

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

AN EXAMINATION BY THE PUBLIC SERVICE)	
COMMISSION OF THE ENVIRONMENTAL)	
SURCHARGE MECHANISM OF KENTUCKY)	
POWER COMPANY FOR THE SIX-MONTH)	CASE NO.
BILLING PERIODS ENDING JUNE 30, 2006 AND)	2007-00381
DECEMBER 31, 2006, AND FOR THE TWO-YEAR)	
BILLING PERIOD ENDING JUNE 30, 2007)	

O R D E R

On May 27, 1997, the Commission approved Kentucky Power Company's ("Kentucky Power") environmental surcharge application and established a surcharge mechanism.¹ Pursuant to KRS 278.183(3), at 6-month intervals, the Commission must review the past operations of the environmental surcharge. After hearing, the Commission may, by temporary adjustment in the surcharge, disallow any surcharge amounts found not to be just and reasonable and reconcile past surcharges with actual costs that are recoverable pursuant to KRS 278.183(1). At 2-year intervals, the Commission must review and evaluate the past operations of the environmental surcharge. After hearing, the Commission must disallow improper expenses and, to the extent appropriate, incorporate surcharge amounts found just and reasonable into the existing base rates of the utility.

¹ Case No. 1996-00489, The Application of Kentucky Power Company d/b/a American Electric Power to Assess a Surcharge Under KRS 278.183 to Recover Costs of Compliance with the Clean Air Act and Those Environmental Requirements Which Apply to Coal Combustion Waste and By-Products, final Order dated May 27, 1997.

The Commission has determined that it will be administratively efficient and reasonable to review the pending 6-month periods and the 2-year period in the same case. Therefore, the Commission hereby initiates the 6-month reviews of the surcharge as billed from January 1, 2006 to June 30, 2006 and from July 1, 2006 to December 31, 2006, and the 2-year review of the surcharge as billed from July 1, 2005 to June 30, 2007.²

To facilitate this review, a procedural schedule is set forth in Appendix A, attached hereto and incorporated herein. In accordance with that schedule, Kentucky Power is to file prepared direct testimony: (a) in support of the reasonableness of the application of its environmental surcharge mechanism during the time periods under review; and (b) on a proposal to roll-in its environmental surcharge into existing base rates. In addition, Kentucky Power is to file its response to the information requested in Appendix B, attached hereto and incorporated herein. Since each of the periods under review in this proceeding may have resulted in over- or under-recoveries, the Commission will entertain proposals to adopt one adjustment factor to net all over- or under-recoveries.

Since the approval of its original environmental compliance plan and surcharge mechanism, Kentucky Power has sought and been granted three amendments to its

² Since Kentucky Power's surcharge is billed on a two-month lag, the amounts billed from January 2006 through June 2006 are based on costs incurred from November 2005 through April 2006; amounts billed from July 2006 through December 2006 are based on costs incurred from May 2006 through October 2006; and amounts billed from July 2005 through June 2007 are based on costs incurred from May 2005 through April 2007.

original compliance plan and surcharge mechanism.³ In Case No. 2005-00341,⁴ the capital expenditures and operating expenses associated with the original and first amendment to the environmental compliance plan as of the test-year were rolled-in to Kentucky Power's base rates. After this roll-in, the environmental surcharge provides recovery of the incremental costs associated with the original and first amendment to the compliance plan as well as the costs associated with the second and third amendments to the compliance plan. When determining its over- and under-recovery of the surcharge in this proceeding, Kentucky Power should reflect the impacts of these prior cases, as applicable.

IT IS THEREFORE ORDERED that:

1. The procedural schedule set forth in Appendix A, attached hereto and incorporated herein, shall be followed in this proceeding.
2. Kentucky Power shall appear at the Commission's offices on the date set forth in Appendix A, to submit itself to examination on the application of its

³ See Case No. 2002-00169, The Application of Kentucky Power Company d/b/a American Electric Power for Approval of an Amended Compliance Plan for Purposes of Recovering the Costs of New and Additional Pollution Control Facilities and to Amend Its Environmental Cost Recovery Surcharge Tariff, final Order dated March 31, 2003; Case No. 2004-00081, Motion of Kentucky Power Company d/b/a American Electric Power for Approval of Additional Operating Expenses Associated with Its Environmental Compliance Plan, final Order dated April 16, 2004; Case No. 2005-00068, Application of Kentucky Power Company for Approval of an Amended Compliance Plan for Purposes of Recovering Additional Costs of Pollution Control Facilities and to Amend Its Environmental Cost Recovery Surcharge Tariff, final Order dated September 7, 2005; and Case No. 2006-00307, The Application of Kentucky Power Company for Approval of an Amended Compliance Plan for Purposes of Recovering Additional Costs of Pollution Control Facilities and to Amend Its Environmental Cost Recovery Surcharge Tariff, final Order dated January 24, 2007.

