BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

In the Matter of a Proposed Experimental Regulatory Plan of Kansas City Power & Light Company	))	Case No. EO-2005-0329

STAFF SUGGESTIONS IN SUPPORT OF STIPULATION AND AGREEMENT

Comes now the Staff of the Missouri Public Service Commission (Staff) in support of the Stipulation And Agreement (Agreement)[1] filed on March 28, 2005 establishing the instant case, Case No. EO-2005-0329, regarding principally, but not solely, the construction by Kansas City Power & Light Company (KCPL) of an 800-900 MW coal-fired baseload unit at Weston, Missouri, referred to as "Iatan 2," with a projected in-service date of June 1, 2010, at the site of the present Iatan baseload generating station and the coal-fired baseload generating unit referred to as "Iatan 1."[2] The Staff, although not the initiator of the filing that led to the Agreement, participated fully in the process that led to the filing of the Agreement and is a Signatory Party thereto. The Staff believes that approval of the Agreement and a faithful implementation of its terms will result in the provision of safe and adequate electric service at just and reasonable rates by KCPL.

On April 27, 2005, before the Kansas Corporation Commission (KCC), a Stipulation And Agreement among, and a Joint Motion To Approve Stipulation And Agreement of, KCPL, the Staff of the KCC (KCC Staff) and Sprint and the Kansas Hospital Association, was filed respecting a regulatory plan for the construction of Iatan 2, in particular. On April 28, 2005,

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[1] Attachment 1 to the Staff's Suggestions In Support is an Index to the Agreement filed on March 28, 2005.

[2] Iatan 1 went into commercial operation in 1980. Iatan 1 is jointly owned by The Empire District Electric Company (12%), Aquila, Inc. (18%) and KCPL (70%). KCPL is the majority owner and managing partner. *See Re Kansas City Power & Light Co.*, Case No. ER-80-48, Report And Order, 23 Mo.P.S.C.(N.S.) 474 (1980).

KCPL made an informational filing in the instant proceeding of that Stipulation And Agreement and Joint Motion To Approve Stipulation And Agreement.

The Agreement filed on March 28, 2005 establishing the instant proceeding states, in part, in Paragraph "III.B.6. Agreement Conditioned On Regulatory Plan Approval By Kansas Corporation Commission" that the Signatory Parties' approval of KCPL's Missouri Regulatory Plan is conditioned upon (1) KCC approval of a Regulatory Plan (otherwise referred to as the Stipulation And Agreement before the KCC), and (2) the terms of the Regulatory Plan approved by the KCC being substantially similar to the terms of the Regulatory Plan agreed to by the Signatory Parties in Missouri and approved in Missouri by this Commission.

Paragraph III.B.6. further provides that the non-KCPL Signatory Parties in Missouri will have seven (7) days, from the filing with this Commission of a Kansas Regulatory Plan approved by the KCC, to advise this Commission whether the non-KCPL Signatory Parties still support approval of the Regulatory Plan agreed upon in Missouri. In addition, Paragraph III.B.6. states that if the terms of the Regulatory Plan agreed upon before the KCC and/or required by the KCC are not comparable to the Regulatory Plan agreed upon in Missouri and/or required by this Commission, KCPL will offer to the other Signatory Parties in Missouri, and accept for its Missouri jurisdictional operations, comparable terms to those terms agreed upon in Kansas and/or required by the KCC.

The Staff identifies in Attachment 2 the differences that it has been able to note between the Agreement reached in Missouri and the Stipulation And Agreement reached in Kansas. There is one very material difference between the two documents respecting which the Staff chooses the provision negotiated in Kansas rather than the provision in the Missouri Agreement. Although in Missouri KCPL agreed to a 125 basis point reduction to the equity portion of the

allowance for funds used during construction rate (AFUDC), in Kansas KCPL agreed to a 250 basis point reduction to the equity portion of the AFUDC rate. This difference appears in Attachment 2 along with the other differences that the Staff has been able to identify between the Regulatory Plan agreed to in Missouri and the Regulatory Plan agreed to in Kansas. The Staff would note that the Office of Public Counsel (Public Counsel) is a signatory to the Agreement in Missouri, but the Citizens Utility Ratepayers Board (CURB in Kansas is the counterpart to the Public Counsel in Missouri) is not a signatory to the Stipulation And Agreement in Kansas. The Staff will seek to amend the Regulatory Plan in Missouri to reflect the term agreed upon in Kansas.

Paragraph III.B.11.c. of the Agreement provides that the Staff shall file suggestions or a memorandum in support of the Agreement the other Signatory Parties shall have the right to file responsive suggestions or prepared testimony. No time is set for responses to the Staff's Suggestions In Support, and in addition to there being other Signatory Parties there is at least one intervenor that is objecting to the Agreement. The Staff assumes that pursuant to 4 CSR 240-2.080(15) all have ten (10) days to respond to the Staff's Suggestions in Support.

It is not the intent of the instant Staff Suggestions In Support to attempt to address every facet of the Agreement. The Staff has attempted to anticipate questions that the Commissioners may have and provide this pleading in a timely manner. In support of the Agreement, the Staff states as follows:

I. Necessity For Additional Proceedings

Given the "Wherefore" language of the Agreement, it seems appropriate to begin with the end, i.e., the last sentence of the Agreement: "Wherefore, the Signatory Parties respectfully request that the Commission approve the Agreement to be effective May 15, 2005, if possible."

A May 15, 2005 effective date is not possible, and was not likely even on the date that the Agreement was filed given: (a) the need for an intervention period, (b) the desire of the Public Counsel for local public hearings, (c) the indication from the Concerned Citizens of Platte County (CCPC) and the Sierra Club that they opposed the Agreement, (d) the contingency that a complementary regulatory plan be adopted in Kansas by the Kansas Corporation Commission (KCC) and (e) the requirement in the Agreement that any provision or term in a complementary stipulation and agreement in Kansas may be adopted by the Signatory Parties and the Commission in Missouri.

The Commission set an intervention period ending April 19, 2005. The Public Counsel on April 1, 2005 and the Concerned Citizens of Platte County, Inc. (CCPC) and the Sierra Club on April 7, 2005 made filings requesting that the Commission schedule local public hearings. Public Counsel stated, in part, as follows:

> 2. . . . Public Counsel believes that it would serve the public interest for the Commission to hold two or three public hearings at convenient times and places within KCPL's service territory, allowing members of the public to comment on the proposed Regulatory Plan and to raise any issue relating to KCPL which they may believe the Commission should address in this case.
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> 3. Furthermore, Public Counsel believes that such local public hearings should be scheduled early enough to allow Public Counsel (and other interested parties) sufficient time to review the transcript of those hearings and prepare responses to the public testimony prior to any Commission action on the proposed Agreement.

The CCPC and the Sierra Club also on April 7, 2005 filed Objections to the Agreement and on April 19, 2005 filed a request for the setting of evidentiary hearings.[3]

[3] On April 4, 2005, Jackson County, Missouri (Jackson County) filed Objection Of Jackson County, Missouri To Stipulation And Agreement in which it states that because Jackson County is shown on the signature page and is referred to as a Signatory Party in the first paragraph of the Agreement, it is concerned that if it did not file its objection, the Agreement would be considered unanimous and Jackson County would have waived any right to a hearing. Thus, Jackson County filed its Objection on April 4, 2005. Whereas CCPC and Sierra Club have always made their opposition and the basis of their opposition to the construction of Iatan 2 clear, the Staff is not aware of the basis of Jackson County's opposition to the Agreement.

On April 19, 2005, the United States Department of Energy (USDOE) filed an Application To Intervene in which it stated, among other things, as follows:

> 11. . . . USDOE objects to the approach taken in the Stipulation and Agreement whereby KCPL requests its customers to agree, that in future cases, they will not take positions that investments in certain infrastructure additions or improvements should be excluded from rate base on the grounds that the projects were not necessary or timely, or that alternative fuels should have been used by KCPL. USDOE is opposed to customers being requested to pre-approve specific public utility investments as being prudent and used and useful. Such a request may be contrary to Missouri's "File and Suspend" law for fixing fair and reasonable rates. USDOE submits that it is the obligation of KCPL to continually monitor its investments to assure that when KCPL requests that these investments be included in rate base they remain both prudent and used and useful to prove by competent and substantial evidence that they are in the public interest.

The Staff addresses below in the section "IX. Preapproval" the objections raised by USDOE.

The Staff notes that the Commission generally schedules local public hearings to provide the opportunity for the public to appear before the Commission in addition to, not in lieu of, formal evidentiary hearings or other due process that the Commission provides as a matter of law to petitioners, intervenors and parties as a matter of right. Local public hearings are not akin to the evidentiary hearings that the Western District Court of Appeals found necessary in *State ex rel. Fischer v. Public Serv. Comm'n*, 645 S.W.2d 39 (Mo.App. 1982), when the Commission in considering objections to a stipulation and agreement, unlawfully limited the proceedings that it accorded the objecting party.

On April 11, 2005, KCPL filed the prepared direct testimony of the following KCPL witnesses on the following topics: Chris B. Giles - Policy; Michael W. Cline - Financial Modeling; Lori A. Wright - Accounting; John R. Grimwade - Integrated Resource Planning;

(*footnote continued*)

The City of Kansas City, Missouri (Kansas City) is also shown on the signature page and is referred to as a Signatory Party in the first paragraph of the Agreement based upon representations made by KCPL. Kansas City has yet to execute the Agreement, and the Staff is not aware whether Kansas City will do so.

Susan K. Nathan - Demand Response, Affordability and Efficiency Programs; William P. Herdegan - Distribution; and Wm. Edward Blunk - SO_2 Management.

The Commission on April 21, 2005 scheduled a prehearing conference for Tuesday, May 3, 2005 and set May 10, 2005 as the date by which the parties are to file a procedural schedule(s). The prehearing conference occurred on May 3, 2005 and the parties in attendance scheduled a conference call for May 4, 2005. The conference call occurred on May 4, 2005 and the parties in attendance advised the Regulatory Law Judge assigned to the case that they had reached agreement on a procedural schedule. On May 6, 2005, the Regulatory Law Judge issued by delegation of authority an Order Establishing Procedural Schedule in which it set local public hearings for May 24, 2005 and evidentiary hearings for June 6-8, 2005.

II. Necessity For Additional Filing: KCPL Financing Plan For Construction Of Iatan 2

KCPL will need to issue debt securities as a result of significant investment in its infrastructure including the construction of Iatan 2. Also KCPL will refinance all of a portion of debt securities scheduled to mature during the Regulatory Plan. KCPL will seek Commission approval of its financing plan so that it will not be required to file with the Commission for approval each time that it issues new debt securities or refinances debt securities. The debt securities may be senior or subordinated and may be issued as unsecured or secured in conjunction with the debt securities, KCPL will also enter into interest rate hedging instruments. Appendix B to the Agreement filed on March 28, 2005, is the long-term financial plan that KCPL provided to the Signatory Parties. KCPL will make a filing with the Commission in the near future seeking Commission authorization to engage in all of these issuances.

III. Unrefuted Need For Iatan 2

In the long months engaged in Case No. EO-2004-0577 and Case No. EW-2004-0596, no participant credibly demonstrated that baseload capacity will not be needed by approximately 2010 to serve the retail customers of investor owned utilities in Western Missouri. Furthermore, it was not shown that coal-fired generation is not the most economic alternative available to meet this need.

Prior to the suspension in 1999 of the Commission's Electric Resource Planning rules, Chapter 22, 4 CSR 240-22, each investor owned electric utility was required to file its resource planning and analysis with the Commission every three-years pursuant to Chapter 22. In 1999, certain of these electric utilities proposed the rescission of Chapter 22, but in lieu of the proposed rescission of Chapter 22, each investor owned electric utility agreed to meet semiannually with the Staff, Public Counsel and others to address their resource planning activities since their last semiannual integrated resource planning (IRP) meeting. The Staff, in making its determination regarding the need for additional baseload capacity for investor owned utilities in Western Missouri, has relied on the analysis performed by KCPL, Aquila, Inc. (Aquila) and The Empire District Electric Company (Empire).

In addition to information presented in KCPL's semiannual IRP meetings, the Staff reviewed, in the workshop process of Case No EW-2004-0596, KCPL's resource planning process and decisional analysis whereby it decide to construct Iatan 2 to meet its baseload capacity needs. The Staff submitted data requests to KCPL, and reviewed KCPL's responses. Besides meeting with KCPL in Jefferson City, the Staff met with KCPL at the KCPL's offices in Kansas City.

