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October 30, 2015

Via Hand-Delivery

RECEIVED
OCT 30 2015
PUBLIC SERVICE COMMISSION

Mr. Jeffrey Derouen
Executive Director
Kentucky Public Service Commission
P.O. Box 615
211 Sower Boulevard
Frankfort, KY 40602

Re: In the Matter of: The Application of East Kentucky Power Cooperative, Inc. for Deviation from Obligation Resulting from Case No. 2012-00169
PSC Case No. 2015-00358

Dear Mr. Derouen:

Enclosed please find for filing with the Commission in the above-referenced case an original and ten (10) copies of the Application of East Kentucky Power Cooperative, Inc. for Deviation from Obligation Resulting from Case No.2012-00169. Please return a file-stamped copy to me.

Do not hesitate to contact me if you have any questions.

Very truly yours,

David S. Samford

Enclosures

M:\Clients\4000 - East Kentucky Power\8790 - PJM Related Advice (Post Integration)\Correspondence\Ltr. to Jeff Derouen (2012-00169)- re Application - 151030.docx

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OCT 30 2015

PUBLIC SERVICE
COMMISSION

COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

THE APPLICATION OF EAST KENTUCKY POWER COOPERATIVE, INC. FOR DEVIATION FROM OBLIGATION RESULTING FROM CASE NO. 2012-00169	) Case No. 2015-00358

APPLICATION

Comes now East Kentucky Power Cooperative, Inc. ("EKPC"), by counsel, pursuant to KRS Chapter 278 and other applicable law, and for its Application for approval to deviate from a directive of the Kentucky Public Service Commission ("Commission") originating in Case No. 2012-00169 (the "PJM Integration Case"),[1] respectfully states as follows:

I. INTRODUCTION

1. EKPC is a not-for-profit generation and transmission rural electric cooperative corporation with its headquarters in Winchester, Kentucky. EKPC provides wholesale electricity to its sixteen Owner-Member distribution cooperatives, which in turn serve approximately 525,000 Kentucky homes, farms and commercial and industrial customers in eighty-seven (87) Kentucky counties.

2. On May 3, 2012, EKPC filed an application with this Commission seeking approval, pursuant to KRS 278.218, to transfer functional control of certain transmission facilities to PJM Interconnection, LLC ("PJM"), effective June 1, 2013.[2] Although EKPC had been a member of PJM since 2005 for purposes of participating in the regional transmission organization's ("RTO")

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[1] *In the Matter of the Application of East Kentucky Power Cooperative, Inc. to Transfer Functional Control of Certain Transmission Facilities to PJM Interconnection, LLC* (filed May 3, 3012).

[2] *Id.*

energy market and reserving transmission service within the PJM region, EKPC believed it could realize significant economic and reliability benefits through full integration within PJM. The Commission found EKPC's request sufficiently supported by competent evidence, and thus it approved EKPC's request to fully integrate within PJM by Order entered December 20, 2012 (the "PJM Integration Order").[3]

3. To ensure EKPC's continued membership in PJM is beneficial to its Owner-Members and consumers, the PJM Integration Order requires EKPC to annually provide the Commission with a comprehensive report ("PJM Annual Report") detailing transmission rights, hedging strategies, and PJM benefits and costs.[4] EKPC has fully complied with this requirement, and its most recent PJM Annual Report was tendered to the Commission on July 31, 2015.

4. In addition to annual reports, the PJM Integration Order requires EKPC to file, "no later than November 30, 2015, an application for approval of a rate mechanism to flow back to customers the capacity market benefits expected to accrue from membership in PJM."[5] In light of the tremendous uncertainty and potentially massive complications that accompany recent federal environmental regulations, EKPC respectfully requests that the Commission grant it permission to deviate from the PJM Integration Order's directive regarding the implementation of a capacity benefits sharing mechanism ("CBS Mechanism") and suspend the obligation for a period of eighteen (18) months, or until May 31, 2017.[6]

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[3] Case No. 2012-00169, *In the Matter of the Application of East Kentucky Power Cooperative, Inc. to Transfer Functional Control of Certain Transmission Facilities to PJM Interconnection, LLC* (Ky. P.S.C., Dec. 20, 2012).

[4] *Id.*, at pp. 19-20; *see also* Case No. 2015-00116, *In the Matter of East Kentucky Power Cooperative, Inc.'s Request to Modify the Due Date of the Annual Report on Participation in the PJM Interconnection, LLC* (Ky. P.S.C., May 14, 2015) (modifying the date by which EKPC must file its annual reports to better align with PJM's operating year).

[5] *Id.*, at p. 20.

[6] EKPC's Board of Directors has authorized this filing, and a copy of the relevant Resolution from the Board Meeting held October 13, 2015, is attached hereto and incorporated herein as Exhibit 1.

II. FILING REQUIREMENTS

5. Pursuant to 807 KAR 5:001, Section 14(1), EKPC's mailing address is P. O. Box 707, Winchester, Kentucky 40392-0707 and its electronic mail address is psc@ekpc.coop. Counsel for EKPC should be served at the following email addresses: mdgoss@gosssamfordlaw.com, david@gosssamfordlaw.com, and ebuckley@gosssamfordlaw.com.

6. Pursuant to 807 KAR 5:001, Section 14(2), EKPC is a Kentucky rural electric cooperative corporation established under KRS Chapter 279 and incorporated on July 9, 1941. EKPC is in good standing within and throughout the Commonwealth of Kentucky.

III. NECESSITY OF RELIEF

7. Present circumstances—which simply could not have been foreseen in 2012—weigh strongly in favor of postponing the creation of the CBS Mechanism called for by the PJM Integration Order.[7] Although EKPC remains committed to directly sharing its PJM capacity benefits with its Owner-Members and the ultimate consumers, it would be imprudent and unreasonable to implement such an allocation arrangement at this juncture.

8. As the Commission is aware, generation and transmission cooperatives such as EKPC are among the most stringently environmentally regulated entities in the United States. The pace of revisions to federal environmental rules has increased substantially over the past decade and significantly impacted EKPC's business as a result.

