

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

In the Matter of the Application of Midwest)
Power Company for a Certificate of Public) Docket No. 19-MPCE-064-COC
Convenience and Necessity to Transact the)
Business of a Public Utility in the State of Kansas.)

**REPLY BRIEF OF WESTAR ENERGY, INC. AND KANSAS GAS AND ELECTRIC
COMPANY**

I. Introduction

In this Reply Brief, Westar Energy, Inc. and Kansas Gas and Electric Company, (“Westar”) respond to the Initial Brief of Midwest Power Company (“MWP” and “MWP Brief”). Westar anticipated many of MWP’s arguments in its initial brief and will endeavor not to repeat those arguments here. Westar’s failure to respond directly to any point raised in MWP’s initial brief should not be construed as agreement with MWP.

As MWP stated in its brief, this case turns on one issue – whether MWP has shown that it meets the financial prong of the Commission’s test for determining whether or not a certificate of convenience and necessity (“CCN”) should be granted.¹ It is clear that MWP does not and cannot meet the financial requirements test in the absence of a guaranty from its corporate parent.

**II. MWP has not demonstrated that it has the financial resources required to
obtain a CCN.**

MWP’s sole asset is its 8% undivided interest in JEC.² MWP holds the asset “as the sole participant and beneficiary in a Trust for which Wilmington Trust Company (“WTC”) is the

¹ MWP Brief, at ¶10.

² Paine Direct, at 4.

owner trustee.³ And, although MWP admits that the Trust has financial obligations under the various agreements related to the JEC interest,⁴ neither MWP nor the Trust have the wherewithal to meet those financial obligations. As the record shows, the trust estate currently has a balance of only \$100.⁵ And MWP's 8% interest in JEC – MWP's sole asset – will run at a cumulative loss through at least 2022⁶ even under MWP's rosy assumptions. The inability of the Trust and MWP to fund its share of the operations of JEC is the result of its parent's decision not to fund the Trust or MWP and to divert all revenue from the lease to the Trust participants.⁷

In the almost certain event that MWP and the Trust fail to pay the expenses associated with their 8% interest, the Trust will be in default under the terms of the Consent and Assumption Agreement and the Operating Agreement.⁸ At that time, in the absence of a guaranty from MWP and MWP's parent, under the terms of the Consent and Assumption Agreement, Westar would be required to cover such expenses.⁹ MWP asserts that the existence of Westar's obligation to backstop its non-existent finances enables it to claim that it meets the

³ *Id.*

⁴ Paine Rebuttal, at p. 6, line 17 to p. 7, line 1 (“This language makes it clear that no personal liability or responsibility is assumed by WTC, and any person making a claim under the various agreements, including the Operating Agreement, **must look solely to the Trust Estate** for satisfaction of such claim.”) (emphasis added); Paine, Tr. at p. 36, line 18-24 (“Q. (By Ms. Dinges:) . . . you indicate that Midwest Power Company and Wilmington Trust Company do not have obligations in their personal capacities to cover expenses related to the 8 percent interest at Jeffrey, **and that only the trust estate has those obligations**. Is that correct? A. (By Ms. Paine:) Yes.” (Emphasis added.))

⁵ Paine Tr. at 39-40.

⁶ *Id.* at 42-43.

⁷ See Paine, Tr. at 38, in which MWP witness Paine indicates that all of the income from the lease is paid to the trust participants and that none of the lease payments are paid into the trust estate.

⁸ As is discussed more fully below, Sections 3.1 and 3.2 of the Consent and Assumption Agreement make the Trust primarily liable to pay and perform all liabilities and obligations of the Ownership and Operating Agreements after termination of the lease. See MWP Exhibit 1, at 9.

⁹ MWP Exhibit 1, at 9.

Commission's financial resources requirements. There is no basis in the record or in law or logic for that position.

First, and most importantly, MWP's position merely highlights its inability to meet the Commission's financial integrity requirements. Westar's obligation to cover shortfalls created by MWP's and the Trust's inability to pay would only arise if the Trust fails to meet its admitted financial obligations related to the 8% JEC interest. Stated differently, MWP argues that, when the Trust defaults in its obligations to pay costs related to the JEC interest due to its lack of any substantial resources, MWP nevertheless has sufficient financial resources because Westar has the ability to pay. However, MWP has not cited any authority for the extraordinary proposition that a CCN applicant can meet the Commission's financial integrity test by intentionally underfunding itself and passing the buck to another, unrelated entity. Indeed, no such authority exists.

