THE STATE CORPORATION COMMISSION
OF THE STATE OF KANSAS

Before Commissioners: Brian J. Moline, Chair
Robert E. Krehbiel
Michael C. Moffet

In the Matter of the Applications of Westar Energy, Inc and Kansas Gas and Electric Company for Approval to Make Certain Changes in their Charges for Electric Service.	)))))	Docket No. 05-WSEE-981-RTS

Joint Reply Comments of CURB, KIC and USD 259

The Citizens' Utility Ratepayer Board (CURB), the Kansas Industrial Consumers Group, Inc. (KIC), and Unified School District No. 259 (USD 259) (jointly, the Intervenors) respond jointly, as follows, to the *Comments of Westar Energy and Kansas Gas and Electric Company Concerning Procedures to be Followed on Remand* (Comments), which were filed in the above-captioned docket on December 18, 2006. Reply comments on or before January 5, 2007, are permitted by the November 20, 2006, Order of the Kansas Corporation Commission (KCC or Commission) requesting comments from the parties following judicial review of the Commission's final order on Westar's application for a rate increase in this docket.

I. Increasing the return on equity to offset the removal of terminal net salvage would be arbitrary and contrary to the evidence in the record.

1. In its Comments, Westar argues that the Commission should increase the company's return on equity to offset the "effect that removing terminal net salvage has on the reasonableness of its rate order." (Comments, ¶26). However, it would be entirely unreasonable for the Commission to increase the company's return on equity in order to provide Westar

revenues to replace those revenues included in consumer rates that are attributable to costs that the court found that the company is not incurring. The very suggestion that rates should be increased to give Westar money for expenses it does not have is repugnant to the principles of ratemaking and would be arbitrary and capricious if adopted. Westar's proposal should be summarily rejected by the Commission.

2. It must be remembered that the Commission Staff opposed inclusion of the terminal net salvage claim, and the Commission adopted an ROE within Staff's recommended range. The Commission cannot reasonably increase the ROE now, because Staff's position on the rate of return was developed in tandem with Staff's position that the terminal net salvage claim should be denied. In other words, the company is facing no more risk now than Staff had anticipated in recommending its ROE. The ROE the Commission adopted was therefore appropriate for a company that does not include terminal net salvage in rates. There is no need whatsoever to reopen the record on the ROE, as Westar characterizes it, "to reflect the effect that removing terminal net salvage has on the reasonableness of its rate order, Westar's investment risk and cost of equity," (*Id.*, at ¶26). The removal of the terminal net salvage claim had already been factored into Staff's recommended range for the ROE. If the Commission were to increase the rate of return on equity—an issue that was not appealed by any of the parties—the Commission would necessarily have to find that its previous determination of the ROE was arbitrary and capricious. The record does not support such a determination. Furthermore, the recent history of Westar's stock performance is a matter of public record, and it would not require reopening the record in this case for the Commission to ascertain for itself that the public record does not support such a determination, either. There is simply no justification for

reopening the record.

3. However, if the Commission adopts Westar's proposal to reopen the case for new evidence, then the Commission must be prepared to hear re-argument of much of the evidence that has been introduced in this case, as well as new evidence on the unreasonableness of increasing the return on equity to "replace" the revenues the company failed to prove up. If the evidence is reopened on the basis of Westar's argument that its investment risk is increased as a result of the Court of Appeals decisions, then the Commission must allow the Intervenors to introduce evidence that there was no negative impact. Additionally, reopening the record would require opening the door to evidence of whether the performance of utility stock is subject to other influences beyond a few accounting adjustments made in a rate case, which could result in extended debate. There most certainly will be disagreements over the extent to which stock performance accurately reflects investment risk. Disputes over the ROE in testimony and at the hearing are usually among the most contentious and time-consuming issues in any rate case. Add the issue of whether Westar's investment risk has been negatively or positively affected by the appellate decisions—and whether that is even relevant to the Commission's duty to carry out the will of the Court of Appeals—and the hearing will be even more time-consuming. There would be no quick resolution of this case, because there is simply no way for the parties to present substantial evidence and arguments on such controversial subjects in a few hours. It is not unreasonable to expect that the hearing on these issues alone would take several days.

