

1 BEFORE THE PUBLIC UTILITIES COMMISSION OF OHIO

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3 In the Matter of the :
4 Application of Columbus :
5 Southern Power Company for:
6 Approval of its Electric :
7 Security Plan; an : Case No. 08-917-EL-SSO
8 Amendment to its Corporate:
9 Separation Plan; and the :
10 Sale or Transfer of :
11 Certain Generating Assets.:

 :
8 In the Matter of the :
9 Application of Ohio Power :
10 Company for Approval of :
11 its Electric Security : Case No. 08-918-EL-SSO
12 Plan; and an Amendment to :
13 its Corporate Separation :
14 Plan. :

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13 PROCEEDINGS

14 before Ms. Kimberly W. Bojko and Ms. Greta See,
15 Hearing Examiners, at the Public Utilities Commission
16 of Ohio, 180 East Broad Street, Room 11-C, Columbus,
17 Ohio, called at 9:00 a.m. on Thursday, November 20,
18 2008.

19 - - -

20 VOLUME IV

21 - - -

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1 Thursday Morning Session,

2 November 20, 2008.

3 - - -

4 EXAMINER SEE: Let's go on the record.

5 Do we do abbreviated appearances this morning?

6 Starting with the companies.

7 MR. RESNIK: For the companies, Marvin

8 Resnik, Steve Nourse and Dan Conway.

9 MR. SMALZ: For APAC -- excuse me, for

10 Appalachian People's Action Coalition, Michael Smalz

11 and Joseph Maskovyak.

12 MR. O'BRIEN: For the Ohio Hospital

13 Association, Tom O'Brien and Rick Sites.

14 MR. MARGARD: On behalf of the commission

15 staff, Assistant Attorneys General Werner Margard,

16 John Jones, Thomas Lindgren.

17 MS. ELDER: Betsy Elder.

18 MS. GRADY: On behalf of the residential

19 ratepayers of the companies Janine Migden-Ostrander,

20 Ohio Consumers' Counsel, Maureen R. Grady, Jacqueline

21 Lake Roberts, and Michael E. Idzkowski.

22 MR. RANDAZZO: On behalf of the

23 Industrial Energy Users, Joseph Clark, Lisa

24 McAlister, and Sam Randazzo.

25 MS. WUNG: On behalf of the commercial

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1 group, Grace Wung.

2 MR. KURTZ: For Ohio Energy Group, Mike
3 Kurtz.

4 MR. BELL: For the Ohio Manufacturers
5 Association, Lang Bell.

6 MR. YURICK: On behalf of the Kroger
7 Company, John Bentine, Mark Yurick, and Matthew
8 White.

9 EXAMINER SEE: Who at the company is
10 going to be presenting Dr. Makhija?

11 MR. CONWAY: I am, your Honor.

12 EXAMINER SEE: Mr. Conway.

13 MR. CONWAY: Thank you, your Honor. At
14 this time the company calls Dr. Anil Makhija.

15 (Witness sworn.)

16 EXAMINER SEE: Mr. Conway.

17 MR. CONWAY: Thank you, your Honor.

18 - - -

19 ANIL MAKHIJA

20 being first duly sworn, as prescribed by law, was

21 examined and testified as follows:

22 DIRECT EXAMINATION

23 By Mr. Conway:

24 Q. Mr. Makhija, could you state your full

25 name for the record.

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1 A. My name is Anil Kumar Makhija.

2 Q. And could you tell us who your employer
3 is and what your position is.

4 A. I am employed by Ohio State. I am the
5 chairman of the finance department there, and I am
6 also the associate dean for the Fisher College of
7 Business.

8 Q. And, Dr. Makhija, have you prepared
9 direct testimony that's been prefiled in this
10 proceeding?

11 A. Yes, I have.

12 MR. CONWAY: And at this time, your
13 Honor, I would like to mark as Companies' Exhibit
14 No. 5 Dr. Makhija's prefiled direct testimony.

15 EXAMINER SEE: The exhibit will be so
16 marked.

17 (EXHIBIT MARKED FOR IDENTIFICATION.)

18 Q. And, Dr. Makhija, do you have any
19 corrections to make to your prefiled direct testimony

20 at this time?

21 A. Yes, I do. On Exhibit III, which is on
22 page 45, there are two numbers that were carried from
23 the previous exhibit, Exhibit II, but carried over
24 incorrectly. So in Panel A where we have Columbus
25 Southern Power Company for 2006 and 2005, I will give

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1 you the new numbers. They are .1891, so this is
2 under 2006 for Columbus Southern Power, and for 2005
3 the number is .1293. These were the same numbers on
4 Exhibit II and are also the numbers that are
5 correctly used throughout the analysis. It's just a
6 typo in carrying it over.

7 MS. ROBERTS: Mr. Conway, would you
8 repeat those for me, please. I'm sorry.

9 THE WITNESS: Let me repeat it. So on
10 Exhibit III Panel A for Columbus Southern Power
11 Company --

12 Q. Dr. Makhija, which row are you in at this
13 point?

14 A. This is the last row for the numbers
15 given in Panel A and under 2006, the number should
16 read .1891; and for 2005, it should read .1293. And
17 these are also the same numbers that are used
18 throughout the analysis, so it's simply a typo from
19 Exhibit II to III.

20 Q. And for the benefit of the other counsel
21 here, could you just describe which numbers were
22 incorrectly listed on that exhibit.

23 A. Yes. So incorrectly it had said ".1757"
24 for Columbus Southern under 2006 and the incorrect
25 number in 2005 was ".1395."

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1 MR. CONWAY: Ms. Roberts, were you able
2 to follow that?

3 MS. ROBERTS: Yes, thank you very much.

4 Q. And, Dr. Makhija, what is the next
5 correction that you have?

6 A. At this point that would be all.

7 Q. Okay. Dr. Makhija, if I were to ask you
8 the questions in your prefiled direct testimony today
9 as they appear therein together with the corrections
10 that you just identified, would your answers be the
11 same?

12 A. Yes.

13 MR. CONWAY: And at this time, your
14 Honor, Dr. Makhija is available for
15 cross-examination.

16 I would move the prefiled direct
17 testimony, Company's Exhibit No. 5, into the record
18 subject to cross-examination.

19 EXAMINER SEE: Okay. Any volunteers to

20 cross? Mr. Kurtz?

21 MR. KURTZ: Oh, yeah, that's fine. Thank

22 you, your Honor.

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1 CROSS-EXAMINATION

2 By Mr. Kurtz:

3 Q. Good morning, Doctor.

4 A. Good morning.

5 Q. Assume that the Commission were to adopt
6 your -- your testimony exactly as written. Where
7 would the Commission exercise its judgment in setting
8 the significantly excessive earnings test for any
9 particular year?

10 A. The Senate Bill 221 specifically provides
11 for such discretion in several mitigating factors.
12 For example, it offers taking into account the
13 capital expenditures once some threshold has been set
14 as a mitigating factor so there is discretion
15 available to the Commission in applying the numbers
16 that have been presented here.

17 Q. Okay. Is that the only place the
18 Commission would exercise discretion if they adopted
19 your testimony as written?

20 A. Well, there are some other issues which
21 are not directly dealt with in my testimony. For
22 example, the deal with whether these are adjustments
23 that were made to earnings that led to the excessive
24 earnings and those would also be separate issues
25 beyond what is presented here.

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1 Q. Those adjustments, those would be in the
2 determination of the utility's actual earned rate of
3 return?

4 A. Correct.

5 Q. Okay. Where would the Commission
6 exercise its judgment or discretion if it adopted
7 your testimony exactly as written with respect to
8 setting the benchmark for significantly excessive
9 earnings?

10 A. There is also the issue of the Commission
11 accepting the levels of confidence that I have placed
12 here.

13 Q. And what are those levels of confidence?

14 A. I have recommended a 95 percent level of
15 confidence for the confidence interest values that I
16 have presented.

17 Q. That's the two standard deviations?

18 A. That's correct.

19 Q. So if the Commission adopted your

20 testimony exactly as written, it could -- it could

21 use its judgment to take one standard deviation

22 instead?

23 A. I would argue against such an

24 application, but it's certainly a choice they would

25 have for several reasons 95 percent confidence level

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1 is perhaps the most frequently applied confidence
2 level in such situations. I can also walk you
3 through that. It actually presents a fair amount of
4 what I would call false positives. And finally, when
5 you hear most of the time on T.V. and other
6 situations when people talk about, you know, polls
7 and margins of error, et cetera, they are usually
8 talking 95 percent, so while there -- discretion
9 exists, I would imagine they would have to be
10 compelling reasons to move from such a standard.

11 Q. Now, where in your testimony do you
12 recognize the Commission has discretion to not adopt
13 two standard deviations?

14 A. It's my recommendation that they accept
15 the 95 percent, but you might recall that in my
16 testimony I also point out what would happen if the
17 standard were different from this, for example, if
18 they had taken a one standard deviation, what would
19 be the extend of false positive. As demonstrated,

20 false positives would be very frequent. However, if
21 they took a three standard deviations test, it would
22 be rare and so I have provided the argument leading
23 up to the 95 percent.

24 Q. Now, using two standard deviations as you
25 recommend for the year 2007, for example, you

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1 concluded that after tax, return on equities below
2 27.33 percent would not be excessive; is that
3 correct?

4 A. Given the nature of what happened to the
5 nonutility firms in that year, that's what we find,
6 yes.

7 Q. Have you also quantified the threshold at
8 one standard deviation?

9 A. It's not provided in the testimony, but
10 it's something that could be easily calculated.

11 Q. Was 2007 a relatively robust year for
12 earnings of the utility and the nonutility companies
13 in your study?

14 A. If I go by the average rates of returns
15 that were earned by utilities in that year and in
16 particular look at the utility peer sample group that
17 I provided, yes, indeed 17.28 percent for the utility
18 group as provided in my Exhibit II. And if I look at
19 the nonutility group, it was somewhat lower, perhaps

20 closer to 14 percent or perhaps 13.9, so it's a
21 matter of judgment whether you consider those rates
22 to be particularly good years, but on the surface,
23 yes.

24 Q. You understand that the first year
25 application of this test in reality will be using

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1 2009 data for the 2010 review period?

2 A. That's correct.

3 Q. Okay. If the economy continues to sink
4 further into recession, assume, and the earnings of
5 the comparable nonutility groups will -- were
6 negative, substantially negative, so that the results
7 of your analysis came up with a return -- threshold
8 return that threatened the financial viability of
9 these utilities, should the Commission be able to use
10 its judgment to raise the threshold?

11 A. Perhaps we have to think a little harder
12 on that issue because if you think about the Senate
13 Bill, it asks us -- it requires us to look at the
14 nonutility sample. Subsequently if you follow the
15 spirit of the law, it would lead you unfortunately to
16 have a lower average return for nonutilities in the
17 circumstances you describe.

18 But there is one other element which
19 didn't come up in your analysis and that is the

20 nonutility firms also tend to have wider variance so
21 it's an empirical issue whether the low mean would be
22 counter-weighted by a higher variance leading to
23 potentially thresholds that could still be
24 economically meaningful.

25 Q. Do you think the Commission should retain

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1 discretion to make sure that this utility provides
2 essential services that it would not have such a low
3 threshold that its financial viability would be
4 threatened?

5 A. Well, in fact, I have a feeling you are
6 asking me to make a legal judgment because if I
7 should agree with you, I must also simultaneously say
8 that we should walk away from the spirit and letter
9 of Senate Bill 221 because that's what it says to
10 take utility and nonutility firms and subsequently
11 look at their returns as a comparison point. But you
12 are asking me should a commission walk away from that
13 sort of a conflicting situation.

14 Q. Does Senate Bill 221 indicate the
15 weighting between the utility and the nonutility
16 50/50, 70/30, 99-to-1, or any other weighting?

17 A. While it's silent on the weights, it does
18 provides us guidance as to how the sample would be
19 developed.

20 Q. But it doesn't provide any guidance to
21 the Commission as to how the utilities and the
22 nonutilities would be weighted in the analysis; isn't
23 that true?

24 A. Well, it's an automatic outcome of
25 matching the business and financial risks and so the

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1 sample is decided on those criteria. If you walk
2 away from that and attempt to come up with a
3 proportion of how many utilities and nonutilities
4 there might be, we may not find that we met the other
5 requirements of the law, that the businesses and
6 financial risks are unmatched.

7 Q. Does the law specify a weighting between
8 the utilities and the nonutility companies in the
9 comparable groups?

10 A. It only allows for that to emerge as a
11 result of business and financial risk matching.

12 Q. Have you quantified the dollar impact of
13 your conclusion that in 2007 the threshold would be
14 27.33 percent?

15 A. Please, could you explain that further as
16 to the dollar impact for whom?

17 Q. Let me ask you, do you -- do you know
18 what the revenue requirement would be for every 1
19 percent increase in rate of return return on equity

20 afforded to these items?

21 A. I didn't address that issue.

22 Q. Did you look at the testimony of OEG

23 Witness Mr. Kollen where he qualified the revenue

24 requirement effect of every 1 percent ROE for Ohio

25 Power at \$37 million and for Columbus Southern \$19

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1 million?

2 A. I would have to visit that and those
3 numbers at this point. I can accept whatever you've
4 read from his testimony.

5 Q. Are you familiar that less than a week --
6 three days ago the Virginia Commission approved a
7 settlement that AEP Virginia, the Appalachian Power
8 subsidiary, entered into with the Commission staff
9 and other intervenors where they agreed -- where AEP
10 agreed to a return on equity of 10.2 percent?

11 MR. CONWAY: Objection. Your honor, if I
12 might forward looking -- the forward-looking cost to
13 capital established in a rate case in some other
14 jurisdiction is not relevant to the issue in this
15 case, which is what should be the methodology for
16 establishing a significantly excessive earnings test
17 which, of course, is a retrospective review of
18 earnings.

19 MR. KURTZ: I would say that the

- 20 comparable rate of return on equity of a sister
- 21 affiliate company is the most relevant comparable
- 22 group that we would have in this -- under this law
- 23 where we are looking at comparable earnings.
- 24 EXAMINER SEE: And I am going to allow
- 25 Dr. Makhija to answer the question to the extent that

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1 he can.

2 A. The law is very specific. It has
3 wordings that say to look at -- look back at the
4 annual period of earnings and subsequently walks away
5 from forward-looking allowed cost -- allowed rates of
6 returns or cost of capital. So using a benchmark
7 that deals with the allowed rate of return to infer
8 how other utilities and nonutilities may have
9 provided -- provided returns prospectively is not a
10 comparable benchmark.

11 Q. Let me go back to my question. Were you
12 aware that AEP agreed -- Appalachian Power, sister
13 company of Ohio Power and Columbus & Southern, AEP
14 agreed to a 10.2 percent return on equity three days
15 ago -- well, it was approved three days ago by the
16 Virginia Commission? Were you aware of it? That's
17 my only question.

18 A. For the simple reason that these
19 forward-looking items are not relevant, I have not

20 been paying attention to that.

21 Q. Okay. Well, would you accept that the
22 math of the difference between 27.33 percent, which
23 is the 2007 benchmark you have derived, and 10.2
24 percent is 17.13 percent?

25 A. And at the same time I might add to that

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1 difference that there is no guarantee that the firm

2 would actually earn that extra return.

3 Q. Would you agree with my math

4 17 percent -- 17.13 percent higher rate of return

5 given the 1 percent revenue requirement -- 1 percent

6 ROE equals \$37 million for Ohio Power and 19 for

7 Columbus, that 17.13 percent difference between what

8 Virginia approved and what you recommend would cost

9 Ohio consumers \$633 million for Ohio Power and

10 \$325 million for Columbus & Southern per year?

11 MR. CONWAY: Objection.

12 EXAMINER SEE: Basis?

13 MR. CONWAY: First of all, he is

14 testifying himself. If he wants to get up here and

15 get cross-examined, I would be happy to do it.

16 Secondly, he is asking the witness to

17 make a comparison that the witness said he was not --

18 the fundamentals the witness said he was not familiar

19 with in the first place.

20 And, thirdly, he is speculating about
21 what the consequences to Ohio customers on a
22 benchmark in Ohio on a retrospective earnings test is
23 based on what happens in some other jurisdiction;
24 that's irrelevant. And I don't -- the witness is not
25 qualified to answer the question and neither is

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1 Mr. Kurtz.

2 MR. KURTZ: I asked if he agreed with my
3 mathematics. That's -- that's the question on the
4 table, but in a broader sense I think that this case
5 to the extent that the Commission is concerned with
6 the public interest and the economy of Ohio and how
7 Ohio rates compare to the affiliate rates of the
8 other AEP companies, these are absolutely the type of
9 issues the Commission should be addressing and aware
10 of in this record.

11 MR. CONWAY: Your Honor, if I might, he
12 asked him what impact the cost impact on Ohio
13 customers would be if he accepted all of his
14 assumptions and his calculations. He didn't ask him
15 to simply accept what the math was which, of course,
16 the record -- anyone can do the math so that's
17 irrelevant to begin with. But he did not ask the
18 question would you agree with my math. He asked him
19 whether this would lead to a cost impact on Ohio

20 customers.

21 And, secondly, I don't like -- I object

22 to Mr. Bell standing up and intervening in this

23 argument on this objection. It is his -- it is

24 Mr. Kurtz's cross-examination; it's not Mr. Bell's.

25 And I think you ought to stay out of it.

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1 EXAMINER SEE: Okay. Read the question

2 back for me, please.

3 (Record read.)

4 MR. CONWAY: It's also a compound

5 question.

6 MR. KURTZ: Well, your Honor --

7 EXAMINER SEE: Thank you. Wait a minute.

8 Mr. Kurtz, rephrase your question.

9 Thank you, gentlemen. Sit down.

10 MR. KURTZ: Okay.

11 Q. (By Mr. Kurtz) Would you agree with my

12 math under the numbers we just described in the prior

13 question?

14 A. There are so many assumptions within that

15 math that it leads me to imply items that I certainly

16 don't agree with. For example, you've used numbers

17 out of someone else's testimony. Yet another issue

18 is that I have not at all dealt with the revenue

19 implications. That was not the purpose of this

20 testimony. It was simply to establish what the
21 significantly excessive earnings test would imply as
22 threshold items, so while the arithmetic might be all
23 right, it leaves an impression which is not exactly
24 quite defensible.

25 Q. Do you think the Commission should

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1 exercise its judgment when applying this test and
2 take into account issues like the impact on
3 ratepayers, the economy, the level of electric rates,
4 jobs, and factors such as those?

5 A. All I have done is implement Section
6 4928.143(F) of SB 221.

7 Q. I asked you, do you think the Commission
8 should exercise -- when applying the test, should
9 they exercise their judgment, for example, in using
10 one standard deviation instead of two if they -- if
11 the Commission believed that that would be more
12 appropriate for the economy of the state of Ohio?

13 A. It is the Commission's right to choose
14 the confidence level, but it has to be one that is
15 defensible, I presume, and while they could choose
16 one standard deviation, there would be a burden to
17 explain the large amount of false positives that
18 would occur.

19 Remember those false positives are

20 harmful not just to rate -- not only to share
21 owners -- holders, but also to ratepayers because
22 they place the firm in a position where being perhaps
23 too efficient can lead you into expropriations.

24 Q. When you did your analysis, you didn't
25 consider the affiliate relationships between Ohio

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1 Power, Columbus Southern, Indiana and Michigan,
2 Appalachian Power, and Kentucky Power as members of
3 the AEP Interconnection Agreement, did you?

4 A. I have used AEP as a whole as a parent
5 company without looking at the specific pieces that
6 you have mentioned.

7 Q. For example, did you take into account
8 the fact that Ohio Power is required to sell its
9 excess capacity -- excess energy to its affiliates at
10 cost before selling that power off system?

11 A. I am wondering how that element would
12 affect the significant excessive test.

13 Q. Just a small point. You recommend
14 combining the earnings of Columbus Southern and Ohio
15 Power for purposes of this test; is that correct?

16 A. Not exactly. What I have done is I have
17 applied the test specifically to Ohio Power and
18 specifically to Columbus Southern Power. However, I
19 have suggested that in looking at their rates of

20 return it may be useful as additional benchmarks to
21 look at what the combined rate of return would have
22 been.

23 Q. Let me quote to you a portion of the
24 statute that you have cited on page 10 of your
25 testimony. It says: "In making its determination of

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1 significantly excessive earnings under this division,
2 the Commission shall not consider directly or
3 indirectly the revenue expenses or earnings of any
4 affiliate or parent company." How do you square
5 combining the -- combining the earnings of these
6 affiliates given this statutory prohibition?

7 A. Okay. So what you are reminding us is
8 that the statute is very explicit with regard to how
9 we should ignore the revenues, expenses, and earnings
10 of the parent or affiliates in applying the test.
11 And as you will see in my testimony, I have not
12 explicitly taken into account the revenue expenses or
13 earnings of this parent or the affiliates. What I
14 have done, however, is used the parent firm to impute
15 what might be the market's perception of the
16 riskiness of the AEP-Ohio companies, which is I think
17 a distinctly different action.

18 Q. Let me go back to my first question. I
19 think this is my last one. Are there any other

20 elements of judgment or discretion that you think the
21 Commission should exercise in applying the earnings
22 test other than the ones you've already mentioned?
23 A. In the narrow confines of 4928.143(F),
24 those are the mitigating factors as I mentioned
25 earlier.

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1 MR. KURTZ: Thank you, Doctor. Thank
2 you, your Honors. No more questions.

3 EXAMINER SEE: Mr. Bell.

4 MR. BELL: No questions.

5 EXAMINER SEE: Mr. Yurick.

6 - - -

7 CROSS-EXAMINATION

8 By Mr. Yurick:

9 Q. Doctor, can you hear me okay?

10 A. Yes, thank you.

11 Q. Okay. On page 6 you talk about your
12 calculations for return on equity. This is on page
13 6, lines 3 and 4 of your testimony.

14 A. Which lines are you referring to?

15 Q. 3 and 4. And you say: "Significant
16 Excessive Earnings test requires a book measure of
17 earnings, ROE, calculated as net income divided by
18 book equity." Do you see that?

19 A. Yes.

20 Q. Would you agree with me that net income

21 would include or have you included income from

22 off-system sales in your calculation?

23 A. As you know, in my testimony I have made

24 no adjustments to the income at this point. However,

25 I am aware that other witnesses from the company are

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1 discussing this particular issue of off-system sales.
2 While I might support their position, I have not
3 actually included that correction into my net income,
4 so I will leave it to them to defend that issue and
5 to see how the Commission would like those items to
6 be incorporated. You might argue that, you know,
7 off-system sales --

8 Q. I think you answered my question so at
9 this point you are just kind of -- okay. I think you
10 answered my question. You are not the correct
11 witness to ask this so that's fine.

12 MR. YURIK: And I don't have any further
13 questions of this witness.

14 EXAMINER BOJKO: I'm sorry, are
15 off-system sales included in your net income number
16 because they were included in somebody else's net
17 income number that you used?

18 THE WITNESS: That's right. I have not
19 removed them.

20 EXAMINER BOJKO: Thank you.

21 EXAMINER SEE: Ms. Wung.

22 MS. WUNG: Yes, actually, just one or two

23 questions.

24 - - -

25

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1 CROSS-EXAMINATION

2 By Ms. Wung:

3 Q. Good morning, Dr. Makhija. My name is
4 Grace Wung. I am with the commercial group. Just
5 actually one or two questions.

6 Do you believe that the significantly
7 excessive earnings test for AEP should be reasonable
8 comparable to the same test for other Ohio utilities?

9 A. We have good guidance from the Bill on
10 that issue. It asks us to match the business and
11 financial risks so subsequently it is quite possible
12 that utilities within the same state might differ in
13 the levels of their business and financial risks, so
14 following the spirit and letter of the Senate Bill
15 that's what one should do and it might, therefore,
16 end up with perhaps different comparable samples.

17 Q. So because of the varying or differing
18 financial or business risks associated with each of
19 the Ohio utilities they may -- may or may not be

20 reasonable to compare one to the other?

21 A. Yes.

22 Q. Have you also examined the other Ohio

23 electric utilities in terms of Duke Energy or

24 FirstEnergy?

25 A. No, I've not done any analysis on those.

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1 Q. And did you review any of their -- their
2 financial or business risks to determine whether or
3 not they would fall into a comparable sample?

4 A. I have not done that determination but
5 there is no reason to presume that -- that all
6 utilities in Ohio are identical.

7 Q. But you have not conducted that analysis?

8 A. That is true.

9 Q. So comparing your comparable peer group
10 you didn't review whether or not Duke Energy Ohio,
11 FirstEnergy companies in Ohio would be comparable?

12 A. I have not done that analysis, but I have
13 no reason to believe that they are necessarily
14 identical.

15 Q. Why is it you would have no reason to
16 believe if you haven't conducted an analysis?

17 A. While I would not be able to speak to the
18 great details of what follows, I am generally aware
19 of the differences in, for example, beta risks of

20 companies and so forth. And as you might know, they

21 are not the same.

22 MS. WUNG: Thank you, Dr. Makhija. I

23 have no further questions.

24 EXAMINER SEE: Mr. Randazzo.

25 MR. RANDAZZO: Yes.

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1 - - -

2 CROSS-EXAMINATION

3 By Mr. Randazzo:

4 Q. Yes. Good morning.

5 A. Good morning.

6 Q. Did you assist in any way in the
7 preparation of AEP's electric security plan, in the
8 preparation of that plan?

9 A. Only to the extent that I addressed the
10 issue in Section 4928.143(F).

11 Q. Have you -- did you review the plan as
12 part of your preparation for this case?

13 A. Only in passing, nothing that I would be
14 able to, you know, address in specifics.

15 Q. So as far as your methodology is
16 concerned, it stands alone and is not connected to
17 the plan that was filed by AEP; is that correct?

18 A. The purpose of my activity here was to
19 develop a methodology. Subsequently -- the specific

20 numbers used as an illustration for that methodology

21 are not important ultimately. Subsequently the

22 contents of the ESP are not directly relevant yet.

23 Q. All right. And so you didn't look at the

24 ESP that was filed by the AEP Ohio companies for

25 purposes of examining how it might alter the current

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1 risk financial and business risks that are described
2 in your testimony; is that correct?

3 A. Yeah. And given that the law -- the SB
4 221 about significantly excessive is a look-back law,
5 I presume that determination would also occur not
6 looking forward but looking back in 2010.

7 Q. Right. And at least from an academic
8 perspective, it would be appropriate to take a look
9 at this methodology at the time that you were looking
10 back for purposes of making sure that the methodology
11 still was valid, correct?

12 A. I agree.

13 MR. RANDAZZO: Thank you.

14 That's all I have. I'm sorry. A little
15 slow today. Injected with drugs. Sorry.

16 EXAMINER SEE: Ms. Roberts?

17 MS. ROBERTS: Thank you, your Honor. I
18 probably need a microphone. I'm losing my voice.

19 EXAMINER SEE: Yes.

20 - - -

21 CROSS-EXAMINATION

22 By Mr. Roberts:

23 Q. Good morning, Dr. Makhija.

24 A. Good morning.

25 Q. I just have a couple of preliminary

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1 matters. First, would you agree in finance there is
2 a presumption of a positive relationship between risk
3 and return?

4 A. Yes.

5 Q. And would you agree that beta which you
6 have used is considered to be a measure of investment
7 risk?

8 A. Yes.

9 Q. And would you agree beta reflects both
10 business and financial risk?

11 A. Indeed that's what I have argued myself.

12 Q. On page 3 of your testimony you indicate
13 you have appeared as an expert witness before FASB.
14 What is FASB and what does it do?

15 A. FASB is the Financial Accounting
16 Standards Board, and the issue before FASB had been
17 how one -- how utilities should close/cancel plant,
18 and in that context I appeared before FASB in
19 Stamford to give my opinion.

20 Q. And on page 3, line 4, you indicate you

21 submitted a report to FERC?

22 A. Yes, I did.

23 Q. Was that on generic determination of rate

24 of return?

25 A. Yes.

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1 Q. Did you testify in that proceeding?

2 A. No, only a report was submitted.

3 Q. And on page 4 you indicate you testified
4 as an expert witness in Pennsylvania?

5 A. Yes, I did.

6 Q. What did your -- what were the subject
7 matters of your testimony?

8 A. This was litigation that involved
9 majority share owner versus a minority share owner
10 and the question was what was the value of minority
11 shares, in which case one deals with issues dealing
12 with minority rights and also liquidity when you have
13 only two owners and one of them owns very little.

14 Q. When did this testimony occur? What
15 year?

16 A. Give me a moment. Shall I get that exact
17 information for you later?

18 Q. Just generally.

19 A. It's more than 10 years back.

20 Q. All right. That's fair. And did this

21 case involve determining a rate of return?

22 A. No.

23 Q. And it didn't involve determining

24 significantly excess earnings, correct?

25 A. That's right.

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1 Q. Did you testify in any other Pennsylvania
2 cases?

3 A. No.

4 Q. On page 4 you indicate that you have made
5 presentations or presented papers to a number of
6 organizations; is that correct?

7 A. That's correct.

8 Q. What was the subject of your presentation
9 to American Electric Power?

10 A. It's a number of different topics that
11 have been covered in presentations that I have made
12 before American Electric Power. They are part of the
13 executive development program that is offered by the
14 Fisher College of Business, and it's a program that
15 has been going on for several years. It includes
16 reviewing the financials of electric utilities,
17 paying particular attention to AEP, looking at their
18 capital structure, looking at the rates of returns
19 they have earned, and various related matters.

20 Q. Is that an executive MBA program?

21 A. I also do teach in the executive MBA

22 program but this is separate from that which is

23 specifically customized to the issues of American

24 Electric Power.

25 Q. Did you make any presentations to them on

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1 the calculation of rate of return, return on equity,
2 or significantly excess earnings?

3 A. As you know, Ohio is about the only state
4 that has that law so the chances of doing a
5 significantly excessive test for anyone else is a
6 near zero probability.

7 Q. I think my question was did you make a
8 presentation to American Electric Power on
9 significant -- on the calculation of significantly
10 excess earnings?

11 A. No.

12 Q. On calculation of rate of return or cost
13 of equity?

14 A. Yes, those are items that I have
15 presented in those including estimates of what I
16 think are the cost of capital for AEP.

17 Q. Have you ever testified in a utility rate
18 proceeding or a state utility commission?

19 A. No, I have not.

20 Q. Have you ever testified before the

21 Federal Energy Regulatory Commission?

22 A. Apart from submitting that report, I have

23 not.

24 Q. On page 5 of your testimony, lines 8

25 through 11, you say that: "Since both OP and CSP are

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1 wholly-owned subsidiaries of American Electric Power
2 and share in its electric and financial pools, the
3 methodology for the implementation of the
4 Significantly Excessive Earnings Test cannot be
5 isolated to the two operating companies but must
6 incorporate the business and financial risk of AEP";
7 is that correct?

8 A. Yes.

9 Q. And you also interpret SB 221 as it
10 relates to the description of this test to require
11 you to incorporate the business and financial risks
12 of AEP in calculating significantly excess earnings
13 for Ohio Power Company and Columbus Southern Power
14 Company; is that correct?

15 A. Yes, I do and, in fact, I'm not alone in
16 doing so as provided in my testimony particularly on
17 page 16 Standard & Poor's Todd Shipman in its Ratings
18 Direct in July of 2007 specifically points out that
19 when looking at the -- at Ohio Power or looking at

20 Columbus Southern one ought to look at AEP, so I am

21 not alone, the market also -- the street also does

22 the same.

23 Q. And did they offer testimony before this

24 Commission on the calculation of significantly excess

25 earnings?

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1 MR. CONWAY: Object.

2 A. No, they have not to my knowledge.

3 Q. All right. When you form your portfolio
4 of publicly traded firms irrespective of each firm's
5 industry affiliation, you attempt to match the
6 business and financial risks of AEP and thus for OPC
7 and Columbus Southern; is that fair?

8 A. Yes.

9 Q. How many utility subsidiaries does
10 American Electric Power have?

11 A. Could you please repeat that?

12 Q. How many utility subsidiaries does
13 American Electric have?

14 A. I don't want to guess that at this point.

15 Q. Do you know what states American Electric
16 Power operates in?

17 A. Oh, yeah, I think they are in 11
18 different states.

19 Q. Do you know what those states are?

20 A. Well, I could try to remember them all,

21 but yeah, I know most of them.

22 Q. All right. How many nonutility

23 subsidiaries does American Electric Power have?

24 A. Well, I don't know the specific numbers

25 of them, but we do know that American Electric Power

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1 draws 90 percent of its earnings to its revenues from
2 its electric operations. So we have --

3 Q. Both regulated and unregulated or only
4 regulated?

5 A. I would have to look at the details. I
6 am trying to understand how this is leading to the
7 significant test, however.

8 Q. I think it will become apparent. Would
9 it make a difference in your analysis and
10 determination of what comparable business financial
11 risk is to know whether 90 percent of the company you
12 selected as a proxy, American Electric Power,
13 receives its revenues from regulated operations or
14 unregulated operations?

15 MR. CONWAY: Could I have the question
16 reread, your Honor.

17 EXAMINER SEE: Yes.

18 (Record read.)

19 MR. CONWAY: Just so I am clear, is the

20 question would it make a difference whether you
21 assume that 90 percent were from regulated operations
22 on the one hand and on the other hand that 90 percent
23 were from unregulated operations?

24 MS. ROBERTS: Yes.

25 EXAMINER SEE: You can answer the

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1 question.

2 A. Okay. There are many factors that you
3 could point out about a utility and they would all be
4 potentially interesting. But at the end of the day I
5 would be interested in summatively what did they
6 imply for the risk of the company. In my testimony I
7 provide summative risk measures.

8 Q. I'm sorry to interrupt, the what risk
9 impact?

10 A. Summative.

11 Q. Summative?

12 A. Yeah, because what I am suggesting is
13 that you could, Mrs. Roberts, could come up with a
14 whole series of individual aspects which may all
15 speak to the riskiness of the firm and surely some
16 aspects might point one way and others in another
17 way, but at the end of the day I am employing a risk
18 measure which looks at the totality of the risk and
19 subsequently, yes, those factors are ultimately

20 working their way into that summary measure.

21 Q. Well, let me just get down to it,

22 Dr. Makhija, have you done any risk analysis of AEP

23 subsidiaries to support your claim that Ohio Power

24 and Columbus Southern Power have the same risk

25 profile as AEP?

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1 A. I would certainly love to address that
2 issue. As you know, I have provided a summative risk
3 measure for American Power.

4 Q. I'm sorry, Mr. Makhija, could you answer
5 my question yes or no first so I know whatever else
6 you said?

7 THE WITNESS: Could you please repeat the
8 question?

9 EXAMINER SEE: Reread the question for
10 the witness.

11 (Record read.)

12 MR. CONWAY: And, your Honor, I would
13 object to the interjection by counsel. She is
14 guessing -- he hasn't even had a chance to answer it,
15 and she is objecting to his answer. I think he was
16 addressing her question, and I would just ask that he
17 been allowed to complete his answer before she
18 follows up.

