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DUKE ENERGY OHIO EXHIBIT____

BEFORE

THE PUBLIC UTILITIES COMMISSION OF OHIO

In the Matter of the Application of Duke Energy Ohio, Inc., for an Increase in Gas Rates.	)))	Case No. 12-1685-GA-AIR
In the Matter of the Application of Duke Energy Ohio, Inc., for Tariff Approval.	)))	Case No. 12-1686-GA-ATA
In the Matter of the Application of Duke Energy Ohio, Inc., for Approval of an Alternative Rate Plan for Gas Distribution Service.	))))	Case No. 12-1687-GA-ALT
In the Matter of the Application of Duke Energy Ohio, Inc., for Approval to Change Accounting Methods.	)))	Case No. 12-1688-GA-AAM

DIRECT TESTIMONY OF

WILLIAM DON WATHEN JR.

ON BEHALF OF

DUKE ENERGY OHIO, INC.

____ Management policies, practices, and organization

____ Operating Income

____ Rate Base

____ Allocations

____ Rate of Return

__X__ Tariffs

__X__ Alternative Regulation Plan

__X__ Other: Rate Case Drivers

July 20, 2012

TABLE OF CONTENTS

I. INTRODUCTION AND PURPOSE

Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

A. My name is William Don Wathen Jr., and my business address is 139 East Fourth Street, Cincinnati, Ohio 45202.

Q. BY WHOM ARE YOU EMPLOYED AND IN WHAT CAPACITY?

A. I am employed by Duke Energy Business Services LLC (DEBS) as Director of Rates and Regulatory Strategy for Ohio and Kentucky. DEBS provides various administrative and other services to Duke Energy Ohio, Inc., (Duke Energy Ohio or Company) and other affiliated companies of Duke Energy Corporation (Duke Energy).

Q. PLEASE BRIEFLY SUMMARIZE YOUR EDUCATIONAL BACKGROUND AND PROFESSIONAL EXPERIENCE.

A. I received Bachelor Degrees in Business and Chemical Engineering, and a Master of Business Administration Degree, all from the University of Kentucky. After completing graduate studies, I was employed by Kentucky Utilities Company as a planning analyst. In 1989, I began employment with the Indiana Utility Regulatory Commission as a senior engineer. From 1992 until mid-1998, I was employed by SVBK Consulting Group, where I held several positions as a consultant focusing principally on utility rate matters. I was hired by Cinergy Services, Inc., in 1998 as an Economic and Financial Specialist in the Budgets and Forecasts Department. In 1999, I was promoted to the position of Manager, Financial Forecasts. In August 2003, I was named to the position of Director - Rates. On December 1, 2009, I took the position of General Manager and Vice President of Rates, Ohio and Kentucky.

On July 3, 2012, as a result of the merger, my job title changed to my current title of Director of Rates and Regulatory Strategy for Ohio and Kentucky.

Q. PLEASE SUMMARIZE YOUR RESPONSIBILITIES AS DIRECTOR OF RATES AND REGULATORY STRATEGY FOR OHIO AND KENTUCKY.

A. As Director of Rates and Regulatory Strategy for Ohio and Kentucky, I am responsible for all state and federal rate matters involving Duke Energy Ohio and Duke Energy Kentucky.

Q. HAVE YOU PREVIOUSLY TESTIFIED BEFORE THE PUBLIC UTILITIES COMMISSION OF OHIO?

A. Yes. I previously testified in a number of cases before the Public Utilities Commission of Ohio (Commission) and other regulatory commissions.

Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY IN THESE PROCEEDINGS?

A. On behalf of Duke Energy Ohio, I am submitting this testimony to support the reasonableness of the Company's request to increase its base natural gas distribution revenues; its requests for certain tariff modifications; and its requests for certain accounting authority related to the overall request, including the continued deferral of its Manufactured Gas Plant (MGP) remediation expense. I discuss the background of Duke Energy Ohio's requested rate increase and the drivers for Duke Energy Ohio's current revenue deficiency. I also support the Company's request to re-approve the Company's Rider AMRP (Accelerated Main Replacement Program) and its Rider AU (Advanced Utility), as well as a request to implement a new rider related to a program to accelerate the replacement of service lines, Rider ASRP (Accelerated Service Replacement Program). Finally, I sponsor certain elements of the Company's Alternative Regulation Plan.

