COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

IN THE MATTER OF:

APPLICATION OF SOUTH KENTUCKY RURAL	)	
ELECTRIC COOPERATIVE CORPORATION	)	**CASE NO.**
FOR APPROVAL OF MASTER POWER PURCHASE	)	**2018-00050**
AND SALE AGREEMENT AND TRANSACTIONS	)	
THEREUNDER	)	

POST-HEARING BRIEF OF EAST KENTUCKY POWER COOPERATIVE, INC.

Pursuant to the Commission's Order of May 18, 2018, East Kentucky Power Cooperative, Inc. ("EKPC"), by counsel, submits the following post-hearing brief.

INTRODUCTION

This case involves the application by South Kentucky Rural Electric Cooperative Corporation ("South Kentucky") for approval of a transaction with Morgan Stanley Capital Group, Inc. ("Morgan Stanley") whereby:

-- South Kentucky will purchase 58 Megawatts ("MW") of electricity at a 100 percent load factor on a 24/7/365 basis from Morgan Stanley at a fixed price for the next twenty (20) years. The electricity may come from any number of generating sources within the 13 states and District of Columbia PJM footprint, which sources are not identified in the transaction documents.

-- South Kentucky and Morgan Stanley will also participate in a derivative financial hedge transaction whereby one party will owe the other based on the market price of energy capacity versus an agreed upon set contract price, with Morgan Stanley paying South Kentucky if the market price of capacity is above the contract price and South Kentucky paying Morgan Stanley if the market price is lower than the contract price. South Kentucky does not purchase

capacity from Morgan Stanley under this transaction. South Kentucky must purchase capacity at the market price or under some other yet-to-be-determined arrangement, and then "settle" with Morgan Stanley pursuant to the derivative financial hedge transaction described above.

The primary financial driver for the transaction is South Kentucky's purchase of approximately 40 percent of its current energy consumption from the market, rather than from EKPC -- the Generation and Transmission Cooperative South Kentucky co-owns for the benefit of its customers.[1] By doing so, South Kentucky expects to avoid the fixed costs that are included in EKPC's rates for the entire 20 years of the Morgan Stanley agreements. Notwithstanding any attempted window-dressing from South Kentucky or its hired witnesses, it is indisputable that this is the fundamental financial principle underlying the transaction. After some initial hesitation, South Kentucky and its expert acknowledge this fact, as they must:

> *"Q. So what is the big difference between just acquiring this from East Kentucky the way they have been and acquiring in the market? What's the price difference based on?*
>
> *A. The price difference based on? How much comes out of their pocket.*
>
> *Q. Well, no. That's not what causes the price to be different. That's the result of the price being different. What causes the price to be different is there is no fixed costs, right?*
>
> *A. They're avoiding some fixed costs.*
>
> *Q. The vast majority of the value of this deal is avoiding fixed costs. Can we just agree to that?*
>
> *A. Yes.*
>
> *Q. Ok. We danced around this yesterday like it was some secret. The whole deal here is based on avoiding fixed costs. And that generates hundreds of millions of dollars in savings, is that your opinion?*
>
> *A. Yes, I believe.*

[1] Dennis Holt Hearing Testimony, May 16, 2018 Hearing Video Transcript ("H.V.T"). at 1:13:40 PM to 1:14:31 PM.

Q. Who pays those fixed costs?

A. If they're not mitigated, then the member owners of East Kentucky."[2]

In its written testimony, its data responses, and now in its brief, South Kentucky unabashedly asserts that it is *irrelevant* whether its actions shift substantial fixed costs to its fellow fifteen owner-members and their customers. This is because, according to South Kentucky's view, the sixteen owner-members entered into an agreement known as "Amendment 3 to the Wholesale Power Contract" whereby all the owner-members and EKPC agreed that South Kentucky could obtain energy from other sources, and thus take these very actions. Moreover, South Kentucky explains, the owner-members and EKPC eliminated any question by entering into a Memorandum of Understanding (the "MOU") in 2015 that acknowledged their collective interpretation of Amendment 3 to allow for this precise action.

South Kentucky then asserts that because Amendment 3 and the MOU have been filed with EKPC's tariffs at the direction of the Commission, that EKPC, the other 15 owner-members – *and the Commission* – have no grounds to challenge South Kentucky's actions.

What South Kentucky has failed to grasp, however, is that *nothing* in Amendment 3, the MOU, or the Commission's Orders, states or implies, that a party can unilaterally exercise such rights without regard to applicable statutory and regulatory oversight by the Commission. When taken at face value, South Kentucky's position is that even if Amendment 3 and the MOU provided that rates could be set on the basis of whether a customer is left-handed or right-handed, those rates are enforceable and not subject to anything more than the most cursory review and adherence by the Commission. South Kentucky and its expert, Mr. Seelye, assert that when the Commission dismissed the "Grayson" case and, in the Order doing so, directed that the MOU be filed along with EKPC's tariffs, that the Commission essentially pre-approved

[2] May 16, 2018 H.V.T. at 9:52:50 AM through 9:53:47 AM.

the substantive actions undertaken by South Kentucky here. Thus, they assert, the Commission has no authority to now review South Kentucky's actions, regardless of whether the actions result in unfair, unreasonable or unjust rates, and regardless of whether they constitute unreasonable and unnecessary duplication of assets. South Kentucky's position is a very simple, "We got here first and are taking what we are 'entitled to' and no matter what the impact on rates, customers or our G&T's finances, EKPC, its owner-members, and the Commission cannot say or do anything about it – as a matter of law."

South Kentucky, acting through its new interim CEO,[3] decided that it wanted to exercise its rights under the MOU so as to unburden itself of the costs of fixed assets (EKPC's "steel on the ground") that had been approved by EKPC's Board of Directors, including South Kentucky's Director, and which assets had been built, encouraged and approved by the Commission, to serve South Kentucky's customers and all other owner-members. Once South Kentucky got past any concern for cooperative principles and made its fundamental conclusion that shifting of costs or duplication of assets was "irrelevant," the die was cast and regardless of any subsequent "due diligence" or consultant opinion, the outcome was a foregone conclusion. South Kentucky's new interim CEO and its Board first aggressively pursued an alternate source with an independent power producer which had yet to build any generation assets in Kentucky. When its consultant and EKPC told South Kentucky that they might want to consider more than one option for an alternate source and actually seek proposals, South Kentucky swiftly pivoted away from its first choice and undertook a Request for Proposals ("RFP") for an even easier method of shedding its fixed cost burdens – a market based purchased power agreement ("PPA") with a power marketer that would sell essentially the same electricity from the same Regional Transmission Organization as EKPC, but *without* the fixed costs that EKPC must include in its

[3] May 15, 2018 H.V.T. at 10:37:00 AM through 10:37:20 AM.

bundled rates. Those costs would simply be thrown off on EKPC's other existing or future customers. Not surprisingly, in a period of less than 90 days, South Kentucky had "fully vetted" the transaction, signed the papers, and tendered the alternate source notice to EKPC under the MOU.

South Kentucky then filed its Application at the Commission and almost immediately began revising the net present value ("NPV") analysis upon which it had based its entire financial case, a process that continued right up through the scheduled hearing and even beyond – with South Kentucky's primary financial expert submitting his "final" NPV analysis for the first time in *post-hearing data responses.* The urgency and hurried nature of this evolution was not surprising. As CEO Holt acknowledged, South Kentucky was afraid someone else might get in front of them. The result is that the Commission has been asked to approve an Application based on South Kentucky's analysis that the net present value of the savings from the transaction will be $77.7 million. Or $110.8 million. Or $122.8 million. Or $235.9 million.[4] Again, the theme here is simple: "If we throw off all of our fixed cost burden for over 40 percent of our energy purchases, how can we *not* save major dollars?! The amount is unimportant." Notably, even with these purported massive savings, South Kentucky's CFO, Michelle Hermann, testified that South Kentucky's savings "will delay a possible rate adjustment until at least 2023," or within 5 short years.[5]

In its eagerness to jump on any opportunity that would allow it to shift its fixed costs to those less "savvy," South Kentucky ignores legitimate, serious questions about whether it even understands the contractual obligations it has assumed. First, it characterized its capacity

---

[4] South Kentucky Response to Commission Staff's First Posthearing Request for Information, Item 4, Attachment PHPSC-2, page 9; Rebuttal Testimony of Carter Babbit at p.15:11-17.

[5] Application, Exhibit 17, Direct Testimony of Michelle Herrman ("Herrman Direct") at 13.

transaction as one where it would purchase capacity from Morgan Stanley.[6] Then, when faced with questions about the very substantial potential of Morgan Stanley to revise the "fixed" pricing of the purchased electricity over the next *twenty* years due to "environmental changes in law," South Kentucky scoffed and asserted its own definitive interpretation of the contract – without any reliable explanation for the fact that the interpretation it asserts is totally absent from or directly contrary to the actual terms of the contract, notwithstanding the fact that South Kentucky and its paid consultant "negotiated" the terms.

In sum, South Kentucky has done what it knew it was going to do from the moment its Board and its new interim CEO decided that there was a windfall to be had if they acted swiftly to exploit the MOU to the maximum extent possible – and be the first to do so. All the consultants, paid witnesses, power-point presentations, NPV analyses, corrections to those analyses, and corrections to the corrections of those analyses, were not going to change that foregone conclusion. And thus, having the complete burden to now support its decision before the Commission and obtain the Commission's requisite approval, South Kentucky essentially tells the Commission there is nothing to evaluate here. According to South Kentucky, the evaluation occurred when the Commission ordered that MOU be filed in its Order dismissing the Grayson case, and the Commission now has no authority to question the merits of the Application, the effects of the transaction, or the fairness or reasonableness of the outcome.

South Kentucky is wrong as a matter of fact and of law. Its Application must be denied.

STATEMENT OF THE CASE

As a borrower of funds from the federal agency, the Rural Utilities Services (formerly the Rural Electrification Administration) ("RUS"), EKPC and its owner-members are required to

[6] See Application at 2, footnote 1; Application at 5; Exhibit 16, Direct Testimony of Dennis Holt ("Holt Direct") at 14; and Herrman Direct at 12.

enter into all-requirements contracts for the purchase and sale of electricity as a precondition to RUS lending funds. Accordingly, on or about October 1, 1964, EKPC entered into Wholesale Power Contracts ("WPC") with each of its owner-members. Under those contracts, EKPC sold and delivered to each of the sixteen owner-members and each of the sixteen owner-members purchased and received, all of the electric power for the operations of their respective electric system from generation assets constructed and operated in Kentucky, and approved by the Commission.

