BEFORE

THE PUBLIC UTILITIES COMMISSION OF OHIO

In the Matter of the Application of Duke Energy Ohio, Inc., for Authority to Change Accounting Methods.	)))	Case No. 19-1873-GE-AAM

APPLICATION OF DUKE ENERGY OHIO, INC., FOR AUTHORITY TO ESTABLISH A REGULATORY ASSET FOR PENSION SETTLEMENT ACCOUNTING

Comes now Duke Energy Ohio, Inc., (Duke Energy Ohio or Company) and states as follows:

1. Duke Energy Ohio, Inc., (Duke Energy Ohio or the Company) is an electric light company as defined in Revised Code (R.C.) 4905.02(A) and 4905.03(C), and a natural gas company within the meaning of R.C. 4905.02(A) and 4905.03(E). As such, Duke Energy Ohio is a public utility subject to the jurisdiction of the Public Utilities Commission of Ohio (Commission).

2. Under R.C. 4905.13, the Commission "may establish a system of accounts to be kept by public utilities" and "may prescribe the manner in which such accounts shall be kept."[1] The Federal Energy Regulatory Commission (FERC) has established a Uniform System of Accounts (USOA) for both electric and gas utilities. This system of accounts is applicable to Ohio's regulated electric and gas utilities only to the extent it has been adopted by the Commission.

3. Under this authority, the Commission has determined, through the promulgation of Ohio Administrative Code (O.A.C.) 4901:1-9-05(A) and 4901:1-13-13(A), that electric and

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[1] R.C. 4905.13.

natural gas utilities shall keep their books of accounts and records in accordance with the FERC-prescribed USOA except to the extent that the provisions of said USOA are inconsistent in any way with any outstanding orders of the Commission.[2] Further, both O.A.C. 4901:1-9-05(B) and 4901:1-13-13(B) authorize the Commission to require the creation and maintenance of additional accounts.[3]

4. Through this Application, Duke Energy Ohio respectfully requests that the Commission approve the establishment of a regulatory asset and liability for the income statement impacts, including gains and losses, arising from Pension Settlement Accounting.

5. Pension Settlement Accounting is prescribed by the United States Generally Accepted Accounting Principles (U.S. GAAP) under Accounting Standard Codification 715-30 and is an irrevocable transaction that relieves an employer of primary responsibility for benefit obligations under a benefit plan and eliminates significant risks related to the obligation and assets used to affect the settlement. Pension Settlement Accounting triggers recognition in earnings of any gains or losses from settlements equal to the percentage of the settled obligations when the cost of all settlements during a year is greater than the sum of the service cost and interest cost component of net period pension cost for the pension plan for the year.

6. The net periodic pension cost is the amount recognized in an employer's financial statements as the cost of a pension plan for a period. The term net periodic pension cost is used instead of net pension expense because the service cost component recognized in a period may be capitalized as part of an asset such as inventory. Components of net periodic pension cost under Accounting Standards Codification (ASC) 715 are:

[2] *See* O.A.C. 4901:1-9-05(A) and 4901:1-13-13(A).
[3] *See* O.A.C. 4901:1-9-05(B) and 4901:1-13-13(B).

- Service cost. Service cost is the actuarial present value of benefits attributed by the plan's benefit formula to services rendered by employees during the period.
- Interest cost. Interest cost is the increase in projected benefit obligation due to passage of time.
- Expected return on plan assets. The expected return on plan assets is calculated by applying the expected rate of return on plan assets to the beginning of year amount of plan assets.
- Gain or loss amortization. Gains and losses are changes in the amount of projected benefit obligations or plan assets due to actual experience that is different than assumed experience, as well as changes in assumptions, such as the discount rate applied to future cash flows expected to satisfy the pension obligation. Amortization expense is included in net periodic pension cost when beginning of year unrecognized gain or loss exceeds a "corridor" of ten percent of the greater of the projected benefit obligation or the market-related value of plan assets. Amounts in excess of the corridor are amortized over the average remaining future service of active plan participants, or average remaining life expectancy for plans, where almost all (more than 90%) of the plan participants are inactive.
- Prior service cost or credit. Prior service cost or credit represents the cost of retroactive benefits granted in a plan amendment that increase or decrease the projected benefit obligation. Amounts are amortized over the average remaining future service of active plan participants, or average remaining life expectancy for plans, where almost all (more than 90%) of the plan participants are inactive.