II. BACKGROUND AND DRIVERS FOR REQUESTED RATE INCREASE

Q. WHEN DID THE COMMISSION APPROVE DUKE ENERGY OHIO'S CURRENT GAS RATES?

A. Duke Energy Ohio's current gas rates were approved by this Commission pursuant to an Order dated May 28, 2008, in Case No. 07-589-GA-AIR, *et al.* The test period in that proceeding was the twelve months ended December 31, 2007, and the date certain was March 31, 2007. The rates went into effect on or about June 4, 2008.

Q. WHY DOES DUKE ENERGY OHIO BELIEVE A GAS RATE INCREASE IS NECESSARY AT THIS TIME?

A. Since March 31, 2007, the date certain in the prior case, Duke Energy Ohio has invested approximately $500 million in capital additions and improvements to provide safe and reliable gas service. Duke Energy Ohio's current rates are not sufficient to recover the costs associated with the investments made. In addition, distribution-related operation and maintenance (O&M) expenses have increased. The increased investment and operating costs prevent Duke Energy Ohio from earning a reasonable return on its gas business, absent an increase in its current rates.

Duke Energy Ohio gas operations are projected to earn a 4.90 percent return on rate base during the twelve month test period ended December 31, 2012. This return is below the 8.45 percent return on rate base authorized by this

Commission in Case No. 07-589-GA-AIR, *et al.*, and is below the 8.13 percent return on rate base proposed in these proceedings. In order to earn a fair return, Duke Energy Ohio's retail rates must be increased by $44.6 million, to satisfy a total revenue requirement of approximately $291 million, exclusive of all riders.

Q. WHAT ARE THE PRIMARY DRIVERS FOR THIS EARNINGS ATTRITION?

A. The primary drivers of the proposed $44.6 million rate increase include:

- $6.5 million is attributable to incremental plant investment;
- $11.8 million is attributable to increased operating costs;
- $21.8 million is attributable to amortization of Manufactured Gas Plant site remediation.
- $5.9 million is attributable to declining natural gas sales volumes;
- $1.7 million is attributable to higher real estate taxes and other non-income taxes;
- $7.6 million is attributable to increased depreciation expense; and
- $2.7 million is attributable other amortization expenses.

Factors offsetting these rate increase drivers include:

- $3.0 million is attributable to decreased financing costs and return on equity; and
- $10.4 million is attributable to increases in accumulated deferred income taxes and other rate base items.

Q. WHAT RATE RELIEF IS DUKE ENERGY OHIO REQUESTING IN THESE PROCEEDINGS?

A. In its July 9, 2012, application, Duke Energy Ohio specifically requested that the Commission issue an Order:

- To increase base rates by $44.6 million;
- To re-approve the Company's Rider AMRP and its Rider AU.
- To establish new riders:
  - Rider ASRP
  - Rider FRT (Facilities Relocation – Mass Transportation)
  - Rider NGV (Natural Gas Vehicle Fuel)
  - Rider GGIT (Gas Generation Interruptible Transportation Rider)
  - Rider ED (Economic Development)
- To modify the language of the Company's Tariff for Reconnection Charges; and
- To continue the existing MGP deferral for ongoing remediation expense incurred beyond the test year.

III. DUKE ENERGY OHIO'S PROCESS AND METHODOLOGY FOR PREPARATION OF ITS RATE CASE

Q. WHAT IS THE OVERALL GOAL OF THE RATEMAKING PROCESS?

A. The overall goal of the ratemaking process is to give the regulated utility the opportunity to recover all of its prudently incurred operating expenses and to earn a fair return on its capital invested in the business. The Ohio Revised Code succinctly recognizes traditional ratemaking. In particular, R.C. 4905.22 states that all charges for service shall be just and reasonable and not more than allowed by law or by order of the Commission. That is precisely the objective of the normal ratemaking process and such a goal is to be achieved by charging rates that fairly assign the cost of service to the various customer classes.