19 EXAMINER SEE: Okay.

20 MS. ROBERTS: Your Honor, I am willing to

21 indulge the witness beyond a yes or no answer. I

22 would just like to know whether his answer is yes or

23 no before he extrapolates on it.

24 EXAMINER SEE: Is there an objection or

25 just -- that's okay.

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1 MR. CONWAY: There is an objection.

2 EXAMINER SEE: Dr. Makhija, go ahead and
3 answer the question.

4 THE WITNESS: Could you repeat it one
5 more time, please.

6 (Record read.)

7 A. I guess the answer is a qualified yes.

8 Should I proceed to explain the qualification? What
9 I have done is in looking at AEP as a whole, I have
10 automatically taken the influence of the subsidiaries
11 into account. So subsequently when I talk about the
12 beta for AEP, it is as a result of all the
13 subsidiaries participating in it.

14 Q. On page 6 of your testimony you propose a
15 test for, can we call the significantly excess
16 earnings test S-E-E? Is that acceptable to you,
17 Dr. Makhija?

18 A. Sorry, which line are you referring on
19 page 6?

20 Q. I am going -- I am going to ask you a

21 question about page 6 of your testimony.

22 A. Okay.

23 Q. And before I do would it be acceptable to

24 you to refer to the significantly excess earnings

25 test as SEE or S-E-E?

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1 A. Sure.

2 Q. On page 6 of your testimony you propose a
3 test for SEE using a utility peer group and a
4 comparable risk peer group. Why did you use a
5 utility peer group?

6 A. I started with utility peer group to, in
7 fact, point out that in some cases and in particular
8 this one what seems like an obvious which is to pick
9 up other utilities isn't necessarily the right thing
10 to do because in picking up the utility peer group, I
11 am able to show that at the end of the day even
12 though they are utilities, they don't have the same
13 risk characteristics as the subject utility.
14 Subsequently, it makes a greater case to develop the
15 comparable risk peer group.

16 Q. Continuing to pages 11 and 12 of your
17 testimony, specifically on page 11, lines 20 to 23,
18 and page 12, lines 1 to 2, you seem to indicate that
19 using your Compustat -- Compustat data that the

20 earliest this Commission could determine an
21 application for significantly excess earnings would
22 be the end of August of the year following the year
23 that calculation was made?

24 A. Purely as a practical matter, yes,
25 because even though firms have finished the year, by

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1 the time they file all the data and it shows up in
2 the standard databases, unfortunately it takes a
3 while.

4 Q. But if you were to use Value Line data
5 and FERC Form 1 data, that would be available months
6 earlier, would it not, Dr. Makhija?

7 A. You can imagine the problems that would
8 present since we are welcome to choose comparable
9 firms from all nonutility firms. You can imagine the
10 difficulty of trying to find for all 7,000 plus firms
11 updated data that is, you know, reliable at that
12 point. So as a practical matter, unless one wants to
13 go hand-collect forms, so much data, one might have
14 to wait until these databases are publicly available.

15 Q. Are you saying that this Commission
16 should use only the Compustat database that you have
17 used?

18 A. No. I am perfectly happy with Value
19 Line. In fact, given that only a fragment of the

20 data was available at the time when I used it, I
21 would welcome, you know, updated analyses as well,
22 but just that one should do the analysis when the
23 data is indeed fully available, be it Value Line or
24 other reliable databases.

25 Q. Did I understand you to just say that it

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1 was acceptable to you to use Value Line in this
2 computation or some other source -- recognized source
3 of financial data?

4 A. Not at that point in time because at that
5 point in time I was able to get from Compustat what
6 had been updated for 2007. I did not have the same
7 assurance whether Value Line was also completely
8 updated at that point.

9 Q. But as a data source, you don't take
10 issue with Value Line, do you?

11 A. No, I have not.

12 Q. On page 16 beginning at line 22 of your
13 testimony, when you are discussing utility peer
14 group, you said that you excluded SIC Code 4913 firms
15 (Electric Utilities - West). Why did you do that?

16 A. To the extent that people that put
17 together SIC codes have even determined that the east
18 coast utilities and west coast utilities should be
19 combined into a single four-digit SIC code 4911,

20 that's an exertion that they are better fit as an
21 industry group, whereas, they kept 4391 separate, so
22 I am recognizing that difference.

23 Q. Didn't you say that you excluded Electric
24 Utilities - West because of differences in weather
25 and operating characteristics?

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1 A. Yes, I did. And those might be part of
2 the reasons why people who develop SIC codes
3 considered them to be, in fact, a different
4 four-digit SIC code industrial.

5 Q. Do you know if that is why people that
6 develop the SIC codes gave them a separate SIC code?

7 A. No. But I am offering some possible
8 explanations.

9 Q. But you don't know?

10 A. Correct.

11 Q. And did you do any analysis to support
12 your conclusion that the Electric Utilities - West
13 should be excluded?

14 A. Remember, the purpose of the utility peer
15 group, the purpose of that was to find reasonable
16 companies and show why risk differences might be
17 left. And for that purpose including these utilities
18 would have been including ones that were already
19 known to be in a different SIC code.

20 Q. But you didn't do any studies or analysis
21 of whether it was appropriate to use one or more SIC
22 codes, did you, Dr. Makhija?

23 A. No, because I am not -- my purpose here
24 was not to develop computations of different SIC
25 codes but to accept what is publicly available.

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1 Q. But didn't you just testify that you

2 didn't know why they had different SIC codes?

3 A. I did offer some potential explanations.

4 Q. But you don't know.

5 A. Correct.

6 Q. And you have done no analyses of your own

7 to support that.

8 A. Correct.

9 Q. That distinction you make. Has it been

10 your position regarding the calculation of return on

11 equity for electric utilities that -- that that

12 calculation should exclude certain utility SIC codes,

13 for example, SIC codes 4913 Electric Utility - West?

14 MR. CONWAY: Excuse me. Could I have

15 that question reread, please?

16 EXAMINER SEE: Yes.

17 (Record read.)

18 MR. CONWAY: Your Honor, I object. I

19 think it has been gone over a couple of times.

20 Ms. Roberts -- I think the witness has explained that
21 her disagreement is really with the people who
22 develop the SIC codes, not with him. He is just
23 following what the SIC codes indicate, which ones are
24 separate, and he is trying to find a comparable group
25 of electric utilities based in part on common SIC

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1 codes and I think he has already gone over it and she
2 has -- she has gone through it at least once, if not
3 twice.

4 MS. ROBERTS: Why don't I lay a
5 foundation, your Honor. Maybe that will be helpful.

6 EXAMINER SEE: Please.

7 Q. (By Ms. Roberts) Your calculation of SEE
8 involves determining comparable business and
9 financial risk; is that correct?

10 A. Yes.

11 Q. And is that also -- is that -- are those
12 also criteria you would use in calculating a return
13 on equity for a utility?

14 A. Are you asking prospectively or --

15 Q. Yes.

16 A. -- the actual earned returns?

17 Q. No, prospectively.

18 A. If I were doing a determination of what
19 should be or what is the cost of capital allowed

20 return going forward, I might, yeah.

21 Q. And -- and yet for the SEE test you make

22 a distinction between electric utilities by SIC

23 codes, what I am asking you is would you make that

24 same distinction by SIC codes if you were calculating

25 a projected return on equity for a utility?

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1 A. I think we are talking about two
2 different things here, if I may take just a moment of
3 your time. Remember, in -- there are two different
4 tests being offered here. One is the utility peer
5 group test, and the second is the comparable risk
6 peer group. And in the developing of the utility
7 peer group I am following what is commonly done which
8 is to try to look at utilities that seem most
9 comparable which I do by picking up the SIC code, by
10 looking at size, looking that they are all, you know,
11 traded then on NYSE and so forth and, in fact, at the
12 end of that analysis I am suggesting this may not be
13 the best route because ultimately the groups don't
14 line up being comparable.

15 However, in the second test, because I
16 don't need anymore to simply having chosen the firms
17 to then test if they are comparable, I start by
18 making them comparable on the grounds of business and
19 financial risk and then develop the comparable risk

20 peer group. So the questions in some sense, the
21 reason I am hesitating is that they -- they are two
22 different issues and methodologies and I am being
23 asked to answer the same question on both sides.

24 Q. Do you know of any rate of return experts
25 or economists that have concluded that electric

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1 utility in -- electric utilities in Ohio are not
2 comparable to electric utilities in SIC code 4913
3 Electric Utilities - West?

4 A. No.

5 Q. Panel A shows the 2007 -- 7 comparable
6 risk peer group.

7 MR. CONWAY: Which exhibit?

8 A. What page?

9 Q. That's pages 65 and 66 of your testimony.

10 MR. CONWAY: Just for the record that's
11 Exhibit IX?

12 MS. ROBERTS: Thank you.

13 Q. Is it true that Exhibit IX shows your
14 2007, 2006, and 2005 comparable risk peer group
15 firms?

16 A. Yes, it does.

17 Q. Okay. On line 2401 -- do you see that?

18 MR. CONWAY: If I might inquire, is this
19 on page 65?

20 MS. ROBERTS: It's on Exhibit IX, Panel

21 A.

22 A. Yes.

23 Q. It appears that you include PG&E.

24 A. Yes, I do.

25 Q. Is that an Electric Utilities - West

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1 group?

2 A. Yes, it is.

3 Q. I thought you excluded Electric

4 Utilities - West groups from your --

5 MR. CONWAY: Objection. We have already

6 gone through this. There is two tests, there is the

7 utility peer group approach and then there is a

8 comparable risk peer group approach and he explained

9 two answers before, I think, what the difficulty is

10 in mixing the two approaches which is what OCC is

11 trying to do again. He explained that he didn't use

12 the SIC code in the second approach. He explained

13 why he didn't do it because he directly measures

14 financial and business risk, and he explained why he

15 did do it in the first case with the utility peer

16 group approach. And now, we are going through it

17 again.

18 EXAMINER SEE: Thank you, Mr. Conway.

19 MS. ROBERTS: I just want Dr. Makhija to

20 explain why he used one in one test and not in the

21 other.

22 MR. CONWAY: And he just did in two

23 answers prior.

24 EXAMINER SEE: Thank you, Mr. Conway.

25 Your objection is -- your objection is overruled.

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1 Let's read the answer back and let

2 Dr. Makhija answer the question.

3 (Record read.)

4 EXAMINER SEE: I am sorry, I am going to
5 need to ask you the question again.

6 MS. ROBERTS: That's fine. I am happy to
7 do that.

8 Q. (By Ms. Roberts) On line 2401,
9 Dr. Makhija, you included PG&E in your comparable
10 risk peer group. Isn't that an Electric Utilities -
11 West?

12 A. Yes, I did. Here is the reason for that.
13 In the utility peer group test I am making effort to
14 make the firms comparable by picking up the SIC code
15 in which AEP resides and picking up the firms which
16 are other ones in the same SIC code which are the
17 4911 firms. There my effort is to get comparability
18 by the selection of the comparable firms themselves.
19 However, in the second test I am taking the business

20 risk and financial risk characteristics and then
21 finding the firms that happen to fit that. And
22 subsequently this firm appears as one which lands up
23 having comparable business and financial risk and is
24 included subsequently because there is no SIC test in
25 the second application.

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1 Q. Doesn't that just underscore that
2 comparable utilities in the west could have similar
3 business and financial risks?

4 A. It's possible. Indeed you can always
5 pick a specific firm which could land up having
6 comparable, you know, results but, remember, that in
7 the development of the utility peer group I made a
8 good effort to be in the same industry as narrow as a
9 four-digit SIC code as the firm itself, took size
10 into account, took listing into account, so I am
11 making an effort to make them comparable. That does
12 not mean that you could not find one other firm
13 somewhere else that could also have fit.

14 Perhaps if we had looked at the our
15 4913s, we may have found that putting them in would
16 have been a problem. Look at this Exhibit IX again.
17 How many 4913 firms do we find there? Very few,
18 which means that if I had included them in the
19 utility peer group sample as a whole, I might have,

20 in fact, distorted my analysis.

21 Q. And, finally, on page 17, lines 4 and 5,
22 you discuss the effect of size as related to risk --
23 size of market capitalization as it relates to risk.

24 A. Yes.

25 Q. And is it fair to say that your statement

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1 is that larger firms generally are less risky?

2 A. That's correct.

3 Q. So wouldn't it be true then that Ohio

4 Power and Columbus Southern Power -- you agree they

5 are smaller.

6 A. Yes.

7 Q. -- are generally less risky than AEP or

8 other publicly-traded companies comparable to AEP?

9 A. I'm sorry, because they are smaller they

10 might, in fact, be more risky so, therefore, the test

11 being presented is a conservative test.

12 Q. On pages 17 to 19 do you discuss the

13 capital asset pricing model?

14 A. Yes, I do.

15 Q. Or CAPM?

16 A. Yes.

17 Q. And you used CAPM to examine the risks

18 faced by common equity holders; is that correct?

19 A. Yes.

20 Q. Is the primary use of CAPM and rate of

21 return analysis to measure risk?

22 A. It's frequently used, yes.

23 Q. And you make this statement on page 20,

24 line 12: "Business risks for electric utilities are

25 higher in Ohio than in other states." Did you do any

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1 studies or analyses to determine that this statement
2 is accurate?

3 A. I will refer you to some statements that
4 I have reported from the street. In particular, I
5 believe, there is statements from Merrill Lynch, et
6 cetera talking about how this particular test that we
7 are discussing constitutes special risks in Ohio.
8 But in addition I will point you to testimony I
9 believe that another witness from AEP, Mr. Craig
10 Baker, is placing regarding this very issue in which
11 he lists a whole set of different risks that are
12 special to Ohio. So it is on the basis of both with
13 the market, as in Merrill Lynch, were and what I
14 understand from Mr. Baker, but I will point you to --
15 in his direction to discuss those specific risks.

16 Q. Dr. Makhija, we are going to be here a
17 long time if we can't accomplish me asking you a
18 question and you answering the question without
19 elaborating on it.

20 MR. CONWAY: Objection.

21 MS. ROBERTS: You can -- your Honor, in

22 redirect Mr. Conway can do that.

23 EXAMINER SEE: Ms. Roberts, at this point

24 you can ask the question. Dr. Makhija gets an

25 opportunity to answer.

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1 Q. So I just want to make sure I understand,
2 you have not done any studies or analyses of Ohio
3 electric utilities to determine whether their
4 business risks are higher than utilities in other
5 states?

6 A. I just cited you Merrill Lynch which is a
7 reputable firm.

8 Q. Study.

9 A. I have not done the study, but I am
10 giving you indicators that are available about these
11 higher risks.

12 Q. So you have looked at what Merrill Lynch
13 has said about it, but you have not done a study or
14 an analysis to determine a basis for your statement
15 that business risks for electric utilities are higher
16 in Ohio than other states?

17 MR. CONWAY: Objection. That's been
18 asked and answered. I don't know.

19 EXAMINER SEE: That's enough. I disagree

20 that Dr. Makhija has answered the question. I think
21 it was have you done any studies to determine whether
22 the business risks for electric utilities in Ohio are
23 higher.

24 A. I have not.

25 Q. You have not. Thank you.

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1 EXAMINER BOJKO: Can you -- did Merrill

2 Lynch say "special risk" or "higher risk"?

3 THE WITNESS: Let me look for that quote.

4 If I have your permission, perhaps I could read to

5 you the wordings.

6 EXAMINER BOJKO: Please.

7 THE WITNESS: So this says from Merrill

8 Lynch's focus on Ohio on April 25, 2008, it is cited

9 in my testimony starting on page 27 going to page 28.

10 It says about the significantly excessive earnings

11 test. "The language is quite broad and allows the

12 Public Utilities Commission of Ohio, PUCO,

13 considerable discretion in determining the comparable

14 companies (which are not limited to utilities) and

15 what constitutes significant overearning . . . The

16 earnings test may be something of a 'stick' for the

17 PUCO to moderate the rate impact over time,

18 especially if market prices continue to rise."

19 Given that this test does not apply to

20 any other state, this makes Ohio uniquely riskier on

21 this particular item.

22 EXAMINER BOJKO: Okay. But you got from

23 that statement alone is where you then wrote your

24 statement that the business risk in -- for Ohio

25 utilities is higher.

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1 THE WITNESS: No. In addition I also
2 pointed to Mr. Craig Baker.

3 EXAMINER BOJKO: To an AEP witness.

4 THE WITNESS: Yes.

5 EXAMINER BOJKO: Thank you. Sorry,
6 Ms. Roberts. Please continue.

7 Q. (By Ms. Roberts) So your testimony is
8 that the streets' acknowledgment that this is a
9 unique test in Ohio is what, in fact, makes it
10 riskier?

11 A. This is an element of it, yes.

12 Q. You have studied utilities for some time,
13 haven't you, Dr. Makhija?

14 A. Yes.

15 Q. And you are aware, aren't you, that there
16 are certain rating agencies that evaluate commissions
17 in different states and rate them as less favorable
18 or more favorable --

19 A. Yes.

20 Q. -- in terms of regulation? And being a
21 resident of Ohio and an expert witness for AEP, you
22 are aware, aren't you, of what the Ohio rating is for
23 favorable or unfavorable ratings for the regulation
24 of electric utilities here?

25 MR. CONWAY: Objection, your Honor.

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1 EXAMINER SEE: What grounds?

2 MR. CONWAY: The foundation. We don't
3 have a period of time. Are we talking about the
4 ratings for Ohio in 2007 or 2006, or are we talking
5 about a forecasted valuation for 2009 which is when
6 his testimony is supplied?

7 MS. ROBERTS: I am just asking if he is
8 aware at this point.

9 EXAMINER SEE: Give us the foundation.

10 MS. ROBERTS: I'm sorry?

11 EXAMINER SEE: Give us some foundation
12 for your question, Ms. Roberts.

13 Q. And the ratings agencies you said you
14 were aware of will rate commissions over different
15 periods of time; is that correct?

16 A. They do, yes.

17 Q. They do. And what agencies are you
18 aware -- of what agencies are you aware that do these
19 kind of ratings?

20 A. Similar to, I believe Fitch has
21 something, and I am wondering what you are looking
22 for.

23 Q. And let's take Fitch, for example. What
24 period of time -- for what periods of time does it
25 evaluate commissions and the favorability or

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1 unfavorability of regulation to electric utilities in
2 the states?

3 A. At this point I am not up on all those
4 details.

5 Q. Are you aware of how the Ohio utility
6 commission has been ranked in terms of favorable or
7 unfavorable regulatory environment?

8 A. I don't recall.

9 Q. You don't recall. But you are testifying
10 about a utility's -- you are testifying about the
11 business risk for utilities in Ohio. You don't know
12 how the Commission has been rated?

13 MR. CONWAY: Objection, your Honor. And
14 I will reiterate the grounds I just gave. We are
15 talking about a time period that's relevant for his
16 testimony is the risk the company faces going forward
17 in 2009, '10, and '11 and what might have been the
18 case in 2007, '6, '5, or whatever period it is you
19 are referring to while you are chortling is not

20 relevant.

21 EXAMINER SEE: Thank you, Mr. Conway.

22 MS. ROBERTS: I am finished with this

23 line, your Honor. That helps a bunch.

24 Q. You also use in your testimony,

25 Dr. Makhija, a comparable risk peer group?

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1 A. Yes.

2 Q. Now, to arrive at a benchmark ROE to
3 determine SEE, did you not identify a group of public
4 companies?

5 A. Sorry. I did.

6 Q. You did.

7 A. Yeah.

8 Q. And the public companies you identified
9 comprise the comparable risk peer group?

10 A. Yes.

11 Q. All right. And did you describe the
12 universe of companies covered by the Compustat
13 database to determine this peer group?

14 A. Yes.

15 Q. And on what basis did you divide this
16 universe?

17 A. I followed the dictates of SB 221 which
18 requires the funds be matched on business risk and
19 financial risk so those were the two criteria that I

20 employed.

21 Q. And what business risk indicator did you
22 use?

23 A. I used the unlevered beta.

24 Q. And financial risk?

25 A. The book equity ratio.

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1 Q. If I look at, for example, Value Line or
2 Yahoo!, will I find the unlevered beta or equity
3 market or book equity ratios as you said listed for a
4 company?

5 A. Certainly the data is available to obtain
6 those, yes.

7 Q. But aren't these your calculations and
8 not the published -- not the published data?

9 A. Value Line does provide betas, and when a
10 firm has zero debt, those betas are at that point
11 unlevered, but in cases that do have debt you have to
12 modify them.

13 EXAMINER SEE: I'm sorry, what was the
14 last?

15 THE WITNESS: You have to modify them.

16 Q. And did you do that?

17 A. Yes, I did.

18 Q. All right. And at arriving at your
19 unlevered betas did you use your betas from the Value

20 Line investment survey?

21 A. Yes, I did.

22 Q. Using the unlevered betas book ratio, how

23 did you develop the comparable group of companies?

24 A. So what I do is I divide the available

25 firms into decile form.

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1 Q. I'm sorry, by what?

2 A. Deciles, which are groups of 10
3 percentile, and in that fashion I divide all firms by
4 the unlevered beta and I also do the same thing on
5 the leverage and in this fashion I obtain 100
6 different cells. I choose the cell in which the
7 particular firm I am interested in resides and
8 subsequently all the firms in that cell become its
9 comparable business risk and financial risk firms.

10 Q. And your comparable companies are then
11 listed on Exhibit IX of your testimony, page 65?

12 A. Yes.

13 Q. And there are 25 companies; is that
14 correct?

15 A. That's correct.

16 Q. Are all of these U.S. companies, or are
17 there foreign companies included?

18 A. On --

19 Q. For 2007.

20 A. In Panel A I believe the companies that

21 emerged were all U.S. companies.

22 Q. I'm sorry?

23 A. They were U.S. companies that happened to

24 emerge in the sample in 2005 -- sorry, 2007.

25 Q. Are you saying in 2007 there were foreign

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1 companies that emerged in the sample or U.S.

2 companies?

3 A. Just U.S. companies emerged in the sample

4 in 2007.

5 Q. There is not a Canadian company listed

6 there?

7 A. Oh, yes, there is Fording Canadian Coal.

8 Q. And for 2005 and 2006 did you use U.S.

9 companies, or do your samples use foreign companies?

10 A. Okay. I think I would like to explain

11 the procedure and how the firms emerge. Firms that

12 meet U.S. standards for listing which are level 2 and

13 level 3 of listing and, therefore, develop comparable

14 financial reporting are permissible within the

15 methodology to emerge, but I am certainly open to the

16 alternative methodology where such firms are not

17 included as it is because they were providing SEE

18 level of reporting, therefore, they become part of

19 the database and do appear here.

20 Q. And Dr. Woolridge didn't use foreign

21 companies in his analysis, did he?

22 A. That's true.

23 Q. All right.

24 MS. ROBERTS: If the Bench will permit me

25 to approach the witness.

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1 Q. Dr. Makhija, I want to give you the
2 attachments, the exhibits, to OCC Exhibit 2 which are
3 the exhibits attached to Dr. Woolridge's testimony.

4 EXAMINER SEE: You can approach.

5 MS. ROBERTS: It's already in so I am not
6 going to mark it.

7 Q. If you turn to JRW-6, Dr. Makhija,
8 please. Do you have that, Dr. Makhija?

9 A. Yes, I do.

10 Q. And is this Dr. Woolridge's review of
11 your financial results for 2007 for your comparable
12 group?

13 A. It appears to be, yes.

14 Q. All right. And are these levered betas?

15 A. Yes.

16 Q. Did you previously testify that levered
17 betas reflect both business and financial risk?

18 A. And indeed that is the problem with them
19 that they mix both risks simultaneously.

- 20 Q. If you look at the bottom of column --
- 21 column 6, Dr. Makhija, do you see that Dr. Woolridge
- 22 has provided the mean, high, and low betas?
- 23 A. You mean column 5?
- 24 Q. Five, I'm sorry.
- 25 A. Yes, he does.

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1 Q. And would you agree that the range of the
2 betas from low to high is about 0.75 to 2.1?

3 A. Yeah. And these, of course, are not
4 unlevered betas which I have used.

5 Q. And that range difference is about 1.35?

6 A. Yes.

7 Q. And even with that range in betas
8 employed by Dr. Woolridge, do you believe that these
9 are comparable firms?

10 A. It certainly as -- just one moment, I
11 will find the exhibit. If you look at my Exhibit X
12 where I provide the unlevered betas for the same
13 group, so this is Exhibit X, part B -- no, part A.

14 Q. Would you just give me a second,
15 Dr. Makhija. I am not as quick at this as you are.

16 A. Page 70.

17 Q. Part C?

18 A. No. Page 70, Panel A, that's Exhibit X
19 -- I'm sorry, Part A.

20 Q. Thank you. I have that. Yes.

21 A. So if you see there towards the bottom of

22 that panel, it says: "Comparable risk peer group

23 rank for unlevered beta" the corresponding values run

24 from .85 to .94 roughly, and at that point the beta

25 on -- levered beta for AEP is about .89, so you see

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1 the matching unlevered betas does not have to
2 correspond to the matching on the levered beta so we
3 are comparing two different things now.

4 Q. Do you know what percent of companies
5 covered by Value Line have betas between the range of
6 0.75 and 2.1?

7 A. I would have to go check that.

8 Q. Do you think it would -- would you have
9 an idea of an order of magnitude the companies have
10 reported?

11 A. I imagine it would be a pretty
12 substantial percentage.

13 Q. Be a substantial percentage. And would
14 it -- would it surprise you if that -- by
15 "substantial percentage," could that be as high as 60
16 or 70 percent?

17 A. It's possible.

18 Q. Okay. Also in Exhibit OCC Exhibit 2,
19 Dr. Woolridge's Exhibit JRW-6, he also shows the 2007

20 ROEs provided for your 2007 comparable companies as

21 provided by Value Line; is that correct?

22 A. That's what he says, yes.

23 Q. Yes. Let's focus on column 7. There is

24 a range at the bottom of column 7, isn't there,

25 Dr. Makhija, of a negative 46.15 percent to 98.02

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1 percent?

2 A. Yes, there is.

3 Q. How could these companies be comparable

4 in terms of risk when their returns range from a

5 negative almost 50 percent to a positive almost

6 100 percent?

7 A. Yes. A couple of things. First of all,

8 the ROEs that we are looking at here include

9 nonrecurring items that produce certain amount of

10 variation.

11 Q. What items, Dr. Makhija?

12 A. Producing variation in returns when you

13 have nonrecurring items.

14 Q. Oh, nonrecurring items, thank you.

15 A. But that's not full story. Recall that

16 at the end of the day arguably this is what the

17 shareholders got in the reported earnings in that

18 year, but these firms were matched, as I point out in

19 Exhibit X, Part A, very well. In fact, on both the

20 criteria which SB 221 requires us to look at.

21 So whether we look at the unlevered beta

22 where I give you the range and how tightly that range

23 fits around the subject utility, and at the same time

24 the book equity ratio, the range is also provided in

25 Exhibit X, Part A, and that also fits very closely

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1 with the subject utility. So if you want to compare
2 it with a mix of those factors, which is what the
3 beta is, we would get a wider range and also you
4 would get a wide range in the ROEs simply because
5 some firms on account of the nonrecurring items would
6 have variation.

7 Q. Doesn't Value Line adjust for
8 extraordinary items?

9 A. Well, that's an alternative definition of
10 ROE against -- I am not particularly against that
11 definition, but the different definitions do have
12 different merits and alternatives are certainly
13 entertained.

14 Q. But your data doesn't make any
15 adjustments --

16 A. Not in this.

17 Q. -- for these extraordinary items.

18 A. No.

19 Q. I would like to turn to your ROE

20 threshold calculation.

21 A. What page?

22 Q. Well, I didn't write it down. Do you

23 know where that is, Dr. Makhija? If you find it

24 first, will you let me know, all right?

25 A. It's available in Exhibit X, if that's

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1 what you are looking for.

2 Q. It may be pages 70 and 71. That's

3 Exhibit X, Part A?

4 A. Yes.

5 Q. Pages 70 and 71?

6 A. Yes.

7 Q. All right. Using your results for 2007,
8 can you explain your ROE threshold calculation?

9 A. So this is provided in Panel B and --

10 Q. Panel B is on which page?

11 A. Page 70.

12 Q. Thank you.

13 A. Let me describe what the methodology is
14 and then we can look at the outcome.

15 Q. All right.

16 A. The methodology is to take the 25 firms
17 that have been determined as the comparable group,
18 find their mean and their standard deviations, and
19 those are the statistics that are then employed to

20 determine the threshold. Would you ask me

21 specifically any issues with that?

22 Q. No. But I am interested, Dr. Makhija,

23 that it doesn't appear that you have used data

24 regarding CSP and Ohio Power in arriving at your ROE

25 threshold calculation.

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1 A. Yes.

2 Q. So you did not make a capital structure
3 adjustment for CSP and OPC?

4 A. That's not quite correct. Remember what
5 I have done is having determined what the appropriate
6 business risk is and what the financial risk is,
7 that's how I define the comparable firms. But in
8 forming the business risk, I developed the unlevered
9 beta. And if you look at the methodology for
10 developing the unlevered data, it specifically
11 accounts for capital structure so, for example, the
12 formula says that the beta unlevered is the beta
13 levered divided by 1 plus -- 1 minus the tax times
14 debt to equity so the correction is taking place and
15 we know that that correction is working because if it
16 had been an all equity firm, then the D by E would
17 have been zero and the levered and unlevered betas
18 would have been the same, so quite clearly we have
19 taken the capital structure into account before we

20 did the matching and consequently we only determined
21 those firms with capital structure adjustments taking
22 into account from the comparable firm.

23 Q. But at no point did you use the capital
24 structure of Ohio Power and Columbus Southern Power,
25 did you?

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1 A. Well, this takes us back to the earlier
2 discussion of where, for example, I have cited people
3 that believe that the financial risk of -- of Ohio
4 Power and Columbus Southern Power are comparable to
5 those of AEP and I have taken AEP capital structure
6 into account in the unlevered activity so it's been
7 taken into account as a result.

8 Q. And for that reason it's your testimony
9 that your proposed methodology for calculating SEE
10 complies with the recommendations of Senate Bill 221?

11 A. Yes, because it requires capital
12 structure be taken into account and what I have done
13 is taken into account in setting the matching
14 parameters. Some other individuals could take
15 another approach which is to find the return and then
16 delevered that. There would be other questions
17 related to the nature of that test which don't apply
18 here.

19 Q. It's your testimony in considering the

20 recommendation in the matching parameters -- I'm
21 sorry, in considering the capitalization in the
22 matching parameters, you don't need to specifically
23 adjust for the capitalization of Ohio Power and
24 Columbus Southern Power?
25 A. I'm sorry, I said that I have

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1 accommodated that because AEP is reflective of the
2 financial risks of these firms and subsequently I
3 have used the capital structure information in the
4 unlevering of the beta and also in forming the groups
5 that form the -- you know, the decels for leverage as
6 well.

7 Q. And so you are confident that in this
8 calculation that you are proposing to the Commission
9 that you have measured excessive earnings on the
10 return on common equity of the electric distribution
11 company which is individually Columbus Southern Power
12 and Ohio Power?

13 A. Indeed.

14 Q. By using AEP.

15 A. Yes.

16 Q. Almost done. You discuss on page 37,
17 line 21 of your testimony about the companies' higher
18 capital expense and that you believe that affects
19 their risk.

20 A. You mean on the capital expenditures on

21 page 37?

22 Q. Yes.

23 A. It's not an element of risk but rather

24 SB 221 specifically says that capital expenditures

25 may be used as a mitigating factor in terms of

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1 applying the test.

2 Q. Would it be an inappropriate
3 consideration in your opinion to know whether the
4 capital expenditures were -- were recovered from
5 customers or not in making this evaluation?

6 MR. RANDAZZO: I object. Your Honor, we
7 have had an extended amount of cross-examination.
8 Based on the witness's answers to my questions, it's
9 my understanding this witness's position is that he
10 hasn't looked at AEP's ESP to evaluate changes in
11 business and business that may bring and that in any
12 event he would agree we would need to relook at the
13 methodology at the point of time when it was being
14 applied. We are now at the point of diminishing
15 returns in terms of the value of any further
16 cross-examination of this witness, and in the
17 interest of trying to move the proceeding along, I
18 object.

19 EXAMINER SEE: Would you like to respond,

20 Ms. Roberts?

21 MS. ROBERTS: Yes, yes. I would -- he
22 discusses this in his testimony and I believe I am
23 entitled to cross-examine him on it and I apologize
24 if Mr. Randazzo thinks my returns on cross are
25 diminishing. It's his opinion.

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1 MR. RANDAZZO: If I may briefly.

2 EXAMINER SEE: Briefly.

3 MR. RANDAZZO: I tried to show you my
4 reasoning based upon the answers that the witness
5 gave. To the extent the response from counsel
6 suggests that you need to rely exclusively on my
7 opinion, you heard the answers yourself here today.
8 I think we have got diminishing returns, and in the
9 interest of moving along, I would ask that we move
10 along.

11 EXAMINER SEE: I would agree that we need
12 to move along, but I'm going to trust that
13 Ms. Roberts is asking the questions that she needs to
14 and is taking into account the fact that we have 36
15 more witnesses to go to complete this hearing.

16 MS. ROBERTS: Actually, I only had that
17 one question, and if we had gotten an answer, we
18 would be moving on.

19 EXAMINER SEE: Okay. If we could end the

20 commentary from all counsel around the table, purely
21 respond to the basis of your objection, and end the
22 excess comments, we could move things along.

23 So with that, could you please read

24 Ms. Roberts' question back.

25 (Record read.)

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1 A. My reading of SB 221 does not refer to
2 the source of the recovery, simply to the level of
3 capital expenditures and to -- and I am only
4 addressing that aspect.

5 Q. Are you using a 95 percent confidence
6 level in your analysis, Dr. Makhija?

7 A. Yes.

8 Q. Would you agree as compared to an 85
9 percent confidence level, using a 95 percent
10 confidence level lowers the likelihood of the company
11 earning SEE?

12 A. Yes.

13 MR. CONWAY: Objection.

14 Q. You also express concern about on page 15
15 the asymmetrical risk of the SEC test? I meant to
16 say "SEE." I may have said "SEC."

17 EXAMINER SEE: What page was that again?

18 MS. ROBERTS: 15.

19 A. Did you say page 15?

20 Q. Yes, I did. Oh, I'm sorry, did you
21 address asymmetrical risk in your testimony?

22 A. I did mention it.

23 Q. But not on page 15.

24 A. No.

25 Q. I apologize, Dr. Makhija, that wasn't a

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1 test. And would it affect your concern about
2 asymmetrical risk if you knew that the company that
3 you were evaluating recovered more of its costs
4 through reconciled and trued-up rates than through
5 traditional cost of service base regulation rates?

6 MR. CONWAY: Could I have the question
7 reread.

8 EXAMINER SEE: Yes.

9 (Record read.)

