

KANSAS ELECTRIC POWER COOPERATIVE, INC.

NEWSMAKER

A Touchstone Energy® Cooperative 

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President's Remarks from the KEPCo Annual Meeting

BY KIRK THOMPSON
President, KEPCo Board of Trustees

Friends, colleagues, and guests, welcome to KEPCo's 38th Annual Meeting. Thank you for attending tonight and taking the time to participate in the business of your power supply cooperative.

This past year, it seemed that every week some sort of negative economic news was being reported. Whether it was high unemployment, lower-than-expected GDP, rising gasoline prices, devastating drought, or declining home values, the nation was searching for ways to stretch a dollar and wondering where the next dollar would come from. Well, I think it's time we hear some good news.

First, as many utilities around the nation struggle to procure adequate and economic base load generation, balanced with the appropriate type and amount of renewable generation, KEPCo has invested in and secured a safe, reliable, economic, and Kansas Renewable Energy Standard compliant power supply. KEPCo's power supply includes nuclear, through its six percent ownership of Wolf Creek, 114 MW of hydroelectric, which KEPCo recently executed an extension of its SWPA contract until 2031, 30 MW of coal-fired generation through its ownership of Iatan 2, and purchase power agreements with local utilities, most notably Westar Energy, which includes a combination of coal, natu-

ral gas, nuclear, and wind. Nearly 50% of KEPCo's power supply does not emit any greenhouse gas. As the regulation of carbon and other fossil fuel emissions remain unclear, half of KEPCo's power supply remains shielded from the economic impact of enhanced carbon regulation.

Second, KEPCo's financial position has steadily improved. Over the past five years, KEPCo's equity has risen by 18% and KEPCo is projected to reach 20% equity by the end of 2013. In addition to an improving bottom line, KEPCo also has access to capital with interest rates 300 basis points less than other available capital. Lower interest rates translate to lower wholesale electric rates for KEPCo's Member Cooperatives. Further enhancing KEPCo's financial

position has been the establishment of a \$20 million line-of-credit with CFC and a \$10 million line-of-credit with CoBank. The lines of credit increase financing flexibility and the availability of capital to KEPCo.

Third, KEPCo continues to grow. Electricity is the lifeblood of the U.S. economy. It powers our homes, offices, and industries; provides communications, entertainment, and medical services; powers computers, technology, and the Internet; and runs various forms of transportation. Today, the average U.S. home has more televisions than people in the home. Since 2007, KEPCo's energy sales have increased 15% and peak demand by 12%. Growth allows KEPCo to continue to operate profitably and meet all financial requirements from Rural Utilities Service and other lenders.

In addition to what could be termed "traditional growth," parts of the state are starting to experience non-traditional growth, in the form of

(continued on page 2)

2012-2013

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President's Remarks

(continued from page 1)

the oil boom. Oil companies are preparing to explore for oil and natural gas, and some in fact have already started drilling. A few of our Member Cooperatives are anticipating energy demand on their system to increase by as much as 20%, in a very short period of time, attributable to the oil boom. This type of accelerated growth poses challenges, but they are challenges we are eager and able to meet.

And fourth, electric utilities in 43 states are proceeding with plans to install smart meters. U.S. utilities have installed 16 million meters in pilot programs and full-scale rollouts. Research from the Institute for Electric Efficiency indicates that some 65 million new meters will be deployed nationwide by 2020—about half of U.S. homes. In October, Kansas State University had a ribbon-cutting ceremony on a new laboratory dedicated to performing research on smart grid technology.

KEPCo Member Cooperatives are not following suit, but rather are leading the way on smart meter deployment. A vast majority of KEPCo Member Cooperatives have either installed, or are in the process of installing, smart meters. Smart meters have the potential to substantially change the electric utility industry. Potential benefits include customer access to energy usage information, energy management, enhanced outage notification and restoration, and “on-peak” price signals, to name a few.

Although positioned formidably, KEPCo, and the electric utility industry in general, still face many challenges. Foremost is utility regulation. Utility regulation in its present form remains cumbersome and expensive, and has mired the industry with uncertainty. Rational regulation based on scientific and economic facts and greater reliance on cost-benefit

analysis, along with risk versus risk analysis, should replace the current philosophy of regulation drives policy. Utilities cannot make decisions on critical infrastructure investments designed to last for decades based on rules that may or may not apply for more than a Congressional term.

The path forward is clear. We need all forms of energy. Just like a toolbox in anyone's garage, different tools are needed for different tasks. While wind, solar and other renewables are important, there is little doubt that the U.S. economy is powered by fossil fuels. Moreover, until technology and renewables can actually produce significant amounts of energy, this nation must, and will

continue to depend on fossil fuels for many decades. Further complicating the push for renewables is the fact that advances in technology have opened vast new resources of oil, natural gas and coal. Once thought to be running out of these fossil fuels, the United States has seen an energy renaissance unimaginable only a few short years ago. With an abundant supply of coal, natural gas, and yes, oil, energy independence is in fact attainable. This, coupled with exponential job growth in energy states such as North Dakota, Oklahoma, Arkansas, Texas, and soon-to-be Kansas, are facts that cannot be dismissed for the sake of a “green economy” that has yet to materialize.

