



Conference Call Transcript

DUK - Q2 2008 Duke Energy Corporation Earnings Conference Call

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PRESENTATION

Operator

Good day everyone, and welcome to the Duke Energy second quarter earnings conference call. Today's call is being recorded.

At this time for opening remarks I would now like to turn the conference over to Mr. Sean Trauschke. Please go ahead, sir.

Sean Trauschke - Duke Energy Corporation - VP of IR

Good morning and welcome to Duke Energy's second quarter 2008 earnings review. Leading our discussion today are Jim Rogers, chairman, president and chief executive officer; and David Hauser, group executive and chief financial officer. Jim will begin today's presentation by providing a general overview of the quarter's results, then David will provide more detail and context on the quarter's results from each of our businesses. Following David, Jim will update you on some of our major growth and regulatory initiatives. After our prepared remarks, we'll open the lines up for your questions.

Before we begin, let me take a moment to remind you that some of the things we'll discuss today concern future company performance and include forward-looking statements within the meanings of the securities laws. Actual results may materially differ from those discussed in these forward-looking statements and you should refer to the additional information contained in Duke Energy's 2007 Form 10-K, filed with the SEC, and our other SEC filings concerning factors that could cause those results to be different than contemplated in today's discussion. In addition, today's discussion includes certain non-GAAP financial measures as defined under SEC Regulation G. A reconciliation of those measures to the most directly comparable GAAP measures is available on our Investor Relations website at www.duke-energy.com. As a reminder, prior to the first quarter 2008, we presented ongoing earnings which excluded the impacts of special items and discontinued operations. Like the first quarter, today we are reporting adjusted earnings, which exclude mark-to-market impacts of economic hedges in the Commercial Power segment as well as special items and discontinued operations. With that, I'll turn the call over to Jim.

Jim Rogers - Duke Energy Corporation - Chairman, CEO & President

Thank you, Sean. Good morning, everyone and thank you for joining us today. Most importantly, thank you for your interest and investment in Duke Energy. We had a solid second quarter. We resolved several pending regulatory uncertainties. We continued our successful pursuit of four major commission-approved capital projects. We launched a number of innovative regulatory initiatives and we expanded our wind business. As we said in our earnings news release this morning, we reported adjusted diluted earnings per share of \$0.27 for the second quarter of 2008 versus \$0.24 in the second quarter last year. The increase in adjusted diluted EPS was primarily due to continued strong contributions from each of our two largest businesses – U.S. Franchised Electric and Gas, and our commercial businesses, including Duke Energy International. The increase was partially offset by increased interest expense and lower results at Crescent, which continues to be impacted by the sluggish real estate market. Current year adjustments to reported earnings include real estate project impairments at Crescent, mark-to-market impact of economic hedges at Commercial Power and costs-to-achieve the Cinergy merger. With these results, we remain on track to achieve our 2008 employee incentive target of \$1.27 of adjusted diluted earnings per share.

David will give you more specifics about each segment's results and then I'll update you on our comprehensive approach to meeting our customers' future electricity needs in what will inevitably become a low carbon world. We are turning that comprehensive strategy into action in many different ways. I feel very good about the progress we are making towards our goal of modernizing our fleet and modernizing our grid. I will update you on our recent regulatory activities including our recent ESP filing in Ohio. I will also say a few words about a couple of environmental surprises the courts recently threw at our industry and how we are addressing them. Finally, I'll conclude with a brief discussion about our commercial businesses, with a focus on our emerging wind generation business. With that, let me turn it over to David.

David Hauser - Duke Energy Corporation - CFO

Thank you, Jim. I'll start my review of our second quarter 2008 results with our largest business segment, U.S. Franchised Electric and Gas. That segment reported second quarter 2008 EBIT of \$503 million, an increase of \$51 million over last year's second quarter. The quarter-over-quarter improvement in segment EBIT was primarily driven by the conclusion of clean air amortization and the substantial completion of rate credits in 2007 related to the Cinergy merger. As a result of the 2007 North Carolina rate case, we will no longer amortize our clean air expenditures. The estimated unamortized expenditures of approximately \$800 million will be included in rate base as they are completed. In the second quarter of 2007, we recorded amortization for North Carolina's Clean Air program of approximately \$56 million.

In addition, Franchised Electric and Gas results benefited from rate increases in Ohio and Indiana. The rate increases in Indiana primarily resulted from recovery of our qualifying pollution control costs in rates. As you will recall, Indiana allows us to recover CWIP in rates through a rider. The segment's improved results were also driven by an approximate \$26 million increase in equity AFUDC, which includes the \$18 million impact of a favorable regulatory ruling in Indiana. Equity AFUDC contributed \$44 million in the second quarter of 2008. These positive drivers were partly offset by lower retail rates in North Carolina as a result of last year's rate review. It is important to remember that the decrease in rates in North Carolina is mitigated by the elimination of our Clean Air amortization that I mentioned earlier. In addition, the segment's positive drivers were somewhat offset by an increase of approximately \$35 million in operation and maintenance costs, mostly due to additional planned generation outages. Other offsets were an increase in depreciation expense and the impact of milder weather. While the weather was slightly above normal during the quarter, it wasn't as strong as the above normal levels that we experienced last year. Though we continue to add customers for all of Franchised Electric and Gas, kilowatt-hour sales are affected by market conditions, including the general decline in the textile industry.

