

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

ELECTRONIC APPLICATION OF)	
KENTUCKY UTILITIES COMPANY FOR AN)	CASE NO. 2018-00294
ADJUSTMENT OF ITS ELECTRIC RATES)	

In the Matter of:

ELECTRONIC APPLICATION OF)	
LOUISVILLE GAS AND ELECTRIC)	CASE NO. 2018-00295
COMPANY FOR AN ADJUSTMENT OF ITS)	
ELECTRIC AND GAS RATES)	

JOINT POST-HEARING BRIEF
OF KENTUCKY UTILITIES COMPANY
AND LOUISVILLE GAS AND ELECTRIC COMPANY

Dated: April 1, 2019

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INTRODUCTION

Kentucky Utilities Company (“KU”) and Louisville Gas and Electric Company (“LG&E”) (collectively, the “Companies”) submit this brief and request the Kentucky Public Service Commission (“Commission”) issue an order by April 30, 2019 approving the proposed rates, terms, and conditions set forth in the tariffs submitted with the Companies’ stipulations¹ as adjusted and clarified in the Companies’ responses to the post-hearing data requests.²

On September 28, 2018, KU and LG&E filed base rate applications supported by fully forecasted test periods ending April 30, 2020 and base periods ending December 31, 2018.³ KU and LG&E also proposed to withdraw their Adjustment Clause TCJA from service and cancel the associated billing credits effective when new base rates change.⁴

The Association of Community Ministries, Inc. (“ACM”), Attorney General of the Commonwealth of Kentucky, by and through the Office of Rate Intervention (“AG”), Charter Communications Operating, LLC (“Charter”), Community Action Council for Lexington-Fayette, Bourbon, Harrison, and Nicholas Counties, Inc. (“CAC”), United States Department of Defense and All Other Federal Executive Agencies (“DoD”), Kentucky Industrial Utility Customers, Inc. (“KIUC”), The Kroger Company (“Kroger”), Kentucky School Boards Association (“KSBA”), Lexington-Fayette Urban County Government (“LFUCG”), Louisville/Jefferson County Metro Government (“Louisville Metro”), Metropolitan Housing

¹ *Stipulation and Recommendation* (March 1, 2019) Stipulation Exhibit 6 (KU Tariff), Stipulation Exhibit 7 (LG&E Electric Tariff) and Stipulation Exhibit 8 (LG&E Gas Tariff); *Stipulation and Recommendation* (February 27, 2019) Stipulation Exhibit 1 (KU PSA Rate Schedule) and Stipulation Exhibit 2 (LG&E PSA Rate Schedule).

² See Case No. 2018-00294, Response and Attachments to Response to PSC Post Hearing Question Nos. 3 and 8; Case No. 2018-00295, Response and Attachments to Response to PSC Post Hearing Question Nos. 2 and 8.

³ KRS 278.190(1), (2); 807 KAR 5:001 Section 16(1)(a)2.

⁴ KU Application, ¶ 7; LG&E Application, ¶ 7, 9. By Order dated March 20, 2018, in Case No. 2018-00034, the Commission approved an *Offer and Acceptance of Satisfaction* providing that KU and LG&E “will continue to impose on the bills of their customers the [TCJA Surcredit], adjusted to reflect estimated annual Tax Act benefits, until such time as new base rates resulting from applications to change base rates take effect.”

Coalition (“MHC”), Sierra Club and certain individual members (“Sierra Club”), and Walmart Inc. (“Walmart”) all participated in one or both of the proceedings.⁵ On January 16, 2019, after three rounds of discovery, the intervenors filed their testimony. On February 22, 2019, following a round of discovery, the Companies filed their rebuttal testimony.

At Charter’s request, a video conference was conducted on February 25, 2019 to discuss the issues related to the Companies’ proposed revisions to the Pole and Structure Attachment Charges Schedule (“Rate PSA”).⁶ On February 27, 2019, the Companies filed a *Stipulation and Recommendation* for the disposition of the issues in dispute between the Companies and Charter associated with the proposed changes in Rate PSA (“PSA Stipulation”).

The Commission Staff and all of the parties, with the exception of Charter, participated in an informal conference on February 26 and 27, 2019. On March 1, 2019, all of the parties (collectively the “Stipulating Parties”), with the exception of Charter and the Sierra Club, entered into and filed a *Stipulation and Recommendation*⁷ (“Stipulation”). The Stipulation, with two exceptions, addresses all the issues associated with the proposed revenue requirements, revenue allocation, and rate design of the rates.⁸

On March 5 and 6, 2019, the Commission held a hearing, and received evidence in the form of testimony from all the parties and the Stipulation and PSA Stipulation (collectively

⁵ The Commission dismissed Sierra Club, ACM, CAC, and MHC as parties on March 6, 2019. *See P.S.C. of Ky. v. Phillip J. Shepherd et al.*, Ky. Ct. App. No. 2018-CA-001859-OA (Ky. App. Mar. 6, 2019) (to be published), ACM, CAC, MHC, and Sierra Club’s motion to reconsider and dismiss pending.

⁶ The Companies gave notice and the opportunity to participate to all the parties and Commission Staff of the video conference. In addition to the Companies and Charter, representatives of Commission Staff, Louisville Metro, and the AG attended the conference.

⁷ On March 6, 2019, the Companies filed an *Addendum to the Stipulation*, supplementing it with two additional terms that were inadvertently omitted: Addendum Article 1. Merger Mitigation Depancaking and Addendum Article 2. KSBA-Related Rate Design Adjustments to Rate PS.

⁸ The Stipulation reserved two issues for the hearing: (1) the Companies’ 401(k) contributions for employees who are also participants in the Companies’ defined benefit plans and (2) the topics associated with the basic service charge. Stipulation Section 4.2.

“Stipulations”). The Stipulations represent a reasonable compromise among all of the parties with respect to the revenue requirements, revenue allocations, rate design, and terms and conditions of service.⁹ The Stipulations therefore should be afforded great weight by this Commission when deciding these cases.

I. Stipulation

A. The Revenue Requirements Recommended by the Stipulation are Fair, Just, and Reasonable

The record shows that the parties had various positions on a wide range of issues. As Mr. Blake discussed at the hearing, during the course of the settlement conference, each party represented its own client’s interest and considered the interest of all the Companies’ customers as well, which led to the revenue requirements proposed in the Stipulation.¹⁰

The Stipulation provides a balanced, detailed and comprehensive recommendation for the resolution of all revenue requirement issues with one exception. The Stipulation presents a transparent calculation of the revenue requirements recommended by the Stipulating Parties.¹¹ While the Companies, any other party or the Commission could selectively argue for or against a specific adjustment, as Mr. Blake pointed out, the fact that all of the parties with their varying interests, ultimately agree upon the resulting revenue requirements, evidences that the Stipulation results in a fair, just, and reasonable outcome.¹²

It is equally significant that all parties could compromise and reach a common recommendation on all revenue requirement-related issues except for recovery of the 401(k) matching contribution expense. The Companies and the parties did not reach a settlement on this

⁹ The Sierra Club was not a party to either Stipulation, but expressly stated on the record that it had no objections to the Stipulations. 3/5/19 Hearing, VR 9:07:22.

¹⁰ 3/6/19 Hearing, VR 3:23:27.

¹¹ Stipulation Testimony of Kent W. Blake at 3-4.

¹² 3/6/19 Hearing, VR 3:23:08.

issue principally because the Stipulating Parties relied on the Commission's decision in the Companies' last rate cases on this issue while the Companies believe that more recent Commission precedent, the Companies' subsequent course of conduct and other changes merit a different result.

