

CASE

NUMBER:

99 - 083

ERRATA SHEET OF KIUC WITNESS LANE KOLLEN
Case Nos. 98-426, 98-474, 99-082 and 99-083

RECEIVED

SEP 01 1999

PUBLIC SERVICE
COMMISSION

The following changes should be made to Mr. Kollen's testimonies in the various dockets. These changes are in addition to the changes provided the parties by letter from KIUC dated May 25, 1999.

March 17, 1999 Direct Testimony of Lane Kollen, Case Nos. 98-426:

1. Page 29, line 4: change 1999 to 2000

August 13, 1999 Rebuttal Testimony of Lane Kollen, Case No. 98-426, 99-082:

1. Page 33, lines 16-17 should be stricken and replaced with:

"3. Adjust capitalization to reflect JDC and Trimble County inventory adjustments."

March 17, 1999 Direct Testimony of Lane Kollen, Case Nos. 98-474

1. Page 32, line 4: change 1999 to 2000

August 13, 1999 Rebuttal Testimony of Lane Kollen, Case No. 98-474 and 99-083

1. Page 2, line 9 change \$55.584 to \$55.807.
2. Rebuttal Exhibit (LK-1) should be stricken and replaced with attached revised Rebuttal Exhibit (LK-1).

KENTUCKY UTILITIES COMPANY
SUMMARY OF REVENUE REQUIREMENT
12 MONTHS ENDING DECEMBER 31, 1998
(\$000)

	Unadjust Total KU	Unadjust "Other Juris"	Unadjust "KY Retail Juris"	Adjust to "KY Retail Juris"	Adjusted "KY Retail Juris"
Capitalization (1)	1,208,493	160,914	1,047,579	NA	1,047,579
Required Overall Rate of Return	8.17%	8.17%	8.17%	8.17%	8.17%
Required Operating Income	98,714	13,144	85,570	0	85,570
Per Books Operating Income	125,388	36,947	88,441	30,404	118,845
Operating Income Surplus	26,674	23,803	2,871	30,404	33,276
Revenue Surplus	44,736	39,920	4,816	50,991	55,807
Electric Revenues before Rate Reduction	810,115	225,561	584,554	139,251	723,805
Rate Reduction as % of Electric Revenues	5.52%	17.70%	0.82%		7.71%
Return on Common Equity before Rate Reduction	14.13%	39.36%	10.25%		16.07%
Effect of 1% Change in ROE					8,764

Note 1: Capitalization utilized by Kentucky PSC in lieu of rate base. Approximately equal.

KENTUCKY UTILITIES COMPANY
SUMMARY OF OPERATING INCOME
12 MONTHS ENDING DECEMBER 31, 1998
(\$000)

	Unadjust Total KU	Unadjust "Other Juris"	Unadjust "KY Retail Juris"	Adjust to "KY Retail Juris"	Adjusted "KY Retail Juris"
Operating Revenues					
Residential	238,898	18,107	220,791	4,216 (1)	225,007
Commercial and Industrial	344,907	18,048	326,859	(1,845)(2)	325,014
Public Street and Highway Lighting	6,483	207	6,276		6,276
Other Sales to Public Authorities	52,332	2,497	49,835		49,835
Sales for Resale	179,118	179,118	0	108,690 (3)	108,690
Provision for Refund	(23,724)	(1,567)	(22,157)	22,157 (4)	0
Other Operating Revenues	12,101	9,151	2,950	6,033 (5)	8,983
Total Operating Revenues	810,115	225,561	584,554	139,251	723,805
Operating Expenses					
Fuel, Purchased Power, and Other Oper Exp	465,630	143,534	322,096	82,235 (3),(5)	404,331
Maintenance Expense	63,608	9,756	53,852	6,973 (6)	6,973
Depreciation	86,657	12,016	74,641	(768)(7)	(768)
Other Taxes	15,946	2,746	13,200	1,482 (8)	1,482
Federal and State Income Taxes	53,256	20,615	32,641	(1,662)(9)	(1,662)
Other	(370)	(53)	(317)		53,852
Total Operating Expenses	684,727	188,614	496,113	108,847	74,641
Net Operating Income	125,388	36,947	88,441	30,404	13,200

- Note 1: Year end customers revenue annualization less variable energy costs for all classes.
 Note 2: FAC adjustment for off-system sales line losses.
 Note 3: Reallocation of sales for resale revenues and related expenses to retail and FERC jurisdictions (KU response)
 Note 4: Nonrecurring; includes \$21.5 million one-time ECR refund.
 Note 5: Reallocation of transmission service revenues and related expenses to retail and FERC jurisdictions (KU response to KIUC#3-38(a) page 3 of 4.
 Note 6: KU net retained merger savings.
 Note 7: Net Year 2000 deferral and amortization over 5 years.
 Note 8: Net Risk Management Trust deferral and amortization over 5 years.
 Note 9: Elimination of advertising expenses.

KENTUCKY UTILITIES COMPANY
SUMMARY OF COST OF CAPITAL
12 MONTHS ENDING DECEMBER 31, 1998
(\$000)

	Capital \$ w/o ITC (1)	Capital % without ITC	COC w/o ITC (2)	Wtd COC without ITC	Capital \$ with ITC	Capital % with ITC	COC with ITC	Wtd COC with ITC	Capital \$ ITC Alloc
Long and Short Term Debt	543,584	45.83%	6.99%	3.20%	543,584	44.98%	6.99%	3.14%	553,616
Preferred Equity	39,799	3.36%	5.64%	0.19%	39,799	3.29%	5.64%	0.19%	40,533
Common Equity	602,808	50.82%	9.70%	4.93%	602,808	49.88%	9.70%	4.84%	613,932
Total Capitalization	1,186,191			8.32%	1,186,191				
Investment Tax Credit (3)					22,302	1.85%	0.00%	0.00%	
Total Capitalization with ITC					1,208,493			8.17%	1,208,081

Note 1: Capitalization amounts are for total Company and were provided by Company in supplemental response to Commission Question No. 11 parts (a) and (b) attached to Commission Order dated December 2, 1998.

Note 2: Cost of debt and preferred were provided by Company in response to PSC-4-KU-10(c). Cost of common provided by KIUC witness Baudino.

Note 3: Obtained from KU 1998 SEC Form 10-K page 153.

KENTUCKY UTILITIES COMPANY
SUMMARY OF RATE BASE
12 MONTHS ENDING DECEMBER 31, 1998
(\$000)

	Unadjust Total KU	Unadjust "Other Juris"	Unadjust "KY Retail Juris"	Adjust to "KY Retail Juris"	Adjusted "KY Retail Juris"
Plant in Service	2,602,167	368,761	2,233,406	NA	2,233,406
CWIP	83,361	10,516	72,845	NA	72,845
Accumulated Depreciation	(1,208,183)	(177,620)	(1,030,563)	NA	(1,030,563)
Accumulated Deferred Inc Taxes (Net)	(291,840)	(44,302)	(247,538)	NA	(247,538)
Fuel Inventories	23,927	3,432	20,495	NA	20,495
M&S Inventories	24,248	3,502	20,746	NA	20,746
Net Regulatory Assets/Liabilities	(26,999)	(3,702)	(23,297)	NA	(23,297)
Customer Deposits	(10,354)	(659)	(9,695)	NA	(9,695)
Customer Advances	(1,265)	(53)	(1,212)	NA	(1,212)
Investment Tax Credit	(22,302)	(3,719)	(18,583)	NA	(18,583)
Total Rate Base	1,172,760	156,156	1,016,604	NA	1,016,604

CASE

NUMBER:

99-083
Filed 5-24-79

KY. PUBLIC SERVICE COMMISSION

Index for Case: 1999-00149

AS OF : 03/06/07

American Electric Power

Transfer / Sale / Purchase / Merger

OF KENTUCKY POWER & CENTRAL AND SOUTH WEST CORPORATION

IN THE MATTER OF THE JOINT APPLICATION OF KENTUCKY POWER COMPANY, AMERICAN ELECTRIC POWER COMPANY, INC. AND CENTRAL AND SOUTH WEST CORPORATION REGARDING A PROPOSED MERGER

