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Skill. Integrity. Efficiency.

March 20, 2017

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MAR 21 2017
PUBLIC SERVICE COMMISSION

VIA FEDERAL EXPRESS

Dr. Talina R. Mathews
Executive Director
Public Service Commission
211 Sower Boulevard, P.O. Box 615
Frankfort, Kentucky 40602-0615

Re: *In the Matter of: Application of Big Rivers Electric Corporation for a Declaratory Order*
Case No. 2016-00278

Dear Dr. Mathews:

Enclosed for filing on behalf of Big Rivers Electric Corporation are an original and ten copies of Reply Brief of Big Rivers Electric Corporation.

I certify that on this date, a copy of this letter and a copy of all the enclosures were served on all persons listed on the attached service list by first-class mail and electronic mail. Please feel free to contact me if you have any questions.

Sincerely yours,

James M. Miller
Counsel for Big Rivers Electric Corporation

JMM/abg

Enclosures

cc: Service List

Service List
PSC Case No. 2016-00278

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COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

RECEIVED
MAR 21 2017
PUBLIC SERVICE COMMISSION

In the Matter of:

APPLICATION OF BIG RIVERS ELECTRIC CORPORATION FOR A DECLARATORY ORDER	)))	**Case No. 2016-00278**

REPLY BRIEF OF

BIG RIVERS ELECTRIC CORPORATION

March 21, 2017

1 COMMONWEALTH OF KENTUCKY
2 BEFORE THE PUBLIC SERVICE COMMISSION
3
4
5 In the Matter of:
6
7 APPLICATION OF BIG RIVERS ELECTRIC)
8 CORPORATION FOR A DECLARATORY) CASE NO. 2016-00278
9 ORDER)
10
11
12 **REPLY BRIEF OF BIG RIVERS ELECTRIC CORPORATION**

13 Big Rivers Electric Corporation ("Big Rivers"), by counsel, for its reply brief before the
14 Kentucky Public Service Commission (the "Commission") and in response to the Post-Hearing
15 Brief of the City of Henderson, Kentucky, and the City of Henderson Utility Commission d/b/a
16 Henderson Municipal Power & Light (collectively, "Henderson"), states as follows:

17 **I. Introduction.**

18 Henderson argues in its brief (i) that "[t]he Commission does not have jurisdiction to
19 grant the relief Big Rivers requests," and (ii) that "Big Rivers should bear the losses associated
20 with a soft energy market." Henderson's Post-Hearing Brief at pp. 4, 11. For the reasons
21 explained below, Henderson is wrong on both counts.

22 **II. The Commission has jurisdiction to grant the relief Big Rivers requests.**

23 Henderson fails to reconcile its position that the Commission does not have jurisdiction
24 to grant the relief Big Rivers requests with the statute that clearly grants the Commission that
25 jurisdiction. *See* Henderson's Post-Hearing Brief at pp. 4-11. As discussed in Big Rivers' brief,
26 KRS 278.200 expressly grants the Commission jurisdiction over the rate and service terms of the
27 Power Sales Contract. Big Rivers' Post-Hearing Brief at pp. 3-9. Henderson inexplicably
28 avoids addressing the authority granted to the Commission by this statute. Instead, Henderson

1 bases its argument on unsupported conclusory statements and citations to the record and to
2 authorities that do not support or contradict the propositions for which Henderson cited them.

3 **A. Henderson misconstrues Kentucky Supreme Court case law.**

4 Henderson claims, "The Kentucky Supreme Court has held that, where, as here, the sole
5 issue is a matter of contract interpretation, jurisdiction lies with the courts of the Commonwealth,
6 and not with the Commission." Henderson's Post-Hearing Brief at p. 4. In support of this
7 assertion, Henderson cites *Simpson County Water Dist. v. City of Franklin*, 872 S.W.2d 460 (Ky.
8 1994) and *Carr v. Cincinnati Bell, Inc.*, 651 S.W.2d 126 (Ky. App. 1983). However, neither
9 case stands for the proposition asserted by Henderson.

10 *Simpson County Water Dist.* involved a Water Purchase Agreement whereby the City of
11 Franklin provided treated water to the Simpson County Water District. *Simpson County Water
12 Dist.*, 872 S.W.2d at 461. Years after the parties entered into the Water Purchase Agreement, the
13 city passed two ordinances increasing the rate it charged the water district for treated water. *Id.*
14 The water district refused to pay the rates called for by the ordinances, and the city sued in
15 circuit court for delinquent payments and a declaratory judgment that the Water Purchase
16 Agreement was void. *Id.*

17 The Kentucky Supreme Court held that KRS 278.200 was clear in vesting the
18 Commission with the exclusive jurisdiction over "any contract as to rates and service arising
19 between a city and a utility," including the subject Water Purchase Agreement. *Id.* at 462-63.
20 The Court did not hold that had the matter involved only the interpretation of a contract between
21 a city and a utility, jurisdiction would have been in the circuit court, although it did note that
22 courts and not regulatory bodies have expertise in contract interpretation. *See id.* at 464. The
23 Court's ruling did not turn on whether the issue involved contract interpretation, but rather on

1 whether the Commission or the courts had been vested with jurisdiction to decide the issue
2 presented. *See id.*
3 In *Carr*, a customer sued his telephone utility demanding both (i) an injunction requiring
4 the utility to provide him a telephone number and tariff-free telephone service in another county,
5 and (ii) damages for breach of contract. *Carr*, 651 S.W.2d at 126. The Kentucky Court of
6 Appeals held that the Commission had exclusive jurisdiction over the customer's demand for a
7 telephone number and tariff-free service since that claim "has to do with the type and quality of
8 service," but the Court held that KRS Chapter 278 did not delegate to the Commission the
9 authority to adjudicate contract claims for unliquidated damages. *Id.* at 128. *Carr* does not
10 reference the interpretation of contracts at all. Instead, "the Court's decision was based on an
11 analysis of whether the complaint involved issues within the Commission's jurisdiction, i.e.,
12 service, not an analysis of whether the issues were purely a private concern to one customer" or
13 whether the issues involved contract interpretation. *In the Matter of: The Reasonableness of*
14 *Delayed Payment Charges Pursuant to Various Tariffs of Kentucky Power Co. d/b/a Am. Elec.*
15 *Power with Respect to Late Payments by AK Steel Corp.*, Order, P.S.C. Case No. 2000-062
16 (Aug. 31, 2000). Moreover, *Carr* did not involve a contract between a city and a utility, did not
17 reference KRS 278.200, and was silent on the Commission's authority under that statute.

