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March 24, 2017

PARTIES OF RECORD

Re: Case No. 2016-00312

Attached is a copy of a memorandum which is being filed in the record of the above-referenced case. If you have any comments you would like to make regarding the contents of the memorandum please do so within five days of receipt of this letter.

If you have any questions, please contact Quang Nguyen, Commission Staff Attorney, at 502-782-2586.

Sincerely,

Aaron D. Greenwell for

Talina R. Mathews
Executive Director

QN/ch

Attachments

INTRA-AGENCY MEMORANDUM

KENTUCKY PUBLIC SERVICE COMMISSION

TO: Case File

FROM: Quang D. Nguyen, Assistant General Counsel

DATE: March 24, 2017

RE: Case No. 2016-00312
Electronic Application of Duke Energy Kentucky, Inc. for Deviation from Affiliate Pricing Requirements and to Amend Existing Service Agreements to Include Piedmont Natural Gas as a Party

Pursuant to a Commission Staff Notice issued on March 3, 2017, a telephonic informal conference was held on March 10, 2017, at the Commission's offices in Frankfort, Kentucky. The purpose of the informal conference was to discuss certain outstanding issues related to the application of Duke Energy Kentucky, Inc. ("Duke Kentucky"). A list of the attendees is attached hereto.

Prior to the informal conference, Commission Staff provided Duke Kentucky with the questions that would be asked at the informal conference. A copy of the questions is attached to this memorandum. In responding to the questions regarding the apparent asymmetrical nature of the transfers between Duke Kentucky and Duke Energy Ohio, Inc. ("Duke Ohio") under the current agreement, Duke Kentucky states that the joint "store room" used by Duke Kentucky and Duke Ohio is owned and operated by Duke Ohio and the inventory is recorded on Duke Ohio's books. Duke Kentucky submits purchase orders or requests for inventory that is needed by Duke Kentucky. The transfers from Duke Kentucky to Duke Ohio reflect returns or reissuance of inventory back to Duke Ohio, e.g., Duke Kentucky purchases 10 odorants but ultimately only uses or needs 8 odorants and returns two odorants to Duke Ohio.

Duke Kentucky stated transfers under the current agreement are not impacted by the relative sizes of Duke Kentucky and Duke Ohio. Rather, the arrangement is implemented and designed to have Duke Ohio operate and manage the joint store inventory and the rate of 9 percent is applied to transfers to both Duke Kentucky and Duke Ohio, which rate is based upon the relative cost of managing the joint store.

With respect to the provision in the agreement that no warranty is provided for any transferred item, Duke Kentucky stated that this provision reflects the nature of the warranties associated with the inventory in the store room. Duke Kentucky noted that the warranty is with Duke Energy Corp. and extends to all Duke Energy Corp. affiliates, including Duke Kentucky. The disclaimer is to point out that there are no additional warranties being provided by the affiliate itself.

Duke Kentucky states that 97 percent of the transfers from Duke Ohio to Duke Kentucky is directly related to the store room. This reflects the fact that Duke Ohio is managing and operating the inventories and is recording them on its books. Duke Kentucky noted that as of the date of the informal conference, there has been no effort to change the current arrangement to include Piedmont Gas. Duke Kentucky stated that the cost of each transfer will depend on the ultimate model selected and implemented, but that Duke Energy Corp. will choose the model that creates the most savings to leverage fully the economies of scale of Duke Energy Corp. Under the current arrangement, Duke Kentucky states that customers are not paying the carrying costs of the inventory.

Duke Kentucky indicated that the current affiliate agreements do not contain any conditions imposed by a regulatory agency. However, to the extent that the Commission desires certain conditions to be imposed, Duke Kentucky stated that it would accommodate any conditions required.

Duke Kentucky stated that its application simply requests to have any transaction be on par for all Duke affiliates so that no customer of an affiliate would be worse off under the arrangement. Duke Kentucky also stated that it would commit to a reporting or updating the Commission on best practices implemented by Duke Kentucky.

There being no further discussions, the informal conference was adjourned.

Attachments

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

ELECTRONIC APPLICATION OF DUKE ENERGY KENTUCKY, INC. FOR DEVIATION FROM AFFILIATE PRICING REQUIREMENTS AND TO AMEND EXISTING SERVICE AGREEMENTS TO INCLUDE PIEDMONT NATURAL GAS AS PARTY	)))))	CASE NO. 2016-00312

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March 10, 2017 Informal Conference
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Please sign in:

NAME	REPRESENTING
Quang D Nguyen	PSC
Virginia Gregg	PSC
Leah Faulkner	PSC
Gary Ebler	Duke Energy Kentucky
Ruth Campbell	Duke Energy Kentucky
Rocco D'Ascenzo	Duke Energy Kentucky
Peggy Laub	Duke Energy Kentucky
Nina Roflos	Duke Energy Kentucky
Melissa Abernathy	Duke Energy Kentucky

Via Tele-conference

Case No. 2016-00312 Telephone IC questions

With regard to Duke Kentucky's existing agreement with Duke Ohio Gas:

1. In Case No. 2008-00122, Duke KY said in its application (paragraph 12, page 6) that the transfers under the agreement "are expected to be relatively symmetrical, so that no one utility affiliate is expected to benefit disproportionately from this arrangement." The application also referenced the benefit of the agreement allowing Duke KY to acquire an inventory item from an affiliate at the affiliate's cost and in a more expeditious manner than it could from third party suppliers.
2. The response to Item 7, DR 1 in 2008-00122, laid out Duke KY's purchasing practices, indicating that transfers from an affiliate would occur only when the affiliate could provide an item in the least cost most efficient manner, and that generally purchases would be made by Duke KY from the manufacturer pursuant to blanket purchase contracts.

In Case No. 2016-00312, the response to Staff DR 1 indicates that Duke Ohio's transfers of non-capital equipment to Duke KY were as follows:

Transfers of Non-capital Equipment	Duke Ohio to Duke KY	Duke KY to Duke Ohio
2012	$489,000	$33,700
2013	$574,000	$160,000
2014	$493,000	$30,700
2015	$1,000,000	$110,800
2016	$1,900,000	$81,800

The transfer of capital items as shown in the response was similarly asymmetrical.

Provide a discussion of the magnitude of the difference in the transfers between Duke KY and Duke Ohio. The discussion should include:

1. how the relative size of the two companies impacts the disparity in the transfers;
2. whether 8% is still built in for stores, as Duke KY stated in 2008, and the impact on Duke KY of paying the 8% on the relatively larger transfer amount;
3. the impact of the Agreement provision, which is set out in all caps, that the transferring affiliate provides no warranty of the transferred item, and whether this puts Duke KY at a relative disadvantage given that the transfers do not appear to be symmetrical, as the Commission believed they would be in 2008;
4. the percentage that the transfers from Duke Ohio to Duke KY represent of Duke KY's total purchases, and the same for transfers from Duke KY to Duke Ohio;
5. whether the purchasing practices described in the 2008 response have changed to favor affiliate transfers; **current application does not contain the 2008 explanations re "special circumstances".**
6. whether the Commission could expect the cost of transfers from Piedmont to Duke KY to be higher based on higher transportation cost.
7. **explain the/any conditions imposed in N.C., S.C., and Indiana. Any in Ohio?**
8. **with respect to "the lower of cost or market rule" one could expect the question to be asked: why should Duke KY not be assured of paying cost if it's lower than market? If Duke Ohio's or Piedmont's cost is consistently higher than market, shouldn't the KY Commission be able to expect Duke KY to go to the market and pay market, and not pay its affiliates' costs which are higher than market?**

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