

**BEFORE
THE PUBLIC UTILITIES COMMISSION OF OHIO**

In the Matter of the Application of)	
The Dayton Power and Light Company for)	Case No. 16-395-EL-SSO
Approval of Its Electric Security Plan)	

In the Matter of the Application of)	
The Dayton Power and Light Company for)	Case No. 16-396-EL-ATA
Approval of Revised Tariffs)	

In the Matter of the Application of)	
The Dayton Power and Light Company for)	Case No. 16-397-EL-AAM
Approval of Certain Accounting Authority)	
Pursuant to Ohio Rev. Code § 4905.13)	

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

PUBLIC VERSION

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I. INTRODUCTION

Q1. Please state your name and business address.

A1. My name is 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.

1 **Q4. Please describe your professional experience.**

2 A4. I have been employed by McNees since 2005, where I focus on assisting IEU-Ohio
3 members address issues that affect the price and availability of utility services. As
4 part of my responsibilities, I provide IEU-Ohio members assistance as they
5 evaluate and act upon opportunities to secure value for their demand response
6 and other capabilities in the base residual auction ("BRA") and incremental
7 auctions conducted by PJM Interconnection, L.L.C. ("PJM") as part of the
8 Reliability Pricing Model ("RPM"). Prior to joining McNees, I worked with the Office
9 of the Ohio Consumers' Counsel ("OCC") as Director of Analytical Services. There
10 I managed the analysis of financial, accounting, and ratemaking issues associated
11 with utility regulatory filings. I also spent ten years at Northeast Utilities, where I
12 held positions in the Regulatory Planning and Accounting Departments, provided
13 litigation support in regulatory hearings, and assisted in the preparation of the
14 financial/technical documents filed with state and federal regulatory commissions.
15 I began my career with the Federal Energy Regulatory Commission ("FERC"),
16 where I led and conducted audits of gas and electric utilities in the Eastern and
17 Midwestern regions of the United States. I am a certified public accountant
18 (inactive) and am a member of the American Institute of Certified Public
19 Accountants and the Pennsylvania Institute of Certified Public Accountants.

20 **Q5. Have you previously submitted expert testimony before the Public Utilities**
21 **Commission of Ohio ("Commission" or "PUCO")?**

22 A5. Yes. Since 1996, I have submitted testimony as an expert on numerous regulatory
23 accounting issues and how those issues should be resolved for purposes of

1 establishing rates and charges of public utilities. A listing of cases in which I have
2 submitted expert testimony is attached as Exhibit JGB-1.

3 **Q6. What did you review for purposes of preparing your testimony?**

4 A6. I reviewed the application and pre-filed testimony submitted by The Dayton Power
5 and Light Company ("DP&L") on October 11, 2016, responses to discovery, DP&L
6 FERC Form 1 Reports, DP&L and DPL Inc. SEC 10-K and 10-Q Reports, AES
7 Corporation ("AES") SEC 10-K Reports, and entries issued by the Commission in
8 this proceeding.

9 My recommendations also reflect the knowledge I have accumulated throughout
10 my career.

11 **Q7. Have you summarized your recommendations?**

12 A7. Yes. I recommend that DP&L's proposal to implement a Clean Energy Rider
13 ("CER") and a Regulatory Compliance Rider ("RCR") be rejected by the
14 Commission. If the Commission nonetheless considers the RCR, then I
15 recommend that certain components of the RCR be rejected by the Commission,
16 for reasons I explain later in my testimony. I also recommend that the Commission
17 reject DP&L's Distribution Modernization Rider ("DMR") request.

18 **II. CLEAN ENERGY RIDER**

19 **Q8. What has DP&L proposed in this case with respect to a CER?**

20 A8. DP&L witness Hale indicated in prefiled testimony that DP&L is proposing that the
21 CER recover, among other things, any currently unknown environmental

1 compliance costs and decommissioning costs. As support for the rider, she states
2 that DP&L expects that it will incur environmental costs as a result of its current
3 ownership of generation assets, and that future regulations will be imposed that
4 will cause DP&L to incur additional compliance costs. Ms. Hale explained that
5 certain environmental expenses are related to activities involved in serving DP&L's
6 customers and were caused when the generation assets were owned by the
7 regulated entity and were for the benefit of DP&L's customers. Ms. Hale further
8 indicated that those generation assets were originally placed in service years and
9 sometimes decades before the generation market was deregulated.

10 Turning to decommissioning expenses, Ms. Hale explained that certain
11 decommissioning expenses are also related to activities involved in serving
12 DP&L's customers and were caused when the generation assets were owned by
13 the regulated entity and were for the benefit of DP&L's customers. Ms. Hale further
14 indicated that those generation assets were originally placed in service years and
15 sometimes decades before the generation market was deregulated. Ms. Hale
16 concluded that both the environmental expenses and the decommissioning
17 expenses are related to customers' prior use of and benefit from those generation
18 assets.

19 **Q9. What is the initial rate that DP&L is proposing for the CER?**

20 A9. DP&L has proposed that the CER initially be set at a rate of zero. Ms. Hale stated
21 in prefiled testimony that DP&L will apply for recovery of costs through the
22 nonbypassable CER in a separate proceeding once costs are known.

1 **Q10. Besides Ms. Hale's testimony, what other support has DP&L provided for its**
2 **proposal to implement the CER?**

3 A10. In response to interrogatories in IEU-Ohio Set 5 concerning the CER and the types
4 of decommissioning and environmental costs DP&L would seek to recover, DP&L
5 did not provide any specifics. For example, DP&L merely responded that it would
6 apply for cost recovery once the costs are known, in response to Interrogatory IEU-
7 5-16 asking whether requested decommissioning costs would be gross or net of
8 salvage. In response to Interrogatory IEU-5-17 asking whether decommissioning
9 costs included for recovery in the CER would be prorated to reflect DP&L's prior
10 recovery of decommissioning costs, the response was again that once the costs
11 are known, DP&L would apply for recovery. In response to Interrogatory IEU-5-
12 15, DP&L's response regarding environmental costs was that the environmental
13 compliance costs proposed for inclusion in the CER are currently unknown. The
14 responses to the referenced interrogatories are attached as Exhibit JGB-2, Exhibit
15 JGB-3, and Exhibit JGB-4.

