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BEFORE

THE PUBLIC UTILITIES COMMISSION OF OHIO

IN THE MATTER OF THE APPLICATION OF THE CINCINNATI GAS & ELECTRIC COMPANY FOR AN INCREASE IN GAS RATES IN ITS SERVICE AREA	))))	CASE NO. 01-1228-GA-AIR
IN THE MATTER OF THE APPLICATION OF THE CINCINNATI GAS & ELECTRIC COMPANY FOR APPROVAL OF AN ALTERNATIVE RATE PLAN FOR ITS GAS DISTRIBUTION SERVICE	)))))	CASE NO. 01-1478-GA-ALT
IN THE MATTER OF THE APPLICATION OF THE CINCINNATI GAS & ELECTRIC COMPANY FOR APPROVAL TO CHANGE ACCOUNTING METHODS	))))	CASE NO. 01-1539-GA-AAM

DIRECT TESTIMONY OF

LEE T. HOWE

ON BEHALF OF

THE CINCINNATI GAS & ELECTRIC COMPANY

February 15, 2002

DIRECT TESTIMONY OF LEE T. HOWE

Q. **Please state your name and business address.**

A. My name is Lee T. Howe. My business address is 139 East Fourth Street, Cincinnati, Ohio 45202.

Q. **What is your current position?**

A. I am Manager, Revenue Requirements for Cinergy Services, Inc., which provides various administrative services to The Cincinnati Gas & Electric Company (CG&E or Company) and other affiliated companies.

Q. **Please summarize your educational and professional qualifications?**

A. I graduated from Ball State University with a Bachelor of Science in Accounting Degree in 1985. In addition, I earned a Masters of Business Administration Degree from Indiana University in 1998.

Q. **Please summarize your business experience.**

A. Upon my graduation from Ball State University in 1985, I joined Public Service Company of Indiana, now PSI Energy, Inc. (PSI), an affiliated operating utility of Cinergy Corp., as a staff accountant in the Rate Department. Since then I have held various positions in the General Accounting, Plant Accounting and Budget Departments and the Non-Regulated Power Technology and Infrastructure Services Business Unit of Cinergy Corp. I became Manager, Revenue Requirements in October 2001 and I have responsibility for rate matters involving CG&E, PSI and The Union Light, Heat and Power Company.

Q. **Have you previously submitted testimony in this proceeding?**

A. No.

Q. What is the purpose of your direct testimony?

A. My direct testimony has two purposes. The first purpose is that I hereby adopt Paul G. Smith's testimony and supporting schedules as filed in this proceeding on July 31, 2001 and Paul G. Smith's supplemental direct testimony and supporting schedules as filed in this proceeding on October 5, 2001. I also adopt all of Paul G. Smith's responses to the data requests submitted in this proceeding. The second purpose is to support certain of the Company's objections filed February 15, 2002 to the January 18, 2002 Staff Report of Investigation (Staff Report) issued in this proceeding.

Q. Which specific Company objections do you sponsor?

A. The specific objections that I sponsor deal with the amount of the Company's revenue requirement, working capital, certain rate base items, adjustments to revenue and expenses, and certain Staff Report recommendations.

Q. What is the Company's objection to the Staff Report's determination of the amount of the Company's revenue requirement (item 1 in CG&E's Objections)?

A. The Company objects on the grounds that Staff's determination of the Company's revenue requirement significantly understates the amount of the revenue increase to which the Company is entitled, based on the Company's filings in this proceeding. The Staff's understatement of the Company's revenue requirement increase arises from Staff's treatment of various items to which the Company has made objections and which I address later in my testimony.

Q. What is the Company's objection to the Staff Report's determination of working capital (item 2 in CG&E's Objections)?

A. The Company's objection to the Staff Report's computation of working capital is with the determination of the payroll expense lead days and with the Staff Report's exclusion of the Customer Deposits balance from working capital.

