

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

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PUBLIC SERVICE
COMMISSION

In the Matter of:

AN INVESTIGATION OF THE)
ENERGY AND REGULATORY) ADMINISTRATIVE
ISSUES IN SECTION 50 OF) CASE NO. 2007-00477
KENTUCKY'S 2007 ENERGY ACT)

ATTORNEY GENERAL'S COMMENTS

Comes now the intervenor, the Attorney General of the Commonwealth of Kentucky, by and through his Office of Rate Intervention (hereinafter the "Attorney General"), and tenders the following comments in the above-styled matter.

I. Introduction

As part of Section 50 of House Bill 1, enacted by the General Assembly during its 2007 special session, the Public Service Commission was directed to examine and make recommendations to the Legislative Research Commission ("LRC") in regard to four issues contained within Section 50 of the 2007 Energy Act. These issues are as follows:

1. Eliminating impediments to the consideration and adoption by utilities of cost-effective demand-side management strategies for addressing future demand prior to Commission consideration of any proposal for increasing generation capacity;
2. Encouraging diversification of utility energy portfolios through the use of renewables, and distributed generation;
3. Incorporating full-cost accounting that considers and requires comparison of life-cycle energy, economic, public health, and environmental costs of various strategies for meeting future energy demand; and,

4. Modifying rate structures and cost recovery to better align the financial interests of the utility with the goals of achieving energy efficiency and lowest life-cycle energy costs to all classes of ratepayers.

To facilitate this task, the Commission retained an expert consultant to assist in performing the investigation and the evaluation of the data gathered from participants. The consultant sought information from the various stakeholders which included the six (6) electric jurisdictional utilities consisting of Louisville Gas and Electric, Kentucky Utilities, Duke Energy Kentucky, Kentucky Power Company, Big Rivers Electric Corporation and East Kentucky Power Cooperative. The Office of the Attorney General was also made a party and, in addition, the following groups also petitioned for intervention and were granted full intervenor status in the case: 1) Kentucky Industrial Utility Customers, Inc., 2) the Sierra Club, 3) the Association for Community Ministries, People Organized and Working for Energy Reform, 4) Kentucky Association for Community Action, and 5) Community Action Council for Lexington-Fayette, Bourbon, Harrison and Nicholas Counties, Inc.

Evidence was gathered from the participants in the form of data requests to the parties along with participant interviews and pre-filed testimony. The consultant has submitted a written report of its findings and recommendations and will provide assistance to the Commission in preparing its final report to the LRC. A public hearing on the matter is scheduled for April 30th, 2008 at the Commission.

The final report to the LRC is to be submitted by the Commission by July 1, 2008.

II. Attorney General Comments

The Attorney General has reviewed the record including the consultant's report and its recommendations. The Attorney General provides the following comments to address the

recommendations of the consultant which should serve as the foundation for any decision by the Commission. These comments, however, should not be interpreted by any party as a statement of the Attorney General's opinion as to whether the Commission has the authority to implement any of the recommendations absent specific statutory authority.

Recommendation No. 1

In order to properly consider and develop policies, practices and programs adopted by the Commission from recommendations contained in this report, input from non-utility stakeholders, as well as the utilities should be solicited. This input may be developed from workshops sponsored by the Commission Staff, or more formal proceedings, as the Commission deems appropriate.¹

The Attorney General offers no comment regarding this recommendation other than to say that this proceeding is indicative of the Commission's attempt to gather input from the various stakeholders prior to the issuance of a final report to the legislative research commission.

Recommendation No. 2

The Commission should develop a set of standards for how to evaluate the benefits of proposed DSM programs. Such standards should broadly specify the range of benefits to be recognized and the appropriate analytical approaches for evaluating future benefits. The standards should recognize the variety of benefits created by DSM, while also acknowledging that DSM cannot be substituted for power plant development on an undifferentiated basis. The standards should require the development and application of screening models sophisticated enough to systematically compare and contrast the relative attractiveness of alternative DSM options in different settings.²

The Attorney General agrees with the recommendation.

