



SB245

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For the Senate Committee on Financial Institutions & Insurance

Support

February 18, 2021

Good morning, Chairman Longbine and Members of the Committee.

Evergy appreciates the opportunity to appear before you today to offer legislation that proposes a financial tool to allow customers to save money. The concept of securitization is available in some form in 25 other states. We will walk through the bill's features, but first we want to talk about why securitization is needed.

Evergy is generally long on older, more expensive coal generation. In other words, we have older and less efficient coal power plants that are now approaching the end of their lifetimes. It costs us more to run them than it does to run newer generation, and yet because of the way rates are made, we continue to keep these units in use.

After generating assets (or power plants) are placed into service, they begin depreciating the capital generally over a defined period. However, each subsequent investment (like pollution control equipment) adds more capital and increases the base costs needing to be depreciated, effectively lengthening the depreciable life of the asset. This can create a situation where a utility is ready to move on from an investment but is financially incentivized to keep it in service because of the unrecovered capital and the expectation of an opportunity to earn a return on that capital investment. A great example is smaller coal plants that are 60-70 years old but have had emissions upgrades in the last 10 years. The upfront investment cost of those upgrades will not be recovered by the utility for another decade, even as the asset may struggle to be cost competitive in the energy market.

We are also increasingly seeing demand from industrials, municipalities, educational institutions and everyday customers for access to renewable energy. We have abundant access

to wind and solar energy in Kansas, and it could be a real market advantage for Kansas in attracting new jobs. Between our current renewable fleet and Wolf Creek Nuclear Generating Station, Evergy's power is already 50% carbon free for our retail sales.

How Securitization Helps

Securitization is simply a financial tool to help reduce the costs of financing unrecovered assets - that is, power plants that still have costs to be recovered. It's a win-win tool that allows the utility to recover those costs and for customers to realize a savings. By refinancing the unrecovered portion of the asset, at a low interest rate, customers save money. The utility gets back the money invested in the plant, but gives up any future return on investment. It can then redeploy the capital into other needs. In many ways, it's similar to when you pay off your car or mortgage payment early.

Attached to this testimony is an example that helps illustrate how savings would be realized. The illustration shows what it would look like with and without securitization if Evergy retired an asset of \$300 million. The math is straightforward. If you replace a 9% return on investment with a 2% or 3% bond, you save money. In this example, with securitization, you would spend \$15 million less than if you didn't have securitization as a financial tool. That's \$15 million that would not be placed in rates. Customers save money.

Specifically, when the company decides to securitize an asset, it forms a Special Purpose Entity (SPE) that issues bonds. Evergy transfers property to the SPE, in the form of a right to receive revenues produced by a dedicated and non-bypassable charge on customers' bills for electric service, and receives the amount of undepreciated capital costs (or remaining costs) left. The SPE finances the bonds at 2-4%, and a charge is placed on customer bills (Energy Transition Charge or ETC) that pays back the debt service on the bond. The key for bondholders is that the charge is irrevocable and is trued up at least annually to ensure that funds sufficient to pay off the bonds are produced. This gives them the security they need to invest in those bonds.

What are key pieces of the bill?

The bill has basically four parts. The beginning is the basic blocking and tackling of securitization. A key piece here is that securitization must be voluntary and not forced on the utility. If it's not voluntary, you could see environmental groups push to close all coal plants by 2030. We would have reliability concerns if the option weren't voluntary. This section clearly provides for a full proceeding at the Kansas Corporation Commission to seek that body's approval for securitization financing if Evergy applies for it.

The second section of the bill is very short and simply makes it clear that the proceeds of the securitized bonds received by the utility can be used by the utility for purposes it chooses at its sole discretion and, further, should the utility invest those proceeds, or any portion thereof, in electric infrastructure, then those investments would be reviewed for rate purposes according to existing processes.

The third portion is pre-determination for retirement of generation assets. This allows the utility (and all stakeholders) to have the certainty for the retirement of generation assets. It allows for an orderly plan that is beneficial for the utility and stakeholder planning. Without predetermination, a utility might make the call to retire coal generation only to be second-guessed in a later rate proceeding after the plant had been retired from service.