The foregoing all-requirements provision of power continued until 2003, when EKPC's owner-members voted unanimously to amend the WPC, which amendment was approved and entered into by RUS, to permit each owner-member the opportunity to obtain energy from non-EKPC sources, subject to certain limitations and required procedures. This amendment was collectively known as "Amendment No. 3" to the WPC.

In 2012, one of EKPC's owner-members, Grayson Rural Electric Cooperative Corporation ("Grayson") filed a Complaint against EKPC in Mason Circuit Court alleging that EKPC had withheld Grayson's pro-rata share of proceeds resulting from the sale of a wholly owned subsidiary of EKPC, Charleston Bottoms (which had been formed to help finance EKPC's construction of Gilbert #3, a generating unit at Spurlock Generating Station). Grayson's claims were without merit, and the other fifteen owner-members agreed with EKPC's position to that effect. Despite the pleas from EKPC and the other owner-members that Grayson's position was wholly untenable, and that it should dismiss the case voluntarily, the litigation proceeded over the next two to three years with excessive discovery, multiple judges and significant legal costs. In late 2012, more costs and acrimony were added to the mix when Grayson filed a

Complaint at the Commission[7] seeking authority to purchase 15 percent of its peak load, or 9.4 MW of power under Amendment 3, from Magnum Drilling of Ohio, Inc.

As a result of the litigation fatigue and exorbitant costs resulting from the Charleston Bottoms court case and the proceeding at the Commission (thirteen owner-members intervened in the Commission case), EKPC and all of its owner-members, on July 23, 2015, developed and executed the MOU as a means to resolve the court litigation and the Amendment 3 complaint. The MOU provided the general blueprint of the parties' understanding as to how the sixteen owner-members could seek to contract with parties other than EKPC for power and energy ("Alternate Source") to satisfy a defined portion of their power and energy needs and included provisions relating to, among other matters, limitations on the quantities of Alternate Source power than could be acquired, the length of the terms for which the Alternate Source power could be acquired, and the requisite notice to EKPC prior to acquiring the Alternate Source power. Nothing in the MOU changed or altered the governing provisions of Amendment 3. Nor did it purport to modify the PSC's jurisdiction over any such action.

In the current proceeding, when questioned by the Commissioners and the attorneys why the CEO's of the owner-members and EKPC executed the MOU, Mr. Campbell and those testifying owner-member CEO's all pointed to the fact that their respective companies were litigation-weary and had spent excessive sums of EKPC's end-consumers' money to defend Grayson's meritless claims in the civil case and the Amendment 3 matter at the Commission. All parties believed that the time had come to end the dispute.

---

[7] *See In the Matter of Petition and Compliant of Grayson Rural Electric Cooperative Corporation for an Order Authorizing Purchase of Electric Power at the Rate of Six Cents per Kilowatts of Power vs a Rate in Excess of Seven Cents per Kilowatt Hour Purchased from East Kentucky Power Cooperative Under a Wholesale Power Contract as Amended Between Grayson Rural Electric Cooperative Corporation and East Kentucky Power Cooperative, Inc.*, Order, Case No. 2012-00503.

In framing the scope of the complaint at the outset of the Grayson Case -- Case No. 2012-00503 -- the Commission stated that it had jurisdiction over the WPC and raised the question of whether the Commission itself needed to establish an allocation methodology for alternative power under Amendment 3:

> . . . Since the Wholesale Power Contract contains provision relating to utility rates and service, as those terms are defined under KRS 278.010(12) and (13) respectively, *the contract is within the Commission's jurisdiction*. In addition, KRS 278.160(1) requires a utility to have on file with the Commission "schedules showing all rates and conditions for service established by it and collected or enforced," while Commission regulation 807 KAR 5:011, Section 13, requires each utility to file with the Commission "a copy of all special contracts entered into governing utility service that establish rates, charges, or conditions of service not included in its general tariff." *Thus, any complaint or issue that arises under a rates and service contract between a utility and a customer is subject to the exclusive jurisdiction of the Commission*.[8]
>
> In summary, the Commission will dismiss for lack of jurisdiction two of Grayson's claims: (1) that EKPC's actions with respect to Amendment 3 constitutes an unfair and illegal restraint of trade; and (2) that civil penalties should be imposed on EKPC under KRS 278.990(1). The Commission will also deny EKPC's request to dismiss Grayson's complaint for failure to state a claim upon which relief can be granted. *EKPC's Wholesale Power Contract and Amendment 3 thereto is a special contract governing utility rates and service which is within the Commission's exclusive jurisdiction*, and Grayson has raised substantial questions relating to its rights expressed or implied thereunder sufficient to require an investigation. Because the issues raised by Grayson may implicate the rights of EKPC's other 15 Members, the Commission will serve a copy of this Order on each Member and allow them to individually or jointly file by July 30, 2013 a request for intervention and a response to the issues of: (a) *whether Amendment 3 expressly requires a methodology for Members to share the allocation of alternative power, and if not expressly required, should the Commission nonetheless impute such a methodology for the Members to share the allocation of alternative power under Amendment 3*; and (b) the proper form of advance notice to EKPC for an alternative sourced power purchase.[9]

---

[8] *See In the Matter of Petition and Compliant of Grayson Rural Electric Cooperative Corporation for an Order Authorizing Purchase of Electric Power at the Rate of Six Cents per Kilowatts of Power vs a Rate in Excess of Seven Cents per Kilowatt Hour Purchased from East Kentucky Power Cooperative Under a Wholesale Power Contract as Amended Between Grayson Rural Electric Cooperative Corporation and East Kentucky Power Cooperative, Inc.*, Order, Case No. 2012-00503, p. 15-16, (Ky. P.S.C., Jul. 17, 2013)(emphasis added).

[9] *Id.* at 22-23.

In June of 2017, South Kentucky's long-time CEO, Allen Anderson, retired, and Dennis Holt was subsequently named by the Board to serve as interim CEO.[10] Almost immediately, in August of 2017, South Kentucky engaged EnerVision, Inc. ("EnerVision") to assist it in analyzing a proposal from an independent power producer seeking to build a generating asset in Kentucky. By September, based on input from EnerVision, South Kentucky abandoned the potential transaction with the Texas power producer and instead pursued an RFP for PPA's from energy marketers.[11] By November, South Kentucky had reviewed proposals and issued its formal notice to EKPC that it was electing to utilize an Alternate Source to procure 58 MW, or slightly over 40 percent of its electricity needs.[12] By December, it had signed contracts with Morgan Stanley to bind the transaction – subject to Commission approval.[13]

On January 31, 2018, South Kentucky filed its Application with the Commission for an order approving the PPA it had entered into with Morgan Stanley on December 19, 2017. Under the terms of this PPA, South Kentucky would purchase 58 MW of firm energy for twenty (20) years, beginning June 1, 2019 at a fixed price of $33.95 per Megawatt-hour ("MWh"), and for a financial capacity hedge of 68 MW for eighteen (18) years, beginning June 1, 2021.[14]

The Office of the Attorney General, by and through its Office of Rate Intervention ("AG"), Nucor Steel Gallatin ("Nucor"), EKPC, and EKPC's other fifteen (15) owner-members filed for, and were granted, intervention in the proceeding (collectively, the "Intervenors"). At

[10] May 15, 2018 H.V.T. at 10:37:00 AM through 10:37:20 AM.

[11] Application, Exhibit 18, Direct Testimony of Carter Babbit ("Babbit Direct"), at 9-11; also see South Kentucky Response to Distribution Cooperatives' First Request for Information, Item 13, DC Attachment 13.

[12] Application, Exhibit 4, Alternative Source Notice dated November 28, 2017.

[13] Application, Exhibit 5, EEI Master Purchase and Sale Agreement dated December 18, 2017; Exhibit 6, Collateral Annex to the EEI Master Purchase and Sale Agreement dated December 18, 2017; Exhibit 7, Firm Physical Energy Confirmation dated December 19, 2017; and Exhibit 8, Financial Capacity Confirmation dated December 19, 2017.

[14] Application at 1.

the insistence of South Kentucky, an expedited procedural schedule was established providing for two rounds of discovery to South Kentucky, the filing of Intervenor testimony, and, finally, rebuttal testimony by South Kentucky. An evidentiary hearing was held on May 15, 16, and 17 and the parties were directed to file these Post-Hearing Briefs.

ARGUMENT

I. AMENDMENT 3 OF THE WHOLESALE POWER CONTRACT AND THE MOU DO NOT CONSTRAIN THE COMMISSION'S REGULATORY REVIEW OF SOUTH KENTUCKY'S APPLICATION

As described above, in 1964, EKPC entered into separate WPCs with each of its owner-members which contained identical provisions and which required each owner-member to purchase all of its power needs from EKPC. The WPC was amended four times, as a requirement for RUS loaning funds to EKPC during a period of generation construction, which amendments extended the term of the WPC.[15] Under the most recent amendment ("Amendment 4"), executed on May 12, 2009, the financing term has been extended to January 1, 2051.[16]

Amendment No. 3 to the WPC was executed in 2003, and, together with the 2015 MOU, has been relied upon by South Kentucky as the overriding basis for its Application to be approved. In addition to extending the term of the WPC to January 1, 2041, Amendment 3 provided that under the contract each owner-member of EKPC could undertake to purchase power and energy from "persons" other than EKPC so long as it did not amount to more than 15 percent of the rolling average of the owner-member's highest coincident peak demand occurring during each of the three 12-month periods immediately preceding the election of this option by the owner-member. It also provided the Seller [EKPC] "shall sell and deliver to the Member and the Member shall purchase and receive from the Seller all of the electric power and energy which

---

[15] Direct Testimony of Anthony S. Campbell ("Campbell Direct"), at 3.

