

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

APPLICATION OF CUMBERLAND)	CASE NO.
VALLEY ELECTRIC, INC. FOR AN)	2014-00159
ADJUSTMENT OF RATES)	

ORDER

On June 23, 2014, Cumberland Valley Electric, Inc. ("Cumberland Valley") applied for a \$1,605,137 increase in retail electric service rates. The requested increase is 3.95 percent over normalized test-year operating revenues. Cumberland Valley states that the proposed increase was required in order to maintain its financial integrity and stability, cover increases in fixed and variable costs, and meet the terms required by its mortgage agreement. Finding that an investigation would be necessary to determine the reasonableness of Cumberland Valley's proposed increase, the Commission suspended the rates for five months, up to and including December 22, 2014, pursuant to KRS 278.190(2).

BACKGROUND

Cumberland Valley is a consumer-owned rural electric cooperative corporation, organized under KRS Chapter 279, engaged in the distribution and sale of electric energy to approximately 23,700 member-consumers in the Kentucky counties of Bell, Clay, Harlan, Knox, Laurel, Leslie, Letcher, McCreary, and Whitley. Cumberland Valley has no electric generating facilities and purchases its total power requirements from East Kentucky Power Cooperative, Inc. ("EKPC").

The Commission granted a motion to intervene filed by the Attorney General, by and through his Office for Rate Intervention ("AG"). A public hearing was conducted on November 5, 2014. All information requested during the hearing has been submitted. Both parties filed post-hearing briefs on November 25, 2014.

TEST PERIOD

Cumberland Valley proposed and the Commission accepted the 12-month period ended December 31, 2013, as the test period for determining the reasonableness of the proposed rates. In utilizing the historical test year, the Commission considered appropriate known and measurable changes.

VALUATION

Rate Base

Cumberland Valley determined a net investment rate base of \$63,885,540¹ based on the adjusted test-year-end value of plant in service and construction work in progress ("CWIP"), the 13-month average balances for materials and supplies and prepayments, plus a cash working capital allowance, minus the adjusted accumulated depreciation and the test-year-end level of customer advances for construction.

The Commission concurs with Cumberland Valley's proposed rate base with the exceptions that (1) working capital has been adjusted to reflect the pro forma adjustments to operation and maintenance expenses and (2) accumulated depreciation has been adjusted to reflect the adjustment described herein. With these adjustments, Cumberland Valley's net investment rate base for ratemaking purposes is as follows:

¹ Response to Commission Staff's Second Request for Information ("Staff's Second Request"), Item 6, p. 4.

Utility Plant in Service	\$95,051,496
CWIP	<u>816,622</u>
Total Utility Plant	\$95,868,118
ADD:	
Materials and Supplies	\$ 740,992
Prepayments	175,484
Working Capital	<u>937,489</u>
Subtotal	\$ 1,853,965
DEDUCT:	
Accumulated Depreciation	\$33,700,358
Customer Advances for Construction	<u>87,549</u>
Subtotal	\$33,787,907
 NET INVESTMENT RATE BASE	 <u>\$63,934,176</u>

Capital Structure

The Commission finds that Cumberland Valley's capital structure at test-year-end for ratemaking purposes was \$62,330,183. This capital structure consisted of \$19,517,122 in equity and \$42,813,061 in long-term debt. The Commission excluded generation and transmission capital credits ("GTCCs") in the amount of \$20,577,050. Using this capital structure, Cumberland Valley's year-end equity to total capitalization ratio was 31 percent.

REVENUES AND EXPENSES

Cumberland Valley proposes several adjustments to revenues and expenses to reflect current and expected operating conditions. The Commission finds that seven of the adjustments proposed by Cumberland Valley and not opposed by the AG are reasonable and should be accepted without change. Those adjustments are shown in the following table:

<u>Descriptions</u>	<u>Adjustments</u>
Retirement & Security	\$ 34,902
FAS 106 Postretirement Benefits	\$ 33,809
Donations	\$ (10,671)
Professional Fees	\$ 17,164
Purchase Power Cost	\$ (4,394,432)
Normalize Revenues	\$ (4,358,835)
G & T Capital Credits	\$ (2,957,019)

The Commission makes the following modifications to the remaining proposed adjustments:

Interest Expense

Cumberland Valley proposed an increase of \$542,308 to normalize the test-year interest expense. Cumberland Valley's proposed adjustment did not use the Commission's traditional approach to normalize test-year interest expense for long-term debt. Rather Cumberland Valley proposed that a projected seven-year interest rate of 2.17 percent quoted in mid-April by the Federal Financing Bank be used to determine its interest expense.²

Cumberland Valley states that its efforts to minimize interest costs on its long-term debt by taking advantage of a short-term loan program has resulted in an extremely low average interest cost of 0.88 percent for the test year. Cumberland Valley maintains that this interest rate will not last and will be increasing in the future. It also maintains that in times of low or high interest rates, using the Times Interest Earned Ratio ("TIER") approach to determine revenue requirements is not prudent.

² See Prepared Testimony of James R. Adkins ("Adkins Testimony"), Exhibit H, p. 5 of 16. The testimony proposed an interest rate of 2.17 be used to determine the interest expense adjustment. However, Cumberland Valley's adjustment is based on an average rate of 2.094 percent. See also Exhibit 5 of the Application, and Response to Staff's Second Request, Item 28.d.

The AG recommends that the Commission continue to use its traditional approach to determine Cumberland Valley's interest adjustment. The AG states that until Cumberland Valley locks into a higher interest rate for its long-term debt, the ratepayers should not have to pay a rate higher than the rate Cumberland Valley currently enjoys. The AG also maintains that Cumberland Valley's argument that rates will continue to rise is not supported by fact in that Cumberland Valley has been quoted a rate as low as 1.98 percent since the application was filed. He also states that Cumberland Valley has not met its burden of proof to show that the increased interest rate it proposes is fair, just, and reasonable.

The Commission agrees with the AG that it is not appropriate in the context of a historical test-year rate case to use an interest rate based on a quoted rate that Cumberland Valley is not currently paying. Cumberland Valley could have filed this case using a forecasted test year in order to provide for expected increases in interest rates that it believes are likely. However, Cumberland Valley chose not to utilize that option.

The Commission recognizes that determining the interest adjustment using its traditional approach while establishing the revenue requirement based on a 2.0 TIER may not provide Cumberland Valley the revenue necessary to meet its mortgage requirements and cover its operating costs. Therefore, the Commission will utilize a five-year-average interest rate approach based on the actual average interest rate Cumberland Valley experienced for the five year period 2009 through 2013 of 1.34 percent.³ This departure from our traditional approach is based on the unique situation

³ Application, Exhibit H, Adkins Testimony, p. 3 of 16.

in which Cumberland Valley finds itself. Absent a comparable situation arising in the future, the Commission's belief is that its traditional approach for determining interest expense is the appropriate method to be used in future proceedings.

The Commission has recalculated the test-year interest expense using the test-year-end debt balances at a five-year interest rate of 1.34 percent and has decreased the interest expense adjustment from \$542,308 to \$219,353. The Commission commends Cumberland Valley's efforts to minimize its interest costs on long-term debt, thereby benefitting its customers.

Wages and Salaries

Cumberland Valley proposed an adjustment of \$62,741 to normalize total wages and salaries, of which \$21,986 was capitalized⁴ and \$40,755 was expensed. Cumberland Valley's calculations for full-time employees were based on 2,080 hours. Its calculations for its part-time employees were based on the number of hours actually worked during the test year. Test-year actual overtime hours were multiplied by 1.5 times the test-year-end wage rates for employees who come under the current labor agreement.⁵

In calculating its proposed adjustment, Cumberland Valley included a retired employee's wages. In its response to a Commission Staff's information request, Cumberland Valley agreed that the employee's wages should be removed for

⁴The capitalized portion reflects actual capitalized costs and payroll costs allocated to "payroll other." The payroll other includes amounts assigned to clearing accounts and accounts receivable. Unless otherwise noted, references in this Order to "capitalized" reflect this combination of actual capitalized costs and other costs.

⁵ Application, Exhibit 2.

ratemaking purposes.⁶ The Commission recalculated the proposed adjustment excluding the retired employee's wages, resulting in a total adjustment of \$20,437, of which \$7,161 was capitalized and \$13,276 was expensed. Accordingly, the Commission finds that an adjustment to increase test-year wages and salaries by \$13,276 is reasonable.

