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April 7, 2009

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PUBLIC SERVICE
COMMISSION

Via Federal Express

Jeff Derouen
Executive Director
Public Service Commission
211 Sower Boulevard, P.O. Box 615
Frankfort, Kentucky 40602-0615

Re: In the Matter of: Notice and Application of Big Rivers Electric Corporation for a General Rate Adjustment in Rates, P.S.C. Case No. 2009-00040

Dear Mr. Derouen:

Enclosed for filing on behalf of Big Rivers Electric Corporation are an original and ten copies of Big Rivers Electric Corporation's Post-Hearing Brief on Request for Emergency Interim Rate Relief in the above-referenced matter. I certify that copies of this cover letter and brief have been served on the attached service list.

Sincerely,

Tyson Kamuf

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Enclosures

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PSC CASE NO. 2009-00040

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COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

NOTICE AND APPLICATION OF BIG RIVERS ELECTRIC CORPORATION FOR A GENERAL ADJUSTMENT IN RATES	))))	**CASE NO. 2009-00040**

<u>BIG RIVERS ELECTRIC CORPORATION'S POST-HEARING BRIEF ON REQUEST FOR EMERGENCY INTERIM RATE RELIEF</u>

Respectfully submitted,

By: ______________________

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April 8, 2009

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COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

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BIG RIVERS ELECTRIC CORPORATION'S POST-HEARING BRIEF ON REQUEST FOR EMERGENCY INTERIM RATE RELIEF

Big Rivers Electric Corporation ("Big Rivers") by counsel, for its post-hearing brief on its request for emergency interim rate relief in this matter, states as follows:

I. INTRODUCTION AND BACKGROUND

Big Rivers must have the emergency interim rate relief it requests to remain solvent if the Unwind Transaction conditionally approved in Case No. 2007-00455 (the "Unwind")[1] does not close. Big Rivers requires both (1) an additional $16 million by the end of 2009 through the rate increase and (2) a one-time deferral of 60% of its O&M and capital budgets ($13.9 million), for it to have sufficient cash to pay its outstanding obligations and fund its ongoing operations. With cost cutting alone, Big Rivers projects a negative $7.5 million cash balance on January 5, 2010 – and insolvency.[2] Absent interim rate relief, Big Rivers cannot prudently raise the needed cash.

Big Rivers is at a critical juncture in its history, forced to plan for two divergent futures amid a deteriorating economy. On one path, Big Rivers is focusing its resources and manpower on satisfying the conditions to close and operate after the Unwind. Should that closing occur, Big Rivers will regain control over its generating units, eliminate its current negative equity,

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[1] *In the Matter of: The Applications of Big Rivers Electric Corporation for: (1) Approval of Wholesale Tariff Additions for Big Rivers Electric Corporation, (2) Approval of Transactions, (3) Approval to Issue Evidences of Indebtedness, and (4) Approval of Amendments to Contracts; and of E.ON U.S., LLC, Western Kentucky Energy Corp. and LG&E Energy Marketing, Inc. for Approval of Transactions,* PSC Case No. 2007-00455 (Order dated March 6, 2009).

[2] Big Rivers' Response to the Commission Staff's 2nd Data Request, Item 6(b), p. 2 at l. 5-25; Big Rivers Redirect Exhibit 2.

replenish its cash levels, and obtain investment grade credit ratings permitting it to finance its future needs like any other utility.[3] This remains Big Rivers' hope and expectation. But prudence demands that Big Rivers protect itself and its Members against a less attractive alternative future should the Unwind fall apart, which remains outside Big Rivers' control.[4]

The second path requires Big Rivers to project its future cash flows in a declining economic market without the benefits of the Unwind. It is difficult to be optimistic in this scenario. Economic contraction has significantly reduced power market prices since September 2008 when Big Rivers prepared its 2009 budget,[5] and prices have continued to decline in the time since Big Rivers prepared and filed its case in February.[6] The only certainty is that 2009 marketing revenues and margins will be substantially less than those in 2008.[7]

The dramatic depletion in Big Rivers' cash reserves dictating the need for this filing has its root cause in the ongoing global financial market turmoil. On June 19, 2008, Ambac Assurance Corporation's ("Ambac") credit rating was downgraded.[8] This set in motion a process that culminated with Big Rivers' September 30, 2008 decision to buy out its leveraged leases with Phillip Morris Capital Corporation ("PMCC").[9] Big Rivers had no practical alternative to this buyout and was fortunate it had the cash reserves to accomplish it.[10] The PMCC Buyout required a $109.4 million cash payment and a short term $12.4 million

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[3] Direct Testimony of C. Willliam Blackburn, Application Exhibit 47, p. 8 at l. 8-22 – p. 9 at l. 1-9.
[4] Direct Testimony of Mark A. Bailey, Application Exhibit 45, p. 13, at l. 12-14 ("In my view it would be extraordinarily imprudent to bet Big Rivers' future existence on the closing of the Unwind Transaction, when there are so many reasons the Unwind Transaction may not close that are out of Big Rivers' control.")
[5] Testimony of C. William Blackburn, Video Transcript of March 26, 2009 Hearing ("Tr.") at 11:27'21 (September 2008 prices were used in 2009 budget).
[6] Big Rivers' Response to Commission Staff's 2nd Data Request, Item 6(b), p. 3, l. 8-9; Testimony of C. William Blackburn, Tr. 11:40'52 (March 19 forward price curve is $30/MWh higher than September 2008) & Tr. 12:31'22 (forward price curve has fallen to $38/MWh).
[7] Testimony of C. William Blackburn, Tr. at 12:08'31; Tr. 12:12:09 (in worst case, arbitrage revenues could fall $8 million below *pro forma* amount).
[8] Direct Testimony of C. William Blackburn, Application Exhibit 47, p. 22, at l. 8-13.
[9] *Id.* at pp. 16-38; Application Exhibit 53 (Affidavit of C. William Blackburn submitted in Case No. 2007-00455).
[10] Direct Testimony of Mark A. Bailey, Application Exhibit 45, p. 12, at l. 11-17.

