

ORIGINAL

In The
Supreme Court of Ohio

The Office of the Ohio Consumers'
Counsel,

Appellant,

v.

The Public Utilities Commission of
Ohio,

Appellee.

:
:
: Case No. 09-1547
:
:
: On appeal from the Public Utilities
: Commission of Ohio, Case Nos. 07-
: 1080-GA-AIR, et al., In The Matter of
: the Notice of Intent of Vectren Energy
: Delivery of Ohio for an Increase in its
: Natural Gas Rates.
:
:
:

MERIT BRIEF
SUBMITTED ON BEHALF OF APPELLEE,
THE PUBLIC UTILITIES COMMISSION OF OHIO

Janine L. Migden-Ostrander (0002310)
Consumers' Counsel

Maureen R. Grady (0020847)
Counsel of Record
Joseph P. Serio (0036959)
Michael E. Idzkowski (0062839)
Assistant Consumers' Counsel
10 West Broad Street, Suite 1800
Columbus, OH 43215-3485
614.466.8574 (telephone)
614.466.9475 (fax)
grady@occ.state.oh.us
serio@occ.state.oh.us
idzkowski@occ.state.oh.us

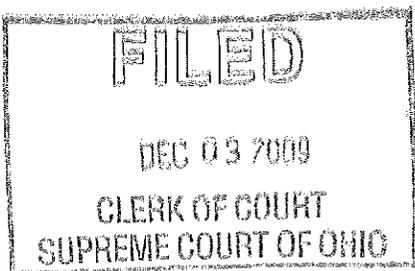
Counsel for Appellant,
Office of the Ohio Consumers' Counsel

Richard Cordray (0038034)
Ohio Attorney General

Duane W. Luckey (0023557)
Section Chief

Anne L. Hammerstein (0022867)
Counsel of Record
Werner L. Margard III (0024858)
Assistant Attorneys General
Public Utilities Section
180 East Broad Street, 6th Fl
Columbus, OH 43215-3793
614.466.4397 (telephone)
614.644.8764 (fax)
duane.luckey@puc.state.oh.us
anne.hammerstein@puc.state.oh.us
werner.margard@puc.state.oh.us

Counsel for Appellee,
The Public Utilities Commission of Ohio



Samuel C. Randazzo (0016386)

Counsel of Record

Gretchen J. Hummel (0016207)

Lisa J. McAlister (0075043)

McNees Wallace & Nurick LLC

21 East State Street, 17th Floor

Columbus, OH 43215

614.469.8000 (telephone)

614.469.4653 (fax)

sam@mwncmh.com

ghummel@mwncmh.com

lmcalister@mwncmh.com

**Counsel for Intervening Appellee,
Vectren Energy Delivery of Ohio, Inc.**

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The Office of the Ohio Consumers’ Counsel,	:	:	Case No. 09-1547
Appellant,	:	:	On appeal from the Public Utilities Commission of Ohio, Case Nos. 07- 1080-GA-AIR, <i>et al.</i> , <i>In The Matter of the Notice of Intent of Vectren Energy Delivery of Ohio for an Increase in its Natural Gas Rates.</i>
v.	:	:	
The Public Utilities Commission of Ohio,	:	:	
Appellee.	:	:	

**MERIT BRIEF
SUBMITTED ON BEHALF OF APPELLEE,
THE PUBLIC UTILITIES COMMISSION OF OHIO**

INTRODUCTION

The Office of the Consumers’ Counsel (OCC), *the statutorily designated representative of residential ratepayers in proceedings before the Public Utilities Commission of Ohio* (Commission), has the temerity to claim that the rate design proposed by Vectren Energy Delivery of Ohio, Inc. (Vectren or Company) was not properly noticed to Vectren’s residential customers. As required by law, the Commission approved the published notice that relayed to residential customers Vectren’s “propose[d] changes to the rate design for Rate 310 (Residential Sales Service) and Rate 315 (Residential Transportation Service) that initiate a gradual transition to a straight fixed variable rate for distribution service.” Thus, residential ratepayers *and* their representative, OCC, were put on notice at the beginning of the case that the Company

wanted to recover more of its fixed costs through the customer charge. OCC promptly intervened before the Commission filed objections to the Commission's Staff's recommendation on the issue, and filed testimony that advocated a different type of rate design decoupling than that proposed by Vectren and ultimately adopted by the Commission. These actions conflict with OCC's lack of notice argument. Customers had a more than adequate opportunity to be heard regarding the proposed change in rate design, and residential customers were active participants in both the evidentiary and local public hearings in this case.

Residential ratepayers, through the published notice provided to them and through their statutory representative, were fully aware of the proposed rate design. Through OCC, they exercised to the fullest their opportunity to be heard by the Commission by presenting numerous witnesses in support of their own rate design decoupling proposal. In other words, OCC agreed that distribution rates should be decoupled from the historic rate design relationship to the volume of gas sold, but could not agree with Vectren or the Commission on *how* rates should be decoupled.

In making its rate design decision in this case, the Commission carefully weighed the merits of the proposals, the credibility of the evidence presented, and the impact the proposals would have on residential customers, conservation, and the Company. There was evidence in the record supporting both decoupling proposals. The Commission found the evidence supporting the levelized rate design to be more credible than OCC's evidence against it. OCC ignores this finding. In addition, OCC fails to weigh the implications of the choice of rate designs on all parties impacted and blithely dismisses

evidence that it is unable to dispute. Similarly, OCC makes a number of arguments not properly raised to the Court in either its application for rehearing or notice of appeal.

On the other hand, the Commission balanced the interests of residential ratepayers and the Company before concluding that the levelized rate design is the most appropriate proposal. The Commission's decision permits Vectren a more reasonable opportunity to recover the fixed costs of distribution, is easier for residential customers to understand, encourages Vectren to promote conservation and customers to conserve, and sends an appropriate price signal to residential ratepayers.

The Commission's order is reasonable and should be affirmed.

STATEMENT OF THE FACTS AND CASE

The narrow challenges before the Court are how the Commission designs rates for residential gas distribution service, and what constitutes proper notice to residential customers. In the case below, all parties, except one who did not oppose, agreed that Vectren was entitled to both the rate increase and the amount granted. *See In re Vectren Energy Delivery of Ohio, Inc.*, Case Nos. 07-1080-GA-AIR, *et al.* (hereinafter *In re Vectren*) (Stipulation and Recommendation at 23) (September 8, 2008), Sec. Supp. at 95.¹ Additionally, the same parties either agreed to or did not oppose the amount of the increase to be collected from residential customers.

¹ References to documents included in Appellee's Second Supplement are denoted as "Sec. Supp. at ___;" references to Appellee's Appendix attached hereto are denoted as "App. at ___;" references to documents included in Appellant's Supplement are denoted as "OCC Supp. at ___;" and references to documents included in Appellant's Appendix are denoted as "OCC App. at ___."

On September 28, 2007, Vectren filed its notice of intent for an increase in its natural gas rates. Prior even to Vectren filing its rate increase application, OCC filed a motion to intervene with the Commission on November 5, 2007. Vectren filed its application to increase gas distribution service rates on November 20, 2007. The Commission issued an Entry on January 16, 2008, that approved the proposed newspaper notice to which OCC objects. OCC did not file an application for rehearing from the Commission's approval of this newspaper notice. The Commission's Staff investigated the application and supporting information and issued a Staff Report of Investigation on June 16, 2008. Several parties representing diverse interests filed objections to the report and extensive discovery was conducted in preparation for the hearing on the rate application.

Following extensive negotiations, a settlement was reached. A Stipulation and Recommendation (Stipulation) filed on September 8, 2008 was signed by all parties but one, and resolved all issues in the case but one. *Id.* at 23, Sec. Supp. at 95. The only party not a signatory to the Stipulation, Honda of America Mfg., Inc. (Honda), affirmatively indicated that it did not oppose the Stipulation. *Id.* at 23, Sec. Supp. at 95.

The issues reserved for litigation were the rate design for residential rates and notice. Specifically, the parties agreed that rate design issues associated with Rate Schedules 310 (Residential Sales Service) and 315 (Residential Transportation Service) would be fully litigated and submitted to the Commission for resolution on the merits. Although rate design is largely a policy matter, extensive evidence was taken over nine days of hearings beginning on August 19, 2008 and concluding on September 9, 2008.

The rates levelized in the case below were those rates charged to residential customers to recover Vectren's distribution or gas delivery costs. Distribution costs are separate from what the customer pays for the gas itself, which makes up 75 to 80 percent of the average customer's monthly bill. *In re Vectren* (Opinion and Order at 8) (January 7, 2009), OCC Supp. at 229. Gas utility distribution costs are predominately fixed costs – meaning they do not vary with the volume of gas delivered to each customer. The historical rate design charged customers for these fixed distribution costs by use of both a fixed rate (the customer charge) and a volumetric rate. Because the customer or fixed rate charge was low, this left the majority of the fixed distribution costs subject to recovery through the volumetric rate. As a result of high gas prices and customer conservation practices, less gas was purchased. Applying these lower volumes to the volumetric part of the rate meant gas companies under-recovered the fixed costs of distribution. The straight fixed variable or levelized rate design permits utilities a more reasonable opportunity to recover the fixed costs of distribution, is easier for customers to understand, and encourages utilities to promote conservation to benefit customers.

OCC and Ohio Partners for Affordable Energy (OPAЕ) proposed a decoupling mechanism different than the levelized rate design adopted by the Commission. OCC and OPAЕ proposed that rates be designed as they had been historically with a low fixed customer charge, a volumetric based charge, and a decoupling or sales reconciliation rider (SRR). *Id.* at 11, OCC Supp. at 232. The decoupling rider permits the utility to offset any under-recovery of fixed costs through the volumetric charge with an adjustable rider. *Id.* at 11-12, OCC Supp. at 232-233. The proposed adjustable rider would thus

increase rates to customers after the fact as a result of the utility under-recovering its fixed costs through the historically low volumetric rate. The Commission found, as a result, “the SRR proposed by OCC and OPAE [would cause] consumers ... [to] pay a higher portion of their fixed costs during the heating season when overall natural gas bills are already at their highest, and rates would be less predictable because they are subject to annual adjustments to recover lower-than-expected sales.” *Id.* Thus, all parties in the Commission proceedings agreed that rates should be designed to remove the connection between the utility’s ability to recover its fixed distribution costs and residential customer’s consumption of gas. The Commission found in favor of the levelized rate design. While both methods address revenue and earnings stability issues through ensuring recovery of fixed costs of delivering gas to consumers, and both methods remove any utility disincentive to promote conservation and energy efficiency, the Commission determined that “a levelized rate design has the added benefit of producing more stable customer bills throughout the year because fixed costs will be recovered evenly throughout the year.” *Id.* at 11, OCC Supp. at 232.

During the adjudicatory hearing, eleven witnesses appeared and sponsored direct, supplemental, and rebuttal testimony, both in support of the Stipulation and addressing rate design. In addition, four local public hearings were held, during which 18 witnesses offered sworn testimony. A number of the public witnesses at the public hearings testified regarding the rate design issue. Transcript at 5-8, 15-16 (September 3, 2008) (Sidney, OH Public Hearing), Sec. Supp. at 66-69, 70-71; Transcript at 5 (September 4,

2008 at 6:00 p.m.) (Dayton, OH Public Hearing), Sec. Supp. at 73; Transcript at 8-17 (September 8, 2008) (Washington Courthouse, OH Public Hearing), Sec. Supp. at 75-84.

The Commission issued its opinion and order on January 7, 2009 to which OCC addressed its February 6, 2009 application for rehearing. When the Commission issued its entry on rehearing on August 26, 2009, OCC initiated this appeal through a notice filed with this Court on the same date.

ARGUMENT

Proposition of Law No. I:

The Commission properly exercised its judgment and discretion in developing Vectren's rates. *General Motors Corp. v. Pub. Util. Comm'n*, 47 Ohio St. 2d 58, 351 N.E.2d 183 (1976). Where the Commission exercised its considerable discretion in rate design matters in accord with the manifest weight of the evidence, the Commission's decision should be upheld. *Citywide Coalition for Utility Reform v. Pub. Util. Comm'n*, 67 Ohio St. 3d 531, 620 N.E.2d 832 (1993).

The Commission possesses well-established authority and discretion to set customer rates for utility services. The Court has recognized the broad and plenary authority delegated to the Commission to establish utility rates and terms of service. *See, e.g., Kazmaier Supermarkets, Inc. v. Toledo Edison Co.*, 61 Ohio St. 3d 147, 573 N.E.2d 655 (1991). Ratemaking is not, nor has it ever been, an exact science.² Ratemaking constantly requires an application of seasoned and studied judgment. Where the Commission applies its discretion and judgment in a manner consistent with the evidence before

² The United States Supreme Court has long recognized that rate design is “not a matter for the slide-rule. It involves judgment on a myriad of facts. It has no claim to an exact science.” *Colorado Interstate Co. v. FPC*, 324 U.S. 581, 589 (1945).

it, it acts lawfully under its statutory ratemaking authority. Ohio Rev. Code Ann. § 4909.15 (West 2009), App. at 4-8; *General Motors Corp. v. Pub. Util. Comm'n*, 47 Ohio St. 2d 58, 351 N.E.2d 183 (1976). The Commission's judgment and expertise in rate design matters should not be disturbed unless it is shown to be against the manifest weight of the evidence. *Citywide Coalition for Utility Reform v. Pub. Util. Comm'n*, 67 Ohio St. 3d 531, 620 N.E.2d 832 (1993).

OCC bears a difficult burden of showing that the Commission's decision is against the manifest weight of the evidence or clearly unsupported by the record. *See, e.g., Ohio Partners for Affordable Energy v. Pub. Util. Comm'n*, 115 Ohio St. 3d 208, 210, 874 N.E.2d 764, 767 (2007); *Monongahela Power Co. v. Pub. Util. Comm'n*, 104 Ohio St. 3d 571, 820 N.E.2d 921 (2004). There is ample record evidence supporting both the Commission's decision to "rethink" how it designs natural gas rates and its adoption of the levelized rate design in this case. OCC fails to sustain its burden.

A. The manifest weight of the evidence supports adoption of the levelized rate design because it is reasonable, understandable, and sends the proper price signal to customers.

The manifest weight of the evidence in the record supports the Commission's determination that "a levelized rate design sends better price signals to consumers." *In re Vectren* (Opinion and Order at 12) (January 7, 2009), OCC Supp. at 233. Even OCC, or at least its witness, Mr. Colton, agrees that a basic ratemaking principle "is that rates should reflect costs" and "to the extent practicable, one set of customers should not be charged for costs that a different set of customers cause a utility to incur." Direct Testi-

mony of R. Colton (OCC Ex. 2) at 21-22, OCC Supp. at 64-65. As the Commission acknowledged, straight fixed variable (SFV) rate design is a change from the current rate design and, “as with any change, there will be some customers who will be better off and some customers who will be worse off, as compared to the existing rate design.” *In re Duke Energy Ohio*, Case Nos. 07-589-GA-AIR, *et al.* (Opinion and Order at 19) (May 28, 2008), App. at 12; *see also In re Vectren* (Opinion and Order at 13-14) (January 7, 2009), OCC Supp. at 229. These results do not mean a subsidy is created.

Rather than creating a subsidy, the straight fixed variable rate *reduces* a subsidy that existed under Vectren’s historical rate design. The previous rate design recovers most of the Company’s fixed distribution costs through a rate that varies with usage, and it recovers only a small part of the costs through a fixed rate. Accordingly, the Commission found that the prior rate design distributes more of the fixed costs to higher users of natural gas. The straight fixed variable rate design more appropriately distributes fixed cost responsibility by increasing the portion of those costs recovered through a fixed rate component, thereby matching fixed and variable cost recovery more closely to the costs actually incurred. Testimony of S. Puican (Staff Ex. 3) at 4-5, OCC Supp. at 148-149. Because some low usage customers have not paid the entirety of their fixed costs under the prior rate design, they may now pay more. The converse is true for higher usage customers. In its order, the Commission explained:

The levelized rate design will impact low-usage customers more than high-usage customers, since they [low-usage customers] have not been paying the entirety of their fixed costs under the existing rate design. High-usage customers, who

have been paying more than their share of the fixed costs, will actually experience a reduction in their gas bills.

In re Vectren (Opinion and Order at 14) (January 7, 2009), OCC Supp. at 235. As the Commission described, the new rate design does not create a *subsidy*. Instead, the new rate design reduces a subsidy caused by the historical rate design. Thus, the new rate design results in a more appropriate reflection of cost causation and is a proper rate design.

B. Straight fixed variable designed rates do not disproportionately impact low income customers.

The rate effects of the straight fixed variable rate design are not impacted by the income of individual ratepayers. Higher use customers who have been overpaying their fixed costs, including those with low income, will experience a reduced bill. Conversely, lower use customers who have not been paying all their fixed costs, including those with low-income, will experience an increase. Average use customers who have been paying their fixed costs, including those with low income, will not be impacted by this change in rate design. *In re Duke Energy Ohio*, Case Nos. 07-589-GA-AIR, *et al.* (Opinion and Order at 19) (May 28, 2008), App. at 13; *In re Vectren*, Case Nos. 07-1080-GA-AIR, *et al.* (Opinion and Order at 13-14), OCC Supp. at 234-235.

