CURB: THE CITIZENS' UTILITY RATEPAYER BOARD OF THE STATE OF KANSAS

CURBside News

NEWS FROM THE WATCHDOG FOR RESIDENTIAL AND SMALL COMMERCIAL CONSUMERS OF UTILITIES AUG. 2014

Partial settlement on Atmos rate case; contested issues tried

CURB, the KCC Staff and Atmos Energy have reached a partial settlement agreement in the company's rate case. The remaining contested issues were the subject of a two-day evidentiary hearing before the Commission that began July 1.

The settlement established a unique sliding-scale set of options for the Commission to determine the revenue requirement. Depending on the return on equity (ROE, or shareholder profit) allowed by the Commission, the revenue requirement will be from $3.3 million to $6.3 million. The recommended ROEs ranged from the low 8.5% recommended by CURB to the 9% recommended by Staff, to the high of 10.53% requested by Atmos. Actual rate expenses of the hearing will be added to the amount approved by the Commission.

The settlement also established a capital structure of 47% debt and 53% equity and a more equitable ratio of volumetric charges to facilities charges for residential customers. Other issues relating to post-retirement benefits and pension costs, ad valorem tax expense, and class cost of service were resolved through the agreement.

There were two strongly-contested issues that could not be resolved among the parties. The wide difference between CURB's and Staff's ROE recommendations and that of the company foreclosed the possibility of settlement. Additionally, the company's proposal for a regulatory asset (RA) mechanism for system integrity replacements was strongly opposed by CURB. Staff proposed a set of modifications for the RA proposal that the company strongly opposed. So these issues were tried before the Commission.

The RA mechanism was ostensibly proposed to allow the company to preserve its claims for costs of infrastructure replacements made between rate cases. However, while one purpose of the RA is to reduce the effect of regulatory lag, another is to include the cost of taxes that the company currently doesn't pay. Both features of the RA favor shareholders over ratepayers.

The company's testimony also revealed that Atmos doles out discretionary funds to its several utility divisions based on which ones have succeeded in securing the most shareholder-friendly policies from regulators and legislators. Witnesses for Atmos argued that most other states in which the company operates utilities offer more shareholder-friendly policies than Kansas, which leads the company's leadership to allocate fewer discretionary dollars to Kansas for infrastructure replacements. Thus, although the RA is purportedly intended to enable more safety replacements and provide Atmos a guarantee that it would recover costs between rate cases, the RA was intended primarily to please the corporate heads of Atmos in providing another perk for shareholders—a perk that would incidentally enable the Kansas division of Atmos to compete with the other utility divisions in the intra-company competition for discretionary funds.

So apparently, approving the RA would increase the odds that Kansas would receive more of those discretionary dollars. But the company offered no guarantees to Kansas ratepayers in exchange for the guaranteed returns on their investments, and no guarantees that the risk

of explosions due to aging corroding pipes would be reduced if the RA was approved.

CURB argued that the RA offered no tangible benefits to customers, and that it also attempted to provide Atmos a way to get around the annual recovery limitations of the Gas Safety and Reliability Surcharge (GSRS). Staff offered a modification that would have limited Atmos' recovery of costs through the RA to a similar level allowed under the GSRS, but CURB noted that no testimony established the level of expenditures needed to maintain an acceptable level of risk.

Regarding setting the level of shareholder profits, CURB and Staff made similar recommendations on the ROE. CURB's witness, Dr. Randy Woolridge, recommended an ROE of 8.5%, and Adam Gatewood, the Staff witness, recommended 9.0%. Both witnesses utilized similar analyses, and Gatewood admitted that the academic research of Dr. Woolridge, who is an economics professor at Pennsylvania State University, had influenced his current method of determining an appropriate return. Dr. William Avera, the witness for Atmos, advocated an analysis that differed significantly from that of CURB's and Staff's witnesses in making his 10.53% recommendation.

Post-hearing briefs have been filed, and Atmos is due to file its reply brief on August 4.

KCC Docket No. 14-ATMG-320-RTS

Black Hills files first Kansas rate case

Black Hills Energy, the South Dakota-based utility that purchased Aquila's natural gas distribution system in Kansas in 2008, has filed its first rate increase application with the Commission. Black Hills serves about 110,000 customers in Kansas, including the cities of Lawrence, Garden City, Goodland and parts of Wichita.

The $7.3 million increase requested includes $2.2 million in property tax that has been previously approved by the KCC for inclusion in rates in this case, and $2.2 million already being paid by customers in the Gas Safety and Reliability (GSRS) surcharge that will be moved out of the surcharge into base rates.

The company is seeking a return on equity (shareholder profit, or ROE) of 10.6%, based on a capital structure of 50.34% equity and 49.66% debt.

The company is seeking a pension and post-retirement benefits tracker, a mechanism that most other regulated utilities in Kansas already have. This will ensure that customers only pay for contributions to pensions and other retirement benefits that the company actually makes.

The company is also seeking two new riders and an accounting order mechanism. The accounting order mechanism would allow the company to preserve its claims for expenditures on a work force development program that will train new workers in anticipation of the large number of employee retirements that Black Hills expects in the next few years. One of the riders is designed to recover the costs of five identified safety-related projects, and the other is intended to credit ratepayers with the revenues from several former Anadarko customers who have the capability of bypassing the Black Hills system.