4. By addressing what may happen if another hearing is held, the Intervenors do not abandon their contention that there is no need for the Commission to receive new evidence or hold another hearing. The Intervenors also do not abandon their basic position that the Court of

Appeals ordered the Commission to remove the costs of future terminal net salvage in calculating the company's revenue requirement: increasing the ROE to offset their removal would be an act in deliberate evasion of the court's holding that Westar may not charge customers for future costs that it has not proven it will incur. However, if the Commission reopens the docket to allow Westar the opportunity to offer argument or new evidence, due process demands that the Intervenors are afforded the same opportunity. They do not intend to let the opportunity pass.

5. In summary, Westar's suggestion that the Commission should increase the company's return on equity to offset the reduction in revenues for costs that the Court of Appeals found were nonexistent would produce the untenable result that a company that fails to bring forth substantial evidence of its claims for costs and expenses would receive a higher ROE than another company that did. To adjust the ROE so that Westar may evade the consequences of failing to prove its claims would prove that the entire process of setting rates of return is arbitrary—that all the work that the parties and the Commission expended in an effort to establish a fair and reasonable ROE in light of the fact that Westar was to be granted an ECA and the environmental surcharge was just a wasted effort, to be discarded and ignored if the Commission decides the company should recover a certain amount of revenue, regardless of the lack of supporting evidence in the case. To do so would also invite additional appeals.

II. The TDC refunds may not be calculated based on rates not yet approved by the KCC, and the November 2006 FERC rate may only be implemented prospectively.

6. Westar sought to implement a transmission delivery charge (TDC) in the rate case, but the Court of Appeals held that the Commission did not implement the TDC in

compliance with the statute permitting utilities to charge their transmission costs in a separate line item. Westar is in accord with the Intervenors that the TDC cannot be implemented in this proceeding. However, Westar wants to continue charging for some of its transmission costs in a separate line item—which is simply not contemplated by the statute requiring "revenue-neutral" implementation of a line-item charge for transmission.

7. Westar also states in its comments that the refund related to transmission costs is "not directly related to the Court's ruling on the TDC." (¶36) Westar fails to acknowledge that the court based its decision that the TDC as implemented was not revenue-neutral, and therefore illegal, on the fact that the Commission approved a settlement that allowed the company to collect $13 million more for annual transmission costs in the TDC than the company had requested in its application. The amounts illegally charged to customers since the rate went into effect must be returned to customers, regardless of whether the TDC is implemented in this case or not.

8. Westar's revelation that the final FERC rate that was approved on November 7, 2006, was lower than the interim rate on which the Commission based the revenue requirement in this case aptly demonstrates the folly of attempting to set rates in anticipation of proceedings that are not yet final. As a result, customers have been overcharged for transmission for nearly a year. Since the Court of Appeals found the overcharges to be illegal, they must be refunded. The refunds to customers must be calculated based on Westar's filed costs for transmission (based on the FERC rates in effect during the test year), from the day the new rates were charged up to the date that the Commission orders new rates on remand. That is the only way to properly refund the amounts illegally charged to customers. The November 2006 FERC rates are irrelevant to the

calculation of refunds, because the Commission may not retrospectively approve their inclusion in rates.

