

VECTREN UTILITY HOLDINGS INC
Form 10-Q
November 09, 2007

**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549**

FORM 10-Q

(Mark One)

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE
SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended September 30, 2007

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE
SECURITIES EXCHANGE ACT OF 1934

For the transition period from _____ to _____

Commission file number: **1-16739**

VECTREN UTILITY HOLDINGS, INC.
(Exact name of registrant as specified in its charter)

INDIANA **35-2104850**
(State or other jurisdiction of incorporation or (IRS Employer Identification No.)
organization)

**One Vectren Square,
Evansville, Indiana,
47708**
(Address of principal executive offices)
(Zip Code)

812-491-4000
(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

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Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of “accelerated filer and large accelerated filer” in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer Accelerated filer Non-accelerated filer

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes No

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

<u>Common Stock- Without Par Value</u>	<u>10</u>	<u>October 31, 2007</u>
Class	Number of Shares	Date

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Access to Information

Vectren Corporation makes available all SEC filings and recent annual reports free of charge, including those of its wholly owned subsidiaries, through its website at www.vectren.com, or by request, directed to Investor Relations at the mailing address, phone number, or email address that follows:

Mailing Address:	Phone Number:	Investor Relations Contact:
One Vectren Square	(812) 491-4000	Steven M. Schein
Evansville, Indiana 47708		Vice President, Investor Relations

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Definitions

AFUDC: allowance for funds used during construction	MMBTU: millions of British thermal units
APB: Accounting Principles Board	MW: megawatts
EITF: Emerging Issues Task Force	MWh / GWh: megawatt hours / thousands of megawatt hours (gigawatt hours)
FASB: Financial Accounting Standards Board	NOx: nitrogen oxide
FERC: Federal Energy Regulatory Commission	OCC: Ohio Office of the Consumer Counselor
IDEM: Indiana Department of Environmental Management	OUCC: Indiana Office of the Utility Consumer Counselor
IURC: Indiana Utility Regulatory Commission	PUCO: Public Utilities Commission of Ohio
MCF / BCF: thousands / billions of cubic feet	SFAS: Statement of Financial Accounting Standards
MDth / MMDth: thousands / millions of dekatherms	USEPA: United States Environmental Protection Agency
MISO: Midwest Independent System Operator	Throughput: combined gas sales and gas transportation volumes

Table of Contents**PART I. FINANCIAL INFORMATION****ITEM 1. FINANCIAL STATEMENTS**

VECTREN UTILITY HOLDINGS, INC. AND SUBSIDIARY COMPANIES
CONSOLIDATED CONDENSED BALANCE SHEETS
(Unaudited – In millions)

	September 30, 2007	December 31, 2006
<u>ASSETS</u>		
Current Assets		
Cash & cash equivalents	\$ 7.0	\$ 28.5
Accounts receivable - less reserves of \$3.2 & \$2.6, respectively	78.9	134.8
Receivables due from other Vectren companies	0.8	0.3
Accrued unbilled revenues	43.9	121.4
Inventories	170.2	141.9
Recoverable fuel & natural gas costs	-	1.8
Prepayments & other current assets	117.0	103.2
Total current assets	417.8	531.9
Utility Plant		
Original cost	3,990.8	3,820.2
Less: accumulated depreciation & amortization	1,499.1	1,434.7
Net utility plant	2,491.7	2,385.5
Investments in unconsolidated affiliates	0.2	0.2
Other investments	21.7	21.4
Nonutility property - net	174.7	163.1
Goodwill - net	205.0	205.0
Regulatory assets	138.1	116.8
Other assets	10.7	16.9
TOTAL ASSETS	\$ 3,459.9	\$ 3,440.8

The accompanying notes are an integral part of these consolidated condensed financial statements.

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VECTREN UTILITY HOLDINGS, INC. AND SUBSIDIARY COMPANIES
CONSOLIDATED CONDENSED BALANCE SHEETS
(Unaudited – In millions)

	September 30, 2007	December 31, 2006
<u>LIABILITIES & SHAREHOLDER'S EQUITY</u>		
Current Liabilities		
Accounts payable	\$ 118.0	\$ 136.2
Accounts payable to affiliated companies	29.9	68.2
Payables to other Vectren companies	24.8	25.3
Refundable fuel & natural gas costs	26.0	35.3
Accrued liabilities	113.9	115.8
Short-term borrowings	352.2	270.1
Current maturities of long-term debt	-	6.5
Long-term debt subject to tender	20.0	20.0
Total current liabilities	684.8	677.4
Long-Term Debt - Net of Current Maturities & Debt Subject to Tender		
	1,025.4	1,025.3
Deferred Income Taxes & Other Liabilities		
Deferred income taxes	264.7	282.2
Regulatory liabilities	303.1	291.1
Deferred credits & other liabilities	114.3	108.1
Total deferred credits & other liabilities	682.1	681.4
Commitments & Contingencies (Notes 8 - 10)		
Common Shareholder's Equity		
Common stock (no par value)	632.9	632.9
Retained earnings	434.2	422.9
Accumulated other comprehensive income	0.5	0.9
Total common shareholder's equity	1,067.6	1,056.7
TOTAL LIABILITIES & SHAREHOLDER'S EQUITY	\$ 3,459.9	\$ 3,440.8

The accompanying notes are an integral part of these consolidated condensed financial statements.

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VECTREN UTILITY HOLDINGS, INC. AND SUBSIDIARY COMPANIES
CONSOLIDATED CONDENSED STATEMENTS OF INCOME
(Unaudited – In millions)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2007	2006	2007	2006
OPERATING REVENUES				
Gas utility revenues	\$ 114.0	\$ 116.8	\$ 890.0	\$ 848.6
Electric utility revenues	143.6	123.2	361.6	324.4
Other revenues	0.4	0.5	1.3	1.4
Total operating revenues	258.0	240.5	1,252.9	1,174.4
OPERATING EXPENSES				
Cost of gas sold	52.9	59.9	592.0	577.4
Cost of fuel & purchased power	50.5	46.8	129.5	115.8
Other operating	65.6	61.6	198.4	182.8
Depreciation & amortization	40.4	38.0	119.4	112.8
Taxes other than income taxes	11.3	10.5	49.6	44.9
Total operating expenses	220.7	216.8	1,088.9	1,033.7
OPERATING INCOME	37.3	23.7	164.0	140.7
OTHER INCOME - NET	1.3	2.0	6.2	4.8
INTEREST EXPENSE	20.8	19.2	58.8	57.4
INCOME BEFORE INCOME TAXES	17.8	6.5	111.4	88.1
INCOME TAXES	7.1	-	41.8	31.1
NET INCOME	\$ 10.7	\$ 6.5	\$ 69.6	\$ 57.0

The accompanying notes are an integral part of these consolidated condensed financial statements.

