

**TESTIMONY OF ELLIOTT BATSON, JR.
VICE PRESIDENT, REGULATED FUELS
DUKE ENERGY BUSINESS SERVICES LLC
ON BEHALF OF DUKE ENERGY INDIANA, INC.
CAUSE NO. 38707-FAC92 BEFORE THE
INDIANA UTILITY REGULATORY COMMISSION**

1 **Q. STATE YOUR NAME AND BUSINESS ADDRESS.**

2 A. My name is Elliott Batson, Jr., and my business address is 526 South Church
3 Street, Charlotte, North Carolina 28202.

4 **Q. BY WHOM ARE YOU EMPLOYED AND IN WHAT CAPACITY?**

5 A. I am employed as Vice President, Regulated Fuels by Duke Energy Business
6 Services LLC, a service company subsidiary of Duke Energy Corporation
7 (collectively with its subsidiaries, "Duke Energy") and a non-utility affiliate of
8 Duke Energy Indiana, Inc. ("Duke Energy Indiana" or "Company").

9 **Q. PLEASE BRIEFLY DESCRIBE YOUR EDUCATIONAL BACKGROUND
10 AND BUSINESS EXPERIENCE.**

11 A. I am a 1985 graduate of the University of South Carolina with a Bachelor of
12 Science in Business Administration. I have been employed with Duke Energy
13 since 1986 and have worked in various fossil fuel procurement functions and
14 leadership roles since 1990. I am a member of the North Carolina Coal Institute.

15 **Q. PLEASE BRIEFLY DESCRIBE YOUR DUTIES AND
16 RESPONSIBILITIES AS VICE PRESIDENT, REGULATED FUELS.**

17 A. As Vice President, Regulated Fuels, I participate in all aspects of the purchase and
18 delivery of fuel that the Duke Energy regulated utilities use for the generation of
19 electricity. As part of this activity, I monitor and participate in the development

1 of various fuels of current and potential interest, including forecasts of supply and
2 demand, price, quality, availability, economics and deliverability. These fuel
3 forecasts cover both existing supply sources and potential future supply sources. I
4 also supervise the Company's fuel procurement activity, including the negotiation
5 and administration of long-term and spot purchase contracts.

6 **Q. PLEASE EXPLAIN HOW COAL CONTRACTS ARE ENTERED INTO**
7 **BY THE COMPANY.**

8 A. Coal is generally purchased under long-term contracts of one year or longer to
9 assure a reliable supply of large quantities of coal that meet consistent quality
10 characteristics needed for a particular generating station and at a competitive
11 price. Coal supply proposals are secured from producers and evaluated
12 thoroughly, taking into account coal quality, quantity, transportation alternatives
13 and price, among other factors. The producer (or producers) whose coal offers
14 the best value, particularly with regard to overall utilization costs, is selected for
15 further negotiations to produce a long-term contract or contracts. It is important
16 to note that many of our long-term contracts either contain provisions for periodic
17 price reopener negotiations, some type of price escalations, or a mechanism to
18 adjust prices based upon a published market price index. In addition, all of our
19 coal transportation contracts in Indiana contain fuel price surcharge provisions
20 that are based upon published fuel price indices.

21 **Q. HOW MANY OF THE COMPANY'S GENERATING STATIONS**
22 **RECEIVE COAL UNDER LONG-TERM CONTRACTS?**

1 A. Gibson, Wabash River, Cayuga and, most-recently, Edwardsport IGCC Stations
2 are supplied by long-term agreements for more than 90% of their annual
3 requirements. Gallagher Station will be supplied by spot purchases, if any,
4 throughout the remainder of 2012 because the Company currently forecasts that,
5 due to higher per-unit fuel costs, low 2012 forward power prices and the
6 retirement of two units at the end of January 2012, the Gallagher generating units
7 will operate infrequently for the remainder of 2012.

8 **Q. HOW DOES THE COST OF COAL PURCHASED PURSUANT TO**
9 **LONG-TERM CONTRACTS COMPARE WITH THE SPOT COST OF**
10 **COAL?**

11 A. For the twelve-month period ended February 29, 2012, the Company purchased a
12 total of approximately 12.4 million tons of coal (pursuant to both long and short-
13 term contract commitments) at an approximate average cost of \$2.55/mmBTU.
14 The delivered cost of coal purchased under long-term commitments averaged
15 \$2.54 /mmBTU and made up greater than 98% of total coal receipts. The
16 delivered cost of coal purchased under short-term commitments averaged
17 \$2.65/mmBTU. The vast majority of spot coal purchased during the twelve-
18 month period was for Gallagher Station. The delivered spot price for Gallagher
19 Station is higher than Duke Energy Indiana's long-term contract coal due to the
20 fact that Gallagher is subject to the New Source Review (NSR) compliance
21 requirements, and, as such, must burn coals with a much lower sulfur coal
22 content. This low sulfur coal is priced higher in the market when compared
23 against higher sulfur coals.

