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VIA OVERNIGHT MAIL

March 2, 2005

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MAR 0 3 2005

PUBLIC SERVICE COMMISSION

Ms. Elizabeth O'Donnell
Executive Director
Kentucky Public Service Commission
211 Sower Boulevard
Frankfort, KY 40602

Case 2005-00096

RE: Application of The Union Light, Heat and Power Company for Approval of Modification to Accounting Practices to Establish Regulatory Assets and Liabilities Related to Certain MISO-Related Costs and Revenues not Already included in Existing Base Rates

Dear Ms. O'Donnell:

Enclosed please find an original and twelve (12) copies of The Union Light, Heat and Power Company's Application and the testimony of Paul K. Jett in the above-referenced case.

Please file and date-stamp the two extra copies of the filing and return them to me in the enclosed envelope.

Should you have any further questions, please do not hesitate to call me.

Very truly yours,

John Finnigan

John J. Finnigan, Jr.
Senior Counsel

JJF/sew

Enclosures

141099

COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:	)	
	)	
APPLICATION OF THE UNION LIGHT, HEAT AND POWER COMPANY FOR APPROVAL OF MODIFICATION TO ACCOUNTING PRACTICES TO ESTABLISH REGULATORY ASSETS AND LIABILITIES RELATED TO CERTAIN MISO-RELATED COSTS AND REVENUES NOT ALREADY INCLUDED IN EXISTING BASE RATES	)	Case No. 2005 -______

APPLICATION

Pursuant to KRS 278.030, 278.040 and 278.220, The Union Light, Heat and Power Company (ULH&P) respectfully requests approval to modify its current accounting practices to establish deferred regulatory assets and liabilities, respectively, related to incremental costs incurred and revenues received from the Midwest Independent Transmission System Operator, Inc. (MISO). In support of this application, ULH&P states as follows:

1. **Utility Status**. ULH&P is a Kentucky corporation with its principal office and principal place of business at 1697 A Monmouth Street, Newport Shopping Center, Newport, Kentucky 41071. Its mailing address is P. O. Box 960, Cincinnati, Ohio 45201. ULH&P supplies gas and electric service to retail customers in Kentucky and is a "utility" within the meaning of KRS 278.010(3)(a) and (b) and is subject to the Commission's regulation as to rates and service pursuant to KRS Chapter 278.

2. **Articles of Incorporation**. Pursuant to 807 KAR 5:001, Section 8(3), ULH&P states that a certified copy of its Articles of Incorporation, as amended, is on file with the Commission in Case No. 2005-00042.

3. **ULH&P's Retail Electric Rates**. ULH&P does not seek a rate increase in this proceeding; rather, ULH&P merely requests approval to establish the accounting accruals discussed above. ULH&P has not applied to increase its retail electric rates since 1991. When the Commission approved the current wholesale power contract between ULH&P and The Cincinnati Gas & Electric Company (CG&E), its parent company, ULH&P proposed, and the Commission approved, a settlement which froze ULH&P's retail electric rates through December 31, 2003, and limited ULH&P from certain rate increases through December 31, 2006.[1] The Commission's order permitted ULH&P to seek increases to its retail transmission and distribution-related rates any time after July 1, 2003.[2] ULH&P does not anticipate seeking recovery of the deferrals requested herein until it files a general rate case, to be effective January 1, 2007.

4. **Transfer of Generating Plants to ULH&P**. ULH&P currently obtains its power through the above-referenced wholesale power contract. On December 5, 2003, the Commission conditionally approved the transfer from CG&E to ULH&P of the following generating plants, representing 1,105 megawatts (MW) of generating capacity: CG&E's 69% share of East Bend No. 2 (a 648 MW unit); Miami Fort No. 6 (168 MW); and the Woodsdale Generating Station (490 MW).[3] The closing for this transaction is presently scheduled for an effective date of April 1, 2005. The wholesale power contract will be terminated at that time. CG&E will retain its transmission facilities associated with these

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1 *In the Matter of the Application of the Union Light, Heat and Power Company for Certain Findings Under 15 U.S.C. § 79Z,* Case No. 2001-00058 (Order) (May 11, 2001).

2 *Id.* at 17; *In the Matter of the Application of the Union Light, Heat and Power Company for Certain Findings Under 15 U.S.C. § 79Z,* Case No. 2001-00058 (Amended Offer of Settlement at 7) (March 13, 2001).

