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FILE

BEFORE THE PUBLIC UTILITIES COMMISSION OF OHIO

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In the Matter of: : : The Application of Vectren: Energy Delivery of Ohio, : Inc., for Authority to : Amend its Filed Tariffs to: Increase the Rates and : Charges for Gas Services : and Related Matters. :	Case No. 07-1080-GA-AIR
In the Matter of: : : the Application of Vectren: Energy Delivery of Ohio, : Inc., for Approval of an : Alternative Rate Plan for : a Distribution Replacement: Rider to Recover the Costs: of a Program for the : Accelerated Replacement of: Cast Iron Mains and Bare : Steel Mains and Service : Lines, a Sales : Reconciliation Rider to : Collect Difference Between: Actual and Approved : Revenues, and Inclusion in: Operating Expense of the : Costs of Certain : Reliability Programs. :	Case No. 07-1081-GA-ALT

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TELEPHONE DEPOSITION OF KERRY A. HEID

ARMSTRONG & OKEY, INC.
185 South Fifth Street, Suite 101
Columbus, Ohio 43215-5201
(614) 224-9481 - (800) 223-9481
Fax - (614) 224-5724

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ORIGINAL

taken before me, Rosemary F. Anderson, a Notary Public in and for the State of Ohio, at the offices of Ohio Consumers' Counsel, 10 West Broad Street, Columbus, Ohio, on Wednesday, August 13, 2008 at 10:07 a.m.

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APPEARANCES:

McNees, Wallace & Nurick
By Ms. Gretchen J. Hummel (via telephone)
Fifth Third Center, Suite 1700
21 East State Street
Columbus, Ohio 43215

On behalf of the Company.

Janine L. Migden-Ostrander
Ohio Consumers' Counsel
By Ms. Maureen R. Grady
10 West Broad Street, Suite 1800
Columbus, Ohio 43215-3485

On behalf of the Residential Consumers of the State of Ohio.

ALSO PRESENT:

Vectren:
Mr. Larry Friedeman
Mr. Jerrold Ultry

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KERRY A. HEID

being first duly sworn, as hereinafter certified, deposes and says as follows:

EXAMINATION

By Ms. Grady:

Q. Good morning, Mr. Heid.

A. Good morning.

MS. GRADY: At this time I would like to mark as Deposition Exhibit No. 1 the Notice to Take Deposition Upon Oral examination of Kerry A. Heid and Request for Production of Documents dated June 27, 2008.

(EXHIBIT MARKED FOR IDENTIFICATION.)

Q. Now, Mr. Heid, in that Notice of Deposition you were directed to produce at the time of your deposition all documents relating to your testimony or to your knowledge and expertise with regard to the subject matter of these proceedings and/or your responses to discovery, including, but not limited to, the results of any studies done for these proceedings and any backup documentation, including raw data for those studies.

In response to that notice, what documents did you bring to the deposition this morning?

A. I have brought my direct testimony, including all of the applicable exhibits that were referenced in that testimony, including exhibits or Schedules B-4 and E-5. I've also brought with me copies of my supplemental testimony, including all of the applicable exhibits referenced in that testimony. I've brought with me copies of the workpapers that I filed in this proceeding. I've got two binders that contain the testimony from the OCC and the various parties and the objections that they filed in this proceeding, as well as the Staff Report and the Eagle report and various other workpapers.

Q. Now, Mr. Heid, you said various workpapers. Can you describe those?

A. They were various workpapers that I've used, including the preparation of the cost-of-service study and rate design.

Q. Would those have been workpapers that were filed in this proceeding or no?

A. Those would include workpapers that were filed in this proceeding. It included various items that I consider the official file, which would include copies of the prefiled and notice, copies of the decoupling order, copies of the main study and meter study, which I think were also included in field workpapers, just the various copies of the depositions that have occurred to date.

Q. Thank you.

MS. GRADY: Gretchen, if I could have one minute, I would appreciate it.

