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August 22, 2007

HAND DELIVERED

Ms. Beth O'Donnell
Executive Director
Public Service Commission of Kentucky
211 Sower Boulevard
P.O. Box 615
Frankfort, Kentucky 40602-0615

RE: Legislation Working Group

Dear Ms. O'Donnell:

Kentucky Power Company nominates Mark R. Overstreet, Stites & Harbison PLLC, 421 West Main Street, P.O. Box 634, Frankfort, Kentucky 40602-0634 for membership on the Working Group to consider legislation making clear the Commission's express authority to approve surcharges and rate adjustments outside of base rate cases. Mr. Overstreet has more than 27 years experience practicing before the Commission and has represented electric, gas, water and telecommunications companies before the Commission.

Sincerely,

Errol K Wagner
Director Regulatory Services

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August 22, 2007

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HAND DELIVERED

Ms. Beth O'Donnell
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Public Service Commission of Kentucky
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RE: Surcharge Interim Options

Dear Ms. O'Donnell:

These comments are submitted on behalf of Kentucky Power Company. Kentucky Power appreciates the opportunity to provide the Commission with its recommendations regarding the Commission's course of action with respect to surcharges pending the outcome of all appeals in *Commonwealth ex rel. Stumbo v. Public Service Commission,* Civil Action 06-CI-00269 (Franklin Circuit Court August 1, 2007).

Kentucky Power strongly recommends the Commission maintain the status quo pending the resolution of all appeals by continuing to administer all Kentucky Power surcharges (and surcredits) in accordance with existing practice. This course accords the August 1, 2007 Opinion and Order of the Franklin Circuit Court its full legal effect and will avoid the adverse consequences to ratepayers and utilities that likely would result if the Commission abandoned or modified its current administration of surcharges and surcredits. Neither of the other two proposed interim options would yield these benefits.

A. The August 1, 2007 Opinion and Order and Its Legal Effect.

1. *Stumbo v. Public Service Commission*[1] Did Not Address The Validity Of Any Surcharge or Surcredit Other Than The Duke Energy AMRP.

The only surcharge before the Franklin Circuit Court in *Stumbo v. Public Service Commission* was Union, Light, Heat and Power Company's (n/k/a "Duke Energy") Accelerated Mains Replacement Program Rider ("AMRP Rider"). No other surcharge, including the Fuel Adjustment Clause, Kentucky Power's System Sales Tracker, Kentucky Power's Merger Credit Adjustment and Kentucky Power's Capacity Surcharge was before the court. Likewise, the only

[1] Civil Action 06-CI-00269 (Franklin Circuit Court August 1, 2007).

orders before the court were the Commission's orders granting Duke Energy the right to impose the surcharge and approving subsequent adjustments.

The limited nature of the Franklin Circuit Court's proceedings, and the scope of the August 1, 2007 Opinion and Order, is evident upon the face of the pleadings and the Court's August 1, 2007 Opinion and Order. For example, the Attorney General's complaint upon appeal in Civil Action No. 06-CI-00269 (in which the Opinion and Order was issued) provided in pertinent part:

> 1. This is an action brought pursuant to KRS 278.410 for review of orders of the defendant Public Service Commission of Kentucky ("Commission") in Case Number 2005-00042, *In the Matter of: An Adjustment of the Gas Rates of Union, Light, Heat and Power Company.*
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> ...
>
> 9. Union proposed a tariff, Rider AMRP, to recover the costs of its mains replacement program between rate cases that bears the same language as preceding Rider AMRP used by Union before the enactment of KRS 278.509.
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> ...
>
> 11. By Order dated December 22, 2005, a copy of which is attached as Exhibit A, the Commission authorized Union to place the tariff, Rider AMRP, on file and ruled it will allow Union to amend that tariff annually to recover the added costs of its main replacement program.
>
> **WHEREFORE**, the Commonwealth of Kentucky, ex rel. Gregory D. Stumbo, Attorney General, respectfully requests this Court to:
>
> A. Declare void *ab initio* and vacate the Commission's Orders of December 22, 2005, and February 2, 2006 [order denying rehearing], and restrain and enjoin the Commission from authorizing between rate case increases in the Rider AMRP or including a return on investment in the cost recovery under Rider AMRP....[2]

Thus, on its face, the Attorney General's appeal sought review only of the Commission's orders in cases involving a single utility – Duke Energy – and establishing and adjusting a single surcharge – the Rider AMRP.

