



LARRY M. COWGER
Director, Law

December 12, 2002

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Kansas Corporation Commission
/S/ Jeffers

STATE CORPORATION COMMISSION
DEC 12 2002
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Docket Room

J. Michael Peters
Assistant General Counsel
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1500 SW Arrowhead Rd.
Topeka, KS 66604-4027

Re: In the Matter of the Application of Western Resources, Inc. for Approval to Make Certain Changes in its Charges for Electric Services; and In the Matter of the Application of Kansas Gas and Electric Company for Approval to Make Certain Changes in its Charges for Electric Services; Docket No. 01-WSRE-436-RTS

Dear Mr. Peters:

This letter is to inform the parties that there is no information in Staff's Final Report or Recommendation or the November 13, 2002 *Review of Power Marketing and Trading Activities and Procedures at Westar Energy prepared by Navigant Consulting, Inc.* that Westar Energy considers confidential or proprietary. Therefore, the "confidential" designation may be removed.

Sincerely,

Larry M. Cowger

jmm
cc: All Parties

BEFORE THE STATE CORPORATION COMMISSION
OF THE STATE OF KANSAS

STATE CORPORATION COMMISSION

DEC 10 2002

In the Matter of the Application of Western Resources, Inc. for Approval to Make Certain Changes in its Charges for Electric Service)

)Docket No. 01-WSRE-436-RTS

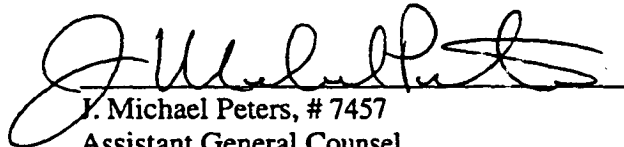
In the Matter of the Application of Kansas Gas and Electric Company for Approval to Make Certain Changes in its Charges for Electric Service)

Jeffery S. Nassan Docket Room

STAFF'S FINAL REPORT AND RECOMMENDATION

Pursuant to the Commission Order of November 7, 2002, Staff submits the attached Memorandum from Larry Holloway and the attached Review of Power Marketing & Trading Activities and Procedures at Westar Energy prepared by Navigant Consulting Inc. for filing.

Respectfully submitted,



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CONFIDENTIAL



Kansas Corporation Commission

Bill Graves, Governor John Wine, Chair Cynthia L. Claus, Commissioner Brian J. Moline, Commissioner

MEMORANDUM

December 10, 2002

In the Matter of the Application of Western Resources, Inc. for Approval To Make Certain Changes in its Charges for Electric Service.)	
)	
)	Docket No.
)	01-WSRE-436-RTS
In the Matter of the Application of Kansas Gas and Electric Company for Approval To Make Certain Changes in its Charges for Electric Service.)	
)	

To: Chair Wine
Commissioner Claus
Commissioner Moline

From: Larry Holloway *LH*

DATE SUBMITTED TO LEGAL: 12/10/02

DATE SUBMITTED TO COMMISSIONERS: 12/10/02

RE: Staff Recommendations Regarding the Timing and Details of a Thorough Review of Western's Resources' Power Marketing Activities (Docket No. 01-WSRE-436-RTS, July 25, 2001 Order on Rate Applications, ¶ 101)

The purpose of this memo is to address Staff's review of the audit of Western Resources, Inc.'s (now Westar Energy, Inc.) power marketing activities and provide the Commission with Staff's recommendations for implementing audit findings and recommendations.

Background

In its July 25, 2001 Order in Docket 01-WSRE-436-RTS the Commission expressed concern regarding the lack of an audit trail and the complexity of the Western Resources, Inc.'s Power Marketing (WRPM) transactions. The Commission ordered Western Resources (now Westar Energy, Inc.) to file their written procedures for differentiating,

classifying and tracking asset and non-asset based transactions. Additionally the Commission ordered Staff or an independent third party to perform a thorough review of the Applicants' power trading activities and procedures.

On September 7, 2001 Western Resources filed documentation regarding the WRPM and WRRU interface process entitled, "Western Resources Procedures for Differentiating, Classifying and Tracking Asset and Non-Asset Based Transactions."

On December 17, 2001 Staff filed its recommendations for performing a third-party audit of Western Resources power marketing function. On January 18, 2002 the Commission issued an order accepting Staff's recommendations.

On August 16, 2002 Navigant Consulting, Inc. (Navigant) was selected to perform the audit. On September 9, 2002 Navigant began its audit. On November 13, 2002 Navigant completed its audit report. Since that time, Staff has met with Navigant and discussed both the results of the audit and the process.

Summary of Navigant Report

Summary of Navigant's Findings

- Generally Westar documents and classifies its trading transactions in a manner that is consistent with its stated policies and procedures

Navigant analyzed over 200 executed transactions and performed additional testing on other contracts. Based on its review Navigant believes that generally Westar followed its internal procedures. However Navigant did note that it found several exceptions of inconsistencies that occurred. Navigant found in all but one case that these errors were immaterial. Navigant did identify one material error that has subsequently been correctly booked. Westar highlighted this error and Navigant has concluded that it was an isolated error and not indicative of any intentional effort to manipulate profit margins between the System and Marketing groups.

- An inconsistency exists between Westar's internal policies and the description of the classification of asset and non-asset based transactions as describe to the Commission in Westar's September 7, 2001 filing.

Navigant identified an inconsistency with Westar's procedures for classifying asset and non-asset based transactions, filed with the Commission on September 7, 2001, and Westar's own internal policies. In essence, Westar's filing with the Commission stated that an asset based transaction remains asset based when executed, however asset based transactions are also used to balance hourly purchases and sales executed solely for the marketing group. Westar's actual policy is to compensate the "system" (the regulated assets whose transactions are recorded "above the line") with asymmetrical pricing. Purchases from the system (asset-based sales) are valued at the greater of either incremental generation costs or market prices. Sales to the system (asset-based

purchases) are valued at the lesser of either decremental generation costs or market prices. Navigant noted that it found no evidence that Westar had not followed this asymmetrical pricing methodology.

- As part of its normal course of business Westar uses certain transactions to transfer energy from its system to its marketing group.

Navigant identified a series of transactions providing energy to the marketing group from the systems (asset-based) group, for purposes of balancing, through a third party. Navigant investigated these transactions and found that all appear to have been valued at market prices and appear to have had little impact on the system or the marketing entity. However, while Navigant did not identify any instances where this practice violated Westar's internal asymmetrical pricing policy, Navigant does believe these types of transactions are difficult to segregate, audit and verify. For this reason, Navigant has made recommendations for additional controls and documentation.

- Westar should take action to formalize the independent roles of the Utility Resource Planner (URP) and the internal audit functions.

Navigant identified areas where improvement to internal controls should be implemented or strengthened to document and review the energy trading functions. Navigant identified a weakness in formal documentation by the URP as required by Westar's internal policies and procedures. Additionally, Navigant identified a need for Westar to strengthen its support of its internal audit function.

Summary of Navigant's Recommendations

- Controls should be strengthened to improve confidence
 - Documentation of asset/non-asset classification process
 - Enhancement of internal audit function
 - Establishment of documentation retention program

These recommendations address the importance of the URP and internal audit function and would require Westar to increase its documentation and record retention for power trading activities.

- Controls should be established for pricing of inter-company transactions
 - Initiate independent review for inter-company transactions
 - Perform spot review of internal trade transactions

These recommendations address concerns that a bias could develop between system and marketing transactions. While Navigant did not identify any such bias, this recommendation is to assure that it does not develop.

- Procedures should be clarified and updated
 - Power marketing procedures filed at the Commission should be updated

- o Internal procedures should be updated

These recommendations reflect two concerns. First, as discussed, Westar's power marketing practices for classification of asset and non-asset based trades are different than those filed with the Commission on September 7, 2001. Second, Westar's internal procedures should be updated to reflect their current practices and organizational structure.

Discussion

Staff has reviewed the Navigant report and met with Navigant and Westar on several occasions regarding the audit. Staff notes that Westar cooperated fully with both Staff and Navigant during the audit. Furthermore, throughout discussions and meetings Westar indicated that it was approaching the audit as an opportunity to improve its practices and procedures and Staff notes that this approach and attitude was evident throughout the process. Staff has reviewed Navigant's findings and recommendations and has several observations.

First, Staff notes that Navigant has identified Westar power marketing practices that do not agree with the classification procedures filed with the Commission on September 7, 2001. While Staff is concerned that these practices do appear to be somewhat different than those stated to the Commission, Staff notes that Westar's approach and practice appears to be one of appropriate asymmetrical pricing. Westar's practice of lesser than pricing for purchases made by the system (above the line) from the power marketing group, and greater than pricing for sales by the system (above the line) to the power marketing group, is consistent with standard regulatory practices for asymmetrical pricing between regulated utilities and their unregulated affiliates. However, Staff concurs with Navigant's recommendation that Westar's actual filed procedures should be updated and filed with the Commission.

Second, Staff notes that Navigant has recommended enhancements to Westar's documentation and procedures. Staff believes that for future reviews and audits it will be essential that Westar have clearly defined internal procedures and documentation. While Staff notes that Navigant has not identified any problems with Westar's application of market pricing, Staff also recognizes the difficulty of proving that actual price manipulation did not occur. For this reason Staff concurs that additional clarification of procedures and documentation is needed. These steps should provide future auditors with a workable "audit trail" and Westar management with confidence that its power marketing function maintains adherence to current practices.

Third, Staff notes that Navigant did discuss an isolated event where an options transaction had been inappropriately booked as a charge against the systems group. Staff notes that Navigant has performed additional testing after finding this error, and has found no additional occurrences. Furthermore, Navigant has indicated that Westar highlighted this error and agreed to correctly book the transaction. Additionally, Navigant has determined that it was not indicative of any intentional effort to manipulate

profit margins. Staff concurs with Navigant that this event is likely isolated, but believes that implementation of Navigant's recommendations could help prevent future recurrence.

Fourth, Staff notes that Navigant has recommended enhancing the internal audit function. Staff believes this may be the most critical aspect of power marketing oversight. Without truly knowledgeable, dedicated and independent internal auditing, it is likely difficult for personnel caught up in the hectic day to day marketing activities to have the time or perspective to recognize when internal practices begin to vary from stated procedures and objectives. Staff notes that this is in no way critical of current Westar audit personnel. Instead Staff believes that Westar should ensure that it has dedicated adequate personnel and resources to support an ongoing internal audit function in accordance with Navigant's recommendations.

Fifth, Staff notes that one of the objectives of Navigant's audit was to provide Staff with some insight and direction for future audit activities as well as any necessary reporting activities. Navigant has indicated that after the first of the year they will meet with Staff to go over in detail all aspects of their audit and answer any questions Staff has regarding the details of Navigant's process and testing. Additionally Staff notes that Navigant's recommendations, when implemented, will increase the amount of information, written internal procedures and documentation created and maintained by Westar. Staff believes these actions are likely adequate, but will review these changes when they are incorporated.

Recommendations

Staff recommends that:

- The Commission accept Navigant's findings and recommendations as detailed in their November 13, 2002 report.
- The Commission require Westar to file a plan detailing how and when it will implement Navigant's recommendations.
- Staff meet with Westar to review the implementation of Navigant's recommendations when completed.

cc: Mike Peters
Joe White
Susan Cunningham
Jeff Wagaman
Jeff McClannahan
Kyle Clem
Pat Renner
George Rohrer



Navigant[™]
CONSULTING, INC.

Review of Power Marketing & Trading Activities and Procedures At Westar Energy

A Report Prepared for:

*The Kansas Corporation Commission and
Westar Energy*

November 13, 2002

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I. Executive Summary

Scope of Work

In August 2002, the Kansas Corporation Commission (the Commission or the KCC) and Westar Energy, Inc. (Westar) engaged Navigant Consulting, Inc. (Navigant Consulting) to perform a review of Westar's power marketing and trading activities and procedures. Specifically, Navigant was engaged to provide the following services:

1. Perform a review of the defined procedures filed with the Commission on September 7, 2001, for differentiating, classifying, and tracking asset and non-asset based transactions;
2. Perform a compliance review of the transaction lifecycle;
3. Develop findings and recommendations and provide suggestions for future audits.

Navigant Consulting has performed a review in accordance with this scope and submits this report based on our findings. A copy of that scope of work has been included as Exhibit I.

Procedures Performed by Navigant Consulting

A description of the process we used to perform this scope is included in the section of this report titled, "Procedures Performed by Navigant Consulting". As noted within Section II of this report, Navigant Consulting has performed a variety of procedures during the course of our review. Our work to date has included the following:

- Detailed transactional testing at a level which exceeds that described within our agreed upon scope of work. For each transaction, the relevant information related to each energy trade was tracked through the various phases of the transaction lifecycle.
- Review of various futures contracts and options agreements entered into by Westar's System and Marketing operations. For each type of transaction, we reviewed and analyzed selected contracts to ensure that all information was correctly recorded within both the operational records of the organization and the risk management records maintained by the middle and back office.
- Interviews with key personnel within the energy trading operations.
- Review of OpSym Modeling Forecasts.
- Review of existing compensation structure.

A more detailed description of these tasks has also been included within Section II of this report.

Overall Conclusions

As has been noted in our detailed report, Navigant Consulting has no reason to believe that power marketing and trading activities are being used to disadvantage regulated customers. While we found areas where procedures should be clarified and controls should be strengthened, there were no findings that bring immediate concerns. Navigant Consulting has no reason to believe that the absence of these suggested improvements during the review period have had a negative financial impact on Westar's operations. However, we believe that the implementation of our suggested improvements would enhance Westar's overall control environment and would provide for greater oversight of the energy trading function.

Navigant Consulting's review of Westar's power marketing and trading operations resulted in the following findings:

- Generally, Westar documents and classifies trading transactions in a manner that is consistent with its stated policies and procedures.
- Westar's September 7, 2001 filing (a 5-page document) summarized various policies and procedures relating to the classifying and tracking of energy transactions. Westar also maintains more detailed internal policies and procedures for Power Trading Administration. In regards to certain types of inter-company transactions, there is an inconsistency between these two sets of policies and procedures and we believe they should be updated to provide for a more detailed explanation of the procedures used in the accounting for inter-company transactions.
- As part of its normal course of business, Westar enters into certain transactions that transfer energy from the System to the Marketing function in line with industry norms. While our review has not detected any type of pricing issues, additional procedures should be established to ensure that inter-company and "balancing" transactions are independently validated and clearly documented.
- Additional formalized controls would help to strengthen the independent roles of the Utility Resource Planner and the Internal Audit functions.

In considering our findings, it should be noted that the level of risk undertaken by Westar has been commensurate with the level of risk controls. Although the risk controls currently implemented may have been sufficient in the past, specific recommendations contained in this report are designed to enhance the existing control environment and reduce the likelihood of future risk events.

