

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

ELECTRONIC APPLICATION OF DUKE ENERGY)	
KENTUCKY, INC. TO BECOME A FULL PARTICIPANT)	
IN THE PJM INTERCONNECTION LLC, BASE RESIDUAL)	CASE NO.
AND INCREMENTAL AUCTION CONSTRUCT FOR THE)	2024-00285
2027/2028 DELIVERY YEAR AND FOR NECESSARY)	
ACCOUNTING AND TARIFF CHANGES)	

DUKE ENERGY KENTUCKY, INC.’S INITIAL MERIT BRIEF

Comes now Duke Energy Kentucky, Inc. (Duke Energy Kentucky or the Company), by counsel, pursuant to the Commission’s February 27, 2025, Order setting a schedule for the filing of briefs in the above-styled case, and other applicable law, does hereby respectfully state as follows:

I. Introduction

On September 9, 2024, Duke Energy Kentucky filed its Application and Direct testimony in this proceeding, seeking to exit the Fixed Resource Requirement (FRR) and to transition to full participation in the PJM Interconnection LLC (PJM) Reliability Pricing Model (RPM) Base Residual Auction (BRA) and Incremental Auction (IA) construct. The Company is also seeking authority to amend its Profit Sharing Mechanism (Rider PSM) to account for capacity-related revenues and costs from PJM Billing Line Item (BLI) and bilateral markets and to reconcile the net capacity-related revenues and charges so that customers receive 100 percent of the benefit or costs of capacity outside of the current sharing percentages for other components of Rider PSM. Finally, the Company requested

approval of any necessary accounting treatment, waivers, and approvals to accomplish its realignment and the recovery.

At the time the Company filed its Application in this proceeding, the earliest the Company could complete its realignment was with the June 1, 2027, through May 31, 2028, (2027/2028) Delivery Year. However, due to delays in PJM's BRA schedule, if the Commission issues its decision and grants its approval by May 1, 2025, the Company could actually complete its realignment for the 2026/2027 delivery year to the benefit of customers. For the reasons explained in the Company's Application, Direct and Rebuttal Testimony, and as supported in responses to numerous data requests, the Commission should approve the Company's Application.

II. Background

A. Duke Energy Kentucky's Participation in PJM

PJM is the nation's first fully functioning Regional Transmission Organization (RTO) operating the power grid and wholesale electric market for all or parts of thirteen states and the District of Columbia.¹ PJM's electric market consists of an energy market, capacity market, Ancillary Services Market (ASM), and a Financial Transmission Rights (FTR) market.² PJM's operation is governed by agreements and tariffs approved by the Federal Energy Regulatory Commission (FERC) including the Operating Agreement, Open Access Transmission Tariff (OATT), and the Reliability Assurance Agreement (RAA).³ Duke Energy Kentucky joined PJM effective January 1, 2012, having received Commission authorization to do so by Order dated December 22, 2010, in Case No. 2010-

¹ Direct Testimony of John D. Swez pg. 3.

² *Id.*

³ *Id.*

00203 (Realignment Order).⁴ As a PJM member, Duke Energy Kentucky is subject to these agreements, which among other things, require Duke Energy Kentucky to offer its available generation to PJM and to purchase its energy to serve customer load from the PJM Day-Ahead or Real-Time Energy Markets.⁵ And, since completing its realignment, the Company has remained an FRR participant, as per the Realignment Order, in the PJM Capacity market.⁶

Under the FRR election, Duke Energy Kentucky must secure and commit its own, unit-specific capacity, identifying the precise generating units in sufficient quantities to satisfy its load obligations, including adequate reserves.⁷ FRR entities are unable to procure any capacity to satisfy their FRR plan obligation through the PJM auctions because the auction products are not unit-specific capacity.⁸ Additionally, as an FRR member, the Company does not and cannot directly and freely participate in the PJM capacity RPM auction construct, and is limited in its ability to sell any excess capacity in those auctions. Instead, the Company is required to annually submit an FRR capacity plan to satisfy the unforced capacity (UCAP) obligation for all loads in the Company's FRR service area, including all expected load growth.⁹ Duke Energy Kentucky satisfies its PJM capacity demand requirements through its own generation assets located in the Duke Energy Ohio and Kentucky Local Delivery Area (DEOK LDA), demand response

⁴ See Direct Testimony of John Swez, pg. 4 (September 9; 2024); See also *In the Matter of the Application of Duke Energy Kentucky, Inc., for Approval to Transfer Functional Control of its Transmission Assets from the Midwest Independent Transmission System Operator to the PJM Interconnection Regional Transmission Organization and Request for Expedited Treatment*, Case No. 2010-00203, p. 18, (Ky.P.S.C. Order) (December 22, 2010).

⁵ Swez Direct, pg. 4.

⁶ *Id.*

⁷ Unit-specific capacity requires the Company to point to specific assets to satisfy its load obligations that are not otherwise or already committed in the RPM auctions.

⁸ See Response to AG-DR-02-004.

⁹ Application pg. 4.

programs, and necessary bilateral capacity purchases.¹⁰ Duke Energy Kentucky's generating assets consist of approximately 1,076 MW of summer generating capacity consisting of: 1) East Bend Unit 2 Generating Unit (East Bend), a 600 MW (net rating) coal-fired base load unit located along the Ohio River in Boone County; 2) Woodsdale Generating Station (Woodsdale), a 476 MW (net summer rating) six-unit natural gas-fired combustion turbine (CT) facility with fuel oil back-up located in Trenton, Ohio; and 3) 9.3 MW of solar assets consisting of the nameplate ratings of Walton 1 (2 MW), Walton 2 (2 MW), Crittenden (2.8 MW), and Aero Solar (2.5 MW).¹¹

Under the RPM BRA/IA construct, generators submit competitive bids into the BRA and IAs, and load serving entities purchase the necessary capacity to satisfy their load obligations. The BRA auction occurs based upon a Delivery Year that is typically three years in the future. In the BRA, PJM first accepts offers to provide capacity at the lowest cost. As the auction progresses, PJM accepts progressively higher-priced offers until enough capacity is assembled to meet the projected demand plus reserve requirement for the future delivery year. At that point, when the auction clears, all sellers receive the last or "marginal" offer price. This marginal price is also known as the auction clearing price.¹²

While historically, the FRR construct has proven to be the right decision for customers, saving customers between \$1 million and \$1.8 million annually,¹³ the Company now believes that will not be the case going forward and that a move to the RPM BRA/IA construct is in the best interest of customers and remaining an FRR entity is increasingly

¹⁰ *Id.*

¹¹ Swez Direct pp 6-7.

¹² *Id.* pg. 6.

¹³ See Response to AG-DR-02-01.

risky and will ultimately cost customers more.¹⁴ Such a transition is justified due to: 1) the risk of and potential for large and sudden load growth at a rate faster than the Company can construct or acquire additional baseload generation; 2) uncertainty and change in the balance between demand and supply in the DEOK zone in PJM driven by announced generating asset retirements; 3) the lack of available bilateral capacity in the DEOK zone should future zonal separation occur and Duke Energy Kentucky finds itself in a position where it needed additional bilateral capacity to meet its FRR plan; 4) anticipated changes to PJM's FRR construct that would negatively impact the Company's participation as a FRR entity; 5) the energy transition in PJM due to retirements of fossil generation and PJM's own prediction of shrinking reserve margins and higher capacity prices; and 6) the change in the FRR shortfall penalty to the greater of 1.75 x Net Cost of New Entry (Net Cone) or Gross CONE¹⁵. These factors support a change to provide less risk and greater value for Duke Energy Kentucky's customers.

Under PJM regulations, the transition from an FRR entity to a full RPM auction participant generally requires a three-year transition to align with BRA Delivery Year procurement. This is because PJM's BRA is for a delivery year that is three years into the future.¹⁶ However, due to PJM's suspension of its auction process as its new rules were under consideration by FERC, and PJM's subsequent efforts to "catch-up" and conduct BRAs on an accelerated period, Duke Energy Kentucky has a unique opportunity to transition to the RPM auction construct sooner than would otherwise and typically be available.¹⁷

¹⁴ *Id.*

¹⁵ *Id.* pp. 9-10.

