

FILE

14

COMPANIES REMAND EXHIBIT NO. _____

BEFORE
THE PUBLIC UTILITIES COMMISSION OF OHIO

In the Matter of the Application of)
Columbus Southern Power Company for)
Approval of an Electric Security Plan; an) Case No. 08-917-EL-SSO
Amendment to its Corporate Separation)
Plan; and the Sale or Transfer of Certain)
Generating Assets.)

In the Matter of the Application of)
Ohio Power Company for Approval of an) Case No. 08-918-EL-SSO
Electric Security Plan; and an Amendment)
to its Corporate Separation Plan.)

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

PUCO

2011 JUL 25 PM 4:25

RECEIVED-DOCKETING DIV

Filed July 25, 2011

This is to certify that the images appearing are an
accurate and complete reproduction of a case file
document delivered in the regular course of business.
Technician Am Date Processed 7/25/11

INDEX TO DIRECT TESTIMONY OF
THOMAS E. MITCHELL

	<u>Page No.</u>
1. Personal Data	1
2. Purpose of Testimony	3
3. GAAP Related to Deferral of FAC Expenses.....	4
4 GAAP Related to Deferral of Alternative Revenue Programs	10

BEFORE
THE PUBLIC UTILITIES COMMISSION OF OHIO
DIRECT TESTIMONY OF
THOMAS E. MITCHELL
ON BEHALF OF
COLUMBUS SOUTHERN POWER COMPANY
AND
OHIO POWER COMPANY

1 **PERSONAL DATA**

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

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

5 **Q. DID YOU PREVIOUSLY FILE TESTIMONY IN THIS CASE?**

6 A. No.

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

8 A. I am testifying on behalf of Columbus Southern Power Company (CSP) and Ohio
9 Power Company (OPCo) or collectively AEP Ohio or the Companies.

10 **Q. BY WHOM ARE YOU EMPLOYED AND IN WHAT CAPACITY?**

11 A. I am employed by American Electric Power Service Corporation (AEPSC), a
12 subsidiary of American Electric Power Company, Inc. (AEP), as Managing Director
13 of Regulatory Accounting Services. AEP is the parent company of CSP and OPCo.

14 **Q. WHAT ARE YOUR RESPONSIBILITIES AS MANAGING DIRECTOR OF**
15 **REGULATORY ACCOUNTING SERVICES?**

16 A. My primary responsibilities include providing the AEP System operating subsidiaries,
17 including CSP and OPCo, with accounting support for regulatory filings. This
18 support includes the preparation of cost-of-service adjustments, accounting schedules,

1 and accounting testimony. I direct a group of professionals who provide accounting
2 expertise, compile necessary historical accounting schedules, present expert
3 accounting testimony and respond to data requests in connection with rate filings with
4 eleven regulatory commissions and the Federal Energy Regulatory Commission
5 (FERC).

6 **Q. PLEASE DESCRIBE YOUR EDUCATIONAL BACKGROUND AND**
7 **PROFESSIONAL EXPERIENCE.**

8 A. I received a Bachelor of Science Degree in Accounting from Virginia Polytechnic
9 Institute and State University (Virginia Tech) in 1977. I also hold a Master of
10 Business Administration Degree from Virginia Tech and a Bachelor of Arts Degree in
11 Government from the University of Notre Dame. I have been a Certified Public
12 Accountant since 1978. I was first employed by Appalachian Power Company
13 (APCo) in 1979, an affiliated operating company of CSP and OPCo and, except for
14 employment with Norfolk Southern Corporation as an Assistant Accounting Manager
15 (1984-1985), have held various positions in the Accounting Department continuously
16 since that date. In 1998, I was promoted to Director, Accounting Policy & Research
17 and in 2008, I was promoted to my present position as Managing Director of
18 Regulatory Accounting Services. I have served as Chairman of the Accounting
19 Standards Committee of the Edison Electric Institute (EEI) and am currently
20 Chairman of the Joint Accounting Liaison Committee of the EEI which meets
21 annually with the FERC Accounting Staff to discuss accounting issues of mutual
22 interest to EEI and the FERC.

