

COMMONWEALTH OF KENTUCKY  
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

APPLICATION OF KENTUCKY POWER	)	
COMPANY FOR APPROVAL OF THE TERMS	)	
AND CONDITIONS OF THE RENEWABLE	)	
ENERGY PURCHASE AGREEMENT FOR	)	
BIOMASS ENERGY RESOURCES BETWEEN	)	CASE NO.
THE COMPANY AND ECOPOWER	)	2013-00144
GENERATION-HAZARD LLC; AUTHORIZATION	)	
TO ENTER INTO THE AGREEMENT; GRANT	)	
OF CERTAIN DECLARATORY RELIEF; AND	)	
GRANT OF ALL OTHER REQUIRED	)	
APPROVALS AND RELIEF	)	

ORDER

On April 10, 2013, Kentucky Power Company ("Kentucky Power") filed an application, pursuant to KRS 278.300, seeking approval of the terms and conditions of a Renewable Energy Purchase Agreement for Biomass Energy Resources ("REPA") and authorization to enter into the REPA with ecoPower Generation-Hazard LLC ("ecoPower"). Kentucky Power also seeks a declaration that the recovery of all costs associated with the REPA via a monthly rider or surcharge is appropriate.

On July 3, 2013, Kentucky Power filed a motion requesting permission to amend its application to include a proposed Biomass Energy Rider ("Tariff B.E.R."), pursuant to KRS 278.271, to recover the costs for the purchase of renewable energy under the REPA. According to its motion, Kentucky Power and ecoPower also agreed to amend the REPA to extend the deadline in which a final, non-appealable decision from the Commission is issued.

In addition to amending its application, Kentucky Power requests to deviate from the financial exhibit requirements of 807 KAR 5:001, Section 12, which requires the exhibit to reflect operations for a 12-month period ending not more than 90 days prior to the date the application is filed. Kentucky Power proposes to update the required financial exhibit to use an income statement and balance sheet from March 31, 2013. Kentucky Power requests this deviation, arguing that the March 31, 2013 income statement and balance sheet are only four days beyond the period prescribed by the regulation and consistent with the date used in its pending rate application,<sup>1</sup> which would provide a meaningful basis for evaluating the proposed REPA.

Kentucky Power also requests to deviate from the notice requirements of 807 KAR 5:011, Section 8(2)(b)(3), which requires any notice provided by newspaper advertisement be made by the date the filing is submitted. Kentucky Power requests a deviation to permit it to make the first publication by no later than July 17, 2013, due to its efforts to file the motion to amend, and the amended application, at the earliest possible date. Kentucky Power argues that the requested deviation would not prejudice its customers or the parties to this matter, given that, at that time, the formal hearing was still two months away.

The following parties sought and were granted full intervention in this matter: the Attorney General of the Commonwealth of Kentucky, by and through his Office of Rate Intervention ("AG"), and Kentucky Industrial Utility Customers, Inc. ("KIUC"). The Commission issued orders establishing procedural schedules for the processing of this

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<sup>1</sup> Case No. 2013-00197, *Application of Kentucky Power Company for a General Adjustment of Electric Rates* (filed June 28, 2013).

matter, which provided for discovery upon Kentucky Power's application, an opportunity to file intervenor testimony, discovery on intervenor testimony, and an opportunity for Kentucky Power to file rebuttal testimony. A formal evidentiary hearing was conducted on August 28 and 29, 2013. The parties filed post-hearing briefs on September 23, 2013, and Kentucky Power filed its responses to post-hearing data requests on September 13, 2013. The matter now stands submitted for a decision.

### **BACKGROUND**

Kentucky Power is an electric utility organized under KRS Chapter 278 and is engaged in the generation, purchase, transmission, distribution, and sale of electric power to approximately 173,000 customers located in 20 eastern Kentucky counties. Kentucky Power is a direct, wholly owned subsidiary of American Electric Power ("AEP") and a member of PJM Interconnection, LLC ("PJM"). AEP is a multi-state public utility holding company, whose operating companies, including Kentucky Power, provide electric utility service to customers in parts of 11 states. PJM is a federally regulated regional transmission organization which coordinates the movement of wholesale electricity in all or parts of 13 states and the District of Columbia.

EcoPower is a limited liability company organized under the laws of Kentucky, with its principal office located in Lexington, Kentucky. On May 18, 2010, the Kentucky State Board on Generation and Electric Transmission Siting approved ecoPower's request for a certificate to construct a 58.5-MW biomass-fired merchant electric generating facility ("Biomass Facility") and a 69-kV non-regulated transmission line in

Perry County, Kentucky.<sup>2</sup> The ecoPower Biomass Facility is to be built on a 125-acre tract of reclaimed coal mine land situated within the Coal Fields Regional Industrial Park. The Biomass Facility will be fueled with wood biomass or byproducts (sawdust, bark, wood chips, tip wood, low-quality logs, etc.). The Biomass Facility will be interconnected to Kentucky Power's system at its 69-kV Engle substation located approximately 1.5 miles from the ecoPower facility.

