

153 FERC ¶ 61,129
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Norman C. Bay, Chairman;
Cheryl A. LaFleur, Tony Clark,
and Colette D. Honorable.

Kentucky Power Company

Docket No. ES15-53-000

ORDER AUTHORIZING ISSUANCES OF SECURITIES

(Issued November 2, 2015)

1. On July 24, 2015, as amended and restated on August 31, 2015, Kentucky Power Company (Kentucky Power) filed an application requesting authorization to issue short-term debt in an amount not to exceed \$225 million at any time outstanding.¹ We will grant the requested authorization, as discussed below.

I. Restated Application

2. Kentucky Power seeks Commission authorization to issue “commercial paper, promissory notes and other forms of short-term indebtedness having varying maturities not to exceed one year” (Short-Term Debt) in an aggregate amount not to exceed \$225 million at any time outstanding.² Kentucky Power seeks authorization to issue

¹ Application Under Section 204 of the Federal Power Act for Authorization to Issue Securities, Docket No. ES15-39-000 (Jul. 14, 2015) (Application). The Application was amended and restated on August 31, 2015. Amended and Restated Application Under Section 204 of the Federal Power Act for Authorization to Issue Securities, Docket Nos. ES15-39-000, ES15-49-000, ES15-50-000, ES15-51-000, ES15-52-000, ES15-53-000, ES15-54-000, ES15-55-000, ES15-56-000, ES15-57-000. (Aug. 31, 2015) (Restated Application).

² Restated Application at 3-4. In the Application, Kentucky Power requested authorization to issue Short-Term Debt in an aggregate amount not to exceed \$250 million at any time outstanding. Application at 3. In the Restated Application, Kentucky Power reduced the requested authorization amount to \$225 million at any time outstanding. Restated Application at 4.

Short-Term Debt directly and/or to participate as a borrower in the AEP Utility Money Pool (Money Pool)³ at interest rates not to exceed the 30-day London Interbank Offered Rate (LIBOR) as referenced in the Wall Street Journal at <http://online.wsj.com> and in effect at the time of borrowing plus up to 375 basis points.⁴

3. Kentucky Power explains that the funds obtained through the issuances of Short-Term Debt will be used, together with other available funds, to “finance the construction, acquisition, maintenance, and/or modification or improvement to, new and existing electric generation, transmission and/or distribution facilities, to refinance existing debt, to meet working capital needs (including construction expenditures), and for other general corporate purposes...”⁵

4. According to Kentucky Power, the facts set out in the Restated Application show that the proposed financing transactions are for lawful purposes, to fund the day-to-day operations of Kentucky Power, which are within Kentucky Power’s corporate purposes as set forth in its articles of incorporation and properly authorized by its board of directors. Kentucky Power states that the issuance of Short-Term Debt is necessary, appropriate for and consistent with the proper performance by Kentucky Power of its service obligations as a public utility.

5. Kentucky Power agrees that any secured or unsecured debt securities issued pursuant to the authorization requested in the Restated Application will be subject to the four restrictions on such securities specified in *Westar Energy, Inc.*⁶

³ Commission-regulated entities are required to file their cash management agreements with the Commission. *See* 18 C.F.R. § 141.500 (2015). The information provided is used to aid the Commission in monitoring cash management programs. The rule is not in the nature of a regulation governing participation in cash management programs. Therefore, this order does not address any request for authorization to participate in a cash management program. *See Regulation of Cash Management Practices*, Order No. 634-A, FERC Stats. & Regs. ¶ 31,152 (2003) (Order No. 634-A) (Cross-Referenced at 105 FERC ¶ 61,098 (2003)). Kentucky Power states that the current Utility Money Pool Agreement has been filed with the Commission pursuant to 18 C.F.R. § 141.500 in accordance with Order No. 634-A. Restated Application at 6.

⁴ Restated Application at 4.

⁵ *Id.* at 9.

⁶ 102 FERC ¶ 61,186, at PP 20-21 (2003) (*Westar*).

II. Notice of Filing

6. Notice of the Application was published in the *Federal Register*, 80 Fed. Reg. 45,651 (2015), with interventions and protests due on or before August 14, 2015.⁷ None was filed.

7. Notice of the Restated Application was published in the *Federal Register*, 80 Fed. Reg. 56,978 (2015), with interventions and protests due on or before September 21, 2015. None was filed.