promissory note due December 15, 2009.[11] In addition to the $12.4 million PMCC payment in December 2009, Big Rivers must make a $15.8 million quarterly payment to the Rural Utilities Service ("RUS") on January 4, 2010. These obligations create an acute cash crisis for Big Rivers.[12] The proposed rate increase together with the drastic cost reductions are the only means Big Rivers has identified that permit it a reasonable opportunity to remain solvent.

Mr. Kollen, the witness for Kentucky Industrial Utility Customers, Inc. ("KIUC"), suggests that the Commission wait three months and evaluate Big Rivers' needs at that time. But it would not be prudent to bet Big Rivers' future on Mr. Kollen's raw speculation. Big Rivers has an equity position of negative $154.6 million[13] and is very limited in its ability to borrow new funds.[14] Without the combination of the interim rate increase and the identified cost reductions, Big Rivers will default on its obligations and will be unable to fund its operations. Federal payment priority law establishing potential personal liability on management and board members if any debt is paid before debt owing to the RUS would have the practical effect of assuring a Big Rivers bankruptcy upon insolvency.[15] A Big Rivers bankruptcy could create years of uncertainty surrounding disposition of its generating assets and would severely depress the economy of western Kentucky.[16] Big Rivers' Members' wholesale power contracts would be at risk, and they might end up paying substantially higher market rates for power.

It is simply not prudent to delay Big Rivers' request for interim rate relief. Big Rivers remains hopeful that the Unwind will close. However, the Unwind will not close April 9, and

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[11] *Id.* at p. 16, at l. 2-5.
[12] Testimony of C. William Blackburn, Tr. at 12:08'31; Tr. 12:12:09.
[13] Big Rivers' Response to the Commission Staff's 1st Data Request, March 18, 2009, Item 2, p. 1, at l. 19-20.
[14] Direct Testimony of C. William Blackburn, Application Exhibit 47, p. 13. at l. 9-18.
[15] 31 U.S.C.A. § 3713.
[16] Testimony of C. William Blackburn, Tr. at 12:21'05 (RUS foreclosed on Big Rivers in 1984 when it defaulted on payment); Testimony of Mark A. Bailey, Tr. at 10:36'21 (RUS acceleration of debts would mean hundreds of millions of dollars owed by Big Rivers which it would be unable to pay, making bankruptcy the likely ultimate result).

there is no way to know when or whether the Unwind will close with so many closing conditions being outside Big Rivers' control. But each day of delay means that the interim rate increase will have to be that much greater if Big Rivers is to have the cash needed for its obligations. For example, to avoid an insolvency the emergency rate increase would have to be 34.6% if delayed until July 1, 2009 – inducing acute rate shock for Big Rivers' Members.[17]

By contrast, there is no risk if the emergency interim rate relief is approved now. If the Unwind does not close, Big Rivers projects it will remain solvent and viable, and the Commission later can revisit the interim relief granted. If the Unwind closes, every dollar collected in the increase will be refunded.[18] While a refunded rate increase is not ideal, granting Big Rivers' interim rate request is the most prudent means to avoid insolvency. The sooner the interim relief is granted, the less the increase and shock to the Members there will be. Immediate approval by the Commission is an obvious and easy decision under these circumstances.

II. STANDARD OF REVIEW

In reviewing Big Rivers' requested emergency interim rate relief, the Commission should apply the standard of review set forth in KRS 278.190(2). That standard requires a finding that an emergency interim rate increase must be necessary to prevent a material impairment of the applicant's credit or operations. The record demonstrates that Big Rivers meets this standard.

III. BIG RIVERS' EMERGENCY RATE INCREASE IS PROPERLY SIZED AND NECESSARY TO PREVENT A MATERIAL IMPAIRMENT OF BIG RIVERS' CREDIT AND OPERATIONS

As demonstrated below, the rate increase sought is based on a best case estimate of Big Rivers' expected 2009 revenues and is the <u>minimum</u> amount, together with identified reductions, needed to satisfy Big Rivers' projected cash needs through January 2010. Establishing rates any

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[17] Direct Testimony of William Steven Seelye, Application Exhibit 46, p.14 at l. 1-2.
[18] Direct Testimony of Mark A. Bailey, Application Exhibit 45, p. 8, at l. 1-4; Direct Testimony of C. William Blackburn, Application Exhibit 47, p. 8, l. 1-22 - p. 9, l. 1-9.

lower would leave Big Rivers with an insufficient level of cash to fund its operations in a prudent and reliable manner and would endanger its ability to continue serving its Members.

A. Contrary to KIUC's claims, there is no additional \$6 million available to offset a three-month delay in the implementation of the requested relief.

