

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	)	CASE NO.
TWO-YEAR BILLING PERIOD ENDING	)	2009-00317
JUNE 30, 2009 AND THE PASS-THROUGH	)	
MECHANISM FOR ITS SIXTEEN MEMBER	)	
DISTRIBUTION COOPERATIVES	)	

O R D E R

On August 18, 2009, the Commission initiated a two-year review of East Kentucky Power Cooperative, Inc.'s ("EKPC") environmental surcharge<sup>1</sup> as billed to its member distribution cooperatives for the two-year period from July 1, 2007 to June 30, 2009. Pursuant to KRS 278.183(3), the Commission must review, at six-month intervals, the past operations of the environmental surcharge, disallow any surcharge amounts that are found not to be just and reasonable, and reconcile past surcharges with actual costs recoverable. At two-year intervals, the Commission must review and evaluate the past operations of the environmental surcharge, disallow improper expenses and, to the extent appropriate, incorporate surcharge amounts found just and reasonable into the existing base rates of the utility.

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<sup>1</sup> EKPC's environmental surcharge was initially approved in 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).

The August 18, 2009 Order also initiated a two-year review of the 16 EKPC member distribution cooperatives' ("Member Coops") pass-through mechanism as billed to retail member customers for the two-year period from August 1, 2007 to July 31, 2009.<sup>2</sup>

The Commission issued a procedural schedule that provided for discovery, the filing of prepared testimony, an informal conference, and a public hearing. EKPC filed prepared direct testimony and responded to requests for information. There were no parties requesting intervenor status to this proceeding. On November 24, 2009, EKPC filed a response to the Commission's November 19, 2009 Order stating that there were no material issues of fact that warranted a hearing in this case. EKPC further stated that this case may be submitted for decision on the current record without a hearing.

#### SURCHARGE ADJUSTMENT

The August 18, 2009 Order initiating this case indicated that, since the period 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 under-recovery of its environmental costs of \$1,300,633.<sup>3</sup> EKPC proposed that it be authorized to collect the

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<sup>2</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. The costs incurred in the months of June 2007 through May 2009 are billed to the member distribution cooperatives in the months of July 2007 through June 2009, with these same costs passed through to the member customers on the bills for August 2007 through July 2009.

<sup>3</sup> Response to Commission Staff's First Data Request dated September 24, 2009, item 1, page 5 of 5.

under-recovery from its Member Coops by increasing the total jurisdictional environmental surcharge revenue requirement by \$650,316 per month for the first two months following the Commission's decision in this proceeding.

The Commission has reviewed and finds reasonable EKPC's calculation of a net under-recovery of \$1,300,633 for the review period covered in this proceeding. The Commission also finds reasonable EKPC's proposal to collect that under-recovery over two months, resulting in an increase of \$650,316 in the total jurisdictional environmental surcharge revenue requirement in each of the first two billing months following the date of this Order.

#### RATE OF RETURN

The Settlement Agreement approved in Case No. 2004-00321 provided that the rate of return would be based on a weighted average debt cost of the debt issuances directly related to the four 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>4</sup>

EKPC updated the weighted average cost of debt as of May 31, 2009 and determined the rate of return utilizing a TIER factor of 1.35 which was authorized in Case No. 2008-00409.<sup>5</sup> Utilizing these components, EKPC proposed an overall rate of

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<sup>4</sup> Case No. 2004-00321, March 17, 2005 Order, Appendix A, at 3.

<sup>5</sup> Case No. 2008-00409, General Adjustment of Electric Rates of East Kentucky Power Cooperative, Inc. (Ky. PSC Mar. 31, 2009).

return of 6.051 percent to be used starting with the first month following the final Order in this case.<sup>6</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 6.051 percent for all environmental surcharge monthly filings submitted after the date of this Order.

### RETAIL PASS-THROUGH MECHANISM

#### Retail Pass-Through Adjustment

Each of the Member Coops determined an over- or under-recovery for its surcharge pass-through mechanism, with ten of the Member Coops having over-recoveries and six having under-recoveries. Like EKPC, the Member Coops 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.

The Commission has reviewed and finds reasonable the Member Coops' calculations of their respective over-recoveries and under-recoveries for the review period covered in this proceeding. In addition, the Commission finds reasonable the Member Coops' proposals 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 Coop and the related monthly adjustments is shown in the Appendix to this Order.

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<sup>6</sup> Response to Commission Staff's First Data Request dated September 24, 2009, item 6, page 2 of 2.

### SURCHARGE ROLL-IN

EKPC proposes to not incorporate, or “roll-in,” any of its environmental surcharge amounts into its existing base rates. EKPC stated that it is planning to undertake a rate design feasibility study in 2010. EKPC plans to examine how the roll-in of the environmental surcharge could best be accomplished when cost-of-service based rates are in effect.<sup>7</sup>

The environmental surcharge statute directs the Commission to incorporate surcharge amounts found just and reasonable in the utility’s existing base rates, but only “to the extent appropriate.” The Commission has reviewed and finds reasonable EKPC’s recommendation to not roll-in environmental surcharge amounts at the present time.