MR. HUMMEL: Okay.

(Discussion off record.)

Q. (By Ms. Grady) Mr. Heid, go to your direct testimony, page 4, lines 14 through 15. You testified the E-3.2 was the cost-of-study service for the test year ending May 31, 2008 with the date certain of August 31, 2007; is that correct?

A. Yes.

Q. And then you go on to state that the cost-of-service study is based on three months of actual data and nine months of estimated data.

A. Yes, sir.

Q. Now, the pro forma A revenue levels that you refer to in the schedules, those would be the present revenue levels of the company showing the three months actual and nine months projected without adjustments, if you know?

A. It would not include the proposed rate increase. It would be made up of the test year actual numbers, plus the pro forma adjustment, but not including the proposed rate increase itself.

Q. Okay. Just so I'm clear, it would be the three and nine with the pro forma adjustment at the actual -- at the present revenue levels?

A. That is correct.

Q. Now, pro forma B would show the results with the proposed revenue that's being sought by VEDO; is that correct?

A. That is correct.

Q. And the three and nine data would be adjusted for the pro forma adjustments that the company is making in this case.

A. Yes. They tie back to the income statement from Ms. Hardwick.

Q. Now, page 28 of your schedule, that would be 28 of E-3 -- let me back up a second. E-3.2 is your cost-of-service study; is that correct?

A. Yes.

Q. If we go to page 28 of that study, we see, do we not, a comparison of the pro forma operating revenues and the resulting dollar subsidy at present and proposed rates. Is that what that shows?

A. Yes.

Q. I want to focus on that schedule for a moment. Line 1, rates 310 and 315 would be residential customer class, correct?

A. That's correct.

Q. And Column B is the revenues at present rate, that would be the three and nine plus the pro forma adjustments.

A. Yes.

Q. Now, then you compare the revenues at present rates to the revenues required for equalized returns. That would be Column C.

A. Correct.

Q. And could you tell me the derivation of Column C?

A. The derivation of Column C is included in the preceding workpapers or the preceding schedule, pages 1 through 27. That is simply adjusting the revenues so that it would generate equal rates of return by rate class.

MR. HUMMEL: I think someone may have joined the call. Is someone else on the phone now?

Okay. I sorry, I thought I heard a beep.

MS. GRADY: I did hear a beep as well.

MR. HUMMEL: That's comforting, thank you. And Mr. Freedmen just joined me.

MR. FRIEDEMAN: Good morning.

MS. GRADY: Is it Mr. Friedeman that caused the beep.

MR. FRIEDEMAN: My pacemaker.

MR. HUMMEL: Oh, thank you.

Q. You said Column C is derived from the preceding workpaper or the preceding schedule, page 1 through 27 of E-3.2, did you say that?

A. Yes, I did.

Q. Then you would subtract Column B from Column C to get the present subsidy under the pro forma revenues at present rates.

A. Yes.

Q. Okay. On the other half of this schedule you have the pro forma revenues proposed rates, and, again, when we say pro forma there, we're talking about the three and nine test year data plus any adjustments proposed by the company to the three and nine at proposed rate levels, correct?

A. Yes. In other words, Column C and D

would be the pro forma A that we initially talked about; Columns E, F and G the pro forma B.

Q. Now, in the section of Schedule E-3.2, page 28 of 40, entitled Pro Forma Revenues Proposed Rates, which you call pro forma B, can you tell me the first column, Revenues Required for Equalized Returns, is that derived from the previous 27 pages to E-3.2?

A. Yes. Actually, all of these numbers were derived on those preceding pages.

Q. And the column entitled Ending Subsidy is Column F minus Column E?

A. Correct.

Q. And the column entitled Subsidy Reduction, that reflects the rate design decision of the company to reduce the subsidy; is that correct?

A. That's correct.

Q. Now, Mr. Heid, if the pro forma revenues at present rates are understated for class 310 and 315, then the subsidy or Column D would be overstated; is that correct?