9. The Commission may, as Westar notes, recognize known and measurable changes in Westar's costs and allow the company to collect sufficient revenues to cover its costs. However, the Commission can only change rates *prospectively*. The Commission may, if it finds evidence supporting the change, issue an order on remand approving the inclusion of Westar's costs under the November 2006 FERC rates in consumer rates, but it can only do so prospectively. To do otherwise is retroactive ratemaking. For the period from January 2005, when the illegal TDC went into effect, until a final order is issued on remand that eliminates the TDC, Westar must refund the amounts illegally collected from customers under the TDC, which are the amounts over and above the final FERC rate that was in effect during the test year. Even if Westar can prove that it incurred higher costs during the refund period, Westar cannot calculate refunds based on those higher costs because they were not approved for inclusion in customer rates by the Commission at that time. Allowing Westar to take into account the "known and measurable" change in FERC rates in November to calculate refunds to customers prior to the Commission's approval of the November 2006 FERC rate for inclusion in customer rates would be retroactive ratemaking, which is not permitted under Kansas law. The Commission may, prospectively, approve the inclusion of the new November 2006 FERC rate in Westar's retail rates on remand, but the new FERC rate may not be used to reduce refunds from rates illegally charged in the past. The Commission must order Westar to base the amounts refunded to customers on the final approved FERC rate that was effective when the company filed its application and the Commission issued its rate case order. To do otherwise is retroactive

ratemaking and will invite further appeals.

III. There are no factually incorrect rulings in previous cases that would justify changing the policy on the LaCygne 2 accounting treatment.

10. Regarding the deficiencies that the Court of Appeals found in the Commission's reversal of the accounting treatment of the Lacygne sale and leaseback, Westar proposes that the Commission may simply declare that its ruling in the 2001 rate case was "factually incorrect" (¶10) to correct the deficiencies in the Commission's ruling in this case. However, the Commission would have to rewrite history in order to justify its reversal.

11. As noted in the 2001 rate case order, the basis for the accounting treatment was set forth in a 1987 order, of which the company did not seek reconsideration by the Commission nor review by the court. Although the issue was proposed by Staff in the 1997 rate case, the 1997 case was settled and the Commission's order approving the settlement did not address this specific issue. In the 2001 rate case, Staff and KIC proposed the treatment again. The company objected to the proposed accounting treatment as not what the company had intended to propose in 1987, but the Commission said "what is controlling is the language in the Order and the intent of the Commission . . . . The provisions of the 1987 Order are clear and reasonable." (Order on Rate Applications, Docket No. 01-WSRE-436-RTS at ¶76.) After Westar petitioned for reconsideration of the issue on the basis that the Commission was improperly giving all the benefits of the LaCygne transaction to ratepayers, the Commission stated that "both shareholders and ratepayers have benefitted [sic] from the LaCygne transaction." (Order on Reconsideration, Docket No. 01-WSRE-436-RTS at ¶17). The Commission stated that the 1987 Order "spent

several pages discussing the necessary benefits to ratepayers," and having considered and rejected the contention that the company was unfairly treated by the ruling, stated that the company was making an effort "to change the terms of an Order 14 years after it was filed." (*Id.* at ¶18.) The Commission unequivocally stated that "the Commission is following and implementing the clear requirements of the 1987 Order." (*Id.*)

12. It must be noted that there were no dissents filed by any of the Commissioners in issuing the 1987 Order, the 1997 Order, or the 2001 Order. The orders were unanimous.

13. Additionally, Westar appealed the issue to the Kansas Court of Appeals. The court stated that language in the company's original application in 1987 indicated that it intended benefits of the transaction to be passed on to ratepayers, and said that the Commission's order had provided the company "clear notice" that the initial accounting treatment was subject to change in a future proceeding. The court concluded that "the KCC's order regarding the LaCygne 2 adjustment is not contrary to prior KCC orders. There is no evidence that [the company's] shareholders were deprived of benefit from the proceeds from the sale/leaseback transaction. Moreover, the decision is supported by substantial competent evidence." *Western Resources, Inc. v. State Corp. Comm'n*, 30 Kan. App. 2d 348, 363 (2002).

