

Approved: MARCH 3, 1999
Date

MINUTES OF THE SENATE UTILITIES COMMITTEE

The meeting was called to order by Chairperson Sen. Pat Ranson at 1:30 p.m. on February 17, 1999 in Room 531-N of the Capitol.

All members were present except:
Sen. Hensley was excused

Committee staff present:
Lynne Holt, Legislative Research Department
Mary Torrence, Revisors of Statutes Office
Jeanne Eudaley, Committee Secretary

Conferees appearing before the committee:
Steve Johnson, Executive Director, Corporate Relations, Kansas Gas Service
Chris McKenzie, Executive Director, League of KS Municipalities
Louis Stroup, Jr., Executive Director, Kansas Municipalities
Barbara Hueter, Director, State Government Affairs, Enron Corp.
Larry Holloway, Chief of Electric Rates, Kansas Corporation Commission

Others attending:
See attached list

Sen. Ranson introduced the pages, who are assisting the committee today; they are from Sen. Salisbury's district. She announced distribution of information on the New Jersey restructuring bill, from Matthew Brown, who has appeared before the committee (Attachment 1). She also announced the agenda for next week, noting the committee will be able to meet Monday and Tuesday only, but will meet from 1:00 to 2:30 p.m. Monday will be spent working bills the committee has heard, and Tuesday will be a hearing on **SB 284-concerning the state corporation commission; relating to certain deliberations.**

Sen. Ranson continued the hearing on **SB 217-concerning natural gas service; providing for competition in retail sales.** The following presented information to the committee:

Steve Johnson, (Attachment 2)
Louis Stroup, Jr., (Attachment 3)
Chris McKenzie, (Attachment 4)

Mr. Johnson stated he supports the bill, but pointed out that long-term contracts would have to be reviewed and re-negotiated, making the July 1, 2002 deadline hard to meet. He also recommended utilizing pilot programs for a 2-year period, making it possible to evaluate the first year before moving on. His recommendation is to move gradually on the program. Sen. Steffes stated concern regarding the supplier of last resort and standby service which Mr. Johnson addressed in his presentation. He stated his company has received no calls requesting customer choice. Sen. Pugh asked questions regarding the unbundling issue and the fact that consumers will probably receive more than one bill.

Mr. Stroup introduced representatives from the municipals, who are supporting his testimony. Mr. Stroup emphasized local control and home rule and stated his concern with the intent of the bill is to exclude municipal gas distribution systems. He offered an amendment (which is part of his testimony) to clarify that intent. The committee discussed the proposed amendment, and Sen. Barone questioned if the bill is good for the public, why would the municipals want to be excluded? Sen. Ranson believes the municipals may "opt in", if they so desire. She stated those consumers outside the 3-mile limit are under KCC regulation and that the committee will work to clarify the language during deliberations.

Mr. McKenzie recalled the history of franchise fees and taxes, when local units of government were authorized and required compensation for the use of public property. He stressed the importance of the franchise fees, since they are financing the government entity and referred to a Research Bulletin, which is a part of his testimony. He also referred to Page 3, which is a proposed amendment, allowing cities to revise natural gas agreements, and he discussed the long-term agreements which some

CONTINUATION SHEET

MINUTES OF THE SENATE UTILITIES COMMITTEE, Room 531-N Statehouse, at 1:30 p.m. on February 17, 1999.

municipalities have negotiated. Mr. McKenzie reminded the committee that the municipals are owned and operated by its customers. They elect the governing body of their municipality, and they, in turn, operate the utility. He also stated the need for a level playing field and that he supports the Kansas Municipal Utilities' proposed amendment. The committee also discussed if the citizens could petition their municipality and ask for choice, since they own the distribution system. Mr. McKenzie warned that some municipalities have multiple suppliers. Sen. Ranson asked Mr. Doran, representing one of the municipalities in Garnett, how they find the best price and from whom; Sen. Ranson concluded that if the governmental entity does not provide natural gas to its citizen's to suit their needs, they simply vote them out of office; she also stated the municipality is then a transport only customer. The committee also discussed school districts and franchise fees. If they do not pay franchise fees, it then costs the city money.

Sen. Ranson stated there are two people who cannot attend tomorrow's meeting, who want to make brief remarks regarding the two siting bills being heard tomorrow. She introduced Barbara Hueter, who gave brief remarks regarding the bills. Sen. Ranson then introduced Larry Holloway, who also gave brief testimony on both siting bills. Their testimony will be distributed to the committee tomorrow when the hearing is scheduled. Mr. Holloway stated representatives from his office will attend the meeting tomorrow to answer questions.

Sen. Ranson announced the agenda for next week.

Meeting adjourned at 2:30.

Next meeting will be February 18.

SENATE UTILITIES COMMITTEE GUEST LIST

DATE: Feb. 17, 1999

NAME	REPRESENTING
JIM BARTLING	Greerley Gas Co / UNITED CITIES GAS
Glenn Smith	KCC
Jamy Holloway	"
Louis Stroup Jr.	KS Municipal Utilities
Richard G DORAN	City of Garnett / Kmu
Joe Dick	BPUKCA
Steve Johnson	Kansas Gas Service
Whitney Dameron	KS Gas Service
Susan Cunningham	KCC
BURTON CRAWFORDS	KCPCL
Maria Espinoza	Sen. Clinton to Kansas
MARK BURGHART	Atmos
Dave Pittman	KCC
JC Long	UCU
Tim Gullett	LKM
Angie L. Grinnell	Midwest Energy
Karen Miller	KMEA
Jim Widener	KMEA

From: "Matthew Brown" <matthew.brown@ncsl.org>
To: "Energy-l" <energy-l@ncsl.org>
Date: Wed, Feb 10, 1999 11:34 AM
Subject: new jersey restructuring bill article

A-1
(2/17)

Legislature OKs energy deregulation
01/29/99
By TRACEY L. REGAN
Staff Writer

TRENTON -- State lawmakers in both houses approved a bill yesterday opening up the state's energy markets to retail competition and requiring an across-the-board discount to utility customers for the next four years.

The Republican-sponsored legislation allows electricity customers to shop for a new supplier on Aug. 1 and calls for a 5 percent discount on utility electric rates to go into effect as soon as the markets open.

Gov. Christie Whitman, who left for Europe yesterday, plans to sign the bill when she returns next week, a spokeswoman said. When she does, New Jersey will join its neighbors in the Northeast in restructuring its electricity markets.

The bill is expected to primarily benefit large businesses that buy energy in bulk, which initiated the call for reforms several years ago. Lawmakers included the discount to protect smaller buyers, while also establishing mechanisms for them to band together in municipal buying blocks to exert purchasing power.