Next I'll review Commercial Power. For the quarter, Commercial Power reported adjusted segment EBIT from continuing operations of \$128 million, compared to \$42 million in the second quarter of 2007. The \$86 million increase in Commercial Power's results was due primarily to gains on the sales of emission allowances, lower purchase accounting expenses, and improved RSP rider collections. Commercial Power's results also benefited from improved operations, resulting from increased generation due to fewer plant outages, in addition to lower O&M costs. These positive drivers were partially offset by milder weather. A \$4 million improvement at our Midwest gas fired assets also contributed to Commercial Power's improved results. We continue to see improvement in these assets. For the quarter, these plants had adjusted EBIT losses of approximately \$1 million. As we've said before, we expect these assets to be EBIT positive on an adjusted basis by 2009. As Sean mentioned earlier, starting with the first quarter of 2008, we began to exclude the mark-to-market impacts of economic hedges in the Commercial Power segment and present adjusted earnings. We believe that by excluding the impact of mark-to-market changes from adjusted earnings, until the settlement of these economic hedges, we are better matching the financial impact of the derivatives with the underlying assets. Ultimately, we will recognize the effect of the economic hedges in adjusted earnings when the contract settles.

Now let's turn to our International business. For the second quarter of 2008, Duke Energy International reported adjusted segment EBIT from continuing operations of approximately \$116 million, an increase of \$19 million when compared to last year's second quarter. International's improvements were primarily driven by higher results at National Methanol of \$14 million and favorable foreign exchange rates of \$9 million. Remember, the earnings impact from changes in foreign exchange rates is reduced by the corresponding effect on interest expense of local currency Brazilian debt. Results in Latin America were relatively flat when compared to last year.

Next is Crescent Resources. Given the challenges facing the real estate business, it's not surprising that Crescent experienced a tough quarter. During the quarter, Crescent recorded impairment charges. Duke Energy's proportionate share of those impairment charges is approximately \$113 million. Before I talk about Crescent's quarterly results, let me first explain how we have recorded those charges. In June, Crescent restructured the terms of its corporate credit facility. That led to a management decision to revise its business strategy, which resulted in accelerating the sales of certain property holdings. Consequently, Crescent recorded impairment charges on those assets. Our proportionate share of those impairment charges is approximately \$100 million. And because the charges resulted from a change in Crescent's business strategy, we consider them to be a special item for the quarter and have excluded them from the segment's adjusted equity earnings.

Crescent also recorded additional impairment charges on joint venture projects related to its normal business. Our proportionate share of those impairment charges is approximately \$13 million. Because those charges were the results of Crescent's normal business, we have included them in the segment's adjusted equity earnings for the quarter. As a result of the \$13 million of impairment charges, as well as lower residential and commercial sales, the segment reported an \$8 million adjusted equity earnings loss for the second quarter of 2008, compared to \$17 million in positive adjusted equity earnings in the prior year's quarter. As of June 30th, 2008, Duke Energy's carrying value of its investment in Crescent was approximately \$125 million. In addition, I would like to remind you that Crescent's debt is non-recourse to Duke Energy.

Our Other category primarily includes costs associated with corporate governance and Duke Energy's captive insurance company. Other reported a second quarter 2008 adjusted net expense from continuing operations of \$69 million, compared to \$42 million in the second quarter of 2007. The increase for the quarter was due to a variety of items, including higher captive insurance losses and increased benefits costs.

Now I will turn to a few important non-operating items. At the end of the second quarter, we had a net cash balance of almost \$800 million, approximately \$1.2 billion of cash, cash equivalents and short-term investments, offset by about \$400 million of short-term commercial paper. Through June 2008, we have issued roughly \$2.4 billion in debt. Interest expense for the three months ended June 30th, 2008 increased \$35 million, compared to the same period in 2007. The increase was due primarily to higher debt balances as well as foreign exchange rate impacts on Brazilian denominated debt. Offsetting interest expense was capitalized interest, which was approximately \$18 million during the quarter. This amount is consistent with the \$19 million of capitalized interest during the same period in 2007. The effective tax rate for the quarter was approximately 33%, compared to 34% for the same period last year.

Overall, we are pleased with our financial results for the first half of 2008. However, the third quarter is normally the largest contributor to our annual results. We must continue to stay focused on executing our plan during the remainder of the year. With that, I'll turn it back over to Jim.

