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Via Overnight Mail

November 21, 2012

Mr. Jeff Derouen, Executive Director
Kentucky Public Service Commission
211 Sower Boulevard
Frankfort, Kentucky 40602

Re: Case No. 2012-00226

Dear Mr. Derouen:

Please find enclosed the original and ten (10) copies of the BRIEF OF KENTUCKY INDUSTRIAL UTILITY CUSTOMERS, INC. for filing in the above-referenced docket.

By copy of this letter, all parties listed on the Certificate of Service have been served. Please place this document of file.

Very Truly Yours,

Michael L. Kurtz, Esq.
Kurt J. Boehm, Esq.
Jody M. Kyler, Esq.
BOEHM, KURTZ & LOWRY

MLKkew
Attachment
cc: Certificate of Service
Faith Burns, Esq.

G:\WORK\KIUC\KP Cases\2012-00226 (Real Time Pricing RTP)\KPSC Ltr.docx

CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing was served by mailing a true and correct copy via electronic mail (when available) and Overnight Mail to all parties on this 21st day of November, 2012.

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PUBLIC SERVICE COMMISSION

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

IN THE MATTER OF: THE APPLICATION OF KENTUCKY POWER COMPANY TO WITHDRAW ITS TARIFF RTP PENDING SUBMISSION BY THE COMPANY AND APPROVAL BY THE COMMISSION OF A NEW REAL-TIME PRICING TARIFF	:	**Case No. 2012-00226**

BRIEF OF
KENTUCKY INDUSTRIAL UTILITY CUSTOMERS, INC.

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November 21, 2012

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**BRIEF OF
KENTUCKY INDUSTRIAL UTILITY CUSTOMERS, INC.**

INTRODUCTION

This case is not about large manufacturing customers shifting their production processes and associated energy usage to off-peak periods. Whether and to what extent load-shifting on Tariff RTP has satisfied Kentucky Power Company's ("Kentucky Power" or "Company") unwritten guidelines or its intent in establishing the rate is not relevant since load-shifting is not required under the language, terms, and conditions of the tariff. Load-shifting can only be measured through the use of a customer baseline. A customer baseline is the centerpiece of the newly proposed Rider RTP, but is conspicuously absent from the currently effective Tariff RTP. Kentucky Power's protest that Tariff RTP customers have not load-shifted is merely an after-the-fact attempted justification by the Company to renege on a bargain it now considers uneconomic.

This case is about the integrity of the settlement process and about money. As part of a major rate case settlement a little over two years ago, Kentucky Power agreed to extend the experimental Tariff RTP for an additional three years (through June 2013). Tariff RTP explicitly gives up to ten customers the option to have electricity provided by Kentucky Power be subject to market-based pricing, as determined by PJM capacity and energy rates, plus transmission, distribution and administrative charges. A market-based real-time pricing program was uniquely adopted for Kentucky Power, and is not used by any other utility in Kentucky.

Subjecting their load to market-based pricing is a risk that has been evaluated carefully by customers for many years. Five Kentucky Industrial Utility Customers, Inc. ("KIUC") members who take service from Kentucky Power (Air Liquide Large Industries U.S. LP, AK Steel Corporation, Air Products & Chemicals, Inc., EQT Corporation and Catlettsburg Refining LLC, a subsidiary of Marathon Petroleum) have agreed to take that risk. In July 2012, those customers lost money as market-based pricing was more expensive than Kentucky Power's average embedded cost rates. How the economics will work out through June 2013 remains uncertain. But those KIUC customers who agreed to the 2010 rate case settlement and who have elected to accept the risks under Tariff RTP through June 2013 have a legal entitlement to do so, absent a compelling public interest to the contrary. The money which Kentucky Power forecasts that its shareholders may lose is exactly equivalent to the money its customers stand to gain.

This case only affects Kentucky Power's shareholders and the five KIUC customers. No other ratepayers will be impacted. Any revenue loss or revenue gain to Kentucky Power over the one-year period in question will be a one-time nonrecurring event which cannot be reflected in base rates or otherwise. Moreover, Kentucky Power's current after-tax return on equity is in the range of 10%-11%. These earnings figures demonstrate more than adequate profits for the Company, not financial hardship, even after months of customers taking service under Tariff RTP.

It would be perfectly appropriate for this Commission to adopt the newly-proposed Rider RTP and its customer baseline approach on a going-forward basis beginning July 2013. But the existing Tariff RTP should be allowed to continue for the full term agreed to by the parties in the Commission-approved unanimous settlement from Kentucky Power's last major rate case.

ARGUMENT

I. Kentucky Power's Request To Withdraw Existing Tariff RTP And To Establish The Fundamentally Different Proposed Rider RTP Would Violate The Explicit Language Of The Unanimous Settlement Agreement In Kentucky Power's Last Rate Case And The Commission's June 28, 2010 Order Approving That Settlement.

In reaching the Settlement in Kentucky Power's last base rate case, parties expressly bargained for, and Kentucky Power agreed to, a three-year extension of *existing* Tariff RTP. Specifically, paragraph 9 (a) of the Settlement provides:

> *"The **existing RTP Tariff** shall be extended for an additional three-year period; further the tariff shall be amended to permit customers to enroll at any point during a year for a minimum twelve consecutive month period."*[1]

The Commission's June 28, 2010 Order approving the Settlement likewise states that *existing* Tariff RTP would be extended for three years:

> *"Kentucky Power's **existing Real-Time Pricing tariff** shall be continued for three years, with customers able to enroll at any point during a year for a minimum period of 12 months."*[2]

Hence, based upon the parties' unanimous agreement in the Settlement, the Commission explicitly approved of the extension of *existing* Tariff RTP through June 30, 2013. And in filings before the Commission, Kentucky Power reiterated this Settlement commitment. For example, in June 2011, the Company stated:

> *"It is noteworthy to mention that in a Commission Order in Kentucky Power Company's last retail rate case (Case No. 2009-00459), the RTP tariff was continued for three years, and will allow customers to enroll at any point during the year for a minimum period of 12 months."*[3]

Kentucky Power also acknowledged its Settlement commitment regarding Tariff RTP in December 2011:

> *"However, as part of the Unanimous Settlement Agreement in Case No. 2009-00459, Kentucky Power has agreed to extend the RTP tariff for an additional three years."*[4]

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[1] KIUC Ex. 1 (emphasis added).
[2] KIUC Ex. 4, Commission Order, Case No. 2009-00459 (June 28, 2010) at 6 (emphasis added).
[3] KIUC Ex. 6, Kentucky Power Annual Report (June 30, 2011).
[4] KIUC Ex. 7, Kentucky Power Report on Real-Time Pricing Tariff (Dec. 16, 2011).