On March 15, 2013, Kentucky Power and ecoPower executed the REPA, which is subject to the Commission's approval. Under the terms of the REPA, Kentucky Power would purchase all of the output produced from the Biomass Facility, which includes the energy, capacity, environmental attributes, including renewable energy credits ("RECs"),<sup>3</sup> and all other ancillary services available from the facility. Kentucky Power intends to bank the RECs, which inures to the benefit of its customers. Kentucky Power states that it may also investigate the options of selling the RECs in the short-term and credit any net proceeds to customers. The REPA has a 20-year term with an initial all-in, around-the-clock contract price of \_\_\_\_/MWh.<sup>4</sup> The REPA also contains

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<sup>2</sup> Case No. 2009-00530, *Application of ecoPower Generation-Hazard, LLC for a Certificate to Construct and Operate a Merchant Electric Generating Facility and a 69 kV Transmission Line in Perry County, Kentucky* (Ky. State Board on Electric Generation and Transmission Siting, May 18, 2010).

<sup>3</sup> RECs are part of the power characteristics produced by renewable energy generators, such as the Biomass Facility. Each REC represents 1 MWh of generation sourced from a qualifying renewable energy resource. RECs, whose market values are dependent on location and type of generation, can be sold, banked, or retired.

<sup>4</sup> Kentucky Power filed a petition for confidential treatment of the contract pricing terms. The Commission issued an order on August 27, 2013 denying that petition. Kentucky Power then filed a motion for rehearing, which was granted for the purpose of further consideration. The rehearing request is discussed and denied in this order. Pursuant to 807 KAR 5:001, Section 13(5), when confidentiality is denied, "the material shall not be placed in the public record for the time period permitted pursuant to KRE 278.410 to bring an action for review."

an escalator provision in which the contract price would increase by \_\_\_\_ percent each year.<sup>5</sup>

Kentucky Power's witness testified that this escalator provision is normal and reasonable when compared to other purchase power agreements and is designed to lessen the rate impact in the earlier years of the REPA.<sup>6</sup> Kentucky Power is obligated to pay only for power that it actually receives from the Biomass Facility and only at the contract price. It is anticipated that the Biomass Facility will begin commercial operation in early 2017.

### **KENTUCKY POWER'S ARGUMENT**

Kentucky Power contends that the proposed REPA presents it with a unique opportunity to invest in its service territory, promote economic development, provide for future load growth, and diversify its generation portfolio with a Kentucky-based renewable resource. Kentucky Power asserts that the REPA complies with the requirements of KRS 278.300. In particular, Kentucky Power argues that the financial obligations to be assumed by it under the REPA are for lawful objects within its corporate purpose because it will add capacity and energy resources that will support economic development for a biomass renewable energy project in Kentucky Power's service territory. Kentucky Power points out that the Biomass Facility is expected to create approximately 230 construction jobs during the two-year construction period, approximately 30 full-time jobs at the Biomass Facility, and approximately 225 timber- and trucking-related jobs in the local eastern Kentucky area. Kentucky Power contends that the REPA is needed to allow it to diversify its generation portfolio and support

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<sup>5</sup> *Id.*

<sup>6</sup> Jay Godfrey's August 28, 2013 hearing testimony at 15:34:35.

renewable development in Kentucky as set forth in Governor Beshear's 2008 Energy Plan, titled "Intelligent Energy Choices for Kentucky's Future." The energy plan called for an increase in renewable energy generation to 1,000 MW by 2025 and specifically called for the development of woody biomass-fueled energy.

Kentucky Power maintains that the REPA is needed to mitigate the loss of as much as 30 MW of capacity as a result of the retirement of its 800-MW Big Sandy Unit 2 and replacing it with a 780-MW interest in the Mitchell Generating Station, as well as the anticipated repowering of its 278-MW Big Sandy Unit 1 as a 268-MW natural gas-fired generating facility. Kentucky Power also points out that in 2017, when the Biomass Facility is scheduled to come online, and based on its current load forecast without the REPA generation, it will have an 18 percent reserve margin, which is 3 percent above the reserve margin required by PJM. With the REPA generation, Kentucky Power is expected to have a cushion of approximately 6 percent above what is required by PJM, which, according to Kentucky Power, would give it the ability to satisfy needed load growth without going to the market or constructing new generation assets. Kentucky Power also contends that the REPA will be needed as a capacity resource after the AEP-East Interconnection Agreement ("Pool Agreement") is terminated on January 1, 2014. Kentucky Power noted that it has enjoyed access to low-cost capacity and energy for over five decades as a member of the Pool Agreement and, after the Pool Agreement terminates, it will be required to address any capacity and energy deficits as a stand-alone company within PJM. Kentucky Power asserts that the REPA would provide it with price certainty and would preclude the need to pay prices set for power in the PJM market.

