KCC's Efforts at Achieving Regionally Competitive Rates

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Kansas Corporation Commission

KCC's Efforts to Achieve Regionally Competitive Rates

Outline of Presentation:

1. KCC's 2018 Rate Study
2. Kansas Legislative Coordinating Council 2020 Rate Study
3. Regulatory Compact and Legal Standards
4. KCC's Efforts to Monitor and Achieve Regionally Competitive Rates

KCC’s 2018 Rate Study

- In order to address rate concerns expressed primarily by KIC, Staff and parties to Westar and KCP&L’s merger included a condition to the non-unanimous settlement agreement that required KCC Staff and Evergy to conduct a rate study.
- The study period was from 2008 to 2017.
- Staff’s Rate Study determined that Westar and KCP&L’s rate increases during the study period were generally due to the cumulative effect of prior capital investments during a period of declining volumetric sales.
- The capital investments were driven by the following factors:
  1. Environmental regulations requiring the retrofitting of existing coal-fired generating units with pollution control equipment.
  2. New fossil-fuel generation facilities (Emporia Energy Center and Iatan 2).
  3. New renewable generation facilities.
  4. Transmission system investments to replace aging assets and to relieve congestion caused by new renewable generation facilities.

KCC's 2018 Rate Study (Cont.)

- Other issues affecting Westar and KCP&L's rates:
  1. Both KCP&L and Westar had declining sales with Westar's decline primarily due to a loss of industrial sales.
  2. KCP&L experienced an increase in coal costs and a significant loss of revenue from wholesale energy sales that are credited to its fuel clause.
  3. Natural gas costs declined enabling utilities with a high percentage of natural gas-fired generation to achieve low-rates. Another rate advantage for these utilities was the avoidance of capital investments in environmental retrofits.

Kansas Legislative Coordinating Council Rate Study

Overview:

- Sub. for SB 69 (SB 69) directed the Legislative Coordinating Council to authorize a study of Kansas electric public utilities.
- The purpose and scope of SB 69 was defined as:

The bill specifies the purpose of the study is to provide information that may assist future legislative and regulatory efforts in developing electric policy that includes regionally competitive rates and reliable electric service. The utilities subject to the study include electric public utilities, as defined in Chapter 66 of the *Kansas Statutes Annotated*; electric cooperative public utilities exempt from Kansas Corporation Commission (KCC) jurisdiction; and the three largest municipally owned or operated electric utilities by customer count. [Summary of Legislation].

Kansas Legislative Coordinating Council Rate Study (Cont.)

Overview continued:

- SB 69 included a large number of issues to be studied and was separated into two parts.
    1. The first part covered the effectiveness of current Kansas ratemaking practices and options available to the KCC and the Kansas Legislature to affect electricity prices and become regionally competitive *while providing the best practical combination of price, quality, and service*. The study was conducted by London Economics International (LEI).
    2. The second part covered other consequential energy issues materially affecting Kansas electric rates. This study was conducted by AECOM.

LEI Rate Study Recommendations

LEI recommended four near-term steps targeted at achieving regionally competitive electric rate over time.

1. Establish a State Energy plan.
2. Mandate integrated resource plans from utilities with a competitive procurement framework.
3. Allow the KCC to explore the development of initial Performance Based Regulatory (PBR) mechanisms.
4. Establish a framework allowing for the securitization of uneconomic assets.

Staff's Response to LEI Rate Study Recommendations

Recent testimony before this Committee on SB 88 made assertions regarding the KCC's inaction on SB 69's recommendation regarding regionally competitive rates. Specifically, the following was stated:

<u>No action on regionally competitive rates</u>. In 2018 the Senate passed SCR 1612 which called on the KCC to take all lawful action to bring regionally competitive rates to Kansas or tell the Legislature what tools it needs.

- *In 2019, SB 69 (rate study bill) was intended "to help craft forward-looking electric policy that leads to regionally competitive electric rates and reliable electric service." The KCC has never acted on either of these legislative directives.* [KIC/KLER Testimony, February 13, 2023]. [Emphasis added].

The following slides will address the KCC's efforts and participation in addressing the SB 69 rate study.

Staff's Response to LEI Rate Study Recommendations (Cont.)

1. Establish a State Energy plan.
   - Staff's response to the LEI rate study in a Senate Utilities presentation stated the following:

     Staff is supportive of a State Energy Plan. Staff would note that state energy plans can be challenging and time consuming to develop due to the number of stakeholders involved. This can make it difficult to keep the energy plan current in what is now a rapidly changing and dynamic utility environment. This is possibly illustrated in Figure 103, which is a summary of regional states' energy plans. The year published ranges from 2008 to 2016, with the majority being published prior to 2015. [Staff Response to London Economics Rate Study, Senate Utilities Committee, February 6, 2020, Slide 9].