Jim Rogers - Duke Energy Corporation - Chairman, CEO & President

Thank you, David. We are making great progress in our fleet and grid modernization strategies. Let me address the Carolinas first. Construction is well underway on our 800-megawatt Cliffside coal plant in North Carolina. When completed, it will be one of the cleanest, most efficient pulverized coal plants in the U.S. We are addressing ongoing environmental challenges to the plant, which I will discuss in a moment. Notwithstanding these challenges, the project is still moving forward and is on target for completion in 2012. Also in June, we received separate CPCNs, granting us authorization to build two 620-megawatt combined cycle gas fired units, one at our Buck Station and the other at our Dan River Station. We expect to receive the air permit for the Buck unit by the end of this month and for the Dan River unit by the end of September. We expect construction to begin on the Buck plant by October. Current plan is to bring the Buck plant online as a peaking plant in 2010 and as a combined cycle unit in 2011. The Dan River plant will be brought on as a peaking plant in 2011, and as a combined cycle unit in 2012. These new stations will enable us to retire older existing coal fired units at each site. We further continue to advance our plans to build the new Lee Nuclear Station. We anticipate filing a CPCN in the fourth quarter of this year.

Our fleet modernization plans also include a key renewable energy initiative for North Carolina that we launched in June. We proposed a \$100 million plan to install solar panels at up to 850 sites including homes, schools, stores, and factories. To implement the solar distributed generation program, we are asking for approval to install, to own, operate, and dispatch the solar panels. This initiative will help us meet the state's renewable and energy efficiency portfolio standard. Also, it will enable us to evaluate the role of distributed generation on our system and gain

additional experience in owning and operating renewable energy resources. We filed our testimony for this initiative last month and hearings are scheduled with the North Carolina Commission in October.

Next, in Indiana, construction is underway at our 630-megawatt Edwardsport IGCC plant. Later this month, the IURC will hold a hearing on our updated cost estimate, which is approximately 18% higher than the amount previously approved. We expect the Commission to rule on this later this year. In addition to modernizing our fleet in Indiana, we continue to take significant steps to modernize our grid. You may remember that in May, we filed with the Indiana Commission a request for support of a program to modernize our power delivery system. Our plan is to install more than 800,000 new digital smart meters over the next five years, one for virtually every home and business we serve in Indiana. Over time, we will complement the smart meters with advanced technology designed to help customers save energy, to bolster system reliability, and to improve our customer service. Our plan will seek appropriate regulatory treatment for the cost of implementing the smart grid technology, including appropriate riders for capital expenditures. We will file our testimony later this month with hearings anticipated for next February. Additionally, a similar smart grid plan is part of our ESP filing in Ohio. Further, we plan to file similar initiatives in our other jurisdictions over the next several years. We have smart grid demonstrations underway in the Carolinas, Ohio, and Kentucky, and we've already installed in total nearly 15,000 smart meters in those states.

Next, let me update you on some of our key regulatory initiatives. First, our energy efficiency or more specifically our save-a-watt filings. We are advancing plans in each of our five states to implement our save-a-watt model. As you all remember, this model is designed to place energy efficiency investments on a level playing field with new power plant investments. Our plan offers our investors a fair return on efficiency, while delivering cost savings to our customers. The save-a-watt hearings began in North Carolina last week and I plan to testify later this month. Last week, in Indiana, we reached a constructive settlement in principle with the Indiana Utility Consumer Counselor on our save-a-watt proposal. We will formalize and file the settlement with the IURC by August the 15th. In the meantime, we plan to discuss the settlement with other interveners. Ultimately, this settlement will be presented to the Indiana Commission in an evidentiary hearing in the fall. You all might also remember that we have a settlement now pending before the South Carolina Commission and we expect a decision later this year.

Let me now turn to Ohio. Last month, the Commission approved a settlement agreement for an increase of \$18.2 million or 3% in our Ohio natural gas base rates. The agreement permits continued recovery of costs for our accelerated main replacement program. And last week we filed an application to increase our annual T&D revenues in Ohio by \$86 million or approximately a 5% overall increase. We will file our testimony in a few weeks and we would expect a Commission order in the second quarter of 2009.

Now I will update you on our Electric Security Plan, a filing we made in Ohio just last Thursday. Our ESP covers aspects of both generation and transmission and distribution. Our plan will allow us to provide reliable electric generation service and to maintain competitive, predictable pricing for our Ohio customers. Our plan spans three years, from January 1 2009 through December 31 2011. The initial ESP request would result in an increase of 6.2% in total annual electric revenues. The increase reflects, one, inflationary increases to our base generation price, which has been frozen since 1993, and, two, market compensation for dedicating our generation assets to serve our Ohio customers. Even with this increase, our rates under the ESP will remain at or close to the national average. On a comparative basis, our proposed increases are less than the ones proposed by First Energy and AEP. Our ESP achieves two major goals. First, it continues our existing riders and proposes new riders to cover the cost of modernizing our generation assets and to develop our smart grid and energy efficiency programs. Second, it includes plans to meet new mandated targets for renewable energy and energy efficiency. To prepare for this, you may remember that in June we issued an RFP for renewable generation capacity during the ESP term. In anticipation of our ESP filing, last week you also saw that we issued an RFP for up to 1,400 megawatts of peaking and our intermediate generating assets or long-term purchase power agreements that can be recovered under the new law. I just want to take a moment and thank the entire Duke Energy Ohio team for all the work that went into our ESP filing and our two RFPs.

