IN THE MATTER OF: )
)
THE APPLICATION OF KENERGY ) CASE NO.
CORP. FOR AN ADJUSTMENT IN ) 2006-00369
EXISTING RATES )

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**RESPONSE OF KENERGY CORP.**
**TO FIRST DATA REQUEST OF**
**KENTUCKY INDUSTRIAL UTILITY CUSTOMERS, INC.**

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**CASE NO. 2006-00369**

**Item 1)** Based upon Kenergy's cost-of-service study, please provide the annual dollar amount by which the distribution rates paid by the Smelters are above cost-of-service.

**Response)** As shown on page 1 of Exhibit 16, the operating margin produced by the Smelters in 2005 was $194,071, or 0.1% of revenue. The expenses assigned to the Smelters were $189,202,692, of which $213,802 was for distribution expenses. Kenergy considers the margins produced by the Smelters to be reasonable. In Case No. 2003-00165, the Commission agreed. In their order, the Commission stated the following: "After reflecting this rate reduction, the level of margins provided by the distribution adder for Schedules 32 and 34 are fair, just, and reasonable. Absent a significant change in Kenergy's circumstances, there is no basis for any further reductions to these distribution adders". Therefore, the distribution rates paid by the Smelters are not above cost-of-service including a fair, just and reasonable margin.

**Witness)** Jack Gaines

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**Item 2)** Based upon Kenergy's cost-of-service study, please provide the annual dollar amount by which the distribution rates paid by the direct served large industrial customers are above cost-of-service.

**Response)** As shown on page 1 of Exhibit 16, the operating margin produced by the Class B large industrials in 2005 was $142,094, or 0.6% of revenue. The expenses assigned to the Class B large industrials were $21,764,606 of which $94,217 was for distribution expenses. Kenergy considers the margins produced by the Class B customers to be reasonable. In Case No. 2003-00165, the Commission agreed. In their order, the Commission stated the following: "After reflecting this rate reduction, the level of margins provided by the distribution adder for Schedules 32 and 34 are fair, just, and reasonable. Absent a significant change in Kenergy's circumstances, there is no basis for any further reductions to these distribution adders". Therefore, the distribution rates paid by the Class B customers are not above cost-of-service including a fair, just and reasonable margin.

**Witness)** Jack Gaines

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**Item 3)** Please explain why Kenergy did not propose to lower the distribution rates paid by the direct served large industrial customers and the Smelters.

**Response)** Kenergy does not believe the rates for direct served large industrial customers and the Smelters should be lowered because Kenergy considers the margins produced by the two classes to be reasonable for the reasons cited in responses to 1) and 2). Furthermore, the Smelters and Class B customers have benefited from reduced rates in the last two cases filed by Kenergy. Even if the margins paid by the direct served large industrial customers and the Smelters are found by the Commission in this case to be unsupported by the cost of service, the distribution rates paid by them should not be reduced for the same reason that Kenergy is not proposing to reduce its Three Phase rates and the Class C rates. The results of Kenergy's proposal are that an increase of 7.59% is applied to residential and an increase of 7.54% is applied to small commercial. No increase was applied to Three Phase, Lights or the Direct Served Industrials. To decrease revenues from any of these three classes would result in even greater increases to the residential and small commercial classes.

**Witness)** Jack Gaines

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**Item 4)** Please explain why Kenergy believes that the current distribution rates paid by the direct served large industrial customers and the Smelters are reasonable.

**Response)** In its order in Case No. 2003-00165, the Commission stated: "The customers served under those two schedules are unique to Kenergy's system both in their size and the nature of their service. While recognizing these factors, the Commission has also considered non-cost factors, such as revenue stability, rate continuity, and gradualism, as we have historically done in prior rate cases. Considering both the cost and non-cost factors discussed herein, as well as the need for Kenergy to make a further filing by the end of this year to address its earnings after the consolidation credit rider has expired - - - - , the Commission finds that the $162,347 rate reduction approved herein should be allocated to rate Schedules 32 and 34. After reflecting this rate reduction, the level of margins provided by the distribution adder for Schedules 32 and 34 are fair, just, and reasonable. Absent a significant change in Kenergy's circumstances, there is no basis for any further reductions to these distribution adders."
The Class A and Class B rates provide margins of .1% and .6% of revenue. The amounts paid are reasonable given the magnitude of the revenues and sales volumes.

**Witness)** Jack Gaines