

BEFORE

THE PUBLIC UTILITIES COMMISSION OF OHIO

In the Matter of the Application of The)
Cincinnati Gas & Electric Company Now) Case No. 01-1228-GA-AIR
Known as Duke Energy Ohio, Inc. for an)
Increase in Its Gas Rates in Its Service)
Territory.

In the Matter of the Application of The)
Cincinnati Gas & Electric Company Now) Case No. 01-1539-GA-AAM
Known as Duke Energy Ohio, Inc. for)
Approval to Change Accounting Methods.)

SIXTH OPINION AND ORDER

The Commission, considering the latest application, testimony filed, the applicable law, proposed stipulation, and other evidence of record, and being otherwise fully advised, hereby issues its Sixth Opinion and Order.

APPEARANCES:

John J. Finnigan, Jr., 139 East Fourth Street, Room 2500 Atrium II, Cincinnati, Ohio 45201-0960, on behalf of The Cincinnati Gas & Electric Company, now known as Duke Energy Ohio, Inc.

Janine L. Migden-Ostrander, Ohio Consumers' Counsel, by Larry Sauer, Assistant Consumers' Counsel, 10 West Broad Street, Suite 1800, Columbus, Ohio 43215-3485, on behalf of the residential consumers of Duke Energy Ohio, Inc.

McNees, Wallace & Nurick LLC, Gretchen G. Hummel, 21 East State Street, Suite 1700, Columbus, Ohio 43215-4228, on behalf of Industrial Energy Users-Ohio.

Marc Dann, Ohio Attorney General, by Duane W. Luckey, Section Chief, William Wright, Assistant Attorney General, 180 East Broad Street, Columbus, Ohio 43215-3793, on behalf of the Commission Staff.

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OPINION:

I. Procedural Background of the Accelerated Main Replacement Program

In the Opinion and Order adopted on May 30, 2002 (2002 Order) in these proceedings, the Commission approved a Stipulation and Recommendation filed on April 17, 2002, (2002 AMRP Stipulation) by the majority of the parties to Case Nos. 01-1228-GA-AIR and 01-1539-GA-AAM.¹ The 2002 Order approved the request by The Cincinnati Gas & Electric Company (Duke)² to recover the costs associated with a new, accelerated main replacement program (AMRP). The objective of the AMRP is to replace all cast iron and bare steel mains on Duke's system, covering approximately 1,200 miles, over a 10-year period. Duke contends that the replacement program will improve the safety and reliability of its gas system, given the leak rate for the cast iron mains and because the bare steel mains are near the end of their useful lives. Duke's special recovery mechanism for the AMRP allows each year's costs to be recovered through a special annual rider (AMRP Rider), while also passing on any savings realized from fewer leaks on the system. At the initiation of the AMRP, Duke estimated that the cost over the 10 years of the AMRP would be approximately \$716 million. The 2002 Order established caps on the amount that the AMRP Rider may increase each year. Further, pursuant to the 2002 Order, Duke may not seek any direct increase in the AMRP Rider after May 2007, but the AMRP Rider rates placed into effect in this Sixth Opinion & Order shall continue until the effective date of the rates set in the company's next base rate case. The 2002 Order also authorized Duke to create certain regulatory assets needed to implement the AMRP. Pursuant to the AMRP process approved in the 2002 Order, Duke has the opportunity to defend the continuation of the AMRP Rider by prefiling, each November, an application containing support for the rider, with the formal filing to be made by the end of February of the following year. Staff investigates the AMRP Rider application and makes its recommendation. The other parties to these proceedings may file objections to the AMRP Rider application. The goal is to have each year's AMRP Rider approved to be implemented for the first billing cycle of the May revenue month.

¹ The parties to Case Nos. 01-1228-GA-AIR and 01-1539-GA-AAM are: Utility Workers Union of America (UWUA); Independent Utilities Union, Local Union 600 of the UWUA (Local Union 600); Ohio Consumers' Counsel (OCC); Ohio Partners for Affordable Energy (OPAE); Industrial Energy Users-Ohio (IEU-Ohio); Communities United for Action (CUFA); The Ohio Home Builders Association (OHBA); Staff of the Commission (Staff); and People Working Cooperatively, Inc. (PWC). The OHBA, the UWUA and Local Union 600 did not enter into the 2002 AMRP Stipulation.

