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BEFORE
THE PUBLIC UTILITIES COMMISSION OF OHIO

In the Matter of the Application of Columbia Gas of Ohio, Inc. for Authority to Amend Filed Tariffs to Increase the Rates and Charges for Gas Distribution.	))))	Case No. 08-72-GA-AIR
In the Matter of the Application of Columbia Gas of Ohio, Inc. for Approval of an Alternative Form of Regulation and for a Change in its Rates and Charges.	))))	Case No. 08-73-GA-ALT
In the Matter of the Application of Columbia Gas of Ohio, Inc. for Approval to Change Accounting Methods.	)))	Case No. 08-74-GA-AAM
In the Matter of the Application of Columbia Gas of Ohio, Inc. for Authority to Revise its Depreciation Accrual Rates.	)))	Case No. 08-75-GA-AAM

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OBJECTIONS TO THE STAFF REPORT
OF INVESTIGATION
AND SUMMARY OF MAJOR ISSUES
BY
THE OFFICE OF THE OHIO CONSUMERS' COUNSEL

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September 22, 2008

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I. INTRODUCTION

The Office of the Ohio Consumers' Counsel ("OCC"), a party to the above-captioned cases, hereby submits these objections[1] to the Staff Report of Investigation ("Staff Report") which was filed on August 21, 2008 concerning the Application of Columbia Gas of Ohio, Inc. ("COH" or the "Company") to increase its rates and charges for natural gas distribution service to Ohio customers.[2] The OCC is the state representative of approximately 1.4 million COH residential natural gas utility customers

[1] The objections are filed pursuant to R.C. 4909.19 and Ohio Adm. Code 4901-1-28(B).

[2] COH's application ("Application") in this proceeding was filed on March 3, 2008.

in this proceeding before the Public Utilities Commission of Ohio ("PUCO" or "Commission").

The OCC submits that these objections meet the specificity requirement of Ohio Adm. Code 4901-1-28. The OCC's objections point to matters in the Staff Report where COH's rates or service terms would exceed or contravene what is reasonable and lawful for residential consumers.

OCC reserves the right to amend and/or supplement its objections in the event that the PUCO Staff changes, modifies, or withdraws its position, at any time prior to the closing of the record, on any issue contained in the Staff Report. Additionally, where PUCO Staff has indicated that its position on a particular issue is not known at the date of the Staff Report, OCC reserves the right to later supplement its objections once PUCO Staff's position is made known. OCC also reserves the right to file additional expert testimony, produce fact witnesses and introduce additional evidence. OCC also submits that the lack of an objection in this pleading to any aspect of the Staff Report does not preclude OCC from cross-examination or introduction of evidence or argument in regard to issues on which the PUCO Staff changes, modifies, newly raises or withdraws its position on any issue between the issuance of the Staff Report and the close of the record. Moreover, the OCC reserves the right to contest other aspects of COH's Application not specifically addressed by the Staff Report.

Pursuant to R.C. 4903.083, OCC submits a "Summary of Major Issues" that outlines the major issues to be determined in this proceeding. OCC respectfully requests that these issues be included in the notices to be sent to customers to inform them of the local public hearings that will be scheduled in accordance with R.C. 4903.083.

II. OBJECTIONS TO THE STAFF REPORT

A. Revenue Requirements

The OCC objects to the Staff recommended revenue increase on Schedules A-1 because it is excessive due to the use of inappropriate and incorrect rate base, operating expenses, and rates of return, as detailed below in the OCC's objections to Staff's determination regarding these matters.

The OCC objects to each component of the Staff Report's Schedules A-1 recommended revenue increases to the extent that other OCC objections have an impact on the calculation of the recommended revenue increase (e.g. rate base, operating income, rate of return).

B. Rate Base: Other Rate Base Items

1. Cash Working Capital

a. Federal Income Tax

The OCC objects to the negative current income tax reflected on Schedule B-5, Line (13) of the Staff Report, as the Company will not incur a negative current income tax expense under normal conditions. In addition, it has not been established that any lag would be applicable to a negative current income tax expense.

b. Interest Expense

The OCC objects to the negative interest expense reflected on Schedule B-5, Line (25) of the Staff Report. The interest expense included in the lead-lad study should be the positive interest calculated by multiplying the weighted cost of debt by the Company's rate base.