¹⁶ Swex Direct pg. 48.

¹⁷ Application pg. 6; Swex Direct pg. 48.

B. Summary of the Company's Requests

In its Application, Duke Energy Kentucky requests the following relief: 1) authorization to exit the FRR capacity construct and begin participation in the PJM auction-based capacity procurement construct effective with the PJM delivery year beginning June 1, 2027; and 2) modifications to its Rider PSM to include: a) the BLIs, charges and credits, that will begin to be allocated to the Company, once it begins participating in the auctions; b) costs and revenues in the bilateral markets to meet PJM's FERC-approved reliability requirements; and c) modifications to the sharing mechanism to separately account for the capacity portion of Rider PSM to net 100 percent of the costs and revenues of the capacity markets to customers.¹⁸ In addition, the Company further requested the Commission grant any additional accounting authority, waivers, and authorizations that the Commission deems necessary.¹⁹ While this Application was pending, PJM shifted the timing of its BRA procurement timeline such that Duke Energy Kentucky could actually complete its realignment a full delivery year earlier, effective with the delivery year beginning June 1, 2026.²⁰

C. Applicable Law

Pursuant to the Realignment Order, Duke Energy Kentucky participates in PJM under the FRR option for purposes of meeting PJM's Resource Adequacy requirement.²¹ Per the Realignment Order, the Company was directed to remain an FRR entity until it

¹⁸ Application pg. 12.

¹⁹ *Id.*

²⁰ Swez Rebuttal pg. 6.

²¹ Application pg. 12.

requested and received Commission approval to transition to the RPM capacity auction construct.²²

The transition from the FRR self-supply capacity construct to one that is market based and administered via a competitive, yet structured, auction construct constitutes a change in the right to control, or functional control, of a utility asset.²³ KRS 278.218 provides in relevant part that “No person shall acquire or transfer ownership of or control, *or the right to control*, any assets that are owned by a utility. without prior approval of the commission, if the assets have an original book value of one million dollars (\$1,000,000) or more and:

1. The assets are to be transferred by the utility for reasons other than obsolescence; or
2. The assets will continue to provide the same or similar service to the utility or its customers.”²⁴

KRS 278.218(2) further sets forth the standard under which the Commission will consider a transaction, providing in relevant part, that the “Commission shall grant its approval if the transaction is for a proper purpose and consistent with the public interest.”²⁵

The Company submits it has met this burden, and the Commission should approve the Company’s Application, as filed, to allow the transition to the BRA/IA participation as early as possible. The record is replete with evidence supporting that the transition to BRA/IA participation is both for a proper purpose and is in the public interest. The Company submitted its Application with supporting testimony of two witnesses explaining the justification for the transition and the analysis performed that led the Company to its

²² Realignment Order, pp. 13-14 and 18.

²³ Application pg. 9.

²⁴ KRS 278.281 *Emphasis added*.

²⁵ *Id.*

conclusion that the time to leave the FRR construct has arrived. The Commission Staff issued three sets of discovery to the Company. The Kentucky Office of the Attorney General (KYOAG), the only intervening party to this proceeding, submitted two rounds of data requests as well as Direct Testimony of two consulting witnesses. Importantly, the KYOAG does not oppose the Company's Application, but did submit testimony arguing that if the Commission approved the Company's Application it should impose specific conditions on the Company. Through Rebuttal Testimony, the Company objected to those recommendations and explained why the KYOAG consulting witnesses' recommendations were unnecessary and should not be adopted. This case now stands ready for decision.

III. Discussion

A. The Transition is for a Proper Purpose and in the Public Interest

1. Transitioning to RPM Auction Participation should be approved

The transfer to full RPM auction participation is for a proper purpose and is in the public interest as it will allow the Company to continue to provide reliable service to customers by providing sufficient generation capacity to meet customer demand, provides an opportunity for incremental value to customers, and avoids risks that exist with continued FRR participation. The transition will not adversely impact the Company's ability to continue providing reliable service to customers, meet their demand, and will not adversely impact the operation or expectation of the operational and useful life of the generating portfolio.²⁶ The transition will have no impact to the Company's participation in the PJM energy market and ASM,²⁷ its ability to engage in off-system sales of energy

²⁶ See Response to AG-DR-01-010.

²⁷ See Response to AG-DR-01-017.

or capacity to other Kentucky utilities, and will not change the commitment and dispatch of Duke Energy Kentucky's generating units.²⁸ The transition has the potential to increase the Company's ability to utilize its demand response programs under the RPM auction construct from what exists currently as an FRR.²⁹ The transition to RPM auction participation will not change how the Company conducts its integrated resource planning (IRP) to meet customer demand.³⁰ Duke Energy Kentucky will continue to retain and deploy its generating assets to provide a hedge against capacity and energy costs to its customers and will continue its IRP planning processes to meet customer demand. As evidenced by the Company's most recent IRP, Duke Energy Kentucky plans for and assumes that any unit retirement would result in a replacement by a unit of similar sized capacity.³¹ Kentucky's IRP process is unchanged by the Company's transition to full RPM auction participation and will provide the Commission and stakeholders with assurances that the Company will continue to plan to meet demand with sufficient capacity without materially impacting the DEOK zone capacity clearing prices.³² The change from FRR to full RPM auction participation will not change the Company's incentive to acquire or construct additional capacity in the DEOK Zone.³³ And outside of short-term capacity procurements to meet customer demand that appears faster than the Company can add a resource, the Company does not intend to just use the auctions to address capacity needs.³⁴

The Company anticipates that transferring to the RPM auction construct will provide greater flexibility to meet the reliability needs for customers and respond to

²⁸ See Response to AG-DR-01-011.

²⁹ See Response to AG-DR-01-015.

³⁰ See Response to AG-DR-01-042.

³¹ See Response to AG-DR-02-006c.

³² *Id.*

³³ See Response to AG-DR-02-009.

³⁴ *Id.*

unanticipated and sudden changes in customer demand. Auction-based capacity procurement provides a faster path to securing capacity than may be possible through the FRR construct. If the Company experiences a sudden increase in load, faster than the Company can build or acquire unit-specific capacity, it could find itself in an untenable situation where it is capacity deficient and subject to significant penalties.

Further, the change to RPM auction participation will mitigate or eliminate several FRR-specific costs and risks the Company and its customers now face. These incremental risks include but are not limited to: 1) potential FRR plan penalties if the plan does not satisfy demand requirements; 2) avoiding the FRR capacity holdback limitation; 3) over procuring capacity due to the reserve margin differential between FRR and RPM during high capacity prices; 4) the FRR minimal zonal capacity requirement; and 5) risk of limited bilateral capacity to meet an FRR plan.³⁵ The Company respectfully submits that the transfer to full RPM participation is in the public interest in that RPM best protects customers from the risk of a large energy intensive customer locating in the Company's service territory and requiring service prior to the Company building or acquiring generation. Further, the transition to RPM helps insulate the Company from the risk of an anemic bilateral capacity market due to announced retirements within the DEOK zone and throughout PJM that limits the Company's ability to procure additional or emergency capacity for its FRR plan. Lastly, PJM has contemplated changes to PJM's FRR construct that would negatively impact the Company's participation as an FRR entity in the future. Additionally, the move to RPM is anticipated to produce numerous benefits to customers, including the ability to fully monetize excess capacity in the BRA that is not possible as an

³⁵ Swez Direct, pg. 24.

FRR entity resulting in greater capacity sales and revenues to customers, the ability to avoid FRR deficiency penalties, and potentially lower reserve requirements at high-capacity prices.

The move from an FRR participation to RPM auction participation will likely have a nonconsequential impact on the cleared PJM capacity price. Duke Energy Kentucky will be moving both its generation position and load position to the RPM auction. Thus, since Duke Energy Kentucky is relatively small, has a portfolio that is balanced between load and capacity, slightly long in capacity, the transition should have little to no effect on the wholesale market or other participants in PJM.³⁶ As supported in the testimony accompanying this Application, the Company's analysis shows that a move to RPM provides greater benefits and/or lower costs to customers in the majority of capacity positions and price scenarios analyzed than by remaining an FRR entity. The most recent PJM BRA for the 2025/2026 delivery year cleared at a price that is nearly ten times higher than the last BRA, indicating that capacity is becoming more valuable in PJM and as the Company's analysis shows, provides greater benefit to customers than remaining in the FRR.