The AG expressed concern with what he described as Cumberland Valley's continuous and systematic salary and wage increases, even though the overall economy of its service territory is in decline. He states that, based on actual increases from 2008 through 2013, plus expected wage and salary increases for 2014 and 2015, Cumberland Valley will have granted pay raises to all employees totaling 26.5 percent increase. The AG believes there is an inherent problem for Cumberland Valley's CEO to negotiate pay raises with the union employees and then, along with the Board of Directors, grant the same increase to salaried employees, including himself. The AG claims there is no incentive for the CEO and Board of Directors to limit pay increases if the CEO and other salaried employees will receive the same benefit. The AG also cites merit increases in the test year and other increases to certain employees (including the CEO of \$5,000), in addition to the annual percentage increases. The AG is concerned that Cumberland Valley does not base its pay increases on the prevailing wages of its service territory, but compares itself to other Kentucky cooperatives in establishing its wage structure. The AG recommends that Cumberland Valley conduct a salary and wage survey in the counties which it serves to justify wage and salary increases. The AG also recommends that Cumberland Valley implement a performance review system on which to base future pay increases. Cumberland Valley stated that it bases its pay

⁶ Response to Staff's Second Request, Item 26.d.

structure on what other Kentucky cooperatives pay for similar jobs in order to retain an experienced workforce.

The Commission shares the AG's concern that there seems to be an inherent problem with Cumberland Valley's method for determining pay increases for salaried employees. While there is evidence that increases for bargaining-unit employees are properly determined through negotiations by both sides, there seems to be the expectation that whatever pay increase is granted to union employees will automatically be granted to the salaried employees. The Commission believes that any pay increase for salaried employees needs to be properly justified and not simply based on the increase negotiated for union employees. The Commission will allow the increases proposed in this case, but future increases granted to or proposed for salaried employees will need to be fully justified and documented to show the basis for any proposed increases.

Payroll Taxes

Cumberland Valley proposed to increase its payroll taxes by \$4,017,⁷ based on the proposed normalization of wages and salaries and reflecting the Federal Insurance Contribution Act ("FICA") base wage limit of \$117,000 for 2014, and federal and state unemployment wage limits and rates in effect at the test-year end. Of this amount, \$1,325 was capitalized and \$2,692 was expensed.⁸

As with the wage and salary normalization, the Commission finds that the impact of the retired employee's payroll taxes should be removed. The Commission has

⁷ Response to Commission Staff's First Request for Information ("Staff's First Request"), Item 23.a.

⁸ Application, Exhibit 3, and Response to Staff's First Request, Item 23.a.

recalculated the proposed adjustment excluding the retired employee's wages, resulting in a total adjustment of \$618, of which \$204 is capitalized and \$414 is expensed. Accordingly, the Commission finds that an adjustment to increase test-year payroll taxes by \$414 is reasonable.

Depreciation

Cumberland Valley depreciates its distribution plant using varying rates that have been in effect since December 31, 1990. Cumberland Valley proposed an adjustment to increase test-year depreciation expense by \$262,207. The proposed adjustment was due to a change in the depreciation rate for meters and increases in Cumberland Valley's utility plant in service over the course of the test year.

The depreciation adjustment was not supported by a current depreciation study. Cumberland Valley filed its previous study conducted as of December 31, 2004. In response to an information request questioning why a new depreciation study had not been conducted, Cumberland Valley stated that it had expected its financial situation to improve so that a rate application would not be necessary. However, its financial condition did not improve, Cumberland Valley stated, thus requiring this rate application to be filed, and there was not enough time to update its last study.⁹ Cumberland Valley stated that the change in the Meters depreciation rate from 3.23 percent to 6.70 percent is due to the implementation of Automated Metering Infrastructure ("AMI"), and is consistent with the rate applications filed by other electric cooperatives since 2001.¹⁰

⁹ Response to Staff's Second Request, Item 25.a.

¹⁰ *Id.*, Item 27.b.