At the hearing, the Commission also questioned whether the Stipulation on revenue requirements was based primarily on the deferral of costs.¹³ But a number of the revenue adjustments were reductions rather than deferrals. The record demonstrates that the Companies' investments are reasonable and prudent and the Companies' operations are efficiently managed and the Stipulation reflects that. Despite the reasonableness of their filed positions, the Companies recognized the need to compromise on their requested return on equity and acknowledge the effect of subsequent changes in the market (e.g., projected interest rates on the Companies' First Mortgage Bond offering) and updates for business activities taken on behalf of their customers (e.g., the proceeds from the refined coal contracts associated with the Trimble County and Mill Creek generation stations¹⁴ and their joint application with the Federal Energy Regulatory Commission to remove the merger mitigation de-pancaking component in transmission Rate Schedule No. 402).¹⁵

The Stipulation's use of deferral accounting and adjustments of depreciation expense are consistent with established ratemaking, accounting, and depreciation practices and does not otherwise create an unjustified deferral of costs for recovery in the future. The Stipulation's

¹³ 3/6/19 Hearing, VR 4:42:50.

¹⁴ Stipulation at 5-12; Addendum to the Stipulation, Addendum Article 1. Merger Mitigation Depancaking; *see also* Stipulation Testimony of Kent W. Blake at 9-11.

¹⁵ *Joint Application Under FPA Section 203 and Section 205 of Louisville Gas and Electric Company and Kentucky Utilities Company*, FERC Docket Nos. EC98-2-00 and ER1 8-2162-000. The Federal Energy Regulatory Commission conditionally granted the Companies' request to remove the merger mitigation de-pancaking component, subject to a transition mechanism for the Transition Customers; *See Louisville Gas and Elec. Co. and Kentucky Utilities Co.*, 166 FERC ¶ 61,206, at P 2, 35 (2019) (March 21, 2019).

adjustments that use deferral accounting¹⁶ do not result in undue intergenerational inequities and are not inconsistent with Commission orders.¹⁷ The Companies originally proposed to shorten the depreciation lives of the ash ponds to end when they are capped and closed (which would have effectively accelerated the recovery of these costs), but agreed in the Stipulation to accept KIUC's position by continuing to match the lives of the generating units that the ash ponds support and avoid altering the associated Commission-approved depreciation rates.¹⁸ As Vice Chairman Cicero noted, this means the \$8 million reduction due to this adjustment does not cause a further deferral of costs.¹⁹ Accordingly, the Stipulation's use of deferral accounting and adjustment of depreciation expense does not result in unjustified deferral of costs.

1. The Commission Should Approve Full Rate Recovery of 401(k) Matching Contribution Expense

The Stipulation did not address recovery of the 401(k) matching contribution expense, reserving resolution of this issue for the hearing. The Companies believe that their subsequent course of conduct and other changes since the 2016 rate case decision merit complete recovery. Two parties, the AG and KIUC, contend the Commission's decision in the last rate cases, notwithstanding the Companies' subsequent actions, additional evidence and the Commission's decision in Case No. 2017-00321²⁰ should continue to be applied. Through the Companies'

¹⁶ E.g., recovery of the expense to repair Brown 1 stack, reduction for late payment charge waiver, and the extended amortization period for the July 2018 Storm regulatory assets.

¹⁷ The Commission approved a ten-year amortization of the Utilities' regulatory assets approved by the Commission concerning the 2008 Wind Storm and 2009 Winter Storm. *In the Matter of: Application of Kentucky Utilities Company for an Adjustment of Base Rates*, Case No. 2009-00548, Order at 12, 19-20 (Ky. PSC July 30, 2010); *In the Matter of: Application of Louisville Gas and Electric Company for an Adjustment of Electric and Gas Base Rates*, Case No. 2009-00549, Order at 12, 21-22 (Ky. PSC July 30, 2010).

¹⁸ Stipulation at 8-9, 12; *see also* Stipulation Testimony of Kent W. Blake at 8.

¹⁹ 3/6/19 Hearing, VR 4:46:28.

²⁰ *In the Matter of: Electronic 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, Order at 22-23 (Ky. PSC Apr. 13, 2018).

diligent management of their labor expense, including their retirement expense, the Companies have demonstrated that these costs are prudent and reasonable.

In the Companies' 2016 rate cases, the Commission disallowed rate recovery of employer-provided 401(k) matching contribution expense for some employees who participate in the Companies' defined benefit plan ("DB Plan"). Based on the records of the current cases, however, the Commission should reach a different conclusion now. After the last ruling, the Companies engaged independent experts to perform benchmarking studies of their compensation and benefits offerings and negotiated, where necessary, new contract language with the unions to provide flexibility to make future benefit changes to remain consistent with market. The Companies have proven that: (1) their overall total cash compensation expense is reasonable and consistent with market; (2) their overall retirement and welfare benefits expense is reasonable and consistent with market; and, therefore, (3) their total remuneration (compensation plus benefits) in the aggregate paid to employees is reasonable. Given that reasonableness, and because the Companies must offer a total compensation and benefits package to existing and prospective employees,²¹ full rate recovery of all labor expense should be allowed.

As for overall total cash compensation, the Companies commissioned and submitted a compensation study prepared by Willis Towers Watson ("WTW Study").²² As explained in that study and by Mr. Meiman, the Companies' total cash compensation expense, including base and incentive compensation, is reasonable because it is aligned with market when compared to both utilities and general industry.²³ The WTW Study specifically included entities (utilities and non-

²¹ Direct Testimony of Gregory J. Meiman at 4.

²² The WTW Study was attached to the Companies' Applications at Tab 60, Attachment 3.

²³ Direct Testimony of Gregory J. Meiman at 9-10; WTW Study at 3-5.

utilities) with Kentucky operations in the comparison groups.²⁴ No intervenor proposed any disallowance to the Companies' total compensation expense.

Regarding welfare and retirement benefits, the Companies commissioned and submitted a benefits study prepared by Mercer ("Mercer Study").²⁵ As explained by Mr. Meiman and in the Mercer Study, the Companies' welfare and retirement benefit expense is also reasonable because it is aligned with market.²⁶

The Commission should approve the Companies' entire compensation and benefits package for rate recovery. The record shows that the Companies do an excellent job of managing their 3600-member workforce in a way that provides market-based total remuneration, while, at the same time, avoiding excessive turnover.²⁷ And they do so without paying a "premium" to retain employees.²⁸ Of course, this directly benefits customers as proven by the fact that the Companies are a top quartile performer in cost per megawatt sold.²⁹ Conversely, a failure to provide competitive compensation and benefits could lead to unreliable service and higher costs of service.³⁰

The Companies have aggressively managed their retirement expense in the precise manner the Commission has found to be reasonable. In *allowing* recovery of 401(k) matching contributions to those already participating in a *separate* pension plan (and over the same AG objection made in the cases at bar) in a recent Duke Energy case, the Commission stated:

²⁴ See the Companies' responses to Item 112 of the AG's First Request for Information in each case which identify the entities in the comparator groups and include: American Electric Power (parent company of Kentucky Power Company); Atmos Energy; Duke Energy; and NiSource (parent company of Columbia Gas of Kentucky).

²⁵ The Mercer Study is attached to the Companies' Application at Tab 60, Attachment 4.

²⁶ Direct Testimony of Gregory J. Meiman at 19-20; Mercer Study at 4.

²⁷ 3/5/19 Hearing, VR 3:32:50.

²⁸ 3/5/19 Hearing, VR 3:34:00.

²⁹ Direct Testimony of Kent W. Blake at 12.

³⁰ Direct Testimony of Gregory J. Meiman at 5-7.

Duke Kentucky states that it has aggressively managed costs related to its retirement benefits program by closing the DDB pension plans to new hires, and, for existing employees, lock and freezing final average pay benefit formulas for all non-union employees and transitioning those employees from a final average pay formula to a more “Defined Contribution like” cash balance benefit formula. Lastly, Duke Kentucky asserts that its benefits packages, including retirement programs, as a whole are designed to be market competitive and are benchmarked to ensure that is the case.

The Commission is in partial agreement with Duke Kentucky on this issue and concludes that Duke Kentucky’s retirement plan expense should be *accepted as proposed*.³¹

The Commission allowed rate recovery of 401(k) matching contributions based on the following:

(1) Duke Energy had aggressively managed its retirement plan costs; (2) some Duke Energy employees were transitioned to a “cash balance benefit formula”; and (3) Duke Energy’s overall benefits package, including its retirement programs, is as a whole designed to be market competitive. The Commission should reach the same conclusion here.

