

166 FERC ¶ 61,194
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Neil Chatterjee, Chairman;
Cheryl A. LaFleur, Richard Glick,
and Bernard L. McNamee.

Kansas Electric Power Cooperative, Inc.

Docket No. EL19-17-000

v.

Westar Energy, Inc.

ORDER DENYING FORMAL CHALLENGE AND COMPLAINT

(March 21, 2019)

1. On November 16, 2018, pursuant to sections 206, 306, and 309 of the Federal Power Act (FPA),¹ Rule 206 of the Commission's Rules of Practice and Procedure,² and Westar Energy, Inc.'s (Westar) Cost-Based Formula Rate Agreement for Full Requirements Electric Service (Formula Rate Agreement),³ Kansas Electric Power Cooperative, Inc. (KEPCo) filed a Formal Challenge and Complaint against Westar. KEPCo alleges that Westar has violated and continues to violate its formula rate, as well as Commission orders, regulations, and ratemaking policies, by failing to reflect in the rates paid by KEPCo and calculated pursuant to the Generation Formula Rate (GFR) the reduction in the federal corporate income tax rate that went into effect on January 1, 2018. KEPCo also asserts that Westar improperly included, in the 2018 Annual Update⁴ of the GFR, approximately \$551,000 associated with Westar's settlement of a personal injury lawsuit. In this order, we deny the Formal Challenge and Complaint.

¹ 16 U.S.C. §§ 824e, 825e, 825h (2012).

² 18 C.F.R. § 385.206 (2018).

³ Westar, Cost-Based Tariffs, Rate Schedules, and other Agreements, KEPCo Full Requirements Electric Service Agreement.

⁴ The Annual Update is Westar Energy's annual recalculation of the Demand Charge and Variable Operating and Maintenance (VOM) expenses under the Formula Rate Agreement.

I. Background

2. On December 22, 2017, the President signed into law the Tax Cuts and Jobs Act of 2017 (Tax Cuts and Jobs Act), which, among other things, reduced the federal corporate income tax rate from 35 percent to 21 percent, effective January 1, 2018.⁵ This means that, beginning January 1, 2018, companies subject to the Commission's jurisdiction will compute income taxes owed to the Internal Revenue Service (IRS) based on a 21 percent tax rate. The tax rate reduction will result in less corporate income tax expense going forward.⁶

3. On March 15, 2018, pursuant to section 206 of the FPA, the Commission issued two orders to show cause directing public utilities that use stated transmission rates or transmission formula rates with a fixed line item of 35 percent for the federal corporate income tax rate under an Open Access Transmission Tariff or transmission owner tariff to propose revisions to their stated transmission rates or transmission formula rates to reflect the reduced federal corporate income tax rate or show cause why they should not be required to do so.⁷

4. Westar's Formula Rate Agreement rate is the product of a settlement between Westar and its customers, which the Commission approved on August 21, 2009.⁸ Westar's rates for the service provided under the Formula Rate Agreement are calculated pursuant to a formula rate template—the GFR—contained in Attachment D to the Formula Rate Agreement. In addition, under Attachment H to the Formula Rate Agreement (Protocols) on or before June 1 of each year Westar is required to submit the Annual Update for the upcoming Contract Year, which is the twelve-consecutive-month period beginning on June 1 and ending on May 31 of the following year. In addition, the Protocols provide processes for customers to submit information requests and for preliminary and formal challenges to Annual Updates each year.

⁵ Tax Cuts and Jobs Act, Pub. L. No. 115-97, 131 Stat. 2054 (2017).

⁶ *See id.* § 13001, 131 Stat. at 2096.

⁷ *See AEP Appalachian Transmission Co., Inc.*, 162 FERC ¶ 61,225 (2018) (Formula Rates Show Cause Order); *Alcoa Power Generating Inc., – Long Sault Division*, 162 FERC ¶ 61,224 (2018) (together, Tax Show Cause Orders).

⁸ *Westar Energy, Inc.*, 128 FERC ¶ 61,174 (2009).

II. Formal Challenge and Complaint

5. KEPCo alleges that Westar violated its GFR in two ways: (1) failing to reflect in the rates paid by KEPCo and calculated pursuant to the GFR the reduction in the federal corporate income tax rate that went into effect on January 1, 2018; and (2) improperly including approximately \$551,000 associated with Westar's settlement of a personal injury lawsuit.⁹ KEPCo estimates that, taken together, the violations of the formula rate have resulted in GFR rates that are overstated by about \$2,904,698.

