

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

AN INVESTIGATION OF EAST KENTUCKY) CASE NO.
POWER COOPERATIVE, INC.'S NEED FOR) 2010-00238
THE SMITH 1 GENERATING FACILITY)

O R D E R

The Commission, on its own motion pursuant to KRS 278.260, hereby initiates this investigation of the need of East Kentucky Power Cooperative, Inc. ("East Kentucky") for Smith 1, an electric generating unit previously authorized to be constructed by Order dated Aug. 29, 2006 in Case No. 2005-00053.¹ While the Commission does not typically investigate issues that have already been adjudicated, there are unique facts and circumstances relating to Smith 1 that justify this course of action. They include the passage of over 3.5 years since the date the Commission approved the facility and all necessary permits still not obtained by East Kentucky, a very substantial escalation in the estimated cost of construction, and issues raised by three retail customers in a separate complaint case challenging Smith 1 as neither needed nor least-cost.

¹ Case No. 2005-00053, Application of East Kentucky Power Cooperative, Inc. for a Certificate of Public Convenience and Necessity, and a Site Compatibility Certificate, for the Construction of a 278 MW (Nominal) Circulating Fluidized Bed Coal Fired Unit and Five 90 MW (Nominal) Combustion Turbines in Clark County, Kentucky (Ky. PSC Aug. 29, 2006).

BACKGROUND

East Kentucky is a generating and transmission cooperative organized under KRS Chapter 279. It provides wholesale electric generation and transmission service to its 16 member/owner distribution cooperatives who in turn serve approximately 500,000 retail customers in Kentucky. East Kentucky applied to the Commission on January 31, 2005 for a Certificate of Public Convenience and Necessity (“CPCN”) to construct a 278 MW circulating fluidized bed coal-fired generating facility (“Smith 1”) at its Smith Station in Clark County, Kentucky.² After conducting an investigation and hearing, the Commission granted East Kentucky the authority to construct Smith 1 based on finding that East Kentucky’s “load projections are reasonable and they demonstrate a need for approximately 270 MW of base load generation.”³

Included in East Kentucky’s load projections were the generation needs of Warren Rural Electric Cooperative Corporation (“Warren RECC”), a distribution cooperative in Kentucky that had historically purchased its generation from the Tennessee Valley Authority (“TVA”). Although Warren RECC had decided in 2004 to switch its power supply from TVA to East Kentucky, Warren RECC cancelled that decision on December 8, 2006. As a result of Warren RECC’s decision to retain TVA as its supplier, the Commission initiated an investigation of East Kentucky’s continued need for all of the additional generating facilities that were then approved but not yet

² East Kentucky also requested and was granted authority to construct five 90 MW combustion turbines, two of which have been completed and are in service, the other three having been cancelled in early 2007. None of these combustion turbines are the subject of this investigation.

³ Case No. 2005-00053, Order dated August 29, 2006, at 4.

constructed, including Smith 1.⁴ That investigation was concluded upon the Commission finding, among other things, that Smith 1 “is needed to serve EKPC’s growing native load, ease demand for more expensive purchased power, and improve the overall system reliability.”⁵ Based on this finding, the Commission authorized East Kentucky to retain the previously issued CPCN authorizing the construction of Smith 1.⁶

RETAIL CONSUMERS’ COMPLAINT
CASE NO. 2009-00426

On October 28, 2009, three retail consumers on the East Kentucky system, John Patterson, John Rausch, and Wendell Berry (collectively, “Retail Customers”), along with three environmental organizations, Sierra Club, Kentucky Environmental Foundation, and Kentuckians for the Commonwealth (collectively, “Environmental Groups”), filed a formal complaint against East Kentucky.⁷ The complaint set forth a number of claims related to Smith 1, including allegations that it was not needed and was not least-cost. The Commission accepted that portion of the complaint as filed by the Retail Customers, but not by the Environmental Groups due to their lack of standing, challenging Smith 1 as not needed and not least-cost, and directed East Kentucky to file

⁴ Case No. 2006-00564, An Investigation Into East Kentucky Power Cooperative, Inc.’s Continued Need for Certificated Generation, Order dated January 5, 2007.

⁵ Id. Order dated May 11, 2007, at 9.

⁶ Id. at 13.

⁷ Case No. 2009-00426, Dr. John Patterson, Fr. John Rausch, Wendell Berry, Sierra Club, Kentucky Environmental Foundation and Kentuckians for the Commonwealth v. East Kentucky Power Cooperative, Inc. (hereinafter “Complaint Case”).

an answer to the complaint.⁸ East Kentucky filed an answer and a request that the complaint be dismissed. The Retail Customers filed a response in opposition to the request to dismiss, and East Kentucky filed a reply. The motion to dismiss is now pending a decision by the Commission, as is the Retail Customers' motion to file an amended complaint.