Though the Companies have not locked, frozen, and replaced their DB Plan like Duke Energy did for a portion of their employees, the Companies did completely lock their DB Plan to *all* new entrants—both union and non-union employees—eight years *before* Duke Energy completely locked its DB Plan for certain employees. Nevertheless, the result of the Commission’s ruling is to allow 401(k) recovery for employees with a traditional defined benefit formula and for others with a cash balance defined benefit formula.³² Indeed, the Companies locked their DB Plan to all new entrants for anyone hired (or rehired) after December 31, 2005.³³

³¹ *In the Matter of: Electronic 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, Order at 22-23 (Ky. PSC Apr. 13, 2018) (emphasis added).

³² *Id.*

³³ Rebuttal Testimony of Gregory J. Meiman at 3.

As demonstrated in the record, the Companies have aggressively managed their benefit offerings. Even prior to the 2006 transition, the Companies managed the cost of providing retirement benefits by requiring employees to contribute to the cost of retirement through participation in the Savings Plan. By taking this contributory approach, as opposed to providing the entire retirement benefit in a traditional defined benefit, customers were not required to fully fund retirement expense, and employees were required to personally invest in their retirement. The Companies' 2005 decision established a path to completely eliminate the DB Plan structure³⁴ whereas a move to a cash balance plan structure (as Duke Energy did) does not alter the nature of employer risk.³⁵ Thus, (1) there have been no new participants eligible for the DB Plan for over thirteen years; (2) the number of eligible participants in the DB Plan began decreasing in 2006 and has been decreasing continuously since then; and (3) the number of eligible participants will eventually reach zero.³⁶ Of those remaining, the average age is approximately 54 years with approximately 28 years of experience.³⁷ A significant number of those employees are projected to retire in the next several years. Given the reasonableness of providing 401(k) matching contributions to those employees as demonstrated in the record and the Commission's approval of similar contributions in the Duke Energy case, the Companies should be allowed to honor their commitment to their employees while still providing service at fair, just and reasonable rates for their customers.

In addition to locking the DB Plan, the Companies have taken additional steps to manage retirement expense and reduce employer risk. In 2000, they merged their respective defined benefit plans to save administrative costs; in 2013 and again in 2014, they offered voluntary

³⁴ 3/5/19 Hearing, VR 2:37:15.

³⁵ Rebuttal Testimony of Gregory J. Meiman at 4-5; Meiman Rebuttal Exhibit A.

³⁶ Rebuttal Testimony of Gregory J. Meiman at 3.

³⁷ *Id.*

lump-sum elections rather than a monthly benefit; and, in 2016, they amended their DB Plan to make lump sum elections instead of a monthly benefit a permanent feature.³⁸ These actions demonstrate that the Companies' overall retirement benefits are aligned with market, which is the standard the Commission applies -- instead of "cherry-picking" a single aspect of benefits for an adjustment. As the Duke Energy witness aptly put it:

... the value of the Company's retirement benefit is what is important, rather than whether the Company chooses to deliver the value through multiple components. A one dollar bill has equal value to four quarters even though they are denominated in different forms."³⁹

And the Commission appears to agree that an evaluation of retirement benefits should consider the total benefit rather than a selective component.⁴⁰ Here, the Mercer Study valued the total benefit") and determined that the Companies' benefits package is reasonable. Likewise, the value of the Companies' retirement benefit is comparable to the benefits previously approved by the Commission, which included a cash balance defined benefit for certain employees.⁴¹ The point of overall value was important to the Commission in allowing rate recovery of 401(k) matching contributions for Duke Energy employees who also receive a defined retirement benefit from another funding source. It should likewise be important to the Commission in these cases. Even Mr. Kollen for KIUC noted that the Duke Energy decision may impact the Commission's decision here.⁴² And Ms. Mullinax offers nothing substantive to the contrary.

³⁸ Direct Testimony of Gregory J. Meiman Direct at 17-18.

³⁹ Case No. 2017-00321, Rebuttal Testimony of Thomas Silinski at 9 (Ky. PSC Filed Feb. 14, 2018).

⁴⁰ 3/5/19 Hearing, VR 10:11:08.

⁴¹ The values of the retirement benefit approved in Case No. 2017-00321 were 10.3% for those employees with a traditional or enhanced choice formula and 9.3% for those with cash balance formula. (Case No. 2017-000321, Duke Energy's Response to Commission Staff's Post-Hearing Data Requests, No. 4 (Ky. PSC Filed Mar. 23, 2018)). These percentages are comparable to the value of the Companies' benefit, which is 10.9%. Direct Testimony of Gregory J. Meiman at 22.

⁴² Direct Testimony of Lane Kollen at 46, n.46.

Additionally, elimination of 401(k) matching contributions for DB Plan participants *which have been in place for approximately 30 years* would mean that post-2006 hires would receive greater valued retirement benefits than pre-2006 hires, which, of course, runs counter to the concept of acknowledging employees with the most service and conflicts with the Companies' need to effectively manage the aggregate workforce of 3,600 employees.⁴³ However, in light of the Commission's decision in their 2016 rate cases, the Companies recognized the need to examine the entirety of their compensation and benefits to ensure reasonableness, which is exactly what they did.

As Mr. Meiman explained⁴⁴ and as the record shows, since the 2016 rate cases, the Companies: (1) commissioned the WTW Study to assess the entire compensation package against market which found total compensation to be at market;⁴⁵ (2) commissioned the Mercer Study to measure the entire benefits package against market which found that package to be at market;⁴⁶ (3) developed data on the effects of its retirement cost control efforts as a percentage of pay;⁴⁷ (4) negotiated new union contracts where needed;⁴⁸ (5) continued to implement various welfare benefit cost control measures;⁴⁹ and (6) were guided by the Commission's decision in the Duke Energy case, which was decided less than ten months after the Commission decided the

⁴³ Rebuttal Testimony of Gregory J. Meiman at 6; Direct Testimony of Gregory J. Meiman at 22.

⁴⁴ Rebuttal Testimony of Gregory J. Meiman at 11-12.

⁴⁵ See Applications, Tab 60, Attachment 3.

⁴⁶ See Applications, Tab 60, Attachment 4.

⁴⁷ Direct Testimony of Gregory J. Meiman at 22.

⁴⁸ *Id.* at 20.

⁴⁹ Those welfare benefit cost control measures include: 1996 implementation of premium sharing for medical and dental coverage; 2002 decision to self-insure medical coverage; 2008 increase in amounts employees pay for spousal coverage; 2012 additional increase for spousal coverage if a spouse works and is eligible under another plan; 2014 implementation of a tobacco user surcharge; 2014 shift to 100% of premium paid by employee for vision coverage; participation in a LiveHealth online program; implementation of many award-winning wellness initiatives which we call "Healthy for Life"; and 2017 efforts to ensure alignment with market levels by increasing employee out-of-pocket costs (comprised of deductibles, out-of-pocket maximums, copays, and co-insurance), imposition of additional prescription utilization management, and a recalibration of spousal coverage premiums. Direct Testimony of Gregory J. Meiman at 23-28.

Companies' 2016 cases. For these reasons, the Commission should approve rate recovery for all 401(k) matching contribution expense.

2. Other Revenue Requirement and Regulatory Issues Raised at the Hearing

a. A Slippage Adjustment is Unreasonable and Unnecessary

The Companies' budgeting process has proven to be reasonably accurate. The Companies use the same forecast presented in the rate case to plan their business, and the record does not show any pattern of overspending or underspending.⁵⁰ To the contrary, the evidence shows on average only minor differences between the budgeted amounts and the spent amounts.⁵¹ In fact, on average, the Companies have completed projects under budget, which benefits customers.⁵²

Perhaps most importantly, a slippage adjustment harms customers by incenting the Companies' to *not* control their capital construction costs. As Mr. Blake explained, a slippage factor creates a perverse incentive to spend all budgeted money on a project instead of continuing to look for ways to save money.⁵³ Indeed, if the slippage adjustment is applied symmetrically, it incents utilities to overspend their budgets in the years before filing a rate case.⁵⁴

Additionally, a slippage adjustment compounds regulatory lag, as suggested at the hearing.⁵⁵ Regulatory lag is a separate phenomenon that occurs regardless of whether a slippage

⁵⁰ See Rebuttal Testimony of Kent W. Blake, Exhibit KWB-5; 3/6/19 Hearing, VR 4:39:27; 3/6/19 Hearing, VR 4:48:55.