During the first year, the average residential ratepayer should save between \$36 and \$50 on the price of energy, consumer groups said. The discount would increase to 10 percent within three years. After the fourth year, utilities will be allowed to charge market rates. The distribution portion of the industry will remain regulated.

Businesses have been able to pick a natural gas supplier since 1994. The legislation allows residential consumers to choose at the end of this year.

THE LEGISLATION passed by wide margins in both houses, although a vocal group of Assembly Democrats assailed the bill for failing to protect consumers and the environment.

"This is based on a premise that does not exist in the real world -- that the consumer will be protected when there is competition," said Assemblywoman Nia Gill, D-Montclair, one of more than a dozen Assembly Democrats who did not support the bill. Gill argued that rather than ending a monopoly, as its supporters contend, the bill would give rise to "an unregulated monopoly."

Critics also cautioned that the bill gives too much discretion to the state Board of Public Utilities to shape important provisions, such as the amount of debt that utilities will be able to recover through rates in the newly

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Attach. 1

competitive marketplace and the level of shopping credit -- the reimbursement utility customers would receive if they decide to choose a new energy provider -- now-regulated companies would be required to provide.

The issue of shopping credits is a hotly contested one. Both business and consumer groups insist that the shopping credit be larger than the utility's avoided expenses -- including the cost of energy -- to encourage competition in the marketplace. Public Service Electric & Gas Co., the state's largest energy utility, was equally adamant that it not give what they said would be a discount larger than the one already mandated by the bill.

"I don't see how we could provide service at these higher (discount) levels. If this becomes unfairly taking of our property, then we would pursue a legal remedy," PSE&G President Lawrence Codey said earlier this month.

THE BILL leaves it to the BPU to establish a universal service fund, which would provide money for social programs and consumer education.

"Considering that the surrounding states have already started to restructure, I'm pleased to see New Jersey on this road, but this bill is skeletal in nature," said Blossom Peretz, the New Jersey ratepayer advocate, referring to the many items left to the BPU to decide.

The legislation won mostly praise, however, from the business lobby, which has long complained that energy costs in New Jersey are far higher than in other regions of the country and demanded that the state lower them -- or risk defections to other states.

Independent energy producers, including large businesses that generate their own electricity, or hope to, said they were pleased with the final version of the bill. It allows them to leave the grid without having to pay "exit fees," a portion of utility debt now being paid by all ratepayers. Only when their collective departure reached 7.5 percent of a utility's 1999 revenues would new ventures be assessed such a fee, said Steve Gabel, an energy consultant.

The bill prevents the utilities from breaking their long-term -- and in some cases above-market-rate -- contracts with independent energy producers to buy power, said Adam Kaufman, director of the Independent Energy Producers of New Jersey.

CODEY ALSO praised the bill, saying it "allows our workers a chance to compete."

"It doesn't bankrupt us, and it views our stranded costs as legitimate," Codey said, referring to the billions of dollars in investments in nuclear power plants and long-term energy contracts that the utilities do not feel they could recoup in a competitive market. The legislation leaves it to the BPU to determine how much of this debt they can continue to recover through rates, but sets no ceiling.

The bill establishes protections for utility workers who lose their jobs due to restructuring, which include benefits such as ratepayer-subsidized severance pay, medical benefits and worker training.

"The utilities had a lot of say in (the bill's) formation and they're comfortable with it," said David Schanzer, an analyst with Janney Montgomery Scott Inc. "There is no question that stock prices have been edging up in anticipation of a fair and balanced deregulation bill."

Schanzer said the legislation, which allows the utilities to refinance the majority of their debt, frees them up to "change their focus." He said he expected to see more consolidation in the industry and "major alliances in pursuit of nonregulated business."

But environmentalists said the bill was woefully lacking in funding for conservation measures, among others, and pollution protections.

It provides for a minimum of \$140 million in ratepayer-subsidized spending on energy conservation measures and funding for renewable energy initiatives, and stipulates that 4 percent of the kilowatt hours sold in the state must come from renewable power sources by 2012.

GROUPS SUCH AS the Environmental Federation, the New Jersey Public Interest Research Group and the Sierra Club were also disappointed that the bill does not establish air emission portfolio standards for energy providers that emphasize nonpolluting sources of power. Instead, it ties New Jersey's adoption of such a policy with that of neighboring states in the Pennsylvania Jersey Maryland (PJM) power pool. Critics have said it is unlikely that New Jersey's largest neighbor, coal-producing Pennsylvania, would adopt such a standard.

"The bill provides chump change for consumers and a windfall for polluters," lamented David Pringle, of the New Jersey Environmental Federation. Before the bill had even passed, he and others had begun working on amendments.

Sen. John Bennett, R-Little Silver, has said he and Sen. Diane Allen, R-Edgewater Park, will introduce legislation to increase spending on energy conservation programs and drop garbage incinerators from inclusion as a renewable energy source.

Bennett said he is also considering introducing a bill that would tie New Jersey's action on emissions standards to states such as Massachusetts and Connecticut, which have taken more aggressive positions on environmental safeguards.

Matthew Brown
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A-2-

**Testimony Before
The Senate Committee on Utilities
by
Steve Johnson, Executive Director Corporate Relations
Kansas Gas Service
February 17, 1999**

Madam Chair Ranson and members of the Committee:

Thanks again for inviting Kansas Gas Service to appear before you today. We are here to discuss the ramifications of providing our customers a choice for their gas supplier or unbundling our services to them.

Your committee has proposed SB 217 which basically requires the Kansas Corporation Commission to provide opportunities for all customers to choose their natural gas supplier by July 1, 2002. I would like to address several areas that will be impacted such as, gas purchase contracts, stranded costs, "provider of last resort" considerations, the utility's obligation to serve under current terms and conditions, administration and measurement of transportation gas, and consumers' education.

Gas Purchase Contracts

Kansas Gas Service has prudently negotiated several long-term contracts such as our Base Contracts with Amoco, Oxy, Mesa, and several other major producers. We have also entered into a contract entitled "Tight Sands" with Amoco as a result of litigation several years ago including the State of Kansas, the KCC, and Farmland Industries. Each of these contracts require review, including the possibility of renegotiation or buyout if all residential customers were allowed to choose a different supplier. Provisions regarding price and volume would become the major points of negotiation.

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Additionally, this Kansas gas sold to Kansas consumers could move to different parts of the country becoming more competitive and possibly hurt this Kansas industry in the long term.

Stranded Costs

Kansas Gas Service contracts for transportation capacity from companies such as Williams, KN, and Kansas Pipeline for all classes of customers. If, in the midst of a contracting period, a number of customers were allowed to find their own marketer who may (or may not) supply capacity, then the capacity we have for them must still be paid by the remaining customers on the system. This is included as a portion of the cost of gas and is passed along, penny-for-penny, to sales customers left on the system, unless these stranded costs are allocated to those customers opting for transportation.

