COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

AN INVESTIGATION INTO THE IMPLEMENTATION OF ECONOMIC DEVELOPMENT RATES BY ELECTRIC AND GAS UTILITIES	)))	ADMINISTRATIVE CASE NO. 327

O R D E R

On February 10, 1989, the Commission initiated this proceeding to examine its guidelines regarding economic development rates and to seek comments and recommendations from the major gas and electric utilities in the state on the use of these special rates. For the purposes of this investigation, an economic development rate ("EDR") is considered to be a gas or electric rate discount, offered to large commercial and industrial customers, which is intended to stimulate the creation of new jobs and capital investment both by encouraging existing customers to expand their operations and by improving the likelihood that new large commercial and industrial customers will locate in Kentucky.

The Commission's EDR guidelines were outlined in its July 1, 1988 Order in Case No. 10064[1]. As stated in that Order, any utility wishing to offer economic development rates to specific customers should satisfy the following six guidelines:[2]

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1 Case No. 10064, Adjustment of Gas and Electric Rates of Louisville Gas and Electric Company.

2 Case No. 10064, Order dated July 1, 1988, pages 93-94.

1. Each utility should be required to provide an affirmative declaration and evidence to demonstrate that it has adequate capacity to meet anticipated load growth each year in which an incentive tariff is in effect.

2. Each utility should be required to demonstrate that all variable costs associated with the transaction during each year that the contract is in effect will be recovered and that the transaction makes some contribution to fixed costs. Furthermore, the customer-specific fixed costs associated with adding an economic development/incentive customer should be recovered either up front or as a part of the minimum bill over the life of the contract.

3. Each utility that offers an economic development rate should be required to document and report any increase in employment and capital investment resulting from the tariff and contract. These reports should be filed on an annual basis with the Commission.

4. Each utility that intends to offer economic incentive rates should be required to file a tariff stating the terms and conditions of its offering. Furthermore, each utility should be required to enter into a contract with each customer which specifies the minimum bill, estimated annual load, and length of contracting period. No contract should exceed 5 years. All contracts shall be subject to the review and approval of the Commission.

5. Each utility should be required to include a clause in its contract that states that the tariff will be withdrawn when the utility no longer has adequate reserve to meet anticipated load growth.

6. Each utility should be required to demonstrate that rate classes that are not party to the transaction should be no worse off than if the transaction had not occurred. Under special circumstances, the Commission will consider utility proposals for contracts that share risk between utility shareholders and other ratepayers. However, if a utility proposes to charge the general body of ratepayers for the revenue deficiency resulting from the EDR through a risk-sharing mechanism then the utility will be required to demonstrate that these ratepayers should benefit in both the short- and long-run. In addition, at least one-half of the deficiency will be absorbed by the stockholders of the utility and will not be passed on to the

general body of ratepayers. The amount of the deficiency will be determined in future rate cases by multiplying at least one-half of the billing units of the EDR contract(s) by the tariffed rate that would have been applied to customer(s) if the EDR contract(s) had not been in effect.

The following gas and electric utilities were made parties to this proceeding: Louisville Gas and Electric Company ("LG&E"); Kentucky Power Company ("KPC"); Kentucky Utilities Company ("KU"); The Union Light, Heat and Power Company ("ULH&P"); Big Rivers Electric Corporation ("Big Rivers"); East Kentucky Power Cooperative, Inc. ("EKPC"); Columbia Gas of Kentucky, Inc. ("Columbia"); Delta Natural Gas Company, Inc. ("Delta"); and Western Kentucky Gas Company ("Western"); collectively ("participating utilities"). In addition, the following parties sought and were granted intervention status: the Office of the Attorney General ("AG"); Green River Electric Corporation ("Green River"); Henderson-Union Rural Electric Cooperative Corporation ("Henderson-Union"); and the Kentucky Cabinet for Economic Development ("Cabinet").

In its February 10, 1989 Order in this case, the Commission posed several questions pertaining to the feasibility, design and implementation of EDRs. The responses filed by the participating utilities and testimony filed by the Cabinet greatly assisted the Commission in its consideration of effective EDR guidelines. In addition, testimony provided at a hearing conducted on June 22, 1989, and post-hearing briefs filed by several parties further elucidated some of the important issues related to EDRs. The primary issues to be addressed by the Commission in this Order are

adequate capacity requirements, variable cost recovery, customer-specific fixed cost recovery, job creation and capital investment criteria, implementation of EDRs, risk allocation, load eligibility, retention rates, waivers of gas main extension costs, and the appropriate term of EDR contracts. Finally, the Commission will address a Cabinet proposal that it be allowed to file comments pertaining to utilities' EDR contracts.