A more detailed description of these findings and our related recommendations have been included as Sections III and IV of this report.

II. PROCEDURES PERFORMED BY NAVIGANT CONSULTING

Introduction

As part of its work on this matter, Navigant Consulting was engaged by the KCC and Westar to perform a review of Westar's power marketing and trading activities and procedures. Specifically, Navigant was engaged to provide the following services:

1. Perform a review of the defined procedures filed with the Commission on September 7, 2001, for differentiating, classifying, and tracking asset and non-asset based transactions;
2. Perform a compliance review of the transaction lifecycle;
3. Develop findings and recommendations and provide suggestions for future audits.

This section of the report focuses on the specific procedures that were performed by Navigant Consulting during the performance of our work on this assignment. Subsequent sections of this document will summarize the results of our findings while performing these procedures and the various recommendations that we would propose be considered by both Westar and the KCC.

Agreed Upon Scope of Work

The nature of this review and the understanding of the various parties has been summarized in a four page targeted scope of work that was provided to the Commission on August 6, 2002. A copy of this document has also been included as Exhibit I. This document outlines a three-phased approach to performing the review, with the first phase focusing on the review of certain procedures that were filed with the KCC on September 7, 2001. The second phase of the project focused on the performance of certain compliance procedures to ensure that transactions undertaken by Westar were in accordance with appropriate policies and procedures. The final phase of the project focused on the preparation of recommendations and findings. This report addresses, in large part, Navigant Consulting's roles and responsibilities under this third phase.

As noted within the scope of work, the period of time covered by this review was October 1, 2001 through July 31, 2002. Navigant performed no substantive testing of any transactions that occurred outside of this specified time period.

Review of Procedures

As part of our initial review at Westar, we performed a series of interviews with the key individuals who are involved with the energy trading process. These interviews were designed to obtain an understanding of the background of these individuals, the various tasks performed by each individual, the nature of the risks facing the organization, the controls in place to detect these risks, and the daily procedures performed by the department to execute transactions and record the activity within the books and records of the organization.

Interviews were conducted with all individuals who manage or perform some type of key function in either the front, middle, or back office. Our list of interviews included the following individuals:

1. **Doug Gaumer (Senior Director – Energy Marketing and Trading)** - As the overall director of the power marketing and trading activities, Mr. Gaumer has a unique understanding of all the in the front, middle, and back offices. Mr. Gaumer provided us with an overview of the trading operations and provided us with his understanding of the specific tasks performed by each of the employees under his control.
2. **Greg Umscheid (Senior Director, Generation and Marketing Administration Services)** - As the manager of the middle and back office functions, Mr. Umscheid has the responsibility for ensuring that all transactions are properly executed and classified by the organization. Mr. Umscheid described for us the flow of transactions through the middle and back office and explained to us the various accounting and tracking systems that existed within the organization to ensure that the Institution's risk profile was being monitored and that the transactions that were executed were correctly recorded within the accounting systems.
3. **Jo Hunt (Vice President, Risk Management)** - Ms. Hunt serves as the primary coordinator of the organization's risk management function. She provided us with an understanding of how the organization manages its risk and the specific tasks performed by each member of the risk management team. She further described her role in the evaluation of credit and the management of the value at risk calculation.
4. **Steven Massey (Senior Manager, Asset Management – Energy Marketing and Trading)** - Mr. Massey serves as the Utility Resource Planner for Westar. In that capacity, he manages the generation of power by the System and makes all determinations regarding the sale of output from System assets and the purchases of power associated with the native load. Mr. Massey also interacts with the various traders to determine which transactions, if any, the System will enter into during a given period of time. Mr. Massey is also responsible for the real time trading and hourly transactions that are performed to benefit the System assets. Finally, Mr. Massey is responsible for the inputs to and use of the OpSym system¹ for projecting the daily system dispatch.
5. **Grant Wilkerson (Senior Manager, Trading)** - Mr. Wilkerson is the most senior trader within Westar's trading operations. While he reports to and has extensive dealings with Mr. Gaumer, Mr. Wilkerson has the authority to commit Westar to most of its trading transactions. He also supervises a relatively small group of traders who execute the bulk of Westar's futures and options activities.
6. **Jeff Lenherr (Manager, Internal Audit)** - Mr. Lenherr is part of Westar's internal auditing staff. He performs many of the internal reviews of Westar's trading operations and provided us with an overview of the control structure in place at Westar.

¹ Navigant Consulting also interviewed Mr. Brandon Sack. Mr. Sack is a Senior Associate and is responsible for inputting the variables into the OpSym system. However, all of the actual results from any OpSym analysis are actually reviewed and approved by Mr. Massey before any decisions are made or before any information is provided to the trading staff.

These interviews provided Navigant Consulting with insight into and an understanding of how Westar's power marketing and trading procedures work in the day-to-day operations of the business. We used this understanding to define details of our transaction testing process for the compliance review and as critical input into our review of filed procedures used by Westar for differentiating, classifying, and tracking asset and non-asset based transactions that are commented on later in this report.

In conjunction with these interviews, Navigant also reviewed the organizational structure of positions involved in Westar power marketing and trading functions with a particular emphasis on separation of control functions. We found that the control functions report up through an organization separate from the front-office functions reporting to Doug Gaumer, which is appropriate. Most of the middle and back-office functions are performed in Greg Umscheid's Administrative Services group that reports through Mr. Hodson to Mr. Sterbenz. Even more separate, is the recent creation of a Vice President of Risk Management position (May 2002) reporting to the Executive Vice President and Strategic Officer, independent of Mr. Sterbenz's Generation and Marketing organization.

Copies of various relevant organizational charts provided by Westar have been included as Exhibit 2. Based upon our review of these documents, it appears that the organization is properly structured and warranted no specific comments or recommendations separate from the comments on controls made later in this report.

In addition to these formal interviews, Navigant conducted a variety of additional discussions with various Westar personnel on a more informal basis. In addition, Navigant met with members of the Commission's staff to understand their various concerns with the operations of Westar's trading function.

Detailed Testing of Transactions

As noted above, the scope of our review as agreed upon with the KCC and Westar included an extensive amount of detailed transactional testing. This transactional testing involved the review of individual transactions that were selected from various databases of transactional data that were provided by Westar. While not a purely random sample, our selection process was designed to capture representative transactions from a variety of different types of energy sales and purchases. In addition, Navigant Consulting selected transactions from both the "System" and the "Marketing" side of Westar's operations. Finally, we attempted to select transactions that occurred during the entire time period that was the subject of our review.

Description of Population to be Tested

As noted within their policies and procedures, the energy trading operations of Westar are segregated into two separate units. The System group is responsible for all purchases and sales that are entered into that as part of Westar's efforts to serve the requirements of its native load (i.e. those residential and business customers who rely on Westar for electric power). As part of its efforts to serve the native load, this group is responsible for managing (i.e. selling or using) all of the energy generated from Westar owned generating units.

In contrast, the Marketing group is responsible for conducting all transactions that do not serve Westar's native load requirements. The transactions entered into by the Marketing group do not have a direct effect on system generation operations. The risk of all transactions conducted by the Marketing group is borne by Westar Energy shareholders and not customers of the Westar's utilities services.

Both the System group and the Marketing group enter into energy transactions as part of their mandate to meet the needs of their respective constituencies. These transactions include either the

immediate delivery of energy (e.g. hourly energy trading to meet immediate needs), or they can take the form of agreements to provide energy at some point in the future at a specified price (e.g. futures and option agreements). Regardless of the nature of the transactions, Westar's middle and back-office functions process all of the energy transactions through the same accounting systems. Based upon our review of data provided by Westar, we understand that the following transaction volumes were recorded by Westar during the period under review (i.e. October 1, 2001 through July 31, 2002):

Sales Transactions Executed by Westar

Unit	Transactions	MWH	\$\$\$
Systems Group	11,608	5,945,758	\$ 143,940,672
Marketing Group	11,621	6,167,095	\$ 181,944,266
Total	23,229	12,112,853	\$ 325,884,938

Purchase Transactions Executed by Westar

Unit	Transactions	MWH	\$\$\$
Systems Group	6,392	3,147,645	\$78,665,096
Marketing Group	11,608	6,169,350	\$174,257,865
Total	18,000	9,316,995	\$252,922,961

The amounts shown above represent the actual transactions that were executed by Westar during the period under review. The amounts do not include options or futures contracts that were not exercised or trades that were conducted in natural gas, coal or oil.

The total number of transactions sampled totaled 202 and are described in the following four categories.

Initial Review - 100 Selected Transactions

In performing our testing, we initially focused upon the population of transactions that had been settled during the period under review (see description above). From this population, we selected 100 sample transactions. These transactions, which represented actual sales or purchases of energy, were chosen without regard to the nature of the trading vehicle that was used to generate the sale².

Our transaction testing focused on confirming the various pieces of transactional information from the inception of the transaction through its final execution and recording in Westar's general ledger. For each transaction in the sample, we initially collected deal tickets, power deal sheets, broker confirmations, electronic transaction reports³, daily schedules, bookout schedules,

² For example, some of the transactions that were tested have been entered into by Westar as part of some type of forward purchase or forward sale transactions. In these cases, Westar agreed to provide or sell energy to another party at some future point in time. In contrast, other transactions were same-day trades that were performed by Westar to meet its daily energy needs. All of these transactions were eventually settled by Westar as part of its normal operations. As discussed below, additional testing was performed

³ The electronic version of the deal tickets were maintained by Westar in a separate system and were identified to Navigant as "Wattage Reports". For control purposes, a Peterson consultant was with the Westar staff when all of the wattage reports were printed.

transactional summary reports (i.e. journal entry summaries) and other types of transactional information.

Once all of the relevant documents were collected, Navigant reviewed the documents that described the initial inception of the trade (i.e. deal tickets or power deal sheets) and then compared that information to the information contained within the middle and back office function documentation. In regards to the middle office, this testing involved the review of middle office accounting system (i.e. the Wattage System) and the various broker-dealer confirms or remittances to confirm that the information contained within the Wattage System and the broker confirmations or remittances were, in fact, the same as that which was shown to in the documents that detailed the terms of the deal at its inception. By performing this testing, we were able to confirm that that information placed into the energy trading accounting system was correct and accurately reflected the terms and conditions of the energy transaction.

In regards to the back office, our testing focused on ensuring that the information contained within the general ledger and the other sources of settlement information was identical to the information contained within the deal inception documents. In addition, we focused our testing on ensuring that Westar's practices for recording information were accurate and that acceptable controls were in place to ensure that transactions were being properly recorded within the general ledger. To accomplish these tasks, we traced the monthly totals from the transaction summary reports to their respective journal entries and onto the general ledger⁴.

Additional Testing of Forward Contracts – 51 Transactions

The second area of our analysis involved testing forward contracts. Typically these forward contracts were for one month or two months in duration. The purpose of this testing was to ensure that Westar maintained proper documentation from the inception of the contract to the actual delivery date. While our testing of executed transactions included some transactions that were being executed as part of some type of forward commitment, the unique nature of such transactions and the impact that such transactions have on the organizations risk profile led us to expand our testing in this area.

A representative sample was selected by choosing the ten largest (by total dollar value) Market and System transactions for both buy and sell contracts. Furthermore, several additional transactions were selected at random. In all, 51 forward contracts were selected for testing. We collected and tested power deal sheets, broker confirmation (not same terms used before), monthly risk system report, bookout reports, and selected wattage reports that provided proof of the deal's execution.

As with our testing of the executed transactions, we focused our testing on ensuring that the original terms of the contract were correctly recorded at all key recording points during the transaction's lifecycle. As such, our testing of the front, middle and back-office functions was similar to the testing performed on executed forward contracts. However, additional procedures were performed due to the nature of the transactions. For example, we tested to make sure that all forward commitments above certain threshold amounts to make sure that they were authorized as required by Westar's own internal policies and procedures.

In the case of the forward contracts, it was also important to ensure that each of the forward contracts was captured within Westar's risk management system for the entire duration of the forward commitment. To ensure that this was the case, we tested the forward commitments to ensure that all potential exposures were captured within the value at risk (VaR) calculations. While we did not assess the overall reasonableness of the assumptions used within these VaR calculations,

⁴ Two sets of documents were used to trace transaction summaries. One relates to System and Marketing purchases and the other relates to System and Marketing sales.

we were able to determine that these forward commitments were included within the calculations themselves.

Additional Testing of Options Contracts – 21 Transactions

The third area of Navigant Consulting's analysis involved testing option contracts. The purpose of this testing was to ensure that Westar maintains proper documentation from the inception of the option contract to the actual delivery date, if it is exercised. A total of 21 option contracts were tested as part of our review.

The documentation collected and steps followed for the option testing were similar to the forward testing with some slight differences. These differences generally related to the fact that due to the timing of certain transactions, certain execution documents were not available. For example, during the period under review, Westar's trading operations may have entered into an option contract for the delivery of energy during the 2003 time period. For unexpired options, certain execution documents have not yet been prepared or processed by Westar. In addition, if Westar had an option that was not exercised, the execution documents would not exist.

As with the forward contracts, our testing of the option contracts also focused upon determining whether Westar's risk management system captured both exercised and non-exercised options. Our testing centered, in large part, on ensuring that all potential exposures were captured within the organizations risk management systems.

Additional Testing of Oil/Gas Contracts – 30 Transactions

The final area of analysis involved testing oil and gas transactions. As with the forward transactions and the executed transactions, the purpose of this testing was to ensure that Westar maintains proper documentation from the inception of the option contract to the actual delivery date. A total of 30 oil and gas contracts were tested as part of our review.

The documentation collected and steps followed for the oil and gas contracts was similar to the executed transaction testing described above. While some slight differences existed between the nature of the transactions (due, in large part, to the storage and physical transmission of the products), the actual methodology for recording and executing the transactions was similar.

Review of Incentive Compensation Structure

Compensation, and in particular, incentive compensation, is a critical tool for the attraction and retention of qualified trading personnel as well as for providing the proper signals to individuals and the team for what is valuable to customers and shareholders. While a detailed compensation review was not performed⁵, Navigant Consulting felt that it was important to review incentive compensation policies and procedures to understand the potential incentives that might exist for members of the trading operation to shift the profitability of the overall trading operations into the System or the Market portion of Westar's business.

We reviewed the Westar power marketing and trading incentive compensation plan and found it to have a neutral bias that gives equal weight to customer and shareholder interests. Incentive compensation is based on a net margin calculation that includes both "System" and "Marketing" transactions. Therefore, a dollar shifted from one category to the other makes no difference in the

⁵ Such a review would be outside the scope of our assignment as shown in Exhibit 1 to this report.

compensation pool for those participating in the plan⁶. In addition, the incentive compensation is based on net margin rather than sales volumes. Such incentives serve to reduce the risk of any type of abuses related to volume building or price manipulation.

