COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

ELECTRONIC APPLICATION OF DUKE ENERGY KENTUCKY, INC. FOR 1) AN ADJUSTMENT OF THE ELECTRIC RATES; 2) APPROVAL OF NEW TARIFFS; 3) APPROVAL OF ACCOUNTING PRACTICES TO ESTABLISH REGULATORY ASSETS AND LIABILITIES; AND 4) ALL OTHER REQUIRED APPROVALS AND RELIEF	)))))))	CASE NO. 2020-00055

O R D E R

The matter is before the Commission upon a motion for rehearing filed by Duke Energy Kentucky, Inc. (Duke Kentucky). The motion sought rehearing on certain aspects of the April 27, 2020 Order (Final Order) in this matter. Among other things, the Final Order approved a $24.124 million increase in Duke Kentucky's electric base rate. The Attorney General of the Commonwealth of Kentucky, by and through the Office of Rate Intervention (Attorney General), filed a response addressing each of the issues Duke Kentucky raised in its rehearing motion. Duke Kentucky filed a reply in support of its rehearing request. The matter now stands submitted for a decision by the Commission.

Duke Kentucky raised seven issues in its motion for rehearing. Each of the issues will be discussed along with the findings as follows.

1. Excessive Plant Additions

The first issue raised by Duke Kentucky for rehearing involves an adjustment related to excessive plant additions. Duke Kentucky argues that the Commission's determination that it included $66.324 million in forecasted plant additions in excess of its projected capital construction budget was erroneous because the analysis was based upon a comparison of tables and schedules that, according to Duke Kentucky, contain different data sets and are used for different purposes. Specifically, Duke Kentucky contends that the three-year capital construction budget, which it filed with its Application pursuant to 807 KAR 5:001, Section 16(7)(b), did not include capital spending for projects that would be recovered through its environmental surcharge mechanism (ESM), whereas its projected additions to plant in service, shown on Schedule B-2.3 and in spreadsheets filed in response to requests for information, include additions for projects that would be recovered through the ESM. Duke Kentucky contends that it made an adjustment to remove $69.086 million from plant in service during the forecasted test period, as shown in Schedule B-2.2, to remove projects that would be recovered through the ESM from plant in service, and it argued that adjustment accounted for the discrepancy between the projected capital construction budgets and plant additions noted by the Commission. Thus, Duke Kentucky asserts that the record does not support the revenue requirement reduction for excessive plant additions, which totaled $5.518 million, and that the Commission should grant rehearing to correct that error.[1]

The Attorney General contends that Duke Kentucky seeks rehearing only on the issue of how the adjustment was calculated and not on the reasonableness of the adjustment itself. The Attorney General agrees that the rehearing request should be granted to determine the calculation of the plant additions related to the ESM. The Attorney General is of the belief that the adjustment has been overstated because of the inclusion of plant additions related to the ESM. The Attorney General notes that the

[1] Duke Kentucky's Motion for Rehearing at 2–4.

correct calculation should reflect an adjustment of $28 million, which is the difference between the entire plant related to ESM in the test year of $69 million and the entire plant related to ESM in the base year of $48 million.

On reply, Duke Kentucky contends that it specifically requests rehearing with respect to not only the calculation of the excessive plant addition adjustment, but also that the adjustment itself is not reasonable. Duke Kentucky also contends that the Attorney General's proffered calculation of the excessive plant addition is erroneous.

As an initial matter, the Commission rejects Duke Kentucky's contention that the three-year capital construction budgets filed pursuant to 807 KAR 5:001, Section 16(7)(b), should not be compared to additions to its plant in service to assess the reasonableness of those additions. Commission regulations require a utility using a forecasted test year to base its forecasts on the same assumptions and methodologies used by management or to explain when and why different assumptions and methodologies are used.[2] The reason for that requirement, at least in part, is that information prepared in the ordinary course of business is seen as more reliable than information prepared specifically to advocate for a position in court or before an administrative agency.[3] The requirement in 807 KAR 5:001, Section 16(7)(b), that a utility using a forecasted test year file its "most

[2] *See* 807 KAR 5:001, Section 16(7)(e) (stating that a utility must attest that an application for a rate adjustment based on a forecasted test period is based on a forecast that "contains the same assumptions and methodologies as used in the forecast prepared for use by management, or an identification and explanation for differences that exist, if applicable").

