COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

ELECTRONIC INVESTIGATION OF THE FUEL	)
ADJUSTMENT CLAUSE REGULATION 807 KAR	) CASE NO.
5:056, PURCHASED POWER COSTS, AND	) 2022-00190
RELATED COST RECOVERY MECHANISMS	)

REPLY COMMENTS OF KENTUCKIANS FOR THE COMMONWEALTH, MOUNTAIN ASSOCIATION, METROPOLITAN HOUSING COALITION, AND EARTH TOOLS, INC.

Kentuckians for the Commonwealth (KFTC), Mountain Association (MA), Metropolitan Housing Coalition (MHC) and Earth Tools, Inc. (ETI) (collectively "Joint Proposed Intervenors") submit the following reply comments regarding the Kentucky Public Service Commission's ("Commission" or "PSC") above-captioned *Electronic Investigation Of The Fuel Adjustment Clause Regulation 807 KAR 5:056, Purchased Power Costs, And Related Cost Recovery Mechanisms*. In their initial comments, the Joint Proposed Intervenors identified for further evaluation three steps to help alleviate the impact of the rising and increasingly volatile fuel costs being charged to captive ratepayers through the Fuel Adjustment Clause ("FAC"):

- Averaging the FAC charge over a period of months or even annually, rather than basing it on a single month

- A cost-sharing mechanism through which the utilities would remain responsible for between 2% to 10% of the costs that would otherwise be passed through the FAC

- Ensuring that the full benefits of zero-fuel resources (i.e., renewable energy, energy efficiency, demand side management, and storage) are robustly factored into resource planning and decision making

In this comment letter, the Joint Proposed Intervenors address some points relevant to their recommendations that were raised in the initial comments filed in this docket by various Kentucky utilities, the state Attorney General ("AG"), Kentucky Industrial Utility Customers ("KIUC"), and others.[1]

I. The Commission Should Carefully Evaluate Averaging FAC Costs Over Multiple Months or An Annual Period

Many commenters expressed support for considering the spreading of FAC costs over multiple months as a means to help reduce FAC volatility.[2] Options for doing so include levelizing the costs over a period of months at the end of which the FAC resets, basing the FAC on a rolling average of multiple months, and/or providing utilities with increased flexibility to defer the recovery of large FAC increases to future months. These options should be more fully evaluated to determine which approach would most effectively minimize volatility for customers, avoid any unfair advantage to the utilities, and provide for a transparent process that is easily verifiable by the Commission, Staff, and interested parties.

As a starting point for such further evaluation, Joint Proposed Intervenors note that it would appear that Duke Energy's proposal[3] of using a twelve-month rolling average to calculate the FAC, which is an approach that is also being evaluated by EKPC,[4] is the most

[1] The Joint Proposed Intervenors' silence regarding a point or proposal made by another commenter in this proceeding should not be considered to constitute agreement or disagreement with that point or proposal.

[2] Comments on Behalf of East Kentucky Power Cooperative Inc. and its Sixteen Owner-Members at 28-29 (hereinafter "EKPC Comments"); Comments of Duke Energy Kentucky, Inc. at 2-4 (hereinafter "Duke Comments"); Initial Comments of Kentucky Power Company at 3-5 (hereinafter "Kentucky Power Comments"); Comments of Kentucky Industrial Utility Customers, Inc. at 1 (hereinafter "KIUC Comments"); Attorney General's Comments at 13-14 (hereinafter "AG Comments").

[3] Duke Comments at 2-4, citing *Electronic Application of Duke Energy Kentucky, Inc. for 1) an Adjustment of the Electric Rates; 2) Approval of New Tariffs; 3) Approval of Accounting Practices to Establish Regulatory Assets and Liabilities; and 4) All Other Required Approvals and Relief,* Case No. 2019-00271, Direct Testimony of William Don Wathen, Jr., at 14-19 (September 3, 2019) (hereinafter "Case No. 2019-00271").

