

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

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| APPLICATION OF DUKE ENERGY KENTUCKY,) | |
| INC. FOR APPROVAL TO ESTABLISH A) | CASE NO. |
| REGULATORY ASSET) | 2016-00159 |

ORDER

On April 29, 2016, Duke Energy Kentucky, Inc. ("Duke Kentucky") filed an application seeking approval to establish a regulatory asset in the amount of \$2,185,381¹ for the costs associated with gas main pressure testing that must be performed in order to maintain Duke Kentucky's natural gas pipeline systems' historic maximum allowed operating pressure ("MAOP") in accordance with federal regulations.

There are no intervenors in this proceeding. Duke Kentucky responded to two rounds of data requests issued by Commission Staff. The matter now stands submitted to the Commission for a decision based upon the evidentiary record.

BACKGROUND

In December 2011, Congress enacted the Pipeline Safety, Regulatory Certainty, and Job Creation Act of 2011 ("Pipeline Safety Act of 2011"), which became effective on January 3, 2012. The federal regulations require more stringent safety and reliability protocols for both the Department of Transportation and Owners/Operators.² Among other things, the Pipeline Safety Act of 2011, and advisory bulletins by the Pipeline and

¹ Duke Kentucky's Response to Commission Staff's First Request for Information, Item 3.a. Duke Kentucky's original request for the amount of the regulatory asset per its application was \$1,920,600.

² Application at 2.

Hazardous Materials Safety Administration (“PHMSA”), clarified expectations of requirements for operators of gas transmission lines to verify accuracy of records of their system which include providing traceable, verifiable, and complete documentation to support MAOP.³

Duke Kentucky states that areas of its natural gas transmission and distribution systems date back to the 1950s. Much of this system was not originally installed by Duke Kentucky, but was acquired through various mergers and acquisitions.⁴ Further, as a result of PHMSA’s clarification of its expectations of compliance under the Pipeline Safety Act of 2011, Duke Kentucky began reviewing its records for compliance with the Pipeline Safety Act of 2011 and consistency with PHMSA’s guidance.⁵ Upon completion of its review of its records, Duke Kentucky determined that it had incomplete and insufficient records available for some of its pipeline systems when evaluated under the newly redefined requirement standards by PHMSA that require immediate corrective action.⁶ As a result, Duke Kentucky must begin performing pressure testing of certain existing transmission pipelines in order to provide traceable, verifiable, and complete documentation to support existing MAOP levels per CFR Title 49 Parts 192-501 and 192-619.⁷ Duke Kentucky states that if it fails to perform the pressure testing, Duke Kentucky will no longer be able to support operating its system at historic MAOP levels.

³ *Id.*

⁴ *Id.*

⁵ *Id.*

⁶ *Id.* at 2 and 3.

⁷ *Id.* at 3.

Instead, it will have to reduce operating pressures, creating the potential that the system will have insufficient pressure during a time of need.⁸

Specifically, Duke Kentucky must conduct pressure testing along certain segments of its transmission pipeline, AM07, consisting of approximately three miles.⁹ The work includes removing the line from service, purging the residual natural gas, separating the section to be tested, filling the line with water, bringing the pressure up to the specified test value, removing the water after the test, and returning the line to service. Duke Kentucky states that the cost of performing this work was neither anticipated nor known and is not currently reflected in its base rates.¹⁰ Further, it states that the expense is a significant and material, unanticipated, one-time expense beyond its control and must be incurred as a result of PHMSA's clarified interpretations to federal regulations.¹¹

In support of its request to establish a regulatory asset for the costs described herein, Duke Kentucky states that a regulatory asset is created when a utility is authorized to capitalize an expenditure that, under traditional accounting rules, would ordinarily be recorded as a current expense.¹² This reclassification of an expense to a capital item allows the utility the opportunity to request future recovery of the amount capitalized in rates. Duke Kentucky asserts that the Commission is endowed with plenary authority to establish regulatory assets and that such authority is rooted in KRS

⁸ *Id.*

⁹ *Id.* at 4.

¹⁰ *Id.*

¹¹ *Id.*

¹² *Id.* at 5.