SEQ NBR	Date	Remarks
1	(M) 04/14/99	MOTION TO ENTER PROCEDURAL ORDER & TO SCHEDULE INFORMAL CONFERENCE (MARK OVERSTREET / KENTUCKY POWER)
2	04/15/99	Application.
3	04/15/99	Acknowledgement letter.
4	04/20/99	Order setting forth the procedural schedule to be followed in this case.
5	04/22/99	No deficiency letter.
6	(M) 04/22/99	MOTION TO INTERVENE (E BLACKFORD AG)
7	(M) 04/22/99	DUPLICATE OF NOTICE AND REQUEST TO PUBLISH (ERROL WAGNER AMERICAN ELECTRIC POWER)
8	(M) 04/23/99	STIPULATION & SETTLEMENT AGREEMENT (PSC)
9	(M) 04/27/99	LETTER CONCERNING MEETING ON MAY 4,99 & REQ FOR ORDER TO BE ENTERED (MARK OVERSTREET)
10	(M) 04/27/99	MOTION TO INTERVENE (KES SMITTY TAYLOR)
11	04/28/99	Data Request Order; info due 5/4/99 from KPC, AEP and Central & So. West Corp.
12	(M) 04/28/99	REQUEST FOR INFORMATION TO KY POWER CO & AMERICAN ELECTRIC POWER (AG E BLACKFORD)
13	(M) 04/28/99	JOINT APPLICANTS RESP TO STAFF ORAL DATA REQ 2-4 MADE APRIL 22,99 (MARK OVERSTREET KY POWER, AMERICAN E)
14	(M) 04/29/99	ASSESSMENT OF GENERATION & TRANSMISSION ADEQUACY (KY POWER & AMERICAN ELECTRIC POWER)
15	04/30/99	Order scheduling IC on 5/4/99 at 9:30 in Hearing Room 2.
16	05/04/99	Order granting motion of Attorney General for full intervention.
17	05/04/99	Order granting motion of Kentucky Electric Steel for full intervention.
18	(M) 05/04/99	PETITION TO INTERVENE (DAVID BOEHM KIUC)
19	(M) 05/04/99	RESPONSE TO INFO REQ DATED APRIL 28,99 (MARK OVERSTREET KY POWER)
20	05/07/99	Letter granting pet. for conf. filed 4/29/99 on behalf of AEP and KPC.
21	(M) 05/07/99	SUPPLEMENTAL RESPONSE TO DATA REQUEST (MARK OVERSTREET / KY POWER)
22	05/11/99	Data Request Order, response due 5/17/99.
23	05/11/99	Order granting motion of the KIUC to intervene.
24	(M) 05/11/99	SECOND REQUEST FOR INFO. PROPOUNDED BY THE A.G. (ELIZABETH BLACKFORD ASS. ATTORN. GEN)
25	05/14/99	Order scheduling IC on 5/17/99 at 9:30 in Hearing Room 2.
26	(M) 05/14/99	MOTION FOR FULL INTERVENTION (J D MYLES KY ASSOC OF PLUMBING HEAT)
27	(M) 05/17/99	RESPONSE TO PSC INFO REQ DATED MAY 11,99 (MARK OVERSTREET KY POWER)
28	(M) 05/18/99	OPPOSITION OF JOINT APPLICANTS TO MOTION OF KY ASSOCIATION (MARK OVERSTREET KENTUCKY POWER)
29	05/19/99	Order scheduling IC on 5-20-99 at 2p.m. in Hearing Room 2.
30	05/20/99	Order denying the Contractors' motion to intervene
31	(M) 05/24/99	STIPULATION & SETTLEMENT AGREEMENT (MARK OVERSTREET)
32	(M) 05/26/99	DIRECT TESTIMONY OF RICHARD MUNCZINSKI (MARK OVERSTREET AMERICAN ELECTRIC POW)
33	(M) 05/26/99	ORIGINAL 16,19,17 PAGES WITH ORIGINAL SIGNATURES (MARK OVERSTREET AMERICAN ELECTRIC PO)
34	(M) 05/27/99	MOTION FOR RECONSIDERATION (JD MYLES ATTORNEY)
35	(M) 06/03/99	OPPOSITION TO JOINT MOTION OF KY ASSOC OF PLUMBING & KY PROPANE (KY POWER & CENTRAL & SOUTH WEST CORP)
36	06/14/99	Final Order approving terms and conditions of attached Settlement Agreement.
37	(M) 06/14/99	Hearing held on 5/28/99. (Connie Sewell/Court Reporter)

- 38 (M) 07/02/99 REVISED TARIFF (MARK OVERSTREET AMERICAN ELECTRIC P)
- 39 (M) 12/08/00 Errol K Wagner - American Electric Power - AEP's responses to the information requests pursuant to the Commission's Order dated June 14, 1999.
- 40 (M) 01/31/01 COPY OF LETTER INTENDS TO SERVE TO SECURITIES & EXCHANGE COMMISSION (ERROL K. WAGNER AEP)
- 41 02/22/01 Letter to Errol Wagner, addressing his concerns.
- 42 (M) 04/18/01 RESPONSE TO ORDER OF FEB 22,01 (ERROL WAGNER AMERICAN ELECTRIC POWER)
- 43 (M) 05/15/01 RESPONSE TO COMMISSION'S ORDER (MARK OVERSTREET/KY POWER)
- 44 (M) 08/10/01 Mark R Overstreet - Stites & Harbison - REPORTS FOR THE PERIODS ENDING MARCH 31, 2001 AND JUNE 30, 2001
- 45 (M) 11/26/01 Response to Commission's Order of June 14, 1999
- 46 (M) 05/15/02 Mark R Overstreet - Stites & Harbison - Supplementary response to the data request set forth in the Order of June 14,99
- 47 (M) 08/30/02 Mark R Overstreet - Stites & Harbison - Revised Net Merger Savings Credit Tariff
- 48 (M) 08/30/02 Mark R Overstreet - Stites & Harbison - Revised Net Merger Savings Credit Tariff & supporting calculations
- 49 (M) 11/26/02 Mark R Overstreet - Stites & Harbison - Supplementary responses of KY Power to the data requests set forth in the PSC Order dated June 14,99
- 50 (M) 05/16/03 Mark R Overstreet - Stites & Harbison - Responses of Kentucky Power to the data requests set forth in the PSC Order of June 14, 99 they are for the period of December 31, 02
- 51 (M) 06/09/03 Mark R Overstreet - Stites & Harbison - Responses to data requests set forth in the June 14, 1999 order filed by American Electric Power
- 52 (M) 08/20/03 Mark R Overstreet - Stites & Harbison - Supplemental responses of Kentucky Power to the data request set forth in the PSC Order of June 14, 1999
- 53 (M) 11/21/03 Mark R Overstreet - Stites & Harbison - Supplemental responses of Kentucky Power to the data request set forth in the PSC Order of June 99
- 54 (M) 03/24/04 Mark R Overstreet - Stites & Harbison - Supplemental responses of American Electric Power to PSC June 14, 99 Order & requests to reconsider June 14, 99 Order requiring quarterly filings
- 55 (M) 05/18/04 Mark R Overstreet - Stites & Harbison - AEP supplemental responses to PSC June 14, 99 Order for Year ended Dec 31, 03 & quarter ended March 31, 04
- 56 06/14/04 Order entered; the 6/14/1999 Order is modified to the limited extent that the information required to be filed quarterly shall be filed annually, and all information required to be filed annually shall be due by March 31 of each year, beginning March 31, 2005; Kentucky Power's request to file its annual information by May 15 of each year is denied
- 57 (M) 06/29/04 Mark R Overstreet - Stites & Harbison - American Electric Power's Petition for rehearing
- 58 07/16/04 Order entered; the 6/14/2004 Order is amended to require the annual filing of information to be due by May 15 of each year, beginning 3/15/2005; All other provisions of the 6/14/2004 Order shall remain in full force and effect
- 59 (M) 08/01/05 Mark R Overstreet - Stites & Harbison - Revised response of Kentucky Power to Item 15 that was filed May 16, 2005
- 60 (M) 08/22/05 Errol K Wagner - American Electric Power - Net merger tariff from Kentucky Power
- 61 (M) 05/15/06 Mark R Overstreet - Stites & Harbison - Supplemental responses of Kentucky Power to the PSC June 14, 99 Order

KY. PUBLIC SERVICE COMMISSION

Index for Case: 1999-00083

AS OF : 03/06/07

Kentucky Utilities Company

Complaints - Rates

OF KENTUCKY INDUSTRIAL UTILITY CUSTOMERS

IN THE MATTER OF KENTUCKY INDUSTRIAL UTILITY VS. KENTUCKY UTILITIES COMPANY

SEQ NBR	Date	Remarks
1	03/08/99	Application.
2	03/09/99	Acknowledgement letter.
3	(M) 03/10/99	NOTIFICATION OF PARTIES WHO RECEIVED COPIES OF FILING (DAVID BOEHM KIUC)
4	(M) 03/12/99	MOTION TO DISMISS COMPLAINTS OF KENTUCKY IND UTILITY CUSTOMERS (KENDRICK RIGGS LOUISVILLE GAS & ELEC)
5	(M) 03/22/99	MOTION TO INTERVENE (ANTHONY MARTIN COMMUNITY ACTION COUN)
6	(M) 03/22/99	RESPONSE TO MOTION TO DISMISS (MIKE KURTZ KIUC)
7	(M) 03/25/99	KUS REPLY TO KIUC RESPONSE TO MOTION TO DISMISS (RICHARD NEWELL LG&E & KU)
8	04/06/99	Order granting motion of the Community Action Council to intervene.
9	04/13/99	Order entered; denies motion; info due 4/23; transfers case to 98-426 & 98-474
10	(M) 05/24/99	DIRECT TESTIMONY OF RICHARD BAUDINO LANE KOLLEN (MIKE KURTZ KIUC)
11	(M) 08/16/99	REBUTTAL TESTIMONY OF LANE KOLLEN (MIKE KURTZ KIUC)
12	(M) 08/16/99	REBUTTAL TESTIMONY OF RICHARD BAUDINO (MIKE KURTZ KIUC)
13	(M) 08/19/99	RESPONSE TO LG&E & KU AUG 17,99 DATAT REQUEST (MIKE KURTZ KIUC)
14	(M) 09/01/99	ERRATA SHEET FOR MARCH 17,99 DIRECT TESTIMONY OF LANE KOLLEN (MIKE KURTZ KIUC)

