

**COMMONWEALTH OF KENTUCKY**  
**BEFORE THE PUBLIC SERVICE COMMISSION**

**In the Matter of:**

**PADDOCK AT EASTPOINT, LLC, LOUIS K. :  
KLEMENZ, AND ST JOSEPH CATHOLIC :  
ORPHAN SOCIETY :**

**COMPLAINANTS :**

**v. :**

**LOUISVILLE GAS AND ELECTRIC :  
COMPANY :**

**DEFENDANT :**

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**NOV 16 2004**

**PUBLIC SERVICE  
COMMISSION**

**CASE NO. 2004-00293**

**REPLAY BRIEF OF  
LOUIS K. KLEMENZ AND  
ST. JOSEPH CATHOLIC ORPHAN SOCIETY'S**

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Comes the Complainants, Louis K. Klemenz and St. Joseph Catholic Orphan Society, by counsel, and hereby submit their Reply Brief in opposition to Louisville Gas and Electric Company's ("LG&E") Motion to Dismiss the above-styled and numbered action.

**ARGUMENT**

LG&E contends that KRS 278.020, as amended July 13, 2004, is retro-active and is not applicable to the above-styled action. It argues that KRS 278.020(2) created a substantive change. We submit that KRS 278.020(2) is procedural and is applicable to LG&E's proposal to extend a

138 kV<sup>1</sup> electrical transmission line in a route which crosses approximately 1,849 feet of property held by Complainants. LG&E has further advised that it intends to presently provide energy only to one of the two 138 kV lines. Notwithstanding, the subject lines will transmit 276 kV.

In Duerson v. East Kentucky Power Cooperative, Inc., Ky. App., 843 S.W.2d 340 (1992) the Kentucky Court of Appeals held that KRS 278.020(1) does not require a Certificate of Convenience and Necessity with respect to (i) retail service connections, and (ii) ordinary course of business extensions. We submit that each of the above exceptions presents questions of fact. Herein, those questions may only be answered by an evidentiary hearing. A determination of fact must be had as to whether LG&E's extension of two (2) 138 kV electrical transmission lines will serve Kentucky retail service connections, or whether LG&E's proposed extension of its electrical lines are in the ordinary course of business considering that such extension will provide power to users (e.g. out-of-state utilities), which transmission admittedly is in a stand-by mode.

LG&E in its initial brief injects certain facts which LG&E would suggest support its position. However, we submit that the injection of these purported facts has created a clear question of fact which may only be determined by a evidentiary hearing to be conducted by the Public Service Commission ("Commission"). The issue to be determined is highlighted by LG&E in its 2003 Financial Report. Pages 26 and 27 with respect to MISO. A copy of pages 26 and 27 are attached hereto and made a part hereto and marked "Exhibit A". By its own admission, LG&E is a founding member of MISO. LG&E reports that it turned over operational control of its high voltage transmission facilities ("100 kV and above") to MISO. LG&E states that MISO controls over

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<sup>1</sup>LG&E has stated that the proposed 100 foot towers which will be constructed within the easement will carry two (2) 138 kV lines.

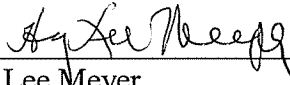
100,000 miles of transmission over 1.1 million square miles located in the northern Midwest between Manitoba, Canada and Kentucky. With that admission there certainly arises a question of fact as to whether LG&E is in compliance with KRS 280.020(1) as it was written prior to the July 13, 2004 amendment. That issue stands regardless of the imposition of the July 13, 2004 amendment.

On July 13, 2004, a Statement of Emergency 807 KAR 5:120E was signed by the Honorable Ernie Fletcher, Governor, Mark David Goss, Chairman of the Public Service Commission and LaJuana S. Wilcher, Secretary of the Environmental Protection Cabinet, a copy of which is attached hereto and made a part hereof and marked Exhibit "B". The Statement, in pertinent part, declared that the Emergency Regulation was necessary to prevent harm to the public health, safety and welfare that would result if a Certificate procedure (our emphasis) was not in place to handle applications for such a new Certificate under KRS 278.020, Chapter 75 (Senate Bill 246). The Statement noted that the procedure is needed to prevent harm to human health and the environment that would result from such a line being built without Commission authorization. Thus, the subject Statement of Emergency addresses applications which we have previously argued is a procedural point not substantive (our emphasis). In support of the position that the July 13, 2004 amendment was procedural, we refer to Administrative Regulation No. 807 KAR 5:120. A copy of which is attached hereto and made a part hereof and marked Exhibit "C". In paragraph (1)(a) the analysis speaks that the subject regulation establishes a procedure for application for a Certificate of Convenience and Necessity for construction lines under KRS 278.020. It is clear that Exhibit "C" speaks to the issue of procedure and the requisite application for a utility to file in compliance with KAR 278.020(2). The substance of the information to be provided is consistent with KRS 278.020(1).

