



Corporation Commission

Pipeline Safety

Mark Sievers – Chairman, Kansas Corporation Commission

October 18, 2011

Agenda

- KCC Mission
- Challenges & Opportunities
 - National Economic Outlook

KCC' s Economic Mission

Minimize public harm due to market failures

- **Prevent the Harmful Exercise of Market Power**
 - Traditional utility regulation (electric, gas, water, telecom)
 - Direct regulation of rates, revenues, profits, service levels to emulate the results that would occur if the firm functioned in a competitive environment
- **Minimize Externalities Arising from Competition**
 - Conservation, Transportation, Pipeline safety regulation
 - Licensing, insurance requirements -- ensure minimum levels of competence, safety and environmental protection that would otherwise not be present in a competitive environment
 - Prevent over-exploitation of a shared resource
 - Common oil fields exploited by competitors will be quickly exhausted absent orderly, regulated process

KCC's Legal Mission

Ensure complete and fair proceedings

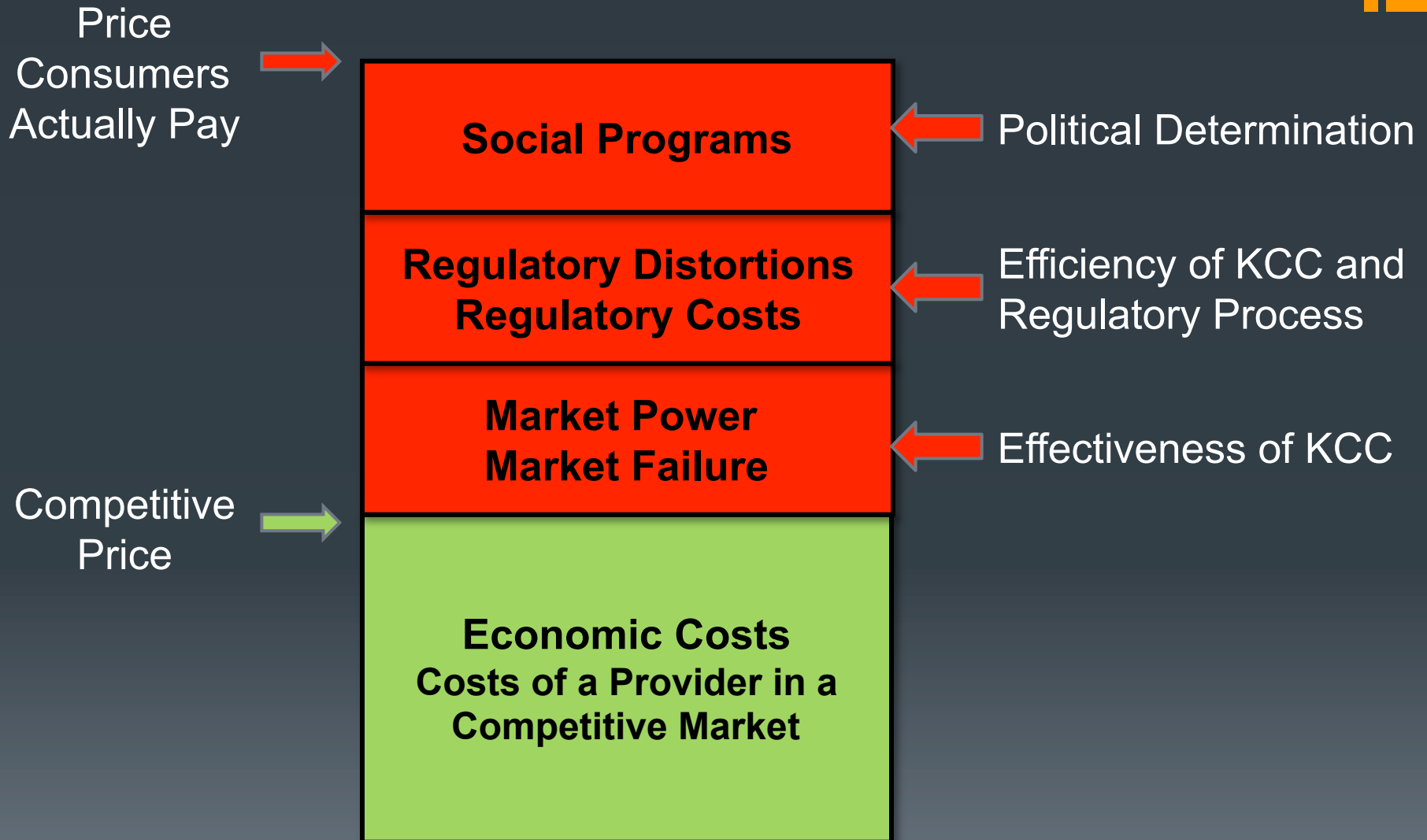
- **5th Amendment Mission** – due process, just compensation
 - *[No person shall] “be deprived of life, liberty, or property without due process of law; nor shall private property be taken for public use, without just compensation.”*
 - Just and reasonable rates for property devoted to public service
- **14th Amendment Mission** – due process, equal protection
 - *“nor shall any State deprive any person of life, liberty, or property, without due process of law; nor deny to any person within its jurisdiction the equal protection of the laws.”*
- **Compliance Mission** – comply with all applicable laws (state and federal) and KCC regulations
 - *Propose and pursue changes in laws when outdated, inefficient, ineffective or adverse to the public interest*

