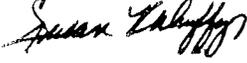


THE STATE CORPORATION COMMISSION
OF THE STATE OF KANSAS

Before Commissioners: Thomas E. Wright, Chairman STATE CORPORATION COMMISSION
Michael C. Moffet
Joseph F. Harkins
JAN 24 2008

In the Matter of the Petition of Westar)
Energy, Inc. and Kansas Gas and Electric)
Company (collectively "Westar") for)
Determination of the Ratemaking Principles) Docket No. 08-WSEE-309-PRE
and Treatment that Will Apply to the)
Recovery in Rates of the Cost to be Incurred)
by Westar for Certain Electric Generation)
Facilities and Power Purchase Agreements)
under K.S.A. 2003 Supp. 66-1239.)
 Docket Room

**RESPONSE OF CURB TO PETITION FOR CLARIFICATION
AND RECONSIDERATION OF WESTAR ENERGY, INC.
AND KANSAS GAS AND ELECTRIC COMPANY**

COMES NOW the Citizens' Utility Ratepayer Board (CURB) and files its Response to the Petition for Clarification and Reconsideration filed by Westar Energy, Inc. and Kansas Gas and Electric Company (Westar) on January 14, 2008, which requested that the Commission clarify or reconsider its December 27, 2007, Final Order (Order) in the above captioned matter. In support of its Response requesting the Commission deny Westar's Petition for Clarification and Reconsideration, CURB states:

I. THE COMMISSION SHOULD NOT CLARIFY OR RECONSIDER ITS DECISION TO ACCEPT WESTAR'S CAPACITY FACTORS AND HOLD WESTAR TO THOSE CAPACITY FACTORS.

1. The Commission Order states "Westar has asserted its capacity factor estimate are reasonable. For purposes of this hearing, the Commission will accept Westar's figures, and it will hold Westar to them." (Order, at ¶ 34). Westar now asks that the Commission clarify that its Order

does not set any capacity factor guarantees or performance standards based on the estimates provided by Westar in its application. (Westar PFR, at ¶ 12). Westar asks the Commission to clarify that its intention was not to convert good faith performance estimated into performance guarantees in some future proceeding. (Westar PFR, at ¶ 10). The Commission must deny Westar's request and should clarify that, given the risk consumers are exposed to through the ownership model, the evidence presented at hearing and relied upon by the Commission in finding Westar's application prudent should be deemed the standard at which Westar is held accountable.

2. In this case, CURB argued strongly that allowing Westar to own wind generating facilities was unreasonable because ownership was more expensive than purchase power agreements and that ownership placed consumers at a higher level of cost risk than do purchase power agreements. At best, Westar could only maintain that it believed ownership costs were about equal to PPA costs. While the Commission granted Westar's request over CURB's objections, the Commission specifically noted that ownership involves greater operating performance risk for ratepayers, O&M costs are likely greater than forecast, and that the probability of wind production below forecasted levels is higher than the probability wind production will exceed Westar's estimates. (Order, at ¶ 65). The Commission further stated that "unless wind turbines are tended and maintained at a high level, their performance and the wind capacity factor will diminish, and as a result, the cost of wind energy will rapidly escalate for ratepayers." (Order, at ¶ 79).

3. Having granted Westar's request to own wind generating facilities, and having recognized that ownership shifts risk to consumers, the Commission should now hold Westar to the cost and capacity factor estimates presented in evidence in support of its application. This Commission, in approving Westar's request to own a portion of the wind generating facilities, relied

on scenarios created by Westar's witness Ellenbaas and Staff witness Dr. Cita. However, Dr. Cita admits that if the costing assumptions he started with changed, it would affect whether or not the four scenarios he laid out are likely to be prudent. (Cita, Tr. Vol. 3, at 498). A change in the capacity factor assumptions used in Ellenbaas' model or Dr. Cita's analysis, by definition, change the cost scenarios relied upon by the Commission in granting Westar's request. If Westar cannot maintain the capacity factors it supported in evidence (evidence relied upon by the Commission in determining the ownership of wind is prudent), then whether the Commission's decision is supported by substantial competent evidence is called into question.

4. The Commission determined that Westar asserted it is capable of maintaining a certain capacity factor level, which the Commission found to be an important pillar of Westar's application and the issues of prudence in this docket. The Commission further determined that Westar vigorously countered Staff and CURB's assertions that Westar may be overstating the level of performance that may be expected. (Order, at ¶ 81). Westar must be held accountable for its evidence.

