Approved: 2-6-02

MINUTES OF THE SENATE UTILITIES COMMITTEE.

The joint meeting of the Senate and House Utilities Committees was called to order by Chairperson Carl Holmes at 9:40 a.m. on January 15, 2002 in Room 526-S of the Capitol.

All members were present except:

Committee staff present: Raney Gilliland, Legislative Research
Emalene Correll, Legislative Research
Bruce Kinzie, Revisor of Statutes
Ann McMorris, Senate Utilities Secretary
Robert Chapman, Legislative Research
Jo Cook, House Utilities Secretary

Conferees appearing before the committee:
Robert Chapman, Legislative Research

Others attending: See attached list. on House Utilities Committee minutes of same date

Chairperson Holmes called on staffer Robert Chapman of Legislative Research to review the reports of the Special Committee on Utilities to the 2002 Legislature. (Attachment 1)

Three topics were studied by the interim committee - (1) Municipal Annexation and Electric Service Territories; (2) National and State Energy Plans; and (3) Natural Gas Pricing and Supply.

The conclusions and recommendations on each of the three topics were reviewed and discussed.

Chairpersons Holmes and Clark announced their proposed committee agenda for the next week.

The next meeting of the joint committees will be at 9:30 a.m. on January 16, 2002.

Adjournment at 10:20 a.m.

Respectfully submitted,

Ann McMorris, Secretary

Attachment - 1

Unless specifically noted, the individual remarks recorded herein have not been transcribed verbatim. Individual remarks as reported herein have not been submitted to the individuals appearing before the committee for editing or corrections.

REPORTS of the SPECIAL COMMITTEE ON UTILITIES to the 2002 KANSAS LEGISLATURE

Chairperson: Representative Carl Holmes

Vice-Chairperson: Senator Stan Clark

Ranking Minority Member: Representative Laura McClure

Other Members: Senators Jim Barone, Jay Emler and Mark Taddiken
Representatives Nile Dillmore, Patricia Lightner, Don Myers, Tom Sloan and Jerry Williams

STUDY TOPICS

National and State Energy Plans
Natural Gas Pricing and Supply
Municipal Annexation and Electric Service Territories

Special Committee on Utilities

MUNICIPAL ANNEXATION AND ELECTRIC SERVICE TERRITORIES

CONCLUSIONS AND RECOMMENDATIONS

The Committee recommends the amendment of the Electric Retailers Suppliers Act to require notice to electric retail suppliers of city annexation decisions and to require cities to consider certain factors when deciding which electric supplier should provide service to newly annexed areas.

Proposed Legislation: The Committee recommends one bill.

BACKGROUND

Topic No. 1 called for a study of Kansas Corporation Commission (KCC) certified electric distribution service territories and the impact of municipal annexation.

The topic was requested by the Kansas Electric Cooperatives, Inc. and by Senator Stan Clark, Chair of the Senate Utilities Committee. The concern expressed in both requests was that electric cooperatives often loose the right to serve in annexed areas due to the ability of cities to extinguish this right. Further, the concerns were that there are no objective standards in place to determine which electric provider should serve these annexed territories. The issue of financial compensation for loss of territory also was suggested as a topic for review.

History of Retail Electric Suppliers Act

1976 Law. The Kansas Retail Electric Suppliers Act was enacted in 1976 as a culmination of at least three years of consideration of the issue by the Kansas Legislature. See Proposal No. 108—Electric Utility Territories, *Reports of Special Committees to the 1974 Kansas Legislature* and Proposal No. 74—Electric Utility Territories, *Reports of Special Committees to the 1975 Legislature.*

Briefly, the 1976 law, HB 2047, provided for creation and certification of exclusive electric service territories by the KCC. Within each electric service territory, only one retail supplier was to be able to provide retail electric service. In the existing dual certified service territories, areas where more than one electric supplier had been granted a service certificate, the boundaries of each retail electric utility territory were to be established substantially equidistant between the supplier's existing distribution lines and the nearest existing distribution lines of any other supplier.

A municipal retail electric supplier providing the only service in a single-service territory was to be granted a single certified territory, the boundaries of which were to be one-half mile in every direction from its existing distribution lines. In a single-service territory served by a municipal and a nonmunicipal supplier, the boundary was to be established equidistant between existing distribution

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lines. However, the municipal territory was not to be more than one-half mile in any direction from its distribution lines or beyond the original service territory boundary. Single certified territories not assigned to a municipal supplier were to be retained by the originally certified retail electric supplier.

Municipally owned or operated retail electric utilities were made subject to KCC jurisdiction as a public utility with respect to all operations extending more than three miles of it's corporate boundaries. A municipal retail electric supplier was made subject to regulation by the KCC in matters relating to right to serve in the territory within the three-mile ring of the city, but the KCC had no jurisdiction concerning retail electric suppliers within a city's corporate limits. See KSA 66-1, 1174.

1986 Law (a Moratorium) and Interim Committee Study. A law was enacted in 1986 (SB 740) which provided that from and after the effective date of the act and prior to July 1, 1987, each retail electric supplier was to continue to have the right to serve all customers within its certified territory as it existed on the effective date of the act. No changes in the certified territory of retail electric suppliers could be made during this period without the agreement of the suppliers involved and without the approval of the KCC. The same provisions applied to territory annexed by a city, thereby imposing a one-year freeze on certified territories regardless of annexation by a city.

An interim study topic was assigned to the 1986 Special Committee on Energy and Natural Resources to "study and make recommendations concerning the impact of municipal annexation on electric utilities serving existing certified territories and to determine whether the moratorium established by the enactment of SB 740 should be continued."

The 11-member interim Committee, in its report (note two minority reports) to the 1987 Legislature, recommended SB 10 for passage. SB 10, as introduced, included a provision which would have provided that the inclusion by annexation of the certified territory of a retail electric supplier within the boundaries of any city would not impair or affect the retail electric suppliers' exclusive right to serve, granted by the KCC. A city would have been required to either: (1) grant a franchise to the retail electric supplier serving the annexed area; or (2) make application to the KCC for reassignment of the territory to another electric supplier.

SB 10 was sent to the Senate Local Government Committee and was substantially amended by a substitute bill (Sub. for SB 10). The supplemental note for Sub. for SB 10, as it passed the Senate Local Government Committee, noted that the amendments represented a compromise between various interests. Provisions in the original bill requiring a city which annexes territory to grant a franchise to the retail electric supplier or to make application to the KCC for another supplier were deleted.

1987 Legislation. Two laws enacted in 1987 (Sub. for SB 10 and SB 333) requiring compensation for displaced electric suppliers. Sub. for SB 10 amended the electric service territory law to require "fair and reasonable" compensation be paid to a retail electric supplier whose territory is diminished as a result of annexation by a city. The bill provided that compensation shall be either an amount mutually agreed upon or the sum of four

criteria listed. If no agreement can be reached, either party may apply to the district court for determination of compensation. Sub. for SB 10 also deleted language enacted in 1986 which established a moratorium on any changes in electric service territories due to city annexation until July 1, 1987. The 1987 law provided that the originally certified electric supplier to an area which has been annexed may continue to serve that area and charge its ordinary rates without paying franchise fees to the city until such time as another supplier assumes services. There was a time frame established, however, wherein the original electric supplier, if not displaced, may be required to obtain a franchise from the city in order to continue service.

SB 333, also enacted in 1987, required cities which terminate a franchise agreement with a retail electric supplier prior to the expiration of the franchise to pay the supplier for the electric distribution system in an amount mutually agreed upon, or in accord with a formula established in the law. If the parties are unable to reach an agreement as to the amount of compensation under the formula, either party may apply to the court for determination of compensation.

Retail Electric Suppliers Act

The Retail Electric Suppliers Act was enacted in 1976. The following is a summary of the Act.

Public Policy of the Act

KSA 66-1,171 declares that it is the public policy of this state to:

(a) encourage the orderly development of retail electric service;

(b) avoid wasteful duplication of facilities for the distribution of electricity;

(c) avoid unnecessary encumbrance of the landscape of the state;

(d) prevent waste of materials and natural resources;

(e) facilitate the public convenience and necessity; and

(f) minimize disputes between retail electric suppliers which may result in inconvenience, diminished efficiency and higher costs in serving the consumer.

Division of State Into Electric Service Territories

In pursuing this public policy, it is the purpose of the act is to provide for the division of the state into territories within which retail electric suppliers are to provide the retail electric service as provided in this act. The KCC is required under KSA 66-1,172 to divide the state into electric service territories. Within each territory, only one retail electric supplier shall provide retail electric service, and any territory established shall be certified to the retail electric supplier by the KCC. The area shall be provided retail electric service exclusively by the supplier.

Every retail electric supplier under KSA 66-1,173 has the exclusive right and responsibility to furnish retail electric service to all electric consuming facilities located within its certified territory. Any retail electric supplier, with the approval of the KCC, may extend distribution or transmission facilities through the certified territory of another retail electric supplier, if the extension is necessary for

the supplier to connect with any of its facilities or those of others to serve consumers within its own territory.

Commission Control Over Cities Limited

Municipally owned or operated retail electric utilities are subject to KCC jurisdiction as a public utility with respect to all operations extending more than three miles of it's corporate boundaries. A municipal retail electric supplier shall be subject to regulation by the KCC in matters relating to right to serve in the territory within the three-mile ring of the city but the KCC shall have no jurisdiction concerning retail electric suppliers within it's corporate limits. See KSA 66-1, 1174.

Effect of Annexation on Electric Service Suppliers

KSA 66-1,176(a) provides that all rights of a retail electric supplier, to provide electric service in an area annexed by a city, shall terminate 180 days from the date of annexation, unless the electric supplier is then holding a valid franchise for service in the area granted by the annexing city. The period of 180 days shall be extended to 210 days from the date of annexation if a franchise is granted to the retail electric supplier pursuant to a referendum conducted according to applicable franchise laws of the State of Kansas within 210 days. If electric service rights are terminated, the KCC shall certify the annexed area as a single certified territory to the supplier holding a franchise for or then providing retail electric service in the city immediately prior to the annexation.