If its application is approved, Black Hills estimates that the average residential customer's monthly bill will increase about $4.17, and the customer charge will increase from $16.00/mo. to $21.70/mo. The per therm commodity charge will decrease from $.14524 to $.14355.

Commercial customers will see the same decrease in the commodity charge as residential customers, but their customer charges will increase from $22.75/mo. to $36.00/mo.

A public hearing on the rate increase was held in Lawrence on July 10, with video-conferencing to locations in Wichita, Garden City and Goodland. The evidentiary hearing will begin on October 27 at the Commission's offices in Topeka.

CURB has begun its analysis of Black Hills's application. While the analysis is not yet complete, we can see already that the 10.6% return on equity that the company is seeking for its shareholders is way too high in today's economy. By comparison, in Atmos Energy's current rate case, the recommended ROEs range from 8.5% (CURB) to 9% (KCC Staff) to

10.53% (Atmos). The evidence certainly doesn't support ROEs over 10% for natural gas utilities, which generally require a lower ROE than electric utilities. With KCPL's ROE at 9.5%, it's highly unlikely that Black Hills's request for a 10.6% ROE will be approved.

Black Hills, like Atmos, has also requested a rider to provide special recovery of expenditures on safety-related projects, even though the Commission rejected a similar request of KGS in 2012. The natural gas utilities seem to have banded together nationwide to take advantage of the concerns over several high-profile natural gas explosions to seek reduced lag for safety-related replacement of aging infrastructure. They seem to be forgetting that one of their fundamental obligations as regulated utilities is to maintain safety, and that meeting this obligation doesn't merit special treatment.

Black Hills has also requested special treatment of costs it will incur in training employees to replace those expected to retire in the coming years. While the company should be commended for thinking ahead and addressing its future work force needs, it's not clear why an accounting order is necessary to accomplish the task. Again, it appears that the company simply wants a special reward for doing something that all well-run companies should be doing.

By the time that CURB files its direct testimony on September 12, we should have more answers to our many questions about Black Hills's application. We'll keep you posted.

KCC Docket No. 14-BHCG-502-RTS

Randy Brown, former CURB member, loses bout with cancer

Randy Brown, a former member of CURB's board, died on July 23 after a two-year bout with cancer.

Brown, of Wichita, was a Pulitzer Prize-winning journalist who worked for the Omaha Sun, the Wichita Eagle, KAKE-TV, and various other news organizations in Nebraska, Texas and Oklahoma before settling in Wichita. He capped his career by serving as a Senior Fellow with the WSU Elliot School of Journalism.

A founder of the Wichita Sun newspaper, Brown was also a perennial emcee and writer for the Gridiron show, an annual musical comedy fundraiser in which local journalists poked fun at politicians and current events to raise scholarship money for journalism students. His sense of humor was legendary. His obituary in the Wichita Eagle recalled his unsuccessful campaign for a seat in the Kansas Legislature. He introduced himself door-to-door by saying, "Madam, I may have lost my mind, but I'm running for the Kansas Legislature." The staff at CURB also enjoyed his sense of humor and keen insight honed by years of observing and writing about state politics.

Appointed to CURB in 2005 by then-Governor Kathleen Sebelius, Brown served as Vice Chair in 2007 and 2008. He was especially helpful to CURB in sorting out open meetings issues, his expertise developed in his longtime service to the Kansas Sunshine Coalition, an organization that promotes transparency in government.

Brown, 73, is survived by his wife Linda Parks, his sons Chris and Chad; a stepdaughter, Keisha Kingdon, two brothers and three grandchildren. Memorials have been established with the Kansas Sunshine Coalition for Open Government c/o Elliott Department of Mass Communications at Wichita State University, 1845 Fairmount, Wichita, KS 67260, and the American Cancer Society, 330 S. Main St. #100, Wichita, KS 67202.

The staff of CURB offers our condolences to his family and the many friends and colleagues who mourn his passing.

Tom Day installed as acting KCC Executive Director

The KCC's Executive Director, Kim Christiansen announced her retirement earlier this summer, after only a year at the Commission. The Kansas Electric Cooperatives recently announced that she has taken a position with the organization as Manager of Public Relations.

In her place, the Commission has appointed Tom Day as the Acting Executive Director. Day, whose position as head of the Docket Room at the KCC has made him well-known to everyone who files documents at the KCC, has also served as the KCC's primary liaison with the legislature for many years.

No search for a permanent replacement has been announced. Because the directoship of the KCC is a patronage job, the governor has the final say in the selection of a candidate to fill the position.

Westar prepay option OK with modifications

Late last year, Westar Energy proposed a new pilot program that would waive deposit requirements for customers in exchange for their agreement to prepay for electric service. This program would be available only to Westar customers whose homes have the new automated electric meters. Currently, only customers in Lawrence and some areas of Wichita have access to these automated meters.

As proposed, Westar Energy customers with automated (so-called "smart") meters can voluntarily opt into the prepay pilot program. If they are current customers with a security deposit on file, the deposit will be applied to any past due amount, or applied to the customer's account as prepayment for electric service.