- Because of the scope of a State Energy Plan and the number of stakeholders involved, the directive to develop such a plan generally comes from either a legislative directive or from the Governor.

Staff's Response to LEI Rate Study Recommendations (Cont.)

2. Mandate integrated resource plans (IRP) from utilities with a competitive procurement framework.
   - An IRP framework was jointly recommended by Westar, KCP&L, Staff, and CURB in Docket No 19-KCPE-096-CPL.
   - The Capital Plan and IRP framework was vetted by a large number of stakeholders and the first Capital and IRP filings were submitted by Evergy in 2021. The Capital Plan and IRP filings are on filed on an annual basis and the 2022 Capital Plan and IRP were reviewed last year. The 2023 filings are underway.
   - Both the Capital Plan and IRP processes continue to evolve based on stakeholder feedback and Evergy's IRP will now include third-party solicitations via an RFP process in order to evaluate purchase power agreement versus ownership for new generation assets.

Staff's Response to LEI Rate Study Recommendations (Cont.)

3. Allow the KCC to explore the development of initial Performance Based Regulatory (PBR) mechanisms.
   - LEI's report at Section 1.5.2 on page 16 notes that "…there is not 'one size fits all' PBR formula." and that "…[A] PBR design needs to be customized to the specific environment and circumstances of the regulated utilities. The regulator needs to take each utility's unique characteristics, type of customers served, and underlying economic environment into account, together with state energy policies."
   - Staff has been conducting a thorough review of PBR mechanisms across the country in order to evaluate and make any recommendations regarding implementing new PBR mechanism(s) in Kansas. Staff is currently finalizing its work and will have a final report later this year.
   - Staff also notes that we have used or are using PBR mechanisms for discrete issues and that Southern Pioneer's rates are set using a PBR mechanism.

Staff's Response to LEI Rate Study Recommendations (Cont.)

4. Establish a framework allowing for the securitization of uneconomic assets.
   - Staff worked with stakeholders to pass Senate Sub. For HB 2072 during the 2021 Session. The securitization bill allowed certain generating facilities and extraordinary costs to be securitized.
   - Other Issues:
     - There are a number of other issues contained in the LEI report that have been addressed. For example LEI recommended economic development initiatives. During the 2020 Session, Senate Sub. For House Bill 2585 was passed which authorizes the KCC to approve special contracts that are not based on an electric utilities cost of service and to approve economic development rates that are discounted.
     - Another issue that has been addressed are the tax rates paid by Kansas Utilities. Senate Sub. For House Bill 2585 also exempted electric and natural gas utilities from Kansas income taxes. The bill also requires utilities to track changes in state and federal income tax rates and defer any over collection or under collection.

Legal Standards Impacting the KCC's Efforts to Achieve Regionally Competitive Rates

As noted previously, recent testimony before this Committee on SB 88 made assertions regarding the KCC's inaction on regionally competitive rates. Specifically, the following was stated:

No action on regionally competitive rates. *In 2018 the Senate passed SCR 1612 which called on the KCC to take all lawful action to bring regionally competitive rates to Kansas or tell the Legislature what tools it needs*.

> ○ In 2019, SB 69 (rate study bill) was intended "to help craft forward-looking electric policy that leads to regionally competitive electric rates and reliable electric service." The KCC has never acted on either of these legislative directives. [KIC/KLER Testimony, February 13, 2023]. [Emphasis added].

The following slides will address the legal standards that limit the KCC's authority to simply reduce rates to regionally competitive levels.

Regulatory Compact

The regulatory compact is an agreement codified by statute and case law that is unique to the utility space and calls for:

1. the utility to provide safe, reliable and reasonably priced service;
2. the commission to provide the utility with a reasonable opportunity to recover its costs and earn a return similar to that of other investments that have similar risk characteristics;
3. the customer to pay the approved rates; and,
4. the investor to supply the capital necessary to maintain or expand the utility system.

Source: RRA Regulatory Focus, The rate case process: a conduit to enlightenment, p.1. (July 3, 2018).

Legal Standards

1. K.S.A. 66-101b—Requires Efficient and Sufficient Service at Just and Reasonable Rates.
2. Just and Reasonable Rates have been interpreted by the Kansas Supreme Court as:

…a rate fixed within the "zone of reasonableness" after the application of a balancing test in which the interests of all concerned parties are considered. In rate-making cases, the parties whose interests must be considered and balanced are these: (1) the utility's investors vs. the ratepayers; (2) the present ratepayers vs. the future ratepayers; and (3) the public interest.

