

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In The Matter of:

Electronic Application of Kentucky Power)	
Company For (1) A General Adjustment of Its)	
Rates for Electric Service; (2) An Order)	
Approving Its 2017 Environmental Compliance)	CASE No.
Plan; (3) An Order Approving Its Tariffs and)	2017-00179
Riders; (4) An Order Approving Accounting)	
Practices to Establish a Regulatory Asset or)	
Liability Related to the Big Sandy 1 Operation)	
Rider; and (5) An Order Granting All Other)	
Required Approvals and Relief)	

POST-HEARING BRIEF
OF THE KENTUCKY ATTORNEY GENERAL

Respectfully submitted,

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ATTORNEY GENERAL’S POST-HEARING BRIEF

Comes now the intervenor, the Attorney General of the Commonwealth of Kentucky, by and through his Office of Rate Intervention, and states as follows for his post-hearing brief in the above-styled matter.

STATEMENT OF THE CASE

On April 26, 2017 Kentucky Power Company [“KPCo” or “Company”] filed its notice of intent seeking permission, *inter alia*, to increase its base rates. The instant case thus marks the first rate case since Case No. 2014-00396, wherein the Commission approved the Big Sandy Retirement Rider,¹ and the Big Sandy 1 Operating Rider. The company’s application, utilizing a historic test period ending February 28, 2017 was filed on June 28, 2017. Due to deficiencies in the company’s application, the Commission deemed the application filed as of July 20, 2017.

¹ KPCo now seeks to rename this rider the “Decommissioning Rider.”

On August 7, 2017 KPCo filed an amendment to its application to reflect reduced debt cost resulting from the June, 2017 refinancing of the company's long-term debt. As a result of that refinancing, KPCo reduced the amount of additional revenue sought in the instant case from the original \$65.672 million to \$60.397 million, which included a proposed 15.03% increase in residential base rates.²

Seven parties were granted intervention and four were denied.³ On November 22, 2017, KPCo filed documents in support of a non-unanimous settlement it had reached with KIUC, KLC, KSBA, KCTA and Wal-Mart. The non-unanimous settlement recommends that the Commission approve \$31.79 million in new revenues, which includes a 14.15% increase in non-fuel residential base rates.⁴ The Attorney General and KCUC did not join in the non-unanimous settlement. The final evidentiary hearing was held on December 6, 7 and 8, 2017.

ARGUMENT I: KPCo's Existing Rates Are Unaffordable and the Company Has Failed to Justify its Request for an Increase

1. Courts Have Upheld the Consideration of Affordability in Prior Cases

*"I am retired, live alone, and live month to month on Social Security. I cannot sustain another increase on my power bill. I am on the [] budget plan and pay \$262.00 a month which leaves me with barely enough to pay my other bills and buy groceries. I keep the thermostat on 60° F and wear a jacket in the house to stay warm."*⁵ -- Bradora C. Plummer

In *Nat'l-Southwire Aluminum Co. v. Big Rivers Elec. Corp.*, 785 S.W.2d 503 (Ky.App.1990), the Court of Appeals upheld the Commission's consideration of affordability

² KPCo Supp. Response to Staff 1-73 filed Aug. 28, 2017, attachment 97, updated COSS 8-28, tab Sheet 1.

³ The parties denied intervention were: International Brotherhood of Electrical Workers Local Union 369; Progress Metal Reclamation Company d/b/a Mansbach Metal Company; Riverside Generating Co., LLC; and Community Action of Kentucky.

⁴ Satterwhite Amended Testimony filed Nov. 30, 2017, Settlement Agreement Exhibit MJS-1S.

⁵ Public Comment from Bradora C. Plummer, as read into the record by Chairman Schmitt, Dec. 8 Video Transcript of Evidence ["VTE"] at 11:59:55–12:01:00.

when it, *sua sponte*, created a unique variable utility rate tied to market prices of aluminum. In that case, two aluminum smelters, which consumed large quantities of power and employed hundreds of employees, were facing a crisis the court characterized as “monstrous.”⁶ The smelters were faced with potential shut-downs due to falling world aluminum market prices if relief could not be obtained to make power bills more affordable. As the Court noted, the variable rate the Commission itself created:

“ . . . [w]as designed to require the smelters to pay more for electricity when aluminum prices are high, when they likely can **afford** to pay more. The variable rate will protect the smelters from high production costs when aluminum prices are low. . . . By selling 70 percent of its output to NSA and Alcan, Big Rivers is definitely linked to the aluminum business. The fortunes of the producer and the consumer are dependent on each other.”⁷

The *National-Southwire* court noted that “. . . the real goal for the PSC is to establish fair, just and reasonable rates,”⁸ and specifically affirmed the Commission’s creation of a rate designed to make power more affordable for two key customers,⁹ while also noting that “. . . it would be good to see more clear concern for the consumer.”¹⁰ The Commission-approved rates were effectively bound to the smelters’ margins, thus tying the rates they paid to the margins they earned and were able to pay.

The U.S. Supreme Court has also addressed the need to consider affordability in setting rates. In *Federal Power Comm’n v. Hope Nat. Gas Co.*,¹¹ the Court noted that in prior rulings, it has found that a rate setting Commission is “. . . not bound to the use of any single

⁶ *National-Southwire*, *supra*, at 506-509, 515.

⁷ *National-Southwire*, *supra* at 515 [emphasis added].

⁸ *Id.* at 513.

⁹ *Id.* at 517.

¹⁰ *Id.* at 513 (*see also* Wilhoit, Judge, concurring in part and dissenting in part, “Just as a utility should not be denied a fair return on its investment properly included in rate base, so a customer or consumer should not be required to pay for investments made by the utility which are of no benefit to the consumer.” *Id.* at 518).

¹¹ 320 U.S. 591, 64 S.Ct. 281, 88 L.Ed. 333 (1944).

formula or combination of formulae in determining rates. Its rate-making function, moreover, involves the making of ‘pragmatic adjustments.’¹² . . . Under the statutory standard of ‘just and reasonable’ it is the result reached not the method employed which is controlling.¹³ Moreover, in the ratemaking process, “the fixing of ‘just and reasonable’ rates, involves a balancing of the investor **and the consumer interests.**”¹⁴ This Commission is not limited solely to KPCo’s biased opinion of the “regulatory compact.” Rather, the Commission must balance all interests – including those of the consumer, which obviously is predicated upon the establishment of just rates which they are able to pay.

In *Kentucky Industrial Utility Customers, Inc. v. Kentucky Pub. Serv. Comm’n*, 504 S.W.3d 695 (Ky. App. 2016), the Court of Appeals found the Commission’s approval of a renewable energy production agreement [“REPA”] to be unreasonable because it was based on expressions of state and federal environmental policies,¹⁵ and failed to consider “. . . the reasonableness and fairness of the substantial rate increase Kentucky Power’s customers are being asked to bear over two decades for an additional 3% increased energy reserve.”¹⁶ While the REPA may have met the goals of KRS 154.27-020(2), nonetheless “. . . [f]airness, justness and reasonableness remain the determinative considerations.”¹⁷

In overruling the Commission’s approval of the REPA, the Court of Appeals further noted:

Kentucky Power, a retail electric supplier, has the “exclusive right to furnish retail electric service to all electric-consuming facilities located within its certified territory[.]” KRS 278.018. **This right strips consumers of the right**

¹² *Id.*, 64 S. Ct. 281 at 287 (citing *Federal Power Commission v. Natural Gas Pipeline Co.*, 315 U.S. 575, 586, 62 S. Ct. 736, 743, 86 L.Ed. 1037).

¹³ *Id.*, citations omitted.

¹⁴ *Id.*, 64 S. Ct. 281, 288 [emphasis added].

¹⁵ 504 S.W.3d at 707-708.

¹⁶ *Id.* at 708.