The prepay program will allow customers to make payments as they choose: in smaller payments at more frequent intervals or in larger payments at less frequent intervals. For example, instead of paying a $125 monthly bill, a customer in the prepay program could pay $20 this week, and $40 next week, or as often as the customer chooses to make payments. So long as they maintain a positive balance, the amount or frequency of payments is up to the customer.

But because there is no such thing as a free lunch, customers who enroll in this program will pay a $4 per month service fee.

Customers will receive text or email alerts, notifying them how much money is left in their electricity account. Think of it like the gas gauge on your car: when the fuel light comes on, the car is warning you it's time to refill the tank. If you don't put more gas in the tank, you run the risk of running out of gas. Westar's alerts will warn customers in a similar manner.

CURB and the KCC Staff originally opposed Westar's proposal for this prepay pilot program. CURB was concerned that the program, as proposed, didn't include enough customer protections. Further, "smart" meters permit remote disconnections and reconnections of service with the push of a button. The prepay program would likely increase the number of times that customers would be disconnected and reconnected, raising our concerns about the possible negative impacts on households that are repeatedly disconnected.

CURB and Staff expressed concerns about the lack of customer protections in their testimony filed with the Commission. In response to CURB and Staff's concerns, Westar agreed to add several customer protections to the program. For example, instead of being eligible to have their electricity disconnected 24 hours after getting text or email alerts, customers now have 72 hours to make a payment to refill the tank.

Because this is a pilot program, there is a lot to learn about how the program will work and (perhaps) won't work. As part of our agreement to recommend that the Commission approve the program, CURB requested stringent reporting and monitoring of the program to ensure that customers in the program have the same level of consumer protection as customers who don't enroll in the prepay program.

CURB also secured a commitment from Westar to exclude customers with excessive past due amounts from the pilot, in order to see if Westar's prediction is correct that many customers who aren't struggling with utility bills will opt for the prepay program. CURB is wary of the prepay option becoming the only path through which customers who can't afford a deposit will be able to obtain service.

The Commission held a hearing on May 1, 2014, at which CURB, Staff and Westar

explained their agreement that Westar's amended prepay program should be approved. The Commission approved the prepay pilot program on May 29. CURB will continue to closely monitor the program's progress.

KCC Docket Nos. 14-WSEE-148-TAR

No hearing in Southern Pioneer rate case

The Commission has cancelled a scheduled hearing in the Southern Pioneer rate case for August 14, and has ruled in favor of the KCC Staff in determining the adjustments that shall be applied to the company's rate request.

Southern Pioneer is the sole non-profit utility in Kansas that is owned by a utility cooperative—a uniquely-positioned utility in which there are no shareholders to please, as in an investor-owned utility, but in which the customers do not own the utility, either, as they would in a coop.

As a result, Southern Pioneer cases tend to be fraught with arguments about whether Southern Pioneer should be treated like an investor-owned utility in KCC proceedings—or like a coop where the consumer protections are fewer because the customers own the utility and presumably have some say in developing the coop's policies.

Southern Pioneer's rates are governed by a "Debt Service Coverage Formula Based Rate Plan", which basically permits the utility to seek rate adjustments based on the amount that it needs to meet its cost of service and service its debt (Debt Service Coverage, or DSC), plus an amount that provides a margin of safety in case revenues decrease or costs increase between rate cases. This margin is a generally a ratio that lenders require the utility to maintain in exchange for access to capital on favorable terms.

The main issue in this filing is related to expenses included in the company's filing. Southern Pioneer included corporate image advertising costs and dues to organizations that lobby for pro-utility policies.

Since Southern Pioneer is not a for-profit corporation, CURB and Staff believe that corporate image advertising is not only inappropriate for recovery in rates, but is completely unnecessary: the utility has no need to attract investors.

The dispute over lobbying costs that are buried in association dues is a perennial issue that arises in many rate cases. There is nothing wrong with utilities joining associations, but if the association dues include the costs of lobbying for legislation or policies that may not be beneficial to ratepayers, the utility's customers should not pay for the costs. Sometimes it's difficult, however, to get information on how much of the association's dues are spent on lobbying. So generally, consumer advocates and many utility commissions advocate across-the-board exclusion of all association dues in the utility's cost of service.

In this case, Southern Pioneer argues that the utility's Consumer Advisory Council, an internal group of customer representatives who ostensibly represent all of the customers' point of view, has approved the expenditures to which CURB and Staff object, and therefore the utility should be allowed to recover them in rates. In response, Staff and CURB have both expressed skepticism that the Council is an adequate substitute for the traditional consumer protections provided by the KCC and CURB.

The company's application requests a decrease in rates of $497,909, based on a DSC ratio of 1.75. CURB recommends a larger decrease, having found $114,157 in expenses that should have been excluded from the filing. Staff recommends an adjustment that would make the decrease about $50,000 larger.

The Commission decided that an evidentiary hearing wouldn't be needed and decided the case on the basis of the parties' filings. It chose Staff's position on advertising and dues as "more reasonable" and "supported by the record".

However, the order provided no guidance for why, given the strong similarity in CURB's and Staff's positions on advertising, association dues and donations, it deemed Staff's position "more reasonable" than CURB's. The order did not identify the "substantial and competent evidence" supporting Staff's position, or discuss what it deemed lacking in CURB's position.

