Exhibit No.:
Issues: MEPPH Capacity Contract, Off-System Sales, and Jeffrey Shares
Witness: Stephen L. Ferry
Sponsoring Party: Missouri Public Service
Case No.: ER-2001-672

Before the Public Service Commission
of the State of Missouri

Rebuttal Testimony

of

Stephen L. Ferry

****Denotes Highly Confidential Information****

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BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI
REBUTTAL TESTIMONY OF STEPHEN L. FERRY
ON BEHALF OF MISSOURI PUBLIC SERVICE,
A DIVISION OF UTILICORP UNITED INC.
CASE NO. ER-2001-672

Q. Please state your name and business address.

A. My name is Stephen L. Ferry. My business address is 10750 East 350 Highway, Kansas City, Missouri.

Q. Are you the same Stephen L. Ferry who submitted direct testimony in this case?

A. Yes.

Q. Are there any changes to your work experience since the filing of your direct testimony in this case?

A. Yes. Effective July 1, 2001, I was named Vice President, Wholesale Power Services. In this position I continue to be responsible for planning, developing and recommending power supply strategies and proposals for UtiliCorp's regulated wholesale power supply business unit. I also continue to be responsible for procuring fuel for UtiliCorp's domestic regulated coal-fired generating plants.

Q. Do you have any corrections to your direct testimony in this case?

A. Yes, I have two corrections. Please refer to page 5, Table 2 of my direct testimony. The contract capacity for the purchase from Associated Electric Cooperative, Inc. ("AECI") should be 190MW instead of 100MW.

On page 16, line 6 of my direct testimony, the statement, "a $1.00 change in gas prices has approximately a $7 million effect on total fuel costs" should read, "a $1.00 change in gas prices has approximately an $8.6 million effect on total fuel costs".

Q. What is the purpose of your rebuttal testimony?

A. The purpose of this testimony is to rebut the direct testimony in this case of Missouri Public Service Commission Staff ("Staff") and Sedalia Industrial Energy Association ("SIEUA") witnesses on the issues of the capacity purchase from Merchant Energy Partners – Pleasant Hill ("MEPPH"), off-system sales, and Jeffrey Shares.

Q. How is your rebuttal testimony organized?

A. My rebuttal testimony is organized as follows:

I. MEP Pleasant Hill Unit Participation Purchase

a. Cost Recovery Associated with the Current Contract

b. Capacity Purchase versus Ownership/Rate Basing

II. Off-System Sales

a. Margin Sharing

b. Jeffrey Shares

I. MEP Pleasant Hill Unit Participation Purchase

Q. What are the issues regarding the MEP Pleasant Hill Unit Participation Purchase ("MEPPH purchase")?

A. While Staff has yet to provide its recommended position on the rate treatment for the

MEPPH purchase, Staff witnesses Featherstone and Oligschlaeger have stated in their direct testimonies that Staff is considering cost recovery associated with the MEPPH purchase that is less than the expense that will be incurred by MPS. Specifically, Mr. Oligschlaeger suggested that demand charges should be reduced by a factor of 350/580 from what will be paid by MPS. Applying this factor to the contractually incurred demand charges would cause MPS to under-recover its costs by **_____**. Mr. Featherstone proposed that $.0253/kw-mo in demand charges be denied for recovery since it was the result of a cost overrun. This would result in MPS under-recovering its properly incurred costs by $106,260 (12 x 200,000 x $0.0253 plus 6 x 300,000 x $0.0253) per year.

In addition, Mr. Oligschlaeger testified that MPS should own and rate-base the Aries units, the source of the MEPPH purchase, rather than buy capacity under a purchase power agreement ("PPA").

Q. Do you intend to submit a complete response to Mr. Featherstone's and Mr. Oligschlaeger's testimonies at this time?

A. I will respond to some of their arguments, but because their testimonies are preliminary, by their own terms, I will reserve the ability to supplement this testimony and submit additional testimony at a later date, to respond to any additional arguments or final conclusions that Mr. Featherstone, Mr. Oligschlaeger or another Staff witness may decide to submit concerning MPS' purchase of power from MEPPH.

a. Cost Recovery Associated with the Current Contract

Q. How does Mr. Oligschlaeger propose to treat the costs of the transaction between MPS and MEPPH?

A. Starting on page 7 of his testimony, Mr. Oligschlaeger suggests that the appropriate policy for treating the costs resulting from a transaction between affiliates in which the regulated entity purchases goods and services from an unregulated entity should be valued at the "lower of the fully distributed cost or market price." Therefore, Mr. Oligschlaeger argues that the mere fact MPS purchased energy from MEPPH in the open marketplace, at a competitive price, is insufficient for purposes of demonstrating that the costs do not represent affiliate abuse.

Q. Why does Mr. Oligschlaeger advocate the "lower of the fully distributed cost or market price" theory?

A. Mr. Oligschlaeger suggests that this theory is appropriate to insure that the agreement between MEPPH and MPS does not take advantage of their affiliate relationship, thereby passing on additional costs to the consumer.

Q. What does he mean by "affiliate abuse"?

A. Mr. Oligschlaeger argues that MPS is not making decisions based on the best interests of the customers, but is rather focused on the best interests of Aquila, an affiliated entity.

Q. Do you agree with this conclusion?

A. No. First of all, the Missouri Commission did not adopt its affiliate rules until Feburary

2000, well after MPS had executed its contract to buy energy from MEPPH. Mr. Oligschlaeger carefully sidesteps alleging that MPS has violated the Commission's rules because, of course, it could not possibly have violated those rules. The rules post-date the MPS power purchase contract by many months. Second, there is nothing "abusive" about the power purchase contract itself. It contains market-based rates, and was entered into after a perfectly public bidding process. There is no rational reason for believing that the rates in the contract do not represent market-based rates.

Q. How do the rates in the contract compare to rates at which other unaffiliated parties were willing to sell power to MPS?

A. As Mr. Oligschlaeger himself recognizes, the rates offered by MEPPH were lower than the rates offered by other unaffiliated parties. In fact, Mr. Oligschlaeger also admits that Staff was informed about the MEPPH bid before MPS executed any contract to buy power from MEPPH. He states at page 8 of his testimony that, "Based upon that review, the Staff concluded that MEPPH's bid was a reasonable selection when compared to the other bids received." It is difficult to understand how Staff should be allowed to whipsaw MPS by first recognizing that a certain power purchase option is reasonable, but then when it is time for the rate case and a decision to include those costs in rates, for Staff to turn around and argue that the contract represents affiliate abuse and the costs of the contract should not be allowed. That sort of conduct by Staff represents pure gamesmanship.

Q. Why does Mr. Oligschlaeger conclude that the agreement between MPS and MEPPH takes

advantage of the MPS-Aquila relationship?

A. Throughout his testimony, Mr. Oligschlaeger suggests that by entering into an agreement in which an affiliated entity is connected, must result in affiliate abuse. This is wrong. A transaction that involves two entities that are affiliated is not automatically abusive. In the present case, MPS solicited competitive bids in 1998, resulting in an arm's length proposal from MEPPH.

Q. Do you agree with Mr. Oligshalaeger's proposal to reduce MPS' cost recovery of the demand charges associated with the MEPPH purchase by the factor 350/580?

A. No. Mr. Oligshalaeger justifies this reduction by claiming that MPS is only buying 350 "average" megawatts from the 580 MW Aries project, and as a result MPS should only be allowed to collect 350/580 of the charges. Under the terms of the agreement, MPS purchases 200 MW for twelve months of the year, and an additional 300 MW for the months of May through October. The price paid for the 200 MW is **_____**; the price paid for the 300 MW is **_____**.

Q. How was the pricing for the MEPPH purchased determined?

A. That two-tiered pricing structure was bid by MEPPH as a proposal in response to MPS' 1998 power supply RFP. That was a competitive bidding process involving the evaluation of eight proposals from eight entities. After a detailed review process, MEPPH was selected as the lowest cost bid.

