STATE OF MISSOURI
PUBLIC SERVICE COMMISSION
JEFFERSON CITY

September 24, 1991

CASE NO. EM-91-213

John K. Rosenberg, Michael C. Pendergast & David Naugle, The Kansas Power and Light Company, 818 Kansas Avenue, Topeka, Kansas 66612
James M. Fischer, Akre, Wendt & Fischer, 102 East High Street, Suite 200, Jefferson City, Missouri 65101
Debra H. Janoski, Attorney at Law, Union Electric Company, 1901 Chouteau Ave., P.O. Box 149 (M/C 1310), St. Louis, Missouri 63166
Stuart W. Conrad, Paul S. DeFord, Attorneys, 2600 Mutual Benefit Life Bldg., Kansas City, MO 64108
Paul W. Phillips, United States Department of Energy, 1000 Independence Ave., S.W., Room 6D-033, Washington, D.C. 20585
Gary W. Duffy, Brydon, Swearengen & England, P.O. Box 456, Jefferson City, Missouri 65102
Lewis R. Mills, Jr., Attorney, Office of the Public Counsel, P.O. Box 7800, Jefferson City, Missouri 65102
Robert C. Johnson & Catherine Moore, Peper, Martin, Jensen, Maichel & Hetlage, 720 Olive St. 24th Floor, St. Louis, Missouri 63101

Enclosed find certified copy of ORDER in the above-numbered case(s).

Sincerely,

Brent Stewart

Brent Stewart
Executive Secretary

Uncertified Copy:

Gary L. Myers, General Counsel & Secretary, St. Joseph Light & Power Company, 520 Francis Street, St. Joseph, Missouri 64502
Dennis Williams, Director of Regulation, Utilicorp United, Inc., P.O. Box 13287, Kansas City, Missouri 64199

Mark G. English, Kansas City Power & Light Company, 1330 Baltimore Avenue, Kansas City, Missouri 64105

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Robert C. Yardley, Jr., Chairman, Department of Public Utilities, Leverett Saltonstall Building, Government Center, 100 Cambridge Street, Boston, MA 02202

BEFORE THE PUBLIC SERVICE COMMISSION

OF THE STATE OF MISSOURI

In the matter of the application of The Kansas Power and Light Company and KCA Corporation for approval of the acquisition of all classes of the capital stock of Kansas Gas and Electric Company, to merge with Kansas Gas and Electric Company, to issue stock, and incur debt obligations.	))))))	CASE NO. EM-91-213

APPEARANCES: Michael C. Pendergast, Managing Attorney - Regulation
John K. Rosenberg, Executive Vice President, General Counsel and Secretary, The Kansas Power and Light Company, 818 Kansas Avenue, Topeka, Kansas 66612, and
J. Michael Peters, Attorney at Law, P. O. Box 208, Wichita, Kansas 67201, for The Kansas Power and Light Company.

Mark G. English, Deputy General Counsel, Kansas City Power & Light Company, 1330 Baltimore Avenue, Kansas City, Missouri 64105, and
James M. Fischer, Attorney at Law, Akre, Wendt & Fischer, 102 East High Street, Suite 200, Jefferson City, Missouri 65101, for Kansas City Power & Light Company.

Arthur L. Smith, Catherine L. Moore, and Robert C. Johnson, Attorneys at Law, Peper, Martin, Jensen, Maichel and Hetlage, 720 Olive Street, 24th Floor, St. Louis, Missouri 63101, for Industrial Intervenors: The Quaker Oats Company, et al.

Paul W. Phillips, Deputy Assistant Counsel for Regulatory Interventions, United States Department of Energy, 1000 Independence Avenue, S. W., Washington, DC 20585, and
W. L. Rowberry, Attorney at Law, P. O. Box 202, Kansas City, Missouri 64141, for United States Department of Energy and Federal Executive Agencies.

Stuart W. Conrad, and Paul S. DeFord, Attorneys at Law, Lathrop, Norquist & Miller, 2345 Grand Avenue, Kansas City, Missouri 64108, for Armco Inc. and Midwest Gas Users Association.

Sondra B. Morgan, and James C. Swearengen, Attorneys at Law, Brydon, Swearengen & England, P.C., P. O. Box 456, Jefferson City, Missouri 65102-0456, for Missouri Public Service and St. Joseph Light & Power Company.

Lewis R. Mills, Jr., First Assistant Public Counsel, Office of the Public Counsel, P. O. Box 7800, Jefferson City, Missouri 65102, for Office of the Public Counsel and the Public.

Steven Dottheim, Deputy General Counsel, Robert J. Hack, Assistant General Counsel, and William M. Shansey, Assistant General Counsel, Missouri Public Service Commission, P. O. Box 360, Jefferson City, Missouri 65102, for Staff of the Missouri Public Service Commission.