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VECTREN UTILITY HOLDINGS, INC. AND SUBSIDIARY COMPANIES
CONSOLIDATED CONDENSED STATEMENTS OF CASH FLOWS
(Unaudited – In millions)

	Nine Months Ended September 30,	
	2007	2006
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income	\$ 69.6	\$ 57.0
Adjustments to reconcile net income to cash from operating activities:		
Depreciation & amortization	119.4	112.8
Deferred income taxes & investment tax credits	4.1	(0.4)
Expense portion of pension & postretirement periodic benefit cost	2.9	3.1
Provision for uncollectible accounts	11.5	11.2
Other non-cash charges - net	3.1	1.6
Changes in working capital accounts:		
Accounts receivable, including to Vectren companies		
& accrued unbilled revenue	121.4	268.2
Inventories	(28.3)	(38.9)
Recoverable/refundable fuel & natural gas costs	(7.5)	31.9
Prepayments & other current assets	(18.2)	(27.4)
Accounts payable, including to Vectren companies		
& affiliated companies	(59.9)	(145.0)
Accrued liabilities	(15.5)	(36.5)
Changes in noncurrent assets	(10.2)	(23.1)
Changes in noncurrent liabilities	(19.3)	-
Net cash flows from operating activities	173.1	214.5
CASH FLOWS FROM FINANCING ACTIVITIES		
Requirements for:		
Dividends to parent	(57.4)	(55.9)
Retirement of long-term debt	(6.5)	-
Net change in short-term borrowings	82.1	0.7
Net cash flows from financing activities	18.2	(55.2)
CASH FLOWS FROM INVESTING ACTIVITIES		
Proceeds from other investing activities	0.3	0.1
Requirements for: Capital expenditures, excluding AFUDC-equity	(213.1)	(168.2)
Net cash flows from investing activities	(212.8)	(168.1)
Net decrease in cash & cash equivalents	(21.5)	(8.8)
Cash & cash equivalents at beginning of period	28.5	11.7
Cash & cash equivalents at end of period	\$ 7.0	\$ 2.9

The accompanying notes are an integral part of these consolidated condensed financial statements.

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**VECTREN UTILITY HOLDINGS, INC. AND SUBSIDIARY COMPANIES
NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS
(UNAUDITED)**

1. Organization and Nature of Operations

Vectren Utility Holdings, Inc. (Utility Holdings or the Company), an Indiana corporation, serves as the intermediate holding company for Vectren Corporation's (Vectren) three operating public utilities: Indiana Gas Company, Inc. (Indiana Gas or Vectren North), Southern Indiana Gas and Electric Company (SIGECO or Vectren South), and the Ohio operations. Utility Holdings also has other assets that provide information technology and other services to the three utilities. Vectren is an energy holding company headquartered in Evansville, Indiana. Vectren and Utility Holdings are holding companies as defined by the Energy Policy Act of 2005.

Indiana Gas provides energy delivery services to approximately 565,000 natural gas customers located in central and southern Indiana. SIGECO provides energy delivery services to approximately 141,000 electric customers and approximately 112,000 gas customers located near Evansville in southwestern Indiana. SIGECO also owns and operates electric generation to serve its electric customers and optimizes those assets in the wholesale power market. Indiana Gas and SIGECO generally do business as Vectren Energy Delivery of Indiana. The Ohio operations provide energy delivery services to approximately 318,000 natural gas customers located near Dayton in west central Ohio. The Ohio operations are owned as a tenancy in common by Vectren Energy Delivery of Ohio, Inc. (VEDO), a wholly owned subsidiary, (53% ownership) and Indiana Gas (47% ownership). The Ohio operations generally do business as Vectren Energy Delivery of Ohio.

2. Basis of Presentation

The interim consolidated condensed financial statements included in this report have been prepared by the Company, without audit, as provided in the rules and regulations of the Securities and Exchange Commission. Certain information and note disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States have been omitted as provided in such rules and regulations. The Company believes that the information in this report reflects all adjustments necessary to fairly state the results of the interim periods reported. These consolidated condensed financial statements and related notes should be read in conjunction with the Company's audited annual consolidated financial statements for the year ended December 31, 2006, filed with the SEC February 27, 2007 on Form 10-K. Because of the seasonal nature of the Company's utility operations, the results shown on a quarterly basis are not necessarily indicative of annual results.

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the statements and the reported amounts of revenues and expenses during the reporting periods. Actual results could differ from those estimates.

3. Subsidiary Guarantor and Consolidating Information

The Company's three operating utility companies, SIGECO, Indiana Gas, and VEDO are guarantors of Utility Holdings' \$515 million in short-term credit facilities, of which \$352.5 million is outstanding at September 30, 2007, and Utility Holdings' \$700 million unsecured senior notes outstanding at September 30, 2007. The guarantees are full and unconditional and joint and several, and Utility Holdings has no subsidiaries other than the subsidiary guarantors. However, Utility Holdings does have operations other than those of the subsidiary guarantors. Pursuant to Article 3-10 of Regulation S-X, disclosure of the results of operations and balance sheets of the subsidiary guarantors separate from the parent company's operations is required. Following are consolidating financial

statements including information on the combined operations of the subsidiary guarantors separate from the other operations of the parent company.

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Condensed Consolidating Statement of Income for the three months ended September 30, 2007 (in millions):

	Subsidiary Guarantors	Parent Company	Eliminations & Reclassifications	Consolidated
OPERATING REVENUES				
Gas utility revenues	\$ 114.0	\$ -	\$ -	\$ 114.0
Electric utility revenues	143.6	-	-	143.6
Other revenues	-	10.1	(9.7)	0.4
Total operating revenues	257.6	10.1	(9.7)	258.0
OPERATING EXPENSES				
Cost of gas sold	52.9	-	-	52.9
Cost of fuel & purchased power	50.5	-	-	50.5
Other operating	74.3	-	(8.7)	65.6
Depreciation & amortization	34.5	5.8	0.1	40.4
Taxes other than income taxes	10.1	1.2	-	11.3
Total operating expenses	222.3	7.0	(8.6)	220.7
OPERATING INCOME	35.3	3.1	(1.1)	37.3
OTHER INCOME (EXPENSE) - NET				
Equity in earnings of consolidated companies	-	10.2	(10.2)	-
Other income (expense) – net	(0.2)	12.1	(10.6)	1.3
Total other income (expense) - net	(0.2)	22.3	(20.8)	1.3
Interest expense	17.7	14.8	(11.7)	20.8
INCOME BEFORE INCOME TAXES	17.4	10.6	(10.2)	17.8
Income taxes	7.2	(0.1)	-	7.1
NET INCOME	\$ 10.2	\$ 10.7	\$ (10.2)	\$ 10.7