Kentucky Power acknowledges that the REPA is more expensive than other traditional fossil-fuel options for capacity and energy needs. However, it contends that renewable energy as a whole is typically more expensive and that the REPA provides other benefits that must be weighed in evaluating whether the capacity and energy to be added is considered wasteful duplication. According to Kentucky Power, those benefits represent an investment in economic development of its service territory in the form of renewable biomass energy located in the Commonwealth of Kentucky, an increased generation margin for future load growth, and diversifying its generation portfolio. Kentucky Power points out that in Kentucky, and particularly in its service territory, there is neither an established market for renewable energy resources nor an abundance of available renewable technologies to consider.

Kentucky Power asserts that the financial obligations assumed under the REPA are necessary and appropriate for, and consistent with, the provision of electric service in its service territory because the REPA presents Kentucky Power with a unique opportunity to invest in its service territory, promote economic development, and provide for future load growth. Kentucky Power also asserts that the REPA will not impair its ability to provide adequate, efficient, and reasonable electric service to its customers. Kentucky Power states that the REPA contains numerous provisions that protect Kentucky Power and its customers from risk over the long term of the agreement, noting that it pays only for the power it actually receives from ecoPower and only at the expressed contract rate. Any potential increase in fuel costs, costs to comply with environmental regulations, or transmission upgrades are to be borne by ecoPower. Kentucky Power contends that the REPA would not negatively impact its credit rating

and that its borrowing costs would not be thus impacted because Tariff B.E.R. contains provisions that ensure timely recovery of all of the REPA costs. In addition, KRS 278.271 provides for full cost recovery of the REPA over the entire initial term of the agreement upon the Commission's approval of the same.

In light of the benefits associated with the REPA and the protections found in the agreement, Kentucky Power argues that the financial obligations assumed by it under the REPA are reasonably necessary and appropriate for its provision of electric service.

With respect to its request for approval of Tariff B.E.R., pursuant to KRS 278.271, to recover the costs not otherwise recovered in rates for the purchase of renewable energy under the REPA, Kentucky Power contends that the REPA satisfies all of the requirements of KRS 278.271. Kentucky Power argues that the Biomass Facility received a certificate from the Kentucky State Board on Electric Generation and Transmission Siting in Case No. 2009-00530. Kentucky Power also argues that the REPA is consistent with the policies outlined in KRS 154.27-020(2) because it promotes the development of an innovative energy-related business that advances the public purposes of creating new jobs and new investments, achieving energy independence, and creating new sources of tax revenues. Lastly, Kentucky Power contends that the full costs of the REPA are fair, just, and reasonable given the benefits associated with the REPA in the form of economic development, increased capacity to meet future load growth, fuel diversity, and investment in renewable energy technology. The evidence indicates that the rate impact of the REPA in 2017, when the Biomass Facility is expected to be operational, is 5.99 percent.<sup>7</sup>

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<sup>7</sup> Kentucky Power's Response to Commission Staff's Post Hearing Data Request filed Sept. 13, 2013.



### **AG'S ARGUMENT**

The AG states that it could not support the proposed REPA because Kentucky Power has failed to demonstrate that the REPA is needed; because the REPA is not the least-cost alternative even assuming arguendo that Kentucky Power has a need for capacity and energy resources; and because the cost of the REPA would not result in fair, just, and reasonable rates. In particular, the AG cites to Kentucky Power's admission that it did not conduct or perform any studies or analyses to determine whether there is a need for the REPA. The AG also argues that Kentucky Power failed to conduct any analysis to determine whether the REPA would be the least-cost alternative, assuming that additional power is needed by Kentucky Power, noting that the Commission has historically applied a least-cost standard in cases involving supply-side planning or acquisition, including purchase power agreements.

The AG contends that the standard to be applied under KRS 278.271 for recovery of costs not currently in rates for the purchase of electric power from a biomass energy facility is that of a reasonable standard based on a plain reading of the statute and which is consistent with the setting of any tariff or rate. As applied in the instant matter, the AG maintains that Kentucky Power has failed to demonstrate that the costs associated with the proposed REPA, which would amount to approximately \$50 million annually, or a total of over \$1 billion over the 20-year term of the contract, are fundamentally reasonable. The AG argues that Kentucky Power has conducted no studies or analysis to evaluate the economics of the REPA or to demonstrate that the REPA is economically feasible as compared to other generation resources, including other renewable resources. The AG avers that the evidence in this case indicates the

Biomass Facility would result in a net economic loss to the region, rather than being an economic driver for the region, as suggested by Kentucky Power.

