

**STATE OF MISSOURI
PUBLIC SERVICE COMMISSION**

At a session of the Public Service
Commission held at its office in
Jefferson City on the 28th day of
November, 2006.

Application of Aquila, Inc., for an Order Authorizing)	
Applicant (if and to the Extent the Transaction)	
Described Herein Would Impose a Mortgage or)	
Encumbrance under Section 393.190, (RSMo)) to)	
Execute, Deliver and Perform the Agreements and)	
Instruments Necessary to Assume a Lease and Related)	<u>Case No. EO-2007-0172</u>
Documents Pertaining to the Aries Combustion)	
Turbine Generator Facility Owned by a Subsidiary of)	
Calpine Corp. and Cass County, Which Was)	
Constructed as Part of a Revenue Bond Project under)	
Chapter 100 RSMo)	

ORDER DISMISSING APPLICATION FOR LACK OF JURISDICTION

Issue Date: November 28, 2006

Effective Date: December 8, 2006

Syllabus: This order dismisses Aquila, Inc.'s application because the Missouri Public Service Commission finds it lacks jurisdiction to enter a dispositive order in this matter.

Background

On September 22, 2006,¹ Aquila, Inc. ("Aquila") entered into an Asset Purchase and Sale Agreement ("APA") with MEP Pleasant Hill, L.L.C. to acquire the Aries Facility, a 580 megawatt gas-fired combined cycle electric generating facility in Pleasant Hill, Cass County, Missouri. MEP is a wholly owned subsidiary of Calpine Corporation. Calpine and its debtor affiliates, including MEP, filed for bankruptcy relief in the United States

¹ All dates throughout this order refer to the year 2006 unless otherwise noted.

Bankruptcy Court for the Southern District of New York. The sale of the Aries Facility has been following a time line set by the Bankruptcy Court, and the Bankruptcy Court's Sale Order is expected to be issued on December 11.

The Aries Facility has been in commercial operation as part of an Industrial Revenue Bond project approved by Cass County, Missouri, pursuant to Chapter 100, RSMo 2000.² Under this arrangement, the County issued a single taxable industrial revenue bond in connection with the purchase and construction of the Aries Facility. Cass County owns the Aries Facility, and because the municipality owns the project, it is exempt from property taxes. Cass County leases the facility to MEP. The Lease requires MEP to operate and maintain the Aries Facility and, pursuant to an Economic Development Performance Agreement, make specified payments in lieu of taxes ("PILOT payments") to the County. MEP, as the lessee, makes its lease payments to Cass County, and these payments fund all payments by the County to the bondholder. In this instance, MEP also purchased the Bond so the Chapter 100 bond arrangement has no economic substance except for eliminating property tax liabilities to encourage economic development.

Aquila's Application

On October 31, 2006, Aquila, Inc., ("Aquila") filed an application with the Commission seeking a determination that assumption of the lease and related documents pertaining to the purchase of the Aries combustion turbine facility ("Aries Facility") in Cass County, Missouri, did not require Commission approval pursuant to Section 393.190. In the alternative, Aquila seeks expedited approval of its APA, by December 8, so that it may purchase the Aries Facility in accordance with the APA. The Commission issued notice

² All statutory citations reference RSMo 2000 unless otherwise noted.

and set a deadline for requests for intervention or for a hearing. No requests for intervention or for a hearing were filed.³

Aquila states it will pay \$158,500,000 in cash to assume MEP's rights and obligations under the Lease and acquire all of MEP's rights, title and interest in the Bond. Exhibit 7 to Aquila's application, its Consolidated Balance Sheet, reveals that the company's cash and equivalents total \$201,100,000, thus reflecting adequate funds to execute the transaction. The Balance Sheet also records a negative "Pro Forma Adjustment" for the Aries transaction resulting in a balance of cash and cash equivalents after the sale totaling \$42,600,000.

