Approved: Carl Dean Holmes
Date 3-9-99

MINUTES OF THE HOUSE COMMITTEE ON UTILITIES.

The meeting was called to order by Vice-Chairman Tom Sloan at 9:03 a.m. on February 16, 1999 in Room 522-S of the Capitol.

All members were present except: Rep. Carl Holmes

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

Conferees appearing before the committee:
Earl Watkins, Sunflower
Jon Miles, KEC
Terry Leatherman, KCCI
Bruce Graham, KEPCo
Jim Ludwig, Western Resources
Chris Giles, KCPL

Others attending: See Attached List

Vice-Chairman Sloan noted that copies of the Wall Street Journal (Attachment 1) that were distributed to the committee were provided by Bruce Graham of KEPCo. He also stated that copies of an article from the Wichita Business Journal regarding Western Resources-City of Wichita relations (Attachment 2) were provided to each member.

Continued hearing on HB 2025 - Electric Utility Restructuring Act

Earl Watkins, General Counsel for Sunflower Electric Power Corporation, presented testimony in opposition to **HB 2025** (Attachment 3).

Jon Miles, Director of Governmental Relations and Administration for the Kansas Electric Cooperatives, Inc. submitted testimony as a qualified opponent to **HB 2025** (Attachment 4).

Terry Leatherman, Executive Director of the Kansas Industrial Council for the Kansas Chamber of Commerce and Industry, next testified as a qualified opponent to the bill (Attachment 5)

Bruce Graham, Kansas Electric Power Cooperative, Inc.'s Vice President of Member Services & External Affairs, was the next to testify in opposition to **HB 2025** (Attachment 6).

Jim Ludwig, Senior Director of Regulatory Affairs for Western Resources, presented testimony in opposition to the bill (Attachment 7).

Chris Giles, Director Regulatory Services for Kansas City Power & Light Company, then presented testimony as an opponent to the bill (Attachment 8).

Testimony was concluded by conferees, from both days of hearings on **HB 2025**, responding to questions from the committee.

Meeting adjourned at 10:53 a.m.

Next meeting is Wednesday, February 17.

HOUSE UTILITIES COMMITTEE GUEST LIST

DATE: February 16, 1999

NAME	REPRESENTING
Joe Dick	KCKBPU
Tom Nestermann	Sunflower
Steve Miller	Sunflower
Earl Watkins	Sunflower
Bill Jancee	BOEING
Whitney Damron	Empire District Electric Co.
Bill Eichman	EMPIRE DISTRICT ELEC. Co.
Jack Glaves	KN-Oxy + Duke
TERRY KELLER	BOEING
Terry Leatherman	KCCI
Dave Holthaus	Western Resources
Louis Stroup Jr.	KS Municipal Utilities
J.C. LONG	UCU
BURTON CRAWFORD	KCPL
Patrick J Hurley	KCPL

HOUSE UTILITIES COMMITTEE GUEST LIST

DATE: February 16, 1999

NAME	REPRESENTING
Don K Miles	KEC
LESTER MURPHY	KEC
Chris Giles	KCPL
Robert M. Badenoch	KUCR, NVU
Larry Holloway	KEC
David Bybee	KDOCH
Jim Ludwig	Western Resources
Julie Hein	Hein & Weir, Chtd.
Sandy Braden	McGill, Gaches & Assoc.
Don Ryan	USD 321 Kaw Valley
Kim Gulley	LKM
Chris McKenzie	LKM
DICK CARTER	ENRON
BRUCE GRAHAM	KEPCo

Wall Street Journal

Distributed by Bruce Graham of KEPCO

Held in file in office of

Utilities Chairman

Carl Holmes

Room 115-S

House Utilities

February 16, 1999

Attachment 1

Wichita Business Journal

February 15, 1999

Wittig threatens to move KGE from city

Jerry Siebenmark

Western Resources Inc. has fired a warning shot across Wichita's bow.

The current flap over the electric rate disparity issue and a subsequent blow to KGE employee morale is prompting its parent company's chief, David Wittig, to consider pulling a majority of KGE's 800 employees and its headquarters out of Wichita.

"That will be an issue for us in 1999," said Wittig, president and chief executive officer of Western Resources.

The current flap stems from the electric-rate disparity issue in which critics claim that KGE customers pay as much as 40 percent more for electricity than do KPL customers in Topeka.

Wittig said the resulting clamor in Wichita and its lasting effects have negatively impacted the morale of KGE employees in Wichita.

"I just do not, as manager of this company, want to subject the employees to this," he said. "I'm very frustrated for these employees. It just kills me."

Nowhere throughout Western's subsidiaries, he added, is morale lower than in Wichita.

And in a city where KGE employees are involved in a variety of community interests, Wittig said, "If the mayor and the people of Wichita don't want us here, maybe we should move to Hutchinson."

HOUSE UTILITIES

DATE: 2-16-99

ATTACHMENT 2

But Wichita Mayor Bob Knight takes exception to what he called Wittig's "threat."

"Threatening and intimidating are not going to change the facts," Knight said. "And the fact is (the) rate disparity ... (is) not justified."

Knight believes the rates should be uniformly spread among Western's subsidiaries, and that Western and Wittig are more concerned with shareholders than with the customers the company serves.

"He's (Wittig) spent too much time on Wall Street and not enough time on Main Street," Knight said. "They try to act like this is an intractable problem ... the solution is to quit trying to privatize the profits."

But Wittig and KGE President Annette Beck said higher rates are necessary because of where KGE's power comes from.

