

COMMONWEALTH OF KENTUCKY  
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

AN EXAMINATION BY THE PUBLIC SERVICE	)	
COMMISSION OF THE ENVIRONMENTAL	)	
SURCHARGE MECHANISM OF EAST KENTUCKY	)	
POWER COOPERATIVE, INC. FOR THE	)	
SIX-MONTH BILLING PERIODS ENDING	)	CASE NO.
DECEMBER 31, 2007; JUNE 30, 2008; AND	)	2009-00039
DECEMBER 31, 2008; AND THE PASS-THROUGH	)	
MECHANISM FOR ITS SIXTEEN MEMBER	)	
DISTRIBUTION COOPERATIVES	)	

O R D E R

On February 23, 2009, the Commission initiated three six-month reviews of East Kentucky Power Cooperative, Inc.'s ("EKPC") environmental surcharge<sup>1</sup> as billed to the member distribution cooperatives for the six-month periods July 1, 2007 to December 31, 2007; January 1, 2008 to June 30, 2008; and July 1, 2008 to December 31, 2008. Pursuant to KRS 278.183(3), the Commission must review, at six-month intervals, the past operations of the environmental surcharge. After hearing, the Commission may, by temporary adjustment in the surcharge, disallow any surcharge amounts found not to be just and reasonable and reconcile past surcharges with actual costs recoverable pursuant to KRS 278.183(1).

The February 23, 2009 Order also initiated three six-month reviews of the 16 EKPC member distribution cooperatives' ("Member Cooperatives") pass-through

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<sup>1</sup> Case No. 2004-00321, Application of East Kentucky Power Cooperative, Inc. for Approval of an Environmental Compliance Plan and Authority to Implement an Environmental Surcharge (Ky. PSC Mar. 17, 2005).

mechanisms<sup>2</sup> as billed to retail member customers for the six-month periods August 1, 2007 to January 31, 2008; February 1, 2008 to July 31, 2008; and August 1, 2008 to January 31, 2009.<sup>3</sup>

The Commission issued a procedural schedule on February 23, 2009 that provided for discovery, the filing of prepared testimony, and an informal conference.<sup>4</sup> EKPC filed prepared direct testimony and responded to Commission Staff's requests for information.

Owen, Fleming-Mason and Gallatin Steel Company ("Gallatin") requested and were granted full intervenor status in this proceeding. Owen and Fleming-Mason

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<sup>2</sup> Case No. 2004-00372, Application of Big Sandy RECC, Blue Grass Energy Cooperative Corporation, Clark Energy Cooperative, Cumberland Valley Electric, Farmers RECC, Fleming-Mason Energy ("Fleming-Mason"), Grayson RECC, Inter-County Energy Cooperative, Jackson Energy Cooperative, Licking Valley RECC, Nolin RECC, Owen Electric Cooperative ("Owen"), Salt River Electric, Shelby Energy Cooperative, South Kentucky RECC ("South Kentucky") and Taylor County RECC for Authority to Pass Through the Environmental Surcharge of East Kentucky Power Cooperative, Inc. (Ky. PSC Mar. 17, 2005).

<sup>3</sup> The Settlement Agreement approved in Case Nos. 2004-00321 and 2004-00372 allows the member distribution cooperatives to pass through the environmental surcharge to their customers at approximately the same time as EKPC bills the environmental surcharge to the member distribution cooperatives, thus avoiding a billing lag for the member distribution cooperatives. Therefore, the costs incurred from June 2007 through November 2007 are billed to the member distribution cooperatives in the months of July 2007 through December 2007, with these same costs passed through to the member customers on the bills for August 2007 through January 2008. The costs incurred from December 2007 through May 2008 are billed to the member distribution cooperatives in the months of January 2008 through June 2008, with these same costs passed through to the member customers on the bills for February 2008 through July 2008. The costs incurred in the months of June 2008 through November 2008 are billed to the member distribution cooperatives in the months of July 2008 through December 2008, with these same costs passed through to the member customers on the bills for August 2008 through January 2009.

<sup>4</sup> The February 23, 2009 procedural schedule provided for, but did not schedule, a public hearing and the filing of briefs.

proposed a change in the retail pass-through allocation methodology for customers whose rates are based upon EKPC's Section B or C rate schedules or are served under special contracts. Owen and Gallatin participated in an informal conference held on April 2, 2009, but did not request the opportunity to submit data requests or file comments. The Commission's April 14, 2009 Order made the other 14 Member Cooperatives parties to this proceeding and included a data request to the Member Cooperatives concerning the operation of the pass-through mechanism during the three review periods. Twelve Member Cooperatives responded to the data request. On July 7, 2009, a supplemental data request was sent to the Member Cooperatives requesting that they state whether they were proposing a change to their allocation method and, if so, what that change would be and whether the affected customers had been notified. All Member Cooperatives responded to the second data request.<sup>5</sup>

On August 19, 2009, the Commission ordered any party desiring a hearing to file a request with an accompanying statement identifying any material issues of fact and ordered South Kentucky to state whether it desired a hearing on the implementation of a kWh-based allocation methodology. No party requested a hearing, and South Kentucky responded that it would not request a hearing to pursue implementing a kWh-based allocation methodology and would maintain its current pass-through methodology.

