COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

In The Matter of:

The Electronic Application of Duke Energy Kentucky, Inc., for: 1) An Adjustment of the Natural Gas Rates; 2) Approval of a Decoupling Mechanism; 3) Approval of New Tariffs; and 4) All Other Required Approvals, Waivers, and Relief.	)))))))	Case No. 2018-00261

PETITION OF DUKE ENERGY KENTUCKY, INC.
FOR CONFIDENTIAL TREATMENT OF INFORMATION
CONTAINED IN ITS REBUTTAL TESTIMONY

Comes now Duke Energy Kentucky, Inc. (Duke Energy Kentucky or Company), by counsel, pursuant to 807 KAR 5:001, Section 13, and respectfully requests the Commission to classify and protect certain information provided by the Company in its Application for an adjustment of its natural gas rates, respectfully stating as follows:

1. The information for which Duke Energy Kentucky seeks confidential treatment is contained in the Confidential Attachment to the Rebuttal Testimony of Gary J. Hebbeler (GJH-Rebuttal-1). This document is referred to herein as the "Confidential Information" and, broadly speaking, includes a critical system map.

2. Duke Energy Kentucky requests confidential treatment for the transmission system map included in the Confidential Information. This information shows the location of Critical Energy Infrastructure Information (CEII) and the interconnected nature of the system, which has been granted confidential treatment in the past. Duke Energy Kentucky takes all reasonable steps in order to protect CEII, including, but not limited to, only sharing

such information internally on a need-to-know basis. This information need to be kept confidential in order to continue to provide delivery of safe and reliable service to Duke Energy Kentucky customers. Furthermore, the release of this information would provide a security risk for the Company and its customers.

3. The Kentucky Open Records Act exempts from disclosure information that, due to its confidential and proprietary nature, would would have a reasonable likelihood of threatening the public safety by exposing a vulnerability in preventing, protecting against, mitigating, or responding to a terrorist act and limited to: "[i]nfrastructure records that expose a vulnerability referred to in this subparagraph through the disclosure of the location, configuration, or security of critical systems, including public utility critical systems. These critical systems shall include but not be limited to information technology, communication, electrical, fire suppression, ventilation, water, wastewater, sewage, and gas systems.[1]

4. The information for which Duke Energy Kentucky is seeking confidential treatment consists of locations of natural gas delivery systems that constitutes critical utility infrastructure and was either developed internally, or acquired on a proprietary basis, by Duke Energy Corporation and Duke Energy Kentucky personnel, is not on file publicly with any public agency, and is not publicly available from any commercial or other source. The aforementioned information is distributed within Duke Energy Kentucky only to those employees who must have access for business reasons, and is generally recognized as confidential and proprietary in the utility industry.

5. Duke Energy Kentucky does not object to limited disclosure of the Confidential Information described herein, pursuant to an acceptable protective agreement

[1] KRS 61.878 (1)(m)(1)(f).

entered into with any intervenors with a legitimate interest in reviewing the same for the sole purpose of participating in this case.

6. In accordance with the provisions of 807 KAR 5:001, Section 13(2)(e), the Company is filing one copy of the Confidential Information separately under seal, and one appropriate number of copies with the Confidential Information redacted.

7. Duke Energy Kentucky respectfully requests that the Confidential Information be withheld from public disclosure indefinitely. This will assure that the Confidential Information will not become available to the general public.

8. To the extent the Confidential Information becomes generally available to the public, whether through filings required by other agencies or otherwise, Duke Energy Kentucky will notify the Commission and have its confidential status removed, pursuant to 807 KAR 5:001 Section 13(10)(a).

WHEREFORE, Duke Energy Kentucky, Inc., respectfully requests that the Commission classify and protect as confidential the specific information described herein.

Respectfully submitted,

Duke Energy Kentucky, Inc.,

Rocco O. D'Ascenzo (92796)
Deputy General Counsel
Duke Energy Business Services LLC
139 East Fourth Street, 1303-Main
Cincinnati, Ohio 45201
(513) 287-4320
rocco.d'ascenzo@duke-energy.com

And

David S. Samford
L. Allyson Honaker
GOSS SAMFORD, PLLC
2365 Harrodsburg Road, Suite B-325
Lexington, KY 40504
(859) 368-7740
david@gosssamfordlaw.com
allyson@gosssamfordlaw.com

Counsel for Duke Energy Kentucky, Inc.

CERTIFICATE OF SERVICE

This is to certify that the foregoing electronic filing is a true and accurate copy of the document being filed in paper medium; that the electronic filing was transmitted to the Commission on January 22, 2019; that there are currently no parties that the Commission has excused from participation by electronic means in this proceeding; and that a copy of the filing in paper medium will be delivered to the Commission within two business days and a copy of the filing is also being emailed to the following:

Hon. Rebecca W. Goodman
Hon. Larry Cook
Hon. Kent Chandler

Rocco O. D'Ascenzo

COMMONWEALTH OF KENTUCKY

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REBUTTAL TESTIMONY OF

NICHOLAS GIAIMO

ON BEHALF OF

DUKE ENERGY KENTUCKY, INC.

January 22, 2019

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I. INTRODUCTION AND PURPOSE

Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

A. My name is Nicholas Giaimo, and my business address is 4720 Piedmont Row Drive, Charlotte, North Carolina 28210.

Q. BY WHOM ARE YOU EMPLOYED AND IN WHAT CAPACITY?

A. I am employed by Duke Energy Business Services LLC (DEBS) as Director, Regulated Utility Gas Operations Finance on behalf of Duke Energy Kentucky, Inc. (Duke Energy Kentucky or the Company). DEBS provides various administrative and other services to Duke Energy Kentucky and other affiliated companies of Duke Energy Corporation (Duke Energy).

Q. PLEASE BRIEFLY SUMMARIZE YOUR EDUCATION AND PROFESSIONAL EXPERIENCE.

A. I graduated from Wake Forest University in Winston-Salem, North Carolina in 2003 with a Bachelor's degree in Economics. I later earned a Master's degree in Business Administration from the Fuqua School of Business at Duke University in Durham, North Carolina in 2011. I started my employment with Piedmont Natural Gas, Inc. (Piedmont) in 2007 as a financial analyst in the Investor Relations Department. I became Manager – Capital Markets and Investor Relations in 2011 where I assumed leadership responsibility for both Piedmont's Investor Relations efforts as well as all of our capital raising activity. In 2014, I also began leading the Company's Enterprise Risk Management and Treasury Operations functions and was named Assistant Treasurer by Piedmont's Board of Directors. I held this position until the merger between Duke Energy and Piedmont closed on October 3,

2016. Since the merger I have served as Director, Regulated Utility Gas Operations Finance where I oversee the financial support for all of Duke Energy's gas businesses including Duke Energy Kentucky, Duke Energy Ohio, Piedmont Natural Gas and Duke's Gas Transmission & Storage business.

Q. PLEASE SUMMARIZE YOUR RESPONSIBILITIES AS DIRECTOR, REGULATED UTILITY GAS OPERATIONS FINANCE.

A. I am responsible for the short and long-term financial plan of Duke Energy's Gas business as well as for the financial performance of that business.

Q. HAVE YOU PREVIOUSLY PROVIDED TESTIMONY BEFORE THE KENTUCKY PUBLIC SERVICE COMMISSION?

A. No.

Q. WHAT IS THE PURPOSE OF YOUR REBUTTAL TESTIMONY?

A. The purpose of my testimony is to adopt the Direct Testimony, Filing Requirements, and corresponding data requests sponsored by Robert H. "Beau" Pratt in these proceedings that relate to the Company's forecast and budgeting processes submitted in its application. More specifically, I adopt pages 14 through 25 of Mr. Pratt's testimony and sponsor Filing Requirements (FR) 16(6)(a), 16(6)(b), 16(6)(d), 16(6)(e), 16(7)(b), 16(7)(c), 16(7)(d), 16(7)(f), 16(7)(g), 16(7)(h), and 16(7)(o). In response to FR 16(8)(b), I sponsor certain information contained in Schedules B-2, B-2.1, B-2.2, B-2.3, B-2.4, B-2.5, B-2.6, B-2.7, B-3, B-3.1, B-3.2, and B-4 that are supported by Duke Energy Kentucky witness Ms. Cynthia Lee. I sponsor the information contained in B-5 and B-5.1 and certain information contained in Schedule B-8 that is supported by Duke Energy Kentucky witness Michael Covington. In response to FR 16(6)(a), 16(6)(b) and 16(8)(d), I sponsor Schedules D-2.1 through D-2.14, and D-2.25. I also sponsor the forecasted data on Schedules I-1 through I-5 in response to FR 16(8)(i), and Schedule K in response to FR 16(8)(k).

II. ADOPTION OF TESTIMONY

Q. ARE YOU FAMILIAR WITH THE TESTIMONY SUBMITTED BY MR. ROBERT H. "BEAU" PRATT IN THESE PROCEEDINGS AND THE FILING REQUIREMENTS AND DATA REQUEST RESPONSES HE SPONSORED THAT RELATE TO THE COMPANY'S FORECAST AND BUDGETING PROCESSES?

A. Yes.

Q. DO YOU HAVE ANY CHANGES, OR CORRECTIONS TO THAT INFORMATION?

A. No.

Q. AS DIRECTOR, REGULATED UTILITY GAS OPERATIONS FINANCE, DO YOU HEREBY ADOPT THE DIRECT TESTIMONY OF ROBERT H. "BEAU" PRATT FILED IN THIS PROCEEDING AS YOUR OWN?

A. Yes.

III. CONCLUSION

Q. DOES THIS CONCLUDE YOUR REBUTTAL TESTIMONY?

A. Yes.

VERIFICATION

STATE OF NORTH CAROLINA)
) **SS:**
COUNTY OF MECKLENBURG)

The undersigned, Nicholas Giaimo, Director, RU Gas Operations Fiance, being duly sworn, deposes and says that he has personal knowledge of the matters set forth in the foregoing rebuttal testimony and that it is true and correct to the best of his knowledge, information and belief.

Nicholas Giaimo Affiant

Subscribed and sworn to before me by Nicholas Giaimo on this 9th day of January, 2019.

NOTARY PUBLIC

JACQUELINE M. BERRY
NOTARY
PUBLIC
UNION COUNTY, NC

My Commission Expires: 11/29/2021

COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

The Electronic Application of Duke Energy Kentucky, Inc., for: 1) An Adjustment of the Natural Gas Rates; 2) Approval of a Decoupling Mechanism; 3) Approval of New Tariffs; and 4) All Other Required Approvals, Waivers, and Relief.	)	Case No. 2018-00261

REBUTTAL TESTIMONY OF

GARY J. HEBBELER

ON BEHALF OF

DUKE ENERGY KENTUCKY, INC.

January 22, 2019

TABLE OF CONTENTS

I. INTRODUCTION AND PURPOSE

Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

A. My name is Gary J. Hebbeler and my business address is 139 East 4th Street, Cincinnati, Ohio 45202.

Q. BY WHOM ARE YOU EMPLOYED AND IN WHAT CAPACITY?

A. I am employed by Duke Energy Business Services LLC (DEBS) as Vice President, Gas Operations. DEBS provides various administrative and other services to Duke Energy Kentucky, Inc. (Duke Energy Kentucky or the Company) and other affiliated companies of Duke Energy Corporation (Duke Energy).

Q. ARE YOU THE SAME GARY HEBBELER THAT SUBMITTED DIRECT TESTIMONY IN THIS PROCEEDING?

A. Yes.

Q. WHAT IS THE PURPOSE OF YOUR REBUTTAL TESTIMONY?

A. The purpose of my rebuttal testimony is to address two of the recommendations made by Lane Kollen on behalf of the Kentucky Attorney General in this proceeding. Specifically, I respond to Mr. Kollen's recommendation to reduce Duke Energy Kentucky's revenue requirement as it relates to the integrity management deferral costs that were authorized by the Commission in Case No. 2016-00159. Second, I respond to Mr. Kollen's recommendation to reduce the Company's revenue requirement to exclude integrity management costs required to meet federal regulations that were not reflected in the Company's initial forecast.

II. INTEGRITY MANAGEMENT DEFERRAL

Q. PLEASE SUMMARIZE MR. KOLLEN'S RECOMMENDATION REGARDING THE COMPANY'S INTEGRITY MANAGEMENT DEFERRAL.

A. Mr. Kollen recommends that the Commission disallow recovery of the full and actual costs incurred in completing necessary pressure testing of the Company's natural gas transmission line. His recommendation is to disallow approximately $700,000 in costs that were incurred in completing the project. His recommended disallowance is based simply on the fact that the actual costs exceeded the Company's estimates that were included in its application for a deferral. Mr. Kollen also recommends that any amounts authorized for recovery should be amortized over ten years instead of the five-year amortization proposed by the Company. Duke Energy Kentucky witness Ms. Lawler addresses the timing of amortization in her rebuttal testimony.

Q. DOES DUKE ENERGY KENTUCKY AGREE WITH MR. KOLLEN'S RECOMMENDED DISALLOWANCE?

A. No.

Q. WHY NOT?

A. First, Mr. Kollen does not in any way allege that these costs are unreasonable or were not necessary. The costs were prudently incurred and there is no evidence to suggest the contrary. His only objection and justification for full recovery is that these costs exceeded the Company's initial estimates. Second, the Company acted reasonably in performing the necessary pressure testing to maintain its natural gas delivery system, to meet customer expectations for safety and reliability, and to comply with federal regulations, specifically requirements of the Pipeline Hazardous Materials Safety Administration (PHMSA).