Second, while relying on Westar's obligation under Section 3.3 of the Consent and Assumption Agreement to cover any shortfall due to MWP's and the Trust's lack of financial integrity, MWP conveniently ignores the language in that very section which indicates the reason for Westar's undertaking. Section 3.3 states that the obligation of UtiliCorp (which Westar later assumed) was undertaken "for the benefit of each of the Consenting Owners."¹⁰ The term "Consenting Owners" is defined to "mean the collective reference to Centel, UtiliCorp, KPL and KGE."¹¹ Thus, the obligation to cover shortfalls that might arise as a result of the lease was to protect the other owners from the inability or unwillingness of the Trust to pay its share of the costs – not to provide financial integrity to the Trust where none exists.

¹⁰ MWP Exhibit 1, at 9.

¹¹ *Id.* at 3. (KPL and KGE are predecessors to Westar.)

Third, MWP's position also ignores the plain language of Sections 3.1 and 3.2 of the Consent and Assignment agreement. Those sections state, in pertinent part:

3.1 Ownership Aareemeat. [sic] Owner Trustee hereby assumes and agrees for the benefit of each of the Consenting Owners to pay and perform all liabilities and obligations arising under the ownership Agreement from and after delivery of the Transfer Documents solely in connection with the Undivided Interest

3.2 Operating Aareement. [sic] Owner Trustee hereby assumes and agrees for the benefit of each of the Consenting Owners to pay and perform all liabilities and obligations arising under the Operating Agreement from and after delivery of the Transfer Documents solely in connection with the Undivided Interest, from and after the Lessor Possession Date.¹²

The term "Lessor Possession Date" is defined as "the earlier of (a) the date of expiration or earlier termination of the Lease and (b) the date of loss of use or possession by the lessee under the Lease of the Undivided Interest by reason of exercise of remedies of the lessor under the Lease."¹³

The effect of these provisions is that the Trust under Section 3.1 was, **for the benefit of the Consenting Owners**, obligated to meet the obligations of the Ownership Agreement from the inception of the lease and under Section 3.2 to meet the obligations of the Operating Agreement after termination of the lease by any means. And, to use MWP's counsel's turn of phrase, those obligations run "forever and a day."¹⁴

In its brief, MWP states, "no party has disputed MWP's interpretation of the contractual provisions requiring payment of shortfalls by Westar."¹⁵ That statement while true is, however,

¹² *Id.*, at 9.

¹³ *Id.* at 3.

¹⁴ *See, e.g.*, Paine, Tr. at 74.

¹⁵ MWP Brief, at ¶17.

highly misleading. First, the statement ignores that the Trust has the primary responsibility to meet the obligations under the JEC Ownership and Operating Agreements. Westar's obligation only arises after the Trust defaults in its obligations. Secondly, MWP's statement ignores the consequences of the Trust's default in paying its obligations under the JEC agreements – namely, Westar's right to right to recoup those payments from the Trust¹⁶ and to foreclose on the 8% interest under terms of the JEC agreements.¹⁷

In order to meet the Commission's financial resources requirements for issuance of a CCN, MWP and the Trust must show that they are capable of meeting those obligations. The issuance of a CCN to an entity that admittedly does not have the financial ability to pay the costs of ongoing operations would shift those costs to Westar and its customers. Consequently, the CCN application does not meet the financial resources standard. Issuance of the CCN without conditions designed to ensure the financial integrity of MWP and the Trust would not be in the public interest.

III. Applying the proposed conditions is reasonable under the circumstances and does not constitute taking sides in potential litigation or rewriting the agreements between the parties.

In its brief, MWP argues that if the Commission adopts the conditions proposed by Westar and Staff that it will be taking sides in potential litigation between Westar and MWP¹⁸ and rewriting the JEC contracts.¹⁹ MWP misses the mark with both arguments.