KSA 66-1,176(b) provides that in the event the electric supplier holding a franchise or then providing retail electric service does not provide electric service to the annexed area at the termination of the applicable 180-day or 210-day period, then the originally certified electric supplier shall have the right to continue service to the annexed area and charge its ordinary rates until the other electric supplier does assume service to the annexed area. The electric service shall be free of any franchise fee or other compensation to the city or the electric supplier holding the franchise. The city may require the originally certified supplier to obtain a franchise in order to continue service in the annexed area.

Compensation Due to an Electric Supplier (Without a Franchise) Whose Service is Terminated

Note that under KSA 66-1,176(c) whenever the service rights of a retail electric supplier are terminated pursuant to subsection (a), where no franchise exists, fair and reasonable compensation shall be paid to the retail electric supplier by the supplier subsequently authorized to provide electric service. Compensation shall be an amount mutually agreed upon by the affected suppliers, or the sum of the four items: (1) depreciated replacement costs for the electric utility facilities in the territory whose service rights are terminated; (2) reasonable costs of detachment; (3) an amount equal to the gross revenues attributable to the customers in the territory for the next twelve months; and (4) an amount equal to the State and federal tax liability produced by the income generated by the compensation.

If the parties are unable to agree upon an amount of compensation to be paid pursuant to subsection (c), KSA 66-1,176(d) provides that after 60 days following the date of termination of service rights either party may apply to the dis-

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trict court for determination of compensation. Such determination shall be made by the court sitting without a jury.

Compensation Required if Franchise Holders Rights Terminated

KSA 66-1,176b *et seq.* was enacted in 1987 by SB 333 and provides that when the service rights of a retail electric supplier are terminated by a city during the period in which a valid franchise is in effect, and the service rights are assumed by the terminating city, the governing body of the city shall acquire, from the terminated supplier, the parts of the local electric distribution system necessary to serve all customers within the previously franchised area, and the terminated supplier shall sell the system to the governing body of the city for fair compensation. Compensation shall be an amount mutually agreed upon by the affected parties or an amount determined by the formula under KSA 66-176b(a) which includes:

1. depreciated replacement cost for facilities both inside and outside the area;
2. take or pay power contracts, or participation power agreements;
3. reasonable detachment costs;
4. net revenues for a 12 month period; and
5. State and federal tax liability.

If the parties are unable to agree upon the amount of compensation to be paid under KSA 66-1,176b after 60 days following the date of termination of service rights, either party may apply to the district court. The determination shall be made by the court sitting without a jury.

KSA 66-1,176c, provides that, in addition to the fair cash value of any plant and appurtenance thereto, a retail electric supplier whose service rights have expired by reason of nonrenewal of a valid franchise agreement shall be entitled to compensation for all reasonable and prudent costs of detaching the electric system facilities to be sold. Further compensation is allowed for all reasonable and prudent costs of reintegrating the remaining electric system facilities.

Issues Decided by the Kansas Court of Appeals

The Kansas Court of Appeals on May 11, 2001, in an unpublished opinion, in the case of *Nemaha-Marshall Electric Cooperative Association, Inc.*, v. *State Corporation Commission and City of Seneca* (Case No. 84,908), upheld the right of a city to displace the rural electric cooperative who had supplied service to an area annexed by the city.

A second case, *Lyon-Coffey Electric Cooperative, Inc.* v. *State Corporation Commission and City of Burlington*, Case No. 86,071, decided August 17, 2001, in a published opinion, also held that current law did not require the KCC to make a finding of public convenience in order to grant a certificate to a municipally owned and operated utility. Further, the court held that the law was not unconstitutional as an improper delegation of power to a city to decide a statewide issue in violation of Article 2, Section 21 of the *Kansas Constitution*.

Testimony of Conferees

The Joint Committee held a one day hearing on the annexation topic at its August meeting. The Joint Committee heard from ten representatives of rural electric cooperatives; and three represen-

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tatives of Kansas Municipal Utilities and cities.

Representatives of rural electric cooperatives included several representatives and the general counsel for the Kansas Electric Cooperatives, the CMS Electric Cooperative of Meriden, the DS&O Rural Electric Cooperative of Meade, the Bluestem Electric Cooperative of Wamego, the Kaw Valley Electric Cooperative of Topeka, the Butler Rural Electric Cooperative of El Dorado, the Sedgwick County Electric Cooperative of Cheney, and the Lyon-Coffey Electric Cooperative of Burlington. These representatives said the current law lacks fairness, since the electric cooperatives have no voice in the decision. The issue is unilaterally decided by city governing bodies. They said the loss of territory by rural electric cooperatives and loss of the potential for growth of customers perpetuates rate disparities. They suggested legislation that would require the KCC to hold a hearing and to make a determination regarding the advisability of the detachment of a territory from a rural electric cooperative.

Representatives of the Kansas Municipal Utilities and several cities opposed any change in the current law. They noted legislation that currently applied was developed by consensus of all the various parties in 1976 and again in 1987. They said growth rates of rural electric cooperatives and investor owned utilities indicated these entities have not been harmed by the current annexation law. They said an amendment to current law to give the KCC jurisdiction to determine the advisability of detaching territory from a rural electric cooperative as a result of city annexation would undercut local control and city home rule powers. They said such changes would stifle the orderly growth of cities and inhibit economic development.

Conclusions and Recommendations

The Committee directed that the various interested parties to meet and to resolve the concerns expressed by the conferees. A series of meetings were held and a compromise bill was presented to the Committee at the November meeting with the following notation. The changes outlined in KSA 66-1,176(1) have been agreed to by the cooperatives, the League of Kansas Municipalities, Kansas Municipal Utilities, Western Resources, and Empire District Electric, Kansas City Power and Light is neutral. Utilicorp agrees with all changes except those set forth in KSA 66-1,176(a)(2), (4), and (5).

The Committee recognizes the cooperation and effort exhibited by representatives of the Kansas Rural Electric Cooperatives Inc., the Kansas Municipal Utilities, the various investor owned utilities, and the League of Kansas Municipalities in arriving at suggested legislation to address concerns arising from city annexation of lands served by various retail electric suppliers. The Committee believes that the bill should proceed forward.

The Committee therefore recommends legislation for favorable consideration by the 2002 Legislature. The bill would amend the Kansas Retail Electric Suppliers Act as follows:

- The bill requires a city which proposes to annex land that is located within the certified territory of a retail electric supplier as defined by KSA 66-1,170, to provide notice to the retail electric supplier in the manner prescribed by KSA 12-520a a part of the city annex-

ation law. KSA 12-520a requires a copy of the city resolution providing for the public hearing on the proposed annexation to be mailed not more than 10 days following the resolution adoption to various parties listed.

- The bill requires that whenever the city annexes land that is located within the certified territory of a retail electric supplier as defined by KSA 66-1,170, the city shall negotiate for the issuance of a franchise agreement pursuant to KSA 12-2001 *et seq.* (the city franchise law) with a retail electric supplier holding a certificate within the annexed area.

- The city must consider certain factors when making the electric supplier selection including, but not limited to: 1.) the public convenience and necessity; 2.) rates of various providers; 3.) desires of the customer or customers to be served; 4.) economic impact on the suppliers; 5.) economic impact on the customers of the suppliers; 6.) the utility's operation ability to serve the annexed area; 7.) avoiding the wasteful duplication of facilities; 8.) avoiding unnecessary encumbrance on the landscape; 9.) preventing the waste of materials and natural resources.

- The bill, shall not be construed, however, to require a supplier holding both a certificate of convenience and a franchise for the area annexed to obtain a new franchise.

  The bill clarifies that the city shall have the final selection of which provider receives a franchise to operate with the annexed area.

- Any supplier aggrieved within thirty days of the final decision of the city, may maintain an action in the district court of the county in which the annexed area is located to determine the reasonableness of the final decision. In the event that an appeal of the decision is filed in the district court, the retail electric supplier providing services at the time of annexation shall continue to provide service until such time as the appeal has been concluded.

- A factor in the compensation formula is changed under both KSA 66-1,176(c) and KSA 66-1,176(b) to provide that an amount equal to two times (currently not doubled) the gross revenues attributed to customers in the terminated territory during the 12 preceding months be paid.

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Special Committee on Utilities

National and State Energy Plans

Conclusions and Recommendations

On the topic of electricity infrastructure the Committee recommends that an update on the status of Regional Transmission Organizations and transmission constraints be provided in a Joint Meeting of the Senate and House Utilities Committees.

On the topic of energy conservation the Committee recommends:

- Promotion of energy efficiency and energy conservation efforts overall and increased efforts to educate consumers on ways to improve efficiency and conservation.
- Reviewing during the 2002 Session efforts to create more awareness of energy assistance programs, and examining what the Department of Commerce and Housing and SRS are doing to alert those consumers who are eligible for the Weatherization Assistance Program.
- Utilization by the Board of Regents of incentives to reduce energy costs.

In addition to various policy recommendations on energy-related issues, the Committee recommends that legislation be introduced to:

- Urge the U.S. Congress to proceed with all due haste to approve and begin storage of radioactive waste at Yucca Mountain in Nevada.
- Urge the U.S. Congress to reauthorize and extend the Federal Tax Credits for wind generation facilities.
- Urge the U.S. Congress to open Alaska's Arctic National Wildlife Refuge for the exploration of oil.

Proposed Legislation: The Committee recommends three concurrent resolutions.

