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JOINT CUSTOMERS GROUP'S PRELIMINARY CHALLENGES REGARDING THE AEP EAST 2019 OpCo AND 2019 TRANSCO TRANSMISSION FORMULA RATE UPDATES

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VIA E-MAIL TO: slburbure@aep.com

RE: AEP East Operating Companies and AEP East Transmission Companies In the AEP Zone - Joint Customer Group Preliminary Challenges to 2018 Annual Transmission Formula Rate True-up as Presented in the 2019 Annual Update

Dear Ms. Burbure:

Pursuant to the Formula Rate Implementation Protocols for the AEP East Operating Companies and the AEP Transmission Companies in the AEP Zone (Attachments H-14A and H-20A, respectively, to the PJM Open Access Transmission Tariff), the Joint Customer Group ("JCG")[1] hereby notifies American Electric Power Service Corp. ("AEP") of Preliminary Challenges to certain components of (i) the AEP East Operating Companies' ("OpCos") Annual Transmission Formula Rate True-up for 2018, which was originally filed with the Federal Energy Regulatory Commission ("FERC") on May 28, 2019 in Docket No. ER17-405-000 ("2019 OpCo Update")[2], and (ii) the AEP East Transmission Companies' ("TransCos") Formula Rate Annual Update for 2018, which was filed with FERC on May 28, 2019 in Docket No. ER17-406-000 ("2019 Transco Update").

The items that are the subject of JCG's Preliminary Challenges are briefly described below and have been divided into two groups. The first group outlines those issues JCG believes have been resolved based on AEP's responses to the information requests. To the extent AEP disagrees with JCG's assertion that a certain issue has been resolved, JCG hereby states a Preliminary Challenge with respect to that issue. The second group of issues outlines those matters that JCG considers to be unresolved

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1 The Joint Customer Group consists of American Municipal Power, Inc., Blue Ridge Power Agency, Craig-Botetourt Electric Cooperative, Indiana Municipal Power Agency, Indiana Michigan Municipal Distributors Association, Old Dominion Electric Cooperative, and Wabash Valley Power Association.

2 AEP East subsequently resubmitted their filing on July 10, 2019 to reflect corrections for certain errors discovered in the 2018 OpCo Update.

and, consequently, JCG states a Preliminary Challenge under the Formula Rate Implementation Protocols with respect to each of these issues.

For clarity, we identify each Preliminary Challenge with the designator "JCG," the year of the update that includes the challenged items ("2018"), and a title. Unless specified, each Preliminary Challenge relates both to the AEP East OpCos and the AEP East TransCos.

Potential Challenges Resolved by Agreement

JCG-2018-01 Incorrect Accounting for Certain Revenue Credits

AEP's response to JI 1-50 states "There were four payments made to Operating Companies for ROW use by utility pipelines. As shown in JI-50 Attachment 1, two of these items were for rental payments on non-transmission plant, and would not be a revenue credit to the formula rate of the receiving company. The other two payments were for assets owned by Ohio Power Company's transmission function and should be credits as reported on W/S E to OPCo formula rate. However, in the preparation of this response, it was determined that one of the payments was incorrectly recorded to account 421. Because this payment should have been a revenue credit to the formula rate the Company will apply this amount ($14,430), and associated interest, as part of the true-up adjustment to be included in 2020 projected revenue requirement."

JCG-2018-02 Incorrect Jurisdiction Designation

AEP's response to JI Set 1-82 states, "The use of the phrase 'Kingsport Jurisdiction' is incorrect and should say 'Tennessee Jurisdiction.' This will be corrected on the Projected and Actual formulas filed in the future updates."

JCG-2018-03 Incorrect Depreciation Rate

AEP's response to JI Set 1-254 states, "AEP agrees that Worksheet P for AEP Kentucky Transmission Company's working version of the formula template should reflect a depreciation rate 1.44% for plant account 350.1, and will correct this in the next update filing. Please note that the rate is properly presented in the corresponding page for Worksheet P found in Attachment H-20B of the PJM OATT."