**CONCLUSION**

Complainants submit either prior to or subsequent to July 13, 2004, LG&E is obligated to respond to statutory dictates. Questions of fact must be reviewed which govern LG&E's proposed extension of its electrical transmission line. We urge that LG&E's Motion to Dismiss be overruled.

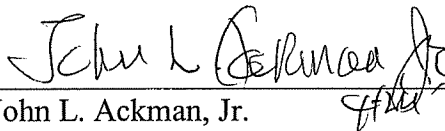
Respectfully submitted,



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- and -



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**CERTIFICATE OF SERVICE**

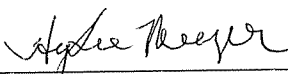
I hereby certify that a true and correct copy of the within Brief on behalf Louis K. Klemenz and St. Joseph Catholic Orphan Society was served this 16th day of November, 2004, by pre-paid first class U.S. mail, to the following:

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Harry Lee Meyer, Esq.

Regarding the transmission system, the Kentucky Commission concluded that the transmission system within Kentucky can reliably serve native load and a significant portion of the proposed new unregulated power plants. However, it will not be able to handle the volume of transactions envisioned by FERC without future upgrades, the costs of which should be borne by those for whom the upgrades are required.

The Kentucky Commission pledged to continue to monitor all relevant issues and advocate Kentucky's interests at all opportunities.

**FERC SMD NOPR.** On July 31, 2002, FERC issued a NOPR in Docket No. RM01-12-000 which would substantially alter the regulations governing the nation's wholesale electricity markets by establishing a common set of rules, defined as SMD. The SMD NOPR would require each public utility that owns, operates, or controls interstate transmission facilities to become an Independent Transmission Provider (ITP), belong to an RTO that is an ITP, or contract with an ITP for operation of its transmission assets. It would also establish a standardized congestion management system, real-time and day-ahead energy markets, and a single transmission service for network and point-to-point transmission customers. Review of the proposed rulemaking is underway and no time frame has been established by the FERC for adoption of a final rule. While it is expected that the SMD final rule will affect LG&E revenues and expenses, the specific impact of the rulemaking is not known at this time.

**MISO.** LG&E and KU are founding members of the MISO. Membership was obtained in 1998 in response to and consistent with federal policy initiatives. In February 2002, LG&E and KU turned over operational control of their high voltage transmission facilities (100kV and above) to the MISO. The MISO currently controls over 100,000 miles of transmission over 1.1 million square miles located in the northern Midwest between Manitoba, Canada and Kentucky. In September 2002, FERC granted a 12.88% ROE on transmission facilities for LG&E, KU and the rest of the MISO owners.

In October 2001, the FERC issued an order requiring that the bundled retail load and grandfathered wholesale load of each member transmission owner be included in the current calculation of the MISO's "cost-adder," the Schedule 10 charges designed to recover the MISO's costs of operation, including start-up capital (debt) costs. LG&E and KU, along with several other transmission owners, opposed the FERC's ruling on this matter. The opposition was rejected by the FERC in 2002. Later that year, the MISO's transmission owners, appealed the FERC's decision to the United States Court of Appeals for the District of Columbia Circuit. In response, in November 2002, the FERC requested that the Court issue a partial remand of its challenged orders to allow the FERC to revisit certain issues, and requested that the case be held in abeyance pending the agency's resolution of such issues. The Court granted the FERC's petition in December 2002. In February 2003, FERC issued an order reaffirming its position concerning the calculation of the Schedule 10 charges and in July 2003 denied a rehearing. LG&E and KU, along with several other transmission owners, have again petitioned the District Court of Columbia Circuit for review. This case is currently pending.

