

**COMMONWEALTH OF KENTUCKY**  
**BEFORE THE PUBLIC SERVICE COMMISSION**

**In the Matter of:**

<b>APPLICATION OF KENTUCKY UTILITIES</b>	)	
<b>COMPANY FOR AN ADJUSTMENT OF ITS</b>	)	<b>CASE NO. 2014-00371</b>
<b>ELECTRIC RATES</b>	)	

**KENTUCKY INDUSTRIAL UTILITY CUSTOMERS, INC.'S**  
**RESPONSE TO COMMISSION STAFF'S**  
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1. Refer to the Direct Testimony and Exhibits of Lane Kollen ("Kollen Testimony"), page 7, specifically, the chart showing the total electric rates of Kentucky Utilities Company ("KU") from 2004-2013.
  - a. Explain whether Mr. Kollen has attempted to break down the increases in KU's rates depicted in the aforementioned chart to reflect the amounts of increase in base rates, fuel costs, environmental charges, etc.
  - b. Explain whether Mr. Kollen has attempted to compare, or match, these prior increases in KU's electric rates with increases in its investment in electric plant over the period 2001 -2013.

**RESPONSE:**

- a. No. The purpose of the charts was to show the significant increases in customer rates. Mr. Kollen did not attempt to determine the reasons for the increases.
- b. No. The purpose of the charts was to show the significant increases in customer rates. Mr. Kollen did not attempt to determine the reasons for the increases.

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2. Refer to the Kollen Testimony, page 14, line 24, to page 16, line 2. The Testimony refers to increases in employee staffing levels since the purchase of KU in 2010 by PPL Corporation. Explain whether Mr. Kollen recognized the commercialization of Trimble Unit No. 2 in his review of changes in KU's generation facilities since 2010 that may have impacted staffing levels.

**RESPONSE:**

Trimble County 2 entered commercial operation in January 2011. Mr. Kollen believes that the additional employees required to operate and maintain the unit were hired in 2010, not in January 2011.

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3. Refer to the Kollen Testimony, page 5, Summary of Revenue Requirement Adjustments: page 21, line 14, to page 22, line 3; and Exhibits (LK-12) and (LK-13). The Exhibits show actual and projected operating expenses for Green River Units 3, 4, and common. On pages 21 and 22, Mr. Kollen states that the majority of the expenses included in KU's forecasted operations for these units are nonrecurring. On page 5, he shows that removal of these nonrecurring expenses from KU's forecasted test year will reduce KU's revenue requirement by \$10.1 million. Provide a copy of the workpapers prepared by Mr. Kollen that show the derivation of the nonrecurring expenses from the Exhibits, and the calculation of their impact on KU's revenue requirement.

**RESPONSE:**

Please refer to Mr. Kollen's workpapers attached.

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4. Refer to the Kollen Testimony, page 27, lines 18-20, and Exhibit (LK-19). The Testimony states that KU seeks an increase in pension expense of \$15.3 million compared to its calendar year 2014 expense and an increase of \$12.5 million compared to its base year expense. The Exhibit, which reflects the proposed test-year expense of \$26 million, supports the statement in the testimony. The Exhibit also reflects that the 2014 expense of \$10.7 million was the lowest annual expense since \$10 million in 2008. It also reflects that for the years from 2009-2013 the annual expense ranged from \$21.4-\$29.7 million and averaged \$26.3 million, \$0.3 million less than the proposed test-year level. Explain whether Mr. Kollen would have the Commission focus only on the level of increase cited in his testimony and ignore the older historical levels, including the level in the test year of KU's previous rate case.

**RESPONSE:**

Pension expense varies from year to year based on actual trust fund assets and various assumptions used to project future trust fund assets and the pension obligation, including the return on trust fund assets, discount rate, mortality statistics, employee compensation increases, and the timing and amounts of future pension payments, among others. Given all these changes from year to year, the pension expense in years prior to the most recent actual historic calendar year is irrelevant for a projected test year. In fact, this is true for pension accounting aside from ratemaking. The Companies' actuaries perform a new standalone calculation of pension expense each year that has nothing to do with the pension expense calculated in prior years, except to the extent the expense changed certain asset or liability amounts. The Companies' actuaries use certain actual and estimated asset and liability amounts at the end of the most recent calendar year (trust fund assets, transition obligation, participant demographics, pension benefit obligation, etc.) including the effects of various assumptions to project all components of pension expense. In other words, the expense in years prior to the most recent actual historic calendar year is irrelevant to the actuaries or their calculation of the projected pension expense for 2015, 2016 and the test year.