KCC' s Managerial Mission

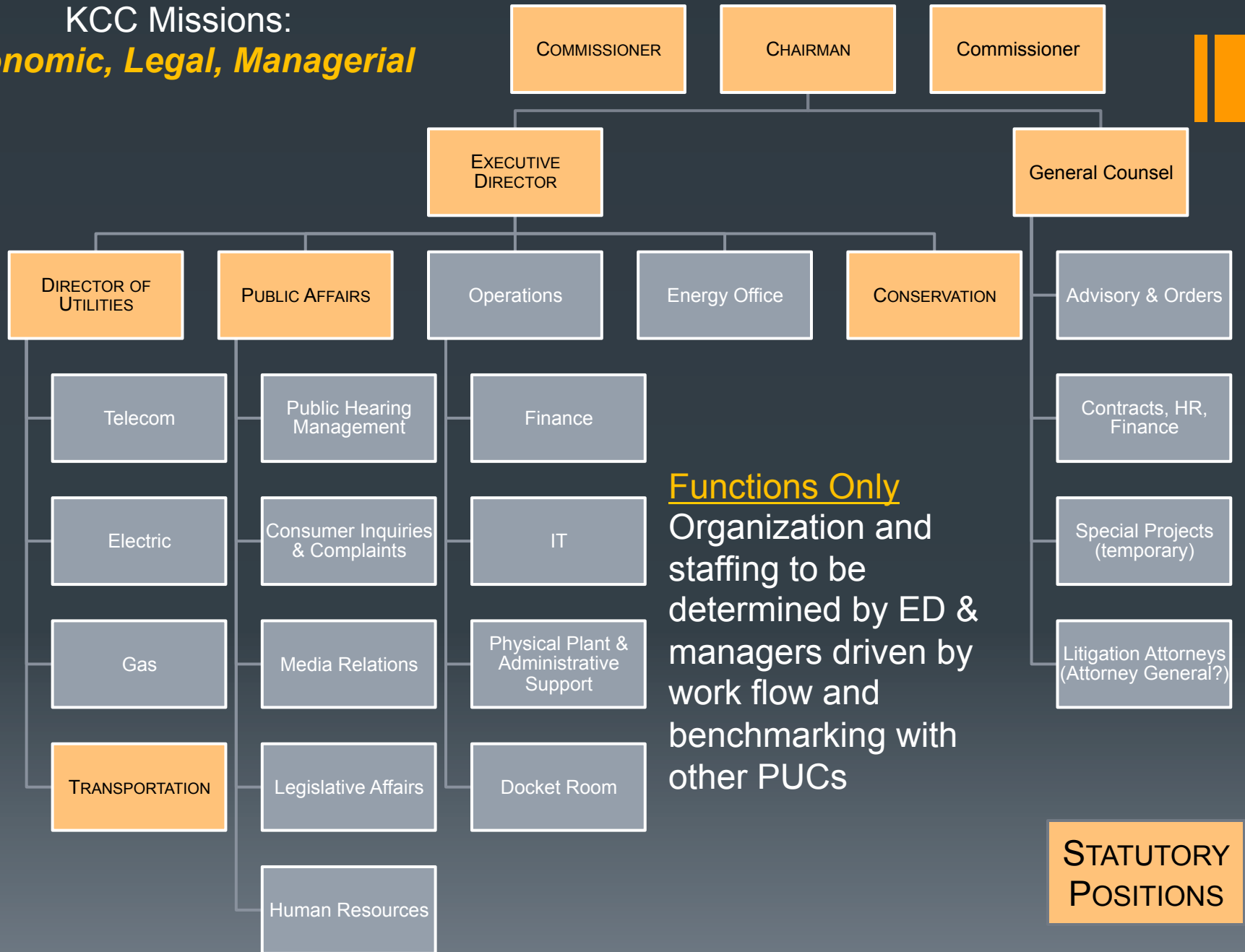
Responsible Steward of Public Resources

- Efficiency
 - Are we minimizing unnecessary costs and distortions borne by regulated utilities the costs of which are passed on to customers?
- Effectiveness
 - Are we accomplishing our core missions?
 - Are we implementing the public policies of the Governor and the Legislature?
- Accountability
 - Are we focused on the most important tasks and held accountable for achieving those tasks?
- Transparency
 - Are our actions visible to the public?