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[2] Complaint, *Commonwealth ex rel. Stumbo v. Public Service Commission,* Civil Action 06-CI-00269 at 1, 2, 3, 4 (Franklin Circuit Court August 1, 2007).

The Franklin Circuit Court likewise limited its Opinion and Order. As the court initially explained "This action is before the Court for final resolution of the Attorney General's appeal of the final order of the Public Service Commission (PSC), allowing Union, Light, Heat and Power (Union) to adjust its rates to reflect pipeline replacement expenditures through an interim rate review, passing those costs on to its customers through a surcharge on its base rate."[3] In its conclusion, the court limited the relief granted:

> "Absent statutory authority for an interim review and surcharge, ***the cost of the AMRP*** must be considered in the context of a rate case.... Accordingly, ***the final administrative order of the Public Service Commission*** is REVERSED and ***this action*** is REMANDED to the Public Service Commission for further proceedings not inconsistent with this judgment."[4]

Thus, the court's order on its face is limited to the Rider AMRP. The only actions remanded to the Commission for further proceedings were the appeals by the Attorney General of the Commission's orders establishing and adjusting the Rider AMRP for Duke Energy. Nothing in the August 1, 2007 Opinion and Order affects any surcharge other than the Rider AMRP or any utility other than Duke Energy. Nor could it.

2. The Franklin Circuit Court's August 1, 2007 Order In *Stumbo v. Public Service Commission*[5] Could Affect Only The Duke Energy Rider AMRP.

A court has authority to decide only the issues squarely before it and even then only as to the parties to that action.[6] In *Matthews v. Ward*, for example, a declaratory judgment action was brought challenging a Highway Department regulation and contract granting transferring employees lump sum payments in lieu of actual relocation expenses. Premising its decision on the Commonwealth's inherent authority to pay such expenses, the circuit court determined the contract was proper.[7] On appeal, the Court noted that KRS 64.710, which had not been argued before the trial court, expressly prohibited lump sum payments. As a result, the Court held the

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[3] *Commonwealth ex rel. Stumbo v. Public Service Commission,* Civil Action 06-CI-00269 at 1 (Franklin Circuit Court August 1, 2007).

[4] *Id.* at 8. (emphasis supplied).

[5] Civil Action 06-CI-00269 (Franklin Circuit Court August 1, 2007).

[6] *Matthews v. Ward,* 350 S.W.2d 500, 501-502 (Ky. 1961); *Funk v. Milliken,* 317 S.W.2d 499, 513 (Ky. 1958).

[7] *Matthews,* 350 S.W.2d at 501.

contract was illegal.[8] Turning to the question of whether the Commonwealth had authority to make lump sum payments, the Court held that the Court lacked authority to decide that issue:

> The parties in their briefs debate the question of whether or not, as a general proposition, expenses of this character could properly be paid. It is not within the scope of our proper function to decide questions not in issue.... Our views concerning the general authority of the department with respect to the payment of employees' expenses would be no more than obiter dictum. The only real controversy (which KRS 418.020 requires) concerns a particular procedure painstakingly established by the Department.[9]

The importance of all affected parties being before the Court was addressed in *Funk*. There, county officials brought an action against their predecessors in office concerning the propriety of certain payments and fiscal practices. One of the issues raised by the plaintiffs in the trial court was whether excess fees collected by the sheriff were to be paid to the county or the county school system.[10] The trial court refused to decide the issue because the school board, which would have been affected by the decision, was not a party. On appeal, the Court affirmed, recognizing that a court should not decide an issue absent all directly affected parties being before it.[11]

