

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) CASE NO.
UTILITIES COMPANY FOR THE SIX-MONTH) 2013-00436
BILLING PERIOD ENDING OCTOBER 31, 2013)**

**RESPONSE OF
KENTUCKY UTILITIES COMPANY
TO
COMMISSION STAFF'S SECOND REQUEST FOR INFORMATION
DATED FEBRUARY 26, 2014**

FILED: March 13, 2014

VERIFICATION

COMMONWEALTH OF KENTUCKY)
) SS:
COUNTY OF JEFFERSON)

The undersigned, **Christopher M. Garrett**, being duly sworn, deposes and says that he is Director – Accounting and Regulatory Reporting for LG&E and KU Services Company, and that he has personal knowledge of the matters set forth in the responses for which he is identified as the witness, and the answers contained therein are true and correct to the best of his information, knowledge and belief.

Christopher M. Garrett

Christopher M. Garrett

Subscribed and sworn to before me, a Notary Public in and before said County and State, this 11th day of March 2014.

Sheri Gardner (SEAL)

Notary Public

My Commission Expires:

SHERI L. GARDNER
Notary Public, State at Large, KY
My Commission expires Dec. 24, 2017
Notary ID # 501600

KENTUCKY UTILITIES COMPANY

**Response to Commission Staff's Second Request for Information
Dated February 26, 2014**

Case No. 2013-00436

Question No. 1

Witness: Robert M. Conroy

- Q-1. In its response to Commission Staff's First Request for Information ("Staff's First Request"), item 1, KU calculated the true-up adjustment to recognize the change in KU's cost of debt based on rates for the billing month of October 2013 rather than for the expense month of August 2013. Provide KU's reasons for using the billing month of October 2013.
- A-1. KU used the billing month of October 2013 in its response to Staff's First Request, item 1 to calculate the true-up adjustment consistent with the calculations provided in previous ECR review cases. In Case No. 2000-00439, the Commission approved the use of an overall rate of return for the 2001 ECR Plan. In the first review case to consider the billing periods that included the use of the overall rate of return, Case No. 2003-00068, the questions regarding the true-up adjustment specifically included the *billing month* that corresponded to the end of the billing period under review. The questions regarding the true-up adjustment also included a request for information used to review and re-establish the cost of debt on a going-forward basis in the monthly filings. In the next review, Case No. 2006-00129, the current format and wording of the question in Staff's First Request, item 1 was issued but did not include a date. Consistent with the information and calculations provided in previous reviews, KU prepared the response as of the last billing month in the period under review. In addition, in Case No. 2006-00129, the question regarding the review and re-establishment of the cost of debt on a going-forward basis in the monthly filings was added and specifically requested the information as of the last *expense month* in the period under review.

Therefore, consistent with prior Commission proceedings and requests for information, the last *billing month* in the review period is used for the true-up adjustment and the last *expense month* in the review period is used to re-establish the overall rate of return used on a going-forward basis.

KENTUCKY UTILITIES COMPANY

**Response to Commission Staff's Second Request for Information
Dated February 26, 2014**

Case No. 2013-00436

Question No. 2

Witness: Christopher M. Garrett / Robert M. Conroy

- Q-2. Refer to KU's response to Staff's First Request, item 1, page 3 of 3.
- a. Footnote (a) indicates that the short-term debt and long-term debt amounts are based on an average daily balance per the Settlement Agreement in Case No. 2011-00161.¹ Provide the time frame of average daily balances used to determine the amounts of short-term and long-term debt indicated on this schedule.
 - b. Provide the time period used to calculate the Annual Cost Rate shown in column 14.
 - c. Provide in Excel spreadsheet format, with formulas intact and unprotected and all rows and columns accessible, the calculations supporting each of the Annual Cost Rates shown in column 14.
 - d. Does the Company believe that using the average daily balances and daily interest rate for short-term debt and long-term debt for each expense month during the review period to calculate the actual weighted average cost of capital to be used in the true-up calculation would be consistent with the intent of Section 3.04 of the Settlement Agreement in Case No. 2011-00161? If not, explain.
 - e. In Excel spreadsheet format, with formulas intact and unprotected and all rows and columns accessible, calculate the weighted cost of capital grossed up for income tax effect for each of the six expense months ending with August 2013 using the average daily balances and daily interest rate for short-term debt and long-term debt for each expense month.
- A-2. a. The time frame of the average daily balances used to determine the amounts of short-term and long-term debt shown on KU's response to Staff's First Request, item 1, page 3 of 3 is the six-month billing period ending October 31, 2013.