HEARING EXAMINER: Beth O'Donnell

REPORT AND ORDER

Procedural History

On November 21, 1990, The Kansas Power and Light Company (KPL or Applicant) and its wholly-owned subsidiary, KCA Corporation (KCA), filed an application in this case requesting authority to acquire, and merge with, Kansas Gas and Electric Company (KGE). By order issued December 18, 1990, the Commission established a procedural schedule for this case and directed its Executive Secretary to provide notice of this application.

The Commission granted the applications to intervene of Quaker Oats Company, General Motors Corporation, Rockwell International, Cargill, Inc., Archer-Daniels Midland, Ford Motor Company, Missouri Portland Cement Company, and AT&SF Railway (collectively referred to hereinafter as Industrial Intervenors); Armco, Inc., and Midwest Gas Users Association (collectively referred to hereinafter as MGUA); Kansas City Power & Light Company; Union Electric Company; St. Joseph Light & Power Company; Missouri Public Service, a division of UtiliCorp United, Inc.; and the United States Department of Energy and the Federal Executive Agencies. The Commission's Staff (Staff) and the Missouri Office of the Public Counsel (Public Counsel) also participated in this case.

Testimony was prefiled in this case by KPL, Staff and Public Counsel. Pursuant to the prehearing conference a hearing memorandum was filed in the case delineating the positions of the parties and an oral hearing was held May 6 through May 10, 1991. Briefs were filed by the parties pursuant to a schedule established by the hearing examiner.

Two motions remain outstanding in this case. The first is a motion to strike and the second is a motion for leave to file position statement out-of-time. The motion to strike was made shortly prior to hearing but both KPL and Staff requested that the Commission take the motion with the case and refrain from ruling on it until the Report and Order thereby giving the parties a chance to brief it.

KPL moves to strike all references to the studies of John W. Mayo and Rodney Stevenson and all testimony and calculations presented by the Staff based on these studies including those references and calculations appearing in the Report submitted by the Law and Economics Consulting Group, Inc. (LECG) on behalf of Staff and at page 5 of the rebuttal testimony of Dr. Raymond S. Hartman. KPL asserts that it will be denied due process because no witness on behalf of Staff will be available for meaningful cross-examination on the Mayo and Stevenson studies on the results of which the LECG based much of its studies and calculations. KPL urges the Commission to exclude these matters from evidence since Mayo and Stevenson were not present to cross-examine.

The Staff responds to the motion to strike by stating that the testimony of Dr. Hartman, who is the Staff's witness sponsoring the portions of the LECG Report containing the Mayo and Stevenson studies, is admissible as the opinion testimony of a qualified expert. Staff notes that experts are permitted to rely upon published or reported data in forming their expert opinions.

The Commission determines that the motion to strike should be denied and will do so hereinafter. There are three exhibits the receipt into evidence of which was withheld pending a ruling on the motion to strike. These are Exhibits 30, 59, and 62, which the Commission will receive into evidence in their entirety since the motion to strike will be denied.

Exhibit numbers were reserved for Exhibits 65, 77, 77HC and 78 so that these exhibits could be late-filed. All four of these exhibits have been submitted to the examiner and the reporter has received them for marking. There being no objection to these four exhibits, the Commission will receive them.

Exhibits 38 and 47 were not offered and will not be received into evidence by the Commission.

On July 1, 1991, MGUA filed a motion for leave to file position statement out-of-time. In support of its motion MGUA states that due to the press of other business MGUA was unable to meet the deadline for filing an initial brief which was June 25, 1991. MGUA states that acceptance of its position paper will not prejudice any party because all parties will have adequate opportunity to respond to the position statement in their reply briefs which were due July 10, 1991. No party filed in opposition to this motion. The Commission determines that the motion should be denied since MGUA had ample opportunity to request an extension.

Findings of Fact

The Missouri Public Service Commission, having considered all the competent and substantial evidence on the whole record, makes the following findings of fact.

KPL is a Kansas corporation authorized to do business in the State of Missouri. KPL provides gas service in the states of Missouri and Oklahoma, and both gas and electric service in Kansas. KGE is a Kansas corporation providing electric service in the State of Kansas.

By this application KPL requests that the Commission authorize KPL to acquire all of the capital stock of KGE and merge KGE into KCA which is a Kansas corporation and a wholly-owned subsidiary of KPL. KCA would then change its name to Kansas Gas and Electric Company.

KPL also requests the Commission authorize it to issue stock and debt to finance the acquisition. Specifically, KPL seeks authority to issue up to approximately $28 million in shares of KPL common stock to holders of KGE's common stock and to issue debt in the amount of $600 million, $500 million of which would be senior-term debt and $100 million of which would be a revolving loan facility. The proposed financing would be secured by at least $250 million of KPL's first mortgage bonds and 100 percent of the capital stock of KCA.