1 Q. DESCRIBE HOW YOU BUY SPOT COAL.

2 A. Duke Energy's Regulated Fuel Department stays continually informed as to the
3 current market for spot and contract coal and specific opportunities for the
4 purchase of such coal. Coal supply needs are determined by an ongoing review of
5 generating station stockpiles, consumption projections, and current coal supply
6 quantities already contracted. A current record of relevant information for each
7 producer, not only in the immediate area of supply but throughout much of the
8 Illinois Coal Basin and other coal supply areas, is maintained within the
9 Regulated Fuel Department. In addition, Duke Energy's Regulated Fuel
10 Department personnel visit each of the Company's contract producers and mining
11 operations regularly and any potential new spot producers as well, gathering
12 information that assists in our analysis of spot coal needs. This information,
13 coupled with constant monitoring of pricing information published in various
14 places (e.g. industry newsletters, trade publications, regulatory filings, etc.), as
15 well as a close review by the Regulated Fuel Department of the weekly spot
16 market pricing indices published by brokers and traders provides a thorough
17 understanding of the various spot coal (and long-term) alternatives. At the time
18 the Company identifies a need to purchase spot coal, Regulated Fuels will seek
19 proposals from potential suppliers, and the resulting commitment or commitments
20 are based on the suppliers providing the best economic value to Duke Energy
21 Indiana, which is a combination of the lowest delivered cost, coal qualities, and
22 best overall utilization characteristics of a given unit or units. Usually, spot coal

1 commitments are made for small quantities of coal to cover peak periods of burn
2 over short durations, as compared to long-term contracts of one year or more.

3 **Q. WHAT OTHER STEPS DO YOU TAKE TO KEEP COAL PRICES**
4 **DOWN?**

5 A. We use various methods and strategies to keep prices down, including the use of
6 staggered terms on long-term contracts, seeking to maintain a diversified mix of
7 suppliers and using indices, at times, in the determination of adjustment of prices.
8 The Company also works with fuel and transportation suppliers to increase their
9 operating flexibility and in return receive a price or rate reduction. In addition,
10 we are vigilant about monitoring and enforcing the provisions of our coal
11 contracts with respect to quantities and qualities of coal due the Company.
12 Further, the coal quality provisions of the Company's coal supply agreements
13 typically include penalties for non-conforming coal deliveries.

14 **Q. PLEASE DESCRIBE THE LATEST TRENDS IN COAL MARKET**
15 **CONDITIONS.**

16 A. Published market prices for all coal basins have decreased significantly over the
17 last six months. High-sulfur Illinois basin coal prices are trending down from the
18 upper \$40's during late Summer of 2011 to the upper \$30's per ton for prompt
19 delivery and low \$40's for 2013 delivery. Central Appalachia coal prices have
20 decreased from approximately \$80 per ton during late Summer of 2011 to the mid
21 \$50's per ton for prompt delivery. The northern Appalachia and Powder River
22 coal basin market prices have decreased significantly as well. The biggest drivers
23 for these pricing changes are sharply falling natural gas prices and extremely mild

1 weather this past winter that have led to significant reductions in coal generation.
2 According to recent coal industry publications, the national coal burn for
3 December 2011 through February 2012 was more than 23% below average.
4 Overall utility inventories grew by as much as 22 Million tons in the United States
5 over these same three winter months (as compared to a typical average decrease
6 of 15 Million tons). According to the same industry publications, coal inventories
7 at U.S. power plants as of the end of February are more than 45 million tons
8 above normal.

9 Looking forward, we continue to see volatility in the coal markets, with
10 such driving forces being: (a) the decline of the Central Appalachian steam coal
11 supplies, (b) the growth of Illinois Basin coal production, (c) uncertainties around
12 the export market, (d) low natural gas prices, (e) declining power prices, and (f)
13 uncertainties associated with compliance requirements for the Cross-State Air
14 Pollution Rule and other environmental regulations. Several suppliers have
15 conveyed plans to reduce 2012 coal production in light of lower U.S. coal
16 demand, including recent announcements by Alpha Natural Resources, Patriot
17 Coal Company and Consol Energy; this will further impact coal market
18 conditions. History has shown that small imbalances in coal supply and demand
19 can cause large changes in coal market prices.

20 **Q. HOW DO YOU EXPECT THESE TRENDS TO AFFECT DUKE ENERGY**
21 **INDIANA'S COAL BURN?**

22 A. As noted in my supplemental testimony filed on February 22, 2012, due to
23 increasingly lower power prices and reduced demand for coal generation, Duke

1 Energy Indiana's coal burn projections for 2012 have been adjusted downward.
2 For example, coal burn for Duke Energy Indiana stations in December 2011
3 through February 2012 were approximately 45% less than the coal burn compared
4 to the same months over the prior 5 years. If natural gas and power prices
5 continue to be depressed, there likely will be further downward pressure on Duke
6 Energy Indiana's coal generation.

