

MINUTES OF THE SENATE UTILITIES COMMITTEE

The meeting was called to order by Chairman Stan Clark at 9:30 a.m. on February 5, 2004 in Room 526-S of the Capitol.

All members were present.

Committee staff present:

Bruce Kinzie, Revisor of Statutes
Raney Gilliland, Legislative Research
Ann McMorris, Secretary

Conferees appearing before the committee:

Susan Cunningham, General Counsel, KCC
Stuart Lowry, Corporate Counsel, Kansas Electric Cooperatives

Others attending:

See Attached List.

Chairman Clark opened the hearing on:

SB 310 - Public utilities subsidization of non-regulated affiliates

Proponents:

Susan Cunningham, General Counsel, Kansas Corporation Commission, noted that KCC supports **SB 310** as it is designed to prevent regulated public utilities from using their regulated operations to subsidize their non-regulated operations or to impair the financial integrity of the public utility, as well as to protect ratepayers from the financial burdens and related risks associated with non-regulated affiliates. **SB 310** clarifies the Commission's authority to develop comprehensive rules and regulations which would address the primary issues of cost allocations and pricing guidelines between regulated utilities and their affiliates. She provided a copy of **Senate Bill 310** with revised language as proposed by the KCC. (Attachment 1)

Much discussion and questions regarding two issues (1) appropriate pricing and (2) proper allocation to deal with subsidies.

Stuart Lowry, Corporate Counsel for Kansas Electric Cooperatives, Inc. supports **SB 310** and KCC proposed language changes. (Attachment 2)

Chair asked if there were any others present who wished to speak on this matter. None were forthcoming.

Chair closed hearing on **SB 310**.

The next meeting of the Senate Utilities Committee is February 9, 2004.

Adjournment.

Respectfully submitted,

Ann McMorris, Secretary

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SENATE UTILITIES COMMITTEE GUEST LIST

DATE: February 5, 2004

Name	Representing
DAVE HOLTHUIS	KEC
STUART LOWEY	KEC
SUSAN CUMMINGS	KCC
MARK SCHREIBER	Westar Energy
TOM DAY	KCC
Ron Seiber	Gov Law Firm
Bruce GRAHAM	KEPL
Amy Campbell	Midwest Energy, Inc.
J. Long	AQUILA, INC.
Whitney Damron	KS Gas Service
STEVE JOHNSON	Kansas Gas Service
Sandy Braden	KCP

**BEFORE THE SENATE UTILITIES COMMITTEE
PRESENTATION OF THE KANSAS CORPORATION COMMISSION
FEBRUARY 5, 2004**

SENATE BILL 310

Thank you, Chairman, and members of the Committee. My name is Susan Cunningham, General Counsel for the Kansas Corporation Commission (Commission). I appreciate the opportunity to testify on behalf of the Commission on Senate Bill 310.

In the past few years, certain external and internal factors have caused many public utilities with non-regulated affiliates to experience financial difficulties, up to and including loss of investment grade rating, delisting from the NYSE and potential insolvency. The purpose of this proposed legislation is to prevent regulated public utilities from using their regulated operations to subsidize their non-regulated operations or to impair the financial integrity or creditworthiness of the public utility, as well as to protect ratepayers from the financial burdens and related risks associated with non-regulated affiliates.

There is an inherent tension between regulated public utilities and their non-regulated affiliates: that is, through the process of regulation, the regulated utility is given the opportunity to recover its public utility-related costs and earn a fair rate of return, while at the same time its non-regulated affiliate is seeking opportunities and sources of funding to bolster its finances and gain a competitive advantage. Senate Bill 310 is intended to eliminate the tension on regulated operations and ratepayers by expressly clarifying the Commission's authority to develop comprehensive rules and regulations which would establish standards of behavior between regulated entities and their unregulated affiliates. The envisioned rules and regulations would address the primary issues of cost allocations and pricing guidelines between regulated utilities and their affiliates. An initial set of rules applying to electric and natural gas public utilities has

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already been drafted by Commission Staff and the Commission has held a roundtable discussion on those proposed rules. Comments were received by industry participants and Staff is in the process of incorporating many of those comments into its next round of proposed rules.

Joint comments submitted by a group electric cooperative utilities involved whether cooperatives should be subject to certain affiliate rules. The argument was made that incentives for affiliate abuse do not exist when the owners of the public utility are one and the same as the consumers. Electric cooperative representatives met with us to discuss the possibility of revising Senate Bill 310 in a way which recognizes the cooperatives' unique corporate governance and structure while at the same time preserving the Commission's authority to protect ratepayers. The Commission and the coops ultimately agreed upon the revised language which appears on Attachment A to this testimony.

The Commission certainly has general authority to do all things necessary to protect ratepayers as evidenced by its exercise of that general authority in significant dockets pertaining to Westar and Aquila. After lengthy investigations and hearings to determine whether Kansas ratepayers have suffered from corporate actions attributable to affiliates, the Commission ordered remedial actions. The Commission believes that specific express language articulating the public policy that ratepayers will not pay for or suffer from the effects of investments in non-regulated businesses will clarify Commission expectations. This is especially important in light of the proposed repeal of certain historic federal protections such the Public Utility Holding Company Act. For the reasons described in this testimony, the Commission respectfully requests that you favorably pass out Senate Bill 310, as amended in Attachment A to this testimony.

Unless there are questions from the Committee, I have no further comments on Senate Bill 310. Thank you for the opportunity to appear before you this morning.