Q. Was the Staff given the opportunity to review MPS' evaluation?

A. Yes. The evaluation process was presented by MPS to the Staff in conjunction with the Missouri Integrated Resource Planning process. The contract and the evaluation process were also reviewed by the Staff in conjunction with Case No. EM-99-369. The expenses to be incurred by MPS under the MEPPH purchase agreement are the expenses MPS is seeking to recover in its rates. These expenses are the result of the same contract that MPS requested the Commission approve in EM-99-369.

Q. Is this capacity purchase used and useful?

A. Yes. This capacity purchase is being used by MPS to serve its Missouri customers. In addition, both the Staff and MPS, in their fuel runs in this case, modeled the MEPPH purchase at 200 MW for all 12 months and an additional 300 MW for the months of May through October.

Q. Has the need and cost-effectiveness of this capacity been demonstrated in previous analyses?

A. Yes. The need for this capacity was demonstrated to the Staff in Integrated Resource Planning presentations and to the Commission in Case No. EM-99-369. In that case, both the Staff and Office of Public Counsel ("OPC") acknowledged in their recommendations to the Commission that the MEPPH capacity was the most cost effective supply option for MPS to meet its capacity and energy obligations. Both the Staff and OPC, in their fillings in EM-99-369, recommended the Commission authorize MPS to enter into the MEPPH PPA. Copies of the Staff and OPC filings in Case No.

EM-99-369 are attached to this testimony as Schedules SLF-1 and SLF-2. I have also attached a copy of the Commission's order in that case authorizing MPS to enter into the agreement with MEPPH. I show the Commission's order as my Schedule SLF-3.

Q. Do you believe it is inappropriate to deny the Company recovery on $0.0253/kw-mo in demand charges because of cost overruns in the construction of the Aries units?

A. Yes. The terms of the MEPPH PPA permitted MEPPH, in the event of cost overruns, to raise monthly demand charges, subject to a cap. The $0.0253/kw-mo is consistent with the contract. Again, the provisions in the contract permit passing through portions of overruns. These provisions are the same as were presented to the Staff and Commission in the previously mentioned IRP presentation and docket.

Q. Do you believe it is imprudent to have a provision in a contract allowing the seller to pass along cost overruns?

A. No, provided that the increased cost is capped at a level maintaining the competitiveness of the bid with respect to other competing alternatives. I reviewed MPS' evaluations associated with the MEPPH purchase, and determined that even with the additional capacity purchased demand charges resulting from the cost overruns, the MEPPH purchase is still the most cost-effective alternative.

b. Capacity Purchase versus Ownership/Rate-Basing

Q. Do you agree with Mr. Oligschlaeger's testimony that MPS owning and rate-basing the Aries plant is more cost effective for the ratepayers than MPS purchasing capacity from

the plant for the period June 2001 – May 2005?

A. No. While Mr. Oligschlaeger acknowledges correctly that the capacity purchased demand charges incurred by MPS under the terms of the PPA will result in overall less expense during that four years than rate basing the plant, he further testifies incorrectly that had the purchased power agreement been long term, rate-basing the unit would have resulted in less expense for the ratepayer than the long term agreement.

Q. Why do you say that Mr. Oligschlaeger is incorrect regarding rate-basing the unit?

A. Over a term longer than four years, MPS' resource needs are expected to change from what they are currently. While the addition of the 500 MW MEPPH purchase of natural gas-fired combined-cycle capacity to MPS' resources produces the lowest costs today and into 2005, it is not expected to beyond 2005. For the future beyond 2005, I expect a generation mix consisting of more coal-fired base-load capacity and less natural gas-fired intermediate capacity than what MPS has under the MEPPH purchase will produce the lowest overall resource costs. Had MPS owned and rate-based the Aries plant in 2001, it would have been committed to that level of natural gas-fired capacity for the life of the plant. At the end of the four-year PPA, MPS will be able to adjust its generation mix in 2005 to a more cost effective blend of base-load and intermediate capacity than it would have had if it rate-based the Aries plant in 2001.

Q. By recommending that the MEPPH unit be rate-based, has Mr. Oligschlaeger made an incorrect assumption regarding MPS' long-term resource needs?

A. The point is not so much that he has made an incorrect assumption, it's that he has speculated on MPS' long-term resource requirements when he doesn't have to. Rate-basing the unit commits MPS and its customers to an inflexible, long-term resource plan that may not be -- and in my opinion isn't -- the most cost-effective plan. Unlike rate-basing the unit, a purchase from MEPPH provides MPS the opportunity to reassess its 2005 and beyond resource needs and implement a plan responsive to those needs.

Q. Has Mr. Oligschlaeger made any other incorrect assumptions regarding the MEPPH purchase?

A. Yes. Mr. Oligschlaeger assumes that the MEPPH financing arrangements are abusive, when it is actually advantageous from a cost perspective for the MPS customers. By entering into these arrangements MEPPH is able to gain favorable tax treatment on the facility, thereby reducing the costs that would ultimately be passed to the consumer. In any event, the MEPPH 's financial arrangements cannot possibly represent affiliate abuse – there is no affiliate relationship between Cass County and MEPPH.

II. OFF-SYSTEM SALES

Q. What are the issues in this case associated with off-system sales?

A. The Company has identified two issues associated with the treatment of off-system sales in this case. The first has to do with the sharing of off-system sales margins. In its direct-filed case, MPS proposed to share the margins associated with off-system sales equally between the ratepayer and the Company. Staff and SIEUA in their direct

testimonies in this case recommended that all margins associated with off-system sales be imputed to cost-of-service; i.e., according to Staff and SIEUA, all benefit from off-system sales should go to the ratepayer and none to Company.

Q. What is the second off-system sales issue?

A. The second off-system sales issue is associated with Staff's treatment of Jeffrey Shares. Jeffrey Shares are an energy exchange at cost between MPS and WestPlains Energy – Kansas ("WPEK"). In other words, MPS sells energy at cost to WPEK and WPEK sells energy at cost to MPS. There is no margin or "profit" associated with these exchanges. However, Staff has treated the Jeffrey Shares exchange as a normal off-system sale and included assumed or hypothetical margins for the exchange.

Q. Have MPS and the Staff agreed to a true-up of off-system sales?

A. Yes. MPS and the Staff have agreed that the Commission should utilize for rate-making in this case the level of off-system sales expenses and revenues for the twelve months ending January 31, 2002. That would make off-system sales consistent with the other fuel and purchased power items in the true-up.

a. Margin Sharing

Q. Regarding the first of the off-system sales issues you identified, do you agree with Staff's position to include 100% of off-system sales in the revenue requirement?

A. No. In his direct testimony, Mr. Featherstone stated that the company benefits from off-system sales because of revenue growth and the increase in net margins from one rate

proceeding to the next. From 1996 to 1998, off-system sales did increase significantly from year to year. However, off-system sales have declined steadily since that time from $56 million in 1998 to $17 million in the year 2000. The projected revenue in 2001 is only $6 million. This decline in revenue is a regulatory-lag risk to the Company rather than a benefit. The Staff's approach to ratemaking on this topic, as advocated by Mr. Featherstone, would be a disincentive to the Company to enter into off-system sales transactions. By adopting the Company's proposal to share off-system sales between ratepayers and shareholders, the regulatory risk of declining sales is mitigated and the native load customers will still benefit.

b. Jeffrey Shares

Q. What are Jeffrey Shares?

A. The MPS and WPEK operating divisions of UtiliCorp are joint participants in the Jeffrey Energy Center ("JEC"), a three-unit, coal-fired generating station located northeast of Topeka, Kansas. MPS and WPEK each own or have rights to 178 MW of Jeffrey capacity. MPS and WPEK each have a transmission path on Western Resources' ("WR") transmission system from their respective systems to JEC, and as result have a transmission path to each other. Thus, in addition to providing MPS and WPEK access to JEC, the transmission path through WR can also be used to exchange energy between MPS and WPEK. The energy that is exchanged between MPS and WPEK using this transmission path is referred to as Jeffrey Shares.