The Staff also met with CCPC in the context of Case No. EW-2004-0596 and has considered the Objections filed by CCPC and Sierra Club on April 7, 2005. The Staff notes that CCPC made a presentation in the context of Case No. EW-2004-0596 to the Staff and Public Counsel on November 23, 2004.[4] The same presentation was made to the Commissioners earlier the same day.

Had Chapter 22 not been suspended, the Staff would have been in a much better position to determine KCPL's need for additional baseload capacity and its choice of Iatan 2 to meet that need. In the context of Case No. EW-2004-0596, KCPL provided to the Staff detailed analysis that it did not provide in the semiannual IRP meetings. But even in Case No. EW-2004-0596, the information was not volunteered. Information and in particular supporting documents were provided only if and after participants requested it. Prior to the suspension of Chapter 22, detailed analysis, documents and workpapers were provided to the Staff at the beginning of the process.

The suspension period agreed to in Case No. EO-99-365 for the Commission's Chapter 22 resource planning rules for each electrical corporation has ended, or is about to end. As a consequence, each electrical corporation is required by Chapter 22 to file consistent with the

[4] The last two slides of the CCPC presentation state as follows:

> In Conclusion
> - Using technology to reduce our energy demands makes common sense.
> - It saves consumers and businesses money with reduced energy and healthcare costs, creating jobs and protecting our health and water supply.
> - Please do a complete analysis to determine whether efficiency and renewables can meet our energy needs without building additional coal burning power plants.
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> What we want from the MO PSC
> We urge you to create a rate structure for KCPL that rewards them with the *highest possible rate of return* on investments in efficiency and renewables;
> and a structure that gives them NO RETURN on building a new coal-burning power plant.

The web site of CCPC is www.TELLKCPLNO.org.

requirements of Chapter 22, commencing with (a) AmerenUE by December 5, 2005, followed by (b) KCPL by July 5, 2006, (c) Aquila Networks – MPS division by February 5, 2007, (d) Empire by September 5, 2007 and (e) Aquila Networks – L&P[5] division by April 7, 2008. As a result of the Commissioners' determinations respecting the Surveillance Reporting And Generic Policy Rulemaking Workgroup of the Case Management Efficiency Roundtable, a resource planning workshop has been scheduled for May 20, 2005 to review the Chapter 22 rules for resource planning for electrical corporations and to address whether the Commission should adopt resource planning rules for gas corporations.

IV. Staff Earnings Audit Of KCPL

In the past, it has been customary for the Staff to perform an abbreviated and limited financial audit of a utility when a rate moratorium ends, a utility seeks the initiation of an alternative form of regulation, a utility files with the Commission for approval of a very significant event, such as a merger, or financial surveillance information or other analysis causes the Commission or the Staff to believe the utility is earning substantially in excess of its last authorized rate of return or a rate of return that reflects current market conditions and Commission ratemaking decisions. Thus, when the Commission established Case No. EW-2004-0596, the Staff commenced an abbreviated and limited financial audit of KCPL. The results of the Staff's audit and recent Commission decisions on rate of return and interim net salvage were reflected in the Staff's abbreviated and limited audit, and discussions with KCPL and the other participants in Case No. EW-2004-0596.

One Commissioner, several years ago at an on-the-record presentation respecting a regulatory plan that included a rate reduction, asked if the Staff had left any money on the table

[5] At the present, it is not clear whether Aquila will seek to comply with Chapter 22 on a basis treating its two Missouri utility operating divisions on separate or combined schedules.

in its negotiations with the utility. Counsel for the Staff explained that it is the Staff's practice to leave money on the table because the Staff does not want to drive so hard a bargain that an unforeseen, but reasonable, change in events could drive the utility into a need for a rate increase case. Similar thinking on the part of the Staff causes it to never file a rate reduction case when a utility is only marginally earning in excess of a reasonable rate of return.

The results of a financial audit can be reflected in ways other than by an increase or a decrease in the existing rates charged customers. As previously noted, the Staff performed an abbreviated and limited financial audit of KCPL. The results of the Staff's audit are reflected in the terms of the Agreement. Although there is to be no change in current rate levels through December 31, 2006, as a result of the Staff's limited financial audit, there is to be a continuation of a current amortization, which was adopted as a result of a previous Staff financial audit, and the commencement of a second amortization, and both amortizations are to be used as an offset to rate base in future rate proceedings of KCPL or its successors. Both of these amortizations are to continue only until the January 1, 2007 effective date of the tariffs resulting from Rate Filing #1, per Paragraph III.B.3.a of this Agreement. (Rate Filing #1 is to be filed by KCPL on February 1, 2006.) These two amortizations are as follows:

A. Continuation of the $3.5 million annual amortization expense authorized in *Re Customer Class Cost of Service and Comprehensive Rate Design Investigation of Kansas City Power & Light Company*, Order Approving Stipulation and Agreement, Case No. EO-94-199, 5 Mo.P.S.C.3d 76 (1996) which has remained in effect since July 3, 1996[6]; and

B. Commencement of $10.3 million amortization expense, beginning with the effective date of the instant Agreement, equal to the change in depreciation expense reflecting

[6] Paragraph 1.C. of the Stipulation And Agreement in Case No. EO-94-199, states in relevant part as follows:

> . . . Furthermore, KCPL will book an amortization totaling $3.5 million annually upon approval of this Stipulation and Agreement, which amortization shall continue until the Commission approves a change either: (1) upon agreement of the parties made with due regard to KCPL's then-existing earnings situation, or (2) in the course of a general rate proceeding. . . .

a change in service life span of the Wolf Creek Nuclear Generating Station from 40 to 60 years provided for in Paragraph III.A.3.n of the Agreement.[7]

As indicated, these two amortizations end with the change in rates effectuated by Rate Filing #1. The change in rates to be effectuated by Rate Filing #1 will occur as a result of a rate case filing by KCPL and a financial audit by the Staff.

It should be noted that the instant Agreement provides for a new amortization totaling $17 million to commence with the effective date of the rates resulting from Rate Filing #1 and a decrease of 1.25% or 125 basis points in the equity portion of the AFUDC[8] rate applicable to

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[7] Upon the effective date of the instant Agreement, KCPL will begin recording depreciation expense for Wolf Creek based on a 60-year life span. Whereas KCPL has recorded depreciation expense for its Missouri retail jurisdiction (*footnote continued*)

based on a 40-year life span, KCPL records depreciation expense before the KCC based on a 60-year life span. KCPL Controller Lori A. Wright in her direct testimony filed on April 11, 2005 at pages 5-6 states, in part, as follows:

> The Wolf Creek Nuclear Operating Corporation ("WCNOC"), the operating agent for Wolf Creek, anticipates seeking and obtaining a 20-year extension of its license for Wolf Creek. . . .
>
> . . . .
>
> . . . WCNOC informed the NRC that WCNOC intends to submit its license renewal application in September 2006. Additionally, KCPL began using Kansas jurisdictional depreciation rates for Wolf Creek based on a 60-year useful life effective January 2003 based on an Order received from the Kansas Corporation Commission ("KCC") in Case No. 02-KCPE-840-RTS.
>
> . . . .
>
> The rates shown in Appendix G for the various nuclear plant accounts are the same as the Kansas jurisdictional nuclear depreciation rates authorized in KCC Case No. 02-KCPE-840-RTS, which, as explained, also adopted a 60-year useful life for depreciation.

[8] AFUDC is an accounting convention used to capitalize the financing costs of construction until the construction is in commercial operation or commercial use so that ratepayers do not pay for the cost of construction until the plant is "fully operational and used for service." Once the construction is fully operational and used for service, the capitalized financing cost is included in rate base and the utility earns a return of and return on the investment.

The Western District Court of Appeals explained the procedure required under Section 393.135 in a Southwestern Bell Telephone Company case decision:

> With respect to general CWIP, two different approaches are taken by the courts. One widely used approach is to completely exclude the present cost of CWIP from the rate base, on the ground that rate payers receive no benefit from a new plant or facility until it is placed in service. *E.g., Bell Tel. Co. v. Public Utility Com'n.*, 47 Pa.Cmwlth. 614, 408 A.2d 917, 925-26 (Pa.Commw.1979); *State ex rel. Utilities Commission v. Morgan*, 277 N.C. 255, 177 S.E.2d 405, 416-17 (N.C.1970); *Gulf States Utilities Co. v. Louisiana, etc.*, 364 So.2d 1266, 1269-71 (La.1978). To avoid working an injustice to the utility or

Iatan 2. The $17 million amortization also is a component of Rate Filing #2 and Rate Filing #3, but it is not a component of Rate Filing #4. This $17 million amortization may be adjusted as specified in Paragraph III.B.1.i which is the section on Additional Amortizations To Maintain Financial Ratios. The decrease of 1.25% or 125 basis points in the equity portion of the AFUDC rate applicable to Iatan 2 is to continue for the entire period that Iatan 2 is accruing AFUDC.

V. Agreement Neither Violates The Prohibition Of Section 393.135 RSMo. 2000 Against AFUDC In Rate Base Nor The Prohibition Of *UCCM* Against Single-Issue Ratemaking

Simply put, the Agreement neither violates the prohibition of Section 393.135 RSMo. 2000 against placing in rate base funds for construction of plant before the plant is "fully operational and used for service" nor the *State ex rel. Utility Consumers Council of Missouri, Inc. v. Public Serv. Comm'n*, 585 S.W.2d 41 (Mo. banc 1979) (hereinafter referred to as *UCCM*)[9] prohibition against single-issue ratemaking.[10] (In other states, the Section 393.135 prohibition is referred to as the principle of not recovering in rates the cost of construction of plant before the plant is "used and useful.")

(*footnote continued*)

> its investors under this approach, the utility is allowed to capitalize interest accrued in the cost of capital and construction and thus recover through depreciation its capital expenditures from future rate payers once the plant is dedicated to public service. *New Eng. T. & T. Co. v. Public Utilities Commission,* 116 R.I. 356, 358 A.2d 1, 19 (R.I.1976). This approach is dictated by statute in Missouri, but only with respect to electric utilities. Section 393.135 (Initiative Proposition No. 1).

State ex rel. Southwestern Bell Telephone Co. v. Public Serv. Comm'n, 645 S.W.2d 44, 52-53 (Mo.App. 1982)

[9] The Missouri Supreme Court's 1979 decision in *UCCM* respecting electric fuel adjustment clauses should not be confused with an earlier St. Louis District Court of Appeals decision styled *State ex rel. Utility Consumers Council of Missouri, Inc. v. Public Serv. Comm'n*, 562 S.W.2d 688 (Mo.App. 1978) or a later decision of the Western District Court of Appeals styled *State ex rel. Utility Consumers Council of Missouri, Inc. v. Public Serv. Comm'n*, 606 S.W.2d 222 (Mo.App. 1980). The earlier *UCCM* decision is frequently cited, in part, for the principle that a utility need not apply for authority to construct plant in an area for which it has a certificate of convenience and necessity to provide utility service, 562 S.W.2d at 690. The later *UCCM* decision involves, in part, a Section 393.135 issue and is addressed below in this section of the Staff's Suggestions In Support.

[10] A new factor that needs to be reflected in any analysis of an assertion that a matter/item is in violation of the prohibition against single-issue ratemaking is the prospective signing into law of Senate Bill 179 which at a minimum makes certain single-issue ratemaking lawful.

The phrase "fully operational and used for service" is found in Section 393.135 and it should be noted that the phrase as used in Section 393.135 applies only to any charge made or demanded by an electrical corporation:

> Any **charge made or demanded by an electrical corporation** for service, or in connection therewith, which is based on the costs of construction in progress upon any existing or new facility of the electrical corporation, or any other cost associated with owning, operating, maintaining, or financing any property before it is **fully operational and used for service**, is unjust and unreasonable, and is prohibited.