The record shows that many low income customers will benefit from the change. Historically the average annual usage of Percentage of Income Payment Plan (PIPP) customers has been greater than the average annual usage of non-PIPP customers. As Staff witness Puican testified:

The data shows that, for the 12 months ending September 2007, PIPP customers' average usage was 110.9 Mcf and non-PIPP residential customers' average usage was 81.5 Mcf. Although PIPP customer usage may not be a perfect representation of all low-income customer usage, it is the best readily available proxy. The usage data indicates that low-income customers are, on average, not low-usage customers. Because high-usage customers will benefit from the SFV [straight fixed variable] rate design, and low-income customers are more likely to be high-usage customers, it is reasonable to conclude that low-income customers are actually more likely to benefit from SFV.

Testimony of S. Puican (Staff Ex. 3) at 6-7, OCC Supp. at 150-151.

Contrary to OCC witness Colton's testimony, Company witness Overcast further corroborated that in fact low income customers on Vectren's system are in fact among the Company's higher usage customers. Rebuttal Testimony of H.E. Overcast (Co. Ex. 8a) at 11, Sec. Supp. at 13. Mr. Overcast found that "[b]ased on the analysis of actual billing information for VEDO's residential customer[s] and available Census block group data for VEDO's service area, . . . low income customers in VEDO's service area consume on average more natural gas annually than all but the highest income residential customers in VEDO's service area." *Id.* at 14, Sec. Supp. at 16. OCC's witness Colton based his conclusions on national and statewide data that the Census Bureau cautioned may be unreliable, not Vectren-specific data. *In re Vectren*, 07-1080-GA-AIR, *et al.* (Opinion and Order at 13) (January 7, 2009), OCC Supp. at 234. Vectren and the Staff presented evidence based on Company-specific information. Testimony of S. Puican (Staff Ex. 3) at 6-7, OCC Supp. at 150-151; Rebuttal Testimony of H.E. Overcast (Co. Ex. 8a) at 11-

14, Sec. Supp. at 13-16. In citing Mr. Overcast, Mr. Puican, and Mr. Colton's testimony, the Commission found:

“The evidence in the record of this case does not support the conclusion that low income customers are low usage customers Although OCC's witness Coulton [sic] testified that his analysis indicated that low-income customers were also low-usage customers, Mr. Coulton based his analysis upon monthly surveys conducted by the Census bureau, using data which the Census bureau cautioned may be unreliable (Tr.V at 56-634; Co. Ex. 81 at 11), thus, Mr. Coulton's testimony regarding whether low-income customers are also low-usage customers is of little probative value in this proceeding. We find that the record demonstrates that low-income customers, on average, would actually enjoy lower bills under the levelized rate design. *In re Vectren*, Case No. 07-1080-GA-AIR, *et al.* (Opinion and Order at 13) (January 7, 2009), OCC Supp. at 234.

Accordingly, the record supports the Commission's decision and demonstrates that many customers with low income have been overpaying their fixed costs and they will benefit from a change to the straight fixed variable rate.

C. Straight fixed variable designed rates send the appropriate price signal to Vectren's customers and encourage conservation.

The straight fixed variable rate design encourages appropriate conservation by consumers and sends the appropriate price signal to consumers. Based on the record the Commission found that a levelized or straight fixed variable rate design sends a better price signal to consumers. *In re Vectren*, Case Nos. 07-1080-GA-AIR, *et al.* (Opinion and Order at 12) (January 7, 2009), OCC Supp. at 233. As Mr. Puican explained, “customers make conservation decisions based on their total bill.” Testimony of S.

Puican (Staff Ex. 3) at 3, OCC Supp. at 147. The largest and volatile component of that bill is the cost of natural gas. *Id.* The gas cost rate is many times greater than the distribution rate. *Id.* For example, Mr. Puican noted:

Vectren used a gas cost rate of \$9.686 per Mcf in its application and regardless of which rate design is ultimately approved in this proceeding, the variable component of base rates will be relatively small in comparison to the cost of the gas itself. Customers will always achieve the full value of the gas cost savings regardless of the distribution rate. I believe most customers make conservation decisions based on their total bill rather than by an explicit cost/benefit analysis based solely on the variable portion of rates, particularly given the volatility of the gas cost component.

Id. at 3-4, OCC Supp. at 147-148. OCC ignores that the cost of natural gas is the largest factor, by far, in conservation decisions. The Commission, however, recognized the savings in the cost of natural gas drive the size of bills and, accordingly, conservation decisions. *In re Vectren* (Opinion and Order at 12) (January 7, 2009), OCC Supp. at 233. The rate design does not affect the cost of gas and, for that reason, it will not significantly affect conservation decisions.

A change in a consumer's total bill due to a change in distribution rate design should not have a chilling effect on conservation decisions. The largest component of those bills, the cost of natural gas, is volatile. Testimony of S. Puican (Staff Ex. 3) at 3-4, OCC Supp. at 147-148. For example, those costs increased every month from January 2008 through July 2008. *Id.* In one month the increase was \$1.78 per Mcf, and that was 6 times greater than a \$0.28 increase from the prior month. *Id.* at 4, OCC Supp. at 148. The entire period experienced a \$5.04 increase, approximately a 69% increase. *Id.* Such

fluctuations led Mr. Puican to conclude, “[g]iven these types of extreme fluctuations, I believe customers recognize the imprecision of any payback analysis and will incorporate that uncertainty into their energy efficiency investment decisions.” *Id.* Accordingly, the change to a straight fixed variable rate structure cannot be expected to adversely affect consumer conservation investment decisions.

Rather than impede investment decisions, the straight fixed variable rate design will benefit them because it sends better price signals. Including fixed costs in a variable rate distorts price signals. *Id.* at 4, OCC Supp. at 148. Because the straight fixed variable rate design aligns fixed costs with fixed rate components and variable costs with variable rate components better than the current rate structure, it provides better price signals for consumers’ conservation investment decisions. *Id.* Mr. Puican explained:

The variable rate component of rates should reflect a utility’s true avoided costs, *i.e.* the costs that a utility does not incur with a unit reduction in sales. The SFV [straight fixed variable] rate design satisfies this condition by more closely matching fixed and variable cost recovery to those actual costs incurred. Artificially inflating the volumetric rate beyond its cost basis skews the analysis and will cause an over-investment in conservation.

Id. The straight fixed variable rate design provides better information and results in more informed consumer decisions. That is a benefit, not a detriment, to consumers and conservation.

In that fashion also, the straight fixed variable rate design eliminates a disincentive for Vectren to promote energy efficiency. Mr. Puican explained that any gas distribution

utility has a disincentive to promote energy efficiency when it must recover its fixed costs through volumetric rates. *Id.* He stated:

To artificially require the Company to recover its fixed costs through the volumetric rate creates a disincentive for the Company to promote energy efficiency. Staff is proposing a rate design [straight fixed variable] that eliminates this disincentive. The relatively small potential disincentive for customers to conserve due to the volumetric rate is more than offset by the removal of the Company's disincentive to actively promote and fund energy-efficiency.

Id. at 4, OCC Supp. at 148. Even if some small potential disincentive were associated with the straight fixed variable rate design, it is more than offset by the removal of the Company's disincentive to promote and fund energy efficiency programs. *Id.*

For these reasons, the record demonstrates that the straight fixed variable rate design encourages conservation. It is in accord with state policy and is consistent with any provision of the Revised Code encouraging conservation.

D. The straight fixed variable rate design proposal incorporates the rate design principle of gradualism.

OCC argues that the Commission proceeded too quickly in adopting a straight fixed variable rate design. OCC has suggested the utilization of studies and other time-consuming activities. In adopting the levelized rate design, the Commission found such proposals are not necessary. The record reflects that the levelized rate design more appropriately aligns fixed costs with fixed rate components, and better reflects the fixed costs customers should incur and the utility should recover. Additionally, this rate design does not affect recovery of the principal cost that drives a consumer's bill, the commodity

cost. Moreover, the levelized rate design incorporates the principle of gradualism. The Commission's order contains a two-stage transition to eventual recovery of all fixed costs through a fixed distribution rate in the second phase. The first phase leaves a portion of the fixed costs for recovery through a variable rate component while transitioning to the recovery of all fixed costs (all distribution costs) from the fixed rate component in the second year. *In re Vectren*, Case No. 07-1080-GA-AIR (Opinion and Order at 15) (January 7, 2009), OCC Supp. at 236.

OCC has not sustained its burden.

Proposition of Law No. II:

Where a utility publishes a Commission-approved notice of a change in rate design, specifically mentioning that this is a change, this is sufficient to put customers on notice of the proposal. It would give customers a "reason to view the exhibits on file at the Commission...[and if interested participate] in the hearings before the Commission." *Committee Against MRT v. Pub. Util. Comm'n*, 52 Ohio St. 2d 231, 234, 371 N.E.2d 547, 549 (1977).

- A. OCC is the statutory representative of residential customers. Its participation in the proceedings from before the time of the application demonstrates that residential customers, through their representative, were on notice of the proposal.**

Vectren submitted its notice with its rate increase application on November 20, 2007 and the Commission approved the notice by entry on January 16, 2008. Prior to Vectren's submission of the notice and the Commission's approval, OCC, the statutorily appointed representative of residential ratepayers, promptly intervened in the case on November 5, 2007. The Commission's docket shows that OCC did not file an applica-

tion for rehearing from the entry approving the notice. In fact, OCC did not bring the issue to the Commission's attention until it filed its objections to the Staff Report of Investigation on July 16, 2008, seven months after Commission approval of the notice. OCC objections to the Staff Report at 28-29, Sec. Supp. at 98-99.

Citing *Duff v. Pub. Util. Comm'n*, OCC mistakenly claims that *Duff* stands for the proposition that the "Court has determined that the notice provisions of R.C. 4909.18 and 4909.19 are jurisdictional." 56 Ohio St. 2d 367, 376, 384 N.E.2d 264, 271-272 (1978). First, this portion of the *Duff* opinion does not discuss R.C. 4909.18. OCC is wrong about that. Second, what the *Duff* Court considered was a different part of R.C. 4909.19 that required the Commission to serve the Staff Report of Investigation upon the mayors of the municipalities in the utility's service area. *Id.* at 368, 384 N.E.2d at 267. One of the *Duff* appellants alleged that the failure to serve the Staff Report bore jurisdictional consequences and nullified the Commission's order. *Id.* at 376, 384 N.E.2d at 271-272.

The Court held:

This court disagrees. The General Assembly did not require that the staff reports be sent to the mayors as a means of giving notice of application, pursuant to which jurisdiction is acquired; rather, this provision was intended to facilitate meaningful contest of rate increase applications by providing interested parties with the materials necessary for an informed challenge. It is akin to a mandatory discovery provision, independent of jurisdictional requirements.

Id. The Court went on to describe the provision in R.C. 4909.19 that is the jurisdictional provision, but that discussion was not central to its holding. This was *dicta*.

R.C. 4909.19 does require the utility to “publish the substance and prayer of such application, *in a form approved by the public utilities commission*, . . . in a newspaper published and in general circulation throughout the territory in which such public utility operates and affected by the matters referred to in said application.” Ohio Rev. Code Ann. § 4909.19 (West 2009), App. at 9. The Commission approved the notice. Further, in its opinion and order the Commission found that the notice stated the substance of the proposal and provided enough information for customers to decide whether to look further into the matter or to intervene. *In re Vectren*, Case No. 07-1080-GA-AIR (Opinion and Order at 16) (January 7, 2009), OCC Supp. at 237. Finally, the Commission determined “that the notices at issue substantially comply with the applicable statutes.” *Id.*

OCC was fully aware of the issues in the case; it litigated the rate design issues, and appealed them to the Court. Consequently, it is disingenuous of OCC to now say that residential ratepayers were not aware of the substance and prayer of the application. R.C. 4911.15 states that “[t]he consumers’ counsel, at the request of one or more residential consumers . . . or whenever in his opinion the public interest is served, may represent those . . . whenever an application is made to the public utilities commission by any public utility. . . .” Ohio Rev. Code Ann. § 4911.15 (West 2009), App. at 11. In the cases discussed below, the interested parties were *prevented* from participating in proceedings before the Commission by the *complete* lack of notice of the significant change in rate design. That is not the factual circumstances here. OCC chose to intervene, represented

the interests of residential ratepayers, and litigated the rate design issue on their behalf, so OCC cannot say with credibility either OCC or its clients lacked notice of the proposal.

B. The notice contained the substance and prayer of the proposed change to the straight fixed variable rate design in Vectren’s application in accordance with R.C. 4909.18 and R.C. 4909.19.

R.C. 4909.18(E) requires a utility upon filing a rate increase application with the Commission to include a proposed notice “fully disclosing the substance of the application.” Ohio Rev. Code Ann. § 4909.18(E) (West 2009), App. at 8. In addition, R.C. 4909.19 demands that “the public utility shall forthwith publish the substance and prayer of such application, in a form approved by the public utilities commission....” Ohio Rev. Code Ann. § 4909.19 (West 2009), App. at 9. Vectren filed its proposed notice with the Commission. Among other things the notice stated:

This notice describes the substance of the Application. However, any interested party seeking detailed information with respect to all affected rates, charges, regulations and practices may inspect a copy of the Application.... In the Application, VEDO [Vectren] *proposes changes to its rate schedules to reflect increases to the cost of service. Additionally, VEDO proposes changes to the rate design for Rate 310 (Residential Sales Service) and Rate 315 (Residential Transportation Service) that initiate a gradual transition to a straight fixed variable rate for distribution service.*

OCC Supp. at 124-125. The notice states that Vectren proposed “changes to the rate design” for residential sales service. This gives more than enough notice so that a residential customer might inquire as to what the changes would be, regardless of whether customers understood what a “straight fixed variable rate” might be. It was clear

a change in the rate structure was to be determined in this case, regardless of whether the actual second phase rates were contained in the notice.

The Court has determined that “[w]hile generally the published notice required under R.C. 4909.19 *need not contain every specific detail affecting rates* contained in the application (indeed, such a requirement would be highly impractical and unnecessarily expensive), the court notes that the statute does require that the ‘substance’ of the application be disclosed.” *Committee Against MRT v. Pub. Util. Comm’n*, 52 Ohio St. 2d 231, 234, 371 N.E.2d 547, 549 (1977). As OCC recognized in its brief, in *Committee Against MRT*, “the utility *failed to mention its proposal* [regarding a switch to measured rate service] in the notice, although it had fully explained the measured rate service in its application filed at the commission.” OCC Merit Brief at 9. Here, Vectren gave specific notice of the proposal to change the residential rate design to transition to straight fixed variable. This is a very different scenario from that in *Committee Against MRT* where the utility made “*no mention of this important proposal*” in its notice. 52 Ohio St. 2d at 234, 371 N.E.2d at 549. The residential customers who would to review the published notice would see that a *change* was proposed and take advantage of the opportunity to look further into the proposal at the Commission.

OCC also cites *Ohio Assn. of Realtors v. Pub. Util. Comm’n* to support its claim that notice was insufficient. 60 Ohio St. 2d 172, 175, 398 N.E.2d 784, 785-786 (1979). Just as it did in its discussion of *Committee Against MRT*, OCC accurately relates that “[e]ven though a portion of the application converted the utility’s business customers to a measured rate service, *the utility failed to refer to the change in it published notice.*”

OCC Merit Brief at 10. Again, Vectren's published notice pointed out that the utility proposed to gradually change its residential rate design to straight fixed variable. Vectren customers had notice that a change was in the works that might impact them and were free to investigate as they chose. This was decidedly not the factual setting in either of the cases cited by OCC. In *Ohio Assn. of Realtors*, the Court held that "[t]he notice requirement of the statute as discussed by this court in *MRT* ... is not an unreasonable one. It requires only that the notice state the reasonable substance of the proposal so that consumers can determine whether to inquire further as to the proposal or intervene in the rate case." 60 Ohio St. 2d at 176, 398 N.E.2d at 786. As the Commission found in its entry on rehearing, "the notice at issue in this proceeding stated the reasonable substance of VEDO's [Vectren's] proposal, including sufficient information for consumers to understand that VEDO had proposed a new rate design along with its proposed increase in rates." *In re Vectren* (Entry on Rehearing at 4) (August 26, 2009), OCC App. at 90. Both *Ohio Assn. of Realtors* and *Committee Against MRT* support the Commission's position that the notice met Revised Code requirements. The Commission's finding should be affirmed.