As a separate matter, MISO, its transmission owners and other interested industry segments reached a settlement in mid-2002 regarding the level of cost responsibility properly borne by bundled and grandfathered load under these FERC rulings (such settlement expressly not prejudicing the transmission owners' and LG&E's right to challenge the FERC's ruling imposing cost responsibility on bundled loads in the first instance). In February 2003, FERC accepted a partial settlement between MISO and the transmission owners. FERC did not accept the only contested section of the settlement, which would have allowed the transmission owners to immediately treat unrecoverable Schedule 10 charges as regulatory assets. FERC will consider allowing regulatory asset treatment of unrecoverable Schedule 10 charges on a case-by-case basis.

The MISO plans to implement a congestion management system in December 2004, in compliance with FERC Order 2000. This system will be similar to the Locational Marginal Pricing (LMP) system currently used by the PJM RTO and contemplated in FERC's SMD NOPR, currently being discussed. The MISO filed with FERC a mechanism for recovery of costs for the congestion management system. They proposed the addition of two new Schedules, 16 and 17. Schedule 16 is the MISO's cost recovery mechanism for the Financial Transmission Rights Administrative Service it will provide. Schedule 17 is the MISO's mechanism for recovering costs it will incur for providing Energy Marketing Support Administrative Service. The MISO transmission owners, including LG&E and KU, have objected to the allocation of costs among market participants and retail native load. A hearing at FERC has been completed, but a ruling has not been issued.

The Kentucky Commission opened an investigation into LG&E's and KU's membership in MISO in July 2003. The Kentucky Commission directed LG&E and KU to file testimony addressing the costs and benefits of MISO membership both currently and over the next five years and other legal issues surrounding continued membership. LG&E and KU engaged an independent third party to conduct a cost benefit analysis on this issue. The information was filed with the Kentucky Commission in September 2003. The analysis and testimony supported the exit from MISO, under certain conditions. The MISO filed its own testimony and cost benefit analysis in December 2003. A final Kentucky Commission order is expected in the second quarter of 2004.

**Merger Surcredit.** As part of the LG&E Energy merger with KU Energy in 1998, LG&E Energy estimated non-fuel savings over a ten-year period following the merger. Costs to achieve these savings for LG&E of \$50.2 million were recorded in the second quarter of 1998, \$18.1 million of which was deferred and amortized over a five-year period pursuant to regulatory orders. Primary components of the merger costs were separation benefits, relocation costs, and transaction fees, the majority of which were paid by December 31, 1998. LG&E expensed the remaining costs associated with the merger (\$32.1 million) in the second quarter of 1998.

In approving the merger, the Kentucky Commission adopted LG&E's proposal to reduce its retail customers' bills based on one-half of the estimated merger-related savings, net of deferred and amortized amounts, over a five-year period. The surcredit mechanism provides that 50% of the net non-fuel cost savings estimated to be achieved from the merger be provided to ratepayers through a monthly bill credit, and 50% be retained by LG&E and KU, over a five-year period. The surcredit was allocated 53% to KU and 47% to LG&E. In that same order, the Kentucky Commission required LG&E and KU, after the end of the five-year period, to present a plan for sharing with ratepayers the then-projected non-fuel savings associated with the merger. The Companies submitted this filing in January 2003, proposing to continue to share with ratepayers, on a 50%/50% basis, the estimated fifth-year gross level of non-fuel savings associated with the merger. In October 2003, the Kentucky Commission issued an order approving a settlement agreement reached with the parties in the case. LG&E's merger surcredit will remain in place for another five-year term beginning July 1, 2003 and the merger savings will continue to be shared 50% with ratepayers and 50% with shareholders.

Any fuel cost savings are passed to Kentucky customers through the fuel adjustment clause. See FAC above.

**Environmental Matters.** LG&E is subject to SO<sub>2</sub> and NO<sub>x</sub> emission limits on its electric generating units pursuant to the Clean Air Act. LG&E was not subject to Phase I SO<sub>2</sub> emissions reduction requirements. LG&E's strategy for Phase II SO<sub>2</sub> reductions, which commenced January 1, 2000, is to increase FGD removal efficiency to delay additional capital expenditures and may also include fuel switching or upgrading FGDs. LG&E met the NO<sub>x</sub> emission requirements of the Act through installation of low-NO<sub>x</sub> burner systems. LG&E's compliance plans are subject to many factors including developments in the emission allowance and

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TIME: 4 pm  
JUL 13 2004  
*Conrad Kemper*  
REGULATIONS COMPILER

