

EXHIBIT NO. _____

BEFORE
THE PUBLIC UTILITIES COMMISSION OF OHIO

In the Matter of the Application of)	
Columbus Southern Power Company and)	
Ohio Power Company for Authority to)	Case No. 11-346-EL-SSO
Establish a Standard Service Offer)	Case No. 11-348-EL-SSO
Pursuant to §4928.143, Ohio Rev. Code,)	
in the Form of an Electric Security Plan.)	
In the Matter of the Application of)	
Columbus Southern Power Company and)	Case No. 11-349-EL-AAM
Ohio Power Company for Approval of)	Case No. 11-350-EL-AAM
Certain Accounting Authority.)	

SUPPLEMENTAL DIRECT TESTIMONY OF
THOMAS E. MITCHELL
ON BEHALF OF
COLUMBUS SOUTHERN POWER COMPANY
AND
OHIO POWER COMPANY

Filed July 1, 2011

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1 **PERSONAL DATA**

2 **Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.**

3 A. My name is Thomas E. Mitchell and my business address is 1 Riverside Plaza
4 Columbus, Ohio 43215.

5 **Q. ON WHOSE BEHALF ARE YOU TESTIFYING IN THIS PROCEEDING?**

6 A. I am testifying on behalf of Columbus Southern Power Company (CSP) and Ohio
7 Power Company (OPCo) or collectively referred to as AEP Ohio or the Company.

8 **Q. ARE YOU THE SAME THOMAS E. MITCHELL WHO PREVIOUSLY**
9 **SUBMITTED DIRECT TESTIMONY IN THIS PROCEEDING?**

10 A. Yes.

11

12 **PURPOSE OF TESTIMONY**

13 **Q. WHAT IS THE PURPOSE OF YOUR SUPPLEMENTAL TESTIMONY IN**
14 **THIS PROCEEDING?**

1 A. The purpose of my supplemental testimony is to describe the accounting related to the
2 proposed Turning Point Solar Project (Project).

3 **PROPOSED OVER/UNDER ACCOUNTING FOR THE PROPOSED SOLAR PROJECT**

4 **Q. IN YOUR DIRECT TESTIMONY IN THIS PROCEEDING, YOU**
5 **IDENTIFIED CERTAIN ADDITIONAL NON-FAC RIDERS PROPOSED BY**
6 **THE COMPANY IN THE 2012 - 2014 ESP THAT WERE TO BE SUBJECT**
7 **TO OVER/UNDER ACCOUNTING. WAS ONE OF THOSE PROPOSED**
8 **RIDERS THE GENERATION RESOURCE RIDER (GRR)?**

9 A. Yes.

10 **Q. DID YOU ALSO IDENTIFY THE ACCOUNTING REQUIREMENTS TO**
11 **RECORD REGULATORY ASSETS AND REGULATORY LIABILITIES**
12 **RELATED TO OVER/UNDER REGULATORY ACCOUNTING?**

13 A. Yes.

14 **Q. SPECIFICALLY, WHAT WOULD AEP OHIO DO MONTHLY TO RECORD**
15 **THE OVER/UNDER ACCOUNTING RELATED TO THE GRR?**

16 A. AEP Ohio would first record the GRR revenue in the respective Residential,
17 Industrial, Commercial and Industrial revenue accounts and then compare the revenue
18 to the total of the Project costs and record the difference as a regulatory asset or
19 regulatory liability.

20 **PROPOSED ACCOUNTING FOR THE PROPOSED SOLAR PROJECT**

21 **Q. CAN YOU OUTLINE THE PROPOSED ACCOUNTING FOR THE**
22 **PROJECT?**

1 A. Yes. I address the proposed accounting for the Project from the following
2 perspectives: 1) the Turning Point Solar Generation Company (TPS Generation); and
3 2) AEP Ohio.

4 **Q. PLEASE FIRST SUMMARIZE THE PROPOSED FINANCIAL STRUCTURE**
5 **FOR THE TURNING POINT SOLAR GENERATION COMPANY.**

6 A. Turning Point Solar Generation Company (TPS Generation) plans to build and own
7 the solar generation facilities. Upon satisfaction of certain conditions discussed in
8 Company witness Godfrey's Supplemental Direct testimony, there will be a financial
9 closing to include construction financing (to be retired at each phase by permanent
10 debt financing) where TPS Generation will buy certain development assets from the
11 project developer, Turning Point Solar LLC. TPS Generation would then construct
12 the Project in three phases as discussed by Company witness Godfrey and would
13 lease the Project to AEP Ohio, which would operate the Project and as lessee, be
14 responsible for operation and maintenance expenses, and any necessary capital
15 additions. The sources of the permanent financing (as discussed by Company witness
16 Godfrey) are expected to be an AEP Ohio equity contribution of \$20 million¹ over the
17 three phases, equity from third-party investors, and third party loans as well as a loan
18 from AEP Ohio related to the anticipated qualification for investment tax credits
19 related to the Project (as discussed by Company witnesses Godfrey and Kelley).

