EAST KENTUCKY POWER COOPERATIVE

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PUBLIC SERVICE COMMISSION

June 2, 2014

Mr. Jeff Derouen, 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. to Transfer Functional Control of Certain Transmission Facilities to PJM Interconnection, LLC,* P.S.C. Case No. 2012-00169 - Annual Report of East Kentucky Power Cooperative, Inc.

Dear Mr. Derouen,

In accordance with the December 20, 2012 Order of the Kentucky Public Service Commission ("Commission") in the above-styled case, please accept this as the annual report of East Kentucky Power Cooperative, Inc. ("EKPC") regarding its participation in the PJM Interconnection, LLC ("PJM"). In accordance with the Order, I would request that you place this annual report in EKPC's company correspondence file.

In addition, as set forth below, EKPC respectfully requests that the Commission either provide a letter or enter an appropriate Order moving the filing deadline for this Annual Report in all years subsequent to this one to July 31 in order to adequately capture a full year's worth of PJM operating data since PJM's operating year runs from June 1 to May 31 of each year, and it takes approximately six weeks after the final operating day of a given month to adequately assemble all of the data associated with that operational month.

With regard to the four specific topics of interest in the Commission's December 20, 2012 Order, I can report as follows.

Transmission Rights Awarded and Purchased

EKPC received Auction Revenue Rights ("ARRs"), based on its load requirements, during the annual allocation in April 2013. Those ARRs are used to obtain Financial Transmission Rights ("FTRs") to hedge the transmission congestion costs to serve EKPC's load throughout the delivery year. The ARRs can either be self-scheduled into FTRs or can be financially settled in the daily market and that revenue is used to purchase additional FTRs or used to off-set congestion costs. Attached is an Excel file (EKPC Auction Results 13_14.xlsx) on the enclosed CD, with the amount of Financial Transmission Rights ("FTRs") that EKPC had in total during the delivery year June 1, 2013 through May 31, 2014. The spreadsheet also shows the costs for the FTRs purchased and the value of the FTRs "self scheduled". The values are listed for the 5x16 portion, which includes values applicable Monday through Friday from 7:00

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am through 10:00pm. The "wrap" is the off peak hours of 11:00 pm through 6:00am from Monday through Friday plus the entire 24 hours on Saturday and Sunday. EKPC estimates the net value of the ARRs and FTRs to its members from June 1, 2013 through March 31, 2014 to be roughly [redacted]. This value has been included in the Trade Benefits described later in this report.

<u>Description of Hedging Plans and Strategies</u>

EKPC utilizes services from ACES to assist with the hedging plans and strategies for transmission congestion. Each month, EKPC, with assistance from ACES, analyzes its expected transmission positions and needs through the remainder of the delivery year (June 1 through May 31). Based on this analysis, bids are developed for the monthly FTR auctions. EKPC plans to hedge up to [redacted] of its FTR needs in the Long Term Auctions (3 year auctions), an additional [redacted] in the annual auctions (covering the delivery year from June 1 through May 31), an additional [redacted] in the quarterly auctions and the final [redacted] in the monthly auctions. This strategy allows EKPC to layer its exposure to different price points in the market and to take advantage of potential low cost opportunity markets. It also allows EKPC to adjust its expected needs based on actual loads realized in the near term and adjust its expectations as needed, so that its FTR position is not over hedged in the market. EKPC's strategy is to match its FTR position as closely to its load serving requirements as possible to minimize its exposure to congestion costs. Transmission congestion within the EKPC system has not been a significant issue since joining PJM.

Regarding Hedging Plans and Strategy for Market Prices for Capacity and Energy, EKPC's strategy is to fully hedge its price exposure in the capacity auction based on its load requirements and to sell all excess capacity for additional revenues. EKPC must purchase capacity based on its Net System Peak Load ("NSPL"). NSPL is based on EKPC's native load requirements coincident with the PJM summer peak load. EKPC will pay the same amount for its NSPL requirements on a $/MW-Day basis as it sells its capacity. Thus, EKPC's price exposure is hedged in the capacity market as long as its generation available to sell is equal to or greater than its NSPL. EKPC realizes additional value from the capacity auction by having excess capacity to sell. EKPC is a price taker on the excess capacity it sells.