9. For instance, EKPC currently complies with multiple EPA rules governing air emissions, including: New Source Performance Standards ("NSPS"); New Source Review Rules ("NSR")

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[7] For example, as late as this summer, the United States Environmental Protection Agency ("EPA") announced a revised Clean Power Plan that included terms which were much less favorable to Kentucky's utilities, including EKPC. The dramatic reversal on the part of the EPA has unexpectedly injected significant uncertainty into utilities' planning processes. This and other federal environmental rules are discussed in more depth later.

and the Green House Gas Tailoring Rule ("Tailoring Rule") revisions to the NSR; Title IV of the Clean Air Act ("CAA") and associated rules governing pollutants that contribute to acid rain ("Acid Rain Rules"); CAA Title V operating permit requirements ("Title V Requirements"); Summer ozone trading program requirements based upon Section 126 petitions and the Ozone State Implementation Plan Call ("Summer Ozone Program"); National Ambient Air Quality Standards ("NAAQS") for Sulfur Dioxide ("SO_2"), Nitrogen Dioxide ("NO_2"), Carbon Monoxide ("CO"), Ozone, Particulate Matter ("PM"), Particulate Matter of 2.5 microns or less ("PM 2.5") and Lead; the Cross State Air Pollution Rule ("CSAPR"); the Clean Air Visibility Regional Haze Rule; National Emissions Standards for Hazardous Air Pollutants ("NESHAPs"); and the Mercury and Air Toxics Standards ("MATS").[8]

10. In addition, EKPC currently complies with several other environmental rules and permits established and issued by the EPA, the U.S. Army Corps of Engineers, the Kentucky Division of Air Quality, the Kentucky Division of Water and the Kentucky Division of Waste Management.

11. EKPC is also undertaking efforts to evaluate and comply with certain other federal environmental rules which are likely to have future impacts upon the cooperative's ability to generate electricity, including: the Coal Combustion Residuals Rule ("CCR"); the 316(b) Rule under the Clean Water Act ("316(b) Rule"); the Effluent Limitation Guidelines Rule ("ELG"); Ozone NAAQS; and, perhaps most notably, the Clean Power Plan.

[8] On June 29, 2015, the United States Supreme Court determined that the MATS Rule was not properly reviewed and promulgated by the EPA, thereby reversing a decision of the D.C. Circuit Court of Appeals and remanding the case challenging the rule to the lower court. Since the decision was directed at the scope of the EPA's rationale and not the agency's authority to promulgate the rule, it is widely anticipated that the MATS Rule will be re-promulgated by the EPA in the near future. Regardless, many utilities, including EKPC, have already been forced to make investment decisions based upon MATS prior to the Supreme Court's ruling.

12. The Clean Power Plan, promulgated by the EPA under the authority of the CAA section 111(d), is a rule designed to reduce greenhouse gas emissions from existing fossil fuel-fired electric generating units. It was finalized by notice issued on August 3, 2015, and will become effective sixty (60) days after publication in the Federal Register (which publication occurred on October 23, 2015). The Clean Power Plan is perhaps the most important, challenging, costly and impactful environmental regulation faced by EKPC in its history.

13. Through the Clean Power Plan, the EPA is establishing carbon dioxide (CO_2) emission performance rates representing the best system of emission reduction for two subcategories of existing fossil fuel-fired electric generating units ("EGUs") – fossil fuel-fired electric utility steam generating units and stationary combustion turbines. The final rule establishes an emission performance rate of 1305 lbs. of CO_2 per net megawatt-hour ("MWh") for all affected steam EGUs nationwide and an emission performance rate of 771 lbs. of CO_2 per net MWh for all affected stationary combustion turbines nationwide. It should be noted that neither of these limits are capable of being met by either existing or new EGUs available in the market today.

14. The Clean Power Plan also establishes state-specific CO_2 goals reflecting the CO_2 emission performance rates, as well as guidelines for the development, submittal and implementation of state plans that set emission standards or other measures to implement the CO_2 emission performance rates. Final state implementation plans ("SIPs") must be submitted no later than September 6, 2016. However, due to the numerous and varied actions states must take to complete a SIP, including technical work, state legislative and rulemaking activities, a robust public participation process, coordination with third parties, coordination among states involved in multi-state plans, and consultation with reliability entities, the EPA is allowing an optional two-phased submittal process for SIPs. Under the two-phase process, a state must still submit an initial

SIP by September 6, 2016, but may request a two-year extension to submit its final SIP. The extension may be granted by the EPA if various criteria are met, including: the state must identify the final plan approach or approaches under consideration, including a description of progress made to date; the state must provide an appropriate explanation for why it needs additional time to submit a final plan beyond September 6, 2016; and the state must demonstrate how it has been engaging with the public, including vulnerable communities, and provide a description of how it intends to meaningfully engage with community stakeholders during the additional time (if an extension is granted) for development of the final SIP. If a state does not submit a SIP, or if the EPA disapproves a state's SIP, then the EPA has the express authority under CAA section 111(d) to establish a federal plan for the state.

15. Although a full description of the wide-ranging and incredibly onerous provisions of the Clean Power Plan is not herein included, it is evident that environmental regulations affecting generation and transmission utilities are both dynamic and increasingly stringent. Exacerbating the challenges presented by the Clean Power Plan is the tremendous uncertainty that currently surrounds its implementation at both the federal and state level.

16. Undoubtedly, the Clean Power Plan will face numerous legal challenges once effective. In fact, EKPC has already joined with energy providers and industry groups throughout the United States to seek judicial review of the Clean Power Plan.[9] The EPA's authority to issue the rule, the rule's conformity with existing statutory law, and the manner in which the rule was devised and issued are just a few of the many issues the judicial system will address in the coming months. Such legal opposition may result in changes to the rule's substantive provisions, a stay with respect

[9] *See National Rural Electric Cooperative Association, at al. v. U.S. Environmental Protection Agency*, No. 15-1376 (D.C. Cir. filed October 23, 2015).

to compliance by impacted utilities, and/or the remanding or vacating of the rule. EKPC continues to evaluate the validity and likelihood of success of such legal arguments.

