

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

ELECTRONIC APPLICATION OF KENTUCKY)	
POWER COMPANY FOR APPROVAL OF A)	
CERTIFICATE OF PUBLIC CONVENIENCE AND)	
NECESSITY FOR ENVIRONMENTAL PROJECT)	CASE NO.
CONSTRUCTION AT THE MITCHELL)	2021-00004
GENERATING STATION, AN AMENDED)	
ENVIRONMENTAL COMPLIANCE PLAN, AND)	
REVISED ENVIRONMENTAL SURCHARGE)	
TARIFF SHEETS)	

ORDER

On August 19, 2021, the Commission granted Kentucky Power Company's (Kentucky Power) request for partial rehearing of the July 15, 2021 final Order in this proceeding. Kentucky Power requested and the Commission granted rehearing on the following issues: (1) Kentucky Power's proposed 20 percent annual depreciation rate for coal combustion residual rule (CCR) compliance investments at Mitchell Generation Station (Mitchell); (2) Kentucky Power's request that \$1.903 million of Kentucky jurisdictional Mitchell effluent limitations guidelines (ELG) compliance costs incurred prior to the July 15, 2021 Order be deemed prudently incurred; and (3) Kentucky Power's request for regulatory asset treatment for \$1.903 million of Kentucky jurisdictional Mitchell ELG costs incurred prior to July 15, 2021 Order, for which Kentucky Power will request recovery in its next base rate case.

The Attorney General of the Commonwealth of Kentucky, by and through the Office of Rate Intervention (Attorney General), Kentucky Industrial Utility Customers, Inc.

(KIUC), and Sierra Club are intervenors in this proceeding. The Attorney General and KIUC (jointly, Attorney General/KIUC) jointly sponsored a witness and filed a joint response to the rehearing request. Kentucky Power responded to multiple rounds of rehearing data requests and filed updated responses to Commission Staff's Rehearing Request for Information, Item 1, every ten days as required. This matter now stands submitted for a final decision on rehearing.

LEGAL STANDARD

KRS 278.400, which establishes the standard of review for motions for rehearing, limits rehearing to new evidence not readily discoverable at the time of the original hearings, to correct any material errors or omissions, or to correct findings that are unreasonable or unlawful. A Commission Order is deemed unreasonable only when “the evidence presented leaves no room for difference of opinion among reasonable minds.”¹ An Order can only be unlawful if it violates a state or federal statute or constitutional provision.²

By limiting rehearing to correct material errors or omissions, and findings that are unreasonable or unlawful, or to weigh new evidence not readily discoverable at the time of the original hearings, KRS 278.400 is intended to provide closure to Commission proceedings. Rehearing does not present parties with the opportunity to relitigate a matter fully addressed in the original Order.

¹ *Energy Regulatory Comm'n v. Kentucky Power Co.*, 605 S.W.2d 46 (Ky. App. 1980).

² *Public Service Comm'n v. Conway*, 324 S.W.3d 373, 377 (Ky. 2010); *Public Service Comm'n v. Jackson County Rural Elec. Coop. Corp.*, 50 S.W.3d 764, 766 (Ky. App. 2000); *National Southwire Aluminum Co. v. Big Rivers Elec. Corp.*, 785 S.W.2d 503, 509 (Ky. App. 1990).

In accordance with KRS 278.030 and case law, Kentucky Power is allowed to charge its customers only fair, just and reasonable rates.³ Pursuant to KRS 278.190(3), Kentucky Power has the affirmative burden of proof to show that the proposed rates and expenses are just and reasonable.

KRS 278.183 provides that a utility shall be entitled to the current recovery of costs to comply with certain federal, state, or local environmental requirements that apply to coal combustion wastes and by-products from facilities used for the production of energy from coal. The Commission must render a decision that considers and, if the plan and rate surcharge are found reasonable and cost-effective for compliance with the applicable environmental requirements, approves the compliance plan and rate surcharge. The Commission must also establish a reasonable return on compliance-related capital expenditures and approve the application of the surcharge.