Q. Describe the Company's objection to the Staff Report regarding the payroll expense lead days.

A. The Staff Report, on Schedule B-5, includes a calculation of the lead days associated with payroll expense at 45.64 days. Included in the calculation is an assumption for vacation pay of a one-year lead. The vacation pay should have a one-half year lead as the employee becomes entitled to vacation pay for the following year by being employed with the Company on December 31 of the current year. The vacation is then taken by the employee and paid by the Company over the next 12 months. The Company assumes that the vacation is taken ratably throughout the year, thereby supporting the one-half year lead.

Q. Describe the Company's objection to the Staff Report regarding the exclusion of the Customer Deposit balance from working capital.

A. The Staff Report excluded the liability for Customer Deposits in its calculation of working capital and included it as a reduction to Rate Base on Schedule B-6. Customer Deposits represent payments made by customers as security for potential non-payment, based on certain criteria established by the Company. The Company later returns the deposit, plus interest, based on certain criteria established by the Company, one of which is that the customer has demonstrated consistent payment of their utility bills. The collection and returning of Customer Deposits occurs on a regular basis as part of normal operations. Additionally, one of the reasons for requiring Customer Deposits is that it provides the Company with protection in its working capital if the customer does not pay. Therefore, the Company believes that Customer Deposits is properly reflected as working capital and not as a rate base adjustment.

Q. Describe the Company's objection to the Staff Report regarding Deferred Taxes (item 3 in CG&E's Objections).

A. The Staff Report, on Schedule B-6, excluded the following Deferred Taxes in its calculation of rate base.

Account Number	Description	Amount
190310	Miscellaneous Deferred Items	\$2,109,022
282490	Section 174	(\$1,468,858)
282940	Property Tax	\$1,119,298
283050	Miscellaneous Items	\$3,053,350
Total		\$4,812,812

These Deferred Tax balances represent assets or liabilities generated by timing differences between book and taxable income. The tax expenditure or deferral of a tax expenditure is made on behalf of customers, represents a cash expenditure or deferral of a cash expenditure, and, accordingly, is properly included in the calculation of rate base.

Q. Are there any other Company objections to the Staff Report regarding Deferred Taxes?

A. Yes. This objection is set forth at item 4 of CG&E's Objections. The Staff Report calculated a Deferred Tax liability balance for uncollectible accounts PIPP/Pre PIPP of ($358,504) as of the date certain by arbitrarily taking 25% of the deferred tax benefit generated in the test year as shown on Schedule C-4. This calculation fails to consider the book/tax timing differences prior to the test year that generated either a deferred tax liability or deferred tax asset. The Company reflected all timing differences up to the date certain for this item and properly reflected $833,378 as a Deferred Tax asset, the balance on the Company's books as of March 31, 2001, and reflected such balance on the Company's Schedule B-6, in its calculation of the rate base adjustment. The Staff Report should have reflected the same amount.

Q. Do you agree with the Staff's calculation of test year annualized labor expense (item 6 in CG&E's Objections)?

A. No. The Staff calculated the Company's annual labor expense based on the average employees, hourly rate and resulting cost for the months of June, July and August. The Company believes that the method used in its filing based on the 3 months actual and 9-month budget is consistent with the determination of other operation and maintenance expenses in this case. This better reflects the representative employment level during the test year and the resultant test year level of expenses, and therefore is a better indicator of the annual amounts to be incurred during the period when rates will be in effect.

Q. Do you agree with the Staff's calculation of test year pension and benefits expense (item 7 in CG&E's Objections)?

A. No. As a result of test year labor expense being understated, as discussed above, the Company believes that pension and benefits expense have been understated.

Q. Describe the Company's objections to the Staff Report regarding the Limited Early Retirement Program (item 8 in CG&E's Objections).

A. The Staff Report's disallowance of the amortization of costs associated with the Company's Limited Early Retirement Program (LERP) failed to recognize that the customer is receiving the benefit of the LERP through lower labor expense in the test year. As provided in response to data request OCC-2-10, the Company reduced its employee count by 116 employees resulting in an estimated annual savings of approximately $2.5 million. The annual labor expense reduction is reflected in the test year and provides a benefit to customers. The Company's annualized LERP costs based on a three-year amortization period is $708,484, which is significantly less than the savings reflected in the test year. Additionally, the Commission has allowed recovery of the costs of similar programs in the past.

