

**BEFORE THE STATE CORPORATION COMMISSION
OF THE STATE OF KANSAS**

Received
on

Before Commissioners:

Mark Sievers, Chairman
Ward Loyd
Thomas Wright

MAY 14 2012

by
State Corporation Commission
of Kansas

In the Matter of the Application of The)
Kansas Power Pool, A Municipal)
Energy Agency, for Approval of its)
Annual Transmission Revenue)
Requirement (ATRR) for its)
Transmission Facilities)

Docket No. 12-KPPE-630-MIS

**JOINT RESPONSE TO STAFF REPORT OF SUNFLOWER ELECTRIC POWER
CORPORATION AND MID-KANSAS ELECTRIC COMPANY, LLC**

COMES NOW, Sunflower Electric Power Corporation (Sunflower) and Mid-Kansas Electric Company, LLC (Mid-Kansas), pursuant to the Order Designating Prehearing Officer and Setting Procedural Schedule, and hereby provide the following Response to the Commission Staff Report and Recommendation (Staff Report). In support of this Response, Sunflower and Mid-Kansas state as follows:

1. This proceeding involves the application filed by The Kansas Power Pool (KPP) for approval of a transmission formula rate (TFR) to spread the costs of facilities owned and operated by the City of Winfield (Winfield) to all customers served by the Southwest Power Pool, Inc. (SPP) in the Westar Energy, Inc. (Westar) pricing zone (Zone). This is a good deal for Winfield, whose retail customers were bearing *all* of the costs of these facilities. And one could argue that the effect on non-Winfield customers

is *de minimis*.¹ However, this relatively modest rate proposal belies the potential for future impacts to Kansas retail customers because:

KPP anticipates that it may in the future wish to transfer control of other transmission facilities to SPP and recover the costs of other facilities in the Westar zone which could be owned by either member cities or KPP itself, [and thus] KPP chose to develop a formula template for determining its ATRR for all such facilities as they are placed under SPP's functional control from time to time.

KPP Application, ¶ 6. As Staff has noted, the nature of a TFR is provide the means to determine the revenue requirement for regulated assets and then update it annually. Staff Report, p. 3. The initial approval is therefore critically important because the Commission's finding is that the use of the formula will produce lawful rates even as the actual charges increase over time with updated cost inputs.

2. In the instant case, the initial approval of the template is even more important because the Commission is being asked to approve rates for the use of facilities owned by a non-regulated municipal utility that does not maintain its books and records in accordance with Commission rules. Given KPP's express desire to use this filing to establish a template for use with other facilities acquired in the future, it is reasonable to assume that KPP envisions using the same sort of assumptions and proxy numbers over and over again. In other words, the Commission is not presented in this docket with a proposed formula of a regulated utility using prescribed systems of accounts. Rather, KPP seeks a blank check for spreading across "other" Kansas consumers costs that have been incurred by small cities to serve their own customers and for which there are inadequate records to establish actual investment or ongoing

¹ As stated in SPP's FERC Tariff, Attachment H – Zonal ATRRs, the combined Westar Zonal rate is currently \$148,462,476, of which KPP represents \$528,917 and Westar represents \$147,933,559. In other words, the SPP transmission customers experienced a mere .00357% increase in Annual Transmission Revenue Requirements as the result of the SPP/KPP filing at FERC.

expenses. As more fully set forth below, Staff has hit the nail on the head – the Application should be denied and KPP should be directed to refile a case that meets its burden of proving that its proposed rates are just and reasonable.

I. Background

3. The Commission Staff filed its Report on May 3, 2012. In it the Staff recommends that the Commission dismiss KPP's filing in this Docket and that KPP refile its request for a TFR once KPP has completed the recommendations listed on pages 5 and 6 of the Staff Report. Those recommendations are that KPP

- 1) Prepare an accounting manual to aid [City of] Winfield accounting staff (and subsequent municipalities contributing transmission assets to KPP) in tracking investments in and expenses related to the Winfield Transmission Assets using the FERC Uniform Chart of Accounts (USoA);

- 2) Submit the accounting manual to the KCC for approval;

- 3) Complete one year of tracking transmission related assets, revenues, and expenses using the accounting manual and following the USoA;

- 4) Hire an outside, independent auditor to conduct annual audits of its transmission related financial records and certify that KPP has followed its accounting manual and USoA;

- 5) Each year file an annual report with the KCC using FERC Form 1 format; and

- 6) Work with Staff to produce protocols.