[16] *Id.* at 4.

shall be required to serve Member's *load* including all electric power and energy required for the operation of the Member's system…the Member shall have the option…with notice to the Seller, to receive electric power and energy, from persons other than the Seller, or from facilities owned or leased by the Member….provided the aggregate amount….shall not exceed five (5) percent of the rolling average of the Seller's coincident peak demand" for this same three 12 month period. (Emphasis added.) Amendment 3 further provided that "the Member may make or cancel any such election or elections by giving at least 18 months or greater notice to Seller with respect to any *load or loads* with an average coincident peak demand….of 5.0 MW or more in the annual aggregate." (Emphasis added.) This contractual authority to pursue the purchase of power "from persons other than the Seller, or from facilities owned or leased by the Member" was also conditioned and limited by the requirement that *all* owner-member purchases, in the aggregate, could be no more than 5 percent of the rolling average of EKPC's highest coincident peak demand occurring during each of the three 12-month periods immediately preceding the election of this option by the owner-member.[17]

Amendment No. 3 is deficient in procedural detail and did not set forth a satisfactory method of dealing with the obvious problem that if some owner-members undertook these arrangements at 15 percent of their load, it was mathematically impossible that all other owner-members could do the same and still result in an overall reduction of only 5 percent of EKPC load. Likewise, Amendment 3 did not set forth any procedure for dealing with these priority or allocation issues, nor did it address the possibility that an owner-member could utilize an election in a manner that would allow it to avoid fixed costs and shift those to other EKPC owner-members and their respective customers. Thus, in 2004, the EKPC Board of Directors

[17] *Id.*

attempted to establish allocation procedures by the adoption of Board Policy 305. The purpose of the policy was to provide a reasonable approach to allocate the 5 percent of EKPC's Peak Demand among the owner-members so that those owner-members with identifiable, qualified projects could proceed in a timely manner. While this Board Policy was effective to some degree, it still did not provide sufficient detail to assist EKPC and its Board in providing the necessary objective parameters to evaluate all elections made by owner-members, without injecting a critical subjective element which evaluated a proposed off-system purchase on fundamental fairness grounds and the projected impact the purchase would have on the non-electing owner-members.[18] Following the adoption of the MOU, Board Policy 305 was rescinded.

Over the years, EKPC wrestled with several owner-members' attempted elections under Amendment 3 in an attempt to fairly allocate non-EKPC power. Ultimately, as a result of Grayson filing its Complaint at the Commission,[19] the MOU was developed in an attempt to settle the Grayson civil case, the Grayson case at the Commission, and to address the continued uncertainty regarding the allocation issue with Amendment No. 3 and the Board Policy

South Kentucky contends in this proceeding that it entered into the PPA with Morgan Stanley and issued its notice of alternate source election in compliance with all the MOU requirements and, therefore, the Commission is bound to approve this transaction notwithstanding any statutory or regulatory burdens to the contrary.[20] EKPC has not challenged South Kentucky's manner of election or notice under the MOU, and even attempted to assist

[18] *Id.* at 6.

[19] Case No. 2012-00503.

[20] Holt Direct at 13; Rebuttal Testimony of Dennis Holt ("Holt Rebuttal") at 6; Rebuttal Testimony of William Steven Seelye ("Seelye Rebuttal") at 5-6.

South Kentucky in complying with the procedures set forth in the MOU, as EKPC understands them.[21] As testified by Mr. Holt, EKPC has acted entirely consistent with its obligations under the MOU in handling South Kentucky's election.[22] Importantly, however, Amendment 3 and the MOU are simply the contractual provisions for how an owner-member can go about seeking to engage in an Alternate Source transaction as it pertains to the parties' obligations under the Wholesale Power Contract. Neither Amendment 3 nor the MOU in any way state or imply that the *contractual* availability of such an exercise usurps or nullifies the requisite regulatory approvals that are necessary for such an application – nor could they. Neither EKPC~~,~~ nor the owner-members, can contractually modify Kentucky law with respect to the Commission's statutory and regulatory oversight over utility rates and financing.

While South Kentucky states that the Commission accepted the MOU as a reasonable resolution of all the issues raised in Case No. 2012-00503, South Kentucky goes further and states that the Commission and RUS approved the MOU, thus suggesting that the Commission now has limited or no authority to review or regulate the substance of any transaction undertaken pursuant to the MOU.[23] This is an overstatement, at best.

It has long been recognized in regulatory practice that this Commission "speaks through its Orders." In its December 18, 2015 Order in Case No. 2012-00503, the Commission stated:

> Based on a review of the evidence of record and being otherwise sufficiently advised, the Commission finds that the Amendment 3 MOU is comprehensive in nature, does not violate any legal or regulatory principle, and ***results in a reasonable resolution of all issues to be investigated in this case***. As we noted in our July 17, 2013 Order initiating this case, any written agreement that contains provision relating to utility rates and service, as those terms are defined under

[21] Campbell Direct at 24; May 16, 2018 H.V.T. at 11:26:44 PM through 11:27:08 PM.

[22] May 15, 2018 H.V.T. at 10:59:34 AM through 11:00:20 AM.

[23] Holt Direct at 7; Holt Rebuttal at 6-7, Seelye Rebuttal at 9-10.

> KRS 278.010(12) and (13) respectively, is within the Commission's jurisdiction. In addition, KRS 278.160(1) requires a utility to have on file with the Commission "schedules showing all rates and conditions for service established by it and collected or enforced," while Commission regulation 807 KAR 5:011, Section 13, requires each utility to file with the Commission "a copy of all special contracts entered into governing utility service that establish rates, charges, or conditions of service not included in its general tariff." Thus, ***in granting the pending motions to dismiss,*** we will require EKPC to file in the Commission's Tariff Filing System one copy of the Amendment 3 MOU with the signature pages of each of its 16 Members.[24]

As referenced above, the Commission did not conduct any hearing or take any testimony regarding the substance of Amendment 3 or the MOU, and certainly did not hold that any Alternate Source election taken pursuant the MOU was *ipso facto* fair, just and reasonable, necessary and not duplicative. The ordering paragraphs in the December 18, 2015 Order granted the motions to dismiss the complaint case, addressed pending confidentiality requests, established the date by which EKPC would file the signed MOU in the Commission's Tariff Filing System, closed the case and removed it from the docket.[25]

The Commission never ruled in Case No. 2012-00503, or any other case, that any power transaction initiated under the MOU was presumptively approved under the governing statutes and regulations of this Commission. No Application was ever filed by a party, no testimony was ever tendered, and no hearing was ever conducted on the MOU's precedential impact.[26] In fact, not even South Kentucky considered compliance with the terms of the MOU to be the sole legal requisite for an Alternate Source transaction. Both the Energy Confirmation and the Financial Capacity Confirmation ("Confirms"), as part of the South Kentucky/Morgan Stanley PPA, explicitly required that South Kentucky "promptly file for approval of the Agreement and this

---

[24] Case No. 2012-00503, Order, p. 5-6, (Ky. P.S.C., Dec. 18, 2015)(Emphasis added).

[25] *Id.* at 7-8.

[26] May 15, 2018 H.V.T. at 3:27:30 PM through 3:27:50 PM.

Confirmation with the Commission as soon as reasonably practicable after the Trade Date, and shall diligently pursue such Commission approval, including by using all reasonable efforts to promptly respond to any Commission staff inquiry and promptly furnish or cause to be furnished any information or documents requested by the Commission…"[27] The effective and binding nature of both Confirms was expressly conditioned on the Commission issuing "a final, non-appealable order approving the Agreement and this Confirmation on or before 5/31/2018".[28]

II. STANDARD OF REVIEW FOR APPLICATION

South Kentucky has requested approval of the PPA as evidence of indebtedness under KRS 278.300(3), which provides in pertinent part that:

> The commission shall not approve any issue or assumption unless, after investigation of the purposes and uses of the proposed issue and the proceeds thereof, or of the proposed assumption of the obligation or liability, the commission finds that the issue or assumption is for some lawful object within the corporate purposes of the utility, is necessary or appropriate for or consistent with the proper performance by the utility of its service to the public and will not impair its ability to perform that service, and is reasonably necessary and appropriate for such purpose.

In its "Request for Relief" on page 7 of the Application, South Kentucky alleges that "[b]ecause the transactions at issue include ongoing, fixed take/pay obligations and represent long-term commitments that will require footnote disclosure in South Kentucky's annual financial statements, the utility seeks an Order of the Commission approving and authorizing the Agreement and transactions as a proper issue of evidences of indebtedness."[29] Addressing the requirements outlined in KRS 278.300(3), South Kentucky asserts that the PPA it has entered into with Morgan Stanley was for a lawful object within the corporate purposes of South

---

[27] Application, Exhibit 7, Section 16(c) and Exhibit 8, Section 19(c).

[28] Application, Exhibit 7, Section 14(iii) and Exhibit 8, Section 17(iii).

[29] Application at 7-8.

Kentucky, was necessary or appropriate for or consistent with the proper performance by South Kentucky of its service to the public and would not impair its ability to perform that service, and was reasonably necessary and appropriate for such purpose.[30]

In two previous Kentucky Power Company proceedings, this Commission detailed the standard of review for cases involving the approval of a purchase power agreement as an evidence of indebtedness under KRS 278.300. In Case No. 2013-00144 the Commission stated:

> In Case No. 2009-00545, we articulated the standard of review for cases involving approval of a purchase power agreement as evidence of indebtedness under KRS 278.300. Pursuant to KRS 278.300, a utility must establish that the proposed assumption of obligation or liability is for some lawful object within the corporate purposes of the utility, is necessary or appropriate for or consistent with the proper performance by the utility of its service to the public and will not impair its ability to perform that service and is reasonably necessary and appropriate for such purpose. In addition to the standards set forth in KRS 278.300, the Commission must also analyze the need for the purchase power agreement under the Commission's existing statutory authority where, as here, the purchase power agreement is intended to add supplemental generating capacity to the utility. In examining the statutory criteria for approving financing under KRS 278.300(3), the "purposes and uses of the proposed issue" are for the acquisition of new generation; and for the debt to be "for some lawful object within the corporate purposes of the utility." ***A utility must also establish a need for additional generation and the absence of wasteful duplication, both as required under KRS 278.020(1)***.[31]

The Commission continued and stated that "need" required:

> [A] showing of a substantial inadequacy of existing service, involving a consumer market sufficiently large to make it economically feasible for the new system or facility to be constructed or operated.
> [T]he inadequacy must be due either to a substantial deficiency of service facilities, beyond what could be supplied by normal improvements in the ordinary

[30] *Id.* at 8.

[31] *In the Matter of Application of Kentucky Power Company for Approval of the Terms and Conditions of the Renewable Energy Purchase Agreement for Biomass Energy Resources Between the Company and ecoPower Generation-Hazard LLC; Authorization to Enter into the Agreement; Grant of Certain Declaratory Relief; and Grant of All Other Required Approvals and Relief*, Order, Case No. 2013-00144, p. 12-13 (Ky. P.S.C., Oct. 10, 2013) (Emphasis added).

