Duke Energy®

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Rocco O. D'Ascenzo
Associate General Counsel

VIA OVERNIGHT DELIVERY

RECEIVED

MAY 17 2011

PUBLIC SERVICE
COMMISSION

May 16, 2011

Mr. Jeff Derouen
Executive Director
Kentucky Public Service Commission
211 Sower Blvd
Frankfort, KY 40601

Re: Case No. 2011-00091
Application of Duke Energy Kentucky, Inc. to Implement a Hedging Program to Mitigate Price Volatility in the Procurement of Natural Gas

Dear Mr. Derouen:

Duke Energy Kentucky respectfully submits its response to the Commission Staff's Verbal Data Request propounded at the May 10, 2011 Technical Conference in the above referenced case.

If you have any questions, please contact Rocco O. D'Ascenzo.

Please date-stamp the two copies of the letter and the Data Requests and return to me in the enclosed envelope.

Sincerely,

Rocco O. D'Ascenzo

cc: Larry Cook (w/enclosures)

VERIFICATION

State of Ohio	)	
	)	**SS:**
County of Hamilton	)	

The undersigned, Jeff L. Kern, being duly sworn, deposes and says that he is the Manager, Gas Resources, that he has supervised the preparation of the response to the foregoing information request; and that the matters set forth in the foregoing responses to information requests are true and accurate to the best of his knowledge, information and belief, after reasonable inquiry.

Jeff L. Kern, Affiant

Subscribed and sworn to before me by Jeff L. Kern on this 13th day of May 2011.

NOTARY PUBLIC

My Commission Expires:

NOTARIAL SEAL
STATE OF OHIO

Julie M. Thompson
Notary Public, State of Ohio
My Commission Expires 11-19-2015

415051

STAFF-DR-01-001

REQUEST:

Please discuss the reasonableness of continuing with the Company's hedging plan and strategy under the current market conditions of low and stable prices for the natural gas commodity.

RESPONSE:

The goal, to the extent possible, of Duke Energy Kentucky's natural gas hedging plan is to mitigate the volatility in natural gas prices to our customers, which in turn will also protect our customers against extreme price increases. Although the current market for natural gas is at historically low and relatively stable price levels, the need for a hedging plan still exists if Duke Energy Kentucky is to achieve the goal set forth above. Volatility in natural gas prices can arise for a number of different reasons. Among the many factors impacting natural gas prices, the increased supply of natural gas from unconventional sources such as shale formations is often cited as one of the primary reasons that prices have declined since 2008. However, environmental concerns regarding hydraulic fracturing, which is used to extract natural gas from shale, could result in legislation that could limit supply from shale and cause prices to once again increase. On the demand side, an economic recovery and/or new uses for natural gas such as Natural Gas Vehicles could also cause prices to rise. These are only two examples that demonstrate the fact that there is no guarantee that natural gas prices will remain at their current level.

From a strategic perspective, a period of low and stable prices is actually a good time to lock in fixed prices for the customer. If prices remain stable, intuitively the fixed price set by the hedging plan will end up close to the market price. This means that the delta between the fixed price and the actual market price would be negligible enough that there would be little difference between the use of a hedging plan or letting prices go to market. However, since price shifts often occur with little or no warning, there is a distinct advantage to locking in prices while they are low and stable. If a company waits until prices are once again rising, the rationale behind the hedging process is lost.

Further, based on the customer survey conducted by Shaw Strategic Marketing in 2002 (Case No. 2001-128), customers overwhelmingly supported a price hedging strategy. 60% of those surveyed thought that stabilizing gas prices was "Very Appropriate" and 40% chose "Somewhat Appropriate." These customers also stated a willingness to pay an additional 5% of their gas bill, on average, to assure stable prices.

PERSON RESPONSIBLE: Jeff L. Kern