Q. Describe the Company's objections to the Staff Report regarding the Uncollectible Accounts Expense (item 9 in CG&E's Objections).

A. The Staff Report calculated the uncollectible accounts expense ratio at 1.2497% on Schedule C-3.10 by taking the total provision for uncollectible accounts expense of $6,020,895 and dividing it by the total revenue of $481,792,264. The Staff Report should have excluded from the total revenue those items for which uncollectible accounts expense is neither generated nor recovered. The items to be excluded, as shown on the Company's Schedule C-2.1, are Interdepartmental Sales, Late Payment Charges, Reconnection Charges, Customer Diversion, Bad

Check Charges, Transportation Switching Fee, Other Produced Gas for Associated Companies, Agency Service-Woodsdale, Gas Suppliers-Metered Pool, Rents, Sales and Use Tax Collection Fee and Gas-Losses Damaged Lines. With all of these items excluded, the proper total revenue to use in the calculation of the uncollectible accounts expense ratio would be $472,754,604, resulting in a corrected ratio of 1.274%, which the Company used in determining the uncollectible accounts expense.

Q. Describe the Company's objection to the Staff Report regarding the Riser Inspection Program expense (item 10 in CG&E's Objections).

A. The Staff Report, on Schedule C-3.13, excluded $237,270 from the Company's Riser Inspection Program Expense when determining the overall cost of the program. The $237,270 represents the total cost over the term of the program for a full time field supervisor dedicated to this program. This person was hired specifically for this program and is properly included as part of the incremental costs to the Company. This staff position was not included in test year labor expenses. The employee began work in May 2001 on this program and will continue until the program is complete, which is to be no longer than three years per the Stipulation and Recommendation approved by the Commission in Case No. 00-681-GA-GPS.

Q. Does the Company have any other objections to the Staff Report regarding the Riser Inspection Program Expense?

A. Yes. The Staff Report improperly changed the Company's amortization period from three years to five years, even though the Stipulation and Recommendation approved by this Commission in Case No. 00-681-GA-GPS requires the Company to complete the program in a three-year period. Additionally, a three-year amortization period is consistent with the Staff Report's recommendation regarding recovery of the accelerated main replacement program expenses through Rider AMRP.

Q. **Describe the Company's objection to the Staff Report regarding amortization of Rate Case Expenses (item 11 in CG&E's Objections).**

A. The Staff Report changed the three-year amortization period proposed by the Company to five years, even though a three-year amortization period is consistent with Staff's recommendation regarding recovery of the accelerated main replacement program expenses through Rider AMRP. Additionally, a three-year amortization period is consistent with past decisions by this Commission.

Q. **With regard to the Cost of Long-Term Debt, do you agree with the Staff's calculation of the interest cost for the loss/gain on reacquired debt (item 16(a) in CG&E's objections)?**

A. No. The Staff Report improperly calculated the interest costs for the loss on reacquired debt and the gain on reacquired debt at a summary level. On pages 25-28 of the Staff Report, Table 3, entitled "Cost of Long Term Debt," the Staff calculated the interest cost for the loss on reacquired debt and the gain on reacquired debt by taking the total balance by Company and annualizing the amortization based on the long-term debt issue with the highest number of years to maturity. For example, on page 25 of the Staff Report, the annual interest cost reported for the loss on reacquired debt for The Cincinnati Gas & Electric

Company is $350,345, which was derived by taking the unamortized balance of $7,970,342 and dividing by 22.75 years, which is the longest term to maturity for a single bond issue for The Cincinnati Gas & Electric Company. In fact, the unamortized balance of all of the Company's gains and losses on reacquired debt represents several issues with various maturity dates. The Company's Schedule D-3 represents the summation of the calculation of these individual items. This calculation is supported by the attached Schedule LTH-1, which I prepared and which I sponsor.

Q. Does the Company have any other objections to the Staff Report regarding Cost of Long-Term Debt?

A. Yes. This objection is set forth at item 16(b) in CG&E's Objections.

Q. Please describe.

A. Notwithstanding the previous objection to the Staff Report's calculation of the cost on long-term debt, the Staff Report included in its interest cost a credit amount that should have been reflected as a debit amount. On page 26 of the Staff Report, the interest cost calculated for the Loss on Reacquisition of Debt for The Union Light, Heat and Power Company should have been a debit rather than a credit of $125,623, thereby reducing interest cost in error by $251,266.