BOEHM, KURTZ & LOWRY

ATTORNEYS AT LAW
2110 CBLD CENTER
36 EAST SEVENTH STREET
CINCINNATI, OHIO 45202
TELEPHONE (513) 421-2255
TELECOPIER (513) 421-2764

RECEIVED

MAY 24 1999

PUBLIC SERVICE
COMMISSION

Via Hand Delivery

May 24, 1999

Hon. Helen Helton
Executive Director
Kentucky Public Service Commission
730 Schenkel Lane
Frankfort, Kentucky 40601

Re: Kentucky Industrial Utility Customers, Inc. v. Kentucky Utilities Company, Case No. 99-083

and

Re: In The Matter Of: Application of Kentucky Utilities Company for Approval of an Alternative Method of Regulation Of Its Rates and Service, Case No. 98-474

Dear Ms. Helton:

Please find enclosed the original and ten copies of the Additional Direct Testimony of Richard A. Baudino and Lane Kollen on behalf of Kentucky Industrial Utility Customers, Inc. in the above-referenced matters. By copy of this letter, all parties listed on the Certificate of Service have been served.

Please place this document of file.

Very Truly Yours,



Michael L. Kurtz, Esq.
BOEHM, KURTZ & LOWRY

MLK/kew
Attachment

CC: Certificate of Service

CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing was served by mailing a true and correct copy, by regular U.S. mail (unless otherwise noted) to all parties on this 24th day of May, 1999.

Elizabeth E. Blackford, Esq.
Utility & Rate Intervention Division
1024 Capital Holding Center Dr.
Suite 200
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(Via Overnight Mail)

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Shelbyville, KY 40065

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Vice President of Regulatory Affairs
Kentucky Utilities Company
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(Via Overnight Mail)

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Assistant Jefferson County Attorney
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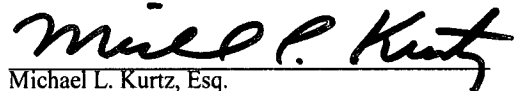
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Hon. Iris Skidmore
Hon. Ronald P. Mills
Counsel for NREPC
Office of Legal Services
201 West Short Street
Lexington, KY 40507-1374


Michael L. Kurtz, Esq.

COMMONWEALTH OF KENTUCKY

BEFORE THE

PUBLIC SERVICE COMMISSION

IN THE MATTER OF: APPLICATION OF	:	
KENTUCKY UTILITIES COMPANY FOR	:	
APPROVAL OF AN ALTERNATIVE METHOD	:	CASE NO. 98-474
OF REGULATION OF ITS RATES AND SERVICE	:	
	:	
and	:	
	:	
KENTUCKY INDUSTRIAL UTILITY	:	
CUSTOMERS, INC.	:	
Complainant	:	CASE NO. 99-083
v.	:	
	:	
KENTUCKY UTILITIES COMPANY	:	
	:	
Defendant	:	

ADDITIONAL DIRECT TESTIMONY

AND EXHIBITS

OF

RICHARD A. BAUDINO

AND

LANE KOLLEN

ON BEHALF OF THE

KENTUCKY INDUSTRIAL UTILITY CUSTOMERS, INC.

J. KENNEDY AND ASSOCIATES, INC.
ATLANTA, GEORGIA
MAY 1999

COMMONWEALTH OF KENTUCKY

BEFORE THE

PUBLIC SERVICE COMMISSION

IN THE MATTER OF: APPLICATION OF :
KENTUCKY UTILITIES COMPANY FOR : **CASE NO. 98-474**
APPROVAL OF AN ALTERNATIVE METHOD :
OF REGULATION OF ITS RATES AND SERVICE :

and

KENTUCKY INDUSTRIAL UTILITY :
CUSTOMERS, INC. : **CASE NO. 99-083**

Complainant :

v. :

KENTUCKY UTILITIES COMPANY :

Defendant :

ADDITIONAL DIRECT TESTIMONY

AND EXHIBITS

OF

RICHARD A. BAUDINO

ON BEHALF OF THE

KENTUCKY INDUSTRIAL UTILITY CUSTOMERS, INC.

J. KENNEDY AND ASSOCIATES, INC.

ATLANTA, GEORGIA

MAY 1999

COMMONWEALTH OF KENTUCKY

BEFORE THE

PUBLIC SERVICE COMMISSION

IN THE MATTER OF: APPLICATION OF	:	
KENTUCKY UTILITIES COMPANY FOR	:	CASE NO. 98-474
APPROVAL OF AN ALTERNATIVE METHOD	:	
OF REGULATION OF ITS RATES AND SERVICE	:	

and

KENTUCKY INDUSTRIAL UTILITY	:	
CUSTOMERS, INC.	:	CASE NO. 99-083

Complainant

v.

KENTUCKY UTILITIES COMPANY

Defendant

ADDITIONAL DIRECT TESTIMONY OF RICHARD A. BAUDINO

1 Q. Please state your name and business address.

2 A. Richard A. Baudino, J. Kennedy and Associates, Inc. ("Kennedy and Associates"), 35
3 Glenlake Parkway, Suite 475, Atlanta, Georgia 30328.

4

5 Q. Are you the same Richard Baudino who submitted direct testimony in this
6 proceeding on behalf of the Kentucky Industrial Utility Customers ("KIUC")?

7 A. Yes.

8

9 Q. What is the purpose of your additional direct testimony in this proceeding?

10 A. The purpose of my additional direct testimony is to update my cost of equity

1 calculation with more recent data. I am sponsoring Exhibits ____ (RAB-7) through
2 ____ (RAB-10) which provide the updates to my discounted cash flow ("DCF")
3 analysis and my Capital Asset Pricing Model ("CAPM") analysis.
4

5 **Q. Are there any changes to your comparison group?**

6 A. Yes. I eliminated Northern States Power because of a recently announced merger.
7

8 **Q. What is the updated dividend yield for the group?**

9 A. Exhibit ____ (RAB-7) shows that the updated six-month dividend yield for the
10 comparison group is 4.64%.
11

12 **Q. What is your recommended growth rate range?**

13 A. My recommended growth rate range is now 4.40% to 5.20%. The updated growth
14 rates are presented in Exhibit ____ (RAB-8). The range encompasses the Value Line
15 earnings and retention growth forecasts and the Institutional Brokers Estimate System
16 ("IBES") earnings forecasts.
17

18 **Q. What is your updated DCF return on equity range?**

19 A. Exhibit ____ (RAB-9) presents the updated DCF range, which is 9.14% to 9.96%, with
20 a midpoint of 9.55%. This is slightly higher than the midpoint of 9.45% in my direct
21 testimony.
22

23 **Q. Please present your results for the CAPM analysis.**

24 A. Updating the analysis results in a CAPM cost of equity range of 7.16% to 9.13%.
25

1 Q. Does this conclude your additional direct testimony in this proceeding?

2 A. Yes.

COMMONWEALTH OF KENTUCKY

BEFORE THE

PUBLIC SERVICE COMMISSION

IN THE MATTER OF: APPLICATION OF :
KENTUCKY UTILITIES COMPANY FOR : CASE NO. 98-474
APPROVAL OF AN ALTERNATIVE METHOD :
OF REGULATION OF ITS RATES AND SERVICE :

and

KENTUCKY INDUSTRIAL UTILITY :
CUSTOMERS, INC. : CASE NO. 99-083

Complainant

v.

KENTUCKY UTILITIES COMPANY

Defendant

ADDITIONAL EXHIBITS

OF

RICHARD A. BAUDINO

ON BEHALF OF THE

KENTUCKY INDUSTRIAL UTILITY CUSTOMERS, INC.