- C. **The right to notice in a ratemaking proceeding is statutory, not constitutional, and absent express statutory provision, a ratepayer has no right to notice and hearing under the Due Process Clauses of the Ohio and United States Constitutions. *Office of the Consumers' Counsel v. Pub. Util. Comm'n*, 70 Ohio St. 3d 244, 248-249, 638 N.E.2d 550, 553-554 (1994).**

The Court has held on numerous occasions that “absent express statutory provision, a ratepayer has no right to notice and hearing under the Due Process Clauses of the Ohio and United States Constitutions.” *Consumers' Counsel*, 70 Ohio St. at 248-249, 638 N.E.2d at 553-554. (citations omitted). Notice was published on this case. The Commission found that:

The notices at issue in this proceeding stated the reasonable substance of VEDO's proposal and provided sufficient information for consumers to determine whether to inquire further into the proposal or intervene in the case Further, the published notice provided sufficient information to consumers to understand that VEDO had proposed a new rate design so that consumers could determine whether to inquire further into the case or to intervene.” *In re Vectren*, Case Nos. 07-1080-GA-AIR, et al. (Opinion and Order at 16) (January 7, 2009).

The Commission's finding that the notice substantially complied with R.C. 4909.18(E) and R.C. 4909.19 is reasonable and should be sustained by this Court.

OCC attempts to argue for the first time on brief that the notice provided was unconstitutional in violation of the Due Process clauses of the Ohio and United States Constitutions. OCC Merit Brief at 18-33. Given the body of decisions by the Court to the contrary, OCC's argument should be denied.

D. There is no legitimate claim of entitlement to conservation assistance similar to that recognized for continued utility service.

In this matter, no customer is being denied utility service, had service terminated or even threatened to be terminated as a consequence of the Commission's opinion and order. Neither does OCC claim this is the case. What OCC does assert is that recent energy conservation programs coupled with codified state policy provisions that encourage energy conservation rise to the level of a protected property interest under both the Ohio and federal due process provisions. OCC Merit Brief at 24. While the United States Supreme Court has recognized that *continued utility service* is a constitutionally protected property interest, it has not gone so far as to recognize such a right of entitlement in energy efficiency programs. OCC cites no such cases and none came to light in researching this brief.

In *Memphis Light, Gas & Water Div. v. Craft*, the Court found that customers held a legitimate claim of entitlement to continued utility service within the due process clause of the Fourteenth Amendment to the United States Constitution. 436 U.S. 1, 98 S.Ct. 1554 (1978). The *Memphis* appellants experienced extreme difficulty in having a duplicate meter removed from their home and in dealing with the duplicate bills that arose from that situation. In other words, the billing for their service was disputed. Tennessee law required that a utility could only terminate service if there was just cause. 436 U.S. at 11, 98 S.Ct. at 1560. Ultimately, the appellants' service was shut off for nonpayment even though the bill was disputed. 436 U.S. at 2, 98 S.Ct. at 1559-61. The Court further determined that the appellants were entitled to notice and hearing, and that the utility's

failure to make those provisions amounted to a deprivation of property without due process of law. 436 U.S. at 21, 98 S.Ct. at 1567. There are numerous federal court cases in accord with this finding. But OCC cites a plethora of them in its brief. *See* OCC Merit Brief at 23. OCC cites no case supporting the proposition that it raises here.

There is no threat of unjust service termination involved in this matter. The nature of the so-called “entitlement” that OCC argues is not of the same character as wrongful termination of gas, water, or electric service. Wrongful termination of utility service can threaten the life and livelihood of an individual or business. *See Donnelly v. City of Eureka*, 399 F.Supp. 64, 67-68 (N.D. Kansas 1975). Utility services are life-sustaining services. Energy conservation is not. It is not, as the U.S. Supreme Court stated in *Board of Regents of State Colleges v. Roth*, a claim “upon which people rely in their daily lives, reliance that must not be arbitrarily undermined.” 408 U.S. 564, 576, 92 S.Ct. 2701 (1972).

Ohio Revised Code Title 49 is a comprehensive regulatory scheme that includes due process protections for customers and utilities alike. The provisions that are in part the subject of this appeal, that is notice, were followed in this case. There was no denial of due process. *See supra* at 16. The Revised Code provisions that OCC mistakenly and improperly (*see infra* at 26-31) brought to the Court, R.C. 4905.70 and 4929.02(A)(4), are policy guidelines and this Court recognized them as such in *Ohio Partners*, but they are not a claim “upon which people rely in their daily lives.” Utility sponsored conservation programs, are not of the same nature as protections from wrongful termination of utility service.

In addition, the Commission's order does not deny the benefit of conservation to Vectren's customers. The Commission specifically found based on record evidence that:

[c]ustomers will not be misled into believing that reductions in consumption will allow them to avoid the fixed costs of the distribution system.... However, the commodity portion of a customer's bill, the actual cost of gas the gas used [sic], will remain the biggest driver of the bill. In fact, commodity costs comprise 75 to 80 percent of the total bill (Tr. III at 68). *Therefore, we believe that the gas usage will still have the biggest influence on the price signals received by customers when making gas consumption decisions and that customers will still receive the appropriate benefits of any conservation efforts.*

In re Vectren (Opinion and Order at 12) (January 7, 2009), OCC Supp. at 233. OCC relies on what the Commission found to be an inappropriate price signal, one that would disguise the true cost of gas delivery service, cause utilities to under-recover their cost of service, and mislead consumers into basing their conservation decisions on avoidance of fixed costs for which they are responsible. OCC's argument should be denied.

Proposition of Law No. III:

Where appellants fail to raise specific grounds for rehearing before the Commission or specific errors to this Court in a notice of appeal, the Court lacks jurisdiction to consider those arguments. Ohio Rev. Code Ann. § 4903.10 (West 2009), App. at 1; Ohio Rev. Code Ann. § 4903.13 (West 2009), App. at 2; *Consumers' Counsel v. Pub. Util. Comm'n*, 114 Ohio St. 3d 340, 349, 872 N.E.2d 269, 278 (2007).

A. OCC's violation of due process arguments and argument that R.C. 4909.18 and R.C. 4909.19 are jurisdictional requirements are not properly before the Court.

For the first time at any stage of this proceeding, OCC raised a number of arguments before this Court under its first and second propositions of law. OCC introduced the theory that an alleged failure of notice occurred in the case below that violated residential customers' right to due process in protection of their property interest in savings to be achieved through conservation. OCC Merit Brief at 18-33. Additionally, OCC claims for the first time that the notice required by R.C. 4909.18 and R.C. 4909.19 is a jurisdictional requirement not met in the case below. None of these arguments were specifically set forth in either OCC's application for rehearing to the Commission or its notice of appeal to this Court. As a result, these untimely arguments should be rejected by the Court.

OCC's application for rehearing sets forth only a broad, general claim in the second assignment of error that "[t]he Commission erred by failing to provide adequate notice of the second stage rate increases to the customers of Vectren, violating customers' due process rights under the 14th Amendment to the Constitution." OCC Application for Rehearing at 10-11 (February 6, 2009), Sec. Supp. at 44-45. In the application for rehear-

ing's discussion of this alleged error, all that is mentioned is the alleged failure of notice impaired customers' ability to decide if they should challenge or object to the matter. OCC then stated in its request for rehearing that "customers' rights to due process in the form of an opportunity to be heard were violated." *Id.* at 11, Sec. Supp. at 45.

In contrast, OCC's merit brief argues at great length that "[w]here a utility fails to provide adequate notice in a rate related proceeding and the customers' *property interests*, established by statute, rules, or understandings are implicated, the customers' due process rights are violated." OCC Merit Brief at 18-28 (emphasis added). Further, through OCC's several sub-propositions of law in this section, OCC attempts to explain why due process is necessary and how the alleged *property interest* was created. None of the arguments regarding the alleged "*property interest*" found in OCC's second proposition of law appear in OCC's application for rehearing. Similarly, none of these arguments are contained in OCC's notice of appeal. The only due process related error claimed in OCC's notice of appeal is simply that "[t]he PUCO's [sic] erred in unlawfully approving the utility's proposed straight fixed variable rate design when the utility failed to provide adequate legal notice of the rate design, violating VEDO's [Vectren's] residential customers' due process rights under the 14th Amendment to the Constitution." OCC Notice of Appeal at 2. OCC's failure to specifically set forth its grounds appealed from and the underlying arguments in either its application for rehearing or its notice of appeal is fatal to this Court's consideration of the arguments.

Similarly, OCC's merit brief presents arguments that R.C. 4909.18 and R.C.4909.19 are jurisdictional requirements that were not met by Vectren's notice. OCC

Merit Brief at 16-18. Just as the arguments discussed above, these jurisdictional arguments were not brought before the Commission in OCC's application for rehearing, nor were they raised to this Court in OCC's notice of appeal. As a consequence, these arguments are not properly before this Court.

In *Ohio Partners for Affordable Energy v. Pub. Util. Comm'n*, the Court found that "[a]ccording to R.C. 4903.10, rehearing applications 'shall set forth specifically the ground or grounds on which the applicant considers the order to be unreasonable or unlawful.' The court held:

in *Consumers' Counsel v. Pub. Util. Comm'n*, 70 Ohio St. 3d 244,247, 638 N.E. 2d 550 (1994), that 'setting forth specific grounds for rehearing is a jurisdictional prerequisite for our review.' " 115 Ohio St. 3d 208, 210-211, 874 N.E.2d 764, 768 (2007). (emphasis added).

OCC failed to set forth these specific grounds for rehearing just as the appellant did in *Ohio Partners*, where the appellant argued in its merit brief that the Commission failed to meet a number of Ohio Administrative Code requirements in handling the Dominion East Ohio Gas Company's application for an exemption from certain Revised Code provisions. *Ohio Partners*, 115 Ohio St. 3d at 211, 874 N.E.2d at 768. The Court recognized that Ohio Partners' failure to raise any of the arguments related to the Administrative Code procedure in its application for rehearing meant that the Court was precluded from entertaining the arguments on appeal. *Id.* Further, the Court in *Ohio Partners* determined that where, as is the case here, the appellant failed to include the arguments found in its brief in its notice of appeal, the Court was also constrained by

R.C. 4903.13 and lacked “jurisdiction to consider arguments not included in a notice of appeal.” *Id.*

The Court has strictly construed the specificity test set forth in R.C. 4903.10, in finding that “appellants’ grounds for rehearing allege nothing more than broad, general claims, and they failed to set forth specifically the same errors alleged in their ... proposition of law.” *Discount Cellular, Inc. et al. v. Pub. Util. Comm’n*, 112 Ohio St. 3d 360, 374-376, 859 N.E.2d 957, 971-972 (2007). In *Discount Cellular*, the appellant failed to specifically set forth the issues it raised in its seventh proposition of law in its application for rehearing instead; the appellant only broadly stated that the Commission failed to hold a hearing under R.C. 4905.26. *Id.* That is all OCC did in this case.

The Court also addressed its lack of jurisdiction over an improperly raised allegation of a failure of due process in *City of Akron, et al. v. Pub. Util. Comm’n*, 55 Ohio St. 2d 155, 161-162, 378 N.E.2d 480, 484-485 (1978). In *Akron* a number of municipalities appealed an order of the Commission approving an electric utility’s rate increase based on a stipulation between the company and the Commission’s Staff. *Id.* The appellant cities asserted that parties to a stipulation cannot bypass this Court’s authority by agreeing to reopen the case before the Commission if the order is overturned, and that this is a further violation of due process given that utilities are not required to refund monies collected when a rate order is subsequently overturned on appeal. *Id.* The *Akron* Court found that this proposition was neither asserted in the appellants’ application for rehearing, nor in their notice of appeal to the Court and could not be considered on appeal. As a consequence of OCC raising these due process arguments without mentioning them in

either the application for rehearing or the notice of appeal, OCC's arguments must be dismissed.

B. Arguments concerning R.C. 4905.70 and R.C. 4929.02 were not contained in OCC's notice of appeal and must be rejected.

OCC's fourth proposition of law asserts that "[t]he PUCO violated R.C. 4929.02 and R.C. 4905.70" and second proposition of law, part C, argues that "R.C. 4905.70 and 4929.02(A)(4), along with customer funding and customer participation in past DSM programs, have created a property interest protected by the due process clause." OCC Merit Brief at 24, 33. None of OCC's four errors alleged in their notice of appeal even mentions R.C. 4905.70 or R.C. 4929.02, or the concept of a *property interest*. As discussed above and as determined by the Court in *Consumers' Counsel v. Pub. Util. Comm'n*, where "OCC also failed to set forth this specific issue in its notice of appeal to this court, this failure precludes ... [the Court from] considering the issue. 114 Ohio St. 3d 340, 349, 872 N.E.2d 269, 278 (2007); R.C. 4903.13; *Cincinnati Gas & Electric Co. v. Pub. Util. Comm.*, 103 Ohio St.3d 398, 2004-Ohio-5466, 816 N.E.2d 238, at para. 21." For the same reasons, this Court should also reject OCC's second proposition, part C, and fourth proposition of law.

C. OCC's failure to timely raise an issue regarding R.C. 4909.18(E) prevents the Court from considering the argument.

OCC again raises a new argument without having mentioned it either in its application for rehearing or notice of appeal. OCC refers to language in the notice that

informs interested persons that “[a]ny person . . . may file, pursuant to Section 4909.19 of the Revised Code, an objection to such proposed increased rates by alleging that such proposals are unjust and discriminatory or unreasonable.” OCC Merit Brief at 13. OCC claims this language “was not ‘prominently displayed’ as required by R.C. 4909.18(E).” *Id.*

First, on behalf of residential customers, OCC filed numerous objections with the Commission on July 16, 2008. Thereby residential customers did in fact object to the Staff Report of Investigation. Second, OCC never raised this objection before the Commission and as with those previously discussed, the Commission never had an opportunity to address OCC’s argument. As discussed above, R.C. 4903.10 mandates that rehearing applications “set forth specifically the ground or grounds on which the applicant considers the order to be unreasonable or unlawful.” Ohio Rev. Code Ann. § 4903.10 (West 2009). This OCC failed to do. OCC also neglected to set forth this ground as one of the errors complained of in its notice of appeal. By virtue of these failures to meet the jurisdictional prerequisites of R.C. 4903.10 and R.C. 4903.13, OCC’s argument should be disregarded by this Court. *Ohio Partners*, 115 Ohio St. 3d at 211, 874 N.E.2d at 768.

CONCLUSION

The Commission’s order was reasonable and based on the manifest weight of record evidence. The published notice was approved by the Commission and lawfully given to Vectren’s residential customers. OCC failed to timely challenge the notice and

improperly raised these issues on appeal. As a result, the Commission's order should be affirmed.

Respectfully submitted,

Richard Cordray (0038034)
Ohio Attorney General

Duane W. Luckey (0023557)
Section Chief



Anne L. Hammerstein (0022867)
Counsel of Record

Werner L. Margard III (0024858)
Assistant Attorneys General

Public Utilities Section
180 East Broad Street, 6th Fl
Columbus, OH 43215-3793
614.466.4397 (telephone)
614.644.8764 (fax)

duane.luckey@puc.state.oh.us

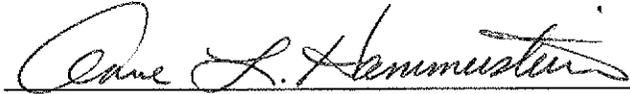
anne.hammerstein@puc.state.oh.us

werner.margard@puc.state.oh.us

**Counsel for Appellee,
The Public Utilities Commission of Ohio**

PROOF OF SERVICE

I hereby certify that a true copy of the foregoing **Merit Brief**, submitted on behalf of appellee, the Public Utilities Commission of Ohio, was served by regular U.S. mail, postage prepaid, or hand-delivered, upon the following parties of record, this 3rd day of December, 2009.



Anne L. Hammerstein
Assistant Attorney General

Parties of Record:

Janine L. Migden-Ostrander

Consumers' Counsel

Maureen R. Grady

Counsel of Record

Joseph P. Serio

Michael E. Idzkowski

Assistant Consumers' Counsel

10 West Broad Street, Suite 1800

Columbus, OH 43215-3485

grady@occ.state.oh.us

serio@occ.state.oh.us

idzkowski@occ.state.oh.us

Samuel C. Randazzo

Counsel of Record

Gretchen J. Hummel

Lisa J. McAlister

McNees Wallace & Nurick LLC

21 East State Street, 17th Floor

Columbus, OH 43215

sam@mwncmh.com

ghummel@mwncmh.com

lmcalister@mwncmh.com

APPENDIX

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4903.10 Application for rehearing.

After any order has been made by the public utilities commission, any party who has entered an appearance in person or by counsel in the proceeding may apply for a rehearing in respect to any matters determined in the proceeding. Such application shall be filed within thirty days after the entry of the order upon the journal of the commission.

Notwithstanding the preceding paragraph, in any uncontested proceeding or, by leave of the commission first had in any other proceeding, any affected person, firm, or corporation may make an application for a rehearing within thirty days after the entry of any final order upon the journal of the commission. Leave to file an application for rehearing shall not be granted to any person, firm, or corporation who did not enter an appearance in the proceeding unless the commission first finds:

(A) The applicant's failure to enter an appearance prior to the entry upon the journal of the commission of the order complained of was due to just cause; and,

(B) The interests of the applicant were not adequately considered in the proceeding.

Every applicant for rehearing or for leave to file an application for rehearing shall give due notice of the filing of such application to all parties who have entered an appearance in the proceeding in the manner and form prescribed by the commission.