Pursuant to the merger agreement KPL would purchase KGE's common stock at the price of $32 per share by a combination of cash and the newly issued KPL stock. KPL states that by mixing cash and debt in buying KGE's common stock the debt ratio of the combined companies would remain within the bounds of a typical utility. Based upon 30,989,036 shares outstanding of KGE common stock, the offer has a value of $992 million of which $434 million would be in cash with $24 million to $28 million in newly issued shares of KPL stock, the exact amount depending on the average closing price of KPL stock for 15 consecutive trading days preceding the fifth trading day before the effective date of the merger. KPL will redeem KGE's preferred stock, including payment of accrued dividends for cash, according to the terms of each issue, at a cost of $19.7 million.

The total cost of the acquisition would be $1,031.7 million with $388 million being the amount of the acquisition premium.

The basic matter at issue in this case is whether the Commission should authorize KPL to acquire, and merge with, KGE. The Commission may not withhold its approval of this proposed merger unless the merger is detrimental to the public interest. *State ex rel. City of St. Louis v. Public Service Commission of Missouri*, 335 Mo. 448, 73 S.W.2d 393, 400 (Mo. banc 1934). *State ex rel. Fee Fee Trunk Sewer, Inc. v. Litz*, 596 S.W.2d 466, 468 (Mo. App. 1980).

Applicant's primary tool for examining the propriety of the proposed merger is the Merger Report. In the Merger Report, Applicant states that the proposed merger will not be detrimental to the public interest because it will result in substantial savings for the merged companies of costs which would otherwise be incurred by each company individually. These savings would occur in such areas as consolidation of distribution functions, integration of dispatching and production operations and streamlining of inventories and purchasing economies. Applicant anticipates savings of $140 million for the entire company over the five years following merger. Applicant admits that the majority of these savings will not directly affect the Missouri jurisdiction.

Applicant anticipates that the merger will directly affect the Missouri jurisdiction in the areas of administrative and general (A&G) costs, capital costs and the cost of the service line replacement program. Applicant believes that the merger will generate sufficient cash flow to finance the service line replacement program without borrowing outside funds. This improved cash flow is expected to arise from the seasonal and cyclical nature of the cash flow of the separate companies. The lowered capital costs are expected to arise from debt leveraging and the lowered A&G costs are expected to arise from lowered personnel, vehicle and facilities costs. In total, Applicant projects direct savings affecting the Missouri jurisdiction of at least $60 million of the $140 million savings for the total company over the first five years of the merger.

KPL not only requests that the Commission approve the proposed merger but permit Applicant to institute a program of sharing the merger savings between shareholders and ratepayers with each receiving 50 percent. To ensure that only savings resulting from the proposed merger are shared by Applicant's shareholders, KPL proposes that a cost savings tracking system (CSTS) be established. The purpose of the CSTS would be to separate savings which would have occurred without the merger from those generated solely by the merger so that only ratepayers would benefit from nonmerger savings while merger savings would be split with shareholders. Company views the savings sharing plan as an integral part of the proposed merger and its chief executive officer states, in effect, that he would need to reassess the decision to merge if the Commission should approve the merger without approving the sharing plan. In its initial brief, KPL states, "(w)ithout a means to recover those (merger) costs, the merger will not occur...."

Staff feels that Applicant's projection of savings is inflated and that there is a substantial risk of increased costs flowing from the merger to the Missouri ratepayers.

Staff asserts that the Merger Report only evaluates the effect of the merger on the entire multijurisdictional company rather than on KPL in Missouri alone, thereby creating an illusion of benefit to Missouri ratepayers. Staff argues that most of the savings which KPL estimates would arise from the proposed merger would benefit the ratepayers of other jurisdictions, not the ratepayers of Missouri.

Staff states that the effect of the proposed merger on Missouri ratepayers would be in the areas of A&G and capital costs. Staff foresees that A&G costs will rise significantly. In addition, Staff anticipates that capital costs would rise after the proposed merger following an initial fall. Staff admits that KPL's initial capital costs would fall because the debt incurred by KPL to acquire KGE would result in the phenomenon known as debt leveraging whereby the capital costs of a company drop when it increases the amount of debt in its capital structure vis-a-vis equity since debt is the less expensive form of capital.

However, Staff believes that, since KPL's bond rating will fall as a result of KGE's lower bond rating, the merged company would ultimately experience higher costs for capital due to the lowered bond rating. Staff further believes that this higher cost of capital, plus the higher A&G costs Staff anticipates, would be passed on to the Missouri ratepayers to their detriment unless the allocation of costs by the total company to Missouri ratepayers were cut significantly.