The "blended" rate for KGE customers -- an average of the rates charged to residential, commercial and industrial customers -- is 6.55 cents per kilowatt hour, 1.39 cents more than the blended 5.16 cents per kilowatt hour charged to KPL customers.

However, KGE's cents per kilowatt hour charge is 0.65 cents less than the national average of 7.20 cents per kilowatt hour.

KGE customers pay more, argue Western officials, because a portion of the rates they pay go toward the cost of paying for a portion of the $3 billion Wolf Creek nuclear power plant in Burlington, Kan., which began supplying KGE customers with electricity after it became operational in 1985.

And the cost to run Wolf Creek is higher because it requires more personnel to operate it than does the Jeffrey Energy Center, a coal-fired electric generation plant in St. Mary's, Kan., that provides power to KPL customers.

Wolf Creek, which generates 585 megawatts of electricity, needs 1,003 employees to operate it, while Jeffrey, with generation capacity of 2,171 megawatts, only employs 322.

Additionally, Beck said, interest accruing on the cost to build Wolf Creek also added to the difference in rates between the two utilities.

Furthermore, Wittig said that even under the Western umbrella, KGE and KPL are two separate subsidiaries operating in different areas, and as such their rates are subject to what the market calls for in those areas as well as the difference in operating costs between two separate companies.

And that practice is in line with much of the industry, Wittig said.

KGE rates are, however, expected to fall more than 2 percent following the merger, which would offer the company an estimated $950 million in savings during the next 10 years.

Knight, however, is standing firm in his efforts to encourage Western to lower KGE's rates and says it's not a personal battle he's fighting, but one on behalf of KGE customers.

"Eighty-five thousand people signed a petition, and we could probably double that," said Knight of the petition drive he launched in July to protest the rate disparity.

And although Knight is sympathetic to the low morale among KGE employees, he doesn't hold himself or Wichitans responsible.

"Somehow, it seems to me, it is his responsibility to take care of the morale of employees," he said. "That kind of attitude really goes to the heart of the problem."

Week of February ... Leading Stories | Top of the page

Updated **SATURDAY** February 13, 1999

Local

KGE threat to leave Wichita irks mayor

But Knight says "corporate blackmail" won't keep him from trying to reduce the area's electric rates.

By Lori Lessner
The Wichita Eagle

Wichita Mayor Bob Knight's vigorous pursuit of lower electric rates for south-central Kansas has prompted Western Resources to consider hitting Wichita where it's most vulnerable: its job market.

Company officials said this week they are seriously considering whether to pull most of their 800 KGE employees out of Wichita because the mayor is not making them feel welcome. Western Resources is KGE's parent company.

"Like any other business, we want to be in a community that is supportive," said Carl Koupal, the company's chief administrative officer and executive vice president.

Knight on Friday called Western Resource's threat misguided. He said it smacks of "corporate blackmail."

And it won't work, Knight added. He said he will not back off his push to end a rate disparity in which KGE customers pay about one-third more for electricity than do customers of KPL, a Western Resources company that serves northeast Kansas.

Western Resources was hoping for a friendlier response.

"We're disappointed that the first response from the mayor is what we feel is a personal attack," Koupal said. "We would hope that the mayor takes a hard look at the facts."

But Knight said "the facts" are what's fueling his push.

"I spend most of my waking hours trying to work with others on building a strong economy for the next century," he said. "Unless we can make progress on things like electric rates, we're not going to reach our potential. That's why it is important to me that I do not retreat from something like this that is absolutely critical."

It was last year that Knight began trying in earnest to get KGE's rates lowered. He led a drive in which about 85,000 people -- nearly a third of KGE's customers -- signed a petition protesting what they pay.

Later, the Wichita City Council voted to intervene in a proposed merger between Western Resources and Kansas City Power & Light Co. Because the merger must be approved by the Kansas Corporation Commission, Knight and the council saw an opportunity for regulators to order that Western use any savings from the merger to cut rates.

According to Western Resources, KGE has higher rates because its customers are obligated to pay 47 percent of the Wolf Creek nuclear power plant's building costs. The bill for the plant, which cost $3 billion to build, will not be paid off until 2025.

KGE spokeswoman Suzanne Coin said that the company does not mind debating the electric-rate disparity but takes exception to how Knight is approaching the topic. She said Knight is ignoring certain facts, most notably that KGE rates have been cut from 10 percent above the industry average to 10 percent below since merging with KPL in 1992.

As he presses his case on rates, Knight recruited several south-central Kansas legislators to his cause. A bill has been introduced that would result in shareholders, not ratepayers, shouldering certain costs of the merger. If that were to happen, the bill's proponents say, all Western Resources customers would see lower bills.

But if the bill were to pass, it would kill the merger, a Western Resources spokesman has said.

Topeka legislators immediately lined up against the bill. Western Resources executives said last summer they would move their headquarters if Topeka did not support the company. Topeka has made it clear it wants the company to stay.

Koupal said that the threats to leave Topeka and, now, Wichita were not meant as scare tactics to keep the cities from interfering in the merger. He said the company simply wants to do business in a positive environment.

He said Wichita employees told Western Resources' president, David Wittig, this week they are upset with the way Knight has been "continually attacking" the company over the rate disparity.

About 500 KGE employees work in areas such in customer service, a phone center and maintenance. The rest, about 300, work for Protection

One private security.

Koupal and Coin said it is too early to know how many workers would stay in Wichita if the company relocated, possibly to Hutchinson. Some would have to stay to respond quickly to emergencies, such as downed power lines from a storm.

As evidence that considerations are in the early stages, the company has not even contacted Hutchinson officials to discuss moving there.