Q. How does UtiliCorp account for the expense and revenue associated with Jeffrey Shares?

A. UtiliCorp treats Jeffrey Shares as an intra-company transfer with zero margin. That is, when WPEK transfers energy to MPS, the revenue shown on WPEK's books is the same as its expense in providing the energy. Likewise, the purchase price shown on MPS' books is the same as WPEK's cost; and vice versa.

Q. Is the energy associated with Jeffrey Shares being provided from JEC?

A. No. Jeffrey Shares are off-system sales at zero margin from MPS to WPEK or WPEK to MPS that utilize the JEC transmission path. For example, let's say that MPS has a need for 50 MW of energy. The 50 MW of energy can be provided by increasing MPS generation or increasing MPS purchases, whichever is most cost-effective. If WPEK has energy surplus to its native load requirements that is more cost effective than MPS' generation or other purchase options, then UCU dispatchers transfer the energy from WPEK to MPS across the JEC transmission path. The price MPS pays for the energy is equal to WPEK's cost.

Q. Does JEC generation output change as a result of a Jeffrey Share exchange?

A. No. JEC generation, because of its relative low cost, is normally fully utilized within the MPS and WPEK systems to meet native load requirements. However, on the JEC station books, deliveries of JEC generation to MPS or WPEK are adjusted corresponding to the amount of Jeffrey Shares exchange. For the previously mentioned 50 MW example, WR would increase JEC delivery to MPS by 50 MW and reduce delivery to WPEK by 50

MW. WPEK would either increase its other generation or purchases by 50 MW to replace the 50 MW of JEC generation. The cost WPEK charges to MPS for the 50 MW would be equal to the cost WPEK incurs for increasing its other generation or purchasing the energy.

Q. For the 50 MW example just cited, do WPEK's net costs increase as a result of this exchange?

A. No. The net costs associated with serving WPEK's native load remain unchanged. WPEK sends 50MW of energy to MPS at a cost equal to WPEK's cost to procure the additional 50 MW. The 50 MW that WPEK generated from other generation or purchased is received into its system, but WPEK only pays JEC station's cost to generate the 50 MW.

Q. Do Jeffrey Shares benefit MPS and WPEK retail customers?

A. Yes. Since Jeffrey Shares are provided at cost, both MPS and WPEK customers are able to receive energy at cost, and therefore avoid paying margin on the exchange.

Q. Have you reviewed Staff's work papers regarding pricing of Jeffrey Shares?

A. Yes.

Q. Do you agree with Staff's proposed adjustment?

A. No. The Staff's adjustment recalculates the price that MPS charged to WPEK for inter-company exchanges that were made utilizing the JEC transmission path. When MPS sells to WPEK via the JEC path, the inter-company revenue is recorded based upon the

average purchased power price that MPS incurred to replace the energy that was redirected to WPEK. Staff's work paper is proposing that the cost be revised to $13.68/MWH. Staff contends part of the sales were sourced from JEC at $11.61/MWH and the remaining portion were sourced at a market price of $14.60/MWH. If these costs are used to source the sales, then a corresponding revenue adjustment must be made to reflect this weighted average cost as the inter-company revenue.

Q. Why is it necessary to make this revenue adjustment?

A. Since there is no margin associated with Jeffrey Shares transactions, an adjustment is necessary to match the revenues with the expenses.

Q. What is your recommended adjustment to revenues?

A. The recommended adjustment is to reduce off-system sales revenues by $2,694,945.

Q. How was this adjustment calculated?

A. By multiplying the difference between the actual price per MWH that MPS charged WPEK of $30.79/MWH and Staff's weighted average cost of $13.68/MWH times the Jeffrey Shares volumes of 157,507 MWH.

Q. If the margin associated with Jeffrey Shares is zero, does it make any difference what price is established for Jeffrey Shares?

A. Provided that the revenues for Jeffrey Shares in this case are adjusted to equal the cost, it doesn't make any difference what the cost is. Therefore, regardless of what price Staff would set as the cost associated with providing Jeffrey Shares, I recommend that the

revenues in this case be adjusted to equal those costs.

Summary

Q. Please summarize your recommendations regarding the MEPPH Pleasant Hill Unit Participation Purchase.

A. The MEPPH purchase is the most cost effective alternative to meet MPS' increasing capacity and energy requirements for the period 2001 – 2005. Staff's contention that the Aries unit, the source of the MEPPH purchase, should have been owned and rate-based by MPS ignores MPS' resource requirements for the future following 2005. The MEPPH purchase contract was entered into as the result of a competitive bidding process that was reviewed by the Staff and OPC and approved by the Commission in Case No. EM-99-369. The annual capacity purchase demand charges associated with the MEPPH purchase agreement are **_____**, and should be included in cost of service.

Q. Please summarize your recommendations regarding off-system sales.

A. Regarding margin sharing, the Company believes that sharing the margins associated with off-system sales between the ratepayer and the Company, rather than imputing all margins to the ratepayer, provides an incentive to the Company to be more aggressive in pursuing off-system sales, and ultimately will benefit the customer. Staff's contention that regulatory lag alone provides this incentive is untrue, especially in a declining wholesale market.

Jeffrey Shares are an intra-company exchange of energy at cost between MPS and

WPEK. Because these transactions occur at cost, they reduce overall expense and benefit Missouri ratepayers. There is no margin or "profit" on these exchanges. As a result, revenues associated with Jeffrey Shares in the Staff's case showed be decreased by $2,694,945 to match the Jeffrey Shares expense in Staff's case.

Q. Does this conclude your testimony at this time?

A. Yes.

MEMORANDUM

TO: Missouri Public Service Commission Official Case File
Case No. EM-99-369

FROM: Mark L. Oligschlaeger (in LD)
Regulatory Auditor V

Steven Dottheim SD
Chief Deputy General Counsel

4/5/99
Utility Services Division/Date

4/5/99
General Counsel's Office/Date

SUBJECT: Staff's Recommendation For Approval Of The Application Of UtiliCorp United, Inc. Under §32(k) Of The Public Utilities Holding Company Act Of 1935 Concerning A Proposed Power Sales Agreement Between MEP Pleasant Hill, L.L.C. And UtiliCorp United, Inc., d/b/a Missouri Public Service

DATE: April 5, 1999

I. INTRODUCTION

On March 1, 1999, UtiliCorp United, Inc. (UtiliCorp), d/b/a Missouri Public Service (MPS) filed an Application with the Missouri Public Service Commission (Commission) for an Order no later than May 1, 1999 that:

> (A) determines specifically that, in order to protect against abusive affiliate transactions, the Commission has sufficient regulatory authority, resources and access to books and records of UtiliCorp and Merchant Energy Partners Pleasant Hill, L.L.C. (MEPPH)[1] to exercise its duties under §32(k) of the Public Utility Holding Company Act of 1935 (PUHCA)[2] to ensure that a Power Sale Agreement (PSA) between UtiliCorp and MEPPH :
>
> (1) benefits consumers;

[1] UtiliCorp caused MEPPH to be established to engage in merchant energy activities, including the purchase and sale of power and construction of power plants. MEPPH will construct a 500 MW combined cycle combustion turbine generation plant in Cass County, Missouri near the town of Pleasant Hill, which plant will be operated by MEPPH in order to meet its contractual obligations under the PSA. UtiliCorp states in its Application that MEPPH (a) is not and will not be an "electrical corporation" in that it will sell electric power exclusively at wholesale, and, therefore, will not be engaged in the sale of electric power at retail to the general public, and (b) will be regulated by the Federal Energy Regulatory Commission (FERC) with respect to wholesale energy rates.