SMITH 1 FINANCING
CASE NO. 2009-00476

On December 30, 2009, East Kentucky filed an application for approval to issue evidences of indebtedness, consisting of \$900 million in secured private placement debt and approximately \$21.4 million of unsecured debt.⁹ The proceeds of the debt are to be used to fund the construction of Smith 1. Gallatin Steel Company ("Gallatin Steel"), the largest consumer of electric power on the East Kentucky system, requested and was granted intervention. A procedural schedule was established which provided for two rounds of discovery to East Kentucky, an opportunity for intervenors to file testimony, and discovery to intervenors.

As part of Gallatin Steel's discovery, it requested East Kentucky to provide information relating to the current projected need for Smith 1, whether or not Smith 1 represents the least-cost power supply option, and the cost to cancel Smith 1. East Kentucky refused to provide the requested information, stating that it went beyond the

⁸ Case No. 2009-00426, Order dated December 22, 2009.

⁹ Case No. 2009-00476, Application of East Kentucky Power Cooperative, Inc. for Approval of the Issuance of \$900,000,000 of Secured Private Placement Debt and Up to \$21,435,000 of Unsecured Debt (hereinafter "Financing Case").

scope of the issues that are appropriate in a case seeking approval of financing under KRS 278.300.

On February 18, 2010, a motion to intervene was filed by four retail consumers on East Kentucky's system and the Environmental Groups. Of the four retail consumers, three are the Retail Customers who are the named complainants in Case No. 2009-00426, and the fourth consumer is Mike Hannon. The three Environmental Groups requesting intervention are the same ones that requested and were denied status as named complainants in Case No. 2009-00426. The request to intervene questions East Kentucky's need for Smith 1, the estimated cost for Smith 1, and East Kentucky's ability to obtain reasonable terms and rates for the proposed financing. East Kentucky filed an objection to this request for intervention, and the four retail consumers and the Environmental Groups filed a response thereto.

On April 15, 2010, East Kentucky filed a motion to withdraw the Financing Case, stating that it wanted to reassess its financing needs and that it would refile a new financing application at a later time.¹⁰

COMMISSION FINDINGS

Based on the evidence of record in Case Nos. 2009-00426 and 2009-00476, the Commission finds that there are substantial issues relating to Smith 1 that warrant the initiation of this investigation. Those issues include East Kentucky's current projected need for additional base load generating capacity, whether or not Smith 1 remains the

¹⁰ East Kentucky has now filed a new financing application for approval of a three-year revolving credit facility to be used to refund an existing credit facility and to fund capital new expenditures other than for Smith 1. Case No. 2010-00166, Application of East Kentucky Power Cooperative, Inc. for Approval of a Three-Year Senior Unsecured Revolving and Term Credit Facility in an Amount up to \$500,000,000.

least costly option available to meet a need for additional base load capacity, and the impact to East Kentucky's financial integrity and its future electric rates from either constructing Smith 1 or pursuing an alternative option if additional base load capacity is needed. Although many of these issues have been raised in the Complaint Case and in the Financing Case, the Commission believes that it will be more efficient, in terms of conserving valuable and limited personnel and resources, avoiding duplication of effort, and achieving administrative economy, for all of the issues relating to Smith 1 that are within our jurisdiction to be reviewed in one proceeding. Concurrent with the initiation of this investigation, Orders will be entered today closing the Complaint Case and the Financing Case.

The Commission notes at the outset that the scope of our jurisdiction is limited by KRS 278.040(2) to "the regulation of rates and service of utilities." The Commission does not have jurisdiction over environmental issues, including, but not limited to, the permissible types and levels of emissions and wastes from a power plant, the health impacts of using fossil fuels to generate electricity, and whether or not the environmental equipment proposed for a new power plant is sufficient for the issuance of necessary permits by other federal, state or local agencies. Thus, these environmental issues and others that are within the jurisdiction of other agencies are not appropriate for investigation here. Rather, this investigation will be limited to whether there is a current need for additional base load capacity and, if there is such a need, whether Smith 1 is the least costly option for meeting that need and the potential impact of Smith 1 on East Kentucky's rates and service.

The Commission, again on its own motion, will make those who were already parties to either the Complaint Case or the Financing Case parties to this investigation. Thus, East Kentucky, the Retail Customers, and Gallatin Steel are parties to this investigation. The Commission recognizes that, in the Complaint Case, there is an outstanding motion by the Retail Customers to file an amended complaint which would, among other things, join one additional named individual and the Environmental Groups as complainants. Similarly, in the Financing Case, there was a pending motion to intervene that was filed on behalf of the Retail Customers, one additional named individual, and the Environmental Groups.

The Environmental Groups were previously denied status as complainants in the Complaint Case due to lack of standing based on the omission of the name of any member of any of the three groups that had authorized the groups to act on their behalf. In the amended complaint and in the request to intervene in the Financing Case, the Environmental Groups now reveal the names of their members that have authorized their participation: the three already named Retail Customers; and the one additional named individual. However, neither the amended complaint nor the request to intervene in the Financing Case discloses any differences in the interests or positions to be advocated by the Retail Customers, the additional named individual, or the Environmental Groups. To the contrary, the pleadings indicate that they all share common interests and positions with respect to Smith 1. In addition, no reason is offered to support a finding that the three named Retail Customers are not capable of competently advocating the interests and positions that they share in common with the additional named individual and the Environmental Groups. Consequently, the

additional named individual and the Environmental Groups will not be listed as parties to this investigation, but they may work with and assist the Retail Customers to the extent they choose to do so.