17. Irrespective of the questionable legality of all or parts of the Clean Power Plan, it remains entirely unclear under what type of implementation plan Kentucky may operate. First, the state may choose to adopt and submit a SIP, which could take one of two general forms. One approach, known as an "emission standards" state plan type, would apply all requirements for meeting the emission guidelines to affected EGUs in the form of federally enforceable emission standards. The second approach, known as the "state measures" plan type, would allow the state mass CO_2 emission goals to be achieved by affected EGUs in part, or entirely, through state measures that apply to affected EGUs, other entities, or some combination thereof. The state measures plan type also includes a mandatory contingent backstop of federally enforceable emission standards for affected EGUs that would apply in the event the plan does not achieve its anticipated level of emission performance as specified in the state plan during the period that the state is relying on state measures. Each of these general SIP types, which may be implemented on a single-state or multi-state basis, may contain many intricacies and variations that are simply unknowable at this time (*e.g.*, mass-based approach, rate-based approach, emission trading programs, etc.).

18. Kentucky may also refuse to submit a SIP, or submit a non-approvable SIP, thereby requiring the EPA to impose a federal implementation plan ("FIP") upon the state.[10] The nature

[10] During the 2014 Regular Session, the Kentucky legislature passed HB 388, which was subsequently signed by the Governor and is now codified at KRS 224.20-140 *et seq.* The law establishes criteria by which the Kentucky Energy and Environment Cabinet can establish performance standards for the regulation of carbon dioxide emissions from existing fossil fuel-fired electric generating units; moreover, the law restricts the ability of the Cabinet to submit a SIP to the EPA unless specific requirements are met. *See* KRS 224.20-145 (requiring, *inter alia*, that any SIP submitted to the EPA be prepared in consultation with Commission to ensure that the plan minimizes the impacts on current and future industrial, commercial, and residential consumers and does not threaten the affordability of Kentucky's rates or the reliability of electricity service). The state's decision to submit SIP, as well as the content of a SIP should one be submitted, will likely be significantly impacted by this law.

and terms of a FIP applicable to Kentucky presents similar challenges with respect to uncertainty that a possible SIP presents, and it is safe to presume the that EPA may be less aware of and unresponsive to local priorities and statewide needs.

19. Compounding the issues of ambiguity that surround the implementation of the Clean Power Plan are the upcoming state and national elections that will occur during the next thirteen (13) months. The leaders chosen and their respective positions regarding energy, the environment, and economic welfare will have a considerable impact on the regulatory climate and enforcement of standards. The oft-changing landscape of state and federal public policy, especially in the context of the Clean Power Plan and similar environmental regulation, results in significant and costly consequences for EKPC, its Owner-Members, and Kentuckians at large.

20. In light of the foregoing, EKPC is faced with numerous, important decisions that must be made in order to best move forward in the interest of its Owner-Members. Of course, EKPC's unwavering focus is on the provision of reliable and affordable energy. Whether EKPC ultimately determines that it should upgrade its existing EGUs to comply with applicable law (including not only the Clean Power Plan, but CCR, ELG, Ozone NAAQS, and other relevant standards), construct new generation resources, explore power purchase agreements, rely on market purchases, or some combination of these and other options, there can be no doubt that the environmental regulation discussed herein will have an enormous financial impact on EKPC's business in both the near and long term.

21. Due to the regulatory landscape in general, and the tremendous uncertainty associated with the Clean Power Plan in particular, EKPC believes it necessary and prudent to request an extension of time to file the CBS Mechanism contemplated by the PJM Integration Order. All interested parties recognize that the cost of producing and delivering safe and reliable electricity

will increase substantially as a result of stringent environmental regulations; however, until at least some of the many uncertainties described herein are resolved, it is impossible to know the full extent of the financial impact. EKPC expects significant capital outlays in the years to come in order to remain compliant, and it is imprudent and unreasonable at this time to impede EKPC's ability to address forthcoming challenges by requiring the immediate distribution of PJM capacity benefits.

III. REQUEST FOR DEVIATION

22. EKPC's Board of Directors has made the reasonable and prudent strategic business decision to request an extension until May 31, 2017, to file for Commission approval of a CBS Mechanism. The requested deviation will afford EKPC an opportunity to better develop compliance strategies with respect to the Clean Power Plan and other influential environmental regulations, as well as allow EKPC to gain a better understanding of the regulations' operational and financial impacts on both EKPC and the PJM capacity market at large. Moreover, an 18-month extension will permit EKPC and its Owner-Members additional time to discuss and develop better-aligned rate structures that provide workable solutions to the equitable sharing of benefits and costs, consistent with EKPC's strategic objectives. Finally, the requested temporary postponement of the CBS Mechanism will result in no significant harm, especially considering that other quantitative benefits of EKPC's PJM participation, such as trade benefits, are already largely returned to EKPC's Owner-Members and their retail customers through the utilities' Fuel Adjustment Clauses.[11] For these reasons, EKPC respectfully requests that the Commission grant

[11] *See* PJM Integration Order, at p. 20 ("Finally, the Commission finds that the bulk of the trade benefits that EKPC expects to accrue as a member of PJM will flow back to its 16 member cooperatives and their retail customers through the Fuel Adjustment Clause.").

it permission to deviate from the PJM Integration Order's directive regarding the implementation of a CBS Mechanism and suspend the obligation until May 31, 2017.

V. OVERVIEW OF TESTIMONY

23. As part of its Application, EKPC is tendering herewith the testimony of two (2) witnesses who support the averments set forth herein.

24. Mr. Don Mosier, EKPC's Executive Vice President and Chief Operating Officer, describes EKPC's Strategic Plan. Mr. Mosier also provides testimony on the impact the Clean Power Plan and other stringent environmental regulations may have on EKPC's business affairs. Mr. Mosier's testimony is attached hereto and incorporated herein as Exhibit 2.

25. Mr. Michael McNalley, EKPC's Executive Vice President and Chief Financial Officer, provides an overview of EKPC's recent financial performance and underscores the financial considerations which support EKPC's requested relief in this proceeding. Mr. McNalley's testimony is attached hereto and incorporated herein as Exhibit 3.

VI. CONCLUSION

WHEREFORE, on the basis of the foregoing, EKPC respectfully requests the Commission to enter an Order approving this Application and:

1) Granting EKPC permission to deviate from the Commission's directive in the PJM Integration Order regarding the implementation of a capacity benefits sharing mechanism and extending the deadline by which it must file the CBS Mechanism for a period of eighteen (18) months, or until May 31, 2017;
2) Granting the relief requesting herein on or before November 30, 2015, or entering an interim order declaring that EKPC is not required to comply with the relevant directive until a reasonable time has elapsed following a final Order in this case; and

3) Granting any other relief to which EKPC may be entitled.