⁵¹ The 10-year average slippage factors for KU and LG&E are 97.969% and 97.029%, respectively. Rebuttal Testimony of Kent W. Blake, Exhibit KWB-5.

⁵² *Id.*; 3/6/19 Hearing, VR 4:49:20.

⁵³ 3/6/19 Hearing, VR 4:40:35; 3/6/19 Hearing, VR 4:49:20 ("It sort of does get to the point of . . . I want to get to a 100% slippage factor so I better make sure I spend every dollar I have in my budget.").

⁵⁴ *In the Matter of: Application of Kentucky-American Water Company to Increase Its Rates*, Case No. 95-554, Order (Ky. PSC Sept. 11, 1996).

⁵⁵ 3/6/19 Hearing, VR 4:40:46.

factor is applied.⁵⁶ Finally, not imposing a slippage adjustment remains consistent with past Commission's precedent both in the Companies prior rate cases and in decisions for all utilities, in which the Commission has rarely applied slippage adjustments.⁵⁷

b. Capitalization Remains the Reasonable Valuation Method

The use of capitalization is supported by Kentucky law, Commission precedent, and the Stipulation. Consistent with the Companies' approach in at least their six most recent base rate cases,⁵⁸ the Companies valued their property in this proceeding using the capitalization methodology. Where, as here, rate base and capitalization result in similar values, capitalization should always be chosen because it is the most objective measure of valuation and reflects the actual value of the capital supporting the assets used to provide service to customers. Mr. Blake put it best at the hearing: "Capitalization is the actual amount of funds needed to fund capital investment and operations."⁵⁹ The Commission has agreed, recognizing that the "capitalization of the utility is a better measure of the real cost of providing service."⁶⁰ Rate base, in contrast, relies on a theoretical calculation to determine the extent to which the Companies fund their working capital.

⁵⁶ 3/6/19 Hearing, VR 4:47:40.

⁵⁷ With the exception of rate proceedings involving Kentucky-American Water Company ("KAWC"), the Commission appears to have applied a slippage adjustment in only one other proceeding. *In the Matter of: An Adjustment of the Gas Rates of Union Heat, Light and Power Company*, Case No. 2005-00042, Order (Ky. PSC Dec. 22, 2005). The Commission's treatment of KAWC appears to be based upon historic concerns regarding that utility's budgeting process.

⁵⁸ The Companies also continued to use capitalization with the recognition that Kentucky law and Commission precedent favor a utility's continued use of the same method of valuation. KRS 278.290 requires the Commission to consider the history and development of the utilities and their property and other elements of value long recognized for ratemaking purposes. The Commission has indicated a preference for a utility to continue using the property valuation methodology it has historically used. *In the Matter of: The Application of Louisville Gas & Electric Company to Adjust Its Gas Rates and to Increase Its Charges for Disconnecting Service, Reconnecting Service and Returned Checks*, Case No. 2000-00080, Order at 7 (Ky. PSC Sept. 27, 2000).

⁵⁹ 3/6/19 Hearing, VR 4:15:27.

⁶⁰ Case No. 2000-00080, Order at 11 (Ky. PSC Sept. 27, 2000).

Additionally, the inquiries at the hearing do not support a departure from the Companies' long-standing use of capitalization. As Mr. Blake testified, the Companies' funding of operating expenses with short-term debt does not favor the use of rate base because such funding causes increases to both capitalization and rate base.⁶¹ And, as the inquiries demonstrated, it is not feasible to determine the extent to which operating expenses have been funded through capitalization; as such a determination would require going back to the start of time for each utility.⁶²

The Commission has stated that it "will consider using a [valuation] approach different from that previously used" only if a justification exists.⁶³ No such justification exists in this record. Customers will not be harmed by the Companies' continued use of capitalization to value their property.⁶⁴

c. The Companies Have a Reasonable CPCN Policy

The Companies responded to a number of inquiries regarding their process utilized in determining whether to request a Certificate of Public Convenience and Necessity ("CPCN"), describing in detail their process of determining whether to request a CPCN.⁶⁵ KRS 278.020(1) and 807 KAR 5:001, Section 15(3), together, identify those facilities for which a CPCN is not

⁶¹ 3/6/19 Hearing, VR 4:17:07 ("There is an allowance created for the funding of operating expenses through working capital allowance within a rate base calculation just like there is an actual capitalization increase to cover basically net of operating cash flows versus investing activity.").

⁶² 3/6/19 Hearing, VR 4:17:45.

⁶³ Case No. 2000-00080, Order at 7 (Ky. PSC Sept. 27, 2000).

⁶⁴ In fact, the Companies have committed to continuing to use capitalization in future cases, even if it produces a valuation that is lower than rate base. KU Response to AG's First Request for Information, No. 30; LG&E Response to AG's First Request for Information, No. 30.

⁶⁵ See LG&E's Response to DR No. 58 of the Commission Staff's Second Request for Information, KU's Response to DR 49 of the Commission Staff's Second Request for Information and the Companies' Responses to DR No. 20 of the Commission Staff's Third Request for Information; *see also* the Companies' Responses to DR No. 17 of the Commission Staff's Fourth Request for Information;

required.⁶⁶ The Commission has distilled its regulation into a review of three factors, holding that a CPCN is not necessary “for facilities that do not result in the wasteful duplication of utility plant, do not compete with the facilities of existing public utilities, and do not involve a sufficient capital outlay to materially affect the existing financial condition of the utility involved or to require an increase in utility rates.”⁶⁷ The Companies center their analysis on this and other Kentucky law and regulations, and Commission orders and Commission Staff Opinions.

As to the first factor, when determining whether the proposed project will duplicate any existing facilities, the Companies assess whether the proposed facilities are intended to serve unserved or underserved areas, meet additional demands due to customer growth, or whether portions of the project replace, repair or refurbish existing facilities. If so, they are not considered to be duplicative. Similarly, the Companies consider whether the planned facilities are necessary to comply with statutory or regulatory requirements, and, if so, they are not considered duplicative. As to the second factor, the Companies examine whether the proposed facilities will compete with the facilities of other utilities given the constraints of the territorial boundary law. As to the third factor, the Companies consider whether a proposed project will materially affect their respective existing financial conditions by comparing the proposed project’s cost with the relevant Company's current net utility plant.⁶⁸

⁶⁶ *The Application of Northern Kentucky Water District (A) For Authority to Issue Parity Revenue Bonds in the Approximate Amount of \$16,545,000; and (B) A Certificate of Convenience and Necessity for the Construction of Water Main Facilities*, Case No. 2000-481 (Ky. PSC Aug. 30, 2001) at 4 (referring to §15(3) prior to revisions in 807 KAR 5:001 resulted in renumbering).

⁶⁷ *Id.*

⁶⁸ *Application of Northern Kentucky Water District for Approval of Dixie Highway Water Main Improvements, Issuance of a Certificate of Convenience and Necessity and Approval of Financing*, Case No. 2014-00171 (Ky. PSC Aug. 6, 2014)(“In assessing whether a proposed project is a system extension in the ordinary course of business, Kentucky courts have traditionally looked to the size and scope of a project in the context of the monetary cost involved. The Commission has similarly adopted this method and likewise looks to the scale of a proposed project in relation to the relative size of the utility and its present facilities.”)