1 **Q. HAVE YOU PREVIOUSLY TESTIFIED OR SUBMITTED TESTIMONY IN**
2 **ANY REGULATORY PROCEEDINGS?**

3 A. Yes, I recently submitted prefiled testimony on behalf of CSP and OPCo before the
4 Public Utilities Commission of Ohio (PUCO or the Commission) in the 2012 - May
5 2014 (2012 - 2014) Electric Security Plan (ESP) proceedings, Case No. 11-349-EL-
6 AAM and Case No. 11-350-EL-AAM, and the Companies' distribution base rate case
7 in Case Nos. 11-351-EL-AIR and 11-352-EL-AIR. I also testified before the PUCO
8 on behalf of CSP and OPCo regarding the 2009 Significantly Excessive Earnings Test
9 (SEET) proceedings, Case No. 10-1261-EL-UNC. In addition, I have filed accounting
10 testimony and testified on behalf of APCo and Wheeling Power Company before the
11 Public Service Commission of West Virginia, and on behalf of APCo before both the
12 Virginia State Corporation Commission and the FERC. I have also filed accounting
13 testimony on behalf of Indiana Michigan Power Company before the Indiana Utility
14 Regulatory Commission.

15 **PURPOSE OF TESTIMONY**

16 **Q. WHAT IS THE PURPOSE OF YOUR REBUTTAL TESTIMONY IN THIS**
17 **PROCEEDING?**

18 A. The purpose of my rebuttal testimony is to rebut certain testimony of IEU witness
19 Joseph G. Bowser given July 21, 2011 before the Commission concerning the
20 application of Generally Accepted Accounting Principles (GAAP) principally in
21 connection with amounts deferred pursuant to AEP Ohio's Fuel Adjustment Clause
22 (FAC) during the 2009-2011 ESP. Specifically, Mr. Bowser incorrectly refers to
23 deferred FAC expenses as "deferred revenues" throughout his written testimony (IEU

1 Remand Ex.3) and during his cross examination (e.g. Tr. IV at 600-616).
2 Consequently, I clarify that the amounts deferred pursuant to the FAC were deferred
3 costs and not deferred revenues. This concept discussed below of deferral of
4 expenses (and not deferred revenues) as regulatory assets is also applicable to other
5 regulatory assets including the Economic Development Rider recorded pursuant to
6 AEP Ohio's 2009-2011 ESP.

7 **GAAP RELATED TO DEFERRAL OF FAC EXPENSES**

8 **Q. FIRST, WHAT IS THE GAAP THAT APPLIES TO REGULATED**
9 **ACCOUNTING FOR REGULATED OPERATIONS?**

10 A. Financial Accounting Standards Board (FASB) Accounting Standards Codification
11 (ASC) 980-10-15-2 (formerly FASB Statement No. 71, Accounting for the Effects of
12 Certain Types of Regulation) applies to an enterprise that has regulated operations
13 that meet all of the following criteria:

14 a. The entity's rates for regulated services or products provided to its
15 customers are established by or are subject to approval by an
16 independent, third-party regulator or by its own governing board
17 empowered by statute or contract to establish rates that bind customers.
18

19 b. The regulated rates are designed to recover the specific entity's costs
20 of providing the regulated services or products. This criterion is
21 intended to be applied to the substance of the regulation, rather than its
22 form. If an entity's regulated rates are based on the costs of a group of
23 entities and the entity is so large in relation to the group of entities that
24 its costs are, in essence, the group's costs, the regulation would meet this
25 criterion for that entity.
26

27 c. In view of the demand for the regulated services or products and the
28 level of competition, direct and indirect, it is reasonable to assume that
29 rates set at levels that will recover the entity's costs can be charged to
30 and collected from customers. This criterion requires consideration of
31 anticipated changes in levels of demand or competition during the
32 recovery period for any capitalized costs. This last criterion is not

1 intended as a requirement that the entity earn a fair return on
2 shareholders' investment under all conditions; an entity can earn less
3 than a fair return for many reasons unrelated to the ability to bill and
4 collect rates that will recover allowable costs. For example, mild
5 weather might reduce demand for energy utility services. In that case,
6 rates that were expected to recover an entity's allowable costs might not
7 do so. The resulting decreased earnings do not demonstrate an inability
8 to charge and collect rates that would recover the entity's costs; rather,
9 they demonstrate the uncertainty inherent in estimating weather
10 conditions. This requirement must also be evaluated in light of the
11 circumstances. For example, if the entity has an exclusive franchise to
12 provide regulated services or products in an area and competition from
13 other services or products is minimal, there is usually a reasonable
14 expectation that it will continue to meet the other criteria. Exclusive
15 franchises can be revoked, but they seldom are. If the entity has no
16 exclusive franchise but has made the very large capital investment
17 required to provide either the regulated services or products or an
18 acceptable substitute, future competition also may be unlikely.