Such application shall be in writing and shall set forth specifically the ground or grounds on which the applicant considers the order to be unreasonable or unlawful. No party shall in any court urge or rely on any ground for reversal, vacation, or modification not so set forth in the application.

Where such application for rehearing has been filed before the effective date of the order as to which a rehearing is sought, the effective date of such order, unless otherwise ordered by the commission, shall be postponed or stayed pending disposition of the matter by the commission or by operation of law. In all other cases the making of such an application shall not excuse any person from complying with the order, or operate to stay or postpone the enforcement thereof, without a special order of the commission.

Where such application for rehearing has been filed, the commission may grant and hold such rehearing on the matter specified in such application, if in its judgment sufficient reason therefor is made to appear. Notice of such rehearing shall be given by regular mail to all parties who have entered an appearance in the proceeding.

If the commission does not grant or deny such application for rehearing within thirty days from the date of filing thereof, it is denied by operation of law.

If the commission grants such rehearing, it shall specify in the notice of such granting the purpose for which it is granted. The commission shall also specify the scope of the additional evidence, if any, that will be taken, but it shall not upon such rehearing take any evidence that, with reasonable diligence, could have been offered upon the original hearing.

If, after such rehearing, the commission is of the opinion that the original order or any part thereof is in any respect unjust or unwarranted, or should be changed, the commission may abrogate or modify the same; otherwise such order shall be affirmed. An order made after such rehearing, abrogating or modifying the original order, shall have the same effect as an original order, but shall not affect any right or the enforcement of any right arising from or by virtue of the original order prior to the receipt of notice by the affected party of the filing of the application for rehearing.

No cause of action arising out of any order of the commission, other than in support of the order, shall accrue in any court to any person, firm, or corporation unless such person, firm, or corporation has made a proper application to the commission for a rehearing.

4903.13 Reversal of final order - notice of appeal.

A final order made by the public utilities commission shall be reversed, vacated, or modified by the supreme court on appeal, if, upon consideration of the record, such court is of the opinion that such order was unlawful or unreasonable.

The proceeding to obtain such reversal, vacation, or modification shall be by notice of appeal, filed with the public utilities commission by any party to the proceeding before it, against the commission, setting forth the order appealed from and the errors complained of. The notice of appeal shall be served, unless waived, upon the chairman of the commission, or, in the event of his absence, upon any public utilities commissioner, or by leaving a copy at the office of the commission at Columbus. The court may permit any interested party to intervene by cross-appeal.

4905.26 Complaints as to service.

Upon complaint in writing against any public utility by any person, firm, or corporation, or upon the initiative or complaint of the public utilities commission, that any rate, fare, charge, toll, rental, schedule, classification, or service, or any joint rate, fare, charge, toll, rental, schedule, classification, or service rendered, charged, demanded, exacted, or proposed to be rendered, charged, demanded, or exacted, is in any respect unjust, unreasonable, unjustly discriminatory, unjustly preferential, or in violation of law,

or that any regulation, measurement, or practice affecting or relating to any service furnished by the public utility, or in connection with such service, is, or will be, in any respect unreasonable, unjust, insufficient, unjustly discriminatory, or unjustly preferential, or that any service is, or will be, inadequate or cannot be obtained, and, upon complaint of a public utility as to any matter affecting its own product or service, if it appears that reasonable grounds for complaint are stated, the commission shall fix a time for hearing and shall notify complainants and the public utility thereof. Such notice shall be served not less than fifteen days before hearing and shall state the matters complained of. The commission may adjourn such hearing from time to time.

The parties to the complaint shall be entitled to be heard, represented by counsel, and to have process to enforce the attendance of witnesses.

Upon the filing of a complaint by one hundred subscribers or five per cent of the subscribers to any telephone exchange, whichever number be smaller, or by the legislative authority of any municipal corporation served by such telephone company that any regulation, measurement, standard of service, or practice affecting or relating to any service furnished by the telephone company, or in connection with such service is, or will be, in any respect unreasonable, unjust, discriminatory, or preferential, or that any service is, or will be, inadequate or cannot be obtained, the commission shall fix a time for the hearing of such complaint.

The hearing provided for in the next preceding paragraph shall be held in the county wherein resides the majority of the signers of such complaint, or wherein is located such municipal corporation. Notice of the date, time of day, and location of the hearing shall be served upon the telephone company complained of, upon each municipal corporation served by the telephone company in the county or counties affected, and shall be published for not less than two consecutive weeks in a newspaper of general circulation in the county or counties affected.

Such hearing shall be held not less than fifteen nor more than thirty days after the second publication of such notice.

4905.70 Energy conservation programs.

The public utilities commission shall initiate programs that will promote and encourage conservation of energy and a reduction in the growth rate of energy consumption, promote economic efficiencies, and take into account long-run incremental costs. Notwithstanding sections 4905.31, 4905.33, 4905.35, and 4909.151 of the Revised Code, the commission shall examine and issue written findings on the declining block rate structure, lifeline rates, long-run incremental pricing, peak load and off-peak pricing, time of day and seasonal pricing, interruptible load pricing, and single rate pricing where

rates do not vary because of classification of customers or amount of usage. The commission, by a rule adopted no later than October 1, 1977, and effective and applicable no later than November 1, 1977, shall require each electric light company to offer to such of their residential customers whose residences are primarily heated by electricity the option of their usage being metered by a demand or load meter. Under the rule, a customer who selects such option may be required by the company, where no such meter is already installed, to pay for such meter and its installation. The rule shall require each company to bill such of its customers who select such option for those kilowatt hours in excess of a prescribed number of kilowatt hours per kilowatt of billing demand, at a rate per kilowatt hour that reflects the lower cost of providing service during off-peak periods.

4909.15 Fixation of reasonable rate.

(A) The public utilities commission, when fixing and determining just and reasonable rates, fares, tolls, rentals, and charges, shall determine:

(1) The valuation as of the date certain of the property of the public utility used and useful in rendering the public utility service for which rates are to be fixed and determined. The valuation so determined shall be the total value as set forth in division (J) of section 4909.05 of the Revised Code, and a reasonable allowance for materials and supplies and cash working capital, as determined by the commission.

The commission, in its discretion, may include in the valuation a reasonable allowance for construction work in progress but, in no event, may such an allowance be made by the commission until it has determined that the particular construction project is at least seventy-five per cent complete.

In determining the percentage completion of a particular construction project, the commission shall consider, among other relevant criteria, the per cent of time elapsed in construction; the per cent of construction funds, excluding allowance for funds used during construction, expended, or obligated to such construction funds budgeted where all such funds are adjusted to reflect current purchasing power; and any physical inspection performed by or on behalf of any party, including the commission's staff.

A reasonable allowance for construction work in progress shall not exceed ten per cent of the total valuation as stated in this division, not including such allowance for construction work in progress.

Where the commission permits an allowance for construction work in progress, the dollar value of the project or portion thereof included in the valuation as construction work in progress shall not be included in the valuation as plant in service until such time as the total revenue effect of the construction work in progress allowance is offset by the

total revenue effect of the plant in service exclusion. Carrying charges calculated in a manner similar to allowance for funds used during construction shall accrue on that portion of the project in service but not reflected in rates as plant in service, and such accrued carrying charges shall be included in the valuation of the property at the conclusion of the offset period for purposes of division (J) of section 4909.05 of the Revised Code.

From and after April 10, 1985, no allowance for construction work in progress as it relates to a particular construction project shall be reflected in rates for a period exceeding forty-eight consecutive months commencing on the date the initial rates reflecting such allowance become effective, except as otherwise provided in this division.

The applicable maximum period in rates for an allowance for construction work in progress as it relates to a particular construction project shall be tolled if, and to the extent, a delay in the in-service date of the project is caused by the action or inaction of any federal, state, county, or municipal agency having jurisdiction, where such action or inaction relates to a change in a rule, standard, or approval of such agency, and where such action or inaction is not the result of the failure of the utility to reasonably endeavor to comply with any rule, standard, or approval prior to such change.

In the event that such period expires before the project goes into service, the commission shall exclude, from the date of expiration, the allowance for the project as construction work in progress from rates, except that the commission may extend the expiration date up to twelve months for good cause shown.

In the event that a utility has permanently canceled, abandoned, or terminated construction of a project for which it was previously permitted a construction work in progress allowance, the commission immediately shall exclude the allowance for the project from the valuation.

In the event that a construction work in progress project previously included in the valuation is removed from the valuation pursuant to this division, any revenues collected by the utility from its customers after April 10, 1985, that resulted from such prior inclusion shall be offset against future revenues over the same period of time as the project was included in the valuation as construction work in progress. The total revenue effect of such offset shall not exceed the total revenues previously collected.

In no event shall the total revenue effect of any offset or offsets provided under division (A)(1) of this section exceed the total revenue effect of any construction work in progress allowance.

(2) A fair and reasonable rate of return to the utility on the valuation as determined in division (A)(1) of this section;

(3) The dollar annual return to which the utility is entitled by applying the fair and reasonable rate of return as determined under division (A)(2) of this section to the valuation of the utility determined under division (A)(1) of this section;

(4) The cost to the utility of rendering the public utility service for the test period less the total of any interest on cash or credit refunds paid, pursuant to section 4909.42 of the Revised Code, by the utility during the test period.

(a) Federal, state, and local taxes imposed on or measured by net income may, in the discretion of the commission, be computed by the normalization method of accounting, provided the utility maintains accounting reserves that reflect differences between taxes actually payable and taxes on a normalized basis, provided that no determination as to the treatment in the rate-making process of such taxes shall be made that will result in loss of any tax depreciation or other tax benefit to which the utility would otherwise be entitled, and further provided that such tax benefit as redounds to the utility as a result of such a computation may not be retained by the company, used to fund any dividend or distribution, or utilized for any purpose other than the defrayal of the operating expenses of the utility and the defrayal of the expenses of the utility in connection with construction work.

(b) The amount of any tax credits granted to an electric light company under section 5727.391 of the Revised Code for Ohio coal burned prior to January 1, 2000, shall not be retained by the company, used to fund any dividend or distribution, or utilized for any purposes other than the defrayal of the allowable operating expenses of the company and the defrayal of the allowable expenses of the company in connection with the installation, acquisition, construction, or use of a compliance facility. The amount of the tax credits granted to an electric light company under that section for Ohio coal burned prior to January 1, 2000, shall be returned to its customers within three years after initially claiming the credit through an offset to the company's rates or fuel component, as determined by the commission, as set forth in schedules filed by the company under section 4905.30 of the Revised Code. As used in division (A)(4)(c) of this section, "compliance facility" has the same meaning as in section 5727.391 of the Revised Code.

(B) The commission shall compute the gross annual revenues to which the utility is entitled by adding the dollar amount of return under division (A)(3) of this section to the cost of rendering the public utility service for the test period under division (A)(4) of this section.

(C) The test period, unless otherwise ordered by the commission, shall be the twelve-month period beginning six months prior to the date the application is filed and ending six months subsequent to that date. In no event shall the test period end more than nine months subsequent to the date the application is filed. The revenues and expenses of

the utility shall be determined during the test period. The date certain shall be not later than the date of filing.

(D) When the commission is of the opinion, after hearing and after making the determinations under divisions (A) and (B) of this section, that any rate, fare, charge, toll, rental, schedule, classification, or service, or any joint rate, fare, charge, toll, rental, schedule, classification, or service rendered, charged, demanded, exacted, or proposed to be rendered, charged, demanded, or exacted, is, or will be, unjust, unreasonable, unjustly discriminatory, unjustly preferential, or in violation of law, that the service is, or will be, inadequate, or that the maximum rates, charges, tolls, or rentals chargeable by any such public utility are insufficient to yield reasonable compensation for the service rendered, and are unjust and unreasonable, the commission shall:

(1) With due regard among other things to the value of all property of the public utility actually used and useful for the convenience of the public as determined under division (A)(1) of this section, excluding from such value the value of any franchise or right to own, operate, or enjoy the same in excess of the amount, exclusive of any tax or annual charge, actually paid to any political subdivision of the state or county, as the consideration for the grant of such franchise or right, and excluding any value added to such property by reason of a monopoly or merger, with due regard in determining the dollar annual return under division (A)(3) of this section to the necessity of making reservation out of the income for surplus, depreciation, and contingencies, and;

(2) With due regard to all such other matters as are proper, according to the facts in each case,

(a) Including a fair and reasonable rate of return determined by the commission with reference to a cost of debt equal to the actual embedded cost of debt of such public utility,

(b) But not including the portion of any periodic rental or use payments representing that cost of property that is included in the valuation report under divisions (F) and (G) of section 4909.05 of the Revised Code, fix and determine the just and reasonable rate, fare, charge, toll, rental, or service to be rendered, charged, demanded, exacted, or collected for the performance or rendition of the service that will provide the public utility the allowable gross annual revenues under division (B) of this section, and order such just and reasonable rate, fare, charge, toll, rental, or service to be substituted for the existing one. After such determination and order no change in the rate, fare, toll, charge, rental, schedule, classification, or service shall be made, rendered, charged, demanded, exacted, or changed by such public utility without the order of the commission, and any other rate, fare, toll, charge, rental, classification, or service is prohibited.

(E) Upon application of any person or any public utility, and after notice to the parties in interest and opportunity to be heard as provided in Chapters 4901., 4903., 4905., 4907., 4909., 4921., and 4923. of the Revised Code for other hearings, has been given, the commission may rescind, alter, or amend an order fixing any rate, fare, toll, charge, rental, classification, or service, or any other order made by the commission. Certified copies of such orders shall be served and take effect as provided for original orders.

4909.18 Application to establish or change rate.

Any public utility desiring to establish any rate, joint rate, toll, classification, charge, or rental, or to modify, amend, change, increase, or reduce any existing rate, joint rate, toll, classification, charge, or rental, or any regulation or practice affecting the same, shall file a written application with the public utilities commission. Except for actions under section 4909.16 of the Revised Code, no public utility may issue the notice of intent to file an application pursuant to division (B) of section 4909.43 of the Revised Code to increase any existing rate, joint rate, toll, classification, charge, or rental, until a final order under this section has been issued by the commission on any pending prior application to increase the same rate, joint rate, toll, classification, charge, or rental or until two hundred seventy-five days after filing such application, whichever is sooner. Such application shall be verified by the president or a vice-president and the secretary or treasurer of the applicant. Such application shall contain a schedule of the existing rate, joint rate, toll, classification, charge, or rental, or regulation or practice affecting the same, a schedule of the modification amendment, change, increase, or reduction sought to be established, and a statement of the facts and grounds upon which such application is based. If such application proposes a new service or the use of new equipment, or proposes the establishment or amendment of a regulation, the application shall fully describe the new service or equipment, or the regulation proposed to be established or amended, and shall explain how the proposed service or equipment differs from services or equipment presently offered or in use, or how the regulation proposed to be established or amended differs from regulations presently in effect. The application shall provide such additional information as the commission may require in its discretion. If the commission determines that such application is not for an increase in any rate, joint rate, toll, classification, charge, or rental, the commission may permit the filing of the schedule proposed in the application and fix the time when such schedule shall take effect. If it appears to the commission that the proposals in the application may be unjust or unreasonable, the commission shall set the matter for hearing and shall give notice of such hearing by sending written notice of the date set for the hearing to the public utility and publishing notice of the hearing one time in a newspaper of general circulation in each county in the service area affected by the application. At such hearing, the burden of proof to show that the proposals in the application are just and reasonable shall be upon

the public utility. After such hearing, the commission shall, where practicable, issue an appropriate order within six months from the date the application was filed.

If the commission determines that said application is for an increase in any rate, joint rate, toll, classification, charge, or rental there shall also, unless otherwise ordered by the commission, be filed with the application in duplicate the following exhibits:

(A) A report of its property used and useful in rendering the service referred to in such application, as provided in section 4909.05 of the Revised Code;

(B) A complete operating statement of its last fiscal year, showing in detail all its receipts, revenues, and incomes from all sources, all of its operating costs and other expenditures, and any analysis such public utility deems applicable to the matter referred to in said application;

(C) A statement of the income and expense anticipated under the application filed;

(D) A statement of financial condition summarizing assets, liabilities, and net worth;

(E) A proposed notice for newspaper publication fully disclosing the substance of the application. The notice shall prominently state that any person, firm, corporation, or association may file, pursuant to section 4909.19 of the Revised Code, an objection to such increase which may allege that such application contains proposals that are unjust and discriminatory or unreasonable. The notice shall further include the average percentage increase in rate that a representative industrial, commercial, and residential customer will bear should the increase be granted in full;

(F) Such other information as the commission may require in its discretion.

4909.19 Publication - investigation.

Upon the filing of any application for increase provided for by section 4909.18 of the Revised Code the public utility shall forthwith publish the substance and prayer of such application, in a form approved by the public utilities commission, once a week for three consecutive weeks in a newspaper published and in general circulation throughout the territory in which such public utility operates and affected by the matters referred to in said application, and the commission shall at once cause an investigation to be made of the facts set forth in said application and the exhibits attached thereto, and of the matters connected therewith. Within a reasonable time as determined by the commission after the filing of such application, a written report shall be made and filed with the commission, a copy of which shall be sent by certified mail to the applicant, the mayor of any municipal

corporation affected by the application, and to such other persons as the commission deems interested. If no objection to such report is made by any party interested within thirty days after such filing and the mailing of copies thereof, the commission shall fix a date within ten days for the final hearing upon said application, giving notice thereof to all parties interested. At such hearing the commission shall consider the matters set forth in said application and make such order respecting the prayer thereof as to it seems just and reasonable.