As will be discussed herein, any assertion that the Signatory Parties have agreed in the KCPL Regulatory Plan to violations of Section 393.135 displays a fundamental misunderstanding of Section 393.135. What KCPL originally proposed in discussions with the participants in the workshops in Case No. EW-2004-0596 would have been a violation of Section 393.135. KCPL's efforts to argue that the Commission in respect to the construction of Iatan 2 could approve a regulatory plan involving predetermined rate increases that would be permitted to go into effect without a financial audit by the Staff or Public counsel were rejected by the Staff and other participants as being unlawful. The Staff and various of the other participants made it clear that they would not agree to a regulatory plan in violation of Section 393.135. The Signatory Parties have agreed to KCPL filing rate cases as part of the Agreement. KCPL does not need the Signatory Parties agreement to file these rate cases.

A further indication that the Agreement does not violate Section 393.135 is that the Signatory Parties have agreed to the in-service criteria that will be utilized to determine whether Iatan 2 is "fully operational and used for service" before KCPL can recover in rates the costs of construction of Iatan 2. Iatan must meet the criteria in Appendix H to the Agreement for a coal plant in order to be placed in rate base.

Furthermore, the Signatory Parties have agreed to construction accounting for Iatan 2 between the time that it becomes fully operational and used for service and the time that recovery of costs is reflected in rates. Due to Section 393.135 barring construction work in progress (CWIP) being placed in ratebase, or otherwise being recovered in rates, electrical corporations in Missouri try to synchronize the in-service date of power plants with the operation-of-law date of the first rate case where they seek rate recovery of the costs of the unit.

Contrary to *UCCM,* KCPL initially suggested to the participants that it be authorized to increase rates based on its costs of constructing Iatan 2 to the exclusion of the consideration of all other factors. *UCCM*, among other things, provides that the Commission, pursuant to Section 393.270.4 RSMo. must consider all relevant factors in determining whether to approve an increase in rates. (Another principle for which *UCCM* is cited is that in determining whether or not to permit a proposed rate to go into effect without suspension and a hearing, the Commission must still consider all factors relevant to the proper maximum price to be charged. 585 S.W.2d at 49.)

There is a dearth of court cases on Section 393.135. A review of the few cases that exist may be of some benefit: *State ex rel. Utility Consumers Council of Missouri, Inc. v. Public Serv. Comm'n*, 606 S.W.2d 222 (Mo.App. 1980); *State ex rel. Missouri Pub. Serv. Co. v. Public Serv. Comm'n*, 627 S.W.2d 882 (Mo.App. 1981); *State ex rel. Union Electric Co. v. Public Serv. Comm'n*, 687 S.W.2d 162 (Mo. banc 1985); and *State ex rel. Union Electric Co. v. Public Serv. Comm'n*, 765 S.W.2d 618 (Mo.App. 1988). The Section 393.135 issues in the first two cases principally involved tax timing difference issues and the last two cases involved UE's requested

recovery of the cancellation costs of the abandoned second generating unit at the Callaway nuclear generating station, referred to herein as Callaway II.[11]

The last in chronology of the three *UCCM* cases, 606 S.W.2d 222, involved in relevant part interest, property taxes, pensions and other costs charged to construction, which would be capitalized for ratemaking recovery purposes, but for then current income tax purposes would be deducted from income, resulting in a then current reduction of income taxes. Interest, property taxes, pensions and other costs charged to construction would be added to the cost of the production facilities. These construction expenses and the income tax savings would be amortized over the life of the facilities beginning when the facilities are placed in service. The court stated: "Sec. 393.135, RSMo 1978, prohibits the company from earning any return upon facilities before they are actually placed in service." 606 S.W.2d at 226. Under the tax "normalization" method approved by the Commission, the income tax savings resulting from the current deduction of these expenses were not "flowed through" to ratepayers concurrently. *Id.* (Stated another way flow through treatment requires the utility to charge, as an operating expense and recover in rates from customers, only the amount of taxes actually paid to the

[11] Respecting the cancellation of Callaway II, the Commission first disallowed recovery of the partial construction and cancellation costs of the abandoned Callaway II unit on the basis that the terms of Proposition One, Section 393.135, precluded the Commission from allowing recovery of any amount from ratepayers relating to abandoned construction. In the first appellate court decision respecting UE's effort to recover in rates the costs associated with the abandoned Callaway II unit, the Missouri Supreme Court held that Proposition One, Section 393.135, did not have the purpose and did not have the effect, of divesting the Commission of the authority to make any allowance for the costs of abandoned generating plant construction. The Court based its conclusion "the established practice of allowing such charges, absent a statutory command to the contrary, and on the absence from Proposition One of explicit language dealing with abandoned construction." 687 S.W.2d at 168.

The case was remanded to the Commission for further proceedings. After further proceedings on the remanded issues, the Commission again rejected recovery in rates of the construction and cancellation costs of Callaway II. The Commission held that UE's shareholders had already been compensated for some of their loss through the rates of return in prior UE cases. 765 S.W.2d at 621. Among other things, the Commission determined that UE shareholders had received some compensation for the risk of their investment in UE which included a risk of cancellation of Callaway II. The Court found that the Commission's decision was within the Commission's discretion and was supported by competent and substantial evidence. *Id.* at 623-24.

Internal Revenue Service (IRS), whereas normalization treatment allows the utility to charge, as an operating expense and recover in rates from customers, the amount of taxes which it would have been required to pay to the IRS had it not taken advantage of the accounting practices which allow it to reduce the amount of taxes it pays in the earlier years of payment, but ultimately require it to make up in its payments to the IRS in the later years of payment.)

The Court held that (1) the Commission's order approving normalization of income taxes for construction expenses was supported by good and valid reasons, (2) UCCM had not demonstrated that the Commission's order regarding this matter was unlawful or unreasonable and (3) the Commission's order regarding this matter was within the zone of allowable discretion which is not to be disturbed upon judicial review. 606 S.W.2d at 227.

The *Missouri Pub. Serv. Co.* case, involved several issues, two of which, (a) the flow through, instead of normalizing, certain income tax timing differences and (b) the exclusion from rate base of compensating bank balances, the Western District Court of Appeals found related to Section 393.135, and one of which, (c) the inclusion in rate base of only 25% of the cost of constructing the generating facilities "common facilities," the Western District Court of Appeals found unrelated to Section 393.135.[12] The Commission filed a Motion To Dismiss with the Western District Court of Appeals on the grounds of mootness because the tariffs at issue had been superseded by subsequent tariffs and thus the reviewing court could not give any relief because any error which may have been made could not be corrected retroactively or prospectively because the tariffs at issue on appeal had been replaced by subsequent tariffs filed and approved. An exception may be made by the court where an issue presented is of a recurring nature, is of general public interest and importance and will evade appellate review unless the

[12] The court in the context of the attrition issue noted that a future or projected test year, instead of an historical test year "would not be available in Missouri because of the adoption by popular vote of Initiative Proposition 1, now Section 393.135." 627 S.W.2d at 888.

court exercises its discretionary jurisdiction. The court held that some of the issues on appeal fit into the exception to the mootness rule and others did not. 627 S.W.2d at 884-85.

Taking the normalization versus flow through issue first, the Commission allowed normalization treatment of tax credit, accelerated depreciation, amortization of extraordinary purchased power costs and various quick turn around items, but ordered flow through treatment of funds used during construction, pensions and taxes capitalized, Jeffrey Energy Trust deduction and removal costs. The Court in *Missouri Pub. Serv. Co.* case noted that the problem of normalization versus flow through treatment was discussed in *State ex rel. Utility Consumers Council of Missouri, Inc. v. Public Serv. Comm'n*, 606 S.W.2d 222 (Mo.App. 1980) in which it was held that the choice was a matter of administrative discretion. The Court stated:

> . . . The Commission has adopted the policy that "cash flow, interest coverage and internally generated funds analyses will determine the need of a given company for normalization." . . . This presents a purely factual question which does not fall within the exception to the mootness doctrine. This matter therefore will not be reviewed. *State ex rel. Mo. Public Service Co. v. Fraas, supra.*

627 S.W.2d at 891. Thus, the court applied the mootness doctrine in not ruling on the issue.

Regarding compensating bank balances, the Commission excluded these monies from the utility's rate base on various grounds including that the lines of bank credit were used to finance CWIP. The court stated that there are well considered cases that to the extent compensating bank balances are used for the purpose of supporting the financing of CWIP, that cost should not be included in rate base but instead should be allowed in AFUDC. The court held that this approach seems in accord with and demanded by Section 393.135 and that a declaration of law

to that effect is appropriate under the exception to the mootness doctrine.[13] 627 S.W.2d at 890-91.

Finally, concerning the Jeffrey Energy Center common facilities, the court held that the common facilities issue fell within the exception to the mootness doctrine and Section 393.135 was not applicable. The Jeffrey Energy Center was a four generating unit site. The first of the four units went into commercial service during the test year. The utility sought to include in rate base all of the common facilities. The Commission held that that only 25% of the common facility costs should be allowed in rate base because ratepayers should not be required to pay for facilities that were also for units 2, 3 and 4 which were not in service. The court reversed the Commission finding that the common facilities were in full use during the test year. 627 S.W.2d at 889-90.

The Staff believes that Section 393.155 RSMo. 2000 is not relevant. Section 393.155 permits a phase-in of rates due to an unusually large rate base addition, i.e., a nuclear generating unit, once the unit is fully operational and used for service, but not while it is still CWIP, as KCPL initially proposed. Section 393.155.1 was enacted to address the Callaway nuclear unit of AmerenUE and the Wolf Creek nuclear unit of KCPL and subsequently amended to address the Grand Gulf nuclear unit of Arkansas Power & Light Company (APL). (APL subsequently sold its Southeast Missouri service territory to AmerenUE.) Section 393.155.1 provides as follows:

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[13] The court further explained exception to the mootness doctrine as follows:

> An exception, however, is made where an issue is presented of a recurring nature, is of general public interest and importance, and will evade appellate review unless the court exercises its discretionary jurisdiction. *State ex rel. Laclede Gas Co. v. P.S.C.*, 535 S.W.2d 561 (Mo.App.1976); *State ex rel. The Empire District Electric Company v. Public Service Commission of State of Mo., supra*; *State ex rel. Laclede Gas Co. v. P.S.C.*, 600 S.W.2d 222 (Mo.App.1980). The question of whether to exercise this discretionary jurisdiction comes down to whether there is some legal principle at stake not previously ruled as to which a judicial declaration can and should be made for future guidance. If the matter in dispute is simply a question of fact dependent upon the evidence in the particular case, there is no necessity for a declaration of legal principle such as to call the exception into play.

627 S.W.2d at 885.

> If, after hearing, the commission determines that any electrical corporation should be allowed a total increase in revenue that is primarily due to an unusually large increase in the corporation's rate base, the commission, in its discretion, need not allow the full amount of such increase to take effect at one time, but may instead phase in such increase over a reasonable number of years. Any such phase-in shall allow the electrical corporation to recover the revenue which would have been allowed in the absence of a phase-in and shall make a just and reasonable adjustment thereto to reflect the fact that recovery of a part of such revenue is deferred to future years. In order to implement the phase-in, the commission may, in its discretion, approve tariff schedules which will take effect from time to time after the phase-in is initially approved.

A. Rate Increase Case And Rate Decrease Case Moratoriums

The Agreement provides for a moratorium on rate increase cases and rate decrease cases till January 1, 2007, i.e., the Signatory Parties agree that they will not file a rate increase case or a rate decrease case that would result in a general rate increase or general rate decrease going into effect prior to January 1, 2007. The Agreement sets out exceptions to this prohibition agreed to by the Signatory Parties. Also, the Commission itself is not a Signatory Party to the Agreement, so it is not bound by this prohibition. Thus, non-signatories to the Agreement may request or file for an earnings/revenues investigation of KCPL, and the Commission in response may direct the Staff to conduct an earnings/revenues investigation of KCPL. The Staff does not believe that anything that it has agreed to respecting the KCPL Regulatory Plan is a challenge to Section 393.135. There is nothing in the Agreement that either prohibits rate decrease cases from being filed with the Commission or prohibits the Commission from ordering KCPL to reduce its rates.

B. Rate Filing #1 (2006 Rate Case)

This rate case does not encompass any Iatan 2 or non-Iatan 2 CWIP being placed in rate base. This rate case will include prudent expenditures related to 100 megawatts (MWs) of wind

generation and the additions to transmission and distribution infrastructure identified in Appendix D that are in service prior to the agreed upon true-up date.

