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January 27, 2012

Mark David Goss, Esquire  
Frost Brown Todd LLC  
250 West Main Street, Suite 2800  
Lexington, KY 40507-1749

**PSC STAFF OPINION 2012-005**

RE: Request for Staff Opinion Relating to 807 KAR 5:056

Dear Mr. Goss:

Commission Staff acknowledges receipt of your letter dated December 2, 2011, on behalf of East Kentucky Power Cooperative, Inc. ("EKPC"), in which you request an opinion confirming your position that the cost of alternative fuels are eligible for cost recovery through the fuel adjustment clause ("FAC") mechanism as governed by 807 KAR 5:056.

According to the letter, EKPC's Gilbert Unit and Spurlock Unit 4, both of which are circulating fluidized bed ("CFB") baseload coal-fired generating units, have the capability of burning a wide range of fuel blends with the coal they already use. The types of fuel blends include tire derived fuels ("TDF"), biomass, and switchgrass. The typical fuel blend consists of 97 percent coal and 3 percent alternative fuel. The CFB units are permitted to burn up to a 10 percent blend of TDF by weight.

Your letter points out the benefits of using alternative fuel sources to the environment, the coal industry, and to EKPC's members. Protecting the environment "through the use of economically viable renewable energy sources and pursuing prudent diversity in the fuel mix of the generation portfolio" is one method that EKPC endeavors to pursue in order to attain its strategic objective of delivering reliable and affordable energy. EKPC desires to utilize alternative fuels, particularly TDF, only when it is economic to do so, noting that the incentive to use such alternative fuels would decrease if it was unable to recover the cost of alternative fuels.

As also pointed out in your letter, the terms used in the preamble to the FAC regulation are broader and more encompassing than those used in the body of the regulation itself. While the preamble to the FAC regulation states that its purpose is to

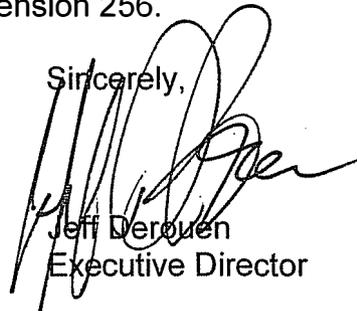
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allow for the recovery of increases in "fuel costs," Section 1(3)(a) of the regulation specifically references the recovery of costs for "fossil fuel" consumed in the utility's own plants, and there is no definition of "fossil fuel" in the governing regulation.

Whether the cost of alternative fuels can be recovered pursuant to the FAC mechanism is an issue of first impression for the Commission. In light of the fact that neither this particular issue, nor any similar issue relating to the types of fuels recoverable through the FAC has been previously addressed by the Commission, Commission Staff is unable to provide an advisory opinion. The best course of action is for EKPC to file an application for the issuance of a declaratory order by the Commission. Alternatively, EKPC could incur the cost of alternative fuel, include the cost in its FAC, and have the issue reviewed in the course of a periodic FAC review conducted pursuant to 807 KAR 5:056, Sections 1(11) and (12). Either of these alternatives would allow the issue to be fully vetted and explored by the Commission, EKPC and any and all potential stakeholders.

This letter represents Commission Staff's interpretation of the law as applied to the facts presented. This opinion is advisory in nature and not binding upon the Commission should the issues presented herein be formally presented for Commission resolution. Questions concerning this opinion should be directed to Quang D. Nguyen, Staff Attorney, at (502) 564-3940, extension 256.

Sincerely,



Jeff Derouen  
Executive Director

QDN/kar