COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

APPLICATION OF BIG RIVERS ELECTRIC CORPORATION FOR AN ADJUSTMENT OF RATES	)))	CASE NO. 2012-00535

ORDER

On January 15, 2013, Big Rivers Electric Corporation ("Big Rivers") tendered an application requesting approval to increase its wholesale electric rates for service to its three member-owner distribution cooperatives, Jackson Purchase Energy Cooperative ("JPEC"), Kenergy Corp. ("Kenergy"), and Meade County Rural Electric Cooperative Corporation ("Meade County"). Big Rivers proposed to increase its wholesale electric base rates by $74.5 million,[1] or 21.4 percent, effective February 18, 2013, based on a forecasted test year covering the period from September 2013 through August 2014. The Commission found that an investigation would be necessary to determine the reasonableness of Big Rivers' proposed rates and suspended them for six months, up to and including August 17, 2013, pursuant to KRS 278.190(2).[2]

[1] Recognizing the additional revenue awarded in the rehearing order in Case No. 2011-00036, Application of Big Rivers Electric Corporation for a General Adjustment in Rates (Ky. PSC Feb. 21, 2013) along with the correction of errors in its application, in its February 28, 2013 response to Item 36 of Commission Staff's Second Request for Information, Big Rivers lowered its calculated revenue deficiency to $73.0 million. Recognizing the elimination of the interest expense on pollution control bonds it chose not to refinance, as approved in Case No. 2012-00492, Application of Big Rivers Electric Corporation for Approval to Issue Evidences of Indebtedness (Ky. PSC Mar. 26, 2013), in its June 24, 2013 rebuttal testimony, Big Rivers lowered its calculated revenue deficiency further to $68.6 million.

[2] *See* Commission Order entered Feb. 1, 2013.

Intervening in this proceeding are the Attorney General of the Commonwealth of Kentucky, by and through his Office of Rate Intervention ("AG"), Kentucky Industrial Utility Customers, Inc. ("KIUC"), Ben Taylor and the Sierra Club ("Sierra Club"), JPEC, Kenergy, and Meade County.[3] The Commission established a procedural schedule that provided for discovery, intervenor testimony, and rebuttal testimony. The AG, KIUC and Sierra Club put forward data requests to Big Rivers, as did Commission Staff. The AG, KIUC and the Sierra Club all filed testimony. Public meetings were held in the cities of Henderson, Owensboro and Brandenburg on June 13, 2013, and in Paducah on June 18, 2013, to allow members of the public to comment on the proposed rate increase.

The Commission held an evidentiary hearing on the proposed rate adjustment on July 1, 2, and 3, 2013, at its offices in Frankfort, Kentucky. Post-hearing briefs were filed by Big Rivers, the AG, KIUC, and Sierra Club. All information requested at the hearing has been filed and the case now stands submitted for a decision. As discussed more thoroughly throughout this Order, the Commission is granting Big Rivers a base rate increase of $54,227,241, or 15.5 percent, which is roughly 73 percent of the amount of its original request.[4]

BACKGROUND

Big Rivers is a member-owned rural electric generation and transmission cooperative organized pursuant to KRS Chapter 279. Its three member-owners sell electricity to approximately 112,000 retail customers in 26 western Kentucky counties.

[3] Rio Tinto-Alcan ("Alcan") had initially intervened but subsequently withdrew from the case.

[4] On August 19, 2013, pursuant to KRS 278.190(2), Big Rivers notified the Commission of its intent to put its proposed rates into effect for service rendered on and after August 20, 2013. Our Order of August 20, 2013 acknowledged Big Rivers' compliance with the statutory provisions for placing its rates into effect and required that it maintain its records so that amounts to be refunded could be determined in the event refunds were ultimately required in this proceeding.

In July 2009, Big Rivers consummated what is referred to as the "Unwind Transaction" under which it terminated a long-term lease of its generation.[5] In conjunction with the Unwind Transaction, Big Rivers negotiated new power agreements with the aluminum smelters served by Kenergy, Alcan, and Century Aluminum of Kentucky General Partnership ("Century"), ultimately entering into new agreements ("Smelter Agreements") with them. Those agreements set out the terms of service to the smelters and the rates and charges negotiated in conjunction with the Unwind Transaction. A provision of each Smelter Agreement allowed the smelter to terminate the agreement upon providing Big Rivers a one-year notice of termination.

On August 20, 2012, Century provided Big Rivers its one-year termination notice. Since 2009, Century has represented roughly 40 percent of Big Rivers' native load sales and has accounted for approximately 35 percent of Big Rivers' annual revenue. Century's announced termination was the primary driver behind Big Rivers' decision to file the application which is the subject of this proceeding.[6]

With the Century termination, the demand on Big Rivers' system would decline by approximately 482 MW, which is roughly 10 percent greater than the combined capability of the three generating units which make up Big Rivers' Coleman Generating

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[5] The Commission approved the Unwind Transaction in Case No. 2007-00455, 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 (Ky. PSC Mar. 6, 2009) (the "Unwind proceeding").

[6] On January 31, 2013, Alcan provided its one-year notice of termination, which is the primary driver of Big Rivers' more recent application for a base rate increase, which has been docketed as Case No. 2013-00199, Application of Big Rivers Electric Corporation for a General Adjustment of Rates Supported by a Fully Forecasted Test Period, and is presently pending before the Commission (filed June 28, 2013). On June 5, 2013 Alcan submitted a motion to withdraw as an intervenor in this case in which it informed the Commission that, as of May 31, 2013, it had consummated an Asset Sale Agreement with Century under which Century purchased the assets that comprise the entirety of the Sebree, Kentucky, smelter formerly owned and operated by Alcan.

Station. Given that it is located near the Century smelter and that its generating costs are among the highest on the Big Rivers system, Big Rivers initially determined that it would idle the Coleman Station as a means of reducing its operating costs in response to the Century termination.

Before it could make a final decision on idling the Coleman Station, Big Rivers, as a member of the Midcontinent Independent System Operator, Inc. ("MISO"), was required to seek a decision from MISO on whether the Coleman Station could be idled, or whether its operation would be required to ensure the reliability of the regional transmission system that is under MISO's functional control. While awaiting MISO's decision, Big Rivers filed the rate application which is the subject of this proceeding. Based on its understanding, when it filed its application, of prior MISO decisions requiring specific generating facilities to be considered "must-run" and designated as System Support Resource ("SSR"), Big Rivers filed its application to reflect the idling of the Wilson Station rather than the Coleman Station.

Based on information it received from MISO concerning the impact of a generating station is being designated an SSR, in June 24, 2013 rebuttal testimony, Big Rivers filed additional information in this case to reflect the continued operation of the Wilson Station and the "effective" idling of the Coleman Station instead.[7] Days later, Big Rivers filed a second application for an adjustment of base rates which, among other things, reflected its plan to idle the Wilson Station effective February 1, 2014, concurrent with the termination of its service to the Alcan smelter located in Sebree, Kentucky.[8]

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[7] The implications of this change and the "effective" idling of the Coleman Station are discussed in greater detail later in this Order.

[8] Case No. 2013-00199 (Ky. PSC June 28, 2013).

TEST PERIOD

Big Rivers proposed the 12 months ending August 31, 2014 as its forecasted test period to determine the reasonableness of its proposed rates. None of the intervenors offered objections to the proposed test period or suggested an alternative test period. However, the AG criticized how Big Rivers developed certain projected revenues and expenses and claimed that Big Rivers' internal processes and financial model were not sufficiently transparent or documented to permit a thorough analysis thereof. The AG argued that Big Rivers did not adequately respond to certain data requests propounded by the AG that were intended to elicit information that would have permitted a more thorough and in-depth review of Big Rivers' internal processes and financial model.[9]

KIUC claimed that, as Big Rivers' test period did not reflect the effects of Alcan's termination of its Smelter Agreement, to become effective in January of 2014, the test period was incomplete and inaccurate.[10] KIUC argued that Big Rivers also did not properly update its proposed test period for other post-application events and change of circumstances.

On rebuttal, Big Rivers stated that it developed the revenues and expenses included in its forecasted test period based on its sound budgeting process, and that its forecast was supported by a significant amount of data and is reasonable.[11] Big Rivers explained that it provided all relevant historical data that it had reasonably available and provided all available forecast data regarding the Century termination.[12] It also

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[9] Direct Testimony of Bion C. Ostrander ("Ostrander Testimony") at 16-19.

[10] Direct Testimony and Exhibits of Lane Kollen ("Kollen Testimony") at 44-49.

[11] Rebuttal Testimony of Deanna M. Speed ("Speed Rebuttal") at 18-19.

[12] *Id.*, at 19.

explained why certain payroll data was not available for 2009 and prior years and that the administrative regulation governing forecasted rate applications did not permit the type of updates to its forecast that the intervenors argued it should have made.[13]

Big Rivers stated that its load forecast process is rigorous and that it utilizes the expertise of GDS Associates, a firm which performs similar analyses for a number of electric utilities throughout the country.[14] Big Rivers asserted that, due to the timing of this case, the Alcan termination, and the likely timing of a Commission decision in Case No. 2013-00199, the impacts of that termination and other changes that occurred subsequent to filing its application in this case should be addressed in that proceeding rather than in this proceeding.[15]

The Commission finds Big Rivers' use of the proposed forecasted test period to be reasonable. The intervenors have had the opportunity to conduct discovery for the purpose of analyzing the proposed test period and the components contained therein. Big Rivers' rebuttal testimony adequately described its internal processes and financial model. Big Rivers also provided reasonable explanations for why it was unable to respond to certain of the AG's data requests. Given the timing of its more recent rate application, Case No. 2013-00199, the Commission finds reasonable the explanation provided by Big Rivers for why it did not update the test period in this case to recognize the Alcan termination and other changes that occurred subsequent to when its pending application was filed.

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[13] Response to AG 1-76 and Rebuttal Testimony of James V. Haner ("Haner Rebuttal") at 5.

[14] Rebuttal Testimony of Lindsay Barron at 7.

[15] Rebuttal Testimony of John Wolfram ("Wolfram Rebuttal") at 4-5.

VALUATION

Rate Base

Big Rivers proposed a net investment rate base of $1,218,570,396[16] based on the test-year-average value of plant in service and construction work in progress; the 13-month average balances for fuel stock, materials and supplies, and prepayments; plus a cash working capital allowance, minus the adjusted accumulated depreciation balance. Although the AG, KIUC, and Sierra Club asserted that there would be unneeded generating capacity on Big Rivers' system after the smelter terminations become effective, none of the intervenors specifically addressed Big Rivers' proposed rate base. To the extent that Big Rivers has unneeded generating capacity due to the Century termination, the Commission intends to recognize that by excluding from the revenue requirement established for Big Rivers in this Order the depreciation expense associated with the cost of the investment in said generation, as discussed later in this Order.