¹ Case No. 2011-00161, Application of Kentucky Utilities Company for Certificates of Public Convenience and Necessity and Approval of its 2011 Compliance Plan for Recovery by Environmental Surcharge (Ky. PSC Dec. 15, 2011).

- b. The time period used to calculate the short-term debt and long-term debt rates in column 14 is the six-month billing period ending October 31, 2013. The annual cost rate for common equity is the return on equity as agreed to and approved by the Commission in its December 20, 2012 Order in KU's most recent rate case, Case No. 2012-00221.
- c. Please see the attachment being provided in Excel format.
- d. No, the Company does not believe the calculation described in the question would be consistent with the intent of Section 3.04 of the Settlement Agreement in Case No. 2011-00161. The intent of the Settlement Agreement was to maintain the long-standing true-up calculation methodology and to reflect the average daily balances and daily interest rates for short-term and long-term debt over the six-month review period instead of the end-of-period balances and rates.
- e. Please see the attachment being provided in Excel format.

KENTUCKY UTILITIES

Adjusted Electric Rate of Return on Common Equity
As of March 31, 2013

	Balance at 03-31-13 (1)	Capital Structure (2)	EEI (3)	Investments in OVEC and Other (Col 2 x Col 4 Line 4) (4)	Adjustments to Total Co. Capitalization (Sum of Col 3 - Col 4) (5)	Adjusted Total Company Capitalization (Col 1 + Col 5) (6)	Jurisdictional Rate Base Percentage (7)	Kentucky Jurisdictional Capitalization (Col 6 x Col 7) (8)
1. Short Term Debt	\$ 141,789,949 (a)	3.33%	\$ -	\$ (40,683)	\$ (40,683)	\$ 141,749,266	87.63%	\$ 124,214,882
2. Long Term Debt	1,841,279,398 (a)	43.21%	-	(527,905)	(527,905)	1,840,751,493	87.63%	1,613,050,533
3. Common Equity	2,277,704,473	53.46%	(504,066)	(653,132)	(1,157,198)	2,276,547,275	87.63%	1,994,938,377
4. Total Capitalization	<u>\$ 4,260,773,820</u>	<u>100.000%</u>	<u>\$ (504,066)</u>	<u>\$ (1,221,720)</u>	<u>\$ (1,725,786)</u>	<u>\$ 4,259,048,034</u>		<u>\$ 3,732,203,792</u>

	Kentucky Jurisdictional Capitalization (8)	Capital Structure (9)	Environmental Surcharge (Col 9 x Col 10 Line 4) (10)	DSM Rate Base (Col 9 x Col 11 Line 4) (11)	Adjusted Kentucky Jurisdictional Capitalization (Col 8 + Col 10 + Col 11) (12)	Adjusted Capital Structure (13)	Annual Cost Rate (14)	Cost of Capital (Col 13 x Col 14) (15)
1. Short Term Debt	\$ 124,214,882	3.33%	\$ (13,615,910)	\$ (20,419)	\$ 110,578,553	3.33%	0.38%	0.01%
2. Long Term Debt	1,613,050,533	43.22%	(176,720,604)	(265,015)	1,436,064,914	43.22%	3.68%	1.59%
3. Common Equity	1,994,938,377	53.45%	(218,549,658)	(327,743)	1,776,060,976	53.45%	10.25%	5.48%
4. Total Capitalization	<u>\$ 3,732,203,792</u>	<u>100.000%</u>	<u>\$ (408,886,172)</u>	<u>\$ (613,177)</u>	<u>\$ 3,322,704,443</u>	<u>100.000%</u>		<u>7.08%</u>
5. Weighted Cost of Capital Grossed up for Income Tax Effect {ROR + (ROR - DR) x [TR / (1 - TR)]}								<u>10.12%</u>

(a) Average daily balance per Settlement Agreement in Case No. 2011-00161.