Now an environmental update: As I mentioned earlier, the D.C. Circuit Court has thrown the industry a couple of environmental curve balls in the past few months. I'll now spend a few moments discussing these developments and how we are addressing them. First of all, earlier this year the DC circuit threw out the EPA's Clean Air Mercury Rule. Overall, we don't believe this decision has any immediate impact on our coal plant operations. However, certain environmental groups in North Carolina have used the D.C. Circuit's ruling to initiate a challenge to our Cliffside coal plant air permit. Specifically, they are contending that the state of North Carolina should have required us to perform a Maximum Achievable Control Technology, or MACT, assessment before the air permit could be issued. Not surprisingly, they have asked a federal court to halt construction of the project. We are vigorously defending this challenge to our permit because it is based on a court decision that occurred after our permit was issued. Nevertheless, we have also taken the additional step of voluntarily performing a MACT assessment to demonstrate that our plant will already have some of the lowest mercury emissions of any coal plant in the nation and additional controls would not be cost effective or prudent. That assessment has been submitted to the North Carolina Department of Environment and Natural Resources. We don't believe any of these changes will change our course of action and construction continues to move forward, even as we speak.

The DC Circuit's second curve ball came about three weeks ago, when it threw out EPA's Clean Air Interstate Rule or CAIR. First, I want to say that although Duke was one of the many parties seeking judicial review of this rule, our challenge to the rule was narrow and was not the basis for the Court's invalidation of the entire set of CAIR rules. The Court's decision to vacate CAIR has created some confusion and some uncertainty in the industry as to what individual company compliance obligations are in the absence of the rule. Our judgment is that even though the rule has been vacated, there will eventually be a new CAIR rule and it could be tougher and more stringent than the one the court threw out. In the meantime, we plan to operate our environmental equipment much like we were before the rule was thrown out, but we will do so in close consultation with our state utility regulators so that they fully understand and are comfortable with how we are operating this equipment during this period of uncertainty.

Now let me turn to our Commercial Businesses. As you may recall, this business has three major components -- Midwest Generation, Wind Generation, and International. I'm going to focus primarily on wind generation, as that's where most of the recent activity has been. Almost a year ago, we acquired a wind development business, and since then we have seen fuel prices continue to rise and public support of low carbon generation, such as wind, grow. Also, we're beginning to see significant transmission investment authorized to support wind energy in key regions of the country. This continues to strengthen our belief that renewables and specifically wind will play a growing role in the generation mix in the U.S. In May, we announced the acquisition of Catamount to further the growth in our wind business. When we close this transaction later this year, we will be a co-owner of the Sweetwater project in Texas, which is one of the largest wind projects in the world. In addition, we will develop -- we will add a highly experienced team of wind energy developers and operators to our current team. Our combined wind platform will have approximately 500 megawatts of wind power in operation by 2009, and have a development pipeline of more than 5,000 megawatts in 12 states. From this development pipeline, we are positioned to bring 200 to 300 megawatts of wind energy online annually.

Last quarter, we told you that to capture these additional growth opportunities and to confirm the value of our Commercial Businesses, we are looking at creative ways to bring in additional capital, including partnerships or joint venture relationships. Our assessment is ongoing and we will inform you of significant developments as they occur. As you can see, we are in a strong financial position. We are focused on our operations and we're making good progress, launching new innovative regulatory initiatives as well as bringing them to satisfactory conclusions as we did in the second quarter. In June, we increased our quarterly dividend \$0.01. Our current dividend yield is approximately 5.2%. In addition to the yield, we also expect continued growth in earnings.

Putting it all together, we believe this is a great value proposition for our investors. We'll talk more about everything we've covered today in much greater depth at the analyst meeting we are planning for November 21st in New York. At the meeting, we will provide updated projections for our CapEx spend and earnings growth over the next five years, as we did last year. You will also hear from other members of our senior management team who will discuss in detail their operations. We will be providing you with the meeting details in the coming weeks. With that, let's open the line so that David and I can take your questions.

QUESTION AND ANSWER

Operator

Thank you, Mr. Rogers. Ladies and gentlemen, the question-and-answer session will be conducted electronically. (OPERATOR INSTRUCTIONS) We'll pause for just a moment. We'll take our first question from Dan Eggers with Credit Suisse.

Jim Rogers - Duke Energy Corporation - Chairman, CEO & President

Dan, welcome.

Dan Eggers - Credit Suisse - Analyst

Thank you, Jim, on the ESP you said your rates would look below the national average and the smallest increase of the Ohio utilities, and you guys have [mathed] through everybody's plans. How do your rates look relative to the other Ohio guys, based on your ask relative to their ask?

Jim Rogers - Duke Energy Corporation - Chairman, CEO & President

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I think as I would recall, we are less than First Energy. We are -- our rates are higher than AEP.

Dan Eggers - Credit Suisse - Analyst

Okay. On this wind conversation, this is -- seems to be gaining a decent amount of internal momentum. How do we think about the capital going into this business? Is this new CapEx on top of what you guys were planning or is this carving out dollars from other places you had earmarked money?

