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Via Overnight Mail

February 21, 2014

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

Re: Case No. 2013-00413

Dear Mr. Derouen:

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

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

Very Truly Yours,

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MLKkew
Attachment
cc: Certificate of Service
Quang Nyugen, Esq.
Richard Raff, Esq.

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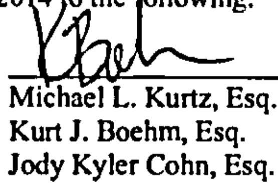
CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing was served by electronic mail (when available) and by regular, U.S. mail, unless other noted, this 21st day of February, 2014 to the following:



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COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In The Matter of: The Joint Application of Kenergy Corp. and Big Rivers Electric Corporation for Approval of Contracts and for a Declaratory Order	: : :	Case No. 2013-00413

PETITION FOR REHEARING OF
KENTUCKY INDUSTRIAL UTILITY CUSTOMERS, INC.,

Pursuant to KRS § 278.400, Kentucky Industrial Utility Customers, Inc., ("KIUC") petitions the Kentucky Public Service Commission for rehearing of its January 30, 2014 Order in Case No. 2013-00413. KIUC seeks rehearing because:

1) The Commission's conclusion that the Century Sebree Transaction Agreements "*were a product of extensive and good faith negotiations among Big Rivers, Kenergy, and* [Century]" that achieved a "*delicate balance*" that would be jeopardized by the imposition of KIUC's proposed stranded cost charge is not supported by the evidence in this proceeding. There is insufficient evidence in the record to support the conclusion that the Century Sebree smelter ("Sebree smelter") is not profitable and would likely terminate the Transaction Agreements if required to make a contribution toward stranded costs it caused.

2) The Commission failed to address whether the profitability of the Sebree smelter is a relevant issue when determining fair, just, and reasonable rates for both the Sebree smelter and Big Rivers Electric Corporation's ("Big Rivers" or "Company") remaining customers. The evidence demonstrates that the Sebree smelter is financially capable of making a contribution toward stranded costs and that it would be unreasonable and discriminatory for Big Rivers' remaining non-smelter customers to pay the costs of the excess capacity resulting from the Sebree Smelters' market-based rate without any contribution from the Sebree smelter.

3) The Commission's Order approving the Sebree Transaction Agreements without requiring evidence that the Sebree smelter was financially unable to contribute to the costs of the excess capacity resulting from

its market-based pricing is arbitrary, unreasonable, and may violate KRS § 278.170(1) and KRS § 278.030(1) depending upon the Commission's ultimate decision in Case No. 2013-00199.

4) The Commission's Order fails to achieve a balance of interests between Big Rivers, its creditors, and its customers consistent with the Commission's Order in Case No. 2012-00535. This problem could be cured if the pending rate case (Case No. 2013-00199) results in the *"right-sizing"* of Big Rivers to serve the non-smelter load such that consumers are not required to pay for excess capacity that is not *"used and useful."* However, the result of the rate case is not yet known and it is therefore premature to conclude that the Sebree smelter should have no obligation to contribute to the stranded costs it caused.

ARGUMENT

ASSIGNMENT OF ERROR #1: The Commission's conclusion that the Century Sebree Transaction Agreements "*were a product of extensive and good faith negotiations among Big Rivers, Kenergy, and* [Century]" that achieved a "*delicate balance*" that would be jeopardized by the imposition of a stranded cost charge is not supported by the evidence in this proceeding.

On pages 18 and 19 of its Order, the Commission rejected KIUC's proposal that the Sebree smelter pay a contribution toward the stranded generation costs it caused by contracting with Big Rivers and Kenergy to take generation service through a market-based rate. The Commission stated:

> *With respect to the market access charge, we adopt our findings in Case No. 2013-00221 and find that KIUC's recommendation to conditionally approve the proposed transaction agreements subject to a future market access charge not reasonable. Like the transaction agreements relating to the Century Hawesville smelter, the Century Sebree Transaction Agreements "were a product of extensive and good faith negotiations among Big Rivers, Kenergy, Century [Sebree], and Century Aluminum with the goal of keeping the [Sebree] smelter viable while not subjecting the remaining customers to any additional incremental costs after [January 31, 2014] due to Kenergy's continuing to serve Century [Sebree] or Big Rivers serving as the Market Participant." The imposition of a market access charge would unreasonably jeopardize the delicate balance achieved by the proposed transaction agreements.*

