



S T O L L · K E E N O N · O G D E N
P L L C

2000 PNC PLAZA
500 WEST JEFFERSON STREET
LOUISVILLE, KY 40202-2828
MAIN: (502) 333-6000
FAX: (502) 333-6099
www.skofirm.com

W. DUNCAN CROSBY III
DIRECT DIAL: (502) 560-4263
DIRECT FAX: (502) 627-8754
duncan.crosby@skofirm.com

April 1, 2008

RECEIVED

APR 01 2008

**PUBLIC SERVICE
COMMISSION**

VIA HAND DELIVERY

Stephanie L. Stumbo
Executive Director
Kentucky Public Service Commission
211 Sower Boulevard
Frankfort, KY 40601

**RE: An Investigation of the Energy and Regulatory Issues in Section 50 of
Kentucky's 2007 Energy Act
Administrative Case No. 2007-00477**

Dear Ms. Stumbo:

Enclosed please find and accept for filing the original and ten copies of the Supplemental Testimony of Lonnie E. Bellar on behalf of Kentucky Utilities Company and Louisville Gas and Electric Company in the above-referenced matter. Please confirm your receipt of this filing by placing the stamp of your Office with the date received on the enclosed additional copies and return them to me in the enclosed self-addressed stamped envelope.

Should you have any questions please contact me at your convenience.

Sincerely,

W. Duncan Crosby III

WDC:ec
Enclosures as mentioned
cc: Parties of Record

400001.129032/517413.1

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In re 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)	

RECEIVED

APR 01 2008

PUBLIC SERVICE
COMMISSION

SUPPLEMENTAL TESTIMONY OF
LONNIE E. BELLAR
VICE PRESIDENT, STATE REGULATION AND RATES
E.ON U.S. SERVICES, INC.

Filed: April 1, 2008

1 **Q. Please state your name, position and business address.**

2 A. My name is Lonnie E. Bellar. I am Vice President, State Regulation and Rates for E.ON
3 U.S. Services Inc., which provides services to Kentucky Utilities Company (“KU”) and
4 Louisville Gas and Electric Company (“LG&E”) (collectively “the Companies”). My
5 business address is 220 West Main Street, Louisville, Kentucky.

6 **Q. What is the purpose of your testimony?**

7 A. The purpose of my testimony is to provide the Companies’ positions and proposals
8 concerning certain of the recommendations made in the Overland Consulting Report filed
9 in this proceeding on March 4, 2008.

10 **Q. Do the Companies believe the Commission should consider recommending that the**
11 **General Assembly revise the DSM statute to give the Commission express authority**
12 **to act on its own initiative or direction to investigate and direct utilities to**
13 **implement particular DSM programs, the costs of which would be recovered by the**
14 **surcharge?**

15 A. The Companies believe that such authority is unnecessary for several reasons. First, the
16 current DSM statute already has given rise to an impressive array of DSM and energy
17 efficiency programs in Kentucky, and utilities continue to propose more, and more
18 expansive, DSM and energy efficiency programs thereunder. For example, on March 31,
19 2008 in Case No. 2007-00319, the Commission approved the Companies’ application for
20 a significant portfolio of such programs, some of which are expansions of existing
21 programs, but the majority of which are new. Given the current abundance of such
22 programs among Kentucky’s utilities and the apparent momentum toward increasing the

1 number and scope of such programs, there simply is no need for the Commission to direct
2 utilities to implement particular programs.

3 Moreover, the Commission already possesses the requisite statutory authority to
4 encourage the development and implementation of new and expanded DSM and energy
5 efficiency programs by providing new and innovative kinds of incentives for utilities to
6 do so. As I testified previously in this proceeding, the Companies believe there are
7 several kinds of incentives the Commission should explore, including incentive rates of
8 return on equity (“ROE”) for capital investments in energy efficiency programs and fair,
9 reasonable, and equitable distributions of energy efficiency program savings between
10 customers and utility applicants. With innovative incentives like these and others, there
11 would be little, if any, need for the Commission to order utilities to implement DSM or
12 energy efficiency programs.