In support of its Application, Duke Energy Kentucky submitted a cost-benefit analysis that evaluates the differences between participation in PJM as both an FRR and full BRA auction participant.³⁷ This analysis supports that going forward, when considering the aforementioned costs and risks, as well as the possibility of large loads

³⁶ See Responses to AG-DR-01-005 and AG-DR-01-008.

³⁷ Direct Testimony of John Swez, Attachment JDS-1.

coming online faster than the Company is able to build or acquire unit-specific capacity, that a transition to full RPM auction participation is proper.³⁸

As explained by Company witness John D. Swez, the Company's analysis depicts the potential value of the Company's generating portfolio in four capacity and energy pricing scenarios: 1) capacity exceeding demand with low prices; 2) demand exceeding capacity with low prices; 3) capacity exceeding demand with high prices; and 4) demand exceeding capacity with high prices.³⁹ This analysis shows that transitioning to the full RPM participation was the most beneficial strategy in three of the four possible scenarios.⁴⁰

In analyzing the possible scenarios of market prices and capacity positions, the Company factored in all relevant information available, including the existing PJM rules and market assumptions for participation as both an FRR entity and as a full auction participant going forward.⁴¹ These factors include: 1) the amount of capacity hold-back required of FRR members before they can sell any excess generation in PJM; 2) the Company's current required reserve margin as an FRR; 3) the PJM capacity demand curve; 4) the cost of replacement capacity if the Company is short on capacity; and 5) the relationships between the BRA and incremental capacity auction clearing prices.⁴² The Company also considered the risks and costs of PJM penalties if the Company's FRR plan is deficient and replacement capacity is unavailable.⁴³ As explained by Mr. Swez, the risks of such shortfalls extend beyond the obvious reliability implications for customers as the monetary penalties for an FRR deficiency could be significant, especially if replacement

³⁸ Swez Direct pg. 11.

³⁹ *Id.* pg. 12.

⁴⁰ *Id.* pp. 14-19.

⁴¹ *Id.* pg. 17.

⁴² *Id.*

⁴³ *Id.* pp. 17-19.

capacity is not available. As Mr. Swez explains, the FRR deficiency penalty is calculated at the shortfall amount multiplied by the *greater* of either the Gross Cost of New Entry (CONE) or 1.75 multiplied by Net CONE.⁴⁴ Per Mr. Swez, the shortfall penalty of a 100 MW deficiency where there is no replacement capacity available, would be \$16.2 million.⁴⁵

As a BRA participant, Duke Energy Kentucky would not be subject to the risks of the FRR capacity holdback requirement. This means that the Company would be able to sell 100 percent of its available capacity, including all excess capacity over demand, in the BRA, allowing customers to see the full value of the capacity being paid for through base rates. Today, because of the capacity hold-back requirement for an FRR, Duke Energy Kentucky must hold back 30 MWs of its available capacity from the BRA.⁴⁶ Once a full BRA participant, Duke Energy Kentucky would be able to offer, and customers will receive the value of, all capacity cleared in the auction, the proceeds of which will be provided to customers through Rider PSM.⁴⁷ Had Duke Energy Kentucky been able to fully monetize all excess capacity in PJM's most recently completed BRA, an additional \$2.364 million in incremental revenue would have been shared with customers.⁴⁸

Transition to full BRA participation also reduces the costs and risks associated with the reserve margin differential between an FRR entity and a BRA participant. As an FRR entity, the required self-supply reserve margin remains relatively constant. However, as a BRA participant, the reserve requirement changes based upon the price of capacity, meaning that because the amount of reserves needed for BRA participants depends upon

⁴⁴ *Id.* pg. 18.

⁴⁵ *Id.*

⁴⁶ *Id.* pg. 20.

⁴⁷ *Id.* pg. 21.

⁴⁸ *Id.* pg. 21.

PJM's sloped demand curve, a lesser amount of reserves would be procured by the Company during periods of extremely high capacity prices.⁴⁹ Put another way, as an FRR entity, during periods of very high capacity prices, the Company is over procuring reserves as compared to a BRA participant. As capacity prices are predicted to continue to have upward pressures, remaining an FRR entity would mean the Company is likely to pay a higher cost for its reserve position.⁵⁰

The risk and exposure to FRR capacity deficiency penalties and the minimum internal zonal limitations are eliminated through the transition to full RPM auction participation. As Mr. Swez explained, the potential for deficiency penalties in an FRR plan can be severe.⁵¹ A plan deficiency can occur due to a sudden increase in customer demand, planned or unplanned unit retirements, or through unit derates.⁵² As a full RPM auction participant, Duke Energy Kentucky would not be subject to the FRR capacity penalty risk. Also, as an FRR participant, PJM's rules require Duke Energy Kentucky to locate a certain, PJM-determined amount of unit specific generation capacity within the DEOK Zone. This restriction places an unnecessary limitation on the Company's ability to purchase bilateral capacity necessary to meet its obligations.⁵³ This limitation is volatile, ranging from 4.4 percent to over 29 percent. With the limited amount of capacity within the DEOK Zone, coupled with announced additional retirements, there is a potential scarcity of bilateral capacity risk for remaining in the FRR construct that does not exist for RPM auction participants.⁵⁴ Transitioning to full RPM auction participation will also save customers

⁴⁹ Swez Direct, pp. 20-21.

⁵⁰ *Id.*

⁵¹ *Id.* pg. 22.

⁵² *Id.*

⁵³ *Id.*

⁵⁴ *Id.* pp. 22-26.

money under high-capacity cost scenarios, and if the DEOK Zone separates again in the future and the Company is in a short position unable to procure capacity inside the DEOK zone, the FRR deficiency penalty is avoided.⁵⁵

Duke Energy Kentucky is not alone in its evaluation of exiting the FRR and transitioning to full RPM auction participation. Of the fourteen regions in PJM (thirteen states and the District of Columbia), six of those regions are fully regulated, including the Commonwealth of Kentucky.⁵⁶ And within those six regulated regions, only three load-serving entities were FRR entities in PJM for the 2024/2025 delivery year: 1) Dominion (VA); 2) AEP (WV, KY, TN, IN); and 3) Duke Energy Kentucky (KY).⁵⁷ Effective with the 2025/2026 delivery year, Dominion has announced that it is exiting the FRR and will be returning to full RPM auction participation, leaving Duke Energy Kentucky and AEP as the only remaining FRR entities in PJM.⁵⁸

2. Amending the PSM to include the capacity-related BLI's and adjusting the sharing percentage should be approved

Amending Rider PSM is also for a proper purpose and is in the public interest. Once its transition to RPM auctions is complete, the Company's PJM settlement statement will begin to include the charges and credits related to capacity auction participation incurred to meet PJM's FERC-approved reliability requirements. Amending Rider PSM will enable the Company to net the costs with anticipated revenues of participating in the PJM RPM auction constructs. Given the variability and magnitude of charges and credits, the Company needs the mechanisms and accounting authority put in place to appropriately and

⁵⁵ *Id.* pg. 28.

⁵⁶ *See* Response to AG-DR-02-003.

⁵⁷ *Id.*

⁵⁸ *Id.*; Dominion's stated transition was due to changes in PJM rules, including the minimum internal resource requirement and increases in data center demand in the region.; *Id.*

properly account for and net these charges and credits. Amending Rider PSM to include all of the capacity-related transactions from PJM and bilateral markets will ensure that customers are paying for and receiving the benefit of participation in the PJM RPM auction structure, including receiving the full value of generating resources used to serve customer demand. And since the Company's participation in PJM's RPM allows customers to receive a reliable supply of electricity by providing ready access to capacity and energy markets, the public interest is served.

