COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

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PUBLIC SERVICE COMMISSION

In the Matter of:

APPLICATION OF KENTUCKY POWER COMPANY)
FOR A CPCN AUTHORIZING THE TRANSFER)
OF AN UNDIVIDED FIFTY PERCENT INTEREST IN) CASE NO. 2012-00578
THE MITCHELL GENERATING STATION AND)
ASSOCIATED ASSETS *ET AL*)

ATTORNEY GENERAL'S POST-HEARING BRIEF

Comes now the intervenor, the Attorney General of the Commonwealth of Kentucky, by and through his Office of Rate Intervention, and tenders his post-hearing brief in the above-styled matter. For the reasons set forth in this brief, the Attorney General states that the application does not meet the relevant standards required under KRS Chapter 278 and, therefore, should be denied.

STATEMENT OF THE CASE

On December 19, 2012, Kentucky Power Company ("KPCo" or "the Company"), a wholly-owned subsidiary of American Electric Power Company, Inc. ("AEP"), filed with the Public Service Commission ("the Commission") an application seeking approval to transfer an undivided fifty percent (50%) interest in the Mitchell generating station, a coal-fired electric plant located in Moundsville, West Virginia. As a result of deregulation in Ohio, AEP desires to transfer Mitchell from an unregulated entity to KPCo, a regulated subsidiary, at a projected cost of $536 million. [1]

[1] *See* Verified Application, Case No. 2012-00578 (December 19, 2012) at 2-7; *see also* Pauley Direct TE at. 5-6 (describing Ohio deregulation, Orders of the Ohio Public Utilities Commission and Ohio Power Company's ("OPCo") approved corporate separation from and creation of AEP Generation Resources, Inc. – the unregulated entity) and Pauley TE on Cross, July 10, 2013, Video Transcript of Evidence ("VTE") at 10:53:50-10:54:00 and 11:58:45-12:01:03 (discussing the Ohio deregulation).

KPCo seeks the Commission's approval for said purchase as well as other related relief. KPCo offers this plan as its alternative to retrofitting with federally-mandated environmental controls the Company's currently-owned and operational asset, the Big Sandy Unit 2 Generating Station, located in Louisa, Kentucky. According to KPCo, "the Company will be required to retire Big Sandy Unit 2 by June 2015."[2]

In addition to the Attorney General, the following parties were granted full intervention in these proceedings: (1) the Kentucky Industrial Utility Customers ("KIUC") representing Air Liquide Large Industries U.S. Limited Partnership, AK Steel Corporation, Air Product & Chemicals, Inc., EQT Corporation and Catlettsburg Refining Limited Liability Company, a subsidiary of Marathon Petroleum Limited Partnership, and (2) Ben Taylor and the Sierra Club ("Sierra Club"). All parties and the Commission staff convened for informal conferences for the purpose of discussing settlement on May 16, May 22 and May 24, 2013. Confidential settlement discussions between all parties and staff concluded without a unanimous settlement by the parties, and with the Attorney General exiting any further negotiations.

On May 28, 2013, one day prior to the scheduled hearing in this matter, KPCo advised the Commission that it had reached a tentative agreement to settle with two (2) intervening parties – KIUC and the Sierra Club. KPCo filed with the Commission a Memorandum of Understanding, to which the Attorney General was not a signatory. In response to informal communications among the parties, KPCo advised the Commission

[2] *Id.* at 9; *see also Third Joint Modification to Consent Decree* (February 22, 2013), AG Hearing Exh. 7 at 2, ¶1 (explaining that original Consent Decree was entered on December 10, 2007, ***five (5) years*** before KPCo presented its definitive plan regarding the impending impact to the Big Sandy Unit 2 facility).

that it was prepared to proceed with the hearing scheduled for May 29, 2013, on the application itself, but desired to have a bifurcated process whereby the parties would return to the Commission to present the final settlement for approval. In response to this proposal, the Attorney General vehemently opposed such bifurcation as unduly prejudicial and a violation of due process. By Order dated May 28, 2013, the Commission continued the full evidentiary hearing in this matter until July 10, 2013, but proceeded to hold a public hearing on May 28, 2013, solely for the purpose of taking public comments.[3]

On July 5, 2013, KPCo filed with the Commission a partial stipulation and settlement agreement, to which the Attorney General was not a party. A public and full evidentiary hearing on KPCo's application and the proposed, partial stipulation and settlement was held on July 10, 11 and 12, 2013.

In its Verified Application, in conjunction with discovery in this matter and during the hearing, KPCo advised that its plan to purchase a fifty percent interest in the Mitchell generating station was parallel to a plan to have AEP-subsidiary Appalachian Power Company ("APCo") purchase the other fifty percent interest in Mitchell and, via an operating agreement between the affiliated companies, have APCo operate the plant.[4] Further, KPCo advised that APCo required the approval of both the West Virginia Public

[3] In addition to the public hearings on May 28, 2013, and July 10-13, 2013, respectively, the Commission held a public meeting on May 14, 2013, in Louisa, Kentucky, and a public meeting with video conference on May 15, 2013, for Hazard and Whitesburg, Kentucky. The impassioned comments presented by state and local government officials, representatives of social service agencies and businesses and residential ratepayers as to the economic impact of retiring the Big Sandy Unit 2, including the loss of tax revenue and jobs, and the impact of rate increases may stand alone on their merits. The Attorney General advocates that the Commission take these public comments into consideration in making its final determination.

[4] *See* Verified Application at 11-12 and Pauley Direct at 14.

Service Commission and the Virginia State Corporation Commission.[5] After the hearing, KPCo advised the Kentucky Commission that the Virginia State Corporation Commission entered its order on July 31, 2013, "denying the transfer of a fifty percent undivided interest in the Mitchell generation station to Appalachian Power Company."[6]

ARGUMENT

A. Introduction

Kentucky Power Company asserts that its "plan for the transfer of an undivided fifty percent interest in the Mitchell generating station ... is the least cost and best alternative."[7] Further, despite the Virginia Corporation Commission's express denial of the plan and rejection of the valuation of a 50% interest at the price of $536 million,[8] which involves multiple affiliated companies all wholly-owned and operated by AEP, KPCo continues to assert that the Mitchell transfer plan should proceed and is best for KPCo's ratepayers.[9] Yet, only six (6) months prior to the filing of KPCo's Mitchell transfer application, KPCo advised the Commission that retrofitting the Big Sandy Unit 2 at a cost in excess of $1 billion represented "the least-cost, least-risk real world alternative available to the Company and its customers."[10] ***So, what changed?***

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[5] Wohnhas TE in response to questions from Commissioner Breathitt, July 11, 2013, VTE at approx. 12:16:50-12:17:00.

[6] *See* KPCo Supplemental Response to PSC Post-Hearing Data Requests, Item 1 (August 5, 2013); *see also Application of APCo for approval of transactions to acquire interests in the Amos and Mitchell generating plants and to merge with Wheeling Power*, Virginia State Corporation Commission ("VSCC" or "Virginia Commission"), Case No. PUE 2012-00141, Order (July 31, 2013), attached and submitted herewith.

[7] *See* Verified Application at 2.

[8] *Id.* at 6 ("The net book value of the fifty percent interest as of December 31, 2011, was $519 milliion and presently is forecasted to be approximately $536 million at time of closing.") The proposed affiliate agreements place no cap on the net book value of an undivided 50% interest in the Mitchell generating station, and KPCo's President and COO testified that the price was only estimated and could still increase. *See* Pauley TE in response to Vice-Chair Gardner, July 10, 2013, VTE at 12:45:44-12:46:50.

