COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

ELECTRONIC APPLICATION OF LOUISVILLE	**)**	
GAS AND ELECTRIC COMPANY FOR RENEWAL	**)**	**CASE NO.**
AND PROPOSED MODIFICATION OF ITS	**)**	**2019-00437**
PERFORMANCE-BASED RATEMAKING	**)**	
MECHANISM	**)**	

RESPONSE OF
LOUISVILLE GAS AND ELECTRIC COMPANY
TO
COMMISSION STAFF'S SECOND REQUEST FOR INFORMATION
DATED MARCH 5, 2020

FILED: MARCH 20, 2020

VERIFICATION

COMMONWEALTH OF KENTUCKY)
)
COUNTY OF JEFFERSON)

The undersigned, **J. Clay Murphy**, being duly sworn, deposes and says that he is Director – Gas Management Planning, and Supply for Louisville Gas and Electric Company, 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.

J. Clay Murphy

J. Clay Murphy

Subscribed and sworn to before me, a Notary Public in and before said County and State, this 20th day of March 2020.

Judy Schooler

Notary Public

Notary Public, ID No. 603967

My Commission Expires:

7/11/2022

VERIFICATION

COMMONWEALTH OF KENTUCKY)
)
COUNTY OF JEFFERSON)

The undersigned, **Pamela L. Jaynes**, being duly sworn, deposes and says that she is Manager - Gas Supply for Louisville Gas and Electric Company, and that she has personal knowledge of the matters set forth in the responses for which she is identified as the witness, and the answers contained therein are true and correct to the best of her information, knowledge and belief.

Pamela L. Jaynes

Pamela L. Jaynes

Subscribed and sworn to before me, a Notary Public in and before said County and State, this 30th day of March 2020.

Judy Schooler

Notary Public

Notary Public, ID No. 603967

My Commission Expires:

7/11/2022

LOUISVILLE GAS AND ELECTRIC COMPANY

Response to Commission Staff's Second Request for Information
Dated March 5, 2020

Case No. 2019-00437

Question No. 1

Witness: J. Clay Murphy / Pamela L. Jaynes

Q-1. Refer to LG&E's response to Commission Staff's First Request for Information (Staff's First Request), Item 2, pages 1-2. Explain LG&E's decision process for evaluating whether to purchase at the first-of-the-month or daily prices.

A-1. Generally, LG&E seeks to maximize the purchase of gas at a first-of-the-month ("FOM") price as gas prices rise above that FOM price during the course of the month. Conversely, as gas prices move below the FOM level, LG&E seeks to minimize FOM purchases and replace them with gas priced at the lower daily price. This requires LG&E to monitor daily price movements (as well as zonal price movements) in the context of overall system requirements and operating parameters. Intra-month price movements above and below the FOM level can occur numerous times during a given month.

These FOM- versus daily-priced purchase capabilities may be limited by the gas supply contracts that LG&E has in place with FOM pricing options, the number of volumetric changes included in each of those FOM-priced contracts, the expected duration of the purchase, system operational limitations, weather, and other factors. For example, just because a daily price moves below an FOM price (which could be the result of the lack of weather-driven demand) does not mean that there is sufficient system load to make purchases at a daily price. This is an example of one of the risks inherent in the PBR mechanism.

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Question No. 2

Witness: J. Clay Murphy / Pamela L. Jaynes

Q-2. Refer to LG&E's response to Staff's First Request, Item 2, in which LG&E confirms that the only gas companies in Kentucky that have Performance-Based Ratemaking (PBR) mechanisms are LG&E, Columbia Gas of Kentucky, Inc. (Columbia Kentucky), and Atmos Energy Corporation (Atmos). Refer also to LG&E's response to Staff's First Request, Item 4, in which it states that the "absence of a well-constructed PBR mechanism will stifle risk-taking and innovation designed to produce lower gas costs." Explain in full detail how all of the other gas companies in Kentucky provide low-cost gas to its customers without a PBR mechanism.

A-2. A prudence standard may be achievable without a well-constructed PBR mechanism, but an LDC may be able to achieve results for customers superior to the results produced by a prudence standard alone. LDCs currently without a PBR mechanism could be incented by a well-constructed PBR mechanism to procure gas supplies that may be lower than those being currently being achieved. See also LG&E's response to PSC Question No. 2-6.

