COMMONWEALTH OF KENTUCKY
BEFORE THE KENTUCKY STATE BOARD ON
ELECTRIC GENERATION AND TRANSMISSION SITING

In the Matter of:

THE APPLICATION OF THOROUGHBRED	**)**	
GENERATING COMPANY, LLC FOR A MERCHANT	**)**	**CASE NO. 2002-00150**
POWER PLANT CONSTRUCTION CERTIFICATE	**)**	
IN MUHLENBERG COUNTY, KENTUCKY	**)**	

POST-HEARING BRIEF
OF KENTUCKY UTILITIES COMPANY
AND LOUISVILLE GAS AND ELECTRIC COMPANY

November 24, 2003

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Pursuant to the procedural schedule adopted at the evidentiary hearing held on November 10, 2003, Kentucky Utilities Company ("KU") and Louisville Gas and Electric Company ("LG&E") (collectively referred to at times as the "Companies") hereby submit their post-hearing brief in the above-captioned proceeding. The Companies' interest in this proceeding, although limited in focus, raises an issue of fundamental importance to this state and its utilities' customers, namely, the proper allocation of costs associated with merchant plant development. In short, KU and LG&E urge the Siting Board to ensure (through the measures described below) that their customers are not burdened with construction costs incurred *solely* to accommodate the Facility proposed by Thoroughbred.

I. Issue Presented

The singular issue raised by KU and LG&E in this proceeding pertains to cost recovery. As discussed below, under existing federal law, KU and LG&E must refund to Thoroughbred all monies collected upfront from Thoroughbred associated with transmission system upgrades constructed solely to accommodate the Facility, *regardless* of whether Thoroughbred purchases

transmission service through KU's and/or LG&E's transmission system(s). KU and LG&E submit that, unless the refund obligations imposed on them under federal law can be lawfully excused or waived, as described below, Thoroughbred will be unable to comply with state law, and a siting certificate cannot issue.

II. Standard of Compliance: Relevant State Law

With respect to merchant plant development in Kentucky, state law provides, in pertinent part, as follows:

> [n]otwithstanding any other provision of law, any costs or expenses associated with upgrading the existing electricity transmission grid, as a result of the additional load caused by a merchant electric generating facility, shall be borne solely by the person constructing the merchant electric generating facility and shall in no way be borne by the retail electric customers of the Commonwealth.

KRS 278.212 (2003). Thoroughbred has advised the Board that it will "comply with all requirements of Kentucky law," including, presumably, KRS Section 278.212, "if it is granted a Construction Certificate in this matter." Post-Hearing Data Request submitted November 17, 2003, at 2. Unfortunately, however, as discussed below, Thoroughbred's understanding of federal law is misguided, rendering its commitment to comply with state law notably suspect.

III. KU's and LG&E's Obligations Under Federal Law

KU and LG&E are "public utilities" subject to the jurisdiction of the Federal Energy Regulatory Commission ("FERC") under the Federal Power Act ("FPA"). Accordingly, the FERC, by its exercise of authority over the terms and conditions of electric generator interconnections, will necessarily play a key role in assigning cost responsibility for transmission system upgrades required on either utility's system to accommodate Thoroughbred's Facility.

On July 24, 2003, in Order No. 2003, the FERC revised its regulations under the FPA to implement new rules governing generator interconnections to the transmission grid.[1] Among other things, these rules speak directly to how the costs of transmission system upgrades required to accommodate such generators are allocated as between (i) the generator (i.e., the "Interconnection Customer") and the transmission owner/provider with which the generator directly interconnects; and (ii) the generator and the "Affected System" owner/operator (the "downstream" transmission owner whose facilities may be affected by the generator's interconnection with the transmission provider/owner.)[2]

Under the current generator interconnection plan (*see* Williams Direct Testimony at 8), KU's transmission system is an "Affected System" that will experience an "Adverse System Impact" when the Facility commences operation unless specific "Network Upgrades" are constructed on the transmission system to accommodate the Facility's output.[3] *See* System Map distributed October 21, 2003 (depicting transmission line upgrades as identified in Thoroughbred Energy Campus Interconnection Study); Commonwealth Associates Interconnection System

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[1] Order No. 2003, FERC Stats & Regs. ¶31,146 (2003). Appended to Order No. 2003 are standardized Large Generator Interconnection Procedures ("LGIP") that establish the procedures governing the interconnection process; and a standardized Large Generator Interconnection Agreement ("LGIA") that "sets forth the legal rights and obligations of each party, addresses cost responsibility issues, and establishes a process for resolving disputes." Order No. 2003, slip op. at 1-2. The FERC has required that all public utilities submit "compliance filings" that add the LGIP and the LGIA standard templates to the utilities' FERC-jurisdictional tariffs. Because KU and LG&E are currently members of the Midwest Independent Transmission System Operator, Inc. ("MISO"), MISO will be filing on behalf of both utilities.