2. Gas Stored Underground

The OCC objects to the balance of gas stored underground reflected on Schedule B-5, Line (29) of the Staff Report. The balance of gas stored underground of $95,830,000 is not representative of the average balance that could reasonably be expected to exist during the forecasted months of the test year and the balance that has, in fact, existed during the months in 2008 for which actual data are available..

3. Accumulated Deferred Income Taxes

a. The OCC objects to the balance of accumulated deferred income taxes on Schedule B-6, Line (20) of the Staff Report, in that the balance of deferred taxes related to the Headquarters Building is understated by $144,000

b. The OCC objects to the balance of accumulated deferred income taxes on Schedule B-6, Line (24) of the Staff Report, in that the balance of deferred taxes related to PIPP is understated by $660,000.

4. Deferred Bad Debt

The OCC objects to the inclusion of Deferred Bad Debt – Unamortized 2001 Balance of $7,293,000 (Staff Report, Schedule B-6, Line (28)) in rate base, because: a) the Commission never approved the creation of a regulatory asset for this item, and b) the balance will be completely amortized shortly after the rates in this case go into effect. Alternatively, if the Deferred Bad Debt is included in rate base, the balance should be offset by applicable deferred taxes.

C. Operating Income

1. Revenues

The OCC objects to the Staff's determination of adjusted and pro forma revenues, because the test year use per customer for residential customers in the Staff Report is understated.

2. O&M – Expenses – Effect of IBM Contract

The OCC objects to the Staff's O&M Expense Adjustment on Schedule C-3.15 of the Staff Report, in that said adjustment fails to completely remove the effect of the failed IBM outsourcing contract from the determination of the Company's test year operating expenses and revenue requirement.

3. Incentive Compensation

The OCC objects to the Staff Reports' inclusion of incentive compensation in the revenue requirements related to the attainment of financial goals. The cost of incentive compensation related to the attainment of financial goals should be borne by shareholders, not ratepayers, since such incentive compensation benefits only shareholders.

4. Uncollectible Accounts Expense

The OCC objects to the Staff's calculation of adjusted uncollectible expense on Schedule C-3.7 of the Staff Report, in that the Staff method of determining annualized uncollectible expense improperly includes the gross receipts "gross up" in the uncollectible expense calculation

5. Deferred Survey Costs

The OCC objects to the Staff's failure to remove the charge-off of deferred survey costs incurred prior to the test year from adjusted test year operation and maintenance expense

6. Amortization of Warm Choice Costs

The OCC objects to the Staff's amortization of the Warm Choice Program Balance over three years on Schedule C-3.14 of the Staff Report. The deferred balance should be amortized over five years, consistent with Staff's amortization of rate case expense.

7. Property Taxes

The OCC objects to the Staff's adjusted property tax expense on Schedule C-3.17g of the Staff Report. Staff improperly used a projected property tax rate instead of the latest known actual property tax rate to calculate the adjusted property tax expense.

8. Payroll Taxes

The OCC objects to the Staff Reports' calculation of *pro forma* payroll tax expense, since the payroll taxes should be adjusted to reflect necessary adjustments to labor expense as described in the OCC's previous objections regarding labor expense.

9. Flow Through Tax Depreciation

The OCC objects to the Staff's calculation of the "Deferred Income Tax Adjustment – Flow Through" on Schedule C-4, Page 2 of the Staff Report. Staff improperly bases the calculation of this item on a speculative and overstated estimate of the 2008 excess of book over tax depreciation.

10. Gain on Sale of Property

The OCC objects to the Staff's failure to adjust test year operating income to reflect the gain on sale of property as described ion pages 99-100 of the Report by Blue Ridge Consulting Services, Inc. submitted August 13, 2008.

D. Rate of Return

The OCC objects to the Staff Report's recommendation for a common equity rate in the range of 9.95% to 10.96%,[3] which is unreasonably high. The OCC objects to the Staff Report's calculated common equity cost and rate of return on the following bases:

1. Group of Comparable Utilities

The OCC objects to the Staff Report's use of a group of only six companies in its group of "comparable utilities" that served as a basis of its capital structure and cost of capital analysis. Furthermore, this group of six companies includes Center Point Energy (CNP) and Sempra Energy (SRE), companies which are considered to be integrated or combination electric and natural gas companies and not a natural gas distribution company.