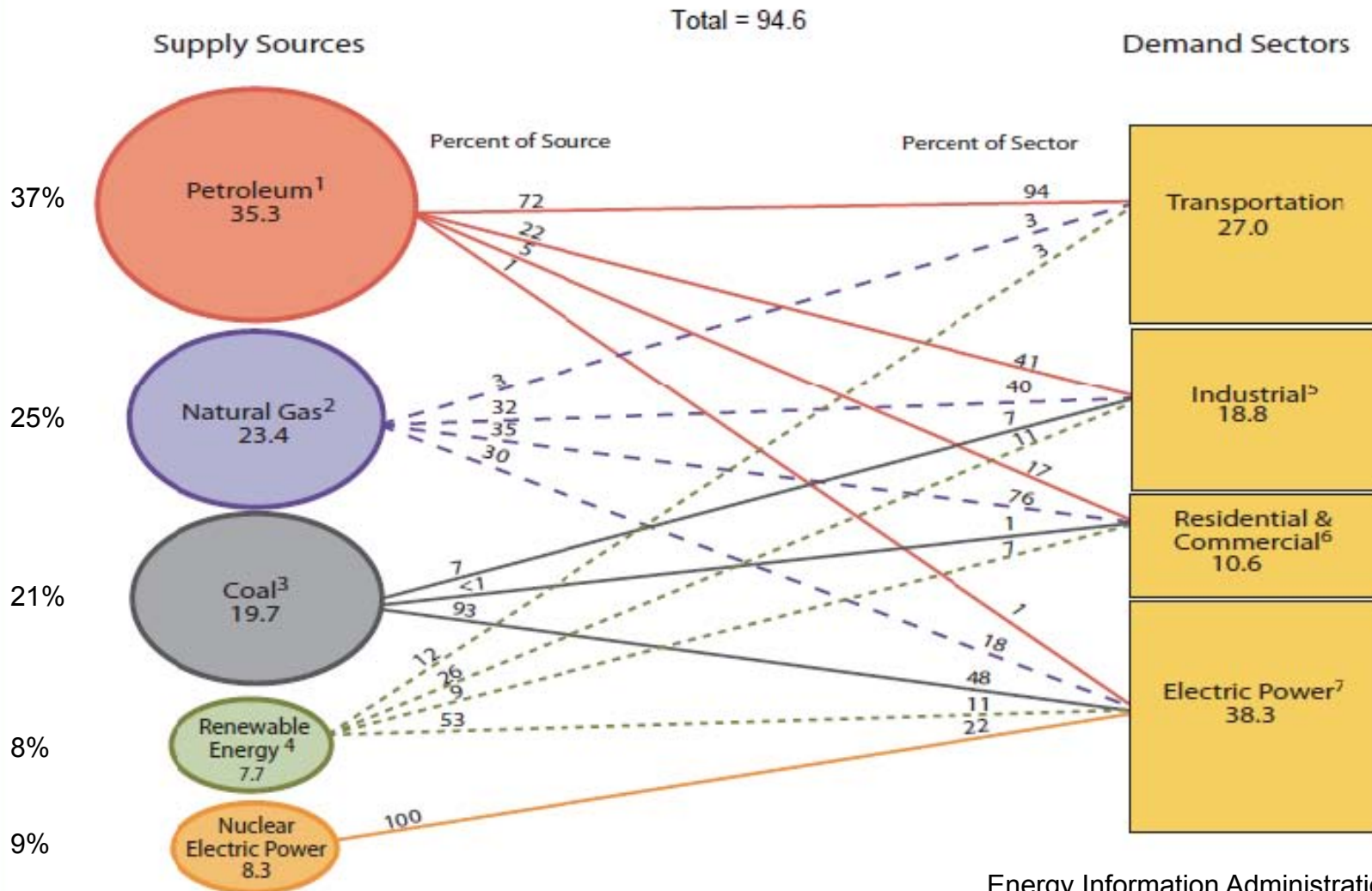
CONSUMERS ULTIMATELY PAY FOR REGULATION



KCC Missions: *Economic, Legal, Managerial*



Why Oil & Gas Matters



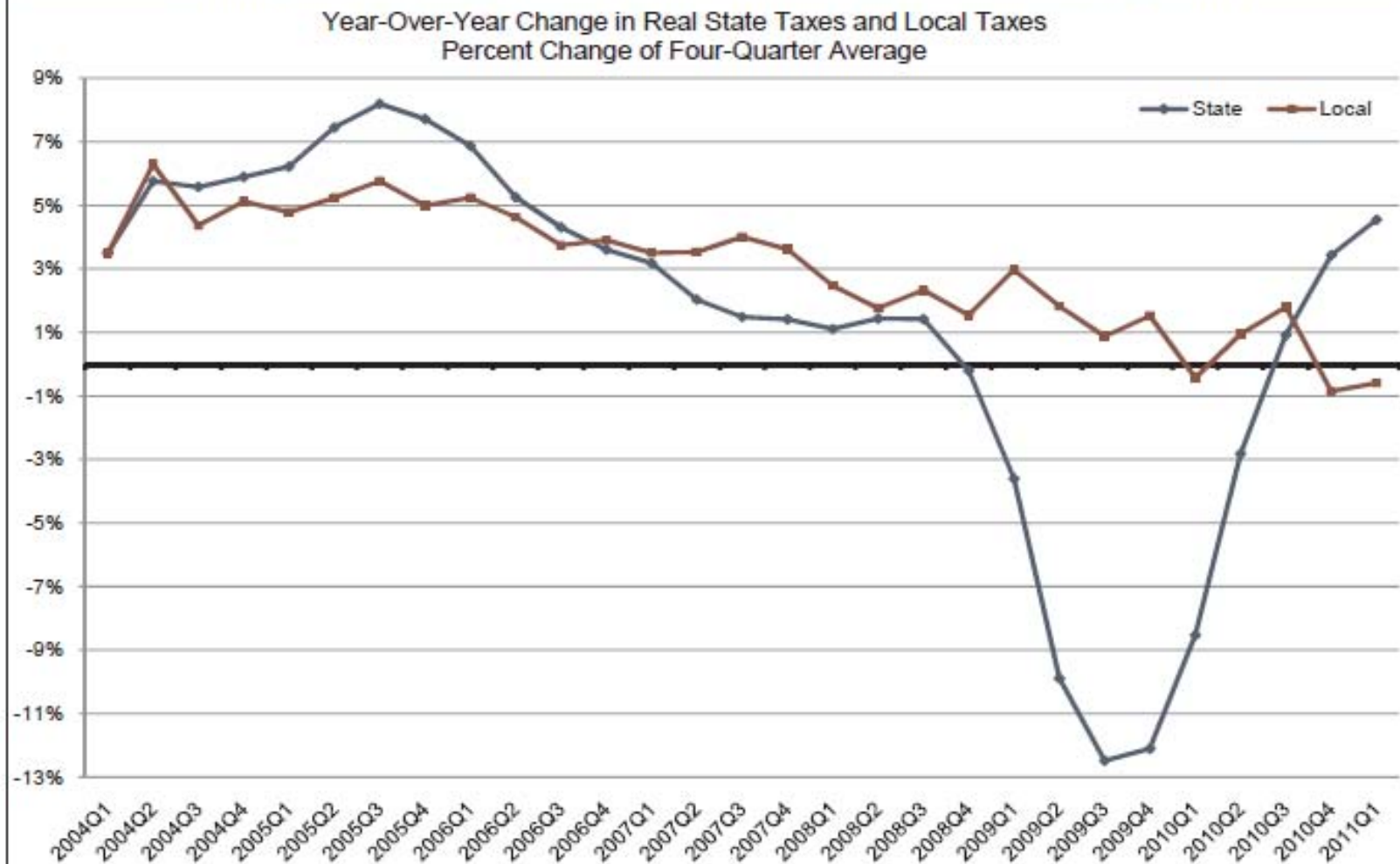
Challenges

National Economic Outlook

- So what makes this recession different?
 - Recession was substantially larger than any in the last 50 years
 - US GDP declined >14% in 2009
 - Stock market dropped about 45% -- DOW 2011 ≈ DOW 1998
 - 28 consecutive months of unemployment > 9% (not recovering)
 - Impact on state income & sales tax revenues
 - Failures of significant companies – Fannie Mae, Freddie Mac, AIG, Lehman Brothers, Merrill Lynch, GM, Washington Mutual, Wachovia, Madoff Securities, Circuit City, Mervyns, ...
 - More than 400 bank failures – dried up 3d party financing; banks now hold more cash than loans in their asset mix
 - Housing (real estate) prices collapsed (not recovering)
 - 2011 housing prices are 31% below 2006 level
 - Home equity dropped from about \$13 trillion to \$8 trillion (40% decline)
 - About 20% of US home sales are foreclosure sales
 - Substantial reduction in local property tax revenues

Impact on Tax Revenues

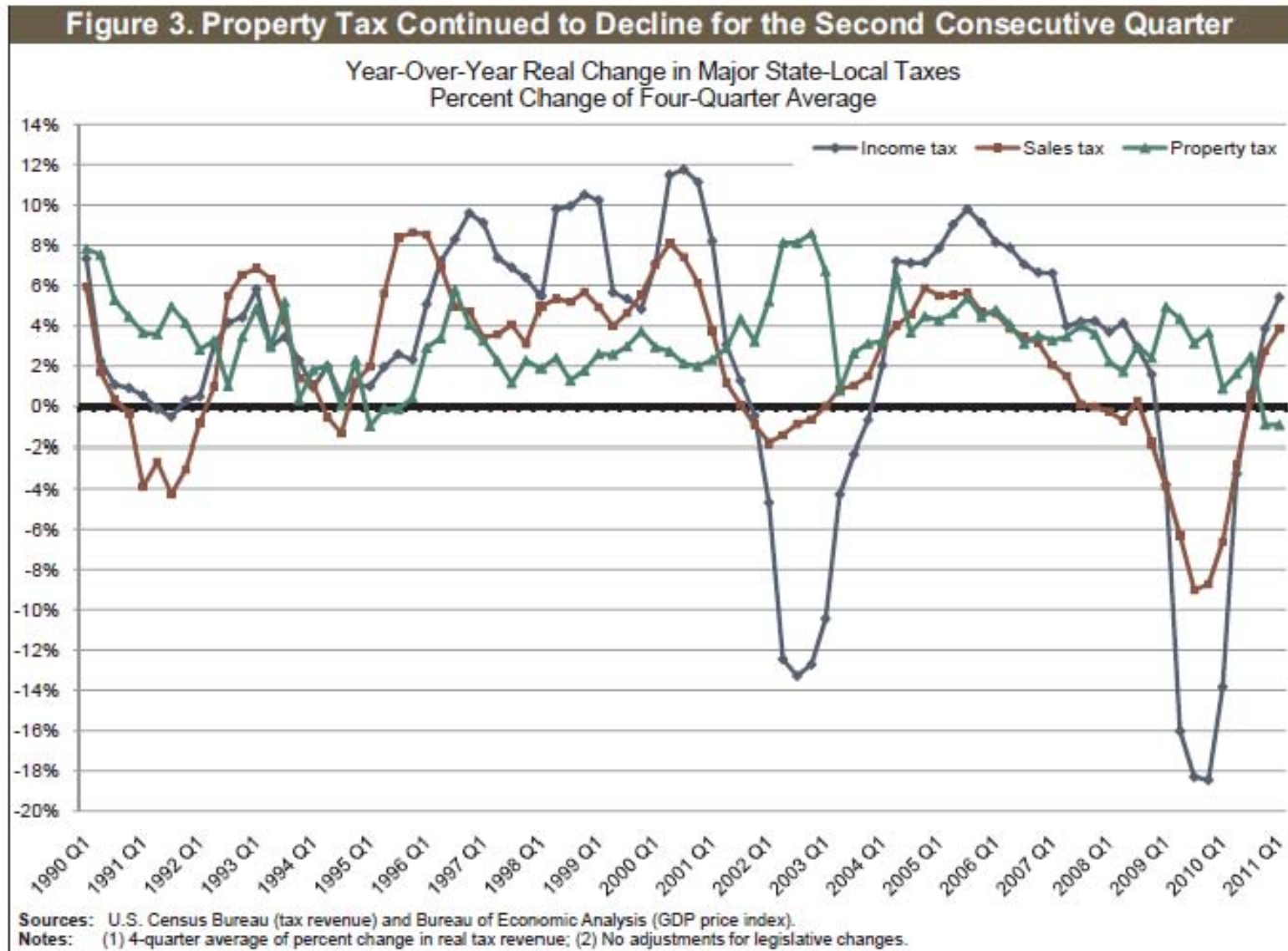
Figure 2. State Taxes Are Improving While Local Taxes Are Declining