Q. HOW DOES DUKE ENERGY OHIO PREPARE A GAS DISTRIBUTION RATE CASE?

A. The lengthy and often complicated gas rate case preparation process essentially consists of three primary steps: (1) determine the annual gas revenue requirement; (2) develop a cost of service study that assigns and allocates the gas revenue requirement to each retail rate schedule based on the applicable cost to serve; and (3) design the retail rates and rate schedules to yield the necessary retail revenue requirement.

Q. PLEASE GIVE AN OVERVIEW OF THE REVENUE REQUIREMENT DETERMINATION PROCESS EMPLOYED BY DUKE ENERGY OHIO.

A. Duke Energy Ohio's revenue requirement process focuses on determining: (1) the current level of capital invested in the gas business; (2) the appropriate capital structure and cost of capital to finance the investment; and (3) the ongoing level of annual expenses related to operating and maintaining the gas business. Duke Energy Ohio witness Peggy A. Laub supports the determination of Duke Energy Ohio's jurisdictional revenue requirement.

Q. PLEASE GIVE AN OVERVIEW OF THE RETAIL COST OF SERVICE STUDY PROCESS EMPLOYED BY DUKE ENERGY OHIO.

A. The gas distribution cost of service study assigns each component of revenue requirement formula to the various retail rate schedules. The components are directly assigned, or allocated, based on operational and/or accounting data with the objective being to allocate costs to customers in a manner that reflects the costs the Company incurs to serve them. Duke Energy Ohio witness James E. Ziolkowski discusses the Company's gas distribution cost of service study.

Q. WHAT ARE THE OBJECTIVES OF THE RATE DESIGN PROCESS?

A. The primary objectives of the rate design process are to develop rates that: (1) provide the utility with the opportunity to recover its annual revenue requirement; and (2) distribute the revenue recovery among customers within each retail rate schedule in a manner that is consistent with the cost of providing gas service. Duke Energy Ohio witness James A. Riddle supports Duke Energy Ohio's proposed rate design.

Q. MR. STEPHEN DE MAY SPONSORS DUKE ENERGY OHIO'S CONSOLIDATED CAPITAL STRUCTURE AS OF MARCH 31, 2012. WHY DO YOU RECOMMEND USING DUKE ENERGY OHIO'S CAPITAL STRUCTURE FOR ESTABLISHING RATES IN THESE PROCEEDINGS?

A. In addition to the long-standing precedent in Ohio for using the operating company's capital structure rather than the capital structure of the parent, I believe the Duke Energy Ohio consolidated capital structure is the appropriate capital structure to use as the basis for setting Duke Energy Ohio's gas distribution rates. The use of an alternative capitalization, such as Duke Energy's capital structure, would cause the rates in these proceedings to be impacted by a number of factors unrelated to Duke Energy Ohio's gas distribution operations. For instance, Duke Energy's capitalization reflects the practices and events of its regulated operations in Indiana, North Carolina, and South Carolina; its non-regulated domestic and international operations; and the spin-off of the gas pipeline businesses. It would be inappropriate to allow the capitalization practices and events in these affiliate activities to impact Duke Energy Ohio's gas distribution rates.

Q. IS THE COMPANY MAKING ANY ADJUSTMENTS TO ITS CONSOLIDATED CAPITAL STRUCTURE FOR RATE SETTING PURPOSES?

A. Yes. As described in the testimony of Company witness Daniel J. Reilly, Duke Energy Ohio's consolidated capital structure has been adjusted to eliminate the impact of: (1) purchase accounting recorded pursuant to the Duke Energy/Cinergy Corp (Cinergy)[1] merger; and (2) equity associated with Duke Energy North America generating assets acquired by Duke Energy Ohio in the 2006 Duke Energy/Cinergy merger (*i.e.*, the DENA assets). Although the DENA assets were transferred from being directly owned by Duke Energy Ohio to a subsidiary, there was no immediate impact on Duke Energy Ohio's consolidated balance sheet as these assets are still under the Duke Energy Ohio corporate structure and, therefore, should be removed.

