

BEFORE THE STATE CORPORATION COMMISSION
OF THE STATE OF KANSAS

In the Matter of the Joint Application of)
Westar Energy, Inc. and Kansas Gas and) Docket No. 19-WSEE-355-TAR
Electric Company for Recovery of Certain)
Costs Through Their RECA.)

REPLY BRIEF OF KANSAS INDUSTRIAL CONSUMERS GROUP, INC.

COMES NOW the Kansas Industrial Consumers Group, Inc. ("KIC"), and respectfully files this *Reply Brief* in the above-referenced case, pursuant to the Order of the State Corporation Commission of the State of Kansas ("Commission" or "KCC") dated April 11, 2019. In support of its Reply Brief, KIC states as follows:

I. Background

1. On March 4, 2019, Westar Energy, Inc., and Kansas Gas and Electric Company (collectively referred to as "Westar") filed an Application to recover costs related to a short-term lease, acquisition, and the future operations of 174 MW of new generating capacity – an 8% interest in the Jeffrey Energy Center ("JEC") currently owned by Midwest Power Company ("MWP").¹ The 8% interest in JEC, including associated operating costs, is not currently used to serve Westar's retail customers and, thus, is not included in Westar's retail rates.²

2. On July 16, 2019, the Commission held an Evidentiary Hearing in this matter. During the hearing, the prefiled testimonies of witnesses for KIC, Unified School District #259 Sedgwick County, Kansas ("USD 259"), the Citizens' Utility Ratepayer Board ("CURB"), Staff of the Commission ("Staff"), and Westar were admitted into evidence.

¹ Joint Application for Recovery of Costs through RECA, March 4, 2019, ¶¶ 26-31. (Application, ¶¶ 26-31.)

² Docket No. 18-WSEE-328-RTS, Non-Unanimous Stipulation and Agreement, July 17, 2018, ¶ 27. (18-328 Settlement, ¶ 27.)

3. On July 31, 2019, KIC, USD 259, CURB, Staff, and Westar filed initial post-hearing briefs. The official record and relevant legal authority are described and cited at length in KIC's Initial Brief.

II. Reply to Westar & Staff

4. KIC submits this Reply Brief to address the Initial Briefs of Westar and Staff. To avoid repeating the comprehensive arguments set forth in KIC's Initial Brief, KIC responds only to several specific aspects of Westar and Staff's Initial Briefs. KIC's decision not to address every element of these briefs should not be construed as agreement with or acquiescence to the positions of Westar and Staff. Rather, a non-response indicates KIC's Initial Brief and the existing record sufficiently covers the point. KIC's position, unless explicitly stated otherwise in this Reply Brief, remains the same as articulated in its Initial Brief.

A. Westar's Arguments regarding Past Benefits Do Not Justify a Rate Increase to Current and Future Ratepayers.

5. In its Initial Brief, Westar (and Staff to a very limited extent)³ contends it would be unreasonable for Westar to bear all the "wrap-up" costs of its business relationship with MWP because that relationship benefitted ratepayers in the past (through a now-expired lease).⁴ This position is inconsistent with Kansas law and balanced regulatory policy.

6. As detailed at paragraphs 69-76 of KIC's Initial Brief, rates are set prospectively to reflect the lowest reasonable ongoing cost of providing service. These forward-looking rates are based on current costs and customer needs. It is inconsistent with Kansas law, therefore, to set rates at an artificially high or low level to compensate for past costs or benefits.

³ Post-Hearing Brief of Commission Staff, July 31, 2019, p. 15. (Staff Brief, p. 15.)

⁴ Initial Brief of Westar Energy, Inc. and Kansas Gas and Electric Company, July 31, 2019, pp. 1-2, 19-20. (Westar Brief, pp. 1-2, 19-20.)

7. Westar has, in the past, made decisions that were not optimal and unnecessarily increased costs to customers. For instance, the company spent substantial amounts of capital on retrofits of, additions to, and maintenance of coal-fired generation facilities before coal-fired generation became uneconomic in the wholesale energy markets. Staff recently explained Westar's heavy reliance on coal generation capacity has been a primary contributor to its regionally-high electric rates.⁵ As noted in KIC's Initial Brief, Westar would surely not contend its future rates should be set at an artificially low level to compensate customers for these costly past decisions. Westar would likely call such an action "retroactive ratemaking" or "hindsight regulation."⁶

8. KIC agrees the Commission's rate-setting process should be prospective in nature. For example, the Commission has ongoing legal authority to evaluate whether Westar's property remains "used and required to be used" in setting current and future rates. But such a determination must be based on the current and future usefulness of the property.⁷ The Commission cannot decide to set rates at an artificially low level simply to compensate ratepayers for past excessive costs or financial detriments.

