COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

AN INVESTIGATION OF ELECTRIC RATES OF LOUISVILLE GAS AND ELECTRIC COMPANY TO IMPLEMENT A 25 PERCENT DISALLOWANCE OF TRIMBLE COUNTY UNIT NO. 1	))))	CASE NO. 10320

O R D E R

In accordance with a procedural order entered after an informal conference, Louisville Gas and Electric Company ("LG&E") filed a motion in limine ("LG&E Motion") on January 25, 1995. The Attorney General, Jefferson County, and Metro Human Needs Alliance (jointly referred to as "Intervenors") filed a joint response on February 28, 1995. The Kentucky Industrial Utility Customers ("KIUC") responded on the same date. LG&E filed its reply on March 7, 1995.

LG&E seeks to have the Commission limit the testimony to be presented at the public hearing in this matter scheduled to begin May 9, 1995. The testimony to which it objects is detailed in Appendix A to its motion but is more generally described in the motion as certain prefiled testimony of intervenor witnesses Baudino, DeWard, Kinloch, and Krieger to the affect that "LG&E must refund revenues collected for services rendered between June 1, 1979 and May 19, 1988." LG&E Motion, at 6.

The motion raises the same basic issues which were addressed by the Commission in its Order dated July 8, 1994, in response to the Attorney General's motion to recuse Commissioners. In that

order, the Commission concluded that no sitting Commissioner had exhibited any prejudice by relying on previous decisions of the Commission in this matter which had not been reversed by an appellate court. In fact, the Commission noted that it was obligated to comply with those previous decisions. LG&E's motion seeks to exclude testimony which addresses issues decided in those prior cases.

The intervenors in turn argue that the testimony is proper. They rely on a phrase in the opinion of the Court of Appeals which reversed Franklin Circuit Court and remanded the instant case to the Commission. The Court of Appeals sent the case back for "a new hearing on all of the issues." Louisville Gas and Electric Co. v. Com. ex rel. Cowan, Ky.App., 862 S.W.2d 897 (1993), at p. 902. The issue before the Commission is whether in using the phrase, 'all of the issues,' the Court of Appeals meant all of the issues before the Commission in Case No. 10320, as argued by LG&E, or to all of the issues relating to cash return on construction work in progress (CWIP) since the construction of LG&E's Trimble County plant began in the late 1970's, as argued by the Intervenors. It is the opinion of the Commission that the Court of Appeals could only have meant that the hearing be held on all of the issues before the Commission in Case No. 10320 because only the issues in Case No. 10320 were before the Court of Appeals.

The Commission set forth the history of this proceeding and various orders which are binding upon it and the courts in its July 8, 1994, Order addressing the Attorney General's recusal motion.

The Sturm und Drang of the intervenors' response to LG&E's motion notwithstanding, these orders have imposed rates which have been collected. It is impossible to argue with any form of logical consistency that an attempt to change them is anything other than retroactive ratemaking. In fact, the intervenors do not even attempt such an argument. Rather, they argue that there are various exceptions to the rule where retroactive ratemaking is permissible, despite the rule against it.

The parties agree that the rule against retroactive ratemaking "... prohibits a utility commission from making a retroactive inquiry to determine whether a prior rate was reasonable and imposing a surcharge when rates were too low or a refund when rates were too high." State v. Public Utility Comm'n of Texas, 883 S.W.2d 190, 199 (Tex. 1994). The parties agree on little else.

The first case cited by the intervenors under the heading of "'Permissible' Retroactive Ratemaking" is Washington Gas Light Co. v. Public Service Com'n of District of Columbia, 450 A.2d 1187 (D.C. App. 1982). They conclude from this case that the District of Columbia Public Service Commission engaged in permissible retroactive ratemaking when it ordered future amortization of gains from the repurchase of outstanding bonds. The Commission noted, however, that it was,

> "... very careful not to indulge in retroactive ratemaking. The Commission's decision does not deprive stockholders of any past gains to which they were entitled prior to our decision in this case. They are permitted to keep all those gains which would have been amortized prior to the test year had the Commission instituted a policy of

> passing on the gains to the customers at the time the gains were realized. The customers get only the remaining pro forma unamortized gains which fall within the test period and in successive years. Under these circumstances, we do not think that is can be fairly said that we have engaged in retroactive ratemaking."