2. Capital Structure

The OCC objects to the Staff Report's use of an unlawful hypothetical capital structure which is the average book value capital structure of the six companies in the Staff's comparable group.[4] This is not the capitalization used by the Company to attract and raise capital.

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[3] Staff Report at 10-12 Schedule D-1 (Pg. 96) (August 21, 2008).

[4] R.C. 4909.15(D)(2)(a).

3. Capital Asset Pricing Model ("CAPM")

The OCC objects to the Staff Report's inappropriate risk premium of 6.5% in the CAPM.[5] The risk premium stated in the Staff Report was based on the spread of the arithmetic mean of historical total returns between large stocks for large companies and long-term government bonds between 1926 and 2007. This approach is subject to a myriad of empirical errors which make these historical returns poor measures of expected returns. The use of historical return to estimate an expected risk premium can be erroneous because (1) ex post returns are not the same as ex ante expectations, (2) market risk premiums can change over time, increasing when investors become more risk-averse, and decreasing when investors become less risk-averse, and (3) market conditions can change such that ex post historical returns are poor estimates of ex ante expectations. This approach is outdated, ignores twenty years of academic and professional research on the equity risk premium, and is out of touch with the real world of finance. The research and surveys of investment banks, consulting firms, and Chief Financial Officers, who use the equity risk premium concept every day in making financing, investment, and valuation decisions, indicates an equity risk premium in the 4 percent range is appropriate.

4. Discounted Cash Flow ("DCF") Analysis

The OCC objects to the Staff Report's use of a multistage DCF model which includes a growth rate that is a combination (1) the average of projected EPS growth from Wall Street analysts (as collected and compiled by Reuters, Yahoo!, and MSN) and *Value Line* and (2) a long-term growth rate equal to the projected GNP growth rate. It is well known that the EPS growth rate projections of Wall Street analysts are

[5] Staff Report at 14.

upwardly biased and produce an overstated DCF equity cost rate. Furthermore, the Staff had provided no theoretical or empirical support to justify using the projected GNP growth rate as the expected long-term DCF growth rate.

5. Flotation Costs

The OCC objects to the Staff Reports' incorporation of an excessive flotation cost adjustment to the cost of equity.[6] This adjustment is erroneous. The Staff has not identified any actual flotation costs for the Company. Therefore, the Staff is recommending that the Company receives annual revenues in the form of a higher return on equity for flotation costs that have not been identified by the Staff.

6. Rate of Return Adjustment for Alternative Regulation

The OCC objects to the Staff Report's failure to make an adjustment to reduce the recommended rate for common equity in recognition of the reduced risks that the Company will face with respect to revenues and cost recovery if the Commission approves any of the risk-reducing mechanisms or Riders proposed by the Company. These mechanisms are the Infrastructure Replacement Program ("IRP") Rider which, as proposed by the Company, will provide for the recovery of costs associated with 1) an accelerated main replacement program, 2) the costs of a natural gas riser/service line replacement program, and 3) a new advanced metering program. In addition, the Staff recommends a dramatic change to the Company's existing rate design that guarantees revenues for its distribution service by significantly increasing the fixed monthly charge and decreasing/eliminating the volumetric rate over the next two years. Although the Staff Report acknowledged that these mechanisms would reduce the risk faced by the

[6] Staff Report at D 1.1.

Company, the Staff failed to make any corresponding reductions to the rate of return to reflect these reduced risks.[7]

E. Rates And Tariffs

1. Rate Design

OCC objects to the Staff's recommendation of a rate structure primarily based on a fixed distribution service charge, or Straight Fixed Variable ("SFV").[8] The Staff unreasonably strayed from the traditional, and more appropriate, rate structure of a minimal customer charge (presently $6.50 per month, or alternatively reduced for purposes of conservation) and a volumetric rate or blocks of rates. A Decoupling Rider that includes a customer charge at its present level (or further reduced for purposes of conservation), with sufficient consumer safeguards, and with an accurate weather normalization calculation is preferable to the Staff's SFV recommendation. The Staff's SFV design sends an improper price signal to the consumer, fails to encourage conservation, adversely affects the Company's energy efficiency efforts, and does not comport with the economic theory of competitive markets or the actual practices of competitive markets. Finally, the Staff admits the SFV design results in price increases to low use customers[9] who may ultimately be driven from the system leaving their additional costs to be absorbed by fewer remaining customers.