C. Rate Filing #2 (2007 Rate Case)

This rate case does not encompass any Iatan 2 or non-Iatan 2 CWIP being placed in rate base. This rate case will include prudent expenditures related to installation of a Selective Catalytic Reduction (SCR) facility at LaCygne 1 and the additions to transmission and distribution infrastructure identified in Appendix D that are in service prior to the agreed upon true-up date.

D. Rate Filing #3 (2008 Rate Case)

This rate case does not encompass any Iatan 2 or non-Iatan 2 CWIP being placed in rate base. This rate case will include prudent expenditures related to installation of an SCR facility, a Flue Gas Desulphurization (FGD) unit and a Baghouse at Iatan 1, 100 MWs of wind generation and the additions to transmission and distribution infrastructure identified in Appendix D that are in service prior to the agreed upon true-up date.

E. Rate Filing #4 (2009 Rate Case)

This is the Iatan 2 rate case. This rate case does not encompass any Iatan 2 or non-Iatan 2 CWIP being placed in rate base. Only those costs for plant that is in-service within the time frame of the true-up process in this rate case will be included in rate base. Thus, this rate case will include Iatan 2 prudent expenditures, the FGD unit and the Baghouse at LaCygne 1 and the additions to transmission and distribution infrastructure identified in Appendix D that are in service prior to the agreed upon true-up date.

VI. Additional Amortizations To Maintain Financial Ratios

In 2001 in Case No. EM-2001-464, the case in which KCPL sought Commission authorization to reorganize itself into a holding company structure under the Public Utility Holding Company Act of 1935, KCPL agreed to maintain its debt at investment grade.[14] The Signatory Parties in the instant proceeding agree that it is desirable to maintain KCPL's debt at investment grade during the period of the construction of Iatan 2, which ends June 1, 2010. They commit to work to ensure that based on prudent and reasonable actions by KCPL, KCPL has a reasonable opportunity to maintain its bonds at an investment grade during this construction period. The Signatory Parties' reference point is the Standard and Poor's BBB investment grade and the Standard and Poor's credit ratio ranges and definitions for three financial ratios as they relate to its BBB investment grade. The three financial ratios of importance are: (1) Total Debt to Total Capitalization, (2) Funds from Operations Interest Coverage and (3) Funds from Operations as a Percentage of Average Total Debt.

To this end, the Signatory Parties agree to support an additional amortization amount added to KCPL's cost of service in a rate case, when the projected cash flows resulting from KCPL's Missouri jurisdictional operations, as determined by the Commission, fail to meet or exceed the Missouri jurisdictional portion of the lower end of the top third of the Standard and Poor's BBB range shown in Appendix E, for (1) the Funds from Operations Interest Coverage ratio and (2) the Funds from Operations as a Percentage of Average Total Debt ratio. The additional amortization amount added to KCPL's cost of service in a rate case will increase KCPL's revenue requirement to be recovered from ratepayers. Current guidelines for the top

[14] KCPL also agreed to submit quarterly to the Commission's Financial Analysis Department the following key financial ratios as defined by Standard and Poor's Credit Rating Service: (1) pre-tax interest coverage; (2) after tax coverage of interest and preferred dividends; (3) funds flow interest coverage; (4) funds from operations to total debt; (5) total debt total capital (including preferred); and (6) total common equity to total capital.

third of the Standard and Poor's BBB category for a Standard and Poor's business profile 6 company (equivalent business profile to KCPL):

51% Total Debt to Total Capitalization

3.8x Funds from Operations Interest Coverage (an operational guideline)

25% Funds from Operations as a Percentage of Average Total Debt (an operational guideline)

Appendix F "Illustration: Adjustment of Amortization Amounts" illustrates the adjustment process that the Signatory Parties agree to use to determine the Missouri jurisdictional amortization levels discussed herein.

If KCPL meets the Standard and Poor's BBB+ credit rating values but does not receive an investment grade credit rating, KCPL agrees that the Signatory Parties are under no obligation to recommend any further cash flow or rate relief to satisfy the obligations under this section. KCPL also recognizes and agrees that its Missouri operations are only responsible for and will only provide cash flow for its Missouri operating share of the necessary cash flows.

Historically, financial ratios are a matter that has been of concern to the Commission, in particular regarding utilities engaged in construction projects necessary to the continued provision of safe and adequate service to customers. It should be noted that no Missouri court has found the Commission's application of its standard for interim rate relief or normalization versus flow through of tax timing differences to be a violation of Section 393.135 for companies needing interim relief because of construction projects. This matter of the relationship of financial ratios to the granting of interim rate relief or normalization of tax timing differences by the Commission is set out in much more detail in Attachment 3 hereto. The Commission has based its determination of whether to grant interim rate relief or normalization of tax timing differences based on certain financial ratios of the utility, i.e., interest coverages in the matter of

interim rate relief, and cash flow, interest coverage and internally generated funds in the matter of normalization of tax timing differences.

In Case No. ER-78-252, the KCPL rate increase case immediately preceding the Iatan 1 in commercial operation case, Case No. ER-80-48, KCPL was engaged in the final stages of the construction of the Iatan station, i.e., Iatan 1, and at the same time was engaged in the funding of the construction of its 47% share of the Wolf Creek nuclear generating station, the Commission authorized normalization of certain tax timing differences due to the level of the relevant financial ratios of KCPL. In a subsequent KCPL interim rate relief case in 1979-1980, Case No. ER-80-204, KCPL's interest coverages no longer permitted KCPL to raise funds other than by an increase in customer rates which the Commission granted on an interim basis in Case No. ER-80-204 pending the processing of Case No. ER-80-48. (It should be noted, respecting the Commission's use of financial ratios for determination of whether interim rate relief will be authorized, that the Western District Court of Appeals held in the *Laclede* case that the Commission is not necessarily limited to the emergency standard for the granting of interim rate relief. The Court thereby indicated that the Commission could use financial ratios for the granting of rate relief in a manner other than how it has previously used financial ratios for the granting of rate relief.)

VII. Amortizations: Ten (10) Year Recognition Of Future Benefits

Some of the amortizations provided for by the Agreement include a rate base offset that accrues to the benefit of KCPL's customers in future rate proceedings. Although no potential legislation is known of that would end these customer benefits, KCPL has agreed that notwithstanding any future changes to Chapters 386 and 393, such benefits shall be reflected in rates for at least ten (10) years following the effective date of a Commission Order approving the

Agreement.[15] The amortization events that are covered by this provision of the Agreement are the following:

AMORTIZATIONS	START	END
$3.5 M, annually – started as part of settlement in Case No. EO-94-199 – continues to effective date of Report And Order in 1st rate case (2006 rate case)	1994	1/1/07 estimate
$10.3 M, annually – Wolf Creek life-span increase from 40 years to 60 years – commences with Commission authorization of the Agreement and continues to effective date of Report And Order in 1st rate case (2006 rate case)	2005	1/1/07 estimate
$17.0 M, annually – included in revenue requirement in 1st, 2nd and 3rd rate cases (2006, 2007 and 2008 rate cases) – possible increase/decrease in the $17.0 M annual amount pursuant to Paragraph III.B.1.i. of the Agreement and Appendices E and F to the Agreement	1/1/07 estimate - 1st rate case Report And Order effective Date	9/1/10 estimate - 4th rate case (Iatan 2) Report And Order effective date
SO_2 emission allowance sales proceeds recorded as a regulatory liability – this regulatory liability will be amortized over the same time period used to depreciate environmental assets, assuming IRS treats it as like-kind exchange	9/1/10 estimate - 4th rate case (Iatan 2) Report And Order effective date	

VIII. Demand Response, Efficiency And Affordability Programs

The Signatory Parties have agreed to the following Demand Response, Efficiency and Affordability Programs. The costs shown are the initially budgeted, cumulative expenditures that KCPL has committed to for Missouri for a five (5) year period beginning in 2005:

Affordability Programs - $2.5 million over 5 years

Low-Income Affordable New Homes Program

Low Income Weatherization And High Efficiency Program

Efficiency Programs - $12.7 million over 5 years

Online Energy Information And Analysis Program
Using Nexus® Residential Suite

[15] The KCPL Regulatory Plan Stipulation And Agreement filed with the KCC contains the following language at II.F., page 14, last sentence of first complete paragraph: "Furthermore, KCPL will not make any efforts or support any efforts to have legislation enacted that have the effect of changing or modifying the terms of this Agreement."

Home Performance With Energy Star® Program - Training

Change A Light– Save The World

Cool Homes Program

Energy Star® Homes – New Construction

Online Energy Information And Analysis Program
Using Nexus® Commercial Suite

C&I Energy Audit

C&I Custom Rebate - Retrofit

C&I Custom Rebate – New Construction

Building Operator Certification Program

Market Research

Demand Response Programs - $13.8 million over 5 years

Air Conditioning Cycling

The Alliance, An Energy Partnership Program

Details respecting these programs are set out in Appendix C to the Agreement. MDNR, the Staff, Public Counsel and any other interested Signatory Party are to serve as an advisory group to KCPL in the development, implementation, monitoring and evaluation of these programs. Further evaluation needs to be made on the Efficiency Programs listed above prior to implementation to determine the impact of the Efficiency Programs on KCPL and the anticipated cost-effectiveness of the Efficiency Programs presented. KCPL will work with the advisory group to complete the necessary pre-implementation evaluations to determine the initial implementation plan for the Efficiency Programs within four (4) months of the effective date of an Order approving the Agreement. The initial implementation plan for Efficiency Programs may be modified (such modifications may include deleting currently proposed programs or

adding new programs, as well as increases in the overall funding level for Efficiency Programs) based on results from the pre-implementation evaluations and input from the advisory group. KCPL shall complete a detailed post-implementation review of the initial two (2) years of each program within six (6) months of the end of each program's second year. These evaluations will then be used in the selection and design of future programs.

KCPL will accumulate the Demand Response, Efficiency and Affordability Program costs in regulatory asset accounts as the costs are incurred. Beginning with the 2006 Rate Filing, KCPL will begin amortizing the accumulated costs over a ten (10) year period. Signatory Parties reserve the right to establish a fixed amortization amount, in any KCPL rate case prior to June 1, 2011, to be amortized over a period greater or lesser than a ten (10) year period. The amounts accumulated in these regulatory asset accounts shall be allowed to earn a return not greater than KCPL's AFUDC rate. The class allocation of the costs will be determined by the Commission when the amortizations are approved by the Commission in a rate proceeding.

The settlement of the Staff's excess earnings/revenues complaint case against AmerenUE (Case No. EC-2002-1) resulted in Ameren committing the contribution of the following amounts of shareholder monies to the following program areas, i.e., customers' rates were not reduced by these amounts but AmerenUE provided the following monies: (a) $9.0 million total to Dollar More Program ($5.0 million first year and additional $1.0 million each of four subsequent years), (b) $4.0 million to low income weatherization fund ($2.0 million first year and additional $0.5 million each of four subsequent years), (c) $9.0 million total to Ameren Community Development Corporation ($5.0 million first year and additional $1.0 million each of four subsequent years), and (d) $4.0 million to a residential and commercial energy efficiency fund ($2.0 million first year and additional $0.5 million each of four subsequent years).

In Empire's most recent rate increase case (Case No. ER-2004-0570 Demand Response, Efficiency And Affordability Program issues settled in late 2004), the parties reached agreement on Empire's funding of various programs as follows: (a) no less than $155,000 annually for a low income weatherization program, (b) no less than $20,000 annually for the Change a Light, Change the World Program, (c) no less than $100,000 annually for an appliance and HVAC Rebate Program for residential customers and (d) no less than $25,000 annually to fund a portion of the cost of technical energy efficiency audits for commercial customers and provide incentives for installation of energy efficiency measures.

In Aquila's most recent rate increase case (Case No. ER-2004-0034 settled in entirety in April 2004), the parties reached agreement on Aquila's funding of a low income weatherization program, commercial energy audit and/or Change-A-Light program through annual contributions of $93,500 of shareholder funds, until the next general rate proceeding involving Aquila's Missouri electric rates.