[3] *See, e.g. United States v. Kim*, 595 F.2d 755 (D.C. Cir. 1979) (noting that business records prepared in the ordinary course of business are presumed to be trustworthy because a business that relies on its records will ensure that those records are accurate); *Johnson v. Manitowoc Boom Trucks, Inc.*, 484 F.3d 426, 434 (6th Cir. 2007) ("This Court has recognized for some time that expert testimony prepared solely for purposes of litigation, as opposed to testimony flowing naturally from an expert's line of scientific research or technical work, should be viewed with some caution.").

recent capital construction budget containing at a minimum a three (3) year forecast of construction expenditures," along with related filing requirements, serves the purpose of providing the Commission with information regarding a utility's actual capital construction budgets, prepared in the ordinary course of business, that can be compared with the plant in service a utility used to calculate its revenue requirement.

Here, Duke Kentucky specifically indicated that it based its projected plant additions on its most recent capital construction budget[4] and that the budget filed pursuant to 807 KAR 5:001, Section 16(7)(b), contained "the most recent capital construction budget containing the forecasted construction expenditures for a minimum of three years."[5] Further, while the budget filed pursuant to Section 16(7)(b) does indicate that it does not include projects recovered through the ESM, Duke Kentucky's witnesses, James Mosley and Ash Norton, indicated that they provided the information in the budget to Christopher Jacobi, who was responsible for forecasting plant additions, "for [his] use for the forecasted financial data."[6] Thus, it was logical and reasonable for the Commission to examine the projected capital construction budgets filed pursuant to Section 16(7)(b) to assess the plant in service Duke Kentucky used to calculate rates.

The Commission recognizes that adjustments were made to the projected capital construction budgets to reach the plant in service used to calculate rates and notes that those adjustments were the subject of significant investigation in this matter. For instance, Mr. Jacobi noted that he made adjustments to the projected capital construction

[4] February 19, 2020 Hearing Video Transcript (HVT) at 15:54:10-15:57:34.

[5] Direct Testimony of Christopher M. Jacobi (Jacobi Testimony) at 26; Direct Testimony of James Michael Mosley (Mosley Testimony) at 16; and Direct Testimony of Ash M. Norton (Norton Testimony) at 16.

[6] Mosley Testimony at 16; Norton Testimony at 16, *see also* Jacobi Testimony at 23.

budgets based on updated estimates and time of spending,[7] but stated that those updates were included in the filing made pursuant to Section 16(7)(b).[8] Duke Kentucky also indicated that projected capital construction budgets were adjusted based on when the relevant projects would have to be placed in service,[9] and the Commission addressed that issue in the final Order. However, after being questioned extensively about adjustments made to projected capital expenditures to project additions compared to plant in service, Duke Kentucky's witness, who was responsible for projecting the additions to plant in service and who sponsored the projected capital construction budget filed pursuant to Section 16(7)(b), was not able to explain why the additions to plant in service in 2019 and 2020 exceeded the projected capital expenditures that possibly could have been placed in service during that period.[10]

Duke Kentucky now explains the discrepancy by pointing to an adjustment in Schedule B2.2 reducing the 13-month average plant in service in the forecasted test period by $69.0863 million to remove "assets recovered through the ESM rider."[11] Given that Duke Kentucky has the burden of establishing that its proposed rates are reasonable,

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[7] Jacobi Testimony at 20.

[8] February 19, 2020 HVT at 15:54:10-15:57:34.

[9] Duke Kentucky's response to Commission Staff's Second Request for Information (Staff's Second Request), Item 7(d) ("Forecasted additions are the result of projected capital spend, generally within a few categories (project classes) per FERC function, and assumptions for when that capital spend will be placed in service.").

[10] February 19, 2020 HVT at 16:331:15-16:33:36; *see also* Duke Kentucky's response to Staff's Second Request, Item 8 (in which Duke Kentucky provided a schedule showing plant additions within 17 categories by month for only the forecasted test period when asked to "[b]riefly describe the expected projects and capital expenditures, provide the total expected cost of the projects and capital expenditures, provide the date when Duke Kentucky expects work on any projects identified to begin, and the date on which Duke Kentucky expects any project identified to be placed in service" for projects or capital expenditures shown as additions on Schedule 2.3 in the base and forecasted periods).

[11] Schedule B2.2, page 2 of 2.

evidence of that adjustment alone would not justify granting rehearing on this issue because it is possible that Duke Kentucky was removing plant placed in service prior to 2019 and therefore would not be included in the relevant additions. There is evidence that may have occurred in this case, as the adjustment removing plant recovered through the ESM was made to an account that did not show $69.086 million in additions to plant in service during the relevant period.[12] This would indicate the adjustment was made to remove items that were placed in service prior to that period if the adjustment was made on a comparative basis.