STATEMENT OF EMERGENCY

807 KAR 5:120E

- (1) Nature of the emergency: Chapter 75 (Senate Bill 246) of the last legislative session enacted an amendment to KRS 278.020 giving the Public Service Commission certificating authority over certain transmission lines, effective July 13, 2004. This emergency regulation is necessary to prevent harm to the public health, safety, and welfare that would result if a certificate procedure were not in place to handle applications for such a new certificate. Specifically, the procedure is needed to prevent harm to human health and the environment that would result from such a line being built without Commission authorization. This harm could include destruction of personal property, environmental and health consequences of unwarranted construction, and damage to air and water resources that could impact human health or the environment.
- (2) The reasons an ordinary administrative regulation is not sufficient. The statute is effective July 13, 2004. An ordinary regulation could not be effective by that date. Thus an emergency regulation is required to bridge the time between the effective date of the statute and the time needed to put a regular regulation in place.
- (3) This emergency administrative regulation shall be replaced by an ordinary administrative regulation filed with the Regulations Compiler.

7.13.04  
Date

*Ernie Fletcher*  
Ernie Fletcher, Governor

7/7/04  
Date

*Mark David Goss*  
Mark David Goss, Chairman  
Public Service Commission

7/13/04  
Date

*LaJuana S. Wilcher*  
LaJuana S. Wilcher, Secretary  
Environmental and Public Protection Cabinet

EXHIBIT "B"



## REGULATORY IMPACT ANALYSIS

Administrative Regulation #: 807 KAR 5:120

Contact Person: A.W. Turner, Jr.

(1) Provide a brief summary of:

(a) What this administrative regulation does: This regulation establishes a procedure for applications for a certificate of convenience and necessity for construction of a transmission line under KRS 278.020. It also provides for public notice of such an application and a procedure for members of the affected public to participate in the certificate proceedings.

(b) The necessity of this administrative regulation: This proposed regulation will assist the Public Service Commission in enforcing the statutes, and is necessary to the Public Service Commission's authority to regulate utilities and enforce KRS Chapter 278.

(c) How this administrative regulation conforms to the content of the authorizing statutes: KRS 278.020 authorizes the Commission to grant certificates of convenience and necessity for construction of certain utility plant. The amendments of Chapter 75 (Senate Bill 246) of the latest legislative session extend this authority to certain significant transmission lines. This regulation establishes procedures for utilities to apply for such a certificate and provides for public participation in that process.

(d) How this administrative regulation currently assists or will assist in the effective administration of the statutes: This regulation establishes the procedure for a public electric utility to apply for a certificate of convenience and necessity to construct a transmission line that, under the amendments to KRS 278.020, requires such a certificate. In addition, the regulation explains how the affected public may participate in the certificate case. Adoption of the regulation will therefore assist the Commission in administering this new set of certificate cases.

(2) If this is an amendment to an existing administrative regulation, provide a brief summary of:

(a) How the amendment will change this existing administrative regulation: NA

(b) The necessity of the amendment to this administrative regulation: NA

(c) How the amendment conforms to the content of the authorizing statutes: NA

(d) How the amendment will assist in the effective administration of the statutes: NA

(3) List the type and number of individuals, businesses, organizations, or state and local governments affected by this administrative regulation: This regulation will affect 21 rural electric utilities their customers, 5 investor-owned electric utilities their customers, and any persons owning property over which a utility proposes to locate such a transmission line.

EXHIBIT "C"

(4) Provide an assessment of how the above group or groups will be impacted by either the implementation of this administrative regulation, if new, or by the change if it is an amendment: The impact of implementing this administrative regulation is not extensive. It will establish necessary procedures for processing applications for transmission line certificates.

(5) Provide an estimate of how much it will cost to implement this administrative regulation:

(a) Initially: Implementation of the proposed amendment will not involve additional costs.

(b) On a continuing basis: No additional costs are expected.

(6) What is the source of the funding to be used for the implementation and enforcement of this administrative regulation: No additional funding is required.

(7) Provide an assessment of whether an increase in fees or funding will be necessary to implement this administrative regulation, if new, or by the change if it is an amendment: No increase in fees or funding is necessary.

(8) State whether or not this administrative regulation establishes any fees or directly or indirectly increases any fees: No.

(9) TIERING: Is tiering applied? (Explain why tiering was or was not used.) Yes, tiering is used in this proposed regulation. The regulation only requires an application for those facilities that are larger and have higher transmission capacities. Larger facilities create a greater potential for disrupting the environment and the use and enjoyment of property upon or near where the lines are proposed to be placed. In addition, larger facilities tend to generate more public involvement in the process.