> course of business; or to indifference, poor management or disregard of the rights of consumers, persisting over such a period of time as to establish an inability or unwillingness to render adequate service.[32] (footnote omitted)

Lastly, the Commission addressed "wasteful duplication":

> "Wasteful duplication" is defined as "an excess of capacity over need" and "an excessive investment in relation to productivity or efficiency, and an unnecessary multiplicity of physical properties." For an applicant to demonstrate that a proposed facility does not result in wasteful duplication, we have held that the applicant must demonstrate that a thorough review of all reasonable alternatives has been performed. Selection of a proposal that ultimately costs more than an alternative does not necessarily result in wasteful duplication. All relevant factors must be balanced.[33]

III. SOUTH KENTUCKY HAS NOT DEMONSTRATED THAT IT HAS A NEED FOR THE PROPOSED PPA OR THAT IT WILL NOT RESULT IN WASTEFUL DUPLICATION.

South Kentucky did not provide any support in its Application or in its direct testimony to satisfy the requirements of KRS 278.300 and did not address the issues of need and wasteful duplication at all. Only in its *rebuttal testimony* did South Kentucky attempt to dance around the grounded requirements of this Commission by opining that its Application did not fit the mold of the typical KRS 278.300 transaction and the legal precedents setting forth the burden of proof required by that statutory section. South Kentucky, in essence, has taken the unprecedented position that the wasteful duplication standard does not apply in this case, since it is not supplementing generation, but is "replacing" a portion of its purchased power by exercising a right to designate an Alternate Source of supply.[34] South Kentucky states:

> As has been demonstrated in the Application and in the testimony filed by South Kentucky in this proceeding, the *need* served by the Proposed Transaction is the

[32] *Id.* at 13.

[33] *Id.* at 13-14 (footnotes omitted).

[34] Holt Rebuttal at 15.

> reduction of cost and cost uncertainty associated with the provision of service to South Kentucky's members/customers, relative to the current supply arrangement by which all of South Kentucky's needs are the responsibility of a single entity, EKPC. The Proposed Transaction does not result in any wasteful duplication on South Kentucky's system. As I discussed earlier, the Proposed Transaction represents an exercise by South Kentucky of a bargained-for right obtained as part of the overall agreement by EKPC and the Member Systems to Amendment 3. As for the transaction itself, it affords South Kentucky price certainty over an extended period, with the opportunity to realize significant cost savings over its current arrangement with EKPC.[35]

While EKPC agrees that South Kentucky had the option to seek an Alternate Source under the MOU, the existence of that option does not in any way negate the Commission's standard of review for the PPA at issue in the current proceeding. South Kentucky appears to be arguing that the simple fact they have the option under the MOU automatically establishes that the proposed transaction is reasonable and satisfies all statutory and regulatory requirements. This is simply not the case. The proposed Morgan Stanley transaction has to be reviewed and considered under the same standards as any other purchased power transaction.

At no time during this proceeding has South Kentucky claimed or documented that the service provided by EKPC under the WPC has been inadequate or that reliability has been at issue. Likewise, there has been no claim or evidence of an inability or unwillingness on the part of EKPC to provide adequate service to South Kentucky under the WPC.[36] Consequently, South Kentucky has not demonstrated an adequate "need" for the proposed 58MW Morgan Stanley transaction and this Commission should deny the Application.

In *rebuttal testimony*, South Kentucky has claimed that the statutory "need" is satisfied by reducing its purchased power cost and providing what it believes to be cost certainty from the proposed transaction. That perception is not a *need*, but rather the *desire* of South Kentucky to

---

[35] Seelye Rebuttal at 28.

[36] May 15, 2018 H.V.T. at 11:34:07 AM through 11:34:50 AM.

lower its purchased power costs, which are a significant portion of its total operating costs. This desire does not satisfy the definition of what constitutes need under the Commission's standard of review and, accordingly, the Application should be denied. And, as discussed below, the most credible and reliable evidence at the hearing in this matter, reflects that South Kentucky has not even secured the cost certainty it claims exists in the proposed transaction nor is it even certain that the purchased power costs under the PPA will provide any savings to the ratepayers of South Kentucky. What is certain is that any purported savings, if any, will be as the result of South Kentucky avoiding the fixed costs of EKPC and shifting them to the other fifteen owner-members.[37]

Finally, in *rebuttal testimony*, South Kentucky contends the wasteful duplication standard does not apply in this case as it is not supplementing existing generation, but instead substituting generation from one source with another, as is its right to do so under Amendment No. 3 and the MOU. As noted previously, exercising the permission accorded by the terms of the MOU does not in any way invalidate, or avoid, the requisite regulatory requirements for approval of the transaction by the Commission. Notwithstanding South Kentucky's attempts to recharacterize the unnecessary and duplicative nature of contracting for generated electricity to "replace" the electricity it receives from EKPC, the reality is that the very nature of the transaction is to duplicate the service presently being provided by EKPC through its generation assets and PJM transactions. No EKPC generating assets are retired when South Kentucky commences taking its 58 MW of electricity at a 100 percent load factor from Morgan Stanley. While there will be some decrease in variable costs in the operation of EKPC's assets, the assets and the financial obligations undertaken to construct them still exist. While South Kentucky may myopically view the transaction as a "replacement" within the South Kentucky system, that "replacement"

[37] May 15, 2018 H.V.T. at 10:55:00 AM through 11:11:50 AM

indisputably creates a wasteful duplication of the generating assets owned by EKPC and made available to, and for the benefit of, its owner-members – including South Kentucky, an owner of EKPC. As such, the proposed transaction results in creation of an unnecessary excess of capacity over need. Again, South Kentucky has not claimed or documented any reliability or adequacy of service issues by EKPC under the WPC. Thus, securing another power supply source for over 40 percent of its energy when there is no demonstrated need for the Alternate Source constitutes wasteful duplication of the generating assets that EKPC built and financed with the authority of its owner-member Board, and that were approved (and for that matter, strongly encouraged[38]) by the Commission.

The proposed Morgan Stanley transaction has not satisfied the "need" or "wasteful duplication" standards for the review of a purchased power agreement as an evidence of indebtedness. Accordingly, the Application should be denied.

IV. SOUTH KENTUCKY HAS NOT MET ITS BURDEN IN DEMONSTRATING THAT THE PROPOSED PPA IS NECESSARY OR APPROPRIATE FOR, OR CONSISTENT WITH, THE PROPER PERFORMANCE BY THE UTILITY OF ITS SERVICE TO THE PUBLIC AND WILL NOT IMPAIR ITS ABILITY TO PERFORM THAT SERVICE

South Kentucky asserts that the certainty of the "fixed" prices for twenty years under the PPA and the savings by virtue of avoiding fixed costs, are necessary and appropriate for its performance of its service to the public and will not impair South Kentucky's ability to perform that service. As set forth above, South Kentucky has contracted with Morgan Stanley for the provision of 58 MWs of firm energy at a 100 percent load factor for 20 years, beginning June 1,

---

[38] *See In the Matter of An Examination of the Application of the Fuel Adjustment Clause of East Kentucky Power Cooperative, Inc. from November 1, 2013 Through April 30, 2014*, Order, Case No. 2014-00226, p. 8 (Ky. P.S.C., Jan. 30, 2015). "The Commission believes it is important to maintain the limitation for recovery through the FAC of 'non-economy energy purchases' in order to incentivize utilities to keep outages to a minimum and to have sufficient capacity to meet load."

2019, at a fixed price per MWh. South Kentucky has also contracted with Morgan Stanley for a financial capacity hedge of 68 MWs for 18 years, beginning June 1, 2021, at an established price per MW-day.[39] South Kentucky and its expert consultant, EnerVision, have asserted to the Commission that these agreements will result in significant wholesale power cost savings, calculated on an NPV basis, over the term of the agreements. They likewise assert that the substantial savings can be obtained with minimal financial risk to South Kentucky and its customers.

As addressed in the testimony and data responses filed by the parties as well as evidence at the hearing, there are several serious flaws in the financial analysis that South Kentucky has submitted in support of its Application, and South Kentucky has failed to sustain its burden in demonstrating to the Commission that the transactions South Kentucky proposes to enter into are financially prudent and will not impair South Kentucky's ability to provide service to its customers In its rush to maneuver to the perceived "front of the line" in attempting to utilize its MOU rights to procure an Alternate Source, the evidence in the record reflects that South Kentucky has failed to demonstrate that it has undertaken the reasonable and prudent due diligence appropriate for entering into a transaction of this nature, length and magnitude.

1. **Environmental Change in Law**. Throughout this proceeding, South Kentucky has pointed to the firm energy purchase at a fixed price and the financial capacity hedge price as significant benefits of the proposed transaction. However, a review of the agreements revealed the existence of significant provisions which would permit Morgan Stanley to legally charge South Kentucky additional amounts under certain conditions, thus calling into serious question

[39] Application at 1.

the purported "fixed pricing" that South Kentucky touts as a primary motivator for the transaction. Both the Firm Physical Energy Confirmation and the Financial Capacity Confirmation contain provisions identified as "Environmental Change in Law".[40] The documents define Environmental Change in Law as:

> (a) Except as provided in this Section 17, each Party shall bear responsibility for any change in costs or operational characteristics relating to any generating resource or contract resource which it owns or to which it has entitlement rights.
> (b) In the event of a Change in Law with respect to any Environmental Law or Tax Law, (i) MSCG shall provide to SKRECC a good faith market-based quotation of the amount required to reimburse MSCG for assuming responsibility for such Additional Environmental Costs; and, (ii) MSCG shall have an obligation to take commercially reasonable efforts to minimize any Additional Environmental Costs. SKRECC shall be responsible for and shall pay or reimburse Seller for any Additional Environmental Costs suffered or incurred by Seller, but only to the extent that such Additional Environmental Costs are paid, incurred or suffered during the Delivery Period, and relate to obligations incurred or due to be performed or settled during the Delivery Period.[41]

The documents also define numerous terms utilized in the Confirmations, including the following:

> "Additional Environmental Costs" means:
>
> > (i) any and all fees, licenses, charges, green tags, certificates, expenses and products (including but not limited to any charges or products required on a per unit-of-energy-output, per-unit-of-energy-input, per-weight-of-pollutant, cap and-trade or other basis) and all losses, costs and liabilities with respect thereto, imposed or required by a Governmental Authority with respect to this Transaction or supplied hereunder; and
> > (ii) any and all Taxes and all costs and liabilities with respect thereto, imposed or required by a Governmental Authority with respect to this Transaction or supplied hereunder;
>
> in each case, only to the extent such Additional Environmental Costs result from or are attributable to a Change in Law with respect to any Environmental Law or

---

[40] Application Exhibit 7, Section 17, and Exhibit 8, Section 20 respectively.

[41] *Id.* In Exhibit 8, the definition of "Environmental Change in Law" references Section 20 rather than Section 17, but the texts are identical. "MSCG" and "Seller" refers to the Morgan Stanley Capital Group while SKRECC refers to South Kentucky.