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<sup>5</sup> South Kentucky responded and stated that it wished to change to an allocation based on a per kilowatt-hour ("kWh") methodology.

## SURCHARGE ADJUSTMENT

The February 23, 2009 Order initiating this case indicated that, since each of the three periods under review in this proceeding may have resulted in over- or under-recoveries, the Commission would entertain proposals to adopt one adjustment factor to net all over- or under-recoveries. EKPC determined that it had a net over-recovery of its environmental costs of \$4,060,313.<sup>6</sup> EKPC proposed that the over-recovery be returned to its Member Cooperatives by decreasing the total jurisdictional environmental surcharge revenue requirement by \$2,030,156 per month for the first two months following the Commission's decision in this proceeding rather than the six-month amortization period EKPC has used in the past.<sup>7</sup>

As part of this review, EKPC proposed to implement a two-month "true-up" adjustment. Although it had previously argued against establishing such an adjustment, EKPC now believes that implementing a two-month true-up will provide for a more timely refund or recovery of the surcharge and will help eliminate timing differences that occur due to the difference of a given billing month's revenue from the 12-month average revenues used in the determination of the billing factor. EKPC also proposes that the Member Cooperatives' retail pass-through mechanism be revised to include a similar two-month "true-up" adjustment to timely refund to, or collect recoveries from, their retail customers.

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<sup>6</sup> Response to the Commission Staff's First Data Request dated March 26, 2009, Item 1, at 4.

<sup>7</sup> Wood Testimony at 6.

The Commission has reviewed and finds reasonable EKPC's calculation of a net over-recovery of \$4,060,313 for the review periods covered in this proceeding. The Commission also finds reasonable EKPC's proposal to refund that over-recovery over two months rather than six months as approved in the past, resulting in a decrease of \$2,030,156 in the total jurisdictional environmental surcharge revenue requirement in each of the first two billing months following the date of this Order. We further find reasonable EKPC's proposal to implement a two-month "true-up" adjustment for itself and its Member Cooperatives in the first two monthly filings submitted after the date of this Order.

#### RATE OF RETURN

The Settlement Agreement approved in Case No. 2004-00321 provided that the overall rate of return reflect the weighted average cost of the debt issuances directly related to the compliance projects in EKPC's compliance plan, multiplied by a Times Interest Earned Ratio ("TIER") factor. The Settlement Agreement further provided that EKPC update the return as of the end of each six-month review period and request Commission approval of the updated average cost of debt.<sup>8</sup>

EKPC updated the weighted average cost of debt as of November 30, 2008 and determined the rate of return, utilizing the TIER factor of 1.35 which was authorized in Case No. 2008-00409.<sup>9</sup> Utilizing these components, EKPC proposed an overall rate of return of 6.429 percent to be used starting with the first month following the final Order

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<sup>8</sup> Case No. 2004-00321, March 17, 2005 Order, Appendix A, at 3.

<sup>9</sup> Case No. 2008-00409, General Adjustment of Electric Rates of East Kentucky Power Cooperative, Inc. (Ky. PSC Mar. 31, 2009).

in this case.<sup>10</sup> The Commission has reviewed and finds reasonable EKPC's determination of the updated rate of return which reflects the updated weighted average cost of debt and a 1.35 TIER factor. EKPC should use a rate of return of 6.429 percent for all environmental surcharge monthly filings submitted after the date of this Order.

### RETAIL PASS-THROUGH MECHANISM

#### Operation of Retail Pass-Through Mechanism

In the previous environmental surcharge review case, Case No. 2007-00378,<sup>11</sup> some Member Cooperatives indicated that a problem existed in the methodology used to calculate the retail pass-through mechanism. These Member Cooperatives claimed that the retail pass-through methodology had not allocated enough of the monthly environmental surcharge costs to large industrial customers, resulting in an under-recovery of surcharge revenue from this customer group. The Member Cooperatives stated that EKPC was aware of the problem and was developing a solution that would be presented to the Commission. As part of the discovery in this review, EKPC was asked to provide any proposed changes in the retail pass-through mechanism that it had presented to its Member Cooperatives as a way to address the allocation issue. As part of its response, EKPC provided two alternatives that it had presented to its Member

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<sup>10</sup> Response to the Commission Staff's First Data Request dated March 26, 2009, Item 7, at 2.

<sup>11</sup> Case No. 2007-00378, An Examination by the Public Service Commission of the Environmental Surcharge Mechanism of East Kentucky Power Cooperative, Inc. for the Six-Month Billing Periods Ending June 30, 2006 and December 31, 2006, for the Two-Year Billing Period Ending June 30, 2007, and the Pass-Through Mechanism for Its Sixteen Member Distribution Cooperatives (Ky. PSC Aug. 1, 2008).