Aquila asserts that this transaction does not dispose of, or encumber the whole or part of its franchise, works, or system, necessary or useful in the performance of its duties to the public, and therefore believes the transaction does not require Commission approval pursuant to Section 393.190. Aquila contends that its ratepayers will benefit from the transaction because the PILOT payments will be substantially less than the property taxes it would be required to pay if it acquired the Aries Facility without entering the Chapter 100 bond arrangement.

Aquila also maintains that because it will own the Bond, and because the transaction requires no substantive financing, that it will not incur any indebtedness that would need to be recorded on its accounting books. Instead, Aquila will record an amount matching the acquisition cost of the Aries Facility as being part of its net utility plant assets. Aquila

³ Although MEP is a party to the APA, they did not join in the application. Consequently, On November 1, the Commission added MEP as a necessary party to have a full and fair adjudication of this matter, issued notice and set an intervention schedule. The Commission also directed that any requests for a hearing should be filed by November 13. No requests for intervention or for a hearing were filed.

further asserts that even if the Commission would construe the APA as creating long-term indebtedness, that Aquila, being a Delaware corporation, does not require Commission approval to incur long-term indebtedness. Aquila cites to *Public Service Commission v. Union Pacific Railroad Company* in support of this latter proposition.⁴

Staff Recommendation

The Staff of the Missouri Public Service Commission filed its verified Recommendation and Memorandum on November 22. Staff does not directly address the issue of the Commission's jurisdiction over this matter. Instead, Staff states: "Further, similarly to how the parties requested the Commission to act in Case Nos. EA-2006-0499 and EA-2006-0500 regarding certificates of convenience and necessity for substations, the Staff notes that, even if the Commission does not have jurisdiction over the transaction in question here, no harm will be caused by the Commission authorizing Aquila, Inc. to engage in this transaction—Staff's conditional recommendation in this case."⁵

⁴ *Public Service Commission v. Union P.R. Co.*, 197 S.W.39, 42 271 Mo. 258,268-270 (Mo. Banc 1917).

⁵ Case Nos. EA-2006-0499 and EA-2006-0500 involved applications by Aquila to obtain permission, approval and certificates of public convenience and necessity authorizing Aquila to acquire, construct, install, own, operate, maintain, and otherwise control and manage electrical distribution substations and related facilities to be located within Jackson County, near the City of Raymore, Missouri, and in unincorporated St. Clair County, near the City of Osceola, Missouri. In these cases, the jurisdictional issue centered around whether the Western District's opinion in *StopAquila.org v. Aquila, Inc.*, 180 S.W.3d 24 (Mo. App. 2005), created uncertainty as to whether an electric utility could lawfully construct and operate any electrical substation within the utility's certificated service area without first obtaining a § 393.170.1, RSMo. certificate of convenience and necessity from the Commission. Certain parties to these actions believed that Commission certification was not required, but all of the parties agreed that the granting of a "footprint" certificate was not harmful and would serve the need for expedited construction of the substations in question. Consequently, the parties agreed that the Commission should authorize the projects and did not contest the Commission's jurisdiction in these matters.

Based upon prior case law and prior decisions by the Commission, Staff believes the appropriate standard for approval of Aquila's application is whether the proposed transaction is "not detrimental to the public interest." Staff asserts that, based on its review of the transaction and its investigation, it found no issues such as encumbrances on the facility (other than those in connection with the Chapter 100 financing), compliance of the facility with zoning requirements, or other legal challenges that would affect the legality of the facility or similar matters such as those Aquila, Inc., has encountered with respect to its South Harper combustion turbine generating facility. Staff concludes that the transaction has the potential to result in lower rates to customers and property tax savings to Aquila and that the proposed transaction would not be detrimental to the public interest.

Based on its review, the Staff recommends the Commission approve Aquila, Inc.'s application, subject to the following conditions:

A. Aquila shall continue to record the land and improvements (combined cycle unit) that are the subject of this transaction as a regulatory asset on its books similar to other utility property it owns.

B. Aquila shall record the investment described above in accordance with the Uniform System of Accounts as adopted by this Commission for recordkeeping purposes.