### **KIUC'S ARGUMENT**

KIUC recommends that the Commission reject Kentucky Power's application for approval of the proposed REPA. KIUC argues that Kentucky Power has failed to demonstrate that the full costs of the REPA over its 20-year term are fair, just, and reasonable. KIUC contends that Kentucky Power has not provided any evidence to establish that the price of the REPA is reasonable. Notably absent, KIUC proffers, is any analysis showing how the cost of the REPA compares to Kentucky Power's cost projections of other generation sources or market prices over the 20-year term of the REPA or any competitive solicitation for resources which would gauge how the costs of the REPA would compare to other alternatives. Moreover, KIUC points out that Kentucky Power acknowledged that it conducted no studies or analysis to determine whether the REPA is least-cost.

KIUC argues that Kentucky Power also failed to demonstrate that the proposed REPA promotes the policy set forth in KRS 154.27-020(2). Other than a basic quantification of the number of jobs and wages to be paid to ecoPower employees, KIUC maintains that Kentucky Power failed to conduct any economic-impact study associated with the Biomass Facility. KIUC asserts that the economic benefit of new jobs being created by the Biomass Facility must be evaluated by the cost of the REPA to Kentucky Power's ratepayers to determine if the REPA, in fact, creates new jobs, new investments, and new tax revenues as set forth in KRS 154.27-020(2). Based on its own economic analysis of the Biomass Facility, KIUC contends that the REPA would

result in a net economic loss to the area of eastern Kentucky served by Kentucky Power. Specifically, KIUC maintains that its economic analysis shows that the additional jobs claimed by Kentucky Power in connection with the Biomass Facility would result in approximately \$9.1 million of additional annual revenues to the local economy. However, the REPA would cost approximately \$35 million to \$39 million annually in the form of increased rates that Kentucky Power's ratepayers would have to bear. This potential \$30 million net cost would reflect a drain or leakage in the local economy, as all of that amount would not be reinvested in the eastern Kentucky economy, causing the local economy to shrink rather than expand.

KIUC asserts that the REPA is not needed, based upon Kentucky Power's admission that under its current generation-resource plan, there is no need for the capacity, and upon the absence of any studies or analysis by Kentucky Power indicating such a need for capacity. KIUC also asserts that the REPA is not the least-cost alternative of providing capacity and energy to Kentucky Power's customers, noting that Kentucky Power failed to conduct any study or analysis which would purport to indicate that the REPA is the least-cost source of capacity and energy. KIUC contends that the REPA is not least-cost, but is expensive when comparing the capital cost of the Biomass Facility to the recently certificated natural gas combined-cycle unit currently being constructed by Louisville Gas and Electric Company and Kentucky Utilities Company,<sup>8</sup> or even when compared to Kentucky Power's own decision to purchase a

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<sup>8</sup> Case No. 2011-00375, *Joint Application of Louisville Gas and Electric Company and Kentucky Utilities Company for a Certificate of Public Convenience and Necessity and Site Compatibility Certificate for the Construction of a Combined Cycle Combustion Turbine at the Cane Run Generating Station and the Purchase of Existing Simple Cycle Combustion Turbine Facilities from Bluegrass Generation Company, LLC in LaGrange, Kentucky* (Ky. PSC May 3, 2012).

50 percent interest in the Mitchell Generation Station.<sup>9</sup> KIUC argues that the rate impact will be higher than Kentucky Power has projected. KIUC also contends that the REPA will be treated by credit-rating agencies as imputed debt and that Kentucky Power will be required to increase its actual common equity at the expense of less expensive long-term debt in its capital structure, thereby making the REPA even more costly. KIUC argues that the RECs are not likely to provide a significant offset to the costs of the REPA. Lastly, KIUC maintains that there are likely other renewable resources available that are significantly less expensive than the proposed REPA.

### **DISCUSSION**

In Case No. 2009-00545,<sup>10</sup> we articulated the standard of review for cases involving approval of a purchase power agreement as evidence of indebtedness under KRS 278.300. Pursuant to KRS 278.300, a utility must establish that the proposed assumption of obligation or liability is for some lawful object within the corporate purposes of the utility, is necessary or appropriate for or consistent with the proper performance by the utility of its service to the public and will not impair its ability to perform that service, and is reasonably necessary and appropriate for such purpose. In addition to the standards set forth in KRS 278.300, the Commission must also analyze the need for the purchase power agreement under the Commission's existing statutory

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<sup>9</sup> Case No. 2012-00578, *Application of Kentucky Power Company for (1) a Certificate of Public Convenience and Necessity Authorizing the Transfer to the Company of an Undivided Fifty Percent Interest in the Mitchell Generating Station and Associated Assets; (2) Approval of the Assumption by Kentucky Power Company of Certain Liabilities in Connection with the Transfer of the Mitchell Generating Station; (3) Declaratory Rulings; (4) Deferral of Costs Incurred in Connection with the Company's Efforts to Meet Federal Clean Air Act and Related Requirements; and (5) All Other Required Approvals and Relief* (Ky. PSC Oct. 7, 2013).

