

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

APPLICATION OF LOUISVILLE GAS AND)	
ELECTRIC COMPANY FOR AN ADJUSTMENT)	CASE NO.
OF ELECTRIC AND GAS BASE RATES)	2009-00549

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O R D E R

Louisville Gas and Electric Company (“LG&E”), a wholly owned subsidiary of E.ON US LLC (“E.ON US”), is an electric and gas utility that generates, transmits, distributes, and sells electricity to approximately 389,000 consumers in Jefferson County, Kentucky and in portions of eight other Kentucky counties.¹ It purchases, stores, transports, distributes, and sells natural gas to approximately 317,000 consumers in Jefferson County and in portions of 15 other Kentucky counties.²

BACKGROUND

On December 30, 2009, LG&E filed a letter giving notice of its intent to file an application for approval of an increase in its electric and gas rates based on a historical test year ending October 31, 2009. On January 29, 2010, LG&E filed its application, which included new rates to be effective March 1, 2010, based on requests to increase its electric and gas revenues by \$94,973,371 and \$22,598,160, respectively.³ The

¹ The eight counties are Bullitt, Hardin, Henry, Meade, Oldham, Shelby, Spencer, and Trimble.

² The 15 counties are Barren, Bullitt, Green, Hardin, Hart, Henry, Larue, Marion, Meade, Metcalfe, Nelson, Oldham, Shelby, Trimble, and Washington.

³ LG&E’s sister utility, Kentucky Utilities Company (“KU”), filed a rate application concurrently, which was docketed as Case No. 2009-00548, Application of Kentucky Utilities Company for an Adjustment of Base Rates.

application also included proposals to revise, add, and delete various tariffs applicable to its electric and gas services. To determine the reasonableness of the requests, the Commission suspended the proposed rates for five months from their effective date, pursuant to KRS 278.190(2), up to and including July 31, 2010.

The following parties requested and were granted full intervention: the Kentucky Industrial Utility Customers, Inc. ("KIUC"); the Attorney General of the Commonwealth of Kentucky, by and through his Office of Rate Intervention ("AG"); The Kroger Company ("Kroger"); the United States Department of Defense and Other Federal Executive Agencies ("DOD"); the Kentucky School Boards Association ("KSBA"); the Kentucky Cable Telecommunications Association ("KCTA"); AARP; and the Association of Community Ministries ("ACM").

On February 16, 2010, the Commission issued a procedural order establishing the schedule for processing this case. The schedule provided for discovery, intervenor testimony, rebuttal testimony by LG&E, an evidentiary hearing, and an opportunity for the parties to file post-hearing briefs.⁴ Intervenor testimonies were filed on April 22 and 23, 2010. LG&E filed its rebuttal testimony on May 27, 2010.

On June 2 and 3, 2010, an informal conference was held at the Commission's offices to discuss procedural matters and the possible resolution of pending issues.⁵ All of the parties, except the AG, participated in the conference. Also on June 2, 2010, the

⁴ After establishing the procedural schedule for the evidentiary portion of the case, the Commission scheduled and conducted four public meetings in the service territories of LG&E and KU. The public meetings were held on April 27, 2010, in Harlan; May 3, 2010, in Louisville; May 4, 2010, in Madisonville; and May 6, 2010, in Lexington.

⁵ For administrative efficiency, the informal conference was a joint conference for this case and the rate case of KU, Case No. 2009-00548.

AG filed a motion to dismiss this case claiming that the pending acquisition of E.ON by PPL Corporation (“PPL”) renders the historical test year proposed by LG&E unreasonable for use in setting rates.⁶ On June 7, 2010, LG&E and KU filed a joint response in opposition to the AG’s motion to dismiss. The Commission, in an Order issued June 8, 2010, denied the AG’s motion without prejudice, stating that “[t]he AG may pursue this issue and renew his motion if he so chooses.”

On June 8, 2010, LG&E, KU, and the intervenors in this case and Case No. 2009-00548, with the exception of the AG, filed a Stipulation and Recommendation (“Stipulation”), attached hereto as Appendix A, which was intended to address all of the issues raised in the two rate cases. Under the terms of the Stipulation, the utilities and signatory intervenors agreed to forego cross-examination of each other’s witnesses at the evidentiary hearing.

Because the Stipulation was not unanimous, the hearing set for June 8, 2010, convened as scheduled for the purposes of hearing (1) testimony by LG&E and KU in support of the Stipulation and (2) testimony by LG&E, KU and the AG on contested issues related to the amount of the revenue increases sought by LG&E and KU.⁷ On June 25 and 29, 2010, respectively, LG&E and the AG filed their post-hearing briefs. The AG also filed on June 29, 2010, a renewed motion to dismiss this case and the KU rate case, to which LG&E and KU filed a joint response on July 8, 2010. This matter now stands submitted to the Commission for a decision.

⁶ The AG’s motion to dismiss also applied to KU’s case, Case No. 2009-00548.

⁷ The AG stated at the hearing that he did not object to the manner in which non-revenue requirement issues were addressed and resolved in the Stipulation.

AG'S RENEWED MOTION TO DISMISS

On June 29, 2010, the AG filed a renewed motion to dismiss both LG&E's rate application and KU's, which is pending in Case No. 2009-00548. The basis for the renewed motion is a claim that the announced acquisition of LG&E and its affiliate, KU, by PPL has created a material change which renders the historic test year no longer reasonable for use in setting rates in this case. The AG previously filed a similar motion on June 2, 2010, prior to the evidentiary hearing held on June 8, 2010. By Order issued on June 8, 2010, the Commission denied the AG's earlier motion based on the absence of any evidentiary support for his claim that the historic test period was no longer reasonable for setting rates. That denial was, however, without prejudice to his renewing the motion after the hearing if he could present evidentiary support either through the supplemental testimony of his own witnesses or through cross-examination at the hearing.

The AG's renewed motion cites to a number of references in the record, some of which predate the hearing, which he argues support his claim that LG&E's test year is unreliable for setting rates. He also argues that the use of known and measurable adjustments will not render the test period reliable, and that the evidentiary record is insufficient to determine whether the proposed acquisition by PPL is irrelevant and immaterial to the rate case. Finally, he argues that if the PPL acquisition is approved, it will result in a material change to LG&E, but LG&E has failed to address in this case the impacts of that change on its going-forward operations.

On July 6, 2010, LG&E and KU filed a joint response in opposition to the AG's renewed motion. LG&E states that the evidentiary record cited by the AG shows

nothing more than vague allegations that if the PPL acquisition is consummated, it may have a potential impact at some time in the future. LG&E also dismisses the AG's claim that LG&E's witnesses were somehow remiss in failing to revise their testimony or data responses to reflect the impacts of the proposed PPL acquisition. No such revisions were necessary, according to LG&E, because the acquisition will have no impact on this rate case.

Based on the AG's renewed motion to dismiss and being otherwise sufficiently advised, the Commission finds that the evidentiary references cited by the AG do not demonstrate that the historic test year used in this case is unreliable for setting rates. At best, the AG's citations show that if the PPL acquisition is consummated, there is the mere potential for expenses to change at some indefinite time in the future.

The record does, however, contain other evidence, not cited by the AG, that demonstrates that the PPL acquisition has been structured to have no financial impact on LG&E.⁸ Thus, any impacts of the proposed PPL acquisition are simply too far off and too remote to render unreliable LG&E's test year in this case, the 12 months ending October 31, 2009. The AG's evidentiary references do not persuade us to reject LG&E's test year for use in setting rates in this case. To the contrary, LG&E has shown its test year, with the pro forma adjustments, to be reliable as a starting point for setting rates.

The Commission also finds that, when a historic test year is used for setting rates, pro forma adjustments are allowed for changes that are known and measurable. But the mere fact that a future event, such as a proposed transfer of control, which is

⁸ June 8, 2010 Hearing Video Transcript at 1:15:50 pm.

not now measurable, may cause changes in future revenues or expenses does not render the historic test year unreliable. There will always be future events that occur well beyond the end of the test year that may have an impact on the future revenues or expenses of a utility. If a test year was rendered unreliable due to the potential that future events might impact revenues or expenses, no utility would ever be able to adjust its rates.

However, should a future event occur which does adversely impact the revenues or expenses of a utility, KRS Chapter 278 provides ample protection to all those who might be affected. Under KRS 278.260(1), any person with an interest in the rates, including the AG, may file with the Commission a complaint against any utility that any rate is unreasonable, and the Commission may on its own motion initiate such a complaint. And if the utility believes that its rates are unreasonable, it is authorized by KRS 278.180(1) to file a revised schedule of rates.

Finally, there are other consumer protections afforded by KRS Chapter 278, such as for a transaction involving a transfer of control, where the Commission “may grant any application . . . in whole or in part and with modification and upon terms and conditions as it deems necessary or appropriate.” KRS 278.020(6). As we stated in our June 8, 2010 Order, the financial impacts of a proposed transfer of control have traditionally been considered as part of an application for approval of the transfer, not as part of a concurrent rate application. The AG, and others, are parties to PPL’s application to acquire LG&E, and issues of the future financial impacts of that acquisition are properly considered in that case.

AG'S MOTION TO COMPEL

During the discovery phase of this proceeding, LG&E objected to a data request from the AG requesting LG&E to "List each proposed pro forma entry which was considered in this filing but not made and state the reason(s) why the entry was not made."⁹ The basis for LG&E's objection was that such information was protected by the attorney-client privilege and the work product doctrine. LG&E asserted that decisions relating to its rate case adjustments were made in consultation with legal counsel and the response to this request would divulge the contents of communications with counsel and the mental impressions of counsel.

Due to LG&E's objection to providing the information requested, the AG filed a motion to compel the responses, arguing that LG&E failed to provide specific reasons why the information requested would be covered by the attorney-client privilege. The AG contends that such privilege "does not automatically attach because legal counsel has reviewed a matter." The AG also requests that that the procedural schedule be suspended until this discovery dispute is resolved.

LG&E and its sister company, KU, filed a joint response objecting to the AG's motion to compel. LG&E asserts that compelling it to respond to the AG's request for information regarding adjustments contemplated but not included in the rate application would necessarily disclose privileged communications between the utility and its counsel, which are protected from disclosure under the Kentucky Rules of Evidence, KRE 503(b). LG&E contends that any discussions it had with its attorneys concerning the choice of which pro forma adjustments to exclude is not subject to discovery under

⁹ AG's Initial Data Requests, Item AG 1-30.

the absolute privilege applicable to the opinion work product as that privilege is codified in the Kentucky Rules of Civil Procedure, CR 26.02(3).¹⁰ LG&E notes that the creation of such adjustments and the determination of which adjustments to include in its rate application are always done in consultation with its counsel, making the facts and its counsel's opinions inseparable. Lastly, LG&E maintains that even if the information sought to be discovered were deemed to be fact work product rather than opinion work product, the AG has failed to establish that he has a substantial need of the materials in the preparation of his case and that he is unable to obtain the equivalent of the materials by other means entitling him to discovery of the information requested.

In his reply, the AG argues that LG&E's interpretation of the attorney-client and work product privileges was too broad. The AG avers that the privileges only protect disclosure of communications and not disclosure of the underlying facts by those communicating with the attorney. The AG states that the information requested is needed by his retained experts in order to properly and fully evaluate whether LG&E's proposed rate increase is fair, just, and reasonable. The AG further states that he cannot duplicate the information concerning possible pro forma adjustments based on the information in the application alone.

In its sur-reply, LG&E reiterated that the determination of which adjustments to include or exclude was based on the advice of counsel and made exclusively in the context of these legal proceedings. Thus, the information sought to be discovered is part and parcel privileged communications between LG&E and its counsel. LG&E

¹⁰ CR 26.02(3) provides, in relevant part, that, "[T]he court shall protect against disclosure of the mental impressions, conclusions, opinions, or legal theories of an attorney or other representative of a party concerning the litigation.

contends that the AG's claims of substantial need and undue hardship are insufficient to entitle him to discovery of information protected by the work product privilege. LG&E points out that it has produced significant amounts of actual data and documents in addition to the volumes of information contained in its application to allow the AG's experienced and capable legal team as well as his three retained experts to fully process and evaluate the reasonableness of LG&E's proposed rate increase.

