

**Louisville Gas and Electric Company /
Kentucky Utilities Company
Case Nos. 2018-00295 / 2018-00294**

**United States Department of Defense and All Other Federal Executive Agencies'
Responses to Kentucky Utilities Company and
Louisville Gas and Electric Company's First Set of Data Requests**

Mr. Selecky

Data Request No. 1:

Provide copies of all electronic files in native format with formulas intact used in your analysis. This includes copies of all work papers supporting your testimony, analyses, and conclusions.

Response:

Copies of all electronic files and work papers are provided in KU-LGE DR1 DOD-FEA Q1 Attach 1

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Mr. Selecky

Data Request No. 2:

Provide a list of all utilities and case numbers where a state regulatory commission has issued orders approving a six CP methodology for allocating fixed production costs.

Response:

Several regulatory commissions utilize the CP method to allocate fixed production costs. The number of monthly peaks used varies from 1 to 12. The Indiana Utility Regulatory Commission in I&M rate cases approved the use of the 6 CP methodology to allocate fixed production costs in Cause Nos. 39314 and 44075.

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Mr. Walters

Data Request No. 3:

Provide copies of all electronic files in native format with formulas intact used in your analysis. This includes copies of all work papers supporting your testimony, analyses, and conclusions.

Response:

The requested items were previously supplied to the Companies on January 25, 2019.

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Mr. Walters

Data Request No. 4:

At page 5, line 3, Mr. Walters indicates that “[t]he industry average authorized ROE is inflated by certain outlier ROEs that are much higher than the rest of the industry.”

- a. Please identify all such “outlier” results supporting this statement.
- b. Please indicate the basis on which Mr. Walters determined that these values were “outliers,” and include copies of all work papers or supporting documents.
- c. Did Mr. Walter’s identify any outliers that were much lower than the rest of the industry? If so, please identify any such values.
- d. If the answer to subpart (3c) is “no,” please explain why, in Mr. Walter’s view, it is appropriate to remove values that are “much higher” without also removing values that are much lower.

Response:

- a. A review of the Table 1 being discussed in the particular portion of Mr. Walters’ testimony will show that the Average ROE for 2017 is 7 basis points higher than the median. This is indicative of high-end outlier results. A review of the underlying data would show that included in the average of 9.67% is a decision in Alaska that awarded an ROE of 11.95%, which is 228 basis point above the average and 235 basis point above the median.
- b. See the response to (a) above.
- c. Please see the response to (a) above.
- d. This question mischaracterizes Mr. Walters’ testimony. The outlier result identified in (a) above was not removed from the figures shown in Table 1.

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Mr. Walters

Data Request No. 5:

Please provide a copy of the document referenced in footnotes 1, 2, 3 to Mr. Walter's testimony.

Response:

The requested items were previously supplied to the Companies on January 25, 2019.

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Mr. Walters

Data Request No. 6:

At page 12, lines 11-12, Mr. Walter’s indicates that “the Federal Reserve actions on short-term interest rates and unwinding its balance sheet have not resulted in material increases in long-term interest rates.”

- a. Please identify the time period underlying Mr. Walter’s statement, including copies of all work papers or source documents supporting this statement.
- b. Please identify and describe the standard for “material,” as used by Mr. Walters.
- c. Please identify the specific bond securities or indices, including their maturity, that Mr. Walter’s is referring to in the referenced statement.

Response:

- a. Please refer to Figure 2 on page 11 of Mr. Walters’ direct testimony. Furthermore, the requested items were previously supplied to the Companies on January 25, 2019.
- b. The term “material” was not based on a standard, per se. Rather, it was based on the clear observation of the nine increases in the target Federal Funds rate has increased from a midpoint of 0.125% to 2.375% (which is 19x higher than 0.125%). Relative to the 9 increases in the Federal Funds rate, as shown on Figure 2 of Mr. Walters’ testimony, Treasury yields have traded within a range of approximately 2.25% and 3.50% since July 2015 and, as shown on that graph practically unchanged from July 2015 vs December 2018. Similarly, A-rated utility bond yields have traded within a range of 3.50% and 4.50% and, as shown on that graph practically unchanged from July 2015 vs December 2018.
- c. Please see the responses above, as well as Figure 2 on page 11 of his testimony.

