BEFORE THE PUBLIC SERVICE COMMISSION
STATE OF MISSOURI

In the Matter of the Joint Application of Great Plains Energy Incorporated, Kansas City Power & Light Company, and Aquila, Inc., for Approval of the Merger of Aquila, Inc., with a Subsidiary of Great Plains Energy Incorporated and for Other Related Relief	))))))))	**Case No. EM-2007-0374**

STAFF AND INDUSTRIAL INTERVENORS' PROPOSED FINDINGS OF FACT AND CONCLUSIONS OF LAW

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The following is not a complete procedural history, but includes events of note that the Staff thinks should be in the Report And Order.

Procedural History

On April 4, 2007 Great Plains Energy, Inc. (Great Plains), Kansas City Power & Light Company (KCPL, a wholly-owned subsidiary of Great Plains) and Aquila, Inc. (Aquila) (jointly Joint Applicants) filed a joint application with the Public Service Commission of Missouri (Commission) for authority to engage in transactions whereby Aquila would become a wholly-owned subsidiary of Great Plains. In the Joint Application, as part of their request, they sought approval of a regulatory plan that, among other things, would allow the use of additional amortizations to maintain credit ratios in Aquila's next general rate case after achieving the financial metrics necessary to support an investment-grade credit rating—anticipated on closing, recovery from ratepayers of Aquila's actual debt cost, recovery of transaction costs, and recovery from ratepayers of fifty percent (50%) of presumed synergy savings over five years.

On April 9, 2007 the Commission issued an order in which it directed that notice of the joint application be given to designated entities, set an intervention date of April 30, 2007 and directed the Commission's staff to file a recommendation, status report or request a prehearing conference. The following parties sought and were allowed to intervene:

In response to the Commission's April 9, 2007 order, the Commission's staff stated it needed more information to evaluate the joint application and recommended that technical and prehearing conferences be held. The Commission ordered the conferences be held on May 23 and 24, 2007, respectively. The Commission also ordered the parties to file their positions and a proposed procedural schedule by May 31, 2007. On June 5, 2007, the Staff of the Commission, on behalf of the parties, filed a proposed procedural schedule for this case. Among other things, that schedule included the Joint Applicants filing on August 8, 2007 supplemental direct testimony on the topics of updated synergy analysis, elimination/retention of employee positions, and quality of service and customer service center; the other parties filing their rebuttal testimony to all the Joint Applicants' direct testimony on October 12, 2007; the filing of all surrebuttal testimony on November 14, 2007; and evidentiary hearings on December 3-7 and 10-14, 2007. By order dated June 19, 2007, the Commission, with the exception of the proposed briefing schedule and position statements, adopted the proposed procedural schedule.

The evidentiary hearings began on December 3, 2007. On December 5, 2007 the Industrial Intervenors filed a motion for partial summary determination challenging the Joint Applicants' request for a regulatory amortization on the basis it violated section 393.135, RSMo. 2000. On December 6, 2007, the Joint Applicants requested that the evidentiary hearing be recessed so that they could attempt to address concerns raised during the hearing by certain parties, as well as Commissioners, about some of the proposals contained in the Joint Application and in the pre-filed testimony of the Joint Applicants by presenting an "alternative proposal" to the other parties. There was no objection to this request and the Commission continued the hearing.

On December 13, 2007 Public Counsel moved to dismiss this case on the basis of alleged meetings by the Joint Applicants with Commissioners, held without public notice and in circumvention of the Sunshine Law, that created actual or the appearance of impropriety which rendered the Commission an ineffective tribunal in this case. By order dated January 2, 2008 the Commission denied the motion. Public Counsel filed its motion for reconsideration on January 11, 2008, and the Commission denied reconsideration on January 24, 2008.

On December 13, 2007 the Commission ordered a settlement conference on December 19, 2007, and directed the parties, separately or jointly, to file a revised proposed procedural schedule by 3:00 p.m. on December 21, 2007. The settlement conference was held as scheduled.

By filings dated December 14, 2007, December 21, 2007 and January 10, 2008, the Joint Applicants requested extensions of time to file a revised proposed procedural schedule, or settlement, to permit an opportunity for settlement with the parties. The Commission granted each request. On January 31, 2008 the Joint Applicants proposed a revised procedural schedule in which they, among other things, suggested, that although settlement discussions were taking place, hearings reconvene March 17-21 and 24-28, 2008. Public Counsel, Commission staff and the Industrial Intervenors filed a response requesting until February 13, 2008, after the Joint Applicants proposed to present their revised plan to the Commission, to respond to the proposed revised procedural schedule and indicating they could not both prepare for hearing and engage in settlement discussions. Thereafter, on February 6, 2008, the Joint Applicants requested leave to withdraw their proposed revised procedural schedule and, instead, file a status report by February 20, 2008 if a settlement proposal was not presented to the Commission by then. On February 14, 2008, the Commission ordered the Joint Applicants to file by February 20, 2008 a status report about settlement negotiations, the extent the relief requested would change and procedural matters.

The Joint Applicants timely filed the status report asserting they planned to revise their original proposal only by removing certain requests, which would be revealed in additional testimony they proposed to file February 25, 2008, and they proposed the following procedural schedule:

February 25, 2008 Joint Applicants' Additional Supplemental Direct Testimony

March 24, 2008 Rebuttal Testimony

March 31, 2008 Surrebuttal Testimony of Joint Applicants and Cross Surrebuttal

April 15, 2008 List of Issues and Order of Witnesses

April 21-May 2, 2008 Evidentiary Hearings

Public Counsel, the Commission's Staff and the Industrial Intervenors responded by suggesting a prehearing conference be held on February 28, 2008.

On February 25, 2008, with a motion for leave to do so, the Joint Applicants filed testimony and advised the Commission they were withdrawing certain relief they had requested. They asserted they were no longer requesting the following:

- Aquila Interest Expense: Joint Applicants do not seek to recover in any future general ratemaking proceeding any interest expense in excess of equivalent investment-grade debt that is currently held by Aquila.
- Merger Savings: Joint Applicants do not request a specific merger savings sharing mechanism, but rather will rely upon the traditional regulatory ratemaking process so that any merger savings will be passed through to Aquila and KCPL customers in future rate cases.
- Regulatory Amortizations: Joint Applicants do not request authority in this proceeding for Aquila to use regulatory "Additional Amortizations" to maintain the investment-grade credit rating that Aquila anticipates receiving upon approval of its acquisition by Great Plains Energy.
- Aquila Senior Executive Severance Costs: Joint Applicants will not request recovery in a future rate case of $16.7 million in severance expense related to departing Aquila senior executives. When combining this adjustment with the re-classification of $13.6

million in non-executive severance expense as Transition Costs, the total amount of Transaction Costs that Joint Applicants will seek to recover has been reduced from $95.2 million to $64.9 million, of which $47.2 million is Missouri jurisdictional.

The Commission held a prehearing conference on February 28, 2008. After the prehearing conference Commission Staff, Public Counsel and Industrial Intervenors proposed eliminating the March 24 and March 31 rounds of testimony, and extend the time allotted for the evidentiary hearings. On March 11, 2008 the Commission established a procedural schedule that, among other things, set the evidentiary hearing for April 21-25, April 28-May 2 and May 5-7, 2008, beginning at 8:30 a.m.

On March 12, 2008 Great Plains and KCPL sought for the Commission to quash deposition *subpoenas duces tecum*. The Commission denied the request on March 20, 2008.

On March 13, 2008 the Industrial Intervenors filed a motion seeking for a prehearing ruling that testimony prefiled February 25, 2008, regarding plans to merge the operations of Aquila and KCPL postmerger should not be admitted in evidence because the Joint Application included no request for authorization to merge the operations of Aquila and KCPL. The Commission denied that motion on April 8, 2008. The Industrial Intervenors raised the issue as a continuing objection during the evidentiary hearing.

On April 17, 2008 the Joint Applicants filed a motion to limit the scope of the evidentiary hearing by excluding certain witnesses from testifying and not taking evidence on certain matters designated as issues in the list of issues submitted by the Commission's staff on April 16, 2008. On April 24, 20008, on the record during the evidentiary hearing, the Commission granted the motion. The Commission ruled evidence regarding anonymous allegations, codes of corporate conduct or policies on gifts and gratuities were "wholly irrelevant" and not even an offer of proof could be made. The Commission ruled that evidence related to additional amortizations was irrelevant, but allowed an offer of proof. The Commission limited the witnesses on the issues of the relationship between KCPL's construction at Iatan and Great Plains' acquisition of Aquila.

The evidentiary hearing concluded on May 1, 2008. However, in response to a motion filed by Industrial Intervenors to reopen the record, on June 11, 2008, the Commission heard evidence on the impacts the May 23, 2008 collapse of a crane used in the construction of the environmental upgrades at Iatan I will have on the Iatan construction projects and, in turn, on GPE/KCPL's post-merger credit rating.

