

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

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In the Matter of:

AN INVESTIGATION OF NATURAL GAS)
RETAIL COMPETITION PROGRAMS) CASE NO. 2010-00146

POST-HEARING BRIEF OF DUKE ENERGY KENTUCKY, INC.

Comes now Duke Energy Kentucky, Inc. (“Duke Kentucky” or “Company”), by and through counsel, and submits its Post-Hearing Brief to the Kentucky Public Service Commission (the “Commission”).

I. INTRODUCTION

This investigation of natural gas retail competition programs was initiated by the Commission in response to Kentucky House Joint Resolution 141, enacted and signed by Governor Steven L. Beshear on August 12, 2010.¹

The Resolution directs the Commission to:

“commence a collaborative study of natural gas retail competition programs to determine if benefits could be derived from these programs, and to determine whether natural gas retail competition programs could be crafted to benefit Kentucky consumers.”²

The Commission’s Order initiating the investigation set forth certain elements essential to the inquiry.³ It made as parties to this proceeding all jurisdictional natural gas distribution utilities having 15,000 or more Kentucky customers. Other interested parties were invited to

¹ Case No. 2010-00146, Commission Order, April 19, 2010.

² Kentucky General Assembly 2010 Regular Session, House Joint Resolution 141, April 12, 2010, at 1.

³ Case No. 2010-00146, Commission Order, April 19, 2010, pp. 4-5.

intervene and several did including natural gas suppliers and marketers, consumer and low-income groups and the Kentucky Attorney General.

The Commission entered a Procedural Order⁴ providing for the filing of both direct and rebuttal testimony, two rounds of discovery and a date for hearing of the issues. The Commission convened that hearing on October 19 and 20, 2010, where testimony was received. At the conclusion of the hearing, the Commission directed that the parties file simultaneous briefs summarizing their positions by November 1, 2010.

II. DUKE KENTUCKY DOES NOT BELIEVE THAT THE GENERAL ASSEMBLY SHOULD IMPLEMENT A MANDATORY STATE-WIDE RETAIL NATURAL GAS CHOICE PROGRAM.

Duke Kentucky's position regarding the implementation of a mandatory state-wide retail natural gas choice program is provided through the testimony of its witness, Mitch Martin.⁵ Mr. Martin has worked for Duke Energy Business Services, LLC (or its affiliates) for approximately 19 years and is currently the Manager of City Gate Operations within the Gas Operations Department of Duke Energy Corporation and its subsidiaries, Duke Energy Kentucky and Duke Energy Ohio. He is responsible for the operation of Duke Energy's gas transportation programs, including Duke Energy Ohio's Gas Customer Choice Program and Duke Energy Kentucky's Interruptible Transportation (IT) and Firm Transportation – Large (FT-L) programs. He has other duties in the administration of these programs as well (Martin direct testimony, pp. 1-2). Mr. Martin's testimony provides two clear reasons why there should not be a mandatory state-wide retail natural gas choice program (Martin direct testimony, pp. 4-6).

⁴ Case No. 2010-00146, Commission Order, June 8, 2010.

⁵ Mr. Martin's pre-filed direct testimony was filed with the Commission on June 21, 2010. In addition, Mr. Martin testified at the hearing on October 19, 2010. His testimony begins on the digital video record at 10/19/10, 2:38:35 p.m.

First, Duke Kentucky is not aware of any empirical study that proves retail competition results in lower prices for customers. Retail choice is about just that, “choice” – the ability of a customer to decide who will supply the natural gas commodity. Currently, Kentucky’s retail natural gas utilities’ actual cost of gas flows through the gas cost adjustment (“GCA”) with no mark-up. As such, Kentucky gas customers are paying for gas at market prices adjusted either monthly or quarterly. Therefore, the only clear benefit of choice is the fact that suppliers can offer pricing alternatives other than the utility’s direct pass-through of actual cost of natural gas (Martin direct testimony, p. 4).

While Duke Kentucky does not dispute that some customers may be willing to pay more for gas in exchange for the right to choose a supplier and to lock in a fixed commodity price for a period of time, that ability alone is an insufficient reason for the Kentucky General Assembly to implement a mandatory state-wide retail natural gas choice program.