Such failures to articulate the deliberative process in sufficient detail to enable a reviewing court to discern the basis for the agency's reasoning and affirm that the agency considered the record as a whole is an example of why the legislature revised the standard for judicial review of administrative decisions to require agencies to demonstrate in their orders that they considered the whole record, not just the parts that support its decision. Otherwise, it is impossible for a reviewing court to determine whether the agency actually considered all the evidence in the record and actually made a rational decision that is, indeed supported by the evidence in the record.

KCC Docket No. 14-SPEE-507-RTS

Howison Heights troubles continue

We have run through a lot of paper updating customers on the Howison Heights, Inc., water utility and its ongoing troubles. It our last update, we told you that the Commission had approved a $27,266 rate increase for Howison Heights. The Commission also ordered the owner of Howison Heights to make certain improvements to the water system.

CURB and Staff continue to monitor the situation at Howison Heights. Here's a summary of the events that have transpired since the Commission's April 8, 2014, Order.

On June 18, Staff requested an emergency Commission order that required the owner of Howison Heights to hire an industry expert to evaluate and repair the chlorination system. This request was in response to a thirteen-day boil water advisory that was issued by the Kansas Department of Health and Environment on June 5.

The advisory was prompted by an extended power outage in the area that may have shut off power to chlorination systems. A neighboring water district was under the same boil water advisory, but unlike Howison, was able to reestablish water quality quickly; its boil advisory was rescinded within two days. Howison's inability to provide proof of sufficient chlorination of its supply to KDHE led to an extended boil water advisory, and prompted Staff to request emergency intervention.

Then, a customer's inquiry to CURB about whether Howison was correctly charging customers for the new rates led CURB to file a motion asking the Commission to clarify its April 8 order that approved the $27,266 rate increase. The Commission's order approved two things: a rate increase of $27,266 *and* Staff's proposed rate design, which proposed phasing in the rate increase over a two-year period. CURB's motion pointed out that approving Staff's rate design would preclude Howison from charging rates that reflect the full increase in the first year.

The Commission granted CURB's motion to clarify its order, but unfortunately for customers, clarified that it had not intended to approve the two-year phase in of rates. The order effectively approved the rates that Howison started charging in April.

On June 30, the United States Bankruptcy Court in Kansas granted the motion of Howison Heights' creditors to dismiss Howison's bankruptcy application. The dismissal cancels the stays of debt collection actions against Howison, so the foreclosures initiated by two Salina-area banks can now go forward. It is not yet known what will happen to the water system if the banks foreclose on the utility property.

On July 22, 2014, in response to the Commission's emergency order issued in June, Howison filed an inspection report that was completed by a local engineering company. The report highlighted the concerns within the chlorination system and identified ten solutions to resolve the chlorination problems. The Commission Staff has yet to render an opinion on the engineering report.

As we have previously reported, the Howison Heights water utility has been plagued with financial troubles. It's unclear whether the utility can implement any of the chlorination solutions in its current financial condition. CURB will continue to monitor the Howison Heights situation and keep you informed of further developments that may impact its customers.

KCC Docket Nos. 13-HHIW-570-RTS and 13-HHIW-460-GIV

KCC takes comments on developing more access to natural gas in rural Kansas

On May 13, the Commission opened a docket to investigate the development of distribution infrastructure for natural gas in rural Kansas. The KCC Staff is concerned that a recurring problem in rural Kansas is a lack of access to natural gas service, even in areas that are certificated to a regulated natural gas utility.

A number of issues prompted Staff's concerns. Many rural customers in southwest Kansas have historically relied on farm taps for access to unprocessed natural gas, but declining pressures and volumes in the Hugoton gas field have led to withdrawal of service by gathering systems and pipelines. Additionally, the discovery of the presence of dangerous hydrogen sulfide (H2S) gas in unprocessed gas in some areas has led insurers to demand that some providers cease providing unprocessed gas to end users. The withdrawal of access to unprocessed natural gas has hit irrigators the hardest, because irrigation pumps that run on natural gas cannot be economically converted to operate on propane or electricity. Most of them aren't located near existing natural gas distribution lines, either.

Several irrigators have registered complaints with the KCC that natural gas utilities that hold certificates of convenience in their areas are refusing to extend service to them at a reasonable cost. The utilities maintain that extending distribution systems into new areas of rural Kansas is not economic, but they also fiercely protect their service territories and object when other providers step in to with offers to provide service.

Ranchers and farmers who exchanged farm taps for easements through their property to pipeline companies and were guaranteed access to natural gas "so long as it is available" have argued that turning off their taps before the supply is exhausted is a breach of contract. They argue that just because the gas is at lower pressures and is uneconomic to deliver to the tap doesn't make it "unavailable" and they have sought support for their view from the state government.

Some irrigators have even argued that they should be allowed to continue operating their irrigation pumps with unprocessed natural gas from sources where deadly H2S gas has been detected, because the appearance of H2S in the supply is often a temporary and correctible condition, and because the isolated location of the pumps in large areas of uninhabited crop land poses a minimal hazard to people or livestock.

These arguments haven't had much traction with regulators. In recent years, the KCC and the legislature have tightened up safety regulations in areas where unprocessed natural gas is still being used, requiring cautionary signage and public safety measures that will help assure that no one is harmed by unintentional releases of H2S gas.