Q. ARE THE ADJUSTMENTS TO THE CAPITAL STRUCTURE BEING PROPOSED HERE NEW?

A. No. Duke Energy Ohio has filed two retail rate cases since the Duke

[1] *In the Matter of the Joint Application of Cinergy Corp., on Behalf of the Cincinnati Gas & Electric Company, and Duke Energy Holding Corp. for Consent and Approval of a Change of Control of The Cincinnati Gas & Electric Company,* Case No. 05-732-EL-MER, *et al.,* Finding and Order (December 21, 2005).

Energy/Cinergy merger was consummated; one for electric distribution (Case No. 08-709-EL-AIR, *et al.*) and one for gas distribution (Case No. 07-589-GA-AIR, *et al.*). The capital structure adjustments being proposed in the current case are the same as adjustments made, and accepted by the Commission, in these two prior cases. It is worth noting that the impact of all these adjustments is to reduce the Company's equity ratio and, consequently, reduce the Company's jurisdictional revenue requirement.

Q. DESCRIBE THE IMPLICATIONS OF THE COMPANY'S APPPLICATION TO TRANSFER ITS LEGACY GENERATION ASSETS TO AN AFFILIATE AS IT RELATES TO THIS RATE APPLICATION.

A. As part of the Commission-approved stipulation in the Company's most recent standard service offer application, Case No. 11-3549-EL-SSO, *et al.*, Duke Energy Ohio agreed to transfer its direct ownership interest in all of its Legacy Generation[2] to an affiliate or subsidiary by December 31, 2014.[3] As discussed by Company witness De May, the asset transfer will result in some recapitalization; however, as of the date of this filing, there is insufficient information upon which to base any adjustments to the Company's March 31, 2012, date certain capital structure to be used in this case. Consequently, the impending asset transfer has no impact on the rates being proposed in this rate application.

Q. AFTER ADJUSTING THE ACTUAL CAPITAL STRUCTURE TO ELIMINATE THE IMPACT OF PURCHASE ACCOUNTING, THE

[2] *In the Matter of the Application of Duke Energy Ohio, Inc., for Authority to Establish a Standard Service Offer Pursuant to Section 4928.143, Revised Code, in the Form of an Electric Security Plan, Accounting Modifications, and Tariffs for Generation Service*, Case No. 11-3549-EL-SSO, *et al.*, Attachment CRW-1 to the Supplemental Testimony of Charles R. Whitlock (October 28, 2011).
[3] Id, at Stipulation and Recommendation (October 24, 2011).

IMPACT OF THE GOODWILL AND OTHER ASSET IMPAIRMENTS AND TO ELIMINATE THE EQUITY ASSOCIATED WITH THE DENA ASSETS, WHAT IS THE CAPITALIZATION OF DUKE ENERGY OHIO FOR PURPOSES OF THESE PROCEEDINGS?

A. Duke Energy Ohio's consolidated capital structure at March 31, 2012, as adjusted, is approximately 46.70 percent debt and 53.30 percent common equity. This is shown on Schedule D-1.

It should be noted that the capital structure underlying the Company's requested revenue requirement is well above the limits established by the Federal Energy Regulatory Commission (FERC) and this Commission. The FERC and this Commission imposed a minimum limit on the equity ratio of 30 percent. The limit reflects the FERC orders that approved the Duke Energy/Cinergy merger[4] and the Commission orders that approved an accounting modification to address the impact of required accounting treatment for the purchase accounting associated with the Duke Energy/Cinergy merger from 2006.[5]

IV. <u>NEW TARIFF PROPOSALS</u>

Q. PLEASE DESCRIBE THE SIGNIFICANT NEW RATES AND TARIFFS THE COMPANY IS PROPOSING IN THESE PROCEEDINGS.

A. The Company is proposing several new tariffs in this application. Duke Energy Ohio is also proposing to make a modification to its Reconnection Tariff, Sheet 82, to address voluntary disconnection/reconnections.