KENTUCKY UTILITIES

Adjusted Electric Rate of Return on Common Equity
As of April 30, 2013

	Balance at 04-30-13 (1)	Capital Structure (2)	EEI (3)	Investments in OVEC and Other (Col 2 x Col 4 Line 4) (4)	Adjustments to Total Co. Capitalization (Sum of Col 3 - Col 4) (5)	Adjusted Total Company Capitalization (Col 1 + Col 5) (6)	Jurisdictional Rate Base Percentage (7)	Kentucky Jurisdictional Capitalization (Col 6 x Col 7) (8)
1. Short Term Debt	\$ 76,493,213 (a)	1.82%	\$ -	\$ (22,235)	\$ (22,235)	\$ 76,470,978	87.63%	\$ 67,011,518
2. Long Term Debt	1,841,305,779 (a)	43.80%	-	(535,113)	(535,113)	1,840,770,666	87.63%	1,613,067,335
3. Common Equity	2,285,693,928	54.38%	(504,066)	(664,372)	(1,168,438)	2,284,525,490	87.63%	2,001,929,687
4. Total Capitalization	<u>\$ 4,203,492,920</u>	<u>100.000%</u>	<u>\$ (504,066)</u>	<u>\$ (1,221,720)</u>	<u>\$ (1,725,786)</u>	<u>\$ 4,201,767,134</u>		<u>\$ 3,682,008,540</u>

	Kentucky Jurisdictional Capitalization (8)	Capital Structure (9)	Environmental Surcharge (Col 9 x Col 10 Line 4) (10)	DSM Rate Base (Col 9 x Col 11 Line 4) (11)	Adjusted Kentucky Jurisdictional Capitalization (Col 8 + Col 10 + Col 11) (12)	Adjusted Capital Structure (13)	Annual Cost Rate (14)	Cost of Capital (Col 13 x Col 14) (15)
1. Short Term Debt	\$ 67,011,518	1.82%	\$ (7,788,584)	\$ (12,704)	\$ 59,210,230	1.82%	0.35%	0.01%
2. Long Term Debt	1,613,067,335	43.81%	(187,482,355)	(305,792)	1,425,279,188	43.81%	3.69%	1.62%
3. Common Equity	2,001,929,687	54.37%	(232,673,263)	(379,501)	1,768,876,923	54.37%	10.25%	5.57%
4. Total Capitalization	<u>\$ 3,682,008,540</u>	<u>100.000%</u>	<u>\$ (427,944,202)</u>	<u>\$ (697,997)</u>	<u>\$ 3,253,366,341</u>	<u>100.000%</u>		<u>7.20%</u>
5. Weighted Cost of Capital Grossed up for Income Tax Effect {ROR + (ROR - DR) x [TR / (1 - TR)]}								<u>10.29%</u>

(a) Average daily balance per Settlement Agreement in Case No. 2011-00161.

KENTUCKY UTILITIES

Adjusted Electric Rate of Return on Common Equity
As of May 31, 2013

	Balance at 05-31-13 (1)	Capital Structure (2)	EEI (3)	Investments in OVEC and Other (Col 2 x Col 4 Line 4) (4)	Adjustments to Total Co. Capitalization (Sum of Col 3 - Col 4) (5)	Adjusted Total Company Capitalization (Col 1 + Col 5) (6)	Jurisdictional Rate Base Percentage (7)	Kentucky Jurisdictional Capitalization (Col 6 x Col 7) (8)
1. Short Term Debt	\$ 146,208,367 (a)	3.41%	\$ -	\$ (41,661)	\$ (41,661)	\$ 146,166,706	87.63%	\$ 128,085,884
2. Long Term Debt	1,841,491,499 (a)	42.92%	-	(524,362)	(524,362)	1,840,967,137	87.63%	1,613,239,502
3. Common Equity	2,302,500,761	53.67%	(504,066)	(655,697)	(1,159,763)	2,301,340,998	87.63%	2,016,665,117
4. Total Capitalization	<u>\$ 4,290,200,627</u>	<u>100.000%</u>	<u>\$ (504,066)</u>	<u>\$ (1,221,720)</u>	<u>\$ (1,725,786)</u>	<u>\$ 4,288,474,841</u>		<u>\$ 3,757,990,503</u>