[4] EKPC Comments at 28-29.

straightforward and transparent way to minimize volatility in the FAC. Such an approach would smooth out monthly swings in fuel costs, thereby reducing the large month-to-month changes in electric bills that customers have been experiencing. And, at least on Duke's telling, in comparison to the current FAC, "there would be no economic benefit and no economic harm" to the utilities from adopting a twelve-month rolling average approach to calculating the FAC.[5] While the Commission rejected such an approach in a 2019 rate case filed by Duke, the only reason the Commission provided for doing so was that the current FAC regulation, 807 KAR 5:056 Section 1, "states that the monthly FAC rate will be based upon the most recent actual monthly cost and sales and does not have a deviation clause."[6] The present investigation provides an opportunity for the Commission to evaluate whether the FAC regulation should be revised to allow for such averaging.

Other options identified by commenters would, on initial review, appear to be less effective in achieving the goals of minimizing volatility in a transparent and verifiable fashion. For example, the 12-month forward forecast with an annual (rather than monthly) true-up could reduce month-to-month volatility but, as Kentucky Power notes, runs the risk of a rate shock at the end of the 12-month period when both the true-up would occur and the forward forecast would be reset.[7] Increased flexibility for utilities to defer significant FAC costs to future months without the need for pre-approval from the Commission[8] could also provide a tool for utilities to reduce volatility for their customers. But relying on case-by-case decisions by each utility as to whether and when to defer costs creates transparency and verification challenges, risks that the reduction of volatility would not

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[5] Case No. 2019-00271, Wathen Testimony at 19.

[6] Case No. 2019-00271, Commission Order (April 27, 2020) at 63.

[7] Kentucky Power Comments at 3-4.

[8] Kentucky Power Comments at

be prioritized, and therefore would appear to be a poor substitute for an across-the-board mechanism for minimizing volatility.

While two commenters raised concerns about making any changes to the FAC regulation to allow for the minimization of volatility, their concerns do not merit avoiding a full evaluation of potential changes. Big Rivers recommends against the Commission requiring "any specific volatility reduction mechanism" because of possible "serious negative short-term impacts to Big Rivers' or its Members' available cash positions."[9] But while minimizing price volatility can be critical to a family living paycheck-to-paycheck, it is hard to see how a utility such as Big Rivers, which had approximately $368 million in revenues in 2021,[10] would be harmed by having any increase or decrease to its base fuel costs recovered on a 12-month rolling average rather than monthly. Notably, Big Rivers did not provide any analysis to support such claim of potential harm.

LG&E/KU contends that volatility reduction mechanisms are not necessary, at least for their own companies, because of the actions that they take to reduce fuel price volatility.[11] In particular, LG&E/KU claims that their strategy of contracting for coal up to six years in advance and forward purchases of gas for their combined cycle gas plant, combined with their "limited need to purchase economy power from wholesale markets," shields the companies from significant fuel price volatility.[12] LG&E/KU do not, however, address whether such strategies come at a higher overall cost than the costs incurred by "utilities that purchase power from the wholesale market and rely upon suppliers with a much different generation mix."[13] Regardless, even assuming that the

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[9] Joint Comments of Big Rivers Electric Corporation, Jackson Purchase Energy Corporation, Kenergy Corp., and Meade County Rural Electric Cooperative Corporation at 6-7 (hereinafter "Big Rivers Comments").

[10] Kentucky Public Service Commission, Annual Report Statistics – 2021, at 1, available at https://psc.ky.gov/utility_financial_reports_NET/stats/200_338.pdf

[11] Response of Kentucky Utilities Company and Louisville Gas and Electric Company to the Commission's Order of November 2, 2022 at 6-10 (hereinafter "LG&E/KU Comments").

[12] *Id.* at 6.

[13] *Id.*

relatively lower FAC volatility that LG&E/KU have experienced continues, it is difficult to see how the companies would be harmed if their monthly FAC charge were set based on a rolling twelve month average.

