



SUNFLOWER ELECTRIC POWER CORPORATION

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Kansas Department of Health and Environment

Statement of Earl Watkins
Concerning the Proposed Kansas Air Quality Construction Permit
Of Sunflower Electric Power Corporation

August 2, 2010

My name is name is Earl Watkins. I am the President and Chief Executive Officer for Sunflower Electric Power Corporation. Sunflower is a not-for-profit generation and transmission company operated cooperatively. Its mission is to provide reliable energy at the lowest possible cost to its members. The purpose of my remarks today is to give you a glimpse of why we have proposed this power plant and why I believe the agency should approve the draft permit under consideration.

I realize the agency's duty is only to concern itself with this specific permit, but as Sunflower's CEO it is my responsibility to manage all our resources for the benefit of our members in a way that is within the bounds of the law. As a result, I have considered not only this specific unit but also the long term implications of this decision.

First, one only has to look at our history to realize that at any given time a specific fuel source might be out of favor for a period of time. But the fact is all fuels have distinctive characteristics that make them suitable for specific projects. My job is to make certain that our generation portfolio is not only diverse but also balanced, and that will always require base load, intermediate and peaking assets.

Before I proceed, let me describe our generation portfolio history. Prior to 1983, our portfolio consisted only of natural gas units. Today, 48% of the capacity of our units is powered by natural gas, while 42% of our capacity is powered by coal. The remaining 10% comes from 325 wind turbines operating at two locations west of Salina on Interstate 70 and in southwest Kansas near Montezuma. We do rely on our coal units at

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Holcomb and at the Jeffrey Energy Center for more energy because they are our most economical base load resources.

As for our renewable assets, in 2007 Sunflower became one of the first utilities in Kansas, along with Midwest Energy, to meet then Gov. Sebelius' goal of 10% wind by 2010. We are also poised to meet the 2020 target of 20% wind that was established by the Kansas Legislature.

We are also actively involved in completing an arrangement to purchase the majority of the electrical output from the nation's first hybrid cellulosic ethanol facility that will be located near Hugoton. This facility will be able to produce 98 megawatts of base load energy in addition to 15 million gallons of cellulosic ethanol annually.

Looking toward the future, Sunflower has joined with a consortium of utilities that are working to advance the development of small, modular nuclear units. These 125 megawatt units will be scalable according to need and are being developed by the nuclear experts at Babcock and Wilcox in conjunction with Bechtel. If a "cookie cutter" unit can be successfully designed, the permitting and construction time will be cut in half.

So why propose coal for this unit? Like all utilities, our system demand requires base load, intermediate and peaking generation resources. This project is designed to meet those base load needs. If you're not familiar with this term, base load refers to the minimum amount of electricity that is demanded daily in a utility's system. These resources are the most capital intensive units, but financially, they are the most affordable resource for this type of demand. Wind and solar technologies, on the other hand, are not dispatchable and therefore not considered base load options.

Base load resources must be fueled using natural gas, coal, nuclear or hydro electric technologies. Hydro isn't a viable option for obvious reasons. Large nuclear plants are terribly expensive, plus they have an estimated 5-year permitting process and 6-year construction cycle, which means huge amounts of capital are tied up for more than 10 years before a traditional unit comes online.

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That leaves coal and natural gas as options for our system. The fuel cost for newer natural gas units averages 5.5 cents per kilowatt hour while coal averages about 1.5 cents per kilowatt hour. Even though the capital cost of a combined cycle natural gas unit is one half of the construction costs of a coal unit, the fuel cost is four times more expensive and volatile. Although the cost of natural gas has decreased to a current level of \$5/mmBtu, our cost for gas was \$13/mmBtu in August of 2008. It dropped to \$3 in February 2009, increased to \$9 in July 2009, and was \$5 on July 25.

Using coal, we can secure 20-year contracts for coal to stabilize prices for our members. Contracts of that nature are simply not available for natural gas. Since we have 48% of our capacity in natural gas, our confidence in that fuel is well demonstrated. However, natural gas is not the right choice for this project.

The Sunflower system is growing. In July we set an all-time hourly peak demand of 1,086 megawatts—an increase of six percent over the 2009 peak. Ironically, part of that growth is due to natural gas producers who have switched their compressors from using natural gas as a fuel to electricity to take advantage of our lower-cost coal generation resources, yet some in that industry may speak at these hearings saying coal should be replaced by natural gas as a generation fuel.