ADEQUATE CAPACITY REQUIREMENT

The capacity requirements contained in Guidelines 1 and 5 are based on two premises. First, additional load resulting from discounted rates should not create a need for new plant capacity. Second, during periods of excess capacity, the load resulting from EDRs increases a utility's operating efficiency and allows sales of capacity that may not have occurred without the EDRs. Any capacity in excess of a reserve margin normally considered adequate to ensure system reliability could be used to provide service under EDRs without unduly hastening the need for new capacity.

Several participating utilities contend that specific capacity requirements should not be imposed on utilities offering EDRs. Columbia and Delta assert that adequate capacity availability is a responsibility of the utility and should not be a specific requirement of an EDR.[3] EKPC contends that, as long as EDRs exceed marginal costs, EDRs should be offered, even if a

3 Columbia's Response to the Commission's Order dated February 10, 1989, Item 11; Delta's Response to the Commission's Order dated February 10, 1989, Item 11.

utility must add capacity to serve the load.[4] Similarly, KPC states that economic growth should not be capped by a desire to avoid electric capacity additions.[5]

LG&E, on the other hand, contends that without an adequate capacity requirement, new capacity additions could be required to serve a load that is not sharing fully in the fixed cost associated with the capacity addition.[6] Big Rivers states that a utility should demonstrate that adequate capacity is available to serve EDR customers unless the utility can show that any additional capacity needed to serve the new load would not increase its cost of service.[7] Western states that the availability of EDRs should be contingent on a demonstration of adequate capacity.[8]

The Commission finds that EDRs should only be offered during periods of excess capacity and that each utility should demonstrate, upon submission of each EDR contract, that the load expected to be served during each year of the contract period will not cause the utility to fall below a reserve margin that is considered essential for system reliability. Such a reserve

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4 EKPC's Response to the Commission's Order dated February 10, 1989, Item 11.

5 KPC's Response to the Commission's Order dated February 10, 1989, Item 11.

6 LG&E's Response to the Commission's Order dated February 10, 1989, Item 11.

7 Big Rivers' Response to the Commission's Order dated February 10, 1989, Item 11.

8 Western's Response to the Commission's Order dated February 10, 1989, Item 11.

margin should be identified and justified with each EDR contract filing.

Guideline 5 currently requires utilities to withdraw the EDR if adequate reserves are not available to meet anticipated load growth. There is a general feeling among the participating utilities that once the Commission approves an EDR contract for a customer it should not be withdrawn. Columbia maintains that the use of EDRs should be discontinued if adequate capacity is not available to serve new EDR load, however EDRs should not be withdrawn from customers to whom commitments have already been made.[9] Big Rivers states that, at the time an EDR contract is being considered, if the added load cannot be served without increasing system costs, a contractual commitment should not be made.[10] The Commission concludes that, while the load of EDR customers should not create a need for additional capacity, an EDR should not be withdrawn from a customer already under contract.

VARIABLE COST RECOVERY

Guideline 2 currently requires all EDRs to recover variable costs and make some contribution to system fixed costs. The requirement that EDRs exceed variable costs is essential to an effective EDR policy. Revenues received from EDRs that exceed variable costs contribute to a portion of the utility's fixed costs that otherwise would have been paid by nonparticipating

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9 Columbia's Response to the Commission's Order dated February 10, 1989, Item 11(b).

10 Big Rivers' Response to the Commission's Order dated February 10, 1989, Item 11(b).

ratepayers. This contribution results in lower costs for all ratepayers as utility fixed costs are spread over a larger total load.

The participating utilities agree that discounted rates should, in all instances, cover the variable costs associated with serving EDR customers. In addition, EKPC maintains that short-run marginal (variable) costs should include the marginal cost of capacity as well as the marginal cost of energy.[11] LG&E contends that EDRs should not only recover all customer and variable costs, but should also make a contribution to system fixed costs.[12] Western, Big Rivers, KPC and ULH&P assert that utilities should be required to demonstrate that the discounted rate recovers variable cost each time an EDR contract is submitted to the Commission for approval.[13] ULH&P also suggests that a follow-up analysis be performed after the EDR has been in place for at least one year. This analysis should use cost-of-service principles to compare scenarios with and without the EDR customer. Similarly, EKPC states that utilities should submit an annual report to the Commission showing revenues collected from each EDR customer as

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11 EKPC's Response to the Commission's Order dated February 10, 1989, Item 12, page 1 of 3.

