

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

LOUISVILLE GAS AND ELECTRIC COMPANY'S)
ANNUAL EARNINGS SHARING MECHANISM) CASE NO.
FILING FOR CALENDAR YEAR 2001) 2002-00071

and

KENTUCKY UTILITIES COMPANY'S ANNUAL)
EARNINGS SHARING MECHANISM FILING FOR) CASE NO.
CALENDAR YEAR 2001) 2002-00072

O R D E R

On November 4, 2002, the Kentucky Industrial Utility Customers, Inc. ("KIUC") filed an application for rehearing of the Commission's October 16, 2002 Orders concerning the operation of the Earnings Sharing Mechanisms ("ESM") of Louisville Gas and Electric Company ("LG&E") and Kentucky Utilities Company ("KU"). LG&E and KU filed a joint petition for rehearing on the Orders on November 6, 2002.

Based on the petitions and the responses thereto, the Commission will grant rehearing on the issues discussed in the findings below.

Interest on Refunds

KIUC seeks rehearing on the issue of whether interest should be included in the refunds required by the October 16, 2002 Orders. KIUC notes its agreement with the Commission's decision on the substantive issues contained in the October 16, 2002 Orders, but believes that the Commission overlooked the matter of including interest in the amounts to be refunded. KIUC asserts that interest needs to be included on the

refunds for ratepayers to be made whole and its application cites legal precedent in support of its position.

On November 15, 2002, LG&E and KU filed a joint response in opposition to KIUC's application. LG&E and KU contend that if the Commission grants their joint petition and reconsiders the October 16, 2002 Orders, KIUC's application will be moot. LG&E and KU further contend that if their joint petition is not granted and the October 16, 2002 Orders are not reconsidered, KIUC's application requesting interest is unwarranted because LG&E and KU are complying with their respective ESM tariffs.

Based on a review of the arguments presented, the Commission finds good cause to grant rehearing to consider whether interest should be awarded on the refunds required by the October 16, 2002 Orders. The procedural schedule set forth in Appendix A to this Order establishes dates for KIUC to file direct testimony on the reasonableness of requiring interest on the refunds and the appropriate rate of interest, and for LG&E and KU to file response testimony on this issue.

Creation of Deferred Debit

LG&E and KU seek rehearing on the issue of when the deferred debits associated with the 2001 Workforce Transition Separation Program ("Workforce Reduction") should be recorded and recognized for the ESM calculations. LG&E and KU contend that the Commission's October 16, 2002 decision that the deferred debits had to be recorded on their respective books in December 2001 is inconsistent with the

Commission's December 3, 2001 Order in Case No. 2001-00169.¹ LG&E and KU argue that the December 3, 2001 Order in Case No. 2001-00169 authorized them to begin in April 2001 to amortize monthly the Workforce Reduction expenses on their income statements for rate-making purposes. LG&E and KU reason that to amortize the Workforce Reduction expenses over the 9-month period ending December 31, 2001, the associated deferred debits had to be established as of April 1, 2001, not in December 2001 as they claim was arbitrarily determined by the Commission in the October 16, 2002 Orders.

On November 19, 2002, KIUC filed its response in opposition to LG&E and KU's joint petition for rehearing. KIUC states that the Commission did not commit the error alleged by LG&E and KU. Further, KIUC argues that the Commission never construed the Global Settlement that resolved the issues in Case No. 2001-00169 to allow LG&E and KU to establish deferred debits retroactively beginning April 1, 2001. KIUC contends that the regulatory asset was established and the amortization expense was recognized on LG&E's and KU's financial statements in December 2001 in accord with the terms of the Global Settlement. KIUC concludes that the Global Settlement provided the very matching that LG&E and KU argue has been denied.

Based on a review of the arguments presented, the Commission finds good cause to grant rehearing on this issue to determine how LG&E and KU have accounted for the Workforce Reduction deferred debits and how such accounting impacts the ESM

¹ Case No. 2001-00169, Joint Application of Louisville Gas and Electric Company and Kentucky Utilities Company for an Order Approving Proposed Deferred Debits and Declaring the Amortization of the Deferred Debits to be Included in Earnings Sharing Mechanism Calculations.

calculations. In accordance with the procedural schedule, LG&E and KU should file direct testimony and supporting documentation addressing the following:

- Did LG&E and KU restate any financial statements to reflect the creation of the deferred debits and the monthly amortization of the Workforce Reduction retroactive to April 1, 2001 during 2001?
- What accounting entries did LG&E and KU make to their books and records in conjunction with the Workforce Reduction provisions of the Global Settlement approved in Case No. 2001-00169 and on what dates were these entries made?