<sup>10</sup> *Application of Kentucky Power Company for Approval of Renewable Energy Purchase Agreement for Wind Energy Resources between Kentucky Power Company and FPL Illinois Wind, LLC* (Ky. PSC June 28, 2010).

authority where, as here, the purchase power agreement is intended to add supplemental generating capacity to the utility. In examining the statutory criteria for approving financing under KRS 278.300(3), the “purposes and uses of the proposed issue” are for the acquisition of new generation; and for the debt to be “for some lawful object within the corporate purposes of the utility.” A utility must also establish a need for additional generation and the absence of wasteful duplication, both as required under KRS 278.020(1).

“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 or operated.

[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.<sup>11</sup>

“Wasteful duplication” is defined as “an excess of capacity over need” and “an excessive investment in relation to productivity or efficiency, and an unnecessary multiplicity of physical properties.”<sup>12</sup> For an applicant 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 reasonable alternatives has been performed.<sup>13</sup>

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<sup>11</sup> *Kentucky Utilities Co. v. Public Service Commission*, 252 S.W.2d 885, 890 (Ky. 1952).

<sup>12</sup> *Id.*

<sup>13</sup> Case No. 2005-00142, *Joint Application of Louisville Gas and Electric Company and Kentucky Utilities Company for a Certificate of Public Convenience and Necessity for the Construction of Transmission Facilities in Jefferson, Bullitt, Meade, and Hardin Counties, Kentucky* (Ky. PSC Sept. 8, 2005).

Selection of a proposal that ultimately costs more than an alternative does not necessarily result in wasteful duplication.<sup>14</sup> All relevant factors must be balanced.<sup>15</sup>

Because this case involves the application of KRS 278.271, our analysis must also fully consider the statutory mandates set forth in that statute. KRS 278.271 provides in full as follows:

Notwithstanding any provision of law to the contrary, upon application by a regulated utility, the commission may allow recovery of costs which are not recovered in the existing rates of the utility for the purchase of electric power from a biomass energy facility that has received a certificate from the Kentucky State Board on Electric Generation and Transmission Siting pursuant to KRS 278.700 to 278.716. No recovery shall be allowed unless the full costs of the purchase power agreement over the full term of the agreement, which shall be included as part of the application, have been found by the commission to be fair, just, and reasonable. In determining whether the agreement is fair, just, and reasonable, the commission may consider the policy set forth by the General Assembly in KRS 154.27-020(2). The commission's approval of cost recovery under this section shall be valid for the entire initial term of the agreement.

KRS 154.27-020(2) provides in full as follows:

The General Assembly hereby finds and declares that it is in the best interest of the Commonwealth to induce the location of innovative energy-related businesses in the Commonwealth in order to advance the public purposes of achieving energy independence, creating new jobs and new investment, and creating new sources of tax revenues that but for the inducements to be offered by the authority to approved companies would not exist.

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<sup>14</sup> See *Kentucky Utilities Co. v. Pub. Serv. Comm'n*, 390 S.W.2d 168, 175 (Ky. 1965). See also Case No. 2005-00089, *Application of East Kentucky Power Cooperative, Inc. for a Certificate of Public Convenience and Necessity for the Construction of a 138 kV Electric Transmission Line in Rowan County, Kentucky* (Ky. PSC Aug. 19, 2005).

<sup>15</sup> Case No. 2005-00089, *East Kentucky Power*, Order dated August 19, 2005 at 6.

KRS 278.271 was enacted on March 5, 2013, and the instant matter represents a case of first impression for the Commission's consideration of KRS 278.271. Based upon our reading of KRS 278.271, the Commission finds that the statute has broadened our statutory authority when considering whether the costs associated with a purchase power agreement for the purchase of electric power from a certificated biomass energy facility are fair, just, and reasonable. Historically, the Commission has applied a least-cost analysis in setting rates that are fair, just, and reasonable and in reviewing applications for certificates to construct utility facilities under KRS 278.020(1),<sup>16</sup> as was applied in Case No. 2012-00578 involving Kentucky Power's acquisition of the Mitchell Generating Station. However, KRS 278.271 expands the least-cost analysis to include the legislative policies set forth in KRS 154.27-020(2), i.e., the inducement of innovative energy-related business to be located in Kentucky in order to achieve energy independence, create new jobs and new investments, and create new sources of tax revenues. Thus, in considering the proposed REPA in the case sub judice, the Commission must determine whether there is a need for the REPA and whether the cost of the REPA is reasonable in light of the legislative policies set forth in KRS 154.27-020(2).