Condensed Consolidating Statement of Income for the three months ended September 30, 2006 (in millions):

	Subsidiary Guarantors	Parent Company	Eliminations & Reclassifications	Consolidated
OPERATING REVENUES				
Gas utility revenues	\$ 116.8	\$ -	\$ -	\$ 116.8
Electric utility revenues	123.2	-	-	123.2
Other revenues	-	9.2	(8.7)	0.5
Total operating revenues	240.0	9.2	(8.7)	240.5
OPERATING EXPENSES				
Cost of gas sold	59.9	-	-	59.9
Cost of fuel & purchased power	46.8	-	-	46.8
Other operating	69.9	-	(8.3)	61.6
Depreciation & amortization	32.4	5.5	0.1	38.0
Taxes other than income taxes	10.2	0.3	-	10.5
Total operating expenses	219.2	5.8	(8.2)	216.8
OPERATING INCOME	20.8	3.4	(0.5)	23.7
OTHER INCOME (EXPENSE) - NET				
Equity in earnings of consolidated companies	-	4.0	(4.0)	-
Other income (expense) – net	1.3	10.6	(9.9)	2.0
Total other income (expense) - net	1.3	14.6	(13.9)	2.0
Interest expense	16.4	13.2	(10.4)	19.2
INCOME BEFORE INCOME TAXES	5.7	4.8	(4.0)	6.5
Income taxes	1.7	(1.7)	-	-

NET INCOME	\$	4.0	\$	6.5	\$	(4.0)	\$	6.5
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Condensed Consolidating Statement of Income for the nine months ended September 30, 2007 (in millions):

	Subsidiary Guarantors	Parent Company	Eliminations & Reclassifications	Consolidated
OPERATING REVENUES				
Gas utility revenues	\$ 890.0	\$ -	\$ -	\$ 890.0
Electric utility revenues	361.6	-	-	361.6
Other revenues	-	30.3	(29.0)	1.3
Total operating revenues	1,251.6	30.3	(29.0)	1,252.9
OPERATING EXPENSES				
Cost of gas sold	592.0	-	-	592.0
Cost of fuel & purchased power	129.5	-	-	129.5
Other operating	224.2	-	(25.8)	198.4
Depreciation & amortization	101.8	17.3	0.3	119.4
Taxes other than income taxes	47.7	1.8	0.1	49.6
Total operating expenses	1,095.2	19.1	(25.4)	1,088.9
OPERATING INCOME	156.4	11.2	(3.6)	164.0
OTHER INCOME (EXPENSE) - NET				
Equity in earnings of consolidated companies	-	65.6	(65.6)	-
Other income (expense) – net	2.5	33.5	(29.8)	6.2
Total other income (expense) - net	2.5	99.1	(95.4)	6.2
Interest expense	50.6	41.6	(33.4)	58.8
INCOME BEFORE INCOME TAXES	108.3	68.7	(65.6)	111.4
Income taxes	42.7	(0.9)	-	41.8
NET INCOME	\$ 65.6	\$ 69.6	\$ (65.6)	\$ 69.6

Condensed Consolidating Statement of Income for the nine months ended September 30, 2006 (in millions):

	Subsidiary Guarantors	Parent Company	Eliminations & Reclassifications	Consolidated
OPERATING REVENUES				
Gas utility revenues	\$ 848.6	\$ -	\$ -	\$ 848.6
Electric utility revenues	324.4	-	-	324.4
Other revenues	-	27.5	(26.1)	1.4
Total operating revenues	1,173.0	27.5	(26.1)	1,174.4
OPERATING EXPENSES				
Cost of gas sold	577.4	-	-	577.4
Cost of fuel & purchased power	115.8	-	-	115.8
Other operating	206.9	-	(24.1)	182.8
Depreciation & amortization	96.6	16.1	0.1	112.8
Taxes other than income taxes	44.0	0.8	0.1	44.9
Total operating expenses	1,040.7	16.9	(23.9)	1,033.7
OPERATING INCOME	132.3	10.6	(2.2)	140.7
OTHER INCOME (EXPENSE) - NET				
Equity in earnings of consolidated companies	-	52.3	(52.3)	-
Other income (expense) – net	2.2	31.1	(28.5)	4.8
Total other income (expense) - net	2.2	83.4	(80.8)	4.8
Interest expense	49.3	38.8	(30.7)	57.4
INCOME BEFORE INCOME TAXES	85.2	55.2	(52.3)	88.1
Income taxes	32.9	(1.8)	-	31.1

NET INCOME	\$	52.3	\$	57.0	\$	(52.3)	\$	57.0
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Condensed Consolidating Statement of Cash Flows for the nine months ended September 30, 2007 (in millions):

	Subsidiary Guarantors	Parent Company	Eliminations	Consolidated
NET CASH FLOWS FROM OPERATING ACTIVITIES	\$ 144.3	\$ 28.8	\$ -	\$ 173.1
CASH FLOWS FROM FINANCING ACTIVITIES				
Requirements for:				
Dividends to parent	(57.4)	(57.4)	57.4	(57.4)
Retirement of long-term debt	(6.5)	-	-	(6.5)
Net change in short-term borrowings	105.2	82.1	(105.2)	82.1
Net cash flows from financing activities	41.3	24.7	(47.8)	18.2
CASH FLOWS FROM INVESTING ACTIVITIES				
Proceeds from:				
Consolidated subsidiary distributions	-	57.4	(57.4)	-
Other investing activities	-	0.3	-	0.3
Requirements for:				
Capital expenditures, excluding AFUDC-equity	(186.2)	(26.9)	-	(213.1)
Net change in notes receivable to other Vectren companies	-	(105.2)	105.2	-
Net cash flows from investing activities	(186.2)	(74.4)	47.8	(212.8)
Net decrease in cash & cash equivalents	(0.6)	(20.9)	-	(21.5)
Cash & cash equivalents at beginning of period	5.7	22.8	-	28.5
Cash & cash equivalents at end of period	\$ 5.1	\$ 1.9	\$ -	\$ 7.0

Condensed Consolidating Statement of Cash Flows for the nine months ended September 30, 2006 (in millions):