Accordingly, as recently as last year, Kentucky Power openly acknowledged its commitment to extend *existing* Tariff RTP for three years, in accordance with the Settlement. Yet now, when customers have actually begun taking service under Tariff RTP, Kentucky Power seeks to quickly withdraw existing Tariff RTP in violation of its Settlement commitment and to deprive customers of an important benefit of the Settlement.

Paragraphs 14(b) and (d) of the Settlement require the signatory parties to act in good faith and support enforcement of the Settlement:

> *"(b) Kentucky Power and the Intervenors shall act in good faith and use their best efforts to recommend to the Commission that this Unanimous Settlement Agreement be approved in its entirety and without modification, and that the rates and charges set forth herein implemented.*
>
> *(d) Kentucky Power and the Intervenors further agree to support the reasonableness of this Unanimous Settlement Agreement before the Commission, and to cause their counsel to do the same, including in connection with any appeal from the Commission's adoption or enforcement of this Settlement Agreement."*

Kentucky Power's unreasonable attempt to deprive customers of an important benefit of the Settlement runs counter to this language. The immediate withdrawal of existing Tariff RTP is directly contrary to the Settlement and the Commission's Order approving that Settlement. The Commission should not endorse Kentucky Power's request to be excused from its Settlement commitment. Instead, the Commission should allow Tariff RTP to continue until its stipulated expiration in June 2013, in accordance with the Settlement and the Commission's Order approving that Settlement.

II. There Is No Valid Reason To Justify The Modification Of The Settlement Or The Commission's Order Approving That Settlement.

KIUC acknowledges that the Commission has ongoing authority to modify a utility's rates to ensure that the rates continue to be just and reasonable, pursuant to multiple provisions of KRS 278.[5] Paragraph 16 of the

[5] KRS 278.030; *See also* Order, Case No. 2011-00036 (April 12, 2012) at 3 ("It is clear from the Court's March 8, 2012 Order that both KIUC and Big Rivers have disputes over the Rate Order, and that the Commission is the agency with jurisdiction over all of the rate matters in dispute. Pursuant to KRS 278.040(2) and KRS 279.210(1), the Commission has exclusive jurisdiction over the rates of Big Rivers. In addition, KRS 278.260(1) empowers the Commission with original jurisdiction over complaints as to the rates of Big Rivers, and the Commission can make such investigation of those rates as it deems necessary or convenient, either upon a complaint in writing or on its own motion. Further, pursuant to KRS 278.390, the Rate Order continues in force until revoked or modified by the Commission, unless the Order is suspended or vacated in whole or in part by order or decree of a court of competent jurisdiction, while, under KRS 278.270, the Commission is authorized to prescribe a just and reasonable rate to be charged prospectively after conducting an investigation under KRS 278.260(1)").

Settlement acknowledges this authority. Further, equating the Settlement to a contract, the *Mobile-Sierra* doctrine would allow the Commission to modify the Settlement if the Commission found that the Settlement would seriously harm the public interest.[6] The Commission has relied upon the doctrine for a similar purpose in the past.[7] But Kentucky Power has failed to provide any legitimate reason why existing Tariff RTP causes rates to be unjust or unreasonable and/or how Tariff RTP seriously harms the public interest.

Kentucky Power provides two primary reasons in support of its request to immediately withdraw Tariff RTP, alleging that Tariff RTP has not fulfilled its "intent" of encouraging customers to engage in load-shifting and that Kentucky Power may incur revenue losses as a result of customers taking service under the tariff.[8] KIUC responds to each of these arguments below.

A. Kentucky Power's Argument That Tariff RTP Has Not Satisfied Its "Intent" Is Contrary To The Plain Language Of The Tariff.

1. The Plain Language Of Existing Tariff RTP Does Not Require Customers To Alter Their Regular Production Schedules In Response To Market Prices, But The Plain Language Does Allow Customers To Place A Designated Portion Of Their Load On PJM Market Capacity And Energy Pricing.

As an initial matter, Kentucky Power has acknowledged that the language of Tariff RTP sets out four minimum qualifications for taking service under the tariff. Kentucky Power has also acknowledged that the KIUC members currently taking service under Tariff RTP meet those four qualifications. In response to Staff's Second Set of Requests for Information, Item No. 6, Kentucky Power stated:

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6 *NRG Power Mktg., LLC v. Maine Pub. Utilities Comm'n*, 130 S. Ct. 693, 696, 175 L. Ed. 2d 642 (2010) (Under this Court's *Mobile–Sierra* doctrine, FERC must presume that a rate set by 'a freely negotiated wholesale-energy contract' meets the statutory 'just and reasonable' requirement…'The presumption may be overcome only if FERC concludes that the contract seriously harms the public interest'").