7. Duke Energy Ohio maintains a regulatory asset or regulatory liability on its books that includes pension actuarial losses or gains. These losses or gains are created when the pension plans' actual experience differs from assumed experience or due to changes in assumptions. Current accounting rules specify that those regulatory assets or regulatory liabilities are to be amortized over the average remaining service life if the pension plan is active, or the life expectancy of the plan participants if the pension plan is inactive. This amortization expense is one component of pension expense and is recorded in FERC Account 926, Employee Pensions and Benefits. The amortization expense is included in cost of service.

8. If Pension Settlement Accounting is triggered for regulated entities, the losses on the settled portion of the net periodic pension obligation must be reflected as an expense immediately, unless it is probable the costs (the amortization of which are currently a portion of pension cost being recovered through rates) will be recovered through rates. Examples of settlement transactions include making lump-sum cash payments to plan participants in exchange for their rights to receive their pension benefit, assumption of the benefit obligation by a buyer as part of a business combination, and the purchase of a nonparticipating annuity contract to cover participants' vested benefits.

9. In 2018, Duke Energy Corporation and its subsidiaries, including Duke Energy Ohio, undertook efforts to reduce and reallocate workforce by a significant number of employees for both service company and gas and electric operations.[4] Many of those employees have chosen to take lump sum payments from the pension plan in 2019. As a result, it was determined probable, in the second quarter of 2019, that the lump sum payments would exceed the threshold amount for Duke Energy Corporation under the plan. Therefore, in the second quarter of 2019, Duke Energy

[4] Approximately 1,900 in total workforce reduction was achieved across Duke Energy Corporation.

Ohio triggered Pension Settlement Accounting for the first time and booked settlement accounting entries for the second quarter. Additional settlement accounting entries will be booked for the remainder of 2019. Settlement charges for 2019 are estimated to be approximately:

	Settlement Charges 2019[a]
Duke Energy Ohio electric	$1,252,506
Duke Energy Ohio gas	$ 538,950

[a] Estimated charges based on forecast.

10. Duke Energy Ohio also anticipates recognizing future settlement charges in subsequent years because the Company has closed its pension plans to new employees, which means the threshold amounts for triggering settlement accounting will continue to decrease, thereby increasing the frequency of triggering settlement accounting in the future. Charges in future settlement events could well exceed these levels.

11. Duke Energy Ohio requests approval to continue to record settlement amounts that are incremental to base rates, in regulatory asset and regulatory liability accounts and to continue amortizing those amounts in the same way they would be amortized absent this Pension Settlement Accounting trigger. Absent this approval, the Company will be required to recognize expense or income impacts to its financial statements that are uneven, volatile, and are not aligned with current rates. Additionally, absent this approval, the Company would be treating Pension Settlement Accounting differently than all other aspects of its pension plan accounting.

12. The Company proposes that the settled portion of the losses or gains be moved to a separate regulatory asset or liability account and continue to be amortized over the average remaining service period of the pension plan participants. The Company's request will simply enable it to record all Pension Settlement Accounting impacts in regulatory asset or regulatory liability accounts and to amortize those assets or liabilities in the same manner they would have

been amortized had the Pension Settlement Accounting not been triggered. The Commission would adjust those amortization amounts or periods in future rate cases if needed. The Company is requesting Commission approval of this treatment for both the Pension Settlement Accounting triggered in 2019 and any future Pension Settlement Accounting that may be triggered.

13. The Company already has deferral authority for all other aspects of its pension plan accounting. Approval of this application will result in keeping the treatment of Pension Settlement Accounting consistent with all other aspects of the Company's pension plan accounting.

14. Commission approval of the requested accounting treatment is necessary for the Company to assert probability of recovery of such expenditure under generally accepted accounting procedures.

15. In some recent deferral authority proceedings, Staff of the Commission (Staff) has delineated six criteria that it believes the Commission has historically considered in determining whether to grant such deferral authority. Those criteria are described by Staff as:

- Whether the current level of costs included in the last rate case is insufficient;
- Whether the costs requested to be deferred are material in nature;
- Whether the problem was outside of the Company's control;
- Whether the expenditures are atypical and infrequent;
- Whether the costs would result in financial harm to the Company; and
- Whether the Commission could encourage the utility to do something it would not otherwise do through the granting of deferral authority.[5]

[5] *See, e.g., In the Matter of the Application of Duke Energy Ohio, Inc. for Approval of a Grid Modernization Opt-Out Tariff and for a Change in Accounting Procedures Including a Cost Recovery Mechanism*, Case No. 14-1160-EL-UNC, *et al.*, Pre-filed Testimony of David M. Lipthratt, pp. 5-6 (October 2, 2015).