18 **B. The Commission has jurisdiction over the rate and service terms of the**
19 **Power Sales Contract.**

20 Henderson argues that the Power Sales Contract "is unrelated to rates or service. Thus,
21 the nature of the parties' contractual relationship is exempt from Commission regulation."
22 Henderson's Post-Hearing Brief at p. 5. Henderson explains that "[n]othing in the agreement
23 establishes rates for utility service, or parameters for the delivery of such service. Nothing in the
24 agreement calls for either party to furnish utility service to the other, or to pay or collect a rate in

1 compensation for such service." *Id.* at p. 6. Henderson ignores that the nature of the agreement

2 here is a *Power Sales* Contract, pursuant to which Henderson is providing a service to Big Rivers

3 in the form of the supply of energy, and that Big Rivers is purchasing that energy. For example,

4 Section 1.3 of the Power Sales Contract[1] provides:

> 5 Big Rivers, which is a public utility in this state whose rates and services are
> 6 regulated by the Kentucky Public Service Commission, is desirous of *purchasing*
> 7 *the surplus power and energy from time to time available from City's municipal*
> 8 *electric system, including its proposed Station Two*, and is willing to execute and
> 9 fulfill the terms of this Agreement entitling it to take, and obligating it to pay for
> 10 such surplus electric power and energy, subject to the terms and conditions recited
> 11 herein. (Emphasis added).

12 Section 1.4 similarly provides, "By its addition of Station Two, City will be able to provide more

13 economical and reliable electric service to itself and its inhabitants, and through its *sales of*

14 *surplus electric power and energy to Big Rivers*, as provided by this Agreement, City can assure

15 economic feasibility of such addition" (emphasis added).

16 The Power Sales Contract provides the parameters for the service provided to Big Rivers

17 by Henderson. For example, Section 7.1 of the agreement provides, "Service to Big Rivers from

18 City's Station Two shall be at 161KV, 3 phase 60 cycles, unless otherwise agreed upon by the

19 parties." And Section 8 addresses metering, meter testing, and billing adjustments.

20 Additionally, the Power Sales Contract sets forth the amount Big Rivers pays Henderson

21 for energy. Under the Power Sales Contract, as amended by the arbitration award, the energy

22 associated with Henderson's capacity reservation that is in excess of the needs of Henderson and

23 its inhabitants (the "Excess Henderson Energy" or "EHE") belongs to Henderson, and

24 Henderson has certain rights to sell that energy to third parties, subject to Big Rivers' right of

25 first refusal. *See* Big Rivers' Post-Hearing Brief at p. 10 (noting Big Rivers' right of first

26 refusal); *id.* at p. 11 ("The Arbitration Award made clear that the EHE 'shall be considered to

---

[1] The Power Sales Contract is attached as Exhibit 1 to Big Rivers' Application.

belong to [Henderson],' and Henderson has acknowledged that the EHE belongs to it") (footnotes omitted). If Henderson receives a firm bona fide third party offer for EHE, Big Rivers can purchase that energy from Henderson by paying Henderson the offer price. *Id.* at p. 5. If Henderson does not receive a firm bona fide third party offer, Big Rivers can elect to take the EHE by paying the variable costs used to produce that energy and by paying Henderson $1.50/MWh for any energy so taken. *Id.*

The provision of the energy that Big Rivers purchases from Station Two, including the EHE Big Rivers elects to take, is a service, and the amount Big Rivers pays Henderson for that power is a rate. Big Rivers' Post-Hearing Brief at pp. 3-9. A "rate" is compensation paid for service. KRS 278.010(12). Henderson fails to distinguish the EHE Big Rivers takes, the allocation of the variable costs to Big Rivers for the energy Big Rivers takes, or the payments to Henderson for the energy Big Rivers takes from the rates for service over which the Commission has jurisdiction under KRS 278.200. For example, Henderson makes no attempt to distinguish how the City of Franklin providing treated water under a Water Purchase Agreement is any different from Henderson providing EHE to Big Rivers under a Power Sales Contract. Henderson's unsupported conclusory statements that rates and service are not involved here do not make it so.

1. <u>The standard Henderson relies upon is incorrect</u>.

Henderson cites *Bee's Old Reliable Shows, Inc. v. Kentucky Power Co.*, 334 S.W.2d 765 (Ky. 1960), for the proposition that the Kentucky Supreme Court has limited the Commission's jurisdiction to the "regulation of rates for 'usual service rendered to the public generally.'" Henderson's Post-Hearing Brief. But *Bee's Old Reliable Shows, Inc.* has been superseded on that point. *Bee's Old Reliable Shows, Inc.* was issued when KRS Chapter 278 required ten

1 customers for the Commission to have jurisdiction over a complaint, and KRS Chapter 278 has

2 since been amended to vest the Commission with jurisdiction over individual complaints, as the

