Exhibit No.:
Issue: Synergies
Witness: Frank A. DeBacker
Sponsoring Party: UtiliCorp United Inc.
Case No.: EM-2000-292
Date Prepared: June 26, 2000

MISSOURI PUBLIC SERVICE COMMISSION
Case No. EM-2000-292

Surrebuttal Testimony

of

Frank A. DeBacker

Jefferson City, Missouri

Exhibit No. 20
Date 7-13-00 Case No. EM-2000-292
Reporter ma

BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI
SURREBUTTAL TESTIMONY OF FRANK A. DEBACKER
ON BEHALF OF UTILICORP UNITED INC.
CASE NO. EM-2000-292

Q. Please state your name and business address.

A. My name is Frank A. DeBacker and my business address is 10750 East 350 Highway, Kansas City, Missouri 64138.

Q. By whom are you employed and what is your present position?

A. I am employed by UtiliCorp United Inc. ("UtiliCorp") as Vice President, Fuel and Purchased Power in its domestic regulated electric utility operations.

Q. Are you the same Frank A. DeBacker who previously adopted the direct testimony of Robert W. Holzwarth in this proceeding involving the merger of UtiliCorp with St. Joseph Light & Power Company ("SJLP")?

A. Yes I am.

Q. What is the purpose of your surrebuttal testimony in this proceeding?

A. My surrebuttal testimony will respond to the rebuttal testimony of the Missouri Public Service Commission Staff ("Staff") with respect to the following areas:

- First, I will address the results of the analysis of the merged system power costs and the recommended conditions for approval of the merger presented by Staff Witness Mr. Tom Y. Lin in his rebuttal testimony.
- Second, I will address those sections of Staff Witness Dr. Michael S. Proctor's rebuttal testimony where he:
    - Assumes that the wholesale energy market is perfectly competitive; and,

- Concludes that "What the Applicants call energy cost savings represent, in large part, energy cost-related opportunities rather than merger-related savings;" and as a result recommends that," only $6.8 million of the Merger Applicants' estimate of energy cost-related savings be included as merger-related …".
- Third, I will also address Dr. Proctor's proposed changes to the Applicants' Electric Allocations Agreement and his attachment thereto titled Regulatory Plan for Energy Costs (Proctor, Schedule 4.2).

- Finally, I will address the Staff's apparent disregard of the capacity savings resulting from the merger.

Q. Have you reviewed the rebuttal testimony of Mr. Tom Y. Lin?

A. Yes I have.

Q. Do you have a general response to the analysis contained in his testimony?

A. Yes. Except for the scenarios specifically requested by Dr. Proctor, I have no material disagreements with Mr. Lin's analysis. Mr. Lin and I used essentially the same database and software to determine the impact of the proposed merger on power costs. As noted in his testimony, Mr. Lin made several minor changes to the input assumptions that for the most part had minor impact on the results. In fact, Mr. Lin's results are quite close to the Applicants' results in all scenarios with the exception of those scenarios requested by Dr. Proctor.

Q. Which scenarios did Dr. Proctor instruct Mr. Lin to prepare?

A. It is my understanding that Dr. Proctor instructed Mr. Lin to prepare scenarios using the assumption that each stand-alone company had the same wholesale sales opportunities as the merged company.

Q. Do you have a response with respect to this assumption?

A. Yes. I do not agree with this assumption.

Q. What merger conditions did Mr. Lin recommend the Commission order?

A. Mr. Lin recommended that:

- "MPS and SJLP must continue to provide the historical actual hourly generation, energy purchases and sales data, and other information for the MPS and SJLP divisions of UCU required under Commission Rule 4 CSR 240-20.080 in electronic format assessable by a spreadsheet program"
- "...that the Commission may access and require without the necessity of subpoena the production of all accounts, books, contracts, records, documents, memoranda, papers, and employees of UtiliCorp United, Inc....".

Q. Do you agree with Mr. Lin's recommendations?

A. UtiliCorp, its Missouri Public Service ("MPS") operating division and SJLP agree that they should be held to the same reporting standards as other utilities under the jurisdiction of this Commission and will comply with any and all reporting requirements established by the Commission.