[2] Section 32(k) of PUHCA, 15 U.S.C. Section 79z-5a(k), is Section 711 of the Energy Policy Act of 1992.

(2) does not violate any state law;

(3) does not provide MEPPH with any unfair competitive advantage by virtue of its affiliation with UtiliCorp; and

(4) is in the public interest;

(B) authorizes UtiliCorp to enter into, execute and perform in accordance with the terms and conditions of the proposed PSA by and between UtiliCorp and MEPPH;

(C) authorizes UtiliCorp to enter into, execute and perform in accordance with the terms of all documents reasonably necessary and incidental to the performance of the transactions which are the subject of the Application; and

(D) grants such other authority as may be just and proper under the circumstances.

UtiliCorp seeks an Order by May 1, 1999 approving its Application because it asserts it is "imperative that MEPPH commence by the end of July of 1999 with the construction of the involved combustion turbine generation plant" so as to have in place the necessary capacity by 2001. MEPPH states that once it has obtained this Commission's approval, MEPPH will file with the FERC a request for certification as an exempt wholesale generator (EWG) and a request for approval of the PSA under the applicable provisions of PUHCA and the Federal Power Act (FPA).

Concurrent with the filing of this recommendation, the Staff is filing the recommendation of the Commission's Chief Energy Economist, Dr. Michael S. Proctor, who recommends that the Commission grant UtiliCorp the approvals requested in its March 1, 1999 Application in the instant docket, with conditions. The purpose of this document is to provide support for Dr. Proctor's recommendation and suggest additional conditions for the granting of the requested approvals.

II. STATE COMMISSIONS WHICH HAVE CONDITIONED PUHCA §32 FINDINGS

The Staff would not expect UtiliCorp's Application to cite to case law for authority for the Commission to grant the approvals requested by UtiliCorp with the conditions proposed by the Staff, but the Staff would note that the Application of UtiliCorp cites to no case law for anything other than one Missouri case respecting the determination of what constitutes a public utility. See UtiliCorp's Application at page 4, paragraph 9, citation to State ex rel. M.O. Danciger & Co. v. Public Serv. Comm'n, 205 S.W. 42 (Mo. 1918).

There is at least one state commission case on point and another related, both of which will be addressed herein regarding a state conditioning its granting of PUHCA §32 findings: Re Golden Spread Electric Cooperative, Inc., Docket No. 15100, Order, 176 PUR4th 587 (Tx.Pub.Util.Commn. 1997) and Re New England Power Co., DR 97-251, Order No. 22,982 (N.H.Pub.Util.Commn. 1998)(unreported decision).

In the Golden Spread Electric Cooperative case, Golden Spread Electric Cooperative, Inc. (Golden) filed in 1995 an application with the Texas Public Utility Commission (Texas PUC) seeking, among other things, the PUHCA §32(k) findings that were required in order for Golden to enter into a purchased power contract with an EWG that is an affiliate of Golden. The Golden contract with the EWG has a term of 25 years. The Texas PUC made the necessary PUHCA §32(k) findings, but conditioned the findings as they might be proposed to be related to stranded cost recovery and future purchased power contracts stating that its approval of the contract in question may not be relied upon as a basis for stranded cost recovery nor does approval imply or assure blanket approval of future purchased power costs. 176 PUR4th at 588. In particular regarding stranded cost recovery, the Commission found as follows:

> . . . the Commission finds that there is a risk of regulatory change during the life of the proposed power contracts. Consequently, Golden Spread Electric Cooperative, Inc. (Golden Spread or the Cooperative) may not rely on this Order as a basis for stranded cost recovery if and when such recovery becomes appropriate. . . . [Id.]

In the New England Power Co. case, New England Power Co. (NEP) requested that the New Hampshire Public Utilities Commission (New Hampshire PUC) authorize it to transfer its New Hampshire hydroelectric facilities, located in whole or in part in New Hampshire, to USGen New England, Inc. (USGenNE), in a proposed transaction in which NEP agreed to sell substantially all of its non-nuclear generating assets and unit entitlements. NEP is a Massachusetts corporation and a wholly owned subsidiary of the New England Electric System (NEES). It owns and operates generation and transmission facilities throughout Northern New England. NEP provides wholesale requirements service to affiliated retail electric utilities, including to Granite State Electric Company (GSEC) in New Hampshire. NEP sought certain "eligible facilities", i.e., EWG, findings from the New Hampshire PUC pursuant to PUHCA §32(c) to enable USGenNE to acquire NEP's generating assets without becoming subject to PUHCA. NEP stated that USGenNE made the receipt of EWG status a condition to the closing of the divestiture transaction.

PUHCA § 32(c) provides, in part, that if a rate or charge for electric energy produced by a facility was in effect under the laws of any state as of October 24, 1992, in order for the facility to be considered an eligible facility, every state commission having jurisdiction over any such rate or charge must make a specific determination that allowing such facility to be an eligible facility:

(1) will benefit consumers;

(2) is in the public interest; and

(3) does not violate state law.

PUHCA §32(c) also addresses the case where such rate or charge is a rate or charge of an affiliate of a registered holding company.

The New Hampshire PUC granted NEP's request for these findings relative to those facilities which NEP was transferring to USGenNE pursuant to the proposed divestiture transaction. The New Hampshire PUC premised its PUHCA §32 findings on the condition that USGenNE would agree to provide GSEC "transition service" consistent with the outcome of Docket No. DR 98 – 012. (Said docket was created to consider a settlement proposal relative to GSEC's compliance with the electric utility restructuring chapter of New Hampshire statutes.) Transition service was intended to (1) be a generation option for customers who did not choose to take generation service from a competitive provider and (2) provide GSEC's customers with stable prices as the competitive electric market developed. The New Hampshire PUC stated that by approving the NEP – USGenNE transaction, it was not implying that a similar approach should be adopted in the case of any other utility.

III. STAFF'S PROPOSED CONDITIONS

PUHCA §32(k) states in part that an electric utility company may enter into a contract to purchase electric energy at wholesale from an exempt wholesale generator (EWG) that is an affiliate or associate company if every state commission having jurisdiction over the retail rates of such electric utility company determines in advance of the electric utility company entering into such contract "that such commission has sufficient regulatory authority, resources and access to books and records of the electric utility company and any relevant associate, affiliate or subsidiary company to exercise its duties under this subparagraph." (Emphasis supplied). Thus, the Staff believes that two conditions that should be placed upon the Commission's approval of

UtiliCorp's Application so that the Commission will not be frustrated in carrying out its statutory duties should be the following:

(1) UtiliCorp shall agree to make available to the Commission and its Staff, at reasonable times and reasonable places, all books and records and employees and officers of MEPPH and any affiliate or subsidiary of UtiliCorp engaged in any activity with MEPPH.

(2) MEPPH shall agree to employ accounting and other procedures and controls related to cost allocations and transfer pricing to ensure and facilitate full review by the Commission and its Staff and to protect against cross-subsidization of non-MPS businesses by MPS customers.

FERC has jurisdiction over wholesale electric energy transactions. A state commission must allow, as reasonable operating expenses, costs incurred by a utility as a result of paying a FERC-determined wholesale rate. Nantahala Power and Light Co. v. Thornburg, 476 U.S. 953 (1986). FERC approval of an energy supplier's rate does not necessarily mean it was reasonable for the purchaser to incur the expense. A state commission can challenge the prudence of a utility's decision to purchase power at a FERC-approved rate under what has become known as the Pike County doctrine. Pike County Light and Power Co. v. Pennsylvania Pub. Util. Commn, 465 A.2d 735 (Pa. 1983). The Staff also would note that a state commission must defer to certain FERC approved allocations contained in operating or system agreements among affiliates of a registered holding company. Mississippi Power & Light Co. v. Mississippi ex rel. Moore, 487 U.S. 354 (1988).

