COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

ELECTRONIC TARIFF FILING OF	**)**	
KENTUCKY POWER COMPANY FOR	**)**	
APPROVAL OF A SPECIAL CONTRACT	**)**	**Case No. 2022-00424**
UNDER ITS ECONOMIC	**)**	
DEVELOPMENT RIDER AND DEMAND	**)**	
RESPONSE SERVICE TARIFFS WITH	**)**	
CYBER INNOVATION GROUP, LLC	**)**	

POST-HEARING MEMORANDUM BRIEF OF THE ATTORNEY GENERAL

The Attorney General of the Commonwealth of Kentucky, through his Office of Rate Intervention ("Attorney General") provides this Post-Hearing Brief related to Kentucky Power Company's ("Kentucky Power" or "Company") pending proposal seeking approval of a special contract with Cyber Innovation Group, LLC ("Cyber").

I. INTRODUCTION

Kentucky Power recently filed an application for a general adjustment of electric rates, requesting this Commission approve a tariff that will increase residential customer's rates by 18.3%.[1] Eastern Kentuckians already pay some of the highest electric bills in the state.[2] Any endeavor that may increase rates even further must be reviewed critically.

While the Attorney General fully supports efforts to promote economic

[1] *Electronic Application of Kentucky Power Company for (1) a general adjustment of its rates for electric service; (2) approval of tariffs and riders; (3) approval of accounting practices to establish regulatory assets and liabilities; (4) a securitization financing order; and (5) all other required approvals and relief*, Case No. 2023-00159.
[2] Kentucky Energy Affordability Dashboard, https://kystats.ky.gov/Reports/Tableau/2022_EnergyDash.

development throughout the Commonwealth and specifically in Eastern Kentucky, proposals to facilitate economic development warrant careful scrutiny to ensure existing ratepayers receive a real benefit when others receive a preferential rate. The Commission established this precedent when it issued Administrative Order No. 327 in 1990.[3] Administrative Order No. 327 concluded an investigation of special contracts between utilities and businesses entered for the purpose of economic development ("Economic Development Rates" or "EDRs"). That investigation resulted in eighteen findings that all jurisdictional gas and electric utilities are required to comply with when entering such contracts.[4] Those findings help to protect existing ratepayers from negative consequences that might result from special contracts containing unreasonable terms.

One of those findings limits offers of EDR contracts to periods of excess capacity.

> EDRs should only be offered during periods of excess capacity. Utilities should demonstrate, upon submission of each EDR contract, that the load expected to be served during each year of the contract period will not cause them to fall below a reserve margin that is considered essential for system reliability. Such a reserve margin should be identified and justified with each EDR contract filing.[5]

Another requires utilities to demonstrate that existing ratepayers will not be adversely affected.

> During rate proceedings, utilities with active EDR contracts should demonstrate through detailed cost-of-service analysis that nonparticipating ratepayers are not adversely affected by these EDR customers.[6]

Further, utilities are required to make an initial demonstration that existing ratepayers will not be harmed by a proposed special contract through the submission of a marginal cost analysis.

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[3] Administrative Case No. 327, September 20, 1990 Order.
[4] Administrative Case No. 327, September 20, 1990 Order at 34-39.
[5] Administrative Order No. 327, September 20, 1990 Order at 35.
[6] Administrative Order No. 327 at 36.

> Upon submission of each EDR contract, a utility should demonstrate that the discounted rate exceeds the marginal cost associated with serving the customer. Marginal cost includes both the marginal cost of capacity as well as the marginal cost of energy. In order to demonstrate marginal cost recovery, a utility should submit, with each EDR contract, a current marginal cost-of-service study. A current study is one conducted no more than one year prior to the date of the contract.[7]

The Commission is right to view special contracts through the lens of protecting existing ratepayers. Kentucky Power has a responsibility to all of its customers, not just Tariff E.D.R. or special contract customers it seeks to attract. So, EDR special contracts cannot be viewed in a vacuum. The ratepayers of Eastern Kentucky must not be forced to pay more for their utilities so that a private business can achieve a private benefit without a general overall public benefit. Contrary to the Company's assertions, not all economic development projects are the same.[8] While they all may bring potential benefits, some bring more than others do. Economic development is critical, and incentives are an important tool. However, the evidence here raises substantial questions regarding whether existing ratepayers will "lose" under this proposal.

