COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

ELECTRONIC APPLICATION OF KENTUCKY POWER COMPANY FOR AN ORDER APPROVING ACCOUNTING PRACTICES TO ESTABLISH A REGULATORY ASSET RELATED TO THE EXTRAORDINARY EXPENSES INCURRED BY KENTUCKY POWER COMPANY IN CONNECTION WITH CHARGES RELATED TO GREENHAT ENERGY, LLC DEFAULT	)))))))))	CASE NO. 2020-00034

O R D E R

On February 14, 2020, Kentucky Power Company (Kentucky Power) filed an application, pursuant to KRS 278.030, KRS 278.040, and KRS 278.220, requesting authority to establish a regulatory asset for Kentucky Power's expenses incurred in connection with PJM Interconnection, LLC (PJM) Billing Line Item 1999A (BLI 1999A) as a result of the GreenHat Energy, LLC (GreenHat) default.

By Order dated February 27, 2020, the Commission established a procedural schedule for the processing of this matter. The procedural schedule provided for a deadline for intervention requests and two rounds of discovery upon Kentucky Power's application. There were no parties requesting intervenor status to this proceeding. On May 5, 2020, Kentucky Power requested that the Commission take this matter under submission without a hearing. Because there are no intervenors in this case and a hearing is not necessary in the public interest, the Commission will adjudicate this case based on the evidence of record.

BACKGROUND

The Financial Accounting Standards Board's Statement of Financial Accounting Standards No. 71, Accounting for the Effects of Certain Types of Regulation, which was codified as Accounting Standards Codification (ASC) 980, Regulated Operations, provides the criteria for recognition of a regulatory asset.[1] The Commission has historically approved regulatory assets where a utility has incurred (1) an extraordinary, nonrecurring expense, which could not have reasonably been anticipated or included in the utility's planning; (2) an expense resulting from a statutory or administrative directive; (3) an expense in relation to an industry sponsored initiative; or (4) an extraordinary or nonrecurring expense that over time will result in a saving that fully offsets the cost.[2]

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[1] ASC 980-340-25-1 provides, in full, as follows:

> **25-1** Rate actions of a regulator can provide reasonable assurance of the existence of an asset. An entity shall capitalize all or part of an incurred cost that would otherwise be charged to expense if both of the following criteria are met:
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> a. It is probable (as defined in Topic 450) that future revenue in an amount at least equal to the capitalized cost will result from inclusion of that cost in allowable costs for rate-making purposes.
>
> b. Based on available evidence, the future revenue will be provided to permit recovery of the previously incurred cost rather than to provide for expected levels of similar future costs. If the revenue will be provided through an automatic rate-adjustment clause, this criterion requires that the regulator's intent clearly be to permit recovery of the previously incurred cost.
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> A cost that does not meet these asset recognition criteria at the date the cost is incurred shall be recognized as a regulatory asset when it does meet those criteria at a later date.

[2] Case No. 2008-00436, *The Application of East Kentucky Power Cooperative, Inc. for an Order Approving Accounting Practices to Establish a Regulatory Asset Related to Certain Replacement Power Costs Resulting from Generation Forced Outages* (Ky. PSC Dec. 23, 2008), Order at 4.

GreenHat was a PJM member that participated in the Financial Transmission Rights (FTR) market. On June 21, 2018, GreenHat defaulted on its obligations in the FTR market and PJM initiated liquidation of its remaining FTR portfolio.[3] As an FTR market participant, Kentucky Power was allocated GreenHat default charges through BLI 1999A beginning in July 2018 and expects the last charge in June 2021.[4] The Commission denied recovery of the GreenHat default charges through Kentucky Power's Fuel Adjustment Clause (FAC) in its most recent FAC 2-year review case on the basis that the PJM BLI 1999 is not included in the Commission-approved enumerated BLIs listed in Kentucky Power's FAC tariff.[5]

KENTUCKY POWER'S PROPOSAL

Kentucky Power expects that it will be allocated $335,261 of GreenHat default expense for July 2018 through June 2021.[6] Of this amount, Kentucky Power states that that $47,383 would be associated with off-system sales margins and included in its System Sales Clause factor calculation.[7] Kentucky Power contends that it had a reasonable and good faith basis to conclude that the GreenHat default charges were recoverable through its FAC.[8] Kentucky Power claims that the GreenHat default charges

[3] Application at 2.

[4] Application at 2 and 4 and Kentucky Power's response to Commissions Staff's First Request for Information (Staff's First Request) (filed Apr. 1, 2020), Item 2.

[5] Case No. 2019-00002, *Electronic Examination of the Fuel Adjustment Clause of Kentucky Power Company from November 1, 2016 through October 31, 2018* (Ky. PSC Dec. 26, 2019).

[6] Application at 3. *See also* Kentucky Power's response to Staff's First Request, Item 2 and Item 3, Attachment 1. Kentucky Power recorded GreenHat default charges of $132,456 in 2018 and $136,061 in 2019 and expects to record $64,954 in 2020 and $1,790 in 2021.

[7] Direct Testimony of Ranie K. Wohnhas (Wohnhas Testimony) at 4.

