

EXHIBIT NO. _____

BEFORE
THE PUBLIC UTILITIES COMMISSION OF OHIO

In the Matter of the Commission's)	
Investigation of the Financial Impact of the)	
Tax Cuts and Jobs Act of 2017 on Regulated)	Case No. 18-47-AU-COI
Ohio Utility Companies.)	

DIRECT TESTIMONY OF
WILLIAM A. ALLEN
ON BEHALF OF
OHIO POWER COMPANY

Filed: June 15, 2018

BEFORE
THE PUBLIC UTILITIES COMMISSION OF OHIO
DIRECT TESTIMONY OF
WILLIAM A. ALLEN
ON BEHALF OF
OHIO POWER COMPANY

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

2 A. My name is William A. Allen, and my business address is 1 Riverside Plaza, Columbus,
3 Ohio 43215.

4 **Q. BY WHOM ARE YOU EMPLOYED AND WHAT IS YOUR POSITION?**

5 A. I am employed by the American Electric Power Service Corporation (AEPSC) as
6 Managing Director of Regulatory Case Management. AEPSC supplies engineering,
7 regulatory, financing, accounting, and planning and advisory services to the electric
8 operating companies of the American Electric Power System, one of which is Ohio Power
9 Company (“AEP Ohio” or “the Company”).

10 **Q. WOULD YOU PLEASE DESCRIBE YOUR EDUCATIONAL AND**
11 **PROFESSIONAL BACKGROUND?**

12 A. Yes. I received a Bachelor of Science in Nuclear Engineering from the University of
13 Cincinnati in 1996 and a Master of Business Administration from the Ohio State University
14 in 2004.

15 I was employed by AEPSC beginning in 1992 as a Coop Engineer in the Nuclear
16 Fuels, Safety and Analysis department and upon completing my degree in 1996 was hired
17 on a permanent basis in the Nuclear Fuel section of the same department. In January 1997,
18 the Nuclear Fuel section became a part of Indiana Michigan Power Company (I&M) due
19 to a corporate restructuring. In 1999, I transferred to the Business Planning section of the
20 Nuclear Generation Group as a Financial Analyst. In 2000, I transferred back to AEPSC

1 into the Regulatory Pricing and Analysis section as a Regulatory Consultant. In 2003, I
2 transferred into the Corporate Financial Forecasting department as a Senior Financial
3 Analyst. In 2007, I was promoted to the position of Director of Operating Company
4 Forecasts. In that role, I was primarily responsible for the supervision of the financial
5 forecasting and analysis of the AEP System's operating companies, including AEP Ohio.
6 In 2010, I transferred to the Regulatory Services Department as Director of Regulatory
7 Case Management. I was named to my current position in January 2013.

8 **Q. WHAT ARE YOUR RESPONSIBILITIES AS MANAGING DIRECTOR OF**
9 **REGULATORY CASE MANAGEMENT?**

10 A. I am primarily responsible for the supervision, oversight and preparation of major filings
11 with state utility commissions.

12 **Q. HAVE YOU PREVIOUSLY SUBMITTED TESTIMONY IN ANY REGULATORY**
13 **PROCEEDINGS?**

14 A. Yes. I have previously testified before the Public Utilities Commission of Ohio
15 (Commission) on behalf of AEP Ohio. I have also submitted testimony or testified before
16 the Michigan Public Service Commission, the Indiana Utility Regulatory Commission, the
17 Kentucky Public Service Commission, the West Virginia Public Service Commission and
18 the Virginia State Corporation Commission on behalf of various other electric operating
19 companies of the American Electric Power system.

20 **Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?**

1 A. My testimony discusses the impact of Tax Cuts and Jobs Act (TCJA) on AEP Ohio and
2 whether the Company should be required to establish deferred tax liability effective
3 January 1, 2018.

