

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)
Electric Rates; 2) Approval of New Tariffs; 3)) Case No. 2019-00271
Approval of Accounting Practices to Establish)
Regulatory Assets and Liabilities; and 4) All)
Other Required Approvals and Relief.)

DUKE ENERGY KENTUCKY, INC.’S
REPLY IN SUPPORT OF MOTION FOR REHEARING

Comes now Duke Energy Kentucky, Inc. (Duke Energy Kentucky or Company), by counsel, pursuant to KRS 278.400, 807 KAR 5:001, Section 5 and other applicable law, and does hereby tender its Reply in Support of its Motion for Rehearing, respectfully stating as follows:

I. INTRODUCTION

Following the Commission’s entry of an Order on April 27, 2020, Duke Energy Kentucky filed a Motion for Rehearing on May 18, 2020. Only the Attorney General (AG) tendered a Response and, of the seven (7) issues raised in Duke Energy Kentucky’s Motion, the AG only contested granting rehearing on three (3) issues.¹ On a fourth issue – excessive plant additions – the AG recommended granting rehearing but in a manner that is inconsistent with Duke Energy Kentucky’s request. In accordance with the Commission’s regulation regarding the limited scope

¹ The Attorney General does not challenge Duke Energy Kentucky’s assertions that: (1) disallowed depreciation expense was “double-counted”; (2) normalization rules of the Internal Revenue Code should be respected in the amortization of protected EDITs; and (3) a clerical error in the calculation of disallowed incentive compensation should be remedied.

of a reply in support of a motion for rehearing,² the Company addresses the four issues substantively addressed by the AG. Duke Energy Kentucky also disagrees with the AG's premise that, if rehearing is granted, he should be allowed to seek out other points upon which the Company's revenue requirement might be further reduced. Without having timely filed his own motion for rehearing, the AG is barred from raising new issues in the event that rehearing is granted.

II. ARGUMENT

A. Excessive Plant Additions

With respect to the Company's claim that the Order errs by making an adjustment to rate base in light of a misanalysis of non-comparable data, the AG concedes that he "did not propose these adjustments and thus provided no testimony or argument regarding them."³ The AG then "agrees that the Commission should grant rehearing limited solely to the issue of the *calculation* of the plant additions related to the Environmental Surcharge (ES)."⁴ However, the AG claims that any rehearing "should not be open-ended" and that the question of whether the adjustment itself was appropriate is not a matter for rehearing.⁵ The AG then agrees with Duke Energy Kentucky that the calculation in the Order is incorrect, but argues that the Company's calculation is also incorrect. According to the AG, only \$28 million in environmental plant should be added back to the calculation of rate base.⁶ In other words, although the AG agrees with the Company that the Commission made an error in its excessive plant additions adjustment by failing to remove plant additions related to plant-in-service recovered through the Company's environmental

² See 807 KAR 5:001, Section 5.

³ See AG's Response, p. 2.

⁴ See *id.* (emphasis in original).

⁵ See *id.*

⁶ See *id.*, p. 3.

surcharge mechanism (ESM), the AG does not agree with the Company's proposal to subtract \$69 million from the Commission's calculated maximum plant additions from January 2019 through December 2020 of \$376 million.

As an initial matter, the AG's claim that Duke Energy Kentucky did not challenge the validity of the Order's adjustment – just its calculation – is rooted in sophistry.

Using properly reconciled data on an apples-to-apples comparison, there are no excessive plant additions. As a result, the rate base reduction of \$45,403,842 for what are described as "excessive plant additions" and the corresponding adjustment to depreciation expense is unreasonable, inappropriate and clearly confiscatory. The Commission should grant rehearing, reverse its adjustment to the Company's projected plant additions and restore the entire \$5,517,663 in revenue requirement that the Order eliminates.⁷

How this passage could be construed as a concession that the adjustment was incorrectly calculated, but nevertheless appropriate, is entirely unclear. The AG's invitation to adopt a "magic words" type of pleading requirement is altogether unnecessary and inappropriate – particularly in this case. Clearly, Duke Energy Kentucky did not agree with the adjustment to rate base in the Order and requested the Commission to "reverse" it and "restore the entire... revenue requirement." To be clear, the AG's procedural assertion is wrong. Duke Energy Kentucky opposes the adjustment and explained why in its Motion for Rehearing.

With regard to the substance of the AG's Response, two things are clear. First, the Order's reliance upon Filing Requirement 16(7) data in this context to support a reduction in rate base is analytically erroneous. Second, even if the Commission were to grant rehearing and use the correct data to recalculate rate base, the AG's calculation is also inaccurate.