3 *In the Matter of the Application of the Union Light, Heat and Power Company for a Certificate of Public Convenience to Acquire Certain Generation Resources and Related Property; for Approval of Certain Purchase Power Agreements; for Approval of Certain Accounting Treatment; and for Approval of Deviation from Requirements of KRS 278.2207 and 278.2213(6),* Case No. 2003-00252 (Interim Order) (December 5, 2003).

generating plants; however, ULH&P will schedule transmission service from MISO and will incur costs and receive revenues associated with such transmission service, as more fully described below.

5. Transmission Service and Retail Rate Recovery of Transmission Costs. ULH&P currently receives service from CG&E-owned transmission facilities pursuant to a transmission service agreement under the Cinergy Services, Inc. Open Access Transmission Tariff (OATT), which has been assigned to MISO. ULH&P will continue to receive service from CG&E-owned transmission facilities under a MISO network integration transmission service agreement after the wholesale power contract terminates. ULH&P also owns and operates transmission facilities at 69,000 volts and below. CG&E is a "Transmission Owner" under MISO's current OATT. ULH&P is a "Transmission Owner," "Transmission Customer," and "Transmission User" under the MISO OATT.

As a "Transmission Customer," ULH&P incurs incremental MISO charges related to transmission service for ULH&P's retail customers on ULH&P's transmission facilities and related to receiving transmission service on CG&E-owned facilities. The costs that ULH&P incurs for transmission service under the MISO OATT are reflected in ULH&P's retail electric rates, except for the following costs discussed below.

6. MISO Schedules 16 and 17. Effective at the startup of MISO's day-ahead and real-time energy markets (the MISO Day 2 Market), currently scheduled to commence on April 1, 2005, MISO will implement charges under Federal Energy Regulatory Commission (FERC)-approved Schedule 16 – Financial Transmission Rights Administrative Service Cost Recovery Adder and Schedule 17 – Energy Market Support Administrative Service Cost Recovery Adder. Schedule 16 allows MISO to recover its costs for administering Financial Transmission Rights (FTRs) among the stakeholders in the transmission system who hold FTRs. Schedule 17 allows MISO to recover its costs for managing the day-ahead and real-time energy markets which will be created under the MISO's Open Access Transmission and Energy Markets Tariff (TEMT). ULH&P will incur incremental costs related to Schedules 16 and 17 when MISO implements the day-ahead and real-time energy markets under the TEMT. Such incremental costs are not currently reflected in ULH&P's retail electric rates.

7. MISO Schedule 10 and Schedule 10-FERC. MISO implemented Schedule 10 effective December 15, 2001 and implemented Schedule 10-FERC effective September 1, 2003. Schedule 10 allows MISO to recover all costs associated with operating MISO exclusive of those costs recovered pursuant to Schedules 1, 16 or 17. Schedule 10-FERC allows MISO to recover from its transmission customers the FERC's Assessment Fee invoiced to the MISO. ULH&P has incurred incremental costs related to Schedule 10 and Schedule 10-FERC since these dates, not currently reflected in ULH&P's retail electric rates, except for a portion of the Schedule 10-FERC costs. ULH&P seeks to defer the Schedule 10 costs as well as the Schedule 10-FERC costs not recovered in retail electric rates.

8. MISO TEMT. On August 6, 2004, the FERC issued an order conditionally approving MISO's TEMT. The TEMT contains the terms and conditions under which MISO will manage transmission congestion and provide for real-time balancing by dispatching generating units located throughout the Midwest on a real-time basis. Under the TEMT, MISO will administer real-time and day-ahead energy markets based on principles of locational marginal pricing (LMP) and FTRs.

9. **New Costs and Revenues under the TEMT.** Under the TEMT, ULH&P will incur the following new costs and receive new revenues not currently provided for under the OATT and not currently reflected in ULH&P's electric base rates: (1) LMP charges related to energy purchase and sale transactions in MISO's day-ahead and real-time energy markets; (2) charges and credits related to the settlement of FTRs held by market participants; (3) charges and credits related to certain uplift costs that the Midwest ISO will socialize and collect from all or a certain group of market participants; (4) administrative charges designed to ensure that MISO will recover its costs of administering the energy markets and FTRs; (5) charges incurred under MISO Schedule 22 (Seams Elimination Charge/Cost Adjustments/Assignments (SECA) charges from customers within its pricing zones/ and, if applicable, designated sub-zones. The SECA is a mechanism for recovery of the lost revenues resulting from the elimination of the through and out rates for transactions between the Midwest ISO and PJM.); and (6) other miscellaneous charges, costs and credits.