5. Westar's CEO stated on the stand that the Commission has the authority and jurisdiction, irrespective of the adoption of ratemaking principles in this docket, to conduct future prudence review of Westar's wind generation plants. (Order, at ¶ 12). Westar further conceded the Commission's continuing authority and jurisdiction to review its operations and disallow imprudently spent costs, including reducing Westar's return on investment in wind generation and any incentive return. (Order, at ¶ 86). Mr. Moore specifically testified:

Well, we put the asset that we own in the rate base, but as you well know, the Commission always has the right to come back, and if we're not operating our facilities correctly, they have the right to come back and, and say that's a problem,

Westar, you need – put some penalty on us at that point in time. (Moore, Tr. Vol. 1, at 56).

6. Westar’s petition for clarification, if granted, would mean that the evidence relied upon by the Commission in granting Westar’s application is inherently unreliable. Having granted Westar’s application and placed consumers at risk for ownership costs, the Commission will have no standard by which to judge Westar’s performance if it does not hold Westar to the evidence it submitted. If Westar’s wind capacity factors turn out to be substantially less than submitted and supported by Westar in its application, consumers will bear the cost with no recourse. Consumers are only protected if the Commission holds Westar to the capacity factors it presented in evidence to the Commission to support its proposal as being prudent. If Westar now believe those standards are too high, the Commission should re-open its decision and re-determine whether Westar’s decision is prudent based on more realistic capacity factors. Absent this, Westar’s request for clarification should be denied, and the Commission should hold Westar to the capacity factors relied upon in approving this application.

II. THE COMMISSION SHOULD NOT RECONSIDER ITS DECISION TO DENY WESTAR’S REQUESTED PREMIUM RATE OF RETURN.

7. Westar’s argument that the Commission should reconsider its denial of Westar’s request for a premium rate of return under K.S.A. 66-117(e) is premised on its statement that,

The Commission’s decision on this issue was based, in part on (1) the Commission’s statement that Westar’s shareholders – without any additional return – are already receiving “an almost 11% ROR (pre-tax cost of capital)” on wind generation owned by Westar, and (2) the Commission’s conclusion that a distinction can be made between investment in wind generation and investment in energy efficiency programs in the application of K.S.A. 66-117(e).

8. Before even addressing these two points raised by Westar, it is important to note that Westar's request for reconsideration focuses solely upon two factors, which were among numerous additional factors cited by the Commission in support of its decision on this issue. While Westar implicitly acknowledges this by admitting the Commission's decision was only "based, **in part**" on these two factors, CURB will summarize below both the numerous additional factors cited by the Commission in support of its decision to deny the premium return, as well as other substantial competent evidence in the record that provides further support to the Commission's decision on this issue.

9. The numerous additional factors cited by the Commission in support of its decision are summarized below:

- No rate of return premium has been granted in prior wind energy dockets heard by the Commission. (Order, at ¶ 109).
- The 1% additional rate of return requested by Westar would have amounted to an addition of approximately \$47 million over the period from 2009 through 2029. (Order, at ¶ 110).
- Westar's risk in its wind generation proposal was effectively mitigated by the Commission's other determinations in this predetermination docket. (Order, at ¶ 111).
- The circumstances in this preapproval docket justify relieving ratepayers of the cost of an additional return in light of the close analysis involved in determining prudence and weighing Westar's PPA and ownership proposal. (Order, at ¶ 112).
- Despite Staff's recommendation and not unwarranted concerns, the Commission declined to implement an incentive mechanism at this time. (Order, at ¶ 112).
- The balance between shareholders and ratepayers is adequately addressed without the 1% incentive in light of:
 - the uncertainties inherent in wind generation and
 - the narrow margins as to whether PPAs or ownership is more costly, even assuming O&M costs and capacity factors are as forecasted. (Order, at ¶ 112).
- The possibility of additional costs to ratepayers related to firm transmission. (Order, at ¶ 112).
- The opportunity for Westar to make a request again in the event Westar's performance or other circumstances support an argument the Commission should consider changing its decision. (Order, at ¶ 112).
- In approving Westar's proposal to own wind generation, the Commission determined that the

ownership and PPA options were of comparable cost, and removing the 1% incentive from Westar witness Elenbaas' forecasts increased the forecast net benefit attributable to wind resources. (Order, at ¶¶ 37, 57).