Creditworthiness

<u>Findings Of Fact</u>

The Joint Applicants' filed their Joint Application and Direct Testimony on April 4, 2007. They also filed Supplemental Direct Testimony on August 8, 2007 and Surrebuttal Testimony on November 13, 2007. The Staff filed the Rebuttal Testimony and Staff Report of Robert E. Schallenberg on October 12, 2007. The Staff recommended that the Commission deny the Joint Application because the proposed transaction was detrimental to the public interest. The Staff Report states: "GPE does not have the financial strength to acquire Aquila and absorb Aquila's financial difficulties without seriously weakening GPE's financial condition. GPE's acquisition of Aquila will weaken KCPL's financial condition at a time when KCPL is committed to significant capital expenditures."[1] The evidentiary hearings commenced on December 3, 2007 and were suspended by request of the Joint Applicants on December 6, 2007 so that they could determine whether they might amend their filed proposal based on concerns

[1] Ex. 101, Schallenberg, p. 1.

expressed by the Commissioners and parties and still maintain the creditworthiness of KCPL and a return to creditworthiness of Aquila.

The Joint Applicants filed additional testimony on February 25, 2008 which terminated their request for recovery of (1) interest costs associated with non-investment grade Aquila debt, (2) a specific synergy savings adder, i.e., retention of 50% of purported operational synergies, (3) an additional amortization for Aquila to meet credit metrics similar to the KCPL Regulatory Plan additional amortization to meet credit metrics, and (4) certain transaction costs - change in control costs and rabbi trust costs of Aquila senior management. GPE/KCPL had its amended proposal evaluated by Standard & Poor's and Moody's ratings evaluation services.[2] This February 25, 2008 additional testimony also addressed the credit rating or creditworthiness implications of the changes to the Joint Applicants' proposed transaction.[3]

During the suspension of the evidentiary hearings from December 6, 2007, the Staff, Public Counsel, and Industrial Intervenors became aware of the significance of an effort underway to redetermine a forecast of the cost and schedule of the Iatan 1 and Iatan 2 projects.[4] It was this information which caused these parties to further raise creditworthiness as an issue. They have asserted that GPE's proposed acquisition of Aquila is a detriment because of the negative impact to KCPL's creditworthiness while KCPL has undertaken the KCPL Regulatory Plan which comprises various infrastructure projects for KCPL through 2010. These parties have questioned GPE/KCPL's ability to successfully manage GPE's proposed acquisition of Aquila in addition to the KCPL Regulatory Plan when KCPL is purportedly encountering difficulty managing the KCPL Regulatory Plan as evidenced by the reforecast.

[2] Ex. 37NP, Bassham, pp. 1-5.
[3] Ex. 38HC, Cline.
[4] Ex. 138.

Section III.B.1.q. of the KCPL Regulatory Plan Stipulation And Agreement, Case No. EO-2005-0329, states at page 28 as follows:

> **q. Cost Control Process for Construction Expenditures**
>
> 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.

The KCPL Regulatory Plan Stipulation And Agreement does not limit a Signatory Party's right to inquire into or challenge the prudence of a construction cost. Therefore, KCPL is at risk of not being able to place in ratebase all of its costs respecting the Iatan 1 and Iatan 2 projects and the other infrastructure projects that are part of the KCPL Regulatory Plan, such as the environmental enhancements to LaCygne 1.

There is another section of the KCPL Regulatory Plan Stipulation And Agreement, III.B.1.f. "Financing Plan To Be Subsequently Filed By KCPL For Commission Authorization," which states in part: "The Signatory Parties understand that making the capital investments and initiating the customer programs described in Paragraph III.B.4 and Paragraph III.B.5 of this Agreement will require KCPL to issue debt securities." There was testimony from GPE/KCPL witness Michael W. Cline that KCPL financing cases, EF-2005-0498 and EF-2008-0214, are directly related to the KCPL Regulatory Plan Stipulation And Agreement.[5]

GPE/KCPL received a rating assessment letter from Standard & Poor's Rating Evaluation Service [6] and a rating assessment letter from Moody's Investors Service[7] based upon presentations made and information presented respecting the revised proposal for acquisition of Aquila that GPE/KCPL indicated it would pursue before the Commission. The record of the

[5] Vol. 20HC, Cline, Tr. 2588-91.
[6] Ex. 125HC.
[7] Ex. 124HC.

evidentiary hearings held in April 2008 indicate that various of the assumptions contained in the materials presented to S&P's and Moody's by GPE/KCPL in January 2008 and/or that are set out in S&P's and Moody's letters to GPE/KCPL have not occurred or are inaccurate.[8] Also, the Commission notes respecting Iatan that the new Iatan Project Director, who started in May 2008, is the fourth Iatan Project Director. His predecessor was in the position less than a year before he left.[9]

Although GPE/KCPL senior management professes confidence that GPE/KCPL will not experience a downgrading from the credit rating agencies as a consequence of the acquisition of Aquila, they stated that there was some risk that a downgrade would result by the rating agencies from approval of the transaction as presently proposed by the Joint Applicants.[10] Moreover despite the display of confidence by GPE/KCPL's senior management that a downgrading would not occur, the GPE/KCPL senior management is not willing to support that display of confidence with the commitment that GPE/KCPL shareholders would fund the costs of any downgrading and not KCPL's ratepayers.[11]

KCPL began time and opportunity tables in the April/May 2007 timeframe to record and track cost and schedule risks, i.e., increases / pressures, and cost and schedule opportunities, i.e., decreases / relief. Because of the increasing trend of the costs and the depletion of the contingency, the decision was made to start a reforecast of the cost and schedule for the Iatan 1 and Iatan 2 projects in December 2007.[12] There is some indication that a reforecast was to be

[8] Vol. 18HC, Bassham, Tr. 2335-38, 2359-2361; Ex. 38HC, Schedule MWC-18HC, p. 9, "Key Assumptions" and Schedule MWC-19HC, p. 9, "Key Assumption"; to Exhibit 38HC has the heading "Key Assumptions."
[9] Vol. 19, Easley, Tr. 2650; Vol. 19, Downey, Tr. 2487-88; Vol. 21, Rose, Tr. 2817.
[10] Vol. 19, Chesser, Tr. 2539-41; Vol. 19, Downey, Tr. 2497-2504; Vol. 17, Bassham, Tr. 2320-21, 2325.
[11] Vol. 19, Chesser, Tr. 2539-41; Vol. 19, Downey, Tr. 2496, 2598, 2599; Vol. 17, Bassham, Tr. 2319-20, 2321, 2323-25.
[12] Vol. 21, Rose, Tr. 2829-2833.

completed in the early months of 2008, but what GPE/KCPL calls the reforecast was not completed, adopted by the GPE Board of Directors and publicly released until May 2008.[13]

On May 7, 2008 GPE/KCPL made a Form 8-K filing with the U.S. Securities and Exchange Commission and publicly announced the results of the reforecast. Based on the top end of the new estimate range for the projected costs of the Iatan 1 environmental projects, the increase in projected costs is 33 percent compared to the top end of the previous range estimate for the Iatan 1 environmental projects. Based on the top end of the new estimate range for the projected costs of the Iatan 2 project, the increase in projected costs is 15 percent compared to the top end of the previous range estimate for the Iatan 2 project.[14] GPE/KCPL has indicated that a second reforecast for the Iatan 2 project is possible or likely.[15]

Conclusions of Law

Under the decision of the Missouri Supreme Court in *State ex rel. AG Processing Inc., v. Public Serv. Comm'n*, 120 S.W.3d 732, 736 (Mo. banc 2003), creditworthiness is a "necessary and essential issue" for the Commission to consider in deciding whether to approve the amended proposal of the Joint Applicants. The KCPL Regulatory Plan is a prior commitment of GPE/KCPL. The accommodations made to KCPL by the Signatory Parties and approved by the Commission in the KCPL Regulatory Plan case, EO-2005-0329, were agreed to or authorized so that KCPL could make the infrastructure improvements provided for in the Stipulation And Agreement in Case No. EO-2005-0329, not to permit GPE to acquire Aquila. The record in this proceeding indicates that the effect on the creditworthiness of GPE/KCPL of the proposed transaction as amended by the Joint Applicants, if approved by this Commission, would be detrimental to the public interest.

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[13] Late-Filed Ex. 305.
[14] *Id*.
[15] Vol. 19, Downey, Tr. 2486-87; Vol. 19, Chesser, Tr. 2524, 2535; Vol. 21, Foster, Tr. 2776-77, 2797-98.

Merger Synergy Savings

1. Are the estimates of savings from synergies reliable?

A. Could any of the synergy savings be achieved by KCPL or Aquila on a stand-alone basis absent the acquisition/consolidation/ integration?

B. Are any of the identified synergy savings dependent on KCPL and Aquila consolidating/integrating/merging their operations?

2. Is it likely that the actual synergy savings exceed the sum of the transaction, transition and incremental interest costs that the Joint Applicants propose to recover over the first five (5) years following the acquisition/merger/consolidation? If not, is the proposed merger not detrimental to the public interest?