Id. at 1217, quoting District of Columbia Public Service Commission Order 6060 dated March 16, 1979. The appellate court apparently agreed and concluded that the Commission had not indulged in illegal retroactive ratemaking. Id. at 1219.

This is a conclusion with which this Commission concurs. In the cited case, no preexisting rate was changed. No refunds were ordered. The effects of an accounting change were implemented for rates established for the future.

The intervenors correctly note that similar reasoning was used in Southern Union Gas Company v. Railroad Commission of Texas, 701 S.W.2d 277 (Tex. App. 1985). There, the court concluded that a similar future treatment of an investment tax credit "... does not constitute retroactive ratemaking." Id. at 280. Rather than supporting the intervenors' position that retroactive ratemaking is "permissible" in the instant case, these cases hold that prospectively applied changes in accounting policy do not constitute retroactive ratemaking in the first place.

The intervenors next seek support in the case of Mike Little Gas Co. v. Public Serv. Com., Ky.App., 574 S.W.2d 926 (1978). That case however, stands for the rather unremarkable proposition that the Commission, other administrative agencies, and the courts have authority to issue nunc pro tunc orders to correct obvious clerical

errors. How this holding can be construed to authorize the refund of rates lawfully collected under orders which were either not appealed or which were affirmed on appeal is not immediately or later apparent.

The applicability of Building Owners and Managers Association of Metropolitan Detroit v. Public Service Commission, 424 Mich. 494, 383 N.W.2d 72 (1986) is equally obscure. The primary holding of the case is that failure to give proper notice of a hearing did not deprive the Michigan Public Service Commission of jurisdiction or render rates, subsequently found fair, just, and reasonable, void ab initio. The court gave the issue of retroactive ratemaking scant treatment. It noted that,

> A rate was set and a subsequent hearing supplied the necessary finding of reasonableness after proper notice to the ratepayer. The rate was not changed after the fact, but found to be reasonable by a subsequent determination. Contrary to [a case cited by intervenors], where we prohibited a refund to ratepayers ordered by the Public Service Commission from rates in effect prior to the order, the 1977 order [which was the subject of the appeal] contained exactly the same rate as the initial order in this case.

Id. at 80-81. If this case may be cited as authority by either side in this proceeding, it would appear to support LG&E's contention that this Commission is prohibited from ordering a refund to ratepayers from rates in effect in a prior order.

The intervenors next cite three cases which each hold that extraordinary, one-time expenses may be recovered without violating the prohibition against retroactive ratemaking. The first is Narragansett Electric Company v. Burke, 415 A.2d 177 (R.I. 1980).

In that case, the Rhode Island Supreme Court overturned an order by that state's public utilities commission which refused a temporary rate increase to allow Narragansett to recover the costs it incurred to restore service after a freakish ice storm. Intervenors correctly note the court's comment that, "no rule should be blindly applied. . . ." Id. at 178. The court went on to say that the rule ". . .protects the public by ensuring that present consumers will not be required to pay for past deficits of the company in their future payments" and ". . . prevents the company from employing future rates as a means of ensuring the investments of its stockholders." Id. at 179. The court further noted that the utility's existing rates were "'not in any fashion [based on] the extraordinary expenses of restoration of service after the ice storm.'" Id., quoting the order from which the appeal was taken. In concluding its opinion, the court pointed out that,

> The plethora of cases from other jurisdictions permitting a utility to recover the extraordinary costs associated with an unusually severe storm indicate that the rule against retroactive ratemaking does not come into play in such instances.

Id., (Citations omitted).

The situation presented in Narragansett is clearly distinguishable from the instant case. The court went out of its way to emphasize that the exception should not swallow the rule. The event in Narragansett was unpredictable. The freakish storm was not something for which the utility could plan, nor could it seek recovery prior to the event.

The issues of LG&E's continuing need for Trimble County and recovery of construction financing costs were discussed for several years before this case was initiated. Trimble County Unit No. 2 was cancelled by LG&E on its own initiative in the early 1980's, and completion of Unit No. 1 was recognized by the Commission to be the "primary issue" when it initiated Case No. 9243[1] in 1985. Thus, LG&E's rates prior to the instant case were established with Trimble County very much at the center of discussion.