UtiliCorp in its Application in the instant proceeding recognizes and accepts the Commission's historical approach of not granting pre-approval of electric resource additions, wherein UtiliCorp states, at paragraph 15 of its Application, as follows:

> UtiliCorp understands that an order containing the findings required by the PUHCA with respect to the PSA shall in no way be binding on the Commission

> or any party to a future rate case to contest the ratemaking treatment to be afforded the PSA.

Nonetheless, there is more than pre-approval that is occurring with UtiliCorp's proposed transaction.

As a result of the Nantahala Power and Light Co. and Mississippi Power & Light Co. cases, the Staff believes that Commission use of the language contained in paragraph 15 of UtiliCorp's Application is not an adequate condition to the Commission making the PUHCA §32(k) findings. The Staff believes that the following additional condition should be placed upon the Commission's approval of UtiliCorp's Application for an Order respecting the PSA between UtiliCorp and MEPPH. The Commission's approval of UtiliCorp's Application should be contingent upon the following occurring:

> (3) UtiliCorp shall agree that an order containing the findings required by the PUHCA with respect to the PSA shall in no way be binding on the Commission or any party to a future rate or earnings complaint case to contest the ratemaking treatment to be afforded the PSA. UtiliCorp shall agree that it will not seek to overturn, reverse, set aside, change or enjoin, whether through appeal or the initiation or maintenance of any action in any forum, a decision or order of the Commission which pertains to recovery, disallowance, deferral or ratemaking treatment of any expense, charge, cost or allocation incurred or accrued by MEPPH or MPS in or as a result of the PSA on the basis that such expense, charge, cost or allocation has itself been filed with or approved by the FERC, or was incurred, pursuant to the PSA.

Finally, the Staff would recommend that the Commission adopt the following condition in order that Commission approval of the instant Application, should that occur, not be used as authority for the approval of any subsequent PUHCA §32(k) application:

(4) The Commission's approval of the instant PSA does not imply or assure approval of any future contracts to purchase electric energy at wholesale from an EWG that is an affiliate or associate company of an electrical corporation within the Commission's jurisdiction.

Copies:

Bob Schallenberg, Director of Utility Services, Missouri Public Service Commission
Gordon Persinger, Director of Research & Public Affairs, Missouri Public Service Commission
Dan Joyce, General Counsel, Missouri Public Service Commission
Bill Washburn, Manager Electric Department, Missouri Public Service Commission
Gary Clemens, Manager Regulatory Services, UtiliCorp United, Inc.
James C. Swearengen, Brydon, Swearengen & England, P.C.
Paul A. Boudreau, Brydon, Swearengen & England, P.C.
John B. Coffman, Office of the Public Counsel

MEMORANDUM

TO: Missouri Public Service Commission Official Case File
Case No. EM-99-369

FROM: Michael S. Proctor
Chief Regulatory Economist

Director-Utility Operations Division/Date — General Counsel's Office/Date

SUBJECT: Staff's Recommendation For Approval Of The Application Of UtiliCorp United, Inc. Under §32(k) Of The Public Utilities Holding Company Act Of 1935 Concerning A Proposed Power Sales Agreement Between MEP Pleasant Hill, L.L.C. And UtiliCorp United, Inc., d/b/a Missouri Public Service

DATE: April 5, 1999

Missouri Public Service Commission Determinations under §32(k) of PUHCA

In order for Missouri Public Service (MPS), a division of UtiliCorp United, Inc. (UtiliCorp) to enter into a Power Sales Agreement (PSA) with Merchant Energy Partners Pleasant Hill, L.L.C. (MEPPH), a subsidiary of UtiliCorp, subsection 32(k) of the Public Utility Holding Company Act (PUHCA) of 1935 requires the Missouri Public Service Commission (Commission) to make the following determinations regarding the PSA:

1. it will benefit consumers;
2. it does not violate any state law;
3. it would not provide MEPPH any unfair competitive advantage by virtue of its affiliation or association with UtiliCorp; and
4. it is in the public interest.

The Commission must also make a determination that it has sufficient regulatory, resources and access to books and records of UtiliCorp and any relevant associate, affiliate or subsidiary company to exercise its duties under subparagraph 32(k)(2) of PUHCA. UtiliCorp in its Application at page 5, paragraph 11 states that:

> . . . The Commission's existing rules and regulations permit it to examine the books and records of UtiliCorp. Furthermore, the Commission, its Staff and the Office of the Public Counsel may examine the books, accounts, contracts and records of MEPPH as required for the effective discharge of the Commission's regulatory responsibilities affecting the provision of electric service by MPS."

In this memorandum and the accompanying memorandum of Staff members Mark Oligschlaeger and Steve Dottheim, it will be shown that the PSA, subject to the review and ratemaking conditions proposed by the Staff, meets all four of the subsection 32(k) PUHCA standards.

1. **The PSA will benefit consumers**

The capacity from PSA between MPS and MEPPH is required to meet the capacity reliability needs of MPS customers and is therefore of benefit to consumers. What follows is a description of the process by which the Staff has determined that there is a capacity need which the PSA will meet to the benefit of consumers.

The Staff has met with MPS on a regular basis following UtiliCorp's initial resource plan filing[1] required by 4 CSR 240-Chapter 22. In these meetings, MPS has provided Staff with updates on load forecasts as well as other changes that have occurred in its resource acquisition plans. In its resource plan filing, MPS stated its intention to implement a competitive bidding process to acquire the capacity needed to meet the requirements of its customers for capacity and energy. This need comes from two sources: (1) load growth in the MPS service territory; and (2) expiration of existing purchased power contracts. Most of the changes in UtiliCorp's resource acquisition strategy have come in the timing of resource additions.

[1] In its 1995 Missouri Energy Plan filed in May 1995 in Case No. EO-95-187, UtiliCorp included supply-side options for 206 megawatts (MW) in combined cycle capacity for the summers of 2000 and 2001. The supply-side implementation plan strategy included a competitive-bidding process that was to be completed in 1997.

For the summer of 1999, MPS has accredited generation capacity of 1,047 MW with 280 MW of purchased power from existing purchased power contracts to meet a total capacity requirement[2] of 1,366 MW. Not directly related to this pleading, MPS is evaluating bids for purchased power of 50 MW to meet its capacity requirement for this summer. The contracts making up the 280 MW of purchase power will expire and not be available to meet load for the summer of 2000. Thus, there is clearly a need for either purchased power or MPS owned capacity starting with the summer of 2000.

It is important to note that the MPS purchase power acquisition strategy was split between meeting a short-term need and a long-term need. For the short-term (prior to the summer of 2001), MPS planned to enter into one- or two-year contracts for purchased power. Starting for the year 2001, MPS would seek longer-term contracts. In part, the rationale behind this strategy is that the short-term contracts would have to come from generating units that were already built, while the longer-term contracts would allow bids from new generating units that would not be available to supply power in the short-run.[3] The PSA between MPS and MEPPH is for a longer-term contract.

In the year 2001, MPS plans to improve the accredited capacity of its existing generating units from 1,047 MW to 1,085 MW. MPS plans to have a short-term purchase of 25 MW and begin the first year of its long-term contract with MEPPH with 320 MW of combustion turbine capacity. This provides a total capacity of 1,430 MW to meet a capacity requirement of 1,430. In the year 2002, the short-term purchased power contracts are terminated and the long-term

[2] The capacity requirement is the peak demand forecast, minus demand-side reductions such as interruptible load, plus a capacity reserve margin of 12 percent.

[3] How this strategy evolved is described in the third section of this memorandum.

contract with MEPPH goes up to 500 MW as MEPPH adds 180 MW of combined cycle capacity to the 320 MW of combustion turbines.