Findings of Fact

1. The Joint Applicants estimate the Missouri-jurisdictional share of the synergy savings that will result from approval of the proposed transaction at $549 million over ten years, and $222 million in the first five years.[16] On a total-company basis, the figures are $755 million over ten years and $305 million over the first five years.[17]

2. The Joint Applicants state that they have "not taken credit for other synergies that will occur in the future but that cannot be clearly quantified today."[18] Presumably, these are the fuel and purchased power synergies referred to by expert witness William J. Kemp.[19]

3. The savings will arise from the integration and centralization of the operations of Aquila and KCPL and, in the absence of this operational integration and centralization, the Joint Applicants warn that there will be no savings.[20]

4. The bulk of the estimated synergy savings are projected to occur in the fifth

[16] Bassham, Additional Supp'l Direct, 3; Tr. 9:1223.
[17] Tr. 9:1222.
[18] Bassham, Additional Supp'l Direct, 6. Presumably, these are the fuel and purchased power synergies referred to by Kemp, Supp'l Direct, 15.
[19] Kemp, Supp'l Direct, 15.
[20] Giles, Additional Supp'l Direct, 1.

year.[21]

5. The Joint Applicants seek to recover Missouri jurisdictional transaction costs of $47.2 million and Missouri-jurisdictional transition costs of $42.8 million, for a total of $90 million, from the ratepayers by deferring them and amortizing them to cost of service over five years.[22] Under this scheme, ratepayers pay an additional $18 million in rates for each of the first five years following the transaction.

6. $222 million less $90 million is $132 million.[23] However, ratepayers will receive only about $100 million of the estimated savings because the rest will be directed to GPE via regulatory lag.[24]

7. The proposed transaction has been approved by the Federal Energy Regulatory Commission (FERC), and by other interested state commissions in Colorado, Iowa, Kansas, and Nebraska.[25] Only the approval of this Commission is now wanting.[26]

8. The Joint Applicants' own hired expert, William Kemp, testified that "An important measure of the public interest test is the long-term impact on rates to customers -- do the ratepayers receive a price benefit from the transaction?"[27] Kemp's answer to this question was, that in the sixth year following the transaction, "rates would be lower than they would otherwise be."[28]

9. The level of synergy savings predicted by the Joint Applicants exceeds the

[21] Tr. 11:1510.
[22] Bassham, Additional Supp'l Direct, 5; Tr. 9:1223.
[23] Bassham, Additional Supp'l Direct, 5, 6; Tr. 9:1223.
[24] Bassham, Additional Supp'l Direct, 3-4; Giles, Additional Supp'l Direct, 5-6.
[25] Tr. 9:1231.
[26] *Id.*
[27] Tr. 7:1025.
[28] Tr. 7:1029. Kemp admitted that "managing ratepayer expectations will be a challenge for both the Commission and for the applicants." Tr. 7:1030.

savings actually achieved in other electric-industry mergers and consolidations.[29]

10. In a joint proxy statement/prospectus dated August 27, 2007, the Joint Applicants identified "[t]he risk of cost savings and synergies not being achieved" as a "key risk" of the proposed transaction.[30] The prospectus goes on to say:[31]

> Great Plains Energy's board of directors noted that expected cost savings and synergies are estimates, that they may change and that achieving the expected cost savings and integration synergies is subject to a number of risks and uncertainties.
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> * * *
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> • *Integration*. Great Plains Energy's board of directors evaluated the challenges inherent in the combination of two business enterprises of the size and scope of Great Plains Energy and Aquila, including the possibility the anticipated cost savings and synergies and other benefits sought to be obtained from the merger might not be achieved in the time frame contemplated or at all.

Finally, the prospectus provides:[32]

> ***The anticipated benefits of combining the companies may not be realized.***
>
> We entered into the merger agreement with the expectation that the merger would result in various benefits, including, among other things, synergies, cost savings and operating efficiencies. Although we expect to achieve the anticipated benefits of the merger, achieving them cannot be assured.
>
> Approximately $275 million, or roughly 43%, of our total estimated cost savings and synergies over the first five years following the merger are expected to come from reductions in Aquila's corporate overhead and other costs currently allocated to the assets and businesses to be sold by Aquila to Black Hills. These costs are not being recovered through Aquila's Missouri utility rates, and are not expected to be recovered through Aquila's or KCP&L's utility rates following the merger. These reductions are expected to result from the elimination of corporate support positions and duplicative third-party services, as well as other overhead cost reductions. Although we expect to eliminate these costs following the completion of the merger, if we are not able to eliminate these costs as anticipated, the results from operations of the combined company will be negatively impacted.
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> * * *

[29] Kemp, Supp'l Direct, 18, 19.
[30] Late–filed Ex. 147:5; Bassham, Tr. 9:1368, ln. 1 to 1370, ln. 9.
[31] Late–filed Ex. 147:64 and 67; Bassham, Tr. 9:1370, ln. 21 – 1371, ln. 8; 1371, ll. 9-20.
[32] Late-filed Ex. 147:28, 30. Emphasis in the original.

There is no assurance regarding the amount of benefit-savings, or other regulatory treatment, in rate cases occurring after the closing of the Transactions.

11. The Joint Applicants assert that approval of the proposed transaction will result in two types of synergy savings: "created savings" and "enabled savings."[33]

12. "Created synergies," resulting from the consolidation of redundancies and economies of scale, are a direct result of the transaction; while "enabled synergies," the result of transfers of skills, adoption of best practices, and increased marketplace leverage, are not a direct result, but are facilitated or enabled by the transaction.[34]

13. James Dittmer, Public Counsel's expert witness, testified that the so-called "enabled savings" of at least $59 million could be achieved without the transaction.[35]

14. The Joint Applicants find savings in four areas:[36]

AREA	SAVINGS
Non-fuel O&M Departmental Budget Reductions	$87 million
Non-fuel O&M Integration Projects	$33 million
Supply Chain	$131 million
Projects that Decrease Purchased Power or Increase Revenue	$54 million
Total:	**$305 million**[37]

15. The Joint Applicants calculated the savings using Aquila's historical non-fuel O&M spending for 2006 as a base.[38] The base savings were then escalated by 3.1 percent per annum over five years and ten years in order to forecast the final figure for each of those

[33] Zabors, Supp'l Direct, 6.
[34] Zabors, Supp'l Direct, 6; Kemp, Supp'l Direct, 6.
[35] Dittmer, Rebuttal, 13, 28.
[36] Zabors, Supp'l Direct, 6.
[37] Total-company basis.
[38] Zabors, Supp'l Direct, 6-10.

periods.[39]

16. It is the fact that Aquila and KCPL operate in adjacent service territories that makes any synergies available at all.[40]

17. In the area of Non-fuel O&M Departmental Budget Reductions, savings of $87 million are predicted from reduction of payroll, economies of scale and reductions in non-labor spending.[41]

18. Some 355 jobs out of Aquila's total of 1,254 will be eliminated on Day 1, immediately after the closing of the transaction, with another 56 eliminated by the end of the first five years, for a total of 411.[42] Most these will be professional management employees.[43]

19. The remainder of Aquila's workforce will all become employees of KCPL. Aquila will have no employees of its own.[44]

20. About $50 million per annum in salaries will not be paid on a going-forward basis after the transaction is consummated.[45]

21. A consequence of mass terminations may be a failure of service quality.[46]

22. The Joint Applicants have not announced projections of the costs that will be incurred in providing work spaces for those Aquila employees that are transferred to KCPL employment.[47]

23. The estimated savings from economies of scale and elimination of redundancies may not be as great as predicted because Aquila's Kansas City-area electric utility operation is

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[39] Zabors, Supp'l Direct, 6-10; Tr. 7:1104.
[40] Kemp, Supp'l Direct, 8, 16, and Tr. 7:1016, 1034; Marshall, Surr., 7. Dittmer, Rebuttal, 47.
[41] Zabors, Supp'l Direct, 10.
[42] Zabors, Supp'l Direct, 14 and Sch. RTZ-9; Tr. 7:1121-1122; Tr. 9:1410.
[43] Tr. 7:1079.
[44] Tr. 7:1114.
[45] Tr. 9:1417.
[46] Staff Report, 11, 16.
[47] Dittmer, Rebuttal, 38.

already a component in a larger concern.[48]

24. In the area of Non-fuel O&M Integration Projects, savings of $22 million are projected from the elimination of Aquila's headquarters building and attached parking garage.[49]

25. The Commission finds that Aquila's headquarters and garage will probably be sold at a loss of $20 million to $30 million.[50] The Missouri share of this loss will be $11.3 million to $15.4 million.[51]

26. Additional savings of $11.5 million are projected to result from consolidating five existing service centers into two and the implementation of automated meter reading (AMR) for 310,000 to 330,000 Aquila customers.[52]

27. In the Supply Chain area, the Joint Applicants estimate savings of $131 million.[53]

28. The Supply Chain estimated synergy savings include $98 million in synergy savings from eliminating duplicate expenditures, adopting best prices currently available to either KCPL or Aquila, applying best demonstrated management practices from each company, leveraging greater scale and scope of spending, reducing unneeded reserve equipment and materials, a larger purchasing organization, reducing managerial overhead, and increased sharing of labor, equipment and material;[54]

29. The Supply Chain estimated synergy savings include $33 million in additional savings from $90.9 million in reduced capital spending on sourced materials through "improved strategic sourcing in supply, delivery and corporate as the capital process is made more

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[48] Dittmer, Rebuttal, 36.
[49] Zabors, Supp'l Direct, 10.
[50] Dittmer, Rebuttal, 38-9.
[51] Dittmer, Rebuttal, 40.
[52] Zabors, Supp'l Direct, 11; Tr. 7:1099.
[53] Buran, Supp'l Direct, 3.
[54] Buran, Supp'l Direct, 3.

efficient."[55]

30. It will cost $5.3 million to achieve the projected supply train savings.[56]

31. The estimated amount of Supply Chain savings increased 261.8% following the filing of Joint Applicants' initial direct testimony. Initially, the Joint Applicants represented there would be $50 million of supply chain synergy savings over the first five years.[57]

32. Both KCPL and Aquila have ongoing programs to improve employee performance, refine supply chain access, and improve vendor pricing.[58]

33. KCPL's Regulatory Plan obligates KCPL to prudently manage costs, continuously improve productivity, and maintain service quality during the Regulatory Plan.[59]

34. Lora Cheatum, KCPL executive responsible for procurement, testified that KCPL has not considered consortium buying as a means to create supply chain savings for KCPL on a stand-alone basis.[60]

35. Despite the contention that one source of savings will be leveraging better pricing, no single vendor has been identified as the source of such savings.[61] If the contract-by-contract method of merger-supply-chain-synergy-savings analysis alluded to by the Joint Applicants had truly been employed, the Commission finds that such a fact would have necessarily surfaced.