[9] *See supra*, n. 6, KPCo Supp. Data Response.

[10] *In the Matter of Application of KPCo for Approval of its 2011 Environmental Compliance Plan, for Approval of its Amended Environmental Cost Recovery Surcharge Tariff, and for the Grant of a CPCN for the Construction and Acquisition of Related*

Between May 2012, when KPCo advised that retrofitting the Big Sandy Unit 2 was the least-cost option and failed to consider even a twenty percent use of the Mitchell facility, and December 2012, when KPCo filed to transfer a fifty percent interest in the Mitchell plant, the Company's parent, AEP, awoke to the "real world" result of partial deregulation of the electric industry in Ohio.[11] Confronting the financial risk of having a coal-fired generating station available in a competitive, deregulated market (Ohio), ***AEP decided*** that transferring the asset to the regulated markets of Kentucky, West Virginia and Virginia, through transactions between it and among its affiliated subsidiaries, would be the economic solution that was the least-cost and least-risk to its shareholders' bottom-line.[12]

However, the rate impacts did not change for Kentucky's ratepayers. In proposing to retrofit the Big Sandy Unit 2 with $1 billion in environmental equipment, KPCo sought a 31% rate increase from its customers.[13] Now, even before approval of its plan to purchase a fifty percent interest in the Mitchell facility for one-half the sum, KPCo has filed a rate case

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Facilities, Case No. 2011-00401, ("2011-2012 ECR Case") KPCo's Post-Hearing Brief (May 11, 2012) at 1. KPCo withdrew its application only days before a final decision from the Commission was anticipated. Pauley TE, July 10, 2013, VTE at 10:57:31. Note that the Attorney General opposed KPCo's plan as filed by the company as ***not economically feasible*** due in part to the following: (1) the company's presumption that the installation of a high-tech dry flue-gas desulphurization ("DFGD") system would not extend the life of the Big Sandy Unit 2 beyond 2040, (2) the company's admissions at hearing that flowing the $1 billion cost through the environmental surcharge mechanism would result in a 31% increase on the average residential customer's bill, and (3) the company's failure to explore all options and alternatives for replacement generation through a request for proposal ("RFP") process. *Id.*, Attorney General's Post-Hearing Brief (May 11, 2012). The Attorney General criticized KPCo for failing to give adequate consideration to ***all*** alternatives that a transparent, arms-length RFP process could reveal, including but not limited to purchasing power representing 20% of the total average annual capacity of the Mitchell generating station.

[11] *See* Verified Application at 8, n. 7 referencing www.aep.com/investors/currentRegulatoryactivity/regulatory/ferc.aspx; *see Application for Authorization to Transfer Jurisdictional Assets Under Section 203 of the Federal Power Act* (OPCo/AEP Gen Oct. 31, 2012).

[12] In considering all the facts presented, this is the only reasonable conclusion. To conclude that the decision to transfer Mitchell was envisioned prior to KPCo's 2011-2012 ECR case would mean that the retrofit application was nothing short of a sham proceeding. To conclude that the decision to transfer Mitchell was made based on the arguments proposed by the intervenors and/or the Kentucky Commissioners during the 2011-2012 ECR case is (a) unreasonable (at best), since the Company did not follow the recommendation to pursue a 20% interest in Mitchell or (b) offensive (at worst), since the Company expressly **rejected** the Commissioners' clear recommendation to conduct an RFP process.

[13] *See* Case No. 2012-00578, Hearing, Pauley TE on Cross, July 10, 2012, VTE at 10:54:35-10:54:50 advising a 31% actual impact on customers.

seeking a 31% rate increase from its customers.[14] At least one Commission has already disagreed with this plan. For the reasons set forth in this brief, the Attorney General advocates that the Commission follow Virginia's lead and reject this self-serving plan.

B. The Commission's Legal Standards for Approval

1. Need for the Proposed Facility

Before a utility may secure or construct a new facility in the Commonwealth of Kentucky, KRS 278.020(1) requires the utility to first prove[15] that the requested facility is required for public convenience and necessity, and "the utility must demonstrate a need for such facilities and an absence of wasteful duplication."[16] The Kentucky Supreme Court has held and the Commission has enforced that ***"Need"*** requires:

> a showing of a substantial inadequacy of existing service, involving a consumer market sufficiently large to make it economically feasible for the new system or facility to be constructed and operated.
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> . . . [T]he inadequacy must be due either to a substantial deficiency of service facilities, ***beyond what could be supplied by normal improvements in the ordinary course of business; or to indifference, poor management or disregard of the rights of consumers, persisting over such a period of time as to establish an inability or unwillingness to render adequate service.***[17]

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[14] *See In the Matter of: Application of KPCo for a General Adjustment of Electric Rates,* Case No. 2013-00197, Application (July 1, 2013) at 7.

[15] "The burden of demonstrating the reasonableness of a proposed rule or condition of service is upon the utility." *In the Matter of Hardin County Water District No. 1,* Case No. 2009-00113, 2010 WL 4250014 (Ky.P.S.C.), citing *Energy Regulatory Commission v. Kentucky Power Company,* 605 S.W.2d 46,50 (Ky. App. 1980)(applicants before an administrative agency have the burden of proof). Further, administrative findings must be based on substantial evidence. *Kentucky Board of Nursing v. Ward,* 890 S.W.2d 641, 642 (Ky. App. 1994).

[16] *See In Re: The Application of Kentucky-American Water Company for a Certificate of Public Convenience and Necessity Authorizing the Construction of Kentucky River Station II, Associated Facilities and Transmission Main,* Case No. 2007-00134, (Ky. PSC Apr. 25, 2008) at 29 (citing *Kentucky Utilities Co. v. Public Serv. Comm'n,* 252 S.W.2d 885 (Ky. 1952)).

[17] *Id.* at 29 (citing *Kentucky Utilities,* 252 S.W.2d at 890). (Emphasis supplied.)

Moreover, the Court defined "wasteful duplication" as "an excess of capacity over need" and "an excessive investment in relation to productivity or efficiency and an unnecessary multiplicity of physical properties."[18] For a utility to comply with its burden of proof in this regard, the Commission has held "that ***the applicant must demonstrate that a thorough review of all alternatives has been performed***."[19]

Pursuant to KRS 278.020(1), the Commission has the exclusive jurisdiction to issue or refuse to issue a Certificate of Public Convenience and Necessity ("CPCN") for the securing or construction of such a facility.[20] Within this statutory jurisdiction, the Commission has broad authority to approve, modify or disapprove an application; and the statute gives the Commission discretion to conduct a hearing or decide the case as filed. In pertinent part, KRS 278.020(1) provides:

> Upon the filing of an application for a certificate, and after any public hearing which the commission may in its discretion conduct for all interested parties, the commission may issue or refuse to issue the certificate, or issue it in part and refuse it in part...

If the Commission determines that the evidence presented in KPCo's application and testimony is insufficient to determine the reasonableness and cost-effectiveness of its proposed CPCN and ECR plan, the Commission has authority to either disapprove of the petition, or to dismiss it without prejudice, pursuant to KRS 278.020.

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[18] *Id.*

[19] *Id.* at 30 (citing *In Re: The Joint Application of LG&E and KU for the Construction of Transmission Facilities*, Case No. 2005-00142 (Ky. PSC Sept. 8, 2005). (Emphasis supplied.)

[20] *Id.* at 29.