II. The Commission Should Evaluate Modifying the FAC to Provide for Some Level of Cost Sharing.

While averaging or otherwise spreading FAC costs over multiple months is a primary way to reduce fuel cost volatility, the impact of such volatility on customers can be further minimized by reducing the overall fuel costs that utilities seek to pass along to customers. One potential way to do so is by taking steps to ensure that utilities have an economic incentive to reduce their fuel costs. Unfortunately, no such incentive currently exists. Instead, as explained in our initial comments,[14] the FAC provides an almost textbook example of a moral hazard by, as the Commission's November 2 Order notes, making utilities "economically indifferent to the cost and recovery of fuel."[15] By ensuring recovery of 100% of fuel costs, subject to only an after-the-fact review with a presumption of reasonableness, the FAC removes virtually any incentive for utilities to work proactively to hold down fuel costs. To avoid this moral hazard, Joint Proposed Intervenors recommend that the Commission carefully evaluate whether to adopt a cost sharing mechanism that would ensure that the utilities have some economic stake in maximizing the reduction of their fuel costs.[16] In particular, by making the utilities, rather than their customers, responsible for even a small portion (2% to 10%) of the FAC costs, a cost

[14] Joint Proposed Intervenors Comments at 8-11.

[15] Nov. 2 *Order* at 12, question 6.

[16] Joint Proposed Intervenors Comments at 10-11.

sharing mechanism could ensure that utilities have an economic interest in holding their fuel costs down and, therefore, prompt more proactive effort by the utilities to do so.

In their comments, the utilities all contend that, despite the virtual assurance that they will recover 100% of their fuel costs from their captive ratepayers, they are not economically indifferent to their fuel costs. In support, commenters point to Commission oversight of their fuel procurement practices, including the review of FAC charges every six months and two years, 807 KAR 5:056 Section 3(3) and (4), the Commission's authority to reject and order the refund of costs found to be unreasonable or imprudent, *id*. at Section 3(1), (3)(b), and 4(a), and the Commission's ability to order investigations and audits of a utility's practices, *id*. at Section 3(2); *see also* KRS 278.250 and 278.260.[17] According to the utility commenters, such broad Commission review authority ensures that the utilities engage in reasonable fuel procurement practices that seek to keep costs low for customers.

But that review authority is inadequate for at least two reasons. First, there is a significant distinction between avoiding imprudent behavior and proactively working to minimize fuel costs as much as possible. Even if one assumes that the Commission's review authority prevents utilities from engaging in imprudent fuel procurement practices, the 100% pass through of costs virtually eliminates any economic motivation for the utilities to prioritize the minimization of fuel costs.

Second, the FAC review provisions are inadequate because, as the Commission explained in its November 2 Order, the "onerous burden" of demonstrating that any FAC costs were unreasonable effectively falls to the Commission. This is because FAC review proceedings are

[17] LG&E/KU Comments at 14-15; Kentucky Power Comments at 10; Duke Comments at 8.

generally governed by a presumption that a utility's decision to incur a fuel cost is reasonable.[18] As a result, it is up to the Commission every six months and two years to review FAC charges and "thousands of pages of information . . . without any information or evidence on the operation or status of relevant generation units" in order to identify any imprudent behaviors and then try to overcome the presumption that such behaviors are reasonable.[19]

LG&E/KU disputes this contention, noting that the law is clear that the presumption that a utility's management decisions are reasonable is rebuttable, and the ultimate burden of proof lies with the utility to show that any increased rate or charge is just and reasonable.[20] In reality, however, the hurdle of the presumption of reasonableness combined with the utility having all of the relevant information renders the ultimate burden of proof essentially meaningless. In fact, the two FAC review cases leading to disallowances that LG&E/KU identify in their initial comments demonstrates just how difficult it typically is for a disallowance to occur. LG&E/KU cite to a $673,000 fuel cost disallowance against KU in 2003, but neglect to mention that the Commission in that case specifically found that the presumption of reasonableness did not apply because the fuel purchase at issue was a transaction involving affiliates.[21] LG&E/KU also cite to a $10.8 million fuel cost disallowance against Big Rivers in 1990. That disallowance, however, occurred against the backdrop of Big Rivers' former general manager entering into a $500,000 consulting agreement with one of the utility's coal suppliers, that same general manager being investigated by the FBI, the utility's Board showing an "obvious lack of interest in fuel

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[18] Nov. 2 *Order* at 10.

[19] *Id*.

[20] LG&E/KU Comments at 25.