KEPCo Hires Chief Administrative Officer

William J. Riggins has been hired by Kansas Electric Power Cooperative, Inc. (KEPCo) as Senior Vice President and Chief Administrative Officer. Mr. Riggins most recently was with the law firm of Husch Blackwell. Prior to this, Mr. Riggins was General Counsel and Chief Legal Officer with Kansas City Power & Light and Great Plains Energy. As Senior Vice President and Chief Administrative Officer, Mr. Riggins will act as general counsel and be responsible for all legal and administrative functions of KEPCo. Mr. Riggins has over 27 years of experience in the electric utility industry.

Mr. Riggins received his undergraduate degree and juris doctorate degree from the University of Kansas and an MBA from the University of Missouri – Kansas City. Mr. Riggins and his wife, Stacy, reside in Lawrence and have three children.

“William Riggins' vast experience in the utility industry will be an immediate asset to KEPCo and its Member Cooperatives as we deal

with the complexities of power supply and transmission related issues,” said Steve Parr, Executive Vice President and CEO.

Mr. Riggins is replacing the retiring J. Michael Peters. Mr. Peters, KEPCo's Vice President of Administration & General Counsel, began his tenure with KEPCo in 2005 and is retiring on January 2, 2013. “Mike has been a valuable asset to KEPCo, in particular his regulatory expertise. His work ethic and dedication to KEPCo and our Member Cooperatives has been exemplary and I wish him a long and enjoyable retirement,” said Steve Parr.



William J. Riggins



J. Michael Peters

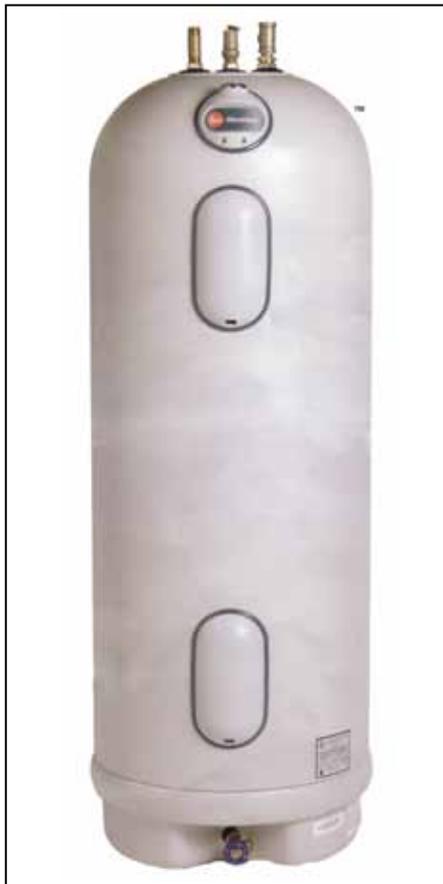
Electric Co-ops Push Back on DOE Water Heater Issues

Electric cooperatives are opposing separate U.S. Department of Energy (DOE) actions regarding electric resistance water heater efficiency standards that, if enacted, will increase costs for consumers and undermine co-op load management programs.

For starters, DOE is considering a proposal—which would be submitted to the International Energy Conservation Code Council as an amendment to model building codes—that would effectively eliminate the use of electric resistance water heaters in new residential and commercial structures and those undergoing significant renovations. Many states and municipalities adopt those codes locally.

Electric cooperatives have emphasized that such a move would force consumers to find other, potentially more expensive options. The result would be significantly higher consumer energy costs, especially for electric co-op members whose only option is installing electric water heaters of some kind. The elimination of electric resistance water heaters would also undermine and eventually eliminate many cooperative demand-response programs, as the electric water heaters that would be permitted by the amended building codes would not be suitable for such programs.

To help keep electric bills affordable, more than 240 co-ops in 21 states are able to interrupt electric service to hundreds of thousands of electric resistance water heaters as well as thousands of air conditioners, electric thermal storage heating cabinets and furnaces, and other specialized equipment in the homes of volunteer consumers for brief stretches, typically just a few hours. Control generally takes place on very cold mornings or hot, humid weekday afternoons during times of peak demand—the electric utility industry's equivalent of rush-hour traffic, when



power costs skyrocket.

As a result, load management efforts essentially work like a power plant in reverse, helping co-ops boost electric system efficiency, reduce expensive demand charges for purchase power, offset the need for building additional power plants and transmission lines, and create the potential to 'store' renewable energy. In 2011, electric co-ops cut 2,200 MW of load, the electric use equivalent of 1.1 million average-sized homes, saving members close to \$100 million in generation fuel costs and offsetting more than 2,000 tons of carbon dioxide emissions.

