

# Kansas Energy Problem

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*High electric rates rising higher*

House Energy, Utilities & Telecommunications Committee  
March 1, 2022



# How Utility Rates Are Set

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*(A simplified view of a complex process)*

**Utility rates are set using the following simplified formula:**

(Rate base x rate of return) + operating expenses = revenue requirement

Revenue requirement / expected kWh sales = kWh rate

For example: Assume a utility had a rate base of \$1B, a 10% ROR, \$100M in annual operating expenses and \$2B in annual kWh sales. Using the above formula, you would get:

$$(\$1,000,000,000 \times .10) + \$100,000,000 = \$200,000,000$$

$$\$200,000,000 / 2,000,000,000 = \$0.10 \text{ kWh rate (10 cents a kWh)}$$



# Utilities make money by investing

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- Investor-owned utilities (IOUs) like Evergy make money for shareholders by investing capital. Invested capital is tracked in a utility's "rate base" and utilities earn a return on their rate base.
- Utilities can't easily control sales, but they can increase their rate base to generate additional earnings for shareholders.

## Accounting principals:

- Evergy's annual depreciation is \$880M, meaning without additional investment, rate base would go down \$880M each year.
- Going forward, Evergy can invest \$880M each year without requiring an increase in rates.
- Some states require longer depreciation schedules to moderate increases.



# Regulatory Basics

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Rates are set by customer class (residential, commercial, industrial) based on cost of service studies. Generally, customers pay what it costs to serve them, plus a return (profit) for the utility.

Commercial & Industrial customers take various types of service:

- Secondary level – similar to a residential customers
  - Pay for generation, transmission costs, substations and distribution lines
- Primary level – Take service directly from a utility substation
  - Pay for generation, transmission costs and substations
- Transmission level – Customers own their own substations
  - Pay for generation and transmission costs
- Special contracts and economic development rates



# Rate Study (SB 69) -- Major Concerns Cited

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- **Current ratemaking methods favor utilities**
  - *“the current IOU ratemaking practices reflect some degree of imbalance between utility incentives and public interest objectives (such as achieving regionally competitive rates or other public policy objectives)”*
- **Underutilized assets are a drag on rates**
  - *“while the KCC’s primary objective standards and vetting process for ensuring the prudence of utility investments are sound, they are limited in terms of protecting ratepayers from paying for investments that are underutilized. For instance, declining capacity factors of currently operating rate-based Kansas coal plants (two of which have capacity factors significantly below the regional average) suggest a need to periodically review their usefulness”*
- **Surcharges need adjustment**
  - *“there is potential for improvement in the processes for review of recovery of surcharges and riders”*

# Regionally high electric rates

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For the last several years, Kansas has had the highest electric rates in the region.

