Goss ▪ Samford PLLC
Attorneys at Law

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PUBLIC SERVICE COMMISSION

January 4, 2013

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

Dear Mr. Derouen:

Please find enclosed for filing with the Commission, an original and ten copies of East Kentucky Power Cooperative, Inc.'s Petition for Declaratory Order.

Should you have questions or need additional information, please contact me.

Very truly yours,

David S. Samford
Counsel

Enclosures

2365 Harrodsburg Road, Suite B-130 | Lexington, Kentucky 40504

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JAN 04 2013

PUBLIC SERVICE COMMISSION

COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter Of:

Petition of East Kentucky Power Cooperative, Inc. for a Declaration of Its Authorization to Sell the Smith Unit 1 Assets Without a Transfer of Control Filing Under KRS 278.218	**Case No. 2012-**

Petition for Declaratory Order

East Kentucky Power Cooperative, Inc.("EKPC") respectfully petitions the Kentucky Public Service Commission ("Commission") for an Order declaring that EKPC is authorized to sell its Smith Unit 1 Assets without a Transfer of Control filing under KRS 278.218. In support of this Petition, EKPC respectfully states as follows:

Establishment of a Regulatory Asset for the Smith Unit 1 Assets—Case No. 2010-00449

On February 28, 2011, the Commission entered an Order authorizing EKPC to establish a regulatory asset in the amount of $157,388,715, which includes both the amounts expended on Smith 1 and EKPC's estimate of the costs to unwind its Smith 1 vendor contracts. The Commission also Ordered EKPC to file quarterly reports with the Commission summarizing the status of its mitigation efforts to reduce the balance of the regulatory asset through the sale of the Smith 1 physical assets, with the first report to be filed by July 1, 2011. Page 5 of the Order states:

> EKPC states that it will seek to mitigate the amount of the regulatory asset by determining if components of the Smith 1 facility can be: (1) sold to another electric generator, either domestically or internationally; (2) used in its other circulating fluidized bed coal-fired units; (3) sold as scrap metal; or (4) some combination thereof. While it estimates that this process could take as long as 18 months, EKPC states that, to the fullest extent reasonably and practically possible, it will seek to mitigate the

balance of the regulatory asset balance prior to seeking recovery of the cost of the asset.

Requirements of KRS 278.218

KRS 278.218 states:

> (1) No person shall acquire or transfer ownership of or control, or the right to control, any assets that are owned by a utility as defined under KRS 278.010(3)(1) without prior approval of the commission, if the assets have an original book value of one million dollars ($1,000,000) or more and:
>
> (a) The assets are to be transferred by the utility for reasons other than obsolescence; or
>
> (b) The assets will continue to be used to provide the same or similar service to the utility or its customers.
>
> (2) The commission shall grant its approval if the transaction is for a proper purpose and is consistent with the public interest.

EKPC's Mitigation Efforts

As required by the Commission's Order dated February 28, 2011, EKPC has filed seven quarterly mitigation reports. As reported in its December 2011 mitigation report, EKPC negotiated final settlement of all Smith Unit 1 contracts. The regulatory asset balance relating to Smith Unit 1 has been reduced to $150,925,119 as of December 28, 2012. This balance includes expenses associated with marketing the assets and preserving the assets for potential sale. EKPC continues to work through equipment brokers to market the Smith assets and to identify and screen potential purchasers. As reported in its December 28, 2012, mitigation report, three hundred twenty-four (324) inquiries regarding the assets have been received. EKPC is currently engaged in due diligence activities with one US prospect and seven international prospects. In the event that one or more of these prospective buyers makes a substantive offer, EKPC needs to have the ability to respond quickly in order to finalize and complete the transaction.

Summary of Interpretation

The Commission's Order dated February 28, 2011, albeit silent with respect to the need for approval of the sale, recognizes EKPC's mitigation efforts and its plans to reduce the balance in the regulatory asset prior to filing an application for rate recovery. The regulatory asset was established as a result of the cancellation of its Smith Unit 1 generating unit. Page 6 of the Order states:

> In addition, based on the significance of the decline in load growth reflected in EKPC's 2010 load forecast, the increased capital costs of Smith 1, and the impact of cancellation on EKPC's financial condition, the cost of cancellation must be considered an extraordinary nonrecurring cost which could not have reasonably been anticipated or included in EKPC's planning. Having accepted the Settlement reached in Case No. 2010-00238, which reflects EKPC's decision to cancel Smith 1, and based upon our review of EKPC's present value analysis of the costs of continuing with the construction of Smith 1, as well as the costs of pursuing other power supply alternatives, we find that it is less costly to cancel Smith 1 and recover the amount invested therein than it would be to complete construction of the unit.

Further, the page 6 of the Order in Case No. 2010-00238 states:

> The primary factor behind the decrease in projected load growth was due to the severe economic recession which began in late 2007 and which has caused EKPC's peak load to decrease by more than 10 percent since 2008. The full extent of the recession is reflected in the 2010 load forecast, including the high unemployment level of EKPC's territory, which is not expected to return to pre-recession levels for nearly 10 years, reduction in personal income level, and a severe decline in the automotive industry.

A transfer of control filing is not required under KRS 278.218 (1)(a) if the transfer is a result of obsolescence. The American Society of Appraisers defines the term "economic obsolescence" as the "loss in value or usefulness of a property caused by factors external to the property, such as increased cost of raw materials, labor or utilities (without an offsetting increase in product price); reduced demand for the product; increased competition; environmental regulations; inflation or high interest rates; or similar factors."[1] The two quoted passages from the above-mentioned Orders clearly show that the Commission recognizes EKPC's need to liquidate the Smith Unit 1 assets for economic obsolescence. In addition, through its mitigation reports, EKPC has kept the Commission fully informed of these efforts to liquidate these assets. The need for EKPC to be able to act quickly to consummate any sale is critical in maximizing any mitigation effort.

Wherefore, EKPC respectfully requests that the Commission enter an Order declaring that EKPC is authorized to sell its Smith Unit 1 Assets without a Transfer of Control filing under KRS 278.218.

Respectfully submitted,

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Counsel for East Kentucky Power Cooperative, Inc.

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[1] Sourced from "Property Tax Audits: Applying Asset Obsolescence in a Good Way." Journal of State Taxation, May-June 2006, page 44.