Pipelines and gathering systems that have shut down the supply of unprocessed gas to farm taps have not been forced to continue providing service, although litigation has been initiated by irrigators who lost their sole natural gas supply. Some irrigators have banded together under the legislature's "self-help" statute and built their own nonprofit natural gas distribution systems, but most irrigators would prefer just to have a reliable supply of natural gas delivered to them, rather than having to spend money on building their own mini-utilities.

However, there are some legitimate reasons for not expanding access to natural gas service. Utilities must consider the possibility of not recovering their costs of extending natural gas service to irrigators who are pumping water from the dwindling Ogallala Aquifer, for example. Just as the Hugoton gas field—once the largest known natural gas deposit in the world—has been depleted to the point where declining pressures and volumes make it uneconomical to pump the remaining gas in many areas of the field, the Ogallala is a huge unrenewable resource that is also becoming depleted. Many areas that have relied on the Ogallala for water are finding that it is no longer economically viable to pump the remaining water, because it is too deep and too tightly locked within the rocks

that form the aquifer. Extending gas service to areas where pumping water from the Ogallala is in danger of becoming uneconomic may be an exercise in futility.

Additionally, other utility customers may ultimately contribute to the costs of extending natural gas distribution lines to irrigators. All ratepayers should be concerned about who would pick up the stranded costs if irrigators run out of water before the cost of extending service to them is recovered by the utility.

These problems have given rise to a number of vexing questions. Do certificated utilities have the right to refuse to serve customers within their service territories—especially if they are actively opposing any other entity from providing service in the same area? Although it's generally assumed that possessing a certificate of convenience for a defined service territory conveys the exclusive right to provide utility service in that area, the Commission has found in previous disputes that the right to serve customers is not necessarily exclusive. It's also not clear to what extent a utility's obligation to serve includes the obligation to serve isolated customers located in areas that don't generate enough customer revenues to justify the expense of expanding the distribution system to the area.

Another question is whether pipelines have an obligation to provide natural gas service to farm taps "for as long as the gas is available" until every last cubic inch of gas has been squeezed from the field. However, the contract disputes between customers with farm taps and their suppliers must be resolved in district courts rather than at the KCC.

While the questions concerning farm tap contracts and whether it is environmentally wise to encourage further drawdowns of the Ogallala are important, the KCC has no jurisdiction to regulate irrigation or contracts. This investigation will be limited to issues that the KCC is authorized to address. The KCC Staff recommended that parties limit their comments to the following issues:

(1) Developing or relinquishing certificated territory held by existing public utilities;

(2) Allowing open competition/multiple certificates of convenience and necessity to entities wishing to distribute natural gas in rural areas;

(3) Providing transparency and objectivity in line extension policies;

(4) The appropriate mechanism for recovery of line extension costs that encourages rural development without cross-subsidization of customer classes;

(5) The use of customer-specific certificates of convenience and necessity and what, if any, obligation to serve exists for the certificated utility to serve future customers; and

(6) The ability to access gas supply from interstate pipelines.

Question (4) is the question of most interest to residential and small commercial ratepayers, who should not be required to subsidize the costs of extensions of service to isolated areas that won't provide sufficient revenues to justify the expense. It is an attractive idea politically to extend access to natural gas service to a greater proportion of rural Kansas, but frankly, it is unlikely to be economic and may leave utilities with stranded costs when irrigators can no longer economically pump water from the Ogallala aquifer. Protecting current ratepayers from subsidizing uneconomic extensions should be the Commission's highest priority.

The first round of comments from interested parties is available on the KCC's website. The second round of comments is due by August 27.

KCC Docket No. 14-GIMG-514-GIG

Atmos proposes changes to PGA

Last November, Atmos Energy applied for approval to add two new components to its Purchased Gas Adjustment (PGA) schedule. If approved, the changes would have allowed Atmos to split 50/50 with customers any savings from reducing upstream gas transportation costs, and any savings resulting from constructing new interconnects with pipelines other than the ones Atmos usually uses to supply gas it purchases for customers.

Then in February, Atmos met with the Commission Staff to discuss what the Company would do with its share of the savings. During this meeting,

Staff encouraged Atmos to amend its application to propose that Atmos retain 100% of any savings gained, rather than share the savings 50/50 with customers. Staff proposed that Atmos use the savings to fund a variety of Commission-approved capital improvements projects.

Some of these projects would extend natural gas service lines to underserved areas, such as all-electric subdivisions and large irrigation systems. Other proposed projects include constructing new storage facilities so that the company can buy more gas when prices are lower, and building new transmission pipelines to enable Atmos to access less expensive sources of natural gas and to be more competitive in purchasing transportation.

Atmos agreed to amend its application per Staff's proposal. It is now requesting that the company retain 100% of any savings gained from the new PGA for capital projects that it identified as having potential to generate savings for customers.

If approved, the PGA, which was created to pass through the actual cost of natural gas to customers, would no longer be solely based on the actual cost of gas. Instead, Atmos would determine a "benchmark" rate, which would be based upon the historical cost of gas. It would be this benchmark rate that would be passed through to customers. The difference between the rate charged to customers and the actual cost to Atmos to procure the natural gas would be considered "savings" to be retained by Atmos.