Hand and glove with these two principles is the equally long-standing recognition that broad statements of general legal principles, such as the Franklin Circuit Court's statement "this Court finds the PSC may not allow a surcharge without specific statutory authorization,"[12] are not binding beyond the facts of the case in which they are made even where they form part of the legal basis for the holding of the case. The continuing viability of this principle was demonstrated by two recent United States Supreme Court decisions. In *Seminole Tribe of Florida v. Florida*,[13] the Supreme Court held that the Indian Commerce Clause did not empower Congress to abrogate the States' Eleventh Amendment immunity. In the course of its reasoning the Court broadly observed that "even when the Constitution vests in Congress complete lawmaking authority over a particular area, the Eleventh Amendment prevents Congressional

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[8] *Id.*

[9] *Id. See also, Funk*, 317 S.W.2d at 508 ("the question of whether the fiscal court could have paid it directly out of the county treasury was not in issue and should not have been adjudicated.")

[10] *Funk*, 317 S.W.2d at 513.

[11] *Id.*

[12] *Commonwealth ex rel. Stumbo v. Public Service Commission,* Civil Action 06-CI-00269 at 7 (Franklin Circuit Court August 1, 2007).

[13] 517 U.S. 44, 116 S.Ct. 1114, 134 L.Ed.2d 252 (1996).

authorization of suits by private parties against unconsenting States."[14] In fact, the Supreme Court continued in *Seminole Tribe* by making clear that the broad principle it announced was equally applicable to the enforcement of the bankruptcy laws – another area of exclusive federal jurisdiction – in actions against the States in federal courts.[15]

Ten years later, and directly contrary to the clear language of general principle set out in *Seminole Tribe*, the Supreme Court held in *Central Virginia Community College v. Katz*[16] that Congress had the authority under the Bankruptcy Clause of the Constitution to abrogate the States' immunity under the Eleventh Amendment with respect to adversary claims in bankruptcy. In so holding, the *Katz* Court recognized that its holding was inconsistent with both the broad principle relied upon by the majority in *Seminole Tribe* to support its holding, as well as the Court's further discussion concerning applicability of the principle to actions brought pursuant to the Bankruptcy Clause:

> We acknowledge that statements in both the majority and dissenting opinions in ... [*Seminole Tribe*] reflected an assumption that the holding in that case would apply to the Bankruptcy Clause.... For the reasons stated by Chief Justice Marshall in *Cohens v. Virginia*, 6 Wheat 264, 5 L.Ed. 257 (1821), we are not bound to follow our dicta in a prior case in which the point now at issue was not fully debated..... "It is a maxim not to be disregarded, ***that general expressions, in every opinion, are to be taken in connection with the case in which those expressions are used.*** If they go beyond the case, they may be respected, ***but ought not to control the judgment in the subsequent suit when the very point is presented for decision.***"

Id. (emphasis supplied). Kentucky follows *Cohens*.[17]

Each of the principles above is embodied in the Franklin Circuit Court's directions on remand "for further proceedings not inconsistent ***with this judgment.***[18] That is, remand was limited to proceedings consistent with the court's judgment and not its Order and Opinion. A judgment, by definition, is "a court's final determination of the rights and obligations of the

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[14] *Seminole Tribe*, 116 S.Ct. at 1131.

[15] *Id.* at 1131-1132 n.16.

[16] __ U.S. __, 126 S.Ct. 990, 996 (2006).

[17] *See, Louisville Water Company v. Weis*, 25 Ky. L. Rptr. 808, 76 S.W. 356 (1903) (quoting *Cohens*).

[18] *Commonwealth ex rel. Stumbo v. Public Service Commission,* Civil Action 06-CI-00269 at 8 (Franklin Circuit Court August 1, 2007) (emphasis supplied).

parties in a case."[19] Kentucky Power was not a party to the proceedings giving rise to the appeals and its rights and obligations were not, and could not be, determined in that case.

B. The Circuit Court In *Stumbo v. Public Service Commission*[20] Did Not Address The Commission's Express Statutory Authority[21] To Adjust Rates Outside The Confines Of A General Rate Case.