10. **Reasonableness and Necessity of ULH&P's Incremental MISO Costs.** As a "Transmission Owner," "Transmission Customer," and "Transmission User" under the MISO's tariffs, ULH&P necessarily incurs costs under MISO's rate schedules for transmission service that ULH&P utilizes to provide retail electric service for its customers.

11. **Establishment of Accounting Accruals.** The Commission has instructed ULH&P to obtain approval before establishing accounting adjustments to establish a cost as a new deferred regulatory asset.[4] The Commission has approved the establishment of

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[4] *In the Matter of Adjustment of Gas Rates of The Union Light, Heat and Power Company,* Case No. 2001-00092 (Order at 14) (January 31, 2002).

accounting accruals under various circumstances.[5] ULH&P respectfully submits that it would be reasonable for the Commission to approve the accounting accruals requested by ULH&P based on the circumstances described herein.

WHEREFORE, based on the foregoing, ULH&P respectfully requests approval to modify its current accounting practices to establish deferred regulatory assets and liabilities, respectively, related to incremental costs incurred and revenues received from MISO, as described above.

THE UNION LIGHT, HEAT AND
POWER COMPANY

By: ____________________
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[5] *In the Matter of Application of Louisville Gas and Electric Company for an Order Approving an Accounting Adjustment to be Included in Earnings Sharing Mechanism Calculations for 2003 and Application of Kentucky Utilities Company for an Order Approving an Accounting Adjustment to be Included in Earnings Sharing Mechanism Calculations for 2003,* Case Nos. 2003-00426 and 2003-00427 (Opinion) (December 23, 2003) (regulatory assets and regulatory liabilities related to adoption of SFAS No. 143, relating to asset retirement obligations); *In the Matter of the Application of the Union Light, Heat and Power Company for a Certificate of Public Convenience to Acquire Certain Generation Resources and Related Property; for Approval of Certain Purchase Power Agreements; for Approval of Certain Accounting Treatment; and for Approval of Deviation from Requirements of KRS 278.2207 and 278.2213(6),* Case No. 2003-00252 (Interim Order) (December 5, 2003) (regulatory asset relating to transaction costs of acquiring generating plants); *In the Matter of the Annual Earnings Sharing Mechanism Filing of Louisville Gas and Electric Company and the Annual Earnings Sharing Mechanism Filing of Kentucky Utilities Company; Application of Kentucky Utilities Company for an Order Approving Revised Depreciation Rates; Application of Louisville Gas and Electric Company for an Order Approving Revised Depreciation Rate; Joint Application of Louisville Gas and Electric Company and Kentucky Utilities Company for an Order Approving Proposed Deferred Debits and Declaring the Amortization of the Deferred Debits to be Included in Earnings Sharing Mechanism Calculations,*Case Nos. 2001-00054, 2001-00055, 2001-00140, 2001-00141, and 2001-00169 (Order) (December 3, 2001) (regulatory asset relating to workforce reduction expenses); *In the Matter of Louisville Gas and Electric Company and Goshen Utilities, Inc. Investigation into Alleged Unsafe Utility Practices,* Case No. 99-00042 (Order) (October 2, 2000) (regulatory asset relating to sewer mapping costs).

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MAR 3 2005

PUBLIC SERVICE COMMISSION

COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:	)	
	)	
APPLICATION OF THE UNION LIGHT, HEAT	)	
AND POWER COMPANY FOR APPROVAL OF	)	Case No. 2005 -______
MODIFICATION TO ACCOUNTING	)	
PRACTICES TO ESTABLISH REGULATORY	)	
ASSETS AND LIABILITIES RELATED TO	)	
CERTAIN MISO-RELATED COSTS AND	)	
REVENUES NOT ALREADY INCLUDED IN	)	
EXISTING BASE RATES	)	

DIRECT TESTIMONY OF

PAUL K. JETT

ON BEHALF OF

THE UNION LIGHT, HEAT AND POWER COMPANY

I. INTRODUCTION AND PURPOSE

Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

A. My name is Paul K. Jett. My business address is 139 East Fourth Street, Cincinnati, Ohio 45202.

Q. BY WHOM ARE YOU EMPLOYED?

A. I am employed by Cinergy Services, Inc. and my new position, effective March 1, 2005 is Director, RTO Activities.

Q. WHAT DUTIES AND RESPONSIBILITIES DO YOU HAVE IN YOUR CURRENT POSITION?

A. My chief responsibilities are primarily related to the execution of the regional transmission organization ("RTO") activities and support of Cinergy Corp. and its subsidiaries' (collectively, "Cinergy"), including The Union Light, Heat and Power Company ("ULH&P") initiatives regarding the RTO, from the perspective of Cinergy's Regulated Businesses Unit. Cinergy's Regulated Businesses Unit consists of ULH&P's and CG&E's regulated gas and electric transmission and distribution operations, as well as PSI's regulated electric transmission and distribution operations. My key responsibilities include: supporting the Midwest ISO Transmission Owners with respect to the Midwest Independent Transmission System Operator, Inc. ("MISO"), providing input into business practices supporting the MISO, monitoring MISO filings and business practices monitoring regulatory environment for changes in rules, representing Cinergy concerning MISO.

