

COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

RECEIVED

In the Matter of:

APR 04 2007

PUBLIC SERVICE COMMISSION

AN EXAMINATION BY THE PUBLIC SERVICE )  
COMMISSION OF THE ENVIRONMENTAL )  
SURCHARGE MECHANISM OF KENTUCKY )  
POWER COMPANY FOR THE SIX-MONTH )  
BILLING PERIODS ENDING DECEMBER 31, 2002, )  
DECEMBER 31, 2003, JUNE 30, 2004, )  
DECEMBER 31, 2004, AND DECEMBER 31, 2005, )  
AND FOR THE TWO-YEAR BILLING PERIODS )  
ENDING JUNE 30, 2003 AND JUNE 30, 2005 )

CASE NO. 2006-00128

NOTICE OF COMPLIANCE AND REQUEST FOR COMMISSION APPROVAL OR, IN THE ALTERNATIVE, PETITION FOR REHEARING

On March 12, 2007, the Commission entered its Order granting the Attorney General's Petition for Rehearing and finding that the environmental compliance costs authorized in the Commission's January 31, 2007 Order should be collected subject to refund, to the extent the costs are associated with out-of-state generating facilities. In response to that Order, Kentucky Power submits this Notice of Compliance for the Commission's approval. Should the Commission disapprove of Kentucky Power's compliance plan, then Kentucky Power petitions for rehearing of the Commission's March 12, 2007 Order.

I. THE COMMISSION'S ORDERS

This is a case brought by the Commission pursuant to KRS 278.183(3) to review the operation of Kentucky Power's environmental surcharge mechanism for the six-month billing periods ending December 31, 2002, December 31, 2003, June 30, 2004, December 31, 2004, and December 31, 2005, and for the two-year billing periods ending June 30, 2003 and June 30, 2005. KRS 278.183(3) requires the following of the Commission with respect to these reviews:

At six (6) month intervals, the commission shall review past operations of the environmental surcharge of each utility, and after hearing, as ordered, shall, by temporary adjustment in the surcharge, disallow any surcharge amounts found not just and reasonable and reconcile past surcharges with actual costs recoverable pursuant to subsection (1) of this section. Every two (2) years the commission shall review and evaluate past operation of the surcharge, and after hearing, as ordered, shall disallow improper expenses, and to the extent appropriate, incorporate surcharge amounts found just and reasonable into the existing base rates of each utility.

The Commission performed its duties under this statute with respect to the operation of Kentucky Power's environmental surcharge mechanism in Case No. 2006-00128. In its Order issued on January 31, 2007, the Commission determined that Kentucky Power had a net under-recovery of its environmental costs totaling \$572,963 for the period under review, as well as for the seven expense months immediately following the end of the last review period included in the proceeding. The Commission found that Kentucky Power should collect this under-recovery by adjusting its environmental surcharge revenue requirement by \$95,494 in each of the first six billing months following the entry of the Order.

On February 20, 2007, the Attorney General petitioned the Commission for rehearing. The Attorney General argued that the Commission's Order contained no provision for the collection of any part of the environmental compliance costs subject to refund, nor did it require record keeping that would allow for refunds of any nature should the Attorney General and the Kentucky Industrial Utility Customers prevail on their argument that Kentucky Power should not be entitled to recover its portion of environmental compliance costs incurred by its out-of-state sister companies in the AEP Pool. The Commission granted the Attorney General's request, finding as follows:

Therefore, the Commission finds that the AG's request for rehearing should be granted and the environmental surcharge collections authorized in the January 31, 2007 Order that are associated with out-of-state generating facilities should be collected subject to refund and that Kentucky Power should maintain its records

in such a manner that Kentucky Power, the Commission, or any of Kentucky Power's customers will be able to determine the amounts to be refunded and to whom if the Court should rule that these costs are not eligible for recovery pursuant to KRS 278.183.<sup>1</sup>

As set forth above, the Commission authorized the recovery of \$572,963 in its January 31, 2007 Order. Of that amount, \$164,109 is attributable to Kentucky Power's portion of the environmental compliance costs associated with out-of-state generating facilities for which Kentucky Power bears responsibility pursuant to the AEP Interconnection Agreement. Accordingly, Kentucky Power intends to collect this amount subject to refund pursuant to the terms of the Commission's March 12, 2007 Order.