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Question No. 3

Witness: J. Clay Murphy / Pamela L. Jaynes

Q-3. Refer to LG&E's response to Staff's First Request, Item 2, in which LG&E asserts that its PBR mechanism is more fully aligned with least-cost purchasing strategies, has a higher risk level, and a lower level of reward when compared to Atmos and Columbia Kentucky. Based on these assertions, explain whether LG&E is stating that the PBR mechanisms of Atmos and Columbia Kentucky should be more similar to LG&E's PBR mechanism.

A-3. It is not LG&E's assertion that the PBR mechanisms of Atmos Energy Corporation ("Atmos") and Columbia Gas of Kentucky ("Columbia Kentucky") should be similar to LG&E's PBR mechanism.

LG&E is reminded of the Commission's Order in Case No. 384 which states that "[t]he Commission recognizes that LDCs face different circumstances and that differences in operating characteristics among LDCs mean that there is not one PBR approach that is right for all of them." (See Order dated July 17, 2001, at p. 7)

LG&E's point in its response is that, given the robust design of LG&E's PBR mechanism, LG&E's sharing mechanism should be at least as favorable as the sharing mechanism of the other two LDCs. This would allow LG&E to complete the transition apparently contemplated in the Commission's Order in Case No. 2014-00476 dated June 30, 2015, which stated that the change proposed by LG&E was "too abrupt." (Order at p. 6) Therefore, in this application, LG&E is requesting to complete the transition to the sharing mechanism proposed by LG&E in Case No. 2014-00476, which is the same sharing mechanism applicable to the PBR mechanisms of Atmos and Columbia Kentucky.

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Question No. 4

Witness: J. Clay Murphy / Pamela L. Jaynes

Q-4. Refer to LG&E's response to Staff's First Request, Item 4, pages 2-3.

a. State whether ceasing or eliminating the listed optimization activities would violate the regulatory prudence standard discussed in response to Item 1. Explain why continuing these activities at or near LG&E's historical level would not be a natural outcome of the experience it has gained through the PBR mechanism.

b. For each optimization activity that LG&E asserts may cease or be limited without "a well-constructed and properly incentivized PBR mechanism," describe why the activity would be discontinued or limited. The response may group together activities with similar reasoning.

A-4. a. Presumably, the reference to Item 1 is a reference to the first paragraph of LG&Es response to PSC Question No. 1-4 which discusses inter alia the Commission's Order in Administrative Case No. 384. The July 17, 2001, Order in that case states:

> LDCs should maintain their objective of procuring wholesale natural gas supplies at market clearing prices, within the context of maintaining a balanced natural gas supply portfolio that balances the objectives of obtaining low cost gas supplies, minimizing price volatility and maintaining reliability of supply.

The PBR is a risk/reward mechanism which encourages optimization activities designed to achieve results that are superior to a prudence standard. Without the risk/reward structure of a well-constructed PBR mechanism there would be no reason to continue optimization activities. Even with a well-constructed PBR mechanism, there is no guarantee that continuing these activities would continue to produce superior results. The PBR mechanism encourages LG&E to modify its optimization activities over time in order to respond to gas market changes.

Therefore, ceasing or limiting optimization activities would not be a violation of the Commission's prudence standard and continuing these activities at or near historical levels would not be a natural outcome of eliminating the PBR mechanism.

b. See LG&E’s response to PSC Question No. 2-5.

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Question No. 5

Witness: J. Clay Murphy / Pamela L. Jaynes

Q-5. Refer to LG&E's response to Staff's First Request, Item 4. State the extent to which any of the optimization activities listed on pages 2-3 have resulted in gas cost losses.

A-5. As LG&E has described, some of its activities under the PBR mechanism have been more effective than others. However, in total, all of these activities, either separately or in combination, have enabled LG&E to achieve savings under the PBR mechanism. Appendix A of the 2019 Report sets forth the savings made available to customers of $13,720,840.

LG&E has provided several concrete examples of the kinds of losses to which it can be exposed under the PBR mechanism and the benefits to customers of various PBR-related activities. LG&E's potentially limited or discontinued activities fall into four main areas:

Gas Commodity Procurement:

In its response to PSC Question No. 1-2, LG&E describes how it optimizes purchases during the course of the month as prices change in order to achieve savings. In the absence of a well-constructed PBR mechanism, there would be no incentive to follow daily price movements to secure gas below the applicable benchmarks.