Sources: U.S. Census Bureau (tax revenue) and Bureau of Economic Analysis (GDP price index).

Notes: (1) 4-quarter average of percent change in real tax revenue; (2) No adjustments for legislative changes.

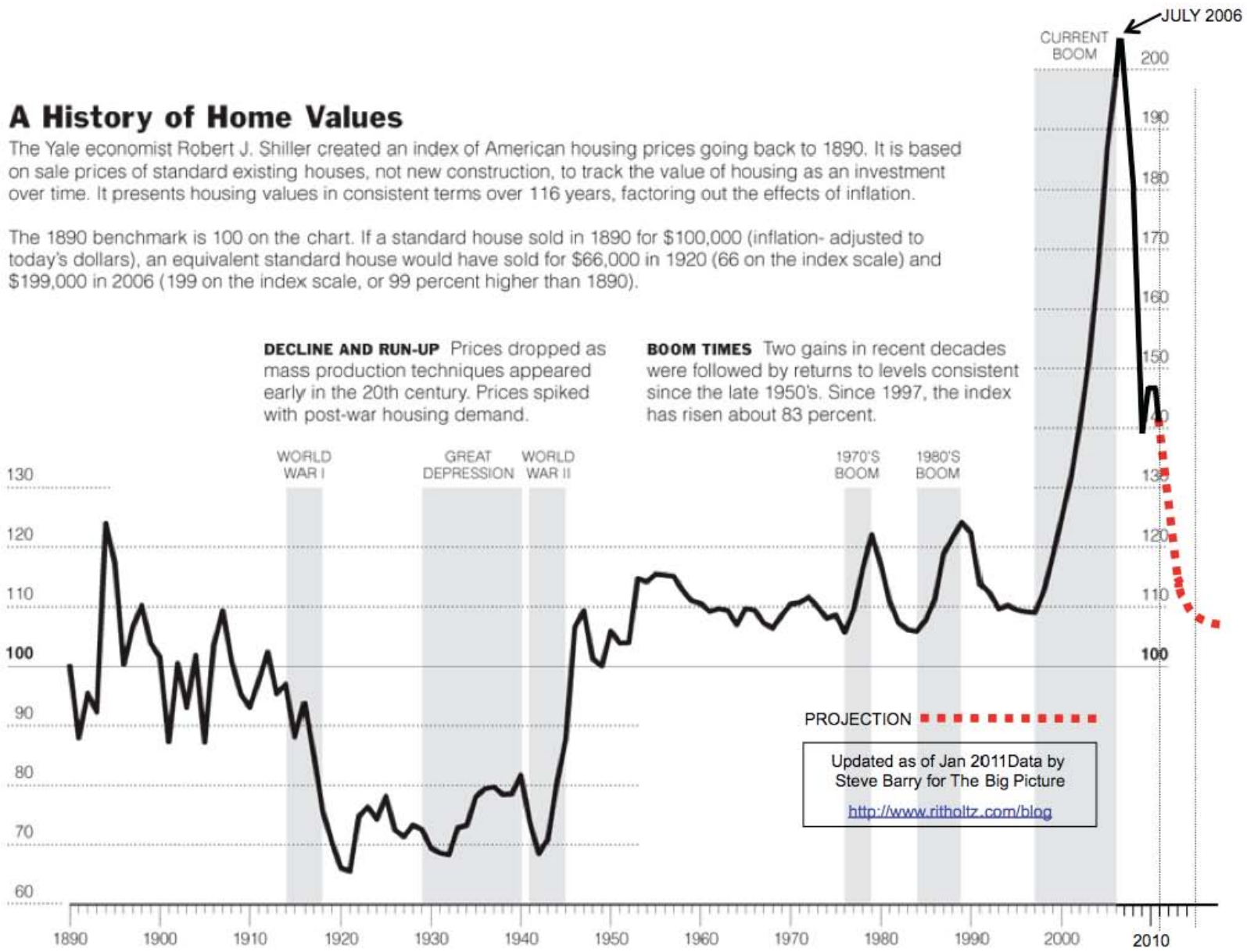
Impact on Tax Revenues



A History of Home Values

The Yale economist Robert J. Shiller created an index of American housing prices going back to 1890. It is based on sale prices of standard existing houses, not new construction, to track the value of housing as an investment over time. It presents housing values in consistent terms over 116 years, factoring out the effects of inflation.

The 1890 benchmark is 100 on the chart. If a standard house sold in 1890 for \$100,000 (inflation-adjusted to today's dollars), an equivalent standard house would have sold for \$66,000 in 1920 (66 on the index scale) and \$199,000 in 2006 (199 on the index scale, or 99 percent higher than 1890).



DECLINE AND RUN-UP Prices dropped as mass production techniques appeared early in the 20th century. Prices spiked with post-war housing demand.

BOOM TIMES Two gains in recent decades were followed by returns to levels consistent since the late 1950's. Since 1997, the index has risen about 83 percent.

