

COMMONWEALTH OF KENTUCKY  
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

Investigation into the Membership of Louisville  
Gas and Electric Company and Kentucky  
Utilities Company in the Midwest Independent  
Transmission System Operator, Inc.

Case No. 2003-00266

RECEIVED

JUN 29 2006

PUBLIC SERVICE  
COMMISSION

**Reply to Louisville Gas and Electric Company's  
and Kentucky Utilities Company's Response to  
the Midwest ISO's Application for Rehearing**

The Midwest Independent Transmission System Operator, Inc. ("Midwest ISO") hereby replies to the Response of Louisville Gas and Electric Company ("LG&E") and Kentucky Utilities Company ("KU") to its Application for Rehearing of the order issued in the above-captioned case on May 31, 2006 ("the 5/31/06 Order"). In their Response, LG&E and KU repeatedly contend that the Midwest ISO Application does not establish that Commission findings or determinations in the 5/31/06 Order are "unlawful" or "unreasonable" — the standard for a reviewing court to vacate or set aside a Commission order. *See* KRS 278.410(1). The Commission is not restricted to rehearing matters on which a KRS 278.410(1) showing is made or to vacating or setting aside an order on rehearing.<sup>1</sup> As such, the Midwest ISO has laid out a proper foundation in its Application for the Commission to consider and grant a rehearing of the 5/31/06 Order.

**The LG&E/KU Response highlights the need for a rehearing in this matter.**

In their Response, LG&E and KU do not defend the Commission's decision that prior approval pursuant to KRS 278.020(5) was required for the transfer to the Midwest ISO. Instead, they dismiss as "wholly unsupported" (Response at 5) the prejudicial effect of that decision on

---

<sup>1</sup> On rehearing, "the commission may change, modify, vacate or affirm its former orders, and make and enter such order as it deems necessary." KRS 278.400.

consideration of the net benefits of continued Midwest ISO membership. LG&E's and KU's failure to obtain prior approval became a "wrong" that the 5/31/06 Order erroneously concludes diminished the Commission's effective jurisdiction.<sup>2</sup> The only way to right such a wrong was to find that "the Companies' reacquisition of the functional control of their transmission system is for a proper purpose and is consistent with the public interest...." Response at 10. LG&E and KU even assert that "the public interest standard ... includes jurisdictional and other regulatory issues of concern to the Commission, the Companies, and their customers." Response at 11 (emphasis added). Although no authority is cited for that assertion, it reinforces the Midwest ISO's point that legal and factual mistakes in the interpretation and application of KRS 278.020(5) ramified throughout the 5/31/06 Order. Rehearing is necessary to reconsider such jurisdictional issues and to ensure that Commission review of the evidence and testimony is without prejudice toward regaining the jurisdiction of which it believed it had been improperly deprived.

LG&E and KU do attempt a *post hoc* rationalization of the Commission's decision authorizing a transfer of control from the Midwest ISO as consistent with their having the burden of proof. There are, however, a number of problems with this attempt. First, it is for the Commission to make findings based on the record evidence and correct legal standards — not for the parties to speculate about what standard the Commission used or how it might have assessed the evidence relative to a particular standard. In his dissent, Chairman Goss expressly notes the majority's silence about the burden of proof and that the evidence it considered "falls short of the quantification we have required in prior cases...." 5/31/06 Order at 31.

---

<sup>2</sup> In their Response, LG&E and KU do not contest the point made in the Application for Rehearing (at 5-9) that the 5/31/06 Order is based on an exaggerated view of the consequences from the transfer of limited functional control to the Midwest ISO.

Second, weighing the evidence is indeed the province of the Commission, *Energy Reg. Comm'n v. Kentucky Power Co.*, 605 S.W.2d 46, 50 (Ky. App. 1980), but the Commission must use the correct legal standard in doing so. Even if the majority in the 5/31/06 Order expressly determined that the Midwest ISO's benefit-cost studies should be accorded no weight, that would not be equivalent to determining that the LG&E/KU studies met the burden of proof that was established in Case No. 02-475.<sup>3</sup> Finding fault with the Midwest ISO's studies is not an appropriate substitute for addressing issues raised about the LG&E/KU studies and considering the effect of such problems as the underestimated exit fee. Moreover, the burden of proof requires a comparison of the *status quo* with the projected effects of the proposed transfer -- but the LG&E/KU studies did not make a comparison with the only transfer they have actually now proposed. Any deference due is thus to Chairman Goss's findings as to the significance and credibility of the evidence, giving particular weight to his unfavorable comparison of the evidence here to that required in prior cases.

