



EARTHJUSTICE

ALASKA CALIFORNIA FLORIDA MID-PACIFIC NORTHEAST NORTHERN ROCKIES
NORTHWEST ROCKY MOUNTAIN WASHINGTON, DC INTERNATIONAL

RECEIVED

July 19, 2013

JUL 19 2013

Mr. Jeff Derouen
Executive Director
Kentucky Public Service Commission
211 Sower Boulevard
Frankfort, Kentucky 40602

PUBLIC SERVICE
COMMISSION

Via Courier

**Re: CASE NO. 2013-00221, COMMENTS OF BEN TAYLOR AND
SIERRA CLUB**

Dear Mr. Derouen:

Enclosed are an original and ten copies of the Comments of Ben Taylor and Sierra Club and a certificate of service in docket 2013-00221 before the Kentucky Public Service Commission. This filing contains no confidential information.

Sincerely,

Grant Tolley
Earthjustice
1617 John F. Kennedy Boulevard
Suite 1675
Philadelphia, PA 19103
(215) 717-4523

**COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION**

In the Matter of:

**JOINT APPLICATION OF KENERGY)
CORP. AND BIG RIVERS ELECTRIC)
CORPORATION FOR APPROVAL OF)
CONTRACTS AND FOR A)
DECLARATORY ORDER)**

CASE NO. 2013-00221

COMMENTS OF BEN TAYLOR AND SIERRA CLUB

This proceeding is one of a trilogy of cases dealing with the precarious financial situation in which Big Rivers Electric Corporation (“BREC” or “Company”) finds itself. The fundamental problem facing BREC is that the departure of its two biggest customers – the Hawesville and Sebree smelters – has left the Company saddled with substantial amounts of excess capacity that is uneconomic in today’s energy markets and faces significant costs moving forward. Having announced its intent to leave the BREC system, the Century smelter has negotiated a series of nine agreements (referred to herein collectively as the “Century Agreements”) through which the Century smelter would receive market power through BREC and its member Kenergy. The Kentucky Public Service Commission (“Commission”) is now faced with the question of whether to approve these Century Agreements.¹

Under Kentucky law, the guiding principle for Commission decision making is ensuring that the electric rates that BREC’s remaining rural and industrial customers pay are just and reasonable. KRS 278.190. BREC and Kenergy assert that the Century Agreements would have no impact on BREC’s rates and, therefore, are irrelevant to the justness and reasonableness of

¹ While only the agreements related to the Hawesville smelter are directly at issue in this proceeding, the Commission’s ruling here will likely impact the agreements reached with the Sebree smelter as Kenergy has informed its management that “if/when the Hawesville contract is approved, a duplicate effort for Sebree is expected to occur.” BREC Resp. to AG 1-2, June Management Report.

those rates. But in reality the Century Agreements are relevant to BREC's rural and industrial ratepayers in at least two ways that the Commission should address in deciding whether to approve the Century Agreements. First, there are significant concerns that the Hawesville smelter may try to return to the BREC system in the future. BREC's ratepayers, however, will be protected only if the departure of the Hawesville smelter is permanent so that ratepayers are not subject in the future to the risks and rate impacts of the Hawesville smelter once again returning to the BREC system and then departing. Second, the Commission should make sure that ratepayers are made whole by both making sure that all costs of providing market power to the Hawesville smelter will be fully covered by Century, and by evaluating whether there are legacy costs relating to the significant excess capacity that the Company obtained to serve the Hawesville smelter toward which it may be reasonable to expect Century to contribute.

There is substantial uncertainty regarding many of the details of the Century Agreements, and the expedited schedule requested by BREC has prevented a complete evaluation of those details. As such, proposed intervenors Ben Taylor and Sierra Club (collectively "Sierra Club") do not take a firm position regarding whether each specific provision of the Century Agreements is reasonable and appropriate. As a general matter, however, the result of the Century Agreements – that Century would obtain market power through Kenergy and BREC – is unobjectionable so long as the permanence and make whole issues identified above are addressed by the Commission.