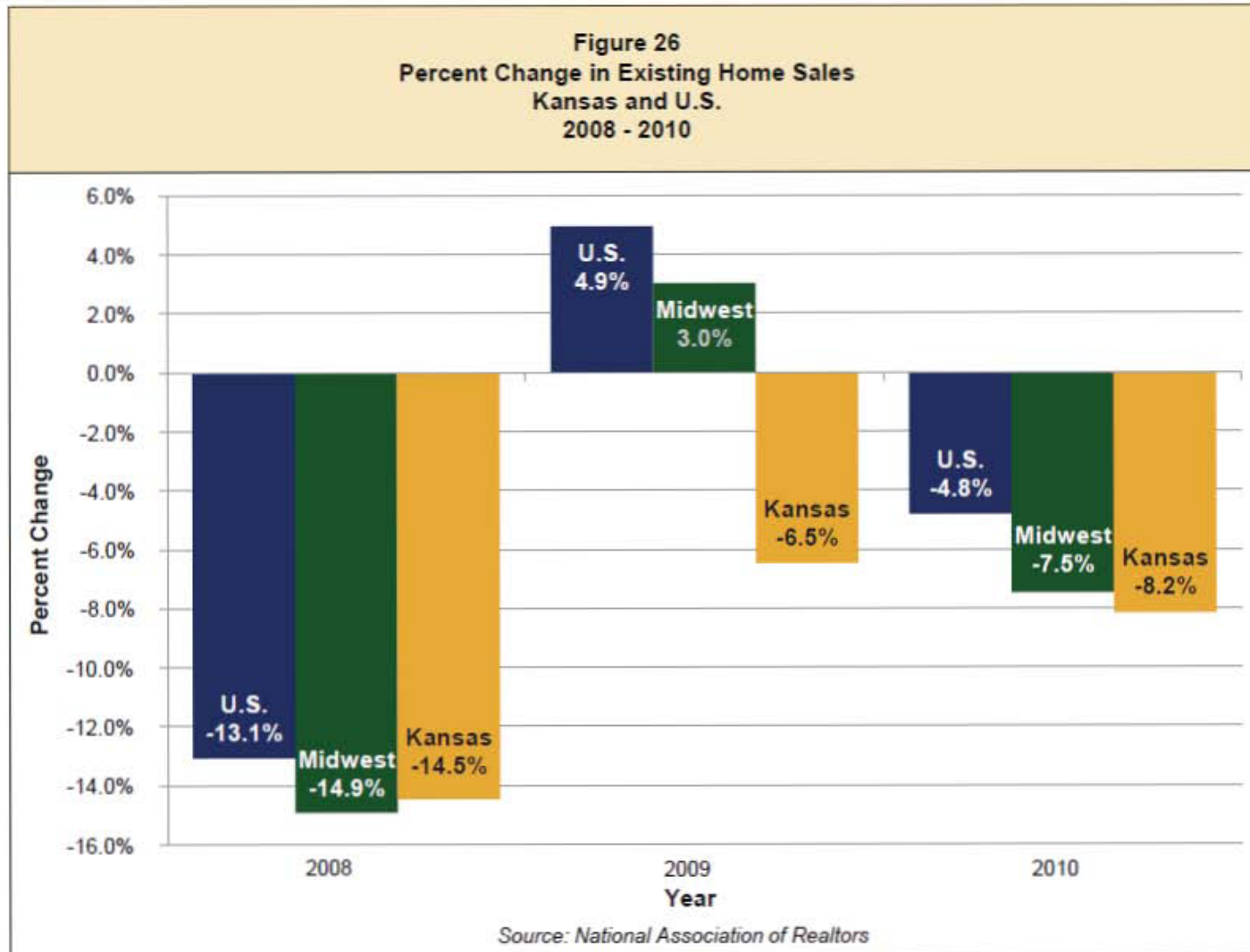
PROJECTION

Updated as of Jan 2011 Data by Steve Barry for The Big Picture
<http://www.ritholtz.com/blog>

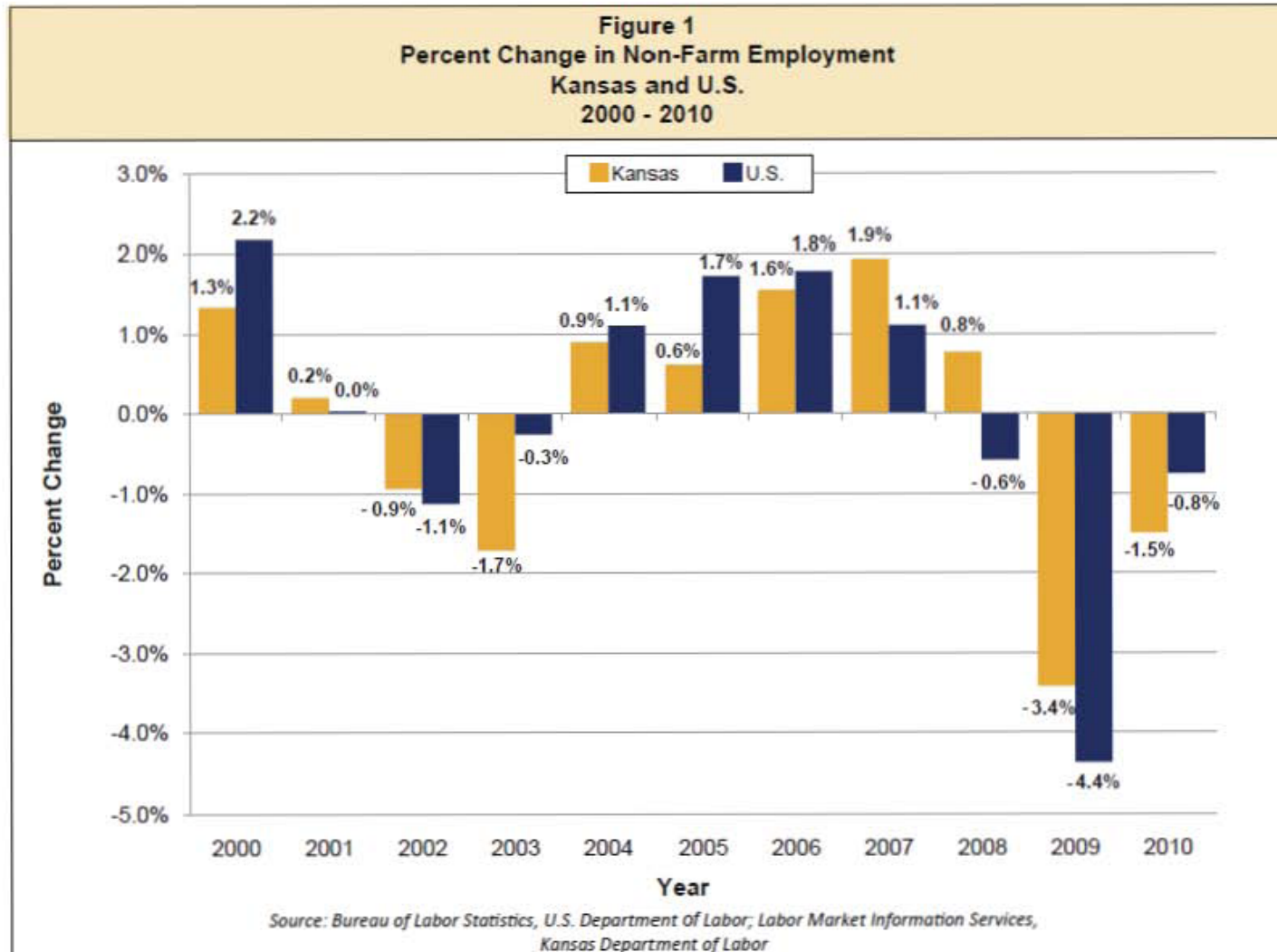
Source: "Irrational Exuberance," 2nd Edition, 2006, by Robert J. Shiller