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Mr. Walters

Data Request No. 7:

Reference page 16, lines 16-20.

- a. Please provide a complete explanation for Mr. Walter's contention that Avangrid should be eliminated from the proxy group because "80% of its stock is owned by its ultimate parent company." Please include copies of all work papers or source documents supporting the response.
- b. Please identify and explain what is referred to as "investor-required premiums."
- c. Does Mr. Walter's have any quantitative evidence demonstrating the existence of such "investors-required premiums?" If so, please provide copies of all such evidence and supporting work papers.

Response:

- a. Please see pages 16-17 of Mr. Walters' testimony. Furthermore, the requested items were previously supplied to the Companies on January 25, 2019.
- b. Mr. Walters has not identified specific investor required premiums. However, given that less than 20% of Avangrid's stock is available to the investing public, investors could potentially be pricing in premiums lack of liquidity, lack of the ability to influence who sits on the board.
- c. Mr. Walters does not have quantitative evidence of such premiums.

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Mr. Walters

Data Request No. 8:

Please provide a complete explanation for Mr. Walter's contention that being "headquartered in Canada" or a "Canada-based company" warrants excluding a company from the proxy group. As part of this explanation:

- a. Please indicate whether it is the fact that a company's headquarters is located in Canada, or the relative proportion of its operations that was the basis for Mr. Walter's contention.
- b. Please provide copies of any analyses Mr. Walter's undertook to compare the relative portion of U.S. operations with the total for each company he excluded on this basis.
- c. Please provide copies of any investment-advisory publications or other source documents supporting Mr. Walter's view that investors would differentiate between these utilities and those included in his proxy group because they are "headquartered in Canada."

Response:

While being "headquartered in Canada" or a "Canada-based company" served as partial reasons for exclusion for a few companies (Algonquin, Emera, and Fortis), the only company Mr. Walters excluded from his proxy group on the sole basis for being "headquartered in Canada" or a "Canada-based company" was Fortis. Reasons to exclude Canada-based companies include, but are not limited to, volatility in rates of return and possible Country-based risk premiums. Please see page 7 of Confidential KU-LGE DR1 DOD-FEA Q8 Attach 8. Here, Duff & Phelps provides a list of reasons often cited for adding a country risk premium adjustment.

Additionally, please see page 8 of Confidential KU-LGE DR1 DOD-FEA Q8 Attach 8. There, Duff & Phelps shows the summary statistics of annual returns for several global indexes. As shown on this table, over the period of 1970-2017, the Canada index returns had a standard deviation of 21.5% compared to 17.5% standard deviation for the World index and 17.0% standard deviation for the U.S. index. Furthermore, please see page 9 to Confidential KU-LGE DR1 DOD-FEA Q8 Attach 8. On that page, Duff & Phelps notes that the "Canadian index was the riskiest in the 2000s as well as the most recent decade." The domestic U.S. portfolio was the least risky in the most recent decade." (emphasis added). Also, as shown on that same page in the Duff & Phelps Exhibit 12.12: Annualized

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Monthly Standard Deviation by Decade (%), in every time period shown, the Canada index had higher volatility than the U.S. index and the World index.

- a. See the explanation above.
- b. Mr. Walters did not undertake any analyses to compare the relative portion of U.S. operations for each company.
- c. Please refer to Confidential KU-LGE DR1 DOD-FEA Q8 Attach 8.

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Mr. Walters

Data Request No. 9:

If not already provided in Mr. Walter's work papers, please provide hard copies of the source documents from S&P Global Market Intelligence referenced in footnote 1 to Exhibit CCW-2.

Response:

Mr. Walters does not possess "hard copies" of the documents being requested. Furthermore, the requested items were previously supplied to the Companies on January 25, 2019.

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Mr. Walters

Data Request No. 10:

Reference page 22, lines 3-4. Is Mr. Walter’s aware of any investment advisory reports published in the last ten years that discuss the implications of expected GDP growth in connection with their evaluation of individual stocks? If so, please provide copies of all such reports.