Based on the AG's motion and being otherwise sufficiently advised, the Commission finds that, while our proceedings are not governed by either Kentucky's Rules of Evidence or its Rules of Civil Procedure, any privilege so established which shields the disclosure of attorney-client communications must be recognized and applied here. The AG has correctly asserted that the attorney-client privilege does not automatically attach to anything reviewed by counsel. However, under the facts as presented in this rate case, the information sought to be discovered is protected under the opinion work product privilege. The information that the AG seeks to discover – pro forma adjustments contemplated by LG&E but not included in its rate application – was formulated by LG&E in consultation with its counsel solely in anticipation of filing this base rate case. LG&E does not create or maintain lists of possible pro forma adjustments and expenses as part of its ordinary business practices. Because LG&E's potential pro forma adjustments are made in contemplation of litigation in rate proceedings, such information is protected by the work product privilege.

The AG claims to seek discovery of only the underlying facts of the communication between LG&E and its counsel regarding potential pro forma adjustments. However, since LG&E consults with its counsel prior to making a

determination of whether a pro forma adjustment passes legal ratemaking muster, the AG's request encroaches into an area which would require LG&E to disclose the mental impressions, conclusions, opinions or legal theories of its attorneys. While the AG characterizes his discovery request as one limited to underlying facts, the disclosure of such information would, in essence, reveal LG&E's counsel's impressions of the legal strengths, weaknesses, and best strategic approach in this rate proceeding because the determination of which adjustments to include or exclude are, at their roots, matters of legal strategy. The information sought to be discovered by the AG is absolutely protected under the opinion work product privilege.

The Commission notes that our decision on this issue is expressly limited to discovery of adjustments contemplated, but not filed, by a party in a rate case. Further, our decision applies with equal force to shield from discovery rate case adjustments considered by a utility in conjunction with its counsel, as well as those considered by an intervenor in conjunction with its counsel. Even though contemplated rate case adjustments, when considered in conjunction with counsel, are not subject to discovery, all other aspects of a utility's rate application and its financial records are subject to discovery. Thus, all parties to a rate case have ample opportunity to test and verify the accuracy of the test year and the adjustments proposed thereto, and the need for additional adjustments to ensure that rates are fair, just, and reasonable.

In light of the fact that discovery has been completed and the proceedings are at a conclusion, the Commission finds that the AG's request to suspend the procedural schedule is moot.

STIPULATION

The Stipulation reflects the agreement of the parties, except for the AG, on all issues raised in this case as well as the KU rate case. The main provisions of the Stipulation as they relate to LG&E's revenues and rates are as follows:

- LG&E's electric revenues should be increased by \$74 million and its gas revenues should be increased by \$17 million effective August 1, 2010.
- The allocations of the increases in LG&E's electric and gas revenues, respectively, are set forth in Exhibits 2 and 3 to the Stipulation and are fair, just and reasonable rates for LG&E, the parties and LG&E's customers.
- The electric and gas rates in Exhibits 5 and 6, respectively, to the Stipulation are the fair, just, and reasonable rates for LG&E and those rates should be approved by the Commission.
- The monthly residential electric customer charge should be \$8.50 and the monthly residential gas customer charge should be \$12.50.
- A reasonable range for LG&E's return on equity is 10.25 to 10.75 percent, with 10.63 percent continuing to be used in LG&E's monthly environmental cost recovery filings.

The Stipulation addresses several other issues, including revenue allocation, rate design, tariffs, and contributions to various low-income assistance programs. The major provisions of the Stipulation for LG&E's operations are as follows:

- New curtailable electric service riders, CSR 10 and CSR 30, will be implemented as set forth in Exhibit 5 to the Stipulation.
- Upon request, customers on either CSR 10 or CSR 30 will be provided monthly explanations for any curtailments.
- Upon request, LG&E will provide CSR customers with good-faith, non-binding estimates of the duration of requested service interruptions under Riders CSR10 and CSR 30.
- LG&E will work with its curtailable customers to install needed

telecommunication and control equipment to allow for control of the customers' loads by LG&E.

- The minimum demand ratchet for transmission service under Rate FLS will be 40 percent.
- LG&E will withdraw its proposal for kVa billing for Rate ITODP in this proceeding; however, the parties agree not to object to kVa-based billing for commercial and industrial rates in LG&E's next base rate proceeding.
- LG&E should be permitted to recover its actual rate case expenses for this case over a three-year period to begin in the month after the month in which a final order in this case is issued.
- The costs related to LG&E's 2001 and 2003 environmental compliance plans are to be recovered in its base rates and removed from LG&E's monthly environmental surcharge filings effective with the August 2010 expense month.
- LG&E's request to establish and amortize over 24.75 years a regulatory asset for the costs associated with the interest rate swap agreement between LG&E and Wachovia Bank, N.A., with the amortization beginning in the month after the month in which the final order in this case is issued, should be approved.
- LG&E should be permitted to amortize over ten years the regulatory assets previously authorized by the Commission for the costs incurred in conjunction with the 2008 wind storm and 2009 winter storm, with the amortization beginning in the month after the month in which the final order in this case is issued.
- LG&E should be permitted to amortize over four years the regulatory asset previously authorized by the Commission for LG&E's participation in the Kentucky Consortium for Carbon Storage ("KCCS"), with the amortization beginning in the month after the month in which the final order in this case is issued.
- LG&E should be permitted to amortize over ten years the regulatory asset previously authorized by the Commission for LG&E's participation in the Carbon Management Research Group ("CMRG"), with the amortization beginning in the month after the month in which the final order in this case is issued.

- LG&E commits to propose, in its next Demand-Side Management application, to modify its existing commercial conservation and rebates program to broaden the financial incentives for qualifying commercial customers to replace relatively inefficient equipment.
- The parties acknowledge that LG&E has established a FLEX Option program to allow customers unable to pay their bills, due to the timing of receipt of a monthly check, 16 additional days to pay their bills, the details of which are shown in Exhibit 7 to the Stipulation.
- LG&E's residential electric customer deposit shall remain at \$135 while its residential gas customer deposit shall be reduced to \$115, with the deposit for a combined residential electric and gas customer being \$250. All other customer deposit amounts will be as filed by LG&E in this case.
- LG&E shall continue its current policy of permitting customers required to make a deposit as a condition of reconnection after disconnection for non-payment to make their deposits in up to four monthly installments, upon request.
- Starting October 1, 2010, residential customers receiving a pledge or notice of low-income energy assistance from an authorized agency will not be assessed a late payment charge for a period of 12 months.
- The due date provisions of LG&E's tariffs will be modified to specify that the due date for payment is 12 calendar days from the date of the bill and that a late payment charge will be assessed if payment is not received within three calendar days of the due date.
- On and after August 1, 2010, LG&E will print on each bill issued to customers the date on which the bill was mailed.
- For 2011 and 2012, LG&E shall continue its current matching contribution from shareholder funds to the Wintercare program to match Wintercare funds collected from customers.
- For a period of two years beginning February 6, 2011, LG&E shall make dollar-for-dollar contributions from shareholders to its Home Energy Assistance ("HEA") program to match HEA funds collected from customers (up to \$300,000 a year on a combined basis with KU).

- LG&E will continue its current matching contribution to the ACM/Metro Match program for two years after implementation of the rates included in the Stipulation. LG&E's contribution for each of the two years shall not exceed \$225,000.
- By January 1, 2011, LG&E will have decreased the targeted window of time in which to read a customer's meter from five days to three days.
- LG&E's per-attachment annual rental charge under Rate CTAC for cable television attachments shall be \$5.35.
- LG&E shall exempt locations that install back-up generators using less than 2,000 cf per hour from the application of Rate DGGS if the customers owning such generators agree to use them only to provide emergency power.
- Except as modified in the Stipulation and the attached exhibits, the rates, terms and conditions proposed in LG&E's application shall be approved as filed.

In its application, LG&E proposed annual increases in its electric and gas revenues of \$94,973,371 and \$22,598,160, respectively. The AG proposed an annual decrease in LG&E's electric revenues of \$8,344,769 and no change in its gas revenues. With the exception of the AG, the parties agree that annual increases in electric revenues of \$74,000,000 and gas revenues of \$17,000,000, as provided in the Stipulation, are reasonable. Since all parties have not reached a unanimous settlement on the level of revenues, the Commission must consider the evidentiary record on this issue and render a decision based on a determination of LG&E's capital, rate base, operating revenues, and operating expenses as would be done in any litigated rate case.

TEST PERIOD

LG&E proposes the 12-month period ending October 31, 2009 as the test period for determining the reasonableness of its proposed rates. Although the AG has

renewed his motion to dismiss this case based on the alleged unreasonableness of the proposed test year, he utilized the same test period in his analysis of LG&E's revenue requirements. Other than his argument that the recently announced proposed acquisition of LG&E by PPL Corporation renders the test year unreliable, the AG has provided no other challenge to the test year.

The Commission finds it reasonable to use the 12-month period ending October 31, 2009 as the test period in this case. That period is the most recent feasible period to use for setting rates, and the revenues and expenses incurred during that period are neither unusual nor extraordinary, except as have been adjusted by normalization and known and measurable changes. In using this historic test period, the Commission has given full consideration to appropriate known and measurable changes.

RATE BASE

Rate Base Allocation Ratio

LG&E proposed a test year electric rate base of \$1,903,319,053. The electric rate base is divided by the total company rate base to derive a rate base allocation ratio ("allocation ratio"). This ratio is then applied to LG&E's total company capitalization to derive its electric capitalization, while the inverse of the allocation ratio is used to derive the gas capitalization. The allocation ratio uses the test-year-end rate base before any rate-making adjustments applicable to either electric or gas operations are recognized. LG&E used an allocation ratio of 79.62 percent.¹¹ The Commission has reviewed and agrees with the calculation of LG&E's test year electric rate base for purposes of establishing the rate base allocation ratio.

¹¹ Rives Direct Testimony, Exhibit 3.

Electric Rate Base

LG&E calculated a pro forma electric rate base of \$1,848,557,684, which reflects the types of adjustments made by the Commission in prior rate cases to determine a utility's pro forma rate base. The AG did not address LG&E's proposed electric rate base in his testimony. The Commission has accepted LG&E's pro forma electric rate base for rate-making purposes except for the allowance for cash working capital, which is adjusted based on the adjustments to operation and maintenance expenses discussed later in this Order. Based on our findings, we have determined LG&E's pro forma electric rate base for rate-making purposes as of October 31, 2009 to be as follows:

Total Utility Plant in Service	\$ 3,774,003,710
Add:	
Materials & Supplies	78,422,832
Prepayments	3,236,899
Cash Working Capital Allowance	75,535,857
Mill Creek Ash Dredging – Regulatory Asset	<u>2,400,596</u>
Subtotal	\$ 159,596,184
Deduct:	
Accumulated Depreciation	\$ 1,703,730,284
Customer Advances	1,848,625
Accumulated Deferred Income Taxes	338,384,167
SFAS 109 Accumulated Deferred Income Taxes	37,321,392
Asset Retirement Obligation – Net Assets	3,342,267
Asset Retirement Obligation – Regulatory Liabilities	<u>703,529</u>
Subtotal	\$ 2,085,330,264
Pro Forma Electric Rate Base	<u>\$ 1,848,269,630</u>

Gas Rate Base

LG&E calculated a pro forma gas rate base of \$486,583,169 based on the inverse of the rate base allocation ratio used to develop the electric rate base and capitalization. The AG did not address LG&E's proposed gas rate base in his testimony. It reflects the types of adjustments made by the Commission in prior rate cases to determine the pro forma rate base. The Commission has accepted LG&E's gas rate base for rate-making purposes except for the allowance for cash working capital, which is adjusted based on the adjustments to operation and maintenance expenses discussed later in this Order. Based on our findings, we have determined LG&E's pro forma gas rate base for rate-making purposes as of October 31, 2009 to be as follows:

Total Utility Plant in Service	\$ 726,844,571
Add:	
Materials & Supplies	60,055
Prepayments	659,791
Cash Working Capital Allowance	7,745,080
Gas Stored Underground	<u>66,447,790</u>
Subtotal	\$ 74,912,716
Deduct:	
Accumulated Depreciation	\$ 252,316,182
Customer Advances	7,485,292
Accumulated Deferred Income Taxes	48,874,215
SFAS 109 Accumulated Deferred Income Taxes	4,053,496
Asset Retirement Obligation – Net Assets	131,229
Asset Retirement Obligation – Regulatory Liabilities	<u>2,353,476</u>
Subtotal	\$ 315,213,890
Pro Forma Gas Rate Base	<u>\$ 486,543,397</u>

Reproduction Cost Rate Base

LG&E presented a total company reproduction cost rate base of \$5,233,171,482, an electric operations reproduction cost rate base of \$4,176,096,342 and a gas operations reproduction cost rate base of \$1,057,075,140.¹² The costs were determined principally by indexing the surviving plant and equity using the Handy-Whitman Index of Public Utility Construction Costs and the Consumer Price Index.¹³ The Commission has given appropriate consideration to the proposed reproduction cost rate base, but finds that using LG&E's historic cost for rate base is more appropriate and consistent with the precedents for LG&E as well as other jurisdictional utilities within Kentucky.

