COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

KENTUCKY INDUSTRIAL UTILITY CUSTOMERS, INC. **COMPLAINANT** **v.** **KENTUCKY UTILITIES COMPANY, LOUISVILLE GAS AND ELECTRIC COMPANY, KENTUCKY POWER COMPANY, AND DUKE ENERGY KENTUCKY, INC.** **DEFENDANTS**	**)))))))))))))**	**CASE NO. 2017-00477**

ANSWER OF LOUISVILLE GAS AND ELECTRIC COMPANY
TO COMPLAINT AND PETITION AND OFFER OF SATISFACTION

Defendant, Louisville Gas and Electric Company ("LG&E" or the "Company"), by counsel, for its response to the Order of the Kentucky Public Service Commission ("Commission") dated December 27, 2017, and the *Complaint and Petition for the Establishment of a Regulatory Liability to Provide Consumers a Rate Reduction Because of Tax Expense Savings* filed by the Kentucky Industrial Utility Customers, Inc. ("Complainant") on December 20, 2017, states as follows:

COUNTER-STATEMENT OF THE CASE

For many months, LG&E and Kentucky Utilities Company ("KU") (collectively, the "Companies") have been actively supporting the passage of the recently enacted Tax Cuts and Jobs Act ("Tax Act").[1] The Tax Act is beneficial to customers both in terms of utility rates and

[1] Tax Cuts and Jobs Act, H.R. 1, Public Law 115-97, 131 Stat. 2054 (Dec. 22, 2017).

their personal income tax expense. The Tax Act is also beneficial to the economy and economic development.

As the legislation reached the conference committee session, and before the Complaint in this case was filed, LG&E began planning to establish a regulatory liability to accurately reflect the excess deferred taxes associated with the Tax Act. In the Order of December 27, 2017, the Commission ordered LG&E to establish such a regulatory liability. LG&E will establish the regulatory liability as it closes its books for the year ended December 2017.

LG&E anticipated the customers' and the Commission's interest in the effect of the Tax Act on its rates. LG&E agrees the Commission should consider the impact of the changes in the tax law on its existing base rates. However, the analysis of the effect of the Tax Act must consider all circumstances and factors and is much more complex than the cursory analysis in the Complaint suggests. The Complaint ignores at least four impacts of the Tax Act that will partially offset the positive revenue requirement impact of the Tax Act:

1. The Tax Act requires the use of the Average Rate Assumption Method ("ARAM") based on the vintage account data of LG&E for the amortization of excess deferred taxes resulting from the Tax Act.

2. LG&E's cost of capital will increase as a result of the elimination of "bonus depreciation" and other changes to deferred taxes, including the amortization of excess deferred taxes.

3. The Complaint fails to distinguish between base rates and other rate mechanisms, including the Environmental Cost Recovery ("ECR") surcharge, the Demand Side Management ("DSM") Mechanism, and the Gas Line Tracker ("GLT"). These

other rate mechanisms contain provisions that will timely reflect the impacts of the Tax Act.[2]

4. The Complaint ignores the impact on the state income tax deduction due to the lower federal income tax rate.

Rates must be set at a level to allow LG&E the opportunity to recover all its reasonable expenses, including taxes, and to provide shareholders the opportunity to earn a fair return on their invested capital. In its Order in Case No. 2016-00371 on June 22, 2017, the Commission found that "LG&E's required ROE [return on equity] falls within a range of 9.20 percent to 10.20 percent."[3] Any objective analysis of the extent to which the Tax Act causes LG&E's retail rates to no longer be fair, just and reasonable outside of a base rate case should be considered in this context.

The Complaint inappropriately names as defendants four electric utilities with very different circumstances. Two of the parties to this case, Duke Energy Kentucky, Inc. and Kentucky Power Company, have pending base rate cases before the Commission.[4] KU and LG&E do not. Thus, all parties are not similarly situated as the Complaint suggests. Accordingly, KU and LG&E have filed independent Answers and a motion to separate the complaint into four separate cases. In response to the motion, KIUC expressed agreement that its

---

[2] Answer and Offer of Satisfaction, Par. 16.

[3] *In the Matter of: Electronic Application of Louisville Gas and Electric Company for an Adjustment of its Electric and Gas Rates and For Certificates of Public Convenience and Necessity*, Case No. 2016-00371, Order at 20 (June 22, 2017). The Commission set base rate revenues based on the midpoint of the range or 9.7 percent.