10 MR. CONWAY: I don't understand the
11 question so I guess the objection is I don't
12 understand it. I am not quite sure what the
13 comparison is between what and when you use as the
14 basis for saying some assist -- asymmetry is I guess
15 what you are asking is mitigated, but I didn't
16 understand what the comparison was between regulated
17 rates and then trued-up rates.

18 EXAMINER SEE: I'm sorry, Mr. Conway, I
19 need you to speak up and -- first, I need to know

20 does the witness understand the question?

21 THE WITNESS: I am not quite sure what

22 exactly is being asked.

23 EXAMINER SEE: Ms. Roberts, you need to

24 rephrase your question.

25 MS. ROBERTS: I will.

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1 Q. (By Ms. Roberts) Dr. Makhija, your
2 concern is that in applying the significantly excess
3 earnings test a company that overearns in one period
4 would have to return those earnings while in another
5 period, if they underearned, they wouldn't be able to
6 recover the earnings and you have called that an
7 asymmetrical risk; is that correct?

8 A. Yes. And I think when you moved on to
9 bringing in those other aspects, you moved on to
10 those issues of adjustments and so forth and, as I
11 said earlier, I am not taking a position on those and
12 so this becomes a very hypothetical question for me
13 to answer because I don't know what exactly would
14 occur in the trueup, et cetera.

15 Q. No, I understand, and I don't mean to ask
16 you any specific issues about rate -- about
17 ratemaking. What I want to ask is just a very
18 general question to the extent that a company is not
19 risk -- not at risk for underearning, would that

20 change the asymmetry of the risk that you identify?

21 A. Well, the test is applied only in one

22 direction so there could be earnings that fall below

23 at the same parallel threshold on the low side that

24 would still be left unaddressed.

25 Q. But isn't that an assumption you are

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1 making that the risk would -- that the risk of not
2 earning would be the -- would be the same risk as
3 overearning?

4 A. But nowhere does -- in SB 221 does it
5 even address when you fall on the low side so how can
6 I assume beyond what the SB 221 says that something
7 will be done on that when it's silent on that?

8 Q. Did you read Mr. Cahaan's testimony filed
9 in this proceeding, Staff Witness Cahaan?

10 A. Yes.

11 Q. Yes. And is it his proposal that if the
12 company overearns its return, it returns the entire
13 return or just the part of the return over the
14 threshold constituting significantly excess earnings?

15 A. Well, I will allow him to stand for his
16 testimony, but I am not sure how -- how this is
17 addressing the question you had asked.

18 Q. Does that change the symmetry of the risk
19 if the company is allowed to overearn their return?

20 A. I am sure he would say no because the

21 testimony speaks to one direction.

22 Q. I am asking you what you say, your

23 opinion.

24 A. The test only applies in one direction

25 and --

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1 Q. And in your opinion there are no
2 mitigating factors to that symmetry?

3 A. That would be --

4 EXAMINER SEE: I'm sorry, it is very
5 helpful if the two of you do not speak at the same
6 time. If you allow her to complete her question and
7 if you will allow him to finish his answer.

8 MS. ROBERTS: I'm sorry, your Honor.

9 Q. From 2007, you used a sample size of 25
10 companies. Would that be considered by statisticians
11 to be a small sample for this kind of test?

12 A. I don't think so. I think it's an
13 adequate sample but, remember, this was for
14 illustrative purposes to develop a methodology.

15 Q. I just have two other questions. I asked
16 you earlier about your presentations before AEP, and
17 you indicated you made cost of capital estimates for
18 AEP.

19 A. Yes.

20 Q. And for what period or proceeding was

21 that?

22 A. This was for educational purposes and

23 purely illustrative to show how cost of capital

24 calculations are made, et cetera, and I have done

25 them pretty much every year, usually in fall when

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1 such a program occurs at the Fisher College.

2 Q. And you do refer in your testimony --

3 this is my last question, I want to get it right --

4 to regression analysis, page 18, line 21. Can you

5 tell me what the sum of the remainders in a

6 regression analysis is?

7 A. Why are we -- I'm sorry. I'm sorry,

8 what's the question again?

9 Q. Can you tell me what the sum of the

10 remainders in a regression analysis is?

11 A. Could you explain that further to me?

12 Q. No. Are there remainders in a regression

13 analysis?

14 A. The undertones are, yes.

15 Q. And the sum of the remainders, do you

16 know what the sum of the remainders in a regression

17 analysis would be?

18 A. In the kind of regression that I am

19 presenting what we do is the least squares analysis,

20 so I am not quite sure your question is going with
21 the regression that is here. Here, we are looking
22 for the sum of square residuals, so could you explain
23 your question then?
24 Q. No. I just wanted to know if you could
25 respond to that.

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1 MS. ROBERTS: I have no other questions,
2 your Honor.

3 EXAMINER SEE: Thank you.

4 Ms. Elder.

5 MS. ELDER: No questions, your Honor.

6 EXAMINER SEE: Mr. O'Brien.

7 MR. O'BRIEN: No questions, your Honor.

8 EXAMINER SEE: Mr. Smalz.

9 MR. SMALZ: Just a very few.

10 EXAMINER SEE: I need you to put the mic
11 on, Mr. Smalz.

12 - - -

13 CROSS-EXAMINATION

14 By Mr. Smalz:

15 Q. Dr. Makhija, first, in response to a
16 question from Mr. Kurtz, I think you testified that
17 you did not deal with the revenue impact of the
18 proposed methodology in your testimony; is that
19 correct?

20 A. Yes.

21 Q. Do you mean to suggest that the revenue
22 impact is totally irrelevant?

23 A. No. It's just that I did not deal with
24 that aspect.

25 Q. I see. Thank you. In response to a

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1 question towards the end of OCC's cross-examination,
2 I think you testified your proposed methodology is
3 illustrative, and you explained that in response to a
4 question about the relatively small sample size; is
5 that correct?

6 A. Well, it's illustrative for one thing
7 that the statute -- the Senate Bill 221 doesn't even
8 come into application until 2010, so any exercise
9 done at this point is simply to illustrate the
10 procedures.

11 Q. But are you recommending that your
12 methodology in every detail be adopted by the
13 Commission as the methodology for applying the
14 significant excessive earnings test?

15 A. I certainly laid out the principles of
16 such a methodology.

17 Q. So you are recommending adoption of the
18 principles, but not necessarily every detail?

19 A. Well, we don't know what samples would be

20 available, et cetera, so we -- we need to have the

21 actual situation in 2010 to proceed here.

22 Q. Okay. Turning to page 20 of your

23 testimony, the third full paragraph beginning at line

24 12, second sentence which reads, "For example, there

25 is migration risk since customers have

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1 come-and-go-rights, while the electric utility
2 retains provider of last resort status at tariff
3 rates." My question is have you done any studies or
4 analyses of that migration risk to measure that
5 migration risk?

6 A. No, I have not.

7 Q. And are you aware of any such studies or
8 analyses?

9 A. I am aware of the nature of this risk and
10 that's all I am referring to.

11 Q. Thank you.

12 In applying the significantly excessive
13 earnings test to the Ohio AEP companies, in your
14 opinion, Dr. Makhija, should all the companies'
15 earnings including off-system sales be included in
16 the application of that test?

17 A. I have not taken any position with regard
18 to that. I am aware of arguments that have been made
19 on it, but it has not impacted my analysis at all.

20 MR. SMALZ: Thank you. I have no more

21 questions, your Honor.

22 - - -

23 EXAMINATION

24 By Examiner Bojko:

25 Q. Dr. Makhija, a couple of questions before

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1 staff proceeds. In response to Ms. Roberts you
2 stated that others have done the analysis to
3 determine that the AEP-Ohio companies have a similar
4 corporate structure to the AEP parent company, who
5 did that analysis? Or did you not say "others"? Did
6 you mean yourself? Who did that analysis?

7 A. I'm sorry, first of all, the assertion,
8 could you repeat that.

9 Q. The corporate structure of the Ohio
10 subsidiaries is comparable or similar to the parent
11 company.

12 A. What I said is that in imputing the
13 financial risk of the -- for Ohio Power and for
14 Columbus Southern Power it is appropriate to take the
15 financial risk of AEP, and the reasoning for that
16 being that the market turns to AEP to impute the
17 financial risk of the -- with these two companies.

18 Q. Because that's what the market does.

19 A. That's what the market does.

20 Q. So when you said "others," you were
21 probably referring to the street, which I think you
22 have used that term today, or the market.

23 A. Yes.

24 Q. Okay. And then in response to Ms. Wung
25 you stated you are generally aware that the other

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1 Ohio utilities have differences. Where did that
2 knowledge come from? Was that your analysis or is
3 this from the street as well, or from a company?

4 A. Recalling that I have not done any
5 specific analysis, but as you read through these
6 company comparisons, et cetera, sometimes you run
7 into how the beta risks itself for firms across Ohio
8 are not necessarily the same, and that's for sure
9 that they don't all have the same beta, for example,
10 which is a measure of risk, so that leads me to
11 wonder why they would necessarily match out as
12 comparable business and financial risk.

13 Q. So any readings that you would have done
14 or reviews or betas that you would have come across
15 would have been based on the current status of those
16 Ohio utilities, not the future under any ESPs or in
17 2010?

18 A. Well, just with one caveat, that when
19 people do betas, it is true they use historical data

20 to estimate them, but they do make adjustments in
21 terms of future risk as well. So to that extent
22 that's been reflected, but remember, most of the
23 analysis here goes up to only 2007 so what will be
24 the future risk as the ESP gets decided remains to be
25 seen.

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1 Q. Okay. And that would be true -- just as
2 you answered Mr. Randazzo, that would be true of the
3 other Ohio utilities as well.

4 A. Yes.

5 EXAMINER BOJKO: Okay. Thank you.

6 Mr. Margard.

7 MR. MARGARD: Thank you, your Honor.

8 Just a couple of questions, if I can, please.

9 - - -

10 CROSS-EXAMINATION

11 By Mr. Margard:

12 Q. Good morning, Dr. Makhija.

13 A. Hi.

14 Q. You have recommended use of a comparable
15 risk peer group methodology as part of your
16 testimony; is that correct?

17 A. Yes.

18 Q. And you have presented to the Commission
19 for illustrative purposes comparable risk peer groups

20 for years 2005, 2006, and 2007.

21 A. Yes.

22 Q. And those are contained in your Exhibit

23 No. IX.

24 A. Yes.

25 Q. And just to be clear, they are purely

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1 intended to illustrate the application of your
2 methodology and you are not recommending the adoption
3 of any of these peer groups as a test, as part of the
4 SEE test, are you?

5 A. In fact, I would go one step further and
6 point out that the comparables do change as the
7 business and financial risks of firms emerge and
8 subsequently the sample is likely to change.

9 Q. You would expect the sample to change
10 then from year to year.

11 A. Yes.

12 Q. And it does not surprise you then that
13 the sample groups for these three years are, in fact,
14 very different.

15 A. Yes.

16 Q. That's what you would expect as part of
17 your test. Let me ask you to turn to page 40, if you
18 would, please, of your testimony. Let me direct your
19 attention to line 19, if you will indicate when you

20 have the reference. Are you there? The sentence
21 there indicates "To be earning significantly
22 excessive earnings would require ROE values higher
23 than the upper bound, an ROE greater than 27.33
24 percent." Now, this specific reference is with
25 respect to your application of your methodology for

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1 the calendar year for 2007; is that correct?

2 A. Correct.

3 Q. And in this paragraph you discuss AEP's
4 ROE relative to the peer group and you specifically
5 reference the mean and the median of the comparable
6 risk peer group. And am I correct in understanding
7 that the mean is identified in your Exhibit X?

8 A. Yes.

9 Q. And specifically in Panel B?

10 A. Yeah. Also in Panel A.

11 Q. Also in Panel A. In fact, in Panel A is
12 where we find the median.

13 A. Yes.

14 Q. And the 27 percent figure that you
15 indicated is the upper bound indicated as the 95th
16 percent confidence interval in the three comparisons
17 in Panel B.

18 A. Yes.

19 Q. And that that 27 percent, roughly, is not

20 quite twice the mean.

21 A. As it happens to be.

22 Q. As it happens in this particular

23 application.

24 A. Yes.

25 MR. MARGARD: That's all I have. Thank

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1 you, your Honor.

2 EXAMINER SEE: Mr. Conway.

3 MR. CONWAY: Your Honor, I have just a

4 few questions on redirect. Is that what you were

5 giving me the opportunity to do?

6 EXAMINER SEE: Yes.

7 - - -

8 REDIRECT EXAMINATION

9 By Mr. Conway:

10 Q. Dr. Makhija, there has been some
11 discussion about the difference between recommending
12 a methodology in this case and the application of the
13 methodology for illustrative purposes in this case
14 and the use of the methodology in a future period
15 such as 2010. Do you recall those discussions?

16 A. Yes, I do.

17 Q. Is it your recommendation that the
18 Commission should adopt your methodology that you
19 propose in this case for use in the future periods?

20 MR. RANDAZZO: I object. The question is
21 decidedly leading and this is a critical -- critical
22 point, and I don't think it's fair to have the
23 counsel leading the witness.

24 EXAMINER SEE: Your objection is
25 overruled.

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1 A. Yes. I do recommend this methodology to
2 be adopted, yeah.

3 Q. You are not -- you are not recommending
4 that the illustrative aspect of your application be
5 transferred to a future period.

6 A. That's right.

7 Q. Do you recall some questions from
8 Ms. Wung about the FirstEnergy and Duke companies and
9 the extent to which they entered into the mix for
10 your analysis?

11 A. Yes.

12 Q. FirstEnergy is a publicly-traded company,
13 correct?

14 A. Yes.

15 Q. And is Duke Energy a publicly-traded
16 company?

17 A. Yes.

18 Q. And so would Duke Energy and FirstEnergy
19 have been in the pool of companies from which you

20 ultimately drew your comparable risk firms in your
21 illustrative example?
22 A. They were very much available as
23 potential matches, and the fact that they did not
24 show up necessarily shows whether or not they were
25 perfect matches against the subject utility.

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1 Q. Dr. Makhija, you are an expert in matters

2 of finance, correct?

3 A. Yes.

4 Q. And that's reflected in your credentials,

5 I believe, and in your experience.

6 MR. BELL: Objection. That's in his

7 direct testimony. This is asked and answered three

8 or four times and he is an expert witness and counsel

9 is telling him he is an expert witness.

10 MR. CONWAY: I would be happy to take

11 that.

12 EXAMINER SEE: Okay, okay, gentlemen.

13 Next question, Mr. Conway.

14 Q. Dr. Makhija, you are testifying on behalf

15 of the companies based on your expertise in financial

16 matters, correct?

17 A. Yes.

18 Q. You are not an expert in financial

19 matters because of the number of times you have

20 testified in the past, are you?

21 A. No, but you can see my testimony I have
22 written some ten-plus papers on electric utilities
23 and their financials.

24 MR. CONWAY: Thank you. That's all I
25 have, your Honor.

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1 EXAMINER SEE: Recross?

2 MR. YURICK: Nothing, thank you, your
3 Honor.

4 EXAMINER SEE: Mr. Bell.

5 MR. BELL: So tempted, but no questions.

6 EXAMINER SEE: Mr. Kurtz.

7 MR. KURTZ: No, your Honors.

8 EXAMINER SEE: Ms. Wung.

9 MS. WUNG: No questions, your Honor.

10 EXAMINER SEE: Ms. Roberts.

11 MS. ROBERTS: No, your Honor.

12 EXAMINER SEE: Mr. Randazzo.

13 MR. RANDAZZO: No, your Honor.

14 EXAMINER SEE: Ms. Elder.

15 MS. ELDER: No, your Honor.

16 EXAMINER SEE: Mr. O'Brien.

17 MR. O'BRIEN: No, your Honors.

18 EXAMINER SEE: Mr. Smalz.

19 MR. SMALZ: No, your Honor.

20 EXAMINER SEE: Mr. Margard.

21 MR. MARGARD: No, your Honor. Thank you.

22 EXAMINER SEE: Let's take a -- I'm sorry,

23 go ahead, Mr. Conway.

24 MR. CONWAY: At this time, your Honor, I

25 would move for the admission of Companies' Exhibit

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1 No. 5, Dr. Makhija's direct testimony into the
2 record.

3 EXAMINER SEE: Are there any objections
4 to Companies' Exhibit 5?

5 Hearing none, Companies' Exhibit 5 will
6 be admitted into the record.

7 (EXHIBIT ADMITTED INTO EVIDENCE.)

8 EXAMINER SEE: Let's go off the record
9 for a second.

10 (Discussion off the record.)

11 EXAMINER SEE: Let's go back on the
12 record. Rather than continue to wait for Ms. Bojko
13 to complete the conference call, let's take a lunch
14 break and reconvene at 1 o'clock.

15 (At 11:40 a.m., a lunch recess was taken
16 until 1:00 p.m.)

17 - - -

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3 - - -

4 EXAMINER SEE: Let's go back on the
5 record.

6 Mr. Resnik, the next witness.

7 MR. RESNIK: Thanks, your Honor. The
8 companies call Mr. Assante as the next witness.

9 (Witness sworn.)

10 MR. RESNIK: Your Honor, can I have
11 marked as Companies' Exhibit No. 6 the direct
12 testimony of Leonard V. Assante.

13 EXAMINER SEE: It is so marked.

14 (EXHIBIT MARKED FOR IDENTIFICATION.)

15 MR. RESNIK: Thank you.

16 - - -

17 LEONARD V. ASSANTE

18 being first duly sworn, as prescribed by law, was
19 examined and testified as follows:

20 - - -

21 DIRECT EXAMINATION

22 By Mr. Resnik:

23 Q. Would you please state your name for the
24 record.

25 A. Leonard V. Assante.

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1 Q. Mr. Assante, do you have before you a
2 copy of what's just been identified as Companies'
3 Exhibit 6?

4 A. Yes, I do.

5 Q. Can you identify that exhibit for the
6 record, please.

7 A. Yes, that is my prefiled direct
8 testimony.

9 Q. And are there any corrections that need
10 to be made to your -- to Companies' Exhibit 6?

11 A. Yes, I have one correction. On page 25,
12 line 8 where it says "RSP" that should be "ETP." And
13 on line 12 where it says "RSP" that should also be
14 "ETP."

15 EXAMINER SEE: I'm sorry, what was that
16 second line?

17 THE WITNESS: Line 12, RSP should be ETP.

18 Q. You said line 12 and 8?

19 A. Line 8 and line 12, yes.

20 Q. Both places, okay. And I'm sorry,
21 Mr. Assante, I may have missed it, was there another
22 change in line 8 other than just changing RSP to ETP?

23 A. The word "already," I'm sorry, the word
24 "already" should also be strike -- taken out.

25 Q. Thank you. Mr. Assante, with those

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1 corrections if I were to ask you the questions that
2 appear in Companies' Exhibit No. 6, would your
3 answers be the same as they are?

4 A. Yes, they would.

5 MR. RESNIK: Your Honor, I have no other
6 questions of Mr. Assante, and he is available for
7 cross-examination.

8 EXAMINER SEE: Who wants to go first?

9 MS. GRADY: I would be happy to go first.
10 Like in speech class, you didn't want to sit through
11 everybody else's speech and worry.

12 - - -

13 CROSS-EXAMINATION

14 By Ms. Grady:

15 Q. Good afternoon, Mr. Assante.

16 A. Good afternoon.

17 Q. Mr. Assante, if you could turn to page 4
18 of your testimony.

19 A. Okay. I am on page 4 by chance.

20 Q. Yes. On lines 21 through 22 you indicate
21 you were requesting to make the ESP revenue
22 requirement more affordable to ratepayers by phasing
23 in the incremental FAC. When I say FAC, I mean full
24 adjustment clause expenses during the three-year ESP
25 period. Do you see that reference?

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1 A. Yes, I do.

2 Q. And there you are speaking of the
3 proposal to limit the increases to 15 percent per
4 year for the first three years; is that correct?

5 A. Yes, I am.

6 Q. Now, in making the -- the proposal more
7 affordable during the first three years of the ESP
8 period, your proposal also, does it not, push costs
9 incurred during the three-year period into the future
10 years for future recovery?

11 A. Yes. It's a phase-in plan. The
12 methodology is to defer costs, FAC costs for future
13 recovery.

14 Q. And the costs that are pushed into future
15 years for recovery will be accrued carrying charges,
16 isn't that correct, at the weighted average cost of
17 capital?

18 A. That's correct.

19 Q. Now, turning to page 5 of your testimony,

20 I want to direct your attention to line 17 through
21 20. And you indicate there that the companies are
22 proposing to defer any unrecovered incremental FAC
23 costs that are incurred in the 2009 through 2011
24 period plus a carrying charge and that you want to
25 collect that over 10 years. Do you see that

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1 reference?

2 A. Yes, I do.

3 Q. And the company has estimated, has it
4 not, the amount of unrecovered incremental FAC costs
5 that it expects to incur in 2009 as a result of the
6 phase-in?

7 A. That's correct. Company Witness Roush
8 provided me with that estimate.

9 Q. And for CSP you have estimated -- or
10 Mr. Roush has estimated, has he not, that CSP will
11 be -- is to defer \$112 million and Ohio Power will
12 need to defer 300 million of 2009 FAC costs?

13 A. That's correct. That's his estimate.

14 Q. And those costs are the costs that are
15 inclusive of carrying charges; is that correct?

16 A. No. Those are just FAC costs. They do
17 not include the carrying charge.

18 Q. When we look at your Exhibit LVA-1, is
19 that a depiction of those costs?

20 A. LVA-1 is an illustrative example. The
21 reason it's an illustrative example I was not
22 provided with fuel -- or FAC statements for 2010 and
23 11 and I assumed that the amount would be the same,
24 the FAC costs would be the same; in other words,
25 there would be no increment in those years over 2009.

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1 It also includes an assumption that there is no
2 trueup adjustment so it's an illustrative example of
3 what this phase-in would appear if, in fact, those
4 assumptions were correct.

5 Q. Yes. But for the 2009 period it actually
6 is the assumption of the company; is it not?

7 A. For 2009, yes, it should be fairly
8 accurate since it is an estimate I was provided.

9 Q. Now, we look at LVA-1 for Columbus
10 Southern Power Company, their deferrals only in 2009,
11 and that would show the \$112 million worth of
12 deferrals with \$6.2 million of carrying charges?

13 A. That's correct.

14 Q. And you indicated before that the
15 carrying charges would be at the weighted average
16 cost of capital before taxes; is that correct?

17 A. That is correct.

18 Q. And if we wanted to find the weighted
19 average cost of capital, that would be in

20 Mr. Nelson's testimony; is that correct?

21 A. Yes. Mr. Nelson has an exhibit. I think

22 it's PJN-11.

23 Q. Yes.

24 A. In which he has an after tax weighted

25 average cost of capital. I have used the before tax

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1 weighted average cost of capital and I computed that
2 by just dividing the gross up factor 62.5 percent
3 into the equity and coming up with the before tax
4 11.15 percent.

5 Q. And if we looked at the 2009 deferred
6 carrying charge, would that be the result of half a
7 year's worth of carrying charges on the deferred --
8 deferred FAC expense; if you know?

9 A. That's correct. We did a half year
10 conversion.

11 Q. Now, Mr. Assante, on line -- well, it is
12 an unlined schedule on the line that's entitled
13 Regulatory Asset Balance, that merely reflects, does
14 it not, the deferred FAC plus the carrying charges?

15 A. That's correct. It shows the cumulative
16 deferral.

17 Q. Now, using your exhibit and I understand
18 that you did -- you made certain assumptions and
19 those assumptions as you stated in your testimony at

20 the footnote and as you orally indicated, that
21 subject to the assumptions, this schedule would show
22 that for CSP there are \$99.4 million worth of
23 carrying costs on the 2009 deferral; is that correct?
24 A. Yes. Throughout the entire phase-in
25 period, which is 10 years, the carrying cost would

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1 amount to \$99 million, that's correct.

2 Q. And the way your proposal works, does it
3 not, Mr. Assante, the carrying charges accrue on the
4 regulatory asset balance and then actually you get
5 carrying charges on carrying charges, correct?

6 A. Yes. The carrying charge, like all
7 interest, is compounded.

8 Q. Mr. Assante, do you know if the company
9 has estimated the amount of unrecovered FAC expense
10 that it expects to incur for 2010 and 2011 as a
11 result of the phase-in proposal?

12 A. Well, I presume the company has because
13 it had to provide supplemental pro forma information
14 which would have been -- which was an income
15 statement, so in order to do the income statement and
16 the balance sheet, they would have had to estimate
17 the unrecovered amount.

18 Q. Now, Mr. Assante, if I presented you with
19 a copy of the -- the pro forma income statement,

20 would you be able to show me where on that income
21 statement I would be able to decipher the unrecovered
22 incremental FAC that the company expects to incur
23 from 2000 -- in 2010 and 2011 under its proposal?

24 A. I may be able to.

25 MS. GRADY: Your Honor, may I approach

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1 the witness?

2 EXAMINER SEE: Yes.

3 MS. GRADY: Your Honor, if the record
4 would reflect I have handed Mr. Assante OCC Exhibit
5 No. 4.

6 EXAMINER BOJKO: How about -- oh, Exhibit
7 4 being the October 16, 2008, data?

8 MS. GRADY: Yes, your Honor.

9 EXAMINER BOJKO: I apologize.

10 MR. RESNIK: Is there a specific question
11 pending?

12 MS. GRADY: I can make one.

13 Q. (By Ms. Grady) Mr. Assante, I have given
14 you a chance to look at what has been marked for the
15 record purposes as OCC Exhibit 4. Do you recognize
16 that as a pro forma information that you understood
17 that the company filed on October 16 of this year?

18 A. Yes, I do.

19 Q. And would that be the information from

20 which you believe that you could -- let me strike

21 that.

22 After reviewing that information, are you

23 able to tell me how much the company has estimated it

24 will not recover from incremental -- of incremental

25 FAC costs for the 2009 -- excuse me, 2010 and 2011

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1 period for CSP as well as Ohio Power?

2 A. Well, I am looking at the income
3 statement and the balance sheet for Ohio Power right
4 now, and I don't think it's possible to answer your
5 question because the regulatory asset would be buried
6 in the line regulatory assets. The company has other
7 regulatory assets so I couldn't tell how much that
8 increased from year to year, and on the income
9 statement it just has cost of sales. There would be
10 a deferral credit buried in there but I couldn't tell
11 you how much that is.

12 Q. Now, the schedules you were looking at,
13 if you could tell me what page within that exhibit,
14 that would be helpful.

15 A. On page 5 of 10 for the income statement
16 for Ohio Power and the balance sheet 6 of 10.

17 Q. Yes.

18 A. There isn't enough detail here for me to
19 answer that question.

20 Q. Mr. Assante, were you involved in

21 preparation of this document for filing?

22 A. No, I was not.

23 Q. Do you know if there is any company

24 witness that would have been involved in the

25 preparation of this document for filing?

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1 A. Well, the department that I understand
2 put this document together was our forecasting and
3 budgeting group. Mr. Nelson, who is a witness in
4 this case, is a manager at that group so I would
5 think he would be able to possibly answer your
6 questions.

7 Q. Thank you. Now, for purposes going back
8 to your exhibit, Mr. Assante, for purposes of LAV-1,
9 you are assuming there is no deferred fuel adjustment
10 clause expense for CSP for 2010 and 2011?

11 A. No, that's not correct. I am assuming
12 that the -- that there is no increase in fuel
13 expenses, in other words, if you looked at Columbus &
14 Southern, the -- the estimate for the base FAC is
15 260 million and in '10 and '11 I am still using
16 260 million, and so I am assuming there is no
17 increase, but there is a fuel cost in -- and there is
18 deferrals -- there are deferrals for 2009 and 2010
19 for CSP.

20 Q. Thank you for that correction. Do you
21 think that is a -- an accurate assumption to assume
22 that the fuel costs for Columbus Southern Power as
23 well as Ohio Power will remain the same as you have
24 indicated for 2009 into the future for 2010 and 2011?

25 A. It would be highly unlikely that that

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1 would be an accurate assumption. I would presume

2 there would be some increase or decrease.

3 Q. Now, if the fuel costs were to increase,

4 Mr. Assante, that would create more deferrals, would

5 it not, and with the deferrals would come more

6 carrying charges and a higher regulatory asset

7 balance upon which the carrying charges are based?

8 A. Yes, the same thing -- the opposite would

9 be true, however, if there was a decrease in fuel

10 costs.

11 Q. And for purposes of this exhibit, why did

12 you make that assumption that there would be no

13 change in the FAC revenue requirement for those three

14 years?

15 A. Well, it's just out of necessity because

16 I was not given any estimate for fuel cost for 2010

17 and 2011. I was only given 216 and 367 million

18 dollars.

19 Q. Now, going back to page 5 of your

20 testimony. On page 5 of your testimony at line 22
21 you talk about there that: "The Companies are
22 requesting that the Commission approve the proposed
23 phase-in plan inclusive of the recovery of their
24 phase-in regulatory assets." Do you see that
25 reference?

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1 A. Can you give me a line, reference,
2 please?

3 Q. I'm sorry, that would be line 21 --
4 starting on 20 going to 22.

5 A. Yes.

6 Q. And that the phase-in regulatory assets
7 you are referring to there, those would be what you
8 characterized as the regulatory asset balance on
9 LVA-1?

10 A. That's correct.

11 Q. Now, on page 6, Mr. Assante, you talk
12 about -- and I am looking at lines 4 through 5, that
13 the "phase-in will be accomplished through the
14 deferral of a sufficient amount of FAC costs not
15 being recovered in current rates." Do you see that
16 reference?

17 A. Again, if you could give me a line
18 reference.

19 Q. That would be line 5 on page 6 of your

20 testimony.

21 A. Yes.

22 Q. And you define "sufficient" by tying it

23 to the 15 percent; is that correct?

24 A. That's correct.

25 Q. Now, on page 19 of your testimony you

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1 were talking again about LVA-1 and you indicate there
2 on lines 20 through 21 that you have assumed there
3 will be no under or over recoveries under the trueup
4 mechanism in 2009 through 2011 under your Exhibit
5 LVA-1. Do you see that reference?

6 A. Yes, I do.

7 Q. Mr. Assante, what happens in terms of the
8 total cost if there are underrecoveries under the
9 trueup mechanism?

10 A. I think that Mr. Roush indicates in his
11 testimony that if there are underrecoveries, that
12 they would be added to the FAC costs subject to being
13 phased in, and if we already had a deferral in that
14 period, it would probably increase that deferral.

15 Q. If there is an increase in the deferral ,
16 that would also under your LVA-1 increase the
17 ultimate cost of the phase-in plan; is that correct?

18 A. Only to the extent there would be
19 carrying cost, yes.

20 Q. For purposes of LVA-1 is it reasonable --

21 let me strike that.

22 Is it reasonable to assume under the

23 company's proposed phase-in plan that there would be

24 no under- or overrecoveries under the trueup

25 mechanism in the 2009 through 2011 period?

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1 A. Again, that would be unlikely there would
2 probably be a difference between the FAC revenues
3 recovered and the actual FAC costs.

4 Q. Now the total fuel adjustment clause with
5 the carrying costs under the assumption you have made
6 for LVA-1 for CSP would be 879 million and
7 approximately 1.463 billion for Ohio Power Company
8 over that ten-year period?

9 MR. RESNIK: Your Honor, could I have
10 that question read back, please.

11 EXAMINER SEE: Yes.

12 (Record read.)

13 A. That would be the total revenue
14 requirement, assuming my assumption is correct.

15 Q. Now, let's go back to page 9 in your
16 testimony, Mr. Assante. Let's go to the top of that
17 page. And there's a carry-over sentence there from
18 page 8, and in that carry-over sentence you indicate
19 that on a monthly basis the phase-in incremental FAC

20 cost deferrals can be increased by any additional
21 new -- any additional revenue requirement. Do you
22 see that?

23 A. Yes.

24 Q. And by revenue requirement there, are you
25 referring to the transmission cost recovery rider and

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1 any government mandates?

2 A. No. I'm -- no, I am not. I am referring
3 to probably additional FAC cost, in other words, FAC
4 costs were greater than we had forecasted. If they
5 were increased, it would then go into the 15 percent
6 test and would probably result in an increase of the
7 deferrals.

8 Q. I guess I really misspoke. I was meaning
9 to go down three lines and I want to focus on that
10 testimony as opposed to the testimony I directed you
11 to.

12 Where you say: "Phase-in plan deferrals
13 will be adjusted when this occurs in order to return
14 to the limitation," and here is where I want you to
15 pay attention, "except for when the increase results
16 from FERC initiated costs included in the Companies'
17 Transmission Cost Recovery rider." Are you there
18 saying that the 15 percent cap on the increase to
19 customers during the 2009 through 2011 period would

20 not be applied to the transmission costs recovery

21 rider costs?

22 A. If -- if that rider would increase

23 according to the application, at least my reading of

24 the application, that would not be included in the

25 approximately 15 percent cap.

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1 Q. So customers could see more -- more than
2 a 15 percent increase under your proposal if that
3 rider increases?

4 A. Yes, under the companies' proposal they
5 could see more than a 15 percent increase if that
6 happened.

7 Q. Are there any other increases that are
8 not included in the 15 percent cap that could be
9 incurred that would push that increase above and
10 beyond the 15 percent other than the transmission
11 costs recovery rider?

12 A. It's my understanding that the
13 application also provides for any government mandated
14 costs that may occur.

15 Q. And what would those costs be,
16 Mr. Assante; if you know?

17 A. That could be almost anything. They
18 could be a carbon tax. Whatever the government
19 decides to do, either the State, Federal Government

20 does. Even the cities, localities can raise their
21 costs any time they want by passing legislation.
22 Q. And your testimony today would be that
23 the application specifically provides for these items
24 not to be included in the 15 percent determination;
25 is that correct?

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1 A. Yes.

2 Q. Now, on page 9 at the bottom on lines 21
3 and 22, you indicate that "A significantly longer
4 recovery period would increase the carrying costs to
5 be paid." Do you see that reference?

6 A. Yes.

7 Q. Can you define "significantly" for me?

8 A. Any increase in the period of recovery
9 would have an effect on the carrying costs. A
10 significant increase would certainly have a
11 significant effect. So the word "significant"
12 really -- that's a term that everyone has to define
13 for themselves in my opinion.

14 Q. Would a shorter recovery period decrease
15 the carrying costs paid by customers?

16 A. Yes, it would.

17 Q. Let's go to page 22 of your testimony.

18 EXAMINER SEE: I'm sorry, what page was
19 that?

20 MS. GRADY: I'm sorry, 22.

21 Q. Now, on page 22 you indicate, and I am
22 looking at the top portion of your testimony, lines 1
23 through 3, you indicate that the Companies will add
24 periodic over- and underrecovery adjustments to the
25 total incremental FAC costs to be phased in. Do you

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1 see that?

2 A. That's correct.

3 Q. And that there will be under- or

4 overrecovery that will be collected or returned to

5 customers.