Jon Daveline, president of the Hutchinson/Reno County Chamber of Commerce, said Friday that he is flattered Western Resources would consider calling the town home.

At the same time, he said, it would have to be the company's decision. Hutchinson officials would not want to strain relations with Wichita by actively recruiting the company.

Knight said the move would do nothing toward addressing the rate disparity and is meant to pit the company's Wichita employees against him.

And he said the move would add further insult to ratepayers. On top of paying more for electricity, those in Wichita would have to deal with the impact of 800 less jobs.

Tim Witsman, president of the Wichita Area Chamber of Commerce, hinted that the electric company was doing what it could to make sure it is treated as a significant player. He said the chamber will work with the company to see what can be done to keep the 800 jobs in Wichita.

He added that Wichitans should keep any possible job losses in perspective.

"It doesn't make me happy when these companies depart, but in the last few years leading up to this year ... the numbers of employees at our largest companies have increased by one-third," he said.

"Unless we can make progress on things like electric rates, we're not going to reach our potential. That's why it is important to me that I do not retreat from something like this that is absolutely critical."

"We're disappointed that the first response from the mayor is what we feel is a personal attack. We would hope that the mayor takes a hard look at the facts."

Carl Koupal, KGE chief administrative officer

Opinion

A column by Denney Clements

Electric bill has wrong focus

Regular readers of this column know that our local electricity provider, Western Resources, is not my favorite institution. They especially will be surprised that I'm taking Western's side in one of the many legislative disputes in which it's now embroiled.

This dispute concerns Western's decision last summer -- after it got really hot -- to browbeat customers into ratcheting down their electricity use. On two occasions in early summer, the company threatened south-central Kansas residential, business and industrial customers who failed to turn up their thermostats with "rolling blackouts" -- the arbitrary shutoff of electric service on a neighborhood-by-neighborhood basis.

Only several months later, as the coolness of fall set in, did the captive electric ratepayers of south-central Kansas learn why Western had subjected them to such bully-boy tactics: The company had sold off a significant chunk of its excess generating capacity to out-of-state utilities.

When it got hot, Western chose to honor those contracts rather than use its excess generating capacity -- which we paid for -- to guarantee the comfort of its own ratepayers.

One of the customers that got stiffed in this fashion was Boeing, which pays a premium industrial rate for power that supposedly can't be interrupted. It, too, succumbed to the rolling blackout threat in the belief -- erroneous, as it turned out -- that Western's capacity was strained to the limit (a belief that Western did nothing to discourage).

So you can't blame Rep. Don Myers, R-Derby, the chairman of the House Utilities Committee, for proposing a bill that would bar Kansas utilities from selling power out of state when they can't meet the needs of their own customers. Indeed, I get so aggravated thinking about what happened last summer that a bill to put Western generators under control of the Kansas National Guard almost makes sense to me.

But the better, more rational side of my nature understands that the root problem here can't be fixed with legislation further restricting how electric utilities do business.

As one Western spokesman rightly told the utilities committee this week, such a law would drive electricity costs even higher while increasing the risk that rolling blackouts could become a way of life in the summertime. If Western were barred from selling power out of state, utilities out of state would refuse to sell their spare power to Western in times of extreme heat. This knife cuts both ways.

A better course for Mr. Myers -- one that also would cause him and like-minded legislators to butt heads with Western's phalanx of exquisitely attired lobbyists -- would be to develop legislation to force utilities to compete for business here at home.

Retail wheeling, as electric competition is formally known, is another hot dispute. Western is willing to allow competition into its own backyard only on terms that would make it virtually impossible for outside electric utilities to operate profitably in Kansas. And it has lobbied hard to keep retail wheeling from taking effect until well after the new century begins.

If Western had to compete for business in south-central Kansas, its execs would never dream of leaving its customers -- especially the Boeings on its grid -- stewing on 100-degree days.

They'd carefully weigh their power-sharing responsibilities against their responsibilities to their customers. And utilities with generating capacity to spare would market it directly to customers -- particularly on the industrial side.

In time, rolling blackout threats would cease to exist because there'd *be* no shortage of generating capacity. Just as it has with the Internet and long distance, competition would bring new capacity into being.

Mr. Myers and his counterpart at the Senate's utilities committee, Sen. Pat Ranson, R-Wichita, know all this. If he really wants to make Western more accountable to its customers, Mr. Myers should focus on getting something done on retail wheeling this year.

And Ms. Ranson should help.

Mr. Myers' bill seems aimed at making us feel more comfortable about our electric bondage. What we really need is legislation that blows our shackles away for good.

Readers can reach Denney Clements by e-mail at dclements@wichitaeagle.com or (316) 268-6261.

TESTIMONY SUBMITTED TO
THE HOUSE UTILITIES COMMITTEE

By
Mr. Earl Watkins, General Counsel
SUNFLOWER ELECTRIC POWER CORPORATION

February 15, 1999

COMMENTS ON HOUSE BILL 2025

Thank you, Mr. Chairman and members of the Committee, for providing Sunflower time to share our thoughts with you on this important legislation. My name is Earl Watkins. I serve as Sunflower's legal counsel and have done so for more than 20 years.

Before I discuss several specific matters contained in this legislation, I want to provide you with two important general points about Sunflower's position regarding any retail wheeling legislation.

First, Sunflower is, and always will be, opposed to any construction of the law that may increase the cost of electrical service to our consumers in rural western Kansas. It is easy to get so bogged down in the details of a large issue like this that we sometimes forget to consider that most important question, "Will this change result in lower costs or better service to the retail consumer?"