6. According to KEPCo, on or around June 1, 2018, Westar populated the GFR for the Contract Year running from June 1, 2018, through May 31, 2019. KEPCo adds that, following its review of the proposed rates, on September 17, 2018, it submitted a list of informal challenges to the 2018 Annual Update in accordance with the Protocols. KEPCo states that on October 15, 2018, Westar provided a response and indicated that it had rejected certain of the issues identified in KEPCo's challenges and believed that all charges in the 2018 Annual Update were appropriate.¹⁰

7. With regard to its allegation that Westar improperly calculated the federal corporate income tax expense in the 2018 Annual Update, KEPCo maintains that: (1) Westar should have corrected the overstated tax expense from January 1, 2018 through May 31, 2018 as a mistake in the 2018 Annual Update; (2) Westar utilized the improper federal corporate income tax rate in the 2018 Annual Update for the 2018-2019 Contract Year; and (3) to the extent the Commission finds that a change to the GFR is needed to address the tax issues, the Commission has the authority and factual record upon which to order such changes, in which case the Commission should order refunds as of January 1, 2018.

8. First, regarding the period from January 1, 2018 to May 31, 2018, KEPCo states that although the federal corporate tax rate was 35 percent when Westar populated the GFR in June 2017, as of January 1, 2018, the 35 percent data input was no longer correct. KEPCo argues that the use of the 35 percent tax rate was a mistake and should have been changed to 21 percent. KEPCo states that section 1.4 to the Protocols provides that corrections of mistakes are to be reflected in the Annual Update for the next effective Contract Year.¹¹ KEPCO maintains that the Commission has authority pursuant to section 309 of the FPA to enforce the terms of the GFR to give effect to the reduced

⁹ KEPCo Complaint at 1-2.

¹⁰ *Id.* at 5.

¹¹ *Id.* at 9.

federal tax rate effective January 1, 2018.¹² KEPCo states, further, that the Protocols provide as follows:

“Mistake” shall mean errors or omissions regarding the values inputted into the Formula Rate, such as, but not limited to, arithmetic and other inadvertent computational errors, erroneous Form 1 references or the like. Mistakes shall not include matters involving exercise of judgment or substantive differences of opinion regarding the derivation of an input that is more properly the subject of the annual review process.¹³

KEPCo argues that there is no fixed federal corporate income tax rate specified in the Westar GFR, but that it is one of the “values inputted into the Formula Rate” on an annual basis. KEPCo also asserts that the Protocols identify certain specific inputs to the formula rate that shall not change absent a filing with the Commission under section 205¹⁴ or section 206 of the FPA. KEPCo adds that, as the federal income tax rate input is not listed, it is one of the values that can automatically update to match currently-effective income tax rates or, as needed, can be corrected through the procedures specified for mistakes in the Protocols. Therefore, KEPCo concludes, the Commission should order Westar to recalculate the 2017 formula rate charges to account for the reduced federal corporate income tax rate and direct Westar to provide such refunds, with interest, as are required to make KEPCo whole, and to ensure that KEPCo pays only the actual cost of Westar’s service.¹⁵

9. Second, KEPCo maintains that Westar used the incorrect federal income tax rate in the 2018 Annual Update by retaining the 35 percent rate even though the 21 percent rate had been in effect for five months. KEPCo reiterates that the GFR is a cost-based rate designed to recover Westar’s actual cost of providing service, and that as Westar will at no point in the 2018-2019 Contract Year pay federal income taxes at a 35 percent rate, it is inappropriate to allow Westar to charge customers at that rate.¹⁶

¹² *Id.* at 8-9.

¹³ *Id.* at 9-10 (citing Westar, Cost-Based Tariffs, Rate Schedules, and other Agreements, KEPCo Full Requirements Electric Service Agreement (0.0.0), Attachment H (Demand Charge and VOM Protocols) (1.0.0)).

¹⁴ 16 U.S.C. § 824d (2012).

¹⁵ KEPCo Complaint at 10.

¹⁶ *Id.* at 11.

10. KEPCo states that, in an October 15, 2018 correspondence with KEPCo, Westar took the position that using 2017 data is appropriate because the GFR uses historical data.¹⁷ KEPCo argues, however, that the income tax allowance component of the GFR is not based on historical costs, but is calculated by taking the “Current Income Tax” and multiplying it by the “Return” as calculated by the Annual Update. KEPCo asserts that Westar’s response to KEPCo’s informal challenge placed great weight on the GFR’s reference to the federal income tax rate at “year end” and assumed that the reference is to the end of the calendar year. But KEPCo contends that the phrase “year end” is not defined in the GFR and Westar’s interpretation is inconsistent with other provisions of the GFR relevant to the federal income tax rate. KEPCo states that the GFR includes a defined term “Contract Year” defined as the “twelve-consecutive-month period beginning at midnight on June 1 and ending at midnight on May 31 of the following year.”¹⁸ KEPCo maintains that reading “year end” to refer to the end of the prior contract year, which as applied to this scenario would be May 31, 2018, produces a more reasonable projection of Westar’s tax liability and is consistent with recovering Westar’s actual cost of providing service to KEPCo.¹⁹

11. In addition, KEPCo states that in the Formula Rates Show Cause Order the Commission stated the following: “For formula rates with inputs that are adjusted annually, the current 21 percent federal corporate income tax rate will be reflected in a transmission revenue requirement without requiring a revision to the formula rate.”²⁰ KEPCo adds that the Commission stated that “[w]hen tax expense decreases, so does the cost of service.”²¹ KEPCo contends that, although Westar is not one of the named utilities against whom the Tax Show Cause Orders were issued, the Commission could have included Westar had it anticipated Westar’s refusal to pass through to wholesale customers the benefits of the lower federal corporate income tax rate. KEPCo argues that Westar’s position that KEPCo must wait until June 1, 2019 to begin to receive any benefit of the tax cut is entirely inconsistent with an annually-adjusting, cost-based

¹⁷ *Id.*

¹⁸ *Id.* at 12 (citing Cost Based Agreement at Article 1, definition 12).

