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BEFORE
THE PUBLIC UTILITIES COMMISSION OF OHIO

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

DIRECT TESTIMONY OF JOSEPH G. BOWSER ON BEHALF OF INDUSTRIAL ENERGY USERS-OHIO

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DIRECT TESTIMONY OF JOSEPH G. BOWSER
ON BEHALF OF INDUSTRIAL ENERGY USERS-OHIO

I. INTRODUCTION

Q1. Please state your name and business address.

A1. Joseph G. Bowser, 21 East State Street, 17th Floor, Columbus, Ohio 43215.

Q2. By whom are you employed and in what position?

A2. I am a Technical Specialist for McNees Wallace & Nurick LLC ("McNees") providing testimony on behalf of the Industrial Energy Users-Ohio ("IEU-Ohio").

Q3. Please describe your educational background.

A3. In 1976, I graduated from Clarion State College with a Bachelor of Science degree in Accounting. In 1988, I graduated from Rensselaer Polytechnic Institute with a Master of Science degree in Finance.

Q4. Please describe your professional experience.

A4. I have been employed by McNees for over five years where I focus on assisting IEU-Ohio members address issues that affect the price and availability of utility services. Prior to joining McNees, I worked with the Office of the Ohio Consumers' Counsel ("OCC") as Director of Analytical Services. There I managed the analysis of financial, accounting, and ratemaking issues associated with utility regulatory filings. I also spent ten years at Northeast Utilities, where I held positions in the Regulatory Planning and Accounting departments of the company, provided litigation support in regulatory hearings and assisted in the preparation of the financial/technical documents filed with state and federal regulatory commissions. I began my career with the Federal Energy Regulatory Commission ("FERC"), where I led and conducted audits of gas and electric utilities in the Eastern and Midwestern regions of the United States.

Q5. Have you previously submitted expert testimony before the Public Utilities Commission of Ohio ("Commission")?

A5. Yes, since 1996, I have submitted testimony as an expert on numerous regulatory accounting issues and how those issues should be resolved for purposes of establishing rates and charges of public utilities. More specifically, I have submitted expert testimony in the following cases: *In the Matter of the Application of The East Ohio Gas Company for Authority to Implement Two New Transportation Services, for Approval of a New Pooling Agreement, and for Approval of a Revised Transportation Migration Rider*, Case No. 96-1019-GA-ATA; *In the Matter of the Applications of Columbus Southern Power*

Company and Ohio Power Company for Approval of Their Electric Transition Plans and for Receipt of Transition Revenues, Case Nos. 99-1729-EL-ETP, *et al.*; *In the Matter of the Commission's Investigation Into the Policies and Procedures of Ohio Power Company, Columbus Southern Power Company, The Cleveland Electric Illuminating Company, Ohio Edison Company, The Toledo Edison Company and Monongahela Power Company Regarding the Installation of New Line Extensions*, Case Nos. 01-2708-EL-COI, *et al.*; *In the Matter of the Application of Columbus Southern Power Company to Adjust its Power Acquisition Rider Pursuant to Its Post-Market Development Period Rate Stabilization Plan*, Case No. 07-333-EL-UNC; *In the Matter of the Application of Ohio Edison Company, The Cleveland Electric Illuminating Company and The Toledo Edison Company for Authority to Increase Rates for Distribution Service, Modify Certain Accounting Practices and for Tariff Approvals*, Case Nos. 07-551-EL-AIR, *et al.*; *In the Matter of the Application of Ohio Edison Company, The Cleveland Electric Illuminating Company, and The Toledo Edison Company for Authority to Establish a Standard Service Offer Pursuant to Section 4928.143, Revised Code, in the Form of an Electric Security Plan*, Case No. 08-935-EL-SSO; *In the Matter of the Application of Columbus Southern Power Company for Approval of its Electric Security Plan; an Amendment to its Corporate Separation Plan, and the Sale or Transfer of Certain Generating Assets*, Case Nos. 08-917-EL-SSO, *et. al.; In the Matter of the Application of The Dayton Power and Light Company for Approval of Its Electric Security Plan*, Case

Nos. 08-1094-EL-SSO, *et al.;* and *In the Remand Proceeding in Case Nos. 08-917-EL-SSO, et al.* already listed above.

Q6. What does your testimony in this case address?