- The lower revenue requirement resulting from the Commission's decision not to grant the 1% ROR adder results in a cushion against greater than anticipated O&M costs and lower than anticipated performance capacity factors. (Order, at ¶ 87).
- Ownership involves greater operating performance risk for ratepayers than PPAs, including:
 - It is more likely wind O&M costs will be greater than forecasted rather than lower than forecasted.
 - It is more likely wind production will be lower than forecasted rather than higher than estimated by Westar.
 - Wind generation's declining, asymmetrical cost structure means increases in production will not lower per unit costs as much as similar decreases in production will increase unit costs. (Order, at ¶ 65).
- PPAs could be less risky to customers than ownership for the reason that price is fixed under PPAs and the developer, not ratepayers, bear such risks as lower than optimal performance, higher than anticipated O&M costs, and other risks. (Order, at ¶ 66).

10. Additional substantial competent evidence in the record that provides further support to the Commission's decision on this issue, although not specifically cited by the Commission, include:

- When enacted in 1978, utilities had to risk capital and invest first, then come to the Commission to seek recovery of their investment. Now, with pre-approval, no such risk exists and the Commission should do a public interest analysis before considering a request for a rate of return premium. (Post-Hearing Suggested Findings Of Fact And Conclusions Of Law With Supporting Memorandum Of The Citizens' Utility Ratepayer Board, ¶ 90).
- K.S.A. 66-117(e) permits the KCC to apply a return on investment premium, but it does not require that utilities be awarded a return premium. Thus, the KCC has the discretion to decide whether or not a premium return is warranted. (Crane D. Test., at 29-30).
- Westar's request for a 1% premium in its overall return represents a 2.24% increase in return on equity. The 1 percent return on investment premium requested by Westar will add approximately \$46.8 million to ratepayers' bills over the next 20 years. (Crane, D. Test., at 31-32; Glass, Tr. Vol. 3, at 443).
- Awarding a return on investment premium would provide a significant incentive for utilities to own wind generation rather than to enter into PPAs that may be more economical. This creates a bias toward ownership by the utility, ownership that may not be in the best interests of ratepayers. The Company's own studies in this proceeding demonstrate that the addition of wind generation is likely to cost ratepayers more than the

addition of conventional generation alone and that owning wind generation is more expensive for ratepayers than entering into PPAs. (Crane, D. Test., at 30).

- The KCC should not require ratepayers to pay a premium return to shareholders, especially since it is ratepayers that will be exposed to the subsequent risks of ownership, such as potential O&M cost increases, capacity factor fluctuations, transmission upgrade costs, regulation, intra-hour costs, and increased integration capacity costs, performance problems, and rapidly evolving technology. (Crane, D. Test., at 30; Cita, Tr. Vol. 3, at 501; Glass, Tr. Vol. 3, at 437-439; Reed, Tr. Vol. 2, at 265-266; Sanderson, Tr. Vol. 3, at 416-419).
- The potential for federal renewable portfolio standards weighs against approving a premium return to shareholders for investing in wind energy. (Crane, Vol. 2, at 369).
- If the premium return determination is made in this predetermination proceeding, the Commission will not be able to revisit that issue in the 20 years the wind turbines are intended to be in operation. (Crane, Vol. 2, at 370, 372).
- Ratepayers will be experiencing significant rate increases over the next few years with respect to Westar's planned \$2.64 billion of capital expenditures over the 2006-2009 period, including \$344.8 million of actual expenditures made in 2006. The 2006-2009 capital expenditures will initially add over \$300 million to the Company's annual revenue requirement, assuming Westar's currently authorized rate of return. Westar's jurisdictional ratepayers will likely be responsible for a large majority of this additional revenue requirement. Westar has also indicated that a high level of capital expenditures is likely to continue for some intermediate period. In evaluating Westar's request for a return on investment premium, it is imperative that the KCC consider the significant financial burden that will be placed on the State's ratepayers in any case. There is no reason to place an even greater burden on ratepayers by awarding shareholders a premium return, especially when one considers the significant rate increases that ratepayers are likely to experience over the next few years. The requested return on investment premium will add approximately \$46.8 million to ratepayers' bills over the next 20 years. Moreover, shareholders will receive this premium without incurring any additional risk. (Crane, D. Test., at 31-32; Tr. Vol. 2, at 343, 370).
- Utilities should be a partner with the Governor, the legislature, and other organizations that are advocating for wind energy, so a premium return should not be necessary. (Crane, Vol. 2, at 370-371).
- Staff concluded the only relevance of the 1 percent rate of return adder requested by Westar is that it raises the cost of ownership for ratepayers. (Glass, D. Test., at 7; Tr. Vol. 3, at 441).
- Staff pointed out that the rate of return adder will make wind generation even more expensive and less competitive as an investment from a ratepayer's point of view. Staff also notes that to maintain public support for renewable resources, the added expense of wind generation needs to be minimal – if the gap between wind generation and conventional generation becomes too large, public opinion may turn against wind generation. (Glass, D. Test., at 23).

