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Commissioner

April 20, 2015

**PARTIES OF RECORD**

Re: Case No. 2015-00020 and Case No. 2015-00021

Attached is a copy of a memorandum which is being filed in the record of the above-referenced case. If you have any comments you would like to make regarding the contents of the memorandum, please do so within five days of receipt of this letter. If you have any questions, please contact Jeb Pinney, Staff Attorney, at (502) 782-2587.

Sincerely,

  
Jeff Derouen  
Executive Director

JP/ph

Attachment

## INTRA-AGENCY MEMORANDUM

### KENTUCKY PUBLIC SERVICE COMMISSION

**TO:** Main Case Files 2015-00021 and 2015-00020

**FROM:** J.E.B. Pinney, Staff Attorney

**DATE:** April 20, 2015

**SUBJECT:** Case No. 2015-00021: An Examination by the Public Service Commission of the Environmental Surcharge Mechanism of Louisville Gas and Electric Company for the Six-Month Billing Period Ending April 30, 2014

And

Case No. 2015-00020: An Examination by the Public Service Commission of the Environmental Surcharge Mechanism of Kentucky Utilities Company for the Six-Month Billing Period Ending April 30, 2014

On March 12, 2015, Commission Staff, and representatives from Kentucky Utilities Company ("KU") and Louisville Gas and Electric Company ("LG&E") (collectively the "Companies") participated in an informal conference at the Commission's offices. A copy of the sign-in sheet of those who participated is attached.

The purpose of the informal conference was to discuss the Companies' testimonies and responses to the first round of data requests filed as part of the Commission's review of the Companies' environmental surcharge mechanism. Attached to this memorandum is a handout distributed by the Companies that provided an overview of their filings in these cases. The Companies noted that both KU & LG&E had over-recoveries for the review period. KU proposed a two-month distribution period and LG&E proposed a one-month distribution period of their over-recoveries.

The Companies also discussed the Companies' utilization of bonus tax depreciation for 2014 and the resulting impact on income tax rates due to loss of the Section 199 deduction and the gross-up revenue factor used in rate of return calculations. Staff asked a few clarifying questions related to bonus tax depreciation and the Section 199 deduction, as well as the Companies' Staff asked a few clarifying questions related to testimony and data responses.

Thereafter the conference concluded.

Attachment

COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

AN EXAMINATION BY THE PUBLIC SERVICE )  
COMMISSION OF THE ENVIRONMENTAL ) CASE NO.  
SURCHARGE MECHANISM OF LOUISVILLE ) 2015-00021  
GAS & ELECTRIC COMPANY FOR THE SIX- )  
MONTH BILLING PERIOD ENDING APRIL 30, )  
2014 AND OCTOBER 31, 2014 )

AN EXAMINATION BY THE PUBLIC SERVICE )  
COMMISSION OF THE ENVIRONMENTAL ) CASE NO.  
SURCHARGE MECHANISM OF KENTUCKY ) 2015-00020  
UTILITIES COMPANY FOR THE SIX-MONTH )  
BILLING PERIODS ENDING APRIL 30, 2014 )  
AND OCTOBER 31, 2014 )

SIGN IN SHEET FOR MARCH 12, 2015 INFORMAL CONFERENCE

<u>NAME</u>	<u>PARTY</u>
<u>J. B. T. King</u>	<u>PSC - OGL</u>
<u>Jason Knox</u>	<u>LG&amp;E / KV</u>
<u>Allyson Sturgen</u>	<u>LG&amp;E / KH</u>
<u>Ron Handziak</u>	<u>PSC - FA</u>
<u>Chris Bennett</u>	<u>LG&amp;E / KV</u>
<u>Robert M. Conroy</u>	<u>LG&amp;E / KV</u>
<u>Andrea Schroeder</u>	<u>LG&amp;E / KV</u>
<u>Bob Russell</u>	<u>PSC - FA</u>
_____	_____
_____	_____

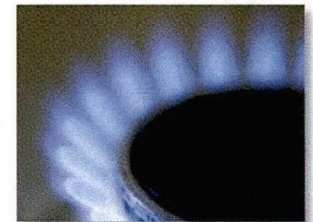
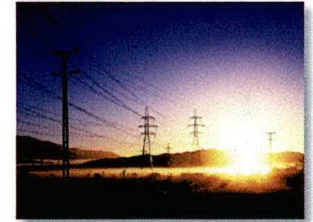
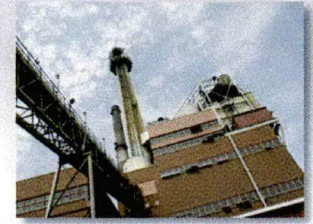