A6. My testimony addresses the propriety of certain charges that have been attributed to compensation for carrying costs on environmental investments, which were proposed and included in the first electric security plans ("ESP") of Ohio Power Company ("OPCo") and Columbus Southern Power Company ("CSP"), collectively "AEP-Ohio", or "the Companies". My testimony identifies why these charges are not includable through the provisions which may be included in an ESP. In addition, I address the flow-through effects of excluding these charges as well as provider of last resort ("POLR") charges on the Companies' proposed phase-in rider. These flow-through effects are similar to those which I identified in the remand phase of the proceedings in Case Nos. 08-917-EL-SSO, *et al.* I also address the changes proposed by AEP-Ohio to the Environmental Investment Carrying Cost Rider ("EICCR") in this proceeding, and AEP-Ohio's securitization proposal as it relates to the carrying charge rate on phase-in amortizations.

Q7. What did you review for purposes of preparing your testimony?

A7. For the purpose of preparing my testimony, I reviewed the direct testimony of Companies' witnesses Moore, Mitchell, Hawkins, and Nelson, discovery responses, and Commission entries filed in this case. In addition, I reviewed the filings and discovery responses in the remand phase of Case Nos.

08-917-EL-SSO, *et al.* and in AEP-Ohio's EICCR proceedings (Case Nos. 10-155-EL-RDR and 11-1337-EL-RDR). My opinions and recommendations also reflect the knowledge I have accumulated throughout my career.

II. PROPRIETY OF ENVIRONMENTAL CARRYING COSTS BEING INCLUDED IN THE ESPS OF CSP AND OPCO

Q8. Please provide background information on environmental carrying costs for AEP-Ohio.

A8. In the ESPs of CSP and OPCo for the years 2009 through 2011 (Case Nos. 08-917-EL-SSO, *et al.*) the Commission, in its Opinion and Order dated March 18, 2009, authorized CSP and OPCo to establish rates for the standard service offer ("SSO"). The revenue which the Commission authorized CSP and OPCo to collect through the ESP rates and charges included revenue components that were calculated to provide, among other things, a return on and of certain environmental capital expenditures that were alleged to be over and above that amount embedded in the Companies' legacy rates and charges. Such capital expenditures occurred between 2001 and 2008 and prior to January 1, 2009. I shall refer to this revenue component as the "Pre-2009 Component."

In addition, the Commission authorized CSP and OPCo to establish a separate charge that produced incremental revenue for "carrying costs" on capital expenditures for environmental plant made on or after January 1, 2009 and during the ESP period. I shall refer to this revenue component as the "Post-2008 Component". With regard to the Post-2008 Component, the Commission

1 directed the Companies to propose, through an annual filing, a charge for such
2 carrying costs "after the investments had been made." (Opinion and Order dated
3 March 18, 2009 in Case Nos. 08-917-EL-SSO, *et al.* at page 30.)

4 After the Commission's decision in the Companies' ESP cases was appealed to
5 the Ohio Supreme Court ("Court"), on April 19, 2011, the Court held, among
6 other things, that the Commission had erred in authorizing CSP and OPCo to
7 collect revenue for items not specifically authorized by statute. The Court also
8 stated that on remand the Commission may determine whether any of the listed
9 categories of Section 4928.143(B)(2), Revised Code, authorizes recovery of
10 environmental carrying charges.

11 In an Entry issued on May 25, 2011, regarding the remand phase referenced
12 above, the Commission stated that the Companies and the intervenors should be
13 afforded an opportunity to present testimony and to offer additional evidence in
14 regard to the environmental carrying charges remanded to the Commission. The
15 Commission also directed AEP-Ohio to file revised tariffs specifically stating that
16 the Pre-2009 Component charges and the POLR riders would be collected
17 subject to refund, effective as of the first billing cycle of June 2011.

18 The Commission also established a procedural schedule to address the issues
19 raised by the Ohio Supreme Court's decision. On June 6, 2011, the Companies
20 filed the testimony of Mr. Philip Nelson in support of the continuation of the Pre-
21 2009 Component environmental charges in the remand phase of Case Nos.
22 08-917-EL-SSO, *et al.*

1 **Q9. Has the Commission issued a decision addressing the contested issues in**
2 **the remand phase of Case Nos. 08-917-EL-SSO, *et al.*?**
3 A9. No. At the time of my writing of this testimony, the hearings in the remand case
4 were scheduled to end on July 28, 2011, with briefing to follow. In effect, there is
5 an overlap of the procedural schedules for the remand phase of Case Nos.
6 08-917-EL-SSO, *et al.* and the proceedings initiated to address the issues raised
7 by the ESP proposal filed in these proceedings.

