

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

APPLICATION OF BIG RIVERS ELECTRIC CORPORATION FOR TERMINATION OF CONTRACTS AND A DECLARATORY ORDER AND FOR AUTHORITY TO ESTABLISH A REGULATORY ASSET)	CASE NO.
)	2018-00146
)	
)	

ORDER

On May 1, 2018, Big Rivers Electric Corporation (BREC) filed an application seeking a declaratory order confirming BREC's determination that the Station Two Generation Station (Station Two) units are no longer capable of normal, continuous, reliable operation for the economically competitive production of electricity, and that a series of related contracts (Station Two Contracts), except the Joint Facilities Agreement, have terminated.¹ BREC also requests a finding from the Commission authorizing BREC to continue to operate Station Two under the terms of the Station Two Contracts to allow the city of Henderson, Kentucky and the Henderson Utility Commission (collectively, "Henderson") time to find alternate arrangements for the operation of Station Two and for the city's power supply needs, if Henderson desires that BREC do so.² Lastly, BREC requests Commission authorization to establish, for accounting purposes, a regulatory asset to defer the expenses related to the termination of the Station Two Contracts.³

¹ Application at 4.

² *Id.*

³ Application at 6-7.

BREC states that it currently has an asset on its books of approximately \$89.6 million relating to the value of the Station Two Contracts that BREC would have to retire and write off as a result of the termination of the Station Two Contracts.⁴ BREC also proposes to apply the revenues it receives through rates associated with Station Two depreciation expense (Station Two Depreciation Revenues) to offset the Station Two regulatory asset.⁵

The intervenors in this matter are the Attorney General of the Commonwealth of Kentucky, by and through the Office of Rate Intervention (Attorney General), and Kentucky Industrial Utility Customers, Inc. (KIUC).

An interim declaratory Order was issued on August 29, 2018, confirming BREC's determination that the Station Two units are no longer economically viable; that the Station Two Contracts, except the Joint Facilities Agreement, have terminated pursuant to its terms; and authorizing BREC to continue to operate Station Two under the terms of the Station Two Contracts until May 31, 2019, unless BREC and Henderson reach a mutually acceptable agreement regarding the ongoing operation of Station Two prior to May 31, 2019, or the Commission directs BREC to cease operation of Station Two prior to May 31, 2019. The August 29, 2018 Order specifically reserved ruling on BREC's request for authorization to establish a regulatory asset until a later date.

Subsequent to the issuance of the August 29, 2018 Order, BREC sought and was granted a request to hold the proceedings in abeyance to allow the parties to this matter adequate time and opportunity to finalize the terms of a unanimous settlement agreement

⁴ *Id.*

⁵ Application at 7–8.

addressing the remaining issues in this matter. On September 26, 2018, BREC filed a motion requesting leave to file a Settlement Agreement, Stipulation, and Recommendation (Settlement Agreement) with supporting testimony. The Commission finds that BREC has established good cause to allow it leave to file the Settlement Agreement and supporting testimony and that its motion should be granted.

A status conference hearing was held on October 2, 2018, in which BREC presented the terms of the Settlement Agreement, and each party articulated its justification for approving the Settlement Agreement. This matter now stands submitted for a decision.

SETTLEMENT AGREEMENT

BREC states that the Settlement Agreement reasonably resolves the remaining issues in the instant proceeding. The remaining issues principally involve BREC's request to establish a regulatory asset to defer expenses it incurs relating to the termination of the relevant Station Two Contracts (Station Two Regulatory Asset), including the asset of approximately \$89.6 million relating to the remaining net book value of BREC's historical investment in Station Two that BREC would otherwise have to retire and write off as a result of the termination of the Station Two Contracts.⁶ BREC also proposes to apply the Station Two Depreciation Revenues to offset the Station Two Regulatory Asset.⁷ BREC notes that KIUC, in its filed testimony, recommended the Commission (1) deny BREC's request for authority to establish the Station Two

⁶ Supplemental Direct Testimony of Robert W. Berry (Berry Supplemental Testimony) at 3.