16 **Q11. Has DP&L previously recovered costs of removal?**

17 A11. Yes. DP&L's last case related to depreciation was filed in 1991. At that time,
18 DP&L was regulated as a vertically integrated utility, with its generation rates fully
19 regulated. In that case, Case No. 91-414-EL-AIR, the Staff Report indicated at
20 page 18 that DP&L had filed a depreciation study in Case No. 91-433-EL-AAM for
21 all of its electric plant, including its generating assets. DP&L allocated its
22 depreciation reserve by function to individual plant accounts using the theoretical
23 reserve calculated in the depreciation study. In Case No. 91-414-EL-AIR, the Staff

1 conducted independent depreciation studies on the wholly-owned generating
2 plants, CG&E ("Cincinnati Gas and Electric Company")/DP&L ("CD") commonly-
3 owned generating plants, and CSP ("Columbus Southern Power
4 Company")/CG&E/DP&L ("CCD") commonly-owned plants. The Staff also
5 performed a study to establish accrual rates for the Zimmer station. The Staff
6 recommended new accrual rates for DP&L to use for book depreciation purposes
7 as shown on Staff Report Schedule 9.4. In addition to providing accrual rates for
8 distribution and transmission plant, Schedule 9.4 provided for each generating
9 plant asset by FERC account, the average service life, the net salvage percentage
10 and the depreciation accrual rate. Per Schedule 9.4 in the Staff Report, cost of
11 removal estimates were built into the net salvage percentages. A stipulation was
12 reached on November 6, 1991, which increased the depreciation accrual rate for
13 the Zimmer generating plant to 4.07% from the 2.97% that the Staff had
14 recommended in the Staff Report. In the Commission's Opinion and Order dated
15 January 22, 1992, the Commission adopted the stipulation, noting at page 10 that
16 the actual revenue requirement in the stipulation related to depreciation expense
17 was approximately \$24.1 million higher than the amount in the Staff Report. Based
18 on the foregoing, DP&L was recovering its estimated costs of removal as part of
19 its depreciation rates associated with the generation plants. The recovery of costs
20 of removal continued to be recovered in base rates through 2001, when rates were
21 unbundled. Rates were unbundled based on the then-existing rates. With the
22 unbundling of rates, there also was a one-time opportunity to receive certain
23 generation-related costs through stranded cost recovery for a period of time.

1 **Q12. What is your opinion on DP&L's CER request regarding decommissioning**
2 **costs?**

3 A12. Regarding Ms. Hale's assertion that certain generation assets have been serving
4 regulated customers for decades, it is important to note that DP&L was recovering
5 the estimated decommissioning costs (cost of removal) of those assets through
6 depreciation rates, thus compensating DP&L for those costs while the plants were
7 serving regulated customers. Now that the generating assets no longer serve
8 regulated customers, those customers should no longer be responsible for the
9 decommissioning costs through a regulated rate, as the assets are no longer
10 rendering public utility service for retail customers.

11 **Q13. What is your opinion on DP&L's CER request regarding future environmental**
12 **liabilities?**

13 A13. The Commission's Order in Case No. 13-2420-EL-UNC issued September 17,
14 2014, approving the transfer of DP&L's generation assets (by December 31, 2016)
15 to an Ohio generating company ("GENCO"), provided that all environmental
16 liabilities associated with the generating plants also be transferred to an Ohio
17 GENCO as part of the asset transfer transaction. Specifically, the Order states at
18 page 12 that "DP&L agreed to transfer the future environmental liabilities with its
19 generation assets, in order to carry out its separation" The language at page
20 12 goes on to state, "The Commission finds that DP&L should transfer the
21 environmental liabilities with the generation assets, consistent with DP&L's
22 representation that it has agreed to do so." And the Commission directed DP&L
23 to include "provisions in any contract or other agreement to divest the generation

1 assets which transfer all environmental liabilities with the assets and which fully
2 insulates ratepayers from any potential recovery of the costs of any such
3 environmental liabilities.” In the Asset Contribution Agreement (“ACA”) filed with
4 FERC in Case No. EC16-173-000 on August 25, 2016, DP&L indicated that the
5 environmental liabilities would be transferred with the generation assets to AES’
6 GENCO, AES Ohio Generation, LLC (“AES Ohio Gen”). Specifically, Section 2.03
7 of the ACA provides that the transferee shall assume and become responsible for
8 “all future Liabilities of Transferor related to Environmental Conditions arising
9 under or related to the Transferred Assets.” Accordingly, environmental costs
10 should not be included in the CER and billed to DP&L’s customers.

11 **Q14. What is your recommendation regarding the CER?**

12 A14. I recommend that the Commission deny DP&L’s proposal to implement the CER.
13 For the reasons discussed above, it would not be proper to assign the recovery of
14 these costs to DP&L’s distribution customers through this nonbypassable rider.

15 **III. REGULATORY COMPLIANCE RIDER**

16 **Q15. As a preliminary matter, has DP&L offered any substantive testimony in**
17 **support of its request for authorization of the RCR in its application or**
18 **amended application for an ESP?**

19 A15. No. Based on this failure to support its request with any application, IEU-Ohio has
20 filed a motion to dismiss DP&L’s request for authorization of the RCR because the
21 request does not comply with Commission rules.

1 **Q16. What is your understanding of the source of DP&L's request for**
2 **authorization of the RCR?**

3 A16. DP&L referenced the testimony of Mr. Teuscher that was filed in its pending
4 application to increase distribution rates.

5 **Q17. Has Mr. Teuscher been identified as a witness in the ESP case?**

6 A17. No.

7 **Q18. Given the fact that DP&L has failed to file support for its proposed rider, why**
8 **are you addressing it in your testimony?**

9 A18. Out of an abundance of caution. If the Commission strikes this portion of the
10 amended application seeking the RCR, then IEU-Ohio would withdraw any
11 testimony concerning that rider. Further, my discussion below of Mr. Teuscher's
12 testimony is descriptive only. I am not indicating that the Commission should
13 accept as accurate any of the assertions made by Mr. Teuscher and I am not
14 suggesting that my testimony should be used by the Commission as a basis for
15 approving either a rider or the recovery of any costs that DP&L is seeking in its
16 distribution rate case.

17 **Q19. What is your understanding of DP&L's proposed RCR?**

18 A19. As initially proposed by DP&L in its distribution rate case (Case Nos. 15-1830-EL-
19 AIR, *et al.*), this nonbypassable rider would recover costs that DP&L has incurred
20 or will incur as a result of matters outside DP&L's normal course of business,
21 including potential costs due to changes in legislation, changes in regulation,
22 and/or Commission orders that require all Ohio utilities to implement new

1 processes or to modify computer systems to address changes in the competitive
2 retail electric market. As DP&L witness Teuscher indicated in his prefiled
3 testimony in the distribution rate case, DP&L foresees that expenditures on
4 projects or items that would be eligible for inclusion in the RCR are atypical and
5 infrequent in nature, as opposed to ongoing administrative or operational costs.
6 Witness Teuscher indicated that the proposed RCR initially would include for
7 recovery the balances for several existing deferrals, to be recovered over a three-
8 year period. In addition, any future amounts beyond these initial deferral
9 recoveries to be included in the RCR would be required to be approved by the
10 Commission. The six separate deferral balances initially proposed for inclusion in
11 the RCR for recovery, and their balances as of September 30, 2015, are as follows:

- 12 (1) Consumer education campaign costs - \$3.0 million;
- 13 (2) Retail settlement system costs - \$3.1 million;
- 14 (3) Green pricing tariff costs - \$75,670;
- 15 (4) Bill format redesign costs incurred up to September 30, 2015 -
16 \$327,400;
- 17 (5) Generation separation costs incurred up to September 30, 2015 -
18 \$3.6 million; and
- 19 (6) Unbilled fuel costs incurred up to September 30, 2015 - \$13.36 million.

