COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

APPLICATION OF DUKE ENERGY KENTUCKY, INC. TO IMPLEMENT A HEDGING PROGRAM TO MITIGATE PRICE VOLATILITY IN THE PROCUREMENT OF NATURAL GAS	)))))	CASE NO. 2015-00025

ORDER

On January 28, 2015, Duke Energy Kentucky, Inc. ("Duke") filed its request for approval to continue its existing gas cost hedging plan for three years, through March 31, 2018. Duke has had a Commission-approved hedging program in place since July 2001. The most recent version of its hedging program was approved through March 31, 2015, in Case No. 2012-00180,[1] with the ability to hedge through October 31, 2017. Duke responded to one Commission Staff Request for Information ("Staff's First Request"). There are no intervenors in this proceeding, and this matter now stands submitted for decision.

BACKGROUND

On September 12, 2000, the Commission issued an order initiating Administrative Case No. 384[2] ("Admin. 384") to investigate increases in wholesale natural gas prices which had recently occurred and the impacts of such increases on

[1] Case No. 2012-00180, *Application of Duke Energy Kentucky, Inc. to Implement a Hedging Program to Mitigate Price Volatility in the Procurement of Natural Gas* (Ky. PSC Aug. 24, 2012).

[2] Administrative Case No. 384, *An Investigation of Increasing Wholesale Natural Gas Prices and the Impact of Such Increases on the Retail Customers Served by Kentucky Jurisdictional Natural Gas Distribution Companies* (Ky. PSC Sept. 6, 2001).

the retail customers served by Kentucky's jurisdictional natural gas local distribution companies ("LDCs"). In that Order, the Commission identified several specific issues it intended to explore, one of which concerned possible strategies the LDCs could use to mitigate higher natural gas prices. The Commission's January 30, 2001 Order in Admin. 384 referenced the LDCs' indication that, although hedging strategies would not necessarily be a means of reducing prices, they could be used as a means of reducing the volatility in prices. The Commission stated in that Order that the use of storage facilities, performance-based ratemaking, hedging strategies, and budget payment plans were the most prominent approaches identified as ways of mitigating the impact of higher prices on retail customers. The Commission found that the LDCs should be encouraged to pursue these options in order to ensure that all reasonable efforts were being made to provide natural gas service in a cost-effective, efficient manner. It also required each LDC to file a detailed report describing, among other things, the results of an investigation of financial hedging practices that the Commission directed each of the LDCs to perform. The Commission's July 17, 2001 Order in Admin. 384 found that LDCs should consider limited hedging programs as one means of attaining the objectives of obtaining low-cost gas supplies, minimizing price volatility, and maintaining reliability of supply.

DISCUSSION

As mentioned previously, Duke has had a Commission-approved hedging program in place since 2001. Duke proposes to continue its hedging activities with no modifications to its currently approved program for three years, through March 31, 2018. During the course of the processing of this case, Duke was asked in Staff's First

Request whether it was aware of the Commission's decisions denying the requests of Columbia Gas of Kentucky, Inc.[3] ("Columbia") and Atmos Energy Corporation[4] ("Atmos") to continue their gas cost hedging programs, and of the letter filed October 16, 2014, by Delta Natural Gas Company, Inc. ("Delta") in Case No. 2012-00025,[5] which informed the Commission of its decision to discontinue its Gas Supply Hedging Plan based on the Commission's decisions in the previously cited cases. Duke informed the Commission that it was not aware of the Commission's decisions with regard to Columbia's and Atmos's hedging programs, or of Delta's decision concerning its own program. In response to a request to provide an evaluation of how its hedging program specifically addresses the concerns and findings set out in the Commission's Orders in Case Nos. 2013-00354 and 2013-00421, Duke stated that its program is not materially different from Columbia's and Atmos's programs, and that it includes nothing that would address the Commission's concerns and findings in those cases.[6] Duke declined to request withdrawal of its application in this proceeding due to its belief that it was required to file an application to continue its program based on the Commission's final Order in Case No. 2012-00180, but declared its willingness to discontinue seeking to extend its program if the Commission did not want the program to be continued.[7]

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[3] Case No. 2013-00354, *Application of Columbia Gas of Kentucky, Inc. to Extend Its Gas Price Hedging Plan* (Ky. PSC Sept. 17, 2014).

[4] Case No. 2013-00421, *Application of Atmos Energy Corporation for Continuation of Its Hedging Program* (Ky. PSC Sept. 18, 2014).

[5] Case No. 2012-00025, *Application of Delta Natural Gas Company, Inc. to Extend Its Natural Gas Supply Hedging Plan to March 31, 2015* (Ky. PSC May 7, 2012).

[6] Response to Staff's First Request, Item 4.a.

[7] *Id*. at Item 3.

Based on the evidence of record and being otherwise sufficiently advised, the Commission finds that Duke's hedging program should not be extended. The Commission's concern with regard to the extension of gas cost hedging programs, as discussed extensively in Case Nos. 2013-00354 and 2013-00421, was that continued low and stable gas prices could obviate the need for hedging. This was the conclusion that we reached in those cases and is the conclusion we now reach in this case. While there is no guarantee that higher levels of gas prices and volatility will not recur, current projections from the United States Energy Information Administration's 2014 Annual Energy Outlook indicate prices are not expected to exceed $8.00 per Mcf through 2040 using the reference case and are not expected to exceed $8.15 per Mcf using the High Growth scenario. More importantly with regard to volatility, the trend in price increases is projected to be gradual and steady in the long run. The Commission finds that current conditions and the outlook for future natural gas supplies and prices are sufficiently different in 2015 from what they were in 2001 to allay our previous concern regarding the potential adverse impact of price volatility on customer bills. We therefore conclude that it is no longer reasonable to impose the cost attendant to hedging, to the extent there is net cost rather than net savings, to be passed along to Duke's customers as part of their gas cost.

While the Commission finds that any future benefit to customers in terms of reduced volatility does not appear to be sizable enough to justify extension of the hedging program, we also find that Duke has made every reasonable effort to comply with the express direction contained in the Commission's Orders in Admin. 384. The Commission commends Duke for those efforts.

IT IS THEREFORE ORDERED that:

1. Duke's request to continue its hedging program is denied, and it shall cease hedging activities as of the date of this Order.

2. Duke shall reflect in its Gas Cost Adjustment applications the net cost and benefits of its previously approved hedging activities associated with its natural gas procurement and supply performed through October 31, 2017.

By the Commission

ENTERED
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KENTUCKY PUBLIC
SERVICE COMMISSION

ATTEST:

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