6 A. During deferral period '09, '10, '11,

7 Mr. Roush indicates in his rate design that if we had

8 an underrecovery or overrecovery, it would adjust the

9 amounts to be phased in and included in his

10 15 percent test. Subsequent to 2011 the -- we assume

11 the FAC would continue, fuel adjustment clause would

12 continue and under/overrecovery would be deferred and

13 recovered or refunded in the FAC period, quarterly

14 FAC period.

15 Q. Under the 2009-2011 time period if there

16 are any deferrals that under or overrecovery, it will

17 not be returned or collected from customers in the

18 subsequent fuel period; is that correct?

19 A. I believe Mr. Roush uses the term "may"

20 be treated that way. As I understand it, if the
21 Commission were to prefer that it be refunded to
22 customers in the next period, we would do that.

23 Q. So it's your understanding that the
24 Company is not proposing to -- let me strike that.

25 Would Mr. Roush be the appropriate

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1 witness to ask about whether or not that really is
2 the companies' proposal or not?

3 A. I think he would be the best person to
4 answer this.

5 Q. Is it your understanding that the --
6 the -- in the period from 2012 through 2018 the over
7 and underrecovery mechanism -- the over and
8 underrecovery mechanism works as a traditional fuel
9 clause would work where the following period the -- a
10 true-up would be occurring and dollars would either
11 be flowing from -- flowing to customers or collected
12 from customers based on the previous period?

13 A. That's my -- that's my understanding,
14 yes.

15 Q. But that's different, in your opinion,
16 from how it works during the 2009 through 2011 period
17 if there are deferrals.

18 A. I guess all I am saying is that Mr. Roush
19 in his testimony indicates that he may adjust the FAC

20 costs that go into the 15 percent test as a way of
21 handling under and over recoveries. That's not
22 desired. It's my understanding the company wouldn't
23 have a problem with refunding over recoveries or
24 collecting underrecoveries in the next period.

25 Q. Now, for the underrecovered fuel

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1 adjustment clause expenses which would be deferred,
2 does the company propose carrying charges for those
3 deferrals from 2009 through 2011?

4 A. Yes.

5 Q. For the overrecovered FAC expenses, if
6 there are deferrals, does the company propose
7 carrying charges for those?

8 A. Yes. Any amounts deferred, the company
9 is proposing to be made whole by charging a carrying
10 cost.

11 Q. If you overrecover fuel adjustment clause
12 expenses, the company is already being made whole,
13 right?

14 A. If we overrecover, it would reduce the
15 deferrals under Mr. Roush's suggestion. The
16 suggestion and as a result it would automatically
17 reduce the carrying costs going forward.

18 Q. And the reduced deferrals, the customers
19 would not see the benefits of the reduced deferrals

20 until those deferrals were subsequently collected
21 from customers in the 2012 through 2018 period; is
22 that correct?

23 A. If that's the method that's chosen, they
24 would get the benefit each year during that period of
25 time as they recover one year's worth of those

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1 deferrals.

2 Q. So the customer could overpay in 2009 and
3 then receive its money back in 2012 through 2018?

4 A. With interest, correct.

5 Q. Under your proposal, Mr. Assante, the FAC
6 deferral is nonbypassable during the ESP period?

7 A. That's not my proposal. That's what the
8 law says. Section, I think it is, 4928.144 indicates
9 that phase-in -- phase-in rider would be
10 nonbypassable and the deferrals would be in
11 accordance with generally accepted accounting
12 principles.

13 Q. Is the company proposing that its FAC
14 deferral mechanism is nonbypassable consistent with
15 the 4928.144?

16 A. That's correct.

17 Q. Now, if you know, Mr. Assante, is the FAC
18 deferral nonbypassable for the 2012 through 2018
19 period under the companies' proposal?

20 A. Phase-in rider would be nonbypassable for

21 the entire ten-year period, correct.

22 Q. Mr. Assante, I am going to turn to the

23 discussion in your testimony about the possible early

24 plant closure accounting. And I think that begins on

25 page 23 of your testimony.

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1 A. Yes.

2 Q. And on page 23 of your testimony, and I
3 am looking at lines 4 through 9, you indicate that
4 Mr. Baker testifies that it is possible that one or
5 more of the companies' generating units may have to
6 close earlier than the retirement date assumed
7 currently for depreciation purposes. Do you see that
8 reference?

9 A. Yes, I do.

10 Q. And one of the reasons that you list for
11 the companies closing the generating units earlier
12 than the retirement date assumed is economic reasons.
13 Now, is that -- is that something that you are
14 testifying to or something that Mr. Baker is
15 testifying to?

16 A. I don't see anyone that would be
17 testifying to the -- an economic reason to close the
18 plant because we presently do not have one. All I am
19 stating here is that I believe what Mr. Baker is

20 saying if we were to have a failure, safety issue,
21 major environmental issue at one of our older units,
22 it may not be economical to repair it or to fix the
23 problem and the unit may have to be closed as
24 occurred in 2005 when we had a safety issue at our
25 Conesville Units 1 and 2. The unit could have been

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1 repaired but due to the age of the units, it was not
2 considered economical. It would cost more to repair
3 it than benefit to the company and the customers
4 continuing to have it on line.

5 So if that were to occur, the purpose of
6 this -- again, the purpose of this testimony is to
7 try to ask permission to be authorized to defer those
8 costs so the Commission could consider during the ESP
9 process whether those costs are prudent and whether
10 or not they should be recovered or not.

11 Q. Now, I want to focus on your discussion
12 about the economic reasons. Are you -- would you
13 include within an economic reason the fact that power
14 is available on the market to customers that's at or
15 below the price being -- of the power in one of these
16 early retirement units?

17 A. Well, certain if we could buy power at a
18 lower cost than these units could generate. It
19 wouldn't make sense to repair the unit and put it

20 back on line, so that would be an economical
21 expenditure of funds. Of course, we have to consider
22 whether that's a temporary price or long-term price.
23 Q. So that would be a reason in your -- in
24 your recommendation for collecting early plant
25 closure costs; would it not?

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1 A. That may be a reason why it was
2 determined not to be economical to repair the unit
3 and to shut it down. And it would -- it certainly
4 would be a reason the Commission would have to
5 consider as to the prudence of that decision.

6 Q. I guess I'm -- maybe we are not
7 communicating and I am sure it's my fault. I was
8 speaking of the instance where we were talking about
9 the economics of whether or not power could be
10 purchased on the market by a customer at a price
11 lower than what -- the power that was being generated
12 at one of your units, and I guess I didn't understand
13 that to be something with -- having to do with repair
14 of the units. And when you started to talk about
15 repair, I think you were mixing -- mixing the two
16 concepts up. I am speaking of economic in terms of
17 the purchase of the power.

18 And so I guess my question then is under
19 the -- under that kind of economic situation you are

20 asking the -- that the Commission allow you to
21 institute certain accounting for that early closure
22 of that plant; is that correct?

23 MR. RESNIK: Your Honor, if I may,
24 because I got a little lost there, if I could just
25 ask for a clarification whether you are -- at one

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1 point you said something about the price of the power
2 customers could acquire the power at. Then I thought
3 you were shifting back to the price of power that the
4 company would be able to purchase to replace the
5 capacity. I am not sure which one.

6 MS. GRADY: I think in either condition.

7 My question is premised in either condition.

8 A. Well, I think we are getting a little
9 confused. I believe Mr. Baker was not testifying to
10 that situation you are speaking of.

11 Q. I agree.

12 A. He was testifying to a situation where a
13 power plant would be a failure or were to have a
14 safety issue and would need to be repaired. We would
15 take it off line and we would make an economic
16 determination, as we do with every capital
17 expenditure, whether it made sense to spend the money
18 to repair, or in the case of the unit if it would
19 cause a shutdown, to shut the unit down. You are

20 speaking of an economic decision to shut a unit down

21 because you can buy power cheaper on the market.

22 Q. Yes.

23 A. And that is not what I believe this is --

24 we are asking for.

25 Q. Okay. I think that clarifies it.

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1 A. Okay.

2 Q. Now, on page 24 I am looking at lines 4
3 through 6, and you indicate there that if the
4 companies' generation/supply business were still
5 cost-base regulated, you could avoid the loss by
6 charging the investment to the Accumulated Reserve
7 for Depreciation Account. Do you see that reference?

8 A. Yes.

9 Q. Is it possible that if the companies'
10 generation supply business were still cost based,
11 that the Commission could determine that the
12 remaining investment would not be recoverable in
13 rates?

14 A. Yes, that's what's in the Commission's
15 purview.

16 EXAMINER SEE: I'm am sorry, could you
17 repeat the question.

18 (Record read.)

19 A. Yes, that's within the Commission's

20 purview to make that decision.

21 Q. Now, on page 25 of your testimony if you
22 go to lines 10 through 12, you indicate there that
23 the net loss of 39 million related to Conesville No.
24 1 and 2 was not recovered from ratepayers since it
25 was not contemplated and, therefore, was not included

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1 in the determination of the already adjudicated RSP
2 rate increases. Do you see that reference?

3 A. I think I corrected that from RSP rate to
4 ETP rate.

5 Q. Yes, thank you for that, ETP. Do you see
6 that?

7 A. I didn't catch the page number, I'm
8 sorry.

9 Q. That's line 10 through 12 on page 25.

10 A. Yes.

11 Q. And by the adjudicated ETP rate increase,
12 what case numbers are you referencing there?

13 A. I haven't got them committed to memory,
14 but it's the 2000 ETP Decision. It was a settlement
15 case.

16 Q. Were the increases in that case cost
17 based; if you know?

18 A. Well, that was a transmission case under
19 SB 3, so in accordance with the accounting rules,

20 which would be the EITF No. 97-4 and FASB statement
21 No. 101, the company was forced by the passage of
22 that act to discontinue application of SFAS 71 and is
23 no longer considered to -- for accounting purposes to
24 have cost-base regulated rates and that's because SB
25 3 set the company on a path or transition to market

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1 rates in 2006.

2 Q. So essentially they were not cost-based
3 rates because otherwise you could have continued with
4 SFAS 71?

5 A. Whether the rates were cost based or not
6 at the time is debatable, but under the accounting
7 rules we no longer were considered to have cost-based
8 rates.

9 Q. And does -- did those rates generate
10 revenues for both Columbus Southern Power and Ohio
11 Power?

12 A. Yes.

13 Q. Are you familiar with how much revenue
14 was generated or produced by the ETP cases for Ohio
15 Power or CSP?

16 A. No, I am not.

17 Q. Are you familiar with the expenses that
18 were incurred by those companies during that time
19 frame?

20 A. When you say familiar, I mean, I am
21 familiar with it but I certainly couldn't tell you
22 how much that was.

23 Q. Wouldn't it be difficult, Mr. Assante, to
24 determine whether or not the \$39 million was
25 recovered from ratepayers based upon the fact that

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1 the -- based upon how the rates were set in the ETP
2 cases?

3 A. Well, the rates were frozen in the ETP
4 cases so I don't see how we could have collected a
5 cost that we never had before.

6 Q. You were collecting re --

7 A. They couldn't have been included in those
8 rates since the rates were frozen in 2000 and the
9 loss happened in 2005, so I think it's safe to
10 presume that those costs were not specifically being
11 recovered.

12 Q. You were recovering revenues; were you
13 not?

14 A. Yes, we were.

15 Q. And you don't know how much more revenues
16 you recovered than your expenses during that time
17 frame, do you?

18 A. I cannot give you that number.

19 Q. Now, going to page 25, line 23, you

20 indicate there that "If one of the Companies
21 experience net early closure costs that it will file
22 a timely request with the PUCO to recover such
23 prudent early closure costs through a nonbypassable
24 rider." Do you see that reference?
25 A. Yes, I do.

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1 Q. When you refer to "prudent early closure
2 costs" there, can you tell me when those costs were
3 determined to be prudent?

4 A. Well, since we haven't had a closure, it
5 will happen some date in the future, if we do have
6 one. We are hopeful we don't. We don't expect to
7 have one, but if we did have one at some date in the
8 future, we would determine whether we thought those
9 costs were prudent. If we felt they were prudent, we
10 would file for recovery if this is approved.

11 Q. And it would ultimately be up to the
12 Commission to determine if there was -- those were
13 prudently incurred costs; is that correct?

14 A. That's correct.

15 Q. And you also indicate on page 26, and I
16 am looking at lines 4 through 5, that you are asking
17 for a carrying charge to be established until the
18 regulatory deferral is fully recovered. Do you see
19 that reference?

20 A. Yes, I do.

21 Q. And how long would that carrying charge
22 be -- how long would that run; if you know?

23 A. Again, we haven't had the situation. We
24 haven't put together a filing and I don't know what
25 period of time we would ask for. That would be a

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1 rate decision to be made by our regulatory
2 management, by our rate design people, and it also
3 would be dependent on the Commission's view on how
4 long that period should be.

5 Q. Now, at this time, Mr. Assante, you don't
6 expect that any of AEP generating plants will close
7 prematurely and you have no plans -- when I say
8 "you," the company has no plans that you are aware of
9 to close any of its plants prematurely for the
10 reasons that you stated in your testimony; is that
11 correct?

12 A. That's correct.

13 Q. Now, on page 27, lines 4 through 8, you
14 indicate that the unit being shut down early will
15 continue to benefit ratepayers under the provisions
16 of SB 221 for the remainder of its productive life.
17 Can you tell me how if you shut a plant down early,
18 it will continue to benefit ratepayers under SB 221?

19 MR. RESNIK: Can I have the question read

20 back, please.

21 (Record read.)

22 A. I'm sorry if my testimony is confusing to

23 you, but I honestly did not mean that a plant would

24 benefit after it was shut down. What I was trying to

25 convey there was that between the passage of SB 221

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1 and its effective date, which I guess is January 1,
2 2009, and the date of this early closure, would be
3 benefiting customers through a POLR obligation.
4 That's what I meant to say and I think it was a
5 little misleading. I apologize.

6 Q. So as long as the plant is in service, it
7 is benefiting ratepayers, but once it's taken out of
8 service or shut down, it no longer benefits the
9 customers; is that your testimony?

10 A. It's not productive. It doesn't benefit
11 anyone.

12 Q. Mr. Assante, you testify to gridSMART
13 accounting; do you not?

14 A. Yes.

15 Q. Let's turn to page 40 of your testimony.
16 You begin discussing gridSMART on lines 20 through 22
17 -- or 20 through 23 on page 40 of your testimony.
18 And then you reference Ms. Sloneker's testimony. And
19 you indicate that Ms. Sloneker's testimony includes

20 estimated costs of gridSMART including the costs
21 associated with premature retirement of existing
22 meters and other equipment. Do you see that
23 reference?

24 A. Yes.

25 Q. When you say "premature retirement," can

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1 you explain what you mean there?

2 A. Well, it's my understanding they will be
3 replacing all of the meters in the eastern quadrant
4 of CSP territory, Central Ohio service territory.
5 Obviously most of those meters still have a
6 productive life or would have had a productive life
7 if they weren't replaced. That would be a premature
8 retirement. Anything before the end of the
9 depreciation life would be premature retirement.

10 Q. Now, these meters are these dumb meters
11 as opposed to smart meters?

12 A. I prefer to call them traditional meters.

13 Q. Now, the traditional meters, Mr. Assante,
14 generally have a life of about 30 years; is that
15 correct?

16 A. Yes, that's the life we use.

17 Q. Now, you have also got a reference to
18 other equipment to be replaced. And what are you
19 referencing there beyond the meters?

20 A. Well, it's my understanding that they
21 will be replacing voltage regulators, switches, other
22 conductor equipment basically in order to replace it
23 with equipment that does the same thing and is
24 capable of receiving communications, you know,
25 through wireless communication so that they can be

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1 controlled.

2 Q. And is this other equipment being
3 prematurely retired as well under the gridSMART
4 program?

5 A. If the equipment --

6 Q. The other equipment that you just
7 described.

8 A. Yes. Again, any retirement prior to the
9 normal replacement at the end of the physical life or
10 sometime shortly thereafter would be a premature
11 retirement.

12 Q. Thank you. In Ms. Sloneker's testimony
13 the costs associated with retiring this premature
14 retirement of meters is approximately \$1.9 million;
15 is that correct?

16 A. I do not recall.

17 Q. Was that a figure that you would have
18 provided to her?

19 A. No, it is not. I understand those were

20 engineering estimates that our distribution engineers

21 worked up for her.

22 Q. You just have to implement the accounting

23 for it; is that correct?

24 A. We would account for the actual

25 retirements, yes.

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1 Q. Now, you testify on page 41 of your
2 testimony that as gridSMART equipment is installed,
3 the old reclosures, switches and voltage regulators
4 can be reused or salvaged for parts. Do you see that
5 reference? And I am looking at lines 21 through 23.

6 A. Yes.

7 Q. What accounting treatment do you propose
8 for these recycled and reused parts in your
9 application?

10 A. They are not being included in the rider
11 that Ms. Sloneker estimates. And our accounting
12 treatment would be to retain them since they are --
13 since we can use them, reuse them, as assets of the
14 company.

15 Q. Would it be appropriate to offset the
16 rider by these costs since they are then being reused
17 in the depreciation -- and would then have
18 depreciable lives associated with them remaining?

19 A. No, I don't believe that would be

20 appropriate. Those costs are already built in and

21 should already be built into our rate structures.

22 Q. Now, on page 42 of your testimony, and I

23 am looking at lines 9 through 12, you testify that

24 the current smart meters have two separate components

25 consisting of a communication or computer component

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1 and then a basic meter component. Do you see that

2 reference?

3 A. That's correct.

4 Q. Now, the communication component has an

5 expected seven-year useful life; is that correct?

6 A. Yes.

7 Q. And the meter component has a 15-year

8 physical life?

9 A. Yes.

10 Q. And you have indicated that the company

11 plans to capitalize the meters as one retirement unit

12 with a seven-year life. Do you see that?

13 A. That's correct.

14 Q. Can you -- strike that.

15 And you further indicate in your

16 testimony that by the time the meters are replaced in

17 five to seven years with advanced smart meters, the

18 new advanced smart meters are expected to be one --

19 one unit and not just separate units as they are now.

20 A. Yes. And that's the reason why I am
21 proposing to treat them as one retirement unit with
22 one life and, of course, if you have to replace the
23 computer component in five to seven years, then
24 obviously useful life is not 15 years but rather
25 seven years at best. That's why I am proposing to

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1 use seven years as the useful life because we are
2 told that the manufacturers are going to cease
3 manufacturing these meters in the future in two
4 parts, in other words, you are not going to be able
5 to pull out the computer communications part and put
6 it -- and replace it. They are going to have to
7 replace the entire meter.

8 Q. Now, do you know what a smart meter costs
9 as a unit currently for the company and the cost
10 that's included in the gridSMART application -- or
11 the gridSMART part of your ESP?

12 A. No, I do not.

13 Q. Would you accept subject to check that
14 under KLS, and that's Ms. Sloneker's Exhibit No. 1,
15 page 2 of 7, that the cost of a smart meter is
16 \$333.45?

17 A. Yes, subject to check. Yes, subject to
18 check.

19 MS. GRADY: I'm sorry, I thought -- I

20 thought that Marv was saying I object.

21 MR. RESNIK: No, no. no. I know you

22 heard that a lot but not yet.

23 MS. GRADY: I just was thinking that was

24 coming.

25 Q. (By Ms. Grady) Now, do you know the value

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1 or the components of the current smart meter that has
2 been included in the gridSMART program, that is,
3 could you breakdown the cost of the \$333.40? Would
4 you know what the cost of the communication piece of
5 it is that could be separated from the basic meter
6 component piece?

7 A. Well, as I indicated, in the future you
8 won't be able to make that separation. I do not know
9 that though.

10 Q. But for the current period you are asking
11 for the current smart meters that are included in the
12 gridSMART, you are asking for the seven-year life;
13 isn't that correct, that have the two components?

14 A. Yes. And the reason for that is under
15 Accounting Research Bulletin 43 the equipment is --
16 should be depreciated over its expected useful life
17 not its physical life and we -- I have been informed
18 by Ms. Sloneker and her engineer staff and customer
19 service engineering staff that these meters will --

20 are expected to be replaced in five to seven years.

21 Q. But that's the companies' decision to

22 replace these meters in five to seven years. The

23 meters will still be working in five to seven years;

24 wouldn't you agree?

25 A. Well, my cell phone will still be

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1 working, but I am going to replace it with new
2 technology.

3 Q. And --

4 A. I am told we intend to employ this
5 technology and upgrade it when the technology is
6 significantly better and they expect that will happen
7 in a five- to seven-year period.

8 Q. But the company is making a decision, is
9 it not, that the technology should be replaced in
10 five to seven years regardless of the fact of whether
11 it continues to work; isn't that correct?

12 A. It's my understanding that we expect we
13 will make that decision if, in fact, the -- the
14 technology improves as we expect it will and the
15 customer will have more functionality and the company
16 will have greater functionality with the new meters.

17 Q. When you said if the technology improves,
18 in the application that the company has, it is
19 assuming that it will make that purchase; is it not?

20 In fact, you are asking for the accounting to fulfill
21 that acquisition in years -- in years seven of
22 advanced smart meter.

23 A. Again, I am making that recommendation
24 based on our engineers informing me they expect
25 useful life of these new meters, these so-called

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1 smart meters, to be five to seven years.

2 Q. And what you are talking about is that in
3 seven years getting even more advanced smart meters,
4 not just smart meters but advanced smart meters,
5 replacing the initial smart meters put in in Phase 1
6 of your program with advanced smart meters in year
7 seven regardless of whether the smart meters are
8 still working; isn't that correct?

9 A. That's my understanding what they believe
10 they will be doing, again, as a result of technology
11 enhancements or improvements.

12 Q. Mr. Assante, are you aware of any federal
13 legislation that sets the depreciable life of smart
14 meters at ten years as opposed to the seven years you
15 are seeking Commission approval for here?

16 A. The only federal legislation I am aware
17 of is recent legislation in one of the bailout bills
18 in which it provided that smart meters should be
19 depreciated for tax purposes over ten years. The tax

20 rates are traditionally different.

21 Q. Would that be HR 1424 that you are

22 referencing; if you know?

23 A. I don't know the bill number, I'm sorry.

24 Q. Do you know if there are any standards or

25 provisions in SB 221 that affect the depreciation

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1 schedules or accounting methods proposed by AEP

2 regarding its gridSMART program?

3 A. Not to my knowledge.

4 Q. Do you know, Mr. Assante, or are you

5 aware of any evidence that the company has that the

6 more advanced smart meters are more cost effective or

7 beneficial than what is currently being installed in

8 the phase-in gridSMART program?

9 MR. RESNIK: Your Honor, I'm going to

10 object. That is beyond the witness's testimony. He

11 is just testifying to the accounting consequences as

12 he sees them from what he has been told the company

13 plans to do with these meters.

14 EXAMINER SEE: Did you have a response,

15 Ms. Grady?

16 MS. GRADY: I think it's a good question.

17 EXAMINER SEE: Objection sustained.

18 Q. (By Ms. Grady) If the Commission were to

19 adopt your proposed accounting -- strike that.

20 Mr. Assante, would you agree with me, and
21 chances are you are not going to, but would you agree
22 with me the Commission should make the determination
23 as to the appropriate depreciation rates to set at
24 the same time or after it determines that it's
25 reasonable to replace meters?

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1 A. No, I don't agree with that because at
2 that point it's too late. You have already
3 underdepreciated. These meters will have a large
4 amount of strain and cost sitting in the account. We
5 will have to deal with another loss. I don't think
6 it's prudent to be -- when you are expecting to
7 replace meters in five to seven years, to be setting
8 up depreciable life that is substantially longer than
9 that, it will result in undepreciated balance that
10 will trade a loss. Accounting requires that you do
11 your best to depreciate equipment over its expected
12 useful life in order to match the revenues. It
13 generates costs.

14 Q. Are you expecting the Commission to make
15 a determination in this case that it's appropriate in
16 seven years -- seven years down the road to replace
17 the Phase 1 smart meters with advanced smart meters?

18 A. I am expecting the Commission to decide
19 whether -- whether it agrees with the companies'

20 proposal or not. That's its job. I understand

21 that's not an easy thing to do at times.

22 Q. Mr. Assante, I am going to move to

23 off-system sales. Are you aware of the accounting

24 for off-system sales?

25 A. Yes, I am.

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1 Q. Now, when the company files its 10K and
2 its financials, do you exclude off-system sales from
3 your reported earnings?

4 A. No, we do not.

5 Q. Are the margins on off-system sales
6 included in the earnings for purposes of the ESP and
7 the SEE test in this case?

8 MR. RESNIK: May I have the question read
9 back, please?

10 EXAMINER SEE: Sure.

11 (Record read.)

12 MS. GRADY: For purposes -- I'm sorry, if
13 I could clarify.

14 MR. RESNIK: Sure.

15 Q. (By Ms. Grady) For purposes of the SEE
16 test in this case --

17 MR. RESNIK: And just to be clear, we are
18 not talking about applying a SEE test in this
19 proceeding but rather the SEE methodology proposed by

20 the company for application in 2010.

21 MS. GRADY: Yes. Thank you for that

22 clarification.

23 THE WITNESS: After all that, could you

24 please -- could I please have the question?

25 EXAMINER SEE: Sure.

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1 (Record read.)

2 A. I am not sure I understand that question.

3 Could it be -- could you repeat the question? That

4 didn't --

5 Q. I don't think I can. I am going to move

6 on. You are not proposing, Mr. Assante, that

7 off-system sales be included in the fuel adjustment

8 clause in this proceeding or offset the revenue

9 requirements being requested, are you?

10 MR. RESNIK: Your Honor, I am going to

11 object. This is not the witness on fuel adjustment

12 cost. If you want to ask about the companies'

13 proposal, Mr. Nelson would be up and I would suggest

14 that would be the appropriate witness.

15 Q. Well, you testified to the FAC phase-in

16 rider, didn't you?

17 A. Yes, I -- yes, I testified to the

18 phase-in plan accounting. Nowhere in my testimony do

19 I speak to system sales.

20 Q. In the phase-in accounting that you
21 testified to, are you aware of in your review of the
22 phase-in accounting and your sponsorship of that
23 accounting whether or not the off-system sales are
24 somehow figured into that?

25 A. Well, what I am aware of is that to my

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1 knowledge, system sales have never been included in
2 Ohio in the fuel clause when it existed, so I assume
3 it wouldn't be included in this fuel clause either.

4 Q. Are you aware of whether off -- how
5 off-system sales for AEP have been treated in the
6 past outside of a fuel cost proceeding?

7 A. Off-system sales in the past in Ohio have
8 always been treated as a base rate item.

9 Q. And isn't it your understanding that in
10 the treatment of off-system sales there was some
11 sharing of the revenues from off-system sales between
12 ratepayers and shareholders?

13 MR. RESNIK: Your Honor, I am going to
14 object. I am trying to rehash what the law was and
15 what ratemaking was prior to Senate Bill 3 is
16 irrelevant. We don't have cost-of-service ratemaking
17 for generation function any more. So you may as well
18 be asking about reconstruction cost new less
19 appreciation.

20 MS. GRADY: Your Honor, I think the
21 witness -- I am following up on what the witness
22 responded to. I am just exploring his response. He
23 opened the door.

24 MR. RESNIK: Well, the door was open by
25 the question. I gave some latitude by not objecting

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1 to that one. That doesn't mean I am precluded from
2 objecting as we continue going down the road. And
3 Mr. Nelson is the witness on the fuel costs.

4 EXAMINER BOJKO: Well -- I mean, your
5 whole FAC premise baseline is based on a 1999 number
6 which is prior to Senate Bill 3 as well so he is the
7 one that mentioned where we -- how we got here today,
8 so I think that counsel has the right to explore
9 that, so the objection is overruled.

10 Q. (By Ms. Grady) I think there is a
11 question pending. Do you need that repeated?

12 A. Yes, I would appreciate it.

13 MS. GRADY: If you could repeat it.

14 (Record read.)

15 A. The last rate case we had was a long time
16 ago in Ohio. My recollection was that I don't
17 remember there being sharing. It's quite possible
18 there was, but I do not recall that.

19 MS. GRADY: If I may have a moment, your

20 Honor, that may be it, but I just want to check my

21 notes very quickly.

22 I think that's all. Thank you,

23 Mr. Assante.

24 THE WITNESS: Thank you.

25 EXAMINER SEE: Mr. Maskovyak.

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1 MR. MASKOVYAK: No questions, your Honor.

2 EXAMINER SEE: Mr. Randazzo.

3 MR. RANDAZZO: Just a couple, I think.

4 - - -

5 CROSS-EXAMINATION

6 By Mr. Randazzo:

7 Q. Good afternoon, Mr. Assante.

8 A. Good afternoon, Mr. Randazzo.

9 Q. If you would turn to page 5 of your
10 testimony, and the question and answer on the bottom
11 half of that page, as I understand it, I just want to
12 explore the structure of your proposal. You are
13 recommending that certain fuel-related costs be
14 deferred for recovery in the future and the recovery
15 period would be of the regulatory assets created by
16 the deferral process would be from 2012 through 2018,
17 correct?

18 A. That is correct. Unless as Mr. Roush
19 states in his testimony, I believe he states that if

20 it were to happen, the fuel costs would decline, he
21 could, you know, he could, if that was acceptable to
22 the Commission, he could reduce deferrals or amortize
23 deferrals down against that cost reduction.

24 Q. Right. But the accounting authority you
25 are seeking here would set up the opportunity, at

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1 least, for the amortization of the regulatory asset

2 to occur over that seven-year period, correct?

3 A. Yes.

4 Q. Okay. And I guess what I am struggling

5 with, and I will just confess this to you and see

6 where it goes, is we have got a three-year ESP with a

7 tail of seven years. And to what -- is your

8 amortization period connected at all to there being a

9 fuel adjustment mechanism in the period from 2012 to

10 2018?

11 A. No, there is no connection. We are

12 presuming there would be one for at least some of

13 that period, and what my testimony states is that

14 that would operate independently of this phase-in.

15 In other words, it would be deferred separately and

16 it would be recovered in the next period whenever the

17 Commission ruled it would be recovered or refunded in

18 the next period that -- and that would not get into

19 the phase-in. The phase-in would close at the end of

20 2012. There would be no new deferrals other than
21 carrying costs.

22 Q. And so that what we have structurally
23 here you have a surcharge, if I can use that word, to
24 amortize potentially regulatory assets and that
25 surcharge, at least during the period from

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1 potentially from 2012 to 2018, would be disconnected
2 from any price or rate that might be established in
3 this proceeding; is that correct?

4 A. Well, the use of the term disconnected, I
5 would characterize it differently. The law provides
6 for the phase-in option. If the Commission
7 authorizes a phase-in, we would -- we would have a
8 separate rider for that phase-in which by law is
9 nonbypassable. So it would be a separate rider that
10 would continue throughout that period, yes.

11 Q. Independent -- that rider would continue
12 independent of any price established or rate
13 established in this proceeding, correct?

14 A. Yes, it would continue.

15 Q. Okay. And then I take it that your
16 understanding of the phase-in that is permitted under
17 Senate Bill 221 is one that would allow for the
18 surcharge to operate independent of any rate or price
19 that's established in this proceeding; is that

20 correct?

21 A. Well, it would be a separate rider if

22 approved by the Commission. It would be recovered if

23 they approved over -- over that seven-year period to

24 end in 2018. Because it's a separate rider I guess

25 it would be separate from -- from other riders that

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1 would be approved in this filing.

2 Q. Now, if I were to tell you that the
3 Section 4928.144 says that the surcharge to amortize
4 the regulatory asset created as a result of a
5 phase-in has to be attached to the rate or price
6 that's established in this proceeding as a matter of
7 law, what you are proposing here is different than
8 that, correct?

9 A. In other words, you had to amortize the
10 regulatory asset during the term of the ESP plan
11 itself.

12 Q. You are not proposing that, correct?

13 A. No, I am not proposing that and that's
14 not how we read the law.

15 Q. Understood. Now, meters used to measure
16 consumption by customers, typically that would be
17 distribution plant; is that correct?

18 A. Yes.

19 Q. And the depreciation useful life --

- 20 useful service life of distribution plant is usually
- 21 something that would be considered in a distribution
- 22 rate case, correct?
- 23 A. It could be also considered in the
- 24 depreciation filing.
- 25 Q. Sure.

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1 A. But if you had a depreciation filing and
2 a depreciation in a distribution rate case, it could
3 be considered there, yes.

4 Q. Right. And meters come and go all the
5 time, right? I mean, it's item of plant where you
6 have a lot of items coming in and a lot of items
7 going out and you end up having a depreciation
8 reserve that's not for each individual meter but for
9 meters --

10 A. Composite depreciation, yes.

11 Q. Right. So that the -- what ends up being
12 reflected in the depreciation reserve is essentially
13 the average life of all the meters that are
14 installed, various vintages and various technologies,
15 correct?

16 A. That's correct.

17 Q. Now, with regard to the -- I understand
18 that Mr. Nelson is responsible for the capitalization
19 ratio that's used to compute the carrying cost rates

20 that are described in your testimony; am I correct

21 about that?

22 A. Yes. Mr. Nelson sponsors that rate.

23 Q. All right. Now, and you say at page 26

24 of your testimony that he supports a 50/50 debt to

25 equity ratio, and I am not going to ask you about the

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1 ratio itself. I want to talk to you about the effect
2 of that capitalization ratio. Are you aware of
3 circumstances in which the carrying cost rate applied
4 to an accumulated balance of a regulatory asset might
5 be specified as the embedded cost of debt? Are you
6 aware of circumstances where that has been done?

7 A. I don't believe I am aware of
8 circumstances somewhere that's been done that I am
9 aware of. I am not saying it hasn't been done. I am
10 just not aware of it.

11 Q. If -- if we were to compare the effect of
12 a carrying cost rate specified at the embedded cost
13 of debt versus a carrying cost rate specified at a
14 50/50 debt to equity ratio, would it be at least
15 conceptually correct to say that the 50/50 ratio
16 would be making a positive contribution to earnings?

17 MR. RESNIK: Your Honor, if I may, I
18 don't want to miss the opportunity, I would like to
19 pose an objection. The carry cost rate average,

20 carrying cost including the use of the 50/50
21 capitalization, is a matter that is sponsored by
22 Mr. Nelson. I believe the questions would be
23 appropriate for him rather than this witness.

24 EXAMINER SEE: Okay.

25 MR. RANDAZZO: If Mr. Resnik assures me

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1 Mr. Nelson will be in a position to talk about the
2 effect of the capital ratio on earnings, I would be
3 happy to defer the line of questions.

4 MR. RESNIK: He seems to think he can.

5 MR. RANDAZZO: I am happy to move on.

6 EXAMINER SEE: Okay.

7 Q. (By Mr. Randazzo) Now, with regard to the
8 early generating unit closure costs, again, somewhat
9 at least conceptually like the discussion we had
10 about meters, you will find, will you not, sir, in
11 the case of an electric utility various types of
12 generating units having various service -- useful
13 service lives, various -- various technologies being
14 deployed by the utility to service its customers,
15 correct?