⁷ Duke Energy Kentucky's Motion for Rehearing, p. 4. Additional text in the Motion for Rehearing also demonstrates that the Company opposed the adjustment.

With regard to the usefulness of Filing Requirement 16(7), the AG does not dispute the Company's assertion that this is the wrong data to use when calculating rate base. Indeed, the very purpose of the various B Schedules in the base rate case filing is to provide the Commission and intervenors with the data necessary to calculate rate base. Thus, both the Company and the AG agree that rehearing is necessary to assure that – if any adjustment to rate base is made (and the Company does not agree such an adjustment is necessary) – it should be made with data that is better suited to the task.

Here the Company and the AG depart. The AG suggests that the Order errs by excluding the environmental surcharge plant “additions,” but that the Company goes too far by excluding the “entirety” of the environmental surcharge plant.⁸ The AG correctly points out that the \$69 million adjustment represents the 13-month average balance of ESM plant-in-service eliminated from the forecasted test period. The AG then offers that the amount of ESM plant additions that should be deducted is \$28 million, calculated by subtracting the \$41 million of ESM plant-in-service at the end of the base period (November 30, 2019) from the \$69 million 13-month average balance of ESM plant-in-service for the forecasted test period. This is a grossly incorrect and inaccurate calculation. Subtracting a base period ending balance (November 30, 2019) from a 13-month average forecasted period balance ending March 31, 2021 does not equate to a period of January 2019 through December 2020.

In order to exactly calculate the amount of plant additions for January 2019 through December 2020, one would need to subtract out ESM related plant additions from January 2019 through December 2020. Obviously comparing a base period balance as of November 2019 to a 13-month average *forecasted* (i.e., future) balance (March 31, 2020 through March 31, 2021) gets

⁸ See AG's Response, p. 3.

nowhere close to the time period of January 2019 through December 2020. The Company used the \$69 million in the Company's Application because this was the only amount in the record close enough to the January 2019 through December 2020 time period to illustrate the inaccuracy and inappropriateness of the Commission's calculation. The Company would be able to provide ESM related plant additions upon request but this data was never requested by the Commission or the AG during the rate case proceeding and therefore is not included in the record. The fact that this data is not in the record further supports the inappropriateness of the Order's adjustment which ignored the required test period schedules (B Schedules in the Company's filing) in favor of an independent calculation. All this highlights and underscores the necessity of granting rehearing.

The Company has clearly outlined in its Motion for Rehearing the reasons why this adjustment is inappropriate. The Company has asked for rehearing on the validity of the adjustment as well as the merits of the calculation itself. While the Company appreciates the AG's support and agreement that the Commission failed to remove ESM plant additions, the AG's calculation of the proposed adjustment is also misstated. The Commission should not give any consideration to the AG's faulty calculation and should grant rehearing on this matter for the reasons outlined in the Company's Motion for Rehearing and supported by the AG.

B. Increased Depreciation Expense

The AG also opposes the Company's request for rehearing on the Order's arbitrary reduction of depreciation expense recovery as a result of unchanged depreciation rates. The basis for the AG's opposition to rehearing stems from a handful of snippets taken from a voluminous record. For instance, the AG cites the testimony of Duke Energy Kentucky's witness, Mr. Spanos, as follows: "For most plant accounts, the application of such rates... is reasonable for a period of

three to five years.”⁹ Mr. Spanos’s general statement is correct – the application of depreciation rates for a period of three to five years is appropriate *for most plant accounts* where there has not been substantial investment during the intervening interval of time. But what is clear from this record is that there have been substantial investments in the Steam Production Plant, Other Production Plant and Distribution Plant accounts.¹⁰ The AG’s reliance upon the statement of a general rule of depreciation is misplaced in the specific context of the uncontroverted and unchallenged investments in the *specific* plant accounts identified. Moreover, the AG fails to acknowledge that Mr. Spanos made this distinction very clear elsewhere in his testimony and upon cross-examination.¹¹ It is unfair and unreasonable to give weight to a witness’s general characterization of depreciation principles and then refuse to consider the same witness’s specific and relevant explanation of depreciation principles as applied to the actual facts of the matter at hand.