The procedural schedule also provides an opportunity for KIUC to file response testimony on this issue.

Restatement of Capital

LG&E and KU seek rehearing of the October 16, 2002 Orders, contending that absent a retroactive restatement of their respective capital accounts, customers receive a double rate benefit from the Workforce Reduction expense. LG&E and KU argue that their objective in entering into the Global Settlement approved in Case No. 2001-00169 was only to share with customers 40 percent of the net savings derived from the Workforce Reduction expense and no more. LG&E and KU claim that the recognition in the October 16, 2002 Orders of 9 months of Workforce Reduction amortization expense in December 2001 results in a double rate benefit, comprised of the Workforce Reduction VDT Surcredits and the impact of amortization expense on the calendar year 2001 ESM calculations. LG&E and KU contend that there is an unintended impact on the ESM calculations due to recording the Workforce Reduction amortization in December 2001 and using average capitalization to determine the ESM.

In its November 19, 2002 response, KIUC contends that LG&E and KU's argument regarding the alleged double rate benefit is predicated on the use of

hypothetical common equity levels, rather than actual common equity levels as required for the ESM. KIUC argues that the use of such hypothetical common equity levels is not authorized by the Global Settlement and its use harms customers because it assumes the Workforce Reduction expense write-off in March 2001 never occurred, and that the amortization of the deferred debit and payment of the Workforce Reduction VDT Surcredit were recognized on the utilities' books from April 2001 through November 2001. KIUC notes that there is no provision in the Global Settlement, similar to that for the depreciation issue, that allows the deferred debit or the amortization expense to be restated retroactively to March 2001 for either book accounting or rate-making purposes.

Based on a review of the arguments presented, the Commission finds good cause to grant rehearing on whether the rate-making treatment adopted in the October 16, 2002 Orders is consistent with LG&E's and KU's actual average capital structures and whether ratepayers receive benefits that are inconsistent with the provisions of the Global Settlement approved in Case No. 2001-00169. In accordance with the procedural schedule, LG&E and KU should file testimony addressing all ratepayer benefits flowing from the Global Settlement, a calculation of each benefit, and an explanation of whether each benefit is inconsistent with the Global Settlement. Since the impact of using average capitalization has been raised in conjunction with this issue, the testimony should also include an analysis of all provisions of the Global Settlement relating to the resolution of KIUC's claim that average capitalization should be used every year to calculate the ESM. Therefore, LG&E and KU should also provide the impact on their respective initial ESM calculations, for calendar year 2000, as if KIUC's

original claim to use average capitalization had been adopted, rather than rejected. The procedural schedule also allows KIUC to file response testimony on this issue.

IT IS THEREFORE ORDERED that:

1. Rehearing is granted to consider whether interest should be awarded on the refunds required by the October 16, 2002 Orders and, if so, the appropriate rate of interest.
2. Rehearing is granted to investigate how LG&E and KU have accounted for the Workforce Reduction deferred debits and how this accounting impacts the ESM calculations.
3. Rehearing is granted to investigate the retroactive restatement of capital, the rate benefits received by customers as a result of the October 16, 2002 Orders, and whether any such benefits are inconsistent with the provisions of the Global Settlement.
4. The procedural schedule set forth in Appendix A, attached hereto and incorporated herein, shall be followed during the rehearing phase of these proceedings.
5. LG&E, KU, and KIUC shall file an original and 6 copies of all testimony and information addressing the issues on rehearing, as discussed in this Order.

Done at Frankfort, Kentucky, this 25th day of November, 2002.

By the Commission

ATTEST:


Executive Director

APPENDIX A

APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE COMMISSION
IN CASE NOS. 2002-00071 AND 2002-00072 DATED NOVEMBER 25, 2002

KIUC shall file its prepared direct testimony on the
issue of awarding of interest no later than.....12/16/02

LG&E and KU shall file prepared direct testimony and
the required supporting documentation and calculations
on the issues of the accounting for the Workforce Reduction,
the retroactive restatement of capital, and the ratepayer
benefits of the Global Settlement no later than.....12/16/02

KIUC shall file response testimony, if any,
no later than.....01/06/03

LG&E and KU shall file response testimony, if any,
no later than.....01/06/03

Public Hearing is to begin at 9:00 a.m., Eastern
Standard Time, in Hearing Room 1 of the Commission's
offices at 211 Sower Boulevard, Frankfort, Kentucky,
for the purpose of cross-examination of witnesses of
LG&E, KU, and KIUC.....To Be Scheduled