A regulatory asset is created when a rate-regulated business is authorized by its regulatory authority to capitalize an expenditure that under traditional accounting rules would be recorded as a current expense, which allows the regulated business the opportunity to request recovery in future rates of the amount capitalized. The authority for establishing regulatory assets arises under the Commission's plenary authority to regulate utilities under KRS 278.040 and the Commission's authority to establish a system of accounts under KRS 278.220. The criteria for recognition of a regulatory asset is codified as Accounting Standards Codification (ASC) 980, Regulated Operations in the Financial Accounting Standards Board's Statement of Financial Accounting Standards No. 71, Accounting for the Effects of Certain Types of Regulation. The Commission has

³ *Public Serv. Comm'n v. Com. ex rel. Conway*, 324 S.W.3d 373, 377 (Ky. 2010).

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.⁴

BACKGROUND

Kentucky Power and its affiliate, Wheeling Power Company (Wheeling Power), each have an undivided 50 percent interest in Mitchell, which is located in West Virginia. Kentucky Power is subject to the jurisdiction of this Commission. Wheeling Power is subject to the jurisdiction of the West Virginia Public Service Commission (WVPSC).

Kentucky Power filed this application requesting, among other things, a Certificate of Public Convenience and Necessity (CPCN) to construct projects at Mitchell to comply with revisions to federal CCR and ELG rules. In the July 15, 2021 Order, the Commission found that Kentucky Power provided sufficient evidence that the CCR project was needed to comply with CCR environmental regulations while providing safe, adequate, and reasonable service to Kentucky Power's customers and would not create a wasteful duplication of facilities, and thus met the legal standard to approve a CPCN under KRS 278.020 and KRS 278.183.

The Commission further found that Kentucky Power failed to provide sufficient evidence that the ELG project was needed to provide adequate, efficient and reasonable service to Kentucky Power's customers, and would not create a wasteful duplication of

⁴ Case No. 2008-00436, *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.

facilities, and therefore was denied for failing to meet the legal standards established in KRS 278.020 and KRS 278.183. Because the CPCN was denied for the ELG project, Kentucky Power was not authorized to recover costs related to ELG compliance project at Mitchell in an environmental surcharge tariff. Because the ELG compliance project was needed to operate Mitchell after 2028, not granting the ELG CPCN would have the result of Kentucky Power not being permitted to operate Mitchell after 2028.

Because the WVPSC approved a CPCN for both the CCR and ELG projects, Wheeling Power is permitted to operate Mitchell through Mitchell's expected retirement date in 2040.

DISCUSSION AND FINDINGS

CCR Depreciation Rate

In its request for rehearing, Kentucky Power stated that its proposed 20 percent annual depreciation rate for the CCR compliance project at Mitchell was based on an in-service date of November 2023 and closure of Mitchell in December 2028, or a remaining life of five years. Kentucky Power noted that its existing depreciation rates for Mitchell, approved in Case No. 2017-00179, are based on balances on December 31, 2013, and an expected estimated retirement date for Mitchell of 2040.⁵ Kentucky argued that its proposed 20 percent depreciation rate was necessary to fully recover the CCR project through Mitchell's useful life to Kentucky Power.

⁵ 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).

The Attorney General/KIUC argued that the proposed depreciation rate should be denied and the presently authorized rates remain in effect, with the remaining net book value at retirement and actual decommissioning costs recovered through Kentucky Power's Decommissioning Rider.⁶ Sierra Club took no position on the CCR depreciation rates.⁷

In granting rehearing, the Commission stated that it was limited to determining the closure date of Mitchell, either 2028 or 2040, and that the closure date would guide a decision regarding the appropriate depreciation rate.

