

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)	
UTILITIES COMPANY FOR THE SIX-MONTH)	CASE NO.
BILLING PERIOD ENDING OCTOBER 31, 2006)	2007-00379
AND FOR THE TWO-YEAR BILLING PERIOD)	
ENDING APRIL 30, 2007)	

O R D E R

On July 19, 1994, the Commission approved Kentucky Utilities Company's ("KU") 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 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. 1993-00465, The Application of Kentucky Utilities Company to Assess a Surcharge Under KRS 278.183 to Recover Costs of Compliance with Environmental Requirements for Coal Combustion Wastes and By-Products, final Order dated July 19, 1994.

The Commission has determined that it will be administratively efficient and reasonable to review the pending 6-month period and the 2-year period in the same case. Therefore, the Commission hereby initiates the 6-month review of the surcharge as billed from May 1, 2006 to October 31, 2006 and the 2-year review of the surcharge as billed from May 1, 2005 to April 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, KU 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, KU 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, KU has sought and been granted four amendments to its original

² Since KU's surcharge is billed on a two-month lag, the amounts billed from May 2006 through October 2006 are based on costs incurred from March 2006 through August 2006 and amounts billed from May 2005 through April 2007 are based on costs incurred from March 2005 through February 2007.

environmental compliance plan and surcharge mechanism.³ In Case No. 2003-00068,⁴ KU's surcharge mechanism was changed from the incremental approach to the base-current approach and a portion of the environmental surcharge was incorporated, or "rolled-in," to existing base rates. In Case Nos. 2003-00434 and 2006-00129,⁵ the capital expenditures and operating expenses associated with the original environmental compliance plan were rolled-in to KU's base rates. After this last roll-in, the environmental surcharge provides recovery of the costs associated with the four amended environmental compliance plans. When determining its over- or under-

³ See Case No. 2000-00439, The Application of Kentucky Utilities Company 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 Surcharge Tariff, final Order dated April 18, 2001; Case No. 2002-00146, The Application of Kentucky Utilities Company for Approval of Its 2002 Compliance Plan for Recovery by Environmental Surcharge, final Order dated February 11, 2003; Case No. 2004-00426, The Application of Kentucky Utilities Company for a Certificate of Public Convenience and Necessity to Construct Flue Gas Desulfurization Systems and Approval of Its 2004 Compliance Plan for Recovery by Environmental Surcharge, final Order dated June 20, 2005; and Case No. 2006-00206, The Application of Kentucky Utilities Company for a Certificate of Public Convenience and Necessity to Construct a Selective Catalytic Reduction system and Approval of Its 2006 Compliance Plan for Recovery by Environmental Surcharge, final Order dated December 21, 2006.

⁴ Case No. 2003-00068, An Examination by the Public Service Commission of the Environmental Surcharge Mechanism of Kentucky Utilities Company for the Six-Month Billing Periods Ending January 31, 2001, July 31, 2001, January 31, 2002, and January 31, 2003 and for the Two-Year Billing Periods Ending July 31, 2000 and July 31, 2002, final Order dated October 17, 2003.

⁵ Case No. 2003-00434, An Adjustment of the Electric Rates, Terms, and Conditions of Kentucky Utilities Company, final Order dated June 30, 2004 and Case No. 2006-00129, An Examination by the Public Service Commission of the Environmental Surcharge Mechanism of Kentucky Utilities Company for the Six-Month Billing Periods Ending July 31, 2003, January 31, 2004, January 31, 2005, July 31, 2005, and January 31, 2006 and for the Two-Year Billing Period Ending July 31, 2004, final Order dated January 31, 2007.

recovery of the surcharge in this proceeding, KU 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. KU 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 environmental surcharge as billed to consumers from (a) May 1, 2006 through October 31, 2006 and (b) May 1, 2005 through April 30, 2007. At the public hearing there shall be no opening statements or summaries of testimony.

3. KU 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 two 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 17, 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, KU shall provide the party with a copy of its monthly environmental surcharge reports as filed with the Commission for each review period.

7. KU'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. 1993-00465, 2000-00439, 2002-00146, 2003-00068, 2003-00434, 2004-00426, and 2006-00206 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

Commissioner Clark Abstains

ATTEST:


Executive Director

APPENDIX A

APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE
COMMISSION IN CASE NO. 2007-00379 DATED September 19, 2007

- KU shall file its prepared direct testimony and responses to the information requested in Appendix B no later than 10/17/07
- An informal technical conference is to begin at 1:30 p.m., Eastern Daylight Time, in Conference Room No. 1 of the Commission's offices at 211 Sower Boulevard, Frankfort, Kentucky for the discussion of issues 10/24/07
- All additional requests for information to KU shall be filed no later than..... 10/31/07
- KU shall file responses to additional requests for information no later than..... 11/14/07
- Intervenor testimony, if any, in verified prepared form shall be filed no later than 11/30/07
- All requests for information to Intervenors shall be filed no later than..... 12/14/07
- Intervenors shall file responses to requests for information no later than..... 01/04/08
- Last day for KU to publish notice of hearing date To be scheduled
- 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 KU 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. 2007-00379 DATED September 19, 2007

