



## **REPORT OF THE NOMINATING AND CORPORATE GOVERNANCE COMMITTEE**

The Nominating and Corporate Governance Committee (“**Governance Committee**”) is primarily responsible for corporate governance matters affecting the Company and its subsidiaries. The Governance Committee has four members and is composed entirely of non-employee directors all of whom the Board has determined to be independent pursuant to the New York Stock Exchange (“**NYSE**”) rules. The Governance Committee met three times during the past fiscal year. At each meeting, the Governance Committee conducts an executive session without management present.

### **Scope of Responsibilities**

The Governance Committee has a number of significant responsibilities which are set forth in its charter posted at [www.vectren.com](http://www.vectren.com), including:

- Serving as a conduit for shareholders and other interested parties to communicate with the non-employee members of the Board regarding nominees and other matters affecting Company business;
- Overseeing the succession planning process for the office of Chief Executive Officer, senior management and the primary leadership of the Company’s subsidiaries and affiliates;
- Monitoring other corporate governance matters, including periodically reviewing the Company’s Code of By-Laws and Articles of Incorporation as they relate to corporate governance;
- Formulating recommendations concerning the composition, organization and functions of the Board and its committees;
- Identifying and selecting qualified nominees for election to the Board, including assessing the viewpoint, background and demographics of nominees, and whether their presence on the Board would contribute to the overall diversity of the Board;
- Recommending programs for continuing Board member education and development;
- Establishing qualification criteria for service as a member of the Board, including “independence;”
- Assessing the contributions of existing members of the Board for reelection;
- Monitoring the effectiveness and functioning of the Board and its various committees;
- Approving management participation on compensated third party boards of directors; and
- Establishing compensation for non-employee members of the Board.

### **2011 Accomplishments**

Throughout the year, the Governance Committee gathered, assessed, and, as appropriate, acted upon information relating to corporate governance, including governance-related items described in the Sarbanes-Oxley Act of 2002 (“**Sarbanes-Oxley**”), the Dodd-Frank Wall Street Reform and Consumer Protection Act (“**Dodd-Frank**”), and those regulatory changes affecting listed companies established by the New York Stock Exchange (“**NYSE**”) and the Securities and Exchange Commission (“**SEC**”). These efforts by the Governance Committee are ongoing.

As required by the Governance Committee's Charter, which is posted on the Company's website at [www.vectren.com](http://www.vectren.com), the Governance Committee conducted an annual review of the Corporate Governance Guidelines applicable to the full Board. Based upon that review, the Governance Committee concluded that two modifications, which are discussed later in this report, were advisable. The current Corporate Governance Guidelines are posted on the Company's website at [www.vectren.com](http://www.vectren.com).

The Governance Committee considers nominees for director, including nominees recommended by security holders. The policy for director nominations by shareholders is included under "Nomination of Directors by Shareholders" beginning on page 9 of this proxy statement. The criteria considered by the Governance Committee and the full Board when assessing candidates are contained in the Company's Code of By-Laws ("**By-Laws**") and are also set forth in *Appendix A* of this proxy statement.

During the year, the Governance Committee provided ongoing oversight with respect to each Board member's relationship with the Company and its subsidiaries. This action was required under the "independence" standards for the Board, which were developed by the Governance Committee as required by the Company's Corporate Governance Guidelines, and were approved by the full Board. The independence standards are set forth and discussed on pages 19-20 of this proxy statement. Based on these standards, the Board has determined that with the exception of Mr. Ellerbrook, who is the retired Chief Executive Officer of the Company, and Mr. Chapman, who is Board Chair, President and Chief Executive Officer of the Company, all members of the Board are independent.

During the year, the Governance Committee evaluated each Board member's presence on committees in light of the applicable qualification requirements, including additional independence requirements pertinent to certain of the committees. Based upon this evaluation the Governance Committee recommended the composition and leadership of each committee to the full Board. Thereafter, those recommendations were adopted by the full Board.

During the year, the Governance Committee oversaw a formal communication process to ensure there is adequate information provided to the Board regarding actions taken by the boards of directors at the Company's wholly-owned subsidiaries and affiliates. That process provides for quarterly management updates to the Governance Committee relative to these actions.

The Governance Committee oversees non-employee directors' compliance with the stock ownership guidelines that have been established by the Board. Those guidelines are more fully discussed on pages 18-19 of this proxy statement. During the past year, stock ownership by directors was monitored and, as discussed on pages 18-19 of this proxy statement, as of February 10, 2012, each director, with the exception of Robert G. Jones, who was elected to the Board effective February 2, 2011, met the ownership threshold required by those guidelines. There is a five year transition period for compliance by new directors and Mr. Jones is still within that transition period.