In rehearing discovery, Kentucky Power explained that its share of the CCR compliance project would total an estimated \$13 million. Kentucky Power asserted that, because the CCR compliance project would be substantially depreciated as of December 2028, that the net book value of the CCR project would be approximately \$0, and thus would not increase the total remaining net book value of Mitchell as of December 2028. If Kentucky Power was required to use the previously authorized depreciation rate, 85 percent of the \$13 million net book value of the CCR project, or \$11 million, would remain as of December 2028 for recovery from Kentucky Power customers.⁸

Based upon the case record, and with the expectation that Kentucky Power will be selling its 50 percent undivided interest in the Mitchell plant to Wheeling Power before 2029, the Commission finds that 2028 will mark the end of Kentucky Power ownership of

⁶ Attorney General/KIUC's Response to Kentucky Power's Motion for Rehearing (Attorney General/KIUC's Response) (filed Aug. 6, 2021) at 2.

⁷ Sierra Club's Response to Kentucky Power's Motion for Rehearing (Sierra Club's Response) (filed Aug. 9, 2021) at 2.

⁸ Kentucky Power's Response to Commission Staff's Second Rehearing Request for Information (Staff's Second Rehearing Request) (filed Oct. 4, 2021), Item 2(b)–(c).

Mitchell and should be deemed the actual closure date of Mitchell for Kentucky Power. As such, the Commission finds that the 20 percent depreciation rate should be approved to reflect the five-year remaining life of the CCR project. As the Commission stated in the July 15, 2021 Order, Kentucky Power provided sufficient evidence that it reviewed reasonable alternatives, and that constructing the CCR project was the most reasonable, least-cost alternative that enabled Kentucky Power to comply with the CCR rules while providing safe, adequate, and reliable service to Kentucky Power's customers. But for constructing the CCR compliance project, Mitchell would have been retired in October 2023 under the revised CCR rules, which would have resulted in a capacity shortfall that, in turn, would have caused a substantial inadequacy of service. Further, given that Kentucky Power will have to terminate its interest in Mitchell by December 31, 2028, to comply with the Commission's July 15, 2021 Order, Kentucky Power will not receive value from the CCR project after 2028. Finally, given the Commission's expectation that Kentucky Power's undivided 50 percent interest in Mitchell will be sold to Wheeling Power at approximately net book value, with adjustments to the price as necessary, it would be unreasonable for Kentucky Power to purposefully push out the recovery of costs, only to increase the net book value at the time of sale. For these reasons, the Commission concludes that the practical effect of the unique facts present in this proceeding is that 2028 should be deemed the retirement date for Mitchell. Using 2028 as the retirement date, authorizing a 20 percent depreciation rate for the CCR project approved in this proceeding will allow for full recovery of the CCR project's costs. However, should Wheeling Power or the WVPSC determine that Wheeling Power will not purchase Kentucky Power's interest in the Mitchell Plant at approximately net book value, with

reasonable adjustments, the Commission finds the depreciation rate of the CCR project should be amended accordingly.

In approving the 20 percent depreciation rate, we also approve amendments to Kentucky Power's Tariff Environmental Surcharge (Tariff E.S.) and monthly filing formats. Tariff E.S. provides Kentucky Power with a method of recovering the cost of certain approved environmental projects through a customer environmental surcharge in accordance with KRS 278.183. In the event that the total monthly environmental costs to Kentucky Power exceed those already recovered in base rates, then customers are charged the difference through the environmental surcharge.

Based on the above, the Commission finds that Kentucky Power's Tariff E.S. and monthly filing formats should be updated to include the 20 percent depreciation rate for the Mitchell CCR project approved in the July 15, 2021 Order.

ELG Costs Incurred Prior to July 15, 2021

In its request for rehearing, Kentucky Power argued that it was allocated approximately \$1.903 million for Mitchell ELG compliance project costs incurred prior to the July 15, 2021 Order. Kentucky Power further argued that the costs were prudently incurred in conjunction with preliminary planning for the ELG compliance project, and thus Kentucky Power should be approved to recover the costs.