Background

The Legislative Coordinating Council created the Special Committee on Utilities and assigned it the task of studying issues relating to the state's role in implementing the National Energy Plan being proposed by the Bush Administration and considered by the U.S. Congress. Discussion of the state's role in an energy plan included topics and issues such as electricity infrastructure, energy policy, energy conservation, alternative fuel usage, energy assistance programs, alternative energy sources, Regional Transmission Operators (RTOs), and planning for future

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energy needs. Committee members also expressed an interest in discussing the status of the state energy emergency plan given the recent dramatic events on September 11, 2001. The Committee met on August 20-21, October 10-12, and November 7-8.

Committee Activities

The members of the Special Committee on Utilities heard presentations from several conferees and from legislative staff concerning the potential development of a state energy policy that includes implementation of portions of the national energy plan that affect Kansas.

On August 21, the Committee heard presentations from the following:

- Senator Stan Clark provided the Committee with a report on the National Association of Regulatory Utility Commissioners (NARUC) 43rd Annual Regulatory Studies Program; legislative staff, Robert Chapman, Kansas Legislative Research Department (KLRD), also summed up his experience at the conference;
- Robert Chapman, KLRD, reviewed the state's role in a national energy plan;
- Mary Torrence, Revisor of Statues Office, reviewed past state energy legislation;
- Dick Brewster, Director of Governmental Affairs for BP Amoco, submitted written testimony about BP Amoco's energy policy and its impact on Kansas;
- David M. Dayvault, a practicing CPA and Chairman of KIOGA Tax Committee, discussed the tax provisions of the Bush Energy Plan;
- Earl Watkins, Legal Counsel for Sunflower Electric Power Corporation, described the planning process Sunflower utilizes to provide wholesale power;
- Richard Kaup, Director of Business Development, Kinder Morgan, Inc., talked about Kansas' future energy needs, focusing on natural gas;
- Chuck Dehart, Williams Gas Pipeline, described his company's planning process;
- Laine Lobban, Business Development, Western Pipeline Group, El Paso, presented maps and charts of the Anadarko Basin;
- Chris Giles, Senior Director of Revenue and Resource Management, Kansas City Power and Light, explained how the company meets its load obligations by using a wide mix of resources;
- Larry Berg, Community Services Manager, Midwest Energy, Inc., described the difference between retrospective and forward-looking public policy;
- John McKinney, Vice President of Electric, Utilicorp United, Inc., discussed transmission access and business risks associated with building new regulated generating facilities;
- Bruce Graham, Vice President of Member Services External Affairs, Kansas Electric Power Cooperative, Inc. (KEPCo), submitted written testimony commenting on the need for an energy policy; and

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- Jim Ploger, Energy Program Manager, Kansas Corporation Commission (KCC), reported on the current progress of the State Energy Program and the Kansas Institutional Conservation Program; he also discussed energy conservation in general and wind energy.

On October 10, 11, and 12, the Committee heard presentations from the following:

- Thaine Hoffman, Director, and Dale Worley, Program Administrator, Division of Architectural Services, Department of Administration (DOA), presented an overview of the Energy Loan Program;

- Joe Fritton, Director, Division of Facilities Management, DOA, reported on the state purchase of alternative fueled vehicles;

- Rick Kreul, Vice President, Network Operations, Utilicorp United, described the future implications of changes to RTOs;

- Bill Malcolm, Midwest Independent System Operator, reviewed issues involving RTOs;

- Pat Bourne, Southwest Power Pool, provided his company's perspective on proposed RTOs;

- Bill Brier, Edison Electric Institute, presented an overview of electricity infrastructure and issues involving transmission lines;

- Ken Rose, Senior Institute Economist, National Regulatory Research Institute (NRRI), Ohio State University, reviewed electric power markets and provided an evaluation of the California energy crisis;

- Jim Ploger, Emergency Planning, KCC, reviewed the workings and purpose of the State Energy Office;

- Robert L. Kistner, President, Energy Planning Consultants, Inc., Denver, Colorado, reviewed the State Energy Emergency Plan;

- Susan Mahoney, Governor's Office, described the Governor's position regarding the State Energy Emergency Plan;

- Neil Hartman, Deputy Assistant Regional Director for Law Enforcement, U.S. Fish and Wildlife Service, Denver, Colorado; Ron Klataske, Audubon, Kansas; Dr. Tim Kimmel, Kansas Master Falconer, Advisory Committee Member, International Association of Falconers; Diane Johnson, Director, Operation Wildlife Rehabilitation, Topeka, Kansas; (written testimony); and Brad Loveless, Western Resources, Inc., provided perspective on the pros and cons of bird-proofing of transmission lines;

- Greg Wright, Senior Director, Business Development for Western Resources, Inc., described the residential demand management, or C.A.S.H. System, and bill-stuffers; he explained efforts to promote energy conservation and consumer education;

- Dick Rohlfs, Director of Regulatory Requirements at Western Resources, Inc., described PowerStat pre-pay metering;

- Sandra Hazlett, Director of Economic and Employment Support, Depart-

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ment of Social and Rehabilitation Services, reviewed the Low Income Energy Assistance Program (LIEAP);

- Randy L. Speaker, Director of Housing, Department of Commerce and Housing, described the Weatherization Assistance Program (WAP);
- Larry Holloway, KCC, reviewed the issue of electric generation capacity and reliability requirements, and explained docket number 99—GIME, 321—GIE;
- Staff from the KCC reviewed the national energy plan from information distributed during 2nd week of NARUC and provided an update of the comparison of federal restructuring legislation of the 106th Congress;
- Bill Griffith, Conservation Chairman of the Kansas Chapter of the Sierra Club, described some of the recent national developments concerning renewables, focusing primarily on wind energy;
- Joe King, Coriolis Architecture and Energy, Lawrence, and Dr. Richard Nelson, Assistant Professor, Engineering Extension Programs, Kansas State University, addressed energy obtained from wind, biomass, and photovoltaics; and
- Joseph Franz, Agricultural Energy Services, Wind Energy, presented wind energy resource development in Kansas.

On November 7, the Committee heard presentations from the following:

- Larry Holloway, Chief of Energy Operations, KCC, reported on the possible merger between Southwest Power Pool (SPP) and Midwest Independent Transmission System Operator, Inc. (MISO) and the issue of two RTOs serving Kansas;
- Carroll Waggoner, Senior Manager, Transmission Policy, Sunflower Electric Power Corporation, described the process his company utilizes to provide wholesale power supply to member cooperatives;
- Bruce Graham, Vice President of Member Services and External Affairs, KEPCo, informed the Committee on generation planning and fuel mixes;
- William N. Dowling, Vice President of Energy Management and Supply, Midwest Energy, Inc., described his company's generation capacity;
- Burton Crawford, Manager of Deregulation, Great Plains Energy, Kansas City Power and Light Company (KCPL), described his company's reserve margin and mix of generating resources;
- Dick Dixon, Senior Vice President Customer Operations, Western Resources, Inc., explained the reliability assessment conducted by the North American Electric Reliability Council;
- Joe Bahr, Retail Energy Markets Team, and Carl Huslig, Director of Transmission Business Operations, Utilicorp United, reviewed RTOs;
- William Eliason, Vice President—Gas Strategy, Kansas Gas Service, a Division of ONEOK, described natural gas resource planning;

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- Colin Hansen, Executive Director, Kansas Municipal Utilities (KMU), described his association's members' planning generation needs;

- Rick Anderson, McPherson Board of Public Utilities (BPU), discussed BPU's generation of low-price electricity;

- Warren Corman, University Architect, described energy conservation efforts at the University of Kansas; and

- H. Edward Phillips, Vice Chancellor for Administration, Kansas University Medical Center (KUMC), answered questions concerning KUMC's involvement in the ad valorem tax court settlement.

Federal Energy Plan

The Committee reviewed the federal energy plan as proposed by the Bush Administration and the energy plan as proposed by the Democratic Party. The Committee focused on understanding the state's role in implementing a federal energy plan.

Legislative staff presented a worksheet to the Committee which compared the Bush plan with the Democratic National Energy Plan and included state actions already taken in respect to these federal energy plans. Staff reviewed the history of Kansas energy resources and energy planning legislation.

Representatives of KIOGA; Sunflower Electric Power Corporation; Kinder Morgan; El Paso; KCPL; Midwest Energy, Inc.; UtiliCorp United, Inc.; KEPCo; BP Amoco; and, the KCC, offered recommendations to the Committee on energy policy. Specifically, they recommended that the state should:

- Provide a tax structure which recognizes the cyclic nature of the industry and provide tax relief at a time when the price of the product is low;

- Encourage investment in infrastructure through long-term contracts and reasonable tax policies;

- Provide incentives for the construction of electric transmission lines;

- Utilize a forward-looking approach rather than a retrospective approach in the regulation of utilities;

- Reexamine its definition of "marginal gas well";

- Accelerate the transition between dwindling fossil fuels and investments in a renewable resource base; and

- Promote energy efficiency and conservation efforts.

A spokesperson for the Energy Program of the KCC reviewed the State Energy Program and the Institutional Conservation Program, administered by the KCC. The KCC consistently has over 25 projects funded through a combination of federal grant moneys and matching oil overcharge moneys. These moneys are used on conservation projects for buildings, education, alternative fuels transportation, and utilities. Another funding source will be needed to match federal funds to continue the State Energy Program in approximately two to three years when oil overcharge funding is exhausted.

A consultant, who is helping create the Kansas State Energy Emergency Re-

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sponse Plan (SEERP), provided an introduction to, and overview of, the work being done on formulating such a plan. SEERP represents policies, procedures, and regulations that may be adopted or enacted by the state if an energy emergency occurs. An energy emergency is defined as "an actual or impending shortage or curtailment of usable, necessary energy resources, such that the maintenance of necessary services; the protection of public health, safety, and welfare; or the maintenance of a basically sound economy is imperiled in any geographical section of the state or throughout the entire state." Such a plan is designed to reduce the impacts of a shortage to the state's energy supply and to the state's economic well-being. The KCC's State Energy Programs Section is responsible for implementation of the plan. The Kansas Division of Emergency Management directs the energy emergency contingency operations in the state at the direct order of the Governor's declaration of an emergency.