The Commission concurs with Big Rivers' proposed rate base with the exception that working capital has been adjusted to reflect the pro forma expense adjustments found reasonable herein. Based on this adjustment to working capital, Big Rivers' net investment rate base which the Commission finds reasonable for rate-making purposes is as follows:

Utility Plant in Service	$ 2,061,811,395
Construction Work In Progress	74,889,729
Total Utility Plant	$ 2,136,701,124
ADD:	
Fuel Stock	$ 33,565,933

[16] Big Rivers' Application, Volume 4, Tab 48.

Materials and Supplies	27,023,114
Prepayments	2,308,635
Working Capital	25,407,210
Subtotal	$ 88,304,892
DEDUCT:	
Accumulated Depreciation	$ 1,006,671,142
NET INVESTMENT RATE BASE	$ 1,218,334,874

Capitalization and Capital Structure

Big Rivers' test-year-average capitalization is $1,354,598,637[17] and consists of $404,125,400 in equity and margins and $950,473,237 in long-term debt. Using this capital structure, Big River's equity to total capitalization ratio is 29.8 percent. None of the intervenors addressed Big Rivers' proposed capitalization. The Commission finds Big Rivers' test-year-end capitalization to be reasonable for ratemaking purposes.

REVENUES AND EXPENSES

Big Rivers' operating statement for the forecasted test period is based on its internal budgets for calendar years 2013 and 2014. As required by 807 KAR 5:001, Section 10(8)(a), the forecasted test period was presented by Big Rivers in the form of pro forma adjustments to its base period, the 12 months ending April 30, 2013 .[18] In its application, Big Rivers stated that $63 million of its requested $74.5 million increase was due to recognizing the loss of the Century load. Based on that loss and other assumptions factored into its budgets, Big Rivers calculated its test period operating revenues and operating and maintenance ("O&M") expenses, amended in its June 24,

[17] *Id.*, Volume 1, Tab 23.

[18] *Id.*, Tab 20.

2013 rebuttal testimony, to be $409,058,933 and $431,129,682, respectively.[19] It proposed adjustments to these amounts for the following purposes: (1) eliminating, for ratemaking purposes, revenues and expenses which are addressed in non-base rate mechanisms; (2) eliminating various dues, lobbying and advertising expenses which are not typically allowed for ratemaking purposes; (3) removing non-recurring expenses; and (4) normalizing certain expenses. With these adjustments, Big Rivers' revenues were reduced $50,465,271, to $358,593,662 while its O&M expenses were reduced $53,452,087, to $377,677,595.[20]

Based on the adjusted revenues and O&M expenses stated above, Big Rivers' test period operating margins are ($19,083,933). To this amount it added projected interest income of $1,717,360 and projected capital credits and patronage dividends of $2,706,448, and subtracted its projected interest on long-term debt of $43,511,699. The net result of these additions and subtraction is adjusted net margins of ($58,171,824). Based on its adjusted level of interest on long-term debt and a proposed Times Interest Earned Ratio ("TIER") of 1.24, Big Rivers' revised requested increase is $68,614,632.[21]

Implications of Century Termination

In response to the Century termination notice, Big Rivers developed a mitigation plan in which it established parameters and specific actions it planned to undertake to mitigate the financial impacts of no longer supplying the power required to serve the

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[19] Wolfram Rebuttal, Exhibit Wolfram-2.3 revised.

[20] *Id.*

[21] Wolfram Rebuttal at 24.

Century load. One specific action included in Big Rivers' mitigation plan was to idle, or shut down, generating facilities. Closing the Century smelter would dictate that Big Rivers idle its Coleman Generating Station, as that station is located in close proximity to the smelter.

There were issues other than the proximity of the Coleman Station to the Century smelter, however, for Big Rivers to consider. Prior to filing its rate application in this matter, Big Rivers began negotiations with Century concerning potential means by which the Century smelter could remain open in conjunction with its being able, through Kenergy and Big Rivers, to acquire electricity at market-based prices. Another factor for Big Rivers to consider was whether MISO, the Regional Transmission Organization in which it is a member, would require the Coleman Station to be operated in a "must-run" capacity for reasons related to the reliability of the transmission grid within the MISO footprint.

Based on these considerations, which were mere possibilities when it prepared its application, Big Rivers assumed that MISO would require that the Coleman Station operate in a "must-run" capacity and would designate the station an SSR. Therefore, Big Rivers filed its application based on idling the Wilson Station, rather than idling the Coleman Station. During this proceeding, a number of events occurred which directly impacted the future operation of Big Rivers' generating facilities and its treatment of those facilities in this case. First, Big Rivers, Century, and Kenergy negotiated agreements under which the Century smelter will continue to operate, with Kenergy

providing power from a supplier other than Big Rivers.[22] Second, Big Rivers requested and received a decision from MISO concerning the status of the Coleman Station with the Century smelter continuing to operate, as well as a more informed understanding of its responsibilities and obligations during the period the station will operate in a "must-run" capacity. Third, based on the first and second events, Big Rivers revised its position when it filed its rebuttal testimony to recognize the effect of idling the Coleman Station, from the perspective of its generation portfolio, rather than idling the Wilson Station.

POSITIONS OF THE INTERVENORS

The approach taken by the intervenors in their direct testimony to not address specific issues concerning Big Rivers' forecasted revenues and expenses and revenue requirement does not lend itself to an issue-by-issue discussion of the parties' positions and recommendations, as is typical in Commission rate orders.[23] Therefore, in some instances this portion of the order will discuss each intervenor's positions and the related recommendations, followed by Big Rivers' rebuttal to the intervenors and then the Commission's analyses and findings on the opposing positions. In other instances in which the intervenor testimony lends itself to an issue-by-issue discussion, that is the approach that will be taken.

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[22] Those agreements were filed with the Commission and approved in Case No. 2013-00221, Joint Application of Kenergy Corp. and Big Rivers Electric Corporation for Approval of Contracts and a Declaratory Order (Ky. PSC Aug. 14, 2013).

[23] It is noted that the AG did address several specific issues in his testimony related to Big Rivers' revenue requirement and that KIUC also addressed a few specific revenue requirement issues in its testimony. It is likewise noted that Sierra Club did not address any specific items related to Big Rivers' forecasted revenues and expenses or its forecasted revenue requirement.

ISSUES FACING BIG RIVERS AND CURRENT FINANCIAL CONDITION

Sierra Club

In its direct testimony, Sierra Club recommended that Big Rivers' requested rate increase be rejected, citing several reasons in support of its recommendation. Those reasons include: (1) the amount of generating capacity, and the costs related thereto, which is in excess of what is needed to meet the needs of the customers on Big Rivers' system in the future; (2) the potential costs of bringing Big Rivers' generating fleet into compliance with stricter environmental standards; (3) subsidizing the aluminum smelters to save jobs should be the responsibility of the Commonwealth of Kentucky, not the ratepayers of Big Rivers' member owners; (4) Big Rivers has not adequately pursued the potential sale or decommissioning of some if its generating facilities as a means of mitigating the loss of load it faces; (5) Big Rivers' requested rate increase will not solve its financial problems; and (6) the possibility of bankruptcy should be considered by Big Rivers as an alternative, along with all other alternatives, to rate increases of the size needed to offset the loss of revenues historically provided by the smelters.[24]

The Sierra Club cites these same reasons in its post-hearing brief. It also cites changes that occurred after this case was initiated and argues that Big Rivers' rate request is premised on a long-term strategy that has little hope of succeeding.[25] Sierra Club states in its post-hearing brief that the Commission should provide Big Rivers with only temporary and limited rate relief that is sufficient to ensure Big Rivers' fiscal viability through the next rate proceeding. It also recommends that the Commission urge Big

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[24] Direct Testimony of Frank Ackerman at 3-4.

[25] Sierra Club post-hearing brief at 8.

Rivers to work in advance of the next rate hearing with its creditors, the parties to this case, and other interested stakeholders to reach a solution to its present fiscal problems that is just and reasonable for all involved.[26]

KIUC

In its direct testimony, KIUC addressed few specific components contained in Big Rivers' rate request. It cited many of the same issues raised by Sierra Club in arguing against the proposed increase. It argued that Big Rivers should open negotiations with its creditors to receive more favorable loan terms before receiving an increase in rates. Unlike Sierra Club, KIUC offered a recommendation for an alternative rate increase to that proposed by Big Rivers.[27] Based on the amount it identified as excess generating capacity after the loss of both the Century and Alcan loads, KIUC proposed that the costs related to that capacity be shared by customers on the Big Rivers system and by Big Rivers' creditors. Claiming that Big Rivers' creditors were aware of the risk of the potential loss of the smelter loads at the time of the Unwind Transaction and, more recently, when they negotiated the terms of new loans with Big Rivers in mid-2012, KIUC contends that those creditors should bear a portion of the costs previously borne by the smelters.[28] Recognizing the level of sales to non-smelter customers prior to the smelters' terminations as a percentage of Big Rivers' total sales, KIUC calculated 31.3 percent as the portion of excess capacity-related costs that should be borne by those non-smelter customers. KIUC recommended that the other 68.7 percent of those costs be borne by Big Rivers' creditors, meaning they would not be included in the calculation

[26] *Id.*, at 9.

[27] Kollen Testimony at 56-61.

[28] *Id.*, at 34-36.

of Big Rivers' revenue requirement.[29] Based on these percentages, KIUC claimed that Big Rivers' revenue requirement should be reduced by $43.3 million to reflect its recommended treatment of the costs of Big Rivers' excess capacity.[30]

In its post-hearing brief, KIUC modified its proposal to reflect only the loss of the Century load from Big Rivers' system. Based on Century's share of the internal load on the Big Rivers system, it recommended that 40 percent of the costs related to excess capacity be removed from the determination of Big Rivers' revenue requirement.[31] The impact of this removal would reduce Big Rivers' proposed increase by $14.5 million.

AG

The AG addressed Big Rivers' rate request increase in two ways. First, citing reasons similar to those cited by both Sierra Club and KIUC, he recommended that Big Rivers be granted none of the $63 million increase related to the excess capacity he claimed would exist after Big Rivers lost the smelter loads.[32] Based on Big Rivers' application, the AG claimed the Wilson Station was not "used and useful" and that ratepayers should not be burdened with the costs of such a facility.[33] Second, the AG recommended several adjustments to Big Rivers' forecasted test year, which in total would reduce Big Rivers' proposed revenue increase by $9,020,129. The AG's overall

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[29] *Id.*, at 58-59.

[30] *Id.*, at 60.

[31] KIUC post-hearing brief at 5.

[32] Direct Testimony of David Brevits ("Brevits Testimony") at 33.