Q. PLEASE SUMMARIZE WHY THE PRESSURE TESTING WAS NECESSARY.

A. The pressure testing was necessary to meet federal regulatory requirements. In December 2011, Congress passed the Pipeline Safety, Regulatory Certainty, and Job Creation Act of 2011, an amendment of Title 49 United States Code 60101 (Pipeline Safety Act of 2011). The federal regulations required more stringent safety and reliability protocols for both Department of Transportation and Owners/Operators. Among other things, the Pipeline Safety Act of 2011, and advisory bulletins by PHMSA clarified expectations of requirements for operators of gas transmission lines to verify accuracy of records of their system which includes providing traceable, verifiable, and complete documentation to support maximum allowable operating pressure.

Areas of Duke Energy Kentucky's natural gas transmission and distribution systems date back to the 1950's. Much of this system was not originally installed by Duke Energy Kentucky, but rather has been acquired through various mergers and acquisitions dating back many decades. Because of PHMSA's clarification of its expectations of compliance under the Pipeline Safety Act of 2011, Duke Energy Kentucky began reviewing its records for compliance with the Pipeline Safety Act of 2011 and consistency with PHMSA's guidance.

Upon receiving this PHMSA guidance, Duke Energy Kentucky, in compliance with Pipeline Safety Act of 2011, and to maintain the integrity of its natural gas delivery system, as well as to ensure that it continues to operate the system at the appropriate and historic maximum allowed operating pressure (MAOP), conducted and completed a very thorough segment by segment review of all transmission pipelines and facilities to determine both the existence and adequacy of its system records. This thorough and comprehensive record review involved not only investigating Duke Energy Kentucky's existing records, but reaching out to prior owners of parts of the Duke Energy Kentucky natural gas delivery system, such as Columbia Gas, to search for any system records that might exist and that were not provided to the Company as part of various mergers and acquisitions decades ago. It was only after the Company completed this review and analyzed the documentation that was available, that the Company could determine whether additional action was necessary or required under the federal regulations, and the immediacy of any such actions. To the extent documentation was not sufficient to verify the MAOP for particular segments as required PHMSA, Duke Energy Kentucky was obligated to act to verify the capabilities of these segments.

Pressure testing of existing transmission pipelines was necessary to provide traceable, verifiable, and complete documentation to support existing the MAOP levels per CFR Title 49 Parts 192.501 and 192.619. If Duke Energy Kentucky did not perform this pressure testing, the Company could no longer support operating its systems at historic MAOP levels, and would have to reduce operating pressures creating the potential that the system will have insufficient pressure during a time of need.

Q. PLEASE BRIEFLY EXPLAIN THE PRESSURE TESTING THAT WAS PERFORMED AND IS NOW AT ISSUE.

A. The pressure testing at issue was along Duke Energy Kentucky's AM07 line, comprising approximately three miles and running East to West from Taylor Mill Road to just East of Dudley Road. Confidential Attachment GJH-Rebuttal-1 depicts a map of the AM07 line. The line connects to Duke Energy Kentucky's UL16 line that runs from north to south. The Company performed this pressure testing in a way that minimized customer interruption of natural gas service while ensuring safety to employees and the public during the test.

Q. PLEASE EXPLAIN HOW THE COMPANY PERFORMED THE PRESSURE TESTING.

A. The pressure testing work included 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 a successful test, and returning the line to service. Because the AM07 line is a key artery in the Company's natural gas delivery system, and is the source to feed the UL16 line, the Company determined that it should conduct this pressure testing in two phases, with the dividing point at the connection to the UL16 line, so to continue to feed this line and not risk losing the system, especially during the winter heating season. Phase 1 of the testing consisted of the portion to the East of the UL16 line connection and Phase 2 was the western portion.

Q. PLEASE EXPLAIN HOW THE COMPANY DETERMINED THE INITIAL COST ESTIMATE FOR THE PRESSURE TESTING.

A. The initial costs were based upon the best available information at the time of the filing. As the Company explained in its initial deferral application, the initial cost estimates were developed using bid pricing received for the project as well as historical Duke Energy Kentucky project costs.[1] The Company further explained that as additional information is learned, such as new and additional work streams or processes are required, the actual costs could change. Based upon the information known to the Company at the time, the project costs, including overheads and indirect loading allocations, were estimated to be approximately $2.2 million in May 2016.[2] This was before the Company determined that it could not complete both phases of the pressure testing prior to the winter 2016/2017 heating season and that the phases should be divided between the heating season.

Q. PLEASE EXPLAIN WHY THE COMPANY DECIDED TO PERFORM THE PRESSURE TESTING IN TWO PHASES.

A. The reasons for conducting the pressure testing in two phases were twofold. First, the Company had always intended to test the AM07 line in segments to maintain the flow of natural gas to its UL16 line that is fed from the AM07 line and delivers natural gas to the southern portion of the Company's territory. Because the AM07 line is the artery feeding the UL16 line, if the Company took the AM07 line completely off line, it would lose the UL16 line and all customers fed from that line to the south. The AM07 line testing in phases was performed in such a way that gas

[1] Case No. 2016-00159, STAFF-DR-01-003.
[2] Id.

flows could continue to be directed to the UL16 line without interruption.

Second, while performing its final engineering for the pressure testing, the Company determined that it needed to ensure there was sufficient time, if necessary, to perform any required improvements if the testing indicated additional action was required. The Company, as a prudent operator, determined that the best way to perform this work was to divide the two phases of work around the winter heating season so as to not place any portion of the AM07 pipeline at risk for being out of service during the winter heating season. Phase 1 was thus completed before the winter 2016/2017 heating season and Phase 2 completed after. This split between the winter heating season was not part of the initial plan, but was determined to be the most prudent course to maintain reliability and integrity of the system.

Q. DID THE COMMISSION AUTHORIZE DUKE ENERGY KENTUCKY TO DEFER THE ACTUAL COSTS INCURRED IN PERFORMING THE PRESSURE TESTING AT ISSUE?

A. Yes. The Commission's Order that authorized the Company's deferral request explicitly states that "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."[3]

[3] *In the Matter of the Application of Duke Energy Kentucky, Inc for Approval to Establish a Regulatory Asset,* Case No. 2016-00159 KY.P.S.C. Order (July 22, 2016). *Emphasis added.*

Q. DID THE COMPANY PROVIDE UPDATES TO THE COMMISSION REGARDING THE PRESSURE TESTING STATUS AND ACTUAL COSTS?

A. Yes. The Company updated its cost projections through discovery and submitted journal entries for actual costs as part of its post-case correspondence. Duke Energy Kentucky filed its initial journal entries and results of pressure testing for phase 1 of the project on September 30, 2016. In that letter, the Company explained that it was necessary to conduct the testing in two phases to allow an opportunity to make any necessary improvements if testing indicated additional action was required so to allow sufficient time to have the pipe in service during the winter heating season. The Company explained that remaining pressure testing would be completed following the conclusion of the 2016-2017 winter heating season.

On March 15, 2017 Duke Energy Kentucky filed updated journal entries and a revised estimate of costs for the completion of the pressure testing in Case No. 2016-00159.[4] With this filing, the Company explained that the estimated costs for the pressure testing had increased due to the following factors:

- The actual costs of the first phase of the hydro test were higher than initially anticipated due primarily to the greater than anticipated usage of compressed natural gas (CNG) to maintain service to a large commercial customer that was connected directly to the AM07 line.

[4] Id. Post Case Correspondence March 15, 2017.

- To accomplish this testing, additional and unanticipated and unforeseeable measures including physical security, privacy barriers around CNG equipment, security patrols, and property restoration were necessary for the Company to perform the test and continue service to this large commercial customer that was not anticipated at the time of the original project estimates.
- There was also a significant amount of grading and access road improvement required to place equipment at a testing location that was not originally anticipated and grading and restoration required for water storage tanks due to unexpected rain flooding problems at the staging area.

In fact, the Company provided an updated estimate for the total pressure testing expense of $3.05 million.[5] The final and actual costs are less than that revised projection.

Q. PLEASE EXPLAIN WHY THE COMPANY EXPERIENCED ADDITIONAL COSTS RELATED TO THE FIRST PHASE OF THE PRESSURE TESTING.

A. Duke Energy Kentucky had a large commercial customer in the financial industry that was fed directly from the AM07 line. Duke Energy Kentucky knew that it would have to install a temporary CNG station to continue to provide natural gas service to this customer during the initial phase of testing due to their location along the line. There was no other way to reasonably provide natural gas service to this

[5] Id.

customer during the testing period. Serving this customer required placing CNG equipment on the customer's property and operating the station. While this customer was very accommodating and appreciative of the Company's efforts to ensure they were not without natural gas service, nonetheless, they had significant concerns from a safety perspective with having Duke Energy Kentucky's natural gas storage tanks and other equipment sitting on their property near employee parking, and along remote access roads for an extended period. The customer requested that the Company provide reasonable security and barriers to ensure that its employees were not able to encounter any of this equipment. Duke Energy Kentucky worked with this customer to provide this added and unanticipated level of assurance and protection.

In addition, by dividing the two testing phases between the winter heating season, additional costs were necessary for re-mobilization that were not contemplated when the original estimate was performed.

Q. DO YOU BELIEVE THAT THE ACTUAL COST INCURRED IN CONDUCTING THE PRESSURE TESTING WERE REASONABLE AND NECESSARY TO COMPLETE THE REQUIRED PRESSURE TESTING AND MEET FEDERAL REQUIREMENTS?

A. Yes. Again, the pressure testing was necessary. Duke Energy Kentucky's estimates were based upon the best available information at the time. The Company kept the Commission informed as to the status of its testing and the costs. These costs are reasonable, necessary and were prudently incurred. Duke Energy Kentucky should be allowed to recover all its actual costs.

Mr. Kollen has provided no testimony to suggest that the costs the Company incurred were not necessary or were somehow imprudently incurred. Mr. Kollen has not testified that he has any experience in operating a natural gas delivery system. The Commission should disregard his recommendation to disallow any portion of these costs. To do so, would suggest that the Company should not attempt to estimate its deferral requests with any degree of precision, but rather should provide broad and unsupportable cost estimates with such application or else risk disallowance of costs that were prudently incurred simply because the Company could not foresee every possible and uncontrollable expense. The position Mr. Kollen takes is unreasonable and would promote a bad public policy where estimates – not actual, prudently incurred costs – govern the extent of recovery of known and measurable deferred costs.

III. ONGOING INTEGRITY MANAGEMENT COSTS NOT INCLUDED IN THE INITIAL FORECAST

Q. PLEASE EXPLAIN MR. KOLLEN'S RECOMMENDATION TO EXCLUDE COSTS FOR OTHER INTEGRITY MANAGEMENT WORK THAT WAS NOT INCLUDED IN THE COMPANY'S FORECAST.

A. Mr. Kollen recommends that the Commission disallow $1.065 million in ongoing integrity management expenses that the Company identified after it performed its budget. Mr. Kollen's justification to exclude these costs is simply that they were not budgeted initially. He claims that the Company did not cite any new initiative or laws or demonstrate that these costs were not already included in the budget. He also claims that the Company has not demonstrated that the failure to incur these incremental costs will result in non-compliance with any laws.

Q. HOW DO YOU RESPOND TO MR. KOLLEN'S CLAIMS?

A. Mr. Kollen accurately stated that the additional integrity management expenses were not included in the forecast because they were identified after the budget had been established. The explanation for this is simple. At the time the budget was prepared by Gas Operations in the summer of 2017 for 2018, the Company had not identified the need to perform these activities in Kentucky. The application for this rate case proceeding was based upon a forecast that was prepared in early 2018, which was based upon the budget that was prepared in 2017 as adjusted for what was then known and measurable in early 2018. The need for performing these additional programs, and the corresponding costs were identified after the inputs for the rate case forecasted budget had been established. During the preparation of the rate case in the late second/early third quarter of 2018, Gas Operations concluded that these additional programs should be performed in Kentucky. The programs identified and the corresponding costs, are not currently being performed in Kentucky. These additional programs, as detailed in the Company's Attachment in response to STAFF-DR-02-030, support Duke Energy's pipeline integrity management initiatives, which are designed to further improve safety benefits to its customers by similar improvements to its natural gas distribution system.

Q. MR. KOLLEN IS ALSO CRITICAL THAT THE COMPANY HAS NOT IDENTIFIED ANY CHANGE IN LAW THAT PROMPTED THE COMPANY TO ADD THESE NEW PROGRAMS. HOW DO YOU RESPOND?

A. Mr. Kollen misunderstands the requirements under existing laws. Therefore, to explain in more detail the initiatives and laws underlying the desire to implement these initiatives it is useful to provide a historic context for the Company's integrity programs:

In December 2009, the U.S. Department of Transportation Pipeline and Hazardous Materials Safety Administration (PHMSA) amended the Federal Pipeline Safety Regulations, 49 C.F.R. 192, to include a new subpart, Subpart P "Gas Distribution Pipeline Integrity Management." This federal regulation requires operators of gas distribution pipelines to develop and implement a gas Distribution Integrity Management Program (DIMP) that includes a written integrity management plan. The DIMP approach was designed to promote continuous improvement in pipeline safety by requiring operators to identify and implement appropriate risk control measures.

At the recommendation of the National Transportation Safety Board, the American Petroleum Institute (API) developed a comprehensive framework for the development of "Pipeline Safety Management Systems" for pipeline operators. As a result, the API's Recommended Practice 1173 (RP 1173) – Pipeline Safety Management Systems was issued in July 2015. RP 1173 identifies safety management system requirements as guidance "and leaves the details associated with implementation and maintenance of the requirements to the individual pipeline operators." (RP 1173 at 1). This again illustrates both the importance of integrity management and the requirement to continuously improve.