¹⁷ *Id.* at 707.

to price shop for the most affordable electric rates. Consumers of public utilities must rely on the Commission to protect them from unreasonable and unfair rates. “Because utilities are allowed to charge consumers only ‘fair, just, and reasonable rates’ under KRS 278.030(1), **the [Commission] must ensure that utility rates are fair, just, and reasonable to discharge its duty under KRS 278.040 to ensure that utilities comply with state law.**”¹⁸

Additionally, the Court of Appeals noted seven key facts established at the hearing, which included, *inter alia*: (i) if the REPA was approved, the average residential customer in the first year would experience a 5.9% to 7% rate increase but in subsequent years the increase could go as high as 13%; and (ii) KPCo did not conduct any economic or cost-benefit analyses to determine whether the price at which it entered into for the REPA would be, in the long-term, economical.¹⁹ The Court further noted that while KPCo failed to provide an economic justification for the REPA, the petitioner, KIUC, did present evidence regarding the REPA’s economic impact,²⁰ and that:

“None of the Commission’s findings relate specifically to the REPA at hand or the reasonableness and fairness of the substantial rate increase K[PCo]’s customers are being asked to bear over two decades for an additional 3% increased energy reserve. [KPCo] **failed to put forth any evidence** as to how the REPA compared to other renewable sources of energy or even other similar biomass contracts. It also failed to perform any analysis to estimate the reasonableness of the costs under the REPA for years two through twenty. In fact, there was no evidence put before the Commission that the REPA would result in a direct or indirect economic benefit for K[PCo]’s customers or the region as a whole. . . . The Commission still has a duty to insure that the rate increase that is being imposed on customers is fair, just and reasonable.”²¹

Finally, the *Kentucky Industrial Utility Customers, Inc.* Court noted that under its ruling in *National Southwire, supra*:

¹⁸ *Id.* at 705 (quoting *Kentucky Pub. Serv. Comm’n v. Com. ex rel. Conway*, 324 S.W.3d 373, 377 Ky.2010)) [emphasis added].

¹⁹ *Id.* at 708.

²⁰ *Id.*

²¹ *Id.*[emphasis added].

We explained that “[o]ur Court’s role is also to insure that the conflicting interests of all parties concerned with utility rates are fairly balanced. If the PSC accomplishes this, we have no reason to substitute our judgment or reverse the PSC . . . The problem in this case is that the Commission failed to fairly balance the competing interests. . . . While the Commission was entitled to give some positive weight to the fact that this was a biomass facility, **it was still required to consider other factors such as the reasonableness of the costs in comparison with other alternatives.** While the statute *allows* the Commission to consider the policy objectives of KRS 154.27–020(2), it mandates that the Commission consider whether the full costs of the power agreement over the full term of the agreement are fair, just and reasonable. **The Commission’s failure to do so represents a complete abdication of its statutory responsibility to ensure that the rates for public utilities in this Commonwealth remain “fair, just and reasonable.”**²²

The Court of Appeals made it abundantly clear that the reasonableness of costs as it relates to the consumer -- *affordability* – is a key factor the Commission *must* take into consideration when ruling upon whether rates are fair, just and reasonable. In fact, in coming to its conclusion, the Court took notice that customers residing in the twenty counties comprising KPCo’s service territory live either at or below the poverty line, and that the costs at issue in that case would cause economic harm to the service territory.²³ The Court thus concluded that, **“[i]n no way, shape or form can we accept that the General Assembly intended the citizens of this Commonwealth to shoulder this type of burden. Given the facts, we must conclude that it was unreasonable for the Commission to approve Kentucky Power’s application.”**²⁴

In the instant case, it is not merely one or two customers facing a crisis, but the largest class of ratepayers – residentials -- who are facing a “monstrous” crisis. As set forth in the testimony of Attorney General witness Dr. David E. Dismukes, between 2006 and 2014,

²² *Id.* at 709 [italicized emphasis in original, bolded emphasis added].

²³ *Id.*

²⁴ *Id.* [emphasis added].

KPCo has increased the residential energy charge 48.45% and the customer charge by 87.71%.²⁵ If approved, the non-unanimous settlement²⁶ would increase those figures to 71.03% for the residential energy charge and 138.9% for the residential customer charge, since 2006.²⁷

Moreover, KPCo ratepayers currently pay a *far higher* percentage of their monthly gross income for their electric utility bill than do electric customers of the other three investor-owned electric utilities [“IOUs”] in the Commonwealth: Kentucky Utilities, Duke (Kentucky) and Louisville Gas & Electric. As set forth in KPCo’s response to AG 1-13,²⁸ residential customers of these three other IOUs utilizing 1000 kWh per month pay an average of \$96.63, whereas a KPCo residential customer with the same usage pays \$132.71 under *current* rates, or 37.33% more than the average IOU customer. Considering the *average* monthly household wages in Eastern Kentucky of \$3097, KPCo residential customers pay 4.29% of their income for electric service, while a comparable customer of Kentucky’s other IOUs on average pay only 2.52% -- a difference of nearly 70% more than the latter.²⁹ But this major differential applies only to *existing* rates. If the new revenues set forth in the non-unanimous settlement are taken into effect, that same average KPCo residential customer will be paying significantly more of his income to KPCo. Even more importantly, these percentages are only part of the story as they are based merely on the *average* monthly income

²⁵ Dr. David E. Dismukes Direct Testimony, pp. 7-8, and exhibit DED-3.

²⁶ See Exhibit AEV 3S, filed November 30, 2017.

²⁷ Figures are based on the increases proposed in the non-unanimous settlement, and upon historical data provided in Dr. David E. Dismukes Direct Testimony, pp. 7-8, and Exhibit DED-3; and Exhibit AEV 3S, filed November 30, 2017.

²⁸ KPCo_R_AG_1_13_Attachment1.xls, tab “AG 1-013b.”

²⁹ Over the 12-month period ending the 2nd quarter of 2016, assuming 1000 kWh per month usage. Sources: Dismukes Direct Testimony pp. 10-11, exhibit DED-2; and workpapers of Dr. David E. Dismukes provided in response to KPCo’s data requests to the Attorney General, item no. 5, attachment DED-1_DED-2_KY_Labor_Market_Data_FINAL.xlsx, “Labor Market Data” tab, columns B and D.

for Eastern Kentucky; when low-income customers are considered, the effect is even *more* stark.

KPCo's ratepayers are captive to these increases, and have no ability to shop for a rate they can afford. *Only* the Commission can protect them from "unreasonable and unfair rates."³⁰ Given the disastrous economic conditions in Eastern Kentucky, residential ratepayers have no choice but to depend on the Commission to "ensure that utility rates are fair, just and reasonable."³¹ The time is now for the Commission to show "more clear concern for the consumer"³² by denying the entirety of the proposed increase for residential customers.

2. KPCo's Ratepayers Cannot Afford Yet Another Rate Increase

*"Please no more rate hikes. I get 465.00 a month to live on. I would be better off dead. I am only existing, not living. My life should be better than this in a country so rich."*³³-- Margie Prater

The Commission's mission statement provides that its mission is to, ". . . foster the provision of safe and reliable service at a *reasonable* price to the customers of jurisdictional utilities while providing for the financial stability of those utilities by setting *fair* and *just* rates, and supporting their operational competence by overseeing regulated activities."³⁴ KRS 278.030 (1) requires the Commission to set rates that are "fair, just and reasonable." However, these terms are not defined in KRS Chapter 278, nor anywhere else in the Kentucky Revised Statutes. Nonetheless, available to the Commission in this case is testimony reflecting several key metrics that can be used to determine whether rates are fair and just.

The testimony of Roger McCann, Executive Director of Community Action Kentucky,

³⁰ *Kentucky Industrial Utility Customers, Inc.*, *supra* at 705.

³¹ *Id.* at 705 (quoting *Kentucky Pub. Serv. Comm'n v. Com. ex rel. Conway*, 324 S.W.3d 373, 377 (Ky.2010)).

³² *National-Southwire*, *supra* at 513.

³³ Public Comment submitted into the record from Margie Prater, as read by Chairman Schmitt, Dec. 8, 2017 VTE at 12:01:17–12:01:32.

³⁴ <https://psc.ky.gov/Home/About#AbtComm> [emphasis added]

Inc., and Dr. David E. Dismukes provide illustrations of several key metrics which together demonstrate that KPCo ratepayers cannot pay the rates currently in effect, before considering any proposed increase.

If the Commission accepts the terms in the non-unanimous settlement, KPCo residential customers will have seen a **71% increase** in their energy charge, and a **139% increase**³⁵ in their monthly customer charge over the past four rate cases³⁶ and a doubling of bills for the average residential customer since 2005.³⁷ Constant increases in utility bills have a negative impact on economic growth because it precludes the ability of customers to afford other life-sustaining needs and services.