Kan. Gas and Electric Co. v. State Corp Comm'n, 239 Kan. 483, 488 (1986).

Legal Standards (Cont.)

1. The KCC is required to balance the public need for adequate, efficient, and reasonable service with the public utility's need for sufficient revenue to meet the cost of furnishing service and to earn a reasonable profit. Danisco Ingredients USA, Inc. v. Kansas City Power & Light Co., 267 Kan. 760, 773 (1999).

2. There is a also Constitutional basis behind the “Just and Reasonable” Standard. The Fifth Amendment provides that, “No person shall…be deprived of…property, without due process of law; nor shall private property be taken for public uses without just compensation.” The Fourteenth Amendment provides that “No State…shall deprive any person of…property, without due process of law…” Leonard Saul Goodman, The Process of Ratemaking, p. 132. (Public Utility Reports, Inc., 1998).

Legal Standards (Cont.)

Based on the legal standards outlined above, any adjustment based solely on lowering rates to achieve regionally competitive rates would most likely be illegal because:

- In setting cost-based rates, the Commission must have factual evidence that supports any adjustment to reduce the cost to serve a utility's customers.
- The adjustment would most likely violate the Fifth and Fourteenth Amendments discussed above.
- The adjustment would also not meet the balancing of interests outlined by the Kansas Supreme Court, which would result in rates that are unjust and unreasonable.

KCC's Efforts to Monitor and Achieve Regionally Competitive Rates

Stakeholder testimony on SB 88 has also made the following assertions:

- "Kansas continues to experience the highest electricity cost in the region for residential, commercial and industrial customers. This uncompetitive position on such an important input for ratepayers has caused our members to voice strong concerns over the relationship between the regulatory agency responsible for oversight of our state's investor-owned utility and **lack of concern** over the impact their decisions have had on ratepayers in our state." [Kansas Chamber Testimony, February 13, 2023]. [Emphasis added].
- "The current commission has shown almost **no interest in respecting concerns from the ratepayers, or the Legislature which has directed the commission to look for policies to move Kansas toward regionally competitive electric rates**." [Kansas Chamber Testimony, February 13, 2023]. [Emphasis added].
- The following slides will address how the KCC is monitoring and seeking to achieve regionally competitive rates.

KCC's Efforts to Monitor and Achieve Regionally Competitive Rates (Cont.)

- Elements of the criticism leveled at the KCC is a lack of policy promulgated by the KCC.
- Policy is primarily promulgated by the legislature.
- The KCC has the authority to define or determine policy when it is within the existing statutory authority of the Commission.
- KIC/KLER has criticized the KCC for not proposing the legislative recommendations contained in the LEI study, despite the fact that it has taken the lead in proposing legislation to address the LEI recommendations as well as other legislation to address regionally competitive rates at a rapid pace.
- The KCC has proposed legislative changes to the transmission delivery charge via HB 2225 this session.

KCC's Efforts to Monitor and Achieve Regionally Competitive Rates (Cont.)

- Both the Commission and Staff take positions in docketed matters that seek to promote and achieve regionally competitive rates, regardless of whether there is an explicit statement regarding regionally competitive rates.
- The following dockets are examples of the KCC's efforts:
  1. <u>Docket No. 16-KCPE-593-ACQ – In the Matter of the Joint Application of Great Plains Energy Incorporated, Kansas City Power & Light Company, and Westar Energy, Inc. for Approval of the Acquisition of Westar Energy, Inc. by Great Plains Incorporated</u>: GPE does not dispute that they will incur a large amount of debt to acquire Westar. Nor does it dispute it has no written plan to deleverage. The Joint Application is deficient. It does not include plans showing which generation plants will be retired early. *There are no examples of reduced spending through procurement savings and no evidence that customers will see any savings. The Joint Application simply does not give the Commission any assurances that it will be able to service the newly-incurred debt without raising rates or reducing services. Therefore, the Commission has no choice but to find the proposed transaction is not in the public interest.* Accordingly, the Commission denies GPE's application to acquire Westar. [Emphasis added].

KCC's Efforts to Monitor and Achieve Regionally Competitive Rates (Cont.)

Continued:

2. <u>Docket No. 19-WSEE-355-TAR – Order on Westar's Application to Recover Certain Costs Through its R.E.C.A Related to the 8% Portion of Jeffrey Energy Center:</u> "Customers do not benefit by paying for capacity and/or energy they are not reasonably expected to need. Westar was aware that the 8% portion of JEC was not necessary for it to meet its capacity requirements when it entered into its new lease and purchase agreement. *Therefore, the Commission finds Westar has not demonstrated that it would be prudent for customers to bear the new costs associated with the new lease and purchase of the 8% interest.* [Emphasis added].