This 30th day of October, 2015.

VERIFICATION

COMMONWEALTH OF KENTUCKY)
COUNTY OF CLARK)

Comes now Michael McNalley, Executive Vice President and Chief Financial Officer of East Kentucky Power Cooperative, Inc., in my official capacity, and, after being duly sworn, I do hereby solemnly swear that the averments set forth above are true and correct to the best of my knowledge and belief as of this 31st day of October, 2015.

MICHAEL McNALLEY, Executive Vice President and Chief Financial Officer of East Kentucky Power Cooperative, Inc.

Signed before me, the NOTARY PUBLIC, by Michael McNalley, Executive Vice President and Chief Financial Officer of East Kentucky Power Cooperative, Inc., after being duly sworn, on this 30th day of October, 2015.

NOTARY PUBLIC, Commission # 508144

My Commission Expires 11-30-17

GWYN M. WILLOUGHBY
Notary Public
State at Large
Kentucky
My Commission Expires Nov 30, 2017

Respectfully submitted,

Mark David Goss
David S. Samford
M. Evan Buckley
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Counsel for East Kentucky Power Cooperative, Inc.

Index of Exhibits

FROM THE MINUTE BOOK OF PROCEEDINGS
OF THE BOARD OF DIRECTORS OF
EAST KENTUCKY POWER COOPERATIVE, INC.

At a regular meeting of the Board of Directors of East Kentucky Power Cooperative, Inc. held at the Headquarters Building, 4775 Lexington Road, located in Winchester, Kentucky, on Tuesday, October 13, 2015, at 9:30 a.m., EDT, the following business was transacted:

Request for Authorization to Seek from the Kentucky Public Service Commission an Extension of Time for Filing EKPC's PJM Capacity Market Benefits Mechanism

After review of the applicable information, a motion to approve the Request for Authorization to Seek from the Kentucky Public Service Commission an Extension of Time for Filing EKPC's PJM Capacity Market Benefits Mechanism, was made by Strategic Issues Committee Chairman Landis Cornett, and passed by the full Board to approve the following:

Whereas, East Kentucky Power Cooperative, Inc., ("EKPC") is required by the Kentucky Public Service Commission's ("Commission") December 20, 2012 Order in Case No. 2012-00169 to file a PJM Capacity Market Benefits mechanism no later than November 30, 2015; and

Whereas, The dollar value of the demand credit resulting from the PJM Capacity Market Benefits mechanism to retail customers would at present be small; and

Whereas, The standard residential rate structure for EKPC's Member Distribution Cooperatives does not include a demand charge component, making the development of a methodology to provide a demand credit for this customer class unworkable; and

Whereas, The financial requirements for EKPC's compliance with the Environmental Protection Agency's Clean Power Plan are likely substantial and capacity-related; and

Whereas, An extension of 18 months in the filing of the required PJM Capacity Market Benefits mechanism would allow EKPC the opportunity to determine if there will be improvement in the capacity market benefits and to better determine the financial demands of the compliance strategy for the Clean Power Plan;

Resolved, The EKPC Board hereby authorizes the Chief Executive Officer, or his designee, to seek regulatory approval from the Commission for an 18-month extension for the filing of the PJM Capacity Market Benefits mechanism required by the Commission's December 20, 2012 Order.

EXHIBIT

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The foregoing is a true and exact copy of a resolution passed at a meeting called pursuant to proper notice at which a quorum was present and which now appears in the Minute Book of Proceedings of the Board of Directors of the Cooperative, and said resolution has not been rescinded or modified.

Witness my hand and seal this 13th day of October 2015.

Michael Adams

Michael Adams, Secretary

Corporate Seal

COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

THE APPLICATION OF EAST KENTUCKY POWER COOPERATIVE, INC. FOR DEVIATION FROM OBLIGATION RESULTING FROM CASE NO. 2012-00169	)) Case No. 2015-_______)

DIRECT TESTIMONY OF DON MOSIER

ON BEHALF OF EAST KENTUCKY POWER COOPERATIVE, INC.

Filed: October 30, 2015

EXHIBIT

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2

I. Introduction

Q. PLEASE STATE YOUR NAME, POSITION, AND BUSINESS ADDRESS.

A. My name is Don Mosier and my business address is East Kentucky Power Cooperative, Inc. ("EKPC"), 4775 Lexington Road, Winchester, Kentucky 40391. I am Executive Vice President and Chief Operating Officer at EKPC.

Q. PLEASE BRIEFLY DESCRIBE YOUR EDUCATION AND PROFESSIONAL EXPERIENCE.

A. I obtained my Bachelor of Science degree in civil engineering from the University of Virginia and my Master of Business Administration degree from the Kenan-Flagler Business School at the University of North Carolina. My professional experience includes work at Carolina Power & Light (now Duke Energy Progress, Inc.) in Raleigh, North Carolina, developing merchant generation projects and marketing activities, regulatory affairs, and nuclear power plant engineering and operations. I also was an engineering manager of U.S. Operations for Canatom Corp., a Canadian-based engineering firm that provides nuclear plant engineering and construction services. Immediately prior to joining EKPC, I was Vice President of St. Louis-based Ameren Energy Marketing ("AEM'), a subsidiary of Ameren Corp. At AEM, I managed wholesale power trading, plant dispatch, NERC and SERC compliance, transmission and congestion management activities, and customer account management for Ameren Corporation's unregulated merchant generation fleet located in the Midcontinent ISO and PJM Interconnection, LLC ("PJM").

Q. PLEASE BRIEFLY DESCRIBE YOUR DUTIES AT EKPC.

A. I manage the day-to-day operations of power production and construction, power delivery, power supply, and system operations. I report directly to EKPC's Chief Executive Officer, Mr. Anthony Campbell.

Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY IN THIS PROCEEDING?

A. The purpose of my testimony is first to describe EKPC's Strategic Plan as it pertains to building and maintaining financial strength and embracing a prudent, equitable rate structure. My testimony will also elucidate the impact the contemplated CBS Mechanism (as that term is defined herein) may have on EKPC's business affairs, especially in light of the Clean Power Plan and other stringent environmental regulations.