8 **Q10. How do the unresolved issues in the remand phase of Case Nos.**
9 **08-917-EL-SSO, *et al.* relate to these proceedings?**
10 A10. Since the resolution of the issues in the remand phase of Case Nos.
11 08-917-EL-SSO, *et al.* will determine the rates and charges that are properly
12 includable in the current ESP and the ESP proposed in these proceedings builds
13 on the current ESP's rates, charges and revenue, the resolution of the issues in
14 the remand phase of Case Nos. 08-917-EL-SSO, *et al.* has a direct effect on the
15 starting point for the ESP proposed in these proceedings.

16 **Q11. You indicated earlier that you submitted testimony in the remand phase of**
17 **Case Nos. 08-917-EL-SSO, *et al.* What opinions and recommendations**
18 **were in that testimony?**
19 A11. Based on my understanding of the April 19, 2011 decision of the Ohio Supreme
20 Court and the specific categories in Section 4928.143(B)(2), Revised Code,
21 through the advice of counsel and my understanding of the applicable accounting
22 principles, I expressed the opinion that the charges for the Pre-2009 Component

are not includable in an ESP. Therefore, I recommended that CSP's and OPCo's ESP rates be adjusted downward to remove the Pre-2009 Component from the ESP rates and charges effective with the first billing cycle of June 2011. In addition, I recommended that the Commission require that CSP and OPCo return to customers (through a refund or bill credit) the amounts that have been collected subject to refund since the first billing cycle of June 2011, per the Commission's May 25, 2011 Entry referenced above. I also observed that my recommended downward adjustment to rates was not sufficient to fully remove the Pre-2009 Component from CSP's and OPCo's future rates and charges because the Companies' first ESPs included a phase-in that was based on the *revenue collection including the Pre-2009 Component. Therefore and to fully* reflect the elimination of the Pre-2009 Component on all future rates and charges, I also recommended that the effect of the Pre-2009 Component on the amount eligible for future collection as a result of the phase-in deferral, delta revenue related to reasonable arrangements, and the Universal Service Fund ("USF") Rider also needed to be recognized.

Based on testimony filed by IEU-Ohio witness Murray in the remand phase of Case Nos. 08-917-EL-SSO, *et al.* who concluded that the Companies' POLR should not be approved by the Commission, I also recommended that CSP's and OPCo's ESP rates be adjusted downward to remove the POLR Rider from the ESP rates and charges, effective with the first billing cycle of June 2011. In addition, I recommended that the Commission should require that CSP and OPCo return to customers (through a refund or a bill credit) the amounts that had

been collected subject to refund through their POLR Riders since the first billing cycle of June 2011, per the Commission's May 25, 2011 Entry referenced above.

Because the Companies' ESPs included a phase-in that will be based on the revenue collection including the POLR revenues, I also recommended that the effect of the POLR revenues on the amount eligible for future collection as a result of the phase-in deferral, delta revenue related to reasonable arrangements, and the USF Rider must also be recognized.

Q12. Can you elaborate on your recommendation in your remand testimony with respect to the significance of the phase-in?

A12. Yes. I explained that in the current ESPs, the Commission authorized the Companies to collect a pot of ESP dollars or a total authorized ESP revenue requirement. The Commission then limited that amount of the authorized revenue that the Companies could collect during the ESP period ending December 31, 2011. The balance of the total authorized revenue that would have been collected during the ESP period but for the Commission's bill increase limitations was deferred for future collection. The revenue eligible for future collection is the phase-in portion of the total revenue authorized by the Commission and the Commission stated that this amount would be determined as a function of other components of the ESP and the total bill increase limits established by the Commission. To the extent the amount of revenue collected by the Companies during the ESP period was based on items that are not properly includable in an ESP, the amount of revenue postponed (deferred) for

future collection is not proper. The Commission's Opinion and Order issued on March 18, 2009, at page 22, limits recovery to the amount of deferred revenues as determined at the end of 2011 that is "allowed." In my remand phase testimony, I explained that in order to address this problem, the Commission must reduce the total authorized revenue by the amounts not properly collectible as part of an ESP, and subtract the amount actually collected from the adjusted ESP total to determine how much, if any, of the authorized revenue is eligible for future collection after the end of the current ESPs. Otherwise, the improperly included ESP charges would be embedded in the revenue postponed for future collection.

Q13. What specific adjustments did you recommend to the revenues postponed for future collection (phase-in deferral) in the remand case?