To think of it another way, it's like teenagers asking Mom and Dad for gas money for their cars. Mom and Dad oblige and give the teenager $50, which has been the amount usually required for a fill-up, but the teenager gets to keep any change that is left over if he can find a station that has cheaper gas. Atmos's customers are like Mom and Dad, paying more than the actual cost, while Atmos is the teenager who gets to keep the change.

CURB and Staff filed testimony in this docket on July 18, 2014. Staff reversed its suggestion from its February meeting with Atmos, and now suggests that Atmos should get to keep 75% of the savings, while passing the remaining 25% of savings back to customers through the PGA.

CURB recommended the Commission deny Atmos's application for several reasons. First, the PGA has been an effective way for the utilities to recover the actual cost of gas for 37 years. There is no profit or "savings" calculated in the PGA. Customers can be reassured that the price they pay to heat their homes in the winter is the actual cost for Atmos to deliver that natural gas to their homes.

Second, Atmos's proposal does not require the Company to actually use these "savings" to complete any capital improvement projects. Despite Staff's testimony that 75% of the savings generated from the amended PGA would be used for capital projects, the reality is that the extra money customers are paying will just go to Atmos's shareholders.

According to Atmos's proposal, if it retains $2 million in savings, and then completes a capital project that also costs $2 million, Atmos will include the $2 million capital project in its next rate case and recover the full amount (plus a return for shareholders) from its Kansas customers. The $2 million dollars "saved" from the PGA will not have any impact on the $2 million capital project. Atmos's customers will pay for both.

Third, some of the capital projects that Atmos suggested it may complete, like extending service lines to all electric subdivisions, are not economic projects. In other words, the cost to complete the project will exceed any benefits that may be received from the completion of the project. Considering that Atmos is already keeping the "savings" from the amended PGA, completing uneconomic projects means that current Atmos customers will be paying rates for projects that provide no actual benefit to them.

Finally, public utilities have a continuing obligation to operate efficiently and prudently on behalf of its customers; if switching pipelines will create net savings for customers, Atmos should do so as a part of its obligations as a monopoly provider. Customers should not have to provide additional profits to regulated utilities to ensure they

take action to locate and develop ways to reduce the cost of obtaining and delivering natural gas.

An evidentiary hearing is scheduled in this docket on August 28, 2014. CURB will continue to recommend denial of this proposal.

KCC Docket Nos. 14-ATMG-230-TAR

Atmos construction tariff OKd

On May 20, 2014, Atmos Energy received Commission approval to revise its "Customer Advances for Construction of Mains and Company Service Lines" tariff. This tariff establishes the charges for hooking up consumers located within Atmos's service territory who currently do not receive natural gas service from Atmos. For example, if you build a new home in an area within Atmos's certificated territory that does not have natural gas service lines, in order to receive natural gas service, you would need to pay Atmos to extend its distribution system to serve your home.

Atmos's revisions increased the prices charged for the construction to extend its mains and service lines, based upon Atmos's overall average embedded costs. These increases will have no impact on customers who currently receive natural gas service from Atmos Energy.

KCC Docket Nos. 14-ATMG-467-TAR

KGS moves from equal pay plans to average pay

On April 18, 2014, Kansas Gas Service, a Division of ONE Gas, Inc., filed an application seeking Commission approval to discontinue its equal payment plan and offer an average payment plan in its place.

Kansas Gas requested the change because it recently performed upgrades to its operating system. The new upgrades allow Kansas Gas Service to offer an average payment plan instead of an equal payment plan.

For Kansas Gas customers currently enrolled in the equal payment plan, there will be little change to their monthly bill. The equal payment plan was based upon a twelve-month average. Once a year, the customer's usage for the last twelve months was totaled and then divided by twelve. The result was the amount billed each month for the next twelve months. The monthly bill remained the same until the annual update was performed.

Customers who enroll in the average payment plan will find that their monthly bills will vary somewhat from month-to-month. The bills will be calculated each month based on a "rolling average." The most recent usage will be added to the twelve-month average calculation, while the oldest usage amount is dropped from the calculation. There will be no need to update the billing amount each year, because the system continuously adjusts the average each month in each new billing cycle.

The Commission approved Kansas Gas Service's request on July 2. The company's request complies with the Commission's billing standards. The same cancellation policy will be left in place, and the arrearage policy will also be the same. The Cold Weather Rule policy will remain in effect and unchanged by Kansas Gas Service's proposal.

KCC Docket Nos. 14-KGSG-476-TAR

KCPL's annual EE Rider approved

Last March, Kansas City Power & Light (KCPL) filed its annual Energy Efficiency Rider requesting to recover $827,410 from its customers for energy-efficiency programs.

The Energy Efficiency Rider is a separate line item on consumer bills that recovers KCPL's investment in Commission-approved energy-efficiency programs. KCPL's request shows that it spent $796,688 on energy-efficiency programs in Kansas during 2013, and that it carried over $30,722 that it did not recover in the previous year's Energy Efficiency Rider.

CURB recommended the Commission approve recovery of $798,453, which was based upon an actual audit of energy-efficiency program expenditures. CURB's audit of actual expenditures for KCPL's Energy Optimizer program showed

that $798,452 was the amount KCPL actually spent on the program during 2012 and 2013.

