

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

GENERAL ADJUSTMENTS IN ELECTRIC)
AND GAS RATES OF LOUISVILLE GAS) CASE NO. 8284
AND ELECTRIC COMPANY)

ORDER ON REHEARING

On January 4, 1982, the Commission issued its Order granting the Louisville Gas and Electric Company ("LG&E") approximately \$34.1 million in additional revenue from its electric and gas customers on an annual basis. On January 22, 1982, LG&E filed a petition for rehearing of the Commission's Order, alleging six "points" in support of its claim that further consideration of this case was necessary. On January 25, 1982, LG&E's senior vice president submitted a letter to the Commission concerning the finding regarding the accounting treatment accorded profits on sales of gas from storage. The Commission will treat this letter as a part of LG&E's petition for rehearing.

On January 29, 1982, the Attorney General, through its Consumer Protection Division, filed a response in opposition to the granting of rehearing in this case. Jefferson County and the City of Louisville filed their joint response in opposition to rehearing on February 1, 1982.

LG&E prefaces its petition for rehearing by informing the Commission that the purpose of a petition for rehearing is to give this agency the "opportunity to right wrongs and to correct deficiencies," and that LG&E assumes that its petition will receive "careful and thoughtful consideration." 1/ The Commission is in absolute agreement with LG&E as to the purpose of a petition for rehearing, and we further assure it that every pleading submitted to this agency receives careful and thoughtful consideration before any action is taken thereon.

The first point raised by LG&E in support of rehearing is that the Commission misinterpreted the cost of money evidence presented by the various witnesses for LG&E and the intervenors. 2/ The Commission's Order of January 4, 1982, may not have been as explicit as it should have been on this issue, hence LG&E's confusion on this point. We will, accordingly, address in more detail the evidence relied upon in support of the finding regarding a fair, just and reasonable return on equity for LG&E.

All three of the rate of return witnesses included in their cost of money recommendations an allowance for the costs associated with the issuance of new shares of common stock: market price fluctuations at the time of issuance, market pressure due

1/ LG&E's Petition for Rehearing (hereafter "Petition"), p. 2.

2/ Id. at pp. 2 - 5.

to issuance, and actual stock issuance or flotation costs. 3/ On page 14 of the Order, we cited each witness' preliminary cost of money estimate, i.e., before adjustment for issuance costs, as taken from each witness' direct testimony. 4/ The apparent basis for LG&E's confusion on this issue stems from the Commission's characterization of these preliminary cost of money estimates as the "cost of common equity," while terming the witnesses' final recommendations as "recommended rate of return." 5/ The Commission concedes that none of the witnesses actually used the same terminology as we did when reviewing their testimony in the text of the Order. However, the Commission believed that a company such as LG&E would understand our terminology from the context of the Order.

Lest there be any further misunderstanding regarding the evidence the Commission relied upon in determining that 15.5 percent was the fair, just and reasonable rate of return on common equity, the Commission emphasizes that the 14.5 to 16.0 percent range of returns on common equity found to be fair, just and reasonable is the same range as the preliminary cost of equity

3/ Brigham prefiled testimony, pp. 48-49; Weaver prefiled testimony, p. 55; and Loconto prefiled testimony, pp. 27-28.

4/ Brigham prefiled testimony, pp. 48-49; Weaver prefiled testimony, p. 55; and Loconto prefiled testimony, pp. 22 and 27.

5/ January 4, 1982, Order (hereafter "Order"), p. 14.

estimates put forward by the intervenors' witnesses. 6/ Thus there was clearly evidence to support a 14.5 percent return on equity if the Commission had so chosen because, as we stated in our Order, the Commission is not convinced that allowing a rate of return greater than the cost of common equity (i.e., the "preliminary" cost of equity) is appropriate. Nevertheless, the Commission pointed out that a return on equity of 15.5 percent would fully cover whatever additional "costs" might arguably be incurred by the issuance of new shares of common stock. 8/ Moreover, even if the Commission were to agree that "issuance costs" were a proper factor in determining a return on equity, and if we accepted LG&E's own testimony that this additional cost should be .6 percent, 9/ then the new range the Commission finds fair, just and reasonable would be 15.1 percent to 16.6 percent. Again, our original determination that 15.5 percent is the proper return on equity is supported by the evidence in this record.

LG&E objects to the consideration by the Commission of current economic conditions in determining the fair, just and reasonable return on equity. 10/ The hearings in this case

6/ Weaver prefiled testimony, p. 55; Loconto prefiled testimony, pp. 22 - 27.

7/ Order, p. 15.

8/ Order, p. 15.

9/ Order, p. 14; Brigham prefiled testimony, p. 49.

