COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

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PUBLIC SERVICE COMMISSION

In the Matter of:

THE APPLICATION OF EAST KENTUCKY POWER COOPERATIVE, INC., INTER-COUNTY ENERGY COOPERATIVE CORPORATION, NOLIN RURAL ELECTRIC COOPERATIVE CORPORATION, AND SALT RIVER ELECTRIC COOPERATIVE CORPORATION, FOR AUTHORITY TO IMPLEMENT A FIXED BILL PILOT PROGRAM	)))))))	Case No. 2004-00330

COMMENTS OF THE ATTORNEY GENERAL

EKPC is proposing a flat bill pilot which, like budget billing, offers a customer the opportunity to pay the same amount for service each month. Unlike budget billing, the flat bill would have no true up at the end of a year of service to bring service used into line with service paid for in accord with the standard rates predicated on cost of service. Instead, via a formula that determines the flat bill price to be paid based on an estimated probable usage at cost of service rates plus a risk adder to compensate the provider for the risk attendant to it from offering, the customer is charged a fixed price paid over twelve months with no true up to reflect actual usage. This change makes the flat bill a price based product rather than a cost based product.[1]

PRICE BASED PRODUCTS ARE NOT COMPATIBLE WITH FULLY REGULATED RATES.

Price based products may be appropriate in environments of competition and retail choice, but they are not appropriate in Kentucky, where the legislature has deliberately determined that regulated rates are more beneficial to Kentucky's consumers than competition would be. In a competitive environment a price based product places the full risk of the offering,

[1] EKPC also considers this to be a price based product. See Response to Question 35, page 2 of 204, filed September 24, 2004, to the Request for Information posed by the Attorney General.

including the risk that its provider will take a beating and possibly be driven from the market altogether, on the seller. In Kentucky's regulated rate environment, the provider is never fully responsible for the risk that a rate will fail to recover its cost to serve, including a return. This fact was just brought home by LG&E and KU's general rate cases. There the utilities, despite having agreed to alternative rate making under the earnings sharing mechanism, exercised their statutory right to seek a rate increase once the earnings fell below a level acceptable to them.[2]

KRS Chapter 278 guarantees utilities the right to increase rates in the event of under earnings. Should the utility seek a rate increase in a year where the flat bill has not proven profitable, there is no way to isolate the impact of the flat bill on test year revenues. Though the formula utilized to establish the amount to be paid by the flat bill customer is supposed to assure adequate margin to cover EKPC's cost to serve plus its TIER, it is designed to do that over time, not annually. Should the amount paid by collective flat bill customers be less than costs plus TIER during a test year, this will create a reduction of revenues that will impact the rates of other customers.[3] Because EKPC is in an expansion mode, the likelihood of a rate case is substantial.

THE ONE-WAY OPERATION OF THE RISK MARGIN IS WRONG FOR ANY KENTUCKY UTILITY.

The flat bill operates to give the utility a profit margin greater than standard cost of service rates whenever the usage assumed for the flat bill customer matches or exceeds that assumed in flat bill amount the customer will pay. The utility gets to keep that added profit, over and above the cost to serve that includes a return on investment. Only if the flat bill customer uses substantially more energy than that assumed in calculating the amount to be paid will the

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[2] See, *In the Matter of: Application of Louisville Gas and Electric Company for an Adjustment of the Gas and Electric Rates, Terms and Conditions,* Case No. 2003-00334 and *Application of Kentucky Utilities Company for an Adjustment of the Electric Rates, Terms and Conditions,* Case No. 2003-00434.

[3] See Response to Question 35, page 10 of 204 filed September 24, 2004, in response to the Request for Information posed by the Attorney General where it is stated in bold "Flat pricing programs are not designed to win every year. Rather, they are designed to earn a given return over multiple years."

utility loose. In the long run, that loss is supposed to balance the periods of profit to make the flat bill a going proposition for the utility. But, because of the statutory right to seek rate increases in times of under earning, that loss may translate into increased rates for other customers.[4] The risk of absorbing that loss does not stay with the utility. Because EKPC is a cooperative, the one way operation of the flat bill profit and risk is not as bad EKPC's customers as it would be for the customers of for-profit providers. The customers of the cooperative have the ability to share in that profit as well as being at risk for the loss, in theory at least.

The problem is that once a special tariff is granted to any utility in any circumstance, regardless of the lack of precedent that grant is supposed to set, it does act as precedent for other utilities to seek and receive a like tariff in different circumstances. This fact has just been demonstrated in the Delta Natural Gas general rate case.[5] There the Commission pointed to terms that were part of unanimous settlements for two other utilities, both of which were not to create any precedent, as the grounds for its action with reference to a contested tariff. Given that the one way operation of a flat bill risk margin would be wholly unacceptable in the context of an investor-owned utility, it cannot and should not be granted for the cooperative either.

