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Elizabeth O'Donnell
Executive Director
Kentucky Public Service Commission
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Frankfort, KY 40602

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**PUBLIC SERVICE
COMMISSION**

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November 30, 2006

**RE: AN EXAMINATION BY THE PUBLIC SERVICE COMMISSION
OF THE ENVIRONMENTAL SURCHARGE MECHANISM OF
LOUISVILLE GAS AND ELECTRIC COMPANY FOR THE SIX-
MONTH BILLING PERIODS ENDING OCTOBER 31, 2003,
APRIL 30, 2004, OCTOBER 31, 2004, OCTOBER 31, 2005, AND
APRIL 30, 2006, AND FOR THE TWO-YEAR BILLING PERIOD
ENDING APRIL 30, 2005 – CASE NO. 2006-00130**

Dear Ms. O'Donnell:

Please find enclosed and accept for filing the original and ten (10) copies of Revised Corrected Testimony of Robert M. Conroy. The revisions to Mr. Conroy's corrected testimony (corrected testimony filed November 21, 2006) are found on pages 5 and 6. These revisions are to correct a typographical error and provide an explanation for Louisville Gas and Electric Company's ("LG&E") proposal for a 12-month recovery period rather than the four month period originally proposed. LG&E is making this proposal because the magnitude of the under-collection in this case is similar to the magnitude of the over-collection experienced by Kentucky Utilities Company ("KU") in Case No. 2003-00068. In that proceeding, KU experienced a total over-collection of ECR revenues of \$6,022,047 and reflected that over-collection through adjustments to the twelve monthly filings submitted after receipt of the Commission's Order.

Should you have any questions concerning the enclosed, please contact me at your convenience.

Sincerely,

Handwritten signature of Robert M. Conroy in cursive, followed by the initials "RAC" in a bold, sans-serif font.

Robert M. Conroy

Enclosures

cc: Parties of Record

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

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PUBLIC SERVICE
COMMISSION

In the Matter of:

AN EXAMINATION BY THE PUBLIC SERVICE)
COMMISSION OF THE ENVIRONMENTAL)
SURCHARGE MECHANISM OF LOUISVILLE GAS)
AND ELECTRIC COMPANY FOR THE SIX-MONTH)
BILLING PERIODS ENDING OCTOBER 31, 2003,)
APRIL 30, 2004, OCTOBER 31, 2004,)
OCTOBER 31, 2005, AND APRIL 30, 2006, AND)
FOR THE TWO-YEAR BILLING PERIOD ENDING)
APRIL 30, 2005)

CASE NO. 2006-00130

REVISED CORRECTED
DIRECT TESTIMONY OF

ROBERT M. CONROY
MANAGER, RATES
E.ON U.S. SERVICES INC.

Filed: November 30, 2006

1 During the billing periods from September 2004 through the present, LG&E
2 continued to calculate its monthly environmental surcharge calculations in
3 compliance with the Commission's Order in Case No. 2002-00147 by reducing
4 operating and maintenance expenses by a monthly amount of \$22,593.

5 This proceeding presents the first opportunity to remedy the operation of
6 LG&E's environmental surcharge, as this is the first review of the operation of the
7 surcharge for the periods impacted. LG&E's under-recovery position includes the
8 impact of eliminating the expense exclusion ordered by the Commission and LG&E
9 is proposing that the elimination of this exclusion be approved for all months from
10 July 2004 to present and continuing. Upon issuance of an Order in this proceeding,
11 LG&E is proposing to eliminate this expense reduction from the monthly ECR filings
12 and will include an adjustment for the period from March 2006 to the month
13 preceding the Commission order in this proceeding in the appropriate six-month
14 review periods in the future.