III. Discussion

8. FPA section 204(a) provides that requests for authorization to issue securities or to assume any obligation or liability as guarantor, indorser, surety, or otherwise in respect of any security of another person shall be granted if the Commission finds that the issuance or assumption: (1) is for some lawful object, within the corporate purposes of the applicant and compatible with the public interest, which is necessary or appropriate for or consistent with the proper performance by the applicant of service as a public utility and which will not impair its ability to perform that service; and (2) is reasonably necessary or appropriate for such purposes.⁸

9. In reviewing an application under FPA section 204, the Commission utilizes an interest coverage ratio calculation to determine whether the issuances for which authorization are sought “will not impair [a public utility’s] ability to perform” service as a public utility.⁹ The Commission typically bases its finding that proposed issuances of securities will not impair an applicant’s ability to perform service as a public utility in part upon the applicant’s demonstration that it will have an interest coverage ratio that is 2.0 or higher.¹⁰ In making this finding, the Commission reviews the financial statements

⁷ An errata notice correcting the July 24, 2015 notice was issued by the Office of the Secretary on August 4, 2015. See Errata Notice, Docket Nos. ES15-39-000, ES15-49-000, ES15-50-000, ES15-51-000, ES15-52-000, ES15-53-000, ES15-54-000, ES15-55-000, ES15-56-000, ES15-57-000 (Aug. 4, 2015).

⁸ 16 U.S.C. § 824(c)(a) (2012).

⁹ See, e.g., *Old Dominion Electric Cooperative*, 145 FERC ¶ 61,132, at P 12 (2013); *Startrans IO, LLC*, 122 FERC ¶ 61,253, at P 18 (2008) (*Startrans*).

¹⁰ *Startrans*, 122 FERC ¶ 61,253 at P 18 (stating that “this screen is a mid-way number in a range that has been used by lenders and borrowers and provides a buffer against unforeseen, adverse financial events that might impair Startrans IO’s ability to perform as a public utility”).

submitted with an application filed under FPA section 204 and applicant's calculation of the interest coverage ratio, which is the sum of income before interest and income taxes divided by total interest expense.¹¹ The interest coverage ratio is a screen test used primarily to provide the Commission with comfort that the financing authorized will not impair an applicant's ability to perform public utility service.¹² The Commission has stated, however, that whether or not an applicant meets the 2.0 interest coverage ratio screen does not by itself determine whether the Commission will authorize or deny the application.¹³ The Commission has approved FPA section 204 applications that have not met the 2.0 interest coverage ratio threshold.¹⁴

10. Kentucky Power has filed, as Exhibits C, D, and E to the Restated Application, actual and *pro forma* financial statements. Exhibit E of the Restated Application shows that Kentucky Power has a *pro forma* interest coverage ratio of 1.36, which is below the Commission's 2.0 interest coverage ratio test.

11. According to Kentucky Power, it currently does not meet the interest coverage ratio screen of 2.0 due to the effects of recording a one-time, \$36 million regulatory disallowance for fuel costs in December 2014. Kentucky Power states that it recorded the disallowance as a result of a January 2015 order issued by the Kentucky Public Service Commission (Kentucky Commission) that disallowed certain fuel adjustment clause costs during the period of January 2014 through May 2015.¹⁵ Kentucky Power states that, since the interest coverage ratio is administered on a twelve months' period ended basis, the effect of the regulatory disallowance distorts its income and has caused it to not meet the interest coverage ratio screen.

¹¹ *Westar*, 102 FERC ¶ 61,186 at P 15, n.15.

¹² *Montana Alberta Tie Ltd.*, 128 FERC ¶ 61,217, at P 16 (2009) (citing *Startrans*, 122 FERC ¶ 61,253, at P 18). The Commission has also described the interest coverage ratio as a measure of a utility's ability to meet future debt and interest payments. *Westar*, 102 FERC ¶ 61,186 at P 15.

¹³ *See, e.g., Startrans*, 122 FERC ¶ 61,253 at n.7.

¹⁴ *See, e.g., NorthWestern Corp.*, 151 FERC ¶ 61,120 (2015); *ITC Great Plains, LLC*, 147 FERC ¶ 61,005 (2014); *Mississippi Power Co.*, 145 FERC ¶ 61,218 (2013).

¹⁵ Restated Application at 15.