On July 14, 2018, the Commission became responsible for enforcing Kentucky's Underground Facility Protection statute, KRS 367.4917, commonly known as the call-before-you-dig law, as it pertains to natural gas and hazardous liquid pipelines. The Commission investigates incidents of excavation-caused damage and may assess penalties as are appropriate. As such, it emphasizes the importance of underground damage prevention and encourages effective damage prevention programs by operators. Currently, third-party damages to Duke Energy Kentucky's pipeline system present the single largest risk. Enforcement of this important statute illustrates the Commission's commitment to, and understanding of, the importance of pipeline integrity. The initiatives identified and included in this rate case,[6] and the associated incremental costs, are largely directed at reducing excavation damages by improving records, identifying untoneable assets and educating the public and excavators on safe excavating practices.

Q. HOW DID DUKE ENERGY KENTCKY RESPOND TO THE CHANGES IN LAW THAT YOU PREVIOUSLY DESCRIBED?

A. Duke Energy Kentucky developed an internal organization whose role is to lead, develop and support a program that addresses specific criteria as required by PHMSA including: (a) knowledge of the Company's natural gas distribution system; (b) threat identification; (c) risk evaluation and ranking; (d) implementation of measures to address risk; (e) measurement of performance, monitoring results, and evaluating effectiveness; (f) periodic evaluation and improvement; and (g) reporting results. The purpose of the plan is to formalize the procedures, guidelines, and organizational support that will minimize the risk to people, property, and the environment through managing the integrity of natural gas distribution pipelines. It

[6] *See* Company's Response to STAFF-DR-02-030, Attachment detailing the incremental programs and associated costs identified.

also includes details on the roles, responsibilities, and qualifications of the personnel involved in various components.

In response to federal regulation and in accordance with the RP 1173 process, Duke Energy Kentucky implemented a continuous process to review, analyze and assess the integrity of its natural gas delivery systems. This systematic approach is iterative, continually evolving and intended to guide the Company to continue evaluating its system and programs to find and correct ineffective measures or gaps that are not otherwise addressed by current and existing integrity management programs. Once these gaps are identified, there is an expectation that utilities will develop plans of action to address these deficiencies. This process has resulted in the integrity initiatives to target identified threats to Duke Energy Kentucky's system. The initiatives involve both distribution (DIMP) and transmission (TIMP) and will assist Duke Energy Kentucky in adding additional programs and processes required to enhance pipeline integrity.

As part of its requirement to periodically evaluate and improve its integrity management programs, Duke Energy Kentucky has identified areas that require additional focus. The initiatives proposed address the threats in a manner that will increase the effectiveness of its program and reduce risks to the public. Duke Energy Kentucky has historically executed, and will continue to execute, integrity management practices, follow regulation guidelines, manage training qualifications, and repair leaks; nonetheless, these initiatives will be above the costs reflected in the current base rates.

Q. DO YOU BELIEVE THE INCREMENTAL INTEGRITY COSTS THAT WERE INCLUDED IN THE FORECASTED TEST YEAR IN THIS CASE ARE NECESSARY AND PRUDENT?

A. Yes. The costs of implementing these pipeline integrity initiatives reflect prudent and necessary business expenses to be incurred by Duke Energy Kentucky in compliance with PHMSA's regulations. They were identified after the budget used for this rate case was prepared. These programs, planned to be implemented in 2019, were not in place at the time of the Company's last natural gas base rate case and, therefore, such costs are not recovered in Duke Energy Kentucky's current base rates. Although the aforementioned PHMSA regulations did exist at the time of the Company's last rate case, the initiatives described above are new and are proposed to be implemented beginning in 2019. These new pipeline integrity initiatives were identified as being necessary as a result of the actions that the Company has taken since its last natural gas base rate case in direct response to these PHMSA regulations. Indeed, this iterative continuous improvement process is precisely the intent and design of PHMSA's regulations.

Q. PLEASE EXPLAIN WHETHER THESE ADDITIONAL INTEGRITY COSTS ARE TRULY INCREMENTAL COSTS TO THOSE COSTS ALREADY INCLUDED IN THE BUDGET USED TO PREPARE THE RATE CASE.

A. These incremental costs are for new and ongoing programs, and are not existing programs in Kentucky. As I explained above, as risk is identified by the continuous improvement process, projects and initiatives are developed to mitigate risk.

Implementing these initiatives now, in lieu of scheduling them in later years will help mitigate the risk sooner and increase the safety of our natural gas system for our customers, contractors and employees. These initiatives would be ongoing, continuing annually and are not included in the current budget nor our current rates.

Q. ONE OF THE NEW PROGRAMS IDENTIFIED INCLUDES RECORDS MANAGEMENT. DOES DUKE ENERGY KENTUCKY CURRENTLY HAVE A RECORDS MANAGEMENT PROGRAM AS PART OF ITS DIMP AND TIMP INITIATIVES?

A. While Duke Energy Kentucky does currently have record management programs, Duke Energy Kentucky has recognized opportunities to improve its records to better support the integrity management program. Its team, composed of Leadership, Engineers, Field Inspectors, and back office support (Compliance and GIS/Document Management staff), is reexamining processes and procedures to improve how the Company designs, builds, and records its information. This will include change management, training, new technologies, and assessing resource support needs.

This new initiative will implement technologies designed to reduce human errors and risks associated with data collection which provides more accurate data from the field. This requires total input from every portion of the "project life cycle" with an understanding of the importance of traceable, verifiable, and complete data. API recommended practice 1173 – Pipeline Safety Management Systems will aid in this change management process.

The "Records" projects will be in direct alignment with PHMSA's directive to provide system records that are "traceable, verifiable and complete." PHMSA has stressed the importance of accurate records in several Advisory Bulletins. The additional integrity management expenses will be utilized to contract with contingent workers and vendors to augment our existing staff to accelerate completion of the records improvements. This work will include scanning and indexing records into one central system of record. Having records in one central system will provide a benefit to the public by having necessary information readily available to aid in performing operations and maintenance on our pipelines.

Q. PLEASE DESCRIBE THE DAMAGE PREVENTION PROGRAMS AND HOW THOSE ARE INCREMENTAL AND DIFFERENT TO CURRENT PROGRAMS.

A. Mr. Kollen states that projects for "Damage Prevention" include "corrective maintenance" on mains and services, costs that are included in ongoing distribution maintenance and should already be in the budget. Mr. Kollen's assumption is not accurate. The Damage Prevention program included in this case is incremental to what is already being performed and thus represents incremental costs not currently reflected in existing budgets.

As the number one risk to Duke Energy Kentucky's system, addressing excavation damages is essential to improving reliability and safety. Our existing budget does include corrective maintenance on our system as they are discovered during normal operations and maintenance activities. However, further investigations and repairs are needed into untoneable locates that will help prevent damages resulting from incorrect markings. Accurate marking of service lines is occasionally difficult due to inadequate historic records, as discussed above, as well as field issues that range from buried curb boxes to bad (or no) tracer wire. New processes are necessary to locate these lines to prevent excavation damages. Duke Energy Kentucky intends to utilize contractors and vendors for proactively locating untoneable mains and services, which includes using an investigator to verify if the service is truly untoneable and use reasonable means to successfully locate the line. If the lines are found to be untoneable then the contractor will make the necessary repairs. Again, this proactive initiative would accelerate the finding of these untoneable mains and services, in lieu of finding them during normal operations and maintenance activities, and make them locatable sooner which will increase public safety by reducing excavation damages as a new accelerated action as described under CFR 49 192.1007 (d) Identify and Implement Measures to Address Risk.

Another new program directed at reducing excavation damages is to implement one-call ticket risk ranking software for identifying high risk tickets. This software utilizes current one-call ticket data and incorporates asset information from GIS to focus damage prevention resources and activities on locate requests with the highest risk (frequent offenders). The software identifies the riskiest excavation tickets every day so outreach to the high-risk tickets can be made to prevent damages before they happen. We expect to use this information to evaluate, on a daily basis, the riskiest tickets and setting up communication to the excavator about safe digging practices. This communication can be in the form of a field visit, phone call, email, *etc*. This product has a demonstrated history, from other operators, that identifying and educating the excavators included in the top 10% of riskiest excavation tickets you can prevent 55% of damages by being proactive. We are optimistic that we will see a decrease in excavation damages using this software. These damage prevention initiatives are intended to support and be in alignment with Commission's responsibility to enforce the Kentucky's Underground Facility Protection statute.

Q. MR. KOLLEN RECOMMENDS DISALLOWANCE OF COSTS ATTRIBUTABLE TO TRAINING AND FOR RADIO AND BILLBOARDS AND MAILINGS TO INCREASE AWARENESS OF DUKE ENERGY KENTUCKY'S GAS DISTRIBUTION SYSTEM. DO YOU AGREE?

A. No. These costs are for public awareness and safety which, as I understand, are recoverable through rates. The additional integrity management expenses for training is directly related to reducing excavation damage by expanding the Duke Energy Kentucky's Public Awareness Program (PAP). This will include radio ads, billboards and mailings intended to reach homeowners, who frequently do not utilize the one-call system, and excavators that are in addition to our annual PAP to inform them of their obligation to use the one-call system and to educate them regarding the need for safety around the natural gas delivery system. The additional integrity management expenses would also include hosting safety and educational events in our Northern Kentucky service territory to proactively educate the public regarding the need for safety and to protect the underground natural gas infrastructure. These costs are reasonable, necessary and prudent and should be includable in rates.

IV. CONCLUSION

Q. WAS CONFIDENTIAL ATTACHMENT GJH-REBUTTAL-1 PREPARED BY YOU OR UNDER YOUR DIRECTION AND CONTROL?

A. Yes.

Q. DOES THIS CONCLUDE YOUR REBUTTAL TESTIMONY?

A. Yes.

VERIFICATION

STATE OF OHIO	)	
	)	**SS:**
COUNTY OF HAMILTON	)	

The undersigned, Gary J. Hebbeler, Vice President Gas Operations, being duly sworn, deposes and says that he has personal knowledge of the matters set forth in the foregoing rebuttal testimony and that it is true and correct to the best of his knowledge, information and belief.

Gary J. Hebbeler

Gary J. Hebbeler, Affiant

Subscribed and sworn to before me by Gary J. Hebbeler on this 22nd day of Jan., 2019.

Adele M. Frisch

NOTARY PUBLIC

NOTARIAL SEAL
STATE OF OHIO

ADELE M. FRISCH
Notary Public, State of Ohio
My Commission Expires 01-05-2024

My Commission Expires: 1/5/2024

CONFIDENTIAL PROPRIETARY TRADE SECRET

CONFIDENTIAL ATTACHMENT GJR-Rebuttal-1

FILED UNDER SEAL

COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

The Electronic Application of Duke Energy Kentucky, Inc., for: 1) An Adjustment of the Natural Gas Rates; 2) Approval of a Decoupling Mechanism; 3) Approval of New Tariffs; and 4) All Other Required Approvals, Waivers, and Relief.	)))))))	Case No. 2018-00261

REBUTTAL TESTIMONY OF

SARAH E. LAWLER

ON BEHALF OF

DUKE ENERGY KENTUCKY, INC.

January 22, 2019

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PAGE

I. INTRODUCTION AND PURPOSE

Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

A. My name is Sarah E. Lawler, and my business address is 139 East Fourth Street, Cincinnati, Ohio 45202.

Q. BY WHOM ARE YOU EMPLOYED AND IN WHAT CAPACITY?

A. I am employed by Duke Energy Business Services LLC (DEBS) as Director Rates & Regulatory Planning. DEBS provides various administrative and other services to Duke Energy Kentucky, Inc., (Duke Energy Kentucky or Company) and other affiliated companies of Duke Energy Corporation (Duke Energy).

Q. ARE YOU THE SAME SARAH LAWLER THAT SUBMITTED DIRECT TESTIMONY IN THIS PROCEEDING?

A. Yes.

Q. WHAT IS THE PURPOSE OF YOUR REBUTTAL TESTIMONY?

A. The purpose of my rebuttal testimony is to respond to certain opinions and recommendations expressed by Attorney General (AG) witness Lane Kollen. Specifically, I address: (1) Mr. Kollen's recommendation that cash working capital be set to zero because the Company did not file a lead/lag study; (2) Mr. Kollen's recommendation to include intercompany no notice transportation revenues in determining the revenue requirement increase; (3) Mr. Kollen's recommendation to reduce test year payroll expense and payroll tax expense; (4) Mr. Kollen's recommendation to reflect cost savings associated with the extension of the meter testing cycle from 10 years to 15 years; and (5) Mr.

Kollen's recommendation to extend the amortization period on deferred integrity management expenses from five-years to ten-years.

II. CASH WORKING CAPITAL

Q. PLEASE DESCRIBE MR. KOLLEN'S PROPOSAL REGARDING CASH WORKING CAPITAL.

A. Mr. Kollen recommends that Duke Energy Kentucky's cash working capital should be set at $0 absent the Company filing a lead/lag study because the 1/8 methodology the Company used to calculate cash working capital is "outdated and inaccurate."

Q. DO YOU AGREE WITH MR. KOLLEN'S RECOMMENDATION THAT DUKE ENERGY KENTUCKY'S CASH WORKING CAPITAL SHOULD BE SET AT $0?

A. No, I do not. While Mr. Kollen may not like the fact that the 1/8 O&M methodology for calculating cash working capital has been accepted by this Commission in previous proceedings, that is the case. In fact, prior witnesses for the Attorney General have acknowledged the Commission's practice of using the 1/8 O&M method. As noted by Robert J. Henkes, testifying for the Attorney General in Case No. 2009-00202, a prior Duke Energy Kentucky natural gas rate case, "…it is my understanding that the Commission has *consistently allowed* [Duke Energy Kentucky's] cash working capital to be determined based on this modified 1/8th method."[1] (emphasis added)

[1] *In re Application of Duke Energy Kentucky, Inc. for an Adjustment of Gas Rates,* Case No 2009-00202 (Direct Testimony of Robert J. Henkes, p. 18) (October 12, 2009).

Duke Energy Kentucky followed this longstanding precedent in developing its estimate of cash working capital as it has done in every rate case for electric and natural gas over many years.