CAPITALIZATION

Electric Capitalization

LG&E proposed an adjusted electric capitalization of \$1,805,791,767.¹⁴ Included in its electric capitalization were adjustments for the Job Development Investment Tax Credit ("JDIC"), the removal of 25 percent of inventories associated with Trimble County Unit 1, the Advanced Coal Investment Tax Credit, LG&E's equity investment in the Ohio Valley Electric Corporation, the Trimble County joint use assets transferred from LG&E to KU, and removal of the environmental compliance investments which remain part of the environmental rate base included in LG&E's environmental surcharge mechanism. As with LG&E's rate base, the AG did not address LG&E's electric capitalization. LG&E

¹² Id. Exhibit 5.

¹³ Id. at 31.

¹⁴ Id. Exhibit 2.

determined its electric capitalization by multiplying its total company capitalization by the rate base allocation ratio described earlier in this Order. This is consistent with the approach used by the Commission in previous LG&E rate cases. Based on our review of LG&E's adjustments, we will accept its proposed electric capitalization of \$1,805,791,767.

Gas Capitalization

LG&E proposed an adjusted gas capitalization of \$466,472,963.¹⁵ The only adjustment included in LG&E's gas capitalization was for JDIC. The AG did not address LG&E's gas capitalization. LG&E determined its gas capitalization in the same manner as its electric capitalization based on the inverse of the rate base allocation ratio described earlier in this Order. This is consistent with the approach used by the Commission in previous LG&E rate cases. Based on our review of LG&E's adjustments, we will accept its proposed gas capitalization of \$466,472,963.

REVENUES AND EXPENSES

For the test year, LG&E reported actual net operating income from its electric and gas operations of \$133,953,246 and \$19,920,343, respectively. LG&E proposed a series of adjustments to revenues and expenses to reflect more current and anticipated operating conditions, resulting in adjusted electric net operating income of \$90,862,701 and adjusted gas net operating income of \$24,681,748.¹⁶ During the course of this case, LG&E identified and corrected errors and revised several of the adjustments included in its application. These changes resulted in increasing LG&E's adjusted

¹⁵ Id.

¹⁶ Id., Exhibit 1.

electric net operating income to \$91,297,699 and increasing its adjusted gas net operating income to \$25,000,038.¹⁷ The AG opposed six of the proposed adjustments, five affecting LG&E's electric operations and one affecting its gas operations. The AG also proposed adjustments to the calculation of LG&E's income tax expense. We find that the adjustments proposed by LG&E and accepted by the AG are reasonable and should be accepted by the Commission. For the remaining adjustments, which relate to (1) the treatment of regulatory assets related to storm restoration costs, (2) the treatment of regulatory assets related to participation in carbon capture and storage projects, (3) electric weather normalization and (4) the appropriate income tax rate, the Commission makes the following findings and conclusions:¹⁸

Storm-Related Regulatory Assets

LG&E requests recovery of amortization of regulatory assets for storm removal costs related to the 2008 Wind Storm and 2009 Winter Storm.¹⁹ Total electric expense adjustments related to the amortization of these items is \$27,630,386 for the 2008 Wind Storm and \$8,734,140 for the 2009 Winter Storm.²⁰ LG&E's gas expense adjustment related to the 2009 Winter Storm is \$33,538.

¹⁷ LG&E's Response to Commission Staff's Fourth Data Request, Item 2, Revised Exhibit 1, page 3 of 3.

¹⁸ There are both electric and gas regulatory asset adjustments and income tax adjustments; hence, the earlier reference to six adjustments.

¹⁹ The regulatory asset related to the 2008 Wind Storm was authorized in Case No. 2008-00456, while the regulatory asset related to the 2009 Winter Storm was authorized in Case No. 2009-00175.

²⁰ The adjustment related to the 2008 Wind Storm reflects reversing net credits during the test year to establish the regulatory asset along with a five-year amortization of the asset.

The AG claims it is unnecessary for the Commission to allow rate recovery of the amortization expenses because these costs were “prefunded” through recovery of the asset removal cost component of LG&E’s depreciation. The AG argues that LG&E has recovered \$259 million more in asset removal costs than its actual cost of removal expenses. Thus, he contends there are “excess” funds available to offset the deferred storm damage costs.²¹

LG&E contends that amortization of the storm damage costs is appropriate for rate recovery as these costs reflect prudently incurred expenses which the Commission authorized it to defer as regulatory assets. Further, LG&E points out that asset removal costs recovered via depreciation should only be used for their intended purpose, namely asset removal. Otherwise, the funds will not be available when assets require removal.²²

We are not persuaded by the AG’s arguments. The amounts deferred by LG&E were approved by the Commission in previous cases. The AG does not dispute the amounts that were deferred; he only challenges the rate treatment of these amounts. LG&E’s proposal to amortize these amounts in this rate proceeding is in accordance with long-standing generally accepted rate-making practices employed by the Commission. The amounts collected by LG&E through depreciation for asset removal costs should only be used for their intended purpose, which is to fund the costs to remove assets. Any concerns the AG has regarding the alleged “excessive” recovery of

²¹ Majoros Testimony at 4-6.

²² Charnas Rebuttal Testimony at 5-9.

asset removal costs should be raised by the AG when LG&E files its next depreciation case with the Commission.

Carbon Project Regulatory Assets

LG&E requests recovery of the amortization expense for regulatory assets for research contributions paid to the KCCS and the CMRG. The total expense adjustments related to the amortization of these items is \$343,330 for the KCCS and \$(1,940) for the CMRG.²³

Based on the same arguments he relies upon in contesting the storm-related adjustments, the AG contends the Commission should not allow rate recovery of these amortization expenses because these costs were “prefunded” through recovery of the asset removal cost component of LG&E’s depreciation. As with the storm-related regulatory assets, the AG argues that LG&E has “excess” funds available to offset the deferred storm damage costs.²⁴

LG&E argues that amortization of the KCCS and CMRG costs is appropriate for rate recovery given that they are prudently incurred costs which the Commission has authorized it to defer as regulatory assets. As in the case of the storm-related costs, LG&E states that asset removal costs recovered via depreciation should only be used for their intended purpose, asset removal, or the funds will not be available when assets require removal.²⁵

²³ The KCCS adjustment includes reversing the credit during the test year to establish the regulatory asset in addition to the amortization of the asset. The CMRG adjustment reflects the net of the test year expense and the yearly amortization.

²⁴ Majoros Testimony at 6.

²⁵ Charnas Rebuttal Testimony at 9-11.

Again, the Commission is not persuaded by the AG's arguments. There is clearly no relationship between the costs of carbon capture and storage projects and the cost of removal component of LG&E's depreciation. The amounts deferred by LG&E were previously authorized by the Commission. LG&E's proposal to amortize these amounts in this rate proceeding is consistent with this Commission's long-standing generally accepted rate-making practices. The amounts collected by LG&E through depreciation for asset removal costs should only be used for their intended purpose, which is to fund to costs to remove assets. The AG can raise any concerns he has with alleged "excessive" recovery of asset removal costs when LG&E files its next depreciation case with the Commission.

Electric Weather Normalization

LG&E proposes an electric weather normalization adjustment which increases revenues by \$5,151,223 and expenses by \$1,899,644.²⁶ The AG opposes the proposed adjustment, arguing that LG&E's method is improper because it separates and analyzes each month of the year mutually exclusive from the other months and then adjusts only those months with significant temperature variations from the norm. This methodology ignores the fact that significant fluctuations in temperature in one month may be offset by less dramatic fluctuations in other months when considered on a combined basis.²⁷

The Commission recognizes that LG&E's continued refinement to the method it uses to calculate the proposed adjustment has greatly improved its ability to measure

²⁶ Rives Direct Testimony, Exhibit 1, Reference Schedule 1.11.

²⁷ Watkins Testimony at 3 – 5.

the impact of temperature on its sales of electricity. However, the Commission shares the concerns expressed by the AG regarding the exclusive nature of the methodology employed by LG&E to develop its electric weather normalization adjustment. Accordingly, we will not approve LG&E's proposed electric weather normalization adjustment.

Income Tax Rate

In past rate cases, LG&E has been allowed rate recovery of state and federal income taxes based on statutory tax rates. It requested the same rate treatment in this case, using a state tax rate of 6 percent and a federal tax rate of 35 percent.

The AG claims that this method of tax recovery is unreasonable and that the Commission should instead use the same "effective tax rate" methodology as it used for Kentucky-American Water Company ("Kentucky American") in Case No. 2004-00103.²⁸ The AG argues that LG&E does not actually pay the statutory tax rates because its profits are netted against losses of affiliated companies on a consolidated tax return filed by LG&E's intermediate parent, E.ON US. The AG calculated the effective federal tax rate paid by LG&E as 6 percent based on the average tax payments for the previous two years. The AG calculated the impacts of these adjustments as reductions to LG&E's electric and gas rate increases of \$34.9 million and \$4.3 million, respectively.²⁹

LG&E's rebuttal to the AG contains several arguments: 1) the AG's proposal represents a radical and abrupt departure from 20 years of well-established, sound, and

²⁸ Adjustment of Rates of Kentucky-American Water Company (Ky. PSC Feb 28, 2005).

²⁹ Majoros Testimony, Exhibit MJM-1, Schedule 1.4.1 and Exhibit MJM-3, Schedule 3.3.1.

balanced policy prohibiting affiliate cross-subsidization;³⁰ 2) the AG's proposal violates LG&E's Corporate Policies and Guidelines for Intercompany Transactions, which require allocation of income tax liability on a "stand alone" basis; 3) the proposal violates the "benefits-burden" principal, meaning that, since its customers bore none of the risk of the losses incurred by the affiliates, which produced the tax losses, they should not benefit from those losses; 4) the proposal would preclude LG&E from the opportunity to achieve its authorized rate of return; 5) Case No. 2004-00103 should not be considered precedent setting in this case as the Commission approved the adjustment in that case because Kentucky-American promoted the tax savings as a benefit to merger in Case No. 2002-00317,³¹ a fact that is absent in the current situation; and 6) in previous LG&E cases, the Commission rejected effective tax rate adjustments proposed by the AG where the AG used 2004-00103 as a precedent.³²

We are not persuaded by the AG's arguments in this case on this issue any more than we were in Case No. 2003-00433.³³ Acceptance of the AG's proposal would preclude LG&E from the opportunity to earn its authorized rate of return; would violate the "stand-alone" rate-making principal the Commission has long employed; and would result in cross subsidization of LG&E and its ratepayers by its unregulated affiliates.

³⁰ LG&E created a holding company approximately 20 years ago. Prior to then, it did not have non-utility affiliates and use of a consolidated tax return was not an issue.

³¹ A Change of Control of Kentucky American Water Company (Ky. PSC Dec. 20, 2002).

³² Rives Rebuttal Testimony at 15-19.

³³ Adjustment of the Gas and Electric Rates, Terms and Conditions of Louisville Gas and Electric Company (Ky. PSC June 30, 2004 and Mar. 31, 2006).

Net Operating Income Summary

After considering all pro forma adjustments and applicable income taxes, LG&E's adjusted net operating income is as follows:

Combined Operating Revenues	\$ 1,028,519,781
Combined Operating Expenses	<u>915,473,623</u>
Combined Adjusted Net Operating Income	<u>\$ 113,046,158</u>

RATE OF RETURN

Capital Structure

LG&E proposed an adjusted test-year-end capital structure containing 46.14 percent long-term debt and 53.86 percent common equity.³⁴ The absence of short-term debt reflects LG&E's use of such funds to reacquire, but not retire, approximately \$150.7 million in bonds during the test year.

