COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In The Matter Of:

Electronic Application Of Kentucky Power Company For (1) A General Adjustment Of Its Rates For Electric Service; (2) An Order Approving Its 2017 Environmental Compliance Plan; (3) An Order Approving Its Tariffs And Riders; (4) An Order Approving Accounting Practices To Establish Regulatory Assets Or Liabilities; And (5) An Order Granting All Other Required Approvals And Relief.	: : : : : : :	**Case No. 2017-00179**

KENTUCKY INDUSTRIAL UTILITY CUSTOMERS, INC. RESPONSE TO KENTUCKY POWER COMPANY'S PETITION FOR REHEARING

On February 7, 2018, both Kentucky Power Company ("Kentucky Power" or "Company") and Kentucky Industrial Utility Customers, Inc. ("KIUC") filed requests for rehearing of the Commission's January 18, 2018 Order ("Order"). Pursuant to Section 18(b) of the November 22, 2017 Settlement Agreement, "*Kentucky Power the and Settling Intervenors shall act in good faith and use their best efforts to recommend to the Commission that this Settlement Agreement be approved in its entirety and without modification and that the rates and charges set forth herein be implemented.*" Consistent with this commitment, KIUC submits this Response to Kentucky Power's rehearing request.

I. <u>Alleged Errors In The Commission's Calculation Of Tax Expense Reduction.</u>

In its Order, the Commission reduced Kentucky Power's rate increase by $13,943,890 to reflect the tax expense savings resulting from a reduction in the federal corporate income tax rate from 35% to 21%.[1] Kentucky Power claims that the Commission's methodology was incorrect and that the reduction in the Company's revenue requirement was overstated by $765,030.

[1] Order at 41-42, Appendix F.

KIUC has reviewed the methodology used by the Commission and believes that it is correct and reasonable. However, the methodology used by Kentucky Power is a reasonable alternative.

The Commission methodology derives income tax expense from the weighted equity return on capitalization multiplied by the difference in the 35% and 21% gross revenue conversion factors ("GRCF"). Even though reasonable, this is not how the Company calculates income tax expense on its accounting books.

In its rehearing, the Company starts with its per books income tax expense and then makes adjustments for the tax expense effects of ratemaking adjustments (all of which are included in the filing), then ratios this expense downward by 40% (21/35), and then grosses up the difference by the new 21% GRCF. This methodology also appears reasonable and is arguably more consistent with the rate case filing.

II. Recovery Of Forced Outage Expense in Base Rates And Proposal For Deferral Authority.

In its Order, the Commission denied recovery of purchase power forced outage expense through Tariff PPA. Instead, it was determined that "*[t]he Commission will allow recovery of the test year amount of purchase power reasonably incurred, but excluded from the FAC.*"[2]

Kentucky Power asserts that having denied Tariff PPA recovery, the test year amount of $1,158,285 in forced outage purchase power expense was incorrectly removed from the Company's base rate revenue requirement. Because this purchase power was a reasonable and prudent expense that is recoverable in rates, KIUC agrees that the base rate increase was understated by this amount.

However, the Company's request for accounting authority to establish a regulatory asset to defer any forced outage purchase power expense above the test year amount of $1,158,285 for recovery in its next base rate case is unreasonable. First, if there is a deferral, then it should be for any difference (both above and below) the test year amount. But more to the point, the requested deferral is functionally the same as dollar-for-dollar recovery through Tariff PPA, albeit on a delayed basis. And this approach was specifically rejected by the Commission.

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[2] Order at 55.

III. Changes To The Peaking Unit Equivalent Calculation.

The Company seeks authority to add to the Peaking Unit Equivalent Calculation costs associated with transportation retainage, the park and lend rate and the FERC annual charge adjustment. However, the Company has failed to quantify or estimate the dollar impact of this change. Therefore, KIUC does not take a position on this issue.

The Company also seeks clarification that gains and losses from incidental gas sales be reported in its monthly FAC filing rather than through a separate proceeding. The Company claims that incidental gas sales are an ordinary part of normal business operations and that a formal proceeding would be impractical and cost prohibitive. KIUC agrees with the Company. Submitting this information as part of the monthly FAC is more practical and more transparent for consumers since the FAC filings are regularly posted on the Commission's website.

IV. Clarification On Recovery Of The Rockport Deferral.

The Order provides that "*the recovery period of the Proposed Rockport Deferral Mechanism is contingent upon Kentucky Power not renewing the Rockport UPA.*"[3] The Order also states that the Commission "*recognizes that there are inherent risks associated with any deferral mechanism, especially since the deferral recovery is contingent upon not renewing the Rockport UPA.*"[4]

Kentucky Power argues that recovery of the $50 million Rockport deferral should not be contingent on the Rockport UPA not being renewed. KIUC believes that the Company is correct.

The $50 million of Rockport UPA expense that will be deferred represents reasonable and prudent costs incurred by the Company pursuant to a FERC-approved agreement. The Company is legally entitled to recovery under the doctrine of federal preemption.[5] These costs were deferred as part of a plan to keep rates low now in order to allow the economy to recover while Kentucky Power's economic development efforts take hold.

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[3] Order at 39.
[4] Order at 40.
[5] *Nantahala Power & Light v. Thornburg*, 476 U.S. 953 (1986); *Mississippi Power & Light Co. v. Mississippi ex. rel. Moore*, 487 U.S. 354 (1988).

Further, making recovery contingent on not renewing the Rockport UPA would create economic distortions. While KIUC believes that renewal of the Rockport UPA is unlikely, there might be future circumstances where renewal is the least-cost option for consumers. But if the price of renewal was the forfeiture of all or part of the $50 million deferral, then Kentucky Power would have an incentive to make the incorrect decision.

V. Accounts Receivable Financing.

The Commission disallowed $391,702 through an adjustment to the Company's capital structure because of an unreasonable use of accounts receivable financing and reduced the cost of the receivables financing to remove the uncollectible accounts expense. The Company claims that its use of accounts receivable financing is economic compared to other forms of financing, consistent with its past actual and ratemaking practice, and has uniformly been approved in the past. In addition, the Company claims that its uncollectible accounts expense is included in the cost of the receivable financing and not as a separate operation and maintenance expense, so that there is no double recovery issue. KIUC has reviewed this issue and agrees with the Company.

VI. Venue For Rate Adjustments.

The Company asks that any change in its revenue requirement be addressed in this case or through an adjustment to its amortization of excess ADIT in Case No. 2018-00035. Whatever adjustment is made must also address KIUC's rehearing assertion that the federal income tax expense associated with the Rockport UPA should be reduced by $1.31 million.

As to the proper venue, KIUC believes that this case and Case No. 2018-00035 should remain separate. Kentucky Power has the burden of proof in this proceeding and KIUC has the burden of proof in Case No. 2018-00035. Moreover, the parties involved in the two cases are different. Because any net change to Kentucky Power's base rate revenue requirement is likely to be small, that change should be addressed in the rate case.

Respectfully submitted,

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