Staff also views the possibility of increased capital costs as a threat to the ability of KPL to finance the service line replacement program. Staff views as inflated and unrealistic KPL's estimates of vastly increased cash flows resulting from the proposed merger which could be used to fund the service line replacement program.

Therefore, Staff recommends that the Commission deny the application for authority to merge. In the alternative, Staff recommends that, should the Commission approve the proposed merger, certain conditions be imposed on KPL by the Commission to shield Missouri ratepayers from any detriment. Most of these conditions are in the nature of ceilings which would be applied to KPL's cost of capital and A&G expenses in postmerger rate cases. If KPL's costs were to rise above these ceilings, these excess costs would be presumed to be associated with the merger and would not be permitted to be reflected in the ratemaking process.

Staff maintains that the Commission should adopt these conditions now to protect Missouri ratepayers from any increased costs and to give KPL advance notice of the rate treatment it can expect so that KPL makes an informed decision as to whether to proceed with the merger.

Staff also recommends that the savings sharing plan be rejected. Staff sees the sharing plan as nothing more than a means for KPL to recover the costs of the merger, including the acquisition premium, at the expense of Missouri ratepayers.

Public Counsel and the Industrial Intervenors agree with Staff that the application to merge should be denied but if the application is approved, Public Counsel and the Industrial Intervenors would place conditions on KPL substantially similar to Staff's except that the Industrial Intervenors would impose a true-up on KPL between rate cases to assure that ratepayers share in <u>all</u> merger-related savings and would treat KPL and KGE as separate companies for ten years for purposes of ratemaking. DOE recommends that the Commission approve the application for merger only if the Commission imposes Staff's conditions. In opening statements MGUA stated that, only if Missouri ratepayers can be shielded from detriment, should the merger be approved.

The Commission determines that KPL should be authorized to acquire and merge with KGE. While the Commission finds there is some merit to the arguments of the parties opposing the merger as to the undue optimism of KPL in regard to the merger and its failure to use the latest analytical techniques in assessing the propriety of the merger, the Commission does not agree that KPL has failed to show that some savings will result from the merger. The Merger Report shows substantial savings and no party has suggested that KPL would experience no savings resulting from the merger.

The issue among the parties actually concerned the amount and distribution of the savings and whether enough of those savings would be allocated to the Missouri jurisdiction to offset increased costs allocated to the Missouri jurisdiction. Although the Commission is doubtful that KPL will experience the level of savings projected by its management as a result of the merger and even if the cash flows projected as a result of the merger do not materialize, no party argues that KPL will be unable to borrow the money necessary to complete the pipeline replacement program to which it has committed itself or that such a financing would be ruinously expensive. Therefore, the Commission determines that KPL's management should be permitted to proceed with the merger since there is no evidence in this case showing that the merger would interfere with KPL's capacity to render safe and adequate service to its Missouri ratepayers.

However, the Commission believes there is considerable merit in the concerns of the other parties that detriment could accrue to the Missouri ratepayers as a result of the merger through increased capital and A&G expenses. Although all parties agree that KPL's capital costs would initially fall due to debt leveraging, the evidence indicates that KPL's capital costs might eventually rise in the future because KGE's lower bond rating is expected to lower KPL's higher bond rating. This possibility is particularly salient because KPL might need to borrow money to pursue its service line replacement program if increased cash flows do not materialize as KPL expects as a result of the merger. The evidence also indicates that the A&G costs of merged companies often rise more precipitously than the A&G rates of companies that have not merged. Thus, it is reasonable to anticipate such an increase in A&G costs following KPL's merger with KGE.

The Commission further believes it is important that Missouri ratepayers be shielded from any possible ill effects from the merger. The evidence brought forward by Staff indicates that some of KPL's estimates of savings might be unduly optimistic and many of the savings, even if they do materialize, will not benefit Missouri ratepayers. Because of these possibilities, along with the chance that A&G and capital costs might ultimately increase, the Commission believes it is essential that Applicant understand that the Commission will take all necessary steps to protect Missouri ratepayers from any such ill effects.

First, the Commission will not approve at this time the savings sharing proposal. Staff has persuasively argued that KPL has a strong incentive to view savings as merger-related even if they are not and to classify them in the CSTS so as to increase the pool of savings subject to the sharing plan. Staff demonstrated several flaws in the CSTS which could allow nonmerger savings to seep into the pool of savings to be shared.