Recommendation No. 3

The Commission should develop or adopt recognized measurement and verification guidelines, so that actual results of DSM programs can be independently assessed and validated. In order to legitimize program continuation, DSM program benefits should be linked to measured and verified achievements, as much as practically possible.³

¹ Report of Overland Consulting, p 42

² Report of Overland Consulting, p 53

³ Report of Overland Consulting, p 53

The Attorney General strongly agrees with the recommendation and suggests that the Commission also consider whether the use of “engineered savings” by utilities in evaluating program impacts is appropriate. “Engineered savings” are derived from the use of statistical estimates of savings based on the measure employed and an estimate of its impact on the energy consumption of a participant. From recent DSM applications, it appears that many of the jurisdictional utilities are relying nearly exclusively upon the use of engineered savings to justify their recovery of funds.

Jurisdictional utilities have claimed that to require engineered savings be verified using actual results, as measured at the participants electric meter, would be burdensome, expensive, and unreliable. They claim that savings may not be readily apparent due to the fact that a *participant may add new appliances or devices during the evaluation period* or that consumption may vary due to other factors. However, utilities already possess historical usage information on the majority of their customers. This information could be used to correct for any large, abnormal variations in consumption. Further, such abnormalities could even be discounted entirely if a large enough sample is utilized. As has been seen from recent applications, the utilities and their evaluation vendors are quite adept at the development of customer surveys to estimate engineered savings. In fact, one recent application purported to estimate the number of hours a CFL would be in use by participants on average based on the participants’ responses to a survey question. It would seem that the addition of a few simple questions relating to the purchase or use of a new appliance by the participant would overcome any concerns of the utilities. The Attorney General notes that actual results must also be used as part of any evaluation as *this is the only reliable way to verify that claimed savings bear some reasonable relationship to the savings actually received by participants, who are funding these programs.*

The Attorney General maintains that at least 5% of participants in any program should be subject to verification using actual results.

Finally, the Commission should adopt standards for utility companies to use in evaluating vendors offering measurement and verification services to utilities. A list of “approved vendors” of such services supplied from the utilities could then be maintained by the Commission. Such a list would ensure that evaluations were being performed uniformly by such vendors and lend confidence that results were accurately, fairly and consistently reported.

Recommendation No. 4

The KPSC should consider the need to revise the DSM statute to expressly authorize the KPSC to act on its own initiative or direction to investigate and direct utilities to implement particular DSM programs, the costs of which would be recovered by the surcharge.⁴

The Attorney General interprets this recommendation to also include the specification of standard DSM programs which would share the same, or substantially similar, program design and recovery mechanisms. With that understanding, the Attorney General agrees with this recommendation. While some DSM programs offered by individual utilities are tailored to fit the specific needs of their demographic areas, there are programs that are common enough within and among the industry to warrant the Commission to order their implementation across all the jurisdictional utilities. Specific examples would include weatherization services, home audits, and electrical control of condensing units and/or water heaters in load shedding programs. Programs such as these are typically offered by all the jurisdictional utilities and the public would benefit from the implementation by the PSC of program standards which would ensure that consistent services are offered by utilities throughout the state. Additionally, such

⁴ Report of Overland Consulting, p. 54

standardization would also assist in the evaluation of program results with the addition of standardized reporting requirements.

Recommendation No. 5

Rules governing industrial customer exclusion from DSM program participation should be clarified, standardized, and uniformly applied. It is important that customers who seek to opt-out of the DSM program make a showing of their own energy efficiency efforts, before they are allowed an exemption from the DSM surcharge and related programs.⁵

The Attorney General agrees with this recommendation. Although, there are some large industrial customers who are currently very focused on their energy consumption and take appropriate steps to employ energy saving measures in their manufacturing processes, a reporting requirement to verify that exclusion from the DSM tariff is appropriate and should cause little inconvenience to these customers. Given that roughly half of the electricity consumed in the state is by industrial customers, to exclude the entire class based on the activities of a few makes little sense. The same reasons which justify the inclusion of all residential customers within the DSM tariff also apply in the case of industrial customers and the inclusion of industrial customers would add to efforts to reduce energy consumption statewide. There appears to be no reasonable basis for their continued exclusion. While the elimination of the statutory exclusion is the prerogative of the legislature, the Commission should consider whether the exclusion for industrial customers be re-examined.

Recommendation No. 6

As new DSM programs are brought before the Commission that clearly reduce system costs, it should consider if such programs should be more properly allocated to all jurisdictional customers.⁶

⁵ Report of Overland Consulting, p 56

⁶ Report of Overland Consulting, p 57

The Attorney General agrees with the recommendation.

