

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

THE APPLICATION OF KENTUCKY UTILITIES)
COMPANY TO ASSESS A SURCHARGE UNDER KRS)
278.183 TO RECOVER COSTS OF COMPLIANCE) CASE NO. 93-465
WITH ENVIRONMENTAL REQUIREMENTS FOR COAL)
COMBUSTION WASTES AND BY-PRODUCTS)

O R D E R

On July 25, 1994, the Kentucky Industrial Utility Customers ("KIUC") filed an application requesting rehearing of the Commission's July 19, 1994 Order approving an environmental surcharge tariff for Kentucky Utilities Company ("KU"). KIUC raises three issues in support of its request for rehearing.

First, KIUC seeks clarification of the discussion in the Commission's July 19, 1994 Order, at pages 12-13, of KU's need to maintain a cumulative environmental rate base between general rate cases which will reflect KU's current level of environmental surcharge costs less those incorporated into base rates every two years. KIUC questions whether this procedure was established to address its concern that absent a tracking of the depreciation included in existing rates, KU's environmental surcharge might allow it to over-earn between rate cases. KIUC also questions whether adjustments to reflect growth in sales or changes in cost of capital are to be reflected in future surcharges subsequent to KU's next rate case. In addition, KIUC urges the Commission to clarify whether it intends to prevent KU from prospectively over-

earning under the surcharge and, if so, to require sufficient information to be maintained to analyze KU's earnings.

Second, KIUC requests modification of the Commission's Order to require KU to include as a credit in the first month of the surcharge the revenues received from the sale of admission allowances in the 1994 Environmental Protection Agency ("EPA") Auction. This treatment would mirror the Commission's directive that the revenues from EPA's 1993 Auction be credited to ratepayers in the first month of the surcharge.

Third, KIUC takes issue with the Commission's decision in granting KU almost all of the environmental surcharge revenues requested and suggests that the Commission should have adopted a variation of KIUC's approach for determining which environmental costs are not included in existing rates. KIUC argues that this alternative approach was endorsed by KU and should have been adopted by the Commission as a compromise approach.

The Commission, having considered KIUC's request for rehearing, KU's response in opposition and being otherwise sufficiently advised, hereby finds that rehearing should be denied. The first issue raised by KIUC requires no clarification. The July 19, 1994 Order expressly states that KU must maintain a cumulative environmental rate base with appropriate credits for accumulated depreciation. When surcharge revenues are rolled into base rates at two year intervals, KU's cumulative environmental rate base will reflect the amounts incorporated into base rates. This approach will allow for the tracking of depreciation on the environmental

costs not already included in existing rates and prevent KU from over-earning through the surcharge on these environmental costs.

Contrary to KIUC's assertion, the environmental surcharge will provide no opportunity for KU to over-earn on the environmental costs not already included in its existing rates. In addition to the tracking of the depreciation associated with the projects included in the environmental rate base, any change in the level of KU's sales will be reflected in the denominator of the surcharge calculation. Also, any over- or under-earnings in a particular month will be reflected in the tariff's balancing account. Such amounts will then be collected or refunded in the following month. KIUC has not specified any data that needs to be filed to supplement what KU is already required to file on either a monthly, semi-annual, or bi-annual basis.

KRS 278.183(2)(b) directs the Commission to establish a reasonable return on KU's compliance-related capital expenditures. KU proposed and the Commission accepted a return of 5.85 percent, the actual cost of KU's most recent pollution control bond issue. The environmental surcharge tariff approved for KU is a formula which includes as one component the return on compliance-related capital expenditures. Should evidence be presented in the future to persuade the Commission that this return needs to be changed, such change will automatically be reflected in subsequent calculations of the surcharge through the formula.

No evidence was offered to challenge the appropriateness of the 15 environmental compliance projects KU proposed for inclusion

in its surcharge or the level of costs associated with such projects. Rather, KIUC and others challenged KU's approach for determining whether its environmental costs are not already included in existing rates. The environmental surcharge will allow KU to recover on a dollar-for-dollar basis the costs associated with its 15 environmental projects. To the extent that KIUC is concerned that KU may be over-earning through its base rates which were established over a decade ago, the July 19, 1994 Order discusses the remedy available to KIUC under KRS 278.260.

The request for modification to reflect EPA's 1994 auction is now moot. KU has filed the documentation supporting its August 1994 monthly surcharge. This information demonstrates that KU has treated the revenues from EPA's 1994 Auction as a credit to ratepayers as KIUC has suggested.

Finally, the criticism that the allowed level of environmental surcharge constitutes excessive generosity is unwarranted. There is no evidence that any of the 15 projects are unreasonable, unnecessary or excessive. Absence such evidence, the approval of KU's environmental surcharge is mandated by KRS 278.183. The implication of KIUC's argument is that the Commission should reduce KU's environmental surcharge solely to prevent it from recovering substantially all of its legitimate costs. Such a reduction would result in arbitrary and capricious administrative action.

Simply because the Commission found two differing methodologies reasonable does not constitute a basis for selecting a compromise alternative. KIUC has quoted KU's argument out of

context, implying that KU supported a compromise alternative to determine its environmental surcharge. This compromise was an alternative to KIUC's proposal, not KU's. KIUC has conveniently ignored those portions of KU's argument explaining that this compromise would deny KU recovery of a substantial portion of environmental costs not in existing rates. KU's argument clearly stated that its proposed incremental methodology is the most reasonable and should be approved by the Commission.

IT IS THEREFORE ORDERED that KIUC's application for rehearing be and it hereby is denied.

Done at Frankfort, Kentucky, this 15th day of August, 1994.

PUBLIC SERVICE COMMISSION


Chairman


Vice Chairman


Commissioner

ATTEST:


Executive Director