A13. I recommended that the revenues collected from the beginning of the ESP through May 2011 for the Pre-2009 Component for environmental carrying charges ($62.8 million for CSP and $203 million for OPCo) be credited against the revenues deferred for future collection (phase-in deferral). In addition, I recommended that the revenues deferred for future collection be reduced by $235.3 million for CSP and $132.4 million for OPCo for POLR revenues collected from the beginning of the ESP through May 2011. The foregoing amounts do not include any recognition of interest that should be added to these amounts for purposes of making the required reconciliation of the revenue deferred for future collection.

I also explained in my remand testimony that practical reasons differentiated the results of my recommended downward adjustments to the revenues postponed for future collection. Based on the differences between the two utilities' ESPs, it currently appears that only OPCo will have a portion of the total authorized revenue that is subject to future collection after the ESP period. Accordingly, the opportunity to reduce the going-forward effects of the inappropriate inclusion of the environmental charges and POLR revenues is limited to OPCo. I suggested that the Commission could consider reducing CSP's regulatory assets included in Account 182.3 – Other Regulatory Assets, for items such as deferred line extension costs, deferred storm expense, and deferred deregulation implementation costs.

I also explained that other ratemaking adjustments were necessary to reflect the going-forward effects of the elimination of environmental charges and POLR charges, in the computation of allowable revenue for "delta revenue" and the USF Rider.

Q14. Do your recommendations from the remand case impact the ESP proposal that has been filed in these proceedings?

A14. As I have briefly indicated already, the resolution of the issues in the remand phase of Case Nos. 08-917-EL-SSO, *et al.* will affect the proposed ESP in these proceedings. Because the outcome of the remand case has not yet been determined, my recommendations from the remand case also apply to identify the current ESP starting point for purposes of evaluating the ESP proposed in

1 these proceedings. The ESP proposal in this proceeding rests on a revenue
2 foundation that includes the revenue from charges that the Ohio Supreme Court
3 held were not properly authorized by the Commission. Accordingly, my
4 recommendations in the remand phase of Case Nos. 08-917-EL-SSO, *et al.* must
5 be picked up in these proceedings to ensure that the flow-through effects of the
6 Ohio Supreme Court's remand order on postponed revenues and other
7 regulatory assets, and other issues such as delta revenues, are picked up in the
8 evaluation of the current ESP proposal. Further, because my recommendations
9 in the remand phase included the recommendation that CSP's and OPCo's ESP
10 rates be adjusted downward to remove the Pre-2009 Component from the ESP
11 rates and charges (embedded in non-fuel adjustment clause ("FAC") generation
12 rates) effective with the first billing cycle of June 2011, there is also an impact on
13 the embedded non-FAC generation rates that the Companies are proposing, in
14 these proceedings, to transfer to the Standard Offer Generation Service Rider
15 ("Rider GSR") effective January 1, 2012. I would like to add that the Companies
16 have filed a placeholder for the phase-in rider (Rider PIR) by which the
17 Companies propose to recover the ultimately allowed level of postponed
18 revenues deferred, on a charge per kWh that has not yet been determined. I
19 recommend that the Commission not make its final ruling on the rate or structure
20 for Rider PIR until the final level of postponed revenues allowed has been
21 determined.

Q15. Do you have any other recommendations regarding environmental carrying charges that affect the ESP proposed in these proceedings?

A15. Yes. Based on advice of counsel regarding the meaning of provisions in Section 4928.143(B)(2), Revised Code, and the use of accounting principles to identify the effects of the eligibility criteria in such Section, it is my opinion that the charges associated with the Post-2008 Component are not eligible for inclusion within an ESP. Because the ESP proposed in these proceedings expands the scope of the charges that the Companies associate with the post-2008 capital expenditures to include certain operation and maintenance ("O&M") expenses and also proposes to make the new ESP charges non-bypassable, my opinion extends to the entirety of the Companies' proposed charges associated with Post-2008 environmental plant. Accordingly, I recommend that the proposed charges associated with Post-2008 environmental plant not be included in any ESP that the Commission may approve in this proceeding.

I should note that the proposed charges associated with post-2008 environmental plant are not separate charges for CSP and OPCo in their capacity as electric distribution utilities ("EDU"). As explained by IEU-Ohio witness Murray, the Companies are proposing an ESP for AEP-Ohio which is not an EDU. My discussion of the Companies' proposed charges associated with post-2008 environmental plant should not be interpreted as an agreement that ESP rates and charges can be established for an entity that is not an EDU. Rather, I have focused on the question of whether the proposed charges associated with post-2008 environmental plant are, based on the facts and

circumstances in this case, properly includable in an ESP which is proposed by an EDU.