19
20 **Q. DOES AEP OHIO MEET FASB ASC 980 FOR APPLYING REGULATED**
21 **ACCOUNTING FOR THE FAC?**

22 A. Yes, the recovery of fuel costs via the FAC is a regulated portion of AEP Ohio
23 because it was explicitly provided for in the ESP by the Commission in its final
24 decision in these cases. Based on the advice of counsel, it is my understanding that
25 the Supreme Court's April 19, 2011 decision did not reverse or remand any aspects of
26 the Commission's initial decision involving either the FAC or the phase-in rate cap
27 plan.

28 **Q. FOR REGULATED ENTITIES, WHAT REQUIREMENTS DOES FASB ASC**
29 **980 PRESCRIBE TO RECORD A REGULATORY ASSET SUCH AS**
30 **DEFERRED FAC COSTS?**

31 A. FASB ASC 980-340-25-1 states that:

32 Rate actions of a regulator can provide reasonable assurance of the existence
33 of an asset. An entity shall capitalize all or part of an incurred cost that would

1 otherwise be charged to expense if both of the following criteria are met:

2
3 a. It is probable (as defined in Topic 450) that future revenue in an amount at
4 least equal to the capitalized cost will result from inclusion of that cost in
5 allowable costs for rate-making purposes.

6
7 b. Based on available evidence, the future revenue will be provided to permit
8 recovery of the previously incurred cost rather than to provide for expected
9 levels of similar future costs. If the revenue will be provided through an
10 automatic rate-adjustment clause, this criterion requires that the regulator's
11 intent clearly be to permit recovery of the previously incurred cost.

12
13 A cost that does not meet these asset recognition criteria at the date the cost is
14 incurred shall be recognized as a regulatory asset when it does meet those
15 criteria at a later date.

16
17 The term "probable" is defined in the Contingency Topic (450) under FASB ASC
18 450-20-20 as "the future event or events are likely to occur."

19 **Q. ARE FAC REVENUES DISTINCT AND IDENTIFIABLE REVENUE UNDER**
20 **THE COMPANIES' TARIFFS?**

21 A. Yes. The tariffs of both CSP and OPCo have FAC riders that include separate rates
22 for the collection of FAC expenses.

23 **Q. SPECIFICALLY, CAN YOU PROVIDE A REFERENCE TO THE**
24 **COMMISSION ORDER THAT ADDRESSED THE TIMING OF THE**
25 **RECOVERABILITY OF THE DEFERRED FAC COSTS?**

26 A. Yes, the Commission's final decision in these cases provides for a quarterly
27 reconciliation to actual FAC costs incurred, which establishes the charge for the
28 subsequent quarter and a phase-in deferral from 2012 to 2018 (March 18, 2009
29 Opinion and Order at pages 20-24 and as confirmed in the July 23, 2009 Entry on
30 Rehearing at pages 6-10).

1 **Q. ARE THE DEFERRED AMOUNTS RECORDED BY AEP OHIO PURSUANT**
2 **TO THE FAC, DEFERRED COSTS OR DEFERRED REVENUES?**

3 A. The amounts are incurred costs (i.e. expenses) that were simply larger than the FAC
4 revenues provided. In no way can deferred expenses recorded pursuant to FASB
5 ASC 980 be construed as deferred revenues under GAAP.

6 **Q. WHAT ACCOUNTING ENTRY IS MADE WHEN THE FAC REVENUES**
7 **ARE SMALLER THAN FAC EXPENSES?**

8 A. AEP Ohio records a regulatory asset for the shortfall and reduces the FAC expenses,
9 thereby providing equality between expense and revenue.

10 **Q. DOES THE FASB ALSO PROVIDE FOR REGULATORY LIABILITIES**
11 **UNDER GAAP?**

12 A. Yes, FASB ASC 980-405-25-1 also provides for regulatory liabilities in three
13 instances where refunds are imposed by the regulator, where revenues provide for
14 future costs yet to be incurred, but for which the regulated entity is accountable, and
15 lastly for instances where a gain is deferred and amortized over a period.

16 **Q. WHAT ACCOUNTING ENTRY IS MADE WHEN THE FAC REVENUES**
17 **ARE LARGER THAN FAC EXPENSES?**

18 A. AEP Ohio would first reduce any previously recorded regulatory asset and then
19 establish a regulatory liability for any excess revenue above FAC expenses, thereby
20 providing an equality between revenue and expense.