The incentive compensation plan covers individuals that contribute directly to the success of the trading operation and is allocated by a committee of management representatives. While there appears to have been some recent changes in the listing of participants in the overall plan, it appears that these changes were made to make the program more inclusive within the energy trading operations group. Westar's Internal Audit group reviews the annual incentive compensation plan calculation and audits the margin it is based upon. In this regard, we did not perform a review of those calculations.

OpSym Forecast Model

Our review included the Westar's use of the OpSym model used for the purpose of making projections for load and system dispatch. These projections are critical as they set price/quantity parameters that guide the next day's trading activities where the asset and non-asset transaction decisions are made. Our review concluded that the use of the OpSym model was appropriate and the tested model inputs appeared to be in line with what would be considered reasonable. Also, our review uncovered no particular bias in the way model runs were managed. The goal was accuracy with no particular need to have a daily load forecast be higher or lower than actual.

Limitations of Our Review

The procedures performed as part of this assignment did not constitute a full or comprehensive audit of the Westar energy trading function. Instead, Navigant Consulting performed a targeted review with a clearly defined scope. This review was designed to test Westar's operations and to identify potential or perceived control weaknesses. We focused on transactional testing and internal control reviews, but did not rely upon any type of statistical sampling or other type of testing that could be used for extrapolation purposes. As such, the findings contained within this report should be considered to be relevant to only the trading operations of Westar during the period under review. It should not be used as a basis for any type of assessment of Westar's operations as a whole or on the activities of the trading group during periods outside of this review.

In addition, procedures performed during this review were not performed as part of an effort to detect fraud or mismanagement within the organization⁷. Instead, our testing focused upon determining whether the transactions entered into by Westar were appropriately classified, tracked and recorded within the books and records of the Company. We did not attempt to assess the reasonableness of trading decisions (i.e. whether a transaction was prudent) and we did not attempt

⁶ It is important to note that this policy of basing incentive compensation on margins generated by both the System and Marketing aspects of the operations was in effect for the entire period under review. However, for periods prior to 2001 (i.e. outside of the review period), a different compensation structure was in place. The incentive plan included as part of that compensation structure based bonuses on the margins achieved on only the Marketing aspect of Westar's operations. This change during the 2001 time period represents a strengthening of Westar's overall controls.

⁷ If, in fact, such fraud or negligent mismanagement had been detected by Navigant Consulting, it would have been included within this report. However, our testing was not designed to specifically seek out such fraud and negligent mismanagement. As such, our report cannot provide any type of findings or conclusions regarding the existence of fraud within the operations of Westar's energy trading operations.

to determine if the operations of the Marketing group were fiscally appropriate for the organization⁸. Instead, we focused upon how the transactions were recorded and classified after Westar elected to enter into these transactions.

Finally, Westar's operations are not conducted within a vacuum and that the impact of changes in the general market for energy futures and options will have an effect on the operations of Westar. We have not attempted to assess the overall industry and have assumed, for the purposes of this review, that the industry as a whole was operating as an effective market during the period under review⁹.

⁸ It was not in Navigant Consulting's scope to determine if the transactions entered into by the Marketing group were appropriate transactions for Westar. For example, we did not attempt to determine if Westar's Marketing Group was making trades that were inappropriate given either the market conditions or the risk levels within the company or industry. No attempt was made to determine what level of market risk was acceptable for a company such as Westar.

⁹ For example, recent press reports have suggested that traders from other energy trading operations had entered into transactions that were either inappropriate, misleading, or illegal. Traders from other companies have been accused of manipulating market rates and market indices. For the purposes of our review, we have assumed that the transactions entered into by Westar were not affected by the actions of these other traders. As such, we have assumed that "market prices" quoted to Westar by various counterparties were the actual market prices in effect at the time of the transaction.

I. Findings

Introduction

Based upon the results of detailed testing, we have summarized our findings and highlighted the most significant areas of potential risk for Westar. These findings focus specifically on the information derived from our review of procedures, including our discussions with management and our limited transaction testing, and are meant to focus solely on the energy trading aspect of Westar's operations.

In considering these findings, many represent potential control or operational weaknesses that may not necessarily have a current financial impact on the operations of Westar. As such, there is not an effective means to quantify the potential financial impact, if any, that the absence of certain controls may have on the overall operations of the organization¹⁰. However, we believe that the findings shown below, if unaddressed, could expose the organization in the future to some degree of risk. These potential weaknesses may present operational risks for Westar. This, in turn, could lead to potential losses for both the System and Marketing aspects of Westar's energy trading operations.

SPECIFIC FINDINGS

1. Generally, Westar documents and classifies its trading transactions in a manner that is consistent with its stated policies and procedures.

As noted in previous sections of this report, our review included an analysis of approximately 100 executed transactions and a series of additional tests on forward contracts, option agreements, and oil and gas contracts. The testing that was performed was more substantive and comprehensive than that which was described within our original scope of work.

IA. Based upon the results of our testing, Navigant Consulting believes that the procedures employed by Westar serve to adequately differentiate, classify, and track the various asset and non-asset based transactions that were executed during the period under review. Navigant Consulting testing focused on the entire lifecycle from trade inception, invoicing, execution and recording of that transaction in the books and records of Westar. While certain improvements could be made, the documentation maintained by the organization provides sufficient evidentiary information that supports the actual transactions.

IB. Improvements could be made to Westar's documentation and tracking procedures. For example, documentation processes could be improved and a more comprehensive document retention program should be adopted by the organization. While such improvements would strengthen the control environment, we believe that our testing to date adequately addressed and adjusted for these control weaknesses.

¹⁰Operational controls serve as a form of checks and balances within the organization to ensure that improper transactions are detected and minimized. While the absence of such controls may expose the organization to greater risk, there may be no financial impact associated with this absence of controls if, in fact, the organization did not undertake any type of improper transactions.

1C. During the course of testing, Navigant identified several isolated exceptions or inconsistencies that occurred during the normal course of Westar's operations¹¹. In all but one case, these exceptions or inconsistencies were of an immaterial nature and were not indicative of any pervasive weaknesses within either Westar's operations or its efforts to accurately track and record energy transactions. In these cases where immaterial problems existed, Westar's management was able to provide reasonable explanations for the exception or inconsistency¹².

1D Through testing, a single transaction was identified which contained a material error in regards to the classification and tracking of an asset-based transaction. This transaction involved an option agreement that was entered into by Westar's Marketing group. At the time of the option's execution, Westar received a benefit from this option transaction and subsequently recorded that benefit as revenue to the Marketing group. However, as Westar performed during the option period, the charges against the option were applied against the System group. In other words, the benefits associated with this single transaction were record within the Marketing group and the costs associated with the transaction were recorded within the System group. While this transaction was incorrectly booked, our subsequent testing of additional option agreements¹³ has indicated that this was an isolated error and was not indicative of any intentional effort on the part of Westar to manipulate the profit margins of the System and Marketing groups¹⁴. Senior management of Westar highlighted this transaction for Navigant Consulting, has agreed with our finding and has indicated that this error would be immediately corrected in the 2002 books of the energy trading group.

2. In regards to certain types of inter-company transactions, there is an inconsistency between Westar's internal policies and the procedures filed with the KCC on September 7, 2001 that should be clarified by updating procedures.

2A. Procedures filed with the KCC outline two types of transactions within Westar's energy trading operations. Transactions that relate to the regulated aspects of Westar's operations are described as "Asset" or "System" based transactions, while transactions relating to Westar's non-regulated transactions are described as "Non-asset" or "Marketing" transactions. More specifically, the procedures define the two types of transactions as follows:

¹¹ For example, several of the trades tested contained illegible trader names. For certain other transactions, the methodology used for assigning Wattage numbers was inconsistent, and, for several transactions, data was entered into the Wattage system inconsistently. All of these errors were immaterial to the operations of the organization and did not have a financial impact on the System or Marketing groups.

¹² It should be noted that, in some cases, an absence of adequate documentation prevented Westar from being able to completely justify these immaterial exceptions or inconsistencies. Given the nature of these exceptions and inconsistencies, the verbal explanations provided by Westar appeared reasonable.

¹³ After this error was identified, Navigant Consulting selected additional option contracts for testing. Our review of these additional option contracts identified no other errors.

¹⁴ Based upon our review, this transaction was originally executed by an employee who no longer works for Westar. Had this employee been present when the option was executed, it appears that the incorrect application of the benefit payment would have been detected by Westar in a more timely fashion.

Asset Based Transactions: Asset based transactions are purchases that are intended to serve native load requirements within the Western Resources control area and sales where energy is expected to come from Western Resources generating units. Generally, asset based transactions will affect system generation operations by causing Western Resources to either increase or decrease the output of its generating units.

Non-Asset Based Transactions: Non-asset based transactions are those which are not intended to serve native load requirements within the Western Resources control area. Generally, non-asset based transactions will not affect system generation operations by causing Western Resources to either increase or decrease the output of its generating units. The risk of these transactions is borne by Western Resources shareholders and not customers. (Page 1 of The Filed Procedures – See Exhibit 3)

- 2B. Filed procedures indicate that asset based transactions would not be converted or transferred to the “non-asset” side of Westar’s operations. According to these procedures:

Any transaction which is classified as an asset based transaction when it is executed, will, from that time forward remain an asset based transaction until the transaction is closed out. (Page 1-2 of the Filed Procedures – See Exhibit 3)

- 2C. These excerpts from the Filed Procedures are inconsistent with Westar’s own internal policies that clearly indicate a relationship exists between the asset and non-asset based components of Westar’s operations. According to Westar’s own internal policies:

The marketing group does not have generation resources available, therefore hourly purchases and sales must be balanced. If the non-asset related transactions have an hourly imbalance (purchases and sales not equal), the asset related group is favorably compensated for the energy imbalance. If the asset related group is selling to the non-asset related group the price is the greater of the incremental generation cost or the market value of like sales from Generation assets. If the asset related group is buying it is the lower of the decremental generation cost or market value of like purchases for load. This same pricing methodology is utilized when the system has resources available to sell or needs to purchase power to meet load requirements. (Detailed Internal Procedures – See Exhibit 4)

- 2D. We have discussed this inconsistency with Westar’s management team. They have indicated that it arose as a result of their effort to simplify, condense and summarize the internal policies and procedures (Exhibit 4) into a more succinct version filed with the KCC (Exhibit 3). In testimony submitted as part of filing the procedures with the KCC, Mr. Mathis’s discussion of these types of transactions provides evidence that they were part of Westar’s trading business to be addressed in the filed procedures. Finally, it should be noted that the policies and procedures described within Westar’s internal policies are consistent with industry practices.

- 3. As part of its normal course of business, Westar enters into certain transactions that transfer energy from the System to the Marketing function. Additional procedures should be established to ensure that these inter-company and “balancing” transactions are independently validated and clearly documented.**

- 3A. During the course of our review, we found a series of sales/purchases whose sole purpose was to account for the certain balancing transactions transferring energy from the “asset” (or System) category to the “Non-asset” (or Marketing) category. These transactions are customary in the industry and are generally referred to as “sleeve transactions”. In some cases, these transactions were performed through an existing relationship with a third party,

while other transfers were accomplished through the use of internal transactions that did not involve other third parties. The nature and volume of these transactions are summarized below:

Transfers from System to Marketing

Counterparty	Transactions	MWH	\$\$\$
Coral Power	83	15,086	\$259,852
CLEC	128	52,716	\$1,234,890
SETC	3	8	\$177
Internal Transfers	63	201,600	\$4,244,064
Total	277	269,410	\$5,738,983

Transfers from Marketing to System

Counterparty	Transactions	MWH	\$\$\$
Coral Power	56	9,778	\$190,729
CLEC	122	28,667	\$608,211
SETC	4	15	\$337
Internal Transfers	9	7,200	\$179,672
Total	191	45,600	\$978,949

The fundamental risk associated with this type of transaction is that the transfers between these two organizations could be priced at a level that was inconsistent with the market price at the time of the actual transactions. If non-market pricing was used, the profit margins of the System and Marketing operations could be manipulated by the individuals involved in the trading operations¹⁵. Based on our review, Navigant Consulting found no such inappropriate manipulation.

- 3B. The sleeve transactions described above were discussed with Westar management. Management has indicated that because the Marketing group does not have generation resources available, they must balance their hourly purchases and sales. By using the sleeves to transfer MWh's between the two organizations, management is able to properly control and fairly account for the use of the generation assets of the System to balance the daily book of the Marketing group. In return, the System is able to generate profits by either selling excess capacity to the Marketing group during periods of availability or may obtain energy from the Marketing group during times when the Marketing group is a net seller of energy. Such transactions are common in trading operations that have both System and Marketing components.

¹⁵ It should be noted that the net profits to Westar as a whole would be unaffected. For example, if the System was to sell energy to the Marketing group at a discount, the System's profits would be lower. However, the profits of the Marketing group would be increased by a corresponding amount because the Marketing group paid less for this energy. In other words, when the profit margins of the System and Marketing groups are combined into a single profit margin for Westar as a whole, the net effect of such transactions is eliminated.

- 3C. Based upon our review of the available data, all of these transactions appear to have been performed at current market prices¹⁶ and, therefore, there appears to have been little, if any, impact on the overall operations of either the System or Marketing entity. In fact, the vast majority of these transactions had a legitimate business purpose that allowed both the System and Marketing side of the businesses to meet their respective goals. Assuming that these transactions were performed at market rates, they would not be a detriment to either the System or the Marketing for entering into these types of transactions.
- 3D. As previously noted under Finding #2, Westar's internal policies address this specific type of transaction. According to those policies:

If the asset related group is selling to the non-asset related group the price is the greater of the incremental generation cost or the market value of like sales from Generation assets. If the asset related group is buying it is the lower of decremental generation cost or market value of like purchases for load. This same pricing methodology is utilized when the system has resources available to sell or needs to purchase power to meet load requirements. (Detailed Internal Procedures – See Exhibit 4)

If Westar complies with these written policies and procedures, the risks associated with the transfer of energy from the System to the Marketing unit is minimized. However, it should be noted that there are no formal checks performed by Westar to ensure compliance with this pricing policy.