J. KENNEDY AND ASSOCIATES, INC.
ATLANTA, GEORGIA

MAY 1999

**KENTUCKY UTILITIES
ELECTRIC UTILITY COMPARISON GROUP
AVERAGE PRICE, DIVIDEND AND DIVIDEND YIELD**

		Nov '98	Dec '98	Jan '99	Feb '99	Mar '99	Apr '99
DPL	High Price (\$)	20.500	21.750	22.000	19.000	19.313	17.875
	Low Price (\$)	18.938	19.938	18.938	17.438	16.438	16.313
	Avg. Price (\$)	19.719	20.844	20.469	18.219	17.875	17.094
	Dividend (\$)	0.235	0.235	0.235	0.235	0.235	0.235
	Mo. Avg. Div.	4.77%	4.51%	4.59%	5.16%	5.26%	5.50%
	6 mos. Avg.	4.96%					
FPL Group	High Price (\$)	64.750	64.938	61.938	55.438	58.125	57.563
	Low Price (\$)	60.750	60.625	54.500	50.313	50.125	52.875
	Avg. Price (\$)	62.750	62.781	58.219	52.875	54.125	55.219
	Dividend (\$)	0.500	0.500	0.500	0.520	0.520	0.520
	Mo. Avg. Div.	3.19%	3.19%	3.44%	3.93%	3.84%	3.77%
	6 mos. Avg.	3.56%					
OGE Energy	High Price (\$)	28.500	29.000	29.063	25.813	25.750	24.250
	Low Price (\$)	26.250	27.313	25.313	23.625	22.563	21.813
	Avg. Price (\$)	27.375	28.156	27.188	24.719	24.156	23.031
	Dividend (\$)	0.333	0.333	0.333	0.333	0.333	0.333
	Mo. Avg. Div.	4.86%	4.72%	4.89%	5.38%	5.51%	5.77%
	6 mos. Avg.	5.19%					
SIGCorp	High Price (\$)	36.875	35.750	36.125	32.625	29.563	29.000
	Low Price (\$)	33.375	33.625	32.500	28.750	26.250	26.125
	Avg. Price (\$)	35.125	34.688	34.313	30.688	27.906	27.563
	Dividend (\$)	0.303	0.303	0.310	0.310	0.310	0.310
	Mo. Avg. Div.	3.44%	3.49%	3.61%	4.04%	4.44%	4.50%
	6 mos. Avg.	3.92%					
Wisconsin Energy	High Price (\$)	32.125	31.875	31.563	26.875	27.375	26.875
	Low Price (\$)	30.188	30.000	25.938	25.063	25.188	25.063
	Avg. Price (\$)	31.156	30.938	28.750	25.969	26.281	25.969
	Dividend (\$)	0.390	0.390	0.390	0.390	0.390	0.390
	Mo. Avg. Div.	5.01%	5.04%	5.43%	6.01%	5.94%	6.01%
	6 mos. Avg.	5.57%					
Group Dividend Yield, 6 Mo. Avg.		4.64%					
Source: Standard and Poor's Stock Guide, December 1998 through May 1999.							

**KENTUCKY UTILITIES
ELECTRIC UTILITY COMPARISON GROUP
DCF Growth Rate Analysis**

<u>Company</u>	(1) Value Line DPS	(2) Value Line EPS	(3) IBES	(4) Value Line B x R
DPL	1.25%	3.25%	5.00%	3.88%
FPL Group	3.71%	4.81%	5.70%	6.68%
OGE Energy	2.43%	6.06%	3.70%	6.40%
SIGCorp	2.66%	5.76%	4.30%	6.36%
Wisconsin Energy	2.33%	6.40%	3.10%	2.67%
<u>Averages</u>	2.48%	5.25%	4.36%	5.20%

Sources: Institutional Brokers Estimate System, May 1999 Earnings Reports
Value Line Investment Reports, March 12 and April 9, 1999

Value Line Projected Dividend Per Share Growth

<u>Company</u>	1998 DPS	Projected 02 - '04 DPS	Compound Growth Rate
DPL	\$ 0.94	\$ 1.00	1.25%
FPL Group	\$ 2.00	\$ 2.40	3.71%
OGE Energy	\$ 1.33	\$ 1.50	2.43%
SIGCorp	\$ 1.21	\$ 1.38	2.66%
Wisconsin Energy	\$ 1.56	\$ 1.75	2.33%
Average			2.48%

**KENTUCKY UTILITIES
ELECTRIC UTILITY COMPARISON GROUP
DCF Growth Rate Analysis**

Value Line Projected Earnings Per Share Growth

<u>Company</u>	<u>3-Year Avg. EPS</u>	<u>Projected 02 - '04 EPS</u>	<u>Compound Growth Rate</u>
DPL	\$ 1.20	\$ 1.45	3.25%
FPL Group	\$ 3.58	\$ 4.75	4.81%
OGE Energy	\$ 1.76	\$ 2.50	6.06%
SIGCorp	\$ 1.93	\$ 2.70	5.76%
Wisconsin Energy	\$ 1.65	\$ 2.25	6.40%
Average			5.25%

Note: 1998 EPS is used in place of 3-year average for Wisconsin Energy.

Sustainable Growth Calculation

<u>Company</u>	<u>Forecasted Payout Ratio</u>	<u>Forecasted Retention Ratio</u>	<u>Expected Return</u>	<u>Growth Rate</u>
DPL	68.97%	31.03%	12.50%	3.88%
FPL Group	50.53%	49.47%	13.50%	6.68%
OGE Energy	60.00%	40.00%	16.00%	6.40%
SIGCorp	51.11%	48.89%	13.00%	6.36%
Wisconsin Energy	77.78%	22.22%	12.00%	2.67%
Average	61.68%	38.32%	13.40%	5.20%

Source: Data come from Value Line's 2002-2004 forecasts.

**RETURN ON EQUITY CALCULATION
COMPARISON GROUP**

Dividend Yield	4.64%	4.64%
Growth Rate Range	4.40%	5.20%
Expected Dividend Yield	4.74%	4.76%
DCF Return on Equity	9.14%	9.96%
Midpoint of Range		9.55%

KENTUCKY UTILITIES
Capital Asset Pricing Model Analysis
Electric Utility Comparison Group Beta

30-Year Treasury Bond

Line No.		(1) S&P 500	(2) Value Line
1	Market Required Return Estimate		
2	Expected Dividend Yield	1.38%	1.58%
3	Expected Growth	<u>7.50%</u>	<u>10.30%</u>
4	Required Return	8.88%	11.88%
5	Risk-free Rate of Return, 30-Year Treasury Bond		
6	Average of Last Six Months	5.34%	5.34%
8	Risk Premium		
9	@ 6 Month Average RFR (Line 4 minus Line 6)	3.54%	6.54%
10	Comparison Group Beta	0.58	0.58
11	Comparison Group Beta * Risk Premium		
12	@ 6 Month Average RFR (Line 10 * Line 9)	2.05%	3.79%
13	CAPM Return on Equity		
14	@ 6 Month Average RFR (Line 12 plus Line 6)	7.39%	9.13%

5-Year Treasury Bond

1	Market Required Return Estimate		
2	Expected Dividend Yield	1.38%	1.58%
3	Expected Growth	<u>7.50%</u>	<u>10.30%</u>
4	Required Return	8.88%	11.88%
5	Risk-free Rate of Return, 5-Year Treasury Bond		
6	Average of Last Six Months	4.80%	4.80%
8	Risk Premium		
9	@ 6 Month Average RFR (Line 4 minus Line 6)	4.08%	7.08%
10	Comparison Group Beta	0.58	0.58
11	Comparison Group Beta * Risk Premium		
12	@ 6 Month Average RFR (Line 9 * Line 10)	2.37%	4.11%
13	CAPM Return on Equity		
14	@ 6 Month Average RFR (Line 12 plus Line 6)	7.16%	8.90%

KENTUCKY UTILITIES Supporting Data for CAPM Analyses

S&P Dividend Yield Data:

	<u>Avg. Yield</u>
November 1998	1.43%
December 1998	1.37%
January 1999	1.31%
February 1999	1.32%
March 1999	1.30%
April 1999	<u>1.24%</u>
6 month average	1.33%

Source: S& P's Central Inquiry Unit

30 Year Treasury Bond Data

	<u>Avg. Yield</u>
November 1998	5.23%
December 1998	5.09%
January 1999	5.18%
February 1999	5.40%
March 1999	5.58%
April 1999	<u>5.56%</u>
6 month average	5.34%

Source: Compuserve Data Base

Value Screen III Growth Rate Data:

Forecasted Data:	
Earnings	14.10%
Book Value	11.90%
Dividends	<u>4.90%</u>
Average	10.30%

Source: Value Screen III, May 1999

Value Line Industrial Composite Data:

Forecasted Data:	
Earnings	11.50%
Dividends	8.00%
Retention Growth	<u>15.00%</u>
Average	11.50%

Source: Value Line Selection & Opinion,
January 22, 1999.5 Year Treasury Bond Data

	<u>Avg. Yield</u>
November 1998	4.50%
December 1998	4.53%
January 1999	4.61%
February 1999	4.94%
March 1999	5.16%
April 1999	<u>5.07%</u>
6 month average	4.80%

Source: Compuserve Data Base

Value Line BetasComparison Group:

DPL	0.65
FPL Group	0.55
OGE Energy	0.50
SIGCorp	0.65
Wisconsin Energy	<u>0.55</u>
Average	0.58

Source: Value Line Investment Reports,
March 12 and April 9, 1999.

COMMONWEALTH OF KENTUCKY

BEFORE THE

PUBLIC SERVICE COMMISSION

IN THE MATTER OF: APPLICATION OF :
KENTUCKY UTILITIES COMPANY FOR :
APPROVAL OF AN ALTERNATIVE METHOD : **CASE NO. 98-474**
OF REGULATION OF ITS RATES AND SERVICE :

and :

KENTUCKY INDUSTRIAL UTILITY :
CUSTOMERS, INC. :
Complainant : **CASE NO. 99-083**

v. :

KENTUCKY UTILITIES COMPANY :
Defendant :

ADDITIONAL DIRECT TESTIMONY
AND EXHIBITS
OF
LANE KOLLEN

ON BEHALF OF THE
KENTUCKY INDUSTRIAL UTILITY CUSTOMERS, INC.