Supplier of Last Resort

When customers are allowed to choose their own supplier, many considerations need to be understood regarding this ongoing service. The marketer selling them gas must be prepared to address the customers' inability to pay, the customers' desire to receive firm service, and the various options given customers today to pay their bills. Kansas Gas Service will continue to provide a system to provide any customer a safe product, its reliability may be in someone else's hands. Provisions would need to be negotiated to be able to provide gas through a contracted pipeline, possibly at spot-market prices which could have an adverse affect on the customer transporting or all other customers remaining on the system. Someone must be designated as the supplier of last resort and adequately compensated for this possibility.

Obligation to Serve

This concept is closely aligned with the supplier of last resort. Which entity will be required to uphold the "Cold Weather Rule" terms? Who will be required to serve a new customer if they are required to find their own supplier of gas? Would Kansas Gas Service still be required to follow their extensive notice and collection procedures which could include the cost of gas sold to the customer through a marketer? Who would be responsible to provide payment plans and work with collection agencies to collect overdue bills? Many of Kansas Gas Service's current general terms and conditions would have to be rewritten to accommodate a separate supplier of gas. Once the obligation to serve is distinctly allocated, inefficiencies related to collections, notice procedures, behavior modification opportunities, and other costs of service should be clearly reflected in the LDC's costs to serve, further emphasizing their high costs with low return.

Administration and Measurement

Providing this type of transportation service to all commercial customers and eventually all residential customers would be more expensive than directly selling the gas. New programming must be developed, installed and tested, contracts must be followed and enforced, customers' bills need to be revised and likely expanded to be able to explain the various portions of our bill which may include separate billing from their marketer as well. Today, most of our meters are read and billed on cycle billing, approximately 32,000 customers are billed daily. Once we allow large groups of customers their choice of supplier, new procedures will need to be implemented to read meters on different schedules, aggregation of loads and balancing will need to be offered to protect the marketer from penalty on capacity shortfalls and many customers will need to understand the process to be able to understand their bills.

Customer Education

This is probably the most important aspect of unbundling. In a truly unbundled environment the customer should be shown the true cost of each portion of his bill. The separations will likely be: a basic service charge coupled with a volumetric charge for local distribution, a reservation or capacity charge to compensate the transportation pipeline, and the marketers' costs for the gas. This education process can be very expensive and should be borne by the customer as part of the decision to give them a choice. Giving the customer proper price signals allows them the opportunity to compare Kansas Gas Service's cost of gas and transportation to those of the marketer and can also give them a better indication of savings related to conservation.

In summary, several states have begun a customer choice program on a pilot basis. If approved, Kansas Gas Service's pilot program should be for two years or more to be able to develop the procedures and rules, implement education programs, and then operate for a 12-month period analyzing as the second and possibly third years are completed. We believe opening up customer choice for all commercial and industrial customers is inevitable and will happen within the next two years with or without the KCC's urging, yet we also believe that residential customers in Kansas will save very little on their gas bills, (due to its relatively low cost today) and would happily forego the opportunity to worry about their supply of gas.

These issues and several others will be discussed at length before the Commission and at times before this Committee. Our Company is supportive of this bill once all the possible ramifications are understood.

We do not want these to be perceived as a negative response to SB 217, we are merely outlining some of the many steps which need to be taken to provide true and fair choice to our customers.

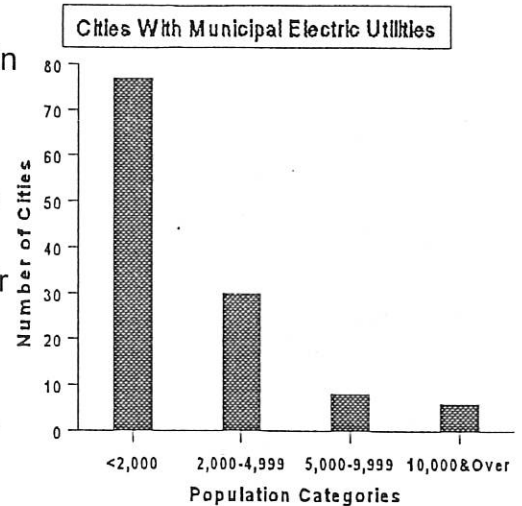
TESTIMONY ON SB 217
Before Senate Utilities Committee
February 17, 1999

Madam Chair, members of the committee, I am Louis Stroup, Jr., executive director of Kansas Municipal Utilities, Inc., a statewide association of municipal gas, electric and water cities which was founded in 1928.

Types of municipal utilities

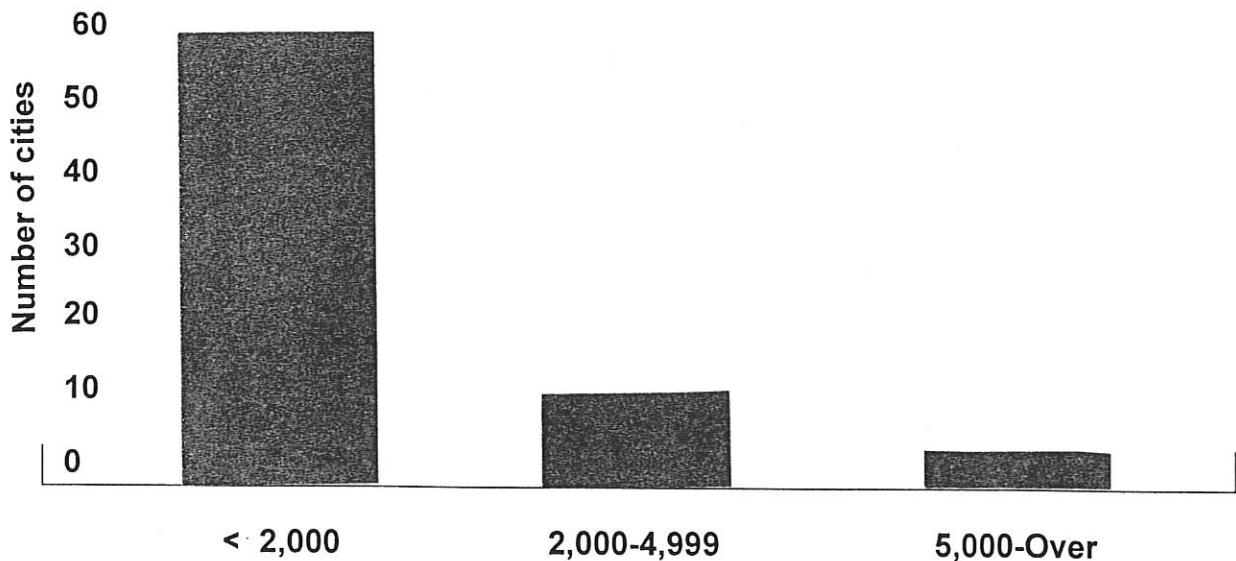
Water – a majority of the state’s 627 cities operate their own water systems.