Jim Rogers - Duke Energy Corporation - Chairman, CEO & President

We're in the process of working through our five-year plan that we'll present in November. And I suspect it will be a combination of both, but that work is a work-in-progress and more to come, Dan, in November.

Dan Eggers - Credit Suisse - Analyst

Okay. And then on the IGCC in Indiana, with the review, does the Indiana Commission have the ability to halt plans at this point in time and when you do the cost analysis, given the move in coal prices, given the continued inflation in construction, how does the economics of that plant look relative to, say, gas or some other option?

Jim Rogers - Duke Energy Corporation - Chairman, CEO & President

It's my judgment that -- well, first, they have the ability to really rule that this plant can't go forward. In that event, we have the ability under the statute to recover all our investment in the plant to date. My judgment is that while coal prices have moved and gas prices have moved and they will continue to be very volatile over the next year, five years, 10 or the life of the plant -- it's my judgment, based on the analysis that we've done that the Commission will reaffirm their commitment to the plant at the higher capital cost. But that proceeding will be this fall and we'll have an answer this year.

Dan Eggers - Credit Suisse - Analyst

Now, will you have to provide, with this proceeding updated economics and a new cost benefit analysis relative to other options with the fall filing?

Jim Rogers - Duke Energy Corporation - Chairman, CEO & President

I'm sure we will have to supply additional information so the Commission can take a look at it and we will, and I think we already have provided some information to date. But yes, they take a look at it and make a judgment as to whether this is the right thing for Indiana going forward. It's our belief that it is and our expectation is they will reaffirm their commitment.

Dan Eggers - Credit Suisse - Analyst

Okay. Thank you.

Jim Rogers - Duke Energy Corporation - Chairman, CEO & President

Thank you.

Operator

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Thank you. We'll hear next from Paul Patterson with Glenrock Associates.

Jim Rogers - Duke Energy Corporation - Chairman, CEO & President

Paul, welcome this morning.

Paul Patterson - Glenrock Associates - Analyst

Thank you. Back to CAIR, you guys I think have benefited from some emission allowance sales. What's the outlook if -- what's the outlook I guess going forward with what's happened in the emission allowance market and what have you?

Jim Rogers - Duke Energy Corporation - Chairman, CEO & President

I think that -- I think the outlook for us is we have completed most of the equipment construction. We still have more to do by 2010. And again, one of our objectives is to continue to operate that equipment in consultation with our state commissions, so that they are comfortable with how we operate. And we have the ability to turn back those units in their operations, but not the ability to bypass them.

Paul Patterson - Glenrock Associates - Analyst

I believe you guys have sold some emission allowances and that benefited earnings. I guess what I'm wondering is what's the outlook for additional emission sales or how should we think about that with what's happened in the emissions market?

David Hauser - Duke Energy Corporation - CFO

Paul, this is David. Let me speak to that one second. We did \$36 million of sales of NOx emission in the second quarter. In the current market, you would not be able to get that value, but if you look at our plans for the balance of the year, it was very modest what emission sales were in there. So you shouldn't view that as something that will impact our ability to achieve our employee incentive target.

Paul Patterson - Glenrock Associates - Analyst

Right. And I guess you guys had about \$12 million, I believe, in the first quarter?

David Hauser - Duke Energy Corporation - CFO

We did.

Paul Patterson - Glenrock Associates - Analyst

Right. Going forward, though, we shouldn't expect anything like that I guess unless we get a change in the CAIR thing before the end of 2009? Does that make sense?

David Hauser - Duke Energy Corporation - CFO

I think that's right. The market value of those emission allowances has declined at this point significantly.

Paul Patterson - Glenrock Associates - Analyst

Okay. And then the accelerated sales at Crescent and the loss that you guys booked on that, is that a non-cash item, number one? Number two, does that continue? I mean, in other words, was that a recognition of -- was this just a write-down because hey, we're going to -- because Crescent

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decided they're going to be selling the property sooner? Or, as they sell the property, are we going to see additional losses associated with this change in business strategy, if you follow me?

Jim Rogers - Duke Energy Corporation - Chairman, CEO & President

David, you want to take that one?

David Hauser - Duke Energy Corporation - CFO

Yes. What you said at the beginning was exactly right, Paul. What we've done is we've changed the business strategy and we said it's in Crescent's best interest to sell some properties faster than they were planning to. As a result of that decision, they have to go ahead and write those properties to market value. So now they'll go ahead and that is a non-cash write-down, just as you said. Now they will be actually executing on that and as they sell the properties, one of two things will happen. Either their write-down will be a little high or it will be a little low as they actually execute on the sales. Obviously, what we've recorded is our best estimate of what we think will happen.

Paul Patterson - Glenrock Associates - Analyst

Okay. And if it ends up that it's higher, then it will show up in operating income as -- if it ends up as a bigger loss -- and if there's less of a loss then there would be a write-up so-to-speak, with respect to this loss in ongoing earnings; is that right?

David Hauser - Duke Energy Corporation - CFO

You could have a write-up or a write-down.