We continue to be concerned that while some believe that Kansas will be a "net winner" in a competitive electricity market, they also predict that there will be winners and losers. Our concern is that, in the marketplace, rural people are generally the losers.

Many believe that competition affords customers greater choice in the products they purchase. History shows us that is just not the case for people living in rural Kansas. Only 316,000 people live in the 46 counties that comprise the western 48% of Kansas. That is compared to the 2.3 million Kansans that live in the other 52% of the state. If you were marketing a product, how much of your time would you allocate to western Kansas? We urge the Committee to recognize that rural areas of the state are different

HOUSE UTILITIES
DATE: 2-16-99
ATTACHMENT 3

from urban areas and may not benefit from retail wheeling unless consideration is given to the unique characteristics of the rural areas in Kansas.

I won't burden you with details, but most people I know do not believe that the recent changes that brought competition to the airlines, to cable TV, and many other industries, have resulted in lower costs and better service to the general public.

The best evidence of this is the fact that, as most of you know, the price for deregulated wholesale power skyrocketed last summer as a series of unfortunate events across the Midwest saw the price of non-firm power jump from $20 to nearly $10,000 per MWh. In Illinois, had costs reflected in the market been passed through to retail consumers as the free market would normally do, the average residential bill for June 1998 would have been $5,000. Can you imagine the hardships, not to mention the phone calls, that such bills would cause in Kansas?

Some may say that I am wrong by arguing that the free marketplace would produce benefits for everyone. That is a debate that could last long into the night, but I think it would only result in one obvious conclusion: *the time to open the retail electric market to competition has not yet arrived.*

With this in mind, and with an eye toward protecting all areas of the state, we urge the Committee to insert language in the legislation to prohibit any increase in the total delivered cost of power to residential and small business consumers in Kansas. In our view, if this Legislature cannot provide this guarantee to the smallest among us, Kansas has no business tinkering with the existing system. On the other hand, if you can find a way to provide this protection, then we say, "Let the games begin."

Even though we have serious concerns about electric utility restructuring, we believe the Legislature will ultimately implement some form of retail choice, so I would like to speak to the issue of universal service. Some have argued the language contained in Section 10 is not appropriate. We disagree with that view. Most studies agree that rural people will see increasing costs as a result of retail wheeling. The universal service language in the HB 2025 will provide residential consumers and small business owners in rural Kansas some degree of protection. We ask for your support for universal service because it is a matter of critical importance if we are to maintain the rural infrastructure to those living in low population density, high-cost distribution service areas in Kansas.

Our second important point deals with Sunflower's financial condition. As you know, the overwhelming majority of our debt obligations are to the federal government. Because of the legal obligations accompanying that debt, Sunflower cannot support any element of this legislation that fails to provide a mechanism for the repayment of our federal debt obligations. To do otherwise could put Sunflower's officers and board members in violation of federal laws and subject each to personal liability.

Should you decide to move this legislation, Sunflower could support the basic implementation schedule identified in Sections 4 and 6 if our rural consumers are afforded the protections we've described. However, we believe careful study is required to make sure all of the underlying changes that need to be made to prepare for competition can be achieved in time for the implementation date of July 1, 2002. To us, this looks like a daunting task to achieve in a very short period of time.

We continue to be concerned with the intermingling of the transmission and distribution elements of the bill. While these two segments of the business are anticipated to remain regulated, the regulatory scheme for transmission operations is different from that involved in the regulation of distribution systems. To illustrate this point, consider the different organizational structures of utilities in Kansas. The investor-owned companies are vertically integrated to include generation, transmission and distribution. Sunflower and KEPCo provide only generation and transmission services where our individual member systems provide distribution services. In certain cases, there are distribution cooperatives that also provide transmission service in their individual systems as well.

We ask that you modify the current bill to distinctively separate its transmission and distribution elements. We believe that due diligence at this point in the process may well save the Kansas consumer considerable expense resulting from legal arguments in the future over the intent of this legislation on these important issues.

Section 7 deals with the determination of recoverable competitive transition costs (CTCs). Given our unique financing structure, we advocate a provision whereby cooperatives could seek a final determination of its CTCs from the Kansas Corporation Commission (KCC) in order to develop a restructuring plan for their debt obligations with the federal government. In our view, this is the only way Sunflower can honor its allegiance to its consumers and its duties to its creditors. We propose that the following language be added as Section 7(f):

> *For purposes of restructuring their federal debt obligations, electric cooperatives, including generation and transmission cooperatives, may request a final determination of their CTCs. The KCC's determination will be finalized within 240 days of an applicant's filing.*

We are also concerned with the amount of cost that would result from the proposed 12-year ongoing review of this process. It seems to us that once the KCC determines the appropriate amount of CTCs, it becomes a simple matter of calculating the "per kWh" charge and collecting the approved amount per kWh until the total amount is fully collected. If the total amount is not collected in 12 years, the revenue stream would end. To involve the KCC after the initial approval process seems to us to be imposing unnecessary costs on the consumer and uncertainties for other stakeholders.

Finally, we are concerned that consumers who choose new suppliers may not be inclined to remit these CTC charges to their original supplier. We advocate that the local distribution utilities be charged with collecting the CTCs and remitting them to the KCC for distribution.

Section 15 deals with the standards of conduct for transmission and distribution utilities. We believe this section needs to be re-organized to recognize that the cooperative utilities could not possibly comply with the standards of conduct specified in this section. We don't argue with the concept of establishing standards of conduct, but we certainly don't think they should be organized in a way that fails to recognize the difference between cooperatives and other forms of utility structures.