Third, if the Commission's assessment of the LG&E/KU "net benefit projections was independent of the consideration of the exit fee and its appropriate regulatory accounting" as

---

<sup>3</sup> Attempts in the Response to cast the majority's determination as one of "credibility" are inapposite. As a trier of fact, the Commission does have "the exclusive province to pass on the credibility of witnesses," *ERC*, 605 S.W.2d at 50; however, in general, the deference accorded to the trier of fact is given because "the factfinder is in a better position to make judgments about the reliability of some forms of evidence than a reviewing body acting solely on the basis of a written record of that evidence. Evaluation of the credibility of a live witness is the most obvious example ...." *Concrete Pipe and Prod. of Calif., Inc. v. Construction Laborers Pension Trust of So. Calif., Inc.*, 508 U.S. 602, 623 (1993). It is not only that triers of fact "observed the proceedings," but also that "they actively participated by asking many questions of the witnesses themselves...." *New v. Commonwealth*, 156 S.W. 3d 769, 773 (Ky. App. 2005). In this case, the one Commissioner who had the opportunity to hear all the evidence and testimony presented and to judge the credibility of every witness is the dissenter from the majority's conclusions in the 5/31/06 Order. (Commissioner Coker was appointed after the 2004 hearings concluded, and was present for the last two days of hearing, in July 2005.)

LG&E and KU contend (Response at 4), then that reflects an overwhelming legal and factual error in the 5/31/06 Order. Projections of net benefit cannot reasonably be considered to be “independent” of the exit fee — which is undisputedly a major cost to net against hypothesized benefits. Furthermore, the regulatory accounting for that fee affects the showing required of LG&E and KU that the proposed transfer “will not adversely affect the existing level of utility service or rates.” *Kentucky Power*, Case No. 02-475 (Ky. PSC Aug. 25, 2003) at 4.<sup>4</sup> The LG&E/KU cost-benefit study was based on a gross underestimate of the exit fee, and there has been no showing of anticipated net benefits even to LG&E and KU if a reasonable amount is assigned to this cost of withdrawing from the Midwest ISO.

**Information that became available only after the last day of hearing in this case needs to be addressed either on rehearing in this case or in Case No. 05-471.**

LG&E and KU argue that the existence of additional evidence about Day 2 markets not available at the former hearing does not warrant a rehearing of the issues presented. This assertion ignores that the Commission expressly reopened the investigation in this matter in part to consider that very information. All issues in this case had been briefed and submitted to the Commission for consideration when, on June 22, 2004, the Commission issued an Order (“the 6/22/04 Order”) stating that the Day 2 markets’ “impact on the costs and benefits of MISO membership has not been subject to examination and review in this proceeding.” 6/22/04 Order at 1. The Commission reopened the record “[t]o ensure that the evidentiary record in this case is fully developed” regarding the effect of the Day 2 markets. 6/22/04 Order at 2.

---

<sup>4</sup> In his dissent, Chairman Goss specifically notes that there is nothing to protect retail customers from “the consequence if LG&E’s and KU’s projections are wrong.” 5/13/06 Order at 36.

LG&E and KU now argue that analysis of a year's worth of Day 2 market information is unnecessary to the Commission's determination. Response at 8-9.<sup>5</sup> To the contrary, as noted by Chairman Goss:

If a full year's worth of market data were analyzed using both LG&E's, KU's, and MISO's models, it would be possible to test their validity more accurately. While the first year of the market would not produce enough information to estimate the long-run benefits of membership to [LG&E and KU], it would have shown which model had higher predictability and therefore greater certainty.... [I]t would have been easy to reopen the record for the limited purpose of receiving a full year's worth of market data.

5/31/06 Order at 31-32. The Commission viewed the Day 2 market effects as important enough to reopen the record in 2004; to reach a fully informed decision, the Commission should grant a rehearing and consider the question with a fully developed record.

On a related note, LG&E and KU contend that the Midwest ISO tendered an unauthorized filing under KRS 278.400, and thus the document should be stricken from the record. Response at 9. The filing at issue was attached as Exhibit B to the Midwest ISO's Application and serves merely as an example of the type of information the Midwest ISO would offer as evidence if rehearing is granted. The order cited by LG&E and KU to support their request to strike deals with testimony and affidavits filed in support of an application for rehearing, neither of which were filed as part of the Midwest ISO's application.<sup>6</sup> Exhibit B was not introduced or offered as evidence and the Midwest ISO did not intend for the Commission to consider it as such.

Importantly, in its June 13, 2006 Order in Case No. 05-471 ("the 6/13/06 Order"), the Commission found that the accounting and ratemaking provisions contained in LG&E's and

---

<sup>5</sup> *But see* Motion of KU and LG&E to Schedule an Informal Conference, filed 6/22/04, at 1 (requesting an informal conference on issues surrounding the Midwest ISO's proposed Day 2 markets and their anticipated impact).

<sup>6</sup> *See* Response at 9 (citing *An Investigation of Toll and Access Charge Pricing etc.*, Case No. 8838 (Ky. PSC Feb. 4, 1985) at 5).

KU's Stipulation, filed June 2, 2006, may alter the basis upon which the Commission issued the 5/31/06 Order in this matter. 6/13/06 Order at 2. The Commission then suggested two alternate routes to modification of the 5/31/06 Order: (1) if new and relevant information emerged after the hearing in this case but before issuance of the 5/31/06 Order, a rehearing should be requested; or, (2) if new and relevant information emerged since issuance of the 5/31/06 Order, it could be determined in Case No. 05-471 whether changed circumstances justify modification of the 5/31/06 Order. *Id.*

Therefore, the Midwest ISO is attempting to follow the Commission's guidance in seeking a rehearing in this case. The new and relevant Day 2 market information relates to the time period running between the July 2005 hearing and the issuance of the 5/31/06 Order. The Midwest ISO believes the 6/13/06 Order directs that consideration of the Day 2 market information be on rehearing of the 5/31/06 Order. Whether the Commission decides to consider new information in a rehearing of this matter or as part of Case No. 05-471,<sup>7</sup> the purpose would be to make the necessary determinations on a fully developed record.