Q16. How does the ESP proposed in these proceedings deal with the Post-2008 Component?

A16. This subject is addressed by the Companies' ESP Application at page 10. The Application states:

> 4. Environmental Investment Carrying Cost Rider
>
> The proposed ESP includes continuation and modification of the Environmental Investment Carrying Cost Rider (EICCR). The Company is proposing some modifications to the existing rider, including changing it to be a nonbypassable rider. The EICCR will continue to recover the incremental environmental capital carrying costs incurred after 2009 as these are being recovered today. The Company is proposing that, first, it be permitted to forecast the cost, with a subsequent periodic true-up, in order to eliminate the lag that occurs today. Secondly, there are certain operating and maintenance expenses (O&M) associated with environmental equipment that are not being recovered in either the current environmental rider or the FAC, such as O&M associated with Flue Gas Desulfurization (FGD) equipment, that the Company seeks to include beginning in 2012. Additional details on the proposed rider are discussed in the testimony of Company witnesses Nelson, Moore and Mitchell.

The direct testimony of Companies' witness Mitchell does not address whether the proposed charges associated with post-2008 environmental plant are includable within an ESP. He touches on some accounting related to the Companies' proposal to use forecasted (not actual) expenditures to establish the EICCR going forward.

The direct testimony of Companies' witness Moore does not address whether the proposed charges associated with post-2008 environmental plant are includable

within an ESP. She discusses how the current charges will be mixed in the EICCR when, as the Companies propose, estimated expenditures are introduced. She notes that the Companies are proposing to collect the charges through one entity, AEP-Ohio.

The direct testimony of Companies' witness Nelson does not address whether the proposed charges associated with post-2008 environmental plant are includable within an ESP. At page 16 of his direct testimony, he does state that the Companies are requesting that the EICCR be transformed into a non-bypassable charge "... as contemplated by section 4928.143(B)(2)(b)."

None of the testimony of the Companies' witnesses attempts to demonstrate that the revenue that the Companies can collect through other rate elements, including the base generation charge, is insufficient to provide a reasonable return on and of environmental-related capital expenditures and recovery of the targeted O&M expenses properly allocable to SSO customers.

Q17. If the Companies had demonstrated that the revenue that the Companies can collect through other rate elements, including the base generation charge, is insufficient to provide a reasonable return on and of environmental-related capital expenditures and recovery of the targeted O&M expenses properly allocable to SSO customers and also claimed that the proposed charges associated with post-2008 environmental plant are eligible to be included within an ESP based on Section 4918.143(B)(2)(b), Revised Code, would such a claim be correct?

A17. No. Based on the advice of counsel regarding the meaning of Section 4928.143(B)(2)(b), Revised Code, applicable accounting principles and the information I have obtained from the Companies during the discovery phase of this proceeding, the Companies' proposed EICCR is not eligible for inclusion in an ESP.

Q18. Please explain.

A18. Based on advice of counsel, it is my understanding that Section 4928.143(B)(1), Revised Code, requires that an ESP include provisions dealing with the supply and pricing of electric generation service and Section 4928.143(B)(2), Revised Code, identifies nine provisions that **may** be included in an ESP if the eligibility criteria within each provision are met and subject to other limitations that may result, for example, from the application of the policy objectives expressed in Section 4928.02, Revised Code.

It is my understanding that any provision that may be included within an ESP as a result of Section 4928.143(B)(2)(b), Revised Code, must fit within the following language:

> A reasonable allowance for construction work in progress for any of the electric distribution utility's cost of constructing an electric generating facility or for an environmental expenditure for any electric generating facility of the electric distribution utility, provided the cost is incurred or the expenditure occurs on or after January 1, 2009. Any such allowance shall be subject to the construction work in progress allowance limitations of division (A) of section 4909.15 of the Revised Code, except that the commission may authorize such an allowance upon the incurrence of the cost or occurrence of the expenditure. No such allowance for generating facility construction shall be authorized, however, unless the commission first determines in the proceeding that there is need for the facility

> based on resource planning projections submitted by the electric distribution utility. Further, no such allowance shall be authorized unless the facility's construction was sourced through a competitive bid process, regarding which process the commission may adopt rules. An allowance approved under division (B)(2)(b) of this section shall be established as a nonbypassable surcharge for the life of the facility.

It is my understanding that the Ohio Supreme Court issued a decision in which it addressed certain claims regarding the scope of ESP provisions that are eligible for inclusion in an ESP. More specifically, it is my understanding that this scope is limited by categories specifically identified in Section 4928.143(B)(2), Revised Code.