One last point. Let's make sure that as you consider this legislation, you don't impose a plethora of new ongoing responsibilities for the KCC. Every new responsibility you legislate on this agency equates to a new cost on the Kansas consumer. Every new requirement you impose on us as deregulated utilities will be a cost the consumer will ultimately pay for.

I ask the Committee, as you continue to deliberate this vitally important issue, to not lose sight of the fact that a new, deregulated power industry just might end up like the cable industry with its higher rates, or like the unfortunate thousands of passengers on the deregulated American Airlines who found themselves stranded in airports all across the country just last week. Deregulation is not necessarily a solution that will benefit the Kansas ratepayer.

Thank you Mr. Chairman for the time to share our views with the Committee. We look forward to working with you on this very important issue. I would be happy to answer any questions.

TESTIMONY OF JON K. MILES

Director, Governmental Relations and Administration
Kansas Electric Cooperatives, Inc.

on
HB 2025

Submitted to the House Utilities Committee

Vice Chairman Sloan and members of the Committee, I am Jon Miles, Director of Governmental Relations and Administration for Kansas Electric Cooperatives, Inc., the statewide association for the state's twenty-nine distribution rural electric cooperatives and two generation and transmission cooperatives. These systems provide power to more than 300,000 Kansans in 103 counties with electricity being moved over nearly 65,000 miles of line. The rural electric cooperatives' territory serves about 80% of the landmass in Kansas. Cooperatives are organized under Kansas law as non-profit member-owned corporations.

I appreciate the opportunity to appear before the House Utilities Committee to continue the dialogue on the restructuring of the electric utility industry. In the course of the last three years, this committee has done much to increase its understanding of a very complex industry. Not only have these hearings demonstrated the degree to which the electric industry is changing, but they have also reinforced the importance of providing reliable, affordable electric service to each and every family and business in the state of Kansas. We appear today to support the effort of the Retail Wheeling Task Force that you have before you in the form of HB 2025, and to again express our concern that retail wheeling may not be good for Kansas, particularly rural Kansas.

Electric cooperatives want to ensure that any changes made to the electric utility industry benefit all consumers, including those that live in rural Kansas.

HOUSE UTILITIES
DATE: 2-16-99
ATTACHMENT 4

Rural electric cooperatives serve rural Kansas—the most sparsely populated, rugged, difficult-to-serve areas in the country. As a former distribution manager, I remember attempting to service lines along roads in rain-swollen areas near creeks and rivers. Rivers ran out of their banks and high waters made it difficult to replace a washed out pole. In addition, I cannot forget what it is like to live in rural areas when an ice storm decides to make things a little rough.

In Kansas, electric cooperatives serve nearly 70 percent of the rural households today. The remaining 30 percent is made up of small business, commercial/industrial, irrigation and some seasonal loads, i.e., cabins, etc. The fact that we serve predominately residential and small business consumers in rural areas defines our priorities in the debate about restructuring. Changes made to how the electric utility industry is regulated, either at the state or federal level, must bring real benefits to rural, residential and small business customers, too. Rural electric cooperatives stand ready to support legislation that would bring benefits to all our customers.

In 1996, the rural cooperatives in Kansas took a seat at the Retail Wheeling Task Force. We saw this as an opportunity to participate in the debate on this very important issue. During the course of the exhaustive and lengthy task force meetings, the rural electric cooperatives did their homework. KEC, Sunflower, and KEPCo commissioned a study by the Docking Institute at Fort Hays State University to understand the potential price and service impacts of retail wheeling. In short, the study showed that while some areas of the state would benefit, most rural areas would be adversely affected. The study covered rural electric territory in all four corners of the state.

Another rural electric cooperative study was recently completed in South Dakota. The information was just released on January 14. The study was prepared by the University of South Dakota Business Research Bureau. The study showed that residential users who consume 71 percent of the power distributed by the state's electric cooperatives could see an average rate increase of $61 per year, costing consumers nearly $6 million. The study showed that residential customers will see increases in the cost of power.

The Retail Wheeling Task Force produced the bill that is before you today. While we do support the work of the Task Force, we believe we must answer the question of whether this bill will result in lower costs or better service. One provision in the bill that will help alleviate the problems associated with serving in rural areas is the provision for a universal service fund. This fund is a mechanism to recognize the high cost of serving customers in rural Kansas. This fund would offer some protection for customers whose rates exceed the statewide average by 25%. The debate over this provision in the bill was extensive, and, like many of the provisions in the bill, was the result of compromise among the many participants at the task force.

For example, as we heard yesterday, the tax changes resulting from retail wheeling could have a $30 million impact on the state. The interim Senate and House Committee met during the summer months to discuss this issue, but no recommendation has come forward as to how it might be addressed. Section 26 in HB 2025 calls for a joint committee to study, investigate and analyze the ramifications to the tax issue. While this is a good idea, we feel that the tax issue needs to be addressed before retail wheeling bill is passed.

Another issue is the uncertainty regarding system and service reliability. The task force dealt with some extremely complex issues and how they might be treated. The bulk of these issues were left in the air, with the KCC left to sort out the details. For example, the cold weather rule was discussed at length. There were questions as to whether or not this program should be continued in a competitive environment.

It is true that this bill represents a great deal of time and effort from Legislators, utility representatives, commercial and industry, and residential consumer input. It has been stated that no one got everything they wanted in the bill, nor does everyone like the bill. However, it may be the most consumer-friendly bill that we have seen so far.

We believe that Kansas has been wise to wait for other states to work out some of the problems associated with retail wheeling. It has been to our advantage to watch the work and progress of other states over the last couple of years. So far, we have seen some marketers pull out of states because the interest or savings promised simply weren't there. In other states where legislation allows competition, Legislators have had to go back and work out problems associated with the shortage of tax revenues caused by the need to level the playing field for utilities and marketers.