However, Duke Kentucky adjusted plant in service at the end of the base period by only $41.089 to remove assets recovered through the ESM.[13] This indicates that Duke Kentucky adjusted plant in service for the forecasted test period to remove additional plant that was placed in service at some point between the end of the base period and the end of the forecasted test period. Consequently, the evidence does not support simply accepting Duke Kentucky's conclusion that the adjustment removing plant recovered through the ESM would account for the discrepancy between budgeted capital expenditures and plant additions. However, the Commission finds that because Duke Kentucky failed to provide sufficient data that would support a logical definitive conclusion a rehearing is necessary on this issue to investigate whether and to what extent the removal of plant recovered through the ESM accounts for the difference.

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[12] *See* Schedule B2.1, page 7 of 12 (showing the $69.086 million adjustment being made to plant in service in FERC Account No. 311); Duke Kentucky's response to Staff's Second Request, Item 6 (d), STAFF-DR-02-006 Attachment (showing additions to FERC Account No. 311 during the base period and the balance at the end of the base period); and Duke Kentucky's response to Staff's Second Request, Item 7(c), STAFF-DR-02-007 Attachment (showing additions to FERC Account No. 311 during the forecasted test period and the balance at the beginning of the test period).

[13] Schedule B2.2, page 1 of 2.

2. Depreciation Expense

Duke Kentucky argues that the $7.446 million revenue requirement reduction associated with the finding that Duke Kentucky should continue to utilize the depreciation rates approved in Case No. 2017-00321[14] is unreasonable. Duke Kentucky contends that the Commission erred in determining that there had been no significant change in the depreciation parameters, noting that total investments increased significantly through the end of the test year, which results in increased depreciation expense absent any change in assumptions such as asset life. Duke Kentucky also points out that there is no finding with respect to any extension in useful life, which would negate the increase in depreciation expense from increased investment in Steam Production Plant, Other Production Plant, and Distribution Plant. Duke Kentucky argues that this omission undermines the premise that the change in depreciation rates is unwarranted.

Duke Kentucky further contends that the effect of the disallowance is to unreasonably defer the recovery of its investment in plant and equipment until some point in the future. This, according to Duke Kentucky, violates the matching principle in that future generations of ratepayers will be forced to pay for investments that benefitted current generation of ratepayers.

The Attorney General states that the industry norm for review and reconsideration of depreciation rates is no more frequent than three to five years. The Attorney General points out that Duke Kentucky's current depreciation rates were established less than two years ago in its last rate case and that its proposed depreciation rates in the instant matter

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[14] Case No. 2017-00321, *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* (Ky. PSC Apr. 13, 2018).

are unduly aggressive and unnecessary. The Attorney General argues that Duke Kentucky failed to present evidence to justify an increase in depreciation rates so soon after rates were set based upon estimates for the same expenses the company requested in the last rate case. The Attorney General further states that the Commission's decision is appropriate and reasonable on this issue as Duke Kentucky is still allowed to recover all prudent and reasonable plant costs through depreciation expense, but should not be permitted to accelerate recovery of those costs through the proposed increase in depreciation rates.

Should the Commission consider granting rehearing on the depreciation expense adjustment, the Attorney General contends that a further review of Duke Kentucky's decommissioning estimates is warranted to exclude contingencies and reflect current dollars for the terminal net salvage component for the depreciation rates proposed for the East Bend and Woodsdale plant accounts. The Attorney General further contends that the Commission should extend the Woodsdale Station's probable retirement date to 2042 rather than 2032 as proposed by Duke Kentucky and increase the lifespan by from 40 years to 50 years.

On reply, Duke Kentucky argues that the Attorney General's contention that Duke Kentucky is seeking to accelerate its recovery through increased depreciation expense is not accurate. Duke Kentucky points out that its depreciation expense increased as a result of necessary investments in certain plant assets and that those investments did not extend the service lives of those particular plant assets. Duke Kentucky contends that allowing recovery for the increased depreciation expense permits the company to maintain the pace of fully recovering its investment during the useful life of the assets.

With respect to the timing of the recovery of the proposed depreciation expense, Duke Kentucky asserts that any delay of recovery of otherwise reasonable depreciation expense benefits current customers to the detriment of future customers and that this generational inequity will grow in proportion to the interval between the resetting of depreciation rates.

Having reviewed the relevant record, the rehearing pleadings, and being otherwise sufficiently advised, the Commission finds that Duke Kentucky's request for a rehearing regarding the adjustment for depreciation expense should be denied.

