COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

IN THE MATTER OF: THE APPLICATION OF KENTUCKY UTILITIES COMPANY FOR CERTIFICATES OF PUBLIC CONVENIENCE AND NECESSITY AND APPROVAL OF ITS 2016 COMPLIANCE PLAN FOR RECOVERY BY ENVIRONMENTAL SURCHARGE	: : : : :	**Case No. 2016-00026**

KENTUCKY INDUSTRIAL UTILITY CUSTOMERS, INC.'S RESPONSE TO THE COMMISSION STAFF'S REQUEST FOR INFORMATION

1. **Refer to the Direct Testimony of Lane Kollen ("Kollen Testimony"), page 5, lines 1-5, which states, "I recommend that the Commission reject KU's [Kentucky Utilities Company's] request for approval of Project 39 included in its 2016 Compliance Plan and, if it is approved, reject recovery of the costs of this project through the ERC [environmental surcharge recovery] over a four-year amortization period. KU Project 39 involves surface impoundment closures at Green River, Pineville, and the Tyrone, all of which are retired and no longer operating."**

    a. **Explain whether coal-fired power plants that are being shuttered, regardless of reason, under current environmental compliance regulations would, or would not, be allowed surface impoundment closure costs to be recovered through the ECR; explain also how would those plants' surface impoundment closure costs and recovery differ from those of the Green River, Pineville, and Tyrone plants.**

    b. **Explain in detail why you recommend that the Commission reject the four-year amortization period proposed by KU.**

    c. **Explain the rationale for and consequences of utilizing a ten-year amortization period, which you recommend, versus the four-year amortization period proposed by KU.**

RESPONSE:

a. The determining factor is whether the proposed project meets the requirements set forth in KRS 278.183 either for approval in a compliance plan or recovery through the ECR. To be recoverable in the ECR, project costs must be incurred pursuant to an "environmental requirement." Environmental costs that are discretionary cannot be recovered in the ECR. Discretionary environmental costs are recoverable in base rates.

The statute authorizes environmental surcharge recovery of approved projects only if the costs are incurred pursuant to the "Federal Clean Air Act as amended and those federal, state, or local environmental requirements which apply to coal combustion wastes and by-products from facilities utilized for production of energy from coal in accordance with the utility's compliance plan as designated in subsection (2) of this section." Subsection 2 requires the utility to "submit to the Commission a plan . . . for complying with the applicable environmental requirements set forth in subsection (1) of this section." Subsection 2(a) states the Commission shall conduct a hearing to "consider and approve the plan and rate surcharge tithe Commission finds the plan and rate surcharge reasonable and cost-effective for compliance with the applicable environmental requirements set forth in subsection (1) of this section." (emphasis added). If the proposed project does not meet the requirements for approval in a compliance plan or recovery through the ECR, the utility nevertheless may proceed with the project and seek recovery of the costs through the base ratemaking process.

b,c. There are several reasons why Mr. Kollen opposes KU's proposal to recover the estimated costs over four years. The first reason is that there is no legal requirement to incur the costs. The second reason is that the costs are not known and measurable. They are estimated. It is not necessary to estimate these costs. Under Mr. Kollen's proposal, the actual costs would be deferred. The third reason is that, at least initially, revenues would exceed the costs incurred for actual impoundment closure activities. The excess recoveries would be considered taxable income and would cause income tax payments and an asset ADIT in rate base. This additional cost to customers is unnecessary and is solely the result of KU's proposal to prematurely recover the estimated costs before they are incurred. The fourth reason is that the four year amortization period is arbitrary and unnecessarily short. The recovery period does not have to match the period over which the projected costs are incurred and there no longer is any remaining physical service life. Thus, the amortization period is subjective and can be longer in order to mitigate the effects on customers. Mitigation is appropriate because customers will pay for the costs of impoundment pond closures as well as the cost of new construction at the at the active and operating plant sites.

2. Refer to the Kollen Testimony, page 10, lines 11-14, which states, "Although Mr. Spanos did not provide the depreciation rates resulting from the KU proposal, instead showing only the annual depreciation expenses, the proposed depreciation rates for Tyrone, Green River, and Pineville are 569.24 percent, 775.57 percent, and 2,193.86 percent, respectively." Provide the numerical calculation by plant for each of the depreciation percentages.

<u>RESPONSE:</u>

Please see attached.

3. Refer to the Kollen Testimony, page 14, line 21 through page 16, line 9, and Exhibit LK-6. Provide an ECR - Gross-up Revenue Factor & Composite Income Tax Calculation using the format and calculations contained in Exhibit LK-6, but include the Internal Revenue Code §199 manufacturing tax deduction for KU.

RESPONSE:

Please see attached. The calculation results in a combined federal and state income tax rate of 35.69%. The 35.516% rate stated on page 15 line 12 of Mr. Kollen's testimony should be corrected to the 35.69% calculated on the attachment.

Respectfully submitted,

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Q. #2 Attachment

KENTUCKY UTILITIES COMPANY

Account	Location	Plant in Service	Cost of Removal		Depr Exp Accrual	Depr Rate
RETIRED PLANTS						
312	**Boiler Plant Equipment**					
	Tyrone 3	575456	13,103,000	4.0	3,275,750	569.24%
	Green River 3	1831841	56,829,000	4.0	14,207,250	775.57%
	Pineville 3	91266	8,009,000	4.0	2,002,250	2193.86%
	Total	2,498,563	77,941,000		19,485,250	779.86%

Q. #3 Attachment

ECR - Gross-up Revenue Factor &
Composite Income Tax Calculation
Including Federal Section 199 deduction

(1 Assume pre-tax income of	$100.00	
(3) State income tax (see below)	5.64	
(5) Taxable income for Federal income tax		
(6) before production credit	94.36	(1)-(3)
(7) a. Production Rate	9.00%	
(8) b. Allocation to Production Income	100.00%	
(9) c. Allocated Production Rate (a x b)	9.00%	
(11) Less: Production tax credit	8.49	(6)*(9)
(13) Taxable income for Federal income tax	85.87	(6)-(11)
(15) Federal income tax	30.05	(13)*35%
(I8) Total State and federal income taxes	35.69	(3)+(15)
(20) Gross-up Revenue Factor	64.31	100-(18)