[21] *In re an Examination by the Public Service Commission of the Application of the Fuel Adjustment Clause of Kentucky Utilities Company From May 1, 2001 to October 31, 2001*, KPSC Case No. 2000-00497-B, Order (Jan. 28, 2003) at 10-11.

procurement matters," and the Board's Executive Committee approaching its fiduciary duty with a "cavalier attitude" at best and a "rejection of the spirit and principles of the rural electric cooperative movement" at worst.[22]

In adopting a fuel cost-sharing mechanism in 2008, the Missouri Public Service Commission found that:

> an after-the-fact prudence review is not a substitute for an appropriate financial incentive, nor is an incentive provision intended to be a penalty against the company. Rather, a financial incentive recognizes that fuel and purchased power activities are very complex and there are actions AmerenUE can take that will affect the cost-effectiveness of those activities.[23]

We urge this Commission to apply the same logic and carefully evaluate the establishment of an FAC cost-sharing mechanism as a way to reduce the increasing fuel costs and volatility that Kentuckians are dealing with every day.

III. The Commission Should Ensure that the Full Benefits of Zero-Fuel Resources Are Being Evaluated in Utilities' Resource Planning

In their initial comments, the Joint Proposed Intervenors highlighted how zero-fuel resources such as energy efficiency, demand response, wind, solar, and storage, can reduce overall fuel costs and exposure to price volatility.[24] Fully valuing such benefits of zero-fuel resources in Integrated Resource Planning, Certification of Public Convenience and Necessity, Demand Side Management / Energy Efficiency, and other Commission dockets is critical to any strategy for reducing the risk of increasing and volatile fuel prices.

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[22] *In re an Examination by the Public Service Commission of the Application of the Fuel Adjustment Clause of Big Rivers Electric Corporation From November 1, 1991 to April 30, 1992*, KPSC Case No. 90-360-C, Order (July 21, 1994) at 30-33.

[23] Missouri Public Service Commission, Case ER-2008-0318, Report and Order at pp 72-73

[24] Joint Proposed Intervenors Comments at 12-13.

The state Attorney General ("the AG"), however, has taken an entirely different path in his comments, claiming that "the only thing that can truly be done to meaningfully reduce energy prices today, and therefore reduce electric bills, is to remove barriers to the use of fossil fuels."[25] Such a claim is plainly at odds with the fact that the increasing fuel costs and volatility impacting Kentucky ratepayers are occurring at a time when more than 90% of electric generation in the state comes from fossil fuels.[26] Regardless, the AG's claims are based on a series of errors and flawed assumptions, including:

- While acknowledging that "natural gas prices are high and volatile,"[27] the AG claims that the culprit is a purported attempt by the current Presidential Administration to restrict gas production and make it more expensive.[28] In reality, as reported by the U.S. Energy Information Administration ("EIA"), after a dip at the start of the Covid-19 pandemic, natural gas production in the U.S. now exceeds pre-pandemic records from 2019.[29] Despite such production increases, natural gas prices have risen substantially not just because of increased domestic use, but also because of increasing LNG exports and the continued impacts of Russia's invasion of the Ukraine.[30] In short, the U.S. natural gas market is becoming increasingly global, which is placing significant upward pressure on prices.[31]

- As Joint Proposed Intervenors detailed in their initial comments, a return to increased use of coal would not be an economically prudent path for Kentucky ratepayers, as the price of coal has increased significantly over the past twelve to eighteen months and is expected to stay high for at least the near term.[32]

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[25] AG Comments at 12.

[26] Nov. 2 *Order* at 4.

[27] AG Comments at 11.

[28] *Id*. at 4-5.

[29] EIA, Monthly U.S. Natural Gas Gross Withdrawals, https://www.eia.gov/dnav/ng/hist/n9010us2M.htm (visited Dec. 19, 2022); EIA, Short Term Energy Outlook (Dec. 2022) at p. 7.

[30] EIA, Short Term Energy Outlook at 1, 6-7.

[31] https://www.forbes.com/sites/rrapier/2022/09/27/why-natural-gas-prices-quadrupled-in-two-years/?sh=594afc7b3ccf

[32] Joint Proposed Intervenors Comments at 6-7.