[33] *Id.*, at 36.

recommendation, which mirrored that of Sierra Club, was that Big Rivers should receive no increase in rates.[34]

To some extent, the AG, as well as Sierra Club and KIUC, all advocate that Big Rivers negotiate concessions from its lenders before seeking future rate relief. KIUC and the AG cite the Commission's order in Case No. 9613[35] as support for the argument that remaining ratepayers should not be made to bear the cost of the excess capacity that will exist on Big Rivers' system after the loss of the smelter loads.[36] All three of these intervenors argue that the remaining ratepayers are not responsible for excess generating capacity resulting from the smelter terminations and, therefore, should not be required to pay for it.

Big Rivers' Rebuttal

Big Rivers' argued that adoption of the intervenors' recommendations regarding its surplus generating capacity would leave it with insufficient revenues to meet its service obligations to its members and its payment obligations to its creditors. It stated that denial of its requested rate increase would likely trigger a sequence of events that would force it to cease operations or seek bankruptcy protection.[37]

Big Rivers claimed that the intervenors' positions ignore the serious service and financial obligations and credit issues it must manage in a time-sensitive manner.[38] It

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[34] Ostrander Testimony at 6.

[35] Case No. 9613, In the Matter of Big Rivers Electric Corporation's Notice of Changes in Rates and Tariffs for Wholesale Electric Service and of a Financial Workout Plan (Ky. PSC Mar. 17, 1987).

[36] Kollen Testimony at 6-7 and 18-21. Brevits Testimony at 46-47.

[37] Rebuttal Testimony of Mark A. Bailey ("Bailey Rebuttal") at 5.

[38] Rebuttal Testimony of Billie J. Richert ("Richert Rebuttal") at 12.

stated that it should be given time to execute its mitigation plan, but that it would not have such time if the Commission were to adopt the intervenors' recommendations to deny or severely limit the recovery of the costs of facilities previously devoted to serving the smelters.[39]

Big Rivers stated that if it were forced to pursue bankruptcy, its lenders would likely view a filing under Chapter 11 of the bankruptcy code as a hostile action.[40] It also stated that only after developing a plan to maximize revenues, minimize expenses, and adjust its operations and asset utilization to fit the short- and long-term goals of that plan would it "have sufficient credibility to rationally negotiate with its lenders."[41]

Commission Findings

After extensive review of the positions and arguments of Big Rivers, the AG, Sierra Club, and KIUC, the Commission finds that Century's decision to terminate its contract for the purchase of power supplied by Big Rivers results in Big Rivers' having a significant reserve margin which is much higher than optimal.[42] However, this excess capacity is not the result of improper planning or unneeded construction by Big Rivers. To the contrary, in 1998, Big Rivers entered into a 25-year lease of all of its generating facilities and it agreed to a 25-year purchase of limited quantities of power to meet the needs of its three distribution cooperatives and their retail customers, excluding the smelters. Also in 1998, Century and Alcan agreed to forgo any right or entitlement to

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[39] Bailey Rebuttal at 5.

[40] Rebuttal Testimony of William K. Snyder, CTP, at 6.

[41] *Id.*

[42] While the intervenors' arguments reflected the terminations of both the Century and Alcan smelters, as stated in the TEST PERIOD section earlier in this Order, the Commission's consideration in this proceeding reflects its acceptance of Big Rivers' test year without adjustments related to the Alcan termination.

power on a cost-of-service basis from Big Rivers' generating facilities. Rather, Century and Alcan agreed to purchase some power from the lessee of Big Rivers' generation facilities and the remainder from the market, with the market power purchases increasing to 100 percent by 2011.

However, by 2007, Century and Alcan asserted that they could no longer remain in business under their 1998 agreements providing for electric power to be supplied at market-based prices. By 2007, market-based power prices were expected to continue to be higher than what would be cost-of-service prices utilizing Big Rivers' generating facilities. Thus, today's excess generating capacity is a direct result of Big Rivers' 2007 request to enter into the Unwind Transaction. That transaction consisted of terminating the 25-year lease of Big Rivers' generating facilities so it could reacquire those facilities and resume using them to supply electricity to Century and Alcan at cost-of-service-based rates in an effort to avoid the potential of an economic disaster for western Kentucky if Century and Alcan were to close due to high market-based power prices.

The Unwind Transaction, which was consummated in July 2009, was fully supported by Century and Alcan, and was not opposed by KIUC, which was an intervenor in that case.[43] Although the AG did oppose the Unwind Transaction as presented to the Commission, no appeal was filed in response to the Commission's Order approving the transaction. The potential risks to Big Rivers and its ratepayers of terminating the then-existing generating facilities lease and of having Big Rivers reacquire all of its generating facilities were explored in detail in Case No. 2007-00455.

[43] The industrial customers participating as part of KIUC in this case are the same ones that participated in the Unwind case and they are now represented by the same counsel that represented them and both smelters in the Unwind case.

Based on that evidentiary record, the Commission determined that approving the Unwind Transaction would result in significant benefits to Big Rivers, the smelters, and all other ratepayers, as well as the economy of western Kentucky. Enabling the smelters to resume buying power from Big Rivers at cost-based rates, which were then below market prices, was expected to "enable [the smelters] to maintain their current competitive positions and continue in operation over the long term."[44]

Big Rivers' power was for some years priced below market prices, and the Unwind Transaction did enable the smelters to continue in business and operate with power supplied by Big Rivers until 2013. However, neither Big Rivers, the smelters, KIUC, nor the Commission was able to anticipate in 2009 that the economic recession that had started in 2008 would not now be behind us, that worldwide aluminum prices would still be depressed, or that vast quantities of shale gas would now be sold at prices that allow market power to be priced lower than Big Rivers' rates under the Smelter Agreements.

In approving the Unwind Transaction, efforts were taken to mitigate the potential risks of the smelters' closing. The Smelter Agreements required one year's advance notice before either smelter could close. Big Rivers constructed an additional transmission line to increase its power export capability in the event that one, or both, of the smelters did terminate their respective power agreement. In addition, Big Rivers planned to sell any excess capacity on the market to make up for lost sales due to the closing of one or both smelters. Despite all of these efforts, Big Rivers now has excess capacity and it is proposing to idle the Coleman Station for a number of years until

[44] Case No. 2007-00455, Order dated Mar. 6, 2009, at 15.

reopening the facility is justified by new or increased system load or higher market prices for power.

Under the circumstances presented in this case, the Commission finds that in setting rates, we must balance the interests of both the utility and its ratepayers. In performing this duty, the Commission acknowledges that this excess generating capacity is not a result of any imprudent decisions by Big Rivers,[45] but is a direct result of Big Rivers' actions to reacquire its generating facilities in an effort to keep the smelters operating in western Kentucky. We also acknowledge that Big Rivers is a cooperatively organized utility. Unlike an investor-owned utility which has equity capital supplied by shareholders who choose to invest in the enterprise, a cooperative utility is owned by its members, who are its customers. In addition, Big Rivers' facilities are financed substantially with debt. Absent sufficient revenue to pay the interest on that debt, Big Rivers will be in default on its financial obligations and this could lead to bankruptcy.

Having considered all of these factors, the Commission finds it both reasonable and necessary to exclude some costs of the Coleman Station from Big Rivers' rates. It would simply not be fair to require ratepayers to pay all of costs of the excess capacity. Therefore, we will exclude the depreciation expense associated with the Coleman Station from rates at this time, as discussed more fully later in this Order. Further, we find it reasonable to afford Big Rivers the time to pursue its mitigation strategies, including operational changes to reduce costs, seeking to acquire replacement load, increasing off-system sales, and attempting to sell or lease its generating facilities. The

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[45] No party to this case alleges that the current excess capacity situation is a result of imprudent action or decision by Big Rivers.

decision we make today is not an easy one, and some of our rate-making adjustments may be viewed as atypical. But we firmly believe that today's decision fairly balances the interests of all stakeholders. Ratepayers will not be required to pay for depreciation on the Coleman Station that is currently excess capacity, and Big Rivers' will to be able to avoid a default on its debts, continue to provide safe and reliable electric service to the 112,000 customers served by its member-owners, be able to implement its mitigation plan, and possibly attract new load.

SIGNIFICANT PAYROLL COST INCREASES

The AG argued that Big Rivers awarded pay increases to some of its top officers, primarily during the period of the Unwind Transaction, that were excessive, or "significant" in the AG's words, and that such increases should not be allowed for rate making purposes. Although he claimed that these increases totaled approximately $4.4 million, the AG's recommended adjustment was limited to pay increases awarded in 2009 and 2011 and certain bonuses/incentives resulting in an overall adjustment to decrease Big Rivers' expenses by $1,444,273.[46]

Big Rivers responded to the AG's recommendation by explaining that the pay increases awarded in 2009 in connection with the Unwind Transaction recognized the increase in its organization's size upon reacquiring control of its generating facilities, which resulted in its becoming a generating and transmission cooperative rather than being solely a transmission cooperative.[47] Big Rivers also described various increases in the responsibilities of its chief executive officer ("CEO"), as well as its chief operating

[46] Ostrander Testimony at 35.

[47] Haner Rebuttal at 9.

officer ("COO") and chief financial officer ("CFO") during the time of the Unwind Transaction which contributed to the increases in management compensation cited by the AG.[48]

Big Rivers also explained how the 2011 increases cited by the AG had reflected increased responsibilities by various members of upper management and pay raises to various employees based on the structure of its compensation progression program. Finally, Big Rivers described how its bonus/incentive program is funded with savings actually achieved or increased non-member revenues, and that costs for bonuses or incentives were not included in its forecasted test period.[49]

Having considered the AG's recommendations and Big Rivers' response thereto, the Commission finds that the adjustments proposed by the AG are not adequately supported by the evidence and should be rejected. Accordingly, we will not adopt his recommended $1,444,273 decrease in Big Rivers' payroll costs.

BASE PERIOD AND TEST PERIOD PAYROLL COST INCREASES

The AG proposed to reduce Big Rivers' test period O&M expenses by removing $920,306 in payroll costs based on pay raises of 2.25 percent in both the base period and test period for non-bargaining employees. Of this amount, $470,802 represents the base-period pay increases, while $449,504 is the amount of the test-period increases. The AG stated that the base-period increases should be removed in part because past increases have been sufficient and significant, but also to reflect the need for Big Rivers

[48] Big Rivers pointed out that the 2009 CFO had retired and stated that the AG's proposed adjustments would reduce its CEO's pay to 71 percent of its current level and reduce its COO's pay to 64 percent of its current level and 11 percent less than the level at which he was hired in 2009.