Second, the twenty counties located within KPCo's service territory have some of the highest poverty rates in the Commonwealth, with an average poverty rate of 30.19%.³⁸ The poverty rate in eighteen of those counties exceeds 20%, which the U.S. Census Bureau defines as "extremely high."³⁹ Nineteen of those counties report poverty rates in excess of Kentucky's overall 18.3% poverty rate.⁴⁰ These counties rank as some of the poorest in the U.S., in a state that ranks 47th in highest poverty rates.⁴¹ Of KPCo's 136,344 residential customers,⁴² an estimated 35,755 (or 26.22% of all of its residential customers) live in poverty.⁴³ Of all the children living in the counties comprising KPCo's service territory, approximately 37% live

³⁵ Figures are based on the increases proposed in the non-unanimous settlement, and upon historical data provided in Dr. David E. Dismukes Direct Testimony, pp. 7-8, and Exhibit DED-3; and Exhibit AEV 3S, filed November 30, 2017.

³⁶ Dr. David E. Dismukes Direct Testimony, Exhibit DED-3.

³⁷ Dr. David E. Dismukes Direct Testimony, pp. 10-12, assuming 1,295 kWh of usage per month.

³⁸ Roger McCann Direct Testimony, p. 7.

³⁹ *Id.*

⁴⁰ *Id.*

⁴¹ *Id.*

⁴² KPCo response to AG 2-1 Attachment 1, Column D Total.

⁴³ McCann Direct Testimony, p. 7.

in households below the poverty line.⁴⁴ As pointed out in the testimony of Attorney General witness Roger McCann:

*“By definition, families with incomes at or below the poverty line cannot meet their basic needs. . . . [f]or a senior citizen on a fixed income, utility service is not only a basic need, it is a **survival need**. With more money needed for utilities, there is less money for other basic needs like food, housing, medication, and other necessities. The energy assistance needs cited above represent the current situation (based on existing KPCo rates). With any rate increase at all, the affordability gap will greatly widen.”⁴⁵*

In addition to the prevalence of poverty, the high unemployment rates in Eastern Kentucky form a second metric in considering the affordability of KPCo rate. As depicted in the testimony of Dr. David E. Dismukes, employment in the Commonwealth as a whole experienced significant loss due to the 2008 recession, but recovered in the fourth quarter of 2014.⁴⁶ However, job loss in Eastern Kentucky was greater than the state as a whole, and has yet to recover. In fact, Eastern Kentucky employment is still 15.5% lower than levels just prior to the recession.⁴⁷ Additionally, Eastern Kentucky has historically reported average earnings 10%-20% lower than the state as a whole.⁴⁸ Eastern Kentucky was starting to see a closing of that differential, but over the past several years, that progress has eroded and the earnings differential has again expanded to 20% lower than the statewide average.⁴⁹

⁴⁴ Source: U.S. Census Bureau Small Area Income and Poverty Estimates, “Table” tab, accessible at: https://www.census.gov/data-tools/demo/saipe/saipe.html?s_appName=saipe&map_yearSelector=2016&map_geoSelector=aa_c&menu=map_proxy

⁴⁵ McCann Direct Testimony at pp. 8-9 [italicized and bolded emphasis in original]. As an example of inability to meet basic needs, one Letcher County ratepayer stated that she knew of another KPCo customer, 85 years old, who attended the same church for 50 years and faced a \$700 KPCo power bill almost every month. She could not afford to connect her hot water heater, and even had to boil water on her stove in order to take a bath. Because she could not afford her bill or groceries, she recently had to move to another town to live with family members. Now she is no longer able to attend the church that she has been an integral part of for 50 years, all because of the high cost of her electric bill. Public Hearing in Hazard, Elizabeth Jones Public Comment, VTE at 1:30:12–1:30:54.

⁴⁶ Dr. David E. Dismukes Direct Testimony, p. 5, and exhibit DED-1.

⁴⁷ *Id.*

⁴⁸ *Id.* at pp. 5-6.

⁴⁹ *Id.* at p. 6.

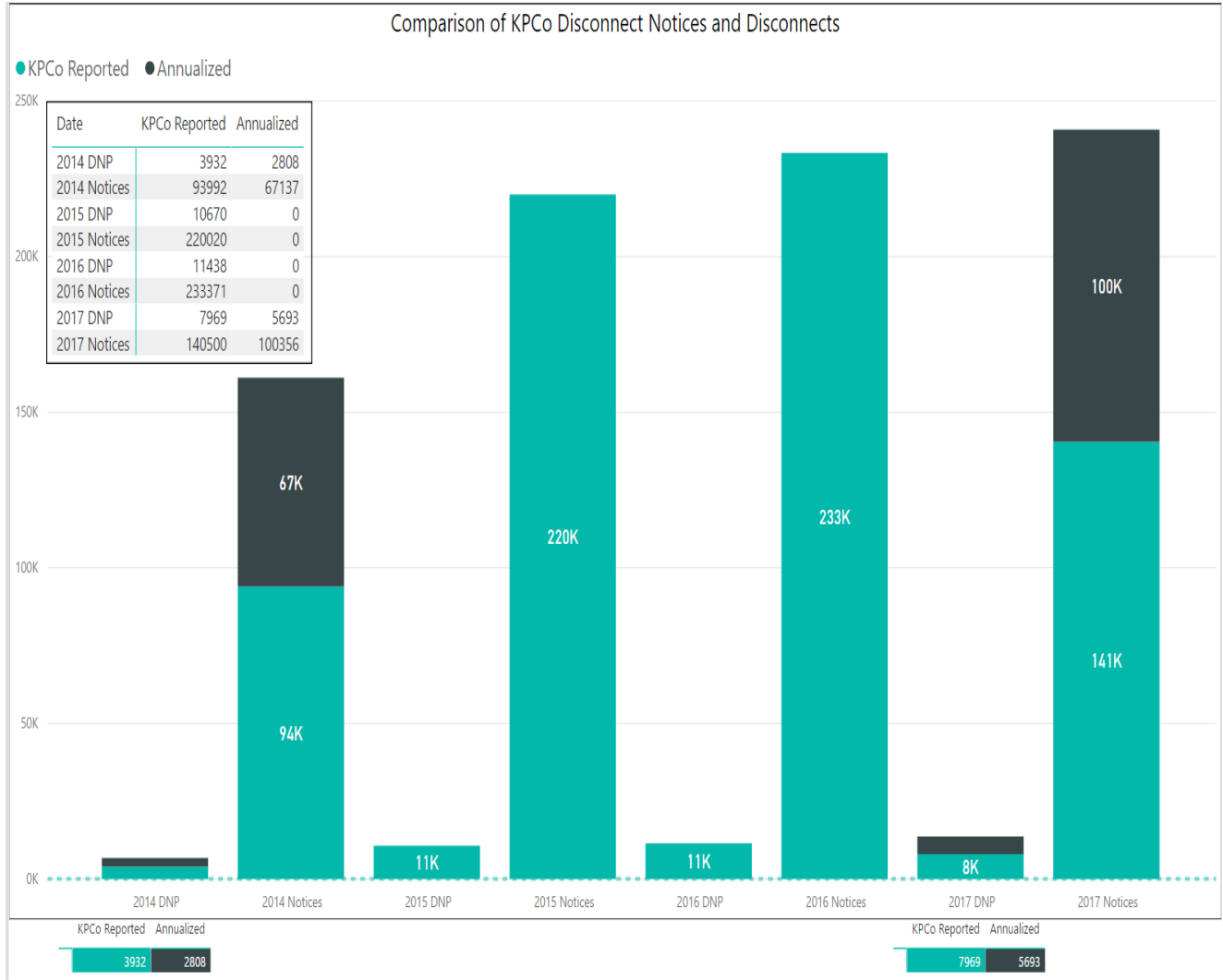
The third metric is the level of disconnect notices compared with actual disconnections. Significantly, although the Commission requires utilities to file reports of disconnections for nonpayment, this data is not publicly available. This data was provided in response to the Attorney General’s discovery requests.⁵⁰ While the number of disconnection notices – nearly *double* the number of actual residential customers – is disturbing by itself, it is far more troubling that the number of actual disconnections for 2017, as depicted in the chart below,⁵¹ is on pace to exceed the level established in 2015 and 2016. This high level of disconnects is a burden for both ratepayers and the company itself, which is forced to spread costs associated with disconnects among its other ratepayers. As one ratepayer who has experienced multiple disconnects commented during the public comment hearing in Hazard, “I can’t pay my electric bill and I have to pay rent . . . we’ve lived in the dark before, we can do it again.”⁵²

[CONTINUED ON FOLLOWING PAGE]

⁵⁰ See, e.g., KPCo Responses to AG 2-1 – 2-13.

⁵¹ *Id.* at pp. 11-12; source: KPCo response to AG 2-4 Attachment 1 and AG 2-10 Attachment 1.

