

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

AMENDMENT NO. 1 TO THE AGREEMENT FOR)
ELECTRIC SERVICE BETWEEN HENDERSON)
UNION ELECTRIC COOPERATIVE AND) CASE NO. 94-313
COSTAIN COAL COMPANY)

O R D E R

On July 28, 1994, Henderson Union Electric Cooperative ("Henderson Union") filed Amendment No. 1 ("Amendment") to its Agreement for Electric Service ("Agreement") with Costain Coal, Inc. ("Costain") for Commission approval. The Amendment recognizes the construction of a second transmission line by Henderson Union's wholesale power supplier, Big Rivers Electric Corporation ("Big Rivers") to extend from Costain's substation yard to Costain's Asher Fan Substation. The Amendment also creates a security provision whereby Costain agrees to provide a bond or letter of credit equal to the sum of the termination charges and demand credits set forth in the Agreement but only in the event that Costain's net worth falls below twice the amount of the aforementioned charges and credits. The original Agreement, which covered the construction of a transmission line from Big Rivers' system to Costain's substation yard, did not include a security provision.¹ By Order entered August 25, 1994, the Commission suspended the Amendment pending further investigation and required

¹ Case No. 93-229, The Contract for Electric Service Between Henderson-Union Rural Electric Cooperative Corporation and Costain Coal Company, Order dated October 7, 1993.

Henderson Union to provide additional information regarding the terms of the Amendment.

In response to the Commission's Order, Henderson Union stated that Costain's current net worth exceeds \$1 million² and that the current termination charges and demand credits under the Agreement, as amended, were slightly less than \$500,000. Henderson Union also stated that Costain preferred that its net worth not be disclosed because of pending litigation in which Big Rivers is attempting to have its three coal supply contracts with Costain terminated. Henderson Union indicated it did not require a bond or letter of credit as a condition of entering the Amendment because it was attempting to keep the overall cost of service to Costain as low as reasonably possible while having adequate security for performance of the Agreement as amended.

Henderson Union indicated that Costain's three contracts with Big Rivers comprise only 15 percent of the total sales by Costain's western division and that the termination of those contracts would have a minimal impact on Costain's ability to meet its obligations under the Amendment. Henderson Union also indicated that the service provided under the original Agreement, as well as the Amendment, was to Costain's East Portal operation while the coal supplied Big Rivers came primarily from Costain's Smith operation.

In Case No. 93-229 Henderson Union's main arguments in support of the original Agreement were: (1) Costain's sound

² The support for this statement was a letter from Costain's independent auditor which indicated that its stockholders' equity was in excess of \$1,000,000 as of December 31, 1993.

financial condition; (2) the existence of the three long-term coal supply contracts between Costain and Big Rivers (from which Big Rivers could withhold payment in the event Costain did not fulfill its obligations under the Agreement); and (3) Costain's recent investment of \$52 million for the development of its area coal reserves. Based on these representations the Commission approved the Agreement. Now, one year later, it appears that two of the three representations are no longer valid.

Recent published reports that Costain is for sale highlight its deteriorating financial condition.³ With Costain declining to disclose its net worth the record does not truly reflect Costain's current financial condition. Nor does the record provide any evidence of Costain's ability to continue to operate under the type of losses it has reportedly incurred in the first half of this year. With Big Rivers seeking to terminate its coal supply contracts with Costain there is little likelihood that Henderson Union will retain any of the leverage it presently has, through Big Rivers, to enforce the terms of the Agreement. Given that Costain is reportedly for sale, and the uncertainties and risks inherent in such a situation, the fact that Costain invested \$52 million to develop its coal reserves may provide scant security for its unsecured obligation under the amendment.

³ The Late Kentucky Edition of The Courier Journal of September 14, 1994, page 8 of Section B and The State Journal of September 14, 1994, page 10 of Section A included reports that Costain was for sale and had incurred operating losses of \$15 million in the first half of 1993.

Given the uncertainties discussed above the Commission is not persuaded that the proposed Amendment provides adequate security for Henderson Union, or for Big Rivers. Therefore, it finds that the proposed Amendment should be rejected. Henderson Union should negotiate a satisfactory security provision and resubmit the Amendment within 60 days from the date of this Order.

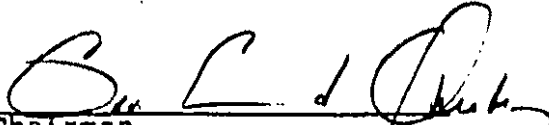
IT IS THEREFORE ORDERED that:

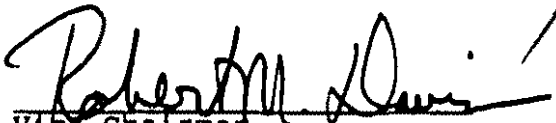
1. Amendment No. 1 to the Agreement for Electric Service between Henderson Union and Costain be and it hereby is rejected.

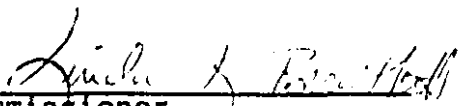
2. Henderson Union shall renegotiate and resubmit the Amendment within 60 days of the date of this Order.

Done at Frankfort, Kentucky, this 21st day of October, 1994.

PUBLIC SERVICE COMMISSION


Chairman


Vice Chairman


Commissioner

ATTEST:


Executive Director