- 3E. As noted above, approximately 75% of the amounts included within these sleeve transactions (which are a very small part of all transactions) were actually inter-company transfers that did not go through any type of third party. These transactions did not take the same form as the typical "balancing" transactions that would be expected in the normal course of business¹⁷. According to Westar's management, these inter-company transfers resulted from an agreement that entailed the generation of significant MWh's by the System's unit for the sole purpose of providing balancing generation to the Marketing unit. These generation efforts were planned in advance by Westar, and the Marketing unit entered into various transactions that anticipated this generation¹⁸. According to management, these transactions were priced at market prices and profits were recorded by the System unit for these various sales. Given this representation, the transactions themselves provided the System unit with profit margin. However, given the nature and volume of these transactions, the financial consequences associated with potential manipulation of market rates would have a more significant effect

¹⁶ Navigant's testing of the actual market price was relatively limited and was based, in large part, on comparisons made between the amounts paid in the hourly energy markets by Westar and the amounts paid by the Marketing group for the various "balancing" transactions. These analyses suggest that there were no significant differences between the hourly energy rates and those paid by the Marketing group for the various balancing transactions. A summary of these analyses has been included as Exhibit 5. While these relatively simple analyses provide anecdotal support for the Westar's position that all of these intercompany transactions were priced at market rates, the volatility and nature of the markets makes it difficult to reconstruct the actual market price at the time that the transactions were conducted. Such an analysis would be technically difficult and would require the use of third party data. This type of analysis is beyond the scope of our current assignment and has not been performed.

¹⁷ Typical "balancing" transactions were for relatively small amounts of MWh's at different times and on different days. The volume of "balancing" transactions varied on both an hourly and daily basis because of the fluctuating needs of both the System and Marketing groups.

¹⁸ These transactions were conducted during January and February 2002. The needs of the system during these months has traditionally been very low due to the prevalence of natural gas heaters in the Westar service area. As such, management of the organization has indicated that these months are traditionally low generation months for Westar.

for these inter-company transactions than would the "balancing" transactions that had involved a third party.

- 3F. In addition, Westar's relationship with its various counter parties can make it difficult to segregate the certain types of transactions between the System and Marketing groups. For example, both the System and Marketing units may enter into energy transactions with various counter parties on the same day. While Westar tracks the System and Marketing transactions as two separate transactions (manual process), the counterparty considers Westar to be the same client for both sets of transactions¹⁹. In these cases, Westar receives a transaction confirmation and must determine which of the MWh's shown within this report are chargeable to the System Group and which MWh's are charged to the Marketing Group²⁰. In this case, even though a third party is involved, the potential risks associated with the misallocation of hours could effectively shift profits between the System and Marketing groups²¹. Because this is a manual process, there is a potential risk that should be addressed.
- 3G. Given that there are numerous instances where transactions are conducted without some type of outside verification of market price, there appears to be a risk to both the System and the Marketing groups that transactions could be transferred at a prices other than those prescribed by Westar's internal policies. While the policies themselves provide sufficient documentation of the pricing structure, there is no independent verification to ensure that these policies and procedures are being performed appropriately by Westar's trading personnel.
- 3H. As noted above, Navigant performed certain testing procedures suggest (through anecdotal evidence) that Westar did not violate its policies during the period under review. However, given the volatility and nature of the markets, it is difficult to reconstruct the actual market price at the time that the transactions were conducted. As such, we have not been able to perform definitive testing that would provide complete assurance that these policies and procedures are being adhered to by Westar. Such an analysis would be technically difficult and would require the use of third party data. This type of analysis is beyond the scope of our current assignment and has not been performed.

¹⁹ The separation between the System and Marketing functions is tracked internally by Westar. Counterparties do not recognize the existence of two separate groups (i.e. System group and Marketing group). Instead, the counterparties consider all of their transactions to be with Westar.

²⁰ For example, both the System and the Marketing groups may purchase MWh's from a counterparty on the same day. The hours purchased by the System may be off-peak hours at \$12 per MWh, while the hours purchased by the Marketing group may be peak hours at \$24 per MWh. Aquilla's invoice for these MWh's does not make reference to either the System or Marketing groups, but, instead, charges all of the hours to Westar as a single entity. In this situation, Westar must allocate the off-peak hours to the System group and the peak hours to the Marketing group.

²¹ In other words, if Westar failed to perform its allocations correctly, it could allocate more expensive peak hours to the System group and the cheaper off-peak hours to the Marketing group. This would increase the costs of the System group and would decrease the costs of the Marketing group. This would, in turn, affect the relative profit margins of the two groups.

4. Additional formalized controls would help to strengthen the independent roles of the Utility Resource Planner and the Internal Audit functions.

4A. During the course of our review, we identified several areas where either new internal controls could be implemented or existing controls could be strengthened to provide for better management and oversight of the energy trading function. In particular, we believe that additional controls should be implemented in the areas of asset classification, risk management, the URP classification process, and the internal audit function.

4B. The URP acceptance or rejection of a particular transaction is a key control point in the Westar power marketing and trading process, but currently is documented by two informal methods. While Westar has developed policies and procedures to establish parameters for transactions that would be acceptable to the URP (i.e. the Daily Projection Analysis created by OpSym), our review noted no written documentation that would provide proof that particular transactions were accepted or rejected by the URP. The absence of such documentation, when coupled with Westar's failure to retain OpSym reports for extended periods of time, makes it very difficult to perform any retrospective reviews of transactions to determine if they were appropriate asset based transactions.

4C. As previously noted, part of our review included conducting a review of the role played by Westar's internal auditors in the oversight and review process. While the internal audit department did play a role in the review of trading activities during the period under review, that role has been largely related to the review of specific components of the operation and recurring annual projects such as incentive compensation review issues. While the internal audit function has performed these duties in a relatively efficient manner and has performed the tasks assigned to them in an appropriate fashion, we believe that significant benefits could be derived from a more robust commitment to the internal audit function and to the periodic review of the energy trading function.

V. Recommendations

1. CONTROLS SHOULD BE STRENGTHENED TO GIVE GREATER CONFIDENCE UNDER VARYING CONDITIONS

Generally, controls are designed to provide checks and balances on corporate activities while not placing unneeded inefficiencies on those activities. In the case of power marketing and trading, controls are particularly important given the large dollar values of energy transactions at stake as well as large consequences of making or not making certain transaction decisions.

Navigant Consulting's review of the filed procedures, current Westar practices, and the transaction lifecycle produced the following comments regarding controls on energy trading transactions:

Recommendation 1A: Documentation of the asset/non-asset classification process

Issue/Area for Improvement: Typically, separation of responsibilities into front office, middle office and back-office functions is the basis for strong checks and balances for a trading operation. In the case of a utility related trading operation such as Westar, the added responsibility of serving the best interests of the native load customers, requires specific customer responsibilities be assigned as well. For Westar, this customer responsibility centers on the asset versus non-asset decisions made by the URP.

The filed procedures put the responsibility for determining whether a particular transaction opportunity should be accepted as an asset based transaction for the benefit of Westar customers in the position of Utility Resource Planner.

The Utility Resource Planners accept the transactions that they believe, based on known or anticipated market and operating conditions, will be beneficial to native load requirements.

The URP acceptance or rejection of a particular transaction is a key control point in the Westar power marketing and trading process, but currently is documented in two informal ways. First, the general price and quantity parameters for the URP accepting or rejecting purchases and sales are documented on the daily Projection Analysis report published early each morning for the next day's transactions. Second, a particular transaction is accepted or rejected through a verbal acknowledgement. Our review noted no written documentation that particular transactions were accepted or rejected by the URP.

Recommendation: The URP could improve documentation of controls by initialing the asset/non-asset designation for each power sheet to indicate concurrence with whether it was accepted or rejected for the "System". Formalized written documentation will clearly establish this important control point.

Recommendation 1B: Further enhancement of Internal Audit function

Issue/Area for Improvement: As has been noted, Navigant Consulting discussed many of the issues identified during the course of this review with members of the Internal Audit department. This department has played a role in the review of trading activities during the period under review, but that role has been largely related to the review of specific components of the operation and to non-recurring projects such as incentive compensation review issues. While the Internal Audit function has performed these duties in a relatively efficient manner, significant benefits could be derived from a more robust audit function that provides more comprehensive services to the energy trading operations.

Recommendation: The Internal Audit scope and frequency should be expanded to include more reviews of the operational components of Westar's energy trading function. The internal audit department should play a role in routinely reviewing the transactional activity within the department and should place a greater emphasis on the detection of unusual transactions and/or outlier reviews. The Internal Audit department should review transactional data on a monthly basis and should perform reviews on a periodic basis to assess the reasonableness, accuracy, and validity of the information contained within the various electronic systems maintained by the energy trading group. In addition, the calculations of VaR and other risk management measurements should be spot checked on a periodic basis.

Recommendation 1C: Establishment of documentation retention program for relevant trading documents and transactional data

Issue/Area for Improvement: During the course of our review, we determined that full and complete documentation was not available for certain types of data such as OpSym reports, VaR calculations and other types of daily status reports. While adequate retention policies existed for most elements of the transactional documents, the absence of a retention policy for daily risk management, trading criteria (i.e. OpSym) and other types of summary reports makes it more difficult for the Risk Management and Internal Audit functions to perform their various compliance and transactional review tests.

Recommendation: A comprehensive document retention policy should be initiated to cover all documents created and maintained by Westar's energy trading group. Personnel from the Internal Audit and Risk Management functions of Westar should participate in the creation of this policy.

2. CONTROLS SHOULD BE ESTABLISHED TO ENSURE THE ACCURACY AND VALIDITY OF PRICING FOR INTER-COMPANY TRANSACTIONS

Transactions for the "System" are priced in relation to cost or market. The URP has control of the calculation and dissemination of incremental and decremental costs by means of the daily OpSym analysis and Projection Analysis, but relies on the trading floor to provide accurate and comparable market prices that are used to price transactions. While, in most cases of sales and purchases by the System group with third parties in arms-length transactions, there is no inherent value for traders to give the URP anything other than accurate market price information, in the case of System group selling to Marketing group transactions, potential customer versus shareholder value is at stake. The stated policies indicate that sales from the System to the Marketing group are to be the higher of market or incremental cost. In this situation, an inaccurately low market price might result in "System" getting less money than it was entitled to²².

Recommendation 2A: Initiate independent review of market price for inter-company transactions

Issue/Area for Improvement: As we performed our review of the transaction lifecycle, Navigant Consulting looked for whether there was a particular bias in the way transaction

²² A similar situation would occur in the case of a purchase by the System group

pricing occurred towards the "System" or "Marketing" parts of the businesses. We therefore performed additional analysis to determine if prices were consistent across the two parts of the business. The results of our supplemental analysis of the market prices assigned to similar transactions for the "System" and for "Marketing" is shown in the graph contained as Exhibit 5. Based upon our analysis to date, we have found no indication of that prices for "System" and "Marketing" transactions showed any type of particular "System" versus "Marketing" bias.

Notwithstanding the above, it is important to ensure that adequate controls are in place to ensure that all inter-company transactions are based upon appropriate market rates and that these transactions are accurately recorded within the books and records of the organization. While our reviews to date have not identified any type of bias, the potential exists that such a bias could be introduced into the current system.

Recommendation: Controls on the use of market prices should be improved by having them independently monitored by analysis (similar to the pricing analysis above) and/or sampling on a monthly basis by middle or back-office personnel with quarterly review and sampling by Internal Audit to give added assurance that market price is being accurately being quoted on transactions.

Recommendation 2B: Independent spot reviews of internal trade transactions

Issue/Area for Improvement: Because the potential exists for internal trades to be used to transfer cost or benefits of trading between "System" and "Marketing", these transactions should receive added scrutiny. For example, if market conditions such as unit outages, transmission constraints or counterparty problems cause the "Marketing" portfolio to become short power on a particular day, the use of "System" sales to "Marketing" could be a point where the desire to cover the "Marketing" position might create bias in certain transactions. While our review did not indicate any such bias occurred, sensitivity to the potential of such conditions is important.

Recommendation: Controls on internal trades should be improved by having them independently reviewed monthly by middle or back-office personnel with quarterly sampling review by Internal Audit.

3. CLARIFICATION AND UPDATING OF PROCEDURES

Policies and procedures are important roadmaps and rulebooks for people running a business like power marketing and trading at Westar. Much time and effort goes in to drafting them to be accurate and able to survive the test of time. But time does eventually require policies and procedures be updated to reflect changes in the industry and in the company that operates in that industry.

Earlier in this report we commented that clarification was needed to resolve potential interpretation inconsistencies between filed procedures and detailed procedures. In this section of the report, we make comments on additional areas in which procedures could be updated. In general, we recommend clarification of procedures be made in the form of modifying the procedures or, at a minimum, clarifying how the filed procedures should be interpreted to only prohibit the reclassification of a specific asset based transaction to non-asset based and not to prohibit all internal trades such as the balancing of the daily trading book with fairly valued system resources.

Recommendation 3A: Filed procedures should be updated to more clearly reflect Westar's inter-company transactions

Issue/Area for Improvement: Filed procedures are designed to be broad and cover power marketing and trading activities in particular as they pertain to the differentiation, classification and tracking of asset and non-asset transactions. This focus is because the asset and non-asset distinction is the critical dimension of the power marketing and trading process that involves the interests of the customer that regulatory processes are designed to address. As such, the filed procedures should be written at a broad enough level that they do not require constant updating for the normal changes in business operations that occur on a regular basis, while still addressing the issues of particular relevance to customer interests.

As such, we see only a few areas in which the filed procedures should be changed. First, procedures have some places where they are not quite clear with respect to current practices as we commented on in an earlier section. In general, the use of broad functions rather than specific position titles makes the filed procedures (and their appendices) accurate with the current organizational structure. Second, the FERC has changed its chart of accounts with respect to power marketing and trading activities and the filed procedures are now inconsistent with FERC account designations.

Recommendation: Filed procedures need to be updated to more clearly reflect Westar's current practices and FERC chart of accounts.

Recommendation 3B: Detailed internal procedures should be updated

Issue/Area for Improvement: Detailed procedures by their nature require more frequent updates as power marketing and trading has evolved at Westar. The most common dimension where procedures do not match precisely current practices involve the specifics of position titles. In many places positions cited in the procedures do not reflect positions, as they currently exist.

For example, the *Roles and Responsibilities* section cites a number of positions in the middle office that do not currently exist. It is not to suggest that these functions are not being performed, it is just that these functions are being performed by other personnel in the middle/back office. Updates to position titles may in some cases be made more generic to make the procedures more flexible, without compromising their control intent.

We should note here that our previous comments regarding the strengthening of controls may result in additional realignment of functions and positions, particular in the area of risk management and need to be addressed in coordination with any procedures review that is performed.

In addition, current practices have evolved and have interpreted items such as *Portfolio Risk Limits* in ways that are not formally reflected in the detailed procedures. We would also

comment that the limits as written are very restrictive compared to industry practice and could be modified without sacrificing conservatism.

And lastly, the same FERC chart of accounts changes affecting the filed procedures, affect the detailed procedures making the detailed procedures out of date in the *Accounting Compliance* section.

Recommendation: Detailed internal procedures need to be updated to reflect current practices and organizational structure as well as the current FERC chart of accounts. In this update process, limits should be modified to better reflect industry practices.