9. Westar seeks to apply a different standard in this case. Westar wants rates to increase in recognition of a past decision that, it contends, benefitted past customers for a discrete period of time.⁸ And Westar argues a shareholder bailout is "reasonable" because of those past

⁵ Docket No. 18-KCPE-095-MER, Rate Study of Kansas City Power & Light and Westar Energy for the years 2008 to 2018, January 14, 2019, pp. 8, 142, 145.

⁶ Westar uses this phrase with exceedingly broad application. In its Brief in this proceeding, Westar claims the Commission would be using "improper hindsight regulation" if it even considers the fact that Westar's contracts with MWP contained no financial guarantees, leading to unrecoverable costs.

⁷ K.S.A. 66-128, "The state corporation commission shall determine the reasonable value of all or whatever fraction or percentage of the property of any common carrier or public utility governed by the provisions of this act which property is used and required to be used in its services to the public within the state of Kansas, *whenever the commission deems the ascertainment of such value necessary* in order to enable the commission to fix fair and reasonable rates, joint rates, tolls and charges. [Emphasis added.]

⁸ It should be noted that past customers paid many millions of dollars of lease and operating costs to produce those benefits. And customers faced all the financial risks associated with the lease during its term. The wholesale revenues produced by the lease arrangement were not free benefits to customers.

benefits. Westar wants credit, and financial insulation, when its past decisions work in ratepayers' favor. But Westar also wants no blame or consequences when its decisions adversely impact customers in a material amount.

10. To balance Westar's exclusive right to serve retail customers in its service territory, Westar also has an ongoing obligation to provide service at the lowest reasonable cost. The Commission does not artificially increase or decrease future rates based on the costs or benefits of past utility decisions. The Commission sets rates prospectively to reflect the lowest reasonable ongoing cost of serving customers now and in the future. In this case, current and future customers do not need the energy and capacity of an additional 8% interest in JEC. And, if additional capacity or energy were needed, the 8% interest in JEC would not be the most cost-effective option.

B. Staff and Westar's Argument that the Parties Agreed to Only Examine the Purchase Price Is Inconsistent with the Plain Language of the Settlement.

11. In their legal briefing, Westar⁹ and Staff¹⁰ pursued an unsupportable argument that it is inconsistent with the Westar rate case Settlement for KIC and CURB to challenge the prudence of this transaction on any basis other than the purchase price. Specifically, Westar and Staff contend KIC and CURB should not evaluate the all-in costs of owning MWP's 8% interest when considering whether the acquisition is prudent for ratepayers.

12. Contrary to Staff and Westar's positions, the plain language of the Settlement requires Westar to demonstrate the prudence of any acquisition for its retail customers, and such an evaluation is not limited to the "purchase price." Paragraph 28 states,

In the event that Westar enters into a new lease for this 8% share of JEC, or purchases the 8% portion of JEC outright, the Parties agree that Westar will be permitted to file a request to include these expenses (lease expenses and NFOM) through the RECA....Westar shall be allowed to utilize a regulatory asset to defer actual lease expense and/or NFOM associated with the 8% portion of JEC in the event that a new

⁹ Westar Brief, p. 17.

¹⁰ Staff Brief, pp. 11-15.

lease or purchase agreement is reached. *In the filing before the Commission, Westar shall have the burden of showing that the new lease or purchase agreement is a prudent decision for its retail customers.*¹¹

13. As KIC evaluated this transaction, it became clear the purchase price, alone, would not be the determining factor in whether Westar's ownership of the 8% interest is "a prudent decision for its retail customers." The evidence demonstrates the transaction is not prudent because of the significant expected losses associated with the 8% interest – driven by ongoing operating costs and the significantly reduced market for coal-generated energy. Quite simply, owning the 8% interest is not needed, is not expected to be financially beneficial, and is expected to substantially increase rates. None of these factors are tied to "the purchase price," but they all demonstrate the acquisition is not prudent for retail customers.¹² Thus, it is irrational for Staff and Westar to suggest KIC, CURB, USD 259, or any other customer is required to "bury its head in the sand" and ignore these costs when evaluating the costs and benefits to customers of acquiring the 8% interest.

