

BEFORE

THE PUBLIC UTILITIES COMMISSION OF OHIO

In The Matter of the Application of)	
Duke Energy Ohio, Inc. for an)	Case No. 07-589-GA-AIR
Increase in Gas Rates)	
In the Matter of the Application of)	
Duke Energy Ohio, Inc. for Approval)	Case No. 07-590-GA-ALT
of an Alternative Rate Plan for its)	
Gas Distribution Service)	
In the Matter of the Application of)	
Duke Energy Ohio, Inc. for Approval)	Case No. 07-591-GA-AAM
to Change Accounting Methods)	

SECOND SUPPLEMENTAL TESTIMONY OF

WILLIAM DON WATHEN JR.

ON BEHALF OF

DUKE ENERGY OHIO, INC.

_____	Management policies, practices, and organization
<u> x </u>	Operating income
<u> x </u>	Rate Base
_____	Allocations
_____	Rate of return
_____	Rates and tariffs
_____	Other

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INDEX

Second supplemental testimony relating to certain objections and recommendations made by the Office of Consumers' Counsel in its testimony and Objections to Staff Report.

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ATTACHMENTS

Second Supplemental Attachment WDW-1 - Revised Schedule A-1

Second Supplemental Attachment WDW-1 - Summary of Service Company Allocations

I. INTRODUCTION AND PURPOSE

1 **Q. PLEASE STATE YOUR NAME.**

2 A. My name is William Don Wathen Jr.

3 **Q. DID YOU FILE DIRECT AND SUPPLEMENTAL TESTIMONY IN THIS**
4 **PROCEEDING ON BEHALF OF DUKE ENERGY OHIO INC. (“DE-**
5 **OHIO”)?**

6 **Q. DID YOU FILE DIRECT AND SUPPLEMENTAL TESTIMONY IN THIS**
7 **PROCEEDING ON BEHALF OF DUKE ENERGY OHIO INC. (“DE-**
8 **OHIO”)?**

9 A. Yes.

10 **Q. WHAT IS THE PURPOSE OF YOUR SECOND SUPPLEMENTAL**
11 **TESTIMONY?**

12 A. I will provide a response to a number of issues raised in the direct testimony of
13 certain witnesses filing direct testimony on behalf of the Office of Consumers’
14 Counsel (“OCC”). Specifically, I will address the following issues:

15 Responding to Ms. Kathy L. Hagans

- 16 - Customer deposits
17 - Amortization of rate case and other expenses
18 - Service company allocations

19 Responding to Mr. Steven B. Hines

- 20 - Depreciation expense

21 I am also sponsoring additional attachments. The first, Second
22 Supplemental Exhibit WDW-1, reflects a change in the revenue requirement

1 calculation discussed below to partially accept a recommendation made by the OCC
2 regarding service company allocations. The other attachment, Second
3 Supplemental Exhibit WDW-2, is a summary of the specific components of the
4 service company allocations that were adjusted.

II. WORKING CAPITAL

5 **Q. DESCRIBE THE ISSUE BEING ADDRESSED BY THE OCC WITH**
6 **RESPECT TO THE WORKING CAPITAL.**

7 A. In its “Report by the Staff of the Public Utilities Commission of Ohio” (“Staff
8 Report”), filed on December 20, 2007, the Staff proposed that all of the
9 Company’s working capital, including customer deposits be set to \$0. The OCC
10 contends that the Staff erred in that it should have addressed customer deposits
11 separate from other working capital. The OCC suggests that the Staff should not
12 only have set the working capital, shown on Schedule B-5.1, to \$0 but should also
13 have deducted from rate base the balance of customer deposits at the date certain,
14 March 31, 2007.

15 **Q. WHAT IS YOUR RESPONSE TO THE OCC’S OBJECTION?**

16 A. First, as indicated in my supplemental direct testimony filed on January 29, 2008,
17 the Company objects to the Staff Report insofar as it sets all of working capital to
18 \$0. However, we do agree with the OCC that customer deposits represent
19 customer provided capital which is available to the Company and, thus, should be
20 deducted from whatever amount of other working capital (even if it is \$0) the
21 Commission ultimately approves for the Company. As pointed out by OCC’s
22 witness Ms. Hagans, this adjustment is needed in order to maintain the symmetry

1 between the interest expense on customer deposits included for recovery in the
2 test year and the rate base upon which the Company earns a return.