If objections are filed with the commission, the commission shall cause a pre-hearing conference to be held between all parties, intervenors, and the commission staff in all cases involving more than one hundred thousand customers.

If objections are filed with the commission within thirty days after the filing of such report, the application shall be promptly set down for hearing of testimony before the commission or be forthwith referred to an attorney examiner designated by the commission to take all the testimony with respect to the application and objections which may be offered by any interested party. The commission shall also fix the time and place to take testimony giving ten days' written notice of such time and place to all parties. The taking of testimony shall commence on the date fixed in said notice and shall continue from day to day until completed. The attorney examiner may, upon good cause shown, grant continuances for not more than three days, excluding Saturdays, Sundays, and holidays. The commission may grant continuances for a longer period than three days upon its order for good cause shown. At any hearing involving rates or charges sought to be increased, the burden of proof to show that the increased rates or charges are just and reasonable shall be on the public utility.

When the taking of testimony is completed, a full and complete record of such testimony noting all objections made and exceptions taken by any party or counsel, shall be made, signed by the attorney examiner, and filed with the commission. Prior to the formal consideration of the application by the commission and the rendition of any order respecting the prayer of the application, a quorum of the commission shall consider the recommended opinion and order of the attorney examiner, in an open, formal, public proceeding in which an overview and explanation is presented orally. Thereafter, the commission shall make such order respecting the prayer of such application as seems just and reasonable to it.

In all proceedings before the commission in which the taking of testimony is required, except when heard by the commission, attorney examiners shall be assigned by the commission to take such testimony and fix the time and place therefor, and such testimony shall be taken in the manner prescribed in this section. All testimony shall be under oath or affirmation and taken down and transcribed by a reporter and made a part of the record in the case. The commission may hear the testimony or any part thereof in any case without having the same referred to an attorney examiner and may take

additional testimony. Testimony shall be taken and a record made in accordance with such general rules as the commission prescribes and subject to such special instructions in any proceedings as it, by order, directs.

4911.15 Counsel may represent residential consumer or municipal corporation.

The consumers' counsel, at the request of one or more residential consumers residing in, or municipal corporations located in, an area served by a public utility or whenever in his opinion the public interest is served, may represent those consumers or corporations whenever an application is made to the public utilities commission by any public utility desiring to establish, modify, amend, change, increase, or reduce any rate, joint rate, toll, fare, classification, charge, or rental.

The consumers' counsel may appear before the public utilities commission as a representative of the residential consumers of any public utility when a complaint has been filed with the commission that a rate, joint rate, fare, toll, charge, classification, or rental for commodities or services rendered, charged, demanded, exacted, or proposed to be rendered, charged, demanded, or exacted by the utility is in any respect unjust, unreasonable, unjustly discriminatory, unjustly preferential, or in violation of the law.

Nothing in Chapter 4911. of the Revised Code shall be construed to restrict or limit in any manner the right of a municipal corporation to represent the residential consumers of such municipal corporation in all proceedings before the public utilities commission, and in both state and federal courts and administrative agencies on behalf of such residential consumers concerning review of decisions rendered by, or failure to act by, the public utilities commission.

4929.02 Policy of state as to natural gas services and goods.

(A) It is the policy of this state to, throughout this state:

- (1) Promote the availability to consumers of adequate, reliable, and reasonably priced natural gas services and goods;
- (2) Promote the availability of unbundled and comparable natural gas services and goods that provide wholesale and retail consumers with the supplier, price, terms, conditions, and quality options they elect to meet their respective needs;
- (3) Promote diversity of natural gas supplies and suppliers, by giving consumers effective choices over the selection of those supplies and suppliers;

- (4) Encourage innovation and market access for cost-effective supply- and demand-side natural gas services and goods;
 - (5) Encourage cost-effective and efficient access to information regarding the operation of the distribution systems of natural gas companies in order to promote effective customer choice of natural gas services and goods;
 - (6) Recognize the continuing emergence of competitive natural gas markets through the development and implementation of flexible regulatory treatment;
 - (7) Promote an expeditious transition to the provision of natural gas services and goods in a manner that achieves effective competition and transactions between willing buyers and willing sellers to reduce or eliminate the need for regulation of natural gas services and goods under Chapters 4905. and 4909. of the Revised Code;
 - (8) Promote effective competition in the provision of natural gas services and goods by avoiding subsidies flowing to or from regulated natural gas services and goods;
 - (9) Ensure that the risks and rewards of a natural gas company's offering of nonjurisdictional and exempt services and goods do not affect the rates, prices, terms, or conditions of nonexempt, regulated services and goods of a natural gas company and do not affect the financial capability of a natural gas company to comply with the policy of this state specified in this section;
 - (10) Facilitate the state's competitiveness in the global economy;
 - (11) Facilitate additional choices for the supply of natural gas for residential consumers, including aggregation;
 - (12) Promote an alignment of natural gas company interests with consumer interest in energy efficiency and energy conservation.
- (B) The public utilities commission and the office of the consumers' counsel shall follow the policy specified in this section in exercising their respective authorities relative to sections 4929.03 to 4929.30 of the Revised Code.
- (C) Nothing in Chapter 4929. of the Revised Code shall be construed to alter the public utilities commission's construction or application of division (A)(6) of section 4905.03 of the Revised Code.

Effective Date: 06-26-2001; 2008 SB221 07-31-2008

BEFORE

THE PUBLIC UTILITIES COMMISSION OF OHIO

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

OPINION AND ORDER

The Commission, considering the applications, testimony, the applicable law, proposed Stipulation, and other evidence of record, and being otherwise fully advised, hereby issues its opinion and order.

APPEARANCES:

John J. Finnigan, Jr., Paul A. Colbert, and Elizabeth Watts, 139 East Fourth Street, Room 25, AT II, Cincinnati, Ohio 45201-0960, on behalf of Duke Energy Ohio, Inc.

Janine Migden-Ostrander, The Office of Ohio Consumers' Counsel, by Larry Sauer, Joseph Serio, and Michael Idzkowski, Assistant Consumers' Counsel, 10 West Broad Street, 18th Floor, Columbus, Ohio 43215-3485, on behalf of the residential consumers of Duke Energy Ohio, Inc.

David C. Rinebolt and Colleen Mooney, 231 West Lima Street, Findlay, Ohio 45840-3033, on behalf of Ohio Partners for Affordable Energy.

Bricker & Eckler LLP, by Thomas J. O'Brien, 100 South Third Street, Columbus, Ohio 43215-4236, on behalf of the city of Cincinnati.

Boehm, Kurtz & Lowry, by David F. Boehm and Michael L. Kurtz, 36 East Seventh Street, Suite 1510, Cincinnati, Ohio 45202, on behalf of Ohio Energy Group and The Kroger Company.

Chester, Wilcox & Saxbe, LLP, by John W. Bentine, 65 East State Street, Suite 1000, Columbus, Ohio 43215-4213, on behalf of Interstate Gas Supply, Inc.

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Vorys, Sater, Seymour and Pease LLP, by M. Howard Petricoff and Stephen M. Howard, 52 Gay State Street, P.O. Box 1008, Columbus, Ohio 43215, on behalf of Direct Energy Services, LLC and Integrys Energy Services, Inc.

Christensen, Christensen, Donchatz, Kettlewell & Owens, LLC, by Mary W. Christensen and Jason Wells, 100 East Campus View Blvd., Suite 360, Columbus, Ohio 43235, on behalf of People Working Cooperatively, Inc.

John M. Dosker, 1077 Celestial Street, Suite 110, Cincinnati, Ohio 45202-1629, on behalf of Stand Energy Corporation.

Thomas R. Winters, First Assistant Attorney General, by Duane W. Luckey, Section Chief, and William L. Wright and Thomas Lindgren, Assistant Attorneys General, Public Utilities Section, 180 East Broad Street, 9th Floor, Columbus, Ohio 43215, on behalf of the Staff of the Public Utilities Commission of Ohio.

OPINION:

I. PROCEDURAL BACKGROUND

Duke Energy Ohio, Inc. (Duke, company) is a public utility, engaged in the distribution and sale of natural gas to approximately 424,000 customers in Adams, Brown, Butler, Clermont, Clinton, Hamilton, Highland, Montgomery, and Warren counties, Ohio. As a public utility and a natural gas company within the definition of Sections 4905.02 and 4905.03(A)(6), Revised Code, Duke is subject to the jurisdiction of this Commission in accordance with Sections 4905.04, 4905.05 and 4905.06, Revised Code.

On June 18, 2007, Duke filed notice of its intent to file an application to increase its rates. The Commission issued an entry on July 11, 2007, establishing a test period of January 1, 2007 through December 31, 2007 for the proposed rate increase and a date certain of March 31, 2007, as well as granting certain waivers requested by Duke.

Duke filed the application in Case No. 07-589-GA-AIR, seeking to increase its gas rates on July 18, 2007. Duke also filed separate applications for approval of an alternative rate plan (Case No. 07-590-GA-ALT) and for approval to change accounting methods (Case No. 07-591-GA-AAM). As originally filed, Duke's rate increase application sought approval for a 5.71 percent annual rate increase, an additional \$34 million, over current total adjusted operating revenues. As part of the alternative rate plan application, Duke proposes to: (a) extend the term of the Accelerated Main Replacement Program (AMRP) and the associated rider (Rider AMRP) through the year 2019, (b) establish a process to recover its future investment in Duke's Utility of the Future initiative through a new rider

(Rider AU), and (c) create a new sales decoupling rider (Rider SD) to remove any disincentive for energy conservation initiatives. In the accounting application, Duke seeks approval to defer certain costs to be recovered later as a part of the AMRP expenditures and to capitalize the cost incurred for certain property relocations and replacements.

By entry issued September 5, 2007, the Commission found that Duke's application in Case No. 07-589-GA-AIR complied with the requirements of Section 4909.18, Revised Code, and Rule 4901:1-19-05, Ohio Administrative Code (O.A.C.) and accepted the application for filing as of July 18, 2007. The entry also granted Duke's waiver requests as to certain standard filing requirements and directed Duke to publish notice of the application in newspapers of general circulation in the company's service territory. Duke filed proof of such publication on February 25, 2007. To provide interested parties with an opportunity to make inquiries about the Duke applications, a technical conference was hosted by the Commission's staff on August 20, 2007.

Motions to intervene in these cases were granted to the Ohio Energy Group (OEG), the Kroger Company (Kroger), Interstate Gas Supply, Inc. (Interstate), the city of Cincinnati, the office of the Ohio Consumers' Counsel (OCC), People Working Cooperatively, Inc. (PWC), Integrys Energy Services, Inc. (Integrys), Direct Energy Services, LLC (Direct), Stand Energy Corporation (Stand), and the Ohio Partners for Affordable Energy (OPAE).

Investigations of Duke's applications were conducted and reports filed by the Commission staff and Blue Ridge Consulting Services, Inc. (Blue Ridge), an independent auditing firm. Both the report filed by staff (Staff Report, Staff Ex. 1) and financial audit report filed by Blue Ridge (financial audit report, Staff Ex. 4) were filed on December 20, 2007. Objections to the Staff Report and/or financial audit report were filed by PWC, OEG, Duke, OPAE, OCC, and, jointly, by Integrys and Direct. Motions to strike certain objections were filed by Duke and OCC. Memoranda contra the motions to strike objections were filed by Duke, Interstate, OPAE, and, jointly, by Integrys and Direct.

On January 25, 2008, a prehearing conference was held, as required by Section 4909.19, Revised Code. In accordance with Section 4903.083, Revised Code, local public hearings were held on February 25, 2008, in Cincinnati, Ohio, and on March 11, 2008, in Mason, Ohio.

A total of 27 witnesses testified at the two local hearings in Cincinnati, while four people took the stand at the Mason hearing. Two witnesses testified in favor of the rate increase, particularly as to the accelerated main replacement (AMRP) and riser replacement programs. Another witness testified that, although he was not opposed to the rate increase if Duke required additional money to maintain the gas lines, he was opposed to the extent that the increase is incorporated into the monthly customer charge as

opposed to the volumetric charge. The witness claimed that applying the increase in such a manner discourages energy efficiency and adversely affects residential customers with small homes (Cincinnati Public Hearing I, p. 20-21). The remaining witnesses at the local public hearings were opposed to the increase, asserting that their utility bills are already expensive, particularly for individuals on fixed incomes and for low income individuals and families; while others argued that increasing the customer charge, as proposed, would discourage conservation.

The evidentiary hearing was called on February 26, 2008, and continued, to allow the parties additional time to negotiate a settlement of the issues in these proceedings. On February 28, 2008, the parties filed a Joint Stipulation and Recommendation (Stipulation, Joint Ex. 1) resolving all the issues except the adoption of a new residential rate design. The evidentiary hearing was reconvened on March 5 and March 6, 2008. Duke and staff filed the testimony of Paul G. Smith (Duke Ex. 29) and of J. Edward Hess (Staff Ex. 2), in support of the Stipulation. With respect to the unresolved issue of residential rate design, Duke presented witnesses James A. Riddle (Duke Exs. 10 and 25), Paul G. Smith (Duke Exs. 11 and 19), Donald L. Stork (Duke Exs. 13, 20, and 22), and James E. Ziokowski (Duke Ex. 16); OCC called Wilson Gonzalez (OCC Exs. 5 and 18) and Anthony J. Yankel (OCC Ex. 6 and 17); and Staff presented the testimony of Stephen E. Puican (Staff Ex. 3).

Initial briefs, in support of their respective positions, were filed by Duke, OPAE, OCC, and staff on March 17, 2008. Reply briefs were filed on March 24, 2008.

A. Duke's Motion for Protective Order

On February 21, 2008, Duke filed a motion for protective order for information attached to the direct testimony of Matthew G. Smith (Duke Ex. 27) and marked as Attachment MGS-1. Duke contends that Attachment MGS-1 contains proprietary pricing information from vendors for equipment necessary for Duke's Utility of the Future program. The company states that the information for which Duke seeks confidential treatment is not known outside of Duke and its vendors. Furthermore, Duke states that, within the company, such information is only disseminated to employees who have a legitimate business need to know and act upon such information. Accordingly, Duke considers the information to be proprietary, confidential, and trade secret, as defined in Section 1333.61, Revised Code, and requests that the information be treated as confidential in accordance with the provisions of Sections 1333.61 and 4901.16, Revised Code. No party opposed Duke's request for protective treatment of Attachment MGS-1.

The Commission recognizes that Ohio's public records law is intended to be liberally construed to ensure that governmental records are open and made available to the public, subject to only a few very limited and narrow exceptions. *State ex rel. Williams*

v. Cleveland (1992), 64 Ohio St.3d 544, 549. However, one of the exceptions is for trade secrets. Section 1333.61(D), Revised Code, defines trade secret as:

[I]nformation, including the whole or any portion or phase of any scientific or technical information, design, process, procedure, formula, pattern, compilation, program, device, method, technique, or improvement, or any business information or plans, financial information, or listing of names, addresses, or telephone numbers, that satisfies both of the following:

- (1) It derives independent economic value, actual or potential, from not being generally known to, and not being readily ascertainable by proper means by, other persons who can obtain economic value from its disclosure or use.
- (2) It is the subject of efforts that are reasonable under the circumstances to maintain its secrecy.

The Commission finds that Attachment MGS-1 is financial information that derives independent economic value from not being generally known to or readily ascertainable by proper means by others who can obtain economic value from its use and that it is subject to reasonable efforts to maintain its secrecy. Therefore, we find that it contains trade secret information, as defined under Section 1333.61(D), Revised Code, and, therefore, that it should be granted protective treatment. In accordance with Rule 4901-1-24, O.A.C., Duke's request for a protective order is granted and the information filed under seal, as Attachment MGS-1, shall be afforded protective treatment for 18 months from the date this order is issued. Any request to extend protective treatment shall be made in accordance with Rule 4901-1-24(F), O.A.C.

B. Duke's Motion for Waiver and Leave to File Depositions

On February 25, 2008, Duke filed a motion for waiver of a Commission filing requirement and leave to file depositions *instanter*. Duke states that depositions were conducted on February 21, 2008. On Friday, February 22, 2008, Duke filed notice that it would be filing the deposition transcripts of five witnesses and commenced electronic transmission of the depositions. However, Duke states that it subsequently learned that only one of the five depositions was received by the Commission's Docketing Division before the end of the business day on February 22, 2008. Accordingly, the remaining four depositions were electronically transmitted on Monday, February 25, 2008. Duke requests that the Commission waive the requirement of Rule 4901-1-21(N), O.A.C., that depositions be filed with the Commission at least three days prior to the commencement of the

hearing. In this instance, the Commission finds Duke's request to waive the requirement that deposition transcripts be filed at least three days prior to the commencement of the hearing to be reasonable. Accordingly, the request for waiver should be granted.