EKPC's strategy for hedging its energy prices is to actively manage its expected cost to serve and minimize its risk exposure to price spikes. EKPC models and reviews its energy price exposure on a monthly basis, looking forward three years. EKPC utilizes a production cost model to estimate its energy price exposure within the PJM market. The model considers the expected fuel and operations costs for the EKPC generation fleet and compares those to expected market prices. This comparison determines if EKPC's generation is economic to operate, provides an estimation of how much the EKPC generation fleet will run and defines how much EKPC can expect to pay for its load requirements. Based on the model results, EKPC identifies potential forward purchases or sales that could lower its expected risk profile of its energy costs. This data also provides a view for EKPC's fuel procurement process, which then determines how much fuel should be purchased to ensure adequate and cost effective supplies. An example of the portfolio dashboard graphs that are evaluated monthly is attached.

Additionally, EKPC's Market Operations Center follows load and energy market trends daily and identifies opportunities to lower its net operating costs during the Day Ahead and Real Time markets.

<u>Prior Year's Benefits and Costs of PJM Membership</u>

EKPC identified its costs and benefits from June 1, 2013 (entry into PJM) through March 31, 2014, as shown in the following table. Given the required filing date of the report, it is not feasible for EKPC to provide data through May 31, 2014. It takes approximately six weeks after the final operating day of a given month to adequately assemble all of the data associated with that operational month. In 2015, EKPC can offer a full 12 month view from April 1, 2014 through March 31, 2015. However, that 12 month view will not be coincident with the PJM 12 month operating year. In order to adequately reflect the PJM operating year data (June 1 through May 31), EKPC will need to move the filing date for this informational report to July 31 of each year, and EKPC respectfully requests that the Commission provide a letter or enter an appropriate Order honoring this request.

In the following table, the Administrative Costs and Transmission Costs are based on accounting entries in EKPC's General Ledger and reflect actual out of pocket costs. Trade Benefits are based on a detailed modeling effort. EKPC utilized its production cost model (RTSim – the same model used for its Integrated Resource Plan analysis) and simulated what its operations as a stand-alone Balancing Authority would have cost and compared that to the actual costs from operating within PJM. EKPC modeled actual loads, actual prices, actual generating unit availability statistics and estimated transmission availability from outside resources. This methodology is similar to the methodology utilized in the study completed and entered into EKPC's request to the Commission to join PJM. The difference being that the PJM costs are now actually a known quantity instead of an estimated price. Capacity Benefits are based on the actual cleared Reliability Pricing Model ("RPM") results and are shown on the monthly PJM invoice. The Avoided Point to Point Transmission Charges are based on the contract that EKPC had with PJM to purchase 400 MW of firm transmission and the published tariff associated with that purchase, it does not include in additional charges for actual energy transactions on the transmission. The original estimate of these costs and benefits were provided on a ten year Net Present Value basis and the following table is only for the ten month operational period from June 1, 2013 through March 31, 2014.

<u>Category</u>	<u>Costs</u>	<u>Benefits</u>
Administrative Costs	[redacted]	
Transmission Costs	[redacted]	
Trade Benefits		[redacted]
Capacity Benefits		[redacted]
Avoided PTP Transmission Charges		[redacted]
Subtotal	[redacted]	[redacted]
Net Benefits		[redacted]

Projection of Future Benefits and Costs of PJM Membership

Finally, the December 20, 2012 Order directs EKPC to provide "a projection of future benefits and costs reflecting the most recent PJM capacity auction results." EKPC substituted known cost and benefit data into the worksheet used in the original analysis to project future benefits and costs. The original study was time and resource intensive and EKPC has no reason to believe the underlying basis of the analysis has changed significantly except for the actual costs and benefits that have been realized. The following table reflects inclusion of actual data along with original projections for the remainder of the study. [redacted] The Base Residual Auction for 2017/18 was recently held and the clearing price was $120/MW-Day, which is closer to the original assumptions than last year's price. [redacted] and the market indicates that the likelihood of this trend continuing makes sense.

Category	Costs	Benefits
Administrative Costs	[redacted]	
Transmission Costs	[redacted]	
Trade Benefits		[redacted]
Capacity Benefits		[redacted]
Avoided PTP Transmission Charges		[redacted]
Subtotal	[redacted]	[redacted]
Net Benefits		[redacted]

On behalf of EKPC, I would be delighted to address any further questions that the Commission might have with regard to the company's ongoing participation in PJM. We continue to believe that participation in PJM will allow EKPC to realize long-term value for its Members. Please feel free to contact me if you need any additional information.

Sincerely,

Patrick Woods
Director, Regulatory & Compliance Services

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