3 We disagree with the OCC's proposal to use the date certain balance of
4 customer deposits for the adjustment. Such a proposal is not supported by any
5 Commission precedent and is based on an invalid assumption. In addition, the
6 OCC's argument for the "special" treatment of customer deposits supports the
7 Company's case that the Staff erred in eliminating all other working capital.

8 **Q. WHAT IS THE OCC'S RATIONALE FOR USING A DATE-CERTAIN**
9 **BALANCE FOR CUSTOMER DEPOSITS?**

10 A. Ms. Hagans references recent cases in her testimony in which the Staff has
11 recommended a \$0 working capital allowance as it has in this proceeding. In
12 those cases, the Staff moved the balance of customer deposits from Schedule B-
13 5.1, where each of the companies included it in their original filings, to Schedule
14 B-6 in the respective Staff Reports. It is worth noting that moving customer
15 deposits to Schedule B-6 is at odds with the Commission Rules which clearly
16 show that customer deposits belong on Schedule B-5.1. (*See* Ohio Administrative
17 Code, Chapter 4901:7 Appendix A, Section B, (E)(2)). Nevertheless, because the
18 item is now shown on Schedule B-6 in the Staff Report and, apparently because
19 the balance in the account has been increasing over the thirteen-month period, Ms.
20 Hagans asserts that it should be valued at the date certain balance as is the case for
21 all other items shown on Schedule B-6.

22 **Q. IS THERE ANY MERIT TO THE OCC'S ARGUMENT THAT THE**
23 **COMMISSION HAS ESTABLISHED SOME SORT OF PRECEDENT**

1 **REGARDING CUSTOMER DEPOSITS THAT MUST BE FOLLOWED**
2 **HERE?**

3 A. None that is evident. In her eagerness to point out examples of prior cases where
4 the Staff has moved customer deposits from Schedule B-5.1 to Schedule B-6, Ms.
5 Hagans must have missed the point that in each of those cases the valuation of
6 customer deposits maintained a thirteen-month average balance. I agree with her
7 that items found on Schedule B-6 are valued using date certain balances but, as I
8 pointed out earlier, per the Commission's rules under the O.A.C., customer
9 deposits do not belong on Schedule B-6.

10 Furthermore, Ms. Hagans fails to mention that the OCC has not objected
11 to the use of the thirteen-month average for customer deposits in any of the prior
12 cases she cites. Inexplicably, the OCC is choosing to create an issue here in rate
13 base valuation that has not existed before.

14 The OCC's recommendation to use the date certain balance is not founded
15 on any substantive basis and is certainly not supported by any Commission
16 precedent or OCC prior practice. Therefore, the OCC's recommendation to use a
17 thirteen-month average valuation for customer deposits should be rejected by the
18 Commission. Similarly, her recommendation to modify the Company's proposed
19 adjustment for interest expense on customer deposits should be rejected.

20 **Q. IS THERE ANYTHING NOTEWORTHY ABOUT THE**
21 **RECOMMENDATION TO TREAT CUSTOMER DEPOSITS**
22 **DIFFERENTLY FROM OTHER WORKING CAPITAL?**

1 A. It is ironic that so much attention is paid to the notion that “customer funded”
2 capital should be treated differently from other components of working capital.
3 The Company has, in the past, and continues to argue that the various elements of
4 “non-cash” working capital are different from cash working capital and that the
5 Company should earn a return on non-cash working capital. For example, insofar
6 as customer deposits are unique in that they are funded by customers, they are
7 deducted from rate base but the Company is allowed to include the interest it pays
8 on the deposits as a test year expense in the calculation of its revenue
9 requirement. Yet, at the same time, the Company purchases millions of dollars of
10 natural gas to be stored on behalf of its customers which the OCC apparently
11 believes should be financed solely by the Company’s shareholders and not
12 included in rate base. There is clearly an imbalance in the logic applied by the
13 Staff and the OCC towards the individual components of working capital. Given
14 the magnitude and nature of the investment in such assets as gas stored
15 underground, and given the need to maintain some degree of symmetry between
16 ratepayer and shareholder funded investments, the Company believes the
17 Commission must allow it to recover a return on such a large shareholder
18 investment.