¹⁹ *Id.* at 11-12.

²⁰ *Id.* at 12 (citing Formula Rates Show Cause Order, 162 FERC ¶ 61,225 at P 4).

²¹ *Id.* (citing Formula Rates Show Cause Order, 162 FERC ¶ 61,225 at PP 3-4).

formula rate and the Commission's clear expectation of how tax expense would be treated under those formulas.²²

12. Third, KEPCo maintains that, to the extent a change to the GFR is required to implement any portion of the relief KEPCo seeks, the Commission has ample authority to order the necessary changes. KEPCo argues that if "year end" is not interpreted as KEPCo has demonstrated, then the provision is plainly unjust and unreasonable because it permits the rates charged to KEPCo to be based not on the actual cost of service, which will result in Westar receiving a permanent, unjust enrichment of approximately \$2,059,291 for the 2018-2019 Contract Year and \$858,038 for the 2017-2018 Contract Year at KEPCo's expense.²³ KEPCo also maintains that, to the extent the Commission finds that a change to the GFR is needed, the Commission should order refunds as of January 1, 2018.²⁴

13. With regard to its allegation that Westar inappropriately included in the 2018 Annual Update a payment of \$551,614.89 related to the settlement of a \$2 million personal injury lawsuit, KEPCo asserts that despite requesting a detailed description of this item, Westar answered only that "[t]his amount was a payment to settle a personal injury lawsuit that was filed against Westar," but provided no information about the lawsuit that would be needed for KEPCo to determine whether the expense is properly includable in the GFR. KEPCo asks that the Commission order Westar to recalculate the GFR to exclude this settlement payment in the 2018 Annual Update and direct Westar to provide refunds with interest.²⁵

III. Notice of Filing and Responsive Pleadings

14. Notice of the Formal Challenge and Complaint was published in the *Federal Register*, 83 Fed. Reg. 60,836 (2018), with interventions and protests due on or before December 6, 2018. On November 21, 2018, Westar filed a motion requesting a 14-day extension of time to submit its answer and on December 3, 2018, the Commission's Secretary issued a notice extending the comment period to and including December 20, 2018.

²² *Id.* at 12-13.

²³ *Id.* at 13-14.

²⁴ *Id.* at 14-15.

²⁵ *Id.* at 16.

15. The Kansas Corporation Commission filed a notice of intervention. FreeState Electric Cooperative filed a timely motion to intervene. Kansas Municipal Energy Agency (KMEA) filed a timely motion to intervene and comments, and Doniphan Electric Cooperative and Nemaha-Marshall Electric Cooperative (together, the Cooperatives) jointly filed a timely motion to intervene and comments.

16. On December 20, 2018, Westar filed its answer to the Formal Challenge and Complaint. On January 4, 2019, KEPCo filed an answer to Westar's answer, and on January 22, 2019, Westar filed an answer to KEPCo's answer.

A. Westar Answer

17. Westar maintains that KEPCo is incorrect that Westar has violated the GFR and that its argument is an impermissible collateral attack on the settlement that established the parties' contract. Westar states that, in that settlement, it provided a populated example of the GFR that makes clear the GFR relies on tax rates from the previous calendar year. Westar further argues that to the extent KEPCo seeks to modify the GFR, its request should be denied because KEPCo fails to distinguish the Commission's conclusion, made one day before KEPCo filed its Complaint, that a virtually identical historical formula rate need not be modified.²⁶ Westar also asserts that KEPCo fails to allege, let alone demonstrate, how the GFR as a whole is unjust and unreasonable.²⁷

18. Westar points out that KEPCo's witness recognizes in his affidavit that Westar's GFR utilizes a "Historical Test Year approach with no true-up mechanism," and that the witness further explains in his affidavit that "Westar's Rate Year under the GFR runs from June 1 to May 31, and is generally based on costs from the prior calendar year. For example, the 2016 GFR Annual Update was...based on 2015 cost...and the resulting rate was in effect June 1, 2016 to May 31, 2017."²⁸ Westar argues that the Commission, in an order discussing a contract between Westar and City of Arma, Kansas that uses the same formula rate template as that in the contract between Westar and KEPCo, similarly recognized that this is how the GFR operates: "Under the formula, the Demand Charge and two of the three components of the Energy Charge (Variable Operation and Maintenance, and Off-System Sales Margin) will change each June 1 based on cost data

²⁶ Westar Answer at 21 (citing *UNS Electric, Inc.*, 165 FERC ¶ 61,093 (2018) (*UNS Electric*)).