[4] *Cincinnati Gas and Electric Company d/b/a Duke Energy Ohio and Union Light, Heat and Power Company, d/b/a Duke Energy Kentucky*, FERC Order, EL06-66-000.
[5] *In the Matter of Duke Energy Ohio's Application for Change in Accounting Methods*, Case No. 09-620-GE-AAM and Case No. 11-5985-GE-AAM.

A. Rider ASRP

Q. PLEASE DESCRIBE THE RIDER ASRP PROPOSAL.

A. As part of its Alternative Regulation Plan in these proceedings, Duke Energy Ohio is proposing to accelerate the replacement of its service lines. As described more fully in the testimony of Company witness Gary J. Hebbeler, the program is designed to further improve the integrity, safety, and reliability of the natural gas delivery system. Company witness Laub sponsors the schedules supporting the proposal.

B. Rider FRT

Q. PLEASE DESCRIBE THE RIDER FRT PROPOSAL.

A. As part of its application in these proceedings, the Company is proposing to create a new tariff for relocating its facilities. Duke Energy Ohio witness James E. Mehring discusses the operational issues involved with regard to facility relocation, but generally, the tariff seeks to ensure that the principles of cost causation are aligned with cost recovery. Traditional ratemaking necessarily involves a level of socialization for certain costs incurred by a utility. Utilities frequently have to relocate electric and gas facilities for private and public construction programs and, often, the cost is simply incorporated into base rates and recovered over all distribution rates. Other times, the cost to relocate is paid for directly by the party requesting the relocation and the utility's other customers have no burden for that cost.

The new tariff being proposed in these proceedings, Facilities Relocation – Mass Transportation Rider (Rider FRT), focuses on recovery of the costs of relocations due to certain projects required by governmental subdivisions. In particular, Rider FRT will be a means for the Company to recover the cost of relocations associated with mass transportation projects initiated by governmental subdivisions. The rider is designed to give the governmental subdivision the option of paying the Company directly for the cost of relocation or, alternatively, to charge only those customers residing within its governmental boundaries for the cost of the project. For example, the city of Cincinnati (City) is requesting that Duke Energy Ohio relocate facilities, at considerable expense, to accommodate its proposed streetcar project. Under Rider FRT, the City will have the option either to pay Duke Energy Ohio directly for the cost, in lump sum or over time, (Option 1) or to allow the Company to collect, via a charge to customers located within the City, the cost of relocation over a period of time (Option 2). The charge under either option would be sufficient to pay for the cost of relocating the facilities, plus a carrying charge at the weighted-average cost of capital established in these proceedings.

Q. IS THE COMPANY PROPOSING RATES FOR RIDER FRT AT THIS TIME?

A. No. The tariff has not yet been approved by the Commission. Consequently, no governmental entity has had the opportunity to utilize this tariff. Upon approval of this tariff, should an eligible governmental entity seek Option 2, Duke Energy Ohio will submit its calculations to the Commission for its review and approval before implementing the charges. The Company will accrue carrying costs on any unrecovered balance of the eligible relocation cost until recovery is completed.

C. Rider NGV

Q. PLEASE DESCRIBE THE RIDER NGV PROPOSAL.

A. As explained in detail by Company witness Mehring, Duke Energy Ohio is proposing to establish a new tariff to encourage the development of natural gas as a fuel alternative. The rider is intended to establish the terms and conditions, including the rates to be charged, under which the Company will provide service to customers who are looking to invest in natural gas vehicles or natural gas vehicle fueling stations.

D. Rider GGIT

Q. PLEASE DESCRIBE THE RIDER GGIT PROPOSAL.

A. Mr. Mehring also describes a Company proposal to establish a new rider meant to encourage the development of distributed generation. Rider GGIT will provide eligible customers an estimated 10 percent average discount over the Company's Interruptible Transportation (IT) tariff. The rider will be available to customers for delivery of natural gas to commercial, gas-fired electric generator, including, but not limited to, customer-owned generation.