Electric – there are 121 municipal electric cities in Kansas, representing 19% of the cities and 18% of all Kansas citizens. Most serve small cities. 77 serve cities of the third class (i.e., less than 2,000 population). Webber is the smallest of these with 39 residents, 63 of the cities generate part or all of their electric energy supplies and the remaining 58 cities purchase all of their electric energy needs.



Gas – there are 70 municipal gas distribution cities of which 83% (58) serve cities of the third class. 9 serve cities between 2,000 and 5,000 population and 3 serve cities with more than 5,000 population. Olivet is the smallest with a population of 67.

Cities with municipal gas distribution systems



Population categories

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Attach. 3

SENATE BILL No. 217

By Committee on Utilities

2-3

9 AN ACT concerning natural gas service; providing for competition in
10 retail sales.

11

12 *Be it enacted by the Legislature of the State of Kansas:*

13 Section 1. (a) As used in this section:

14 (1) "Commission" means the state corporation commission.

15 (2) "Distribution" means the business of distribution of natural gas
16 or the ownership, operation or control of distribution facilities.

17 (3) "Distribution facility" means any plant or equipment, other than
18 a transportation facility, that is used for the distribution of natural gas.

19 **(4) "Exempt utility" means a natural gas utility owned and
20 operated by municipality that provides service to retail customers;
21 provided, the governing body of any such municipality may elect not
22 to have its natural gas utility be exempt from the provisions of this**

23 **Act.**

24 ~~(4 5)~~ "Retail supplier" means a person or entity selling or offering to
25 sell natural gas at retail in this state.

26 ~~(5 6)~~ "Transportation" means the business of transporting natural
27 gas or the ownership, operation or control of transportation facilities.
28 "Trans-~~portation~~" does not include delivery of natural gas service to a
29 retail customer.

30 ~~(6 7)~~ "Transportation facility" means any plant or equipment that is
31 used for the transportation of natural gas and is under the jurisdiction of
32 the federal energy regulatory commission.

33 (b) The commission shall develop and implement a plan to allow all
34 retail natural gas customers in this state, **other than those served by an
35 exempt utility**, to select a retail supplier of the customer's choice on and
36 after July 1, 2002.

37 (c) On and after July 1, 2002, for the purposes of chapter 66 of the
38 Kansas Statutes Annotated, "natural gas public utility" does not include
39 the business of selling or offering to sell natural gas at retail.

40 (d) For all taxable years commencing on or after July 1, 2002, for the
41 purposes of K.S.A. 79-1439 and amendments thereto:

42 (1) Natural gas public utility property, whether real or personal, tan-
43 gible or intangible, includes only property subject to regulation and in-
44 cluded in natural gas public utility rate bases by the commission; and

45 (2) all other property of a retail supplier shall be considered property
46 used for commercial and industrial purposes.

47 (e) Nothing in this section shall be construed to limit or otherwise
48 affect the commission's jurisdiction, authority and duty to regulate
49 distribution as a public utility.

SB 217

2

1 Sec. 2. This act shall take effect and be in force from and after its
2 publication in the statute book.

We've been asked to do 2 things today:

- provide a profile of municipal gas cities and explain how they operate and how they differ from private natural gas operators, marketers and brokers.
- present our views on SB 217.

Assisting me will be:

Jim Widener, general manager, Kansas Municipal Energy Agency/Kansas Municipal Gas Agency, Overland Park

Ron Huxman, city administrator, Moundridge & president of KMG

Karin Miller, director, natural gas program, KMG

Rick Doran, city manager, Garnett

Many of our municipal gas distribution systems were established in small rural communities because no private firm would provide service – not unlike the development of electric service in this state where a number of cities serve outside their limits and rural electric cooperatives were founded to provide an essential service the private sector wouldn't provide.

All of the 70 cities are under the Kansas Corporation Commission for safety purposes (KCC is the agent in Kansas for the U.S. Department of Transportation). Only 21 of the 70 cities have natural gas customers outside the 3-mile limit and therefore, are also under KCC rate regulation. SB 217 would not change either of these situations.

Profile data

I have attached 2 sheets of data to provide you with a profile of many of the 70 Kansas municipal gas distribution systems. Breakdowns are shown on number of residential, commercial and industrial customers, and percentage of loads within each customer class.

Proposed amendments

It is my understanding the intent of SB 217 was not to include municipal gas distribution systems (or at least only the portion outside the 3-mile limit). We do not feel the bill's language provides that protection. **Thus, we will offer clarifying language to make sure that municipal gas distribution systems are exempt – including the portion of the 21 cities systems outside the 3-mile limit.**

Kansas Municipal Utilities, Inc.

Local control and home rule

- **Local Decisions By Local Officials.** The public is able to hold locally elected officials accountable for the operation of their community-owned and operated natural gas distribution system. No one has to travel to far-off corporate headquarters or to Topeka to resolve a dispute.
- **Accountable To Electors.** The board of directors of the municipal gas utility or the city governing body are elected and “unelected” based in part on their success in managing this important community asset.
- **Taxpayer Dividend: In-Lieu of Tax Payments and Fund Transfers.** Revenues received by municipal gas utilities represent a valuable “taxpayer dividend” in the form of in-lieu of tax payments and fund transfers which finance a host of municipal and community programs. Furthermore, the use of utility employees for general city functions significantly enhances the value of this community asset. The taxpayers in these cities would pay substantially higher property taxes if these revenues were not available to help fund these community functions.
- **Local Decisions Generally Best.** Municipal gas utilities have achieved a high level of service at reasonable costs while providing ultimate community control and benefits. In these cities, natural gas is an essential community service, not just a commodity, similar to fire and police protection, water, electricity, sewer or refuse collection.

Concerns

- Municipal gas systems have numerous concerns about being part of natural gas unbundling or customer choice. Cities should retain all existing authority to control use, excavation, and repair of municipal rights-of-way.
- Future capacity planning activities. Would be very difficult for cities if they are forced to open their systems.
- Impact on residential customers could be extremely harmful if benefits were only to flow to large industrial customers.
- Impact on small commercial customers also could be harmful if benefits were only to flow to large industrial customers.
- Rates could actually increase to the residential and commercial customers.

- Impact on safety – a very large concern – if revenues drop off because of loss of customers.
- Who is the utility of last resort?