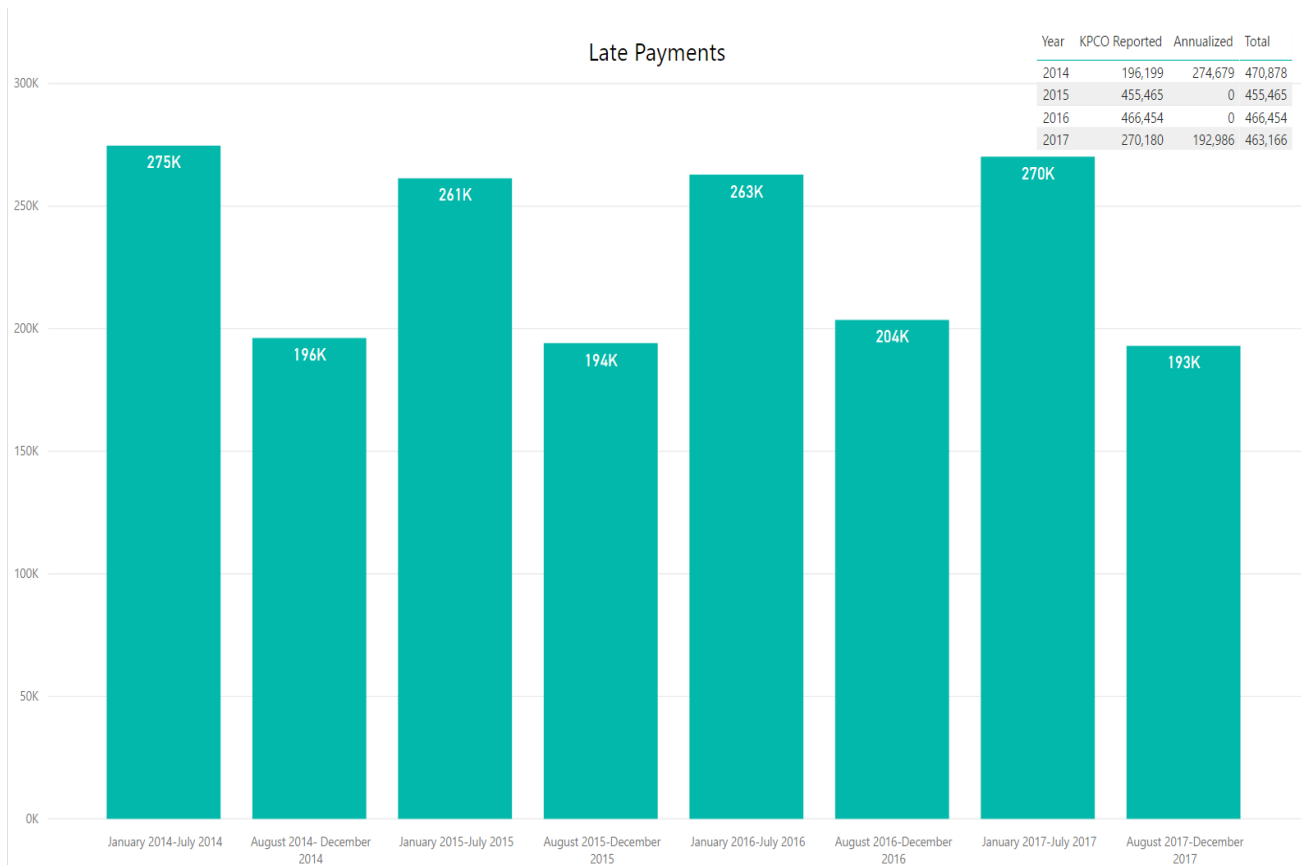
⁵² Public Hearing in Hazard, KY, Alice Craft Public Comment, VTE at 1:17:50–1:18:23.



Moreover, the number of accounts receiving *multiple* disconnects has steadily increased over the 2014 to 2017 timeframe. In 2015, 1,386 customers had two or more disconnects, which increased to 1,469 customers in 2016. In the first seven months of 2017, 933 accounts had two or more disconnects. If that pace of disconnects continues, by the end of 2017 approximately 1,600 customers will have received multiple disconnects. This amounts to an 8.2% increase year-over-year.⁵³

⁵³ KPCo Response to AG 2-4, KPCo_R_AG_2_4_Attachment 1.

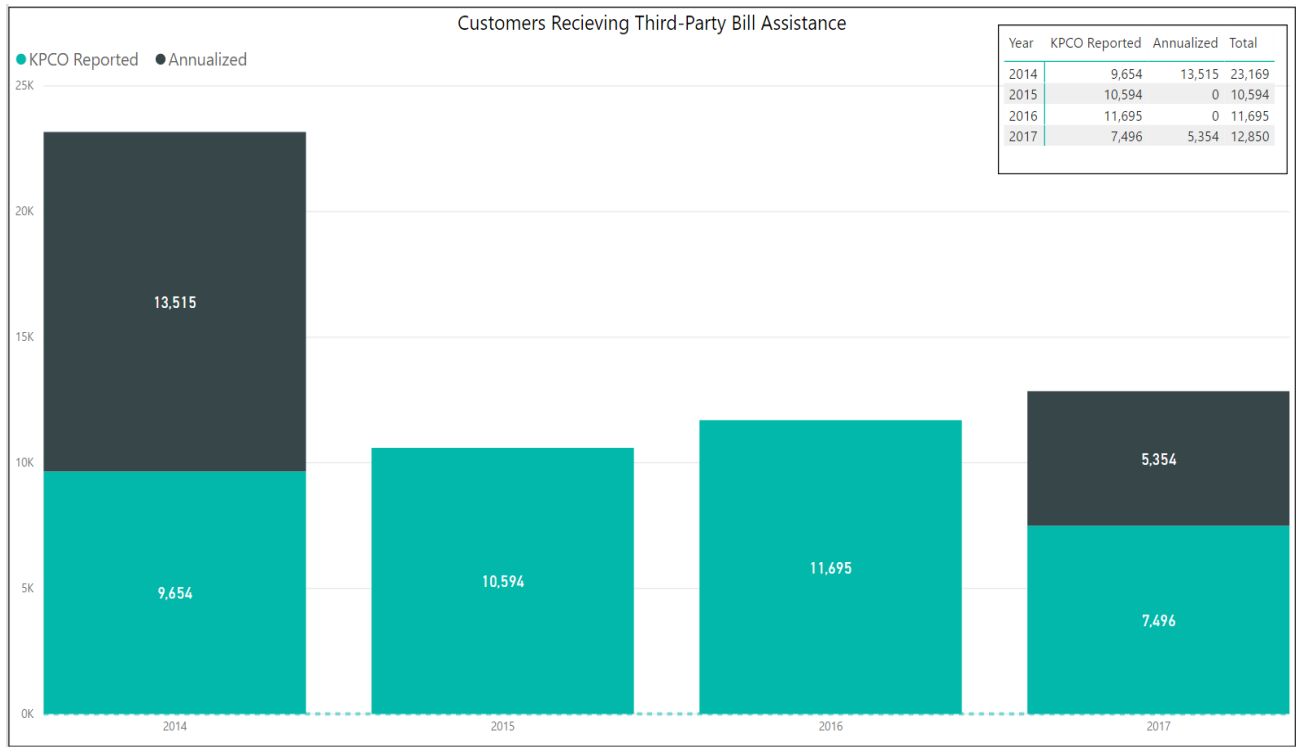
The fourth metric illustrating the inability of KPCo residential customers to pay their current rates is the number of late payments in each of the years 2014 through July 31, 2017. As the chart below depicts, KPCo had well-in excess of *1 million* late payments over that period:⁵⁴



Given that approximately 26% of KPCo’s residential customers live below the poverty line, it should come as no surprise that a significant number of them receive bill paying assistance from a third-party agency.⁵⁵ This fifth metric is depicted in the following graph:

⁵⁴ KPCo Response to AG 2-3 and KPCO_R_AG_2_3_Attachment1.xlsx.

⁵⁵ KPCo Response to AG 2-11 and KPCO_R_AG_2_11_Attachment1.xls.



Taken together, these five metrics provide solid, objective evidence upon which this Commission must rely to find that KPCo’s residential ratepayers cannot afford the proposed rate increase set forth in the non-unanimous settlement because they cannot afford to pay their bills today. KPCo customers merely want affordable, reliable electric service, something the Company is either unwilling or unable to provide. Any proposed increase would produce rates that are unfair, unjust and unreasonable pursuant to KRS Ch. 278.