Unfortunately, because this DOE plan is a "proposed recommendation" to a standards-setting organization, it does not require the same review and approval process as federal regulations. Electric co-ops are pushing to get the DOE recommendation modified, before it is submitted to the

council, to ensure that electric resistance water heaters can continue to be used. If necessary, cooperatives will oppose the proposal at the ICC as well, but it would be better to stop it before it gets to that point.

The second DOE effort, a water heater efficiency standard adopted in 2010 and set to take effect in 2015, would effectively ban large-volume electric resistance water heaters—those with a storage capacity of 55 gallons or more. The rule as written will require all large-capacity water heaters to operate at 200 percent efficiency, a level that only certain heat-pump water heaters can meet.

Electric co-ops are urging DOE to create a new appliance category for grid-connected, large-capacity water heaters. Otherwise, the new efficiency standard would, over time, cripple extremely successful co-op load management and demand-response initiatives that have been built around the appliance.

When co-ops launched pioneering load management efforts in the late 1970s, electric resistance water heaters quickly became the "peak shift" device of choice—water could be heated and stored during periods of low power consumption, such as late night and early morning hours. Thanks to big tanks (commonly 80 gallons or more), the units could be turned off for long stretches without a household being inconvenienced by running out of hot water.

However, the proposed DOE rule will have a negative impact on load control because heat-pump water heaters can't be cycled like electric resistance models and can't heat water to as high a temperature. Also, the high cost of large-volume heat-pump water heaters, in the range of \$2,000 or more, will put them out of reach for many families. At those prices, co-ops won't be able to justify financial incentives sufficient to influence water heater purchasing decisions.

Making Strides with Clean-Coal Technology

Despite the recent “green” energy revolution and the explosion of natural gas drilling rigs across the American landscape, our nation’s primary fuel for producing electricity is coal—as it has been for more than a century.

Electricity in the U.S. generated by coal fell from 42 percent in 2011 to 37.5 percent in 2012, largely because of low natural gas prices, the retirement of older coal-fired power plants due to new emissions regulations from the U.S. Environmental Protection Agency (EPA), and uncertainty about further regulations in the future.

But coal is far from dead. Electricity from coal is predicted to rise about three percent this year while natural gas’s contribution will drop from 30.5 percent to 27.3 percent, according to the U.S. Energy Information Administration’s (EIA) Short-Term Energy Outlook for 2013. And natural gas prices are forecasted to rise this year due to higher demand and a slowdown in production.

“Coal still has a future as a source of electricity,” says Steve Parr, KEPCo Executive Vice President & CEO. “Whether you are for or against the use of coal to generate electricity, the fact is that the United States remains home to the largest reserves of coal in

the world. That’s why electric cooperatives like KEPCo are fully behind efforts to explore and test clean-coal technologies.”

One driver in the effort is EPA’s Mercury and Air Toxics Standards rule, designed to significantly curb emissions of hazardous air pollutants, such as mercury and arsenic, from coal- and oil-fired electric generating units 25 MW or larger by 2016. Some coal-fired generating units will be shut down, rather than retrofitted, because the needed changes would be too expensive to implement.

America’s electric cooperatives and the trade association that represents them, the National Rural Electric Cooperative Association (NRECA), are exploring new approaches to burn coal more cleanly. NRECA’s Cooperative Research Network (CRN) recently completed a demonstration of an innovative new multi-pollutant control system that shows promise for helping coal-fired power plants meet stringent emissions standards advanced by EPA. Even better, the technologies tested do so at a fraction of the cost of traditional measures.

The demonstration, conducted in July 2012 at a power plant owned and operated by Arizona Electric Power Cooperative, a generation and

transmission co-op (G&T) based in Benson, Ariz., was sponsored by CRN along with a coalition of 10 G&Ts and other industry organizations. Results showed that by combining mercury controls—which were successfully tested by CRN in November 2011 at a plant operated by San Miguel Electric Cooperative, a G&T in Jourdan-ton, Texas—with trona (a naturally occurring mineral similar to baking soda), significant emissions reductions were achieved. In addition, the tested technologies cut the cost of meeting new environmental rules by a factor five to 10.

“Results for these full-scale power plants were very encouraging,” notes John Hewa Jr., NRECA vice president of engineering, research & technical services. “But they were based on limited-duration runs. To verify long-term performance, the results need to be confirmed with extended trials.”

“We’re supportive of the multi-pollutant control technologies being studied by CRN because they can show us how to best use one of our most abundant natural resources, coal, and keep rates low for our Members,” Steve Parr concludes. “KEPCo is proud to support innovations that will allow KEPCo to continue to provide safe, affordable, reliable, and environmentally responsible power for our Members.”