[4] *In the Matter of: Application of Kentucky Power Company for (1) A General Adjustment of Its Rates for Electric Service; (2) An Order Approving Its 2017 Environmental Compliance Plant; (3) An Order Approving Its Tariffs and Riders (4) An Order Approving Accounting Practices to Establish Regulatory Assets and Liabilities; and (5) An Order Granting All Other Required Approvals and Relief*, Case No. 2017-00179, Application (Ky. Pub. Serv. Comm'n June 28, 2017); *In the Matter of: Application of Duke Energy Kentucky, Inc. for: 1) An Adjustment of the Electric Rates; 2) Approval of an Environmental Compliance Plan and Surcharge Mechanism; 3) Approval of New Tariffs; 4) Approval of Accounting Practices to Establish Regulatory Assets and Liabilities; and 5) All Other Required Approvals and Relief*, Case No. 2017-00321, Application (Ky. Pub. Serv. Comm'n Sept. 1, 2017);

complaint case should be divided into separate, specific proceedings for KU, LG&E, Duke Energy Kentucky and Kentucky Power.[5]

LG&E desires to determine whether the issues raised in the Complaint can be resolved efficiently and expeditiously, and, accordingly, is tendering an Offer of Satisfaction with its Answer. The Offer of Satisfaction is described in further detail at the conclusion of the Answer. LG&E is filing a separate motion requesting an informal conference for the purpose of discussing the Answer and Offer of Satisfaction.

ANSWER

1. With regard to the statements in paragraph 1 of the Complaint LG&E accepts the statements that the Commission has jurisdiction and venue to hear this Complaint.

2. Based upon information and belief, LG&E accepts the statements in paragraph 2 of the Complaint. LG&E, however, provides retail electric or gas transportation service to only Carbide Industries LLC, Cemex, The Chemours Company, AAK USA K2, LLC, and Ford Motor Company.

3. Based upon information and belief, LG&E accepts the statements in paragraph 3 of the Complaint.

4. With regard to the statements in paragraph 4 of the Complaint, LG&E accepts that KU is a utility as defined in KRS 278.010(3) and a subsidiary of PPL Corporation. LG&E accepts that KU is subject to the jurisdiction of the Commission. PPL Corporation is only subject to the jurisdiction of the Commission to the extent of its change of control commitments.[6]

---

[5] KIUC also indicated that issues raised by its Complaint could be addressed in Duke Energy Kentucky's pending rate case. *See* Reply and Response of Kentucky Industrial Utility Customers, Inc. filed January 5, 2018.

[6] *Joint Application of PPL Corporation, E.ON AG, E.ON US Investments Corp., E.ON U.S. LLC, Louisville Gas and Electric Company, and Kentucky Utilities Company for Approval of an Acquisition of Ownership and Control of Utilities,* KPSC Case No. 2010-00204 Order (September 30, 2010).

LG&E accepts that the addresses for KU and PPL Corporation listed in paragraph 4 of the Complaint are correct.

5. LG&E accepts the statements in paragraph 5 of the Complaint.

6. With regard to the statements in paragraph 6 of the Complaint, LG&E accepts that it is a utility as defined in KRS 278.010(3) and is a subsidiary of PPL Corporation. LG&E accepts that it is subject to the jurisdiction of the Commission. PPL Corporation is only subject to the jurisdiction of the Commission to the extent of its change of control commitments.[7] LG&E accepts that the addresses for LG&E and PPL Corporation listed in paragraph 6 of the Complaint are correct.

7. LG&E accepts the statements in paragraph 7 of the Complaint.

8. LG&E is not representing Kentucky Power Company and therefore declines to admit or deny the statements in paragraph 8 of the Complaint.

9. LG&E is not representing Kentucky Power Company and therefore declines to admit or deny the statements in paragraph 9 of the Complaint.

10. LG&E is not representing Duke Energy Kentucky, Inc. and therefore declines to admit or deny the statements in paragraph 10 of the Complaint.

11. LG&E is not representing Duke Energy Kentucky, Inc. and therefore declines to admit or deny the statements in paragraph 11 of the Complaint.