The difference between KCPL's request and CURB's audit was attributable to KCPL's inclusion of costs incurred prior to 2012 that had not been booked. Without any way to audit these expenses from before 2012, CURB argued the Commission should not allow KCPL to recover those specific expenses in the rider, and proposed an adjustment to remove them from KCPL's claim.

On July 1, the Commission rejected CURB's adjustment. In the order, the Commission granted KCPL permission to recover $827,410 through its Energy Efficiency Rider.

For customers who use 1100 kWh per month, the Commission-approved Energy Efficiency Rider will increase their monthly bills by $0.18.

Each year, KCPL files a new Energy Efficiency Rider on or before March 31 to recover actual costs incurred during the previous calendar year.

KCC Docket Nos. 14-KCPE-442-TAR

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Westar, KCPL seek special accounting treatment for 2015 rate cases

In a Joint Agreement filed on July 21, 2014, Westar Energy, Kansas City Power & Light, KCC Staff and CURB requested that the Commission approve procedural schedules for Westar and KCP&L's rate cases to be filed early in 2015. The agreement also requests special accounting treatment for Wolf Creek outage costs and for certain costs related to the $1.2 billion La Cygne coal plant retrofit.

Westar and KCP&L jointly own the La Cygne coal generation plant, which has been undergoing a Commission-approved retrofit to meet Environmental Protection Agency emission standards. While some of the retrofit cost is already in customer rates, Westar and KCP&L plan to file rate cases early next year to begin recovery of the full cost of the finished retrofit. Beginning in April, the retrofitted plant will begin operating in stages through July when it is expected to be fully operational.

Westar and KCP&L sought special accounting treatment for the La Cygne retrofit costs because between the date when the plant comes online—the in-service date—and when the cost of the plant is fully in customer rates, there is a short time period during which the companies are incurring deprecation expenses and carrying costs but not recovering them in rates. Shareholders essentially eat these costs during this lag period.

This lag in cost recovery is a fairly normal regulatory outcome; it happens in every rate case. But with the magnitude of costs associated with the La Cygne retrofit, the impact on shareholders is larger than normal. Thus, the utilities are requesting some accounting relief.

From an accounting standpoint, during this lag period, Westar will be able to track the depreciation and carrying costs that are not being recovered in rates and book these costs to what is called a regulatory asset. This just means Westar creates an account and puts the unrecovered costs in the account, to be recovered in customer rates at a later date. This is similar to what happens after a large storm hits Westar's system. Westar spends money getting the system back online, and the costs to repair the system are put into an account for recovery from customers at a later date.

Since KCP&L will file and complete its rate case earlier than Westar, KCP&L will use a slightly different accounting approach. KCP&L will use a forecast of the final La Cygne cost to formulate its rate request in its case next year. Then

KCP&L will track actual costs against the costs customers are paying in the approved rates until its next rate case, and will refund to customers any amount recovered in rates over the actual costs incurred.

For the Wolf Creek outage cost, the timing of the outage will require a similar accounting treatment if the cost is to be recovered from customers.

Westar and KCP&L also agree to stagger the filing of their rate cases, so as not to overwhelm the staffs of the KCC and CURB. Both the Westar rate case and the KCP&L rate case will be full rate cases, meaning that in addition to the La Cygne and Wolf Creek costs covered by the accounting treatment above, all other increases in costs the companies believe are appropriate for inclusion in customer rates will also be included in the rate case. Given the staffing levels at CURB and the KCC, working two major rate cases at the same time would be a challenge. While it wouldn't be impossible to handle, staggering the filings two months apart gives better assurance that each case will receive full scrutiny from both KCC and CURB analysts.

The accounting treatment in the agreement is favorable to the companies. But the Commission has granted this type of accounting treatment in other similar cases, with less money at stake. Rather than fight a losing battle, CURB worked with the companies to narrow the scope and timing of the costs that could be included and to insure a proper true-up to actual costs. While it's not a perfect solution, choosing to negotiate gave CURB the opportunity to bargain for terms that treat customers a bit more fairly than they might otherwise have been.

The agreement requests that the Commission grant or deny the joint proposal no later than September 15, 2014. If granted, KCP&L will file its rate case on January 2, 2015, with rates effective October 1, 2015, and Westar will file on March 2, 2015, with rates effective October 28, 2015. If the proposal isn't granted, we'll have to go back to the bargaining table. We'll let you know how it turns out in a future issue.

KCC Docket No 15-GIME-025-MIS

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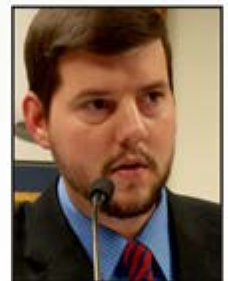

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Consumer Counsel's

CORNER

We're lagging here in the Corner. No, it's not that we're slow because we're in the doldrums of summer. And no, it's not that we've fallen behind on our work. It's just that we seem to be spending an inordinate amount of time arguing about "regulatory lag". I can see you shaking your head, so let me explain. Regulatory lag is shorthand for the time period between utility rate cases when a utility can't change its rates.

Once upon a time in Kansas, a utility came in for a rate case, its books were scrutinized, rates were set and the utility was sent on its way. It continued to charge those rates until such time that it had made large enough investments, or incurred large enough expenses that the allowed rates were no longer sufficient. It would bring all its new cost data to the Commission, undergo the same scrutiny, get new rates and go on its way again. Between cases, customer rates could not be changed.