7 *See Re: Big Rivers Electric Corporation*, Case No. 9885, Order (Aug. 10, 1987) ("The case law cited in NSA's brief definitively states that regulatory commissions possess the authority to order changes or modifications to rates embodied in a utility's contract with a customer, if: '[T]he rate is so low as to adversely affect the public interest-as where it might impair the financial ability of the public utility to continue its service, cast upon other consumers an excessive burden, or be unduly discriminatory.' *Federal Power Commission v. Sierra Pacific Power Co.*, 350 U.S. 348, 355, 12 PUR3d 122, 126, 100 L.Ed. 388, 76 S.Ct. 368 (1955). In this case the Commission has determined that NSA's existing contract rate does impair Big Rivers' financial condition and that compelling reasons exist to implement flexible rates.").

8 Application (June 1, 2012) at 4.

> *"The minimum qualifications for contracting to take service under Tariff R.T.P. are (1) that there be an open position in the experimental queue of ten customers; (2) that the customer have a demand of not less than 1 MW; (3) that the customer specify at least 100 kW as being subject to the tariff; and (4) that the customer must be taking service under Tariff Q.P. or Tariff C.I.P.-T.O.D. at the time of the request. The ten customers met these minimum criteria."*

However, Kentucky Power now seeks to supplement those four minimum qualifications by inserting a new unwritten requirement that customers taking service under Tariff RTP must engage in some unspecified amount of load-shifting which is to be measured through some unspecified process. Kentucky Power's new requirements cannot be found within the plain language of existing Tariff RTP.

Kentucky Power relies heavily upon the following sentence within existing Tariff RTP in making its argument:

> *"The RTP Tariff will offer customer the opportunity to manage their electric costs by shifting load from higher cost to lower cost pricing periods or by adding new load during lower price periods."*

But nothing in this sentence expressly mandates that customers taking service under Tariff RTP must alter their regular production schedules by moving more production to off-peak hours. It only gives customers the *opportunity* to do so. Further, Kentucky Power conveniently ignores the next sentence of Tariff RTP, which provides for a wholesale real-time market-pricing option:

> *"The experimental pilot will also offer the customer the ability to experiment in the wholesale electricity market by designating a portion of the customer's load subject to standard tariff rates with the remainder of the load subject to real-time prices."*

This language clarifies that customers who satisfy the minimum conditions for service are provided the ability to experiment in the wholesale electric market with their load. Tariff RTP then established a very precise formula whereby the customer's designated real-time load will be charged PJM capacity and energy charges, plus transmission, distribution and administrative charges. Even though the actual electricity is provided by Kentucky Power and not some third party, this is a pure form of market-based pricing. While the RTP customers also have the *opportunity* to alter their regular production schedules in response to PJM energy and capacity prices, they are not required to do so. The plain language of Tariff RTP gives customers the discretion to determine whether or not to alter their regular production schedules in response to PJM market conditions. Moreover, if the RTP customers ultimately decide not to alter their regular production schedules in response to market conditions, then that is just one finding gained from implementing Tariff RTP as an experimental pilot program.

It is certainly true that Tariff RTP *could have* been written to require customers to alter their regular production schedules as a condition of taking service under the tariff. During the negotiation and review of the Settlement, either Kentucky Power or the Commission itself could have revised the language of Tariff RTP to expressly require customers to shift their energy usage to off-peak periods if that was the only intended purpose of Tariff RTP. But that is not how the plain language of existing Tariff RTP is actually written. Tariff RTP was specifically designed as a surrogate market pricing mechanism, not a mandatory load-shifting mechanism.

The Settlement should not now be altered. There are many components in the Settlement (i.e., \$63.66 million rate increase, 10.5% ROE on the environmental surcharge, 60/40 sharing of off-system sales profits) that *could have* been negotiated and written differently. But the parties must accept the Settlement and Tariff RTP as written. Customers are acting in accordance with the plain language of Tariff RTP. Therefore, Kentucky Power's request to immediately withdraw Tariff RTP in violation of the Settlement should be rejected.

2. The Fact That Existing Tariff RTP Does Not Require Customers To Engage In Load-Shifting Is Made Clearer By The Fundamental Differences Between Tariff RTP And Proposed Rider RTP.

The fact that Tariff RTP does not require customers to alter their regular production schedules in response to PJM market prices is made clearer when the design of existing Tariff RTP is compared to the design of proposed Rider RTP. Some key differences between the two real-time pricing mechanisms are presented in the following chart:

Tariff RTP	Rider RTP
Provides no information outlining a load-shifting baseline methodology or that instructs a customer regarding how much load to shift, which hours to shift such load, the consequences of not shifting load, or any other reference to load-shifting procedures.	Specifically defines the load-shifting baseline methodology.
No provisions for customer and Kentucky Power to jointly determine a customer baseline to measure load-shifting.	Specific language that governs the process used to develop a customer baseline jointly between the customer and Kentucky Power.
Specifically designed to reflect PJM market capacity and energy prices, as well as FERC-approved OATT Transmission rates, distribution rates and administrative charges. All load subject to Tariff RTP is priced at PJM equivalent market rates, not the existing regular tariff rates.	Specifically designed to maintain existing tariff rates, unless a customer shifts its load. The amount of the load-shift is priced at PJM energy rates, while all other charges are based upon existing regular tariff rates.

As demonstrated in the chart, there are stark differences between Tariff RTP and proposed Rider RTP. Tariff RTP was intended to function as a surrogate market pricing mechanism, which allows customers to decide whether and how to respond to PJM market pricing signals. Customers taking service under the Tariff must pay PJM energy, capacity, and transmission rates at all times for their designated RTP load and therefore have discretion to determine if and when those PJM rates are so high as to make continued production during on-peak hours uneconomic. Conversely, proposed Rider RTP only subjects customers to PJM energy pricing if customers alter their energy usage patterns or "load-shift." Otherwise, those customers pay standard tariff rates. Thus, while proposed Rider RTP is specifically designed to provide market-pricing only to shifted load, existing Tariff RTP provides market-pricing at all times to the designated RTP load.