I want to thank you, Mr. Chairman and Members of the Committee, for continuing this dialogue on a very important subject. On behalf of the rural electric cooperatives of Kansas, let me thank the committee for its willingness to deal with this topic thoughtfully and carefully.

LEGISLATIVE TESTIMONY

Kansas Chamber of Commerce and Industry

web: www.kansaschamber.org

835 SW Topeka Blvd. Topeka, KS 66612-1671 (785) 357-6321 FAX (785) 357-4732 e-mail: kcci@kansaschamber.org

HB 2025

February 16, 1999

KANSAS CHAMBER OF COMMERCE AND INDUSTRY

Testimony Before the

House Committee on Utilities

by

Terry Leatherman
Executive Director
Kansas Industrial Council

Mr. Chairman and members of the Committee:

My name is Terry Leatherman. I am the Executive Director of the Kansas Industrial Council, a division of the Kansas Chamber of Commerce and Industry. Thank you for this opportunity to briefly comment on HB 2025.

The Kansas Chamber of Commerce and Industry (KCCI) is a statewide organization dedicated to the promotion of economic growth and job creation within Kansas, and to the protection and support of the private competitive enterprise system.

KCCI is comprised of more than 3,000 businesses which includes 200 local and regional chambers of commerce and trade organizations which represent over 161,000 business men and women. The organization represents both large and small employers in Kansas, with 47% of KCCI's members having less than 25 employees, and 77% having less than 100 employees. KCCI receives no government funding.

The KCCI Board of Directors establishes policies through the work of hundreds of the organization's members who make up its various committees. These policies are the guiding principles of the organization and translate into views such as those expressed here.

The members of the Kansas Chamber believe in free enterprise. As a result, KCCI supports moving the generation of electricity from rate regulation to open competition. Injecting free enterprise

HOUSE UTILITIES

DATE: 2-16-99

ATTACHMENT 5

in e sale of electricity holds the promise of the power of competition positively affecting the co electricity and promoting marketplace innovation.

With its support for free enterprise as its foundation, the Kansas Chamber would have several concerns regarding HB 2025.

- At the heart of KCCI's support for retail electric competition is the belief that open competition will benefit all Kansans, not just business and industry. Reliable and affordable electricity for all consumers in the state must be maintained in a deregulated system. However, KCCI believes the creation of a universal service fund for the purpose of subsidizing electric rates in a given region of the state is tantamount to regulation, and should not occur.
- Competition cannot occur without a level playing field. KCCI is concerned that the key issues of tax relief for our Kansas based utilities will continue to be the subject of debate in a special committee created by this bill, while market competition is being initiated.

Thank you for considering KCCI's comments regarding HB 2025, and for advancing our state's efforts to prudently move from rate regulation to competition for electricity. I would be happy to answer any questions.

KEPCo
Kansas Electric Power Cooperative, Inc.
A Touchstone Energy℠ Partner

Testimony on House Bill 2025

Before the House Utilities Committee -- February 16, 1999

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

From the beginning of the debate over retail wheeling, KEPCo has been cautious. We've expressed concern that there was more potential for risk than reward and that rural customers have often been the losers in other industry restructurings. We've stated our belief that a market rate doesn't automatically mean a lower rate and questioned whether there will be competition in rural areas of the state over the long run.

With that in mind, the KEPCo Board of Trustees adopted the following policy back in 1996: *KEPCo opposes retail wheeling in Kansas, unless it can be conclusively shown that such a policy will provide reliable electric service at a reasonable price for the people, business and industry of rural Kansas.*

That doesn't mean we've been a roadblock, instead we have been active in the process. KEPCo was proud to have been a part of the work of the Retail Wheeling Task Force and we worked with other task force members to find language that might protect rural consumers.

It is interesting to note that the accomplishments of the Retail Wheeling Task Force which produced H.B. 2025 are still leading a pack of states exploring this topic--in fact we've done more work than some of the states which have been headlining the retail wheeling debate.

- Oklahoma has approved the implementation of retail wheeling but left many decisions to be determined through a series of task force studies. In fact, some of those decisions were deemed important enough, such as a fair and equitable tax policy, that without a resolution the original law says retail wheeling should be delayed.
- Colorado set up much the same study structure as Kansas, appointing a 30-member task force to examine the impact of retail wheeling and a report is due to the Colorado Legislature in the fall of 1999. Colorado also commissioned an independent study similar in scope to the McFadden/RDI study authorized by the Kansas Task Force, a draft of which is due July 1.
- Nebraska has established a task force and advisory board that is meeting regularly to review restructuring issues and has decided not to support any legislation in 1999.
- In Missouri, a joint interim committee has been studying the issue for two years and is not recommending action in 1999 to restructure the industry. They do hope to focus on tax related matters this year.

Therefore, KEPCo still believes that Kansas need not hurry to make retail wheeling news. The Task Force developed an understanding of many complex issues and addressed

HOUSE UTILITIES

DATE: 2-16-99

ATTACHMENT 6

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them in H.B. 2025. At the same time, many other decisions were turned over to the Kansas Corporation Commission for its management. Everyone is interested in learning more from states like California and Pennsylvania as they push forward--we can examine the impact on rates, how to implement an effective customer education program, reliability issues, and tax implications of making a switch to the competitive market.

H.B. 2025 includes many provisions that are consumer friendly, good for rural electric distribution cooperatives, and should be protected in final legislation. Those key issues include a retail wheeling option, protection of service territory and no-by pass, plus REC consumers could benefit through a universal service mechanism.