Duke Kentucky's primary argument for granting rehearing is that the Commission erred in rejecting its depreciation expense because the Commission acknowledged that total investments increased significantly through the end of the test year and that increase would necessarily increase the depreciation rate absent a change in the remaining useful life of the assets included in plant in service. However, the depreciation expense proposed by Duke Kentucky was not calculated by looking at the plant in service in forecasted test period and determining the remaining useful lives of the assets included therein. Rather, Duke Kentucky's witness calculated depreciation expense as of December 31, 2018, using the plant in service as of that date, its estimates of the remaining useful lives of assets in plant as of that date, and its estimates of the salvage value for the plant in service as of that date. Duke Kentucky then simply used its calculated depreciation expense as of December 31, 2018, which itself was an estimate of when capital expenditures for plant in service should be expensed, to calculate composite depreciation rates for the various plant accounts that it then used to estimate its depreciation during the forecasted test period.[15]

Although it is not uncommon for utilities to project their depreciation expense using this method, there are issues with using Duke Kentucky's depreciation study in this case. Between the depreciation study used to calculate depreciation rates in Case No. 2017-00321 and the depreciation study in this case, Duke Kentucky indicated that it had significant plant additions arising from improvements to assets that Duke Kentucky projected would not increase the useful lives of the assets improved. In fact, Duke Kentucky noted that the bulk of the increase in its composite depreciation rates arose from those plant additions as of December 31, 2018, that did not increase the composite remaining useful life of Duke Kentucky's plant in service.[16]

Additions to plant in service would generally affect the useful lives of plant and would generally extend the composite remaining useful life for the account to which the plant was added. There are accounting rules, which apply in most such situation, that specifically prohibit spending on existing plant from being capitalized unless it constitutes a substantial addition or a substantial betterment.[17] Further, new plant additions, as distinguished from capital spending on existing plant, would be at the beginning of their

[15] Direct Testimony of John Spanos at 2; Duke Kentucky's 2018 Annual Depreciation Study.

[16] *See* Rebuttal Testimony of John Spanos at 2 ("I also note that, while the depreciation study results in an increase in depreciation expense, most of this increase is not due to changes to service lives and net salvage recommended in the study. Instead, most of the increase is due to large capital additions at the Company's generating facilities."); *see also* Duke Kentucky's Motion for Rehearing at 7 (indicating that the increase in expense associated with the change in the rate, as opposed to the application of the existing rate to plant additions, is driven by plant additions within certain categories of plant).

[17] CFR Title 18, Chapter 1, Subchapter C, Part 101, Electric Plant Instructions, 10. Additions and Retirements of Electric Plant.

life cycle such that it would extend the average remaining life of the plant in service recorded in the account to which it was added, because the account would contain similar property of an older vintage.[18] Thus, even assuming the remaining useful lives it estimated for its plant in service as of December 31, 2018, were accurate, the resulting increase in depreciation rates used by Duke Kentucky to estimate depreciation in the forecasted test year would have arisen from an unusual situation in which Duke Kentucky had significant additions to plant in service that did not extend the remaining useful lives of its plant in service.

However, when Duke Kentucky calculated depreciation rates in December 31, 2018, it was in the beginning of a significant capital spending campaign. Duke Kentucky projected at least $389.358 million in additions from January 2019 through the end of the forecasted test period in March 2021.[19] Those additions, which would constitute about 37.8 percent of Duke Kentucky's net plant in service as of December 31, 2018,[20] were not included in Duke Kentucky's calculation of depreciation rates, and it is unlikely that those additions, collectively, would have the effect of increasing plant in service without increasing the remaining useful lives of Duke Kentucky's plant in service for the reasons discussed above. Thus Duke Kentucky's calculation of its depreciation rates as of

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[18] *See* Duke Kentucky's 2018 Annual Depreciation Study at 50-4 (discussing how Duke Kentucky's expert calculated the composite remaining useful lives of its plant in service).

[19] This amount was calculated by taking the additions from January 2019 through November 2019 as shown on Duke Kentucky's Response to Staff's Second Request, Item 6 (d), STAFF-DR-02-006 Attachment, the additions in the forecasted test period as shown on Duke Kentucky's Response to Staff's Second Request, Item 7(c), STAFF-DR-02-007 Attachment, and the difference in plant in service between the end of November 2019 and the end of March 2020 as shown on those documents.

[20] $389,358,000 / $1,029,087,018 = 0.378 x 100 = 37.8%

December 31, 2018, is unlikely to be representative of Duke Kentucky's depreciation rates during the forecasted test period.

