Kansas
Citizens' Utility Ratepayer Board

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House Committee on Energy, Utilities and Telecommunications
Testimony of Citizens' Utility Ratepayer Board
Opposing Written and Oral Testimony
House Bill 2527
February 6, 2024

Chairman Delperdang and members of the House Committee on Energy, Utilities and Telecommunications, thank you for this opportunity to testify regarding House Bill (HB) 2527. My name is David Nickel. I am the Consumer Counsel for the Citizens' Utility Ratepayer Board (CURB). CURB is the advocate for residential and small commercial ratepayers before the Kansas Corporation Commission (KCC or Commission) and the Kansas Legislature. My testimony principally reflects how CURB's constituents would be negatively affected by HB 2527.

HB 2527 makes several amendments to Kansas statutes and KCC practices regarding utility rate regulation for Kansas utilities, as defined by K.S.A. 66-104. Chief among these is that HB 2527 requires the KCC to utilize the test year capital structure of a "large public utility" (a utility serving at least 20,000 retail customers), without reference to the capital structures or investments of entities affiliated with the large public utility, if the large public utility's parent holds an investment-grade credit rating from one or more nationally-recognized credit rating agency. In addition, HB 2527 allows a large public utility to elect to base its rate of return on equity (ROE) upon the fully-litigated case 12-month average from the most recent report issued in the regulatory research association regulatory focus publication (or successor publication) for the applicable utility type, but excluding observed rates of return for certain types of utilities cases.

Additionally, HB 2527 alters the discounts that may be approved by the KCC under economic development rate schedules which provide discounts from otherwise applicable standard rates for electric service for new or expanded facilities of certain industrial or commercial customers. It eliminates tracking mechanisms associated with reductions in revenues associated with such discounted rates as well as the requirement that the revenue reductions be deferred to a regulatory asset and rate treatment of the same.

With respect to certain rate-making predeterminations under K.S.A. 66-1239, HB 2527 changes the regulatory filings required for the pertinent utility applications. With respect to a new gas-fired generating facility, the public utility may implement new rate adjustment mechanisms designed to recover the return on 100% of amounts recorded to construction work in progress on the public utility's books, unless the KCC has determined the stake acquired by the utility to be unreasonable.

It is important to note that the majority of these amendments to Kansas utility regulatory practices are intended to insulate utility shareholder profits. Essentially, several of the amendments take authority and judgment away from the KCC, which has been entrusted by Kansas statutes to carefully weigh the evidence before it in utility cases and to balance the interests of the parties. It has been so entrusted for over 100 years, under Kansas statutes that were first enacted in 1911.

Although no agency ever operates perfectly, the KCC has performed well in balancing the interests of ratepayers and utility shareholders. There are no credible allegations otherwise. Therefore, in CURB's view, it would be unwarranted to take away the KCC's authority to balance shareholder rights against ratepayer burdens under current law.

CURB is troubled by many aspects of HB 2527, including Section 3 of the bill which increases utility service discounts for purposes of economic development. We question the need for these increased discounts, noting that Evergy has stated that its rates are not hindering economic development. However, CURB is willing to meet with Evergy and other stakeholders to discuss how, if at all, Section 3 will benefit residential and small commercial ratepayers. Similarly, CURB is willing to meet with Evergy and other stakeholders to discuss how, if at all, Section 4 of HB 2527 is in the interest of Kansas ratepayers. CURB is hopeful that other stakeholders will collectively address problematic aspects in Sections 3 and 4 of HB 2527 for the Committee's benefit.

Nonetheless, in the interest of brevity, CURB will highlight only problems associated with Section 2 of HB 2527. In particular, CURB is opposed to the bill's provisions concerning a large public utility's ROE. In CURB's view, the changes made by HB 2527 to the manner in which a large public utility's ROE is determined in Kansas is unnecessary and unwise. HB 2527 allows the ROEs of large public utilities to be determined in a manner that would unduly harm Kansas residential and small commercial ratepayers.

Under well-established law, including Kansas Supreme Court precedent, the ROE to be authorized by a utility commission must meet the following objectives: It should be commensurate with returns on investments in other enterprises having corresponding risks. It should also be sufficient to assure confidence in the financial integrity of the utility, so as to maintain its credit and to attract capital. Finally, the ROE must change over time as the money market and business conditions change. As to that last criterion, the ROE must correspond to the money market and business conditions existing and pertinent to the subject utility when the ROE is established.

Those objectives are met by applying various finance methodologies, such as a discounted cash flow analysis and a capital asset pricing model analysis, to a set of utilities that are similar to the utility seeking the rate of return. This set of utilities is called a proxy group. Careful analysis of the proxy group is necessary to ensure that this group has comparable risks to that of the subject utility. Indeed, it is imperative that the return should be as specific as possible to the utility in question.