Q. PLEASE DESCRIBE YOUR EDUCATION AND EMPLOYMENT

HISTORY.

A. I earned an Associate Degree of Applied Science in Electrical Engineering Technology from the University of Cincinnati in 1991. I earned a Bachelor of Science Degree in Electrical Engineering Technology from the University of Cincinnati in 1998. I earned a Masters of Business Administration Degree from Thomas More College in 2000.

I joined The Cincinnati Gas & Electric Company ("CG&E") in March 1987 as a substation operator. I then progressed through a variety of positions of increasing responsibility.

In 2001, I served as Cinergy's project manager to prepare for the transfer of functional control of the operation of Cinergy's transmission systems to the MISO. In February 2002, the MISO began providing services as a "Day 1" RTO under its own Open Access Transmission Tariff ("OATT"). As Cinergy's Day 1 project manager, I oversaw the establishment of Cinergy's business practices, systems, and interfaces necessary to do business with the MISO following the Day 1 startup in February 2002.

In March 2003 I was promoted to Director, Federal Regulatory Policy. Among other duties, my current responsibilities include helping Cinergy analyze and prepare for the MISO's planned launch of its "Day 2" initiative, which will establish a centralized security-constrained economic dispatch platform supported by a day-ahead and real-time energy market design, including locational marginal pricing (sometimes referred to as "LMP") and financial transmission rights (sometimes referred to as "FTRs"). My promotion to Director, RTO Activities, became effective March 1, 2005.

Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?

A. The purpose of my testimony is to describe generally the MISO's Day 1 operations, including the MISO charges which ULH&P currently incurs on behalf of its retail electric customers in Kentucky. Next, I will provide a high level description of the energy markets that the MISO plans to implement on April 1, 2005, including an overview of the types of charges which ULH&P will incur on behalf of its retail electric customers once the MISO commences Day 2 operations.

II. <u>THE MISO'S DAY 1 OPERATIONS</u>

Q. PLEASE DESCRIBE THE SERVICES THE MISO PERFORMS TODAY.

A. When the MISO began Day 1 operations, it assumed responsibility for certain functions that were formerly performed by transmission owners in the MISO region. That responsibility includes the determination of transfer capability, processing of requests for transmission service, OASIS (*i.e.*, Open Access Same-Time Information System) administration and scheduling of transmission transactions. The MISO also assumed responsibility for evaluating regional security conditions to determine whether requests for transmission service can be accommodated on the transmission system and whether transactions actually scheduled result in power flows that remain within or violate security limits designed to ensure reliable operation of the interconnected transmission grid. Consistent with that role, the MISO is responsible for determining whether transmission schedules should be curtailed to maintain power flows within security limits. Thus, while the MISO does have some redispatch and transmission system reconfiguration authority in MISO Day 1, the MISO's primary means of managing congestion on the transmission system in MISO Day 1 are essentially limited to screening and denying requests for transmission service that would violate security limits and ordering the curtailment of scheduled transactions when necessary.

ULH&P did not transfer functional control of any of its transmission facilities to MISO when the Day 1 market commenced because ULH&P only owns transmission facilities with a nominally rated voltage of 66 kV and below. When MISO assumed functional control of transmission facilities from transmission owners at the start of the Day 1 market, it only assumed functional control over facilities with nominally rated voltage of 100 kV and above, with certain minor exceptions which did not apply to ULH&P. After the start of the Day 1 market, ULH&P, on behalf of its retail electric customers, began receiving transmission service from MISO as a "Transmission Customer."

Q. IS ULH&P OBLIGATED TO PURCHASE TRANSMISSION SERVICE FROM THE MISO?

A. Yes. The MISO is the exclusive transmission provider of all transmission service requested and scheduled on the transmission facilities under its functional control. The Federal Energy Regulatory Commission ("FERC") has mandated that all transmission customers must take transmission service from the MISO for service over the transmission facilities under the MISO's functional control. Thus, ULH&P, on behalf of its retail electric customers in Kentucky, is a Transmission

Customer under the MISO OATT with respect to transmission service required to serve its retail electric customers, which will ultimately include the transmission of electricity produced at generating facilities owned and operated by ULH&P after ULH&P acquires generating facilities from CG&E, and transmitted across transmission facilities owned by CG&E and other transmission owners, but under the functional control of the MISO.