With such changes, the Century Agreements could be an important step towards the ultimate solution to BREC's financial troubles, which is the right-sizing of BREC through the retirement or sale of the Coleman and Wilson generating units. Such right-sizing would relieve BREC's remaining customers of having to pay to maintain and make capital investments in

nearly three times as much capacity as is needed to serve them. It would also help avoid a situation in which BREC's rural and industrial customers are again subject to significant costs and uncertainties were the Century smelter to return to the BREC system and then depart yet again. In order to achieve these results, however, the Commission must condition any approval of the Century Agreements to ensure that the Hawesville smelter's departure is permanent, and to ensure that BREC and its ratepayers are really being made whole through these Agreements.

I. Having the Smelters as Part of the BREC System Poses Significant Financial Risks to BREC and its Ratepayers.

The primary cause of BREC's current financial troubles is the departure of the Century and Alcan smelters, which has left the Company with far more capacity than it needs. BREC owns and operates 1444 MW of capacity and has contractual rights to another 375 MW, for a total of 1819 MW. With both smelters, the highest forecast monthly billing demand in 2013 is 1529 MW, so BREC has an ample 19% reserve margin. Without the Hawesville smelter, BREC's 2013 highest monthly demand drops to 1047 MW, implying a 74% reserve margin; after the departure the Sebree smelter a few months later, the corresponding peak demand will be 679 MW, and the reserve margin would be 168%. (Direct Testimony of Frank Ackerman, Case No. 2012-00535, at p. 3). As a result, BREC's ratepayers will be paying to maintain approximately three times as much generating capacity as needed, while facing a significant drop in revenue that is exacerbated by the fact that the Company's generating units are not competitive with today's low market prices.

The present situation grew out of the 2009 Unwind Transaction, in which BREC decided to end a 1998 reorganization plan that originally was to run through 2023. Under the reorganization plan, BREC had leased its generating assets to Western Kentucky Energy

Corporation (“WKEC”) and purchased power from WKEC’s parent company, E.ON. As part of the Unwind Transaction, BREC regained full control over its generating assets meaning that the Company was again responsible for operating and maintaining its generating units, and for being able to profitably sell the energy generated by those units. BREC also entered into long term contracts to sell power to the Hawesville and Sebree smelters, which at the time of the Unwind Transaction faced significant financial problems stemming from reliance on then higher priced market power.

At the time of proposing the Unwind Transaction, BREC acknowledged the significant risks involved, stemming primarily from the fact that two-thirds of the Company’s load would be two aluminum smelters. If either or both of those smelters were to go out of business, BREC would face a major loss of revenue and have a significant amount of excess capacity. As BREC’s then-CEO Michael Core testified,

Before entering into the negotiations, Big Rivers assessed the risks associated with taking back the operations of the plants. Included in its analysis, Big Rivers considered many risks - chief among them were generation, load concentration, fuel, and financial risks - associated with serving the energy needs of the two Smelter loads from Alcan’s Sebree plant and Century’s Hawesville plant.

....

Big Rivers felt that its Members needed to be compensated by the Smelters for taking back the risks of operating the power plants as well as the load concentration risk posed by the Smelters.

(Testimony of Michael H. Core, Case No. 2007-00455, at pp. 5, 7). In an effort to shield ratepayers from these risks, the Unwind Transaction included approximately \$750 million in asset transfers from E.ON to BREC, much of which went into economic reserve funds, along with an agreement that the Hawesville and Sebree smelters could leave the BREC system only if they intended to end operations. Despite these protections, the smelters are both leaving the BREC system, and BREC is proposing significant rate increases for its rural and industrial

ratepayers that would become even larger when the economic reserve funds created by the Unwind Transaction would be depleted in 2014 for industrial ratepayers and 2015 for rural ratepayers.