C. Aquila shall depreciate the combined cycle unit plant accounts at the following annual rates:

i. Account No. 341 (Structures & Improvements): 1.67% (ASL: 60 years);

ii. Account No. 342 (Fuel Holders, Producers & Accessories): 2.50% (ASL: 40 years);

iii. Account No. 343 (Prime Movers): 3.03% (ASL: 33 years);

iv. Account No. 344 (Generators): 3.03% (ASL: 33 years);

v. Account No. 345 (Accessory Electric Equipment): 2.50% (ASL: 40 years);

vi. Account No. 346 (Miscellaneous Power Plant Equipment): 2.86% (ASL: 35 years).

These depreciation rates are the depreciation rates Staff will propose in the current rate case, Case No. ER-2007-0004 if Aquila successfully acquires the Aries combined cycle unit. On a composite basis they approximate the 2.86% depreciation rate (35 year ASL) ordered in The Empire District Electric Case No. 2004-0570 for the combined cycle unit plant accounts.

D. Aquila shall book each payment in lieu of tax ("PILOT") to operating expense during the remaining term of the Chapter 100 financing arrangement, as each annual payment is made.

E. No ratemaking determination is being made by the Commission in this proceeding and no party to this case has acquiesced to any present or future ratemaking treatment as it relates to this transaction. The ratemaking treatment of this transaction may be addressed in Aquila's next rate case or the Staff's next earnings complaint case, but no ratemaking treatment is being sought by Aquila in this proceeding.

F. Aquila shall seek and obtain Commission approval before it transfers any of the rights it holds pursuant to the lease where such rights are necessary or useful in the provision of regulated utility service, including the right to purchase the facility at the end of the lease.

G. Aquila shall not sell its rights to the Bond Purchase Agreement acquired through its acquisition of the Aries Facility without Commission approval.

Discussion

Section 393.190.1 provides, in pertinent part:

No gas corporation, **electrical corporation**, water corporation or sewer corporation **shall hereafter sell, assign, lease, transfer, mortgage or otherwise dispose of or encumber the whole or any part of its franchise, works or system, necessary or useful in the performance of its duties to the public**, nor by any means, direct or indirect, merge or consolidate such works or system, or franchises, or any part thereof, with any other corporation, person or public utility, without having first secured from the commission an order authorizing it so to do. Every such sale, assignment, lease, transfer, mortgage, disposition, encumbrance, merger or consolidation made other than in accordance with the order of the commission authorizing same shall be void.

It is clear that if Aquila executes the APA, it would not be selling, assigning, leasing, transferring, or mortgaging the whole or any part of its franchise, works or system, necessary or useful in the performance of its duties to the public. The issue of the Commission's jurisdiction pursuant to Section 393.190 rests on whether this transaction would "encumber" any part of Aquila's assets that are necessary or useful in the performance of its duties to the public.

Aquila represents that the APA will be consummated with a cash transaction. Its Consolidated Balance Sheet reflects sufficient cash and cash equivalents to cover the \$158,500,000 purchase price to assume MEP's rights and obligations under the Lease and acquire all of MEP's rights, title and interest in the Bond. Staff's investigation did not reveal any type of financing arrangements that would result in Aquila encumbering the whole or any part of its franchise, works or system. There is no evidence in the record before the Commission to support the contention that Aquila has encumbered any Missouri rate-based assets that are necessary or useful to meet the public needs, as is required for the Commission to assert its jurisdiction pursuant to Section 393.190.

Aquila's also contends that even if the Commission would construe the APA as requiring Aquila to issue some form of long-term indebtedness, that Aquila, being a Delaware corporation, does not require Commission approval to incur long-term indebtedness. This position has merit, although the case cited by Aquila to support this proposition is not particularly persuasive. In *Union Pacific Railroad*, the court was interpreting Sections 54, 55 and 57 of the Public Service Act of 1913 and ultimately held

that the railroad could sell bonds without the approval of the Commission.⁶ The court reasoned that to hold otherwise would constitute an interference with interstate commerce.⁷

The Commission no longer regulates railway companies and the current statute pertaining to the regulation of indebtedness of electric corporations is Section 393.200, a statute which has not been construed by Missouri courts to stand for the same proposition articulated in *Union Pacific*.⁸ However, Section 393.200 expressly applies to only those corporations “organized or existing or hereinafter incorporated under or by virtue of the laws of this state.”