A. Are you speaking in terms that the total revenues being overstated or by customer class?

Q. By customer class.

A. I don't understand your question.

Q. I guess if we look at rates -- the subsidies that you calculated are on a rate class basis; is that correct?

A. Yep.

Q. Okay. So if the pro forma revenues at present rates are understated for a particular class, then the subsidy that you calculate for that class would be overstated; is that correct?

A. Well, its depends.

Q. Can you explain?

A. It depends on how that pro forma revenue at present rates was lower than what we reflect here. If it is a function that all of the so-called pro forma A revenues are lower, in other words, the total revenues of present rates were lower, then that would have a flow-through effect, including an effect on the subsidy reduction.

Q. And is that because the subsidy reduction -- the revenues required for equalized return are backed into?

A. Yes.

Q. Okay. So what you're saying is if the total revenue shown at present rates is understated, then the revenue required for equalized return would be overstated and the subsidies would be overstated.

A. If the pro forma revenues at present rates are understated, then that's going to, as I said, have a flow-through effect. It would affect the total amount of the increase and would affect the subsidies by customer class, as well as the amount of the overall increase.

Q. And, Mr. Heid, the rate design adopted by the company is based in large part upon conclusions the company reaches as to whether a subsidy is present for a particular rate class; is that correct?

A. Yes. Our goal is to move towards equal rates of return that at the same time consider and mitigate any potential rate shock resulting from that movement.

Q. Now, on page 7 of your testimony, lines 29 through 33, you speak to the data used to perform the cost-of-service study, and you indicate on line 31 that: "The customer and volume statistics by rate class were developed by summarizing data contained in E-4 and E-4.1."

A. Yes.

Q. If the customer volume and statistics that you relied upon to run your cost-of-service study were inappropriate, it would have an impact on your cost-of-service study, wouldn't it?

A. Yes. As we discussed, if the pro forma A revenues change, it will have a flow-through effect on virtually all of the numbers.

Q. Now, on page 11 of your testimony you reference at line 18 "the long-established Commission policy." Do you see that reference?

A. Yes, I do.

Q. Are you talking about the PUCO or some other commission?

A. Well, both, actually. Here I'm specifically talking about the Ohio Commission, but I think it would be fair to generalize that virtually all of the commissions have a goal and probably a statutory requirement as well to move towards cost-based rates.

Q. Do you know if the Ohio Commission has a statutory requirement to move towards cost-based rates?

A. I could not point to a specific statute. I'm sure there is a statute that probably requires that rates be not unduly discriminatory, and that is commonly defined as cost based.

Q. Now, is your knowledge of the longest established -- let's talk about the commission policy being the PUCO. How did you gain your knowledge of the PUCO policy with respect to revenue distribution?

A. Well, as I say, I couldn't point to a specific statute, but this was really based more on general observation and knowledge and by participation in the previous VEDO rate case.

Q. Beyond the previous VEDO rate case, do you have any independent knowledge of the PUCO policy with respect to revenue distribution?

A. Well, I am familiar with the rate cases that other companies have filed. They typically file a cost-of-service study. A cost-of-service study is required to be filed in Schedule E-3.2, and the only purpose of filing a cost-of-service study would be in determining the cost to serve individual customer classes.

Q. So you're saying that the other companies that have filed E-3.2. Can you tell me, have you read those filings, or are you just intuitively saying if other companies are required to file E-3.2, then the cost-of-service study must be used in the design of rates.

A. Both.

Q. Can you tell me how you define "long" in that phrase, "long established" in terms of the PUCO?

A. No, I couldn't give you a specific number of years.

Q. Can you explain to me how you used the earnings indices to guide you in moving to equal rates of return as referenced on page 11, lines 25 through 26?