The Commission should reject this special contract in order to protect existing ratepayers, because (1) Kentucky Power does not have excess capacity, (2) and the marginal cost analysis submitted in support of the special contract is flawed.

II. ARGUMENT

A. Kentucky Power does not have excess capacity.

Administrative Order 327 requires, "[a]n E.D.R. contract should only be offered during periods of excess capacity for the utility, and the utility must demonstrate that the E.D.R. contract will not cause it to fall below a reserve margin essential for system

[7] Administrative Order No. 327 at 35-36.
[8] Hearing Transcript at 14:21:10.

reliability." The Commission recently reiterated the necessity of an adequate demonstration of excess capacity when seeking approval of economic development special contracts.[9] This proposed special contract violates Administrative Order 327 because it fails to limit discounted rates to periods of excess capacity.

Kentucky Power admits that the special contract is being offered during a period when the Company is capacity short. Company Witness Brian West states, "Kentucky Power finds itself in a capacity short position after the expiration of the Rockport UPA and must contract for capacity to serve all of its customers."[10] Thus, it is beyond dispute that the proposed special contract violates Administrative Order No. 327.

Kentucky Power offers various reasons why the Commission should ignore the requirement of Administrative Order No. 327 that EDRs be limited to periods of excess capacity, none of which are persuasive.

1. Kentucky Power's lack of excess capacity is not remedied by its membership in PJM.

Kentucky Power argues it is capacity "sufficient" due to its membership in PJM, and that compliance with its Fixed Resource Requirement ("FRR") plan with PJM constitutes adequate service under Kentucky law by definition.[11] This argument is illogical and inconsistent with the Commission's interpretation of Kentucky law. Buying power and building generation are fundamentally different. In Kentucky Power's previous IRP case, the Commission confirmed that a utility cannot satisfy its state law

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[9] See Order of October 31, 2022 at 11 in Case No. 2022-00292, *Electronic Application of Atmos Energy Corporation for Approval of Special Contract Pursuant to its Economic Development Rider*. "For future EDR contracts, Atmos shall file specific detailed support for the Administrative Case 327 Order, Finding 5 showing that Atmos has adequate system capacity to serve the proposed customer and that the load served will not cause it to fall below a reserve margin considered essential for system reliability."
[10] Rebuttal testimony of Brian West at R6. See also Hearing Transcript at 9:56:40.
[11] Hearing Transcript at 10:15:45.

obligations by relying heavily on market purchases.[12] "Advocating to explicitly not have enough generation to satisfy retail demand, and using the remaining PJM members as a backstop is contrary to the FRR construct and Kentucky Power's obligation of service under Kentucky law."[13] The Commission should reiterate that the Company is bound by Kentucky law when it comes to its obligations to serve ratepayers.

Additionally, the General Assembly's recent passage of Senate Bill 4, which requires Commission approval of certain utility retirements and replacements, is further evidence of a policy preference in the Commonwealth that utilities control their own generation destiny. This preference seems increasingly reasonable given recent testimony PJM has provided to the General Assembly. PJM's Vice President for State and Member Services Asim Haque recently told the Interim Joint Committee on Natural Resources and Energy that, PJM is, "concerned about being in a supply crunch by the end of this decade."[14] This supply crunch is being brought about due to the early retirement of thermal resources that are needed to preserve reliability of the grid. A supply crunch means prices increase for buyers. Thus, increasing exposure to market risk is bad for ratepayers. Cyber's load, while small, adds to the Company's load not covered by native generation. This arrangement will be increasingly problematic as the PJM supply crunch materializes.

2. The special contract is inconsistent with the terms of the Tariff E.D.R.

Kentucky Power argues the Commission waived the excess capacity limitation

[12] Electronic 2019 Integrated resource Planning Report of Kentucky Power Company, Case No. 2019-00443, Order of June 4, 2021 and Order of June 9, 2021.
[13] *Id.* Order of June 4, 2021 at page 5.
[14] Interim Joint Committee on Natural Resources and Energy Hearing August 3, 2023, YouTube video at 13:2513:33, available at https://www.youtube.com/watch?v=Bja3IDPFPMs (accessed August 16, 2023).

when they approved their Tariff. "Kentucky Power is permitted to offer EDR contracts to customers even when it is capacity-short. In instances when sufficient generating capacity is not available, the Company will procure the additional capacity to serve the customer on the customer's behalf. In that instance, the customer's EDR discount(s) will be reduced commensurately with the cost of the capacity procured."[15] Kentucky Power has recently taken a contradictory position.[16] Nonetheless, the language of the Company's Tariff E.D.R. speaks for itself.