In considering any discrete project, it may be tempting to ask why the Companies did not request a CPCN or seek a Staff Opinion as to whether a CPCN should be obtained. Neither approach is feasible or efficient given the number of capital projects the Companies must undertake each year, especially for the repair and replacement of existing facilities. The Companies' capital budgets contain hundreds of projects each year; over the last ten years KU and LG&E have each engaged in over 12,000 capital construction projects.⁶⁹ KU's Kentucky jurisdictional capitalization is \$4.08 billion and its rate base is \$4.05 billion and LG&E electric and gas capitalization is \$3.36 billion and its combined rate base is \$3.32 billion.⁷⁰ If the Companies requested a CPCN or obtained a Staff Opinion for even half of the projects in their capital budgets, it would increase regulatory expense, delay the completion of ordinary repairs, result in a significant upsurge of cases filed with the Commission, and impede the Companies from providing responsive, efficient customer service.

The Companies review and consider the Commission's orders that provide guidance as to when a CPCN is necessary. This precedent continues to evolve, especially with regard to the relative magnitude of the capital outlay that may trigger the request for a CPCN. Based upon a review of the decisions of the Commission to date and given the size of the Companies' net utility plant, the Companies believe that a standard of zero to five percent of its current net utility plant should be utilized when evaluating the need for a CPCN for an investor owned utility.⁷¹ If a project's expected cost represents five percent or less of the current net utility plant, it should

⁶⁹ See KU Response to Commission Staff's First Request for Information, No. 13(a); LG&E Response to Commission Staff's First Request for Information, No. 13(a).

⁷⁰ Rebuttal Testimony of Christopher M. Garrett at 6.

⁷¹ See, e.g., *Application of Madison County Utility District for an Order Issuing a Certificate of Public Convenience and Necessity and for Authority to Borrow Funds and to Refinance Certain Indebtedness of the District*, Case No. 2007-00424 (Ky. PSC Mar. 20, 2008) (five percent of net utility plant);

be considered as having no material effect on the investor owned utility's financial condition and therefore no CPCN should be required.

B. The Stipulation's Recommended Revenue Allocation and Rate Design are Fair, Just, and Reasonable

The Companies and several parties took a variety of positions on how the increase in electric revenue should be allocated.⁷² The Stipulation sets forth in detail a comprehensive resolution of these issues, with one exception, that all parties support as a reasonable outcome.

At the hearing, Mr. Seelye presented the work paper used during the settlement to illustrate how the recommended allocation of the increase in electric revenues reflects a compilation of, and compromise between, the positions of the Companies and the parties.⁷³ The more detailed actual allocations by specific customer class can be found on Schedule M-2.1 in Stipulation Exhibits 3 and 4.

For its gas line of business, LG&E proposed an overall revenue increase of 7.50%.⁷⁴ Because the rates of return on the Residential Gas Service rate class and the Commercial Gas Service rate class were significantly lower than for the other rate classes, LG&E recommended that all of the revenue increase be allocated to these two rate classes.⁷⁵ The proposed revenue increase was 8.12% for each of these classes.⁷⁶ Although none of the intervenor witnesses opposed LG&E's position,⁷⁷ the Stipulation recommends a lower increase of 6.30% for each of the classes.⁷⁸

⁷² Compare Direct Testimony of Robert M. Conroy and Direct Testimony of William Steven Seelye *with* intervenor testimony by AG witness Watkins, KIUC witness Baron, DOD witness Selecky, and Walmart witness Tillman.

⁷³ 3/6/19 Hearing, VR 12:58:00; LG&E and KU Hearing Room Exhibit 1.

⁷⁴ Direct Testimony of William Steven Seelye at 50.

⁷⁵ *Id.* at 50-51.

⁷⁶ *Id.* at 51.

⁷⁷ Rebuttal Testimony of William Steven Seelye at 28.

⁷⁸ Stipulation Exhibit 5, Page 1 of 11.

The Commission should approve the Stipulation's allocations and associated rate design as a reasonable resolution of this highly disputed issue.

1. The Companies' Proposed Residential Basic Service Charges are Reasonable

The Stipulation did not address the amount of the residential Basic Service Charges ("BSCs") and related issues, reserving resolution of those issues for the hearing. Philosophical differences regarding the purpose of BSCs and how such charges should be calculated caused the impasse on this issue.

The record of evidence demonstrates that the Companies' proposed residential electric and gas BSCs are cost-of-service supported, comport with gradualism, and will increase conservation incentives more than current rates.⁷⁹ In short, the Companies' proposed BSCs meet all of the criteria the Commission has established for customer charges and therefore should be approved as proposed.

No party disputed that the Companies' proposed residential electric and gas BSCs are consistent with their cost-of-service studies. No party challenged the Companies' zero-intercept analyses, which the Commission has long recognized or endorsed for classifying distribution assets,⁸⁰ nor did they assert that the analyses were inconsistent with the NARUC Electric Utility Cost Allocation Manual, which the Commission has repeatedly cited as an authority to follow.⁸¹

⁷⁹ Net of Tax Cuts and Jobs Act surcredits, which are applied on kWh and Ccf bases for residential rates. See Kentucky Utilities Company, P.S.C. No. 18, Second Revision of Original Sheet No. 89; Louisville Gas and Electric Company, P.S.C. Electric No. 11, Second Revision of Original Sheet No. 89; Louisville Gas and Electric Company, P.S.C. Gas No. 11, Second Revision of Original Sheet No. 89.

⁸⁰ See, e.g., *In the Matter of: Application of Licking Valley Rural Electric Cooperative Corp. to Adjust Electric Rates*, Case No. 98-321, Order at 16 (Ky. PSC Feb. 16 1999) ("According to the 1992 Electric Utility Cost Allocation Manual of the National Association of Regulatory Utility Commissioners (NARUC Manual), the Minimum-Intercept method yields the most accurate allocation to the customer component."); *In the Matter of: an Adjustment of Gas and Electric Rates of the Union Light, Heat, and Power Company*, Case No. 90-041, Order at 55 (Ky. PSC Oct. 2, 1990) ("The Commission has even endorsed the zero-intercept methodology as an appropriate way to determine the customer-related component."); *In the Matter of: an Adjustment of Rates of Columbia Gas of Kentucky, Inc.*, Case No. 10201, Order at 53-54 (Ky. PSC Oct. 21, 1988) ("The Commission is of the opinion that

The Companies' proposed charges increase the current levels moderately, moving gradually toward cost-of-service. Based on the Companies' cost of service studies, KU's residential customer-related cost was calculated to be \$23.89 per month and LG&E's residential customer-related cost was calculated to be \$20.34 per month.⁸² The Companies are proposing an increase of the BSC for residential customers from an equivalent monthly charge of \$12.25 to \$16.13,⁸³ well under the 50% guideline prescribed by the Commission.⁸⁴ The Commission has approved and encouraged the principle of gradualism for almost 40 years.⁸⁵

The AG's position stands in stark contrast to the Commission's long-standing policy toward cost-based ratemaking, advocating a minimalist approach that disregards which components of distribution costs are demand- or customer-related.⁸⁶ Instead, the AG's witness, Glenn Watkins, advocates for BSCs that recover only the cost of connecting customers to the

the zero-intercept methodology is an acceptable way to divide distribution main costs into demand-related and customer-related components. . . . The Commission is of the opinion and finds that Columbia should maintain the data necessary to accurately perform a zero-intercept study"); *In the Matter of: Adjustment of Gas and Electric Rates of Louisville Gas and Electric Company*, Case No. 10064, Order at 83 (Ky. PSC July 1, 1988) ("Furthermore, the Commission will continue to accept the zero-intercept methodology for the allocation of distribution costs between customer and demand components of the cost of service study.").

⁸¹ Case No. 98-321, Order at 16 (Ky. PSC Feb. 16 1999) ("According to the 1992 Electric Utility Cost Allocation Manual of the National Association of Regulatory Utility Commissioners (NARUC Manual), the Minimum-Intercept method yields the most accurate allocation to the customer component."); Case No. 90-041, Order at 55 (Ky. PSC Oct. 2, 1990) ("ULH&P followed the guidelines published in the NARUC 'Electric Utility Cost Allocation Manual' to develop KW, KWH, and customer allocation factors The allocation of electric expenses and investments follow methodologies and procedures approved in previous proceedings and accepted by the NARUC. Therefore, ULH&P's electric cost-of-service study is approved as a basis for rate design.").