Q. ARE YOU SPONSORING ANY EXHIBITS?

A. No.

II. EKPC Strategic Plan and Membership in PJM

Q. DOES EKPC HAVE A STRATEGIC PLAN CURRENTLY IN PLACE?

A. Yes. Following a Commission-directed management audit, EKPC's Board adopted a Strategic Plan in 2011 that identified various core strategies, including but not limited to pursuing prudent diversity in the fuel mix of the Cooperative's generation portfolio and evaluating new investments using sound financial principles. EKPC has convened Strategic Planning retreats annually since 2011 with the most recent being held in July of 2015. Cornerstones of EKPC's Strategic Plan include financial stability (with a specific emphasis on improving the cooperative's equity ratio) and the appropriate apportionment of costs and benefits through carefully-designed, equitable rates.

Q. WHEN DID EKPC BECOME A MEMBER OF PJM?

A. EKPC originally became a member of PJM in 2005 for purposes of participating in the regional transmission organization's ("RTO") energy market and reserving transmission service within the PJM region. During the ensuing years, EKPC participated in PJM in its capacity as an "Other Supplier" under the PJM Operating Agreement and as an electric utility under the terms of PJM's Open Access Transmission Tariff. By 2012, however, EKPC believed it could realize significant economic and reliability benefits through full integration within PJM. In May of that year, EKPC filed an application with the Commission seeking approval to transfer functional control of certain transmission facilities to PJM effective June 1, 2013. The Commission found EKPC's request sufficiently supported by competent evidence, and thus it approved EKPC's request to fully integrate within PJM by Order entered December 20, 2012 (the "PJM Integration Order").

Q. DID THE PJM INTEGRATION ORDER REQUIRE EKPC TO PERFORM ANY FUTURE ACTIONS?

A. Yes. The PJM Integration Order requires EKPC to annually provide the Commission with a comprehensive report detailing transmission rights, hedging strategies, and benefits and costs associated with EKPC's PJM membership. The PJM Integration Order also requires EKPC to file, "no later than November 30, 2015, an application for approval of a rate mechanism to flow back to customers the capacity market benefits expected to accrue from membership in PJM." This contemplated PJM capacity benefits sharing mechanism is referred to herein as the "CBS Mechanism."

Q. HAS EKPC FILED ANNUAL REPORTS IN SATISFACTION OF THE PJM INTEGRATION ORDER?

A. Yes. EKPC's most recent annual report was tendered to the Commission on July 31, 2015.

Q. PLEASE DESCRIBE THE RELIEF REQUESTED BY EKPC IN THIS PROCEEDING.

A. EKPC respectfully requests that the Commission grant it permission to deviate from the PJM Integration Order's directive regarding the implementation the CBS Mechanism and suspend the obligation for a period of eighteen (18) months, or until May 31, 2017.

III. Considerations and Developments in Support of the Requested Deviation

Q. IS EKPC SUBJECT TO EXTENSIVE ENVIRONMENTAL REGULATION?

A. Yes. As a generation and transmission utility, EKPC is among the most stringently environmentally-regulated entities in the United States. Environmental oversight of EKPC's operations is maintained by the U.S. Environmental Protection Agency ("EPA"), the U.S. Army Corps of Engineers, the Kentucky Division of Air Quality, the Kentucky Division of Water, and the Kentucky Division of Waste Management, among other authorities. The degree to and manner in which EKPC is regulated continually evolves, and the pace of revisions to federal environmental rules has increased substantially over the past decade.

Q. HAS EKPC RECENTLY OFFERED TESTIMONY TO THE COMMISSION CONCERNING THE ENVIRONMENTAL RULES AND REGULATIONS WITH WHICH IT IS IN COMPLIANCE?

A. Yes. As part of its Application in Case No. 2015-00267, EKPC offered testimony of its Director of Environmental Affairs, Jerry B. Purvis, in which he details the extensive list of environmental rules and regulations applicable to EKPC.[1] For instance, EKPC currently complies with multiple rules governing air emissions, including: New Source Performance Standards ("NSPS"); New Source Review Rules ("NSR") and the Green House Gas Tailoring Rule ("Tailoring Rule") revisions to the NSR; Title IV of the Clean Air Act ("CAA") and associated rules governing pollutants that contribute to acid rain ("Acid Rain Rules"); CAA Title V operating permit requirements ("Title V Requirements"); Summer ozone trading program requirements based upon Section 126 petitions and the Ozone State Implementation Plan Call ("Summer Ozone Program"); National Ambient Air Quality Standards ("NAAQS") for Sulfur Dioxide ("SO2"), Nitrogen Dioxide ("NO2"), Carbon Monoxide ("CO"), Ozone, Particulate Matter ("PM"), Particulate Matter of 2.5 microns or less ("PM 2.5") and Lead; the Cross State Air Pollution Rule ("CSAPR"); the Clean Air Visibility Regional Haze Rule; National Emissions Standards for Hazardous Air Pollutants ("NESHAPs"); and the Mercury and Air Toxics Standards ("MATS").[2] Of course, there are many more rules and

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[1] *See* Case No. 2015-00267, *In the Matter of The Application of East Kentucky Power Cooperative, Inc. for Approval of the Acquisition of Existing Combustion Turbine Facilities form Bluegrass Generation Company, LLC at the Bluegrass Generating Station in LaGrange, Oldham County, Kentucky and for Approval of the Assumption of Certain Evidences of Indebtedness*, Application at Exhibit 6 (filed July 24, 2015).

[2] On June 29, 2015, the United States Supreme Court determined that the MATS Rule was not properly reviewed and promulgated by the EPA, thereby reversing a decision of the D.C. Circuit Court of Appeals

regulations with which EKPC must comply other than the foregoing, including those that deal with water quality, soil, and wastes. EKPC is also undertaking efforts to evaluate and comply with certain other federal environmental rules which are likely to have future impacts upon the cooperative's ability to generate electricity, including: the Coal Combustion Residuals Rule ("CCR"); the 316(b) Rule under the Clean Water Act ("316(b) Rule"); the Effluent Limitation Guidelines Rule ("ELG"); Ozone NAAQS; and, perhaps most notably, the Clean Power Plan.

