COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

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PUBLIC SERVICE COMMISSION

In the Matter of:

AN EXAMINATION BY THE PUBLIC SERVICE COMMISSION OF THE ENVIRONMENTAL SURCHARGE MECHANISM OF KENTUCKY UTILITIES COMPANY FOR THE SIX-MONTH BILLING PERIODS ENDING JULY 31,2003, JANUARY 31, 2004, JANUARY 31,2005, JULY 31,2005, AND JANUARY 31,2006 AND FOR THE TWO-YEAR BILLING PERIOD ENDING JULY 31, 2004	)	CASE NO.2006-00129

and

AN EXAMINATION BY THE PUBLIC SERVICE COMMISSION OF THE ENVIRONMENTAL SURCHARGE MECHANISM OF LOUISVILLE GAS AND ELECTRIC COMPANY FOR THE SIX-MONTH BILLING PERIODS ENDING OCTOBER 31,2003, APRIL 30,2004, OCTOBER 31,2004, OCTOBER 31, 2005, AND APRIL 30,2006, AND FOR THE TWO-YEAR BILLING PERIOD ENDING APRIL 30,2005	)	CASE NO.2006-00130

COMMENTS AND BRIEF OF THE ATTORNEY GENERAL

For the stated reason of addressing class contribution to purported base rate cost of service inequities remaining after the most recently established base rates, in their applications the Companies posit an alternative allocation for the Commission's consideration. The alternative allocation would incorporate into base rates the revenue requirements for the environmental costs heretofore collected via the surcharge on a basis other than: (1) that which has been utilized for the monthly surcharge collection of those costs, and (2) a total revenues allocation flowing from the total revenues flowing from the allocation of the base revenue

requirements in the Companies' most recent base rate cases to produce the existing base rates.

This alternative both must and should be rejected because KRS 278.183 does not authorize the use of the two-year incorporation of the surcharge amounts into the existing base rates to address base rate cost of service contributions/subsidies or to create changes in allocated responsibility for contribution to revenue requirements approved in the general rate case. Furthermore, the alternative proposal both must and should be rejected because the base rates found fair, just and reasonable in the Companies' last base rate cases are producing the revenues they were designed to produce without any change to warrant a finding under KRS 278.270 that those base rates are unjust, unreasonable or insufficient. Rather than an incorporation of surcharge amounts into existing base rates, the Companies' proposal to allocate the revenue requirement associated with the environmental costs previously collected by surcharge in amounts designed to address base rate cost of service issues by realigning the overall revenues collected from each class is nothing short of a base rate change, and would require action by the Commission under KRS 278.270.

KRS 278.183 is a cost recovery statute designed to allow the utility to recover added revenues for environmental compliance costs outside of a general rate case as an incentive for utilities to consider scrubbing as an alternative to fuel switching in achieving compliance. *Kentucky Industrial Utility Customers v Kentucky Utilities*, 983 S.W.2d 493 at 501(Ky. 1998); also see, Preamble to Senate Bill 342, now codified as KRS 278.183, 1992 Acts of the General Assembly, Chapter 102, pp. 521-522. The statute is specifically designed to avoid a base rate case and does not attempt to address base rates issues. Opening with the language, "[n]otwithstanding any other provision of this chapter," KRS 278.183 is clearly designed to be self-contained, acting on its own rather than in concert with KRS 278.030, 278.080, 278.190 and

278.270. The use of KRS 278.183 to address any base rate issue is entirely contrary to the incentive benefit of cost recovery accomplished outside of a general rate case, is beyond the scope of the statute, and is thus well outside its intended function.

The right to cost recovery outside of a general rate case is a new right, separate and apart from the rights to base rate recovery set out under other provisions of Chapter 278. *Kentucky Industrial Utility Customers,* Id.at 500. (The surcharge creates a new right for all electric utilities, that is, the right to recover expenses as well as a return on and a return of capital costs associated with environmental projects without filing a general rate case. These new rights and responsibilities did not exist before the enactment of the surcharge). In KRS 278.183, a statute otherwise replete with specifics about what is to be considered and how and when that consideration is to occur, the rectification of purported class subsidies in base rates is not established as an issue to be considered by the Commission. KRS 278.183 (3) specifically states that every two years the Commission is to: "review and evaluate past operation of the surcharge...disallow improper expenses...and...**incorporate surcharge amounts** found just and reasonable **into the existing base rates** of the utility." For the so-called roll-in, the statute's charge to the Commission is to "incorporate" surcharge amounts found just and reasonable "into the existing base rates." The charge is not to create *de facto* base rate allocation changes and the consequent new base rates by manipulating the allocations of the environmental compliance revenue requirements during the roll-in. The alternative methodology designed to move the classes' base rate contributions closer to the base rate cost of service does not accomplish the incorporation of surcharge amounts into existing base rates.