14. In order to find now that the 2001 Order was mistaken, the Commission would also have to find that the 1987 Order was mistaken, the 2001 Order was mistaken, the 2001 Order on Reconsideration was mistaken, AND the Kansas Court of Appeals was mistaken—not to mention the Kansas Supreme Court, which declined to review. The Commission, which once found that the company was impermissibly trying to revise a 14-year old order, would now have to revise a nearly 20-year old order, by finding that the provisions that it found "clear and

reasonable" in 1987 are now unclear and unreasonable. It would have to find that the accounting treatment, which a court and two previous Commissions found reasonable and fair to both ratepayers and shareholders, is no longer reasonable and fair to ratepayers and shareholders. It would have to explain why the "substantial competent evidence" that the Court of Appeals found in the 2001 case was not actually as substantial and competent as the Commission and the Court of Appeals had once believed.

15. Attempting to rescue the Commission's decision on the basis that "mistakes were made" is not like finding and correcting a policy that had been based on a gross mathematical error made in the past that was only recently discovered. There is no such error. It is instead a matter of finding, in the face of no substantial competent evidence to the contrary, that a policy decision made in 1987, which has been upheld by two commissions and the Kansas Court of Appeals, is no longer a good policy decision. And it is not just a matter of now agreeing that the previous orders were not in concordance with the wishes of the company, because the Commission has previously ruled against the wishes of the company and was upheld, on substantially the same facts in evidence in this case. The Commission will be hard pressed on remand to find one piece of evidence in the record of this case that would support such a conclusion that it did not use in a previous case to support precisely the opposite conclusion. The better (and much simpler) course for the Commission is to accept the decision of the Court of Appeals and simply rule that the facts and arguments presented by the company in this case are in substance identical to those that the Commission found unpersuasive in previous proceedings, and, therefore, the Commission declines to change the policy established almost 20 years ago that contemplated a sharing of the benefits of the LaCygne transaction among ratepayers and

shareholders. Any other ruling will only lead to further appeals.

IV. Conclusions

16. The Commission must not adopt Westar's recommendations on remand. Increasing Westar's return on equity to offset the reduction in revenues for its unproven claim for terminal net salvage on steam plant would be unreasonable, arbitrary and capricious, and inconsistent with the evidence in the record. Allowing Westar to calculate customer refunds of the overcharges relating to the TDC by using a FERC rate that was not yet approved for inclusion in customer rates by the Commission would violate the prohibition against retroactive ratemaking. Additionally, allowing Westar to pass through only some of its transmission costs in a separate line item would not be consistent with the requirement that such line-item charges be revenue-neutral. Furthermore, adopting Westar's recommendation to find that the Commission's 1987 and 2001 decisions on the appropriate accounting treatment for LaCygne 2 were "factually incorrect" would result in an order that is itself factually incorrect. For all practical purposes, it would be far simpler and more direct to end this case, and advise Westar that filing a new rate case is its only recourse. Attempting to rescue this case in the manner proposed by Westar only invites additional appeals.

17. Therefore, the Intervenors respectfully and jointly request the Commission, without rehearing and taking new evidence, to simply issue an order pursuant to the orders of the Court of Appeals, as they recommended in their *Joint Comments* filed on December 18, 2006, and to refund the recommended amounts in a manner that does not violate the prohibition against retroactive ratemaking.

Respectfully submitted,

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VERIFICATION

STATE OF KANSAS)
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COUNTY OF SHAWNEE)

I, Niki Christopher, of lawful age, being first duly sworn upon her oath states:

That she is an attorney for the above named petitioner; that she has read the above and foregoing, and, upon information and belief, states that the matters therein appearing are true and correct.

Niki Christopher

SUBSCRIBED AND SWORN to before me this 5th day of January, 2007.

Notary of Public

My Commission expires: 2-18-2010

Vermona E. Runnebaum
Notary Public - State of Kansas
My Appt. Expires February 18, 2010

CERTIFICATE OF SERVICE

05-WSEE-981-RTS

I, the undersigned, hereby certify that a true and correct copy of the above and foregoing document was placed in the United States mail, postage prepaid, hand-delivered this 5th day of January, 2007, to the following:

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