⁸² See Direct Testimony of William Steven Seelye, Exhibit WSS-2.

⁸³ *Id.* at 13.

⁸⁴ See, e.g., *In the Matter of Application of Farmers Rural Electric Cooperative Corporation for an Increase in Retail Rates*, Case No. 2016-00365, Order at 14 (Ky. PSC May 12, 2017) ("Farmers' proposed increase in the residential customer charge from \$9.35 to \$14.00 results in a 50 percent increase, which support the general principle of gradualism.")

⁸⁵ See, e.g., *In the Matter of: Consideration of the New Federal Standards of the Energy Independence and Security Act of 2007*, Case No. 2008-00408, Order at 63 (Ky. PSC Oct. 6, 2011) ("As to rate design and rate structure, the Commission notes its consistent position that rates should be cost-based. That position was set forth in Administrative Case No. 203 where, among other standards, the Commission adopted the PURPA cost-of-service standard which requires the rates charged to each class to be designed to reflect the cost to serve each class."), citing *The Determinations with Respect to the Ratemaking Standards Identified in Section 11 1 (d)(1)-(6) of the Public Utility Regulatory Policies Act of 1978*, Administrative Case No. 203, Order at 7-9 (Ky. PSC Feb. 28, 1982).

⁸⁶ See Direct Testimony of Glenn A. Watkins at 32-38, Scheds. GAW-5, GAW-6.

Companies' electric and gas distributions systems.⁸⁷ Mr. Watkins asks the Commission to engage in this flawed logic by asserting that such rates better reflect pricing in competitive markets.⁸⁸ However, competitive markets that have relatively high fixed capital costs and relatively low incremental costs of production, e.g., cell-phone service, Internet service, and rental cars, often use exclusively fixed pricing.⁸⁹

As Commission Staff's cross-examination of Mr. Conroy showed,⁹⁰ the Companies' proposed BSCs would have little to no effect on customers' ability to save money if they use less energy. For example, under the stipulated KU residential revenue allocation and the Companies' proposed electric BSC, a KU residential customer who chose to reduce average monthly consumption by 100 kWh would save about \$9.10 per month, whereas retaining KU's current BSC with the stipulated revenue allocation would result in savings of \$9.45.⁹¹ The notion that a \$0.35 per month saving difference compared to a total monthly savings of over \$9.00 would have any material effect on a customer's incentive to conserve energy is unreasonable. Approving the Companies' proposed residential electric and gas BSCs will move the charges closer to cost of service, will be consistent with the principle of gradualism, and will not harm current conservation incentives.

Moreover, the Commission has been exceedingly clear in its recent orders that utilities should collect most, if not all, customer-related costs through customer charges rather than volumetric rates.⁹² Perhaps most notably, the Commission rejected Mr. Watkins' substantively

⁸⁷ *Id.*

⁸⁸ See Direct Testimony of Glenn A. Watkins at 24-28.

⁸⁹ See Rebuttal Testimony of William Steven Seelye at 38-39.

⁹⁰ 3/6/19 Hearing, VR 10:57:00 – 11:00:02.

⁹¹ KU Response to Commission Staff Stipulation, No. 1. See also LG&E Response to Commission Staff Stipulation, No. 1.

⁹² *In the Matter of: Electronic Application of Water Service Corp. of Kentucky for a General Adjustment in Existing Rates*, Case No. 2018-00208, Order at 21 (Ky. PSC Feb. 11, 2019) (“While the proposed monthly service charge

identical customer cost analysis⁹³ performed in Duke Energy Kentucky’s 2018 rate proceeding.⁹⁴ In its final order, the Commission granted Duke a more than 140% increase in its residential customer charge to a level just \$0.31 below the cost of service support Duke had provided for its proposed increase.⁹⁵

Mr. Watkins’s supporting authorities are problematic. First, regarding his quotation from Prof. Bonbright’s treatise, the passage concerns classification and revenue allocation, not ratemaking per se, which Mr. Watkins contends to be entirely distinct activities (contrary to the Commission’s long-held view).⁹⁶ Second, Mr. Watkins’s citation to what he characterizes as “a NARUC Publication entitled Charging for Distribution Utility Services: Issues in Rate Design,”⁹⁷ is not a NARUC publication at all,⁹⁸ and it does not purport to represent NARUC’s views.⁹⁹ The document also advocates policy positions that are contrary to Kentucky law, because KRS 278.018 forbids retail competition in electric service and the Commission has stated that environmental concerns are outside its jurisdiction.¹⁰⁰

does not completely recover customer costs, the Commission approves the proposed increase as it recovers a greater percentage of customer costs than the present customer charge and moves the utility closer to completely cost-based rates.”); *In the Matter of: Electronic 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, Order at 42-45 (Ky. PSC Apr. 13, 2018).

⁹³ See Direct Testimony of Glenn A. Watkins, Scheds. GAW-5, GAW-6; Case No. 2017-00321, Order at 43-44 (Ky. PSC Apr. 13, 2018).

⁹⁴ Case No. 2017-00321, Order at 42-45 (Ky. PSC Apr. 13, 2018).

⁹⁵ *Id.* at 44-45.

⁹⁶ Direct Testimony of Glenn A. Watkins at 36. See also 3/6/19 Hearing, VR 3:16:22 – 3:18:00.

⁹⁷ Direct Testimony of Glenn A. Watkins at 37.

⁹⁸ Case No. 2018-00294, Attachment to AG Response to Commission Staff, No. 15; Case No. 2018-00295, Attachment to AG Response to Commission Staff, No. 17.

⁹⁹ *Id.* at 1.

¹⁰⁰ See, e.g., *In the Matter of the Joint Application Pursuant to 1994 House Bill No. 501 for the Approval of Kentucky Power Company Collaborative Demand-Side Management Programs, and for Authority to Recover Costs, Net Lost Revenues and Receive Incentives Associated with the Implementation of Three New Residential Demand-Side Management Programs beginning January 1, 2009*, Case No. 2008-00349, Order at 4 (Ky. PSC Dec. 4, 2008) (“[T]he Commission has no jurisdiction over the quality of the air . . . , the ‘significant health problem’ associated with mercury pollution from coal-fired power plants, or ‘the carbon dioxide released [which] contributes to global warming.’ . . . [T]he Commission’s jurisdiction is limited to the ‘rates’ and ‘service’ of utilities.”).

In addition, the Virginia and Washington commission orders Mr. Watkins cited as adopting his minimalist approach either do not do so or are inapposite.¹⁰¹ First, the Virginia State Corporation Commission (“VSCC”) authority he cites clearly states that the VSCC was *not* adopting any particular approach to setting customer charges.¹⁰² Second, as Commission Staff noted at hearing, the Washington Utilities and Transportation Commission (“WUTC”) orders cited by Mr. Watkins also either advocate for,¹⁰³ or note the existence of decoupling mechanisms for affected utilities.¹⁰⁴ As the WUTC has stated, the purpose of a decoupling mechanism is to eliminate the “throughput incentive,” essentially ensuring utilities recover their costs regardless of how much energy they sell.¹⁰⁵ Advocating for guaranteeing utilities’ cost recovery is inconsistent with Mr. Watkins’s implicit criticism of the Companies as seeking increased BSCs to “guarantee revenue collection and profitability.”¹⁰⁶ The Companies respectfully recommend that the Commission continue its longstanding and consistent policy of moving utilities’

¹⁰¹ See AG Response to Companies’ Request for Information, No. 10.