On the other hand, retail wheeling impacts electric cooperatives like KEPCo much differently. KEPCo is a generation and transmission cooperative which has served the wholesale power needs of our member RECs for more than 20 years. While this legislation provides no assurance of our future, KEPCo is working to prepare for competition in generation services. As you heard earlier in the session, KEPCo implemented a ten percent rate decrease to our member cooperatives at the end of 1998 and we are working on further strategies to change and grow.

Before that, at least one significant issue must be addressed, the recovery of stranded costs from our investment in the Wolf Creek Generating Station. We are concerned because as a generation and transmission electric cooperative, KEPCo doesn't have stockholders. Therefore, this bill leaves current customers of the distribution cooperatives alone to absorb KEPCo's stranded costs. There is a solution to this problem but one that the Legislature probably can't influence--KEPCo must be successful in negotiations with the Rural Utilities Service to restructure its debt. Otherwise, we face a customer revolt if KEPCo is forced to compress from 20+ years to twelve, the collection of $220 million in debt while at the same time making customers face the risk and irritation of a new market environment.

KEPCo is also concerned about the regulatory review demanded by this statute, however, our concern is not so much in the amount of review but who is responsible for the costs of implementing competition. According to the fiscal note included with the Retail Wheeling Task Force report, the KCC would have to immediately boost its staff by four; in the second year to an equivalent of eleven staff or consultants; back to nine in the third year; and to three permanent new employees thereafter. The cost just to write new rules is estimated to be $2.6 million in the first three years alone. These costs are covered by assessments on KCC regulated utilities. Therefore, a utility not currently operating in the state, but poised to enter a competitive Kansas, will not be subject to the costs to develop rules and other safeguards necessary to restructure regulation of the industry.

Meanwhile, there are several steps that can be taken to lay the groundwork, some of which may be addressed in the next year or two such as the amendments to the siting act and recommendations on tax adjustments which will place native electric utilities in a competitive position.

At this time, KEPCo believes that action on retail wheeling is premature but when the time is right, H.B. 2025 will be an excellent launching pad.

Testimony
before the
HOUSE UTILITIES COMMITTEE
by
Jim Ludwig, Senior Director, Regulatory Affairs
Western Resources
February 16, 1999

Chairman Holmes and members of the Committee:

HB 2025 would implement a restructuring process for a transition to retail wheeling. This is the same bill that the Task Force on Retail Wheeling submitted to the legislature last year, except the milestone dates have all been moved back one year. Competition in the generation segment of the electric business would begin July 1, 2002. Jim Martin of Western Resources was a member of the task force.

Part of the task force report was a position statement signed by nine members. Jim Martin signed the statement on behalf of Western Resources. The statement says that the time is not yet right to pass retail wheeling legislation in Kansas because information on critical issues is not yet available. In preparing my testimony, I have tried to contact each of the nine signatories of the statement to ask whether they thought the information was now in hand. The consensus is that the statement is as true today as it was when they signed it. Several of the task force members (or their representatives) are testifying on HB 2025 to state their positions in their own words.

Western Resources believes the statement is still relevant and that it is not yet the right time to implement retail wheeling in Kansas.

We made comments before the task force on many issues. Some of the most important issues to us included:

- the opportunity to recover stranded costs (the difference between expected market prices and the amount recovered under regulation);
- securitization (a financial instrument that may be used to mitigate stranded costs);
- bill unbundling (separately itemizing generation, transmission, distribution and tax components of the monthly bill); and
- tax reform.

We also believe that implementation in Kansas ought to be contingent upon resolving a transmission issue relating to the use and allocation of existing transmission system resources. Since transmission systems are interconnected over several state boundaries, this issue must be addressed by either Congress or the Federal Energy Regulatory Commission (FERC). Although it is likely that the transmission function will remain regulated, it is imperative that existing transmission system resources be used to their maximum extent.

Some argue that the capacity shortages of this past summer would have been averted if generation

HOUSE UTILITIES
DATE: 2-16-99
ATTACHMENT 7

had already been deregulated. Others argue just the opposite, that the crises of the summer should be a clarion call against retail wheeling. I believe both arguments are too facile. But the events of the summer are instructive.

During the capacity shortages of this past summer, there were critical times when we could arrange to buy power, but regional transmission pool operators and individual transmission owners curtailed the transactions because of transmission constraints. Even firm purchases were cut off. We believe many of these transactions could have been done if transmission operators would have implemented more flexible line loading relief procedures. FERC is grappling with this issue. In fact, last Thursday I attended a FERC meeting with state public utility commissioners in St. Louis to discuss independent system operators (ISOs) and other types of regional transmission operators. These issues can only be resolved by FERC or, if necessary, Congress. For better or worse, these transmission issues fall under their purview, not the states'.

Until the transmission problems are resolved, it is not prudent to implement retail wheeling in Kansas. Retail wheeling is meaningless if electricity cannot be delivered. Transmission curtailments this past summer were a leading factor, among several, in the capacity shortages and record price spikes for power.

Our retail electric customers were insulated from these price spikes because they take service under regulated retail prices. If our customers had been exposed to market rates as high as $3.50/kWh, as we were at wholesale, their bills would have been many times higher than any they have ever experienced. Running an air conditioner for just one day at those prices would have cost a residential customer between $140 and $245. Regulated retail residential rates in Kansas today range from about 6 cents to 12 cents a kWh. Running an air conditioner on a hot day at those rates costs a residential customer $3.30 to $6.60.