12. LG&E accepts the statements in paragraph 12 of the Complaint. The Tax Act was passed by the United States Senate and House of Representatives on December 20, 2017.[8]

13. With regard to the statements in paragraph 13 of the Complaint, LG&E affirmatively states that President Trump signed the Tax Act into law on December 22, 2017.[9]

---

[7] *Id.*
[8] Tax Cuts and Jobs Act, H.R. 1, Public Law 115-97, 131 Stat. 2054 (Dec. 22, 2017).

14. With regard to the statements in paragraph 14 of the Complaint, LG&E accepts that the procedural formalities for a potential delay in signing were explained in footnote 2 of the Complaint, but affirmatively states that there was no delay in the bill being signed into law.

15. With regard to the statements in paragraph 15 of the Complaint, LG&E accepts that the Tax Act will lower the maximum federal corporate income tax rate from 35% to 21% effective January 1, 2018. However, the Tax Act will also have numerous other implications, including the elimination of bonus depreciation, the elimination of the Section 199 deduction, and the resulting reduction in state income tax benefits which are not mentioned in the Complaint.

16. With regard to the statements in paragraph 16 of the Complaint, LG&E accepts that its current retail rates were set based on a federal corporate income tax rate of 35%. LG&E is not representing Kentucky Power Company or Duke Energy Kentucky, Inc. and thus is without sufficient information to admit or deny the current costs included in their retail rates. LG&E's other rate mechanisms, such as the ECR surcharge, DSM mechanism, and the GLT, already have embedded procedural provisions to provide a true-up of actual tax rates and associated rate base amounts. LG&E will employ these procedural mechanisms to return the benefits of the Tax Act associated with cost of the facilities recovered through the mechanisms to customers. For example, the Commission's December 19, 2017 Order in Case No. 2017-00267 approved an overall weighted cost of capital ("WACC") of 10.34 percent for use in all monthly environmental surcharge filings beginning the second full billing month following the date of the order.[10] In a separate filing, LG&E is requesting the Commission modify the tax gross-up for the

---

[9] *Id.*

[10] *In the Matter of: An Electronic Examination by the Public Service Commission of the Environmental Surcharge Mechanism of Louisville Gas and Electric Company for the Two-Year Billing Period Ending April 30, 2017,* Case No. 2017-00267, Order at 6 (Dec. 19, 2017).

WACC to reflect the changes in the Tax Act effective with the expense month of January 2018 for the ECR surcharge. In addition, in its next ECR review case, LG&E will propose to modify the ECR Forms to account for the return of the excess deferred taxes. LG&E also will take timely and comparable actions with respect to the calculation of its other rate mechanisms. With regard to the DSM mechanism, the 2018 tariff filings have already been approved. LG&E will incorporate the Tax Act changes into the 2018 DSM rates when it makes the balancing adjustment filing at the end of February 2018 with new rates effective April 1, 2018. For its GLT, LG&E will include the effect of the Tax Act changes in the 2018 annual filing being made at the end of February 2018 with rates effective May 1, 2018.

17. With regard to the statements in paragraph 17 of the Complaint, LG&E states as follows:

(a) LG&E accepts that the federal corporate income tax expenses currently included in its retail tariffed rates do not reflect the lower federal corporate income tax rate or the other changes in tax requirements established under the Tax Act effective on January 1, 2018.

(b) LG&E denies that the implementation of the new federal tax rate will lower the revenue requirements of the Defendants by $209 million or more annually for at least four reasons. The four impacts of the Tax Act ignored by the Complaint are set forth in the Counter-Statement of the Case beginning on page 2 of this Answer, and are incorporated herein by reference.

(c) LG&E acknowledges that the Complaint's estimated annual revenue requirement reduction is listed in Paragraph 35, but denies that it is appropriate or correct as it ignores the full effects of the Tax Act or other changes in costs and revenues. As LG&E has not completed its analysis of the impacts of the Tax Act, LG&E cannot deny or confirm that

Complainant's estimate of an average rate reduction of 4%-7% is reasonable or appropriate for LG&E. However, LG&E currently estimates the impact of the Tax Act, inclusive of base rate and other rate mechanism effects, could be within this range at the time of LG&E's next base rate case with respect to its electric operations, but below this range with respect to its gas operations.

(d) LG&E is not representing Kentucky Power Company or Duke Energy Kentucky, Inc. and thus is without sufficient information to admit or deny the effect of the Tax Act on their rates.