Q. IF THE COMMISSION AGREES WITH MR. KOLLEN'S ARGUMENT, SHOULD THE COMMISSION IMPLEMENT SUCH A REQUIREMENT IN THIS CASE?

A. No. I am not aware of any rule in the Kentucky Administrative Regulations or in the Kentucky Revised Statutes that requires a utility to develop a lead/lag study for its estimate of cash working capital. The Commission found the Company's initial application to be fully compliant and issued a notice on September 10, 2018, that there were no deficiencies in the Company's initial application. It would be unfair to the Company to reduce rate base by over $3 million because the Company failed to comply with a requirement that does not exist.

A utility is guided by two principles when making regulatory filings. One is simply the codified rules and regulations. The second principle guiding such filings is Commission precedent. Commission precedent for establishing Duke Energy Kentucky's cash working capital has, for many, many years, been to use the 1/8 O&M method. It would be unfair to change the rules in the midst of this case.

Therefore, if the Commission ultimately agrees to reject its longstanding precedent of using the 1/8 O&M method in favor of any other method for computing a cash working capital allowance in rate base, it should only be implemented prospectively and not in this instant proceeding.

Q. DO YOU HAVE ANY COMMENTS ABOUT MR. KOLLEN'S STATEMENT THAT SEVERAL OF DUKE ENERGY KENTUCKY AFFILIATES HAVE USED THE LEAD/LAG METHODOLOGY IN SETTING RATES?

A. First, the Kentucky Public Service Commission is not bound by the regulatory models of other jurisdictions; consequently, it is not relevant whether other Duke Energy Kentucky affiliates file lead/lag studies or not. Nevertheless, although Mr. Kollen points out several examples of the Company's affiliates relying, at least in part, on lead/lag studies, he neglects to mention that the same affiliates use the 1/8 O&M method for calculating their cash working capital allowance in their wholesale rate formulas. Even Duke Energy Kentucky's wholesale transmission rate, approved by the Federal Energy Regulatory Commission (FERC), includes a cash working capital allowance based on the 1/8 O&M method. Therefore, where Mr. Kollen states, on page 13, lines 1 through 2 of his testimony, that "[other] Duke Energy, Inc., utilities *unilaterally* set their working capital at $0," (emphasis added) he apparently did not fully research all of the regulatory filings made by Duke Energy affiliates. It is simply not factually correct to say that ALL of the Duke Energy, Inc., utilities *unilaterally* set their working capital at $0.

He also points to testimony provided by a former Duke Energy witness in an Ohio rate case but Mr. Kollen failed to mention that the Public Utilities Commission of Ohio (PUCO) has accepted the 1/8 O&M method for computing working capital allowance in other cases in Ohio. One would presume that by approving the use of the 1/8 O&M method in these instances, the PUCO, would deem this to be a *reasonable* method as well.

Q. DO YOU AGREE WITH MR. KOLLEN THAT A LEAD/LAG STUDY CAN BE PERFORMED 'IN-HOUSE' AT NO INCREMENTAL COST?

A. It depends on how one defines "incremental" cost. For the Company to perform such a study in-house it will require an individual or a group of individuals to dedicate a portion of their time to perform a rather detailed study. While that may not generate incremental cost to the Company, *i.e.*, overall payroll may not change, it does require that these individuals shift their time from whatever they are normally doing to focus on a lead/lag study.

The Company would most likely hire an outside consultant to perform such a study and that would, in no uncertain terms, be an incremental cost that will be borne by customers. This is particularly true now, given that the Company relied upon prior Commission precedent in its preparation and submittal of its application in this proceeding using the accepted 1/8 O&M method.

Q. SHOULD THE COMMISSION ADJUST THE COMPANY'S REVENUE REQUIREMENT TO SET DUKE ENERGY'S WORKING CAPITAL TO $0?

A. No. The Commission should reject this recommendation. There is no reason for the Commission to change precedent in this instance. The 1/8 O&M method has long been considered a reasonable approximation of working capital and has been approved by this Commission to establish the Company's rates in the past. The Company believes this method should continue to be used. Reducing the

Company's working capital because the Company relied upon and followed prior Commission precedent and regulations for submittal of rate case applications by using the 1/8 O&M method and did not anticipate a change in rate case filing requirements would be unreasonable and punitive.

III. NO NOTICE TRANSPORTATION REVENUES

Q. PLEASE DESCRIBE MR. KOLLEN'S PROPOSAL REGARDING INTERCOMPANY NO NOTICE TRANSPORTATION REVENUES.

A. Mr. Kollen recommends that the Company make an adjustment to its requested revenue requirement to reflect an increase in intercompany no notice transportation revenues of $603,445.

Q. DOES THE COMPANY AGREE WITH THIS RECOMMENDATION?

A. Yes. There were none such revenues contemplated in the Company's Schedule M and therefore the Company agrees with Mr. Kollen that an adjustment should be made to include intercompany no-notice transportation revenue of $603,445. The Company agrees to reduce its revenue requirement including gross-ups by $604,654 to reflect the additional revenue.

IV. PAYROLL EXPENSE AND PAYROLL TAX EXPENSE

Q. PLEASE DESCRIBE MR. KOLLEN'S RECOMMENDATION REGARDING TEST YEAR PAYROLL EXPENSE.

A. Mr. Kollen claims that the Company's total payroll cost and expense amounts are significantly greater in the test year compared to the actual amounts in prior calendar years, especially given the fact that the Company claims that test year payroll has been reduced to reflect the termination of meter reader positions due to the automated meter initiative. As a result, Mr. Kollen believes that the forecasted test year payroll expense should be reduced. Mr. Kollen utilized information from Schedule G-1 and Company responses to AG-DR-01-055 and STAFF-DR-02-016 to develop his recommended adjustment to reduce payroll tax expense by $333,883 and related payroll tax expense by $28,058.

Q. DO YOU AGREE WITH MR. KOLLEN'S RECOMMENDATION?

A. No. Schedule G-1 was prepared based on the Company's forecast for the test period. As already established in our application, the Company is using a forecasted test period in this case, not historical. Mr. Kollen is basing his adjustment on historical 2017 data, rather than the forecasted test period data that the Company presented in this case. As discussed in the direct testimony of Mr. Beau Pratt, on an annual basis, the Company conducts a very vigorous budgeting process. The forecasted data used in this case is based on that budget. Many factors and assumptions are used in determining the budget. While historical data is always considered in developing a budget, that is not the only variable or assumption to consider. There is no reason to believe that the budget is incorrect. Mr. Kollen's proposal would suggest that all of the Company's efforts to produce its forecast could be abandoned and that it should just take a trend of historical costs. In reality, the Company's financial forecasting process is much more sophisticated than the simplistic methodology Mr. Kollen is advocating. The Commission should reject Mr. Kollen's proposed adjustment.

Q. IF THE COMMISSION DECIDES TO ACCEPT MR. KOLLEN'S PROPOSAL TO USE HISTORICAL PAYROLL TRENDS TO ADJUST THE COMPANY TEST YEAR PAYROLL COST, SHOULD IT RELY ON MR. KOLLEN'S CALCULATIONS?

A. No. It bears repeating that the Company does not agree with Mr. Kollen in this instance; however, if the Commission does adopt Mr. Kollen's recommendation then the calculation should be corrected. When calculating his adjustment, Mr. Kollen started with 2017 actual payroll expense provided to him by the Company in discovery. He then attempted to normalize the 2017 payroll expense by excluding what he apparently believed was the total payroll costs for meter reading that should recur in the future. But when he excluded meter reading costs, he excluded ALL costs in Account 902 which totaled $452,047. He failed to consider the fact that Account 902 includes payroll and non-payroll expenses. By definition in the FERC Code of Federal Regulations, Account 902 "shall include the cost of labor, materials used and expenses incurred in reading customer meters." Account 902 included $170,591 of non-payroll expenses for calendar year 2017. If the Commission adopts Mr. Kollen's recommendation, it must use the correct math. Under Mr. Kollen's proposal, it would only be appropriate to reduce 2017 actual payroll expense by $281,456. That correction changes the amount of Mr. Kollen's proposed reduction in test year payroll expense to $151,546 and his proposed reduction to payroll tax expense by $12,735. Applying the appropriate gross up factors, this would result in a reduction to the Company's revenue requirement increase of $151,850 for payroll expense and $12,761 for payroll tax expense.

V. COST SAVINGS ASSOCIATED WITH EXTENSION OF METER TESTING CYCLE

Q. PLEASE DESCRIBE MR. KOLLEN'S RECOMMENDATION REGARDING COST SAVINGS ASSOCIATED WITH THE EXTENSION OF THE METER TESTING CYCLE.

A. Mr. Kollen recommends that $340,000 of annualized cost savings from the company's proposed extension of its meter testing cycle from ten years to fifteen years be reflected in its revenue requirement request.

Q. DOES THE COMPANY AGREE WITH THIS RECOMMENDATION?

A. As noted in the company's response to STAFF-DR-02-022, The Company agrees with this recommendation only if the Commission approves the change in the meter testing cycle. This annualized cost savings is only achieved by moving to the longer meter testing cycle. This would result in a reduction in the test year revenue requirement request including gross-ups of $340,681.

VI. DEFERRED INTEGRITY MANAGEMENT EXPENSES AMORTIZATION PERIOD

Q. PLEASE DESCRIBE THE DEFERRED INTEGRITY MANAGEMENT EXPENSES.

A. In Case No. 2016-00159 the Company was authorized to defer certain integrity management expenses related to pressure testing of segments of its AM07 transmission pipeline that were required by the Pipeline Safety Act of 2011. The Commission's Order in that case said: "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." The Commission's Order did not specify an amortization period. The Company incurred $2.887 million in costs to perform the pressure testing and is requesting amortization of these costs over a five-year period.

Q. PLEASE DESCRIBE MR. KOLLEN'S RECOMMENDATION REGARDING THE AMORTIZATION OF DEFERRED INTEGRITY MANAGEMENT EXPENSES.

A. Mr. Kollen recommends a ten-year amortization period due to the magnitude and nonrecurring nature of the expense.

Q. DO YOU AGREE WITH MR. KOLLEN'S RECOMMENDATION?

A. No. The magnitude of the deferred expense is not so great that it should preclude recovery over a five-year period. It is reasonable to amortize certain expenses over a period of time that is expected to exist between rate cases. Five years is the Company's best approximation of the estimated time period between rate cases. Further, in the Company's most recent electric rate case filing in Case No. 2017-00321, the Commission granted regulatory asset amortization of several of the Company's regulatory assets over a five-year period.

As the Commission stated in its Order in Case No. 2016-00159, "these costs are extraordinary, nonrecurring expenses that could not have been reasonably anticipated." The Company is not earning carrying costs on the deferred asset so some consideration should be given for the time value of money. Even over the Company's proposed five-year amortization period, the net present value of the recovery is significantly less than the amount of money already spent. The Company would be willing to consider an amortization period longer than five years if it were permitted to accrue carrying costs on the unamortized balance of the regulatory asset.

VII. REVISED REVENUE REQUIREMENT REQUEST

Q. DOES THE COMPANY HAVE A REVISED REVENUE REQUIREMENT REQUEST BASED ON YOUR REBUTTAL TESTIMONY?

A. Yes. The following table reflects the Company's revised revenue requirement increase based on my testimony and assumes that the Commission approves the Company's request to extend its meter testing cycle to fifteen years, the Company's revised revenue requirement request is $9,593,117. If the Commission rejects the change in the meter testing schedule, then this revised overall adjusted revenue increase should be increased by $340,681.

1	Duke Energy Kentucky Initial Request	$10,542,199
2	Add Intercomany No Notice Transportation Service	(603,445)
3	Reduce O&M for Savings from Extending Meter Testing Cycle	(340,000)
4	Total Adjustments to Company's Proposed Revenue Requirement	($943,445)
5	Adjustment for B/D and PSC Gross Up	(1,891)
6	Adjustment to Cash Working Capital as a result of above changes*	(3,746)
7	Total Grossed Up Adjustments	($949,082)
8	Duke Energy Kentucky Revised Revenue Requirement Request	$9,593,117

*The Company uses the 1/8th O&M method to calculate Cash Working Capital. The adjustment on line 3 reduces O&M and therefore reduces Cash Working Capital.

VIII. CONCLUSION

Q. DOES THIS CONCLUDE YOUR PRE-FILED REBUTTAL TESTIMONY?

A. Yes.

VERIFICATION

STATE OF OHIO)
) **SS:**
COUNTY OF HAMILTON)

The undersigned, Sarah E. Lawler, Director Rates & Regulatory Planning, being duly sworn, deposes and says that she has personal knowledge of the matters set forth in the foregoing rebuttal testimony and that it is true and correct to the best of her knowledge, information and belief.

Sarah E. Lawler Affiant

Subscribed and sworn to before me by Sarah E. Lawler on this 9th day of January, 2019.

NOTARY PUBLIC

My Commission Expires: July 8, 2022

NOTARY PUBLIC ★ STATE OF OHIO ★

E. MINNA ROLFES-ADKINS
Notary Public, State of Ohio
My Commission Expires
July 8, 2022

COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

The Electronic Application of Duke Energy Kentucky, Inc., for: 1) An Adjustment of the Natural Gas Rates; 2) Approval of a Decoupling Mechanism; 3) Approval of New Tariffs; and 4) All Other Required Approvals, Waivers, and Relief.	))))))))	Case No. 2018-00261

REBUTTAL TESTIMONY OF

RENEE H. METZLER

ON BEHALF OF

DUKE ENERGY KENTUCKY, INC.

January 22, 2019

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I. INTRODUCTION AND PURPOSE

Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

A. My name is Renee Metzler. My business address is 550 South Tryon, Charlotte North Carolina.

Q. BY WHOM ARE YOU EMPLOYED AND IN WHAT CAPACITY?

A. I am employed by Duke Energy Business Services LLC (DEBS), as Managing Director – Retirement and Health and Welfare. DEBS provides various administrative and other services to Duke Energy Kentucky, Inc., (Duke Energy Kentucky or Company) and other affiliated companies of Duke Energy Corporation (Duke Energy).