As shown by the Companies' own computations, the types of costs which the Companies propose to roll into the EICCR are unrelated to an allowance for construction work in progress ("CWIP"). For example, the Companies have included a return on and of capital investment for purposes of developing the carrying charge rate that is used to calculate the revenue they propose to recover through the EICCR. But, CWIP is for plant that is being constructed and is not operating or "in service." Because CWIP accounting accumulates costs incurred for plant or equipment during construction and prior to the plant or equipment being placed in service or becoming operational, CWIP accounting does not include a component for a return of capital. The return of capital occurs through depreciation which commences only once the plant or equipment is placed in service. Also, the information provided by the Companies in response to discovery indicates that the Companies do not have the ability to identify what portion of the Post-2008 Component expenditure is associated with CWIP or

1 plant in service. Additionally, the EICCR proposed by the Companies in this
2 proceeding includes certain O&M expenses. O&M expenses are not accounted
3 for as CWIP and, based on my understanding of Section 4928.143(B)(2)(b),
4 Revised Code, and the applicable accounting principles, the O&M expenses
5 identified by the Companies are not eligible for inclusion in an ESP either through
6 Section 4928.143(B)(2)(b), Revised Code, or, based on the information
7 presented by the Companies, any other provision within Section 4928.143(B)(2),
8 Revised Code.

9 Based on advice of counsel, it is also my understanding that any non-bypassable
10 charge authorized under Section 4928.143(B)(2)(b), Revised Code, must be
11 tested against the CWIP limitations in Section 4909.15, Revised Code, and that
12 the Commission must, pursuant to Section 4928.143(C), Revised Code, ensure
13 that the benefits derived as a result of an ESP charge authorized under Section
14 4928.143(B)(2)(b), Revised Code, are reserved and made available to those who
15 bear the surcharge.

16 Finally, it is also my understanding that the Commission must consider, pursuant
17 to Section 4928.20(K), Revised Code, the effect that any non-bypassable
18 generation-related charge might have on large-scale governmental aggregation.

19 The Companies' direct testimony fails to address the requirements of Section
20 4909.15, Revised Code, or the effect that their proposed non-bypassable EICCR
21 charge might have on large-scale governmental aggregation.

So, even if the Companies had demonstrated that the revenue that the Companies can collect through other rate elements, including the base generation charge, is insufficient to provide a reasonable return on and of environmental-related capital expenditures and recovery of the targeted O&M expenses properly allocable to SSO customers, it is my opinion that the proposed EICCR is not eligible for inclusion in an ESP based on the facts and circumstances in this case.

Q19. Are there any other reasons why you believe that the EICCR is not eligible for inclusion in an ESP based on the facts and circumstances in this proceeding?

A19. Yes. As a result of the information I obtained during discovery, it appears that the capital expenditure and related depreciation portions of the carrying charge rate that the Companies propose to use to calculate the EICCR are related to environmental facilities that were not all constructed and sourced through a competitive bidding process.

Q20. What is your understanding of the meaning of the term "competitive bid process"?

A20. A competitive bid process entails a process for issuing requests for proposals or bids, and evaluating responses based on the best price and contract terms.

Q21. Did you identify projects for which the Companies are seeking recovery for which at least some portion was not subject to a competitive bid?

A21. Yes. I found that the Companies did not competitively bid certain contracts awarded for the following projects: Amos Unit 3 Ash Disposal, Cardinal Units 1 and 2, Flue Gas Desulfurization, and Conesville Unit 5, Flue Gas Desulfurization. It is my understanding that Section 4928.143(B)(2)(b), Revised Code, limits eligibility to facilities that are constructed and sourced though a competitive bidding process.

Q22. Have the Companies proposed to alter the design of the EICCR charge?

A22. Yes. The Companies are proposing that the EICCR charge be changed from a percentage rate that is applied to a customer's non-fuel base generation charge to a per/kWh charge, effective January 1, 2012. Also, as I explained previously, the Companies are not seeking separate EICCR charges for CSP and OPCo. Rather, they are proposing that the EICCR be calculated to reflect the same charge for both EDUs and to ignore the individual EDU EICCR computations that would otherwise occur. As I also explained earlier, the Companies are proposing to make the EICCR non-bypassable beginning January 1, 2012 meaning that the EICCR will not be avoidable by customers securing their generation supply from a competitive retail electric service ("CRES") supplier.