Response:

As a matter of principle, no company’s earnings and/or dividends can grow faster than the economy in which it sells goods and services into perpetuity. In the long-run, earnings growth will be limited by several factors, including, but not limited to, competition and market saturation.

As the CFA Institute has stated (see Confidential KU-LGE DR1 DOD-FEA Q10 Attach 10A):

For earnings growth to exceed GDP growth, the ratio of corporate profits to GDP must trend upward over time. It should be clear that the share of profits in GDP cannot rise forever. At some point, stagnant labor income would make workers unwilling to work and would also undermine demand, making further profit growth unsustainable. Thus, in the long run, real earnings growth cannot exceed the growth rate of potential GDP.

Also, Dr. Morin states the following in his book, “New Regulatory Finance” (see Confidential KU-LGE DR1 DOD-FEA Q10 Attach 10B):

“It is useful to remember that eventually all company growth rates, especially utility services growth rates, converge to a level consistent with the growth rate of the aggregate economy.”

Further, Dr. Morin continues to state (see Confidential KU-LGE DR1 DOD-FEA Q10 Attach 10B):

“[...] it is quite possible that a company’s dividends can grow faster than the general economy for five years, but it is quite implausible for such growth to continue into perpetuity.”

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Additionally, please refer to the discussion of the multi-stage DCF in Mr. Walters' testimony.

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Mr. Walters

Data Request No. 11:

Is Mr. Walters aware of any investment analyst reports published in the last ten years that advise investors to consider growth in GDP as a ceiling on the long run growth rate for an electric utility or gas utility stock, or specifically references expected growth in GDP in developing its expectations or advising investors as to the utility's future prospects? If so, please provide copies of all such reports.

Response:

Please see the response to No. 10 above. Additionally, please see the direct testimony of Mr. Walters at pages 24-29.

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Mr. Walters

Data Request No. 12:

Page 25 of Mr. Walter's notes a "rational expectation that a period of high or low short-term growth can be followed by a change in growth to a rate that is more reflective of long-term sustainable growth." Please provide copies of any investment advisory reports for electric utilities discussing an expectation that "a period of high or low short-term growth" will be followed by "a change in growth to a rate that is more reflective of long-term sustainable growth."

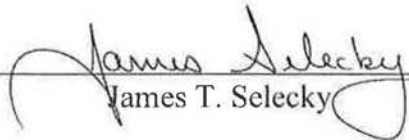
Response:

Please see the response to No. 10 above. Additionally, please see the direct testimony of Mr. Walters at pages 24-29.


VERIFICATION

STATE OF MISSOURI)
)
COUNTY OF ST. LOUIS) SS:

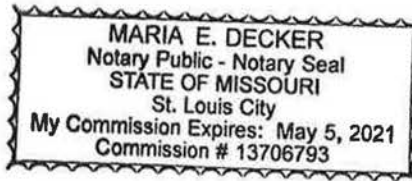
The undersigned, **James T. Selecky**, being duly sworn, deposes and says that he is a Principal of Brubaker & Associates, Inc., and that he has personal knowledge of the matters set forth in the responses for which he is identified as the witness, and the answers contained therein are true and correct to the best of his information, knowledge and belief.


James T. Selecky

Subscribed and sworn to before me, a Notary Public in and before said County and State,
this 7th day of February 2019.


Notary Public


My commission expires: May 5, 2021



VERIFICATION

STATE OF MISSOURI)
)
COUNTY OF ST. LOUIS) SS:

The undersigned, **Christopher C. Walters**, being duly sworn, deposes and says that he is a Senior Consultant of Brubaker & Associates, Inc., and that he has personal knowledge of the matters set forth in the responses for which he is identified as the witness, and the answers contained therein are true and correct to the best of his information, knowledge and belief.



Christopher C. Walters

Subscribed and sworn to before me, a Notary Public in and before said County and State, this 7th day of February 2019.



Notary Public

My commission expires: May 5, 2021