3 Commission has explained:

> 4 Apparently, out of concern that the number of individual customers filing
> 5 complaints against utilities over rates and service could result in conflicting
> 6 decisions and interpretations for utilities that operate in numerous counties, the
> 7 General Assembly amended KRS 278.260(1) in 1982. The requirement for 10
> 8 persons was eliminated, thus authorizing Commission jurisdiction over a
> 9 complaint by just one person. The complaint statute now provides, in pertinent
> 10 part, as follows:
>
> > 11 The Commission shall have original jurisdiction over complaints
> > 12 as to rates and service of any utility, and upon a complaint in
> > 13 writing made against any utility by any person . . . the commission
> > 14 shall proceed, with or without notice, to make such investigation as
> > 15 it deems necessary or convenient.
>
> 16 KRS 278.260(1) (emphasis added).
>
> 17 Subsequently, in *Carr v. Cincinnati Bell, Inc.*, 651 S.W.2d 126, one customer
> 18 filed an action in circuit court against a telephone utility seeking a change in
> 19 service and damages for breach of contract. The circuit court dismissed both
> 20 claims for lack of jurisdiction, finding jurisdiction rested in the Commission. The
> 21 Court of Appeals reversed the dismissal on the claim for damages, holding that
> 22 the Commission lacked jurisdiction "to adjudicate contract claims for
> 23 unliquidated damages." *Id.* at 128. However, the Court affirmed the dismissal on
> 24 the claim for a change in utility service, holding such claim to be within the
> 25 Commission's exclusive jurisdiction as relating to "the type and quality of
> 26 service." *Id.* Significantly, the Court's decision was based on an analysis of
> 27 whether the complaint involved issues within the Commission's jurisdiction, i.e.,
> 28 service, not an analysis of whether the issues were purely a private concern to one
> 29 customer.

30 *In the Matter of: The Reasonableness of Delayed Payment Charges Pursuant to Various Tariffs*

31 *of Kentucky Power Co. d/b/a Am. Elec. Power with Respect to Late Payments by AK Steel Corp.*,

32 Order, Case No. 2000-062 (Aug. 31, 2000). The Commission now regularly exercises its

33 jurisdiction over individual contracts, and it has exercised its jurisdiction over the very contracts

34 at issue in this case. *See* Big Rivers' Post-Hearing Brief at p. 3. Moreover, *Bee's Old Reliable*

Shows, Inc. did not involve a contract between a utility and a city, KRS 278.200 or the extent of the Commission's jurisdiction over contracts between a city and a utility under that statute.

2. The Power Sales Contract involves service over which the Commission has jurisdiction.

Henderson argues that the Power Sales Contract does not involve the kind of service over which the Commission has jurisdiction by claiming that "Big Rivers concedes that the approval or denial of its application will not impact the quantity or quality of service to its customers." Henderson's Post-Hearing Brief at p. 7. But Henderson completely ignores the fact that this case directly impacts the quantity of EHE that Big Rivers purchases from Henderson. *See* Big Rivers' Post-Hearing Brief at pp. 4-5. In *Benzinger v. Union Light, Heat & Power Co.*, the Kentucky Court of Appeals, then the Commonwealth's highest court, explained that the service over which the Commission had exclusive jurisdiction included the quality and quantity of the product to be served:

> The first section of the Public Service Commission Act is definitive, among which are definitions of "facility" or "facilities" and a definition of "service" as employed in the act. In the latter definition it says that the word "service" is used in its broadest and most inclusive sense, including practice or requirements relating to the service, "including the voltage of electricity; the heat units and pressure of gas, the purity, pressure and quantity of water, and in general the *quality, quantity* and pressure of any commodity or product used or to be used for or in connection with the business of any utility." (Our emphasis) Our interpretation of that language is, that the legislature only intended for the word "service" to apply to and comprehend "quality" and "quantity" of the product to be served, and to that end for the word to also include and comprehend any part of the facility of the utility that bottle–necked the required service of quantity and quality; but did not transfer jurisdiction on the commission over other portions of facilities which did not obstruct, prevent or interfere with the quality and quantity of the furnished product. Therefore, when any controversy relating to quantity and quality—preferred either by the municipality against the utility, or by a customer of the latter—the commission was given exclusive jurisdiction of that question, including the further jurisdiction over facilities insofar as any part thereof might obstruct or curtail quality or quantity of the furnished product.

Benzinger v. Union Light, Heat & Power Co., 293 Ky. 747, 170 S.W.2d 38, 41 (1943) (emphasis in original); *see also Simpson Cty. Water Dist.*, 872 S.W.2d at 464 ("Also, the service regulation over which the Commission was given jurisdiction refers clearly to the quantity and quality of the commodity furnished as contracted for with the facilities provided"). The Court determined in *Benzinger* that the Commission did not have jurisdiction because there was not even an allegation that the quality or quantity of energy would be affected. *Benzinger*, 170 S.W.2d at 42. Here, however, one issue is precisely the quantity of energy Big Rivers is required to take and pay for under the Power Sales Contract.

3. The Power Sales Contract involves rates over which the Commission has jurisdiction.

While ignoring the Commission's jurisdiction over the service terms of the Power Sales Contract, Henderson spends several pages of its brief arguing that the Power Sales Contract does not involve a rate over which the Commission has jurisdiction. *See* Henderson's Post-Hearing Brief pp. 7-10. Henderson claims (i) that requiring Big Rivers to be responsible for the variable costs of the unwanted EHE does not "constitute rates nor bear any relationship to any disputed rate Big Rivers has identified" because "the variable costs are, of course, the result of Big Rivers' decisions to generate energy whether it is economic or not;" (ii) that any impact on Big Rivers' fuel adjustment clause ("FAC") is "attributable to the increased volume of energy Big Rivers opts to generate, and not the natural fluctuation in fuel prices that the [FAC] was designed to accommodate;" and (iii) that any impact on Big Rivers' rates to its members is unknown and speculative. Henderson's Post-Hearing Brief at pp. 7-8, 10.

First, Big Rivers has fully addressed Henderson's claim that Big Rivers chooses to generate the unwanted EHE. *See* Big Rivers' Post-Hearing Brief at pp. 17-22. In its brief, Big Rivers showed, for example, that the record was "replete with examples of how Henderson

1 exerts significant control over the operation of Station Two, demanding that Big Rivers operate
2 both Station Two units continuously even when the cost of operating the units exceeds the price
3 of energy in the market, and threatening to sue Big Rivers for merely suggesting that there is a
4 more prudent way to operate the units." *Id.* at p. 18. Rather than challenge this evidence,
5 Henderson simply reiterates its baseless allegation that Big Rivers chooses to generate the
6 unwanted EHE.