¹ Case No. 10-1261-EL-UNC the Commission accepted Columbus Southern Power's commitment to invest \$20M of equity in the Turning Point Solar Project. In anticipation of the merger of Columbus Southern Power and Ohio Power by the time these equity investments are made, the investment is referred to as an AEP Ohio investment.

1 **Q. PLEASE DESCRIBE THE ACCOUNTING BY TPS GENERATION FOR THE**
2 **LEASE TO AEP-OHIO AND WHAT TYPES OF COSTS ARE INCLUDED IN**
3 **THE LEASE?**

4 **A.** The lease from TPS Generation to AEP Ohio is anticipated to be for 25 years with
5 quarterly lease payments. It is anticipated that there will be a separate 25-year lease
6 for each completed phase. From the perspective of TPS Generation, the lease will be
7 treated as a direct financing lease. At the start of the lease, TPS Generation will
8 record a lease receivable (at the gross value of the expected lease payments) and
9 credit the constructed facility cost (the present value of the lease) with an additional
10 credit to unearned carrying cost revenue related to both interest and equity costs on
11 the invested capital. Upon receipt of a lease payment, TPS Generation will reduce its
12 receivable and recognize the appropriate amount of the deferred carrying charges on
13 invested capital. Note the future charges from American Electric Service Corporation
14 (AEPSC) to be rendered to TPS Generation pursuant to the planned Business Services
15 Agreement (BSA) as discussed by Company witness Godfrey will be billed monthly
16 to AEP Ohio as a part of the lease transaction.

17 **Q. WHAT WILL TPS GENERATION DO WITH THE LEASE REVENUE**
18 **RECEIVED FROM AEP OHIO?**

19 **A.** TPS Generation will 1) repay the debt and equity funds (the invested principal) to the
20 respective investors including AEP Ohio which contributed both debt and equity; 2)
21 pay a carrying cost on the invested equity and debt capital; and 3) pay AEPSC for its
22 costs rendered under the planned BSA.

1 **Q. WHAT NET INCOME IS EXPECTED ON TPS GENERATION DUE TO THE**
2 **PROJECT?**

3 A. TPS Generation's net income will be the equity carrying costs recognized related to
4 the equity investments on the Project. This net income will be realized through the
5 equity carrying cost portion of the lease payments received from AEP Ohio. The
6 portion of the lease revenue from AEP Ohio related to the debt invested capital and
7 the AEPSC BSA charges will be offset with expenses.

8 **Q. PLEASE CONTINUE WITH A DESCRIPTION OF THE PROPOSED**
9 **ACCOUNTING FOR AEP OHIO RELATED TO THE LEASE WITH TPS**
10 **GENERATION.**

11 A. As the lessee of the Project from TPS Generation, AEP Ohio will be subject to
12 generally accepted accounting principles for leases. In accordance with the Financial
13 Accounting Standards Board's (FASB) Accounting Standards Codification (ASC)
14 section 840 - Leases (ASC 840), certain qualifying leases are recorded as capital
15 leases, which record the Project as an asset and a liability for the present-value of the
16 lease payments on AEP Ohio.

17 **Q. WHAT ARE THE REQUIREMENTS FOR A CAPITAL LEASE AND DOES**
18 **AEP OHIO MEET THOSE REQUIREMENTS?**

19 A. If a lease meets one or more of the following requirements, the lease is a capital lease:
20 1) ownership transfers to the lessee; 2) a bargain purchase option exists; 3) the
21 noncancelable lease term is equal to 75% or more of the expected economic life of
22 the asset; and 4) the present value of the minimum lease payments is equal or greater
23 than 90% of the fair value of the asset. The tests are done sequentially, and if one

1 criterion is met, the lease is treated as a capital lease. The lease of the Project from
2 TPS Generation, is expected to meet criteria 2 above based on Article 14.1 of the
3 draft form Facilities Lease Agreement (attached to the Participation Agreement
4 discussed by Company witness Godfrey). Accordingly, AEP Ohio will recognize an
5 asset and a liability for the present-value of the lease payments.

6 **Q. HOW WILL AEP OHIO CHARGE THE LEASE PAYMENT MADE TO TPS**
7 **GENERATION?**

8 A. AEP Ohio will charge the lease payment to rent expense. However, as noted above, it
9 would record the balance sheet effect of the transaction by reducing equally the
10 previously recorded capitalized leased asset and liability by the appropriate principal
11 portion of the lease payment.

12 **Q. IN ADDITION TO LEASE PAYMENTS TO TPS GENERATION, WHAT**
13 **OTHER COSTS WILL AEP OHIO RECORD RELATED TO THE PROJECT?**

14 A. In addition to the lease payments to TPS Generation, AEP Ohio will record such
15 expenses as property taxes, operation and maintenance expense (excluding AEPSC
16 billings under the BSA that are recorded directly by TPS Generation), income taxes,
17 and carrying costs to include both a return of and on any necessary future capital
18 additions. Finally, AEP Ohio would record either an overrecovery (charge) or an
19 underrecovery (credit) to expense, representing the difference between the GRR
20 revenues and the total of the Project costs less the interest revenue earned on AEP
21 Ohio's debt investment in TPS Generation, discussed below.