## **II. KENTUCKY POWER'S COMPLIANCE PLAN**

In addition to ordering that Kentucky Power recover the \$164,109 subject to refund, the Commission also ordered that Kentucky Power "maintain its records in a manner that will permit refunds of these costs to be made should refund be required by the Courts."<sup>2</sup> Should a court of competent jurisdiction ultimately disallow recovery of the \$164,109 through the environmental surcharge, Kentucky Power maintains that the costs should be returned to its customers through a prospective decrease in its jurisdictional environmental revenue requirement. This approach is consistent with both Kentucky law and the Commission's past practice, and Kentucky Power requests the Commission's approval for complying with the March 12, 2007 Order by maintaining its records in a manner that will allow for this adjustment.

KRS 278.183(3) requires the Commission to "disallow any surcharge amounts found not just and reasonable and reconcile past surcharges with actual costs recoverable" through a "temporary adjustment in the surcharge." In drafting the law in this manner, the General

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<sup>1</sup> March 12, 2007 Order at 3-4.

<sup>2</sup> *Id.* at 4.

Assembly determined that any adjustments deemed necessary by the Commission following review of the operation of an electric utility's environmental surcharge mechanism—whether those adjustments result in increases or decreases in the utility's jurisdictional environmental revenue requirement—should be effectuated prospectively. The negative implication of this authorization is that the Commission has no authority under KRS 278.183(3) to require Kentucky Power to either return disallowed costs or recoup actual costs recoverable through retroactive refunds to or collections from the customers it served during these prior periods. Accordingly, should Kentucky Power's recovery of the \$164,109 be disallowed, this statute requires that the costs be returned prospectively to Kentucky Power's customers by an adjustment in the surcharge.

The Commission has followed this approach of ordering environmental surcharge adjustments in six-month and two-year review cases involving Kentucky Power. In addition to this case, the Commission also ordered Kentucky Power to include a \$6,632 increase in its environmental surcharge revenue requirement in the monthly report following the entry of the Commission's Order in Case No. 2002-00393. This is the approach that should be followed in the event the \$164,109 in environmental compliance costs authorized by the Commission in its March 12, 2007 Order ultimately are disallowed, and Kentucky Power requests that the Commission approve of its plan to maintain its records in a manner that will allow for this to occur.

Should the Commission disapprove of Kentucky Power's compliance plan, then Kentucky Power requests rehearing of the March 12, 2007 Order. As grounds, Kentucky Power states that any Order that requires Kentucky Power to collect, subject to refund, environmental

compliance costs in addition to the \$164,109 authorized in this case subject is an unlawful extension of the Commission's authority under KRS 278.183.

Accordingly, Kentucky Power requests that the Commission approve its plan for compliance with the Commission's Order of March 12, 2007.

Respectfully submitted,



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COMPANY

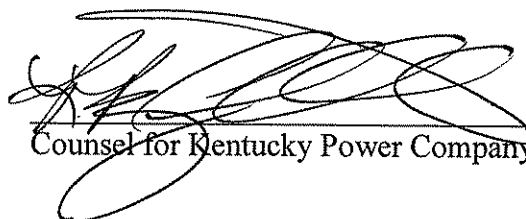
**CERTIFICATE OF SERVICE**

I hereby certify that a true and accurate copy of the foregoing was served by first class mail, postage prepaid, upon the following:

Michael L. Kurtz  
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Elizabeth E. Blackford  
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Suite 200  
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on this 4th day of April, 2007.



Counsel for Kentucky Power Company

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AN EXAMINATION BY THE PUBLIC SERVICE	)	
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POWER COMPANY FOR THE SIX-MONTH	)	CASE NO.
BILLING PERIODS ENDING DECEMBER 31, 2002,	)	2006-00128
DECEMBER 31, 2003, JUNE 30, 2004,	)	
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O R D E R

On February 20, 2007, the Attorney General of the Commonwealth of Kentucky, by and through his Office of Rate Intervention ("AG"), filed a petition for rehearing of the Commission's January 31, 2007 Order granting Kentucky Power Company ("Kentucky Power") authority to increase its jurisdictional environmental revenue requirement by \$95,494 in each of the first 6 billing months after the date of the Order. Specifically, the AG requests that the Commission amend the January 31, 2007 Order to require the environmental costs associated with the out-of-state generating facilities that are included in the environmental surcharge to be collected subject to refund and to require Kentucky Power to maintain its records in such a manner that would allow appropriate refunds to be made should refunds be required.