36. GPE/KCPL, when buying for Iatan, is purchasing for an endeavor with a scope greater than just GPE/KCPL's share, as Iatan is jointly-owned by several utilities including Aquila. The Commission finds that there is no evidence in this record that items purchased for Iatan cost less because GPE/KCPL is purchasing on behalf of an entity larger than itself.

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[55] Zabors, Supp'l Direct, 13.
[56] Buran, Supp'l Direct, 13, 18, and Sch. WPB-4.
[57] Ex. 30, p. 11, ll. 16 – 17.
[58] Tr. 11:1519, ln. 14, to 1520, ln. 9.
[59] KCPL Regulatory Plan Stipulation & Agreement, Case No. EO-2005-0329, at 19.
[60] Tr. 11:1505 (Cheatum).
[61] Tr. 11:1503-1504.

37. The Commission finds that the calculation of the potential supply chain savings do not take into account various risks to the ability to achieve the projected savings, such as volatility in the utility industry, although the Joint Applicants acknowledge that factors such as supply constraints could limit the ability of a utility of any size to leverage favorable pricing from a vendor.[62]

38. The Commission finds that little or no consideration was given to potential limitations to the ability of a combined entity to achieve favorable pricing, even to the extent of merely estimating the percentage of the projected savings that could be susceptible to market risks.[63]

39. The projected supply chain synergy savings were escalated assuming inflation of 3.1% per year in costs,

40. The Commission finds that this escalation exaggerated the potential savings by increasing the projected costs.[64]

41. The Commission finds that the costs-to-achieve were not similarly adjusted.[65]

42. The cost-to-achieve figure will be incurred regardless of whether any savings are ever realized.[66]

43. The costs-to-achieve were not adjusted for known risks in the utility industry and other factors that are likely to increase the level of the costs to achieve.[67]

44. The Joint Applicants point to an array of projects under the heading "Projects that Decrease Purchased Power or Increase Revenue," including:[68]

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[62] Tr. 11:1506, 1507-1508.
[63] Tr. 11:1509.
[64] *Id.*
[65] Tr. 11:1512.
[66] Tr. 11:1512.
[67] *Id.*
[68] Zabors, Supp'l Direct, 12; Steinke, Supp'l Direct, 3.

- Optimization of Sibley 3, including induced draft booster fans, moving load following operations to other units, improving the effectiveness of soot-blowing with instrumentation, upgrading coal blending facilities, and applying KCPL's cyclone boiler combustion expertise, saving $17 million in purchased power over 5 years.

- Combine both companies' combustion turbine (CT) operations, saving $3.1 million over 5 years.

- Improving plant heat rate at the Aquila plants, saving $0.6 million over 5 years.

- Implementing KCPL's Boiler Tube Failure Reduction and Cycle Chemistry Improvement ("BTFR/CCI") program on the Aquila coal-fired fleet, worth $5.6 million over 5 years.

- Reduced outages needed for boiler cleaning at Sibley 1 and 2, saving $1.6 million over 5 years.

- Applying KCPL's expertise at energy efficiency to Aquila's customers, saving $13 million over 5 years.

- Applying Aquila's expertise to KCPL's billing processes, saving $12.8 million over 5 years.

45. KCPL witness Marshall testified that "we intend to track these synergies for our senior management team and workforce as well as for our board to show that we do, in fact, perform them." Tr. 7:1150-1151.

46. The Joint Applicants offer to track the synergy savings actually achieved and to continue to defer costs scheduled for amortization to cost of service if the synergies do not cover the amortization.[69]

47. The Joint Applicants' proposed tracking mechanism is found in the testimony of Lori Wright: "I suggest establishing base period costs and then each year subsequent to the Merger comparing that year's actual costs to the base year costs, as adjusted for inflation. The

[69] Bassham, Add'l Supp'l Direct, 6-7. In fact, KCPL witness Marshall testified that "we intend to track these synergies for our senior management team and workforce as well as for our board to show that we do, in fact, perform them." Tr. 7:1150-1151.

net decrease in expense would be considered synergy savings."[70] Wright proposes 2006 as the base year, because it served as the test year in an Aquila rate case and a KCPL rate case and so is well-known in detail to all the stakeholders.[71] Wright would adjust the calculation for known and measurable changes such as wage increases and inflation.[72]

48. Wright herself admits: "Tracking synergy savings with any degree of accuracy is problematic at best as business operations are not conducted in a static environment, but rather under constant change, including customer growth, technological improvements, etc. Tracking will become more difficult each successive year after the Merger."[73]

49. Staff's consistent view is that merger savings cannot be accurately tracked and notes that this Commission has never accepted a merger savings tracking device.[74]

50. This Commission has previously recognized that merger savings cannot be reliably tracked.[75]

51. Industrial Intervenors' expert witness Maurice Brubaker disagreed with the adequacy of Wright's proposed tracking mechanism, stating: "This approach assumes that, but for the merger, base year costs will escalate at the rate of inflation. This completely ignores any reductions in cost that may be achieved as a result of normal business operations, improvements in efficiency and reductions in head count as a result of productivity improvements through technology and other means, changes in practices and policies with respect to employee benefits, and any other actions that are normally taken as a matter of course in operating an electric utility."[76]

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[70] Wright, Direct, 5-6.
[71] Wright, Direct, 6.
[72] Wright, Direct, 6.
[73] Wright Direct, 5.
[74] Staff Report, 46, 48.
[75] *See supra,* § I in general and subsection I.C., discussing Case No. EM-98-213, in particular.
[76] Brubaker, Rebuttal, 7.

52. The Joint Applicants' own expert witness, William J. Kemp of Black & Veatch, testified that the estimated synergy savings, at 10% of Aquila and KCPL's combined non-fuel O&M costs for 2006, are "significantly" higher than the 1% average of actually realized synergy savings in 15 electric utility transactions.[77]

53. Maurice Brubaker, an expert witness for the Industrial Intervenors, agrees that the estimated synergies are "significantly above the average" and notes that "[g]iven the aggressive nature of Applicants' synergy claims, it would not be wise to decide this case based on the assumption that these claimed savings are certain to be realized."[78]

54. Staff's expert witness, Robert Schallenberg, called the estimated savings "overstated."[79]

55. Public Counsel's expert witness James Dittmer characterized the estimates as "overstated" and "uncertain."[80]

56. Staff predicted that the transaction will weaken the financial positions of both Great Plains and KCPL.[81]

57. Great Plains Energy admitted in a response to a Data Request that only half of electric industry mergers have been successful.[82]

58. William Kemp, the Joint Applicants' expert witness, agreed that the ratepayers will pay more if the projected level of synergy savings are not realized.[83]

59. Public Counsel's witness, James Dittmer, testified that the transaction might very

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[77] Tr. 7:1034, *and see* Kemp, Supp'l Direct, 22. Brubaker characterizes Kemp's figures as showing that the Joint Applicants' estimates are "quite aggressive." Brubaker, Rebuttal, 10.
[78] Brubaker Rebuttal, 4, 11.
[79] Staff Report, 11.
[80] Dittmer, Rebuttal, 5.
[81] Staff Report, 1.
[82] Staff Report, 21-22.
[83] Tr. 7:1036.

well lead to a credit-rating downgrade for KCPL if the projected synergies are not all realized.[84]

60. Dittmer testified, "We are paying above traditional cost of service rates just to keep the credit rating acceptable, and now we are exposing that credit rating to a downgrade through this purchase through the other costs -- if the company is not allowed to recover all the costs that they were asking for in this case or in the next rate case where they do ask for regulatory amortization on the Aquila side."

61. Based on the credible evidence adduced, the Commission finds that the amount of synergy savings estimated by the Joint Applicants are significantly exaggerated and that savings of no more than 1% or 2% -- say $44 million over five years -- will likely be realized. Thus, there will be no net benefit after transaction and transition costs.