Q. PLEASE GENERALLY DESCRIBE THE CLEAN POWER PLAN.

A. The Clean Power Plan, promulgated by the EPA under the authority of the CAA section 111(d), is a rule designed to reduce greenhouse gas emissions from existing fossil fuel-fired electric generating units. It was finalized by notice issued on August 3, 2015, and will become effective sixty (60) days after publication in the Federal Register (which publication occurred on October 23, 2015).

Q. PLEASE PROVIDE AN OVERVIEW OF SOME OF THE MORE NOTABLE REQUIREMENTS OF THE CLEAN POWER PLAN.

A. Through the Clean Power Plan, the EPA is establishing carbon dioxide (CO_2) emission performance rates representing the best system of emission reduction for two subcategories of existing fossil fuel-fired electric generating units ("EGUs") – fossil fuel-fired electric utility steam generating units and stationary combustion

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and remanding the case challenging the rule to the lower court. Since the decision was directed at the scope of the EPA's rationale and not the agency's authority to promulgate the rule, it is widely anticipated that the MATS Rule will be re-promulgated by the EPA in the near future. Regardless, many utilities, including EKPC, have already been forced to make investment decisions based upon MATS prior to the Supreme Court's ruling.

turbines. The final rule establishes an emission performance rate of 1305 lbs. of CO_2 per net megawatt-hour ("MWh") for all affected steam EGUs nationwide and an emission performance rate of 771 lbs. of CO_2 per net MWh for all affected stationary combustion turbines nationwide. It should be noted that neither of these limits are capable of being met by either existing or new EGUs available in the market today.

The Clean Power Plan also establishes state-specific CO_2 goals reflecting the CO_2 emission performance rates, as well as guidelines for the development, submittal and implementation of state plans that set emission standards or other measures to implement the CO_2 emission performance rates. Final state implementation plans ("SIPs") must be submitted no later than September 6, 2016. However, due to the numerous and varied actions states must take to complete a SIP, including technical work, state legislative and rulemaking activities, a robust public participation process, coordination with third parties, coordination among states involved in multi-state plans, and consultation with reliability entities, the EPA is allowing an optional two-phased submittal process for SIPs. Under the two-phase process, a state must still submit an initial SIP by September 6, 2016, but may request a two-year extension to submit its final SIP. The extension may be granted by the EPA if various criteria are met, including: the state must identify the final plan approach or approaches under consideration, including a description of progress made to date; the state must provide an appropriate explanation for why it needs additional time to submit a final plan beyond September 6, 2016; and the state must demonstrate how it has been engaging with the public, including vulnerable communities, and provide a description of how it intends to meaningfully engage with community stakeholders during the additional time (if an extension is granted) for development of the final SIP.

Q. DOES EKPC KNOW WHETHER THE COMMONWEALTH OF KENTUCKY WILL ADOPT AND SUBMIT A SIP?

A. No. During the 2014 Regular Session, the Kentucky legislature passed HB 388, which was subsequently signed by the Governor and is now codified at KRS 224.20-140 *et seq*. The law establishes criteria by which the Kentucky Energy and Environment Cabinet can establish performance standards for the regulation of carbon dioxide emissions from existing fossil fuel-fired electric generating units; moreover, the law restricts the ability of the Cabinet to submit a SIP to the EPA unless specific requirements are met. *See* KRS 224.20-145 (requiring, *inter alia*, that any SIP submitted to the EPA be prepared in consultation with Commission to ensure that the plan minimizes the impacts on current and future industrial, commercial, and residential consumers and does not threaten the affordability of Kentucky's rates or the reliability of electricity service). The state's decision to submit a SIP, as well as the content of a SIP should one be submitted, will likely be significantly impacted by this law.

Q. IF KENTUCKY WERE TO ADOPT AND SUBMIT A SIP, DOES EKPC KNOW WHAT THE PLAN'S CONTENT AND REQUIREMENTS WOULD BE?

A. No. Under the Clean Power Plan, a SIP may take one of two general forms. One approach, known as an "emission standards" state plan type, would apply all requirements for meeting the emission guidelines to affected EGUs in the form of federally enforceable emission standards. The second approach, known as the "state measures" plan type, would allow the state mass CO_2 emission goals to be achieved by affected EGUs in part, or entirely, through state measures that apply to affected EGUs, other entities, or some combination thereof. The state measures plan type also includes a mandatory contingent backstop of federally enforceable emission standards for affected EGUs that would apply in the event the plan does not achieve its anticipated level of emission performance as specified in the state plan during the period that the state is relying on state measures. Each of these general SIP types, which may be implemented on a single-state or multi-state basis, may contain many intricacies and variations that are simply unknowable at this time (*e.g.*, mass-based approach, rate-based approach, emission trading programs, etc.).

Q. WHAT HAPPENS IF THE COMMONWEALTH OF KENTUCKY DOES NOT ADOPT AND SUBMIT A SIP?

A. Under the Clean Power Plan, if a state does not submit a SIP, or if the EPA disapproves a state's SIP, then the EPA has the express authority under CAA section 111(d) to establish a federal implementation plan ("FIP") for the state. The nature and terms of a FIP applicable to Kentucky present similar challenges with respect to uncertainty that a possible SIP presents, and it is safe to presume that the EPA may be less aware of and unresponsive to local priorities and statewide needs.

Q. DOES EKPC EXPECT THE CLEAN POWER PLAN TO FACE LEGAL CHALLENGES ONCE IT BECOMES EFFECTIVE?

A. Yes. In fact, EKPC has already joined with energy providers and industry groups throughout the United States to seek judicial review of the Clean Power Plan.[3] The EPA's authority to issue the rule, the rule's conformity with existing statutory law, and the manner in which the rule was devised and issued are just a few of the many issues the judicial system will address in the coming months. Such legal opposition may result in changes to the rule's substantive provisions, a stay with respect to compliance by impacted utilities, and/or the remanding or vacating of the rule. EKPC continues to evaluate the validity and likelihood of success of such legal arguments.