20 Witness Teuscher indicated that the deferral balances for items 4 and 5 above are
21 currently accruing carrying costs at DP&L's cost of debt, and that carrying costs at
22 the cost of debt will be included for the other four deferrals when collection of the
23 RCR commences.

1 In the future, DP&L proposes to include in the RCR future costs associated with
2 the following items:

- 3 (1) The remaining bill format redesign costs from October 1, 2015 to the
4 date of approval of the RC;
- 5 (2) The remaining generation separation costs from October 1, 2015 to
6 the date of approval of the RCR;
- 7 (3) Any other costs incurred as part of the Commission-ordered
8 investigation in Case No. 12-3151-EL-COI; and,
- 9 (4) Costs incurred as a result of future legislation or regulations that may
10 not be known at this time.

11 DP&L anticipates that it would file a rider update that includes new forecasted costs
12 and begin recovery with approval of the filing. DP&L would subsequently file a
13 true-up to adjust the rate once the amortization period for the forecasted costs has
14 ended, which would trigger a prudence review by the Commission.

15 **Q20. I understand that IEU-Ohio has filed a motion to dismiss the request for the**
16 **RCR. Do you also have an opinion whether authorization of any cost**
17 **recovery of components of the RCR is reasonable?**

18 A20. Yes. If the Commission approves the RCR as a term of the ESP, it should reject
19 four of the proposed RCR's components: (1) the recovery of the deferral for
20 unbilled fuel amounts; (2) the component that would permit future costs incurred
21 as a result of future legislation or regulations that are not known at this time; (3)
22 the recovery of the deferral for generation separation costs; and (4) the application

1 of carrying costs to the deferral balances for the items not currently accruing
2 carrying costs, when recovery of the RCR commences.

3 With respect to the deferral for unbilled fuel amounts, for ratemaking purposes fuel
4 has been a bypassable cost for shopping customers and, therefore, under the
5 principles of cost-causation, the recovery of this deferral should not be included in
6 the RCR, which is proposed to be a nonbypassable rider. The Commission
7 recognized similar treatment in its decision in DP&L's Reconciliation Rider–Non-
8 bypassable ("Rider RR-N") update in Case No. 15-43-EL-RDR. In that proceeding,
9 DP&L had proposed that it be permitted to recover certain deferred fuel costs
10 through Rider RR-N, a nonbypassable rider. The Commission Staff instead
11 recommended that standard service offer ("SSO") customers should bear the costs
12 because these fuel costs were incurred on behalf of the DP&L's SSO customers.
13 In an Order dated December 9, 2015, the Commission agreed with the Staff that
14 the fuel-related costs should be recovered through the bypassable FUEL Rider.

15 **Q21. Are there any other reasons why you recommend that the recovery of the**
16 **deferral for unbilled fuel amounts should be denied?**

17 A21. Yes, it appears that DP&L did not secure Commission approval to recognize this
18 deferral. In response to Interrogatory IEU-Ohio INT-8-2, DP&L indicated that the
19 fuel balance in question was not included in the balance of the FUEL Rider when
20 it was trued up for the final time, and that the balance actually originated with the
21 implementation of the FUEL Rider in Case No. 09-1012-EL-FAC, which became
22 effective January 1, 2010.

1 **Q22. Please discuss the other components of the RCR.**

2 A22. Turning to the RCR component that would include costs incurred as a result of
3 future legislation or regulations that are not known, I recommend that this provision
4 should be rejected, as it is premature. At this time, DP&L does not know the costs
5 nor the magnitude of the costs that it might seek for recovery. If DP&L incurs future
6 costs related to legislation or regulations which it believes it is entitled to recover,
7 DP&L would have existing means through which to seek recovery of its costs, such
8 as through a distribution rate case.

9 Regarding the recovery of generation separation costs, in the Commission's
10 Opinion and Order in Case No. 13-2420-EL-UNC, it authorized DP&L to defer all
11 financing costs, redemption costs, amendment fees, investment banking fees,
12 advisor costs, etc. (i.e. generation separation costs) that DP&L incurs to transfer
13 its generation assets. However, the Commission did not indicate that DP&L was
14 entitled to recovery of the deferrals, instead ordering that the costs will be subject
15 to Staff review. In my opinion, the deferral should not be recovered from DP&L
16 customers, as the generation assets are subject to competitive forces and have
17 been removed from regulated treatment.

18 Regarding the application of carrying costs to the deferral balances for the RCR
19 items not currently accruing carrying costs when recovery of the RCR commences,
20 this should be rejected, as the Commission did not authorize carrying costs on
21 these deferrals when the deferrals were approved.

1 In addition to the three components of the proposed RCR that I recommend be
2 rejected above, there is also another potential issue with carrying costs on the
3 generation separation deferral. Mr. Teuscher stated in prefiled testimony in the
4 distribution rate case that the deferral for generation separation costs is currently
5 accruing carrying costs, but it does not appear that the Commission approved
6 carrying costs on this deferral in its Order in Case No. 13-2420-EL-UNC. Even if
7 the Commission rejects my recommendation that the generation separation cost
8 recovery be denied, the related carrying charges on this component should be
9 disallowed.

10 In conclusion, my recommendation on the RCR is that the Commission should
11 reject the RCR for the reasons stated earlier. However, if the Commission
12 nonetheless considers the RCR, then I recommend that certain components of the
13 RCR be rejected by the Commission, for the reasons set forth above.

14 **IV. DISTRIBUTION MODERNIZATION RIDER (“DMR”)**

15 **Q23. What is the position of IEU-Ohio on the DMR?**

16 A23. IEU-Ohio witness Kevin Murray has recommended that the Commission should
17 reject DP&L’s request to implement the DMR. I provide additional support for the
18 rejection of the DMR.

19 **Q24. What additional support do you provide for rejecting the authorization of the** 20 **DMR?**

21 A24. In addition to the reasons Mr. Murray provides, my testimony offers the following:

1 (1) [REDACTED]

2 [REDACTED]

3 [REDACTED] The Commission has already determined that ratepayers are not
4 responsible for the acquisition premium.