Recently, in Case No. EO-2005-0156, *In the Matter of the Application of Aquila, Inc. for Authority to Acquire, Sell and Lease Back Three Natural Gas-Fired Combustion Turbine Power Generation Units and Related Improvements to be Installed and Operated in the City of Peculiar, Missouri*, the Commission dismissed the portion of Aquila’s application asking for approval of a Chapter 100 financing arrangement finding that it had no jurisdiction pursuant to Section 393.190. The Commission also examined whether Section 393.200 applied and stated:

A Missouri electrical corporation must seek Commission approval to issue debt; Aquila is not a Missouri electrical corporation. A Missouri electric corporation needs Commission approval before issuing debt that is based upon assets that necessary or useful to meet the public needs.⁹

⁶ *Public Service Commission v. Union P.R. Co.*, 197 S.W.39, 42 271 Mo. 258,268-270 (Mo. Banc 1917).

⁷ *Id.*

⁸ In *Public Service Commission v. Union P.R. Co.*, 197 S.W.39, 42 271 Mo. 258,268-270 (Mo. Banc 1917), the court examined Section 57 of the Public Service Commission Act of 1913, entitled *Approval of Issues of Stocks, Bonds and Other Forms of Indebtedness*. The corollary statute applicable to electric companies at that time was in Article IV, Section 75. Section 75 from 1913 is essentially identical to the current version of Section 393.200 RSMo 2000, excepting that sewer corporations were not included in Section 75.

⁹ *In the Matter of the Application of Aquila, Inc., for Authority to Acquire, Sell and Lease Back Three Natural Gas-Fired Combustion Turbine Power Generation Units and Related Improvements to be Installed and Operated in the City of Peculiar, Missouri*, Case No. EO-2005-0156.

Aquila is not a Missouri corporation and there is no evidence in the record to support the contention that Aquila has issued debt encumbering any Missouri rate-based assets that are necessary or useful to meet the public needs in order to execute the APA. No other statutory authority exists that confers jurisdiction upon the Commission for the regulation of a foreign electric corporation's long-term indebtedness, if that indebtedness does not encumber Missouri rate-based assets that are necessary or useful to meet the public needs.

Decision

The Commission has reviewed the parties' verified pleadings, which are hereby admitted into evidence. Pursuant to Commission Rule 4 CSR 240-2.080(16), the Commission shall grant Aquila's motion for expedited treatment because of the Bankruptcy Court's time-table for issuing a final ruling on the sale. The Commission shall also dismiss Aquila's application finding that it lacks jurisdiction pursuant to Sections 393.190 and 393.200 to issue a dispositive order in this matter.

IT IS ORDERED THAT:

1. The motion for expedited treatment filed by Aquila, Inc., is granted.
2. The application filed by Aquila, Inc., on October 31, 2006, seeking an order authorizing it to execute, deliver and perform the agreements and instruments necessary to assume a lease and related documents pertaining to the Aries combustion turbine generator facility, assigned case number EO-2007-0172, is dismissed for lack of jurisdiction.
3. Nothing in this order shall be considered a finding by the Commission of the reasonableness or prudence of the expenditures herein involved, or of the value for

ratemaking purposes of the properties herein involved, nor as acquiescence in the value placed on said property.

4. The Commission reserves the right to consider the ratemaking treatment to be afforded the properties herein involved, and the resulting cost of capital, in any later proceeding.

5. This order shall become effective on December 8, 2006.

6. This case may be closed on December 9, 2006.

BY THE COMMISSION

A handwritten signature in black ink, appearing to read 'Colleen M. Dale', written over a horizontal line.

Colleen M. Dale
Secretary

(S E A L)

Davis, Chm., Murray and Appling, CC., concur
Gaw and Clayton CC., dissent

Stearley, Regulatory Law Judge