22 **Q. WHAT CARRYING COST RATE WOULD AEP OHIO APPLY TO ANY**
23 **NECESSARY FUTURE CAPITAL ADDITIONS?**

1 A. AEP Ohio proposes to use the last Commission-approved weighted average cost of
2 capital in its AEP Ohio Distribution filing as discussed by Company witness Nelson.

3 **Q. HOW WILL AEP OHIO ACCOUNT FOR ITS EQUITY INVESTMENT IN**
4 **TPS GENERATION?**

5 A. AEP Ohio will account for its equity investment in TPS Generation by charging an
6 investment account. As carrying charge income is earned and paid to AEP Ohio on
7 its equity investment (AEP Ohio's share of TPS Generation's net income), AEP Ohio
8 will recognize income and when equity distributions are made from TPS Generation
9 to AEP Ohio, it will reduce its equity investment.

10 **Q. HOW WILL AEP OHIO ACCOUNT FOR ITS DEBT INVESTMENT IN TPS**
11 **GENERATION?**

12 A. AEP Ohio will account for its debt investment (loan) in TPS Generation by charging
13 a loan receivable. As carrying charge income is earned and paid on its debt loan
14 investment (AEP Ohio's share of TPS Generation's interest expense), AEP Ohio will
15 recognize interest income and when debt distributions are made from TPS Generation
16 to AEP Ohio, it will reduce its debt investment.

17 **Q. IN ADDITION TO THE TREATMENT OF THE TPS GENERATION**
18 **FACILITY AS A CAPITAL LEASE BY AEP OHIO, IS THERE AN**
19 **ADDITIONAL ACCOUNTING STANDARD THAT NEEDS TO BE**
20 **CONSIDERED FOR AEP OHIO CONSOLIDATED, AS REPORTED TO THE**
21 **SECURITIES AND EXCHANGE COMMISSION (SEC)?**

22 A. Yes. FASB ASC 810 provides guidance related to accounting for a variable interest
23 entity (VIE). If an entity, such as TPS Generation, is deemed to be a VIE, ASC 810

1 requires an analysis to determine whether a primary beneficiary exists related to that
2 VIE. Based on the results of the analysis, the primary beneficiary is required to
3 consolidate the VIE into its financial statements as if it were an owned entity. In
4 accordance with ASC 810, a largely qualitative analysis is completed to determine
5 whether a company has a controlling financial interest in a VIE and therefore, is the
6 primary beneficiary of that VIE. A company that has a controlling financial interest
7 in a VIE possesses the following characteristics and is deemed to be the primary
8 beneficiary: 1) The power to direct the activities of a VIE that most significantly
9 impact the VIE's economic performance, and 2) The obligation to absorb losses of
10 the VIE that could potentially be significant to the VIE or the right to receive benefits
11 from the VIE that could potentially be significant to the VIE. Given several factors,
12 including that AEP Ohio fully participated in the establishment of TPS Generation
13 and as described in Company witness Godfrey's direct testimony, controls all of the
14 electrical output of the Facility, directs the operation and maintenance of the Project
15 and controls all of the environmental attributes, including RECs produced by the
16 facility, AEP Ohio is deemed to have a variable interest in TPS Generation. Based on
17 analysis of the criteria above, AEP Ohio is deemed to have a controlling financial
18 interest and as the primary beneficiary, is required to consolidate TPS Generation into
19 its financial statements. Elimination of certain lease receivables/payables and
20 elimination of intercompany equity/investments and the related debt loan investment
21 and interest related to certain tax benefits (see testimony of Company witness Kelley)
22 will effectively leave the Project assets and the corresponding debt on the

1 consolidated balance sheet of AEP Ohio, along with the noncontrolling interest
2 related to the third party equity investors.

3 **Q. DOES ASC 810 EFFECTIVELY SUPPLANT THE REQUIREMENTS OF**
4 **LEASE ACCOUNTING AND EFFECTIVELY RECORD THE TPS**
5 **GENERATION BALANCE SHEET (INCLUDING DEBT AND THIRD**
6 **PARTY NON-CONTROLLING EQUITY) ON AEP OHIO'S**
7 **CONSOLIDATED BALANCE SHEET FOR SEC REPORTING PURPOSES?**

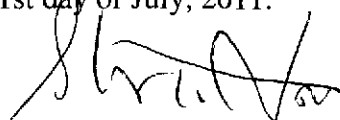
8 A. Yes.

9 **Q. DOES THIS CONCLUDE YOUR SUPPLEMENTAL DIRECT TESTIMONY?**

10 A. Yes.

CERTIFICATE OF SERVICE

The undersigned hereby certifies that a true and correct copy of the foregoing Supplemental Direct Testimony of Thomas E. Mitchell on behalf of Columbus Southern Power Company and Ohio Power Company has been served upon the below-named counsel via First Class mail, postage prepaid, this 1st day of July, 2011.



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