19 **Q. DO YOU HAVE ANY OTHER COMMENTS ON THE WORKING**
20 **CAPITAL ISSUE?**

21 A. Yes. As I indicated earlier, the OCC’s witness apparently desires to use recent
22 case history to support her recommendations for treatment of customer deposits.
23 In particular, she references the Staff Report in the Suburban Natural Gas

1 (“Suburban”) case, Case No. 07-689-GA-AIR. A review of the working capital
2 recommendations in the Staff Report in that case raises even more interesting
3 issues than just the treatment of customer deposits. The Staff recommends using
4 a formula method for computing cash working capital rather than insisting on a
5 lead/lag study as it does in DE-Ohio’s current case. DE-Ohio agrees with the
6 Staff’s rationale for using a formula methodology for estimating cash working
7 capital but we believe the same formula methodology should have been applied in
8 the present case.

9 **Q. IS THERE ANY REASON THAT SURBURBAN SHOULD BE TREATED**
10 **DIFFERENTLY THAN DE-OHIO IN ESTABLISHING WORKING**
11 **CAPITAL?**

12 A. None that I can determine. Suburban, like DE-Ohio, made its filing under the
13 standard filing requirements for large gas utilities, *i.e.*, those with more than
14 10,000 customers. In its Staff Report in that case, Staff states that the formula
15 method (one-eighth of non-fuel O&M) has been approved by the Commission in
16 previous cases. DE-Ohio recommended substantially less working capital, \$0, in
17 its initial Application than application of the one-eighth of O&M formula would
18 have suggested. It stands to reason that if the formula method accepted by the
19 Staff for computing working capital is acceptable and reasonable, then the
20 Company’s conservative estimate of \$0 for cash working capital should be
21 acceptable and reasonable.

1 **III. AMORTIZATION OF RATE CASE AND OTHER EXPENSES**

2 **Q. DESCRIBE THE OCC’S RECOMMENDATION WITH RESPECT TO**
3 **THE PROPOSED AMORTIZATION OF RATE CASE AND OTHER**
4 **EXPENSES.**

5 A. The OCC recommends that the Commission approve an amortization period of at
6 least six years, and possibly up to nine years, to recover the cost of presenting this
7 case and to recover the deferred costs for curb-to-meter service and riser
8 replacement costs that were removed from the test year expenses.

9 **Q. WHAT IS THE BASIS OF THE OCC’S RECOMMENDATION?**

10 A. The OCC suggests that, based on DE-Ohio’s “recent history” of rate case filings,
11 the Company should only be allowed a six-year amortization period for these
12 expenses. It further suggests that, if the Commission approves the Company’s
13 riders, most of which the OCC opposes in whole or in part, the amortization
14 period should be as long as nine years.

15 **Q. WHAT IS YOUR RESPONSE TO THAT RECOMMENDATION?**

16 A. If the OCC is using history as a guide for choosing the proposed amortization
17 period, it should reach back slightly further beyond the 1995 case it discusses in
18 this case. From 1990 to current, DE-Ohio has had five retail rate cases in those 17
19 years which means it is averaging an interval of about 3.4 years between rate
20 cases. If anything, applying this logic supports the Company’s proposal to use the
21 three-year amortization period.

22 The fact is, however, that the Staff has been recommending amortization
23 periods for other companies without any consideration as to the frequency with

1 which these companies file rate cases. Reviewing other recent case filings,
2 including the ones listed by Ms. Hagans in her testimony, the Staff's
3 recommendation has, in many cases, been to amortize such expenses over as little
4 as three years for companies that have had far fewer rate cases than DE-Ohio has
5 had in the past twenty years.