[8] Application at 5.

are “nonrecurring and extraordinary in their causes, scope, and amount.”[9] Therefore, Kentucky Power requests authority to establish a regulatory asset for the GreenHat default charges.[10] Kentucky Power proposes that this treatment be granted for the GreenHat default charges from 2018 and 2019 and any future GreenHat Default charges, expected to end in June 2021.[11]

Kentucky Power explains that FTR are hedges for congestion costs on the transmission systems controlled by PJM and that its FTR charges and credits flow through its FAC.[12] Kentucky Power asserts that it could not have anticipated nor planned for the default and the resulting default charges.[13] Kentucky Power states that it has not included the GreenHat default charges in its FAC or System Sales Clause.[14] Kentucky Power asserts that it recorded both a regulatory asset and an offsetting credit for the GreenHat default expenses because it did not have sufficient time between the denial of FAC recovery on December 26, 2019, and the closing of its 2019 books to receive approval of a regulatory asset.[15] Kentucky Power states that these offsetting entries serve as a memo entry for internal reporting purposes only and did not impact the expenses reported on its financial statements.[16]

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[9] *Id.*

[10] Application at 6.

[11] *Id.* and Kentucky Power’s response to Staff’s First Request, Item 2.

[12] Wohnhas Testimony at 3 and 5–6.

[13] *Id.* at 8.

[14] *Id.* at 6.

[15] Kentucky Power’s response to Staff’s First Request, Item 4(a) and Kentucky Power’s response to Commission Staff’s Second Request (Staff’s Second Request) (filed Apr. 30, 2020), Item 1(a).

[16] Kentucky Power’s response to Staff’s First Request, Item 4(a).

<u>DISCUSSION</u>

As described above, Kentucky Power argues that the GreenHat default expenses should be treated as a regulatory asset because they are extraordinary or nonrecurring expenses, which could not have reasonably been anticipated or included in its planning. Kentucky Power also argues that, on an absolute basis, its GreenHat default charges cannot be fairly characterized as *de minimis*.[17] Kentucky Power's total allocated default charges, which span 36 months, are estimated to be $335,261. Kentucky Power's 2018 and 2019 transmission expenses were $38.5 million and $52.5 million, respectively, of which Kentucky Power's total GreenHat default charges equate to less than 1 percent.[18]

The Commission has historically not allowed a utility to establish a regulatory asset after a cost has been recorded as an expense and the utility has closed its books for the relevant fiscal year.[19] The Commission has also historically denied regulatory asset treatment for expenses deemed immaterial.[20] The Commission finds that Kentucky Power has failed to establish that the expenses at issue are material to Kentucky Power's financial position and therefore warrant deferral accounting, and therefore Kentucky Power's request to establish a regulatory asset for GreenHat default charges should be denied. Regarding Kentucky Power's contention that the GreenHat default could not

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[17] Kentucky Power's response to Staff's Second Request, Item 2(d).

[18] Kentucky Power's response to Staff's First Request, Item 5, Attachment 1 at 1.

[19] Case No. 2010-00523, *Application of Duke Energy Kentucky, Inc. for an Order Approving the Establishment of a Regulatory Asset Related to Voluntary Opportunity and Other Post-Retirement Expenses* (Ky. PSC July 14, 2011).

[20] Case No. 2000-00120, *Application of Kentucky-American Water Company to Increase Its Rates* (Ky. PSC Nov. 27, 2000), final Order at 20–22 and Case No. 2008-00440, *Request of Kentucky-American Water Company for Approval to Defer Certain Expenses as Regulatory Assets* (Ky. PSC Aug. 26, 2009).

have been anticipated and that it had no ability to mitigate the default charges, the Commission notes that the Report of the Independent Consultants on the GreenHat Default identified a participant default in PJM's FTR market 12 years earlier that had similarities to the GreenHat default.[21] The Commission also notes that as a Load Serving Entity and a Transmission Owner within PJM, FTRs and their related policies are central to Kentucky Power's on-going participation in PJM. Kentucky Power's membership in PJM requires diligent participation, including ensuring adequate and appropriate market and credit rules. Kentucky Power and other members failed to fulfill these requirements in the case of the rules that led to the GreenHat default. Given that Kentucky Power's ratepayers bear the costs of Kentucky Power's membership and participation in PJM, the Commission expects Kentucky Power to vigorously work through the PJM stakeholder process to protect its customers' interests.[22] Since Kentucky Power's customers effectively pay the cost of PJM membership and participation, they should not also bear the burden of ensuring PJM rules, and in this case credit rules, are adequate. That is the job of Kentucky Power as the PJM member.

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[21] Report of the Independent Consultants on the GreenHat Default at 15. This report can be accessed via the following link: https://www.pjm.com/-/media/library/reports-notices/special-reports/2019/report-of-the-independent-consultants-on-the-greenhat-default.pdf (Last viewed Aug, 24, 2020).

[22] Case No. 2017-00179, *Electronic Application of Kentucky Power Company for (1) A General Adjustment of Its Rates for Electric Service; (2) An Order Approving Its 2017 Environmental Compliance Plan; (3) An Order Approving its Tariffs and Riders; (4) An Order Approving Accounting Practices to Establish Regulatory Assets and Liabilities; and (5) An Order Granting All Other Required Approvals and Relief* (Ky. PSC Jan. 18, 2018), final Order at 54.

CONCLUSION

Based on the evidence of record and being otherwise sufficiently advised, the Commission finds that Kentucky Power's request to establish a regulatory asset should be denied.

IT IS THEREFORE ORDERED that:

1. Kentucky Power's request for authorization to establish a regulatory asset for the deferral of GreenHat default charges is denied.

2. This case is closed and removed from the Commission's docket.

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By the Commission

ENTERED

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