2. Economic Feasibility

In *Kentucky Utilities Co. v. Pub. Serv. Comm'n*, 252 S.W.2d 885 (Ky. 1952), Kentucky's then-highest Court noted that a utility must be able to prove the need for facilities that are the subject of the proposed CPCN, which requires:

> " . . . a showing of a substantial inadequacy of existing service, involving a consumer market sufficiently large to make it ***economically feasible*** for the new system or facility to be constructed and operated."[21]

The Commission has adopted and applied this standard in prior CPCN cases. Specifically, regarding *The Application of Kentucky-American Water Company for a Certificate of Public Convenience and Necessity Authorizing the Construction of Kentucky River Station II, Associated Facilities and Transmission Main*,[22] the Commission discussed the application of *Kentucky Utilities*, holding that:

> To demonstrate that a proposed facility does not result in wasteful duplication, we have held that the applicant must demonstrate that ***a thorough review of all alternatives*** has been performed. . . .
>
> With regard to the issue of economic feasibility, we are of the opinion that the record ***must contain evidence supporting the economic feasibility of the proposed facilities.*** The evidence must address the effect on the demand for utility service from the rates necessary to recover the cost of the proposed facilities and provide a reasonable rate of return on them. If the resulting rates would significantly reduce demand for utility services so as to negate or significantly reduce the need for the proposed facilities, then the facilities are not economically feasible and a Certificate should not be granted.[23]

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[21] *Id.* at 890. (Emphasis supplied.)
[22] *See* Case No. 2007-00134, Final Order (Apr. 25, 2008).
[23] *Id.* at 30 (*citing Case No. 2005-00142, The Joint Application of Louisville Gas & Electric Co. and Kentucky Utilities Co. for the Construction of Transmission Facilities In Jefferson, Bullitt, Meade, and Hardin Counties, Kentucky*, Final Order (Sep. 8, 2005). (Emphasis supplied.)

It is beyond dispute that the solutions proposed by KPCo to address the Big Sandy Unit 2, if approved as submitted, has the potential to lead to one of the most major rate increases ever faced by ratepayers in Eastern Kentucky in the past several decades. The ramifications are so great, in fact, that they would likely carry a significant impact on the viability of the economy of the counties comprising KPCo's dedicated service territory. It is likewise beyond dispute that the counties comprising KPCo's certified service territory are among the most economically deprived regions of the Commonwealth, and are on average 28% below the federal poverty line.[24]

3. Affiliate Transactions

KRS 278.2207(1)(b) governing "the terms for transactions between a utility and its affiliates" provides in relevant part:

> Services and products provided to the utility by an affiliate shall be priced at the affiliate's fully distributed cost ***but in no event greater than market*** or in compliance with the utility's existing USDA, SEC, or FERC approved cost allocation methodology.

Further, if a utility seeks a deviation from the below-market price required under KRS 278.2207(1)(b), it carries "the burden of demonstrating that the requested pricing is reasonable" and must demonstrate that "the deviation is in the public interest."[25]

In summary, in order to approve the transaction as proposed by KPCo for the affiliate transfer of an undivided fifty percent interest in the Mitchell facility, KPCo carries the burden of proving: (1) that the facility is needed and will not result in wasteful duplication that could have otherwise been avoided by prudent management; (2) that the company has

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[24] *See* KPCo ECR Case, Attorney General Hearing Exhibit 3, map of counties depicting poverty level in KPCo's service territory; data source: Kentucky Data Center.
[25] *See* KRS 278.2207(2).

conducted a thorough analysis of all alternatives; (3) that the facility is economically feasible; and (4) that the proposed transfer price is either less than market or reasonable and in the public interest.

C. Kentucky Power Company Has Failed to Carry its Burden of Proof for Approval to Transfer a 50% Interest in the Mitchell Facility

Pursuant to KRS 278.020 and the Commission's regulations thereunder, 807 KAR 5:001 Section 15, and KRS 278.2207(1)(b), KPCo carries the burden of proof to demonstrate that its proposal meets the statutory standard for a CPCN to transfer the Mitchell generating station. For the reasons outlined below, KPCo has failed to carry its burden of proof.

1. KPCo fails to demonstrate prudent and independent decision-making regarding its plan to transfer the Mitchell facility to replace the Big Sandy Unit 2.

Confronting the decision to "retrofit, refuel, repower or retire the Big Sandy Unit 2"[26] in 2007 – a decision of inordinate importance to the welfare of Eastern Kentucky's residents – KPCo as well as its parent company, AEP, adopted nothing short of a 'wait-and-see' philosophy.[27] In the meantime, AEP chose to retrofit the Mitchell units[28] in West Virginia and installed less expensive environmental controls at its Rockport facilities, while simultaneously negotiating with the EPA and environmental interests to extend final plans for the Rockport units by nearly a decade.[29]

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[26] Third Amended Consent Decree, AG Hearing Exh. 7 *supra* at 6.
[27] KPCo ECR Case, Case No. 2011-00401, McManus TE in response to Chairman Armstrong, May 1, 2012, VTE at 12:09-12:12
[28] Several witnesses described the Mitchell plant as basically the same unit as the Big Sandy plant, including e.g. Pauley TE, July 10, 2013, VTE at 2:34:00-2:34:50.
[29] Third Amended Consent Decree, AG Hearing Exh. 7 *supra* at 6.

After waiting for direction from AEP and the assistance of AEP Service Corporation ("AEPSCO"),[30] what "rigorous analysis"[31] did KPCo conduct to make the "once-in-a-lifetime" (*supra*) decision, which may only be equated with building a new generation utility? According to President and Chief Operating Officer, Gregory G. Pauley, in making his final decision, he relied upon a single email from AEP and a summary "Re-analysis" of his company's options, comprised of four (4) pages.[32] Further, he confirmed that the "rigorous analysis" performed by his parent company involved the modeling of capacity scenarios or options, using proprietary software for which KPCo did not possess the trained employees or licensing to conduct on its own.[33]

Moreover, the modeling conducted by AEPSCO using Strategist™ and Aurora™ software provides the only basis for KPCo's decision to transfer into its rate base a one-half billion dollar investment in a plant that it has not built and which it will not operate.[34] Neither KPCo, the other intervenor experts, nor the third-party expert KPCo hired to review the modeling could ***independently*** reproduce the results arrived at by AEPSCO's staff.[35] In fact, KPCo's expert did not question or otherwise audit any of the assumptions used by AEPSC nor did he even meet with the staffer responsible for the modeling.[36]

It is readily apparent from the record that the modeling conducted to support the application is completely self-serving if not also questionable as to the credibility of the data

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[30] See Pauley TE on Cross, July 10, 2013, VTE at 10:59:30-11:01:00, describing the "collaborative" team making the decision, including not fewer than five (5) senior officials with AEP.
[31] Pauley Rebuttal TE at 5:20-21.
[32] *See* Pauley TE on Cross, July 10, 2013, VTE at 11:02 to 11:10 and AG Hearing Exh. 1 and 2.
[33] *Id.* at 11:11:45 – 11:14:00.
[34] *Id.* at 11:14:00 – 11:14:10.
[35] *Id.* at 11:15:30 – 11:16:15 and AG Hearing Exh. 3.
[36] *See* McDermott TE in response to Vice-Chair Gardner, July 11, 2013, VTE at 19:04-19:05 (advising that he never met with Scott C. Weaver, the AEPSCO modeling staff member, and that consultation telephone calls with the staff totaled less than half a day).

inputs. The assumptions built into the modeling are exclusively those of AEPSCO, which come at the direction of AEP.[37] Also, note that in modeling a retrofit to the Big Sandy Unit 2, KPCo used a useful life that would continue until 2040, but conceded that the likely life would only be to 2030. For example, from the Attorney General's post-hearing brief in Case No. 2011-00402 at page 11, the following observation was made:

> Although KPCo's own model indicates option 1 is the least cost option, the company did not model what option would be the least cost if Big Sandy 2 retired in 2030, which company witness Wohnhas acknowledged was **likely to occur.**"[38] The company defended the failure to take this probable, crucial fact into consideration only by saying that it's "not reasonable that a retrofitted Big Sandy Unit 2 would retire in 2030."[39] Company witness Becker further conceded that the Strategist model itself retired Big Sandy Unit Two by 2030,[40] yet the company has offered no data to support this supposition and conjecture. Also, capital costs were not modeled using Strategist or any modeling software.