The authorized 6-month increase in the jurisdictional environmental revenue requirement results from the Commission's determination that Kentucky Power had under-recovered its environmental surcharge during the review periods at issue and

during the seven expense months subsequent to the review periods.<sup>1</sup> A portion of that under-recovery included costs associated with out-of-state generating facilities. In Case No. 2005-00068,<sup>2</sup> the Commission approved Kentucky Power's request to amend its environmental compliance plan and its environmental surcharge mechanism to permit the recovery of certain environmental costs associated with out-of-state generating facilities. The AG and the Kentucky Industrial Utility Customers, Inc. ("KIUC") appealed the Commission's decision in that case to the Franklin Circuit Court, arguing that it was inappropriate to include the environmental costs associated with the out-of-state generating facilities in Kentucky Power's environmental surcharge. On October 30, 2006, the Franklin Circuit Court upheld the Commission's decision holding that costs related to the out-of-state generating facilities did qualify for environmental surcharge recovery pursuant to KRS 278.183. The AG and KIUC have appealed the Franklin Circuit Court decision to the Kentucky Court of Appeals.

On March 6, 2007, Kentucky Power filed its response in opposition to the AG's petition for rehearing and put forth two arguments in support of its opposition. First, Kentucky Power argues that since the AG did not raise the issue of making the surcharge collections subject to refund during the processing of the review case, he is prohibited by KRS 278.400 from raising the issue on rehearing. Second, Kentucky Power contends that the AG is asking the Commission to presume the September 7,

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<sup>1</sup> January 31, 2007 Order at 4-5.

<sup>2</sup> Case No. 2005-00068, Application of Kentucky Power Company for Approval of an Amended Compliance Plan for Purposes of Recovering Additional Costs of Pollution Control Facilities and to Amend Its Environmental Cost Recovery Surcharge Tariff, final Order dated September 7, 2005.

2005 Order in Case No. 2005-00068 was improper and invalid. Kentucky Power states that the Commission's Orders are presumed valid and continue in full force unless and until modified or vacated by a court of competent jurisdiction. Kentucky Power argues that if the AG believes the environmental costs in question should be collected subject to refund, then the AG should appeal the January 31, 2007 Order and ask for relief from the Franklin Circuit Court. Kentucky Power notes that if the Commission's January 31, 2007 decision is reversed, then the refund question can be addressed by the parties. Kentucky Power reasons that until that time, the AG's request is premature and it is improper to utilize the provisions of KRS 278.400 to plan for a contingency that may never occur.

In previous cases where an issue has been appealed and the outcome of that appeal is not known at the time the Commission is required to enter another Order addressing that same issue, the Commission has found that public policy requires the Commission to recognize the uncertainties surrounding that issue. Under those circumstances, the Commission has found it reasonable to require that the revenues associated with the disputed issue be collected subject to refund.<sup>3</sup> Kentucky Power has failed to persuade the Commission that similar treatment is not justified in this case.

Therefore, the Commission finds that the AG's request for rehearing should be granted and the environmental surcharge collections authorized in the January 31, 2007

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<sup>3</sup> See Case No. 2002-00107, An Adjustment of Rider AMRP of The Union Light, Heat and Power Company, final Order dated August 30, 2002 and rehearing Order dated October 7, 2002; Case No. 2003-00103, An Adjustment of Rider AMRP of The Union Light, Heat and Power Company, final Order dated August 25, 2003; and Case No. 2004-00098, An Adjustment of Rider AMRP of The Union Light, Heat and Power Company, final Order dated August 24, 2004.



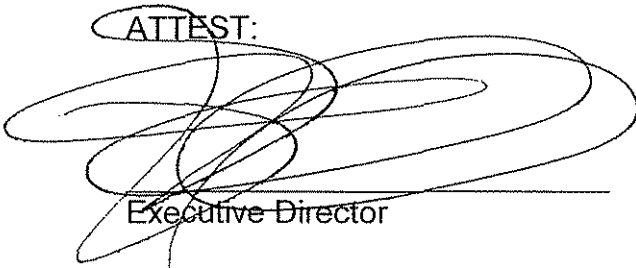
Order that are associated with out-of-state generating facilities should be collected subject to refund and that Kentucky Power should maintain its records in such a manner that Kentucky Power, the Commission, or any of Kentucky Power's customers will be able to determine the amounts to be refunded and to whom if the Court should rule that these costs are not eligible for recovery pursuant to KRS 278.183.

IT IS THEREFORE ORDERED that the AG's request for rehearing is granted in that the January 31, 2007 Order is amended to require all environmental surcharge collections associated with the costs of out-of-state generating facilities to be collected subject to refund and to require Kentucky Power to maintain its records in a manner that will permit refunds of these costs to be made should refunds be required by the Courts.

Done at Frankfort, Kentucky, this 12th day of March, 2007.

By the Commission

ATTEST:



Executive Director