In its response to PSC Question No. 1-2, LG&E describes how it optimizes purchases from lower cost zones in order to achieve savings. Purchases from any zone would meet the criteria of purchasing gas at market-clearing rates. LG&E's PBR mechanism encourages the extra step of optimizing purchases from the lowest cost zone(s).

In its response to PSC Question No. 1-2 (at p. 5 of 6), LG&E describes the fact that it may have exposure to losses if it must purchase gas above the applicable benchmark. Managing storage to avoid the purchase of gas at peak prices would no longer be incented under a PBR mechanism. Instead, purchases would be made at the market-clearing price at the time of purchase in order to preserve system reliability.

In its response to PSC Question No. 1-16 (b) incorporating by reference Question 2 of the 2018 Procurement Audit (p. 3 of 8), LG&E describes how it has utilized gas supply contracts with two-part pricing in order to optimize gas supply purchases. These kinds of contracts may no longer be applicable without a PBR mechanism.

In its response to PSC Question No. 1-16 (b) incorporating by reference Question 2 of the 2018 Procurement Audit (p. 3 of 8), LG&E describes how it has utilized term contracting in order to secure gas supplies and optimize gas supply purchases. These kinds of contracts may no longer be applicable without a PBR mechanism.

In its response to PSC Question No. 1-16 (b) incorporating by reference Question 2 of the 2018 Procurement Audit (p. 5 of 8), LG&E describes how it seeks new counterparties in order to develop new supply relationships as a part of its overall PBR-incented goals to beat benchmarks. LG&E already has several counterparties. There would no longer be a need to continue searching for new counterparties who might be able to supply LG&E from non-traditional supply areas or under innovative supply arrangements.

In its response to PSC Question No. 1-16 (a) incorporating by reference Question 2 of the 2018 Procurement Audit (p. 5 of 8), LG&E has described how it has investigated and used new pricing mechanisms in order to optimize savings. The absence of a PBR mechanism would negate the need to develop new pricing scenarios designed to optimize performance.

In its response to PSC Question No. 1-7, LG&E describes the fact that about 23% of the gas commodity purchases were made in excess of the weighted average monthly benchmark, thereby contributing to potential losses under the mechanism. Each of the above optimization activities contribute in some way to LG&E's performance under the PBR mechanism. Sometimes these activities have produced savings, sometimes they have produced expenses; but, taken as a whole, these activities have produced positive results for customers by beating the established benchmarks. These activities could be discontinued or limited because the positive results they produce would no longer be incented by the PBR mechanism.

Pipeline Capacity:

In its response to PSC Question No. 2-12, LG&E recounts the very limited capacity release revenues available and would cease or limit seeking capacity release opportunities because there would be continued risk but no associated reward.

In its response to PSC Question No. 1-11(a) and in its 2019 Report (at p. 10), LG&E has described the fact that pipelines are not obligated to discount their services. While LG&E would not discontinue its capacity planning efforts as a part of ensuring that there is not excess capacity, LG&E would not be incented to seek discounted rate transactions like those that are currently being incented by its PBR mechanism.

In its response to PSC Question No. 1-9, LG&E described how it has benefited customers though the PBR mechanism by participating in open seasons for incremental capacity that provides access to new supply areas. Because there would be no PBR mechanism to incent this activity, it would cease or be limited to the extent that it was available.

In its response to PSC Question No. 1-2 (pp. 4 - 5 of 6), LG&E has described the benefits of contracting for delivered supplies in lieu of pipeline capacity. Because there would be no incentive mechanism for doing so, LG&E would simply contract directly with pipelines for such capacity at the applicable FERC approved tariff rates.

Off-System Sales:

In its response to PSC Question No. 1-13, LG&E describes how it may be exposed to potential losses when it makes an off-system sale of natural gas to a counterparty. Because such risks would no longer be rewarded under a PBR mechanism, such activities would cease or be limited because of the risk involved.

