COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

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In the Matter of:

GENERAL ADJUSTMENTS IN ELECTRIC RATES OF KENTUCKY POWER COMPANY) CASE NO. 8429

O R D E R

On July 8, 1982, Kentucky Power Company ("Kentucky Power") filed a petition for rehearing and a motion for oral argument in support of its petition for rehearing. The motion for an oral argument was granted by the Commission on July 23, 1982, and the Commission heard the oral argument of Kentucky Power and other parties of record on August 4, 1982.

In the petition for rehearing and oral argument, Kentucky Power addressed five areas in which it alleges the Commission either misunderstood Kentucky Power's position or reached erroneous conclusions on the record.

First, Kentucky Power argues that the Commission should have allowed the investment in Franklin Realty as a part of its capitalization. The Commission found in its Order that the uses of the property held in the name of Franklin Realty were speculative because property is not transferred to Kentucky Power until it is actually placed into service. Moreover, the investment in Franklin Realty, to the extent that the property has not been placed in service, is clearly non-utility property. The Commission is not convinced that the ratepayers of Kentucky Power realize any benefit from this arrangement. Kentucky Power argues that $171,167 of the investment in Franklin Realty is already in service. However, the Commission finds no evidence in the record which reflects when this property was placed in service or specifies the necessity of the property. The record reflects, and Kentucky Power acknowledges, that at the end of the test period this property was included in other investments. On rehearing, the Commission will consider any other references to specific information in the record regarding the $171,167 of property which Kentucky Power maintains should have been classified as plant in service. With regard to the other property held in the name of Franklin Realty the Commission hereby affirms its original decision.

The second issue raised by Kentucky Power is the Commission's decision to deny repricing of the coal inventory on hand at the end of the test period. The Commission is of the opinion that Kentucky Power should be allowed to present evidence on rehearing in support of its position that the entire 60-day coal inventory should be revalued at the October 1981 price and that the decision of the Commission in the last Kentucky Power case should be followed in this case. The Commission advises Kentucky Power that it has allowed no adjustment to the value of coal inventory in recent cases involving other electric utilities.

The third issue contested by Kentucky Power in its petition for rehearing was the provision of $9.4 million for production plant maintenance costs. Kentucky Power argues that the Commission was unfair in reducing the production plant maintenance costs below those which were actually experienced during the test period. Kentucky Power contends that the $9.4 million is not representative of its expected normal costs.

In its Order of June 18, 1982, the Commission allowed average production plant maintenance costs based on the past 3 years of actual cost. The record does not support either of the production plant maintenance figures proposed by Kentucky Power. Responses to inquiries about the derivation of the $10.4 million production plant maintenance costs produced no useful information. Furthermore, the record contains no evidence which would reflect that the actual costs incurred during the test period of $10,167,615 are normal or representative of the annual costs that could reasonably be expected to occur over a complete maintenance cycle.

The Commissioners and Commission staff have spent considerable time searching the record in this matter for evidence supporting the position taken by Kentucky Power on the issue of production plant maintenance. Kentucky Power's responses to several interrogatories and information requests of the Commission and the intervenors are incomplete, vague and "unresponsive." The Commission advises Kentucky Power to respond to, or seek clarification of, information requests in future rate cases.

In this case the Commission will allow Kentucky Power on rehearing to refer it to any information contained in the record or otherwise available to the Commission which supports its contention that:

1) The $10.4 million estimated annual production plant maintenance costs are based on sound forecasting techniques and reflect known and measurable costs for a future period.

2) The normalized production plant maintenance costs of $10.4 million are representative of expected future costs given the unique operating characteristics of Kentucky Power (only one generating station).

3) The actual production plant maintenance costs of $10,167,615 are normal based on the level of routine maintenance, cycle maintenance, and any extraordinary maintenance occurring in the test period.

The Commission reminds Kentucky Power that, should it wish to offer additional evidence, it must prove that such evidence could not have been offered with reasonable diligence during the course of these proceedings. KRS 278.400.

The fourth issue presented by Kentucky Power concerned the decision of the Commission to apply the overall rate of return to Construction Work in Progress in determining the appropriate level of Allowance for Funds Used During Construction ("AFUDC"). Kentucky Power has presented no compelling arguments in its petition for rehearing to persuade the Commission to modify its Order. Therefore, the Commission hereby affirms its original decision on this issue with the exception of the total AFUDC included in the determination of the revenue requirements. In the Order of June 18, 1982, on page 19, the Commission inadvertently included the total company AFUDC of $7,533,616 rather than the Kentucky jurisdictional component which should be $7,491,777. This understated the revenue deficiency by $41,839. Therefore, the Commission will modify its Order to provide additional revenue after the provision for state and federal income taxes of $82,669.

The fifth area in which Kentucky Power asserted error was rate of return on equity. Kentucky Power pointed out an error in the calculation of the before tax interest coverage ratios stated on page 24 of the Commission's Order of June 18, 1982. The before tax earnings figure used in the calculation was based on taxes reflecting fully incremental tax rates. However, the earnings before interest and taxes allowed in the Order were based on actual test year taxes, as adjusted. Therefore, the first paragraph on page 24 should be amended to read as follows:

> With the capital structure and debt costs approved in this Order, the range of returns on equity of 14.5 percent to 16 percent provides before tax interest coverage ratios of approximately 2.45 times to 2.64 times. These ratios are within the range acceptable for A-rated bonds. Therefore, the Commission is of the opinion that a return on equity in this range will maintain Kentucky Power's financial integrity and permit it to attract capital at reasonable costs.

As Kentucky Power presented no other facts or arguments not previously considered by the Commission, the motion for rehearing is denied on the issue of rate of return on equity.

IT IS THEREFORE ORDERED that the petition for rehearing on the first, second and third issues presented by Kentucky Power as set out herein is granted for the purposes specified in this Order.

IT IS FURTHER ORDERED that a hearing be and it hereby is scheduled for September 14, 1982, at the Commission's offices in Frankfort, Kentucky, at 10:00 a.m., Eastern Daylight Time.

IT IS FURTHER ORDERED that Kentucky Power shall provide references supporting its contentions on the issues of the investment in Franklin Realty and the production plant maintenance costs on or before September 3, 1982.

IT IS FURTHER ORDERED that subsequent to the rehearing, the Commission will order appropriate modifications to its June 18, 1982, Order, on the issues of AFUDC and return on equity based on the findings herein.

Done at Frankfort, Kentucky, this 25th day of August, 1982.

PUBLIC SERVICE COMMISSION

Marlin M. Volz
Chairman

Katherine Randall
Vice Chairman

Commissioner

ATTEST:

Secretary