The Franklin Circuit Court's Opinion invalidating Duke Energy's AMRP nowhere squarely addresses the question of the Commission's express statutory authority to adjust rates outside the confines of a general rate case. Rather, its analysis of the Commission's authority is limited to the issue of whether Commission enjoys implicit authority to implement single item rate adjustments.[22] Thus, the court nowhere examines the language of the two statutes expressly granting the Commission general authority to adjust rates outside a general rate case. Indeed, its discussion of the Commission's authority to adjust rates outside a general rate case is entitled "Inherent Authority."[23]

Chapter 278 makes clear the Commission enjoys express authority to adjust rates; it nowhere limits that authority to a general rate case in which all revenues and costs are examined and all rates are subject to adjustment. Two statutes in particular bear on the issue.

First, KRS 278.180, which is entitled "Changes in Rates, How Made," expressly recognizes that individual rates can be adjusted:

> Except as provided in subsection (2) of this section, no change shall be made by any utility in ***any rate*** except upon thirty (30) days' notice to the commission....[24]

If the General Assembly had intended to limit the Commission to adjusting rates only in the context of a general rate case, KRS 278.180(1) would have provided "no change shall be made by any utility in any rate except *by means of a general rate case and* except upon thirty (30) days' notice to the commission...."

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[19] Black's Law Dictionary 846 (7th Ed. 1999).

[20] Civil Action 06-CI-00269 (Franklin Circuit Court August 1, 2007).

[21] Because express authority exists, Kentucky Power does not have an opinion on whether the Commission has the implicit authority to make such rate adjustments outside a general rate case.

[22] *Commonwealth ex rel. Stumbo v. Public Service Commission,* Civil Action 06-CI-00269 at 5-8 (Franklin Circuit Court August 1, 2007).

[23] *Id.* at 5.

[24] KRS 278.180(1) (emphasis supplied).

Second, KRS 278.190, which prescribes the procedure by which the Commission may review a proposed change in a rate, provides:

> (2) Pending the hearing and decision thereon, and after notice to the utility, the commission may ... defer the use of ***the rate, charge, classification, or service*** ....
>
> (3) At any hearing involving ***the rate or charge*** to be increased....[25]

The General Assembly's use of the phrases "the rate, charge" and "the rate or charge" again expressly provides for the adjustment of a single rate.

These express grants of authority to adjust "any rate" or "the rate or charge" stand in contrast to the absence of any language expressly limiting a utility to adjusting its rates only in a general rate case in which all revenues and expenses are examined and all rates are subject to change. In the absence of an ambiguity, neither the Commission nor the courts may add to or subtract from the language employed by the General Assembly in enacting statutes.[26] That is, the reach of a statute must be determined from "the words used in enacting statutes rather than surmising what may have been intended but was not expressed.'"[27] Nothing in KRS 278.180 or KRS 278.190 limits their provisions to general rate cases. Indeed, only by impermissibly reading such limitations into the statutes can they be so construed.

By contrast, the General Assembly clearly was aware of the concept of a general increase in rates and knew how to use the phrase when that is what it intended. For example, KRS 278.192(1) prescribes the types of test years a utility may use in seeking to justify "the reasonableness of a ***general increase*** in rates...."[28] There would have been no need for the General Assembly to employ the adjective "general" in front of "increase in rates" in KRS 278.192 if the Commission's authority under KRS 278.180 and KRS 278.190 was limited to general rate cases.[29]

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[25] KRS 278.190(2), (3) (emphasis supplied). Kentucky Power recognizes that other portions of the statute use the terms "rates" and "charges." The General Assembly apparently did so in those parts of the statute in the context of the specific syntax employed so as to ensure the statute applied to any and all rates changes. By contrast, if the General Assembly had intended to limit rates changes to general rate cases the syntax never would have required the use of "the rate or charge."

[26] *Posey v. Powell*, 965 S.W.2d 836, 838 (Ky. App. 1998).

[27] *Stopher v. Conliffe*, 170 S.W.3d 307, 309 (Ky. 2005).

[28] (Emphasis supplied.)

[29] *Stopher*, 170 S.W.3d at 309 (General Assembly's use of the adjective "defending" in front of attorney was required to be given effect and was intended to indicate legal counsel during a distinct stage of criminal proceedings.)