Storage Optimization:

In its response to PSC Question No. 1-16 (a) incorporating by reference Question 2 of the 2018 Procurement Audit (p. 6 of 8), LG&E describes how it has utilized the storage "swing" methodology to purchase gas from lower cost zones. Because such activities would no longer be rewarded under a PBR mechanism, such activities would cease or be limited.

Potential Alternate Gas Supply Strategies:

As one alternative to any or all of these strategies, LG&E could simply purchase gas on a day-to-day basis at a "market-clearing" rate irrespective of the zone of origin. It could also purchase pipeline capacity at the FERC-approved tariff rates. As an alternative, these strategies would fulfill the regulatory obligation to provide reliable service at a market-clearing price. These strategies would be potential alternatives for LG&E to evaluate in lieu of the supply optimization activities undertaken by LG&E in light of its PBR mechanism.

In summary, without the incentives found in LG&E's PBR mechanism, optimization activities would not be undertaken because there would be no reward and no benchmarks to beat. Consequently, LG&E would seek to mitigate risk-taking encouraged by the PBR mechanism. Instead, LG&E would focus on the recovery of gas costs by relying upon the prudence standards set forth by the Commission. (See LG&E's response to PSC Question No. 2-4.)

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Question No. 6

Witness: J. Clay Murphy / Pamela L. Jaynes

Q-6. Refer to LG&E's response to Staff's First Request, Item 8, in which LG&E asserted to "[s]ee the response to Question No. 4." This answer is not adequate. As previously requested, explain why the least cost acquisition standard in purchasing natural gas supplies and pipeline transportation services does not exist absent LG&E's PBR mechanism.

A-6. Absent a well-constructed gas supply cost PBR mechanism, LG&E will follow the otherwise applicable guidance provided by the Commission in its Orders in Administrative Case No. 297[1] and amplified in Administrative Case No. 384[2] which states that "LDCs should maintain their objective of procuring wholesale natural gas supplies at market clearing prices, within the context of maintaining a balanced natural gas supply portfolio that balances the objectives of obtaining low cost gas supplies, minimizing price volatility and maintaining reliability of supply." (Order No. 384 dated July 17, 2001, at p. 18.) This Commission guidance is the prudence standard (or as referenced by the Commission in this question: "the least cost acquisition standard"). This prudence standard is the one which LDCs observe in the absence of a well-constructed PBR mechanism.

However, it should be noted that the Commission has a longstanding history of supporting performance-based ratemaking ("PBR") mechanisms as a means to achieve superior performance by LDCs. The Commission's support can be found in the Orders referenced above and other Orders issued by the Commission. (Please see LG&E's response to PSC Question No. 1-4.) With a well-constructed PBR mechanism, the LDC is incented to undertake manageable risks in order to surpass the least cost acquisition standard ("prudence standard") by achieving savings when compared to the benchmarks of its gas supply costs PBR mechanism.

[1] "An Investigation of the Impact of Federal Policy on Natural Gas to Kentucky Consumers and Suppliers"
[2] "An Investigation of Increasing Wholesale Natural Gas Prices and the Impacts of Such Increases on the Retail Customers Served by Kentucky's Jurisdictional Natural Gas Distribution Companies"

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Question No. 7

Witness: J. Clay Murphy / Pamela L. Jaynes

Q-7. Refer to LG&E's response to Staff's First Request, Item 9. Explain whether LG&E's proposal to increase its sharing percentages would encourage decreased reliability.

A-7. LG&E's proposal to increase LG&E's sharing mechanism to match those of Atmos and Columbia Kentucky would not encourage decreased reliability.

Reliability is an over-arching obligation of any LDC. Because LG&E's PBR mechanism does not encourage it to take actions that would diminish reliability, changes to the sharing percentages would have no impact on reliability.

As explained in PSC Question No. 1-9, LG&E's PBR mechanism does not encourage it to take risks that reduce reliability because the rewards under the mechanism are not great enough to overcome the costs associated with restoring gas customer outages and the related "brand damage" that could result from unreliable contracting practices. Even with the more appropriate sharing percentages proposed by LG&E, the rewards would be inadequate in light of the potential costs associated with diminished reliability.

Lastly, and as a point of reference, LG&E is unaware that the natural gas customers of either Atmos or Columbia Kentucky have experienced curtailments, interruptions, or a general lack of supply reliability as the result of the PBR sharing mechanisms approved by the Commission.