DATA REQUEST TO KENTUCKY UTILITIES COMPANY

For Each of the Six Periods Under Review

1. Concerning the rate of return on the original environmental compliance plan ("1994 Plan") and the four amendments to the environmental compliance plan ("Post-1994 Plans"), provide the following information for each of the billing periods under review:

a. For the 1994 Plan, calculate any true-up adjustment needed to recognize changes in the weighted average cost of KU's pollution control debt during the applicable months of each review period. Include all assumptions and other supporting documentation used to make this calculation. Any true-up adjustment is to be included in the determination of the over- or under-recovery of the surcharge for the corresponding billing period under review.

b. For the Post-1994 Plans, calculate any true-up adjustment needed to recognize changes in KU's cost of debt, preferred stock, accounts receivable financing (if applicable), or changes in KU's jurisdictional capital structure. Include all assumptions and other supporting documentation used to make this calculation. Any true-up adjustment is to be included in the determination of the over- or under-recovery of the surcharge for the corresponding billing period under review.

2. Consistent with the Commission's Order in Case No. 2004-00426, for each applicable billing period under review, calculate the effect of removing from the reported inventory of emission allowances included in the environmental compliance rate base the sulfur dioxide ("SO₂") emission allowances assigned or allocated to gas-fired generating units. Include all assumptions and other supporting documentation used to make this calculation. In addition, include this calculation as an adjustment to the over- or under-recovery of the surcharge determined for the corresponding billing period under review.

3. Prepare a summary schedule showing the calculation of Total E(m), Net Retail E(m), and the surcharge factor for the expense months covered by the applicable billing period. 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. The summary schedule is to incorporate all corrections and revisions to the monthly surcharge filings KU has submitted during the billing periods under review. Include a calculation of any additional over- or under-recovery amount KU believes needs to be recognized for the 6-month review or the 2-year review. Include all supporting calculations and documentation for any such additional over- or under-recovery.

4. Provide the calculations, assumptions, workpapers, and other supporting documents used to determine the amounts KU has reported during each billing period under review for Pollution Control Deferred Income Taxes.

5. Provide the percentage of KU's long-term debt that has a variable interest rate as of the last expense month in the applicable billing period under review.

Billing Period from May 1, 2006 through October 31, 2006

6. Refer to ES Form 2.50, Pollution Control – Operations & Maintenance Expenses, for the March through August 2006 expense months. For each expense account number listed on this schedule, explain the reason(s) for any change in the expense levels from month to month if that change is greater than plus or minus 10 percent.

Billing Period from May 1, 2005 through April 30, 2007

7. Refer to ES Form 2.31, Inventory of Emission Allowances (SO₂) – Current Vintage Year, for the January 2007 expense month. Explain the reason(s) for the negative 736 allowance adjustment classified as “Allocations/Purchases.”

8. Refer to ES Form 2.50, Pollution Control – Operations & Maintenance Expenses, for the December 2006 expense month. Is the total expense shown as \$372,355 correct? Monthly environmental surcharge filings for expense months after February 2007 do not report this level of expense.

9. Refer to ES Form 2.50, Pollution Control – Operations & Maintenance Expenses, for the September 2006 through February 2007 expense months. For each expense account number listed on this schedule, explain the reason(s) for any change in the expense levels from month to month if that change is greater than plus or minus 10 percent.

10. In Case No. 2006-00129, the Commission determined an overall rate of return on capital that included a rate of return on common equity for the environmental surcharge of 10.5 percent. The Commission also found that the rate of return on

common equity used in the determination of the overall rate of return on capital should be examined as part of the 2-year surcharge review proceeding.

a. Does KU 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 KU propose for its environmental surcharge? Provide a detailed analysis and testimony supporting KU's position.

11. 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.

a. Provide the surcharge amount that KU believes should be incorporated into its existing base rates. Include all supporting calculations, workpapers, and assumptions.

b. The surcharge factor reflects a percentage of revenue approach, rather than a per kWh approach. Taking this into consideration, explain how the surcharge amount should be incorporated into KU's base rates. Include any analysis that KU believes supports its position.

c. Provide the Base Period Jurisdictional Environmental Surcharge Factor ("BESF") that reflects all environmental surcharge amounts previously incorporated into existing base rates and the amount determined in part (a). Include all supporting calculations, workpapers, and assumptions.

d. Does KU believe that there will need to be modifications to either the surcharge mechanism or the monthly surcharge reports, other than a revision to BESF, as a result of incorporating additional environmental surcharge amounts into KU's existing base rates? If yes, provide a detailed explanation of the modifications and provide updated monthly surcharge reports.

12. In Case No. 2000-00439, the Commission ordered that KU's cost of debt and preferred stock would be reviewed and re-established during the 6-month review case. Provide the following information as of February 28, 2007:

a. The outstanding balances for long-term debt, short-term debt, preferred stock, and common equity. Provide this information on total company and Kentucky jurisdictional bases.

b. The blended interest rates for long-term debt, short-term debt, and preferred stock. Include all supporting calculations showing how these blended interest rates were determined. If applicable, provide the blended interest rates on total company and Kentucky jurisdictional bases.

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

13. In its January 31, 2007 Order in Case No. 2006-00129, the Commission noted KU's efforts at identifying and resolving internal issues related to the preparation of the monthly surcharge filings. Provide a status report on KU's efforts to submit the most accurate and timely information available in its monthly surcharge reports.