Electricity Infrastructure and Energy Policy

A spokesperson from the NRRI, Ohio State University, reported on the performance of electric power markets and the California energy crisis. Committee members were updated on the status of the state's electric industry restructuring efforts. Fifteen states and Washington, D.C., currently allow retail access. The average revenue per kilowatt hour in Kansas is around 6.2 cents, which is just below the national average of 6.4 cents. Committee members learned that evaluating the performance of retail markets is based on the number of offers, offers with savings opportunities, the number of suppliers, the type of offers, and the percent of customers that selected an alternative energy supplier. Wholesale market performance is judged by how closely actual prices are tracking expectations in a fully competitive market, where suppliers have no ability or only limited ability to control the price. The Committee learned that "market power" is the "ability of a firm or group of firms to raise and maintain the product price significantly above the competitive level." The Committee also learned that wholesale power prices and volatility have hampered the development of retail markets. Generation owners have considerable market power in wholesale markets. Given the characteristics of electric supply and demand, this market power may continue for some time. The lack of price information in many regions of the country also will contribute to wholesale market power problems. The transition to a more competitive retail market has been more difficult and is taking longer than expected.

The Committee also learned that the California electric restructuring meltdown started in the summer of 2000, when the wholesale price of electricity climbed much higher than the 6.5 cent cap the legislature set on the retail price. A combination of factors aligned to cause the steep price increases: strong demand led to load growth, which was then coupled with supply constraints (it takes at least six years to install new transmission lines in California—three years to plan and three years to build), while production costs (natural gas prices increased dramatically) increased and design flaws emerged in the wholesale and retail markets (higher wholesale prices were prevented from being passed through to retail customers). Kansas could learn from the mistakes made in California by observing future supply and demand imbalances, transmission constraints,

concentrated wholesale and retail markets, the lack of price transparency (which limits information for market participants), plant outages, and price spikes.

A representative of the Edison Electric Institute told the Committee that U.S. electric demand is increasing faster than total electric generation additions and that, nationally, new demands for electricity will offset gains in energy efficiency, thus requiring new generation. In addition, competition among electricity suppliers and the number of transactions on the transmission grid have increased significantly and today's transmission systems were not designed to be electric "superhighways." This causes increased congestion on transmission lines. Congestion threatens system reliability and increases costs to consumers. The Committee learned that the Federal Energy Regulatory Commission's (FERC) Order 2000 established RTOs which will assume strategic planning functions on a regional basis, including grid operation, reliability, congestion management, and planning and expansion. The representative suggested Congress expand transmission grids by providing FERC with the authority to site transmission lines, providing financial incentives to attract capital to fund transmission expansion, depreciating lives of property from 20 years to 7 years, repealing the Public Utility Holding Act and updating the U.S. tax code and bringing it in line with changes in the electric industry to enhance competition and reliability. He recommended Kansas support FERC in its formation of RTOs and support the idea of RTO participation by all transmission owners.

A representative from Utilicorp informed the Committee about FERC's proposals concerning the operations and geographical limitations of RTOs. The proposals would impact the way electricity is transmitted within and between states. A representative from the MISO provided the Committee with a background of its service territory, its super regional rate area with Alliance RTO, and its proposed merger talks with Southwest Power Pool.

A spokesperson for the KCC reviewed the issue of reliability requirements and electric generation capacity, providing for the Committee various definitions used in determining net capability capacity, internal demand, capacity margins, and reserve margins. The spokesperson noted that the Southwest Power Pool requires a minimum capacity margin of 12.0 percent.

Energy Conservation Improvement Program

Representatives from the Division of Architectural Services, DOA, briefed the Committee on the Facilities Conservation Improvement Program (FCIP) which identifies potential conservation projects that would save state dollars by financing projects through bonds and covering the debt service with the savings. If fully implemented, the program could save the state $17.0 million annually. During the 2000 Legislative Session, HB 2603 was signed into law. The bill enabled energy service performance contracting. Since then, the FCIP has contracted with four Energy Service Companies (ESCO) to provide service for the State of Kansas. It was expressed to the Committee that the Board of Regents alone last year spent $35 million on utility costs (costs at the University of Kansas (KU) and KUMC were over $15 million) and that the energy program was not being fully utilized by

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KU and KUMC.

Representatives from KU explained KU's participation in the Energy Conservation Bond Program. KU's architect explained that all Regents' universities are making efforts to reduce energy costs and have done so for a number of years. University budgets are constructed and funded with the incentive to reduce energy costs. According to the architect, a dollar saved in utilities is a dollar available for other education needs. Although KU and KUMC spent $15 million for utilities costs in FY 2001, it is difficult to compare utility expenditures among campuses. It was the architect's opinion that campus mission statements are different and those differences are reflected in their physical plants and the demands those facilities place on energy use. Campuses also have different energy suppliers that can result in cost differences. But, to-date, it was admitted by a KU spokesman that efforts to maximize small savings (such as changing to more efficient light bulbs) have not been aggressively pursued. It was mentioned that the utility expenditures by KU and KUMC comprise approximately 43 percent of the total Board of Regents' system energy budget. However, these two institutions' physical plants comprise more than 41 percent of the gross square footage in the Board of Regents' system.

Conferees representing Emporia State University (ESU) detailed usage of the Energy Conservation Bond Program within their institution and demonstrated before the Committee mechanical objects used to conserve electricity consumption. The conferees stated that ESU is not currently working with the ESCOs.

The Director of the Division of Architectural Services, DOA, reported to the Committee on life cycle costing for state building construction projects. Life cycle costing is a process of considering the costs of utilities, maintenance, and operation over the life of a building as they relate to certain design decisions, and then comparing these to the initial costs of the design options to see which option is less expensive over the life of the building. The Director suggested three measures could be taken: 1) adopt and enforce the new conservation standards from ASHRAE; 2) assign someone from Architectural Services to study life cycle costing and explain its benefits to others; and, 3) make the FCIP financing program available to finance optional items that have a reasonable payback period.

Alternative Fuel Initiatives

A representative from the Division of Facilities Management, DOA, informed the Committee that the Central Motor Pool (CMP) currently has 46 credits with the federal Department of Energy for purchasing more alternative fueled vehicles (the Federal Energy Policy of 1992 established the alternative fuel vehicle purchase percentages for states). The CMP contracted with its fuel provider in September 2000, to purchase 10 percent ethanol blended fuel which will increase consumption in Kansas by 260,000 gallons per year. According to the Kansas Corporation Commission's State Energy Office, there are no funds available under the new Bush energy plan to subsidize the purchase of alternative fueled vehicles.

Bird Proofing of Electrical Transmission Lines

A representative from the U.S. Fish and Wildlife Services explained to the Committee efforts made by the service to

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reduce the number of eagles, raptors (hawks and owls), and other migratory birds that are electrocuted by contact with power lines and distribution equipment. Such contact can result in costs associated with the downtime of transmission lines and outages, which impact utilities and consumers. The Committee was informed that federal courts have ruled that the taking of eagles and other migratory birds by industry, including electric utility companies, regardless of their knowledge or intent, constitutes a violation of federal laws. The representative said the thrust of the Avian Protection Plan is to reduce mortality of raptors through cooperative efforts with the Fish and Wildlife Service and utility companies. At the core of this program is a Memorandum of Understanding (MOU) between the Service and a utility company which establishes policies and procedures to be followed by parties when dealing with eagles or other migratory birds that may be present, injured, or killed on the utility company's property during the tenure of the MOU. If the company voluntarily signs the MOU and does not materially breach its terms, the Service agrees not to use civil or criminal prosecution against any of the company's agents, employees, officers, or directors during the duration of the MOU. The cost of retrofitting lines would depend on the accessibility of the area where the problem occurred and the complexity of the needed line retrofit.

A representative of the Falconry Community informed the Committee that falconers have two important reasons to be interested in the issue of raptor interactions with electrical power utility installations which can result in a raptor's injury or death. The first reason is that falconers partially depend on wild raptor populations as a source of birds for their sport and any factor that negatively affects those wild populations is a concern to that community. The second reason is that when falconers train and hunt with raptors, the birds are placed at risk by environmental factors, including electrical power lines and transformers. He said the cost to replace one of his birds was about $1,000.

A representative of the Audubon Society informed the Committee that raptor electrocutions often cause outages resulting in damaged equipment, safety problems, and loss of service to customers.

The Committee heard a presentation from a representative of Western Resources who informed the Committee that the company requires wildlife protector shields to be installed on all transformer insulators. The Company also takes other precautionary measures, such as using insulated jumper wires between phase conductors and energized transformer bushings, ten foot cross-arms, and fiberglass insulators on the tops of downed guy-wires to prevent them from being a ground for birds. When local conditions warrant, the company also requires installations of extra insulation, different types of bird perch diverters, and substitute perches.

Peak Shaving Devices, Bill Stuffers and Powerstat

Representatives of Western Resources explained that a phase out of a bill credit for peak shaving devices on customers' air conditioners occurred because the costs of the program exceeded benefits. KPL and KGE installed devices that cycled off air conditioner compressors for brief periods of each hour during hot summer weather. The goal was to shave system peaks in a cost-effective manner

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and extend to customers the credit resulting from cost savings. The program failed to work as planned because of mechanical failure by some devices, and improper location of other devices (they were not in the direct sunlight, so they could not reach a high enough temperature to activate). The program also failed because some devices were disconnected by customers, and some customers adjusted their thermostats downward and inadvertently offset the effect of the devices. As a result, payments to customers in the form of credits far exceeded the value of the capacity created by the devices. Other conservation programs are available to the customer. Conservation tips and money-saving ideas are made available to the customer through the company's website and through brochures and videos on making homes more energy efficient. "Bill stuffers" on energy efficiency in cold and hot weather are also included with bills. The company also publishes an energy efficient guide for small businesses.