18. LG&E accepts the statements in paragraph 18 of the Complaint.

19. With regard to the statements in paragraph 19 of the Complaint, LG&E notes the Commission's December 27, 2017 Order found "that KIUC has established a *prima facie* case that as of January 1, 2018, the rates of [LG&E] will no longer be fair, just, or reasonable."

20. With regard to the statements in paragraph 20 of the Complaint, LG&E accepts that the effect of the lower income tax expense and the amortization of excess accumulated deferred income taxes ("ADIT") are not currently reflected in its rates. Presuming no subsequent change in federal income tax rates, previous tax benefits on LG&E's books as of December 31, 2017 will "reverse" at 21% rather than at the 35% rate, creating "excess deferred taxes." LG&E will reclassify the excess deferred taxes as a regulatory liability as it closes its books for the year ended December 2017. LG&E presently estimates property-related or "protected" excess deferred taxes at approximately $375 million.[11] Amortization of these excess deferred taxes will begin in January 2018 using ARAM as required by the Tax Act.[12] Excess deferred taxes for non-property items, also known as "unprotected", will also be reclassified to the regulatory liability in

[11] Tax Cuts and Jobs Act § 13001(b)(6)(A), amending § 1561(d)(1), H.R. 1, Public Law 115-97, 131 Stat. 2054 (Dec. 22, 2017).
[12] *Id.* at § 13001(b)(6)(A), amending § 1561(d)(2), (d)(3)(B).

December 2017.[13] LG&E presently estimates these excess deferred taxes at approximately $23 million. LG&E expects the amortization period for these non-property excess deferred taxes to be established in its next base rate case. LG&E will continue to review and adjust the regulatory liability as it closes its books for the year ended December 2017.

21. With regard to the statements in paragraph 21 of the Complaint, LG&E acknowledges the statements in paragraph 21 of the Complaint generally illustrate the long-standing equity gross-up procedure used in ratemaking. LG&E denies the example in paragraph 21 of the Complaint is a reasonable representation of the full equity gross-up procedure because it does not include the gross-up for state corporate income taxes, the gross-up for bad debt expense, or the Commission's assessment fee. Including the state statutory rate in the calculation of the gross-up factor will change the current blended income tax rate used in the gross-up factor from 38.9% to 25.74%. LG&E accepts that LG&E's revenue requirement will be reduced through a reduction in the equity gross-up because of the effects of the Tax Act.

22. With regard to the statements in paragraph 22 of the Complaint, LG&E accepts that the statements in paragraph 22 of the Complaint correctly characterize the creation of excess ADIT. LG&E accepts that customers should receive the benefit for excess ADIT and the method for doing so is ARAM as required by the Tax Act. LG&E also affirmatively states that while the Complaint recognizes there is an impact to the cost of capital due to ADIT, the Complaint did not reflect this impact in its high-level estimate of the impact of the Tax Act on LG&E's revenue requirement.

23. LG&E accepts that paragraph 23 of the Complaint accurately quotes the 2013 Edison Electric Institute report entitled "*Comprehensive Tax Reform Priorities: Excess Deferred Tax Transition Issues*" and that an accurate copy of the report is attached at Attachment B.

[13] *See Id.* at § 13001(b)(6)(A), amending § 1561(d)(1).

24. LG&E accepts the statements in paragraph 24 of the Complaint.

25. LG&E accepts that paragraph 25 of the Complaint accurately quotes in part the Commission's language in the Tax Reform Act of 1986 cases.

26. LG&E accepts that paragraph 26 of the Complaint accurately quotes in part the Commission's language in the Tax Reform Act of 1986 cases.

27. LG&E accepts so much of the statements in paragraph 27 of the Complaint that describe the Commission's actions in the Tax Reform Act of 1986 cases. LG&E is without sufficient information to admit or deny KIUC's statement that the total amount of rate reductions was in excess of $75 million and therefore denies the same.

28. LG&E accepts that paragraph 28 of the Complaint accurately quotes portions of an article published by Regulatory Research Associates dated January 25, 2017, and that an accurate copy of the article is attached at Attachment C.

29. LG&E accepts the statements in paragraph 29 of the Complaint.

30. LG&E accepts the statements in paragraph 30 of the Complaint. LG&E notes that the authority cited in support of the statement in the paragraph 30 is the Commission's order in Case No. 2010-00204 approving the "*Acquisition Savings Sharing Deferral Methodology*." The *Acquisition Savings Sharing Deferral Methodology* considered all changes in revenues and expenses as part of its procedure to determine whether LG&E's earnings exceeded the upper end of the range for the return on equity authorized by the Commission for this calculation.