E. Rider ED

Q. PLEASE DESCRIBE THE RIDER ED PROPOSAL.

A. Company witness Julia S. Janson describes the purpose of Rider ED in her testimony. The rider will recover the cost to fund the economic development activity contemplated. It will recover no less or more than what is actually spent and is subject to true-up on an annual basis.

F. <u>Reconnection Fees, Sheet 82</u>

Q. PLEASE DESCRIBE THE CHANGES THE COMPANY IS PROPOSING TO ITS RECONNECTION TARIFF, SHEET 82.

A. Duke Energy Ohio's last natural gas rate case, Case No. 07-589-GA-AIR, *et al.*, was resolved by way of a Stipulation and Recommendation (Stipulation) that was approved by the Commission. The Stipulation included a significant movement for residential base rates from commodity-based to a fixed bill. In the current case, the Company is proposing to continue with this modified straight-fixed variable rate, with a fixed charge for residential customers (excluding low-income customers) of $33.03 per bill.

Under the Company's Sheet 82, Charge for Reconnection of Service, the existing reconnection charge for customers who voluntary disconnect their service is only $17. Thus, customers who disconnect their service only to reconnect it a short time thereafter pay the modest reconnection fee in lieu of the monthly customer charge approved by the Commission. Since the implementation of the new rates from the prior rate case, a number of customers have taken advantage of the tariff language and rate design to avoid paying the fixed charge during summer months.

But as it has been well established, and consistent with the straight-fixed variable rate design, the cost of distribution service for gas customers is independent of throughput. It is the <u>availability</u> of the gas distribution service that causes the cost. Consequently, to the extent a customer temporarily suspends gas service to their premises and avoids the monthly customer charge, Duke Energy Ohio is not being fairly compensated for its costs to provide service to that customer.

To remove such inequities and prevent customers from avoiding costs to serve, Duke Energy Ohio proposes modifications to its Charge for Reconnection of Service provisions. More specifically, Duke Energy Ohio proposes that the reconnection fee be changed from $17 to an amount equal to the total of avoided costs where customers voluntarily disconnect their natural gas service, only to reconnect it at the same premises within eight months. Absent this adjustment, the only way Duke Energy Ohio can fully recover its cost of service is to charge other customers for the avoided charges

Q. DOES THIS CHANGE AFFECT ALL CUSTOMERS RECONNECTING TO DUKE ENERGY OHIO'S GAS SERVICE?

A. No. It only affects those customers who <u>voluntarily</u> disconnect service and reconnect within a certain period of time. Customers who are involuntarily disconnected and customers who voluntarily disconnect because they moved premises are not impacted by the change.

V. <u>CONTINUING DEFERRAL AUTHORITY FOR MGP COSTS</u>

Q. DESCRIBE THE COMPANY'S REQUEST FOR CONTINUING DEFERRAL AUTHORITY RELATED TO ITS MGP CLEANUP ACTIVITIES.

A. In Case No. 09-712-GA-AAM, the Commission granted Duke Energy Ohio authority to defer costs related to the remediation of two former MGP sites. The

Company has since been deferring such costs and is proposing to begin recovering such costs via an adjustment, Schedule C-3.2, to its test year revenue requirement as described by Company witness Laub. Because the remediation work is not yet complete, the Company intends to continue to defer costs consistent with the deferral authority reflected in the Commission's November 12, 2009, order. The November 2009 order, pursuant to which deferral authority was initially established, allows Duke Energy Ohio to create a separate subaccount and defer all costs related to environmental investigation and remediation. Costs incurred after December 31, 2012, will be deferred for recovery in a future recovery similar to how the Company is proposing to recover the costs incurred up through the test year and pursuant to the November 2009 order.

VI. ALTERNATIVE REGULATION

Q. PLEASE PROVIDE THE DETAILS FOR DUKE ENERGY OHIO'S ALTERNATIVE REGULATION PLAN, SETTING FORTH THE FACTS AND GROUNDS UPON WHICH THE APPLICATION IS BASED AND THE ELEMENTS OF THE PLAN.