Having reviewed the record, and being otherwise sufficiently advised, the Commission finds that Kentucky Power has sufficiently established that there is a need for the REPA and that the REPA is fair, just, and reasonable as required under the

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<sup>16</sup> See, Case No. 2011-00375, *Joint Application of Louisville Gas and Electric Company and Kentucky Utilities Company for a Certificate of Public Convenience and Necessity and Site Compatibility for the Construction of a Combined Cycle Combustion Turbine at the Cane Run Generation Station and the Purchase of Existing Simple Cycle Combustion Turbine Facilities from Bluegrass Generation Company, LLC in LaGrange, Kentucky* (Ky. PSC May 3, 2012), at 15, citing Case No. 2009-00545, *Application of Kentucky Power for Approval of Renewable Energy Purchase Agreement for Wind Energy Resources Between Kentucky Power Company and FPL Illinois Wind, LLC* (Ky. PSC June 28, 2010).



recently established standard in KRS 278.271. We note that Kentucky Power is undergoing a fundamental change in its generation portfolio with the retirement of the 800-MW Big Sandy Unit 2 to be replaced with the acquisition of 780-MW from the Mitchell Generating Station and the anticipated request to convert the 278-MW coal-fired Big Sandy Unit 1 into a 268-MW natural gas-fired facility. This change would leave Kentucky Power with approximately 30 MW less capacity, which would be mitigated by the 58.5 MW to be purchased from the REPA. More significantly, the REPA will satisfy Kentucky Power's need to diversify its generation portfolio in light of pending environmental regulations that would place additional economic constraints on the continued reliance on coal-fired electric generation facilities. The Commission takes note of President Obama's June 25, 2013 Climate Action Plan and Presidential Memorandum directing the Environmental Protection Agency to "...issue proposed carbon pollution standards, regulations, or guidelines, as appropriate, for modified, reconstructed, and existing power plants by no later than June 1, 2014."<sup>17</sup> Carbon standards for existing power plants, in whatever form they take, are expected to increase the constraints on utilities, such as Kentucky Power, that rely heavily on coal-fired generation.

Moreover, with the recent release of the EPA's Proposed Carbon Pollution Standard for New Power Plants on September 20, 2013, it is necessary to investigate new sources for electricity generation in the Commonwealth of Kentucky. Subsequent to developing the 2008 Energy Plan, Governor Beshear recognized the importance of biomass as a source of energy and convened the Executive Task Force on Biomass

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<sup>17</sup> Presidential Memorandum of June 25, 2013, Power Sector Carbon Pollution Standards, 78 Fed. Reg. 39535 (2013).



and Biofuel Development in August 2009.<sup>18</sup> The task force was charged with facilitating “the development of a sustainable biomass and biofuels industry in Kentucky that will generate prosperity in a carbon-constrained environment, and revitalize rural Kentucky by creating new jobs and strengthening local economies.”<sup>19</sup> The Final Report from the Executive Task Force on Biomass and Biofuels Development in Kentucky (“Final Report on Biomass and Biofuels Development in Kentucky”) found, among other things, that:

1. As carbon dioxide becomes a regulated greenhouse gas, Kentucky's cost of electricity is at high risk unless supplemented by renewable energy.
2. Kentucky's geography and climate give it an advantage for meeting a portion of base load generation with biomass.
3. By 2025 Kentucky can produce 2,000 megawatts of renewable electricity capacity using 15 million tons of biomass. This is a feasible means of reducing electricity cost risks associated with carbon management.<sup>20</sup>

The proposed REPA would allow Kentucky Power to address its need to diversify its generating portfolio, and at the same time, it would promote biomass energy development in Kentucky, consistent with the policy directives set forth by Governor Beshear's 2008 Energy Plan and the Final Report on Biomass and Biofuels Development in Kentucky.

The Commission further finds that Kentucky Power has established that the REPA is fair, just, and reasonable in conformity with the requirements of KRS 278.271. While the Commission recognizes that the cost of the proposed REPA would not have

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<sup>18</sup> Final Report from the Executive Task Force on Biomass and Biofuels Development in Kentucky, at 7 (Dec. 10, 2009).

<sup>19</sup> *Id.* at 2.