The Companies have pointed out that KRS 278.183 does not specify how the roll-in is to occur and take this as leave to use the statute as a tool to address base rate issues. That contention

is clearly erroneous -- the statute does specify what is to be done, and it does not include the creation of new allocations of base rate revenue requirements in the process. Regardless, if the contention were true, the issue the Companies now suggest should be addressed is that the long lapse of time between general rate cases has meant that the doctrines of gradualism and rate continuity have not been in play to accomplish the gradual cost of service contribution shifts that would have occurred absent KRS 278.183, when the Companies would have been forced to come in for more regular general rate cases. That passage of time is a direct consequence of the success of KRS 278.183 in doing its job: allowing the Companies obtain rate increases outside of general rate cases. To say that KRS 278.183 should also now be used to address base rate case issues is to have one's cake and eat it too. Not having general rate cases means foregoing both the consequences and benefits of general rate cases. It does not make general rate case issues the concern of KRS 278.183 or permit its use to address such issues. General rate case issues are not the concern of this statute, and it neither can nor should be manipulated into use for such purposes. Furthermore, such a use of KRS 278.183 is prohibited by KRS 278.270.

Existing base rates consequent to the general rate case are the product of applying each class's allocated share of that total revenue requirement to each class in order to create a rate that will generate that class's allotted portion of that revenue requirement. Changing the portion of the base revenue requirement for which each class is responsible in the course of moving the collection of the additional compliance-related revenue requirements from the surcharge into the base rates goes far beyond incorporating the new revenue requirements into the existing base rates by changing the existing base rates. If a class is to pay a greater or lesser share of a **base** rate revenue requirement than it did under the rates that reflect the rate case allocation approved in the last general rate case, then that is a change in the existing **base** rates. The statue does not

provide for the change of existing base rates and a methodology that deliberately affects such a change is wholly contrary to the express provisions of KRS 278.183 (3).

The Companies' alternative proposal is presented as a way to affect changes in the existing base rates recently found fair, just and reasonable. Not so much as a nod is given to the requirement of KRS 278.270 that a finding must be made that the prior rate is unjust, unreasonable, insufficient, unjustly discriminatory or otherwise in violation of the chapter as a prerequisite to establishing a new just and reasonable rate to be followed in the future. The existing base rates, the rates found fair, just and reasonable in the Companies' most recent base rate cases, are operating as they were expected to operate. All parties knew the expected contribution of each class to the base rate cost of service when the allocation methodology was proposed to the Commission as just and reasonable in the recent general rate cases. The Commission accepted the proposal and found the rates thus established to be fair, just and reasonable. The Companies make no claim that the existing rates are not performing exactly as expected and say only that purported inequities present when the rates were established continue to exist.[1] This is not a change of circumstance that renders the existing base rates unjust, insufficient, or unreasonably discriminatory or allows the prescription of new rates for any class to be followed in the future under KRS 278.270.

KRS 278.183 cannot and should not be used to implement policies it does not address or to affect results with which it is not concerned. The Commission should continue to refuse to use KRS 278.183 to manipulate base rate case cost of service in the course of incorporating the surcharge amounts into the existing base rates under Subsection (3) of the statute, just as it

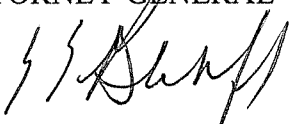
[1] See both Kentucky Utilities' and Louisville Gas & Electric's Responses to Attorney General Request for Information, Question 3 (F) and (G) and Question 10.

refused to use Subsection (2) of the statue to do so in PSC Cases numbers 93-465,[2] 2004-00421[3] and 2004-00426[4] when establishing the allocation of the revenue requirement to be collected by surcharge from each class.

Instead, the Commission should continue the incorporation of the surcharge into existing base rates under the first method proposed by the Companies, which is the method that is consistent with that the Commission has previously used for such roll-ins and with the requirements of KRS 278.183 (3).

Respectfully submitted,

GREGORY D. STUMBO
ATTORNEY GENERAL



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[2] *In the Matter of: The Application of Kentucky Utilities Company to Assess a Surcharge Under KRS 278.183 to Recover the Costs of Compliance with Environmental Requirements for Coal Combustion Wastes and By-Products.*
[3] *In the Matter of the Application of Louisville Gas and Electric Company for Approval of its 2004 Compliance Plan for Recovery by Surcharge.*
[4] *In the Matter of the Application of Kentucky Utilities Company for Approval of its 2004 Compliance Plan for Recovery by Surcharge.*

NOTICE OF FILING AND CERTIFICATION OF SERVICE

I hereby give notice that I have filed the original and nine true copies of the foregoing with the Executive Director of the Kentucky Public Service Commission at 211 Sower Boulevard, Frankfort, Kentucky, 40601 this the 28th day of September, 2006, and certify that this same day I have served the parties by mailing a true copy, postage prepaid, to the following:

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