²⁷ *Id.* at 2.

²⁸ *Id.* at 4 (citing Myers Affidavit at P 4).

from the prior calendar year.”²⁹ Westar also asserts that KEPCo’s Complaint recognizes that the allowance for Westar’s federal corporate income taxes is a component of the Demand Related O&M Expenses component of the Westar GFR; or in other words, is part of the Variable Operations and Maintenance component of the Energy charge, and therefore is a component that “changes each June 1 based on cost date from the prior calendar year.”³⁰ Westar further states that the Commission accepted the proposed rate and found that it relies on established cost-of-service principles, a statement to which Westar maintains KEPCo concurred.

19. Westar further states that, as part of the settlement agreement, Westar included a populated GFR for rates on and after June 1, 2008 to demonstrate how the proposed GFR would operate for the 2008 rate year. Westar adds that, in the income tax section of the populated GFR, for purposes of the “Current Income Tax Calculation,” Westar relied on a federal corporate income tax rate of 35 percent and a state corporate income tax rate of 7.35 percent, which reflect the tax rates in effect at the end of calendar year 2007, consistent with the other entries in the GFR. Westar states that use of a 2007 tax rate for the 2008 Rate Year was also supported by the fact that it used the state corporate income tax rate of 7.35 percent in this same GFR, which was the 2007 rate, and not the 2008 rate, which was 7.1 percent. Westar further states that every year since service under the contract began, Westar has inputted the tax rate, both state and federal, in effect at the end of the previous calendar year to the rate year in question, and that this was the case even for years in which the state corporate tax rate decreased, which happened in three subsequent years. Finally, Westar contends that KEPCo has never contested this application of the formula.³¹

20. To answer KEPCo’s arguments directly, Westar responds in two parts. First, Westar states that it did not violate the filed rate in either the 2017-2018 Contract Year or the 2018-2019 Contract Year. Westar argues that KEPCo’s argument—that the GFR does not rely on historical tax costs, including tax rates, to derive charges for a given year—amounts to a collateral attack on the settlement agreement the parties entered into and to the order the Commission issued approving the GFR, and further, has no substantive merit because it is at odds with the plain language of the filed rate and would contravene Commission policy. Westar maintains that, as a collateral attack, KEPCo’s

²⁹ *Id.* at 5 (citing *Westar Energy, Inc.*, 129 FERC ¶ 61,128, at P 5 (2009) (*Westar*)).

³⁰ *Id.*

³¹ *Id.* at 6-7.

filed rate argument can be resolved summarily and raises no issue of material fact.³² Westar further maintains that, putting aside that KEPCo is foreclosed from making its argument, the term “year end” as used in the GFR consistently refers to the previous calendar year, consistent with Commission precedent. Westar states that KEPCo claims that the GFR’s reference to “the federal income tax rate at year end” means the end of the “Contract Year” (i.e., May 31), and not the end of a calendar year (i.e., December 31).³³ Westar contests this argument by pointing out that in the title heading of Item 4 of the GFR, the formula rate for the 2018 Annual Update specifically notes that the calculation is “[f]or Contract Year Beginning June 1, 2018, Based on 2017 Data.”³⁴ Westar states that, were KEPCo’s interpretation correct, the tax rates input into Item 4 would not be based on 2017 data, but on 2018 data. Westar further argues that, although KEPCo is correct that “year end” is not a defined term under the contract, in every other instance where the term is used in the GFR, it refers to the calendar year end, and accordingly, that the use of the same term signified an intent to use it consistently. Westar also argues that giving credence to KEPCo’s argument would contravene Commission policy, which disallows selective changes to formula rate inputs.³⁵ Westar also argues that KEPCo’s argument also ignores the Commission’s prior interpretation of the contract,³⁶ and the consistent course of conduct taken by both parties in applying the GFR. Westar states that, in every year charges under the GFR have been assessed, it has relied on the tax rates in effect for the prior calendar year, even when income tax rates changed.³⁷

21. Westar also contends that KEPCo’s arguments concerning the 2017-2018 Contract Year are without merit, as (1) to the extent KEPCo wished to challenge charges to be assessed in the 2017-2018 Contract Year, it was required to do so by November 2017, pursuant to the Protocols, and its action is now untimely;³⁸ (2) KEPCo’s argument that the GFR contained a mistake that needed fixing finds no support in the contract as

³² *Id.* at 9-12.

³³ *Id.* at 12 (citing KEPCo Complaint at 11-12).

³⁴ *Id.* at 13 (citing Attachment B to the Answer).

³⁵ *Id.* at 13-14.

³⁶ *Id.* at 14 (citing *Westar*, 129 FERC ¶ 61,128 at P 5).

³⁷ *Id.* at 16.

