

**COMMONWEALTH OF KENTUCKY**  
**BEFORE THE PUBLIC SERVICE COMMISSION**

**In the Matter of:**

|   |   |                   |
|---|---|-------------------|
| <b>AN EXAMINATION OF THE APPLICATION OF</b> | ) |                   |
| <b>THE FUEL ADJUSTMENT CLAUSE OF</b>        | ) |                   |
| <b>KENTUCKY UTILITIES COMPANY FROM</b>      | ) | <b>CASE NO.</b>   |
| <b>NOVEMBER 1, 2012 THROUGH OCTOBER 31,</b> | ) | <b>2014-00452</b> |
| <b>2014</b>                                 | ) |                   |

|  |   |                   |
|--|---|-------------------|
| <b>AN EXAMINATION OF THE APPLICATION OF</b>    | ) |                   |
| <b>THE FUEL ADJUSTMENT CLAUSE OF</b>           | ) |                   |
| <b>KENTUCKY UTILITIES COMPANY FROM</b>         | ) | <b>CASE NO.</b>   |
| <b>NOVEMBER 1, 2013 THROUGH APRIL 30, 2014</b> | ) | <b>2014-00227</b> |

**DIRECT TESTIMONY OF**  
**MIKE DOTSON**  
**MANAGER, LG&E AND KU FUELS**  
**LG&E AND KU SERVICES COMPANY**

**Filed: February 20, 2015**

1 **Q. Please state your name, position and business address.**

2 A. My name is Mike Dotson. I am the Manager of LG&E/KU Fuels for LG&E and KU  
3 Services Company, which provides services to LG&E and KU Energy, LLC. My  
4 business address is 220 West Main Street, Louisville, Kentucky 40202. A statement  
5 of my education and work experience is attached to this testimony as Appendix A.

6 **Q. What is the purpose of your testimony?**

7 A. I am submitting this testimony in response to the Order entered in this proceeding by  
8 the Commission on February 5, 2015 (“Order”), directing KU to file written direct  
9 testimony on a number of issues relating to fuel procurement during the two-year period  
10 ended October 31, 2014 (“Review Period”).

11 **Q. Please comment generally on the reasonableness of KU’s fuel procurement  
12 practices during the Review Period.**

13 A. KU’s coal procurement practices are sufficiently flexible to allow the Company to  
14 respond effectively to changes in market conditions. Although KU typically issues  
15 formal, sealed-bid solicitations to meet its coal consumption and inventory needs, under  
16 its written fuel procurement policy, it may solicit offers through more informal means,  
17 or may respond to unsolicited offers to the extent prices and terms and conditions of  
18 such offers are competitive with existing market conditions. These practices, by which  
19 KU is able to make optimal use of the market, are memorialized in KU’s written fuel  
20 procurement policies and procedures. As noted in response to the Commission’s Order,  
21 Item No. 31, the fuel procurement policies and procedures were last changed effective  
22 January 1, 2011 and were provided to the Commission in response to Question No. 15  
23 in Case No. 2011-00247.

1                   During the 2-Year Review Period, KU conducted five (5) written coal supply  
2                   solicitations and two (2) oral coal supply solicitations in the competitive marketplace.  
3                   A description of each solicitation and associated bid tabulation sheet for the six-month  
4                   period ended October 31, 2012, is contained in the response to the Commission’s  
5                   Order, Item No. 25(a) and (b) and Commission’s Order, Item No. 26 (a) and (b). In  
6                   addition, each vendor from whom KU purchased coal during the six-month period  
7                   ended October 31, 2012, and the quantities and nature of each purchase (including  
8                   whether such purchase was a spot or contract purchase), are identified in response to  
9                   the commission’s Order, Item No. 27.

10 **Q. Did KU comply with these fuel procurement policies during the Review Period?**

11 A. Yes.

12 **Q. Please describe the coal suppliers’ adherence to contract delivery schedules**  
13 **during the Review Period.**

14 A. With the slowdown in the U. S and global economy it has been a difficult year for the  
15 coal market: weak demand, highly competitive natural gas prices and record consumer  
16 stockpiles resulting from mild weather have forced many producers to cut supply. With  
17 the slowdown in the market and export demand, coal suppliers have been pushing for  
18 delivery under their current contracts.