Tax Law and directly cause the price of Product paid by SKRECC to be increased.

"Change in Law" means, with respect to this Confirmation, (i) a material change or the enactment, promulgation or issuance or material amendment of any constitution, charter, act, statute, regulation, ordinance, order (including any order waiving application of a legal requirement as to Buyer), ruling, rule or other Applicable Law, or (ii) a material change in the specified standards or objective criteria contained in a permit, license, or other approvals, which standard or criteria must be met in order for a Seller Resource to generate electric energy, or (iii) other legislative or administrative action of any Government Authority of competent jurisdiction or a final decree, judgment, or order of a court of competent jurisdiction (including temporary restraining orders) occurring subsequent to the Trade Date, in each case related to the regulation, generation, transmission, transportation or consumption of energy, its emissions or by-products, or of the regulation of the environment related to any of the foregoing, and including the creation of a new retail access environment for consumers of electric energy in Kentucky. For purposes of this definition, no enactment, adoption, promulgation, amendment or modification of an Applicable Law shall be considered a Change in Law if, as of the Trade Date, (1) such Applicable Law would have directly affected the performance of the obligations hereunder by either Party after the Trade Date in the absence of this Agreement and (2) either such Applicable Law was (A) officially proposed by the responsible agency and promulgated in final form in the Federal Register or equivalent federal, state or local publication and thereafter becomes effective without further action or (B) enacted into law or promulgated by the appropriate federal, state or local body before the Trade Date, and (i) the comment period with respect to which expired on or before the Trade Date and (ii) any required hearings concluded on or before the Trade Date, in accordance with applicable administrative procedures and which thereafter becomes effective without further action. For the avoidance of doubt, a "Change in Law" hereunder shall not include any change with respect to the regulation of banks or financial firms or their affiliates, nor with respect to the treatment of such entities or their contracts in bankruptcy, insolvency or receivership proceedings.

"Environment" means soil, surface waters, groundwaters, land, stream sediments, surface or subsurface strata, ambient air, and any other environmental medium.

"Environmental Law" means any Applicable Law relating to pollution, GHGs or the protection of the Environment whether existing as of the Trade Date or previously enforced.

> "GHGs" means any emissions of carbon dioxide (CO2), nitrous oxide (N2O), methane (CH4) and other greenhouse gases that have been alleged or are alleged in the future to contribute to the actual or potential threat of altering the Earth's climate. Other greenhouse gases may include hydrofluorocarbons (HFCs), perfluorocarbons (PFCs), and sulfur hexafluoride (SF6), which are generated in a variety of industrial processes.
>
> "Governmental Authority" means a Federal, state, local or municipal governmental body; any governmental, regulatory or administrative agency, commission, body or other authority exercising or entitled to exercise any administrative, executive, judicial, legislative, policy, regulatory or taxing authority, jurisdictional power; any court or governmental tribunal; or any applicable independent system operator, Regional Transmission Organization, regional power pool, NERC or other regional entity performing similar functions.[42]

In its responses to environmental-related questions from the AG, South Kentucky acknowledged that it had not conducted any due diligence reviews pertaining to additional environmental risk and additional environmental costs.[43] South Kentucky also stated its *belief* that the definition of Additional Environmental Costs covered costs such as fees, licenses, charges, and the like but did *not* include capital investment or expenditures incurred by a utility to comply with the Clean Air Act or mandates affecting coal combustion wastes and by-products from coal-fired facilities.[44] In its rebuttal testimony, South Kentucky expanded this position by stating:

> . . . Capital investments and associated O&M expenses are not a basis for Additional Environmental Costs. Rather, the Additional Environmental Costs provision covers situations like Mr. Holt discusses in his rebuttal testimony, a federal or state carbon or greenhouse gas fee or tax.[45]

---

[42] Application Exhibit 7, Section 18, and Exhibit 8, Section 23 respectively.

[43] South Kentucky Response to AG's Supplemental Data Requests, Item 1.

[44] *Id.*, Response to Item 2(a)

[45] Babbit Rebuttal at 6-7.

During the public hearing, South Kentucky was asked to provide support for its conclusory interpretation that the Additional Environmental Cost provisions could not include capital investments and operation and maintenance expenses. South Kentucky indicated this was its "understanding" of the transaction documents but could not identify any actual terms of the documents that supported these limits, nor did it ever discuss or negotiate those terms with Morgan Stanley, obtain clarification from Morgan Stanley, or seek an opinion of counsel to support the South Kentucky interpretation despite the fact that "Change in Law" is clearly defined as any "material change or material amendment of any…statute, regulation…" and "Additional Environmental Costs" means "any and all…expenses…, costs…with respect thereto, imposed or required by a Governmental Authority…"[46]

South Kentucky's unilateral understanding and interpretation of the Environmental Change in Law provisions and the accompanying definitions contained in the two Confirmation documents is seriously lacking and misleading. While the language in the Confirmation documents may restrict any additional environmental costs associated with environmental laws currently in effect, there are no restrictions on future laws, rules, or regulations being eligible for consideration as an additional environmental cost. There certainly is no language in the Confirmation documents that supports the interpretation that capital investments and associated O&M expenses cannot be the basis for additional environmental costs. While Morgan Stanley is required to take commercially reasonable efforts to minimize any additional environmental costs, that requirement cannot be reasonably viewed as meaning such costs could not be incurred and billed in the future over the long term of that agreement.

[46] May 15, 2018 H.V.T. at 11:50:40 AM through 11:56:36 AM and 3:47:50 PM through 3:52:30 PM; May 16, 2018 H.V.T. at 10:41:35 AM through 10:54:03 AM, 11:28:22 AM through 11:39:40 AM, and 11:55:55 AM through 11:57:25 AM.

As Don Mosier testified, "The environmental language that is included in both confirms, you could drive a truck through. So I believe that South Kentucky faces price risk associated with that 'fixed amount' or 'fixed price' they agreed to with Morgan Stanley."[47] Mr. Mosier was not critical of Morgan Stanley including such a provision in the contract, but rather was a natural characteristic of a firm LD, fixed-price contract for such a long term: "I don't believe that Morgan Stanley or any other energy provider would extend a 20-year contract unless there was a good opportunity for a re-opener at some point in time."[48] He explained that there was nothing nefarious about Morgan Stanley including such a provision, but rather, it was simply shrewd business acumen for a contract like this. "I agree Morgan Stanley has [commercial reasonableness] duties and obligations and I trust that they will, I know that they will, because I've dealt with them before and think they are an honorable counterparty. But there's a good opportunity for this price to change meaningfully over a 20-year period of time." [49] In sum, Mr. Mosier's primary criticism was that South Kentucky steadfastly failed or refused to acknowledge this very real probability in assessing the risks and benefits of the proposed transaction. "I think they should have performed more due diligence and sensitivities around what could happen as a result of changes to the fixed price."[50]

While South Kentucky has premised the desirability of this transaction on the purported "fixed pricing" for the next 20 years, in reality, the actual express terms of the Environmental Change in Law provisions in both Confirmation documents leave South Kentucky exposed to pricing adjustments well beyond the limits of South Kentucky's "interpretation." These

---

[47] May 16, 2018 H.V.T. at 4:23:26 PM.

[48] Id. at 4:24:25 PM.

[49] Id. at 4:25:43 PM.

[50] Id. at 4:24:44 PM.

provisions, and South Kentucky's lack of appreciation for their breadth, bring into serious question just how fixed or certain the transaction prices are for the twenty-year terms and the degree of understanding South Kentucky's Board had when it approved this proposed transaction.

2. **EnerVision.** South Kentucky retained EnerVision in August 2017 to assist it in evaluating a proposal to obtain a portion of South Kentucky's wholesale power supply from another supplier. EnerVision is a Georgia firm that provides consulting services in numerous areas of expertise including power supply planning and analysis, power marketing negotiations, transmission services, and strategic planning. EnerVision has assisted distribution cooperatives in seven states with power supply-related issues.[51] EnerVision's witness, Mr. Babbit, stated that he personally had extensive experience in contract administration, including regulatory approvals, but also admitted he had not offered testimony before the Commission or any other state regulatory commissions previously, as the cooperatives he had assisted in the past were not regulated by the utility regulatory commission in the respective states.[52] However, when asked to identify cooperatives who had provided services to, Mr. Babbit initially indicated he could not disclose that information subject to confidentiality agreements.[53] Then, in confidential session,

---

[51] Babbit Direct, Exhibit CB-1.

[52] Babbit Direct at 2 and 4.

[53] May 16, 2018 H.V.T. at 9:05:20 AM through 9:05:56 AM. However, when asked to identify distribution cooperatives in Kentucky that EnerVision had worked with, the information was provided with no citation to a need for confidentiality. See South Kentucky Response to EKPC's First Request for Information, Item 20. South Kentucky also retained as an expert witness Mr. Seeyle with The Prime Group, LLC, a consulting firm which provides many of the same services provided by EnerVision. Mr. Seeyle had no problem disclosing an extensive list of previous clients in his rebuttal testimony. See Seeyle Rebuttal, Exhibit WSS-1.

when pressed on the details of transactions he had worked on, it was clear that none was substantially similar to the terms or structure of the transaction in a situation such as this one.[54]

3. **NPV Analysis.** The NPV analysis submitted by South Kentucky, and its consultant EnerVision, as the underpinning of its financial case under KRS 278.300 for the proposed transaction contained significant and serious errors in its assumptions and projections and demonstrates a lack of sophistication and accuracy for a transaction of this nature and magnitude. In fact, no NPV calculations were actually provided with South Kentucky's Application, instead, a simple graphic presentation of the results was submitted.[55] The calculations and supporting assumptions for the NPV analysis were not provided until requested by the Intervenors in the initial requests for information.[56] These errors included:

- The Alternate Source Network Integration Transmission Service ("NITS") cost was calculated by multiplying the annual 508,080 MWh reduction times a $/kW-month transmission rate. Using the $/kW-month rate, the calculation should have been this rate times 58 MW times 1000 times 12 months.[57]
- The costs for the applicable loads and purchases for the analysis' base case and scenario reflecting the Alternate Source were based on EKPC's Rate E1, while South Kentucky takes service under EKPC's Rate E2.[58]

---

[54] May 16, 2018 H.V.T. at 9:31:21 AM [Confidential Session].

[55] Babbit Direct, Exhibit CB-9.

[56] See Distribution Cooperatives' First Request for Information, Item 30 and EKPC's First Request for Information, Item 26.