Second, because Kentucky’s natural gas utilities are not identical, there needs to be sufficient flexibility in a utility’s ability to design and implement any type of service offering, including retail customer choice programs. A comprehensive and mandatory state-wide program would likely be very rigid and impose greater costs upon Kentucky customers as each utility would have to conform its unique operations to a standard program that may not be operationally feasible. If the utility itself decided that a retail choice program was in the best interests of both the company and its customers, that utility should be able to present such a plan to the Commission for its review, approval and oversight (Martin direct testimony, p. 5).

Duke Kentucky believes that each utility should have the ability to choose whether to design and implement a customer choice program for retail natural gas service because the natural gas utilities in Kentucky are unique unto themselves and vary greatly from each other.

For instance, the Delta Gas system is much different than the Louisville Gas and Electric system in terms of number of customers, customer classifications, geography of service territory and cost of service. A “one size fits all” approach to retail natural gas service in Kentucky would be very cumbersome. What might work in the Columbia service territory might not work at all in the Delta Gas or Duke Kentucky service territories. A rigid program applicable to all natural gas utilities in Kentucky would likely increase costs to end-use consumers (Martin direct testimony, p. 5). This result is antithetical to the stated desire of the Kentucky General Assembly to insure that Kentucky natural gas customers receive reliable natural gas services at fair, just and reasonable rates.⁶

Duke Kentucky believes that, in the event the Kentucky General Assembly were to enact some form of retail natural gas choice in Kentucky, certain criteria should be addressed in minimum standards or guidelines for retail choice program development. Those criteria are: (Martin direct testimony, pp. 7-8).

- A description of the Commission’s role in the competitive marketplace;
- A general policy regarding the obligation to serve customers of both the competitive retail gas provider and the utility;
- A designation of the utility as the supplier of last resort in the event of supplier default;
- Alternative commodity procurement or pricing options;
- A policy of non-discriminatory access for customers to retail gas services;
- A code of conduct for marketers of retail gas services including utility affiliates with protections for customer information and data;

⁶ House Joint Resolution 141, April 12, 2010, preamble.

- Billing guidelines which include options for utility consolidated billing and dual billing for customers and the option for utility purchase of receivables at a reasonable discount rate based upon the utility's carrying costs and collection experience;
- Payment priority for the utility such that regulated charges are allocated from the first dollars paid by a customer;
- Certification process for competitive suppliers at the Commission and a registration process that includes bonding or parental guarantees with the utility;
- Recovery of a utility's transition costs from customers;
- Recovery of a utility's stranded costs;
- Recovery of a utility's uncollectibles including purchased receivables;
- Authority for only the utility to disconnect for non-payment of a competitive supplier's portion of the bill;
- Necessary steps to maintain system integrity; and,
- Access to pipeline storage capacity.

Besides these minimum standards, Duke Kentucky believes that the Commission should maintain all of its current authority over utilities and maintain its role in consumer protection (Martin direct testimony, p. 8). The company believes that the Commission should continue to exercise its authority to approve a fair, just and reasonable retail natural gas choice program, just as it has done with Columbia Gas of Kentucky's Customer Choice pilot. The Commission should maintain this authority with sufficient flexibility to review and approve programs proposed by natural gas utilities that are customized to fit the unique characteristics of that utility's operations and customer base (Martin direct testimony, p. 9). The Commission should

likewise have regulatory oversight over any competitive supplier wishing to participate in a utility's program to insure that there are adequate protections for Kentucky's consumer base, the regulated utilities, and competing suppliers. The Commission must be able to certify all competitive suppliers wishing to operate in Kentucky based upon a finding of financial, technical and managerial expertise. Those suppliers should be required to renew their certificates with the Commission every two years and to maintain official corporate information on file with the Commission. The competitive suppliers must also be subject to the consumer complaint process, provide annual reports to the Commission and pay a fair portion of the Commission's annual assessments (Martin direct testimony, p. 9).

The Commission should also have the authority to assess penalties against the competitive supplier if that supplier fails to: (1) abide by the contractual terms with the customer or the utility; or (2) follow any rules established by the Commission, whether for safety, billing, reporting or general practices. The potential penalty should include the authority to revoke, suspend, modify, limit or condition the certification and should include the authority to assess a monetary penalty payable to the general fund as with penalties assessed against regulated utilities (Martin direct testimony, p. 9).

