COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

ELECTRONIC APPLICATION OF DUKE ENERGY KENTUCKY, INC. FOR APPROVAL TO AMEND ITS GAS MAIN EXTENSION TARIFF PURSUANT TO 807 KAR 5:022, SECTION 9(16)(D)	)))))	CASE NO. 2016-00298

ORDER

On August 29, 2016, Duke Energy Kentucky, Inc. ("Duke Kentucky") submitted an application requesting to revise its gas main extension policy and modify its Rider X, Main Extension Policy ("Rider X") tariff to provide a standard methodology to cost-justify gas main extensions for customers in excess of the first 100 feet which Duke Kentucky must provide at no cost pursuant to 807 KAR 5:022, Section 9(16). On September 28, 2016, the Commission issued an Order suspending the proposed October 1, 2016 effective date for five months, up to and including February 28, 2017. Duke Kentucky responded to one Commission Staff ("Staff") request for information. There are no intervenors in this proceeding, and the matter now stands submitted to the Commission for a decision.

BACKGROUND

The Commission's Administrative Regulations contain the following provisions for the extensions of the distribution mains of gas utilities to customers who request such extensions:

> KAR 5:022, Section 9(16) Extension of services.
> (a) Normal extension. An extension of 100 feet or less shall be made by a utility to an existing distribution main without charge for a

prospective customer who shall apply for and contract to use service for one (1) year or more and provides guarantee for such service.

(b) Other extensions.

1. When an extension of the utility's main to serve an applicant or group of applicants amounts to more than 100 feet per customer, the utility shall, if not inconsistent with its filed tariff, require the total cost of the excessive footage over 100 feet per customer to be deposited with the utility by the applicant(s), based on average estimated cost per foot of the total extension.

2. Each customer receiving service under such extension will be reimbursed under the following plan: each year for a refund period of not less than ten (10) years, the utility shall refund to the customer(s) who paid for the excessive footage, the cost of 100 feet of extension in place for each additional customer connected during the year whose service line is directly connected to the extension installed, and not to extensions or laterals therefrom. Total amount refunded shall not exceed the amount paid to the utility. After the end of the refund period, no refund shall be required.

(c) An applicant desiring an extension to a proposed real estate subdivision may be required to pay all costs of the extension. Each year for a refund period of not less than ten (10) years, the utility shall refund to the applicant who paid for the extension a sum equivalent to the cost of 100 feet of extension installed for each additional customer connected during the year. Total amount refunded shall not exceed the amount paid to the utility. After the end of the refund period from the completion of the extension, no refund shall be required.

(d) Nothing contained herein shall be construed to prohibit the utility from making extensions under different arrangements provided such arrangements have been approved by the commission.

(e) Nothing contained herein shall be construed to prohibit a utility from making, at its expense, greater extensions than herein prescribed, provided the same free extensions are made to other customers under similar conditions.

(f) Upon complaint to and investigation by the commission, a utility may be required to construct extensions greater than 100 feet upon a finding by the commission that such extension is reasonable.

Duke Kentucky's current Rider X reflects much of the regulation language above, providing up to 100 feet of gas main extensions at no charge to the applicant, and requiring applicants requesting extensions exceeding 100 feet to deposit with the utility the entire estimated cost of any excess footage over 100 feet. In order to make cost-effective extensions of its distribution system which are in excess of 100 feet more affordable to potential customers, Duke Kentucky proposes an addition to Rider X for a Net Present Value ("NPV") tool which it proposes to apply uniformly to requests for extensions greater than 100 and less than 2,000 feet.[1] A positive or zero NPV investment would be considered cost justified and the applicant would not be required to make a contribution in order to extend the main. A negative NPV result would indicate that the investment is not cost justified without a customer contribution to justify the project, and the applicant would be required to deposit the amount indicated by the analysis to make the extension cost-effective before construction would begin.[2]

For residential customers, the NPV calculation is proposed to include:

- Future expected revenue streams of the main extension applicant based on 20 years of usage,[3] plus estimated revenue streams of likely subsequent connections due to conversions from other energy sources based on residential conversion rates and residential revenue per home from Duke's revenue reports. Future revenue streams are proposed to be discounted to present value based on the 7.377 percent[4] weighted average cost of capital ("WACC") approved in Duke Kentucky's last rate case.

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[1] Duke Kentucky did not propose to include the parameter of less than 2,000 feet in its Rider X language addition, but intends to use that length as the upper limit, as it does in the service territory of Duke Energy Ohio, Inc. ("Duke Ohio"). For extensions longer than 2,000 feet, Duke Kentucky states in response to Commission Staff's Initial Request for Information ("Staff's First Request"), it prefers to have the flexibility to undertake a more involved cost/benefit analysis.

[2] Application, Exhibit 1, proposed Rider X tariff.

[3] Response to Staff's First Request, Item 2.f.

[4] Application, Exhibit 1, proposed Rider X tariff.