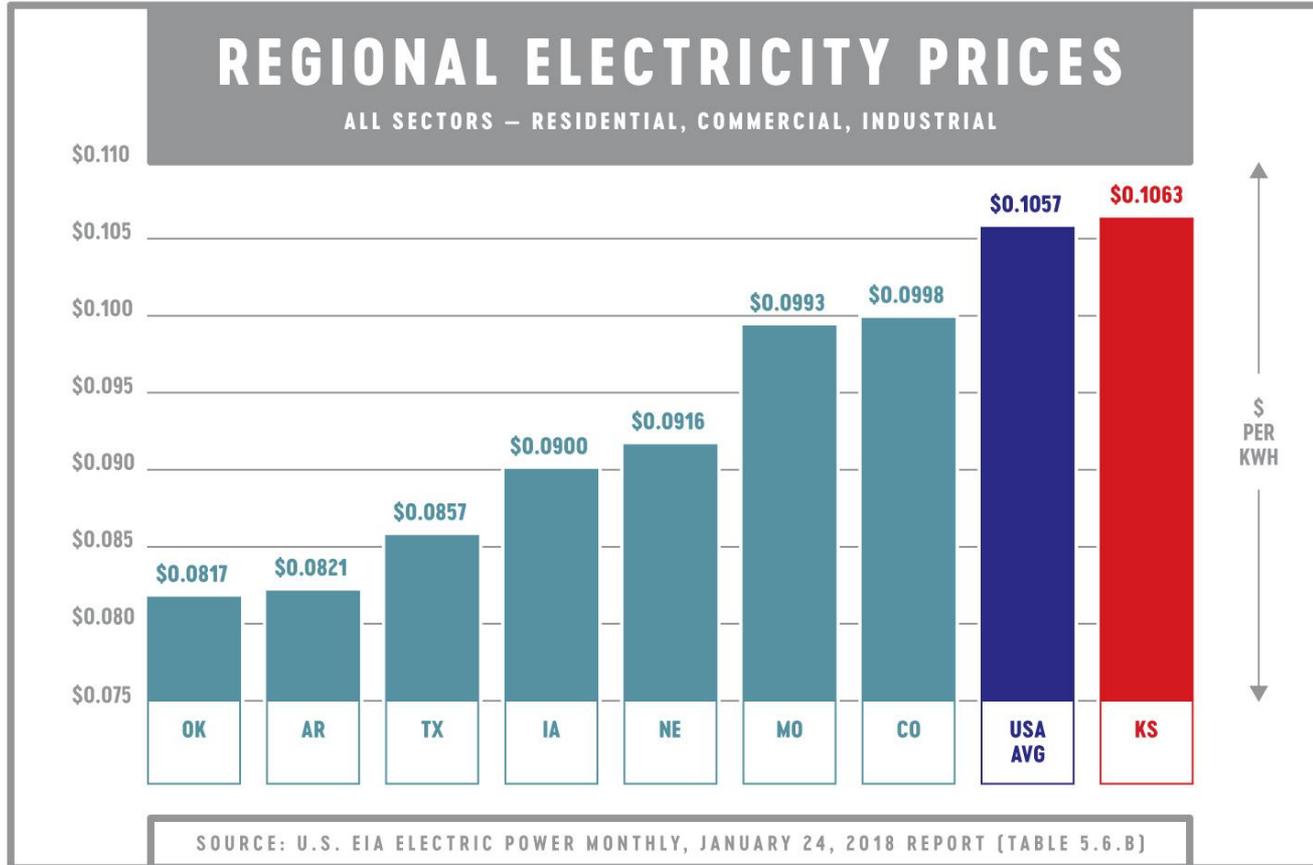
This is confirmed by data from:

- Federal Energy Information Agency
- London Economics (Phase 1 Rate Study consultant)
- AECOM (Phase 2 Rate Study consultant)
- Evergy internal analysis
- Additional outside sources (including KIC & KLER)

There is no dispute that Kansas has the highest rates in the region. Evergy sells about 75% of the total retail electric sales in the state, and is the wholesale supplier for much the remaining sales through KEPCo and Midwest Energy.



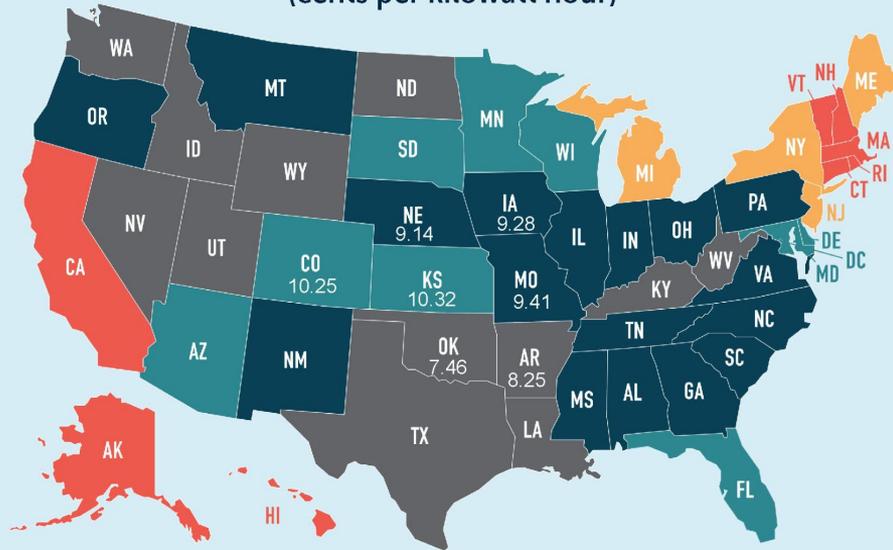
# Original 2018 Chart





# Rate Examples

## 2020 U.S. Average Electricity Retail Prices (cents per kilowatt hour)

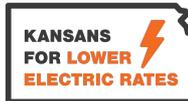


Source: U.S. Energy Information Administration; Electric Power Monthly; February 2021