31. LG&E accepts that paragraph 31 of the Complaint accurately quotes in part the language from the Commission's order in Case No. 2016-00180.

32. With regard to the statements in paragraph 32 of the Complaint, LG&E accepts that deferral in a regulatory liability is appropriate to account for the excess deferred tax effects

of the Tax Act. LG&E will establish such a regulatory liability as part of closing its books for December 2017. LG&E will also establish a regulatory liability for other implications of the Tax Act to the extent it causes those rates to no longer be fair, just and reasonable as described in LG&E's Offer of Satisfaction tendered with this Answer.

33. With regard to the allegations in paragraph 33 of the Complaint, LG&E denies that there is no legal constraint on the Commission's authority to act upon this Complaint. In *Kentucky Pub. Serv. Comm'n v. Com. ex. rel. Conway*, cited in paragraph 33 of the Complaint, the Kentucky Supreme Court expressly noted that the Commission's plenary rate making authority is circumscribed by "its duty to ensure that rates are 'fair, just and reasonable.'"[14] The courts of other jurisdictions have found that single issue rate making distorts the ratemaking process and is likely to produce unfair and unreasonable rates.[15] The Commission has found that focusing upon one expense or revenue without consideration to all expenses and revenues will likely result in unreasonable and unfair rates and has warned of the unintended consequences that may result from such the use.[16] While the Complainant relies upon the *Conway* decision to support its request that the Commission engage in single-issue ratemaking, it fails to note that *Conway* addressed only the Commission's authority in a base rate proceeding to establish a rider

[14] *Kentucky Pub. Serv. Comm'n v. Com. ex. rel. Conway* , 324 S.W.3d 373, 382 n. 25 (Ky. 2010).

[15] *See, e.g., Bus. & Prof'l People for the Pub. Interest v. Ill. Commerce Comm'n*, 585 N.E.2d 1032, 1061 (Ill. 1991) ("The rule against single-issue ratemaking recognizes that the revenue formula is designed to determine the revenue requirement based on the aggregate costs and demand of the utility. Therefore, it would be improper to consider changes to components of the revenue requirement in isolation. Often times a change in one item of the revenue formula is offset by a corresponding change in another component of the formula."); *Public Service Co. of New Mexico v. FERC*, 832 F.2d. 1201, 1205 (10th Cir. 1987) ("In determining a just and reasonable rate, the Commission must consider several factors, including operating expenses, depreciation expense, taxes, and a reasonable return to the utility's investors.")

[16] *In the Matter of: Big Rivers Electric Corporation's Proposed Mechanism to Credit Customers Amounts Recovered in Judicial Proceedings Involving Fuel Procurement Contracts*, Case No. 94-453, Order at 7-8 (February 21, 1997) ("A separate rate which requires the refund of litigation proceeds without examining BREC's other expenses and revenues may also have unintended policy consequences. A utility which incurs a significant expense in one area, but which is otherwise earning large profits, may request a rate designed solely to recover the significant expense. If a utility can be ordered to refund particular revenues, it can also be authorized to collect a particular expense. While a refund of any litigation proceeds may be attractive in the short run, in the long run the precedent which it establishes may greatly disadvantage utility ratepayers.")

to be charged as a separate line item on customer bills and did not address whether a utility's revenue requirement may be adjusted outside of the context of a base rate case.

34. With regard to the statements in paragraph 34 of the Complaint, LG&E accepts the Commission has granted Complainant's request for an immediate deferral in its order of December 27, 2017 in ordering paragraph numbered 2.

35. With regard to the allegations in paragraph 35 and Attachment A of the Complaint, LG&E denies that the calculations of LG&E tax savings due to the Tax Act are accurate or reasonable. The Complainant's quantifications are incorrect for numerous reasons:

(a) First, the Complaint ignores at least four impacts of the Tax Act that will partially offset the positive revenue requirement impact of the Tax Act. The four impacts of the Tax Act are described in detail in the Counter-Statement of the Case beginning on page 2 of this Answer, and are incorporated herein by reference.

(b) Second, the information used to derive the Complainant's calculations is stale and outdated.