² Cinergy Corporation was the parent company of The Cincinnati Gas and Electric Company until Cinergy merged into Duke Energy Corporation, effective April 3, 2006. Following that transaction, The Cincinnati Gas and Electric Company was renamed Duke Energy Ohio, Inc. It will be referred to as Duke throughout the remainder of this opinion and order.

Since the initiation of the AMRP, the rates have been as follows:

Rate Class	May 2002 – April 2003 ³	May 2003 – April 2004 ⁴	May 2004 – April 2005 ⁵	May 2005 – April 2006 ⁶	May 2006 – April 2007 ⁷
Residential Service and Residential Firm Transportation ⁸	\$1.00/billing cycle	\$1.84/billing cycle	\$2.84/billing cycle	\$3.81/billing cycle	4.80/billing cycle
General Service and Firm Transportation	\$3.75/billing cycle	\$9.84/billing cycle	\$15.55/billing cycle	\$20.60/billing cycle	\$25.56/billing cycle
Interruptible transportation, subject to a per-month cap of \$500.	\$0.01/mcf	\$0.02/mcf	\$0.03/mcf	\$0.03/mcf	\$0.03/mcf

By Commission entry issued December 19, 2002, the date certain in this process was established as December 31 of each year. In that entry, the Commission also agreed that the test periods would be based on nine months of actual data and three months of projected data for the calendar year. On November 30, 2006, Duke filed its notice of intent to file an application for an increase in the AMRP Rider rates and supporting documentation.

By entry issued December 7, 2006, Duke was directed to file updated actual test year data by no later than February 28, 2007. By the same entry, the Staff was directed to file its recommendations, and any party wishing to file objections to the application to file their objections, by no later than March 16, 2007. The entry also scheduled these matters for a hearing to commence on April 4, 2007, if necessary.

³ Pursuant to the 2002 AMRP Stipulation and the 2002 Order.

⁴ Pursuant to the Stipulation filed April 14, 2003 (2003 AMRP Stipulation) and Second Opinion and Order issued on April 29, 2003.

⁵ Pursuant to the Stipulation filed April 7, 2004 (2004 AMRP Stipulation) and Third Opinion and Order issued on April 21, 2004.

⁶ Pursuant to the Stipulation filed April 5, 2005 (2005 AMRP Stipulation) and Fourth Opinion and Order issued on April 20, 2005.

⁷ Pursuant to the Stipulation filed April 4, 2006 (2006 AMRP Stipulation) and Fifth Opinion and Order issued on April 19, 2006.

⁸ The residential AMRP rates effective for the period May 2002 – April 2003 were applicable to residential service customers only.

On February 16, 2007, Duke filed its application for an increase in the AMRP rates, along with the direct testimony of Duke's witnesses, Gary J. Hebbeler and William Don Wathen, Jr. On February 27, 2007, Duke filed Schedules 1 through 18 reflecting actual data for the 12 months ended December 31, 2006 for the new proposed AMRP Rider, among other information.

The Commission Staff filed its report of investigation on March 16, 2007. As a part of the Staff investigation, the Staff reviewed and analyzed all the documents filed by Duke and traced them to supporting work papers and source information, issued data requests, conducted investigative interviews of Duke personnel and performed independent analyses to determine if Duke's filed exhibits and application justify the requested adjustment to the revenue requirement for the AMRP. Staff's investigation of Duke's operating income was limited to a review of expenses related to depreciation, amortization of post in-service carrying charges, meter relocations, customer-owned service lines, property taxes and maintenance savings. With regard to rate base, Staff examined Duke's plant accounting system to ascertain its reliability. Staff also examined the computation for the allowance of funds used during construction (AFUDC) and verified the existence and the used and useful nature of rate base assets. Additionally, Staff reviewed certain carrying costs, tax issues, and the contractor bidding process (Staff Report at 3). Staff determined that Duke replaced 67.3 miles of mains in 2006, which brings the total mains replaced since the AMRP was initiated to 529.3 miles (Staff Report at 4).