5 (2) [REDACTED]

6 [REDACTED]

7 [REDACTED]

8 [REDACTED]

9 (3) The maintenance of investment grade credit ratings does not justify the
10 requested revenue requirement of the proposed DMR.

11 I discuss each of these recommendations in my testimony that follows.

12 1. [REDACTED]

13 [REDACTED]

14 [REDACTED] *The Commission has already determined that ratepayers are not*
15 *responsible for the acquisition premium.*

16 Q25. What are the proposed terms of the DMR?

17 A25. The proposed DMR is a nonbypassable rider designed to collect \$145 million per
18 year for a seven-year period, for a total of \$1.015 billion. [REDACTED]

19 [REDACTED]

20 [REDACTED]

21 [REDACTED]

22 [REDACTED]

23 [REDACTED]

1 [REDACTED]

2 [REDACTED]

3 [REDACTED]

4 **Q26. Does Mr. Jackson provide more specifics on DP&L's plan to pay down debt**
5 **at DPL Inc. and DP&L?**

6 A26. [REDACTED]

7 [REDACTED]

8 [REDACTED]

9 [REDACTED]

10 [REDACTED]

11 [REDACTED]

12 [REDACTED]

13 [REDACTED]

14 [REDACTED]

15 [REDACTED]

16 [REDACTED]

17

18 **Q27. What is your understanding of the circumstances that are driving DPL Inc.'s**
19 **alleged credit issues that in turn are driving the request for the DMR?**

20 A27. To place in proper context DP&L's request for the DMR, it is necessary to look
21 back to AES' acquisition of DPL Inc. and the resulting impacts of that acquisition
22 on DPL Inc. and to compare the financial situation of DPL Inc. to DP&L. Based on

1 that review, it is my opinion that the request for the DMR in this case is mainly a
2 result of debt that DPL Inc. took on as part of the merger.

3 **Q28. Please provide more background information on the merger.**

4 A28. On May 18, 2011, AES, its subsidiary Dolphin Subsidiary II, Inc. ("Dolphin"), along
5 with DPL Inc. and its subsidiary, DP&L, jointly filed an application seeking the
6 PUCO's approval of a merger between Dolphin and DPL Inc., in Case No. 11-
7 3002-EL-MER. Following the proposed merger, Dolphin would cease to exist and
8 DPL Inc. would become a wholly-owned subsidiary of AES. As part of the merger,
9 AES agreed to pay a large premium for DP&L which AES financed through a
10 highly-leveraged transaction. AES funded the purchase price with a \$1.05 billion
11 term loan, proceeds from a private offering of \$1.0 billion of notes, proceeds from
12 private offerings of \$450 million of 6.5% senior notes due 2016 and \$800 million of
13 7.25% senior notes due 2021, and temporary borrowings of \$251 million under a
14 revolving credit facility.

15 DP&L and the other applicants filed three stipulations in an effort to secure
16 Commission approval of the application. On November 22, 2011, the Commission
17 issued an order ("Merger Order") approving the three Stipulations without
18 modification.

19 On November 28, 2011, AES completed its acquisition of 100% of the common
20 stock of DPL Inc. for approximately \$3.5 billion. AES recognized net identifiable
21 assets acquired of \$994 million and goodwill of \$2,489 million, for total net assets
22 acquired of \$3.483 billion. A subsequent adjustment revised the net identifiable

1 assets acquired value to \$907.3 million and the goodwill value to \$2,576.3 million.
2 Stated another way, AES received approximately 29 cents worth of tangible assets
3 for each dollar it paid to acquire DPL Inc. Goodwill represents the price paid in
4 excess of the fair value of the assets acquired, or the future economic benefits
5 arising from the assets acquired in the acquisition that are not individually identified
6 and separately recognized. This price in excess of the fair value of the assets
7 acquired is also sometimes referred to as the acquisition premium. Goodwill is
8 evaluated for impairment at least annually. Goodwill may be impaired if
9 acquisitions do not perform as expected and in evaluating the potential impairment
10 of goodwill, estimates are made about revenues, capital expenditures, operating
11 cash flows, discount rates, growth rates, etc., based on forecasts, projections, and
12 market expectations of returns on similar assets.

13 In its 2011 SEC Form 10-K Report, AES reported that the factors primarily
14 contributing to it paying a price in excess of the fair value of the net assets included,
15 but were not limited to: (1) the ability to expand the U.S. utility platform in the
16 Midwest market; (2) the ability to capitalize on utility management experience
17 gained from Indianapolis Power and Light Company (an electric utility acquired by
18 AES in 2000); (3) enhanced ability to negotiate with suppliers of fuel and energy;
19 (4) the ability to capture value associated with AES' U.S. tax position; (5) a well-
20 positioned generating fleet; and (6) the ability of DPL Inc. to leverage its assembled
21 workforce to take advantage of growth opportunities. AES cautioned that its ability
22 to realize the benefits of DPL Inc.'s goodwill depended on the realization of
23 expected benefits resulting from a successful integration of DPL Inc. into AES'

existing operations and AES' ability to respond to the changes in the Ohio utility market. AES also stated that utilities in Ohio were continuing to face downward pressure on operating margins due to the evolving regulatory environment, which was moving toward a market-based competitive pricing mechanism, and declining energy prices were reducing operating margins.

Q29. What were the effects of the merger that were recorded on DPL Inc.'s books?

A29. The accounting impacts of the acquisition, including goodwill recognition, were "pushed down" to DPL Inc., resulting in the assets and liabilities of DPL Inc. being recorded at their respective fair values as of the November 28, 2011 merger date. Goodwill recognized by DPL Inc. was \$2,576.3 million. No goodwill was recorded on DP&L's books. In addition, Dolphin (a wholly-owned subsidiary of AES) issued \$1,250 million of debt, which, as a result of the merger of DPL Inc. and Dolphin, was assumed by DPL Inc.

Prior to the merger, as of December 31, 2010, DPL Inc.'s long-term debt outstanding was approximately \$1,324 million and after the merger, as of December 31, 2011, its long-term debt was approximately \$2,629 million. As of December 31, 2011, DPL Inc.'s capital structure was approximately 54% debt and 46% common equity.

Per the response to Interrogatory IGS-2-1, of the \$1.25 billion of debt at DPL Inc. associated with the merger, approximately \$730 million remained on the books of DPL Inc. as of December 31, 2015. As of August 31, 2016, DPL Inc.'s total

consolidated debt, which includes DP&L debt, was approximately \$1,914 million (response to Interrogatory IEU-Ohio INT-8-17, Attachment 1).

Q30. What were DPL Inc.'s credit ratings prior to the 2011 merger?