21 **Q. ARE REGULATORY LIABILITIES DEFERRED REVENUES?**

22 A. No.

1 **Q. DOES IEU WITNESS BOWSER APPEAR TO RECOGNIZE THAT AEP**
2 **OHIO HAS, IN FACT, DEFERRED FAC EXPENSES AND NOT REVENUES**
3 **ON THEIR BOOKS?**

4 A. Not exactly. He states on lines 21-24 on Tr. IV at 615 that “I believe it was an
5 authorization of deferred revenues. But for accounting purposes the way the
6 companies reflected that was deferring expenses on their books.” At Tr. IV page 616,
7 line 16, he describes the “deferred revenue” as “postponed.” Whereas IEU witness
8 Bowser suggests that the Commission authorized deferred revenues and the
9 Companies unilaterally decided to account for the transaction by deferring expenses, I
10 believe it is clear from the Commission’s final decision that fuel costs (i.e. expenses)
11 were being deferred under the adopted FAC and rate cap/phase-in plan (reference the
12 March 18, 2009 Opinion and Order at pages 20-24 and as confirmed in the July 23,
13 2009 Entry on Rehearing at pages 6-10).

14 **Q. WHAT IS THE INACCURACY UNDER GAAP RELATED TO IEU WITNESS**
15 **BOWSER’S USE OF THE TERM “DEFERRED REVENUES” TO REFER TO**
16 **AEP OHIO’S DEFERRED FAC EXPENSES?**

17 A. As described above, GAAP allows for deferral of incurred costs (i.e. expenses). IEU
18 witness Bowser confuses the GAAP terminology, apparently in order to support the
19 notion that disallowance of recovery based on reasons having nothing to do with the
20 prudence of fuel expenses actually incurred would be a prospective revenue change.
21 In fact, a prospective rate change that would disallow (based on revenues prior to
22 June 2011 for POLR revenues and carrying costs on 2001-1008 environmental
23 investments) deferred FAC expenses entails a write-off of previously deferred FAC

1 expenses pursuant to Commission order.

2 **Q. DO YOU AGREE THAT RECOVERY OF THE DEFERRED FAC EXPENSES**
3 **AUTHORIZED UNDER THE MARCH 18, 2009 OPINION AND ORDER IS**
4 **TO COMMENCE JANUARY 2012?**

5 A. Yes.

6 **Q. WHY IS IT IMPORTANT TO CLARIFY THAT THE DEFERRED FAC**
7 **COSTS ARE IN FACT DEFERRED EXPENSES AND NOT DEFERRED**
8 **REVENUES, UNDER GAAP?**

9 A. The FAC expenses were deferred as noted above by comparing actual FAC revenues
10 charged to customers under ESP tariffs to actual FAC expenses, with the excess
11 expenses above the related revenue being deferred.

12 Simply labeling the timing of the recovery of these expenses as prospective, in no
13 way justifies reducing the deferrals or denigrates the amount of actual FAC expenses
14 deferred or the prudence of the deferred FAC expenses that have been under-
15 recovered during the 2009 through 2011 ESP period.

16 **Q. PLEASE SUMMARIZE WHAT FINANCIAL RESULT WILL OCCUR IF**
17 **THE COMMISSION AGREES WITH IEU TO USE CERTAIN BILLED**
18 **REVENUES PRIOR TO JUNE 2011 (THE EFFECTIVE DATE OF THE**
19 **REMAND REVENUES BEING SUBJECT TO REFUND) TO LOWER THE**
20 **RECOVERABLE FAC AMOUNT FOR OHIO POWER OR OTHER**
21 **REGULATORY ASSETS FOR CSP?**

22 A. AEP Ohio would have to write-off any previously deferred FAC expenses that may
23 be disallowed, as well as related carrying costs.

GAAP RELATED TO DEFERRAL OF ALTERNATIVE REVENUE PROGRAMS

Q. THE PRECEDING PART OF YOUR REBUTTAL TESTIMONY HAS DISCUSSED THE GAAP REFERENCES TO DEFERRAL OF FAC COSTS. DOES GAAP ALSO ADDRESS THE DEFERRAL OF REVENUES BY REGULATED ENTITIES?

A. Yes. FASB ASC 980-605-25-1 through 4 addresses the accounting for certain Alternative Revenue Programs as follows:

Traditionally, regulated utilities whose rates are determined based on cost of service invoice their customers by applying approved base rates (designed to recover the utility's allowable costs including a return on shareholders' investment) to usage. Some regulators of utilities have also authorized the use of additional alternative revenue programs. The major alternative revenue programs currently used can generally be segregated into two categories, Type A and Type B.