See also LG&E's responses to PSC Question No. 1-10.

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Case No. 2019-00437

Question No. 8

Witness: J. Clay Murphy / Pamela L. Jaynes

Q-8. Refer to LG&E's response to Staff's First Request, Item 13, in which LG&E stated that the "most significant risk of loss under an off-system sale is that the counterparty will not reimburse LG&E for the gas sold ."

a. Provide a detailed explanation with examples of LG&E not being reimbursed for gas sold by a counterparty.

b. Explain how the risk that the counterparty will not reimburse LG&E for the gas sold is controlled.

A-8. a. Presumably, the question is in reference to gas sold by LG&E <u>to</u> a counterparty.

Off-system sales of natural gas require LG&E to purchase the gas from Supplier A and sell that gas to Supplier B (a counterparty). This sale causes LG&E to incur a payment obligation to Supplier A and to be at risk for payment from Supplier B (the counterparty) to whom LG&E has sold the gas.

For example, LG&E may buy gas from Supplier A for $10,000 and sell gas to Supplier B (the counterparty) for $15,000.

LG&E mitigates the risk of non-payment by the counterparty in two ways. Firstly, LG&E evaluates creditworthiness, establishes credit limits, and obtains financial guaranties when required for all potential counterparties to ensure that they have the financial means to pay LG&E for any gas purchased from LG&E. Secondly, LG&E may be able to sell gas to a counterparty from which LG&E is also purchasing gas under another supply transaction, thereby allowing LG&E to net the cost of the purchase and the amount due to LG&E for the sale into a single, lower amount owed by LG&E to the supplier/counterparty.

For example, LG&E may purchase gas from Supplier A for $10,000 and sell gas to Supplier B (the counterparty) for $15,000. LG&E may also be purchasing gas from Supplier B under another transaction in the amount of $20,000. In this case, LG&E would net the sale of $15,000 to Supplier B and the purchase of $20,000 from Supplier

B to yield a net obligation by LG&E to Supplier B of $5,000 ($20,000 - $15,000). LG&E remains obligated to pay Supplier A for the natural gas purchased at $10,000. This netting is designed to eliminate the risk of not receiving payment from the counterparty for the gas sold to the counterparty.

b. See LG&E's response to part (a).

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Case No. 2019-00437

Question No. 9

Witness: J. Clay Murphy / Pamela L. Jaynes

Q-9. Refer to LG&E's response to Staff's First Request, Item 15.

a. Confirm that LG&E's proposed sharing percentages would increase customers' gas costs by 0.35 percent, all else being equal.

b. Explain whether LG&E's proposed incentive levels, as compared to the current levels, will create a disincentive for LG&E to create as much savings as possible under the mechanism given the risks and rewards embodied in the mechanism.

c. Explain whether the shareholder portion of the total savings approaching 50 percent of the total savings indicates that LG&E's sharing percentage bands do not appropriately challenge LG&E's ability to reduce gas costs.

A-9. a. LG&E can confirm that, based upon the historical data provided by LG&E in Appendix A of the 2019 Report and in LG&E's response to PSC Question No. 1-15, the increase in the shareholder portion would increase by 0.35% [($8,572,508 – $7,005,625) / $447,680,992].

Importantly, with a new sharing mechanism, all else will not be equal. Altering the sharing mechanism as proposed by LG&E is designed to incorporate the same 2% threshold found in the PBR mechanism of Atmos and Columbia Kentucky.

b. No. Because LG&E's sharing mechanism does not include a cap, LG&E will continue to be incented to maximize savings under the PBR mechanism. LG&E is requesting that the Commission approve the same sharing mechanism for LG&E as Atmos and Columbia Kentucky. (See LG&E's response to PSC Question No. 2-3.)

c. The fact that the shareholder portion of the total savings has approached the 50% sharing level does not indicate that LG&E's sharing percentage bands do not appropriately challenge LG&E's ability to reduce gas costs. On an historical basis (as shown in Appendix A of the 2019 Report), the fact that LG&E has participated in 50% of the savings above the current 3% threshold indicates that LG&E is responding to the incentives under the mechanism as it attempts to maximize savings under the mechanism.