The Attorney General/KIUC deferred to the Commission's discretion regarding the \$1.903 million ELG costs incurred prior to July 15, 2021.⁹ Sierra Club argued that Kentucky Power provided scant information regarding ELG compliance costs, and thus Kentucky Power's request should be denied because Kentucky Power failed to meet its

⁹ Attorney General/KIUC's Response at 3.

burden of proof. Sierra Club further argued that the ELG compliance costs should be the responsibility of shareholders, not ratepayers.¹⁰

In granting rehearing, the Commission stated that Kentucky Power never explained how it calculated \$1.903 million in ELG expenses incurred prior to July 15, 2021 and no discovery was conducted on the ELG expenses. The Commission granted rehearing to obtain a breakdown of the expenses.

The Commission notes that Kentucky Power requested to recover expenses incurred in preliminary pre-construction activities conducted in evaluating reasonable alternatives for complying with environmental laws and for which Kentucky Power requested, but was denied, a CPCN. Thus, the Commission's review involves whether the costs were prudently incurred. Granting rehearing on this discrete issue is not inconsistent with the Commission's finding in the July 15, 2021 Order that Kentucky Power failed to meet its burden of proof that constructing the ELG project would not result in wasteful duplication, or that the ELG project, as a whole, was reasonable and cost-effective. Because the pre-construction evaluation was necessary to the determination of whether to pursue a CPCN, the Commission will review the prudence of such pre-construction evaluation costs in this case.

In rehearing discovery, Kentucky Power provided spreadsheets with Mitchell ELG project costs incurred through June 2021 in FERC Account 107 totaling \$1,446,998.35 that Kentucky Power requested to recover in a regulatory asset.¹¹ The categories of expense included construction overhead, allowance for funds used during construction

¹⁰ Sierra Club's Response at 3.

¹¹ Kentucky Power's Supplemental Response to Commission Staff's Second Rehearing Request (filed Oct. 15, 2021), Item 1.

debt and equity, labor costs, professional services, legal services, fleet clearing, and taxes. The Commission takes administrative notice that in Case No. 2021-00421, Kentucky Power provided a spreadsheet indicating that, of the \$1,446,998.35 total, \$1,438,713.23 was to evaluate Mitchell bottom ash pond CCR compliance and \$8,285.12 was for the Mitchell FGD wastewater treatment.¹²

As the Commission has noted recently, the Commission expects jurisdictional utility seeking a CPCN to present to the Commission the engineering plans and specifications for those projects and to base its costs of construction and costs of operation estimates on data pertaining to the project it intends to construct.¹³ In order to provide the necessary information to consider a CPCN, Kentucky Power was required to perform certain preconstruction activities. Based upon a review of the case record, the Commission finds that the Mitchell ELG project costs incurred through June 2021 in FERC Account 107 totaling \$1,446,998.35 were prudently incurred preconstruction activities appropriate for the pursuit of a CPCN.

Regulatory Asset for ELG Costs

In its request for rehearing, Kentucky Power argued that the ELG costs represented extraordinary, nonrecurring expenses that could not have been anticipated or included in Kentucky Power's planning, as well as expenses resulting from statutory and administrative directives, and thus are eligible for approval as regulatory asset.

¹² Case No. 2021-00421, *Electronic Application of Kentucky Power Company for Approval of Affiliate Agreements Related to the Mitchell Generating Station* (filed Nov. 19, 2021), Kentucky Power's Response to Commission Staff's First Request for Information (filed Dec. 22, 2021), Item 16.

¹³ Case No. 2021-00183, *Electronic Application of Columbia Gas of Kentucky, Inc. for an Adjustment of Rates; Approval of Depreciation Study; Approval of Tariff Revisions; Issuance of a Certificate of Public Convenience and Necessity; and Other Relief* (Ky. PSC Dec. 28, 2021).