Neither Westar nor Staff is requesting the Commission to rewrite the JEC agreements or take a side in potential litigation between Westar and MWP. To the contrary, Westar and Staff

¹⁶ *Lindsay v. Zeller*, 10 Kan. App. 2d 4, 7 (1984).

¹⁷ Ives Direct, at 7, 8-9.

¹⁸ MWP Brief, at ¶21.

¹⁹ *Id.* at ¶22.

are merely requesting that the Commission apply existing precedent that requires a CCN applicant to demonstrate that it has the financial integrity to support its ownership in assets for which the CCN is required. No rewriting of the JEC contracts is needed to require MWP and the Trust to show financial ability that emanates from within the corporate structure of which they are a part. The Commission has consistently applied such a requirement in CCN and merger proceedings.²⁰

MWP asserts that the parties did not expect ownership of the 8% interest in JEC by MWP and the Trust after expiration of the lease.²¹ It should be noted, however, that there is no evidentiary support for this suggestion in the record. Moreover, the Consent and Assumption Agreement specifically addresses the possibility that the Lessor – that is, the Trust – could end up owning the 8% interest after termination of the lease.²² While MWP may have expected Westar to exercise its option, Westar always had the ability simply to allow the lease to end.

Notwithstanding the existence of Westar’s option not to purchase the 8% interest when the lease ends, it is clear that the Commission was not asked to and did not evaluate the implications of that possibility when it reviewed the sale/leaseback transaction in 1991. As all parties to this proceeding have acknowledged, MWP and the Trust were not considered “public utilities” under Kansas law because they only had a financial interest in JEC.²³ Now the situation has changed and MWP and the Trust will, under the applicable statutes, be Kansas electric utilities upon expiration of the lease and are required to seek a CCN, albeit “under

²⁰ See Westar’s Initial Brief at pp. 19-21.

²¹ See, e.g., MWP Brief, at ¶5.

²² See MWP Exhibit 1 at 3 (definition of “Lessor Possession Date”) and 9 (Section 3.2).

²³ Paine, Tr. at 48.

duress,”²⁴ because the financial interest exemption will no longer apply after termination of the lease.²⁵ Applying the standard requirements for a CCN to MWP when it proposes to become a public utility under Kansas law does not require rewriting any of the JEC agreements. It is simply the result of the Commission necessarily applying the law and Commission precedent to the situation now presented to it for the first time.

IV. As owner of 8% of JEC, MWP is a “public utility” under Kansas law and has control over assets that affect the public interest whether or not such assets are “severable.”

There is no doubt that by owning 8% of JEC, MWP is a “public utility” under Kansas law. Generally, any party that owns, controls, operates or manages plant for the generation of electricity is a public utility.²⁶ There are exceptions to the rule including an exception for electric generation facilities that are both (1) newly constructed and placed in service on and after January 1, 2001 and (2) not in the rate base of a public utility.²⁷ There is no question that JEC was in service on and before January 1, 2001. Therefore, an entity that owns or controls any portion of JEC is clearly a public utility.

Despite meeting the definition of public utility, MWP appears to chafe under the yoke of regulation. Thus, it filed its application here “under duress”²⁸ and belittles the statutorily established cut-off date as “arbitrary.”²⁹ Additionally, MWP’s counsel derided the “2001 provision in the statute”³⁰ as “that one little provision in the statute.”³¹ In its brief, MWP appears

²⁴ *Id.*

²⁵ *Id.*

²⁶ K.S.A. 66-104(a).

²⁷ K.S.A. 66-104(e).

²⁸ Paine, Tr. at 48.

²⁹ MWP Brief, at ¶12.

³⁰ Unrein, Tr. at 129 (question by Mr. Caro).

to argue that despite the language of the statute, the Commission should treat it as though it were an IPP that built new generation after 2001 and that “many of the traditional concerns and analyses of a CCN application are inapplicable.”³² MWP’s argument is baseless.

MWP’s opinion of the importance or arbitrariness of the “2001 provision in the statute” is irrelevant. Presumably, the legislature had a reason for establishing such a date. Quite simply, it is likely that the legislature wanted to encourage new investment in generation in Kansas by non-utility operators. With such an intent, the need for a forward-looking effective date would have been essential to incent future investment.