In the current regulatory environment, utilities such as Duke Kentucky have an obligation to serve customers located within boundaries of their defined service territories. In a competitive market, where customers may choose who is supplying the commodity, customers will still rely upon the utility to provide safe and reliable natural gas delivery. And, those customers should not bear the risk of losing their commodity source should their chosen supplier leave the market for any reason. Therefore, the regulated natural gas utility must act as the Supplier of Last Resort (or, Provider of Last Resort) to assure that there is an adequate and reliable source of

natural gas supply (Martin direct testimony, p. 10). Supplier of last resort service will impose costs upon a utility providing the service and the Commission should continue to grant the utility cost recovery for all reasonably incurred supplier of last resort costs with a reasonable return where applicable, including but not limited to, maintaining gas supply and capacity, necessary overhead, and any hedging or storage costs (Martin direct testimony, p. 10). Even the testimony of the gas supplier witnesses acknowledged this to be the case (see, for example, cross-examination of Stand Energy witness, John Dosker, 10/20/10, 1:56:20 p.m.).

Duke Kentucky also believes that, in the event a retail natural gas choice program were to be mandated in Kentucky, there should be a code of conduct applicable to all suppliers who wished to participate in any utility-proposed program. Such a code of conduct would serve as a consumer protection device from deceptive marketing or unfair business practices of any retail supplier (Martin direct testimony, p. 12).⁷

Another issue which should be addressed in the event that a retail natural gas choice program is mandated in Kentucky is “rate-ready” utility consolidated billing and dual billing. “Rate-ready” utility consolidated billing allows the gas supplier to provide monthly rates according to pricing arrangements agreed upon between the supplier and customer, and to which the utility attaches rate codes for billing purposes. The customer receives one bill from the utility that indicates the name of the supplier and contains both the regulated utility and competitive supplier charges. Naturally, the supplier should pay a reasonable fee to the utility for this billing service. With dual billing, the customer will receive two bills. The utility will bill and collect for the regulated utility charges and the supplier is responsible for billing and collecting the competitive gas supply charges, including any past due amounts related to the

⁷ Mr. Martin provides an in-depth description of the types of rules which should be addressed in a competitive retail natural gas service supplier code of conduct (Martin direct testimony, pp. 13-15).

competitive charges. The supplier should be required to pay the utility for any billing system changes required to support any other billing options requested by the supplier (Martin direct testimony, p. 15).

Duke Kentucky believes that there should be a clear payment priority between regulated and competitive charges on customer bills, especially if a utility is providing customers with a consolidated bill. The regulated charges should always receive priority over a competitive charge, including in the case of arrearages. If a customer makes a partial payment, the payment should be applied first to utility charges and arrears, then to utility current charges, then to supplier charges and arrears, and then to supplier current charges (Martin direct testimony, pp. 15-16).

A utility should also have the flexibility to include the purchase of supplier receivables in any choice program if it chooses to do so. Utilities should be able to purchase the receivables at some reasonable discount rate based upon the utility's carrying costs and collection experience (Martin direct testimony, p. 16).

The Commission should also have a standard process for certification of competitive gas suppliers to operate in Kentucky. The application forms provided by the Commission should provide for sufficient information to enable the Commission to assess: (1) the supplier's managerial, financial and technical capability to provide the service it intends to offer; (2) its ability to provide reasonable financial assurances sufficient to protect regulated sales service customers and natural gas companies from default, and; (3) its ability to comply with Commission rules or orders (Martin direct testimony, pp. 16-17). At the very least, this information should include:

1. ownership and organizational descriptions;

2. managerial experience and capabilities and prior regulatory or judicial actions;
3. balance sheets, credit ratings, and other relevant financial information;
4. technical ability and experience in nominating, scheduling and providing natural gas to retail customers;
5. proof of a Kentucky office and an employee in this state; and,
6. statements as to whether the applicant has ever been terminated from any choice program, or if applicant's certification has ever been revoked, or suspended, or if applicant has ever been in default for failure to deliver. (Martin direct testimony, pp. 16-17).

Finally, there should also be a registration process that is uniform for all suppliers. The supplier should be required to provide financial information to the utility so that the utility may assess the best method to cover its financial exposure to the supplier's operations. The utility should be allowed to require the supplier to provide a parental guarantee, letter of credit, cash deposit, or other evidence of financial security in the event of abandonment (Martin direct testimony, p. 17). The method of calculating the utility's financial exposure to the supplier should be included as part of the utility's plan and approved by the Commission so that there is a clear and transparent process that is fairly administered (Martin direct testimony, pp. 17-18).