15 **Q. Is LG&E proposing any modifications to the operation of the environmental**
16 **surcharge going forward?**

17 A. Not in this proceeding.

18 **Q. What kind of adjustment is LG&E proposing in this case as a result of the**
19 **operation of the environmental surcharge during these billing periods?**

20 A. LG&E is proposing that the cumulative under-recovery of \$6,912,066 be recovered
21 over the twelve months following the Commission's Order in this proceeding.
22 Specifically, LG&E recommends that the Commission approve the increase of the
23 Environmental Surcharge Revenue Requirement by \$576,005 per month for the first
24 six months and \$576,006 per month for the next six months, beginning in the first full

1 billing month following the Commission's Order in this proceeding. LG&E
2 originally proposed a four-month recovery period, consistent with the method of
3 implementing previous over- or under-recovery positions in prior ECR review cases.
4 However, with the determination that LG&E's under-recovery position is
5 approximately \$6.9 million, LG&E is now proposing a recovery period of 12 months.
6 A twelve-month period was approved for KU in Case No. 2003-00068¹, when KU
7 refunded to its customers an over-recovered amount of approximately \$6 million.
8 Because the magnitude of KU's previous over-recovery and LG&E's current under-
9 recovery are similar, LG&E is proposing a recovery period consistent with that
10 approved in KU's prior review case.

11 **Q. What costs were included in the calculation of the environmental surcharge**
12 **factors for the billing periods under review?**

13 A. The capital and operating costs included in the calculation of the environmental
14 surcharge factors for these billing periods were the costs incurred each month by
15 LG&E from March 2003 through February 2006, as detailed in the attachment to
16 Question No. 2 of the Commission Staff Request for Information, incorporating all
17 required revisions. All capital and operating costs are for the pollution control
18 projects identified in the Commission's April 6, 1995 Order in Case No. 94-332, the
19 Commission's April 18, 2001 Order in Case No. 2000-386, the Commission's
20 February 11, 2003 and September 4, 2003 Orders in Case No. 2002-00147, and the
21 Commission's June 20, 2005 Order in Case No. 2004-00421. The environmental rate

¹ In the Matter of: *An Examination By The Public Service Commission Of The Environmental Surcharge Mechanism Of Kentucky Utilities Company For The Six-Month Billing Periods Ending January 31, 2001, July 31, 2001, January 31, 2002, And January 31, 2003 And For The Two-Year Billing Periods Ending July 31, 2000 And July 31, 2002*

1 base amount and pollution control expenses are reasonable and accurate, and are
2 based upon LG&E's business records.

3 The monthly environmental surcharge factors applied during the billing
4 periods under review were calculated consistent with the Commission's
5 determinations in LG&E's previous applications to assess or amend an environmental
6 surcharge, as well as determinations made in previous review cases, most recently
7 Case No 2003-00236. The depreciation rates used to calculate the depreciation
8 expenses were changed following the Commission's approval of the new rates in
9 Case No. 2001-141. The monthly environmental surcharge reports filed with the
10 Commission during this time reflect the various changes to the reporting forms
11 ordered by the Commission from time to time.

12 **Q. Should the Commission in this case approve the incorporation into LG&E's base**
13 **electric rates the environmental surcharge amounts found just and reasonable**
14 **for the two-year billing period ending April 2005?**

15 A. Yes. It is appropriate, at this time, to incorporate surcharge amounts found just and
16 reasonable for the two-year billing period ending April 2005 into electric base rates.
17 LG&E recommends that a surcharge amount of \$8,669,729 be incorporated into base
18 rates at the conclusion of this case. LG&E determined the roll-in amount of
19 \$8,669,729 using the base-current methodology as proposed by Commission Staff
20 and further recommends adoption of the base-current methodology to calculate the
21 monthly environmental surcharge factors going forward. The details of this
22 methodology and the calculation of the amount are presented as attachments to

1 LG&E's response to Question No. 11 to the Commission Staff Request for
2 Information.

3 **Q. What methodology should the Commission use to accomplish the roll-in?**

4 A. The Commission's April 25, 2006 Order in this case at Data Request No. 11 states
5 that "the surcharge factor reflects a percentage of revenue approach, rather than a per
6 kWh approach" and asks "taking this into consideration, explain how the surcharge
7 amount should be incorporated into LG&E's base rates" and to provide any analysis
8 that LG&E believes supports its position. The Commission previously approved
9 LG&E's proposed roll-in methodology in Case No. 2003-00236² which spread the
10 amount of the roll-in equally to every tariff subject to the environmental surcharge. In
11 this proceeding, in response to the Commission's inquiry, LG&E is presenting the
12 total revenue method and an alternative methodology for allocating the roll-in
13 amounts to the various classes of service in a way that gives some recognition to the
14 inter-class rate subsidies that currently exist in LG&E's base rates. While either
15 method will effectively incorporate the correct amount of the surcharge revenues and
16 expenses into base rates, the appropriateness of either method is a policy question for
17 this Commission. The evidence presented by Mr. Seelye clearly shows there are
18 classes with high rates of return providing larger contributions to the companies
19 operating income than those classes with low rates of return. In previous
20 environmental surcharge and base rate proceedings, the Attorney General and the
21 Kentucky Industrial Utility Customers, representing their respective interests, have
22 advanced proposals for correcting inter-class subsidies or have challenged any such