	Kentucky Jurisdictional Capitalization (8)	Capital Structure (9)	Environmental Surcharge (Col 9 x Col 10 Line 4) (10)	DSM Rate Base (Col 9 x Col 11 Line 4) (11)	Adjusted Kentucky Jurisdictional Capitalization (Col 8 + Col 10 + Col 11) (12)	Adjusted Capital Structure (13)	Annual Cost Rate (14)	Cost of Capital (Col 13 x Col 14) (15)
1. Short Term Debt	\$ 128,085,884	3.41%	\$ (14,962,645)	\$ (46,830)	\$ 113,076,409	3.41%	0.35%	0.01%
2. Long Term Debt	1,613,239,502	42.93%	(188,371,370)	(589,560)	1,424,278,572	42.93%	3.67%	1.58%
3. Common Equity	2,016,665,117	53.66%	(235,453,243)	(736,915)	1,780,474,959	53.66%	10.25%	5.50%
4. Total Capitalization	<u>\$ 3,757,990,503</u>	<u>100.000%</u>	<u>\$ (438,787,258)</u>	<u>\$ (1,373,305)</u>	<u>\$ 3,317,829,940</u>	<u>100.000%</u>		<u>7.09%</u>
5. Weighted Cost of Capital Grossed up for Income Tax Effect {ROR + (ROR - DR) x [TR / (1 - TR)]}								<u>10.14%</u>

(a) Average daily balance per Settlement Agreement in Case No. 2011-00161.

KENTUCKY UTILITIES

Adjusted Electric Rate of Return on Common Equity
As of June 30, 2013

	Balance at 06-30-13 (1)	Capital Structure (2)	EEI (3)	Investments in OVEC and Other (Col 2 x Col 4 Line 4) (4)	Adjustments to Total Co. Capitalization (Sum of Col 3 - Col 4) (5)	Adjusted Total Company Capitalization (Col 1 + Col 5) (6)	Jurisdictional Rate Base Percentage (7)	Kentucky Jurisdictional Capitalization (Col 6 x Col 7) (8)
1. Short Term Debt	\$ 157,650,274 (a)	3.65%	\$ -	\$ (44,593)	\$ (44,593)	\$ 157,605,681	87.63%	\$ 138,109,858
2. Long Term Debt	1,841,517,534 (a)	42.63%	-	(520,819)	(520,819)	1,840,996,715	87.63%	1,613,265,421
3. Common Equity	2,320,901,623	53.72%	(504,066)	(656,308)	(1,160,374)	2,319,741,249	87.63%	2,032,789,256
4. Total Capitalization	<u>\$ 4,320,069,431</u>	<u>100.000%</u>	<u>\$ (504,066)</u>	<u>\$ (1,221,720)</u>	<u>\$ (1,725,786)</u>	<u>\$ 4,318,343,645</u>		<u>\$ 3,784,164,535</u>

	Kentucky Jurisdictional Capitalization (8)	Capital Structure (9)	Environmental Surcharge (Col 9 x Col 10 Line 4) (10)	DSM Rate Base (Col 9 x Col 11 Line 4) (11)	Adjusted Kentucky Jurisdictional Capitalization (Col 8 + Col 10 + Col 11) (12)	Adjusted Capital Structure (13)	Annual Cost Rate (14)	Cost of Capital (Col 13 x Col 14) (15)
1. Short Term Debt	\$ 138,109,858	3.65%	\$ (16,711,841)	\$ (56,938)	\$ 121,341,079	3.65%	0.33%	0.01%
2. Long Term Debt	1,613,265,421	42.63%	(195,185,143)	(665,004)	1,417,415,274	42.63%	3.68%	1.57%
3. Common Equity	2,032,789,256	53.72%	(245,961,668)	(838,001)	1,785,989,587	53.72%	10.25%	5.51%
4. Total Capitalization	<u>\$ 3,784,164,535</u>	<u>100.000%</u>	<u>\$ (457,858,652)</u>	<u>\$ (1,559,943)</u>	<u>\$ 3,324,745,940</u>	<u>100.000%</u>		<u>7.09%</u>
5. Weighted Cost of Capital Grossed up for Income Tax Effect {ROR + (ROR - DR) x [TR / (1 - TR)]}								<u>10.15%</u>

(a) Average daily balance per Settlement Agreement in Case No. 2011-00161.

