

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

AN INVESTIGATION INTO THE FUEL)
PROCUREMENT PRACTICES OF KENTUCKY) CASE NO. 9631
UTILITIES COMPANY)

O R D E R

On July 1, 1987, Kentucky Utilities Company ("KU") filed a Motion and supporting memorandum requesting that:

1. The scope of this investigation be limited to a determination of KU's prudence in administering its South East and River Processing coal contracts since April 1982, the date its fuel costs were last approved by Order of the Commission;

2. This investigation be held in abeyance pending the initial decision in Federal Energy Regulatory Commission ("FERC") Docket EL84-15-000;

3. Various consultants submitting bids on this investigation project be disqualified because of appearances and testimony against KU in prior regulatory proceedings;

4. The consultant's role be redefined to assure due process and give KU the opportunity to fully participate in the investigation, and the cost of the consultant be paid by the Commission.

On July 24, 1987, the Utility and Rate Intervention Division of the Attorney General's office ("AG") filed a memorandum in response to KU's Motion. The AG concurred in that part of KU's

Motion seeking to exclude certain consultants from consideration in this proceeding and opposed the remaining portions of the Motion.

A public hearing, for the purpose of presenting oral arguments on KU's Motion, was held on July 27, 1987. Participants at this hearing were KU, the AG and the Kentucky Industrial Utility Customers ("KIUC").

DISCUSSION OF ISSUES

Scope of Investigation

KU contends that this investigation should be limited to the prudence of its actions since April 1982, the date its fuel costs were last approved by Order of the Commission in a six-month review pursuant to 807 KAR 5:056, Section 1(11). The AG's memorandum states that the Commission's subsequent two-year review of KU's fuel costs, pursuant to 807 KAR 5:056, Section 1(12), resulted in an Interim Order that withheld approval of those two-year fuel costs pending further investigation. That Interim Order, entered in Case No. 8590, An Examination By The Public Service Commission Of the Fuel Adjustment Clause of Kentucky Utilities Company From November 1, 1980, to October 31, 1982, also put KU on notice that the fuel costs for those two years were subject to refund.

The Commission finds that every periodic Fuel Adjustment Clause ("FAC") review of KU starting with Case No. 8590 has resulted in Interim Orders imposing a potential refund obligation. The last time that the Commission approved KU's fuel costs in a

two-year review was for the two years ended October 1980. Consequently, all fuel revenues collected since November 1, 1980, have been collected subject to refund and those fuel costs are the subject of this investigation. Evaluating these fuel costs will obviously require a review of KU's fuel procurement practices in earlier years and this point was expressed by the Commission in the Request for Proposals ("RFP") appended to its Order entered May 1, 1987. The Commission finds KU's arguments on this issue to be unpersuasive and therefore the scope of this investigation should not be limited as requested by KU.

Abeyance Pending FERC Decision

KU argues that this investigation should be held in abeyance pending a decision by an administrative law judge ("ALJ") in a similar investigation of KU's fuel procurement practices before the FERC in Docket No. EL84-15-000. KU contends that by waiting for the ALJ's decision the Commission may avoid duplicative litigation on similar issues. KU also raises the question of whether the Commission would be collaterally estopped from investigating the same or similar matters as are being reviewed at the federal level.

The AG makes the point that this investigation is not limited to the matters before the FERC and that there is no authority by which this Commission could be estopped from investigating issues that are within its exclusive regulatory jurisdiction.

The Commission finds that its regulatory jurisdiction over KU is coexistent with, not duplicative of or inferior to, that of the FERC. This Commission's rate jurisdiction is exclusive with

respect to KU's retail electric sales in the Commonwealth of Kentucky, whereas FERC's jurisdiction is exclusive to KU's sales for resale. This Commission will not be bound by the decision of the ALJ or any subsequent decision in the FERC proceeding. As FERC itself has recognized, in a wholesale rate proceeding, FERC is not bound by any state commission's retail determination of prudence. Likewise, any FERC decision on prudence will not be binding on a state commission. See Monongahala Power Company, et al., 39 FERC [61,350 (1987)]. Furthermore, by KU's own admission at the oral argument, the ALJ's decision will almost certainly be appealed regardless of its outcome.