³⁸ *Id.*

Westar's reliance on historical data was intentional;³⁹ and (3) KEPCo's requested relief is barred by the doctrine against retroactive ratemaking.⁴⁰

22. Westar further contends that KEPCo's general citations to FPA section 309 do nothing to advance its case because, although it is true that FPA section 309 can give the Commission authority to order refunds if it finds violations of the filed tariff, no such violations have occurred here.⁴¹

23. Second, Westar argues that, to the extent KEPCo wishes to modify the GFR, it has failed to meet its section 206 burden.⁴² Westar states that KEPCo fails to distinguish *UNS Electric*, which the Commission issued one day before KEPCO filed its Complaint, and that terminated a section 206 investigation into a formula rate with the same historical year construct as the GFR.⁴³ Westar states that KEPCo has also failed to demonstrate how a historical formula rate is unjust and unreasonable as a whole. Westar reasons that lag in recovery of actual Westar cost components might hurt KEPCo in a year where such cost components later decreased, but help KEPCo where other cost components later increased, and that focusing on a single cost component, as KEPCo urges, does not demonstrate that the charges determined under the GFR, are unjust and unreasonable over the life of the contract, or how its proposal to would be just and reasonable.⁴⁴ Westar also states that KEPCo ignores the law in arguing that a possible refund effective date could be January 1, 2018, as under section 206, the Commission may not order refunds for any period prior to the filing of the Complaint.⁴⁵

24. Concerning KEPCO's argument that Westar improperly included costs associated with the settlement of a personal injury lawsuit, Westar provides further information explaining the \$551,614.89 amount that it included in FERC Account No. 925 ("Injuries

³⁹ *Id.* at 17.

⁴⁰ *Id.* at 17-18.

⁴¹ *Id.* at 19-20.

⁴² *Id.* at 20.

⁴³ *Id.* at 21-23.

⁴⁴ *Id.* at 23.

⁴⁵ *Id.* at 27.

and Damages”). In addition, Westar explains why it believes it was appropriate to recover those costs through the GFR.⁴⁶

B. Comments in Support

25. KMEA and the Cooperatives support KEPCo’s Complaint. KMEA contends that shortly after the federal corporate income tax rate went into effect on January 1, 2018, the Commission announced a clear and unambiguous expectation that all cost-based jurisdictional rates reflect the lower tax rate so that customers could begin receiving the benefit of the lower tax rate as soon as possible.⁴⁷

26. KMEA contends that although the Tax Show Cause Orders were issued to jurisdictional entities with cost-based transmission rates on file, it would be folly to suggest that the Commission’s expectation was limited to transmission rates, and that it was unintentional that the Commission did not also issue an order to show cause to jurisdictional entities with cost-based power supply rates.⁴⁸ KMEA states that KEPCo correctly explains that the federal corporate income tax rate is among the inputs in the GFR that are to be adjusted annually, yet it intentionally included the higher 35 percent tax rate in the most recent annual update. KMEA argues that this is inconsistent with the GFR, which only allows Westar to recover “current income taxes.”⁴⁹

27. KMEA supports KEPCo’s argument that Westar overstated its federal income tax expense from January 1, 2018 to May 31, 2018, and that the GFR allows for correction to the rates where an input to the formula is found to be incorrect.⁵⁰ The Cooperatives also support KEPCo’s arguments that Westar improperly calculated the federal income tax expense when populating the 2018 Annual Update. The Cooperatives contend that Westar’s use of the 35 percent federal corporate income tax rate will result in overstated tax expense and provide a permanent windfall to Westar, since the GFR does not include a true-up mechanism.⁵¹

⁴⁶ *Id.* at 27-30.

⁴⁷ KMEA Comments at 3.

⁴⁸ *Id.*

⁴⁹ *Id.* at 3-4.

⁵⁰ *Id.* at 4 (citing Complaint at 9).

⁵¹ Cooperatives Comments at 4.

28. KMEA argues that when Westar performed its annual rate update for June 1, 2018, it should have also calculated its over-collection of charges for the period of January 1, 2018, through May 31, 2018, as a result of the incorrect inclusion of the 35 percent tax rate for that period, and it should have refunded those over-collections to its GFR customers.⁵² The Cooperatives agree that Westar should have corrected its use of the 35 percent tax rate for the time period from January 1, 2018 through May 31, 2018, and recalculated the 2017 GFR charges to account for the reduction of the tax rate as of January 1, 2018 to 21 percent. The Cooperatives also agree with KEPCo that Westar should have used the 21 percent tax rate when populating the GFR for the 2018-2019 Contract Year so as not to impose charges on KEPCo based on the incorrect tax rate of 35 percent.⁵³ The Cooperatives state that although Westar has taken the position that the income tax allowance component of the GFR is based on historical costs, that position is inconsistent with other provisions of the GFR regarding the federal income corporate tax rate, and agree that only KEPCo's interpretation achieves the GFR's stated purpose of recovering Westar's actual cost of providing service.⁵⁴