Staff Report, pp. 5-6. The Staff Report was expressly limited to accounting and financing issues and “does not and is not intended to address” legal issues regarding the jurisdiction of the Commission and the Federal Energy Regulatory Commission (FERC) with respect to KPP.

4. On May 9, 2012, the Prehearing Officer issued an Order for Prehearing Briefs to address the issue of Commission jurisdiction in this matter. KPP's brief is due by May 17, 2011 and Staff and Intervener briefs are due by May 24, 2012.

5. In their March 15, 2012, Joint Petition to Intervene and Comments (Joint Petition), Sunflower and Mid-Kansas addressed the issue of the Commission's jurisdiction under K.S.A. 66-101c and K.S.A. 66-136, and provided comments regarding the KPP Application. It is Sunflower's and Mid-Kansas' intent to file a further brief on jurisdiction by May 24, 2012, and that issue is therefore reserved and outside the scope of this Response.²

II. Joint Response

6. Sunflower and Mid-Kansas support all findings in the Staff Report. They also expressly incorporate by reference their comments on the Application contained in the Joint Petition. In particular, Sunflower and Mid-Kansas agree with Staff's opinion that there should be a uniform set of requirements that apply to this and to KPP's future TFR filings and protocols – important because of KPP's acknowledgment that there will likely be additions to its TFR, as more members assign their municipally-owned assets to KPP.

7. Sunflower and Mid-Kansas are affected because KPP has member cities located in Mid-Kansas' transmission zone and there are cities in the Sunflower transmission zone that theoretically may join KPP in the future. Any filing requirements and protocols must be just and reasonable as applied in whatever zone KPP chooses to control city-owned facilities or build its own. As the Staff Report demonstrates, KPP has

² The jurisdiction issue will drive the resolution of questions raised in the Joint Petition, *inter alia*, whether KPP may collect under its FTR before the effective date of a Commission order approving the FTR under Kansas law, how the Protocols must be altered regarding any disputes about annual updates, and whether FERC precedent on use of proxy costs is controlling.

failed to meet its burden of proof to establish why each proxy number is necessary in the first place and, for those using Westar costs, why Westar is the appropriate reference.

A. Proxies Are Appropriate, But Not For Virtually Every Cost

8. First, Sunflower and Mid-Kansas wish to make clear that they do not oppose the use of proxies in all elements of ratemaking. For example, public power entities, like cooperatives, enjoy greater access to lower-cost capital than investor-owned utilities (IOUs) and, as a result, often have higher debt/equity ratios than IOUs. They are not stock companies owing a return on equity (ROE). For that reason,

Determining a revenue requirement for a municipal system does not necessarily follow the same formula as an investor owned utility. As opposed to earning a rate of return on ratebase as is the case with investor owned utilities, municipal systems' revenue requirements are routinely determined by allowing a margin over and above operating expenses.

Staff Report, p. 3. For example, Mid-Kansas' formula-based transmission rate now under consideration in a separate docket proposes a proxy (hypothetical) capital structure.³ However, KPP proposes proxy numbers for virtually every rate component.

9. KPP has made much of the fact that FERC accepts proxies. However, even when FERC accepts the use of proxies, it requires an examination of *why* the particular proxy is appropriate:

Regarding Vernon's use of Edison as a proxy for the rate of return on common equity and the depreciation rate, the Orders on review provide only an inadequate conclusory statement that FERC thought use of Edison as a proxy was appropriate because Edison and Vernon were in the same TAC area. *Vernon Order*, 93 F.E.R.C. at 61,286. Not only does the record reflect that Vernon itself sought to distinguish itself from Edison, at least for the purposes of being allowed to include unused transmission expense in its TRR, the filed protests presented unanswered challenges to allowing Vernon to use Edison's rates. *Vernon Order*, 93 F.E.R.C. at 61,284; see also *Rehearing Order*, 94 F.E.R.C. at 61,563. While use of a surrogate

³ See Commission Docket No. 12-MKEE-650-TAR.

capital structure or return on equity may be appropriate for a governmental entity, FERC did not explain why such a proxy was necessary nor justify the selection of Edison as a surrogate by considering and examining, for example, whether Vernon and Edison share common risks. *Cf. S. Cal. Edison Co.*, 92 FERC ¶ 61,070, at 61,264-67, 2000 WL 1100260 (2000). Vernon's use of Edison's rate-making methodology bears no obvious correlation to an appropriate return on equity for Vernon, and mere geographical proximity hardly appears, absent further explanation, a sufficient warrant for the same return on equity or the same capital structure. A similar problem exists with regard to FERC's explanation of its approval of Vernon's reliance on Edison's 3.2% rate of depreciation. FERC's conclusion that its choice is "reasonable," *Rehearing Order*, 94 F.E.R.C. at 61,565, is thus insufficient to survive arbitrary and capricious review.

