

1 FERC promulgated its currently-effective interconnection policy in July 2003 when it issued its final
2 rule in a rule making concerning the standardization of interconnection agreements and procedures
3 for large generators. In the Final Rule, FERC affirmed most of its preexisting interconnection-
4 related policies and clarified other aspects of its policy.

5 FERC's policy, articulated in the Final Rule, is as follows:

- 6 ● Direct Cost Assignment for Interconnection Facilities. The transmission provider
7 (public utility or non-public utility) may directly assign to the interconnection
8 customer all costs of "interconnection facilities," which are defined as all
9 interconnection-related facilities located between the generating facility and the point
10 of interconnection. The customer bears all such costs and does not earn any
11 transmission credits for its payment. Final Rule ¶¶ 676, 693.
- 12 ● Initial Cost Assessment for Network Upgrades. The transmission provider (public
13 utility or non-public utility) may assess the cost of all "network upgrades," which are
14 defined as all interconnection-related facilities and equipment located at and beyond
15 the point of interconnection needed to accommodate the interconnection of the
16 generating facility, against the interconnection customer. Final Rule ¶¶ 676, 693.
17 FERC expects that the transmission provider typically will roll into its transmission
18 rates the cost of network upgrades, and the payment of transmission credits will
19 ensure that the transmission provider will not cause the interconnection customer to
20 pay both the incremental cost of the upgrade (the up-front payment) and the
21 embedded cost of the upgrade (the component of a rolled-in transmission rate
22 attributable to the upgrade), which would violate FERC's transmission pricing policy
23 against "and" pricing (i.e., charging both an incremental rate and an embedded rate).
24 Final Rule ¶ 694.
- 25 ● Public Utility Transmission Credit Obligation. Public utility transmission providers
26 that have assessed the cost of network upgrades against the transmission customer are
27 required to pay the customer a cash equivalent refund (i.e., credit) equal to the total
28 amount paid for the network upgrades, including any tax gross-up or other tax-related

1 payments. The refund must be paid to the interconnection customer on a dollar-for-
2 dollar basis, as credits against the interconnection customer's payments for
3 transmission services, with the full amount to be refunded, with interest, within five
4 years of the date the network upgrades are placed in service, so long as the
5 transmission provider continues to receive payments for transmission service with
6 respect to the generating facility during this period. Final Rule ¶¶ 676, 693.

- 7 ● Five-Year Payment of Transmission Credits. Regarding the specific rules for a public
8 utility's payment of credits, FERC clarified in the Final Rule that the interconnection
9 customer is entitled to a full refund of the payments it makes toward the cost of
10 network upgrades within five years after the generator's commercial operation date,
11 as long as the generating facility remains in operation through the five year period.
12 During the five year period, credits must be awarded by the public utility on a dollar-
13 for-dollar basis as payments are made for transmission services. FERC also permits
14 the payments to be made on any other basis that is mutually agreeable to the
15 Interconnection Customer and the Transmission Provider. Final Rule ¶ 720.
- 16 ● Lump Sum Payment of Credits Balance After Five Years. Public utility transmission
17 providers must make a lump-sum payment to the interconnection customer for any
18 balance owed to the interconnection customer five years after the interconnection
19 customer has begun commercial operation. Final Rule ¶ 721.

20 FERC's policies can negatively affect retail customers in different ways. First, FERC deems
21 all interconnection-related equipment, facilities, and upgrades located at and beyond the point of
22 interconnection to constitute "network upgrades." FERC requires public utility transmission
23 providers to give transmission credits to interconnection customers with respect to the costs of those
24 facilities, forcing public utilities and their customers to subsidize the interconnection customer under
25 some circumstances, irrespective of whether they utilize or benefit from the upgrades. This
26 subsidization can cause inefficient generation siting decisions and can force utilities and their
27 customers to absorb the cost of "network upgrades" that primarily benefit the generation customer,
28 but not the utility and its customers. In the event the network upgrades serve solely to permit the

1 generator to export its power off-system, the utility and its customers will obtain no benefit from
2 them, but they could bear the cost of them.