Conclusions of Law

The Commission may approve the proposed transaction only if the Joint Applicants show that it is more-likely-than-not that the transaction will not be detrimental to the public interest. Rule 4 CSR 240-3.115(1)(D); *State ex rel. AG Processing, Inc. v. Public Service Commission,* 120 S.W.3d 732, 736 (Mo. banc 2003). "What is required is a cost-benefit analysis in which all of the benefits and detriments in evidence are considered. * * * Approval should be based on a finding of no net detriment." *In the Matter of Union Electric Co.,* 13 Mo.P.S.C.3d 16, 40 (October 6, 2004).

Based on the evidence adduced by the Staff, the Public Counsel and the Industrial Intervenors, the Commission concludes that the proposed transaction would constitute a detriment to the public interest, and thus cannot be approved, because the sum of the transaction and transition costs are likely to exceed the sum of any synergy savings actually realized over the first five years following consummation of the transaction.

[84] Tr. 13:1680, 1681, 1684, and 1755.

Affiliate Transactions Rule Waiver Request

Findings of Fact

The Joint Applicants request this Commission to issue an order finding the affiliate transactions rule 4 CSR 240-20.015 would not apply to transactions between KCPL and Aquila post-merger or, alternatively, or to grant a variance to exempt such transactions from being required to comply with the rule.[85] Aquila is now and is planned to be regulated by this Commission as to its retail electric operations in Missouri.[86] Similarly, KCPL is now and is planned to be regulated by this Commission as to its retail electric operations in Missouri.

The Joint Applicants plan that post-merger Aquila will have no employees; Aquila's current employees will be terminated, although some will be hired by Great Plains or KCPL.[87] Instead, Great Plains, KCPL and Great Plains Energy, Inc. employees will provide the services Aquila requires.[88] In particular, KCPL employees will perform all generation, transmission, distribution and utility support functions for both KCPL and Aquila,[89] and Great Plains Energy Services, Inc., a wholly-owned subsidiary of Great Plains, and KCPL will provide human resources, legal and accounting services to Aquila.[90]

The Joint Applicants contend 4 CSR 240-20.015 should not apply to transactions between KCPL and Aquila because KCPL and Aquila both are now and post merger will be utilities this Commission regulates.[91] Alternatively, they request a variance that would relieve KCPL and Aquila from compliance with the rule for transactions between them.[92]

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[85] Joint Application, Ex. 32, pp. 19 and 21.
[86] Great Plains witness Bassham Direct, Ex. 1, pp. 2-3.
[87] Great Plains witness Bassham Direct, Ex. 1, p. 7; Great Plains witness Downey Direct, Ex. 13, p. 4; Great Plains witness Wright Direct, Ex. 29, p. 7.
[88] Great Plains witness Bassham Direct, Ex. 1, p. 7; Great Plains witness Wright Direct, Ex. 29, pp. 7-8.
[89] Staff witness Schallenberg Rebuttal, Ex . 100, Staff Report p . 64.
[90] Great Plains witness Bassham Direct, Ex. 1, p. 7.
[91] Joint Application, Ex. 32, pp. 19 and 21.
[92] Joint Application, Ex. 32, pp. 19 and 21.

The Commission has clearly stated its ultimate intent for 4 CSR 240-20.015 in the statement of the purpose of the rule published in the Code of State Regulations. In pertinent part, that purpose statement is: "This rule is intended to prevent regulated utilities from subsidizing their nonregulated operations. . . . The rule and its effective enforcement will provide the public the assurance that their rates are not adversely impacted by the utilities' nonregulated activities." The definition of affiliated entity in the rule is broad and expressly includes electrical corporations such as Aquila and KCPL. 4 CSR 240-20.015(1)(A). Likewise, the definition of affiliated transactions expressly includes transactions involving the unregulated business operations of a regulated electrical corporation. 4 CSR 240-20.015(1)(B).

KCPL providing services to Aquila is not part of the regulated business operations of KCPL, unlike operating a power plant that is jointly owned with others. If for no other reason than KCPL and Aquila can time rate cases to the nonregulated business costs of KCPL services onto Aquila ratepayers, KCPL and Aquila should not be allowed relief from the requirements of 4 CSR 240-20.015.

Conclusions of Law

Rules are construed by the same principles used to construe statutes and the purpose of construing them is to give effect to the intent of the drafter. (*State ex rel. Evans v. Brown Builders Elec. Co., Inc.*, --- S.W.3d ----, 2008 WL 2102419 (Mo. banc, 2008).

If 4 CSR 240-20.015 did not encompass transactions between regulated entities, the inclusion of the reference to unregulated business operations of a regulated electrical corporation in 4 CSR 240-20.015(1)(B) would be meaningless.

The affiliate transaction rules are premised on asymmetric pricing to prevent a public utility from subsidizing its nonregulated operations. Therefore, goods and services provided by a public utility to any affiliate (regulated or not) are to be priced at the higher of market value or the cost to the public utility in providing the goods and services. Conversely, goods and services provided by any affiliate (regulated or not) to a public utility are to be priced at the lower of market value or the cost to the public utility in providing the goods and services to itself In this way, the public utility should be indifferent as to whether it sells or receives goods and services from an affiliate, regulated or not, or a third party.

It is not in the public interest for the Commission to grant the requested variance. It is denied.

Transaction Costs

Findings of Fact

The Joint Applicants request that the majority of the transaction costs for Great Plains' acquisition of Aquila should be given regulatory accounting treatment on the books of KCPL and Aquila by establishing them as regulatory assets with five year amortization periods.[93] Aquila and KCPL could then seek inclusion of the annualized amount of this respective regulatory asset their respective costs of service resulting in an increase in rates charged its customers.[94]

The Joint Applicants urge the Commission to give them the opportunity to recover from ratepayers their transition and transaction costs because they must incur transaction and transition costs to obtain any merger-related synergy savings.[95]

"Transaction costs" are costs necessarily incurred to consummate a transaction—costs such as attorneys' fees for agreement review and execution, and bankers' fees for deal valuation

[93] Joint Application, Ex. 32, para. F; Great Plains witness Bassham Direct, Ex. 1, p. 16.
[94] Great Plains witness Wright, Vol. 15, Tr. 2007-2009.
[95] Great Plains witness Bassham Direct, Ex. 1, p. 16.

and equity placement.[96] In contrast, "transition costs" are costs incurred to integrate the operations of Aquila and KCPL.[97]

Originally, the Joint Applicants requested transaction costs totaling $95 million be placed in regulatory assets.[98] The Joint Applicants' witnesses acknowledged transaction costs can readily be distinguished from transition costs.[99] However, when the Joint Applicants modified their request in February of 2008, they recategorized $13.6 million in severance costs from transaction costs to transition costs[100] and they removed from their request what they described as the Great Plains' share of Aquila executive change in control cost ($8.9 million), the tax gross-up of that Aquila executive change in control cost ($0.5 million) and the Rabbi trust that represents Aquila's supplemental executive retirement plan ($7.3 million) totaling $16.7 million.[101] As a result the total amount of the transaction costs they request be amortized, before jurisdictional allocation is now $65 million.[102]

The Joint Applicants assert transition and transaction costs should be allocated by state based on the retail, wholesale and merchant operations of KCPL and Aquila in proportion to projected savings, as adjusted based on energy sales.[103] Doing so results in an allocation of transaction costs of $28.7 million that would established as a regulated asset on Aquila's books

[96] Staff witness Schallenberg Rebuttal, Ex. 100, Staff Report p. 51; Great Plains witness Bassham, Vol. 15, Tr. 1929; Great Plains witness Wright, Vol. 15, Tr. 1989-90; Great Plains witness Wright Direct, Ex. 29, pp. 3-4; Great Plains witness Zabors Direct, Ex. 30, pp. 12-14; Great Plains witness Zabors Supp. Direct, Ex. 31, pp. 14-15; Great Plains witness Bassham Direct, Ex. 1, p. 16.
[97] Great Plains witness Bassham, Vol. 15, Tr. 1929; Great Plains witness Wright Direct, Ex. 29, p. 4; Great Plains witness Zabors Direct, Ex. 30, pp. 12-14; Great Plains witness Zabors Supp. Direct, Ex. 31, pp. 14-15.
[98] Great Plains witness Bassham Direct, Ex. 1, p. 16; Great Plains witness Zabors Supp. Direct, Ex. 31, p. 14 and Sch. RTZ-10.
[99] Great Plains witness Wright, Vol. 15, Tr. 1990; Great Plains witness Bassham, Vol. 15, Tr. 1929-1930.
[100] Great Plains witness Bassham Add'l. Supp. Direct, Ex. 37, pp. 4-5; Great Plains witness Bassham, Vol. 15, Tr. 1930-1932; Great Plains witness Wright, Vol. 15, Tr. 1990; Great Plains witness Zabors, Vol. 21, Tr. 2922.
[101] Great Plains witness Bassham Add'l. Supp. Direct, Ex. 37, pp. 4-5; Great Plains witness Zabors Supp. Direct, Ex. 31, Sch. RTZ-10; Great Plains witness Zabors, Vol. 21, Tr. 2921-2922.
[102] Great Plains witness Bassham Add'l. Supp. Direct, Ex. 37, p. 5; Great Plains witness Zabors Supp. Direct, Sch. RTZ-10; Great Plains witness Zabors, Vol. 21, Tr. 2921-2922.
[103] Great Plains witness Rush, Ex. 23, p.6 and Sch. TMR-1; Great Plains witness Giles Add'l. Supp. Direct, Ex. 39, pp. 4-6 and Sch. CBG-1.

and amortized over five years. This would mean that the annual amount of $5.74 million would be available for inclusion in Aquila's cost of service for ratemaking purposes.[104] The corresponding amount of transaction costs for KCPL is stated to be $18.5 million which means that $3.7 million could be included in KCPL's cost of service for ratemaking purposes.[105] Each would result in higher rates for the ratepayers of Aquila and KCPL, respectively.

