Written Testimony of John D. Quackenbush, CFA

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For the Kansas House Committee on Energy, Utilities and Telecommunications

Support for HB2527

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Chair Delperdang and members of the Committee:

I respectfully offer the following comments based on my past experiences as the Chairman of the Michigan Public Service Commission, Managing Director and Senior Investment Analyst at UBS Global Asset Management, Chief Financial Analyst of the Illinois Commerce Commission, and Manager, Capital Markets for Sprint Corporation.

I support HB2527's use of an actual capital structure for large public utilities that hold an investment grade credit rating. Capital structure is an important issue and regulatory best practice is to use a utility's actual capital as long as it has a direct interface with the capital markets. Clearly, HB2527's reference to an investment grade credit rating ensures that the utility has a direct interface with the capital markets by issuing its own debt on a stand-alone basis.

This best practice is described in the National Association of Regulatory Utility Commissioners (NARUC) "A Cost of Capital and Capital Markets Primer for Utility Regulators" that I authored in 2019. NARUC is a non-profit organization dedicated to representing state public service commissions that regulate the utilities that provide essential services. On pages 11-12, the Primer indicates:

> "The capital structure is typically measured at the corporate level at which the utility actually interfaces with the capital markets. Some utilities participate directly in the capital market and have a capital structure disciplined by the capital markets. Actual capital structure ratios are generally used for a utility that has market-traded stock and/or debt directly issued to investors."

Hypothetical or parent capital structures should be a last resort only when a utility does not have market-traded debt. Artificially imposing a hypothetical or parent capital structure, as recommended by KCC staff in Evergy's recent rate case, Docket No. 23-EKCE-775-RTS, is highly unusual, not a best practice, is just another way to create regulatory lag, ensure that the utility will earn a return below the authorized return, and is contrary to the public interest because it imposes additional costs on customers in the long-run.

During my time at the Illinois Commerce Commission and the Michigan Public Service Commission, I was diligent about using the utility's actual capital structure for ratemaking in order to avoid creating the perception that Illinois and Michigan were hostile to investment dollars that contribute to economic development. If Kansas chooses to deviate from this best practice, it would be an outlier among North American regulatory jurisdictions.

Investors have a fiduciary duty to make investments in jurisdictions with reasonable regulatory treatment. Likewise, utility management has an incentive and a duty to allocate capital where it is treated fairly. My concern is that potential punitive decisions of the KCC, such as deviating from the use of actual capital structures, demonstrate to investors that their investment dollars are not welcome in the state of Kansas. The KCC is already widely recognized by investors as well below average compared to other state jurisdiction and recent rankings place the KCC as among the three least supportive regulatory environments in the United States.

The NARUC Primer indicates on page 9:

> "Customers benefit by having a financially stable utility that has the earnings and cash flow sufficient to attract equity and debt on reasonable terms, and the resulting ability to provide safe, reliable, and affordable utility service. Receiving a reasonable authorized ROE and capital structure from regulators is an important contributor to financial stability. The customer benefits that result from being served by a financially healthy utility outweigh the illusory short-term "benefits" of a negative regulatory climate that heightens regulatory risk."

In my opinion, it is best that Kansas not chase short-term illusory "benefits" that only harm customers in the long-run and ironically provide a disincentive to invest in Kansas at a time of significant economic development opportunity.

In that regard, HB2527 will enhance Kansas' reputation in the investment community, provide long-term benefits to customers, and enhance economic development.

ABOUT JQ RESOURCES, LLC

JQ Resources, LLC assists clients with utility regulatory matters, provides strategic advice, and researches and communicates complex regulatory issues while bridging the gap between the regulatory and investment communities. Its President, John D. Quackenbush, CFA, offers a unique balanced combination of state regulatory leadership, investment sector knowledge, and financial experience in transitional industries. John has served as Chairman of the Michigan Public Service Commission, Chief Financial Analyst at the Illinois Commerce Commission, and Managing Director and Senior Financial Analyst at UBS Global Asset Management, as well as in several management positions in the telecommunications industry.

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