In this matter, KPCo made a similar concession, when President and COO, Greg Pauley, advised Commission staff that any ***stranded costs*** that may result from a retirement of the Mitchell plant before 2040 – which by all accounts is very likely, since the plant would be 70 years old by said date – would be borne by KPCo's ratepayers.[41]

Accordingly, the Commission would be remiss to rely exclusively on the proprietary, licensed modeling and questionable data used by AEPSCO, or AEP, that is not independently replicable by another entity – a fact which AEPSCO acknowledged.[42] This ***'Just-Trust-Us'*** approach, which KPCo and AEP have adopted by relying only upon internal

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[37] *Id.; see also supra* n. 27; *see also* Wohnhas TE on Re-Direct beg. at 12:42, referencing Woolf's testimony but advising that AEP sets targets and earnings.
[38] Referencing KPCo ECR Case, Hearing, April 30, 2012 VTE beginning at approximately 15:34:30.
[39] *Id.*, Weaver TE on Cross, May 1, 2012 VTE, beginning at approximately 19:18:30 and 19:28:20.
[40] *Id.*, May 2, 2012 VTE at approximately 10:01:00.
[41] See Pauley TE on Cross, July 10, 2013, VTE at 12:28:30-12:30:12.
[42] *See supra* at n. 32.

modeling with questionable data inputs and no independent evaluation, in lieu of a RFP-process (discussed *infra*), is utterly deficient on its face. If the PSC accepts this method for approving CPCNs, future decisions would almost certainly be dictated *de facto* by utility applicants without independent evaluation and support.

2. KPCo failed to issue an RFP for the Big Sandy Unit 2, thereby ignoring clear direction and precedent of the Commission.

In its most recent CPCN cases, the Commission has clearly indicated that a Request for Proposals ("RFP")-process is the preferred benchmarking tool for the analysis of least cost generation and integrated resource planning decisions.[43] However, despite this clear direction, and with six months between its withdrawal of a retrofit plan and its Application in this matter, KPCo failed to conduct an RFP. In his testimony, President & COO Pauley advised Commission staff that the fair market value of the Mitchell asset was "greater than" the $536 million asking price proposed by his corporate parent, AEP, but could point to nothing in the record, other than AEP's self-serving model, to support such an assertion.[44] Not only did it fail to conduct an RFP, the preferred benchmarking tool for making such a decision, it failed to adopt any independent method of appraising or otherwise valuating the result its modeling produced. Despite arguing against the need for an independent valuation, KPCo's witnesses supporting AEPSCO's modeling conceded that an independent valuation would indeed have lent credence to KPCo's application.[45]

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[43] *See In the Matter of Joint Application of LG&E/KU for CPCN*, Case No. 2011-00375, Final Order (May 3, 2012) at 18-19; *see also* McDermott TE on Cross, July 11, 2013, VTE at 18:54:00-18:58:10.
[44] See Pauley TE on Cross, July 10, 2013, VTE at 12:17-12:18.
[45] *See* Fransen TE on Cross, July 11, 2013, VTE at approx. 16:38:45-16:39:40; *see also* McDermott TE on Cross, July 11, 2013, VTE at 18:59:00-19:02:10 (who did **not** provide an independent appraisal or in-depth review of AEPSCO's modeling assumptions).

In fact, this same expert advised on questioning by Vice-Chairman Gardner that all a utility should have to do is "identify" the least-cost option, then leave the actual analysis and decision up to the Commission.[46] KPCo's adamant refusal to conduct a RFP results in not only lack of credible evidence, but also taints the analysis the Company presented to the Commission. Because the Company bears the burden of proof and refused to adhere to the guidance if not demands of the Commission in Case No. 2011-00401 by avoiding a RFP in the instant case, the use of a model and data not independently verifiable by any other entity other than the company should be soundly rejected.

In addition to its own precedent, the Commission may also reasonably rely on the recent opinion of the Virginia State Corporation Commission, which denied APCo's request to acquire the other fifty percent interest in the Mitchell generating station.[47] The Virginia Commission opined: "we find that the Company did not provide compelling evidence regarding market alternatives."[48] The Virginia Commission was willing to consider other relevant evidence, including APCo's institutional and operational knowledge, as to the Amos facility, which "is unlike the typical affiliate arrangement to which the Commission's lower of cost or market analysis is traditionally applied."[49] However, as to the Mitchell facility, the Virginia Commission held that APCo had not satisfied Virginia's least cost test and had not satisfied the Commission that the transfer would be in the public interest and would not impair or jeopardize adequate service to ratepayers at just and reasonable rates.[50]

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[46] McDermott TE on Cross *supra.*
[47] *See supra* APCo/Virginia Order at n. 6 and attached.
[48] *Id.* at 9.
[49] *Id.* at 9-10.
[50] *Id.* at 6.

Therefore, the Virginia Commission rejected the transfer proposed when presented with insufficient evidence, which failed to demonstrate the proper use of either a RFP process or, at the very least, an independent, third-party analysis of market alternatives and valuation of the asset. KPCo has failed to present credible, **independently** verifiable evidence in this proceeding that (1) definitely proves that the proprietary, modeling analysis offered is reliable; (2) would lend credence to or offer an independent valuation of the $536 million price-tag that AEP has assigned to the acquisition of Mitchell; or (3) the Mitchell acquisition would otherwise be "in the public interest",[51] be economically feasible and result in fair, just and reasonable rates.

3. <u>KPCo should not be permitted to bootstrap the Big Sandy Unit 1 RFP responses to support AEPSCO's self-serving modeling regarding the Big Sandy Unit 2.</u>

An important supplement to the Verified Application presented by Kentucky Power, which lacks independent verification and support, is the strategy by which the Company has avoided filing its mandatory Integrated Resource Plan ("IRP") for as long as possible and until after a determination on the Mitchell transfer. Based on KPCo's own motion, the Company's current deadline for its IRP is December 31, 2013.[52]

Kentucky's IRP process serves as the definitive long-term planning process for a utility's generation and transmission. A company's IRP sets forth in a transparent and independently verifiable fashion the utility's long-term needs and plans for its statutory

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[51] KRS 278.2207(2).

[52] *In the Matter of: Kentucky Power Company's Motion for Extension of Time to File Its Integrated Resource Plan*, Case No. 2012-00344, Order (July 30, 2012).

duty to provide safe, adequate and reliable service to its customers at fair, just and reasonable rates.

In lieu of filing an IRP, KPCo has chosen to file a piecemeal series of cases to address its long term needs. One of those planned filings, was a RFP for Big Sandy 1.[53] However, KPCo did not time the RFP for the Big Sandy Unit 1 to coincide with this filing – which relates exclusively to transferring Mitchell to replace the Big Sandy Unit 2. Ultimately, the full Big Sandy Unit 1 RFP process was completed and the confidential resulting proposals filed ***only upon the demand*** of the Commission.[54] Given the Company's historical approach to its generation planning through filings before the Commission to meet same, it is not surprising that the RFP results generated conclusions in support of the modeling used in the current case. In spite of the self-serving results communicated by KPCo at the hearing, the Company's lack of prudent statutory planning for generation and transmission planning via the IRP process, the piecemeal generation approach employed by the Company in its filings, and the dubious results from the Company's RFP donot meet the Company's burden of proof in a request to transfer 50% interest of the Mitchell Facility.