The Commission should reject any argument that a return of the Hawesville smelter to the BREC system would be beneficial to ratepayers or help restore BREC to a solid financial footing. Instead, as the Unwind Transaction has shown, having such a large portion of BREC's capacity concentrated in two smelters creates great financial uncertainty. Such impact is only heightened if the Company maintains significant excess capacity on the hope that the Hawesville smelter will return. A more secure approach for BREC and its ratepayers is to require that the Hawesville smelter's decision to leave the BREC system be permanent so that BREC can focus on right-sizing itself through the retirement or sale of the Wilson and Coleman generating units.

II. The Century Agreements Do Not Preclude the Century Smelter From Returning to the BREC System.

In light of the history between the Hawesville smelter and BREC, there has been considerable concern regarding whether, even if the Century Agreements are approved, the Hawesville smelter would try to return to the BREC system after a few years. The Attorney General sought clarification of this issue through the following data request to BREC:

If the Application and agreement(s) are approved and the agreements finalized, is there anything in the agreements to preclude Century from returning to Big Rivers system for the delivery of wholesale power supply?

(AG Data Request 1-26). Big Rivers responded "yes" and then identified "Section 14.4 of the Arrangement Agreement, Section 14.5 of the Electric Service Agreement and Section 3.7 of the Direct Agreement" as purportedly precluding Hawesville's return to the Big Rivers system. In reality, none of those provisions preclude such a return.

Instead, the cited language provides only that BREC does not have an “obligation” to serve the Hawesville smelter outside of the Century Agreements. For example, the Electric Service Agreement provides in relevant part as follows:

14.4 --Termination Obligation. Upon termination of this Agreement in the circumstances described in Section 7.3.1(b), and subject to Section 14.5, neither Kenergy nor Big Rivers will have any contractual obligation under this Agreement to supply any Electric Services to Century other than pursuant to a Post-Termination Service Agreement. In all other circumstances, (a) Century acknowledges and agrees that Kenergy will not have any contractual obligation to supply Electric Services to Century or any of its Affiliates with respect to the Hawesville Smelter or its portion thereof, and (b) Century would need to negotiate a new arrangement with Kenergy for the provision of Electric Services.

14.5 Right to Supply from Big Rivers. Century acknowledges and agrees that Big Rivers has no obligation to serve or supply any Electric Services from System Resources for the benefit of all or a portion of the Hawesville Smelter or any Affiliates, spin-offs or successors of Century during the Service Period or thereafter other than as provided in the Arrangement Agreement for the purchase of Electric Services in the Day Ahead Market or the Real Time Market or from a Bilateral Counterparty; *provided*, that Century Parent or an affiliate of Century may seek a contractual service arrangement, with Big Rivers and Kenergy with respect to the Sebree smelter.

Similar language providing that Big Rivers has no “obligation” to serve the Hawesville smelter is set forth in Section 3.7 of the Direct Agreement and Section 14.4 of the Arrangement Agreement. What such language does not do is prevent Century from seeking to return to the BREC system, or make clear that BREC has no intent to allow Century to do so. Without such provisions in the Century Agreements, there is no assurance that BREC and the Hawesville smelter will not be right back in this same situation in the near future.

The concern that the Hawesville smelter will return to the BREC system (and then likely leave again) is heightened by the lax termination provisions in the Century Agreements. In particular, Section 7.3.1 of the Electric Service Agreement provides Century the ability to terminate the Agreement “for Convenience” with 60 days’ notice. BREC and Kenergy do not

appear to have the same termination rights under the Agreement. But what this means is that Century can with almost total impunity decide to leave the arrangement with BREC and Kenergy proposed here and try to bargain for yet a different arrangement including, presumably, returning to being wholesale customers served by the BREC system. It is simply not in the best interest of BREC's ratepayers to allow the Hawesville smelter to join and then walk away from the BREC system at its own convenience. The Commission should make sure that the Century Agreement does not allow Century to do so.