The Companies are requesting that, beginning with the 2012 EICCR filing, a forecast of spending be incorporated into the rider to eliminate the lag between

1 expenditures and recovery. The Companies are also requesting that, beginning
2 January 2012, the environmental rider include environmental O&M expense.

3 **Q23. Do you agree with the Companies' proposed design of the EICCR?**

4 A23. No. Even if the proposed EICCR was eligible for inclusion in an ESP, it would be
5 unreasonable to make the EICCR non-bypassable. The proposed EICCR is for
6 generation-related items. Allowing the EICCR to become non-bypassable would
7 place CRES suppliers at a competitive disadvantage, give the Companies a
8 competitive advantage and deprive consumers of the benefits that they might
9 otherwise obtain as a result of shopping.

10 If the Commission were to provide the Companies with a non-bypassable
11 EICCR, it would be unreasonable to establish the carrying charge rate based on
12 a weighted average cost of capital ("WACC") methodology as proposed by the
13 Companies. Any carrying charge rate in this circumstance should be calculated
14 based on a debt rate reflecting the benefits that the Companies obtain from
15 special types of financing that are available for environmental control facilities.
16 Using a WACC approach assumes that the shareholders are assuming the
17 business and financial risks associated with the underlying investment but a non-
18 bypassable charge shifts risk to customers. The Companies should not be able
19 to unreasonably inflate the carrying charge rate by including a cost of common
20 equity component in circumstances where customers are subjected to a non-
21 bypassable EICCR.

With regard to the Companies' proposal that the EICCR be based on forecasted expenditures and based on the advice of counsel, it is my understanding Section 4928.143(B)(2)(b), Revised Code, limits eligibility to provisions that address incurred rather than forecasted expenditures. Therefore, if the Commission were to approve any EICCR charge in this proceeding, it should be based on incurred expenditures (and only expenditures that are in CWIP and not in plant in service).

Finally, the Companies' proposal to collect the EICCR on a kWh basis is unreasonable. This aspect of the Companies' proposal treats fixed costs (return of and on capital expenditures, depreciation and taxes) as though they are variable costs. The kWh charge will also tend to shift responsibility for the EICCR revenue to larger and higher load factor customers, which will work against Ohio's effort to retain and expand its manufacturing sector.

III. SECURITIZATION AND THE CARRYING CHARGE RATE ON PHASE-IN DEFERRAL AMORTIZATION

Q24. What is your understanding of AEP-Ohio's position regarding securitization of any amounts that might be recovered as deferred revenue due to bill limitations in the 2009-2011 ESP?

A24. In the direct testimony of Companies' witness Hawkins, she describes the use of securitization bonds as a means of financing the phase-in revenue deferrals associated with the ESP approved by the Commission in Case Nos. 08-917-EL-SSO, *et al.* Companies' witness Hawkins testifies that with appropriate securitization legislation, customers would benefit from a reduced carrying cost over the remaining life of the phase-in deferral (2012–2018)

because securitization bonds have a carrying cost generally equal to AAA rated debt, whereas the unamortized balance of the phase-in regulatory assets would otherwise have carrying costs at the WACC (approximately 11.77%). Companies' witness Hawkins states that customers could also benefit because the Companies could amortize the phase-in balance over a longer term than the seven-year period contemplated in the Companies' ESP in Case Nos. 08-917-EL-SSO, *et al.*

Companies' witness Hawkins further indicates that OPCo may have been able to issue securitization debt at a rate of approximately 3.50% in July 2010, and stated that on a phase-in deferral balance of $643 million, the annual carrying costs at a WACC rate of 11.77% would be approximately $76 million versus an annual interest cost of securitization bonds of $19 million.

Q25. Do you agree with the magnitude of possible savings that Companies' witness Hawkins has provided?

A25. In my opinion, Companies' witness Hawkins has significantly overstated the benefits of securitization and ignored how securitization of the type she has suggested will transfer risks away from the Companies and to the State of Ohio as well as the costs that must be incurred to proceed with the type of securitization that she recommends.

Q26. Please explain.

A26. First, the Commission already has the ability to specify the carrying cost rate to be applied when amortization of the phase-in deferral balance begins, and could

1 specify that a debt rate rather than the WACC rate be used once amortization
2 commences. Indeed, the Commission has ordered that such amortizations
3 proceed using a debt-based carrying charge rate in other cases such as *In the*
4 *Matter of the Application of Ohio Edison Company, The Cleveland Electric*
5 *Illuminating Company, and The Toledo Edison Company for Approval of a New*
6 *Rider and Revision of an Existing Rider*, Case No. 10-176-EL-ATA, Opinion and
7 Order at 24 (May 25, 2011).