The evidence in the record does not support the Commission's conclusion that the Sebree Transaction Agreements, "*were a product of extensive and good faith negotiations among Big Rivers, Kenergy, and* [Century]" that achieved a "*delicate balance*" that would be jeopardized by the imposition of a stranded cost charge. No party to this case provided sufficient evidence to demonstrate that levying additional fees on the Sebree smelter would likely result in the termination of the Transaction Agreements by Century.

The Companies provided no quantitative support whatsoever for the severe reduction in the Sebree smelter rate they propose in this proceeding. Big Rivers witness Robert Berry conceded this point at hearing:

> Q: "*...neither Big Rivers nor Kenergy conducted an economic analysis to support this application pending before the Commission, is that correct?*
>
> *A: That's correct.*"[1]

As the record reflects, *"[n]either Big Rivers nor Kenergy performed any financial analysis of whether a market-based power supply was necessary to keep the Sebree smelter in operation."*[2]

At the hearing, witnesses for Big Rivers confirmed that the proposed arrangements were entered into with no inquiry or knowledge of the Sebree smelter's profitability:

> Q: *"...you've conducted no analysis to know how profitable or unprofitable the Sebree smelter is, correct?*
>
> Mr. Berry: *"That's correct."*[3]
>
> Q: "*How can you say the only alternative is for* [the Sebree Smelter] *to shut down if you really don't really have any information on how profitable it is?*
>
> Mr. Berry: *"Well, I'm basing that off of the negotiations that we held with Century....And, you know, we're basing that on the negotiations and what Century's feedback from the negotiations are saying.*"[4]

Based on Big Rivers' acknowledgement that they made no inquiry into the finances of the Sebree smelter, it is impossible to conclude that the agreement achieved a "*delicate balance*" that would be jeopardized by the imposition of a stranded cost charge. In fact, the only evidence in the record that offered any insight into the Sebree smelter's profitability indicated that the smelter is not on the verge of closing, but instead is profitable and perhaps able to pay a higher rate than the rate negotiated by Big Rivers.

While the intervenors did not have the right to conduct discovery on Century, per the Commission's November 26, 2013 Order, the intervenors were able to piece some information together through correspondence between Big Rivers and the Sebree smelter's owners (Century, and previously Alcan) that points to the Sebree smelter's profitability.[5]

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[1] Tr. at 30:23-31:1.
[2] Direct Testimony of Lane Kollen ("Kollen Testimony") at 13:14-20 (citing Big Rivers' Response to KIUC 1-12(b))
[3] Tr. at 35:22-25.
[4] Tr. at 50:3-13.
[5] Kollen Testimony at 8

The record also showed that Alcan offered to continue purchasing electric service from Big Rivers at a rate of $43/MWh. This offer, if it had been accepted by Big Rivers, would have paid for a significant portion of the fixed costs incurred to serve the Sebree smelter.[6] The fact that Alcan made this offer also may indicate that the Sebree smelter can be profitable at a rate higher than its projected average market rate. Obviously, if Big Rivers would have accepted this offer from Alcan, Big Rivers would have been able to avoid much of its currently pending request of a $71.2 million,[7] and keep its Wilson generating station open for the foreseeable future.

Although Century submitted post-hearing data responses disputing claims regarding its profitability,[8] neither Staff nor the intervenors had an opportunity to respond to the representations made in Century's data responses, nor have they been able to conduct discovery in order to fill in missing data points or cross-examine Century witnesses regarding these data responses. Further, while Century is telling the Commission that it must accept the proposed agreements without modification or the Sebree smelter will shut down, Century is telling Wall Street that the proposed market-based rate will increase its annual profits by approximately $66.4 million.[9] Century's representations to Wall Street are inconsistent with a company that is on the verge of shutting down its smelter. Thus, Century's claims fail to provide adequate assurance that the proposed arrangements will not result in non-Smelters excessively subsidizing the Sebree smelter's preferential access to market-based rates.