[2] Order No. 2003 defines "Affected System" as "an electric system other than the Transmission Provider's System that may be affected by the proposed interconnection." Order No. 2003, Standard LGIA, at 3.

[3] "Adverse System Impact" is defined under Order No. 2003 as "the negative effects due to technical or operational limits on conductors or equipment being exceeded that may compromise the safety or reliability of the electric system." Order No. 2003, Standard LGIA at 3. "Network Upgrades" as defined in Order No. 2003 include any additions, modifications and upgrades to the transmission system required to accommodate the interconnection of the generating facility. Although the definition refers specifically to construction required on the transmission provider's system (with which the generator interconnects directly), the quote from Order No. 2003 referenced herein (page 2) makes clear that the FERC intends to apply the same definition to Affected Systems.

Impact Study, included in Section 5.4 of Thoroughbred Application submitted July 18, 2003. Specifically, the Facility, although directly interconnecting with Big Rivers Electric Corp. ("BREC"), will require the construction of a 345 kV interconnection between KU and BREC, as well as other transmission system upgrades east of this interconnection, to accommodate delivery of the Facility's output through BREC's system without degrading the reliability of KU's transmission system. *See id.*

Regarding such upgrade costs, the FERC in Order No. 2003 clarified that Affected Systems must assume full responsibility for these costs, *even where*, as here,[4] the generator has not agreed to purchase transmission service through the Affected System (thereby providing a means of partially offsetting such costs). Specifically, under Order No. 2003, although an Affected System owner/operator may require the generator to pay "upfront" for system upgrades required to accommodate the latter's generation facility, the Affected System owner/operator must, within (at most) five years, *refund the entire amount to the generator* (including interest):

> The [LGIP and LGIA included in the FERC's proposed rulemaking] included no pricing provisions that specifically address situations where Network Upgrades must be constructed on Affected Systems to protect the reliability of those systems. However, the [FERC] concurs . . . that the . . . LGIA should be modified to expressly allow for refunds to be provided to the Interconnection Customer when such Network Upgrades must be constructed, and the Interconnection Customer is required to pay for them. Therefore, the Commission modifies Article 11.4 of the Final Rule LGIA to make it applicable to all jurisdictional Affected System Operators on whose systems Network Upgrades are constructed to accommodate the Interconnection Customer's Interconnection Request. This means that, prior to the Commercial Operation Date, an Affected System Operator

[4] *See* Tr. at 74 (Thoroughbred witness Williams noting that it is "unclear at this point" whether Thoroughbred would purchase transmission service over KU's transmission system; Tr. at 75 (Thoroughbred witness Williams noting that "[i]t's unclear who we are going to sell to, *to the north at this time*, because no one has entered into contracts") (emphasis added). Deliveries to the north, through BREC into Cinergy Corp.'s service territory, clearly would not require transmission through KU's or LG&E's transmission system. *See* System Map distributed October 21, 2003.

> may require the Interconnection Customer to pay for all Interconnection Facilities and Network Upgrades constructed to accommodate the Interconnection Customer's Interconnection Request. *Then, upon commencement of commercial operation, any Affected System Operator that has received payments from the Interconnection Customer must begin to refund to the Interconnection Customer the costs of Network Upgrades that the Interconnection Customer has paid.* ***Furthermore, refunds are to be provided without regard to whether the Interconnection Customer has contracted for delivery service on the Affected System Operator's Transmission System.*** *If the Interconnection Customer has not contracted for delivery service, and in the absence of another mutually agreeable payment schedule, refunds shall be provided by means of a uniform stream of monthly payments designed to fully reimburse the Interconnection Customer, with interest, over a five-year period commencing with the Generating Facility's Commercial Operation Date.*

Order No. 2003, slip op. at 145 (emphases added). The language of the standard LGIA elaborates on this finding (Section 11.4.2) (emphases added):

> ***Refunds are to be made without regard to whether the Interconnection Customer contracts for transmission service on the Affected System.*** If the Interconnection Customer does not contract for transmission service, and in the absence of another mutually agreeable payment schedule, refunds shall be established at a level equal to the Affected System's rate for firm point-to-point transmissions service multiplied by the output of the Large Generating Facility assumed in the Interconnection Facilities Study. All refunds must be paid within five years of the Commercial Operation Date.

In so ruling, the FERC ignored claims that its "credit back" policy unfairly burdens the customers of affected transmission owners by requiring the latter to subsidize the cost of upgrades constructed solely to accommodate the generator, relying largely on its pro-competitive market stance to support its decision. *See* Order No. 2003, slip op. at 130-145.