7 **Q. PURSUANT TO THE COMMISSION'S ORDER IN FAC 91, PLEASE**
8 **EXPLAIN THE COMPANY'S COAL INVENTORY POSITION.**

9 A. As noted in supplemental testimony filed on February 22, 2012, Duke Energy
10 Indiana's coal inventories as of February 15, 2012, had grown to approximately
11 3,800,000 tons (over 60 days of coal supply at a full load burn rate per day) across
12 the system, including more than 450,000 tons in storage at the existing Gibson
13 Station Remote pile. From December 1, 2011, through February 15, 2012, coal
14 inventories increased by approximately 800,000 tons, a period of time in which
15 historically inventories have decreased across the system. As of April 11, 2012
16 coal inventories were approximately 3,600,000 tons (the equivalent of 58 days of
17 coal supply). The reduction in coal inventory is due to increased coal burns since
18 the implementation of the coal price decrement (further described in Witness
19 Swez testimony) on February 24, 2012 as well as reduced coal shipments over
20 this time period. However, based on the Company's latest forecast for coal
21 generation, the Duke Energy Indiana expects coal inventories to increase through
22 the remainder of 2012 and into 2013. Further, as noted in my testimony filed on
23 January 22, 2012, the Company entered into an agreement with an Indiana

1 supplier for low sulfur coal to be delivered in 2012 for the purpose of compliance
2 with the Cross State Air Pollution Rule (“CSAPR”). Upon the stay of CSAPR,
3 the Company evaluated its options related to this relatively small volume of coal.
4 Currently, the Company has placed some of the low sulfur coal in storage at a
5 river terminal for possible resale, and the remaining tonnage has been shipped to
6 Gibson Station for consumption. We continue to evaluate the best options for
7 future deliveries, including ongoing negotiations with the coal supplier about
8 cancellation of future 2012 deliveries.

9 **Q. BESIDES IMPLEMENTING THE COAL PRICE DECREMENT, WHAT**
10 **STEPS IS THE COMPANY UNDERTAKING TO MITIGATE THE**
11 **INVENTORY PROBLEM?**

12 A. As noted in supplemental testimony filed on February 22 in the Company’s
13 FAC91 proceeding, the Company is undertaking and continues to evaluate a host
14 of options in order to effectively manage the growing inventories. The Company
15 has met with each of its long-term suppliers in Indiana to discuss deferral,
16 cancellation and other commercial and operational options to decrease the
17 shipments for 2012. In addition, we have commissioned and completed a survey
18 to determine the maximum storage capabilities at all of our stations. Duke Energy
19 Indiana shaped and compacted the existing Gibson Remote Pile adjacent to
20 Gibson station for receipt of additional coal for storage. Furthermore, we have
21 explored options to increase the storage capabilities at both on-site and off-site
22 facilities, including a possible second Gibson Remote pile. The Company has
23 also been actively exploring the option to resell surplus coal into the market.

1 Finally, the Company is considering its options to buy-out of the existing
2 contracts or to pursue other legal options. The Company will continue to closely
3 monitor its anticipated coal requirements and inventories and take every action
4 available to cost effectively control coal inventories in the least cost-impact
5 manner for customers.

6 **Q. ARE YOU AWARE OF ANY SIGNIFICANT OUT OF PERIOD**
7 **ADJUSTMENTS TO FUEL INVENTORY OR FUEL EXPENSE BEING**
8 **MADE IN THIS PROCEEDING?**

9 A. Other than the adjustment resulting from the aerial coal inventory survey
10 discussed in the testimony of Mr. Barry Blackwell, I am not aware of any.

11 **Q. BASED UPON YOUR EXPERIENCE, DO YOU HAVE AN OPINION AS**
12 **TO WHETHER THE COMPANY PURCHASED COAL AT THE**
13 **LOWEST PRICES REASONABLY POSSIBLE?**

14 A. I do.

15 **Q. WHAT IS THAT OPINION?**

16 A. In my opinion, the Company purchased coal at prices as low as reasonably
17 possible at the time the purchases were made.

18 **Q. REFERRING NOW TO THE COMPANY'S PURCHASE OF OIL, WILL**
19 **YOU DESCRIBE THOSE PURCHASES?**

20 A. Oil for peaking and cycling units is purchased from one supplier at the lowest
21 delivered price available under prearranged logistics. Our primary oil
22 requirements are for #2 ultra low sulfur fuel oil, which varies little in delivered
23 quality.

1 Q. **BASED UPON YOUR EXPERIENCE, DO YOU HAVE AN OPINION AS**
2 **TO WHETHER THE COMPANY PURCHASED OIL AT THE LOWEST**
3 **PRICES REASONABLY POSSIBLE?**

4 A. Yes. It is my opinion that the Company purchased oil at the lowest cost
5 reasonably possible.

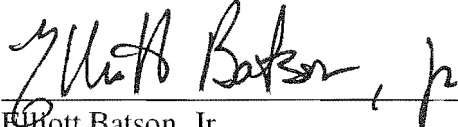
6 Q. **DOES THIS CONCLUDE YOUR PREPARED TESTIMONY?**

7 A. Yes, it does.

VERIFICATION

I, Elliott Batson, Jr., affirm under penalties for perjury that the foregoing representations are true to the best of my knowledge, information, and belief.

Dated this 30 day of April, 2012.



Elliott Batson, Jr.