PPL companies

# ECR Review Case Nos. 2015-00020 and 2015-00021

*March 12, 2015*



# Overview

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- Review Period:
  - *Two six-month periods for expense months of September 2013 through February 2014 and March 2014 through August 2014*
  - *ECR Plans in effect - 2009 and 2011*
- Impacts to Rate of Return Calculation:
  - *Bonus Tax Depreciation*
  - *Gross-up Revenue Factor*
- Next Steps
- Appendix



# Over/(Under) Reconciliation

	KU	LG&E
Combined Over/(Under) Recovery	\$1,478,110	\$325,553
Due to Change in Rate of Return	(1,998,164)	(686,273)
Use of 12-Month Average Revenues (Note 1)	<u>3,476,274</u>	<u>1,011,826</u>
Total	<u>\$1,478,110</u>	<u>\$325,553</u>

*Note 1: The 12-month period reflects weather that was more severe than typical, including the polar vortex, for KU for the billing months of January, February and March 2014; and weather that was warmer than typical for LG&E for the billing months of July and September 2014.*

# Over/(Under) Recovery Position

- KU - over-recovery position
  - *Total over-recovery for the two 6-month periods is \$1,478,110*
  - *Calculated as of the end of each 6-month expense period (Feb-14 / Aug-14)*
  - *Recommend distribution over 2 months*
  - *Impact to residential customer using 1,247 kWh/mo is (\$0.65) per month*
- LG&E - over-recovery position
  - *Total over-recovery for the two 6-month periods is \$325,553*
  - *Calculated as of the end of each 6-month expense period (Feb-14 / Aug-14)*
  - *Recommend distribution over 1 month*
  - *Impact to residential customer using 984 kWh/mo is (\$0.37) per month*



# Bonus Tax Depreciation

- In December 2014, the 2014 Tax Increase Prevention Act ("ACT") was passed into law.
  - *The Act included an extension of 50% bonus tax depreciation for qualified property placed into service before January 1, 2015.*
  - *As a result of bonus tax depreciation, KU and LG&E will incur tax losses in 2014 and will be unable to take the IRS Section 199 Manufacturing Tax Deduction.*
  - *The loss of the Section 199 deduction results in an increase in KU and LG&E's effective income tax rates, thereby, increasing the gross-up revenue factor used in the rate of return calculations.*



# Impact to Gross-up Revenue Factor

- Commission's past practice has been to recognize impacts to the gross-up revenue factor calculations resulting from changes to tax laws.
- Propose use of effective income tax rates for the rate of return true-up calculations as follows:
  - *35.6937% for September-December 2013 expense months, includes Section 199 deduction;*
  - *38.6660% for January-August 2014 expense months, excludes Section 199 deduction.*

# Rate of Return Going Forward

- Continued use of 10.25% return on equity
  - *Consistent with the Commission's recent Orders in Case Nos. 2012-00221 and 2012-00222 (most recent base rate cases affirming the ROE for all Plans for ECR purposes, Orders issued December 20, 2012)*
  - *Overall rate of return established based on capitalization for the month ended August 2014 (end of expense period) and use of the 2015 gross-up revenue factor (35.6937%) that includes the Section 199 manufacturing tax deduction*
    - 10.15% for KU
    - 10.07% for LG&E



# Recommendations – KU and LG&E

- Approve distribution of over-recovery positions:
  - *KU over-recovery of \$1,478,110 over a two month period*
  - *LG&E over-recovery of \$325,553 over a one month period*
- Find environmental surcharge amounts for the billing periods ending April 2014 and October 2014 just and reasonable
- Approve the use of an overall rate of return on capital using a return on equity of 10.25% beginning in the second billing month following the Commission's Order
  - *10.15% for KU*
  - *10.07% for LG&E*

# Next Steps

## Procedural Schedule

- *All additional requests for information to KU and LG&E .....* **March 19**
- *KU and LG&E shall file responses .....* **April 2**
- *Intervenor testimony, if any, to be filed .....* **April 14**
- *All requests for information to Intervenors .....* **April 22**
- *Intervenors shall file responses .....* **May 1**
- *Last day for KU and LG&E to request a hearing or submit the case for decision based on the record.....* **May 8**



# *Appendix*

# Recent Changes to the ECR

- In December 2011, the Commission approved the 2011 ECR Compliance Plans for KU and LG&E
  - *Use of Group 1 and Group 2 ECR billing factors*
  - *Use of average daily balances and daily interest rates for short- and long-term debt rates in calculation of overall rate of return true-up adjustment*
- On December 20, 2012, the Commission approved the elimination of the 2005 and 2006 ECR Compliance Plans from the monthly filings for KU and LG&E
  - *Plan eliminations were an approved provision in the most recent rate case settlement*



# Recent Changes to the ECR

- On November 14, 2013, the Commission issued final Orders in the ECR Two-Year Reviews
  - *Approved roll-in of incremental ECR charges to base rates*
  - *Effective with the November 2013 expense month billed in January 2014*
  - *ES forms revised to reflect the elimination of the 2005 and 2006 Compliance Plans*

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