Thoroughbred, in its response to the Board's post-hearing data requests, attempts to reconcile KU's "credit back" obligation under FERC Order No, 2003 with Thoroughbred's obligation under state law to assume full responsibility for all upgrade costs as follows:

> Thoroughbred's receipt of transmission credit does not require that retail electric customers bear any cost of the network upgrades associated with Thoroughbred's proposed facility *because Thoroughbred only receives any such credit if it obtains transmission service from those utilities that install network upgrades in order to accommodate Thoroughbred's interconnection request.*

Thoroughbred Post-Hearing Data Request Response dated November 17, 2003, at 4 (emphasis added). As the above-quoted language from FERC Order No. 2003 makes clear, however, this statement is simply not correct. *See also* Tr. at 81 (Thoroughbred counsel noting that "the state of Kentucky's consumers would not be impacted because we're giving other revenues to offset the costs that were originally incurred"). It necessarily follows that where Thoroughbred is not "giving other revenues to offset the costs that were originally incurred" (*see* note 4), Kentucky's customers are indeed adversely affected.

With regard specifically to the Thoroughbred project as it affects KU, the FERC will enforce the rules set forth in Order No. 2003, or address any proposed departure therefrom, in ruling on the agreement governing the upgrade construction that KU must file and obtain approval of as a FERC-jurisdictional entity.[5] Specifically, the terms and conditions governing the upgrade construction, including the parties' respective cost responsibility, will be set forth in a construction agreement entered into directly with Thoroughbred, or will otherwise be incorporated into the interconnection agreement between KU and BREC. In the latter case,

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[5] Because KU is currently a member of MISO, MISO will likely be a third-party signatory to the agreement KU files at FERC. If the parties cannot agree on the allocation of cost responsibility, KU will file an unexecuted agreement, and the FERC will resolve the issue either summarily or after the completion of hearing procedures.

At hearing, BREC witness Housley stated that "FERC-jurisdictional companies are compelled short of a bilateral agreement" to file interconnection agreements at FERC. Tr. at 219. KU and LG&E take strong exception to this statement: as a FERC-jurisdictional entity, KU will be required by law to file and seek FERC approval of any bilateral agreement between KU and BREC, or otherwise between KU and Thoroughbred, regarding transmission upgrades on KU's system. LG&E would be subject to the same obligation should transmission system upgrades be required on its system.

BREC will act, in effect, as a conduit, incorporating the same terms in its interconnection agreement with Thoroughbred. *See* Order No. 2003 at 145:

> When the Interconnection Customer is required to pay for Network Upgrades on an Affected System, it must enter into an agreement with the Affected System Operator unless the payments are incorporated in the interconnection agreement that the Interconnection Customer signs with the Transmission Provider [BREC]. Any agreement with an Affected System Operator must specify the terms governing payments to be made by the Interconnection Customer as well as the payment of refunds by the Affected System Operator.

Consistent with this finding, Section 11.4.2 of the FERC's standard LGIA provides, in pertinent part as follows:

> Special Provisions for Affected Systems. Unless the Transmission Provider [BREC] provides, under the LGIA, for the payment of refunds for amounts advanced to [the] Affected System Operator for Network Upgrades, the Interconnection Customer and Affected System Operator shall enter into an agreement that provides for such payment. The agreement shall specify the terms governing payments to be made by the Interconnection Customer to the Affected System Operator as well as the payment of refunds by the Affected System Operator.[6]

IV. Requested Relief

As KU will be bound by the FERC's ruling on the agreement filed by KU as described above, KU and LG&E submit that any certificate issued by the Board authorizing construction of the Facility must be conditioned on KU's receipt of, and Thoroughbred's acceptance of, a final FERC order waiving the above-described refund/crediting rules or otherwise permitting

[6] At hearing, Thoroughbred's witness suggested that, because FERC Order No. 2003 imposes "credit back" obligations on KU, any conflict between federal and state law as described herein is, in effect, KU's problem -- *i.e.*, KU has the "option to comply" with its obligations under federal law. *See* Tr. at 83. Such a suggestion is absurd. KU obviously cannot be placed in the untenable position of violating, or otherwise required to violate, federal law simply to allow Thoroughbred to comply with its obligations under KRS 278.212.

Thoroughbred to assign back to KU any credits owed under Order No. 2003.[7] Absent such order, Thoroughbred will be unable to comply with state law, and a siting certificate should not issue. *See* KRS Section 287.212.

Respectfully submitted,

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Linda S. Portasik

On behalf of
Louisville Gas and Electric Company
and Kentucky Utilities Company

[7] A final FERC order is a FERC order that is no longer subject to further proceedings before the FERC, *i.e.*, an order is deemed final as of the date rehearing is denied, or the date on which the right to seek rehearing expires.

CERTIFICATE OF SERVICE

The undersigned hereby certifies that on this day a true and correct copy of the foregoing brief was served by first class mail on the persons named on the official service list in this proceeding.

Dated: November 24, 2003.

Counsel for
Louisville Gas and Electric Company
and Kentucky Utilities Company