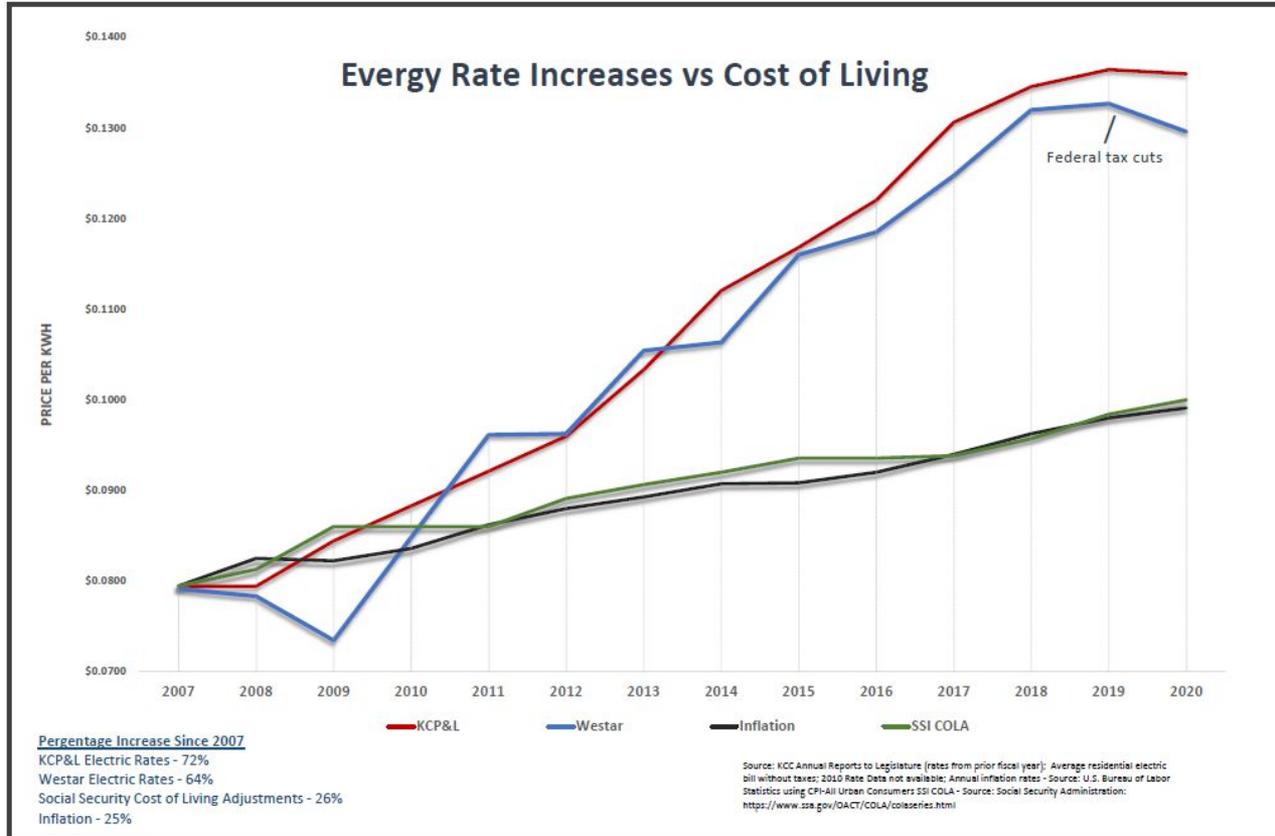
A large Kansas manufacturing company, using 250,000,000 kWh of electric energy on an annual basis, would have an annual electric bill as follows:

- Wichita - \$18,875,000
- Tulsa - \$9,575,000
- Oklahoma City - \$9,850,000
- Des Moines - \$13,950,000
- Fayetteville - \$14,025,000
- Denver – \$15,550,000