3. KPCo Failed to Satisfy its Burden to Justify the Increase

“Last year alone, we had at least fourteen (14) fires in Breathitt County that were caused by old heating stoves and stuff because they couldn’t afford to turn on their electric furnaces and they had to go back to the old coal stoves and the old coal furnaces and wood furnaces. And it wasn’t safe in mobile homes and some of the homes they were living in. They lost everything to fires.”⁵⁶-- Rose Wolf, Mayor of Jackson

Utilities seeking increases in rates bear the burden of proving that the proposed

⁵⁶ Public Hearing in Hazard, KY, Mayor of Jackson, Rose Wolf Public Comments, VTE at 54:58–55:50.

increase is just and reasonable. KRS 278.190 (3) provides:

At any hearing involving the rate or charge sought to be increased, **the burden of proof to show that the increased rate or charge is just and reasonable shall be upon the utility**, and the commission shall give to the hearing and decision of such questions preference over other questions pending before it and decide the same as speedily as possible, and in any event not later than ten (10) months after the filing of such schedules.

During cross examination KPCo witnesses were repeatedly asked whether the company had conducted any studies, reports, analyses or provided any information regarding whether the proposed rate increases were affordable, and each one responded that no such studies or analyses were conducted.⁵⁷ One of the final such answers was illustrative of this point, as Mr. Vaughan noted that “I have no specific economic or other studies done about the affordability of the rates. . .”⁵⁸ The Company’s dismissive nature when pressed about what studies or analyses it has conducted regarding the affordability of any proposed increase is interesting provided their past experiences. Whereas KPCo in *KIUC, supra* was criticized by the Court for failing to meet its burden to justify the economic necessity of the REPA, nonetheless the Company in 2017 utilized *extensive* economic data, including employment and income rates of its residential customers, to seek preferential utility rates for businesses involved in coal processing.⁵⁹ For the Company to now argue against considering economic data of distressed populations in determining whether the rates paid by residential customers are fair, just and reasonable, when they have already used the same data to request (and receive) preferential rates for an entirely different class, is disingenuous at best.

⁵⁷ See, e.g., VTE Dec. 6, 11:36:00 – 11:38:47; 12:09:28 – 12:10:16; Dec. 7, 10:36:40 – 10:40:59; 4:24:56 – 4:26:36; 5:15:32 – 5:16:03; Dec. 8, 1:58:36 – 1:59:13; 3:28:19 – 3:29:38; 4:14:45 – 4:15:29.

⁵⁸ VTE Dec. 8, 3:28:19.

⁵⁹ Case No 2017-00099, Application pp. 8-9.

It is apparent from the record that KPCo witnesses have summarily concluded *in their own mind* that the requested revenue increases are reasonable, but nowhere in the record has any evidence been introduced showing that the increase is affordable for its residential customers. Just as KPCo failed to produce any evidence regarding whether its customers could afford the cost of the REPA in *Kentucky Industrial Utility Customers, supra*, KPCo has once again failed to meet its burden to prove that the requested new rates are just and reasonable. Therefore, its request to establish new rates must be denied.

ARGUMENT II: The Commission Should Use the Following Adjustments as an Additional Basis for Rejecting the Increases Set Forth by the Company in its Application and the Non-unanimous Settlement

1. Return on Equity

The non-unanimous settlement into which KPCo entered seeks a return on equity [“ROE”] of 9.75%. Although this a significant reduction from the outrageous return the company sought in both its direct and rebuttal testimony (10.23%), nonetheless it remains greatly in excess of the return shareholders require.

Two intervening witnesses testifying to the proper return on equity in this case recommended a far lower return. Dr. Woolridge, testifying on behalf of the Attorney General, testified that a proper return would be 8.6%,⁶⁰ while Mr. Rick Baudino, on behalf of KIUC testified that the ROE should be 8.85%.⁶¹ Dr. Woolridge testified that his recommendation was based chiefly on the fact that actual interest rates have been falling, and capital costs have been low.⁶² In support of his recommendation, during the hearing Dr. Woolridge noted that

⁶⁰ See generally Dr. J. Randall Woolridge Direct Testimony.

⁶¹ See generally Rick Baudino Direct Testimony.

⁶² VTE Dec. 7, 11:26:22.

a utility in Illinois, Ameren, had just been awarded an ROE of 8.4%.⁶³ Of course, as Mr. McKenzie agreed, Ameren competes with other companies such as Kentucky Power/AEP within the same capital market (U.S. Stock and Bond Markets).⁶⁴ Apparently, Ameren's regulator is confident an 8.4% ROE is sufficient to meet investors' expectations -- the same investors who would consider investing in KPCo. Of course, it is readily possible to determine whether capital markets have faith in KPCo's ability to operate and that is by examining the outcome of its involvement in capital markets. As evidenced by KPCo's updated application and testimony filed August 7, 2017, the company was able to refinance nearly \$400,000,000 at a *lower rate*.⁶⁵ KPCo was able to refinance its debt, all while the company had earned an ROE between 4.2% and "six-something" between 2014 and 2016.⁶⁶ If investors "required" an ROE in excess of 10%, then the Company would have likely not been able to refinance a large amount of debt at such a low rate, while earning a "paltry" return for shareholders. What is more likely is that KPCo, as all utilities seem to, chronically overstates its necessary ROE.

When asked whether his testimony supports a 9.75% ROE, KIUC's witness Mr. Baudino answered that it does not, and in fact his high-end is 9.55%.⁶⁷ Further, Mr. Baudino noted that he did not agree with i) Mr. McKenzie's incorporation of an outlook of capital costs, ii) Mr. McKenzie's use of forecasted interest rates in risk premium and CAPM analyses, iii) Mr. McKenzie's omission of low end DCF results, iv) Mr. McKenzie's use of the expected market return component of his CAPM or ECAPM analyses, v) Mr. McKenzie's application of the utility risk premium approach, vi) Mr. McKenzie's application of the expected earnings

⁶³ VTE Dec. 7, 11:25:00 – 11:26:03.

⁶⁴ VTE Dec. 7, 4:00:00.

⁶⁵ See Ranie K. Wohnas Supplemental Direct Testimony, August 7, 2017.

⁶⁶ VTE Dec. 8, 2:38:35.

⁶⁷ VTE Dec. 7, 2:22:00.

approach, and vii) Mr. McKenzie's application of the nonutility benchmark approach.⁶⁸ Regardless of KIUC's agreement to the non-unanimous settlement, its expert's testimony does not support the 9.75% ROE provided for within. In fact, not only do Mr. Baudino's numbers not support such an ROE, he finds significant fault with the analyses used by Mr. McKenzie, whose testimony is the only support in the record for such a generous return. Given the testimony of the two ROE witnesses for the Attorney General and KIUC, the Attorney General argues that it is appropriate for the Commission to award an ROE of 8.6%.

2. Adjustments the Commission Should Utilize to Reduce the Revenue Impact of the Application

Regardless of the fact that Kentucky Power customers cannot pay their current rates, or the fact that the Company has failed to consider whether customers can afford the proposed rates, the Company's Application does not bear up under scrutiny. The testimony of AG witness Smith provided evidence that the company has failed to provide adequate justification for adjustments of at least \$20M. Notably, none of Attorney General witness Smith's adjustments were incorporated in the non-unanimous settlement agreement. In addition to considering the reality of unaffordable rates, the Commission should use the Attorney General's adjustments as an additional basis for rejecting any rate proposal.

a. Decommissioning Rider ("Big Sandy Retirement Rider")

In Case No. 2014-00396, the Commission approved a new tracking mechanism designed to recover the approximately \$238.5 million in stranded costs resulting from the premature retirement of Big Sandy Unit 2, and infrastructure related to the usage of coal at Big Sandy Unit 1.⁶⁹ Under the terms of the Commission's final order in that case, the

⁶⁸ VTE Dec. 7, 2:23:15 - 2:31:15.

⁶⁹ The Big Sandy Retirement Rider, now known as the Decommissioning Rider.

approximately \$238.5 million in costs within the Decommissioning Rider [“DR”], previously known as the Big Sandy Retirement Rider, are being amortized over a period extending beyond twenty years. Those costs will also include carrying charges, which themselves will total in excess of \$225 million. The carrying charges include KPCo’s weighted average cost of capital [“WACC”], one component of which is the company’s long-term debt. By the time all costs within the DR have been paid, KPCo customers will have paid approximately \$463.6 million, almost one-half of which will have been carrying costs.