6 Take the current First Energy case, for example, Case No. 07-551-EL-
7 AIR. The Staff recommended a three-year amortization period and, interestingly,
8 the OCC offered no opposition in its filed Objections to the Staff Report even
9 though the last time any of the First Energy companies filed a full retail rate case
10 was in 1995, twelve years ago. By the OCC's logic, the amortization period they
11 should have recommended for rate case expense in the First Energy case was at
12 least twelve years. The Staff submitted testimony supporting its recommended
13 amortization period saying that "[t]he Staff has historically amortized rate case
14 expense over a period of three to five years. This approach assumes that rates
15 are to be in effect for at least this range."¹ This leaves us with a mystery as to
16 why a shorter amortization period is recommended for First Energy than for DE-
17 Ohio. The fact that the First Energy case is an electric distribution case as
18 compared to our current gas distribution case is irrelevant. The fact that both are
19 subject to essentially the same regulations for determining revenue requirements,
20 and rates, is the critical common denominator.

21 Another example involves another gas distribution company, Suburban
22 Natural Gas case, Case No. 07-689-GA-AIR. Sixteen years have passed since its

¹ See Testimony of Trisha J. Smith, page 6, in Case No. 07-551-EL-AIR, *et al.*, filed February 11, 2008.
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1 last rate case and, again, the Staff recommended just a three-year amortization
2 period. Inexplicably, a different standard is recommended for a similarly
3 regulated company.

4 There are examples of the Staff recommending five-year amortization
5 periods (DE-Ohio's 2001 case and Vectren's 2004 case) for such costs but, even
6 in those cases, there is no apparent evidence that the Staff considered the period
7 between rate cases as a determining factor in its recommendations or that it
8 considered the existence of any riders in making its recommendation.

9 **Q. WHAT OTHER FACTORS SHOULD BE CONSIDERED IN**
10 **DETERMINING THE AMORTIZATION PERIOD TO USE?**

11 A. One significant issue that should not be overlooked is that the issue in question in
12 this case is more than just rate case expenses. In addition to the \$485,000 in total
13 rate expenses (including the fee for Blue Ridge Consulting Services, Inc.), the
14 Company's Application includes a proposal to amortize costs that would
15 otherwise have been collected in one year in the Rider AMRP filing. Included in
16 the Company's test year expenses is \$8,458,123 in curb-to-meter and riser
17 replacement costs. DE-Ohio made a proposal in its Application to begin
18 assuming ownership of the facilities involved in this expense. Because these
19 items will be capitalized and no longer be treated as an expense, we have
20 proposed to set rates at a level which will recover a portion of such costs over the
21 proposed three-year period in order to be made whole for these test year costs.

22 There are two relevant issues related to these expenses that should be
23 weighed when determining the appropriate treatment in the revenue requirement

1 calculation. First, the magnitude of the issue, over \$8.5 million, clearly
2 commands more attention than the relatively minor amount of rate case expenses,
3 only \$485,000. Spreading out recovery of \$8.5 million over an extended period
4 of time increases the likelihood that the Company will not be made whole given
5 the punitive effects of the time-value of money. Possible remedies to avoid losses
6 due to the time-value of money are to either shorten the amortization period or to
7 authorize carrying costs on the unrecovered balance of the cost being amortized.
8 DE-Ohio's proposed three-year amortization without carrying costs is an
9 appropriate balance of all of these factors.

10 A second consideration is that the bulk of the costs at issue relate to
11 expenses that would normally be recoverable over one year in the Rider AMRP.
12 Although the revenue requirement calculation in the Rider AMRP only includes
13 items directly impacted by the AMRP program or, in the modified Rider AMRP,
14 the Riser Replacement program, this accounts for most of the \$8.5 million in
15 expenses proposed to be amortized.

