issuance of any form of permanent capital will increase KPL's revenue requirement, it is the Staff's opinion that the Company must issue permanent capital in the near future to maintain its credit profile and not exceed its unsecured debt limitations. Staff's primary concern is keeping the Company's pre-tax cost of capital as low as possible.

In attempting to arrive at an opinion as to whether or not earnings of KPL will support the issuance of the Preference Stock a number of evaluations of after-tax coverage of interest and preferred dividends were performed. It is the Staff's opinion that the proposed issuance would reduce KPL's after-tax coverage of interest and preferred dividends from 2.24 times to 2.05 times and the pre-tax interest coverage ratio would improve from 2.85 times to 3.33 times. It is therefore the Staff's opinion that KPL's earnings are adequate to cover both interest expense and anticipated dividends on the proposed issue.

A study of recent similar issues by other utility companies indicates the range for the cost to be 7.9 to 10.1 percent. Therefore, the Staff is of the opinion that the proposed rate of 9.0 percent is reasonable.

The final concern of the Commission Staff was the comparison between the effects on KPL's pre-tax cost of capital by issuing Preference Stock as opposed to long-term debt. As a result of a number of analyses the Staff indicates that the contemplated issue would increase KPL's pre-tax cost of capital from 13.69 percent to 14.22 percent. Based on its entire analysis, the Staff is of the opinion that issuance of Preference Stock rather than long-term debt will result in a 32 basis point increase in the Company's cost of capital. It is the Staff's opinion that KPL desires to issue Preference Stock rather than long-term debt so that the Company can

maintain its AA bond rating since the Company expects its bond rating to be down-graded if its contemplated merger with Kansas Gas and Electric is approved. The Staff is of the opinion that the potential spread of 32 basis points is substantially material, and if the choice of financing is approved by the Commission, the results should be considered in the Company's pending rate case. Staff has multiplied the 32 basis point differential by KPL's jurisdictional rate base filed in its pending rate Case No. GR-91-291. It is the Staff's opinion that the issuance of Preference Stock will increase KPL's revenue requirement by \$639,102. That amount would be in addition to the \$20 million increase sought by the Company's rate case filing.

On being apprised of the Staff's position, KPL on May 29, 1991, recommended to the Commission that it approve the issuance with the condition that any ratemaking treatment to be afforded the financing transaction, including its resulting effect on the Company's cost of capital, be deferred until a later proceeding wherein the potential recovery of such costs is at issue. The Company's request states that it will not in any manner argue that the Commission's approval of this issuance precludes any party from recommending, or the Commission from adopting, a particular ratemaking treatment for the cost associated with this transaction. The Company's supplemental request expresses the view that such approach would reasonably balance the Company's desire to take advantage of what it believes are appropriate and favorable financing opportunities, with the Staff's desire to protect customers from any detrimental effects.

On May 30, 1991, the Company filed its Response To Staff Recommendation in which it reinforced its concerns expressed in its previous response by letter.

In the opinion of the Commission, the funds to be procured from the proposed financing are reasonably required for the purposes specified and those purposes are not, in whole or in part, reasonably chargeable to operating expenses or to income. We are of the opinion, however, that, we are unable to find that the

instant issuance is in the public interest or that it is not detrimental to the public interest. Having no desire to substitute our judgment for that of the Company's management, we are of the opinion that the instant application should be approved with the reservations suggested by both the Company and the Staff. The Staff's analysis and position in this matter will be considered in KPL's pending rate Case No. GR-91-291.

IT IS THEREFORE ORDERED:

1. That subject to the reservations herein expressed, The Kansas Power and Light Company be authorized to issue and sell up to 1,500,000 shares of Preference Stock on the terms and subject to the limitations recited in its application filed herein on May 16, 1991.

2. That the proceeds to be received by The Kansas Power and Light Company from the sale and issuance of the new stock shall be used for the purposes recited and only for such purposes, however, The Kansas Power and Light Company is hereby authorized to pay out of the gross proceeds from the sale of the new stocks its reasonable expenses incurred in connection with the issue and sale thereof.

3. That The Kansas Power and Light Company be authorized to execute any and all documents and agreements necessary to execute the authority herein granted.

4. That nothing in this Order shall be considered as a finding by the Commission of the reasonableness of the expenditures herein involved, or of the value for ratemaking purposes of the properties herein involved, nor as an acquiescence in the value placed upon said properties by the Applicant. Furthermore, the Commission reserves the right to consider the ratemaking treatment to be afforded these transactions, the resulting cost of capital, and any proper adjustment to the cost of capital resulting therefrom, in the Company's pending rate Case No. GR-91-291.

5. That this Order shall become effective on the date hereof.

BY THE COMMISSION

Brent Stewart

Brent Stewart
Executive Secretary

(S E A L)

Mueller, Rauch, McClure,
and Perkins, CC., Concur.
Steinmeier, Chm., Absent.