13 **Q. Is there a need for greater efforts to be made to make utility customers aware of**
14 **energy conservation and DSM programs? If so, should additional utility resources**
15 **be committed to customer education programs sponsored by utilities or independent**
16 **third parties?**

17 A. The Companies believe it is advisable to make greater efforts to increase the awareness of
18 their customers about the DSM and energy efficiency programs they offer, which is why
19 the Companies’ recently approved portfolio of such programs in Case No. 2007-00319
20 contains a significant public awareness and education component. That being said, the
21 Companies believe that before pursuing involvement of third parties in providing
22 customer education concerning DSM or energy efficiency programs, the effort must be
23 coordinated with, and perhaps supervised by, the utility concerned. On the whole, the

1 utilities themselves are likely to be the most familiar with both their customers and their
2 programs, and therefore likely to be best suited to provide customer education. Any
3 involvement of independent third parties should be coordinated with the utility involved
4 to ensure the quality and accuracy of the information being provided, as well as to ensure
5 there is no unnecessary duplication of efforts. The Commission, utility, and independent
6 third parties should also establish clearly how the third parties' efforts are to be funded.

7 **Q. Concerning the need to increase customer awareness of DSM and energy efficiency**
8 **programs, Overland recommends that the DSM statute, KRS 278.285, and the**
9 **Commission's regulation on utility advertising, 807 KAR 5:016, be amended to**
10 **remove what Overland sees as a conflict between the regulation's allowance of cost**
11 **recovery for energy conservation advertising and its disallowance of cost recovery**
12 **for advertising promoting the use of particular appliances. Do the Companies agree**
13 **that there is a conflict that requires revising either the DSM statute or the**
14 **Commission's advertising regulation?**

15 A. The Companies do not believe there is a conflict between the two different provisions of
16 the Commission's advertising regulation that Overland cites. The regulation prohibits the
17 Commission from taking into account an advertising cost for rate-making purposes unless
18 the advertising produces a "material benefit."¹ Among the kinds of advertising the
19 regulation defines as producing a material benefit is, "Advertising limited exclusively to
20 demonstration of means for ratepayers to reduce their bills or conserve energy [.]"²
21 Taken alone, this provision seems to allow a utility to recover the cost of advertising

¹ 807 KAR 5:016 § 2(1).

² 807 KAR 5:016 § 3(1)(a).

1 advocating for the use of energy-saving appliances, such as Energy-Star-approved
2 appliances or energy-saving compact fluorescent light bulbs (“CFLs”).

3 On the other hand, the regulation explicitly prohibits the recovery of promotional
4 advertising, including: “[A]ny advertising for the purpose of encouraging any person to
5 select or use the service or additional service of an energy utility, or the selection or
6 installation of any appliance or equipment designed to use such utility’s service.”³ The
7 thrust of this portion of the regulation seems clearly to be that energy utilities should not
8 recover from their customers the cost of being encouraged to use more energy, which
9 would include efforts to encourage customers to obtain and install additional energy-
10 consuming appliances.

11 The Companies’ view is that there is no conflict between the express language
12 and clear intent of the advertising regulation’s provision concerning bill-reduction and
13 conservation advertising and the clear intent of the provision concerning promotion of
14 additional energy usage. For example, though an energy utility’s advertisement
15 advocating that customers switch to energy-saving CFLs could, on a straitened
16 understanding of the regulation, be construed as promotional advertising “encouraging ...
17 the selection or installation of any appliance or equipment designed to use such utility’s
18 service[,]” such an understanding would rob the provision of its clear purpose and would
19 ignore the regulation’s provision construing conservation and bill-reduction advertising
20 as producing a “material benefit.” Therefore, rather than seeing a conflict between these
21 provisions of the advertising regulation, the Companies believe the clear intent of each
22 provision compliments the other; one allows cost recovery of conservation advertising,
23 while the other prohibits cost recovery of advertising advocating for increased energy

1 use. There is, therefore, no need to amend either the DSM statute or the utility
2 advertising regulation.

3 **Q. What is the Companies' position concerning Overland's recommendation that the**
4 **Commission should cause uniform standards to be developed and tarified, at least**
5 **by utility, for net metering and interconnection?**

6 A. With respect to the Companies, the recommendation is somewhat moot because they
7 already have net metering and interconnection tariffs. Their tariffs do not limit net
8 metering technology strictly to solar power, but also include wind and hydroelectric
9 generation sources, demonstrating the current authority of the Commission to approve
10 such tariffs. The Companies also already have interconnection tariffs for small and large
11 cogeneration facilities, negating any need to cover such facilities under net metering
12 tariffs.

13 Concerning all interconnections with the Companies facilities, it is the
14 Companies' position, reflected in their tariffs, that all customer-generators must bear the
15 costs for system interconnection and system upgrades to carry their load and power
16 production, and to protect the Companies' facilities from potential troubles the
17 customers' facilities could cause.