Big Rivers' January 5, 2010 cash reserve levels are a critical element of this case. Big Rivers must increase cash to pay both PMCC its \$12.4 million on December 15, 2009 and the RUS its \$15.8 million on January 4, 2010. But it is equally critical that Big Rivers' cash levels thereafter permit it to meet its costs of operations. Big Rivers' request has been sized at the minimally acceptable level to do this, and is sufficient only if no unanticipated costs arise.[19] There is no margin for error as the rates include nothing to protect against unanticipated costs.

At the hearing, Mr. Kollen recommended a three-month delay in the consideration of this request because Big Rivers' calculation of its \$8.5 million expected January 2010 cash balance was \$5.7 million greater than a \$2.8 million *pro forma* cash balance found in Mr. Blackburn's testimony.[20] Because the requested rate increase would generate approximately \$2 million per month, Mr. Kollen suggested that a three-month delay would not harm Big Rivers given these "new" funds.[21] But this recommendation is based on the erroneous assumptions that Big Rivers had proposed to operate and could operate with a \$2.8 million cash balance. Big Rivers never did so and could not afford such an inadequate safety net.

Big Rivers has been unwavering in advocating a combination of the requested rate increase <u>and</u> one-time cost cuts and deferments as the only solution to its January 2010 cash crisis. The \$2.8 million figure cited by Mr. Kollen was to a projected Big Rivers' cash balance

[19] Testimony of C. William Blackburn, Tr. at 1:55'52 (amounts requested "do not include anything for any contingencies.")
[20] Testimony of Lane Kollen, Tr. at 2:45'47.
[21] Testimony of Lane Kollen, Tr. at 2:47'11 (Big Rivers will still have \$2.5 million if 3 month delay) & Tr. at 3:10'42.

which incorporated Big Rivers' *pro forma* costs and requested rate increase (and thus used the *pro forma* levels of O&M and capital expenditure) with no cost reductions.[22] In presenting the $2.8 million *pro forma* level of cash in its Application, Big Rivers' stressed that "[t]his amount would be augmented by any additional cost savings Big Rivers could obtain by deferral or elimination of costs."[23] The $2.8 million cash balance figure relied upon by Mr. Kollen as Big Rivers' proposal included none of the intended cost cuts and deferments Big Rivers is relying on as the necessary one-time source of funds to supplement the requested rate increase.

By contrast, the $8.5 million shown in Big Rivers' Redirect Exhibit 2 presented at the hearing, and included earlier in Big Rivers' response to Commission Staff's 2nd Data Request Item 6(b), is the January 5, 2010 cash balance Big Rivers expects after incorporating identified budget reductions.[24] Those cuts and deferments resulted in a reduction of Big Rivers' 2009 Transmission and A&G Capital and Construction Budget to $8.2 million, $9.9 million lower than the original 2009 budget of $18.1 million,[25] and $6.1 million lower than the *pro forma* level used to derive the $2.8 million figure.[26] There is thus no "new" $6 million cushion to support a three-month delay, as Big Rivers had already counted these funds. The $8.5 million projected cash balance is the bare minimum Big Rivers needs to remain solvent. A $2.8 million (or lower) cash balance on January 5, 2010 would be quickly depleted.

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[22] Direct Testimony of C. William Blackburn, Application Exhibit 47, p. 41, at l. 12-15; *see also* Notice, Application, and Motions, p. 7, at l. 17-20 ("Big Rivers must additionally defer or cancel certain budgeted expenditures in 2009 to have adequate cash for those purposes.")

[23] Direct Testimony of C. William Blackburn, Application Exhibit 47, p. 47, l. 13-15; Big Rivers' Response to Commission Staff's 2nd Data Request, Item 1(b), p. 2, l. 7-12 ("In seeking emergency interim rate relief in the amount requested, Big Rivers' March 2nd Application proposed reducing its cash on hand (as augmented by significant deferrals and cuts in Big Rivers' expenditures) to a bare minimum level in January of 2010 that left little to no room for Big Rivers to meet any additional unplanned adverse financial development that might arise between now and next January or in the months immediately thereafter.")

[24] Big Rivers' Response to Commission Staff 2nd Data Request, Item 6(b), p. 2, l. 22-25.

[25] *Id.*, Item 6(c) attachment at p.2.

[26] Exhibit Seelye-2 (to the Direct Testimony of William Steven Seelye, Application Exhibit 46), Schedule 1.03, line 4 shows a $14.3 million *pro forma* transmission and general capital expenditure.

Big Rivers explained its minimum cash requirements in its response to Commission Staff 2nd Item 1(b).[27] Big Rivers must retain cash to pay its daily operating costs at all times and must plan to bridge all gaps in its monthly cash inflows due to the timing of payments.[28] Big Rivers has a twenty-day gap between its WKEC rental payment on the first of the month and its payment from ACES Power Marketing ("APM") on the 20th of each month.[29] Big Rivers estimates that these monthly ordinary costs (budgeted O&M and capital expenditures associated with ongoing operations) amount to $10 million (i.e., $500,000 per day) over this twenty-day period.[30] Big Rivers thus needs to retain sufficient funds from January 5 to January 20 to pay 15 days of operations (5 days already having been incorporated into the January 5 cash balances).[31] Assuming representative costs of $7.5 million during these 15 days, a $2.8 million January 5, 2010 cash balance would be negative well in advance of January 20. By contrast, the $8.5 million cash balance provides just enough cash reserves to bridge this cash inflow gap.[32] Big Rivers can only achieve the $8.5 million cash balance with the rate increase and cost-cutting.