2. The PSA does not violate any applicable state law

Staff counsel has advised that state law does not prohibit any utility from purchasing power rather than building generation. In addition, Staff counsel has indicated that there is no state law that prohibits any electric utility from purchasing power from an affiliate.

3. The PSA did not provide MEPPH any unfair competitive advantage by virtue of its affiliation with UtiliCorp

As described below, the competitive bidding strategy employed by MPS involves a complex process that would more properly be described as a competitive negotiation. In addition, this process was flexible; allowing MPS to change its strategy as information became available. The Staff's limited observation/review of that process found no evidence to indicate that an unfair competitive advantage was afforded MEPPH.

As MPS developed its resource acquisition strategy for purchased power, the Staff made it clear that if an affiliate of UtiliCorp were to bid, that affiliate would need to be on a level playing field with all other potential bidders. This means no communications regarding the competitive bid between people representing the interests of MPS and those representing the interests of the affiliate, except through the formal competitive bidding/negotiation process. It also means that the affiliate would have to bid at the same time as others and that a transparent evaluation of the bids would need to take place.

The history of the competitive bidding/negotiation process for the long-term purchased power contract is as follows:

(1) Initial Request for Proposals was issued by MPS on May 22, 1998. At this time, MPS wanted capacity to be supplied beginning June 1, 2000 and go through May 31, 2004; i.e., a four-year contract, with capacity initially available for the summer of 2000.

(2) Eight proposals were received on July 3, 1998. The eight proposals were opened on July 6, 1998. One of the eight proposals was from Aquila Power Corporation (Aquila), a power-marketing subsidiary of UtiliCorp. Both Aquila and UtiliCorp/MPS have their principal offices and places of business at 10750 East 350 Highway, Kansas City, Missouri 64138. An outside consultant, Burns & McDonnell, a Kansas City engineering and consulting firm, reviewed all proposals. Initial evaluation of the proposals was completed on August 21, 1998 by Burns & McDonnell. On August 25, 1998, all bidders were requested to confirm their interest and update their proposals. All but three of the bidders (New Century Energies, Aquila and Basin Electric Cooperative) stated that they would not be able to provide capacity in time for the summer of 2000. From the three that could meet the summer 2000 requirement, the Basin Electric Cooperative bid was determined to not be cost effective because of its high capacity charge. In addition, UtiliCorp was in the process of negotiating purchased power for its West Plain's service territory in Kansas, for which it had received a bid from Sunflower Electric Cooperative (Sunflower) that included capacity that would be available for the June 2000 to May 2001 period. MPS made the decision to split its purchases between short-term capacity and long-term capacity, with the three bidders that could meet the short-term need (Aquila, New Century Energies and Sunflower) being included in the evaluation process for the short-term purchase power contracts.

(a) At this time, UtiliCorp concluded that it could build a generation plant at a lower cost than what it had received in bids from those who were proposing to supply from newly built generation. UtiliCorp was seriously considering building its own generation to meet the MPS long-term capacity need and in September 1998 formed MEPPH as a subsidiary to develop, own and manage UtiliCorp's portfolio of exempt wholesale generators (EWG), independent power producers (IPP) and cogeneration facilities and to possibly build and own generation for Missouri retail jurisdictional needs as an EWG. However, this capacity would not be available for the summer of 2000 and perhaps not even for the summer of 2001. The EWG option under consideration by MPS and the Aquila proposal for June 2001 through May 2004 were assigned to MEPPH.

(b) By November 3, 1998, the evaluation of the three short-term bids was completed with MPS determining that a combination of Sunflower and Aquila resources was the most cost effective.

(3) On November 6, 1998, MPS requested that bidders again confirm their interest and update their proposals that would begin supply in the summer of 2001. On November 30, 1998, only two of the eight companies submitted revised bids: Aquila Power/MEPPH and Houston Industries for the June 2001 through May 2006 period. These bids were evaluated by MPS as well as by its outside consultant, Burns & McDonnell. It was determined that the Houston Industries bid was not competitive. MPS contacted Houston Industries on December 21, 1998 to advise it that its bid was not cost effective and requested that it consider revising its

proposal. Houston Industries revised its proposal on January 6, 1999, and MPS received confirmation that MEPPH would replace Aquila as the owner of the proposed EWG and would be the entity contracting with MPS. MEPPH revised its proposal on January 12, 1999. It appears that in the evaluation/negotiation process, Houston Industries was given the first opportunity to revise its bid, and then MEPPH was given an opportunity to respond. The rational for this sequence is that the bidder with the non-competitive bid is allowed the first opportunity to make its bid competitive. After receiving the January 12, 1999 revision from MEPPH, MPS informed Houston Industries on January 13, 1999 that its revised bid was not competitive. On January 14, 1999, Houston Industries responded that it was not able to improve its offer. On January 15, 1999, Houston Industries was advised that it was not the successful bidder, and MPS awarded the contract to MEPPH, subject to further negotiations on final terms and conditions.

4. <u>The PSA is in the public interest</u>

The public interest is met when electricity is provided to end-use consumers at the lowest expected cost consistent with reasonable levels of risk associated with cost varying from its expected level. In today's environment of competitive wholesale power, properly implemented competitive bidding and/or negotiation for purchased power is a process by which least-cost acquisition of resources can be obtained. Based on the information presently available, the competitive bidding/negotiation process used by MPS appears to be consistent with obtaining the needed purchased power at least cost. Therefore, the Staff is willing to state that the PSA between MPS and MEPPH is in the public interest, subject to the conditions and ratemaking

standards discussed below and in the accompanying recommendation, which will permit a detailed review of the transaction in the context of a rate increase or earnings complaint case.

It is important to note that the Staff has not evaluated the two proposals to determine which is least cost or whether accepting either of the two proposals would be a prudent management decision. Moreover, this Commission does not pre-approve the acquisition of resources by electric utilities. Instead, in its 1993 rulemaking on electric resource acquisition (4 CSR 240-Chapter 22), this Commission enacted rules that focused on the process, not the outcome. At the time these rules were adopted by the Commission, the Federal Energy Regulatory Commission (FERC) had not issued Order No. 888, which is premised on open transmission access on a non-discriminatory basis as being a means of fostering a competitive wholesale market for electricity. Thus, the Chapter 22 rules do not include any specific guidelines for competitive bidding or negotiations.

Since the Commission's adoption of 4 CSR 240-Chapter 22, there has been only one case in which the Commission was asked to evaluate whether or not the resource chosen by an electric utility was least cost prior to introducing the costs associated with the resource into rates.[6] This request that the Commission evaluate whether a resource chosen is least cost occurred because one of the options that was rejected by the utility was a cogenerator, and under the Public Utility Regulatory Policies Act of 1978 (PURPA), utilities are required to purchase from cogenerators that are competitive under an avoided cost criteria. Neither Houston Industries nor MEPPH are claiming to be a cogeneration facility. It is important to note that a review of the testimony submitted in that case indicates that a significant amount of analysis is required to determine which alternative is least cost.

[6] Alstrom Development Corporation vs. Empire District Electric Company, Case No. EC-95-28, Report And Order, 4 Mo.P.S.C.3d 187 (1995).

At this time, the Staff has not performed a detailed analysis of which of the two alternatives is least cost. Such an analysis should be done prior to the Commission approving the costs of the PSA in rates for Missouri Public Service customers. Subject to this condition, it is not necessary that this analysis be conducted at this time in order to determine whether or not the PSA is in the public interest. Moreover, to make such a determination at this time would put the Commission in the position of pre-approval of the prudency of MPS entering into the PSA, which is an approach that the Commission uniformly has rejected over many years. UtiliCorp in its Application recognizes and accepts the Commission's historical approach, wherein at paragraph 15, UtiliCorp states as follows:

> UtiliCorp understands that an order containing the findings required by the PUHCA with respect to the PSA shall in no way be binding on the Commission or any party to a future rate case to contest the ratemaking treatment to be afforded the PSA.