16 **Q. IS THERE A WAY TO ADDRESS THE OCC'S AND STAFF'S CONCERN**
17 **THAT THE COMPANY WILL OVERCOLLECT ITS DEFERRED COSTS**
18 **IF IT IS GRANTED A RELATIVELY SHORT AMORTIZATION**
19 **PERIOD?**

20 A. Yes. If the Commission allowed the Company to incorporate the deferred curb-
21 to-meter and riser replacement costs in the Rider AMRP, it is possible to ensure
22 that no more or less than the actual expense being deferred will be collected from
23 customers. We have already proposed similar treatment for AMRP-related

1 maintenance savings that would normally be included in the test year. As OCC
2 points out in its Objections, “[t]he Company has acknowledged that an estimated
3 amount of \$2,195,736 should have been included” in the Rider AMRP related to
4 maintenance savings.

5 One option to remedy the issue is to reduce base rates by \$2.85 million
6 from the Company’s initial request (*i.e.*, the net adjustment to test year expenses
7 to reflect the proposed three-year amortization of this deferred expense) and then
8 net the deferred \$8.5 million expense with the \$2.2 million maintenance savings
9 amount for the same period. The net number would be included in the Rider
10 AMRP revenue requirement calculation for recovery during the first year the
11 Rider AMRP is once again in effect. After year one of the Rider AMRP, the
12 amount to recover would be \$0.

13 A slightly different alternative is to spread out the net number over a
14 longer period as a rate base component and include a recovery of and on that
15 amount in the Rider AMRP revenue requirement calculation. The effect on base
16 rates would be the same but the impact on the Rider AMRP would be spread out
17 over more than one year. Either way, there should be some appeal in this option
18 for both customer and shareholder in that there is no chance of over- or under-
19 recovery because the Rider AMRP is adjusted each year. The net costs are fully
20 amortized with only \$1 of revenue matching each \$1 of expense – no more and no
21 less. This proposal should satisfy the OCC’s concerns that a short amortization
22 period may permit the Company to over-recover these costs.

1 **Q. WHAT IS YOUR RECOMMENDATION WITH RESPECT TO THE**
2 **RATE CASE AND OTHER EXPENSE AMORTIZATION?**

3 A. I stand by the Company's original proposal to amortize the total of these costs
4 over a three-year period. In my opinion, it is a fair and simple proposal, and it is
5 consistent with similar treatment the Commission and Staff have allowed other
6 similar utilities in the State of Ohio. The only viable alternative is to remove the
7 issue completely from the base revenue requirement calculation, as discussed
8 above, and include a net amount to be recovered in the Rider AMRP over as little
9 as one but no more than three years.

10 **IV. ACCOUNT 894 ADJUSTMENT**

11 **Q. DESCRIBE THE ISSUE RAISED BY THE OCC INVOLVING ACCOUNT**
12 **894 – MAINTENANCE OF OTHER EQUIPMENT?**

13 A. In its Objections to the Staff Report, the OCC objected to "the Staff's failure to
14 make an adjustment in Account 894..." The OCC argues that there were two
15 problems in the Company test year revenue requirement related to this account.
16 First, the test year amount of the expense was not representative of actual test year
17 expense activity and, second, the Company did not budget an appropriate level of
18 revenue to offset the expense. The gist of the OCC's recommendation is that it
19 proposes to reduce the test year expenses by \$504,631.

20 **Q. WHAT IS THE COMPANY'S RESPONSE TO THE OCC'S**
21 **RECOMMENDATION?**

22 A. The Company accepts the OCC's recommendation.

23 **V. SERVICE COMPANY ALLOCATIONS**

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1 **Q. DESCRIBE THE ISSUE RAISED BY THE OCC RELATED TO SERVICE**
2 **COMPANY COSTS ALLOCATED TO DE-OHIO'S NATURAL GAS**
3 **BUSINESS FROM DUKE ENERGY SHARED SERVICES, INC. ("DESS").**

4 A. In its Objections to the Staff Report, the OCC objects to including certain charges
5 allocated from DESS in the test year. Costs allocated to DE-Ohio, from DESS
6 and Duke Energy Business Services, Inc. ("DEBS"), are governed by a Service
7 Company Utility Service Agreement ("Service Agreement") which is referenced
8 by the OCC in its objections. The Service Agreement lists 23 functions or types
9 of services that are provided by the DESS to its client companies. The OCC
10 specifically objects to charges described as associated with (1) Electric System
11 Maintenance; (2) Electric Transmission and Distribution Engineering and
12 Construction; (3) Power Engineering and Construction; and (4) Power Planning
13 and Operations.