Contrary to MWP’s argument, its position in this case clearly demonstrates why the “traditional concerns and analyses” of a CCN application apply to this case. The central purpose of the CCN requirement is to ensure that the public interest – not the purely private interest of the applicant – will be served by granting the application.³³ As the Kansas Supreme Court has stated: “In determining whether such certificate of convenience should be granted, the public convenience ought to be the Commission’s primary concern, the interest of public utility companies already serving the territory secondary; and the desires and solicitations of the applicant a relatively minor consideration.”³⁴ In this case, only the interest of MWP would be served by granting the certificate without proper conditions. If an unconditioned certificate were granted, MWP would be free to offer its 8% interest in JEC into the market without any risk or obligation to pay the associated costs while imposing those costs on Westar and its customers.

³¹ *Id.* at 130.

³² *See*, MWP Brief, at ¶12.

³³ *Central Kansas Power Co. v. KCC*, 206 Kan. 670, 676 (1971).

³⁴ *Kansas Gas & Electric Co. v. PSC*, 122 Kan. 462, 466 (1927).

And even if the 8% interest generates a profit in later years, MWP maintains it would not have any obligation to repay Westar for prior year shortfalls.³⁵

MWP also argues “MWP, WTC and KeyCorp have virtually no control over the operations of the JEC”³⁶ That simply is not true. Even though MWP witness Paine stated that MWP would “have very very limited control, if any,”³⁷ she had to admit that MWP will be able to decide whether it wanted to sell its share of JEC to a third party or into the SPP market and that MWP would receive the revenue from any such sale.³⁸ And, as Westar witness Ives explained, MWP will have the ability to choose whether or not to offer its 8% interest into the market and would therefore, subject to market and operating conditions, control whether its share of the plant runs.³⁹

MWP also suggests that the typical concerns in a CCN application do not apply in this case because the 8% interest is not severable from the rest of JEC.⁴⁰ In fact, just the opposite is true. As the Commission is aware, electric generation costs are largely fixed – that is, as MWP states, they will be incurred whether or not the plant runs.⁴¹ From its in-service date to today, JEC – including the 8% subject to the lease – has been used to serve Kansas retail electric

³⁵ Paine, Tr. at 43.

³⁶ MWP Brief, at ¶12.

³⁷ Paine, Tr. at 49.

³⁸ *Id.*

³⁹ Ives, Tr. at 93-95. As Westar witness Ives indicated, whether MWP’s 8% interest is actually sold into the market will be affected by other factors than MWP’s decision to offer it for sale. For instance, the plant has operating minimums that would not allow it to run if only the 8% interest is offered into the market and the SPP makes the ultimate decision whether to accept commitments. Ives, Tr. at 92, 93. But, as Mr. Ives noted, MWP will have the same level of control as any other minority owner in JEC. *Id.* at 92.

⁴⁰ MWP Brief, at ¶12.

⁴¹ *See*, MWP Brief, at ¶19.

customers.⁴² In recent years, revenues to support the 8% interest subject to the lease were provided by a power sale by Westar to Mid-Kansas Electric Company that used the power to supply its Kansas customers.⁴³

With the end of the lease and of Westar's power sale to Mid-Kansas, MWP will obtain control of the 8% interest in the plant currently subject to the lease. As a certified utility, MWP will be able to sell energy and capacity associated with its interest in JEC on the wholesale market.⁴⁴ However, there will be no revenue stream to support the costs associated with the 8% interest unless it is supplied by MWP. Because the 8% interest cannot be severed from the rest of the plant and because fixed costs associated with it will continue to be incurred as along with variable costs when MWP sells its share into the market, the financial resources of MWP are implicated. Unlike a typical IPP – which bears the risk associated with the ownership and operation of its generation facilities and whose operations and financial condition affect only its owners – MWP proposes to shift all of the risk of its ownership onto Westar and its customers and take any profit its share of JEC may generate. Consequently, unless MWP's parent is obligated to pay the expenses associated with running MWP's share of JEC when its running costs are below the market price of power, MWP would have no disincentive to offering its share into the market at a loss. Requiring MWP and its parent to bear the financial risk of its ownership of an interest in JEC puts it on a similar financial footing as the IPPs to which it attempts to compare itself.