Revised Language for Senate Bill 310
Proposed by the Kansas Corporation Commission

Section 1. (a) The state corporation commission shall ensure that a public utility, as defined in K.S.A. 66-104, and amendments thereto, does not use regulated operations to subsidize nonregulated activities of such utility or to subsidize activities of an affiliated entity. Except in rate making, revenue requirements, cost of service or similar proceedings, this paragraph and any rules and regulations of the commission adopted pursuant to this paragraph shall not apply to any member or consumer-owned public utility.

(b) The commission shall ensure that the nonregulated activities of a public utility or affiliated entity do not materially impair the finances or credit of a public utility.

(c) The commission shall have full power and authority to adopt all reasonable and necessary rules and regulations and orders for carrying out this section.

(bd) As used in this section:

(1) "Affiliate" or "affiliated entity" means any person, including an individual, corporation, firm, partnership, limited liability partnership, limited liability company, corporation or firm, corporate entity or subsidiary, ~~and~~ nonutility business unit which is not a public utility and which directly or indirectly, through one or more intermediaries, is controlled by or is under common control with a public utility.

(2) "Control", including the terms "controlled by" and "common control", means the direct or indirect possession of the power to direct or the ability to cause the direction of the management or policies of an entity. Control may exist whether the power to direct or ability to cause the direction is exercised alone, through one or more intermediary entities or in conjunction with or pursuant to an agreement with one or more other entities. Control may be exercised through a majority or minority ownership or voting of securities, common directors, officers or stockholders, voting trusts, holding trusts, affiliated entities, contract or any other direct or indirect means. The beneficial ownership of 10% or more of voting securities or partnership interest of an entity constitutes control for purposes of this article.

(3) "Non~~utility~~regulated activity" means all business activities, whether performed by the public utility or an affiliate, not involving the utility business for which the public utility is certificated.

(4) "Nonutility business unit" means any division, business unit, employee or group of employees of a public utility conducting a non~~utility~~regulated activity.

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

**JOINT TESTIMONY SUBMITTED TO THE
SENATE UTILITIES COMMITTEE**

SB 310

By

Kansas Electric Cooperatives, Inc.

Kansas Electric Power Cooperative, Inc

Sunflower Electric Power Corporation

February 5, 2004

Thank you, Mr. Chairman and members of the Committee for providing us an opportunity to speak today on Senate Bill 310, a proposal to codify the Kansas Corporation Commission's authority to ensure that a public utility, as defined in K.S.A. 66-104 does not use regulated operations to subsidize non-regulated activities of such utility or to subsidize activities of an affiliated entity. My name is Stuart Lowry. I am corporate counsel for Kansas Electric Cooperatives, Inc., the statewide association of electric cooperatives in Kansas.

The study of the issues addressed in SB 310 actually began on June 6, 2003, when the KCC Staff issued a draft of proposed affiliate regulations. On July 10, 2003, the KCC held an informal roundtable discussion during which the Commission heard the comments, concerns and suggestions of the participants concerning the Commission's draft of the proposed affiliate regulations.

During this proceeding joint comments were offered to the KCC by the Kansas Electric Cooperatives, Inc., Kansas Electric Power Cooperative, Inc., Kansas Municipal Energy Agency, Inc., Midwest Energy, Inc., Pioneer Electric Cooperative, Inc., Sunflower Electric Power Corporation, and Wheatland Electric Cooperative, Inc. regarding the proposed affiliate regulations. Each of these entities is a consumer-owned electric utility. The activities and affairs of each of these consumer-owned utilities are governed by representatives elected from among the consumer-owners. In the case of an electric cooperative, the affairs and activities of the

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cooperative are governed by a board of trustees elected from among the membership. In the case of a municipal supplier, the affairs and activities are governed either by a board of public utilities or by the city council or commission. Due to the unique ownership and governance of consumer-owned utilities, we do not believe that incentives exist for subsidy abuses because the owners of the public utility are one and the same as the consumers.

Moreover, Senate Bill 310 and the proposed affiliate regulations also present unique operational problems for the consumer-owned segment of the industry. For example, electric cooperatives are member-owners of many other entities organized on a cooperative basis that provide various services to the electric cooperatives, such as insurance services (Federated Rural Electric Insurance Exchange), data processing services (National Information Solutions Cooperative), fuel procurement services (Western Fuels Association), generation resource management and consulting (ACES Power Marketing), financing (National Rural Utilities Cooperative Finance Corporation, and CoBank), telecommunication services and Internet access (National Rural Telecommunication Cooperative) and association services (National Rural Electric Cooperative Association, and Kansas Electric Cooperatives, Inc.). Our concern was that the result of Senate Bill 310 and the KCC's proposed affiliate regulations would be that each of these entities would be affiliates, and thus regulated under the rule.

Since the bill introduction we have worked with the KCC to address the unique concerns of the member-owned segment of the electric utility industry in Kansas. We believe the bill as modified and presented to you today by the KCC addresses these concerns. As you can see, the electric cooperatives would not be subject to the proposed KCC rule, the intent of which is to allow the KCC stand-alone authority to address issues arising out of subsidies to non-regulated activities and affiliated entities. The KCC would, however, be able to address any subsidy concerns specific to electric cooperatives in the context of a rate proceeding.

This approach is similar to the approach utilized by the State of

Missouri where the affiliate regulations do not apply to municipal suppliers or electric cooperatives.

We thank you for the opportunity to comment and explain the bill modifications described in the testimony of the KCC.