Once it transitions to full RPM auction participation, the Company will begin receiving additional PJM BLI charges and credits related to its auction participation.⁵⁹ These BLIs are properly charged to participants in accordance with PJM's FERC-approved tariffs and are necessary for full participation. It is reasonable and proper for Duke Energy Kentucky to include these charges and credits as proposed in the Application as they enable the Company to participate in PJM's auctions in accordance with PJM's rules and enable customers to receive the full value of the Company's rate-based generation in the wholesale market capacity auctions. As listed in Mr. Swez's Direct testimony, these new and tariffed capacity-related BLIs include:

- 1600- RPM Auction- charges for the auction resource clearing price, make-whole payments;
- 1610- Locational Reliability- daily unforced capacity obligation prices at the applicable zonal capacity price for the delivery year;
- 1650- Auction Specific MW Capacity Transaction- Bilateral capacity transactions for multi-day durations settled in the PJM market;
- 1660- Demand Resource Interruptible Load for Reliability Compliance Penalty- Penalty for sellers that cannot demonstrate hourly real-time performance;

⁵⁹ *Id.* pg. 36.

- 1661- Capacity Resource Deficiency- charged when capacity resources are unable or unavailable to deliver unforced capacity and do not obtain replacement unforced capacity to satisfy the cleared sell offer;
- 1662-Generation Resource Rating Test Failure- charged when generation capacity resources fail a capacity test;
- 1663-Qualifying Transmission Upgrade Compliance Penalty- penalty for cleared qualifying transmission upgrades delayed in coming into service;
- 1664- Peak Season Maintenance Compliance Penalty-charged to generation capacity cleared that is out of service and on a maintenance outage that is not authorized by PJM;
- 1665- Peak-Hour Period Availability- Incentives to resources that exceed expected availability, and penalties are assessed to those who fall short;
- 1666- Load Management Test Failure- penalty charge to sellers with committed demand resources that fail performance tests;
- 2600-RPM Auction- sell offers for generation, demand, or qualified transmission upgrade resources MWs cleared in the RPM auction and paid the clearing price in the applicable auction. Also includes resource make-whole payments;
- 2605-RPM Seasonal Capacity Performance Auction- payments for sell offers for generation, demand, or qualified transmission upgrade resource MWs cleared in the RPM Auction. Also includes make-whole payments;
- 2620-Interruptible Load for Reliability-credit for certified zonal MW priced at the applicable zonal ILR price;
- 2625-LSE Price Responsive Demand- Annual capacity resource provided by a price responsive demand provider that represents customers that will reduce load based on price;
- 2630 Capacity Transfer Rights-recognizes the value of import capability to constrained LDAs;
- 2640-Incremental Capacity Transfer Rights (CTRs)- provided to fund transmission upgrades that increase import capability into a constrained LDA;
- 2650-Auction Specific MW Capacity Transaction- settlements of bilateral capacity transactions for multi-day durations;

- 2660-Demand Resource and ILR Compliance Penalty- Sellers with zonal aggregate committed Demand Resources or nominated ILR that cannot demonstrate hourly real-time performance pay a penalty charge;
- 2661-Capacity Resource Deficiency-Capacity resources that are unable or unavailable to delivery unforced capacity, and do not obtain replacement unforced capacity to satisfy their cleared sell offer pay this deficiency charge;
- 2662- Generation Resource Rating Test Failure-Charge to generation capacity resources that fail a capacity test;
- 2663- Qualifying Transmission Upgrade Compliance Penalty- a penalty charge for cleared qualifying transmission upgrades delayed in coming into service for the applicable delivery year;
- 2664- Peak Season Maintenance Compliance Penalty- penalty for generation capacity resources that fail to have available unforced capacity during the peak season to satisfy their cleared MWs;
- 2665-Peak Hour Period Availability-incentives to resources that exceed expected available and penalties to those who fall short; and
- 2666-Load Management Test Failure- a charge to sellers with committed DR that fail performance tests;⁶⁰

Since the Company must receive these BLIs to participate in the PJM RPM auction construct, and as proven in this Application, the transition to the full RPM participation is reasonable, beneficial to customers, and otherwise for a proper purpose and in the public interest. The Commission should authorize the Company to include these items for recovery, crediting, and netting through the Rider PSM. To do otherwise, would place unreasonable and uncompensated risks on the Company, deny the Company the ability to recover costs it incurs to provide service to customers, and would result in a regulatory taking that creates financial harm to the Company.

⁶⁰ Swez Direct pp. 36-46.

The Commission should grant authorization to modify the Rider PSM sharing mechanism to separately account for the capacity portion of Rider PSM to net 100 percent of the charges and credits of participating in the capacity markets to customers. This modification ensures that customers will receive 100 percent of the net benefits or costs as a result of the Company's participation in the RPM BRA and IAs and any costs or revenues in bilateral markets to meet PJM's FERC-approved reliability requirements. Rider PSM will continue to operate as it does today in all other respects.

Adjusting the profit-sharing percentages for capacity related transactions to a 100 percent customer-focused allocation is reasonable, for a proper purpose and is in the public interest. The Company's generation portfolio and capacity resource planning is all designed to meet customer demand. Because generating assets are sized to serve customers' needs, customers pay for these assets whether they are steel-in-the-ground assets or bilateral purchases.⁶¹ The Company's proposal to move to full RPM auction participation is being proposed for the benefit of customers and so, it is reasonable that customers receive the net revenues or costs of such participation. Full RPM auction participation increases the value of the existing generating portfolio because the Company will be able to sell 100 percent of its excess generating capacity, above customer demand, which the Company is proposing to provide completely to customers. Because the Company is proposing to give customers 100 percent of the capacity benefits, it is also symmetric and fair that customers also bear 100 percent of the costs.⁶²

Once transitioned to full RPM auction participation, the Company will continue to actively manage the daily energy market position of the generating portfolio as it does

⁶¹ Swez Direct pg. 46.

⁶² *Id.*

today. Nothing will change in that regard. Therefore it is logical, proper, and in the public interest for the Company to continue to share in the energy market revenues under the current 90/10 sharing percentage. Energy markets are more volatile, changing hourly, with day-ahead and day of energy market commitments. Duke Energy Kentucky will continue to have managerial responsibility for the operation and dispatch of these assets, and it is logical for the Company to maintain a small share of the risk and benefit of managing that position and maximize their value by keeping the assets operating in an efficient, reasonable, and beneficial manner.⁶³

B. The Attorney Generals Recommendations are Unnecessary and Unreasonable and Should Not Be Adopted

1. Overview of the Attorney General Recommendations

The KYOAG is the only intervening party in this proceeding, having conducted robust discovery, submitting more than eighty data requests, not including subparts.⁶⁴ The KYOAG submitted testimony of two consulting witnesses, Lane Kollen and Phillip Hayet, from J. Kennedy and Associates, Inc. These consulting witnesses, who provide testimony on behalf of the KYOAG, do not oppose the Company's Application in these proceedings, but rather, make recommendations the Commission should include in any approval of the Company's Application.⁶⁵ In response to these recommendations, the Company submitted the Rebuttal Testimony of Mr. Swez and Ms. Steinkuhl. As explained in the Company's Rebuttal Testimonies, many of the KYOAG consulting witnesses' recommendations are unnecessary, overly complicate the Company's rates while providing no benefit to

⁶³ Swez Direct pg. 47

⁶⁴ See Attorney General Initial Data Requests, October 4, 2024, and Supplemental Data Requests, November 15, 2024.

⁶⁵ See generally, Direct Testimony of Phillip Hayet and Lane Kollen.

customers and are otherwise unreasonable. Where the Company agrees with the recommendations, the Company's witnesses explained.