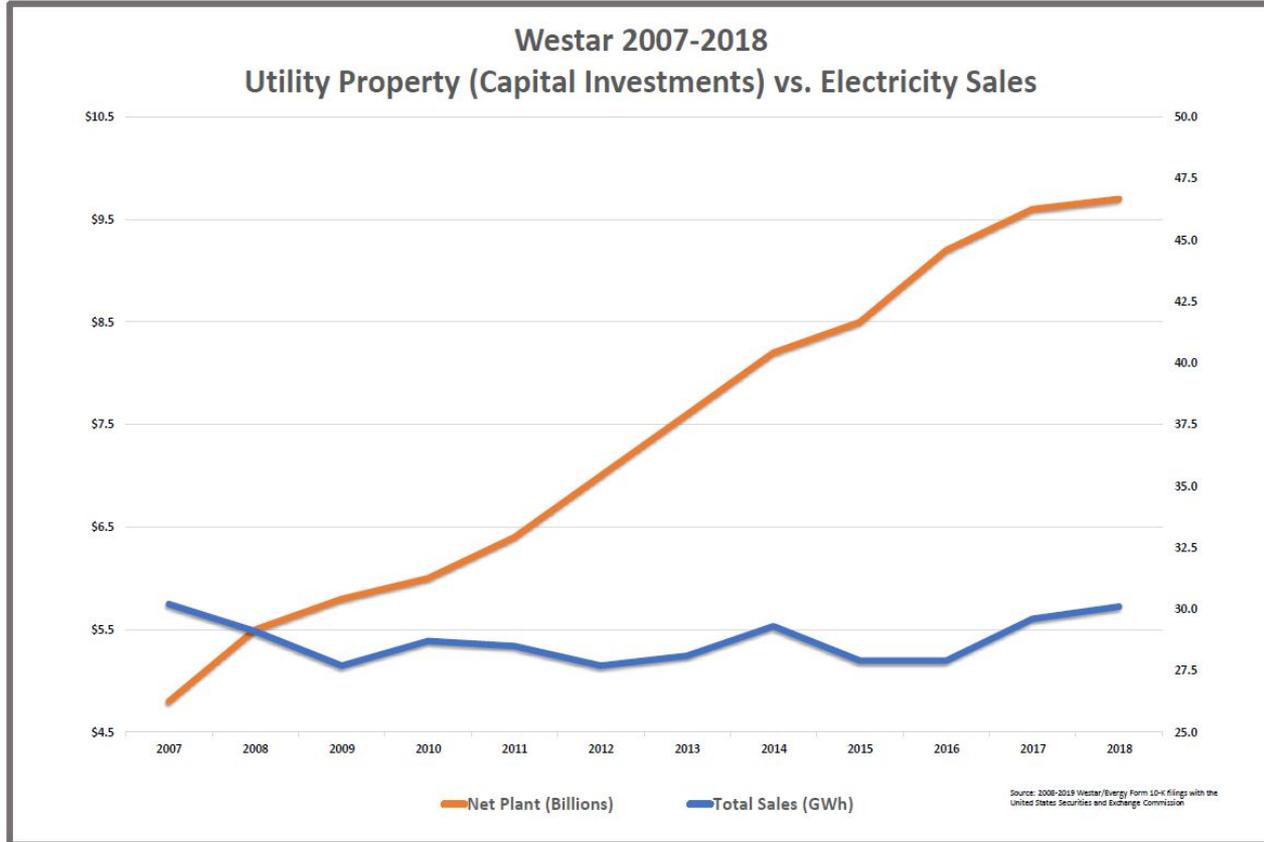


# Rates increased far more than CPI





# Sales are flat, but investments rapidly grow



# No real rate moratorium – TDC increases

The merger-related rate moratorium applies to base rates only, not to riders and surcharges like the Transmission Delivery Charge (TDC). Roughly half of Evergy bills are comprised of surcharges, riders or other adjustments that continue to be adjusted through the moratorium.