Q. ARE YOU THE SAME RENEE H. METZLER THAT SUBMITTED DIRECT TESTIMONY IN THIS PROCEEDING?

A. Yes.

Q. WHAT IS THE PURPOSE OF YOUR REBUTTAL TESTIMONY IN THIS PROCEEDING?

A. The purpose of my Rebuttal Testimony is to address the erroneous claims and adjustments made by the Attorney General's witness Lane Kollen related to the Company's Incentive Compensation and Retirement Plan expenses. Specifically, Mr. Kollen recommends adjustments to the Company's revenue requirement related to its 401(k) matching, retirement plan expenses, medical premiums, and the inclusion of restricted stock units (RSUs) as part of the incentive compensation package.

II. DISCUSSION

Q. PLEASE DESCRIBE MR. KOLLEN'S ADJUSTMENT RELATED TO THE COMPANY'S 401(k) MATCHING.

A. Mr. Kollen begins his discussion of his recommended adjustment on page 26 of his direct testimony. Mr. Kollen claims that, according to the Commission's recent precedent, benefit expense should be adjusted to remove 401(k) matching expense for those employees who also participate in a defined benefit plan.

Q. DID THE COMMISSION MAKE THIS ADJUSTMENT AS PART OF DUKE ENERGY KENTUCKY'S MOST RECENT ELECTRIC BASE RATE CASE?

A. No. It did not. Mr. Kollen made this same recommendation in the Company's recent electric base rate case, Case No. 2017-00321 and the Commission rejected it.[1] Therefore, the Commission's most recent precedent for Duke Energy Kentucky, established less than one year ago, is not to make the adjustment proposed by Mr. Kollen. In fact, the Commission agreed with Duke Energy Kentucky's inclusion of 401(k) matching costs given the Company's significant efforts to reduce retirement related expenses but still remain competitive. In addition, the Commission did not make a distinction between union and non-union employees to give the Company an opportunity to address the higher traditional defined benefit retirement costs as it relates to union employees.[2]

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[1] *In re: Electronic Application of Duke Energy Kentucky, Inc. for: 1) An Adjustment of the Electric Rates; 2) Approval of an Environmental Compliance Plan and Surcharge Mechanism; 3) Approval of New Tariffs; 4) Approval of Accounting Practices to Establish Regulatory Assets and Liabilities; and 5) All Other Required Approvals and Relief* Case No. 2017-00321 (Ky P.S.C. April 13, 2018) at 22-23.
[2] *Id.*

Q. WHY SHOULD THE COMMISSION REJECT MR. KOLLEN'S PROPOSED ADJUSTMENT AGAIN IN THIS PROCEEDING?

A. The same justifications and reasoning that was applicable in the Company's electric rate case holds true today and support inclusion of these costs in base rates.

Q. HAS DUKE ENERGY KENTUCKY HAD AN OPPORTUNITY TO ADDRESS THESE ISSUES WITH RESPECT TO UNION EMPLOYEES SINCE THE COMMISSION'S APRIL 13, 2018, ORDER IN CASE NO. 2017-00321?

A. No. Union contracts for Duke Energy Kentucky gas employees were in effect when the Company filed its base rate case in August 2018 and the contracts covering the majority of Duke Energy Kentucky gas employees continue through May 2021. As the Commission is aware, any mid-term negotiations that would result in a reduction in benefits for employees would be highly unlikely because the union would likely not agree to even discuss it outside a contract negotiation. Negotiations with these unions will begin after the test period, and our negotiation strategy has not been determined at this time.

Q. DO YOU AGREE WITH MR. KOLLEN'S RECOMMENDED ADJUSTMENT?

A. No. Mr. Kollen's sole justification for his elimination of approximately $297,000 from the Company's revenue requirement is that certain employees have both a defined benefit pension plan benefit and a defined contribution plan benefit. As the Company explained in Case No. 2017-00321, the value of the Company's retirement benefit is what is important, rather than whether the Company chooses to deliver the value through multiple components. The same holds true here today. In other words, a one dollar bill has equal value to four quarters, even though they are denominated in different forms. Mr. Kollen offers no support whatsoever that the benefit being provided from these plans is not market competitive. Second, he ignores the fact that many companies, including Duke Energy, have significantly reduced retirement related expenses by transitioning many employees eligible for pension benefits to a less rich formula and partially utilizing those pension savings to enhance 401(k) matching formulas. The Company's total rewards package, as a whole, is designed to be market competitive and compensation and benefit programs are benchmarked to ensure that is the case. Mr. Kollen makes no claim to the contrary.

Duke Energy has aggressively managed costs related to its retirement benefit program by closing the defined benefit pension plan to new hires, and, for existing employees, freezing final average pay benefit formulas for all non-union employees and transitioning employees from a final average pay formula to a more "Defined Contribution like" cash balance pension formula. To offset the impact of those pension changes, the Company utilized some of the pension savings to enhance the 401(k) matching formula for those employees to stay competitive with the market. Under the final average pay formula, retirement costs (traditional pension plus 401(k) match) were approximately 15 percent of pay. Under the cash balance program (cash balance pension plus 401(k) match) and the new hire program (401(k) match and non-matching contributions) costs are 10-12 percent of pay. To arbitrarily eliminate recovery of retirement cost because some employees have benefits under two plans, would penalize the Company for aggressively managing its retirement costs. Like all prudent and cost-minded companies that offer benefit packages that include retirement programs for employees, Duke Energy continually evaluates these programs for cost and reasonableness. As these programs change and evolve over time, it must be done in a manner that is fair to employees who make employment and continued employment decisions based upon the existence of such plans. To arbitrarily require the Company to cease funding programs that current or retired employees previously participated in and relied upon is unreasonable and unfair to those employees. Moreover, it also provides a significant disincentive for the Company to consider and pursue opportunities to revisit programs and follow market trends and implement new programs that will overall reduce its expenses.

Q. WHAT IS YOUR RECOMMENDATION REGARDING MR. KOLLEN'S ADJUSTMENT RELATED TO POST-RETIREMENT PLAN EXPENSES?

A. The Commission should once again ignore Mr. Kollen's arbitrary and unsupported proposal to reduce the Company's retirement plan expenses. The same justifications and reasoning that was applicable in the Company's electric rate case holds true today and support inclusion of these costs in base rates.

Q. PLEASE DESCRIBE MR. KOLLEN'S PROPOSED ADJUSTMENT TO REDUCE PENSION AND OTHER POST EMPLOYMENT BENEFITS EXPENSE IN THE BUDGET PORTION OF THE BASE YEAR AND IN THE FORECASTED TEST YEAR.

A. Mr. Kollen recommends that the Commission assume his estimate of a normalized pension and other post-employment benefits (OPEB") expense for the entire test year, rather than the Company's forecasted increases as assumed in the base rate case test year. The effect of his adjustment would be a reduction to the employee benefit expense of $0.116 million and to the Company's revenue requirement of approximately $0.116 million.

Q. DO YOU AGREE WITH THIS ADJUSTMENT?

A. No.

Q. PLEASE EXPLAIN.

A. Mr. Kollen is simply attempting to dismiss the Company's ability to forecast its expenses. The only rationale he offers for his recommendation related to OPEB expense is he believes that the forecasted increase in OPEB expenses from 2019 to 2020 "cannot be verified because they are not known and measurable at this time." Mr. Kollen is essentially asserting that this "forecasted" increase in costs should be ignored because it is a forecast. Kentucky statutes provide that utilities are allowed to use a fully forecasted test period for setting base rates. OPEB expenses are just one of many costs that must be "forecasted" for the test period used in such filings. Mr. Kollen's standard of disallowing costs because they are not strictly known and measurable would completely undermine the concept of using a forecasted test period.

Without question parties can debate the reasonableness of the components of a forecasted test period but to say that increases in future costs are not allowed simply because they are not known and measurable would corrupt the entire process of using a forecasted test period.

Q. IS MR. KOLLEN'S VIEW THAT FORECASTED INCREASES SHOULD BE DISALLOWED BECAUSE THEY'RE NOT KNOWN AND MEASURABLE CONSISTENT THROUGHOUT HIS TESTIMONY?

A. No. In another section of his testimony, Mr. Kollen proposes an adjustment to labor expense related to meter reading expense. In making this adjustment, Mr. Kollen reflects a 3 percent increase in labor costs for merit increase "through the end of the test year."[3]

Q. WHAT IS THE BASIS FOR MR. KOLLEN'S ADJUSTMENT?

A. He recommends that the Commission assume that normalized pension and OPEB expense included for the first eight months of the test year will continue for the last four months of the test year and completely disregards the forecast the Company has put forth for the last four months of the test year.

Q. IS THE BASIS FOR MR KOLLEN'S ADJSUTMENT REASONABLE?

A. No. Mr. Kollen states that the monthly amounts increase in December 2019, January 2020 and February 2020 and claims there is no obvious reason why there should be any increase. The Company records their annual vacation accrual in December which causes that month to be higher than other months, but ensures the year is properly stated. Additionally, company matches for certain employee savings plans are front loaded in the beginning of the calendar year causing

[3] Kollen Direct, pg 20, Line 12.

expense in the first three months of the calendar year to be higher. It is necessary to look at the full 12 months of data to ensure the year is properly stated. As outlined in RHM-REBUTTAL-1 Attachment, which shows costs in account 926 by month for both the base and forecasted test periods, the forecasted test period is actually projected to be lower than the base period. This is just another instance where Mr. Kollen is cherry picking data to his advantage.

Q. SHOULD THE COMMISSION ACCEPT MR. KOLLEN'S RECOMMENDATION?

A. Absolutely not. Mr. Kollen's recommendation is based solely on his view that forecasted costs cannot be known and measurable. That position is significantly at odds with Commission precedent and Kentucky law. Because he offers no other reasoned basis for modifying the Company's proposed OPEB expenses, his proposal should be rejected. For whatever reason, Mr. Kollen was okay with this estimated increase and acknowledged in discovery that he "relied on the Company's overall wage increase budget" for making that adjustment.

It is inexplicable that Mr. Kollen is willing to accept some of the Company's forecasted increases and reject others.

Q. PLEASE EXPLAIN MR. KOLLEN'S RECOMMENDATION TO REDUCE EMPLOYEE BENEFITS EXPENSE TO REFLECT INCREASED EMPLOYEE SHARING OF PREMIUMS.

A. Mr. Kollen claims that the Commission's precedent is to provide recovery of medical insurance premiums based on the assumption that the employee pays 21 percent of the premium cost for single coverage and 33 percent of the premium cost for all other types of coverage, to provide recovery of dental insurance premiums based on the assumption that the employees pay 60 percent of the premium cost of coverage, and to provide no recovery for long-term disability insurance premiums. The effect of his proposed adjustment is a reduction in the employee benefits expense of $0.218 million and a reduction of $0.218 million in the revenue requirement.

Q. DO YOU AGREE WITH MR. KOLLEN'S PROPOSED ADJUSTMENTS?

A. No.

Q. PLEASE EXPLAIN.

A. First, Mr. Kollen's claim that recent Commission precedent requires this adjustment is incorrect or at least misleading. Again, the Commission did not make this adjustment as part of the Company's most recent base electric rate case, Case No. 2017-00321, less than a year ago. The Company is not aware of any recent case involving a major investor-owned utility that received an order for such disallowances. Mr. Kollen even acknowledged in discovery that he is unaware of ANY Commission order denying recovery for long-term disability.[4] The health and insurance benefit plans offered to the employees of the Company's electric business are the same as those offered to employees of its natural gas business. Therefore, it makes absolutely no sense to treat them differently and, as Mr. Kollen suggests, the Commission should follow its precedent for how it treated this expense for Duke Energy Kentucky in the past. Second, Mr. Kollen

[4] Response to Company Data Request 34.

has not claimed that the Company's health and insurance benefit plans are unreasonable or inconsistent with the market. He offers no analysis or support for his adjustment other than a blanket statement that the Commission has done this before in reference to two rural electric cooperatives and a water district.[5] Finally, Mr. Kollen's adjustment myopically focuses on just the employee responsibility in terms of the premium and completely ignores the other significant components of cost-sharing of total medical and dental expense, namely what portion of the total cost the employee is obligated to pay through co-pays, deductibles, and the like.

As I explained in my direct testimony, in designing medical and dental plan options and determining employee cost share, Duke Energy focuses on the total cost of coverage – not just the premium (or contributions since medical and dental coverage is self-insured) that is deducted from employees' paychecks. Total cost of coverage includes the additional out-of-pocket costs such as copays, deductibles and co-insurance. Looking at only the premium does not provide the total picture of employees' cost share.

Duke Energy's plans and employee cost sharing are designed to encourage good consumer health care choices by providing opportunities for lower employee premiums and higher out-of-pocket costs at the point of service so that the utilizers of health care services are paying for it. For example, premiums for the high deductible health plan (HDHP) options have higher costs at the point of service, but lower premiums. Alternatively, the preferred provider organization

[5] Kollen Testimony at FN 37.

(PPO) option has lower costs at the point of service and higher premiums. 76 percent of our covered employee population is enrolled in our HDHP options.

Duke Energy employees' total cost of medical coverage (premiums and out-of-pocket costs) for 2018 are projected to be 34 percent, which falls between that of employers in general industry (35 percent) and utility industry (29 percent). For dental coverage, the employee pays on average 35 percent of the premium and 56 percent of the total cost of coverage (premium plus out-of-pocket costs).