OCC objects to the Staffs failure to recommend that if SFV rate design is implemented, notwithstanding OCC's objections to the contrary, modifications

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[7] Staff Report at 12.

[8] Staff Report at 21-24.

[9] Staff Report at 22.

are needed in COH's proposed SFV rate design to provide relief to low income low usage customers.

2. Cost of Service

OCC objects to the Staff's finding that the Company's cost of service methodology is reasonable.

a. The Company improperly allocated its largest plant investment, Mains, partially on number of customers and partially on its selected demand allocator. There is no reasonable planning, design, or operational reason to allocate any portion of COH's Mains based on customer counts.

b. The Company's cost of service methodology for demand-related costs improperly relies on the system coincident, design day method to assign cost responsibility. This method does not reasonably reflect COH's cost causation and assumes facts and circumstances that are not present in COH's system. The cost of Mains should be allocated using the Peak and Average method in which equal weight is given to annual throughput (average demand) and design day peak demand.

3. Revenue Distribution

OCC objects to Staff's failure to consider a properly conducted cost of service study, competition/value of service, and gradualism in its recommended distribution to customer classes of the revenue increase in this case. No class should receive more than 150% of the Company-wide revenue increase and no class should receive less than 50%.

4. Volume Banking and Balancing Service

OCC objects to the Staff's failure to consider a review of the rates that COH charges customers who subscribe to the Volume Banking and Balancing Service to assure that the rates are cost based and not subsidized.

F. Proposed Alternative Regulation Plan

1. Infrastructure Replacement Program ("IRP") Rider

OCC objects to the Staff's failure to oppose the Company's proposed IRP Rider on the basis that it represents single issue ratemaking. The recovery through the IRP Rider considers only one aspect of the determination of fair and reasonable rates. With regard to both the Company's metallic Accelerated Mains Replacement Program ("AMRP") and Advanced Meter Reading ("AMR") installation programs, there does not appear to be anything extraordinary about these programs that would jeopardize the financial integrity of the Company absent automatic rate recovery. Single issue ratemaking ignores the matching principle of considering cost savings directly associated with such capital programs, and more importantly, does not reflect or consider all other aspects of the ratemaking process such as increased utilization through customer growth, decreases in expenses through technological change, changes in capital costs, etc.

2. Accelerated Main Replacement Program

a. Staff has supported COH's AMRP proposal despite a failure by COH to support its proposal with cost/benefit analysis.

OCC objects to Staff's recommendation that the Columbia's AMRP proposal to replace all trouble prone mainlines will enhance the safety and reliability of Columbia's pipeline system and that these costs should be recovered through an alternative regulation mechanism, Rider IRP. The Staff and the Company provide no estimates of the total costs and benefits of the AMRP based on any clearly-defined and commonly-accepted cost/benefit analysis methodologies.

OCC objects to Staff's citation of the approximately $8.5 million in O&M savings achieved through another LDC's (i.e. Duke Energy Ohio) Accelerated Main Replacement Program without mention the total investment of $255 million made by Duke on the AMRP up to now. Any O&M savings must be compared with the investment involved in achieving such a saving. Furthermore, the Staff has failed to define the baseline for the O&M expenses for purposes of determining this offset.

OCC objects to Staff's support of Columbia's AMRP in general. Staff's support is not based on any cost-benefit analysis of the AMRP conducted by Columbia, the PUCO Staff, or any independent third parties. There is no evidence in the record to support the Company's 25-year plan with annual replacement of 160-miles mains at an average cost of $73.6 million per year (in 2007 dollars) as reasonable and cost-effective.

b. Staff has supported COH's AMRP proposal despite a failure to demonstrate that the AMRP is necessary for the provision of safe and reliable service.

OCC objects to Staff's support of Columbia's AMRP as there is no finding that Columbia is not currently providing safe and reliable service (Columbia's application and discovery response specifically states that it is providing safe and reliable service), or any existing state or federal regulations mandating the replacement of bare-steel, unprotected coated steel, and cast or wrought-iron within a specific period of time.

c. Staff has supported COH's AMRP proposal despite a failure by COH to provide accurate and reflective estimates of future costs.