KCPL is not a party to the merger transaction[106] and there is no agreement for KCPL to pay Great Plains' transition or transaction costs.[107] Both transaction and transition costs of Great Plains' proposed acquisition of Aquila are being recorded on Great Plains' books.[108] As of April 24, 2008 Bridge Strategy Group had billed Great Plains a total of $4.3 million that is categorized as transaction costs and a total of about $5.2 million categorized as transition costs;[109] Great Plains paid the billings.[110] Based on the evidence before it, the Commission finds that it is appropriate that Great Plains bear these costs because they are costs the board of directors Great Plains chose to incur.[111]

The Commission also finds that, because of inadequate cost control procedures at Great Plains and KCPL in reviewing and paying invoices, the Joint Applicants' quantification of the transaction costs is dubious.[112] No party has cited to a case where this Commission has authorized a utility to record parent company expenses on the books and records of the utility, absent an agreement that obligates the utility to pay the expenses.

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[104] Great Plains witness Giles Add'l. Supp. Direct, Ex. 39, Sch. CBG-1.
[105] Great Plains witness Giles Add'l. Supp. Direct, Ex. 39, pp. 4-6 and Sch. CBG-1.
[106] Joint Application, Ex. 32, Exhibit 4 to application; Great Plains witness Bassham Direct, Ex. 1, p. 6.
[107] Great Plains witness Wright, Vol. 15, Tr. 1995.
[108] Great Plains witness Wright, Vol. 15, Tr. 1990-1995.
[109] Great Plains witness Wright, Vol. 15, Tr. 2001; Exs. 126, 128 and 129; Great Plains witness Zabors, Vol 21, Tr. 2896-2897.
[110] Great Plains witness Zabors, Vol. 21, Tr. 2910 and 2901.
[111] Staff witness Schallenberg Rebuttal, Ex . 100, Staff Report p . 51.
[112] Ex. 127; Ex. 128; Ex. 129; Ex. 130; Great Plains witness Zabors, Vol. 21, Tr. 2899-2901, 2907-2910, 2912-2913, 2917-2919; Great Plains witness Wright, Vol. 15, Tr. 1996-1999, 2004-2007; Staff witness Rose, Vol. 21, Tr. 2806, 2809-2812.

Because KCPL is not a party to the proposed merger transaction and is not responsible for any of the transaction costs, the Commission finds that there should not be an opportunity for KCPL to recover any of the transaction costs from the Missouri customers of KCPL.

In *State ex rel. AG Processing, Inc. v. Public Service Commission*, 120 S.W.3d 732 (banc 2003), the Missouri Supreme Court held the Commission had to consider UtiliCorp United, Inc.'s request for the opportunity to recover a $92 million acquisition premium made as part of its request for authority to acquire St. Joseph Light & Power Company. On remand, although postmerger Aquila, Inc. abandoned its request to recover this acquisition premium, the Commission went on to issue a Second Report and Order on February 26, 2004 rejecting any opportunity to recover the acquisition premium through rates stating:

> As a general rule, only the original cost of utility plant to the first owner devoting the property to public service, adjusted for depreciation, should be included in the utility's rate base. That principle is known as the net original cost rule.
>
> The net original cost rule was developed in order to protect ratepayers from having to pay higher rates simply because ownership of utility plant has changed, without any actual change in the usefulness of the plant. If a utility were allowed to revalue its assets each time they changed hands, it could artificially inflate its rate base by selling and repurchasing assets at a higher cost, while recovering those costs from its ratepayers. Thus, ratepayers would be required to pay for the same utility plant over and over again. The sale of assets to artificially inflate rate base was an abuse that was prevalent in the 1920s and 1930s and such abuses could still occur.[113]

The Commission finds that establishing a mechanism to allow recovery of the transaction costs of a merger would have the same effect of artificially inflating rate base in the same way as allowing recovery of an acquisition premium. Additionally, it would create an added incentive to sell a utility since, if the buyer is able to recover all or part of the transaction costs through customer rates, a buyer will be willing to pay a higher purchase price than it would otherwise.

[113] *Re UtiliCorp United, Inc.*, 12 Mo.P.S.C.3d 388, 389-90 (2004).

Importantly, this would result in an increase in rates to ratepayers that would exceed what would otherwise be the case.

The Joint Applicants quote from *Re Union Electric Company*, 6 Mo.P.S.C. 3d 28 (Feb. 21, 1997), as support for the Staff having "concurred with the request of merging utilities to amortize transaction and transition costs over time." However, that case was resolved by a stipulation and agreement and is no precedent for positions of any party to that case in any other case. *Re Union Electric Company*. Both KCPL and Aquila (then known as UtiliCorp United, Inc.) were signatories to that stipulation and agreement. That stipulation and agreement, as approved by the Commission, included the following provision:

> 13. No Acquiescence
>
> None of the signatories to this Stipulation And Agreement shall be deemed to have approved or acquiesced in any question of Commission authority, accounting authority order principle, cost of capital methodology, capital structure, decommissioning methodology, ratemaking principle, valuation methodology, ***cost of service methodology or determination***, depreciation principle or method, rate design methodology, cost allocation, ***cost recovery***, or prudence, that may underlie this Stipulation and Agreement, or ***for which provision is made in this Stipulation And Agreement***.

(Emphasis added.) *Id*. at 57. Because it deters settlement, the Commission does not encourage parties to disregard commitments they make in settling matters before the Commission, or elsewhere.

Regardless of *Re Union Electric Company* having no precedential value, as when Aquila cited to *Re Union Electric Company* in Case No. EM-2000-292 (*Re UtiliCorp United, Inc.*, 12 Mo.P.S.C.3d 388 (2004)) in support of it recovering the acquisition premium that Aquila had paid for St. Joseph Light and Power Company, this Commission summarily dismisses the invitation to rely on *Re Union Electric Company*. Specifically, in *Re UtiliCorp United, Inc.* this Commission stated:

> UtiliCorp also cites two Commission cases in which it argues that the Commission has allowed for the indirect recovery of acquisition premium. UtiliCorp indicates that in the case in which the Commission approved Union Electric Company's merger with Central Illinois Public Service Company, it allowed for the recovery of the acquisition premium through operation of an earnings-sharing grid. UtiliCorp also points out that in the case in which the Commission approved Kansas City Power & Light Company's plan to merge with Western Resources, Inc., it approved a rate freeze that would allow enough time for the company to recover the acquisition premium through the operation of regulatory lag. While what UtiliCorp says about those two cases is correct, it is important to note that both cases were resolved through unanimous stipulations and agreement that were approved by the Commission. In neither case did the Commission purport to establish any policy that would apply to UtiliCorp's request to recover its acquisition premium in this case.

(footnotes omitted.) *Re UtiliCorp United, Inc.,* 12 Mo.P.S.C.3d at 391. While the Commission has accepted, as part of an overall settlement of a case, the opportunity to recover merger transaction costs from ratepayers in isolated instances, the Joint Applicants have provided no support that this Commission has ever allowed a utility the opportunity to recover merger transaction costs from its customers when that issue is before it as a separate and distinct matter for decision. The Joint Applicants in this case have simply provided no compelling ground(s) to cause this Commission to change its approach and allow the Joint Applicants the benefits of the opportunity to recover from KCPL and Aquila customers the transaction costs of this merger between Aquila and a subsidiary of Great Plains. This Commission denies the Joint Applicants request that the Commission authorize KCPL and Aquila to establish regulatory assets and amortize into cost of service the transaction costs of the merger.

<u>Conclusions of Law</u>

Based on the foregoing findings of fact, the Commission concludes that authorizing the Joint Applicants to establish regulatory assets with five year amortization periods for the opportunity to include them in cost of service for recovery from ratepayers of Aquila and KCPL would be detrimental to the public interest. Accordingly, Joint Applicant's request to do so should be denied.

Service Quality

1. Can service quality problems resulting from a merger/consolidation/acquisition of a works or system necessary or useful in the performance of duties to the public preclude the merger/consolidation/acquisition from being not detrimental to the public interest?

2. Has GPE/KCPL taken adequate measures to ensure that its proposed postconsolidation/ post-merger/post-acquisition operations will not be detrimental to the public interest by precluding service quality issues arising from the consolidation/merger/acquisition?

Findings Of Fact

The August 27, 2007 GPE-Aquila joint proxy statement/prospectus states at page 67, among other things:

> - *Integration*. Great Plains Energy's board of directors evaluated the challenges inherent in the combination of two business enterprises of the size and scope of Great Plains Energy and Aquila, including the possibility the anticipated cost savings and synergies and other benefits sought to be obtained from the merger might not be achieved in the time frame contemplated or at all.

