COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

AN INVESTIGATION OF BIG RIVERS CORPORATION'S WHOLESALE POWER CONTRACT WITH HOOSIER ENERGY RURAL ELECTRIC COOPERATIVE, INC.	))) CASE NO. 93-163)

O R D E R

This investigation was initiated by the Commission on April 6, 1993, based on its preliminary review of a wholesale power contract between Big Rivers Electric Corporation ("Big Rivers") and Hoosier Energy Rural Electric Cooperative, Inc. ("Hoosier Energy"). A public hearing on the proposed contract was held on September 30, 1993. Intervenors of record are the Attorney General of the Commonwealth of Kentucky ("AG") and the Kentucky Industrial Utility Customers ("KIUC").

On October 19, 1993, the Commission denied Big Rivers' motion to dismiss this case on the grounds that the Commission lacked subject matter jurisdiction over the proposed contract. On November 5, 1993, Big Rivers appealed the Commission's October 19, 1993 Order to Franklin Circuit Court. The appeal was dismissed on November 3, 1995 pursuant to a stipulation of dismissal, thereby placing the case back before the Commission for a final decision.

The proposed contract calls for Big Rivers to supply "unit power capacity" from D. B. Wilson Unit No. 1 ("Wilson") for the months of June through September for each year from 1993 through 1999. The amount of capacity provided escalates from 10,000 kilowatts in 1993 to 170,000 kilowatts in 1999; the rates escalate from $4.85 per kilowatt-month in 1993 to $7.50 per kilowatt-month in 1999. For "unit power energy" taken under the contract, Hoosier Energy will pay rates escalating from 21 mills per kilowatt-hour in 1993 to 31 mills per kilowatt-hour in 1999. The contract was approved by the Rural Electrification Administration in 1993.

The AG and KIUC offer different positions on the contract. The AG commends Big Rivers for generating additional revenue by making a four month peaking sale when a year-round firm capacity sale could not be made. KIUC does not strongly oppose the contract but recommends that two conditions be imposed to assure that Big Rivers' native load customers are not adversely affected by the contract. Those conditions are that: (1) energy sales under the contract be assigned the highest incremental fuel cost incurred on Big Rivers' system at the time of the sale, and; (2) Hoosier Energy be required to pay capacity charges on any energy purchases during the October to May period not covered by the contract.

Big Rivers states that while the contract is structured as a unit power sale from Wilson, the energy will be priced at system incremental costs. Thus, fuel costs for energy sold might or might not be from Wilson since the energy will be priced at the incremental fuel costs resulting from the economic dispatch of Big Rivers' system. Big Rivers contends that KIUC's first condition would result in a departure from the Commission's fuel adjustment clause ("FAC") regulation by requiring it to assign the highest fuel cost incurred on the system at the time of the Hoosier Energy sale to inter-system sales regardless of whether the higher cost is actually "related to" the Hoosier Energy sale. In response to KIUC's second proposed condition, Big Rivers states that neither it nor the Commission can unilaterally alter the terms of the contract; Big Rivers suggests that should it attempt to impose such a condition, Hoosier Energy would opt to purchase power elsewhere during the October to May period rather than make capacity payments on economy power purchases.

Based on the evidence of record and being otherwise sufficiently advised, the Commission finds that KIUC has failed to demonstrate the need for or reasonableness of either of its proposed conditions. Big Rivers' intention to reflect the fuel costs related to the sale as a credit in its FAC calculation is consistent with both industry practice and the Commission's FAC regulation. KIUC's proposal that the Hoosier Energy sale be priced at the system's highest fuel cost at the time of the sale appears to be based solely on the desire to have the system's lowest cost generation assigned to native load customers regardless of the circumstances affecting the sale and the manner in which the system is dispatched. While the Commission would like to see the lowest cost generation assigned to Big Rivers' native load customers, our focus in this case is whether the revenue to be received under the sale to Hoosier Energy is reasonable and in the best interests of Big Rivers' and its native load customers.

KIUC's proposal would assign the lowest cost generation to native load customers even though such generation might not have been dispatched absent the Hoosier Energy sale. In theory under an economic dispatch operation, the generating units with the lowest operating costs are run first, followed by the incrementally higher cost units on an as needed basis. Unfortunately, many utilities, including Big Rivers, cannot operate under a theoretical economic dispatch because they have one or more high volume, minimum-take coal contracts with vintage prices above current market prices.

For these utilities, the obligation to purchase large quantities of above-market priced coal skews their economic dispatch because the higher cost units must be run first to avoid excessive inventory levels. Consequently, it is the lower cost generation that is often run on an incremental basis to make off-system sales, such as the one proposed here to Hoosier Energy. Under these circumstances, assigning fuel costs under the contract based on the actual dispatching order of generating units is reasonable. Furthermore, native load customers will not be adversely affected by this allocation of fuel costs because they will not pay for more than they would have paid absent the sale to Hoosier Energy.

KIUC's second condition, requiring Hoosier Energy to pay capacity charges on energy purchased during the eight months not covered by the contract, is neither reasonable nor within the scope of the proposed contract. Capacity charges are properly included in a sale of power only when the seller has set aside some generating capacity for the benefit of the buyer.

In this case, Big Rivers has agreed to set aside capacity for Hoosier Energy only during the months of June through September. Since Big Rivers is free to sell that capacity the remaining eight months of the year, Hoosier Energy should not be required to pay any capacity charges. Big Rivers remains obligated to use its best efforts to sell at the highest available price all power not needed to serve native load customers. To the extent that Big Rivers is able to sell power during the October through May period and recover both energy and capacity charges, native load customers will benefit. To the extent that power can only be sold during that period at a price greater than the incremental cost of generation, native load customers will still benefit, albeit to a lesser degree.

IT IS THEREFORE ORDERED that Big Rivers' contract to sell peaking power to Hoosier Energy is approved as filed.

Done at Frankfort, Kentucky, this 5th day of January, 1996.

PUBLIC SERVICE COMMISSION

Linda K Breathitt
Chairman

Vice Chairman

Robert M. Davis
Commissioner

ATTEST:

Don Mills
Executive Director