UtiliCorp also notes in its Application that:

(1) a copy of the RFP was forwarded to the Staff and the Office of the Public Counsel (Public Counsel) on August 24, 1998 for comment under the integrated resource plan format (page 3, paragraph 5 of Application);

(2) the eight (8) proposals received in response to the RFP were forwarded to the Staff and Public Counsel on August 24, 1998 under the integrated resource plan format (page 3, paragraph 6 of Application); and

(3) the reviews and evaluations of the proposals were provided to the Staff and Public Counsel on February 8, 1998 (page 3, paragraph 6 of Application).

As previously commented upon above, the 4 CSR 240-Chapter 22 rules focus on process, not outcome, and the review under these rules is not intended to have the Commission and its Staff engage in a contemporaneous evaluation with the utility of the proposals solicited to determine which is least cost or whether accepting any one of them would be a prudent management decision. Although the Commission generally has or can acquire sufficient regulatory resources

to exercise its ratemaking duties when a utility seeks to reflect a resource decision in rates, the Staff does not want its position to be misinterpreted as indicating or implying that the Commission also has sufficient regulatory resources to exercise its ratemaking duties if utilities were to also seek pre-approval of their resource decisions.

The timing of the instant project to meet the June 1, 2001 on-line date is crucial. A determination of which of the options is least cost would involve a Staff analysis that at best could take several weeks, but more likely would take several months, to complete. If the results of the analysis were not in favor of approval of the PSA with MEPPH, written testimony and hearings would need to take place. All of this would put off the time at which MEPPH would initiate the building of the generating units required to meet the June 1, 2001 deadline for capacity.

The Staff believes that what is needed to determine that the PSA is in the public interest is a review of the process followed by MPS in acquiring the needed capacity. In the context of its ongoing efforts in reviewing the resource plans of MPS, the Staff believes that the process followed by MPS is adequate to meet the public interest standard, subject to the review and ratemaking conditions set out above and the accompanying Staff recommendation of Staff members Mark Oligschlaeger and Steve Dottheim.

Copies:
Bob Shallenberg, Director of Utility Services, Missouri Public Service Commission
Gordon Persinger, Director of Research & Public Affairs, Missouri Public Service Commission
Dan Joyce, General Counsel, Missouri Public Service Commission
Bill Washburn, Manager Electric Department, Missouri Public Service Commission
Gary Clemens, Manager Regulatory Services, UtiliCorp United Inc.
James C. Swearengen, Brydon, Swearengen & England P.C.
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April 5, 1999

Mr. Dale Hardy Roberts
Secretary/Chief Regulatory Law Judge
Missouri Public Service Commission
P. O. Box 360
Jefferson City, MO 65102

RE: UtiliCorp United, Inc. d/b/a Missouri Public Service
Case No.: EM-99-369

Dear Mr. Roberts:

Enclosed for filing in the above referenced case, please find the original and 14 copies of the **Public Counsel Recommendation.** Please "file stamp" the extra enclosed copy and return it to this office. I have on this date mailed, faxed, or hand-delivered the appropriate number of copies to all counsel of record.

Thank you for your attention to this matter.

Sincerely,

John B. Coffman
Deputy Public Counsel

JBC:rjr

cc: Counsel of Record

Enclosure

BEFORE THE PUBLIC SERVICE COMMISSION OF THE STATE OF MISSOURI

In the Matter of the Application of UtiliCorp United, Inc. under Section 32(k) of the Public Utilities Holding Company Act of 1935 Concerning a Proposed Power Sales Agreement Between MEP Pleasant Hill, L.L.C. and UtiliCorp United Inc. d/b/a Missouri Public Service.	)))))))	**Case No. EM-99-369**

PUBLIC COUNSEL RECOMMENDATION

COMES NOW the Office of the Public Counsel ("Public Counsel") and for its recommendation states as follows:

1. On March 1, 1999, UtiliCorp United, Inc. d/b/a Missouri Public Service ("Company") filed an Application requesting that the Public Service Commission ("Commission") make specific determinations regarding a proposed Power Sales Agreement ("PSA"). These determinations that are a prerequisite to approval of the PSA by the Federal Energy Regulatory Commission ("FERC"). Federal law ("PUHCA") requires these determinations be made by a state commission whenever an electric utility proposes a PSA with an affiliated exempt wholesale generator ("EWG"). Company is proposing a Power Sales Agreement ("PSA") between it and its affiliate MEP Pleasant Hill, L.L.C. ("MEPPH"). On March 5, 1999, the Commission requested recommendations regarding the approval or rejection of UtiliCorp's Aplication by April 5, 1999.

2. Company is accordingly requesting that the Commission specifically determine that it has sufficient regulatory authority:

> ...the Commission has sufficient regulatory authority, resources and access to books and records of UtiliCorp and MEPPH to exercise its duties under section 32(k) of PUHCA to ensure that the proposed PSA (i) benefits consumers, (ii) does not violate any state law, (iii) does not provide MEEPPH with any unfair competitive advantage by virtue of its affiliation with UtiliCorp and (iv) is in the public interest; (B) authorizing UtiliCorp to enter into, execute and perform in accordance with the terms and conditions of the proposed Power Service Agreement by and between MEPPH and UtiliCorp; (C) authorizing UtiliCorp to enter into, execute and perform in accordance with the terms of all documents reasonably necessary and incidental to the performance of the transactions which are the subject of this Application; and (D) granting such other authority as may be just and proper under the circumstances. (Application, pp. 6-7).

3. Public Counsel recommends that the Commission make these requested determinations only upon certain conditions. The fact that Company is proposing a PSA with an affiliate (MEPPH) raises concerns that it may not be in the public interest. Public Counsel believes that the Commission should ensure that the cost advantage purported to be gained from this transaction is not outweighed by the potential negative impacts to Company's captive ratepayers. It is not as simple to monitor and determine the impact on the public from such an affiliate transaction as it is when the transaction occurs between entities that are wholly separate. The monitoring of yet another affiliate transaction will require the expenditure of additional regulatory resources.

4. Public Counsel is also concerned about the potential detrimental effects on wholesale and retail markets in Company's region. Such detrimental effects could develop as a result of an over-concentration of the ownership of generation facilities. As market power is

accumulated under one parent company, the potential harm to consumers in a future competitive retail marketplace grows.

5. Because of the concerns raised about the structure of the proposed PSA, Public Counsel urges the Commission to make the requested determinations in a very specific manner. Particularly, the Commission should require Company to assure the Commission that it would still retain jurisdiction over any and all generation costs that would be passed on to its regulated customers through retail rates. Company should also acknowledge that FERC jurisdiction does not supercede the Commission's ability to review and disallow any purchased power costs that are found to be imprudent or unreasonable after a proper review and hearing on the prudency of the costs and rate impact of such costs. In particular, Public Counsel has concerns that the pricing adjustment provisions contained in subsections (a) and (b) of section 5.1 of Article 5 constitute an inappropriate shifting of risk to the purchaser, UtiliCorp United, Inc.

6. Furthermore, Company should assure that the Commission and Public Counsel have full and unfettered access to all the books and records of Company and MEPPH in order to protect the public interest.

WHEREFORE, Public Counsel respectfully submits its recommendation that the Commission approve the proposed application only if it receives the specific assurances set out above from Company and MEPPH.