Recommendation No. 7

Greater efforts should be made to make utility customers aware of energy conservation and DSM programs. Additional utility resources should be committed to customer education programs sponsored by the utilities or independent third parties. The KPSC may also release public information communications that support energy efficiency programs.⁷

The Attorney General interprets this recommendation to suggest that additional efforts be made to inform the general public about the various DSM programs and services offered by the jurisdictional utilities and the program benefits to participants. With that understanding, he generally supports the recommendation. However, these efforts should be targeted to increase enrollment in specific programs. “Generic” messages which encourage energy conservation but do not relate to a specific program, are not appropriate uses of ratepayer funds.

Recommendation No. 8

Assuming that proper utility incentives and recovery mechanisms are in place, utilities should consider providing or expanding rebates or financing programs to support customer investment in energy efficiency and DSM programs; especially those that are likely to reduce peak demand. A set of pre-approved technology types may be promoted to customers through education and incentives showing the expected payback characteristics for each technology.⁸

The Attorney General believes that the use of customer incentives should be carefully considered prior to approval by the Commission. While incentives may be appropriate as part of a specific DSM program, the use of incentives should be examined to determine whether the incentive plays any part in encouraging customer participation in an individual program and the appropriate amount of any incentive to be offered. Because incentives are financed through money collected from ratepayers, the Commission should be cautious and ensure that such

⁷ Report of Overland Consulting, p. 57.

⁸ Report of Overland Consulting, p. 58.

incentives are properly and reasonably used by any specific program. Further, any programs offered should be made available equally to all members of the class from which the funds are collected.

Recommendation No. 9

The Commission should consider the need to revise the current DSM application and approval process to accelerate the procedural timeline for projects below a defined funding level. The standard of review for modifications to current programs, or programs under a specified budget amount, should be further streamlined to accommodate increased participant interest in successful programs.⁹

The Attorney General disagrees with this recommendation as his office believes it is not necessary given the fact that the Commission has great latitude in setting the procedural schedule for any specific filing.

Recommendation No. 10

The KPSC may wish to consider whether to recommend an RPS target to the General Assembly, consistent with similar initiatives in many other states. If it does so, we recommend that the target be voluntary, providing financial incentives for Kentucky utilities who choose to comply. The target must be realistic and cost effective in light of Kentucky geological constraints, with a range of perhaps 5 to 10% of energy served, graduated to 2020.¹⁰

The Attorney General takes no position on this recommendation because nearly all of the jurisdictional utilities are already pursuing RPS options on their own accord. Therefore, with the suggested recommendation merely advocating a voluntary RPS target, it does not appear that any action is necessary at this time.

⁹ Report of Overland Consulting, p. 58

¹⁰ Report of Overland Consulting, p. 69

Recommendation No. 11

The Commission should consider the need to provide for fast track applications for small-scale generation, possibly as part of a more formalized Standard Offer Contract process.¹¹

The Attorney General has no comment on this recommendation.

Recommendation No. 12

To properly compensate utilities for increased renewables project risks, and to attract utility commitments to these investments, the Commission should consider allowing a premium of up to 300 basis points over the latest authorized rate of return for these investments.¹²

The Attorney General does not agree with the recommendation. While there are risks associated with investment in renewable energy sources, the risks associated with conventional generation sources are rapidly increasing. In light of these increasing risks, the jurisdictional utilities are already pursuing renewable projects without the need for further incentives or premiums. The Attorney General strongly supports renewables and is open to discussion on the means by which to accomplish investment in same.

Recommendation No. 13

One of the solutions to the renewable market pricing problem could be a KPSC requirement for utilities to use an RFP process for all resources, based on IRP, or just renewables, where the contracts signed with the winners would include a capacity component in the remuneration.¹³

The Attorney General has no comment on this recommendation.

Recommendation No. 14

Uniform standards, at least by utility, for net metering and interconnection should be developed, as set forth in a tariff. Current limits on technology restrictions should be reconsidered, as well as limits on total participation levels. Finally, current limits on generating capacity should also

¹¹ Report of Overland Consulting, p 70.