The Company's Tariff E.D.R. was approved in 2015[17] and states that the Company, "will offer the EDR… when the Company has sufficient generating capacity available. When sufficient generating capacity is not available, the Company will procure the additional capacity on the customer's behalf. The cost of capacity procured on behalf of the customer shall reduce on a dollar-for-dollar basis the customer's IBDD and SBDD."[18] In approving the Tariff, the Commission stated, "[t]he proposed tariff's Terms and Conditions section contains a provision that the EDR will be offered when sufficient generating capacity is available, but that if it is not available to serve an EDR customer, Kentucky Power will procure the capacity with the cost reducing the customer's otherwise

[15] Response to Attorney General's Data Request 1-8(b).
[16] Case No. 2022-00181, *Electronic Application of Kentucky Power Company for an Order Approving the Company's Amended Tariff E.D.R to Increase the Capacity Available to the Served under the Tariff and for Deviations from the Commission's September 24, 1990 Order in Administrative Case No. 327*. In Case No. 2022-00181, the Company sought to increase the total capacity for which it could offer Tariff E.D.R. contracts from 250 MW to 550 MW. In the application for that case, Kentucky Power argued that it would be, "capacity short even in the absence of the Tariff E.D.R. agreements being negotiated," and "the Company will be unable to address its urgent need for additional load and customers to allow it to spread fixed costs over a larger base absent a waiver of the Commission's Administrative Case No. 327 Order (and related tariff provisions) limiting the offer of economic development rates to 'periods of excess capacity.'" The Company then proposed a revised tariff, "deleting the Tariff E.D.R. provisions limiting the offer of E.D.R. rates to periods of excess capacity…" The Company later withdrew this application, leaving that version of Tariff E.D.R. in effect, including the limitations expressed by the Company. See Order of July 26, 2022.
[17] *Application of Kentucky Power Company for (1) Approval of an Economic Development Rider; (2) for any required deviation from the Commission's Order in Administrative Case No. 327; and (3) all other required approvals and relie*f, Case No. 2014-00336. Order of May 4, 2015.
[18] See P.S.C. Ky. No. 12 Original Sheet No. 37-1, Terms and Conditions, Section (1).

eligible billing demand discount under the proposed Tariff E.D.R."[19]

The effect of the provision is clear. The Commission is allowing Kentucky Power to offer EDRs when it is capacity short, if and only if, it recovers all marginal costs driven by the contract from the EDR customer. This is in harmony with the requirements of Administrative Order 327.

Kentucky Power nonetheless proposes to enter EDRs during a period when it is capacity short *without* reducing the discounts to Cyber to offset capacity purchases made to serve it. Kentucky Power argues that the discount-reducing provisions of the Tariff are, "inapplicable because the Company will not be purchasing excess capacity solely to serve Cyber Innovation."[20] But this rationalization of Kentucky Power's preferred outcome is not based on any provision of law or tariff language allowing for deviation from its Tariff, and is entirely inconsistent with the rationale of the Tariff language calculated at passing these marginal costs to the cost driver and holding existing ratepayers harmless in the process.

The Tariff only allows for capacity-short offerings if the Company pays for the replacement capacity through reduction of the discounts to be received, IBDD and SBDD, "on a dollar-for-dollar basis." The Company cannot have it both ways. The Company cannot argue that an exception in its Tariff allows it to offer Tariff E.D.R. during times when it is capacity short and simultaneous argue that the terms that control the application of that exception be ignored.

The existence of the Cyber load directly drives capacity purchases that would not be made but for the contract. The Company repeatedly failed to offer any reasonable

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[19] *Id.* at 2.
[20] Rebuttal testimony of Brian West at R6-R7.

explanation for why its capacity purchases for others negate its requirement to pass along these costs to the recipient of that purchase. The failure to appreciate the marginal nature of these costs is evident in the exchange between Company Witness West and the Chairman at the Hearing.