Type A programs adjust billings for the effects of weather abnormalities or broad external factors or to compensate the utility for demand-side management initiatives (for example, no-growth plans and similar conservation efforts). Type B programs provide for additional billings (incentive awards) if the utility achieves certain objectives, such as reducing costs, reaching specified milestones, or demonstratively improving customer service.

Both types of programs enable the utility to adjust rates in the future (usually as a surcharge applied to future billings) in response to past activities or completed events.

Once the specific events permitting billing of the additional revenues under Type A and Type B programs have been completed, the regulated utility shall recognize the additional revenues if all of the following conditions are met:

- a. The program is established by an order from the utility's regulatory commission that allows for automatic adjustment of future rates. Verification of the adjustment to future rates by the regulator would not preclude the adjustment from being considered automatic.
- b. The amount of additional revenues for the period is objectively determinable and is probable of recovery.
- c. The additional revenues will be collected within 24 months following the end of the annual period in which they are recognized.

1 **Q. IS THE ACCOUNTING FOR ALTERNATIVE REVENUE PROGRAMS**
2 **APPLICABLE TO DEFERRED FAC EXPENSES OR TO OTHER**
3 **REGULATORY ASSETS RECORDED PURSUANT TO AEP OHIO'S 2009-**
4 **2011 ESP?**

5 A. No. The regulatory assets recorded pursuant to Commission authorization in AEP
6 Ohio's 2009-2011 ESP including FAC expenses do not involve Alternative Revenue
7 Programs of either Type A or Type B.

8 **Q. DOES THIS CONCLUDE YOUR REBUTTAL TESTIMONY?**

9 A. Yes.

CERTIFICATE OF SERVICE

The undersigned hereby certifies that a true and correct copy of the foregoing Columbus Southern Power Company's and Ohio Power Company's Rebuttal Testimony of Thomas E. Mitchell has been served upon the below-named counsel via electronic mail, this 25th day of July 2011.



Steven T. Nourse

Greta.See@puc.state.oh.us
Sarah.Parrot@puc.state.oh.us
agamarra@wrassoc.com
bakahn@vorys.com
barthroyer@aol.com
bill.wright@puc.state.oh.us
bsingh@integrysenergy.com
cgoodman@energymarketers.com
charlieking@snavely-king.com
cmiller@szd.com
cmooney2@columbus.rr.com
cynthia.a.fonner@constellation.com
david.fein@constellation.com
dboehm@bklawfirm.com
dclark1@aep.com
dconway@porterwright.com
dmancino@mwe.com
doug.bonner@snrdenton.com
drinebolt@aol.com
dsullivan@nrdc.org
emma.hand@snrdenton.com
eric.weldele@puc.state.oh.us
etter@occ.state.oh.us
fdarr@mwncmh.com
gardner.gillespie@hoganlovells.com
gary.a.jeffries@dom.com
gdunn@sزد.com
glawrence@mwe.com
grady@occ.state.oh.us
gwung@mwe.com
Greg.Price@puc.state.oh.us
henryeckhart@aol.com
jbentine@cwslaw.com
jkyler@bklawfirm.com
john.jones@puc.state.oh.us
joliker@mwncmh.com
Jodi.Bair@puc.state.oh.us
katie.burke@hoganlovells.com
keith.nusbaum@snrdenton.com
khiggins@energystrat.com
kschmidt@ohiomfg.com
lbell33@aol.com
lgearhardt@ofbf.org
lkollen@jkenn.com
lmcaster@bricker.com

mhpeticoff@vssp.com
mjsatterwhite@aep.com
mkurtz@bklawfirm.com
mwarnock@bricker.com
myurick@cwslaw.com
nedford@fuse.net
nmoser@theOEC.org
ricks@ohanet.org
rplawrence@aep.com
rstanfield@nrdc.org
sam@mwncmh.com
sbaron@jkenn.com
sbloomfield@bricker.com
smhoward@vssp.com
stephen.chriss@wal-mart.com
steven.huffman@morganstanley.com
stnourse@aep.com
thomas.lindgren@puc.state.oh.us
tobrien@bricker.com
todonnell@bricker.com
tommy.temple@ormet.com
trent@theOEC.org
werner.margard@puc.state.oh.us