Exhibits

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Exhibit 1 – Scope of Work

A. Scope of Work

The Kansas Corporation Commission (Commission) and Westar Energy, Inc. (Westar Energy) are requesting expert services to perform a thorough review of the power trading activities and procedures of Westar Energy. More specifically, the Commission and Westar Energy wish to engage Navigant Consulting, Inc. (NCI), an independent consultant which will provide the following services (the "Scope of Work"):

1. Perform a review of the defined procedures filed with the Commission on September 7, 2001, for differentiating, classifying, and tracking asset and non-asset based transactions;
2. Perform a compliance review of the transaction lifecycle;
3. Develop findings and recommendations and provide suggestions for future audits.

This Scope of Work provides an explanation of NCI's proposed approach based on the Order on Power Trading and correspondence entitled the Refined Scope received from Westar Energy on July 25, 2002.

Phase 1 – Perform a Review Westar Energy's Defined Procedures as filed with the KCC on September 7, 2001

In this phase, NCI will conduct a high-level review of the functions directly associated with differentiating, classifying, and tracking asset and non-asset based transactions to ensure that these functions comply with the procedures filed with the Commission on September 7, 2001.

Our proposed tasks will include:

- Reviewing the transaction flow of front, middle and back office functions as directed in the order, including the following:
 - The review of front office functions will include the process for forecasting load and supply, review of OpSym (forecasting model), involvement of Asset Optimization Manager in activities, transfer of data to short-term traders, decision making process to buy or sell generation assets. NCI will make use of existing detailed flow charts developed by Westar Energy and will review models and business processes

through interviews in order to determine the ability of the front office functions to adequately support differentiating, classifying, and tracking asset and non-asset based transactions.

- The review of the mid-office function will involve reviewing how asset based transactions are scheduled and/or classified as a "system" deal.
- The review of the back-office function will involve reviewing how asset based transactions are recorded, as an accounting function, per the deal ticket.

- NCI will also review in broad terms the compensation structure for Utility Resource Planners and trading staff to ensure that there are appropriate incentives for following the procedures. In addition, NCI will provide informal feedback to Westar Energy during the course of this review as to the appropriateness of the organizational structure and whether the effectiveness of the front, middle and back office are reasonably consistent with industry standards. Where improvement opportunities can be identified, NCI will communicate such opportunities to Westar Energy.

Phase 2 – Perform Compliance and Documentation Review of Westar Energy's Activities

In this next phase, NCI will perform a compliance review with a focus on the transaction lifecycle to determine if the filed procedures are being followed. The review of the transaction lifecycle will include an examination of the documentation associated with the various power trading transactions. To complete this portion of the engagement, NCI will perform a review of Westar Energy's compliance with its own procedures. This will be accomplished through the review and testing of a representative sample of transactions. NCI will develop a sampling plan to test Westar Energy's compliance with its various procedures. NCI will draw a representative number of sample transactions from all transactions for the defined compliance period based on a variety of different criteria including seasonality, product, category (financial/physical), and value range. Within the scope, NCI anticipates selecting approximately 75-100 transactions as a representative sample based on the following criteria:

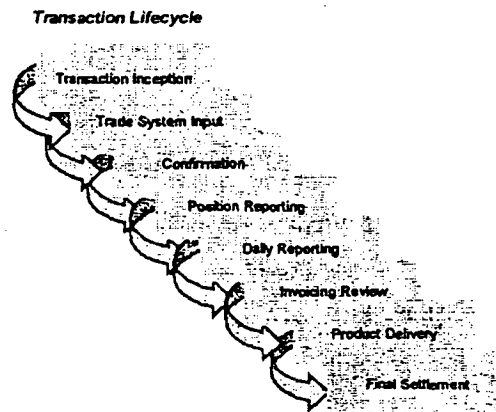
- Look back to the period October 2001 through July 2002.
- Selecting sample periods which are material from the perspective of revenue and MWh traded.

- Sampling 3-5 days of trades for 1-2 unique periods and potential 1-2 days of random, "normal" operations (e.g., December outage period, July hot weather period, other unusual events), with all such sampled days that are selected to be mutually agreed between Westar Energy, the KCC and NCI.

In addition, NCI will also sample a representative number of hourly (real time) trades for this assessment. While NCI will ensure that hourly trades are reviewed, a detailed examination of hourly trades will not be conducted unless material non-compliance issues are discovered in the initial sample. If material non-compliance issues are discovered, in the audit of hourly trades, and the parties agree that additional review is required, NCI will require a "change order" to the budget and scope, and any such work will be considered additional to the scope and budget contained herein. In addition, if there is a requirement to select a sample size greater than 75-100 transactions as set forth above as a result of material non-compliance issues being uncovered, NCI will require a "change order" to the budget to meet the additional scope required.

NCI will perform a compliance review that will include tracking the entire transaction lifecycle - from deal inception, execution, deal system inputting, invoicing, and reporting to final delivery or payment, as illustrated in Figure 1 below. This review will compare these targeted transactions to stated policies and procedures. NCI will review each transaction in detail to ascertain how the deal was entered into Westar Energy's tracking system, how the deal was confirmed, how the confirmation was checked, and the types of controls in place to ensure that transactions are properly accounted for. In addition, transactions will be evaluated to ensure that they meet the definitions contained in the filing, are handled appropriately by functional groups, and are subject to adequate controls.

FIGURE 1: TRANSACTION LIFECYCLE



In conjunction with our compliance review, NCI will perform various tests of the documentation and tracking information that exists for each selected transaction. Each transaction review will include workpaper documentation identifying all relevant information used in tracking the transaction lifecycle and in completing the assessment.

Phase 3 – Prepare Findings and Recommendations

This phase will focus on developing and communicating our findings, as defined by the Scope of Work, to Westar Energy and the Commission. In addition, NCI will provide suggestions as to how future audits of energy trading transactions could be performed efficiently. NCI will discuss our draft findings with Westar Energy and the Commission's Staff in a joint session (or with either party separately). This will allow all parties to understand NCI's findings and will enable the parties to have some level of input into NCI's final report which shall be limited to Scope of Work. We understand that NCI's report, with redacted confidential information, will become a public document and we intend to work closely with the Commission and Westar Energy to make sure the final report meets their objectives. Notwithstanding this, NCI's report will be its independent opinion of the situation based on the information provided to NCI at the time of the engagement. NCI will not be providing any testimony or other litigation support to Westar Energy or the KCC in connection with the Scope of Work set forth in this proposal.

B. Price Proposal

NCI proposes a lump sum not-to-exceed price for professional services and expenses of \$160,000. The price breakdown (including allocation of expenses) by phase of work is as follows:

- Phase 1 – \$40,000
- Phase 2 – \$90,000
- Phase 3 – \$30,000

NCI believes that this price is highly competitive for the level of experience and commitment of senior staff that will be on site to execute the work program. NCI's approach to the engagement is to fully deploy a combination of highly qualified senior staff members with more junior staff, who have extensive process-based consulting skills and very strong quantitative skills. In this regard, our clients get the full value of our experience. We also have the capability to leverage the collective knowledge of our Energy and Financial and Claims practices to the benefit of the Commission and Westar Energy.

C. Schedule

NCI proposes to begin the work at or around the week beginning September 16, 2002 and will take approximately two months to complete the scope of work. We would anticipate a kick-off meeting with Westar Energy and the Commission early during the week of September 16 and that Westar Energy would be able to provide NCI with background material, including organization charts and process flow diagrams, at least two weeks prior to the kick-off meeting. NCI anticipates that a draft final report will be prepared and delivered to Westar Energy and the Commission at or around November 11, 2002. A meeting to discuss the findings will be scheduled shortly after submission of NCI's draft final report. Subsequent to the meeting, NCI will prepare the final report, including a redacted public version of NCI's findings.

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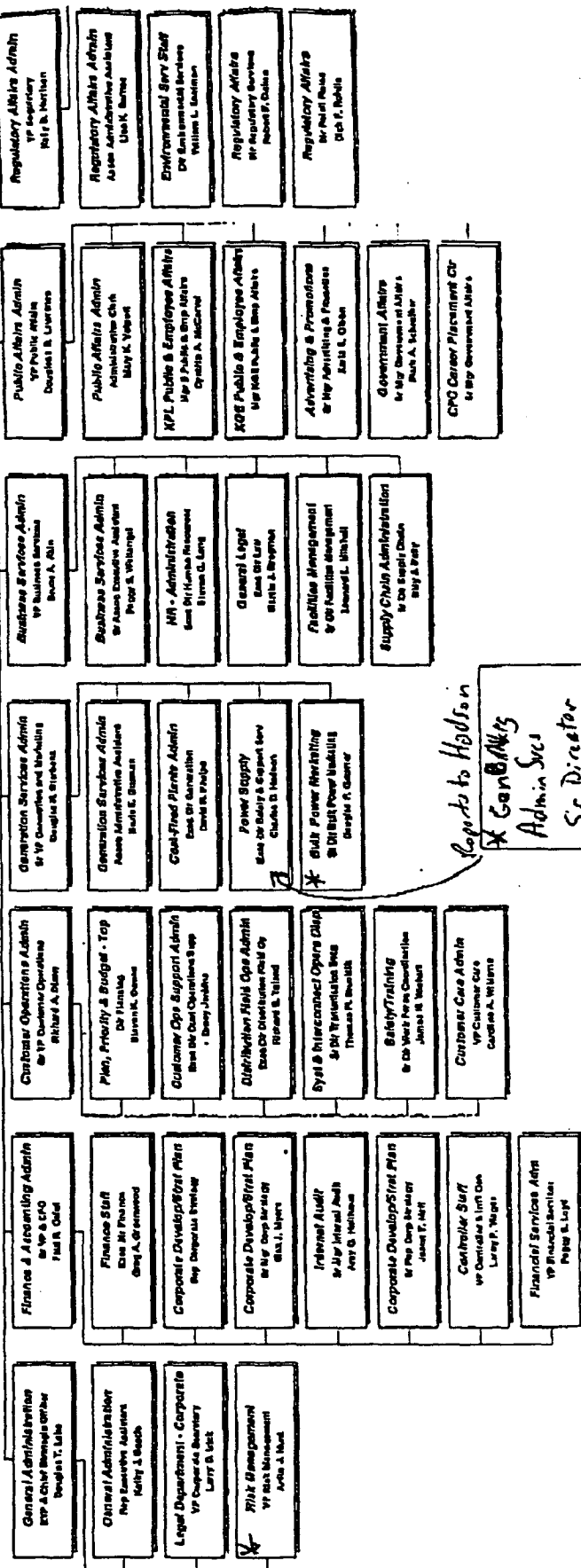
Exhibit 2 – Organization Charts

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Westar Energy, Inc.
General Administration

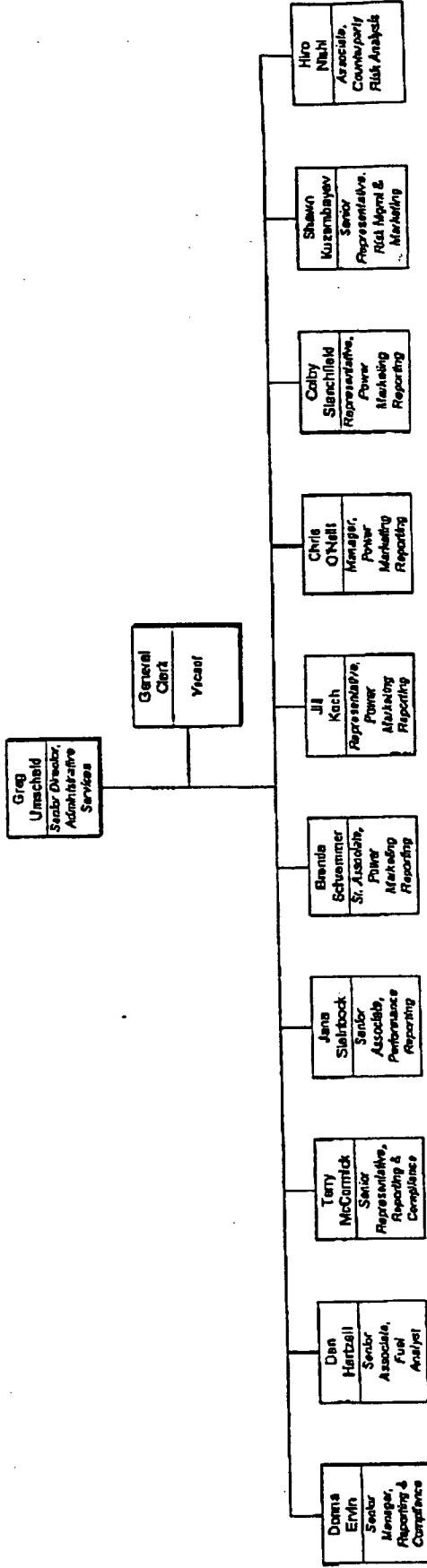
General Administration
VP Public Affairs
Douglas B. Lyles

General Administration
VP Business Services
Bryan A. Allen



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Generation & Marketing
Administrative Services - RA 05853