	Subsidiary Guarantors	Parent Company	Eliminations	Consolidated
NET CASH FLOWS FROM OPERATING ACTIVITIES	\$ 211.7	\$ 2.8	\$ -	\$ 214.5
CASH FLOWS FROM FINANCING ACTIVITIES				
Proceeds from:				
Additional capital contribution	20.0	-	(20.0)	-
Long-term debt - net of issuance costs & hedging proceeds	150.0	-	(150.0)	-
Requirements for:				
Dividends to parent	(55.9)	(55.9)	55.9	(55.9)
Net change in short-term borrowings	(183.9)	0.7	183.9	0.7
Net cash flows from financing activities	(69.8)	(55.2)	69.8	(55.2)
CASH FLOWS FROM INVESTING ACTIVITIES				
Proceeds from:				
Consolidated subsidiary distributions	-	55.9	(55.9)	-
Other investing activities	-	0.1	-	0.1
Requirements for:				

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Capital expenditures, excluding AFUDC-equity	(150.7)	(17.5)	-	(168.2)
Consolidated affiliate and other investments	-	(170.0)	170.0	-
Net change in notes receivable to other Vectren companies	-	183.9	(183.9)	-
Net cash flows from investing activities	(150.7)	52.4	(69.8)	(168.1)
Net decrease in cash & cash equivalents	(8.8)	-		(8.8)
Cash & cash equivalents at beginning of period	11.0	0.7		11.7
Cash & cash equivalents at end of period	\$ 2.2	\$ 0.7	\$ -	\$ 2.9

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Condensed Consolidating Balance Sheet as of September 30, 2007 (in millions):

<u>ASSETS</u>	Subsidiary Guarantors	Parent Company	Eliminations	Consolidated
Current Assets				
Cash & cash equivalents	\$ 5.1	\$ 1.9	\$ -	\$ 7.0
Accounts receivable - less reserves	78.9	-	-	78.9
Receivables due from other Vectren companies	0.4	251.2	(250.8)	0.8
Accrued unbilled revenues	43.9	-	-	43.9
Inventories	169.3	0.9	-	170.2
Prepayments & other current assets	109.0	10.6	(2.6)	117.0
Total current assets	406.6	264.6	(253.4)	417.8
Utility Plant				
Original cost	3,990.8	-	-	3,990.8
Less: accumulated depreciation & amortization	1,499.1	-	-	1,499.1
Net utility plant	2,491.7	-	-	2,491.7
Investments in consolidated subsidiaries	-	1,137.7	(1,137.7)	-
Notes receivable from consolidated subsidiaries	-	575.4	(575.4)	-
Investments in unconsolidated affiliates	0.2	-	-	0.2
Other investments	15.9	5.8	-	21.7
Nonutility property - net	5.5	169.2	-	174.7
Goodwill - net	205.0	-	-	205.0
Regulatory assets	125.4	12.7	-	138.1
Other assets	15.0	0.3	(4.6)	10.7
TOTAL ASSETS	\$ 3,265.3	\$ 2,165.7	\$ (1,971.1)	\$ 3,459.9

LIABILITIES & SHAREHOLDER'S

<u>EQUITY</u>	Subsidiary Guarantors	Parent Company	Eliminations	Consolidated
Current Liabilities				
Accounts payable	\$ 108.8	\$ 9.2	\$ -	\$ 118.0
Accounts payable to affiliated companies	29.9	-	-	29.9
Payables to other Vectren companies	34.3	0.3	(9.8)	24.8
Refundable fuel & natural gas costs	26.0	-	-	26.0
Accrued liabilities	106.1	14.5	(6.7)	113.9
Short-term borrowings	-	352.2	-	352.2
Short-term borrowings from other Vectren Companies	236.9	-	(236.9)	-
Long-term debt subject to tender	20.0	-	-	20.0
Total current liabilities	562.0	376.2	(253.4)	684.8
Long-Term Debt				
Long-term debt - net of current maturities & debt subject to tender	327.2	698.2	-	1,025.4
Long-term debt due to Utility Holdings	575.4	-	(575.4)	-
Total long-term debt - net	902.6	698.2	(575.4)	1,025.4
Deferred Income Taxes & Other Liabilities				
Deferred income taxes	255.1	9.6	-	264.7
Regulatory liabilities	300.8	2.3	-	303.1
Deferred credits & other liabilities	107.1	11.8	(4.6)	114.3

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Total deferred credits & other liabilities	663.0	23.7	(4.6)	682.1
Common Shareholder's Equity				
Common stock (no par value)	776.3	632.9	(776.3)	632.9
Retained earnings	360.9	434.2	(360.9)	434.2
Accumulated other comprehensive income	0.5	0.5	(0.5)	0.5
Total common shareholder's equity	1,137.7	1,067.6	(1,137.7)	1,067.6
TOTAL LIABILITIES & SHAREHOLDER'S EQUITY	\$ 3,265.3	\$ 2,165.7	\$ (1,971.1)	\$ 3,459.9

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Condensed Consolidating Balance Sheet as of December 31, 2006 (in millions):

<u>ASSETS</u>	Subsidiary Guarantors	Parent Company	Eliminations	Consolidated
Current Assets				
Cash & cash equivalents	\$ 5.7	\$ 22.8	\$ -	\$ 28.5
Accounts receivable - less reserves	134.8	-	-	134.8
Receivables due from other Vectren companies	6.1	146.0	(151.8)	0.3
Accrued unbilled revenues	121.4	-	-	121.4
Inventories	139.6	2.3	-	141.9
Recoverable fuel & natural gas costs	1.8	-	-	1.8
Prepayments & other current assets	91.2	14.7	(2.7)	103.2
Total current assets	500.6	185.8	(154.5)	531.9
Utility Plant				
Original cost	3,820.2	-	-	3,820.2
Less: accumulated depreciation & amortization	1,434.7	-	-	1,434.7
Net utility plant	2,385.5	-	-	2,385.5
Investments in consolidated subsidiaries	-	1,129.7	(1,129.7)	-
Notes receivable from consolidated subsidiaries	-	575.3	(575.3)	-
Investments in unconsolidated affiliates	0.2	-	-	0.2
Other investments	15.4	6.0	-	21.4
Nonutility property - net	5.2	157.9	-	163.1
Goodwill - net	205.0	-	-	205.0
Regulatory assets	103.3	13.5	-	116.8
Other assets	16.1	0.8	-	16.9
TOTAL ASSETS	\$ 3,231.3	\$ 2,069.0	\$ (1,859.5)	\$ 3,440.8