The Commission is not opposed to the concept of the savings sharing plan provided that only merger-related savings are shared. The Commission does not wish to discourage companies from actions which produce economies of scale and savings which can benefit ratepayers and shareholders alike. However, the Commission wishes to ensure that savings which would have been offset against the cost of service without the merger, benefit ratepayers one hundred percent. To avoid any detriment to ratepayers it is imperative that only savings which would not have occurred absent the merger be shared by ratepayers with shareholders.

The Commission is not convinced that KPL's tracking plan will exclude all nonmerger savings from the pool of merger savings to be shared. The Commission notes with approval that Staff suggested various methods which would help prevent such seepage. However, the Commission believes that no tracking plan can work without the cooperation of KPL. Therefore, the Commission will direct the parties to meet for the purpose of attempting to devise a method for tracking merger-related savings. If the parties are unable to agree on such a system within sixty days, the Commission will hold a hearing to gather the information necessary to decide if any tracking plan can exclude nonmerger-related savings and, if so, which system would be best suited to this purpose.

Second, the Commission will not permit costs generated by the merger to flow to Missouri ratepayers through increased A&G and capital costs. The Commission believes it is premature to establish benchmarks by which KPL's expenses will be judged in subsequent rate cases. However, the Commission places Applicant on notice that merger expenses will not be allowed to adversely affect the cost of service in Missouri.

Increases in capital costs due to a lower bond rating or other effects of the merger will not be allowed to increase Missouri rates. Any increased capital costs will not be permitted to adversely affect the pipeline replacement program to which KPL has committed itself.

The Commission will direct its Staff to carefully audit KPL in future rate cases to screen out costs caused by the merger and to suggest methods, if necessary in future rate cases, such as those recommended herein, which might be used to shield Missouri ratepayers from costs arising from the merger.

The Commission will also direct KPL to keep its books so that costs associated with the merger are clearly segregated. Abnormal increases in A&G expenses will be carefully scrutinized and, unless persuasively explained as not related to the merger, will be associated with the merger. In that regard the Commission notes that KPL and Staff have agreed on various features to be incorporated into the payroll accounting system of KPL to enable Staff to determine whether A&G costs are being properly allocated following the merger. This agreement is set forth in Exhibit 67 which is attached to this Report and Order as Attachment A and incorporated herein by reference. No party opposes this agreement between KPL and Staff. The Commission finds this stipulation between KPL and Staff to be reasonable and will approve this agreement of Staff and KPL.

Staff points out that KPL has done no study of how allocations might change as a result of the proposed merger. KPL has proposed that the postmerger allocation of costs be examined either in the course of KPL's first postmerger rate case or through the convening of a multijurisdictional workshop or panel to recommend a postmerger allocation process. Staff believes that studying the allocation process to find the appropriate allocation formula is fundamental to protecting Missouri ratepayers from merger costs and fairly allocating savings to the Missouri jurisdiction.

Staff recommends that the Commission require KPL to do a detailed allocation study subject to the Commission's approval by at least the end of five years after the merger in order to determine the appropriate allocation of A&G expenses to the different jurisdictions. The Commission will adopt Staff's recommendation in this case in order to ensure that a thorough allocation study is completed which focuses on the need to protect Missouri ratepayers from unfair allocation of costs and savings.

The Commission believes that, by committing itself to these protections for Missouri ratepayers, it is possible to find in this case no detriment to the public interest arising from the proposed merger as required by Missouri case law.

Having approved the proposed merger, the Commission has considered the request of KPL for approval of the financing necessary to effectuate the merger. No party has questioned the proposed financing. The Commission determines that the money and property to be procured by the issuance of such stocks, bonds, notes or other evidences of indebtedness are reasonably required for the purposes specified in this order and such purposes are not, in whole or in part, reasonably chargeable to operating expenses or to income.

The Commission determines that the fees authorized pursuant to Section 386.300, RSMo 1986, apply to this financing to the extent that this issuance is not used to discharge any bond, note or other evidence of indebtedness. The Commission will direct KPL to file journal entries with the Commission's Internal Accounting Department so that a determination can be made as to the amount of fees to be paid, if any.

Finally, Staff has requested that the Commission find KPL's planned preference stock issue, authorized by the Commission May 31, 1991, in Case No. GF-91-374, merger related. The Commission determines that Staff's request is inappropriate in this docket since this docket is not considering the propriety of the preference stock issue. As stated in the order authorizing issuance of the preference stock, the appropriate docket to address this question is KPL's pending rate case, GR-91-291.

Conclusions of Law

The Missouri Public Service Commission has arrived at the following conclusions of law.

KPL is a public utility rendering gas service in the State of Missouri under the jurisdiction of this Commission pursuant to Chapters 386 and 393, RSMo 1986, as amended. The Commission has jurisdiction of this case pursuant to Sections 393.180, 393.190, and 393.200, RSMo 1986. Section 393.190, RSMo 1986, provides, in pertinent part, that no gas or electric corporation shall merge its works or system or franchise with any other corporation without having first secured from the Commission an order authorizing it to do so.