⁴ Case No. 2005-00341, General Adjustments of Electric Rates of Kentucky Power Company, final Order dated March 14, 2006.

environmental surcharge as billed to consumers from (a) January 1, 2006 through June 30, 2006; (b) July 1, 2006 through December 31, 2006; and, (c) July 1, 2005 through June 30, 2007. At the public hearing there shall be no opening statements or summaries of testimony.

3. Kentucky Power shall, by the date set forth in Appendix A, file its prepared direct testimony in support of the reasonableness of the application of its environmental surcharge mechanism during the three periods under review.

4. Any party filing testimony shall file an original and 10 copies.

5. a. The information requested herein is due on or before October 24, 2007. Responses to requests for information shall be appropriately bound, tabbed and indexed and shall include the name of the witness responsible for responding to the questions related to the information provided, with copies to all parties of record and 7 copies to the Commission.

b. Each response shall be answered under oath or, for representatives of a public or private corporation or a partnership or association or a governmental agency, be accompanied by a signed certification of the preparer or person supervising the preparation of the response on behalf of the entity that the response is true and accurate to the best of that person's knowledge, information, and belief formed after a reasonable inquiry.

c. Any party shall make timely amendment to any prior responses if it obtains information which indicates that the response was incorrect when made or, though correct when made, is now incorrect in any material respect.

d. For any requests to which a party fails or refuses to furnish all or part of the requested information, that party shall provide a written explanation of the specific grounds for its failure to completely and precisely respond.

6. Within 7 days of the Commission granting intervention to a party, Kentucky Power shall provide the party with a copy of its monthly environmental surcharge reports as filed with the Commission for each review period.

7. Kentucky Power's monthly environmental surcharge reports and supporting data for the review periods shall be incorporated by reference into the record of this case.

8. The case records of Case Nos. 1996-00489, 2002-00169, 2004-00081, 2005-00068, 2005-00341, and 2006-00307 shall be incorporated by reference into the record of this case.

9. The Commission does not look favorably upon motions for continuance. Accordingly, motions for extensions of time with respect to the schedule herein shall be made *in writing and will be granted only upon a showing of good cause.*

10. Nothing contained herein shall prevent the Commission from entering further Orders in this matter.

Done at Frankfort, Kentucky, this 19th day of September, 2007.

By the Commission

ATTEST:


Executive Director

Case No. 2007-00381

APPENDIX A

APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE
COMMISSION IN CASE NO. 2007-00381 DATED September 19, 2007

Kentucky Power shall file its prepared direct testimony and responses to the information requested in Appendix B no later than..... 10/24/07

An informal technical conference is to begin at 10:00 a.m., Eastern Daylight Time, in Conference Room 1 of the Commission's offices at 211 Sower Boulevard, Frankfort, Kentucky for the discussion of issues..... 10/31/07

All additional requests for information to Kentucky Power shall be filed no later than..... 11/07/07

Kentucky Power shall file responses to additional requests for information no later than..... 11/21/07

Intervenor testimony, if any, in verified prepared form shall be filed no later than..... 12/07/07

All requests for information to Intervenors shall be filed no later than..... 12/21/07

Intervenors shall file responses to requests for information no later than..... 01/08/08

Public Hearing is to begin at 9:00 a.m., Eastern Standard Time, in Hearing Room 1 of the Commission's offices at 211 Sower Boulevard, Frankfort, Kentucky, for the purpose of cross-examination of witnesses of Kentucky Power and Intervenors..... To be scheduled

Briefs, if any, shall be filed by To be scheduled

APPENDIX B

APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE
COMMISSION IN CASE NO. 2007-00381 DATED September 19, 2007

DATA REQUEST TO
KENTUCKY POWER COMPANY

For Each of the Three Periods Under Review

1. Prepare a summary schedule showing the calculation of E(m) and the surcharge factor for the expense months covered by the applicable billing period. Use ES Form 1.00 as a model for this summary. Include the expense months for the two expense months subsequent to the billing period in order to show the over- and under-recovery adjustments for the months included for the billing period under review. Include a calculation of any additional over- or under-recovery amount Kentucky Power believes needs to be recognized for each 6-month review or 2-year review. Include all supporting calculations and documentation for any such additional over- or under-recovery. Kentucky Power's calculations should recognize the Commission's decision in Case No. 2006-00128¹ concerning the recovery of costs associated with surcharge reporting errors applicable to seven expense months that are included in the current review case.