Cumberland Valley's meters are recorded in the following accounts:¹¹

Account No. 370.0	Meters	\$2,211,882
Account No. 370.1	Turtle 1	\$ 139,455
Account No. 370.11	Turtle 2	\$3,637,953
Account No. 370.12	Meter w/Disconnect Switch	\$ 370,201
Account No. 370.15	Remote Service Switches	<u>\$ 371,337</u>
	Total Meters	\$6,730,828

Cumberland Valley stated that it had added AMI modules to its existing meters (which are recorded in Account No. 370.0, Meters), 16,436 of which were mechanical and 11,943 of which were solid state meters.¹² The existing meters are currently being depreciated using a useful life of 31 years. While the Commission has accepted a shorter life of 15 years for newer technology meters such as AMI, it does not find that the life of existing meters will be shortened by the addition of an AMI module.

Accordingly, the Commission has prorated the cost of the meters in Account 370.0 based on the number of mechanical and solid state meters provided by Cumberland Valley, resulting in \$1,281,035 assigned to mechanical meters and \$930,847 assigned to solid state meters. The Commission finds that the mechanical meters recorded in Account No. 370.0, Meters should continue to be depreciated at 3.23 percent or 31 years. The Commission also finds that it is reasonable that the solid state meters in Account 370.0, Meters should be depreciated at 6.70 percent or 15 years. The Commission also finds that Account Nos. 370.1, 370.11, 370.12 and 370.15 should be depreciated at a rate of 6.70 percent or 15 years. Therefore, the Commission will reduce the proposed depreciation adjustment by \$44,448 to \$217,759.

¹¹ Application, Exhibit Y, p. 3 of 6.

¹² Response to Commission Staff's Third Request for Information ("Staff's Third Request"), Item 7.b.

Rate Case Expense

Cumberland Valley estimated its rate case expense at \$75,000. It proposed to recover this expense through a three-year amortization. This estimate did not include in-house labor. Throughout this proceeding, Cumberland Valley has been providing updates of the actual expenses incurred in presenting this rate case. As of November 5, 2014, Cumberland Valley had expended \$100,159 to prepare and process this rate case. The Commission finds that a three-year amortization of these expenses is reasonable and will allow an increase in operating expense of \$33,386 to reflect the first year of the amortization for ratemaking purposes.

Directors' Fees and Expenses

During the test year Cumberland Valley paid its seven active directors and two retired directors fees and expenses totaling \$201,020. Cumberland Valley proposed an adjustment to reduce this expense by \$111,074 to exclude certain expenses for ratemaking purposes.¹³ The Commission agrees with the exclusions identified by Cumberland Valley.

The Commission has identified an additional adjustment that should be made to the directors' fees and expenses. Based on information provided,¹⁴ a director attending the annual meeting of the National Rural Electric Cooperative Association ("NRECA") did not attend any director training opportunity. Therefore, the cost of this director's attendance will be disallowed, as he was not the designated representative

¹³ Application, Exhibit 10. The \$111,074 adjustment comprised health insurance premiums and stipends, per diems, meeting fees paid to retired directors, and Christmas gifts.

¹⁴ Application, Exhibit 10, and Response to Commission Staff's Fourth Request for Information, Item 7.

to NRECA. The Commission will adjust the director fees and expenses by an additional \$2,052. Based on these findings, the Commission has reduced Cumberland Valley's operating expenses by \$113,126.

Property Taxes

Cumberland Valley did not include an adjustment for property taxes in the detailed schedule of adjustments filed with the application. However in response to an information request, Cumberland Valley provided an adjustment amount of \$55,027 to normalize property taxes for the test year.¹⁵ The Commission agrees with Cumberland Valley's response to the information request and finds that the property taxes should be increased by an additional \$55,027.

Amortization of Management Audit Expense

In Case No. 2005-00187,¹⁶ the Commission ordered a focused management audit of Cumberland Valley's operations. Cumberland Valley was to defer the costs of the management audit for recovery in its next general rate case. Cumberland Valley did not propose any adjustment in this case for the management audit, citing an oversight on its part. Through discovery it was determined that Cumberland Valley had expensed the full amount of the audit's cost of \$72,367 in 2007.¹⁷ Cumberland Valley stated that the audit's cost should not be amortized and be considered as an increase in expense for the test year.¹⁸ The Commission does not agree that the full amount of \$72,367

¹⁵ Response to Staff's First Request, Item 24.