The Commission may not withhold its approval of the disposition of assets unless it can be shown that such disposition is detrimental to the public interest since to deny a property owner the opportunity to dispose of such assets, in the absence of a showing of detriment to the public, would be to deny the property owner an important aspect of property ownership. *State ex rel. City of St. Louis, op. cit.*, *State ex rel. Fee Fee Trunk Sewer, Inc., op. cit.*

The Commission has found no evidence in this record that KPL would be unable to render safe and adequate service to its Missouri ratepayers as a consequence of the proposed merger. However, the Commission has found that the savings sharing plan proposed by KPL as part of its merger application has the potential of exposing Missouri ratepayers to higher rates than would be the case without the merger which would be detrimental to the public interest. Therefore, the Commission has determined that the savings sharing plan should not be approved until the Commission can be assured that no nonmerger savings can seep into the pool of merger savings which would be shared between ratepayers and shareholders.

The Commission has also found that there is the potential for a detrimental effect on Missouri ratepayers from the merger through increased A&G and capital costs. Therefore, the Commission, in order to shield Missouri ratepayers from such detriment, has made it clear to KPL that such costs will be carefully scrutinized in any future, postmerger rate case to assure that no such detriment is suffered by Missouri ratepayers.

Based upon these findings and determinations, the Commission concludes that Missouri ratepayers will be shielded from any potential ill effects from the proposed merger and will suffer no detriment as a result. Therefore, the Commission concludes that, in the absence of a finding of detriment to the public interest, it may not withhold its approval of the proposed merger and will authorize KPL to acquire and merge with KGE.

Section 393.180, RSMo 1986, vests in this Commission the supervision of the privilege of gas corporations to issue stocks, bonds, notes and other evidences of indebtedness. Section 393.200, RSMo 1986, provides, in pertinent part, that a gas corporation incorporated by virtue of the laws of this state may issue stocks, bonds, notes or other evidences of indebtedness provided there shall have been secured from the Commission an order authorizing such issue, stating the amount thereof and the purposes to which such issue is to be applied, and the opinion of the Commission that the money and property to be procured or paid for by such issuance is reasonably required for the purposes specified in the order and not in whole or in part reasonably chargeable to operating expenses or income.

The Commission has determined the amount of the financing and the purposes to which it is to be applied. The Commission has also determined that the proposed financing is reasonably required for the purposes set forth herein and is not in whole or in part reasonably chargeable to operating expenses or income. Therefore, the Commission concludes, pursuant to Sections 393.180 and 393.200, RSMo 1986, that the proposed financing should be approved.

Pursuant to Section 536.060, RSMo 1986, the Commission may approve a stipulation and agreement concluded between parties to a contested case. The Commission has determined that the agreement of KPL and Staff as to payroll accounting procedures is reasonable and, therefore, the Commission concludes that this stipulation should be approved.

IT IS THEREFORE ORDERED:

1. That Kansas Power and Light Company be authorized hereby to acquire all the capital stock of Kansas Gas and Electric Company and to merge Kansas Gas and Electric Company into KCA Corporation.

2. That Kansas Power and Light Company be authorized hereby to incur debt and borrow funds up to an amount of six hundred million dollars ($600,000,000) of which five hundred million dollars ($500,000,000) will be in senior-term debt and one hundred million dollars ($100,000,000) will be in a revolving loan facility for the purpose of achieving the merger authorized herein with any unused amount available for working capital.

3. That Kansas Power and Light Company be authorized hereby to issue and pledge two hundred fifty million dollars ($250,000,000) of its First Mortgage Bonds and one hundred percent (100%) of the capital stock of KCA Corporation to secure the financing authorized herein and to create any lien which such issuance and pledge might produce.

4. That Kansas Power and Light Company be authorized hereby to issue new common stock in its company to the holders of common stock in Kansas Gas and Electric Company in an amount not exceeding twenty-eight million (28,000,000) shares for the purpose of achieving the merger authorized herein.

5. That Kansas Power and Light Company be authorized hereby to execute and deliver any and all documents and agreements necessary to effectuate the authority granted herein.

6. That Kansas Power and Light Company be directed hereby to conduct a study to identify the appropriate allocation of costs and savings after the merger among the various jurisdictions in which Kansas Power and Light Company operates and to submit the preliminary results of such study to the Commission's Energy Department on or before December 31, 1992, at which time deadlines will be set for the submission of final results.

7. That the Commission's Staff be directed hereby to carefully audit Kansas Power and Light Company in future rate cases to screen out costs caused by the merger authorized herein.