Kentucky Power's Responses to the Attorney General in Case No. 2007-00166, in which Tariff RTP was established reinforce that, in implementing its real-time pricing program under Tariff RTP, Kentucky Power designed the program to be the equivalent of the customer purchasing market power directly:

"Q: Please provide a detail explanation of exactly what costs the company will incur by utilizing the PJM RTO rates rather than its own costs of generation?

A: AEP/Kentucky Power treats the portion of the load designated by the customer as subject to real-time pricing as if the customer is purchasing its requirements directly from the market. AEP will separately identify the real-time load and will be purchasing from the market the requirements for that load. The costs AEP incurs to do that will be passed on to the customer. Those costs are detailed in the RTP tariff and include demand, energy, ancillary and transmission charges...[9]

***

Q: As participants are to be charged for a portion of a load they designate at their current tariff rate plus any portion of additional load they designate as subject to real-time pricing, does the possibility exist for over or under recovery from individual participants? If so, how does the company propose to allocate such over or under recovered funds?

A: No, the Company believes that individual participants will pay for the costs they cause the Company to incur. The current tariff rates are cost based and the price paid for usage under real-time pricing reflects the costs customer would incur if they purchased the electricity in the competitive market."[10]

In his first testimony filed in this case, Company witness Ranie K. Wohnhas candidly acknowledged that Tariff RTP provides customers a choice to pay market-based rates:

"The current tariff effectively allows customers to choose between the lower of cost-based rates and market-based rates, which was neither the Company's, nor the Commission's intention when the experimental tariff was approved."[11]

The notion that Tariff RTP was only designed for customers that can change their regular production schedules in response to on-peak PJM market prices is a new theory presented by Kentucky Power as the case developed as an after-the-fact justification for changing the existing program.[12] This new theory should be rejected.

There are distinct differences in the language of existing Tariff RTP versus proposed Rider RTP. Proposed Rider RTP outlines a method for determining the baseline used to measure whether customers are actually shifting their energy usage to off-peak hours in response to PJM market prices. Conversely, nowhere in

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[9] Baron Testimony, Ex. SJB-3 at 1, Kentucky Power Company's Responses to Attorney General's Second Set of Data Requests (June 28, 2007), Item No. 6(b).
[10] Baron Testimony, Ex. SJB-3 at 4, Kentucky Power Company's Responses to Attorney General's First Set of Data Requests (June 5, 2007), Item No. 6(E).
[11] KIUC Ex. 2, Direct Testimony of Ranie K. Wohnhas (June 1, 2012) at 6:18-21.
[12] Contrary to Kentucky Power's assertions, it is very likely that some KIUC members would in fact respond to PJM marginal energy cost price signals and reduce usage during high-priced hours. This would certainly be the case for AK Steel.

the language of existing Tariff RTP is it explained how Kentucky Power would measure a customer's load-shifting and/or how the Company would determine whether a customer's reduction in load was actually in response to market conditions. The language of existing Tariff RTP provides no baseline against which usage data can be compared to determine whether customers are actually load-shifting. Under its theory, Kentucky Power would enjoy seemingly unconstrained discretion to determine whether customers have altered their energy usage in response to PJM market conditions.

The language of existing Tariff RTP also does not set forth what level of load-shifting would be required, if customers were in fact required to alter their on-peak energy usage in response to PJM market conditions. Under its interpretation of existing Tariff RTP, Kentucky Power would presumably be permitted to use its own subjective judgment to decide whether customers were satisfying the unwritten load-shifting "requirements" of Tariff RTP. Though Kentucky Power speculated regarding what amount of customer load-shifting would be satisfactory at the hearing,[13] the Company could point to no express language in Tariff RTP that explicitly sets forth what amount of load-shifting would be required. Conversely, proposed Rider RTP sets forth what shifts in energy usage would be considered load-shifting.

Records from the case where the Commission initially established Tariff RTP further clarify that there are intentional differences between Tariff RTP and a real-time pricing mechanism like proposed Rider RTP. Proposed Rider RTP uses the Customer Baseline Load ("CBL") approach that other Kentucky utilities have adopted. However, existing Tariff RTP was specifically designed to serve as an alternative to the CBL approach. The Commission's February 1, 2008 Order in Case No. 2007-00166 recounts how Kentucky Power expressly defended its decision not to use a CBL approach:

> *"Kentucky Power responds to the AG's concern regarding its decision not to use a CBL approach by acknowledging that the Commission did not direct the companies to implement a particular type of program. Kentucky Power argues that by allowing* ***flexibility in designing programs, the Commission freed the companies to use their company-specific experience to develop programs that provide their customers with appropriate price signals while avoiding the allocation of additional costs to other customers. In addition, Kentucky Power argues the deployment of both CBL programs and Kentucky Power's model will provide the Commission with additional information it would otherwise lack.****"*[14]

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[13] Tr. at 12:35:39-12:37:50 and 14:22:50-14:24:27.

[14] Order, Case No. 2007-00166 (Feb. 1, 2008) at 11 (emphasis added).

Thus, Kentucky Power acknowledged the value of implementing an intentionally distinct real-time pricing mechanism that used a non-CBL approach. The Commission also explicitly recognized the value of Kentucky Power's decision not to adopt a CBL approach, noting that "*Kentucky Power's model will provide information that may not be available if Kentucky Power was required to utilize a CBL.*"[15]

These records indicate that Tariff RTP was specifically designed to represent an alternative approach to the CBL approach – a surrogate market pricing approach. Adopting a different real-time pricing mechanism through Tariff RTP allowed the Commission to garner information about how effective different real-time pricing mechanisms may be, given that this was adopted as an experimental pilot program.