18 **Q. Please comment on Overland's recommendation that the Commission should create**
19 **a new surcharge to include and accelerate expenditures associated with efficiency**
20 **improvements in utility generation facilities, as well as Overland's related**
21 **recommendation that the rate of return on Commission-approved efficiency**
22 **improvement projects should be fifty basis points higher than the most recent**
23 **authorized return in a utility's rate proceedings.**

³ 807 KAR 5:016 § 4(1)(b).

1 A. Although the Companies support the concept of incentive ROEs, there are challenges
2 related to efficiency improvement projects that the Commission should consider. The
3 efficiency of fossil fuel generation is typically evaluated by the net heat rate, because it is
4 a direct measure of the amount of fuel required to produce a kilowatt hour of electrical
5 energy. Because less fuel results in lower costs, the Companies continuously search for
6 ways of improving the heat rates of their units. The Companies place a focus on testing
7 and reviewing approaches for making incremental efficiency improvements to existing
8 thermal generation in order to optimize performance.

9 However, improved heat rate largely depends on the design of the equipment and
10 the way in which the equipment is operated. As a result, heat rate improvement projects
11 may sometimes be difficult to justify solely on the potential for efficiency improvements.
12 For example, actual savings may not be realized if there is a change in operating
13 parameters, which can depend upon system load or other factors. Though utilities can
14 implement changes in equipment design which should result in improved efficiency,
15 system conditions may force utilities to operate individual units inefficiently at times in
16 order to maintain the reliability of the system. In addition, changes in environmental
17 regulations may require the addition of pollution control equipment that will reduce
18 overall efficiency due to increased auxiliary power requirements. Though some
19 regulations may require utilities to change the operating parameters of a unit in order to
20 reduce emissions, these changes can have the unintended effect of detrimentally
21 impacting efficiency.

22 In addition to operational and environmental challenges and concerns, it is
23 possible that modifying existing generation facilities in an attempt to increase efficiency

1 could necessitate federal New Source Review (“NSR”) procedures, which likely would
2 increase the cost of any efficiency project due to the Best Available Control Technology
3 requirements of NSR.

4 **Q. What is the Companies’ position concerning the suggestion that the General**
5 **Assembly may wish to work with utilities in developing securitization bond funding**
6 **in support of qualifying conservation investments and environmental mandates,**
7 **including advanced-coal technologies?**

8 A. The Companies agree that securitization would require statutory authority but do not see
9 a need for such authority at this time. There are several issues the Commission should
10 consider while deliberating on this suggestion. First, the Commission should take into
11 account the considerable amount of capital investment a utility would have to make to
12 justify the cost of arranging such financing. In other words, though there may be lower
13 costs of capital available through such financing, the cost of achieving the financing must
14 be considered. Second, though securitization is a valid approach for financing such
15 projects, utilities would not be able to earn a return on the investment, which is a
16 financial disincentive as compared to allowing utilities to earn ROEs on capital
17 investments associated with such programs or projects. Third, the Commission and
18 utilities must, even with securitized debt, be mindful of a utility’s debt-to-equity ratio and
19 ensure that a utility’s debt security financing does not have an adverse affect on the
20 utility’s cost of capital or ability to borrow in the future.

21 **Q. What concerns, if any, do the Companies have with respect to Overland’s suggestion**
22 **that the Commission may find it advisable to implement a rate cap on the costs of**
23 **DSM, energy efficiency, and other Section 50-related programs, allowing utilities to**

1 **defer for future recovery the approved costs for such programs in excess of the cap,**
2 **as well as appropriate carrying costs?**

3 A. The Companies generally disfavor rate caps, which create generational inequities for
4 customers and can impair utilities' ability to obtain low-cost financing in capital markets.
5 The net effect of these impacts likely would be to raise unnecessarily the cost of service
6 for future customers by increasing revenue requirements while financially weakening the
7 impacted utilities, potentially limiting their ability to undertake cost-effectively (or to
8 undertake at all) needed or desirable projects in the future by increasing their cost of debt.

9 **Q. Does this conclude your testimony?**

10 A. Yes.

VERIFICATION

COMMONWEALTH OF KENTUCKY)
) SS:
COUNTY OF JEFFERSON)

The undersigned, **Lonnie E. Bellar**, being duly sworn, deposes and says he is the Vice President State Regulation and Rates for E.ON U.S. Services Inc., that he has personal knowledge of the matters set forth in the foregoing testimony, and the answers contained therein are true and correct to the best of his information, knowledge and belief.

Lonnie E. Bellar

LONNIE E. BELLAR

Subscribed and sworn to before me, a Notary Public in and before said County and State, this 1st day of April 2008.

Jammy J. Ely (SEAL)

Notary Public

My Commission Expires:

November 9, 2010