[49] Haner Rebuttal at 12.

to put pay increases on hold so it "can use these funds in part to catch up on its deferred maintenance. . . ."[50] The AG claimed that the test period increases should be removed because (1) increases in a future period ending August 31, 2014 are not known and measurable, (2) it is not possible to anticipate or evaluate employee performance or cost-of-living changes this far in advance of the end of the test period, and (3) the number of employees during a future test period to which the estimated pay increases might apply is not known and measurable.[51]

In response to the AG's recommendations, Big Rivers stated that there is no basis for the AG's apparent position that because employees received pay increases in the past, they should not receive pay increases in the future.[52] It also stated that there was no connection between any pay raises that have been awarded and its deferral of maintenance on its generating units, so there is likewise no connection between future pay raises and any perceived need to catch up on deferred maintenance.[53] Big Rivers claimed, due to its use of a forecasted test period, that it could not understand the AG's argument that the test-year increase projected for January 2014 should be denied because it was not known and measurable.[54]

After reviewing the AG's arguments in support of his proposed recommendations and Big Rivers' opposing arguments, the Commission finds insufficient evidence to support the AG's position that there is a connection between any of Big Rivers' pay

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[50] Ostrander Testimony at 41.

[51] *Id.*, at 40.

[52] Haner Rebuttal at 14.

[53] Rebuttal Testimony of Robert W. Berry ("Berry Rebuttal") at 26-27.

[54] Haner Rebuttal at 14.

increases and its decisions since 2009 to defer maintenance on its generating units. Accordingly, we are unable to disallow Big Rivers' base-period or test-period pay increases on that basis. Further, with respect to the base-period pay increase, considering its magnitude of 2.25 percent and that it occurred at approximately the same time that Big Rivers filed its application in this proceeding, the Commission finds no basis for eliminating that pay increase.

While recognizing that the nature of a forecasted test period all but eliminates the use of the known and measurable standard, the Commission is concerned about the accuracy of projected pay increases for non-bargaining employees. The Commission has an even greater concern, however, about a utility's conducting "business as usual" in regard to discretionary pay raises at the same time it is requesting approval of a rate increase of the magnitude Big Rivers is seeking. Given the financial circumstances it is facing, it appears that Big Rivers is disinclined to "share the pain" with its ultimate ratepayers. While the Commission does not have the authority to direct a utility to forego pay raises, we do have the authority to deny recovery of pay raises from ratepayers. In this instance, we find it inappropriate and unreasonable for a future discretionary increase in employee compensation to be passed on to Big Rivers' distribution cooperatives for ultimate billing to retail ratepayers. Accordingly, although for reasons that differ from those offered by the AG, the Commission will accept the AG's proposed adjustment to reduce test-year operating expenses by $449,504 to eliminate Big Rivers' projected 2014 pay raises for ratemaking purposes.

WAGES AND SALARIES EXPENSED VS. CAPITALIZED

The AG recommended an adjustment to reduce Big Rivers' O&M expenses by $555,308 based on reducing the percentage of payroll costs being charged to expense to the average percent that was expensed in the three most recent historical periods.[55] The percent of payroll costs being charged to expense by Big Rivers in the test period is projected to be 99.22, while the average percent charged to expense during calendar years 2011, 2012, and the base period was 98.23.[56]

On rebuttal, Big Rivers stated that establishing the "split" between expenses and capitalized payroll costs was not appropriate without considering its current capital planning. It cited the fact that its construction budgets had declined from 2012 to 2013 and from 2013 to 2014 as support for less of its internal labor being capitalized going forward than had been the case in the past.[57]

The Commission agrees with Big Rivers that an adjustment such as that recommended by the AG is not appropriate. However, we find the intent of the adjustment recommended by the AG to be appropriate and will reflect such an adjustment, albeit one based on a somewhat different calculation. For calendar years 2011 and 2012, Big Rivers experienced variances of 0.74 percent and 0.75 percent, respectively, between the percentage of labor costs to be expensed, according to its annual budgets, and the percentage actually charged to expense.[58] While this experience is only for two years, it reflects a reasonably consistent relationship between

[55] Ostrander Testimony at 67.

[56] Exhibit BCO-2, Schedule A-7 to the Ostrander Testimony.

[57] Hanner Rebuttal at 15-16.

[58] Big Rivers' Post-Hearing Data Response, Item 12.

Big Rivers' budgets and its actual experience. Accordingly, using the average variance for the past two calendar years, the Commission has reduced Big Rivers' test-year percentage of labor costs expensed from the budgeted level of 99.22 percent to an adjusted level of 98.475 percent. Applying this percentage to Big Rivers' total test-year payroll costs of $45,768,947 results in $45,070,971 as the adjusted amount charged to expense. Compared to the amount of test-year labor costs of $45,410,144[59] charged to expense by Big Rivers, this results in an adjustment that reduces O&M expenses by $339,173.

ADJUSTMENT TO REFLECT REHEARING REVENUE IN CASE NO. 2011-00036

At the time Big Rivers filed its rate application in this case, a rehearing was still pending before the Commission in Big Rivers' prior rate case, Case No. 2011-00036. On January 29, 2013, the Commission issued an Order on rehearing, granting Big Rivers additional revenue of $1,042,535 annually. In response to Commission Staff's second request for information, Item 36, Big Rivers filed revised exhibits to reflect that additional revenue and to correct certain mathematical errors that had been made. The AG claimed that an error in the amount of $62,500 was reflected in Big Rivers' revised exhibits as filed in that information response. Based on the alleged error, the AG calculated a reduction of $1,568,516 in Big Rivers' revenue requirement, whereas the reduction contained in Big Rivers' response to the information request was $1,507,989.

In its rebuttal testimony, Big Rivers explained that there was a discrepancy in the amounts contained in two exhibits that were updated in its response to Item 36 of that information request. Correcting one of the exhibits eliminated the discrepancy and

[59] Exhibit BCO-2, Schedule A-7 to the Ostrander Testimony.

clarified that the reduction of $1,507,989 in Big Rivers' revenue requirement shown in the response was accurate.

Based on the AG's proposal and Big Rivers' response thereto, the Commission finds that the AG's adjustment should be rejected.

DEBT REFINANCING

KIUC proposed a reduction to the revenue requirement based on Big Rivers' decision not to issue $58.8 million in new pollution control bonds that had been incorporated into the forecasted test period.[60] The amount of that reduction was $4.375 million, based on the projected interest expense and associated TIER included in Big Rivers' test period.[61] Including this further reduction in its overall recommendation, KIUC's position based on its direct testimony was that Big Rivers was entitled to an increase of no more than $25.29 million.[62]

The AG proposed an adjustment similar to that of KIUC, eliminating interest expense and other costs associated with the refinancing of $58.8 million in pollution control debt reflected in the test period.[63] The AG calculated an adjustment of $4,189,083 based on Big Rivers' decision, made subsequent to filing its rate application, to not refinance that pollution control debt.[64]

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[60] Kollen Testimony at 60.

[61] *Id.*

[62] *Id.*, at 61.

[63] As stated earlier in this order, subsequent to filing its application in this proceeding, Big Rivers made the decision to not refinance its existing pollution control debt. See Case No. 2012-00492, Application of Big Rivers Electric Corporation for Approval to Issue Evidences (Ky. PSC May 26, 2013.)

[64] Ostrander Testimony at 50 and Exhibit BCO-2, Schedule A-5.

In its rebuttal testimony, Big Rivers acknowledged that an adjustment was appropriate to reflect the elimination of the interest and other costs of the new pollution debt included in the test year for debt that it decided not to issue.[65] It stated, however, that the correct amount to be eliminated was $4,353,499, which was the amount in its response to Item 13 of Commission Staff's February 14, 2013 request for information.[66] It further stated that this amount was factored into the reduction of its rate request to $68,614,632.[67]

The Commission, based on its review of the different calculations, finds that the reduction of $4,353,499 calculated by Big Rivers is the most reasonable and is the amount we will reflect in the determination of Big Rivers' revenue requirement.

RATE CASE EXPENSE

Big Rivers estimated that it would incur expenses of $1,585,977 related to the preparation of its rate application and the prosecution of its case in this proceeding.[68] Consistent with the Commission's normal ratemaking practices, Big Rivers proposed to amortize this amount over three years, resulting in an annual expense of $528,659, which is the amount incorporated into its test-year O&M expenses.

In its rebuttal testimony, based on the Commission's rehearing decision in its previous general rate case, Case No. 2011-00036, Big Rivers proposed an adjustment to amortize over three years the remaining unamortized rate case expense allowed by

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[65] Big Rivers had provided the calculation of the amount of such an adjustment in its response to Item 13 of the Commission Staff's Feb. 14, 2013 Request for Information.

[66] Wolfram Rebuttal at 21-22.

[67] *Id.*

[68] Direct Testimony of John Wolfram ("Wolfram Testimony") at 18.

the Commission for that case. Based on the amount of such expenses recovered through August 2013, the last month prior to the beginning of the test year in this case, Big Rivers had $610,056 remaining to be recovered after the effective date of the rates to be awarded in this case. Again, based on the three-year amortization period normally permitted by the Commission, Big Rivers proposed an adjustment of $203,352 to reflect and recover these remaining expenses over the three-year period beginning September 1, 2013.[69]

The AG recommended that Big Rivers' projected rate case expenses for this case be reduced by $1,027,929, resulting in a reduction of $342,643 in the amortized expense included in Big Rivers' projected test period.[70] According to the AG, the basis for his recommendation was that (1) much of the amount Big Rivers had estimated was unspent at the time of his testimony, (2) Big Rivers had not provided documentation or other verifiable evidence regarding its rate case expenses, and (3) some of the hourly rates for legal services were excessive and Big Rivers had not provided documentation to show that highly compensated legal counsel was needed for particular tasks, as required by the Commission's rehearing order in the prior rate case.[71]

On rebuttal, Big Rivers stated that the AG ignored Commission precedent in his proposal to disallow unspent legal fees associated with this rate case, noting that it has been the Commission's practice to allow recovery of reasonable rate case expenses incurred through the month of the hearing in a rate case.[72] Big Rivers claimed that its

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[69] Wolfram Rebuttal, Exhibit Wolfram-2.3, page 11, Reference Schedule 1.09.

[70] Ostrander Testimony at 52.

[71] Id., at 53.

[72] Speed Rebuttal at 16.

estimated rate case expenses were reasonable, well supported, and appropriately documented. It noted that it did not engage the international law firm of Hogan Lovells LLP in this proceeding, which lowered the overall hourly rate incurred for legal services.[73] Big Rivers also pointed out that the rehearing order to which the AG referred had not been issued at the time it filed its application in this proceeding.[74]

The Commission finds that Big Rivers has adequately documented its rate case expenses. While Big Rivers' rate case expenses tend to be greater than those of most other large electric utilities under the Commission's jurisdiction, it should be noted that Big Rivers has no in-house legal department and does not maintain the type of regulatory staff maintained by other utilities, most notably the investor-owned electric utilities jurisdictional to the Commission. It should come as no surprise that a significant portion of the rate case expenses a utility has estimated at the time it files its application will not have been spent by the time intervenor testimony is filed.[75] The Commission takes note that, as required by our rehearing order in its most recent base rate case, Case No. 2011-00036, Big Rivers provided unredacted invoices for the rate case services it receives. Contrary to the AG's arguments, Big Rivers has provided adequate support for, and documentation of, its actual rate case expenses, and it has made improvements in both areas since its last rate case.