8. That Kansas Power and Light Company be directed hereby to keep its books so that costs associated with the merger are clearly segregated from other costs.

9. That the parties to this case be directed hereby to meet for the purpose of attempting to devise a merger savings tracking plan (MSTP) which will ensure that all nonmerger savings can be excluded from the merger savings to be shared between ratepayers and shareholders. The parties shall file this plan with the Commission for its approval on or before
November 22, 1991.

10. That a hearing be set hereby commencing at 10:00 a.m. on December 4, 1991, at the Commission's hearing room on the fifth floor of the Truman State Office Building, 301 West High Street, Jefferson City, Missouri, to address the matter of the merger savings tracking plan (MSTP). This hearing shall be cancelled if the parties are able to agree on a tracking system acceptable to this Commission.

11. That nothing in this order shall be considered as a finding by the Commission of the reasonableness of the expenditures herein involved or of the value

for ratemaking purposes of the properties herein involved or as an acquiescence in the value placed upon said properties by Kansas Power and Light Company. Furthermore, the Commission reserves the right to consider the ratemaking treatment to be afforded these transactions, the resulting cost of capital and any proper adjustment to the cost of capital resulting therefrom in any later proceeding.

12. That Kansas Power and Light Company be directed hereby to file journal entries with the Commission's Internal Accounting Department so that the amount, if any, of the fees authorized pursuant to Section 386.300, RSMo 1986, might be calculated and assessed.

13. That the motion to strike portions of the Report prepared by the Law and Economics Consulting Group, Inc., on behalf of the Commission's Staff and the rebuttal testimony of Raymond S. Hartman, made by Kansas Power and Light Company be denied hereby.

14. That Exhibit Nos. 30, 59, 62, 65, 77, 77HC and 78, be received hereby into evidence.

15. That the motion for leave to file position statement out-of-time made by Armco, Inc., and Midwest Gas Users Association, be denied hereby.

16. That any objections not heretofore ruled upon be overruled hereby and any motions remaining outstanding be denied hereby.

17. That this Report and Order shall become effective on the 4th day of October, 1991.

BY THE COMMISSION

Brent Stewart

Brent Stewart
Executive Secretary

(S E A L)

Steinmeier, Chm., Concurs in separate opinion.
Rauch, McClure and Perkins, CC., Concur.
Mueller, C., Dissents in separate opinion.
All certify compliance with the provisions of Section 536.080, 1986.

Dated at Jefferson City, Missouri, on this 24th day of September, 1991.

ATTACHMENT A

PAYROLL ALLOCATIONS

In order to address Staff's concerns about allocating payroll on an ongoing basis after the merger, the Company agrees to include the following features in its payroll accounting system:

1. The Company will incorporate a four week payroll monitoring period completed annually to provide the basis for the ensuing year's payroll distribution. Judgment will be incorporated to provide for known exceptions to the four week monitoring period. To the extent judgment is incorporated, it shall be noted and the reasons for the exceptions shall be documented and maintained.

2. The system will provide for "exception" reporting to facilitate temporary activities, or changes in activities, from normal payroll allocations.

3. The system will allow individuals to make permanent changes in payroll distributions as job functions change.

4. Documentation will be retained for individual and departmental distributions. Documentation will be maintained in greater detail than is presently the case.

5. The Company will exercise its best efforts to work to insure consistent payroll allocations between individuals and departments.

6. The system will provide flexibility to charge payroll:
   a) between jurisdictions;
   b) between capital and O&M;
   c) to track merger & acquisitions activity; and
   d) to track nonregulated activities.

7. The system will provide to Staff, as needed, the basis for payroll allocation percentages for specific individuals or departments; and

8. Evaluate the use of a "common" department for the purpose of collecting operating payroll costs not directly assigned to a specific jurisdiction, and develop a method to allocate common pool of costs.

For a one year period following the merger, or until such time when the information is deemed no longer necessary, the Company will also do the following:

1. Track all payroll costs associated with the KPL/KGE merger, including the Integration Planning activities;

2. Evaluate the use of a "common" department for the purpose of collecting operating payroll costs not directly assigned to a specific jurisdiction, and develop a method to allocate common pool of costs; and

3. Exercise its best efforts to estimate merger-related payroll charges incurred from July 23, 1990 through the completion of the merger.

4. Documentation will be retained for individual and departmental distributions. Documentation will be maintained in greater detail than is presently the case.

Exhibit No. 62
Date 5-10-91 Case No. EM-91-

CONCURRING OPINION OF CHAIRMAN WILLIAM D. STEINMEIER
Case No. EM-91-213
KPL/KG&E Merger Case

I concur in the Commission's Report and Order approving the merger and providing for the possibility of a savings sharing plan, although I would have ideally preferred that the savings sharing plan be less contingent than it is.