16 A. Correct.

17 Q. And you may have some units that are
18 retired early and some units that actually operate
19 for years beyond their useful life, correct?

20 A. That's correct.

21 Q. And in your proposal to capture the cost
22 of early generating unit closure, are you proposing
23 to net against those costs the benefits associated
24 with generating units that may run beyond their
25 useful service lives?

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1 A. There is no accounting mechanism to do
2 that. We don't know which units will run beyond
3 their useful life and in addition as generally
4 substantial capital expenditures are necessary to
5 enable those units to run beyond their useful lives,
6 so we say benefits, certainly there is a benefit to
7 extending the life of the unit but there is also a
8 cost so there is a net benefit.

9 Q. Right.

10 A. I can't quantify that because we don't
11 know what units we are going to extend the life of
12 and what it's going to cost to do that and what the
13 value of power will be in the future. From an
14 accounting sense, there is no way to do that offset.

15 Q. Well, you can figure out what the net
16 cost associated with early closure is but you can't
17 figure out what the net benefit of life extension is;
18 is that what you are telling me?

19 A. I don't have a crystal ball. If a plant

20 closes, I can figure out what -- what the early
21 closure costs are, what the unappreciated balance is,
22 what any losses would be in the inventory pile in
23 regard to M&S inventories. I can't tell you what the
24 net benefit will be from a unit continuing beyond its
25 useful life unless I know a lot of information,

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1 including what the cost of electricity will be, what
2 the cost to extend that life. From an accounting
3 sense, there is no mechanism to do that.

4 Q. Are you familiar with the mechanism that
5 was used by the Commission for purposes of estimating
6 the amount of transition costs that should be
7 recovered by utilities as part of the implementation
8 of Senate Bill 3?

9 A. Vaguely.

10 Q. Are you aware that the amount of
11 transition costs that was recoverable was based upon
12 a net analysis costs that had none -- uneconomic
13 values compared to the cost above market value for
14 purposes of determining the net amount of transition
15 costs?

16 MR. RESNIK: Excuse me, just to be clear,
17 when you say "recoverable," you mean conceptually as
18 opposed to specifically recoverable by these
19 companies.

20 MR. RANDAZZO: Yes, absolutely.

21 A. Could you repeat the question? Am I

22 aware of what?

23 Q. Never mind. Now, on page 34 you talk

24 about the net regulatory assets for Monongahela Power

25 integration. If -- if you recall, did AEP pay a

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1 premium to book for the acquisition of the Mon Power
2 system in Ohio Mon Power assets?

3 A. I believe we did.

4 Q. And if you recall, was that premium
5 approximately \$10 million?

6 A. I know there was a \$10 million amount. I
7 am not sure if that was the premium. I just don't
8 recall.

9 Q. And if you know, was that -- the premium
10 whatever the amount was, was it collected from
11 customers?

12 A. No, it hasn't been collected.

13 Q. So it's your understanding that that
14 premium was not subject to collection by AEP through
15 charges that customers paid subsequent to the
16 acquisition of the Mon Power system?

17 A. No. It's my understanding it is
18 collectible. It just hasn't been collected yet, I
19 believe.

20 Q. But you have not proposed netting the
21 premium that is subject to recovery from customers
22 against the cost associated with integration?

23 A. No.

24 Q. You were good enough in your testimony to
25 give us a reference to Senate Bill 221 for purposes

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1 of recovering the costs that you described as being
2 related to the phase-in and we talked about that
3 earlier in my cross. Do you have a similar reference
4 for the early closing generating unit proposal?

5 A. No, I do not.

6 Q. And by the way, I looked through the
7 application that was filed in this proceeding and
8 maybe I missed it, but is there anything in the
9 application that was filed by AEP in this proceeding
10 that addresses cost recovery for early plant
11 closures?

12 A. I thought that was in the application.
13 Give me a moment, I'll look. I know it was in
14 Mr. Baker's testimony.

15 On page 18 of the application, section
16 Roman numeral VI.C, possible early plant closure.

17 Q. Thank you very much. And this is the
18 paragraph that would deal with fuel inventory as well
19 -- or is this the section dealing with the fuel

20 inventory portion of your proposal dealing with early
21 closures of generating units?
22 A. In my testimony I explained that a loss
23 from early closure could involve several components
24 undepreciated balance if it is an early closure,
25 unusable M&S or unit specific M&S that would not be

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1 usable at another unit and possibly lost coal that
2 gets compressed into the ground. When you get to the
3 bottom of the pile, when you dig out the pile, you
4 may find that the books show you have more coal than
5 actually exists. Those would all be losses that
6 result in closing a power plant.

7 Q. And in this section of the application it
8 indicates that in the last sentence that the
9 companies would come back to the Commission at some
10 point in time to determine the appropriate treatment.

11 A. Yes, that's the proposal.

12 Q. Okay. And, again, would that be within
13 the ESP period or could be beyond the three-year term
14 of the ESP period?

15 A. It's my understanding that this
16 application only applies to the three-year ESP
17 period, so I think we are only requesting permission
18 to defer costs if a closure occurs during that
19 three-year period.

20 MR. RANDAZZO: Okay. Thank you. That's

21 all I have. Thank you very much, Mr. Assante.

22 EXAMINER SEE: Ms. Wung.

23 MS. WUNG: Just briefly. Steal a

24 microphone.

25 - - -

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1 CROSS-EXAMINATION

2 By Ms. Wung:

3 Q. Good after, Mr. Assante.

4 A. Good afternoon.

5 Q. Grace Wung for the Commercial Group here.

6 I just have a couple of quick questions.

7 Can you turn to your Exhibit LVA-1 in

8 your direct testimony. Are you there?

9 A. Yes.

10 Q. Thank you. Is the deferred carrying
11 charge that you have listed in the line item there on
12 your chart based on assumed rate of return of
13 11.15 percent times the deferred fuel adjustment
14 clause balance?

15 A. Yes. It's 11.15 percent times the
16 unrecovered regulatory asset balance, yes.

17 Q. And the underrecovered regulatory asset
18 based on your chart, it's the line item directly
19 above the deferred carrying charge.

20 A. Well, the cumulative -- the cumulative
21 regulatory balance is the last line of the regulatory
22 asset balance.

23 Q. Right.

24 A. Last line on the chart.

25 Q. Okay. Thank you. But that line item is

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1 the correct fuel deferred adjustment for expense
2 where you have credit listed there, that's where the
3 fuel adjustment clause balance is shown on that
4 chart.

5 A. The deferred FAC expense line you are
6 referring to?

7 Q. Yes.

8 A. That does not include deferrals for
9 carrying costs and, again, as I pointed out earlier,
10 the carrying costs compounds.

11 Q. So in response to OCC's counsel you said
12 that would be -- there would be carrying charges on
13 top of the carrying SSO; is that correct?

14 A. If -- if we are owed carrying charges,
15 then we would -- as time goes on we would get the
16 carrying charge on what we are owed, yes.

17 Q. Thank you. Is it possible then,
18 Mr. Assante, that these fuel adjustment clause
19 expenses would be considered expense for income tax

20 purposes in the year they were incurred whether or
21 not they are fully recovered by fuel adjustment
22 clause revenues?

23 A. That's correct.

24 Q. And then would the deferral of the fuel
25 expense create a deferred income tax balance until

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1 the fuel cost is recovered?

2 A. That's correct, yes.

3 Q. And would that deferred income tax

4 balance provide AEP with temporary income tax

5 savings?

6 A. It would reduce our income tax.

7 Q. Yes. So that would potentially be a

8 savings for AEP.

9 A. It would -- yes, it would generate a

10 lower income tax.

11 Q. Could then the temporary tax savings be

12 used to help finance the unrecovered fuel balance as

13 a net deferred tax offset to the deferred fuel

14 balance?

15 A. No. No, that's not correct. I think you

16 are getting confused with what happens when you have

17 a traditional cost of service filing, a traditional

18 cost of service filing, which this is not, and

19 especially this fuel area because we are talking

20 about generation. Generation is not cost based. In
21 that type of a filing the deferred tax is used in the
22 computation of the cost of capital return. And if a
23 rate base -- you reduce the rate base by your
24 deferred taxes and that has the effect of reflecting
25 cost -- cost-free capital from a deferred tax in

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1 determining a cost of capital return.

2 This is not a cost of service filing, ESP
3 filing. We are not determining the return based on a
4 cost of capital rate base approach. We are
5 determining that return based on what the company
6 owns as adjusted for by the earnings test, the
7 excessive earnings test. That earnings test is not
8 based on the company's cost of capital but rather is
9 based on the return of the companies with similar
10 risks, the actual earned return of those companies so
11 it's inappropriate in my opinion to offset the cost
12 of money benefited deferred taxes in determining the
13 carrying cost.

14 When you buy a car from a car company,
15 from a car dealership, you don't compute the interest
16 after -- after his tax deduction. You compute the
17 tax on the balance owed. In this case what is owed
18 us is the FAC deferrals plus the carrying cost. So
19 it's inappropriate to do what you are suggesting.

20 Q. In your opinion it's inappropriate. Is
21 it for any tax accounting purposes inappropriate?

22 A. For what?

23 Q. For any tax accounting purposes
24 inappropriate?

25 A. It's inappropriate in the context of this

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1 filing. It's irrelevant and inappropriate in my
2 opinion.

3 Q. And that's your opinion.

4 A. That would be other people's opinion as
5 well.

6 Q. Thank you.

7 MS. WUNG: Thank you, Mr. Assante. I
8 have no further questions.

9 EXAMINER SEE: Mr. Kurtz.

10 MR. KURTZ: Thank you, your Honor.

11 - - -

12 CROSS-EXAMINATION

13 By Mr. Kurtz:

14 Q. The accumulated deferred income tax
15 balance would typically be a rate base also in a --
16 in a fully regulated environment?

17 A. In a cost-of-service filing, yes.

18 Q. And that's what would occur in the other
19 states where AEP operates?

20 A. Well, we are not subject to cost of
21 service in every state. Texas, for example, has also
22 gone through a restructuring, but in most of our
23 other states we are subject to cost-of-service
24 ratemaking, yes.

25 Q. Let me clarify. When I say AEP, I mean

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1 AEP East, the interconnection agreement affiliate
2 members, not the old central southwest, but for the
3 AEP East utilities there would be a rate base also.

4 MR. RESNIK: Your Honors, I am going to
5 object. What happens in other jurisdictions that
6 have different laws and different ratemaking is
7 irrelevant here in Ohio where we are operating under
8 Senate Bill 221.

9 EXAMINER BOJKO: I understand that, but I
10 think he is just trying to lay some foundation.

11 Please proceed.

12 Can you answer please, too?

13 THE WITNESS: Excuse me?

14 EXAMINER BOJKO: If you can answer his
15 question, please do. Do you remember the question?

16 THE WITNESS: I believe the question was,
17 is the accumulated balance deferred taxes offset
18 against rate base in determination of rates an other
19 jurisdiction in the eastern zone of AEP.

20 Q. Yes.

21 A. The answer would be in determining the
22 cost of capital return, yes, it would be.

23 Q. Has the Commission always given AEP a
24 pretax overall cost of capital with respect to
25 carrying costs on deferred balances?

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1 A. To my knowledge, they have. It's hard to
2 answer a question when you say "always." I have and
3 AEP's a lot older than I am. Thank God.

4 Q. Do you have an example where the
5 Commission recently have -- well, what's the most
6 recent deferral case involving the AEP companies here
7 in Ohio?

8 A. Well, I guess the RSP case. We had in
9 that case, we had environmental deferrals, those
10 carrying costs were not net of taxes being suggested
11 by Ms. Wung.

12 Q. They were pretax?

13 A. They were pretax, yes.

14 Q. Did the Commission -- is that the case
15 where the Commission told the companies to use the
16 Section 199 deduction in the computation of the cost?

17 A. No, that was a 4 percent case, later
18 case.

19 Q. Did you include the Section 199 tax

20 deduction for purposes of computing your carrying

21 costs here?

22 A. I don't --

23 MR. RESNIK: Again, if I can object.

24 Mr. Nelson is the sponsor of the weighted average

25 carrying charge.

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1 EXAMINER BOJKO: Hold on. If the witness
2 can answer a question, Mr. Resnik, then let's let the
3 witness answer. If the witness cannot, then I think
4 the witness should tell us that he cannot as opposed
5 to you telling us.

6 MR. RESNIK: Okay.

7 Q. In the 11.15 percent carrying charge --

8 EXAMINER BOJKO: Is there a question
9 pending?

10 MR. KURTZ: Well, yeah. I was just going
11 to restate it.

12 EXAMINER BOJKO: Oh, thank you. Okay.

13 Q. (By Mr. Kurtz) In the 11.15 percent
14 carrying charge you have in the footnote on Exhibit
15 LVA-1, does that include the Section 199 deduction;
16 if you know?

17 A. I believe it does not. I am familiar
18 with what Mr. Nelson did. I do not believe he picked
19 up that deduction.

20 Q. All right. The -- let me follow-up one
21 other area from counsel from OCC, this discussion
22 about margins or profits from off-system sales. Do
23 you remember that?

24 A. Yes.

25 Q. Okay. You indicated that in the last

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1 rate case you believed that the profits for
2 off-system sales were a base-rate offset; is that
3 correct?

4 MR. RESNIK: Excuse me, your Honor, that
5 is not what the record will reflect.

6 MR. KURTZ: That's why I am asking.

7 Q. Do you remember the question about
8 profits from off-system sales in the last rate case,
9 how were they treated?

10 A. Again, the last rate case for CSP and
11 Ohio Power, the last cost-of-service rate case that
12 involved generation was a long time ago. My
13 recollection is a little fuzzy, but I believe that
14 they were base-rate items.

15 Q. Now, when you indicated there was no
16 sharing, did you mean that 100 percent of the benefit
17 was allocated to consumers and that there was no
18 sharing in the sense of shareholders got a piece of
19 it?

20 A. I don't believe I said there was no
21 sharing. I said I did not believe there was. I was
22 not certain.

23 Q. When you said you did not believe there
24 was sharing, you don't think that shareholders got
25 100 percent. Are you saying you don't but that you

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1 think ratepayers got 100 percent?

2 A. I believe ratepayers received the entire
3 benefit, but as I said, I think it's about 15 years
4 ago and my memory is very foggy.

5 Q. Could you turn to your Exhibit 1, LVA-1.

6 A. Yes.

7 Q. I am going to ask you this, sort of
8 superimpose this a little bit over something
9 Mr. Roush did, but just looking at this exhibit,
10 the -- the deferred FAC expense for Columbus and
11 Southern is \$112 million in 2009.

12 A. Yes.

13 Q. Is that correct? I was going to ask you
14 to see if I am understanding this very simply. Do
15 you have Mr. Roush's Exhibit 1 where he shows the
16 percentage rate increase?

17 A. No, I do not. No, I do not.

18 Q. Could you turn to that, please.

19 EXAMINER BOJKO: He said he doesn't have

20 it.

21 MR. KURTZ: Oh, I am sorry. Counsel.

22 Q. Could you turn to -- well, I guess

23 counsel is getting it for you, DMR-1 page 1 of 2.

24 MR. RESNIK: Excuse me. Do you mind if I

25 look over his shoulder?

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1 A. Okay.

2 Q. If it was a decision of the Commission
3 not to allow any deferrals and to give the company
4 full recovery of what it's asked for, would the rate
5 increase in 2009 for CSP go from 238.488 million to
6 -- we would ask for the \$112 million deferral -- to
7 that giving us \$350 million rate increase?

8 A. That's correct.

9 Q. Okay. Would that yield a 19.7 percent of
10 rate increase to consumers rather than the 13.41
11 percent shown on this exhibit?

12 A. I have no idea. I don't have the
13 information to compute that.

14 Q. One, we simply divide the rate increase
15 by the current rates shown here on the Roush exhibit,
16 1.778 million.

17 A. Yes, you would. I guess I would have to
18 do that division.

19 Q. Would you accept, subject to check, that

20 it's possible a 19.2 percent -- if you have a

21 calculator, go ahead.

22 A. 19.6 is what I got.

23 Q. 19.6 percent increase; is that correct?

24 A. Yes.

25 Q. Turn to Roush Exhibit -- or page 2 of 2,

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1 the Ohio Power, do you see that the rate increase for
2 2009, 224.45 million?

3 A. Yes.

4 Q. Now, again, if the Commission were to
5 give AEP everything it's asking for but said "we
6 don't want any deferrals" -- turn back to your
7 exhibit, the deferral for fuel adjustment in 2009 is
8 300 million.

9 A. Yes.

10 Q. So then the rate increase would go from
11 224 million to 524 million; is that right?

12 A. Yes.

13 Q. Okay. Will you calculate what the first
14 year rate increase would be if the Commission denies
15 the deferral you are asking for here, but gives you
16 all the money?

17 A. Yes, I will. I got 30.3 percent.

18 Q. Okay. And you are also asking for a
19 deferral for Ohio Power in 2010 of \$139 million,

20 correct?

21 A. My example shows that, but I believe

22 Mr. Roush modified that to a data request.

23 Q. What's the right number?

24 A. From 139 to 92.

25 Q. Okay. Same point though if you were to

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1 get the 92 million in cash instead of a deferral, the
2 rate increases in 2010 would be higher than what's
3 shown on the Roush exhibit?

4 A. Yes.

5 Q. Okay. Am I right that the deferral for
6 Ohio Power in 2009 of 300 million is more than the
7 actual amount of the rate increase you are asking for
8 of 224 million?

9 A. That's correct.

10 Q. The -- the -- the deferred fuel amounts
11 or excuse me, the fuel adjustment act -- turn back to
12 your Exhibit 1, if you would, please.

13 MR. RESNIK: Are we done?

14 MR. KURTZ: Yes, I think so. Thank you.

15 Q. Okay. The base FAC revenue requirement
16 260 million in '09 for Columbus, 367 -- 367 million
17 for Ohio Power in 2009.

18 A. That's correct.

19 Q. Okay. Who gave you those numbers?

20 A. I believe Mr. Roush gave them to me, but
21 they came from -- Mr. Nelson developed those numbers.

22 Q. Do you know anything about how these
23 numbers were derived?

24 A. I reviewed Mr. Nelson's testimony. I
25 wouldn't consider myself highly knowledgeable but I

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1 have a -- some familiarity to how they were derived.

2 Q. Well, if you know, would the fuel
3 adjustment amounts be lower -- excuse me. Do these
4 fuel adjustment amounts include the 5 percent market
5 purchases at \$88 a megawatt-hour for CSP and \$85 a
6 megawatt-hour for Ohio Power that's shown on
7 Mr. Baker's Exhibit 2?

8 A. It's my understanding that those amounts
9 are included in the FAC, yes.

10 Q. Now, if the Commission were to say those
11 purchases are unreasonable or imprudent or denies
12 those purchases in some way, would the deferrals that
13 you are requesting go down?

14 A. Yes, they would.

15 Q. Okay. If the Commission were to say that
16 the profits or margins from off-system sales should
17 be included in the fuel adjustment as an off set,
18 would the deferrals you are asking for go down?

19 MR. RESNIK: And just to be sure,

20 Mr. Kurtz, we are assuming the company has gone ahead

21 and accepted the modified ESP.

22 MR. KURTZ: Well, I am assuming that the

23 Commission will order what it orders and I am not

24 assuming anything about what the company does.

25 MR. RESNIK: Well, all I am saying --

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1 your Honor, all I am saying, there may not be any

2 deferrals.

3 EXAMINER BOJKO: We all understand. We

4 all understand.

5 Q. Can you remember the question?

6 A. Can I have it repeated?

7 Q. I will rephrase. If the Commission

8 decides to -- or orders that profits from off-system

9 sales be included as a fuel adjustment charge offset,

10 would the deferrals you are asking for go down?

11 A. They may go down in 2009. They may go up

12 in 2010. It depends on whether fuel costs go up or

13 down after that point.

14 Q. But for 2009 will they go down?

15 A. I would think so, yes.

16 Q. The fuel adjustment charge includes the

17 capacity equalization payments that CSP makes to the

18 surplus members of the AEP East Interconnection

19 Agreement; is that correct?

20 A. That's my understanding.

21 Q. If the Commission said based upon

22 symmetry, or whatever reason, that the capacity

23 equalization revenues received by Ohio Power should

24 be included as a fuel adjustment charge offset, would

25 Ohio Power's deferral request go down?

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1 A. Could you repeat the question? I'm

2 sorry.

3 Q. If the capacity equalization revenues

4 were treated in the same way as the capacity

5 equalization costs, that is, included in the FAC,

6 wouldn't Ohio Power's fuel deferral go down?

7 A. I presume. I really -- I am not familiar

8 with the difference between -- I wasn't aware that

9 the revenues were included. I am not sure on that

10 and I question how to answer you.

11 Q. You are not sure if the capacity

12 equalization revenues are or are not included in the

13 fuel adjustment?

14 A. That's right.

15 Q. Assume that they are not. If they

16 were -- if those revenues were included, wouldn't the

17 deferral go down?

18 A. You know, obviously since they are a

19 credit, they should go down.

20 MR. KURTZ: Thank you, Mr. Assante.

21 Those are all my questions.

22 EXAMINER SEE: Mr. Bell?

23 MR. BELL: Thank you, your Honor.

24 I will move so that I can look at

25 Mr. Assante. Not that the reporter is not

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1 unattractive, but she is in the way.

2 - - -

3 CROSS-EXAMINATION

4 By Mr. Bell:

5 Q. We have not met before, Mr. Assante. My

6 name is Langdon Bell and I represent Ohio

7 Manufacturer's Association in this case. And please

8 bear with me. I want you to educate me because I am

9 not an accountant and I have trouble just balancing

10 my checkbook and recognizing the difference between a

11 debit and a credit. Would you accommodate me in that

12 vein?

13 A. I will do my best.

14 Q. Now, you indicate on page 1 of your

15 prefiled testimony, lines 21 and 22, you are vice

16 president of Regulatory Accounting Services for the

17 Service Corporation; correct?

18 A. That's correct.

19 Q. And you are responsible for providing

20 regulatory accounting expertise in support to the
21 Service Corporation and its operating subsidiaries.
22 A. That's correct.
23 Q. And that includes participation as
24 indicated on the top of page 2 of both you and your
25 staff in the development of regulatory strategy; is

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1 that correct?

2 A. Well, we don't develop a strategy.

3 That's done by the regulatory people, but we assist

4 them on accounting matters that are involved in

5 setting that strategy.

6 Q. I was quoting your language. You said:

7 "My staff and I participate in the development of

8 regulatory strategy," nothing more or less.

9 A. Yes, we participate, correct.

10 Q. And in that vein, do you work with and

11 report to, although I recognize you are both vice

12 presidents, Mr. Baker, who on his number --

13 unnumbered page 1 has testified that he is

14 responsible for the development and advocating of

15 public policy before regulatory agencies.

16 A. Well, Mr. Baker is a senior vice

17 president. I am a vice president.

18 Q. Oh.

19 A. I don't report to Mr. Baker. I report to

20 the controller of AEP. However, if Mr. Baker has a
21 question about accounting or accounting issue, my job
22 is to provide him with that expertise.

23 Q. Well, Mr. Baker, you worked with
24 Mr. Baker in the development of your testimony, did
25 you not?

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1 A. I developed my own testimony.

2 Q. Okay. Would you turn to page 3 -- 23 of
3 your prepared testimony, line 7, and do you not
4 indicate there and quote, "Mr. Baker has asked me to
5 testify regarding how the companies would propose to
6 account for any resultant early generating unit
7 closures and recover the resultant costs," end quote.

8 A. Yes, he asked me to testify.

9 Q. Okay. You are aware, are you not,
10 Mr. Assante, that with respect to the development of
11 the revenue authorization request of the companies in
12 this proceeding, that that revenue responsibility or
13 revenue authorization was predicated upon market
14 prices with respect to generation? Or don't you
15 know?

16 A. My only knowledge is that the company
17 determined that the ESP rates were preferable to the
18 MRO rates, which would have been a market --

19 Q. And you don't know how they determined or

20 structured their ESP rates, I take it?

21 A. No.

22 Q. You are just a vice president under the

23 service corporation on accounting.

24 MR. RESNIK: I would object to the word

25 "just."

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1 EXAMINER BOJKO: Sustained, Mr. Bell.

2 Q. I would like to learn a little bit more
3 about the Financial Accounting Standards Board and
4 its pronouncements.

5 A. Okay.

6 Q. Now, as I understand it from your
7 testimony starting on page 13, with the passage of
8 Senate Bill 3 it was determined by someone that SFAS
9 71 was no longer applicable to the generation
10 business accounting; is that correct?

11 A. That's correct.

12 Q. Who made that determination?

13 A. Back when SB 3 was passed --

14 Q. Could you speak up. I don't know whether
15 your microphone is on.

16 A. It's on. Back in 1999, I believe it was,
17 when SB 3 was passed, I consulted with our auditors
18 and made that determination.

19 Q. Okay. And that determination was not

20 challenged.

21 A. It has not been challenged.

22 Q. Okay. Now, as I understand your

23 testimony, we've gone through an evolutionary process

24 from SB 3 through Senate Bill 221; is that correct?

25 A. That's correct.

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1 Q. And it's your position, is it not, that
2 with the passage of Senate Bill 221 the generation
3 business, the generation side of the business of
4 American Electric Power is once again a cost-based
5 regulated business, it's a regulated enterprise; is
6 that not correct?

7 A. No, that's not correct. With the passage
8 of 221, if the Commission approves a fuel clause, the
9 companies' fuel purchase power operations will be
10 cost-based regulated. The rest of its generation
11 will not be.

12 Q. So that I am perfectly clear with respect
13 to your response to my last question, it is your
14 position in testimony that with the passage of Senate
15 Bill 221 that the generation side of AEP's business
16 is not regulated and it's not cost-based regulation;
17 is that correct?

18 A. When you say the generation side, are you
19 referring to fuel and purchased power?

20 Q. I am talking about everything that goes
21 into the generation business that was deregulated in
22 1999.

23 A. SB 3 does not reinstate cost-based
24 regulation of the companies generation business.
25 However, it provides for a fuel clause. If the

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1 Commission approves a fuel clause and if it's cost

2 based, then --

3 EXAMINER BOJKO: Are you talking about SB

4 221?

5 A. SB 221.

6 EXAMINER BOJKO: I think you said SB 3.

7 A. I'm sorry, SB 221. If the Commission

8 approves a fuel clause in this proceeding, then I

9 believe we will conclude with our auditors that the

10 fuel component of the generation business is cost

11 based but the rest of the generation business remains

12 noncost based.

13 Q. Okay. I will get to that in a moment,

14 Mr. Assante, and I am not suggesting with you and I

15 am just trying to educate myself because this is

16 terribly complex, and as I mentioned, I am not an

17 accountant. You do state on the bottom of page 13 of

18 your prefiled testimony beginning on lines 18 that

19 the companies -- the companies, plural -- and by

20 "companies" you mean what companies?

21 A. CSP and Ohio Power Company.

22 Q. The companies were required to cease

23 practicing regulator deferral accounting with the

24 passage of legislation that transformed them off of

25 cost-based regulation, correct?

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1 MR. RESNIK: Your Honor, I think Mr. Bell
2 misstated a fairly critical word.

3 EXAMINER BOJKO: Which page are we even
4 on?

5 MR. BELL: We are on page 13. I'm sorry,
6 I thought I read it word for word.

7 MR. RESNIK: You said "transformed"
8 instead of "transitioned."

9 MR. BELL: Transitioned, you are entirely
10 correct. Thank you for the correction. Mr. Resnik,
11 that was not intentional. I misspoke.

12 MR. RESNIK: I didn't think it was.

13 And it was on the last line, your Honor,
14 on page 13.

15 Q. And so that I understand your testimony
16 correctly, at that time it was the legislation that
17 transformed --

18 EXAMINER BOJKO: Transitioned.

19 Q. Transitioned, to me it's the same, but

20 transitioned the operating companies from regulated

21 to unregulated enterprise, correct?

22 A. That's correct.

23 Q. Okay. Now, with respect to the effect of

24 221, whatever effect that is, that's to be determined

25 by the Commission in this proceeding, are you saying

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1 that Senate Bill 221 did not -- did or did not on its
2 face have the effect of transitioning these
3 companies -- I got the right term -- transitioning
4 these companies back to cost-based regulated
5 enterprises?

6 A. Exactly what I am saying, that the
7 passage of SB 221 does not reestablish in the
8 accounting sense these companies as cost-based
9 regulated companies.

10 Q. Thank you.

11 A. For generation purposes.

12 Q. So it is your position, is it not, or
13 your request before this Commission for this
14 Commission to exercise the authority that you believe
15 it has to transition these companies from a
16 nonregulated enterprise to a regulated enterprise,
17 correct?

18 MR. RESNIK: Your Honor, I am going to
19 object. Mr. Bell is jumping between cost-based

20 regulated and just saying regulated. We're here

21 today. It's clear that we are regulated.

22 MR. BELL: I am talking about for

23 purposes of financial reporting, your Honor.

24 EXAMINER BOJKO: Okay. Let's be clear in

25 our words because I think even throughout today the

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1 witness has used both terms so I myself I am a little
2 confused what he believes, so let's both be careful
3 about the words we choose because I was wondering
4 some of these same things.

5 MR. BELL: I appreciate that and
6 apologize for misreading "transitioning" as
7 "transforming," as I think they are the same.

8 EXAMINER BOJKO: No. We are talking
9 about cost-based versus regulation.

10 Q. Do you use cost based in your testimony?
11 Do you not go from cost based to noncost-based
12 regulation?

13 A. Yes. Yes.

14 Q. Now, I will attempt to restate my last
15 question.

16 EXAMINER BOJKO: Please.

17 Q. Are you then, Mr. Assante, on behalf of
18 the companies taking the position that this
19 Commission has the authority to trans -- transition

20 the companies from their current required accounting
21 to accounting as a regulated enterprise? Can you
22 answer that question?

23 A. Under SB 221 the Commission has the
24 authority to approve a fuel adjustment clause. If
25 they approve a fuel adjustment clause, it is clearly

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1 cost based, and the one that we proposed is then the
2 companies' fuel adjust -- fuel adjustment clause
3 operations in my opinion would be -- will be cost
4 based and will return to reapplying or will reapply
5 SFAS 71 regulatory cap.

6 Q. Okay. Fair enough, and I'll explore that
7 statement in a few moments. If, in fact, these
8 companies are for purposes of a fuel adjustment
9 clause implementation and considered to be regulated
10 cost-based enterprises, they would fall under SFAS
11 71, correct?

12 A. That's correct.

13 Q. And as such, that does not in and of
14 itself qualify the companies for -- to engage in any
15 deferral accounting they choose to engage in, do
16 they -- does it?

17 A. No. SFAS 71 has certain requirements to
18 be able to record regulatory asset deferrals.

19 Q. And some of those requirements are set

20 forth in standard 6, as you testified to in your

21 prefiled testimony, correct?

22 A. In what?

23 Q. Standard 6, concept 6.

24 A. No. Concept 6 basically deals with the

25 definition of assets and liabilities. The

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1 requirements in 71 are actually within 71, paragraph
2 6 and 9.

3 Q. I stand corrected. Thank you
4 Mr. Assante.

5 Before -- before the company can, in
6 fact, create a regular -- strike that.

7 SFAS 71 allows a regulated enterprise to
8 create a regulatory asset that is not subject to
9 creation by a nonregulated enterprise, correct?

10 A. That's correct.

11 Q. And with respect to the creation of that
12 asset, does 71 require that the regulated enterprise
13 demonstrate that the asset is subject to probable
14 future recovery?

15 A. Right, that is a predominant requirement.

16 EXAMINER BOJKO: I'm sorry, Mr. Bell, you
17 cut off the witness.

18 I didn't hear. What was your response?

19 THE WITNESS: That's correct. That's the

20 predominant requirement, that it be future recovery.

21 EXAMINER BOJKO: I just didn't hear

22 "predominant."

23 Q. Would you agree with me, Mr. Assante,

24 that there are a number of factors to be considered

25 in making the judgment that, in fact, the asset is

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1 subject to future recovery -- probable recovery?

2 A. That's correct.

3 Q. Would one such factor be the magnitude of

4 the asset being created, the regulatory asset, in

5 relationship to the size of the enterprise, for

6 instance?

7 A. Well, if a regulatory asset got large

8 enough that it wasn't believable or probable that it

9 could be financed or recovered by the company, then I

10 think it would certainly question the probability of

11 the recovery.

12 Q. And would another factor, Mr. Assante, be

13 with respect to determining the probability of the

14 recovery is the size of the base from which that

15 recovery would be derived? In this case, perhaps the

16 size of the number of customers and their electric

17 consumption which would form the basis for the

18 recovery of that regulatory asset. Would you agree

19 that's a relevant factor to consider?

20 A. It would only be a factor if there was
21 a -- a very significant regulatory asset which I have
22 never seen one significant enough to raise that
23 concern but --

24 Q. Conceptually?

25 A. Conceptually if that -- if you had a huge

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1 regulatory asset compared to the companies' revenues
2 and assets, yes.

3 Q. And would the proposed period over which
4 that regulatory asset is intended to be recovered
5 also be a realistic factor to consider in determining
6 the probability of recovery of that asset?

7 A. Yes, that's a definite factor.

8 Q. You mentioned that in your prefiled
9 testimony in a discussion with your accountant; do
10 you not?

11 A. Yes.

12 Q. Now, picking up one line initiated by
13 Mr. Randazzo, ESP in this proceeding -- unless the
14 Commission enlarges it in its wisdom in the order to
15 be issued herein -- is for a three-year period,
16 correct?

17 A. That's correct.

18 Q. And the ESP will only establish the
19 recoverability or the probable recovery of that

20 regulatory asset over the next three years, correct?

21 A. That's not what we are asking for.

22 Q. I know that's not what you are asking

23 for. But with respect to the revenues that are going

24 to be established in this proceeding, they are

25 established for three years, are they not?

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1 A. We are asking them to establish rates for
2 the next three years, but I am also asking them to
3 explicitly approve a charge, a rider that will
4 recover these deferrals over the whole ten-year
5 period.

6 Q. And does your proposed rider create a
7 trust for the deposit of the funds received under
8 that FAC into the trust for the exclusive retirement
9 of the regulatory liability over those three periods
10 associated with that regulatory asset?

11 A. No, we are not requesting that.

12 Q. Thank you. So there is no real assurance
13 that whatever revenues are derived in a fuel
14 adjustment from whatever sales take place from
15 whatever customers exist over the next three years
16 will be sufficient to satisfy the deferred
17 liabilities associated with the FAC and all of the
18 other costs incurred by the company over that period
19 of time, correct?

20 MR. RESNIK: Can I have the question read

21 back, please.

22 EXAMINER BOJKO: Yes.

23 (Record read.)

24 Q. Can you answer the question as framed,

25 Mr. Assante?

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1 A. Well, unfortunately the question doesn't
2 make a lot of sense to me. Obviously if the
3 Commission approves revenues over the next three
4 years, there is no way those revenues could assure
5 recovery of a rider that would go on through 2018.