II. SUMMARY OF THE EVIDENCE

A. Summary of the Proposed Stipulation

The only issue not resolved by the Stipulation is the proposed residential rate design which was litigated and is expressly reserved for our determination. A new design is recommended by the Commission's staff and Duke, but opposed by OCC and OP&E. The city of Cincinnati, PWC, and the commercial and industrial intervenors take no position with respect to this issue (Jt. Ex. 1 at 5). Pursuant to the Stipulation, the parties agree, among other things, that:

- (1) Duke will receive a revenue increase of \$18,217,566, which represents a percentage increase of 3.05 percent and is based on a 8.15 percent rate of return. Duke will not be required to file the 60-day update filing of actual financial data for the test year (Jt. Ex. 1, at 5 and Stipulation Ex. 1).
- (2) Duke's revenue distribution, billing determinants, and rates to be adopted are shown on Exhibit 2 of the Stipulation, and assume the adoption of the new residential rate design. The rates also reflect the shift of \$6,000,000 to the residential class, phased-in over two years, based upon the agreed revenue requirement and Duke's updated cost of service study (*Id.* at 5; Stipulation Ex. 2).¹
- (3) Duke will amortize deferred rate case expenses requested for recovery in its filing in these cases as recommended in the Staff Report (*Id.* at 6).
- (4) Duke will implement new depreciation rates that reflect the mid-point between Duke's proposed depreciation rates and the rates proposed in the Staff Report, as shown on Stipulation Exhibit 5 (*Id.*).
- (5) The allocation of common plant related to the provision of gas distribution service will be based on an updated allocation

¹ OCC and OP&E object to the characterization of this cost reallocation as a "subsidy/excess" used in the Stipulation (*Id.* at 5, footnote 6).

factor of 18.29 percent that excludes the generation plant assets contributed to Duke by Duke Energy North America, LLC (*Id.*).

- (6) Duke will file actual data to support a Rider AMRP adjustment for the last nine months of 2007. The Rider AMRP revenue requirement will be modified to include deferred curb-to-meter expense and riser expense, net of maintenance savings, for calendar year 2007. Such net deferred expense shall be capitalized with carrying charges at an annual rate of 5.87 percent, representing the company's long-term debt rate, and recovered through Rider AMRP, beginning in this filing. Duke may elect to recover this expense in any annual Rider AMRP filings, provided that the recovery does not exceed the Rider AMRP cumulative residential rate caps. If this deferred expense causes Duke to exceed the Rider AMRP cumulative rate cap in any year, Duke may recover that portion of the deferred expense that exceeds the rate cap in a subsequent year as long as the recovery does not exceed the cumulative rate cap. The new Rider AMRP residential rates are limited on a cumulative basis as shown on Stipulation Exhibit 4, at 3, and recoverable pursuant to the Rider AMRP revenue allocation described in paragraph 9 of the Stipulation. Duke may implement these rates, effective with the beginning of the first billing cycle following issuance of the Commission's order, adjusted as necessary to permit the company full recovery of the revenue increase through May 1, 2009, subject to refund, upon Commission approval (*Id.* at 6-7).
- (7) Following the implementation of new Rider AMRP rates, Duke will file a pre-filing notice and application annually to implement subsequent adjustments to Rider AMRP, beginning in November 2008.² The annual filing will support the adjustment to Duke's revenue requirement for any increase to Rider AMRP. Duke shall continue to make its Rider AMRP annual filing until the effective date of the Commission's order in Duke's next base rate case (*Id.* at 8-9).

² Although the Stipulation directs Duke to make its annual filings in Case No. 07-589-GA-AIR, each annual review should be filed in a new case to accommodate the operational efficiencies of the Commission's Docketing Information System. These annual review cases will be linked to the instant proceedings, and Duke should serve all parties to these proceedings with each pre-filing notice and annual AMRP application.

- (8) Duke's revenue requirement calculation and Rider AMRP application filed with the Commission shall include the post-March 31, 2007 (date certain) original cost and accumulated reserve for depreciation of property associated with the AMRP program that is used and useful on December 31 of the prior year in the rendition of service as such property is associated with the AMRP and riser replacement programs, including capital expenditures for new plant (including but not limited to new mains, services and risers), adjustments for the retirement of existing assets, calculated Post-In-Service Carrying Charges ("PISCC") on net plant additions and related deferred taxes until included in rates for collection in Rider AMRP, a proper annual depreciation expense, and any sums of money or property that Duke may receive to defray the cost of property associated with the AMRP capital expenditures. The return assigned to the recovery of all such net capital expenditures shall be at a pre-tax weighted average cost of capital of 11.7 percent (*Id.* at 9-11).³
- (9) Duke will substantially complete the AMRP by the end of 2019 and will complete the riser replacement program by the end of 2012. Duke will file an application with the Commission for approval to extend the AMRP program if not substantially completed by the end of 2019 (*Id.* at 12).
- (10) Duke shall maintain its alternative regulation commitments until the effective date of the Commission's order in the company's next base rate case, except that the incremental \$1,000,000 in funding for weatherization shall be funded through base rates.⁴ If, for any reason, Duke does not expend the \$3,000,000 gas weatherization funding amount in any year, the amount not expended will be carried over to the following year and added to the annual \$3,000,000 funding to be available for distribution to weatherization projects during that year. If a weatherization service provider does not meet its contract requirements, including its failure to meet deadlines, following consultation with the Duke Energy Community Partnership (Collaborative), Duke will reprogram the remaining funding to

³ This rate of return is based on a 10.4 percent return on equity.

⁴ OCC agrees with Duke's incremental \$1 million weatherization funding; however, OCC does not agree that this out-of-test period expenditure should be collected through base rates, and asserts that this amount should instead be collected through a rider.

a different project and/or assign it to another weatherization service provider so that the funding dollars can be spent expeditiously and productively (*Id.* at 12-14).⁵

- (11) The residential rate caps on Stipulation Exhibit 4 apply to Rider AMRP. Duke may establish deferrals for the expenses of the riser replacement program if these expenses cause Duke to exceed the cumulative rate cap, including a carrying cost of 5.87 percent. The rate caps shall be cumulative rather than annual caps such that if the rate increase is below the annual cap in a given year, the unused portion of the cap may be carried forward to future years but can never exceed the cumulative cap. If the deferred curb-to-meter expense or the deferred riser replacement program expense causes Duke to exceed the cumulative rate cap in any year, then Duke may recover that portion of the deferred expense that exceeds the cumulative rate cap in a subsequent year as long as the recovery does not exceed the cumulative rate cap (*Id.* at 17).
- (12) The parties agree that Duke shall take over ownership of the curb-to-meter service, including the riser, whenever a new service line or riser is installed or whenever an existing curb-to-meter service or riser is replaced. Duke shall file its tariffs in these cases such that Duke will be responsible for the cost of initial installation, repair, replacement and maintenance of all curb-to-meter services, including risers, except that consumers shall pay the initial installation costs related to the portion of service lines in excess of 250 feet. In 2008, Duke will begin capitalizing rather than expensing the costs currently described as "Customer Owned Service Line Expense." For this purpose, Duke will submit proposed tariff changes to Staff for review and approval, with a copy to parties, prior to filing the revised sheets with the Commission. Such capitalized costs shall be recoverable through Rider AMRP (*Id.* at 12-14).⁶
- (13) Duke will file, within 60 days of the Commission's final order in this proceeding, a deployment plan for the company's Utility of the Future Program for 2008-2009 (*Id.* at 15-16).

5 The members of the Collaborative include Duke personnel and representatives of the OCC, Staff, the Hamilton County Cincinnati Community Action Agency, City of Cincinnati, and PWC.

6 Neither Direct, Interstate, nor Integrys endorse this provision of the stipulation.

- (14) Duke's base rates do not include any amount for gas storage carrying costs. On a going forward basis, Duke will recover its actual gas storage carrying costs through its gas cost recovery rider (Rider GCR), without reduction to rate base, as shown on Stipulation Exhibit 1. Carrying charges associated with the actual monthly balances of Current Gas in Storage shall be accrued at a 10 percent annual rate as shown on Stipulation Exhibit 3. Further, the parties agree that the Commission should: (a) approve the methodology for the calculation of the storage carrying costs for inclusion in the GCR rate, as demonstrated in Stipulation Exhibit 3; (b) find that such an adjustment to Duke's rates is not an increase in base rates; and (c) approve recovery of such costs in Duke's next GCR filing following the Commission's order in this proceeding (*Id.* at 16-17).
- (15) Duke shall conduct an internal audit of its method and process for allocating service company charges to Duke by no later than 2009, and shall provide the audit report to Staff and the OCC (*Id.* at 18).
- (16) Duke shall continue to use the "Participants Test" as one of the methods for evaluating its Demand Side Management/Energy Efficiency programs as appropriate; however, Duke shall continue to use other cost/benefit tests as the Collaborative deems appropriate (*Id.* at 19).
- (17) Duke will implement a pilot program available to the first 5,000 eligible customers. The intent of the pilot program will be to provide incentives for low-income customers to conserve and to avoid penalizing low-income customers who wish to stay off of programs such as the Percentage of Income Payment Plan (PIPP). Eligible customers shall be non-PIPP low usage customers verified at or below 175 percent of the poverty level. Duke will design a tariff that adjusts the fixed monthly charge for eligible customers as shown on Stipulation Exhibit 2. These rates may be adjusted if the Commission does not approve the fixed customer charge as shown in Stipulation Exhibit 2. Duke will develop the details for this program in consultation with Staff and the parties. Duke shall evaluate the program after the first winter heating season to determine, following consultation with staff and the parties, whether the program should be

continued to all eligible low-income customers, including considerations of program demand and cost (*Id.* at 20).

- (18) Duke will convene a working group or collaborative process, open to interested stakeholders, within 60 days after approval of the Stipulation, to explore implementing an auction to supply the standard service offer. Duke will report to the Commission within one year after approval of this Stipulation, the findings of the working group or collaborative including the facts and arguments which support and or oppose implementation of an auction process. The working group or collaborative process shall also review whether the present allocation of 80 percent of the net revenues from Duke's asset management agreement should continue to flow to GCR customers only, or should be changed to flow to GCR customers and choice customers (*Id.* at 21-22).
- (19) Duke shall revise its GCR tariff to implement a sharing mechanism for sharing of net revenues from off-system transactions.⁷ Such sharing mechanism shall be effective if Duke does not have an asset management agreement transferring management responsibility for its gas commodity, storage and transportation contracts to a third party, and shall provide for sharing of the net revenues from off-system transactions to be allocated 80 percent to GCR and choice customers and 20 percent to Duke shareholders. The revenue sharing percentage proposed by implementation of the sharing mechanism in this Stipulation is expressly limited to gas-related sales transactions, and shall not have precedential value in establishing the sharing percentages for similar electric sales transactions by Duke. This sharing mechanism, but not the 80 percent/20 percent revenue allocation, shall be subject to review in future GCR cases (*Id.* at 21-22).⁸
- (20) Duke shall meet with Staff and other interested parties to discuss eliminating customer deposits for PIPP customers and shall eliminate such deposits if Staff agrees (*Id.* at 18).

⁷ Off-system transactions are defined to include but are not limited to Off-System Sales Transactions, Capacity Release Transactions, Park Transactions, Loan Transactions, Exchange Transactions, and any other similar, but yet unnamed transactions.

⁸ This paragraph does not change the allocation contained in the current sharing mechanism for revenues received under Duke's asset management agreement.

- (21) Duke shall review and fully consider the merits of adopting any new payment plans submitted by any party and, if Duke elects not to implement such new payment plan, Duke shall respond to the stakeholder in writing to state the reason for its decision (*Id.* at 18).
- (22) Duke shall review its use of payday lenders as authorized payment stations and will use its best efforts to eliminate the use of payday lenders as authorized payment stations if other suitable locations for the payment stations are available in the same geographic area. Duke shall provide a list of all payday lenders utilized as authorized payment stations to Staff and other interested parties annually. The annual payday lenders list is to be provided initially on May 1, 2008, and on May 1, each year thereafter (*Id.* at 18-19).
- (23) Duke shall communicate with its customers to educate them about the difference between authorized and non-authorized payment stations. Duke shall work with members of the Collaborative to develop the educational materials and communication strategy (*Id.* at 19).

B. Summary of the Residential Rate Design Issue

This case marks a sea change in the recommendation of the Commission's Staff with respect to the method of determining a gas utility's residential distribution rate design. Traditionally, natural gas distribution rates in Ohio have been set by allocating a relatively small proportion of the fixed costs to the "customer" charge, with the remaining fixed costs recovered through a volumetric component. However, volatile and sustained increases in the price of natural gas, along with heightened interest in energy conservation, have called into question long-held ratemaking practices for gas companies. In this proceeding, Staff and Duke advocate the adoption of a modified Straight Fixed Variable (SFV) residential rate design that allocates most fixed costs of delivering gas to a monthly flat fee with the remaining fixed costs recovered through a variable or volumetric component. Under this proposed new "levelized" rate design, Duke's current \$6.00 residential customer charge would be eliminated. Instead, residential customers would pay a flat monthly fee of around \$20 to \$25, but with a corresponding lower usage component to recover the remaining fixed distribution costs (Staff Ex. 1, at 30-33, 46-48; Stipulation Ex. 2; Duke Ex. 29 at 6; Tr. I at 87-88, 147-148, 159).

In its initial filings, Duke's proposed residential rate design included a \$15.00 customer charge with a sales decoupling rider to address an alleged revenue erosion problem caused by declining average use per customer. The Staff Report noted this

historical trend, but rejected a sales decoupling rider mechanism in favor of a phased-in SFV rate design. Staff's position was subsequently joined by Duke and the new design was used for calculations in the Stipulation exhibits, but adoption of the proposed rate design was expressly reserved for consideration by the Commission (Staff Ex. 1, at 30-33, 46-49; Jt. Ex. 1, at 1, 5, 19-20).

The levelized rate design is opposed by OCC and OPAE, both of whom advocate keeping the current low residential customer charge and high volumetric rates. In the alternative, they argue that, if a decoupling mechanism is to be adopted, the appropriate design is a decoupling rider rather than the flat rates recommended by Duke and Staff. The other parties to these proceedings either have no interest in residential rate design or chose not to take a position on this issue.

OCC and OPAE first cite the projected overall growth in Duke's residential gas revenues for 2008-2012 in contending that Duke has no revenue erosion problem because any revenue loss from declining sales on a per-customer basis will be more than offset by future increases in Duke's residential customer base (OCC Br. at 53; OCC Ex. 6, at 5-6; OCC Ex. 12). OCC and OPAE then argue that, in the event the Commission determines there is a revenue erosion problem, the Commission should adopt a sales decoupling rider to unlink revenue recovery from sales, similar to that stipulated to by Vectren Energy Delivery of Ohio ("Vectren"). *See, In the Matter of the Application of Vectren Energy Delivery of Ohio, Inc. for Approval, Pursuant to Section 4929.11, Revised Code, of a Tariff to Recover Conservation Expenses and Decoupling Revenues Pursuant to Automatic Adjustment Mechanisms and for Such Accounting Authority as May be Required to Defer Such Expenses and Revenues for Future Recovery through Such Adjustment Mechanisms, Case No. 05-1444-GA-UNC, Supplemental Opinion and Order (June 27, 2007).*

Staff maintains that the evidence of record clearly indicates that Duke's revenue erosion problem is real and that the levelized rate design is the better way to balance the utility's desire for recovery of its authorized return with promotion of energy efficiency as a customer and societal benefit through control of energy bills. Staff notes that nearly six million dollars of the total \$34.1 million revenue deficiency identified by Duke in this case is attributable to declining customer usage and cites the decline in per-customer, residential natural gas consumption, which has been accelerating since the marked price increases in the winter of 2000/2001. Staff asserts that, as long as the bulk of a utility's distribution costs are recovered through the volumetric component of base rates, this decline in per-customer usage threatens the utility's recovery of its fixed costs of providing service. Staff contends that the levelized rate design best addresses this issue while simultaneously removing the disincentives to utility-sponsored energy efficiency programs that exist with the traditional rate design (Duke Ex. 11, at 3-6, 11; Staff Ex. 3, at 3-5; Tr. I at 214-216; Staff Br. at 6-7).

Staff points out that the proposed new levelized rate design is a form of decoupling that breaks strict linkage between utility earnings and customer consumption by recognizing that virtually all the costs of gas distribution service are fixed, and the cost to serve a residential customer is largely the same, regardless of the specific customer's usage. Duke and Staff contend that it is neither fair nor accurate to characterize this fixed component as a customer charge because, under Duke's current rate design, the customer charge is set at an artificially low level that only minimally compensates the company for its fixed costs of providing gas service (Duke Ex. 29, at 6; Tr. I at 159; Staff Br. at 6-8;).

Staff and Duke argue that, since the costs of providing gas distribution service are almost exclusively fixed, the proposed rate design will more closely match costs and revenues, thereby giving customers more accurate and timely pricing signals. They also contend that spreading the recovery of fixed costs more evenly over the entire year will help to reduce winter heating bills. Staff and Duke allege that customer incentives to conserve energy will remain strong because 75 to 80 percent of each customer's total bill is the cost of the gas itself (Staff Ex. 3, at 3-5; Tr. I at 159, 214-216; Tr. II at 91-93).