In the AMRP Stipulation filed April 14, 2003 (2003 AMRP Stipulation), which was adopted by the Commission on April 29, 2003, Duke has previously agreed, among other things, to competitively bid at least 80 percent of the work for the AMRP. Staff notes that Duke competitively bid more than 97 percent of the AMRP work, based on construction costs incurred through December 31, 2006.

In the 2003 AMRP Stipulation, Duke also agreed only to award AMRP work to an affiliate if it was economic to do so. Further, Duke agreed that, if AMRP work was awarded to an affiliate, the company would report the name of the affiliate contractor, the amount paid to the affiliate contractor and the reason the work was awarded to the affiliate. Miller Pipeline Corporation (Miller) was an affiliate of Duke and Miller was paid \$10,650 to perform AMRP work. The AMRP work was awarded to Miller through a competitive bid process in which Miller was the lowest bid. Effective July 1, 2006, Duke sold its interest in Miller to Vectren Corporation. Duke also reported that Reliant Services, LLC (Reliant), an affiliate, performed location services for the AMRP. Duke paid Reliant \$19,273 during 2006. Effective October 30, 2006, a non-affiliated company, Central Locating Services, began to provide Duke AMRP line locating services.

Staff also reviewed Duke's management and monitoring of the cost of AMRP construction projects. Pursuant to the 2003 AMRP Stipulation, Duke agreed that actual construction costs may exceed the price per unit reflected in the contract only as a result of certain listed exceptions: (1) unanticipated field conditions; (2) additional right-of-way work imposed by a governmental entity; (3) an increase in the number of units required for the actual work, as compared with the number of units contemplated in the plan drawing; or (4) certain types of construction activities where Duke determines that the contractor could perform the work for a lower cost under other pricing methods. Staff notes that there were cost overruns in the AMRP during 2006 but that such overruns, based on Staff's investigation, were within the guidelines set forth above. Staff concluded, based on its review of Duke's 2006 AMRP job determination, bidding and contracting procedures, job monitoring, and contracting controls, that the management operation, bidder selection and contractor oversight of the AMRP are reasonable.

According to Staff, Duke's calculation of the 2007 AMRP revenue requirement properly includes, among other things, AMRP property used and useful on December 31, 2006, associated carrying charges, taxes, expenses and the authorized rate of return for the AMRP. Based on its determination of the 2007 AMRP revenue requirement of \$42,757,340, Duke calculates the following rates for the 2007 AMRP Rider, by revenue class: (1) \$5.86 per billing cycle, for residential and residential firm transportation services; (2) \$32.88 per billing cycle, for general service and firm transportation; and (3) \$.18 per Mcf, for interruptible transportation, subject to a maximum of \$500.00 per billing cycle.

Staff concluded that, based on the updated, actual data submitted for the year ended December 2006, the calculation of the AMRP revenue requirement is supported by adequate data and information, is just and reasonable, and is properly allocated to the various customer classes. Staff also concluded that the rate design is performed in accordance with the terms and conditions of the 2002 AMRP Stipulation. Further, Staff notes that the 2002 AMRP Stipulation provided that the fixed monthly AMRP charge for the residential class shall not increase by more than a \$1.00 increment during each of the years 2004 through 2007 of the AMRP.⁹ Staff emphasizes that the 2007 AMRP Rider rates, as calculated by Duke, all exceed the caps set forth in the 2002 Order establishing this AMRP process. Pursuant to the rate caps adopted in the 2002 Order and the 2006 AMRP Rider rates, Staff recommends that the 2007 AMRP Rider rates be set at the cap levels: \$5.80 per billing cycle for residential and residential firm transportation services; \$30.44 per billing cycle for general service and firm transportation; and \$.03 per Mcf for interruptible transportation service, subject to a per billing cycle cap of \$500.00.¹⁰ Staff also recommends that the 2007 AMRP Rider rates commence with the May 2007 billing

⁹ 2002 AMRP Stipulation, page 6; Stipulation Ex. 4.

¹⁰ 2002 AMRP Stipulation at Exhibit 4.

cycle or the first billing cycle of the month following the Commission's decision in these matters.

