COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

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PUBLIC SERVICE COMMISSION

In the Matter of:

THE APPLICATION OF EAST KENTUCKY POWER COOPERATIVE, INC. FOR AN ORDER APPROVING THE ESTABLISHMENT OF A REGULATORY ASSET FOR THE DEPRECIATION AND ACCRETION EXPENSES ASSOCIATED WITH THE SMITH STATION LANDFILL ASSET RETIREMENTOBLIGATIONS	)))))))	**CASE NO. 2018-**00027

APPLICATION

Comes now East Kentucky Power Cooperative, Inc. ("EKPC"), by counsel, pursuant to KRS 278.030(1), KRS 278.040(2), KRS 278.220, 807 KAR 5:001, Section 14, and other applicable law, and does hereby request the Kentucky Public Service Commission ("Commission") to approve the establishment of a regulatory asset for the depreciation and accretion expenses associated with EKPC's new J. K. Smith Station landfill ("Smith Station") Asset Retirement Obligations ("AROs"), respectfully stating as follows:

I. Applicant Information and General Filing Requirements

1. EKPC is a not-for-profit, rural electric cooperative corporation established under KRS Chapter 279 with its headquarters in Winchester, Kentucky. Pursuant to various agreements, EKPC provides electric generation capacity and electric energy to its sixteen Owner-Member Cooperatives ("owner-members"), which in turn serve approximately 530,000 Kentucky homes, farms and commercial and industrial establishments in eighty-seven (87) Kentucky counties

2. In total, EKPC owns and operates a total of approximately 2,965 MW of net Summer generating capability and 3,267 MW of net winter generating capability. EKPC owns

and operates coal-fired generation at the John C. Cooper Station in Pulaski County, Kentucky (341 MW) ("Cooper Station") and the Hugh L. Spurlock Station in Mason County, Kentucky (1,346 MW) ("Spurlock Station"). EKPC also owns and operates natural-gas fired generation at the. Smith Station in Clark County, Kentucky (753 MW (summer)/989 MW (winter)) and the Bluegrass Station in Oldham County, Kentucky (501 MW (summer)/567 MW (winter)), and landfill gas-to-energy facilities in Boone County, Laurel County, Greenup County, Hardin County, Pendleton County and Barren County (16 MW total). In November 2017, EKPC added a Community Solar facility (8 MW) in Winchester, Kentucky to its generation portfolio. Finally, EKPC purchases hydropower from the Southeastern Power Administration at Laurel Dam in Laurel County, Kentucky (70 MW), and the Cumberland River system of dams in Kentucky and Tennessee (100 MW). EKPC's record peak demand of 3,507 MW occurred on February 20, 2015.

3. EKPC owns 2,940 circuit miles of high voltage transmission lines in various voltages. EKPC also owns the substations necessary to support this transmission line infrastructure. Currently, EKPC has seventy-four (74) free-flowing interconnections with its neighboring utilities.

4. Pursuant to 807 KAR 5:001, Section 14(1), EKPC's mailing address is P.O. Box 707, Winchester, Kentucky 40392-0707 and its email address is psc@ekpc.coop. The facts and law upon which this Application is based are stated in paragraphs six (6) through seventeen (17) below. Counsel for EKPC should be served at the following email addresses: mdgoss@gosssamfordlaw.com and david@gosssamfordlaw.com.

5. Pursuant to 807 KAR 5:001, Section 14(2), EKPC is a Kentucky corporation that was incorporated on July 9, 1941. EKPC is in good standing to transact business within the Commonwealth of Kentucky.

II. Background

6. In Case No. 2014-00432,[1] the Commission approved EKPC's request to establish regulatory assets for the accretion and depreciation associated with AROs, by type and location, which were in existence as of December 31, 2013. This order covered asbestos AROs at the William C. Dale Generating Station ("Dale Station"), which was retired in 2016, and Cooper Station, and ash impoundment AROs at the Dale Station, Cooper Station and Spurlock Station. The Smith Station Landfill did not yet exist and, therefore, was not a part of the ash impoundment AROs at issue in Case No. 2014-00432.