Q. WHAT MISO CHARGES ARE ULH&P REQUIRED TO PAY TODAY FOR TRANSMISSION SERVICE TAKEN TO SERVE ITS KENTUCKY RETAIL ELECTRIC CUSTOMERS?

A. The MISO is a not-for-profit entity. Accordingly, the MISO OATT contains a variety of scheduled charges designed to ensure that the MISO remains revenue neutral. Under Schedule 1 of its OATT, the MISO recovers the costs it incurs for providing transaction scheduling and system dispatch associated with real-time control of the transmission system. Under Schedule 10, the MISO imposes an administrative adder to recover its operating costs. ULH&P is required to pay this fee for the transmission service it takes on behalf of its Kentucky retail electric customers. Under Schedule 10-FERC, the MISO collects revenues to pay the annual charge assessed by the FERC on the MISO based on the megawatt-hours of electric energy it transmits in interstate commerce as reported on FERC Form 582. ULH&P is allocated a portion of that fee based on the megawatt-hours of network transmission service taken to serve its Kentucky retail electric customers.

Schedules 2, 3, 5 and 6 of the MISO OATT also contain a number of pass-through charges for ancillary services that the MISO procures from generators in the MISO region. The MISO invoices ULH&P for those charges. For example, Schedule 5 of the MISO OATT imposes a charge for spinning reserve service that must be provided or procured by the transmission provider (*i.e.*, the MISO) to ensure online reserves are available in the event of a system contingency. ULH&P procures spinning reserve service from CG&E's plants for ULH&P's loads, so ULH&P is not subject to this MISO charge. Schedules 2, 3 and 6 of the OATT set forth charges for other ancillary services that ULH&P also obtains from CG&E, so ULH&P is not subject to these MISO charges either. Finally, ULH&P, as a transmission-owning member of the MISO, is entitled to certain revenues collected by the MISO under its OATT.

Q. IS IT APPROPRIATE FOR THE ULH&P TO RECOVER THROUGH ITS RETAIL RATES THE CHARGES IMPOSED UNDER THE MISO OATT?

A. Yes. ULH&P taking transmission service under the MISO OATT to serve its retail electric customers is comparable to a Kentucky retail gas utility taking gas transportation service from an interstate gas pipeline to serve its Kentucky retail gas customers. In both situations, a Kentucky utility incurs costs to serve its Kentucky retail customers based upon FERC-approved rates set forth in a FERC-approved tariff. Just as a Kentucky gas utility is permitted by the Commission to recover from its Kentucky retail gas customers the utility's gas transportation costs incurred under a FERC-approved tariff to serve those customers, ULH&P, to the extent it has not already been authorized to do so, should be permitted to recover from its Kentucky retail electric customers the transmission costs incurred to serve those customers.

III. THE MISO'S DAY 2 ENERGY MARKETS

Q. ARE YOU FAMILIAR WITH THE MISO'S DAY 2 ENERGY MARKETS INITIATIVE?

A. Yes. As explained above, my responsibilities include monitoring federal regulatory policy and related matters for Cinergy's Regulated Businesses Unit. Consequently, I have been substantially involved in Cinergy's efforts to prepare for the start-up of the MISO's energy markets.

Q. PLEASE GENERALLY DESCRIBE THE MISO'S DAY 2 ENERGY MARKETS.

A. The principal document governing the operation of the MISO's energy markets is the MISO's Open Access Transmission and Energy Markets Tariff ("TEMT"), which was conditionally accepted by the FERC on August 6, 2004. The TEMT will replace the MISO's currently effective OATT. Thus, upon implementation of the MISO's Day 2 Energy Markets, ULH&P will be required to arrange for and purchase transmission service on behalf of its retail customers pursuant to the TEMT, which will be the successor tariff to the MISO OATT.

Under the TEMT, the MISO will administer both real-time and day-ahead markets for electric energy utilizing locational marginal pricing and financial transmission rights. The real-time energy market will function as the real-time balancing market envisioned by Order No. 2000. The day-ahead market provides a means for market participants to mitigate their exposure to price risk in the real-time markets. It also will provide meaningful information to the MISO regarding expected real-time operating conditions for the next day, which will enhance the

MISO's ability to ensure reliable operation of the transmission system. Additionally, locational marginal pricing will provide a market-based solution to manage congestion in the MISO region.