On August 7, 2017 KPCo filed an update to its application in this case to reflect the successful refinancing of its long-term debt. Based on the lower cost of its refinanced long-term debt, the company appropriately reduced the amount of its revenue requirement, for both its base rates and the costs it seeks to recover in its environmental surcharge mechanism. Seven (7) days after updating its application in the rate case, KPCo filed its annual update to the DR, which incorporated a WACC that used the pre-refinancing LTD rate. The Company should have requested Commission approval to pass through the savings to customers due to the refinancing, rather than reap the windfall benefit of the difference until it updated the overall rate in August of 2018.⁷⁰

As provided in the testimony of Attorney General witness Ralph C. Smith, the DR’s financing cost component is excessive and should be reduced as soon as practicable.⁷¹ Currently, KPCo customers are paying a levelized cost of \$1.68 million per month, each and every month through 2040. However, due to a shrinking ratebase, KPCo customers are paying even more as those costs become spread among remaining ratepayers.

⁷⁰ See Case No. 2014-00396, post case files, Aug. 14, 2017 update, document BSRR Support 1, tab WACC.

⁷¹ Ralph C. Smith Direct Testimony, pp. 63-66.

As a first step towards shielding KPCo's ratepayers from having to pay the DR's exorbitant financing costs, the DR should be adjusted to reflect the lower cost of debt, the lower cost of equity and the fact that the maximum corporate federal income tax rate has been reduced from 35% to 21%, effective January 1, 2018. The non-unanimous settlement utilizes a cost of long-term debt of 4.36%, a cost of short term debt of 1.25%, a cost rate for Accounts Receivable financing of 1.95% and an ROE of 9.75%. The WACC reflected in the Settlement is 6.48%, and the adjusted WACC with the income tax gross-up on the 9.75% ROE as adjusted for the 21% statutory federal income tax rate that is effective January 21, 2018 is 7.9227%, as summarized in KPCo's "Draft Forms Implementing the Partial Settlement Agreement."⁷²

The financing cost rate for the DR should be reduced to 7.9227% effective as of the same date as the effective date for KPCo new base rates. The reduction in the DR financing cost rate should not be postponed until the next DR reset (currently anticipated for August 1, 2018) because that would subject KPCo ratepayers to excessive financing costs for another 6 to 7 more months. If KPCo is allowed to continue to charge a carrying cost based on a long-term debt level that no longer exists, it will be unjustly enriched at the expense of its customers. Additionally, as a second step towards addressing the excessive financing costs associated with the DR, the Commission should investigate whether the remaining un-recovered balance which is being recovered over a 25-year period could be securitized. That could effectively reduce the financing cost rate to something in the range of 4% to 5%. AEP has effectively used securitization for some of its other electric utility operating companies,⁷³ as a cost

⁷² See KPCo_ES_Sample_Forms, and AEV-4S, as Adjusted for New Federal Income Tax Rate.

⁷³ See, e.g.: <http://www.aep.com/Newsroom/newsreleases/default.aspx?id=1265>

effective measure to address large deferred cost balances,⁷⁴ while minimizing the rate impact upon customers.

Furthermore, the Commission could require one or both of the following: (i) requiring AEP to write-down a portion of the principal amount owed in the DR; and/or (ii) reduce the carrying charges so that they reflect only the company's long-term debt instead of the existing WACC. If KPCo is indeed serious about economic development and making its rates more competitive with surrounding utilities, then it needs to recognize that its service territory needs the type of *extraordinary* relief that one or perhaps both of these measures would provide.

b. Savings Plan Expense

As set forth in Attorney General witness Smith's testimony, KPCo employees participating in the AEP 401K retirement savings plan are eligible to receive 100% matching contributions for each employee's first 1% of contributions of eligible compensation and 75% matching contributions for the next 5% of each employee's contributions of eligible compensation.⁷⁵ Mr. Smith's adjustment is based on recent Commission precedent wherein the Commission has disallowed Company matching contributions to 401(k) retirement savings plans for employees who also participate in other retirement plans, such as defined benefit pension plans.⁷⁶ Mr. Smith's adjustment removes \$1.102 million of KPCo's matching contributions.

⁷⁴ See:

<https://www.aep.com/about/IssuesAndPositions/Financial/Regulatory/AlternativeRegulation/Securitization.aspx>

⁷⁵ Ralph C. Smith Direct Testimony, pp. 39-42, Adjustment C-7. See also KPCo Responses to Staff 1-72 Attachment 1, and Staff 2-56 (h).

⁷⁶ See, e.g., In re: *Application of Kentucky Utilities for an Adjustment of Rates*, Case No. 2016-00370, Order dated June 22, 2017, pp. 14-15.

The Attorney General urges the Commission to continue to follow its precedent and remove \$1.102 million from operating income.

c. Salaries – Employee Merit Increases

As Attorney General witness Dr. David E. Dismukes illustrates in his testimony, average wages in Eastern Kentucky have been stagnating over the past decade, as compared with the rest of the Commonwealth.⁷⁷ Despite this, KPCo continues to award its employees annual salary increments in the range of 3.0% to 3.5%.⁷⁸ At a time when wages are stagnant across the area KPCo competes with employers for talent, it is not appropriate for the company to foist these costs onto the backs of its ratepayers due to its status as a monopoly.

d. Supplemental Executive Retirement Expense

Attorney General witness Ralph C. Smith proposed an adjustment to exclude expenses for supplemental executive retirement program [“SERP”].⁷⁹ SERPs are implemented for select executives and provide retirement benefits that exceed amounts limited in qualified plans by Internal Revenue Service regulations. Smith adjustment C-8 removes a total of \$58,726 from operating expense.

The Commission in Case No. 94-355, *In re Cincinnati Bell Tel. Co.*,⁸⁰ order dated May 23, 1995 allowed an adjustment in the sum of \$41,789 proposed by the Attorney General “. . . for SERP costs directly incurred by Cincinnati Bell because the Commission has previously removed from cost of service the cost of plans when benefits for highly

⁷⁷ Dr. David E. Dismukes Direct, p. 6, and Exhibit DED-2.

⁷⁸ Carlin Direct Testimony, p. 18.

⁷⁹ Ralph C. Smith Direct Testimony, pp. 42-43, Adjustment C-8.

⁸⁰ 1995 WL 421787.

compensated employees exceed the pension plan for all employees.”⁸¹ The Attorney General urges the Commission to adopt this adjustment.

e. Corporate Aviation Expense

Attorney General witness Ralph C. Smith proposed an adjustment to remove costs associated with AEP corporate aviation expense charged to KPCo from the AEP Service Company.⁸² KPCo’s response to AG 1-153 stated that for the test year, the company was charged \$388,356 in related O&M expenses. AEP travel logs, provided in response to KPSC-2-055, also indicated that the corporate planes are being used by AEP executives and directors, suggesting that the AEP corporate aircraft is an additional executive and director perquisite. As such, the cost of the AEP corporate aviation should be borne by shareholders, not by KPCo’s ratepayers.

Moreover, the Attorney General believes that most expenses associated with corporate aviation programs are an anachronism dating back to the pre-internet era. Today, many corporations conduct on-line and even satellite meetings in order to save expenses. The costs associated with maintaining “nine full time pilots employed by American Electric Power Service Corporation” is staggering, and is another example of exorbitant costs that ratepayers should not be forced to bear.⁸³

The Attorney General believes it is outrageous that at a time when the Company is aware that the level of its disconnections for nonpayment is increasing, nonetheless it expects its customers to pay these exorbitant aviation expenses. The Attorney General therefore urges

⁸¹ *Id.* at p. 8 (citing Case No. 90-158, *Adjustment of Rates of Louisville Gas and Electric Company*). See also Case No. 2000-00080, *In re Louisville Gas and Elec. Co.*, 2000 WL 1791791 (2000), order dated Sept. 27, 2000, p. 10 (“ . . . ADIT associated with LG&E’s SERP should be excluded from the rate base calculation.”).

⁸² Ralph C. Smith Direct Testimony, pp. 43-44, Adjustment C-9.