2. The net gain or loss from sulfur dioxide ("SO₂") and nitrogen oxide ("NO_x") emission allowance sales are reported on ES Form 3.00, Calculation of Current Period

¹ Case No. 2006-00128, An Examination by the Public Service Commission of the Environmental Surcharge Mechanism of Kentucky Power Company for the Six-Month Billing Periods Ending December 31, 2002, December 31, 2003, June 30, 2004, December 31, 2004, and December 31, 2005, and for the Two-Year Billing Periods Ending June 30, 2003 and June 30, 2005.

Revenue Requirement, Third Component. For each expense month covered by the applicable billing period, provide an explanation of how the gain or loss reported in the expense month was calculated and describe the transaction(s) that was the source of the gain or loss.

3. Included in the environmental costs reported on ES Form 3.10, Costs Associated with Big Sandy, are property taxes. Explain the reason(s) for the fluctuations in the property taxes during the three review periods.

4. Refer to ES Form 3.13, the Operation and Maintenance Expense summary, Line 10, Equipment – Associated Maintenance Expenses. Explain the primary reason(s) for the fluctuations in these maintenance expenses during the 6 expense months that make up each of the three review periods.

Billing Period from January 1, 2006 through June 30, 2006

5. Refer to ES Form 3.11, SO₂ Emission Allowance Inventory, for the December 2005 expense month.

a. Describe the type of transaction reported as "Withdrawals – Intercompany Sales."

b. Explain how the sales price per allowance was determined for these sales.

6. Refer to ES Form 3.12, ECR and NO_x Emission Allowance Inventory, for the April 2006 expense month. Explain why Kentucky Power reported receiving "EPA Allowances" in this expense month.

Billing Period from July 1, 2006 through December 31, 2006

7. Refer to ES Form 3.12, ECR and NOx Emission Allowance Inventory, for the May 2006 expense month. Explain why Kentucky Power reported receiving "EPA Allowances" in this expense month.

8. Refer to ES Form 3.13, the Operation and Maintenance Expense summary, Line 9, Equipment – Associated Operating Expenses. Explain the primary reason(s) for the fluctuations in the operating expenses for each expense month in this review period.

Billing Period from July 1, 2005 through June 30, 2007

9. Refer to ES Form 3.11, SO₂ Emission Allowance Inventory, for the December 2006 expense month.

a. Describe the type of transaction reported as "Withdrawals – Intercompany Sales."

b. Explain how the sales price per allowance was determined for these sales.

10. In Case No. 1996-00489, the Commission ordered that Kentucky Power's rate of return on common equity for the environmental surcharge would be reviewed for reasonableness during the 2-year review case. In Case No. 2005-00341, the approved Settlement Agreement provided that Kentucky Power would utilize a 10.5 percent rate of return on common equity.

a. Does Kentucky Power believe that the 10.5 percent rate of return on common equity for the environmental surcharge is reasonable? Explain the response, and include any analyses or evaluations supporting its conclusions.

b. If no to part (a), what rate of return on common equity does Kentucky Power propose for its environmental surcharge? Provide a detailed analysis and testimony supporting Kentucky Power's position.

11. Provide the following information as of April 30, 2007:

a. The outstanding balances for long-term debt, short-term debt, accounts receivable financing, and common equity.

b. The blended interest rates for long-term debt, short-term debt, and accounts receivable financing. Include all supporting calculations showing how these blended interest rates were determined.

c. Kentucky Power's calculation of its weighted average cost of capital for environmental surcharge purposes.

12. KRS 278.183(3) provides that during the 2-year review, the Commission shall, to the extent appropriate, incorporate surcharge amounts found just and reasonable into the existing base rates of the utility. In Case No. 2005-00341, the approved Settlement Agreement provided that \$28,106,683 from the environmental surcharge was incorporated into Kentucky Power's base rates.

a. Does Kentucky Power believe any additional surcharge amounts need to be incorporated into its base rates in conjunction with this 2-year review?

b. If yes to part (a), provide the additional surcharge amount that Kentucky Power believes should be incorporated into its existing base rates. Explain how the surcharge amount should be incorporated into the base rates. Include all supporting calculations, workpapers, and assumptions as well as any analysis that Kentucky Power believes supports its position.