> Chairman Chandler: If you are having to purchase capacity to serve the additional load, there is a cost to that, correct?
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> Company Witness West: There is a cost to purchase capacity for all of our customers, yes.
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> Chairman Chandler: Answer it however you want. That's fine. Absent the additional load, the load forecast would be lower, and you would not have purchased capacity for these EDR customers, correct?
>
> Company Witness West: If they are not included in the load forecast, then yes, we would not be purchasing that incremental piece.
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> Chairman Chandler: So, by definition, that capacity purchase is a variable cost of serving the incremental demand. Would you agree?
>
> Company Witness West: Mr. Chairman. I don't think we are ever going to agree on this.[21]

Company Witness West goes on to confirm Counsel's assessment that a "true incremental capacity purchase" is "capacity the company otherwise wouldn't have purchased."[22] The Attorney General agrees with that definition; costs are incremental or marginal if the Company would not have made any purchase or portion of a purchase to serve the load. But that is not the way Kentucky Power defines incremental or marginal in practice. In practice, it applies a narrower definition. The Company arbitrarily limits the definition to only purchases made for a specific amount that solely serves a "new" customer.[23] In their words, those are the only "true" incremental purchases.[24] There is

[21] Hearing Transcript 13:47:00.
[22] Hearing Transcript 13:32:56.
[23] *Id.*
[24] *Id.*

simply no basis for this restrictive interpretation.

In sum, the Company's testimony on this topic was confused and cryptic.[25] One is left with the impression that the Company will almost never enforce the requirement that these costs be passed along to Tariff E.D.R. participants.[26]

At times, the Company seemed to imply its refusal to account for these costs is premised at least in part on its inability to track them. "That's right. To the extent we could, you know, pin down to that one customer, that was what the driver was."[27] If a utility cannot identify an incremental cost, then it has no business offering tariffs or special contracts that require those costs to be calculated and passed along to the customer. The Tariff is plain that, in instances where sufficient capacity is not available, capacity can only be procured for the customer if the customers pays for those purchases through discount reductions. The claimed inability to track the purchases driven by specific customers is in direct violation of the plain language of the Tariff E.D.R. that requires the special contract customer to pay for those purchases. If Kentucky Power is unable or unwilling to track required costs, then the Commission should revert to strictly limiting application of Tariff E.D.R. to periods of excess capacity.

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[25] Hearing Transcript 13:47:00.
[26] Hearing Transcript 9:55:30. Kentucky Power has attempted to offer an explanation for when this provision will be triggered in its Response to Commission's Post-Hearing Data Request 5. "Kentucky Power has not yet had cause to implement this provision for any current EDR customers. The Company remains capacity sufficient regarding its generation capacity obligation in PJM. This is because existing EDR customers are captured within the replacement capacity necessary for the loss of the Rockport UPA. Therefore, no incremental capacity was purchased." The Response admits that the Company has purchased "replacement capacity" and the existing customers are "captured within" that replacement capacity, but nonetheless argues "no incremental capacity was purchased." If some of the "replacement capacity" purchases could have been foregone but for the service of the EDR customers, those purchases are, contrary to Kentucky Power's assertions, marginal or incremental. Kentucky Power continues to offer no support for its decisions to summarily exclude certain costs from EDR cost recovery as non-incremental or non-marginal when those costs clearly are incremental or marginal.
[27] Hearing Transcript 13:30:50.

Notably, this is not the first time the Commission has grappled with this issue.[28] In reviewing a special contract between Kentucky Power and Big Run Power Producers, LLC, ("Big Run") the Commission addressed Kentucky Power's pending capacity shortfall stating, "[t]o the extent Kentucky Power is required to purchase capacity for Big Run, these costs would be borne by Big Run."[29] The Company did not enter into the special contract with Big Run during a period when the Company was capacity short. Further, the Commission's approval was based in part on the stipulation that Big Run would be responsible for the costs associated with the capacity purchase made to serve it. Kentucky Power apparently has ignored this latter stipulation.[30]

The special contract proposed here, and the context surrounding it, are distinguishable from the Big Run special contract. Here, Kentucky Power proposes to enter a new special contract during a period when it is capacity short. Further, Kentucky Power proposes to ignore Tariff E.D.R.'s requirement that discounts be reduced in the event capacity purchases are required to serve the E.D.R. customer. Thus, the Company's proposal here is entirely at odds with the plain language of the Tariff in ways the Big Run proposal was not.[31]

For these reasons, the Cyber special contract is inconsistent with Tariff E.D.R.