4 **Q. BRIEFLY DESCRIBE HOW THE TCJA IMPACTED THE COMPANY'S**
5 **ACCUMULATED DEFERRED FEDERAL INCOME TAXES (ADFIT) AND**
6 **CURRENT FEDERAL INCOME TAX.**

7 A. Among other things, the TCJA lowered the maximum Federal corporate income tax rate
8 from 35% to 21%. One major item impacted by this lower tax rate was the Company's
9 ADFIT balances. Approximately 40% of certain ADFIT balances on the books at
10 December 31, 2017, are now considered Excess ADFIT and booked as liabilities. There
11 are two categories of Excess ADFIT - "normalized" or "protected" and "non-normalized"
12 or "unprotected." These two categories are treated differently under the TCJA. The TCJA
13 requires that the protected excess ADFIT be amortized over "the remaining life of the
14 property which gave rise to the reserve for deferred taxes." This amortization period is
15 based on the average rate assumption method (ARAM). The amortization of this liability
16 began in January of 2018. Unprotected Excess ADFIT balances do not have any IRS
17 limitation placed on them and the distribution related balances will remain on the
18 Company's books until there is an order from this Commission related to their treatment.
19 On a going-forward basis, of course, the TCJA has reduced the level of Federal Corporate
20 income taxes that the Companies pay. The Company's federal income tax will be 40% less
21 than it otherwise would have been on the same level of operating income.

1 **Q. SHOULD THE COMMISSION CONTINUE TO REQUIRE AEP OHIO TO DEFER**
2 **AS A REGULATORY LIABILITY ALL SAVINGS ASSOCIATED WITH THE**
3 **TCJA?**

4 A. No. As an initial matter, any deferral should be limited to the Ohio jurisdictional
5 distribution function of AEP Ohio's business. Tax savings associated with AEP Ohio's
6 transmission function are being addressed in FERC Case No. ER18-1202-000 and the
7 associated OATT savings are currently being reflected in the Basic Transmission Cost
8 Recovery rider. And generation-related costs reflected in the context of riders approved
9 through the Company's Electric Security Plan (ESP) have already been addressed outside
10 the context of this proceeding.

11 When the Commission establishes just and reasonable going forward levels of
12 revenue and rates as part of a base rate case, its decision is based on a thorough
13 examination of a utility's costs, revenues, rate base and earned return on equity at a point
14 in time. Federal income tax expense is just one of the many costs that comprise a utility's
15 cost structure. As a general proposition, changing a utility's rates based on a review of one
16 isolated change in cost is not a sound approach. Income taxes are an expense, but they are
17 not a primary or direct expense. Income taxes only become an expense when a utility has
18 generated income subject to taxation. At a minimum, any tax savings for the distribution
19 function should only be deferred as a regulatory liability if the Company is earning above
20 a just and reasonable level from a jurisdictional cost of service perspective.

21 **Q. ARE THERE CIRCUMSTANCES IN WHICH THE SAVINGS ASSOCIATED**
22 **WITH THE TCJA AS OF JANUARY 2018 SHOULD BE DEFERRED OR**
23 **REFLECTED IN CURRENT RATES?**

1 A. Yes. AEP Ohio has certain riders that include a return component and for each of those
2 riders the Company has made adjustments to reflect the savings associated with the
3 reduction in the federal tax rate. These riders are 1) the Distribution Investment Rider
4 (DIR), 2) the gridSMART Phase II rider, 3) the Enhanced Service Reliability Rider
5 (ESRR), 4) the Energy Efficiency Peak Demand (EE/PDR) rider and 5) the Alternative
6 Energy Rider (AER). In each case, these riders are designed to recover current costs and
7 provide a return on the utility's investment (income). As a result of the structure of these
8 riders it is appropriate to reflect the reduction in the federal tax rate because the income
9 taxes are a result of the income generated by the rider after factoring in current expenses.
10 The Company has worked with the Staff to update these rates charged to customers to
11 reflect tax savings during the pendency of this proceeding.

12 **Q. WHAT LEVEL OF DISTRIBUTION RELATED EXCESS ADFIT IS**
13 **CURRENTLTLY DEFERRED ON AEP OHIO'S BOOKS?**

14 A. As of May 31, 2018 the estimated deferred balances of normalized excess ADFIT and non-
15 normalized excess ADFIT were \$278 million and \$178 million, respectively. These values
16 are revenue amounts which includes a gross-up for federal income taxes.

17 **Q. SHOULD ANY ADDITIONAL SAVINGS ASSOCIATED WITH THE TCJA BE**
18 **DEFFERED BY AEP OHIO AS A REGULATORY LIABILITY?**

19 A. No. The remaining tax savings are the result of revenues that are not designed to produce
20 a specified level of earnings based upon the current level of expenses that the Company is
21 incurring. These revenues are split into two categories – riders without a return component
22 and base rates. Riders without a return component do not include an element of current
23 period tax expense so deferring any tax savings associated these riders is not necessary.