In this case, KIUC witness Baron also explained the value of establishing a real-time pricing mechanism without a load-shifting requirement, like Tariff RTP, stating:

> *"The purpose of a real-time pricing tariff is to provide market-based price signals to customers, who can then perform internal economic evaluations for the purpose of optimizing their use of electricity, given their production processes, market demand and prices for their products, with consideration of the overall economic impact of all of their production costs, including electricity. By instituting Tariff RTP, the Commission is providing customers the opportunity to bear the true market costs of their production decisions. Customers then have the choice to make economic decisions based on these market-based electric prices."*[16]

In addition, there can be economic development benefits as a result of establishing a real-time pricing mechanism like Tariff RTP, which provides large businesses a chance to experiment in the electric market, if such a decision is economic.

Now, when customers are actually taking service under Tariff RTP, Kentucky Power asks the Commission to immediately withdraw Tariff RTP and to establish a fundamentally different real-time mechanism using a CBL approach. But customers have adhered to the plain language of Tariff RTP, which both Kentucky Power and the Commission approved of in Case No. 2007-00166 and again in the Settlement. The non-CBL approach adopted by the Commission in Tariff RTP does not require customers to alter their on-peak energy usage in response to PJM market prices, and there is value in existing Tariff RTP's distinct market-based approach, which the Commission recognized. Accordingly, there is no justification for altering the Settlement.

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[15] Order, Case No. 2007-00166 (Feb. 1, 2008) at 12.
[16] Direct Testimony of Stephen J. Baron (Aug. 27, 2012) ("Baron Testimony") at 11:18-12:5.

Instead, the Commission should uphold its decisions approving Tariff RTP's approach to real-time pricing and should allow the tariff to continue through its stipulated expiration in June 2013.

3. KIUC Members Have Not Violated the Terms of the Settlement.

Kentucky Power suggests that it should be allowed to violate the Settlement since it believes that the KIUC members currently taking service under Tariff RTP are also violating the terms of the Settlement by deciding not to alter their production schedules in order to shift their load.[17] The Commission should reject Kentucky Power's suggestion, which is incorrect and unfounded. Nowhere does the Settlement require customers to alter their on-peak energy usage in order to take service under existing Tariff RTP. The Settlement only addresses the three-year extension of that tariff. And as discussed above, the plain language of Tariff RTP does not require customers to alter their regular production schedules to move more production to off-peak hours.

Notably, Kentucky Power did not advise KIUC members who asked to take service under Tariff RTP that the ability to alter their regular production schedules to shift more load to off-peak hours was required under the tariff. For example, Kentucky Power engaged in multiple discussions over many years with Catlettsburg Refining LLC, a subsidiary of Marathon Petroleum LP ("Marathon") regarding Tariff RTP. During Marathon's discussions with the Company, Marathon openly informed Kentucky Power that because of its around-the-clock operations it could not engage in load-shifting.[18] Kentucky Power never indicated to Marathon that such behavior was a required condition to take service under Tariff RTP, but instead moved Marathon's load onto Tariff RTP effective July 1, 2012.

Thus, Kentucky Power registered Marathon, a customer it knew could not alter its regular production schedules in response to on-peak PJM market prices, to take service under Tariff RTP. This undermines the Company's current claim that it allowed customers to take service under Tariff RTP and then planned to monitor their behavior to see if they engaged in load-shifting, and potentially backbill those customers. Kentucky Power knew for a fact that, because of its 24/7 operations, Marathon could not engage in load-shifting when it registered

[17] Tr. at 10:29:21-10:31:04.
[18] Rebuttal Testimony of Ranie K. Wohnhas at 5:19-21.

Marathon to take service under Tariff RTP. If load-shifting was a required condition under the tariff, which it is not, Kentucky Power would not have registered Marathon to take service under Tariff RTP.

Kentucky Power has failed to provide a valid argument that customers currently taking service under Tariff RTP have violated the terms of the Settlement. Accordingly, the Commission should reject the Company's request to immediately withdraw Tariff RTP.

4. Allowing Kentucky Power to Insert Additional Unwritten Requirements into the Plain Language of Tariff RTP Based Upon Its "Intent" in Implementing the Tariff is Contrary to Law and Would Constitute Bad Public Policy.

Allowing Kentucky Power to insert new unwritten requirements into Tariff RTP based upon its "intent" in implementing the tariff is contrary to law and would be a bad policy decision. The Commission regulates a large number of utilities and approves volumes of tariffs. Customers should be able to read the plain language of the tariff that applies to them and understand their rights and responsibilities. Customers should not be required in every scenario to determine the utility's "intent" in developing the tariff. Such a policy is unworkable. In addition, it undermines the rationale for requiring utilities to make their tariffs open for public inspection, which is required under KRS 278.160.

KIUC members justifiably relied upon the continuation of existing Tariff RTP, the integrity of the Commission's settlement process, and Kentucky Power's own assertions to those customers in determining whether to take service under Tariff RTP. Prior to taking service under Tariff RTP, those customers engaged in serious consideration and review of the tariff over the years, relying not only upon the plain language of the Settlement and the Order approving that Settlement, but also upon Kentucky Power's own assertions to those customers.

For example, Marathon reinstated discussions with Kentucky Power about moving its load to Tariff RTP early this year.[19] Marathon informed Kentucky Power that it could not engage in load-shifting, due to the nature of its high-load factor operations.[20] Kentucky Power never indicated to Marathon that such behavior was a required condition to take service under Tariff RTP. And as recently as May 16, 2012, Marathon was assured that

[19] Baron Testimony, Ex. SJB-2 at 15 of 63.
[20] Rebuttal Testimony of Ranie K. Wohnhas at 5:19-21.

no changes in Tariff RTP rate structure were anticipated and that delaying execution of Marathon's Addendum to take service under the tariff would not be an issue. Kentucky Power asserted:

> *"[A]s noted, Kentucky Power expects to be filing the new RTP rate in a couple of weeks.* ***We do not anticipate any changes in the methodology of determining the rate structure.*** *We will share the rate information with you at that time. Since we have language in the current Addendum that is acceptable to both parties, I recommend that we revisit the execution of the Addendum in its current form at that time".*[21]

Despite this May 16, 2012 assurance that the Addendum was fine and no changes in the Tariff RTP methodology were anticipated, it was only two weeks later that Kentucky Power blindsided Marathon by filings its application to immediately withdraw existing Tariff RTP.