It is critical to note, however, that the Commission does not require an applicant to meet every one of the factors identified by Staff. For example, in the same case cited above, the Commission granted the deferral request based on its determination that the expenditure being considered was atypical or infrequent and that the Commission could thereby encourage the applicant to take an action that the Commission deemed desirable.[6]

16. In response to the aforementioned criteria, Duke Energy Ohio states that its deferral request is to keep the Company in the same position it would otherwise be in absent the imposition of Pension Settlement Accounting. While the Company has a level of pension costs embedded in its base rates, the applicability of Pension Settlement Accounting would otherwise require the Company to recognize expense or income impacts to its financial statements that are uneven and are not aligned with current rates. Duke Energy Ohio's last natural gas rate case was approved November 13, 2013,[7] and based upon a test year that ended December 31, 2012. Likewise, the Company's electric rates were recently established but were based upon a test year that ended March 31, 2017.[8]

17. Pension Settlement Accounting is triggered in accordance with GAAP. The settlement charge resulting from the triggering of Pension Settlement Accounting was attributable to the Company's cost savings initiatives in reducing employee headcount, namely lump sum payments from the existing pension plans, which, over time, will offset the costs incurred. Pension Settlement Accounting does not change the cost of the pension plan over the life of the plan, but accelerates the recognition of the gains/losses. The cost savings are derived from reducing

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[6] *Id.*, Opinion and Order, pg. 7 (April 27, 2016).

[7] *In the Matter of the Application of Duke Energy Ohio, Inc., for an Increase in its Natural Gas Distribution Rates*, Case No. 12-1685-GA-AIR, *et al.*, Opinion and Order (November 13, 2013).

[8] *In the Matter of the Application of Duke Energy Ohio, Inc., for an Increase in Electric Distribution Rates,* Case No. 17-0032-EL-AIR, *et al.*, Opinion and Order, (December 19, 2018).

headcount, but the pension costs remains unchanged. Had Pension Settlement Accounting not been triggered, the gains/losses would have been recorded to a FERC account 182.3 regulatory asset and amortized over the estimated remaining service life of the employees in the pension plan.

18. The applicability of the Pension Settlement Accounting is pursuant to recognized accounting principles, which are outside the Company's control and are otherwise atypical and infrequent. The current situation represents the first time the Company's offering of voluntary severance packages has triggered the Pension Settlement Accounting rules. Denying the Company's application would discourage the Company from taking similar action in the future to reduce its labor costs because of the risk of triggering future Pension Settlement Accounting. Rather, the Commission should encourage utilities to look for opportunities to reduce their overhead and labor costs by offering similar severance packages to its employees.

19. If approved, Duke Energy Ohio will hold its deferred costs in Account No. 182.3, Other Regulatory Assets, until such time as the Commission considers the method of recovery in a future rate proceeding.

20. If the Commission approves Duke Energy Ohio's requested regulatory asset treatment, Duke Energy Ohio expects to make the journal entries shown below, based on estimates available as of September 10, 2019. Note that amounts were originally recorded in a 182.3 account but when Pension Settlement Accounting was triggered, it caused the Company to record the resulting settlement charge to a 926 account. Because the Company believes the deferral authority is probable, the Company has recorded the settlement charge temporarily to a 186 account. Once the Commission grants the deferral authority requested in this application, the Company will record the following entries. Amounts may change as new information regarding Pension Settlement Accounting costs estimates becomes available:

Duke Energy Ohio - Electric

Dr. 182.3	Other regulatory assets (Settlements)	$1,252,506
Cr. 186	Misc. deferred debits	$1,252,506

Duke Energy Ohio – Gas

Dr. 182.3	Other regulatory assets (Settlements)	$538,950
Cr. 186	Misc. deferred debits	$538,950

Accordingly, Duke Energy Ohio requests authority to defer the Pension Settlement Accounting impacts and to make any accounting deferrals necessary to establish the associated regulatory assets or liabilities. Commission approval of the requested accounting treatment is necessary for the Company to assert probability of recovery of such expenditure under generally accepted accounting procedures.

21. This application only requests authority for the accounting treatment described above. Recovery of any costs deferred under this application will be addressed in a separate proceeding.

22. The requested change in accounting procedure will not result in any increase in any rate or charge. The Commission may approve this application without a hearing.

WHEREFORE, Duke Energy Ohio respectfully requests that the Commission approve this application as submitted.

Respectfully submitted,

DUKE ENERGY OHIO, INC.

/s/ *Rocco O. D'Ascenzo*

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