Cooperatives.<sup>12</sup> The alternatives were: (1) EKPC would continue to develop a single wholesale environmental surcharge factor based on revenue for billing to its Member Cooperatives, with the Member Cooperatives providing a direct pass-through of EKPC's wholesale environmental costs attributable to their respective Schedule B, C and special contract customers; or (2) EKPC and the Member Cooperatives would all change their environmental surcharges from a revenue-based allocation methodology to a kWh-based methodology. EKPC recommended Alternative 1 to any Member Cooperatives that wished to change their pass-through methodology. Owen and Fleming-Mason proposed that they change their pass-through methodology to Alternative 1.

The Commission has reviewed and finds reasonable Owen and Fleming-Mason's request to change their retail pass-through methodology to Alternative 1 developed by EKPC effective with the first billing month after the date of this Order

#### Retail Pass-Through Adjustment

Each of the Member Cooperatives determined an over- or under-recovery for its surcharge pass-through mechanism, with 10 of them having over-recoveries and six having under-recoveries. Like EKPC, the Member Cooperatives proposed that the over-recoveries be refunded to, or under-recoveries be collected from, ratepayers as an adjustment to the retail pass-through factor for each of the first two months following the Commission's Order in this proceeding.

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<sup>12</sup> Response to the Commission Staff's First Data Request dated March 26, 2009, Item 8, at 2-33.

The Commission has reviewed and finds reasonable the Member Cooperatives' calculations of their respective over-recoveries and under-recoveries for the review periods covered in this proceeding. In addition, the Commission finds reasonable the Member Cooperatives' proposal to adjust their respective retail pass-through factors in each of the first two billing months following the date of this Order. A schedule of the over- or under-recovery for each Member Cooperative and the resulting monthly adjustments are shown in the Appendix to this Order.

IT IS THEREFORE ORDERED that:

1. EPKC shall reduce its jurisdictional environmental revenue requirement by \$2,030,156 per month in each of the first two billing months following the date of this Order.

2. The proposed revisions to the environmental surcharge tariffs of Owen and Fleming-Mason implementing a direct pass-through of EKPC's wholesale environmental costs attributable to retail customers served under tariffs based on EKPC's Schedule B or C or under special contracts are approved, effective in the first billing month following the date of this Order.

3. Owen and Fleming-Mason shall file, within 20 days of the date of this Order, their respective revised environmental surcharge tariffs reflecting the changes in pass-through methodology approved herein and shall list in those tariffs the affected retail rate classes.

4. The Member Cooperatives shall include the applicable monthly retail pass-through adjustments shown in the Appendix in the determination of their



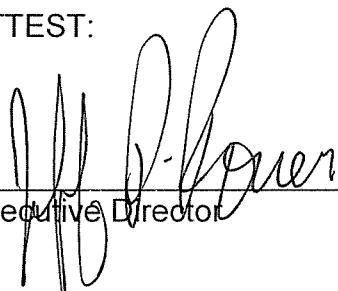
respective pass-through mechanisms in each of the first two billing months following the date of this Order.

5. East Kentucky shall use a rate of return of 6.429 percent in all monthly environmental surcharge filings subsequent to the date of this Order.

By the Commission

ENTERED  
NOV - 6 2009 *al*  
KENTUCKY PUBLIC  
SERVICE COMMISSION

ATTEST:

  
\_\_\_\_\_  
Executive Director

APPENDIX

APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE  
COMMISSION IN CASE NO. 2009-00039 DATED NOV - 6 2009

Member Cooperatives' Adjustments to  
Monthly Pass-Through Mechanism

The EKPC Member Cooperatives shall include the following monthly adjustments in the determination of the applicable pass-through factors for two months after the date of this Order.

	<u>Total Amount of Over-Recovery</u>	<u>Monthly Amount Returned</u>
Blue Grass Energy Cooperative Corp.	\$ 43,220	\$ 21,610
Clark Energy Cooperative	\$ 103,444	\$ 51,722
Grayson RECC	\$ 37,778	\$ 18,889
Inter-County Energy Cooperative Corp.	\$ 201,265	\$ 100,633
Jackson Energy Cooperative	\$ 387,742	\$ 193,871
Owen Electric Cooperative	\$ 223,127	\$ 111,563
Salt River Energy Cooperative Corp.	\$ 118,545	\$ 59,273
Shelby Energy Cooperative, Inc.	\$ 38,611	\$ 19,305
South Kentucky RECC	\$ 150,137	\$ 75,069
Taylor County RECC	\$ 59,984	\$ 29,992
	<u>Total Amount of Under-Recovery</u>	<u>Monthly Amount Collected</u>
Big Sandy RECC	\$ 183,755	\$ 91,878
Cumberland Valley Electric	\$ 131,295	\$ 65,648
Farmers RECC	\$ 304	\$ 152
Fleming-Mason Energy	\$ 24,525	\$ 12,263
Licking Valley RECC	\$ 49,833	\$ 24,917
Nolin RECC	\$ 388,791	\$ 194,396

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