The utilities and stakeholders, including CURB, have performed this very analysis and submitted their analyses in rate cases for decades. In addition to the evidence submitted by these parties in rate cases, the KCC staff has performed its own analysis to form a recommendation for the KCC to consider in deciding the lawful and reasonable ROE to be authorized for Kansas utilities. Simply put, this regulatory framework has functioned well over time. Thus, over the decades, Kansas utilities have maintained financial integrity so as to maintain their credit and ability to attract capital. The relative stability of each Kansas utility's capital structure is some evidence that the *status quo* is workable.

It is also important to note that the KCC's decision on a utility's authorized ROE must meet two additional conditions: It must be based upon substantial and competent evidence in consideration of the record evidence as a whole, which is a test of the reasonableness of the decision. It must also be lawful, that is, it must be in accord with the U.S. and Kansas constitutions and Kansas statutes, as well as the interpretations of those principles by the U.S. and Kansas appellate courts. If the KCC falls short on either of these two necessary elements, Kansas statutes provide appellate court relief to aggrieved parties which would include the subject utilities in rate cases. In short, in order for any ROE authorized by the KCC to be upheld by Kansas appellate courts, there must be substantial and competent evidence that the authorized ROE allows the subject utility to maintain its financial integrity so as to maintain its credit and to attract capital. If the KCC fails, the KCC's decision is set aside by the courts as unreasonable, unlawful or both.

As the Committee may be aware, CURB's evidence in rate cases generally calls for authorization of a low but reasonable ROE for the utility in KCC rate cases. Meanwhile, in CURB's view, the utility's evidence in rate cases generally calls for authorization of a high and unreasonable ROE. The KCC staff typically provides testimony that suggests an authorized ROE in between the utility's suggested ROE and CURB's. In most cases, the parties are able to agree on an authorized ROE that is satisfactory towards their interests, generally between what the KCC staff recommends and what the utility recommends. If any party thinks that the ROE set forth in a settlement agreement is unlawful or unreasonable, they can require the KCC to have a hearing on the issue and, if they don't prevail at the hearing, they can appeal to the courts. For reference, the most recent Evergy rate case led to a *fully unanimous* settlement agreement, which the KCC approved in its entirety. In short, the *status quo* provides a means by which an ROE is fairly determined.

Thus, it should be clear that the current regulatory framework for determination of an authorized ROE is reasonable, lawful and stable. Kansas has utilized that regulatory framework for decades, providing evidence that all reasonable stakeholders are comfortable with the process. Clearly, the manner in which ROEs are determined in rate cases in Kansas accords with applicable law and has sufficient safeguards to protect both the utility and ratepayers.

Therefore, there is no compelling reason to change it now, and certainly not in the manner suggested by HB 2527. First, formulating an ROE from the fully litigated case 12-month average from the most recent report issued in the regulatory research association regulatory focus publication removes ROE from a strenuous comparative analysis of other utilities having corresponding risks to the subject utilities. As noted earlier, careful analysis of that proxy group is necessary to ensure that the group has comparable risks to that of the subject utility. HB 2527 would not permit stakeholders and the KCC to perform such analysis if the utility chooses to base its ROE on the 12-month average. Secondly, there is no way to determine how many fully-litigated cases there will be, and the circumstances that may have affected the fully-litigated case 12-month average. At the very least, a small sample size with outlier economic conditions could yield an absurd result. In the extreme, if all relevant utilities were to adopt the proposed methodology, there would be no average basis. Third, allowing a monopoly to choose its own ROE is terrible public policy. It completely eliminates rate regulation which is the basis for allowing utilities to have a monopoly in their service territories. Finally, it removes local considerations and local governance from the utility regulatory framework. The Governor appoints and the Senate confirms Kansans

to be our utility commissioners. It would simply be ridiculous to confirm commissioners from other states to regulate Kansas utility rates. Yet that is exactly the effect of HB 2527.

CURB opposes HB 2527 since it entails a significant, unwarranted and outrageous change to the utility regulation paradigm in Kansas that has worked to set rates in a lawful manner for over a century. Further, CURB would join in the testimony posited by other conferees that are opposed to other aspects of the house bill. Finally, as indicated CURB would welcome a frank discussion with utilities, KCC staff and other stakeholders regarding reasonable improvements that can be made to the regulatory framework in Kansas, including discussion of Sections 3 and 4 of HB 2527. Thank you for considering CURB's thoughts on HB 2527.