Q. PLEASE EXPLAIN WHAT YOU MEAN BY CONGESTION.

All energy transactions on the transmission system can potentially result in congestion—that is, a transaction may cause one or more transmission elements to exceed its capability. Such congestion can either be resolved through methodologies, such as the North American Electric Reliability Council's ("NERC") Transmission Loading Relief ("TLR") procedures, or through market-based mechanisms, such as the use of locational marginal pricing and FTRs.

Q. WHAT ARE FINANCIAL TRANSMISSION RIGHTS, OR FTRS?

FTRs are financial instruments that provide market participants a means to manage the risk of congestion costs they may incur as a result of scheduling energy transactions in the day-ahead energy market. In fact, as part of its standard market design initiative, FERC proposed the use of FTRs. FTRs are currently a feature of several of the centrally dispatched energy markets operating in the U.S., including the energy markets operated by PJM, the New York ISO and ISO New England.

Q. PLEASE EXPLAIN THE EXPECTED BENEFITS OF LOCATIONAL MARGINAL PRICING OVER THE UTLIZATION OF THE NERC'S TLR PROCEDURES AS A MEANS TO MANAGE CONGESTION.

The MISO only has authority under Day 1 operations to order redispatch under emergency conditions. Since economic re-dispatch is not available to accommodate a given transmission transaction, the MISO's only recourse when a previously approved transmission request would lead to a violation of operating security limits is to curtail one or more transactions using TLR procedures that are based on uneconomic, inefficient criteria. Physical rationing of access to the transmission system through the use of TLR curtailments, however, leads to inefficient use of the transmission grid, because TLRs take little account of the relative economic value of competing transactions. If TLRs are used as the primary means to manage congestion, a party that values transmission capacity through a particular constraint higher than another party may not have an effective recourse to take advantage of this differential. Using TLRs as the primary congestion management tool can also lead to an underutilization of the transmission system. This is because a transmission provider, in order to avoid the excessive use of TLRs, may be overly conservative in approving requests for access to the transmission system in the first instance.

Moreover, the utilization of a TLR may not result in the desired outcome. Relieving congestion by calling a TLR is based on imprecise flow estimates that may not accurately predict the amount of congestion relief actually realized by calling the TLR. Additionally, the time needed to implement a requested curtailment may be unacceptable depending on the nature of the constraint to be relieved.

In contrast, locational marginal pricing, which is the pricing methodology recommended by the FERC in Order No. 2000 and in use by PJM, the New York ISO and ISO New England, is a market-based pricing methodology that aligns the physics of redispatch caused by transmission congestion with the economic consequences. A security-constrained dispatch that prevents security violations before the fact is expected to be a significant improvement to reliability over the current congestion management system, which, as explained above, relies in large part on unpredictable and cumbersome TLR procedures to relieve transmission congestion after the fact.

Q. WILL THE IMPLEMENTATION OF THE MISO'S DAY 2 ENERGY MARKETS RESULT IN NEW CHARGES THAT ULH&P WILL BE REQUIRED TO PAY ON BEHALF OF ITS RETAIL CUSTOMERS?

A. Yes. As noted above, the MISO is a not-for-profit entity. Like the MISO OATT it replaces, the MISO TEMT contains schedules and charges designed to ensure the MISO's continued revenue neutrality. Additionally, ULH&P will be entitled to receive certain payments from the MISO as a result of its participation in the Day 2 energy markets. The new charges and credits that the MISO will impose under the TEMT (*i.e.,* charges and credits not included in the existing OATT) essentially fall into one of the following categories: (1) LMP charges related to energy purchase and sale transactions in the MISO's day-ahead and real-time energy markets; (2) charges and credits related to the settlement of FTRs held by market participants; (3) charges and credits related to certain uplift costs that the MISO will socialize and collect from all or a certain group of market participants; (4) administrative charges designed to ensure that the MISO will recover its costs of administering the energy markets and FTRs; (5) charges incurred under MISO Schedule 22 , which is the mechanism the Midwest ISO uses to charge and collect

Seams Elimination Charge/Cost Adjustments/Assignments (SECA) charges from Customers within its pricing zones/ and, if applicable, designated sub-zones. The SECA is a mechanism for recovery of the lost revenues resulting from the elimination of the through and out rates for transactions between the Midwest ISO and PJM. These SECA charges are collected in compliance with the Commission's November 18, 2004 Order in Docket Nos. ER05-6-000, EL04-135, EL02-111, and EL03-212 and accepted by the Commission; (6) other miscellaneous charges, costs and credits. I have provided an overview of charges and credits set forth in the TEMT at Attachment PKJ-1 to my testimony.