1 Base rates were designed to produce revenues sufficient to allow AEP Ohio to recover its
2 distribution costs and have a reasonable opportunity to earn its authorized rate of return
3 based upon a comprehensive snap shot in time of the Company's jurisdictional cost of
4 service – in this case June 1, 2010 through May 31, 2011 using a date certain for rate base
5 of August 31, 2010. Since that time any number of costs have increased or decreased,
6 customer load has changed, and assets have been placed in service or retired. Each of these
7 changes impacts the Company's ability to earn its authorized return on equity.
8 Consequently, base rate changes should not be unilaterally implemented by the
9 Commission using isolated and selective cost items as the basis but instead should be based
10 upon a comprehensive review of the Company's jurisdictional costs and revenues.

11 **Q. HAS AEP OHIO OPENED A SEPARATE DOCKET FOR RESOLUTION OF ITS**
12 **TAX ISSUES?**

13 A. Yes. AEP Ohio established a new docket (Case No. 18-1007-EL-UNC) in order to address
14 the remaining issues relating to the TCJA as they relate to the Company's Ohio retail rates.
15 The Company requested a procedural schedule in that case to move forward in parallel with
16 this generic investigation in order to move the Company-specific TCJA issues forward
17 efficiently. The Commission issued an Entry on June 12, 2018 in the 18-1007 case
18 establishing a procedural schedule. While the Company reserves the right to fully
19 participate in this generic investigation in order to preserve and advance its positions, the
20 Company intends to pursue resolution of the remaining Company-specific TCJA issues in
21 that docket. For example, while I generally set forth above the recommendation that the
22 Commission should first determine the earned return on equity for its distribution service
23 to determine whether a deferral or rate adjustment should be made for a tax savings during

1 the same period (*i.e.*, only establish a deferral where and to the extent that the Company
2 earns a just and reasonable level), the Company plans to utilize the 18-1007 docket to
3 pursue its demonstration that such a deferral is not justified.

4 **Q. DOES THIS COMPLETE YOUR DIRECT TESTIMONY?**

5 A. Yes.

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 *Ohio Power Company's Direct Testimony of William A. Allen* was sent by, or on behalf of, the undersigned counsel to the following parties of record this 15th day of June 2018, via electronic transmission.

/s/ Steven T. Nourse
Steven T. Nourse

EMAIL SERVICE LIST

Amy.Spiller@duke-energy.com; campbell@whitt-sturtevant.com; bbingaman@firstenergycorp.com; Bryce.mckenney@occ.ohio.gov; cdunn@firstenergycorp.com; cblend@aep.com; christopher.healey@occ.ohio.gov; cmooney@ohiopartners.org; Dresse;@carpenterlipps.com; dsawmiller@nrdc.org; dstinson@bricker.com; Elizabeth.Watts@duke-energy.com; fdarr@mwncmh.com; gkrassen@bricker.com; Jeanne.Kingery@duke-energy.com; jkylercohn@BKLawfirm.com; jfinnigan@edf.org; joliker@igsenergy.com; Josephclark@nisource.com; Kathy.L.Buckley@verizon.com; Kevin.moore@occ.ohio.gov; Bojko@carpenterlipps.com;	kboehm@BKLawfirm.com; mfleisher@elpc.org; whitt@whitt-sturtevant.com; mpritchard@mwncmh.com; mkurtz@BKLawfirm.com; mlozich@securustechologies.com; mnugent@igsenergy.com; Michael.schuler@aes.com; mleppla@theoec.org; mwhelan@egas.net; neil.waggoner@sierraclub.org; paul@carpenterlipps.com; randall.griffin@aes.com; glover@whitt-sturtevant.com; rocco.dascenzo@duke-energy.com; selisar@mwncmh.com; sseiple@nisource.com; stnourse@aep.com; trhayslaw@gmail.com; william.wright@ohioattorneygeneral.gov; Zachary.Woltz@occ.ohio.gov;
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Summary: Testimony Direct Testimony of William A. Allen on Behalf of Ohio Power Company
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