A. Duke Energy Ohio's Alternative Regulation Plan consists of: (1) Rider AMRP; (2) Rider AU; and (3) Rider ASRP. The Company has proposed to implement these rate mechanisms as part of its general gas rate case, as annually adjusted rate mechanisms, and as part of the Alternative Regulation Plan, in order to provide the Commission and the Company with flexibility regarding how the programs are implemented and operated.

Q. PURSUANT TO O.A.C. 4901:1-19-05(C)(2)(a), DOES DUKE ENERGY OHIO'S ALTERNATIVE REGULATION PLAN INVOLVE ANY TRANSITION PLANS?

A. No.

Q. REGARDING O.A.C. 4901:1-19-05(C)(2)(b), PLEASE PROVIDE DUKE ENERGY OHIO'S JUSTIFICATION FOR DEVIATING FROM TRADITIONAL RATE OF RETURN REGULATION, INCLUDING THE RATIONALE FOR THE COMPANY'S ALTERNATIVE REGULATION PLAN.

A. Duke Energy Ohio's Alternative Regulation Plan will facilitate efficient implementation and costs recovery for its existing AMRP and grid modernization programs and for its proposed ASRP. These programs will produce substantial benefits by enhancing pipeline safety and reliability and will improve the efficiency of the Company's natural gas distribution system. Expenses to maintain the gas distribution system will be lower as a result of these programs and all of the proposed riders have provisions for offsetting the costs to be recovered with expenses realized. The AMRP and ASRP will reduce leaks on the systems, which reduces maintenance expenses but, more importantly, enhances the safety and reliability of the system.

Q. PURSUANT TO O.A.C. 4901:1-19-05(C)(2)(c), DOES DUKE ENERGY OHIO'S ALTERNATIVE REGULATION PLAN PROPOSE A SEVERING OF COSTS AND RATES?

A. No.

Q. PURSUANT TO O.A.C. 4901:1-19-05(C)(2)(d), HAS THE COMMISSION PREVIOUSLY AUTHORIZED DUKE ENERGY OHIO TO EXEMPT ANY OF ITS GAS SERVICES FROM COMMISSION REGULATION?

A. No.

Q. PURSUANT TO O.A.C. 4901:1-19-05(C)(2)(e), WILL ANY OF DUKE ENERGY OHIO'S SERVICES OR REGULATIONS BE AFFECTED BY THE ALTERNATIVE REGULATION PLAN?

A. No.

Q. DOES THE COMPANY'S ALTERNATIVE REGULATION PLAN ADVANCE STATE POLICY?

A. Yes. The Alternative Regulation Plan advances a number of the goals established in R.C. 4929.02, as I discuss below.

The Alternative Regulation Plan promotes the availability to customers of adequate, reliable, and reasonably priced service (R.C. 4929.02(A)(1)). As Duke Energy Ohio continues replacing its cast iron and bare steel mains and modernizing its network and accelerates the replacement of its service lines, the natural gas distribution system will become safer, more reliable, and more efficient.

Customers continue to have unbundled and comparable natural gas service as well as a diverse set of suppliers as required under R.C. 4909.02(A)(2) and 4902.02(A)(3).

The Alternative Regulation Plan includes innovative programs that will allow Duke Energy Ohio to replace aging infrastructure in an efficient, cost-effective manner that passes through savings to customers and avoids the necessity for frequent rate cases over the next several years, thereby satisfying R.C. 4929.02(A)(4).

The Company's proposal to continue with its modified straight-fixed variable rate design is an effective method for decoupling revenue from sales, thus removing any disincentive for the utility to promote energy efficiency. Combined with the improved access to metering and billing data as part of its ongoing improvement process and grid modernization program, the Company satisfies R.C. 4929.02(A)(5). The decoupling provided for with the modified straight-fixed variable rate design also promotes the alignment of the Company's interests with consumer interest in energy efficiency and conservation as required in R.C. 4929.02(A)(12).