Q. PLEASE GENERALLY DECRIBE THE LMP CHARGES THAT WILL BE IMPOSED UNDER THE TEMT.

A. All purchases and sales of energy in the day-ahead and real-time energy markets will be made at locational marginal prices, which reflect the market clearing price to serve the next increment of load at a given location. The locational marginal price of energy for a given market interval will reflect: (1) the energy clearing price for that interval, which will be the same for all locations in the MISO region, (2) the congestion costs incurred to deliver the energy to the withdrawal location and (3) a marginal electricity loss component.

Every transaction scheduled through the MISO market will be subject to locational marginal pricing. After ULH&P acquires generating facilities from CG&E, each generator owned by ULH&P will be paid for all the megawatt-hours it supplies to the markets at the market clearing price of the associated generation node. Power generated to serve ULH&P's native load will in essence remain

ULH&P's, but will flow through the MISO transmission system, entering at the associated generator node, and exiting to ULH&P's distribution system at ULH&P's designated load zone. The locational marginal price at ULH&P's designated load zone represents the price of power for the load within that load zone. To the extent that ULH&P's own generators are serving its retail customers, the difference between the market clearing price at ULH&P's generator nodes and the market clearing price at ULH&P's designated load zone will equal the congestion and losses incurred to deliver the energy.

Q. WILL BILATERAL PURCHASES BE SUBJECT TO LOCATIONAL MARGINAL PRICING?

A. Yes. The MISO will impose a charge for congestion and losses between the source and sink for bilateral purchases that are scheduled in the day-ahead or real-time energy market. Thus, to the extent ULH&P makes a bilateral purchase to serve its retail customers, in addition to the purchase price paid to the seller, that purchase will be subject to a charge for congestion and losses to deliver the energy to ULH&P's load zone.

Q. PLEASE DESCRIBE HOW FTRS WILL BE SETTLED IN THE DAY-AHEAD ENERGY MARKET.

A. ULH&P will receive a separate FTR settlement statement for each operating day. After the day-ahead market is cleared, the MISO calculates the hourly financial value of each FTR using day-ahead locational marginal prices. FTR holders receive either credits or charges based upon the type of FTRs and the amount of congestion along the defined path of those FTRs.

Q. PLEASE DESCRIBE THE NEW ADMINISTRATIVE CHARGES IMPOSED UNDER SCHEDULE 16 AND SCHEDULE 17 OF THE TEMT.

A. Under Schedule 16, the MISO will recover all the costs it incurs related to providing FTR Administrative Service. Such costs include, but are not limited to, costs associated with: (1) coordination of FTR bilateral trading; (2) administration of FTRs through allocation, assignment, auction or any other process accepted by the FERC; (3) support of the MISO's on-line internet-based FTR tool; (4) "simultaneous feasibility" analyses to determine the total combination of FTRs that can be outstanding and accommodated by the transmission system under the functional control of the MISO at a given point in time; and (5) the administration of FTRs and revenue distribution.

Schedule 17 provides for the recovery of all costs incurred by the MISO to provide Energy Market Support Administrative Service. Such costs include, but are not limited to, costs associated with: (1) market modeling and scheduling functions; (2) market bidding support; (3) LMP support; (4) market settlements and billing; (5) market monitoring functions; and (6) enabling the least-cost, security-constrained commitment and dispatch of generating resources to serve load in the MISO control areas while also establishing a spot energy market.

Q. PLEASE EXPLAIN WHAT YOU MEAN BY UPLIFT COSTS.

A. Under its TEMT, the MISO has proposed a number of charges that it intends to socialize and collect from all market participants or a certain group of market participants. For example, the MISO will impose a "Real-Time Revenue Sufficiency Guarantee Charge" on all market participants to ensure generators recover certain unit commitment costs for generators committed to be available during real-time operations for reliability purposes. Similarly, a charge or credit will be allocated to market participants for inadvertent energy surpluses or shortages resulting from inadvertent energy between control areas and seams with other markets.

Q. **WHAT ACTION DOES ULH&P REQUEST FROM THE COMMISSION REGARDING THESE CHARGES THAT ULH&P WILL BE REQUIRED TO PAY THE MISO ON BEHALF OF ULH&P'S RETAIL ELECTRIC CUSTOMERS?**

A. ULH&P does not seek a rate increase in this proceeding. ULH&P simply requests Commission approval to establish accounting adjustments to establish these charges and credits as regulatory assets and liabilities, respectively. When ULH&P files its next retail electric base rate case, it will propose a methodology to recover these costs.