The AG recommends an adjusted capital structure for LG&E containing 50.0 percent long-term debt and 50.0 percent common equity based on his review of the capital structure ratios of electric and gas proxy groups.³⁵ LG&E opposes the AG's proposal, citing its long-standing objective of achieving an "A" corporate credit rating as defined by Standard & Poors ("S&P"), and the need to maintain a common equity ratio, as adjusted by S&P, of 50 to 55 percent. Given the consistent downward nature of S&P's adjustments, LG&E argues that a common equity ratio established at 50 percent, prior to recognizing such adjustments would, at best, result in it maintaining its current "BBB" rating. LG&E also points to its historic equity ratios (including both common stock and preferred stock, when it had preferred stock) over the past ten years as

³⁴ Rives Direct Testimony, Exhibit 2.

³⁵ Woolridge Testimony at 13.

ranging between 51.04 and 56.76 percent.³⁶ With its stated goal of achieving an “A” rating and its current equity ratio falling roughly at the mid-point of its historical equity ratios, the Commission finds that LG&E’s capital structure for rate-making purposes should not be adjusted to reflect what would constitute a hypothetical capital structure, as proposed by the AG. Achieving an A rating will provide LG&E greater access to capital markets, access to lower cost debt and greater financial flexibility. We find that LG&E’s capital structure for rate-making purposes should include 46.14 percent long-term debt and 53.86 percent common equity as proposed by LG&E.

Cost of Debt

LG&E proposed a cost of long-term debt of 4.61 percent.³⁷ LG&E filed updated financial information as of March 31, 2010 that included updated cost rates.³⁸ Based on this updated information, LG&E’s cost of long-term debt is 4.60.

The AG used LG&E’s cost of debt as filed in its application. The AG agreed that if interest rates or other capital cost rates change, such changes should be used to determine the rate of return so that LG&E will have a reasonable opportunity to earn its allowed return.

The Commission finds it appropriate to recognize the cost rate for LG&E’s long-term debt as of March 31, 2010 when determining its overall cost of capital. Updates to LG&E’s long-term debt cost rate constitute known and measurable adjustments and

³⁶ Arbough Rebuttal Testimony at 1-4.

³⁷ Rives Direct Testimony, Exhibit 2.

³⁸ LG&E’s Response to Commission Staff’s Fourth Date Request, Item 2, Revised Exhibit 2.

using these updates, rather than the test-year-end cost rates, is more representative of the period in which the rates established in this Order will be in effect. This cost rate will be applied to the capital structure determined herein. Therefore, the Commission finds the cost of LG&E's long-term debt to be 4.60 percent.

Return on Equity

LG&E estimated its required return on equity ("ROE") using the discounted cash flow method ("DCF"), the capital asset pricing model ("CAPM"), and the expected earnings approach.³⁹ LG&E included in its evaluation risks and challenges specific to jurisdictional utility operations in Kentucky, as well as flotation costs. Based on the results of the methods employed in its analysis, LG&E recommended an ROE range for its electric and gas operations of 10.5 to 12.5 percent.⁴⁰ LG&E recommended awarding the midpoint of the range, 11.5 percent, in order to support access to capital and recognize flotation costs.⁴¹ Through settlement negotiations, the Stipulation contains an agreement by all the parties except the AG that a reasonable range for LG&E's ROE is 10.25 to 10.75 percent.⁴²

LG&E employed a comparable risk proxy group in its analysis which consists of 14 electric utility companies classified by *The Value Line Investment Survey* ("Value Line") as having both electric and gas operations; S&P's corporate credit ratings of

³⁹ Avera Direct Testimony, at 5.

⁴⁰ Id. at 5.

⁴¹ Id.

⁴² Joint Motion for Leave to File Stipulation and Recommendation and Testimony, Bellar Testimony at 6.

“BBB”, “BBB+”, “A-”, or “A”; a Value Line Financial Strength Rating of “B++” or higher; and published earnings per share (“EPS”) growth projections from at least two of the following: Value Line; Thomson I/B/E/S; First Call Corporation; and Zacks Investment Research. LG&E also applied the DCF model to a proxy group of comparable risk non-utility companies followed by Value Line that pay common dividends; have a Safety Rank of “1”; have investment grade credit ratings from S&P; and have a Value Line Financial Strength Rating of “B++” or higher. The same criterion was applied to this group as the utility group of having published EPS growth projections from the sources listed above.

As part of its analysis, LG&E provided a discussion of fuel adjustment clause, gas supply clause, environmental cost recovery and weather normalization mechanisms that affect its rates for utility service. It also discussed the evolution of investors’ risk perceptions for the utility industry due to erosion in credit quality, quoting S&P’s identification of environmental compliance costs, decreasing demand, and increasing cost recovery filings as significant challenges for the utility industry.⁴³ LG&E’s need for additional capital for maintenance, replacements, and facilities additions will require support for LG&E’s financial integrity and flexibility, and this will be impacted by energy market volatility and environmental considerations, according to LG&E. In addition to these factors, LG&E points to investors’ recognition of the global recession’s impact on LG&E’s service territory as evidence of LG&E’s need to support its credit standing and financial flexibility through the opportunity to earn a return that reflects these realities.

⁴³ Id. at 10.

The AG criticized LG&E's ROE estimates on several grounds. The AG stated that LG&E's proxy group of utility companies includes companies with a low percentage of regulated utility operations revenue, and that the use of a proxy group of non-utility companies is inappropriate. The AG's major disagreement with LG&E's DCF analysis is the reliance on projected EPS growth rates in developing the growth factor component, and contends that Value Line's estimated long-term EPS growth rates are overstated. The AG stated that the primary problem with LG&E's CAPM analysis is the market risk premium used in the analysis, which the AG contends is based on an expected stock market return which is not reflective of current market fundamentals. The AG disagreed with LG&E's expected earnings approach, and stated that it is subject to error and fails to provide a reliable estimate of LG&E's cost of equity capital. The AG also recommends against LG&E's proposed adjustment for flotation costs. The AG believes that LG&E's analysis overstates its required cost of equity.

The AG estimated LG&E's required ROE for its electric and gas operations separately using the DCF model and the CAPM. Based on the results of these methods, giving primary weight to the DCF, the AG determined an ROE range of 7.8 to 9.5 percent for LG&E's electric operations, recommending that the Commission award 9.5 percent, the upper end of the range.⁴⁴ The AG determined an ROE range of 7.6 to 9.0 percent for LG&E's gas operations, with a recommended award of 9.0 percent.⁴⁵

The AG employed an electric proxy group in his analysis consisting of 20 utility companies listed as an electric or combination electric and gas utility by AUS Utility

⁴⁴ Woolridge Testimony at 2.

⁴⁵ Id. at 2.

Reports; having regulated electric revenues of at least 80 percent of total revenues; with current data available in the Standard Edition of Value Line; having an investment grade bond rating; and having an annual dividend history of three years. The AG's gas proxy group consists of nine natural gas distribution companies listed as a Natural Gas Distribution, Transmission, and/or Integrated Gas Company in AUS Utility Reports; listed as a Natural Gas Utility in the Standard Edition of Value Line; having at least 50 percent of revenues from regulated gas operations; and having an investment grade bond rating by Moody's and S&P.

The AG supported his analysis with a discussion of current economic conditions, concluding that short- and long-term credit markets have "loosened" considerably,⁴⁶ and that the stock market has rebounded significantly from 2009's lows. The AG's discussion includes a reference to a study indicating that the investment risk of utilities is very low, and states that the cost of equity for utilities is among the lowest of all industries in the U.S. as measured by their betas.⁴⁷

On rebuttal, LG&E addressed the AG's recommended ROE and his criticisms of LG&E's analysis. LG&E compared its DCF analysis to that of the AG's, stating that the AG presented historical results as being indicative of investors' future expectations, while LG&E used forward-looking data, which is a superior method due to specific trends in dividend policies and evidence from the investment community; that the AG considered analysts' EPS forecasts as being biased while LG&E's application of the DCF model recognizes the importance of considering investors' perceptions and

⁴⁶ Id. at 11.

⁴⁷ Id. at 21.

expectations; that the AG relied upon personal views rather than the capital markets for investors' expectations; and that while LG&E excludes data in its analysis that would lead to illogical conclusions, the AG relies on averaging or using the median value to eliminate any bias. LG&E also addresses the AG's criticism of the use of a non-utility proxy group, saying that it would be inconsistent with the Hope⁴⁸ and Bluefield⁴⁹ cases to exclude non-utility company returns from consideration. LG&E counters the argument that the expected earning approach is not valid, saying that an allowed ROE for a utility company must be high enough to attract capital from investors who are looking for the best investment opportunity. LG&E recommended that the AG's CAPM analysis be disregarded, noting that the AG gave primary weight to its DCF analysis. LG&E defended the market return used in its CAPM analysis, saying that its analysis appropriately focuses on investors' current expectations. LG&E reiterates the need for a flotation cost adjustment in its ROE calculation, saying that there is no basis to ignore such an adjustment.

The Commission finds merit in both LG&E's and the AG's recommended ranges for ROE and their critiques of each other's analyses. The Commission takes note of several points made in each party's testimony and analysis. LG&E's argument concerning the appropriateness of using investors' expectations in performing a DCF analysis is more persuasive than the AG's argument that analysts' projections should be rejected in favor of historical results. The Commission agrees that analysts' projections

⁴⁸ *Federal Power Commission v. Hope Natural Gas Company*, 320 U.S. (1944).

⁴⁹ *Bluefield Waterworks and Improvement Company v. Public Service Commission*. 262 U.S. 679 (1932).

of growth will be relatively more compelling in forming investors' forward-looking expectations than relying on historical performance, especially given the current state of the economy. It also appears preferable to exclude extreme outliers in ROE analysis; for example, the AG's inclusion of negative results to calculate investors' required ROE does not comport with the constant growth assumption that is inherent in the DCF formula. Concerning the issue of using a non-utility proxy group in analyzing the required ROE for a utility, the Commission agrees with LG&E that investors are always looking for the best investment opportunity and that a utility is in competition with unregulated firms; however, the AG's discussion of the relative risk of electric and gas utilities as reflected in their Value Line Betas supports the attractiveness of utility investments in comparison to riskier alternatives. As to flotation costs, the Commission agrees with the AG's position that no upward adjustment to the equity cost rate is necessary and that this finding is consistent with past Commission practice.

After weighing all the evidence of record, the Commission finds that LG&E's required ROE for both electric and gas operations falls within a range of 9.75 to 10.75 percent with a midpoint of 10.25 percent.

Rate of Return Summary

Applying the rates of 4.60 percent for long-term debt and 10.25 percent for common equity to the capital structure produces an overall cost of capital of 7.64 percent. The cost of capital produces a return on LG&E's rate base of 7.44 percent.

REVENUE REQUIREMENTS

The Commission has determined that, based upon an electric capitalization of \$1,806,059,614 and an overall cost of capital of 7.64 percent, the electric net operating

income that could be justified by the record for LG&E is \$138,038,764. Based upon a gas capitalization of \$466,472,963 and an overall cost of capital of 7.64 percent, the gas net operating income that could be justified by the record for LG&E is \$35,652,960. Based on the adjustments found reasonable herein, LG&E's pro forma electric net operating income and gas net operating income for the test year would be \$88,046,120 and \$25,000,038, respectively. It would need additional annual electric operating income of \$49,992,644 and additional gas operating income of \$10,652,922. After the provision for uncollectible accounts, the PSC Assessment, and state and federal income taxes, LG&E would have an electric revenue deficiency of \$80,042,111 and a gas revenue deficiency of \$17,056,157, for a total of \$97,098,268.