Q. WHAT IS YOUR RECOMMENDATION REGARDING MR. KOLLEN'S ADJUSTMENT RELATED TO MEDICAL EXPENSE PREMIUMS.

A. The Commission should reject this adjustment and permit Duke Energy Kentucky to recover all of its costs as it was permitted in its most recent electric base rate case. The insurance programs offered to its gas employees are the same as those offered to its electric employees. The Commission did not make this adjustment in the Company's most recent electric case and has not made this adjustment in any case involving a major investor-owned utility in recent years. There has been no analysis or claim that the Company's medical plan costs are unreasonable or not supported by the market. Finally, adjusting the Company's revenue requirement solely based upon the premium completely ignores the structure of these plans and the overall costs, including other employee medical cost-sharing by way of deductibles, co-pays, and co-insurance which are the patient's responsibility. These other factors determine the plan's total premium and the responsibility of the Company and the individual employee.

Q. PLEASE EXPLAIN MR. KOLLEN'S PROPOSED ADJUSTMENT RELATED TO RESTRICTED STOCK UNITS.

A. Mr. Kollen recommends that the Commission remove approximately $0.285 million in RSU incentive compensation from the test year revenue requirement. Mr. Kollen accurately states that the Commission disallowed these same costs in the Company's most recent electric base rate case and that appears to be his sole basis for recommending the disallowance. However, the Company continues to believe these costs should be eligible for recovery and are not related in any way to the Company's financial performance, but are in fact, a defined benefit amount that is solely tied to retention of high-performing employees.

Q. DO YOU AGREE THAT THE RSU COMPONENT OF COMPENSATION IS IN ANY WAY TIED TO FINANCIAL PERFORMANCE OF THE COMPANY?

A. No. It is factually incorrect to say that the magnitude of the expense for RSU payments is tied in any way to the financial performance of the Company. Employees eligible for RSUs receive a fixed percentage of their base salary that is paid in the form of RSUs. Although other dollar magnitude of incentives paid to employees can vary with the Company's financial performance, the magnitude of RSUs are fixed...whether the Company has a good year financially or a bad year, the expense for RSU payments to eligible employees is unaffected. The primary incentive associated with RSUs is job retention insofar as an employee must remain with the Company for at least three years to receive the full amount of the RSU he or she was awarded. Excluding the cost of RSUs from the Company's revenue requirement would deprive it of the ability to recover the cost of incentivizing employees to remain with the Company. The Company has a legitimate interest in attracting *and retaining* a skilled workforce as this directly benefits customers through the accumulation of experience and knowledge.[6] The RSU program is one way the Company is able to accomplish this objective at a reasonable cost. The problem appears to arise from the fact that the retention bonus is paid in the form of stock and not as cash. If the Company simply paid an employee a cash bonus for remaining with the Company, it is unlikely that the RSUs would have ever become an issue in either the electric rate case or this rate case.

Q. PLEASE EXPLAIN HOW AN RSU, AS A STOCK UNIT, IS NOT TIED TO THE OVERALL FINANCIAL PERFORMANCE OF THE COMPANY.

A. Assume an employee earns $100,000 and that his compensation package includes a provision that he receive RSUs amounting to 30 percent of his base salary. The expense recorded on the Company's books for this RSU payment is $30,000, which would be accrued over the duration of the vesting period. Although the RSU provided to the employee is in the form of stock that may appreciate or depreciate in value, the "expense" to the Company is and will always be $30,000. It is true that the financial performance of the Company may increase or decrease the value of that stock to the employee, once the RSU is given to the employee, the ONLY expense to the Company is $30,000. Consequently, the Company is only asking that the Commission recognize that this RSU expense is independent

[6] *See* Company Response to Staff DR 03-025b.

of the Company's financial performance. Acknowledging that fact eliminates the basis relied upon by the Commission, and reiterated by Mr. Kollen in his testimony, for excluding the RSU expense from the test year revenue requirement.

III. CONCLUSION

Q. WAS ATTACHMENT RHM-1 REBUTTAL PREPARED BY YOU OR AT YOUR DIRECTION AND UNDER YOUR CONTROL?

A. Yes.

Q. DOES THIS CONCLUDE YOUR PRE-FILED REBUTTAL TESTIMONY?

A. Yes.

VERIFICATION

STATE OF NORTH CAROLINA	)	
	)	**SS:**
COUNTY OF MECKLENBURG	)	

The undersigned, Renee Metzler, Managing Director – Retirement and Health and Welfare, being duly sworn, deposes and says that she has personal knowledge of the matters set forth in the foregoing rebuttal testimony and that it is true and correct to the best of her knowledge, information and belief.

Renee Metzler Affiant

Subscribed and sworn to before me by Renee Metzler on this 14th day of January, 2019.

Felicia Sueann Rutty
NOTARY PUBLIC

My Commission Expires:

FELICIA SUEANN RUTTY
NOTARY PUBLIC
MECKLENBURG COUNTY, NC
My Commission Expires 9-17-2023

Duke Energy Kentucky
Case No. 2018-00261
Employee Pensions and Benefits Expense

Base Period

Account	Description	Total	Dec-17	Jan-18	Feb-18	Mar-18	Apr-18	May-18	Jun-18	Jul-18	Aug-18	Sep-18	Oct-18	Nov-18
926000	EMPL PENSIONS AND BENEFITS	1,995,019	605,558	138,845	125,945	150,301	136,037	126,568	136,711	118,733	118,538	101,113	118,310	118,360

Forecasted Period

Account	Description	Total	Apr-19	May-19	Jun-19	Jul-19	Aug-19	Sep-19	Oct-19	Nov-19	Dec-19	Jan-20	Feb-20	Mar-20
926000	EMPL PENSIONS AND BENEFITS	1,604,029	125,532	123,989	144,312	123,152	122,944	106,490	122,698	122,743	174,995	154,002	151,495	131,677

COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

The Electronic Application of Duke Energy Kentucky, Inc., for: 1) An Adjustment of the Natural Gas Rates; 2) Approval of a Decoupling Mechanism; 3) Approval of New Tariffs; and 4) All Other Required Approvals, Waivers, and Relief.	)))))))	Case No. 2018-00261

REBUTTAL TESTIMONY OF

ROGER A. MORIN, Ph.D.

ON BEHALF OF

DUKE ENERGY KENTUCKY, INC.

January 22, 2019

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PAGE

I. INTRODUCTION AND PURPOSE

Q. PLEASE STATE YOUR NAME, ADDRESS, AND OCCUPATION.

A. My name is Mr. Roger A. Morin. My business address is Georgia State University, Robinson College of Business, University Plaza, Atlanta, Georgia, 30303. I am Emeritus Professor of Finance at the College of Business, Georgia State University and was Professor of Finance for Regulated Industry at the Center for the Study of Regulated Industry at Georgia State University. I am also a principal in Utility Research International, an enterprise engaged in regulatory finance and economics consulting to business and government.

Q. DID YOU FILE DIRECT TESTIMONY IN THIS PROCEEDING ON BEHALF OF DUKE ENERGY KENTUCKY, INC., (DUKE ENERGY KENTUCKY OR COMPANY)?

A. Yes, I did.

Q. WHAT IS THE PURPOSE OF YOUR REBUTTAL TESTIMONY?

A. I have been asked to respond to the cost of capital testimony of Mr. Lane Kollen on behalf of the Kentucky Office of The Attorney General.

II. DISCUSSION

A. SUMMARY

Q. PLEASE SUMMARIZE MR. KOLLEN'S RATE OF RETURN RECOMMENDATION.

A. While Mr. Kollen did not perform any independent studies of Duke Energy Kentucky's return on equity (ROE), he nevertheless recommends a ROE of 9.5%

for Duke Energy Kentucky largely based on selective, self-serving restatements of my own ROE studies.

Q. DID MR. KOLLEN INDEPENDENTLY DEVELOP ANY SAMPLES OF COMPARABLE RISK COMPANIES IN ORDER TO ARRIVE AT HIS RECOMMENDATION?

A. No, he did not.

Q. DID MR. KOLLEN PERFORM AN INDEPENDENT DISCOUNTED CASH FLOW (DCF) ANALYSIS IN ORDER TO ARRIVE AT HIS RECOMMENDATION?

A. No, he did not.

Q. DID MR. KOLLEN PERFORM AN INDEPENDENT RISK PREMIUM ANALYSIS IN ORDER TO ARRIVE AT HIS RECOMMENDATION?

A. No, he did not.

Q. DID MR. KOLLEN PERFORM A CAPITAL ASSET PRICING MODEL (CAPM) ANALYSIS IN ORDER TO ARRIVE AT HIS RECOMMENDATION?

A. No, he did not.

Q. HOW THEN DID MR. KOLLEN ARRIVE AT HIS RECOMMENDED ROE OF 9.5%?

A. First, he adopts the midpoint of my own DCF results, 9.80%, but arbitrarily ignores all the results of my other methodologies which range from 9.6% to 10.7%. Second, he removes the flotation cost component of the 9.80% result to arrive at 9.625%. Thirdly, he arbitrarily subtracts 0.125% from the latter result in order to account for the risk-reducing effect of the Company's weather normalization adjustment mechanism (WNA) to arrive at his final recommendation of 9.5%. No support is provided for the 0.125% downward adjustment, and it is literally pulled out of thin air.

Mr. Kollen also alludes to the Commission's consideration of the ROEs allowed by other regulatory commissions. He also insinuates that natural gas utilities are less risky than electric utilities, without providing any evidence for that position.

I shall now rebut each of Mr. Kollen's viewpoints expressed above.

B. USE OF MULTIPLE METHODS

Q. SHOULD THE COMMISSION RELY EXCLUSIVELY ON THE DCF AS MR. KOLLEN SUGGESTS?

A. No, it should not. No one single method provides the necessary level of precision for determining a fair return, but each method provides useful evidence to facilitate the exercise of an informed judgment. Reliance on any single method or preset formula is inappropriate when dealing with investor expectations because of possible measurement difficulties and vagaries in individual companies' market data. The advantage of using several different approaches is that the results of each one can be used to check the others.

As a general proposition, it is extremely dangerous to rely on only one generic methodology to estimate equity costs. Hence, several methodologies applied to several comparable risk companies should be employed to estimate the cost of common equity.

There are three broad generic methods available to measure the cost of equity: DCF, CAPM, and risk premium. All three of these methods are accepted and used by the financial community and firmly supported in the financial literature. The weight accorded to any one method may vary depending on unusual circumstances in capital market conditions.

Each methodology requires the exercise of considerable judgment on the reasonableness of the assumptions underlying the method and on the reasonableness of the proxies used to validate the theory and apply the method. Each method has its own way of examining investor behavior, its own premises, and its own set of simplifications of reality. Investors do not necessarily subscribe to any one method, nor does the stock price reflect the application of any one single method by the price-setting investor. There is no guarantee that a single DCF result is necessarily the ideal predictor of the stock price and of the cost of equity reflected in that price, just as there is no guarantee that a single CAPM or risk premium result constitutes the perfect explanation of a stock's price or the cost of equity.

Mr. Kollen's deviation from the industry standard puts him on the fringe of valuation professionals, demonstrates an unseemly degree of intellectual torpidity and undercuts the credibility of his conclusions. In short, the Commission should consider all the relevant evidence presented.

C. ALLOWED RETURNS

Q. DR. MORIN, CAN YOU PLEASE COMMENT ON MR. KOLLEN'S SUGGESTION THAT THE COMMISSION SHOULD CONSIDER THE ROEs CURRENTLY ALLOWED BY OTHER REGULATORS?

A. Yes, I can. My first reaction is that it is circular to set a fair return based on the past actions of other regulators, much like observing a series of duplicate images in multiple mirrors. The rates of return earned by other regulated utilities may very well have been reasonable under historical conditions, but they are still subject to tests of reasonableness under current and prospective conditions. I believe each regulator should have a mind of its own.

My second reaction is that the average authorized ROE in a given time period is just that, an average. There are large deviations both above and below the average authorized return presumably due to risk differences between utilities. For example, in the first three quarters of 2018 there were 37 electric ROE decisions reported in RRA's annual compilation of regulatory awards averaging 9.6%[1]. The authorized ROEs varied from 8.6% to 11.2%, with 13 of the 37 decisions higher than the average. The same is true for natural gas utility decisions where there were 27 ROE decisions averaging 9.6% with the authorized ROEs varying from 8.8% to 10.2%, with 9 of the 27 decisions higher than the average. The major point of all this is that regulators do and should take risk into account when authorizing ROEs as attested by the variability in the allowed ROE data, and I strongly believe that the Commission should follow suit and exercise a mind of its own when authorizing ROEs.

[1] *See* S&P Global Intelligence "RRA Regulatory Focus Major Rate Case Decisions – January – September 2018"

D. FLOTATION COSTS

Q. WHAT FLOTATION COST TREATMENT DID MR. KOLLEN RECOMMEND IN THIS CASE?

A. Mr. Kollen's ROE recommendation is based in part on the elimination of the flotation component of my DCF results, and as a result he does not include any allowance for issuance expense. Because Mr. Kollen fails to include any allowance for flotation costs, his DCF estimates of equity costs are understated by 20 basis points, as shown in Appendix A of my direct testimony.

I am surprised by Mr. Kollen's reluctance to accept flotation costs. Obviously, common equity capital is not free. The flotation cost allowance to the cost of common equity capital is routinely discussed and applied in most corporate finance textbooks.

Mr. Kollen's disregard of flotation costs is inconsistent with Value Line data on historical and projected common stock issues. Electric and natural gas utilities have, and will continue to be issuing new common stock in the future.

Q. HOW DOES MR. KOLLEN JUSTIFY HIS DISMISSAL OF FLOTATION COST?

A. He does not provide any conceptual, academic, supportive evidence, or practical reasons as to his dismissal. It is simply a gimmick to arrive at a lower overall ROE.