J. KENNEDY AND ASSOCIATES, INC.
ATLANTA, GEORGIA

MAY 1999

COMMONWEALTH OF KENTUCKY

BEFORE THE

PUBLIC SERVICE COMMISSION

IN THE MATTER OF: APPLICATION OF	:	
KENTUCKY UTILITIES COMPANY FOR	:	
APPROVAL OF AN ALTERNATIVE METHOD:	:	CASE NO. 98-474
OF REGULATION OF ITS RATES AND SERVICE	:	
	:	
and	:	
	:	
KENTUCKY INDUSTRIAL UTILITY	:	
CUSTOMERS, INC.	:	
	:	
Complainant	:	CASE NO. 99-083
v.	:	
	:	
KENTUCKY UTILITIES COMPANY	:	
	:	
Defendant	:	

TABLE OF CONTENTS

I.	QUALIFICATIONS AND SUMMARY	1
II.	PROFORMA ADJUSTMENTS INCORPORATED	5
III.	PROFORMA ADJUSTMENTS REJECTED	16

COMMONWEALTH OF KENTUCKY

BEFORE THE

PUBLIC SERVICE COMMISSION

IN THE MATTER OF: APPLICATION OF :
KENTUCKY UTILITIES COMPANY FOR :
APPROVAL OF AN ALTERNATIVE METHOD: CASE NO. 98-474
OF REGULATION OF ITS RATES AND SERVICE :

and

KENTUCKY INDUSTRIAL UTILITY :
CUSTOMERS, INC. :
Complainant : CASE NO. 99-083

v. :

KENTUCKY UTILITIES COMPANY :

Defendant :

ADDITIONAL DIRECT TESTIMONY OF LANE KOLLEN

I. QUALIFICATIONS AND SUMMARY

1

2 Q. Please state your name and business address.

3 A. My name is Lane Kollen. My business address is J. Kennedy and Associates, Inc.
4 ("Kennedy and Associates"), 35 Glenlake Parkway, Suite 475, Atlanta, Georgia 30328.

5

6 Q. Have you previously filed testimony in this proceeding?

7 A. Yes. I previously filed Direct Testimony on behalf of the Kentucky Industrial Utility
8 Customers, Inc. ("KIUC") in this proceeding addressing the Company's overearnings
9 and the necessity for a base revenue reduction.

1 **Q. What is the purpose of your Additional Direct Testimony?**

2 A. The purpose of this testimony is to update and refine the quantification of Kentucky
3 Utilities Company's (the "Company" or "KU") overearnings and the appropriate base
4 revenue reduction.

5
6 **Q. Please summarize your testimony.**

7 A. The Company's base revenues should be reduced by \$58.412 million, or \$47.812
8 million more than the \$10.600 million base revenue reduction that will be implemented
9 on July 2, 1999 pursuant to the Commission's April 13, 1999 Order in this proceeding.
10 The Company's ratemaking return on common for the test year 1998 is 16.2%
11 compared to a required return of 9.55%. Thus, the Company's current base revenues
12 are excessive and are not fair, just and reasonable. The computations underlying my
13 quantification of the base revenue reduction are summarized on my Exhibit __ (LK-1).

14
15 **Q. Please generally describe the changes that you made to the revenue requirement
16 analysis in your Direct Testimony.**

17 A. I utilized the same revenue requirement methodology, based upon the Commission's
18 historic utilization of rate of return regulation. I updated the test year to the calendar
19 year 1998 from the test year ending September 30, 1998 due to the availability of more
20 detailed information provided by the Company in response to discovery. I relied upon
21 the Company's supplemental response to Item 11 of the Commission's Order dated
22 December 2, 1998, other responses to Commission Staff and KIUC discovery in this
23 proceeding, and other publicly available information.

1

2

The Company proposed numerous proforma adjustments to the 1998 calendar year per books data. These adjustments were proposed in both the supplemental response to Item 11 of the Commission's Order dated December 2, 1998 and the response to PSC#4-KU-7. I have accepted certain of these adjustments and included others of my own. In addition, I have rejected other proforma adjustments proposed by the Company. The following two sections of my testimony address the proformas that I have incorporated and those proposed by the Company that I have rejected.

3

4

5

6

7

8

9

10 **Q. Did you segregate the base, environmental surcharge ("ECR"), and fuel**
11 **adjustment clause ("FAC") components of operating income?**

12 A. No. I assumed that the environmental surcharge cost of service would be incorporated
13 into the base revenue requirement and then reset to zero concurrent with the effective
14 date of the Commission's base revenue reduction in this proceeding. Net incremental
15 environmental costs after that date would be recovered through the ECR. I assumed
16 that FAC revenues were equal to recoverable fuel and purchased power expenses.

17

18 **Q. Did you update the rate of return on common equity reflected in your**
19 **quantification?**

20 A. Yes. I utilized the updated 9.55% recommended by KIUC witness Mr. Baudino.

21

22 **Q. Are the results of your update for the test year 1998 significantly different than**
23 **for the test year ending September 30, 1998 presented in your Direct Testimony?**

- 1 A. No. The base revenue reduction that I recommend is slightly higher for the test year
- 2 1998.

1 **II. PROFORMA ADJUSTMENTS INCORPORATED**

2
3 **Q. Please identify the proforma adjustments that you have incorporated to the per**
4 **books data for the calendar year 1998.**

5 **A.** I have incorporated certain adjustments to operating income, to capitalization, and to
6 rate base. The adjustments that I have incorporated to operating income are as follows:

- 7
- 8 1. Increase revenues to eliminate provision for rate refund.
 - 9
 - 10 2. Increase revenues to reflect increase in customers and sales.
 - 11
 - 12 3. Increase sales for resale revenues to reallocate off-system sales revenue to all
13 jurisdictions, including Kentucky retail.
 - 14
 - 15 4. Increase transmission services revenues to reallocate to all jurisdictions,
16 including Kentucky retail.
 - 17
 - 18 5. Increase O&M expense due to reallocation of sales for resale and transmission
19 services revenues to all jurisdictions, including Kentucky retail.
 - 20
 - 21 6. Increase O&M expense to reflect net retained shareholder savings from merger.
 - 22
 - 23 7. Reduce O&M expense to remove actual Year 2000 costs and replace with
24 amortization over five years.
 - 25
 - 26 8. Increase O&M expense to remove actual Risk Management Trust refund and
27 replace with amortization over five years.
 - 28
 - 29

30 The only adjustment to capitalization that I have incorporated is to reduce common
31 equity to remove nonutility investments.

32
33 The adjustments to rate base that I have incorporated are as follows:

- 34
- 35 1. Reduce rate base to eliminate cash working capital.
 - 36

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- 2. Reduce rate base to eliminate prepayments.
- 3. Reduce rate base to reflect customer deposits.

Q. Please explain why the Commission should eliminate the provision for rate refund.

A. The provision for rate refund is due primarily to the ECR refund booked by the Company in December 1998 related to the settlement of the retroactivity issue. The provision for rate refund is nonrecurring and represents a refund for periods back to 1994. It would be inappropriate to allow the Company to recover the effects of this ECR rate refund as a base revenue requirement. It should be noted that the Company also proposed this proforma adjustment as detailed in its supplemental response to Item 11 of the Commission's Order dated December 2, 1998.

Q. Please explain why the Commission should reflect an increase in revenues in order to annualize customer and sales growth during the test year.

A. The Company achieved customer and sales growth during the test year. However, the test year revenues reflect only one half of that growth going forward. For example, if the number of customers increased by 5% during the year, revenues would reflect only 2.5% of that growth on average. Consequently, the Commission should annualize the effects of the customer and sales growth in the computation of base and ECR revenues.

Q. Please describe how you quantified the increase in revenues in order to annualize customer and sales growth during the test year.

1 A. I determined the weighted average composite growth in customers and applied one half
2 of that growth to the combined test year base and ECR revenues. I determined the
3 weighting of customer growth for this purpose by the combined base and ECR
4 revenues.

5

6 **Q. Please explain why the Commission should adopt a proforma adjustment to**
7 **allocate to Kentucky retail a portion of the revenues from the off-system sales to**
8 **non-all requirements customers (sales for resale).**

9 A. First, such an allocation is consistent with the Commission's prior ratemaking treatment
10 of these amounts. The Company has offered no rationale as to why the Commission's
11 precedent should be overturned and the entirety of these revenues allocated to other
12 jurisdictions.

13

14 Second, such an allocation is consistent with the most basic of cost of service
15 principles. The investment and operating costs necessary to support these off-system
16 sales are allocated to all jurisdictions including Kentucky retail. Thus, the net margins
17 (revenues less incremental costs) also should be allocated to all jurisdictions including
18 Kentucky retail. Without this adjustment, Kentucky ratepayers would be required to
19 pay for the tree, but would receive none of the fruit.

20

21 **Q. Please describe the quantification of the change in sales for resale revenues**
22 **proforma adjustment.**

23 A. The Company performed a jurisdictional cost of service study in response to KIUC-3-

1 38 that provided the reallocation of sales for resale revenues to all jurisdictions,
2 including Kentucky retail. The Company quantified the adjustment to increase
3 Kentucky retail revenues as \$108.690 million.