Staff also investigated whether Duke had overrecovered AMRP Rider residential revenues during 2006. The AMRP revenue requirement attributable to residential service and residential firm transportation for the period of May 2006 through April 2007 was calculated to be \$22,281,965. The actual AMRP Rider residential revenues collected for the nine months ended January 2007 and the estimated residential revenues for the three months ended April 2007 totaled \$22,565,893. Therefore, Staff determined that Duke overcollected the authorized 2006 AMRP residential revenue requirement by \$283,928. However, Staff pointed out that Duke's residential revenue requirement resulted in an actual rate that was higher than the stipulated 2007 AMRP Rider residential rate cap. According to Staff's calculations, adjusting that actual rate (\$5.86) to refund the 2006 overcollection would result in a residential rate for the 2007 AMRP Rider of \$5.80. Because this result is equal to the 2007 cap, Staff found that \$5.80 is a just and reasonable rate for the residential 2007 AMRP Rider.

On March 17, 2006, the Office of the Ohio Consumers' Counsel (OCC) filed objections to Duke's latest AMRP application, which may be summarized as follows:

- (1) OCC objects to Duke's cost management for work performed by certain contractors on AMRP projects. OCC asserts that the total cost overruns for the AMRP for the year ended December 2006 is \$3.1 million, or 16 percent, from work performed on 22 AMRP jobs by certain contractors. OCC notes that Duke has a process in place to identify projects with overruns of seven percent or more, to investigate those overruns, and to explain the reason for the variance. OCC questions whether Duke's process is effective, given the dollar amount of the overruns during this AMRP year and the fact that overruns do not cause any financial consequences for the contractor. OCC requests that the Commission deny Duke's request for recovery, through the AMRP Rider, of cost overruns that exceed seven percent of the work order estimate. OCC asserts that such costs are unjust and unreasonable.
- (2) OCC objects to the inclusion, in the AMRP Rider, of costs associated with the removal and replacement of plastic service lines and mains. OCC contends that the stated purpose of the AMRP is the removal and replacement of cast iron and bare steel service lines and mains only. Therefore, OCC reasons that Duke should be required to recover the cost of removal and

replacement of plastic lines and mains through a traditional base rate application rather than the AMRP cost recovery mechanism.

- (3) OCC states that, as originally proposed, the AMRP is a ten-year program. Further, OCC notes that the direct testimony of Duke witness Hebbeler states that "[Duke] projects the AMRP to be completed by 2015." OCC argues that the Commission should require Duke to terminate the AMRP no later than May 1, 2011, as proposed by Duke and approved by the Commission in the May 30, 2002 Order. Accordingly, OCC objects to any attempt by Duke to extend the AMRP.

OCC also requests that the Commission establish informational filing requirements for Duke and a procedure that would allow for discovery and an opportunity for the intervenors to determine whether or not the AMRP Rider rates continue to be just and reasonable. OCC further states that Duke's informational filing should include data on the progress of the AMRP, including, but not limited to, the number of services replaced, the estimated services yet to be replaced, total miles of pipe replaced (by composition), and the total miles of pipe yet to be replaced (by composition).

On March 27, 2007, Duke, OCC, IEU-Ohio and the Staff filed a Stipulation and Recommendation (2007 AMRP Stipulation) resolving all the current, outstanding issues in these proceedings.¹¹

II. 2007 AMRP Stipulation

In the 2007 AMRP Stipulation, the signatory parties agree, among other things, as follows:

- (1) Duke should receive an annualized revenue requirement under Rider AMRP of \$42,496,234, as calculated in the 2007 AMRP Stipulation Exhibit 1. The revenue distribution, billing determinants, and calculated AMRP charges be as shown on 2007 AMRP Stipulation Exhibit 1, except that the rate for Interruptible Transportation customers (Rate IT) shall be \$0.03 per Mcf, subject to a per month cap of \$500.00; the rate for General Service (Rate GS), Distributed Generation (Rate DGS),

¹¹ Attached as exhibits to the 2007 AMRP Stipulation are Stipulation Exhibit 1 – Ohio AMRP Cap Calculation-Projection by Rate Class (Schedule 16); and Stipulation Exhibit 2 – proposed revised Duke P.U.C.O. Gas No. 18, Tariff Sheet No. 65.5, page 1 of 1.

and Firm Transportation (Rate FT) shall be \$30.44 per month; and the rate for Residential Service (Rate RS) and Residential-Firm Transportation (Rate RFT) customers shall be \$5.77 per month.