LIABILITIES & SHAREHOLDER'S EQUITY

	Subsidiary Guarantors	Parent Company	Eliminations	Consolidated
Current Liabilities				
Accounts payable	\$ 131.5	\$ 4.7	\$ -	\$ 136.2
Accounts payable to affiliated companies	68.1	0.1	-	68.2
Payables to other Vectren companies	44.0	0.1	(18.8)	25.3
Refundable fuel & natural gas costs	35.3	-	-	35.3
Accrued liabilities	107.3	11.2	(2.7)	115.8
Short-term borrowings	-	270.1	-	270.1
Short-term borrowings from other Vectren Companies	133.0	-	(133.0)	-
Current maturities of long-term debt	6.5	-	-	6.5
Long-term debt subject to tender	20.0	-	-	20.0
Total current liabilities	545.7	286.2	(154.5)	677.4
Long-Term Debt				
Long-term debt - net of current maturities & debt subject to tender	327.3	698.0	-	1,025.3
Long-term debt due to Utility Holdings	575.3	-	(575.3)	-
Total long-term debt - net	902.6	698.0	(575.3)	1,025.3
Deferred Income Taxes & Other Liabilities				
Deferred income taxes	265.9	16.3	-	282.2
Regulatory liabilities	285.0	6.1	-	291.1
Deferred credits & other liabilities	102.4	5.7	-	108.1
Total deferred credits & other liabilities	653.3	28.1	-	681.4
Common Shareholder's Equity				

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Common stock (no par value)	776.3	632.9	(776.3)	632.9
Retained earnings	352.5	422.9	(352.5)	422.9
Accumulated other comprehensive income	0.9	0.9	(0.9)	0.9
Total common shareholder's equity	1,129.7	1,056.7	(1,129.7)	1,056.7
TOTAL LIABILITIES & SHAREHOLDER'S EQUITY	\$ 3,231.3	\$ 2,069.0	\$ (1,859.5)	\$ 3,440.8

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Table of Contents**4. Excise and Utility Receipts Taxes**

Excise taxes and a portion of utility receipts taxes are included in rates charged to customers. Accordingly, the Company records these taxes received as a component of operating revenues, which totaled \$4.9 million and \$4.7 million, respectively for the three months ended September 30, 2007 and 2006. For the nine months ended September 30, 2007 and 2006, these taxes totaled \$29.6 million and \$27.9 million, respectively. Expenses associated with excise and utility receipts taxes are recorded as a component of *Taxes other than income taxes*.

5. Comprehensive Income

Comprehensive income consists of the following:

<i>(In millions)</i>	Three Months Ended September 30,		Nine Months Ended September 30,	
	2007	2006	2007	2006
Net income	\$ 10.7	\$ 6.5	\$ 69.6	\$ 57.0
Cash flow hedges				
Unrealized losses	-	-	-	(3.7)
Reclassifications to net income	(0.1)	(0.1)	(0.7)	(2.2)
Income tax benefit (expense)	-	-	0.3	2.1
Total comprehensive income	\$ 10.6	\$ 6.4	\$ 69.2	\$ 53.2

6. Transactions with Other Vectren CompaniesSupport Services and Purchases

Vectren provides corporate and general and administrative services to the Company and allocates costs to the Company, including costs for share-based compensation and for pension and other postretirement benefits that are not directly charged to subsidiaries. These costs have been allocated using various allocators, including number of employees, number of customers and/or the level of payroll, revenue contribution and capital expenditures. Allocations are based on cost. Utility Holdings received corporate allocations totaling \$20.7 million and \$17.7 million for the three months ended September 30, 2007 and 2006, respectively. For the nine months ended September 30, 2007 and 2006, Utility Holdings received corporate allocations totaling \$63.0 million and \$58.4 million, respectively.

Vectren Fuels, Inc.

Vectren Fuels, Inc., a wholly owned subsidiary of Vectren, owns and operates coal mines from which SIGECO purchases fuel used for electric generation. The Company has priced the coal consistent with letter agreements with the OUCC regarding the price of coal that is charged by Fuels to SIGECO. Amounts paid for such purchases for the three months ended September 30, 2007 and 2006, totaled \$30.3 million and \$28.9 million, respectively. For the nine months ended September 30, 2007 and 2006, amounts paid for such purchases totaled \$86.4 million and \$91.4 million, respectively.

Miller Pipeline Corporation

Effective July 1, 2006, Vectren purchased the remaining 50% ownership in Miller Pipeline Corporation (Miller), making Miller a wholly owned subsidiary of Vectren. Prior to the transaction, Miller was 50% owned by Duke Energy Corporation. Miller performs natural gas and water distribution, transmission, and construction repair and rehabilitation primarily in the Midwest and the repair and rehabilitation of gas, water, and wastewater facilities nationwide. Miller's customers include Utility Holdings' utilities. Amounts paid by Utility Holdings to Miller for purchases of utility plant and other services for the three months ended September 30, 2007 and 2006, totaled \$16.6 million and \$5.2 million, respectively. Amounts paid for the nine months ended September 30, 2007 and 2006,

totaled \$28.1 million and \$14.4 million, respectively.

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7. Transactions with ProLiance Energy, LLC

ProLiance Energy, LLC (ProLiance), a nonutility energy marketing affiliate of Vectren and Citizens Gas and Coke Utility (Citizens Gas), provides services to a broad range of municipalities, utilities, industrial operations, schools, and healthcare institutions located throughout the Midwest and Southeast United States. ProLiance also provides services to Vectren's Indiana utilities and nonutility gas supply operations as well as Citizens Gas. ProLiance's primary businesses include gas marketing, gas portfolio optimization, and other portfolio and energy management services.

Purchases from ProLiance for resale and for injections into storage for the three months ended September 30, 2007 and 2006, totaled \$111.0 million and \$107.2 million, respectively and for the nine months ended September 30, 2007 and 2006, totaled \$452.3 million and \$451.2 million, respectively. Amounts owed to ProLiance at September 30, 2007 and December 31, 2006, for those purchases were \$29.5 million and \$68.2 million, respectively, and are included in *Accounts payable to affiliated companies* in the Consolidated Balance Sheets. The Company purchased approximately 70 percent of its gas through ProLiance in 2007 and approximately 71 percent in 2006. Amounts charged by ProLiance for gas supply services are established by supply agreements with each utility which have been approved by the IURC through 2011.

8. Commitments & Contingencies

The Company is party to various legal proceedings arising in the normal course of business. In the opinion of management, there are no legal proceedings, except those discussed herein, pending against the Company that are likely to have a material adverse effect on its financial position or results of operations or cash flows.

9. Environmental Matters

Clean Air/Climate Change

In March of 2005 USEPA finalized two new air emission reduction regulations. The Clean Air Interstate Rule (CAIR) is an allowance cap and trade program requiring further reductions in Nitrogen Oxides (NO_x) and Sulfur Dioxide (SO₂) emissions from coal-burning power plants. The Clean Air Mercury Rule (CAMR) is an allowance cap and trade program requiring further reductions in mercury emissions from coal-burning power plants. Both sets of regulations require emission reductions in two phases. The first phase deadline for both rules is 2010 (2009 for NO_x under CAIR), and the second phase deadline for compliance with the emission reductions required under CAIR is 2015, while the second phase deadline for compliance with the emission reduction requirements of CAMR is 2018. The Company is evaluating compliance options and fully expects to be in compliance by the required deadlines.