In short, the holding of Narragansett is inapposite. The same may be said of the holding of the Iowa Supreme Court concerning recovery of one-time nuclear waste disposal costs assessed under the Nuclear Waste Policy Act of 1992, 42 U.S.C.§10101-10226 (1982), see Office of Consumer Advocate v. Iowa State Commerce Commission, 428 N.W.2d 302 (Iowa 1988), and of the holding of the Rhode Island Supreme Court which allowed recovery of a one-time tax surcharge imposed by the City of Providence. See Providence Gas Company v. Burke, 475 A.2d 193 (R.I. 1984).

After discussing one-time expenses, the intervenors turn their attention to four cases where utilities experienced unusual gains. They indicate that the case of Chesapeake and Potomac Telephone Company v. Public Service Com'n of District of Columbia, 514 A.2d 1159 (D.C. App. 1986), is "...exactly cogent to the instant case." Intervenor's Response at 32. However, there is a very basic

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[1] Case No. 9243, An Investigation and Review of Louisville Gas and Electric Company's Capacity Expansion Study and the Need for Trimble County Unit No. 1, Order dated October 14, 1985, p. 3.

distinction between the facts in the instant case and the facts of Chesapeake Telephone, a distinction which led the court to conclude that there was no retroactive ratemaking involved there. Chesapeake Telephone at 1170. In that case, the utility was not being ordered to refund moneys collected for its own use. Rather, it was ordered to refund revenues it collected and paid to AT&T, and which AT&T was subsequently ordered to refund by the Federal Communications Commission. As the court noted, "C & P was merely a conduit through which the funds passed from the ratepayers to AmBell." Id. As a result, the court concluded that, "[s]ince C & P never had any right to the money in the first place, it cannot complain that the Commission, following the lead of the FCC, gave it back to the ratepayers." Id., footnote omitted.

In the instant case, on the other hand, the intervenors seek refunds of moneys collected by LG&E through its lawfully approved rates which covered a portion of its cost to finance the construction of Trimble County. Under our prior rate orders, LG&E had every right to collect and retain its approved rates for service rendered. Therefore, Chesapeake Telephone is neither controlling nor instructive in the instant case. The same may be said of Turpen v. Oklahoma Corporation Commission, 769 P.2d 1309 (Okla. 1988), which considered the same AT&T reimbursement an "unexpected windfall" when considering the same issue from the opposite procedural stance. Id. at 1332.

Pike County Light and Power Company v. Pennsylvania Public Utility Commission, 87 Pa.Cmwlth. 451, 487 A.2d 118 (1985), and

Richter v. Florida Power Corporation, 366 So.2d 798 (Fla. App. 1979) are also cited under this heading. However, Pike County appears more closely aligned with the Washington Gas Light and Southern Union cases, supra, as it holds that amortizing past tax losses against tax expenses in determining a future rate does not constitute retroactive ratemaking.

The Florida Power case deals with Florida's fuel adjustment clause. In it, the Florida Court of Appeals concluded that Florida's public service commission had the authority to consider adjustment of excessive fuel costs which were the result of an allegedly illegal scheme. Fuel clauses by their very terms allow utilities to collect their fuel costs as incurred without the requirement of filing a formal rate proceeding. In turn, most such clauses, like Kentucky's, provide for review of the costs at a later date. They are therefore outside the normal operation of the rule against retroactive ratemaking. To the extent that the rule does apply after final commission review of the charges, the exception identified by the Florida court which would allow the Florida commission to deal with an illegal scheme to charge excessive fuel charges has no application to the instant case.