Q. ARE THERE ANY OTHER FACTORS THAT EKPC BELIEVES MAY INFLUENCE THE IMPLEMENTATION OF THE CLEAN POWER PLAN?

A. Yes. Compounding the heretofore described issues of ambiguity that surround the implementation of the Clean Power Plan are the upcoming state and national elections that will occur during the next thirteen (13) months. The leaders chosen and their respective positions regarding energy, the environment, and economic welfare will have a considerable impact on the regulatory climate and enforcement of standards.

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[3] *See National Rural Electric Cooperative Association, at al. v. U.S. Environmental Protection Agency*, No. 15-1376 (D.C. Cir. filed October 23, 2015).

Q. DOES EKPC EXPECT THE CLEAN POWER PLAN TO SIGNIFICANTLY IMPACT ITS BUSINESS AND OPERATIONS?

A. Yes. The Clean Power Plan is perhaps the most important, challenging, costly and impactful environmental regulation faced by EKPC in its history. It will require EKPC to make numerous, important decisions in order to best move forward in the interest of its Owner-Members. Of course, EKPC's unwavering focus is on the provision of reliable and affordable energy. Whether EKPC ultimately determines that it should upgrade its existing EGUs to comply with applicable law (including not only the Clean Power Plan, but CCR, ELG, Ozone NAAQS, and other relevant standards), construct new generation resources, explore power purchase agreements, rely on market purchases, or some combination of these and other options, there can be no doubt that the environmental regulation discussed herein will have an enormous financial impact on EKPC's business in both the near and long term.

Q. WHY IS IT NECESSARY AND PRUDENT TO DELAY IMPLEMENTATION OF A CBS MECHANISM IN LIGHT OF THE CLEAN POWER PLAN?

A. Due to the regulatory landscape in general, and the tremendous uncertainty associated with the Clean Power Plan in particular, EKPC believes it necessary to request an extension of time to file the CBS Mechanism contemplated by the PJM Integration Order. All interested parties recognize that the cost of producing and delivering safe and reliable electricity will increase substantially as a result of stringent environmental regulations; however, until at least some of the many uncertainties described herein are resolved, it is impossible to know the full extent of the financial impact. EKPC expects significant capital outlays in the years to come in order to remain compliant, and it is imprudent and unreasonable at this time to impede EKPC's ability to address forthcoming challenges by requiring the immediate distribution of PJM capacity benefits. Finally, and importantly, whether the capacity benefits earned by EKPC through PJM are immediately returned to Owner-Members through a sharing mechanism or retained by EKPC to maintain affordable wholesale rates and strengthen its equity-to-debt ratio, the primary focus of and beneficiaries under the cooperative model remain the end-consumer.

IV. Conclusions

Q. IS THE REQUESTED DEVIATION NECESSARY, PRUDENT, AND IN THE BEST INTEREST OF EKPC, ITS OWNER-MEMBERS, AND THE ULTIMATE CONSUMERS?

A. Yes. The requested deviation will afford EKPC an opportunity to better develop compliance strategies with respect to the Clean Power Plan and other influential environmental regulations, as well as allow EKPC to gain a better understanding of the regulations' operational and financial impacts on both EKPC and the PJM capacity market at large. Moreover, an 18-month extension will permit EKPC and its Owner-Members additional time to discuss and develop better-aligned rate structures that provide workable solutions to the equitable sharing of benefits and costs, consistent with EKPC's strategic objectives. Finally, the requested temporary postponement of the CBS Mechanism will result in no significant harm, especially considering that other quantitative benefits of EKPC's PJM participation, such as trade benefits, are already largely returned to EKPC's Owner-Members and their retail customers through the utilities' Fuel Adjustment Clauses. For these reasons, EKPC respectfully requests that the Commission grant it permission to deviate from the PJM Integration Order's directive regarding the implementation of a CBS Mechanism and suspend the obligation until May 31, 2017.

Q. DOES THIS CONCLUDE YOUR TESTIMONY?

A. Yes.

COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

THE APPLICATION OF EAST KENTUCKY POWER COOPERATIVE, INC. FOR DEVIATION FROM OBLIGATION RESULTING FROM CASE NO. 2012-00169	) Case No. 2015-_______

VERIFICATION OF DON MOSIER

COMMONWEALTH OF KENTUCKY)
)
COUNTY OF CLARK)

Don Mosier, Executive Vice President and Chief Operating Officer of East Kentucky Power Cooperative, Inc., being duly sworn, states that he has read the foregoing prepared direct testimony and that he would respond in the same manner to the questions if so asked upon taking the stand, and that the matters and things set forth therein are true and correct to the best of his knowledge, information and belief.

Don Mosier

Don Mosier

The foregoing Verification was signed, acknowledged and sworn to before me this 29th day of October, 2015, by Don Mosier.

Gwyn M. Willoughby

NOTARY PUBLIC, Notary # 500144

Commission expiration: 11-30-17

GWYN M. WILLOUGHBY
Notary Public
State at Large
Kentucky
My Commission Expires Nov 30, 2017

COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

THE APPLICATION OF EAST KENTUCKY POWER	)
COOPERATIVE, INC. FOR DEVIATION FROM	) Case No. 2015-_______
OBLIGATION RESULTING FROM CASE NO. 2012-00169	)

DIRECT TESTIMONY OF MIKE MCNALLEY

ON BEHALF OF EAST KENTUCKY POWER COOPERATIVE, INC.

Filed: October 30, 2015

EXHIBIT

tabbies

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I. Introduction

Q. PLEASE STATE YOUR NAME, POSITION, AND BUSINESS ADDRESS.

A. My name is Mike McNalley and my business address is East Kentucky Power Cooperative, Inc. ("EKPC"), 4775 Lexington Road, Winchester, Kentucky 40391. I am Executive Vice President and Chief Financial Officer for EKPC.

Q. PLEASE BRIEFLY DESCRIBE YOUR EDUCATION AND PROFESSIONAL EXPERIENCE.

A. I obtained my undergraduate degree in economics from Reed College in Portland, Oregon, and my Masters of Business Administration from Dartmouth College. Prior to joining EKPC, I held various positions with DTE Energy ("DTE"), including Chief Financial Officer and Chief Operating Officer of one of DTE's subsidiaries, DTE Energy Technologies. Prior to joining DTE, I served as the corporate leader of finance or as a senior executive at various companies including Corrillian Corp., System2, Inc., and Oliver & Thompson, Inc., all located in Portland, Oregon. I have been employed by EKPC since July 2010.

