

COMMONWEALTH OF KENTUCKY  
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

APPLICATION OF KENTUCKY POWER	)	
COMPANY FOR (1) A CERTIFICATE OF	)	
PUBLIC CONVENIENCE AND NECESSITY	)	
AUTHORIZING THE TRANSFER TO THE	)	
COMPANY OF AN UNDIVIDED FIFTY	)	
PERCENT INTEREST IN THE MITCHELL	)	
GENERATING STATION AND ASSOCIATED	)	CASE NO.
ASSETS; (2) APPROVAL OF THE	)	2012-00578
ASSUMPTION BY KENTUCKY POWER	)	
COMPANY OF CERTAIN LIABILITIES IN	)	
CONNECTION WITH THE TRANSFER OF THE	)	
MITCHELL GENERATING STATION; (3)	)	
DECLARATORY RULINGS; (4) DEFERRAL OF	)	
COSTS INCURRED IN CONNECTION WITH	)	
THE COMPANY'S EFFORTS TO MEET	)	
FEDERAL CLEAN AIR ACT AND RELATED	)	
REQUIREMENTS; AND (5) ALL OTHER	)	
REQUIRED APPROVALS AND RELIEF	)	

ORDER

On October 30, 2013, the Attorney General for the Commonwealth of Kentucky, by and through his Office of Rate Intervention ("AG"), filed a petition, pursuant to KRS 278.400, seeking a rehearing of the Commission's October 7, 2013 Order in the instant case. The October 7, 2013 Order approved Kentucky Power Company's ("Kentucky Power") application to acquire an undivided 50 percent interest in the Mitchell Generating Station from an affiliate, Ohio Power Company. The AG raises two primary arguments in support of his request for a rehearing.

### Argument of Attorney General

First, the AG contends that the Commission erred in relying upon the stacking analysis conducted by Kentucky Power of the conforming responses to the request for proposals (“RFP”) related to the disposition of Big Sandy Unit 1. The AG argues that bids from the Big Sandy Unit 1 RFP cannot be used as a basis to determine the reasonableness of the Mitchell acquisition. The AG asserts that the RFP required bidders to assume transmission costs and responsibility for any future compliance-related costs and to guarantee pricing and resource availability. The AG states that such costs are not applicable to the Mitchell acquisition because they would be recovered by Kentucky Power through its rates. The AG further argues that Kentucky Power failed to provide any evidence that the Mitchell transfer price satisfied KRS 278.2207, which requires any affiliate transaction to be priced at the lower of cost or market value.

Lastly, on the first argument, the AG proffers that rehearing is required to ensure that the due process rights of the AG are protected, contending that additional evidence is needed to determine the market value of the Mitchell Generating Station and whether the acquisition comports with Kentucky law.

In particular, the AG points out that the Commission retained an outside consultant to assist the Commission in its review and analysis of this case. Citing to<sup>1</sup> KRE 706, the AG argues that “[d]ue process requires that expert evidence relied upon by the Commission to arrive at its final decision be made public by way of presenting the Commission’s own retained expert and subjecting him/her to examination by the

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<sup>1</sup> Attorney General's Petition for Rehearing, at. 7.

intervening parties, including the Attorney General.” The AG contends that further examination should include the opportunity to conduct “discovery, testimony, depositions and/or cross-examinations of all witnesses and experts upon whom the Commission relied....”<sup>2</sup>

The AG’s second argument concerns the Superseding Mitchell Operating Agreement recently filed at the Federal Energy Regulatory Commission (“FERC”) on October 15, 2013 by American Electric Power Service Corporation (“AEP Service Corporation”) on behalf of Kentucky Power and AEP Generation Resources Inc. (“AEP Generation Resources”).<sup>3</sup> The Superseding Mitchell Operating Agreement reflects a change in the ownership structure of the Mitchell Generating Station. As contemplated in the original Mitchell Operating Agreement, Kentucky Power and its affiliate Appalachian Power Company (“APCo”) each would have owned a 50 percent undivided interest in the Mitchell Generating Station, with APCo being the operator of the Mitchell Generating Station. However, due to a decision by the State Corporation Commission of Virginia denying APCo’s request to acquire a half interest in the Mitchell Generating Station, the original Mitchell Operating Agreement has now been revised to provide that Kentucky Power and another affiliate, AEP Generation Resources, (rather than APCo) would each own a 50 percent undivided interest in the Mitchell Generating Station, and Kentucky Power (rather than APCo) would operate the Mitchell Generating Station. The October 15, 2013 FERC filing by AEP Service Corporation requests authority to

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<sup>2</sup> Attorney General’s Petition for Rehearing, at 7-8.