KENTUCKY UTILITIES

Adjusted Electric Rate of Return on Common Equity
As of July 31, 2013

	Balance at 07-31-13 (1)	Capital Structure (2)	EEI (3)	Investments in OVEC and Other (Col 2 x Col 4 Line 4) (4)	Adjustments to Total Co. Capitalization (Sum of Col 3 - Col 4) (5)	Adjusted Total Company Capitalization (Col 1 + Col 5) (6)	Jurisdictional Rate Base Percentage (7)	Kentucky Jurisdictional Capitalization (Col 6 x Col 7) (8)
1. Short Term Debt	\$ 154,174,575 (a)	3.55%	\$ -	\$ (43,371)	\$ (43,371)	\$ 154,131,204	87.63%	\$ 135,065,174
2. Long Term Debt	1,841,544,436 (a)	42.45%	-	(518,620)	(518,620)	1,841,025,816	87.63%	1,613,290,923
3. Common Equity	2,341,938,822	54.00%	(504,066)	(659,729)	(1,163,795)	2,340,775,027	87.63%	2,051,221,156
4. Total Capitalization	<u>\$ 4,337,657,833</u>	<u>100.000%</u>	<u>\$ (504,066)</u>	<u>\$ (1,221,720)</u>	<u>\$ (1,725,786)</u>	<u>\$ 4,335,932,047</u>		<u>\$ 3,799,577,253</u>

	Kentucky Jurisdictional Capitalization (8)	Capital Structure (9)	Environmental Surcharge (Col 9 x Col 10 Line 4) (10)	DSM Rate Base (Col 9 x Col 11 Line 4) (11)	Adjusted Kentucky Jurisdictional Capitalization (Col 8 + Col 10 + Col 11) (12)	Adjusted Capital Structure (13)	Annual Cost Rate (14)	Cost of Capital (Col 13 x Col 14) (15)
1. Short Term Debt	\$ 135,065,174	3.55%	\$ (16,981,002)	\$ (61,088)	\$ 118,023,084	3.56%	0.34%	0.01%
2. Long Term Debt	1,613,290,923	42.46%	(203,102,352)	(730,643)	1,409,457,928	42.46%	3.67%	1.56%
3. Common Equity	2,051,221,156	53.99%	(258,254,733)	(929,048)	1,792,037,375	53.98%	10.25%	5.53%
4. Total Capitalization	<u>\$ 3,799,577,253</u>	<u>100.000%</u>	<u>\$ (478,338,087)</u>	<u>\$ (1,720,779)</u>	<u>\$ 3,319,518,387</u>	<u>100.000%</u>		<u>7.10%</u>
5. Weighted Cost of Capital Grossed up for Income Tax Effect {ROR + (ROR - DR) x [TR / (1 - TR)]}								<u>10.17%</u>

(a) Average daily balance per Settlement Agreement in Case No. 2011-00161.

KENTUCKY UTILITIES

Adjusted Electric Rate of Return on Common Equity
As of August 31, 2013

	Balance at 08-31-13 (1)	Capital Structure (2)	EEI (3)	Investments in OVEC and Other (Col 2 x Col 4 Line 4) (4)	Adjustments to Total Co. Capitalization (Sum of Col 3 - Col 4) (5)	Adjusted Total Company Capitalization (Col 1 + Col 5) (6)	Jurisdictional Rate Base Percentage (7)	Kentucky Jurisdictional Capitalization (Col 6 x Col 7) (8)
1. Short Term Debt	\$ 145,021,963 (a)	3.35%	\$ -	\$ (40,928)	\$ (40,928)	\$ 144,981,035	87.63%	\$ 127,046,881
2. Long Term Debt	1,841,571,120 (a)	42.60%	-	(520,453)	(520,453)	1,841,050,667	87.63%	1,613,312,699
3. Common Equity	2,336,831,556	54.05%	(504,066)	(660,339)	(1,164,405)	2,335,667,151	87.63%	2,046,745,124
4. Total Capitalization	<u>\$ 4,323,424,639</u>	<u>100.000%</u>	<u>\$ (504,066)</u>	<u>\$ (1,221,720)</u>	<u>\$ (1,725,786)</u>	<u>\$ 4,321,698,853</u>		<u>\$ 3,787,104,704</u>