Traditionally, rates are set at a level that will allow the utility a reasonable opportunity to make a profit, all things like weather and sales being normal. *How much profit* is one of those issues we argue about a lot in rate cases. Small or large, the profit built into rates compensates investors for taking on the risk that management will manage well between rate cases. Since it couldn't simply change rates to pass cost increases to its customers without filing another rate case, a utility had to manage its costs and expenditures prudently if it hoped to make a profit and pass along a return to its investors.

Thus, regulatory lag has traditionally served as an essential cost-containment device that exerts pressure on utilities to spend prudently and keep costs down.

Well, like I said … once upon a time.

Over the last decade, both the legislature and the KCC have created numerous line-item charges and accounting mechanisms that reduced or eliminated regulatory lag. (In all fairness, I must disclose that CURB has gone along with several of these mechanisms that we thought made sense, but on balance, CURB has actively opposed most of these changes.)

If you've followed the Corner, you know I've written about many of these changes and how utilities use them to continually increase rates. Since 2009, the running count of Westar rate increases stands at 21 increases and 1 decrease, for a net total increase to customer rates of $537 million. (See CURB's Westar Increase Fact Sheet, http://curb.kansas.gov/).

CURB has also researched the history of the past 35 years in Kansas, and found that the utilities have managed to secure at least 35 different mechanisms that have in some way, reduced regulatory lag or its effects.

In the earlier years, most were granted as "extraordinary" relief—temporary measures to assist with recovering extraordinary expenditures like the costs of repairing major ice storm or tornado damage, or were granted to provide full recovery of the costs of paying property taxes or other costs that were out of the utility's power to control. But base rates remained the primary method of recovery of most costs, which provided valuable protection to customers from runaway spending between rate cases.

So historically, regulatory lag has been viewed as an important tool to keep utility cost increases in check. But if every utility expenditure can quickly be recaptured through higher rates in one mechanism or another, what incentive does the utility have to control costs? Worse, once these mechanisms are in place, they create an additional incentive of their own to spend money to make money.

For perfect examples, look no further than the proposals in the Atmos and Black Hills rate cases described elsewhere in this issue of CURBside. Both companies want a new mechanism that will allow faster recovery (reduced regulatory lag) for investments to replace pipeline on their systems. They say it will improve safety. That doesn't sound unreasonable, unless you consider that the legislature already gave these companies a surcharge (GSRS)

to get rate recovery of safety-related expenditures between rate cases. They already use this surcharge to increase your rates every year. But now they want a whole new surcharge.

Why would these utilities possibly want a new surcharge? Are the pipeline systems unsafe? Are they having problems securing financing? Are they in dire need of new investors? No, no, and no. The companies assure us that everything is safe and sound on their systems, that there is no concern about meeting all safety requirements, and they have access to the capital they need. So will additional investment bring a measurable increase in safety to their customers? We can take a guess that new pipe is safer than older pipe, but no one yet has produced evidence to suggest that customers will be 10 percent or 20 percent or even 2 percent safer if we make these investments and we take more money out of customer pockets sooner. So what could it be that is driving this need for more surcharges?

Maybe it's because the legislature imposed a 40 cents per year cap on increases of the GSRS surcharge on customer bills, and prescribed limits on what kind of expenditures qualify for recovery. So, while the legislature said that safety improvements were important, important enough to justify reducing regulatory lag, the legislature also struck a balance bebetween customers and the companies by limiting the kinds of projects that qualified for GSRS recovery, and limited the impact on monthly customer bills by capping the annual increase at 40 cents, or $2.00 over five years.

So: If the KCC gives Atmos and Black Hills more new surcharges, they get brand-new investment vehicles, without caps on annual recovery and with fewer limits on what kinds of system improvements qualify for recovery. No longer hampered by the legislative cap, they can increase their investments, increase customers' rates, reduce the regulatory lag on getting the return on those investments, and increase returns for shareholders. What's not to like? Surcharges are a gravy train for utilities and they are all jumping on board. It's no wonder they are asking for more.

Someone smarter than me once said "All regulation is incentive regulation; you just have to decide what you want to incent."

In Kansas, the decision has been made to create incentives for shareholders to invest in utilities as a way to grow utility profits. And since it's a low-risk proposition for the utilities that have mechanisms to reduce or eliminate regulatory lag, investment is happening. But utility rates continue to climb in Kansas.

The KCC could soften the impact on customers by reducing profit levels to reflect the lower risk these utilities are facing—to some extent, it has, in a very limited way—but for the most part, customers are still paying high shareholder profits in rates even while regulatory lag and regulatory risk are being reduced with each new surcharge or special recovery mechanism that is approved. As a result, customers bear more risk of higher rates, because reducing regulatory lag not only encourages investment, it also reduces the incentive for utilities to contain costs between rate cases.

Ultimately, the legislature, the KCC and utility customers need to find a way to slow down this gravy train. Here at the Corner, we're thinking that regulatory lag has been—and continues to be—an important regulatory tool that helps puts the brakes on spending. Regulatory lag needs to make a comeback in Kansas.

—Dave Springe

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