Approved: Carl Dean Holmes
Date 2-17-99

MINUTES OF THE HOUSE COMMITTEE ON UTILITIES.

The meeting was called to order by Chairperson Rep. Carl Holmes at 9:04 a.m. on February 8, 1999 in Room 522-S of the Capitol.

All members were present except:

Committee staff present: Lynne Holt, Legislative Research Department
Mary Torrence, Revisor of Statutes
Jo Cook-Whitmore, Committee Secretary

Conferees appearing before the committee:
Larry Holloway, Kansas Corporation Commission
Jim Ludwig, Western Resources
Bruce Graham, Kansas Electric Power Cooperative, Inc.
Burton Crawford, Kansas City Power & Light

Others attending: See Attached List

Hearing on HB 2120 - Electric public utility required to give priority to firm customers in certified territories.

The Chairman welcomed Larry Holloway, Chief of Energy Operations for the Kansas Corporation Commission, who provided neutral testimony on **HB 2120** on behalf of the KCC (Attachment 1).

Mr. Jim Ludwig of Western Resources then presented testimony in opposition to **HB 2120** (Attachment 2).

Chairman Holmes acknowledged Bruce Graham, Vice President of Member Services & External Affairs for KEPCo, who testified in opposition to **HB 2120** (Attachment 3).

The Chair introduced Burton Crawford, Manager of Deregulation Issues for KPCL, who provided testimony in opposition to **HB 2120** (Attachment 4).

The hearing concluded with conferees responding to questions from the committee.

Meeting adjourned at 9:53 a.m.

Next meeting is Tuesday, February 9.

HOUSE UTILITIES COMMITTEE GUEST LIST

DATE: February 8, 1999

NAME	REPRESENTING
Don Gaches	McGill, Gaches & Assn.
Sandy Braden	McGill, Gaches & Assoc.
Larry Holloway	KCC
Burton Crawford	KCPL
Patrick Hickey	KCPL
J.C. Long	UCU
Kim Gulley	League of KS municipalities
Doug Laurence	KEC
Von K Miles	KEC
Bruce Graham	KEPCo
Wayne Kitchen	Western Resources
Dave Holthaus	Western "
Jim Ludwig	" "
John Diedrich	Boeing
Whitney Damron	Empire District Electric Co.

HOUSE UTILITIES COMMITTEE GUEST LIST

DATE: _____

NAME	REPRESENTING
DICK CARTER	ENRON
ED SCHAUB	WESTERN RESOURCES
JOHN C. BOTTENBERG	WESTERN RESOURCES

BEFORE THE HOUSE UTILITIES COMMISSION

PRESENTATION OF THE

KANSAS CORPORATION COMMISSION ON

HOUSE BILL NO. 2120

Thank you Chairman, I'm Larry Holloway, Chief of Energy Operations for the Kansas Corporation Commission and I'm appearing today on behalf of the KCC. The KCC does not take a position on this bill, however I would like to discuss what we believe this legislation accomplishes and how it interfaces with federal jurisdiction and regulation of electric transmission and wholesale electric sales.

This bill sets a priority for firm retail electric customers within the utility's certified territory. The electric utility must supply those customers with service first if it does not have sufficient generation to supply all of its obligations. It is assumed that this would essentially establish a priority list with the utility's firm retail customers, within its certified territory, at the top of the list. References to certified territory apparently envision a retail wheeling scenario where a utility may have firm retail generation service customers outside of its certified distribution territory.

Under it's transmission open access rulings, the Federal Energy Regulatory Commission (FERC) requires each utility to provide transmission services and access to third parties on a nondiscriminatory or "comparable basis". As stated in FERC Order 888:

> "An open access tariff that is not unduly discriminatory or anticompetitive should offer third parties access on the same or comparable basis, and under the same or comparable terms and conditions, as the transmission provider's uses of its system."[1]

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[1] page 37, ORDER NO. 888, issued April 24, 1996, in FERC Docket Nos. RM95-8-00 and RM94-7-001

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ATTACHMENT 1

Because the FERC broadly considers transmission services to include many generation service related functions (such items as generation dispatch, supplying line losses, voltage control, etc) federal jurisdiction could preempt state law regarding priority of service. Additionally, the FERC approves wholesale energy and capacity sales by Investor Owned Utilities (IOUs) and may preempt any state attempt to modify the priority or provisions of these contractual agreements.