⁷ *Id.*

Regulatory Asset and (2) direct BREC to defer KIUC's estimate of the savings resulting from the termination of the Station Two Contracts as a regulatory liability.⁸

Pursuant to the Settlement Agreement, the parties agree that BREC should be allowed to establish the Station Two Regulatory Asset and that, in lieu of offsetting the Station Two Regulatory Asset with the Station Two Depreciation Revenues or deferring KIUC's estimate of the savings, BREC should be allowed to establish the following two credits: (1) the Station Two Depreciation Credit and (2) the TIER Credit.⁹ BREC describes the Station Two Depreciation Credit as being a monthly credit that will reduce BREC's bills to its three-member distribution cooperatives through the Member Rate Stability Mechanism (MRSM) tariff.¹⁰ BREC states that unless it is unable to complete its exit of the Station Two Contracts prior to May 31, 2019, the Station Two Depreciation Credit will be \$453,785 per month for 12 consecutive months, for a total credit of \$5,445,420.¹¹

The Station Two Depreciation Credit reflects the depreciation expense savings from the period beginning when BREC completes its exit of the Station Two Contracts (no later than May 31, 2019) to when BREC anticipates new rates going into effect (January 1, 2021).¹² BREC notes that once it exits the Station Two Contracts it will no longer record a depreciation expense for Station Two on its books, but will continue to recover that expense in its rates until it files its next base rate case, at which time the

⁸ *Id.*

⁹ Settlement Agreement at 4–7. *See also*, Berry Supplemental Testimony at 4.

¹⁰ *Id.* at 18.

¹¹ *Id.* at 19.

¹² *Id.* at 20–21.

Station Two depreciation expense will be removed from rates.¹³ Based on an annual depreciation expense associated with Station Two of \$3,439,211, which was included in the forecasted test period in BREC's most recent rate case,¹⁴ the depreciation expense savings for the 19-month period between May 31, 2019, and January 1, 2021, amounts to \$5,445,420. This amount reflects the total Station Two Depreciation Credit if BREC exits the Station Two Contracts on May 31, 2019.¹⁵

The total Station Two Depreciation Credit will be greater than \$5,445,420 if BREC is able to complete its exit of the Station Two Contracts prior to May 31, 2019. For each day prior to May 31, 2019, that BREC is able to complete its exit of the Station Two Contracts, the total amount of the credit will increase by an amount corresponding to one day's worth of Station Two's depreciation expense, or \$9,422.¹⁶

The Station Two Depreciation Credit will be credited to members for 12 consecutive months, beginning the latter of January 2019 or the month following the Commission's acceptance of BREC's revised MRSM tariff.¹⁷ Each month in which the Station Two Depreciation Credit is owed, BREC will deposit the monthly amount into the applicable Economic Reserve accounts for the Rural Delivery Service (Rural) and the

¹³ *Id.* at 20.

¹⁴ Case No. 2013-00199, *Application of Big Rivers Electric Corporation for a General Adjustment in Rates Supported by Fully Forecasted Test Period* (Ky. PSC Apr. 25, 2014).

¹⁵ Berry Supplemental Testimony at 21.

¹⁶ *Id.* \$3,439,211 ÷ 365 = \$9,422.

¹⁷ Settlement Agreement at 5.

Large Industrial Customer (Large Industrial) classes¹⁸ and the MRSM will draw from those accounts to reduce BREC's Rural and Large Industrial bills to its members.¹⁹ The total amount of each monthly credit will be divided between the Rural and Large Industrial classes by allocating 72.62 percent to the Rural class and 27.38 percent to the Large Industrial class.²⁰ BREC states that the allocation of the credit is based on the allocation of the Station Two depreciation expense in its most recent cost of service study filed in Case No. 2013-00199, and notes that the parties to the Settlement Agreement agreed that this allocation is appropriate because it allocates the credit in the same proportion in which the 2013 cost of service study projected that the classes would pay for the Station Two costs in rates.²¹