Paul Patterson - Glenrock Associates - Analyst

But it wouldn't be a one-timer anymore?

David Hauser - Duke Energy Corporation - CFO

No, I don't think so it -- well, we'll have to address that at the time. We haven't really dealt with that. If it ends up being material, we'll have to deal with that, but I don't expect that because we've recorded what we think is their value.

Paul Patterson - Glenrock Associates - Analyst

Listen, thank you very much.

Jim Rogers - Duke Energy Corporation - Chairman, CEO & President

Paul, thank you.

Operator

Thank you. We'll hear next from Jonathan Arnold with Merrill Lynch.

Jim Rogers - Duke Energy Corporation - Chairman, CEO & President

Jonathan, welcome.

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Jonathan Arnold - Merrill Lynch - Analyst

Good morning. I wanted just to clarify one thing. I think in the prepared remarks it sounded like the \$36 million on emission sales was a delta between the second quarter last year and second quarter this year but was it also the actual amount of sales?

David Hauser - Duke Energy Corporation - CFO

Yes, it was.

Jonathan Arnold - Merrill Lynch - Analyst

That was one. And secondly, on the Crescent, just reading between the lines of the press release it said that this change of business strategy was in conjunction with a redo of the credit facility. So to what extent was this bit of a voluntary change or were you just -- was the line reduced or what happened? Can you just explain a little more the color around that statement?

David Hauser - Duke Energy Corporation - CFO

Yes, we renegotiated the credit facility in May and it was -- it got totally redone. I guess it was actually in June. And if you look at the credit facility, the balance did not change, but Crescent made a decision that it's better to sell properties quicker and pay down the credit facility than to hold those properties with the belief the market will come back. Now, this only applies to a small piece of the total properties Crescent has. They have a lot of other properties they're still developing. But for certain residential properties, largely in Florida, Arizona and Texas, they're going to be selling those more quickly.

Jonathan Arnold - Merrill Lynch - Analyst

Did the rate on the credit facility move materially?

David Hauser - Duke Energy Corporation - CFO

It moved 50 basis points.

Jonathan Arnold - Merrill Lynch - Analyst

Okay. Thank you very much.

Jim Rogers - Duke Energy Corporation - Chairman, CEO & President

Jonathan, thank you.

Operator

We'll next hear from Michael Lapidés with Goldman Sachs.

Michael Lapidés - Goldman Sachs - Analyst

Hey, guys.

Jim Rogers - Duke Energy Corporation - Chairman, CEO & President

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Good morning, Michael.

Michael Lapidès - Goldman Sachs - Analyst

How are you? Good morning. Can you talk us through a little bit just the process between your filing on the 30th and 31st of July in Ohio and new rates coming into effect -- what we can expect, when we can expect it and which interveners are likely to be the most prevalent besides PUCO staff?

Jim Rogers - Duke Energy Corporation - Chairman, CEO & President

I think our first assignment now that we've filed it and we've already had some conversations with some of the parties is to work diligently with them to come up with a resolution of this, rather than -- and to avoid going to hearing. That's always our first bias in terms of dealing with cases like this. So we'll work our way through it and hopefully reach a settlement. It's really too early to tell where the parties will come out on this. I'm sure there will be the standard set of concerns with respect to all aspects of this. I mean, the industrials have a point of view, the Consumer Counsel will have a point of view, but it's too early for us to pinpoint who will be the toughest and exactly what the issues will be, but more to come on all that. And even if we don't reach settlement and even if we don't have a litigated outcome this year, the existing RSP, which is very similar to what we filed, will continue in effect in '09.

Michael Lapidès - Goldman Sachs - Analyst

Okay. And just one other item. When I think about your wind plant development and this is obviously outside of Ohio kind of changing tack a little bit here, any concerns about the significant number of other people building wind in Texas and whether the transmission will actually keep up with the wind plant development?

Jim Rogers - Duke Energy Corporation - Chairman, CEO & President

It appears with the decision a couple weeks ago in building I think almost \$4 billion to \$5 billion worth of new transmission lines, the state is very committed to seeing the development of adequate transmission so that the consumers in the state can access it. That has been a concern with the wind industry that -- will the transmission keep up? There's been debates about whether or not the national corridors are appropriately designed, given the development of wind, and whether or not there should be some redevelopment. But my belief is that based on comments by the leadership at [NARU] based on the Texas decision, what's going on in other regions in the country, I think there's going to be a significant effort to develop the transmission so that the wind will be available. But one of the advantages of the acquisition that we did is that it gives us wind sites in 12 states, very diversified portfolio of options and it allows us to develop -- again, we have a pretty modest aspiration of 200 to 300 megawatts a year, but allows us to develop it in a way consistent with the development of transmission and the market.

Michael Lapidès - Goldman Sachs - Analyst

Got it. Thank you and congrats on a good quarter, guys.

Jim Rogers - Duke Energy Corporation - Chairman, CEO & President

Thanks, Michael.

Operator

Thank you. We'll hear next from Hugh Wynne with Sanford Bernstein.