A. Yes. The cost-of-service study determined the resulting rate of return on rate base by customer class. If you take the rate of return for an individual customer class and divide that by the overall system rate of return, that gives you what is referred to as an earnings index. If that earnings index is below 1, that would show that the customer class rate of return is below the system rate of return, and, therefore, you would conclude that they are being provided a subsidy, whereas if the earnings index was above 1, that would demonstrate the customer class rate of return was greater that the overall system rate of return and, accordingly, you would conclude that they were providing a subsidy.

Once we determined those earnings indices for each customer class, and we want to move each earnings index for each customer class towards a value of 1, and then the only question whether you go all the way to a value of 1 or whether you just move partway in order to mitigate potential rate shock.

Q. When you talk about the rate shock, can you define what you mean there?

A. I always say you know it when you see it.

Q. Like obscenity.

A. Really, there is no definition that I'm aware of.

Q. Now, that leads into my next question, and that goes to page 12 of your testimony on line 16 you indicate that "other factors militate against moving completely to cost of service rates." Do you see that reference?

A. Yes, I do.

Q. Can you tell me what those other factors are?

A. It would primarily be the concern for rate shock for a particular customer class.

Q. Let's talk about the residential class.

Can you define -- I know you said you know it when you see it, but for Vectren can you define when rate shock would occur in terms of moving towards cost of service for the residential customers in the context of this rate case?

A. Well, we certainly would not want to see residential bill impact above 10 percent, so one of our objectives is to keep the residential increase below 10 percent.

Q. When you say residential bill impacts, are you talking about the total bill or talking about customer charge? I want to understand exactly what you're saying, Mr. Heid.

A. I'm talking about the total revenue increase for the customer class and also that would translate into the effect on an average residential customer. In other words, we would not want the overall revenues for the residential customer class to increase in the double digits, nor would we want the average residential customer to have that high of a bill impact.

Q. And average, you are talking about an average use customer, residential?

A. Yes, I am.

Q. And do you know for Vectren what the average use residential customer is, how many Ccf?

A. Give me one moment. I believe I included that in my schedule, but let me look. It's 81 Mcf, to the best of my recollection, but I'm still looking to see whether I included that in my exhibit. 81 Mcf, I apparently did not, but I believe it was in the range of 81 Mcf per year.

Q. Okay. The 10 percent figure that you said, you said you would not want to see the residential bill impacts go into double digits. The 10 percent figure, how is that derived? What is it based on?

A. That really is just an internal Vectren guideline where they do not want to create that great of a bill impact on residential customers.

Q. Was that internal Vectren guideline communicated to you?

A. I'm sorry, say that again.

Q. Was that internal Vectren guideline communicated to you?

A. Yes. When we go through the rate design process, it is not me in isolation, obviously, that is doing that. I actually meet with Mr. Ulrey and other members of the Vectren team and we discuss the amounts of the subsidy reduction and the rate design, and that was communicated in the context of those suggestions. It's also important to point out that the total bill impact that I'm talking about includes gas costs, and so the total bill impact is kind of a moving target because as the gas costs get higher, then, obviously, we recognize that the bill impacts are more severe overall for the residential customers, and we try to maybe moderate bill impacts even below the 10 percent range.

Q. Is it your assumption that the total gas cost will continue to increase for customers?

A. I don't have any opinion on that. You know, certainly it's higher than it has been in preceding rate cases.

Q. You talked about the 10 percent being an internal Vectren guideline. Is there a guideline, other than Vectren's internal guideline, that you have for defining rate shock for Vectren's customers? Let's start with Vectren's customers.

A. I'm sorry, could you say that again?

MR. HUMMEL: And also, Ms. Grady, we might want again for the sake of consistency say

Vectren when only referring to the corporation and VEDO when referring to VEDO.

MS. GRADY: Understood.

Q. Mr. Heid, when I have been using the term Vectren, how have you understood it?

A. I have understood it to mean VEDO generally.

Q. Okay. I appreciate that. I will try to be more accurate with respect to that.

Mr. Heid, where I'm going, we talked about this internal Vectren guideline which essentially says, as you communicated, that you don't want to see the residential bill impact go above 10 percent or go into double digits. My question is, do you have your own internal guideline at which point you would say if the residential bill impact is above X percent, then there is going to be rate shock.