10/ Petition, p. 5.

were held on November 4 and November 12, 1981. Our Order was issued on January 4, 1982. During this post-hearing interval the Commission reviewed information of public record regarding the condition of the financial markets in general and LG&E's financial well-being in particular as determined through information distributed by various financial reporting services. 11/ For example, it was common knowledge, and hence noticeable by the Commission, that the prime interest rate had declined from 17 percent to 15 3/4 percent from the time of the last hearing to the date of the Order's issuance. 12/

Finally, LG&E makes reference to a "puzzling inconsistency between the Commission's recent award to another utility and its inexplicably lower award to the Company herein." 13/ We do not know to which of the 567 utilities we regulate LG&E refers, nor is it relevant. The Supreme Court of the United States long ago rejected the notion that utility rate regulation should be based on comparisons among companies:

There is no particular rate of compensation which must, in all cases and in all parts of the country, be regarded as sufficient for capital invested in

11/ Such as Federal Reserve Bulletins and Moody's Investors Services Public Utility News Reports.

12/ Wall Street Journal, November 11, 1981, p. 40; Wall Street Journal, December 30, 1981, p. 15.

13/ Petition, p. 5.

business enterprises. Such compensation must depend greatly upon circumstances and locality. 14/

Points two and three of LG&E's petition for rehearing contest the Commission's rejection of the electric temperature adjustment LG&E proposed. In support of its position on this issue, LG&E submitted the affidavit of its employee, James W. Kasey, which was made at the request of LG&E counsel to provide "one place in the record which contrasts facts in the record with statements made by the Commission." 15/ The affidavit purported to identify areas where the record supports the weather normalization adjustment proposed by LG&E.

The first issue in the affidavit addressed the statement in the Order that "there was no support for the selection of the month used to determine the base non-cooling load." 16/ LG&E cited Thurman Exhibit 1, page 2 of 4, part II, and the response to staff data request No. 15 Electric, pages 4 to 9. The only substantive statement contained therein concerning the selection of the month of May to determine the base non-cooling load is that "...May is the month prior to the cooling season with very few cooling degree days and usage could not have been substantially affected by furnace fan operation related

14/ Wilcox v. Consolidated Gas Company, 212 U.S. 19, 53 L. Ed 382, 398 (1909).

15/ Affidavit of James W. Kasey, attached to Petition, p.1.

16/ Order, p. 8.

to space heating requirements." 17/ LG&E offered no evidence that the usage in this month was any more representative of the base non-cooling load than usage in the months of November through April, nor did it address the impact on the adjustment of using a base load other than that established in the month of May. The Commission agrees that the evidence of record explains to a limited extent the selection of the month of May to determine the base non-cooling load, but it does not support a finding that this selection should be considered as controlling.

Statement number two of Mr. Kasey's affidavit argues that LG&E did not "establish" the 65 degree mean as the base point for determining cooling or heating degree days. The Commission agrees with LG&E on this point and we will, accordingly, modify the third grammatical sentence on page eight of our January 4, 1982, Order to read as follows: "LG&E also did not consider the effects of conservation on usage for air conditioning in adopting the 65 degree mean." Likewise, in response to Mr. Kasey's argument set forth in statement number three of his affidavit, the Commission will modify the second grammatical sentence on page eight of our January 4, 1982, Order to read as follows: "There was no support for the selection of the month used to determine

17/ Thurman prefiled testimony, Exhibit 2, p. 2 of 4, part II.

the base non-cooling load nor the use of the 30-year average normal degree days."

The fourth issue in the affidavit addresses our statement in the Order that "... in determining the dollar amount of the revenue and expense adjustments, LG&E did not justify the use of the revenue per kwh to adjust revenue and the average fuel cost to adjust expense." 18/ Mr. Kasey cites the location of data used to calculate the revenue and expense adjustments, but does not refute the inconsistency in using the average revenue per kwh to adjust revenue and incremental cost to adjust expense.

In the fifth issue raised in the affidavit, LG&E reminded the Commission that it had considered another measurable volume adjustment by adjusting sales based on year end customers. However, the Commission in its Order specified other factors which should be considered in normalizing sales that were not taken into consideration in the adjustment proposed by LG&E. LG&E does not argue that these other factors should not be considered in normalizing sales. Instead, it implies that one of these factors (i.e., industrial sales) cannot be measured. 19/ The Commission does not agree that the level of kwh sales can be more precisely predicted for the effects of weather on

18/ Order, p. 8.

19/ Petition, pp. 7 - 8.

residential sales than for the effects of the "business cycle" on industrial sales. 20/

The final issue relates to the statement in the Order concerning the volume of kwh sales for the 12 months ending October 1981. The Order clearly reflected that actual sales for given periods (which did not include the abnormal sales occurring in the summer of 1980) were not supportive of an adjustment based on an estimated differential of 314.7 million kwh.

The fourth point raised by LG&E in its petition is that the Commission "penalized" it for its efforts to protect the rate-payers by disallowing a portion of its strike-related expenses. The Commission's disallowance was by no means a signal to LG&E that it should in every instance "accede to the union's demands." 21/ Indeed, we commend LG&E for attempting to keep labor costs as reasonable as possible. The Commission's determination was founded on the basic ratemaking principle which dictates that costs which are extraordinary in nature and "cannot be reasonably expected to recur" 22/ should not be included in determining revenue requirements for a future period. The record reflects that LG&E had never had a labor strike in the past and includes no evidence to support a conclusion by the Commission that a strike might occur in the future.