During the year, the Governance Committee continued with the administration of the succession planning process for the senior management of the Company and the primary leadership of the Company's subsidiaries and affiliates. The Governance Committee believes that actively engaging in the succession planning process is a critical part of the Company's long-term management continuity preparedness. Succession planning is an ongoing process with respect to management positions across the Company, and is an integral part of the Company's normal personnel planning activities. Reports on this process were provided to the Governance Committee during the year. On a regular basis the Chair of the Governance Committee provides updates on this subject to the Board as part of the executive session segments of Board meetings.

As part of their oversight of the succession planning process for the Chief Executive Officer position, the Governance Committee discussed during 2010 and again in 2011 the organizational structures that could result from Mr. Ellerbrook's retirement, which occurred in May of 2010. In 2010, and following Mr. Ellerbrook's retirement as Chief Executive Officer, the Governance Committee decided that he should have a continuing role as non-executive Chair of the Board during the transition of leadership to his successor, Mr. Chapman. Such a continuing role was provided for in Section 1.G. of the Corporate Governance Guidelines. Throughout the remainder of 2010 and in early 2011 the Governance Committee assessed the transition of leadership from Mr. Ellerbrook to Mr. Chapman and concluded that it was successful. As a result, the Governance Committee recommended to the Board that Mr. Chapman be elected Board Chair effective immediately following the 2011 Annual Meeting, subject to his

reelection to the Board by the shareholders at that meeting. To ensure the maintenance of good governance practices, the Governance Committee also recommended that Mr. McGinley be elected as Lead director to assume that role immediately following the 2011 Annual Meeting, which would coincide with the retirement of the then Lead director Robert L. Koch, who retired from the Board last year. These recommendations were accepted by the Board and were acted upon on March 2, 2011. Thereafter, Mr. Chapman was reelected to the Board and he has served as Chair since the time of the 2011 Annual Meeting. Mr. McGinley has also served as the Lead director since that time. This subject is more fully discussed on page 10 of this proxy statement under the heading Board Leadership Structure.

In connection with the conclusion of the transition of leadership from Mr. Ellerbrook to Mr. Chapman, the Governance Committee also considered the continuing service by Mr. Ellerbrook as a member of the Board. Under the Corporate Governance Guidelines for the Company, following such a transition of leadership by the former Chief Executive Officer, it was uncertain whether it would be appropriate for that person to remain as a director. In order to clarify that such continued service could be appropriate based upon the facts and circumstances of each case, the Governance Committee recommended a change to the language in Section 1.G. of the Corporate Governance Guidelines, which was subsequently approved by the Board. In the case of Mr. Ellerbrook, the Governance Committee concluded that his significant business expertise, including his longstanding involvement with the energy industry, positioned him to continue to be a valuable contributor as a director. Under the Corporate Governance Guidelines, as revised, the Governance Committee has recommended that Mr. Ellerbrook be reelected by the shareholders at the Annual Meeting.

Under the oversight of the Governance Committee, formal Board development activities were undertaken during the past year. The Board conducted a multi-day development session where they heard presentations from various external professionals with respect to important issues affecting the Company. As part of that session, the Board also received in-depth presentations from senior management regarding industry issues and processes affecting the Company and its subsidiaries. In addition, some members of the Board attended training activities focused on the development of directors' skills.

The Governance Committee is charged with oversight of compensation for the non-employee members of the Board. Periodically, the Governance Committee directs the preparation of an analysis of the continuing market competitiveness of that compensation. In early 2010 the Governance Committee had such an analysis prepared by Hay Group, Inc., which is the independent compensation consultant employed by the Compensation and Benefits Committee, and determined, based upon the results of that analysis, that the existing level of director compensation was not market competitive. The analysis included a review of the annual board retainer, board meeting attendance fees, committee retainers, committee meeting attendance fees, and equity grants. The analysis primarily relied upon a review of comparative data from the group of companies within the industry peer group that has been used by the Company to measure its performance and used by the Compensation and Benefits Committee when establishing executive compensation. Based upon the analysis and review of current market data, it was the conclusion of the independent consultant that the compensation to outside directors was well below both the average and the median for the Company's peer group. In October of 2010, the Governance Committee took action in response to that information and recommended an increase in director compensation. That recommendation was adopted by the Board at its November meeting, with an effective date of January 1, 2011. During 2012, the Governance Committee would anticipate reviewing the appropriateness of the existing compensation for outside directors in light of current market data. Director compensation is more fully discussed on pages 12-14 of this proxy statement under the heading Director Compensation.

As the plan administrator of the Vectren Compensation At Risk Compensation Plan ("**At Risk Plan**") with respect to compensation for non-employee members of the Board, the Governance Committee has made annual awards of restricted units for directors effective as of May 16, 2012 (subject to their reelection by the shareholders). The role of equity compensation as part of the total compensation provided to non-employee directors is more fully discussed beginning on page 12 of this proxy statement.