If the Companies did not adopt the new mortality tables or reduce the discount rate for 2015, 2016 and the test year, their pension expense would have been comparable to the 2014 level. However, the question facing the Commission is not whether the 2014 expense was

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reasonable, but whether the test year expense is reasonable. The adoption of the new mortality tables and a lower discount rate created a huge increase in the pension obligation. Under GAAP, the Companies will amortize this increase over less than 10 years. Mr. Kollen does not believe that it is reasonable to amortize the increase over this unduly short time period for ratemaking purposes and proposes a longer period to smooth the impact on customer rates. Mr. Kollen also is concerned that the Companies' expense for GAAP will peak in 2015 based on the actuarial report and that the test year pension expenses they propose will result in overrecoveries of this expense in future years, all else equal. Finally, it should be noted that Mr. Kollen's recommendation will not harm the Companies, diminish their earnings, or cause them to underrecover pension expense. They will be able to defer the timing difference between GAAP pension expense and the amount allowed for ratemaking purposes.

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5. Refer to the Kollen Testimony, page 33, lines 8-10. Explain how Mr. Kollen selected 30 years as the amortization period for the net actuarial losses reflected in KU's pension plan.

RESPONSE:

Mr. Kollen understands that the average age of the Companies' employees is 47 based on their workforce study provided in this proceeding. The average life expectancy of men and women now exceeds 80 years. Thus, the average remaining lives of the plan participants exceeds 30 years. The Company's GAAP accounting ostensibly reflects the average remaining "service period of active employees expected to receive benefits." Mr. Kollen did not disagree with or oppose the Companies' GAAP accounting, although he believes that the GAAP requirement to amortize over the average remaining "service period of active employees expected to receive benefits" unnecessarily accelerates the allocation of future pension payments into the next ten years and that this is inappropriate for ratemaking purposes. That is why he provided a constructive recommendation to levelize the allocation of the increase in future pension payments over the next 30 years for ratemaking purposes.

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6. Refer to the Kollen Testimony at page 36, lines 10-20, wherein Mr. Kollen recommends using a five-year historical average to determine the appropriate level of late payment revenues for KU, and Exhibit (LK-24). The question and answer on lines 18-20 read as follows; "Should the Commission use the five year average for late payment revenues in the same manner as you recommend for uncollectible accounts expense?" "Yes, and for the same reasons."

- a. On lines 1-2 of the same page, Mr. Kollen cites the volatility in the amount of uncollectible expense as a reason for using an average level of expense. The last page of the Exhibit shows that KU's electric uncollectible expense over the past five years declined from \$6.5 million in 2010 to \$3.2 million by 2013, then increased to \$7.3 million by 2014. The first page of the Exhibit shows that its electric late payment revenues over the past five years have declined from \$10 million in 2010 to \$7.5 million in 2011, \$6.9 million in 2012, and \$3.4 million in 2013. It slightly increased to \$3.7 million in 2014. Explain whether Mr. Kollen evaluated why uncollectible expense moved down and up by large amounts while the late payment revenues only moved down until 2014 when there was a slight increase.
- b. If, as it appears, KU's late payment revenues have not shown the level of volatility as its uncollectible expense has shown over the past five years, explain why it is appropriate to use an average as Mr. Kollen proposes "for the same reasons" offered in support of his recommended adjustment to uncollectible expense.

**RESPONSE:**

- a. No. Mr. Kollen did not attempt to evaluate the reasons for the changes from year to year. Mr. Kollen would note that the Company did not attempt to explain the reasons for the changes from year to year for the Mitchell plant maintenance and offered no justification for using a three year average other than it provided a leveled amount consistent with Commission precedent.

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b. Unlike in a historical test year where actual revenues are known with certainty, the Companies' projections of revenues in the forecast test year are uncertain and the Commission must determine if those projections are reasonable. The best approach for miscellaneous revenues, such as late payment revenues, is to compare the projections to the actual revenues in prior years. That is why Mr. Kollen proposes the five year average. An average does not require an assessment of the variables that caused the revenues to vary in the prior years or how they may vary in the projected test year and it is consistent with the Company's proposal to use a three year average for the Mitchell plant maintenance expense.



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7. Refer to the Direct Testimony of Stephen J. Baron ("Baron Testimony"), pages 14-15, which discusses the traditional 5 coincident peak ("CP") method of allocating production and transmission demand costs and the PJM Interconnection, Inc. ("PJM") 5 CP method. Given that KU is not a member of PJM, explain why Mr. Baron chose the PJM 5 CP method over the traditional 5 CP method.

**RESPONSE:**

Consistent with Mr. Baron's testimony in LG&E's and KU's 2012 rate cases (Case Nos. 2012-00221 and 00222), Mr. Baron believes that the PJM "highest 5 peaks" methodology is a reasonable approach to allocate production and transmission demand costs and is consistent with cost causation. The PJM 5 CP method recognizes the importance of the annual summer peak in the decision to acquire new resources for the combined LGE/KU system, yet provides some places some weight on a number of peak hours so that an unusual occurrence during a single hour will not unduly impact the result.