A utility proposing a rate increase has the burden of proving that its proposed increase is reasonable.[21] While the Commission's Final Order allowed Duke Kentucky to increase its depreciation expense to recover depreciation expense on plant additions through the forecasted test year at the depreciation rate established in Case No. 2017-00321, Duke Kentucky failed to establish that its proposed increase in depreciation expense arising from its projected increase in depreciation rates was reasonable.

The Commission also believes that using the depreciation rates calculated in Case No. 2017-00321 is reasonable in this case. Those depreciation rates were based on a depreciation study performed by Duke Kentucky in that case, and as noted by the Attorney General's expert, Duke Kentucky's own depreciation expert testified that it is reasonable to rely on such studies to project depreciation expense in future periods for 3 to 5 years.[22] Further, the depreciation rates calculated in Case No. 2017-00321 were based on depreciation expense that was calculated before Duke Kentucky reflected the large additions to plant in service that, according to Duke Kentucky, did not extend the composite remaining useful life of Duke Kentucky's plant, so the Commission believes that the rates from that case will more closely reflect the depreciation rates in the forecasted test period given the amount of capital spending projected by Duke Kentucky after December 31, 2018, and the likelihood that it will, on average, extend the remaining useful life of Duke Kentucky's plant in service.

[21] *Kentucky American Water Company v. Kentucky Public Service Commission*, 847 S.W.2d 737, 741 (Ky. 1993).

[22] Kollen Testimony at 46.

Furthermore, contrary to Duke Kentucky's example, it will not be denied recovery of increased investment if its revised depreciation rates are not accepted. Duke Kentucky's depreciation expense is based on its forecasted gross plant in service of $1,949.360 million, which includes significant additions to its Case No. 2017-00321 gross plant in service of $1,730.844 million. The depreciation study filed in Case No. 2017-00321 is not unreasonably outdated and continuing to use the depreciation rates from that study does not deprive Duke Kentucky of recovery of its investment.

3. Disallowed Depreciation Expense Double Counting

To the extent the Commission denies Duke Kentucky's rehearing regarding the adjustments for excessive plant additions and depreciation expense, Duke Kentucky maintains that the calculation of the adjustment to keep the depreciation rates unchanged from its last rate case should be corrected. Duke Kentucky contends that there appears to be a double counting of the reduction in depreciation expense in arriving at the revenue requirement reductions. Duke Kentucky states that the adjustment to reduce depreciation rates was calculated based upon the as-filed plant in service and resulted in a $7.431 million reduction in depreciation expense. Duke Kentucky asserts that if the Commission is going to modify the company's as-filed plant in service, then the newly adjusted plant in service balances must be used to calculate the adjustment, not the as-filed plant in service balances that were determined to be excessive. Duke Kentucky proposes an adjustment of $0.201 million, calculated by comparing the as-filed and existing depreciation rates and the 13-month average disallowed plant.

The Attorney General states that Duke Kentucky's argument is dependent upon whether the Commission used the company's proposed depreciation rates in its calculation of the depreciation expense on the disallowed plant additions or the existing depreciation rates. If the former, the Attorney General contends that Duke Kentucky is correct and that the company is incorrect if the calculation is based on the latter.

Having reviewed the relevant record, the rehearing pleadings, and being otherwise sufficiently advised, the Commission finds that the request for rehearing on depreciation rates should be denied. The Commission further finds that Duke Kentucky's proposed adjustment would allow it to recover depreciation expense on plant not included in the test year. The Final Order correctly calculated depreciation expense adjustments for both the decreased rates and disallowed plant additions. The Commission notes that the adjustment to reduce depreciation rates used the as-filed plant balances. The adjustment to depreciation expense related to the disallowed plant additions used the existing depreciation rates. If Duke Kentucky's proposed adjustment were accepted, the incremental difference between the depreciation rates would be recovered for disallowed plant additions, which would result in an unreasonable outcome.

4. <u>Amortization of Excess Accumulated Deferred Income Taxes</u>

Duke Kentucky requests that the Commission grant rehearing to clarify the manner in which the Commission required Duke Kentucky to account for its amortization of excess Accumulated Deferred Income Taxes (ADIT). It asserts that the Final Order could be interpreted as:

> (1) Requiring Duke Kentucky to capture the difference between the 2018 Average Rate Assumption Method (ARAM) amortization and the projected test period amortization, when actual ARAM is determined for the forecasted period, and hold that amount as an unprotected regulatory liability for each year rates are in effect until the next rate proceeding; or

(2) Requiring Duke Kentucky to capture the difference between the 2018 ARAM amortization and the actual amortization for all future periods (e.g., 2022, 2023) as an unprotected regulatory liability to be addressed in a future rate proceeding.[23]