• Total cost of the requested extension, based on a rolling three-year average cost of similar projects, including pipe size and estimated footage, and fully loaded for labor, material, equipment, and general conditions such as permitting and surveys.[5]

For Commercial and Industrial customer applicants for gas main extensions in excess of 100 feet, the estimated value of future revenue streams in the NPV calculation would be based on the average usage of Duke Kentucky customers with the same business classification codes.[6] Duke Kentucky states that it may use the results of the NPV tool to calculate minimum usage requirement contracts for these customers, and require them, under some circumstances, to enter into service contracts of no more than six years.[7] According to Duke Kentucky, Duke Ohio has used an NPV tool since July 2015, following approval of its addition to its gas main extension policy by the Public Utilities Commission of Ohio.[8]

ANALYSIS

In support of its request to add the NPV tool to cost-justify extensions of over 100 feet with the possibility of less, or no, customer contributions, Duke Kentucky states that its existing policy has sometimes prevented natural gas connections for residential customers along older neighborhood streets. According to Duke Kentucky, if the potential customer requesting the extension is not immediately adjacent to the existing main, that individual must either convince his or her neighbor(s) to convert to natural

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[5] Response to Staff's First Request, Item 1.

[6] *Id.*, Item 2.h.(3).

[7] Application at 6, paragraph 11.

[8] Response to Staff's First Request, Item 4.b.

gas at the same time, or pay for the entire cost of the extension over 100 feet. Duke Kentucky describes a scenario of several potential customers using other fuel sources who live along a street with a gas main close by, all of whom will likely desire at different points in time to convert to gas, but are not in a position to share in the conversion costs at the same time.[9] Duke Kentucky believes that giving up-front credit to the main extension applicant for the applicant's own future revenue stream as well as that of other likely conversions from other fuel sources will make gas more readily available to more customers who want it, and benefit all of Duke Kentucky's gas customers by spreading its cost of service over more customers and volumes. It also emphasizes in its application that the regulation provides that the utility is not prohibited from making gas main extensions under different arrangements provided that such arrangements have been approved by the Commission.

Having reviewed the evidence of record and being otherwise sufficiently advised, the Commission finds that the proposed addition of the NPV tool to Duke Kentucky's gas main extension policy and tariff is reasonable and should be approved. The revision will enable natural gas service to be extended to more customers at a time when natural gas is generally affordable and also plentiful, and in a uniform manner that is intended to make economic sense for the utility and its other customers.

The Commission further finds that Duke Kentucky's proposed Rider X language revision should be modified to state that the NPV analysis will assume a term of no less than twenty (20) consecutive years, as Duke Kentucky stated in response to a Staff

[9] Direct Testimony of John A. Hill, pages 4–5.

request for information.[10] In conformity with Duke Kentucky's intention to utilize the NPV for all main extensions of 100 to 2,000 feet,[11] Duke Kentucky should also modify its proposed Rider X tariff language to remove the phrase "at its sole discretion" from paragraph 2.(iii) of the EXTENSION PLAN provisions, and state that it "will" (instead of "may") perform a NPV analysis on main extensions in excess of 100 and less than 2,000 feet. This will provide Duke Kentucky the flexibility it desires to perform more detailed analyses for extensions over 2,000 feet, and at the same time ensure the uniformity of treatment for extensions under 2,000 feet.

With each future gas rate case, Duke Kentucky should update the discount rate specified in its Rider X tariff for use in the NPV calculation. Duke Kentucky should also file in its next gas rate case comparative statistics regarding gas main extensions before and after the change in the gas main extension policy and tariff, including the actual annual rate of conversion from other fuel sources.

IT IS HEREBY ORDERED that:

1. An additional and alternative gas main extension policy and use of an NPV analysis tool, as revised herein, is approved for Duke Kentucky effective on and after the date of this Order.

2. Duke Kentucky's proposed Rider X tariff revision is approved with the modifications regarding the 20-year term and the requirement to perform the NPV analysis for extensions of up to 2,000 feet, as discussed herein.

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[10] Response to Staff's First Request, Item 2.f.

[11] *Id.*, Item 2.b.

3. Within 20 days of the date of this Order, Duke Kentucky shall file with this Commission, using the Commission's electronic Tariff Filing System, revised Rider X tariff sheets setting out the revisions approved herein and reflecting that they were approved pursuant to this Order.

4. As part of its next application for an adjustment of its base rates for gas service, Duke Kentucky shall submit its Rider X tariff sheet with a revised discount rate reflecting an updated WACC.

5. As part of its next application for an adjustment of its base rates for gas service, Duke Kentucky shall submit: the number of gas main extensions performed annually beginning 2012, by rate class, for gas main extensions over 100 feet; and the number of subsequent connections to gas main extensions over 100 feet that occurred each year following the issuance of this Order that involved conversions from other fuel sources.

By the Commission

ENTERED
FEB 2 0 2017
KENTUCKY PUBLIC
SERVICE COMMISSION

ATTEST:

Aaron D. Greenwell for
Executive Director

*Debbie Gates
Duke Energy Kentucky, Inc.
139 East Fourth Street
Cincinnati, OH 45201

*Kristen Ryan
Senior Paralegal
Duke Energy Kentucky, Inc.
139 East Fourth Street
Cincinnati, OH 45201

*Duke Energy Kentucky, Inc.
139 East Fourth Street
Cincinnati, OH 45202

*Duke Energy Kentucky, Inc.
139 East Fourth Street
Cincinnati, OH 45202

*Rocco O D'Ascenzo
Duke Energy Kentucky, Inc.
139 East Fourth Street
Cincinnati, OH 45201