Hugh Wynne - Sanford C. Bernstein & Company, Inc. - Analyst

Aug. 05. 2008 / 10:00AM ET, DUK - Q2 2008 Duke Energy Corporation Earnings Conference Call

Good morning.

Jim Rogers - Duke Energy Corporation - Chairman, CEO & President

Good morning and welcome.

Hugh Wynne - Sanford C. Bernstein & Company, Inc. - Analyst

Thank you. Just a question regarding your volume sales. I notice that total regular sales build are down in the quarter and for the year-to-date both in the Carolinas and the Midwest. And I see a fairly large increase in special sales and in the Carolinas also in unbilled sales. I was wondering if I might get your view on what is occurring in the various customer classes with respect to their levels of consumption, what's driving that? And if you might explain for me the offsetting increases in special sales and billed sales and what those mean?

Jim Rogers - Duke Energy Corporation - Chairman, CEO & President

David, you want to start out with an answer and then I'll add to it?

David Hauser - Duke Energy Corporation - CFO

Okay. Let me talk about a handful of things here, Hugh and see if this answers it. First of all, if you look at weather, where earnings for the year were positively impacted compared to normal, but negative compared to last year, so that's one factor. Weather was -- negatively impacted earnings compared to last year. With regard to the specific special sales line, that consists of three things in the Carolinas and, in the Midwest, it's largely wholesale. But in the Carolinas, it's bulk power marketing and it's wholesale that's not your historic Schedule 10 and it's the Catawba interaction. And we have been increasing our wholesale sales, so the reason you see special sales going up both places is the increase that we're having in wholesale sales. The unbilled is simply a function of when the meters are read and it's an estimate at the end of the month. It swings around depending on exactly how the calendar falls. It's not particularly meaningful at the end of the day, because it's really just a function of the billing cycle.

Hugh Wynne - Sanford C. Bernstein & Company, Inc. - Analyst

Okay. And so the -- I assume, then, that the weather impact has been the primary contributor to lower sales in the residential and general service categories. The decline in industrial on the other hand I assume is just a reflection of depressed economic conditions, or what is happening there?

Jim Rogers - Duke Energy Corporation - Chairman, CEO & President

Hugh, the way I would say it is it's a little different in each state. For instance, in Indiana we see weaknesses in the transportation, paper, stone, clay, and the glass industries. In Ohio and Kentucky, we see weakness in the paper and the chemical industries. For the Carolinas, the weakness is more in the furniture, paper, and the printing industries but is offset by gains in the primary metals and rubber and plastics business. We see a continued -- what's been a very long-term structural decline in the textile industry and that continues. But it's different industries in different states, but I think the overall point is that the industrial sales which reflects what's really going on in the economy are all off a little.

Hugh Wynne - Sanford C. Bernstein & Company, Inc. - Analyst

Right, right, right. Okay. Then just a quick question if I could about your two big projects, Cliffside and Edwardsport. With respect to Edwardsport, one of the concerns I have is that the Commission will not -- basically disapprove the project and say the plant cannot go forward, but they'll say it can go forward at a cost less than what you estimate it to cost currently. So instead of granting you the 18% increase, they would grant you a 9% increase or something of that sort. Is that a possible regulatory outcome, and is that a risk that becomes greater as time goes on and subsequent cost increases are incurred? Or should we be thinking about it in a completely different way?

Jim Rogers - Duke Energy Corporation - Chairman, CEO & President

I think I would think about it this way. First, the 18% increase is the increase in the total projected capital cost of the plant. My judgment is that they recognize -- and we talked about it in the hearing, that we're in a worldwide commodity boom and virtually whether you're building a gas plant or a coal plant or a nuclear plant or wind plant, in every instance we're seeing significant cost increases in those and I think that will continue. My judgment is that the Commission will be comfortable with this 18% increase, but they might look differently -- and this is just a might, and not any educated guess on my part -- they might look differently at future cost increases in the plant. But I don't think they would disallow them. They might limit the ROE, is one thing they could do. I mean, there's a variety of things they could possibly do, but Indiana has always been very constructive in their approach. They understand the commodity markets that we're in today. And at the end of the day, they are very committed. In fact, we just had a -- we called it a celebration because the groundbreaking had already been done, but we had 130 people show up, some of the leaders across the state including the Governor was there and it's gotten wide political support throughout the state, not just in the region. And so my belief is that politically there's very strong support for this plant and strong support for us building it -- one, because it's going to use Indiana coal, and two, it fits in very well with our need for base load unit at this time.

Hugh Wynne - Sanford C. Bernstein & Company, Inc. - Analyst

All right. That's great. On the Cliffside plant, I wonder if I could just get a better understanding of the nature of the legal challenge there. I have to assume that that plant was designed with the best available control technology to comply with the Clean Air Act. The fact that CAIR is overturned I don't think would be material in that respect. Is the contention of the suit that you've not dealt with CO2 or what is it that's at stake here?

Jim Rogers - Duke Energy Corporation - Chairman, CEO & President

I think what's at stake is that they're trying to use the DC Circuit decision as sort of a new circumstance that needs to be taken into account. It's my understanding that the mercury requirements under the North Carolina law are tougher than the federal requirements.