Q. Have you reviewed the rebuttal testimony of Staff Witness Dr. Proctor?

A. Yes I have.

Q. Do you agree with his conclusions regarding energy cost savings; i.e.: that "What the Applicants call energy cost savings represent, in large part, energy cost-related opportunities rather than merger-related savings;..." and that "... only $6.8 million of the Merger Applicants' estimate of energy cost-related savings be included as merger-related ..."?

A. No, I do not.

Q. Why not?

A. Dr. Proctor used a very simplistic and unrealistic assumption in order to arrive at this conclusion. He assumed that the wholesale market is in essence perfect and that both UtiliCorp and SJLP each had equal access to the wholesale market. This assumption is not realistic, does not take into account the Federal Energy Regulatory Commission's ("FERC") rules concerning this activity, and is not supported by the SJLP or UtiliCorp internal forecasts of this activity.

Q. What is the position of UtiliCorp and SJLP concerning merger related energy cost savings?

A. As stated in Mr. Holzwarth's direct testimony, the position of UtiliCorp and SJLP is that the total merger related energy cost savings over the ten-year analysis period are approximately $104 million.

Q. What causes the difference between the UtiliCorp/SJLP estimates of $104 million in energy related savings and Dr. Proctor's argument that only $6.8 million in energy related savings are related to the merger?

A. The vast majority of the difference rests with Dr. Proctor's assumption concerning wholesales sales volumes and margins. He assumes that there exists a perfect wholesale market and that MPS, SJLP and the merged company will participate in that market on the same basis, i.e.: each entity will be able to sell at the market price and have the same level of market penetration.

Q. How do you respond to this assumption?

A. I do not agree with it.

Q. Why?

A. This assumption is unrealistic. The wholesale energy market is not perfect and the abilities and opportunities of each of the market participants are not equal. The actual experience of each of UtiliCorp and SJLP in the wholesale market since 1996 is a clear example of the different approaches taken by each on a stand-alone basis and this historical perspective should be taken into account when important assumptions are formulated. Dr. Proctor has apparently chosen not to take the actual experience of each of the companies into account when he formulated this basic assumption.

Q. Please describe the wholesale assumptions used by UtiliCorp and SJLP in connection with the proposed merger ?

A. First, on a stand-alone basis it was assumed that both entities would continue to generate approximately the same level of normalized wholesale volumes and margins over the 10-year study period as those generated in recent years. This assumption was supported by the internal forecasts of each entity, and the fact that SJLP had not actively participated in the deregulating wholesale market to the same extent as MPS. Second, after the merger, it was assumed that the combined company would make all wholesale market sales at market rates, and that the combined company would be able to increase its wholesale market penetration. Thus, the merger would not only result in an increase in the volume of wholesale sales, but an increase in the overall profitability due to use of market-based rates.

Q. What is the basis for the wholesale sales assumption for SJLP and MPS as individual stand-alone companies?

A. This assumption is supported by an examination of the facts surrounding each company's approach to the deregulation of the wholesale market and each company's internal forecasts.

Q. Please describe the SJLP facts.

A. The facts concerning the SJLP wholesale operations are as follows:

- SJLP has not been and is not now active in the wholesale market.
- As one of the smallest investor owned electric utilities in the nation, its size and limited resource mix make it very costly to develop and sustain an effective wholesale marketing group.
- SJLP does not have FERC approval to sell energy at market-based rates. Thus, the margins that it can earn from such sales are limited.
- SJLP elected not to separate its transmission and generation functions due to cost, thus, it does not have approval to sell at market rates and must sell its excess energy at cost based rates.
- SJLP does not currently have a wholesale marketing group dedicated to pursuing the wholesale market and does not have plans to create such a group.

Q. Please describe the MPS facts.

A. The facts concerning the MPS wholesale operations are:

- MPS has been active in the wholesale market since 1996 and has been selling at market rates.
- MPS, as required by FERC, has separated its generation and transmission functions.