Bill Marsh/The New York Times

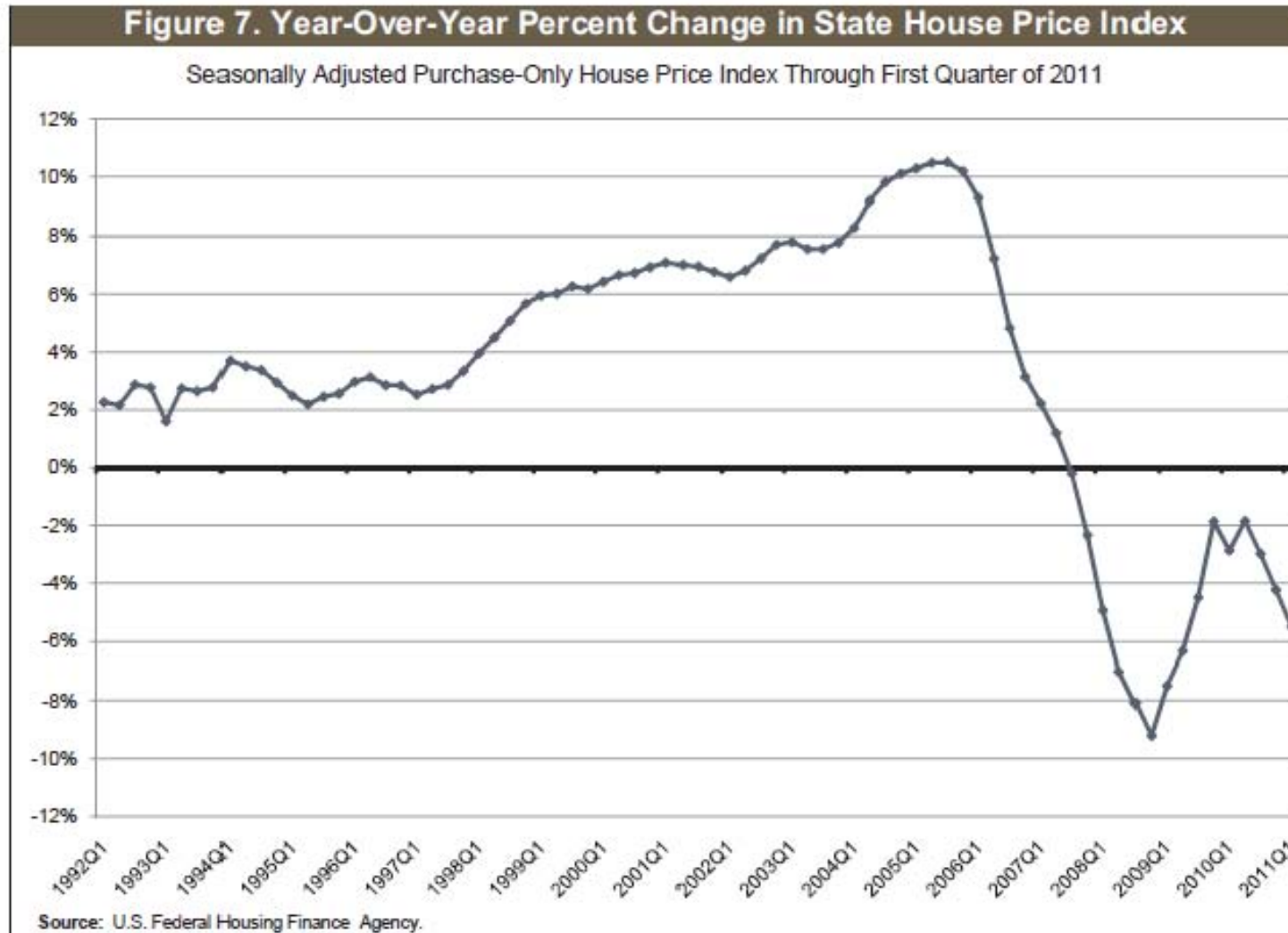
National Economic Outlook



National Economic Outlook

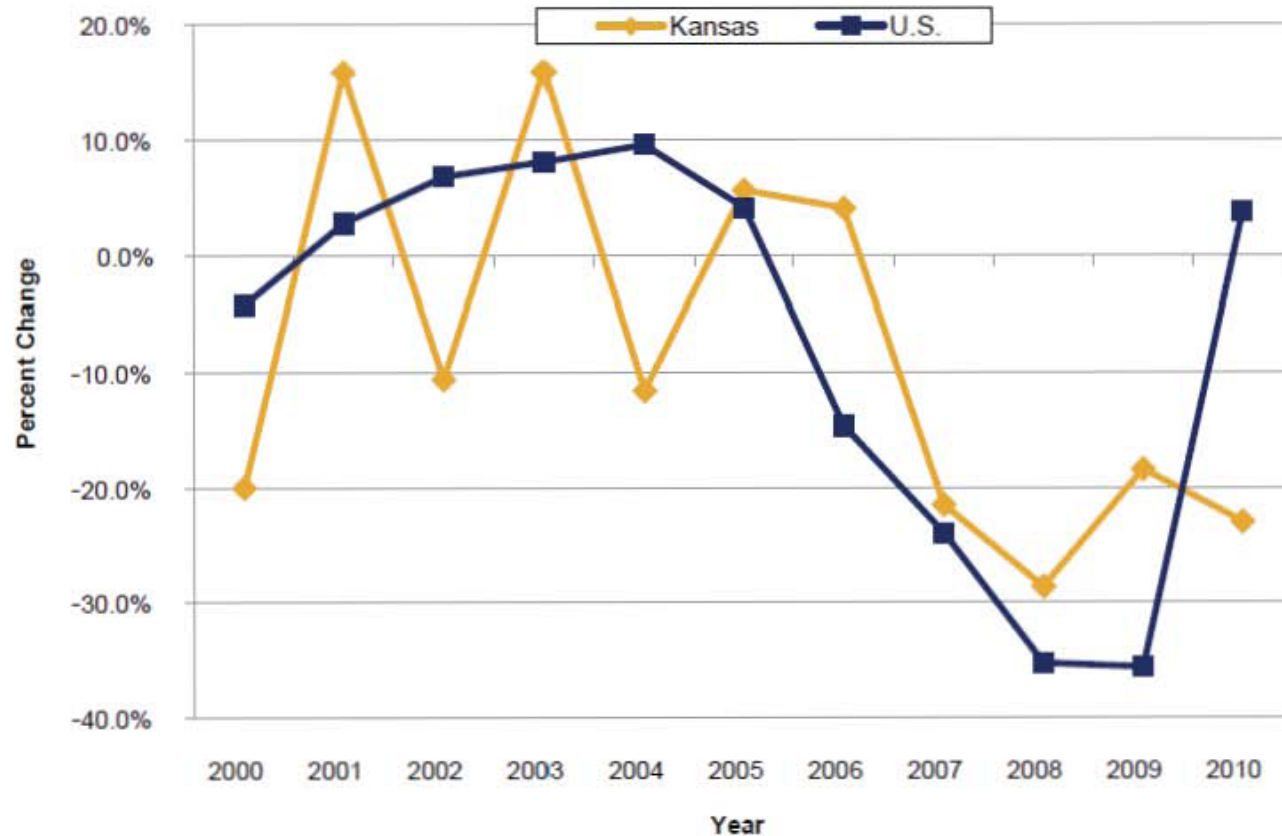


Impact on Tax Revenues



National Economic Outlook

Figure 27
Percent Change in Building Permits
Kansas and U.S.
2000 - 2010



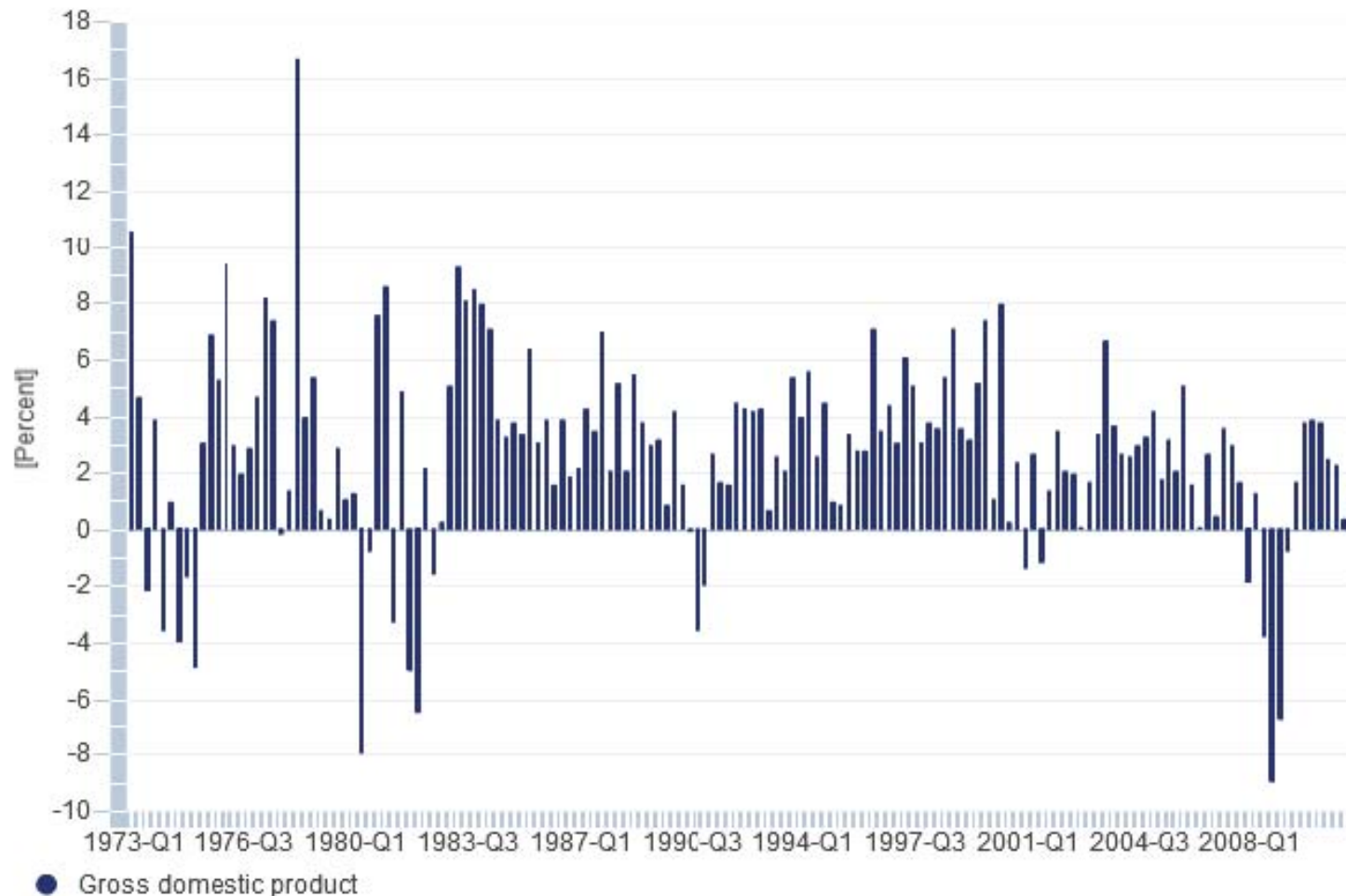
National Economic Outlook

- How have government efforts to combat the recession worked out?
 - **Monetary policy is maxed out with little or no impact**
 - Interest rates at historic lows with little impact
 - Money supply dramatically increased with little impact
 - Quantitative easing; purchase of toxic assets