7 Second, the question of which party is responsible for the variable costs of the unwanted
8 EHE clearly involves a rate dispute requiring the Commission's intervention. The allocation of
9 costs relating to the sale of power in a contract between a utility and a city is a rate over which
10 the Commission has jurisdiction. *See In the Matter of: Forest Creek, LLC v. Jessamine-South*
11 *Elkhorn Water District*, Order, P.S.C. Case No. 2011-00297, at 8 (Mar. 16, 2012) ("On its face,
12 Forest Creek's complaint involves matters within the Commission's jurisdiction. It involves
13 procedures for the design and construction of water main extensions and for the allocation and
14 payment of the cost of such extensions"). There is a dispute in this case over which party should
15 be required to bear the variable costs of the unwanted EHE. The Commission thus has
16 jurisdiction to determine which party is and should be responsible for the variable costs of the
17 EHE that Henderson requires be generated and that Big Rivers does not want.

18 Third, Big Rivers' base rates and FAC charges to its member distribution cooperatives,
19 and their rates and FAC charges to their retail member-customers, will necessarily be impacted if
20 Big Rivers must pay the variable costs of, and pay Henderson $1.50/MWh for, EHE that is
21 uneconomic and that Big Rivers does not want. *See* Big Rivers' Post-Hearing Brief at pp. 7-8.
22 In *Simpson Cty. Water Dist.*, the Kentucky Supreme Court noted that costs that decrease a

utility's revenue directly affect the rates the utility charges its customers and thus implicate the Commission's jurisdiction to insure the utility's rates to its customers are fair:

> Jurisdiction to regulate [a utility's] rates and service has been exclusively vested in the PSC. The record in this case discloses a doubling of the wholesale water rates charged to the District within a two-year period, with a direct impact upon the District's utility rates and service . . . It is apparent that the City, through its enhanced water sale ordinances, did not direct the setting of any particular rate schedule, but its action profoundly and directly impacts the District's general revenue level, which is one of the first steps in rate making.
>
> . . .
>
> The City's unilateral adoption of the two water-rate ordinances doubled the water charge and, in no uncertain terms, was an act that directly related to the rate charged by the water district . . . The manifest purpose of the Public Service Commission is to require and insure fair and uniform rates, prevent unjust discrimination, and prevent ruinous competition.

Simpson Cty. Water Dist., 872 S.W.2d at 464; *see also id.* at 465 ("The rates and service exception effectively insures, throughout the Commonwealth, that any water district consumer/customer that has contracted and become dependent for its supply of water from a city utility is not subject to either excessive rates or inadequate service"); *Benzinger*, 170 S.W.2d at 41 ("Therefore, when any controversy relating to quantity and quality—preferred either by the municipality against the utility, or by a customer of the latter—the commission was given exclusive jurisdiction of that question, including the further jurisdiction over facilities insofar as any part thereof might obstruct or curtail quality or quantity of the furnished product").

Although the exact amount of the impact on Big Rivers' and its members' base rates and FAC charges cannot be known at this time because it depends on future events, such as the amount of EHE that is uneconomic in the future, the cost to produce it in the future, and the market price in the future, Big Rivers has calculated that it would have lost approximately $3.4 million if it had been required to take all of the uneconomic EHE in 2016. *See* Big Rivers' Post-Hearing Brief at p. 8; Big Rivers' response to Item 1 of Henderson's First Request for

1 Information. Henderson has not disputed that calculation. Moreover, although the exact effect
2 on future rates cannot be known at this time, it is certain that Big Rivers will be subject to
3 increased costs if it is required to take and pay for uneconomic EHE that it does not want, and as
4 noted in *Simpson Cty. Water Dist.*, those increased costs will have a direct effect on Big Rivers'
5 base rates to its members. Likewise, changes to Big Rivers' rates to its members will affect their
6 net revenues and have a direct impact on their base rates to their retail customers.

7 Requiring Big Rivers to take and pay for uneconomic EHE that it does not want will also
8 affect its and its members' FAC charges. As Big Rivers described in its responses to information
9 requests, "Because the Station Two units are generally higher cost units, the greater Big Rivers'
10 take from Station Two, the greater the impact of Station Two's costs on Big Rivers system
11 average fuel costs. Those system average fuel costs are used to determine Big Rivers' FAC
12 charges to its members. Thus, if Big Rivers is required to take the uneconomic Excess
13 Henderson Energy, its FAC charges to its members will generally be greater than they would
14 have been had Big Rivers been able to exercise its contractual right not to take such
15 energy." Big Rivers' response to Item 1 of Henderson's First Request for Information; *see also*
16 Hearing Transcript 10:15'05" - 10:15'40". Higher FAC charges to Big Rivers' members will
17 cause their FAC charges to their retail customers to also be higher.

18 4. The Indemnification Agreement is irrelevant to whether the Power
19 Sales Contract involves rates over which the Commission has
20 jurisdiction.

21 Henderson, for the first time, contends at page 10 of its Post-Hearing Brief that the
22 impact of the cost to Big Rivers of producing unwanted EHE is recoverable by Big Rivers from
23 WKEC under the Indemnification Agreement, which was filed under a petition for confidential
24 treatment as an attachment to Big Rivers' response to Item 25 of Henderson's Second Request

for Information. In doing so, Henderson profoundly misrepresents what Mr. Berry said in the hearing and the contents of the Indemnification Agreement.

Rather than "affirm" Henderson's theory, at the hearing Mr. Berry pointed out that the Indemnification Agreement formula for calculation of EHE only applies if Big Rivers ***takes*** the energy. Transcript 10:27. The issue before the Commission involves only the variable production costs of energy that Big Rivers does ***not*** want to take.

Likewise, the Indemnification Agreement applies only to EHE that Big Rivers wants to purchase and either cannot purchase or cannot purchase at the price stated in Section 3.8(c) of the Power Sales Contract. In fact, the Indemnification Agreement expressly excludes variable production costs from the indemnified costs available to Big Rivers. *See* Indemnification Agreement, Sections 2.1(b)(1) and 2.3(c) regarding "Associated Variable Costs." There is no support for Henderson's theory.