B. The marginal cost analysis supporting the application is based on flawed assumptions.

The marginal cost analysis is a crucial factor in the consideration of whether a special contract should be approved. Without an accurate marginal cost analysis, it is

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[28] Electronic Application of Kentucky Power Company for Approval of a contract for electric service under Tariff E.D.R., Case No. 2018-00378, Order of July 9, 2019.
[29] PSC case filing 2018-00378 Order issued July 9, 2019. Speaking to the expiration of Rockport.
[30] Hearing Transcript at 11:12:00.
[31] See also Rebuttal testimony of Brian West at R6. "The Company interprets this tariff provision not to apply here."

impossible to determine whether existing customers will be harmed by the discounts given the EDR customer.[32]

Kentucky Power made a number of errors in its marginal cost analysis related to another recently-submitted special contract with Ebon International, LLC.[33] Some of those same errors were repeated in the marginal cost analysis supporting this proposal, including questionable transmission cost assumptions and a failure to consider the present value of costs and benefits.

First, Kentucky Power unreasonably escalates PJM LSE Transmission costs at a rate of 5%.[34] Kentucky Power acknowledges that utilizing a different assumption for this metric could result in this special contract causing a net cost to ratepayers.[35] Kentucky Power made no efforts to "stress test" its analysis using alternate transmission escalation values.[36] Kentucky Power admits to having concerns about transmission costs outpacing its estimates.[37]

Second, Kentucky Power fails to consider the present value of the costs and benefits of the special contract. A present value economic analysis is a fundamental requirement in a life of contract analysis to measure the net benefits or net costs. A dollar of benefits or costs that occurs in year ten does not have the same economic effect as a dollar of benefit or cost in year one. The Company's analysis is presented on a nominal basis without recognizing the time value of money. A nominal analysis is particularly inappropriate in a period of high inflation.

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[32] Hearing Transcript at 11:13:30-11:17:25.
[33] Electronic Tariff Filing of Kentucky Power Company for Approval of a Special Contract with Ebon International, LLC, Case No. 2022-00387.
[34] See Response to Commission Data Request 1-1 Attachment.
[35] Hearing Transcript at 15:48:00.
[36] Hearing Transcript at 15:48:50.
[37] Hearing Transcript at 15:55:32.

Further, the requirement to have an accurate and robust marginal cost analysis is inextricably linked to the discussion regarding excess capacity above. If Kentucky Power was limited to offering EDRs during periods of excess capacity, this complicated analysis would be avoided in part. Forced consideration of the capacity cost impacts of a special contract complicate marginal cost analyses even further. As evidenced here, such disputes can be tedious and messy. Thus, increased controversy related to marginal cost analyses is simply another reason supporting the Commission's reasonable limitation of EDRs to periods of excess capacity. If EDRs are limited to periods when capacity costs is not a consideration, then the cost side of the cost-benefit analysis is lower and special contracts are easier to validate.

III. CONCLUSION

The Attorney General is in full support of all reasonable economic development initiatives that have the potential to benefit the people of a service territory as long as risks to existing customers are properly mitigated. Unfortunately, Kentucky Power has failed to establish that risks to existing ratepayers have been sufficiently mitigated. In this case, the Commission should deny the special contract because it violates Commission precedent and Kentucky Power's Tariff E.D.R. However, if the Commission is inclined to approve the special contract, such approval should come if and only if Kentucky Power and the Company are willing to ensure and clearly demonstrate that ratepayers are fully protected from the cost impacts of the contract and are protected in the event of default.

Respectfully submitted,

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Certificate of Service and Filing

Pursuant to the Commission's Orders and in accord with all other applicable law, Counsel certifies that, on August 28, 2023, a copy of the forgoing was served via the Commission's electronic filing system.

this 28th day of August, 2023.

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Assistant Attorney General