A. No, I really don't. I share Vectren's belief. You know, keep in mind that I was director of rates for Vectren and worked for them for about 13 years, so I do share a lot of the same beliefs and positions as Vectren, and in this case I certainly share that opinion.

Q. Now, again, this is going back, just

cleaning up here, you had indicated on page 12, line 6, there were other factors militating against moving completely to cost-of-service rates, and we talked about rate shock. Are there any other factors that you are referencing there on those lines of your testimony?

A. That is certainly the primary consideration. I can't think of any other consideration right now.

Q. Now, if I went to E-3.2, page 24 of 40, I would see the rate of returns by class under the present rates; is that right?

A. Give me that reference again.

Q. 3.2, page 24 of 40.

A. Yes. That would show the resulting rate of return at the pro forma A; in other words, that's the present revenue level; in other words, that's what the actual rates are generating as far as rate of return on rate base.

Q. And line 14 you show the current rate of return for each class?

A. Correct.

Q. And that's mathematically derived how?

A. It would be line 12, the net operating income, divided by line 13, the original cost to rate base.

Q. Thank you. E-3.2 page 27 of 40, I'll give you a moment to find that, that's the rate of returns by class proposed to be used in the design of rates for the company; is that right?

A. That's correct.

Q. And to see the movement proposed to reduce the subsidy, we would compare page 27 to page 24; is that right?

A. That's correct.

Q. And for the residential customers the earning index would go from negative 161 to 60 percent?

A. Yes. And that's actually shown on schedule E-3.2, page 29 of 40.

Q. Okay. When you go on the earnings index from a negative 161 percent to a 60 percent, that represents a reduction in the subsidy?

A. Yes, it does. If it's moving closer to a subsidy -- or an earnings index of 1, then that would represent a subsidy reduction.

Q. Okay. Now Schedule E-4 shows the sales by rate revenue; is that right?

A. I'm sorry, if I could maybe expand on my last answer.

Q. I'm sorry, I didn't mean to cut you off.

A. That's fine. Under the earnings index if you move closer to a earnings index of 1, that would demonstrate a subsidy reduction. As I had discussed in my supplemental testimony, it is possible that the earnings index could move closer to a factor of 1, but, yes, a dollar subsidy would increase. So simply because the earnings index would move closer to a factor of 1 does not, by itself, indicate that a subsidy reduction is occurring. It simply indicates that using this measure of subsidy reduction is occurring, but it is possible that the dollar amount of the subsidy would be increasing at the same time.

Q. Okay. Thank you. Now, Schedule E-4, that shows sales by rate revenue; is that right?

A. Yes.

Q. And, if you know, that is based on the three and nine unadjusted revenues by class?

A. No. That would be -- that would include the pro forma adjustments to the volume.

Q. I'm sorry. That would be based on the three and nine plus pro forma adjustments done by the company to its application?

A. That's correct.

Q. Now, E-4.1 shows billing determinates by rate schedule and customer class based on the three months actual and three months estimated; is that right?

A. Yes. E-4.1 simply shows all of the detail and then that rolls up to Schedule E-4. I was going to say they do show the pro forma A adjusted, in other words, including the pro forma adjustments.

Q. Now, Mr. Heid, when is it appropriate to use actual test year revenues by class to establish rate design for a utility?

A. You mean actual without any pro forma adjustments?

Q. Yes.

A. Well, the only time it would be appropriate is if there was no need for the pro forma adjustments; in other words, if your test year was completely representative of your current conditions, which rarely, if ever, exist.

Q. When is it appropriate to use the actual test year revenues by class with pro forma adjustments to establish rate design?

A. Always.

Q. Is it preferable to use actual test year revenues as opposed to a projected test year revenue figure with adjustments?