Respectfully submitted,
OFFICE OF THE PUBLIC COUNSEL

BY: _____

John B. Coffman (Bar No. 36591)
Deputy Public Counsel
Harry S Truman Bldg., Suite 205
301 West High Street, Box 7800
Jefferson City, MO 65102
Telephone: (573) 751-5565
Facsimile: (573) 751-5562

CERTIFICATE OF SERVICE

I hereby certify that the foregoing document has been either faxed, mailed, or hand-delivered to the following counsel of record on this 5th day of April, 1999:

Dana K. Joyce
General Counsel
Missouri Public Service Commission
P. O. Box 360
Jefferson City, MO 65102

James C. Swearengen // Paul A. Boudreau
Brydon, Swearengen & England, P.C.
312 East Capitol Avenue, Box 456
Jefferson City, MO 65102-0456

Gary Glemens
UtiliCorp United, Inc.
10700 East 350 Highway
Kansas City, MO 64138

_____

STATE OF MISSOURI
PUBLIC SERVICE COMMISSION

At a Session of the Public Service Commission held at its office in Jefferson City on the 22nd day of April, 1999.

In the Matter of the Application of UtiliCorp United Inc. Under Section 32(k) of the Public Utilities Holding Company Act of 1935 Concerning a Proposed Power Sales Agreement Between MEP Pleasant Hill, L.L.C. and UtiliCorp United Inc. d/b/a Missouri Public Service.	))))))))	**Case No. EM-99-369**

ORDER REGARDING POWER SALES AGREEMENT

On March 1, 1999, UtiliCorp United Inc. (UtiliCorp) d/b/a Missouri Public Service filed an Application with the Commission seeking an order of the Commission regarding a Power Sales Agreement (PSA) between UtiliCorp and MEP Pleasant Hill, L.L.C. (MEPPH). UtiliCorp proposes to enter into a PSA agreement with MEPPH whereby UtiliCorp would purchase electric power generated by MEPPH beginning on June 1, 2001. MEPPH is an exempt wholesale generator of electric power and is an affiliate of UtiliCorp.

Section 32(k) of the Public Utility Holding Company Act of 1935 (PUHCA), codified at 15 U.S.C. 79z-5a(k), provides that "an electric utility company may not enter into a contract to purchase electric energy at wholesale from an exempt wholesale generator if the exempt wholesale generator is an affiliate or associate company of the electric utility company." The federal statute then goes on to indicate that an electric

utility company may enter into such a contract with an affiliate if every state commission having jurisdiction over the retail rates of such electric utility company makes certain specific determinations in advance of the electric utility company entering into such contract. UtiliCorp's Application asks that the Commission enter an order making the required specific determinations. Because of the need to begin construction of a combustion turbine generation plant by the end of July of 1999, UtiliCorp asked that the Commission issue its order regarding this Application no later than May 1, 1999.

On March 5, the Commission issued a Notice Establishing Time for Filing of Recommendation that directed the Staff of the Public Service Commission (Staff) to file its recommendation regarding approval or rejection of UtiliCorp's Application no later than April 5. The Office of the Public Counsel (Public Counsel) was also allowed until April 5 to file its recommendation.

On April 5, Staff filed two memorandums, one submitted by Michael S. Proctor, Chief Regulatory Economist for the Commission, and the other submitted by Mark L. Oligschlaeger, Regulatory Auditor V, and Steven Dottheim, Chief Deputy General Counsel. Both memorandums evaluate the PSA and recommend that the Commission approve UtiliCorp's application. Staff did, however, recommend that the Commission's approval be subject to several conditions. Public Counsel also filed its recommendation on April 5. Public Counsel recommended approval but only upon certain conditions. 4 CSR 240-2.080(12) provides that parties are allowed ten days from the date of filing in which to respond to any motion or

pleading. No timely response was filed to the recommendations of either Staff or Public Counsel.

The Commission has reviewed and considered the Application filed by UtiliCorp and the recommendations of Staff and Public Counsel. The Commission finds that the Application of UtiliCorp should be granted subject to the conditions recommended by Staff and Public Counsel.

IT IS THEREFORE ORDERED:

1. That, in compliance with Section 32(k) of the Public Utility Holding Company Act of 1935, the Commission determines that:

   a) the Commission has sufficient regulatory authority, resources and access to books and records of UtiliCorp United Inc., MEP Pleasant Hill, L.L.C. and any relevant associate, affiliate or subsidiary company to exercise its duties under subparagraph (k) of Section 32 of the Public Utility Holding Company Act of 1935;

   b) the transaction will benefit consumers;

   c) the transaction does not violate any Missouri law;

   d) the transaction would not provide MEP Pleasant Hill, L.L.C. with any unfair competitive advantage by virtue of its affiliation or association with UtiliCorp United Inc.; and

   e) the transaction is in the public interest.

2. That the Commission's approval of UtiliCorp United Inc. d/b/a Missouri Public Service's Application is specifically conditioned upon the following conditions:

a) That UtiliCorp United Inc. shall make available to the Commission, its Staff and the Office of the Public Counsel, at reasonable times and reasonable places, all books and records and employees and officers of MEP Pleasant Hill, L.L.C. and any affiliate or subsidiary of UtiliCorp engaged in any activity with MEP Pleasant Hill, L.L.C.

b) MEP Pleasant Hill, L.L.C. shall employ accounting and other procedures and controls related to cost allocations and transfer pricing to ensure and facilitate full review by the Commission and its Staff and to protect against cross-subsidization of non-Missouri Public Service business by Missouri Public Service's customers.

c) This order is in no way binding on the Commission or any party regarding a future rate or earnings complaint case to contest the ratemaking treatment to be afforded the Power Sales Agreement. UtiliCorp United Inc. shall not seek to overturn, reverse, set aside, change or enjoin, whether through appeal or the initiation or maintenance of any action in any forum, a decision or order of the Commission which pertains to recovery, disallowance, deferral or ratemaking treatment of any expense, charge, cost or allocation incurred or accrued by MEP Pleasant Hill, L.L.C. or UtiliCorp United Inc. d/b/a Missouri Public Service in or as a result of the Power Sales

Agreement on the basis that such expense, charge, cost or allocation has itself been filed with or approved by the Federal Energy Regulatory Commission, or was incurred pursuant to the Power Sales Agreement.

3. That the Commission's approval of the instant Power Sales Agreement does not imply or assure approval of any future contracts to purchase electric energy at wholesale from an exempt wholesale generator that is an affiliate or associate company of an electrical corporation within the Commission's jurisdiction.

4. That UtiliCorp United Inc. is authorized to enter into, execute and perform in accordance with the terms and conditions of the proposed Power Sales Agreement by and between MEP Pleasant Hill, L.L.C. and UtiliCorp United Inc. d/b/a Missouri Public Service.

5. That UtiliCorp United Inc. is authorized to enter into, execute and perform in accordance with the terms of all documents reasonably necessary and incidental to the performance of the transactions that are the subject of the Application.

6. That this order shall become effective on May 4, 1999.

7. That this case may be closed on May 5, 1999.

BY THE COMMISSION

Dale Hardy Roberts

Dale Hardy Roberts
Secretary/Chief Regulatory Law Judge

(S E A L)

Lumpe, Ch., Murray, Schemenauer
and Drainer, CC., concur
Crumpton, C., absent

Woodruff, Regulatory Law Judge

BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

In the matter of Missouri Public Service of Kansas City, Missouri, for authority to file tariffs increasing electric rates for service provided to customers in the Missouri Public Service area	)))))	Case No. ER-2001-672

County of Jackson)
) ss
State of Missouri)

AFFIDAVIT OF STEPHEN L. FERRY

Stephen L. Ferry, being first duly sworn, deposes and says that he is the witness who sponsors the accompanying testimony entitled "Rebuttal Testimony of Stephen L. Ferry;" that said testimony was prepared by him and under his direction and supervision; that if inquiries were made as to the facts in said testimony and schedules, he would respond as therein set forth; and that the aforesaid testimony and schedules are true and correct to the best of his knowledge, information, and belief.

Stephen L. Ferry

Subscribed and sworn to before me this 7th day of January, 2002.

Notary Public

My Commission expires:

8-20-2004

TERRY D. LUTES
Jackson County
My Commission Expires
August 20, 2004