Q. PLEASE BRIEFLY DESCRIBE YOUR DUTIES AT EKPC.

A. I am responsible for accounting, finance, performance measures, pricing and regulatory services, risk management, marketing, information technology, and supply chain at EKPC.

Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY IN THIS PROCEEDING?

A. The purpose of my testimony is to provide an overview of EKPC's recent financial performance and underscore the financial considerations which support EKPC's requested relief in this proceeding.

Q. PLEASE DESCRIBE THE RELIEF REQUESTED BY EKPC IN THIS PROCEEDING.

A. The Kentucky Public Service Commission ("Commission") granted EKPC permission to fully integrate within PJM Interconnection, LLC ("PJM"), by Order entered December 20, 2012, in Case No. 2012-00169 (the "PJM Integration Order"). The PJM Integration Order requires EKPC to take certain actions related to its PJM membership; most notably, EKPC must file, "no later than November 30, 2015, an application for approval of a rate mechanism to flow back to customers the capacity market benefits expected to accrue from membership in PJM." In light of the tremendous uncertainty and potentially massive complications that accompany recent federal environmental regulations, EKPC respectfully requests that the Commission grant it permission to deviate from the PJM Integration Order's directive regarding the implementation of a capacity benefits sharing mechanism ("CBS Mechanism") and suspend the obligation for a period of eighteen (18) months, or until May 31, 2017.

Q. ARE YOU SPONSORING ANY EXHIBITS?

A. No.

II. Overview

Q. PLEASE GENERALLY DESCRIBE EKPC'S FINANCIAL PERFORMANCE DURING THE MOST RECENT YEAR.

A. EKPC has enjoyed several years of improved financial performance as a result of weather patterns, cost control, and benefits from PJM's energy markets. For the year ended December 31, 2014, EKPC had sales of 13,119,594 MWh resulting in total revenue of $952,771,000. EKPC earned a net margin of $64,845,000 and ended the year with $482,553,000 in Members' Equities. EKPC's equity-to-assets ratio was 14.2% in 2014, well on the way to achieving the Board of Directors' goal of a 15% equity-to-assets ratio by the end of 2015. EKPC's Debt Service Coverage (DSC) ratio was 1.30 and its Times Interest Earned Ratio (TIER) was 1.56. EKPC's recent financial performance is indicative of the careful, considered management approach embraced by the cooperative's leadership, and the results have allowed EKPC's Owner-Members to enjoy steady, affordable wholesale rates.

Q. DOES EKPC HAVE A STRATEGIC PLAN CURRENTLY IN PLACE?

A. Yes. Following a Commission-directed management audit, EKPC's Board adopted a Strategic Plan in 2011 that identified various core strategies, including but not limited to pursuing prudent diversity in the fuel mix of the Cooperative's generation portfolio and evaluating new investments using sound financial principles. EKPC has convened Strategic Planning retreats annually since 2011 with the most recent being held in July of 2015. Cornerstones of EKPC's Strategic Plan include financial stability (with a specific emphasis on improving the cooperative's equity ratio) and the appropriate apportionment of costs and benefits through carefully-designed, equitable rates.

III. Delaying Implementation of the CBS Mechanism is Necessary and Prudent

Q. PLEASE EXPLAIN HOW RECENT ENVIRONMENTAL REGULATION IMPACTED EKPC'S DECISION TO PURSUE ITS REQUESTED RELIEF.

A. As the Commission is aware, EKPC must meet numerous challenges presented by increasingly stringent environmental regulation. EKPC is undertaking efforts to evaluate and comply with numerous federal environmental rules which are likely to have future impacts upon the cooperative's ability to generate electricity, most notably the Environmental Protection Agency's recently-finalized Clean Power Plan. As detailed by Mr. Don Mosier, EKPC's Executive Vice President and Chief Operating Officer, the Clean Power Plan is exceedingly complex and may be the most important, challenging, costly and impactful environmental regulations faced by EKPC in its history. Although all interested parties recognize that the cost of producing and delivering safe and reliable electricity will increase substantially as a result of stringent environmental regulations like the Clean Power Plan, there remains tremendous uncertainty as to the Plan's legality, implementation, and extent of impact on EKPC's operations. Until at least some of the many uncertainties associated with the Clean Power Plan are resolved, it is most prudent to delay the implementation of the CBS Mechanism.

Q. DOES EKPC EXPECT THE CLEAN POWER PLAN TO SIGNIFICANTLY IMPACT ITS BUSINESS AND OPERATIONS?

A. Yes. The Clean Power Plan will require EKPC to make numerous, important decisions in order to best move forward in the interest of its Owner-Members. Of course, EKPC's unwavering focus is on the provision of reliable and affordable energy. Whether EKPC ultimately determines that it should upgrade its existing EGUs to comply with applicable law (including not only the Clean Power Plan, but the Coal Combustion Residuals Rule, the Effluent Limitation Guidelines Rule, and other relevant standards), construct new generation resources, explore power purchase agreements, rely on market purchases, or some combination of these and other options, there can be no doubt that the environmental regulation discussed herein will have an enormous financial impact on EKPC's business in both the near and long term.

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COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

THE APPLICATION OF EAST KENTUCKY POWER COOPERATIVE, INC. FOR DEVIATION FROM OBLIGATION RESULTING FROM CASE NO. 2012-00169	) Case No. 2015-_______

VERIFICATION OF MIKE MCNALLEY

COMMONWEALTH OF KENTUCKY)
)
COUNTY OF CLARK)

Mike McNalley, Executive Vice President and Chief Financial Officer of East Kentucky Power Cooperative, Inc., being duly sworn, states that he has read the foregoing prepared direct testimony and that he would respond in the same manner to the questions if so asked upon taking the stand, and that the matters and things set forth therein are true and correct to the best of his knowledge, information and belief.

Mike McNalley

The foregoing Verification was signed, acknowledged and sworn to before me this 29th day of October, 2015, by Mike McNalley.

Gwyn M. Willoughby
NOTARY PUBLIC, Notary # 500144
Commission expiration: 11/30/17

GWYN M. WILLOUGHBY
Notary Public
State at Large
Kentucky
My Commission Expires Nov 30, 2017