- (2) Duke shall implement the new rates for Rider AMRP pursuant to the terms and conditions set forth in the 2002 AMRP Stipulation.
- (3) Neither the revenue distribution, the allocation of the revenue requirement that forms the basis for the new Rider AMRP rates, nor the accounting provisions contained in paragraph 6 of the 2002 AMRP Stipulation shall have any precedential value in Duke's next base rate case.
- (4) Duke will, for purposes of the ongoing Rider AMRP proceedings, continue to follow the practices and procedures previously agreed to in these cases, including:
 - (a) the terms and conditions establishing the AMRP, as specifically set forth on pages 4-16 of the 2002 AMRP Stipulation;
 - (b) the agreement to identify AMRP contractors, to competitively bid AMRP construction work and to monitor AMRP contractors, among other things, as specifically agreed to on pages 4-7 of the 2003 AMRP Stipulation; and
 - (c) the agreement to identify affiliated entities and the cost paid to such entities to perform AMRP construction or services, to report the number of customer service lines replaced as a part of the AMRP that exceed 70 feet and to report the cost of removal, retirement and addition of coated steel, copper and plastic pipe as a part of the AMRP, as specifically detailed on pages 4-8 of the 2004 AMRP Stipulation.
- (5) The tariff language attached as Stipulation Exhibit 2 should be approved by the Commission.

- (6) Duke shall make annual informational filings to demonstrate that the capped AMRP Rider rates continue to be just and reasonable. The parties reserve the right to perform discovery, to file objections, to hold an evidentiary hearing to resolve any disputed issue, and to challenge the term of the AMRP.

III. AMRP Discussion and Conclusion

Rule 4901-1-30, Ohio Administrative Code, authorizes parties to Commission proceedings to enter into stipulations. Although not binding on the Commission, the terms of the agreement are accorded substantial weight. See, *Consumers' Counsel v. Pub. Util. Comm.* (1992), 64 Ohio St.3d 123, at 125, citing *Akron v. Pub. Util. Comm.* (1978), 55 Ohio St.2d 155. This concept is particularly valid where the stipulation is supported or unopposed by the vast majority of parties in the proceeding in which it is offered and resolves all of the issues in a proceeding.

The standard of review for considering the reasonableness of a stipulation has been discussed in many prior Commission proceedings. See, e.g., *Ohio-American Water Co.*, Case No. 99-1038-WW-AIR (June 29, 2000); *The Cincinnati Gas & Electric Company*, Case No. 91-410-EL-AIR (April 14, 1994); *Western Reserve Telephone Company*, Case No. 93-230-TP-ALT (March 30, 1994); and *Ohio Edison Company*, Case Nos. 91-698-EL-FOR et al. (December 30, 1993). The issue for the Commission's consideration is whether the stipulation, which embodies considerable time and effort by the signatory parties, is reasonable and should be adopted. In considering the reasonableness of a stipulation, the Commission utilizes the following criteria:

- (1) Is the settlement a product of serious bargaining among capable, knowledgeable parties?
- (2) Does the settlement, as a package, benefit ratepayers and the public interest?
- (3) Does the settlement package violate any important regulatory principle or practice?

The Ohio Supreme Court has endorsed the Commission's analysis using these criteria to resolve issues in a manner economical to ratepayers and public utilities. *Indus. Energy Consumers of Ohio Power Co. v. Pub. Util. Comm.* (1994), 68 Ohio St.3d 559 (citing *Consumers' Counsel*, *supra* at 126).

Based on our three-prong standard of review, the Commission finds that the first criterion, that the process involved serious bargaining by knowledgeable, capable parties,

has been met. Counsel for Duke, IEU-Ohio, OCC and Staff have been involved in many cases before the Commission, including cases involving rate issues. Further, we note that all active parties in this proceeding have signed the 2007 AMRP Stipulation. Further, we find that the Stipulation meets the second criterion. The 2007 AMRP Stipulation advances the public interest by resolving all issues raised in the pending proceedings without extensive litigation. Finally, the Commission believes that the 2007 AMRP Stipulation meets the third criterion. The 2007 AMRP Stipulation does not violate any important regulatory principle or practice. Indeed, the 2007 AMRP Stipulation allows Duke to continue to improve the company's gas system safety and reliability in an expeditious manner. Thus, the Commission concludes that the 2007 AMRP Stipulation is in the public interest and represents a reasonable resolution of the pending AMRP application. Therefore, we adopt the 2007 AMRP Stipulation filed on March 27, 2007 in its entirety.