<sup>3</sup> FERC Docket No. ER-14-86.

withdraw the original Mitchell Operating Agreement and replace it with the Superseding Mitchell Operating Agreement.

The AG contends that a rehearing is required to address any potential additional costs, benefits, and risks of the Mitchell acquisition in light of the new ownership structure of the Mitchell Generating Station. The AG argues that additional evidence is required to evaluate these potential additional risks because the Commission in its October 7, 2013 Order did not consider any specific terms or conditions under which an operating agreement would contemplate Kentucky Power co-owning the Mitchell Generating Station with an unregulated, market affiliate. The AG avers that the Commission erred in failing to exercise its authority to consider whether the Superseding Mitchell Operating Agreement would be in compliance with Kentucky state law governing utility transactions with unregulated affiliates and whether the ratepayers of Kentucky Power would be harmed by that new agreement. The AG further contends that the Superseding Mitchell Operating Agreement may be in violation of federal law restricting affiliate transactions.

#### Response of Kentucky Power

On November 6, 2013, Kentucky Power filed a response in opposition to the AG's petition for rehearing. Kentucky Power contends that the AG's petition fails to raise any new evidence or present new issues that could not have been offered by the AG with reasonable diligence as required for the granting of a rehearing under KRS 278.400. With respect to the AG's argument concerning the stacking analysis, Kentucky Power avers that the AG raised the same argument in his post-hearing brief and presented no new evidence that could not be previously discovered with

reasonable diligence. Moreover, Kentucky Power argues that the AG had ample time and opportunity to raise any due process concerns but failed to do so until now. Concerning the Superseding Mitchell Operating Agreement, Kentucky Power asserts that the AG had a full and fair opportunity to raise any issues involving the co-ownership of the Mitchell Generating Station and AEP Generating Resources at the evidentiary hearing and in his post-hearing brief. Kentucky Power notes that it made clear at the evidentiary hearing and in responses to post-hearing data requests that in the event APCo was denied the authority to acquire the remaining 50 percent interest in the Mitchell Generating Station, such interest likely would remain with AEP Generation Resources. Therefore, a revised operating agreement would be filed with FERC reflecting such ownership structure. Kentucky Power also contends that the AG's request to conduct discovery on the role of the Commission's retained consultant could have been raised at any time after the Commission formally notified Kentucky Power and the parties to this case on February 4, 2013, of its intent to retain a consultant,<sup>4</sup> but that the AG failed to timely do so and cannot raise this issue for the first time on rehearing.

In addition to failing to satisfy the minimal requirements for rehearing, the AG's petition provides no substantive grounds to support a grant of rehearing. With respect to the AG's criticism that the Commission erred in relying on the stacking analysis as a basis for determining the market value of the Mitchell acquisition and that the Mitchell acquisition is the least-cost alternative, Kentucky Power contends that the AG's argument is flawed because it ignores the significant compelling testimony to the

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<sup>4</sup> February 4, 2013, Letter from Jeff Derouen, Executive Director of the Commission, to Greg Pauley and the parties to this case.

contrary. This includes testimony by a witness for the Kentucky Industrial Utility Customers, Inc. that the result of the Big Sandy Unit 1 RFP is a very good indicator of pricing and availability of what could be expected in an RFP to replace Big Sandy Unit 2. Further, Kentucky Power's robust economic modeling provided benchmarks that adequately represented the response to any RFP process. This methodology determined by a wide margin that the Mitchell acquisition was the least-cost option and demonstrated that the market value of the Mitchell Generating Station exceeded its net book value. Also Kentucky Power's break-even analysis supports the Commission's decision.