¹² Report of Overland Consulting, p 71

¹³ Report of Overland Consulting, p 72

be relaxed to facilitate the potential for development of distributed generation projects, sizing projects appropriate to each technology.¹⁴

From the responses of the utilities to the data requests and as noted within the report, it appears that there is little or no customer participation and/or interest at this time. Therefore, the Attorney General offers no comment on this recommendation

Recommendation No. 15

We do not believe that Commission responsibility for statewide planning is either practical or particularly beneficial, given the reality that utilities, regulated or not, do not engage in Kentucky-level system planning that would necessarily result in any joint development or operation of generation resources.¹⁵

The Attorney General agrees with this recommendation.

Recommendation No. 16

The current statute defining the CPCN process should be modified to require the consideration of demand and supply-side alternatives including; IPP and merchant power options; energy efficiency and DSM programs; and renewable alternatives.¹⁶

The Attorney General agrees with the recommendation.

Recommendation No. 17

Until such time as anticipated federal legislation is formally enacted addressing carbon emission standards, utility IRP and CPCN filings should provide best available estimates of expected carbon impacts in justifying resource selections among portfolio options.¹⁷

The Attorney General agrees with the recommendation.

Recommendation No. 18

Utilities should be required to file avoided cost data (not less than annually), subject to the review and approval of the Commission. Consideration of energy efficiency and DSM programs, as well as renewables projects, should be measured against the appropriate avoided costs.

¹⁴ Report of Overland Consulting, p. 73

¹⁵ Report of Overland Consulting, p. 83

¹⁶ Report of Overland Consulting, p. 84

¹⁷ Report of Overland Consulting, p. 94

Programs that reliably reduce peak load should be evaluated against the avoided cost of both demand and energy.¹⁸

The Attorney General agrees with the recommendation.

Recommendation No. 19

The Commission should not require the recognition of environmental or public health externalities in the IRP or certificate processes, unless it finds it appropriate to specifically direct a utility (or utilities) to do so.¹⁹

The Attorney General agrees with the recommendation and notes that any recognition of environmental or public health externalities would need to account for both societal costs and benefits. As these costs and benefits are difficult to determine with any precision, they are properly excluded from consideration.

Recommendation No. 20

Assuming that the results of current pilot programs are positive, TOU rates and RTP should be more broadly applied to industrial customers in the future.²⁰

While the Attorney General supports the recommendation, his office reserves the right to object to any specific proposal or program offered by any jurisdictional utility.

Recommendation No. 21

The current DSM Surcharge mechanism should be modified. Utility expenditures (capital, and operating costs related to the period of the program) should be capitalized, with amortization based on the estimated period of program benefits. Utilities should be allowed a minimum return of 100 bp higher than the most recent authorized rate of return in the utility's last rate proceedings. Utilities should be allowed to receive additional incentives based on the actual benefits achieved relative to appropriate targets from energy efficiency and DSM programs. Assuming that program targets are met, these incentives should provide a reasonable opportunity to earn a graduated return of up to 300 bp over the minimum premium, based on results.²¹

¹⁸ Report of Overland Consulting, p 96

¹⁹ Report of Overland Consulting, p 96

²⁰ Report of Overland Consulting, p 105

²¹ Report of Overland Consulting, p 106

The Attorney General does not agree with the recommendation. The current method reflects more of a “pay-as-you-go” type system with a true-up period utilizing review by the Commission of program performance and expenditures. This review ensures that programs are cost effective, expenditures are reasonable and prudent and that programs are meeting their performance targets. Based on the level and scope of DSM programs currently offered and proposed by the jurisdictional utilities, it does not appear that any change in this method is necessary. Under the current method, utilities already receive an incentive under the existing statute that is appropriate and which has encouraged DSM program development and implementation. DSM funds are collected from customers, there are no utility funds invested. Therefore, there is no need to use additional premiums or incentives over and above the most recently authorized rate of return of a utility.

Recommendation No. 22

The DSM statute and advertising regulation should be modified to provide explicit authority for advertising costs associated with DSM and energy efficiency programs. The advertising regulation should be amended with regard to its definition of “promotional advertising” to eliminate potential conflicts with the promotion of energy efficient equipment; programmable thermostats; smart metering devices; etc.²²

The Attorney General does not agree with the recommendation as his office does not believe that a conflict exists. The Attorney General refers to his comments regarding Recommendation No. 7.