The calculation of this overall revenue deficiency is as follows:

Combined Net Operating Income Found Reasonable	\$173,691,724
Combined Pro Forma Net Operating Income	<u>113,046,158</u>
Net Operating Income Deficiency	\$ 60,645,566
Gross Up Revenue Factor ¹⁴⁶	.6245793
Overall Revenue Deficiency	<u>\$ 97,098,268</u>

The Commission has found that LG&E's required ROE falls within a range of 9.75 percent to 10.75 percent, with a mid-point of 10.25 percent. Applying the findings herein on the reasonable cost of debt and the return on common equity to LG&E's electric and gas capitalizations would result in the following revenue increases:

Electric Increase based on LG&E Alternative Proposal	\$74,000,000
Electric Increase justifiable based on ROE mid-point	\$80,042,111
Gas Increase based on LG&E Alternative Proposal	\$17,000,000
Gas Increase justifiable based on ROE mid-point	\$17,056,157

Based on the findings and conclusions herein, the Commission finds that the earnings resulting from the adoption of LG&E's alternative proposals for its electric and gas operations will produce a reasonable result for both LG&E and its ratepayers. The \$74,000,000 electric revenue increase and \$17,000,000 gas revenue increase that LG&E is willing to accept will result in fair, just, and reasonable rates for LG&E. Therefore, we will accept LG&E's alternative proposals to increase its electric revenues by \$74,000,000, and increase its gas revenues be increased by \$17,000,000, rather than the higher levels justified by the record.

FINDINGS ON STIPULATION

Based upon a review of all the provisions in the Stipulation, an examination of the entire case record, and being otherwise sufficiently advised, the Commission finds that the provisions of the Stipulation are in the public interest and should be approved since they will result in lower rate increases than justified by our traditional rate-making analysis. Our approval of the Stipulation is based solely on its reasonableness in toto and does not constitute precedent on any issue except as specifically provided for therein.

As noted above, LG&E's FLEX OPTION, described in detail in Exhibit 7 to the stipulation, will be continued. Upon questioning from the Commission at the hearing on June 8, 2010, LG&E indicated that it preferred that the FLEX OPTION not be made a part of the tariff, so as to enable LG&E the flexibility to make improvements to the program. The Commission will honor this request; however, before any change can be made to the FLEX OPTION, an informal conference with the Commission staff must be held whereby the rationale for the proposed change must be explained and justified to

the satisfaction of the staff. The Commission appreciates the willingness of LG&E to develop and implement this plan which benefits its customers and does not want to limit the ability of LG&E to make necessary changes.

CUSTOMER SERVICE, BILLING AND COLLECTIONS

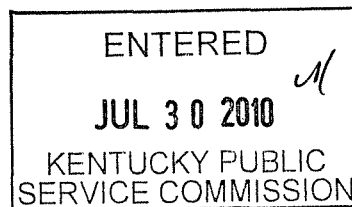
During the course of this proceeding, customers of LG&E filed with the Commission hundreds of complaints, in the form of letters, e-mails, and calls to the Commission, as well as comments presented at the local public meetings. While almost all of those complaints objected to the proposed rate increase, many raised issues related to LG&E's current billing and collection practices and procedures. The Commission also recognizes that last year LG&E brought on-line a new computerized system, known as its Customer Care System ("CCS"), to handle multiple customer related functions, including customer billing. The CCS system was under design and installation for a number of years prior to its implementation. Based on the customer complaints presented to the Commission, we find that, pursuant to KRS 278.255, a focused management audit of the efficiency and effectiveness of LG&E's customer service functions and all related supporting and operational functions that impact retail customers should be performed. The scope of the management audit should include, but not be limited to, a review of all customer service-related functions including meter reading, customer-related accounting functions, customer information systems, billing and collections, call center functions, as well as service installations, and disconnect and reconnect practices.

ORDERING PARAGRAPHS

The Commission, based on the evidence of record and the findings contained herein, HEREBY ORDERS that:

1. The rates and charges proposed by LG&E are denied.
2. The provisions in the Stipulation and Recommendation, attached hereto as Appendix A (without exhibits), are approved in their entirety.
3. The rates and charges for LG&E's electric and gas operations, set forth in Appendix B hereto, are the fair, just, and reasonable rates for LG&E to charge for service, and these rates are approved for service rendered on and after August 1, 2010.
4. A focused management audit shall be performed to review the efficiency and effectiveness of all of LG&E's customer service-related functions including all support and operational functions.
5. The AG's motions to dismiss and to compel data responses are denied.
6. Within 20 days of the date of this Order, LG&E shall file with this Commission its revised tariffs setting out the rates authorized herein, reflecting that they were approved pursuant to this Order.

By the Commission



ATTEST:



Executive Director

APPENDIX A

APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE
COMMISSION IN CASE NO. 2009-00549 DATED JUL 30 2010

RECEIVED

JUN 08 2010

PUBLIC SERVICE
COMMISSION

STIPULATION AND RECOMMENDATION

This Stipulation and Recommendation is entered into this 7th day of June 2010, by and between Louisville Gas and Electric Company (“LG&E”); Kentucky Utilities Company (“KU”) (LG&E and KU are hereafter collectively referenced as “the Utilities”); Kentucky Industrial Utility Customers, Inc. (“KIUC”) and the interests of its participating members as represented by and through the KIUC; The Kroger Co. (“Kroger”); Community Action Council for Lexington-Fayette, Bourbon, Harrison and Nicholas Counties, Inc. (“CAC”); Association of Community Ministries (“ACM”); Kentucky Cable Telecommunications Association (“KCTA”); the United States Department of Defense and Other Federal Executive Agencies (“DOD/FEA”); Wal-Mart Stores East, LP and Sam’s East, Inc. (collectively, “Walmart”); Kentucky School Boards Association (“KSBA”); and AARP in the proceedings involving LG&E and KU, which are the subject of this Stipulation and Recommendation, as set forth below. (The Utilities, KIUC, Kroger, CAC, ACM, KCTA, DOD/FEA, Walmart, KSBA, and AARP are referred to collectively herein as the “Parties.”)

WITNESSETH:

WHEREAS, KU filed on January 29, 2010, with the Kentucky Public Service Commission (“Commission”) its Application for Authority to Adjust Rates, In the Matter of: Application of Kentucky Utilities Company for an Adjustment of Base Rates, and the Commission has established Case No. 2009-00548 to review KU’s base rate application;

WHEREAS, LG&E filed on January 29, 2010, with the Commission its Application for Authority to Adjust Rates, In the Matter of: Application of Louisville Gas and Electric Company for an Adjustment of Its Electric and Gas Base Rates, and the Commission has established Case No. 2009-00549 to review LG&E’s base rate application (Case Nos. 2009-00548 and 2009-00549 are hereafter collectively referenced as the “rate proceedings”);

WHEREAS, the Attorney General of the Commonwealth of Kentucky, by and through his Office of Rate Intervention (“AG”), KIUC, Kroger, KCTA, and KSBA have been granted intervention by the Commission in both of the rate proceedings; CAC and Walmart have been granted intervention by the Commission in Case No. 2009-00548 only; and ACM, DOD/FEA, and AARP have been granted intervention by the Commission in Case No. 2009-00549 only;

WHEREAS, an informal conference, attended in person or by teleconference by representatives of the Parties, AG, and Commission Staff took place on June 2-3, 2010, at the offices of the Commission, during which a number of procedural and substantive issues were discussed, including terms and conditions related to the issues pending before the Commission in the rate proceedings that might be considered by all parties to constitute reasonable means of addressing their concerns;

WHEREAS, the Parties desire to recommend to the Commission that it enter its Order setting the terms and conditions that the parties believe are reasonable as stated herein;

WHEREAS, it is understood by the Parties that this Stipulation and Recommendation does not represent agreement on any specific theory supporting the appropriateness of any proposed or recommended adjustments to the Utilities’ rates, terms, and conditions;

WHEREAS, it is understood by all Parties that this agreement is a stipulation among the Parties concerning all matters at issue in these proceedings pursuant to 807 KAR 5:001, Section 4(6);

WHEREAS, the Parties have spent many hours to reach the stipulations and agreements that form the basis of this Stipulation and Recommendation;

WHEREAS, the Parties, who represent diverse interests and divergent viewpoints, agree that this Stipulation and Recommendation, viewed in its entirety, is a fair, just, and reasonable resolution of all the issues in the rate proceedings; and

WHEREAS, the Parties recognize that this agreement constitutes only an agreement among, and a recommendation by, themselves, and that all issues in these proceedings remain open for consideration by the Commission at the formal hearing in these proceedings.

NOW, THEREFORE, in consideration of the premises and conditions set forth herein, the Parties hereby stipulate, agree, and recommend as follows:

ARTICLE I. Revenue Requirement

Section 1.1. The Parties stipulate that the following increases in annual revenues for LG&E electric operations and for KU operations, for purposes of determining the rates of LG&E and KU in the rate proceedings, are fair, just and reasonable for the Parties and for all electric customers of LG&E and KU:

LG&E Electric Operations: \$74,000,000;

KU Operations: \$98,000,000.

The Parties agree that any increase in annual revenues for LG&E electric operations and for KU operations should be effective for service rendered on and after August 1, 2010.

Section 1.2. The Parties stipulate and agree that, effective for service rendered on and after August 1, 2010, an increase in annual revenues for LG&E gas operations of \$17,000,000, for purposes of determining the rates of LG&E

gas operations in the rate proceedings, is fair, just and reasonable for the Parties and for all gas customers of LG&E.

ARTICLE II. Allocation of Revenue

Section 2.1. The Parties agree that the allocations of the increases in annual revenues for KU and LG&E electric operations, and that the allocation of the increase in annual revenue for LG&E gas operations, as set forth on the allocation schedules designated Exhibit 1 (KU), Exhibit 2 (LG&E electric), and Exhibit 3 (LG&E gas) hereto, are fair, just, and reasonable for the Parties and for all customers of LG&E and KU.

Section 2.2. The Parties agree that, effective for service rendered on and after August 1, 2010, the Utilities should implement the electric and gas rates set forth on the proposed tariff sheets in Exhibit 4 (KU), Exhibit 5 (LG&E electric), and Exhibit 6 (LG&E gas), attached hereto, which rates the Parties stipulate are fair, just, and reasonable for the Parties and for all customers of LG&E and KU.

ARTICLE III. Return on Equity

Section 3.1. The Parties agree that a reasonable range for the Utilities' return on equity is 10.25% - 10.75% in this case, and in connection with Section 3.2 below.

Section 3.2. The Parties agree that the return on equity applicable to the Utilities' recovery under their environmental cost recovery ("ECR") mechanism should remain at its current level, 10.63%, for all billing months subsequent to, and including, the first expense month after the month in which the Commission enters its Orders in these proceedings.

ARTICLE IV. Curtailable Service Riders

Section 4.1. The Parties agree that the Utilities shall replace their existing Curtailable Service Riders with two new Curtailable Service Riders, CSR10 and CSR30 as set forth in Exhibits 4 and 5. The maximum load permitted to take service under such riders per Utility shall be the current curtailable load under curtailable service riders as of August 1, 2010, plus 100 MW (combined across both new riders).

CSR10 shall: (1) require curtailment on ten minutes' notice; (2) require up to 100 hours per year of physical curtailment as described in the tariff, plus up to 275 hours per year of additional curtailment with a buy-through option; (3) provide a monthly credit of \$5.40/kW for transmission service and \$5.50/kW for primary service.

CSR30 shall: (1) require curtailment on thirty minutes' notice; (2) require up to 100 hours per year of physical curtailment as described in the tariff, plus up to 250 hours per year of additional curtailment with a buy-through option; (3) provide a monthly credit of \$4.30/kW for transmission service and \$4.40/kW for primary service.

Both new riders shall calculate the amount of buy-through kWh for a customer by subtracting the product of the customer's firm capacity and the number of hours subject to curtailment from the customer's total kWh consumption during the hours under curtailment:

$$\text{Total kWh} - (\text{firm kW} * \text{hours curtailed})$$

If a customer “buys through” a curtailment period, the customer shall not be charged the otherwise applicable base rate energy charge or ECR rate in addition to the buy-through cost.

The rates, terms, and conditions of CSR10 and CSR30 are fully set out in the proposed tariff sheets contained in Exhibits 4 and 5 hereto.

Section 4.2. The Parties agree that, upon request, the Utilities will provide once per month to customers on either CSR 10 or CSR 30 an explanation of the reasons for any curtailments as described in the tariff.

Section 4.3. The Parties agree that, consistent with the Utilities’ current practice and 807 KAR 5:056 § 1(3)(c), buy-through revenues paid to the Utilities under Riders CSR10 and CSR30 shall be credited to net energy costs under the Utilities’ Fuel Adjustment Clauses.