7. The Smith Station Landfill was placed into commercial operation in 2016 as part of the planned retirement of the Dale Station ash ponds. The retirement plan included the relocation of approximately 560,000 cubic yards of coal ash from the ash ponds, which involved excavating and trucking the stored coal ash to the Smith Station Landfill, located in eastern Clark County, Kentucky. The Commission approved EKPC's plan in Case No. 2014-00252,[2] and EKPC completed the relocation project in December 2017. The Smith Station Landfill was first included in EKPC's AROs for coal ash impoundments as of December 31, 2016, which is shortly after it began receiving ash from the Dale Station. EKPC began recognizing accretion and depreciation associated with the Smith Station Landfill AROs in January 2017.

8. AROs are legal obligations associated with the retirement of long-lived assets that result from the acquisition, construction, development and/or the normal operation of such assets.

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[1] *See In the Matter of the Application of East Kentucky Power Cooperative, Inc. for an Order Approving the Establishment of Regulatory Assets for the Deprecation and Accretion Expenses Associated with Asset Retirement Obligations*, Order, Case No. 2014-00432 (Ky. P.S.C. Mar. 6, 2015).

[2] *See In the Matter of the Application of East Kentucky Power Cooperative, Inc. for a Certificate of Public Convenience and Necessity for Construction of an Ash Landfill at J. K. Smith Station, the Removal of Impounded Ash from William C. Dale Station for Transport to J. K. Smith and Approval of a Compliance Plan Amendment for Environmental Surcharge Recovery*, Order, Case No. 2014-00252 (Ky. P.S.C. Mar. 3, 2015).

Financial Accounting Standards Board Accounting Standards Codification ("ASC") Topic 410-20, *Asset Retirement Obligations*, requires legal obligations associated with the retirement of long-lived assets to be recognized at fair value when incurred and capitalized as part of the related long-lived asset. ASC Topic 410-20 also clarifies the term "conditional asset retirement obligation" where an obligation exists even though the method or timing of settlement may be conditional. The liability is accreted to its present value each period and the capitalized cost is depreciated over the useful life of the related asset. When the asset is retired, the entity settles the obligation for its recorded amount or incurs a gain or loss.

9. Pursuant to KRS 278.220, the Commission has established a system of uniform accounts for EKPC which was issued by the United States Department of Agriculture, Rural Utilities Service ("RUS").[3] The RUS Uniform System of Accounts ("RUS USoA") states:

> (1) An asset retirement obligation represents a liability for the legal obligation associated with the retirement of a tangible long-lived asset that a company is required to settle as a result of an existing or enacted law, statute, ordinance, or written or oral contract or by legal construction of a contract under the doctrine of promissory estoppel. An asset retirement cost represents the amount capitalized when the liability is recognized for the long-lived asset that gives rise to the legal obligation. The amount recognized for the liability and an associated asset retirement cost shall be stated at the fair value of the asset retirement obligation in the period in which the obligation is incurred.[4]

10. The RUS USoA requires that a utility initially record a liability for an ARO in Account 230 — Asset Retirement Obligations, and charge the associated asset retirement costs to the electric utility plant that gave rise to the legal obligation. The asset retirement cost is to be depreciated over the useful life of the related asset that gives rise to the obligation. In periods

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[3] Codified as 7 CFR Part 1767. The current version of the RUS system of accounts became effective May 27, 2008 and is also published and referenced as RUS Bulletin 1767B-1.

[4] Section 1767.15, General Instructions, subpart (y), Accounting for asset retirement obligations.

subsequent to the initial recording of the ARO, the utility shall recognize the period-to-period changes of the ARO that result from the passage of time due to the accretion of the liability by recording a debit to Account 411.11 — Accretion Expense, and a credit to Account 230. For any subsequent measurement changes to the initial liability for the legal obligation recorded in Account 230 for each specific ARO, the utility shall recognize said changes as an adjustment to the liability in Account 230 with a corresponding adjustment to the appropriate electric utility plant account. The utility shall monitor measurement changes of the AROs on a timely basis. Accordingly, the amount recorded as an ARO liability and the corresponding capitalized asset retirement cost represents the best available information at a point in time about the costs and timing associated with the method expected to be used by a utility to satisfy the legal obligation.