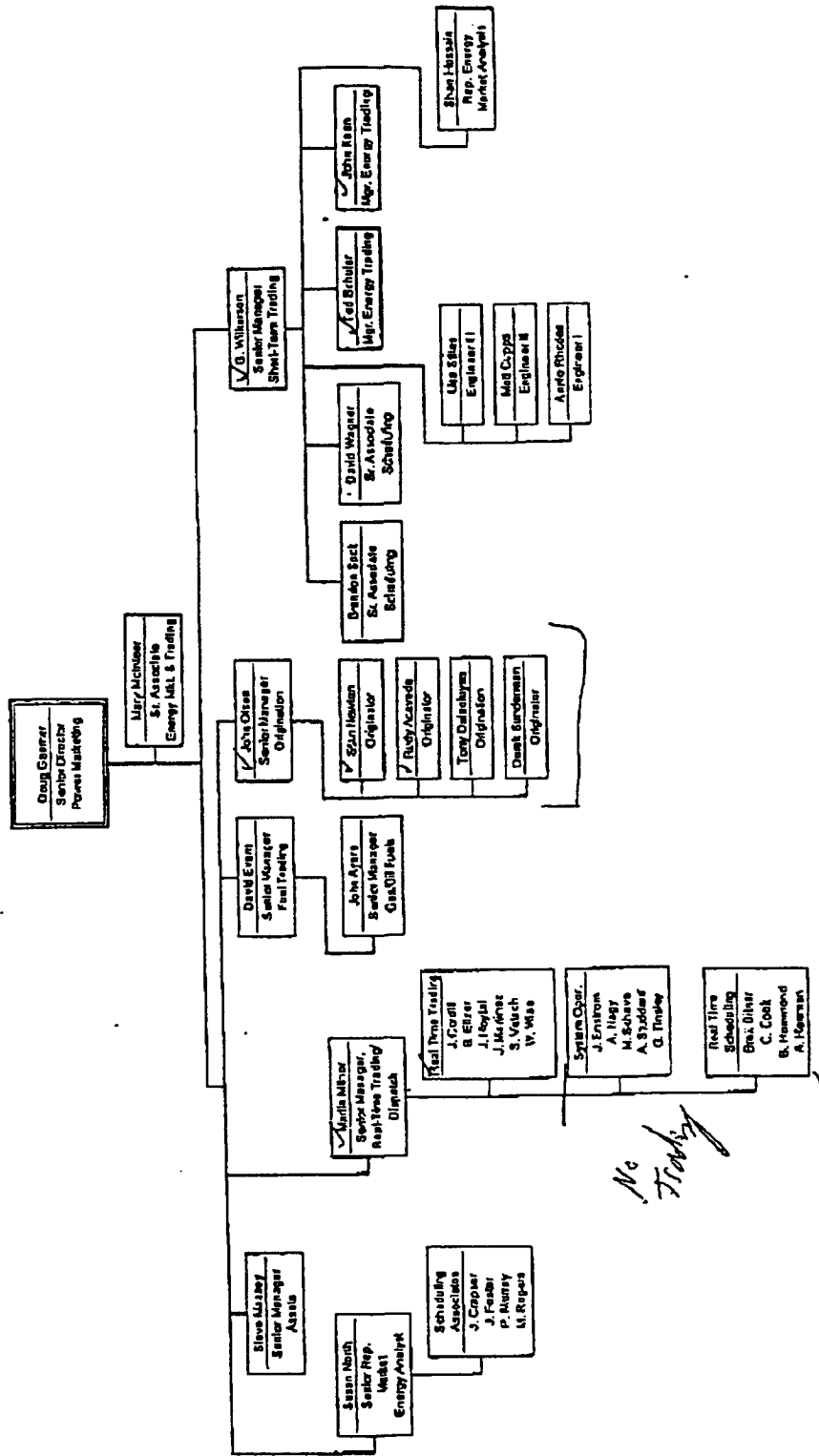


Exhibit 3 – Filed Procedures

**WESTERN RESOURCES PROCEDURES
FOR DIFFERENTIATING, CLASSIFYING AND
TRACKING ASSET AND NON-ASSET BASED TRANSACTIONS**

Background

In its Order on Rate Applications in Docket No. 01-WRSE-436-RTS, dated July 25, 2001, the Commission ordered Western Resources and Kansas Gas and Electric Company (hereinafter referred to as "Western Resources" or "Company") to "provide their written procedures for differentiating, classifying and tracking asset and non-asset based transactions."¹ This filing is made in response to that direction.

Asset Based Transactions

Asset based transactions are purchases that are intended to serve native load requirements within the Western Resources control area and sales where the energy is expected to come from Western Resources generating units. Generally, asset based transactions will affect system generation operations by causing Western Resources to either increase or decrease the output of its generating units.

Non-Asset Based Transactions

Non-asset based transactions are those which are not intended to serve native load requirements within the Western Resources control area. Generally, non-asset based transactions will not affect system generation operations by causing Western Resources to either increase or decrease the output of its generating units. The risk of these transactions is borne by Western Resources shareholders not customers.

Asset Based and Non-Asset Based Transactions²

The traders³ and the Utility Resource Planners are in hourly communication so that the traders are aware of the parameters of transactions in which the Utility Resource Planners may be interested and the Utility Resource Planners are aware of the terms and conditions of prospective sales and purchases identified by the traders. All potential power transactions which meet the parameters provided by the Utility Resource Planners are made available to them. The Utility Resource Planners accept the transactions that they believe, based on known or anticipated market and operating conditions, will be beneficial to native load requirements. Transactions accepted by the Utility Resource Planners are entered into the Trading System⁴ as asset based transactions. Any transaction which is classified as an asset based transaction when it is executed, will, from that time

¹By order of August 27, 2001, the Commission extended the time for this filing to September 7, 2001.

²A flowchart which shows the processes described herein is attached as Appendix A.

³The composition, responsibilities and interactions within the Western Resources Power Marketing Group are generally described in Appendix B.

⁴The computer software used in the Trading System is listed in Appendix C.

forward, remain an asset based transaction until the transaction is closed out.

Any trade which is executed, but not accepted by the Utility Resource Planners, is initially classified as a non-asset based transaction. From that time until the transaction is closed, each non-asset based transaction is available to meet the needs of the Utility Resource Planners. If the Utility Resource Planners decide, based on known or anticipated market and operating conditions, that they need to utilize the transaction for the benefit of native load requirements, the transaction may, at the discretion of the Utility Resource Planners be diverted to serve retail and firm wholesale customers. If that occurs, the transaction will be recorded as asset based.

Tracking of Asset and Non-Asset Based Transactions

Once a transaction has been initially classified as either asset based or non-asset based, a Power Deal Sheet (see sample form attached as Appendix D) will be prepared by a trader. The Power Deal Sheet details commercial terms and is marked to indicate if the transaction is an asset based transaction.⁵ All transactions are entered into the Trading System on a daily basis. Data entry is independently verified by back office personnel through the confirmation process and broker reconciliation reports.

Once the Power Deal Sheet has been marked and entered into the Trading System, the Back Office tracks it until it is closed and is responsible for accounting for the transaction properly. Accounting for asset based and non-asset based transactions is done in accordance with Generally Accepted Accounting Principles (GAAP) using the Federal Energy Regulatory Commission (FERC) chart of accounts. Asset based transactions flowing through the Western Resources control area are recorded in accounts 447 (revenue), 555 (expense), and 565 (transmission expense) in the month settled. Asset based transactions that do not flow through the Western Resources control area are recorded in accounts 451 (revenue) and 557 (expense) in the month settled. Non-asset based transactions are recorded in accounts 417 (revenue) and 417.1 (expense).

⁵Asset based transactions are marked "System." Non-asset based transactions are either not marked or marked "Marketing."

Appendix B**Power Marketing Group Organizational Structure**

The Power Marketing Group is composed of basically three sub-groups: the Front Office, the Middle Office and the Back Office. The composition, roles and responsibilities and interactions of each sub-group are described below.

Front Office

The Front Office consists of the traders, schedulers and the Utility Resource Planners. The traders are responsible for identifying and executing transactions. The Utility Resource Planners are responsible for determining which transactions are suitable for native load customers.

The role of the traders is to locate transactions in hourly, daily, and forward markets which will optimize the value of the Company's trading portfolio within the constraints of their authorized trading limits and the Company's value at risk parameters. Traders are allowed to enter into speculative transactions that are consistent with the risk profile and policies of the Company. The risk associated with these transactions is borne by Western Resources shareholders.

The Utility Resource Planners are responsible for ensuring safe, reliable and economic dispatch of generating units. To fulfill that role, the Utility Resource Planners communicate throughout each day with the traders to identify transactions that are consistent with the needs of native load customers and the utility risk profile. Utility Resource Planners are not allowed to enter into speculative transactions.

Middle Office

The Middle Office consists of Risk Management Personnel.

The Middle Office is responsible for risk management functions. Risk management functions include contract administration, establishment of credit, and compliance with established policies and procedures. Risk management evaluates the creditworthiness of potential counterparties and ensures that individuals monitoring risk exposures are completely independent from trader reporting responsibilities.

Risk management personnel report to the Risk Oversight Committee (ROC) and Generation Services senior management concerning daily trading activity and advises the ROC, Generation Services senior management and the Manager, Bulk Power Trading when authority limits are breached. Risk management also is responsible for ensuring accurate entry of transactions in the trading book and for maintaining independence from traders in the process of entering data in the trading book.

Back Office

The Back Office consists of Interchange Accounting Personnel.

The Back Office manages the accounting, billing and reporting of all trading and interchange activities and ensures the accuracy, timeliness and integrity of trading and financial reporting systems.

Appendix C

Software Utilized by Power Marketing Group

The Power Marketing Group utilizes several types of software that together form the Trading System. A description of the types of software used and its function is provided below:

Custom designed Microsoft Excel/Access/Visual Basic spreadsheets - Used by traders to track their individual transactions.

Microsoft Access database software - Used to track all transactions relating to the forward market.

Oracle database software - Used to process all transactions that are settled each hour.

Access Database/Risk Valuation System - Used to value forward positions compared to the market and to determine Value at Risk (VAR).

Exhibit 4 – Detailed Internal Procedures



*Risk Management
of
Power Trading*

Principles, Policies
&
Procedures

RISK MANAGEMENT DEPARTMENT

AUGUST 2001

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Appendix

Transaction Flowchart

1. Introduction

Reasons for Risk Management

Risk management practices are utilized by Western Resources' Power Trading organization in order to quantify, measure and minimize risk in power trading activities. Western Resources is involved in trading activities primarily to minimize risk from market fluctuations, to maintain a market presence and to enhance system reliability.

Dimensions of Risk Management

Key Operations Risk Management Principles

Minimizing operations risk is fundamental in preventing derivatives debacles. The following guidelines and principles are the basis for investment in key personnel, critical processes and required technology to hedge against operations risk:

- Senior management will be involved in and provide informed oversight and approval of all trading strategies.
- A Risk Manager will independently verify the trading book, validate valuations and monitor trading limits.
- Independent internal audits will be performed to verify adherence to Western Resources' Power Trading policies and procedures.
- Policies and procedures will be clearly documented and changes will be broadcast throughout the trading organization.
- A Risk Manager will monitor compliance to limits such as authorized trading limits and counterparty credit limits.

Key Market Risk Management Principles

Managing market risk is critical in the volatile electricity market. The following are market risk management principles:

- Independent execution of middle office functions and responsibilities is essential for managing market risk.
- Monitoring transactions and positions promotes adherence to risk limit policies.
- Reviewing pricing models and valuation systems will ensure that the proper risk measurement tools are being used throughout the trading organization.

For the independent quantification of market risks, the Risk Management Department will consider the following sub-dimensions:

- Basis risk
- Correlation risk
- Transmission risk
- Forward and option-based derivatives risk
- price (delta)
- convexity (gamma)
- volatility (vega)
- time decay (theta)
- Market liquidity risk
- Corporate investing and funding risk

Key Credit Risk Management Principles

It is the intent of Western Resources to limit the risk exposure of counterparty non-performance in power trading transactions. Accordingly, Western Resources will develop guidelines for determining the credit worthiness of counterparties. Documentation will be maintained that demonstrates that counterparties have been reviewed at periodic intervals to ensure that they have sufficient financial strength to meet their obligations. *The Credit Manual established by the Risk Management Department will explain and detail credit descriptions, parameters and practices.* In all cases, Western Resources will structure transactions to ensure that there is adequate recourse in the event of counterparty non-performance:

- Credit risk on individual derivatives measures the current and potential replacement cost due to counterparty default (on a single transaction).
- Portfolio credit risk measurement quantifies the total credit exposure on a portfolio of transactions with Western Resources' counterparties.
- Current and potential exposure will be measured in order to gain further understanding of credit exposure. Current exposure is the replacement cost or market value of all derivatives transactions, while potential exposure is an estimate of the future replacement cost of derivatives. This is done on a transaction-by-transaction basis.
- Policies and procedures to manage credit risk are addressed through counterparty credit evaluations and credit limit monitoring.
- Settlement risk arises from the time lag between deal execution and actual settlement. It can be mitigated through payment netting provisions established in master agreements.

2. Goals and Objectives

Current Goals

- Manage volatility effectively in daily, forward and regional markets.
- Develop expertise to offer unique pricing alternatives and value added services to customers.
- Develop risk management skills in the wholesale and retail marketing of power.

Current Product Profile

Western Resources currently markets energy in the Midwest region of the United States, and controls over 5,700 MW of generating assets in the state of Kansas.

Products including power, gas, oil, and coal can be categorized along several dimensions:

- ITS
- Non-ITS
- Liquidated damages
- Requirements contracts
- Utility-to-utility wholesale transactions
- Trading OTC Forwards and Options
- Trading Futures and Options
- Financial or physical settlement
- Capacity rights
- Transmission rights
- Etc. (This encompasses the possible creation of unique products associated with the evolving energy industry.)

Current Risk Propensity

Western Resources is committed to structuring a highly successful energy supply business. Owner value will be maximized by generating and dispatching power efficiently, optimizing cost and resource management, and aggressively marketing power and generation related services. *Western Resources believes that success in trading activities will help to create success in its utility business.*

Industry and Market Perspective

Western Resources believes that competition among electricity providers will continue to intensify, with two major results. First, competition will lead to reduced margins throughout the industry. Second, competition will force transactions to increase in both quantity and complexity, requiring additional resources to be deployed for marketing activities.

Also, electricity has experienced extreme price volatility compared to other traded commodities. While new marketing opportunities may emerge rapidly, they also expose Western Resources to significant business risks: operational, market, and credit. Western Resources will emphasize responsible risk taking in its operations.

Western Resources intends to become a leading wholesale electric marketing organization in the Midwest. Western Resources will continue to concentrate on maximizing the price received for energy generated by assets and minimizing the price of energy purchased on behalf of native load customers. Western Resources will meet the reliability criteria established by the North American Electric Reliability Council (NERC). Generating assets will be operated in such a manner that system reliability will not be impaired.

Guidelines

Transaction Identification

Policy for Asset Related Transactions

The goal of this policy is to maximize the value to rate payers by supplying reliable power at the best price through use of the company's generation assets, purchasing power, and selling at profitable market rates. This is accomplished utilizing load forecasting models and marketing strategies.

The load forecast is used to develop system requirements and resources in the short and long term time frames. Factors influencing this include native load, Southwest Power Pool (SPP) operating reserves, and transmission requirements. This forecast data is the basis the marketing group uses to locate opportunities for review by the system control group, which is given the opportunity to accept or reject each deal.

Policy for Non-Asset Related Transactions

The goal of this policy is to increase shareholder value by capturing third-party market value after asset related system control requirements have been met. This is accomplished by speculating in various commodities utilizing derivative products. Trading is conducted in accordance with the Trading Policies and

Procedures. The marketing group does not have generation resources available, therefore hourly purchases and sales must be balanced. If the non-asset related transactions have an hourly imbalance (purchases and sales are not equal), the asset related group is favorably compensated for the energy imbalance. If the asset related group is selling to the non-asset related group the price is the greater of the incremental generation cost or the market value of like sales from Generation assets. If the asset related group is buying it is the lower of decremental generation cost or market value of like purchases for load. This same pricing methodology is utilized when the system has resources available to sell or needs to purchase power to meet load requirements.

Authority Limits

The total dollar loss is determined by a daily MTM (Mark to Market) valuation performed by a Risk Manager and a year-to-date settlement valuation performed by interchange accounting, and does not represent the notional value of trades. These authority limits are cumulative in nature.