The Alternative Regulation Plan, along with the Company's proposed new Rider GGIT, supports distributed generation and recognizes the continuing emergence of natural gas markets. Commission approval of the Alternative Regulatory Plan will support the flexible regulatory treatment required under R.C. 4929.02(A)(6)

The Company continues to have a successful program for advancing customer choice. It has an existing program of purchasing receivables from suppliers and its customers enjoy a number of choices for alternative suppliers. R.C. 4929.02(A)(7) calls for a speedy transition to competition and the Company has met that expectation given it already has an effective competitive market for retail gas supply.

Consistent with R.C. 4929.02(A)(8), the Company's Alternative Regulation Plan does not include any subsidies flowing to or from regulated natural gas services and goods.

Pursuant to R.C. 4929.02(A)(9), the risks and rewards of the Company's offering of non-jurisdictional and exempt services do not affect rates, prices, terms, or conditions of non-exempt, regulated services and goods and do not affect the financial capability of the Company to comply with the state policy goals.

The Company's rate application and its Alternative Regulation Plan provide for competitively priced natural gas service with a concentrated focus on safety, reliability, and efficiency. In addition, the Company offers fully competitive options for purchasing the actual gas commodity from any certified supplier in its service territory. For all these reasons, the Company complies with R.C. 4929.02(A)(10) to facilitate the state's competitiveness in the global economy.

Regarding R.C. 4929.02(A)(11), the Company has a well established program for customer choice. At the time of this filing, there are numerous active suppliers in Duke Energy Ohio's service territory from which customers can choose. Aggregation is thriving in the service territory as evidenced by the recent decision by the city of Cincinnati to aggregate its gas customers.

Q. PLEASE DESCRIBE THE ALTERNATIVE REGULATION PLAN SCHEDULES YOU ARE SPONSORING OR CO-SPONSORING.

A. <u>Schedule A</u> generally describes the Company's Alternative Regulation Plan.

Schedule B provides the justification for deviating from traditional rate of return regulation.

Schedule C confirms that Duke Energy Ohio does not seek a severing of costs and rates.

Schedule D confirms that Duke Energy Ohio has not been authorized to exempt any services under R.C. 4929.04.

Schedule E provides a matrix of Duke Energy Ohio's rates, services, and regulations affected by the Alternative Regulation Plan. Company witness Riddle provides further details about changes to the tariff schedules.

Schedule F confirms that Duke Energy Ohio does not expect any cross-subsidization to result from the Alternative Regulation Plan.

Schedule G discusses how the Company's Alternative Regulation Plan avoids any undue preference of disadvantage for any stakeholders and, as I have discussed in great detail above, complies with the state's policy goals.

Schedule H explains that this schedule refers to requirements established only for electric utilities.

Schedule I references schedules filed by the Company showing the effect on Duke Energy Ohio's financial statements if the Alternative Regulation Plan is adopted.

Schedule J is a list of the witnesses who are sponsoring Schedules A through I of the filing requirements.

VII. <u>CONCLUSION</u>

Q. DO YOU HAVE AN OPINION REGARDING WHETHER DUKE ENERGY OHIO'S RATE REQUEST IS REASONABLE?

A. Yes.

Q. PLEASE STATE YOUR OPINION.

A. Duke Energy Ohio's rate request is fair and reasonable. The date certain in Duke Energy Ohio's last rate case was March 31, 2007, and the date certain for this case is March 31, 2012. Despite more than five years of inflationary pressures and capital investment, Duke Energy Ohio is requesting an overall increase in rates of approximately 6.6 percent. Through aggressive cost management practices, the Company has been able to hold its increase request to a reasonable level.

Q. WERE THE ALTERNATIVE REGULATION SCHEDULES THAT YOU SPONSOR OR CO-SPONSOR PREPARED BY YOU OR UNDER YOUR DIRECTION AND SUPERVISION?

A. Yes.

Q. IS THE INFORMATION CONTAINED IN THE ALTERNATIVE REGULATION PLAN SCHEDULES THAT YOU SPONSOR OR CO-SPONNSOR ACCURATE TO THE BEST OF YOUR KNOWLEDGE AND BELIEF?

A. Yes.

Q. DOES THIS CONCLUDE YOUR PRE-FILED DIRECT TESTIMONY?

A. Yes.