

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 KENTUCKY)	2015-00280
POWER COMPANY FOR THE TWO-YEAR)	
BILLING PERIOD ENDING JUNE 30, 2015)	

ORDER

On September 1, 2015, the Commission initiated a two-year review of Kentucky Power Company's ("Kentucky Power") environmental surcharge as billed to customers for the two-year period July 1, 2013, to June 30, 2015.¹ Pursuant to KRS 278.183(3), the Commission must review, at six-month intervals, the past operations of the environmental surcharge; disallow any surcharge amounts that are not just and reasonable; and reconcile past surcharge collections with actual costs recoverable. At two-year intervals, the Commission must review and evaluate the past operations of the environmental surcharge, disallow improper expenses, and, to the extent appropriate, incorporate surcharge amounts found just and reasonable into the existing base rates of the utility.

The Commission issued a procedural schedule on September 1, 2015, that provided for discovery, the filing of prepared testimony, intervenor testimony and discovery on intervenor testimony. Kentucky Power filed prepared direct testimony and responded to three requests for information. There were no parties requesting intervenor status to this proceeding. On January 6, 2016, Kentucky Power stated that

¹ Since Kentucky Power's surcharge is billed on a two-month lag, the amounts billed from July 2013 through June 2015 are based on costs incurred from May 2013 through April 2015.

this case may be submitted for a decision based on the existing record without a public hearing. Based on the absence of intervenors and finding good cause, the Commission will grant Kentucky Power's request and decide this case on the evidence of record without a hearing.

SURCHARGE ADJUSTMENT

The September 1, 2015 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 determined that it had over-recovered \$14,326 for the billing period from July 1, 2013, through December 31, 2013.² However, the Stipulation and Settlement Agreement ("Settlement Agreement") in Case No. 2012-00578³ and the Final Order in Case No. 2014-00052⁴ precluded Kentucky Power from refunding the over-recovery.⁵ The Settlement Agreement in Case No. 2012-00578 provided that effective January 1, 2014, the environmental surcharge factor will be maintained and fixed at zero percent until new base rates are established by the Commission. The Commission established new base rates for Kentucky Power in Case

² Direct Testimony of Amy J. Elliott ("Elliott Testimony") at 3.

³ Case No. 2012-00578, *Application of Kentucky Power Company for (1) A Certificate of Public Convenience and Necessity Authorizing the Transfer to the Company of an Undivided Fifty Percent Interest in the Mitchell Generating Station and Associated Assets; (2) Approval of the Assumption by Kentucky Power Company of Certain Liabilities in Connection with the Transfer of the Mitchell Generating Station; (3) Declaratory Rulings; (4) Deferral of Costs Incurred in Connection with the Company's Efforts to Meet Federal Clean Air Act and Related Requirements; and (5) All Other Required Approvals and Relief* (Ky. PSC Nov. 22, 2013).

⁴ Case No. 2014-00052, *An Examination by the Public Service Commission of the Environmental Surcharge Mechanism of Kentucky Power Company for the Six-Month Billing Period Ending December 31, 2013* (Ky. PSC Aug. 22, 2014).

⁵ Elliott Testimony at 3.

No. 2014-00396.⁶ Kentucky Power determined it had no over- or under-recoveries for the remaining 18 months of the review period, as the environmental surcharge factor was set at zero percent, in accordance with the Settlement Agreement in Case No. 2012-00578.⁷ The Commission has reviewed and finds reasonable Kentucky Power's determination it had no additional over- or under-recovery for the review period covered in this proceeding.

SURCHARGE ROLL-IN

Kentucky Power is not proposing that additional amounts of the environmental surcharge need to be incorporated into existing base rates as a "roll-in" in this proceeding.⁸ Kentucky Power notes that its environmental costs represent both investment costs, which are normally reflected in demand charges, and operating and maintenance costs, which are normally reflected in energy charges. Kentucky Power argues that the best time to properly allocate or assign these different types of environmental costs is during a base rate case. Kentucky Power stated that \$34,902,677 of environmental surcharge costs were included in base rates in Case No. 2014-00396, and insufficient time has elapsed to necessitate the inclusion of any additional environmental costs in base rates. Kentucky Power contends that whether there is a roll-in or not, there is no effect on the ratepayers or the company, because the total revenue requirement will remain the same.