(Vol. 9, Tr. 1371, lns. 9-20; Late-Filed Ex. 147, p. 67).

Acquisitions and integrations of operations are known to place service quality at risk, and the breadth of these likely disruptions are generally not anticipated or planned for. (*See* Staff Report, p. 71).

There is the notable case of Southern Union Company's acquisition of Western Resources Inc.'s Missouri local distribution gas properties now called Missouri Gas Energy in 1993, *Re Western Resources, Inc., d/b/a Gas Service and Southern Union Co., d/b/a Southern Union Co.*, Case No. GM-94-40, Report And Order, 2 Mo.P.S.C.3d 598 (1993). Numerous very serious customer service problems occurred for several years after that acquisition. Workforce reductions was one of the factors for the resulting problems. (*Id*. at 71-72). The different or previously separate entities have different processes, practices, systems, procedures, cultures, organizational structures and workforces. (*Id*. at 68). New or different ways of operating, while determined to be desirable, disrupt or disturb stability, security of systems, operations and staffs. (*Id*. at 69).

Here, the Joint Applicants are proposing to continue serving KCPL's and Aquila's existing electric customers, and to provide transitional services to Black Hills, all with a significant reduction in employees. (*See* Herdegen, v. 17, p. 2290, L. 3 - 6). The transaction contemplated is significantly more complicated than that involving the Southern Union transaction.

The timing of this transaction results in an elaborate organizational restructuring coinciding with the roll-out of a major change in both companies' vegetation management programs. (*See* Herdegen, v. 17, p. 2289, L. 2 - 7). Further complicating matters is the fact that a portion of the promised synergies are dependent on the implementation of automatic meter reading in the Aquila service territory. (*See* Herdegen, v. 17, p. 2289, L. 8 - 22).

There is inadequate evidence of adequate planning and controls to ensure that the consolidation will occur with minimal disruption to service quality. There is testimony that the consolidation of service centers, viewed by the Joint Applicants as a source of significant net synergies, (*See* Herdegen, v. 17, p. 2289, L. 15 - 22), will occur Day One, including the elimination of a significant number of employees. Given the unreliability, described elsewhere herein, of the Joint Applicants' projected costs and synergies, the likely immediate human resource and loss of institutional knowledge issues should be matters of concern.

Conclusions Of Law

Any degradation of the stand-alone companies' current metrics is a degradation of customer service which must be assessed in the decision of whether to allow the proposed transaction to occur. This approach preserves in advance Service Quality from being debased by cost-saving measures when the costs of the transaction exceed projected levels, or when promised benefits do not materialize. It would be detrimental to the public interest to allow the Joint Applicants to place service quality at risk in any circumstance, but certainly in a futile effort to maintain financial integrity, as there proposed transaction does.

Name Change

Findings of Fact

Joint Applicants seek authority to change the name of Aquila to some undisclosed new name. When requesting Commission authorization for a name change the following are required:

> (5) A name change may be accomplished by filing the items below with a cover letter requesting a change of name. Notwithstanding any other provision of these rules, the items required herein may be filed by a nonattorney. Applications for approval of a change of name shall include:
> (A) A statement, clearly setting out both the old name and the new name;
> (B) Evidence of registration of the name change with the Missouri secretary of state; and
> (C) Either an adoption notice and revised tariff title sheet with an effective date which is not fewer than thirty (30) days after the filing date of the application, or revised tariff sheets with an effective date which is not fewer than thirty (30) days after the filing date of the application.

4 CSR 240-2.060(5). These requirements are primarily directed to avoiding customer confusion and assuring the new name comports with the public interest. Without the proposed name before the Commission cannot determine the propriety of the new name; therefore, the Commission denies the request for authority to change the name of Aquila.

Applicable Legal Standards

Section 393.190.1 RSMo 2000 contains no express standard for the Commission's determination of whether to approve a request to "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 . . ." The Missouri Supreme Court held in *State ex rel. City of St. Louis v. Public Serv. Comm'n*, 73 S.W.2d 393 (Mo. banc 1934) that "not detrimental to the public" is the appropriate standard:

> The state of Maryland has an identical statute with ours, and the Supreme Court of that state in the case of Electric Public Utilities Co. v. Public Service Commission, 154 Md. 445, 140 A. 840, loc. cit. 844, said: "To prevent injury to the public good in the clashing of private interest with the public good in the operation of public utilities, is one of the most important functions of Public Service Commissions. It is not their province to insist that the public shall be benefited, as a condition to change of ownership, but their duty is to see that no such change shall be made as would work to the public detriment. 'In the public interest,' in such cases, can reasonably mean no more than 'not detrimental to the public'".

The Commission has expressly stated in many cases that it is using the standard of "not detrimental to the public interest" in determining whether to approve transactions under Section 393.190.1. In a recent Aquila encumbrancing case *In the Matter of the Application of Aquila, Inc. for Authority to Assign, Transfer, Mortgage or Encumber its Utility Franchise, Works or System in Order to Secure Revised Bank Financing Arrangements*, Case No. EF-2003-0465, Report And Order, 12 Mo.P.S.C.3d 375, 378 (2004), the Commission explained what it meant by the "not detrimental to the public interest" standard as follows:

> The Commission concludes a detriment to the public interest includes a risk of harm to ratepayers. In reviewing a recent merger case involving the same parties, the Supreme Court of Missouri ruled that . . . "(w)hile (the Commission) may be unable to speculate about future merger-related rate increases, it can determine whether the acquisition premium was reasonable, and it should have considered

> (the premium) . . . when evaluating whether the proposed merger was detrimental to the public."[12] In other words, the Commission could not have known whether the acquisition premium would result in rate increases. But it should have looked at the premium's reasonableness. Likewise, the Commission cannot know whether the encumbrances will result in rate increases. But the Commission should look at the reasonableness of the risk of the increases. This analysis conforms to the concept that . . . "(n)o one can lawfully do that which has a **tendency** to be injurious to the public welfare."[13]
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> [12] *State ex rel. AG Processing Inc., v. Public Service Commission*, 120 S.W.3d 732, 736 (Mo. banc 2003).
>
> [13] *State ex rel. City of St. Louis v. Public Service Commission*, 73 S.W.2d 393, 399-400 (Mo. banc 1934)(emphasis supplied).

Id.; Emphasis in original; 4 CSR 240-3.115(1)(D). The Commission's charge is clearly not limited to determining whether the entities acquiring facilities being transferred have the financial and technical capacity to carry through on a project. The Commission may approve the proposed transaction only if the Joint Applicants show that it is more-likely-than-not that the transaction will not be detrimental to the public interest.

In a recent Union Electric Company case, generally referred to as the Metro-East Transfer Case, the Commission said:

> . . . What is required is a cost-benefit analysis in which all of the benefits and detriments in evidence are considered. . . . Approval should be based on a finding of no net detriment.
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> In considering whether or not the proposed transaction is likely to be detrimental to the public interest, the Commission notes that its duty is to ensure that UE provides safe and adequate service to its customers at just and reasonable rates. A detriment, then, is any direct or indirect effect of the transaction that tends to make the power supply less safe or less adequate, or which tends to make rates less just or less reasonable. The presence of detriments, thus defined, is not conclusive to the Commission's ultimate decision because detriments can be offset by attendant benefits. The mere fact that a proposed transaction is not the least cost alternative or will cause rates to increase is not detrimental to the public interest where the transaction will confer a benefit of equal or greater value or remedy a deficiency that threatens the safety or adequacy of the service.

In the Matter of the Application of Union Electric Co., doing business as AmerenUE, for an Order Authorizing the Sale, Transfer and Assignment of Certain Assets, Real Estate, Leased

Property, Easements and Contractual Agreements to Central Illinois Public Service Company, doing business as AmerenCIPS, and in Connection Therewith, Certain Other Related Transactions, 13 Mo.P.S.C.3d 16, 40 (2004). Thus, depending on the circumstances, the Commission may appropriately look more broadly in making its determination whether to approve a transfer. The Missouri Supreme Court recognized this in *Love 1979 Partners v. Public Serv. Comm'n,* 715 S.W.2d 482 (Mo. banc 1986) and recognized this again in *State ex rel. AG Processing Inc., v. Public Serv. Comm'n*, 120 S.W.3d 732, 736 (Mo. banc 2003). In *Love 1979 Partners*, the Missouri Supreme Court found the interest of the St. Louis metropolitan area in solving its refuse problems was an appropriate consideration of the Commission in its deciding whether to approve contracts for Union Electric Company to sell, pursuant to Section 393.190.1 RSMo, its Ashley generating plant and downtown St. Louis steam loop and for authority to discontinue its operations providing steam service.

In *AG Processing*, the Missouri Supreme Court found that although the acquisition premium recoupment issue could be addressed in a subsequent ratemaking case and the Commission may be unable to speculate about future merger related rate increases, the Commission must determine, when determining whether to approve the merger, (1) the reasonableness of the acquisition premium, and (2) whether UtiliCorp would be permitted to recoup the acquisition premium. The Court found these two items to be necessary and essential issues to be determined by the Commission when determining whether to approve the merger. Thus, if the decision of the Commission were to authorize GPE to acquire Aquila, the Commission must decide whether specific components of the Joint Applicants' proposal are reasonable and will be permitted by the Commission.