4

5 **Q. Please explain why the Commission should adopt a proforma adjustment to**
6 **allocate to Kentucky retail a portion of transmission service revenues.**

7 A. First, such an allocation is consistent with the Commission's prior ratemaking treatment
8 of these amounts. The Company has offered no rationale as to why the Commission's
9 precedent should be overturned and the entirety of these revenues allocated to other
10 jurisdictions.

11

12 Second, such an allocation is consistent with cost of service principles. The investment
13 and operating costs necessary to support these transmission services are allocated to all
14 jurisdictions including Kentucky retail. Thus, the revenues also should be allocated to
15 all jurisdictions including Kentucky retail. Again, the Company's position would have
16 Kentucky ratepayers pay for the tree and have shareholders receive the fruit.

17

18 **Q. Please describe the quantification of the change in transmission services revenues**
19 **proforma adjustment.**

20 A. The Company performed a jurisdictional cost of service study in response to KIUC-3-
21 38 that provided the reallocation of transmission services revenues to all jurisdictions,
22 including Kentucky retail. The Company quantified the adjustment to increase
23 Kentucky retail revenues as \$6.033 million.

1

2 **Q. Are reallocations of certain expenses necessary in order to be consistent with the**
3 **proforma adjustments to reallocate sales for resale and transmission services**
4 **revenues?**

5 A. Yes.

6

7 **Q. Please describe the quantification of the proforma adjustment to reallocate**
8 **certain expenses in order to be consistent with the adjustments to reallocate sales**
9 **for resale and transmission services revenues.**

10 A. The Company performed a jurisdictional cost of service study in response to KIUC-3-
11 38 that provided the reallocation of related expenses to all jurisdictions, including
12 Kentucky retail. The Kentucky jurisdictional allocation of operating expenses
13 increased by \$82.235 million, the difference between the \$322.096 million allocation
14 provided by the Company in its supplemental response to Item 11 of the Commission's
15 Order dated December 2, 1998 and the \$404.331 million provided by the Company in
16 response to KIUC-3-38.

17

18 **Q. Please explain why the Commission should reflect an increase to O&M expense in**
19 **order to reflect net retained shareholder savings from the merger.**

20 A. This proforma adjustment is necessary in order to provide the Company with its
21 retained shareholder savings from the merger. Absent this adjustment, all merger
22 savings would flow through to ratepayers. It should be noted that the Company
23 proposed a similar adjustment in its supplemental response to Item 11 of the

1 Commission's Order dated December 2, 1998.

2

3 **Q. Please describe how you quantified the increase to O&M expense in order to**
4 **reflect the net retained shareholder savings from the merger.**

5 A. I utilized the first year net merger savings of \$26.312 million quantified in the merger
6 proceeding. I allocated the net merger savings 47% to LGE and 53% to KU in
7 accordance with the Merger Order. I then quantified the net retained savings at 50%
8 for the Company, also in accordance with the Merger Order. Finally, I multiplied KU's
9 net retained savings by the Kentucky retail jurisdictional factor of 86.708%.

10

11 **Q. Please explain why the Commission should reflect a reduction to O&M expense in**
12 **order to remove actual Year 2000 costs and an amortization expense based upon**
13 **a five year amortization period.**

14 A. Year 2000 costs are nonrecurring. In addition, Year 2000 costs generally extend the
15 useful lives of or otherwise enhance existing software and hardware applications. In
16 some instances, Year 2000 costs replace existing software and hardware applications,
17 thereby creating significant future value. Nevertheless, most Year 2000 costs must be
18 expensed in accordance with generally accepted accounting principles for book
19 accounting purposes. However, the Commission can and should treat these costs as
20 assets with future value and require the Company to defer the costs and amortize them
21 over an appropriate time period. It should be noted the Company also has proposed a
22 similar Year 2000 proforma adjustment in its response to PSC#4-LGE-11 in this
23 proceeding, although it proposed a three year amortization period.

1

2 **Q. Why is a five year amortization period for the Year 2000 costs appropriate?**

3 A. A five year amortization period is appropriate for several reasons. First, five years
4 more closely parallels the merger surcredit period. The amortization period is a matter
5 of judgment and should attempt to balance the effects on ratepayers with the
6 Company's need to recover these costs. It would not be appropriate to set the base
7 revenue requirement to recover these costs over one, two, three, or four years if the
8 Commission does not reasonably anticipate another base rate proceeding within the
9 next four years.

10

11 Second, software and hardware costs are commonly amortized or depreciated over five
12 to ten year periods. The Company has provided no rationale for a three year
13 amortization period.

14

15 Third, a five year amortization period provides the Company full recovery of its Year
16 2000 costs incurred during the test year, although these costs are nonrecurring and the
17 Company already has recovered the costs through retained overearnings.

18

19 **Q. Please explain why the Commission should adopt a proforma adjustment for the**
20 **Risk Management Trust refund.**

21 A. The Company has proposed a proforma adjustment to increase O&M expense in order
22 to reverse the effect of a refund received during the test year. The Company did not
23 propose to amortize the refund. I agree that the refund should not be reflected in a

1 single year because it is nonrecurring. However, the ratepayers should receive the
2 benefit of the refund through an amortization, much as the Company proposed to
3 recover its Year 2000 costs over an amortization period rather than in a single test year.

4 To the extent the discontinuation of the Trust resulted in a refund, the Company
5 overcontributed in prior years through revenues that were paid by ratepayers.

6

7 **Q. What amortization period do you propose for the Risk Management Trust**
8 **refund?**

9 A. I recommend a five year amortization period, consistent with my recommendation
10 regarding the Year 2000 costs.

11

12 **Q. Have you incorporated the Company's proforma adjustment to remove nonutility**
13 **investments from the common equity component of capitalization?**

14 A. Yes. The Company provided the support for this proforma adjustment in its
15 supplemental response to Item 11 of the Commission's Order dated December 2, 1998.

16

17 **Q. Did the Company provide a computation of rate base at December 31, 1998?**

18 A. Yes. The Company provided a computation of rate base in response to the PSC#4-KU-
19 8. I utilized this computation of rate base as a starting point for my computation.

20 **Q. Did you utilize rate base in the KIUC quantification of the Company's revenue**
21 **requirement?**

22 A. Instead of a return on rate base, I utilized the return on capitalization in accordance
23 with the approach historically employed by the Commission. However, I utilized the

1 rate base computations for the purpose of allocating the Company's capitalization to the
2 Kentucky retail jurisdiction.

3

4 **Q. Please explain why the Commission should set cash working capital equal to zero.**

5 A. First, the Company's claim for cash working capital is based upon the one-eighth
6 formula developed by the FERC in the early part of this century, prior to the
7 development and adoption of today's sophisticated cash management techniques and
8 cash flow measurement capabilities. The one-eight formula ensures a positive cash
9 working capital result regardless of the timing of the Company's actual cash flows and
10 simply assumes that investors supply capital for cash working capital purposes.

11

12 Second, the FERC has recognized that the one-eighth formula no longer provides a
13 reasonable quantification of cash working capital requirements. For gas pipeline
14 utilities, FERC assumes that cash working capital is equal to zero unless a party can
15 show differently through a lead-lag study. 18 CFR § 154.306.

16

17 Third, in my experience, it is unusual for an electric utility today to have a positive cash
18 working capital requirement as measured through a properly performed cash lead/lag
19 study. Perhaps understandably, the Company has not performed a cash lead/lag study
20 to enable the Commission actually to quantify the negative amount representing
21 customer supplied cash working capital. Nor has it performed such a study as
22 affirmative evidence that it has a positive cash working capital requirement. In lieu of
23 such a study, it would be reasonable simply to set cash working capital equal to zero

1 for rate base purposes.

2

3 **Q. Please explain why the Commission should set prepayments equal to zero.**

4 A. The reason to set prepayments equal to zero is that the actual cash working capital is or
5 should be sufficiently negative that it would exceed the Company's rate base claim for
6 prepayments.

7

8 **Q. Please explain why the customer deposits should be subtracted from rate base.**

9 A. Customer deposits typically are considered customer supplied capital.

1

2 **Q. Please explain why the Commission should reject the Company's adjustment to**
3 **reduce annual ECR revenues.**

4 A. The KIUC quantification of the Company's revenue requirement is based upon
5 combining the base and ECR revenue requirement for the test year and setting the
6 initial ECR rate to zero on the effective date of the base revenue reduction. The
7 integration of the base and ECR revenue requirement provides the Company full (and
8 higher compared to the current ECR) recovery of its environmental costs. Thus, any
9 deficiency in ECR recovery, represented in part by the Company's proforma
10 adjustment to reduce annual ECR revenues, already is included in the KIUC
11 recommendation. If the Company's adjustment is accepted, there will be a double
12 recovery.