20/ Petition, p. 7.

21/ Petition, p. 10.

22/ Order, p. 11.

The fifth point raised by LG&E concerns our denial of the expense related to its participation in the Louisville Development Committee. Upon cross examination at the hearing on November 4, 1981, the witness for LG&E Mr. Frank Wilkerson could not explain the nature of this expense to the Commission. Therefore, in the absence of any evidence regarding the possible benefits to the ratepayers resulting from the contribution, the Commission denied the expense for ratemaking purposes.

LG&E maintains that our denial of this expense will have a chilling effect on future participation by LG&E (and other similarly-situated utilities) in projects designed to improve the economic well-being of the community at large. LG&E argues that projects such as the Louisville Development Committee are designed to stimulate business and provide more jobs and that participation in them provides indirect benefits to its ratepayers by creating a healthier economic climate and thereby a better quality of life for all who live within its service area. The Commission on reconsideration agrees with LG&E's reasoning on this issue and will, accordingly, modify its Order to allow as a legitimate expense the \$11,250 contribution made to the Louisville Development Committee.

In LG&E's sixth and final point in support of its petition, it poses a series of rhetorical questions regarding the current state of judicial review of administrative orders in Kentucky in light of the Supreme Court's recent decision in Kentucky

Power Company v. Energy Regulatory Commission, 28 K.L.S. 15 (November 24, 1981). The clear implication of this legal tour de force is that if the Commission does not grant the petition, LG&E will see us in court. The Commission is well aware that Section 14 of the Constitution of Kentucky confers such right upon aggrieved parties to proceedings before the Commission.

Last, we will address the question raised by LG&E's senior vice-president regarding the accounting treatment of profits from its sales of gas from its storage facilities. We agree with LG&E that our finding section should be clarified. Accordingly, the language contained in the third paragraph on page 17 of our January 4, 1982, Order should be modified as noted in Finding Number 2.

The Commission finds that the amount of overall revenue deficiency LG&E is incurring is hereby amended to read \$34,153,658, instead of the \$34,142,409 stated in the January 4, 1982, Order. 23/ The effect of the allowance of the contribution to the Louisville Development Committee on LG&E's overall revenues is de minimis, and therefore the Commission will not change LG&E's allowed rates.

Based upon the analysis of the points presented by LG&E as set forth above, and being advised, the Commission hereby finds that:

23/ Order, p. 15.

1. The Commission's Order of January 4, 1982, should be modified to the extent that the contribution of LG&E to the Louisville Development Committee in the amount of \$11,250 should be allowed as an operating expense.

2. The third paragraph on page 17 of our Order of January 4, 1982, relating to the accounting treatment of profits from the sale of gas from storage facilities should be modified as follows:

The Commission is of the opinion that LG&E should be required to calculate profits on sales of gas from storage beginning with sales occurring on October 1, 1981. LG&E should maintain detailed records which show the amount for each month and the balance accumulated subsequent to the above date. We further find that a hearing should be held to allow LG&E and other interested parties to present testimony regarding profits on sales from storage.

3. Except for the modifications noted in Findings 1 and 2, the Petition for Rehearing of LG&E should be denied and the Commission's Order of January 4, 1982, should be affirmed.

IT IS THEREFORE ORDERED that the Commission's Order entered January 4, 1982, be and it hereby is modified in accordance with the findings herein and affirmed in all other respects.

Done at Frankfort, Kentucky, this 16th day of February, 1982.

By the Commission

ATTEST:

Secretary

1. The Commission's Order of January 4, 1982, should be modified to the extent that the contribution of LG&E to the Louisville Development Committee in the amount of \$11,250 should be allowed as an operating expense.

2. The third paragraph on page 17 of our Order of January 4, 1982, relating to the accounting treatment of profits from the sale of gas from storage facilities should be modified as follows:

The Commission is of the opinion that LG&E should be required to calculate profits on sales of gas from storage beginning with sales occurring on October 1, 1981. LG&E should maintain detailed records which show the amount for each month and the balance accumulated subsequent to the above date. We further find that a hearing should be held to allow LG&E and other interested parties to present testimony regarding profits on sales from storage.

3. Except for the modifications noted in Findings 1 and 2, the Petition for Rehearing of LG&E should be denied and the Commission's Order of January 4, 1982, should be affirmed.

IT IS THEREFORE ORDERED that the Commission's Order entered January 4, 1982, be and it hereby is modified in accordance with the findings herein and affirmed in all other respects.

Done at Frankfort, Kentucky, this 16th day of February, 1982.

PUBLIC SERVICE COMMISSION

Marlin M. Vohz
Chairman

ATTEST:

Katherine Gussall
Vice Chairman

Secretary

Ann Carrigan
Commissioner