A30. As reported in DPL Inc.'s 2011 SEC 10-K Report, DPL Inc.'s credit ratings by Moody's were in a range of Baa1 to Baa2 from 2007 until the time of the merger in 2011. Effective with the merger, DPL Inc.'s credit rating was immediately downgraded by two credit agencies.

Q31. Was the Commission aware that the acquisition premium and leverage issues associated with the merger may result in requests to right the financial ship of DPL Inc.?

A31. Yes. IEU-Ohio had warned that the merger transaction could ultimately cause AES to seek cash flows from DP&L to service the debt taken on to fund the merger transaction and that retail customers would be the source of that cash. In its comments concerning the merger application, IEU-Ohio noted that "[t]he highly-leveraged transaction will potentially pressure AES to use its control over DPL to assure that DP&L and other DPL subsidiaries generate adequate cash flow to service the newly issued debt and that debt service can be expected to be drawn from the customers of DP&L."¹ Based on its concerns, IEU-Ohio recommended that this Commission, among other things, assure that the debt service obligations associated with the transaction not be funded through nonbypassable charges,

¹ *In the Matter of the Application of The AES Corporation, Dolphin Sub, Inc., DPL Inc. and The Dayton Power and Light Company for Consent and Approval for a Change of Control of The Dayton Power and Light Company*, Case No. 11-3002-EL-MER, Initial Comments of Industrial Energy Users-Ohio at 7 (July 18, 2011) ("Merger Case").

1 unduly prejudicial capacity charges that apply to shopping customers or their
2 CRES suppliers, or other restrictions on shopping.² DP&L and the other applicants
3 (DPL Inc. and AES) opposed conditions on the transaction, such as ring-fencing
4 (the financial separation of a regulated public utility from a parent company that
5 engages in non-regulated activities), arguing that conditions were unnecessary
6 because DP&L's securities would remain investment grade after the merger.³
7 Despite the warnings about the issues raised by the structure of the transaction,
8 the Commission failed to impose any ring-fencing on the revenue collected by
9 DP&L.

10 **Q32. How were questions about the potential costs of the merger and leverage**
11 **issues addressed?**

12 A32. AES, DPL Inc., and DP&L agreed in the *Merger Case* stipulation that "neither the
13 costs incurred directly related to the negotiation, approval and closing of the
14 merger nor any acquisition premium shall be eligible for inclusion in rates and
15 charges applicable to retail electric service provided by DP&L."⁴ Pursuant to terms
16 of a stipulation joined by the Commission Staff, the Commission also required that
17 DP&L maintain a capital structure that includes an equity ratio of at least 50% and
18 that DP&L would not have a negative retained earnings balance.⁵

² *Id.* at 11.

³ *Merger Case*, Applicants' Reply Comments at 5-6 (Aug. 18, 2011).

⁴ *Merger Case*, Finding and Order at 9 (Nov. 22, 2011 (summarizing the Oct. 26, 2011 stipulation of Applicants, Ohio Manufacturers' Association Energy Group ("OMAEG"), and the PUCO Staff).

⁵ *Id.*

1 Those restrictions were short-lived. In subsequent retail rate and corporate
2 restructuring proceedings, the Commission has approved nonbypassable
3 "stability" charges and temporarily waived the financial commitment to maintain an
4 equity ratio of at least 50%, which had been designed to protect retail customers
5 from the then-anticipated pushdown of the debt obligations that DPL Inc. was
6 saddled with as a result of the merger with AES. Additionally, DP&L, without relief
7 from the Commission, recently announced that its retained earnings were a
8 negative \$61 million following its decision to adjust certain generation-related asset
9 accounts for accounting impairments.

10 [REDACTED]
11 [REDACTED]
12 [REDACTED]
13 [REDACTED]

14 **Q33. Since the merger, what has DPL Inc. reported in the way of its ability to**
15 **generate revenues to support the related debt?**

16 **A33.** Less than a year after the merger, in the third quarter of 2012, DPL Inc. recognized
17 a goodwill impairment of \$1,817 million, representing over 70% of the goodwill that
18 had been recognized at the time of the merger. See 2012 SEC 10-K Report for
19 DPL Inc. The goodwill impairment resulted in a reduction in DPL Inc.'s retained
20 earnings and therefore common equity, which, all else being equal, increased DPL
21 Inc.'s debt to equity ratio. It is important to note that the goodwill is strictly related
22 to the merger transaction.

1 DPL Inc. recognized additional goodwill impairments in subsequent years, and as
2 of December 31, 2015, only four years after the merger took place, the original
3 goodwill balance of \$2,576 million for DPL Inc. was reduced to zero.

4 DPL Inc.'s retained earnings balance has been reduced from \$1,246 million on
5 December 31, 2010 (prior to the merger) to a deficit of \$2,335 million on December
6 31, 2015. Its capital structure has also become more heavily leveraged, increasing
7 from approximately 54% debt at the end of 2011 to approximately 92% debt as of
8 December 31, 2014. As of the end of 2015, common equity for DPL Inc. was a
9 negative amount of \$80 million. Exhibit JGB-5 provides financial data for DPL Inc.,
10 indicating how the merger and subsequent goodwill impairments at DPL Inc. have
11 negatively affected its debt and its debt to equity ratio.

12 **Q34. Why is a review of the impairments taken by DPL Inc. important to your**
13 **evaluation of the DMR?**

14 A34. DPL Inc. derives the bulk of its revenues from DP&L. Moreover, DPL Inc. is
15 significantly leveraged, largely as a result of the acquisition debt. The impairments
16 are evidence that revenues of DPL Inc. have been insufficient to support the value
17 of DPL Inc.'s goodwill assets. As I noted earlier, goodwill represents the future
18 economic benefits arising from the assets acquired in the acquisition that were not
19 individually identified and separately recognized. When the goodwill impairments
20 are recognized, it is an indication that the expected future economic benefits from
21 the assets are not as great as initially expected. At the same time, the impairments
22 do not reduce the debt on the books of DPL Inc. Thus, DPL Inc. has been retaining
23 debt obligations while holding assets that are not generating expected returns.

1 While there are alternatives to solving this problem, the one presented here is to
2 seek to increase DP&L's revenues through an authorization of the DMR.

3 **Q35.** [REDACTED]
4 [REDACTED]

5 **A35.** [REDACTED]
6 [REDACTED]

7 **Q36.** [REDACTED]
8 **A36.** [REDACTED]
9 [REDACTED]
10 [REDACTED]
11 [REDACTED]
12 [REDACTED]
13 [REDACTED]
14 [REDACTED]
15 [REDACTED]

16 **Q37. Is there any other evidence that points to the acquisition debt as the**
17 **problem?**

18 **A37.** [REDACTED]
19 [REDACTED]
20 [REDACTED]
21 [REDACTED]
22 [REDACTED]

1 [REDACTED]

2 [REDACTED]

3 [REDACTED]

4 Again, I reiterate that it is the debt assumed by DP&L's unregulated parent
5 company for a merger that has resulted in negative impacts on DPL Inc.'s balance
6 sheet. The Commission has already determined that an acquisition premium will
7 not be eligible for inclusion in rates and charges applicable to retail electric service
8 provided by DP&L. Based on the Commission's prior order in the Merger Case,
9 the DMR should be rejected.

