

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

AN ELECTRONIC EXAMINATION BY THE)	
PUBLIC SERVICE COMMISSION OF THE)	CASE NO.
ENVIRONMENTAL SURCHARGE)	2017-00327
MECHANISM OF KENTUCKY POWER)	
COMPANY FOR THE TWO-YEAR BILLING)	
PERIOD ENDING JUNE 30, 2017)	

ORDER

On August 31, 2017, the Commission initiated a two-year review of Kentucky Power Company's ("Kentucky Power") environmental surcharge, as billed to customers for the two-year period from July 1, 2015, to June 30, 2017.¹ Pursuant to KRS 278.183(3), the Commission must review, at six-month intervals, the past operations of the environmental surcharge; disallow any surcharge amounts that are not just and reasonable; and reconcile past surcharge collections with actual costs recoverable. At two-year intervals, the Commission must review and evaluate the past operations of the environmental surcharge, disallow improper expenses, and, to the extent appropriate, incorporate surcharge amounts found just and reasonable into the existing base rates of the utility.

The Commission issued a procedural schedule on August 31, 2017, that provided for discovery, the filing of prepared testimony, intervenor testimony and discovery on intervenor testimony. Kentucky Power filed prepared direct testimony and responded to two requests for information. No parties sought to intervene in this

¹ Since Kentucky Power's surcharge is billed on a two-month lag, the amounts billed from July 2015 through June 2017 are based on costs incurred from May 2015 through April 2017.

proceeding. On December 15, 2017, Kentucky Power requested that this case be submitted for a decision based on the existing record without a public hearing.

SURCHARGE ADJUSTMENT

In Case No. 2016-00336,² Kentucky Power identified two errors that affected expense months for the first three six-month periods of the current two-year review period and proposed adjustments to correct the errors. First, Kentucky Power failed to reflect monthly retirements of compliance equipment at its Rockport and Mitchell Generating Stations, which resulted in a total over-recovery of \$425,136 during the two-year review period.³ Kentucky Power returned \$118,185 for the period November 2015 through April 2016, as an adjustment to the jurisdictional revenue requirement in May 2017; returned \$225,754 for the period May 2016 through September 2016 as an adjustment to the jurisdictional revenue requirement for four months beginning in February 2017⁴; and proposes to return the remaining over-recovery of \$81,197 associated with the expense months June 2015 through October 2015, which were prior to the Case No. 2016-00336 review period, in the first month after entry of this Order.⁵

Second, for the expense months of July 2015 through August 2016, Kentucky Power identified a formulaic error that overstated non-residential, non-fuel revenues,

² Case No. 2016-00336, *Electronic Examination by the Public Service Commission of the Environmental Surcharge Mechanism of Kentucky Power Company for the Six-Month Billing Period Ending June 30, 2016* (Ky. PSC Apr. 18, 2017).

³ *Id.*, Final Order at 3. Kentucky Power over-recovered \$81,197 for the period June 2015 through October 2015, \$118,185 for the period November 2015 through April 2016, and \$225,754 for the period May 2016 through September 2016.

⁴ Case No. 2017-00072, *Electronic Examination by the Public Service Commission of the Environmental Surcharge Mechanism of Kentucky Power Company for the Six-Month Billing Period Ending December 31, 2016* (Ky. PSC July 05, 2017), Final Order at 2-3.

⁵ Direct Testimony of Amy J. Elliott (“Elliott Testimony”) at 4.

and understated the non-residential surcharge factor, which resulted in a total misallocation of costs of \$1,588,690 between residential and non-residential customers.⁶ To correct the misallocation of \$877,392 for the November 2015 through April 2016 expense months, Kentucky Power reduced the residential environmental revenue requirement by \$146,232 per month for the six months beginning in May 2017 and increased the non-residential environmental revenue requirement by the same amount.⁷ For the misallocation of \$537,612 that occurred during the expense months of May 2016 through August 2016, Kentucky Power made monthly adjustments of \$134,403 to the February 2017 through May 2017 expense month calculations.⁸ The remaining balance of the misallocation is for the period July 2015 through October 2015 and Kentucky Power proposes to allocate this balance of \$173,686 in the first month after entry of this Order.⁹

Additionally, Kentucky Power identified an over-recovery of \$46,341¹⁰ because the monthly environmental surcharge filings during 21 months of the two-year review period did not accurately reflect a statutory reduction to the Indiana Adjusted Gross Income tax rate included in the weighted average cost of capital (“WACC”) used in the calculation of environmental costs recoverable for the Rockport plant.¹¹ Kentucky

⁶ Case No. 2016-00336, Final Order at 3. ($\$877,392 + \$537,612 + \$173,686$)

⁷ *Id.* at 4.

⁸ Case No. 2017-00072, Final Order at 3.

⁹ Elliott Testimony at 4.

¹⁰ Kentucky Power’s Response to Commission Staff’s Second Request for Information (“Staff’s Second Request”), Item 2. This amount was revised due to rounding differences.

¹¹ Kentucky Power’s Response to Commission Staff’s First Request for Information (“Staff’s First Request”), Item 9.