KIUC's inference at hearing that Big Rivers' cash crisis will somehow be over on January 25th when Big Rivers receives its Member payment is similarly erroneous.[33] Big Rivers' cash levels already will have been depleted from 20 days' of routine operations,[34] and the majority of those payments already will have been committed by Big Rivers to other cash needs such as power payments to E.ON and reserve funds for the next quarterly payment on the RUS

[27] Big Rivers' Response to Commission Staff 2nd Data Request, Item 1(b).
[28] *Id.* at p. 5, at l. 13-14.
[29] *Id.* at p. 5, at l. 14-18.
[30] Big Rivers' Response to Commission Staff 2nd Data Request, Item 1(b), p. 5, at l. 8-20.
[31] *Id.* at p. 6, at l. 18-24.
[32] *Id.*
[33] Testimony of C. William Blackburn, Tr. at 1:55'18; Testimony of Lane Kollen, Tr. at 4:08'14-4:09'04.
[34] Testimony of C. William Blackburn, Tr. 1:56'15 (normal expenses would include power purchase bills, payroll bills, and capital requirements).

New Note and the next pollution control bond ("PCB") interest payment.[35] Big Rivers also must reserve funds to cover the February gap in cash inflows. The same cash cannot be used for two purposes, and the closer Big Rivers approaches its next RUS New Note quarterly payment the higher its cash reserves must be.[36]

Historically, Big Rivers has used a thirteen-month average of one-eighth of its annual O&M expense (approximately $20.1 million during the test year) as its minimum cash requirements.[37] Big Rivers still believes this level of cash to be its true minimum cash reserves (exclusive of additional levels built up to meet unanticipated costs), but to help surmount the January 5, 2010 cash crisis it is willing to drop to the projected $8.5 million figure.[38] But under no circumstances would it be prudent to maintain cash reserves that low on a sustained basis.

B. Big Rivers' financing limitations are real, and undue reliance on its CFC line of credit and/or phantom unsecured lines of credit is not a prudent option, despite Mr. Kollen's unsupported speculation.

In supporting a three-month delay in the consideration of Big Rivers' emergency request, Mr. Kollen proposes that Big Rivers meet its January 2010 cash shortfall through a combination of draw downs on its existing $15 million secured CFC line of credit and new unsecured lines of credit he felt should be widely available from Big Rivers' local depositary bank or elsewhere.[39]

Mr. Kollen's first and repeated error lies in ignoring the financial "straitjacket" restricting all aspects of Big Rivers' operations.[40] Big Rivers has negative equity and no investment grade credit rating absent the Unwind.[41] Big Rivers' financing documents provide no flexibility to

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[35] Big Rivers' Response to Commission Staff 2nd Data Request, Item 1(b) at p. 5, l. 22-30, p. 6, l. 1-3; Testimony of C. William Blackburn, Tr. at 1:56'44
[36] Big Rivers' Response to Commission Staff 2nd Data Request, Item 1(b) at p. 5, l. 22-30 – p. 6., l. 1-3.
[37] Big Rivers' Response to Commission Staff 1st Data Request, Item 11, p. 1 at l. 24-27 & Item 11h.
[38] Big Rivers' Response to Commission Staff 2nd Data Request, Item 1(b), p. 6 at l. 28-30 – p. 7 at 1. 1-2.
[39] Testimony of Lane Kollen, Tr. at 2:54'20; 3:40:36; 4:06'46.
[40] Testimony of Lane Kollen, Tr. at 3:42'25 (concedes restrictions apply but nevertheless claims Big Rivers is same as other utilities).
[41] Big Rivers' Response to the Commission Staff's 1st Data Request, March 18, 2009, Item 2, p. 1, l. 19-20.

permit new secured lenders.[42] Existing lenders hold a first lien on all of Big Rivers' real and personal property.[43] And Big Rivers cannot pledge cash or cash receipts as security.[44]

Big Rivers' sole secured line of credit is its $15 million from CFC. This line serves two crucial roles for Big Rivers, neither of which can be met if it is depleted to meet daily operating costs. First, it is Big Rivers' only source for letters of credit to meet margin calls required by its power trading counterparties.[45] In 2007, Big Rivers simultaneously issued $14.5 million under this facility in support of trading.[46] Undue reliance on this line could impair, or even prevent, Big Rivers from making new sales.[47] Inability to transact in the market is a death sentence for Big Rivers and will lead to bankruptcy as surely as a default on debt payments.

Second, the CFC line of credit is the sole backstop for <u>any</u> new cash need, including unanticipated costs.[48] As Mr. Blackburn testified, if unanticipated costs arise and this line is not available, "There is no place to turn."[49] While Mr. Kollen may not blink at cavalierly expending this last Big Rivers lifeline, he does not bear the consequences of doing so once he returns to Georgia leaving Big Rivers and its Members to their fates should his recommendations leave Big Rivers with no available financing.[50] Although Mr. Kollen dismissed unanticipated costs as "hypothetical",[51] they are very real to Big Rivers, particularly if the Unwind terminates. New capital expenditures due to changes in law, environmental cost exposure, litigation risk with

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[42] Direct Testimony of C. William Blackburn, Application Exhibit 47, p. 13, l. 2-5.
[43] *Id.* at p. 13, l. 9-18.
[44] Testimony of C. William Blackburn, Tr. at 12:20'28 (Big Rivers cannot pledge accounts receivable or cash under RUS Mortgage).
[45] Big Rivers' Response to Commission Staff's 2nd Data Request, Item 1(a), p. 1, l. 20-28; Testimony of C. William Blackburn, Tr. at 2:13'43 (explanation of margin calls).
[46] Big Rivers' Response to Commission Staff's 2nd Data Request, Item 1(a), p. 1, l. 28-30.
[47] Testimony of C. William Blackburn Tr. at 11:37'57 (maxing out CFC letter of credit would "cripple" Big Rivers' ability to transact in the market).
[48] Big Rivers' Response to Commission Staff's 2nd Data Request, Item 1(a), p. 1 at l. 10-13.
[49] Testimony of C. William Blackburn, Tr. at 12:29'20.
[50] Testimony of Lane Kollen, Tr. at 4:14'59 (if projections are wrong regarding future "it is whatever it is.")
[51] Testimony of Lane Kollen, Tr. at 4:16'05.