29. The Cooperatives also support KEPCo's request that if the Commission does not agree with KEPCo's interpretation of the GFR, the Commission should act under section 206 of the FPA and require those changes to the GFR necessary to ensure that the federal corporate income tax rate reduction is reflected in the rates produced by the GFR, and establish a refund effective date as of January 1, 2018.⁵⁵

30. Finally, KMEA and the Cooperatives also supports KEPCo's assertion that Westar improperly included the cost of a settlement related to a personal injury lawsuit in FERC Account No. 925 ("Injuries and Damages").⁵⁶

C. Subsequent Answers

31. In response to Westar's argument that KEPCo's challenge is a collateral attack on the settlement agreement that produced the GFR, KEPCo asserts that it seeks relief from an erroneous application of the formula by Westar; and that it is actually seeking to enforce the GFR's terms. KEPCo states that there is no settled practice between the parties regarding how changes to the federal corporate income tax rate should be

⁵² KMEA Comments at 4.

⁵³ Cooperatives Comment at 4-5.

⁵⁴ *Id.* at 5.

⁵⁵ *Id.*

⁵⁶ KMEA Comments at 4-5; Cooperative Comments at n.3.

reflected in the GFR, as this is the first time the federal corporate income tax rate has changed since the GFR was filed with the Commission, and that Westar's reliance on the fact that neither party took issue with Westar's use of a higher tax rate for the formula rate after the Kansas state income tax rate decreased is misplaced. KEPCo points out that Westar fails to tell the Commission that the Kansas state income tax rate that fell from 7.35 percent to 7.1 percent changed on and after July 1, 2008, and that the GFR was populated showing how rates would have been calculated on June 1, 2008, when the 7.35 percent state tax rate was still in effect. KEPCo argues that, with regard to the state tax rate decreases in 2009 and 2011, Westar offers no evidence to show that it calculated rates based on the higher tax rate in effect in the prior year, and that even if Westar is correct, such a miniscule change would not necessarily have produced a noticeable change in the overall rate, and thus, these later instances of a lowered tax rate also fail to show any evidence of a settled practice between the parties.⁵⁷

32. KEPCo also states that Westar errs in assuming that the tax component of the GFR is a historical cost and that, as explained in the Complaint, the tax component is not designed to recover Westar's tax expense during the prior year but is a calculation performed as part of each annual update designed to recover what Westar's tax liability will be during the effective rate period. KEPCo maintains this is evident from the fact that the tax expense component is calculated during the annual update based on the expected return as calculated for the upcoming rate year,⁵⁸ and that, if the tax expense component were a historical cost, it would not need to be calculated but simply be drawn directly from historical tax returns. KEPCo further argues that, although there are other components of the GFR that are based on historical costs, the GFR, being based on the "Current Tax Rate," is not one such component.⁵⁹ KEPCo claims that its requested relief is not barred by the doctrine against retroactive ratemaking and is consistent with the Commission's statutory authority because the federal income tax component of the GFR is not a fixed component determined by the GFR, but rather a data point; and that as the value Westar entered was a "mistake" under the meaning of that term in the Protocols, KEPCo's requested relief is not prohibited by the rule against retroactive ratemaking.⁶⁰

⁵⁷ KEPCo Reply at 5.

⁵⁸ *Id.* at 6 (citing Attachment D, GFR, at Item 4, n.7).

⁵⁹ *Id.* at 7.

⁶⁰ *Id.* at 8.

33. KEPCo also maintains that the Commission's order in *UNS Electric*⁶¹ has no bearing on the outcome of this proceeding because the order's only finding pertained to the Commission's conclusion that UNS Electric, because it does not have a stated federal income tax line item, should not have been subject to the Formula Rates Show Cause Order. KEPCo states that the Commission made no findings relevant to the misapplication of a formula rate, like the GFR that includes a separate line item requiring the use of the currently effective federal corporate income tax rate.⁶²

34. KEPCo also states that it has met its section 206 burden, as there is ample evidence in the record to support the finding that the existing rates are unjust and unreasonable. KEPCo adds that Westar's argument that KEPCo has failed to demonstrate that the GFR is unjust and unreasonable over its life, or as a whole, is not relevant for an annually adjusting formula rate designed to recover the utility's actual cost of providing service.⁶³

35. Finally, with regard to the settlement of a personal injury lawsuit, KEPCo states that it has reviewed the materials provided by Westar in its answer and is satisfied that the expenses are properly recovered under the GFR, and it therefore withdraws its challenge to the inclusion of these expenses.⁶⁴

36. In its response to KEPCo's reply, Westar contends that the Commission's recent decision in *NCEMC v. Duke Energy Progress, LLC* removes any doubt that the complaint in this case should be denied, as in that case, the Commission denied a substantially identical formal challenge and complaint, stating that the Commission

generally requires that formula rate inputs be calculated on a synchronized basis over the same test period, such that [a utility's] use of a historical formula rate methodology generally dictates that [the utility] use the federal corporate income tax rate in effect during the historical test year period, absent a contrary statement in the filed rate.⁶⁵

⁶¹ *UNS Electric*, 165 FERC ¶ 61,093.