5. Henderson fails to recognize that KRS 278.200 expressly grants the Commission jurisdiction over rates for power provided by a municipality to a utility.

Henderson additionally argues that the $1.50/MWh that Big Rivers pays Henderson is not a rate because Big Rivers is not a customer of Henderson, claiming, "By statute, a rate is compensation for service rendered to a utility customer. KRS 278.010(12). In the case at bar, Big Rivers is not a customer of Henderson, and Big Rivers has cited no rate that is or has been imposed, changed, or modified by Henderson." Henderson's Post-Hearing Brief at pp. 8-9.

Once again, Henderson completely ignores the authority granted the Commission by KRS 278.200. The Court in *Simpson County Water Dist.* made clear that the authority granted the Commission by KRS 278.200 applied not only when the utility was the provider of the commodity but also when the city was the provider of the commodity. *See Simpson Cty. Water*

1 *Dist.*, 872 S.W.2d at 462. Under the Power Sales Contract, Henderson provides power to Big
2 Rivers, and Big Rivers compensates Henderson for that power. KRS 278.200 grants the
3 Commission jurisdiction over the rates in the Power Sales Contract, as well as "all rights,
4 privileges and obligations arising out of" the Power Sales Contract. KRS 278.200. Thus, the
5 amount Big Rivers pays Henderson for power is a rate subject to the Commission's jurisdiction.
6 *See In the Matter of: Forest Creek, LLC v. Jessamine-South Elkhorn Water District*, Order,
7 P.S.C. Case No. 2011-00297, at 8 (Mar. 16, 2012) ("On its face, Forest Creek's complaint
8 involves matters within the Commission's jurisdiction . . . Moreover, the Interim Water Service
9 Agreement clearly relates to the provision of utility service. It sets out fees that Forest Creek
10 must pay as a condition for obtaining the extension of service. It provides the procedures for
11 which the plans for the proposed water main extension will be reviewed, defines Forest Creek's
12 responsibilities and obligations during all phases of the extension and upon completion of the
13 main extension, and establishes general design specifications for the water main extension. It
14 further addresses Forest Creek's right to any refunds from the cost of the water main extension").

15 6. The Commission's jurisdiction over rates extends to whether Big
16 Rivers should or should not be required to pay Henderson $1.50/MWh
17 for the EHE Big Rivers elects not to take.

18 Henderson asserts that even if the $1.50/MWh that Big Rivers pays Henderson for any
19 EHE Big Rivers elects to take is a rate, "the Commission is still without jurisdiction because the
20 rate remains unchanged." Henderson's Post-Hearing Brief at p. 9. But the issues in this case
21 include: (i) whether Big Rivers is required under the Station Two Contracts to be responsible for
22 the variable costs, and to pay Henderson $1.50/MWh for, EHE that Big Rivers does not want,
23 and (ii) if so, whether such requirements are fair, just, and reasonable. In other words, Big
24 Rivers asks the Commission to declare that Big Rivers pays nothing for the variable costs of, and

pays Henderson $0 for, the production of any EHE Big Rivers elects not to take. Henderson, on the other hand, wants Big Rivers to pay all of the variable costs of, and pay Henderson $1.50/MWh for, that EHE. Henderson cannot logically acknowledge that the $1.50/MWh may be a rate, but then still claim that the Commission does not have jurisdiction to determine whether the Power Sales Contract requires or should require Big Rivers to pay that rate.

7. The arbitration proceeding was not a concession that the Power Sales Contract does not involve rates over which the Commission has jurisdiction.

Henderson further interjects a convoluted argument that:

> Big Rivers nonetheless failed to adjudicate the issue it now brings before the Commission . . . If Big Rivers reasonably believed the $1.50 payment to be a rate, then Big Rivers would have made that assertion and brought the issue before the Commission in 2009 . . . By seeking referral of the dispute to arbitration rather than bringing the issue before the Commission, Big Rivers conceded that the $1.50 payment is not a rate subject to Commission jurisdiction.

Henderson's Post-Hearing Brief at pp. 9-10. The record is devoid of support for this new argument raised by Henderson. Responsibility for the variable production costs of unwanted EHE was not an issue in the arbitration, and so, whether Big Rivers was required to pay Henderson $1.50/MWh for EHE that Big Rivers did not want was neither raised nor addressed by the arbitration panel. *See* Application Exhibit 9 (the arbitration award). As shown in detail above, subject matter jurisdiction over the issues presented is conferred in the Commission by KRS 278.200 and the related court decisions. Henderson presents no legal or factual nexus between the act of filing the arbitration proceeding and its unsupported argument that Big Rivers has conceded that the Power Sales Contract does not involve rates over which the Commission has jurisdiction. Subject matter jurisdiction cannot be waived. *Com., Dep't of Highways v. Berryman*, 363 S.W.2d 525, 526–27 (Ky. 1962). Henderson's attempts to characterize the

variable costs and the $1.50/MWh Big Rivers pays for the EHE that Big Rivers takes as something other than rates over which the Commission has jurisdiction should be rejected.

C. The Commission's exercise of jurisdiction in this case does not violate KRS 278.040(2).

Henderson claims that "an exercise of Commission jurisdiction in this instance would violate the prohibition of KRS 278.040(2) against the infringement of a city's contract rights." Henderson's Post-Hearing Brief at p. 11. The Kentucky Supreme Court rejected this argument in *Simpson County Water Dist.*:

> The second sentence of KRS 278.040(2) is the "exception" to the general rule which exempts cities from PSC regulation. It provides:
>
> > The commission shall have *exclusive jurisdiction* over the regulation of *rates* and *service* of utilities, but with that *exception* nothing in this chapter is intended to limit or restrict the police jurisdiction, contract rights or powers of *cities* or political subdivisions. (Emphasis added).
>
> Thus, when a city is involved, the sentence reflects unequivocally the legislature's intent that the PSC exercise exclusive jurisdiction over utility rates and service.
>
> . . .
>
> We find that where contracts have been executed between a utility and a city, such as between the City of Franklin and Simpson County Water District, KRS 278.200 is applicable and requires that by so contracting the City relinquishes the exemption and is rendered subject to PSC rates and service regulation.