- February 17, 2022 TDC increase – \$20.4M**

TDC Adjustments		
Date	Increase	Decrease
April 2018	\$31,456,832	
April 2019		\$7,697,765*
April 2020	\$3,478,797	
April 2021	\$38,091,942	
April 2022 -- <i>proposed</i>	<b>\$20,400,559</b>	
<b>Net Increase = \$85,730,365</b>		

*\*2019 decrease impacted by federal tax cuts*



# Evergy compared to the region

<b>Regional Electric Rate Comparison</b>				
<b>2020/2021 -- Sorted by Residential</b>				
		<b>Residential</b>	<b>Commercial</b>	<b>Industrial</b>
<b>Municipal Utilities</b>	<b>State</b>	(¢/kWh)	(¢/kWh)	(¢/kWh)
McPherson BPU	KS	7.35	6.22	4.66
City of Russell	KS	10.17	9.42	7.25
Omaha Public Power District	NE	13.07	9.83	7.9
Kansas City BPU	KS	14.57	11.78	8.4
Independence Power & Light	MO	15.14	13.42	9.88
<b>Investor Owned Utilities (IOU)</b>				
OG&E Electric Services	OK	8.91	6.5	3.94
Public Service Company of OK	OK	9.33	5.94	3.83
Ameren Missouri	MO	10	7.71	5.76
Southwestern Electric Power	AR	10.35	7.82	5.61
MidAmerican Energy	IA	10.77	7.34	5.58
Public Service Company of CO	CO	11.41	10.11	6.22
Evergy Missouri West	MO	11.46	8.36	6.12
<b>Evergy Kansas Central</b>	KS	12.44	10.5	7.55
<b>Evergy Kansas Metro</b>	KS	12.86	10.74	8.19
Evergy Missouri Metro	MO	13.09	10.78	7.5

Notes:  
Municipal rates include charges for the PILOT and are calculated using current rates and the same billing determinants as IOU rates  
IOU rates are weighted averages of 4 months summer and 8 months of winter Edison Electric Institute rates and does not include any special contract rates.



# The Legislature is taking notice

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## 2018 -- Senate Resolution 1612

- *“A concurrent resolution supporting and facilitating regionally competitive retail electric rates in the state of Kansas and urging the KCC to take all lawful action to promptly set rates for retail electric service in the state of Kansas at regionally competitive levels.”* Passed 30-9

## 2019 -- SB 69 -- Electric Rate Study

- *“To provide information that may assist future legislative and regulatory efforts to craft forward-looking electric policy that leads to regionally competitive electric rates and reliable electric service, the legislative coordinating council shall authorize a study of the retail rates of Kansas electric public utilities.”* Passed 38-1 and 117-7