The second credit mechanism is the TIER Credit, which reflects the savings that BREC will achieve as a result of the termination of the Station Two Contracts.²² Under the TIER Credit, BREC will apply any net margins that it earns above the margins that would result in BREC achieving a times interest earned ratio (TIER) of 1.45 for any calendar year beginning with the calendar year 2019 and ending with the calendar year prior to the year in which new rates become effective in BREC's next base rate case.²³ The TIER Credit will be applied against the Station Two Regulatory Asset and the

¹⁸ The Station Two Depreciation Credit will not apply to industrial loads that currently receive an economic development rate. Aleris is the only retail customer on the BREC system that is served under an economic development incentive rate and the economic incentive rate applies only to the expanded Aleris load and not to its base load prior to expansion. See, Berry Supplemental Testimony at 23–24.

¹⁹ Berry Supplemental Testimony at 19–20.

²⁰ *Id.* at 19.

²¹ *Id.* at 22.

²² *Id.* at 24.

²³ *Id.*

regulatory assets established to defer depreciation expense for the Wilson Station and the Coleman Station.²⁴

BREC states that the 1.45 TIER threshold was determined based on BREC's financial projection that it would achieve a 1.45 TIER in 2020, the first full year without the Station Two Contracts if the Station Two Contracts had continued.²⁵ Thus, BREC avers that the 1.45 TIER represents a reasonable and appropriate threshold for capturing the savings BREC achieves as a result of the termination of the Station Two Contracts.²⁶ The Settlement Agreement also allows BREC discretion to provide a greater TIER Credit, which would ultimately result in further reducing the Station Two, Wilson, and Coleman regulatory assets.²⁷ BREC's ability to provide a greater TIER Credit is conditioned upon it achieving a TIER greater than the 1.30 TIER used to establish BREC's rates in its last rate case and upon a determination by BREC that further reducing the regulatory assets is in its and its members' best interests.²⁸

The Settlement Agreement also contains a stipulation in which BREC agrees in its next rate case to propose the reasonable and prudent utilization of its member equity in such a way as to best achieve the dual goals of minimizing the rate increase and improving BREC's credit metrics to best achieve and maintain investment grade credit ratings.²⁹ The Attorney General and KIUC each agree to support BREC's request for rate

²⁴ *Id.*

²⁵ *Id.* at 28.

²⁶ *Id.*

²⁷ *Id.* at 29.

²⁸ *Id.*

²⁹ Settlement Agreement at 8. *See also*, Berry Supplemental Testimony at 31.

recovery of the Station Two Regulatory Asset amortization.³⁰ KIUC further agrees to support BREC's request for rate recovery of the Coleman regulatory asset, net of the reasonable and prudent utilization of member equity.³¹ The Attorney General agrees to support rate recovery of the Wilson regulatory asset and Wilson's ongoing depreciation expense, and fixed operating costs provided BREC's next rate case application results in a proposed annual impact on the Rural and Large Industrial classes of zero percent or less as compared to the then-current rates.³²

The parties to this matter, and in particular BREC, assert that the Settlement Agreement is a fair, just, and reasonable resolution to the remaining issues in this matter. BREC points out that the terms of the agreement provides immediate cash savings to ratepayers and ensures that they will benefit from the savings that will result from the Station Two Contract termination. BREC also states that the provisions of the agreement will assist its efforts to regain and maintain all three of its investment grade credit ratings. BREC specifically notes that, in the years since the two aluminum smelters exited its system, it has worked diligently and successfully to mitigate the loss of that significant load and is on the verge of completing its plan to return to financial stability since it recently regained one of its investment grade credit ratings. BREC states that approval of the Settlement Agreement by the Commission would show continued regulatory support and would assist in BREC obtaining the other investment grade credit ratings.

³⁰ Settlement Agreement at 8. *See also*, Berry Supplemental Testimony at 31.

³¹ Settlement Agreement at 8. *See also*, Berry Supplemental Testimony at 31.