Simpson Cty. Water Dist., 872 S.W.2d at 462-63 (emphasis in original).

Based on the foregoing and on Big Rivers' brief, the Commission should find that it has jurisdiction to grant the relief requested by Big Rivers in this matter.

III. The Commission should grant the relief requested by Big Rivers.

Henderson's argues that "Big Rivers should bear the losses associated with a soft energy market, just as it reaped profits when market conditions were favorable." Henderson's Post-

1 Hearing Brief at p. 11.[2] For the reasons stated below, the Commission should reject this
2 argument and instead grant the relief requested by Big Rivers.

3 **A. Henderson fails to address the fact that the Station Two Contracts**
4 **require Henderson to be responsible for the variable production costs of**
5 **EHE that Big Rivers elects not to take.**

6 Henderson does not address Big Rivers' arguments in its brief that the Station Two
7 Contracts require Henderson to be responsible for the variable costs of the EHE that Big Rivers
8 elects not to take, beyond an unsupported statement on page 12 that the Power Sales Contract
9 does not address responsibility for the variable costs of uneconomic EHE. Big Rivers and
10 Henderson are separately responsible for the costs associated with their capacity share and for
11 the variable costs associated with the energy each of them uses in a given hour, which includes
12 the obligation that each party must replace at its cost all fuels and reagents consumed for the
13 energy used by that party. Big Rivers' Post-Hearing Brief at pp. 9-10. Because each party is
14 responsible under the Station Two Contracts for the variable costs associated with the energy
15 taken by that party, Big Rivers is responsible for the variable production costs of, and is required
16 to pay Henderson for, any EHE Big Rivers elects to take. *Id.* at 10. However, as even
17 Henderson admits, Big Rivers has no obligation to take any EHE under the Power Sales
18 Contract. *Id.* The arbitration award made clear that the EHE "shall be considered to belong to
19 [Henderson]," and Henderson has acknowledged that the EHE belongs to it. Application Exhibit
20 9 (the arbitration award), p. 3; Big Rivers' Hearing Exhibit 8, p. 184:21. Since EHE belongs to

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[2] Henderson has never acknowledged that if Big Rivers receives the relief requested from the Commission, Big Rivers will still bear the burden of the variable production costs of energy within Big Rivers' capacity allotment that Henderson requires Big Rivers to generate even when doing so is uneconomic. Big Rivers is only asking that Henderson be responsible for the production costs of energy within its capacity reservation.

1 Henderson, and since Big Rivers is not required to take any EHE, the EHE not taken by Big
2 Rivers necessarily must be taken and paid for by Henderson.

3 **B. Even if the Station Two Contracts did not already require Henderson to**
4 **be responsible for the variable production costs of the uneconomic EHE,**
5 **Henderson requires that the uneconomic EHE be generated and should**
6 **therefore bear the costs incurred to produce it.**

7 Henderson's argument boils down to its assertion that "[i]f either party is to bear the
8 losses associated with an anemic energy market, then it should be the party that enjoyed the
9 benefit when market conditions were favorable." Henderson's Post-Hearing Brief at p. 13.
10 There are four main problems with Henderson's argument. First, although Big Rivers has taken
11 the economic EHE in the past, Big Rivers did so pursuant to a contractual right. The Power
12 Sales Contract grants Big Rivers the right but not the obligation to take any or all of the EHE not
13 sold by Henderson to third parties. Henderson has previously agreed that it cannot make Big
14 Rivers take any EHE, yet if Big Rivers is required to bear the costs of the unwanted EHE, Big
15 Rivers' contractual option would be turned into a take or pay obligation. Big Rivers should not
16 be punished for exercising a contractual right. *See* Big Rivers' Post-Hearing Brief at pp. 10-11.
17 Second, although Henderson claims Big Rivers has benefited from taking the EHE in the
18 past, Henderson has sued Big Rivers to recover all of those benefits, and then some.
19 Third, Henderson requires the uneconomic EHE to be generated, and Henderson should
20 therefore bear the costs of that decision. *See id.* at pp. 17-22.
21 Fourth, although Big Rivers has taken the economic EHE in the past, Henderson will
22 receive the economic EHE in the future. The EHE belongs to Henderson, Henderson has the
23 right to sell that energy to third parties, Henderson asserts that it wants to take and sell that
24 energy, and Henderson will sell the EHE to third parties when it is economic to do so. The only
25 real impediment to Henderson taking the economic EHE is Henderson's unreasonable refusal to

work with Big Rivers to develop a commercially complete scheduling protocol. *See id.* at pp. 11, 24-26; Rebuttal Testimony of Robert W. Berry at pp. 25-27.

Thus, Henderson will receive the benefits of the economic EHE in the future, and has sued Big Rivers to recover the benefits of the economic EHE in the past. Plus, it is only because of Henderson's insistence that the Station Two units be run continuously that the uneconomic EHE is generated. It would therefore not be fair, just, and reasonable to impose the variable costs incurred to produce the uneconomic EHE on Big Rivers or to require Big Rivers to pay Henderson $1.50/MWh for the uneconomic EHE.

C. Henderson's argument is based on untrue or unsupported statements.

Henderson relies on untrue or unsupported statements throughout its argument. For example, the second sentence in Henderson's argument asserts that Big Rivers has "refus[ed] to approve a protocol that would have allowed Henderson to schedule its energy for sale to third parties." Henderson's Post-Hearing Brief at p. 11. But as Big Rivers explained in detail in its brief, with supporting evidence from the record, Big Rivers has asked Henderson on more than one occasion for a commercially complete scheduling protocol; that since Henderson would not propose such a protocol, Big Rivers drafted and sent Henderson a complete protocol incorporating new terms proposed by Henderson's consultant, which Henderson rejected, saying no additional terms were needed; and that Henderson refuses to meet with Big Rivers to work out a complete protocol. *See* Big Rivers' Post-Hearing Brief at pp. 24-26. Henderson makes no attempt to refute the evidence in the record or to rebut Big Rivers' argument on these points. If Henderson would sit down with Big Rivers and negotiate a commercially-reasonable protocol, it would put itself in position to "reap the profits" from EHE when the variable production costs of EHE are less than the market price of energy.