Conclusions

Municipal gas utilities in Kansas have a proud history of serving the residents of the 70 cities with reliable, safe and affordable natural gas service. These utilities also have provided related and tangible benefits to their residents, making a lasting contribution to the welfare of their communities. Based on this track record, we respectfully submit that SB 217 should:

Provide an explicit exemption for municipal gas utilities from the Act, including all municipal gas operations outside the 3-mile limit.

Provide an "opt in" provision for cities should they chose to open their systems. This would give locally-elected officials the flexibility to do what is best for all their customers – not just large volume customers.

Prohibit bypass or cherry picking of municipal gas utility systems.

PROFILE OF KANSAS MUNICIPAL GAS DISTRIBUTION CITIES - (1997 DATA)

3-6

City	Pop.	MCF Residential	Load % Res.	Cust. Res.	MCF Commercial	Load % Comm.	Cust. Comm.	MCF Industrial	Load % Ind.	Cust. Ind.	Total Cust.	KCC Cust.	Trans. \$	Equals Mills
Abbyville	143													
Agenda	80													
Alma	842	53,622	81	472	10,452	16	75	2,176	3	3	550	43		
Alta Vista	463	32,072	59	342	21,582	40	61	0	0	0	403	187	\$ 25,000	n/a
Altamont	1030	67,023	100	507	0	0	0	0	0	0	507	0	\$ 25,000	9.72
Argonia	523													
Attica	649	28,798	64	304	10,432	25	58	4,446	11	3	365	0		
Auburn	1032	74,994	65	815	39,639	35	49	0	0	0	864	330	\$ 21,050	6.7919
Aurora	93											22		
Belleville	2394	99,904	60	1,136	41,198	24	165	17,448	10	7	1308	10	\$ 23,000	3.06
Bunker Hill	112													
Burlingame	1096	49,328	62	493	18,160	23	66	0	0	0	559	29		
Burrton	858													
Cassoday	99													
Chanute	9248	385,945	62	3,933	165,008	26	506	75,499	12	69	4,508	0	\$ 549,960	n/a
Cheney	1683	46,542	67	548	23,380	33	73	0	0	0	621	0		
Coats	130	6,615	92	59	435	8	1	0	0	0	60	0		
Denison	211	13,136	90	151	1,433	10	9	0	0	0	160	43		
Eskridge	495	48,569	47	588	54,268	53	71	0	0	0	659	364		
Ford	274	20,187	48	124	21,870	52	14	0	0	0	138	0	\$ 2,000	n/a
Garden Plain	769	34,683	95	266	1,916	5	31	0	0	0	297	13		
Garnett	3244	139,792	67	1453	39,065	18	193	30,947	15	32	1,678	0		
Halstead	2010	57,274	45	639	45,621	35	80	26,329	20	11	730	0	\$ 50,000	4.5
Hamilton	314	10,736	72	143	4,214	28	18	0	0	0	161	0		
Hardtner	195													
Harveyville	254	9,878	79	142	2,686	21	19	0	0	0	161	1		
Havensville	147													
Hazelton	125													
Hesston	3586	73,808	24	873	44,824	15	108	189,081	61	9	990	0	\$ 58,000	3.33
Howard	827	38,805	84.9	408	7,039	15.1	60	0	0	0	468	0	\$ 67,000	1.4
Hudson	156													
Humboldt	2139	68,659	80	761	17,165	20	91	0	0	0	852	0	\$ 75,000	20
Iola	6241	224,515	43	2,434	124,607	24	424	174,401	33	4	2,862	0	\$ 140,000	7.4
Isabel	100													
Jamestown	307	21,378	91	183	2,114	9	11	0	0	0	194	34		
Kechi	831	25,322	51	313	24,325	49	34	0	0	0	347	0		
LaCygne	1206	35,035	52	428	12,524	19	50	19,777	29	3	481	35		

PROFILE OF KANSAS MUNICIPAL GAS DISTRIBUTION CITIES - (1997 DATA)

4-7
B-7

City	Pop.	MCF Residential	Load % Res.	Cust. Res.	MCF Commercial	Load % Comm.	Cust. Comm.	MCF Industrial	Load % Ind.	Cust. Ind.	Total Cust.	KCC Cust.	Trans. \$	Equals Mills
Lancaster	298													
Lebo	911													
Little River	478	21,996	71	230	9,195	29	43	0	0	0	273	0	\$ 25,000	n/a
Longford	66	3,086	54	39	2,654	46	11	0	0	0	50	6		
Louisburg	2230	59,859	65	663	32,232	35	101	0	0	0	764	0	\$ 30,000	3.23
Lyons	3550	153,613	67	1,578	70,500	31	215	3,155	2	4	1,797	0	\$ 84,500	8.1
McFarland	220													
McLouth	785	32,001	89	376	4,008	11	32	0	0	0	408	0		
Milford	511											69		
Moundridge	1541	47,839	50	560	29,723	31	74	16,019	17	17	651	0		
Mulberry	587		93			7			0		330	10	\$ 11,000	n/a
Neodesha	2765													
Neosho Rapids	249	8,499	80	116	2,151	20	8	0	0	0	124	0		
Norwich	460											74		
Offerle	220													
Olivet	67													
Osage City	2940	119,037	64.4	1,226	36,374	19.7	141	6,066	3.3	1	1,369	0	\$ 45,000	3.57
Palmer	117											3		
Partridge	222													
Pawnee Rock	347											2		
Reading	272													
Rozel	180											13		
Sawyer	188													
Sharon	254													
Spearville	753											9		
Stark	80													
Sylvia	313	13,947	60	147	9,630	40	21	0	0	0	168	0		
Uniontown	300	13,181	68	164	6,233	32	14	0	0	0	178	3	\$ 10,000	13.58
Viola	211													
Walton	230	8,730	55	109	7,324	45	14	0	0	0	123	2		
Wetmore	284													
Windom	135	5,191	60	56	1,683	19	11	1,861	21	4	71	0		
Winfield	11804	440,000	55	4,520	172,000	21	500	190,000	24	33	5053	0	\$ 190,741	4.18
TOTALS		2,593,599			1,117,664			757,205			31,282	1,302	\$ 1,432,251	

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PUBLISHERS OF KANSAS GOVERNMENT JOURNAL 300 S.W. 8TH TOPEKA, KS 66603-3896 (785) 354-9565 FAX (785) 354-4186

TO: Senate Utilities Committee
FROM: Chris McKenzie, Executive Director
DATE: February 17, 1999
SUBJECT: SB 217

Thank you for allowing me to testify today on behalf of the League of Kansas Municipalities and our 529 member cities. The issue of retail competition in the sale of natural gas is an important issue and you are to be commended for undertaking it.