III. THE OVERWHELMING EVIDENCE SUGGESTS THAT NEITHER RESIDENTIAL NOR COMMERCIAL RATEPAYERS WOULD BENEFIT FROM THE IMPLEMENTATION OF A MANDATORY STATE-WIDE RETAIL NATURAL GAS CHOICE PROGRAM IN KENTUCKY.

No convincing testimony was received in this investigation that Kentucky natural gas customers would save money if a state-wide retail natural gas choice program was mandated. Indeed, just the opposite seems to be the case. The participants in Columbia Gas of Kentucky's

Customer Choice Program have paid approximately \$17 million more for the natural gas commodity from gas suppliers than if they had purchased the commodity from Columbia Gas (Columbia Gas Response to First Data Requests of AARP, No. 1(b), p. 2). Moreover, the Columbia Gas Customer Choice pilot program has continued much longer than the typical pilot. The Columbia choice program has been in place for approximately 10 years. This is more than a sufficient amount of time for the natural gas market to endure several market cycles. It is logical to believe that the Columbia Gas Customer Choice pilot program can be relied upon as a likely indicator of the results which Kentucky natural gas ratepayers would see if a retail choice program was mandated for Kentucky. The benefit of being able to rely upon the Columbia Gas Choice Program experience is a significant advantage both to the Commission and the General Assembly in deciding whether it is to Kentucky's advantage to initiate a mandatory choice program.

The principal proponent for gas choice in Kentucky is Stand Energy. Stand provided the testimony of three witnesses, John Dosker, Mark Ward and Don Mason. An exhaustive recitation of their testimony is unnecessary. Rather, it is sufficient to remind the Commission that Stand's witnesses made many more claims than they could back up regarding the savings realized by retail gas customers in customer choice programs. Indeed, with regard to Duke Kentucky, Stand's witness, Mark Ward, attempted to convince the Commission that a Kentucky transportation customer would pay several thousand more dollars annually than a like customer in Ohio (Ward direct testimony, pp. 7-8). However, under cross-examination, Mr. Ward admitted that he failed to include several riders in place in Ohio that were not accounted for in his calculations and when they were added the difference between the Kentucky and Ohio customers was much less than stated in his testimony (Ward cross-examination, 10/20/10,

3:15:49 p.m.). It was also very puzzling that Mr. Ward did not seem to understand or even know the difference between the regulatory regimes in place in Ohio and Kentucky even though he is the Vice-President of Regulatory Affairs for Stand Energy and has both states under his responsibility.

IV. CONCLUSION

The record in this case is devoid of any credible evidence to support the proposition that it would be in the best interests of Kentucky ratepayers for a retail natural gas customer choice program to be instituted by the Kentucky General Assembly. In fact, the best and most reliable data in this case, the experience of the Columbia Gas Customer Choice Program, clearly indicates that retail customer choice in Kentucky has failed. This failure has occurred even though the Columbia Gas Choice Program has been given every opportunity to succeed and has been subject to regulatory scrutiny by this Commission. There is nothing in the record of this case that points to a different result if the Kentucky General Assembly were to enact a state-wide retail customer choice program now.

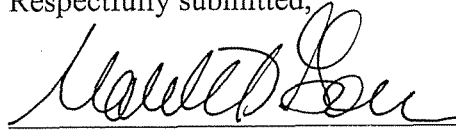
The only benefit of any significance to retail customers from the imposition of a mandatory choice program is the choice itself. Considering all of the added costs to the regulated utilities of having to administer a customer choice program, it is very clear that any benefit to retail customers of having the choice of his commodity provider is far outweighed by these additional costs.

Duke Kentucky respectfully requests that the Commission's report to the General Assembly make the determination that mandatory retail natural gas customer choice in Kentucky should not be enacted. However, in the event that the Commission makes a different determination, Duke Kentucky requests that the Commission recommend that each individual

utility should make its own decision regarding whether retail choice makes sense for it and its customers; and, if so, that it be given the authority and discretion, subject to Commission oversight, to fashion a utility-specific customer choice program after due consideration is given to the unique characteristics of its business, service territory and customer base.

This 1st day of November, 2010.

Respectfully submitted,



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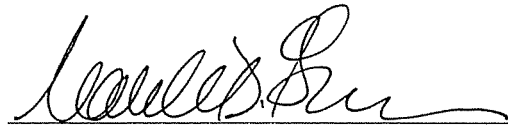
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