In February 2006, the IURC approved a multi-emission compliance plan filed by the Company's utility subsidiary, SIGECO. Once the plan is implemented, SIGECO's coal-fired plants will be 100% scrubbed for SO₂, 90% scrubbed for NO_x, and mercury emissions will be reduced to meet the new mercury reduction standards. The order, as previously agreed to by the OUCC and Citizens Action Coalition, allows SIGECO to recover an approximate 8% return on up to \$110 million in capital investments through a rider mechanism which is updated every six months for actual costs incurred. The Company may file periodic updates with the IURC requesting modification to the spending authority. The Company will also recover through a rider its operating expenses, including depreciation, once the equipment is placed into service. As of September 30, 2007, the Company has made capital investments of approximately \$91 million related to this environmental requirement. Of that amount, \$49.4 million was placed into service on January 1, 2007 and was included in rate base for purposes of determining new base rates that went into effect on August 15, 2007 (See Note 10).

If legislation requiring reductions in carbon dioxide and other greenhouse gases is adopted, such regulation could substantially affect both the costs and operating characteristics of the Company's fossil fuel generating plants and nonutility coal mining operations. At this time and in absence of final legislation, compliance costs and other effects associated with reductions in greenhouse gas emissions remain uncertain.

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Pursuant to an IURC order, SIGECO is studying renewable energy alternatives, and on April 9, 2007, filed a green power rider in order to allow customers to purchase green power and is also seeking approval of a contract to purchase 30 MW of power generated by wind energy. Future filings with the IURC with regard to new generation and/or further environmental compliance plans will include evaluation of potential carbon requirements.

Environmental Remediation Efforts

In the past, Indiana Gas, SIGECO, and others operated facilities for the manufacture of gas. Given the availability of natural gas transported by pipelines, these facilities have not been operated for many years. Under currently applicable environmental laws and regulations, those that operated these facilities may now be required to take remedial action if certain contaminants are found above the regulatory thresholds at these sites.

Indiana Gas identified the existence, location, and certain general characteristics of 26 gas manufacturing and storage sites for which it may have some remedial responsibility. Indiana Gas completed a remedial investigation/feasibility study (RI/FS) at one of the sites under an agreed order between Indiana Gas and the IDEM, and a Record of Decision was issued by the IDEM in January 2000. Although Indiana Gas has not begun an RI/FS at additional sites, Indiana Gas has submitted several of the sites to the IDEM's Voluntary Remediation Program (VRP) and is currently conducting some level of remedial activities, including groundwater monitoring at certain sites, where deemed appropriate, and will continue remedial activities at the sites as appropriate and necessary.

Indiana Gas accrued the estimated costs for further investigation, remediation, groundwater monitoring, and related costs for the sites. While the total costs that may be incurred in connection with addressing these sites cannot be determined at this time, Indiana Gas has recorded costs that it reasonably expects to incur totaling approximately \$20.4 million.

The estimated accrued costs are limited to Indiana Gas' share of the remediation efforts. Indiana Gas has arrangements in place for 19 of the 26 sites with other potentially responsible parties (PRP), which serve to limit Indiana Gas' share of response costs at these 19 sites to between 20% and 50%. With respect to insurance coverage, Indiana Gas has received and recorded settlements from all known insurance carriers under insurance policies in effect when these plants were in operation in an aggregate amount approximating \$20.4 million.

In October 2002, SIGECO received a formal information request letter from the IDEM regarding five manufactured gas plants that it owned and/or operated and were not enrolled in the IDEM's VRP. In October 2003, SIGECO filed applications to enter four of the manufactured gas plant sites in IDEM's VRP. The remaining site is currently being addressed in the VRP by another Indiana utility. SIGECO added those four sites into the renewal of the global Voluntary Remediation Agreement that Indiana Gas has in place with IDEM for its manufactured gas plant sites. That renewal was approved by the IDEM in February 2004. SIGECO is also named in a lawsuit filed in federal district court in May 2007, involving another site subject to potential environmental remediation efforts.

SIGECO has filed a declaratory judgment action against its insurance carriers seeking a judgment finding its carriers liable under the policies for coverage of further investigation and any necessary remediation costs that SIGECO may accrue under the VRP program and/or related to the site subject to the May 2007 lawsuit. While the total costs that may be incurred in connection with addressing these sites cannot be determined at this time, SIGECO has recorded costs that it reasonably expects to incur totaling approximately \$7.7 million. With respect to insurance coverage, SIGECO has received and recorded settlements from insurance carriers under insurance policies in effect when these sites were in operation in an aggregate amount approximating the costs it expects to incur.

Environmental remediation costs related to Indiana Gas' and SIGECO's manufactured gas plants and other sites have had no material impact on results of operations or financial condition since costs recorded to date approximate PRP and insurance settlement recoveries. While the Company's utilities have recorded all costs which they presently expect to incur in connection with activities at these sites, it is possible that future events may require some level of

additional remedial activities which are not presently foreseen and those costs may not be subject to PRP or insurance recovery.

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10. Rate & Regulatory Matters

Vectren South (SIGECO) Electric Base Rate Order Received

On August 15, 2007, the Company received an order from the IURC which approved a settlement agreement with the OUCC and other interveners regarding the proposed changes to the base rates and charges for its electric distribution business in southwestern Indiana. The settlement agreement provides for an approximate \$60.8 million electric rate increase to cover the Company's cost of system growth, maintenance, safety and reliability. The settlement provides for, among other things: recovery of ongoing costs and deferred costs associated with the MISO; operations and maintenance (O&M) expense increases related to managing the aging workforce, including the development of expanded apprenticeship programs and the creation of defined training programs to ensure proper knowledge transfer, safety and system stability; increased O&M expense necessary to maintain and improve system reliability; benefit to customers from the sale of wholesale power by Vectren sharing evenly with customers any profit earned above or below \$10.5 million of wholesale power margin; recovery of and return on the investment in past demand side management programs to help encourage conservation during peak load periods; timely recovery of the Company's investment in certain new electric transmission projects that benefit the MISO infrastructure outside of the Company's service territory; an overall rate of return of 7.32 percent on rate base of approximately \$1,044 million and an allowed return on equity (ROE) of 10.4 percent.

Vectren South (SIGECO) Gas Base Rate Order Received

On August 1, 2007, the Company received an order from the IURC which approved, with a minor modification, the settlement agreement previously reached with the Indiana Office of the Utility Consumer Counselor (OUCC) and other interveners regarding its Vectren South gas rate case. The order provided for a base rate increase of \$5.1 million and an ROE of 10.15 percent, with an overall rate of return of 7.20 percent on rate base of approximately \$122 million. The order also includes removal of \$2.6 million of costs from base rates to be recovered through existing tracking mechanisms.

