March 5, 2010

Kentucky Public Service Commission
P. O. Box 615
211 Sower Blvd.
Frankfort, KY 40602-0615

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PUBLIC SERVICE COMMISSION

RE: LG&E Rate Increase Request (Case Number: 2009-00549)

Dear Public Service Commission Request Reviewer:

I oppose a portion of the rate increases that are being requested by LG&E. They claim they need part of the increase to help them recover the expenses they incurred as a result of extraordinary storm damages in recent years. It would be wrong to grant them an increase in rates for that reason.

When EON purchased LG&E, I believe the acquisition was priced to provide an investment return of over 12% per year. That was not because risk-free investments were yielding that rate of return. It was because they were making an investment in an enterprise involving risks and the 12+% targeted yield was deemed to be the appropriate risk-adjusted yield for the acquisition. If future experience turned out to be consistent with their pricing assumptions, they would realize the priced-for yield. But, if experience turned out to be adverse to those assumptions, their yield would suffer accordingly and could even go negative - - which justifies the higher priced-for yield. Inherent in risk-based pricing is the expectation that an owner enjoys an above market yield when times are good and suffers the consequences when they go bad, or if it turns out that the pricing assumptions were inappropriate.

We can be sure their pricing assumptions had some allowances for ongoing storm damages. The excess losses from these abnormally high storm damages should be viewed as one of those unexpected adverse events that LG&E's owners should absorb, consistent with the theory that justifies the high risk-based return they have enjoyed in favorable times. To permit them to raise rates to recover such excess losses removes their investment risk and invalidates the justification for the above-market yield.

In other words, if the Public service Commission routinely permits LG&E to adjust rates to cover adverse developments so they can achieve their targeted yield, we cannot justify that yield being anywhere near the 12+% level. If LG&E does not face the risk of having to absorb such losses themselves, their owners would be entitled to only a risk-free rate of return - - which would likely be around half of what they have been enjoying.

Naturally, LG&E's shareholders want to continually see consistently high earnings. But, we must not lose sight of the fact that the earnings delivered in most years were justifiably high because of the possibility of there being some years where those earnings could be greatly diminished or wiped out. Such is the nature of equity ownership. Our utilities are regulated to ensure rates are fair. Allowing LG&E to pass these costs to its customers would be wrong. If the Public Service Commission grants this increase on those grounds, it then needs to readdress what rate of return would be appropriate for the LG&E shareholders - - and it would have to be much lower - - and then manage results down to that lower level over future years (which would certainly be unpopular with the shareholders).

Sincerely,

Leonard Buckner

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