While FERC jurisdiction may overrule some of the applications of this bill, the proposal itself is broad and would apply even to utilities the FERC does not regulate. For example, according to K.S.A. 66-104 any entity which transmits power is a public utility. However, since FERC has jurisdiction over IOU transmission tariffs, the KCC is preempted from regulating IOU transmission services. However, for utilities that are not FERC regulated, and that are KCC jurisdictional, such as rural electric cooperatives that own transmission, the KCC clearly has jurisdiction over their transmission services and is not preempted by the FERC. In summary, while the FERC could preempt our enforcement of this act for utilities that are FERC jurisdictional, this overlap does not necessarily create a problem.

Perhaps more significant than any overlap or preemption by federal jurisdiction, is the application of this bill only to KCC jurisdictional utilities. First, the KCC already has broad authority to apply such a priority over its jurisdictional utilities without legislation, and could do so if it found it to be in the public interest. Second, the bill does not address such entities as generating municipalities which for the most part are not KCC jurisdictional. Kansas City Kansas Board of Public Utilities (KCBPU), for example, sells firm wholesale power to other municipal utilities in the state of Kansas. Many of the KCC jurisdictional utilities' firm wholesale contracts are also with municipal utilities in Kansas. Because this bill is limited to KCC jurisdictional utilities, and does not apply to all Kansas electric utilities, some Kansas

municipal utilities would be penalized, solely because of where they purchase power. If the Legislature wants to establish this statewide policy, it should consider the inclusion of all Kansas electric utilities, not just those that are regulated by the KCC.

Testimony
before the
HOUSE UTILITIES COMMITTEE
by
Jim Ludwig, Western Resources
February 8, 1999

Chairman Holmes and members of the Committee:

Western Resources is opposed to HB 2120. This bill gives firm retail electric customers within an electric utility's service territory priority over firm wholesale customers outside its service territory.

Harm to Reliability

The intent of the bill is presumably to assure that firm retail electric customers' service is not interrupted during periods of peak demand. Enacting the bill would defeat its purpose. HB 2120 would reduce the Eastern Interconnection's system reliability by interrupting contractual obligations. If we and others don't keep our wholesale contractual obligations, the whole system's integrity is threatened. HB 2120 would jeopardize service both to retail and wholesale customers.

Retaliatory Response

Self-protectionist behavior will trigger a retaliatory response. If Kansas utilities can't keep their contracts to sell electricity, they won't be able to secure contracts to buy when need is greatest. Electric providers will do business with those who reciprocate. They won't do business with those who don't.

Economic Harm

This committee has recently held hearings to explore how to ensure adequate generation in the state. Who would willingly build a plant in Kansas under the commercial restrictions of this bill? Most new generation is fueled by natural gas, a fact that gives Kansas a singular advantage. This bill would cause Kansas to sit on a wasted opportunity.

Benefits of Wholesale Contracts to Retail Customers

HB 2120 seems to be based on the erroneous assumption that firm wholesale sales do not support the recovery of costs of power plants installed to serve retail customers. The truth is wholesale sales are made to leverage capacity and provide revenue which can be used to lower rates of retail customers. This KCC-approved policy intelligently balances incentives to engage in wholesale transactions with the interests of retail electric customers.

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Wholesale Service Characteristics

KPL and KGE wholesale customers vary, but can be generally categorized. KPL and KGE have about 35 Kansas municipal utility customers who are firm customers. We supply all their electricity needs. We have over 25 Kansas municipal utility customers who have the ability to generate some of their own electricity. These customers ordinarily bring their own generation on line during peak demand conditions in order to help us reliably supply our firm retail customers. Western Resources is pursuing more of these agreements. We have three Kansas rural electric cooperatives who take their full requirements for service from us. We have electric service agreements with KEPCO, which in turn provides firm electric service to over 20 Kansas rural electric cooperatives. Finally, we have participation capacity agreements with Midwest Energy, Empire Electric, Central and Southwest, and the Oklahoma Municipal Power Authority. Participation capacity sales are agreements to take power from a specific generating unit. If the unit is not operating at full capacity, the amount of power under the agreement is reduced *pro rata*. If the unit is not operating, the customer doesn't get power. We also enter contracts with power marketers who are either moving energy across our system or who are buying energy from our system. Contracts and tariffs to serve wholesale customers are regulated and approved by the Federal Energy Regulatory Commission (FERC).