During the year the Governance Committee, with assistance from management, reviewed the institutional controls in place with respect to the Board's oversight of the Company's non-regulated business investments. Those controls had been implemented in 2000 at the inception of the Company's operations. Based upon a review of practices employed by other enterprises comparable in size and scope to the Company, as well as the Governance

Committee's assessment of the Company's existing non-regulated businesses and the Company's strategic plans for that area, revised institutional controls were established and recommended for approval by the Board. Thereafter, the Board approved those controls and they are in use presently.

The Chair of the Governance Committee administered the annual Board performance evaluation process pursuant to which the Board critiqued its performance. The Chair of the Governance Committee then presented the evaluation results to the full Board. In response, senior management will develop an action plan that will be executed over the course of 2012.

During the year the Governance Committee conducted a review of available data relating to the appropriate retirement age, if any, for members of the Board. At the inception of this effort Section 1.H. of the Company's Corporate Governance Guidelines prescribed a retirement age of age 72 for directors. Based upon on a review of practices employed within the energy and general industries, as well as the views of corporate governance firms, the Governance Committee concluded that it would be appropriate to extend that retirement age from 72 to 75. That recommendation was provided to the full Board and thereafter the Corporate Governance Guidelines were amended to reflect this change.

During the year, the Governance Committee, with assistance from independent legal counsel, reviewed the indemnification provisions for officers and directors contained within the Company's organizational documents. Following the consideration of reports and advice from that counsel, the Governance Committee adopted a recommendation to the full Board that indemnification agreements, in a form as recommended by counsel, be adopted and entered into with each of the Board members and the named executive officers. Thereafter, the full Board approved that recommendation and those agreements were executed on behalf of the Company. The form of those agreements has been filed with the Securities and Exchange Commission by the Company.

At the February 2012 meeting of the Governance Committee, the committee confirmed that all Board committees had complied with their respective charters in 2011. At that same meeting the Governance Committee received a presentation regarding the distribution of responsibilities among the Board committees with respect to various compliance matters. During the remainder of the year, the Governance Committee anticipates overseeing the revision to other Board committee charters to reflect this distribution in order to ensure there is an appropriate level of oversight by the Board with respect to such matters.

During the year the Governance Committee amended Section III. B. of its charter to clarify it is the Board, and not management, that is charged with responsibility for the recruitment of new directors. Thereafter, the Governance Committee's recommended changes were approved by the Board.

In connection with the 2012 Annual Meeting, and employing the qualification criteria set forth in the Corporate Governance Guidelines, as well as the director retention criteria approved by the Board, the Governance Committee evaluated all of the nominees who are standing for reelection. As a result of that process, the Governance Committee concluded that the full Board should recommend to the shareholders that, with the exception of Mr. William G. Mays, who is retiring at the 2012 Annual Meeting, all of the existing directors should be reelected. In addition, after reviewing benchmarking data regarding the size of boards for enterprises comparable in scale and scope to the Company, as well as assessing the strengths and experiences of the remaining Board members, the Governance Committee determined, at this time, to not propose a nominee to replace Mr. Mays. As a result, following the Annual Meeting the Code of By-Laws will be modified to reflect the reduction in the size of the Board from twelve to eleven members.

### **Share Ownership Policy**

Our Company's share ownership policy requires officers and non-employee directors to meet share ownership targets. The Governance Committee adopted that policy in 2000 and it provides a five year transition period for non-employee directors to comply with their applicable share ownership targets. The Board expects the covered persons to make ratable progress toward compliance each year. The program includes these key features:

- Participants who are non-employee directors have a share ownership target based on a multiple of five times

their annual cash retainer, which for the past year amounted to \$225,000. As of February 10, 2012, all of the non-employee directors, excluding Mr. Jones, who is still in the transitional five year compliance period, exceeded the established ownership requirements. The Governance Committee reviews non-employee director stock ownership on an annual basis.

- A participant may count toward his or her target the value of owned shares, phantom units of our stock in our nonqualified deferred compensation plans and vested “in the money” stock options, restricted shares and stock unit awards, with value based on the market price of our common stock.

### **Annual Committee Charter Review and Performance Evaluation**

As required by the Governance Committee’s charter, in 2011 the Committee reviewed its charter and determined that one modification was advisable. That modification is discussed earlier in this report. Also, as required by the Governance Committee’s charter, the Governance Committee conducted an annual performance evaluation, the results of which have been discussed among the Governance Committee members.