Perhaps the most intriguing case cited by the intervenors to support their position is Attorney General v. Department of Public Utilities, 455 N.E.2d 414 (Mass. 1983). It is correctly cited for the proposition that, "[t]he utility was entitled to recover its costs associated with the cancellation of a nuclear power plant ... and the court ruled that this was not an example of

retroactive ratemaking." Intervenor's Response at 32-33. The case dealt with the aftermath of a decision by Boston Edison Company to cancel its Pilgrim II nuclear generator. Contrary to longstanding practice for LG&E,

> Rate regulatory practices in the Commonwealth [of Massachusetts] required Edison to exclude the costs of Pilgrim II from its rate structure during the construction process. By these practices, capitalized costs -- costs of construction work in progress (CWIP) and the cost of financing the construction, allowance for funds used during construction (AFUDC) -- are not recoverable from ratepayers until the project is completed.

Attorney General, at p. 420. Yet, this case holds that Edison may recover various costs of the abandoned plant, which never produced electricity, in its future rates. In effect, the Massachusetts court affirmed a decision to allow Edison to recover, after abandonment, costs similar to those the intervenors ask this Commission to require LG&E to disgorge.

The reliance the intervenors place on In Re Commonwealth Edison Co., 103 PUR 4th 80 (Ill. Comm. Comm'n. 1989), aff'd sub nom. Business and Professional People for the Public Interest v. Illinois Commerce Commission, 563 N.E.2d 877 (Ill. 1990) is difficult to fathom. Nowhere in the order of the commission or in the opinion of the court affirming it is a refund mentioned. In fact, neither opinion deals with ratemaking and both refute the contention that allowing a special accounting treatment between a plant's in-service date and subsequent inclusion in ratebase is in any way retroactive ratemaking. Rather, both indicate that the

treatment allowed will be reviewed in a future ratemaking proceeding.

Finally, the intervenors cite the case of Mountain States Telephone & Telegraph Company v. Arizona Corporation Commission, 124 Ariz. 433, 604 P.2d 1144 (Ariz. App. 1979). However, the doctrine of equitable restitution is of no assistance to them. It rests in Mountain States, as it does in Justice Cardozo's opinion in Atlantic Coast Line Railroad Co. v. Florida, 295 U.S. 301 (1935), on the premise that the rate order from which the refund is sought has been held invalid. As has been noted before, the rate orders authorizing the recovery of costs relating to Trimble County have never been held by any court in this Commonwealth to be invalid. The only rate order held invalid was the one determining the amount of rates, collected subject to refund, which should be refunded.

It remains the firm conviction of the Commission that its prior orders in Cases 7301,[2] 7799,[3] 8284,[4] 8924,[5] 9243, 9934,[6] and

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[2] Case No. 7301, General Adjustments in Electric and Gas Rates of Louisville Gas and Electric Company.

[3] Case No. 7799, General Adjustments in Electric and Gas Rates of Louisville Gas and Electric Company.

[4] Case No. 8284, General Adjustments in Electric and Gas Rates of Louisville Gas and Electric Company.

[5] Case No. 8924, General Adjustment in Electric and Gas Rates of Louisville Gas and Electric Company.

[6] Case No. 9934, A Formal Review of the Current Status of Trimble County Unit No. 1.

10064[7] concerning Trimble County are binding upon it and all parties to them and may be relied upon by one and all. Nothing in the various cases cited by the intervenors compels a different conclusion. They have been discussed in considerable detail in this order, as was the procedural history of these proceedings in the order denying the Attorney General's motion to recuse, in an effort to assure the intervenors that every consideration has been given to the authorities they cite and the position they espouse.

LG&E's motion in limine should be granted. As part of its motion, LG&E suggests the possibility of presenting the excluded testimony by means of avowal. As KIUC suggests in its response, this remedy is "at one and the same time, too much and not enough." If the Commission's interpretation of the Court of Appeals opinion and the case law surrounding the rule against retroactive ratemaking is incorrect, it seems exceedingly unlikely that accepting on avowal testimony which is to be excluded would avoid the necessity of yet another hearing in this matter.

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[7] Case No. 10064, Adjustment of Gas and Electric Rates of Louisville Gas and Electric Company.

IT IS THEREFORE ORDERED the motion in limine of LG&E is granted and the testimony identified in Appendix A to its motion shall be excluded from the hearing in this matter.

Done at Frankfort, Kentucky, this 21st day of April, 1995.

PUBLIC SERVICE COMMISSION

Chairman

Vice Chairman

Commissioner

ATTEST:

Executive Director