KCC's Efforts to Monitor and Achieve Regionally Competitive Rates (Cont.)

Continued:

3. Docket No. 21-EKME-088-GIE – Order In the Matter of the Investigation into the Sustainability Transformation Plan of Evergy Metro, Inc, Evergy Kansas Central, Inc. and Evergy South Inc. (collectively Evergy): The Reporting requirements recommended in Staff Comments on STP and Topics Addressed During Commission Workshops are adopted. *Evergy is directed to quarterly report its Board and senior management level Key Performance Indicators in a compliance docket and annually provide a more comprehensive report tracking the granular execution level KPI to allow the Commission to evaluate whether Evergy is executing its STP successfully, and making progress towards regionally competitive rates and reliable electric service.*

KCC's Efforts to Monitor and Achieve Regionally Competitive Rates (Cont.)

3. Docket No. 21-EKME-088-GIE continued:

Thus, the Commission clarifies it is not making any decisions on the merits of the programs within the STP or the prudence of associated investments. Those decisions are reserved for Evergy's future rate cases. As CURB articulated, this Docket is investigatory in nature, rather than ratemaking. *The investigation was necessary to give the Commission and stakeholders insight into the motivations and impacts of Evergy's STP; however, this proceeding has not created a sufficient evidentiary record to make granular determinations on the merits of Evergy's STP. The Commission finds its traditional ratemaking approach affording management discretion to the utility - with an after the fact prudence and cost-recovery review - will be the most protective for consumers in this situation.* As CURB suggests, it is appropriate for the Commission to offer some general guidelines before Evergy files its next rate case. While not making any predetermination on the merits of the STP or its costs, before seeing actual capital expenditure commitments, the Commission has some concerns with the STP in its present form. [Emphasis added].

KCC's Efforts to Monitor and Achieve Regionally Competitive Rates (Cont.)

3. Docket No. 21-EKME-088-GIE continued:
First, it is important for Evergy and other Kansas utilities to achieve and maintain regionally competitive retail rates, and it is unclear at this time whether the STP improves or worsens the trajectory of rates. Evergy claims that the average annual increase in rates in its combined Kansas service territories from 2017 through the end of the STP in 2024, will increase on average less than 1 % (0.9%) a year, or less than half the average rate of inflation over the same timeframe, which is projected to average 2.15% annually. The Commission appreciates the STP's stated objective of keeping rate increases at or below inflation. However, in an era of rising inflation, prevailing rates of inflation may not be an acceptable benchmark for retail rate increases. Further, Evergy's projections of lower than inflation rate increases are merely that - projections. *Actual rate impacts will be highly dependent on Evergy's commitment and execution over the next several years. The Commission will review the success of Evergy's execution in future rate cases*. [Emphasis added].

KCC's Efforts to Monitor and Achieve Regionally Competitive Rates (Cont.)

Continued:

4. Docket No. 22-EKME-254-TAR – In the Matter of the Application of Evergy Metro, Inc., Evergy Kansas South, Inc. and Evergy Kansas Central, Inc. for Approval of its Demand-Side Management Portfolio Pursuant to the Kansas Energy Efficiency Investment Act ("KEEIA"), K.S.A. 66-1283. Testimony in Opposition to Non-Unanimous Settlement Agreement, Justin Grady: "…Given the flaws inherent in the TD [Throughput Disincentive] mechanism included in the settlement, and the excessive levels of EO [Earnings Opportunity] in the Settlement, *Staff contends that the TD and EO mechanisms that are part of the Settlement would not contribute to the creation of just and reasonable rates…"* [Emphasis added].

KCC's Efforts to Monitor and Achieve Regionally Competitive Rates (Cont.)

Conclusion:

- Despite assertions to the contrary, the KCC is focused on closely monitoring Evergy and working with Evergy and its stakeholders to achieve regionally competitive rates.
- However, achieving regionally competitive rates will take a longer-term view. As LEI stated in its study, "Ultimately, there is no single easy fix that would reduce electricity rates. Kansas needs to adopt a portfolio approach that would gradually achieve regionally competitive rates over time." [LEI Rate Study at p. 257].
- Moreover, efforts to achieve regionally competitive rates cannot be so austere that reliability and quality of service are negatively impacted due to postponed capital investments and maintenance.

Questions?

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Kansas Corporation Commission