13

14 **Q. Please explain why the Commission should reject the Company's proforma**
15 **adjustment to reduce revenues to reflect "normal" weather.**

16 A. First, the Commission historically has not adopted weather normalization adjustments
17 for electric utilities. Clearly, the adoption of such an adjustment for the Company
18 would be considered precedential in base revenue proceedings involving other utilities
19 and in future proceedings involving the Company.

20

21 Second, the selection of data series and the development of the regression equations
22 and other aspects of the methodologies are subject to considerable judgment.

23 Consequently, a weather normalization adjustment is not a factual determination, but

1 rather an assessment of opinions as to what constitutes "normal" weather for purposes
2 of quantifying this ratemaking adjustment. In the broadest sense, there is disagreement
3 among scientists regarding the extent of global warming, if any, and the duration and
4 measurement of warming cycles. More specifically, the Company has performed its
5 own computation of temperature normals in lieu of the NOAA computations.

6
7 Third, this proceeding is not conducive to a thorough assessment of alternative
8 quantifications of this adjustment, if the Commission were to change its historic
9 rejection of such adjustments for electric utilities. There are procedural limitations to
10 the development of a comprehensive record on this issue.

11
12 **Q. Please explain why the Commission should reject the Company's proposed**
13 **adjustment for the Team Incentive Award extension to all KU employees.**

14 **A.** First, this proforma adjustment is a selective single issue post test year adjustment. The
15 Company adamantly has refused to provide 1999 budget information in response to
16 KIUC discovery, alleging that to do so would violate federal securities laws.
17 Nevertheless, the Company specifically relied upon its 1999 budget (response to
18 PSC#4-KU-7 page 6 of 60) to compute this adjustment. On a procedural basis alone,
19 this adjustment should be rejected. However, it also should be rejected as a matter of
20 regulatory principle. This adjustment fails to consider all other increases and decreases
21 in the cost of service that should be considered if the test year was calendar year 1999.
22 Yet, no party other than the Company has access to calendar year 1999 budget
23 information. It would be unfair, inequitable, and unreasonable to allow this adjustment

1 in this proceeding.

2
3 Second, the Company failed to provide any rationale for this adjustment, other than a
4 statement that the Team Incentive Award would be extended to all KU employees. If
5 this award is based on cost savings achievement, then there should be a proforma for
6 cost savings. If this award is based upon earning excessive rates of return for
7 shareholders at the expense of the Company's ratepayers, then this award should not be
8 recoverable from ratepayers. In any event, the Commission should reject this proforma
9 adjustment as unsupported and incomplete.

10
11 Third, if the award is based upon actual achievement in 1999, then not only is it a post
12 test year adjustment, it cannot possibly be known and measurable. Thus, it also should
13 be rejected on that basis.

14
15 **Q. Please explain why the Commission should reject the Company's proposed**
16 **adjustment to increase purchased power expense to reflect its projections of 1999**
17 **market prices.**

18 A. First, this adjustment represents a selective single issue post test year adjustment. The
19 Company adamantly has refused to provide 1999 budget information, alleging that to
20 do so would violate federal securities laws. Yet, on this one issue, it understandably is
21 willing to provide its projections of purchased power costs for 1999. Clearly, this
22 adjustment is self-serving and inappropriate.

23 Second, the Company has assumed higher market prices for this adjustment, which

1 would increase its revenue requirement, while also assuming lower market prices for its
2 proposed off-system sales margins proforma adjustment. The Company's position is
3 intractably ridiculous and should be rejected. If the Commission were to utilize
4 historic purchased power costs for the Company, the proforma adjustment would be to
5 significantly reduce purchased power costs. For example, purchased power costs were
6 at a three year high in 1998 at \$126.584 million compared to \$72.542 million in 1997
7 and \$62.490 million in 1996. A three year average of purchased power expense would
8 result in a reduction to purchased power expense of \$39.379 million.

9
10 Third, apparently the Company believes that "forward prices" will increase for
11 purposes of its proposed purchased power adjustment, but that "forward prices" also
12 will decrease, according to its response to KIUC-3-12, a copy of which is attached as
13 my Exhibit ____ (LK-2)

14
15 Fourth, the Company's proforma adjustment to increase purchased power expense and
16 thus the base revenue requirement is premised, at least in part, upon the assumed non-
17 existence of the FAC. Historically, purchased power costs, to the extent they were
18 shown to be purchased on an economic dispatch basis, were allowed recovery through
19 the FAC. If the FAC remains in effect, then all or part of the higher purchased power
20 costs will be recoverable through the FAC.

21
22 Fifth, the Company's proforma adjustment is dependent upon the same level of
23 purchases in 1999. There is no evidence to suggest that will be the case. In fact, there

1 is virtually no probability that 1999 purchased power will be at the same levels as in
2 1998 since new CTs will be operational in 1999, loads will be different, fuel costs will
3 be different, forced outages will be different, and the economics of market purchases
4 will be different.

5
6 **Q. Please explain why the Commission should reject the Company's proposed**
7 **adjustment to reduce the off-system sales margins to hypothetical levels based**
8 **upon historic margins.**

9 A. First, this adjustment is conceptually absurd for the reasons discussed in conjunction
10 with the Company's proposed purchased power adjustment. If the Company believes
11 that market prices are increasing, then its off-system sales margins also should increase,
12 not decline.

13
14 Second, this adjustment is an overt attempt to leverage into the future a higher retention
15 of off-system sales margins. These off-system sales margins are possible largely
16 because of the costs (investment and fixed operating) paid for by ratepayers through the
17 base and ECR revenue requirements. Nevertheless, between base revenue proceedings,
18 the Company is allowed to retain the entirety of off-system sales margins in excess of
19 the levels reflected in the test year utilized in its last base revenue proceeding.

20 Unfortunately, the Company apparently is not satisfied with that arrangement and now
21 has proposed that the test year sales margins not be fully reflected in the revenue
22 requirement. This proposed adjustment is inequitable, unfair, and unreasonable. The
23 balance should not be tipped further toward the Company.

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Third, it would be complete speculation at this time to adjust the test year level of off-system sales margins based upon the expectation that the Company's units may face extended outages to comply with the pending NOx regulations. The NOx regulations are being challenged in court, the state SIP-call is not due until September 1999, and affected sources have until May 2003 to install control measures (unless granted extensions so that the compliance date is delayed). The Company has not proposed a NOx compliance plan detailing which units will receive certain NOx control technology or when. The Commission certainly has not approved any such compliance plan. Therefore, the NOx rules cannot be the justification for a "known and measureable" change to the test year level of off-system sales margins. To the contrary, the resolution of that matter is uncertain.

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14 **Q.**

Please explain why the Commission should reject the Company's proposed adjustment to reflect the hypothetical implementation of the EPBR tariff in 1998.

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16 **A.**

First, the Commission should determine the base revenue requirement without consideration of the EPBR. Conceptually, the EPBR tariff is structured as a reward or penalty to the Company. It would be inappropriate to embed either a reward or penalty pursuant to the EPBR into base rates.

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Second, the Company's adjustment would increase fuel costs in the test year compared to actual for 1998, the FCR component of the EPBR would have resulted in higher fuel costs of \$1.322 million to ratepayers than the currently effective fuel adjustment clause.

1 This fact illustrates the poor design and the detrimental impact of the FCR component
2 of the Company's EPBR, if not the entirety of the EPBR.

3
4 Third, the Company's adjustment would result in a double recovery of the FCR reward
5 both through base rates and the EPBR tariff. That double recovery should not be
6 allowed.

7
8 Fourth, the Company's computation of the SQ component of the EPBR is incorrect.
9 The sign is wrong. The Company's service quality during the test year was less than
10 the standard in the tariff. Therefore, there should have been a penalty, not a reward.

11 However, in the Company's computation, the SQ penalty was incorrectly translated
12 into a reward and an increase in the base revenue requirement. In addition, assuming
13 there had been an SQ reward, the amount is not incrementally recoverable from
14 ratepayers, but only can be utilized to offset the GP component. Company witness Mr.
15 Willhite stated the following in his Direct Testimony in Case No. 98-426:

16 **"Combined service quality measures that result in a reward for the**
17 **current quarter will only be included in the EPBR formula to the**
18 **extent that the Generation Performance amounts are available to**
19 **offset this reward. Any Service Quality reward in excess of the**
20 **Generation Performance will be banked and included in the**
21 **following quarter's Service Quality computation. Any rewards not**
22 **recovered after four quarters will be relinquished. As a result,**
23 **Service Quality rewards do not directly cause an increase in**

1 customers' bills." (emphasis added)

2

3 **Q. Please explain why the Commission should reject the Company's proposed**
4 **adjustment for the EPBR rate reduction.**

5 A. The Commission should first determine the Company's revenue requirement and the
6 appropriate base revenue reduction absent consideration of the EPBR. It then can
7 determine the necessary incremental adjustment to the rate reduction already in effect.
8 In this manner, the rate reduction is not dependent upon the adoption of the EPBR, but
9 rather upon the Company's cost of service.