Section 4.4. The Parties agree that, upon request, the Utilities shall provide to their CSR customers good-faith, non-binding estimates of the duration of requested service interruptions under Riders CSR10 and CSR30; however, customers taking such service shall likewise, upon request, provide to the Utilities good-faith, non-binding short-term operational schedules.

Section 4.5. The Parties agree that the Utilities will work with their curtailable customers to install the necessary telecommunication and control equipment to allow the Utilities to control curtailable customers’ loads, provided that the Utilities’ and the customer’s individual responsibilities are clearly defined, and the customer pays for the necessary equipment, all as set out more fully in the KU Rebuttal Testimony of W. Steven Seelye at

pages 44-46, and in the LG&E Rebuttal Testimony of W. Steven Seelye at pages 45-46, in the rate proceedings.

ARTICLE V. Treatment of Other Specific Issues

- Section 5.1.** The Parties agree that minimum demand ratchet for transmission service under KU's Rate FLS will be 40%. This is reflected in the proposed tariff sheets attached hereto in Exhibit 4.
- Section 5.2.** The Parties agree that LG&E will withdraw its proposal for kVA billing for the proposed Rate ITODP rate schedule. Instead, the rate structure for Rate ITODP will be same as the current Rate ITOD for primary service. This is reflected in the proposed tariff sheets attached hereto in Exhibit 5. KU's proposed kVA billing for proposed Rate ITOD for primary service shall be implemented.
- Section 5.3.** The Parties agree not to object to kVA-based demand billing for commercial and industrial rates in the Utilities' next base rate proceedings.
- Section 5.4.** The Parties agree that LG&E and KU should be permitted to amortize their actual rate case expenses in these proceedings over a three-year period. The amortization should begin in the month after the month in which the Commission enters its Orders in these proceedings.
- Section 5.5.** The Parties agree that all costs associated with KU's and LG&E's 2001 and 2003 environmental compliance plans shall be recovered in the Utilities' base rates and will be removed from the Utilities' monthly environmental surcharge filings effective with the August 2010 expense month after the Commission approves this Stipulation and Recommendation.

Section 5.6. The Parties agree that the Commission should grant LG&E's request, as stated in its Application, to establish and amortize over 24.75 years (the remaining term of the related debt agreements) a regulatory asset for the costs associated with the interest rate swap agreement between LG&E and Wachovia Bank, N.A., as discussed in the pre-filed direct testimony of Daniel K. Arbough. The amortization should begin in the month after the month in which the Commission enters its Orders in these proceedings.

Section 5.7. The Parties agree that the Commission should approve a ten-year amortization of the Utilities' regulatory assets approved by the Commission concerning the 2008 Wind Storm and 2009 Winter Storm, with such amortization to begin in the month after the month in which the Commission enters its Orders in these proceedings.

Section 5.8. The Parties agree that the Commission should approve a four-year amortization of the Utilities' regulatory assets approved by the Commission concerning the Kentucky Consortium for Carbon Storage ("KCCS"), with such amortization to begin in the month after the month in which the Commission enters its Orders in these proceedings.

Section 5.9. The Parties agree that the Commission should approve a ten-year amortization of the Utilities' regulatory assets approved by the Commission concerning the Carbon Management Research Group ("CMRG"), with such amortization to begin in the month after the month in which the Commission enters its Orders in these proceedings.

Section 5.10. The Parties agree that the following monthly basic service charge amounts shall be implemented:

LG&E and KU Rates RS, VFD, and LEV:	\$8.50
LG&E Rate RRP:	\$13.50
LG&E Rates RGS and VFD:	\$12.50
KU Rate AES (single-phase):	\$17.50
KU Rate AES (three-phase):	\$32.50
LG&E and KU Rate GS (single-phase):	\$17.50
LG&E and KU Rate GS (three-phase):	\$32.50
LG&E Rate GRP (single-phase):	\$27.50
LG&E Rate GRP (three-phase):	\$42.50

All other basic service charges shall be the amounts proposed by the Utilities in their Applications filed on January 29, 2010, in the rate proceedings. These basic service charges are reflected in the proposed tariff sheets attached hereto in Exhibits 4, 5 and 6.

Section 5.11. The Parties agree that the Utilities shall propose in their next Demand-Side Management Program application to modify their existing Commercial Conservation (Energy Audits) and Rebates Program to broaden the financial incentives for qualifying commercial customers to replace relatively inefficient equipment. The Utilities will seek input from potentially affected customers on possible modifications through a collaborative process. The modifications the Utilities will propose will include, but will not be necessarily limited to, the following: (1) adding

refrigeration to the kinds of equipment for which incentives are available; (2) introducing a Commercial Customized Rebates program to provide incentives to commercial customers to increase their energy efficiency by replacing or retrofitting equipment not covered by the existing Commercial Conservation/Rebate Program and (3) increasing the rebate cap per meter. To the extent that LED lighting retrofits associated with refrigeration cases located in the Utilities' service territories occurred from 2008 to the present, the Utilities clarify and confirm that under their existing business practices such actions qualify under the Utilities' existing Rebate Program for LED Lighting. The Utilities will work with any customer representatives to ensure the appropriate applications are completed and processed for the purpose of participating in the Utilities' existing Rebate Program for LED Lighting. To the extent that no rebate was provided in the immediately preceding year, the Utilities the Utilities clarify and confirm that under their existing business practices, customers may receive multi-year rebates in a single year where such multi-year rebates do not exceed the aggregate amounts. For example, under the Utilities' current business practices, a customer eligible for a \$50K/year could receive a \$100K/year rebate as long as no rebate was provided in the immediately preceding year.

Section 5.12. The Parties agree that the rates resulting from these proceedings for LG&E gas service will not be set on a Straight-Fixed Variable Design basis as had been proposed in the Application in the rate proceedings.

Section 5.13. The Parties acknowledge that KU and LG&E have established a FLEX Option program to allow customers on fixed incomes 16 additional calendar days to pay their bills (i.e., their bills are due 28 calendar days from the bill date), effectively allowing participating customers to pay their bills after they receive their monthly incomes.

The details of the FLEX Option, including eligibility requirements, are set out in Exhibit 7 hereto.

Section 5.14. The Parties agree that KU's and LG&E's residential electric customer deposit amounts shall remain unchanged from their current levels, and that effective for deposits requested on and after August 1, 2010, the residential gas service deposit amount shall be reduced. The residential customer deposits will be as follows: \$135 for LG&E electric; \$115 for LG&E gas; \$250 for LG&E electric and gas combined; and \$135 for KU. All other customer deposit amounts will be as filed by the Utilities in these proceedings.

Section 5.15. The Parties agree that the Utilities will continue their current policy of permitting customers who are required to make a deposit as a condition of reconnection following disconnection for non-payment to pay required deposits in up to four monthly installments upon request.

Section 5.16. The Parties agree that, beginning October 1, 2010, residential customers who receive a pledge for, or notice of, low-income energy assistance from an authorized agency will not be assessed or required to pay a late payment charge for the bill for which the pledge or notice is received, nor will they

be assessed or required to pay a late payment charge in any of the eleven (11) months following receipt of such pledge or notice. The Utilities retain the right to audit the program to ensure appropriate application of the waiver. The Utilities acknowledge that private information cannot be disclosed by the assistance agencies without authorization from the low-income customers.

Section 5.17. The Parties agree that the Utilities will modify the language of their tariff sheets concerning the due dates of bills and the date on which LPCs are assessed to clarify that payment is due twelve calendar days after the date on which a bill issues, and that an LPC will be assessed if payment is not received within three calendar days of the bill due date. For example, the “Due Date of Bill” provision of the KU residential service tariff sheet now reads, “Customer’s payment will be due within twelve (12) days from date of bill.” Pursuant to this Section, the “Due Date of Bill” provision of the KU residential service tariff sheet will read, “Customer’s payment will be due within twelve (12) calendar days from date of bill.”

Likewise, the “Late Payment Charge” provision of the KU residential service tariff sheet now reads, “If full payment is not received within three (3) days from the due date of the bill, a 5% late payment charge will be assessed on the current month’s charges.” Pursuant to this Section, the “Late Payment Charge” provision of the KU residential service tariff sheet will read, “If full payment is not received within three

(3) calendar days from the due date of the bill, a 5% late payment charge will be assessed on the current month's charges.”

These language changes are reflected in the proposed tariff sheets attached hereto in Exhibits 4, 5, and 6.

Section 5.18. The Parties agree that the Utilities shall print on each bill issued to customers on and after August 1, 2010, the date on which the bill was mailed.

Section 5.19. The Parties agree that for each of calendar years 2011 and 2012, the Utilities shall continue their current matching contribution from shareholder funds to the Wintercare program to match Wintercare funds collected from customers. KU's annual contribution for each of calendar years 2011 and 2012 shall not be less than \$100,000.

Section 5.20. The Parties agree that for a period of two years beginning February 6, 2011, the Utilities shall make a dollar-for-dollar contribution from shareholder funds to the Home Energy Assistance (“HEA”) program to match HEA funds collected from customers (up to \$300,000 per year on a combined-Utilities basis).

Section 5.21. The Parties agree that LG&E will continue its current matching contribution to the ACM/Metro Match program for a period of two years following the implementation of the rates proposed in this Stipulation and Recommendation. LG&E's contribution to the ACM/Metro Match program for each of the two years shall not exceed \$225,000 per year. Section 5.21 is not contingent upon any other specific party's participation.

Section 5.22. The Parties agree that the targeted window of time in which the Utilities may read a customer's meter shall be decreased from the current five days to three days. Because it will take time for the Utilities to obtain the additional meter-reading personnel or services necessary to reduce the meter-reading targeted window from five to three days, the Utilities will have until January 1, 2011, to meet the terms of this provision.

Section 5.23. The Parties agree that the per-attachment annual rental charge under Rate CTAC (Cable Television Attachment Charges) shall be \$5.40 for KU and \$5.35 for LG&E, as shown in the proposed tariff sheets attached hereto in Exhibits 4 and 5.

Section 5.24. The Parties agree that by July 1, 2011, KSBA's members located in the KU service territory will conduct an assessment of their KU accounts to determine whether any school building may be more efficiently served under the now-frozen Rate AES rate schedule. KU will agree to review promptly each assessment to determine each school's eligibility and whether migration to Rate AES may be more cost-advantageous on a prospective basis to one or more of the KSBA member schools located in the KU territory. KU agrees to allow such migration where appropriate up to \$500,000 projected annual savings to such member schools in total. Should the KSBA members identify a number of school buildings that exceed the \$500,000 annual savings total restriction herein, and KU concurs that such school buildings are eligible to be served under Rate AES, KU agrees that at the time of its next base rate case it will propose in

its application to allow those additional school buildings to migrate to Rate AES, subject to any modifications KU may propose. Any school buildings wherein a KSBA representative school board planned and committed to the construction of an "all electric" facility, and the KSBA can demonstrate through prior school board resolutions or meeting notes that such plans and commitments were made prior to the date of this Stipulation, and such plans and commitments were clearly based in part on the anticipated continuation of Rate AES, all to the reasonable satisfaction of KU, KU agrees these facilities may be considered to be served under Rate AES on a prospective basis. Any KSBA member school that notified KU prior to the date of this Stipulation in a documentable format of its interest in being served under Rate AES for any all electric school facility that has or is in the process of migrating to Rate AES shall not be counted toward the \$500,000 restriction herein. Nothing herein shall be construed to create or vest a right in the members of the KSBA to the continuation of or rate structure for Rate AES in any form in the future.

Section 5.25. The Parties agree that LG&E shall exempt from the application of Rate DGGS locations that install back-up generators using less than 2,000 cf/hr (approximately equivalent to a 200 kVA gas-fired generator) if the customers who own such generators agree to use them only to provide emergency power. The proposed Rate DGGS tariff sheet contained in Exhibit 6 hereto contains this exemption.

Section 5.26. The Parties agree that, except as modified in this Stipulation and Recommendation and the exhibits attached hereto, the rates, terms, and conditions proposed by the Utilities in the rate proceedings shall be approved as filed. Approval of this Stipulation and Recommendation shall not be construed to approve or deny the adjustments to LG&E's and KU's electric revenues and expenses associated with the normalization of weather.