Finally, Staff and Duke suggest that a strict matching of fixed rates with fixed costs would result in a \$30.00 fixed residential distribution charge. However, because the proposed rate design is a significant departure from current rates, the Stipulation proposes to phase-in the new design over two years, using a lower fixed charge of \$20.25 in year one, and \$25.33 in year two. In addition, the remaining variable base rate component contains two usage tiers in an effort to minimize impacts on low-use residential customers, since average and larger usage residential customers will either benefit or be unaffected by the levelized rate design proposal (Jt. Ex. 1, at Ex. 2; Tr. I at 55, 87-88, 147-148).

OCC and OPAE counter that the stipulated rate design proposal amounts to a huge jump in the fixed monthly customer charge and violates a 30-year rate-making principle of gradualism. Moreover, they allege, it would violate the state policy to promote energy efficiency under Section 4929.02, Revised Code, because the proposed rate design sends an anti-conservation price signal to consumers, penalizes customers who have invested in energy efficiency by extending the payback period, and takes away the consumers' ability to control their energy bills. In addition, they assert that the levelized rate design is regressive towards low-use customers, and transfers wealth from low-income customers to high-use customers who are predominantly high-income customers (OCC Br. at 17-35, 46-55, 75-76).

Staff and Duke contend that under the proposed new rate design, high-use customers will benefit relative to low-use customers, and cite an analysis of PIPP customers to support the proposition that most low-income customers will actually benefit from this change. According to Duke witness Paul G. Smith, the PIPP customer data indicated that the average PIPP customer consumes approximately 1,000 ccf per year, or

approximately 25 percent more than the average non-PIPP customer and, therefore, levelized rates will actually reduce the annual cost for the average PIPP customer, and the cost of the PIPP program (Duke Ex. 29, at 11-12). Duke and Staff argue that if PIPP customer usage is representative of all of Duke's low-income customers, then most of Duke's low-income ratepayers will actually benefit from this policy change. In addition, they note any adverse impact of the levelized rate design will be mitigated by the new low-income/low-use pilot program included in the Stipulation. This program provides a credit to offset the higher fixed monthly charge for the first 5,000 non-PIPP, low-use customers verified at or below 175 percent of the federal poverty level. (Duke Br. at 17-35, 46-55, 75-76).

OCC and OPAE insist that the levelized rates will harm low-income customers and that the PIPP customer data is not indicative of other Duke low-income customers, but offered no data to support this contention (OCC Br. at 46-53; OPAE Br. at 4, 8).

III. DISCUSSION AND CONCLUSION

A. Consideration of the Stipulation

Rule 4901-1-30, O.A.C., authorizes parties to Commission proceedings to enter into a stipulation. Although not binding on the Commission, the terms of such an agreement are accorded substantial weight. See *Consumers' Counsel v. Pub. Util. Comm.*, 64 Ohio St.3d 123, at 125 (1992), citing *Akron v. Pub. Util. Comm.*, 55 Ohio St.2d 155 (1978). This concept is particularly valid where the stipulation is unopposed by any party and resolves all or most of the issues presented in the proceeding in which it is offered.

In considering the reasonableness of a stipulation, the Commission has used the following criteria:

- (a) Is the settlement a product of serious bargaining among capable, knowledgeable parties?
- (b) Does the settlement, as a package, benefit ratepayers and the public interest?
- (c) Does the settlement package violate any important regulatory principle or practice?

The Ohio Supreme Court has endorsed the Commission's analysis using these criteria to resolve issues in a manner economical to ratepayers and public utilities. *Indus. Energy Consumers of Ohio Power Co. v. Pub. Util. Comm.*, 68 Ohio St.3d 559 (1994) (citing *Consumers' Counsel, supra*, at 126). The court stated in that case that the Commission may

place substantial weight on the terms of a stipulation, even though the stipulation does not bind the Commission (*Id.*).

The Commission finds that the Stipulation filed in these cases appears to be the product of serious bargaining among capable, knowledgeable parties. The signatory parties represent a wide diversity of interests including the utility, residential consumers, low-income residential consumers, commercial and industrial consumers, and Staff. Further, we note that the signatory parties routinely participate in complex Commission proceedings and that counsel for the signatory parties have extensive experience practicing before the Commission in utility matters.

The Stipulation also meets the second criterion. As a package, the Stipulation advances the public interest by resolving all issues raised, except as to residential revenue design, thereby avoiding extensive litigation. While the Stipulation includes a general rate increase of approximately three percent across all customer classes, that increase will allow the company an opportunity to recover its expenses. As for the new AMRP, which now includes riser replacement and company ownership of certain customer service lines, the Stipulation continues the mechanism established for the parties and the Commission to evaluate the reasonableness of the expenses incurred on a consistent, regular basis during the program until another base rate application is filed by Duke. We conclude that the continuance of the main replacement program, the initiation of the riser replacement program and Duke's ownership of customer service lines advances the public interest and safety. As with the previous program, the new AMRP and riser replacement program does not sanction cost recovery of any or all yet-to-be-incurred costs and does institute caps on future recovery. The Stipulation also continues the process under which each year's AMRP and riser replacement expenses can be evaluated for the next AMRP rider, while also addressing questions related to over-recovery and treatment of cost savings. We note that the accounting provisions adopted to facilitate the new AMRP program and the riser replacement program cease at the completion of each program. The Commission further notes that the Stipulation provides for the continuation of the weatherization program and a pilot program for low income customers.

Regarding company ownership of certain customer service lines, Duke should, upon the request of the customer, work with the customer as to location, relocation, and, manner of installation of the service line, to the extent feasible under the gas pipeline safety regulations, Duke's tariff, and Duke's procedures.

Finally, the Stipulation meets the third criterion because it does not violate any important regulatory principle or practice. Indeed, the Stipulation provides a resolution for Duke to economically continue the AMRP and to initiate the riser replacement program facilitating gas system safety and reliability improvements.

On March 14, 2008, Duke moved for waiver of the requirement to file an update of the partially forecasted income statement and any variances for the test year, pursuant to Rule 4901-7-01, Appendix A, Chapter II(A)(5)(d), O.A.C. Duke notes that, as part of the Stipulation, the parties negotiated a revenue increase and further agreed to recommend that Duke be allowed to forgo the requirement of filing actual financial data for the test year (Jt. Ex. 1, at 5, footnote 5).

The Commission finds that the Stipulation filed in these matters is in the public interest and represents a reasonable disposition of all but one of the issues raised in these proceedings. We will, therefore, adopt the Stipulation in its entirety and grant Duke's motion for a waiver of the requirement to file an updated income statement in accordance with Rule 4901-7-01, Appendix A, Chapter II(A)(5)(d), O.A.C.

B. Consideration of the Residential Rate Design

The Commission first notes that there is no disagreement in this case that Duke's residential rates need to go up in order to cover Duke's prudently incurred costs to provide service. There is also no dispute in this case as to the amount of the increase in revenues needed to allow Duke to earn a fair rate of return on its investment. In addition to an overall increase in revenue of 3.1 percent, the settlement before us provides for the assignation of \$6 million in costs from commercial and industrial customers to the residential class. This reallocation reduces a pre-existing subsidy of residential customers by commercial and industrial customers. Thus, the parties have already agreed that residential customers, as a class, will pay an increase of 11.9 percent during the first year and 14.1 percent in the second year for the distribution portion of each residential customer's bill.

The only issue left to the Commission is the design of the rates Duke should bill residential customers to collect the revenues agreed to in the settlement. We agree with Staff that the time has come to re-think traditional natural gas rate design. Conditions in the natural gas industry have changed markedly in the past several years. The natural gas market is now characterized by volatile and sustained price increases, causing customers to increase their efforts to conserve gas. The evidence of record clearly documents the declining sales-per-customer trend over the decades. In fact, more than 15 percent of Duke's revenue deficiency in this rate case is attributable to declining customer usage, a trend which is not just continuing, but is also accelerating (Duke Ex. 11, at 3-6, 11; Staff Ex. 3, at 3-5; Tr. I at 214-216; Staff Br. at 7). Under traditional rate design, the ability of a company to recover its fixed costs of providing service hinges in large part on its actual sales, even though the company's costs remain fairly constant regardless of how much gas is sold. Thus, a negative trend in sales has a corresponding negative effect on the utility's ongoing financial stability, its ability to attract new capital to invest in its network, and its incentive to encourage energy efficiency and conservation.

The Commission, therefore, concludes that a rate design which separates or "decouples" a gas company's recovery of its cost of delivering the gas from the amount of gas customers actually consume is necessary to align the new market realities with important regulatory objectives. We believe it is in the interest of all customers that Duke has adequate and stable revenues to pay for the costs of its operations and capital and to ensure the continued provision of safe and reliable service. We further believe that there is a societal benefit to removing from rate design the current built-in incentive to increase gas sales. A rate design that prevents a company from embracing energy conservation efforts is not in the public interest. Duke's commitment to provide \$3 million for weatherization projects under the Stipulation is critical to our decision in this case (Jt. Ex. 1, at 12-14). Indeed, the Commission notes that a commitment to conservation initiatives will be an important factor in any future decision to adopt a decoupling mechanism. The Commission encourages Duke to review and further enhance its weatherization and conservation program offerings. As one part of this review, Duke should adopt the objective to make cost-effective weatherization and conservation programs available to all low-income consumers and to ramp up such programs as rapidly as reasonably practicable.

Having determined that a new decoupling rate design is appropriate, we must decide the better choice of two methods: a levelized rate design, which recovers most fixed costs up front in a flat monthly fee, or a decoupling rider, which maintains a lower customer charge and allows the company to offset lower sales through an adjustable rider.

On balance, the Commission finds the levelized rate design advocated by Duke and Staff to be preferable to a decoupling rider. Both methods would address revenue and earnings stability issues in that the fixed costs of delivering gas to the home will be recovered regardless of consumption. Each would also remove any disincentive by the company to promote conservation and energy efficiency. The levelized rate design, however, has the added benefit of producing more stable customer bills throughout all seasons because fixed costs will be recovered evenly throughout the year. In contrast, with a decoupling rider, as favored by OCC, customers would still pay a higher portion of their fixed costs during the heating season when their bills are already the highest, and the rates would be less predictable since they could be adjusted each year to make up for lower-than-expected sales.

A levelized rate design also has the advantage of being easier for customers to understand. Customers will transparently see most of the costs that do not vary with usage recovered through a flat monthly fee. Customers are accustomed to fixed monthly bills for numerous other services, such as telephone, water, trash, internet, and cable services. A decoupling rider, on the other hand, is much more complicated and harder to explain to customers. It is difficult for customers to understand why they have to pay

more through a decoupling rider if they worked hard to reduce their usage; the appearance is that the company is penalizing them for their conservation efforts.

The Commission also believes that a levelized rate design sends better price signals to consumers. The rate for delivering the gas to the home is only about 20 to 25 percent of the total bill. The largest portion of the bill, the other 75 to 80 percent, is for the gas that the customer uses. This commodity portion, the cost of the actual gas used, is the biggest driver of the amount of a customer's bill. Therefore, gas usage will still have the biggest influence on the price signals received by the customer when making gas consumption decisions, and customers will still receive the benefits of any conservation efforts in which they engage. While we acknowledge that there will be a modest increase in the payback period for customer-initiated energy conservation measures with a levelized rate design, this result is counterbalanced by the fact that the difference in the payback period is a direct result of inequities within the existing rate design that cause higher use customers to pay more of their fair share of the fixed costs than low-use customers.

The levelized rate design also promotes the regulatory objective of providing a more equitable cost allocation among customers regardless of usage. It fairly apportions the fixed costs of service, which do not change with usage, among all customers, so that everyone pays his or her fair share. Customers who use more energy for reasons beyond their control, such as abnormal weather, large number of persons sharing a household, or older housing stock, will no longer have to pay their own fair share plus someone else's fair share of the costs.

We recognize that, with this change to rate design, as with any change, there will be some customers who will be better off and some customers who will be worse off, as compared with the existing rate design. The levelized rate design will impact low usage customers more, since they have not been paying the entirety of their fixed costs under the existing rate design. Higher use customers who have been overpaying their fixed costs will actually experience a rate reduction. Average users will see only the impact of the increase agreed to by the parties; they will see no additional impact as a result of the Commission choosing the levelized rate design.

The Commission is sensitive to the impact of any rate increase on customers, especially during these tough economic times. We believe that the new levelized rate design best corrects the traditional design inequities while mitigating the impact of the new rates on residential customers by maintaining a volumetric component to the rates, by phasing in the increase over a two-year period, and by not reflecting the full extent of Duke's fixed costs in the proposed fixed charge. Still, we are concerned with the impact on low-income, low-use customers. Thus, crucial to our decision to adopt Duke and Staff's proposed rate design is the Pilot Low Income Program aimed at helping low-income, low-use customers pay their bills. This new program will provide a four-dollar, monthly

discount to cushion much of the impact on qualifying customers. To ensure that this discount is available to as many customers as possible, we direct that Duke expand this pilot program to include up to 10,000 customers, instead of the 5,000 customers specified in the Stipulation. Pursuant to the terms of the stipulation, Duke, in consultation with staff and the parties, shall establish eligibility qualifications for this program by first determining and setting the maximum low usage volume projected to result in the inclusion of 10,000 low-income customers who have previously been defined by the stipulation to be those at or below 175 percent of the poverty level. The Commission expects that Duke will promote this program such that to the fullest extent practicable the program is fully enrolled with 10,000 customers. Following the end of the pilot program, the Commission will evaluate the program for its effectiveness in addressing our concerns relative to the impact on low-use, low-income customers.

We are also concerned about the immediate impact of implementing the levelized rate design during the summer months when overall consumption is lowest. For the average customer, the new rate design will result in lower bills in the winter, but higher bills in the summer. Our concern is that the fixed charge increase may not be anticipated by customers who have budgeted for the traditional lower fixed charge during the low usage summer months. To mitigate this impact, we are directing that, from the initial bills resulting from this order through bills covering the period ending September 30, 2008, the fixed charge be set at \$15.00, consistent with Duke's original proposal. The corresponding volumetric rate for those months should also be adjusted to compensate for any revenue shortfall that this adjustment in the fixed charge will cause. Thereafter, rates will be as proposed in the Stipulation. We believe this additional phase-in of the new residential rate structure will give customers a further opportunity to adapt to this change, including the benefits of the budget billing option.

C. Rate Determinants:

1. Rate Base

The value of Duke's property used and useful in the rendition of natural gas services as of the December 31, 2007, is not less than \$649,964,874, as stipulated by the parties (ft. Ex. 1, at Schedule A-1).

The Commission finds the rate base of \$649,964,874, as provided in the Stipulation, to be reasonable and proper based on the evidence presented in these matters. Accordingly, the Commission adopts the valuation of \$649,964,874 as the rate base for purposes of this proceeding.

2. Operating Income:

In accordance with the proposed Stipulation, the parties agree that Duke's operating revenue is \$597,573,805 and that the net operating income is \$43,274,872 for the 12 months ended December 31, 2007 (Jt. Ex. 1, at Schedule A-1). The Commission finds the operating revenue and net operating income, as provided in the Stipulation, to be reasonable and proper based on the evidence presented in these matters. The Commission will, therefore, adopt these figures for purposes of these proceedings.

3. Rate of Return and Authorized Increase:

As stipulated by the signatory parties, under its present rates, Duke's net operating income is \$43,274,872. Applying this amount to the rate base of \$649,964,874 results in a rate of return of 6.66 percent. Such a rate of return is insufficient to provide Duke with reasonable compensation for the gas service it renders to customers. Accordingly, the signatory parties have agreed that Duke should be authorized to increase its revenues by \$18,217,566, an increase of approximately 3.05 percent above current annual revenues. This would result in an overall rate of return of 8.45 percent, which the Commission finds to be reasonable.

4. Rates and Tariffs:

Duke is directed to file a proposed customer notice. Duke is further authorized to cancel and withdraw its present tariffs governing service to customers affected by these applications and to file tariffs consistent in all respects with the discussion and findings set forth herein for the Commission's consideration. The approved tariffs will be effective for all services rendered after the effective date of the tariffs.

FINDINGS OF FACT:

- (1) On June 18, 2007, Duke filed notice of its intent to file an application to increase its rates. In that notice, the company also requested a test year beginning January 1, 2007, and ending December 31, 2007, with a date certain of March 31, 2007.
- (2) By entry issued July 11, 2007, the Commission approved Duke's request to establish the test period of January 1, 2007, through December 31, 2007, for the rate increase proposal and a date certain of March 31, 2007.
- (3) Duke filed its rate increase application on July 18, 2007. On July 18, 2007, Duke also separately filed requests for approval

of an alternative rate plan, docketed at Case No. 07-590-GA-ALT, and for approval of changes in accounting methods, docketed at Case No. 07-591-GA-AAM.