For purposes of this case and the proposed transaction in question, GPE's acquisition of Aquila, the creditworthiness of GPE/KCPL as a consequence of GPE's proposed acquisition of Aquila is a factor in determining whether the proposed transaction is detrimental to the public interest. Creditworthiness refers to the financial standing/status of GPE/KCPL, in particular, the investment grade rating of the GPE/KCPL debt.

Creditworthiness or credit quality was and is one of the key elements to the KCPL Regulatory Plan. In the case of the KCPL Regulatory Plan, there are criteria, i.e., financial ratios that the Signatory Parties have agreed to that are more specific than just the broad term investment grade status for KCPL debt. There are financial ratios that are used for purposes of calculating revenue requirement in rate cases.

Although there is indication that KCPL needs to successfully complete the KCPL Regulatory Plan in order for it, Aquila, and The Empire District Electric Company to provide safe and adequate service at just and reasonable rates, there is no indication in the record that GPE needs to acquire Aquila in order for either KCPL or Aquila to provide safe and adequate service at just and reasonable rates.

This Commission cannot bind the ratemaking decisions of a future Commission and administrative decisions are not subject to *stare decisis.* Thus, no matter what disposition the Commission might make in this case with respect to future ratemaking, there is no guarantee that that disposition would be implemented in the future.

It is well-established that there is no *stare decisis* respecting Commission decisions. *State ex rel. GTE North, Inc. v. Public Serv. Comm'n,* 835 S.W.2d 356, 371 (Mo.App. W.D. 1992); *State ex rel. General Tel. Co. v. Public Serv. Comm'n*, 537 S.W.2d 655, 661-62

(Mo.App. W.D. 1976)[114] (*General Telephone*); *State ex rel. Chicago, Rock Island & Pacific R.R. Co. v. Public Serv. Comm'n*, 312 S.W.2d 791, 796 (Mo. banc 1958); *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); *State ex rel. Arkansas Power & Light Co. v. Public Serv. Comm'n*, 736 S.W.2d 457, 462 (Mo.App. 1987); *State ex rel. Associated Natural Gas Co. v. Public Serv. Comm'n*, 706 S.W.2d 870, 880 (Mo.App. 1985); *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).

AGP itself is clear that this long-standing principle has not changed:

> . . . In support of its claim that the Applicants were required to submit a market power study, AGP cites several prior PSC decisions in which the PSC required merger applicants to file market power studies. However, an administrative agency is not bound by *stare decisis,* nor are PSC decisions binding precedent on this Court.[18] . . .
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> [18] *State ex rel. GTE N. Inc. v. Mo. Pub. Serv. Comm'n,* 835 S.W.2d 356, 371 (Mo.App.1992); *Cent Hardware Co., Inc. v. Dir. of Revenue,* 887 S.W.2d 593, 596 (Mo. banc 1994).

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[114] 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:

> 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.

Thus, the Joint Applicants know that even if this Commission grants the relief which the Joint Applicants have requested, this Commission cannot guarantee that a future Commission will not take different action. Equitable estoppel will not be available to the Joint Applicants if this were to happen. *Missouri Gas Energy v. Public Serv. Comm'n*, 978 S.W.2d 434 ((Mo. App. W.D. 1998).

Section 393.190. 1 RSMo. provides, in relevant part, as follows:

> **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. . . .**

Paragraph 34 of the Joint Application filed on April 4, 2007, which Joint Application was never amended by the Joint Applicants, states that GPE anticipates "the Merger will result in significant synergies, economies of scale, and efficiencies from the elimination of duplicate corporate and administrative services, all of which ultimately result in a lower cost of operations." These "synergies" will not result merely from the GPE acquisition of Aquila. These synergies can only occur from a merger or consolidation of the Aquila operations with the KCPL operations for which the Joint Applicants have not sought Commission authorization pursuant to Section 393.190.1.[115] KCPL's General Counsel and various GPE/KCPL witnesses

[115] The Commission has a rule, 4 CSR 240-3.115, specifying the minimum "Filing Requirements for Electric Utility Applications for Authority to Merger or Consolidate." This rule requires the filing of "a certified copy of the resolution of the Board of Directors of each applicant authorizing the proposed merger and consolidation." There is no copy of any resolution of the Board of Directors of either KCPL or Aquila authorizing any merger and consolidation of any aspects of their operations filed in this case. Staff's audit of the meeting minutes and presentations to the Boards of Directors of KCPL and Aquila did not reveal any such resolutions authorizing a

related at the evidentiary hearings the reasons why the transaction was not filed as a merger or consolidation of KCPL and Aquila pursuant to 393.190.1.[116]

No authority was sought by the Join Applicants to merge, consolidate, combine or integrate the utility operations of Aquila and KCPL. This dramatically affects the claims of synergies on the part of the Joint Applicants. The Joint Applicants have taken the position that such authority is not required. The Staff, Public Counsel and Industrial Intervenors have opposed that view and have also noted that there is no evidence of operating agreements where such agreements are necessary. It appears that the Joint Applicants' approach has been based on the concept that these details, if for example the Commission believes operating agreements are necessary, can be worked out later.

First of all, the Commission is not willing to grant relief that has not been requested or to consider synergies from a transaction the approval of which has not been sought. Although in some circumstances this issue might have been deemed to have been waived or have been "tried by consent of the parties" or that the original Joint Application had been "amended to conform to the evidence." That is not the case here. In this case the Industrial Intervenors have repeatedly objected through two Motions *In Limine* and through numerous objections to the consensual trial of this issue or to the consensual amendment of the Joint Application. Accordingly, in evaluating whether the proposed merger transaction is not detrimental to the public interest, the Commission will not consider offsets to costs in the form of synergies that are claimed to result

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merger or consolidation of any portion of the KCPL and Aquila systems or works. GPE acknowledged that there are no agreements between KCPL and Aquila to merge any utility functions or activities, except for the previously-filed transaction documents and, to the extent that they may be deemed to be agreements, the post-transaction integration plans. These plans are disclosed in the August 8, 2007, update filing.[115] As to its Board, KCPL noted that "[t]he Board has been kept apprised of the integration planning process. The Board has not been requested to approve the integration plans."[Footnote omitted].

[116] Vol.2, Riggins, Tr. 31-33; Giles, Tr. 251-55.

from the merger or consolidation, either direct or indirect, of the operating utilities of KCPL and Aquila. The Joint Applicants could have sought to amend their Joint Application to seek authority to merge, consolidate, integrate or combine the operations of these two operating utilities, with all that involves, but did not choose to do so for reasons GPE/KCPL only made known at the evidentiary hearings.

Second, even if the Commission were to consider the Joint Application to have been amended by consent (which the Commission does not), it would still have been necessary and incumbent upon the Joint Applicants to have placed before the Commission concrete proposals concerning the specifics of the plans to consolidate the operations of Aquila and KCPL, including but not limited to operating agreements and other plans, from which the Commission could make a decision regarding whether those items provided protection to the ratepayers of the standards of safe and adequate service, and otherwise no net detriment, if the operations were to be consolidated. Joint Applicants also chose not to provide such evidence though such was their obligation under Section 393.190.1.

Alternatively, the Commission could also determine that, even if the Commission were to consider that the original Joint Application had been amended by consent (which, again, the Commission does not do), by failing to provide evidence that would support a decision that such a merger of KCPL and Aquila was not detrimental to the public, Joint Applicants abandoned that effort and thus abandoned any claim, even if it were made, that the Joint Application had been amended by consent or that such authorization was not needed.

Under any of these interpretations or analyses, the Joint Applicants' case is found wanting as clearly detrimental to the public interest under existing Commission precedents and the law as it has been given to the Commission by the General Assembly and the Missouri Supreme Court.

For the Joint Applicants to proceed forward as they propose without obtaining the Commission's authorization pursuant to Section 393.190.1 to merge, consolidate, integrate, or combine the operations of Aquila and KCPL would constitute a void transaction which the Commission will not assist. The consequences of a void transaction are addressed in a number of Missouri cases: *State ex rel. Intercon Gas, Inc. v. Public Serv. Comm'n,* 848 S.W.2d 593 (Mo.App. 1993); *State ex rel. Consumers Public Serv. Co. v. Public Serv. Comm'n*, 180 S.W.2d 40 (Mo. banc 1944) (*Consumers*); *Public Serv. Comm'n v. Kansas City Power & Light Co.*, 325 Mo. 1217, 31 S.W.2d 67 (Mo. banc 1930).

Conclusion:

Based on its review of the Application, testimony and schedules, exhibits, hearing transcripts, briefs and argument, the Commission concludes that the transaction proposed by the Joint Applicants as amended by them after the suspension of the hearings on December 6, 2007 is detrimental to the public interest and should be denied.

IT IS THEREFORE ORDERED:

1. That the Joint Application filed on April 4, 2007 by the Joint Applicants, Great Plains Energy Incorporated, Kansas City Power & Light Company and Aquila, Inc., is hereby denied.

2. That this Report and Order shall become effective on __________.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that a true and correct copy of the foregoing has been mailed, hand-delivered, transmitted by facsimile or electronically served to all counsel of record this 6th day of June, 2008.

/s/ Kevin A. Thompson