Kentucky Power's customers should be able to justifiably rely upon the integrity of the Commission's settlement process as well as Kentucky Power's own assertions to those customers. The agreement to extend *existing* Tariff RTP for three years was part of the delicate balance achieved by the parties in reaching the Commission-approved Settlement. KIUC specifically bargained for and relied upon the three-year extension of *existing* Tariff RTP, not the fundamentally different proposed Rider RTP. Concessions were made to Kentucky Power in exchange for the right to have *existing* Tariff RTP extended for three years. The Commission should not facilitate Kentucky Power's attempt to harm customers by altering the Settlement before customers receive the full benefit of their bargain.

This is an important matter of policy and precedent. If other utilities believe that settlement commitments made by them and approved by the Commission can later be changed to the detriment of one of the signatory parties, then the settlement process is compromised and rendered less effective. If settlement agreements are allowed to be changed after the fact, then parties are less likely to resolve matters through negotiation.

Kentucky Power merely appears to be asking the Commission to bail it out of a deal that could result in a one-year revenue loss to AEP's shareholders. Though Kentucky Power claims that customers will receive a "windfall" under Tariff RTP, only capacity savings are certain for customers. There are no guarantees about market energy pricing. It is possible that high market energy prices could make the RTP rate uneconomic, but all

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[21] Baron Testimony, Ex. SJB-2 at 21 of 63 (emphasis added).

five KIUC member companies were willing to take that risk in taking service under Tariff RTP. It is an option they bargained for as part of the Settlement, and it is wrong for Kentucky Power to try to deny them that right.

B. The Risk Of Future Revenue Losses Was Accepted By Kentucky Power In Signing The Settlement.

1. Kentucky Power Was Fully Aware of the Risk of Revenue Losses When the Company Signed the Settlement in 2010.

Since its inception, Kentucky Power has been fully aware of the risk of revenue losses as a result of establishing Tariff RTP. Kentucky Power openly acknowledged that Tariff RTP could result in revenue losses when it established the tariff in Case No. 2007-00166, as the Company's response to one of the Attorney General's data requests in that case recounts:

> *"Q: Does the company believe that allowing participants to choose the amount of load they are willing to have subject to real-time pricing will result in revenue erosion? If not, why?*
>
> *A: It is anticipated that customers that participate in any program would do so only if they benefit from participation in that program, thereby providing less revenues to the Company..."*[22]

Because Kentucky Power was aware of the possibility of revenue losses as a result of implementing Tariff RTP, it was also fully aware of that possibility when it signed the Settlement extending existing Tariff RTP for three years in 2010.

Kentucky Power's current revenue loss estimate is based, in part, upon the difference between the Company's retail demand charge for capacity and the PJM RPM price for capacity. But the PJM RPM capacity price for the 2012/2013 planning year ($16.46/MW-day or $0.501/kW month) was determined by a capacity auction held in May of 2009. As Kentucky Power itself admits, the Company knew to the penny the PJM RPM capacity price for the 2012/2013 PJM Planning Year a full year before it signed the Settlement.[23] The current drop in capacity prices therefore does not provide a valid reason to justify modifying the Commission-approved Settlement.

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[22] Baron Testimony, Ex. SJB-3 at 6, Responses to AG 1st Set, Response to Item No. 1(B).
[23] Kentucky Power Response to KIUC Motion to Dismiss at 9-10.

Kentucky Power's estimated revenue loss is also based upon its projections of low energy market prices through June 2013.[24] But the risk that PJM marginal energy prices might be depressed in the 2012/2013 time frame was known or should have been known to Kentucky Power when it signed the Settlement. It is unpersuasive for AEP—a company that regularly trades in the wholesale power market—to assert that it did not realize that over a three-year period energy prices could fall.

2. Kentucky Power is Currently Financially Healthy, Even After Months of Customers Taking Service Under Tariff RTP With After-Tax Returns in the 10% - 11% Range.

Kentucky Power has provided no proof of serious financial harm to the Company, but instead only speculation as to the potential for such harm. But mere speculation as to future harm is insufficient to satisfy the *Mobile-Sierra* public interest standard authorizing the Commission's alteration of previously approved settlement agreements.

Currently, Kentucky Power is financially healthy. According to the data in Kentucky Power's August 2012 Financial Report filed Oct 2, 2012 at the Commission, the Company earned an after-tax return on common equity of 10.59% for the twelve months ending August 31, 2012.[25] That report included two months when customers were taking service under Tariff RTP (customers began taking service under the tariff July 1, 2012). The data in the Company's Third Quarter Report for 2012 indicates that Kentucky Power earned an after-tax return on common equity of 11.18% for the nine months ending September 30, 2012.[26] This data included three months when customers were taking service under Tariff RTP. Given that the average return-on-equity authorized by state commissions for electric utilities in the first nine months of 2012 was 10.22%,[27] Kentucky Power is financially healthy, even after months of customers taking service under Tariff RTP. If anything, Kentucky Power's return-on-equity is excessive.

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[24] Kentucky Power Application at ¶7.
[25] KIUC Ex. 8.
[26] KIUC Ex. 9.
[27] KIUC Ex. 10.

Mr. Wohnhas forecasted that over twelve months Kentucky Power's return-on-equity would drop by 2.3%, from 8.9% to 6.6%, if existing Tariff RTP remains in effect.[28] As the discussion above indicates, Kentucky Power's actual returns on equity including three months of Tariff RTP have been significantly higher than the 8.9% figure cited by Mr. Wohnhas. If Kentucky Power's September 30, 2012 return-on-equity of 11.18% dropped by 2.3%, Kentucky Power would still earn a return-on-equity of 8.8% assuming all of Mr. Wohnhas' predictions turn out to be true and were compressed into nine months. Even if this forecast is accurate, an 8.8% ROE for one year does not adversely affect the public interest and cannot serve as the basis for revising a previously approved Settlement.[29] Therefore, changing the Unanimous Settlement would not protect Kentucky Power from substantial financial losses, but instead would merely preserve excessive profit for AEP's shareholders.