The Commission was granted express statutory authority in KRS 278.180 and KRS 278.190 to adjust rates outside the confines of a general rate case. The Commission should not, and in fact can not, abandon that authority absent statutory direction from the General Assembly or until there is a final and non-appealable decision of a court of competent jurisdiction holding that no such express statutory authority exists.

C. Current Kentucky Power Surcharges and Surcredits.

For the reasons set forth above and others, and because Kentucky Power's rates may not be changed absent a full evidentiary hearing, none of Kentucky Power's surcharges and surcredits are implicated by the August 1, 2007 Opinion and Order. To assist the Commission with its information gathering, however, the table below sets outs the Company's current surcharges and surcredits:

Name of Surcharge/Credit	Effective Date	Case Number	12 Mos. Total Revenue	Percent of Annual Revenue
Fuel Adjustment Clause[30]	Nov. 1, 1978	Case No. 7213	$24,350,352	6.07%
System Sales Clause	Oct.28, 1988	Case No. 9061	($14,779,150)	(3.67%)
Net Merger Savings Credit	June. 14, 1999	Case No. 99-149	($4,375,705)	(1.09%)
Rockport Capacity Charge	Dec. 13, 2004	Case No. 2004-00420	$5,000,000	1.25%

[30] Prior to the implementation of the Fuel Adjustment Clause, the Commission authorized Kentucky Power to employ similar surcharges to recover the costs of its fuel:

Name of Surcharge/Credit	Effective Date	Case Number
Coal Clause	Nov. 10 1937	Order No. 22
Fuel Clause	Oct. 1, 1959	

D. Limiting Rate Adjustments To General Rate Cases Would Adversely Affect Ratepayers and Utilities.

Kentucky Power has not completed its analysis of the possible effects of a change in the current statutory framework that would require all jurisdictional utilities to adjust their charges only through a general rate case. Nevertheless, based upon the information currently available to it, Kentucky Power believes the following consequences are likely:

- Utilities would be required to file more frequent cases. For example, in part because of the availability of the fuel adjustment clause, Kentucky Power was able to avoid filing a case seeking an increase in base rates between 1984 and 2005. Without the ability to recover increases in fuel costs outside a general rate case, utilities may be required to file for general increases in rates every 12 to 18 months. Rate case costs are not insubstantial. For example, the costs associated with Kentucky Power's 2005 rate case, which currently are being recovered in Kentucky Power's rates, were approximately $430,700. Moreover, more frequent rate cases undoubtedly would result in increased demands on Commission resources and hence significantly increased Commission assessments to utilities. Both of these types of increased costs would be directly passed on to ratepayers through amortization of rate case expenses and through the utilities' recovery of the Commission's assessments in their rates.

- Although Kentucky Power has not undertaken the type of detailed study that might be required to definitively resolve the question, it expects that the loss by electric utilities of the ability to recover changes in their single largest variable cost on a timely basis will make electric utilities less attractive to the capital markets, thereby increasing their cost of money. Such an increase will be reflected in higher base rates.

E. Any Legislative Initiatives Should Await The Resolution of The Pending Appeal In *Stumbo v. Public Service Commission.*[31]

At the August 16, 2007 meeting Commission Staff, as well as the Attorney General, raised the question of whether Chapter 278 should be amended to grant the Commission the express authority to adjust rates and provide for surcharges outside a general rate case. In light of the unambiguous existing grant of statutory authority to the Commission to do just that, Kentucky Power believes that any such entreaty to the General Assembly would be premature. Rather, the Commission at a minimum should await a final resolution of its appeal of the August 1, 2007 Opinion and Order. Indeed, any such attempt, even if successful, might be misconstrued by a court as indicating that the Commission currently lacks the express statutory authority to adjust rates outside general rate cases.

[31] Civil Action 06-CI-00269 (Franklin Circuit Court August 1, 2007).

Kentucky Power appreciates the opportunity to provide the Commission with these comments.

Very truly yours,

Mark R. Overstreet

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