D. The Commission and Ratepayers should not be tricked or bullied into accepting the Mitchell transaction as a *fait accompli.*

Confronting overwhelming opposition from Kentucky ratepayers and local representatives advocating on their behalf, KPCo and its parent company have adopted

[53] *See* Verified Application at 6, n. 3.

[54] The Company had originally planned on doing a RFP for Big Sandy 1, but included in the partial settlement is a predetermined approach to the Unit without the results of the RFP. *See* Stipulation and Settlement Agreement (Partial) (July 2, 2013) at 9, ¶13. During the course of the proceeding in the instant matter, the Commission demanded the Company continue with the RFP and produce the results to the Commission. *See* Order (May 28, 2013).

trench warfare tactics and a *fait accompli* approach to ratemaking. When confronting a negative regulatory decision in its 2011-2012 ECR case, and after proceeding with a million dollar rate case, the company withdrew its application. In subsequent months, which included tough negotiations with several state consumer advocates and regulators -- including Kentucky's Attorney General and Commission staff -- AEP, KPCo and its affiliates filed a series of complicated, transmission agreements for approval by the Federal Energy Regulatory Commission ("FERC") The FERC filing expressly contemplated the transfer of the Mitchell plant from a deregulated market to regulated markets – subject to state commission approval.[55] Nearly simultaneously, AEP and its affiliates next filed a series of transactional approval filings, including this case, seeking rubber-stamp approval from the states.

While negotiations were conducted with the parties in all three (3) states in which regulatory approval was pending, no consumer advocate settled with AEP. In fact, after the first day of negotiations with intervenors, KPCo filed its notice of intent to file a rate increase.[56] When the Attorney General exited negotiations, KPCo filed its rate application seeking a 31% rate increase and *presuming* that the Commission would approve the acquisition of a fifty percent interest in Mitchell[57]. Now, KPCo seeks to present the partial Stipulation and Settlement Agreement as the definitive solution for ratepayers and disguising it as a substitute to the 31% rate increase, rather than a mere delay to the all but

[55] *See supra* at n. 10.

[56] *See* Notice by Kentucky Power Company Pursuant to 807 KAR 5:001, Section 16(2) of Its Intent to File an Application Seeking a General Adjustment of Its Existing Rates, Case No. 2013-00197 (May 17, 2013).

[57] Not only does KPCo's pending rate application presume approval, but AEP/KPCo issued a press release advising that the proposed rate increase "is necessary to begin recovery of costs associated with transferring the Mitchell Plant Assets to Kentucky Power and it is being filed in anticipation that the Public Service Commission will approve the asset transfer." *See* "Kentucky Power Files Rate Case to Recover Costs of Mitchell Plant Asset Transfer" (AEP/KPCo Jun. 27, 2013).

inevitable rate increase that customers will face if $536 million is transferred into KPCo's rate base. As the Chairman pointedly asked the most senior AEP official testifying before the Commission in this matter: What are he and his Company willing to do for Kentucky?[58] In response, the official stated that AEP "want[s] to be committed to Kentucky", but advised that only a favorable regulatory environment could guarantee such a commitment.[59]

Neither the Commission nor the public should accept such bullying. Rather, ratepayers are entitled to an independent, thorough and fair analysis of utility generation planning resulting in rates that are fair, just and reasonable.

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[58] *See* TE Richard Munczinski, Senior Vice-President, Regulatory Services, AEPSCO, July 12, 2013, 17:12:30-17:13:30; but see preceding TE, VTE at 17:12:01-17:12:25 (Note that in discussing the Stipulation & Settlement Agreement at 9 ¶11, Mr. Munczinski failed to advise the Commission that the $0.12 per residential bill (totaling approximately $250,000 per year) currently going to Home Energy Assistance comes exclusively ***from KPCo's residential ratepayers and not the shareholders.*** Rather, the actual sum offered by AEP to HEA funding in Eastern Kentucky is the additional sum $0.03 per monthly bill for an estimated total of $62,000 a year.

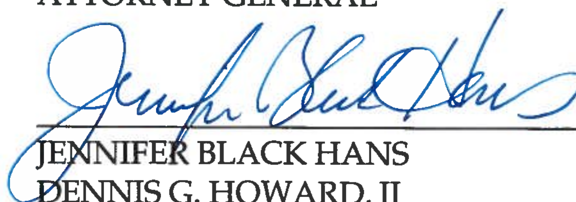
[59] *Id.* at 17:13:30-17:13:45.

CONCLUSION

WHEREFORE, based on the factual record, legal analysis and the reasons set forth in this brief, the Attorney General recommends that the application as filed does not meet the relevant standards required under KRS Chapter 278 and, therefore, should be denied. Further, as expressed herein, the Attorney General opposes the partial Stipulation and Settlement Agreement proposed by the other parties to this matter.

Respectfully submitted,

JACK CONWAY
ATTORNEY GENERAL



JENNIFER BLACK HANS
DENNIS G. HOWARD, II
LAWRENCE W. COOK
ASSISTANT ATTORNEYS GENERAL
1024 CAPITAL CENTER DRIVE,
SUITE 200
FRANKFORT KY 40601-8204
(502) 696-5453
FAX: (502) 573-1009

Certificate of Service and Filing

Counsel certifies that an original and ten photocopies of the foregoing were served and filed by hand delivery to Jeff Derouen, Executive Director, Public Service Commission, 211 Sower Boulevard, Frankfort, Kentucky 40601; counsel further states that true and accurate copies of the foregoing were mailed via First Class U.S. Mail, postage pre-paid, to:

Joe Childers
Joe F. Childers & Associates
300 Lexington Building
201 West Short Street
Lexington, KY 40507

Shannon Fisk
Earthjustice
1617 JFK Boulevard, Suite 1675
Philadelphia, PA 19103

Robb W Kapla
85 Second Street
San Francisco, CA 94105

Kristin Henry
Staff Attorney
Sierra Club
85 Second Street
San Francisco, CA 94105

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

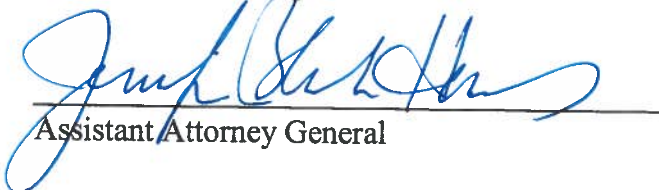
Honorable Mark R Overstreet
Stites & Harbison
421 West Main Street
P. O. Box 634
Frankfort, KY 40602-0634

Hector Garcia
American Electric Power Service Corp.
1 Riverside Plaza, 29th Floor
Columbus, OH 43215-2373

Kenneth J Gish, Jr.
Stites & Harbison
250 West Main Street, Suite 2300
Lexington, KY 40507

Ranie Wohnhas
Managing Director
Kentucky Power Company
101 A Enterprise Drive
P. O. Box 5190
Frankfort, KY 40602

This 12th day of August, 2013.