19 **Q. Do you wish to comment on any other changes that occurred during the Review**  
20 **Period?**

21 A. Yes. As noted in prior two (2) year review, since the enactment by Congress of new  
22 mining and safety legislation and the resulting U. S. Department of Labor, Mine Safety  
23 and Health Administration (“MSHA”) amendment of existing underground mine safety

1 and health regulations (“MINER Act”), there has been a continuing shift in the  
2 regulatory and enforcement environment affecting mine output. There have been a  
3 number of new mine safety rules and regulations and an increase in enforcement  
4 activity and policies. These have resulted in additional costs to mine and supply coal,  
5 loss in mine output, delays in obtaining approvals of mining plans and delays in  
6 permitting. As noted in our response to the Commission’s Order, Item No. 22, a  
7 number of KU Contract suppliers are seeking to recover their cost increases under the  
8 New Impositions Section in KU’s contracts.

9 In addition, the mining industry is having difficulty with and experiencing  
10 delays in obtaining the necessary environmental permits for their mining operations.  
11 This is resulting in mines having to cut production or stop mining in areas altogether  
12 while they wait on permits.

13 **Q. What were KU’s efforts to ensure the coal suppliers’ adherence to contract**  
14 **delivery schedules during the Review Period?**

15 A. A list of all of KU’s long-term fuel contracts is contained in the response to the  
16 Commission’s Order, Item No. 15 (a) – (k).

17 KU regularly communicates with its vendors to identify any potential problems  
18 in meeting agreed-upon delivery schedules. KU works with its suppliers on an ongoing  
19 basis to accommodate genuine production/delivery problems and reach mutually  
20 agreeable resolutions. This includes mine visits by KU representatives, working with  
21 suppliers on allowing deliveries from alternate sources or moving from rail to barge  
22 loading to truck to barge loading.

1           KU continues to work with its suppliers on deliveries and make-up of force  
2 majeure events. This has proven to be an effective strategy over time that results in  
3 reasonably priced coal being delivered to our generation stations. In one case, however,  
4 KU is in litigation with Smoky Mountain Coal/Resources Sales as related to non-  
5 deliveries of coal during 2008 and 2009, as noted in the response to the Commission  
6 Order, Item No. 24.

7 **Q. Please describe KU's efforts to maintain the adequacy of its coal supplies in light**  
8 **of any coal supplier's inability or unwillingness to make contract coal deliveries.**

9 A. KU works with its suppliers on an ongoing basis to ensure deliveries of contracted  
10 amounts of coal. KU worked with its suppliers on allowing deliveries from alternate  
11 sources, and switching modes of transportation when available. KU works to diversify  
12 its source of supply obtaining high sulfur coal from Western Kentucky, Indiana,  
13 Illinois, Ohio and West Virginia.

14           As previously noted with the slowdown in the U. S. and global economy we  
15 have seen a number of producers cutting back production and closing mines. The  
16 Central Appalachian Region experienced the majority of the mine closures. The region  
17 is experiencing thinning coal seams and costly permitting delays which result in rising  
18 production cost. As a result, the Central Appalachian region is losing more production  
19 and market share as buyers switch to lower cost Illinois Basin coal, especially with less  
20 reliance on lower-sulfur coal over time.

21           The Illinois Basin coal demand will continue to grow over the next several  
22 years. Its relatively inexpensive and abundant reserves, favorable location and the

1 continued construction of scrubbers in the East will increase the demand for this kind  
2 of coal.

3 The majority of the coal KU uses is supplied from the Illinois Basin. KU has  
4 seen an increase in supply from the region, new mines opening in the region.

5 These efforts, coupled with ongoing procurement pursuant to the Company's  
6 policies, produced adequate coal supplies through the end of the Review Period.

7 **Q. Were there any changes in coal market conditions that occurred during the**  
8 **Review Period, or that KU expects to occur within the next 2 years that have**  
9 **significantly affected or will significantly affect the Company's coal procurement**  
10 **practices?**

11 A. No. Although the coal market continually changes, there were no material changes in  
12 market conditions that significantly affected, or that KU believes could significantly  
13 affect in the future, the Company's fuel procurement practices.

14 As previously stated with the slowdown in the U. S. and global economy, we  
15 saw inventory stockpiles increase and many producers cut supply. The following  
16 quotes in the U.S. Energy Information Administration's ("EIA") *Short -Term Energy*  
17 *Outlook*, released January 8, 2013 confirm this observation:

18 U. S. Coal Consumption "EIA estimates coal consumption in the electric power sector  
19 totaled 829 million short tons in 2012, the lowest amount since 1992. Lower natural  
20 gas prices paid by electric generators led to a significant increase in the share of natural  
21 gas-fired generation. Higher natural gas prices, coupled with slightly higher electricity  
22 demand, will lead to an increase in coal-fired generation over the forecast period."