Another major influence on this decision evolves from the fact that Sunflower is going to lose a 173 megawatt purchase power contract with the Jeffrey Energy Center by 2019. In fact, our forecast is that in the next ten years we will require an additional 300 megawatts of base load capacity in our system. Our current plan is to use 85 megawatts from this unit and 98 megawatts from the Abengoa project and then choose from other options later to meet our capacity requirements.

We could build a 200 megawatt unit to meet the needs of the Kansas participants, but it would not be as economically beneficial to our members. This project maximizes the use of our existing assets because Sunflower will receive more than \$400 million from this project from various income streams and cost savings during the next 30 years.

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I also want to help you understand why these decisions are difficult for most utilities. The difficulties we face are caused by what could be described as our irrational national energy policy. The only thing consistent about our national energy policy decisions in recent decades is that it has been very inconsistent.

In 1978 the Powerplant and Industrial Fuels Use Act gave utilities and other manufacturers 11 years to switch from using natural gas as a boiler fuel. This legislation was in response to the 1973 oil crisis when Congress deemed natural gas to be a declining natural resource that needed to be protected for only residential use. That legislation certainly encouraged utilities to use coal or nuclear energy until the legislation was repealed in 1987.

When Sunflower needed additional base load resources in the late 1970s, this act prohibited us from building natural gas generation even though our member service territory covered the Hugoton natural gas field, which was, at the time, the largest natural gas field in North America. Nuclear power was widely promoted until the Three Mile Island incident in 1979, so coal was king until just recently.

In the last five years, natural gas, renewable generation, and energy efficiency have been at the top of the list for advocates trying to change the generation technologies used by utilities.

Decisions related to base load generation generally result in facilities that will operate for 50 years, so we must always make choices that allow us to serve our member's needs in accordance with existing laws and regulations.

In the last few years, the legislature has passed many energy initiatives. One of them included a renewable portfolio standard for most utilities. Sunflower negotiated an agreement with Governor Parkinson that not only meets those legislative requirements, but we agreed to meet them four years early. In addition, we have also agreed to facilitate the construction of renewable facilities equal to 20% of the output of the proposed unit.

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Through this agreement and their previous decisions, our board of directors have agreed to go way beyond what is required of other Kansas utilities in order to bring this new resource and a substantial amount of wind generation to Kansas.

I want to emphasize that this plant will be built using the best available pollution control technology in America. It won't be built with second or third best, but it will be the best as determined over the last 55 years by our state and federal regulatory agencies. I often wonder why this project's opponents aren't satisfied with the best technology. What else could rational people expect us to build?

I also realize that some people are simply opposed to any coal-fired power plant—period. I'm not here to criticize that view. Some say natural gas is the answer. Well, we have natural gas, but many will argue the fuel price is too volatile and therefore harsh on consumers. Some environmentalists are opposed to the fracking technology used to release the shale gas.

Some say nuclear is the answer. Well, we are pursuing that technology but it is years away. And some environmentalists say nuclear is too dangerous because the spent fuel is deadly for thousands of years.

Some will say biomass is the answer. Well, we are pursuing biomass, but it requires substantial taxpayer subsidy to be feasible. Some environmentalists oppose biomass as just recycling CO₂.

Some say wind is the answer. Well, we have wind, but it is only available 40% of the time, and some environmentalists oppose wind because of visual pollution, soil erosion and, they argue, that wind turbines kill birds, bats, and bugs.

The fact is that for our American economy to flourish, I know that we must have rules and regulations that govern how businesses operate in order to protect private property rights and to protect the public's interest. That's why the KDHE exists—to ensure that those of us who are going to have an effect on the environment operate our companies in accordance with those laws and regulations.

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For those who believe in the rule of law, I can't imagine why anyone would not support a \$3 billion project that will result in nearly 2,000 people being hired to build a facility that will create more than 300 permanent jobs for 50 years or more and provide a vital service needed by more than 500,000 people using the best, I repeat, the best available control technology in our nation.

Thank you for this opportunity to speak today. I urge you to promptly proceed with the approval of this draft permit.