In total, the KYOAG consulting witnesses made nine recommendations as conditions should the Commission approve the Company's Application:

1. Duke Energy Kentucky should be required to replace any retiring dispatchable capacity with owned or purchased pursuant to bilateral agreement, in-zone (preferably located in Kentucky), dispatchable capacity prior to the retirement of the capacity.⁶⁶
2. Purchases through the BRA auction should be limited so that the Company does not overly rely on the auction to satisfy capacity requirements. The Company should be limited to purchase no more than nine percent of its annual capacity requirement through the BRA auction, and it should be required to bring its long-term capacity imbalance back into balance within a period of six years.⁶⁷
3. As an alternative to the two conditions above, the Commission could consider approving the Company's request to become an RPM entity, but also open a new docket to establish minimum capacity obligations for Kentucky-based RPM entities and set a goal for the new obligations to be in effect within one year of issuing its order in this docket.⁶⁸
4. The Commission should limit the capacity and time period for recovery of net BRA and IA capacity purchase expense in PSM rates consistent with the underlying physical conditions addressed by Witness Hayet.⁶⁹
5. The Commission should ensure there is no double recovery of capacity costs, once through base rates and then another recovery in whole or part through PSM rates... the Commission should impose a condition that requires a credit in the PSM rates to offset the continuing recovery of non-fuel operating expenses and purchased power expense in the base rates that are no longer incurred until base rates are reset in the future and exclude recovery of these costs."⁷⁰
6. The Commission should maintain the ten (10) percent Company and ninety percent (90) customers sharing allocation for all revenue and expense BLIs included in PSM rates, including the new BLIs....⁷¹
7. The Commission should ensure there are no ratemaking incentives to purchase capacity in the BRAs and IAs instead of acquiring new

⁶⁶ Hayet Direct at 5.

⁶⁷ *Id.*

⁶⁸ *Id.*

⁶⁹ Kollen Direct at 8.

⁷⁰ Kollen Direct at 9.

⁷¹ *Id.* at 9.

owned capacity and/or new or additional bilateral capacity purchases to replace retired owned capacity or terminated or reduced capacity purchases...⁷²

8. The Commission should exclude the compliance and other penalty expense BLIs from the PSM and thereby preclude the Company from recovering these avoidable expenses through PSM rates.⁷³
9. Rider PSM should be modified so capacity revenues and costs are allocated based upon demand⁷⁴

Initially, it must be emphasized that the Company's Application to transition to full RPM auction participation is because the Company believes it is in the best interests for customers to do so. The Company's Application is structured such that customers will receive the full benefits (and costs) of such a transition. Duke Energy Kentucky is not a merchant generator. The Company owns, operates, and procures generation capacity, including necessary and sufficient reserves, and cost-effectively dispatches those assets into the wholesale energy markets to meet customer demand. Customers pay for the costs of operating these assets through regulated rates. Transitioning to full RPM auction participation does not change those facts.

Today, as an FRR entity, the value of the existing generating capacity is in meeting the FRR plan requirements. The ability to sell excess capacity as an FRR participant in PJM is capped and limited by PJM's rules. Moving to full RPM participation thus provides customers with added value for this capacity, opportunities for greater credits through the ability to sell all available excess generation, and under the Company's analysis, is more likely to save customers money in the long run, than staying an FRR. That is why, in the Company's Application, customers will receive all of the benefit of the capacity value by adjusting the Rider PSM sharing percentages for capacity participation in the PJM BRA

⁷² *Id.*

⁷³ *Id.* at 10.

⁷⁴ *Id.* pg. 11.

and IA auctions. The KYOAG consulting witness recommendations, while described as providing protections and benefits for customers, really unnecessarily complicate the transition, restrict the Company's ability to manage the generation portfolio for customers' benefits, and place unnecessary costs and risks on the Company in its efforts to maximize benefits to customers. The Company's proposal is based upon what it believes is in the best interests of customers. Placing unnecessary conditions on the Company to affect the transition for customers creates asymmetry of risk for Duke Energy Kentucky, affecting its ability to manage the generation portfolio assets, and potentially harms the Company and its shareholders for advancing the best interests of customers. For these reasons, the Commission should not adopt the KYOAG's consulting witnesses' recommendations as proposed.

2. Requiring the Company to Replace Retiring Dispatchable Capacity with Owned or Purchased Capacity Located In-Zone or in Kentucky is Redundant and the Geographic Limitations are Unnecessarily Restrictive.

As Mr. Swez explained in his rebuttal testimony, the Company agrees that owned generation resources are the best hedge for capacity and energy market prices needed to serve Company load if located within the DEOK zone.⁷⁵ This is true regardless of whether the Company is an FRR or RPM entity.⁷⁶ The Company also agrees with the premise that it makes sense to have replacement resource in place prior to retirement of an existing resource since a resource that is not constructed or purchased cannot be a hedge against either capacity or energy prices.⁷⁷ However, placing such a geographic limiting condition on the Company's transition is unnecessary as Kentucky law, specifically, KRS 278.264

⁷⁵ Swez Rebuttal pg. 9.

⁷⁶ *Id.*

⁷⁷ *Id.*

already defines actions for the retirement of an electric generating unit. Specifically, part (d) states “The utility shall not commence retirement or decommissioning of the electric generating unit until the replacement generating capacity meeting the requirements of paragraph (a) of this subsection is fully constructed, permitted, and in operation, unless the utility can demonstrate that it is necessary under the circumstances to commence retirement or decommissioning of the existing unit earlier.” Thus, the Company believes that any additional requirement is duplicative and unnecessary. The Company must already comply with KRS 278.264 and the General Assembly has spoken on what the utility’s obligation and requirement is under the law.

Based on Mr. Hayet’s recommendation and his response to Duke Energy Kentucky’s Data Request to the Attorney General Data Request 01-021,⁷⁸ the Company believes the only additional difference between Mr. Hayet’s recommendation and KRS 278.264 is that the capacity replacement be located within the DEOK zone and preferably in the state of Kentucky (DEOK/DEK zone/area). Mr. Hayet’s recommendation places an unnecessary limitation on the Company that may prove to be detrimental to customers. Today, the procurement, construction, or acquisition of an interest in a generating asset would require the approval of this Commission and the Company would have the burden of proof to demonstrate the need and reasonableness of such a proposal.⁷⁹ An in-zone or in-state limitation may result in some assets, which may be the most advantageous and beneficial to customers, being excluded from consideration. As Mr. Swez argued, if a particular resource type, like nuclear, was only available outside of the DEOK zone and was the preferred resource selected through the IRP process, a geographic limitation placed

⁷⁸ See Attorney General’s response to DEK-DR-01-021 in this proceeding.

⁷⁹ Swez Rebuttal pg. 12.

now could eliminate such a resource from consideration.⁸⁰ As it stands today, this resource may be the preferred resource selected through the Company's IRP process, and the Company would look to consider this resource. Finally, the established CPCN application process is sufficient to allow the Commission to evaluate the reasonableness of a considered resource, including its geographic location, on a case-by-case basis.

While the Company, all else being equal, would prefer any new resource to be located in the Company's delivery zone,⁸¹ placing such a locational limitation on new capacity resources, especially at this point in time, is unreasonable and unnecessarily restricts the Company's ability to consider all cost-effective options to serve its customers. Further, a limitation that any dispatchable capacity must be located in the DEOK zone would preclude the Company from partnering with other utilities outside of the DEOK zone, including Kentucky-jurisdictional utilities, on an asset, if one were to become available or a joint ownership of a newly constructed asset became feasible.⁸²

Similarly, a geographic limitation on bilateral capacity purchases suffers the same deficiencies in reasoning. Such limitation unreasonably restricts the Company in its ability to procure a reasonable supply to meet customer demand. As Mr. Swez explained in his testimony, there is already a scarcity of capacity currently located in the DEOK zone. And due to known upcoming retirements, the amount of "in-zone" dispatchable capacity is going to continue to decrease. Limiting the Company to in-zone bilateral purchases may mean there is no counterparty for the Company to acquire needed capacity. For these reasons, the Commission should not adopt this recommendation.

⁸⁰ Swez Rebuttal pg. 11.

⁸¹ See Company responses to AG-DR-02-009 and AG-DR-02-011 in this proceeding.

⁸² Swez Rebuttal pg. 11.

3. A Nine Percent Limitation on Annual Capacity Procurements through the BRA and a Six Year limit to Cure Capacity Imbalances are Unreasonable Restrictions.