Authority Limits

Based on Total Marked-to-Market Portfolio

Authority Level	MTM Net Book Dollar Limit
Executive Director, Power Supply	\$0.5 million
Vice President, Commodity Strategy	\$1.0 million
Executive VP, Electric Operations	\$1-2 million
Chief Executive Officer	\$2-5 million
Board of Directors	More than \$5 million

Based on Total Notional Portfolio

Authority Level	Notional Value Transaction Limit
Manager, Bulk Power Marketing	\$1.0 million
Risk Manager	\$1-3 million
Vice President, Commodity Strategy	\$3 million and above

Liquidation Procedures

A Risk Manager will independently mark the book and have the authority to liquidate positions to comply with defined limits or align activities with the corporate risk threshold. *Any time positions are liquidated, the Risk Management Department will document and report actions taken to the ROC (Risk Oversight Committee).*

Portfolio Risk Limits

- The delta limit for the entire portfolio is 300MW per month. *This limit only encompasses on-peak transactions.*
- The Senior Director of Risk Management, or the appropriate designee must approve any transaction with a notional value in excess of \$1,000,000. (The notional values of the options in the portfolio are valued using the premium paid or received, not the contract price.)
- The maximum portfolio VAR (Value at Risk) is set at \$300,000 each for the natural gas and for the electric portfolios. This value is calculated using the risk management software packages and assumes a historical correlation matrix and a 95% confidence interval. Only LD (liquidated damages) and Firm physical transactions will be included in the VAR calculation.
- In the event the portfolio loss for either the natural gas or the electric portfolios exceeds \$250,000 in a single day the CEO and Risk Oversight Committee will be notified directly by the Senior Director of Risk Management.
- In the event the portfolio experiences a loss in excess of \$500,000 of its highest daily closing peak, a hold can be placed on all trading strategies other than pure arbitrage transactions. An immediate meeting will be held by the Risk Oversight Committee in order to determine whether liquidation of positions is warranted.
- In the event the portfolio value exceeds a loss of \$500,000 during the course of a calendar year (This number is calculated as an actual loss, not a paper loss. An example: the portfolio at the beginning of January 1 has a Gross Profit of \$1,000,000 and during the course of the month gains \$500,000, which gives the portfolio a total Gross Profit YTD of \$1,500,000. If, in February, it has a trading loss of \$500,000, this would bring the Gross Profit YTD to \$1,000,000. This represents a paper loss of \$500,000, but there is not an actual loss associated with the portfolio.) all open traded hub positions that do not support a physical position which requires special exit

considerations will be liquidated at the discretion of the Vice President, Commodity Strategy. A hold will be placed on all trading strategies other than pure arbitrage transactions until the Risk Oversight Committee conducts a review of the Marketing and Trading Department's activities.

- Bulk Power Marketing may sell liquidated damages in all months of the year under the following stipulations:

(a) If an LD product is trading for \$50 or more, then short positions must be exited based on the following schedule:

- January - December 1
- February - December 1
- March - February 1
- April - March 1
- May - April 1
- June - May 1
- July - May 15
- August - May 15
- September - August 1
- October - September 1
- November - October 1
- December - November 1

(b) In the event the month is not trading at \$50 or above on the schedule date but subsequently rises to more than \$50, then the short LD position must be exited within two business days. A maximum of two short LD positions will be permitted for months trading above \$50. A maximum of five short LD positions will be permitted for months trading below \$50.

- Intra-Month Products

(a) Bulk Power Marketing will be allowed to maintain short LD positions within the month provided that the price of the product being traded is below \$50.

(b) In the event the price of the product exceeds \$50 then the short LD position must be liquidated by the end of the business day.

3. *Organizational Structure, Roles, and Responsibilities*

Front Office

Composition

- Real Time Traders
- Energy Traders
- Sr. Energy Traders
- Utility Resource Planners

Roles and Responsibilities

Real-Time Traders

- Initiates or responds to deals with counterparties in the hourly markets.
- Structures transaction price and terms.
- Enters trade details into Trading System.
- Reports to a Sr. Trader.

Energy Traders

- Coordinate activities of trading desk.
- Initiates or responds to deals with counterparties in the day and term markets.
- Structures transaction price and term in the day and forward markets.
- Coordinate the input of all trade details into the Trading System.
- Hedges positions in order to minimize certain types of risk.
- Reports to the Manager, Bulk Power Marketing.

Sr. Energy Traders

- Initiates or responds to deals with counterparties in the day and term markets.
- Structures transaction price and term in the day and forward markets.
- Coordinates the input of all trade details into the Trading System.
- Hedges positions in order to minimize pertinent types of risk.
- Develops trading strategies.
- Coordinates activities of assigned area of the trading desk and trading book.
- Works with Risk Management personnel in order to optimize book within constraints of authorization and VAR limits.
- Reports to the Manager, Bulk Power Marketing.

Utility Resource Planners

- Ensure safe, reliable, and economic dispatch of generating units.
- Comply with Regulatory policies and procedures to maintain system integrity.
- Analyze generating capability versus load requirements to maximize system economics.
- Review all potential transactions on behalf of load requirements. Determine and accept those transactions that are beneficial to load requirements.

Interactions

Real-Time Traders

- Execute needs and requirements as communicated by Utility Resource Planners.
- Communicate with all Energy Traders of deals completed.
- Notify Sr. Trader of all transactions.
- If necessary, clarify and solve problems with Middle and Back Offices.

Energy Traders

- Execute needs and requirements as communicated by Utility Resource Planners.
- Communicate with all Energy Traders of deals completed.
- Notify Sr. Trader of all transactions.
- If necessary, clarify and solve problems with Middle and Back Offices.

Sr. Traders

- Execute needs and requirements as communicated by Utility Resource Planners.
- Gather details of trades completed in assigned area from traders.
- Work with Sr. Director of Risk Management on counterparty credit status.
- Develop price and structured product strategies with Energy Traders.
- Ensure effective information flow from Front Office to other departments.

Utility Resource Planners

- Communicate to trading organization the short-term and long-term incremental and decremental system requirements.
- Provide timely updates of system requirements to trading organization.

Middle Office

Composition

- Senior Director, Risk Management
- Manager, Risk Management
- Associates, Risk Management

Roles and Responsibilities

The Middle Office is where responsibility for risk management functions is operationalized.

Senior Director, Risk Management

- Ensures that individuals monitoring risk exposures are completely independent from trader reporting relationships.
- Responsible for the independent monitoring and analyzing market and operational risks, and reporting findings to senior management.
- Responsible for the independent evaluation and review of the credit worthiness of Western Resources' counterparties, and communication of results.
- Develops and outlines appropriate usage for various trading strategies.
- Assists in defining the scope of the types of transactions Western Resources will engage in (e.g., financial, options, swaps).
- Disseminates high level summary report of positions and VAR to senior level management.
- Verifies prices on complex derivatives.
- Tracks changes in pricing model.

Manager, Risk Management

- Maintains an independent and accurate book.
- Generates daily counterparty credit reports, position reports, and VAR analysis results for senior management.
- Reports to Senior Director, Risk Management any breaches of authorization limits.
- Calculates VAR on a daily basis.

Associate, Risk Management

- Generates daily counterparty credit reports.
- Facilitating contract administration.
- Facilitate financial analysis.

Interactions

Senior Director, Risk Management

- Communicates with Manager, Bulk Power Marketing, Generation Services' senior management, and ROC when authority limits are breached.
- Communicates with ROC and Senior Management on daily activities via summary reports.

Manager, Risk Management

- Maintains independence from traders for marking the book.
- Communicates any discrepancies in book to Senior Director, Risk Management.
- Alerts Executive Director, Risk Management of any breaches of VAR or book authority limits.
- Develops new models for risk management systems in conjunction with Senior Director, Risk Management.
- Develops risk analysis tools in conjunction with Senior Director, Risk Management.
- Initiates and modifies contracts with counterparties.

Associate, Risk Management

- Develops new models for risk management systems in conjunction with Senior Director, Risk Management.
- Develops risk analysis tools in conjunction with Senior Director, Risk Management.
- Initiates and modifies contracts with counterparties.

Back Office

Composition

- Senior Manager, Interchange Accounting and Credit
- Representative, Interchange Accounting
- Associate, Interchange Accounting
- Confirmation Clerk *Roles and Responsibilities*

Senior Manager, Interchange Accounting and Credit

- Manages the accounting, billing and reporting of trading activities.
- Ensures the accuracy, timeliness and integrity of reporting systems.
- Coordinates internal profitability reporting.
- Assists Sr. Director, Risk Management in credit risk evaluation and monitoring programs.
- Validate transaction identification, terms and conditions.

Representative, Interchange Accounting

- Prepares monthly billing invoices.
- Verifies system recording of trading transactions.
- Prepares daily accounts receivable and accounts payable record.
- Prepares internal and external trading activity reports.
- Validate transaction identification, terms and conditions.

Associate, Interchange Accounting

- Prepares monthly billing invoices.
- Verifies system recording of trading transactions.
- Prepares daily accounts receivable and accounts payable record.
- Prepares internal and external trading activity reports.
- Validate transaction identification, terms and conditions.

Confirmation Clerk

- Verifies trading activity with counterparties.
- Verifies system recording of trading transactions.
- Facilitates billing and payment processes of transactions.
- Responsible for having confirmations generated and sent to counterparties.

InteractionsSenior Manager, Interchange Accounting and Credit

- Communicates with Middle and Front Offices to report any delays of accounts receivable.
- Works in conjunction with Middle and Front Offices to ensure proper accounting for various derivative transactions.

Representative, Interchange Accounting

- Reconciles any differences with Front Office on differences in billing with approved counterparties.
- Provides assistance to the Front Office in the event that the trading system did not record proper trade details.

Associate, Interchange Accounting

- Reconciles any differences with Front Office on differences in billing with approved counterparties.
- Provides assistance to the Front Office in the event that the trading system did not record proper trade details.

Confirmation Clerk

- Works with trader of record to ensure all of the proper counterparty information has been provided before generating a confirm.
- Brings confirm discrepancies to the attention of the Manager, Bulk Power Marketing and the Senior Director, Risk Management.
- Provides assistance to the Front Office in the event that the trading system did not record proper trade details.
- Provides reconciliation assistance to Front Office in the event that the trade details were not properly entered into the trading system.

Risk Oversight Committee (ROC)

Composition

- Senior Director, Risk Management (Committee Chairman)
- Executive Vice President, Chief Strategic Officer
- Executive Vice President, Chief Financial Officer and Treasurer
- Executive Vice President, Electric Operations
- Vice President, Generation Services
- Vice President, Commodity Strategy
- Vice President, Financial Services
- Controller
- Executive Director, Power Supply
- Manager, Risk Management

Roles and Responsibilities

- Oversee risk management activities.
- Establish the strategic direction and risk threshold for electric operations.
- Define the policies, procedures, and controls for the implementation of effective risk management.
- Review current trading operations and policies at monthly meetings.

Interactions

The responsibility of the ROC is to ensure that the Bulk Power Marketing's trading activities and book positioning are aligned with Western Resources' risk appetite. Additionally, the ROC should have the insight and perspective to understand all potential risks affecting the trading organization at present and in the future. Achieving this will require that the ROC interact with Western Resources and Generation Services' senior management, Risk Management, Legal, Internal Audit, Finance and Human Resources on a regular basis.

The ROC will meet on a regular basis to discuss risk management, operating processes, trading controls and policies review authorization(s) and conduct educational discussions. The ROC chairperson has the overall responsibility for organizing and conducting ROC meetings. Additional meetings can occur at the discretion of the ROC chairperson.

4. *Key Trading Processes*

Front Office

Trade Capture Process

A deal ticket is prepared detailing commercial terms and identified as an asset related or non-asset related transaction based on direction from the Utility Resource Planners. All trades are entered into the Trading system on a daily basis. Data entry is confirmed by Back Office through confirmation process and broker reconciliation reports. It is imperative that the trades are entered into the system as soon as possible in order to track the trades as the market moves as well as to process the transaction efficiently through the middle and back offices.

Middle Office

Operations Risk Management

Liquidation Procedures

- Authority limits are based on total dollar amounts of the MTM portfolio. The authority limits increase by level of management responsibility at Western Resources. Traders can go beyond authority limits with approval from next level of management. Approvals for exceeding trading limits shall be documented. Approval and documentation must be assembled on the same day.
- Dollar limit is determined by a daily MTM valuation performed by a Risk Manager.

Escalation Procedures

A Risk Manager will independently mark the book and have the authority to liquidate positions to comply with defined limits or align activities with the corporate risk threshold. Specifically,

- A Risk Manager will have the authority to liquidate any position at his/her discretion.

- The Risk Manager has the discretion to liquidate positions to maintain a book of approximately \$300,000 daily VAR, and MTM values pursuant to authority guidelines. A Risk Manager must notify the ROC and CEO personally anytime the daily VAR exceeds \$300,000.

Market Risk Management

Portfolio Risk Limits

The sum total of Western Resources' positions will produce a net portfolio position. In its risk management activities, Western Resources will measure its VAR by defining forward price curves in the energy markets and estimating the probability of expected changes in value due to market movements.

Mark to Market

The trading book will be 'marked to market' (MTM) on a daily basis. Where definitive contract prices are available i.e., broker quotes, mid-market prices will be used. Prices will be assessed independently of the traders. The Risk Management Department will maintain independent forward curves where applicable.

Market forecasts will be reviewed and updated on a regular basis to reflect changing market conditions. Any issues with the MTM will be documented and reported by the Risk Management Department to the ROC.

Measuring Market Risk

Market 'Value at Risk' (VAR) based on MTM prices will be measured as a single figure on a daily basis (or deal basis for different risk, size, or product transactions) and compared with the defined market risk limits. A Risk Manager, independent of the traders, for management reporting will undertake this process. All appropriate components of the market risk will be considered and factored into the VAR calculation, depending on the market and specific commodity traded.

MTM Methodology

Western Resources will account for its risk management activities with MTM valuation. Data used to MTM must incorporate outside sources for valuation of open positions whenever possible by a Risk Manager.

Limit Monitoring

The Risk Management Department is responsible for monitoring the limits outlined below:

- Individual trader authority levels are based on ability and experience. Traders may only trade at or below these stated approved limits. Willful violations of established trading limits is grounds for immediate dismissal.
- Value-at-Risk (VAR) measures the worst expected loss over a given time interval, under normal market conditions, at a given confidence level.
- Wholesale Marketing's overall daily VAR limit is \$300,000 and is based on a 95% one-tailed confidence interval, calculated on a one day holding period and assumes a normal distribution.