The Commission will conduct a rigorous and comprehensive investigation of the need for and financial implications of Smith 1. We will closely examine East Kentucky's most recent load projections as set forth in its pending Integrated Resource Plan ("IRP") filing,¹¹ as well as the potential for load reductions resulting from cost-effective energy efficiency and demand-side management programs. The cost estimates for Smith 1 will be reviewed, as well as the cost of alternatives to Smith 1, including, but not limited to, natural gas-fired generation and long-term power purchases. We will also examine the financial impacts of Smith 1 to East Kentucky, including the impact on its electric rates over the next 20 years. The parties will have an opportunity to raise issues that are within the scope of the Commission's jurisdiction, and an evidentiary hearing will be held prior to the issuance of a final decision.

Attached hereto is a procedural schedule for processing this investigation. East Kentucky's direct testimony should, at a minimum, include:

1. A discussion of its most recent long-term load forecast and its existing generating capacity;
2. One or more charts or tables showing, for each of the four past years and each forecast year, winter and summer firm peak demand, required reserves, required capacity, existing capacity, peak and base load planned capacity additions, capacity

¹¹ Case No. 2009-00106, 2009 Integrated Resource Plan of East Kentucky Power Cooperative, Inc.

surplus or deficiency, energy sales by retail customer classes,¹² total energy requirements, energy available from existing generation, and energy surplus or deficiency;

3. A discussion of existing and planned energy efficiency and other demand-side management programs during the forecast period and their impact on the energy and demand forecast;

4. A discussion of the current planned in-service date for Smith 1, a detailed cost estimate of the major components, and an analysis of the operational and financial impacts of delaying the in-service date for Smith 1;

5. A 20-year detailed production cost and financial analysis, including a comparison of East Kentucky's total revenue requirements from members, net present value of revenue requirements, and income statements, assuming Smith 1 is in service as currently planned, is delayed two years, and is delayed five years;¹³

6. A 20-year analysis showing, on a net present value revenue requirements basis, the impact of Smith 1 at its currently planned in-service date versus available alternatives such as gas-fired generation, long-term power purchase contracts, renewable energy, and energy efficiency measures;

¹² As shown in East Kentucky's IRP filing in Case No. 2009-00106, page 7-2, Table 1.

¹³ The analysis should be in a format similar to East Kentucky's response to Item 6 of the Commission's information request dated January 5, 2007 in Case No. 2006-00564.

7. A 20-year estimate of the annual revenue requirements impact to East Kentucky, in both dollars and percent of existing revenue requirements, of Smith 1 at its currently planned in-service date; and

8. A schedule showing East Kentucky's anticipated annual rates by rate schedule for the next 20 years, assuming Smith 1 at the currently planned in-service date, assuming a gas-fired generation in lieu of Smith 1, assuming a long-term power purchase contract in lieu of Smith 1, assuming renewable energy in lieu of Smith 1, and energy efficiency measures in lieu of Smith 1.

Upon conclusion of discovery and the filing of testimony, an evidentiary hearing will be scheduled.

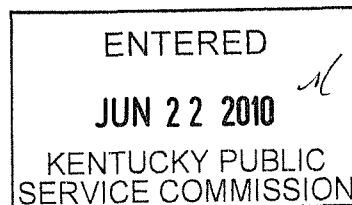
IT IS THEREFORE ORDERED that:

1. This investigation of East Kentucky's need for Smith 1 and the availability of viable alternatives thereto is opened.

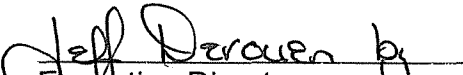
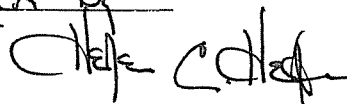
2. The parties to this case shall be East Kentucky, Gallatin Steel, and the three Retail Customers named as complainants in Case No. 2009-00426.

3. The procedural schedule set forth in the attached Appendix shall be followed.

By the Commission



ATTEST:


Executive Director 

APPENDIX

APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE
COMMISSION IN CASE NO. 2010-00238 DATED **JUN 22 2010**

East Kentucky shall file direct testimony, in
verified prepared form, no later than.....07/23/10

Initial data requests to East Kentucky
shall be filed no later than.....08/06/10

East Kentucky shall respond to initial data
requests no later than.....08/20/10

Supplemental data requests to East Kentucky
shall be filed no later than.....09/03/10

East Kentucky shall respond to supplemental
data requests no later than.....09/17/10

Response testimony, if any, shall be filed by
the parties, in verified prepared form, no later than10/01/10

Data requests to the parties shall be filed no later than.....10/15/10

Parties shall respond to data requests no later than.....10/29/10

Rebuttal testimony by East Kentucky, if any, shall be
filed, in verified prepared form, no later than11/12/10

Public hearing for the purpose of cross-examination of the
witnesses of East Kentucky and other parties To be scheduled