Q. IN YOUR DIRECT TESTIMONY, YOU STATED THAT THE RETURN ON EQUITY SHOULD BE ADJUSTED TO INCLUDE AN ALLOWANCE FOR FLOTATION COSTS. PLEASE COMMENT ON FLOTATION COSTS.

A. Flotation costs are very similar to the closing costs on a home mortgage. In the case of issues of new equity, flotation costs represent the discounts that must be provided to place the new securities. Flotation costs have a direct and an indirect component. The direct component represents monetary compensation to the security underwriter for marketing/consulting services, for the risks involved in distributing the issue, and for any operating expenses associated with the issue (printing, legal, prospectus, etc.). The indirect component represents the downward pressure on the stock price as a result of the increased supply of stock from the new issue. The latter component is frequently referred to as "market pressure."

Flotation costs for common stock are analogous to the flotation costs associated with past bond issues which, as a matter of routine regulatory policy, continue to be amortized over the life of the bond, even though no new bond issues are contemplated. In the case of common stock, which has no finite life, flotation costs are not amortized. Therefore, the recovery of flotation cost requires an upward adjustment to the allowed return on equity.

E. ROE ADJUSTMENT FOR WEATHER NORMALIZATION

Q. DO YOU AGREE THAT IT WOULD BE APPROPRIATE FOR THE COMMISSION TO RECOGNIZE THE RISK REDUCING ATTRIBUTES OF THE WNA AND ALLOW A ROE REDUCTION OF 0.125% (12.5 BASIS POINTS)?

A. I strongly disagree with that position. First, Mr. Kollen does not provide any basis for, nor does he offer any evidence whatsoever on, the 0.125% downward ROE adjustment. As with several of his other recommendations, it is literally plucked out of thin air.

Second, the ROE in this case is being set using a proxy group to establish Duke Energy Kentucky's cost of equity. To the extent that companies in that group have risk-mitigating mechanisms such as the WNA, the use of the proxy group takes them into account and the addition of any adjustment would be an unwarranted double counting effect. As a matter of fact, most of the natural gas utilities in the peer group already have such a weather normalization adjustment. Moreover, most of the electric utilities in the peer group have various risk-mitigating mechanisms such as the WNA.

Q. HOW PREVALENT ARE RISK-MITIGATING MECHANISMS IN THE UTILITY INDUSTRY?

A. Risk-mitigating mechanisms such as WNA and fuel adjustment clauses have become the norm for regulated energy utilities across the U.S.

While risk-mitigating mechanisms reduce risk on an absolute basis, they do not necessarily do so on a relative basis, that is, compared to other utilities. For example, a fuel adjustment clause does not reduce relative risk since most electric utilities in the industry already possess such a clause. The approval of adjustment clauses, ROE incentive riders, trackers, forward test years, and cost recovery mechanisms by regulatory commissions is widespread in the utility business and is already largely embedded in financial data, such as stock prices, bond rating and business risk scores.

Moreover, while adjustment clauses, riders, and cost tracking mechanisms may mitigate (on an absolute basis but not on a relative basis) a portion of the risk and uncertainty related to the day-to-day operations, there are other significant factors to consider that work in the reverse direction, for example declining customer energy usage, and the Company's significant capital spending program requiring external financing, none of which were considered by Mr. Kollen.

Q. DID MR. KOLLEN CONSIDER ANY OF THESE RISKS?

A. He certainly did not mention them in his testimony. Whether he is unaware of these risks or purposefully choose to ignore them because they are unhelpful to his cause is unknown. While he seeks to point out - incorrectly, I might add - the risk-reducing impact of the WNA, he inexplicably does not consider the factors that increase risk. Such a faulty analytical method is wholly inconsistent with the academic literature and best practices of professionals who undertake this type of work on a daily basis.

In my direct testimony, I described my recommended return as conservative for two reasons. The first reason is the small relative size of the Company's natural gas business. Duke Energy Kentucky's natural gas distribution business is small relative to that of its peer companies on the basis of revenues, capital base, and number of customers. Investment risk increases as company size diminishes, all else remaining constant. The second reason is that the Company is very likely to raise very large sums of money in a rising interest rate environment over the next five years. Because of the Company's very large construction program relative to its rate base and owners' capital (common equity balance) over the next few years, rate relief requirements and regulatory treatment uncertainty will increase regulatory risks as well. Mr. Kollen did not consider these two elements of added risk in arriving at his recommendation.

Q. IS THERE ANY EMPIRICAL EVIDENCE ON THE IMPACT OF RISK MITIGATORS?

A. Yes, there is. A recent comprehensive study by the Brattle Group[2] investigated the impact of a particular risk-mitigating mechanism on risk and the cost of capital and found that its effect on risk and cost of capital, if any, is undetectable statistically.

Q. DR. MORIN, ARE YOU AWARE OF ANY REGULATORY COMMISSION REDUCING THE ALLOWED ROE IN ORDER TO ACCOUNT FOR THE PRESENCE OF A RISK-REDUCING MECHANISM SUCH AS THE WNA IN RECENT YEARS?

A. No, I am not. To the best of my knowledge, not since 2012 has a regulatory commission applied such a downward return adjustment. Mr. Kollen conceded the point in his own response to Staff's Request for Information to the Attorney General, No. 7.[3]

Q. HAS MR. KOLLEN PRESENTED ANY ARGUMENTS IN HIS TESTIMONY THAT WOULD CAUSE YOU TO ALTER ANY OF YOUR RECOMMENDATIONS AND METHODOLOGIES?

A. No, he has not. His faulty methodologies and self-serving assumptions severely limit the weight which his testimony should be given.

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[2] Wharton, Vilbert, Goldberg & Brown, *The Impact of Decoupling on the Cost of Capital: An Empirical Investigation*, The Brattle Group, February 2011.
[3] Attachment RAM-REBUTTAL-1

III. <u>CONCLUSION</u>

Q. WHAT DO YOU CONCLUDE FROM MR. KOLLEN'S COST OF CAPITAL TESTIMONY?

A. Given the extremely limited scope of the ROE component of his testimony which is limited to three pages, I find that the portion of Mr. Kollen's testimony dealing with the ROE issue lacks any support, rational, empirical or otherwise and should be disregarded.

Q. DOES THIS COMPLETE YOUR REBUTTAL TESTIMONY?

A. Yes, it does.

VERIFICATION

STATE OF FLORIDA)
) **SS:**
COUNTY OF NASSAU

The undersigned, Dr. Roger A. Morin, Professor of Finance and a Principal in Utility Research International, being duly sworn, deposes and says that he has personal knowledge of the matters set forth in the foregoing rebuttal testimony and that it is true and correct to the best of his knowledge, information and belief.

Roger A. Morin

Dr. Roger A. Morin Affiant

Subscribed and sworn to before me by Dr. Roger A. Morin on this 9th day of January 2019.

Karen M. Taylor

NOTARY PUBLIC

My Commission Expires: Nov. 16. 2021

KAREN M. TAYLOR
Notary Public – State of Florida
Commission # GG 161184
My Comm. Expires Nov 16, 2021
Bonded through National Notary Assn.

The Electronic Application Of Duke Energy Kentucky, Inc. For: 1) An Adjustment Of The Natural Gas Rates; 2) Approval of a Decoupling Mechanism; 3) Approval Of New Tariffs; and 4) All Other Required Approvals, Waivers, And Relief
Case No. 2018-00261
Attorney General's Responses to Data Requests of Kentucky Public Service Commission Staff

WITNESS/RESPONDENT RESPONSIBLE:
Lane Kollen
Page 1 of 1

QUESTION No. 7

Refer to the Kollen testimony, page 38, lines 11–12.

a. Provide support for the 0.125 percent reduction in the model ROE midpoint of 9.625 percent.
b. Provide examples of other state Commissions where the ROE was reduced by 0.125 percent, or by any other percent, due to the presence of a weather normalization clause.

RESPONSE:

a. The 0.125 percent was simply a modest reduction to reflect the reduction in business and regulatory risk resulting from a WNA rider.
b. Mr. Kollen has not researched this issue, but it is consistent with Dr. Morin's recommendation to increase his proposed return on equity if the Commission does not adopt the proposed WNA clause.

COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

The Electronic Application of Duke Energy Kentucky, Inc., for: 1) An Adjustment of the Natural Gas Rates; 2) Approval of a Decoupling Mechanism; 3) Approval of New Tariffs; and 4) All Other Required Approvals, Waivers, and Relief.	)))))))	Case No. 2018-00261

REBUTTAL TESTIMONY OF

BRUCE L. SAILERS

ON BEHALF OF

DUKE ENERGY KENTUCKY, INC.

January 22, 2019

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PAGE

I. INTRODUCTION AND PURPOSE

Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

A. My name is Bruce L. Sailers. My business address is 139 East Fourth Street, Cincinnati, Ohio 45202.

Q. BY WHOM ARE YOU EMPLOYED AND IN WHAT CAPACITY?

A. I am employed by Duke Energy Business Services LLC (DEBS), as Pricing and Regulatory Solutions Manager. DEBS provides various administrative and other services to Duke Energy Kentucky, Inc., (Duke Energy Kentucky or Company) and other affiliated companies of Duke Energy Corporation (Duke Energy).

Q. ARE YOU THE SAME BRUCE SAILERS THAT SUBMITTED DIRECT TESTIMONY IN THIS PROCEEDING?

A. Yes.

Q. WHAT IS THE PURPOSE OF YOUR REBUTTAL TESTIMONY?

A. The purpose of my rebuttal testimony is to respond to an opinion and recommendation expressed by witness Lane Kollen on behalf of the Kentucky Attorney General (AG). Specifically, I address Mr. Kollen's recommendation concerning the revenues he describes as transportation revenues in his testimony on page 13 line 12 through page 15 Line 4. Specifically, the revenues Mr. Kollen references are Rate IT, Interruptible Transportation, revenues.

II. DISCUSSION

Q. WHAT DOES ATTORNEY GENERAL WITNESS KOLLEN STATE AND RECOMMEND RELATED TO INTERRUPTIBLE TRANSPORTATION REVENUES?

A. Mr. Kollen states "The Company included forecast transportation revenues of $1.405 million in the test year. The forecast for the test year is less than the $1.501 million that the Company reflected in the base period." Mr. Kollen sourced these values from Company's response to data requests AG-DR-01-041 and STAFF-DR-01-071 which provide information from the Company's revenue requirements calculation. Further, Mr. Kollen states "I recommend that the Commission use the $1.571 million actual transportation revenues recorded for calendar year 2017." Mr. Kollen then incorrectly suggests that the Company's proposed rate increase be reduced by $166,000, which is the difference between $1.405 million he mistakenly believes is included in the forecast test year and the $1.571 million he believes should be included in the test year.

Q. DO YOU AGREE WITH HIS STATEMENTS AND RECOMMENDATION?

A. No.

Q. PLEASE EXPLAIN.

A. First, Mr. Kollen opportunistically singles out one component of forecasted test year revenue while excluding the other components. More specifically, he recommends adjusting the revenue for Interruptible Transportation, likely because it reduces the proposed rate increase, but ignores similar updates for Firm Transportation, likely because it could increase the Company's overall rate increase. Secondly, and more importantly, Mr. Kollen does not appear to understand how these revenues flow through the revenue requirement calculations. Duke Energy Kentucky's projection of Rate IT revenues should be referenced from Schedule M. Schedule M is the ultimate source of the starting revenue in a rate case model. In this schedule, revenues are calculated using projected billing determinates and applying rates. Because this is a more precise method for projecting revenue than the methodology used for producing the Company's budget (which are the figures being referenced by Mr. Kollen), an adjustment is made in Schedule D-2.25 to reconcile the Schedule M detailed calculation of revenue with the amounts reflected in the budget and shown in the revenue requirements model. The values referenced by Mr. Kollen are not the Company's projected revenue for Rate IT that is actually included in the revenue requirement analysis. Consequently, the Commission should not accept Mr. Kollen's recommendation.

Q. WHAT ARE THE BASE REVENUES INCLUDED IN THE COMPANY'S TEST YEAR AT CURRENT RATES?

A. On Duke Energy Kentucky's Schedule M-2.2, page 7 of 7, line 10, total test year base revenue for Rate IT using current rates is $1.524 million. This is the amount of base revenue for Rate IT that is included in the test year, before any increase. Because Mr. Kollen appears to be unaware that Schedule M-2.2 is the amount included in the test year at current rates, he mistakenly assumes that the Company only included $1.405 million.

Q. PLEASE DESCRIBE SCHEDULE M.

A. Schedule M is a one page, side-by-side comparison of Duke Energy Kentucky's forecasted test year revenues at current and proposed rates. Schedule M is based upon base rates which include the gas cost adjustment clause and other riders.

Q. PLEASE DESCRIBE SCHEDULES M-2.2 AND M-2.3.

A. Schedule M-2.2, page 1 of 7, shows the forecasted test year bills in summary form, base revenues under current rates, current total revenues, and proposed base revenue increases, all broken down by rate and revenue class. The billing determinants used on these schedules are normalized sales for the twelve months ended March 31, 2020. Schedule M-2.2, pages 2 through 7, contains a detailed calculation of forecasted test year numbers using current rates as well as the proposed revenue increase, by rate and revenue class, as summarized on Schedule M-2.2, page 1. Schedule M-2.3 is almost identical to M-2.2, page 1, except that it shows the revenue summary and detailed data calculated at the rates proposed in this case. These schedules are integral to the ratemaking process as using billing determinates multiplied by proposed rates is the way the Commission can confirm that the rates are producing the revenue being approved in the case. In a similar manner, the billing determinates multiplied by current rates is the starting point for determining the amount of revenue that would be collected at "current" rates. It follows then, that the difference between these two calculations is the amount of the overall base revenue increase.