Another representative of Western Resources explained a KGE experimental program (Powerstat) that allowed customers to pre-pay for utility service by purchasing energy in advance of using it. The amount of energy purchased was programmed onto a card and the customer inserted the card into a card reader which indicated, among other things, the rate at which customers were using the energy they had purchased. He said the experimental program never took off because it was impractical to make prepayment on a card comply with all the terms and conditions of the billing practices which Kansas utilities are subject to. It also was not feasible to program all the components of residential tariffs on a prepaid card.

Energy Assistance Programs

2002 Low Income Energy Assistance Program (LIEAP). A representative of the Kansas Department of Social and Rehabilitation Services informed the Committee that the program is a federally funded block grant program that helps qualifying households pay a portion of their home energy costs. The representative provided the Committee with a background on the 2000-2001 LIEAP benefit programs. Federal funding for the 2002 program is currently unknown, but it is likely that there will be a decrease in funding from the previous year due to the number of supplemental grants received last year.

Weatherization Assistance Program (WAP). A presentation was made by a representative from the Department of Commerce and Housing who said WAP utilizes federal funds to make repairs to low income families' homes with the goal of lowering energy usage and making homes affordable, safer, and more comfortable. WAP serves families who are at or below 60 percent of the state median income, which is $34,317 for a family of four. WAP had an operating budget of $2,852,811 in FY 1999, $3,370,981 in FY 2000, and $3,761,438 in FY 2001.

Alternative Energy Sources

A representative of the Sierra Club provided information on wind energy as an alternative energy source in different states. He said that Kansas is in a precarious position because it relies heavily on coal as a fuel source and the possibility of carbon taxes and mandated reductions over 5 to 10 years may impact Kansas significantly. He added that by incorporating a Renewable Portfolio Standard which enriches the resource mix of re-

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newable energy to nonrenewable, a state receives better protection against price fluctuations. He recommended Kansas adopt a net metering law so farmers, ranchers, and land owners can take advantage of wind energy.

A representative of Coriolis informed the Committee of the potential for wind, biomass, and photovoltaics. He recommended that the state should:

- Allow retail access for renewable generators;
- Reimpose the sales tax on utilities—exempt renewable (utilities and fuels);
- Make the state a major purchaser of renewable energy generated electricity, reaching 50 percent within 5 years;
- Start an aggressive program to fund a broad research program on Kansas renewable energy resources;
- Set minimum standards for wind leases to protect land owners;
- Create a new class of cooperatives for renewable energy development;
- Encourage the Kansas Congressional delegation to support Farm Bill provisions allowing harvesting of CPR land for biomass energy and enrollment of terraces in the grass buffer program;
- Support research and development on biomass harvesting and end use technologies;
- Support the development of biomass fueled combined heat and power projects;
- Expand the Kansas buffer initiative incorporating biomass energy production; and
- Allow true net metering for residential photovoltaic systems.

The Committee also heard from the President of Wind Energy Resource on the history of wind energy and the potential for development in the State of Kansas.

Planning Generation Needs and RTO Choices

A spokesperson from the KCC reported on the possible merger between Southwest Power Pool (SPP) and MISO and also discussed the potential impact of two RTOs serving Kansas. Two RTOs may complicate the functionality and cost of power generation and transmission. The spokesperson remarked how the territory limits are fluid and constantly changing. If the merger or consolidation is finalized, the new organization will operate an interconnected transmission system encompassing over 120,000 megawatts of generation capacity service in all or part of 20 U.S. States and Manitoba, Canada. Offices would be located in Indiana, Arkansas, and Minnesota.

Various companies presented to the Committee their current generation capacity and projected capacity needs for the future. A spokesperson from Sunflower Electric Power Corporation, described the process his company utilizes to provide wholesale power supply to member cooperatives, and stated that Sunflower strives to maintain planning reserves that are equal to 12.0 percent of its firm load as required by the SPP, its regional reliability council. Sunflower has 54.0 percent of its generation fueled

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by coal and 46.0 percent fueled by natural gas.

A spokesperson from KEPCo, described generation planning and fuel mixes. KEPCo's generation requirements grow at approximately 1.5 to 2.0 percent per year and its reserve requirements grow at approximately 1 megawatt or less per year. Its fuel mix is 38.0 percent from nuclear power (Wolf Creek), 20.0 percent from hydroelectric, and the remaining 42.0 percent is supplied by contracts with other power companies. It was the spokesperson's opinion that the possibility of two RTOs serving Kansas would likely cause higher costs for KEPCo, since it does not own any transmission lines and is dependent on nondiscriminatory bulk transmission service in order to economically serve its member cooperatives.

A spokesperson from Midwest Energy, Inc., described his company's generation capacity. Midwest Energy serves 35,000 customers in central and western Kansas and 44,000 natural gas customers. Midwest Energy currently operates 27 megawatts of internal combustion generation capacity, utilizing either natural gas or fuel oil, which represents only a small portion of its peak firm load of 212 megawatts per year. Its fuel mix is 55.0 percent coal and 45.0 percent natural gas or fuel oil. It has a capacity margin of 21.0 percent, and expects to see that margin decline into the 15.0 percent to 17.0 percent range over the next few years. According to Midwest Energy, one RTO serving Kansas would be better than two RTOs.

A spokesperson from Great Plains Energy, or KCPL, described his company's reserve margin and mix of generating resources. On October 1, 2001, KCPL became a subsidiary of Great Plains Energy, a new utility holding company. Great Plains serves over 460,000 customers in Kansas and Missouri, and during the summer of 2001, its load reached a peak of 3,352 megawatts. With an accredited capacity of 3,904 megawatts, Great Plains had a reserve margin of 16.0 percent. Its peak load is expected to grow at a little over 2.0 percent per year. Its fuel mix is 56.8 percent coal, 14.0 percent nuclear, 12.4 percent natural gas, 11.7 percent fuel oil, and 5.1 percent net purchases from other companies.

A spokesperson from Western Resources, Inc., described the reliability assessment of the North American Electric Reliability Council, covering the period between 2001 and 2010. The generation adequacy over that period for the near-term is satisfactory with capacity margins of more than 20.0 percent in 2004. Future uncertainties include transmission access, siting and environmental issues, financing, fuel, and political and regulatory issues. The transmission adequacy assessment concludes that transmission congestion will continue, that additions to the transmission infrastructure are not keeping pace with new generation additions, and that new investment in transmission facilities must be encouraged. The fuel adequacy assessment concludes that coal remains the predominant fuel, that gas generation, which was at 8.0 percent of total in 1991, will be 20.0 percent in 2009, and that near-term gas supplies are adequate, but long-term supply is questionable. The spokesperson's opinion concerning future RTO development was that any development will ultimately reduce transmission congestion through a combination of market forces and new construction, and that competition will be enhanced. The spokesperson mentioned that Western

Resources had issued on October 30, 2001, a termination notice to SPP, but added that the notice can be pulled back at any time. It also was mentioned that the type of generation capacity needed and being implemented by Western Resources, Inc., is not base capacity, but peaking capacity. The percentage of the sale of peaking capacity going to the residential customer is 85.0 to 90.0 percent, and that the residential customer will bear the burden of implementing peaking capacity generation. The spokesperson reviewed the characteristics and functions of RTOs. RTOs have to be independent from the marketing function. They are required to have a specific scope and configuration. They must possess operational authority, as well as achieve short-term reliability. RTOs have a number of functions, such as tariff administration, congestion management, parallel path flows, ancillary services, market monitoring, planning and expansion, and interregional coordination. Given these functions for RTOs, utility companies still retain the physical operation and maintenance of generation facilities, generation and load balance within the control area, and the economic dispatch within the control area. RTOs provide long-term benefits, such as coordinated regional planning, increased service reliability, development of wholesale markets, and improved market supply prices.

A spokesperson from Utilicorp United reviewed RTO issues and discussed Utilicorp's capacity and energy portfolio. Its fuel mix from owned generation is 22.0 percent coal and 48.0 percent natural gas. The fuel mix from purchased contracts is 28.0 percent natural gas and 2.0 percent wind. Utilicorp's total energy portfolio is 803 megawatts. The conferees displayed data showing the daily average megawatt output load the wind turbines at the Montezuma wind farm generated during the month of October 2001. The output load ranged from 2 to 58 megawatts. This variability had been expected and demonstrates a typical output for a month.

The Executive Director of the Kansas Municipal Utilities (KMU) mentioned that many of the municipal utilities purchase their electricity through the Kansas Municipal Energy Agency, the state's municipal joint action agency. It was mentioned that while a KCC survey of public power systems in 1999 indicated a capacity margin of 25 percent, a growing number of systems are facing the potential of reserve deficits. These systems are actively adding city generation or negotiating new wholesale power contracts. It is KMU's opinion that there is a definite trend toward additional generation.

A spokesperson from the Kansas City Board of Public Utilities described to the Committee the efforts being made in building a new power plant at the site of the existing Nearman Creek Power Station on the Missouri River.

Conclusions and Recommendations

The members of the Special Committee on Utilities made several recommendations to the 2002 Legislature on a variety of energy-related issues: federal and state energy policies; electricity infrastructure; and energy conservation incentives.

Energy Policy

The Committee recommends:

- The introduction of a resolution urging the U.S. Congress to proceed with all due haste to approve and begin

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storage of high-level radioactive waste at Yucca Mountain in Nevada. The Committee finds the 2009 time schedule unsatisfactory and would suggest a speedier conclusion to this issue. The Committee recommends introduction of this legislation in the Senate. The Committee's recommendation on this issue was not unanimous.