<sup>20</sup> *Id.* at 25.

withstood scrutiny based strictly on a least-cost analysis, our consideration of the REPA must also take into account the policy mandates laid out in KRS 154.27-020(2). We conclude that the REPA promotes the inducement of an innovative energy-related business located in Kentucky that would advance the public purposes of achieving energy independence, creating new jobs and new investment, and creating new sources of tax revenues. We note that the Biomass Facility would be the first of its kind in Kentucky and that the project would create 230 construction jobs, 30 full-time jobs at the facility, and 225 timber- and trucking-related jobs. We further conclude that the economic benefits associated with the development of the Biomass Facility in conjunction with the advancement of the expressed policy dictates set forth in KRS 154.27-020(2), as referenced in KRS 278.271, sufficiently justify a finding that the REPA is reasonable and should be approved.

We are persuaded by Kentucky Power's argument that, because the REPA contains provisions that ensure timely cost recovery and because KRS 278.271 provides for full recovery of the REPA costs, its borrowing costs would not be negatively impacted by the REPA. In order to fully protect Kentucky Power's ratepayers in the unlikely event that Kentucky Power would need to increase its common equity position in order to maintain a favorable credit rating as a result of the REPA, the Commission will require Kentucky Power to hold its ratepayers harmless if such an event would occur.

Lastly, we find that Kentucky Power's request for authority to enter into the REPA is for lawful objects within the corporate purposes of Kentucky Power, is necessary and appropriate for and consistent with the proper performance by Kentucky Power of its

service to the public, will not impair its ability to perform that service, is reasonable, necessary, and appropriate for such purposes, and should be approved.

### **MISCELLANEOUS ISSUES**

#### **Off-System Sales**

As we stated earlier, Kentucky Power is in the midst of a unique transformation of its operations, having to consider the disposition of a significant portion of its generation portfolio. This case is just one step towards how Kentucky Power will propose to reconstitute its generation assets. As has been mentioned in this matter, we anticipate that Kentucky Power will file a certificate case for the repowering of Big Sandy Unit 1. Also, the Commission recently granted Kentucky Power's request for approval to acquire a 50 percent interest in the Mitchell Generating Station.<sup>21</sup> The final resolution of the disposition of Big Sandy Unit 1 will bring more clarity to Kentucky Power's capacity and energy needs. Accordingly, the Commission will closely scrutinize Kentucky Power's treatment of its off-system sales and any associated mechanism proposed in its next base rate case.

#### **Reporting Requirement**

In light of the fact that the construction of the Biomass Facility will not be completed until January 2017, at which time the power plant will become operational, the Commission will want to be kept apprised of the progress of the construction project. Accordingly, we will require Kentucky Power, through ecoPower, to submit semi-annual status reports on the construction of the Biomass Facility.

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<sup>21</sup> Case No. 2012-00578, Order issued October 7, 2013.

### Kentucky Power's Motion for Rehearing

On April 11, 2013, Kentucky Power filed a petition seeking confidential treatment, pursuant to 807 KAR 5:001, Section 13, and KRS 68.171(c), of certain terms and provisions of the REPA. The information sought to be treated as confidential included pricing information and certain material contract terms. Kentucky Power contends that this information is generally recognized as confidential or proprietary and, if publically disclosed, would permit an unfair commercial advantage to Kentucky Power's competitors. On August 27, 2013, the Commission issued an order denying the petition on the grounds that Kentucky Power failed to establish that the information identified in its petition was entitled to confidential treatment pursuant to KRS 61.878(c)(1). Specifically, the Commission found that disclosure of the terms and conditions of the proposed REPA would not place Kentucky Power at an unfair competitive advantage in the future because of the unique circumstances giving rise to the execution of the REPA.

On September 16, 2013, Kentucky Power filed a motion for rehearing of the Commission's August 27, 2013 Order. Kentucky Power argues that the Commission's finding that disclosure of those terms and conditions of the REPA sought to be kept confidential would not competitively harm Kentucky Power was unsupported by substantial evidence. Kentucky Power contends that the unique characteristics of the REPA as found by the Commission, does not eliminate or lessen the competitive injury that Kentucky Power is likely to suffer as a result of the public disclosure of the information at issue. Kentucky Power asserts that the unique circumstances described by the Commission in the August 27, 2013 Order, such as the period over which the

contract was negotiated, the economic benefits resulting from the REPA, the statutory basis for cost recovery, and the Commission's consideration of this application, are not relevant in determining whether the disclosure of the terms and conditions of the REPA sought to be kept confidential would provide other sellers of renewable products with an unfair competitive advantage in future negotiations with Kentucky Power.

Kentucky Power contends that the evidence of record substantially supports its request to keep the subject information confidential, arguing that disclosure would subject it to competitive injury. In particular, Kentucky Power noted that (1) the renewable energy market is extremely competitive and it faces strong competition for the most advantageous agreements; (2) the information at issue is sought by other renewable suppliers as a means of obtaining a commercial advantage; (3) such information, if publicly disclosed, would tend to establish a floor for future negotiations to Kentucky Power's detriment; (4) public disclosure of the subject terms and conditions would signal Kentucky Power's willingness to potentially depart from standard terms and conditions; and (5) public disclosure would discourage potential renewable suppliers from participating in future solicitations out of fear that their confidential information could be disclosed.