12. Kentucky Power notes, however, that the ratings agencies did not take any action after the one-time write-off in December 2014, and that its long-term indebtedness is rated investment grade.¹⁶ Kentucky Power states that both Moody's and Standard & Poor's (S&P) affirmed its ratings in February 2015.¹⁷

13. Kentucky Power also explains that, in December 2014, it filed a request with the Kentucky Commission for an increase in rates. Kentucky Power states that, on June 22, 2015, the Kentucky Commission issued an order approving a modified stipulation agreement with respect to the filed rate increase, and that the order is final and non-appealable. Kentucky Power estimates that the net revenue increase of \$45 million approved by the Kentucky Commission in the order will result in earnings in an amount that exceeds the maximum interest costs of the Short-Term Debt for which authorization is sought in the Restated Application (approximately \$8.8 million). As a result, Kentucky Power expects that the recently-approved rate increase authorized by the Kentucky Commission will result in increased earnings more than sufficient to cover the interest expense generated by any new borrowing.¹⁸

14. As explained above, in FPA section 204 filings, the Commission utilizes an interest coverage ratio calculation in its evaluation of a public utility's financial viability, and generally requires an applicant filing under FPA section 204 to demonstrate, on a *pro forma* basis, that net income will equal or exceed twice total interest expense.¹⁹ In this case, Kentucky Power's *pro forma* interest coverage ratio is below 2.0. Other factors, however, provide the Commission with an alternative basis upon which the Commission may conclude that the proposed issuance of Short-Term Debt will not impair Kentucky Power's ability to service the proposed debt securities and continue to provide service as a public utility. Specifically, Kentucky Power has demonstrated that the rate increase approved by the Kentucky Commission will provide earnings in an amount sufficient to cover the interest cost of the Short-Term Debt for which Kentucky Power seeks authorization in the Restated Application. In addition, Kentucky Power's long-term indebtedness is rated investment grade by credit ratings agencies, and those ratings were recently reaffirmed by those agencies.

¹⁶ *Id.* at 24. Kentucky Power's long-term indebtedness is rated Baa2 by Moody's and BBB by S&P.

¹⁷ *Id.*

¹⁸ *Id.* at 25.

¹⁹ *See, e.g., Startrans*, 122 FERC ¶ 61,253 at P 18.

15. We find, based on the statements set forth in the Restated Application, that Kentucky Power has demonstrated that the proposed issuance of Short-Term Debt described in the Restated Application: (1) is for a lawful object within the corporate purposes of Kentucky Power and compatible with the public interest, is necessary or appropriate for, or consistent with, the proper performance by Kentucky Power of its service as a public utility, and will not impair its ability to perform that service; and (2) is reasonably necessary or appropriate for such purposes.

16. Accordingly, based upon the terms and conditions and for the purposes specified in the Restated Application, Kentucky Power is authorized to issue Short-Term Debt in an aggregate principal amount not to exceed \$225 million at any time outstanding. The Short-Term Debt indebtedness may consist of commercial paper, promissory notes, or other forms of short-term indebtedness.

17. The interest rate for the Short-Term Debt will not exceed the 30-day LIBOR as referenced in the Wall Street Journal at <http://online.wsj.com> in effect at the time of borrowing plus up to 375 basis points.

18. In *Westar*, the Commission announced four restrictions on all future public utility issuances of secured and unsecured debt.²⁰ First, public utilities seeking authorization to issue debt backed by a utility asset must use the proceeds of the debt for utility purposes. Second, if any utility assets that secure debt issuances are divested or “spun off,” the debt must follow the asset and also be divested or spun off. Third, if any of the proceeds from unsecured debt are used for non-utility purposes, the debt must follow the non-utility assets. Specifically, if the non-utility assets are divested or spun off, then a proportionate share of the debt must follow the divested or spun off non-utility asset. Finally, if utility assets financed by unsecured debt are divested or spun off to another entity, then a proportionate share of the debt must also be divested or spun off. We will condition our authorization on Kentucky Power abiding by these restrictions.

The Commission orders:

(A) Kentucky Power is hereby authorized to issue Short-Term Debt in an aggregate amount not to exceed \$225 million at any time outstanding at the interest rate stated in the body of this order.

(B) The authorization granted by this order is effective November 2, 2015 through November 1, 2017.

²⁰ *Westar*, 102 FERC ¶ 61,186 at PP 20-21.

(C) The authorization granted in this order is subject to the restrictions specified in the body of this order and the restrictions on secured and unsecured debt as outlined in *Westar*.

(D) The authorization granted in this order is without prejudice to the authority of the Commission or any other regulatory body with respect to rates, service, accounts, valuation, estimates or determination of cost or any other matter whatsoever now pending or which may come before this Commission.

(E) Nothing in this order shall be construed to imply any guarantee or obligation on the part of the United States with respect to any security to which this order relates.

By the Commission.

(S E A L)

Nathaniel J. Davis, Sr.,
Deputy Secretary.