6 Q. Precisely my point. In fact,
7 Mr. Assante, we don't know after 2012 whether or not
8 these companies are going to be subject to cost-based
9 regulation, as you use that term, do we?

10 A. Well, there is a couple of factors.

11 Q. Can you answer the question and then
12 explain away however you wish?

13 MR. RESNIK: Your Honor, the witness
14 should be allowed to answer. He is saying there are
15 a couple of factors. He was about ready to state
16 what they are and then he got interrupted by
17 Mr. Bell.

18 EXAMINER BOJKO: Sustained. He was
19 starting -- let him at least answer your question.

20 MR. BELL: That's fair. Apologize. I

21 didn't mean to intentionally cut you off. I just

22 thought my question --

23 A. The first thing I would like to -- a SFAS

24 71 does not require an assurance that you get

25 recovery. It requires that it be probable that you

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1 get recovery. The word "assurance" is a much higher
2 standard than probable. Secondly, the law provides
3 for a phase-in as a tool that the Commission can use.

4 We are specifically asking the Commission
5 to provide for a phase-in rider under that law in
6 Section 4928.144 that would be nonbypassable. Since
7 it's nonbypassable by law, I think it would be very
8 unlikely that a distribution company wouldn't have
9 customers from which to recover that rider, so I
10 really have a hard time agreeing with your premise
11 that -- that there wouldn't be assurance or in my
12 judgment probably a recovery if the Commission
13 granted an explicit rider to recover those costs in
14 this proceeding, and I believe that is what we are
15 asking them to do.

16 Q. If at the end of the three-year period
17 the company were to propose another ESP and the
18 Commission were to reject it and the Commission --
19 or, excuse me, and the company were then to go to an

20 MRO, wholly market-based rate, your proposal before
21 this Commission, does it not, require that the
22 Commission is assuring, and I am using that term
23 intentionally, assuring these operating companies of
24 AEP that they will continue to recover the regulatory
25 asset for the following seven years; is that correct?

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1 MR. RESNIK: Your Honor, I am going to
2 object. The question suggested that if after the ESP
3 we went under the market rate offer, we would be at
4 entirely market-based rate. Unfortunately that's not
5 what the law provides. If we go to the MRO, we would
6 have 10 percent in the first year based on market and
7 90 percent based on the most recent standard service
8 offer, so I think the question mischaracterizes what
9 would happen.

10 MR. BELL: Well, I will accept that as
11 another alternative. That wasn't the point of my
12 question. The point of my -- if I may, I will
13 rephrase. Could I?

14 EXAMINER BOJKO: Can you just rephrase,
15 please.

16 Q. (By Mr. Bell) Would you agree,
17 Mr. Assante, that regardless at the end of the three
18 years regardless of whether or not the company
19 accepted an ESP or an MRO or what that in the -- how

20 that MRO would be structured, that the companies in
21 this proceeding today are requesting this Commission
22 to give it assurance that from the year 2012 through
23 2018 these companies will receive the deferrals that
24 were generated during the 2009 to 2011 time period?
25 Yes or no.

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1 A. Well, the answer to your question is we
2 are asking them to approve a rider that would provide
3 such assurance and that rider would be in place to
4 2018. It would give us full recovery of the deferred
5 costs that customers benefited from because that cost
6 was incurred to generate power for them to sell them
7 power and they have an obligation to pay us for those
8 costs and that they do so. And we are asking the
9 Commission to explicitly approve that.

10 Q. I will take that as a yes. Mr. Assante,
11 would it be correct that your request thus asked this
12 Commission to impose into generation -- or to affect
13 an intergenerational revenue transfer, that is, you
14 are asking from a customer or the customers that
15 exist in the time period 2012 through 2018, which may
16 not even be in the state today, may not even be
17 alive, to bear the cost that you have requested
18 customers in the period 2009 through 2011 not bear
19 during that time frame; would that be a correct

20 characterization of your proposal?

21 A. Was there a question in there? I'm

22 sorry, could you -- could I have that read back,

23 please.

24 EXAMINER BOJKO: Just a minute.

25 MR. RESNIK: Could we go off the record a

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1 minute?

2 EXAMINER BOJKO: Yes.

3 (Discussion off the record.)

4 Q. (By Mr. Bell) Would you agree,
5 Mr. Assante, ignore the last question, would you
6 agree, Mr. Assante, by deferring the recovery of
7 those revenues to a future time period, you will be
8 recovering them from a different set of customers
9 than those customers that receive the benefits?

10 A. I don't know how you define "set," but
11 there will be some customers in there that were not
12 customers at the time that the FAC costs were
13 deferred, yes.

14 Q. Thank you. Does the company propose to
15 terminate the amortization in 2018 of the unamortized
16 deferrals, FAC deferrals?

17 A. Yes. The -- we would -- if the deferrals
18 are completely recovered, we would stop the
19 amortization.

20 Q. That's not what I said. I said, would
21 the company terminate the amortization of the
22 deferrals at the end of 2018 -- terminate the
23 unamortized deferrals existing at the end of 2018?

24 A. I believe our proposal includes a trueup
25 at the end of the period and that's what I was

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1 referring to at the end of the period. If there were
2 unrecovered balance, for example, in the last year,
3 if the weather were -- were not normal, we had
4 unseasonably mild weather, we might recover enough
5 money under the rate that would be established and we
6 may have an unrecovered balance and at the end of
7 that period, that would have to be trued up and
8 recovered.

9 Q. That's -- thank you. I think you
10 answered my question.

11 On the bottom of page 9, line 15, you
12 state "The 2012 increase will remain in place through
13 the end of 2018 if nothing changes." Do you see that
14 language? And that's what you were referencing?

15 A. Yes.

16 Q. That some event could take place where at
17 the end of 2018 there would still be unamortized
18 deferrals on the books of the company and you would
19 request from this Commission in this order assurance

20 that that -- those unamortized deferrals existing on
21 the books at the end of 2018 would be recovered,
22 correct?

23 A. We are requesting to recover the entire
24 amount of deferrals plus carrying costs, correct.

25 Q. If the Commission were to allow

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1 distribution customers of -- of the operating
2 companies to bypass these deferrals, do you believe
3 that the regulatory asset could be recognized in your
4 financial reporting?

5 A. Well, I am not an attorney but the law
6 provides for this to be nonbypassable. I don't know
7 how the Commission could do that.

8 Q. I said if the Commission, it's implicit
9 in my question. If the Commission provides that
10 these deferrals can be bypassable -- and let me give
11 you an example. Let's assume I am a manufacturing
12 enterprise having no business in the state of Ohio at
13 the present time and I desire to locate within the
14 state of Ohio in 2012. I have received none of the
15 benefits associated with the regulatory asset because
16 I have not done business. I have not been consuming
17 any electricity from your operating companies. If
18 the Commission were to excuse my electricity
19 consumption from the deferral recovery that you

20 propose, do you have an opinion as to whether
21 Deloitte & Touche would say that you now have a
22 regulatory liability that must be booked? Can you
23 answer that question, Mr. Assante?
24 A. Well, it depends on a lot of facts and
25 circumstances.

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1 Q. Yes.

2 A. If we could convince Deloitte & Touche
3 that the remaining customers are more than adequate
4 to pay for the rider offer and it was probable that
5 rider would be paid off, they may allow us to do
6 that.

7 Q. Doesn't this get to the initial series of
8 questions that I asked you about, the base, the size,
9 breadth and depth of the base from which those
10 deferrals will attempt to be recovered?

11 MR. RESNIK: Your Honor, if I may object,
12 those initial questions I am assuming were based on
13 the assumption that the Commission would be following
14 the law. This last question was assuming that the
15 Commission would not follow the law. The statute
16 specifically says that the surcharge would be
17 nonbypassable. I don't see how -- how Mr. Bell can
18 connect the two.

19 EXAMINER BOJKO: Mr. Bell, are we going

20 somewhere?

21 MR. BELL: I am going onto another line

22 of questions.

23 EXAMINER BOJKO: Thank you.

24 MR. BELL: Would you follow me?

25 EXAMINER BOJKO: Yes, briefly.

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1 Q. (By Mr. Bell) I believe Mr. Kurtz's
2 examination of you covered this with respect to the
3 aggregate of the collected in the deferred charges --
4 I'll pass that line.

5 With respect to the third area of your
6 testimony, Mr. Assante, that is following up on
7 Mr. Baker's testimony that the company -- there is a
8 possibility that the generating -- companies'
9 generating units may have to be shut down early and
10 the resultant ratemaking treatment could be accorded.
11 Do you recall that line of your direct testimony?

12 A. Yes.

13 Q. And I think Mr. Randazzo inquired very
14 briefly along that line. Is it the -- your position
15 that the fact that the investment in certain
16 facilities was made during a period of time that
17 cost-based regulation was not in effect, that the
18 Commission should not apply cost-based regulation
19 existing in the future as to the treatment of those

20 assets? Do you understand the question?

21 A. I think that's not an exact

22 characterization of my position.

23 Q. Well, would you recharacterize it if

24 that's not an exact -- does that approximate your

25 position?

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1 A. No, not exactly. My position is that if
2 the plant were to experience a failure or a safety
3 issue or some environmental reason why that plant had
4 to shut down and if it was determined that it was
5 uneconomical to repair or correct the situation and
6 the plant was to close, all I am asking for is
7 authority to defer those costs. Mr. Baker indicates
8 that we would file for recovery and the Commission
9 would determine whether recovery was appropriate on
10 any regime, whether it be cost based or some other
11 regime.

12 Q. Why do you seek that determination in
13 this proceeding when such an event may or may not
14 take place sometime in the future which may be many,
15 many years out?

16 A. Well, if there was to be such an event
17 and we were to incur closing your costs, I would
18 be -- the accounting for that, whether or not
19 cost-base regulated, is to expense those costs.

20 So --

21 Q. Go ahead. I didn't mean to interrupt

22 you.

23 A. Okay. If -- and I would not have the

24 ability, since it's generation and generation is not

25 cost-based regulated under SB 221, I would not have

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1 the ability to record a regulatory asset and seek
2 Commission -- Commission approval if we believe there
3 was probable -- it was recoverable. So we are asking
4 for that authority today from the Commission.

5 Q. Even though you don't know whether or not
6 the event -- the event will ever take place?

7 A. That's correct.

8 Q. For which -- for which the accounting is
9 designed to reflect?

10 A. That's correct. It's a contingency.

11 Q. And it might take place at a point in
12 time where regulation -- where the companies'
13 revenues are established on a different basis than
14 they are in this three-year ESP proceeding?

15 MR. RESNIK: Your Honor -- I'm sorry.
16 Did you finish?

17 MR. BELL: That's it.

18 MR. RESNIK: I am going to object because
19 I think the question assumes that authority

20 Mr. Assante is testifying about is for events that
21 could occur beyond the three-year ESP. His testimony
22 is just focused on the three-year ESP period.

23 MR. BELL: I apologize. I did not get
24 that out of Mr. Assante's testimony.

25 Q. Do you state in your testimony that this

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1 covers only events within the term of the ESP,

2 Mr. Assante?

3 A. Well, I also responded to an earlier

4 question that way.

5 EXAMINER BOJKO: So the answer is yes?

6 THE WITNESS: Yes, and I believe my

7 testimony -- I believe it says that.

8 Q. I apologize.

9 EXAMINER BOJKO: And you feel you need

10 that authority now because generation isn't regulated

11 under standards as if we were in a traditional

12 cost-based regulated state, then you wouldn't need

13 the authorization today.

14 THE WITNESS: Your Honor, when you are

15 involved in regular cost-based regulations,

16 traditional regulations, the auditors accept the fact

17 that costs can be recovered in the future. If you

18 can establish probability by pointing to past

19 precedent, you can set up a regulatory asset. If you

20 can convince them that it's probable, of course, they

21 will tell you to seek recovery as soon as possible.

22 When you are on an SB 221 form of ratemaking, you

23 don't have the right to assume that anything is

24 probable in recovery because it's not cost based.

25 EXAMINER BOJKO: And your reasoning holds

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1 true even though you believe that the FAC portion of
2 the generation rate is cost based?

3 THE WITNESS: Well, this would not -- the
4 fact does not include -- would not include early
5 closure costs. If it did, then -- and if the FAC was
6 approved, then I wouldn't be requesting for this
7 authority because it would be embedded in that
8 deferral.

9 EXAMINER BOJKO: Okay. Thank you.

10 Q. (By Mr. Bell) Moving onto the last area,
11 Mr. Assante, on page 29 you address the subject of
12 M&S inventory losses as a result of a premature or
13 early closure of a generating unit including coal
14 piles or coal that's ground into the earth under the
15 coal piles. Are you not in effect requesting this
16 Commission to authorize the company to book a
17 nonexistent asset at the time the asset is being
18 booked? That is, being booked for future recovery
19 lost coal at the bottom of the coal pile that can't

20 be identified or determined until the coal pile is
21 eliminated and that loss quantified?
22 A. Well, SFAS 71 allows you to record a
23 regulatory asset. It defines a regulatory asset as
24 an incurred cost. If we were to get to the bottom of
25 the pile because the plant was closed, we certainly

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1 would remove the coal, ship it to another plant where
2 it could be burned. If we got to the bottom of the
3 pile and there was coal on the inventory record, that
4 would represent an incurred cost that we incurred at
5 some point in time and we would have the right to
6 defer that as a reg asset if it was probable recovery
7 because it represents an incurred cost. That's the
8 definition of a reg asset. It doesn't have to be an
9 asset. It has to be an incurred cost that's probable
10 future recovery and that's what makes it an asset.

11 Q. You are again providing your
12 interpretation, and I am not going to argue with you
13 on your interpretation of Senate Bill 221. I was
14 simply asking what the effect of your proposal was.
15 Can you answer that question that you are requesting
16 authorization from this Commission to book as an
17 asset something that really doesn't exist, physically
18 exist, and can't be measured in any event until the
19 coal pile is eliminated sometime in the future?

20 A. I am asking for authorization to record
21 an expense or an incurred cost that does exist. It
22 was a cost we incurred to purchase coal. It does
23 exist. It's on our books. And it's probable
24 recovery that becomes an asset, a regulatory asset.
25 MR. BELL: Thank you. That's all I have.

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1 EXAMINER BOJKO: Thank you.

2 Mr. Yurick.

3 MR. YURICK: No questions, your Honor.

4 Thank you.

5 EXAMINER SEE: Mr. Margard.

6 MR. MARGARD: Thank you, your Honor. And

7 just a couple of questions.

8 - - -

9 CROSS-EXAMINATION

10 By Mr. Margard:

11 Q. Good afternoon, Mr. Assante.

12 A. Good afternoon.

13 Q. Have you had an opportunity to read Staff

14 Witness Siegfried's testimony?

15 A. No, I did not. I don't believe I read

16 his testimony.

17 Q. Is my understanding that the companies'

18 alternative energy resource costs are to be included

19 as part of the FAC; is that your understanding?

20 A. Yes.

21 Q. And it's my understanding that it's the
22 companies' position that none of those costs would be
23 included as part of the phase-in rider. Is that your
24 understanding as well?

25 A. It's my understanding that we made a

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1 commitment in the data requests response I believe it
2 was that in order to comply with the law that we
3 would -- we would include that in the part of the FAC
4 that is recovered through a bypassable FAC rider.

5 Q. Now, I just wanted to make sure that I
6 understood that was your position, and you are
7 adopting that commitment as part of your testimony
8 today.

9 A. The -- the company took that position in
10 answer to a data request, and I certainly adopt it.

11 MR. MARGARD: That's all I needed.

12 Thank you, your Honor.

13 EXAMINER BOJKO: So the answer is it
14 wouldn't be part of the phase in? I don't think I
15 heard.

16 THE WITNESS: It would not get into the
17 phase-in deferrals. It would be included in the part
18 of the FAC that was recoverable.

19 EXAMINER BOJKO: Thank you. I didn't get

20 that last connection.

21 MR. MARGARD: That's all I have. Thank

22 you.

23 EXAMINER SEE: Any redirect?

24 MR. RESNIK: No redirect, your Honor. At

25 this time -- unless there are questions from the

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1 Bench.

2 - - -

3

4 EXAMINATION

5 By Examiner Bojko:

6 Q. I'm sorry, do you have -- Mr. Assante,

7 could you turn to page 6 quickly. We will go through

8 this. On line 15 you use the word that "whenever

9 it's necessary Mr. Roush will adjust the incremental

10 FAC cost deferrals." What exactly does "whenever

11 it's necessary" mean? On a daily, monthly,

12 quarterly? When would he look at that and make that

13 kind of adjustment?

14 A. I would believe he would do it quarterly.

15 I really don't know what period he would use, but it

16 certainly would be more than monthly. We don't -- we

17 don't account for things daily or weekly.

18 Q. Could you turn to page 30 -- well, I

19 guess the line of questioning about the Mon Power

20 integration cost again on page 34. But on the top of
21 page 35, line 2, you talk about additional deferrals
22 that will continue for integration costs. And you
23 specifically state on page 34 the itemized list of
24 net reg assets and liabilities that were transferred,
25 but what are you referring to when you talk about

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1 additional deferrals?

2 A. Well, when we acquired Mon Power, we had
3 no O&M costs for that situation. We were not
4 servicing that service territory so we had to hire
5 employees. We purchased trucks. So we have
6 operation and maintenance costs to service the Mon
7 Power service territory. Those costs are not built
8 into our rates and we are deferring those costs as
9 part of this deferral for future recovery.

10 Q. So the O&M costs would be what you would
11 see would be continued additional deferrals?

12 A. Yes, plus there is a carrying cost that
13 continues.

14 Q. And then does that explain on page 36
15 your chart it looks like the actual balances of
16 June 30, 2008, for the Mon Power costs are 8 1/2
17 million but then if you look at the projected for
18 2010, they go up to about 13 1/2 million.

19 A. That's made up of the O&M and the

20 carrying costs, yes.

21 Q. But all of the identified reg assets and
22 liabilities listed on page 34 would end, I would
23 assume, I guess at the end of 2008?

24 A. The only one I know that has a 2008
25 termination date as far as deferrals would be the

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1 line extension. I believe that ends December 31,
2 2008. We are proposing to extend that. We have a
3 witness who's proposing to extend that deferral but
4 the order in 2002 provided for the December 31, 2008,
5 termination date for those deferrals.

6 Q. And I guess maybe this is for Mr. Earl
7 but --

8 A. Yes.

9 Q. You are proposing to extend not only the
10 AEP line extension costs but you are proposing to
11 extend the one specific to Mon Power; is that what
12 you just said to me?

13 A. No, no. The line extension cost is not
14 directly related to Mon Power. I mean, there may be
15 a customer there that has a line extension and we
16 would defer those costs but that's a different
17 deferral.

18 EXAMINER BOJKO: Okay. That's what I was
19 asking. Okay.

20 Thank you. That's all I have.

21 THE WITNESS: You're welcome.

22 MR. RESNIK: Your Honor, the companies

23 move for the admission of Companies' Exhibit 6.

24 EXAMINER SEE: Are there any objections

25 to the admission of Exhibit 6 -- Companies' Exhibit

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1 6?

2 Hearing none, Companies Exhibit 6 is
3 admitted into the record.

4 (EXHIBIT ADMITTED INTO EVIDENCE.)

5 MR. RESNIK: Thank you.

6 EXAMINER SEE: Let's take a 15-minute
7 recess.

8 (Recess taken.)

9 EXAMINER BOJKO: Let's go back on the
10 record.

11 OCC, are you ready to call your next
12 witness?

13 MS. GRADY: Yes, your Honor.

14 OCC calls Wilson Gonzalez to the stand.

15 EXAMINER BOJKO: Let's go off the record.

16 (Discussion off the record.)

17 EXAMINER BOJKO: Let's go back on the
18 record.

19 - - -

20 WILSON GONZALEZ

21 being first duly sworn, as prescribed by law, was

22 examined and testified as follows:

23 DIRECT EXAMINATION

24 By Ms. Grady:

25 Q. Good afternoon, Mr. Gonzalez.

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1 A. Good afternoon.

2 Q. Can you state your name and business
3 address for the record, please.

4 A. Yes, my name is Wilson Gonzalez, 10 West
5 Broad Street, Columbus, Ohio 43215.

6 Q. For purposes of this proceeding, by whom
7 are you employed and in what capacity?

8 A. I am employed by the office of the Ohio
9 Consumers' Counsel.

10 MS. GRADY: Your Honor, at this time I
11 would like to mark for identification purposes as OCC
12 Exhibit No. 5 the direct testimony of Wilson Gonzalez
13 filed October 31, 2008.

14 EXAMINER SEE: The exhibit is so marked.

15 (EXHIBIT MARKED FOR IDENTIFICATION.)

16 MS. GRADY: May I approach?

17 EXAMINER SEE: Yes.

18 THE WITNESS: Maureen, I wanted to make
19 one correction.

20 MS. GRADY: Yes.

21 Q. Now, Mr. Gonzalez, can you identify that
22 document for me, please?

23 A. The document is the direct testimony of
24 Wilson Gonzalez.

25 Q. Mr. Gonzalez, can you speak up? I am

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1 having a little bit -- or even maybe move the
2 microphone closer.

3 A. Yes.

4 Q. And could you restate what you just said?

5 A. The direct testimony of Wilson Gonzalez.

6 Q. Now, this document was filed -- or was
7 this document prepared by you or under your direct
8 supervision?

9 A. Yes, it was.

10 Q. And if I were to ask you today the
11 questions that are posed in this document, would your
12 answers be the same?

13 A. Yes, they would.

14 Q. Now, do you have any additions,
15 corrections, or deletions to this testimony?

16 A. Yes. Subject to one correction on page
17 9, line 13, the No. "175" should read "150."

18 Q. So that bullet should read "Any program
19 serving populations above the 150 percent to the

20 poverty line?"

21 A. That's correct.

22 Q. Subject to that correction, if I were to

23 ask you today whether your answers -- if I were to

24 ask you today, posing these questions, would your

25 answers be the same?

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1 A. Yes, they would.

2 MS. GRADY: Your Honor, at this time I
3 offer Mr. Gonzalez for cross-examination, and I move
4 for the admission of OCC Exhibit No. 5 subject to
5 cross.

6 EXAMINER SEE: Okay. Ready to go,
7 Mr. Yurick?

8 MR. YURICK: No questions of this
9 witness. Thank you, your Honor.

10 EXAMINER SEE: Okay. Mr. Bell.

11 MR. BELL: No questions, your Honor.

12 MR. RANDAZZO: No questions.

13 EXAMINER SEE: Mr. Kurtz.

14 MR. KURTZ: No questions, your Honor.

15 EXAMINER SEE: Ms. Wung.

16 MS. WUNG: No questions.

17 EXAMINER SEE: Mr. Randazzo.

18 MR. RANDAZZO: Still no questions.

19 EXAMINER SEE: Ms. Elder.

20 MS. ELDER: No questions, your Honor.

21 EXAMINER SEE: Mr. O'Brien.

22 MR. O'BRIEN: No questions, your Honor.

23 EXAMINER SEE: Mr. Maskovyak.

24 MR. MASKOVYAK: I'm sorry, I am going to

25 break the string, but it should be brief.

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1 EXAMINER SEE: Okay.

2 - - -

3 CROSS-EXAMINATION

4 By Mr. Maskovyak:

5 Q. Good afternoon, Mr. Gonzalez. I would

6 like you -- to take you to page 9 of your testimony.

7 And I am looking at the first bullet point on line 8

8 through line 10 where you talk about the AEP --

9 AEP-Ohio proposed comprehensive home performance

10 program audit that's currently targeted for low

11 income OCC customer -- or, yeah, low income customers

12 and you recommend that a program be made available to

13 all residential residents. Are you recommending to

14 take or reduce the amount of funding that is

15 currently going to be targeted to low income

16 customers and spreading that same dollar amount to

17 nonlow income customers or are you recommending

18 expanding the program and dollar amounts to include

19 nonlow income customers?

20 A. I don't think I am asking for low income
21 programs to be reduced, in effect, it seems that the
22 company has made at least a commitment to increase
23 the low income budgets, you know, based on 50 percent
24 of 75 million. And there is a question here that
25 perhaps the company may be able to offer that type of

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1 program as a -- one of their standard service offer

2 programs, so it's unclear.

3 Q. But from your standpoint, you are not

4 recommending that they take dollars currently

5 targeted for low income customers and spread them out

6 to nonlow income customers for the same purpose?

7 A. No.

8 MR. MASKOVYAK: Okay. Thank you. That's

9 all I have, your Honor.

10 EXAMINER SEE: Who for the company is

11 conducting? Mr. Nourse.

12 MR. NOURSE: Thank you, your Honor.

13 - - -

14 CROSS-EXAMINATION

15 By Mr. Nourse:

16 Q. Good afternoon, Mr. Gonzalez.

17 A. Good afternoon, Mr. Nourse.

18 Q. You state in your testimony on page 4 in

19 a footnote that when you use the term DSM, you are

20 also including energy efficiency, correct?

21 A. That's -- DSM is a broader term.

22 Q. And I just want to point out for the

23 record when we discuss and you respond in the context

24 of your testimony that you are also including energy

25 efficiency when you talk about DSM, correct?

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1 A. That's correct.

2 Q. Okay. Now, on page 5 of your testimony,
3 next page, you refer to the estimates from AEP
4 operating companies, especially in Texas. Do you see
5 that?

6 A. Yes, I do.

7 Q. Now, you view that as a positive, the
8 fact that AEP has experience with other affiliate
9 companies with demand-side management?

10 A. Yes. I see that as a positive and I
11 think Ohio could benefit from some of the program
12 development that's taking place in those particular
13 territories.

14 Q. Now, you indicate, and I am on page 6
15 now, that there is approximately 178 million proposed
16 by the companies during the ESP period for DSM,
17 correct?

18 A. That's what was in Witness Sloneker's
19 testimony, yes.

20 Q. And then you conclude starting at the
21 bottom of page 6 that the fund -- level of funding
22 which refers to the 178 million, I believe, is at a
23 level that should allow AEP to be successful in
24 implementing the standards under 221; is that
25 correct?

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1 A. Yeah. As I state, generally speaking,
2 yes.

3 Q. Yeah. What did you mean though, that
4 level of funding should allow AEP-Ohio to be
5 successful under the standards?

6 A. It was -- during the ESP periods all the
7 companies, all three companies, to date have filed
8 demand -- programs to meet the benchmarks of Senate
9 Bill 221. Some companies in my belief have proposals
10 I think -- I find lacking so.

11 Q. Well, I guess my question is that the
12 standards are not to spend a certain amount of money,
13 correct?

14 A. That's correct.

15 Q. Okay. So are you saying that you believe
16 that those programs involved with the companies'
17 proposal, that the impact or the attainment that
18 would be achieved by those programs is commensurate
19 with the benchmarks in the statute?

20 A. Again, generally speaking, it's in the

21 ballpark. It's in the range.

22 Q. Okay. Now, also on page 7 in the middle

23 of the page there, you are referring to Company

24 Witness Castle and stating a -- an assumption that he

25 made about 50 percent implementation. Do you see

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1 that discussion?

2 A. Yes.

3 Q. Okay. And I wanted to try to clarify
4 that and since he hasn't testified, I wanted to ask
5 you if -- to try to help clarify that. First of all,
6 are you interpreting Mr. Castle's statements that you
7 are citing there as somehow modifying the statutory
8 benchmarks for DSM?

9 A. I think -- when I first read it, I think
10 that was my initial inclination. And that's why I
11 used the word "appears" because when he talks about
12 a -- he differentiates between a program year and a
13 calendar year.

14 Q. And let me just -- I will ask you to
15 assume that he meant certain things about that if I
16 could and your counsel can follow-up on this later if
17 they would like, but if Mr. Castle was using the
18 50 percent assumption to say that -- to recognize
19 that throughout the course of the year, any given

20 calendar year, company would be implementing programs

21 and rolling them out some period throughout the year,

22 not all on January 1 of every year, is that a fair

23 assumption?

24 A. Yes.

25 Q. So with that in mind, 50 percent

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1 attainment throughout the course of the year would
2 basically say the effect would be that you would have
3 started some during the year and that you would have
4 had some in place for almost the whole year and some
5 for a short period within the year; does that make
6 sense?

7 A. Yes, it does.

8 Q. Okay. And if under your understanding of
9 the benchmarks contained in Senate Bill 221 for DSM,
10 for example, let me pick energy efficiency as an
11 example illustration here, if by the end of 2009
12 AEP -- that the AEP companies individually for this
13 purpose have -- have achieved .3 percent of energy
14 efficiency, energy reductions, would that be your
15 understanding of compliance?

16 A. Yes, it would.

17 Q. Thank you. Now, the next topic you raise
18 in your testimony starting on the bottom of page 7,
19 you are discussing the administrative costs as a

20 percentage of the program costs, and you express some

21 concerns about that, correct?

22 A. Yes.

23 Q. About the level, okay. Now, first of

24 all, would you recognize or agree that there would be

25 a difference in that measure, administrative costs as

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1 a percentage of program costs, for during a ramp-up
2 period or when a company would be aggressively
3 rolling out DSM programs?

4 A. There could be. I think the way the
5 benchmarks were set, they were set to ramp up slowly
6 before you got to real aggressive programs so.

7 Q. Well, they may be smooth but would you
8 agree that the benchmarks in the statute are
9 aggressive?

10 A. I think they become aggressive when you
11 start looking at a 1 percent per year. But I think
12 starting off I think it's appropriate -- it's at a
13 level, for example, we had with the Duke program in
14 2007, last year.

15 Q. Okay. Well, recognizing that, to get to
16 .3 percent energy efficiency, energy reduction by the
17 end of 2009, there -- for AEP-Ohio and your
18 understanding of the companies' programs, there is a
19 period of significant ramp up for the companies to

20 achieve; is that correct?

21 A. I think there is some, you know, ramping
22 up. As you mentioned earlier, I think the benefit
23 you have is from being a multi-state utility and
24 having resources at the corporate level that deal
25 with energy efficiency in different states. I think

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1 that helps -- that's a benefit you bring to Ohio, so
2 I would think that would lower your costs as opposed
3 to a stand-alone utility starting from day one.

4 Q. Well, fair enough. In terms of starting
5 up the program in a particular company, you know, in
6 the state of Ohio for Columbus Southern Power and
7 Ohio Power, even with that experience that AEP has,
8 my question is simply would you recognize a
9 distinction in the level of administrative charges as
10 a function of program costs between a start-up
11 program and one that's been in place, let's say, for
12 several years?

13 A. It could be. I have seen -- I have seen
14 it go either way.

15 Q. Go either way?

16 A. Yeah. I have seen, for example, in the
17 Columbia case they've -- they had a warm choice
18 program. They had a certain level of administrative
19 costs. They proposed new programs coming out of

20 their latest filing and some of their programs had
21 lower administrative costs than the existing program,
22 so it varies case by case but it --

23 Q. Does Columbia have benchmarks they have
24 to comply with for DSM?

25 A. Yes, they do as part of a stipulation.

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1 Q. Okay. But not as part of a statutory
2 requirement?

3 A. That's correct.

4 Q. Now, would you -- would you also or would
5 you agree that the -- as you said, the administrative
6 costs vary, so depending on the type of program, the
7 nature of the program, what measures might be
8 included in that program, in other words, comparing
9 different types of programs, administrative costs
10 vary across different types of programs?

11 A. Yeah, I would agree -- I would agree to
12 that. In effect, what my recommendation is that we
13 kind of pick a number in terms of or percentage as
14 to -- just to pick a percentage and then I am given
15 discretion to -- you know, I understand that may
16 happen and if a program has higher administrative
17 costs because of, you know, XYZ reasons, you know,
18 then we talk about it and we approve it. In fact, in
19 Columbia that's just what happened, went around the

20 table, talked about a number of programs. We
21 developed them in sync. We were online in terms of
22 we understood what the program was going to do, what
23 it was going to take to deliver the energy
24 efficiency, so when it came to the programs that --
25 that exceeded the -- we had a 20 percent threshold in

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1 Columbia. The collaborative was fine with it, so it
2 wasn't an issue, almost like a radar.

3 Q. Okay. So I think what you are saying,
4 the collaborative -- first of all, AEP-Ohio is
5 proposing to -- in fact, has already formulated a
6 collaborative that OCC and yourself personally are
7 involved in; is that accurate?

8 A. Yes.

9 Q. And is it your understanding that issues
10 such as the direction and the future plans and
11 addressing matters such as administrative costs and
12 advertising, consumer educational efforts, all those
13 things would be subjects that the collaborative would
14 meet and discuss and provide input to the company on?

15 A. Yes.

16 Q. So if the collaborative had, through
17 people like yourself, had ideas and input that helped
18 reduce the administrative costs as a function of the
19 program costs, is that something the collaborative

20 could have a positive impact and address the concern

21 you have?

22 A. Yes. I think so. In fact, I think two

23 of the collaborative members have also in their

24 testimony noted that they feel the cost -- the

25 administrative costs are so -- are high so I am sure

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1 that will be one of the topics of discussion at the
2 collaborative.

3 Q. Now, is it your understanding that if
4 that were to be the case and administrative costs
5 that are projected by Ms. Sloneker's testimony turned
6 out to be higher than the actual costs that the
7 companies EEDR rider would reconcile that and trueup
8 to the actual costs that are incurred?

9 A. I believe that's what's in Mr. Roush's
10 testimony.

11 Q. Yeah. What I am asking you is if the --
12 if the collaborative has this in your view positive
13 impact reducing administrative costs as a function of
14 program costs and that lowers the administrative
15 costs that are incurred by the companies, would that
16 not be recovered -- reconciled and reflected in the
17 EEDR rider, the lower level administrative costs?

18 A. I'm not sure of that.

19 Q. Is it your understanding that the

20 companies will be recovering costs in the rider as

21 projected without any reconciliation?

22 MS. GRADY: Objection.

23 EXAMINER SEE: What's your basis?

24 MS. GRADY: Your Honor, I think that this

25 is well beyond the scope of Mr. Wilson -- on

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1 Mr. Gonzalez's testimony. I don't believe that
2 he's -- he indicated earlier that he is not sure how
3 the EEDR works and this is another question right
4 along those lines in a different manner or form.

5 MR. NOURSE: Well, your Honor, I think he
6 indicated he was familiar with -- Mr. Roush had
7 addressed the rider. All I was asking him whether --
8 to address his concern that he raises in his
9 testimony, whether the reconciliation process would
10 help. I can ask him to assume that. If you would
11 like, I can rephrase that.

12 EXAMINER SEE: Please do.

13 Q. So, Mr. Gonzalez, assuming that the EEDR
14 rider is as proposed by Mr. Roush, that it would be
15 reconciled so that actual costs that are incurred are
16 what the company ultimately is able to recover from
17 customers, with that assumption, can you answer my
18 prior question about whether that addresses your
19 concern about administrative costs?

20 A. Yeah. I think that would go away
21 towards it but, again, it depends on I don't know if
22 the rider has, for example, carrying costs on over-
23 or undercharges, and if it's going to -- if it's an
24 asymmetrical type of proposition where it could be
25 over and under on equal property, then I probably

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1 would have less of a problem.

