

COMMONWEALTH OF KENTUCKY  
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

THE APPLICATION OF LOUISVILLE GAS AND	)	
ELECTRIC COMPANY FOR APPROVAL OF ITS	)	CASE NO.
2002 COMPLIANCE PLAN FOR RECOVERY BY	)	2002-00147
ENVIRONMENTAL SURCHARGE	)	

O R D E R

On March 24, 2003, the Commission issued an Order granting rehearing on the issue raised by Kentucky Industrial Utility Customers, Inc. ( KIUC ) of whether Louisville Gas and Electric Company s ( LG&E ) environmental surcharge revenue requirements should be reduced to reflect a decrease in labor expenses at the Mill Creek generating station. The March 24, 2003 Order included an initial rehearing data request and scheduled an informal conference for the purpose of developing a procedural schedule for the rehearing. The informal conference was held at the Commission s offices on April 4, 2003.

On April 16, 2003, the Commission issued an Order providing for supplemental responses to the initial rehearing data request and established May 1, 2003 as the last date for the parties to either submit written comments on LG&E s supplemental responses or request a hearing. On April 29, 2003, the Commission issued a second rehearing data request. Only one party filed comments and no party requested a hearing. In accordance with the April 16, 2003 Order, as no hearing was scheduled, this case stands submitted for decision based on the existing record.

## BACKGROUND

The 2003 Compliance Plan approved by the Commission in its February 11, 2003 Order included projects modifying the scrubber systems at the Mill Creek generating station. As a result of the scrubber modifications, four scrubber operator positions were eliminated at Mill Creek. However, LG&E reassigned the four employees to previously vacant non-environmental positions at Mill Creek. The Commission considered and rejected a proposal by KIUC to reduce the operating and maintenance ( O&M ) expense recovered in the environmental surcharge to reflect the elimination of the four environmental employees.

In the February 11, 2003 Order, the Commission stated, However, LG&E is reminded that it has a continuing obligation to review O&M expenses that are already included in existing rates and to the extent those expenses are impacted by the 2003 Plan projects, that impact must be recognized in the surcharge calculations.<sup>1</sup> In its petition for rehearing, KIUC argued that the Commission failed to follow this principle when it did not reduce the O&M expenses recovered in the environmental surcharge by the expense associated with the elimination of four scrubber operators at Mill Creek. In its response to KIUC s petition, LG&E noted that the four employees were reassigned at Mill Creek and since the employees were still with LG&E, there was no reduction in operation expense. LG&E concluded that since there was no reduction in operation expense, there was no offset required in the surcharge calculations.

In granting KIUC s petition for rehearing, the Commission noted that the record did not indicate whether LG&E s existing base rates included the four environmental

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<sup>1</sup> February 11, 2003 Order at 16-17.

employees whose jobs were eliminated. In its subsequent data responses, LG&E stated that the expenses associated with the four environmental employees had been included in existing base rates and provided the job functions and duties of the vacant positions. LG&E also disclosed that the direct labor charges for the four employees were \$175,000 not including benefits and associated overhead expenses.

The only party to file comments, Mr. Madison, argues that the savings in environmental O&M expenses due to the implementation of the 2003 Compliance Plan must be reflected in the surcharge calculations. He further contends that LG&E did not accurately determine the amount to be excluded, and calculated an annual adjustment of \$274,394.<sup>2</sup>

#### ANALYSIS

As established by KRS 278.183, the environmental surcharge provides eligible electric utilities with the opportunity to recover certain environmental costs and to earn a return on qualifying environmental control-related investments that are not reflected in existing base rates. Because of the focus on plant and expenses not already included in existing rates, the environmental surcharge is a stand-alone cost recovery mechanism.

The record in this case now reflects that the labor expense associated with the four environmental employees was included in LG&E's base rates that were established in Case No. 1998-00426.<sup>3</sup> The labor expense has been recovered through LG&E's

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<sup>2</sup> Madison Reconsideration Brief at 3.

<sup>3</sup> Case No. 1998-00426, Application of Louisville Gas and Electric Company for Approval of an Alternative Method of Regulation of Its Rates and Service, final Order issued January 7, 2000.

base rates, rather than the environmental surcharge. LG&E has disclosed that the total labor expense associated with these four environmental employees included in the test period used in Case No. 1998-00426 was \$271,119.<sup>4</sup> The \$175,000 identified previously reflected only direct labor charges and did not recognize associated overheads and benefit charges.

In its response to KIUC's petition for rehearing, LG&E acknowledged that it has a continuing obligation to review O&M expenses that are already included in existing rates and to the extent that those expenses are impacted by the environmental projects in the 2003 Compliance Plan, that impact must be recognized in the surcharge calculations.<sup>5</sup> Yet throughout the rehearing examination, LG&E has argued against a reduction in surcharge O&M expense because of the reassignment of the four employees. LG&E stresses that the four employees in question were not terminated, but reassigned to vacant positions at Mill Creek. Thus, LG&E contends from an overall operations standpoint it did not experience any reduction in operating expenses, and no offset to the surcharge calculations is required.