In its second recommendation, the KYOAG consulting witness suggests limiting the Company's ability to purchase annual capacity requirement through the BRA auction to nine percent and require the Company to bring any capacity imbalance into balance within six years. As an initial matter, as Mr. Swez explained, the Company agrees that owning resources are the best hedge against volatile capacity prices because it provides the opportunity to sell MWs at the same price as purchases. Nonetheless, the Commission's IRP process remains the means by which Duke Energy Kentucky will make its long-term resource decisions. And, while the Company does not anticipate relying solely on the PJM capacity auction construct to meet capacity needs, there could be times when the Company must rely more heavily upon the BRA/IA capacity purchases, in excess of capacity sales to meet customer demand, particularly if demand increases at a rate faster than the Company can build or acquire interests in capacity.⁸³ Additionally, if the Company is able to procure capacity through the BRA/IA at a price lower than what it can construct or bilaterally purchase, it should not be precluded from doing so due to an arbitrary market purchase capacity.⁸⁴ The bilateral capacity market may not provide the needed resources, especially if the Commission imposes an in-zone geographic limitation on bilateral capacity purchases as the KYOAG consulting witnesses also suggest.

Finally, in a scenario where a large customer data-center load comes online in Duke Energy Kentucky's territory, the Company may have no choice but to procure additional capacity, in excess of a nine percent threshold, to meet that demand and maintain reliability

⁸³ Swez Rebuttal pp. 13-14.

⁸⁴ *Id.* pg. 15.

on the system. It may be impossible to serve this demand in any other way than through auction procurements for some time, until a new asset can be procured or constructed, and that alone could push the Company over a nine-percent capacity procurement collar. The Company will do as it always does and look for the most economical and reasonable solution to meet customer demand, and unnecessary constraints on the Company's ability to manage resources or meet customer demand should not be imposed.

Likewise, a six-year grace period to cure capacity position imbalances is an unreasonable and unnecessary restriction on the Company's ability to properly serve customers and meet their demand in the most economical manner. The PJM interconnection processes, regulatory approvals, and construction timelines all impact the timing of bringing new resources online or procuring existing interests in assets. As Mr. Swez explains, a six-year time limit may force the Company to take actions that are more expensive or less beneficial to customers because it must operate within a six-year ticking clock to reach a capacity balance requirement. The Company provides annual updates on its reserve margin, capacity purchases, and deficits as part of Admin Case No. 387 demonstrating that the Company is continually looking forward towards meeting its customers' demand and informing the Commission of its status.⁸⁵ The Commission maintains its jurisdiction over the prudence of the Company's operations and should not impose further restrictions on the Company's ability to provide for customers by way of a six-year capacity imbalance cure timeline.

⁸⁵ Swez Rebuttal pg. 16.

4. Opening a Docket to Establish Minimum Capacity Obligations for Kentucky-Based RPM Entities is Not Necessary.

The KYOAG consulting witness proposes that if the Commission does not adopt its recommendations regarding capacity replacements or its nine percent limitation, that the Commission instead open a new docket to establish minimum PJM RPM capacity obligations.⁸⁶ As explained by Mr. Swez, the Company does not believe the Commission needs to take such action because a one-sized-fits all approach may not be the best policy for each of the PJM participants given their unique circumstances including generation portfolios, customer load, seasonal peaking, delivery zones, which all may impact capacity obligations.⁸⁷ Nonetheless, if the Commission decides to do so, the Company will participate and would expect to offer similar arguments to those that have been presented in this proceeding.

5. The Commission should not adopt unnecessary and unreasonable recommendations to limit the capacity and time period for recovery of net BRA and IA capacity purchase expense in PSM rates as suggested by Witness Hayet.⁸⁸

The various limitations on capacity and time period for recovery of net BRA and IA capacity purchases are unreasonable as explained by Duke Energy Kentucky witness Swez, through his rebuttal testimony. Nonetheless, Mr. Swez does describe which of those recommendations may be reasonable as modified in his rebuttal testimony.⁸⁹ As previously explained, although the Company agrees that a resource located in the DEOK zone is the best hedge for customers, a recommendation that limits the Company's available choices for additional resources to the DEOK zone could cause customers additional costs and is

⁸⁶ Hayet Direct pp. 20-21

⁸⁷ Swez Rebuttal, pg. 19.

⁸⁸ Kollen Direct pg. 8.

⁸⁹ See Swez Rebuttal Generally and at pp. 10-18.

unnecessary.⁹⁰ Additionally, although a theoretical bilateral purchase from within the DEOK zone may represent the best capacity hedge when a Company-owned asset is not available, such a geographic limitation may unnecessarily restrict the Company from meeting customer demand, especially if such zonal bilateral capacity does not exist or is not the least cost/most reasonable option for customers.⁹¹ The Company strongly disagrees with the recommendation that replacement capacity be limited in any way or amount to bilateral purchases from assets within in the DEOK zone⁹² and fails to see a customer benefit from the recommendation.

The Company does not believe a net position limit is necessary or appropriate and that such a limit could cause higher costs for customers.⁹³ An arbitrary position limit could force the Company into a suboptimal alternative such as a high-cost short-term bilateral capacity purchase. The Company will continue to provide periodic updates to the Commission of its net capacity position, and will do so as it relates to results from the BRA/IA.⁹⁴

6. The concerns about double recovery of capacity costs are premature and the Commission has adequate time and tools to ensure there is no double recovery of capacity costs in rates.

The concern regarding double recovery of capacity costs is founded upon the premise that that if the Company were to retire an existing power plant, the Company will no longer incur, or will incur substantially lower non-fuel operating expenses,⁹⁵ but will continue recovering those costs in base rates, along with the replacement capacity through

⁹⁰ *Id.*

⁹¹ Swez Rebuttal pg. 17.

⁹² *Id.*

⁹³ *Id.*

⁹⁴ *Id.*

⁹⁵ e.g., non-fuel operation and maintenance expense

Rider PSM.⁹⁶ KYOAG consulting witness Kollen also claims that if the Company terminates or reduces bilateral capacity purchases, the Company will no longer incur or will incur lower purchased power expense, but the Company will continue to recover these costs in base rates.⁹⁷

First, the Company has not requested authorization to retire any generating assets as part of this proceeding, nor does it have such an application pending before this Commission. Second, as Company witness Steinkuhl explains in her rebuttal testimony, Mr. Kollen is only partially correct in his assumptions, is mistaken on how the Company recovers costs of capacity and bilateral capacity purchases and overlooks the fact that the Company may not have fully recovered its costs already incurred in providing service prior to a future generating unit's retirement. These facts result in his recommendations being premature, faulty, overly broad, and unreasonable. Company witness Ms. Steinkuhl addresses those misconceptions and provides a more balanced and reasonable approach to address the double recovery concerns.

As an initial premise, the Company agrees that the Company's rates should be adjusted when a generating asset is retired to assure the Company has recovered no more and no less than the costs to serve. That would include any costs in rates that have significantly decreased or are no longer being incurred.⁹⁸ However, it must also be acknowledged that any capacity-related costs that have already been incurred by the Company, but have not yet been fully recovered from customers, must still be fully

⁹⁶ Kollen Direct pp. 7-8.

⁹⁷ *Id.*

⁹⁸ Steinkuhl Rebuttal pg. 3.

recovered in rates.⁹⁹ While the Company agrees that it should not double recover its costs, the Company disagrees with Mr. Kollen's recommendation as to how to ensure there is no double recovery of capacity costs, including bilateral capacity. This protection against double recovery can be accomplished in several ways either through base rates or a separate rider mechanism as this Commission has previously authorized for some utilities.¹⁰⁰

Mr. Kollen's claim that if bilateral capacity purchases are terminated or reduced, the Company will no longer incur or will incur lower purchased power expense but continue to recover these costs in base rates is wrong. As Ms. Steinkuhl explains the Company's base rates do not include any bilateral capacity purchases.¹⁰¹ Rather, all capacity purchases including bilateral capacity purchases are currently included in the PSM and not in base rates.¹⁰² There can be no double recovery if there are no such costs embedded in base rates. Because Rider PSM adjusts periodically, when capacity purchases stop occurring, they are removed from the rider. Any costs or credits associated with capacity purchases including bilateral capacity purchases should continue to be recovered through the PSM as they are today and Mr. Kollen's claim and concern about double recovering capacity purchases are unfounded and based upon a false premise.