¹⁶ Case No. 2005-00187, *Adjustment of Rates of Cumberland Valley Electric, Inc.* (Ky. PSC June 2, 2006).

¹⁷ Response to Staff's Second Request, Item 44.a.

¹⁸ Response to Staff's Third Request, Item 19.

should be allowed as a test-year expense. Accordingly, consistent with Commission practice in rate proceedings involving management audit fees, the Commission will allow the management audit expense of \$72,367 to be amortized over three years for ratemaking purposes only. The Commission will therefore adjust test-year expense by an additional \$24,122.

Miscellaneous Expenses

Cumberland Valley proposed to reduce operating expenses by \$2,365 to remove certain miscellaneous expenses not normally included for ratemaking purposes. The Commission agrees with the reductions proposed by Cumberland Valley.

The AG recommended that adjustments be made to Cumberland Valley's annual meeting expense for food and drinks, a singer, entertainment and buckets and bulbs should be removed for ratemaking purposes. The AG stated that Cumberland Valley had failed to demonstrate that the expenditures provided a material benefit for ratepayers or that they were otherwise reasonable.

The Commission notes that most cooperatives are required to hold an annual meeting according to their by-laws. A cooperative's annual meeting is held for the benefit of the members to inform them of the current status of the cooperative, issues to be addressed affecting cooperative operations, and election of the board of directors. The Commission has allowed these types of expenses in previous cooperative rate proceedings as necessary and reasonable to encourage attendance and participation by the cooperative's members.

Although not accepting the AG's recommendation, the Commission has identified three additional adjustments that should be made. Miscellaneous expenses included an

expenditure of \$1,551 for shirts for Cumberland Valley employees to wear while working at the annual meeting. Cumberland Valley stated that shirts are provided for employees working at cooperative functions to better identify the employees to its members. The Commission believes that there are much less expensive alternatives for identifying cooperative employees (i.e., name tags or badges) than incurring an expenditure of this magnitude. The Commission believes these funds should be expended in a manner that provides a greater benefit to the ratepayers. Accordingly, the Commission will remove \$1,551 from miscellaneous expenses.

Included in test-year miscellaneous expenses was \$250 for a payment to the Boy Scouts of America for presenting the flag at the annual meeting. Cumberland Valley was unable to provide any evidence in the form of an invoice or any other document that the payment was a fee and not a donation. Cumberland Valley stated that the amount of \$250 was determined as a reasonable amount for the flag presentation. Absent any documentation to the contrary, the Commission believes this payment is more in line with a donation and will remove it from the test-year expense.

Miscellaneous expense also included an expenditure of \$500 for advertising in the programs for the Border Bowl football game and sponsorship of the Border Bowl Lineman Award. The Commission believes this to be institutional advertising that should be disallowed. Additionally, it has been the Commission's practice to disallow sponsorships and awards in other rate proceedings.

Adding these additional items to Cumberland Valley's adjustment of \$2,365, the Commission has reduced miscellaneous expenses by a total of \$4,666.

PSC Assessment

Cumberland Valley did not propose an adjustment to its PSC Assessment to reflect the effects of normalizing revenues and purchased power expense or the impact of its proposed revenue increase. The Commission has determined that an adjustment to the PSC Assessment to reflect the normalization of revenue and purchased power expense found reasonable herein is appropriate. Based on the 2014–2015 assessment rate, the adjustment results in a \$494 increase in the PSC Assessment for the test year. The Commission has determined that an adjustment to the PSC Assessment based on the revenue increase being granted herein should also be calculated. This calculation results in an increase in the PSC Assessment Fee of \$1,886. The total result of these adjustments is an increase of \$2,380 in the PSC Assessment Fee.

Customer Growth Adjustment

Cumberland Valley proposed a negative customer growth adjustment of \$44,894.¹⁹ In response to a Staff information request, Cumberland Valley determined its proposed adjustment was incorrect and filed a revised calculation.²⁰ The revised amount of the adjustment is negative \$24,812. The Commission has reviewed the revised calculation and finds it to be reasonable. Therefore, we will accept the customer growth adjustment, as modified by Cumberland Valley, which results in an overall decrease in margins of \$24,812.