Because we believe that the question of whether retail competition should or should not be allowed for all Kansas consumers is a major policy question which can only be answered by the state Legislature, the League does not have a specific position on SB 217. However, there are certain aspects of this issue which are of great concern to Kansas cities.

Control of Rights-of-Way

The current franchise laws (K.S.A. 12-824, K.S.A. 12-848, and K.S.A. 12-2001 et seq) recognizes that cities must maintain control over facilities which are placed in the public rights-of-way. In fact, K.S.A. 12-850 makes it unlawful for anyone to use public rights-of-way without a franchise grant from the city.

Most franchise agreements adopted under these statutes are long-term (up to 20 years) in nature and prescribe methods of conduct by which utility companies must act (e.g., procedures for digging, cutting curbs, safety precautions, etc.) It is imperative that cities maintain this authority in a competitive environment as well.

Franchise Fees

K.S.A. 12-2001 requires that "adequate compensation" be paid to the city for the use of the rights-of-way. This franchise fee not only compensates the city for the use of public property, but also has come to be an important part of the revenue mix in cities which do not operate their own gas utility. The fee is generally computed on a gross receipts basis and is imposed at a rate of 2-5%. SB 217 would allow retail customers to purchase natural gas from a supplier other than the local distribution company (LDC). Most existing franchise agreements were not written to capture the fee when the gas is supplied by an entity other than the LDC.

This is a problem which must be remedied prior to the implementation of full retail choice with respect to natural gas. Because existing agreements would not impose a franchise fee on gas supplied by an entity other than the LDC, cities would experience significant revenue losses. In many cases, the only source of alternative revenues to which cities can turn is the property tax. Further, customers would have an economic incentive not to choose the LDC to provide their energy since the franchise fee would still be imposed if the LDC was the supplier.

Senate Utilities
2-17-99
Attach. 4

Envisioning a future which includes retail competition for natural gas and electricity, some cities have already begun to renegotiate their franchise agreements and convert their franchise fee calculation from a gross receipts-based formula to a volumetric one. I have attached Research Information Bulletin No. 648 which demonstrates what some cities have done in this respect.

In order to assure that LDCs are not put at a competitive disadvantage and to assure that cities are able to collect a franchise fee on all natural gas which is transported using the city rights-of-ways, we recommend that the commission be directed to develop a plan which ensures that local franchise fees are paid on all gas consumed, notwithstanding the supplier of the natural gas. A suggested balloon with these amendments is attached.

The League will work with cities and with the KCC to make certain that we resolve the franchise fee issue prior to the implementation of retail natural gas competition.

Municipal Gas Utilities

There are 70 municipal gas distribution cities in Kansas. These utilities are operated by locally elected officials and serve as a significant revenue source in those communities. The League supports local control of these systems and supports the opt-in amendment offered by Kansas Municipal Utilities.

Thank you for your consideration of these concerns. We appreciate this opportunity.

SENATE BILL No. 217

By Committee on Utilities

2-3

4-3

9 AN ACT concerning natural gas service; providing for competition in
10 retail sales.

11

12 *Be it enacted by the Legislature of the State of Kansas:*

13 Section 1. (a) As used in this section:

14 (1) "Commission" means the state corporation commission.

15 (2) "Distribution" means the business of distribution of natural gas
16 or the ownership, operation or control of distribution facilities.

17 (3) "Distribution facility" means any plant or equipment, other than
18 a transportation facility, that is used for the distribution of natural gas.

19 (4) "Retail supplier" means a person or entity selling or offering to
20 sell natural gas at retail in this state.

21 (5) "Transportation" means the business of transporting natural gas
22 or the ownership, operation or control of transportation facilities. "Trans-
23 portation" does not include delivery of natural gas service to a retail
24 customer.

25 (6) "Transportation facility" means any plant or equipment that is
26 used for the transportation of natural gas and is under the jurisdiction of
27 the federal energy regulatory commission.

28 (b) The commission shall develop and implement a plan to allow all
29 retail natural gas customers in this state to select a retail supplier of the
30 customer's choice on and after July 1, 2002.

31 (c) On and after July 1, 2002, for the purposes of chapter 66 of the
32 Kansas Statutes Annotated, "natural gas public utility" does not include
33 the business of selling or offering to sell natural gas at retail.

34 (d) For all taxable years commencing on or after July 1, 2002, for the
35 purposes of K.S.A. 79-1439 and amendments thereto:

36 (1) Natural gas public utility property, whether real or personal, tan-
37 gible or intangible, includes only property subject to regulation and in-
38 cluded in natural gas public utility rate bases by the commission; and

39 (2) all other property of a retail supplier shall be considered property
40 used for commercial and industrial purposes.

41 (e) Nothing in this section shall be construed to limit or otherwise
42 affect the commission's jurisdiction, authority and duty to regulate dis-
43 tribution as a public utility.

(f) Before July 1, 2002, any city of this state may revise the franchise fee provisions of any natural gas franchise agreement to ensure that franchise fees are paid on all natural gas distributed by the franchised entity without regard to the retail supplier.

4-3

RESEARCH / INFORMATION BULLETIN

League of Kansas Municipalities / 300 S.W. Eighth Street / Topeka, Kansas 66603 / 785-354-9565

Vol. XVII No. 648
October 9, 1998

PRESERVING FRANCHISE REVENUES IN AN ERA OF RETAIL WHEELING AND COMPETITION¹

1. History and Legal Basis of Franchise Agreements. Since 1905 cities have had the clear statutory authority to control the use of public streets, alleys and rights of way by companies providing a range of public services, including the provision of electricity and gas. Three major enactments govern this activity: (1) K.S.A. 12-848, enacted in 1905, applying only to cities of the 2nd and 3rd class; (2) K.S.A. 12-824, enacted in 1915, applying to all cities; and (3) K.S.A. 12-2001, enacted in 1945, applying to all cities. These statutes all authorize the exercise of such control through the approval of ordinances granting companies the privilege or "franchise" to use city-owned right-of-way to provide electricity, natural gas, railway and bus service, telephone or telegraph service, steam heat, water, etc .

In the last few decades, K.S.A. 12-2001 has been used most commonly as the legal basis for the granting of franchises by cities. This extraordinary statute authorizes cities to grant a franchise for up to 20 years after three public readings of the ordinance granting the franchise. The franchise granted also is subject to a public referendum if a sufficient petition is filed. In many respects, the granting of franchises was one of our earliest forms of "privatization" of public services in the cities that chose not to create municipal utilities (currently operated by 121 cities). In such cases, the franchise ordinance contains the terms under which private companies can supply these public services in any city.