OCC objects to Staff's acceptance of the cost estimates of various components of the AMRP program as these cost figures are current estimation of future costs over an extended period of 25 years. These cost figures and the proposed schedule are at best speculative and unreliable. The Company provides no credible explanation on how these cost estimates and schedules were developed and the Staff has not independently verified the schedules or estimates. There is also no credible evidence presented that Company has sufficient management capacity, decision-support infrastructure, and experience in obtaining reliable estimates of the AMRP costs and schedule.

OCC objects to the Company's 25-year AMRP proposal, as well as the Staff's modified 8-year AMRP schedule and cost estimates. The Staff accepts the Company's proposed 8-year IRP relating to its proposed 25-year AMRP without change. The Company has not demonstrated in the record that it can obtain the necessary financing, man-power, permit and support resources to complete the AMRP on time and within budget. Furthermore, there is no mechanism in place or proposed to hold the Company accountable for any unreasonable delay or cost overrun over the initial 8-year period, let alone the full 25-year term of COH's AMRP proposal. By way of example supporting OCC's objection, the Duke AMRP program has been extended from 10 to 16 years (as currently projected), and has estimated a nearly $100 million cost over-run after only 4 years.

d. Staff has supported COH's AMRP proposal based upon unsupported Company commitments.

OCC objects to the Staff's failure to refute the Company's assertion that the approval of the Rider IRP will defer the need for more frequent and expensive base rate proceedings. There is no evidence in the record that such a deferral will happen with the approval of Rider IRP. The Company makes no such commitment and Columbia is not prevented from filing a new rate case whenever it deems it necessary to do so. There are many other factors besides the Rider IRP that may affect Columbia's revenue requirement in meeting the approved rate of return. They include the general level of inflation, the cost of debt, labor cost, and new environmental regulation if any, etc. All these are beyond the control of Columbia. So any talk of deferring future rate case filings as a result of the approval of Rider IRP is probably unrealistic and misleading.

e. Staff's proposed annual Rider IRP annual review processes are deficient.

OCC objects to the Staff's recommendation that the annual increase in Rider IRP for residential customers be capped at $1.00 per month including excise taxes regardless of other circumstances, such as the financial need or the financial performance of COH. This cap is unreasonable and unsupported by the evidence in the record. The Staff has not conducted any independent and credible analysis of the impact of such a substantial increase in monthly fixed charge to all residential customers, especially those low-income and low-usage customers. At the end of the AMRP, each and residential customer of Columbia can potentially face an additional monthly charge of about $25 under the proposed Rider IRP cap. In proposing the cap, the Staff simply accepts Columbia's current annual cost estimate, which itself is speculative and unreliable, and fails to address the eventuality of COH over-spend the cap, in which case the Company should not be permitted to recover any deferrals associated with expenditures in excess of the cap.

OCC objects to the Staff's recommendation regarding the general procedures for processing of the annual updates to Rider IRP. The proposed Rider IRP procedure is unreasonable and does not lead to meaningful and factual investigation of Columbia's filing. The Staff and other parties will have at most 31 days to conduct a full investigation (with all information available), raise objections, and issue its recommendation. Furthermore, the annual Rider IRP review is limited in scope to the justness and reasonableness of the level of recovery of expenditures associated with the IRP program. Additional Information such as AMRP construction plans should be provided with sufficient lead time in the annual Rider IRP review process.

G. Customer Service

The Staff completed a customer service audit in May 2008, OCC objects to the Staff's findings "that overall, the Company was in compliance with the rules and regulations set forth by the Public Utilities Commission of Ohio."[10] As recommended by the testimony of OCC Witness Williams the Staff failed to take necessary action by requiring COH to improve its customer service in order to correct issues in which the PUCO and Company have received numerous complaints. The following customer service related areas should be addressed by the Commission:

1. Service Appointments

Staff failed to take necessary action to assure that COH's customer service practices are more customer-focused by improving upon the limited number of service appointments that are available during the evening hours and the impact this may have on residential consumer.

2. Extended Payment Plans

Staff failed to take necessary action to assure that COH's customer service practices are more customer-focused by expanding the limited options of extended payment plans that the Company is offering to residential customers. Staff further failed

[10] Staff Report at 38.

to take necessary action to assure that COH's customer service practices are more customer-focused by expanding the limited options of back bill payment terms offered by the Company in compliance with Ohio law.[11]

3. Adjust Bill Due Dates

Staff failed to consider and recommend billing options that can help customers better manage utility bills including adjusted bill due dates.