Duke Kentucky argues that if the Final Order was intended to be read pursuant to its first interpretation the Final Order would not violate federal normalization rules because that methodology would allow for "consistency in rates for EDIT, ADIT, tax expense, and book depreciation since they would all be based on data from the projected test period."[24] Duke Kentucky argues that if the Final Order was intended to be read in a manner consistent with its second interpretation that the Final Order would violate federal normalization rules unless Duke Kentucky also tracked a number of other items to be trued up in the next rate case. Duke Kentucky contends that rehearing is necessary to clarify the intent of the Final Order.[25]

Although the Attorney General does not believe that rehearing is necessary in this matter generally, he does not take a position on this issue in particular. To the extent the Commission grants rehearing, the Attorney General opposes any true-up to ADIT, tax expense, and book depreciation.

Having reviewed the relevant record, the rehearing pleadings, and being otherwise sufficiently advised, the Commission finds that rehearing is not warranted on this issue, because the Final Order is clear and allows Duke Kentucky to record the amortization of

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[23] Duke Kentucky's Motion for Rehearing at 11-2 (filed May 18, 2020).

[24] *Id.*

[25] *Id.* at 12.

excess ADIT in a manner that Duke Kentucky acknowledges is consistent with the federal normalization rules. Specifically, the Final Order required Duke Kentucky to:

> attribute the amortization of excess ADIT in base rates to protected excess ADIT to the extent allowed by ARAM *in the forecasted test period*, to be calculated when Duke Kentucky has the information to do so . . . with any remainder allocated to unprotected excess ADIT [emphasis added].[26]

The Final Order noted that this would require Duke Kentucky to record the total amortization of excess ADIT in rates in the forecasted period—i.e., the sum of the amortization of excess protected and unprotected federal ADIT in rates—as the amortization of excess protected ADIT to the extent allowed by ARAM in the forecasted period—April 2020 through March 2021—until Duke Kentucky's next rate case. The Final Order observed that this would not result in a change in the rates set in this case, but that it would result in the balance of unprotected federal ADIT, which is a regulatory liability, being larger in the next rate case if, as expected, the test year ARAM amortization is larger than the 2018 ARAM amortization.[27]

Duke Kentucky's first interpretation of the Commission's Final Order as requiring it to capture the difference between the 2018 ARAM amortization and the ARAM amortization of excess protected ADIT in the test period and hold that amount as an unprotected regulatory liability for each year rates are in effect until the next rate proceeding is consistent with the requirements in the Commission's Final Order. The Commission contends that was clear in the Final Order but to the extent that it was not, it should be clear now. Further, as Duke Kentucky acknowledges, the treatment required

[26] Final Order at 34 (Ky. PSC Apr. 27, 2020).

[27] *Id.* at 31–2.

by the Commission is consistent with federal normalization requirements.[28] Thus, there is no basis for granting Duke Kentucky's request for rehearing regarding how the amortization of excess ADIT should be treated and, therefore, Duke Kentucky's motion is denied with respect to that point.

5. Return on Equity (ROE)

Duke Kentucky acknowledges that the 9.25 percent ROE established in the Final Order is within the range of its own expert's analysis, but argues that it is among the lowest, if not the lowest ROE awarded to a vertically integrated utility in the first Quarter 2020. In addition, Duke Kentucky claims that it is 25 basis points below what its expert considered a "bare bones" award, the omission of flotation costs notwithstanding. Duke Kentucky also opines that the Commission has moved away from its reliance of ROEs awarded to other utilities around the country as a key consideration.

Duke Kentucky goes on to argue that the award does not seem to correlate with the Commission's recent ROE awards to less risky water and natural gas utilities. Finally, Duke Kentucky argues that the award makes it more likely to experience financial stress and make it more difficult to compete in capital markets.

The Attorney General expresses strong opposition to this rehearing issue, arguing that the awarded 9.25 percent ROE was within the range of appropriate ROEs offered by Duke Kentucky's own expert witness and that the 9.25 percent ROE was above what the Attorney General had recommended at 9.00 percent. The Attorney General contends

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[28] Even if it turns out that it is not consistent with federal normalization requirements, due to a subsequent interpretation of the relevant statutes and regulations or some other circumstance, adjustments could be made in future proceedings, before the treatment had any rate effect, to avoid a penalty for a normalization violation. *See* Private Letter Ruling 201334036, 2013 WL 4496049 (issued Aug. 23, 2013) (indicating that inadvertent violations of the normalization requirements will not result in the imposition of normalization penalties if they are corrected when discovered).

that Duke Kentucky did not challenge the Commission's analysis, which fully considered the complex evidence provided by the parties on this issue.