IX. Preapproval

Given the *State ex rel Harline v. Public Serv. Comm'n,* 343 S.W.2d 177 (Mo.App. 1960) holding that a utility does not need further Commission authorization to construct plant in its certificated service territory, the Section 393.135 prohibition against CWIP in rate base and the case law that the Commission is not bound by *stare decisis,*[16] the Staff has not favored efforts to

[16] *State ex rel. Chicago, Rock Island & Pacific R.R. Co. v. Public Serv. Comm'n*, 312 S.W.2d 791 (Mo. 1958); *State ex rel. General Tel. Co. v. Public Serv. Comm'*n, 537 S.W.2d 655, 661-62 (Mo.App. 1976); *State ex rel. Associated Nat. Gas Co. v. Public Serv. Comm'n*, 706 S.W.2d 870, 880 (Mo.App. 1985); *State ex rel Arkansas Power & Light Co. v. Public Serv. Comm'n*, 736 S.W. 2d 457, 462 (Mo. App. 1987); *State ex rel. GTE North, Inc. v. Public Serv.Comm'n,* 835 S.W.2d 356, 371-72 (Mo.App. 1992); *State ex rel. Capital City Water Co. v. Public Serv. Comm'n*, 850 S.W.2d 903, 911 (Mo.App. 1993); *State ex rel. St. Louis v. Public Serv. Comm'n*, 47 S.W.2d 102, 105 (Mo.banc 1931); *Marty v. Kansas City Light & Power Co.*, 259 S.W. 793, 796 (Mo. 1923)

In the *General Telephone* case, the Court of Appeals held that the Commission's decision in a prior General Telephone Company case had no binding effect in a subsequent General Telephone Company case:

obtain preapproval from the Commission. However, the Staff's view has been tempered by the Missouri Supreme Court's decision in *State ex re. AG Processing, Inc. v. Public Serv. Comm'n*, 120 S.W.3d 732 (Mo. banc 2003). The Court held that although the acquisition premium recoupment issue could be addressed in a subsequent ratemaking case, the Commission nonetheless had to decide whether the acquisition premium was reasonable as part of its determination of whether the proposed merger would be detrimental to the public.

(*footnote continued*)

> Insofar as the conclusion in the 1962 case is concerned, it has no binding effect in a future rate case. A concise statement of the applicable rule is found in 2 Davis, Administrative Treatise Section 18.09, 605, 610, (1958), as follows:
>
> > "* * * For an equity court to hold a case so as to take such further action as evolving facts may require is familiar judicial practice, and administrative agencies necessarily are empowered to do likewise. When the purpose is one of regulatory action, as distinguished from merely applying law or applying law or policy to past facts, an agency must at all times be free to take such steps as may be proper in the circumstances, irrespective of its past decisions. * * * Even when conditions remain the same, the administrative understanding of those conditions may change, and the agency must be free to act * * *." (Footnotes omitted.)
>
> Clearly the commission in this case was not bound by the action in the 1962 case.

537 S.W.2d at 661-62.

Another relevant case is *State ex rel. Jackson County v. Public Serv. Comm'n*, 532 S.W.2d 20 (Mo. banc 1975), *cert. denied*, 429 U.S. 822, 97 S.Ct. 73, 50 L.Ed.2d 84 (1976). In this case regarding a general rate increase filed by Missouri Public Service Company (MPS), Jackson County and the City of Kansas City tried to invoke an announcement made by the Commission, on the Commission's own, in the Commission's Report And Order in the immediately preceding MPS rate increase case, that there would be a moratorium on rate increases for MPS for a period of at least two years from the effective date of the Report And Order. MPS subsequently filed for another general rate increase and the Commission granted MPS a rate increase within the two year moratorium period it had previously announced.

Jackson County and the City of Kansas City challenged the rate increase and the Missouri Supreme Court stated that a moratorium was in conflict with the spirit of the Public Service Commission Law, that spirit being continuous regulation to meet changes in conditions as required by these changes in conditions. The Court quoted from a Missouri Supreme Court decision in *State ex rel. Chicago, Rock Island, & Pacific R.R. Co. v. Public Serv. Comm'n*, 312 S.W.2d 791, 796 (Mo. banc 1958) as follows:

> "Its [Commission's] supervision of the public utilities of this state is a continuing one and its orders and directives with regard to any phase of the operation of any utility are always subject to change to meet changing conditions, as the commission, in its discretion, may deem to be in the public interest." To rule otherwise would make §393.270(3) of questionable constitutionality as it potentially could prevent alteration of rates confiscatory to the company or unreasonable to the consumers. [Citation omitted.]

532 S.W.2d at 29.

Thus, the question: as a Signatory Party to the Agreement, has the Staff engaged in any "preapproval" determinations? The Staff has agreed that it is prudent for KCPL to construct at the Iatan site a baseload coal-fired unit, with an in-service date of 2010, and the indicated environmental enhancements and transmission and distribution infrastructure. The Staff has not engaged in preapproval of the final cost or the project management of these construction projects, or that the plant additions will meet the in-service criteria and dates agreed to as part of this Agreement.

Nothing is assumed in the Agreement regarding a finding or determination in advance of KCPL incurring costs that KCPL is prudently managing costs or that KCPL is taking or has taken prudent actions to maintain the investment grade rating for its financial instruments. The Section on Cost Control Process For Construction Expenditures provides that KCPL must develop and have a cost control system in place that identifies and explains any cost overruns above the definitive estimate during the construction period of the Iatan 2 project, the wind generation projects and the environmental investments. This mechanism is intended to allow for a full and complete construction audit of the costs expended to construct these facilities and the determination of whether any of the costs incurred are due to imprudence.

The prudency of the implementation by KCPL of the following agreed to items may be challenged by the Signatory Parties: wind generation, Iatan 2, environmental and transmission and distribution infrastructure additions and enhancements, construction accounting and the Demand Response, Efficiency and Affordability Programs.

The Commission authorized, in a Report And Order issued on November 14, 1973 in Case No. 17,895, the construction of the Iatan Steam Electric Generating Station as a multi-unit site designed for four generating units to be constructed and operated by KCPL. To the Staff, no

further Commission authorization appears to be required regarding the siting of Iatan 2. *Re In the Matter of the Application of Kansas City Power & Light Co. and St. Joseph Light & Power Co. for Certificates of Public Convenience and Necessity to Construct, Own, Operate and Maintain an Electric Generating Station in Platte County, Missouri, and Certain Related 345 kv Transmission Facilities*, Case No. 17,895, Report And Order (1973) (unreported case).

The Staff has noted above the objections and opposition raised in the Application To Intervene Of Department Of Energy. USDOE has stated that it is opposed to customers being requested to preapprove specific public utility investments as being prudent and used and useful, and has noted that such a request may be contrary to Missouri's "File and Suspend" law, Sections 393.140(11) and 393.150 RSMo, for fixing just and reasonable rates. Thus, the Commission must have in mind the question what has it bound itself to if it were to approve the Agreement. The Staff would direct the Commission to the following language in Paragraph III.B.10.g., at pages 53-54, of the Agreement.

> This Agreement does not constitute a contract with the Commission. Acceptance of this Agreement by the Commission shall not be deemed as constituting an agreement on the part of the Commission to forego, during the Regulatory Plan, the use of any discovery, investigative or other power which the Commission presently has. For example, non-signatories to this Agreement may request or file for an earnings/revenues investigation of KCPL, and in response the Commission may direct the Staff to conduct an earnings/revenues investigation of KCPL. Thus, nothing in this Agreement is intended to impinge or restrict in any manner the exercise by the Commission of any statutory right, including the right to access information, or any statutory obligation. . . .

The Staff believes that nonsignatories to the Agreement are not bound by the Agreement and that even if the Commission were to approve the Agreement, nonsignatories may raise any issue and the Commission must consider the issue irrespective of the Agreement. Thus, nonsignatories may raise issues regarding the necessity or timing of Iatan 2, or that alternative technologies or fuels should have been used by KCPL. Should the Commission approve the

Agreement, USDOE is not precluded from raising issues in KCPL rate cases regarding areas not identified by USDOE in its Application To Intervene as areas of concern to it, such as rate of return, return on common equity and capital structure.

The Staff also would note specific language in the Agreement at page 27, in Paragraph "III.B.1.o. Resource Plan Monitoring," which authorizes a Signatory Party to raise as an issue significant changes in factors or circumstances that have not been acknowledged by KCPL and a Signatory Party does not waive any rights to contest, in any proceeding, that KCPL did not properly monitor significant factors or circumstances and as a result did not properly execute its Resource Plan:

> If any Signatory Party believes that there have been significant changes in factors or circumstances that have not been acknowledged by KCPL, any Signatory Party may notify KCPL and all other Signatory Parties and request a meeting of all Signatory Parties to discuss the specific changes in factors or circumstances that give rise to the concern of the Signatory Party giving such notice. If the interested Signatory Parties cannot resolve the dispute within ninety (90) days of a Signatory Party's written notification, the matter will be brought to the Commission for its determination. The burden of proof to demonstrate the continued reasonableness and prudence of the new resource plan shall remain with KCPL in any dispute regarding changed factors or circumstances.
>
> Signatory Parties by signing this Agreement do not waive any rights to contest, in any proceeding, that KCPL did not properly monitor significant factors or circumstances and as a result did not properly execute its Resource Plan.

In attempting to address herein the concerns of USDOE, several subsections in Senate Bill 179 (SB 179) that had not previously occurred to undersigned counsel have risen to a level of interest that at least warrants exploration with KCPL as to KCPL's view of these subsections' applicability, if any. Subsections 386.266(8), (10) and (12) state as follows:

> Section 386.266:
>
> . . . .
>
> (8) In the event the commission lawfully approves an incentive or performance based plan, such plan shall be binding on the commission for the entire term of

> the plan. This subsection shall not be construed to authorize or prohibit any incentive or performance based plan.
>
> . . . .
>
> (10) Nothing contained in this section shall be construed as affecting any existing adjustment mechanism, rate schedule, tariff, incentive plan, or other ratemaking mechanism currently approved and in effect.
>
> . . . .
>
> (12) The provisions of this section shall take effect on January 1, 2006 . . .

Seemingly if the Agreement is to be approved by the Commission on a schedule consistent with the timing presently sought by KCPL, the Commission will render its determination before January 1, 2006.

Finally, the Staff would note that the Agreement terminates under certain conditions, such as under Paragraph III.B.10.c. if the Commission finds a material misrepresentation by KCPL:

> The Signatory Parties enter into this Agreement in reliance upon information provided to them by KCPL. In the event that the Commission finds that KCPL failed to provide the Signatory Parties with material and relevant information in its possession, or which should have been available to KCPL through reasonable investigation, or in the event that the Commission finds that KCPL misrepresented facts relevant to this Agreement, this Agreement shall be terminated.

X. Senate Bill 179 (SB 179) – Interim Energy Charges And Periodic Rate Adjustments

The Regulatory Plan provides that prior to June 1, 2015, KCPL will not seek to utilize SB 179 or other change in state law that would allow riders or surcharges or changes in rates outside of a general rate case based upon a consideration of less than all relevant factors. The other Signatory Parties agree that for that same period of time, if KCPL proposes an interim energy charge (IEC) within certain specified parameters, the other Signatory Parties will not argue that the IEC constitutes single-issue or retroactive ratemaking. Although it is not

addressed in the SB 179 section of the Agreement, there is provision elsewhere that the Signatory Parties agree that they will not take the position that the specified KCPL environmental enhancements should be excluded from KCPL's rate base on the ground that the projects were not necessary or timely, or that alternative technologies or fuels should have been used by KCPL, so long as KCPL proceeds to implement the Resource Plan described in the Agreement (or a modified version of the Resource Plan, where the modified plan has been approved by the Commission) and KCPL is in compliance with Paragraph III.B.1(o) "Resource Plan Monitoring."[17]

The various proceedings regarding KCPL's desire for a Regulatory Plan commenced almost at the same time as the conclusion of the Legislative Session that preceded the Legislative Session in which SB 179 was introduced. KCPL advised the participants that KCPL was interested in effectuating the likely greater certainty of a negotiated Regulatory Plan rather than seeking to utilize possible prospective legislation that would enable the Commission to provide the relief that KCPL is interested in.

Historically parties before the Commission have attempted to address the prospect of legislation in stipulations and agreements. For years the standard language in the rate moratorium sections of stipulations and agreements has stated that the signatory parties agree that the utility's rates should remain at their current levels for a specified period of time, unless a significant event that has a major impact on the utility occurs, including, but not limited to a significant change in federal or state tax laws, or a significant change in federal utility laws or regulations. Such language appears in the instant Agreement.