THE FLAT BILL ENCOURAGES WASTEFUL CONSUMPTION AND REWARDS THE UTILITY THROUGH

[4] *Id*, at page 175 of 204

[5] See, page 59 of the November 10, 2004 Order entered in Case Number 2004-00067, *In the Matter of: Application of Delta Natural Gas Company, Inc. for an Adjustment of Rates,* where the Commission states: "Allowing recovery via a rider is consistent with Commission decisions for two other gas utilities, Atmos Energy and Columbia Gas of Kentucky." Columbia Gas was a case in which the Commission approved as reasonable a unanimous settlement that reduced rates that contained language precluding the use of any of its terms to set precedent. Atmos was also a case in which the Commission approved as reasonable a unanimous settlement that also includes terms precluding its use as precedent.

ADDED PROFITS PER KWH IF WASTEFUL CONSUMPTION DOES NOT OCCUR.

EKPC has indicated that it will continue to encourage conservation. To do so is not only right but profitable for EKPC. EKPC becomes a big winner in the event the flat bill customer does not increase consumption once on the flat bill because of the built in assumptions of increased usage and the risk factor that are a part of calculating the flat bill rate. If the consumer continues conservative consumption, EKPC gets a substantial added return over the cost to serve that customer. This, however, does not seem to be the expected operation of the flat bill tariff.

Despite encouragement to conserve, it is clear that one of the primary draws for the flat bill customer is that it diminishes the need to practice careful conservation. Though wildly excessive usage is discouraged by the ability to bump a customer from the rate, the rate clearly assumes that the flat bill customer will not be as conservative as the standard rate customer. Increased usage is expected in the first year, is planned for in the rate, and is touted as one of the benefits of the rate in that the load factor is improved.

The flat bill is touted as improving load factor by increasing shoulder and off-peak usage among flat bill customers.[6] It is a running joke among consumer advocates that one of the best ways to improve the residential load factor is for residential customers to leave all their lights and TVs on all the time. This may be exactly what is happening with the flat bill customer. EKPC has not been able to provide sufficient detail as to the type of usage change that is expected to occur to allay concerns that wasteful consumption is what gives rise to the expected

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[6] This is not to be confused with a peak shaving program as increases in peak use are also occurring. The expectation of minimum impact on peak use seems to stem from the fact that "cooling systems reach…their peak capacity in such hours even in the absence of fixed billing." Response to Request for Information posed by the Attorney General, Question 35, page 170 of 204 filed September 24, 2004.

load improving increase in consumption by flat bill customers.[7] It is entirely contradictory and inconsistent to encourage wasteful use through a flat bill tariff in a state that so values demand side management that it has enacted a statute to require the benefiting class to pay for the cost of demand side management programs.

CONCLUSION

The flat bill tariff should not be used in a regulated environment. It gives the utility the profit and leaves customers with the added risk posed by the offering. It encourages wasteful usage. The increase in consumption is both expected and taken into account in establishing the flat bill rate. If the consumer does not increase consumption, then a premium has been paid solely for the sake of knowing what the bill will be. This is nothing but a change in packaging. It does not constitute a sound reason to offer this tariff.

Respectfully submitted

GREGORY D. STUMBO
ATTORNEY GENERAL

Elizabeth E. Blackford
Assistant Attorney General
1024 Capital Center Drive, Suite 200
Frankfort, Kentucky 40601-8204
(502) 696-5453
betsy.blackford@ag.ky.gov

[7] See Response to Question 20 of the Request for Information posed by the Attorney General, filed September 24, 2004.

NOTICE OF FILING AND CERTIFICATION OF SERVICE

I hereby give notice that I have filed the original and ten true copies of the foregoing with the Executive Director of the Kentucky Public Service Commission at 211 Sower Boulevard, Frankfort, Kentucky 40601 this the 19 th day of November, 2004, and certify that this same day I have served the parties by mailing a true copy, postage prepaid, to the following:

JIM JACOBUS
CEO
INTER-COUNTY ENERGY COOPERATIVE CORP
P O BOX 87
DANVILLE KY 40423-0087

HON CHARLES A LILE
SENIOR CORPORATE COUNSEL
EKPC INC
P O BOX 707
WINCHESTER KY 40392-0707

MICHAEL L MILLER
PRESIDENT & CEO
NOLIN RECC
411 RING ROAD
ELIZABETHTOWN KY 42701-8701

LARRY HICKS
SALT RIVER ELECTRIC COOPERATIVE CORP
P O BOX 609
BARDSTOWN KY 40004