4. Timely Payment Posting

Staff failed to explore options for ensuring that payments post to accounts on the same day in which the payments are made and thus may subject residential customers unnecessarily to disconnection for non-payment.

5. Social Security Number Requirements

Staff failed to take necessary action to assure that COH's customer service practices limit the Company request for Social Security Numbers to only those situations in which the customer, after being fully informed, has chosen an option (from all of the available options) for establishing financial responsibility that necessitates COH taking the customer's Social Security Number.

6. Authorized Agents

Staff failed to take necessary action to assure that COH's customer service practices are more customer-focused by assuring that COH's public education efforts reach customers' needs for differentiating authorized agents vs. unauthorized payment centers. Staff further failed to take necessary action to improve COH's current customer service practices that experience delays that occur in the posting of payments made at

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[11] Ohio Adm. Code 4901:1-18-04.

authorized agents. Staff has failed to consider potential problems that can arise from customers use of pay day lenders as an authorized or unauthorized agent for COH.

7. Charges for Paying Gas Bills

Staff failed to consider the impact that extra fees and charges customers incur in order to pay their bills, have on residential customers' ability to pay bills.

8. Installment Payments for Security Deposits

Staff failed to assess the impact that billing a security deposit in a single payment, instead of in installments, has on residential customers' abilities to secure service.

9. Access Issues

Staff failed to consider the appropriateness of or the potential for double recovery associated with the continuation of COH's $35 charge (that some customers are currently paying to have Automated Meter Reading Equipment installed), in light of COH's AMR proposal.

10. Collection Charge

Staff failed to eliminate the Collection Charge from the tariff even though the Company does not accept payments from residential customers at the premise.

11. Financial Responsibility

Staff failed to take necessary action to assure that COH's customer service practices are more customer-focused by assuring that at the time customers apply for service, COH fully informs each customer of all of the available options for establishing financial responsibility and allows customers to demonstrate financial responsibility by the method of the customers' choosing other than by paying a deposit (e.g. being a freeholder of property) as required by Ohio law.[12]

12. Bill Format Issue

Staff failed to recommend that COH include OCC's "Comparing Your Energy Choice" on its monthly billing statements.

III. STATEMENT OF MAJOR ISSUES

R.C. 4903.083 requires that, with regard to the scheduling of local public hearings, the Commission must list in the notice to customers "a brief summary of the then known major issues in contention..." by the parties. For this notice the Commission should include the major issues in a form that is understandable and accurate for customers. To accomplish the General Assembly's objective to notify customers of their opportunity to participate in hearings, the Commission should include the following in the notice, with reference as well to the differing positions of parties:

1. The amount of additional revenue that the Company may be authorized to collect through increasing its rates charged to consumers;
2. The inclusion of certain adjustments to the Company's test year rate base and operating income;
3. The appropriate profit the Company will have an opportunity to earn from the charges for distribution service to consumers, as well as the overall authorized rate of return;

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[12] R.C. 4933.12, See also Ohio Adm. Code 4901:1-17-03.

4. For any revenue increase the Commission grants to COH, the fair and equitable amount of that increase that residential customers should pay;

5. The rate design that COH will be authorized to implement, including that the rate design should recognize the basic rate design criteria of fairness and equity and be appropriately structured such that it sends consumers the proper price signal, encourages conservation, removes any disincentive for the Company to undertake energy efficiency programs, and does not unfairly burden the low-use/low or fixed income customers;

6. The level of the monthly customer charge that consumers may pay to COH;

7. Whether COH should be allowed to collect the capital costs of annual Accelerated Main Replacement Program -related system improvements and pipeline replacements, and if so, whether the program should include appropriate price caps and in periodic rate cases in which all costs and profit of the utility are examined;

8. Whether the Commission in the alternative to the proposed rate design, should instead consider continuing the Company's current rate design with a decoupling mechanism with recommended safeguards; and

9. A number of customer service issues to address complaints from customers.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that a copy of *OCC's Objections to the Staff Report of Investigation and Statement of Major Issues* was served on the persons stated below via first class U.S. Mail, postage prepaid, this 22nd day of September 2008.

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