¹⁰² Attachment A to AG Response to Companies’ Request for Information, No. 10, Virginia State Corporation Commission, Case No. PUE-2014-00020, Columbia Gas of Virginia, Order at 6 (“[W]e do not approve a bright-line rule of what costs may or may not be included in the fixed customer charge. Rather, the Commission’s findings in the instant case are based on the specific facts as presented in this proceeding. As noted in the Company’s comments, the Commission has historically exercised discretion in determining the appropriate level of customer charges based on the facts and circumstances of each case. That is what we have done here and we need not adopt a bright-line rule governing what costs may or may not be included in a fixed customer charge.”).

¹⁰³ See Attachment B to AG Response to Companies’ Request for Information, No. 10, Washington Utilities and Transportation Commission, Docket No. UE-140762, Pacific Power & Light Company, Order 08 at page 87, paragraph 206 (“Staff supports its proposed increase in the basic charge by reasoning that ‘in the absence of a decoupling mechanism to reduce Pacific Power’s risk of under-recovering fixed costs due to declining load, it is appropriate to shift the distribution of the Company’s cost recovery toward fixed sources of recovery, such as the monthly basic charge.’”). See also *id.* at pages 92-94, paragraphs 220-222.

¹⁰⁴ See Attachment C to AG Response to Companies’ Request for Information, No. 10, Washington Utilities and Transportation Commission, Docket Nos. UE-170033 and UG-170034, Puget Sound Energy, Order 08 at page 120, paragraph 357 (“Transformer costs should be recovered as distribution charges subject to PSE’s electric decoupling mechanism, which adequately protects the Company’s recovery of its fixed costs.”).

¹⁰⁵ Attachment B to AG Response to Companies’ Request for Information, No. 10, Washington Utilities and Transportation Commission, Docket No. UE-140762, Pacific Power & Light Company, Order 08 at pages 93-94, paragraph 221 (“By ‘decoupling’ sales from revenues, a utility should no longer be encouraged to sell more energy, and conserve less, in order to earn more profit. Ending this so-called ‘throughput incentive’ is the essence of a full decoupling mechanism.”).

¹⁰⁶ Direct Testimony of Glenn A. Watkins at 22.

customer charges toward levels consistent with their cost-of-service studies by approving the Companies' proposed residential electric and gas BSCs.

There was an extended discussion at hearing regarding the effects of increased residential BSCs on low-income customers.¹⁰⁷ The Commission issued its seminal decision on the propriety of setting rates based on income levels more than a decade ago, and has not deviated from it since.¹⁰⁸ Earlier this year the Commission reiterated its position on this issue, stating, “[A]ffordability is not a factor that the Commission can consider because KRS 278.170(1) prohibits rates that establish an unreasonable preference between classes of service for doing a like service under the same or substantially the same conditions.”¹⁰⁹ The Commission further noted that the U.S. Supreme Court has held that a customer’s ability to pay is not a focus of a regulatory agency, which “is charged with both assuring the public of reliable, efficient service at a reasonable price and assuring the utility that it may collect fair, just, and reasonable rates.”¹¹⁰ Moving increasingly toward cost-of-service based BSCs consistent with the ratemaking principle of gradualism is the appropriate course for the Commission to follow for the benefit of all customers.

In response to AG witness Melissa Tibbs’s assertion that “[t]he proposed basic service charge (customer charge) increase will greatly add to the burden of a rate increase on customers with low income,”¹¹¹ Mr. Conroy demonstrated that the assertion could not be universally true for low-income customers precisely because of the only available evidence regarding the usage

¹⁰⁷ See, e.g., 3/6/19 Hearing, VR 10:24:00 – 10:28:00.

¹⁰⁸ *In the Matter of: Application of Kentucky-American Water Company for an Adjustment of Rates* Case No. 2004-00103, Order at 82-83 (Feb. 28, 2005) (“[T]he proposed discount is an unreasonable preference or advantage to a class of customers for ‘a like and contemporary service under the same or substantially the same conditions’ and is one that KRS 278.170(1) prohibits.”)

¹⁰⁹ *In the Matter of: Electronic Application of Kentucky-American Water Company for an Adjustment of Rates*, Case No. 2018-00358, Order at 3 (Ky. PSC Jan. 3, 2019).

¹¹⁰ *Id.* citing *Gainesville Util. Dept. v. Fla. Power Corp.*, 402 U.S. 515, 528 (1971).

¹¹¹ Direct Testimony of Melissa Tibbs at 13, lines 13-14.

of customers receiving third-party assistance.¹¹² The data in the record show that the Companies' residential electric and gas customers who received third-party assistance had above-average usage in the periods about which the low-income advocates requested information.¹¹³ But the Companies are *not* contending that all low-income customers have above-average usage or that all low-income customers on average have above-average usage.

During the hearing, the AG argued that U.S. Census Bureau statistics about poverty levels in 12 Jefferson County zip codes coupled with average usage data for LG&E customers in those zip codes somehow demonstrated that low-income customers have below-average usage.¹¹⁴ The AG's argument is undercut by this fact: the U.S. Census Bureau does not disclose the identity of the low-income customers in the cited zip codes; so there is no way to determine those customers' usage. Thus, there is no way to know the average annual usage of the low-income customers in any single zip code. Moreover, the Companies serve residential electric customers in over 350 zip codes in Kentucky.¹¹⁵ Therefore, no statistically defensible inference can be drawn from the information advanced by the AG at hearing for even a zip code, or for the entirety of the Companies' combined service territory.

Finally, the Companies remain committed to assisting low income customers by providing significant shareholder assistance, well-funded HEA and other assistance programs, a robust low-income-targeted DSM program (WeCare), budget billing, flexible payment plans, and significant volunteer contributions from the Companies' employees and customers.¹¹⁶ In addition, the Companies work closely with low-income advocates across numerous programs to

¹¹² Rebuttal Testimony of Robert M. Conroy at 22.

¹¹³ Case No. 2018-00294, KU Responses to CAC Requests for Information, Nos. 1-15 and 1-16; Case No. 2018-00295, Attachments to LG&E Responses to ACM Requests for Information, Nos. 1-5(a)(b), 1-6(a)(b).

¹¹⁴ See, e.g., 3/6/19 Hearing, VR 10:24:00 – 10:28:00.

¹¹⁵ See attachment to LG&E Response to ACM First Requests for Information,7(a); attachment to KU Response to CAC First Requests for Information, No. 2. (LG&E serves 54 zip codes; KU serves 304 zip codes).

¹¹⁶ See Direct Testimony of Robert M. Conroy at 45-50.

exchange information and provide aid to customers in need. These are the appropriate means for addressing these issues. Setting residential BSCs to benefit one portion of the residential class based on income levels is neither legally permissible nor demonstrably helpful to the very customers sought to be helped.

2. Providing Customers More Accurate Information through Daily BSC and Splitting Energy Charge Empowers Customers and More Closely Aligns With Cost-Causation Principles

There is no dispute that the Companies' proposed daily BSCs will more accurately reflect underlying costs on the Companies' tariffs and customers' bills. Indeed, even Mr. Watkins did not dispute that point at hearing, but rather attempted to counter the Companies' substantive position by merely asserting, "If it ain't broke, don't fix it."¹¹⁷ His simple argument misses the point: daily BSCs more accurately communicate to customers the costs incurred over each billing period, which vary in the number of days billed. Each customer's bill will clearly state the number of days in the billing cycle, show the calculation of the daily BSC times the number of days in the billing cycle, and display the total amount of the BSC included in the customer's bill. While the amount of the BSC could vary from month to month, such variation will be immaterial compared to the variation that occurs month to month because of changes in consumption. Such change in consumption can be significant from month to month. Also, use of a daily BSC is not new to the utility industry and the Commission has approved daily BSCs for Meade County Rural Electric Cooperative Corporation for a number of years.¹¹⁸

¹¹⁷ 3/6/19 Hearing, VR 2:47:55 – 2:48:00. Note that Mr. Watkins then essentially contradicted himself moments later by asserting that he is not opposed to innovation. 3/6/19 Hearing, VR 2:49:44.