[57] South Kentucky Response to EKPC's Supplemental Data Requests, Item 27(c). Mr. Babbit acknowledged that using the $/kW-month rate required the use of the MWs rather MWhs.

[58] *Id.*, Item 27(b). Mr. Babbit stated this error was due to a lack of information on the appropriate rate at the time the analysis was performed. However, South Kentucky had indicated to EnerVision in an October 26, 2017 e-mail that it took service under EKPC's Rate E2; see South Kentucky Response to Distribution Cooperatives' Second Request for Information, Item 39, Attachment 2-39 (Confidential Version), PDF page 15 of 570.

- The NPV analysis did not reflect the current rates for EKPC's Rates E1 and E2.[59] EKPC's energy rates had been revised to reflect changes approved in Case No. 2017-00002[60] and South Kentucky was aware of these changes as it had the companion case, Case No. 2017-00021,[61] pending before the Commission.
- When calculating a combined cost rate for various ancillary services, EnerVision utilized a "Sch. 1A charged to T customers" charge in 2016 for the Transmission Owner Schedule 1A costs instead of EKPC's Ancillary Schedule 1-A rate for 2017.[62]
- While the NITS rate utilized by EnerVision was for the EKPC Transmission Zone, the rate retrieved from a PJM website was effective July 1, 2016. Mr. Babbit stated that EnerVision assumed the 2016 rate for 2017 and escalated the rate by 3 percent. He further stated that at the time of the analysis EnerVision was not aware of the EKPC

---

[59] South Kentucky Response to EKPC's Supplemental Data Requests, Items 27(b) and (e). Mr. Babbit again stated that this error was due to a lack of information on the appropriate rate at the time the analysis was performed. However, South Kentucky's October 26, 2017 e-mail to EnerVision concerning the use of EKPC's Rate E2 also attached a copy of its most recent billing from EKPC. The cover e-mail with the billing disclosed that EKPC's energy rates had been revised to reflect the decision in Case No. 2017-00002 and the billing included the updated energy rates; see South Kentucky Response to Distribution Cooperatives' Second Request for Information, Item 39, Attachment 2-39 (Confidential Version), PDF pages 17 and 34 of 570.

[60] *See In the Matter of An Examination of the Application of the Fuel Adjustment Clause of East Kentucky Power Cooperative, Inc. from November 1, 2014 Through October 31, 2016*, Order, Case No. 2017-00002, (Ky. P.S.C., Aug. 7, 2017).

[61] *See In the Matter of An Examination of the Application of the Fuel Adjustment Clause of South Kentucky Rural Electric Cooperative Corporation from November 1, 2014 Through October 1, 2016*, Order, Case No. 2017-00021, (Ky. P.S.C., Aug. 7, 2017).

[62] Mr. Babbit stated this rate was used to be consistent with the source of other PJM cost assumptions and that at the time of the time of the analysis EnerVision was not aware that the EKPC Ancillary Schedule 1-A rate for the 2017-2018 year was $0.2695 / MWh. EKPC annually updates its transmission rate information, including the Ancillary Schedule 1-A. This updated rate information is effective June 1st of each year and available on the PJM website. See South Kentucky Response to the Commission Staff's First Request for Information, Item 21. In this response Mr. Seeyle provided the link to the PJM website for EKPC's 2017-2018 Formula Rate (Attachment H-24A). The Schedule 1-A Rate calculation is in Appendix A of Attachment H-24A.

NITS rate for the 2017-2018 year.[63] A check of the PJM website identified by Mr. Babbit revealed several NITS rate schedules in effect during 2017 and all postings in 2017 after June included the EKPC NITS rate for the 2017-2018 year.[64]

An integral part of any NPV analysis is the assumptions used to support the escalation of certain costs in order to model expectations for the time period of the analysis. There are four areas of serious concern about the assumptions or escalation factors utilized by EnerVision in the NPV analysis.

- EnerVision escalated the Transmission Enhancement Cost Recovery ("TECR") cost, along with all other identified ancillary costs, at 2 percent, contending that this was consistent with the other escalators utilized in the analysis. However, a review of the changes in the TECR since EKPC joined PJM showed an historic average increase in the costs of *14 percent*.[65]

- EnerVision assumed an escalation factor for EKPC's base rates of 2 percent but failed to reflect EKPC's actual fuel costs, which is recognized by including EKPC's fuel adjustment clause ("FAC") factor.[66]

---

[63] South Kentucky Response to EKPC's Supplemental Data Requests, Items 27(k). It should be noted that South Kentucky retained EnerVision as its consultant in August 2017.

[64] And as noted in the discussion of the EKPC Ancillary Schedule 1-A rate, EKPC's formula transmission rates are updated by June 1st of each year.

[65] Direct Testimony of Michael McNalley ("McNalley Direct"), Exhibits MM-2 and MM-3, PJM Summary Tab, Sheet 4 of 5.

[66] Mr. Babbit argued that the FAC was not included in the analysis as it was variable and could be expected to add to the NPV savings over the 20-year term and including only the base fuel cost component in the NPV analysis was a conservative assumption; see South Kentucky Response to EKPC's Supplemental Data Requests, Items 27 (f) and (g). It should be noted that for the original NPV analysis, EnerVision provided no studies or evaluations to support the claim that adding the FAC would add to the NPV savings.

- EnerVision included a cost for the agency services to be provided by EKPC but assumed those costs would not change during the entire 20-year term of the proposed transaction.

- EnerVision assumed an escalation factor of 3 percent for the NITS costs. Mr. Babbit stated this escalation factor represented a five-year average of historic EKPC transmission rate data as shown in the NPV analysis spreadsheets.[67] However, EnerVision's calculation of the escalator factor assumed that EKPC's NITS rate for the 2012-2013 and 2013-2014 years was the same rate and did not include the actual EKPC NITS rate for the 2017-2018 year. Correcting for these errors produces a historic percentage rate change of *8.07 percent*.[68] Given the importance of transmission costs in purchased power agreements, EKPC also looked at Transmission Service Charges as reported in the State of the Market reports issued by the Independent Market Monitor for PJM. Looking at the same time periods as were used for the EKPC historic transmission data analysis, the annual increases in the Transmission Service Charges for the PJM system range between 8.7 percent and 19 percent, with an average annual increase of *13.1 percent*.[69]

The NPV analysis is erroneous in several respects including unsupported escalation assumptions that are the only evidence South Kentucky has produced in support of its contention that the proposed Morgan Stanley transaction will provide savings over the 20-year term of the agreement. South Kentucky and, in turn EnerVision, have the obligation to ensure that basic information such as applicable rates are accurate and current as of the time an analysis was

---

[67] South Kentucky Response to EKPC's Supplemental Data Requests, Item 25(a)(iv).

[68] McNalley Direct, Exhibits MM-2 and MM-3, Adders Tab, Sheet 5 of 5.

[69] *Id.*

performed, and failed to do so. The reliability and credibility of EnerVision's analysis and opinions create serious issues of concern.

In light of the pervasive errors in South Kentucky's originally submitted NPV analysis and the concerns about escalation factors, EKPC made adjustments to the NPV spreadsheets and submitted two versions of the NPV spreadsheets in its testimony simply to illustrate the significant impact of these erroneous assumptions. Using a NITS transmission escalation rate of 10 percent, the NPV was reduced by *83 percent* from the level South Kentucky and EnerVision determined.[70] Using a NITS transmission escalation rate of 13 percent, the NPV was reduced by 108 percent, in other words, <u>the resulting NPV was negative</u>.[71] In response to a request by the AG, EKPC prepared spreadsheets using the 8.07 percent historic EKPC change in NITS rates that resulted in a 72 percent reduction in the NPV originally determined by South Kentucky and EnerVision.[72]

4. **<u>Rebuttal Testimony Revisions to NPV Analysis.</u>** In his rebuttal testimony, Mr. Babbit took issue with the results shown in Exhibits MM-2 and MM-3 and proposed four adjustments that he believed were "reasonable." The incorporation of these four adjustments nearly restores the NPV results to the significant levels projected in the original analysis.

The first adjustment Mr. Babbit proposed was to incorporate the FAC in the analysis but to exclude it from the escalation of the base rates. He contended that this was reasonable given the projections contained in EKPC's 2015 Long-Range Financial Forecast. He argued that as this forecast is the latest official information available to the owner-members regarding long

---

[70] McNalley Direct, Exhibit MM-2, 20 Yr Compare, Sheet 1 of 5.

[71] McNalley Direct, Exhibit MM-3, 20 Yr Compare, Sheet 1 of 5.

[72] EKPC Response to the AG's Initial Data Request, Item 7(e).

range projections of future power costs under the WPC, it seemed wholly reasonable to use the forecast absent an alternative source of board-approved information.[73]

The 2015 Long-Range Financial Forecast is an unreasonable source to forecast costing information in 2018. There have been significant changes in the conditions that existed at the time the 2015 forecast was prepared and what expectations would be today going forward into the next 20 years. EnerVision claims to have extensive experience in numerous areas related to power supply. Consequently, it should have available, either in-house or by subscription, numerous studies and evaluations concerning expectations of the costs of fuels and market purchase prices. Current studies or evaluations would be a much more reasonable basis for analysis than a three-year-old financial forecast. Further, it makes no sense to escalate the base fuel costs contained in the energy rate but leave those as a constant the FAC. While not a perfect solution, it would be more reasonable to escalate the actual fuel costs at the same rate as the demand charges.

The second adjustment proposed by Mr. Babbit is to include the "net savings to South Kentucky from avoiding the Environmental Surcharge" calculated in Mr. McNalley's Exhibit MM-1 and include the additional expense of the surcharge to the remaining South Kentucky load. Mr. Babbit then de-escalates the surcharge value based on a factor derived from the 2015 Long-Range Financial Forecast.[74]

First, it should be noted that this adjustment is a complete abandonment of the position South Kentucky and EnerVision took in its Application. Originally, South Kentucky contended that as the environmental surcharge is not part of the base rates, it should not be included in a

[73] Babbit Rebuttal at 12.

[74] Babbit Rebuttal at 13.

base rate comparison.[75] In addition, when questioned why costs from the Environmental Change in Law provisions were not included in the NPV analysis, Mr. Babbit stated, "As costs from an Environmental Change in Law would most likely apply and be in similar quantities to purchases South Kentucky makes from EKPC, they were considered to be a wash in the analysis."[76] Second, it is not appropriate to recognize environmental surcharge costs in this analysis without a corresponding recognition of environmental costs that could be expected under the Environmental Change in Law provisions of the proposed Morgan Stanley transaction.