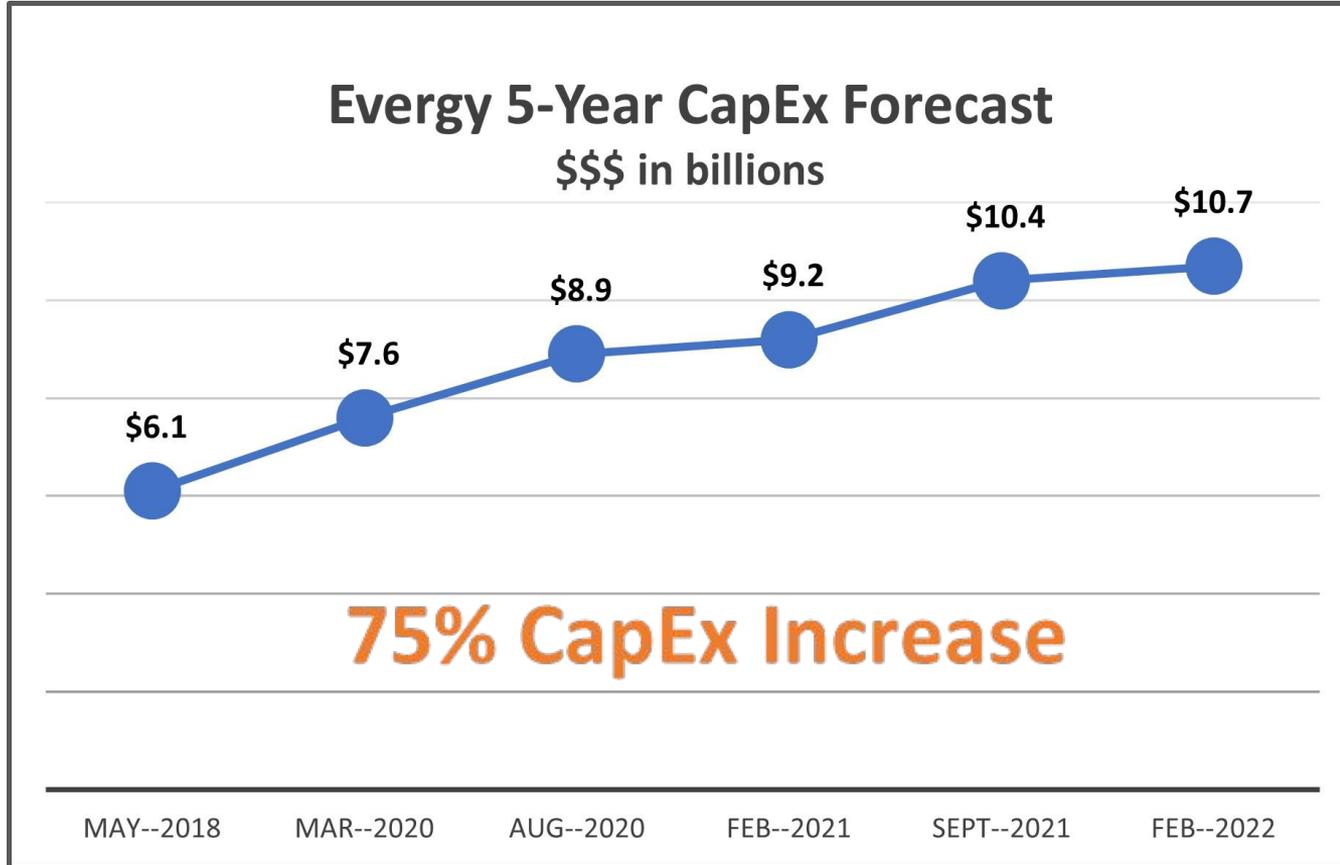
## 2020 -- HB 2585 -- Income Tax Elimination and Economic Development Rates

- Reduced Evergy rates \$30M; Passed 39-1 and 75-45

## 2021 -- Sen. Sub for HB 2705 – Securitization



# CapEx increasing more than 75%





# STP will drive rates higher

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- The Sustainability Transformation Plan (STP) is explicitly designed to increase shareholder returns.
  - Evergy: *“New Five-Year Strategic Plan Delivers Increased Value Creation for Evergy Shareholders”*
  - Evergy: *“Maximize long-term shareholder value”*
- Utilities make money by investing capital. The STP increases Evergy capex by over 70% from estimates in the merger agreement.
- Much of the investment is in transmission and delivery systems.
  - Evergy receives an enhanced return for transmission investments.



# Largest increase in state history

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- The STP is expected to increase rates 10-11% (per Wichita Eagle)
- A 10% increase equals about \$220M/year, every year, or \$2.2B in increases over 10 years. *Evergy has similar investment plans 2025 to 2030.*
- The largest increase in state history was \$134M.

## The KCC has raised the yellow flag. Is it enough?

- The KCC recently said “The Commission is also concerned with new Evergy projections of future spending increases.” And further it said “it is important for Evergy and other Kansas utilities to achieve and maintain regionally competitive retail rates.”

# Next Steps

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The current regulatory process isn't leading toward regionally competitive rates.

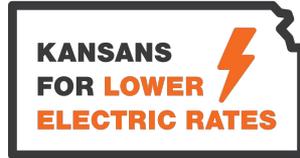
## Options to consider:

- Deregulation
  - Evergy indicated it's open to the discussion
- Performance based rates
  - Instead of being rewarded for investments, reward Evergy for competitive rates
- KCC reform
  - Consider election of commissioners or a change in overall charter



# Contacts

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- Jim Zakoura, President of KIC & KLER | 913-661-9800 | [jim@smizak-law.com](mailto:jim@smizak-law.com)
- Paul Snider, KLER & KIC | (913) 439-9723 | [paul@sniderpa.com](mailto:paul@sniderpa.com)
- Gavin Kreidler, KLER | 316-992-1872 | [gavin@kreidlerconsulting.com](mailto:gavin@kreidlerconsulting.com)