- The introduction of a resolution urging the U.S. Congress to reauthorize and extend the Federal Tax Credits for wind generation facilities. The Committee recommends introduction of this legislation in the House.
- The introduction of a resolution in the Senate that urges Congress to open Alaska's Arctic National Wildlife Refuge for the exploration of oil. The Committee believes that the United States is too dependent on imported oil and that it needs to find ways to lessen reliance on foreign imports. The Committee's recommendation on this issue was not unanimous.

Electricity Infrastructure

The Committee recommends that an update be provided in a Joint Meeting of the Senate and House Utilities Committees on the topic of RTOs and transmission infrastructure and constraints. The Committee recognizes that the situation presents future problems that should be addressed.

Energy Conservation

The Committee recommends:

- Promotion of energy efficiency and energy conservation efforts overall and increased efforts to educate consumers on ways to improve efficiency and conservation. Education could possibly include reviewing the effectiveness of bill-stuffers. The Committee recommends that during the 2002 Session both the House and the Senate Utilities Committees look into various methods to promote efficiency and conservation.
- Reviewing, during the 2002 Session, efforts to create more awareness of energy assistance programs, and examining what the Department of Commerce and Housing and SRS are doing to alert those consumers who are eligible for the Weatherization Assistance Program.
- Utilization by the Board of Regents of incentives to reduce energy costs.

In addition to various policy recommendations on energy-related issues, the Committee recommends that legislation be introduced to:

- Urge the U.S. Congress to proceed with all due haste to approve and begin storage of radioactive waste at Yucca Mountain in Nevada.
- Urge the U.S. Congress to reauthorize and extend the Federal Tax Credits for wind generation facilities.
- Urge the U.S. Congress to open Alaska's Arctic National Wildlife Refuge for the exploration of oil.

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Special Committee on Utilities

Natural Gas Pricing and Supply

Conclusions and Recommendations

The Committee recommends that a joint meeting of the Senate and the House Utilities Committees take place at the beginning of the 2002 Session, so that members can be briefed on the status of the cold weather rule, consumer debt carryover, and any ad valorem tax court settlements that have taken place between Committee action on this interim report and the commencement of the Legislature in January 2002.

The Committee appreciates the role of the Kansas Corporation Commission (KCC) in monitoring various natural gas issues. The Committee recommends that the KCC be vigilant in protecting the interest of Kansas consumers before the Federal Energy Regulatory Commission (FERC), be alert to the increase in the number of consolidations and mergers, and continue its close scrutiny of natural gas contracts.

The Committee recommends that if the Kansas University Medical Center (KUMC) receives money from a pending lawsuit involving the ad valorem tax refund issue (KUMC belongs to an industrial group which is a plaintiff in the lawsuit), then that same amount shall be reduced from KUMC's operating expenditures. During the 2001 Session, legislation was passed and the KCC issued an order stating that those tax refunds should fund an energy assistance program for low income families.

Proposed Legislation: None.

Background

The Special Committee on Utilities studied issues relating to natural gas pricing and supplies. The Committee was also updated on the status of the ad valorem tax refund issue. The Committee had dealt with the issue during the 2000 Interim. The 2001 Legislature passed legislation that established general policy recommendations on the issue.

High Natural Gas Prices

The high natural gas prices during the latter part of 2000 and continuing into the first part of 2001 raised concerns about the long-term prospects for natural gas prices and their potential impact on consumers and on economic growth. Fueling those concerns were fluctuating levels of natural gas supply in storage. The Committee sought to understand why natural gas prices escalated so quickly. The Committee also wanted to know what the natural gas supply outlook would be for both the domestic and national natural gas markets.

Natural gas represented 24.0 percent of the energy consumed and 27.0 percent of the energy produced in the United

States in 2000. The industrial sector was the largest user of natural gas—for co-generation of electric power and as an industrial feedstock. In addition, natural gas was (and is) the largest energy source consumed in the residential sector and the fastest growing energy source for electricity generation.

The volume of natural gas used in the industrial, residential and commercial, and electricity generation sectors combined with the high natural gas price period raised concerns about the present and future operations of the natural gas industry and markets. The recent high prices called into question whether natural gas can play a dominant role in fueling U.S. economic growth in the next 20 years.

According to the Energy Information Administration of the U.S. Department of Energy, the high natural gas prices experienced in 2000 and 2001 were caused by:

- Constrained domestic productive capacity that resulted from a sustained period of relatively low oil and natural gas prices;
- Unusually high demand which was the result of strong economic growth and an unusually warm summer and cold winter; and
- Low storage heading into the winter season (November 2000 through February 2001).

Across the U.S., low oil and natural gas prices for most of the decade before 2000 contributed to the limited natural gas production capacity going into 2000. Annual average wellhead natural gas prices (in 1999 dollars) hovered between $1.61 per million Btu ($1.65 per thousand cubic feet) and $2.32 per million Btu ($2.38 per thousand cubic feet) through all of the 1990s, while crude oil prices (the composite refiners' acquisition cost) ranged from $12.69 to $22.37 per barrel (excluding 1990). Also, oil and gas investments in exploration and production from 1990 through 1996 were lower than investments before 1986. With the decline in industry investment and drilling during the 1990s, natural gas reserves declined from 169 trillion cubic feet at the end of 1990 to 164 trillion cubic feet at the start of 1999.

Annual U.S. production of natural gas during the 1990s increased modestly, but was short of the average annual growth in demand during that period. In 2000, domestic gas production increased by 0.7 trillion cubic feet in response to the higher demand and higher wellhead prices. While this increase was sufficient to meet the major portion of demand growth seen in 2000, a large net drawdown of gas in storage and an increase in imports were also required to meet the remaining demand.

Demand for natural gas increased by about 1 trillion cubic feet in 2000 because of strong economic growth and higher heating and cooling loads served by natural gas. As compared with 1.7 percent average annual growth in demand for natural gas from 1990 to 1999, demand jumped by 4.8 percent in 2000. More importantly, there was virtually no growth in gas consumption between 1996 and 1999, due in part to mild weather. Because natural gas prices began to rise in the spring of 2000, the refill of gas storage was slowed considerably as the industry waited for a possible return to lower prices. Gas storage injections were minimized as demand growth accelerated during the summer and gas acquisition

costs escalated. In the 6 weeks ending October 31, 2000, natural gas storage was aggressively filled to 2.7 trillion cubic feet. However, the additional demand for filling storage in the 6 weeks before winter only served to keep natural gas prices high, and the total amount of gas in storage at the start of the 2000-2001 heating season began at a 5-year low for that time of year.

The U.S. natural gas market began the winter of 2000-2001 with high prices and a relatively weak storage position. Much colder than normal winter weather in November and December 2000 reduced gas stocks to such low levels that it raised concerns about possible supply shortfalls during peak periods for the remainder of the winter. The high natural gas demand and rapid gas stock drawdown strained U.S. productive capacity and drove up natural gas prices at the wellhead. Natural gas prices rose from less than $2.00 per MMBtu in March and April of 1999 to about $5.00 in September of 2000 and to around $9.00 by January of 2001.

High natural gas prices affected Kansas consumers. For the average Kansas household, the total average gas bill for last winter (November 2000 through February 2001) was $434.07. In contrast, the KCC has forecasted this winter's total average gas bill to be $135.72.

Ad Valorem Tax Refund

The events leading up to the ad valorem tax refund issue are the following:

- In 1954, the U.S. Supreme Court held that the Natural Gas Act, enacted in 1938, allows the federal government to control the price of natural gas at the wellhead if the gas was sold to an interstate pipeline. In accordance with that decision, the Federal Power Commission (the predecessor of FERC) established the rates that could be recovered by natural gas producers and established the highest price (maximum lawful price) that could be charged by producers.
- In 1974, the Federal Power Commission issued Opinion No. 699, which authorized producers to recover "production, severance, or other similar taxes." Producers were able to add on to the maximum lawful price an amount equal to those taxes. The Federal Power Commission issued a subsequent ruling (Opinion No. 699-D), in response to a request by the KCC for clarification, that producers could pass through the taxes to their pipeline customers.
- In 1978, Congress passed the Natural Gas Policy Act. Section 110 of that Act specifically allowed "pass through" of the Kansas ad valorem tax. This authorization included the severance tax which was defined as "any severance, production, or similar tax, fee, or other levy imposed on the production of natural gas."
- In 1983, the Kansas Legislature passed the severance tax. Northern Natural Gas petitioned FERC to reconsider the Federal Power Commission's decision in Opinion No. 699-D. Under Opinion No. 699-D, Kansas producers were allowed to pass through both the severance tax and the ad valorem tax.
- In 1986, FERC rejected Northern's request and reaffirmed its earlier opinion. FERC determined that the Kansas ad valorem tax qualified as a severance tax under Section 110 of the Natural Gas Policy Act of 1978, be-

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cause it was based upon production factors.

- In 1988, Colorado Interstate Gas Company appealed the Northern decision to the United States Court of Appeals for the D.C. Circuit. The D.C. Circuit remanded FERC's order for further explanation as to why the Kansas ad valorem tax qualified as a severance tax that could be added to the maximum lawful price and passed through to customers.

- In 1993, FERC issued an Order on Remand reversing Opinion No. 699-D. This order found that the Kansas ad valorem tax had been improperly added to the maximum lawful prices; the tax should be viewed as a property tax and not as a severance tax within the meaning of Section 110 of the Natural Gas Policy Act. FERC determined that the Kansas tax did not qualify as a severance tax because:

  - It was based upon the value of the gas property rather than upon its current production;

  - The volume of production was relevant principally for determining the present value of the gas reserves; and

  - The reserves were taxed year after year until removed from the ground and sold. FERC ordered natural gas producers to pay refunds and interest on the Kansas taxes they had collected retroactive to June 28, 1988 (the date the D.C. Circuit remanded the case to FERC).