Q. HOW DOES THE COMPANY'S REVENUE REQUIREMENT CALCULATION UTILIZE SCHEDULE M?

A. Duke Energy Kentucky's operating revenue used in the calculation of its revenue requirement, as shown on Schedule C-2.1, is forced to match the revenue calculated on Schedule M through an adjustment on Schedule D-2.25. This adjustment is made because the revenue calculated on Schedule M is more accurate than the revenue from the Company's forecast since it uses the most current tariff rates applied to the forecasted billing determinants rather than average realizations which are used in preparing the Company's forecasted revenue.

Q. DOES MR. KOLLEN UNDERSTAND HOW SCHEDULE M IS USED TO CALCULATE THE COMPANYS REVENUE REQUIREMENT?

A. No. Mr. Kollen states in his response to Duke Energy Kentucky's data request number 21 to the AG that Schedule M should not be used as a source for projected revenue. This data request is provided for convenience as attachment BLS-REBUTTAL-1. However, it is not accurate to state that the Company's revenue at current and proposed rates is not best represented by Schedule M. As described above, the revenue calculated on Schedule M is more precise than the revenue shown on Schedule C-2.1 of the Company's revenue requirement model and the Company's revenue requirement model is therefore adjusted via Schedule D-2.25 as discussed above. As such, Mr. Kollen's recommended reduction to the Company's requested rate increase of $166,000 should be disregarded as it is based on incomplete data and ignores the methodology that is used to determine the

Company's overall revenue requirement. Mr. Kollen's recommendation amounts to a change to the Company's modeling as it relates to a single rate schedule to the exclusion of all other rate schedules.

Q. DO YOU HAVE ANY OTHER CONCERNS WITH MR. KOLLEN'S PROPOSAL TO SUBSTITUTE HIS CALCULATION OF PROJECTED REVENUE AT CURRENT RATES FOR THE AMOUNT INCLUDED IN THE COMPANY'S APPLICATION?

A. Yes. Mr. Kollen includes the Company's response to AG-DR-01-041 as support for his proposed starting revenue. Although the Company provided data for all of calendar years 2015, 2016, and 2017, Mr. Kollen chose to use only the information for the calendar year that resulted in a number most favorable to his position. The total base revenue from Rate IT for 2015 was $1.380 million; for 2016, it was $1.499 million; and for 2017 it was $1.571 million. The average for those three calendar years was $1.483 million.

As I discussed above, the amount of base revenue for Rate IT that the Company actually included in the test year was $1.524 million. So, if the Commission chooses to update that figure for the information provided in AG-DR-01-041, it should use all the data provided, *i.e.*, the average of the three years. Doing so demonstrates the Company already represents an increase in Rate IT base rate revenues of $41,000 (*i.e.*, $1.524 million, which is the actual base revenue from Rate IT at current rates included in the Company's application, compared to $1.483 million, which is the average base revenue from Rate IT over the last three years).

Q. IS THE COMPANY REQUESTING THAT THE COMMISSION MAKE AN UPDATE TO RATE IT BASE REVENUES?

A. No. The Company is not requesting to update the base revenue from Rate IT at current rates already included in the model. However, as I have demonstrated above, Mr. Kollen's adjustment is inaccurate, reflects a misunderstanding of how the overall revenue requirement calculation works, and reflects a bias in ignoring all the data that was provided to the Attorney General.

III. <u>CONCLUSION</u>

Q. IS ATTACHMENT BLS-REBUTTAL-1 A TRUE AND ACCURATE COPY OF MR. KOLLEN'S RESPONSE TO THE COMPANY'S DATA REQUEST 21 TO THE ATTORNEY GENERAL?

A. Yes.

Q. DOES THIS CONCLUDE YOUR REBUTTAL TESTIMONY?

A. Yes.

VERIFICATION

STATE OF OHIO	**)**	
	)	**SS:**
COUNTY OF HAMILTON	**)**	

The undersigned, Bruce L. Sailers, Pricing and Regulatory Solutions Manager, being duly sworn, deposes and says that he has personal knowledge of the matters set forth in the foregoing rebuttal testimony and that it is true and correct to the best of his knowledge, information and belief.

Bruce L. Sailers

Bruce L. Sailers, Affiant

Subscribed and sworn to before me by Bruce L. Sailers, on this 22nd day of January, 2019.

NOTARIAL SEAL STATE OF OHIO

ADELE M. FRISCH
Notary Public, State of Ohio
My Commission Expires 01-05-2024

Adele M. Frisch

NOTARY PUBLIC

My Commission Expires: 1/5/2024

The Electronic Application Of Duke Energy Kentucky, Inc. For: 1) An Adjustment
Of The Natural Gas Rates; 2) Approval of a Decoupling Mechanism; 3) Approval Of New Tariffs;
and 4) All Other Required Approvals, Waivers, And Relief
Case No. 2018-00261
Attorney General's Responses to DEK's Data Requests

WITNESS/RESPONDENT RESPONSIBLE:
Lane Kollen
Page 1 of 1

QUESTION No. 21
Mr. Kollen states, on page 13 line 16 of his testimony, "[t]he Company included forecast transportation revenues of $1.405 million in the test year."

(a) Does Mr. Kollen agree that test year revenue projections should be sourced from Schedule M?

(h) Does Mr. Kollen know if the revenue value he states of $1 .405 million contains the same components of revenues that are included in the other revenue values Mr. Kollen states in his testimony on page 13 lines 17 through 19?

(c) Does Mr. Kollen agree that the $1.405 million revenue value is associated with interruptible transportation only?

RESPONSE:

(a) No. The Company's calculations of the revenue requirement and deficiency, including the relevant schedules, workpapers, and calculations, are detailed in the Excel workbook provided in response to Staff 1-71, which does not include Schedule M. These workpapers and calculations include the base year and test year data. The $1.405 million in forecast transportation revenues addressed by Mr. Kollen was the amount included by the Company in account 689000 *Transportation Gas of Others* shown on the FP Rev by Product tab in that Excel workbook. This was the account referenced in AG 1-041 cited by Mr. Kollen and provided as his Exhibit___(LK-4).

(b) Mr. Kollen relied on the Company's Excel workbook and the cited responses to discovery.

(c) Mr. Kollen neither agrees nor disagrees. The Company has other revenue accounts that include an "IC" designation, which he understands refers to interruptible customers. This account does not have an "IC" designation.

COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

The Electronic Application of Duke Energy Kentucky, Inc., for: 1) An Adjustment of the Natural Gas Rates; 2) Approval of a Decoupling Mechanism; 3) Approval of New Tariffs; and 4) All Other Required Approvals, Waivers, and Relief.	)))))))	Case No. 2018-00261

REBUTTAL TESTIMONY OF

JOHN L. SULLIVAN, III

ON BEHALF OF

DUKE ENERGY KENTUCKY, INC.

January 22, 2019

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I. <u>INTRODUCTION AND PURPOSE</u>

Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

A. My name is John L. Sullivan, III, and my business address is 550 South Tryon Street, Charlotte, North Carolina 28202.

Q. BY WHOM ARE YOU EMPLOYED AND IN WHAT CAPACITY?

A. I am employed by Duke Energy Business Services LLC (DEBS) as Director, Corporate Finance and Assistant Treasurer. I am also the Assistant Treasurer of Duke Energy Kentucky, Inc. (Duke Energy Kentucky or the Company). DEBS provides various administrative and other services to Duke Energy Kentucky and other affiliated companies of Duke Energy Corporation (Duke Energy).

Q. PLEASE BRIEFLY SUMMARIZE YOUR EDUCATION AND PROFESSIONAL EXPERIENCE.

I received a Bachelor of Arts degree from the University of North Carolina-Chapel Hill in 1995 and an MBA degree from Wake Forest University in 2000. From 2000 to 2009, I worked in Bank of America's Global Corporate & Investment Banking unit, providing corporate finance, capital markets and strategic advisory services to energy and power clients. In 2009, I joined Duke Energy as a General Manager in the Treasury group. In 2010, I moved to Duke Energy's Corporate Development group where I served as a Director responsible for managing various strategic transactions for the company's regulated and commercial businesses. In January 2016, I returned to Duke Energy's Treasury department and assumed my current role.

Q. PLEASE SUMMARIZE YOUR RESPONSIBILITIES AS DIRECTOR, CORPORATE FINANCE AND ASSISTANT TREASURER.

A. I am responsible for financing the operations of Duke Energy and its subsidiary utilities. This includes the issuance of new debt and equity securities, and obtaining other sources of external funds. My responsibilities also include financial risk management for Duke Energy and its subsidiaries. Additionally, I maintain relationships with Duke Energy's commercial banks, the fixed income investor community and the credit rating agencies.

Q. HAVE YOU PREVIOUSLY PROVIDED TESTIMONY BEFORE THE KENTUCKY PUBLIC SERVICE COMMISSION?

A. Yes. I last provided written testimony in support of Duke Energy Kentucky's base electric rate case application in Case No. 2017-00321.

Q. WHAT IS THE PURPOSE OF YOUR REBUTTAL TESTIMONY?

A. The purpose of my Rebuttal Testimony is twofold. First, I am adopting the Direct Testimony, Filing Requirements, and corresponding data requests sponsored by Robert H. "Beau" Pratt in these proceedings that relate to the Company's financial metrics, including financial objectives, capital structure, cost of capital, credit ratings and forecasted capital needs. More specifically, I am adopting pages 4 through the top of 14 and sponsoring Schedules J-1 through J-4 in response to Filing Requirement (FR) 16(8)(j). I also sponsor FR 12(2)(a), FR 12(2)(b), FR 12(2)(c), FR 12(2)(d), FR 12(2)(e), FR 12(2)(f), FR 12(2)(g), FR 12(2)(h), FR 16(7)(j), FR 16(7)(l) and FR 16(7)(r). In response to FR(16(8)(k), I sponsor the percentage of construction expenditures financed internally, fixed coverage ratios and the rating agencies' ratings in Schedule K. I also provided information relating to consolidated capital structure and common stock related data to Mr. Covington and Ms. Lee for their use in preparing Schedule K. Mr. Pratt is no longer with Duke Energy.

Second, I respond to the recommendation of Attorney General Witness, Lane Kollen's recommendation IV A., to reduce the Company's cost of Long-term Debt to Reflect Actual Cost of 2018 Issuances.

II. ADOPTION OF TESTIMONY

Q. ARE YOU FAMILIAR WITH THE TESTIMONY SUBMITTED BY MR. ROBERT H. "BEAU" PRATT IN THESE PROCEEDINGS AND THE FILING REQUIREMENTS AND DATA REQUEST RESPONSES HE SPONSORED THAT RELATE TO THE COMPANY'S FINANCIAL METRICS, INCLUDING FINANCIAL OBJECTIVES, CAPITAL STRUCTURE, COST OF CAPITAL, CREDIT RATINGS AND FORECASTED CAPITAL NEEDS?

A. Yes.

Q. DO YOU HAVE ANY CHANGES, OR CORRECTIONS TO THAT INFORMATION?

A. No.

Q. AS DIRECTOR, CORPORATE FINANCE AND ASSISTANT TREASURER, DO YOU HEREBY ADOPT THE DIRECT TESTIMONY OF ROBERT H. "BEAU" PRATT FILED IN THIS PROCEEDING AS YOUR OWN?

A. Yes.

III. DUKE ENERGY KENTUCKY'S OBJECTIONS TO MR. KOLLEN'S TESTIMONY

Q. PLEASE DESCRIBE MR. KOLLEN'S RECOMMENDATION TO REDUCE THE COMPANY'S COST OF LONG-TERM DEBT TO REFLECT ACTUAL COST OF 2018 ISSUANCES.

A. Mr. Kollen recommends that the Commission adopt the Company's actual and revised long-term debt rate of 4.36 percent instead of the forecasted 4.398 percent. The result of this recommendation is a reduction to the Company's test year revenue requirement of approximately $.050 million.

Q. PLEASE EXPLAIN WHY DUKE ENERGY KENTUCKY DISAGREES WITH THIS RECOMMENDATION.

A. The long-term debt rate as contained in the Company's application was reasonable. Mr. Kollen's recommendation to adjust this one single item for a reduction in cost is opportunistic and is to the exclusion of all other items in the Company's test year revenue requirement that may have increased. Duke Energy Kentucky is not permitted to update all of the elements of its revenue requirement to reflect actual results. The purpose of a forecasted test year is to project what the Company's revenue requirement is likely to be. It is unfair and unreasonable to single out one component of the revenue requirement that may have been lower than expected without consideration of all other components that may have increased.

Mr. Kollen has not claimed that the Company's forecasted long-term debt rate of 4.398 percent as contained in its Application is unreasonable, nor has he alleged that the Company's methodology for forecasting the long-term debt rate was somehow unreasonable. He is merely selecting one component that would reduce the Company's revenue requirement by updating it for a post-filing change that has occurred to reflect an actual cost rate to the exclusion of all other items that may have increased the Company's revenue requirement. Such a position is contrary to the very purpose of a forecasted test year allowed under Kentucky Law. The Commission should not adopt Mr. Kollen's recommendation, especially in isolation and without consideration of all other changes in variables that may have increased the Company's revenue requirement.

IV. CONCLUSION

Q. DOES THIS CONCLUDE YOUR REBUTTAL TESTIMONY?

A. Yes.

VERIFICATION

STATE OF NORTH CAROLINA)
) **SS:**
COUNTY OF MECKLENBURG)

The undersigned, John L. Sullivan, III, Director, Corporate Finance, being duly sworn, deposes and says that he has personal knowledge of the matters set forth in the foregoing testimony and that it is true and correct to the best of his knowledge, information and belief.

John L. Sullivan III

John L. Sullivan, III Affiant

Subscribed and sworn to before me by John L. Sullivan, III on this 11 day of January, 2019.

HEATHER PAIGE BLUM NOTARY PUBLIC MECKLENBURG COUNTY, N.C.

Heather Paige Blum

NOTARY PUBLIC

My Commission Expires: 1/9/2023