11. Pursuant to the requirements of the RUS USoA, EKPC records depreciation expense for the ARO-related assets and accretion expense for the ARO-related liabilities on a monthly basis. For the year ended December 31, 2017, the ARO-related depreciation expense was $28,071 and the accretion expense was $55,007, for a total of $83,078.

12. While the Smith Station Landfill AROs will be settled and resolved at a future date, under the RUS USoA, EKPC is required to currently recognize depreciation and accretion expenses. EKPC believes that the actual ARO settlement costs will be recoverable in rates or through the Environmental Surcharge mechanism when the costs are finalized. However, this deferred recovery creates a mismatch of revenues and expenses in the financial statements because expenses are recognized as the ARO balances are accreted and depreciated but the revenue will not be recognized until the actual project costs are recovered through either the environmental surcharge or another rate mechanism. The Smith Station Landfill ARO-related expenses therefore reduced EKPC's margins and understated the company's actual financial performance for 2017.

In later accounting periods when the actual costs are being recovered, revenues and expenses will be inflated and thus overstate financial performance. Therefore, EKPC is requesting authorization from the Commission to reclassify the 2017 Smith Station Landfill ARO-related depreciation and accretion expenses of $83,078 as a regulatory asset. EKPC is also requesting that all subsequent ARO-related depreciation and accretion expenses associated with the Smith Station Landfill AROs be recorded as a regulatory asset. This treatment will defer recognition of these ARO expenses until recovery occurs, resulting in an appropriate matching of revenues and expenses in each accounting period. This treatment is also consistent with the Commission's Order in Case No. 2014-00432 for all other EKPC AROs.

III. Request to Establish Regulatory Asset

13. EKPC has not established the requested regulatory assets on its books. EKPC acknowledges that prior Commission approval is required to establish the requested regulatory assets. At this time, EKPC is requesting regulatory asset treatment for accounting purposes only.

14. The Commission has previously authorized EKPC and other jurisdictional utilities to establish regulatory assets. The Commission has exercised its discretion to approve regulatory assets where a utility has incurred: (a) an extraordinary, nonrecurring expense which could not have reasonably been anticipated or included in the utility's planning; (b) an expense resulting from a statutory or administrative directive; (c) an expense in relation to an industry sponsored initiative; or (d) an extraordinary or nonrecurring expense that over time will result in a saving that fully offsets the cost.[5] EKPC believes its request to establish the regulatory asset for the Smith

[5] *See In the Matter of the Application of East Kentucky Power Cooperative, Inc. for an Order Approving Accounting Practices to Establish a Regulatory Asset Related to Certain Replacement Power Costs Resulting from Generation Forced Outages*, Order, Case No. 2008-00436, p. 4 (Ky. P.S.C., Dec. 23, 2008). *Also See In the Matter of Application of East Kentucky Power Cooperative, Inc. for an Order Approving the Establishment of a Regulatory Asset for the Amount Expended on Its Smith 1 Generating Unit*, Order, Case No. 2010-00449, p. 7 (Ky. P.S.C., Feb. 28, 2011).

Station Landfill for the ARO-related depreciation and accretion expenses is consistent with the second listed example, as the ARO-related depreciation and accretion expenses result from the accounting requirements of the RUS USoA and ASC Topic 410-20 concerning ARO accounting.