14 **Q. HAVE YOU HAD AN OPPORTUNITY TO REVISIT THE COMPANY'S**
15 **TEST YEAR EXPENSES AFTER REVIEWING THE OCC'S**
16 **RECOMMENDATIONS?**

17 A. Yes. There are literally thousands of transactions that are ultimately filtered from
18 the service companies down to the various legal entities and lines of business,
19 including DE-Ohio gas distribution. The Company attempted to respond to a
20 discovery request submitted by the OCC, OCC-INT-04-112, which asked for
21 details associated with costs allocated from the service companies. In responding
22 to the discovery requests, the Company grouped these costs into the 23 functions
23 provided for in the service company agreements. Ideally, we would have a

1 category for every possible cost item that gets charged from the service company
2 but, frankly, that is not practicable.

3 It is understandable why the OCC is confused about the validity of some
4 of the costs allocable from the service company given the labeling of the
5 functions but the mere fact that some costs associated with gas service are
6 grouped with electric costs does not mean that such costs are not legitimately
7 assignable to gas service.

8 In terms of addressing the OCC's issue, we did some additional review of
9 the costs that were included in the four functions that formed the basis of the
10 OCC's objections. As a result of that review, we are willing to reduce our
11 expenses allocated from the service company in the test year revenue requirement
12 by approximately \$525,000 in order to ameliorate some of the OCC's concerns
13 principally because these costs were incurred by responsibility centers that have
14 limited input into the gas distribution business. A summary of these adjustments
15 is shown in Second Supplemental Attachment WDW-2 The OCC had
16 recommended that \$2,029,288 be excluded for not being gas related but, based on
17 our further review, the other \$1,504,288 is much less ambiguous. For example,
18 included in the disputed service company allocation costs in the test year revenue
19 requirement is almost \$250,000 for engineering services which are, in fact,
20 allocated from a gas department responsibility center. Another \$600,000 is
21 attributable to costs allocated from the drafting and mapping responsibility center.
22 There should not be much doubt that the gas business relies on these types of

1 service company provided services notwithstanding the fact that it was grouped
2 with what looks like electric services.

3 Based on the Company's analysis and further review, we recommend that
4 the Commission reduce our test year expenses by \$525,000. However, we do not
5 agree with the OCC's recommendation to exclude the \$2.1 million amount as
6 recommended by Ms. Hagans.

VI. DEPRECIATION EXPENSE

7 **Q. DID THE OCC HAVE ANY RECOMMENDATIONS REGARDING THE**
8 **TEST YEAR LEVEL OF DEPRECIATION EXPENSE?**

9 A. Yes. The OCC objects to the Staff Report in that the Staff failed to address a
10 recommendation proposed by the Staff's auditor, Blue Ridge Consulting Services,
11 Inc. ("Blue Ridge") pertaining to accounting for certain retirements.

12 **Q. HOW DO YOU RESPOND TO THE OCC'S RECOMMENDATIONS**
13 **REGARDING DEPRECIATION?**

14 A. First, we believe that Mr. Hines is in error in his recommendations regarding the
15 treatment of retirements. Second, the OCC either ignored or dismissed a
16 significant error in the Staff Report regarding the treatment of salvage value in the
17 calculation of depreciation accrual rates and, therefore, depreciation expense.