The Company's projected revenue losses are not guaranteed to occur. PJM marginal energy prices change hourly and could easily increase over the next year, resulting in greater than expected revenue to Kentucky Power. In fact, in July of this year, Kentucky Power received greater revenues from the customers taking service under Tariff RTP than it otherwise would have due to increased energy prices.[30] Company witness Wohnhas testified that "*actual results show that the July revenue from the 10 customers on Tariff RTP was approximately $107,000 higher than it would have been had these customers been on their respective standard tariffs….*"[31] Hence, the level of any harm or benefit to the Company as a result of Tariff RTP is still uncertain.

In fact, one of the biggest risks that a customer taking service under Tariff RTP takes is that PJM energy prices will change over the next year, thereby making its decision to take service under that tariff uneconomic. PJM marginal energy costs, especially during on-peak hours, routinely are many times greater than Kentucky Power's average coal-based energy charges.[32] By agreeing to take service under Tariff RTP for the twelve-month period required under the tariff, customers have agreed to accept that risk. Should energy prices increase, those customers will have to determine whether and how they would respond to such prices. However, the risk

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[28] Direct Testimony of Ranie K. Wohnhas (June 1, 2012) at 10:3-5 ("A reduction of $17.4 million (3.2%) of retail sales revenue would reduce KPCO's ROE by approximately 2.3% from its April, 2012 level of 8.9%").
[29] Baron Testimony at 17:21-22 (finding that a 6.6% ROE for one year is not serious enough to condone revising a previously approved Settlement).
[30] Tr. at 10:57:35-10:58:05.
[31] Wohnhas Rebuttal Testimony at 10:15-19.
[32] Baron Testimony at 19:6-7.

associated with the volatility of PJM real-time energy prices is not a valid reason to renege on a Commission-approved Settlement since that risk was known at the time the agreement was signed.

Whatever revenue loss or gain may in fact occur during the final year of Tariff RTP will be one-time and non-recurring, assuming that Tariff RTP expires on June 30, 2013 in accordance with the Settlement. Therefore, that loss or gain will not be recoverable in a base rate case or otherwise.[33] Accordingly, while Kentucky Power's shareholders may incur a loss or gain if the Commission upholds the Settlement, customers will not.

3. If Customers Alter Their Regular Production Schedules, as Kentucky Power Suggests They Are Required to Do, Kentucky Power May Experience Greater Revenue Losses.

Kentucky Power expresses concerns about customers not engaging in load-shifting and about the potential for revenue losses resulting from the continuation of Tariff RTP. But if customers actually did engage in load-shifting, as Kentucky Power claims they must, the Company would experience greater revenue losses.

Kentucky Power witness Wohnhas confirmed that, if Tariff RTP customers had in fact engaged in load-shifting in July of 2012, those customers would have paid low-priced off-peak energy prices rather than the high-priced on-peak energy prices. Consequently, Kentucky would have received less revenue from those customers.[34] Thus, if customers engaged in load-shifting, as Kentucky Power suggests, then the Company would have experienced greater revenue losses in July.

Kentucky Power counters that point by arguing that the energy freed up by customer load-shifting could be sold off-system to offset some of that greater revenue loss. But if Kentucky Power sold the freed-up energy off-system, as it suggests, the revenues from those energy sales would be split according to Member Load Ratio among AEP affiliates from various states, under the terms of the AEP Power Pool agreement.[35] Kentucky Power would only get to keep about 7% of the increased margins from those off-system sales as 7% is its MLR. Therefore, Kentucky Power was actually benefitted by Tariff RTP customers who did not load-shift in July 2012

[33] Baron Testimony at 24:3-6.
[34] Tr. 11:18:56-11:19:33.
[35] Tr. 11:20:30-11:22:19.

because Kentucky Power got to keep the all of the greater revenues from its high-priced on-peak energy sales to those customers.

III. Under No Circumstances Should the Commission Backbill Tariff RTP Customers Because Doing So Would Violate the Filed Rate Doctrine and Would Constitute Retroactive Ratemaking.

Kentucky Power's data responses to Staff in this proceeding raised the possibility of backbilling the customers currently taking service under Tariff RTP.[36] The Commission should reject this suggestion as retroactive ratemaking and a violation of the filed rate doctrine.

The Commission's statutory ratemaking authority "*is derived from an integrated, comprehensive system aimed at providing stability and notice to all entities involved in the rate process.*"[37] Consistent with this system, KRS 278.160 forbids a utility from charging any rate other than the rate in effect at the time that service was rendered. KRS 278.160(2) provides as follows:

> *"No utility shall charge, demand, collect, or receive from any person a greater or less compensation for any service rendered or to be rendered than that prescribed in its filed schedules, and no person shall receive any service from any utility for a compensation greater or less than that prescribed in such schedules."*

KRS 278.390 provides that rates set by the Commission are the "filed rate" until revoked or modified by Commission order:

> *"Every order entered by the commission shall continue in force until the expiration of the time, if any, named by the commission in the order, or until revoked or modified by the commission, unless the order is suspended, or vacated in whole or in part, by order of decree of a court of competent jurisdiction."*

Finally, KRS 278.270 empowers the Commission to set "just and reasonable" rates on a prospective basis only. 278.270 states:

> *"Whenever the commission, upon its own motion or upon complaint as provided in KRS 278.260, and after a hearing had upon reasonable notice, finds that any rate is unjust, unreasonable, insufficient, unjustly discriminatory or otherwise in violation of any of the provisions of this*