As part of this review, Commission Staff asked EKPC to provide the Base Environmental Surcharge Factor (“BESF”) that reflects all environmental surcharge amounts previously incorporated into existing base rates. EKPC uses the base/current approach to assure compliance with the requirement pursuant to KRS 278.183 so that only those environmental costs not already included in existing base rates are recovered through the environmental surcharge. In response, EKPC proposed to reset its current BESF to zero percent. EKPC’s current BESF at the end of this two-year review period was 1.21 percent. EKPC states that, with the exception of one asset, it has retired all assets giving rise to 1.05 percent of the BESF. The remaining .16 percent of the BESF relates to EKPC’s Allowance for Funds Used During Construction (“AFUDC”). In Case No. 2008-00409, the Commission approved EKPC’s proposal to

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<sup>7</sup> Wood Direct Testimony at 12.

discontinue accruing AFUDC on capital projects, and no AFUDC was included in the forecasted test year used in that proceeding. Citing all these facts, EKPC states that it believes the BESF should be reset to zero.

EKPC also recommends that its 16 Member Coops revise their tariffs to omit any reference to the base/current method or BESF because this approach is not necessary for the Member Coops' retail pass-through mechanism. The base/current approach is accomplished at the wholesale level through EKPC's environmental surcharge.

The Commission has reviewed and finds reasonable EKPC's proposal to reset its BESF to zero percent for all environmental surcharge monthly filings submitted after the date of this Order. The Commission also finds reasonable EKPC's recommendation that the 16 Member Coops continue the environmental surcharge pass-through mechanism but require modification of the Member Coops' ES tariffs to omit references to a "base/current" approach or a BESF.

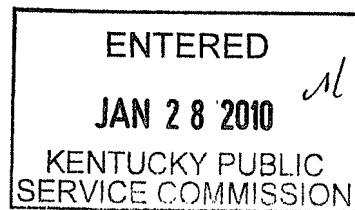
IT IS THEREFORE ORDERED that:

1. EKPC shall include a \$650,316 monthly increase in its jurisdictional environmental revenue requirement determined in each of the first two billing months following the date of this Order as discussed herein.
2. EKPC shall use a rate of return of 6.051 percent in all monthly environmental surcharge filings subsequent to the date of this Order.
3. EKPC's Member Coops shall include the applicable monthly retail pass-through adjustments, shown in the Appendix to this Order, in the determination of each Member Coop's pass-through mechanism as discussed herein.

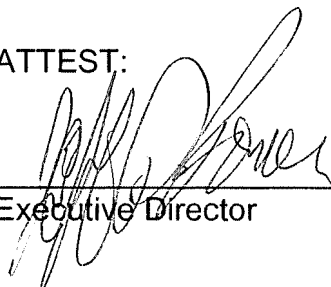
4. EKPC shall use a BESF of zero percent in all monthly environmental surcharge filings subsequent to the date of this Order.

5. The 16 Member Coops, identified in the Appendix of this Order, shall file, within 20 days of the date of this Order, their respective revised environmental surcharge tariffs reflecting the change and shall omit reference to the base/current approach and to BESF as approved herein.

By the Commission



ATTEST:

  
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Executive Director

## APPENDIX

### APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE COMMISSION IN CASE NO. 2009-00317 DATED JAN 28 2010

#### Member Cooperatives' Adjustment 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 the first two months after the date of this Order.

	<u>Total Amount of Over-Recovery</u>	<u>Monthly Amount To Be Returned</u>
Big Sandy RECC	\$ 17,370	\$ 8,685
Blue Grass Energy Cooperative Corp.	\$ 254	\$ 127
Clark Energy Cooperative	\$ 13,842	\$ 6,921
Farmers RECC	\$ 61	\$ 30
Inter-County Energy Cooperative Corp.	\$ 44,677	\$ 22,339
Jackson Energy Cooperative	\$ 24,056	\$ 12,028
Licking Valley RECC	\$ 11,112	\$ 5,556
Owen Electric Cooperative	\$ 275,836	\$ 137,918
Salt River Energy Cooperative Corp.	\$ 69,497	\$ 34,749
Taylor County RECC	\$ 131,809	\$ 65,905

	<u>Total Amount of Under-Recovery</u>	<u>Monthly Amount To Be Collected</u>
Cumberland Valley Electric	\$ 139,518	\$ 69,759
Fleming-Mason Energy Cooperative	\$ 95,358	\$ 47,679
Grayson RECC	\$ 3,535	\$ 1,768
Nolin RECC	\$ 82,839	\$ 41,419
Shelby Energy Cooperative	\$ 11,571	\$ 5,785
South Kentucky RECC	\$ 33,672	\$ 16,836



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