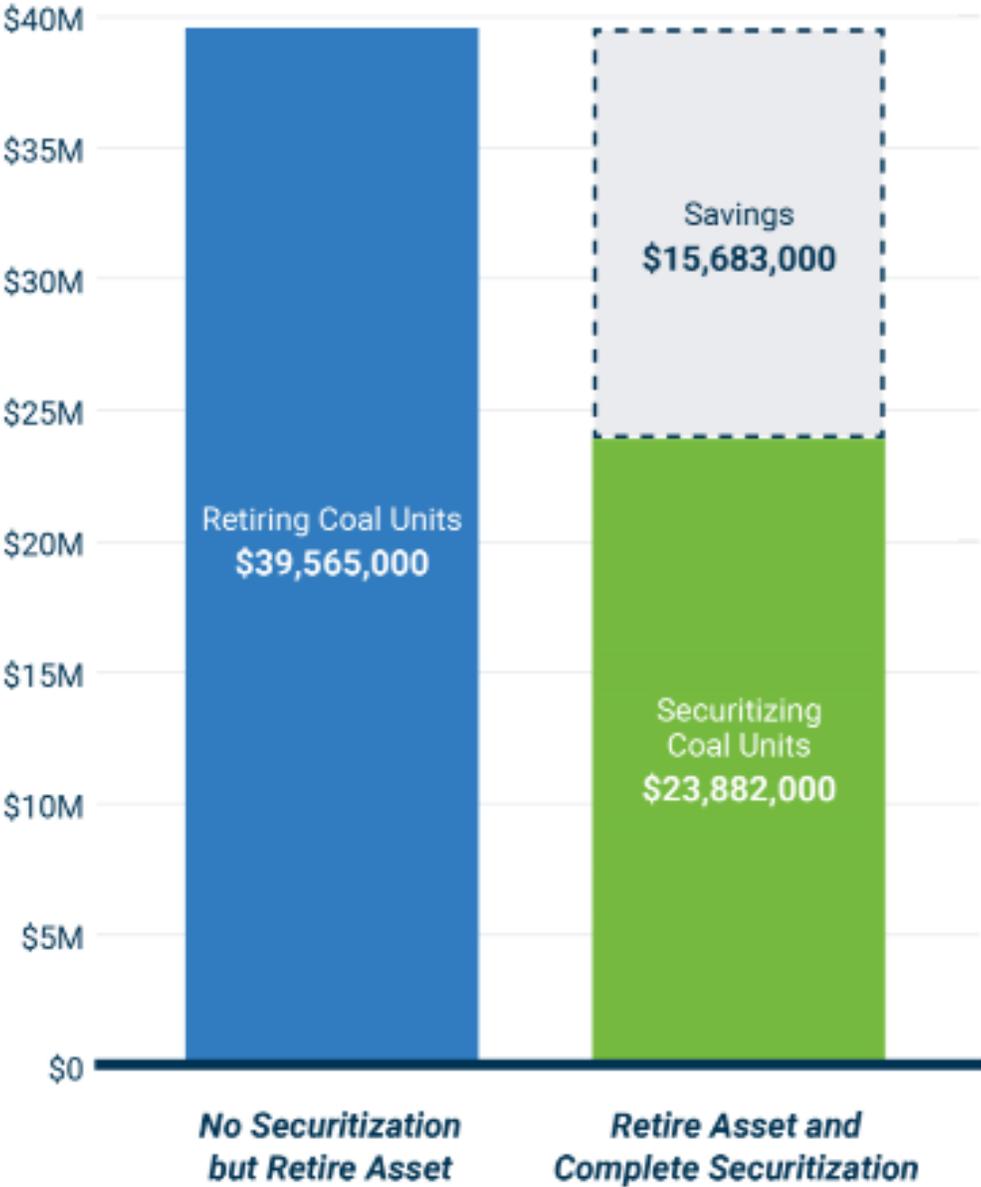
Kansas already has pre-determination for putting new assets INTO service. All that this language would do in SB245 is extend that to taking generation assets OUT of service. The Kansas Corporation Commission continues to have the ability to oversee all of our decisions and proposals.

The fourth and final portion is not controversial and is simply common language to the Uniform Commercial Code that goes along with section 1. This is supporting legal language that doesn't introduce any new concepts into the bill.

Conclusion

We appreciate the Chairman bringing this bill forward. We've had constructive dialogue from many stakeholders and have tried to make this bill work for as many as we could. We believe this is an important policy for the state of Kansas. It allows Evergy to retire older, more expensive generation, saves customers money in the long run, and is a way to re-invest in Kansas. This bill is simply a tool in the toolbox that will help make an orderly transition for any generation asset that is closing.

Securitization



Net Book Value = \$300M

These numbers are for illustrative purposes only, using round numbers and making likely assumptions about the market.