Likewise, the AG’s concern that properly accounting for depreciation expense would lead to a corresponding increase in the calculation of depreciation expense for environmental surcharge purposes is similarly misplaced. The very premise of the suggestion is that utilities should not be allowed to timely recover the cost of, or a return on, the investments they make to serve customers.¹²

Thus, the AG’s next suggestion that Duke Energy Kentucky somehow seeks to accelerate its recovery through increased depreciation expense is not accurate.¹³ The Company’s

⁹ AG’s Response, p. 3, citing John J. Spanos Direct Testimony, Attachment JJS-S, p. 50 of 364.

¹⁰ See Duke Energy Kentucky Response to AG-DR-01-033, Attachment 1, p. 1. The Company’s Motion for Rehearing provides additional detail as to the subaccounts where investment has substantially increased.

¹¹ See Duke Energy Kentucky’s Motion for Rehearing, Notes 18-20 and accompanying text.

¹² See AG’s Response, pp. 3-4.

¹³ See *id.*, p. 4.

depreciation expense increased as a result of a substantial growth in necessary investment, the effect of which is not offset by an extended service life of the assets in question.¹⁴ Allowing recovery of the increased depreciation expense does not “accelerate” cost recovery. To the contrary, it keeps cost recovery on pace with full recovery of investment during the useful life of the assets – which is the goal of depreciation in the first place.

Likewise, the AG’s Response is confused where it states: “DEK’s Petition would have the Commission believe that unless the Company is allowed to immediately begin recovery of depreciation expense on new investments in the instant proceeding the result will be a dire picture of denied recovery of investments and generational inequities.”¹⁵ The question of *whether* the Company will recover its investment is not the issue presented in the Motion for Rehearing. The question before the Commission is *when* the recovery will begin. The AG’s understanding that “the Commission’s actions merely *delayed that recovery until a more appropriate time,*”¹⁶ underscores the fact that any delay of recovery of otherwise reasonable depreciation expense rewards current customers and punishes future customers. The magnitude of this punishment grows in proportion to the interval between the resetting of depreciation rates. In short, the disallowance of approximately \$7.446 million of annual cost recovery in this case means that, in the next rate case, customers will face a much more significant increase in depreciation expense.

¹⁴ Since it is the AG, not the Company, that argues that the service life for the assets in question should be extended, it is the AG, not the Company, that bears the burden of proof on that question. *See In the Matter of the Application of Caldwell Cty. Water Dist. for Rate Adjustment Pursuant to 807 KAR 5:076*, Order, Case No. 2016-00054 (Ky. P.S.C. Dec. 2, 2016) (“KRS 278.190(3) provides, in part, that the utility has ‘the burden of proof to show that the increased rate or charge is just and reasonable.’ Except in those instances in which an intervening party ‘advances proposals in areas or on issues’ that the utility does not address in its application, the intervening party ‘has no burden of proof to meet.’”) citing *In The Matter of the Adjustment of the Rates of Kentucky-American Water Company*, Order, Case No. 2004-00103, p. 2 (Ky. P.S.C. Oct. 27, 2004); *see also In the Matter of the Application of Cumberland Cellular Partnership for Issuance of a Certificate of Public Convenience and Necessity to Construct a Cell Site (Sycamore Flats) in Rural Service Area #5 (Russell) of the Commonwealth of Kentucky*, Order, Case No. 2006-00146 (Ky. P.S.C. Aug. 9, 2006).

¹⁵ *See id.*, p. 6.

¹⁶ *See id.* (emphasis added).

Duke Energy Kentucky cannot gamble on whether the AG will recall his position here and support the far steeper increase in depreciation expense when the Order's I.O.U. comes due. For that reason, the Commission is requested to remedy the situation now so that it will not have to be revisited – with greater impact – in the future.

What is conspicuously absent from the AG's Response is any acknowledgement that the Kentucky Supreme Court has already laid down the law of utility depreciation in Kentucky. Although Duke Energy Kentucky cited *Public Service Commission of Kentucky v. Dewitt Water District*, 720 S.W.2d 725 (Ky. 1986) throughout the depreciation discussion in its Motion for Rehearing, the AG's Response omits any discussion of the Supreme Court's decision and makes no effort to limit or distinguish its application herein. Instead, the AG cites *Kentucky Public Service Comm'n v. Conway*, 324 S.W.3d 383 (Ky. 2010) for the well-known proposition that the Commission has "plenary" ratemaking authority. The *Conway* decision has nothing to do with depreciation expense and does not stand for the proposition that the Commission's authority is unchecked.¹⁷ The Commission is bound by the Constitution and its enabling statutes and the Supreme Court's Orders construing them. The omission of relevant law is a fatal flaw in the AG's argument.