⁸³ KPCo response to Staff Post-hearing Data Request, Nos. 11 & 12.

the Commission to adopt Smith adjustment C-9, in the sum of \$382,769. Moreover, he believes the Commission should initiate a separate investigation of the continued need for this program.

f. Cash Surrender Value of Life Insurance Policies

Attorney General witness Ralph C. Smith proposed an adjustment removing expense associated with the cash surrender value of life insurance policies on former KPCo executives.⁸⁴ Given that these policies cover former executives, there is no rational reason why KPCo ratepayers should have to bear this expense. The Attorney General urges the Commission to adopt this adjustment, in the amount of \$26,941.

g. Relocation Expense

Attorney General witness Ralph C. Smith proposed an adjustment to reduce the level of relocation expense recovered from customers. The Company incurred a test-year relocation expense of \$318,073, of which \$101,938 related to its headquarters moving from Frankfort to Ashland.⁸⁵ Mr. Satterwhite confirmed at the hearing that the Company does not intend on moving its headquarters from Ashland.⁸⁶ As such, it is inappropriate to recover from customers costs that the Company does not intend to incur going forward. In fact, historically the Company has incurred a much lower annual relocation expense, with \$32,192 and \$168,244, from March 2014- Feb. 28, 2015 and March 1, 2015- Feb. 29, 2016, respectively.⁸⁷

h. Rate Case Expense

⁸⁴ Ralph C. Smith Direct Testimony, pp. 47-48, Adjustment C-13.

⁸⁵ Ralph C. Smith Direct Testimony, p. 45; KPCO response to KIUC 1-46; KPCO response to AG 1-251.

⁸⁶ VTE Dec. 6, 12:50:00.

⁸⁷ KPCO response to Staff Post-Hearing Data Request No. 14.

Attorney General witness Ralph C. Smith proposed an adjustment to remove rate case expense.⁸⁸ The first part of this adjustment removes \$11,130 in expense KPCo incurred in the retention of Communication Counsel of America, Inc.,⁸⁹ for the purpose of preparing KPCo witnesses for the evidentiary hearing in this matter.⁹⁰ Such expenses typically fall under services provided by attorneys, and as such is inappropriate for ratepayers to bear.

The second part of Adjustment C-15 removes the remaining rate case expense for the first year of the proposed three-year amortization, in the sum of \$447,203, for a combined total of \$458,333. This adjustment is proposed as an incentive to KPCo to file a case at FERC to reduce the 12.16% ROE governing the Rockport Unit Power Agreement [“Rockport UPA”]. It is unconscionable that KPCo ratepayers should be forced to pay an ROE that was negotiated between parties not subject to the Commission’s jurisdiction, in an era when ROEs were considerably greater than they are today. Although witness Satterwhite at the hearing produced an exhibit⁹¹ which estimated that the actual ROE charged to KPCo ratepayers under the Rockport UPA during the test year was lower than the 12.16% specified in the terms of the Rockport UPA, there is no guarantee either that this “estimate” is correct, or that it will not fluctuate over time. Accordingly, the Attorney General urges that the Commission adopt Smith adjustment C-15 to incentivize KPCo to independently file its own complaint at FERC to protect its ratepayers by seeking to reduce that ROE to a more reasonable level appropriate with prevalent financial conditions. During a period of record cold, and at a time when Eastern Kentuckians are tightening their belts, KPCo continues to spend indiscriminately, as

⁸⁸ Ralph C. Smith Direct Testimony, pp. 48-52, Adjustment C-15.

⁸⁹ An independent communications consulting firm KPCo utilized to help prepare its witnesses. *See* Ralph C. Smith Direct Testimony, p. 50.

⁹⁰ *See* Second Supplemental response to Staff 1-56.

⁹¹ *See* KPCo hearing exhibit 8.

exemplified by its rate case expense in this matter. For instance, the legal fees the Company has run up in this case as of November 30, 2017 total \$677,547, although its total as-filed estimate was \$510,000.⁹²

3. *Proposed Changes to Purchase Power Adjustment Rider (“Tariff PPA”)*

KPCo’s existing Purchase Power Adjustment Rider [“Tariff PPA”] recovers demand credits paid to interruptible customers, certain purchase power expenses not recoverable under the company’s Fuel Adjustment Clause [“FAC”], and costs for purchasing power under new agreements. The company now seeks to include within that rider various PJM Open Access Transmission Tariff [“OATT”] charges and credits that it incurs or receives by participating as a load serving entity [“LSE”] in the organized wholesale power markets of the PJM RTO; purchase power costs excluded from recovery under the FAC; and gains and losses from incidental gas sales.⁹³

The non-unanimous settlement would allow KPCo to track the amount of OATT LSE charges and credits above or below the amount embedded in base rates. KPCo would recover 80% of this annual over- or under-collection of PJM OATT LSE charges through Tariff PPA. Thus, KPCo would absorb 20% of any annual under-collection through base rates of PJM OATT LSE charges. KPCo anticipates that its PJM LSE costs will increase by approximately \$14 million in 2018.⁹⁴

KPCo sought approval for the same tracker in its last rate case. In the final order of that case, the Commission denied the company’s request, finding:

“The Commission is responsible for ensuring that utilities provide safe and reliable electric service at the least cost. The proposed transmission

⁹² See KPCo supplemental response to Staff 1-56, 5th Supplemental Attachment 1.

⁹³ Alex Vaughan Direct Testimony, pp. 25-26.

⁹⁴ Satterwhite amended testimony in support of settlement, pp. 14-15.

adjustment would delegate ratemaking authority for transmission service from the Commission to the Federal Energy Regulatory Commission ("FERC") which would increase the cost of transmission service. Further, the proposal is inconsistent under Kentucky law and precedent which give the Commission retail ratemaking authority for vertically integrated utilities.”⁹⁵

The Attorney General believes that there are no material differences between the tracker proposed in the instant case from that in the last rate case. It would still transfer jurisdiction over a significant portion of retail rates from the Commission to the FERC. Furthermore, tracked recovery reduces a utility’s incentives to control costs as opposed to base rate recovery. The significant increases KPCo expects in its transmission-related costs should receive more scrutiny, such as the need for the project, plans and alternatives that were considered, and cost details. Tracked recovery would provide little more scrutiny than a review of PJM invoices, which would be inappropriate. The better method is base rate recovery, which delays cost recovery enough to incentivize utilities to reduce costs. KPCo and its AEP affiliates do have the ability to exert control over many types of transmission costs they submit to PJM, especially supplemental projects. At the public hearing in this matter, KPCo witnesses provided very little evidence the Company has ever exerted *independent* efforts to help control PJM OATT costs to the benefit of its customers. Instead, it seems the Company is more than happy to sit back and simply “track” the charges its customers now owe, provided that so many of the costs are charged by affiliates.

In response to a post-hearing data request, KPCo provided that in the test year the Company paid \$70,212,659 in PJM LSE OATT costs. Of that \$70M, the Company paid more than \$65M to affiliates, a staggering 92.6% of its costs.⁹⁶ Eastern Kentuckians are continuing

⁹⁵ Case No. 2014-00396, Final Order dated June 22, 2015, p. 34.

⁹⁶ KPCo Response to Attorney General’s post-hearing data requests, item no. 3.

to be asked to pay more so that KPCo can enrich its affiliates. It is time for the Commission to ensure the costs charged to consumers are in the customers' best interests, not AEP's shareholders. Therefore, the Attorney General urges the Commission to deny KPCo's request to track PJM OATT expenses through Tariff PPA, and to ensure greater scrutiny of the pass-through costs KPCo continues to charge customers.

4. Deferral of Rockport Expenses

KIUC witness Kollen proposed that KPCo be allowed to defer \$100 million of the costs KPCo incurs under the Rockport UPA with AEP Generating Company for capacity and energy produced at AEP's Rockport Station. Mr. Kollen's proposal would have deferred those costs over a five-year period, with the company being allowed to earn a carrying charge equivalent to its WACC. At the conclusion of the five-year deferral period, KPCo would be allowed to recover those costs over the ensuing ten years on an annuitized basis through the Tariff PPA surcharge mechanism.⁹⁷

In a data request Commission Staff asked Mr. Kollen why the carrying charge applicable to the Rockport UPA deferral should not be based on KPCo's cost of debt.⁹⁸ Mr. Kollen responded that while KPCo is unlikely to finance a \$100 million deferral solely through debt, nonetheless “. . . it could be appropriate to assume that the deferral is financed through debt if such deferrals are significantly less than under the KIUC proposal.”⁹⁹

The non-unanimous settlement adopted a modified version of Mr. Kollen's deferral proposal, which would defer a significantly reduced sum -- \$50 million -- of non-fuel and non-environmental Rockport UPA costs over the same five (5) year period. Those costs would be

⁹⁷ Lane Kollen Direct Testimony, pp. 7-15.

⁹⁸ Staff data request to KIUC, item 1 (b).