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Question No. 10

Witness: J. Clay Murphy / Pamela L. Jaynes

Q-10. Refer to LG&E's response to Staff's First Request, Items 15, 17, and 20. If LG&E does not separately track costs associated with its PBR-related activities, then explain how a true cost-benefit analysis can be determined.

A-10. As LG&E explained in the 2019 Report at pp. 4-5, the PBR mechanism is the "true" cost/benefit test:

> By specifying benchmarks, LG&E's gas supply cost PBR mechanism establishes <u>the</u> cost/benefit test to determine the effectiveness of LG&E's procurement activity. The benchmarks which are established prior to the beginning of the operation of the PBR mechanism are objective benchmarks that are intended to incent the utility to perform as desired. The benchmarks provide a meaningful framework for measuring and reviewing performance. LG&E's performance is measured by comparing actual costs to benchmark costs to determine the savings or expenses resulting under the PBR mechanism.

Because LG&E's gas supply cost PBR mechanism acts as an incentive mechanism, it does not change <u>what</u> LG&E does in terms of activities related to gas supply procurement, it changes <u>how</u> LG&E procures and manages its gas supply and pipeline transportation portfolio. A well-constructed PBR mechanism incents and rewards the LDC for the risks it undertakes to optimize its gas supply and pipeline transportation portfolio. The PBR mechanism is not a compensatory mechanism designed to recover PBR-related activity costs.

Because the PBR mechanism changes the "how", not the "what," of gas supply procurement, it is not possible for LG&E to track the procurement costs specifically associated with PBR-related activities. A PBR mechanism does not change the kinds of procurement activities that LG&E undertakes. A PBR mechanism changes how those procurement activities are performed.

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Question No. 11

Witness: J. Clay Murphy / Pamela L. Jaynes

Q-11. Refer to the Attachment to the LG&E's response to Staff's First Request, Item 18.

a. Confirm that the label to row 7, "Disincentive to perform over a certain savings level?" refers to a limit on the indicated utility's ability to share savings with customers.

b. Confirm that the utilities in four of the eight states to which LG&E's PBR mechanism is compared are Columbia affiliates only, and that their PBR mechanisms are largely limited to Off System Sales and Capacity Release.

c. State whether LG&E is aware of whether the UGI Utilities' Revenue Sharing Incentive Mechanism in Pennsylvania applies to all utility revenues, or whether it is limited to gas cost procurement.

d. State whether LG&E can confirm whether Spire Missouri still has an authorized Gas Cost Incentive Plan.

e. Confirm that of the eight states for which information is provided, the state with an approved gas cost PBR mechanism most similar to that of Kentucky utilities is California, and that the features of the California mechanisms which differ most with Kentucky mechanisms are the level of savings subject to sharing, the calculation of the sharing portion, and the limit to utility sharing.

A-11. a. Yes, the label "Disincentive to perform over a certain savings level?" refers to a limit on the indicated utility's ability to share savings with customers. These limits act as disincentives by capping the utility's ability to share in the achieved performance. As a result, the utility is not incented to perform above the capped amount. See LG&E's response to PSC Question No. 1-18.

b. Yes, four of the utilities to which LG&E has compared its PBR mechanism are affiliates of Columbia Kentucky. Each of these four utilities operates in different state jurisdictions from Columbia Kentucky – specifically, Maryland, Massachusetts, Pennsylvania, and Virginia. The PBR mechanisms of each utility were approved by the appropriate regulatory body having jurisdiction in the applicable state. Columbia

Gas of Maryland has an incentive to lower gas commodity costs. Columbia Gas of Pennsylvania also has an incentive to lower gas commodity costs on certain summer purchases. All four utilities have an incentive to release pipeline capacity and to make off-system sales.