3 Second, where a utility is required to pay a cash refund to an interconnection customer at the
4 end of five years because the generator has ceased operations and ceased taking transmission service
5 from the utility, the utility and its customers will be left with the financial burden of the refund
6 without the prospect of future use of the transmission system by the interconnection customer. An
7 interconnection customer that underutilizes the upgrades added for it will also receive a cash refund.

8 Finally, the utility and its customers would also be prejudiced under those circumstances by
9 the continuation of operation and maintenance expenses associated with the upgraded facilities to
10 which the interconnection customer either does not contribute, or under-contributes. Under FERC's
11 transmission pricing policy, a transmission provider cannot directly assign to a customer the cost of
12 operating and maintaining network facilities. Rather, O&M costs for network facilities must be paid
13 by all transmission customers. Accordingly, BREC could not charge Thoroughbred for O&M costs
14 for network upgrades even if BREC charges Thoroughbred the cost of constructing those upgrades,
15 so BREC and its transmission customers assume those costs.

16 Big Rivers' rates and tariffs are not subject to FERC jurisdiction under the Federal Power
17 Act. In the Final Rule FERC reiterated its long-standing reciprocity requirements by which non-
18 public utilities that wish to take open access transmission system on public utility systems must have
19 reciprocity tariffs on file with FERC with rates, terms, and conditions comparable to FERC's pro
20 forma tariff (Big Rivers has such a reciprocity tariff on file with FERC). In the Final Rule, FERC
21 holds that a non-public utility that has a "safe harbor" reciprocity tariff can add to its tariff FERC's
22 standardized interconnection procedures and interconnection agreement "if it wishes to continue to
23 qualify for safe harbor treatment." However, with respect to transmission credits, FERC does not
24 require that a non-public utility also provide transmission credits for network upgrades in order to
25 satisfy FERC's reciprocity requirements. Final Rule ¶ 843. To the contrary, FERC expressly held
26 that "[w]e do not require . . . that a non-public utility also provide transmission credits for Network
27 Upgrade costs, to satisfy the Commission's reciprocity condition." *Id.*

28 So what is Big Rivers' position about the relief that the Siting Board should grant to protect

1 Big Rivers and its customers? Thoroughbred is clearly responsible for all directly-assignable costs
2 incurred to interconnect its generating facility with the Big Rivers system (costs for interconnection
3 facilities installed behind the point of interconnection), with no right to credits. Big Rivers believes
4 that it and Thoroughbred are in agreement on this point.

5 As to the costs of networks upgrades (facilities located at and beyond the point of
6 interconnection), the Final Rule gives Big Rivers three options. The first is to follow the rules
7 applicable to FERC-jurisdictional public utilities. This would require Thoroughbred to pay up front
8 the costs of network upgrades. Big Rivers would then (a) roll the costs of those upgrades into Big
9 Rivers' transmission rate base, (b) charge Thoroughbred the new transmission rates for use of the
10 Big Rivers' transmission system, and (c) give Thoroughbred transmission credits equal to the cost of
11 the network upgrades over five years, with a cash payment to Thoroughbred at the end of that five
12 years of the balance of any un-refunded credits. This option is unworkable because any cash
13 payment made by Big Rivers at the end of the five years would be unrecoverable from its customers
14 through its rates for service. Thus, Big Rivers would have no source of revenue to pay such a cash
15 refund.

16 The second option available to Big Rivers under the Final Rule is (a) to require
17 Thoroughbred to pay up front the costs of network upgrades, (b) to not roll the costs of those
18 upgrades into Big Rivers' transmission rate base, (c) charge Thoroughbred Big Rivers' existing
19 transmission rates for use of the existing Big Rivers' transmission system, and (d) to give
20 Thoroughbred no transmission credits. This is the option that Big Rivers will ask the Siting Board to
21 include in its order, because it is the only option of these three that Big Rivers believes the Siting
22 Board has the authority to order consistent with KRS 278.212(2).