¹⁹ Application, Exhibit 16.

²⁰ Response to Staff's Second Request, Item 36.

Pole Attachment Rates

Cumberland Valley proposed increases in its cable television ("CATV") attachment charges that resulted in additional revenues of \$23,512. In response to requests for information, Cumberland Valley revised its CATV rates to reflect errors in the calculation. Cumberland Valley had included 45-foot poles in its calculation of the average cost of two-party poles. Further, through discovery it was determined that Cumberland Valley failed to subtract the cost of ground wiring to arrive at a bare-pole cost for the calculation. The Commission has reviewed the revised calculation to determine CATV rates and finds it to be reasonable and consistent with the methodology set forth by the Commission in Administrative Case No. 251.²¹ However, the Commission believes that the CATV rate calculations should reflect the most current rate of return. Therefore, the Commission finds that Cumberland Valley's CATV rates should be calculated based on the rate of return approved in this Order, resulting in an increase in revenues of \$12,484, rather than the increase of \$23,512 proposed by Cumberland Valley. This results in proposed CATV revenues being decreased by \$11,028.

²¹ Administrative Case No. 251, *The Adoption of a Standard Methodology for Establishing Rates for CATV Pole Attachments* (Ky. PSC Sept. 17, 1982).

Pro Forma Adjustments Summary

The effect of the pro forma adjustments on Cumberland Valley's net income is as follows:

	<u>Actual Test Period</u>	<u>Pro Forma Adjustments</u>	<u>Adjusted Test Period</u>
Operating Revenues	\$46,665,845	\$ (4,371,163)	\$42,294,682
Operating Expenses	<u>46,410,119</u>	<u>(4,123,378)</u>	<u>42,286,741</u>
Net Operating Income	255,726	(247,785)	7,941
Interest on Long-Term Debt	354,342	219,353	573,695
Interest Expense-Other	3,176		3,176
Other Income and (Deductions) – Net	<u>3,133,648</u>	<u>(2,957,019)</u>	<u>176,629</u>
NET INCOME	<u>\$ 3,031,856</u>	<u>\$ (3,424,157)</u>	<u>\$ (392,301)</u>

REVENUE REQUIREMENTS

The actual rate of return earned on Cumberland Valley's net investment rate base established for the test year was 0.67 percent.²² Cumberland Valley requests rates that would result in a TIER excluding GTCCs of 2.00X and a rate of return of 2.81 percent on its proposed rate base of \$63,885,540.²³ Cumberland Valley proposes an increase in revenues of \$1,605,137 to achieve the 2.00X TIER excluding GTCCs.²⁴

Cumberland Valley's actual TIER excluding GTCCs for the test period was 1.21X. For the calendar years 2011 and 2012, it was 1.26X and 3.20X, respectively. After taking into consideration pro forma adjustments, Cumberland Valley would achieve a 0.32X TIER excluding GTCCs without an increase in revenues.

²² Application, Exhibit K, p. 1 of 9.

²³ Response to Staff's Second Request, Item 6, p. 3 of 11.

²⁴ Cumberland Valley's proposal was based on its proposed adjusted-interest expense on long-term debt of \$896,650.

The Commission finds that the use of a 2.00X TIER is reasonable for Cumberland Valley. In order to achieve the 2.00X TIER based on the adjusted test year with interest on long-term debt of \$573,695, Cumberland Valley would need to increase its annual revenues by \$967,882.

Based upon the pro forma adjustments found reasonable, the Commission has determined that an increase in Cumberland Valley's revenues of \$967,882 would result in a TIER of 2.00X. This additional revenue should produce net income of \$573,695, which should allow Cumberland Valley to meet its mortgage requirements and service its mortgage debts.

PRICING AND TARIFF ISSUES

Cost of Service

Cumberland Valley filed a fully allocated cost-of-service study ("COSS") in order to determine the cost to serve each customer class and the amount of revenue to be allocated to each customer class. Cumberland Valley filed revised COSSs in response to Staff's second, third, and fourth requests for information. Having reviewed Cumberland Valley's COSS, as revised through discovery, the Commission finds it to be acceptable for use as a guide in allocating the revenue increase granted herein.