ARTICLE VI. Miscellaneous Provisions.

Section 6.1. Except as specifically stated otherwise in this Stipulation and Recommendation, the Parties agree that making this Stipulation and Recommendation shall not be deemed in any respect to constitute an admission by any party hereto that any computation, formula, allegation, assertion, or contention made by any other party in these proceedings is true or valid.

Section 6.2. The Parties agree that the foregoing stipulations and agreements represent a fair, just, and reasonable resolution of the issues addressed herein.

Section 6.3. The Parties agree that, following the execution of this Stipulation and Recommendation, the Parties shall cause the Stipulation and Recommendation to be filed with the Commission by June 7, 2010, together with a recommendation that the Commission enter its Orders implementing the terms and conditions herein for rates to become effective on August 1, 2010.

Section 6.4. Each signatory waives all cross-examination of the other Parties' witnesses unless the Commission disapproves this Stipulation and Recommendation, and each signatory further stipulates and recommends that the Notice of Intent, Notice, Application, testimony, pleadings, and responses to data requests filed in this proceeding be admitted into the record. The Parties stipulate that after the date of this Stipulation and Recommendation they will not otherwise contest the Utilities' proposals, as modified by this Stipulation and Recommendation, in the hearing of the rate proceedings, and that they will refrain from cross-examination of the Utilities' witnesses during the hearing, except insofar as such cross-examination is in support of the Stipulation and Recommendation.

Section 6.5. The Parties agree to act in good faith and to use their best efforts to recommend to the Commission that this Stipulation and Recommendation be accepted and approved.

Section 6.6. If the Commission issues an order adopting all of the terms and conditions recommended herein, each of the Parties agrees that it shall file neither an application for rehearing with the Commission, nor an appeal to the Franklin Circuit Court with respect to such order.

Section 6.7. The Parties agree that if the Commission does not implement in its Orders in these proceedings all of the terms recommended herein, then: (a) this Stipulation and Recommendation shall be void and withdrawn by the Parties from further consideration by the Commission and none of the Parties shall be bound by any of the provisions herein, provided that no

party is precluded from advocating any position contained in this Stipulation and Recommendation; and (b) neither the terms of this Stipulation and Recommendation nor any matters raised during the settlement negotiations shall be binding on any of the Parties to this Stipulation and Recommendation or be construed against any of the Parties.

Section 6.8. The Parties agree that this Stipulation and Recommendation shall in no way be deemed to divest the Commission of jurisdiction under Chapter 278 of the Kentucky Revised Statutes.

Section 6.9. The Parties agree that this Stipulation and Recommendation shall inure to the benefit of, and be binding upon, the Parties, their successors and assigns.

Section 6.10. The Parties agree that this Stipulation and Recommendation constitutes the complete agreement and understanding among the Parties, and any and all oral statements, representations, or agreements made prior hereto or contemporaneously herewith, shall be null and void, and shall be deemed to have been merged into this Stipulation and Recommendation.

Section 6.11. The Parties agree that, for the purpose of this Stipulation and Recommendation only, the terms are based upon the independent analysis of the Parties to reflect a fair, just, and reasonable resolution of the issues herein and are the product of compromise and negotiation.

Section 6.12. The Parties agree that neither the Stipulation and Recommendation nor any of the terms shall be admissible in any court or commission except insofar as such court or commission is addressing litigation arising out of the

implementation of the terms herein. This Stipulation and Recommendation shall not have any precedential value in this or any other jurisdiction.

Section 6.13. The Parties warrant that they have informed, advised, and consulted with the Parties they represent in the rate proceedings in regard to the contents and *significance of this Stipulation and Recommendation*, and based upon the foregoing are authorized to execute this Stipulation and Recommendation on behalf of the Parties they represent.

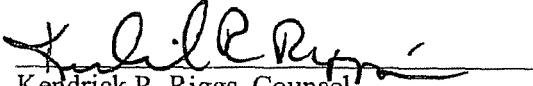
Section 6.14. The Parties agree that this Stipulation and Recommendation is a product of negotiation among all Parties, and that no provision of this Stipulation and Recommendation shall be strictly construed in favor of, or against, any party. Notwithstanding anything contained in this Stipulation and Recommendation, the Parties recognize and agree that the effects, if any, of any future events upon the operating income of the Utilities are unknown and that, if implemented, this Stipulation and Recommendation shall be implemented as written.

Section 6.15. The Parties agree that this Stipulation and Recommendation may be executed in multiple counterparts.

IN WITNESS WHEREOF, the Parties have hereunto affixed their signatures.

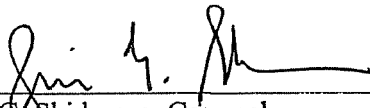
Louisville Gas and Electric Company
and Kentucky Utilities Company

HAVE SEEN AND AGREED:


Kendrick R. Riggs, Counsel
Allyson K. Sturgeon, Counsel

Community Action Council for
Lexington-Fayette, Bourbon, Harrison
and Nicholas Counties, Inc.

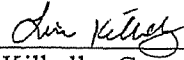
HAVE SEEN AND AGREED:



Iris G. Skidmore, Counsel

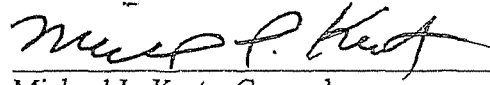
Association of Community Ministries

HAVE SEEN AND AGREED:



Lisa Kilkey, Counsel

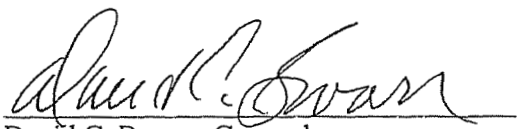
Kentucky Industrial Utility Customers, Inc.
HAVE SEEN AND AGREED:

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Michael L. Kurtz, Counsel
Kurt J. Boehn, Counsel

The Kroger Co.

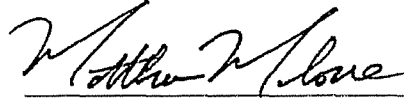
HAVE SEEN AND AGREED:

A handwritten signature in cursive script, appearing to read "David C. Brown", written over a horizontal line.

David C. Brown, Counsel

Kentucky School Boards Association


HAVE SEEN AND AGREED:

A handwritten signature in black ink, appearing to read "Matthew R. Malone". The signature is written in a cursive style with a large initial "M".

Matthew R. Malone, Counsel

Kentucky Cable Telecommunications
Association

HAVE SEEN AND AGREED:



Laurence J. Zielke, Counsel
Gardner F. Gillespie, Counsel
Dominic F. Perella, Counsel

AARP

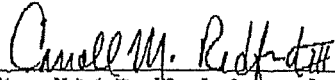
HAVE SEEN AND AGREED:

A handwritten signature in black ink, consisting of a large, stylized initial 'T' followed by a long horizontal stroke and a small loop at the end.

Hon. Tom FitzGerald
On behalf of AARP

Wal-Mart Stores East, LLP and
Sam's East, Inc.

HAVE SEEN AND AGREED:



Carroll M. Redford, Counsel
Holly Rachel Smith, Counsel

APPENDIX B

APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE COMMISSION IN CASE NO. 2009-00549 DATED JUL 30 2010

The following rates and charges are prescribed for the customers in the area served by Louisville Gas & Electric Company. All other rates and charges not specifically mentioned herein shall remain the same as those in effect under authority of this Commission prior to the effective date of this Order.

ELECTRIC SERVICE RATES

SCHEDULE RS RESIDENTIAL SERVICE

Basic Service Charge per Month	\$8.50
Energy Charge per kWh	\$.07068

SCHEDULE VFD VOLUNTEER FIRE DEPARTMENT SERVICE

Basic Service Charge per Month	\$8.50
Energy Charge per kWh	\$.07068

SCHEDULE GS GENERAL SERVICE RATE

Basic Service Charge per Month – Single Phase	\$17.50
Basic Service Charge per Month – Three Phase	\$32.50
Energy Charge per kWh	\$.08051

SCHEDULE PS POWER SERVICE RATE

<u>Secondary Service:</u>	
Basic Service Charge per Month	\$90.00
Demand Charge per kW:	
Summer Rate	\$15.32
Winter Rate	\$13.07
Energy Charge per kWh	\$.03264

Primary Service:

Basic Service Charge per Month	\$90.00
Demand Charge per kW:	
Summer Rate	\$13.48
Winter Rate	\$11.24
Energy Charge per kWh	\$.03264

SCHEDULE CTODP
COMMERCIAL TIME-OF-DAY PRIMARY SERVICE RATE

Basic Service Charge per Month	\$200.00
Maximum Load Charge per kVA:	
Peak Demand Period	\$ 5.70
Intermediate Demand Period	\$ 4.20
Base Demand Period	\$ 2.64
Energy Charge per kWh	\$.03226

SCHEDULE CTODS
COMMERCIAL TIME-OF-DAY SECONDARY SERVICE

Basic Service Charge per Month	\$200.00
Maximum Load Charge per kW:	
Peak Demand Period	\$ 5.81
Intermediate Demand Period	\$ 4.28
Base Demand Period	\$ 3.79
Energy Charge per kWh	\$.03226

SCHEDULE ITODS
INDUSTRIAL TIME-OF-DAY SECONDARY SERVICE RATE

Basic Service Charge per Month	\$ 300.00
Maximum Load Charge per kW:	
Peak Demand Period	\$ 5.20
Intermediate Demand Period	\$ 3.70
Base Demand Period	\$ 5.48
Energy Charge per kWh	\$.02827

SCHEDULE ITODP
INDUSTRIAL TIME-OF-DAY PRIMARY SERVICE RATE

Basic Service Charge per Month	\$300.00
Demand Charge per kW:	
Basic Demand	\$ 4.16
Peak Demand:	
Summer Peak Period	\$ 10.11
Winter Peak Period	\$ 7.31
Energy Charge per kWh	\$.02827

SCHEDULE RTS
RETAIL TRANSMISSION SERVICE

Basic Service Charge per Month	\$500.00
Maximum Load Charge per kW:	
Peak Demand Period	\$ 4.36
Intermediate Demand Period	\$ 2.86
Base Demand Period	\$ 2.61
Energy Charge per kWh	\$.02827

SCHEDULE FLS
FLUCTUATING LOAD SERVICE

<u>Primary:</u>	
Basic Service Charge per Month	\$500.00
Maximum Load Charge per kVA:	
Peak Demand Period	\$ 2.75
Intermediate Demand Period	\$ 1.75
Base Demand Period	\$ 1.75
Energy Charge per kWh	\$.03553

<u>Transmission:</u>	
Basic Service Charge per Month	\$500.00
Maximum Load Charge per kVA:	
Peak Demand Period	\$ 2.75
Intermediate Demand Period	\$ 1.75
Base Demand Period	\$ 1.00
Energy Charge per kWh	\$.03271

SCHEDULE LS
LIGHTING SERVICE

Underground Service

	<u>Lumen Output</u> <u>(approximate)</u>	<u>Monthly Rate</u> <u>Per Light</u>
High Pressure Sodium		
4 Sided Colonial	5,800	\$ 18.59
4 Sided Colonial	9,500	\$ 19.16
4 Sided Colonial	16,000	\$ 20.24
Acorn	5,800	\$ 18.96
Acorn	9,500	\$ 21.16
Acorn (Bronze Pole)	9,500	\$ 22.24
Acorn	16,000	\$ 22.15
Acorn (Bronze Pole)	16,000	\$ 23.16