- The AG's suggestions to the contrary notwithstanding,[33] Kentucky largely does not face significant reliability risks. Much of Kentucky is located within the PJM Regional Transmission Organization. According to the North American Electric Reliability Corporation's ("NERC") latest Long-Term Reliability Assessment ("LTRA"), the PJM region "has extensive capacity resources" and has only a "minimal" risk of shortages during non-peak periods, and a "low" risk during peak periods.[34] A portion of Kentucky is within the SERC region, which the LTRA finds is "projected to maintain sufficient capacity to meet the reliability planning reserve margin" over the 10-year assessment timeframe.[35] Of the regions that include portions of Kentucky, only MISO is projected as being at "high" risk for not meeting resource adequacy criteria such as the 1-day-in-10-year load loss metric, which is a significant challenge that MISO has launched a Reliability Imperative Initiative to address.[36]

- The AG claims that "cost-effective battery capacity for wind and solar generation does not exist today."[37] In reality, significant amounts of battery storage resources are already online or expected in the near future. For example, the LTRA reports the following amounts of projected battery storage capacity in various reliability regions:[38]
    - SERC-Florida Peninsula - 519 MWs in 2023; 2,938 MWs by 2032
    - Texas ERCOT – approximately 7,400 MWs within the next five years[39]
    - WECC-Western Power Pool – 486 MWs in 2023; 1,820 MW by 2028
    - WECC-Southwest Reserve Sharing Group – 785 MWs in 2023; 1,124 MWs by 2025
    - NPCC-New England – 354 MWs by 2024

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[33] AG Comments at 7-8.

[34] NERC, 2022 Long-Term Reliability Assessment (Dec. 2022) at 60, available at https://www.nerc.com/pa/RAPA/ra/Reliability%20Assessments%20DL/NERC_LTRA_2022.pdf (hereinafter "LTRA").

[35] LTRA at 72.

[36] LTRA at 5-6, 60; https://www.misoenergy.org/about/miso-strategy-and-value-proposition/miso-reliability-imperative/

[37] AG Comments at 7-8.

[38] LTRA at 41, 71, 84, 96, and 99.

[39] The LTRA notes that the approximately 7,400 MWs of battery capacity expected in Texas ERCOT "represents projects with signed interconnection agreements and proof of financial commitments to build the interconnecting transmission facilities." LTRA at 84.

Contrary to the AG's assertion, the way to "meaningfully reduce energy prices today, and therefore reduce electric bills" is to focus on an orderly and expeditious ramping up of zero-fuel resources that are both lower cost and lower risk than fossil fuels. As a first priority, the Joint Proposed Intervenors urge the Commission to accelerate energy efficiency investments, as the latest state energy efficiency scorecard by the American Council for an Energy-Efficient Economy, which was released after initial comments were filed in this docket, shows that Kentucky has slipped from 33rd to 38th amongst states for energy efficiency.[40] Improving Kentucky's performance on this metric would provide ratepayers with a tool to help reduce their energy usage and, therefore, their exposure to high and volatile fuel prices.

IV. Conclusion

The Joint Proposed Intervenors appreciate the Commission opening this investigation and providing this opportunity to submit comments and recommendations regarding the fuel price volatility challenges facing Kentuckians. We urge the Commission to take the next step by initiating a process for careful evaluation of: (1) whether the FAC charge should be averaged over a period of months or even annually, (2) a mechanism through which utilities would "share" (i.e. remain responsible for) a portion of the FAC costs, and (3) ways to ensure that the different levels of fuel price risk facing different potential resource options are fully evaluated and taken into consideration during CPCN, IRP, and DSM/EE dockets.

[40] ACEEE, 2022 Scorecard at 16, available at https://www.aceee.org/research-report/u2206

Respectfully submitted,

Ashley Wilmes

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Ashley Wilmes, Esq.
Tom FitzGerald, Esq.
Kentucky Resources Council, Inc.
P.O. Box 1070
Frankfort, KY 40602
(859)312-4162
Ashley@kyrc.org
FitzKRC@aol.com

CERTIFICATE OF SERVICE

In accordance with the Commission's July 22, 2021 Order in Case No. 2020-00085, Electronic Emergency Docket Related to the Novel Coronavirus COVID-19, this is to certify that the electronic filing was submitted to the Commission on December 20, 2022; that the documents in this electronic filing are a true representations of the materials prepared for the filing; that no hard copy of this filing will be made; and that the Commission has not excused any party from electronic filing procedures for this case at this time

Ashley Wilmes

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Ashley Wilmes