Revenue Allocation

The approved increase of \$967,882 results in an overall increase of 2.4 percent in base rate revenue. This is approximately 60 percent of the increase Cumberland Valley requested in its application. As discussed above, Cumberland Valley's proposed increases to the various rate classes were based on its COSS results. The Commission has reviewed Cumberland Valley's allocation proposal and finds it to be reasonable;

however, given the reduction in the increase granted, the Commission finds that no increase to the demand charge will be allocated to Schedule IV-A – Large Power, 50–2,500 kW. With that exception, the \$967,882 increase will be allocated in proportion to the increase proposed by Cumberland Valley.

Rate Design

Cumberland Valley proposes to allocate the proposed increase to its customer classes mainly by increasing the customer charges. For three of its customer classes, Three Phase Schools & Churches, Large Power >2,500 kW, and Large Power 50–2,500 kW, Cumberland Valley proposes to establish a customer charge. Currently, these three classes do not include a customer charge component. Cumberland Valley's COSS shows that the current customer charges for each of its rate classes are insufficient to recover the customer-related costs of serving those classes.

Cumberland Valley proposed changing its kilowatt hour ("kWh") charge only for one class, its Large Power >2,500 kW class, and proposed changing its demand charge for only one class, its Large Power 50–2,500 kW class. For the lighting class, Cumberland Valley proposed an average increase of 6.4 percent.

The AG proposes that any increase should be to the volumetric charge for energy, rather than the customer charge. He argues that by placing a large proportion of the increase on the customer charge, customers have less control over their bills, and that financial risk is shifted from Cumberland Valley to its ratepayers.

With respect to the proposed increases in Cumberland Valley's customer charges, the Commission concludes that, for an electric cooperative that is strictly a distribution utility, there is merit to the argument that there is need for a means to guard

against the revenue erosion that often occurs due to the decrease in sales volumes that accompanies poor regional economics, changes in weather patterns, and the implementation or expansion of demand-side management and energy-efficiency programs. For this reason, and based on the results of the COSS, the Commission has placed the majority of the increase on the class customer charges.

The allocation of the increase granted to Cumberland Valley generally follows the methodology Cumberland Valley proposed to allocate its increase to its individual customer classes. The allocation of revenues to the customer classes and the increases in customer charges for the most part reflect the results of Cumberland Valley's revised COSS.

The chart below provides a comparison of Cumberland Valley's current customer charges, along with its proposed increase, and the rates approved by the Commission:

<u>Rates Class</u>	<u>Current Customer Charge</u>	<u>Proposed Customer Charge</u>	<u>Approved Customer Charge</u>
Schedule I – Residential, Schools and Churches	\$5.74	\$10.70	\$8.73
Schedule II – Small Commercial No Demand	\$5.74	\$11.04	\$8.96
Schedule II – Small Commercial w/ Demand	\$5.74	\$11.04	\$8.96
Schedule III – Three Phase Schools and Churches	\$0.00	\$40.00	\$25.00
Schedule IV – Large Power > 2500	\$0.00	\$50.00	\$50.00
Schedule IV-A – Large Power 50- 2500	\$0.00	\$40.00	\$40.00

Because the implementation of a customer charge on the Schedule IV – Large Power > 2,500 kW class did not fully allocate its proportionate share of the revenue requirement increase, a slight increase was made to the energy charge for this class. Demand charges were left unchanged for all classes with a demand charge. Allocating the lighting class's share of the revenue increase yields an approximate 3.88 percent increase for each of the lights.

Based on Cumberland Valley's average residential usage of 1,146 kWh, the average bill for residential customers will increase \$2.99 from \$103.87 to \$106.86, or 2.88 percent.

OTHER ISSUES

Energy Efficiency and Demand-Side Management ("DSM")

In response to requests for information,²⁵ and testimony at the public hearing, Cumberland Valley stated that it offers its customers DSM programs in conjunction with programs offered by EKPC. Cumberland Valley also stated that it is open to offering DSM programs independent of EKPC if the program is beneficial to the members and the cooperative.