23 The third option is for Big Rivers and Thoroughbred to voluntarily enter into an
24 interconnection agreement that falls somewhere between options one and two, and in which
25 Thoroughbred waives any right it may have to later object to the arrangement agreed upon. Any
26 interconnection agreement would have to be approved by the Kentucky Public Service Commission,
27 however, and found to be consistent with KRS 278.212(2). Big Rivers cannot risk incurring
28 unrecoverable transmission upgrade costs that are prohibited by law from being included in Big

1 Rivers' rates, to handle the load of Thoroughbred's facilities. This option could work if an
2 acceptable agreement could be reached between Big Rivers and Thoroughbred. Neither the Final
3 Rule, nor FERC's rules in general, prohibit an interconnection customer from waiving a right to
4 which it otherwise may be entitled. Moreover, because Big Rivers is not a FERC-jurisdictional
5 public utility for Federal Power Act purposes, it will not be required to file its Thoroughbred
6 interconnection agreement with FERC, and any such waiver will not be subject to FERC review.

7 **DATA REQUEST NO. 2:** What would be FERC's role, if any, and how would it
8 become involved in resolving any issues between the parties, disputed or otherwise, related to the
9 payments of the costs of transmission upgrades required by Thoroughbred's proposed Facility?

10 **RESPONSE:**

11 FERC's role in a dispute involving the payment of the costs of transmission upgrades
12 required by Thoroughbred's proposed Facility likely would be in the context of a proceeding to
13 determine whether FERC's interconnection pricing and transmission pricing policies are fully
14 applicable to Big Rivers, a non-public utility. In such a proceeding, FERC presumably could seek to
15 apply its policies applicable to public utilities to Big Rivers.

16 As a non-public utility, Big Rivers is not subject to FERC's jurisdiction under the Federal
17 Power Act. Big Rivers therefore would not be required to file an interconnection agreement with
18 Thoroughbred with FERC, and FERC would not become involved in the resolution of
19 interconnection-related rate issues in the same manner as it routinely becomes involved in
20 interconnection-related rate issues where the interconnection provider is a public utility.

21 Notwithstanding its non-jurisdictional status, Big Rivers has a non-jurisdictional reciprocity
22 open access transmission tariff on file with FERC. Under FERC's Order No. 888, public utilities are
23 required to provide reciprocal open access transmission service under their open access transmission
24 tariffs to, inter alia, non-public transmission-owning utilities that have non-jurisdictional reciprocity
25 open access transmission tariff on file with FERC. In order to avail itself of open access
26 transmission service on public utility systems to benefit its customer, Big Rivers has filed a non-
27 jurisdictional reciprocity open access transmission tariff with FERC.

28 In the event Big Rivers and Thoroughbred were to have a dispute over the payment of the

1 costs of transmission upgrades required by Thoroughbred's proposed Facility, Thoroughbred could
2 arguably involve FERC in the dispute by filing a complaint or petition with FERC stating that FERC
3 should revoke or reject Big Rivers' non-jurisdictional reciprocity open access transmission tariff
4 because Big Rivers has purportedly failed or refused to comply with FERC's interconnection pricing
5 and transmission pricing policies. But FERC recently held that it will not require a non-utility to
6 provide transmission upgrades for network upgrade costs in order to satisfy the Commission's
7 reciprocity requirements. Standardization of Generator Interconnection Agreements and Procedures,
8 104 FERC ¶ 61,103 at ¶ 843 (2003). Thoroughbred nevertheless potentially could seek an order
9 from FERC to the effect that Big Rivers' reciprocity tariff should be revoked or rejected for failing to
10 comply with FERC's ratemaking policies, thereby placing Big Rivers and its customers at risk of
11 losing their transmission reciprocity rights.

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13 November 17, 2003

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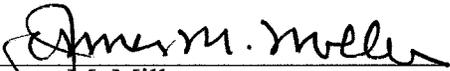
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