12 LG&E's Response to the Commission's Order dated February 10, 1989, Item 12.

13 Western's Response to the Commission's Order dated February 10, 1989, Item 12(a); Big Rivers' Response to the Commission's Order dated February 10, 1989, Item 12(a); KPC's Response to the Commission's Order dated February 10, 1989, Item 12(a); ULH&P's Response to the Commission's Order dated February 10, 1989, Item 12(a).

well as the variable and customer-specific costs associated with serving each customer.[14]

The Commission finds that variable cost recovery is a fundamental requirement of EDRs. Therefore, each time an EDR contract is submitted for approval, utilities should demonstrate that the discounted rate exceeds the total short-run marginal (variable) costs associated with serving that customer for each year of the discount period. Short-run marginal costs will include both marginal capacity costs and marginal energy costs. Demonstration of marginal cost recovery should be accomplished through the use of a current marginal cost-of-service study. A current study is one conducted no more that one year prior to the date of the contract. Furthermore, utilities should submit an annual report to the Commission showing revenues received from each EDR customer and the marginal costs associated with serving each EDR customer. Finally, during rate proceedings, utilities with EDR customers should demonstrate through detailed cost-of-service analysis that nonparticipating ratepayers are not adversely affected by these EDR customers.

CUSTOMER-SPECIFIC FIXED COST RECOVERY

Guideline 2 requires that customer-specific fixed costs associated with serving an EDR customer be recovered either as an up-front payment or as part of a minimum bill over the life of the contract. The participating utilities were fairly evenly divided

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14 EKPC's Response to the Commission's Order dated February 10, 1989, Item 12(a).

on this issue. Columbia, Western, and ULH&P contend that, although customer-specific fixed costs should, in most instances, be recovered from the EDR customer, the recovery mechanism should be developed on a case-by-case basis.[15] EKPC suggests that customer-specific fixed costs be recovered either by a lump-sum payment by the EDR customers or through annual or monthly payments amortized over the EDR period.[16] Big Rivers recommends recovery through a contribution in aid of construction, monthly facilities charge, termination charge, minimum billing demand, or a combination of these methods.[17]

Delta, KU, and LG&E, on the other hand, contend, for various reasons, that customer-specific fixed costs should not be recovered from EDR customers.[18] KU asserts that EDR-specific fixed costs should be assigned to the EDR class as a whole, not to individual customers within the class. LG&E proposes to handle the customer-specific fixed costs associated with EDR customers in a manner similar to its present handling of other customer-specific capital expenditures. LG&E currently provides

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15 Columbia's Response to the Commission's Order dated February 10, 1989, Item 13; Western's Response to the Commission's Order dated February 10, 1989, Item 13; ULH&P's Response to the Commission's Order dated February 10, 1989, Item 13.

16 EKPC's Response to the Commission's Order dated February 10, 1989, Item 13.

17 Big Rivers' Response to the Commission's Order dated February 10, 1989, Item 13.

18 Delta's Response to the Commission's Order dated February 10, 1989, Item 13; KU's Response to the Commission's Order dated February 10, 1989, Item 13; LG&E's Response to the Commission's Order dated February 10, 1989, Item 13.

capital expenditures in an amount up to three times the expected annual net revenues of a customer. The customer must then provide the balance.

The Commission finds that nonparticipating ratepayers should be protected from contributing to the customer-specific fixed costs associated with serving customers who will be receiving a rate discount. It is not unreasonable to require these customers to reimburse the utility for these capital expenditures over the term of an EDR contract. However, the Commission finds that utilities should have the flexibility to design particular mechanisms by which these customer-specific fixed costs are to be recovered. Therefore, all EDR contracts should include a provision allowing for the recovery of customer-specific fixed costs over the term of the contract.

JOB CREATION AND CAPITAL INVESTMENT CRITERIA

Increased economic activity is the major objective of EDRs. Two key indicators of economic activity are job creation and capital investment. EDRs are expected to promote growth in both of these areas. The issue to be addressed here is whether specific job creation and capital investment levels necessary to qualify for EDRs should be established by the Commission, or whether these levels should merely be monitored by the Commission in order to assess the impact of EDRs on economic activity in the state.

The Commission finds that, while job creation and increases in capital investment are the desired outcome of EDRs, requiring

specific levels of job creation and capital investment for EDR eligibility might, in some instances, impede rather than promote economic activity. For instance, such a requirement might prevent a customer from participating in an EDR program even if tangible economic benefits unrelated to job creation or capital investment would have been realized. Furthermore, specific job creation and capital investment levels would be arbitrary and would not recognize the needs and characteristics of individual service areas and of new and expanding customers.