(c) Additionally, Attachment A unreasonably assumes an average asset life of 20 years for purposes of illustrating the amortization of the excess deferred tax balance. LG&E's actual average asset life is greater than 20 years. Using 20 years to calculate a rate reduction is arbitrary and violates tax normalization and the matching principle.[17] The "excess deferred" balances will not be known until the 2017 books are closed. However, LG&E's current estimate is approximately $375 million. Use of the ARAM approach for the amortization of this balance is required by the Tax Act and is consistent with the treatment of excess deferred taxes created

[17] *In the Matter of: Application of South Kentucky Rural Electric Cooperative Corporation for an Adjustment of Electric Rates*, Case No. 2011-00096, Order at 7 (Mar. 30, 2012) ("We find that South Kentucky's request to extend the cut-off date beyond the test year-end for the meter account violates the 'matching principle' long recognized by the Commission. For ratemaking purposes, the matching principle means that all revenues, expenses, rate base components, plant additions, and capital items are updated to the same period.")

by the 1986 Tax Reform Act.[18] The amount of annual amortization will vary over time based on the vintage account data of property which gave rise to the December 31, 2017 deferred tax reserve.

(d) Finally, LG&E is not representing Kentucky Power Company or Duke Energy Kentucky, Inc. and thus is without sufficient information to admit or deny the effect of the Tax Act on their rates.

FIRST AFFIRMATIVE DEFENSE

When determining the reasonableness of LG&E's base rates, considering the changes in tax expense in isolation from other changes in revenues and expenses will likely result in unreasonable and unfair rates. The Commission has repeatedly rejected asymmetrical ratemaking.[19] More than 20 years ago, the Commission explained the rationale for its general prohibition against such ratemaking:

> The rule against single-issue ratemaking recognizes that the revenue formula is designed to determine the revenue requirement based on the aggregate costs and demand of the utility. Therefore, it would be improper to consider changes to components of the revenue requirement in isolation. Often times a change in one item of the revenue formula is offset by a corresponding change in another component of the formula.[20]

---

[18] Tax Reform Act of 1986 § 203(e), Public Law 99-514, 100 Stat. 2085 (Oct. 22, 1986).

[19] *See e.g.*, *In the Matter of: Application of Blue Grass Energy Cooperative Corporation For an Adjustment of its Security Deposit and Cable Television Attachment Rates*, Case No. 2010-00185 (Aug. 23, 2010) (noting the Commission's reluctance to engage in "single issue ratemaking" stating that it would not consider proposed pole attachment rates "in isolation" from the utility's other costs and revenues); *In the Matter of: The Purchased Gas Cost Adjustment Filing of Duke Energy Kentucky*, Case No. 2007-00362, Order (Aug. 28, 2007) ("[T]here is no inherent authority to perform interim single-issue rate adjustments because such a mechanism would undermine the statutory scheme[.]");*In the Matter of: The Request of the Union Light, Heat and Power for Permission to Establish a Process to Recover the Anticipated Increase in its Purchased Power Cost*, Case No. 91-313, Order (Oct. 31, 1991) ("The comments are unanimous in the assertion that there is no statutory or regulatory authority for the acceptance of a one issue rate case as proposed by ULH&P.")

[20] *In the Matter of: Big Rivers Electric Corporation's Proposed Mechanism to Credit Customers Amounts Recovered in Judicial Proceedings Involving Fuel Procurement Contracts*, Case No. 94-453, Order at 7 (February 21, 1997) (quoting *Bus. & Prof'l People for the Pub. Interest v. Ill. Commerce Comm'n*, 585 N.E.2d 1032, 1061 (Ill. 1991)). In the *Business & Professional People* case, which concerned recovery of capital costs incurred in building nuclear plants, the court held that it would be single-issue rate-making to allow the utility to recover deferred

To address the effect of the Tax Act on LG&E's rates outside the context of a base rate proceeding and without considering the full implications of the Tax Act on LG&E's revenue requirement and other changes in revenue and costs would constitute arbitrary ratemaking. As required by the Commission's Order of December 27, 2017, LG&E has established a regulatory liability for excess deferred taxes as of December 2017 and will establish a regulatory liability beginning January 1, 2018 for other impacts of the Tax Act to the extent it causes LG&E's retail rates to no longer be fair, just and reasonable. LG&E's Offer of Satisfaction tendered with this Answer addresses how LG&E would provide this benefit to customers as soon as administratively feasible which LG&E would estimate as beginning with the April 2018 billing period.