Power proposes to refund the over-collection of \$46,341 in the first month after entry of this Order.¹²

The August 31, 2017 Order initiating this case indicated that since the period under review in this proceeding may have resulted in over- or under-recoveries, the Commission would entertain proposals to adopt one adjustment factor to net all over- or under-recoveries. The Commission has reviewed and finds reasonable Kentucky Power's calculation of a net over-recovery of \$127,538¹³ and a misallocation of \$173,686 for the review period covered in this proceeding. The Commission also finds reasonable Kentucky Power's proposal to refund the over-recovery by decreasing the total jurisdictional environmental surcharge revenue requirement by \$127,538, beginning in the first month following entry of this Order. Additionally, the Commission finds reasonable Kentucky Power's proposal to correct the misallocation by decreasing the residential environmental revenue requirement and increasing the non-residential environmental revenue requirement by \$173,686 in the first month after entry of this Order. Kentucky Power states that the average residential customer's monthly usage for the current review period was 1,215 kWh.¹⁴ Using rates and adjustment clause factors in effect for the June 2017 billing month, an average residential customer's bill would decrease by approximately \$1.69.¹⁵

¹² Kentucky Power's Response to Staff's Second Request, Item 2.

¹³ Over-recovery of \$81,197 and \$46,341 (See footnotes 5 & 12).

¹⁴ Kentucky Power's Response to Staff's First Request, Item 8.

¹⁵ *Id.*

SURCHARGE ROLL-IN

Kentucky Power is not proposing to incorporate any additional surcharge amounts into its base rates in conjunction with this two-year review.¹⁶ On January 18, 2018, the Commission established new base rates, which included \$44,379,316 of Mitchell non-FGD and Rockport environmental surcharge amounts, for Kentucky Power in Case No. 2017-00179.¹⁷ The environmental surcharge statute directs the Commission to incorporate surcharge amounts found just and reasonable into the utility's existing base rates, but only "to the extent appropriate."¹⁸ The Commission has reviewed and finds reasonable Kentucky Power's recommendation to not incorporate additional environmental surcharge amounts into base rates in this proceeding.

RATE OF RETURN

In previous environmental surcharge reviews the Commission has been guided by its findings in Case No. 1996-00489¹⁹ with respect to the determination of the WACC to be used prospectively in Kentucky Power's monthly environmental surcharge filings. However, the Settlement Agreement in Case No. 2017-00179 now supersedes the findings in Case No. 1996-00489. The Commission takes notice that Kentucky Power

¹⁶ Kentucky Power's Response to Staff's First Request, Item 4.

¹⁷ Case No. 2017-00179, *The Application of Kentucky Power Company for: (1) A General Adjustment of Its Rates for Electric Service; (2) An Order Approving Its 2017 Environmental Compliance Plan; (3) An Order Approving Its Tariffs and Riders; (4) An Order Approving Accounting Practices to Establish Regulatory Assets and Liabilities; and (5) An Order Granting All Other Required Approvals and Relief* (Ky. PSC Jan. 18, 2018).

¹⁸ KRS 278.183(3).

¹⁹ Case No. 1996-00489, *Application of Kentucky Power Company d/b/a American Electric Power to Assess a Surcharge Under KRS 278.183 to Recover Costs of Compliance with the Clean Air Act and Those Environmental Requirements Which Apply to Coal Combustion Waste and By-Products* (Ky. PSC May 27, 1997).

filed a base rate application docketed as Case No. 2017-00179.²⁰ We also take notice that the Final Order was issued in that proceeding on January 18, 2018, wherein the Commission determined that for environmental surcharge purposes, Kentucky Power is authorized a return on common equity of 9.70 percent.²¹ It also specifies that Kentucky Power utilize a WACC of 6.44²² percent and a gross revenue conversion factor (“GRCF”) of 1.352166²³ in the monthly environmental surcharge filings. Utilizing a WACC of 6.44 percent and a GRCF of 1.352116 produces a rate of return of 7.88 percent to be used in the monthly environmental surcharge filings.²⁴ The WACC and GRCF shall remain constant until the Commission sets base rates in Kentucky Power’s next base rate case proceeding. Therefore, the Commission finds that the combination of these components, which produces an overall grossed-up rate of return of 7.88 percent, should be used in all monthly environmental surcharge filings subsequent to entry of this Order.

IT IS THEREFORE ORDERED that:

1. Kentucky Power’s request to submit this case for a decision on the existing evidence of record without a hearing is granted.
2. Kentucky Power’s determination that it had a net over-recovery of \$127,538 for the review period is approved, and it shall return the over-recovery in the first month subsequent to entry of this Order.

²⁰ Case No. 2017-00179, (Ky. PSC Jan. 18, 2017).

²¹ *Id.* at 27.

²² *Id.*

²³ *Id.* at 66.

²⁴ *Id.*

3. Kentucky Power's determination that it had a misallocation between the residential and non-residential customer classes of \$173,686 for the review period is approved, and it shall correct the misallocation of \$173,686 in the first month subsequent to entry of this Order.

4. Kentucky Power shall use a weighted average cost of capital of 6.44 percent and a tax gross-up factor of 1.352116, a return on equity rate of 9.70 percent, and an overall grossed-up return of 7.88 percent in all monthly environmental surcharge filings subsequent to entry of this Order.

5. The environmental surcharge amounts determined by Kentucky Power for the two-year review period ending June 2017 are just and reasonable.

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By the Commission

ENTERED
FEB 22 2018
KENTUCKY PUBLIC
SERVICE COMMISSION

ATTEST:


Executive Director

Case No. 2017-00327

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