The third sentence in Henderson's argument states that "Big Rivers now seeks to deprive Henderson of the right to decline the generation and sale of unprofitable excess energy." Henderson's Post-Hearing Brief at p. 12. As noted above, Big Rivers' brief demonstrates by reference to evidence in the record that it is Henderson that requires the Station Two units to operate continuously and threatened to sue Big Rivers for even suggesting that the units be run on an economic commitment basis. In a logic-defying tangle of positions, Henderson requires Big Rivers to generate unprofitable excess energy from Station Two and simultaneously accuses Big Rivers of seeking to deprive Henderson of the "right to decline the generation and sale of unprofitable excess energy."

Henderson goes on to state, "[I]t is not Henderson that imposes the requirement of continuous operation. Rather, it is the Power Sales Agreement [sic] itself that makes continuous operation mandatory." *Id.* at p. 12. But in reality, the Station Two Contracts require only that Big Rivers provide "all operating personnel, materials, supplies and technical services required for the continuous operation of City's Station Two." Power Plant Construction and Operation Agreement (Application Exhibit 2), Sections 13.2 and 13.4. What Big Rivers has "covenanted and agreed" to do in the Station Two Contracts is to "at all times operate the City's Station Two on a best efforts basis, in an efficient and economical manner . . . ." *Id.* Thus, the Station Two Contracts provide for the Station Two units to be operated "in an efficient and economical manner" rather than to be run continuously.

Henderson has not shown, and cannot show, that the existing terms of the Station Two Contracts require Big Rivers to operate both Station Two units on a continuous basis in an uneconomical manner. Nor do the "engineering requirements" of Station Two (See Henderson Brief, page 12) require the production of unwanted and uneconomic EHE. The only obstacle to

operation of Station Two on an economical basis is Henderson's policy of forcing continuous operation of Station Two even when the needs of Henderson and its inhabitants for electric service can be satisfied from the market at a considerable cost savings. Big Rivers should not be forced to bear all the costs of Henderson's imprudent business policy.

In consideration of the length of this reply brief, Big Rivers will not attempt to address every misstatement in Henderson's brief, but a few others require a response and are discussed below. Big Rivers does not concede that any of the remaining statements in Henderson's brief not addressed herein are accurate.

Another of Henderson's claims is that it has not refused to discuss with Big Rivers the proposal by Big Rivers to operate Station Two on an economic basis, but rather "has merely declined Big Rivers' invitation to modify the existing contract in the absence of assurances that Henderson will be able to fulfill its obligation as a public entity to provide electricity to city inhabitants at the same or lesser cost than Henderson's Station Two production costs." Henderson's Post-Hearing Brief at p. 12. It is important to remember that, by definition, operation of the Station Two units on an economic commitment basis means the units will run when the market price of energy exceeds the variable production costs of Station Two, and will not run only when energy required by Henderson and Big Rivers is available from the market at a cost that is less than the Station Two variable production cost. Henderson offers no explanation for why this does not satisfy its requirement for price assurances.

Henderson asserts, "Big Rivers provides no study or other data addressing the possibility of cycling any of its other generating units. Big Rivers has segregated Station Two from its total capacity, targeted Station Two as the sole source of the excess energy problem, and identified the decommissioning of one or both units as the sole solution." *Id.* at p. 13. This is a strange and

untrue statement. All of Big Rivers' other units are either idled or operated on an economic commitment basis. *See* Rebuttal Testimony of Robert W. Berry at p. 19. Also, Big Rivers has proposed only that the Station Two units also be operated on an economic commitment basis, not decommissioned. *See,* Henderson's Post-Hearing Brief at p. 12.

Henderson relies on its incorrect and irrelevant definition of EHE to support its argument. *See, e.g., id.* at p. 14. As explained in Big Rivers' brief, Henderson's proffered definition is inconsistent with the Power Sales Contract and the arbitration award and should be rejected. *See* Big Rivers' Post-Hearing Brief at pp. 12-14. Henderson makes no attempt to support its definition.

Henderson alleges that Big Rivers is trying to "shift[] all economic risk to Henderson." Henderson's Post-Hearing Brief at p. 3. However, the only energy at issue in this proceeding is the uneconomic EHE. Big Rivers must still pay the variable costs for the uneconomic energy associated with its allocated share of Station Two's capacity, even though Henderson is the party that requires that energy to be generated. *See* Big Rivers' Post-Hearing Brief at pp. 21-22. The losses Big Rivers incurs associated with its capacity allocation far exceed any losses Henderson will incur if it continues to require the generation of uneconomic EHE and pays the variable costs for that energy. *See id.*

Another of Henderson's incorrect statements is that "Big Rivers asks the Commission to interpret the Power Sales Agreement [sic] in a way that deems Henderson responsible for variable costs associated with producing energy not taken or scheduled for sale by either party. Big Rivers' new practice of allocating to Henderson's account the variable costs of fuel and reagent associated with unwanted energy simply finds no support in the parties' agreement." Henderson's Post-Hearing Brief at p. 14.

