

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

APPLICATION OF LOUISVILLE GAS AND)
ELECTRIC COMPANY FOR AN ORDER)
APPROVING CERTAIN ACCOUNTING) CASE NO. 89-030
TREATMENT OF AMOUNTS PAID FOR)
COAL CONTRACT TERMINATION)

O R D E R

On February 9, 1989, Louisville Gas and Electric Company ("LG&E") filed an application with the Public Service Commission ("Commission") seeking approval of its proposed method of accounting for a \$17.5 million payment to Peabody Coal Company ("Peabody"), as consideration for release from a 1966 coal supply agreement. LG&E proposes to amortize and recover the prepayment of fuel costs through the fuel adjustment clause ("FAC").

There was one intervenor in this case, the Utility and Rate Intervention Division of the Kentucky Attorney General's ("AG") office. A public hearing was held on June 6, 1989.

LG&E negotiated the early release from its Peabody contract which was not scheduled to terminate until December 31, 1990. In executing the release, LG&E paid Peabody \$17.5 million and entered into a 24-month fixed price contract for delivery of 1,700,000 tons per year beginning in January 1989.

The evidence presented by LG&E showed that by terminating the Peabody contract its customers will receive the benefits of lower current coal prices and anticipated lower future coal prices. LG&E estimated that the total fuel cost savings of the coal contract release is approximately \$33.7 million, for a net savings in fuel expense of approximately \$16.2 million after deducting the prepayment of \$17.5 million. The present value of the net savings was estimated to be \$14.6 million.

LG&E proposed to treat the \$17.5 million as a prepayment of fuel expense. It proposed to establish a deferred debit of \$17.5 million in Account No. 186, Deferred Debits. A portion of the \$17.5 million would be charged on a pro rata basis to Account No. 151, Fuel Stock, each month for inclusion in the monthly FAC calculation. LG&E proposed to amortize the \$17.5 million monthly, beginning from the date when the Commission issued an Order approving its application and continuing through December 31, 1990, the date when the Peabody contract would have otherwise terminated. LG&E stated that its customers would receive the benefits of reduced fuel costs throughout the remaining life of the contract, therefore, recovery of the buy-out costs over that same period would be reasonable and equitable.

The AG did not oppose LG&E's buy-out of the Peabody contract and did not object to LG&E's proposed accounting treatment for the recovery of the \$17.5 million.

LG&E's case is similar to the coal contract buy-out case decided by the Commission in Case No. 10214.¹ The \$17.5 million represents a prepayment of fuel costs for the purpose of obtaining a current and future reduction in fuel expense; the buy-out results in an immediate benefit to LG&E's customers which will continue through the remaining life of the contract; and denial of the proposed recovery would tend to discourage utilities from attempting to negotiate for lower rates and prices in existing contracts. Therefore, the Commission is of the opinion that LG&E's proposal to create a deferred debit in Account No. 186, Deferred Debits, and charge a portion of this amount to Account No. 151, Fuel Stock, should be approved. However, the Commission is of the opinion that the charging of the entire \$17.5 payment over the entire remaining life of the contract does not adequately reflect the fact that this buy-out is being made in two installments. The Commission is of the opinion that it is reasonable for the February 1, 1989 payment of \$8.5 million to be amortized, in equal amounts, over the months remaining in 1989 and the 12 months of 1990. The Commission is also of the opinion that the January 1, 1990 payment of \$9.0 million be amortized, in equal amounts, over the 12 months of 1990.

¹ Case No. 10214, Application of Kentucky Utilities Company for an Order Approving Certain Accounting Treatment of Amounts Paid for Coal Contract Release, interim Order issued October 1, 1988.

In approving recovery of costs associated with this particular contract buy-out, the Commission is not establishing a precedent whereby these type costs can automatically be passed through the FAC. Contract buy-outs differ in terms and circumstances. Such costs can be determined as appropriate for FAC recovery only after review of a formal application. Because of this difference in terms and circumstances, the Commission is of the opinion that all future applications of this type will require the submission of a detailed and fully documented present value analysis of the costs and savings of any buy-out proposal.

The Commission, having reviewed the evidence of record and being advised, is of the opinion and finds that:


1. The \$17.5 million paid by LG&E is in effect a prepayment of fuel costs to obtain current and future coal market price benefits for its customers and, therefore, the FAC regulation, 807 KAR 5:056, provides for the recovery of such a prepayment.

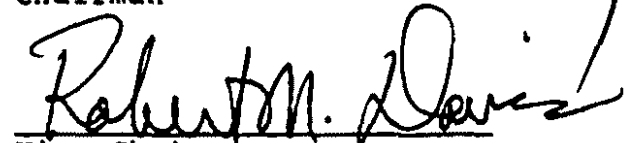
2. LG&E should amortize the prepayment for recovery through the FAC. The February 1, 1989 payment of \$8.5 million should be amortized over the months remaining in 1989 and the 12 months of 1990. The January 31, 1990 payment of \$9.0 million should be amortized for the period January through December 1990.

BE IT SO ORDERED.

Done at Frankfort, Kentucky, this 29th day of June, 1989.

PUBLIC SERVICE COMMISSION


Chairman


Vice Chairman


Commissioner

ATTEST:

Executive Director