On reply, Duke Kentucky asserts that the Attorney General's objections to the company's rehearing request is identical to the arguments that the Attorney General made in his post-hearing brief. Duke Kentucky contends that the Attorney General's arguments do not address the issue that the factors relied upon by the Commission in awarding Duke Kentucky a 9.725 percent ROE in Case No. 2017-00321 have not changed and that the ROE awarded in the instant matter does not permit Duke Kentucky to earn a return commensurate with returns on other enterprises with similar risk profiles.

Having fully reviewed the relevant record, the rehearing pleadings, and being otherwise sufficiently advised, the Commission finds that the request for rehearing on ROE should be denied. Duke Kentucky does not present any new information and simply argues that the award is too low. Further, the award is within Duke Kentucky's ROE expert's range of ROEs and this is acknowledged by Duke Kentucky. The Commission's awarded ROE is within the ranges of both Duke Kentucky's expert's revised ROE recommendations which include flotation costs and that of the Attorney General.

METHODOLOGY	ROE
DCF – Value Line Growth	9.5%
DCF – Analyst Growth	8.4%
CAPM	8.7%
ECAPM	9.7%
Historical Risk Premium	10.2%
Allowed Risk Premium	10.2%

The Attorney General's ROE recommendations are presented below:

SUMMARY OF ROE ESTIMATES

DCF Methodology	
Average Growth Rates	
High	9.45%
Low	8.00%
Average	8.53%
Median Growth Rates	
High	9.09%
Low	7.75%
Average	8.48%
CAPM Methodology	
Forward-looking Market Return:	
Current 30-Year Treasury	7.73%
D&P Normalized Risk-free Rate	8.01%
Historical Risk Premium:	
Current 30-Year Treasury	5.97% - 6.42%
D&P Normalized Risk-free Rate	6.65% - 7.11%

Duke Kentucky also requests the Commission to provide further clarification as to its purported departure from its most recent precedent in establishing the 9.25 ROE in the instant matter. Duke Kentucky states that the "primary factors" relied upon by the Commission in awarding a 9.725 ROE in 2018 has not changed. Duke Kentucky points out those factors as being the company's highly concentrated generation portfolio, ROEs of other utilities being used as a benchmark, continuing lack of diversity in Duke Kentucky's generation fleet, and a lower ROE compared to other utilities would cause financial stress. What Duke Kentucky fails to point out is that its own analysis in the instant case, as pointed out above, results in a proposed ROE range that was significantly lower than the ROE range as developed in the company's analysis in Case No. 2017-00321. In the last rate case, Duke Kentucky recommended a 10.3 percent ROE based upon an analysis that resulted in a range of ROE from 9.0 percent to 10.7, adjusted for flotation cost. Duke Kentucky's ROE analysis in the instant matter produced a much lower ROE range of 8.4 percent to 10.2 percent, reflecting and incorporating economic conditions that were different now as compared to 2018. The Commission weighed the evidence presented and believes the awarded ROE is fair, just, and reasonable.

6. Incentive Compensation Calculation

Duke Kentucky points out that the calculation for an adjustment associated with executive incentive compensation is incorrect. Duke Kentucky notes that the Final Order reflects a $0.661 million adjustment, which should have been $0.611 million based upon the discovery response cited in the Final Order.

The Attorney General states that to whatever extent a clerical error has or has not been made with respect to the adjustment at issue, the record speaks for itself. The Attorney General further states that he yields to the Commission's review and decision on this issue.

Having reviewed the relevant record, the rehearing pleadings, and being otherwise sufficiently advised, the Commission finds that there was an error inputting the incentive compensation adjustment and the correct number is $0.611 million. Accordingly, the Commission finds that Duke Kentucky should be granted rehearing on this issue and that the effect of correcting this error is an increase in the revenue requirement of $0.050 million.

7. LED Outdoor Lighting Tariff

Duke Kentucky's proposal to add a monthly payment option for additional necessary facilities to Rate LED was denied without prejudice because of concerns regarding customers choosing the monthly payment option having to pay the monthly amount in perpetuity. Duke Kentucky argues that the disparity between the amounts paid by customers who pay for the additional facilities upfront and those that choose the monthly payment option is intended to account for the fact that the Duke Kentucky invested capital and the customer needs to pay all costs associated with Duke Kentucky's investment, including financing costs when applicable. Duke Kentucky argues that customers who choose the monthly payment option receive the full benefit of the lighting service before Duke Kentucky recovers its investment. Duke Kentucky claims that the objective is for both types of customers to receive a similar service over the full period of a lighting agreement (minimum of ten years) without the upfront paying customer having to subsidize the monthly paying customer. Duke Kentucky contends that its costs are higher when a customer defers payment for the additional facilities and that the cost is no different than the investment made for fixtures, poles, pole foundations, brackets and wiring listed in Rate LED.