8 Per the workpapers filed with Companies' witness Hawkins' testimony, as of
9 August 2010, the weighted average cost of long-term debt was 5.27% for OPCo,
10 and 5.50% for CSP. Requiring the long-term debt rates to be applied to the
11 unamortized phase-in deferral balance would equate to most of the savings in
12 interest costs that Companies' witness Hawkins attributes to securitization.
13 Further, a debt-based carrying cost rate would be appropriate because the non-
14 bypassable nature of the charge that customers pay through the phase-in rider
15 essentially eliminates AEP-Ohio's financial and business risk regarding the
16 phase-in deferral.

17 Regarding Companies' witness Hawkins' contention that securitization would
18 permit the amortization period for the phase-in deferral to be extended, again, the
19 Commission can specify the amortization period, just as it can specify the interest
20 rate charged to customers on the unamortized deferral balance. However, it
21 should be noted that a longer amortization period is not necessarily beneficial for
22 customers, as a longer recovery period will result in additional interest costs, all

else being equal. In short, neither securitization nor securitization legislation is needed to reduce the costs of any phase-in deferral that may ultimately be found to be eligible for recovery from customers.

Q27. *You indicated that there may be risks for the State of Ohio if the type of securitization discussed by Companies' witness Hawkins is adopted. Why would there be risks for the State of Ohio?*

A27. The securitization structure very generally described by Companies' witness Hawkins omits identification of several details that will need to be included in any legislation of the type she recommends. For example, she assumes that the quality of the bond rating available for the securitization bonds will be AAA (the highest rating). This bond rating assumption and her erroneous assumption that securitization is required to displace the use of a WACC carrying charge rate are the two main sources of her prediction that customers will be better off with securitization. But, to get to the AAA bond rating, the State of Ohio will be required to issue a pledge that guarantees that the revenue stream arising from the non-bypassable charges imposed on customers will not be altered or interfered with once the bonds are issued. Thus, the details of the securitization legislation may implicate the State of Ohio's balance sheet and credit rating.

Q28. Has Companies' witness Hawkins omitted some other important considerations that should be undertaken to evaluate any potential benefit that may come from securitization?

1 A28. Yes. There are costs associated with the issuance of securitization bonds.
2 There are underwriting costs, legal and other costs including, perhaps, costs
3 associated with the Companies' need to restructure current debt requirements to
4 remove the phase-in deferral revenue from the assets that are pledged as
5 collateral for existing debt or other securities. These other costs may, depending
6 on what the securitization legislation requires, be included in the "principal" that
7 is, along with the interest cost, ultimately amortized through non-bypassable
8 securitization bond charges imposed on customers. In her estimate of the
9 consumer benefit that Companies' witness Hawkins describes in her testimony,
10 she has omitted these costs.

11 **Q29. What is your recommendation regarding securitization?**

12 A29. First, it is important to recognize that there are several open Commission
13 proceedings, like the remand phase of Case Nos. 08-917-EL-SSO, *et al.* and the
14 FAC audit proceedings that need to be finally resolved before the amount, if any,
15 of the phase-in deferral can be determined. Accordingly, I believe that any
16 consideration of the use of securitization of the type described by Companies'
17 witness Hawkins be deferred until such time that the final amount of the phase-in
18 deferral is fixed and known. Since it is my view that most of the consumer
19 benefit that Companies' witness Hawkins attributes to securitization can be
20 provided to consumers based on the Commission's precedent regarding the
21 carrying cost rate that attaches once the amortization process commences, I
22 recommend that this consumer benefit be maximized regardless of whether the
23 General Assembly might adopt additional securitization legislation. Once the

1 amount of the phase-in deferral is finally determined and if it appears that
2 incremental securitization legislation could provide consumers with incremental
3 net benefits (benefits that consider the cost of securitization and that are superior
4 to the benefits that are otherwise achievable without legislation), then the
5 Commission should conduct a workshop for the purposes of gathering
6 stakeholders' input regarding the content of any additional securitization
7 legislation that might be beneficial to consumers.

8 **Q30. Does this conclude your prepared direct testimony?**

9 A30. Yes. However, I reserve the right to update this testimony for responses to
10 discovery that are presently outstanding.

CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing *Prepared Direct Testimony of Joseph G. Bowser* has been sent via electronic mail this 25th day of July, 2011 to the following:

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