The Commission is not persuaded by LG&E's arguments. The fact that the environmental employees were actually transferred to existing, vacant non-environmental positions is not relevant to this issue. What is relevant is that the new environmental projects resulted in an O&M savings by eliminating four environmental positions at the Mill Creek scrubber. The O&M expense for those positions was already

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<sup>4</sup> Response to the Commission Staff's Second Rehearing Data Request dated April 29, 2003, Item 1(a).

<sup>5</sup> LG&E Response to Petition for Rehearing of KIUC at 2.

included in base rates and their elimination must now be reflected in the surcharge calculations.

Therefore, the Commission finds that the O&M labor expenses associated with the elimination of four environmental positions should be recognized as a reduction in operating expenses in LG&E's environmental surcharge calculations. This decision is consistent with the Commission's previous findings in its February 11, 2003 Order regarding LG&E's obligation to recognize in its surcharge calculation the impacts of environmental projects on O&M expenses already included in base rates.

The Commission further finds that the reduction should be \$271,119 annually, which reflects the total labor expenses for the four employees that were included in LG&E's last base rate case. As noted previously, the \$175,000 discussed in the February 11, 2003 Order only reflected the direct labor charges for the four employees. The exclusion of only the direct labor charges for the four employees would not adequately reflect the impact of the 2003 Compliance Plan projects.

In order to implement this reduction, the Commission has examined the calculation of the surcharge, which currently reflects the investments and expenses associated with three approved compliance plans. The Mill Creek scrubber modifications are part of the 2003 Compliance Plan, however, no O&M expenses were identified and included in the surcharge calculations for that compliance plan. After reviewing the surcharge calculations, the Commission believes that the most appropriate means to reflect the \$271,119 reduction is to insert a line on ES Form 2.00, page 1 of 2, the section titled Determination of Pollution Control Operating Expenses (OE). Since the surcharge is calculated on a monthly basis, it appears reasonable to

divide the \$271,119 by 12 to determine the monthly adjustment. This calculation results in a monthly reduction to operating expenses recovered through the surcharge of \$22,593. Appendix A to this Order contains a revised ES Form 2.00, page 1 of 2, that should be used by LG&E for all monthly surcharge reports filed subsequent to the date of this Order.

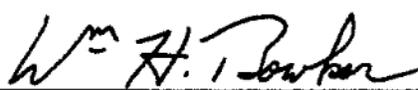
IT IS THEREFORE ORDERED that:

1. LG&E's environmental surcharge revenue requirements shall be reduced to reflect the elimination of four environmental positions at its Mill Creek generating station as a result of the scrubber modifications approved in the 2003 Compliance Plan.
2. LG&E's monthly surcharge calculations shall reflect a reduction to the Total Pollution Control Operating Expenses for the Post-1995 Plan of \$22,593.
3. The reporting format ES Form 2.00, page 1 of 2 included in Appendix A shall be used for each LG&E monthly surcharge filing submitted after the date of this Order. The previous version of that format shall no longer be submitted.
4. All other provisions of the Commission's February 11, 2003 Order shall remain in effect.

Done at Frankfort, Kentucky, this 4<sup>th</sup> day of September, 2003.

By the Commission

ATTEST:

*Deputy*  
  
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Executive Director

## APPENDIX A

### APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE COMMISSION IN CASE NO. 2002-00147 DATED SEPTEMBER 4, 2003

#### Environmental Surcharge Monthly Report Formats

The report format listed below was originally authorized in the Commission's February 11, 2003 Order in this proceeding. As a result of the decision on rehearing, this report format has been modified and will be used by LG&E for all monthly surcharge filings after the date of this Order. This report format will replace the previously approved report format developed for LG&E's environmental surcharge filings. LG&E will not modify any format without the prior consent of the Commission Staff.

ES Form 2.00, page 1 of 2

Current Period Revenue Requirements of Environmental Compliance  
Costs

**LOUISVILLE GAS AND ELECTRIC COMPANY  
ENVIRONMENTAL SURCHARGE REPORT  
Current Period Revenue Requirements of Environmental Compliance Costs  
For the Expense Month of {Month Year}**

Determination of Environmental Compliance Rate Base (RB)

	1995 Plan		Post-1995 Plan	
Eligible Pollution Control Plant				
Eligible Pollution CWIP Excluding AFUDC				
Cash Working Capital Allowance				
Subtotal				
Deductions:				
Accumulated Depreciation on Eligible Pollution Control Plant				
Pollution Control Deferred Income Taxes				
Pollution Control Deferred Investment Tax Credit				
Subtotal				
Environmental Compliance Rate Base				

Determination of Pollution Control Operating Expenses (OE)

	1995 Plan	Post-1995 Plan
Monthly Operations & Maintenance Expense		
Monthly Depreciation & Amortization Expense		
Monthly Property & Other Applicable Taxes (Net of pre-1993 amounts)		
Monthly Insurance Expense (Net of pre-1993 amounts)		
Monthly Emission Allowance Expense		
Monthly Surcharge Consultant Fee		
Monthly Permitting Fees		
Less: Reduction to O&M Expenses associated with 2003 Compliance Plan		22,593
Less: Operating Expenses Associated with Retirements or Replacements Occurring Since Last Roll-in of Surcharge into Existing Rates		
Total Pollution Control Operating Expenses		