 - **Fiscal policy (spending) has had little or no impact**
 - Stimulus spending (about \$1 trillion) has not reduced unemployment or grown the economy
 - **National debt level is at historic high levels and growing at double digits**
 - Federal government borrows about 40¢ for every \$1 it spends
 - Spending by government (Federal, state, local) is about 40% of GDP
 - Debt disasters: Greece, Italy, Spain, Portugal, Argentina, Mexico, Post WWI Germany, Zimbabwe
 - Debt Puzzle: Japan

National Economic Outlook

Table 1.1.1. Percent Change From Preceding Period in Real Gross Domestic Product

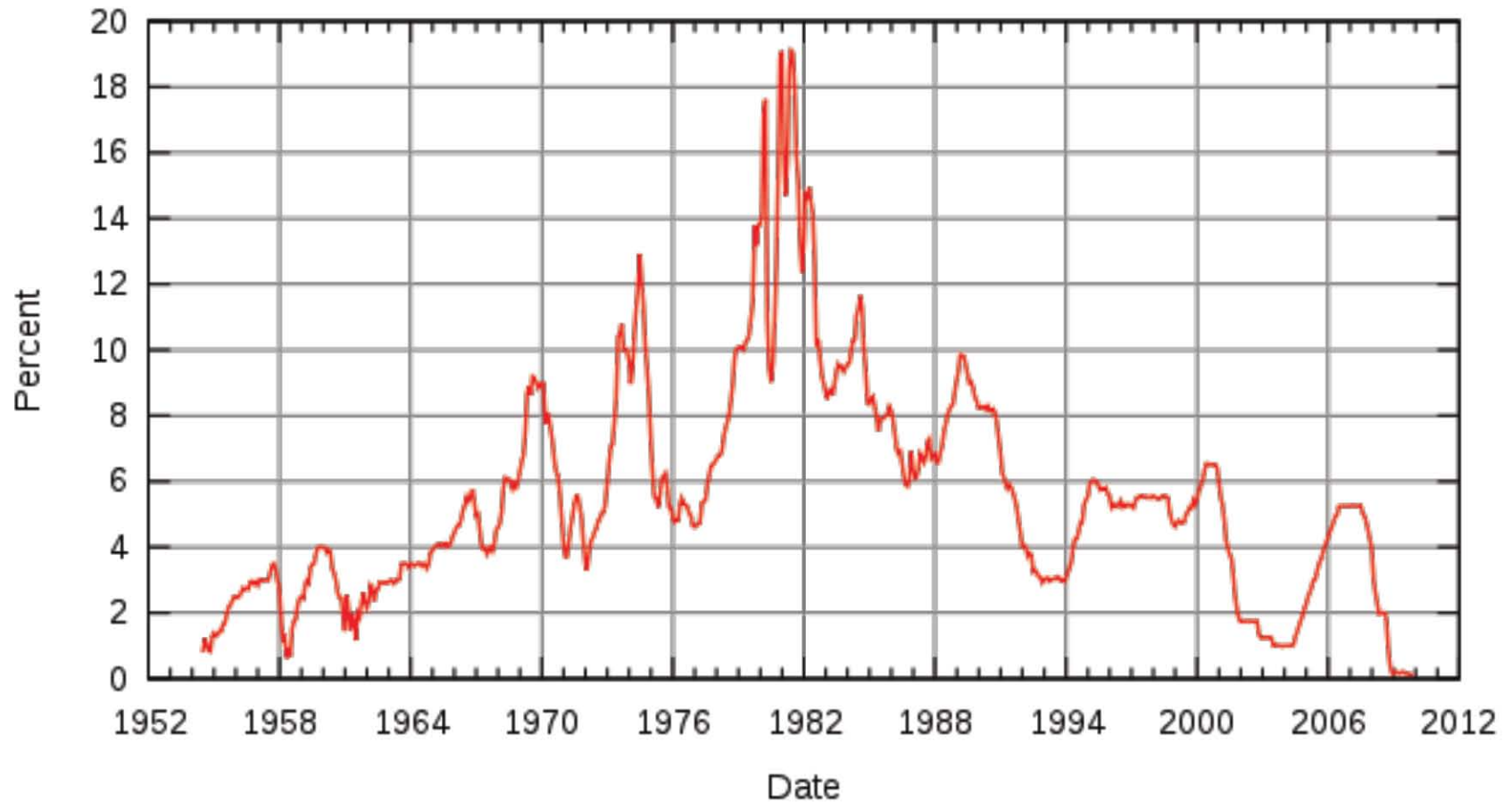
Last Revised on: September 29, 2011 - Next Release Date October 27, 2011