The balance of the AG's argument is little more than an attempt to gain a second bite at the apple. In the absence of filing his own motion for rehearing, the AG asks the Commission to expand the scope of rehearing – should the Company's Motion be granted – to include separate depreciation adjustments suggested by Mr. Lane Kollen and rejected by the Commission.¹⁸

¹⁷ The Company notes the irony that the AG relies upon *Conway* for the proposition that the Commission has "plenary" ratemaking authority when it was a prior AG's unsuccessful argument that the Commission vastly exceeded the scope of its ratemaking authority that gave rise to the Supreme Court's decision.

¹⁸ See AG's Response, pp. 4-5.

C. Return on Equity

The Attorney General's objection to the Company's request for rehearing on the determination of an appropriate return on equity (ROE) is largely limited to rehashing arguments made in his brief. The only authority cited by the AG is *Public Service Comm'n v. Continental Tele. Co. of Ky.*, 692 S.W.2d 794 (Ky. 1985), which he cites for the proposition that the Commission must provide customers with "the lowest possible cost...." This interest must be balanced, however, against the constitutionally assured property rights of investors, which the United States Supreme Court described in the well-known *Hope Doctrine*:

....[T]he investor interest has a legitimate concern with the financial integrity of the company whose rates are being regulated. From the investor or company point of view it is important that there be enough revenue not only for operating expenses but also for the capital costs of the business. These include service on the debt and dividends on the stock. By that standard *the return to the equity owner should be commensurate with returns on investments in other enterprises having corresponding risks*. That return, moreover, should be sufficient to assure confidence in the financial integrity of the enterprise, so as to maintain its credit and to attract capital.

Fed. Power Comm'n v. Hope Nat. Gas Co., 320 U.S. 591, 603 (1944) (citations omitted).

The AG's Response does not address the central issue posed by the Company's Motion for Rehearing. The primary factors cited by the Commission two years ago in awarding a 9.725% ROE have not changed: the Company's generation portfolio remains highly concentrated; ROEs given to other utilities remain "worthy benchmarks;" there is a continuing lack of diversity in the Company's generation fleet; and an ROE that is significantly lower than other investor-owned electric utility authorized ROEs is more likely to cause financial stress. Under the Order, the Company no longer earns a return that is commensurate with returns on investments in other enterprises having corresponding risks. Rehearing should be granted to reconsider the ROE.

Otherwise, an explanation for the departure from precedent is warranted. In the absence of these remedies, the remarkably low ROE appears arbitrary.

D. Rate LED – LED Outdoor Lighting Service

The AG's opposition to rehearing on Rate LED – LED Outdoor Lighting Service is also based largely upon prior arguments. The AG appears to overlook the Company's request to grant rehearing so as to align a new ROE with Rate LED, which should not be opposed. While the rate structure does lead to customers who elect to pay a monthly fee paying differing amounts than customers who pay upfront as the AG claims,¹⁹ this is by design. As set forth in Duke Energy Kentucky's Motion for Rehearing, the objective is for both the upfront-paying customer and the monthly paying customer to receive a substantially similar service over the full period of such an agreement without the upfront paying customer having to subsidize the deferred paying customer.

The goal is to arrive at fairness between the customers who are willing to pay for costs upfront and those who wish to pay over time. The rate for customers who chose to pay for any additional equipment over time is treated no differently than the rate that a customer would pay for a particular type of fixture, pole, pole foundation, bracket or wiring that is listed in the tariff. The Company believes that rehearing would better facilitate a resolution on this topic that achieves the Company's goal while satisfying the Commission's concern. The alternative is to revise tariffs and, very likely, have them suspended so that further review may commence. Rehearing seems like a more economic process, but the Company defers to the Commission's preference.

III. CONCLUSION

The Company again respectfully suggests that rehearing is warranted on each of the issues raised in its Motion. The AG appears to agree on four of these issues (albeit not necessarily for

¹⁹ See AG's Response, p. 10.

the same reason as the Company) and his objections on the contested issues go more to the merits of the issue than the question of whether rehearing is appropriate. Accordingly, Duke Energy Kentucky's Motion should be granted notwithstanding the AG's Response in opposition.

WHEREFORE, on the basis of the foregoing, Duke Energy Kentucky respectfully petitions the Commission to issue an Order granting rehearing and awarding the relief requested herein.

This 1st day of June 2020.

Respectfully submitted,

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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 June 1, 2020; 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 hand delivered to the Commission within thirty (30) days of the end of the current state of emergency.



Counsel for Duke Energy Kentucky, Inc.