Breach of Individual Trader Limits

In the event that a trade is completed, and following evaluation by a Risk Manager is found to exceed one or more of the traders' authority limits, the following procedure will be followed:

A Risk Manager will write a memo identifying the trades in questions and specific details of which limits have been breached. This, together with a copy of the trade document, will be sent to the members of the ROC.

Breach of Portfolio Risk Limits

In the event that a trade or series of trades are completed which take the book beyond its approved and acceptable risk limits, the following procedure will be followed:

- Reason for the exceedance needs to immediately be identified and documented by a Risk Manager.
- A Risk Manager will suspend all trading activity that would further increase the risk of the portfolio. To do this, all relevant traders must be contacted and informed. In addition, the ROC will be notified of the action taken.
- Willful violation of established portfolio risk limits is grounds for immediate trader dismissal.

Recorded Telephone Lines

This method of monitoring is currently used by the Wholesale Marketing's Trading team in order to resolve trader disputes and, in certain circumstances, provide a back up to verify trader confirmations.

Back Office

Administration Procedures

- A transaction confirmation is prepared and forwarded to counterparty.
- If there is a payment required at execution an invoice is prepared or payment is made.
- The transaction is entered in the energy accounting database used to track forward deals.
- During the settlement month, each deal is entered into the Interchange Transaction Scheduler (ITS) by hour, identified as an asset related or non-asset related transaction.
- Each non-asset related transaction entered into by the marketing group will include the estimate for transmission expense.
- If the non-asset related portfolio has an hourly imbalance, the corresponding purchase and sale is transacted with an independent third party.
- At month end all aggregate purchases and sales are verified with each counterparty, at which time invoices are prepared and payments authorized.

Accounting Compliance

Accounting is done in accordance with Generally Accepted Accounting Principles (GAAP) using the Federal Energy Regulatory Commission (FERC) chart of accounts.

- Asset related transactions flowing through the Western Resources control area are recorded in accounts 447 (revenue), 555 (expense), and 565 (transmission expense) in the month settled.
- Asset Related transactions that do not flow through the Western Resources control area are recorded in accounts 451 (revenue) and 557 (expense) in the month settled.
- Non-asset related transactions are recorded in accounts 417 (revenue) and 417.1 (expense) in accordance with Financial Accounting Standards statement 133.

Legal Risk

The Legal Department (Legal) is responsible for establishing and maintaining agreements, standardized contracts, and trade documentation in order to mitigate the risk of non-performance by counterparties. Legal will fulfill these objectives by negotiating and executing master agreements (for both physical and financial products), tariffs (for transmission and transportation) with counterparties, and negotiating and reviewing third party or parental guarantees.

5. Key Definitions

Hedging

The practice of offsetting the price risk inherent in any cash market position by taking an equal but opposite position in the futures or forwards market. Hedgers use the futures and forwards markets to protect their business from adverse price changes.

Portfolio

All securities held by the Power Trading Organization including asset related and non-asset related transactions. This includes all contracts associated with the sale and purchase of power and energy (electricity, gas, oil, and coal), such as; physical deals, options, hub contracts, capacity deals and any other type of unique transaction.

Marking-to-Market

To debit or credit on a daily basis a portfolio's market value based on the close of that day's trading session. In this way, the portfolio's loss or gain can be monitored on a daily basis.

Notional Value

The total dollar amount of a contract (contract \$ X number of units).

Mark-to-Market Value

The liquidation value of a contract prior to delivery ((Market \$ - Contract \$) X (number of units)).

6. Power Trading Organization Member Accountability

The undersigned hereby certifies that he/she has read the *Risk Management Principles, Policies and Procedures* and will adhere to all provisions contained herein. The undersigned further acknowledges and understands that any violation of these policies and procedures shall be considered grounds for disciplinary action, which may include immediate termination of employment.

Signature

Date

Procedures

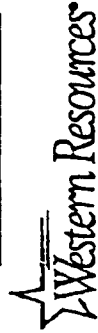
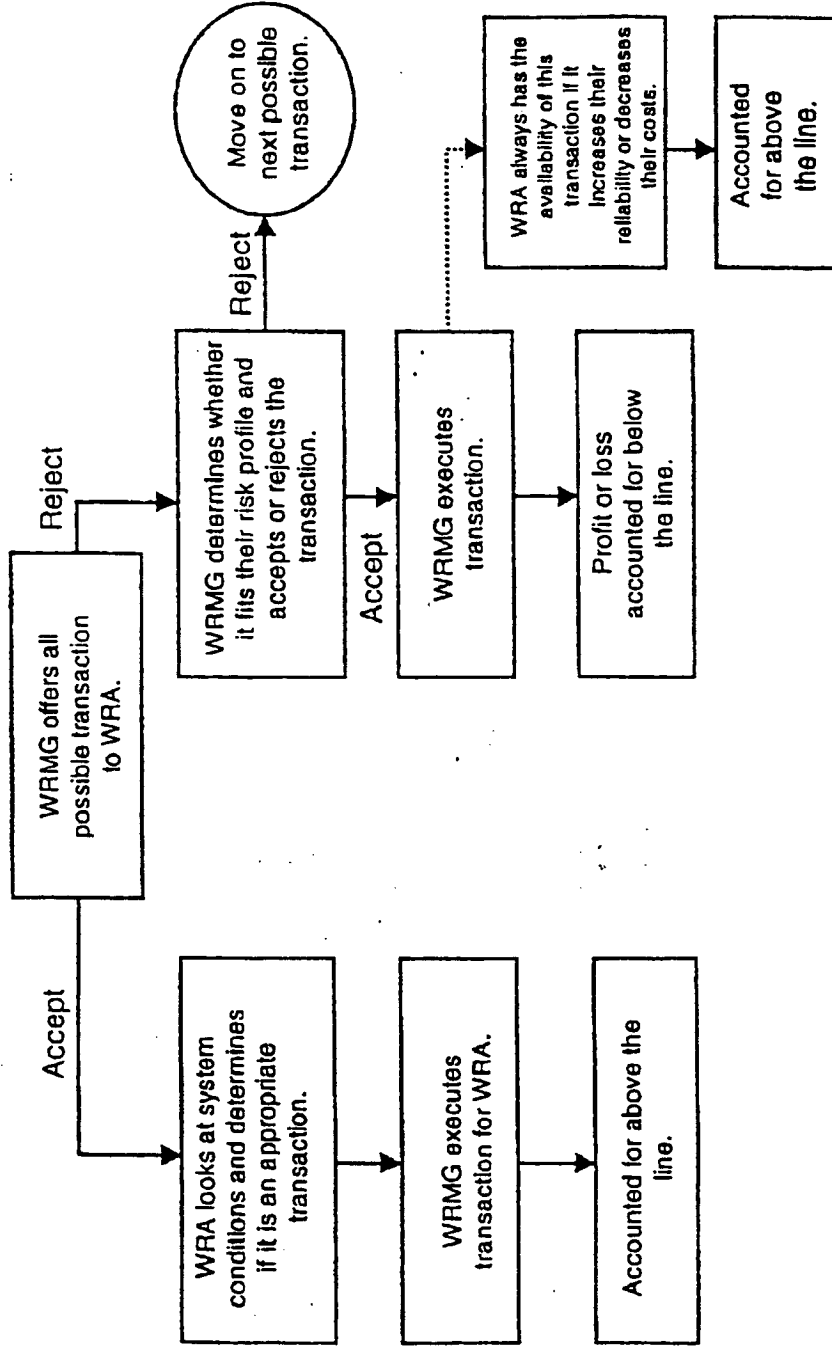


Exhibit 5 – Inter-company Transactions Analysis

Additional Review of Inter-Company Transfers

As noted within the attached report, Navigant Consulting has performed several analyses that compared the market prices paid by the System and Marketing groups. It is the position of Westar's management, that the benefits derived by the sale of this energy to the Marketing group would be equal to or greater than the benefits that would have been recorded if these sales had been conducted with an unrelated third party. These analyses, which are described below, provide analytical support for the Westar's position that all of these inter-company transactions were priced at market rates.

To test the reasonableness of the pricing for various inter-company transfers, Navigant performed a review of market prices for certain inter-company transactions that occurred during the January 2002 through March 2002 time period. As noted within our report, the transactions that occurred during this period, which accounted for approximately 75% of all inter-company transactions¹, were actually transactions that resulted from an agreement that entailed the generation of significant MWh's by the System's unit for the sole purpose of providing balancing generation to the Marketing unit. According to management, these transactions were priced at market prices and all profits were recorded on the System's books.

To test these transfers, we compared price for these inter-company transfers to the average price that was derived by the system for transactions involving third parties. Because we wished to determine the market price for each day (and not the average price paid), we only include those transactions with third parties that involved a single energy transaction. Transactions that were conducted as part of some type of extended futures or options transaction (and were, therefore, not representative of the current market price) were excluded from this analysis. The results of this comparison can be seen in the attached chart.

As shown within the attached chart, the market price for the inter-company transfers approximated the average sales price to third parties for most of the periods during the review. While various differences existed, the analysis shows that, for most periods, the market price approximated or exceeded the average sales price for transactions involving third parties. The differences that do exist can, in part, be attributed to the rough nature of the calculations performed².

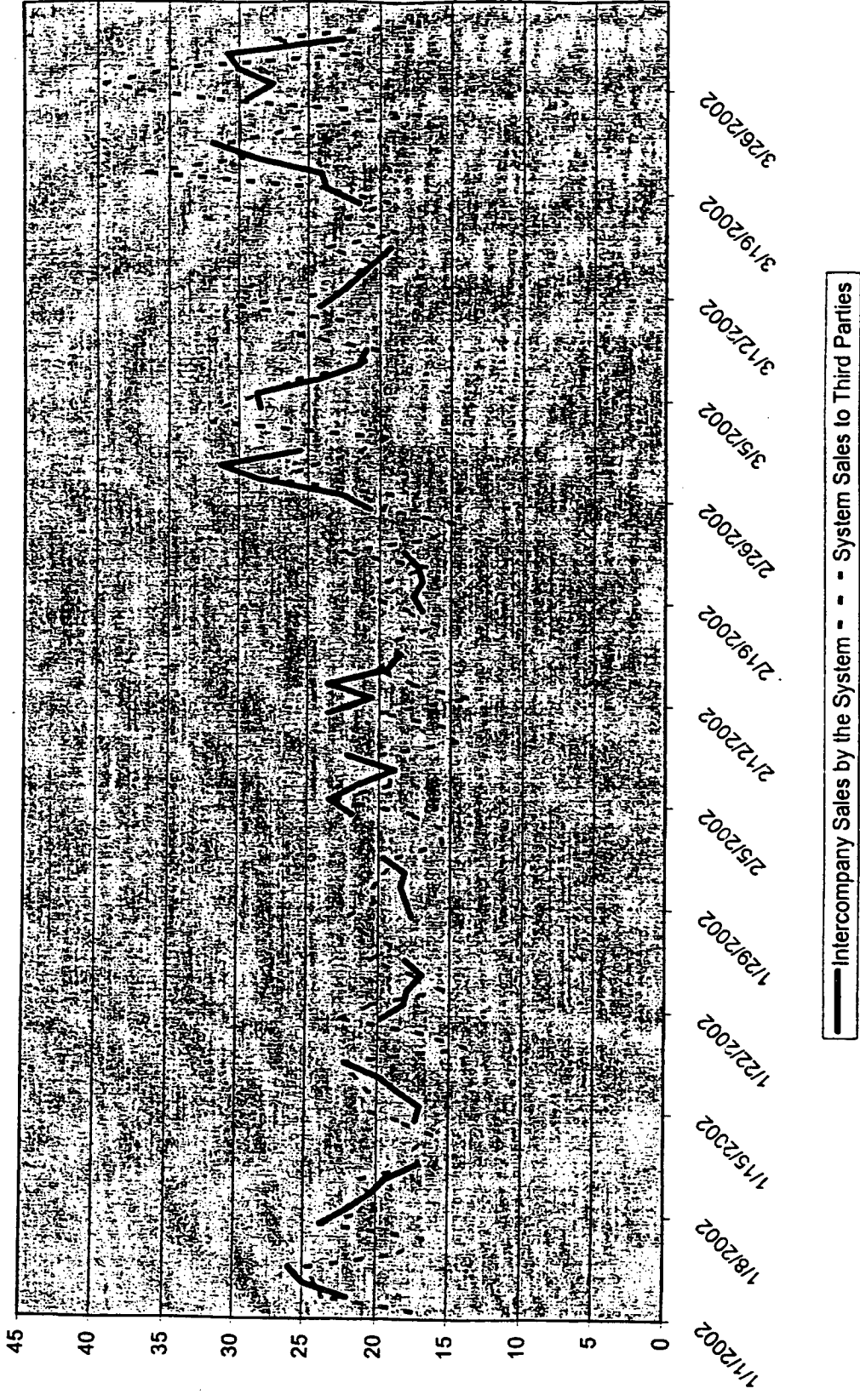
In addition, Navigant Consulting has performed analyses regarding the market prices that were obtained by both the System and Marketing groups. For example, we compared and reviewed the average purchase and sales prices for both groups on a daily basis during the period under review. In addition, we analyzed various transactions where both the System and Marketing groups obtained energy from the same third party on the same day. Our analyses suggest that there was no particular bias in pricing between these two groups.

While these relatively simple analyses provide indirect support for the Westar position that all of these inter-company transactions were priced at market rates, the volatility and nature of the markets makes it difficult to reconstruct the actual market price at the time that the transactions were conducted. Such an analysis would be technically difficult and would require the use of third party data. This type of analysis is beyond the scope of our current assignment and has not been performed.

¹ The remaining inter-company transactions are true "balancing" transactions and involve small amounts of energy that were transferred between the System and Marketing groups to facilitate daily balancing activities. The relatively small size and the timing of these transactions made them unique. As such, a comparison of these "balancing" transactions could not be readily performed with the data available and would be outside of the scope of our work.

² As noted above, our efforts to determine the average sales price to third parties was based upon our analysis of all "single trade" energy transactions (i.e. those trades that were not conducted as part of a future or option contract). However, the nature of the data used in our analysis prevented us from exclude certain types of "next-day" and "forward" type transactions that could have affected the overall average price. In addition, the average sales price calculation includes all transactions throughout the day, while the sales to the Marketing group were focused on certain hours within the day. As such, while our analysis provides a reasonable estimate of the average sales price, certain deviations would be expected between the two prices that are tracked within the attached charts.

Comparison of Average Market Price for Third Party Transactions to Market Pricing of Intercompany Transactions (January 2002 - March 2002)



CERTIFICATE OF SERVICE
(01-WSRE-436-RTS)

I hereby certify that on this 10th day of December, 2002, I caused a true and correct copy of the above and foregoing, *Staff's Final Report and Recommendation*, to be deposited in the United States Mail, postage prepaid, to the following persons:

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* Denotes those receiving the Confidential version.