Hugh Wynne - Sanford C. Bernstein & Company, Inc. - Analyst

Right.

Jim Rogers - Duke Energy Corporation - Chairman, CEO & President

And they would control. And so I believe this is part of a concerted effort by a wide variety of environmental groups, trying to stop the building of coal plants and they've just seized on this decision as another explanation or another approach, another argument they can advance. At the end of the day, it would be my judgment it will be rejected.

Hugh Wynne - Sanford C. Bernstein & Company, Inc. - Analyst

Thank you for your time, I appreciate it.

Jim Rogers - Duke Energy Corporation - Chairman, CEO & President

Thank you, Hugh.

Operator

Thank you. We'll now hear from Paul Fremont with Jefferies and Company.

Jim Rogers - Duke Energy Corporation - Chairman, CEO & President

Paul, welcome.

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Paul Fremont - Jefferies & Company - Analyst

Thank you. Couple questions. First is I think it's a -- the beginning of the year you had indicated a targeted level of ongoing EBIT contribution from Crescent of about \$75 million based on what you experienced in the quarter and based on what's going on in the real estate market, would you still expect to do \$75 million and would you expect that potentially next year's contribution might be affected by what's going on?

Jim Rogers - Duke Energy Corporation - Chairman, CEO & President

David, would you like to take that?

David Hauser - Duke Energy Corporation - CFO

Yes. I do not think that we will be able to do \$75 million in Crescent this year, but I do think that things are going well enough in other aspects of the business that we're still comfortable with our incentive target that we've laid out of \$1.27. As far as next year, we really haven't gotten into projecting what's going to happen with Crescent next year. We'll lay that out, among everything else, when we do our meeting on November 21st.

Paul Fremont - Jefferies & Company - Analyst

And then on the Commercial Power front, there was a sizable improvement in I guess utilization levels or gigawatt hour output this quarter versus last quarter -- looks like almost 30% versus 12%. But none of that seems to have really translated into improved profitability, at least at the Midwest fleet. Can you help us understand what's going on there in terms of the improving utilization levels?

David Hauser - Duke Energy Corporation - CFO

Let me segregate two things. Let's segregate the historic coal plants and the Midwest gas. If you look at Midwest gas, their production was actually down versus last year but their margins were up. And so, in the second quarter of this year, the Midwest gas lost \$1 million versus right at \$6 million last year. If you look at the historic fleet, the coal plants, they did have improved operations. We had a significant outage in '07 and that -- those operations did improve earnings about \$12 million. Is that helpful?

Paul Fremont - Jefferies & Company - Analyst

Yes, thank you.

David Hauser - Duke Energy Corporation - CFO

Okay.

Operator

Thank you.

Jim Rogers - Duke Energy Corporation - Chairman, CEO & President

Paul, thank you.

Operator

We'll take our final question from Steve Fleischman with Catapult.

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Jim Rogers - Duke Energy Corporation - Chairman, CEO & President

Steve, welcome. Good morning.

Steve Fleischman - Catapult Partners - Analyst

Yeah, hi, Jim. I noticed that you guys issued an RFP for new power at Cinergy and I'm curious -- first of all, if the DENA assets would meet any of the requirements for that RFP? And secondly, in your RSP -- in your ESP plan how did you characterize -- how did you characterize how you would recover either plants that you end up buying or building? Would that be dealt with in the ESP plan?

Jim Rogers - Duke Energy Corporation - Chairman, CEO & President

What we have done is that if -- to the extent we purchase power, we have a proposed tracker for purchasing power similar to the one we have today. To the extent we add -- we buy a plant, someone responds to the RSP and we purchase a plant in Duke Energy of Ohio, we have the ability to track those capital costs or capacity costs associated -- I mean capital cost associated and the return associated with that plan. So that's the mechanisms that are embedded in the ESP that would allow us to solve either/or situation.

Steve Fleischman - Catapult Partners - Analyst

Okay. And did the DENA assets fit the requirements of that RFP at all?

Jim Rogers - Duke Energy Corporation - Chairman, CEO & President

They do. Our Commercial Business is taking a look at the RFP now, making determinations as to whether to bid. We're at a point where we're almost as we said before, economically indifferent as the market tightens in the Midwest and we bid into PJM auction. So they're going to be making decisions over the next month with respect to whether or not to bid into the RSP.

Steve Fleischman - Catapult Partners - Analyst

Okay. Okay. Thank you.

Jim Rogers - Duke Energy Corporation - Chairman, CEO & President

Thank you, Steve.

Operator

Thank you. I would now like to turn the conference back over to Mr. Sean Trauschke for any final or closing remarks.

Sean Trauschke - Duke Energy Corporation - VP of IR

Thank you, Kat. As always our team will be available to answer any questions you may have. And I want to thank you on behalf of Jim and David for joining us today and we look forward to speaking with you in the future.

Operator

Thank you. Ladies and gentlemen, this does conclude today's presentation. We thank you for your participation and have a great afternoon.

