



**Paul E. Patton, Governor**

**Janie A. Miller, Secretary  
Public Protection and  
Regulation Cabinet**

**Thomas M. Dorman  
Executive Director  
Public Service Commission**

**COMMONWEALTH OF KENTUCKY  
PUBLIC SERVICE COMMISSION  
211 SOWER BOULEVARD  
POST OFFICE BOX 615  
FRANKFORT, KENTUCKY 40602-0615  
www.psc.state.ky.us  
(502) 564-3940  
Fax (502) 564-3460**

**Martin J. Huelsmann  
Chairman**

**Gary W. Gillis  
Vice Chairman**

**Robert E. Spurlin  
Commissioner**

**August 29, 2002**

**Mr. Robert M. Carper  
General Manager  
Owensboro Municipal Utilities  
2070 Tamarack Road  
P.O. Box 806  
Owensboro, Kentucky 42302-0806**

**Dear Mr. Carper:**

This letter is in response to our conversation of several weeks ago when I spoke to the Municipal Electric Power Association of Kentucky ("MEPAK"). You mentioned the Commission's Administrative Case No. 387 and an issue raised in that proceeding by Owensboro Municipal Utilities ("OMU") regarding whether it was being charged market prices for the reserve margins or capacity made available to it under its agreement with Kentucky Utilities Company ("KU").

It is my understanding that, generally, KU meets the needs of firm requirements customers with its own generating capacity, and since its merger with Louisville Gas and Electric Company ("LG&E"), the available generating capacity of both companies. This is because the generating facilities of the two companies are operated and dispatched on a joint basis. However, there have been occasional instances, such as the summers of 1998 and 1999, when regional transmission constraints and extreme temperatures put pressure on utility systems throughout the Midwest, that utilities such as KU were required to purchase wholesale power to meet their customers' demands.

In those two summers, with increased volumes of north to south power flows across Kentucky, some generation and transmission facilities were constrained and wholesale power prices reached record levels. This resulted in utility customers, both wholesale and retail, incurring higher power bills, to the extent that their supplying utilities had to purchase some of this high-priced power to meet customers' demands. We certainly sympathize with the concerns of OMU; however, all evidence of which the Commission is aware points to those experiences as being isolated occurrences which are not reflective of normal operations by Kentucky's jurisdictional electric utilities.



**AN EQUAL OPPORTUNITY EMPLOYER M/F/D**

August 28, 2002  
Robert M. Carper  
Page Two


The Commission Staff's review of Administrative Case No. 387 reflects that OMU expressed concern about the level of the reserve margins being maintained by jurisdictional utilities and the increased reliance by those utilities on wholesale power purchases for their planned reserve margins. While utilities are relying on purchases to a greater degree to meet reserve margins, the Commission found, in its December 20, 2001 Order in Administrative Case No. 387, that KU and LG&E, have relied upon, and continue to rely upon, their own generation, plus baseload capacity available from OMU, EEI, and OVEC to meet their requirements, including reserve margins.

The Commission agrees with OMU and MEPAK that undue reliance on market-priced wholesale power would negatively impact customers of Kentucky's jurisdictional electric utilities. Given its statutory obligations to the ratepayers of those utilities, the Commission is mindful of the need to monitor and review the resource needs, and the mix of resources, of those utilities in a manner that will ensure that electricity continues to be provided to Kentuckians in a reliable, cost-effective manner. As I stated in my remarks to MEPAK, the Commission's concern about the volatility of market-priced power led it to pursue negotiations in cases involving The Union Light, Heat & Power Company and American Electric Power to lessen the impacts of those utilities' planned reliance on market-priced power to meet their customers' needs.

As long as Kentucky is not forced to restructure its electric industry, it is the intent of the Commission to guard against undue reliance on market-priced power or practices that might result in sending our low-cost generation outside our boundaries. However, as changes dictated by others continue to impact the industry and produce results that are not always beneficial to Kentucky, I must acknowledge that there is no guaranty that we will always be successful in these endeavors.

I hope letter is responsive to your concerns. If you desire further information of a more technical nature, please contact either Mr. Aaron Greenwell or Mr. Jeff Shaw of the Commission's Division of Financial Analysis. Otherwise, feel free to discuss these matters with me further if you so desire.

Sincerely,



Thomas M. Dorman  
Executive Director



AN EQUAL OPPORTUNITY EMPLOYER M/F/D