[17] The Agreement also states that nothing in the Agreement shall be construed to limit any of the Signatory Parties' ability to inquire regarding the prudence of KCPL's expenditures, or to assert that the appropriate amount to include in KCPL's rate base or its cost of service for these investments is a different amount (e.g., due to imprudent project management) than that proposed by KCPL.

SB 179 makes lawful single-issue ratemaking for certain matters/items, prudently incurred fuel and purchased power costs, including transportation, and prudently incurred costs to comply with any federal, state or local environmental law, regulation or rule. KCPL has indicated that it is not interested in proceeding outside the context of a general rate case and this is reflected in the Agreement. The KCPL Regulatory Plan is designed for annual rate increase cases at KCPL's option. Finally, the Staff again would note in SB 179, Section 386.266(10) and (12).

XI. SO_2 Emission Allowances

KCPL is authorized to manage its SO_2 emission allowance inventory, including the sales of such allowances, under the Stipulation And Agreement in Case No. EO-2000-357, *In the Matter of the Application of Kansas City Power & Light Company for Authorization to Manage Sulfur Dioxide Emission Allowance Inventory*, 9 Mo.P.S.C.3d 177 (2000). Under such Stipulation And Agreement, KCPL must record all SO_2 emission allowance sales proceeds as a regulatory liability in Account 254, Other Regulatory Liabilities, for ratemaking purposes. Paragraph III.B.1.d. SO_2 Emission Allowances of the Agreement and the SO_2 Emission Allowance Management Policy ("SEAMP") contained in Appendix A to the Agreement, supersede the plan approved in the Stipulation And Agreement in Case No. EO-2000-357. The proceeds and costs of all transactions identified in the SEAMP will be recorded in Account 254 for ratemaking purposes. The regulatory liability will be amortized over the same time period used to depreciate environmental assets (emission control equipment and other emission control investments). The Agreement recognizes that the sales of SO_2 emission allowances to fund investments in new environmental control equipment, in order to meet emissions standards

required now or in the future by legislation, MDNR or the United States Environmental Protection Agency (EPA) regulations, are like-kind exchanges of assets.

XII. Partnership Issues Involving The Iatan 2 Plant

As indicated above, the Staff is aware of the need of Empire and Aquila for additional baseload generation capacity in the near term and both utilities have made their interest in being part owners of Iatan 2 known to KCPL, in addition to the Staff. Empire and Aquila are presently joint owners with KCPL in Iatan 1. Empire owns 12%, Aquila owns 18% and KCPL owns the remaining 70% of Iatan 1. The Missouri Joint Municipal Electric Utility Commission (MJMEUC) also has made known to KCPL and the Staff its and its members interest in being part owners of Iatan 2. The Staff has expended considerable effort in attempting to have the interests of Empire, Aquila and MJMEUC recognized by KCPL. As a consequence, there is provision in the Agreement that KCPL will consider Empire and Aquila, individually, as preferred potential partners in Iatan 2, of at least a 30% combined share of an 800-900 MW unit, and will consider MJMEUC as a preferred potential partner in Iatan 2, of at least 100 MWs of an 800-900 MW unit, if each of these entities can demonstrate that it has a commercially feasible financing plan for meeting its financial commitments to participate by the later of August 1, 2005, or such date that KCPL shall issue its request(s) for proposal(s) related to Iatan 2. At the same time, KCPL reserves the right to continue to discuss with other entities those entities' participation in Iatan 2.

To facilitate and effectuate these activities, Empire has Case No. EO-2005-0263 (*In the Matter of The Empire District Electric Company's Application for Certificate of Public Convenience and Necessity and Approval of an Experimental Regulatory Plan Related to Generation Plant*) presently pending before the Commission, and Aquila has Case No. EO-2005-

0293 (*In the Matter of the Application of Aquila, Inc., for Approval of Its Experimental Regulatory Plan and for a Certificate of Convenience and Necessity Authorizing It to Participate in the Construction, Ownership, Operation, Maintenance, Removal, Replacement, Control and Management of a Steam Electric Generating Station in Platte County, Missouri, or Alternatively for an Order Specifically Confirming That Aquila, Inc., Has the Requisite Authority under Its Existing Certificate*(*s*)) presently pending before the Commission.

XIII. Customer Class Cost Of Service Study – Comprehensive Rate Design Case

The last customer class cost of service study – comprehensive rate design case for KCPL was Case No. EO-94-199, *In the Matter of the Customer Class Cost of Service and Comprehensive Rate Design Investigation of Kansas City Power & Light Company*, Order Approving Stipulation and Agreement 5 Mo.P.S.C.3d 76 (1996). Case No. EO-94-199 settled by stipulation and agreement in 1996. The Agreement in the instant case provides that no later than February 1, 2006, in the context of KCPL's 2006 rate case, KCPL will submit to the Signatory Parties a Missouri jurisdictional revenue requirement cost of service study and a Missouri jurisdictional customer class cost of service study covering the twelve (12) months ending December 31, 2005. KCPL has agreed that the Missouri customer class cost of service study will include the requirements shown in Appendix I to the Agreement. The Signatory parties have agreed not to file new or updated class cost of service studies or to propose changes to rate structure in the 2007 and 2008 rate cases, if KCPL files such rate cases.

XIV. Commission Has Previously Adopted Or Rejected Other Experimental Alternative Regulation Plans

Experimental Alternative Regulation Plans previously adopted or rejected by this Commission are dissimilar to the instant Agreement comprising the KCPL Regulatory Plan.

Other alternative regulation plans previously adopted or rejected by the Commission include the following:

A. AmerenUE EARP I: 7/1/95 to 6/30/98 and EARP II: 7/1/98 to 6/30/01: Two 3-Year Plans That Provided For Sharing Credits, Not Rate Increases – Provision For Hearings If Dispute Between AmerenUE And Staff And/Or Public Counsel Regarding Sharing Credits

B. SWBT Incentive Regulation Plan (SBIRE) Case No. TO-90-1 – Local Network Modernization Plan Negotiated In Context Of Rate Reduction Report And Order On Appeal – Term of SBIRE: 1/1/90 to 12/31/92, plus an additional year 1/1/93 to 12/31/93

C. SWBT Accelerated Modernization Plan (AMP) Offered To SWBT By Commission In Context of Case No. TC-93-224, But Rejected By SWBT– Local Network Modernization Plan Negotiated In Context Of Rate Reduction Report And Order On Appeal – Term: 1/1/94 to 12/31/98

D. Aquila Proposed Regulatory Plans Respecting Its Proposed Mergers With SJLP And Empire – Commission Rejected Both Proposed Regulatory Plans – Aquila Merger With SJLP Occurred But Aquila Merger With Empire Did Not Occur – Aquila Proposed Five Year Rate Moratorium For SJLP And Empire For 1/1/01 To 12/31/05, But No Rate Moratorium For Aquila

XV. Special Contracts With Ford Motor Company and Praxair, Inc.

Two industrial customers, Praxair, Inc, and Ford Motor Company, that participated in Case No. EO-2004-0577 and Case No. EW-2004-0596, recently signed a Special Interruptible Contract (Praxair) and a Letter of Understanding (Ford Motor Company), respecting a similar arrangement, respectively. KCPL has indicated that it intends to initiate, in the near future, proceedings relating to these special contracts to obtain the Commission's approval of them, or alternatively, a determination from the Commission that no formal regulatory approval is required. As a part of the Agreement, KCPL has agreed that for ratemaking purposes and for other purposes relating to the other terms of the KCPL Regulatory Plan, these special contract customers and other special contract customers will be treated as if they were paying the full

generally applicable tariff rate for service from KCPL and other provisions in special contracts will not affect rate base for regulatory purposes.

XVI. MDNR As A Signatory Party

MDNR is a Signatory Party and is now represented as a Signatory Party by in-house counsel. Up to the execution of the Agreement, MDNR was represented by an Assistant Attorney General. After the Agreement had been executed and filed on March 28, 2005 by the Staff and various other Signatory Parties, the Signatory Parties were advised that MDNR would execute the Agreement by in-house counsel and not by an Assistant Attorney General. References to the Attorney General appear on pages 28 and 54 of the Agreement and were included in the Agreement without objection by Staff counsel because it was believed that an Assistant Attorney General would execute the Agreement on behalf of MDNR. Although these references to the Attorney General are accurate, Staff counsel would have requested the deletion of these references to the Attorney General had the Signatory Parties known that the Attorney General would not represent MDNR as a signatory to the Agreement.

Wherefore, the Staff submits the instant Suggestions In Support of the Stipulation And Agreement filed on March 28, 2005 by Kansas City Power & Light Company.

Respectfully submitted,

DANA K. JOYCE
General Counsel

/s/Steven Dottheim
Steven Dottheim
Chief Deputy General Counsel
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Certificate of Service

I hereby certify that copies of the foregoing have been mailed, hand-delivered, or transmitted by facsimile or electronic mail to all counsel of record this 10th day of May 2005.

/s/ Steven Dottheim

ATTACHMENT 1

INDEX
STIPULATION AND AGREEMENT
CASE NO. EO-2005-329

LIST OF APPENDICES

ATTACHMENT 2

DIFFERENCES BETWEEN KANSAS STIPULATION AND AGREEMENT (KANSAS KCPL REGULATORY PLAN) AND MISSOURI STIPULATION AND AGREEMENT (MISSOURI KCPL REGULATORY PLAN) – LANGUAGE IN KANSAS STIPULATION AND AGREEMENT DIFFERENT THAN LANGUAGE IN MISSOURI STIPULATION AND AGREEMENT

(1) KS. Stipulation And Agreement (S&A) ¶ II.A.2, page 4: "KCPL will accumulate costs for these programs in regulatory asset accounts as the costs are incurred through the next rate case. The amortization of these costs and return will be determined in the next rate case."

(2) KS. S&A ¶ II.A.3, page 4: ". . . the parties intend for the rate plan attached as **Appendix C** to run until June 1, 2010."

(3) KS. S&A ¶ II.A.4, page 5: "Although it is not anticipated that KCPL will need to obtain Commission approval for the issuance such securities, KCPL will file with the Commission within ten days of the issuance of any debt securities occurring during the term of this Agreement, a report including the amount of debt securities issued, date of issuance, interest rate (initial rate if variable), maturity date, redemption schedules or special terms, if any, and use of proceeds. . . With regard to such debt, KCPL agrees that it will abide by the conditions set forth by the Federal Energy Regulatory Commission in its Order issued February 21, 2003, in Docket No. ES02-51-000. KCPL also acknowledges that future proceedings before the Commission will likely address 'ringfencing' and affiliate requirements for utilities in general and that it will be bound by decisions in such proceedings."

On February 21, 2003, the Federal Energy Regulatory Commission issued in Docket No. ES02-51-000 an Order Conditionally Granting Authorization To Issue Long-Term Unsecured Debt And Announcing New Policy On Conditioning Securities Authorizations. On September 6, 2002, Westar Energy, Inc. (Westar (formerly Western Resources, Inc.)) filed an application seeking authorization to issue long-term, unsecured debt in amount not to exceed $650 million at any one time. (Westar's pre-existing debt issuances were authorized by either the FERC or the KCC with no conditions set regarding whether the borrowings could be used for non-utility businesses or whether Westar's assets could be used to secure the debt).

The FERC conditionally authorized Westar's request to issue long-term, unsecured debt in an amount not to exceed $650 million, subject to four conditions.[1] The FERC also specified four additional restrictions on secured and unsecured debt that the FERC said would be applied to all future public utility issuances of secured and unsecured debt authorized by the FERC:

[1] "First, the proceeds of the debt must be used solely for the purpose of retiring outstanding indebtedness, including accrued and unpaid interest due at maturity. Second, Westar is required to file quarterly informational status reports detailing its financial condition and the debt-reduction efforts within 30 days of the end of each calendar quarter. Third, Westar must file a Report of Securities Issued within 30 days after the sale or placement of the long-term, unsecured debt, as stated in the [FERC's] regulations. [footnote omitted]. Finally Westar must also abide by the following restrictions on secured and unsecured debt."