Constitutional and Legal Violations

Attached to my testimony is a legal opinion written by Michael Lennen, a consulting attorney to Western Resources. Mr. Lennen is a former chair of the KCC. His opinion discusses several constitutional and legal faults in HB 2120.

February 5, 1999

VIA FEDERAL EXPRESS TO:

James J. Ludwig
Senior Director-Regulatory Affairs
WESTERN RESOURCES
818 Kansas Avenue
Topeka, Kansas 66603

Re: Constitutionality of House Bill No. 2120

Dear Mr. Ludwig:

You have requested our review of constitutional and other legal issues implicated by House Bill No. 2120. The bill attempts fundamentally to change the regulatory treatment of wholesale energy transactions by Kansas public utilities. It is our opinion that the attempted treatment of these transactions in inconsistent with the federal regulatory scheme and poses an unconstitutional burden on interstate commerce. It is our opinion that the bill, as proposed, would not withstand judicial scrutiny.

I. The Bill Conflicts with Federal Regulation of Electric Energy Sales.

Electric public utilities enter into a variety of contractual arrangements for the sale of power or generation capacity. Typically, only a portion of the electricity generated by an electric public utility is sold by that utility to retail customers located within its exclusive certified territory. Other electricity sales are made to municipal utilities, to rural electric cooperatives, and to other investor-owned electric utilities located both within and without the state. Those sales are subject to federal regulation. The sales contracts for those sales typically are filed with the Federal Energy Regulatory Commission ("FERC") and are subject to FERC approval. Alternatively, the sales are made under FERC-approved tariffs. Congress has determined that federal regulation of wholesale sales of electric energy in interstate commerce is a matter of public interest. 12 U.S.C. § 824(a). FERC has been granted the right to regulate wholesale sales of electric energy. 12 U.S.C. § 824(b).

> Interference with federal regulation of interstate commerce is prohibited. "There can be no divided authority over interstate commerce, and * * * the acts of Congress on that subject are supreme and exclusive." *Missouri Pacific R. Co. v. Stroud*, 267 U.S. 404 408, 45 S.Ct. 243, 69 L.Ed.2d 683 (1925). Consequently, state efforts to regulate commerce must fall when they conflict with or interfere with federal authority over the same activity.

Chicago & North Western Transp. Co. v. Kalo Brick, 450 U.S. 311, 318-19, 101 S.Ct. 1124, 67 L.Ed.2d 258 (1981). The Supreme Court has held that in the area of wholesale electric energy contracts, it is impermissible for a state to adopt an allocation of sources of energy different than that approved by FERC. *Nantahala Power & Light v. Thornburg*, 476 U.S. 953, 106 S.Ct. 2349, 90 L.Ed.2d 943 (1986).

The bill causes direct conflicts with federal regulation, to the extent that it purports to impact contractual obligations under contracts previously approved by FERC. This attempt to change federally approved contractual obligations, certainly does not appear to be consistent with the federal regulatory scheme. Moreover, to the extent it would impose restrictions on the terms of future wholesale sales of electric energy, it likewise appears to invade the province of federal regulation.

Because this bill poses substantial obligations that appear to be directly inconsistent with federal regulatory requirements, it cannot stand.

II. The Bill Violates the Commerce Clause

The Commerce Clause of the United States Constitution vests in Congress the right to regulate interstate commerce. State regulation that is contrary to the Constitutional principle of insuring that the conduct of individual states does not work to the detriment of the nation as a whole are invalid under the Commerce Clause, even in the absence of explicit federal regulation. *Wardair Canada, Inc. v. Florida Dep't of Revenue*, 477 U.S. 1 (1986). To the extent that this measure aims to unduly burden interstate commerce to benefit local interests, there is a serious question about whether the measure could be consistent with the Commerce Clause.