¹¹⁸ See, e.g., *In the Matter of: Application of Meade County Rural Electric Cooperative Corp. for Pass-Through of Big Rivers Electric Corporation Wholesale Rate Adjustment*, Case No. 2013-00321, Order at Appendix page 1 (Ky. PSC Apr. 25, 2014).

In addition, as Mr. Watkins noted at hearing, a daily BSC can better enable different kinds of rate structures customers might desire in the future, including prepaid service.¹¹⁹ Therefore, there are multiple substantive reasons to approve the Companies' proposed residential daily BSCs—e.g., better alignment with cost causation and enabling new rate structures—and no substantive reasons to oppose them.

Moreover, as Mr. Seelye noted in his rebuttal testimony, more than 30 years ago the Commission directed LG&E to do in its gas tariffs what the Companies are now proposing to do with their non-demand electric tariffs:

LG&E proposed to retain the total rate per 100 cubic feet authorized in its last rate case, which includes 35.720 cent as gas costs, rather than putting all gas costs in the GSCA determined in the quarterly filing. To avoid customer confusion at the present time, the Commission will allow such practice. *However, with LG&E's next rate case all gas costs will be included in the GSCA and all other costs will be set out as the distribution cost.*¹²⁰

LG&E did what the Commission directed in subsequent rate applications, and LG&E's current gas tariff continues to reflect that Commission-directed division of costs.¹²¹

In sum, the Commission should therefore approve the Companies' BSCs and proposal to split the energy charge for non-demand rate schedules for tariff purposes only.

II. PSA Stipulation

The PSA Stipulation between the Companies and Charter is reasonable and advances the ongoing efforts to modernize the Companies' pole attachment tariffs to reflect the changing conditions of the twenty-first century. It makes clear who may use the Companies' pole space,

¹¹⁹ 3/6/19 Hearing, VR 2:50:00 – 2:51:44.

¹²⁰ Rebuttal Testimony of William Steven Seelye at 42, quoting Case No. 9133, Order at 2 (Ky. PSC Jan. 7, 1985) (emphasis added).

¹²¹ See, e.g., Louisville Gas and Electric Company, P.S.C. Gas No. 11, Seventh Revision of Original Sheet No. 5 (showing Distribution Charge of \$0.36300 per Ccf and Gas Supply Cost Component of \$0.42104 per Ccf, for a Total Gas Charge per 100 cubic feet of \$0.78404).

reduces financial risks to the Companies and their electric service ratepayers from third parties' use of pole space, encourages greater compliance with the Rate PSA's terms, and enhances protections for worker and public safety and electric service reliability.

Prior to July 1, 2017, the Companies' pole attachment tariffs addressed only pole attachment service to cable television providers. Other entities, such as telecommunication carriers, governmental entities, and educational institutions, had to enter into license agreements that set forth the terms and conditions for placing attachments on the Companies' poles and structures. In the current proceedings, the Companies have again proposed revisions to their PSA tariffs, including: application of the rate schedule to governmental entities and educational institutions and revisions to ensure a more accurate assignment of costs, encourage greater compliance with the Rate PSA's permitting provisions, and, most importantly, provide greater protection for worker and public safety and the integrity of the Companies' distribution systems.

Only Charter opposed some of the proposed revisions. It objected to the direct assessment of audit costs, the penalty for unauthorized attachments, the requirement of a company-inspector for self-help make ready work, and the surcharge for Company corrections to non-compliant attachments.

The Companies and Charter have agreed to modifications of the Companies' original proposal to address Charter's concerns while still improving the existing Rate PSA in these areas, which the PSA Stipulation and the Stipulation Testimony of John K. Wolfe describe in detail.¹²²

In summary, the PSA Stipulation's recommendations concerning the proposed changes to the Companies' PSA tariff permit the continued modernization of the Companies' practices and

¹²² Stipulation Testimony of John K. Wolfe at 2-7. For the textual revisions to the Companies' proposed Rate PSA, see Exhibits 1 and 2 to the PSA Stipulation.

policies regarding pole and structure attachments, ensure a more accurate assignment of the costs and risks related to such attachments, and promote worker and public safety and system reliability to the benefit of all the Companies' customers. The Commission should approve the PSA Stipulation.

CONCLUSION

For the reasons stated in this brief and the record, Kentucky Utilities Company and Louisville Gas and Electric Company request the Commission issue an order by April 30, 2019 granting the Companies the following relief:

A. The Commission should accept the Stipulations as the reasonable disposition of the revenue requirements, revenue allocations, and rate design issues.

B. The Commission should approve the proposed changes in rates, terms and conditions set forth in Stipulations for service rendered by KU and LG&E on and after May 1, 2019.

C. The Commission should acknowledge the expiration of the Tax Cuts and Job Act Surcredit effective with approved change in base rates for service rendered on and after May 1, 2019 in accordance with the Commission's Order dated March 20, 2018 in Case No. 2018-00034.¹²³

D. The Commission should approve the depreciation rates set forth in the Stipulation as reasonable for KU and LG&E.

E. The Commission should approve the amortization amounts associated with the KU and LG&E regulatory liabilities for the state tax reform amounts and for the refined coal

¹²³ By Order dated March 20, 2018, in Case No. 2018-00034, the Commission approved an *Offer and Acceptance of Satisfaction* providing that KU and LG&E "will continue to impose on the bills of their customers the [TCJA Surcredit], adjusted to reflect estimated annual Tax Act benefits, until such time as new base rates resulting from applications to change base rates take effect."

contracts associated with the Mill Creek and Trimble County generation stations, and the KU and LG&E regulatory assets for costs related to the July 2018 storm.

F. The Commission should approve for KU and LG&E the continued use of deferral accounting associated with the generator outage expenses, the regulatory asset accounting of the amounts of late payment charge waivers actually granted, and the regulatory liability accounting for any reduction in costs resulting from the reduction or elimination of the merger mitigation de-pancaking component of transmission Rate Schedule No. 402.¹²⁴

G. The Commission should approve for KU the regulatory asset accounting for the remaining inventory values of Brown Units 1 and 2 and the regulatory asset accounting for the Brown Unit 1 repair expense and a three-year amortization of that asset.

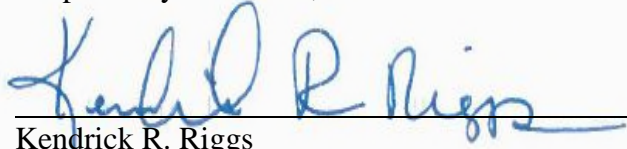
H. The Commission should determine the Companies' employee compensation and benefits in the aggregate is reasonable.

I. The Commission should approve the Companies' proposed residential Basic Service Charges as reasonable and further determine that providing customers more accurate information through a daily Basic Service Charge and splitting the energy charge on the Companies' tariffs, as proposed by the Companies, empowers customers and more closely aligns with cost-causation principles and approve the same.

¹²⁴ *Joint Application Under FPA Section 203 and Section 205 of Louisville Gas and Electric Company and Kentucky Utilities Company*, FERC Docket Nos. EC98-2-00 and ER1 8-2162-000. The Federal Energy Regulatory Commission conditionally granted the Companies' request to remove the merger mitigation de-pancaking component, subject to a transition mechanism for the Transition Customers; *See Louisville Gas and Elec. Co. and Kentucky Utilities Co.*, 166 FERC ¶ 61,206, at P 2, 35 (2019) (March 21, 2019).

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Respectfully submitted,



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CERTIFICATE OF COMPLIANCE

In accordance with 807 KAR 5:001 Section 8(7), this is to certify that Kentucky Utilities Company's and Louisville Gas and Electric Company's April 1, 2019 electronic filing of their Joint Post-Hearing Brief is a true and accurate copy of the document being filed in paper medium; that the electronic filing has been transmitted to the Commission on April 1, 2019; 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 filing in both cases will be filed with the Commission within two business days from the date of the electronic filing.

A handwritten signature in blue ink, reading "Gerald R. Niess". The signature is fluid and cursive, with a long horizontal stroke at the end.

*Counsel for Kentucky Utilities Company
and Louisville Gas and Electric Company*