Several participating utilities express similar concerns. EKPC states that while job creation and increased capital investment are expected results of an EDR, an explicit requirement for increases in these areas would not necessarily help an existing customer whose current investment in facilities and employees is underutilized.[19] KPC asserts that, if the Commission establishes a threshold level of jobs or capital investment necessary to qualify for an EDR, some desired new industry might be lost.[20] Columbia and Western both maintain that job creation and capital investment potential are secondary to the load characteristics of the potential EDR customer.[21]

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[19] EKPC's Response to the Commission's Order dated February 10, 1989, Item 5.

[20] KPC's Response to the Commission's Order dated February 10, 1989, Item 5.

[21] Columbia's Response to the Commission's Order dated February 10, 1989, Item 5; Western's Response to the Commission's Order dated February 10, 1989, Item 5.

The Commission finds that a uniform job creation and capital investment requirement for each EDR contract is inappropriate. However, the Commission has determined that monitoring the job creation and capital investment performance of EDRs would provide it with important information with which to measure the effectiveness of its EDR program. Therefore, all utilities with active EDR contracts should file annual reports to the Commission providing information as shown in Appendix A, which is attached hereto and incorporated herein.

IMPLEMENTATION OF EDRs

An EDR can be implemented by either of two methods. First, a standard EDR tariff or rider, explicitly stating all rates, terms and conditions, is filed by a utility and made available to a general classification of customers. Second, a utility files a special contract with an individual customer, which stutes rates, terms and conditions applicable to that specific customer. Guideline 4 currently requires a utility to submit a general EDR tariff, as well as individual contracts with each EDR customer. This procedure was intended to ensure the uniformity of EDRs while identifying the unique usage characteristics of the EDR customers.

The participating utilities have expressed varying opinions regarding the methods by which EDRs should be implemented. Columbia and Western contend that utilities should have the flexibility to design EDRs to match their individual situations.[22]

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[22] Columbia's Response to the Commission's Order dated February 10, 1989, Item 8; Western's Response to the Commission's Order dated February 10, 1989, Item 8.

Big Rivers, KPC, and ULH&P assert that EDRs should be negotiated and offered through special contracts.[23] KPC further states that special contracts would allow the greatest amount of freedom in identifying a customer's needs, while at the same time minimizing the needless revenue reduction that occurs when all new industrial load is granted an EDR concession. Similarly, ULH&P contends that circumstances to be encountered in implementing an EDR are too diverse in nature to be covered by a general tariff. The utility needs to be flexible in negotiating EDRs.

Conversely, EKPC feels that a general tariff would allow better coordination of the review process by the Commission.[24] LG&E contends that a general tariff would avoid a proliferation of individual contracts that could hamper consistent planning.[25] However, LG&E further states that special contracts may be warranted in cases involving extenuating circumstances (i.e. those instances when application of a tariff would be inequitable to the customer class or to the customer).

Initially, the Commission was concerned that implementing EDRs through special contracts would increase the likelihood of the discriminatory use of EDRs by utilities. Even if price discrimination is unintended, EDR contracts would give utilities

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23 Big River's Response to the Commission's Order dated February 10, 1989, Item 8; KPC's Response to the Commission's Order dated February 10, 1989, Item 8; ULH&P's Response to the Commission's Order dated February 10, 1989, Item 8.

24 EKPC's Response to the Commission's Order dated February 10, 1989, Item 8.

25 LG&E's Response to the Commission's Order dated February 10, 1989, Item 8.

the right to selectively choose the customers to whom discounted rates would be offered. This would be unfair to customers whose usage characteristics were similar to customers receiving EDRs through special contracts but for some reason were not offered an EDR by the utility.

On the other hand, however, the Commission realizes that customers do not require identical incentives in order to locate a new facility in a particular area or to expand existing operations. In fact, for some customers, utility rate incentives may not even be a factor in their locational or expansionary decision-making process. Customers who would have decided to locate in Kentucky or expand existing operations even in the absence of rate discounts, but who would take advantage of EDRs that are offered to all new or expanding customers, in effect, become "free riders" on the utility system at the expense of all other ratepayers.

Current Commission EDR guidelines require utilities to file a general EDR rate schedule. This requirement, in effect, fixes the rate discount that is offered to all EDR customers regardless of their individual needs or usage characteristics. This precludes utilities from determining the minimum discount necessary to provide an incentive to new and existing customers and to identify potential free riders who do not require a discounted rate.