14. KIC will further briefly address the final sentence of paragraph 29. This statement seems to be the basis for Staff's claim that KIC and CURB should not consider the all-in costs of the 8% interest. The relevant sentence states, "In the event Westar ends up negotiating a zero-cost transfer of ownership (defined as \$0 or \$1), Westar is automatically entitled to begin recovering actual NFOM expenses and fuel expenses associated with the 8% ownership of JEC without prior Commission approval." There is a footnote to this sentence, which states, "The zero-cost transfer of ownership is intended only as a mechanism to shift regulatory burden and is not

¹¹ 18-328 Settlement, ¶ 28.

¹² Even if the "purchase price" was the only relevant aspect, this acquisition would not benefit customers when the full costs of ownership are considered. The purchase price is low because the 8% interest is a toxic asset. The 8% interest is expected to lose \$10 million every year. Unless the buyer needs dispatchable capacity – which Westar and its customers do not – the asset holds negative value. From the perspective of Westar's customers, the purchase price should be much less than zero to account for the expected additional costs of owning the interest.

intended to represent either the fair market value of the 8% portion of JEC or the value of the 8% portion of JEC that may ultimately be deemed to be reasonable by the Commission."

15. Staff clearly overreaches with its interpretation of paragraph 29. First, the proposal before the Commission is not a zero-cost transfer. The purchase price, including short-term lease costs, is roughly \$8.5 million.¹³ The last sentence of paragraph 29 does not apply. Its condition precedent was not triggered. Thus, Westar has the burden to demonstrate the transaction benefits customers before passing any costs to customers pursuant to paragraph 28 of the Settlement – a burden Westar has not fulfilled.

16. Further, the Settlement does not say KIC, CURB, or any other party gives up its rights to challenge the prudence of the transaction or reasonableness of the 8% costs if there had been a "zero-cost transfer." The settlement simply recognizes, under a specific circumstance, the burden would be *shifted* to a challenging party to demonstrate unjust and unreasonable rates resulting from the acquisition.

17. KIC and CURB did not agree to ignore the reality of the full costs of ownership when evaluating the prudence of owning the 8% interest. And, as detailed above, Staff and Westar's arguments are plainly inapplicable because the proposal before the Commission is not a "zero-cost transfer."

C. Westar's Discussion of KIC's Statements regarding the Rate Moratorium is Misguided and Inconsistent with the Hearing Transcript.

18. During opening statements, counsel for KIC did not claim the Westar Application violates Westar's base rate moratorium, as Westar suggests.¹⁴ Counsel for KIC provided context

¹³ \$4.83 million in additional short-term lease payments plus the final \$3.7 million purchase price. Westar also agreed to cover any NFOM during the lease, which eliminated millions of dollars of MWP cost obligations and could be fairly considered part of the "purchase price" consideration.

¹⁴ Westar Brief, p. 26.

for the parties to see this transaction from the perspective of ratepayers. Counsel for KIC explained this perspective as follows:

Now, before the moratorium, Westar was allowed one final rate case. And in that case, the KCC removed all the costs associated with the 8 percent interest in Jeffrey because Westar's prior lease of that interest was expiring. And the KCC ordered that the costs of the 8 percent interest would not re-enter rates even if Westar acquired that interest, unless Westar could show the acquisition is a prudent decision for its customers. In other words, to approve today's application, you need to find that customers benefit from buying the 8 percent interest. So you can understand why customers are somewhat confused to be here following a rate case in the midst of a rate moratorium defending against yet another request to increase rates.¹⁵

19. KIC explained the unjustness and unreasonableness of this Application from the perspective of a retail ratepayer. The Commission removed costs of an unowned, unused, and unneeded asset from base rates before Westar entered a base rate moratorium. The parties all agreed those costs would not re-enter rates during the rate moratorium¹⁶ unless there is an acquisition that *benefits* customers.¹⁷ Yet, Westar is now asking the Commission for permission to increase rates (a surcharge rate) as a result of the transaction.

20. From the perspective of customers, the Settlement was an assurance that the 8% JEC issue would not affect retail rates during the moratorium period unless there was a transaction that *benefitted* customers. Logically, KIC expected this provision to require a transaction that *reduces* rates.¹⁸

¹⁵ Tr., pp. 17-18.