- MPS maintains a fully staffed wholesale marketing group to pursue opportunities in the wholesale market.

Q. What do you conclude from these facts?

A. MPS has been and continues to be much more active in the deregulation wholesale market than SJLP. This MPS activity both in terms of volumes and margins has reached a plateau, in part due to transmission limitations. The operations of the combined company, with its enhanced transmission capabilities, will allow it to expand its efforts in the wholesale market much more efficiently than either of the companies could do separately. The reality of this situation is quite the opposite of the assumption used by Dr. Proctor to arrive at his projection of merger related energy savings of only $6.8 million.

Q. Please describe the wholesales sales assumptions used by UtiliCorp and SJLP for the operation of the combined company.

A. It was assumed that UtiliCorp would be able to increase its wholesale market penetration and increase the profit margin on wholesale sales. The increase in wholesale profit margin is due UtiliCorp's ability to sell at market-based rates versus cost-based rates. The increase in market penetration and sales activity are primarily due to the transmission interconnects that the new combined company will have via the interconnections that SJLP has with other utilities in the Mid-Continent Area Power Pool ("MAPP"), and the increase in available capacity for sale into the wholesale market.

Q. Please describe the FERC requirements for the separation of generation and transmission activities.

A. The FERC issued Order No. 889 on April 24, 1996 which included provisions, (Section 37.4 (a) (1), that stated that "the employees of the Transmission Provider engaged in transmission system operations must function independently of its employees, or the employees on any of its affiliates, who engage in Wholesale Merchant Functions". The Order continued by stating; Section 37.4 (b) (1) "Prohibitions. Any employee of the Transmission Provider, or any employee of an affiliate, engaged in wholesale merchant functions is prohibited from: (i) conducting transmission system operations or reliability functions; and (ii) having access to the system control center or similar facilities used for transmission operations or reliability functions that differs in any way from the assess available to other open access Transmission Customers."

Q. On an annual basis, how much does it cost MPS to comply with the FERC rules of separation between generation and transmission?

A. MPS has functionally separated its generation and transmission since the issuing of the FERC order referenced above. Over the past 3 years, our wholesale trading operations has had an annual operating budget averaging $3.5 million and annual capital expenditures (software and equipment) averaging $1 million.

Q. What would you expect SJLP to spend to comply with these FERC rules?

A. SJLP trading operation would be somewhat smaller than UtiliCorp's but due to the separation of the dispatch and transmission function and the obtaining of comparable trading talent would possibly cost SJLP in the area of $1+ million per year. This, however, does not include the change in management attitude to take on the risk that exists in the trading world today and the impact of the possible financial losses that have been incurred by other utilities that have not been as successful as UtiliCorp. These losses can be substantial and have a large impact on the utilities bottom line. To ensure the risk factor is minimized, a utility entering this trading activity will need to ensure a proper Risk Management program is established. I have not included this additional cost in my estimate.

Q. Did Dr. Proctor take the SJLP limitations and the additional operation expense and experience required into account in formulating his basic assumptions concerning the SJLP capability in the wholesale market?

A. Apparently not. SJLP has quite simply not made the investment in the necessary equipment and personnel nor acquired the risk management expertise required to make Dr. Proctor's assumption realistic.

Q. Do you agree with Dr. Proctor's proposed changes to the Electric Allocations Agreement of UtiliCorp and SJLP?

A. Dr. Proctor makes several editorial changes which, for the most part, serve to clarify the language of the agreement. The companies generally agree with these changes. There are three changes proposed by Dr. Proctor with which UtiliCorp and SJLP do not agree.

Q. What is the first proposed change with which the UtiliCorp and SJLP do not agree?

A. The first change occurs in Section 4.02 Capacity Margin Requirements. Dr. Proctor seems to propose that both MPS and SJLP should be required to meet the capacity reserve requirements of both the Southwest Power Pool ("SPP") and MAPP. The designation of a specific reliability council, or power pool should not be included in the Electric Allocations Agreement.