The Commission concludes that the revenue loss resulting from free riders taking advantage of rate discounts offered through general EDR tariffs is detrimental to the utility and all nonparticipating ratepayers. The Commission seeks to minimize the

number of free riders taking advantage of discounted utility rates in Kentucky. Therefore, the Commission finds that utilities should have the ability to negotiate discounted rates with individual customers through the use of special contracts. This flexibility should enable the utilities to limit the number of EDRs they offer, thereby reducing the amount of foregone revenues resulting from discounted rates. Consequently, full contributions to system fixed costs would be made by some industrial customers that, under general EDR tariff provisions, would have automatically received rate discounts.

The Commission has previously approved EDR tariffs for Delta[26], Big Rivers[27], Green River[28], and Henderson-Union.[29] These utilities are hereby advised that the Commission will no longer require the implementation of EDRs through general tariffs. EDRs should now be implemented solely through special contracts negotiated with individual large commercial and industrial customers. The Commission finds that Delta, Big Rivers, Green River, and Henderson-Union should continue to honor all existing

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26 Delta's Economic Development Rate was initially approved in 1986. An extension of the tariff was subsequently approved on November 1, 1988.

27 Case No. 10424, The Notice of Big Rivers Electric Corporation of a Proposed Contract with Henderson-Union RECC to Implement an Industrial Incentive Rate.

28 Case No. 89-215, Green River Electric Corporation's Establishment of an Economic Development Rate.

29 Case No. 10422, The Notice of Henderson-Union RECC of a Proposed Contract with Valley Grain Products, Inc., to Implement an Industrial Incentive Plan.

contracts executed pursuant to an approved EDR tariff, but no new contracts related to an EDR tariff should be executed. Furthermore, each of these utilities should modify the availability clause of its EDR tariff to prohibit new customers after the date of this Order.

RISK ALLOCATION

Guideline 6 was developed to allocate fairly between utility shareholders and ratepayers the risk of revenue deficiencies created by discounted rates. A revenue deficiency is the difference between revenue which would have been received in the absence of an EDR (standard rates) and revenue actually received (discounted rates). The Commission sought to ensure that nonparticipating ratepayers were not negatively impacted by discounted rates. To accomplish this, the Commission ordered that utilities allocate at least one-half of all revenue deficiencies to their shareholders. This would likely have been achieved in a rate case by imputing to a utility's test-year revenue an amount equal to one-half of any revenue deficiency.

The participating utilities argue that if a discounted rate covers the marginal cost associated with serving an EDR customer and makes a contribution to system fixed costs, any difference between the regular tariff and the EDR should not be considered a deficiency and recovery of such revenues should not be imputed to the utility in rate proceedings. KPC states that all ratepayers will benefit from the economic improvements stimulated in part by

EDRs.[30] EKPC contends that EDR customers will not be receiving a subsidy from other ratepayers when their rate is equal to or greater than marginal cost.[31]

The Commission concludes that EDRs which are designed to recover all marginal costs and make a contribution to a utility's system fixed costs will benefit all nonparticipating ratepayers. Furthermore, the ratepayers of Kentucky are likely to enjoy additional benefits as a result of increased economic activity in the state. For these reasons, the Commission finds that a specific risk sharing mechanism designed to allocate revenue deficiencies to utility ratepayers and shareholders would be inappropriate and unnecessary. However, the Commission will continue to require all utilities with EDR contracts to demonstrate during rate proceedings that nonparticipating ratepayers are not adversely affected by EDR customers.

LOAD ELIGIBILITY

An important element in the development of an EDR program is the determination of which type load will be eligible for a rate discount. For new large commercial and industrial customers, an EDR is usually applied to all load in excess of a predetermined minimum usage level. For example, if required minimum usage levels are 1,000 KW per month for new electric customers and

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30 KPC's Response to the Commission's Order dated February 10, 1989, Item 12(c).

31 EKPC's Response to the Commission's Order dated February 10, 1989, Item 12(c).

100,000 Mcf per year for new gas customers, a new large commercial or industrial customer that initially contracts for more than 1,000 KW or 100,000 Mcf would qualify for an EDR on all KW or Mcf in excess of those minimum usage levels. For existing large commercial and industrial customers, new load in excess of a specific incremental usage level above a normalized base level may qualify for an EDR. For example, if required incremental usage levels are 1,000 KW per month for existing electric customers and 100,000 Mcf per year for existing gas customers, an existing customer that increases its load by more than 1,000 KW or 100,000 Mcf above its normalized base load would qualify for an EDR on all load in excess of the required incremental usage levels. EDRs applied to either of these type customers serve as an incentive for customers to locate or expand facilities and create new jobs.