¹⁶ Pursuant to paragraph 31 of the Settlement, Westar is not allowed to seek recovery of any 8% JEC costs until the expiration of its base rate moratorium, absent a beneficial lease or acquisition.

¹⁷ KIC does not, in any way, dispute that paragraph 28 of the Westar rate case settlement allows a specific caveat whereby Westar may evade the rate moratorium by recovering the 8% costs through its RECA surcharge, so long as the transaction is found to be prudent for customers. However, the 8% JEC costs, not including fuel, would typically be recovered through base rates.

¹⁸ KIC expected a transaction that is "prudent for...retail customers" would entail an arrangement where, in conjunction with the acquisition, Westar also secured a long-term contract to sell the energy and capacity of the 8% interest in a manner benefitting customers on an overall basis. As detailed throughout this hearing, no revenue source has been secured to offset the costs of owning the 8% interest. This is the primary difference between the proposed transaction and the previous lease arrangement.

21. Retail ratepayers reject the arguments of Westar and Staff that ratepayers are "benefitting" from this transaction that operates to substantially increase rates. KIC rightfully highlighted that ratepayers are "confused" to be in this position of facing a material rate increase during the rate moratorium. KIC is not contending Westar's request to increase its surcharge rates is a violation of the base rate moratorium. Rather, KIC is providing the necessary context for the Commission to understand the unjustness and unreasonableness of the Westar Application *from the perspective of ratepayers*.

D. Westar and Staff Provide No Additional Support for the Proposition that Westar Could Not Recover the 8% of Costs Assignable to MWP from MWP or Another Entity.

22. At paragraphs 42-50 of KIC's Initial Brief, KIC explains the acquisition of MWP's 8% interest may have been an expedient solution for Westar, but Westar has not proven the transaction to be necessary. KIC will not repeat these facts at length, but the record shows Westar took no steps to collect MWP's share of costs and quickly agreed to pay a substantial amount of money to acquire the 8% interest.

23 Westar and Staff both contend MWP either would not pay or would be "judgment proof." Westar and Staff's positions rely on the statements of MWP – apparently taking the validity of such statements on faith. These MWP positions have not been tested in any manner. In fact, to KIC's knowledge, no evidentiary or legal analysis of these claims has ever been presented to the Commission.

24. Instead of demonstrating to the Commission the actions it took to recover costs from MWP, Westar cites the testimony of Staff witness Justin Grady that "MWP 'was upfront about the fact that it did not intend to pay for any costs over and above what it could generate from

SPP [Integrated Marketplace] market sales and capacity revenues.'"¹⁹ And Staff notes, "MWP's plan was to rely on Westar as a financial backstop for any potential revenue shortfalls...The truth is MWP had no desire to own and operate the 8% portion of JEC."²⁰ These statements are not evidence of the legal merits of MWP's position. These statements just repeat MWP's threats. As noted above, Westar and Staff both appear to rely heavily on the statements – and apparent *potential* litigation positions – of MWP to support the need for this transaction. The record in this docket is devoid of *any* evidence of Westar's collection efforts or consideration of alternatives to an acquisition.

25. KIC also takes issue with Staff's suggestion that CURB and KIC do not appreciate the full context of this transaction and statement that "It is apparent that neither [CURB nor KIC] understands what MWP actually was."²¹ Staff seems to imply that KIC would not advocate for its current positions if it was aware of the proceedings in Docket No. 19-MPCE-064-COC ("19-064 Docket"). Contrary to Staff's suggestion, KIC tracked the 19-064 Docket during its pendency and undertook a detailed review of the official record as part of its analysis of this case. The record of that proceeding is cited throughout KIC's Initial Brief. KIC is aware of the context of the 19-064 Docket and understands MWP's positions in that proceeding. None of MWP's claims in the 19-064 Docket change the facts in this case.

26. Moreover, Westar selected the contents of its Application and supporting testimonies in this Docket. To the extent this proceeding's record is inadequate or does not reflect sufficient "context" (as suggested by Westar and Staff), such an inadequacy should fall on the party

¹⁹ Westar Brief, p. 15.

²⁰ Staff Brief, pp. 16-17.

²¹ Staff Brief, p. 16.

with the burden to support the Application. Such a contention should not be used a shield against consumer interests seeking to voice their concerns about the proposed transaction.

E. Staff's Contention that KIC and CURB have Offered No Guidance on How to Apply a Deregulation Option is Wholly Inconsistent with the Official Record.