Pac. Gas & Elec. Co. v. FERC, 306 F.3d 1112, 1120-1121 (D.C. Cir. 2002). KPP has not met its burden by showing "mere geographical proximity." *See id.*

B. The Proposed Costs Are Not Adequately Justified

10. Sunflower and Mid-Kansas agree with the Staff Report that KPP has not adequately justified the costs that it proposes to pass on in its transmission formula rate.⁴

In particular, there is no support in the application for the actual cost of the facilities (original book less depreciation), the cost for ongoing expenses like Administrative and General (A&G), taxes, and operations and maintenance (O&M), and the proper return that KPP proposes to place into the SPP rates, nor have Staff's discovery requests, which Sunflower and Mid-Kansas have monitored, produced sufficient information to calculate those costs.

11. The first deficiency is in KPP's proof of the cost of the facilities that it proposes to spread to other SPP transmission customers. As KPP's Application admits in the Direct Testimony of Paul D. Reising (Reising Direct), p. 6, l. 18 – p. 7, l. 6:

⁴ Staff Report at pp. 4-5.

The City of Winfield does not maintain its books and records for the electric utility in accordance with the FERC's Uniform System of Accounts, nor do the City's financial reports separate plant in service, accumulated depreciation or operating expenses by function. Data were not available to determine the exact costs attributable to the City's 69 kV transmission facilities. As a result, it was necessary to estimate the gross plant in service, accumulated depreciation and net Exhibit K-1 plant in service by first computing the cost to reproduce that system in 2010 costs and index those costs back to the original installation date using the Handy-Whitman Index for electric utility construction costs for the North Central Region, which encompasses the State of Kansas. The results of the asset valuation process for the Winfield 69 kV facilities are presented in the "Investment Analysis" worksheet of Exhibit K-4. The results of the asset valuation process for the Winfield 69 kV facilities (which I prepared in November 2011) are presented in Part II of the "KPP Transmission Investment" worksheet of Exhibit ___ PDR-3.

12. The issue of jurisdiction will be separately briefed. For purposes of this pleading, Sunflower and Mid-Kansas assume that the "Commission has jurisdiction over KPP's transmission rates pursuant to K.S.A. 12-8,111, 66-101, 66-101b, and 66-104"⁵ and that the "Commission's jurisdiction over wholesale rates is not preempted by FERC because Section 201 of the Federal Power Act exempts municipal energy agencies from federal jurisdiction."⁶

13. KPP has cited no authority (other than the letter agreement with Commission Staff) for the proposition that a *regulated* Kansas public utility may justify the cost of the facilities it wishes to impose on ratepayers by this method. KPP bears the burden to prove that its rate will be just and reasonable under Kansas law. It has failed to do so.

⁵ Prehearing Officer's Order Granting Intervention to Sunflower Electric Power Corporation, Mid-Kansas Electric Company, LLC and Westar Energy, Inc., and Order Granting Admission *Pro Hac Vice* to N. Beth Emery, ¶ 1, March 22, 2012.

⁶ *Id.*

14. KPP also must meet the burden of proving that its proposed expense recoveries are reasonable. This is particularly so in a TFR, which sets up accounts for properly charged costs, which are then automatically passed through each year. KPP has again cited no authority for the proposition that a *regulated* Kansas public utility may use the costs of a different utility (Westar) rather than establishing the costs actually incurred for providing the service.

15. Moreover, use of Westar proxies, even if sensible, makes no sense for facilities that in the future might be located in another Zone. If the Commission approves the concept of proxies for certain costs, the TFR should expressly obligate KPP to establish the justness and reasonableness of future proxy costs (which reference utility will be used and why) where the assets are located outside of the Westar zone.

16. In sum, consistent with the Staff Report and as Westar has noted in its March 21, 2012 Petition to Intervene at p. 5-6, KPP should be required to immediately begin maintaining its records in accordance with the Uniform System of Accounts (USoA) such that KPP's actual expenses incurred for these transmission facilities going forward will be recovered through the formula rate. This includes the necessity of tracking expenses incurred by its member cities, such as Winfield, using the USoA. Under Kansas law, rates are supposed to be cost based. An asserted lack of proper recordkeeping is no justification for adopting proxy numbers. An unsupported assertion that actual costs would presumably be higher is also not adequate proof.