E.ON or the Smelters, and changes in load growth are all among the unbudgeted costs which could cause Big Rivers to take temporary recourse to the CFC line of credit.[52]

Despite Mr. Kollen's attempt to jam Big Rivers' square peg into the typical utility round hole, Big Rivers is quite unlike the utilities he offered in recommending reliance on lines of credit. None has a negative equity like Big Rivers does,[53] nor do any have similar financing limitations[54] or lines of credit as low as Big Rivers' available $15 million.[55] Further, Big Rivers is unsure if it can prudently rely on the CFC line of credit. Were CFC to decide there had been a material adverse change in Big Rivers' financial condition, operations or business prospects from the information provided at the time it entered into the line of credit, CFC could decline an advance.[56] Placing Big Rivers in a position of reliance where any CFC hesitation could lead to financial ruin is not prudent.

Moreover, Mr. Kollen's unsupported opinion that Big Rivers can borrow $10 to $15 million from a bank without security is mere speculation.[57] Rather than indulge that speculation, the Commission should defer to Big Rivers' considered business judgment, based as it is on intimate familiarity with Big Rivers' financial status and actual experience working with lenders.[58] Mr. Kollen has not investigated the availability of unsecured financing and has little or no actual experience in borrowing on a utility's behalf, yet he concludes it should be available

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[52] Direct Testimony of C. William Blackburn, Application Exhibit 47, at pp. 44-49.
[53] Testimony of Lane Kollen, Tr. at 3:41'18.
[54] Testimony of Lane Kollen, Tr. at 3:41'52.
[55] *See* Testimony Lane Kollen, Tr. at 3:43:35 (the amount of financing available to other utilities is "[g]enerally substantially greater than $15 million.")
[56] Big Rivers' Response to the Commission Staff 2nd Data Request, Item 1(a), p. 2 at l. 6-18 & Item 6(d), p. 4 at l. 13-17; Testimony of C. William Blackburn, Tr. at 12:25'04-12:27'04.
[57] Testimony of Lane Kollen, Tr. at 4:06'46 & 4:18'45.
[58] *See In the Matter of: Request for Assistance in the Appointment of Breathitt County Water District Commissioners,* PSC Case No. 2007-00493 (deferral to local water official's judgment); *State of Missouri ex rel. Southwestern Bell Telephone Co. v. Public Service Comm'n of Missouri,* 262 U.S. 276, 288-89 (U.S. 1923) (state commissions should defer to utility financial managers).

due to the "strength" of Big Rivers' income statement.[59] Without the name of a single bank or financial institution that would actually lend to Big Rivers on an unsecured basis, Mr. Kollen's conjecture is without probative value. Again, Mr. Kollen ignores or underestimates Big Rivers' inability under its mortgage to pledge its cash or its income statements to borrow money.[60] Given the weakness of the financial sector in general, and Big Rivers' low cash levels in particular, Big Rivers' management does not share Mr. Kollen's unsubstantiated and exceedingly optimistic assumptions regarding the prospects for unsecured financing from a depository bank.[61] There is simply no basis for giving credence to Mr. Kollen's speculation over the exercise of Big Rivers' management's business judgment,[62] and it would be entirely unreasonable to bet Big Rivers' future on Mr. Kollen's pure speculation that some financing might be available.

C. KIUC's proposed adjustments are meritless and do not support delay.

KIUC's alternative ground for rejecting Big Rivers' requested emergency rates is that Big Rivers' *pro forma* revenue requirement is understated annually by $25.2 million, thus eliminating the need for the proposed $24.9 million increase.[63] Again, KIUC advocates the path of delay, urging the Commission to revisit this request in three months if needed. These adjustments are meritless, and delay would create a need for shock-level Member rates later.

First, Mr. Kollen reduces Big Rivers' debt service interest by $5.0 million annually based on reduction of PCB interest from 18% to 12%.[64] Again, Mr. Kollen speculates regarding Big Rivers' ability to refinance its obligations, ignoring facts which contradict his claim. Big Rivers did not elect to enter into a debt obligation at this rate of interest – the interest rates are a side

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[59] Testimony of Lane Kollen, Tr. at 3:48'10.
[60] Testimony of C. William Blackburn, Tr. at 12:20:28.
[61] Testimony of C. William Blackburn, Tr. at 11:33:34.
[62] Testimony of C. William Blackburn, Tr. at 11:34'58.
[63] KIUC Direct Exhibit 1; Testimony of Lane Kollen, Tr. at 3:05'29-3:10'42.
[64] Testimony of Lane Kollen, Tr. at 3:09'01.