Significantly, LG&E and KU do not dispute the Midwest ISO's assertion that LG&E's and KU's so-called "TORC option," approved by the Commission in the 5/31/06 Order, is not what the companies have proposed to do in Case No. 05-471. As discussed in the Application for Rehearing (at 16-17), a significant portion of the Commission's analysis dealt with the costs/benefits of LG&E and KU leaving the Midwest ISO and implementing the TORC option. This analysis is now moot because the TORC option is not what LG&E and KU actually propose

---

<sup>7</sup> The Midwest ISO has filed a Renewed Motion for Full Intervention in Case No. 05-471. If the Commission wishes to review the new information there, the Midwest ISO must be allowed to intervene in that case.

to do.<sup>8</sup> LG&E's and KU's specific proposals were first disclosed after the hearing day in this matter (July 21, 2005) and before the issuance of the 5/31/06 Order. A rehearing in the present case is not only the logical proceeding to determine the significance of this change, but is the path indicated in the 6/13/06 Order. Additionally, the post-hearing data now available about the Day 2 markets will provide a greater context from which the Commission can reach a determination as to the relative costs/benefits of a transfer from the Midwest ISO.

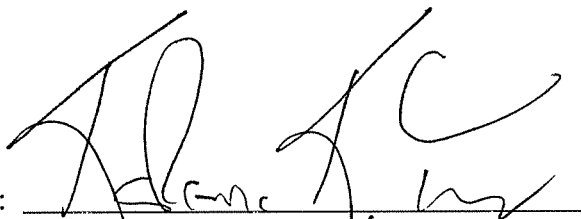
WHEREFORE, for the reasons stated in its Application and in this Reply, the Midwest ISO respectfully requests that the Commission reconsider and rehear matters decided in the 5/31/06 Order and vacate the authorization to LG&E and KU to withdraw from the Midwest ISO.

Respectfully submitted,

Stephen G. Kozey  
MIDWEST INDEPENDENT TRANSMISSION  
SYSTEM OPERATOR, INC.  
701 City Center Drive  
Carmel, IN 46032  
317-249-5431  
fax: 317-249-5912

Katherine K. Yunker  
Oran S. McFarlan, III  
YUNKER & ASSOCIATES  
P.O. Box 21784  
Lexington, KY 40522-1784  
859-255-0629  
fax: 859-255-0746

Stephen L. Teichler  
DUANE MORRIS, LLP  
1667 K. Street N.W., Suite 700  
Washington, DC 20006-1608  
202-776-7830  
fax: 202-776-7801

BY:   
ATTORNEYS FOR MIDWEST INDEPENDENT  
TRANSMISSION SYSTEM OPERATOR, INC.

---

<sup>8</sup> See, e.g., 2nd Am. Jt. Applic. at 7 (¶14), filed in Case No. 05-00471 on February 3, 2006; 4/13/06 FERC compliance filing, filed in Case No. 05-471, at 4-9.

CERTIFICATE OF FILING AND SERVICE

I hereby certify that on the 29th day of June, 2006, the original and ten (10) copies of this Reply were hand-delivered for filing with the Commission, an electronic copy was e-mailed to counsel of record, and a copy was mailed, first-class and postage-prepaid, to:

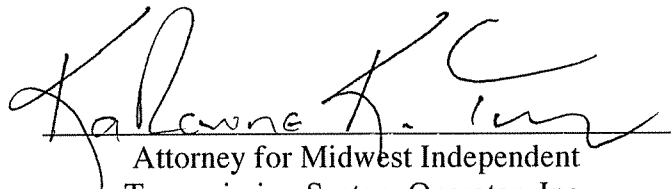
Kent W. Blake  
Director of State Regulation and Rates  
E.ON U.S. LLC  
220 West Main Street  
Louisville, KY 40202

Elizabeth L. Cocanougher  
Senior Corporate Attorney  
E.ON U.S. LLC  
220 West Main Street  
Louisville, KY 40202

David F. Boehm  
Michael L. Kurtz  
BOEHM, KURTZ & LOWRY  
36 East Seventh Street, Suite 1510  
Cincinnati, OH 45202

Elizabeth E. Blackford  
Assistant Attorney General  
Utility and Rate Intervention Division  
1024 Capital Center Drive, Suite 200  
Frankfort, KY 40601

Kendrick R. Riggs  
William Duncan Crosby III  
Sarah K. M. Adams  
STOLL KEENON OGDEN PLLC  
2000 PNC Plaza  
500 West Jefferson Street  
Louisville, KY 40202-2874

  
Attorney for Midwest Independent  
Transmission System Operator, Inc.