Based on my experience when Western Resources still managed a natural gas business, I can attest that gas price volatility was one of the most common sources of customer bill complaints. Unlike our electric rates, the unregulated price of natural gas was recovered on customers' bills. In other words, customers paid the market price for the actual commodity of natural gas. Price variation for natural gas didn't come close to comparing to the volatility of market electricity prices during the summer of 1998, and yet customers are not tolerant of even these relatively modest price swings.

7-2

Testimony before the House Utilities Committee
In Opposition of House Bill No. 2025

By Chris Giles
Director Regulatory Services
Kansas City Power & Light Company
February 16, 1999

Mr. Chairman and members of the Committee:

I am Chris Giles, Director Regulatory Services for Kansas City Power & Light Company, and am appearing before you today in opposition of House Bill 2025 related to allowing competition in the retail sale of electric generating service.

KCPL's opposition to this proposal does not stem from a desire to maintain the status quo for our industry, but rather from the desire to bring about customer choice in the best possible manner for all stakeholders. KCPL does support customer choice, if it is done right.

Getting it right involves dealing with an incredibly large number of issues, some of which are quite controversial. The Legislative Retail Wheeling Task Force (Task Force) that developed this bill spent a considerable amount of time (36 days over 14 months) dealing with many of these issues, and for the most part did a good job. KCPL feels that this bill provides a good starting point for consideration, but needs some additional strengthening. Today, I would like to focus on three areas that need to be improved, market structure, transition costs, and taxes.

Starting with market structure, today's electric industry is composed of three basic parts, generation (where electricity is produced), transmission (high voltage wires that move electricity from the generator), and distribution (low voltage wires that deliver electricity to homes and businesses). These three parts are typically provided by a single service provider in one complete package. For competition to work well in this industry, these three parts need to be arranged differently. The generation component would be open to competition – anyone with the resources to build or buy generating plants could do so, selling electricity to anyone willing to buy it from them. To insure that suppliers have access to customers, the transmission system needs to be opened to all generators on an equal basis. The method used by states moving to a competitive electricity market to insure equal access is called an Independent System Operator (ISO). In these states, the existing transmission system is being operated by ISO's that have no financial interest in generation. The owners of transmission turn over operation control and access to their system, but not necessarily ownership. This insures that all generators have equal access to transmission.

Apart from allowing equal access to the transmission system, ISO's are tasked with many other responsibilities that are now performed by utility operators. Some of these functions include managing congestion on the transmission system, insuring reliability services such as operating reserves, scheduling transmission system repairs, and keeping the entire system in balance between the supply and demand for electricity.

As the Task Force developed this bill, it recognized the need for such an independent operator. Provisions are included in Section 21 that require the state, the Kansas Corporation Commission, and Kansas utilities to work with the federal government and other states to establish an ISO. The reason that the Task Force did not mandate an ISO is that it could only do so for Kansas, which is too small of a region. An ISO should cover as large as area as possible to maximize the ability to move electricity around a region.

KCPL firmly supports the formation of ISO's and is involved with the Southwest Power Pool and the Mid-continent Area Power Pool in their work to establish ISO's in the Midwest. Since KCPL views ISO's (or their functional equivalent) as an absolutely necessary part of a transition to retail electric competition, competition should not start until these entities are in place. Because of this, KCPL could not support any bill that does not make these entities a requirement.

The second issue that I would like to talk about today is the issue of transition costs, also known as stranded costs. HB 2025 defines competitive transition costs as

> "The amount by which the costs of all generation assets deemed prudent by the commission or by another governmental entity operating or regulating a utility and included in the utility's rate base on July 1, 1999, exceed the amount recoverable for all such assets in a competitive marketplace".

In other words, these are costs that have already been incurred by a utility to meet their obligation to serve all of their retail customers. Not only have these costs been incurred, they have also been approved for recovery by the commission, and are in rates today. When electric competition is allowed, rates for electricity will no longer be set by the commission, but by the market. Since it is expected that on average, prices will decrease with competition, utilities may be left with costs from generation assets that can not be recovered. These are transition costs.

The debate surrounding transition cost recovery has been occurring across the nation for several years. In states that now have competition, or plans for competition in place, the results of this debate have lead to allowing utilities to recover transition costs. One notable exception to this is in New Hampshire, where commission rules limit transition cost recovery in some cases. Because of these limits, the move to competition has been tied up in court for over a year and continues to be so.

As written, HB 2025 gives authority to the commission to determine how much recovery will be allowed. While is it appropriate to have the commission determine the magnitude of transition costs, utilities should be allowed the opportunity to recover the full amount. KCPL can not support any bill that does not allow us a reasonable opportunity to recover these costs.

While there are many arguments for and against transition cost recovery, KCPL feels that the legal argument supports the case for recovery best. If a law is passed that changes the structure of our industry such that KCPL can no longer recover these cost incurred and approved by the commission, then an illegal taking of property will occur. KCPL will oppose this vigorously.

The last issue that I will talk about today is taxes. The existing taxation structure related to electricity is based on a single provider of service. Because of this, allowing competition in electric service could have seriously negative implications for residents and businesses in Kansas. This potential was recognized by the Task Force and addressed to some degree in Section 26 of this bill. KCPL supports this provision to further study tax issues related to retail competition, but the bill should go father. Tax reform that insures that the state, local communities, consumers, and suppliers are not adversely affected by the move to competition must be in place prior allowing competition.

In summary, since there are unresolved issues for implementing a successful transition to retail competition, some of which will take time and effort (like the tax issue), and others that are beyond the control of the state (ISO formation), it is premature to pass comprehensive retail competition legislation in Kansas.

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

8-11