The third adjustment Mr. Babbit proposes is to return the escalation factor for the NITS transmission costs back to his originally proposed 3 percent rather than the 13 percent reflected in Exhibit MM-3.[77] EKPC first notes that South Kentucky, and by extension EnerVision and Mr. Babbit, have the burden of proof in this proceeding. EnerVision has expertise in the areas of transmission services and thus should be able to produce its own evaluation of the expectations for the total costs for transmission services. Yet no such evaluation has been presented. Instead, South Kentucky and its consultant simply offer a critique of Mr. McNalley's analysis. Second, Mr. Babbit completely overlooks the fact that EKPC has already demonstrated the basis for his 3 percent escalation rate was calculated in error from using incomplete historic EKPC NITS cost information.[78]

---

[75] South Kentucky Response to EKPC's First Request for Information, Item 21(c).

[76] *Id.*, Item 24(c).

[77] Babbit Rebuttal at 13-14. Mr. Babbit challenges the accuracy of the projected NITS increases based on a review of information on the PJM website related to estimated impacts of planned transmission upgrades in the revenue requirements of transmission owners. However, he acknowledged the information on the PJM website did not reflect the full NITS cost picture.

[78] *Supra* at 30-32.

The last adjustment Mr. Babbit proposes is to return the escalation factor for the TECR to the 2 percent originally utilized rather than the historic cost increase percentage of 14 percent, citing the need to recognize a difference in load factors.[79] EKPC notes that the load factor concerns Mr. Babbit raises for the first time in his rebuttal testimony certainly should have applied to the original NPV analysis. EnerVision made no mention of this issue in its original analysis. Mr. Babbit has provided no documentation in his rebuttal testimony to support these claims and he has not attempted any formal analysis of the exact impact of the difference in load factors.

Just as with its Application, South Kentucky did not provide the updated NPV analysis spreadsheets with its rebuttal testimony. The spreadsheets were not available for examination during the public hearing and were provided as a response to the Commission Staff's post-hearing data request nearly three weeks after the filing of the rebuttal testimony.

In order to be approved, South Kentucky has the burden of proof to demonstrate that the proposed Morgan Stanley transaction is reasonable and beneficial to its customers. The primary evidence for demonstrating the reasonableness of the transaction is the NPV analysis. The NPV analysis must be based on accurate information and reasonable cost assumptions. The strongest NPV analysis is based on assumptions that are well reasoned and sufficiently documented. South Kentucky's NPV analysis has not come close to this level of due diligence and scrutiny.

As South Kentucky noted at the public hearing, this was the first time it had been involved in a purchased power agreement outside of the EKPC WPC.[80] This placed extra responsibility on South Kentucky to ensure the accuracy of the information it provided to the

---

[79] *Id.* at 14-15.

[80] May 15, 2018 H.V.T. at 11:40:50 AM through 10:41:53 AM.

Commission for approval. South Kentucky and EnerVision did not perform any sensitivity scenarios on the NPV analysis, which would have been beneficial in evaluating a transaction such as this. Finally, the revisions suggested in the rebuttal testimony were simply exercises designed to restore the original claimed savings rather than reasonable, thoroughly evaluated alternatives worthy of serious consideration.

Since this NPV analysis is so lacking, South Kentucky has not met its burden of proof and has not demonstrated that the proposed Morgan Stanley transaction is reasonable or beneficial to South Kentucky and its customers. South Kentucky's Application should be denied.

V. SOUTH KENTUCKY HAS NOT DEMONSTRATED THAT THE PROPOSED PPA RESULTS IN FAIR, JUST, AND REASONABLE RATES FOR RATEPAYERS

KRS Chapter 278 provides that "[t]he commission shall have exclusive jurisdiction over the regulation of rates and service of utilities…" [81] The Commission serves as fact-finder and possesses sole discretion to judge the credibility of evidence. Ky. Indus. Utility Customers, Inc. v. Ky. PSC, 504 S.W.3d 695, 705 (Ky. App. 2016). "The [Commission] acts as a quasi-judicial agency utilizing its authority to conduct hearings, render findings of fact and conclusions of law, and utilizing its expertise in the area and to the merits of rates and service issues." Simpson Cty. Water Dist.v. City of Franklin, 872 S.W.2d 460, 465 (Ky. 1994).

In Ky. Indus. Utility Customers, Inc., supra, the Kentucky Court of Appeals examined the propriety of a power purchase agreement entered into between Kentucky Power Company and a biomass company as part of this Commission's responsibility to ensure that utility rates are fair, just, and reasonable. In that case, the Court of Appeals unequivocally defined the role of the Commission in these matters by declaring that regardless of whether a proposed power purchase

[81] KRS 278.040(2)

agreement satisfied certain state policy goals, "[f]airness, justness, and reasonableness remain the determinative considerations" of the Commission in deciding whether to approve such an agreement. The Court's and the Commission's role must be to "insure that the conflicting interests of **all** (emphasis added) parties concerned with utility rates are **fairly balanced** (emphasis in original)." Id.at p. 709.

Likewise, in the current proceeding, regardless of whether the proposed PPA has been exercised in accordance with the requirements of the MOU, this Commission must still balance the interests of EKPC and all owner-members in assessing the reasonableness of South Kentucky's proposed PPA with Morgan Stanley. The Commission has read, heard, and reviewed the testimony of the witnesses and experts in this case. The evidence clearly identified the adverse impact the proposed PPA will have on all other owner-members. The evidence is extensive and as the fact-finder, this Commission is the sole judge of weighing the credibility of all the witnesses. Only one conclusion can be drawn. South Kentucky's Application, in addition to the other grounds set forth herein, must be denied because, after balancing all the interests of the parties, the proposed PPA is not fair, not just, and not reasonable.

Under Section 6(A) of the MOU, the parties stated their interpretation of Amendment 3 to be that EKPC cannot charge any owner-member for "stranded costs" related to the owner-member's implementation of its rights to use an Alternate Source. Thus, any owner-member's election to utilize an Alternate Source will result in a shifting of costs among the remaining owner-members. The MOU permits EKPC to set its rates for all owner-members to produce revenues that are sufficient to cover all of its costs, in accordance with the WPC.

Importantly, as discussed above, while Amendment 3 and the MOU may set forth the *parties'* agreements as to the ability of an owner-member to purchase power from a source other

than EKPC, those contractual provisions do not in any way eliminate or limit the Commission's ability and obligation to substantively review any proposed transaction to determine whether it results in rates that are fair, just and reasonable. That is to say, the simple fact that a party may contractually be able to *seek* to enter into an Alternate Source arrangement under the MOU which is filed with the Commission, does *not* mean that the Commission has pre-approved any such transaction as fair, just and reasonable.

EKPC prepared a preliminary estimate of the potential cost shift resulting from the proposed South Kentucky transaction by reviewing actual billings to South Kentucky for the 12-month period ending November 2017. EKPC estimated that the total reduction in billings to South Kentucky for this 12-month period would be $30.4 million. After recognizing a portion of the environmental surcharge would be reallocated to South Kentucky and factoring in an estimate that approximately half of EKPC's system costs were fixed, EKPC estimated a total annual cost shift of approximately $17.1 million in the absence of any mitigation due to weather conditions or load growth.[82]

The Distribution Cooperatives' witness, Mr. Wolfram, prepared an independent analysis of potential cost shifting utilizing EKPC billing determinant information for 2017.[83] Mr. Wolfram determined there was a potential annual cost shift of approximately $15.9 million to $18.3 million, depending on how the fuel adjustment clause was recognized in the calculations.[84]

Surprisingly, if not alarmingly, South Kentucky conducted no studies or estimated the potential impacts of its proposed transaction on the base rates and environmental surcharges of

---

[82] South Kentucky Response to the AG's First Request for Information, Item 1, Attachment to December 29, 2017 e-mail from Mr. Campbell, "Mitigation of Amendment 3 Load Loss" dated December 27, 2017.

[83] Direct Testimony of John Wolfram at page 18 of 27.

[84] Distribution Cooperatives' Response to South Kentucky's Post Hearing Request for Information, Item 1, Excel file DC_SK_2-1.xlsx.

its fellow owner-members and their customers. Instead, South Kentucky asserted that it had received assurances from EKPC that the loss of 58 MW from its Alternate Source election could be mitigated without an increase in wholesale rates.[85] South Kentucky appears to suggest that these assurances eliminated any need to analyze or evaluate the potential effect of the proposed transaction on the other owner-members. These assurances consisted of two informal discussions in August 2017 and Mr. Campbell's December 29, 2017 e-mail to the Board of Directors, which included EKPC's preliminary estimate of potential cost shifts as well as a discussion of attempts to mitigate the potential cost shifts.

Concerning the two informal discussions in August 2017, while there has been some disagreement as to what was actually discussed, it should be noted that both discussions occurred before South Kentucky issued its RFP on September 19, 2017. The RFP stated that South Kentucky would consider any term length greater than five years but would prefer proposals to outline a path that could achieve a 20-year supply period.[86] The RFP did not state the proposals had to be for a 24/7/365 block or reflect a 100 percent load factor. The responses to the RFP were not due until October 3, 2017. Thus, any discussion about mitigation of an Alternate Source election in August 2017 could only have been in very general terms and not reflect any of the terms and conditions of the proposed transaction.

The Distribution Cooperatives specifically requested documents utilized by the management or board of directors of South Kentucky in connection with the consideration by them of any such potential cost shifts. South Kentucky cited the December 29, 2017 e-mail as

---

[85] See South Kentucky Response to the AG's First Request for Information, Items 1 and 12; South Kentucky Response to Nucor Steel Gallatin's First Request for Information, Item 1; South Kentucky Response to the Distribution Cooperatives' First Request for Information, Item 6; and South Kentucky Response to EKPC's First Request for Information, Item 29.

[86] South Kentucky Response to the Distribution Cooperatives' First Request for Information, Item 13, DC Attachment 13.

the only documentation responsive to the request.[87] Given that South Kentucky provided its notice for an Alternate Source on November 28, 2017 and its board of directors authorized entering into the proposed transaction on December 19, 2017, the management and board of directors of South Kentucky could not have possibly considered the contents of the December 29, 2017 e-mail when deciding to enter into the proposed transaction.

When considering and evaluating an Alternate Source election such as the proposed PPA, prudency dictated that studies or analyses should have been undertaken to estimate the potential cost shifts resulting from the proposed transaction. Such studies or analyses should have been a routine and reasonable element of South Kentucky's due diligence for such a significant and costly investment. Instead, South Kentucky and its expert admit they did not perform these critical evaluations on these legitimate, and significant, cost shifts. Notably, South Kentucky and its consultant did not include *any* analysis or possibility that the EKPC rate structure could change over the next twenty years to minimize or eliminate an owner-member's ability to avoid fixed costs, such as through demand pricing, or other measures entirely consistent with Amendment 3 and the MOU.