Kentucky Power also contends that the AG's argument regarding the modified ownership structure and the Superseding Mitchell Operating Agreement is without merit. Kentucky Power argues that the AG offers no evidence identifying any potential risk associated with Kentucky Power co-owning the Mitchell Generating Station with AEP Generation Resources and provides no specific explanation as to how Kentucky Power's customers would be harmed. Kentucky Power points out that the AG offered no objections regarding the original operating agreement and that the revised operating agreement is substantially based upon the original agreement, including provisions that would continue to reflect the costs attendant to Kentucky Power's ownership and operation of the undivided 50 percent ownership in the Mitchell Generating Station.

#### Reply of the Attorney General

On November 12, 2013, the AG filed a reply memorandum in support of his petition for rehearing. The AG contends that the language of KRS 278.400 specifically authorizes any party to apply for rehearing with respect to any matters determined by

the Commission. The AG maintains that he has set forth clear errors of fact and law entitling him to a rehearing of the Commission's October 7, 2013 Order. The AG argues that the Commission erred in relying upon the stacking analysis conducted by Kentucky Power, which analysis could not be independently verified. The AG asserts that the Commission failed to consider whether the Superseding Mitchell Operating Agreement violates Kentucky and federal law governing affiliate transactions and whether such an agreement would benefit Kentucky Power's shareholders at the expense of its ratepayers.

#### Commission Findings

Having reviewed the pleadings and being otherwise sufficiently advised, the Commission finds that KRS 278.400 expressly limits the new evidence that the Commission can consider on rehearing by providing that, "Upon the rehearing any party may offer additional evidence that could not with reasonable diligence have been offered on the former hearing." As the Commission has previously held, KRS 278.400 "is intended to provide finality to Commission proceedings by limiting rehearing to new evidence not readily discoverable at the time of the original hearing."<sup>5</sup> Thus, on rehearing, a party may present "newly discovered evidence" which has been judicially defined to be limited to evidence that existed at the time of the former hearing, not "new evidence" which did not exist at the time of the former hearing.<sup>6</sup> Based on this standard, the Commission finds that the AG has not alleged the existence of any newly discovered evidence to justify granting rehearing. Further, the AG has not shown that

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<sup>5</sup> Case No. 2008-00250, Proposed Adjustment of the Wholesale Water Service Rates of Frankfort Electric and Water Plant Board (Ky. PSC Apr. 27, 2009), at 3.

<sup>6</sup> *Stephens v. Kentucky Utilities Co.*, 569 S.W.2d 155, 158 (Ky. 1978).

the findings in our October 7, 2013 Order are not supported by substantial evidence or that the AG was denied due process during the proceedings.

With respect to the issue raised surrounding Kentucky Power's stacking analysis, we note that the analysis was not filed by Kentucky Power on its own initiative or upon request by an intervenor. Rather, the stacking analysis was filed in response to the Commission's May 28, 2013 Order continuing the evidentiary hearing until July 10, 2013 and directing Kentucky Power to file no later than June 28, 2013, an economic analysis of the bids received in response to its Big Sandy Unit 1 RFP. The May 28, 2013 Order also specifically noted that the responses to this RFP should provide useful information regarding the current availability and pricing of long-term generation and would assist the Commission in determining the reasonableness of the Mitchell acquisition. Kentucky Power complied with that directive and filed an economic analysis of the responses to the Big Sandy Unit 1 RFP on June 28, 2013, along with supporting testimonies. Thus, the parties to this matter, including the AG, were placed on notice of the potential significance of Kentucky Power's economic analysis of the bids to the Big Sandy Unit 1 RFP and all parties had sufficient opportunity from May 28, 2013, until July 10, 2013, to raise any issues in connection with this economic analysis. Notwithstanding this significant time period, the AG never requested an opportunity to conduct discovery during the seven-week period before the evidentiary hearing, or at any time during the three-day evidentiary hearing, but has now instead sought discovery for the first time on rehearing.