1 U. S. Coal supply “EIA estimates coal production declined by 6.3% in 2012 along with  
2 a drop in domestic consumption. Coal production is expected to decline by a further  
3 3.6% in 2013 as primary and secondary inventory draws combined with a small  
4 increase in coal imports meet a small consumption increase in 2013. Although EIA  
5 forecasts that coal consumption will remain flat and that inventories will stabilize in  
6 2014, production is forecast to grow by 3% as coal exports rise. ”

7 U. S. Coal Trade “EIA estimates coal exports totaled a record 124 million short tons  
8 in 2012. Continuing economic weakness in Europe and lower international coal prices  
9 are expected to contribute to lower coal exports in 2013.”

10 U. S. Coal Prices “Delivered coal prices to the electric power industry increased  
11 steadily over the 10 year period ending 2011, when the delivered coal price averaged  
12 \$2.39 per MMBtu (a 6% increase from 2010). EIA expects that changing market  
13 conditions, including weaker domestic demand for coal and higher coal inventories,  
14 will slow increases in coal prices and contribute to the shut-in of higher cost production.

15

16 Although these changes can affect KU’s bargaining power with suppliers, they  
17 did not alter, nor are they expected to alter, the Company’s coal procurement practices.  
18 KU’s fuel procurement practices allow the Company to respond effectively to changes  
19 in market conditions.

20 **Q. Were KU’s costs of fuel for the Review Period reasonable?**

21 A. Yes. KU’s costs for comparable coals have remained at, about the average and  
22 comparable to other similarly situated utilities as identified in response to the  
23 Commission’s Order, Item No. 18. KU continues to follow the same sound coal

1 procurement practices previously reviewed by the Commission. Given the information  
2 available, in my opinion, the Company's fuel costs during the Review Period were  
3 reasonable.

4 **Q. Were KU's fuel purchases and practices during the Review Period reasonable?**

5 A. Yes. In my opinion, KU's fuel purchases and practices were reasonable during the  
6 Review Period.

7 **Q. Does this conclude your testimony?**

8 A. Yes.



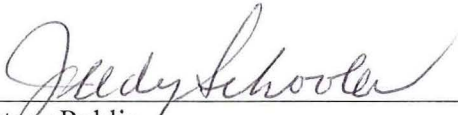
VERIFICATION

COMMONWEALTH OF KENTUCKY )  
 ) SS:  
COUNTY OF JEFFERSON )

The undersigned, **Mike Dotson**, being duly sworn, deposes and says that he is the Manager, LG&E / KU Fuels, LG&E and KU Services Company, that he has personal knowledge of the matters set forth in the foregoing testimony and that the answers contained therein are true and correct to the best of his information, knowledge and belief.

  
\_\_\_\_\_  
**MIKE DOTSON**

Subscribed and sworn to before me, a Notary Public in and before said County and State, this 20<sup>th</sup> day of February 2015.

  
\_\_\_\_\_  
Notary Public

My Commission Expires:  
**JUDY SCHOOLER**  
**Notary Public, State at Large, KY**  
**My commission expires July 11, 2018**  
**Notary ID # 512743**

## Appendix A

### Mike Dotson

Manager, LG&E/KU Fuels  
LG&E and KU Services Company  
220 West Main Street  
Louisville, Kentucky 40202  
(502) 627-2322

#### Education

|  |      |
|--|------|
| Master of Business Administration<br>Xavier University, Cincinnati, Ohio           | 1984 |
| Bachelor of Business Administration<br>University of Kentucky, Lexington, Kentucky | 1973 |

#### Experience

|  |                         |
|--|-------------------------|
| LG&E and KU Services Company<br>July 1998 - Present                            | Manager, LG&E/KU Fuels  |
| Big Rivers Electric Company<br>Vice President of Fuels & Environmental Affairs | Jan 1996 – July 1998    |
| Vice President of Fuels  | Jan 1994 – Dec 1995     |
| Manager of Fuels   | May 1993 – Dec 1993     |
| Kentucky Utilities Company<br>Manager of Fuel Procurement                      | Sep 1991 – May 1993     |
| Fuel Contract Administrator  | July 1986 – Sept. 1991  |
| Diamond Shamrock Coal Company  | Feb. 1984 – July 1986   |
| Island Creek Coal Company  | March 1980 – Feb. 1984  |
| Kentucky American Water Company  | Sept. 1978–March 1980   |
| GTE Sylvania   | Sept. 1976 – Sept. 1978 |
| K-Mart Corp.   | Jan. 1975 – Sept. 1976  |