In sum, the evidence in the record does not support the Commission's conclusion that the Sebree Transaction Agreements were a product of extensive and good faith negotiations among Big Rivers, Kenergy, and Century that achieved a "*delicate balance*" that would be jeopardized if the Commission required the Sebree smelter to make a contribution toward Big Rivers' excess capacity that is no longer "*used and useful.*" KIUC respectfully requests that the Commission initiate a rehearing in order to investigate whether the imposition of a rate that would force the Sebree smelter to contribute to the costs of Big Rivers' excess capacity would in fact jeopardize the Sebree Transaction Agreements.

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[6] Kollen Testimony at 29:18-22.
[7] Case No. 2013-00199.
[8] *See* Century Response to On-The-Record Data Request (January 9, 2014).
[9] KIUC Ex. 7.

<u>ASSIGNMENT OF ERROR #2:</u> The Commission failed to address whether the profitability of the Sebree smelter is a relevant issue when determining fair, just and reasonable rates for both Sebree and Big Rivers' remaining customers.

Big Rivers' stated goal in negotiating the Sebree Transaction Agreements was to ensure that the Transaction would not cause Big Rivers or its customers to absorb "*any of the incremental costs associated with Century Sebree obtaining electric generation from the wholesale market.*"[10] The resulting Transaction Agreements were designed only to recover incremental costs from the Sebree smelter's continued operations and ignored the possibility that the Sebree smelter may be in a financial position to contribute to the fixed costs of excess capacity that Big Rivers is attempting to recover from its remaining customers in Case No. 2013-00199.

Big Rivers claims that the issue of whether the Sebree smelter is profitable is irrelevant and maintains that it had no obligation to negotiate an agreement with Century that would provide a contribution to the fixed costs associated with the excess capacity caused by the departure of the smelter. Under this logic, even if the Sebree smelter were making a billion dollars per year in profit, Big Rivers would maintain that its remaining customers should pay 100% of the costs of the Wilson and Coleman units which are not "*used and useful,*" while the Sebree smelter pays nothing for Big Rivers' investment in those units. The Commission's Order in this case does not specify whether the Commission agrees with Big Rivers that the Sebree smelter's profitability is irrelevant.

The Commission should not view the electric service arrangements between Big Rivers, Kenergy, and Century as mere market access agreements that are completely divorced from Big Rivers' traditional role as a G&T cooperative. Those arrangements constitute the proposed "*rate*" for the Sebree smelter. [11] And the Commission is statutorily charged with setting rates at fair, just, and reasonable levels and on a non-discriminatory basis.

As explained previously, the Wilson and Coleman units were reacquired as a part of the 2009 Unwind Transaction in order to serve the smelters.[12] A fair, just, and reasonable rate for the Sebree smelter would be a rate that allows it to remain profitable, but also provides a contribution toward the fixed costs Big Rivers incurred

[10] Direct Testimony of Robert Berry at 46-47.
[11] KRS 278.010(12)(defining "*rate*" as "*any individual or joint fare, toll, charge, rental, or other compensation for service rendered or to be rendered by any utility, and any rule, regulation, practice, act, requirement, or privilege in any way relating to such fare, toll, charge, rental, or other compensation, and any schedule or tariff or part of a schedule or tariff thereof.*").
[12] *See* KIUC Brief at 5.

to serve the Sebree smelter. Forcing Big Rivers' remaining customers to pay all of the stranded costs associated with the excess capacity reacquired to serve the Sebree (and Hawesville) smelters, without first determining whether the Sebree smelter can afford to make such a contribution would be a lapse in the Commission's statutory duty to set fair, just, and reasonable rates. Failing to consider this question opens up the possibility that the Sebree smelter could be hugely profitable while Big Rivers' remaining customers pay the highest rates in Kentucky[13] in order to cover the costs of the capacity acquired to serve the smelters. This would be a discriminatory and unreasonable result.

