The Fuel Adjustment Clause

A presentation to the
Kentucky House Tourism and Energy Committee

Jeff Derouen
Executive Director
Kentucky Public Service Commission

February 5, 2015

THE FAC: KEY FACTS

Purpose:

To reflect fluctuations in the price of fuel and power purchased by electric utilities through a mechanism that makes adjustments on a regular basis. This reduces the need for utilities to file base rate cases. The FAC reflects the costs of fuel and purchased power without any profit or loss for the utility.

THE FAC: KEY FACTS

Legal basis:

- KRS 278.040: jurisdiction over the regulation of rates and services of utilities
- KRS 278.030(1):rates must be fair, just and reasonable
- 807 KAR 5:056: details of FAC process

Three levels of review

- Monthly
- Six-month
- Two-year

THE FAC: KEY FACTS

How it works:

- A baseline fuel cost is incorporated within the consumption-based (per kilowatt-hour (KWH)) portion of utility's base rates
- If utility's fuel costs in a given month are above the baseline, the FAC appears as per-KWH charge
- If fuel costs fall below the baseline, the FAC appears as a per-KWH credit

THE FAC: KEY FACTS

Monthly review:

- FAC changes monthly to reflect the fuel costs incurred two months earlier.
- Utilities are required to fully document all of their fuel costs - fuel purchase contracts and other materials must be submitted to the PSC
- Monthly FAC filings are reviewed for accuracy by PSC staff

THE FAC: KEY FACTS

Six-month review:

- More detailed review
- Examines issues such as reasonableness of procurement decisions and resulting charges
- PSC may disallow earlier charges because of factors such as improper calculations or unreasonable fuel procurement practices
- PSC can order unreasonable charges to be refunded through reductions in future FACs

THE FAC: KEY FACTS

Two-year review:

- Final review
- Resets baseline fuel cost if necessary
- Baseline reset does not increase total charges – reallocates from FAC to baseline KWH cost – monthly FAC charge or credit gets smaller
- Two-year FAC reviews (and six-month reviews) are conducted as cases before the PSC
- Public hearings
- Public comments permitted

Case No. 2014-00225

1. Kentucky Power Company (AEP)
2. Six-month review case
3. Hearing held 11/12/2014
4. Decision issued 1/22/2015
5. Not final – Kentucky Power can seek rehearing or file appeal

Case No. 2014-00225

Unusual circumstances

- First FAC review covering a portion of 17-month "overlap" period during which utility is operating both the Big Sandy #2 unit in Louisa and its 50% of the Mitchell plant in Moundsville, West Virginia
- Operating both plants creates surplus capacity
- Kentucky Power is trying to sell excess power into the open market

Case No. 2014-00225

1. Main issue was allocation of “no-load costs” – these are costs the utility says are incurred whenever a plant is running, regardless of power output
2. Kentucky Power allocates all no-load costs to its customers in Kentucky
3. Mitchell no-load costs were estimated to be about $54 million during the 17-month overlap period
4. Effects of Mitchell no-load cost allocation were not disclosed during the proceeding in which PSC approved Mitchell purchase to eventually replace Big Sandy #2
5. Intervenors (Kentucky Industrial Utility Customers & AG) argued for disallowing portion of Kentucky Power fuel costs

Case No. 2014-00225

PSC decision: what it did

- <u>Applies only to the overlap period</u>
- Disallowed Mitchell no-load costs as unreasonable
- Ordered refunds, via FAC, of $13 M collected during four months of overlap period within the six-month review period
- Barred future collection through May 2015, when Big Sandy #2 will cease operation
- Other amounts already collected to be addressed in future FAC reviews

Case No. 2014-00225

PSC decision: what it did not do

- Did not say that allocation methodology for no-load costs is inherently unreasonable – only that it produced unreasonable result when applied during overlap period
- Did not "impact (PSC) decision" that the Mitchell purchase "over the long term, still represents the lowest reasonable cost alternative" for replacing Big Sandy No. 2
- No-load cost allocation methodology will be reviewed in future proceedings

Thank you