III. The Commission Should Ensure That the Century Agreements Make BREC and its Ratepayers Whole.

In negotiating the Century Agreements, BREC and Kenergy took the position that any agreements should not impose additional costs on BREC or increase its rural and industrial customers' rates more than if the Hawesville smelter ceased operations. (Berry Testimony at p. 45; BREC Resp. to AG 1-2, Century Term Sheet Summary at p. 2). These are important goals, and the Commission should carefully evaluate the Century Agreements to ensure that those goals will actually be achieved.

In addition, it is likely that simply ensuring that no additional costs are imposed on BREC and its ratepayers as part of the Century Agreements is not enough. In particular, the Commission should carefully evaluate whether there are costs that BREC incurred as part of serving the Hawesville smelter but will be paying for after the smelters leave the system. If so, the Commission should assess whether Century should be required to reimburse BREC for some of those legacy costs, rather than leaving the full costs to BREC's remaining ratepayers. In addition, in the event that BREC's present financial troubles are addressed through any sort of negotiated reorganization, the Commission should leave open the possibility that Century could

reasonably be expected to contribute to putting BREC back on solid financial footing through such reorganization.

IV. Conclusion

For the foregoing reasons, Sierra Club urges the Commission to condition any approval of the Century Agreements on a requirement that the Hawesville smelter's departure from the BREC system is permanent, and that BREC's remaining ratepayers are made whole as part of the Agreements.

Respectfully submitted,



Joe Childers, Esq.
Joe F. Childers & Associates
300 Lexington Building
201 West Short Street
Lexington, Kentucky 40507
859-253-9824
859-258-9288 (facsimile)

Of counsel:

Shannon Fisk
Earthjustice
1617 John F. Kennedy Blvd., Suite 1675
Philadelphia, PA 19103
Phone: (215) 717-4522
sfisk@earthjustice.org

Dated: July 19, 2013

CERTIFICATE OF SERVICE

I certify that I had served a copy of the Comments of Ben Taylor and Sierra Club via electronic mail and U.S. Mail on July 19, 2013 to the following:

Mark A Bailey
President CEO
Big Rivers Electric Corporation
201 Third Street
Henderson, KY 42419-0024

Honorable Thomas C Brite
Attorney At Law
Brite & Hopkins, PLLC
83 Ballpark Road
P.O. Box 309
Hardinsburg, KENTUCKY 40143

David Brown
Stites & Harbison, PLLC
1800 Providian Center
400 West Market Street
Louisville, KENTUCKY 40202

Jennifer B Hans
Assistant Attorney General's Office
1024 Capital Center Drive, Ste 200
Frankfort, KENTUCKY 40601-8204

J. Christopher Hopgood
Dorsey, King, Gray, Norment & Hopgood
318 Second Street
Henderson, KENTUCKY 42420

Honorable Michael L Kurtz
Attorney at Law
Boehm, Kurtz & Lowry
36 East Seventh Street
Suite 1510
Cincinnati, OHIO 45202

Burns E Mercer
Manager
Meade County R.E.C.C.
P. O. Box 489
Brandenburg, KY 40108-0489

Honorable James M Miller
Attorney at Law
Sullivan, Mountjoy, Stainback & Miller,
PSC
100 St. Ann Street
P.O. Box 727
Owensboro, KENTUCKY 42302-0727

G. Kelly Nuckols
President & CEO
Jackson Purchase Energy Corporation
2900 Irvin Cobb Drive
P. O. Box 4030
Paducah, KY 42002-4030

Billie J Richert
Vice President Accounting, Rates & CFO
Big Rivers Electric Corporation
201 Third Street
Henderson, KY 42419-0024

Donald P Seberger
Rio Tinto Alcan
8770 West Bryn Mawr Avenue
Chicago, ILLINOIS 60631

Melissa D Yates
Attorney
Denton & Keuler, LLP
555 Jefferson Street
P. U. Box 929
Paducah, KENTUCKY 42002-0929

Grant Tolley