27. At pages 15-16 of its Brief, Staff states,

While KIC and CURB make generalized suggestions on deregulating the ownership interest, the parties offer no path forward on the process of deregulating the asset or provide any financial analysis as to the impact that decision has on Westar's utility operation. A Commission order that suggests deregulation would have a plethora of outstanding issues that KIC and CURB have ignored and the record is completely silent on. The Commission would be tasked with drafting an order suggesting or requiring deregulation with no guidance or evidence from this docket.²²

28. Staff's statements are entirely inconsistent with the record in this case. In his Direct Testimony, KIC witness Michael Gorman provided specific guidance to the Commission on this issue. Mr. Gorman recommended the Commission disallow specific cost categories related to the 8% interest from retail rates and require Westar and Commission Staff to "agree on appropriate accounting mechanisms to track total JEC costs and allocate them between retail cost of service jurisdictions, and the non-regulated jurisdiction."²³

29. Furthermore, Staff witness Justin Grady testified to the feasibility of this option at hearing, stating,

[I]t wouldn't be anything inventive or difficult to administer. We just, we don't even have to call it a deregulated or unregulated asset. It's below the line. Right. You cannot recover these costs from retail customers. And so you're free to monetize and get all the value out of that asset that you want to. I mean, there probably would have to be some parameters around allocating all of the fixed costs, right, decommissioning costs and any potential shareholder...litigation costs or liability claims. But we could do it.²⁴

²² Staff Brief, pp. 15-16.

²³ Direct Testimony of Michael P. Gorman, June 4, 2019, pp. 17-18.

²⁴ Tr., pp. 173-74.

It is difficult to square the alarmist statement in Staff's brief with Mr. Grady's very candid advice that an "unregulated" approach "wouldn't be anything inventive or difficult to administer."

30. Perhaps most importantly, the Westar rate case Settlement expressly finds the "unregulated" option will be followed if the Commission denies Westar's Application. At paragraph 29, the Settlement states,

In the event that the Commission denies Westar's filing, Westar shall not be allowed to recover the regulatory asset containing deferred lease and NFOM expenses, and Westar shall be allowed to retain any wholesale sales that are directly attributable to the 8% portion of JEC for which the Commission denies Westar recovery of the incurred cost of owning or leasing and operating the 8% portion of JEC.

31. The "default" relief agreed to by all the parties, in the event Westar's Application is denied, is clearly the "unregulated" approach. Yet, Staff now contends the Commission should not adopt this default alternative relief set forth in the Settlement – which was agreed by the parties and approved by the Commission – because the Commission lacks "guidance and evidence" to approve such an approach. Staff's position is inconsistent with the official record and should not be given weight by the Commission.

32. Adopting the alternate "unregulated" approach is feasible. However, if the Commission does not believe it possesses record evidence to implement this approach at this time, its order on Westar's Application can simply require Westar and Staff to "agree on appropriate accounting mechanisms" to track and allocate JEC costs, as recommended by KIC witness Gorman and Staff witness Grady. Following this agreement, the Commission can issue a further order implementing the unregulated approach.

WHEREFORE, KIC respectfully requests the Commission deny Westar's Application and allow Westar to operate the 8% interest in Jeffrey Energy Center as contemplated at paragraph 29

of the 18-328 Settlement and under the regulatory parameters described at pages 17-18 of the Direct Testimony of Michael P. Gorman.

Respectfully submitted,

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VERIFICATION

STATE OF KANSAS)
) ss:
COUNTY OF JOHNSON)

Andrew J. French, being duly sworn upon his oath, deposes and states that he is the Attorney for the Kansas Industrial Consumers Group, Inc., that he has read and is familiar with the foregoing *Reply Brief of Kansas Industrial Consumers Group, Inc.*, and the statements therein are true to the best of his knowledge, information, and belief.



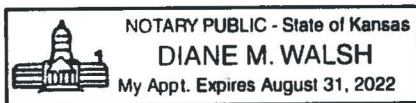
Andrew J. French

SUBSCRIBED AND SWORN to before me this 7th day of August, 2019.



Notary Public

My Appointment Expires:



CERTIFICATE OF SERVICE

I hereby certify a true copy of the foregoing was served by electronic mail (when available) or regular U.S. mail (unless otherwise noted), the 7th day of August, 2019, to the parties below:

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