Further, additional expenditures for a multi-year bare steel and cast iron capital replacement program will be afforded certain accounting treatment that mitigates earnings attrition from the investment between rate cases. The accounting treatment allows for the continuation of the accrual for allowance for funds used during construction (AFUDC) and the deferral of depreciation expense after the projects go in service but before they are included in base rates. To qualify for this treatment, the annual expenditures are limited to \$3.0 million and the treatment cannot extend beyond three years on each project.

With this order, the company now has in place for its South gas territory weather normalization, a conservation and decoupling tariff, tracking of gas cost expense related to bad debts and unaccounted for gas through the existing gas cost adjustment mechanism, and tracking of pipeline integrity expense.

Vectren North (Indiana Gas Company, Inc.) Gas Base Rate Filing

In May 2007, the Company filed a petition with the IURC to adjust its gas base rates and charges in its North service territory. The petition requests an increase of approximately \$41 million in rates to recover the ongoing cost of operating, maintaining and expanding the approximately 12,000-mile distribution and storage system used to serve more than 565,000 natural gas customers. Components of the requested increase include return on additional utility infrastructure investment, costs associated with federally mandated pipeline integrity management, inspection and other reliability programs, and aging workforce. A hearing on the Company's request before the IURC was held in late August 2007 and the final hearing is scheduled for December 2007. The Company expects an order from the IURC in the second quarter of 2008.

Vectren Energy Delivery of Ohio, Inc. (VEDO) Filing of Pre-Filing Notice

In September 2007, the Company issued a pre-filing notice with the PUCO indicating it plans to request an increase in its base rate charges for VEDO's distribution business in its 17-county service area in west central Ohio. The filing indicates that an increase in base rates of approximately \$29 million is necessary to cover the ongoing cost of operating, maintaining and expanding the approximately 5,200-mile distribution system used to serve 318,000 customers. Components of the requested increase include return on additional utility infrastructure investment, costs associated with federally mandated pipeline integrity management, inspection and other reliability programs, and aging workforce.

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In addition, the Company is seeking extension of the decoupling mechanisms currently in place to encourage customer conservation and also is seeking approval of expanded conservation-oriented programs, such as rebate offerings on high-efficiency natural gas appliances for existing and new home construction, to help customers lower their natural gas bills.

Ohio and Indiana Lost Margin Recovery/Conservation Filings

In 2005, the Company filed conservation programs and conservation adjustment trackers in Indiana and Ohio designed to help customers conserve energy and reduce their annual gas bills. The programs allow the Company to recover costs of promoting the conservation of natural gas through conservation trackers that work in tandem with a lost margin recovery mechanism. These mechanisms are designed to allow the Company to recover the distribution portion of its rates from residential and commercial customers based on the level of customer revenues established in each utility's last general rate case.

Indiana

In December 2006, the IURC approved a settlement agreement that provides for a five-year energy efficiency program. It allows the Company's Indiana utilities to recover a majority of the costs of promoting the conservation of natural gas through conservation trackers that work in tandem with a lost margin recovery mechanism. The order was implemented in the North service territory in December 2006, and provides for recovery of 85 percent of the difference between weather normalized revenues actually collected by the Company and the revenues approved in the Company's most recent rate case. Energy efficiency programs began in the South gas territory in December 2006. A similar approach regarding lost margin recovery commenced in the South gas territory on August 1, 2007, as the new base rates went into effect, allowing for recovery of 100 percent of the difference between weather normalized revenues actually collected by the Company and the revenues approved in that rate case. It is expected that after the North filing is acted upon, it will be at 100 percent also. While most expenses associated with these programs are recoverable, in the first program year the Company is required to fund \$1.5 million in program costs without recovery.

Ohio

In June 2007, the Public Utilities Commission of Ohio (PUCO) approved a settlement that provides for the implementation of a lost margin recovery mechanism and a related conservation program for the Company's Ohio operations. This order confirms the guidance the PUCO previously provided in a September 2006 decision. The conservation program, as outlined in the September 2006 PUCO order and as affirmed in this order, provides for a two year, \$2 million total conservation program to be paid by the Company, as well as a sales reconciliation rider intended to be a recovery mechanism for the difference between the weather normalized revenues actually collected by the Company and the revenues approved by the PUCO in the Company's most recent rate case. Approximately 60 percent of the Company's Ohio customers are eligible for the conservation programs. The Ohio Consumer Counselor (OCC) and another intervener requested a rehearing of the June 2007 order and the PUCO granted that request in order to have additional time to consider the merits of the request. In accordance with accounting authorization previously provided by the PUCO, the Company began recognizing the impact of the September 2006 order on October 1, 2006, and has recognized cumulative revenues of \$2.6 million, of which \$1.3 million has been recorded in 2007. The OCC appealed the PUCO's accounting authorization to the Ohio Supreme Court, but that appeal has been dismissed as premature pending the PUCO's consideration of issues raised in the OCC's request for rehearing. Since October 1, 2006, the Company has been ratably accruing its \$2 million commitment.

MISO

Since February 2002 and with the IURC's approval, the Company has been a member of the Midwest Independent System Operator, Inc. (MISO), a FERC approved regional transmission organization. The MISO serves the electrical transmission needs of much of the Midwest and maintains operational control over the Company's electric transmission facilities as well as that of other Midwest utilities.

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On April 1, 2005, the MISO energy market commenced operation (the Day 2 energy market). As a result of being a market participant, the Company now bids its owned generation into the Day Ahead and Real Time markets and procures power for its retail customers at Locational Marginal Pricing (LMP) as determined by the MISO market. The Company is typically in a net sales position with MISO and is only occasionally in a net purchase position. Net positions are determined on an hourly basis. When the Company is a net seller such net revenues are included in *Electric Utility Revenues* and when the Company is a net purchaser such net purchases are included in *Cost of Fuel and Purchased Power*. The Company also receives transmission revenue that results from another members' use of the Company's transmission system. These revenues are also included in *Electric Utility Revenues*.

Pursuant to an order from the IURC received in December 2001, certain MISO startup costs (referred to as Day 1 costs) were deferred, and those deferred costs are now being recovered through base rates that went into effect on August 15, 2007. On June 1, 2005, Vectren, together with three other Indiana electric utilities, received regulatory authority from the IURC to recover fuel related costs and to defer other costs associated with the Day 2 energy market. The order allows fuel related costs to be passed through to customers in Vectren's existing fuel cost recovery proceedings. During 2006, the IURC reaffirmed the definition of certain costs as fuel related; the Company is following those guidelines. Other MISO fuel related and non-fuel related costs were deferred, and those deferred costs are now being recovered through base rates that went into effect on August 15, 2007. The IURC order authorizing new base rates also provides for a tracking mechanism associated with ongoing MISO-related costs and transmission revenues.

