

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

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| AN EXAMINATION BY THE PUBLIC SERVICE |) | |
| COMMISSION OF THE ENVIRONMENTAL |) | |
| SURCHARGE MECHANISM OF KENTUCKY |) | CASE NO. |
| POWER COMPANY FOR THE SIX-MONTH |) | 2012-00504 |
| BILLING PERIODS ENDING DECEMBER 31, 2011 |) | |
| AND JUNE 30, 2012 |) | |

ORDER

On November 30, 2012, the Commission initiated a six-month review of Kentucky Power Company's ("Kentucky Power") environmental surcharge¹ as billed to customers for the six-month periods July 1, 2011 to December 31, 2011, and January 1, 2012 to June 30, 2012.² Pursuant to KRS 278.183(3), the Commission must review, at six-month intervals, the past operations of the environmental surcharge. The Commission may, by temporary adjustment in the surcharge, disallow any surcharge amounts found not to be just and reasonable and reconcile past surcharge collections with actual costs recoverable pursuant to KRS 278.183(1).

The Commission issued a procedural schedule on November 30, 2012 that provided for discovery, the filing of prepared testimony, an informal conference and

¹ Kentucky Power was authorized to implement an environmental surcharge in Case No. 1996-00489, The Application of Kentucky Power Company d/b/a American Electric Power to Assess a Surcharge Under KRS 278.183 to Recover Costs of Compliance with the Clean Air Act and Those Environmental Requirements Which Apply to Coal Combustion Waste and By-Products (Ky. PSC May 27, 1997).

² Kentucky Power's surcharge is billed on a two-month lag. Thus, surcharge billings from July 2011 through December 2011 are based on costs incurred from May 2011 through October 2011; and the amounts billed from January 2012 through June 2012 are based on costs incurred from November 2011 through April 2012.

intervenor testimony. Kentucky Power filed prepared testimony, and responded to requests for information propounded by Commission Staff. On January 16, 2013, an informal conference was held at the Commission's offices to discuss the issues in this case. There were no parties requesting intervenor status to this proceeding. On March 28, 2013, an amended procedural schedule was issued indicating that, as there were no intervenors in the case, the last day for Kentucky Power to request a hearing or request that this case be submitted for decision based on the record would be ten days from the date of issuance of the Order. On April 2, 2013, Kentucky Power filed a response to the Commission's March 28, 2013 Order stating that there are no material issues of fact warranting hearing in this matter. Kentucky Power further stated that this case may be submitted for decision on the current record without a hearing. Since there are no intervenors in this case and a hearing is not necessary in the public interest, the Commission will adjudicate this case based on the evidence of record.

SURCHARGE ADJUSTMENT

The November 30, 2012 Order initiating this case indicated that, since the period under review in this proceeding may have resulted in over- or under-recoveries, the Commission would entertain proposals to adopt one adjustment factor to net all over- or under-recoveries. Kentucky Power stated that it had a net over-recovery of its environmental costs during the expense months of May 2011 through April 2012 in the amount of \$704,292.³ It proposed that the net over-recovery be refunded by decreasing the total jurisdictional environmental surcharge amount by a one-time adjustment of

³ Direct Testimony of Lila P. Munsey on Behalf of Kentucky Power Company, filed December 28, 2012 at 3.

\$704,292 in its first monthly surcharge filing following the Commission's decision in this proceeding.⁴

Having reviewed the record, the Commission finds Kentucky Power's calculation of a net over-recovery of \$704,292 to be reasonable. The Commission also finds reasonable Kentucky Power's proposal to refund the over-recovery amount by a one-time adjustment of \$704,292 in its first monthly surcharge filing following the date of this Order. Kentucky Power stated that the average residential customer's monthly usage for the 12 months ended April 3, 2012 is 1,298 kWh per month.⁵ Kentucky Power calculates that for a residential customer using 1,298 kWh per month, the impact of the over-recovery if the difference had been incorporated into the November 2012 bill would reduce the average-usage residential bill by approximately \$2.21.⁶

RATE OF RETURN

In Case No. 1996-00489, the Commission found that the debt portion of Kentucky Power's weighted average cost of capital should be reviewed and reestablished during each six-month review case, and that the rate of return on common equity would remain fixed and subject to review during the two-year environmental surcharge reviews. The weighted average cost of capital constitutes the rate of return applicable to Kentucky Power's environmental compliance rate base.⁷

⁴ *Id.*, at 13.

⁵ Response to Commission Staff's First Request for Information ("Staff's First Request"), Item 8.

⁶ *Id.*

⁷ This weighted average cost of capital is applied only to the environmental compliance rate base associated with plant installed at Kentucky Power's Big Sandy generating units.

Kentucky Power provided the outstanding balances for its long-term debt, short-term debt, accounts receivable financing, and common equity as of April 30, 2012, the last expense month of the review period. It also provided the blended interest rates for the long-term debt, short-term debt, and accounts receivable financing as of April 30, 2012.⁸ Using this information, along with the currently approved 10.50 percent return on equity,⁹ Kentucky Power calculated a weighted average cost of capital, before income tax gross-up, of 8.12 percent.¹⁰ Kentucky Power also provided its updated income tax gross-up factor reflecting the methodology¹¹ approved in Case No. 2005-00068.¹²

The Commission has reviewed Kentucky Power's determination of its weighted average cost of capital and finds the 8.12 percent calculation to be reasonable. The Commission has also reviewed the determination of the tax gross-up factor and finds that it is consistent with the approach approved in Case No. 2005-00068. Therefore, the Commission finds that the weighted average cost of capital of 8.12 percent and the income tax gross-up factor of 1.5491 which produce an overall grossed-up return of 10.30 percent, should be used in all monthly environmental surcharge filings subsequent to the date of this Order.

⁸ Response to Staff's First Request, Item 3.

⁹ Case No. 2009-00459, Application of Kentucky Power Company for a General Adjustment of Electric Rates (Ky. PSC Jun. 28, 2010).

¹⁰ Response to Staff's First Request, Item 3.

¹¹ Response to Commission Staff's January 16, 2013 Informal Conference Data Request dated January 23, 2013, Item 1. In the response, Kentucky Power determined that its updated income tax gross-up factor was 1.5491.

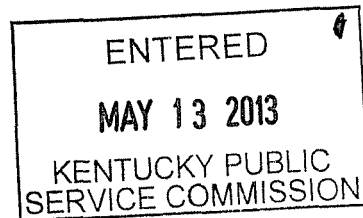
¹² Case No. 2005-00068, Application of Kentucky Power Company for Approval of an Amended Compliance Plan for Purposes of Recovering Additional Costs of Pollution Control Facilities and to Amend Its Environmental Cost Recovery Surcharge Tariff (Ky. PSC Oct. 17, 2005).

IT IS THEREFORE ORDERED that:


1. Kentucky Power shall reduce its jurisdictional environmental revenue requirement determined in the first billing month following the date of this Order by \$704,292 as discussed herein.

2. Kentucky Power shall use a weighted average cost of capital of 8.12 percent and a tax gross-up factor of 1.5491, a return on equity rate of 10.50 percent, and an overall grossed-up return of 10.30 percent in all monthly environmental surcharge filings subsequent to the date of this Order.

By the Commission



ATTEST:


Executive Director

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