2 Q. Okay. Thank you. I would like to
3 discuss your recommendations on page 9 of your
4 testimony. First of all, in line 7 you say those
5 listen are preliminary recommendations. What did you
6 mean by that?

7 A. Well, these are recommendations I
8 recognize we're going to be discussing in a
9 collaborative process and subject to further
10 discussion so those are my early observations based
11 on what I read in Mrs. Sloneker's testimony.

12 Q. Okay. So -- but those are your
13 recommendations as they stand today in this case.

14 A. That's correct.

15 Q. On behalf of OCC?

16 A. That's correct.

17 Q. And one thing I didn't see here I want to
18 ask you about your position. Is it your position
19 that AEP-Ohio given what you said earlier about

20 the -- about the appropriate level of funding to meet
21 the mandates, that the companies should proceed with
22 implementing and starting the programs that they've
23 proposed and subject to ongoing review and input
24 rather from the collaborative that they should move
25 forward now -- and let me stop there and I will break

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1 it up.

2 A. Well, I think -- I would like to see
3 before we move forward we just have estimates from
4 Texas. We would like -- and as a statement in my
5 testimony, I would like to see some of that refined.
6 We would like to see some of the costs in terms of
7 administrative costs broken up in terms of how much
8 is going into O&M and how much it going into
9 training, so I made other recommendations but subject
10 to going through that process and getting the
11 information getting to a comfort level with the
12 group.

13 Q. Okay. Well, you are not suggesting that
14 the companies wait until all those issues are
15 resolved through the collaborative process to begin
16 activity to meet the mandates that are required under
17 Senate Bill 221, are you?

18 A. I believe my -- the requests I just made
19 could be resolved within December or something. You

20 know, it's getting the information and looking at I
21 guess the companies' -- propose a market potential
22 study or market assessment study and once we get all
23 that information I think -- I mean, the programs you
24 propose are programs that are being undertaken in
25 other jurisdictions. I am very familiar with many of

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1 them so there is nothing in there that is -- besides
2 the recommendations I made that I would find
3 objectionable. In effect, the standard service offer
4 is something that I recommended in other proceedings
5 so.

6 Q. Well, my question to you -- unfortunately
7 we are not going to be able to come back and do this
8 again in this proceeding, at least where you can come
9 back and update your testimony necessarily and
10 perhaps give the Commission some sort of supplemental
11 recommendation. So I am asking you as we sit here
12 today that whether it's your position that the
13 company, that you agree based on what you know
14 sitting here today, that the company should proceed
15 and receive cost recovery for the beginning of those
16 activities subject to ongoing input from the
17 collaborative?

18 A. Then I would say subject to the
19 recommendations that I made in my testimony.

20 Q. Okay. And fair enough. And that's what
21 I wanted to get to next. With respect to bullet No.
22 1, Expanding the Home Performance, home diagnostic
23 audit and incentive program for low income customers,
24 you are recommending that that be expanded for all
25 residential customers, correct?

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1 A. Yeah. I want to see that type of program
2 offered to all customers, and like I answered with
3 Mr. Maskovyak, if the company was planning to do that
4 through its standard service offer, that's fine. I
5 just want to make sure that type of program is
6 offered to all residential customers, not just low
7 income.

8 Q. Well, in response to Mr. Maskovyak, you
9 had indicated that programs, it would be funded
10 through the \$75 million Partnership fund proposal I
11 believe; is that correct?

12 A. I said that type of funding was part of
13 the case and in play. It's not clear how it's going
14 to be utilized or whatever.

15 Q. Okay. But I guess the -- first of all,
16 would this expansion be subject to cost-effective
17 screening or satisfying cost-effectiveness criteria?

18 A. Yes. And I think I answered that way in
19 some of your discovery.

20 Q. Well, that's fine, but we have to make a
21 record here today so I have to ask you some of those
22 same questions.

23 Okay. So that's helpful, Mr. Gonzalez?

24 Your point is either the funding for that expansion
25 if it occurs would be either through the EEDR rider

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1 or would count toward a portion of the 75 million

2 Partnership fund proposal.

3 A. That's correct.

4 Q. Okay. With respect to your second bullet

5 you talk about joining up with Columbia Gas of Ohio

6 to do a one-stop shop home performance program. Now,

7 you say "implement" there on line 11. Are you really

8 saying that the collaborative should consider

9 implementing and discussing undertaking that type of

10 effort?

11 A. It will be subject to the -- of the

12 collaborative but the company Columbia Gas would have

13 to open up discussions and work to that.

14 Q. I mean, in terms of you said earlier your

15 overarching recommendation was dependent on these

16 recommendations, so I wanted to try to be clear. You

17 are recommending -- you say implement but I gather,

18 correct me if I am wrong, you meant that the

19 collaborative and the company should consider

20 implementing.

21 A. Yes. And I believe yesterday Witness

22 Sloneker agreed that it would probably make for a

23 more efficient delivery mechanism and it is something

24 the company was willing to pursue.

25 Q. Okay. Thank you. Your next bullet is

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1 about the 150 -- you changed it to 150 percent of

2 poverty line; is that correct?

3 A. Yes, that's correct.

4 Q. Now, when you talk about "competitively

5 bidding out those programs," I gather this applies to

6 any -- any programs serving the populations above

7 150 percent poverty level, correct?

8 A. Yes.

9 Q. Can you just explain what you mean when

10 you say "competitively bid out," how that would work.

11 A. Yeah. If you were going to have a

12 program of that type, let's say, say home performance

13 type program, you would -- you would -- you would

14 have an RFP and there are a number of companies or

15 energy service companies that undertake that. There

16 is an infrastructure of low income weatherization

17 providers in Ohio and you would just open it up and

18 let everybody, you know, all the groups that are

19 interested to -- to respond to the RFP and through

20 that mechanism we would hope to have competitive
21 pricing, discipline pricing for those types of
22 programs.

23 Q. Okay, okay. Now, 150 percent is -- is
24 sort of the floor, if you will. is there a ceiling on
25 how high the -- when you talk about a sliding scale

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1 -- just trying to figure out how this would work and

2 whether it starts at 150 percent. Does it end

3 somewhere else, or is it open ended at the top?

4 A. Well, for -- for the second stage low

5 income program when I think witness -- Witness

6 Hamrock mentioned yesterday you are looking to target

7 some of that move for the people above.

8 Q. The right --

9 A. I know at Columbia Gas there has been a

10 similar program they went up to 180 -- I'm sorry,

11 80 percent of the average median income in accounting

12 so that was their -- if you were within -- below

13 80 percent of the average median income in

14 accounting, you would be eligible -- you would only

15 have to pay 10 percent of any measured costs for that

16 particular program so that was one configuration that

17 they -- that they made so that would be the upper

18 limit. Anything above that would -- would be part of

19 a regular program where your regular incentive levels

20 so on and so forth would take place.

21 Q. Okay. And the sliding scale in between

22 those two would basically give more or less --

23 A. Yes.

24 Q. -- assistance based on the income level.

25 Now, you say that was one option. Again, in terms of

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1 trying to be clear about your recommendation, you say
2 incorporate a sliding scale payment. Again, you are
3 not saying it has to be just like Columbia but you
4 are saying this concept is something you would like
5 to see?

6 A. Concept, yes.

7 Q. Considered by the collaborative and the
8 company?

9 A. That's correct.

10 Q. Okay. Thank you.

11 A. I am trying to make it, if you do go in
12 that direction to work with Columbia's program, I am
13 trying to make it easier down the road when you start
14 talking about program elements.

15 Q. Okay. Thank you. A couple -- a couple
16 areas left here. First area is on page 10 and
17 starting on line 9 you indicate you have been
18 informed by counsel that generation efficiency
19 projects are not eligible to count toward efficiency

20 standard by Ohio law, only transmission and
21 distribution efficiency improvements. Do you see
22 that?

23 A. Yes, I do.

24 Q. So, you know, obviously I think you are
25 being clear here, you are not offering a legal

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1 opinion, correct?

2 A. That's correct.

3 Q. You are just relaying what counsel has
4 indicated to you on that subject, correct?

5 A. I mean, I have read the bill and I had --
6 I have my understanding of the bill and I have talked
7 to counsel. Counsel has reaffirmed it, I believe.

8 Q. So you read the bill and you cite
9 66(A)(2)(d) in the footnote.

10 A. That's correct, yes.

11 Q. Does that statute indicate that only T&D
12 improvements are eligible?

13 A. That's my understanding.

14 Q. It includes the only concept, or does it
15 just list those as being eligible?

16 A. It lists those as being eligible. The
17 part of the energy efficiency 4828 -- 4928.66 which
18 is where the benchmarks reside as opposed to the
19 advanced energy standard.

20 Q. I understand. I was talking about

21 66(A)(2)(d).

22 A. Okay.

23 Q. And you are not -- you are not aware that

24 it says the word "only" or has that only concept in

25 the language; is that correct?

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1 A. I don't have it in front of me.

2 Q. Okay. If for whatever reason that legal
3 conclusion were incorrect as a policy matter given
4 your expertise in energy efficiency and demand-side
5 management, is there any reason that generation
6 efficiency projects would not be counted as a policy
7 matter or a philosophical conceptual matter?

8 A. I believe we are going to need efficiency
9 from all areas moving forward so depending on how the
10 legal, you know, whatever comes out of -- I don't
11 know if that's -- if that issue is specifically
12 addressed in the rulemaking that's pending.

13 Q. Well, I am just asking you for the
14 purpose of that question to not premise your answer
15 on a legal conclusion and just tell me your -- your
16 -- as an energy efficiency demand-side management
17 expert and representative of residential customers
18 whether you believe generation efficiency
19 improvements would be included in energy efficiency.

20 A. I would say if they were included, I
21 would have -- I would have believed the benchmarks
22 should have been higher because generation
23 improvements can really come in big amounts.

24 Q. Okay. Let me also ask you then -- final
25 subject, Mr. Gonzalez. The recommendation at the

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1 bottom of page 10 for -- you are recommending that a
2 standard REC purchase contract be implemented,
3 correct?

4 A. Yes.

5 Q. And in particular what I -- well, I have
6 got a few questions about that. I want to talk about
7 the pricing that you indicate that the - basically
8 you say based on a percentage of the alternative
9 compliance provisions 4928.64(C)(2)(a) and (b). Can
10 you explain in your own terms how -- what you mean by
11 that?

12 A. Yes. I wanted to distinguish the pricing
13 of such a program from the 4928 AEP pricing program.

14 Q. I'm sorry, Mr. Gonzalez, could you repeat
15 your answer?

16 A. Yeah. I reference the Senate Bill 221
17 because I want to differentiate what the program
18 would be to differentiate it from AEP's existing
19 green pricing program, in that I believe that a REC

20 program for that -- a REC -- the Senate Bill 221
21 requirements of 50 percent in-house or in-state
22 renewable plus the other 50 percent has to be
23 delivered into the state, however, that particular
24 language is finalized in the pending legislation. I
25 believe the price of the REC would be higher than

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1 what the AEP green pricing would be so I was trying
2 to draw that differentiation.

3 Q. Okay. Well, without comparing it to the
4 green pricing tariff, what I am asking you is what
5 you meant by in line 20 "based on a percentage of the
6 Alternative Compliance provisions" and that statute.

7 A. Again, I think in -- in discovery -- I am
8 in agreement that it should be a market set price.
9 Okay? And if you look at that provision of the bill
10 especially with respect to solar, it is sort of
11 mimics -- tries to mimic a market price in that it is
12 -- for solar it starts at \$50, the alternative
13 compliance payment, and then keeps going down, in the
14 expectation that competition and so on will drive the
15 prices down.

16 Q. Well, okay. You may be attributing that
17 to mimicking market, but regardless of the intent I
18 guess I am trying to figure out why that -- why you
19 would recommend that the price under that contract be

20 equal to the price the company would pay for

21 noncompliance essentially the penalty for enforcing

22 the statute --

23 A. I am not saying that, I am not saying it

24 should be equal. I just said usually in the lexicon

25 of the developers in places that have mandatory, you

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1 know, renewable portfolio standards, they usually
2 take whatever the price is. They say, well, it is
3 this percentage of the ACP, of the alternative
4 compliance payment, but it's a market. I think what
5 you are getting at whether -- I am supportive of a
6 market-based price so whatever prices are an RFP is
7 just extending that price to smaller customers so
8 they can -- they can have -- they can share in
9 helping the company meet its renewable energy goals.

10 Q. Well, so you are supportive of a
11 market-based pricing for -- as opposed to the
12 alternative compliance provisions?

13 A. Yes. I think that's a clarification,
14 yes.

15 Q. But then how does that compare to a least
16 cost option for the renewable compliance -- renewable
17 mandates?

18 A. Well, I would think that would be very
19 comparable because a market price should get you the

20 lowest -- the lowest price or least cost in that

21 sense for that particular resource.

22 Q. Now, and again, I just want to be clear

23 because your testimony refers to the alternative

24 compliance provisions, those provisions also have I

25 will call them offramps or there is a 3 percent

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1 offramp that's referenced in the alternative
2 compliance provision and there is a force majeure
3 provision in that statute that you cite here in that
4 footnote. You are not -- again, I think with this
5 clarification you have given today you are not saying
6 that those matters impact the -- those features of
7 the alternative compliance statute that you cite, you
8 are not incorporating those or addressing those
9 through this recommendation at all, are you?

10 A. The force majeure of the 3 percent?

11 Q. Yeah.

12 A. No. I am aware that in Mr. Gottfried's
13 testimony, I think Mr. Castle's testimony, the
14 company believes that their -- they will be able to
15 meet the renewable energy standard under the 3
16 percent.

17 Q. Okay. And again, I think your market
18 price clarification helps. I just wanted to make
19 sure since you cited that statute.

20 Now, do you -- how do you envision

21 administration of this type of a program? Would you

22 agree there would be some administrative challenges

23 in dealing with contracts with the mass market

24 customers on this -- on this basis?

25 A. Yeah. That would be -- that would have

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1 to be worked out. We want a program that's
2 transparent so small customers would know, be easy to
3 access.

4 Q. So well, I was referring to
5 administrative issues from the companies' standpoint?

6 A. Yes.

7 Q. In terms of complexity associated cost.

8 A. Yes, something that would have to be
9 developed. There are a number of programs that a
10 company can look to different parts of the country.

11 Q. Right. And so there again, that's a
12 matter that could be taken up in the collaborative
13 considering all those things as well as these cost
14 effectiveness considerations that might come into
15 play in designing and implementing that kind of
16 program.

17 A. Yeah. That could be a form, although we
18 did -- as part of the Duke stipulation, that's --
19 they did agree to that so there is one company in the

20 state that has agreed to it.

21 Q. Well, that's good. Does -- just for

22 clarification, again, when you talk about the

23 standard REC purchase contract, are you including

24 bundling with energy and net metering-type concept --

25 or context or would this be just -- just RECs only

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1 perhaps or can you clarify what you mean there?

2 A. I think it can be either way but I was
3 thinking more of for the residential customer who is
4 already a net metering customer I was thinking just a
5 direct payment so 5 kW moved up unit producing 2-1/2
6 RECs a year, you know, we get something maybe to help
7 promote distributive generation in the state.

8 Q. Right. And all the issues again that go
9 along with that kind of a modified net metering
10 program, again, would be considered by the
11 collaborative and the company and considering this
12 kind of a purchase program you recommend?

13 A. Yeah, we hope so.

14 MR. NOURSE: Okay. Thank you.

15 That's all the questions I have, your

16 Honor.

17 Thank you, Mr. Gonzalez.

18 EXAMINER SEE: Mr. O'Brien, did you have
19 any questions?

20 MR. O'BRIEN: No, I deferred, your

21 Honors.

22 EXAMINER SEE: Okay. Mr. Margard, any

23 questions?

24 MR. MARGARD: No questions, your Honor.

25 EXAMINER SEE: Ms. Grady.

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1 MS. GRADY: Yes, your Honor. I have no

2 redirect.

3 So at this time I would move to have

4 admission of OCC Exhibit 5.

5 EXAMINER SEE: Are there any objections

6 to the admission of OCC Exhibit 5?

7 Hearing none, the exhibit is admitted.

8 (EXHIBIT ADMITTED INTO EVIDENCE.)

9 MS. GRADY: Thank you.

10 EXAMINER SEE: Thank you, Mr. Gonzalez.

11 Let's go off the record for just a

12 second.

13 (Discussion off the record.)

14 EXAMINER SEE: Let's go back on the

15 record.

16 Please call your next witness,

17 Mr. Conway.

18 MR. CONWAY: Thank you, your Honor. At

19 this time the companies call Phil Nelson.

20 (Witness sworn.)

21 EXAMINER SEE: Mr. Conway.

22 - - -

23 PHILIP J. NELSON

24 being first duly sworn, as prescribed by law, was

25 examined and testified as follows:

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1 - - -

2 DIRECT EXAMINATION

3 By Mr. Conway:

4 Q. Mr. Nelson, could you state your name for
5 the record, please.

6 A. Philip J. Nelson.

7 Q. And Mr. Nelson, what is your position and
8 by whom are you employed?

9 A. Director of strategic initiatives, I am
10 employed by American Electric Power Service
11 Corporation.

12 Q. And did you prepare testimony that has
13 been prefiled in this proceeding?

14 A. Yes.

15 Q. And do you have a copy of your testimony
16 with you?

17 A. Yes, I do.

18 MR. CONWAY: At this time, your Honor, I
19 would like to mark as Companies' Exhibit No. 7

20 Mr. Nelson's prefiled direct testimony.

21 EXAMINER SEE: The exhibit is so marked.

22 (EXHIBIT MARKED FOR IDENTIFICATION.)

23 MR. CONWAY: Your Honor, Mr. Nelson's

24 testimony also has attached to it 13 exhibits, number

25 PJN-1 through 13 and yesterday I distributed to the

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1 parties copies of several revisions to three of those
2 exhibits, PJN-1, PJN-4, and PJN-13, and I would like
3 to mark as Companies' Exhibit No. 7A for convenience
4 in referring to the revised exhibits at this time.

5 EXAMINER SEE: Thank you. And that
6 exhibit is also marked.

7 (EXHIBIT MARKED FOR IDENTIFICATION.)

8 Q. (By Mr. Conway) Mr. Nelson, do you have
9 any additions or correction to your testimony? If
10 you could first focus on the narrative part of your
11 testimony which has been marked as Companies' Exhibit
12 No. 7, I would appreciate that.

13 A. Yes. I have three corrections in the
14 narrative. First is on page 7, the last line on that
15 page, line 19, "though" should be changed to
16 "through." The next page is on page 12, third line
17 right at the end, "though" should be changed to
18 "through." Last one is on page 16 and it's line 16,
19 there is a phrase "intend to capitalized," please

20 insert "Be" before to and capitalize it so it should

21 be "intend to Be capitalized."

22 Q. And that completes the corrections you

23 have for your -- for the narrative portion of your

24 testimony?

25 A. Yes, it does.

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1 Q. Mr. Nelson, could you describe the
2 changes to the values in your exhibits, which I
3 mentioned before included PJN-1, PJN-4, and PJN-13,
4 so that we can follow what the changes were to those
5 schedules, and if you would, start with PJN-1 and
6 just let us know which of the input values you have
7 corrected.

8 A. Okay. On PJN-1 I corrected line 19. The
9 new number is 4,791,285.

10 Q. Is that under column D?

11 A. That is under column D, yes. On my copy
12 it has been highlighted. Hopefully you-all's copy is
13 the same. The next input that was changed is on line
14 31 and in column D as well, and the number is
15 524,176. Now, these changes cause some calculations
16 to change and some totals to change. I want to go
17 through all those, but the new rate which is
18 identified as in the current SSO rate is 2.562.
19 Originally that was 2.552.

20 Q. That's on line 38?

21 A. That's correct.

22 Q. And Mr. Nelson, could you run through the

23 same exercise for the correction you have to Exhibit

24 PJN-4.

25 A. Yes. There was one input changed and

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1 that's on line 32 column D. The new number is
2 22,395,369. Again, that changed the subtotals and
3 the rates. The new rate is 1.780. The old rate was
4 1.783.

5 Q. And if you could also explain what
6 correction you've made to PJN-13 as far as the input
7 value that might have changed.

8 A. Yes. On Exhibit 13 in the column under
9 CSP there is a description that reads "Annual Revenue
10 Produced by Settlement 4 percent RSP Case No.
11 07-1278." That number is now 39 million. It was
12 29 million.

13 Q. And then did you follow that change
14 through the rest of the values in that exhibit that
15 depend upon the one you just changed?

16 A. Yes.

17 Q. And Mr. Nelson, can you provide a -- or
18 summarize at least a high level what the nature of
19 these changes is -- are? Excuse me.

20 A. The first one on PJN-1 was a clerical
21 error. I had planned to combine the fuel
22 procurement, fuel handling in one number, decided
23 ultimately to keep it as two and forgot to back it
24 out of my combined numbers, so the 68,238 on line 20
25 was double-counted.

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1 On line 31 when I was reviewing the
2 workpapers supporting my number, I discovered that we
3 had a couple of errors but the more significant was
4 we left off the line expense for Zimmer on that -- on
5 that line.

6 On PJN-4 again, this deals with the line
7 expense. We just had a number that shouldn't have
8 been added into the total, inadvertently added there
9 so that number went down.

10 Oh, I have got one more. Okay. On
11 PJN-13 I reviewed the Case No. 07-1278 and realized
12 that I had updated the revenue. This is cumulative
13 revenue. I forgot to include the first case, which
14 was 07-63, which produced about \$10 million in
15 revenue, so I have updated that number to include the
16 total revenue requirement after all the 4 percent
17 cases.

18 Q. And with the change to PJN-13, do the --
19 does the conclusion you draw from the illustration on

20 that exhibit remain the same even with the change?

21 A. Yes, it does.

22 Q. And the change to PJN-1 and PJN-4 are

23 necessary in order to accurately present the

24 information that you have presented in those

25 exhibits?

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1 A. Yes, that's correct.

2 Q. Mr. Nelson, if I were to ask you the
3 questions in your testimony today as corrected
4 including the corrections you have made to your
5 exhibits, would your answers be the same?

6 A. They would.

7 MR. CONWAY: Thank you. Your Honor.

8 Mr. Nelson is available for
9 cross-examination. And I would move the admission of
10 his testimony in the original form which has been
11 marked as Companies' Exhibit No. 7 as well as the
12 corrected exhibits which are included as Companies'
13 Exhibit No. 7A into the record.

14 EXAMINER SEE: Thank you.

15 Mr. Kurtz.

16 MR. KURTZ: Thank you, your Honor.

17 - - -

18 CROSS-EXAMINATION

19 By Mr. Kurtz:

20 Q. Good evening, Mr. Nelson. Would you turn
21 to your Exhibit 1, please.

22 EXAMINER BOJKO: I am sorry, turn to
23 what?

24 MR. KURTZ: Exhibit 1 revised, PJN-1
25 revised.

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1 Q. Do you have that, sir?

2 A. Yes, I do.

3 Q. Just so I understand this, at the very
4 top, the 1.37 cents per kilowatt hour, that's the
5 frozen fuel amounts in the rates when the unbundling
6 -- when the Senate Bill ETP cases occurred?

7 A. That's correct.

8 Q. Okay. Then what you did is you took the
9 new category of accounts that are allowable under
10 Senate Bill 221 and calculated the 1999 level of
11 expense for those accounts and that's the additional
12 expenditures that gets you to a fuel amount and base
13 rates of 2.562 cents per kilowatt hour; is that
14 correct?

15 A. Yes. Those are a couple of steps in
16 between that, and that's applying the increases that
17 we received in the RSP case to these numbers, so in
18 CSP's case they were escalated about 9 percent and
19 then we also added a PAR acquisition rider to the

20 numbers and that occurred subsequent to the original
21 unbundling case. The total, this will increase over
22 the original numbers the frozen rate and the 99
23 numbers is about 18 percent increase above those
24 original numbers.

25 Q. Okay. And so the amount that ratepayers

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1 are currently paying on average in the standard
2 service offer rates is 2.562 cents per kilowatt hour,
3 correct?

4 A. Yes. That's the FAC that we have
5 identified as being in the existing SSO rate.

6 Q. Okay. That's the base amount.

7 A. How are you defining base amount?

8 Q. Well, the amount that you are going to
9 recover is the amount over and above this, which is
10 your Schedule 2, I think; is that correct?

11 A. It can be looked at that way. I think
12 more technically correct is the idea that we have a
13 total SSO rate. We would be backing out the fuel
14 identified component of that SSO rate to determine
15 the non-FAC rate, so first step is to identify that
16 base level. We are stripping out all these costs
17 from the current SSO and then we will have a tariff
18 we will layer in the new fuel costs.

19 Q. Okay. Let's turn to your Exhibit 2 and

20 the 199 -- the 2009 projected level of fuel expenses
21 for -- here on CSP is 3.649 cents per kilowatt hour;
22 is that correct?

23 A. That's correct.

24 Q. Okay. Now, you -- Mr. Assante calculated
25 in his exhibit the total FAC amount that would be

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1 collected in 2009 without any deferral, and he said
2 he got those numbers from you.

3 A. I provided these rate calculations. I
4 provided them by -- to Mr. Roush and Mr. Assante.

5 Q. Let me ask you, conceptually if we took
6 the amount on Exhibit 2 and subtracted the amount on
7 Exhibit 1 and multiplied it by the forecasted CSP
8 kilowatt-hour, that would be the amount of the fuel
9 adjustment that would be expected to be collected in
10 2009, assuming no deferral?

11 A. Yes, other than there is a loss component
12 that's added by Mr. Roush, I believe.

13 Q. You use kilowatt-hours at the meter for
14 calculating this, don't you?

15 A. Yeah. If you apply this to these
16 numbers, you are fine. If you apply it to the actual
17 retail load, it would be a different number. I think
18 you should probably apply it to the retail load with
19 losses included.

20 Q. Well, retail load would be net of losses,

21 wouldn't it?

22 A. Yes.

23 Q. Okay. So if you take the difference

24 between Exhibit 2 and Exhibit 1 and multiply it by

25 the meter CSP load for 2009, you should get the full

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1 amount of the FAC assuming no deferral; is that
2 right?

3 A. I believe you still need to gross this up
4 for losses, but I will defer this to Mr. Roush. I
5 think he would be in a better position to answer that
6 because I don't touch the loss aspect. I think we
7 can move on. I will accept that subject to
8 Mr. Roush's.

9 Q. I mean, let me ask. Let's do the math
10 very simply for exhibit -- between Exhibit 2 and
11 Exhibit 1 I get 1.087 cents per kilowatt hour.

12 A. Okay.

13 Q. Do you have a calculator?

14 A. I do.

15 Q. Will you check my math just to make sure?

16 A. Are you working from the revised?

17 Q. Yes.

18 A. Okay. Thank you.

19 Q. I get 1.087 cents per kilowatt hour.

20 A. That's what I get.

21 Q. Okay. Now, if you turn to Mr. Assante's

22 exhibit -- do you have his Exhibit No. 1?

23 A. No.

24 Q. Could counsel show you that? Do you have

25 that in front of you?

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1 A. Yes.

2 Q. Okay. Do you see the CSP base FAC
3 revenue requirement \$260 million?

4 A. Yes.

5 Q. Okay. That would be this number we just
6 calculated, 1.087 cents per kilowatt-hour, times some
7 amount of kilowatt-hours to give you the full FAC
8 revenue requirement; would it not?

9 A. Yes. It should.

10 Q. Okay. What kilowatt-hours did you use to
11 get the 260 million or did somebody use? Because I
12 can't find those -- there are a lot of kilowatt-hours
13 for 2009 floating in this case and I can't find the
14 ones that match up.

15 A. I believe the best source would be
16 Mr. Roush.

17 Q. Let me ask you this, in terms of your
18 understanding, this amount that's being requested for
19 deferral, the 260 minus the amount proposed to be

20 collected of 148, the deferral is 112 million, that's

21 the request. Am I reading that schedule right?

22 A. That's an estimate of the deferral, yes.

23 Q. That's what -- is the deferral a set

24 number if the Commission approves your application as

25 filed, or is that number going to be somehow trued

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1 up?

2 A. I don't know. I didn't do any of the
3 deferral calculations and that's a better question
4 again for Mr. Roush.

5 Q. Okay. We could walk through the same
6 math with Ohio Power but your answer would be the
7 same conceptually, everything should be the same?

8 A. Yes.

9 Q. Okay. Let me see if I understand -- you
10 state in your Exhibit 2, now these are -- this fuel
11 adjustment schedule includes more than just fuel,
12 doesn't it?

13 A. It includes fuel purchased power, and
14 environmental costs, and renewable energy credits,
15 which are a bridge to purchasing renewable energy.

16 Q. Okay. It includes on line 36 account 507
17 depreciations and fixed capacity cost of the
18 Lawrenceburg purchase?

19 A. Yeah, that's purchased power demand.

20 Q. Okay. Purchased power demand. Now, in
21 this calculation of 2009 forecasted fuel adjustment,
22 is there included in here the market purchases the 5
23 percent of CSP's load that Mr. Baker calculates at
24 \$100 million on his Exhibit 2?

25 A. Yes.

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1 Q. Okay. And if the Commission were to say
2 no, that market purchase of 5 percent of the load is
3 imprudent, unreasonable or not allowed for some
4 reason, then this fuel adjustment cost would be
5 reduced by \$100 million; is that right?

6 A. Well, no, not precisely because you would
7 have -- it would be replaced with other fuel costs.

8 Q. That's good. Now, it would be replaced
9 with -- with pool energy purchases, wouldn't it?

10 A. I would -- that's a fair
11 characterization. It might be a simplification but
12 it could be, yes.

13 Q. Now, what -- Columbus and Southern is an
14 affiliate -- as a member company of the AEP
15 interconnection agreement is able to buy needed
16 energy from its affiliates that's basically at
17 their -- at their operating cost, at their energy
18 cost; isn't that right?

19 A. Under the pool agreement CSP does

20 purchase energy at the average cost of primary energy

21 for that -- from surplus companies.

22 Q. At the surplus -- well, it isn't even

23 necessarily -- it isn't necessarily?

24 A. Surplus energy companies?

25 Q. Right. It's not even a surplus --

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1 A. Sometimes CSP itself sells in the pool,
2 very little.

3 Q. Right. But CSP is entitled to buy at the
4 affiliates' actual energy costs, which is a lot less
5 than the 88 per megawatt-hour market price assumption
6 in Mr. Baker's testimony; isn't that right?

7 A. CSP is a member of the AEP power pool
8 and, yes, they are entitled to whatever that
9 agreement entitled them to purchase. Is it less than
10 the 88? Yes.

11 Q. Okay. I think Mr. Kollen has actually
12 qualified what that purchase price has been over the
13 last 12 months. Have you looked at his testimony?

14 A. I did review Mr. Kollen's testimony, but
15 I don't recall that particular aspect of it.

16 Q. Every month the AEP East operating
17 companies get a -- get a transaction, I think you
18 have noted as a footnote here on Schedule 1,
19 interchange power statement that shows the purchases

20 of energy, the capacity equalization payments, the

21 member load ratio allocation and off-system sales.

22 All of that is reported monthly to each operating

23 company, isn't it?

24 A. Yes, the interchange power statement

25 accounts for the pool transactions each month.

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1 Q. Okay. So if the Commission -- to go back
2 to my first question. If the Commission were to say
3 this 5 percent purchase -- 5 percent of CSP's native
4 load at market is imprudent, we wouldn't back out the
5 entire 100 million, we'd back out the difference
6 between the \$88 market price and the lower costs that
7 CSP was able to buy through the pool at.

8 A. Generally that would be the case. We in
9 our modeling would probably just remove that purchase
10 from the cost reconstruction of dispatch and the
11 numbers would flow through that modeling to produce a
12 new fuel number.

13 Q. Okay. Now, you have also included here
14 -- go to line 38 account -- or line 38, account 55,
15 which is just purchase power account. That pool
16 capacity, those are the capacity equalization
17 payments that CSP payments to the other affiliated
18 companies that are surplus; is that correct?

19 A. That's correct.

20 Q. Okay. Now, you do not have a similar or
21 you do not have a line item that credits Ohio Power
22 for the capacity equalization revenues it receives
23 from the deficit companies, do you?

24 A. In a sense I do. Let me walk you through
25 a couple of things because I think you -- I read --

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1 was that Mr. Kollen's testimony as well?

2 Q. Yeah.

3 A. I think he is a little mistaken on

4 interpretation first to my schedules and how capacity

5 settlement works and what's included in the capacity

6 settlement. My first point that I want to take to --

7 let's look at -- this might be the best schedule to

8 start with is the environmental schedule, and that's

9 on PJN-8. Capacity settlement calculation is

10 composed of two components, capacity investment rate

11 component and the fixed operating rate component.

12 The investment rate component is a function of a

13 carrying cost applied to plant, installed plant, so

14 -- and it's cost-based rates. So when Ohio Power is

15 receiving capacity revenues, that's because it's --

16 it's based on their cost. Okay?

17 So let's go to this schedule and let's

18 look at column 1 for Ohio Power Company. And you

19 will see something called coal capacity allocation

20 factor and it says 71 percent. What that says is
21 that 29 percent of this carrying cost is being
22 assigned to other members of the pool, the deficit
23 members. And what would happen if you bring in the
24 revenue. You have to then bring in the expense. You
25 can't just have one side that you can't just credit

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1 revenue against this schedule. You need to have the
2 expense there if you are going to credit revenues.

3 So what would happen is you would then
4 not do the 71 percent. You would have 100 percent
5 there. The carrying costs shown of 84 million would
6 increase to 119 million. And then you could bring in
7 an offsetting revenue if you chose to do it that way.
8 I didn't assign the cost away which is conceptually
9 the same as bringing in the revenue. So that one --
10 that's the environmental investment. Now let's go to
11 the FAC because there is a similar situation there.

12 Q. Can I stop you right there.

13 A. Okay.

14 Q. The environmental investment is only part
15 of the cost of the power plant.

16 A. Yeah. That's going to be the other
17 problem I explain to you that Mr. Kollen has. That
18 will be -- I want to first take you into, you know
19 how I have accounted for this and my components and

20 then we will talk about what you need to do if you
21 are going to bring in the total revenue because there
22 is accounts -- I will get there in a minute too in a
23 little more detail, but there's accounts that aren't
24 in my fuel cost that you need to bring in. If you
25 are going to bring in the revenue, you have to bring

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1 in the cost. It's pretty simple.

2 Q. Okay.

3 A. Okay. On Exhibit 5 just to give you a

4 quick example of one of the accounts that is also --

5 it's in the fixed operating company of the FASB

6 settlement and that's on line 44, that's account 902

7 emission control sub accounts, you can see that I

8 have only assigned for Ohio Power 54 percent of that

9 amount, 122 million, to internal load. The other

10 46 million is assigned to off-system sales --

11 off-system sales third party as well as other members

12 of the pool so, again, I have -- instead of bringing

13 in the revenue to offset the full expense I've

14 credited the expense so I think as far as -- as far

15 as we have gone here the pool capacity receipts are

16 accounted for. They are just a reduction expense

17 rather than a credit of revenue.