[36] Kentucky Power Response to Staff's Second Request for Information, Item No. 6.
[37] *Cincinnati Bell Telephone Co. v. Kentucky Public Service Com'n*, Court of Appeals of Kentucky, 223 S.W.3d 829, 837-838 (February 2, 2007).

chapter, the commission shall by order prescribe a just and reasonable rate ***to be followed in the future.***"[38]

Conspicuously absent from this statute is any phrase enabling the Commission to set rates retroactively. The Commission explained that:

> *"The rule against retroactive ratemaking is a 'generally accepted principle of public utility law which recognizes the prospective nature of utility ratemaking and prohibits regulatory commissions from rolling back rates which have already been approved and become final.' . . . It further prohibits regulatory commissions when setting utility rates, from adjusting for past losses or gains to either the utility consumers, or particular classes of consumers."*[39]

The Commission concluded that if it later finds that its rates are not just and reasonable it can adjust those rates prospectively, but not retrospectively. The Commission stated that "*it is specifically authorized by KRS 278.270 to make prospective adjustments to rates if it finds that the rates are unjust, unreasonable, insufficient, unjustly discriminatory or otherwise in violation of any provisions of KRS Chapter 278.*"[40] In addition, an agency may not impose a charge over and above the rates on file at the time of the delivered service for regulated services already rendered because such a charge would violate the filed rate doctrine.[41]

The Tariff RTP rates paid by customers since July 1, 2012, which the Commission authorized in approving the Settlement, remain in full force and effect until the Commission modifies them by order. As recently as June 28, 2012, the Commission itself expressly stated that "*Kentucky Power's existing Tariff RTP has not been suspended and it remains in full force and effect.*"[42] The Commission also explicitly denied Kentucky Power's request that Tariff RTP be suspended after July 1, 2012 during the pendency of this proceeding.[43] The Tariff RTP rates paid by customers during the pendency of this proceeding constituted lawful filed rates. Consequently, Tariff RTP customers cannot be backbilled by Kentucky Power for their service since July 1, 2012 without violating the prohibition against retroactive ratemaking and without violating the filed rate doctrine.

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[38] Emphasis added.
[39] *Office of the Atty. Gen. v. Atmos Energy Corp.*, Case No. 2005-00057, Order (February 9, 2007) at 1.
[40] Id. at 1 (emphasis added).
[41] *See Associated Gas Distributors v. F.E.R.C.*, 893 F.2d 349, 354-56 (D.C.Cir. 1989).
[42] Order, Case No. 2012-00226 (June 28, 2012) at 3.
[43] Id at 4.

IV. Customers Did Not Violate The Notice Requirements Of Tariffs Q.P or C.I.P-T.O.D. In Transferring From Those Tariffs To Tariff RTP.

At the hearing, Staff raised the issue of whether Kentucky Power and/or the customers currently taking service under Tariff RTP adhered to the twelve-month notice requirements set forth under Tariff Q.P. and Tariff C.I.P.-T.O.D.[44] As Kentucky Power clarified, the notice requirements were not violated because customers did not terminate their service contracts with the Company. The twelve-month notice applies to termination of service, not merely switching rate schedules. Any customer may change rate schedules at any time.[45]

The "Rate Schedule Selection" portion of the Terms & Conditions of Service in Kentucky Power's tariff specifically provides:

> *"Customer may change their initial rate schedule selection to another applicable rate schedule* ***at any time*** *by either written notice to Company and/or by executing a new contract for the rate schedule selected, provided that the application of such subsequent selection shall continue for 12 months before any other selection may be made. In no case will the Company refund any monetary difference between the rate schedule under which service was billed in prior periods and the newly selected rate schedule."*[46]

Hence, there was no requirement that current Tariff RTP customers were required to give twelve-month notice prior to switching to Tariff RTP. Those customers could switch rate schedules at any time. It was therefore, appropriate for those customers to begin taking service under Tariff RTP effective July 1, 2012.

V. If The Commission Wishes To Implement A Different Real-Time Pricing Mechanism To Encourage Load-Shifting, The Commission Should Do So While Still Allowing Tariff RTP To Continue Until Its Current Expiration Date Of June 30, 2012, In Accordance With The Settlement.

At the hearing, Commissioner Breathitt appeared concerned that Tariff RTP may not satisfy policy objectives such as demand-side management or energy efficiency. If the Commission is interested in adopting a mechanism that is specifically intended to encourage large manufactures to change their production processes to shift load to off-peak periods, the Commission could establish proposed Rider RTP, or a similar mechanism, immediately and allow it to exist simultaneously with Tariff RTP. Alternatively, the Commission could establish Rider RTP, or a similar mechanism, on July 1, 2013, after Tariff RTP expires. Such an action would not be in direct contravention to the Settlement, provided that Tariff RTP is allowed to continue until its stipulated

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[44] Tr. at 11:30:42-11:32:15.

[45] Tr. at 11:59:00-12:00:39.

[46] Tr. at 12:23:46 (reading Kentucky Power Tariff, Original Sheet 2-7 (emphasis added)).

expiration date on June 30, 2013. Accordingly, irrespective of the Commission's ultimate decision regarding proposed Rider RTP, the Commission should reject Kentucky Power's request to withdraw Tariff RTP prior to its expiration on June 30, 2013.

CONCLUSION

Kentucky Power's request to immediately withdraw existing Tariff RTP should be rejected as a violation of the Commission-approved Settlement and the Commission's Order approving that Settlement. Kentucky Power failed to satisfy the *Mobile-Sierra* standard and/or the requirements of KRS Chapter 278 that would justify modifying either the Settlement or the Commission's Order. In particular, the Company has not proven that the continuation of existing Tariff RTP through its agreed upon term would result in unjust or unreasonable rates or would seriously harm the public interest. Accordingly, the Commission should not allow Kentucky Power to withdraw existing Tariff RTP.

Respectfully submitted,

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