Q. Do you have any other objections to the Staff Report regarding Cost on Long-Term Debt?

A. Yes. This objection is set forth at item 17 in CG&E's Objections.

Q. Please describe.

A. In the Staff Report's calculation of the interest cost, the Staff failed to consider the impact resulting from multiple interest payments occurring throughout the year on the Company's debt, and thereby improperly reduced the interest cost by $3,332.262.

Q. Do you agree with the Staff's calculation of the Gross Revenue Conversion Factor (item 18 in CG&E's Objections)?

A. No. Staff failed to include the PUCO and OCC maintenance taxes as revenue items in the calculation of the gross revenue conversion factor. Since these taxes are assessed based on revenues collected, they should be reflected in the calculation of the revenue conversion factor in order for the Company to properly recover the full amount of these maintenance taxes.

Q. Does the Company have any other objections to the Staff Report regarding the Gross Revenue Conversion Factor?

A. Yes. This objection is set forth as item 18(b) in CG&E's Objections.

Q. Please describe.

A. The Staff's calculation of the gross revenue conversion factor incorrectly reduced the uncollectible expense ratio by using all revenues in its calculation instead of using only the appropriate retail and transportation revenues. The provision for uncollectible accounts expense as booked by the Company is not calculated on Inter-Department sales or Other Miscellaneous revenue. The Staff's calculation does not allow the Company complete recovery of its uncollectible accounts expense.

Q. Describe the Company's objection to the Staff Report regarding the deferral and recovery through Rider AMRP of depreciation and property taxes (item 26 in CG&E's Objections).

A. The Staff Report recommended against the Company's deferral and subsequent recovery of depreciation and property taxes associated with the new mains. These expenses will increase as the accelerated main replacement program progresses and significant regulatory lag will occur absent deferral of these expenses. This regulatory lag will prevent the Company from earning the rate of return to be authorized by the Commission in this case. Additionally, the deferral and recovery of these items through Rider AMRP is consistent with Staff's recommendation in this proceeding for Post in Service Carrying Costs on the same plant.

Q. Does this conclude your direct testimony?

A. Yes.

The Cincinnati Gas & Electric Company
Case No. 01-1228-GA-AIR, Case No. 01-1478-GA-ALT, Case No. 01-1539-GA-AAM
Amortization of Gain/Loss on Reacquired Debt

THE CINCINNATI GAS & ELECTRIC COMPANY

Series	Loss on Reacq. Debt Bal. 03/31/01	End Date	# of Months Remaining	Monthly Amortization	Annual Interest	Staff Amount	Difference
9.85%	2,606,671	10/15/07	78.50	33,206	398,472		
9.15%	1,323,084	01/01/06	57.00	23,212	278,544		
9.625%	507,078	07/01/09	99.00	5,122	61,464		
8.625%	154,996	09/17/01	5.50	28,181	154,996		
10.125%	1,009,560	11/23/19	223.75	4,512	54,144		
7.375%	16,520	11/01/01	7.00	2,360	16,520		
10.125%	920,656	12/01/15	176.00	5,231	62,772		
8.125%	44,244	08/01/03	28.00	1,580	18,960		
10.20%	540,440	12/01/20	236.00	2,290	27,480		
8.95%	437,857	12/15/21	248.50	1,762	21,144		
8.50%	305,830	09/01/22	257.00	1,190	14,280		
7.20%	103,410	10/01/23	270.00	383	4,596		
Total Loss on Reacquired Debt	7,970,346			109,029	1,113,372	350,345	763,027
7.20%	(933,390)	10/01/23	270.00	(3,457)	(41,484)		
Total Gain on Reacquired Debt	(933,390)			(3,457)	(41,484)	(41,028)	(456)