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8. Refer to the Baron Testimony, page 24, lines 1-4, which state, "Since the buy-through option is also being eliminated, this means that a customer would likely face 100 hours of shut-down of its manufacturing operations, without the opportunity to buy-through, whenever the Companies deem that such an interruption should occur." Explain whether KIUC would be supportive of KU's changes to its curtailable service rider tariff if, during the 100 hours of interruption, it included the option to buy-through market power.

**RESPONSE:**

KIUC would support a reduction in the maximum hours of annual interruption to 100 hours, if a customer could buy-through any interruption, unless such interruption is called due to a system emergency event. Notwithstanding this position, KIUC continues to support its proposal to increase the interruptible credit in this case, as recommended in Mr. Baron's testimony.

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9. Refer to page 39 of the Baron Testimony.
- a. Refer to lines 1-3. Provide support for the statement that the operating expenses are allocated using the base-intermediate-peak (BIP) production demand allocation factor.
  - b. Refer to lines 9-15.
    - (1) Provide the calculation of the proposed Retirement Rider for each rate class based on KIUC's recommendations.
    - (2) Explain why the proposed Retirement Rider should be calculated on a \$/kW basis for larger rate classes. -5- Case No. 2014-00371
    - (3) Provide KIUC's recommendations on how often the Retirement Rider would change, when it would be filed with the Commission, and how any true-up would be accomplished.

**RESPONSE:**

- a. Once the units are retired, they provide no energy and it is therefore appropriate to allocate all retirement expenses on the BIP demand factors. To the extent that the units actually run during this period and a rider provides contemporaneous recovery, Mr. Baron agrees that the allocation of the rider costs could reflect a demand/energy classification consistent with the BIP cost of service study. Mr. Kollen has not developed any Retirement Rider cost information that could be used to develop rates, since his recommendation is to defer actual costs for subsequent recovery through the rider.
- b.
  - (1) The amount for each rate class would be \$0 in this proceeding and would depend on actual costs deferred for recovery in future rate cases. In this proceeding, Mr. Kollen recommends that the Commission remove the Green

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River 3 and 4 operating expenses from the base revenue requirement and defer the actual expenses for recovery in a future base rate case. The deferrals should not be based on the projected expenses in the forecast test year. As an alternative, Mr. Kollen recommended that the Commission consider a retirement rider similar to that adopted in Case No. 2012-00578 for the actual Big Sandy retirement costs, although that retirement rider included no operating expenses. In Case No. 2014-00396, KPC proposed that operating expenses be included in the rider on a projected basis. In the KPC proceeding, Mr. Kollen recommended that the Commission reject KPC's proposal and instead direct KPC to defer its actual operating expenses and then seek recovery of the deferrals through the retirement rider in a future base rate case. Mr. Kollen makes the same recommendation in this proceeding.

(2) Because all of the retirement costs are demand related, they should be allocated on a demand basis (BIP factors) in the retirement rider and, to the extent possible based on individual rate class rate design, be recovered on a kW demand basis. As discussed in response to 9(a) above, if the units actually run and there are energy related costs recovered in the Rider, Mr. Baron would not oppose recovering any such energy related costs through a kWh charge. In this case, demand metered rate classes would have both a kW demand charge and a kWh charge. For rate classes, such as the residential class that have energy-only rates, the allocated retirement costs should be recovered on a kWh basis.

(3) Mr. Kollen recommends that the retirement rider rates be reset to recover deferred costs along with any necessary true-up for the difference in revenues versus allowed recoveries in each base rate proceeding until the costs are fully recovered. The rider would expire by its own terms once all retirement costs and the true-up are fully recovered.

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10. Refer to the Baron Testimony, Exhibits (SJB-3), (SJB-4), and (SJB-5). Provide an electronic copy in Excel spreadsheet format of each of the cost-of-service studies that support these Exhibits with the formulas intact and unprotected and with all columns and rows accessible.

RESPONSE:

See attached.

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11. Refer to the Direct Testimony of Mary Jean Riley, page 5. a. The Testimony states, "One of the most sensitive pieces of electrical equipment is the static var compensator (SVC) unit which NAS was required by (sic) to install." State who required North American Stainless ("NAS") to install the SVC. b. Explain how the penalty measurement change from kW to KVA resulted in a greater risk of NAS incurring compliance penalties. c. State the number of times that NAS had to power the SVC up and down because of a curtailment request by KU in calendar years 2012, 2013, and 2014.

**RESPONSE:**

Due to scheduling issues, this question will be answered as soon as reasonably possible.