10

11 **Q. Does this complete your Additional Direct Testimony?**

12 A. Yes.

KENTUCKY UTILITIES COMPANY
SUMMARY OF REVENUE REQUIREMENT
12 MONTHS ENDING DECEMBER 31, 1998
(\$000)

	Unadjust Total KU	Unadjust "Other Juris"	Unadjust "KY Retail Juris"	Adjust to "KY Retail Juris"	Adjusted "KY Retail Juris"
Capitalization (1)	1,206,941	160,707	1,046,234	NA	1,046,234
Required Overall Rate of Return	8.12%	8.12%	8.12%	8.12%	8.12%
Required Operating Income	97,948	13,042	84,906	0	84,906
Per Books Operating Income	125,388	36,947	88,441	31,294	119,735
Operating Income Surplus	27,440	23,905	3,535	31,294	34,829
Revenue Surplus	46,020	40,091	5,929	52,483	58,412
Electric Revenues before Rate Reduction	810,115	225,561	584,554	141,478	726,032
Rate Reduction as % of Electric Revenues	5.68%	17.77%	1.01%		8.05%
Return on Common Equity before Rate Reduction	14.10%	39.33%	10.23%		16.22%
Effect of 1% Change in ROE					8,764

Note 1: Capitalization utilized by Kentucky PSC in lieu of rate base. Approximately equal.

KENTUCKY UTILITIES COMPANY
SUMMARY OF OPERATING INCOME
12 MONTHS ENDING DECEMBER 31, 1998
(\$'000)

	Unadjust Total KU	Unadjust "Other Juris"	Unadjust "KY Retail Juris"	Adjust to "KY Retail Juris"	Adjusted "KY Retail Juris"
Operating Revenues					
Residential	238,898	18,107	220,791	(1),(2)	220,791
Commercial and Industrial	344,907	18,048	326,859	4,598 (1),(2)	331,457
Public Street and Highway Lighting	6,483	207	6,276	(1),(2)	6,276
Other Sales to Public Authorities	52,332	2,497	49,835	(1),(2)	49,835
Sales for Resale	179,118	179,118	0	108,690 (3)	108,690
Provision for Refund	(23,724)	(1,567)	(22,157)	22,157 (4)	0
Other Operating Revenues	12,101	9,151	2,950	6,033 (5)	8,983
Total Operating Revenues	810,115	225,561	584,554	141,478	726,032
Operating Expenses					
Fuel, Purchased Power, and Other Oper Exp	465,630	143,534	322,096	88,995 (3),(5),(6)	411,091
Maintenance Expense	63,608	9,756	53,852		53,852
Depreciation	86,657	12,016	74,641		74,641
Other Taxes	15,946	2,746	13,200		13,200
Federal and State Income Taxes	53,256	20,615	32,641	21,189	53,830
Other	(370)	(53)	(317)		(317)
Total Operating Expenses	684,727	188,614	496,113	110,184	606,297
Net Operating Income	125,388	36,947	88,441	31,294	119,735

Note 1:

Annualization to year end customers/sales levels.

Note 2:

No annualization of merger surcredit revenues and no annualization of customers' savings.

Note 3:

Reallocation of sales for resale revenues and related expenses to retail and FERC jurisdictions (KU response KIUC#3-38(a) page 3 of 4.

Note 4:

\$21.5 million of this provision for rate refund is due to the ECR settlement in December 1998.

Note 5:

Reallocation of transmission service revenues and related expenses to retail and FERC jurisdictions (KU response to KIUC#3-38(a) page 3 of 4.

Note 6:

\$6.046 million first year annual amount of KU net retained savings (projected by KU in merger proceeding as \$26.312 million times 53% KU share times 50% retained share times .86708 KY retail jur). Reversal of Risk Management Trust refund of \$1.852 million less one year amortization of \$0.370 million (over 5 years). Reversal of Year 2000 expense of \$0.960 million less one year amortization of \$0.192 million (over five years).

KENTUCKY UTILITIES COMPANY
SUMMARY OF COST OF CAPITAL
12 MONTHS ENDING DECEMBER 31, 1998
(\$000)

	Capital \$ w/o ITC (1)	Capital % without ITC	COC w/o ITC (2)	Wtd COC without ITC	Capital \$ with ITC	Capital % with ITC	COC with ITC	Wtd COC with ITC	Capital \$ ITC Alloc
Long and Short Term Debt	543,584	45.83%	6.99%	3.20%	532,077	44.08%	6.99%	3.08%	541,909
Preferred Equity	39,799	3.36%	5.64%	0.19%	40,000	3.31%	5.64%	0.19%	40,739
Common Equity	602,808	50.82%	9.55%	4.85%	612,562	50.75%	9.55%	4.85%	623,881
Total Capitalization	1,186,191			8.25%	1,184,639				
Investment Tax Credit (3)					22,302	1.85%	0.00%	0.00%	
Total Capitalization with ITC					1,206,941			8.12%	1,206,529

Note 1: Capitalization amounts are for total Company and were provided by Company in supplemental response to Commission Question No. 11 parts (a) and (b) attached to Commission Order dated December 2, 1998.

Note 2: Cost of debt and preferred were provided by Company in response to PSC-4-KU-10(c). Cost of common provided by KIUC witness Baudino.

Note 3: Obtained from KU 1998 SEC Form 10-K page 153.

KENTUCKY UTILITIES COMPANY
SUMMARY OF RATE BASE
12 MONTHS ENDING DECEMBER 31, 1998
(\$000)

	Unadjust Total KU	Unadjust "Other Juris"	Unadjust "KY Retail Juris"	Adjust to "KY Retail Juris"	Adjusted "KY Retail Juris"
Plant in Service	2,602,167	368,761	2,233,406	NA	2,233,406
CWIP	83,361	10,516	72,845	NA	72,845
Accumulated Depreciation	(1,208,183)	(177,620)	(1,030,563)	NA	(1,030,563)
Accumulated Deferred Inc Taxes (Net)	(291,840)	(44,302)	(247,538)	NA	(247,538)
Fuel Inventories	23,927	3,432	20,495	NA	20,495
M&S Inventories	24,248	3,502	20,746	NA	20,746
Net Regulatory Assets/Liabilities	(26,999)	(3,702)	(23,297)	NA	(23,297)
Customer Deposits	(10,354)	(659)	(9,695)	NA	(9,695)
Customer Advances	(1,265)	(53)	(1,212)	NA	(1,212)
Investment Tax Credit	(22,302)	(3,719)	(18,583)	NA	(18,583)
Total Rate Base	1,172,760	156,156	1,016,604	NA	1,016,604

LOUISVILLE GAS AND ELECTRIC COMPANY
KENTUCKY UTILITIES COMPANY
CASE NOS. 98-426 AND 98-474

Response to KIUC's 3rd Data Request dated April 30, 1999

Question: KIUC#3-12

Responding Witness: Ronald L. Willhite

Q-12 Provide all documents, memoranda, and other written information to support the assertion that off-system sales are expected to decrease by 40% by 2001.

- a) Explain how this forecast includes the added capacity available to KU and LG&E from the two 164 MW CT's currently being built at the Brown site.
- b) Explain how this forecast includes the new all requirements sale by KU to the municipal electric system of Pitcarin, Pennsylvania.

A-12. Please see the response to AG Data Request No. 96.

- a) The forecast levels of off-system sales include three major considerations: available capacity, native load, and the forward price curve. The CTs being built at the Brown site are included in off-system sales forecast simulations. As such, the CTs increase the amount of capacity available to KU and LG&E. However, the forecast for native load also increases over the period. The magnitude of the increase in native load is partially offset by the increase in available capacity provided by the CT addition. The third factor is the forward price curve, i.e., expected market prices for power for future time periods. Forward prices have a significant impact on the off-system sales forecast because those prices determine how much power may be sold on an economic basis. Data that represent the decline in forward prices is provided in the attached Question AG-16 in PSC Case No. 99-056.
- b) The load requirements of the Borough of Pitcarin are included in the KU base load forecast. As such, the sale is included in the forecast for future off-system sales.

LOUISVILLE GAS AND ELECTRIC COMPANY
KENTUCKY UTILITIES COMPANY
CASE NO. 99-056

Response to Attorney General's 1st Data Request Dated April 1, 1999

Question: AG-16

Responding Witness: James Kasey

- Q-16. On page 9 of his testimony, Mr. Kasey provides January and February forward prices for the summer of 1999. Please provide the present forward prices for future months for power as far into the future as prices are available. For these prices please provide details of the type of power (ex. on-peak 5x16).
- A-16. As of April 8, 1999, the following are the prices in \$/MWh for 50 MW of On-Peak (5x16 excluding holidays) firm power with liquidated damages delivered into Cinergy with Seller's choice of interface. (Where two or more months are listed together, the months trade as a package for the same price per MWh.) These prices are subject to change on a daily basis.

Term	Bid (\$/MWh)	Offer (\$/MWh)
May 1999	26.00	26.30
Jun 1999	51.00	52.50
Jul & Aug 1999	104.00	110.00
Sep 1999	32.50	33.50
Q4 1999	24.00	24.40
Jan & Feb 2000	28.25	29.00
Mar 2000	23.25	24.50
Apr 2000	21.75	23.00
May 2000	25.50	26.25
Jun 2000	44.00	48.00
Jul & Aug 2000	80.00	86.00
Jul & Aug 2001	70.00	77.00