As Big Rivers recommended in its rebuttal, the Commission will not accept the AG's proposed reduction in Big Rivers' rate case expenses. Furthermore, consistent

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[73] *Id.*, at 10.

[74] *Id.*, at 6-7.

[75] In this particular instance, the AG was citing the amount of rate case expense Big Rivers had incurred through January 2013, the month in which it filed its application.

with our typical ratemaking practice, the Commission will recognize and allow the rate case expenses incurred by Big Rivers up through and including the month of the hearing in this case. In its August 22, 2013 updated response to Item 54 of Commission Staff's initial request for information, Big Rivers reported total rate case expense of $1,634,971. This amount, which is $48,994 greater than the estimate in Big Rivers' application, will result in a three-year amortization of $544,990, which is the amount the Commission will allow for Big Rivers' rate expenses related to this case.[76]

COLEMAN STATION DEPRECIATION EXPENSE

Although it did not propose a related adjustment in its direct case, KIUC did suggest that the Commission could direct Big Rivers to cease its depreciation of the Wilson Station during the period of time it would be idled.[77] Based on the Wilson Station's utility plant balances, KIUC stated that its suggested cessation of depreciation would reduce Big Rivers' revenue requirement by $20.03 million before applying its recommended customer sharing percentage of 31.3 percent.[78] KIUC stated that if its sharing proposal were to be accepted by the Commission, the revenue requirement would be reduced by $6.27 million. At the hearing, KIUC reiterated its suggestion that depreciation could be suspended for any generating facilities that were idled.

In its rebuttal testimony, Big Rivers argued that it was now proposing to idle the Coleman Station, not the Wilson Station, that the Coleman Station was a prudent investment, and that the Coleman Station remained a used and useful asset. Big

[76] The three-year amortization of $203,352 related to the rate case expense for Big Rivers' previous rate case is also being allowed as proposed.

[77] Kollen Testimony at 63-64.

[78] *Id.*, at 64.

Rivers also claimed that ceasing to record depreciation expense would have "significant adverse effects on cash flow" which would impair its ability to make its principal debt payments.[79] Big Rivers also stated that, even in its idled status, the Coleman Station will continue to provide benefits to its members and their ratepayers.[80]

In a post-hearing data response, Big Rivers cited several sources in support of its position that it should not cease to record depreciation expense on an idled generating station. Those sources include its loan contract with Rural Utilities Service ("RUS"), the Financial Accounting Standards Board ("FASB"), the Internal Revenue Service ("IRS"), the Code of Federal Regulations as it applies to RUS borrowers, and the International Accounting Standards Board ("IASB").

In its post-hearing brief, KIUC stated that the Commission has ratemaking authority over Big Rivers and that, while they provide pronouncements on accounting practices, none of the sources cited by Big Rivers in its post-hearing data response possess similar authority. KIUC took exception to Big Rivers' reliance on the "Basis for Conclusions" issued by the IASB, citing the fact that the FASB established accounting standards (Generally Accepted Accounting Principles or "GAAP") for the United States, and that the FASB has not adopted the international standards promulgated by the IASB. KIUC expanded on its suggestion that depreciation be suspended on the plants idled by Big Rivers. In addition, KIUC proposed, as an alternative to suspending, or

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[79] Richert Rebuttal at 16.

[80] *Id.*

ceasing, depreciation on the idled plants, that the depreciation expense could be deferred and recorded in a regulatory asset account for recovery at a later time.[81]

In its post-hearing brief, Big Rivers argued that the Coleman Station continues to be used and useful, that its investment in the station was a prudent investment that was approved by the Commission, and that recovery of depreciation on the Coleman Station is necessary to ensure its financial viability. It referred to many of the sources provided in its post-hearing data response and noted that its outside auditor, KPMG, has also advised that depreciation should not be discontinued when a plant is temporarily idled. In addition, Big Rivers stated that Burns and McDonnell, the firm that had prepared the depreciation study submitted in this case on behalf of Big Rivers, took the position that depreciation should be continued on a plant that is being temporarily idled.[82]

In studying this issue, the Commission has thoroughly considered the numerous and substantial arguments presented by Big Rivers, KIUC, the AG, and Sierra Club relating both to depreciation and to excess capacity. It must be noted that the issue of discontinuing depreciation when an electric generating station is idled is one of first impression for the Commission. The Commission agrees with KIUC that we are the only agency with ratemaking authority over Big Rivers. We likewise agree with Big Rivers that there are valid reasons for not discontinuing depreciation when a plant is temporarily idled. However, based on the amount of excess capacity on the Big Rivers system as a result of idling the Coleman Station, the expected length of time that the Coleman Station will be idled, and the significant impact on customers of a rate increase of the magnitude requested by Big Rivers, we find it reasonable to require the

[81] KIUC Post-Hearing Brief at 40-47.

[82] Big Rivers' Post-Hearing Brief at 86-90.

depreciation on the Coleman Station to be recorded in a regulatory asset account and excluded from rate recovery at this time. By recording this depreciation in a regulatory asset account, the depreciation expense may be considered for recovery in rates at a future point in time.

With this treatment, for both ratemaking and accounting purposes, Big Rivers will not be changing depreciation rates or charging a rate of zero percent, as was alluded to in the arguments on this matter. Although this type of deferral will reduce its cash flow, Big Rivers will not experience the consequences referenced in its rebuttal testimony and post-hearing brief regarding making its principal debt payments. While the amount of such payments in the test period was identified as $19.8 million, it was confirmed at the hearing, based on Big Rivers' proposed depreciation rates, that test-year depreciation expense was more than double its required principal payments.[83]

Based on the above discussion, Big Rivers will be required to record its test-year depreciation on the Coleman Station of $6,192,660 as a deferred asset rather than as an expense. It should offset its debits to the deferred asset with a credit to its reserve for accumulated depreciation, just as it would if the depreciation were being charged to expense. It is the Commission's intent that the amount recorded as a deferred asset will be considered for amortization at some future point in time if and when the facility is needed to serve customers, is sold, or is permanently closed. This treatment results in a reduction in Big Rivers' test-year depreciation expense of $6,192,660. To match the test year, Big Rivers should recognize this treatment beginning in September of 2013.

[83] Cross-examination of John Wolfram, July 3, 2013 Hearing at 12:54:20 – 12:54:58.

SEVERANCE COSTS

Based on its intent at the time it filed its application to idle or "lay-up" its Wilson Station, Big Rivers calculated a reduction in labor costs of $10,432,610 to reflect the layoff of 92 Wilson Station employees. In conjunction with this planned layoff, Big Rivers projected that it would incur $4,609,073 in severance costs,[84] which it intended to record in a regulatory asset account. Big Rivers sought Commission approval to create a regulatory asset account for this purpose and authority to amortize these costs over a period of 60 months, which equates to an annual expense of $921,814.[85]

At the formal hearing in this matter, KIUC stated that, if none of Big Rivers' generating plants is idled during the test year, the severance costs Big Rivers projected in conjunction with lay-offs of employees at either the Coleman or Wilson generating stations should be removed from the forecasted test year.[86]

During the July 30, 2013 formal hearing in Case No. 2013-00221, Big Rivers' COO indicated during cross-examination by the AG that the severance costs included in its test year could be deferred until the Coleman Station was actually idled.[87]

While it continues to operate in a must-run capacity as required by MISO, the Coleman Station has been effectively idled and removed from Big Rivers' generation portfolio because its operation, variable O&M expenses, and the revenues generated by its operation are within MISO's control during the time it is operated in such a capacity.

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[84] Exhibit Haner-2.

[85] Direct Testimony of Deanna M. Speed at 19-20 and Exhibit Haner-2.

[86] Questioning of Lane Kollen, July 3, 2013 Hearing at 15:24:42 – 15:25:00.

[87] Response by Robert W. Berry, July 30, 2013 Hearing in Case No. 2013-00221 at 10:43:56 – 10:44:20. This response reflected the change in Big Rivers' plans, cited earlier in the Order, to idle the Coleman Station rather than the Wilson Station.

That means the workforce necessary to continue the operation and maintenance of the Coleman Station will remain in place, at least for the near-term future, pursuant to an agreement entered into by Big Rivers and Century. The parties agreed that from August 20, 2013, when Century begins receiving power purchased at market prices, until May 31, 2014, an "abbreviated must run" period would exist. Thus, the Commission recognizes that this must-run period extends through the first nine months of the forecasted test period in this case, and Big Rivers has filed another rate case, Case No. 2013-00199, utilizing the forecasted test period of February 2014 through January 2015 which must be adjudicated by April 27, 2014. Based on these factors, the Commission finds it appropriate and reasonable to remove the annual amortization expense of $921,814 for severance costs from the test year in this case and from the determination of Big Rivers' revenue requirement.

ALCAN TERMINATION

Although it criticized Big Rivers for not reflecting the impacts of the scheduled January 30, 2014 termination of Alcan in its forecasted test year, KIUC did not propose any adjustments to the test year in its direct testimony.[88] When questioned during the hearing, KIUC's revenue-requirement witness identified specific adjustments he would recommend to the test year, which related to (1) debt that was not issued, (2) potential elimination of severance costs, and (3) cessation of depreciation expense.[89] However, no recommendation was offered related to the upcoming Alcan termination.

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[88] Kollen Testimony at 44-46.

[89] Questioning of Lane Kollen, July 3, 2013 Hearing at 15:24:42 – 15:26:37.

In its post-hearing brief, based on Big Rivers' decision to idle the Wilson Station in conjunction with the Alcan termination, KIUC presented two adjustments for the first time. The first, based on the expectation that the Wilson Station will operate only for the first five months of the forecasted test year, called for allowing only five-twelfths of the annual depreciation on the Wilson Station. The second adjustment, also based on the expectation that the Wilson Station will only operate for the first five months of the test year, called for allowing only five-twelfths of the annual "Fixed Departmental Expenses" ("FDE") incurred to operate the Wilson Station. The total of these two adjustments is approximately $28 million.

The Commission finds no reason at this time to make the two adjustments proposed by KIUC. While the Alcan termination and the idling of the Wilson Station are expected to occur during the forecasted test period, Big Rivers has a second general rate application pending before the Commission in which the effective date of the new rates will be January 28, 2014. Consequently, the rates established in today's Order will be superseded by new rates to be effective coincident with the occurrence of those two events. Therefore, it is not appropriate to reduce the depreciation and FDE costs for the Wilson Station in determining Big Rivers' current revenue requirement, since the rates established today will be in effect for only the five months during which the Wilson Station will be operational.

