EAST KENTUCKY POWER COOPERATIVE

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PUBLIC SERVICE COMMISSION

April 13, 2016

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

VIA HAND DELIVERY

RE: *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 – Third Status Report

Dear Executive Director,

In accordance with the Commission's March 2, 2016 Order in the above-styled case, please accept this as the third status report of East Kentucky Power Cooperative, Inc. ("EKPC") regarding the efforts of EKPC, the Kentucky Industrial Utility Customers, Inc. ("KIUC"), the Attorney General's Office of Rate Intervention ("AG"), and the Commission Staff to reach a consensus on the issue of a flow-back rate mechanism for the PJM Interconnection, L.L.C. ("PJM") capacity market benefits.

Representatives of EKPC, KIUC, the AG, and Commission Staff met at the Commission's Offices in Frankfort on March 17, 2016 for continuing discussions. As noted in the Commission Staff's March 28, 2016 informal conference memorandum, EKPC reviewed two capital credit allocation methodologies it had filed on February 26, 2016 and explained why a third methodology was being provided at the informal conference.

EKPC then reported on discussions with the Rural Utilities Service ("RUS") and the Member Cooperatives' CEOs concerning the idea of a capital credit payment proposal. While not outright rejecting the proposal, RUS suggested that PJM net capacity benefits could be used to fund low-income energy efficiency programs or be placed in a cushion of credit account with RUS, which would earn five percent interest and the interest income would benefit EKPC's customers. Also, EKPC reported that the Member Cooperatives' CEOs did not support the capital credit payment proposal, citing concerns of being directed to pay capital credits, the existence of different capital credit payment methodologies, and potential litigation. The Member Cooperatives' CEOs proposed that the PJM net capacity benefits should instead be utilized to reduce the unamortized balance of the Smith Unit 1 regulatory asset.

In the discussion that followed, EKPC indicated that the option of using the PJM net capacity benefits to reduce the Smith Unit 1 regulatory asset should be comparatively easy to implement and not lead to rate-making problems. Nor was this option likely to trigger the filing

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of a base rate case. EKPC stated it would need to model this alternative to better understand the impact, taking into consideration previous settlement agreements approved in the Smith Unit 1 investigation case, the Smith Unit 1 regulatory asset case, and the 2010 base rate case. EKPC noted that its next board meeting is in early April and it would submit a term sheet with some specificity on the surcharge mitigation alternative by mid-April. EKPC also indicated that it would discuss approaches with KIUC in order to preserve the economic benefits established in the previous settlement agreements. No date was set for the next meeting of the group.

Since the last informal conference, EKPC and KIUC have had several discussions on the surcharge mitigation alternative and how to address the arrangements established in the previous settlement agreements. The discussions have been productive and an agreement has been reached in principle. No definitive agreement has been signed by either EKPC or KIUC. Should the mitigation of the Smith Unit 1 regulatory asset be the path forward, EKPC will likely amend its Application in the present proceeding to accomplish and implement the resolution of the PJM Capacity Market Benefits issues and the Smith Unit 1 Regulatory Asset issues.