A well-constructed PBR mechanism, such as LG&E's mechanism, should be comprehensive and include incentives to lower gas commodity costs, lower pipeline transportation costs (including through capacity release), and make off-system sales. Purchasing natural gas and pipeline transportation are the fundamental activities that an LDC performs in its role as a merchant of natural gas. Because of their significance, these activities provide the most opportunity for an LDC to optimize performance and achieve savings for customers, for example through contract management and pipeline discounts. As such, these components should be important components in a PBR mechanism. A PBR mechanism should also encourage an LDC to undertake other more peripheral activities such as releasing pipeline capacity and making off-system sales. However, a PBR mechanism that only includes releasing pipeline capacity and making off-system sales cannot be expected to create meaningful savings opportunities for LG&E's customers. LG&E's capacity and off-system sales activity is a very small component of overall gas procurement costs. For PBR Years 19, 20, 21, and 22, total capacity release revenues have been $15,950, and total off-system sales net revenues have been $746,437, or 0.17% of Total Actual Annual Gas Costs of $447,680,992.

c. LG&E's assessment of UGI Utilities' Revenue Sharing Incentive Mechanism is based on its review of Original Pages 49, 50, 51, and 52 of UGI Utilities' tariff. Those pages describe "Rules And Regulations, 11. Rider B, Section 1307 (F) Purchased Gas Costs". LG&E's understanding of the mechanism described on these pages is that it is limited to activities such as capacity release and off-system sales.

d. LG&E can confirm that the information included for Spire Missouri East is included in Spire Missouri East's current tariff on Sheets No. 11.9, 11.10, and 11.11. The description of the "Gas Supply Incentive Plan" begins on Sheet 11.9. The effective date of these tariff sheets is April 19, 2018.

e. LG&E's PBR mechanism is most like the mechanisms in California and Tennessee which include incentives to achieve lower gas commodity costs, lower pipeline transportation costs (including release of pipeline capacity), and make off-system sales. The sharing mechanisms in California and Tennessee differ from LG&E's PBR mechanism in that those mechanisms place limits on the level of savings subject to sharing. These limits act as a disincentive for the LDC to perform above the specified sharing limit.

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Question No. 12

Witness: J. Clay Murphy / Pamela L. Jaynes

Q-12. Refer to LG&E's response to Staff's First Request, Item 19. State whether the Total Annual Actual Transportation Costs include any capital cost recovery mechanisms for modernization of natural gas facilities from its pipeline suppliers. If so, provide the annual amount from each supplier, and the extent to which discounts from such cost recovery mechanisms are included in Savings from Pipeline Discounts.

A-12. LG&E is subject to various surcharge mechanisms imposed by both Texas Gas Transmission, LLC ("Texas Gas") and Tennessee Gas Pipeline Company, LLC ("Tennessee"). Neither pipeline has agreed to discount any surcharges with respect to LG&E's gas transportation agreements.

Only Tennessee has a surcharge mechanism that is a capital cost recovery mechanism. This mechanism is called the "Pipeline Safety and Greenhouse Gas Cost Adjustment Mechanism" ("PS&GHG"). The mechanism was approved by FERC with the demand and volumetric surcharges adjusted each November 1 subject to FERC approval. As the surcharge change is approved by FERC, LG&E's PBR mechanism provides for a change in the calculation of the benchmark.

Below is a table setting forth the amounts recovered from LG&E by Tennessee through the PS&GHG mechanism.

	Tennessee Gas Pipeline Company
PBR Year	PS&GHG Surcharge
19	$8,395
20	$8,887
21	$8,974
22	$5,712

Since no surcharges have been discounted, no amounts with respect to these pipeline surcharge mechanisms are reflected in savings from pipeline discounts. Changes in the surcharges do not affect savings (or expenses) under the PBR mechanism because any change in the surcharge is accounted in both the actual cost and the benchmark.

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Question No. 13

Witness: J. Clay Murphy / Pamela L. Jaynes

Q-13. Assuming financial hedging instruments impact gas transportation costs, off-system sales and storage service transactions, and actual gas costs during the same period, explain how gains or losses from the use of financial hedging instruments and the transaction costs associated with such instruments are allocated to the PBR mechanism components.

A-13. To the extent that any financial hedging mechanism costs would be incurred by LG&E in the operation of its PBR mechanism, those costs would be assigned to the specific activity that the costs were designed to hedge (e.g., gas commodity costs would be assigned to the GAIF portion of the PBR mechanism, gas transportation costs would be assigned to the TIF portion of the PBR mechanism, and off-system sales and storage service transaction costs would be assigned to the OSSIF portion of the PBR mechanism). To date, LG&E has not undertaken any financial hedging and has therefore incurred no financial hedging costs as a part of the operation of its PBR mechanism, and none are expected.