effect of Ambac's reduced credit rating.[65] Big Rivers is well aware of the desirability of refinancing this PCB debt.[66] But with the Unwind pending it makes no sense to consider a speculative private placement that would need to be redone or abandoned upon an Unwind closing, as an investment grade credit rating would greatly facilitate the cost and timing of a refinancing.[67] Absent that credit rating, it would be "difficult, if not impossible to find someone who will step forward to assist in the refinancing."[68] Mr. Kollen's speculation as to Big Rivers' ability to refinance the PCB's at his chosen interest rate are not grounds to delay or reduce the interim rate request as Big Rivers would not be able to satisfy its obligations if he is wrong.[69]

Moreover, refinancing the PCBs is an expensive, labor intensive process which cannot be accomplished at the snap of Mr. Kollen's fingers to produce the cost savings he assumes. Big Rivers estimates the costs of a PCB refinancing to be a one-time \$5.5 million.[70] A refinancing likely would take six months or longer to complete due to RUS and RUS outside counsel involvement to revise Big Rivers' security documents.[71] The cost of an immediate refinancing thus would outweigh the pro-rated speculative 2009 benefit (\$3.3 million), assuming an unrealistic completion with RUS involvement before January.

Mr. Kollen's second and third adjustments incorporate Big Rivers' one-time 2009 cost savings and deferments in O&M (\$2.2 million)[72] and capital expenditures (\$6.1 million)[73] as

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[65] Direct Testimony of William C. Blackburn, Application Exhibit 47, p. 49, l. 16-p. 50, l. 7.
[66] Testimony of Mark A. Bailey, Tr. at 10:27'22 ("It would be in Big Rivers' interest to refinance as soon as possible.")
[67] Testimony of C. William Blackburn, Tr. at 11:15'45 (within 6 months of closing of unwind).
[68] Testimony of C. William Blackburn, Tr. 11:18'28; Testimony of Mark A. Bailey, Tr. at 10:26'52 ("I'm not sure how easy it would be to refinance them with no credit rating."); Direct Testimony of C. William Blackburn, Application Exhibit 47, p. 50 at l. 9-13.
[69] Moreover, basing rates on such speculation is inappropriate. *See* Order dated October 6, 1989, in *In the Matter of: Columbia Gas of Kentucky, Inc.*, PSC Case No. 10498 (rejecting a proposed *pro forma* adjustment based on unsupported projections).
[70] Testimony of C. William Blackburn, Tr. at 12:13'14-28.
[71] Testimony of Mark A. Bailey, Tr. at 10:50'20 -10:50'45.
[72] Testimony of Lane Kollen, Tr. at 3:05'29 (\$2.2 million is one-half the Big Rivers 2009 proposed O&M cuts).

permanent *pro forma* adjustments to Big Rivers' revenue requirement. These adjustments are improper and not in accord with ratemaking principles.[74] Big Rivers' *pro forma* includes a going-forward representative level of Big Rivers' just and reasonable costs of prudent and reliable operations. By contrast, the bare bones reduced 2009 $4.4 million O&M and $8.2 billion capital budgets are one-time cost savings or deferrals to offset the costs of the one-time $12.4 million PMCC payment.[75] The PMCC payment's costs are <u>not</u> in Big Rivers' *pro forma* revenue requirement, and thus these offsets should not be included either.[76] Reliable operation will require Big Rivers to restore deferred costs as soon as it can, and there is no cause to reduce Big Rivers' revenue requirement to replace representative costs with one-time costs.

Mr. Kollen's fourth adjustment increases Big Rivers' *pro forma* arbitrage revenues by $12.5 million.[77] He calculates this amount as the difference between his projected $38.7 million level of going-forward arbitrage margins taken from Big Rivers' 2009 budget and a calculated $26.5 million figure for test-year arbitrage margins.[78] Mr. Kollen reached this $26.5 million figure by starting with 2008 calendar year arbitrage margins of $45.5 million as a substitute for the test year arbitrage margins. He then subtracted from this $45.5 million Big Rivers' calculated $18.9 million *pro forma* adjustment to reach a test year $26.5 million amount.[79]

Mr. Kollen's calculation is wrong. He begins by improperly rejecting Big Rivers' test year amount based on a mistaken assumption. In response to KIUC's hearing data request, Big

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[73] *Id.* at 3:06'20 (This represents a full $6.1 million reduction in 2009 cuts from the $14.3 million *pro forma* amount).
[74] Under the Commission's rate-making principles, *pro forma* adjustments should be made to reflect representative revenues and expenses going forward. *See* Order dated October 6, 1989, in *In the Matter of: Columbia Gas of Kentucky, Inc.*, PSC Case No. 10498.
[75] Testimony of Mark A. Bailey, Tr. at 10:29'38 ("The plan was to address the Phillip Morris note issue through internal cost cutting. That was a one-time situation so it was not reflected in any *pro forma* adjustment.")
[76] Testimony of Mark A. Bailey, Tr. at 10:29'38; Testimony of William C. Blackburn, Tr. at 1:53'46.
[77] Testimony of Lane Kollen, Tr. at 3:08'16.
[78] *Id.*
[79] Testimony of Lane Kollen, Tr. at 2:58'45-3:01'38.