Duke Kentucky also claims that the rates for Rate LED were not adjusted for the newly authorized ROE.

The Attorney General contends that rehearing is not required for this issue, noting that the proposed design of this rate structure would have created a system in which customers would have been charged potentially differing amounts based on whether the charges were paid upfront or over time and the differential would have depended largely on the useful life of the fixture. The Attorney General further contends that allowing a monthly charge to be made of customers in perpetuity is an inequitable way to compensate Duke Kentucky for the financing costs.

On reply, Duke Kentucky asserts that the rate structure is designed such that a customer paying the costs of the additional facilities upfront would receive the same benefits as a monthly paying customer while mitigating against the potential for the upfront paying customer subsidizing the monthly paying customer. Although it acknowledges that a monthly paying customer would pay an amount that differs from an upfront paying customer for the same additional facilities, Duke Kentucky states that the purpose of the rate structure is to achieve fairness between customers who elect to pay those costs over time and those who are willing to pay for those costs upfront.

Having reviewed the relevant record, the rehearing pleadings, and being otherwise sufficiently advised, the Commission finds that rehearing should be granted on this issue in order to obtain more information and to inquire as to why this provision was not structured similarly to Duke Kentucky's Rate OL-E, Outdoor Lighting Equipment Installation, which has been in Duke Energy's tariff in its current form since at least 2007. Under Rate OL-E, customers pay a monthly system charge based on Duke Kentucky's costs of purchasing and installing the system and a monthly maintenance charge. The monthly system charge ends upon the expiration of the initial agreement term while the monthly maintenance charge continues for the life of the equipment. In addition, the monthly system charge can be reduced by making an upfront payment. Setting the Rate LED provision up similar to Rate OL-E could alleviate that concern, as the customer would only pay the monthly system charge up to the expiration of the initial term of the agreement, which for Rate LED is a minimum of ten years. After the initial term, the customer, including those that paid the entire cost upfront, would still pay the monthly maintenance charge.

Regarding Rate LED rate development, the Commission notes that the LED rates were increased based upon the change in the revenue requirement. The rates were originally developed in Case No. 2017-00321.[29] In the instant case, Duke Kentucky did not update the rates to reflect their proposed ROE, but only increased the rates based upon the proposed revenue requirement. However, Duke Kentucky did propose additional fees for the costs of pole foundations, brackets, or wiring equipment as a monthly charge. Duke Kentucky stated in a discovery response that originally LED rates did not include such costs since customers would pay for these upfront; however, Duke Kentucky noted that based upon feedback received, customers prefer to pay a monthly fee for everything rather than an upfront charge for some equipment and monthly charges for the poles and fixtures.[30] Duke Kentucky did not include support for these monthly charges and they were hard coded into the billing analysis. The Commission grants rehearing on this issue to obtain the cost justification for the LED pole foundations, brackets, and wiring and will update those accordingly.

IT IS HEREBY ORDERED that:

1. Duke Kentucky's motion for rehearing is granted in part and denied in part as discussed in the findings herein.

2. The procedural schedule set forth in the Appendix to this Order shall be followed for the processing of this matter on rehearing.

3. The Final Order shall be amended to the limited extent as set forth in the findings herein.

[29] Case No. 2017-000321, *Duke Energy Kentucky, Inc.* (Ky. PSC Apr. 13, 2018).

[30] Duke Kentucky's response to Staff's Second Request, Item 65.

4. All other provisions of the Final Order shall remain in full force and effect.

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By the Commission

ENTERED

JUN 04 2020 rcs

KENTUCKY PUBLIC SERVICE COMMISSION

ATTEST:

Acting General Counsel

APPENDIX

APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE COMMISSION IN CASE NO. 2019-00271 DATED JUN 04 2020

All initial requests for information to Duke Energy Kentucky, Inc. (Duke Kentucky) shall be filed no later than 06/19/20

Duke Kentucky shall file responses to initial requests for information no later than 07/06/20

All supplemental requests for information to Duke Kentucky shall be filed no later than 07/20/20

Duke Kentucky shall file responses to supplemental requests for information no later than... 08/03/20

Duke Kentucky or any Intervenor shall request either a hearing or that the case be submitted for decision based on the record no later than 08/10/20

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