Because its finances are non-existent and because its lack of resources is likely to impose burdens on Westar and its customers unless appropriate conditions are imposed on it, MWP

⁴² Unrein, Tr. at 128.

⁴³ *Id.*, Tr. at 145.

⁴⁴ Paine Direct, at 10, 12.

cannot claim to be similarly situated to other IPPs. Unlike other IPPs, MWP and its parent bring no new investment in generation to the state and, in the absence of a parental guaranty, bear no risk associated with their share of the plant. Unless proper conditions are applied to MWP, its application cannot be approved because it does not advance the public convenience and necessity.

V. The Commission can and should condition the application on the provision of a guaranty by MWP's corporate affiliates.

MWP argues at length that requiring its affiliates KeyCorp and/or WTC to provide a guaranty is not consistent with precedent and is inappropriate in this case.⁴⁵ At its core, MWP's argument is that “. . . MWP is an IPP and not a franchised traditional public utility. In all cases but this one, IPPs *themselves* are not regulated by the Commission, so extending jurisdiction over an IPP's *parent company* goes much too far.”⁴⁶

The difficulty with MWP's argument is clear on its face. Unlike the IPPs to which it seeks to compare itself – that is, those that constructed generation in Kansas after 2001 – under Kansas law, MWP will be a public utility once it owns or controls a portion of JEC. While MWP may not like the language of K.S.A. 66-104, it cannot avoid its effect by merely asserting that it should be treated as if it were an IPP.

As was discussed above, MWP will own a portion of a generating station that has provided service to Kansas customers for its entire operational life and MWP's failure to pay for its share of the cost of the plant will directly affect Westar and its customers. Consequently, it is appropriate to analyze MWP's CCN application under the precedent applicable to public utilities. Under that precedent, it is both appropriate and necessary for the Commission to

⁴⁵ See MWP Brief, at ¶¶24-28.

⁴⁶ *Id.* at ¶24 (emphasis original).

condition the grant of any CCN to MWP on conditions that will protect Kansas utility customers from harm due to the limited financial resources of both MWP and the Trust.

VI. Conclusion

As MWP noted in its Application, it intends to file “a notice of self-certification as an exempt wholesale generator (“EWG”) pursuant to Section 366.7 of FERC’s regulations, 18 C.F.R. §366.7. MWP’s notice of self-certification as an EWG must contain certain determinations from the KCC.”⁴⁷ The requirement is summarized as follows:

Section 32(c) of PUHCA 1935 provides that any facility that was in a retail rate base on October 24, 1992 cannot be considered to be an eligible facility unless every state commission with jurisdiction over the retail rates in question makes a determination that allowing the facility to be an eligible facility will benefit consumers, be in the public interest, and not violate state law.⁴⁸

Granting a certificate to MWP that would allow it to force Westar to incur costs, including costs to buy coal to operate MWP’s 8% share of Jeffrey, without taking responsibility for paying the full amount of those costs, or for MWP to force Westar into default remedies or costly litigation to take over ownership of MWP’s 8% share of the plant would not benefit consumers or be in the public interest as required by the FERC regulations. Moreover, MWP cannot offer its share of JEC into the market without a KCC-issued CCN.

If MWP wants a certificate of convenience and necessity and determinations by the Commission that satisfy the applicable FERC requirements, MWP needs to take financial responsibility up front and make the financial resources of its parent company, KeyCorp, available to back up that commitment. The conditions Mr. Ives and Mr. Unrein proposed in their direct testimony achieve this result, are consistent with Commission precedent, and would

⁴⁷ MWP Brief, at ¶38.

⁴⁸ www.ferc.gov/industries/electric/gen-info/ewg/what-is-ewg/info-puhca.asp

protect the public interest. Therefore, Westar requests that the Commission approve MWP's request for a certificate only if it includes the conditions proposed by Staff and Westar.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I do hereby certify that a true and correct copy of the foregoing document has been emailed, this 4th day of January, 2019, to all counsel of record.

/s/ Martin J. Bregman