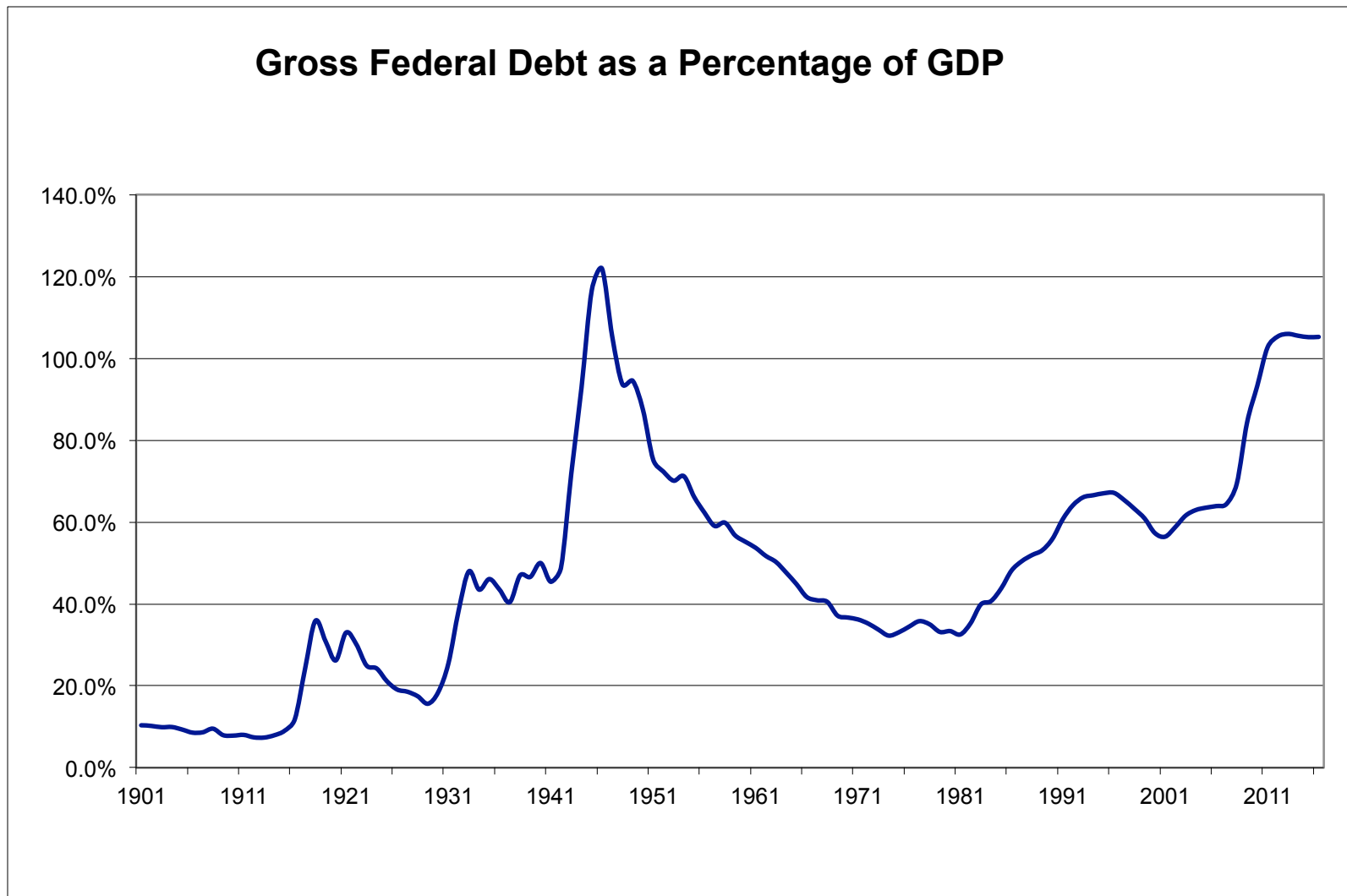
Source: U.S. Bureau of Economic Analysis

National Economic Outlook

Federal Funds Rate (effective)
July 1954 to December 2009



National Economic Outlook



National Economic Outlook

4 possible scenarios for how the crisis may work out

- 1) Everything will work out OK – the economy will recover and grow faster than the accumulation of federal debt
 - Congress will reduce spending and/or increase to bring the debt under control AND the economy will recover and resume normal growth/investment
- 2) Congress will default on the debt driving up interest rates
- 3) Nothing will change and we will devalue the currency through inflation (high interest rates and inflation *ala* 1982)
- 4) Nothing will change and we will accumulate debt and lapse into permanent economic stagnation, like Japan

The economic crisis **WILL** affect elections and money available for critical infrastructure

Why does this Matter to You?

- Government money has dried up for the foreseeable future
 - Federal government spending (deficit) is maxed out
 - State & local government spending (balanced budgets) will decline with: (1) loss of federal government money; (2) decline in property tax revenues; and, (3) continued economic malaise
- Instability of financial markets may make borrowing and access to capital for infrastructure very difficult/expensive
- Long term instability of financial markets may adversely impact personnel and operating costs
 - Operating costs (e.g., wages, materials)
 - Pension funding

Pipeline Safety

The three curses:

- May you live in interesting times
- May you come to attention of higher authority
- May *all* of your dreams come true
- **We're here from the government to help**
- Participants should develop an economic outlook and a business strategy to deal with that outlook