⁶² KEPCo Reply at 10.

⁶³ *Id.* at 11.

⁶⁴ *Id.* at 12.

⁶⁵ Westar Reply at 1 (citing *N. Carolina Elec. Membership Corp. v. Duke Energy Progress, LLC*, 166 FERC ¶ 61,026, at P 44 (2019) (*NCEMC*)).

Westar contends that, as no such contrary statement exists in Westar's GFR, and, in fact, because the GFR explicitly states that the tax rate to be used is the one in effect at the end of the prior calendar year, the Complaint should be denied.

37. Westar contends that KEPCo's Complaint substantively mirrors the complaint evaluated in *NCEMC* and contends that none of KEPCo's reply arguments warrant a different result.⁶⁶ Westar disagrees with KEPCo's argument that because Westar's tax liability is "calculated as a function of 'Current Income Taxes' multiplied by the Company's 'Return,'" the term "Current Income Tax" must mean the tax rate currently in effect. Westar asserts that the Commission rejected this argument in *NCEMC* and, in any event, KEPCo ignores that the GFR specifically defines "Current Income Taxes," to include, in part, the "FIT (Federal Income Tax Rate) as of year end," which means the prior calendar year end. Westar also points out that, although KEPCo states once, without citation, that the GFR is required to be based on the "Current Tax Rate," the phrase "Current Tax Rate" does not even appear in the GFR.⁶⁷ Westar further contends that KEPCo is unable to satisfy the Commission's finding in *NCEMC* that "formula rates must clearly state the source of each input that differs from the general formula rate methodology used,"⁶⁸ because if the tax rate was supposed to be the rate in effect for the upcoming contract year, the formula would have indicated so. In fact, Westar contends, the GFR indicates the opposite: the tax rate to be used is the "FIT (Federal Tax Rate) as of year end."

38. Westar maintains that KEPCo's "mistake" argument also fails because substituting a new tax rate that would not be the "FIT as of year end" would be contrary to the formula and violate the terms of the filed rate.

39. Finally, Westar urges that as the Commission did in *NCEMC*, the Commission should deny KEPCo's request for relief under section 206 of the FPA. Westar argues that KEPCo's argument relies solely on the point that KEPCo's charges will be higher than if the GFR is applied as written. Westar asserts that merely arguing that a higher tax rate causes higher charges inappropriately ignores all the other inputs into the formula rate that are based on historical data.⁶⁹

⁶⁶ *Id.* at 2-3.

⁶⁷ *Id.* at 4 (citing KEPCo Reply at 7).

⁶⁸ *Id.* (citing *NCEMC*, 166 FERC ¶ 61,026 at P 45).

⁶⁹ *Id.* at 5.

IV. Commission Determination

A. Procedural Matters

40. Pursuant to Rule 214 of the Commission's Rules of Practice and Procedure,⁷⁰ the notice of intervention and timely, unopposed motions to intervene serve to make the entities that filed them parties to this proceeding.

41. Rule 213(a)(2) of the Commission's Rules of Practice and Procedure prohibits an answer to an answer unless otherwise ordered by the decisional authority.⁷¹ We will accept Westar's and KEPCo's answers because they have provided information that assisted us in our decision-making process.

B. Substantive Matters

42. We deny KEPCo's Formal Challenge and Complaint. It is clear that the GFR uses a historical test year without a true-up based on actual costs.⁷² We find that Westar correctly applied its historical test year methodology in the 2018 Annual Update. Accordingly, Westar correctly applied a 35 percent federal corporate income tax rate in the calculation of the GFR for the period from January 1, 2018 through May 31, 2018, and for the period from June 1, 2018 through May 31, 2019. The 2018 Annual Update was properly based on 2017 costs, including the 35 percent federal corporate income tax rate in effect in 2017; the reduction in the federal corporate income tax rate did not take effect until January 1, 2018.

43. Our reasoning is similar to the Commission's recent decision in *NCEMC*, which addressed analogous facts. There, Duke Energy Progress, LLC (DEP) also had a cost-based tariff that follows a historical test year methodology and applied the 35 percent tax rate in its 2018 Annual Update. The Commission dismissed the complaint of a wholesale transmission customer seeking the application of a lower federal corporate income tax

⁷⁰ 18 C.F.R. § 385.214 (2018).

⁷¹ 18 C.F.R. § 385.213(a)(2) (2018).