The Commission continues to believe that conservation, energy efficiency and DSM, generally, will become increasingly important as more constraints are likely to be placed upon utilities whose main source of supply is coal-based generation. As we have previously stated, the Governor's proposed energy plan, *Intelligent Energy Choices for Kentucky's Future, November 2008*, calls for an increase in DSM by 2025. In addition, the Commission has stated its support for cost-effective DSM programs in response to several recommendations included in *Electric Utility Regulation and Energy Policy in Kentucky*, the report the Commission submitted in July 2008 to the Kentucky General Assembly pursuant to Section 50 of the 2007 Energy Act.

The Commission recognizes Cumberland Valley's efforts regarding DSM program offerings but believes that it is appropriate to continue to encourage

²⁵ Response to Staff's Second Request, Item 43.

Cumberland Valley and all other electric providers to expand their efforts to offer cost-effective DSM and other energy-efficiency programs.

SUMMARY

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

1. The rates set forth in Appendix A are the fair, just, and reasonable rates for Cumberland Valley to charge for service rendered on and after the date of this order.
2. The rate of return and TIER granted herein will provide for Cumberland Valley's financial obligations.

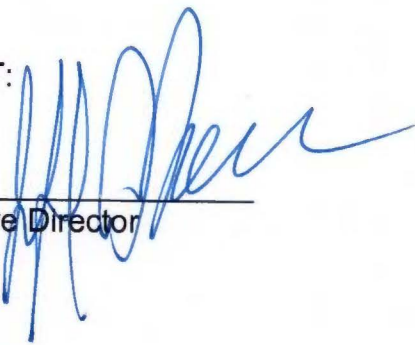
IT IS THEREFORE ORDERED that:

1. The rates proposed by Cumberland Valley would produce revenues in excess of the amount found reasonable herein and are hereby denied.
2. The rates set forth in the Appendix to this Order are approved for services rendered by Cumberland Valley on and after the date of this Order.
3. Within 20 days of the date of this Order, Cumberland Valley shall file with this 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.
4. Cumberland Valley shall perform a depreciation study within five years from the date of this Order, or in connection with the filing of its next rate case, whichever is earlier.

By the Commission

ENTERED
JAN 16 2015
KENTUCKY PUBLIC
SERVICE COMMISSION

ATTEST:



Executive Director

APPENDIX

APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE COMMISSION IN CASE NO. 2014-00159 DATED **JAN 16 2015**

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

SCHEDULE I RESIDENTIAL, SCHOOLS, AND CHURCHES

Customer Charge	\$ 8.73
Energy Charge per kWh	\$.08563

SCHEDULE I MARKETING RATE

Energy Charge per kWh	\$.05138
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SCHEDULE II SMALL COMMERCIAL NO DEMAND

Customer Charge	\$ 8.96
Energy Charge per kWh up to 3,000 kWh	\$.09519
Energy Charge per kWh over 3,000 kWh	\$.0888

SCHEDULE II SMALL COMMERCIAL w/ DEMAND

Customer Charge	\$ 8.96
Demand Charge per kW	\$ 4.22
Energy Charge per kWh up to 3,000 kWh	\$.09519
Energy Charge per kWh over 3,000 kWh	\$.0888

SCHEDULE III THREE PHASE SCHOOLS AND CHURCHES

Customer Charge	\$ 25.00
Energy Charge per kWh	\$.07915

SCHEDULE IV
LARGE POWER >2,500 KW

Customer Charge	\$ 50.00
Demand Charge per kW	\$ 6.55
Energy Charge per kWh	\$.05112

SCHEDULE IV-A
LARGE POWER 50-2,500 KW

Customer Charge	\$ 40.00
Demand Charge per kW	\$ 4.22
Energy Charge per kWh	\$.06078

SCHEDULE VI
OUTDOOR LIGHTING

175W Mercury Vapor	\$ 8.57
400W Mercury Vapor	\$ 12.76
100W Open Bottom	\$ 8.59
100W Colonial Post	\$ 9.68
100W Directional Flood	\$ 10.42
400W Directional Flood	\$ 16.57
400W Cobra Head	\$ 16.57

Cable Television Attachment Charges

Annual attachment charges as follows:

Two-party Pole	\$ 4.26
Three-party Pole	\$ 3.53
Two-party Anchor	\$ 4.05
Three-party Anchor	\$ 2.67
Two-party Ground	\$.19
Three-party Ground	\$.12

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