10 **Q38. Does DP&L face the same debt-related issues as its parent, DPL Inc.?**

11 A38. No. DP&L's outstanding debt is at a lower level that is serviceable by DP&L if it is
12 not required to provide revenues to DPL Inc. to service and retire DPL's debt. For
13 example, for the last full calendar year of 2015, DP&L's interest expense was \$21
14 million on total long-term debt of \$763 million, and DP&L's operating income was
15 \$156 million. [REDACTED]

16 [REDACTED]

17 [REDACTED]

18 [REDACTED]

19 **Q39. Has DP&L been financially sound?**

20 A39. For the period 2010 through 2015, DP&L has had positive net income each year
21 and had a positive retained earnings balance of \$437 million as of December 31,
22 2015. As of December 31, 2015, DP&L's debt was approximately 38% of its capital

1 structure, for a strong leverage ratio of 0.38 to 1.00. DP&L has been strong enough
2 that between 2010 and 2015 DP&L paid out common stock dividends totaling
3 \$1.064 billion. All of this information indicates that DP&L was on sound financial
4 footing. Of course, these positive outcomes were generated in part by
5 nonbypassable charges. The continuation of that revenue stream has been limited
6 by the Ohio Supreme Court's determination that the stability charge approved in
7 DP&L's second ESP was unlawful.

8 **Q40. Does the Company point to any other measure as a basis to support**
9 **authorization of a DMR?**

10 A40. [REDACTED]
11 [REDACTED]
12 [REDACTED]

13 **Q41.** [REDACTED]

14 A41. [REDACTED]
15 [REDACTED]

16 Similarly, in DP&L's prior ESP proceeding (Case Nos. 12-426-EL-SSO, *et al*),
17 DP&L indicated, regarding the Rider SSR revenue requirement, an ROE range of
18 7% to 11% would be reasonable.

19 **Q42.** [REDACTED]

20 A42. [REDACTED]
21 [REDACTED]
22 [REDACTED]

1 [REDACTED]
2 [REDACTED]
3 [REDACTED]
4 Q43. [REDACTED]
5 A43. [REDACTED]
6 [REDACTED]
7 [REDACTED]
8 [REDACTED]
9 [REDACTED]
10 [REDACTED]
11 [REDACTED]
12 [REDACTED]
13 [REDACTED]
14 [REDACTED]
15 [REDACTED]
16 [REDACTED]
17 [REDACTED]
18 [REDACTED]
19 Q44. [REDACTED]
20 A44. [REDACTED]
21 [REDACTED]
22 [REDACTED]

1 [REDACTED]
2 [REDACTED]
3 [REDACTED]
4 Q45. [REDACTED]
5 [REDACTED]
6 A45. [REDACTED]
7 [REDACTED]
8 [REDACTED]
9 [REDACTED]
10 [REDACTED]
11 [REDACTED]
12 [REDACTED]
13 [REDACTED]
14 [REDACTED]
15 [REDACTED]
16 [REDACTED]
17 [REDACTED]
18 Q46. [REDACTED]
19 [REDACTED]
20 [REDACTED]
21 A46. [REDACTED]
22 [REDACTED]
23 [REDACTED]

1 [REDACTED]
2 [REDACTED]
3 [REDACTED]
4 [REDACTED]
5 [REDACTED]

6 Q47. [REDACTED]
7 [REDACTED]

8 A47. [REDACTED]
9 [REDACTED]
10 [REDACTED]
11 [REDACTED]
12 [REDACTED]
13 [REDACTED]
14 [REDACTED]
15 [REDACTED]
16 [REDACTED]
17 [REDACTED]
18 [REDACTED]
19 [REDACTED]

20 3. *The maintenance of investment grade ratings does not justify the requested*
21 *revenue requirement*

22 Q48. [REDACTED]
23 [REDACTED]

1 A48. [REDACTED]
2 [REDACTED]
3 [REDACTED]
4 [REDACTED]
5 [REDACTED]
6 [REDACTED]
7 [REDACTED]
8 [REDACTED]
9 [REDACTED]
10 [REDACTED]
11 [REDACTED]
12 [REDACTED]

13 **Q49. What are the implications of failing to have an investment grade rating?**

14 A49. Many companies have credit ratings below investment grade and continue to
15 attract capital and investors, although their long-term borrowings are at a higher
16 cost than investment grade long-term borrowings. The actual spreads on bonds
17 at investment grade ratings of Baa1 versus non-investment grade bonds rated Ba3
18 will vary over time, depending on, among other things, Treasury bond yields and
19 the term of the corporate bonds. For illustrative purposes, some recent issues of
20 10-year Baa1 bonds have been at a coupon rate of 4.875% and Ba3 10-year bonds
21 at 6.75%, a spread of 187.5 basis points. Even if the spread between Baa1 bonds
22 and Ba3 bonds was 200 basis points and DP&L's current long-term debt

1 outstanding is approximately \$780 million, this spread could be expected to cost
2 an additional \$15.6 million annually in interest expenses.

3 **V. CONCLUSION**

4 **Q50. Please summarize your recommendations.**

5 A50. I recommend that the Commission deny DP&L's proposal to implement the CER,
6 and that, at a minimum, it deny the proposal to implement certain components of
7 the RCR as I describe above. I also recommend that the Commission reject the
8 DMR as discussed above.

9 **Q51. Does this conclude your prepared direct testimony?**

10 A51. Yes. However, I reserve the right to update this testimony for any outstanding
11 discovery responses or additional information that is submitted by other parties in
12 this case.

CERTIFICATE OF SERVICE

In accordance with Rule 4901-1-05, Ohio Administrative Code, the PUCO's e-filing system will electronically serve notice of the filing of this document upon the following parties. In addition, I hereby certify that a service copy of the foregoing *Direct Testimony of Joseph G. Bowser on Behalf of Industrial Energy Users-Ohio* was sent by, or on behalf of, the undersigned counsel for IEU-Ohio to the following parties of record this 21st day of November, 2016, via electronic transmission.

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ATTORNEY EXAMINERS

CASES IN WHICH JOSEPH G. BOWSER HAS SUBMITTED TESTIMONY

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 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., including the remand phase of this proceeding.

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 The Dayton Power and Light Company for Approval of Its Electric Security Plan, Case Nos. 08-1094-EL-SSO, et al.