	Kentucky Jurisdictional Capitalization (8)	Capital Structure (9)	Environmental Surcharge (Col 9 x Col 10 Line 4) (10)	DSM Rate Base (Col 9 x Col 11 Line 4) (11)	Adjusted Kentucky Jurisdictional Capitalization (Col 8 + Col 10 + Col 11) (12)	Adjusted Capital Structure (13)	Annual Cost Rate (14)	Cost of Capital (Col 13 x Col 14) (15)
1. Short Term Debt	\$ 127,046,881	3.35%	\$ (16,599,876)	\$ (60,699)	\$ 110,386,306	3.36%	0.33%	0.01%
2. Long Term Debt	1,613,312,699	42.60%	(211,090,964)	(771,869)	1,401,449,866	42.60%	3.64%	1.55%
3. Common Equity	2,046,745,124	54.05%	(267,827,854)	(979,332)	1,777,937,938	54.04%	10.25%	5.54%
4. Total Capitalization	<u>\$ 3,787,104,704</u>	<u>100.000%</u>	<u>\$ (495,518,694)</u>	<u>\$ (1,811,900)</u>	<u>\$ 3,289,774,110</u>	<u>100.000%</u>		<u>7.10%</u>
5. Weighted Cost of Capital Grossed up for Income Tax Effect {ROR + (ROR - DR) x [TR / (1 - TR)]}								<u>10.18%</u>

(a) Average daily balance per Settlement Agreement in Case No. 2011-00161.

KENTUCKY UTILITIES COMPANY

**Response to Commission Staff's Second Request for Information
Dated February 26, 2014**

Case No. 2013-00436

Question No. 3

Witness: Robert M. Conroy

- Q-3. Refer to KU's response to Staff's First Request, item 2, page 2 of 3, columns (9) and (10).
- a. Explain KU's position regarding the decision to true up any over- or under-recovery of environmental surcharge amounts in a six-month or two-year review versus trueing up any over- or under-recovery on a monthly basis.
 - b. Confirm that the ECR Billing Factor Revenues are available for Group 1 and Group 2 at the time the monthly environmental surcharge report is filed with the Commission for a particular expense month, thereby allowing KU to calculate an over- or under-recovery position for each group, which could be included as a monthly true-up for that particular expense month in the monthly filing.
 - c. Would KU agree that if these over- or under-recovery amounts are reflected in the monthly filings in determining each group's environmental surcharge billing factor, this action would result in a more timely resolution of any over- or under-collection from a ratepayer's standpoint, rather than waiting until the Commission issues an order in a six-month or two-year review?
 - d. Would KU agree that calculating the over- or under-recovery by customer group would more accurately allocate the over- or under-recovery to the customer group generating the over- or under-recovery?
 - e. Would KU agree that by including any over- or under-recovery in the monthly filings, it would eliminate the need to reflect any over/under reconciliation associated with the use of the 12-month average revenues in both the six-month and the two-year environmental surcharge reviews?
- A-3. a. KU has been, and continues to be, open to improvements and modifications to the ECR mechanism to achieve a more timely and accurate result. For example, when the base period environmental surcharge factor ("BESF") was implemented in KU's monthly filings in Case No. 2003-00068, KU supported the addition of a 2-month true-up adjustment as a means to resolve timing differences inherent in

the ECR mechanism and the use of the BESF percentage method to estimate the revenue collected through base rates. In Case No. 2009-00310, the Commission approved a modification of the calculation of the monthly billing factor from a percentage (BESF) method to the current revenue requirement method and elimination of the monthly true-up adjustment. The revenue requirement method uses actual revenues collected through base rates and removes some of the timing differences that created the need for a true-up adjustment. In KU's experience, the true-up adjustment did not result in a reduction of the cumulative over- or under-collection position presented in periodic review cases, as was its intent. The calculation of the previous true-up adjustment also added unnecessary complications to the monthly filing without providing the intended benefit.