Thus, we approve Duke's request to revise its AMRP Rider to reflect an annualized revenue requirement of \$42,496,234 and to implement rates of \$5.77 per billing cycle for residential and residential firm transportation services; \$30.44 per billing cycle for general, distributed generation and firm transportation services; and \$.03 per Mcf for interruptible transportation service, subject to a \$500 maximum per billing cycle.

FINDINGS OF FACT AND CONCLUSIONS OF LAW:

- (1) On November 30, 2006, Duke filed notice of its intent to file an application to increase the AMRP Rider rates. The Commission entry issued December 19, 2002, established the date certain as December 31 of each year and provided that the test periods would be based on nine months of actual data and three months of projected data for the calendar year.
- (2) The Commission Staff conducted an investigation of the AMRP application and filed its report of investigation on March 16, 2007.
- (3) On March 16, 2007, OCC filed objections to Duke's latest AMRP application.
- (4) On March 27, 2007, Duke, OCC, IEU-Ohio and Staff filed the 2007 AMRP Stipulation resolving all the latest issues raised in these proceedings.
- (5) The 2007 AMRP Stipulation is the product of serious bargaining among knowledgeable parties, which benefits

ratepayers, advances the public interest, and does not violate any important regulatory principles or practices.

- (6) Duke's AMRP Rider rates shall be revised to reflect an annualized revenue requirement of \$42,496,234 and to implement rates of \$5.77 per billing cycle for residential and residential firm transportation services; \$30.44 per billing cycle for general, distributed generation and firm transportation services; and \$.03 per Mcf for interruptible transportation service, subject to a \$500 maximum per billing cycle, as agreed to in the 2007 AMRP Stipulation.

ORDER:

It is, therefore,

ORDERED, That the 2007 AMRP Stipulation, is approved in its entirety. It is, further,

ORDERED, That Duke's proposed tariff page reflecting the 2007 AMRP Rider rates, as set forth in the 2007 AMRP Stipulation at Exhibit 2, is approved. It is, further,

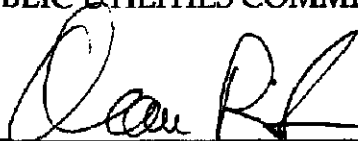
ORDERED, That Duke is authorized to file in final form four complete copies of tariffs consistent with this Sixth Opinion and Order. One copy shall be filed with these case dockets, one copy shall be filed with Duke's TRF docket, and the remaining two copies shall be designated for distribution to the Commission's Utilities Department. Duke shall update its tariffs previously filed electronically with the Commission's Docketing Division. It is, further,

ORDERED, That the effective date of the new tariffs shall be a date not earlier than both the date of this Sixth Opinion and Order and the date upon which the final tariffs are filed with the Commission. The new tariffs shall be effective for bills rendered on or after the first billing cycle of May 2007. It is, further,

ORDERED, That pursuant to Rule 4901:1-1-03(B)(1), Ohio Administrative Code, Duke notify all affected customers of the new AMRP Rider rates. A copy of the customer notice shall be submitted to the Commission's Service Monitoring and Enforcement Department, Reliability and Service Analysis Division, at least ten days prior to its distribution to customers. It is, further,

ORDERED, That a copy of this Order be served upon all parties of record.

THE PUBLIC UTILITIES COMMISSION OF OHIO



Alan R. Schriber, Chairman



Paul A. Centolella



Ronda Hartman Fergus



Valerie A. Lemmie

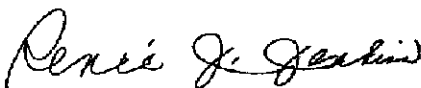


Donald L. Mason

GNS/vrm

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Renee J. Jenkins
Secretary