In the Matter of the Commission Review of the Capacity Charges of Ohio Power Company and Columbus Southern Power Company, Case No. 10-2929-EL-UNC.

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 Nos. 11-346-EL-SSO, et al.

In the Matter of the Application of Akron Thermal, Limited Partnership for an Emergency Increase in its Rates And Charges for Steam and Hot Water Service, Case Nos. 09-453-HT-AEM, et al.

In the Matter of the Application of The Dayton Power and Light Company to Establish a Standard Service Offer in the Form of an Electric Security Plan, Case Nos. 12-426-EL-SSO, et al.

In the Matter of the Fuel Adjustment Clauses for Columbus Southern Power Company and Ohio Power Company and Related Matters for 2010, Case Nos. 10-268-EL-FAC, et al.

In the Matter of the Application of Ohio Power Company for Authority to Establish a Standard Service Offer Pursuant to 4928.143, Revised Code, in the Form of an Electric Security Plan, Case Nos. 13-2385-EL-SSO, et al.

In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company for Authority to Recover Costs Associated with the Construction and Ultimate Operation of an Integrated Gasification Combined Cycle Electric Generating Facility, Case No. 05-376-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 Provide For a Standard Service Offer Pursuant to R.C. 4928.143 in the Form of an Electric Security Plan, Case No. 14-1297-EL-SSO.

In the Matter of the Petition of Jersey Central Power & Light Company Concerning a Proposal for an Economic Stimulus Infrastructure Investment Program and Associated Cost Recovery Mechanism, NJBPU Docket Nos. EO09010049, et al.

In the Matter of the Verified Petition of Jersey Central Power & Light Company for an Economic Stimulus Demand Response and Energy Efficiency Program and Associated Cost Recovery Mechanism, NJBPU Docket No. EO09010062.

5-16. Does DP&L propose to include for collection in the Clean Energy Rider gross decommissioning costs, decommissioning costs net of salvage, or some other net decommissioning cost? If DP&L proposes to include some other net value, explain how that net value would be calculated.

RESPONSE: General Objections Nos. 1 (relevance), 2 (unduly burdensome), 6 (calls for narrative answer), 7 (not in DP&L's possession or available on PUCO website), 12 (seeks information that DP&L does not know at this time). Subject to all general objections, DP&L states that the Clean Energy Rider is proposed to be set initially at zero. As explained in witness Hale's testimony, once those costs are known, the Company will apply for recovery of those costs through the non-bypassable Clean Energy Rider in a separate proceeding.

Witness Responsible: Claire Hale

5-17. Will the decommissioning costs proposed to be included in the Clean Energy Rider be prorated to reflect DP&L's prior recovery of decommissioning costs? If so, explain how DP&L will conduct that proration.

RESPONSE: General Objections Nos. 1 (relevance), 2 (unduly burdensome), 6 (calls for narrative answer), 7 (not in DP&L's possession or available on PUCO website), 12 (seeks information that DP&L does not know at this time). Subject to all general objections, DP&L states please see the Company's response to INT 5-16.

5-15. How do the environmental compliance costs proposed for inclusion in the Clean Energy Rider differ from the environmental compliance costs associated with the RER plants that would be recovered through DP&L's proposed RER?

RESPONSE: General Objections Nos. 2 (unduly burdensome), 5 (inspection of business records), 6 (calls for narrative answer), 10 (possession of DP&L's unregulated affiliate), 12 (seeks information that DP&L does not know at this time). DP&L further objects because the request is unduly burdensome, and can be performed by IEU. Subject to all general objections, DP&L states that the environmental compliance costs proposed for inclusion in the Clean Energy Rider are currently unknown. Any environmental compliance costs included in the current projections for the RER are based on known regulatory requirements. Upon proposing specific costs for recovery through the Clean Energy Rider, DP&L would confirm that such costs were not already included in the RER and would not seek double-recovery of those costs.

Witness Responsible: Claire Hale

DPL Inc.

2010 **2011** **2012** **2013** **2014** **2015** **30-Jun**
2016

(millions of dollars)