- In 1996, the D.C. Circuit agreed with FERC's reversal of Opinion No. 699-D, but held that the refunds were due retroactive to October 4, 1983 (the date the Northern Natural Gas petition was published in the *Federal Register*). The Court held that once the status of Kansas' ad valorem tax as a recoverable production tax was challenged in 1983, producers were on notice that the recoverability of the tax under Section 110 of the Natural Gas Policy Act was at issue. The Court concluded that producers failed to quantify any harm (*e.g.*, the expenditures made and lost in detrimental reliance upon being able to recover the Kansas tax) they might suffer should they have to recover the full amount they had collected.

- In 1997, Kansas producers filed a petition for adjustment to their potential liability to pay refunds back to October 4, 1983, and requested a generic waiver of interest. On September 10, FERC denied the request for generic relief and established a procedure for the payment of the refunds. Pipelines were directed to bill producers by November 1997, and producers were to pay by March 1998. Producers also were responsible for making refunds of reimbursements attributable to royalty interest owners. However, waivers of refunds could be granted on a case-by-case basis upon a producer's demonstration that collection of the refund was attempted and that the refund was uncollectible. The State of Kansas and KCC filed a petition for reconsideration requesting the opportunity to present evidence to support a case for generic equitable relief to all producers.

- In 1998, FERC issued an order denying reconsideration of the order issued on September 10, 1997. In addition,

FERC denied any generic waiver on the interest to be assessed producers. FERC decided to consider hardship cases on an individual producer basis, thus shifting the burden to producers to show that they do not owe money to pipelines. The State of Kansas and the KCC subsequently filed a petition for review with the 10th Circuit Court of Appeals. Several other appeals were filed and ultimately transferred to the D.C. Court of Appeals.

On the legislative front, the 1998 Legislature passed SCR 1616, which urged the Congress to enact legislation providing relief to Kansas producers from penalties and interest on refunds retroactive to 1983. The 1998 Legislature also enacted HB 2419, which is a statute of limitations on civil actions commenced to collect refunds and interest from royalty owners for the period 1983-1988. FERC subsequently held that the Legislature had no authority to impose a statute of limitations.

- In 1999, the State of Kansas and KCC sought a rehearing of FERC's ruling on HB 2419. FERC denied the request for rehearing and deemed the bill an ad hoc statute of limitations.
- In 2000, Senator Steve Morris, Attorney General Carla Stovall, and the KCC scheduled "FERC settlement conferences" in Topeka between all affected parties. Also in 2000, the Kansas District Court in Stevens County ruled that a lawsuit, filed by four large producers seeking payment from defendant royalty owners, was barred from the statute of limitations. The District Court also ruled that HB 2419, now codified as KSA 2000 Supp. 55-1624 was unconstitutional. The District Court's decision was appealed to the Kansas Supreme Court and oral argument is scheduled for mid-January of 2002.

During the 2000 Session, the Senate Energy and Natural Resources Committee held a hearing on SB 571, and the House Utilities Committee held a hearing on HB 3050. Both bills set up a funding mechanism to enable producers to recover their costs to pipeline companies for refunds, including interest. Although neither bill was enacted, a request was made for an interim study. Accordingly, the Legislative Coordinating Council directed the Special Committee on Utilities to study the dollar amount of the lost value of natural gas taken from Kansas, review state legislation which might mitigate this impact and prevent continued exploitation, and consider possible legislation which would reinstate the Kansas tax policy. The Special Committee declared it fully supported resolution of the issue through fair settlement agreements. The Committee recommended, however, that if negotiations failed to resolve the issue, the Legislature would take appropriate action to prevent a major flow of money out of the Kansas economy which also would result in a major injustice to Kansas royalty owners and a large reduction in the exploration capital of Kansas independent oil and gas producers. The Committee did not recommend any legislation.

Progress of Settlement Negotiations

Settlement negotiations have involved the participation of the KCC and facilitation of the Alternative Dispute Resolution Division of FERC. After two informal settlement conferences in March 2000, it

was decided that settlement negotiations should proceed on each pipeline separately. All five pipeline companies with the vast majority of claims against them are pursuing settlement negotiations: Williams, Northern Natural Gas, Colorado Interstate Gas, Panhandle Eastern, and Kinder-Morgan. Central to these negotiations is the use of data committees to collect financial data on outstanding claims. To date, three settlement offers have been filed with FERC:

- Williams Gas Pipelines Central, Inc. with the Missouri Public Service Commission, Missouri Gas Energy, and 43 working interest owners filed a Superseding Supplemental Offer of Settlement dated August 7, 2000.

- Northern Natural Gas Company filed a comprehensive settlement with FERC on November 20, 2000. Northern asked for a decision on the settlement no later than January 2001, so that refunds can be made to the respective customers of each local distribution company this heating season.

- Colorado Interstate Gas Company (CIG), Public Service Company of Colorado, Cheyenne Light, Fuel and Power Company, Colorado Springs Utilities, and others, filed a settlement agreement with FERC on October 12, 2000. CIG and the other signatory parties asked FERC to approve the settlement agreement no later than November 28, 2000.

Beneficiaries of Settlement Agreements

Under the settlement agreements filed to date, certain producers will be required to pay refunds (in many cases, at a reduced amount than originally assessed) to the interstate pipeline companies that are party to the agreements. Producers participating in the settlement negotiations have agreed to waive any claims they may have against royalty owners. The interstate pipeline companies, in turn, are required to return the refunds attributable to FERC jurisdictional sales to their customers. For the most part, these customers are local distribution companies. The KCC investigated how these refunds would flow from the local distribution companies to their retail customers. The KCC also opened a docket to investigate the collection of refunds by the pipeline companies that were not subject to FERC's jurisdiction (direct sales).

Current Status of Ad Valorem Tax Refund Matters

On May 3, 2001, the KCC issued an order announcing it was following the general policy considerations recommended by the Kansas House in HR 6006 and by the Kansas Senate in SR 1808. Accordingly, the KCC established a low income energy assistance program to be funded with ad valorem tax refunds currently held in escrow and subsequently recovered by various Kansas local distribution companies. Participation by Kansas customers who qualify under the KCC's guidelines has been considerable, and the KCC may be required to utilize all of the ad valorem tax refunds to fund the program. Since the KCC's May 3 Order, numerous appeals have been filed in United States Court of Appeals for the District of Columbia, United States District Court for the District of Kansas, the Court of Appeals of the State of Kansas, and the District Court of Johnson County, Kansas. These appeals challenge the KCC's authority to directly distribute the gas supplier refunds. The appeals have

slowed the refund process, and the tax refund moneys currently held in escrow are not sufficient to fully fund the low income energy assistance program established by the KCC. The additional moneys, now stalled by the appeal filed at the United State's Court of Appeals for the District of Columbia of a FERC settlement, are necessary to fully fund the program.

A spokesperson from KUMC informed the Committee that the industrial group KUMC belongs to is a plaintiff in a court case involving the ad valorem tax refund issue. According to the spokesperson, such involvement in an industrial group that purchases a large volume of natural gas was justifiable in that it was more cost-effective. The Committee suggests that the State of Kansas should not be spending money on attorney fees for participation of KUMC in this case. The source of these funds should be further explored and known. The spokesperson commented that the attorneys for the lawsuit work on an hourly basis, but that moneys paid by KUMC are distributed on a contractual basis and then spread out among the group of attorneys. The spokesperson told the Committee that KUMC's involvement in this case is only because it belongs to the industrial group. According to the spokesperson, the money used for attorney fees is not likely to come out of the general use budget of the university, but rather to come out of private funds. The Committee feels that KUMC would have been completely under the state financial umbrella at the time it entered into the lawsuit. It appears that the state is fighting the state if state dollars are being used for litigation procedures.

Committee Activities

The members of the Special Committee on Utilities heard presentations concerning natural gas pricing and supply on October 10 and November 7, 2001. On October 10, the Committee heard presentations from the following:

- Charles B. Wilson, Vice-President of Finance, Berexco Inc., reviewed natural gas spot sales versus contract prices;
- Kevan Vick, General Manager, Nitrogen Manufacturing, Farmland Cooperative System, submitted written testimony concerning the decision to halt production at the Kansas Nitrogen Facility in Lawrence;
- John Cita, Chief Economist, KCC, reviewed the natural gas price forecast for the coming winter season;
- Representatives from BP Amoco, Duke Energy Field Services, and from Williams Companies, described natural gas supply forecasts and discussed changes in gas gathering rates;
- Bob Courtney, Energy Manager, Olathe School District, described the situation school districts face when contracting for the purchase of natural gas;
- Staff from the KCC summarized the audits performed on the annual purchase gas adjustments; and,
- Montgomery Escue, Agricultural Energy Services, and Justin Hamblin, Executive Director, Southeast Kansas Irrigation Association, described the issue of natural gas pricing and consideration of the impact on irrigation

systems farmers use.

On November 7 and 8, the Committee heard presentations from the following:

- William Eliason, Vice President—Gas Strategy, Kansas Gas Service, a Division of ONEOK, described the natural gas resource planning process;
- Steve C. Johnson, Kansas Gas Service, described the Cold Weather Rule, mentioned consumer debt carryover, and updated the Committee on the ad valorem tax issue; and,
- H. Edward Phillips, Vice Chancellor for Administration, KUMC, answered questions concerning KUMC's involvement in the ad valorem tax court settlement.

Natural Gas Pricing and Supply

The Committee heard a presentation concerning spot sales versus contract prices of natural gas. The Committee was informed that there is a diminishing quantity of wellhead gas tied up with old fashioned long-term contracts. Most gas is sold based on terms tied to futures contracts. It was stated that approximately one-third of wellhead gas is sold on month-to-month futures based pricing. When a significant volume of futures contracts are traded, spot prices experience volatility. Many factors, such as weather, perceptions of storage inventories, disruptions of main transmission pipelines, and politics, contribute to the volatility. To reduce this price volatility, producers contracted for term pricing at $3, $4, or $5. The Committee also was informed that the limited period of high natural gas prices resulted from a sustained period of relatively low oil and gas prices, followed by unusually high demand, poor gas storage heading into winter, and bottlenecks at certain pipeline hubs. One natural effect arising from high natural gas prices has been a dramatic increase in domestic drilling for new supplies of natural gas.