The Attorney General/KIUC deferred to the Commission's discretion whether a regulatory asset should be approved for the \$1.903 million ELG costs incurred prior to July 15, 2021.¹⁴ Sierra Club was opposed to any recovery of the \$1.903 million in ELG costs and therefore opposed the regulatory asset.¹⁵

In granting rehearing, the Commission stated that Kentucky Power never provided a basis to include the sum in a regulatory asset. The Commission granted rehearing to determine, if the \$1.903 million ELG costs are deemed prudently incurred, whether a regulatory asset is warranted and the appropriate carrying charge.

In rehearing discovery, Kentucky Power explained that the statutory or administrative directive that required Kentucky Power to incur ELG related expenses in 40 CFR Part 423, which contains a large number of regulations related to discharges from fossil fuel-fired electric generating facilities.¹⁶ Kentucky Power argued that the ELG project expenses were extraordinary and nonrecurring expenses that could not have been anticipated or included in Kentucky Power's planning due to the short period between when the revised ELG regulations were finalized in August 2020 and the October 13, 2021 date for notifying state permitting agencies of an intent to terminate coal fired operations.¹⁷ Kentucky Power further argued that the ELG project expenses were unavoidable because they were incurred in developing and evaluating ELG compliance options, including project initiation, technology feasibility studies, evaluation of risk

¹⁴ Attorney General/KIUC's Response at 3.

¹⁵ Sierra Club's Response at 3.

¹⁶ Kentucky Power Response to Staff's Second Rehearing Request, Item 2(a).

¹⁷ Kentucky Power Response to Staff's Second Rehearing Request, Item 2(b).

balanced technical options, conceptual engineering, permitting, and site investigations.¹⁸ Kentucky Power maintained that the ELG project expenditures were financed through a combination of debt and equity, and therefore a carrying charge at the weighted average cost of capital (WACC) was appropriate.¹⁹ Kentucky Power stated that it would not be charged and would not pay any costs related to the Mitchell ELG project costs incurred after July 15, 2021.

Based upon the case record and the Commission's finding that ELG project costs totaling \$1,446,998.35 were prudently incurred in pursuit of a CPCN, the Commission finds that Kentucky Power's request to establish a regulatory asset is approved. The costs represent extraordinary, nonrecurring expenses that could not have been anticipated or included in Kentucky Power's planning. However, the Commission finds that the regulatory asset should be amortized and recovered through Kentucky Power's Tariff E.S. over two years. Tariff E.S. is an appropriate mechanism for recovery because the costs were incurred to comply with environmental regulations, as Kentucky Power was required to evaluate ELG compliance. Based on the above, the Commission finds that Kentucky Power's Tariff E.S. and monthly filing formats should be updated to include the amortization of the ELG regulatory asset. As such, no carrying charge on the regulatory asset is appropriate.

IT IS THEREFORE ORDERED that:

1. Kentucky Power is authorized to use a 20 percent depreciation rate for the Mitchell CCR compliance project approved in the July 15, 2021 Order.

¹⁸ Kentucky Power Response to Staff's Second Rehearing Request, Item 2(b).

¹⁹ Kentucky Power Response to Staff's Second Rehearing Request, Item 2(b).

2. Kentucky Power is authorized to establish and amortize a regulatory asset for Mitchell ELG compliance costs incurred prior to July 15, 2021.

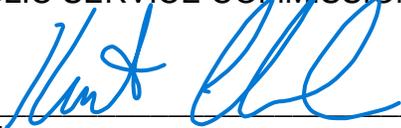
3. Kentucky Power's environmental surcharge tariff and monthly filing formats shall be modified to include a 20 percent depreciation rate for the Mitchell CCR project and the two-year recovery of the ELG regulatory asset.

4. Within 20 days of the date of this Order, Kentucky Power shall file with the Commission, using the Commission's electronic Tariff Filing System, its revised Tariff E.S. as set forth in this Order reflecting that it was approved pursuant to this Order.

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

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PUBLIC SERVICE COMMISSION



Chairman

Vice Chairman

Commissioner



ATTEST:



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