This measure, which aims to benefit electric energy customers located within the certified service territory of the public utility, can be seen as discriminating against

interstate commerce. As defined in the statute, the beneficiaries of this bill can only be within the state. Those potentially adversely impacted by this bill would include out-of-state purchasers of electric energy. As a measure that disproportionately hurts interstate commerce, the bill would be subject to strict scrutiny. "At a minimum such facial discrimination invokes the strictest scrutiny of any purported legitimate local purpose and of the absence of nondiscriminatory alternatives." *Hughes v. Oklahoma*, 441 U.S. 322, 337 (1979).

State measures that are designed to serve local economic interests at the expense of interstate commerce are not consistent with the commerce clause. Examples of laws being struck down for this reason are numerous. In *New England Power Co. v. New Hampshire*, 455 U.S. 331 (1982), the Court considered a law passed by New Hampshire that purported to prevent the transportation of electric energy outside of the state without state commission approval. The law purported to authorize the prohibition of export of power whenever the state commission determined that the energy was "reasonably required for use within this state and that the public good requires that it be delivered for such use." 455 U.S. at 335. This law was struck down as "precisely the sort of protectionist regulation that the Commerce Clause declares off-limits to the states." 445 U.S. at 339. *See also*, *Middle South Energy v. Arkansas Public Service Commission*, 772 F.2d 404, 417 (8th Cir. 1985) (striking down electric energy regulatory measure that constituted "a preference for citizens in the regulating jurisdiction gained at the expense of out-of-state customers").

It appears unlikely that this law could pass muster under the Commerce clause.

III. The Bill Implicates Other Constitutional Concerns.

The harm that this bill may do to existing contractual relationships, as well as its very nature raises other constitutional concerns. To the extent that the bill purports to take contractual benefits away from a public utility that previously has entered into contracts, the bill raises questions about the necessity of paying compensation for property taken. *See, Thompson v. Consolidated Gas Co.*, 300 U.S. 55, 57 S.Ct. 364, 81 L.Ed. 510 (1937). The nature and subject of the regulation raises questions about whether this is special interest economic regulation that does not fall within the state's police powers, or is consistent with due process restrictions. *Manhattan Buildings, Inc. v. Hurley*, 231 Kan. 20,

30, 643 P.2d 87 (1982) (The regulation must be reasonable in relation to its subject and adopted in the interest of the community).

For these reasons, we are of the opinion that House Bill No. 2120 is unconstitutional.

Sincerely,

Michael Lennen
For the Firm

CML/niw

Kansas Electric Power Cooperative, Inc.

A Touchstone Energy℠ Partner

Testimony on HB 2120

Before the House Utilities Committee -- February 8, 1999

Bruce Graham, KEPCo's Vice President, Member Services & External Affairs

Kansas Electric Power Cooperative (KEPCo) was formed in 1975 by a group of rural electric cooperatives to provide wholesale generation and transmission service for its members. Today, KEPCo has a variety of resources including six percent of the Wolf Creek Generating Station, hydropower allocations, and long-term power supply contracts with Investor-Owned-Utilities (IOUs) across Kansas.

HB 2120 would have a very negative effect on utilities like KEPCo, its 21 member cooperatives and their 250,000 consumers. KEPCo is currently, and has been for many years, the largest single wholesale customer of Western Resources and the largest customer of WestPlains Energy (a division of Utilicorp United). As a result, and contrary to the premise of HB 2120, a firm service purchaser like KEPCo pays for the capacity of the Kansas utilities we buy from and, in return, we should receive the same level of service reliability as territorial customers. In addition, revenue from those firm wholesale transactions by Kansas IOUs to KEPCo serves to reduce their customer rates throughout the year.

KEPCo is also a transmission dependent utility which means we contract with utilities that own Kansas transmission facilities to deliver the energy to member cooperative substations. This is not unusual, many utilities depend on each other for a variety of services including transmission, assistance with storm damage, routine construction, load management, and to meet their needs for generation.