The Committee received written testimony in response to the Committee's query about the causes for the Lawrence nitrogen facility closure by Farmland Industries. The testimony explained that the causes for the facility closure were not due to higher natural gas prices.

A representative of the KCC testified that the natural gas supply outlook for the end of 2001 and into 2002 appears near record levels. Hence, the price forecasts for the same period appear to be between the $2.50 to $3.00 per mmBtu level. Compared to last winter's actual average price of $6.89, the current winter price forecast of $2.61 per mmBtu is a difference of $4.28 per mmBtu. This would lower a typical Kansas household natural gas bill by approximately $300.

The Committee was informed by a representative of the Natural Gas Supply Association that there will be a downward prediction on the price for natural gas for year 2001-2002. Such a prediction is based on a slowing economy, normal predicted winter temperatures, increased production, normal demand, and more storage of natural gas. The question arises as to what Kansas can do. Given that natural gas is an international commodity, the answer is limited. According to the spokesperson, what Kansas should do is encourage investment in its mature gas production fields. It can eliminate the price limitations on the incentives for additional drilling, workovers, and other factors now found in statute. It also can make more realistic the definition of a gas

stripper or marginal well. Such wells receive special tax considerations to extend their economic life. The current definition is a well producing less than $89.00 worth of gas daily. The definition should be changed to include gas wells producing 90 or 120 Mcf/d of gas. According to the spokesperson, this can extend the economic life of an increasing number of natural gas wells in the state.

A representative for the Williams Companies, which is an integrated energy company headquartered in Tulsa, Oklahoma, and which engages in producing, gathering, transporting, and marketing of energy products, addressed the subject of gas gathering. Gas gathering is a crucial part of the logistical process of natural gas production that provides a mechanism for natural gas to be transported and aggregated from the wellhead to central transportation points of interstate pipeline networks. The gathering service is governed by long-term, private contractual agreements entered into by companies such as Williams and their producer customers. The rates charged for gathering the gas and the fuel used to operate the compression on the system is calculated on a semi-annual basis. It was the spokesperson's opinion that the availability of gas storage facilities in Kansas creates greater stability in the supply of gas and allows Kansas utilities to better manage their gas inventories.

A representative of Duke Energy gave a brief overview of natural gas supply for the Hugoton field, natural gas supply for irrigation, and natural gas gathering rates in Southwestern Kansas. It was mentioned that the Hugoton field could supply 12 more years of gas at today's production rates. The life of the field would more likely continue for 15 to 20 years, but at significantly reduced rates. The spokesperson concluded that a new set of challenges will face gas producers, irrigation fuel customers, and gas gathering service providers over the next 10 to 20 years. Producers and customers will have to deal with declining reserves.

The Energy Manager for the Olathe School District described the impact high natural gas prices had on school district energy costs. There are two buying groups of natural gas to support school districts. One is sponsored by the Kansas Association of School Boards. The other is the Greenbush Energy Group, which is associated with the Southeast Kansas Service Center at Greenbush, and which is comprised of about 50 school districts. These groups aggregate, for bidding purposes, around 850 MCF, and in spite of the high gas prices of last year, saved around $160,000 in state-allocated tax dollars—dollars that went for education purposes rather than energy purposes.

A spokesperson from the KCC reported on the status of the ad valorem tax refund and corresponding court settlements. On May 3, 2001, the KCC issued an order announcing that it was following the general policy considerations recommended by the Kansas House in HR 6006 and by the Kansas Senate in SR 1808. The KCC established a low income energy assistance program to be funded with ad valorem tax refunds currently held in escrow and subsequently recovered by various Kansas local distribution companies. As a result of the KCC's May 3 Order, numerous appeals have been taken to the courts of several jurisdictions. These appeals challenge the KCC's authority to direct distribution of gas supplier refunds and have slowed the refund process.

The Committee heard testimony from KCC regarding the purchase gas adjust-

ment (PGA) clause, which is the mechanism whereby gas utilities are permitted to recover the fluctuating costs of gas from the ratepayers. The objectives of the audits are:

- To verify the accuracy of the monthly Settlement Computations submitted by natural gas distribution companies (LDCs) in accordance with KCC Docket No. 106,850-U;
- To ensure the actual cost adjustment computed by the LDC reflects actual recoveries and sales;
- To ascertain that the Actual Purchased Gas Costs to be recovered are supported by vendors' invoices and that the deferral account does not include inappropriate costs; and,
- To verify that the PGA factor used to calculate customers' bills agrees with the calculation that the company files with the KCC.

The Committee asked the KCC to furnish more detail concerning the objective of verifying the accuracy of the monthly settlement computations.

The Committee heard from two conferees representing Kansas irrigators, including a spokesperson for the Southwest Kansas Irrigators Association, who shared their views on natural gas prices. The price of various energy sources for irrigation operations was reviewed. The Committee learned how some farmers are purchasing natural gas as an association and thereby getting a negotiated price for natural gas. It was explained that each day irrigators must estimate the amount of natural gas they will require. One conferee expressed a concern about certificated and noncertificated areas for access to wellheads for gas use in irrigation motors.

A spokesperson from ONEOK, Inc., informed the Committee on the logistics of Kansas Gas Service, which is a division of ONEOK and provides service to 635,000 customers in 340 Kansas communities. The spokesperson mentioned that deregulation has caused an efficient deployment of capital dollars and the efficient utilization of physical resources (storage) and creativity (financial markets), but it has also led to volatility. Local distribution companies (LDCs) are experiencing minimal sales growth at 1.0 percent per year. In the future, LDCs will have to compete for gas supply and pipeline capacity with industrial and electrical generation consumers. Also, the total national gas sales growth is accelerating significantly primarily because of electrical generation. Because the location of gas supplies is shifting to other areas, new pipelines must be built to access new sources of gas supply, such as Canada, deep water offshore drilling, the Rockies geographical region, Asian imports brought in by ship, and Alaska. It was mentioned that when the supply of gas is constrained and the price of natural gas is high, LDCs (residentials) buy the gas required for heating, while industrial facilities curtail operations. The spokesperson concluded that natural gas market volatility is here to stay, but can be reduced with hedging. He also concluded that the natural gas industry will continue to become more efficient, and that federal restrictions on the construction of natural gas pipelines that artificially hinder construction or full utilization of existing infrastructure need to be lifted.

A spokesperson from the Kansas Gas Service informed the Committee on the issue of the Cold Weather Rule. The Rule

was put together before 1976, and it is included in docket 106-5010U. The Rule states that consumers can apply to meet the good faith test and can enter into an agreement to apply for assistance to help meet their payments. The rule is designed to minimize the risk of harm to human health and life during winter months due to a severance of utility service for non-payment of utility bills. Many customers have applied to the gas company to make these payments. Because of the severity of last winter, many consumers experienced difficulty paying their high heating bills. If consumers do break their payment plan, they can requalify under the KCC's "Good Faith Test." The emerging problem, according to the spokesperson, is that customers on the Rule are not making their payments. The spokesperson suggested that one way to quantify the number of customers who are taking advantage of the system is to look at the pattern of payments made by these customers. The Cold Weather Rule only applies to residential customers who belong to regulated companies.

The Committee has received testimony that the volume of natural gas futures being traded in a single year is equal to ten times the volume of gas consumed annually in the United States. The Committee points out that the KCC is currently doing a good job conducting contract reviews. The contract review process is not open to the public. The KCC conducts three types of reviews: 1) a monthly review of gas contracts, or the cost of gas purchased; 2) an accounting review at the end of each year; and, 3) an annual "tune-up." The Committee would note that the KCC has not identified any unresolvable concerns after performing such reviews.

Conclusions and Recommendations

The Special Committee on Utilities made several recommendations to the 2002 Legislature on issues related to natural gas.

Ad Valorem Tax Issue

The members of the Committee recommend:

- That a Joint meeting of the Senate and the House Utilities Committees take place during the beginning of the 2002 Legislative Session so that members can be briefed on any court settlements that have taken place between Committee action on this interim report and the commencement of the Legislature in January 2002.

- That if the KUMC receives money from a pending lawsuit involving the ad valorem tax refund issue (KUMC belongs to an industrial group which is a plaintiff in the lawsuit), then that same amount shall be reduced from KUMC's operating expenditures. During the 2001 Session, legislation was passed and the KCC issued an order stating that those tax refunds should fund an energy assistance program for low income families. The Committee suggests that the State of Kansas should not be spending money on attorney fees for participation of KUMC is this case. The Committee feels that KUMC would have been under the state financial umbrella at the time it was paying attorney fees, and that it seems that the state is fighting the state if state dollars are being used for litigation procedures.

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Natural Gas Pricing and Supply

The members of the Committee recommend that:

- The KCC be vigilant in protecting the interest of Kansas consumers before the FERC. Because energy regulation is increasingly concentrated at the federal level, the state will have to play a vital role in the decisions that FERC will make. The role of KCC would be to educate the consumer in the unregulated aspects of the natural gas industry. The state is increasingly becoming an importer versus an exporter and will become more dependent on FERC actions in the future.
- KCC be alert to the increase in the number of consolidations and mergers. The Committee appreciates the role of KCC in monitoring the proposals or rate cases presented to them. The Committee recognizes that KCC will be playing an increasing role in analyzing the mergers and acquisitions in the natural gas industry.
- KCC continue its close scrutiny of natural gas contracts.
- That a joint meeting between the Senate and the House Utilities Committees take place during the beginning of the 2002 Session so that members can be brought up to date on the status of the Cold Weather Rule and consumer debt carryover. The Committee feels there is enough interest in the issue to generate possible action.

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