Rivers has shown that test year arbitrage margins were $47.1 million (not the $51 million KIUC claims Big Rivers used).[80] While this figure is similar to KIUC's calendar year 2008 $45.5 million figure, it has the benefit of being the actual Dec. 2007 to Nov. 2008 historical test year amount. Mr. Kollen also errs in assuming Big Rivers' full $18.9 million *pro forma* adjustment was related to arbitrage margins. The adjusted margins amount was $15.0 million as the other $3.9 million relates to increased off-system purchases for Members and not arbitrage margins.[81]

But there is no logic to Mr. Kollen's next step in which he reduces his inaccurate calendar year arbitrage margins using Big Rivers' $18.9 million *pro forma* adjustment (which, as shown above should be $15.0 million). Big Rivers' adjustment was a calculated figure based on its forecast of projected sales volumes and projected sales prices. Subtracting it from KIUC's alternative test year amount of $45.5 million would make sense only if KIUC were accepting those projected sales volumes and prices, and then calculating its proposed adjustment. Instead, KIUC reduces Big Rivers' projections to get a deflated $26.5 million <u>test year</u> level. KIUC then subtracts this already reduced test year amount from an outdated estimate of future volumes and prices, the $38.7 million from the 2009 Big Rivers budget. Mr. Kollen's suggested adjustment to *pro forma* arbitrage margins is wrong and should be given no weight.

Mr. Kollen's second error is favoring the outdated Big Rivers' 2009 budgeted level of $38.7 million as the *pro forma* margins in lieu of Big Rivers' $32.2 million calculation. There is no basis for using the outdated projections. The 2009 budget used a September 2008 forward power curve that is now $30/MWh higher than March 2009 forward power curves, and $20/MWh higher than the January 22, 2009 forward power curve Big Rivers used.[82] The

[80] Big Rivers' Hearing Data Request Response, March 30, 2009, Item 1, p. 6, and attachment 1, l. 54.
[81] *Id.* at p. 6, l. 1-27 and attachment 1, l. 55.
[82] Testimony of C. William Blackburn, Tr. at 12:29'40-12:31'22.

September budget also projected lucrative Smelter Tier 3 sales through the end of 2009, rather than through August 2009 as in Big Rivers' *pro forma*.[83]

Big Rivers' *pro forma* adjustment now constitutes a *best case* estimate for 2009 margins given known changes that likely will further reduce revenues.[84] March 2009 forward power curves are materially lower than those in January.[85] Lucrative Tier 3 sales projected through the end of August 2009 terminate 60 days after termination of the Unwind, and could end as early as the end of June 2009.[86] And Century and Alcan recently have discontinued 30 MW of around the clock interruptible power priced at $44/MWh, further reducing revenue included in Big Rivers' *pro forma*.[87] Big Rivers' *pro forma* level is most likely $8 million too high, not $12.5 million too low.[88]

IV. CONCLUSION

In order to have a reasonable chance to operate without materially damaging its credit and operations, Big Rivers needs an additional $16 million in cash by year end as augmented by its identified $13.9 million in cost reductions. Big Rivers sought interim rate relief effective April 1, 2009. The Commission's order directing briefs on April 8, 2009 effectively denies that request. But if the effective date of interim relief is delayed, the amount of the interim relief must be increased proportionally to collect the same amount of cash by year-end. Big Rivers therefore asks that the relief granted by the Commission correspond to the level of relief shown on Big Rivers Redirect Exhibit 1, (attached to this brief as Appendix A), based upon the effective date of that relief, to generate the required $16 million in cash by year end.

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[83] *Id.* at 12:30'00-12:30'42 (2009 budget had 12 months of Tier 3 at $58/MWh vs. 8 months in *pro forma*).
[84] Big Rivers' Response to Commission Staff 2nd Data Request, Item 6(b), p. 3, l. 4-26.
[85] Testimony of C. William Blackburn, Tr. at 12:11:31-12:12:42; 12:31'22-12:31'38.
[86] *Id.*, Tr. at 12:08'31-12:09'21.
[87] Big Rivers' Hearing Data Request Response, March 30, 2009, Item 1, p. 3, l.25-p. 4, 1-6;
[88] Big Rivers' Response to Commission Staff Data Request, Item 6, p. 4 at l. 2-4.