- (4) By entry dated September 5, 2007, the Commission found that Duke's rate increase and alternative rate plan applications complied with the requirements of Section 4909.18, Revised Code, and Rule 4901:1-19-05, O.A.C.
- (5) The Commission accepted Duke's rate increase application for filing as of July 18, 2007.
- (6) OEG, Kroger, Interstate, the city of Cincinnati, OCC, PWC, Integrys, Direct, Stand and OP&E each requested, and was granted, intervention in these proceedings.
- (7) Objections to the staff report were filed by Duke, PWC, OEG, OP&E, OCC, and, jointly, by Integrys and Direct.
- (8) Duke published notice of its applications and the hearings and filed the required proofs of publication on February 11, February 25, and March 12, 2008.
- (9) The staff of the Commission and the financial auditor filed their respective reports of investigation on December 20, 2007.
- (10) On January 25, 2008 a prehearing conference was held, as required by Section 4909.19, Revised Code.
- (11) Two local public hearings were held in Cincinnati, Ohio, on February 25, 2008, and another local public hearing was held in Mason, Ohio, on March 11, 2008, in accordance with Section 4903.083, Revised Code. At the Cincinnati hearings a total of 27 witnesses gave testimony and four witnesses gave testimony at the Mason hearing.
- (12) On February 28, 2008, a Stipulation was filed by all the parties to this proceeding resolving all the issues presented in these matters, except rate design.
- (13) The evidentiary hearing commenced as scheduled on February 26, 2008, was continued until February 28, 2008, and reconvened on March 5, 2008. At the evidentiary hearing, Duke and staff each presented one witness in support of the

Stipulation. In regard to the one litigated issue, rate design, Duke presented four witnesses, OCC presented two witnesses and staff presented one witness.

- (14) The Stipulation is the product of serious bargaining between knowledgeable parties, benefits ratepayers, advances the public interest, and does not violate any important regulatory principles or practices.
- (15) The value of all of the company's jurisdictional property used and useful for the rendition of natural gas service to customers affected by this application, determined in accordance with Section 4909.15, Revised Code, is not less than \$649,964,874.
- (16) Under its existing rates, Duke's net operating revenue is \$43,274,872, under its existing rates. This net annual revenue of \$43,274,872, when applied to a rate base of \$649,964,874, results in a rate of return of 6.66 percent.
- (17) A rate of return of 6.66 percent is insufficient to provide Duke reasonable compensation for the service it provides.
- (18) A rate of return of 8.45 percent is fair and reasonable, under the circumstances presented in these cases, and is sufficient to provide the company just compensation and return on the value of its property used and useful in furnishing natural gas service to its customers.
- (19) A rate of return of 8.45 percent applied to the rate base of \$649,964,874 will result in allowable net operating income of \$54,922,032.
- (20) The allowable gross annual revenue to which the company is entitled for purposes of this proceeding is \$615,791,371.

CONCLUSIONS OF LAW:

- (1) Duke's application for a rate increase was filed pursuant to, and this Commission has jurisdiction of the application pursuant to, the provisions of Sections 4909.17, 4909.18, and 4909.19, Revised Code. The application complies with the requirements of these statutes.

- (2) Staff and Blue Ridge conducted investigations of the application, filed their respective reports, and served copies of the Staff Report on interested persons in accordance with the requirements of Section 4909.19, Revised Code.
- (3) The hearings, and notice thereof, complied with the requirements of Sections 4909.19 and 4903.083, Revised Code.
- (4) The Stipulation is the product of serious bargaining between knowledgeable parties, benefits ratepayers, advances the public interest, and does not violate any important regulatory principles or practices. The Stipulation submitted by the parties is reasonable and shall be adopted in its entirety.
- (5) Duke's existing rates and charges for gas service are insufficient to provide Duke with adequate net annual compensation and return on its property used and useful in the provision of natural gas service.
- (6) A rate of return of 8.45 percent is fair and reasonable under the circumstances of this case and is sufficient to provide Duke just compensation and return on its property used and useful in the provision of gas service to its customers.
- (7) Duke should be authorized to cancel and withdraw its present tariffs governing service to customers affected by these applications and to file tariffs consistent in all respects with the discussion and findings set forth herein.
- (8) The levelized rate design, as modified herein, is a reasonable resolution to address Duke's declining sales volumes per customer, allow Duke the opportunity to collect the revenue requirement established in this rate case proceeding and encourage Duke's participation in customer energy conservation programs.

ORDER:

It is, therefore,

ORDERED, That Duke's request for a protective order in regards to Attachment MGS-1 is granted for 18 months from the date this order is issued. It is, further,

ORDERED, That Duke's request for leave to file depositions less than three days prior to the commencement of the evidentiary hearing is granted. It is, further,

ORDERED, That the Stipulation filed on February 28, 2008 is approved in its entirety. It is, further,

ORDERED, That Duke's request for a waiver of the requirement to file an updated income statement, pursuant to Rule 4901-7-01, Appendix A, Chapter II(A)(5)(d), O.A.C., is granted. It is, further,

ORDERED, That Duke implement the levelized rate design for its residential customers as discussed in this order. It is, further,

ORDERED, That Duke's applications to increase its rates and charges for gas service, to implement an alternative rate plan and to modify accounting methods are granted to the extent provided in this opinion and order. It is, further,

ORDERED, That Duke is authorized to cancel and withdraw its present tariffs governing gas service to customers affected by these applications and to file new tariffs consistent with the discussion and findings as set forth in this order. Upon receipt of four complete copies of tariffs conforming to this opinion and order, the Commission will review and consider approval of the proposed tariffs by entry. It is, further,

ORDERED, That a copy of this order be served upon all interested persons of record.

THE PUBLIC UTILITIES COMMISSION OF OHIO

Alan R. Schriber - concurring
OP 11/1/08
Alan R. Schriber, Chairman

Paul A. Centolella - concurring
and dissenting
Paul A. Centolella

Ronda Hartman Ferguson
Ronda Hartman Ferguson

Valerie A. Lemmie
Valerie A. Lemmie

Cheryl L. Roberto
Cheryl L. Roberto

RMB/GNS/vrm

Entered in the Journal

MAY 28 2008

Renee J. Jenkins

Renee J. Jenkins
Secretary

BEFORE

THE PUBLIC UTILITIES COMMISSION OF OHIO

In the Matter of the Application of Duke)
Energy Ohio, Inc. for an Increase in Rates.) Case No. 07-589-GA-AIR

In the Matter of the Application of Duke)
Energy Ohio, Inc. for Approval of an) Case No. 07-590-GA-ALT
Alternative Rate Plan for Gas Distribution)
Service.)

In the Matter of the Application of Duke)
Energy Ohio, Inc. for Approval to Change) Case No. 07-591-GA-AAM
Accounting Methods.)

CONCURRING OPINION OF
CHAIRMAN ALAN R. SCHRIBER

The straight fixed variable (SFV) option proposed by the PUCO Staff and adopted here today appropriately speaks to two significant issues. One is the potential impact on low income customers and the other is the desired effect that the Order shall have upon conservation.

The latter consideration is paramount. As we acknowledge that there are serious energy issues, we strive to promote and adopt advanced and renewable energy sources. While these are necessary and important pursuits, I believe that conservation is the most important measure of all. Nothing is less costly or more effective than simply reducing consumption. As time goes by, I trust that we will expend many resources adopting conservation measures on "both sides of the meter".

What we are attempting to do today is to provide appropriate incentives, through a rational pricing scheme, to encourage a reduction in the consumption of natural gas. By "rational", I mean a balanced approach that penalizes neither those whom have already squeezed the last cubic foot of natural gas from their budget, nor those whom might be inclined to "over-conserve".

The proposed SFV option achieves the optimum balance because it segregates fixed costs from those costs that are within the control of the consumer. In contrast, the current pricing scheme assigns all costs- fixed and variable - to the level of usage. The inherent danger with the current system is that consumers might be led to believe that the more they cut back, the more they save. This is true to a point. The point happens to be that of diminishing returns; over conservation takes place when the fixed costs of providing the

service are no longer covered with revenue. This inevitably leads to a rate case and higher rates. In other words, if usage-sensitive rates are assigned to fixed costs, and if usage falls below a certain point, then fixed costs do not get covered. It is then time for a rate case: what has the consumer saved?

If the solution is appropriate price signals, then prices must be associated with the volume of gas alone. In contrast, under the current pricing scheme, the gas company has no incentive to encourage conservation because those same usage sensitive rates might flow through to fixed costs as consumption grows, much to the utility's advantage. Under the SFV, the fixed costs are covered and the company makes no money on the gas commodity. Therefore, the company might actually promote conservation more aggressively.

One alternative to the old conventional method is a decoupling rider mechanism. In this case, Homeowner A who has already squeezed the last cubic foot of un-needed gas from his home via conservation oriented expenditures is discriminated against. This results from the make-whole provision that accrues to the utility when Homeowner B begins to pare down consumption. In other words, as B's meter begins to spin slower, so too do the company's revenues. Homeowner A will be compelled to make up some share of the shortfall, notwithstanding the fact that Homeowner A can cut back consumption no further.

Finally, those who argue that inadequate price signals are the biggest issue need only look at the impact of budget billing. What signal is being sent when the bill each month is the same regardless of consumption? Yet, is anyone recommending the elimination of budget billing?

The other issue in play is that of the income effect of the SFV methodology. One can conclude that consumers of greater amounts of gas will see their bills fall while those at the low end will see theirs rise. This does not mean that the burden will fall disproportionately on low-income consumers. There is record testimony that suggests that low-income consumers, i.e., PIPP customers consume more on average per year than others. Clearly, PIPP customers are protected. Furthermore, while one can play freely with percentages, the nominal dollar increases due to the rate restructuring is quite small. As a precaution, however, the Commission is modifying the stipulation to provide a four dollar credit to ten thousand non-PIPP customers as opposed to five thousand provided for in the stipulation.

Concurring Opinion of Chairman Alan R. Schriber
Case No. 07-589-GA-AIR et al.
Page -3-

All told, it is important that we arrive at a decision as expeditiously as possible. I believe that over the years the lesson to be learned is that we can never know with one hundred percent certainty all of the facts and all of the possible outcomes. This is precisely why the law has provided this Commission with the ability to react to adverse outcomes should they arise. This is the ultimate consumer protection.



Alan R. Schriber, Chairman

BEFORE

THE PUBLIC UTILITIES COMMISSION OF OHIO

In the Matter of the Application of Duke)
Energy Ohio, Inc. for an Increase in Rates.) Case No. 07-589-GA-AIR

In the Matter of the Application of Duke)
Energy Ohio, Inc. for Approval of an) Case No. 07-590-GA-ALT
Alternative Rate Plan for Gas Distribution)
Service.)

In the Matter of the Application of Duke)
Energy Ohio, Inc. for Approval to Change) Case No. 07-591-GA-AAM
Accounting Methods.)

OPINION OF COMMISSIONER PAUL A. CENTOLELLA
CONCURRING IN PART AND DISSENTING IN PART

The majority concludes that the current residential rate design has a negative impact on the ability of Duke Energy Ohio (hereafter "Duke", "the Company", or "the utility") to maintain financial stability, attract new capital, and on its incentive to encourage energy efficiency and conservation. And, the majority determines that it is necessary to decouple the utility's recovery of fixed costs from its volumetric sales. I concur with the majority in these conclusions and on issues other than residential rate design. I dissent from the majority regarding how to transition toward a residential rate design which decouples the recovery of fixed costs from volumetric rates.

Having determined that a new decoupling rate design is appropriate, the Commission must decide two questions. First, we must decide the better choice between two decoupling methods: a straight fixed variable (SFV) rate design, which recovers fixed costs in a flat monthly customer charge, or a decoupling adjustment, which allows the company to recover the same fixed cost revenue requirement with a lower customer charge by adjusting subsequent year rates to true up revenues received from volumetric charges. Second, in the event the Commission finds the SFV rate design preferable, the Commission should consider how to transition to a rate design which is significantly different from the rate structures that have formed the basis of consumer expectations.

Over the long-term, moving in the direction of a SFV rate design is preferable to keeping a modest customer charge and relying entirely on a decoupling adjustment. Both methods will address revenue and earnings stability issues in that the fixed costs of delivering gas to the home will be recovered irrespective of consumption. When fully implemented, each will remove any disincentive by the Company to promote conservation

and energy efficiency. And, both methods can be implemented in a straight forward manner and, if appropriately designed, easily explained to consumers as a deliberate or more gradual transition toward recovering fixed costs through a customer charge. However, as the ultimate objective, significant movement toward a fixed variable rate design is consistent with developing a more efficient rate structure. Efficient rate design seeks to align price elastic rate elements more closely to marginal costs, while recovering a larger portion of any residual revenue requirements through comparatively price inelastic charges. Experience shows that there is a significant price response to increases in volumetric charges, as evidenced by the recent steep reductions in average per customer consumption as gas costs increased. Given that customer charges are paid to provide access to gas service, it is reasonable to expect comparatively less price response with respect to increases in the customer charge. Over the long-term, this supports significant movement toward a SFV rate design in which a larger portion of the company's fixed cost revenue requirements is recovered through the customer charge.

Additionally, the SFV rate design will reduce the month-to-month variation in customer bills as fixed costs will be recovered evenly throughout the year, making it easier for customers to deal with high winter heating bills. While decoupling adjustments are not difficult to implement, a SFV rate design, when fully implemented, will remove the need for any additional administrative proceedings to review decoupling adjustments.

Consumers have made investment decisions based on expectations regarding natural gas pricing and fairness compels us to move at a measured pace when making fundamental changes in rate design. For this reason, the Commission should carefully consider the appropriate transition path.

On the question of how to transition to a fixed charge rate design, Duke and the Staff have proposed a modified SFV rate design in which the customer charge would be set at \$20.25 per bill in year one and \$25.33 per bill in year two. Fully implementing a SFV rate design would require a customer charge in excess of \$30 per residential consumer bill. Duke and the Staff also proposed and the Commission has expanded a "Pilot Low Income Program" that would provide some low income consumers a discount to cushion the impact of the change in rate design.

In my view, the pace of the transition in this case is more rapid than should be selected given the consumer expectations created by long-standing rate design practices and the recovery of fixed costs should be fully decoupled from sales volumes during the transition.

The pace of the transition proposed in the stipulation could send the wrong message to consumers with respect to energy conservation. Consumers who have made efficiency investments and reduced their consumption could see a significant increase in

the regulated portion of their bills, while their neighbors who have implemented no energy efficiency measures and are high use customers will see the regulated portion of their gas bills decline by similar amounts. Given rising gas commodity costs, increasing dependence on foreign sources of gas supply, and the likely adoption of limits on greenhouse gas emissions from the burning of fossil fuels, encouraging the adoption of cost effective energy efficiency measures should be among our highest priorities. A more gradual transition to a SFV rate design would minimize near term bill increases for low use consumers recognizing the investments that many of these consumers have made to reduce their gas usage, allow consumers to capture a greater portion of the expected benefits of such investments, and avoid the appearance that the Commission is rewarding high use by lowering the gas bills of high use customers.

Second, during the period covered by this Order, the modified SFV approach will not fully decouple recovery of the Company's fixed costs from sales volumes. A modest three percent reduction in sales during the first year would represent a loss to Duke of the opportunity to recover more than a million dollars of its fixed costs.

To address these concerns, I would reach the following result.

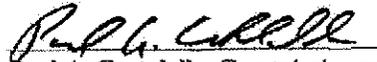
First, the recommendation of the Staff and Company should be modified to reduce the year one customer charge for all residential consumers to \$16.25 per residential bill and establish the base level of the year two customer charge for all residential consumers at \$21.33.

Second, consistent with the majority opinion, the Company should review and further enhance its weatherization and conservation program offerings. As one part of this review, Duke should adopt the objective of making cost-effective weatherization and conservation programs available to all low income consumers and to ramp up programs to facilitate implementation of all such measures as rapidly as reasonably practicable. Low income consumers often face difficult choices between paying their energy bills and meeting other essential needs, yet may be among the last to be able to take advantage of cost-effective energy efficiency investments. Consumers who struggle to make ends meet often find it difficult to pay for the initial cost of efficiency measures. And, many low income consumers live in rental housing with landlords who have little incentive to install efficiency measures that would reduce their tenants' utility bills.

Third, in conjunction with filing a proposal for approval of significantly expanded energy efficiency programs and recovery of the costs of such programs, I would invite the Company to propose an interim decoupling adjustment. This adjustment should be structured to adjust the second and subsequent year base customer charge of \$21.33 for the difference, on a per customer bill basis, between the portion of the Company's fixed cost

residential revenue requirement that is allocated to volumetric rates and the revenues recovered for such fixed costs through volumetric rates at weather normalized sales levels.

To meet the energy challenges of the 21st Century, Ohio will need to greatly improve the efficiency with which we use all forms of energy including natural gas. Efficient price signals will be an important, but not sufficient, element in this transformation. Our increasing knowledge of behavioral economics and experience with utility energy efficiency programs has shown that utility efficiency programs can produce significant net economic benefits. The Commission needs to encourage the cost-effective expansion of such programs. And, we should not wait through the completion of a multi-year transition to a SFV rate design before doing so in full measure.


Paul A. Centolella, Commissioner