> . . . First, public utilities seeking authorization to issue debt that is secured (i.e., backed) by utility assets must use the proceeds of the debt for utility purposes only. Second, with respect to such utility asset-secured debt issuances, if any utility assets that secure such debt issuances are divested or "spun off," the debt must "follow" the asset and be divested or "spun off" as well.
>
> Third, if assets financed with unsecured debt are divested or "spun off," the associated unsecured debt must follow those assets. Specifically, if any of the proceeds from unsecured debt are used for non-utility purposes, the debt likewise must "follow" the non-utility assets and if the non-utility assets are divested or "spun off" then a proportionate share of debt must "follow" the associated non-utility assets by being divested or "spun off" as well. Last, with respect to unsecured debt used for utility purposes, if utility assets financed by unsecured debt are divested or "spun off" to another entity, then a proportionate share of the debt also must be divested or "spun off."

(4) KS. S&A ¶ II.A.5, page 6: "KCPL further recognizes that any finding by the Commission that KCPL has failed to prudently manage its costs, continuously improve productivity, and maintain service quality during the ~~Regulatory Plan~~ five-year period will negate the obligation of the ~~Signatory Parties~~ parties to this Agreement other than KCPL ("non-KCPL parties") contained in this section."

"In order to assist in the goal of providing KCPL a reasonable opportunity to maintain its bonds at an investment grade rating during the construction period ending June 1, 2010, the non-KCPL parties agree to support an amortization accounting referred to as a Contribution in Aid of Construction ("CIAC"). The CIAC is anticipated to result in lower overall costs of the Resource Plan to ratepayers over the life of such investments than traditional ratemaking, while also providing KCPL with adequate cash flow to maintain its debt at investment grade. (The term "resource Plan" includes the capital investments identified in **Appendices A and A-1**, and the Customer Programs identified in **Appendices B and B-1**.) The lower financing costs associated with investment grade ratings increases the benefits of the CIAC to ratepayers. The non-KCPL parties reserve the right to recommend CIAC amounts in each rate case such that the CIAC amounts in aggregate do not exceed the expected cost savings from the amortization mechanism and the lower costs of capital resulting from the investment grade ratings."

"The parties further recognize and agree that the use of the CIAC is extraordinary and is reasonable only in light of the facts and circumstances of this proceeding. It should not be construed as precedential in any other proceeding or for any other company. The parties' agreement is based on unique factors in this case, including, but not limited to: . . . . "

KS. S&A ¶ II.A.5, page 7: " . . . However, no CIAC amounts will be booked after June 1, 2010. The accumulated CIAC amounts will be treated as increases to the depreciation reserve and be deducted from rate base in any future KCPL rate proceedings, beginning with the 2009 case. . . ."

(5) KS. S&A ¶ II.B.2, page 9: "KCPL will not voluntarily incur material capital investments or expenses beyond those contemplated by this Agreement and the Resource Plan without explicit approval by the Commission."

(6) KS. S&A ¶ II.B.3., II.B.3.g) and II.B.3.j) pages 10-11: "KCPL agrees to ~~actively~~ monitor the ~~major factors and circumstances which influence the need for and economics of all elements of its~~ reasonableness and adequacy of the Resource Plan ~~(the term "Resource Plan" is defined for purposes of this Agreement in Paragraph III.B.1.a.)~~ until the capital investments described ~~in Paragraph III.B.5 below~~ therein are completed. KCPL will on its own or upon request of any non-KCPL parties re-assess the reasonableness and adequacy of the Resource Plan if changed circumstances arise that may impact the reasonableness and adequacy of the Resource Plan during the initial and ongoing implementation of the primary elements of the Resources Plan. Such ~~factors and~~ changes in circumstances would include, but not be limited to:

"g) material change in energy market conditions"

"j) material changes in the projected rates and costs to ratepayers resulting from the Resource Plan."

KS. S&A ¶ II.B.3., page 11: "If KCPL's senior management determines that its Resource Plan should be modified because changed factors or circumstances have impacted the reasonableness and adequacy of the ~~r~~Resource ~~p~~Plan, then it shall file notice with the Commission and notify all ~~Signatory~~ ~~P~~parties ~~in writing~~ within ~~forty five (45)~~ ten days of any such determination. . . . Any agreement concerning modification of the resource plan shall be filed with the Commission for approval. . . ."

"If any Signatory Party believes that there have been significant changes in factors or circumstances that have not been acknowledged by KCPL, any Signatory Party may notify KCPL and all other Signatory Parties and request a meeting of all Signatory Parties to discuss the specific changes in factors or circumstances that give rise to the concern of the Signatory Party giving such notice. If the interested Signatory Parties cannot resolve the dispute within ninety (90) days of a Signatory Party's written notification, the matter will be brought to the Commission for its determination. The burden of proof to demonstrate the continued reasonableness and prudence of the new resource plan shall remain with KCPL in any dispute regarding changed factors or circumstances."

"Signatory Parties by signing this Agreement do not waive any rights to contest, in any proceeding, that KCPL did not properly monitor significant factors or circumstances and as a result did not properly execute its Resource Plan."

(7) KS. S&A ¶ II.B.4, page12: " . . . KCPL commits to a fair and objective evaluation of all such proposals for such participation, including any proposals submitted by Kansas utilities. . . ."

(8) KS. S&A ¶ II.B.5, page12: "Future Resource Plans. In order to provide more assurance that future generation or power supply, including Demand Side Management resources, are acquired at the most reasonable cost and to establish a benchmark of reasonable costs, KCPL agrees that its process for considering or acquiring future resources in addition to those

contemplated by this Resource Plan shall include the issuance of a Request for Proposal (RFP) for the supply of such resource by competitive bid. KCPL agrees to consult with Staff in the design and content of the RFP before it is issued."

(9) KS. S&A: Parties do not request that the KCC approve the Stipulation And Agreement to be effective by May 15, 2005 or some other date.

(10) KS. Appendix A, Resource Plan, page 1: "Coal-Fired Generation: . . . Should KCPL build the bridge, parties reserve the right to take any position on the revenue required related to the bridge in a future rate case. KCPL will consult with Staff regarding its negotiations for coal delivery arrangements and the need for the bridge before making a decision regarding the bridge."

"Wind-Power Generation: The second 100 MW investment in new wind generation will not be considered a part of the Resource Plan unless and until a detailed evaluation supports proceeding with its construction and it receives Commission approval. . . . As part of the evaluation of the wind generation, KCPL will issue a Request for Proposal (RFP) for a twenty-year purchase power agreement (PPA) for wind generation from independent third parties on a cost per kilowatt-hour basis, which includes any expected tax credits."

(11) KS. Appendix A-1, Asset Management Plan, chart, page 1: The chart "Proposed Capital Expenditure Level Increases" shows total company dollars.

(12) KS. Appendix C, Rate Plan, A. Rate Filings, 5., page 1: "KCPL shall make a 2009 rate filing that proposes new rate schedules with an effective date of June 1, 2010. . . ."

KS. Appendix C, Rate Plan, A. Rate Filings, 7., page 2: "The parties to this Agreement will not initiate a proceeding at the Commission requesting a change in KCPL's rates during the Rate Plan except the rate cases contemplated above unless at least one of the contingencies listed below applies. . . . (f) It is determined that KCPL failed to provide the Non-KCPL parties with material and relevant information in its possession . . ."

(13) KS. Appendix C, Rate Plan, B. Energy Cost Adjustment, page 2: " . . . Should any special contracts with customers exclude the ECA, the ECA computation shall take into account the sales associated with the contract determining the appropriate ECA."

(14) KS. Appendix C, Rate Plan, C. Off-System Sales, page 3: " . . . KCPL specifically agrees not to propose any adjustment or modification that would remove any portion of its off-system sales costs and revenues from being passed through the ECA mechanism. . . . "

(15) KS. Appendix C, Rate Plan, E. Pension Expense, 4., page 6: "In addition, non-KCPL parties reserve the right to propose a different methodology for addressing FASB 87 pension expense in the first KCPL rate case proceeding after 2010. In the event that the Commission addresses FASB 87 pension expense in a general investigation, KCPL agrees to cooperate in such investigation and be bound by the results thereof in rate proceedings subsequent to 2010."

(16) KS. Appendix C, Rate Plan, F. Customer Programs, page 6: "In calendar years 2005 through 2009, KCPL commits to implement the Demand Response, Efficiency and Affordability programs detailed in Appendix B, subject to the continuing review and prior approval of the Commission on a program-by-program basis. No program will be implemented until such approval has been obtained. . . ."

(17) KS. Appendix C, Rate Plan, G. AFUDC, Construction Accounting And In-Service Criteria, page 7:

"1. AFUDC. With regard to the AFUDC rate applicable to Iatan 2, KCPL agrees to a 2.5% or 250 basis point reduction in the equity portion of the rate. KCPL shall use this 250 basis point reduction in the equity portion of the rate. KCPL shall use this 250 basis point reduction in the AFUDC rate from the effective date of the rates determined in the first rate case (anticipated to be January 1, 2007) and in all subsequent calculations of AFUDC on Iatan 2 until the in-service date of Iatan 2. KCPL shall submit a report to Staff at the beginning of each calendar year during this plan of the AFUDC rates it will use and the calculation thereof."

"2. Construction Accounting. The accrual of AFUDC on new investments shall cease when such plant is considered in service. This specifically precludes any 'Construction Accounting' permitted in other jurisdictions that provides for continued accrual of AFUDC after Iatan 2 is considered in-service until the plant is reflected in rates."

"3. In-Service Criteria. For purposes of determining whether the new generation resources are in service, the parties should use the same criteria as used by the Southwest Power Pool for accreditation. Criteria for determining whether the new emissions control equipment is in service shall be developed by the parties."

(18) KS. Appendix C, Rate Plan, I. Other Conditions, 1. Rate treatment of investments, page 8:

"(c) The non-KCPL parties reserve their rights to review KCPL's decisions regarding its partners in the Iatan 2 plant and assert that such decisions resulted in higher costs that should not be allowed for rate purposes."

(d) The non-KCPL parties reserve the right to oppose adjustments to revenue requirements regarding the prudence of the installed cost, operation and maintenance costs or KWH output of the wind generation as opposed to the costs or output of comparable wind generation facilities.

(e) The parties have not waived their right to argue regarding issues provided for under KSA 66-128."

(19) KS. Appendix C, Rate Plan, I. Other Conditions, 3. Deregulation, page 8:

"KCPL recognizes that if generation assets are deregulated in the future, it is at risk for recovery of stranded costs related to the acquisition of the new generation. Furthermore, KCPL

acknowledges that ratepayers would be entitled to a greater share of a gain on the disposition of the new generation upon deregulation due to possible implementation of the CIAC mechanism."

(20) KS. Appendix C, Rate Plan, I. Other Conditions, 7. Costs of Debt:

"For purposes of determining the cost of debt in the rate proceedings during the plan, the lower of the actual cost of debt or the cost of debt for an investment grade rating will be used."

(21) KS. Appendix C, Rate Plan, I. Other Conditions, 8. Jurisdictional Allocations:

"The parties agree to use the 12 Coincident Peak method of allocating costs to the Kansas jurisdictional cost of service."

(22) KS. Appendix C-1, SO_2 Emission Allowance Management Policy, SO_2 Plans, page 2: ". . . The KCC Staff and Curb will be notified if transactions not included in the annual SO_2 Plan exceed the projections by 50, 000 allowances or more."

The Appendix filed with the KCC reflects an earlier iteration of the Missouri KCPL Regulatory Plan SO_2 Emission Allowance Management Policy (SEAMP).