SECOND AFFIRMATIVE DEFENSE

The Complaint fails to consider all implications of the Tax Act on LG&E. The full effect of the Tax Act on LG&E's revenue requirement will not be available until LG&E's books are closed for 2017, which will be early February 2018. Failure to consider all implications of the Tax Act inaccurately calculates the effect of the Tax Act and is not fair, just and reasonable.

OFFER OF SATISFACTION

LG&E agrees customers should receive their appropriate share of the benefits under the Tax Act on a timely basis. LG&E currently estimates its base rate return on equity for 2018, adjusted for the Tax Act (including amortization of excess deferred taxes), will be over 12% for its electric operations and near the currently authorized 9.7% for its gas operations.[21]

LG&E and its sister utility KU will each file for a change in their base rates no later than September 28, 2018 to address the expiration of the Capacity Purchase and Tolling Agreement

---

charges without also accounting for offsetting decreased operating expenses combined with higher revenues from increased demand. *Id.* at 1062.

[21] These calculations are considered preliminary and are subject to change.

with Bluegrass Generation, the retirement of Brown Units 1 and 2, the departure of nine municipal wholesale customers from the KU system, the effects of the Tax Act, and other changes in LG&E's revenue requirement. Base rates are expected to be reset effective May 1, 2019 based on a forecasted test year.

LG&E tenders the following Offer of Satisfaction: LG&E will establish a bill credit mechanism effective as soon as administratively feasible (estimated to begin with the April 2018 billing cycle) to distribute the amount of earnings forecasted to be in excess of 10.2 percent return on equity, the top end of the return on equity range found reasonable by the Commission on June 22, 2017. The period used to compute the amount to be returned to customers would be January 1, 2018 through April 30, 2019, the date range between the effective date of the Tax Act and the date on which new retail base rates are expected to be reset. LG&E would record as a regulatory liability over the period January 1, 2018 through April 2019 such amounts to be distributed to customers and reduce that liability as those amounts are returned to customers through this bill credit mechanism or changes in base rates. The mechanism will be cancelled and withdrawn concurrent with the implementation of new base rates. The new base rates will reflect the impact of the Tax Act on tax expenses recovered in the base rates.

LG&E's ECR surcharge, DSM mechanism, and GLT already have embedded procedural provisions to provide a true-up of actual tax rates and associated rate base amounts. These procedures are described in detail in paragraph 16 of this Answer and Offer of Satisfaction, and are incorporated by reference herein.

LG&E is requesting an informal conference for purpose of discussing this Offer of Satisfaction.

WHEREFORE, Louisville Gas and Electric Company respectfully requests the Commission:

1. As approved by the Commission's December 27, 2017 order, permit LG&E to establish a regulatory liability effective December 31, 2017 for the excess accumulated deferred taxes that result from the change in the corporate income tax rate under the Tax Act with such regulatory liability to be amortized in accordance with the ARAM prescribed by the Tax Act;

2. Accept its proposed Offer of Satisfaction as the disposition of this case; and

3. For all other relief to which it may be entitled.

Dated: January 8, 2018

Respectfully submitted,

Kendrick R. Riggs

Kendrick R. Riggs
Stoll Keenon Ogden PLLC
2000 PNC Plaza
500 W. Jefferson Street
Louisville, KY 40202-2828
Telephone: (502) 333-6000
kendrick.riggs@skofirm.com

Allyson K. Sturgeon
Senior Corporate Attorney
LG&E and KU Energy LLC
220 W. Main Street
Louisville, KY 40202
Telephone: (502) 627-2088
allyson.sturgeon@lge-ku.com

Counsel for Defendant, Louisville Gas and Electric Company

<u>CERTIFICATE OF SERVICE</u>

This is to certify that Louisville Gas and Electric Company's January 8, 2018 electronic filing of its *Answer and Offer of Satisfaction* is a true and accurate copy of the same document being filed in paper medium; that the electronic filing has been transmitted to the Commission on January 8, 2018; that there are currently no parties that the Commission has excused from participation by electronic means in this proceeding; and that an original in paper medium of the *Answer and Offer of Satisfaction* are being mailed to the Commission on January 8, 2018, by first class United States mail, postage prepaid.

____
Counsel for Defendant, Louisville Gas and Electric Company