I believe that a savings sharing plan will provide a strong incentive to the Company to achieve and realize all potential savings out of the merger. In fact, a savings sharing plan provides a far greater incentive to achieve nonmerger-related savings, as well. Nonmerger savings are less likely to be realized under traditional regulation, where such savings are flowed through to ratepayers in their entirety just as quickly as regulators can make it so.

However, I conclude that this merger case is not the ideal setting for establishing a broader incentive regulation plan for gas or electric utilities. The cost-savings projected by Company to occur as a result of the merger itself are an important part of assessing that the merger would not be a detriment to the public. Therefore, to separate merger-related savings from nonmerger-related savings is appropriate for purposes of any savings sharing plan arising out of this case, and a reasonably precise tracking plan must be developed.

For these reasons, I concur in the majority decision of the Commission in this Case.

Respectfully submitted,

William D. Steinmeier, Chairman

Dated: September 24, 1991

DISSENTING OPINION OF COMMISSIONER ALLAN G. MUELLER
Case No. EM-91-213
KPL/KGE Merger

I respectfully dissent from the Report and Order adopted in this case by a majority of the Commissioners. Although I do not oppose approving the merger, I would reject KPL's savings sharing plan. First, I do not believe it is possible to make the merger savings tracking plan (MSTP) foolproof. It will be in the interest of KPL to classify as many savings as possible as being the result of the merger even though they might have occurred without the merger. Even the most competent auditor will not be able to find and exclude all such instances of miscategorization. Therefore, I believe that savings which would have occurred without the merger will be included in the MSTP to be shared with the stockholders. Without the merger these nonmerger savings would be used one hundred percent to offset the cost of service.

Premerger statistics of the net utility gas plant of KPL indicate a thirty-nine percent jurisdiction for Missouri. This in turn translates into fourteen percent of the total premerger KPL utility plant. On the revenue side, the Missouri jurisdiction accounts for twenty-four percent of the premerger revenues. Given the complexity of translating these factors into a postmerger context, I do not feel that a multijurisdictional tracking plan can be sophisticated enough to accurately reflect the interests of the Missouri ratepayers.

Second, I believe the sharing plan is an indirect way to recover the acquisition premium even though this premium will not be recovered from rates but rather from any savings generated by the merger. Since normally in ratemaking all savings offset the cost of service, sharing one-half of merger savings with shareholders will pay for the acquisition premium resulting in companies being less concerned about bargaining for the lowest possible price for assets purchased. I believe this sends the wrong signal to companies regarding mergers and acquisitions.

Third, I oppose the sharing plan because I believe it will create a climate conducive to acquisitions. While I am not opposed to acquisitions, I do not believe this Commission should create the impression of promoting acquisitions. It is true that some acquisitions can lead to economies of scale and savings which can benefit both ratepayers and shareholders. However, even without the sharing plan, the shareholders of KPL can benefit from any savings generated by this merger because shareholders will benefit one hundred percent from all savings generated as long as no rate case or complaint case is filed.

Fourth, I believe fairness requires that the Commission reject this sharing plan since KPL did not offer to share the benefit with ratepayers when it purchased The Gas Service Company below its book value.

Finally, I oppose the sharing plan because KPL's management does not deserve the reward of having its shareholders receive fifty percent of the merger-related savings which otherwise would be used entirely to offset the cost of service. KPL offered the Commission in this case an optimistic scenario on the results of the merger and did not have available for this Commission the conservative scenario which was generated by Morgan Stanley for Kansas Gas and Electric Company. This failure denied the Commission access to a full range of information on the propriety of the merger.

I feel there is significant risk for the ratepayer as it relates to this merger. Only time will tell whether there are any savings and how it will be shared. But one thing is certain, stockholders may come and go but the ratepayers remain customers of this monopoly. While I believe KPL barely carried the burden of proof to show no detriment to the Missouri ratepayers, given the safeguards this Commission has committed itself to, I do not believe that the case offered to this Commission by KPL deserves the reward implied by even contemplating approval of the sharing plan.

Therefore, I would reject the sharing plan outright rather than give the parties an opportunity to convince the Commission that a tracking plan can be devised which will redeem the drawbacks inherent in the sharing plan.

Respectfully submitted,

Allan G. Mueller

Allan G. Mueller, Commissioner

STATE OF MISSOURI

OFFICE OF THE PUBLIC SERVICE COMMISSION

I have compared the preceding copy with the original on file in this office and I do hereby certify the same to be a true copy therefrom and the whole thereof.

WITNESS my hand and seal of the Public Service Commission, at Jefferson City, Missouri, this 24th day of September, 1991.

Brent Stewart

Brent Stewart
Executive Secretary