Contemporary	16,000	\$ 28.23
Fixture Only	16,000	\$ 15.26
Contemporary	28,500	\$ 31.39
Fixture Only	28,500	\$ 17.31
Contemporary	50,000	\$ 35.73
Fixture Only	50,000	\$ 20.21
Cobra Head	16,000	\$ 24.81
Cobra Head	28,500	\$ 27.13
Cobra Head	50,000	\$ 31.52
* London (10' Smooth Pole)	5,800	\$ 31.56
* London (10' Fluted Pole)	5,800	\$ 33.47
* London (10' Smooth Pole)	9,500	\$ 32.30
* London (10' Fluted Pole)	9,500	\$ 34.21
* Victorian (10' Smooth Pole)	5,800	\$ 30.63
* Victorian (10' Fluted Pole)	5,800	\$ 31.28
* Victorian (10' Smooth Pole)	9,500	\$ 32.53
* Victorian (10' Fluted Pole)	9,500	\$ 33.17
* Bases Available:		
Old Town / Manchester		\$ 2.83
Chesapeake / Franklin		\$ 2.83
Jefferson / Westchester		\$ 2.83
Norfolk / Essex		\$ 3.00
<u>Mercury Vapor</u>		
4 Sided Colonial	4,000	\$ 16.35
4 Sided Colonial	8,000	\$ 17.92
Cobra Head	8,000	\$ 21.89
Cobra Head	13,000	\$ 23.31
Cobra Head	25,000	\$ 26.69
Overhead Service		
<u>High Pressure Sodium</u>		
Cobra Head	16,000	\$ 11.50
Cobra Head	28,500	\$ 13.83
Cobra Head	50,000	\$ 18.22
Directional Flood	16,000	\$ 13.11
Directional Flood	50,000	\$ 19.19
Open Bottom	9,500	\$ 10.20
<u>Mercury Vapor</u>		

Cobra Head	8,000	\$ 10.16
Cobra Head	13,000	\$ 11.59
Cobra Head	25,000	\$ 14.96
Directional Flood	25,000	\$ 16.31
Open Bottom	8,000	\$ 9.90
Additional Pole Charge		\$ 10.92

METAL HALIDE COMMERCIAL AND INDUSTRIAL LIGHTING

Metal Halide

Directional Fixture Only	12,000	\$11.79
Directional Fixture/Wood Pole	12,000	\$13.99
Directional Fixture/Direct Burial Metal Pole	12,000	\$21.20
Directional Fixture Only	32,000	\$16.95
Directional Fixture/Wood Pole	32,000	\$19.16
Directional Fixture/Metal Pole	32,000	\$26.36
Directional Fixture Only	107,800	\$35.07
Directional Fixture/Wood Pole	107,800	\$38.14
Directional Fixture/Metal Pole	107,800	\$44.47
Contemporary Fixture Only	12,000	\$13.02
Contemporary Fixture/Direct Burial Metal Pole	12,000	\$22.45
Contemporary Fixture Only	32,000	\$18.67
Contemporary Fixture/Metal Pole	32,000	\$28.09
Contemporary Fixture Only	107,800	\$37.93
Contemporary Fixture/Metal Pole	107,800	\$47.34

SCHEDULE RLS
RESTRICTED LIGHTING SERVICE

OUTDOOR LIGHTING

<u>Overhead Service</u>	<u>Rate per Month per Unit</u>	
	<u>To 1/1/1991</u>	<u>After 12/31/1990</u>
<u>Mercury Vapor</u>		
100 Watt	\$ 7.89	N/A
175 Watt	\$ 8.82	\$ 10.22
250 Watt	\$ 10.18	\$ 11.65
400 Watt	\$ 12.54	\$ 14.15
1000 Watt	\$ 23.44	\$ 26.08
1000 Watt Flood	\$ 23.44	\$ 26.21
<u>High Pressure Sodium</u>		
100 Watt	\$ 9.88	\$ 9.88
150 Watt	\$ 12.51	\$ 12.51
250 Watt	\$ 14.75	\$ 14.75
400 Watt	\$ 16.03	\$ 16.03
1000 Watt	N/A	\$ 37.40
 <u>Additional Pole Charge</u>	 \$ 1.99	 \$ 1.99

Underground Service

<u>Mercury Vapor</u>		
100 Watt Top Mounted	\$ 13.13	\$ 13.12
175 Watt Top Mounted	\$ 13.91	\$ 14.88
400 Watt Top Mounted	\$ 16.11	\$ 16.11
<u>High Pressure Sodium</u>		
70 Watt Top Mounted	\$ 13.22	\$ 13.22
100 Watt Top Mounted	\$ 17.37	\$ 17.56
150 Watt Top Mounted	N/A	\$ 20.97
150 Watt	\$ 23.41	\$ 23.41
250 Watt	\$ 26.92	\$ 26.92
400 Watt	\$ 30.00	\$ 30.00
1000 Watt	\$ NA	\$ 67.18

Decorative Lighting ServiceRate per monthFixturesAcorn with Decorative Basket

70 Watt High Pressure Sodium \$ 18.37

100 Watt High Pressure Sodium \$ 19.36

8-Sided Coach

70 Watt High Pressure Sodium \$ 18.55

100 Watt High Pressure Sodium \$ 19.56

Poles10 ft. Smooth \$ 10.4410 ft. Fluted \$ 12.46BasesOld Town/Manchester \$ 3.35Chesapeake/Franklin \$ 3.60Jefferson/Winchester \$ 3.62Norfolk/Essex \$ 3.81

PUBLIC STREET LIGHTING

<u>Overhead Service</u>	<u>Rate per Month per Unit</u>	
	<u>To 1/1/1991</u>	<u>After 12/31/1990</u>
<u>Mercury Vapor</u>		
100 Watt	\$ 7.17	N/A
175 Watt	\$ 8.25	\$ 10.04
250 Watt	\$ 9.57	\$ 11.46
400 Watt	\$ 11.64	\$ 13.95
400 Watt (Metal Pole)	\$ 16.15	N/A
1,000 Watt	\$ 22.12	\$ 25.83
<u>High Pressure Sodium Vapor</u>		
100 Watt	\$ 9.58	\$ 9.58
150 Watt	\$ 11.40	\$ 11.40
150 Watt Flood	\$ 13.73	\$ 11.40
250 Watt	\$ 13.64	\$ 13.64
400 Watt	\$ 14.66	\$ 14.66
1,000 Watt	N/A	\$ 32.97
<u>Underground Service</u>		
<u>Mercury Vapor</u>		
100 Watt-Top Mounted	\$ 11.17	\$ 13.86
175 Watt-Top Mounted	\$ 12.15	\$ 14.68
175 Watt (metal pole)	\$ 16.18	\$ 23.12
250 Watt	\$ 17.54	\$ 24.05
400 Watt	\$ 20.85	\$ 27.09
400 Watt (State of Ky. pole)	\$ 20.95	\$ 20.95

High Pressure Sodium Vapor

70 Watt-Top Mounted		N/A	\$	13.30
100 Watt-Top Mounted	\$	13.87	\$	13.87
150 Watt-Top Mounted		N/A	\$	20.14
150 Watt	\$	23.39	\$	23.39
250 Watt	\$	24.98	\$	24.98
250 Watt on State of Ky. Pole	\$	24.98	\$	24.98
400 Watt	\$	27.18	\$	27.18
400 Watt on State of Ky. Pole	\$	27.18	\$	27.18
1000 Watt		N/A	\$	62.75

Overhead Service

Incandescent

100 Watt	\$	8.35	\$	8.35
300 Watt	\$	11.89	\$	11.89

Decorative Lighting Service

Rate per month

Fixtures

Acorn with Decorative Basket

70 Watt High Pressure Sodium	\$	17.92
100 Watt High Pressure Sodium	\$	18.79

8-Sided Coach

70 Watt High Pressure Sodium	\$	18.13
100 Watt High Pressure Sodium	\$	19.39

Poles

10 ft. Smooth	\$	10.44
10 ft. Fluted	\$	12.46

Bases

Old Town/Manchester	\$	3.35
Chesapeake/Franklin	\$	3.60
Jefferson/Winchester	\$	3.62
Norfolk/Essex	\$	3.81

SCHEDULE LE
LIGHTING ENERGY SERVICE

Energy Charge per kWh	\$.05465
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SCHEDULE TE
TRAFFIC ENERGY SERVICE

Basic Service Charge per Month	\$	3.14
Energy Charge per kWh	\$.06623

SCHEDULE CTAC
CABLE TELEVISION ATTACHMENT CHARGES

Per Year for Each Attachment to Pole \$ 5.35

SCHEDULE CSR10
CURTAILABLE SERVICE RIDER 10

	<u>Transmission</u>	<u>Primary</u>
Demand Credit per kW per Month	\$ 5.40	\$ 5.50
Non-compliance Charge Per kW Per Month	\$ 16.00	\$ 16.00

SCHEDULE CSR30
CURTAILABLE SERVICE RIDER 30

	<u>Transmission</u>	<u>Primary</u>
Demand Credit per kW per Month	\$ 4.30	\$ 4.40
Non-compliance Charge Per kW Per Month	\$ 16.00	\$ 16.00

SCHEDULE EF
EXCESS FACILITIES

Monthly Charge for Leased Facilities	1.66%
Monthly Charge for Facilities Supported by One-time CIAC Payment	.86%

SCHEDULE RC
REDUNDANT CAPACITY

Capacity Reservation Charge per kW:

Secondary Distribution	\$ 1.52
Primary Distribution	\$ 1.13

SCHEDULE SS
SUPPLEMENTAL OR STANDBY SERVICE

Contract Demand per kVA:

Secondary	\$ 8.23
Primary	\$ 7.21
Transmission	\$ 6.08

SCHEDULE RRP
RESIDENTIAL RESPONSIVE PRICING SERVICE

Basic Service Charge per Month	\$13.50
Energy Charge per kW:	
Low Cost Hours	\$.04872
Medium Cost Hours	\$.06168
High Cost Hours	\$.11873
Critical Cost Hours	\$.32364

SCHEDULE GRP
GENERAL RESPONSIVE PRICING SERVICE

Basic Service Charge per Month:	
Single-phase	\$27.50
Three-phase	\$42.50
Energy Charge per kWh:	
Low Cost Hours	\$.05649
Medium Cost Hours	\$.07232
High Cost Hours	\$.15134
Critical Cost Hours	\$.32783

SCHEDULE LEV
LOW EMISSION VEHICLE SERVICE

Basic Service Charge per Month	\$ 8.50
Energy Charge per kWh:	
Off Peak Hours	\$.04872
Intermediate Hours	\$.06896
Peak Hours	\$.13274

METER PULSE CHARGE

Charge per Month per Installed Set of Pulse Generating Equipment	\$ 9.00
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CUSTOMER DEPOSITS

Customers Served Under Residential Service Rate RS	\$ 135.00
Combination Gas and Electric Residential Customers	\$ 250.00

GAS SERVICE RATES

RATE RGS
RESIDENTIAL GAS SERVICE

Basic Service Charge Per Month	\$ 12.50
Distribution Charge Per Ccf	\$.22396

RATE VFD
VOLUNTEER FIRE DEPARTMENT SERVICE

Basic Service Charge Per Month	\$ 12.50
Distribution Charge Per Ccf	\$.22396

RATE CGS
FIRM COMMERCIAL GAS SERVICE

Basic Service Charge Per Month	
Meters < 5000 cf/hr	\$ 30.00
Meters >= 5000 cf/hr	\$ 170.00
Distribution Charge Per Ccf	\$.18722

Gas Transportation Service/Standby Rider to Rate CGS

Administrative Charge Per Month	\$ 153.00
Distribution Charge Per Mcf	\$ 1.8722

RATE IGS
FIRM INDUSTRIAL GAS SERVICE

Basic Service Charge Per Month	
Meters < 5000 cf/hr	\$ 30.00
Meters >= 5000 cf/hr	\$ 170.00
Distribution Charge Per Ccf	\$.19022

Gas Transportation Service/Standby Rider to Rate IGS

Administrative Charge Per Month	\$ 153.00
Distribution Charge Per Mcf	\$ 1.9022

RATE DGGS
DISTRIBUTED GENERATION GAS SERVICE

Basic Service Charge Per Month	
Meters < 5000 cf/hr	\$ 30.00
Meters >= 5000 cf/hr	\$ 170.00
Demand Charge per Ccf of Monthly Billing Demand	\$ 1.0110
Distribution Charge per Ccf	\$.02744

RATE GMPS
GAS METER PULSE SERVICE

Monthly Charge for FT Customers	\$ 8.10
Monthly Charge for Non-FT Customers	\$ 21.06

STANDARD RIDER FOR EXCESS FACILITIES

Excess Facilities Charge Percentage Applied to Original Installed Cost:

Monthly Charge for Leased Facilities	1.66%
Monthly Charge for one-time CIAC Payment Facilities	.86%

CUSTOMER DEPOSITS

Customers Served Under Residential Service Rate RGS	\$ 115.00
Combination Gas and Electric Residential Customers	\$ 250.00

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