KIUC respectfully requests that the Commission expressly find that the profitability of the Sebree smelter is a relevant issue, and initiate a rehearing in order to determine if the Sebree smelter is profitable and in a position to make a contribution toward the stranded generation costs it caused.

<u>ASSIGNMENT OF ERROR #3:</u> The Commission's Order approving the Sebree Transaction Agreements without requiring evidence that the Sebree smelter was financially unable to contribute to the costs of the excess capacity acquired to serve the smelters is arbitrary, unreasonable, and may violate KRS § 278.170(1) and KRS § 278.030(1) depending upon the Commission's ultimate decision in Case No. 2013-00199.

KRS §278.170(1) states:

> *No utility shall, as to rates or service, give any unreasonable preference or advantage to any person or subject any person to any unreasonable prejudice or disadvantage, or establish or maintain any unreasonable difference between localities or between classes of service for doing a like and contemporaneous service under the same or substantially the same conditions.*

The Commission's Order approved a ratemaking scheme in which the costs stranded by the Sebree smelter's contract for market-based rates may be allocated to Big Rivers' remaining customers. The Sebree smelter will take electric generation service at market rates without any responsibility to pay for the stranded costs that it caused.

Depending upon the Commission's ultimate decision in Case No. 2013-00199, its Order in this proceeding may violate KRS §278.170(1). The Order acknowledges that there are costs stranded by the Sebree smelter leaving Big Rivers' system in order to receive market pricing, yet it failed to allocate these stranded costs to the cost-causer, the Sebree smelter. This preferential market-based pricing for the benefit of Century will be

[13] *See* Case No. 2013-00199, Sierra Club Ex. 20; KIUC Ex. 12.

unduly discriminatory if the Commission requires Big Rivers' remaining non-smelter customers to pay for the stranded costs caused by Century in Case No. 2013-00199.

The Commission's Order may also violate KRS § 278.030(1). On pages 18-19 of its Order, the Commission stated that the imposition of a stranded cost charge would upset the "*delicate balance*" reached by the Transaction Agreements. The Commission's finding with respect to a stranded cost charge is unreasonable and may be unlawful. KRS § 278.030(1) states:

> *Every utility may demand, collect and receive fair, just, and reasonable rates for the services rendered or to be rendered by it to any person.*

Prior to the January 30, 2014 Order, Big Rivers' rates were designed to recover the capacity costs incurred to serve the load from the Sebree smelter. After the January 30, 2014 Order, the Sebree smelter will receive a significant rate reduction through its market-based rate while Big Rivers petitions the Commission for rates that will recover the costs of Big Rivers' generation units that are no longer *"used and useful"* from its remaining customers. The Commission's Order implicitly assumes that a fair, just, and reasonable rate for the Sebree smelter is the market price. The Commission failed to consider the capacity costs that became "stranded" or uneconomic when the Sebree smelter entered into an arrangement for market-based pricing. The Commission unlawfully and unreasonably failed to consider whether absolving the Sebree smelter from paying any of the costs stranded by its market pricing agreement will result in fair, just, and reasonable rates for Big Rivers' remaining customers.

If Big Rivers' remaining customers are ultimately not required to pay for the capacity costs stranded by the departure of the Sebree smelter in the pending Case No. 2013-00199, then there will be no violation of KRS § 278.170(1) and KRS § 278.030(1), and KIUC's argument on this point may be rendered moot. But the outcome of the pending rate case is unknown at this time.

ASSIGNMENT OF ERROR #4: The Commission's Order fails to "*balance the interests*" of Big Rivers, its creditors, and its ratepayers.