THE UNION LIGHT, HEAT & POWER COMPANY

Series	Loss on Reacq. Debt Bal. 03/31/01	End Date	# of Months Remaining	Monthly Amortization	Annual Interest	Staff Amount	Difference
10.25%	752,790	06/01/20	230.00	3,273	39,276		
10.25%	735,231	11/15/20	235.50	3,122	37,464		
9.70%	1,222,677	07/01/19	219.00	5,583	66,996		
9.50%	288,972	12/01/08	92.00	3,141	37,692		
8.00%	51,750	10/01/03	30.00	1,725	20,700		
Total Loss on Reacquired Debt	3,051,420			16,844	202,128	(125,623)	327,751

The Cincinnati Gas & Electric Company
Case No. 01-1228-GA-AIR, Case No. 01-1478-GA-ALT, Case No. 01-1539-GA-AAM
Amortization of Gain/Loss on Reacquired Debt

PSI ENERGY, INC.

Series	Loss on Reacq. Debt Bal. 03/31/01	End Date	# of Months Remaining	Monthly Amortization	Annual Interest	Staff Amount	Difference
S	49,356	01/01/02	9.00	5,484	49,356		
T (*)	244,018	02/01/04	34.00	7,177	86,124		
W	874,172	08/01/05	52.00	16,811	201,732		
Y	409,170	01/01/07	69.00	5,930	71,160		
Z (*)	1,325,142	10/01/07	78.00	16,989	203,868		
AA	1,651,680	10/01/08	90.00	18,352	220,224		
BB 6.58	17,395	03/01/04	35.00	497	5,964		
FF	6,237,362	02/01/11	118.00	52,859	634,308		
HH	4,224,384	12/01/11	128.00	33,003	396,036		
JJ	6,344,800	12/01/12	140.00	45,320	543,840		
PCN 5 3/4	40,138	12/15/03	32.50	1,235	14,820		
NN	653,424	03/15/12	131.50	4,969	59,628		
QQ	959,310	06/15/13	146.50	6,548	78,576		
CCC	1,525,443	01/15/22	249.50	6,114	73,368		
AAA	385,792	02/01/24	274.00	1,408	16,896		
ITN-A, 8.75%	357,069	05/19/22	253.60	1,408	16,896		
ITN-A, 8.67%	1,168,146	06/01/22	254.00	4,599	55,188		
TT	345,845	03/15/12	131.50	2,630	31,560		
UU	651,073	03/15/15	167.50	3,887	46,644		
YY	1,680,788	02/15/23	262.50	6,403	76,836		
6.35% Deb	1,601,708	11/15/06	67.50	23,729	284,748		
Put/Call Note		12/14/16					
Total Loss on Reacquired Debt	30,746,213			$ 265,352	$ 3,167,772	978,659	2,189,113
PCN 5/34	(25,318)	12/15/03	32.50	(779)	(9,348)		
PATS 6.25	(211,932)	12/15/05	56.50	(3,751)	(45,012)		
AAA	(946,944)	02/01/24	274.00	(3,456)	(41,472)		
Total Gain on Reacquired Debt	(1,184,193)			($7,986)	($95,832)	(37,693)	(58,139)
Total					4,345,956	1,124,660	3,221,296

Ties to Company Schedule D-3

The Cincinnati Gas & Electric Company
Case No. 01-1228-GA-AIR, Case No. 01-1478-GA-ALT, Case No. 01-1539-GA-AAM
Amortization of Gain/Loss on Reacquired Debt

	Carrying Value	Interest Cost	Rate
Long Term Debt per Staff Report	3,133,699,402	218,495,033	6.97%
Adjustment		3,221,296	
Revised Total	3,133,699,402	221,716,329	7.08%
Calculation of Revenue Requirement Impact:			
	LTD % of Total Capitalization	Cost Rate	
Adjusted Weighted Cost %	51.96%	7.08%	3.68%
Weighted Cost % per Staff Report			3.62%
Impact of Adjustment on Rate of Return			0.06%
Impact of Adjustment on Rate of Return including tax effect			0.039%
Rate Base per Staff Report			413,966,638
Incremental Adjustment to Income Deficiency			161,447
Gross Revenue Conversion Factor			1.638030
Incremental Adjustment to Revenue Requirement			264,455