A. I don't really have any opinion on that. If you're asking me whether a completely 12-month historical period is more appropriate than a three and nine test year?

Q. I guess I'm asking you whether an actual 12-month period of time is more appropriate to use than a three months actual and nine months projected period of time for revenues.

A. No. I would not agree with that. First of all, I don't believe that's what the requirement is in Ohio, but I believe that the three and nine is more representative simply because you're able to reflect the changes that you anticipate to occur in that nine-month period.

Q. Do you know for Vectren, in fact, Mr. Heid the three and nine is more representative than the 12-month actual revenues?

A. You're really getting outside of my area here. That would probably be a question more appropriately addressed to Ms. Hardwick. I simply use their revenue requirement numbers in performing the cost-of-service study and rate design. If they had used the 12-month historical, I would have used those numbers for my purposes, so I really don't have any opinion on that. I think that would be more appropriate to address to another witness.

Q. I appreciate that, Mr. Heid. Now, did you review the staff report in this case?

A. Yes, I did.

Q. And, in particular, did you review the staff report, the section of the staff report which addressed rate design and cost of service?

A. Yes, I did.

Q. Would it be your conclusion that the staff has accepted the methodology that you have used in your cost-of-service study?

A. I believe they accepted the results of the cost-of-service study. They did, however, use a different revenue distribution that was based upon the cost-of-service study. So we both started with the same cost-of-service study, but in moving towards equal rate of return, we did that in different ways.

Q. Okay. You have the staff report in front of you, do you not?

A. I can get that here, hold on.

Q. Can you turn to table 3 on page 29 of the staff report.

A. Yes.

Q. Is it fair to say, Mr. Heid, that table 3 compares the staff's proposed allocation of the rate increase with your proposed allocation.

A. I believe that is what that purports to represent. Honestly, I have not checked those numbers to see if that is what is going on on that table because that's simply not the way that we approach the revenue distribution or rate design.

Q. So you wouldn't know why the -- you wouldn't know what the staff's comparison is there and how it would differ from the results of your cost-of-service study?

A. Well, I assume that it differs simply because they used a different approach to revenue distribution than we did.

Q. And that's where you would believe the result, the comparison differs, as opposed to a difference in the cost-of-service study results?

A. Yes. I saw nothing in the study that would lead me to believe that they disagreed in any way with the cost-of-service study, and they did include affirmative statements with respect to the cost-of-service study. They started with the same cost of service that VEDO did, but in moving toward equal rate of return, they used a different approach so they ended up having different revenue targets, if you will, and the total revenue increase to classes, what's different than what VEDO had proposed.

MS. GRADY: Mr. Heid, that's all the questions I have for you this morning. I appreciate your time.

At this point I open up for cross-examination for any other parties that intervened in or represent parties in the rate case.

(No response.)

MS. GRADY: Hearing no response, we can conclude and go off the record.

(The deposition concluded at 10:44 a.m.)

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State of Ohio :
: SS:
County of ____________________ :

I, Kerry A. Heid, do hereby certify that I have read the foregoing transcript of my deposition given on Wednesday, August 13, 2008; that together with the correction page attached hereto noting changes in form or substance, if any, it is true and correct.

____
Kerry A. Heid

I do hereby certify that the foregoing transcript of the deposition of Kerry A. Heid was submitted to the witness for reading and signing; that after he had stated to the undersigned Notary Public that he had read and examined his deposition, he signed the same in my presence on the ________ day of _______________________, 2008.

____
Notary Public

My commission expires ___________________, ________.

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CERTIFICATE

I do hereby certify that the foregoing is a true and correct transcript of the proceedings taken by me in this matter on Wednesday, August 13, 2008, and carefully compared with my original stenographic notes.

Rosemary F. Anderson / Vst

Rosemary Foster Anderson,
Professional Reporter and
Notary Public in and for
the State of Ohio.

My commission expires April 5, 2009.

(RFA-8186)

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