In its Order in Case No. 2012-00535, the Commission addressed Big Rivers' excess capacity as a result of the departure of the smelters from its system and stated that rates should be set in order to *"balance the interests"* of ratepayers and the utility:

> *Under the circumstances presented in this case, the Commission finds that in setting rates, we must balance the interests of both the utility and its ratepayers...*
>
> ***
>
> *[T]he Commission finds it both reasonable and necessary to exclude some costs of the Coleman Station from Big Rivers' rates. It would simply not be fair to require ratepayers to pay all of costs of the excess capacity. Therefore, we will exclude the depreciation expense associated with the Coleman Station from rates at this time...*
>
> ***
>
> *The decision we make today is not an easy one, and some of our rate-making adjustments may be viewed as atypical. But we firmly believe that today's decision fairly balances the interests of all stakeholders. Ratepayers will not be required to pay for depreciation on the Coleman Station that is currently excess capacity, and Big Rivers' will to be able to avoid a default on its debts, continue to provide safe and reliable electric service to the 112,000 customers served by its member-owners, be able to implement its mitigation plan, and possibly attract new load.*[14]

This language is consistent with Commission precedent in which the Commission held that both customers *and* creditors have a role in addressing, resolving, and sharing the effects of Big Rivers' generating capacity that is excess compared to the needs of the utility's customers. In Big Rivers' financial workout plan case, Case No. 9613, the Commission determined that customers should not be held responsible for 100% of Big Rivers' debts. Specifically, the Commission stated:

> *We emphatically reject the claims of REA, the banks, and Big Rivers that the members of the cooperative ultimately bear the total risk and responsibility for the utility's debts. The distribution cooperatives and their members do not stand in the same position as shareholders of an investor-owned company. The REA, with its oversight and monitoring responsibility, bears a substantial amount of the risk associated with Big Rivers' actions. The creditor banks are compensated for the risks they take. Cooperative members must shoulder a portion of the risk, too, since they have a say in the affairs of the utility. Nor are the aluminum companies exempt from responsibility. Until the downturn of recent years, these companies or their predecessors were in frequent contact with Big Rivers' management. Rather than allocate the risk among all parties now, we have chosen to give the participants an opportunity to discuss the allocation among themselves as a revised workout plan is negotiated.*[15]

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[14] Case No. 2012-00535, Order, (October 29, 2013)at 19-20.

[15] *In the Matter of Big Rivers Electric Corporation's Notice of Changes in Rates and Tariffs for Wholesale Electric Service*

In its Order in this case, the Commission did not address whether the smelters, which continue to operate and continue to take service through Kenergy and Big Rivers, should contribute a portion of the costs of servicing the debt and other non-avoidable costs related to the reacquisition of the Wilson and Coleman units for the smelters' benefit.

Given the Commission's Order in this case, the *"balancing of interests"* described in the 2012-00535 Order may not be achieved. The Commission has determined in this case and in Case No. 2013-00221 that the two smelters bear no responsibility for Big Rivers' excess capacity that is no longer *"used and useful."* And in Case No. 2012-00535, the Commission determined that the only excess capacity costs that Big Rivers' remaining customers would not have to pay for presently are the Coleman depreciation expenses, which may or may not be recoverable by Big Rivers from customers in the future.[16] Hence, as it stands today, Big Rivers' remaining, non-smelter customers are responsible for all, or nearly all, of the costs of the excess capacity that was acquired to serve the smelters.

Obviously, the Commission has not yet issued its final order in Big Rivers' most recent rate case (Case No. 2013-00199) in which many of these same issues of excess capacity cost responsibility are being considered. It is possible that the Commission's order in that case could institute a plan that would *"right-size"* Big Rivers and require creditor contributions to pay for Big Rivers' excess capacity. In that instance, ratepayers may not object to the Sebree smelter escaping responsibility to pay for the excess capacity it caused and the arguments in this Petition for Rehearing may be rendered moot. However, if the Commission does not establish such a creditor contribution in Case No. 2013-00199, then the Commission's Order in this case, which determined that the Sebree smelter should not be required to pay any costs of Big Rivers' excess capacity, without even considering the question of whether the Sebree smelter is financially capable of paying such costs, is unduly discriminatory and provides an unreasonable preference to the Sebree smelter at the expense of Big Rivers' remaining ratepayers.

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and of a Financial Workout Plan, Case No. 9613, Order (March 17, 1987) at 19.

[16] Case No. 2012-00535, Order (October 29, 2013) at 19.

WHEREFORE, KIUC respectfully request that the Commission reexamine and modify its Order to correct the errors discussed herein.

Respectfully submitted,

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February 21, 2014