Q. **ARE THERE OTHER CHARGES RELATED TO THE MISO'S OPERATION OF ENERGY MARKETS THAT ULH&P MAY INCUR SUBSEQUENT TO THE IMPLEMENTATION OF DAY 2?**

A. Quite possibly. The discussion of charges in my testimony is based on the TEMT as of the date of this filing. There are a number of issues yet to be resolved in that the MISO Day 2 FERC proceeding. Moreover, while the MISO and its stakeholders have worked hard to address a number of complex issues, it is a virtual certainty that changes will occur as the MISO and market participants, including the ULH&P, gain experience after Day 2 is implemented. Additionally, as the MISO's standard market design efforts continue and it works to implement common markets with PJM and other regional transmission organizations, the MISO will likely provide other services that will result in the imposition of new and different charges on ULH&P.

Q. CAN YOU ESTIMATE THE AMOUNT OF THE DEFERRAL THAT ULH&P WOULD MAKE FOR 2005 IF APPROVED BY THE COMMISSION IN THIS PROCEEDING?

A. ULH&P estimates that it will incur $1.54 million for Schedule 10, Schedule 10-FERC, Schedule 16 and Schedule 17 costs for 2005. This amount is based on the assumption that the MISO Day 2 markets would become operational by April 1, 2005, as currently scheduled. In future years, the estimated cost would be higher, simply because the MISO Day 2 markets would then be in effect for the full year. My estimate does not include congestion costs because these costs cannot be reasonably estimated at this time.

IV. CONCLUSION

Q. DOES THIS CONCLUDE YOUR PREPARED DIRECT TESTIMONY?

A. Yes.

VERIFICATION

State of Ohio)
) SS:
County of Hamilton)

The undersigned, Paul K. Jett, being duly sworn, deposes and says that he is the Director, RTO Activities (effective March 1, 2005) for Cinergy Services, Inc., that he has personal knowledge of the matters set forth in the foregoing testimony, and that the answers contained therein are true and correct to the best of his information, knowledge and belief.

Paul K Jett

Paul K. Jett, Affiant

Subscribed and sworn to before me by PAUL K. JETT on this 2ND day of March, 2005.

John J. Finnigan Jr.

NOTARY PUBLIC

My Commission Expires:

JOHN J. FINNIGAN, JR. Attorney at Law
NOTARY PUBLIC, STATE OF OHIO
My commission has no expiration
date, Section 147.03 O.R.C.

NOTARIAL SEAL STATE OF OHIO

Summary of Charges and Credits Under MISO's TEMT Tariff

I. Charges and Credits Settled in the Day-Ahead Energy Market

A. Charge: Purchases from MISO in the Day-Ahead Energy Market

B. Credit: Sales to MISO in the Day-Ahead Energy Market

C. Charge: Bilateral Purchases Scheduled Day-Ahead

D. Credit: FTR Congestion Revnues

E. Charge: FRT Congestion Costs

F. Charge and Credit: FTR Auction Settlement

G. Charges and Credits: Virtual Bids and Offers in the Day-Ahead Market

H. Credit: Day-Ahead Recovery of Unit Commitment Costs

I. Credit: Excess Congestion Charge Fund Credit

J. Credit: Real-Time Marginal Losses Surplus Credit

II. Charges and Credits Settled in the Real-Time Energy Market

A. Charge: Purchases from MISO in the Real-Time Energy Market

B. Credit: Sale to MISO in the Real-Time Energy Market

C. Charge: Bilateral Purchases Scheduled Real-Time

D. Credit: Recovery of Unit Commitment Costs

E. Credit: Marginal Losses Surplus Credit

F. Charge or Credit: Inadvertent Energy Charge or Credit

III. MISO Administrative Adders

A. Charge: MISO OATT Administrative Adder Costs

B. Charge: FTR Administrative Service Cost Recovery Adder

C. Charge: Energy Market Support Administrative Service Cost Recovery Adder

D. MISO FERC Schedule 10 Administrative Adder Costs

IV. Other Charges and Credits

A. Charge: Day-Ahead Revenue Sufficiency Charge

B. Charge: Real-Time Revenue Sufficiency Guarantee Charge

C. Charge: Uninstructed Deviation Penalties

D. Credit: Revenue From Uninstructed Deviation Penalties

E. Charge and Credit: Costs for Rescheduled Planned Generator Outages

F. Charge: Control Area Operations Costs

G. Charge: Other Internal Costs

H. Charge or Credit: Miscellaneous Penalty