278.040 and KRS 278.220.¹³ Duke Kentucky also acknowledges that it must obtain Commission approval for accounting adjustments before establishing any expense as a regulatory asset.¹⁴

DISCUSSION

The Commission has previously approved regulatory assets for Duke Kentucky and other jurisdictional utilities. Such approval has been granted when a utility has incurred (a) an extraordinary, nonrecurring expense which could not have reasonably been anticipated or included in the utility's planning; (b) an expense resulting from a statutory or administrative directive; (c) an expense in relation to an industry-sponsored initiative; or (d) an extraordinary or nonrecurring expense that over time will result in a saving that fully offsets the cost.¹⁵ Duke Kentucky believes its request to establish a regulatory asset for the necessary MAOP pipeline pressure tests is consistent with the first and second above-listed categories.¹⁶ Duke Kentucky maintains that the need for the necessary pressure tests only recently came to light through PHMSA's newly issued advisory bulletin that provided new and greater interpretation of its regulations and as Duke Kentucky completed a comprehensive record review and gathering of information on its natural gas delivery system to support and maintain its historic MAOP levels.¹⁷

¹³ *Id.* KRS 278.040 sets forth the Commission's authority to regulate utilities. KRS 278.220 authorizes the Commission to establish a system of accounts to be kept by the jurisdictional utilities.

¹⁴ *Id.*

¹⁵ Case No. 2008-00436, *The Application of East Kentucky Power Cooperative, Inc. for an Order Approving Accounting Practices to Establish a Regulatory Asset Related to Certain Replacement Power Costs Resulting from Generation Forced Outages* (Ky. PSC Dec. 23, 2008), Final Order at 4.

¹⁶ Application at 6.

¹⁷ *Id.*

Further, Duke Kentucky asserts the costs to be incurred to effectuate this necessary pressure test are extraordinary and nonrecurring expenses that it could not have anticipated or included in its planning.¹⁸ Finally, Duke Kentucky states that as the need for the additional pressure tests arose through PHMSA's promulgation of new directives and guidance regarding expectations under its regulations, the aforementioned costs could also qualify as an expense resulting from a statutory or administrative directive.¹⁹

Having reviewed the record and being otherwise sufficiently advised, the Commission finds that Duke Kentucky's request to establish a regulatory asset for the necessary and actual costs for its MAOP pipeline pressure tests, excluding carrying charges, is reasonable and should be authorized. These costs are extraordinary, nonrecurring expenses that could not have been reasonably anticipated. We further find that these costs are necessary to ensure the safety and reliability of Duke Kentucky's natural gas transmission pipelines to support operating its system at historic levels, thereby lowering the risk of losing pressure and dropping service during emergencies and extreme weather conditions.

IT IS THEREFORE ORDERED that:

1. The accounting treatment requested by Duke Kentucky to establish a regulatory asset for the necessary and actual costs for its MAOP pipeline pressure tests is approved.

¹⁸ *Id.*

¹⁹ *Id.* at 6–7.

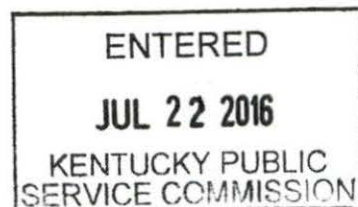
2. The regulatory asset account established in this case is for accounting purposes only. The amount, if any, of the regulatory asset, which includes company labor, authorized herein that is to be amortized and recovered in rates shall be determined in Duke Kentucky's next gas rate case.

3. Duke Kentucky shall, within 14 days of the date of completing the MAOP pressure testing, file with the Commission the results of the MAOP pressure testing.

4. Duke Kentucky shall, within 30 days of completing the MAOP pressure testing, file the accounting entries made on its books to effectuate the creation of the regulatory asset.

5. Any document filed in the future pursuant to ordering paragraphs 3 and 4 herein shall reference this case number and shall be retained in the utility's general correspondence file.

By the Commission



ATTEST:

A handwritten signature in blue ink that reads "Jelina R. Mathews". The signature is written in a cursive style.

Executive Director

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