Second, when the Company retires its existing power plants, such as East Bend, the Company will be required to make filings with the Commission for approval of such retirement. At that time, the Company would likely make a base rate filing or some other filing to address and align its costs with customer rates.¹⁰³ That filing, such as new base

⁹⁹ *Id.* Such costs may include remaining costs of the plant assets at the time of retirement, as well as any costs to retire and decommission the asset.

¹⁰⁰ *Id.*

¹⁰¹ Steinkuhl Rebuttal pg. 3.

¹⁰² *Id.*

¹⁰³ Steinkuhl Rebuttal pg. 4.

rates, would reflect any changes in operating expenses but also ensure that the Company recovers the remaining net book value of the asset.¹⁰⁴ In the alternative, any remaining net costs could also be recovered through a deferral and cost adjustment mechanism approved by the Commission.¹⁰⁵ As Ms. Steinkuhl explained, a separate mechanism for this would be appropriate and reasonable as it would keep these costs out of the PSM calculation and not overly complicate it.¹⁰⁶ With the implementation of a separate mechanism or an update to base rates, there would be no need to apply a credit to the PSM.¹⁰⁷

Nonetheless, it is premature to address these issues now, as they can easily and more appropriately be addressed by the Commission, if and when the Company seeks approval to retire a generating asset.¹⁰⁸ Consistent with KRS 278.264, when the Company makes such a retirement request, it must, among other things, meet the rebuttable presumption against fossil retirement, including demonstrating the retirement does not harm utility ratepayers by causing it to incur net incremental costs that could be avoided by continuing to operate the unit in compliance with the law.¹⁰⁹ Therefore, the Company must file, and the Commission must consider, the costs of retirement as part of retirement analysis. It would be appropriate to decide how to treat such costs at that time, with full consideration of the magnitude of rate implications, if any, at the time of retirement. To do so now, is premature.

¹⁰⁴ *Id.*

¹⁰⁵ *Id.*

¹⁰⁶ *Id.*

¹⁰⁷ *Id.*

¹⁰⁸ *Id.*

¹⁰⁹ KRS 278.264(2)(b)

7. The Company's Proposal to Amend Rider PSM's Sharing Percentages for Capacity-Related BLIs is Reasonable.

It is appropriate for customers to receive 100 percent of the net capacity benefits or costs because these assets are owned, maintained, and operated to serve customer demand and customers pay for the generating resources through base rates.¹¹⁰ Further, it is appropriate to recover the costs associated with such capacity because the Company, regardless of its participation in PJM, maintains the obligation to serve customer demand, provide reasonable service, meet its legal obligations under KRS 278.264, file its periodic IRPs, and thus would have to either build additional generating resources or purchase capacity to provide service to customers.¹¹¹ The netting of the capacity revenues and capacity costs is appropriate, so the customer receives 100 percent the net benefit or 100 percent the net cost.

As explained by Mr. Swez, since the vast majority of new charges and credits that would result from the Company's move from FRR to RPM would be either PJM BLI 1600, 1610 or BLI 2600, limiting the Company to 90 percent recovery would be a fundamental departure from established rate making policy that would mean customers would not pay their full costs to serve their given demand in some situations.¹¹² And since customers should pay the full costs of serving them, including the provision of adequate capacity with sufficient reserves to meet customers' demand, it is fair that customers should also receive 100 percent of the benefits, or revenues for that capacity. Therefore, the Company proposed that 100 percent of all additional revenues and all additional costs for all capacity related PJM BLI's be allocated to customers. As shown in Mr. Swez's Direct Testimony,

¹¹⁰ Swez Rebuttal pg. 20.

¹¹¹ *Id.*

¹¹² Swez Rebuttal pp. 20-21.

customers are more likely to receive net benefits/ credits for capacity sales through the transition to full RPM auction participation.¹¹³ Anything other than a 100 percent allocation of charges and credits to customers for the participation in the capacity market results in an unfair and unreasonable allocation of costs and risks to the Company and its shareholders and also an unfair sharing of all the benefits with customers.¹¹⁴ As Mr. Swez explained the Company uses sound economic principles through an “indifference curve,” process to create its capacity offers in PJM for resources.¹¹⁵ Therefore, the Company makes capacity offers that are agnostic to eventual sharing between the customer and shareholder.¹¹⁶ Thus, for generator offers that the Company utilizes in the capacity auction, the current 90/10 sharing allocation for capacity revenues provides neither an incentive or disincentive for the Company and it is appropriate for the customer to receive 100 percent of the benefits of selling any excess capacity because the customer pays for these generating resources through base rates.¹¹⁷

¹¹³ Swez Direct pg. 13, Table 1 and Attachment JDS-1.

¹¹⁴ Swez Rebuttal pg. 23.

¹¹⁵ Swez Rebuttal pp. 22-24.

¹¹⁶ *Id.*

¹¹⁷ *Id.*

8. The Commission should not place unnecessary restrictions, ratemaking or otherwise, on the Company's ability to manage its generating portfolio for the benefit of customers.

Although Duke Energy Kentucky agrees that there should be no ratemaking incentive favoring one method of satisfying the Company's capacity requirement over another however, as Company witnesses Swez and Steinkuhl explain in their respective rebuttal testimonies, the Company does not agree that conditions should be put in place that unreasonably restrict the Company's ability to manage its portfolio, limit its ability and flexibility to meet customer demand in capacity needs in the most reasonable, reliable, and efficient manner. Moreover, no conditions or restrictions should inappropriately shift the costs between the Company and its customers. The Company's proposal to realign its participation in PJM to auction participation is because remaining in the FRR is no longer in the best interests of customers. If the Commission does not agree, then the Company will simply continue to operate as an FRR for so long as PJM rules continue to allow that possibility. It is unreasonable for the Commission to place unnecessary restrictions on the Company or to shift additional risks to the Company when it is seeking to do what is in the customers' best interests. The Company's proposal to adjust the Rider PSM to provide greater benefits of the long capacity position benefits customers. It is fair and reasonable that customers should also pay the corresponding costs. Kentucky law, Commission resource planning regulations, and the Commission's authority over the management of utilities all dictate that the Company continue to act such that it is providing reasonable service to customers, thus the impetus for this application. The Company believes that transitioning to full RPM participation is reasonable and, in the customers' best interests.

9. The Commission Should Not Exclude the Compliance and Other Penalty Expense BLIs from the PSM and Preclude the Company from Recovering These FERC Authorized and Tariffed Expenses through PSM Rates.¹¹⁸

The Commission should reject the KYOAG consulting witnesses' recommendation to exclude Compliance and Penalty Expense BLIs from Rider PSM because, as Mr. Swez explains in his rebuttal testimony, the recommendation is based upon a faulty premise, that by PJM's use of the words "compliance penalty", "deficiency", and "test failure" that the Company did something wrong or acted imprudently.¹¹⁹ PJM is revenue neutral; therefore, each of these BLIs have both a charge and a credit that go together symmetrically. Thus, BLI 1660 goes with BLI 2660, BLI 1661 goes with BLI 2661, and so forth.¹²⁰ Additionally, as he explains further, the listing of PJM BLIs cited by KYAOG consulting witness Kollen is asymmetric and one-sided, by taking the credits and benefit side provided by the BLIs but inappropriately allocating the corresponding "charging" BLIs back onto the Company. Providing customers with all of the upside and the Company with all of the downside of capacity market risks is unreasonable and untenable, thereby making the transition to RPM harmful to the Company.

Although PJM uses words such as "deficiency" to describe the charges and credits, it does not mean that the Company did something inappropriate or acted in an imprudent manner.¹²¹ As Mr. Swez testified, the Company puts significant effort and analysis into the areas covered by these BLI's, including its capacity supply offers to PJM, demand side management programs, and generating unit maintenance, doing everything possible to

¹¹⁸ *Id.* at 10.

¹¹⁹ Swez Rebuttal pp 25-29.

¹²⁰ Swez Rebuttal pg. 28.