As a result of MISO's operational control over much of the Midwestern electric transmission grid, including SIGECO's transmission facilities, SIGECO's continued ability to import power, when necessary, and export power to the wholesale market has been, and may continue to be, impacted. Given the nature of MISO's policies regarding use of transmission facilities, as well as ongoing FERC initiatives, uncertainties around Day 2 energy market operations and a pending Day 3 market, where MISO plans to provide bid-based-regulation and contingency operating reserve markets, it is difficult to predict near term operational impacts. However, as stated above, it is believed that MISO's regional operation of the transmission system will ultimately lead to reliability improvements. MISO has indicated that the Day 3 ancillary services market would begin in June 2008.

The potential need to expend capital for improvements to the transmission system, both to SIGECO's facilities as well as to those facilities of adjacent utilities, over the next several years will become more predictable as MISO completes studies related to regional transmission planning and improvements. Such expenditures may be significant. The Company will timely recover its investment in certain new electric transmission projects that benefit the MISO infrastructure outside of the Company's service territory at a FERC approved rate of return.

Gas Cost Recovery (GCR) Audit Proceedings

In 2005, the PUCO issued an order disallowing the recovery of approximately \$9.6 million of gas costs relating to the two-year audit period ended October 2002 and in 2006, an additional \$0.8 million was disallowed related to the audit period ending October 2005. The initial audit period provided the PUCO staff its initial review of the portfolio administration arrangement between VEDO and ProLiance. Since November 1, 2005, the Company has used a provider other than ProLiance for these services.

Through a series of rehearings and appeals, including action by the Ohio Supreme Court in the first quarter of 2007, the Company was required to refund \$8.6 million to customers. The Company had previously recorded the impact of the PUCO findings, including its estimate of the share of the ultimate disallowance to be received from its partner in ProLiance.

Integrated Gasification Combined Cycle Project Involvement

In August 2007, the Company announced that it has determined to not participate in the proposed Edwardsport, Indiana, Integrated Gasification Combined Cycle (IGCC) generating plant with Duke Energy Indiana, Inc. (Duke).

Based upon a review and analysis of the Company's expected electric generation requirements, the expected demand for energy on the system may be more appropriately satisfied through the use of other alternatives, including additional natural gas peaking generation, purchased power, renewable resources and increased customer conservation. The Company has paid Duke approximately \$3.0 million for engineering studies and related costs. By separate agreement with Duke, the Company expects to be reimbursed for all costs and expenses it has paid to Duke.

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11. Adoption of FIN 48

Utility Holdings does not file federal or state income tax returns separate from those filed by its parent, Vectren Corporation. Vectren and/or certain of its subsidiaries file income tax returns in the U.S. federal jurisdiction and various states. The Internal Revenue Service (IRS) has conducted its examination of Vectren's U.S. federal income tax returns for tax years through December 31, 2004. The State of Indiana, Vectren's primary state tax jurisdiction, has conducted examinations of state income tax returns for tax years through December 31, 2002. No examinations are currently ongoing.

On January 1, 2007, the Company adopted FASB Interpretation No. 48 (FIN 48) "Accounting for Uncertainty in Income Taxes" an interpretation of SFAS 109, "Accounting for Income Taxes." FIN 48 prescribes a recognition threshold and measurement attribute for financial statement recognition and measurement of tax positions taken or expected to be taken in an income tax return. FIN 48 also provides guidance related to reversal of tax positions, balance sheet classification, interest and penalties, interim period accounting, disclosure and transition.

As a result of the implementation of FIN 48, the Company recognized an approximate \$0.9 million increase in the liability for unrecognized tax benefits, which was accounted for as a reduction to the January 1, 2007 balance of *Retained earnings*. At adoption, the total amount of gross unrecognized tax benefits for uncertain tax positions, including positions impacting only the timing of tax benefits, was \$7.0 million. At September 30, 2007, the liability for uncertain tax positions totaled \$5.0 million. The decrease results from changes in estimates that charge against deferred taxes.

The amount of unrecognized tax benefits, which, if recognized, would impact the effective tax rate as of September 30, 2007, was \$0.6 million. The remaining unrecognized tax benefit relates to tax positions for which the ultimate deductibility is highly certain but for which there is uncertainty about the timing of such deductibility. Because of the impact of deferred tax accounting, other than interest and penalties, the disallowance of the shorter deductibility period would not affect the annual effective tax rate but would accelerate the payment of cash to the taxing authority to an earlier period.

From time to time, the Company may consider changes to filed positions that could decrease the liability for uncertain tax positions. However, it is not expected that such changes would have a significant impact on earnings and would only affect the timing of payments to taxing authorities.

The Company accrues interest and penalties associated with unrecognized tax benefits in *Income taxes*. During the nine months ended September 30, 2007, the Company recognized expense related to interest and penalties totaling approximately \$0.3 million. The Company had approximately \$0.5 million for the payment of interest and penalties accrued as of September 30, 2007.

12. Segment Reporting

The Company's operations consist of regulated operations and other operations that provide information technology and other support services to those regulated operations. The Company segregates its regulated operations into a Gas Utility Services operating segment and an Electric Utility Services operating segment. The Gas Utility Services segment provides natural gas distribution and transportation services to nearly two-thirds of Indiana and to west central Ohio. The Electric Utility Services segment provides electric distribution services primarily to southwestern Indiana, and includes the Company's power generating and marketing operations. The Company cross manages its regulated operations as separated between Energy Delivery, which includes the gas and electric transmission and distribution functions, and Power Supply, which includes the power generating and marketing operations. In total, regulated operations supply natural gas and /or electricity to over one million customers. Utility Holdings has three operating segments as defined by SFAS 131 "Disclosure About Segments of an Enterprise and Related Information"

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(SFAS 131). Net income is the measure of profitability used by management for all operations. Information related to the Company's business segments is summarized below:

<i>(In millions)</i>	Three Months Ended September 30,		Nine Months Ended September 30,	
	2007	2006	2007	2006
Revenues				
Gas Utility Services	\$ 114.0	\$ 116.8	\$ 890.0	\$ 848.6
Electric Utility Services	143.6	123.2	361.6	324.4
Other Operations	10.1	9.2	30.3	27.5
Eliminations	(9.7)	(8.7)	(29.0)	(26.1)
Consolidated Revenues	\$ 258.0	\$ 240.5	\$ 1,252.9	\$ 1,174.4

Profitability Measure - Net Income/(Loss)