18 **Q. WHY DO YOU BELIEVE THE OCC HAS ERRED IN ITS**
19 **RECOMMENDATION REGARDING THE RETIREMENTS ISSUE**
20 **RAISED BY BLUE RIDGE?**

21 A. In a discovery request from the OCC, specifically OCC-INT-13-468, the
22 Company was asked if it agreed with Blue Ridge's recommendation that

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1 depreciation expense be reduced for non-recorded retirements. The Company
2 responded “no.” In the following discovery request, OCC-INT-13-469, OCC
3 asked why the Company disagreed. Apparently, OCC ignored the Company’s
4 response to this request or was not persuaded by Company’s response. The
5 Company’s response was unambiguous in saying that the Blue Ridge conclusion
6 and recommendation regarding this issue was incorrect and that the retirements
7 Blue Ridge reported as “non-recorded” actually have, in fact, been recorded on
8 the Company’s books.

9 **Q. TO WHAT ACTIVITY DOES THE “NON-RECORDED RETIREMENTS”**
10 **RELATE?**

11 A. The retirements Blue Ridge discusses in its Report relate to additions in Account
12 106 – “Completed Construction Not Classified,” particularly additions for the
13 AMRP.

14 **Q. PLEASE EXPLAIN THE COMPANY’S PROCEDURE FOR**
15 **ACCOUNTING FOR AMRP ADDITIONS AND RETIREMENTS.**

16 A. The Company has maintained its AMRP-related additions to Plant in Service in
17 Account 106 since the beginning of the program in order to identify this activity
18 for the periodic Rider AMRP update filings. As explained to the auditor from
19 Blue Ridge, the Company processes and records retirements of mains and services
20 under the AMRP immediately upon removing the plant from service. Contrary to
21 Blue Ridge’s conclusion, the Company is not waiting to unitize the work orders to
22 Plant in Service to book the related retirements.

1 **Q. IS THERE ANY DOCUMENTATION TO SUPPORT THE FACT THAT**
2 **THESE RETIREMENTS HAVE BEEN RECORDED?**

3 A. Yes. The annual Rider AMRP revenue requirement update filing includes detail
4 of the additions and retirements for the current year and on a cumulative basis.
5 The update filing made in February 2007 for the calendar year 2006 includes
6 cumulative addition and retirement amounts that are very similar to the amounts
7 in the Blue Ridge Report discussing this issue. Blue Ridge indicates there were
8 \$207 million of additions to mains in Account 106 from the AMRP since the
9 Company's last base rate case and, using an average retirement percentage it
10 calculated, approximately \$13.8 million should be recorded for retirement of
11 mains. In the Company's February 2007 Rider AMRP update filing, the
12 cumulative amount of main additions was \$215.5 million and approximately
13 \$15.3 million of retirements had been recorded related to those additions. It is no
14 coincidence that these numbers are similar. Blue Ridge's calculations are based
15 on plant activity primarily from the AMRP and, since the activity was properly
16 recorded, the estimate of "non-recorded retirements" is very close to the actual
17 retirements booked.

18 **Q. DESCRIBE THE ISSUE REGARDING SALVAGE VALUE?**

19 A. Presumably the OCC had an opportunity to review the depreciation accrual rates
20 proposed by the Staff. As the Company pointed out in its Objections to the Staff
21 Report, the Staff's spreadsheet, used to compute depreciation expenses, included
22 a formula error that effectively excluded negative salvage value. The OCC's
23 proposed revenue requirement recommendation should have taken into account

1 the fact that Staff failed to include negative salvage value in its calculation its
2 depreciation accrual rates and its test year depreciation expense. I discussed this
3 error and proposed correction in my supplemental direct testimony filed on
4 January 29, 2008.

5 **VII. CONCLUSION**

6 **Q. DOES THIS CONCLUDE YOUR SECOND SUPPLEMENTAL**
7 **TESTIMONY?**

8 **A. Yes.**

CERTIFICATE OF SERVICE

I certify that a copy of the foregoing Second Supplemental Testimony of William Don Wathen Jr. was served on the following parties of record by electronic filing and by e-mail this 22nd day of February 2008.

_____/s/ John J. Finnigan, Jr.
John J. Finnigan, Jr.

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Case No(s). 07-0589-GA-AIR

Summary: Testimony Second Supplemental of William Don Wathen, Jr. electronically filed by ANITA M SCHAFER on behalf of Finnigan, John J. Mr.