Q. Why?

A. It is entirely possible that MPS and SJLP will be in different reliability councils or that both the SPP and MAPP will cease to exist in the future. Each UtiliCorp division, MPS and SJLP, should be required to be a member of a FERC approved reliability organization and to meet the capacity reserve requirements of that organization.

Q. What is the second point of disagreement?

A. The second point of disagreement is the percentages that Dr. Proctor proposes be applied to allocate the reductions in the cost of the energy required to serve the on-system energy needs of MPS and SJLP. Dr. Proctor proposes that a portion of the on-system energy savings be allocated to MPS and a portion allocated to SJLP. UtiliCorp and SJLP's position is that 100% of the savings in on-system energy costs should be allocated to SJLP.

Q. Why?

A. Allocation of 100% of the on-system energy savings to SJLP is appropriate because:

- It is the addition of the SJLP power supply portfolio that produces the cost savings; and,
- Allocation of 100% of the savings places the benefits with the division incurring the cost, including the cost of the premium and the other costs incurred to combined the companies and realize the synergies.

Q. What is the third point of disagreement?

A. The third point of disagreement the allocation percentage that Dr. Proctor proposes to use to allocate margins from off-system energy sales between the divisions. Dr. Proctor proposes that margins from all off-system energy sales be allocated 84.6% to MPS and

2.9% to SJLP. The position of UtiliCorp and SJLP is that 100% of the margins from incremental off-system energy sales should be allocated to SJLP.

Q. What do you mean by "incremental off-system sales"?

A. By "incremental off-system sales", I mean off system sales that are above and beyond those that could have been made by MPS and SJLP on a stand-alone basis.

Q. What are the reasons for the position of UtiliCorp and SJLP?

A. Allocation of 100% of the incremental margins from off -system sales to SJLP is appropriate for two reasons:

- First, these incremental margins would not be possible except for the addition of the SJLP power supply portfolio and transmission assets.
- Allocation of 100% of the incremental margins to SJLP places the benefits with the division incurring the cost, including the cost of the premium and the other costs incurred to combined the companies and realize the synergies.

Q. Earlier in your testimony, you stated that the Staff apparently disregards the capacity savings associated with the merger. Please explain.

A. In Mr. Holzwarth's direct testimony, he shows a capacity savings of $6.2 million over the 10-year analysis period (see the top of page 20 of Mr. Holzwarth's direct testimony). As Mr. Holzwarth states on page 6, line 15 of his testimony, this savings results from "Combining the loads of two systems into a single control area which reduces the amount of capacity required due to the natural diversity between the load profiles of the two systems. This reduction in the amount of required capacity reduces the overall power supply cost to the combined system." On page 22, line 18 of Dr. Proctor's rebuttal testimony where he outlines the components of power supply cost savings, Dr. Proctor seems to agree with Mr. Holzwarth when he states “Second, with respect to joint capacity planning for the merged utilities there are potential savings from combining the loads for purposes of determining peak load capacity requirements. These savings are specifically related to the diversity of load (the assumption that the MPS and SJLP loads do not reach their peaks at the same time).”

In spite of his apparent agreement, Dr. Proctor choose not include the capacity component of power supply savings in any of his analysis and it does not appear in any of the analysis of other Staff witnesses.

Q. Does this conclude your surrebuttal testimony?

A. Yes.

BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

In the Matter of the Joint Application of UtiliCorp United Inc. and St. Joseph Light & Power Company for Authority to Merge St. Joseph Light & Power Company with and into UtiliCorp United Inc., and, in Connection Therewith, Certain Other Related Transactions.	)	Case No. EM-2000-292

County of Jackson)
)
State of Missouri)

AFFIDAVIT OF FRANK A. DEBACKER

Frank A. DeBacker, being first duly sworn, deposes and says that he is the witness who sponsors the accompanying testimony entitled surrebuttal testimony; that said testimony was prepared by him and or 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.

Frank A DeBacker

Subscribed and sworn to before me this 26 day of June, 2000.

Linda C.Howell
Notary Public-Notary Seal
State of Missouri
Jackson County
My Commission Expires: May4, 2004

Linda C. Howell
Notary Public

My Commission expires:

May 4, 2004