ATTACHMENT 3

In *Re Kansas City Power & Light Co.*, Case No. ER-78-252, 23 Mo.P.S.C.(N.S.) 1, 22-23 (1979), the KCPL rate increase case immediately preceding the Iatan 1 in commercial operation case, Case No. ER-80-48, the Commission authorized normalization due to the level of the relevant financial ratios of KCPL:

> . . . but the question remains whether the Commission should reverse its past practice of requiring Company to flow through the items at issue and permit Company to normalize them in the future. Hence, the Commission must determine whether or not Company meets the financial stability test included in the Report and Order in Case No. ER-77-118. This test involves an examination of Company's test year coverage ratios, cash flow and the amount of external financing required to meet Company's construction expenditures.
>
> Company Exhibit No. 31, Schedule 4, shows Company's test year coverage ratios for bonds and preferred stock of 2.53 and 1.54, respectively. Though the coverage ratio of 2.53 for first mortgage bonds would permit Company to issue additional bonds, the coverage requirement for preferred stock of 1.50 would not permit any significant sale of additional preferred stock because the additional dividends resulting from the sale would drive the test year coverage ratio below 1.5. Likewise Company Exhibit No. 31, Schedule 2 indicates that only 20.7 percent of Company's construction expenditures and debt refundings during the test year were provided by internally generated funds. Company witness testified that the utility industry on average meets 35 percent to 40 percent of its construction expenditures with internally generated funds with the balance represented by external funds such as new issues of bonds, preferred stock, and common stock.
>
> The Commission finds that test year results do demonstrate that Company has a severe cash flow problem. During a period of heavy construction expenditures, the Commission would expect the percentage of construction expenditures provided by internally generated funds to decline from the 40 percent norm, but a decline below 30 percent must be viewed as a serious impediment to continuing Company's construction program, at least at budgeted levels. Staff raised the question whether normalization of the items at issue would significantly improve either Company's cash flow or its coverage ratios. However, the financial stability test as applied to this issue does not require normalization to solve a company's cash flow problems, only alleviate them. Therefore, the Commission finds that Company should be allowed to normalize the pension costs, payroll and property taxes which it capitalizes on its books. The Commission also finds that a corresponding offset to rate base in the amount of one-half of the tax liability associated with the items at issue should also be made on the basis that one-half of that liability represents the average additions to rate base which could be

> funded by the proceeds from this issue during the first year in which new rates are in effect.

A subsequent 1979-1980 Commission case involving KCPL is instructive respecting the criteria that the Commission has required for granting interim rate relief, including an explanation of the financial ratios that it has looked to in order to determine whether, and how much, interim rate relief is warranted.[1] In *Re Kansas City Power & Light Co.*, Case No. ER-80-204, Report And Order, 23 Mo.P.S.C.(N.S.) 413 (1980), Commission granted interim rate relief to KCPL on the basis of the Commission's own determination that KCPL's financial position impaired KCPL's financial integrity. KCPL's articles of consolidation required its gross income to be equal to at least one and one half times (1.5x) all interest charges on indebtedness and dividends on its outstanding and proposed preferred stock in order for it to be permitted to issue additional preferred stock. KCPL's coverage was 1.31x so it could not issue additional preferred stock. KCPL's indenture of mortgage and deed of trust required net earnings to be at least two times (2.00x) annual interest charges on its outstanding and proposed first mortgage bonds in order for it to be permitted to issue additional first mortgage bonds. KCPL's coverage was 1.50x so it could not issue additional first mortgage bonds. The Commission commented in its Report And Order that "coverage requirements are not to be construed as a credit rating test." 23 Mo.P.S.C.(N.S.) at 416.

Although the Commission found in the case that there were no restrictions concerning KCPL issuing preference stock, it noted that if KCPL were to do so, it would give KCPL more equity in its capital structure than was considered prudent at capital markets. This situation led

[1] The Commission has set out the interim relief standard in a number of cases including *Re Missouri Public Service Co.*, Case No. 18,502, 20 Mo.P.S.C.(N.S.) 244, 250 (1975) where it stated that:

> . . . it is incumbent upon the Company to demonstrate conclusively that an emergency does exist. The Company must show that (1) it needs additional funds immediately, (2) that the need cannot be postponed, and (3) that no other alternatives exist to meet the need but rate relief.

the Commission to find that if preference stock could be marketed, the cost and terms would be unreasonable and prohibitive. 23 Mo.P.S.C.(N.S.) at 416. In addition, the Commission noted that KCPL exceeded its short term lines of credit, and even though it was possible that short-tem credit could be increased through compensating bank balances or fees, it would not be an advantageous approach given that the prime lending rate then exceeded 18%. *Id.* at 416-17.

For the calendar year 1979, all monies utilized by KCPL for construction had been supplied by external sources, thus the Commission stated that KCPL's elimination of its construction program would not affect its cash flow situation. KCPL's common stock was selling at approximately 60% of book value. 23 Mo.P.S.C.(N.S.) at 417. For the nine months ending December 1979, KCPL paid out approximately $12.0 million more for operating expenses than it received from its customers in payment of services rendered. The Commission commented that the profit of the company was negative. *Id.* at 416-17. The Commission also found that an indicia of an emergency situation was exhibited by the fact that KCPL had adopted an austerity program.[2] *Id.* at 417.

KCPL proposed to sell $50.0 million of first mortgage bonds in December 1980 and in order to do so would need to have the 2.00x interest coverage by the end of October 1980. KCPL projected that if it were to receive $30.0 million in interim rate relief in March or April 1980, it would by September 1980 have the interest coverage necessary to issue $50.0 million of new first mortgage bonds in December 1980, assuming it received permanent rate relief by July 1980 to supersede the interim rate relief. With permanent rate relief in July 1980, but no interim

[2] The components of the KCPL austerity program were: (1) a hiring freeze; (2) a reduction in the amount of overtime; (3) a reduction in business travel and meetings; (3) a reduction in the amount of advertising; (4) a reduction in fuel inventory levels; (5) a possible change to using gas fuel in Hawthorn III and IV boilers rather than a combination of coal and gas; (6) a possible reduction in maintenance on the Northeast generating unit; (7) modification of the 1980 construction budget through cancellation of projects or deferrals through 1981 and beyond; (8) reductions in distribution construction; (9) reductions in transmission and distribution maintenance; and (10) miscellaneous areas for other cost deferrals. *Id.* at 417.

rate relief in March or April 1980, KCPL projected that it would not have the necessary interest coverage before February or March 1981 that it would achieve in September 1980 if it received interim rate relief. 23 Mo.P.S.C.(N.S.) at 417. The Commission authorized interim rate relief in the amount of $25.0 million. *Id.* at 418-19.

Reflecting the Commission's often general discussion of its criteria for granting interim rate relief, the Courts in the cases where this Commission authority has been judicially recognized have also noted the Commission's criteria in general terms. The Western District Court of Appeals in *State ex rel. Laclede Gas Co. v. Public Serv. Comm'n*, 535 S.W.2d 561, 568-69 (Mo.App. 1976) related that the Commission has applied an emergency standard of granting interim relief in advance of the processing of a permanent rate case "'where a showing has been made that the rate of return being earned is so unreasonably low as to show such a deteriorating financial condition that would impair a utility's ability to render adequate service or render it unable to maintain its financial integrity.'" As can be seen regarding Case No. ER-80-204, the Commission's criteria is based in part on financial ratios.

In *State ex rel. Laclede Gas Co. v. Public Serv. Comm'n*, 535 S.W.2d 561 (Mo.App. 1976), in addressing the power of the Commission to grant interim relief the Court noted the broad discretion that the Commission has respecting the setting of rates:

> The 'file and suspend' provisions of the statutory sections quoted above lead inexorably to the conclusion that the Commission does have discretionary power to allow new rates to go into effect immediately or on a date sooner than that required for a full hearing as to what will constitute a fair and reasonable permanent rate. This indeed is the intended purpose of the file and suspend procedure. Simply by non-action, the Commission can permit a requested rate to go into effect. Since no standard is specified to control the Commission in whether or not to order a suspension, the determination as to whether or not to do so necessarily rests in its sound discretion.

535 S.W.2d at 566

> We hold that **the Commission has power in a proper case to grant interim rate increases within the broad discretion implied from the Missouri file and suspend statutes and from the practical requirements of utility regulation**.

535 S.W.2d at 567; emphasis supplied.

In addressing the standard for granting interim rater relief, the Court rejected Laclede's argument that earning a rate of return lower than that which had been set previously by the Commission was unreasonable:

> This same basic argument has been presented to a number of courts through the country and the judicial reaction has been divergent. However, the majority and better view rejects the argument that any return less than the rate previously set must be deemed prima facie unreasonable. . . .

535 S.W.2d at 570. The Court broadly addressed other factors that might be considered in finding a basis for awarding interim rate relief and noting that these factors did not apply to Laclede:

> . . . There remains only to review briefly the factors shown by the record which affirmatively support the Commission's declination to grant an interim increase and which amply show that declination to be at least reasonably debatable.
>
> . . . Laclede was able to serve its customers, it had continued to pay dividends to its stockholders, **its bond coverage continued to be in excess of the coverage required by its bond indentures**, and it ran no risk of a lowering of its bond rating during the period of maximum suspension pending completion of the permanent rate hearing. . . .

Id. at 573; emphasis supplied. The Court held that conceivably there were situations which would warrant the awarding of interim rate relief other than the narrow emergency criteria adopted and adhered to by the Commission:

> It may be theoretically possible even in a purposefully shortened interim rate hearing for the evidence to show beyond reasonable debate that the applicant's rate structure has become unjustly low, without any emergency as defined by the Commission having as yet resulted. Although some future applicant on some extraordinary fact situation may be able to succeed in so proving, Laclede has singularly failed in this case to carry the very heavy burden of proof necessary to do so.

Id. at 574.

In the subsequent *State ex rel. Fischer v. Public Serv. Comm'n*, 670 S.W.2d 24 (Mo.App. 1984), the Western District Court of Appeals in discussing interim rate increases also noted the emergency criteria in general terms:

> **. . .** the Commission's authority to grant an interim rate increase is necessarily implied from the statutory authority granted to enable it to deal with a company in which immediate rate relief is required to maintain the economic life of the company so that it might continue to serve the public.

Id. at 26.

In the recent past, it has been asserted to the Commission that on several occasions the Commission has utilized a standard for interim rate relief other than the emergency standard. In its March 8, 2001 Order Rejecting Tariffs And Granting Motion To Dismiss in *Re Empire District Electric Co.*, Case No. ER-2001-452, 10 Mo.P.S.C.3d 124, 126 n.2 (2001), the Commission rejected this assertion stating as follows:

> As Empire notes in its pleadings, the Commission did partially develop a "good cause" standard for interim relief in *In Re The Empire District Electric Company*, 6 MoPSC 3rd 17 (Case No. ER-97-82). However, in that case the Commission based its denial of Empire's request on its conclusion that: "There is no showing by the Company [Empire] that its financial integrity will be threatened or that its ability to render safe and adequate service will be jeopardized if this request is not granted." The differences, if any, between this good cause standard and the historically applied emergency or near emergency standard were not clearly annunciated, and the Commission now returns to its historic emergency or near emergency standard.

But a year later, the Commission revived the matter of the "good cause" standard in a new Empire interim rate relief case stating as follows in *Re Empire District Electric Co.*, Case No. ER-2002-425, Order Rejecting Tariff And Granting Motion To Dismiss, 11 Mo.P.S.C.3d 280, 283 (2002):

> . . . The Commission has the authority, as Empire argues, to grant nonemergency relief by applying a case-by-case standard.[8] Empire has not, however, demonstrated facts that justify the "good cause" standard, and the Commission determines that it shall continue to follow its historical emergency standard for interim rate relief.

[8] *State ex rel Arkansas Power & Light Company v. Public Service Commission*, 736 S.W. 2d 457 (Mo. App. 1987). [The Western District Court of Appeals noted that the Commission regulates on a case by case basis, unbound by *stare decisis*:

> > . . . the PSC can use a new equation or change methods from case to case depending on the facts. There is no per se requirement the Commission must use the same formula on successive applications by the same company. . . . The Commission is not bound to a single formula, and where there is competent and substantial evidence to support the methodology used, a reviewing court is in no position to reverse.
> >
> > . . . No methodology being statutorily prescribed, and ratemaking being an inexact science, requiring use of different formulas, the Commission may use different approaches in different cases. *Associated Natural Gas*, *supra*, at 880.]

[736 S.W.2d at 462; *Accord State ex rel. GTE North, Inc. v. Public Serv.Comm'n,* 835 S.W.2d 356, 371-72 (Mo.App. 1992).]

Empire in its 2001 interim relief rate case filing asserted a need for immediate rate relief driven by expected increases in natural gas prices and the projected in-service date of a new combined cycling unit. 10 Mo.P.S.C.3d at 124. The Commission related that Empire did not allege inability to finance its operations or negative earnings, but rather that a dip in its returns might influence credit rating agencies, which in turn could affect its cost of new debt and ability to raise equity capital. The Commission, in commenting that Empire's witnesses did not provide an explanation of how a possible increase in its cost of capital could impair Empire's ability to provide safe and reliable electric service to its customers, rejected Empire's proposed interim tariff and granted Public Counsel's motion to dismiss. *Id.* at 125-26.