The participating utilities agree that EDRs should apply both to the incremental load of existing customers and the load of new customers which exceed certain threshold amounts. All agree that an existing customer should be required to satisfy a minimum level of incremental load above a normalized base load and that new customers should be required to satisfy a minimum usage level before qualifying for EDRs. Most of the participating electric utilities state that a minimum incremental usage level of 1,000 KW above a normalized base load should be required for existing customers and a threshold usage level of 1,000 KW should be required of new customers. EKPC, however, suggests that lower levels be established. EKPC contends that by allowing loads in

excess of a minimum incremental usage level of 100 KW to qualify for an EDR, the opportunities for participation by smaller businesses increase significantly.[32] EKPC maintains that lower incremental usage levels would create an incentive for smaller industries in eastern Kentucky to expand, thereby providing more employment opportunities.

Columbia suggests that the threshold for an EDR offering to an existing gas customer be 100,000 Mcf per year of sustained new gas consumption of a high load factor.[33] The other participating gas utilities did not recommend a specific threshold amount.

The Commission concurs that the job creation potential of EDRs might be enhanced by setting required minimum usage levels as low as possible. Providing an opportunity for smaller commercial and industrial customers to qualify for EDRs would likely result in an increase in new jobs in Kentucky. In addition, free riders will be limited since minimum incremental usage requirements would be retained, although at lower levels.

The Commission will not attempt to determine specific minimum incremental usage levels required for existing customers or the base usage levels required for new customers. Rather, the Commission finds that utilities should have the flexibility to determine the usage levels that will best serve to promote economic development in their service areas. However, at the time

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32 EKPC's Response to the Commission's Order dated February 10, 1989, Item 3(b).

33 Columbia's Response to the Commission's Order dated February 10, 1989, Item 3(b).

an EDR contract is filed, the Commission will expect the utility to identify and justify the minimum incremental usage level and the normalized base load required for an existing customer or the minimum usage level required for a new customer, whichever is applicable. In its review of EDR contracts, the Commission will not only consider the customer's load which is eligible for an EDR, but also the number of new jobs, amount of new capital investment, and the general economic benefits associated with the new or expanding load.

RETENTION RATES

Several participating utilities maintain that EDRs should also be used for the retention of existing load. ULH&P contends that the economic benefits derived from a new customer are the same as those derived from the retention of an existing customer.[34] Big Rivers suggests that EDRs could work for the retention of customers.[35] EKPC expresses its support of the concept of retention rates and states that retaining existing customers is an essential economic development goal.[36]

The Commission finds that EDRs used for the purpose of retaining existing load should be strictly limited and closely monitored. Any utility that files such an EDR contract will also be expected to file a sworn affidavit of the customer stating

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34 Transcript of Evidence ("T.E."), page 133.

35 _Id._, page 97.

36 EKPC's Response to the Commission's Order dated February 10, 1989, Item 5.

that, in the absence of a discounted rate, business operations will cease or be severely restricted. The utility must also demonstrate the financial hardship experienced by the existing customer seeking discounted rates in order to maintain its load on the utility's system.

WAIVERS OF GAS MAIN EXTENSION COSTS

Western proposes that gas utilities be allowed to offer discounts or waivers of the costs of gas main extensions as an alternative to rate discounts.[37] Similarly, the Cabinet stresses the importance of gas utilities being allowed to assist industrial customers with gas main extensions.[38]

The Commission believes that inherent differences which exist between the services provided by gas and electric utilities might necessitate certain differences in the style and format of incentives offered to new and existing customers. Discounts or waivers of gas main extension costs could encourage new large commercial or industrial customers to locate in Kentucky. The Commission, therefore, finds that gas utilities proposing to offer a discount or waiver of gas main extension costs should provide a detailed cost-benefit analysis which compares, among other things, the total costs incurred by the utility by offering such a discount or waiver to the expected revenue stream from the new or expanding customer and the number of new jobs and the amount of

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37 Western's Response to the Commission's Order dated February 10, 1989, page 2.

38 T.E., page 17.

new capital investment to be created. Furthermore, the Commission finds that EDR contracts that include a discount or waiver of gas main extension costs should also include a provision which requires the customer to remain on gas service for a specified term. Gas utilities proposing to offer a discount or waiver of gas main extension costs should provide justification for the required contract term.