Assistant Attorney General

COMMONWEALTH OF VIRGINIA

STATE CORPORATION COMMISSION

AT RICHMOND, JULY 31, 2013

SCC-CLERK'S OFFICE
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2013 JUL 31 P 2: 46

APPLICATION OF

APPALACHIAN POWER COMPANY

CASE NO. PUE-2012-00141

For approval of transactions to acquire interests in the Amos and Mitchell generation plants and to merge with Wheeling Power Company

ORDER

On December 18, 2012, Appalachian Power Company ("APCo" or "Company") filed with the State Corporation Commission ("Commission") an Application requesting approval to enter into transactions through which APCo would: (1) acquire a two-thirds ownership interest in unit number 3 of the Amos generating plant; (2) acquire an undivided fifty percent interest in the Mitchell generating plant; (3) operate the entire Mitchell plant pursuant to a proposed operating agreement ("Mitchell Operating Agreement"); and (4) merge with affiliate Wheeling Power Company ("Wheeling"). The Application, as completed on May 2, 2013, seeks Commission approval pursuant to both the Utility Transfers Act, Chapter 5 of Title 56 of the Code of Virginia ("Code"), Code § 56-88 *et seq.* ("Transfers Act"), and the Affiliates Act, Chapter 4 of Title 56 of the Code, Code § 56-76 *et seq.* ("Affiliates Act").

The Amos generating plant, located in Winfield, West Virginia, is a three-unit, coal-fired power plant with an average annual capacity rating of 2,900 megawatts ("MW"). APCo currently owns unit numbers 1 and 2 at the facility in addition to an undivided one-third interest in unit 3.[1] APCo seeks Commission approval to acquire the remaining two-thirds interest in Amos unit 3 ("Amos 3"), or approximately 867 MW. APCo's affiliate Ohio Power Company

[1] Ex. 2 (Application) at 9.

("Ohio Power") currently owns this two-thirds interest in Amos unit 3 that APCo seeks to acquire.[2]

The Mitchell generating plant, located near Moundsville, West Virginia, is a two-unit, coal-fired facility with an average annual capacity rating of 1,560 MW.[3] APCo seeks Commission approval to acquire an undivided fifty percent interest in the Mitchell plant ("Mitchell"), or approximately 780 MW. Mitchell is also currently owned by Ohio Power.[4]

APCo proposes to acquire Amos 3 and Mitchell at their net book values when the facilities are acquired, which the Company estimates would occur on or about December 31, 2013.[5] APCo projects that the net book values for Amos 3 and Mitchell as of December 31, 2013, will be approximately $618 million and $536 million, respectively, or approximately $1.15 billion in total.[6] As proposed, APCo would also assume debts and liabilities associated with Amos 3 and Mitchell.[7]

The parties to the proposed Mitchell Operating Agreement are APCo and its affiliate Kentucky Power Company ("Kentucky Power"). Kentucky Power is currently seeking regulatory approvals necessary to acquire the undivided fifty percent interest in the Mitchell plant that APCo does not propose to acquire.[8] APCo specifically "requests that the Commission

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[2] Ex. 36 (Knight) at 3, Exhibit I; Tr. 174 (Patton).

[3] Ex. 2 (Application) at 10.

[4] Ex. 36 (Knight) at 3, Exhibit I; Tr. 174 (Patton).

[5] Ex. 2 (Application) at 2, 10. The proposed transaction includes appurtenant interconnection facilities and other assets associated with Amos 3 and Mitchell. *Id.* at 9-10.

[6] Ex. 19 (Norwood) at SN-2.

[7] Ex. 2 (Application) at 2, 10-12.

[8] *Id.* at 1, 15-17; Staff's July 2, 2013 Post-Hearing Brief at Appendix B.

approve or determine that it is not necessary for it to approve" the Mitchell Operating Agreement.[9]

In the proposed merger with Wheeling, APCo would acquire Wheeling's assets and assume its debt and liabilities.[10] Wheeling is a public service corporation organized and doing business under the laws of West Virginia, where it serves approximately 41,000 retail customers. Wheeling owns about 300 circuit miles of transmission lines, approximately 1,500 miles of distribution lines, and no generation facilities. APCo would acquire Wheeling's assets at their net book value, which the Company estimates will be approximately $195 million as of December 31, 2013.[11]

On January 10, 2013, the Commission issued an Order for Notice and Hearing that, among other things, established a procedural schedule for this case and directed APCo to provide public notice of this matter. On March 14, 2013, the Commission issued an Order amending the procedural schedule.

The following parties filed notices of participation: the Office of the Attorney General's Division of Consumer Counsel ("Consumer Counsel"); Old Dominion Committee for Fair Utility Rates and East Tennessee Energy Consumers (collectively, the "Committee"); CPV Smyth Generation Company, LLC ("CPV Smyth"); and Steel Dynamics, Inc.

The Commission held a public hearing on the Application on the following days: April 30 and June 4, 5, 10 and 11, 2013. At these hearings, the Commission received testimony from

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[9] Ex. 2 (Application) at 18-19.

[10] *Id.* at 14. Wheeling would merge with and into APCo so that APCo would be the surviving entity. *Id.* at 13.

[11] *Id.* at 5; Ex. 51 (Carr) at 13.

public witnesses and from witnesses on behalf of various participants. The Commission also received written and electronic comments from the public in this case.

On July 2, 2013, the following participants filed post-hearing briefs: APCo; Consumer Counsel; Committee; CPV Smyth; and the Commission Staff ("Staff").

NOW THE COMMISSION, upon consideration of this matter, is of the opinion and finds as follows.

<u>Code of Virginia</u>

Affiliates Act

The Affiliates Act generally applies to contracts or arrangements between a "public service company" that provides regulated public utility service in the Commonwealth and any "affiliated interest" of such company.[12] APCo is such a "public service company" and Kentucky Power, Ohio Power, and Wheeling – all of which are, like APCo, direct wholly-owned subsidiaries of American Electric Power Company ("AEP")[13] – are "affiliated interest[s]" of APCo.[14] NEWCO Appalachian, an entity that AEP will form to facilitate the transfer of Amos 3 and Mitchell from Ohio Power to APCo, is also an "affiliated interest" of APCo under the Affiliates Act.[15]

Section 56-77 of the Code states in part:

> A. No contract or arrangement providing for the furnishing of management, supervisory, construction, engineering, accounting, legal, financial, or similar services, and no contract or arrangement for the purchase, sale, lease or exchange of any property, right or thing, other than those above enumerated, or for the purchase or

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[12] *See* Va. Code § 56-76 (defining, among other terms, "public service company" and "affiliated interest").

[13] Ex. 2 (Application) at Exhibit 11, Attachment D.

[14] *Id.* at 6.

[15] *Id.*

> sale of treasury bonds or treasury capital stock made or entered into between a public service company and any affiliated interest shall be valid or effective unless and until it shall have been filed with and approved by the Commission....
>
> B. The Commission may, in its discretion and upon petition of the public service company or upon the Commission's own action, choose to exempt a public service company from all or any part of the requirements imposed by subsection A if the Commission determines that such an exemption is in the public interest....

Section 56-82 of the Code states in part:

> No public service company shall ... assume, extend or renew any obligation or liability whatsoever of any affiliated interest, whether as guarantor, endorser, surety, or otherwise, unless the Commission shall first have approved such loan or assumption, or the extension or renewal of such loan, obligation or liability, as being not inconsistent with the public interest, and then only upon such terms and conditions as may be set forth in the order of the Commission approving such transaction....

Section 56-80 of the Code addresses the Commission's continuing control over affiliate contracts and arrangements as necessary to protect and promote the public interest:

> The Commission shall have continuing supervisory control over the terms and conditions of such contracts and arrangements as are herein described so far as necessary to protect and promote the public interest. The Commission shall have the same jurisdiction over the modification or amendment of contracts or arrangements herein described as it has over such original contracts or arrangements. The fact that the Commission shall have approved entry into any such contract or arrangement shall not preclude disallowance or disapproval of payments made pursuant thereto in the future, if upon actual experience under such contract or arrangement, it appears that the payments provided for, or made, were, or are, unreasonable. Every order of the Commission approving any such contract or arrangement shall be expressly conditioned upon the reserved power of the Commission to revise and amend the terms and conditions thereof, if, when and as necessary to protect and promote the public interest.