Recommendation No. 23

A new surcharge should be created to include and accelerate expenditures associated with efficiency improvements in utility generation facilities. The rate of return on Commission approved projects should be 50 bp higher than the most recent authorized return in the utility's rate proceedings.²³

²² Report of Overland Consulting, p. 107

²³ Report of Overland Consulting, p. 108

The Attorney General disagrees with the recommendation. The jurisdictional utilities already have incentives to increase efficiency levels in their generation facilities as part of the general rate-making process. If a company increases its operational efficiencies, then they may experience returns in excess of their authorized rate of return. This opportunity is already available to the utilities. The incentive as proposed does not appear necessary; however, the Attorney General is open to modification to ensure these incentives continue. Additionally, as argued by the Attorney General in other matters, an explicit grant statutory power would be necessary to implement the recommendation. Such statutory power is not currently within the purview of the Commission.

Recommendation No. 24

All regulated Kentucky utilities should be required to develop and offer a “Green Energy” optional tariff for their residential customers.²⁴

The Attorney General notes that the report indicates that the jurisdictional utilities either already offer a version of the recommended tariff or are considering one in the near future. While the Commission should encourage the voluntary implementation of a “Green Energy” tariff, the Attorney General would recommend the Commission defer to the individual utility and allow them to determine whether a “Green Energy” tariff would be appropriate to offer their customers.

Recommendation No. 25

The Commission should provide for additional staffing, and relevant training, necessary to support increased activities associated with IRP, DSM, Environmental Surcharge, Certificate, and other filings. The Staff additions would also monitor federal and state energy legislation,

²⁴ Report of Overland Consulting, p 109

*industry research and programs, and Kentucky regulated utility parent-company activities. Staff resources may need to be further supplemented to support increasing requirements over time.*²⁵

The Attorney General defers to the Commission on any such need.

Recommendation No. 26

*The General Assembly should consider explicit support of these Commission initiatives to further encourage the utility industry response, and to limit financial risks associated with these utility commitments.*²⁶

The Attorney General maintains that certain initiatives should be supported but not all as recommended by the consultant's report. Thus, he can not agree with the recommendation as worded. Moreover, the recommendation appears to ignore the financial consequences to the ratepayers. The financial impact on the ratepayers must likewise be considered with any initiative.

Recommendation No. 27

*In support of the development of Section 50 objectives, the General Assembly may wish to work with utilities in developing securitization bond funding in support of qualifying conservation investments and environmental mandates, including advanced-coal technologies. Access to capital at a reduced cost will help bring these programs to fruition on a more economic basis, and will result in lower energy rates.*²⁷

The Attorney General agrees with the recommendation.

Recommendation No. 28

*Any potential customer increase in rates due to programs effective on or after January 1, 2009, which are recoverable by operation of the proposed surcharges contained in this report, should be considered in light of other cost increases in base rates, FAC, or other charges. If the Commission finds it appropriate to do so, it may impose a rate cap on these costs for a particular period or periods. Approved costs, if any, that exceed the rate cap should be deferred for future recovery, including appropriate carrying costs.*²⁸

The Attorney General would agree with the implementation of a true rate cap, however, his office would not support the deferral of any uncollected, approved costs (including carrying

²⁵ Report of Overland Consulting, p 110

²⁶ Report of Overland Consulting, p 112.

²⁷ Report of Overland Consulting, p 113.

costs) to a later time.

Wherefore, the Attorney General tenders his comments and requests the Commission to incorporate them into its decision in this matter.

Respectfully submitted,

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CERTIFICATE OF SERVICE AND NOTICE OF FILING

I hereby give notice that this the 28th day of April, 2008, I have filed the original and ten copies of the foregoing Attorney General's Comments with the Kentucky Public Service Commission at 211 Sower Boulevard, Frankfort, Kentucky, 40601 and certify that this same day I have served the parties by mailing a true copy of same, postage prepaid, to those listed below.

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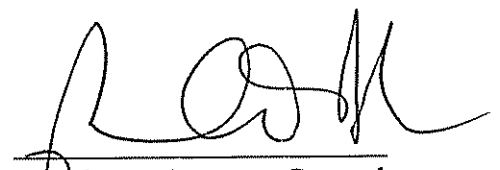
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