The Commission also finds no merit in the AG's argument that the stacking analysis is unreliable and therefore the Commission erred in relying on that analysis in

finding that the Mitchell acquisition is reasonable and is the least-cost alternative. As noted in the October 7, 2013 Order, the Commission's ultimate finding that the Mitchell acquisition was reasonable and the least-cost alternative was based on the substantial evidence of record which included, among other things, Kentucky Power's use of Strategist, a highly sophisticated economic modeling tool accepted industry-wide, to conduct a robust and comprehensive economic analysis of the Mitchell acquisition; the fact that Kentucky Power's economic analysis took into account a wide range of reasonable alternatives, including a market proxy alternative to provide a reasonable means of determining the relationship between the net book value of the Mitchell assets and its fair market value; sensitivity and break-even analyses performed by Kentucky Power to stress the underlying assumptions used by Kentucky Power in its economic modeling; and the impairment analysis, which was reviewed by external auditors and which revealed that the book cost of the Mitchell Generating Station was less than its fair market value. Thus, even if the stacking analysis is excluded from the Commission's discussion, there is substantial evidence of record to support the reasonableness of the Mitchell acquisition.

The Commission also finds that the AG is not entitled to take discovery, including depositions or cross-examination, of the Commission's retained consultant. As Kentucky Power points out, the Commission formally notified Kentucky Power and the parties to this matter by letter of its intent "to retain the services of a consultant to assist the Commission Staff in reviewing the evidence compiled in this case and providing advice to the Commission."<sup>7</sup> The February 4, 2013 letter also provided that any

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<sup>7</sup> February 4, 2013, Letter from Jeff Derouen, Executive Director of the Commission, at 1.

objections from any party to this matter to the Commission's intent to retain a consultant should be filed in the record within seven days from the date of the letter. The scope of the retained consultant's engagement was set forth in the February 4, 2013 letter and was limited to assisting Commission Staff in its review and analysis of the evidentiary record and providing advice and consultation to the Commission. Thus, the Commission's consultant was performing the same role that the Commission Staff performs, i.e., reviewing evidence and advising the Commission. We have long held that, as a general rule, Commission Staff cannot be subject to cross-examination.

Staff is an arm of this Commission; it is not an adversary party to a proceeding before us. Commission Staff could no more be subject to cross examination than could the law clerks of a judge or the staff attorneys of an appellate court. To allow such a procedure at this Commission would inhibit the free flow of ideas between staff members and Commissioners which is crucial to the functioning of our agency.<sup>8</sup>

In light of the fact that the retained consultant acted as an extension of Commission Staff and did not file any testimony, the Commission's retained consultant cannot be subject to discovery or cross-examination in this matter. Moreover, the AG had ample opportunity to raise any due process concerns with the Commission's decision to retain an outside consultant to assist the Commission in reviewing this matter. The AG failed to timely do so and is therefore foreclosed from raising this issue on rehearing.

Lastly, we find that the Superseding Mitchell Operating Agreement is not formally before the Commission for approval but is subject to the jurisdiction of the FERC. The

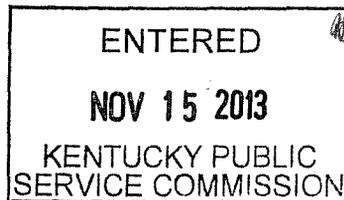
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<sup>8</sup> Case No. 7867, Application of Kentucky Water Service Company, Inc. to Continue Short-Term Financing of \$2,300,000; and Notice of Adjustment of Rates in Somerset, Middlesboro, and Clinton, Kentucky (Ky. PSC Nov. 5, 1982), at 2-3.

AG's petition for rehearing states that he has intervened in the FERC case established to review the Superseding Mitchell Operating Agreement, and we agree that FERC is the appropriate forum for the AG's issues to be raise and reviewed. We note that Kentucky Power has on file with the Commission a cost-allocation manual.<sup>9</sup> Moreover, the Superseding Mitchell Operating Agreement, which was not filed until after the Commission issued its October 7, 2013 Order, is not newly discovered evidence because it did not exist at the time of the July 10-13, 2013 evidentiary hearing. The agreement is new evidence that did not exist at the time of the hearings. It is outside the scope of the rehearing statute and cannot now be considered on rehearing.

IT IS THEREFORE ORDERED that the AG's petition for rehearing is denied.

By the Commission



ATTEST:

A handwritten signature in black ink, appearing to be "M. J. ...", written over a horizontal line. Below the signature is another horizontal line.

Executive Director

<sup>9</sup> See Kentucky Power's Application, at Volume 1-A, filed in Case No. 2009-00459, Application of Kentucky Power Company for a General Adjustment of Electric Rates.

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