Such cooperation has served us well. For example, in the past on a July day where a 105 degree heat wave has a grip on the Midwest, all utilities in Kansas serve their customers but some may grow short on generation. Western Resources, in evaluating their situation, might have appealed to residential, commercial and wholesale customers to conserve and we would respond favorably. Under a future scenario, if this bill was law, Western Resources may make a similar appeal but there would be no real reason for their native

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customers to respond. Therefore, they would have to begin curtailing service, not just to out-of-state customers but also to your friends and neighbors in rural Kansas. As a result, other areas of Kansas would go dark and our contracts could no longer be considered firm…in fact they'd probably be deemed worthless.

Furthermore, if we were unable to depend on fellow Kansas utilities for what was formerly firm power, we would be forced to contract for generation from non-Kansas utilities, thereby diverting revenue to another state and benefiting their customers. Another option would be to construct generation, however, this law would hamper that effort. Normally, any new generation would be built to meet immediate needs with some room for load growth or off system sales. This bill would prohibit the sale of that additional energy on a firm basis to any other utility and, as a result, restrict the construction of new generation.

KEPCo believes that the current system of regulation by the KCC, efforts by reliability groups such as the North American Electric Reliability Council (NERC), and the cooperative spirit of utilities across Kansas to meet the needs of their customers would be disrupted by HB 2120, would ultimately lead to higher costs, and to turmoil in the industry. Thank you for the opportunity to comment in opposition to HB 2120.

Testimony before the House Utilities Committee
In Opposition of House Bill No. 2120

By Burton L. Crawford
Manager of Deregulation Issues
Kansas City Power & Light Company
February 8, 1999

Mr. Chairman and members of the Committee:

I am Burton Crawford, Manager of Deregulation Issues for Kansas City Power & Light Company, and am appearing before you today in opposition of House Bill 2120 that relates to furnishing electric generation service to certain customers.

While the bill appears well intentioned, KCPL's opposition is based on three potential problems that it creates in providing electric service to our customers – both wholesale and retail.

The first potential problem is related to limiting utilities the flexibility of using wholesale contracts to manage their electric supply. Utilities need the ability to both buy and sell wholesale power on a firm basis. Currently, KCPL purchases capacity through firm wholesale contracts to meet our peak load obligations. If the level of firmness of these contracts is changed, KCPL may no longer be able to use this method to meet our obligations – it could force us to build when less costly options are available. In the past, market conditions have allowed us to purchase firm capacity cheaper than we could build it ourselves. Last year, KCPL's capacity responsibility was approximately 3,600 Mw, of which 600 Mw came through these capacity purchases. This bill could limit purchase options in the future, raising costs to all customers.

KCPL also needs the ability to sell any excess capacity that we have. At times, building a larger plant than is needed benefits our retail customers by lowering the average cost of capacity. During the early years when the total capacity is not needed to serve retail

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customers, we can sell the excess at wholesale where the profits from these sales flow back to retail customers. If wholesale customers can only receive a lower priority service from KCPL, they will look elsewhere for service and limit this option for expanding our capacity.

The second potential problem is related to dealing with system emergencies. In an emergency where it becomes necessary to reduce load on the electric system to prevent the system from collapsing, the priority established in this bill may limit options for the utility operators. Utilities in the state need to retain flexibility in managing emergency situations so that disruptions to the system can be minimized.

The third potential problem is related to the regulation of firm wholesale contracts that KCPL has in place or may enter into in the future. These contracts are currently regulated by the Federal Energy Regulatory Commission (FERC), and this bill steps on their jurisdiction. FERC is not likely to agree with establishing a level of service for firm wholesale customers less than retail customers. As an example, FERC has moved to give customer with firm transmission service the same rights to transmission as retail customers. If a utility's transmission system gets to the point where transmission service is to be curtailed, the utility is to curtail retail customer use of the system in the same proportion as other customers with firm transmission rights.

As one last point, if this bill should move forward, we request that language be added to take into consideration that KCPL serves retail customers in two states. This bill could be interpreted to require KCPL to cut-off our Missouri retail customers prior to cutting-off any Kansas retail customers during an emergency. The bill states that the utility shall furnish all electric generation service requirements of firm retail customers "within the utility's certified territory" (which appears to be their Kansas certified territory) before supplying service to "other customers of the utility".

Thank you for your time. I would be happy to take any questions that you have.

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