¹²¹ *Id.* pg. 26.

avoid these types of charges.¹²² Any charge that is received under a BLI that is labeled a compliance penalty, deficiency, test failure, or other term has been or will be due to unforeseen circumstances that can't be avoided, such as a forced outage or a failed performance test.¹²³ Indeed, as Mr. Swez explained, these "charges" also include a corresponding credit. In his example describing of PJM BLI's 1390 and 2390, Fuel Cost Penalty BLI, he explained that the Company works hard to avoid failures of its fuel cost policy, including working with the PJM Independent Market Monitor (IMM) on creating the most effective fuel cost policy, actively monitoring the policy, and double checking every daily cost-based offer to ensure that it is compliance with the fuel cost policy.¹²⁴ Due to those efforts, the Company has received credits from other PJM members from BLI 2390 in every year since the charge started in 2017, with the total revenue received over \$30,000 during this time. The corresponding charge, BLI 1390, through the Company efforts, has only had one failure of its fuel cost policy resulting in a charge of \$502.¹²⁵ Witness Kollen, starting on page 4, line 16 of his testimony, lists the PJM capacity BLI's related to capacity compliance and penalties that are primarily **expenses** (1000 series) as follows:

1660 – Demand Resource Interruptible Load for Reliability (ILR) Compliance Penalty

1661 – Capacity Resource Deficiency

1662 – Generation Resource Rating Test Failure

1663 – Qualifying Transmission Upgrade Compliance Penalty

1664 – Peak Season Maintenance Compliance Penalty

1665 – Peak-Hour Period Availability

1666 – Load Management Test Failure

¹²² *Id.*

¹²³ *Id.*

¹²⁴ *Id.*

¹²⁵ *Id.*

Additionally, the PJM capacity BLI's related to compliance and penalties that are primarily **revenues** (2000 series) are as follows:

- 2660 – Demand Resource and ILR Compliance Penalty
- 2661 – Capacity Resource Deficiency
- 2662 – Generation Resource Rating Test Failure
- 2663 – Qualifying Transmission Upgrade Compliance Penalty
- 2664 – Peak Season Maintenance Compliance Penalty
- 2665 – Peak-Hour Period Availability
- 2666 – Load Management Test Failure

To exclude the capacity related compliance expenses- 1000 series BLI's from Rider PSM as Mr. Kollen suggests, but include the capacity related compliance 2000 series BLI's, listed above, results in the customer getting all of the benefits of RPM participation and would not pay for the costs of those benefits.¹²⁶ Additionally, although 1000 series PJM BLI's are *primarily* a charge and the 2000 series PJM BLI's are *primarily* a revenue, this isn't always the case. At times, 1000 series PJM BLI's can be a revenue, and 2000 series PJM BLI's can be a charge. They can change from a charge to a credit depending on activity. Thus, to exclude the 1000 series of capacity compliance and other penalty PJM BLI's from the PSM and to include 2000 series of capacity compliance and other penalty PJM BLI's in the PSM can result in denying revenues to customers.¹²⁷

As an RPM participant, the total capacity of the Company's generating resources will be offered into PJM, and the total capacity requirement will be purchased from PJM. But if the customer receives all the revenues (benefits) and none of the costs (charges), the customer has not paid for the capacity to fulfill its PJM capacity demand requirements meaning Duke Energy Kentucky is not recovering its costs of providing service and the Company's shareholders are subsidizing the benefits customers would receive.¹²⁸

¹²⁶ Swez Rebuttal pp. 27-28.

¹²⁷ Swez Rebuttal pg. 28.

¹²⁸ *Id.*

Therefore, the revenues must be offset by the costs incurred. This is no different to participation in the PJM energy market, where the total energy generated by the generating resources are sold into PJM and the total load buy is purchased from PJM. If the total generation sold is more than the total load buy, these off-system sales are included in Rider PSM. If the total generation sold is less than the load buy, the difference is a purchase of energy included in Rider FAC.

Finally, in this Application, the Company did not request any change to the two PJM BLI's related to capacity performance, BLI 1667 (Capacity Performance Non-Performance charge) and BLI 2667 (Capacity Performance Bonus Performances payment). The Commission previously approved a modification to the Rider PSM in Case No. 2017-00321 to allow the Company to include both capacity performance charges and bonus payments as part of that sharing mechanism with a 90/10 sharing mechanism where customers receive 90 percent of the net benefits/costs related to capacity performance.¹²⁹ The Commission's Order in that case, found that the Company's proposal to change to the 90/10 sharing, even factoring in the capacity performance risks, was reasonable. Indeed, that was the reason the Company made such a proposal to increase the benefit to customers from the previously Commission-ordered 75/25 split. Customers have clearly benefited from this additional revenue sharing percentage since that case and it would be unreasonable to now say customers only receive benefits and do not bear any risks simply because of a change in PJM market participation, For these reasons, the Commission should not adopt KYOAG consulting witness Kollen's unreasonable, one-sided,

¹²⁹ *In the Matter of the 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, Order (Apr. 13, 2018).

asymmetric and shareholder subsidy-creating recommendation to only include the credit-related PJM BLIs in Rider PSM.

10. Rider PSM capacity-related revenues could be modified to be allocated on demand, but the allocation of costs should not be allocated on demand.

As explained by Company witness Steinkuhl, if the Commission approves Duke Energy Kentucky's transition from an FRR to an RPM entity, the Company is not opposed to changing the allocation of capacity revenues and costs included in the PSM to be based on demand consistent with how capacity costs are allocated in base rates as recommended by KYOAG consulting witness Kollen.¹³⁰ To be consistent with the cost of service in base rates, a 12 Coincident Peak (12CP) from the most recently approved electric base rate case should be used to allocate capacity costs to residential and non-residential customers.¹³¹ The allocation change would apply to all capacity revenues and costs and the PJM capacity performance non-performance charge and bonus payments.

However, the Company does not agree that those capacity revenues and costs should be billed on a demand basis and that it should continue billing residential and non-residential customers based on kWh.¹³² Maintaining the current billing will allow the Company and the Commission time to study how any change in billing determinants will impact certain customer classes.¹³³ A shift in rate design will, by definition, result in revenue/cost shifting between customer classes and without being fully studied, has the potential to result in significant rate increases or decreases to different customer classes.¹³⁴

¹³⁰ Steinkuhl Rebuttal pg. 6.

¹³¹ *Id.*

¹³² *Id.* pg. 7.

¹³³ *Id.*

¹³⁴ *Id.*

The Company's proposal is consistent with the principle of ratemaking gradualism to make rate adjustments over time, rather than sudden changes so as to avoid rate shock to customers.¹³⁵

Additionally, at present, none of Duke Energy Kentucky rider or surcharge mechanisms are billed on a demand basis. Were the Commission to order the Company to change the rate design of the PSM to allow for demand-based billing, the Company would need to make changes to its billing system to allow for this change and the Company has not analyzed the time or cost of doing such a system change.¹³⁶ The Commission should not require the Company to make such a change without knowing the impact to customers or the costs of implementing such a change.¹³⁷

IV. Conclusion

The Company has demonstrated that its request for authorization to transition from operating as an FRR entity in PJM to full participation in the RPM auction construct is both for a proper purpose and is in the public interests. The Company respectfully submits that the Commission should enter an order authorizing: 1) Duke Energy Kentucky to exit the FRR construct and to transition to full participation in the PJM RPM BRA/IA beginning with the 2026/2027 Delivery Year; 2) amendments to the Company's Rider PSM to account for PJM capacity-related BLI revenues and charges and capacity transactions in the bilateral markets to meet PJM's FERC-approved reliability requirements; 3) reconciliation of the net capacity-related revenues and charges with customers receiving 100 percent of the benefit or costs of capacity outside of the current sharing percentages;

¹³⁵ *Id.*

¹³⁶ *Id.*

¹³⁷ *Id.*

4) any necessary accounting treatment; waivers, and approvals necessary; and 5) for expedited treatment and issue its decision no later than May 1, 2025 to effect transition as early as the 2026/2027 Delivery Year. The concerns raised by the KYOAG consulting witnesses' as to double recovery of costs are unfounded, and creating unreasonable restrictions on the Company, including unfairly shifting risks and costs to the Company's shareholders are unreasonable and unnecessary. The Commission should approve the Company's Application as filed and without material modification.

Respectfully submitted,

DUKE ENERGY KENTUCKY, INC.

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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 March 14, 2025; and that there are currently no parties that the Commission has excused from participation by electronic means in this proceeding.

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