15. The Commission has previously approved the establishment of regulatory assets for ARO-related depreciation and accretion expenses. The Commission approved the establishment of regulatory assets for ARO-related depreciation and accretion expenses for Louisville Gas and Electric Company,[6] and Kentucky Utilities Company,[7] when those utilities adopted Statement of Financial Accounting Standards No. 143, *Accounting for Asset Retirement Obligations.*[8]

16. The Commission is requested to authorize EKPC to establish a regulatory asset for ARO-related depreciation and accretion expenses resulting from Smith Station Landfill ARO balances at December 31, 2016 beginning in January 2017 and for all years subsequent to 2017. Consequently, EKPC requests that the Commission approve this request no later than March 1, 2018. Authorization by this date will enable EKPC to establish the regulatory assets for 2017, before the final closing of its books. However, if the Commission is unable to act on this application by March 1, 2018, EKPC would request the Commission to direct EKPC to record a credit to expense and debit the regulatory asset account for $83,078 in the 2018 financial statements to bring the regulatory asset account balance up to the amount requested for December 31, 2017 and to also record all accretion and depreciation in 2018 and subsequent years as

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[6] *See In the Matter of Application of Louisville Gas and Electric Company for an Order Approving an Accounting Adjustment to be Included in Earnings Sharing Mechanism Calculations for 2003,* Order, Case No. 2003-00426, p.6 (Ky. P.S.C., Dec. 23, 2003).

[7] *See In the Matter of Application of Kentucky Utilities Company for an Order Approving an Accounting Adjustment to be Included in Earnings Sharing Mechanism Calculations for 2003,* Order, Case No. 2003-00427, p.6 (Ky. P.S.C., Dec. 23, 2003).

[8] Statement of Financial Accounting Standards No. 143 is now codified as ASC Topic 410.

regulatory assets. The accounting entries reflecting the establishment of the regulatory assets in 2017 and entries for years subsequent to 2017 are shown in Exhibit 1 of this application.

WHEREFORE, on the basis of the foregoing, EKPC respectfully requests the Commission to authorize the establishment of a regulatory asset for the Smith Station Landfill ARO-related depreciation and accretion expenses incurred during 2017 and subsequent years.

Done this 17th day of January, 2018.

VERIFICATION

This will certify that I, Mike McNalley, the Chief Financial Officer of East Kentucky Power Cooperative, Inc., on behalf of said corporation, after having first been duly sworn, did examine the contents of this Application and that, to the best of my knowledge and belief as formed after reasonable diligence and inquiry, said statements are true and correct as of this 17th day of January, 2018

East Kentucky Power Cooperative, Inc.

BY: [signature]

ITS: EVP & CFO

COMMONWEALTH OF KENTUCKY

COUNTY OF CLARK

The foregoing Verification was signed, acknowledged and sworn to before me the 17th day of January, 2018 by Mike McNalley, the Chief Financial Officer of East Kentucky Power Cooperative, Inc., a Kentucky corporation, on behalf of the corporation.

Gwyn M. Willoughby

NOTARY PUBLIC

MY COMMISSION EXPIRES: 11/30/21

NOTARY ID. NO. 590567

GWYN M. WILLOUGHBY
Notary Public
Kentucky – State at Large
My Commission Expires Nov 30, 2021

Respectfully submitted,

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Counsel for East Kentucky Power Cooperative, Inc.

Exhibit 1

Sample Accounting Entries

Entry to Establish Regulatory Asset at December 31, 2017

Account 1823XX—Other Regulatory Assets	$83,078	
Account 403800—Depreciation Expense, Asset Retirement Costs		$28,071
Account 411100—Accretion Expense		$55,007

To establish a regulatory asset for Smith Station Landfill depreciation and accretion expenses recognized in 2017.

Monthly Entries in Subsequent Years to Record Transfer Depreciation and Accretion Expenses to Regulatory Asset

411100—Accretion Expense	$4,584	
23003—Asset Retirement Obligation-Ash		$2,355
23004—Asset Retirement Obligations-Ash Post-Closure		$2,229

To record monthly accretion of Smith Station Landfill asset retirement obligation

403800—Depreciation Expense, Asset Retirement Obligation	$2,339	
108902—Accumulated Depreciation, Asset Retirement Obligation		$2339

To record monthly depreciation of Smith Station Landfill asset retirement costs

Account 1823XX—Other Regulatory Assets	$6,923	
Account 403800—Depreciation Expense, Asset Retirement Costs		$2,339
Account 411100—Accretion Expense		$4,584

To record Smith Station Landfill monthly accretion and depreciation expenses as regulatory assets