2. What Rights Are Granted And Duties Created Under A Franchise? Those not familiar with utility franchise ordinances might incorrectly assume that they only concern fees. This assumption would be very inaccurate. It is clear from a recent Kansas Supreme Court decision that cities, acting in accordance with state statutes, actually do grant a "franchise" to persons, firms or corporations that request to use the public right-of-way and provide public services within city limits.

Although a franchise is granted by a municipality by an extraordinary ordinance (i.e., one subject to referendum and which must be read three times in public), it also comprises a legal contract between the city and the company, conferring valuable rights. In fact, many franchise ordinances read like contracts, specifying the respective privileges and duties of the parties, and providing remedies for nonperformance. Both federal and state courts have recognized that franchise ordinances/agreements are contracts which confer specific property rights. See, e.g., *Kansas Gas & Electric v. City of Independence*, 79 F.2d 32, 35 (1935); and *City of Liberal v. Teleprompter Cable Service, Inc.*, 218 Kan. 289 (1975).

3. Franchise Compensation or Fees. K.S.A. 12-2001 requires companies which receive a franchise from a city to provide "adequate compensation or consideration therefor" and to pay a fixed charge for the right regardless of whether or not other or additional compensation is provided. The statute goes on to say:

Such fixed charge may consist of a percentage of the gross receipts derived from the service permitted by the grant, right, privilege or franchise from consumers or recipients of such service located within the corporate boundaries of such city. [Emphasis added].

¹Presented at 88th Annual Conference of the League of Kansas Municipalities, October 4-6, 1998, in Wichita, Kansas.

The franchise fee may be based on any agreed-upon terms, but it is most commonly based on a percentage of the gross receipts derived by the company from its services in the city. While the League has not done a recent survey of city franchise fee rates, our franchise files contain ordinances with fee provisions ranging from 2% - 5% of gross receipts derived from electric service in the city. Consider this provision from a 1994 franchise ordinance of Yates Center:

As further consideration for the granting of this franchise, and in lieu of any city occupation license, or revenue taxes, the Company shall pay to the City during the term of this franchise two percent (2%) of its gross revenue from the sale of electric energy within the corporate limits of said City, such payment to be made monthly for the preceding monthly period.

The first underlined passage demonstrates a common feature in such provisions; i.e., the franchise fee is the exclusive payment made by the Company and the Company is exempt from other payments. The second passage also is common in these agreements. Franchise payments are typically computed based on sales within the city only. While it may be computed based on a percentage of gross receipts, the franchise fee is not a tax. It is a fee paid for the privilege of using the public rights-of-way to deliver electricity to the residents of a city. By order of the KCC it now appears on ratepayers bills in a way that it appears to be a tax, but it most closely resembles a payment for the use or rental of the rights-of-way in delivering a public service. This is extremely valuable property which, in many instances, the city purchased from private landowners. Recent studies in other states have demonstrated that franchise fees in those states were usually substantially less than the franchisee would pay in fair market rent or for the purchase of comparable property.

4. The Relative Importance of Franchise Fees As A Revenue Source. Franchise fees can comprise a significant component of a city's revenues—easily three times what it derives from its 1% sales tax from the sale of electricity if the franchise fee rate is 3%. A recent League survey revealed that statewide cities receiving electric franchise fees receive an amount which on the average equals 11% of their property tax revenues from all sources, and it would require an average mill levy of 3.8 mills to replace all electric franchise revenues. In cities with populations between 299 - 499, the average mill levy increase to replace the franchise fees would be 10.7 mills.

The 1997 tax and fee payments reported to a 1998 interim legislative committee by Western Resources to cities within its utilities service territories provide a compelling illustration of the relative significance of electric franchise fees to city budgets and as a way of avoiding reliance on the property tax. Western Resources reported it paid the following amounts to cities in 1997:

Payment Type	Amount	Percent Total
City Franchise Fees	\$27,881,643	(81.8%)
City Property Tax	2,890,304	(8.5%)
City Sales Tax	<u>3,278,883</u>	(9.6%)
	\$34,050,830	

Statewide we estimate cities collected \$312 million in sales tax revenue in 1997—with approximately \$14 million (4.6% of the total using the Dept. of Revenue's estimates) being derived from the sale of electricity. In comparison, cities levied \$319 million in property taxes in 1997.

5. How Wheeling May Affect Electric Franchise Revenues. Municipal electric franchise revenues can be expected to be affected by retail wheeling in many of the same ways as sales tax revenues will be affected. In fact, the recent growth in retail competition in supplying "transported" natural gas to some industries has caused some cities to lose natural gas franchise fees that are based on a percentage of gross receipts on natural gas sold locally by the franchisee (i.e., the local distribution company, or LDC). Local franchisees in such cases actually collect lower gross receipts on natural gas which they sell locally, but they offset this revenue loss with distribution fees they collect for the natural gas they "wheel" through their distribution system. In these cases, cities experience revenue losses since older franchise agreements do not cover gas which is transported or "wheeled." In some recent renewals or amendments of gas franchise agreements cities have built in compensation provisions to cover this "transported" gas. When this is not possible, it effectively increases pressure to raise property taxes or increase other revenues.

Retail wheeling of electricity is expected to affect electric revenues in an identical way. Long term franchise agreements have provisions for franchise fees that are typically based on the gross receipts of the franchisee from the sale of electricity within the city limits and not from its distribution on behalf of other suppliers. Secondly, since the duty to make franchise fee payments falls on the franchisee and not other suppliers, cities and their franchisees will have to develop new mechanisms for the collection of franchise fees (or their equivalent) from competitive suppliers. If this potential loss of revenue is not addressed, it will competitively disadvantage franchisees which will sell electricity to a portion of the local market (which will pay the fee) and cities which must turn to other sources of revenue, including the property tax, to replace the lost revenue..

Like the sales tax, municipal franchise revenues also can be expected to be affected by the dropping electricity prices (unless consumption increases) as well as the unbundling of the components of what today is known as the sale of electricity, including amortization of generating plant costs (which in the future may be "stranded investment") and other built-in costs such as universal service.

6. Policy Options. There are both local and state, as well as short-term and long-term, policy options for addressing the franchise revenue concerns raised by retail wheeling. Cities can clearly include provisions in their franchise agreements as they are renewed that anticipate this sea-change and which provide for renegotiation of the fee provisions in the event of electric retail competition. This has advantages, but given the long-term nature of most existing franchises it may take many years to address all cities' needs. In the meantime, substantial revenue losses could occur. An alternative is simply to impose a duty on the franchisee to remit a fee based its distribution of electricity (or gas) on a billed unit of energy basis--whether the franchisee generated or simply distributed the electricity for another supplier. There are drawback to this approach--not the least of which is that if the franchisee/LDC is not responsible for billing the customers of companies for which it simply distributes power, the fee cannot be easily recovered from the customer. It would be necessary for any retail wheeling legislation to address this concern, either requiring use of the LDC for billing or requiring energy suppliers to pay the fee.