Failure to conduct economic, cost-benefit, and financial sensitivity studies and analyses was a significant finding relied upon by the Kentucky Court of Appeals in Ky. Indus. Utility Customers, Inc. in denying Kentucky Power's application to approve a renewable energy production agreement. The evidence in that case established, and the Court concluded,

> "Kentucky Power failed to put forth any evidence as to how the REPA compared to other renewable sources of energy or even other similar biomass contracts. It also failed to perform any analysis to estimate the reasonableness of the costs under the REPA for years two through twenty. In fact, there was no evidence put before the Commission that the REPA would result in a direct or indirect economic benefit for Kentucky Power's customers or the region as a whole."

---

[87] South Kentucky Response to the Distribution Cooperatives' First Request for Information, Item 6, and DC Attachment 4 (Confidential Version), PDF pages 107 through 109 of 118.

Supra. at p. 708.

In the current proceeding, South Kentucky dismisses all of these analyses and studies as "irrelevant." While it may be irrelevant for purposes of issuing a notice under the contractual provisions of the WPC, it is most certainly relevant to South Kentucky's obligation to demonstrate to the Commission that its proposed course of action will not result in unfair, unjust or unreasonable rates, or unnecessary and wasteful duplication.

South Kentucky has the burden of proof in this case to demonstrate that it has reasonably considered all aspects of the proposed transaction and that it has satisfied all legal standards of review. South Kentucky's assumption that EKPC could, and would, simply mitigate the effects of a 100 percent load factor purchase and all the potential cost shifts reflects a naïve and over-simplistic approach to a significant and complex decision concerning a very significant power supply commitment for the next *twenty years*. South Kentucky has failed to meet its burden of proof and the Application should be denied.

VI. RESPONSE TO COMMISSIONERS' COMMENTS REGARDING AMENDMENT 3 AND MOU DISPUTES.

As was painstakingly evident at the hearing in this matter, the issues created by Amendment 3 have been a near constant source of strife for the EKPC cooperative family over the last fifteen years. They have been the source of at least two major disputes among the owner-members at the Commission involving exorbitant expense and untold hundreds, if not thousands, of hours of discussion, debate and distraction. By their very nature they incentivize owner-members to look inward rather than outward for the benefit of the entire cooperative family and the G&T they co-own. While EKPC fulfilled its contractual obligations pursuant to Amendment 3 and the MOU, it is also keenly aware that the ongoing controversies surrounding these issues do not benefit EKPC, its owner-members, or most importantly, their end-consumers.

The Commissioners' comments and admonitions in this regard at the hearing did not go unheeded. At the same time, however, EKPC believes that unless or until the Commission directs otherwise, EKPC and the owner-members are obliged to comply with the terms of Amendment 3 and the MOU, unless EKPC and the owner-members come up with a solution by agreement that resolves the matter once and for all.

Against this backdrop, following the Commission hearing, the EKPC Board (with South Kentucky excluded due to its interest under this Application) reviewed video excerpts of the Commissioners' commentary at the hearing, and engaged in a robust discussion of these issues and a possible resolution. After serious contemplation, at a special Board meeting on June 8, 2018, the EKPC Board by a vote of 15-0[88] adopted the following resolution expressing the Board's position as to a permanent and lasting resolution of the Amendment 3 issues going forward:

> *By way of unanimous agreement with RUS approval, or by way of PSC Order, Adoption of "Amendment 5" eliminating the operative effect of Amendment 3 with regard to Alternate Sources, returning the Wholesale Power Contract to an All-Requirements contract, and adoption of a Board policy that generally Provides as follows:*
>
> *a) If, upon a written request from an owner-member's representative on the EKPC Board, the EKPC Board determines that a local, small community-driven project will be beneficial to an owner-member, its community, and the EKPC system as a whole, and can be pursued in a financially responsible and prudent manner, then EKPC will undertake to pursue such project and EKPC will own or operate all projects such that EKPC will sell the power to its owner-member.*
>
> *b) The Board may condition approval of such a requested project upon reimbursement by the sponsoring owner-member of any operating shortfall from the project.*

[88] South Kentucky's Board Representative was excused from this portion of the meeting due to this ongoing Commission proceeding.

c) *Public recognition of such community-driven projects will be attributed to the EKPC family of cooperatives and the local owner-member cooperative where the project is located.*

d) *Existing, on-line, projects are grandfathered.*

Upon the passage of this resolution, the EKPC Board directed that its designated representatives make contact with South Kentucky to advise of this resolution and to inquire whether South Kentucky had interest in exploring a resolution of this Commission case and the larger Amendment 3/MOU issues. Those overtures were promptly made; however, South Kentucky indicated it was not interested in exploring such a resolution at this time. Thus, the EKPC Board directed that the Commission be apprised of its formal position on a potential resolution of the Amendment 3/MOU issue going forward.

While EKPC has honored the MOU and its obligations thereunder, it also recognizes that the Commission may very well conclude that there are very few, if any, Alternate Source elections under Amendment 3 and the MOU as written that will ever withstand Commission scrutiny on their individual merits – particularly to the extent they are similar to the exercise by South Kentucky in this Application. While it is and has been EKPC's genuine desire that this ongoing fifteen-year controversy be resolved by unanimous agreement of the EKPC family of cooperatives, this has regrettably not occurred.

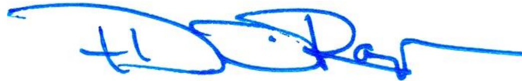
EKPC respectfully submits that South Kentucky's Application should be and can be denied without any necessity of the Commission modifying or invalidating Amendment 3 or the MOU. The Application fails on its own merits under the clear legal standards governing this matter. To the extent the Commission believes, however, that additional action is required with respect to the future of Amendment 3 and the MOU, EKPC recognizes this is the Commission's prerogative. EKPC, however, would encourage the Commission to consider that action separate and aside from its determination on the South Kentucky Application because, as explained

herein, South Kentucky's Application does not satisfy the applicable regulatory standards *regardless* of whether it complies with the contractual provisions of Amendment 3 and regardless of whether the Commission believes action must be taken with respect to Amendment 3 on a going forward basis.

CONCLUSION

South Kentucky's Application should be denied because South Kentucky has not and cannot demonstrate that the proposed transaction is appropriate for or consistent with its proper performance of its service to the public and will not impair its ability to perform that service; that South Kentucky does not have a need for the proposed PPA and that it will result in wasteful duplication of resources; and that the transaction results in rates that are not fair, just and reasonable to utility ratepayers.

Respectfully Submitted,



David T. Royse
Ransdell Roach & Royse PLLC
176 Pasadena Drive, Bldg. 1
Lexington, KY 40503
Telephone: (859) 276-6262
David@RRRFirm.com

David A. Smart, General Counsel
Roger R. Cowden, Corporate Counsel
East Kentucky Power Cooperative, Inc.
P. O. Box 707
Winchester, KY 40392-0707
Telephone: (859) 745-9237
david.smart@ekpc.coop
roger.cowden@ekpc.coop

Counsel for East Kentucky Power Cooperative, Inc.

CERTIFICATE OF SERVICE

This is to certify that a true and correct copy of the foregoing was forwarded electronically on this 2nd day of July, 2018, to the following:

Matthew R. Malone
William H. May
Hurt, Deckard & May, PLLC
127 West Main Street
Lexington, KY 40507
mmalone@hdmfirm.com
bmay@hdmfirm.com

Scott B. Grover
Dan H. McCrary
S. Michael Madison
Jesse S. Unkenholz
Balch & Bingham, LLP
1710 Sixth Ave. North
Birmingham, AL 35203
sgrover@balch.com
dmccrary@balch.com
mmadison@balch.com
junkenholz@balch.com

Kent Chandler
Assistant Attorney General
Office of the Attorney General
700 Capitol Avenue, Suite 20
Frankfort, KY 40601-8204
Kent.Chandler@ky.gov

Rebecca W. Goodman
Assistant Attorney General
Office of the Attorney General
700 Capitol Avenue, Suite 20
Frankfort, KY 40601-8204
Rebecca.Goodman@ky.gov

Honorable W. Patrick Hauser
Attorney at Law
P. O. Box 1900
Barbourville, KY 40906
phauser@barbourville.com

Clayton O. Oswald
Taylor, Keller & Oswald, PLLC
1306 West Fifth Street, Suite 100
P. O. Box 3440
London, KY 40743-3440
coswald@tkolegal.com

John Douglas Hubbard
Jason P. Floyd
Fulton, Hubbard & Hubbard
117 E. Stephen Foster Avenue
P. O. Box 88
Bardstown, KY 40004
jdh@bardstown.com
jpf@bardstown.com

Robert Spragens, Jr.
Spragens & Higdon, P.S.C.
15 Court Square
P. O. Box 681
Lebanon, KY 40033
RSpragens@spragenhidgonlaw.com

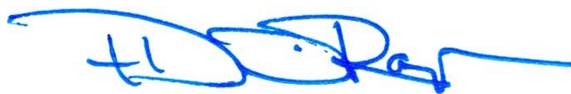
Honorable W. Jeffrey Scott
Brandon M. Music
Attorneys at Law
P. O. Box 608
311 West Main Street
Grayson, KY 41143
wjscott@windstream.net
brandon.m.music@gmail.com

Honorable James M. Crawford
Honorable Ruth H. Baxter
Jake A. Thompson
Crawford & Baxter, P.S.C., Attys at Law
523 Highland Avenue
P. O. Box 353
Carrollton, KY 41008
jcrawford@cbkylaw.com
Rbaxter@cbkylaw.com
Jthompson@cbkylaw.com

Honorable James M. Miller
Attorney at Law
Sullivan, Mountjoy, Stainback &
Miller, PSC
100 St. Ann Street
P. O. Box 727
Owensboro, KY 42302-0727
jmiller@smlegal.com

R. Michael Sullivan
Sullivan, Mountjoy, Stainback &
Miller, PSC
100 St. Ann Street
P. O. Box 727
Owensboro, KY 42302-0727
msullivan@smlegal.com

Honorable Michael L. Kurtz
Attorney at Law
Boehm, Kurtz & Lowry
36 East Seventh Street, Suite 1510
Cincinnati, OH 45202
mkurtz@bkllawfirm.com



Counsel for East Kentucky Power Cooperative, Inc.