17. Agreeing to record actual costs going forward does not, however, insulate KPP from the need to demonstrate the cost basis of the initial charges. Since KPP has made it clear that this is the first of what may be many future filings to include the cost of

existing municipally-owned assets into the SPP rate, it is imperative that the Commission demand as part of the “template” that KPP provide appropriate, fact-based cost of service evidence not just going forward, but also for the rates put into effect initially.

18. In sum, clear requirements for establishing the existing rates for *each* third-party owner’s facilities, record-keeping, use of an acceptable uniform system of accounts, and limitation of any Westar proxies to facilities in the Westar Zone, are necessary predicates for a just and reasonable and not unduly discriminatory KPP formula rate.

C. The Proposed Protocols Are Not Adequate

19. Sunflower and Mid-Kansas agree with Staff recommendation that the Commission reject the protocols proposed by KPP.⁷ For example, Sunflower and Mid-Kansas agree with Staff’s proposal that disputes must come before the Commission for resolution — not FERC, as KPP has proposed. The Protocols need to reflect the Commission’s jurisdiction as the first step in any annual update or filing to change the formula.

20. Further, as Westar has observed in its March 21, 2012 Petition to Intervene, at p. 6, the Protocols do not provide customers with adequate opportunity to challenge the ATRR calculation or to ensure that any necessary corrections are made to the calculation. Sunflower and Mid-Kansas agree with Westar, absent sufficient protocols, customers would have no way to ensure the accuracy, adequacy, and sufficiency of the data and the resulting ATRR calculation. See *id.* Because KPP does not file a FERC Form 1, the right to review annual updates for accuracy and to make

⁷ Staff Report at 5.

necessary corrections is particularly important in the context of KPP's formula rate. See *id.*

21. Finally, while KPP does not discuss the issue in the Application, KPP has defined "Interested Parties" under the Protocols too narrowly:

For purposes of these Protocols, "Interested Parties" shall mean any Transmission Owner in whose SPP zonal rates KPP's ATRR will be included, any load serving entity whose customers will be allocated all or a portion of KPP's ATRR, and any state utility commission or consumer advocate operating in a state in which customers that will be allocated all or a portion of KPP's ATRR are located.

At a minimum, any entity granted intervention in this docket should be an "Interested Party" for purposes of future review of the costs. Moreover, should KPP propose to include the cost of facilities located in other Kansas TO zones in its rates, "Interested Parties" should be all transmission customers in the affected zone. The better approach would be to follow the form of protocols adopted in other Kansas TO formula-based rates, such as that recently filed by Mid-Kansas, which allows any "interested party" (not defined) the right to comment.

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III. CONCLUSION

WHEREFORE, Sunflower and Mid-Kansas pray that the Commission enter an Order as follows:

- A. Accepting the recommendations in Staff's Report, at pp. 5-6, including Staff' recommendation to dismiss KPP's Application in this Docket; and
- B. Providing for all other relief that the Commission deems just and proper.

Respectfully submitted this 14th day of May, 2012 by the undersigned counsel on behalf of:

**SUNFLOWER ELECTRIC POWER CORPORATION
MID-KANSAS ELECTRIC COMPANY, LLC**


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VERIFICATION

STATE OF KANSAS)
)
COUNTY OF ELLIS) ss:

Mark D. Calcara, of lawful age, being first duly sworn on oath states:

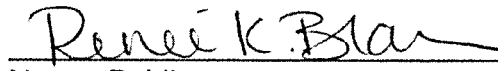
That he is General Counsel of Mid-Kansas Electric Company, LLC; that he has read the foregoing pleading and knows the contents thereof; and that the facts therein are true and correct to the best of his knowledge, information, and belief.



Mark D. Calcara

SUBSCRIBED AND SWORN to before me this 14th day of May, 2012.



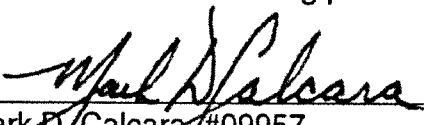


Notary Public

My Commission expires: April 30, 2014

CERTIFICATE OF SERVICE

I, the undersigned, hereby certify that on this 14th day of May, 2012, the above and foregoing Application was submitted to Patrice Petersen-Klein, Executive Director, Kansas Corporation Commission, with the original and nine copies mailed via UPS to the Commission, and electronic service was made on the following parties.



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