The primary components of KU's over- or under-recovery of environmental surcharge amounts are due to the true-up adjustment to recognize changes in the cost of debt and capital structure and timing differences inherent in the ECR mechanism. The changes in the cost of debt and capital structure for a six-month billing period are not known until the end of the period and therefore will continue to result in an over- or under-recovery to be resolved in the review cases. The timing differences inherent in the ECR mechanism are a result of the use of 12-month average revenues to determine the monthly billing factor that is applied to actual revenues two months later. The addition of a true-up adjustment to the monthly filings may provide a more timely resolution to any over- or under recovery associated with the use of 12-month average revenues but the month-to-month volatility to the monthly billing factors would also increase.

- b. The ECR Billing Factor Revenues are available for Group 1 and Group 2 at the time the monthly environmental surcharge report is filed with the Commission for a particular expense month. The Settlement Agreement ("Agreement") in Case No. 2011-00161 states that each utility's total ECR revenues to be collected will be allocated between each rate class on a total-revenue basis. The intent of the Agreement was that the then current method of allocation on total revenue be maintained as modified by a two-step approach. The total amount of ECR revenues to be collected from the rate classes identified in Section 5.03 of the Agreement ("Group 1"), are determined on a total-revenues basis and billed to each customer based on total revenue. The total ECR revenues from the remaining rate classes identified in Section 5.04 of the Agreement ("Group 2") as determined based on a total revenue allocation, are reallocated and billed to each customer on the basis of non-fuel revenues. The intent of the Agreement was to modify the revenue allocation methodology for customers in Group 2 in a manner that would not impact customers in Group 1. It is necessary to maintain the current order of operation in the monthly calculation to comply with this intent. In the two-year review case implementing the new allocation methodology, Case No. 2011-00231, the Commission originally approved the use of ES Forms that included the calculation as described in this question. On February 22, 2012, KU met with Commission Staff to discuss modifications to the monthly billing factor

calculations that were necessary to avoid negatively impacting Group 1 customers that were not to be impacted by the new revenue allocation methodology. Please see the attachment for the example provided at the informal conference that shows how the order of operation impacts the monthly billing factor results. The Commission issued an order on February 29, 2012 approving the proposed revisions to the ES Forms necessary to meet the requirements as well as the intent of the Settlement Agreement in Case No. 2011-00161 for Group 1 and Group 2.

- c. Please see the response to part a and b.
- d. Please see the response to part b.
- e. While implementation of a true-up adjustment in the monthly filings should eliminate the need to reflect over/under recovery associated with the use of the 12-month average revenues in the six-month and two-year environmental surcharge review cases, it would not eliminate the impact of the use of 12-month average revenues inherent in the monthly billing factor calculation. Adding a true-up adjustment would increase the month-to-month volatility of the monthly billing factors and add complexity to the monthly calculations. The implementation of the current revenue requirement methodology without a true-up adjustment has reduced the dramatic fluctuations in the monthly over- or under-recovery positions seen prior to the implementation.

**KENTUCKY UTILITIES COMPANY
ENVIRONMENTAL SURCHARGE REPORT**

**Calculation of Total E(m) and
Jurisdictional Surcharge Billing Factor**

For the Expense Month of January 2012

ONE STEP METHOD (Pre-Settlement)

Calculation of Jurisdictional Environmental Surcharge Billing Factor

(8)	Jurisdictional Allocation Ratio for Expense Month -- ES Form 3.00	=	84.75%
(9)	Jurisdictional E(m) = E(m) x Jurisdictional Allocation Ratio [(7) x (8)]	= \$	14,710,590
(10)	Adjustment for (Over)/Under-collection pursuant to Case No. 2010-00474	=	(596,811)
(11)	Prior Period Adjustment (if necessary)	=	-
(12)	Adjusted Jurisdictional E(m) [(9) + (10) + (11)]	=	14,113,779
(13)	Revenue Collected through Base Rates	= \$	11,614,699
(14)	Net Jurisdictional E(m) = Jurisdictional E(m) less Expense Month Revenue Collected Through Base Rates [(12) - (13)]	= \$	2,499,080
(15)	Jurisdictional R(m) = Average Monthly Jurisdictional Revenue for the 12 Months Ending with the Current Expense Month -- ES Form 3.00	=	105,753,858
(16)	Jurisdictional Environmental Surcharge Billing Factor [(14) ÷ (15)]	=	2.36%