1 movements towards addressing inter-class subsidies. LG&E will be guided by the
2 Commission's decision in this case on whether the change in base rates associated
3 with the ECR roll-in should be accomplished in a way that gives some recognition to
4 the inter-class rate subsidies in current base rates.

5 **Q. If the Commission accepts LG&E's recommendation to incorporate \$8,669,729**
6 **into base rates, what will be the impact on LG&E's revenue requirement?**

7 A. The incorporation of the recommended surcharge amounts into base rates will
8 increase base rates and simultaneously reduce ECR revenues by an equal amount.
9 Therefore, there will be no impact on LG&E's revenue requirement.

10 **Q. What Base Environmental Surcharge Factor (BESF) is LG&E proposing to use**
11 **for the amount rolled into base rates?**

12 A. LG&E calculated a new BESF, using base revenues for the 12-months ending
13 February 2006, of 3.36%. However, the actual BESF will be calculated using base
14 revenues for the 12-month period ending with the month preceding the month the
15 Commission issues an order approving the roll-in. The timing and method LG&E
16 will use to determine the final BESF is consistent with the Commission's Order in
17 Case No. 2003-00068³.

18 **Q. What rate of return is LG&E proposing to use for all ECR Plans upon the**
19 **Commission's Order in this proceeding?**

² In the Matter of: *An Examination by the Public Service Commission of the Environmental Surcharge Mechanism of Louisville Gas and Electric Company for the Two-Year Billing Periods Ending April 30, 2003*, Case No. 2003-00236, Order (December 11, 2003).

³ *In the Matter of: An Examination by the Public Service Commission of the Environmental Surcharge Mechanism of Kentucky Utilities Company for the Six-Month Billing Periods Ending January 31, 2001, July 31, 2001, January 31, 2002, and January 31, 2003 and for the Two-Year Billing Periods Ending July 31, 2000 and July 31, 2002*, Case No. 2003-00068, Order (October 17, 2003).

1 A. As shown in response to the Commission Staff Request for Information, Question No.
2 16, LG&E is proposing an overall rate of return of 11.23%, calculated using adjusted
3 capitalization and the currently approved 10.50% return on equity.

4 **Q. What is your recommendation to the Commission in this case?**

5 A. LG&E makes the following recommendations to the Commission in this case:

6 a) The Commission approve the proposed increase to the Environmental
7 Surcharge Revenue Requirement of \$576,005 per month in the first six
8 months and \$576,006 per month in the next six months, beginning
9 with the first billing month following the Commission's decision in
10 this proceeding;

11 b) The Commission should find environmental surcharge amounts for the
12 two-year billing period ending April 2005 to be just and reasonable;

13 c) The Commission should find that LG&E should eliminate the expense
14 reduction ordered in Case No. 2002-00147 from the monthly ECR
15 filings beginning with the expense month of July 1, 2004;

16 d) The \$8,669,729 should be approved to be the amount to be
17 incorporated into base electric rates for bills rendered on and after the
18 second full billing month following the month in which an order is
19 received in this case;

20 e) The Commission should decide as a matter of policy whether the
21 Environmental Surcharge mechanism should be used to address the
22 inter-class rate subsidies that currently exist in LG&E's base rates and
23 based on that decision approve either the use of allocating the roll-in
24 amount on the basis of class base rate revenues or a methodology that

1 allocates the roll-in amount in a way that gives some recognition to the
2 inter-class rate subsidies that currently exist in base rates;

3 f) The Base Environmental Surcharge Factor be reset to an amount based
4 on the roll-in amount and the most recent 12-month period available
5 following the Commission's Order in this proceeding; and

6 g) The rate of return on the Post-1995 Plan be established as 11.23%.

7 **Q. Does this conclude your testimony?**

8 **A. Yes.**