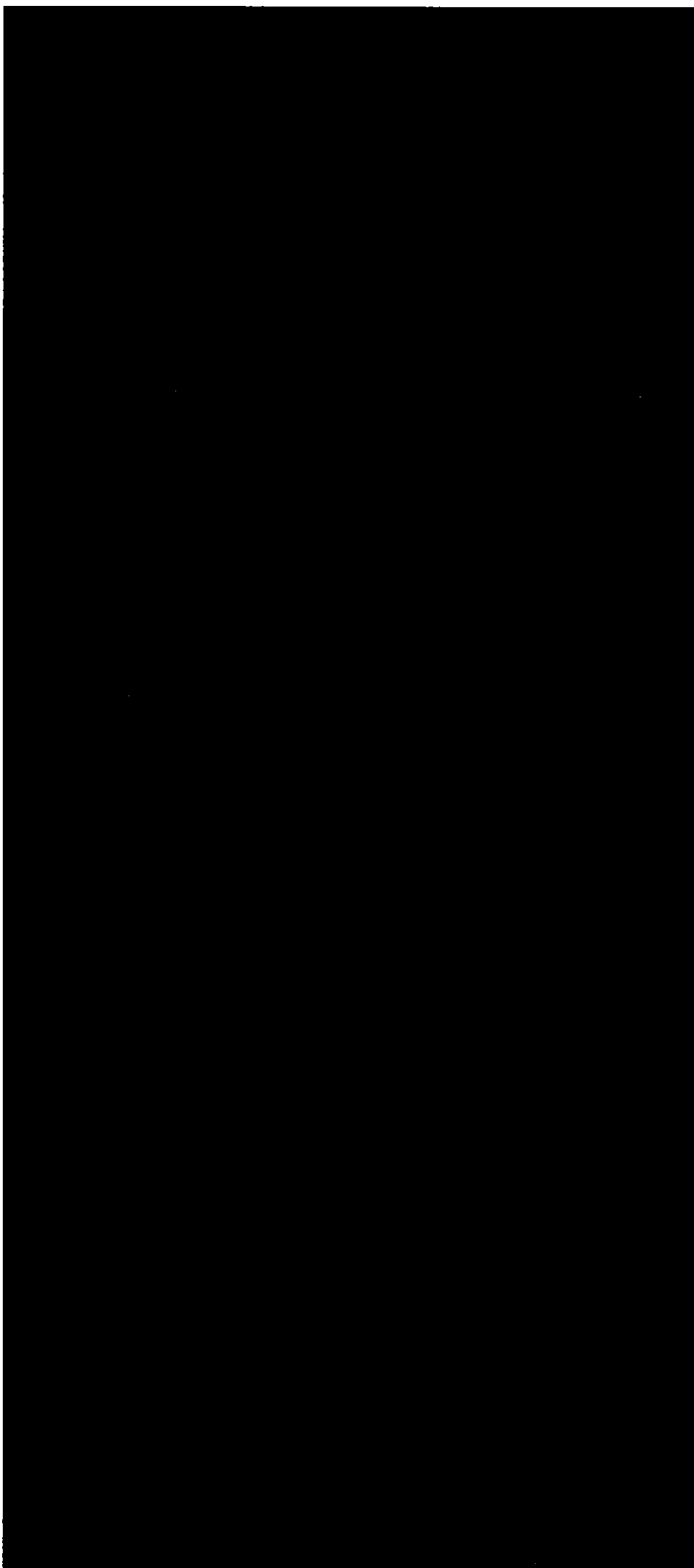
Capital Structure at year end

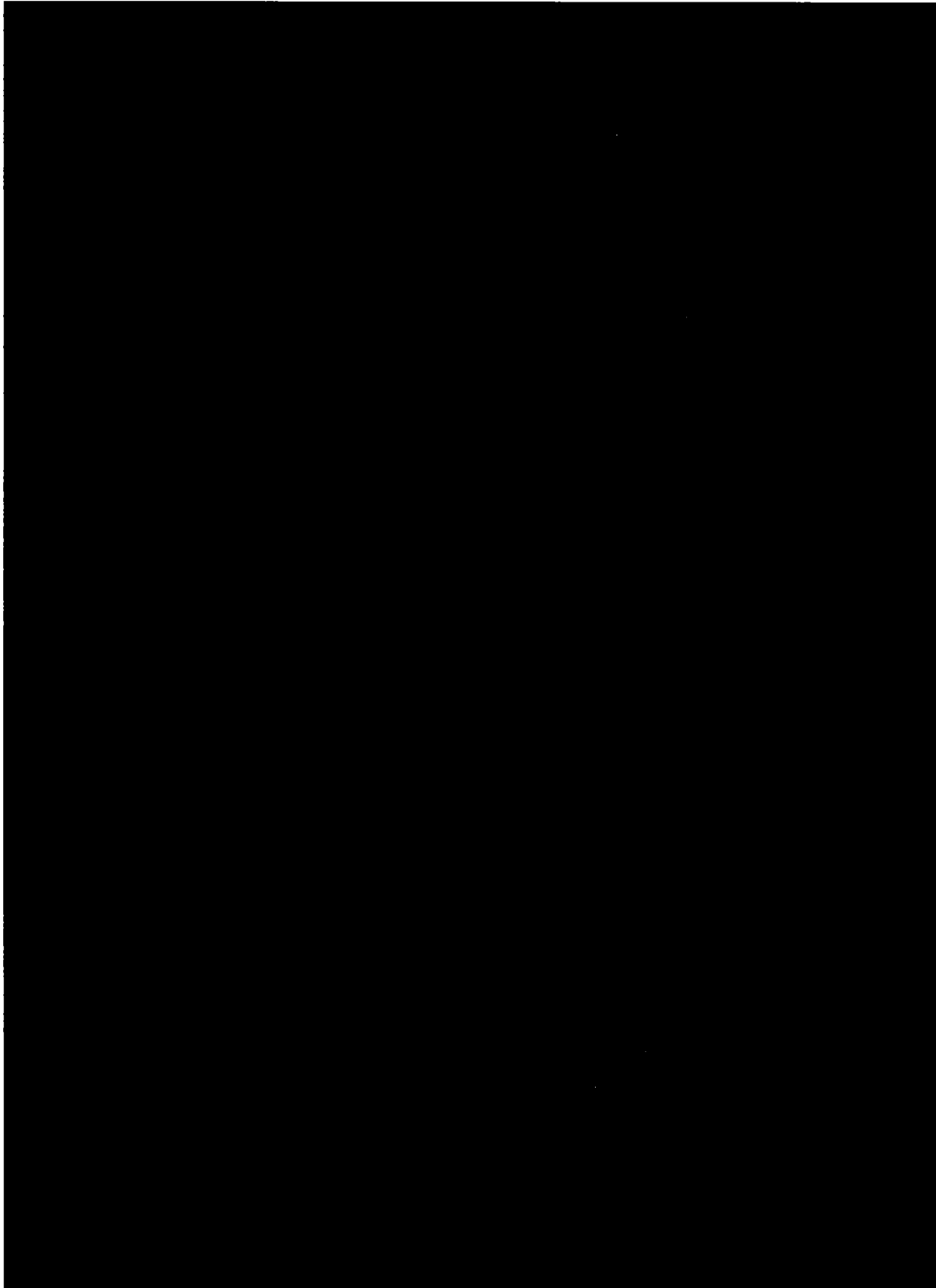
Long Term Debt	\$1,324.4	\$2,629.0	\$2,610.0	\$2,294.4	\$2,159.7	\$2,009.4	\$1,923.3
Preferred	\$22.9	\$18.4	\$18.4	\$18.4	\$18.4	\$18.4	\$18.4
Common Equity	\$1,218.5	\$2,230.7	\$426.8	\$240.0	\$148.2	(\$80.6)	(\$191.4)
Total	\$2,565.8	\$4,878.1	\$3,055.2	\$2,552.8	\$2,326.3	\$1,947.2	\$1,750.3
Long Term Debt	51.62%	53.89%	85.43%	89.88%	92.84%	103.19%	109.88%
Preferred	0.89%	0.38%	0.60%	0.72%	0.79%	0.94%	1.05%
Common Equity	47.49%	45.73%	13.97%	9.40%	6.37%	-4.14%	-10.94%
Total	100.00%	100.00%	100.00%	100.00%	100.00%	100.00%	100.00%
Retained Earnings	\$1,246.0	(\$6.2)	(\$1,806.0)	(\$2,022.0)	(\$2,096.7)	(\$2,335.7)	(\$2,440.7)
Goodwill Balance	\$0.0	\$2,576.3	\$759.1	\$452.8	\$317.0	\$0.0	\$0.0
Goodwill Impairments	\$0.0	\$0.0	\$1,817.2	\$306.3	\$135.8	\$317.0	\$0.0

Source of calendar year information is Annual SEC 10-K Reports

Source of June 30, 2016 information is SEC 10-Q Report for quarter ended June 30, 2016

The 2014 goodwill impairment was subsequently reclassified to discontinued operations





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in

Case No(s). 16-0395-EL-SSO, 16-0396-EL-ATA, 16-0397-EL-AAM

Summary: Testimony Direct Testimony of Joseph G. Bowser on Behalf of Industrial Energy Users-Ohio, PUBLIC VERSION electronically filed by Mr. Frank P Darr on behalf of Industrial Energy Users-Ohio