IDLING OF COLEMAN VS. WILSON

As stated previously, at the time of its application Big Rivers planned to idle the Wilson Station in response to the reduced demand on its system caused by the Century termination. Based on that plan, Big Rivers' forecasted test year reflected a decrease in

FDE costs based on the average savings it estimated it would realize for calendar years 2014 and 2015 based on reductions in both FDE labor costs and FDE non-labor costs. Big Rivers also proposed an adjustment to its test-year O&M expenses to eliminate non-recurring labor expenses that would be incurred in the first three months after the Wilson Station was idled, but that would not be incurred thereafter.[90] The total amount of the FDE cost reductions and the adjustment for non-recurring labor expenses was $28,470,651 and was based on eliminating 92 positions from the Wilson Station workforce.[91]

In its rebuttal, when it stated that the Coleman Station either would be idled if not required to operate in a must-run capacity, or "effectively" idled if required to operate in this manner, Big Rivers stated that "from a financial perspective the Coleman Station will look as if it is idled."[92] Big Rivers averred that under SSR status, MISO retains the revenue from the station's generation to offset the operating costs of the station, so that the Coleman Station would not be a part of its generation portfolio.[93] Big Rivers also stated that, while there would be a minimal difference in its fixed-cost savings if the Coleman Station were idled, its financial forecast would not be affected if that station were idled rather than the Wilson Station.[94]

While the difference in fixed-cost savings from idling the Coleman Station instead of the Wilson Station is fairly small, relatively speaking, the Commission believes that

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[90] Wolfram Testimony at 18-19.

[91] *Id.*, Exhibit Wolfram-2.3, page 12, Reference Schedule 1.10.

[92] Barry Rebuttal at 18.

[93] *Id.*

[94] *Id.*, at 19.

financial recognition should be given to the idling of the Coleman Station rather than the Wilson Station. The information provided by Big Rivers in responses to various data requests indicates that the total savings from FDE reductions and non-recurring labor expenses resulting from idling the Coleman Station, based on a reduction of 95 positions, would be $28,660,568, a reduction that is $189,917 greater than the reduction that would result from idling the Wilson Station. Accordingly, the Commission will reflect an adjustment to reduce Big Rivers' test year O&M expenses by $189,917 to recognize the impact of the Coleman Station's being effectively idled.

OFF-SYSTEM SALES MARGINS

Citing decreases experienced in recent years, Big Rivers included $4.4 million in margins from off-system sales in its test year.[95] This is $15 million less than the amount it realized in the test year in its last rate case, the 12 months ending October 31, 2010.[96]

Pursuant to the Commission's regulation governing the filing requirements for applications based on a forecast test period, Big Rivers' application included a base period consisting of six months of actual data and six months of forecasted data. The base period presented by Big Rivers is the 12 months ending April 30, 2013.[97]

Big Rivers included monthly variance reports for the first six months of the base period (May through October of 2012) in its application. It provided monthly variance reports for the last six months of the base period by providing periodic updates to its application. The variance report for the last month of the base period, April 2013, was

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[95] Direct Testimony of Billie J. Richert at 12.

[96] *Id.*

[97] Wolfram Testimony at 9.

included in the update filed by Big Rivers on July 24, 2013. These variance reports show that Big Rivers' actual margins on off-system sales during the 12-month base period were $7,191,424. Based on these results and the improvement in market prices Big Rivers experienced during the first part of 2013,[98] the Commission has adjusted the forecasted test year to reflect this level of margins on off-system sales, which is an increase of $2,791,424 above the amount Big Rivers had included in the test year.

DEPRECIATION RATES

Pursuant to the Commission's direction in Case No. 2011-00036, Big Rivers filed a depreciation study as part of its application in this proceeding.[99] Based on the outcome of that study and the resulting depreciation rates, the amount of depreciation expense Big Rivers included in its test period was $47,487,509, which is $1,778,761 greater than the annual depreciation expense using its existing depreciation rates.[100]

In recognition that the rates approved in this case will be in effect for a relatively short period of time, the Commission will not authorize Big Rivers to use the new depreciation rates resulting from the depreciation study filed with its application. As depreciation is a non-cash expense, reducing Big Rivers' depreciation expense by $1,778,761 will result in a dollar-for-dollar decrease in the amount of the revenue increase it will receive in this case. However, there will be no impact on the margins and TIER upon which that increase will be based. In light of the temporary nature of the rates awarded herein, the Commission will reflect an adjustment to reduce Big Rivers'

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[98] Cross-examination of Mark Bailey, July 1, 2013 hearing at 15:00:18 – 15:00:23.

[99] Direct Testimony of Ted J. Kelly, Exhibit Kelly-1.

[100] Big Rivers' response to Item 29 of Commission Staff's Feb. 14, 2013 Request for Information.

test-year O&M expenses by $1,778,761 and require it to continue using the depreciation rates that are currently in use and that were authorized by the Commission in Case No. 2011-00036. Big Rivers' new depreciation study has already been filed in its new rate case, Case No. 2013-00199, and will be considered in that case.[101]

PRO FORMA ADJUSTMENTS SUMMARY

The effect of the accepted adjustments on Big Rivers' net income is as follows:

	Forecasted Test Period	Commission Adjustments	Adjusted Test Period
Operating Revenues	$358,593,662	$ 2,791,424	$ 361,385,086
Operating Expenses	377,677,595	(9,855,498)	367,822,097
Net Operating Income	(19,083,933)	12,646,922	(6,437,011)
Interest on Long-Term Debt	43,511,699	0	43,511,699
Total – Non-Operating Items	4,423,808	0	4,423,808
Net Income	$ (58,171,824)	$ 12,646,922	$ (45,524,902)

REVENUE REQUIREMENTS

Big Rivers' test-year rate of return on the net investment rate base found reasonable herein before reflecting an increase in rates is (1.57) percent, while its test-year TIER before reflecting any rate increase is (0.34X). Big Rivers based its revenue requirement determination on the maximum Contract TIER of 1.24X as permitted under the terms of the Alcan Smelter Agreement.[102] This is the same TIER requested by Big Rivers and granted by the Commission in Big Rivers' most recent base rate case.

Referring to the Contract TIER as being required under the Century and Alcan Smelter Agreements, the AG opposed the use of the Contract TIER to determine Big

[101] Big Rivers' response to Commission Staff's First Request for Information, Item 55, filed July 12, 2013, Case No. 2013-00199.

[102] Based on Big Rivers' adjusted test-year level of Interest on Long-Term Debt of $43,511,699, a 1.24X TIER results in margins of $10,442,808.

Rivers' revenue requirement in this case. He argued that since both Smelter Agreements will have been terminated prior to the end of the forecasted test period, the 1.24 Contract TIER will be void and no longer a requirement for Big Rivers.[103] The AG advocated using a Margins for Interest Ratio ("MFIR") to calculate Big Rivers' revenue requirement and recommended using a 1.10 MFIR, which is the minimum annual MFIR Big Rivers must achieve under its loan covenants.[104]

The Commission finds the AG's position on Big Rivers' Contract TIER to be in error. The Contract TIER was not required by the Smelter Agreements; it was the maximum TIER allowed under the Smelter Agreements before Big Rivers would be required to make refunds to the Smelters of amounts in excess of a 1.24 TIER. In recognition that Big Rivers has filed another rate case to reflect the impacts of Alcan's scheduled January 2014 termination, and to be consistent with our consideration of other potential adjustments related to Alcan's termination, the Commission will acknowledge that the Alcan Smelter Agreement remains in effect and that it provides for a maximum Contract TIER of 1.24.

Other than selecting a 1.10 MFIR because that is the coverage ratio required by Big Rivers' loan covenants, the AG did not explain why a MFIR was reasonable. The AG did not provide any rationale for using the minimum annual MFIR Big Rivers must achieve, nor did he discuss, as he did with other of his recommendations, whether he had made any comparable proposals in other jurisdictions and, if so, the rulings on those proposals. A 1.10 MFIR would produce net margins of $4,351,170, the minimum net margins, based on the test-year interest expense on long-term debt of $43,511,699,

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[103] Ostrander Testimony at 10.

[104] *Id.*

required of Big Rivers to comply with the requirements of its loan covenants. This will not provide any "cushion" in the event of either an unexpected decline in revenues or unavoidable increase in expenses. Absent any reasoning or support for using the minimum-interest coverage required of Big Rivers annually to calculate its revenue requirement, the Commission will not adopt the AG's recommendation on this issue.

Consistent with our discussion on delaying for now Big Rivers' adoption of new depreciation rates, the magnitude of its requested rate increase and the short-term nature of the rates approved in this proceeding are highly unusual and unique factors applicable to this case. The AG's recommended use of a 1.10 MFIR would allow Big Rivers a margin of approximately $4.35 million, whereas a 1.2 TIER would allow Big Rivers a margin of approximately $8.7 million. Under its prior mortgage covenants with RUS, Big Rivers was obligated to have a minimum average TIER of 1.05 for the two best of the last three calendar years. However, under its current indenture with U.S. Bank National Association, Big Rivers must achieve a minimum MFIR of 1.10 every year. The requirement of meeting a minimum coverage level each and every year creates a greater need for the use of a coverage ratio that will produce margins above the minimum needed so that an unexpected event, such as a drop in projected revenues or an increase in expenses, does not result in a mortgage default.

For all these reasons, the Commission believes that the use of TIER in this case is the most reasonable approach for determining Big Rivers' revenue requirement. However, in this instance, we find that a slightly lower TIER than that proposed by Big Rivers should be awarded. Given (1) the magnitude of Big Rivers' requested increase, (2) that Big Rivers has another rate case pending before the Commission with a

suspension period that ends approximately three months from now, and (3) that Big Rivers' TIER for the first seven months of calendar year 2013 was 1.67X,[105] the Commission finds that a TIER of 1.20X is reasonable and appropriate at this time. Based upon the adjustments found reasonable herein, the Commission has determined that, in order to produce a TIER of 1.20X, Big Rivers will require an increase in revenues of $54,227,241. This additional revenue should produce net operating income of $47,790,230, resulting in a 3.92 percent rate of return on the net investment rate base of $1,218,334,984 found reasonable herein. Based on a TIER of 1.20X, the interest on long-term debt found reasonable herein of $43,511,699, and the positive non-operating items of $4,423,808 the resulting net margins are $8,702,340.