11. The above demonstrates that the Commission's decision to deny the premium return is supported by substantial competent evidence. Westar's request for reconsideration of the Commission's decision based solely on the two factors cited is unpersuasive and erroneous. Further, Westar's argument with respect to each of these factors is misplaced.

12. Westar first argues that the "premise that Westar's receipt of its standard rate of return on its investment in wind generation obviates the need for an additional return is faulty." The Commission did not state that receipt of its standard rate of return on its investment "obviates" the need for an additional rate of return, or anything similar to this characterization. While the Commission did "note" that granting Westar the ownership it seeks provides its shareholders with an almost 11% rate of return (Pre-tax cost of capital), it clearly followed that statement by finding, "Westar's risk in this venture is effectively mitigated by the Commission's other decisions in this predetermination docket." The Commission's other risk mitigating decisions and reasons supporting the Commission's decision were clearly stated throughout the Commission's Order and are itemized above.

13. Furthermore, Westar's argument about the correct characterization of its return on equity (ROE) is irrelevant and argues facts not in evidence. However, even ignoring the irrelevancy and the facts not in evidence deficiencies, Westar's argument is without merit.

14. Westar argues its ROE is lower than the ROEs authorized for other Kansas utilities and other utilities in this geographic area during the same period of time. This argument simply lacks credibility in light of the evidence in the record in Westar's last rate case. Specifically, Westar complains that its ROE is lower than the 10.5% ROE authorized for Aquila Networks – WPK in the

first quarter of 2005, and argues Westar's authorized ROE is also lower than the average ROE in the United States, citing a national average authorized ROE for the first nine months of 2005 of 10.41%. (Westar PFR, ¶ 18). However, the evidence in the 05-WSEE-981-RTS record showed that second-quarter commission-allowed ROEs in the 9.63% to 10.13% range, *not 10.41%* as asserted by Westar. (See, Westar Hearing Exhibit 9, *Regulatory Focus*, Regulatory Research Associates Inc. (July 2005), 05-WSEE-981-RTS). Clearly, the 10% ROE Westar obtained in its last rate case was not only within the 9.63% to 10.13% range granted by other state Commissions, but was near the top of that ROE range.

15. Westar's complaint that its 10% ROE is lower than the 10.5% ROE obtained by Aquila in 2005 lacks even more credibility in light of testimony offered by its own executive. Westar witness Greg Greenwood testified in Westar's last rate case that not only would the investment community consider Aquila a more risky investment than Westar, but that "Aquila today would be the most risky utility investment in the state." (Greenwood, Tr. Vol. 3, at 469, 05-WSEE-981-RTS) (emphasis added). Westar's complaint that its ROE was not equal to or higher than the ROE granted to Aquila, a utility that Westar's own executives considers the "most risky utility investment in the state," is therefore wholly without merit and unworthy of consideration by the Commission.

16. Westar's second argument likewise lacks merit. While K.S.A. 66-117(e) may not make a distinction between renewable energy generation and energy efficiency programs, the statute conveys to the Commission complete discretion on whether to award an incentive return.

17. As demonstrated above, the Commission cited ample substantial competent evidence supporting its decision denying Westar's request for an incentive return. Whether a renewable

energy generation proposal or energy efficiency program is granted a premium incentive is to be decided by the Commission after viewing the evidence related to the utility's individual application. Here, the Commission specifically concluded that it "decides each case on the unique facts involved, and the decision on the additional rate of return in this case is an example of that principle in action." (Order, at ¶ 115). As a result, the Commission's decision to deny Westar a premium return is fully supported by substantial competent evidence based on Westar's individual application, and is not arbitrary and capricious as alleged by Westar.

III. CONCLUSION.

18. On behalf of Kansas small business and residential ratepayers, CURB urges the Commission to deny Westar's Petition for Clarification and Reconsideration in its entirety. The Commission's decision is not arbitrary or capricious but is reasonable when viewed in its entirety.

Respectfully submitted,



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CERTIFICATE OF SERVICE

08-WSEE-309-PRE

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, or hand-delivered this 24th day of January, 2008, to the following:

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A handwritten signature in black ink that reads "Shonda Titsworth". The signature is written in a cursive style with a horizontal line underneath it.

Shonda Titsworth