Transfers Act

The Transfers Act provides in part as follows:

> It shall be unlawful for any public utility, directly or indirectly, to acquire or dispose of any utility assets situated within the Commonwealth or any utility securities of any other company unless such acquisition or disposition shall have been authorized by the Commission....[16]
>
> If and when the Commission, with or without hearing, shall be satisfied that adequate service to the public at just and reasonable rates will not be impaired or jeopardized by granting the prayer of the petition, the Commission shall make such order in the premises as it may deem proper and the circumstances require, and thereupon it shall be lawful to do the things provided for in such order....[17]

Amos 3 and Mitchell

The Company has established that it has a need for additional generation capacity; no participant effectively challenged this conclusion.[18] We find that the Company has not, however, shown that such need should be fulfilled under the statute by acquiring *both* Amos 3 and Mitchell. Specifically, based on the evidence in this case, the Commission is only "satisfied that adequate service to the public at just and reasonable rates will not be impaired or jeopardized,"[19] and that the public interest will be served,[20] if APCo acquires Amos 3 and not Mitchell.

We consider it relevant and important that APCo already owns Amos units 1 and 2, and one-third of Amos unit 3. APCo has operated and maintained all three Amos units since they were constructed and placed in service in the early 1970s.[21] APCo has performed maintenance

[16] Va. Code § 56-89.

[17] Va. Code § 56-90.

[18] *See, e.g.,* Staff's July 2, 2013 Post-Hearing Brief at 5-6.

[19] Va. Code § 56-90.

[20] *See, e.g., Roanoke Gas Co. v. State Corp. Comm'n,* 217 Va. 850, 853, 234 S.E.2d 302, 304 (1977) ("[T]he Affiliates Act imposes upon a public service company a burden ... to demonstrate that the proposed transactions with affiliated companies will serve the public interest.").

[21] *See, e.g.,* Ex. 61 (LaFleur rebuttal) at 11.

and implemented environmental retrofits for these units.[22] APCo's past ownership and operation of Amos units 1, 2, and 3 should also inform its understanding of the potential future risks associated with these units.[23] APCo, along with Virginia ratepayers, already has a connection to the Amos units that does not exist with Mitchell. Virginia ratepayers already have made substantial investments in the Amos units.

In addition, APCo proposes to assume both known and unknown pre-purchase liabilities of the transferred units.[24] We find that the risks associated therewith are greater for Mitchell than for Amos 3. As explained by Staff, "[s]ince APCo already owns most of the Amos generating plant, including an interest in Amos [unit] 3, the assumption of [unknown pre-purchase] liabilities is likely not as significant as it is for Mitchell, which the Company has not owned or operated."[25] For example, APCo would have to assume new potential unknown future liabilities associated with Mitchell's Fly Ash Impoundment Agreement that we find are not justified under the Affiliates Act and the Transfers Act.[26]

Mitchell also comes with other contractual risks not shared by Amos 3. APCo would have to assume from Ohio Power the obligations and risks related to hundreds of contracts associated with the operation of Mitchell.[27] Indeed, the Company did not expect to identify all

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[22] *See, e.g.*, Ex. 28 (LaFleur direct) at 8.

[23] *See, e.g.*, Ex. 78 (Patton rebuttal) at 8.

[24] *See, e.g.*, Ex. 37 (Ellis) at 13-14.

[25] Staff's July 2, 2013 Post-Hearing Brief at 23.

[26] *Id.* at 23-27. The Impoundment Agreement involves, among other things, impoundments that hold wet-handled coal combustion residuals, and the United States Environmental Protection Agency ("EPA") has assigned a high hazard potential rating to the fly ash impoundment area at Mitchell. *Id.* at 23-24. Contrary to Mitchell, as the operator and majority owner of Amos, APCo is already involved in potential impoundment issues associated therewith.

[27] *See, e.g.*, Ex. 2 (Application) at 10-11; Staff's July 2, 2013 Post-Hearing Brief at 18-19.

such contracts until the actual transfer of assets at the end of 2013.[28] Conversely, since APCo already operates (and owns most of) Amos, the assumption of such new obligations and risks does not come with the transfer of Amos 3.

Next, the transfer of *both* Amos 3 and Mitchell would preclude the Company from further diversifying its generation portfolio. The transfer of both facilities would fill APCo's current capacity need and would continue to fill such need through 2024.[29] If both facilities are transferred, the Company estimates that by 2015 coal would represent 68% of its capacity and 73% of its energy, with the energy percentage increasing to 87% by 2017.[30] We are not satisfied that filling the entire need herein with both of these coal plants (i) will serve the public interest, and (ii) will not impair or jeopardize adequate service to the public at just and reasonable rates.[31] Eliminating the possibility for additional fuel diversity at this time unreasonably increases customers' risks related to coal. Those risks include, for example, the price impacts on customers, decreases in the supply of coal, and – as discussed below – the likelihood of increased federal regulation of carbon dioxide emissions from existing coal plants.[32]

In addition to the fuel price and supply risks that may be caused by eliminating the potential for further fuel diversity, we find that the risks attendant to acquiring both facilities are too great given the uncertainty regarding future regulation of carbon dioxide emissions at the federal level. Indeed, a recent Presidential Memorandum directed the EPA to "issue proposed

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[28] *See, e.g.*, Ex. 61 (LaFleur rebuttal) at 9.

[29] Ex. 52 (Stevens) at 8-9.

[30] *See, e.g.*, Ex. 28 (LaFleur direct) at 5; Ex. 30.

[31] Va. Code § 56-90; *Roanoke Gas Co.*, 217 Va. at 853, 234 S.E.2d at 304.

[32] Moreover, we find that the results of APCo's modeling efforts, which include assumptions that respondents have effectively questioned, also do not require approval for the transfer of both coal facilities.

carbon pollution standards, regulations, or guidelines, as appropriate, for modified, reconstructed, and *existing* power plants by no later than June 1, 2014."[33] As discussed above, however, APCo and Virginia ratepayers have an historical and long-standing stake in the Amos units, which currently represent a reasonably priced source of capacity.[34] Capital investment in all three Amos units has been a significant component of APCo's rates, including the recovery of environmental compliance costs pursuant to Virginia statutes.[35] The carbon risks already apply to the Amos units, and Virginia ratepayers already have an interest in preserving the benefits afforded by those units.

Next, while we find that the Company did not provide compelling evidence regarding market alternatives, APCo has met its statutory burden with respect to Amos 3 for the reasons set

[33] *Presidential Memorandum of June 25, 2013, Power Sector Carbon Pollution Standards*, 78 Fed. Reg. 39535 (2013) (emphasis added). *See also* July 2, 2013 post-hearing briefs of APCo (23-25), Staff (Appendix A at 6-7), Consumer Counsel (19-21), and CPV Smyth (36-37). The Commission takes judicial notice of this Federal Register publication to the extent necessary.

[34] For example, at the approved purchase price below of $565 million for 867 MW, the capacity cost for the remaining two-thirds of Amos unit 3 is approximately $652/kW. *See, e.g.*, Ex. 19 (Norwood) at SN-2; Ex. 51 (Carr) at 14.