PRICING AND TARIFF ISSUES

COST-OF-SERVICE STUDY AND REVENUE ALLOCATION

Big Rivers filed a fully allocated cost-of-service study ("COSS") which used a 12 coincident peak methodology to allocate production and transmission demand-related costs for ratemaking purposes.[106] The COSS showed a negative pro forma system rate of return and that the Smelter class was subsidizing the Rural and Large Industrial classes. The COSS also showed that the Rural class was receiving a subsidy of $4.77 million.[107] Big Rivers proposed to allocate the requested increase to eliminate the gap between the rate of return for the Rural class and the rate of return for the other classes

[105] Big Rivers' Aug. 22, 2013 Seventh Update of its response to Item 43 of Commission Staff's Dec. 21, 2012 Request for Information. For 2013 year-to-date through July 31, 2013, Big Rivers reported net margins of $17,169,690 and interest on long-term debt of $25,686,529. TIER = (net margins + interest on long-term debt) / interest on long-term debt. Accordingly, ($17,169,690 + $25,686,529) / $25,686,529 = 1.67.

[106] Wolfram Testimony at 26.

[107] Calculated using the Revised COSS filed with Wolfram Rebuttal Testimony on June 24, 2013.

on a combined basis.[108] Stated another way, Big Rivers proposed to allocate the revenue increase such that the rate of return for the Rural class will equal the total system rate of return, which would eliminate the Rural subsidy. None of the intervenors filed a COSS and none objected to the one filed by Big Rivers. The Commission has reviewed Big Rivers' COSS and finds it to be acceptable for use as a guide in allocating the revenue increase granted herein.

Among the intervenors, only KIUC filed testimony addressing Big Rivers' proposal to eliminate the Rural subsidy. KIUC supported Big Rivers' proposal and offered additional reasons for why the subsidy should be eliminated.[109] In his post-hearing brief, the AG argued that the elimination of the Rural subsidy in its entirety is not in compliance with the principal of gradualism which was cited by the Commission in its decision on this issue in Big Rivers' most recent rate case, Case No. 2011-00036.[110] The AG proposed that the subsidy be reduced by an amount equivalent to the reduction of $2.4 million made to the subsidy in that case. No other intervenor objected to eliminating the Rural subsidy

After considering the issue, the Commission finds that the Rural subsidy should be eliminated in its entirety. As discussed in the AG's post-hearing brief, the amount of the Rural subsidy at issue in Case No. 2011-00036 was $11.1 million. In the instant case, the subsidy is significantly smaller at $4.77 million. In addition, if this subsidiary is not eliminated, it will be paid solely by Alcan, the only remaining smelter on Big Rivers'

[108] The Smelter rate is based on the Large Industrial rate and therefore any change in the Large Industrial rate affects the Smelter rate and likewise its rate of return.

[109] Kollen Testimony at 61-62.

[110] Case No. 2011-00036, AG Post-Hearing Brief at 45.

system, and Alcan's notice of termination will be effective in less than three months. For these reasons, the Commission finds it reasonable to eliminate this subsidy.

Based on the increase granted herein of $54,227,241 and eliminating the Rural subsidy, the Commission finds that the increase should be allocated to Big Rivers' rate classes as follows: $30.48 million to the Rural class, $5.46 million to the Large Industrial class, and $18.29 million to the Smelter class.[111] This results in an increase of 21.9 percent for the Rural class, 11.8 percent for the Large Industrial class, and 11.2 percent for the Smelter class.

RATE DESIGN

Big Rivers proposed to increase the energy charges of both the Rural and Large Industrial classes to $.0300 per kWh, with the remainder of its requested increase in revenue being accomplished with increases to the demand charges of both classes. The current energy charges are, respectively, $.024508 for the Large Industrial class and $.029736 for the Rural class. For the Large Industrial class, Big Rivers proposed to increase the demand charge from $10.50 per KW to $12.41 per KW, while for the Rural class, it proposed to increase the demand charge from $9.697 per KW to $ 16.95 per KW. This proposed rate design would result in a significant increase to the demand charge of the Rural class. Only one intervenor, the AG, filed testimony objecting to the

[111] As discussed in Big Rivers' response to Item 1 to Commission Staff's July 22, 2013 Request for Information, because total environmental surcharge ("ES") costs are split between native load sales and off-system sales on the basis of total revenues, there is an ES revenue effect that occurs with an increase in base rates. The rates approved in this Order result in a base rate increase of $53,791,979, and the related incremental increase in ES revenues provides the remainder of the increase

rate design proposed by Big Rivers.[112] The AG stated that Big Rivers was proposing a major change in rate design and that, "[a]ssuming Big Rivers' members pass these costs along to the Rural residential and small commercial customers in the same fashion, this will result in a much larger rate impact for those customers with lower than average load factors."[113]

As each of Big Rivers' member cooperatives have filed an application proposing to pass through the wholesale increase to each rate class and within each rate class on a proportional basis, the Commission finds that the wholesale increase is not being passed-through "in the same fashion" as that of Big Rivers. Therefore, the Commission finds the AG's argument to be without merit. However, the Commission has some concerns about the significant increase to the Rural demand charge that would result from Big Rivers' proposed rate design and finds that some adjustment is necessary. The Commission will accept the proposed increase to the Large Industrial class energy charge from $.024508 per kWh to $.0300 per kWh; however, in order to mitigate the increase to the Rural demand charge, we will increase the Rural energy charge from $.029736 per kWh to $.0350 per kWh, an increase similar in magnitude to that for the Large Industrial energy charge. The remaining increase will be achieved by increasing the demand charge from $10.50 to $10.715 for the Large Industrial class, and from $9.697 to $12.914 for the Rural class.

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[112] KIUC questioned Big Rivers' witness Billie Richert about the proposed rate design at the hearing; however when KIUC witness Lane Kollen was questioned by Commission Staff counsel about this issue at the hearing, he stated that KIUC was not proposing an alternative rate design. July 3, 2013 Hearing at 15:06:03.

[113] Direct Testimony of Larry W. Holloway at 20.

ECONOMIC AND RURAL ECONOMIC RESERVE FUNDS

In its application, Big Rivers proposed no change to the operation of the Member Rate Stability Mechanism ("MRSM") which was established pursuant to Case No. 2007-00455 at the closing of the Unwind Transaction.[114] At that time, $157 million was deposited into what is known as the Economic Reserve ("ER") fund, and the MRSM is the tariff provision that now utilizes that fund each month to partially offset fuel and environmental costs for the Rural and Large Industrial classes. Upon exhaustion of the ER fund, the MRSM will utilize a Rural Economic Reserve ("RER"), which was also created at the closing of the Unwind Transaction. The RER is a separate fund created by a $60.9 million contribution from the former lessee of Big Rivers' generating facilities and is to be used exclusively for the purpose of partially offsetting fuel and environmental costs for the Rural class.

The AG, in apparent support of Big Rivers' plan to make no change to the MRSM, stated in his post-hearing brief that "these funds should be maintained and used in the spirit that they were created."[115] KIUC, however, in its post-hearing brief argued that the use of the RER funds to benefit only the Rural class is discriminatory and KIUC recommends that the terms of the RER fund should be amended to also benefit the Large Industrial class.

In reviewing the issue of how the amount of the RER funds should be dispersed, the Commission has reviewed the findings in our March 6, 2009 Order approving the Unwind Transaction in Case No. 2007-00455. In that Order, we specifically stated:

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[114] Case No. 2007-00455 (Ky. PSC Mar. 6, 2009).

[115] AG Post-Hearing Brief at p. 46.

> Unfortunately, under the Unwind Transaction, a combination of higher fuel costs and exhaustion of the Economic Reserve account in 2013 will result in rate increases for Rural Customers that are simply too high. Thus, Big Rivers' reacquisition of control of its generating units will be consistent with the public interest only if some mitigation is provided to offset the projection of higher rates for the Rural Customers.
>
> Since the Applicants have indicated that time is of the essence in completing the Unwind Transaction, the Commission finds that, rather than delaying this case to allow the Applicants time to fashion a remedy, we will create a reasonable remedy and condition this Order upon the Applicants' acceptance thereof. The E.ON Entities have agreed to reimburse Big Rivers for one-half of the cost of the PMCC buy-out, amounting to approximately $60.9 million. The Commission finds that the E.ON Entities should reimburse Big Rivers 100 percent of that cost, with the additional $60.9 million being held by Big Rivers in a new reserve account to be known as the Rural Economic Reserve. This account will be recorded as a regulatory liability and used over 24 months only as a credit against the rates of the Rural Customers upon exhaustion of the Non-Smelter Economic Reserve. This additional $60.9 million should be invested in interest-bearing U.S. Treasury securities, with all interest credited to the Rural Economic Reserve. Big Rivers will need to revise its tariffs to include a new rate mechanism, to be known as the Rural Economic Reserve, to flow back to the Rural Customers the funds in the Rural Economic Reserve Account. [116]

Thus, it is clear from the March 6, 2009 Order in Case No. 2007-00455 that the Commission adopted the AG's position that the Unwind Transaction would result in future rate increases for the Rural class that "are simply too high," and that absent the creation of the RER, the Unwind Transaction would not be in the public interest and would not be approved. The Commission then expressly conditioned approval of the Unwind Transaction upon the creation and funding of the RER by stating in the ordering paragraphs:

[116] Case No. 2007-00455, Order entered Mar. 6, 2009, at 25-26.

> 1. The change in control of generating units from the E.ON Entities to Big Rivers is approved subject to Big Rivers' receipt of an investment grade credit rating and the filing within seven days of the date of this Order of written notices signed by the chief executive officers of Big Rivers and the E.ON Entities that each agrees to accept and be bound by their respective commitments set forth in Appendices A and B to this Order.

The specific condition precedent requiring the RER was set out in great detail in Appendix A to that Order, which provided as follows:

> 24. Big Rivers commits that a Rural Economic Reserve account will be established and funded at closing of the Unwind Transaction in an amount no less than $60.9 million to be used exclusively to credit the bills rendered to the Rural Customers over a period of 24 months commencing upon depletion of all funds in the Economic Reserve. All funds in the Rural Economic Reserve shall be invested in interest-bearing United States Treasury notes, with all interest earned credited to the Rural Economic Reserve. Big Rivers commits that no funds in the Rural Economic Reserve escrow account will be spent, pledged, or otherwise used for any purpose other than as credits on the future bills of Rural Customers in accord with the terms of this commitment.

By separate letters filed March 13, 2009, Big Rivers and the E.ON entities gave their respective notices to accept and be bound by the commitments in the appendices to the March 6, 2009 Order in Case No. 2007-00455. Consequently, upon the closing of the Unwind Transaction $60.9 million was deposited into the RER fund to be used to mitigate future rate increases for the Rural class.