SCHEDULE OF REQUIRED INTERIM RATES BY EFFECTIVE DATE

			Rural		Large Industrial		Cogen & Small
			Rate - $/kW-Month	Rate - $/kWh	Rate - $/kW-Month	Rate - $/kWh	Rate - $/kW-Week
Date	Rate Increase	Change	7.370	0.020400	10.150	0.013715	1.8350
4/1/2009	21.62%		8.963	0.024811	12.345	0.016680	2.2408
4/2/2009	21.71%	0.09%	8.970	0.024829	12.354	0.016693	2.2425
4/3/2009	21.80%	0.09%	8.977	0.024847	12.363	0.016705	2.2442
4/4/2009	21.89%	0.09%	8.983	0.024866	12.372	0.016717	2.2458
4/5/2009	21.98%	0.09%	8.990	0.024884	12.381	0.016730	2.2475
4/6/2009	22.07%	0.09%	8.997	0.024902	12.390	0.016742	2.2491
4/7/2009	22.17%	0.10%	9.004	0.024923	12.400	0.016756	2.2510
4/8/2009	22.26%	0.09%	9.011	0.024941	12.409	0.016768	2.2526
4/9/2009	22.35%	0.09%	9.017	0.024959	12.419	0.016780	2.2543
4/10/2009	22.45%	0.10%	9.025	0.024980	12.429	0.016794	2.2561
4/11/2009	22.55%	0.10%	9.032	0.025000	12.439	0.016808	2.2580
4/12/2009	22.64%	0.09%	9.039	0.025019	12.448	0.016820	2.2596
4/13/2009	22.74%	0.10%	9.046	0.025039	12.458	0.016834	2.2615
4/14/2009	22.84%	0.10%	9.053	0.025059	12.468	0.016848	2.2633
4/15/2009	22.94%	0.10%	9.061	0.025080	12.478	0.016861	2.2652
4/16/2009	23.04%	0.10%	9.068	0.025100	12.489	0.016875	2.2670
4/17/2009	23.14%	0.10%	9.075	0.025121	12.499	0.016889	2.2689
4/18/2009	23.24%	0.10%	9.083	0.025141	12.509	0.016902	2.2707
4/19/2009	23.35%	0.11%	9.091	0.025163	12.520	0.016917	2.2727
4/20/2009	23.45%	0.10%	9.098	0.025184	12.530	0.016931	2.2746
4/21/2009	23.56%	0.11%	9.106	0.025206	12.541	0.016946	2.2766
4/22/2009	23.66%	0.10%	9.114	0.025227	12.551	0.016960	2.2784
4/23/2009	23.77%	0.11%	9.122	0.025249	12.563	0.016975	2.2805
4/24/2009	23.88%	0.11%	9.130	0.025272	12.574	0.016990	2.2825
4/25/2009	23.99%	0.11%	9.138	0.025294	12.585	0.017005	2.2845
4/26/2009	24.10%	0.11%	9.146	0.025316	12.596	0.017020	2.2865
4/27/2009	24.21%	0.11%	9.154	0.025339	12.607	0.017035	2.2886
4/28/2009	24.32%	0.11%	9.162	0.025361	12.618	0.017050	2.2906
4/29/2009	24.43%	0.11%	9.170	0.025384	12.630	0.017066	2.2926
4/30/2009	24.55%	0.12%	9.179	0.025408	12.642	0.017082	2.2948
5/1/2009	24.66%	0.11%	9.187	0.025431	12.653	0.017097	2.2969

SCHEDULE OF REQUIRED INTERIM RATES BY EFFECTIVE DATE

			Rural		Large Industrial		Cogen & Small
			Rate - $/kW-Month	Rate - $/kWh	Rate - $/kW-Month	Rate - $/kWh	Rate - $/kW-Week
Date	Rate Increase	Change	7.370	0.020400	10.150	0.013715	1.8350
5/2/2009	24.78%	0.12%	9.196	0.025455	12.665	0.017114	2.2991
5/3/2009	24.90%	0.12%	9.205	0.025480	12.677	0.017130	2.3013
5/4/2009	25.02%	0.12%	9.214	0.025504	12.690	0.017146	2.3035
5/5/2009	25.14%	0.12%	9.223	0.025529	12.702	0.017163	2.3057
5/6/2009	25.26%	0.12%	9.232	0.025553	12.714	0.017179	2.3079
5/7/2009	25.38%	0.12%	9.241	0.025578	12.726	0.017196	2.3101
5/8/2009	25.50%	0.12%	9.249	0.025602	12.738	0.017212	2.3123
5/9/2009	25.63%	0.13%	9.259	0.025629	12.751	0.017230	2.3147
5/10/2009	25.75%	0.12%	9.268	0.025653	12.764	0.017247	2.3169
5/11/2009	25.88%	0.13%	9.277	0.025680	12.777	0.017264	2.3193
5/12/2009	26.01%	0.13%	9.287	0.025706	12.790	0.017282	2.3217
5/13/2009	26.14%	0.13%	9.297	0.025733	12.803	0.017300	2.3241
5/14/2009	26.27%	0.13%	9.306	0.025759	12.816	0.017318	2.3265
5/15/2009	26.40%	0.13%	9.316	0.025786	12.830	0.017336	2.3289
5/16/2009	26.53%	0.13%	9.325	0.025812	12.843	0.017354	2.3313
5/17/2009	26.66%	0.13%	9.335	0.025839	12.856	0.017371	2.3337
5/18/2009	26.79%	0.13%	9.344	0.025865	12.869	0.017389	2.3361
5/19/2009	26.93%	0.14%	9.355	0.025894	12.883	0.017408	2.3387
5/20/2009	27.07%	0.14%	9.365	0.025922	12.898	0.017428	2.3413
5/21/2009	27.21%	0.14%	9.375	0.025951	12.912	0.017447	2.3438
5/22/2009	27.35%	0.14%	9.386	0.025979	12.926	0.017466	2.3464
5/23/2009	27.49%	0.14%	9.396	0.026008	12.940	0.017485	2.3490
5/24/2009	27.64%	0.15%	9.407	0.026039	12.955	0.017506	2.3518
5/25/2009	27.79%	0.15%	9.418	0.026069	12.971	0.017526	2.3545
5/26/2009	27.93%	0.14%	9.428	0.026098	12.985	0.017546	2.3571
5/27/2009	28.08%	0.15%	9.439	0.026128	13.000	0.017566	2.3599
5/28/2009	28.23%	0.15%	9.451	0.026159	13.015	0.017587	2.3626
5/29/2009	28.38%	0.15%	9.462	0.026190	13.031	0.017607	2.3654
5/30/2009	28.53%	0.15%	9.473	0.026220	13.046	0.017628	2.3682
5/31/2009	28.68%	0.15%	9.484	0.026251	13.061	0.017648	2.3709
6/1/2009	28.83%	0.15%	9.495	0.026281	13.076	0.017669	2.3737