TERM OF EDR CONTRACTS

Some of the participating utilities have indicated that the term of an EDR contract should extend for a period of time following the end of the discount period. Service during the final years of the contract would be provided at the rates contained in the standard tariffs. This ensures that each EDR customer will contribute fully to system fixed costs during a portion of their special contract. KU contends that an EDR customer should agree to be served on a standard rate for a period of time commensurate with the discount period.[39] Big Rivers states that a total ten-year contract period should be allowed so that the utility will receive five years of standard rate revenues following a five-year discount period.[40] Finally, EKPC asserts that it would be appropriate to require a customer to sign a

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[39] KU's Response to the Commission's Order dated February 10, 1989, Item 10.

[40] Big Rivers' Response to the Commission's Order dated February 10, 1989, Item 10.

contract which extends for some period of time beyond the expiration of the discount period.[41]

The Commission concurs with these participating utilities and finds that an EDR contract should extend for a period twice the length of the discount period. Furthermore, the discount period should not extend beyond five years. During the second half of an EDR contract, the rates charged to the customer should be identical to those contained in a standard rate schedule that is applicable to the customer's rate class and usage characteristics.

CABINET'S PROPOSAL TO COMMENT ON EDR CONTRACTS

The Cabinet has suggested that it be afforded the opportunity to assist the Commission in its review of EDR contracts by providing comments on each filed EDR contract and the individual merits of the potential EDR customers.[42] The Cabinet asserts that some potential customers, especially those in declining industries, might not deserve an EDR.[43]

The Cabinet currently works closely with utilities in their efforts to locate industries in the state through the activities of an economic development task force known as the Kentucky Industrial Team ("Team").[44] In addition to locating industries in Kentucky, the Team, which is comprised of utility representatives,

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41 T.E., page 89.

42 Cabinet Testimony filed on May 31, 1980, page 5 and T.E., pages 21-22.

43 T.E., page 22.

44 Id., page 23.

Cabinet officials and local economic developers, helps prepare communities for industry.

The Commission acknowledges that Cabinet officials are experienced in dealing with economic development issues as they pertain to Kentucky communities. Furthermore, through its work with the Team, the Cabinet is likely involved in the development of economic development proposals and negotiations, possibly including EDRs, with new and existing large commercial and industrial customers. The Commission believes that comments submitted by the Cabinet pertaining to EDR contracts filed by utilities may be helpful and pertinent.

As stated in 807 KAR 5:011 Section 13, the Commission's regulations applicable to tariffs containing rates, rules and regulations, and general agreements, also apply to the rates and schedules set out in special contracts. Accordingly, the Commission has 30 days following the filing of a special contract during which it can accept, reject, or suspend the contract. Hence, in order to be sufficiently reviewed and considered by the Commission, any written comments prepared by the Cabinet or other interested parties pertaining to an EDR contract filed by a utility must be received by the Commission no more than 20 days after the filing of an EDR contract.

SUMMARY

The Commission, having considered the evidence of record and being otherwise sufficiently advised, finds that:

1. EDRs will provide important incentives to new large commercial and industrial customers to locate facilities in Kentucky and to existing large commercial and industrial customers to expand their operations, thereby bringing much needed jobs and capital investment into Kentucky.

2. Utilities should have the flexibility to design EDRs according to the needs of their customers and service areas and to offer EDRs to those new and existing customers who require such an incentive to locate new facilities in the state and to expand existing ones.

3. EDRs should be implemented by special contracts negotiated between the utilities and their large commercial and industrial customers.

4. An EDR contract should specify all terms and conditions of service including, but not limited to, the applicable rate discount and other discount provisions, the number of jobs and capital investment to be created as a result of the EDR, customer-specific fixed costs associated with serving the customer, minimum bill, estimated load, estimated load factor, and length of contract.

5. EDRs should only be offered during periods of excess capacity. Utilities should demonstrate, upon submission of each EDR contract, that the load expected to be served during each year of the contract period will not cause them to fall below a reserve margin that is considered essential for system reliability. Such a reserve margin should be identified and justified with each EDR contract filing.

6. Upon submission of each EDR contract, a utility should demonstrate that the discounted rate exceeds the marginal cost associated with serving the customer. Marginal cost includes both the marginal cost of capacity as well as the marginal cost of energy. In order to demonstrate marginal cost recovery, a utility should submit, with each EDR contract, a current marginal cost-of-service study. A current study is one conducted no more than one year prior to the date of the contract.

7. Utilities with active EDRs should file an annual report with the Commission detailing revenues received from individual EDR customers and the marginal costs associated with serving those individual customers.