1 Any EHE that Big Rivers elects not to take still belongs to Henderson and is taken by
2 Henderson. *See* Big Rivers' Post-Hearing Brief at p. 21. Big Rivers treats the EHE taken by
3 Henderson the same as the energy from Station Two that Henderson takes for its native load.
4 *See id.* All of that energy is sold into MISO, and Big Rivers allocates both the revenue from that
5 sale and the variable costs associated with the energy taken by Henderson to Henderson. *See id.*
6 Finally, Henderson says, "In past practice, Big Rivers did not generate any 'Excess
7 Henderson Energy' until after it had generated energy associated with the Station Two capacity
8 allocated to Big Rivers." Henderson's Post-Hearing Brief at p. 2. This statement is false. As
9 Big Rivers explained in its brief:

10 Under the Indemnification Agreement, the amount of EHE was determined
11 differently depending on whether one or both of the Station Two units were
12 operating. When both units were operating, EHE came after both Henderson's
13 native load and Big Rivers' capacity allocation. When only one unit was
14 operating, EHE came before any energy associated with Big Rivers' capacity
15 allocation.

16 Big Rivers' Post-Hearing Brief at pp. 14-15 (footnotes omitted).

17 **D. Big Rivers' methodology for calculating the amount of EHE is**
18 **reasonable.**

19 Henderson also complains that since June 1, 2016, Big Rivers has been utilizing a
20 methodology for calculating the amount of EHE that differs from the methodology previously
21 utilized. Big Rivers explained in its testimony and in its brief why it changed methodologies,
22 that it previously utilized the methodology from the Indemnification Agreement so as not to
23 jeopardize WKEC's obligations under that agreement, and that once the arbitration proceedings
24 concluded and Big Rivers confirmed that it would not jeopardize the Indemnification
25 Agreement, Big Rivers began using the new methodology that was consistent with the arbitration
26 award, the Station Two Contracts, and Henderson's requirement that its energy come first. *See*

1 Big Rivers' Post-Hearing Brief at p. 15. Henderson does not claim that the methodology from
2 the Indemnification Agreement should continue to be used, it does not advocate for a different
3 methodology in its brief, and it offers nothing to refute the reasonableness of Big Rivers'
4 methodology.

5 **E. Big Rivers is not asking the Commission to make management decisions.**

6 The final point Henderson attempts to make is that, "[t]he decision whether to generate
7 unwanted energy, and the decision whether [to] take or not take that energy, are management
8 decisions that do not require Commission approval. KRS 278.200 refers to review of contract
9 rates, and not discretionary management decisions such as the generation and disposition of
10 energy." Henderson's Post-Hearing Brief at p. 15.

11 While the Commission's authority to substitute its judgment for that of management is
12 indeed limited, none of the cases relied on by Henderson address the Commission's authority
13 under KRS 278.200.[3] To determine the extent of the Commission's authority in this case, one
14 must look to KRS 278.200, which grants the Commission authority over the rate and service
15 terms of the Station Two Contracts and over "all rights, privileges and obligations arising out"
16 the Station Two Contracts. The general proposition relating to the Commission's authority with
17 respect to management decisions does not change the fact that the Commission has jurisdiction
18 over the rate and service terms of the Station Two Contracts. Moreover, Henderson's point is
19 irrelevant because Big Rivers is only asking the Commission to determine which party is and
20 should be responsible for the variable costs incurred in producing unwanted EHE.

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[3] Henderson cites a January 31, 1990, order in P.S.C. Case Nos. 89-014, 89-029, and 89-179 that Big Rivers could not locate, but other orders in those cases indicate that the cases were unrelated to KRS 278.200.

1 Henderson's point then switches focus. Instead of continuing to look at the

2 Commission's role in management decisions, Henderson's point concludes by complaining that

3 Big Rivers would be in control of the Station Two units:

> 4 Big Rivers' effort to reinterpret the contract essentially would place Big Rivers in
> 5 control of the Station Two units, and place Henderson, the owner of the units, in a
> 6 subsidiary role unable to maintain the benefits of ownership for its customers.
> 7 Henderson's customers will cease being beneficiaries of ownership, and will
> 8 become nothing more than customers of Big Rivers, subject to the whims of the
> 9 energy market. To avoid such a result is the very reason Henderson constructed
> 10 its own power plant. The Commission is without authority to subject Henderson's
> 11 customers to Big Rivers' retail rate provisions.

12 Henderson's Post-Hearing Brief at p. 17. But this statement is not true and is not based on the

13 record. The relationship of the parties would not change under Big Rivers' proposal to operate

14 the Station Two units on an economic commitment basis. As is the current practice, in hours in

15 which neither Station Two unit is operating, Henderson receives the power needed to meet the

16 needs of itself and its inhabitants from MISO, and Big Rivers receives no margin or other benefit

17 from those transactions. Moreover, if the units are operated on an economic commitment basis,

18 Henderson will maximize the benefits of ownership, generating energy from the Station Two

19 units when they are economic to run, but benefitting from lower-cost market power when the

20 production costs of Station Two exceed market price, thus saving itself and its ratepayers

21 significant amounts of money.

22 Therefore, Henderson's argument that Big Rivers should bear the variable costs of the

23 uneconomic EHE is based on numerous unsupported and untrue statements. Presumably,

24 Henderson hopes such statements will convince the Commission that Big Rivers should bear the

25 variable costs of the uneconomic EHE in addition to the variable costs of the uneconomic energy

26 associated with Big Rivers' capacity allotment that is generated as a result of Henderson's

27 requirements. Instead, Henderson's arguments reveal Henderson's unreasonableness in

1 requiring Big Rivers to generate EHE that is uneconomic and that neither Big Rivers nor
2 Henderson want, while expecting Big Rivers to bear the variable costs of that energy. The
3 Commission should reject Henderson's argument and, for the reasons stated in Big Rivers' brief,
4 find that the Station Two Contracts either already do not, or should not, require Big Rivers to be
5 responsible for the variable costs of, or to pay Henderson for, any EHE that Big Rivers declines
6 to take and utilize.

7 **IV. Conclusion.**

8 For the foregoing reasons, and for the reasons stated in Big Rivers' brief, the Commission
9 should grant the relief requested by Big Rivers in its post-hearing brief.

10 On this the 20th day of March, 2017.

11 Respectfully submitted,
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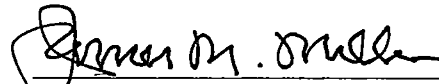
14 

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