[35] *See, e.g., Application of Appalachian Power Company, For a 2011 biennial review of the rates, terms and conditions for the provision of generation, distribution and transmission services pursuant to §56-585.1 A of the Code of Virginia*, Case No. PUE-2011-00037, 2011 S.C.C. Ann. Rept. 477, Final Order (Nov. 30, 2011); *Application of Appalachian Power Company, For a statutory review of the rates, terms and conditions for the provision of generation, distribution and transmission services pursuant to § 56-585.1 A of the Code of Virginia*, Case No. PUE-2009-00030, 2010 S.C.C. Ann. Rep. 308, Final Order (July 15, 2010); *Application of Appalachian Power Company, For an increase in electric rates,* Case No. PUE-2008-00046, 2008 S.C.C. Ann. Rep. 547, Final Order (Nov. 17, 2008); *Application of Appalachian Power Company, For an increase in electric rates,* Case No. PUE-2006-00065, 2007 S.C.C. Ann. Rep. 321, Final Order at 5 (May 15, 2007). *Petition of Appalachian Power Company, For approval of a rate adjustment clause, E-RAC, to recover costs incurred in complying with state and federal environmental laws and regulations, pursuant to Va. Code § 56-585.1 A 5 e*, Case No. PUE-2011-00035, 2011 S.C .C. Ann. Rept. 474, Order Approving Rate Adjustment Clause (Nov. 30, 2011), *aff'd in part, rev'd in part sub nom. Appalachian Power Co. v. State Corp. Comm'n*, 284 Va. 695 (2012); *Application of Appalachian Power Company for adjustment to capped electric rates pursuant to § 56-582 B (vi),* Case No. PUE-2005-00056, 2006 S.C.C. Ann. Rept. 333, Final Order (Nov. 20, 2006); *Application of Appalachian Power Company, For adjustment to capped electric rates pursuant to § 56-582 B (vi) of the Code of Virginia*, Case No. PUE-2007-00069, 2007 S.C.C. Ann. Rept. 474, Final Order (Dec. 13, 2007); *Application of Appalachian Power Company, For adjustment to capped electric rates pursuant to § 56-582 B (vi) of the Code of Virginia*, Case No. PUE-2008-00045, 2008 S.C.C. Ann. Rept. 543, Final Order (Oct. 15, 2008); *Application of Appalachian Power Company, For recovery of environmental and reliability costs*, Case No. PUE-2009-00039, 2010 S.C.C. Ann. Rept. 324, Order Approving Surcharge (Jan. 14, 2010).

forth herein.[36] In addition, the transfer of Amos 3, given APCo's past ownership and operation of the Amos units, is unlike the typical affiliate arrangement to which the Commission's lower of cost or market analysis is traditionally applied. Moreover, the Commission has previously provided Affiliates Act approval to APCo for a generating facility without the typical application of such analysis.[37] We find that the Company has met its burden – with respect to Amos 3 – under the Transfers Act and Affiliates Act based on the record developed in this proceeding.

Finally, we find that the "price at which APCo proposes to acquire the units is overstated by approximately … $53,421,290 for Amos 3."[38] We conclude that the per book balance of accumulated depreciation for Amos 3, which has not been maintained by Ohio Power on a traditional regulatory basis, has resulted in an under-accrual of depreciation (*i.e.*, a reserve deficiency).[39] This reserve deficiency shall be removed from the proposed purchase price for Amos 3.[40] Accordingly, we herein approve the transfer of Amos 3 at $565 million and deny the requested approval at $618 million.

We have considered the entire record in this case, including need, costs, reliability, fuel diversity, carbon and fuel risks, the history of both facilities, and market and other risks

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[36] The Commission has also explained, albeit in a different context, as follows: "[T]he applicant must decide whether it will attempt to prove its case and obtain Commission approval of a proposed generating facility with – or without – evidence resulting from a competitive bid process." *Application of Virginia Electric and Power Company, Notification to the Commission of election to abandon the Company's bidding program and application to revise its cogeneration tariff pursuant to PURPA Section 210*, Case No. PUE-2008-00078, 2010 S.C.C. Ann. Rept. 297, 299, Final Order (May 18, 2010).

[37] *See Application of Appalachian Power Company, AEP Generating Company, and American Electric Power Company, Inc., For authority to enter into affiliate transactions under Title 56, Chapter 4 of the Code of Virginia*, Case No. PUE-2011-00023, 2011 S.C.C. Ann. Rept. 452, Order Granting Authority (July 20, 2011) (acquisition of the Dresden Generating Station).

[38] Staff's July 2, 2013 Post-Hearing Brief at 28 (citation omitted).

[39] *See, e.g.*, Staff's July 2, 2013 Post-Hearing Brief at 27-29; Ex. 42 (Armstrong); Tr. 574-81 (Armstrong); Ex. 51 (Carr) at 13-14.

[40] This reduces the purchase price from approximately $618 million to $565 million.

discussed by the participants, and conclude that the evidence supporting the transfer of Amos 3 satisfies the Transfers Act and the Affiliates Act subject to the requirements set forth herein.[41]

Wheeling Merger

Subject to the requirements below, the Commission finds that the Wheeling merger is in the public interest and will not jeopardize or impair adequate service at just and reasonable rates.[42] APCo's proposal to implement several significant supply changes at the same time as the Wheeling merger complicates efforts to isolate the rate impact expected from the merger.[43] The record, however, identifies potential impacts of the merger, including a reduction in Virginia jurisdictional allocation factors, which the Company expects to benefit Virginia ratepayers.[44] For example, the Company states that the merger should lower the amount of APCo's base rate costs – including such costs associated with Amos 3 – that are allocated to the Company's Virginia jurisdiction.[45]

The Company acknowledges, however, that the merger's base rate benefits for Virginia customers, including those identified above, will be delayed until the completion of APCo's "next biennial review case in early 2015, at which point the Virginia allocation factors would be reduced, reflecting the positive impact of the Wheeling merger."[46] We find that the $3.3 million

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[41] Because the transfer of Mitchell does not satisfy the requirements of the Affiliates Act and the Transfers Act, the Mitchell Operating Agreement is similarly denied.

[42] No case participant has suggested that the Wheeling merger would affect, in any way, the adequacy of APCo's service.

[43] *See, e.g.*, Staff's July 2, 2013 Post-Hearing Brief at 35-36; APCo's July 2, 2013 Post-Hearing Brief at 55-56, 61.

[44] *See, e.g.*, Ex. 51 (Carr) at 11; Ex. 19 (Norwood) at 6; Ex. 34 (Bosta) at 3.

[45] *Id.*; Tr. 1169-70 (Bosta).

[46] APCo's July 2, 2013 Post-Hearing Brief at 61.

surcredit proposed by the Company is necessary to address this timing concern.[47] In addition, APCo emphasized that the "Wheeling load should have a favorable impact on Virginia customers both over the short and long terms...."[48] Thus, as a requirement of our approval of the Wheeling merger, the Company shall implement the $3.3 million surcredit. In addition, we direct the Company, in its next biennial review and fuel factor proceedings, to provide evidence of the total rate impacts of the merger.

Accordingly, IT IS HEREBY ORDERED THAT:

(1) Subject to the findings and requirements set forth in this Order, the Application is granted in part and denied in part as set forth herein.

(2) This case is dismissed.

AN ATTESTED COPY hereof shall be sent by the Clerk of the Commission to all persons on the official Service List in this matter. The Service List is available from the Clerk of the Commission, c/o Document Control Center, 1300 East Main Street, First Floor, Tyler Building, Richmond, Virginia 23219.

A True Copy
Teste:

Clerk of the
State Corporation Commission

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[47] *See Id.*

[48] Ex. 75 (Martin rebuttal) at 4.