The Commission finds that concluding this investigation as expeditiously as possible is of utmost importance. It has been four years since the Commission granted KU's first request to delay this investigation. Further delay must be avoided and this investigation should proceed in a prompt and efficient manner. KU's request to hold this matter in abeyance should be denied.

Disqualification of Consultants

KU requested that six of the consultants bidding on this project be excluded from consideration because of their prior participation in regulatory proceedings involving KU. Such participation, it is alleged, renders the six consultants incapable of performing an independent and unbiased investigation. The AG concurred with KU's request with respect to two of the six consultants.

The Commission has considered the proposals submitted in this case, as well as the comments filed by KU and the AG. The

selection of a consultant lies solely within the Commission's discretion. The Commission will use its best judgment in making its choice, taking all factors into consideration. If either KU or the AG takes exception to the Commission's selection, their objections will be heard at that time. For now, all proposals are being considered and KU's request, as well as the AG's, should be denied.

Redefining the Role of the Consultant

KU claims that, pursuant to the RFP, the consultant's role will be both that of investigator and adjudicator. KU also claims that the consultant will have a financial incentive to find KU imprudent and that ex parte communication between the consultant and the Commission (and its staff) during the investigation will be a violation of due process. Lastly, KU contends that the Commission, not KU, should pay for the consultant's work.

The consultant in this proceeding will perform an investigation of KU's fuel procurement practices. After the investigation is concluded, the consultant will issue a report setting forth its findings, conclusions, and recommendations. It will not be until that point in time that KU will know whether its position is adverse to the consultant's. However, at no time during this proceeding will the consultant perform an adjudicatory role. The Commission alone will hear and weigh the evidence and decide the issues in this case.

The Commission finds no merit in KU's argument that the consultant will have a financial incentive to find KU imprudent.

While it is true that the consultant will be entitled to additional compensation if a public hearing is held, the need for a hearing is not tied to a finding of imprudency. The need for a hearing cannot be determined until the Commission and the parties have had sufficient time to review the consultant's report. However, based on the parties' statements at the oral argument, it appears that a hearing will be necessary whether the consultant concludes that KU was prudent or imprudent. The Commission finds that under these circumstances there is no financial incentive for the consultant's report to be anything but fair and impartial.

The consultant will not be in direct communication with the Commission. All communications will be through the Commission's designated project officer as set out in the RFP. As noted by KU in its memorandum, this communication will take place throughout the investigatory phase of this proceeding and in preparation of the consultant's report. If a hearing is necessary, the consultant will then be in a position similar to that of an adversarial party. At that time, the periodic communication between the consultant and the project officer will cease. There will be no opportunity for the due process violation claimed by KU to occur.

The consultant's cost should be paid by KU. Nothing within KRS 278.255 prevents an audit from being reviewed in a public hearing. The statute requires the audited firm to bear the costs incurred for the audit. These costs include the investigative report and, if necessary, any public hearings to review that

report. The directive that KU pay for the consultant's work is entirely consistent with KRS 278.255.

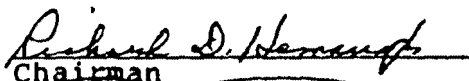
The Commission finds no compelling reason to redefine the role of the consultant in this proceeding or to expand KU's participation in the consultant's activities. To do either could bias or give the appearance of bias to the consultant's work. The Motion should be denied and KU should be required to pay for the consultant's work.

SUMMARY

The Commission, based on the evidence of record and being advised, HEREBY ORDERS that KU's Motion of July 1, 1987, be and it hereby is denied and the Commission's Order entered May 1, 1987, be and it hereby is affirmed in all respects.

Done at Frankfort, Kentucky, this 10th day of September, 1987.

PUBLIC SERVICE COMMISSION


Chairman


Vice Chairman


Commissioner

ATTEST:

Executive Director