⁹⁹ KIUC Response to Staff Data Request item No. 1 (b).

established as a regulatory asset for later recovery. Significantly, those costs “would be subject to carrying charges based on a weighted average cost of capital (“WACC”) of 9.11% until the regulatory asset is fully recovered.”¹⁰⁰ Thus if the Commission approves the deferral mechanism as proposed in the non-unanimous settlement, by the conclusion of the five-year deferral period, ratepayers will have paid a total of \$59 million for costs that otherwise would have totaled only \$50 million.¹⁰¹

As Attorney General witness Ralph C. Smith acknowledged in the hearing, cost deferrals are worthy of the Commission’s consideration in this case, depending on how they would be structured.¹⁰² However, the Rockport cost deferral as proposed in the non-unanimous settlement would represent a profit center to KPCo as in the long run, it will end up extracting an additional \$9 million more from ratepayers. Given Mr. Kollen’s acknowledgement that a significantly smaller deferral than the one he proposed would likely be financed largely through debt, the Attorney General believes it would be more reasonable to reduce the carrying charge to the level of KPCo’s current long-term debt: 4.36%.¹⁰³ Due to the lower risk associated with the stipulated deferral, rather than Mr. Kollen’s proposed version, the Attorney General believes a significantly reduced carrying charge is appropriate, and indeed necessary.

5. Allocation of Any Potential Base Rate Revenue Increase

The Attorney General believes that if the Commission awards any new revenues, it should utilize the principals set forth in Attorney General witness Dr. David E. Dismukes’

¹⁰⁰ Non-Unanimous Settlement, p. 5.

¹⁰¹ *Id.*

¹⁰² Dec. 6, 2017 VTE 3:31:50 – 3:34:49.

¹⁰³ Supplemental Testimony of Zachary C. Miller filed Aug. 7, 2017, p. 5.

testimony. Rigid adherence to cost of service studies, and reductions of alleged subsidies, ignores essential policy decisions. Here, principles such as rate continuity and gradualism must be given significant weight, particularly when considering the effect it will have on the already struggling residential class.¹⁰⁴ Unfair, unreasonable, and unjust allocation of any rate increase to the residential class may decimate the economy of Eastern Kentucky; as the Chairman noted, residential customers cannot pass on costs like the Company and businesses can.¹⁰⁵ The parties to the non-unanimous settlement agreed to allocate to the residential class slightly more than 61% of the overall revenues sought. Regardless of the amount allocated, the proposed allocation is unfair, unjust and unreasonable. Not only is the proposed allocation in the non-unanimous settlement unduly burdensome, it is wholly inappropriate given the high level of poverty and unemployment affecting residential customers. Therefore, in the unfortunate event the Commission awards KPCo any new revenues, the Attorney General urges the Commission to utilize the important policy considerations and principles at its disposal in hopes of mitigating unquestionable negative implications to residential customers.

6. Residential Class Customer Charge

KPCo's original proposal was to increase the current residential customer charge of \$11 per month to \$17.50 per month. The parties to the non-unanimous settlement propose that the charge should be increased to \$14. However, none of the parties to the non-unanimous settlement represent the interests of residential ratepayers.

As indicated in the direct testimony of Dr. David E. Dismukes, KPCo's class cost of service study indicates that customer-related costs for residential class customers account for

¹⁰⁴ Dr. David E. Dismukes Direct Testimony, pp. 12-14.

¹⁰⁵ VTE Dec. 8, 5:35:30.

only \$7.47 per customer per month.¹⁰⁶ KPCo's existing residential customer charge thus recovers over 147% of the customer-related costs required to serve that class. Moreover, the existing customer charge is noticeably greater than the \$9.60 average of a peer group of other regional IOUs.¹⁰⁷

The Attorney General believes that the \$14 residential customer charge proposed in the non-unanimous settlement would recover too much of any potential revenue increase through the customer charge. From an economic perspective, the notion that fixed costs must be recovered through fixed charges is misguided.

An excessively high fixed charge, as the parties to the non-unanimous settlement proposed, undermines future incentives for efficiency and is also unfair to customers who have already invested in those resources, but who would now see a diminished return on their investment. Thus keeping the customer charge at \$11 – which already over-collects the related residential cost -- is consistent with this Commission's longstanding policy to "avoid taking actions that might disincent energy efficiency."¹⁰⁸ Furthermore, as noted by Attorney General witness Roger McCann, any additional increase in customer charges results in an erosion of LIHEAP funds.¹⁰⁹

A smaller increase in the customer charge will preserve a greater degree of customer control over their electric bills, in contrast to a bill composed of a higher fixed charge that customers cannot avoid no matter what investments or behavioral changes they may make to reduce usage. The reduced ability to control and therefore lower one's utility bill is

¹⁰⁶ Dr. David E. Dismukes Direct Testimony, p. 24, and exhibit DED-5.

¹⁰⁷ *Id.* at p. 25, and Exhibit DED-6.

¹⁰⁸ In Re: *Application of Kentucky Utilities for an Adjustment of its Electric Rates*, Case No. 2012-00221, Final Order dated Dec. 20, 2012, p. 11.

¹⁰⁹ Dec. 8 VTE 5:30:45 – 5:33:45.

particularly harmful for low-income customers who have limited financial resources to meet their basic needs.

7. Economic Development Rider

Ratepayers should not be charged for the economic developments efforts of KPCo or AEP. Economic development is not a reasonable or necessary cost of providing safe and reliable electricity service to customers. There are many local and state entities that provide this service as their primary mission. These day-to-day activities distract the company from its real mission -- that of providing safe and reliable service to its customers -- and results in inflated costs that are not directly tied to providing that service.

The Company is seeking recovery of salaries and KEDS funding that relate exclusively or primarily to economic development. These amounts are recovered from customers and expended for the purpose of promoting the Company's economic development efforts, but importantly, customers have no formal input as to how the money is spent. For instance, KPCo President and COO Satterwhite stated, "that's my number one goal after the safety of my employees is economic development."¹¹⁰ Additionally, KPCo employs two others whose "principal functions include lobbying," but are also responsible for KPCo's economic development efforts.¹¹¹ The purpose and effect of these three (3) employees' efforts, or the issues they spend the majority of their time on, are not necessary to provide safe, reliable electricity, therefore, their salaries should not be recovered from customers.

In addition to spending hundreds of thousands of dollars on salaries dedicated to lobbying and economic development, the Company also requests to recover nearly \$500,000

¹¹⁰ VTE Dec.6, 10:27:35.

¹¹¹ KPCo Response to Staff 1-33.

annually so it can provide economic development grants in KPCo's name. The amounts given under the K-PEGG program, half of which are provided by customers, are determined by a team the Company selected. The review team has no customer representation and customers are denied the opportunity to nominate or choose members of the team, because KPCo stated it must select the team "based on experience and understanding of community and economic development as well as availability to participate in the process confidentially, frequently, and reliably."¹¹² It is apparent that in addition to no direct benefit to the customers, there is no transparency as to how the money is distributed.

While customers provide half of the funding under the K-PEGG program, they also take half of the performance risk, without any input in decision-making.¹¹³ As "there is no direct, known and measurable dollar-for-dollar" benefit to ratepayers, customer funding of the grants should end immediately.¹¹⁴ Captive ratepayers who already struggle to pay their bills today should not be providing a slush fund for AEP and Kentucky Power to travel around Eastern Kentucky providing checks bearing the companies' names in the hope of spurring the economy.¹¹⁵ Promoting the Company and its economic development efforts are not reasonable or necessary costs of providing safe and reliable service, and thus under the regulatory compact should not be allowed recovery through rates.

CONCLUSION

WHEREFORE, the Attorney General respectfully requests that the Public Service Commission deny any base rate increase, and reject the totality of the non-unanimous

¹¹² KPCo Response to AG 1-395.

¹¹³ KPCo Response to AG1-358; Dr. David E. Dismukes Direct Testimony, p. 46.

¹¹⁴ Dismukes Direct Testimony, p. 46.

¹¹⁵ See Dr. David E. Dismukes' and Mr. Roger McCann's Direct Testimony, wherein they provide support that customers *already* struggle to pay their KPCo bills, before considering any rate increase.

settlement as it currently stands. In the event the Commission should award any new base rate revenues, he urges the Commission to adopt the alternative measures outlined in this brief to mitigate any rate increase to the greatest extent possible.

Respectfully submitted,

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Counsel certifies that the foregoing is a true and accurate copy of the same document being filed in paper medium with the Commission within two business days; that the electronic filing has been transmitted to the Commission on January 5, 2018; that there are currently no parties that the Commission has excused from participation by electronic means in this proceeding.

This 5th day of January, 2018.



Assistant Attorney General