18 Now, as I mentioned, the third problem is

19 that there are other things that drive the capacity

20 revenue of Ohio Power, and again, it's a cost-based
21 rate. For example, if Ohio Power -- I was looking at
22 their forecasts, they are adding 236 million in plant
23 beyond the environmental plant. They would get a
24 carrying cost on that so here capacity rate would go
25 up. That would produce more revenue for them, but I

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1 don't have that 236 million on the cost side. So you
2 can't just do one side again. I can go on with other
3 examples.

4 Half maintenance is in the capacity
5 settlement rate as well. I don't have maintenance
6 costs in any of my schedules so I'll stop there. I
7 think -- I think that if Mr. Kollen revisits the
8 issue, I think he will realize you have got to look
9 at it that way.

10 Q. Clearly a lot of moving parts. Let me
11 ask you, have you verified and double checked that
12 the way you have done it and the way he did it if he
13 would have made the offsetting adjustments you make
14 would we come out in the same place?

15 A. Well, not with the limited set of
16 accounts we have here. Where you would end up if you
17 want to bring the revenue in, you generally have too
18 many costs of service for Ohio Power, you would have
19 to bring all the accounts to affect the capacity

20 settlement revenue and that's quite a list, which I
21 don't believe is the way to do it. You should be
22 more simple. We don't want to have to do cost of
23 service all the time, bring all of these additional
24 accounts into the fuel clause or whatever, so I think
25 what we have done is accounted for any fuel costs as

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1 well as the environment calculation, a credit offset.

2 Q. Why did you get a different allocation
3 factor in the one -- for the emission control
4 chemical 54 percent and other was 71 percent?

5 A. Well, that has off-system sales in it as
6 well, so off-system sales, let's just simplify, it's
7 the same allocation factor of 29 percent, that number
8 would go up to 83 percent. You still wouldn't
9 allocate 100 percent to the internal load because
10 17 percent would be for off-system sales. Now, I did
11 this on an energy basis rather than a demand basis so
12 you might get a difference in allocation. And this
13 is, of course, is an estimate for 2009, whatever it
14 is in 20008 it will be the trueup to that.

15 Q. Let me go back to your Exhibit 8.

16 A. One other point I want to make and I
17 think this is important. This will help understand
18 as well on the capacity settlement. I want to take
19 you to CSP, okay, because we are including capacity

20 payments in this but it's an advantage to the
21 customer the way I have done it and I can show you
22 how very easily. If you will turn to PJN-1 --
23 Q. Yeah, I saw that it was a bigger number
24 in '99 than '09.

25 A. With escalation we would be pulling out

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1 rates about 125 million for capacity payments, and
2 replacing it with about 34 million in 2009 so that
3 benefit, you know, it's a good thing. We could be
4 symmetrical and I could pull out the capacity
5 payments on the CSP side but I don't think we want
6 that from a customer's standpoint. It benefits the
7 customers.

8 Q. That was a long -- that was a long
9 answer. A lot to think about. Let me think about
10 that and ask you another question, different line.
11 The profits from off-system sales, the margins from
12 off-system sales, you have obviously not included
13 that in the fuel adjustment clause; is that correct?

14 A. That's correct.

15 Q. And you are aware that there is testimony
16 in the case that those profits should be excluded
17 from the earnings test as well?

18 A. Yes, I am aware of that issue.

19 Q. Okay. AEP East in West Virginia, for

20 example, aren't the profits from off-system sales

21 included in their ENEC clause, their version of fuel

22 cost adjustment?

23 MR. CONWAY: Objection. Same basis that

24 was made earlier today when the same kinds of

25 questions were posed to other witnesses. That's not

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1 relevant.

2 MR. KURTZ: I think your objection was
3 overruled.

4 MR. CONWAY: That doesn't -- we stand by
5 the objection. It's not pertinent to be comparing
6 the Ohio regulatory scheme and what ought to be done
7 in Ohio with what's being done in other
8 jurisdictions. I am sure Mr. Kurtz would be
9 objecting if we tried to work from another
10 jurisdiction and convince the Commission it ought to
11 be done here if it was to our advantage if it had
12 been done in a different jurisdiction a different way
13 on the basis it had been done in the other
14 jurisdiction rather than on the basis of what Ohio
15 law requires, what's appropriate for Ohio.

16 MR. KURTZ: I think the question is a
17 fair question in the context of we see how shall --

18 EXAMINER BOJKO: Okay. It's getting
19 late. The objection is overruled. We have been

20 allowing it to lay a little foundation not letting it

21 go too far all day so.

22 Q. Do you know --

23 EXAMINER BOJKO: Please answer the

24 question; if you know.

25 Q. Do you know how off-system sales profits

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1 are treated in the West Virginia fuel adjustment

2 clause?

3 A. Yes. West Virginia has a very expanded
4 clause. They include even transmission revenues and
5 transmission equalization payments and they include
6 the full off-system sales revenue and the full cost
7 in their ENEC.

8 Q. The profits from off-system sales are
9 allocated to CSP and Ohio Power from AEP Service
10 Corporation based upon the member load ratio of the
11 two companies not from whose power plants the sales
12 were made; isn't that correct?

13 A. Well, they are allocated according to the
14 pool agreement. AEP Service Corporation is the agent
15 for that pool agreement, but -- I am not sure they
16 are the provider of off-system sales margin, but --

17 Q. Doesn't the pool agreement allocate
18 profits from off-system sales based upon member load
19 ratio?

20 A. That's correct.

21 Q. Okay. And just if we included profits

22 from off-system sales in your fuel adjustment

23 proposal here, it would lower the cost to consumers;

24 would it not?

25 A. If you included it now -- the reason I

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1 didn't include it as I was dealing with, I will get
2 you the right section, 143(B)(2)(a) and obviously
3 that talks about costs and talks about cost of fuel
4 the cost of purchases, capacity and energy and the
5 costs of allowances, emission allowances, so I was
6 asked to look at designing a fuel clause that met the
7 requirements of SB 221. And to be frank, I didn't
8 even think about including off-system sales margins.

9 For one thing, nowhere in this bill is
10 anything mentioned about off-system sales margins,
11 and it's interesting because they do mention benefits
12 associated with the sale of emission allowances which
13 is a very small number in comparison, so I didn't
14 even think about including off-system sales. It just
15 don't fit in the fuel cost naturally.

16 Q. That section, I forget if it was this ESP
17 or a different ESP, doesn't the beginning say
18 "including but not limited to"?

19 A. Yes, it does.

20 Q. Okay. Mr. Nelson, this is an OCC data

21 response. Has this been marked?

22 MS. GRADY: No, but you can mark it.

23 MR. KURTZ: I will mark it as an OCC

24 exhibit.

25 MS. GRADY: Yeah, OCC Exhibit No. 6 would

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1 be great. I have got copies.

2 MR. KURTZ: Thank you.

3 MS. GRADY: You are talking about which
4 one? 125?

5 MR. KURTZ: Yes. Yes.

6 MS. GRADY: Here.

7 MR. KURTZ: Thank you. Could we have
8 that marked as OCC Exhibit 6?

9 EXAMINER BOJKO: It will be so marked.

10 (EXHIBIT MARKED FOR IDENTIFICATION.)

11 Q. Mr. Nelson, as you are the preparer, are
12 you familiar with this?

13 A. Yes, I am familiar with this.

14 Q. This is the forecasted income statement
15 and balance sheet for CSP and Ohio Power, at least
16 the detail behind it; is that correct?

17 A. Yeah. I am looking at, it's got income
18 statement, cash flow, EI earnings report, FERC
19 balance sheet.

20 EXAMINER BOJKO: Mr. Conway.

21 MR. CONWAY: Your Honor, I would just

22 like to note again on the record our objection, the

23 information that this -- that this document relates

24 to, which is the October 16 submittal, our position

25 is that it's not pertinent to an ESP proceeding. I

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1 understand you've made a ruling on it already, but I
2 wanted to raise it again.

3 EXAMINER BOJKO: Okay. Your objection is
4 noted for the record, but we will allow it.

5 Q. Could you turn to page 1 of 12,
6 Mr. Nelson, the Columbus and Southern income
7 statement.

8 A. Yes.

9 Q. Okay. What assumption is made about how
10 this case will turn out in terms of 2009, '10 and '11
11 revenues? Does it assume anything about what level
12 of rate increase, if any, CSP will get?

13 A. This set of workpapers was filed as --
14 per the Commission's rule as a supplement. This
15 workpaper wasn't filed specifically, but it fed the
16 documents that were filed I believe on October 16,
17 supplemental filing. As we understood, that
18 requirement was to do pro formas that showed the
19 results of our ESP filing so it has all the

20 assumptions of our ESP case.

21 Q. So it assumes you will get full recovery
22 of your ESP and the deferrals and everything else you
23 have asked for?

24 A. Yes, that's the assumption, that's what
25 we believe the Commission was requiring.

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1 Q. Okay. Midway through the net income you

2 see 336,192 for 2009?

3 A. Yes.

4 Q. Okay. Is that the right number to apply

5 to the common equity balance on page -- page 9 of 12

6 at the bottom of 1,581,476 calculate the return on

7 equity?

8 A. You said the 1,556,716? Is that the

9 right number for total proprietary capital.

10 Q. I was just using the equity. We don't

11 get much difference. What's the right number?

12 A. I would apply it to I believe the bottom

13 number.

14 Q. Okay. So if we apply that net income to

15 this total proprietary capital that would get the

16 return on -- of after tax return on equity projected

17 for 2009?

18 A. Yes.

19 Q. I did it with the other number. Let me

20 do it with this one. So that would yield 21.6

21 percent after tax return on equity for CSP?

22 A. 21.6?

23 Q. Yes.

24 A. Yes.

25 Q. Okay. For 2010 doing the same math we

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1 would get an after tax return equity of 20.1 percent;

2 is that correct?

3 A. I didn't check you but I'll -- subject to

4 checking I'll accept that.

5 Q. And for 2011 we would get 23.3 percent

6 subject to check?

7 A. That looks like a reasonable result.

8 Q. Okay. These are lower than Dr. -- your

9 witness this morning said would be the threshold at

10 least based upon 2007 examples even though that

11 wouldn't be the actual numbers that would be used but

12 these are lower than his threshold of 27.33 percent,

13 aren't they?

14 MR. CONWAY: Are you referring to

15 Dr. Makhija?

16 MR. KURTZ: Yes.

17 A. Yes, just comparing those numbers to

18 27 percent, they would be lower.

19 Q. Are you -- are you generally aware of the

20 earnings of the AEP companies and AEP East companies?

21 MR. CONWAY: Objection.

22 EXAMINER BOJKO: Basis?

23 MR. CONWAY: Relevance. It's also --

24 it's a forecast it's not --

25 EXAMINER BOJKO: Would you reread his

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1 question.

2 (Record read.)

3 EXAMINER BOJKO: Overruled.

4 A. Yes, I am generally aware.

5 Q. This would make sales to the

6 ratepayers -- if these numbers panned out if the

7 forecast worked, this would make sales to the

8 consumers who buy electricity from CSP the most

9 profitable retail sales that AEP would make in

10 America, wouldn't it?

11 A. I don't know that. You are making some

12 assumptions going forward.

13 Q. I guess the assumption I am making you

14 would not be earning a 20 to 23 percent after tax

15 return on equity in any of your other jurisdictions.

16 Is that assumption not correct?

17 A. How far out in the future are you going?

18 You know there can be a lot of things that change.

19 This is a forecast.

20 Q. I just have a question. If you turn to
21 page 2 of 12, this is the Ohio Power income
22 statement, do you see the fuel deferred expenses
23 that's very light on this -- on this copy? Do you
24 see that line item about four lines from the top?

25 A. Yeah, it is rather light but I think I

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1 can see it.

2 Q. Okay. But we have 300-some million of
3 fuel deferral forecasted in 2009.

4 A. That's correct.

5 Q. That's actually consistent with what
6 Mr. Assante showed on his schedule. Do you recall
7 that?

8 A. Yes.

9 Q. Okay. The second year the deferral
10 showed on this projection is 213 million and he had a
11 number that was apparently corrected by Mr. Roush of
12 like -- of 92 million. Is there a reason for that
13 major difference?

14 A. Yes. Mr. Assante held fuel flat. This
15 is a forecast of what we think the FAC will be in
16 '10, '11 so this is our forecast at this time.

17 Q. And so this deferral would mean that you
18 would need to defer 213 million to stay below that
19 15 percent rate cap, right? In 2010, is that what

20 this is showing?

21 A. Yes.

22 Q. And then it's showing you would need to

23 defer another 109 million in 2011 to stay below your

24 2015 rate cap; is that right?

25 A. Yes, based on this forecast of fuel

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1 costs.

2 Q. So given this forecast if this deferral
3 was correct, you would be deferring another
4 \$600 million that consumers of Ohio Power would have
5 to pay.

6 A. Well, I don't get 600 million. You said
7 Mr. Assante already had 300 million.

8 Q. Oh, I am not saying -- an additional 300
9 plus 213 plus 109 million would be in excess of
10 600 million.

11 A. Yeah, the total would be that.

12 Q. Right. And Mr. Assante was only showing
13 a deferral of 300 plus 92. That's a difference of
14 more than \$200 million. Is that right?

15 A. I am not sure if I can find the total
16 that Mr. Assante had.

17 Q. It's on his Exhibit LVA-1.

18 A. Okay.

19 Q. Deferred FAC expense -- credit

20 300 million in 2009 and then original schedule 139

21 but then he corrected it to \$92 million.

22 A. Yes, I do see a regulatory asset balance

23 at the bottom by 2011 was 554.4.

24 Q. So you are saying the numbers on this

25 income statement include the carrying costs or are

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1 these just deferrals for the year?

2 A. We did model carrying costs.

3 Q. All right. So is there --

4 A. But I am not -- I can't be certain that

5 it is in that line. I just don't know but I know we

6 modeled the carrying cost in the forms.

7 EXAMINER BOJKO: I'm sorry. So you are

8 saying you don't know if the modeling of the carrying

9 cost is in OCC Exhibit 6, is that the line you just

10 said line -- and I don't know if you were still

11 talking about Assante's exhibit or your exhibit.

12 THE WITNESS: No, it would be this

13 workpaper. And it says "Fuel-Deferred Expense."

14 Now, there was also some assumptions filed with the

15 supplemental filing that I think we might want to

16 stop and look at the assumptions before I commit that

17 the carrying costs were a model. I think it might be

18 set out in the assumptions. And I could probably

19 find a data request, assumptions should have been in

20 OCC 9-270 around the RSP case. That would tell you

21 what we modeled.

22 Q. In any event, as if the Commission were

23 to deny the 5 percent, 10 percent, and 15 percent

24 purchases which are at least modeled to be

25 120 million in 2009, 240 million in 2010, and

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1 360 million for Ohio Power, and 100, 200, 300 million
2 for CSP, Mr. Baker Exhibit 2, if the Commission were
3 to say no, those purchases are -- are not going to
4 have these market purchases at \$88 and \$85, we are
5 going to have the utilities buy from the AEP pool for
6 a lot less, these fuel numbers would be lower,
7 wouldn't they?

8 A. If you substituted a lower cost fuel
9 number for a higher cost fuel number, then the
10 deferral would go down.

11 Q. Either the deferral will go down or the
12 actual FAC would go down, depending on how that was
13 working. Either way --

14 A. Well, one would drive the other, the FAC
15 going down would drive the deferral down.

16 Q. So either way it would be lower cost to
17 consumers replacing the high cost -- high percent
18 cost with a low cost purchase. It reduces rates for
19 the consumers.

20 A. Yeah, I think on that simple assumption I

21 couldn't disagree.

22 Q. And in order to figure out whether or

23 not -- what kilowatt hours were used to calculate the

24 deferrals and whether or not those deferrals are

25 proposed to be trued up, that would be Mr. Roush?

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1 A. Yes.

2 Q. Okay.

3 MR. KURTZ: Thank you, Mr. Nelson.

4 Thank you, your Honor.

5 EXAMINER BOJKO: Let's go off the record.

6 (Discussion off the record.)

7 EXAMINER BOJKO: Let's go back on the
8 record.

9 MR. YURICK: I have just a couple of
10 questions. It will be less than 10 minutes.

11 - - -

12 CROSS-EXAMINATION

13 By Mr. Yurick:

14 Q. On page 11, sir, on line 9 you say about
15 halfway through: "Recent prices for fuel have
16 increased dramatically." Do you see that?

17 A. Yes.

18 Q. Have you updated your testimony as of
19 today?

20 A. No.

21 Q. As we sit here?

22 A. No, I haven't.

23 Q. So as you sit here, you don't know what's

24 happened to fuel pricings since July 31, 2008 when

25 your testimony was filed?

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1 A. I have an inkling.

2 Q. Well, you are under oath, sir. I don't
3 know if an inkling is going to cut the mustard, but
4 if you can do the best you can, do you know what's
5 happened to fuel prices since?

6 A. First of all, are you talking about spot
7 prices or our undelivered price?

8 Q. When you said -- when you say in your
9 testimony "Recent prices for fuel have increased
10 dramatically," do you mean spot prices or do you mean
11 cost to the company?

12 A. I would say I was meaning the cost to the
13 company. That was more important.

14 Q. Okay. So have the costs to the company
15 done anything since July 31?

16 A. They may have gone up a bit more from the
17 original forecast but I don't think it was
18 significant.

19 Q. So not -- it may have been an increase

20 but not a significant one; is that right?

21 A. Yes.

22 Q. That's what you just said?

23 A. That's a fair statement.

24 Q. Okay. Now, a little further down on line

25 11 and I think this is what your -- what you are

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1 talking about -- well, actually stay with line 10 and
2 then on lines 10 and 11 you say: "Since the
3 companies have much of their fuel supply under
4 contracts they have some protection from the
5 increases." Do you see that?

6 A. I'm sorry.

7 Q. Your next sentence on page 11.

8 A. Okay.

9 Q. So when you asked me to differentiate
10 between cost to the company cost the -- generally
11 that's what you are saying, the company has more or
12 less locked up their fuel prices for some period into
13 the future, correct?

14 A. Yes, at a rate much lower than the spot
15 prices.

16 Q. Okay. So then you go on to say:
17 "Unfortunately, however, as they expire lower cost
18 contracts are being replaced by much higher cost
19 contracts." Do you see that?

20 A. Yes.

21 Q. Okay. Now, given what's gone on with
22 fuel prices, if you know, since July 31, 2008, would
23 that modify your testimony based on your inkling or
24 what you know?

25 A. No, I don't believe so because for one

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1 thing understand our plan, we are capping it to
2 15 percent rate increases so it may affect the
3 deferral somewhat but -- and --

4 Q. We are talking about your costs?

5 A. Oh, my costs? No, I think these are a
6 fair estimate of costs at this point. I don't think
7 they could be any way misleading to what we expect in
8 2009.

9 Q. So your statement that recent fuel prices
10 for fuel have increased dramatically and that as your
11 contracts expire, they are going to be replaced by
12 much higher cost contracts, your opinion is the same
13 today as you sit here as it was on July 31?

14 A. Yes, as far as the expectation of 2009
15 costs over what we had been experiencing prior to the
16 filing of the testimony, I think that statement still
17 holds.

18 Q. Okay. So there has been no decrease in
19 cost that would alter your perception of what's going

20 to go on in the future; is that right?

21 A. Well, it depends on how far out in the
22 future you are talking about. It might, for example,
23 alter my opinion of 2011.

24 Q. How would it alter your opinion for 2011?

25 A. Well, we wouldn't have all our coal

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1 committed for 2011 at this point. We have much more
2 not locked in.

3 Q. So would you expect given what's happened
4 in the market, the spot market, and your experience
5 that you would not expect a dramatic increase in
6 costs in 2011 at this point based on what's happened
7 since July 31, 2008?

8 A. Well, we can all have expectations. I
9 would hope that our coal costs --

10 Q. I am referring to your testimony whatever
11 you meant.

12 A. Well, I haven't really dealt with 2012 or
13 2010 or '11, so in my testimony I am just talking
14 right now about 2009. That's all I have dealt with
15 in the testimony. But what I was saying is there's a
16 possibility by 2011 coal costs could moderate but I
17 think maybe to put some things in perspective is, you
18 know, I've heard that spot prices are going down. I
19 have got from the energy administration, you know,

20 spot prices were Central Appalachian coal, 12,500
21 BTU, on October 8 was about \$133 a ton. And it did
22 drop significantly by November 14, but it's about
23 \$111 a ton. However, our expectation of coal
24 deliveries in 2009 were in the 55 to \$60 a ton range
25 so spot prices will have to move down a great deal to

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1 really have significant impact.

2 Q. Could you turn to page 12, it says -- by
3 way of clarification, lines 13 through 15 you say:
4 "Off-system sales of energy to non-AEP companies for
5 the NEC component of fuel cost is determined by a
6 stacking of the companies' generation resources and
7 an assignment of the highest cost resources OSS on an
8 hour-by-hour basis." Do you see that?

9 A. Yes.

10 Q. What do you mean by "stacking the
11 companies' generation resources," I don't know.

12 A. It takes all your generating resources
13 and purchases and stacks them from low cost to high
14 cost just as a simplification and the highest cost
15 units were purchases in each other -- are assigned to
16 off-system sale and that's what I meant by that.

17 Q. And what's the reasoning for that?

18 A. It was always to give the customer the
19 benefit of the lowest cost fuel.

20 MR. YURICK: I don't have any further

21 questions of this witness at this point. Thank you.

22 EXAMINER SEE: Mr. Bell?

23 MR. BELL: I am going to accommodate

24 Mr. Resnik again, no questions.

25 EXAMINER SEE: Ms. Wung.

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1 MS. WUNG: Debating. No questions.

2 EXAMINER SEE: Mr. Randazzo.

3 MR. RANDAZZO: I have a few.

4 - - -

5 CROSS-EXAMINATION

6 By Mr. Randazzo:

7 Q. If we could go to your either original or
8 corrected version of Exhibit PJN-1 and returning to
9 line 25 that deals with pool capacity.

10 A. Yes.

11 Q. One -- what's the nature of the costs?
12 Are those -- that are included in that line.

13 A. Those are purchases from sister companies
14 of capacity.

15 Q. Okay. So it would be the charges you are
16 effectively paying for the use of the capacity
17 provided by other pool members?

18 A. That's correct.

19 Q. Okay. And as I understand the structure

20 of what you are proposing in FAC context, those
21 capacity-related charges would be recovered from
22 customers on an energy basis?

23 A. Yes, under our proposal we include them
24 in the energy charge.

25 Q. Yeah. And you mentioned in response to a

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1 question by Mr. Kurtz that you've allocated costs to
2 the Ohio companies on an energy basis, did you look
3 at what a demand allocation would do?

4 A. Well, I was talking about a specific line
5 item before.

6 Q. Okay.

7 A. I wasn't talking about everything as far
8 as the allocation. So no, but I haven't looked at
9 any different allocation factors than what I have
10 presented here.

11 Q. Okay. That's fair enough. Now, I would
12 like to give you a hint about something I was going
13 to inquire about. You were volunteered as the
14 witness that would be able to handle this so we are
15 all waiting with great expectations.

16 A. I'm excited to accommodate you.

17 Q. I'll bet. We are both sick. Page 15 of
18 your testimony and I'll use this section to sort of
19 try to illustrate the point as I understand the

20 proposal that is described on -- beginning on page 15

21 dealing with carrying costs on environmental

22 investment. Would this be similar to post-in-service

23 carrying charges as that concept is applied in

24 traditional ratemaking?

25 A. You would have to define it for me. That

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1 doesn't have meaning to me.

2 Q. Well, essentially what you are doing here
3 is you are going back to take a look at the amount of
4 capital expenditures from environmental plant that
5 occurred in the period that you described which is
6 beginning in 2001 making a judgment about the level
7 of that capital that was not reflected in rates and
8 then booking or capitalizing a carrying cost from
9 2001 in each year thereafter for purposes of
10 establishing an amount to be amortized. Am I correct
11 about that?

12 A. No. We are not going back in time to do
13 the carrying charge. What we are -- the plant -- any
14 plant that's existing at December 31 would have a
15 capital carrying requirement going forward, so it's
16 just if you think about rate base, it's -- it would
17 be similar to a rate base concept where you are
18 applying a carrying cost on a particular balance and
19 so it would just relate to 2009.

20 Q. But the balances that you calculate on --
21 in 2009 is related to the environmental investment
22 that goes back to the period of 2001 through 2008,
23 correct?

24 A. Yes, but it would be similar to any
25 other, as I said, rate based, it's a couple -- it's a

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1 balance at a point in time.

2 Q. But if it were -- first of all, this

3 would be generation plant, right?

4 A. Right.

5 Q. If it were generation-related plant, you

6 would look at not only the rate base component that

7 may be related to environmental plant but you would

8 be looking at what has happened to the asset in

9 total. You would look at the accumulated

10 depreciation that's taken place. You would have a

11 net rate base value for the entire plant not just for

12 the environmental equipment, right?

13 A. That's correct. If we were cost-based

14 regulated and were in a rate proceeding, that would

15 occur.

16 Q. All right. Now, with regard to this

17 particular item, you indicate on page 16 that the

18 carrying cost rate that was developed used a

19 50 percent common equity and 50 percent debt capital

20 structure, correct?

21 A. That's correct.

22 Q. And was it you that was responsible for

23 selecting the 50/50 capital structure?

24 A. I had a hand in it and I went to our

25 finance department and discussed that capital

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1 structure with them as well as reviewed capital

2 structure from recent periods.

3 Q. Okay.

4 A. And -- but it was really the finance

5 department's recommendation.

6 Q. Okay. So you simply reflected that

7 recommendation in your calculation of the carrying

8 cost rate, correct?

9 A. Yes.

10 Q. All right. If -- if I've got the gist of

11 this, and correct me if I am wrong, by building a

12 50 percent common equity component into the

13 capitalization or capital structure that you used to

14 compute your carrying cost rate, you are effectively

15 building into the carrying charge rate a return on

16 equity component; is that correct?

17 A. Yes.

18 Q. And so as you are -- as you both

19 accumulate or capitalize the carrying cost and as you

20 amortize it, you are building an opportunity to add
21 to the otherwise achieved return on common equity,
22 correct?

23 A. Well, let me back up a minute because I
24 think you used the term capitalize the carrying cost
25 and we are not proposing to capitalize or amortize

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1 the carrying costs. We are building the revenue
2 requirement for the carrying cost into the rate plan.

3 Q. Okay. But at some point in time you
4 would expect to amortize what you build into the
5 plant values, correct?

6 A. As I said, we are not building anything
7 into plant values. We are not capitalizing it.

8 Q. What is the purpose of a carrying charge?

9 A. To get our -- just like in a rate base if
10 you are familiar with the traditional rate base
11 with --

12 Q. Yes, I am.

13 A. -- plant in service. I figured you were.

14 Q. Yeah, yeah.

15 A. You have a return requirement and that's
16 just part of your revenue requirement and it's a
17 current bill to customer not any sort of -- you are
18 thinking maybe about AFUDC perhaps.

19 Q. No, I wasn't. It's -- at some point in

20 time this revenue requirement produces a cash

21 obligation on the part of the customer, right?

22 A. Yes. That cash obligation is January 1,

23 2009.

24 Q. And that cash obligation would reflect --

25 you would reflect a return on common equity based

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1 upon the capitalization ratio that you described

2 here, correct?

3 A. Yes, as in any rate proceeding, you would

4 have a common equity component.

5 Q. Right. And as you've structured it, this

6 rate-based calculation is exclusively limited to

7 environmental plant, correct?

8 A. That's correct.

9 Q. Now, I asked you about the capitalization

10 ratio. Is the -- the 10.5 percent return on common

11 equity that you use according to page 19 of your

12 testimony, that's simply based upon the rate that was

13 approved by the Commission in the prior case that you

14 identified there on line 15?

15 A. Yes.

16 Q. Was there any -- are you aware that there

17 are various techniques for developing the carrying

18 cost rate?

19 A. I suspect there are. This is the way I

20 usually do it.

21 Q. What is the purpose of the carrying cost

22 rate that you built into the --

23 A. Well, it's to provide a cover interest

24 expense for bond holders. Obviously, we have to pay

25 the interest expense on borrowing associated with

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1 constructing the plant, and the second party involved
2 is the common equity stockholder, he needs a return
3 on his capital investment.

4 Q. And for purposes of the computation that
5 you made to determine how much of that plant may not
6 be reflected in current rates, did you make any
7 assumptions about where that plant might have been
8 reflected in the prior rate stabilization increases?

9 A. Yes. The -- I took into account the rate
10 stabilization cases as well as the 4 percent cases
11 and that's how I developed the offset.

12 Q. Okay. All right. And -- never mind.

13 Now, Mr. Kurtz went over OCC Exhibit No.
14 6 with you and on page 1 of 12 and other places that
15 exhibit works to a earnings per share number, am I
16 correct, at the bottom of each page?

17 A. Yes.

18 Q. Are you familiar with the most recent
19 quarterly report and earnings release associated with

20 that and the amount of earnings per share that has
21 been reported by the Ohio companies?

22 A. I know we had a third quarter earnings
23 release and I did glance at it but I don't recall too
24 many specifics from it.

25 MR. RANDAZZO: Your Honor, may I have

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1 marked for identification purposes, I think we are on

2 IEU Exhibit 2.

3 MS. GRADY: Yes.

4 EXAMINER BOJKO: Yes.

5 MR. RANDAZZO: May I approach the

6 witness?

7 (EXHIBIT MARKED FOR IDENTIFICATION.)

8 EXAMINER BOJKO: Yes.

9 Q. Mr. Nelson, do you have before you what

10 has been marked for purposes as IEU Exhibit 2?

11 A. Yes.

12 Q. And would you accept subject to check

13 that's a copy of the third quarter 2008 earnings

14 release presentation that American Electric Power

15 issued on October 31, 2008?

16 A. Yes.

17 Q. Would you turn to page 11, and the page

18 numbers are in the lower right-hand corner.

19 A. Yes, I'm there.

20 Q. Okay. Now, can you tell me what the
21 words "gross margin" mean in the context that appear
22 on this page?

23 A. Yes. It's revenue less fuel and
24 purchased power.

25 Q. And if you are aware, do you know why the

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1 Ohio companies are separately broken out and appear
2 on line 2?

3 A. They are looked at as a -- kind of a
4 separate business from our other East utilities which
5 are regulated for generation as well as T&D; whereas
6 Ohio companies are just regulated on the T&D side.

7 Q. And would you agree, sir, that this page
8 shows the margin available from the Ohio companies
9 and the other business units of AEP on a dollar per
10 megawatt hour and the dollar amount that each of
11 those entities is contributing to earnings per share?

12 A. I'm sorry, could you reread the question.

13 Q. Let me try again. Let's look at line 2
14 for the Ohio companies there.

15 A. Oh.

16 Q. It shows in 2007 46.8 per megawatt hour.
17 Do you see that?

18 A. Yes, I do.

19 Q. And is that the number that is basically

20 the amount of revenue that is used to compute the
21 dollar magnitude of the contribution coming from the
22 Ohio companies to the earnings per share expressed in
23 dollars?

24 A. It's the amount of gross margin that the
25 Ohio companies contribute.

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1 Q. And the East Regulated Integrated

2 Utilities would refer to what; if you know?

3 A. It's the other -- Appalachian Power

4 Company, Kentucky Power Company, I&M, Wheeling Power,

5 I forgot Kingsport Power Company.

6 Q. And if you know, why is it that the Ohio

7 companies' gross margin per megawatt hour is so much

8 higher than the gross margin available from -- for

9 example, the east regulated integrated utilities?

10 A. I haven't analyzed this data.

11 Q. But the number there per megawatt hour

12 would essentially reflect the gross margin that we

13 talked about earlier, right?

14 A. Yes, it would.

15 Q. And the numbers that we went through for

16 2007 are shown on the right side for 2008; is that

17 correct?

18 A. That's correct.

19 Q. And if we were to turn to page 13, that

20 would show the similar information for the month of
21 September as opposed to the quarter that is embedded
22 in this report; is that correct?

23 A. Yes, page 13 is year-to-date September,
24 2008. First year-to-date was September 2007.

25 Q. And if we were to turn to page 14, that

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1 would show the 2007 actual versus the 2008 guidance
2 which was the forecasted earnings per share
3 information, correct?

4 A. Correct.

5 MR. RANDAZZO: Thank you. That's all I
6 have.

7 EXAMINER SEE: Ms. Elder.

8 MS. ELDER: No questions, your Honor.

9 EXAMINER SEE: Mr. Maskovyak.

10 MR. MASKOVYAK: No. Mr. Yurick more than
11 adequately covered where I was going to go.

12 EXAMINER SEE: Mr. Jones?

13 MR. JONES: No questions, your Honor.

14 EXAMINER SEE: Okay. Let's start with
15 Ms. Grady first thing tomorrow morning.

16 MS. GRADY: Thank you, your Honor.

17 MR. RESNIK: I just want to indicate the
18 companies' appreciation. We went forth as far as we
19 were able to this morning and that helps move it

20 along. We appreciate it.

21 MR. NOURSE: Thank you.

22 EXAMINER SEE: You're welcome. Let's --

23 Mr. Randazzo.

24 MR. RANDAZZO: I would move for the

25 admission of IEU Exhibit 2.

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1 MR. CONWAY: Your Honor.

2 EXAMINER SEE: Wait.

3 MR. KURTZ: One other.

4 EXAMINER SEE: Wait, wait, wait. Are
5 there any objections to the admission of IEU Exhibit
6 2?

7 MR. CONWAY: Your Honor, I would suggest
8 holding off until we are done with the
9 cross-examination.

10 EXAMINER SEE: We can do that.

11 MR. RANDAZZO: I just wanted to make sure
12 I got it in sometime.

13 EXAMINER SEE: We have it noted.

14 EXAMINER BOJKO: We will remind you.

15 EXAMINER SEE: We will reconvene tomorrow
16 morning at 9 o'clock and we have already discussed
17 the order.

18 Mr. Kurtz, did you need -- you needed
19 something?

20 MR. KURTZ: I was going to say OCC

21 Exhibit 6, but at the end of the witness, I guess.

22 (At 6:24 p.m. the hearing was adjourned.)

23 - - -

24

25

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CERTIFICATE

I do hereby certify that the foregoing is

a true and correct transcript of the proceedings

taken by me in this matter on Thursday, November 20,

2008, and carefully compared with my original

stenographic notes.

Karen Sue Gibson, Registered
Merit Reporter.

(KSG-5019)

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Commission of Ohio Docketing Information System on

12/5/2008 9:56:39 AM

in

Case No(s). 08-0917-EL-SSO

Summary: Transcript AEP Volume IV 11/20/08 electronically filed by Mrs. Jennifer D. Duffer
on behalf of Armstrong & Okey, Inc.