⁷² See KEPCo Complaint, Attachment A (Myers Affidavit) at 3 (stating that "Westar's GFR . . . utilizes an Historical Test Year approach with no true-up mechanism. As a general matter, the Historical Test Year approach is based on historical costs that are deemed to be a reasonable proxy for the utility's costs during the service/rate year.").

rate because the Commission found that the utility “correctly used the federal corporate income tax rate in effect in 2017 in preparing the 2018 Annual Update.”⁷³

44. As the Commission stated in *NCEMC*,

[t]he Commission generally requires that formula rate inputs be calculated on a synchronized basis over the same test period, such that DEP’s use of a historical formula rate methodology generally dictates that DEP use the federal corporate income tax rate in effect during the historical test year period, absent a contrary statement in the filed rate.⁷⁴

No such contrary statement exists in Westar’s GFR. In addition, this synchronization requirement, and the Commission’s related reluctance to permit selective post-test period adjustments,⁷⁵ protects both utilities and their customers by preventing either from selectively choosing which inputs should come from which time period to one party’s exclusive benefit.⁷⁶

⁷³ *NCEMC*, 166 FERC ¶ 61,026 at P 43.

⁷⁴ *NCEMC*, 166 FERC ¶ 61,026 at P 44 (citing *Ameren Ill. Co.*, 163 FERC ¶ 61,200 at P 4 (citations omitted) (noting “the Commission’s requirement that all rate base components and expenses in rates be calculated on a synchronized basis over the same test period”); *Westar Energy, Inc.*, 122 FERC ¶ 61,268, at P 98 (2008) (citations omitted) (“Under Commission policy, companies must use a fully-synchronized test period cost-of-service study that uses either an historical test period or a projected test period.”); *Metropolitan Edison Co.*, 44 FERC ¶ 61,053, at 61,146 (1988) (“Under Commission ratemaking procedures for developing wholesale cost of service, all test year expenses and revenues, including an allowance for income taxes associated with such revenues, are synchronized.”).

⁷⁵ *E.g.*, *Alamito Co.*, 39 FERC ¶ 61,231, at 61,812 (refusing to require utility to reflect lowered federal corporate income tax rate in its formula rate during the rate year and accepting use of blended rate until beginning of the next rate year), *order on reh’g and clarification*, 41 FERC ¶ 61,312 (1987); *Pub. Serv. Co. of N.M.*, Opinion No. 73, 10 FERC ¶ 61,053, at 61,121-23 (1980) (concluding that it is not proper to adjust the test period cost-of-service data in a cost-of-service rate proceeding to reflect post-test year changes in the federal corporate income tax rates).

⁷⁶ *See Idaho Power Co.*, 153 FERC ¶ 61,212, at P 33 (2015) (“Allowing Idaho Power to continue to use a historic formula rate methodology for recovering all its other expenses, with the certainty and protections that provides to Idaho Power, while allowing

45. KEPCo argues that the tax component of the GFR is an exception to the historical test year approach, yet provides no support other than to state that the “federal corporate income tax allowance in the GFR is a function of the return on rate base and tax rate calculated for the coming rate year; it is not a function of tax expense paid in the prior year.”⁷⁷ We disagree with KEPCo’s argument that the tax component is an exception to the historical test year approach. As described above, unless the formula rate provides otherwise, the Commission generally requires synchronization of formula rate inputs, meaning that the lack of an explicit requirement in Westar’s GFR one way or the other on the correct federal corporate income tax rate favors use of the prior year rate, consistent with the historical test year methodology. This is particularly important where the formula rate at issue was the product of a negotiated settlement between the utility and its customers, as in the case with Westar’s GFR.⁷⁸

46. Further, Westar refutes KEPCo’s claim that the use of the 35 percent tax rate was a mistake. Westar states that it intentionally used the 35 percent tax rate,⁷⁹ which we find, as discussed above, is consistent with the historical test year methodology. In addition, we disagree with KEPCo’s argument that the GFR’s reference to “the federal income tax rate at year end” means the end of the Contract Year. While “year end” is not a defined term, we find that it refers to the calendar year end, not the Contract Year end. Not only does the 2018 Annual Update state that the calculation is “[f]or Contract Year Beginning June 1, 2018, Based on 2017 Data,” but, as described above, the GFR is a historical formula rate based on the prior year’s costs.⁸⁰

47. Finally, because KEPCo withdrew its challenge to Westar’s inclusion of certain expenses in the Injuries and Damages account, we need not address that issue.⁸¹

it to deviate from the prescribed methodology in this one instance would favor Idaho Power’s interests over that of its customers.”).

⁷⁷ KEPCo Complaint at 7.

⁷⁸ See *Westar Energy, Inc.*, 128 FERC ¶ 61,174.

⁷⁹ Westar Answer at 17.

⁸⁰ See also *Westar*, 129 FERC ¶ 61,128 at P 5 (the Commission found that “year end” means the prior calendar year).

⁸¹ See Westar Answer at 27-30 (providing further information related to the expenses); KEPCo Reply at 12 (withdrawing its challenge to the inclusion of the expenses).

The Commission orders:

The Formal Challenge and Complaint is hereby denied, as discussed in the body of this order.

By the Commission.

(S E A L)

Nathaniel J. Davis, Sr.,
Deputy Secretary.