Having reviewed the motion, the evidentiary record, and being otherwise sufficiently advised, the Commission finds that Kentucky Power has failed to satisfy its burden of proof, on rehearing, to persuade the Commission to modify the August 27, 2013 Order. The Commission's ultimate finding that the negotiations and ultimate execution of the REPA were of such a unique and singular nature that the disclosure of the terms and conditions sought to be treated as confidential would not result in any

competitive injury to Kentucky Power remains unchanged. Kentucky Power's argument on rehearing essentially is that public disclosure of such information would cause it competitive harm in future negotiations with other renewable suppliers. We disagree. The Commission notes that the REPA reflects an agreement for the purchase of renewable energy produced from a biomass generating facility located in Kentucky. Kentucky Power entered into such an agreement primarily because it would be able to potentially recover the costs associated with the REPA pursuant to KRS 278.271, which requires, among other things, that the biomass energy facility has received a certificate from Kentucky State Board on Electric Generation and Transmission Siting ("Siting Board"). The Biomass Facility is the first and only kind of its type in Kentucky and, to date, the only merchant biomass energy facility certificated by the Siting Board. The Commission takes administrative notice that there is currently no formal application pending before the Siting Board seeking a certificate to construct a merchant biomass energy facility. The planning and development of a biomass energy facility project would likely take a number of years even before the project could reach the point where formal approval by the Siting Board would occur. The likelihood of Kentucky Power's engaging in negotiations similar to the one at bar is highly remote, especially in the near and intermediate term. Thus, the market for Kentucky-based biomass renewable power is not competitive and Kentucky Power would not suffer competitive injury upon the disclosure of the terms and conditions of the REPA sought to be kept confidential. In addition, we are in this Order approving Kentucky Power's request to recover from ratepayers all costs of the REPA. Those ratepayers have a right to know the actual costs of the renewable power that they are purchasing, and they have a right to know

the evidence upon which the Commission relied in determining that the REPA costs are fair, just, and reasonable. Accordingly, the Commission will deny Kentucky Power's motion for rehearing.

IT IS THEREFORE ORDERED that:

1. Kentucky Power's request to amend its application is approved.
2. Kentucky Power's application, as amended, for approval of the terms and conditions of the REPA and authorizing it to enter into the REPA is approved.
3. Kentucky Power's request to recover the costs for the purchase of renewable energy under the REPA pursuant to KRS 278.271 and via the proposed Tariff B.E.R. is approved.
4. The REPA cost shall be limited to the contract rate as expressed in the REPA. Any additional incremental costs shall be borne by ecoPower, as provided in the REPA, and Kentucky Power's ratepayers shall be held harmless.
5. Any benefits resulting from Kentucky Power's decision to bank the RECs associated with the REPA shall be credited to Kentucky Power's ratepayers.
6. Any net proceeds resulting from Kentucky Power's decision to sell any RECs associated with the REPA shall be credited to Kentucky Power's ratepayers.
7. In the event Kentucky Power's credit rating is negatively impacted by the REPA, causing Kentucky Power to increase its common equity position, Kentucky Power shall hold its ratepayers harmless should such an event occur.
8. Kentucky Power's request to deviate from the financial exhibit requirements of 807 KAR 5:001, Section 12, is granted.



9. Kentucky Power's request to deviate from the notice requirements of 807 KAR 5:011, Section 8(2)(b)(3), is granted.

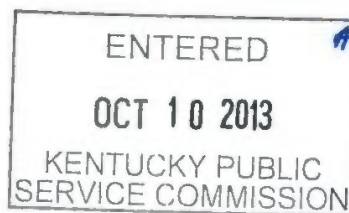
10. Kentucky Power's motion for rehearing is denied.

11. Within 20 days from the date of this Order, Kentucky Power shall file with the Commission, using the Commission's electronic Tariff Filing System, its tariff sheets as approved herein, showing their date of issue and that they were issued by authority of this Order.

12. Beginning January 3, 2014 and every six months thereafter until the Biomass Facility comes online, Kentucky Power shall file with the Commission a written report detailing the status of the construction of the Biomass Facility, including, but not limited to, the progress made since the last written update was submitted, the construction steps to be taken in the upcoming six-month period, whether the construction is meeting its current project schedule, an update of all permits needed for the Biomass Facility and photographs of the construction site depicting the progress of the construction project.

13. Any documents filed pursuant to ordering paragraph 12 of this Order shall reference the number of this case and shall be retained in the utility's general correspondence file.

By the Commission



ATTEST:

  
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Executive Director



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