OPTIONAL FRANCHISE PROVISIONS

Cities have begun to incorporate provisions into their new franchise agreements that contemplate both the "wheeling" of electricity and the "transportation" of natural gas. There is clearly no one way to do this. These samples are provided for illustration purposes only.

ELECTRICITY

City of Lawrence, Ordinance No. 7034

In the event customers of the Company within the area covered by this Agreement are granted the right to purchase electricity from a provider other than the Company, either party may, upon thirty (30) days' notice to the other party, request that the provisions of this Agreement, including the franchise fee rate provided herein, be adjusted to reflect the modifications of governing law allowing the customers of the Company to purchase electricity from providers other than the Company. The parties agree that, upon the giving and receipt of such notice, they will meet in good faith to negotiate any necessary changes to this Agreement to conform it to the intent of the modifications of governing law. The failure to negotiate in good faith shall be considered a material breach of this Agreement.

City of El Dorado, Ordinance No. S-1047

In the event the Company's customers served within the area covered by this Agreement are granted the right to purchase electricity from a provider other than this Company, either party may, upon thirty (30) days' written notice to the other party, request that the franchise fee rate provided for herein be adjusted to reflect the modifications and resolution of franchise fee issues adopted in the legislation which created the right of customers to obtain electricity from providers other than the Company. The parties agree that, upon the giving and receipt of such notice, they will meet in good faith to negotiate any necessary changes to this Agreement. However, if the parties are unable to reach an agreement within

ninety (90) days after the receipt of notice by the receiving party, the City, at its option, has the right to terminate the franchise granted to the grantee by action of the governing body repealing this Ordinance.

Western Resources' Recommendation

In the event Western Resources' customers served within the area covered by this Agreement are granted the right to purchase electricity from a provider other than Western Resources, either party may, upon thirty (30) days' notice to the other party, request that the franchise fee rate provided for herein be adjusted to reflect the modifications and resolutions of franchise fee issues adopted in the legislation which created the right of customers to obtain electricity from providers other than Western resources. The parties agree that, upon the giving and receipt of such notice, they will meet in good faith to negotiate any necessary changes to this Agreement to conform it to the intent of such legislation.

City of Quinter, Ordinance No. 427

If and when retail wheeling becomes an option, this ordinance may be opened so that a franchise tax may be collected on such electric energy that is being wheeled through Midwest Energy's local distribution system in the City limits of Quinter, Kansas. The option to reopen this provision of section 6 will not effect the other terms of this ordinance.

NATURAL GAS

City of Dodge City Ordinance No. 3233

In consideration of the granting of this franchise, the Grantee shall pay to the Grantor an annual Franchise Fee (Fee) of \$.5255 per foot for each foot of the Grantee's gas distribution main within the corporate boundaries of the Grantor, which at the time of the signing of this Franchise is 618,466 feet. The fee shall be computed annually on or before December 31 of each year using the actual footage of mains within the corporate boundaries as of November 30 of that year. At the end of the initial five year term, the Grantor may, by ordinance, change the per-foot amount of the Fee up to ten percent (10%) compared to the existing per-foot amount. Thereafter and no more frequently than once every five years, the Grantor may, by ordinance, change the per-foot amount up to ten percent (10%) compared to the existing per-foot amount. The Grantee shall pay to the Grantor on or before the 15th day of each and every month that portion of the Fee actually collected from Consumers during the previous month, based on the following:

1. The Grantee shall collect the Fee from all Customers within a Customer Class located in the corporate boundaries of Grantor.
2. The Fee shall be collected from the customer classes in the same proportion as the previous year's actual franchise fee receipts from the customer classes. The franchise fee shall be collected from each customer within the class, regardless of the type of natural gas service obtained (i.e., sales or transportation) from Grantee and shall be computed on a volumetric basis. The volumetric rate for each Customer shall be computed annually by dividing the total Fee for the customer class by the previous year's volumes from that customer class (i.e., $\text{Volumetric Rate} = \frac{\text{Customer Class Fee} + \text{Previous Year's Customer Class Volume}}{\text{Customer Class Volume}}$). An example of the computation of the Franchise Fee will be on file with the City Clerk and on file at People's operation headquarters in Dodge City.

The Grantee shall list the Fee to be collected from each Customer as a separate item on bills issued to Customers as a "City Franchise Fee."

The amount so paid by Grantee to Grantor shall be adjusted down for that portion of the Franchise Fee that is uncollectible. The amount paid to Grantor shall be adjusted up for receipt of Franchise Fees paid by Customers towards previously uncollected Franchise Fees.

City of Logan Ordinance No. 532

In consideration of the rights and privileges herein granted, the Grantee shall assess effective the first billing cycle after this franchise customers within the City a franchise tax or fee of two percent (2%) of the gross receipts (exclusive of the franchise fee or tax) derived by Grantee from sales by Grantee to such customers and of \$0.0095 (.95 cents) per therm for gas transported to residential and commercial customers within the City on Grantee's distribution system when Grantee solely provides distribution transportation and not sales service. Grantee shall pay to the City Treasurer a semi-annual payment for each year of the franchise's duration an amount equal to the franchise fee or tax funds collected by Grantee hereunder.

ELECTRICITY OR NATURAL GAS

League of Kansas Municipalities Sample

Section ____. **Franchise Fee.** (a) In consideration of the granting of the franchise, the grantee shall monthly (or quarterly) pay to the city a franchisee fee equal to the following:

(1) **Based on Grantee's Sales.** ____% of the gross receipts derived by grantee from the sale or furnishing of gas (or electricity) by grantee to customers within the present or future boundaries of the city; and

(2) **Based on Sales By Other Suppliers.** ____% of the gross receipts derived by any other supplier from the sale or furnishing of gas (or electricity) through grantee's distribution lines, pipes, and system (hereinafter referred to as the "system") to customers within the present or future boundaries of the city. If, after diligent efforts, grantee is unable to secure gross receipts information from other suppliers using the system to supply gas (or electricity), the governing body may authorize the grantee by ordinance to remit an amount to the city based on the billed unit of energy (mcf or kWh, as appropriate) furnished to customers by other suppliers of gas (or electricity) through the system during the reporting period, multiplied by a factor which is the rate which grantee would have charged for the same commodity and service to such customers during the same time period. Such authorization may be revoked at any time by the governing body. Grantee shall be responsible for payment of all fees required herein based on the sale or furnishing of gas (or electricity) by other suppliers through grantee's system, and grantee may collect from other suppliers any amounts which it pays under the provisions of this paragraph for gas (or electricity) so furnished.