⁶ Case No. 2014-00396, *Application of Kentucky Power Company for: (1) A General Adjustment of Its Rates for Electric Service; (2) An Order Approving Its 2014 Environmental Compliance Plan; (3) An Order Approving Its Tariffs and Riders; and (4) An Order Granting All Other Required Approvals and Relief* (Ky. PSC June 22, 2015).

⁷ Elliott Testimony at 4.

⁸ Kentucky Power's response to Commission Staff's First Request for Information, Item 5.

The environmental surcharge statute directs the Commission to incorporate surcharge amounts found just and reasonable into the utility's existing base rates, but only "to the extent appropriate."⁹ The Commission has reviewed and finds reasonable Kentucky Power's recommendation to not incorporate additional environmental surcharge amounts into base rates at the present time.

RATE OF RETURN

In previous environmental surcharge reviews the Commission has been guided by its findings in Case No. 1996-00489¹⁰ with respect to the determination of the weighted average cost of capital ("WACC") to be used prospectively in Kentucky Power's monthly environmental surcharge filings. In that case, the Commission found that Kentucky Power's debt portion of its WACC should be reviewed and re-established during each six-month review case. It was also found that the rate of return on common equity component would remain fixed and subject to review during the two-year environmental surcharge reviews. The WACC constitutes the rate of return for Kentucky Power's environmental compliance rate base.¹¹

However, the Settlement Agreement in Case No. 2014-00396 now supersedes the findings in Case No. 1996-00489. It specifies that for environmental surcharge

⁹ KRS 278.183(3).

¹⁰ Case No. 1996-00489, *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 Wastes and By-Products* (Ky. PSC May 27, 1997).

¹¹ This weighted average cost of capital is applied only to the environmental compliance rate base associated with plant installed at Kentucky Power's Mitchell generating unit.

purposes, Kentucky Power is authorized a return on common equity of 10.25 percent.¹² It also specifies that Kentucky Power utilize a WACC of 7.34 percent and a gross revenue conversion factor of 1.616424, which will remain constant until changed by the Commission in Kentucky Power's next base rate case.¹³ Together, these factors will produce an overall WACC of 10.128 percent.¹⁴

Kentucky Power states that it believes the 10.25 percent rate of return on common equity established in the Settlement Agreement in Case No. 2014-00396 is the reasonable rate of return for environmental surcharge purposes.¹⁵

IT IS THEREFORE ORDERED that:

1. Kentucky Power's request to submit this case for a decision on the existing evidence of record without a hearing is granted.
2. Kentucky Power's determination that it had no additional over- or under-recovery for the review period is approved.
3. Kentucky Power shall use a weighted average cost of capital of 7.34 percent and a tax gross-up factor of 1.616424, a return on equity rate of 10.25 percent, and an overall grossed-up return of 10.128 percent in all monthly environmental surcharge filings subsequent to the date of this Order.

¹² Case No. 2014-00396, *Kentucky Power Company* (Ky. PSC June 22, 2015), Final Order, Appendix A, Settlement Agreement, numbered paragraph 2 at 5.

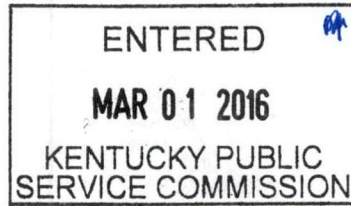
¹³ *Id.*, numbered paragraph 3 at 5–6.

¹⁴ *Id.*, Exhibit 2.

¹⁵ Elliott Testimony at 5.

4. The environmental surcharge amounts determined by Kentucky Power for the review period ended June 2015 are just and reasonable.

By the Commission



ATTEST:

Cara D. Gruenwell
Acting Executive Director *for*

*Amy J Elliott
Kentucky Power Company
101 A Enterprise Drive
P. O. Box 5190
Frankfort, KY 40602

*Kentucky Power Company
101 A Enterprise Drive
P. O. Box 5190
Frankfort, KY 40602

*Judy K Rosquist
Kentucky Power Company
101 A Enterprise Drive
P. O. Box 5190
Frankfort, KY 40602

*Honorable Mark R Overstreet
Attorney at Law
Stites & Harbison
421 West Main Street
P. O. Box 634
Frankfort, KENTUCKY 40602-0634