

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

AN EXAMINATION OF THE APPLICATION OF)
THE FUEL ADJUSTMENT CLAUSE OF)
LOUISVILLE GAS AND ELECTRIC COMPANY) CASE NO.
FROM NOVEMBER 1, 2012 THROUGH OCTOBER 31,) 2014-00453
2014)

AN EXAMINATION OF THE APPLICATION OF)
THE FUEL ADJUSTMENT CLAUSE OF)
LOUISVILLE GAS AND ELECTRIC COMPANY) CASE NO.
FROM NOVEMBER 1, 2013 THROUGH APRIL30,) 2014-00228
2014)

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 LG&E 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 LG&E’s fuel procurement
12 practices during the Review Period.**

13 A. LG&E’s coal procurement practices are sufficiently flexible to allow the Company to
14 respond effectively to changes in market conditions. Although LG&E 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 LG&E is able to make optimal use of the market, are memorialized in LG&E’s written
20 fuel procurement policies and procedures. As noted in response to the Commission’s
21 Order, Item No. 31, the fuel procurement policies and procedures were last changed
22 effective January 1, 2011 and were provided to the Commission in response to Question
23 No. 12 in Case No. 2011-00248 During the 2-Year Review Period, LG&E

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

8 **Q. Did LG&E comply with these fuel procurement policies during the Review**
9 **Period?**

10 A. Yes.

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

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

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

20 A. Yes. As noted in prior two (2) year review, since the enactment by Congress of new
21 mining and safety legislation and the resulting U. S. Department of Labor, Mine Safety
22 and Health Administration ("MSHA") amendment of existing underground mine safety
23 and health regulations ("MINER Act"), there has been a continuing shift in the

1 regulatory and enforcement environment affecting mine output. There have been a
2 number of new mine safety rules and regulations and an increase in enforcement
3 activity and policies. These have resulted in additional costs to mine and supply coal,
4 loss in mine output, delays in obtaining approvals of mining plans and delays in
5 permitting. As noted in our response to the Commission's Order, Item No. 22, a
6 number of LG&E Contract suppliers are seeking to recover their cost increases under
7 the New Impositions Section in LG&E's contracts.

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

12 **Q. What were LG&E's efforts to ensure the coal suppliers' adherence to contract**
13 **delivery schedules during the Review Period?**

14 A. A list of all of LG&E's long-term fuel contracts is contained in the response to the
15 Commission's Order, Item No. 15 (a) – (k).

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

22 LG&E continues to work with its suppliers on deliveries and make-up of force
23 majeure events. This has proven to be an effective strategy over time that results in

1 reasonably priced coal being delivered to our generation stations. In one case, however,
2 LG&E is in litigation with Smoky Mountain Coal/Resources Sales as related to the
3 non-delivery of coal during 2008 and 2009 as noted in the response to the Commission
4 Order, Item No. 24.

5 **Q. Please describe LG&E's efforts to maintain the adequacy of its coal supplies in**
6 **light of any coal supplier's inability or unwillingness to make contract coal**
7 **deliveries.**

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

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

20 The Illinois Basin coal demand will continue to grow over the next several
21 years. Its relatively inexpensive and abundant reserves, favorable location and the
22 continued construction of scrubbers in the East will increase the demand for this kind
23 of coal.

1 The majority of the coal LG&E uses is supplied from the Illinois Basin. LG&E
2 has seen increase in supply from the region, new mines opening in the region.

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

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

9 A. No. Although the coal market continually changes, there were no material changes in
10 market conditions that significantly affected, or that LG&E believes could significantly
11 affect in the future, the Company's fuel procurement practices.

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

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

21 U. S. Coal supply "EIA estimates coal production declined by 6.3% in 2012 along with
22 a drop in domestic consumption. Coal production is expected to decline by a further
23 3.6% in 2013 as primary and secondary inventory draws combined with a small

1 increase in coal imports meet a small consumption increase in 2013. Although EIA
2 forecasts that coal consumption will remain flat and that inventories will stabilize in
3 2014, production is forecast to grow by 3% as coal exports rise. ”

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

7 U. S. Coal Prices “Delivered coal prices to the electric power industry increased
8 steadily over the 10 year period ending 2011, when the delivered coal price averaged
9 \$2.39 per MMBtu (a 6% increase from 2010). EIA expects that changing market
10 conditions, including weaker domestic demand for coal and higher coal inventories,
11 will slow increases in coal prices and contribute to the shut-in of higher cost production.

12 Although these changes can affect LG&E’s bargaining power with suppliers,
13 they did not alter, nor are they expected to alter, the Company’s coal procurement
14 practices. LG&E’s fuel procurement practices allow the Company to respond
15 effectively to changes in market conditions.

16 **Q. Were LG&E’s costs of fuel for the Review Period reasonable?**

17 A. Yes. LG&E’s costs for comparable coals have remained at, about the average and
18 comparable to other similarly situated utilities as identified in response to the
19 Commission’s Order No. 18. LG&E continues to follow the same sound coal
20 procurement practices previously reviewed by the Commission. Given the information
21 available, in my opinion, the Company’s fuel costs during the Review Period were
22 reasonable.

23 **Q. Were LG&E’s fuel purchases and practices during the Review Period reasonable?**

1 A. Yes. In my opinion, LG&E's fuel purchases and practices were reasonable during the
2 Review Period.

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

4 A. Yes.

VERIFICATION

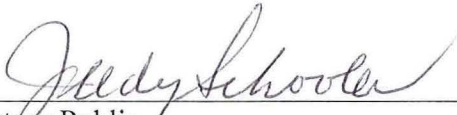
COMMONWEALTH OF KENTUCKY)
) SS:
COUNTY OF JEFFERSON)

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 20th 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 Xavier University, Cincinnati, Ohio	1984
Bachelor of Business Administration University of Kentucky, Lexington, Kentucky	1973

Experience

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