³² Settlement Agreement at 9. *See also*, Berry Supplemental Testimony at 31–32.

Lastly, BREC notes that the Settlement Agreement would also be subject to the review and approval by the Rural Utilities Service.

DISCUSSION

Having reviewed the record and being otherwise sufficiently advised, the Commission finds that terms of the Settlement Agreement are fair, just, and reasonable and that the Settlement Agreement should be approved in full. Regarding the parties' agreement that BREC be permitted to establish the Station Two Regulatory Asset, the Commission finds that this is reasonable given that such costs are extraordinary and non-recurring and that the termination of the Station Two Contracts will result in significant savings that will fully offset the costs.³³ The Commission further finds that the two credit mechanisms established pursuant to the terms of the Settlement Agreement will provide immediate rate benefits to retail customers in the BREC system and mitigate against any increase that BREC proposes in its next rate application while also assisting BREC's efforts to achieve all three of its investment grade credit ratings.

IT IS THEREFORE ORDERED that:

1. BREC's motion for leave to file the Settlement Agreement and supporting testimony is granted.
2. The Settlement Agreement is approved.
3. BREC's request for authority to establish, for accounting purposes, the Station Two Regulatory Asset is approved.

³³ See Case No. 2008-00436, *Application of East Kentucky Power Cooperative, Inc. for an Order Approving Accounting Practices to Establish a Regulatory Asset Related to Certain Replacement Power Costs Resulting from Generation Forced Outages* (Ky. PSC Dec. 23, 2008) (Noting that the Commission has historically exercised its discretion to approve regulatory assets where a utility has incurred, among other things, an extraordinary or nonrecurring expense that over time will result in a saving that fully offsets the cost).

4. BREC's proposed revisions to the MRSM tariff are approved.
5. Within 20 days of the date of entry of this Order, BREC shall file with the Commission, using the Commission's electronic Tariff Filing System, new tariff sheets setting forth the modifications approved herein and reflecting their effective date and that they were authorized by this Order.
5. The case is hereby closed and removed from the Commission's docket.

[REMAINDER OF PAGE INTENTIONALLY LEFT BLANK]

By the Commission



ATTEST:


Executive Director

Case No. 2018-00146

*Jody Kyler Cohn
Boehm, Kurtz & Lowry
36 East Seventh Street
Suite 1510
Cincinnati, OHIO 45202

*Rebecca W Goodman
Assistant Attorney General
Office of the Attorney General Office of Rate
700 Capitol Avenue
Suite 20
Frankfort, KENTUCKY 40601-8204

*Honorable James M Miller
Attorney at Law
Sullivan, Mountjoy, Stainback & Miller, PSC
100 St. Ann Street
P.O. Box 727
Owensboro, KENTUCKY 42302-0727

*Big Rivers Electric Corporation
201 Third Street
P. O. Box 24
Henderson, KY 42420

*Justin M. McNeil
Office of the Attorney General Office of Rate
700 Capitol Avenue
Suite 20
Frankfort, KENTUCKY 40601-8204

*Thomas J Costakis
Krieg DeVault LLP
One Indiana Square
Suite 2800
Indianapolis, INDIANA 46204

*Honorable Kurt J Boehm
Attorney at Law
Boehm, Kurtz & Lowry
36 East Seventh Street
Suite 1510
Cincinnati, OHIO 45202

*Norman T Funk
Krieg DeVault LLP
One Indiana Square
Suite 2800
Indianapolis, INDIANA 46204

*Kent Chandler
Assistant Attorney General
Office of the Attorney General Office of Rate
700 Capitol Avenue
Suite 20
Frankfort, KENTUCKY 40601-8204

*Tyson Kamuf
Corporate Attorney
Big Rivers Electric Corporation
201 Third Street
P. O. Box 24
Henderson, KY 42420

*Lawrence W Cook
Assistant Attorney General
Office of the Attorney General Office of Rate
700 Capitol Avenue
Suite 20
Frankfort, KENTUCKY 40601-8204

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