As previously noted, KIUC was an intervenor in Case No. 2007-00455, representing Alcan and Century, as well as the three large industrial customers it represents in this case: Aleris; Domtar; and Kimberly Clark. At no time during the 14 plus months that Case No. 2007-00455 was before the Commission did KIUC claim that the Unwind Transaction would result in rate increases that would be too high for Aleris,

Domtar, and Kimberly Clark. To the contrary, Alcan and Century filed testimony supporting the Unwind Transaction as beneficial for both Industrial customers and Rural customers:

> For the non-smelter members, the transaction also has benefit. Because of the Smelter Surcharge payments and the Economic Reserve, an increase in rates to the non-smelter members is substantially mitigated and rates for the long term are projected to remain low. And most importantly, the transaction preserves the economic health of Western Kentucky.[117]

KIUC chose to not seek a rehearing or file an appeal of the March 6, 2013 Order in Case No. 2007-00455 on any grounds, including any claim that the establishment of the RER was discriminatory, or that the Unwind Transaction would result in unreasonable rate increases for Aleris, Domtar, and Kimberly-Clark and the RER fund should be amended to benefit them.

The future rate increases described in the March 6, 2009 Order in Case No. 2007-00455 are now, unfortunately, becoming a reality. Although the ER fund has not yet been exhausted, the three industrial customers represented by KIUC now seek to reverse their prior position. KIUC now assails as discriminatory the Commission's findings in Case No. 2007-00455 that the Unwind Transaction would be in the public interest only if the E.ON entities provided additional funds to create the RER to mitigate rate increases for Rural customers.

Based on a review of our prior findings as to the need for the RER fund and the participation by Aleris, Domtar, and Kimberly Clark as intervenors in Case No. 2007-00455, the Commission finds that there has been no showing of sufficiently changed circumstances to justify amending the established purpose of the RER fund. KIUC is

[117] Case No. 2007-00455, Direct testimony of Henry W. Fayne, at 13, filed Jan. 25, 2008.

now trying to relitigate our 2009 findings in Case No. 2007-00455 as to what conditions needed to be established prior to Commission approval of the Unwind Transaction. The time for KIUC to raise its challenge to the RER expired over four years ago.[118]

KIUC has presented no evidence to demonstrate that there has been a change in circumstances since March 6, 2009, sufficient to justify a relitigation of the need and purpose for RER fund. Based on the evidence in this record, we now reaffirm our prior finding that the RER fund is to be used to mitigate rate increases for the Rural class.

TARIFF CHANGES

Big Rivers proposes a number of non-substantive changes to its tariffs to address grammatical and spelling errors. There were no objections to these tariff changes from the intervenors. The Commission finds that Big Rivers' proposed non-substantive tariff changes are reasonable and should be approved.

REFUND REQUIREMENTS

As stated previously, after Big Rivers placed its proposed rates in effect on August 20, 2013, we required it to maintain its records in order that the amount of any refund could be determined if the rates the Commission ultimately granted were less than the rates Big Rivers proposed and which it has placed in effect. Given that the rates authorized herein are less than the proposed rates placed in effect by Big Rivers, the Commission finds that refunds should be made. Accordingly, Big Rivers will be required to refund the excess revenues collected from August 20, 2013, through the

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[118] KIUC's argument that the Commission allowed the Transition Reserve to be used for other than its original purpose is unpersuasive. The Transition Reserve was not a Commission created condition to the Unwind Transaction. The Transition Reserve was established by the Unwind Transaction to benefit all customers and its use for capital expenditures is benefitting all customers. Thus, the intended purpose of the fund has not changed.

date of this Order to its three member cooperatives in compliance with the refund provisions contained in KRS 278.190(4).

Consistent with the Commission's requirement in other rate cases in which refunds were required, Big Rivers will be required to pay interest on the refunded amounts at the average of the Three-Month Commercial Paper Rate as reported in the Federal Reserve Bulletin and the Federal Reserve Statistical Release on the date of this Order.[119] Pursuant to KRS 278.190(4), all refunds must be made within 60 days from the date of this Order.

OTHER ISSUES

REPORTING REQUIREMENTS

The AG, citing Big Rivers' financial condition and his concerns with Big Rivers' decisions regarding salary increases, deferred maintenance, and lack of transparency in various areas, proposed that Big Rivers be required to comply with specific monitoring and reporting requirements he had developed.[120] Some of his proposed requirements would call for Big Rivers to provide immediate notice to both the AG and Commission. Many of the proposed requirements would call for Big Rivers to make quarterly filings with the AG and Commission, while the other proposed requirements call for annual filings to the AG and Commission.[121]

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[119] *See* Case No. 1992-00346, The Application of The Union Light, Heat and Power Company for an Adjustment of Rates (Ky. PSC July 23, 1993) and Case No. 2010-00036, Application of Kentucky-American Water Company for an Adjustment of Rates Supported by a Fully Forecasted Test Year (Ky. PSC Dec. 14, 2010).

[120] Ostrander Testimony at 73-74.

[121] *Id.*

On rebuttal, Big Rivers argued that the AG has provided no rationale for why any of his proposed reporting requirements should be adopted.[122] Big Rivers claimed that the proposed requirements seemed to be designed to review financial and operational data – much of it confidential – that would be relevant only to a future rate case and that the AG should wait until such future rate proceedings to pursue this information.[123]

Based on the AG's arguments in support of the reporting requirements and Big Rivers' arguments in opposition thereto, the Commission is not persuaded that there is a need at this time to impose these additional reporting requirements on Big Rivers. Therefore, the AG's proposal is denied.

ENERGY EFFICIENCY AND DEMAND-SIDE MANAGEMENT

In its prior base rate case, Case No. 2011-00036, Big Rivers acknowledged that, historically, it had not offered significant energy-efficiency ("EE") and demand-side management ("DSM") programs to its member-owners and their retail customers. At that time, it had developed several pilot programs it was just starting to implement. Since that time, Big Rivers has sought and received approval of ten permanent EE/DSM programs.[124]

The Commission commends Big Rivers for the actions it has taken since its prior rate case in the area of EE/DSM. However, as we have stated in many other orders, as greater constraints are placed on utilities whose primary source of energy is coal-fired generation, EE/DSM and conservation have become more important. We note that the

[122] Bailey Rebuttal at 15.

[123] *Id.*

[124] Case No. 2012-00142, Tariff Filing of Big Rivers Electric Corporation to Implement Demand-Side Management Programs (Ky. PSC Aug. 22, 2012).

Governor's energy plan, *Intelligent Energy Choices for Kentucky's Future, November 2008*, calls for an increase in DSM by 2025. Furthermore, the Commission stated its support for cost-effective EE/DSM programs in response to several of the recommendations included in *Electric Utility Regulation and Energy Policy in Kentucky*, the report submitted in July 2008 to the Kentucky General Assembly by the Commission pursuant to Section 50 of the 2007 Energy Act.

In addition to the reasons cited above, the Commission takes note of President Obama's June 25, 2013 Climate Action Plan and Presidential Memorandum directing the EPA to "...issue proposed carbon pollution standards, regulations, or guidelines, as appropriate, for modified, reconstructed, and *existing* power plants by no later than June 1, 2014."[125] Carbon standards for existing power plants, in whatever form they take, are expected to increase the constraints on utilities such as Big Rivers that rely heavily on coal-fired generation. For all these reasons, while commending Big Rivers for what it has done in recent years regarding EE/DSM, the Commission strongly urges Big Rivers, and its member cooperatives, to make a greater sustained effort to offer cost-effective EE/DSM programs to the retail customers on the Big Rivers system.

SUMMARY

The Commission, after consideration of the evidence of record and being otherwise sufficiently advised, finds that:

1. The rates set forth in the appendix to this Order are the fair, just, and reasonable rates for Big Rivers to charge for service rendered on and after August 20, 2013.

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[125] Presidential Memorandum of June 25, 2013, Power Sector Carbon Pollution Standards, 78 Fed. Reg. 39535 (2013) (Emphasis added).

2. The rate of return and TIER granted herein are fair, just, and reasonable and will provide sufficient revenue for Big Rivers to meet its financial obligations.

3. The rates proposed by Big Rivers would produce revenue in excess of that found reasonable herein and should be denied.

4. Beginning with the month of September 2013, Big Rivers should defer the depreciation on the Coleman Station in a regulatory asset account rather than record that depreciation as an expense. It should continue to credit depreciation on the Coleman Station to its accumulated depreciation, or depreciation reserve, account.

5. Big Rivers' proposal to implement new depreciation rates based on the depreciation study filed in this proceeding on its behalf should be denied.

6. Big Rivers should continue to use the depreciation rates currently in effect.

IT IS THEREFORE ORDERED that:

1. The rates and charges proposed by Big Rivers are denied.

2. The rates in the appendix to this Order are approved for service rendered by Big Rivers on and after August 20, 2013.

3. The depreciation rates proposed by Big Rivers are denied.

4. Beginning with the month of September 2013, Big Rivers shall discontinue recording depreciation of the Coleman Station as an expense and shall defer this depreciation and record it in a regulatory asset account. All other aspects of Big Rivers' accounting for depreciation shall remain unchanged.

5. Within 20 days of the date of this Order, Big Rivers shall file with the Commission, using the Commission's Electronic Tariff Filing System, new tariff sheets

setting forth the rates and charges approved herein and reflecting their effective date and that they were authorized by this Order.

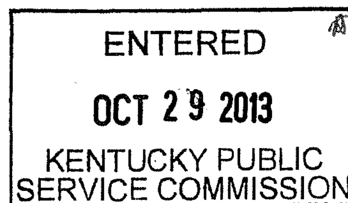
6. Within 60 days from the date of this Order, Big Rivers shall refund with interest all amounts collected for service rendered from August 20, 2013, through the date of this Order that are in excess of the rates set out in the appendix to this Order. The amount refunded to each customer shall equal the amount paid by each customer during the refund period in excess of the rates approved herein.

7. Big Rivers shall pay interest on the refunded amounts at the average of the Three-Month Commercial Paper Rate as reported in the Federal Reserve Bulletin and the Federal Reserve Statistical Release on the date of this Order.

8. Within 75 days from the date of this Order, Big Rivers shall submit a written report to the Commission in which it describes its efforts to refund all monies collected in excess of the rates that are set forth in the appendix to this Order.

9. Any documents filed pursuant to ordering paragraph 8 of this Order shall reference the number of this case and shall be retained in the utility's general correspondence file.

By the Commission



ATTEST:

Executive Director

APPENDIX

APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE COMMISSION IN CASE NO. 2012-00535 DATED OCT 29 2013

The following rates and charges are prescribed for the customers in the area served by Big Rivers Electric Corporation. All other rates and charges not specifically mentioned herein shall remain the same as those in effect under authority of this Commission prior to the effective date of this Order.

RURAL DELIVERY SERVICE

Demand Charge	$ 12.914
Energy Charge per kWh	$ .0350

LARGE INDUSTRIAL CUSTOMER

Demand Charge	$ 10.715
Energy Charge per kWh	$ .0300

COGENERATION/SMALL POWER PRODUCTION SALES – OVER 100 kW

Demand Charge - Weekly	$ 3.01
Energy Charge per kWh	$ .0350

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