### **Director Independence Standards**

In determining director independence, the Board considers broadly all relevant facts and circumstances, including the corporate governance listing standards of the NYSE, which are summarized below. The Board considers the issue not merely from the perspective of a director, but also from that of persons or organizations with which the director has an affiliation. An independent director must be free of any relationship with the Company that impairs the director’s ability to make independent judgments, including indirectly as a partner, shareholder or officer of an organization that has a relationship with the Company.

At a minimum, in making the independence determination, the Board applies the following standards, and it also considers any other relationships it deems relevant. A director will not be considered independent if any of the following criteria apply:

1. The director is, or has been within the last three years, an employee of the Company, or an immediate family member is, or has been within the last three years, an executive officer,<sup>1</sup> of the Company.
2. The director has received, or has an immediate family member who has received, during any twelve-month period within the last three years, more than \$120,000 in direct compensation from the Company, other than director and committee fees and pension or other forms of deferred compensation for prior service (provided such compensation is not contingent in any way on continued service).
3. (A) The director is a current partner or employee of a firm that is the Company’s internal or external auditor; (B) the director has an immediate family member who is a current partner of such a firm; (C) the director has an immediate family member who is a current employee of such a firm and personally works on the Company’s audit; or, (D) the director or an immediate family member was within the last three years a partner or employee of such a firm and personally worked on the Company’s audit within that time.
4. The director or an immediate family member is, or has been within the last three years, employed as an executive officer of another company where any of the Company’s present executive officers at the same time serves or served on that company’s compensation committee.

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<sup>1</sup> For purposes of this standard, the term “executive officer” has the same meaning specified for the term “officer” in Rule 16a-1(f) under the Securities Exchange Act of 1934.

5. The director is a current employee, or an immediate family member is a current executive officer, of a company that has made payments to, or received payments from, the Company for property or services in an amount which, in any of the last three fiscal years, exceeds the greater of \$1 million, or 2% of such other company's consolidated gross revenues.

In determining that the independent directors satisfied the above criteria, the Governance Committee considered the following transactions. In 2011, the Company purchased approximately \$36,750 of advertising time from South Central Communications, Inc., a corporation in which Mr. Engelbrecht has an interest, which represents a very small percentage of that corporation's 2011 revenues. In 2011, the Company had banking relationships with Old National Bank, of which Mr. Jones is President and Chief Executive Officer. The total fees paid for those relationships, which consist of approximately \$147,000, represents a very small percentage of that corporation's 2011 revenues. These fees were solely transactional fees and included: \$54,000 in payments for participation in the \$600 million VUHI and Vectren Capital Corp. syndicated credit facilities at the year end level of \$15 million, in which Old National Bank was a non-lead bank; a \$59,000 payment for provision of three letters of credit to Vectren Fuels, Inc. totaling about \$5.8 million; a \$34,000 payment for bank account service charges related to provision of the Vectren payroll account, which serves several subsidiary companies, provision of the account processing automated customer checking account drafts for Vectren South, provision of the miscellaneous customer billings lockbox account, and provision of the checking account used in connection with a not-for-profit energy payment assistance fund. In addition, Old National Bank purchased utility services from the Company which also did not represent a significant percentage of Old National Bank's revenues. The Governance Committee determined that the amounts involved in these transactions were well below the levels provided in the director independence standards and were not material to the relevant directors or to any person or organization with whom they are affiliated.

### **Selection and Evaluation of Director Candidates**

All director candidates must meet the requirements established by the Governance Committee from time to time and the director qualification standards included in the Company's Corporate Governance Guidelines. Candidates are reviewed in the context of the current composition of the Board, the operating requirements of the Company and the long-term interests of shareholders. In considering director nominees, pursuant to its charter the Governance Committee considers diversity, including geographic as well as other considerations described below, as a key factor in selecting candidates for election to the Board. In discharging this responsibility, the Governance Committee assesses the viewpoint, background and demographics of the candidates. The Governance Committee seeks to create a board that is strong in its collective knowledge and diversity of skills and experience with respect to accounting and finance, management and leadership, vision and strategy, business operations, business judgment, industry knowledge, corporate governance and other factors the Governance Committee deems appropriate. When considering a candidate, the Governance Committee looks specifically at the candidate's qualifications in light of the needs of the Board and the Company at that time, given the then current mix of director attributes, including the matters discussed above, as well as ethnicity, race and gender. Specific selection criteria are set forth in the By-Laws and are also included in Appendix A.

### **Commitment**

The Governance Committee is committed to ensuring that the Company implements and follows corporate governance principles that fulfill its responsibilities under its charter and to enhance, where appropriate, the Company's corporate governance practices. The Governance Committee anticipates meeting at least three times in 2012.

Nominating and Corporate Governance Committee

J. Timothy McGinley, *Chair*,  
James H. DeGraffenreidt, Jr.,  
Anton H. George, and  
William G. Mays