8. During rate proceedings, utilities with active EDR contracts should demonstrate through detailed cost-of-service analysis that nonparticipating ratepayers are not adversely affected by these EDR customers.

9. All EDR contracts should include a provision providing for the recovery of EDR customer-specific fixed costs over the life of the contract.

10. The major objectives of EDRs are job creation and capital investment. However, specific job creation and capital investment requirements should not be imposed on EDR customers.

11. All utilities with active EDR contracts should file an annual report to the Commission providing the information as shown in Appendix A, which is attached hereto and incorporated herein.

12. For new industrial customers, an EDR should apply only to load which exceeds a minimum base level. For existing

industrial customers, an EDR shall apply only to new load which exceeds an incremental usage level above a normalized base load. At the time an EDR contract is filed, a utility should identify and justify the minimum incremental usage level and normalized base load required for an existing customer or the minimum usage level required for a new customer.

13. EDR contracts designed to retain the load of existing customers should be accompanied by an affidavit of the customer stating that, without the rate discount, operations will cease or be severely restricted. In addition, the utility must demonstrate the financial hardship experienced by the customer.

14. The term of an EDR contract should be for a period twice the length of the discount period, with the discount period not exceeding five years. During the second half of an EDR contract, the rates charged to the customer should be identical to those contained in a standard rate schedule that is applicable to the customer's rate class and usage characteristics.

15. Gas utilities proposing to offer a discount or waiver of gas main extension costs should provide a detailed cost-benefit analysis which compares, among other things, the expected revenue stream from the new or expanding customer and the number of new jobs and the amount of new capital investment to be created to the total costs incurred by the utility by offering such a discount or waiver.

16. EDR contracts that include a discount or waiver of gas main extension costs should include a provision which requires the customer to remain on gas service for a specified term. Gas

utilities proposing to offer a discount or waiver of gas main extension costs should provide justification for the required contract term.

17. Comments submitted by the Cabinet or other interested parties pertaining to EDR contracts should be filed with the Commission no more than 20 days following the filing of an EDR contract by a utility.

18. Delta, Big Rivers, Green River, and Henderson-Union should continue to honor all existing contracts executed pursuant to an approved EDR tariff, but no new contracts related to an EDR tariff should be executed. Each of these utilities should modify the availability clause of its EDR tariff to prohibit new customers after the date of this Order.

IT IS THEREFORE ORDERED that:

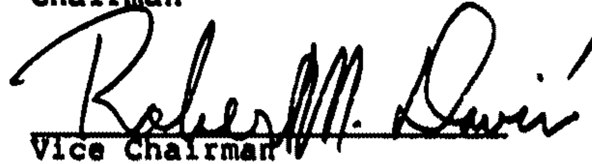
1. When filing EDR contracts, all jurisdictional gas and electric utilities shall comply with Findings 3-17 as if the same were individually so ordered.

2. Delta, Big Rivers, Green River, and Henderson-Union shall continue to honor all existing contracts executed pursuant to an approved EDR tariff, but no new contracts related to an EDR tariff shall be executed. Within 20 days of the date of this Order, each of these utilities shall file new economic development tariffs in which the availability clause has been modified to prohibit new customers after the date of this Order.

Done at Frankfort, Kentucky, this 24th day of September, 1990.

PUBLIC SERVICE COMMISSION

Chairman



Vice Chairman

Commissioner

ATTEST:

Executive Director

APPENDIX A

APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE COMMISSION IN ADMINISTRATIVE CASE NO. 327 DATED 9/24/90

ECONOMIC DEVELOPMENT RATE CONTRACT REPORT

UTILITY: ______________________ YEAR: __________

	Current Reporting Period	Cumulative
1) Number of EDR Contracts -		
Total:	______	______
Existing Customers:	______	______
New Customers:	______	______
2) Number of Jobs Created -		
Total:	______	______
Existing Customers:	______	______
New Customers:	______	______
3) Amount of Capital Investment -		
Total:	______	______
Existing Customers:	______	______
New Customers:	______	______

4) Consumption -

	Current Reporting Period	Cumulative
(A) DEMAND:		
Total:	______ KW|MCF	______ KW|MCF
Existing Customers:	______ KW|MCF	______ KW|MCF
New Customers:	______ KW|MCF	______ KW|MCF
(B) ENERGY/CONSUMPTION:		
Total:	______ KWH|MCF	______ KWH|MCF
Existing Customers:	______ KWH|MCF	______ KWH|MCF
New Customers:	______ KWH|MCF	______ KWH|MCF