**KENTUCKY UTILITIES COMPANY
ENVIRONMENTAL SURCHARGE REPORT**

Calculation of Total E(m) and
Jurisdictional Surcharge Billing Factor

For the Expense Month of January 2012

TWO STEP METHOD - FORMS AS FILED FEBRUARY 17, 2012

Calculation of Adjusted Net Jurisdictional E(m)

(9)	Jurisdictional Allocation Ratio for Expense Month -- ES Form 3.10	=		84.75%
(10)	Jurisdictional E(m) = Total E(m) x Jurisdictional Allocation Ratio [(8) x (9)]	= \$		14,710,590
(11)	Adjustment for (Over)/Under-collection pursuant to Case No. 2011-00231	= \$		(596,811)
(12)	Prior Period Adjustment (if necessary)	= \$		-
(13)	Revenue Collected through Base Rates	= \$		11,614,699
(14)	Adjusted Net Jurisdictional E(m) [(10) + (11) + (12) - (13)]	=		2,499,080

Calculation of Group Environmental Surcharge Billing Factors

			<u>GROUP 1 (Total Revenue)</u>		<u>GROUP 2 (Net Revenue)</u>
(15)	Revenue as a Percentage of 12-month Total Revenue ending with the Current Month -- ES Form 3.00	=	39.50%		60.50%
(16)	Group E(m) [(14) x (15)]	= \$	987,137	\$	1,511,943
(17)	Group R(m) = Average Monthly Group Revenue for the 12 Months Ending with the Current Expense Month -- ES Form 3.00	= \$	41,768,106	\$	36,566,487
(18)	Group Environmental Surcharge Billing Factors [(16) ÷ (17)]	=	2.36%		4.13%

**KENTUCKY UTILITIES COMPANY
ENVIRONMENTAL SURCHARGE REPORT**

Calculation of Total E(m) and
Jurisdictional Surcharge Billing Factor

For the Expense Month of January 2012

TWO STEP METHOD - FORMS AS FILED NOVEMBER 21, 2011

Calculation of Adjusted Total Jurisdictional E(m)

(9)	Jurisdictional Allocation Ratio for Expense Month -- ES Form 3.10	=		84.75%
(10)	Jurisdictional E(m) = Total E(m) x Jurisdictional Allocation Ratio [(8) x (9)]	= \$		14,710,590
(11)	Prior Period Adjustment related to Rate Base or OE (if necessary)	= \$		-
(12)	Adjusted Total Jurisdictional E(m) [(10) + (11)]	=		14,710,590

Calculation of Group Environmental Surcharge Billing Factors

			<u>GROUP 1 (Total Revenue)</u>		<u>GROUP 2 (Net Revenue)</u>
(13)	Revenue as a Percentage of Total Revenue for Current Month -- ES Form 3.00	=	47.44%		52.56%
(14)	Group E(m) [(12) x (13)]	= \$	6,978,704	\$	7,731,886
(15)	Adjustment for (Over)/Under-collection pursuant to Case No. 2011-00231	= \$	(283,127)	\$	(313,684)
(16)	Prior Period Adjustment related to Revenue (if necessary)	= \$	-	\$	-
(17)	Revenue Collected through Base Rates	= \$	4,873,646	\$	6,741,053
(18)	Net Group E(m) = Group E(m) less Expense Month Revenue Collected Through Base Rates [(14) + (15) + (16) - (17)]	= \$	1,821,931	\$	677,150
(19)	Group R(m) = Average Monthly Group Revenue for the 12 Months Ending with the Current Expense Month -- ES Form 3.00	= \$	41,768,106	\$	36,566,487
(20)	Group Environmental Surcharge Billing Factors [(18) ÷ (19)]	=	4.36%		1.85%