Unresolved Issues Designated as Preliminary Challenges

JCG-2018-04 Public Service Commission Fees Included in Taxes Other Than Income Taxes

AEP has included Public Service Commission fees in FERC Account No. 408, Taxes other than income taxes, rather than in FERC Account No. 928, Regulatory commission expenses. In AEP's response to data request no. JI2-4, AEP states: "The expenses that are included in Account 408 include fees that are assessed to the Companies based on the Companies' revenues. These are consistent with FERC USoA instructions, which state that Account 408.1 shall 'include those taxes other than income taxes which relate to utility operating income.'" Public Service Commission fees, however, are not taxes but rather fees AEP describes as "costs incurred due to being a public utility in the state," and on that basis the fees should be charged to FERC Account No. 928. AEP's decision not to include PSC fees in FERC Account No. 928 appears based on a misinterpretation of the scope of FERC Account No. 928. AEP stated that "[t]e public commission fees are not incurred by the utility solely in connection with formal cases before the Commissions." The USoA instructions are clear, however, that there are types of expenses included in Account 928 other than formal cases. The instructions for FERC Account 928 explicitly state: "A. This account shall include all expenses (except pay of regular employees only incidentally engaged in such work) properly includible in utility operating expenses, incurred by the utility in connection with formal cases before regulatory commissions, or other regulatory bodies, or cases in which such a body is a party, **including payments made to a regulatory commission for fees assessed against the utility for pay and expenses of such commission**, its officers, agents, and employees, and also including payments made to the United States for the administration of the Federal Power Act." This clearly encompasses the PSC fees that AEP has instead incorrectly charged to Account 408. Other pertinent responses are AEP's responses to data requests no. JI 1-25 and JI 1-95.

JCG-2018-05 Inclusion of GreenHat Default Charges in Transmission Expense Accounts

Please refer to AEP's responses to data request JI2-5 and JI-07_Attachment 1.xlsx JI 1-26, 1-153 (Attachment 1, tab Query), 2-71, 2-72, 2-73). In AEP's response to data request no. JI2-5 AEP stated that "[t]he AEP East Operating Companies record these expenses in a 561.4 account because of their designation as load serving entities in PJM. The AEP East Transmission Companies, and Ohio Power Company, recorded these expense [*sic*] as a miscellaneous cost in account 566."

First, APCo, I&M, OPCo, and WPCo have recorded these costs as regulatory assets. AEP has not indicated that it has sought and received FERC approval for the recovery of these regulatory assets in its wholesale transmission rates. Commission precedent requires that the amortization of regulatory assets in rates require FERC approval.[3]

Second, AEP has inappropriately recorded these default charges to Accounts 561.4 and 566. Given that these costs are directly related to Financial Transmission Rights ("FTRs"), these expenses should have been recorded to FERC Account No. 575.3 (Transmission Rights Market Facilitation - which is defined as including "the cost of labor, materials used and expenses incurred to manage the allocation and auction of transmission rights").

And third, since AEP recorded the charges or credits associated with Transmission Rights to Account 555 (Purchased Power)[4], for consistency purposes, it would be appropriate to also record the expenses associated with the Greenhat default to Account 555, which is not recoverable in the transmission formula. If there no charges or credits associated with Transmission Rights recorded to Account 555 (as the case may be for the Trancos), the expenses for the Greenhat default should be recorded to whichever account that is utilized for the recording of charges or credits related to the Transmission Rights (e.g., Account 456.1 - Revenues from Transmission of Electricity of Others and should not be included in the transmission revenue requirement.

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[3] In *Piedmont Municipal Power Agency v. Duke Energy Carolinas, LLC,* 162 FERC ¶ 61,109, at PP 34-35 (2018), the Commission found that "[t]he collection of any regulatory asset that was recorded in Account 182.3 and included in rate base and/or included in expense requires submitting a section 205 filing for approval by the Commission."

[4] For example, see Appalachian Power Company's 2018 FERC Form 1, page 397, line 4.

JCG-2018-06 Treatment of CIAC Plant in Rate Base

Please refer to AEP's responses to data request nos. JI 1-28, 2-8, 2-9, 2-10, 2-11, 2-12. AEP's response to data request nos. JI 1-28 and JI 2-8 show the debits and credits set up to record CIAC. AEP's response to data request no. JI2-8 indicates that AEP created a CIAC-related credit to FERC Account No. 107 – CWIP; therefore, this indicates that a contra asset has been established for CIAC. AEP's response to data request no. JI 2-9, however, indicates that rather than using a contra asset, AEP is tracking CIAC by project ID and recording it in property records. This response indicates that in order for CIAC to have no impact on the revenue requirement calculations in the formula rate, the company would have to create a corresponding credit to its property records to properly remove the effect of CIAC. It remains unclear, however, whether AEP has properly excluded the plant and associated depreciation related to CIAC from the formula rate templates. If CIAC plant is indeed included in rate base then Joint Customer Group challenges such inclusion on the basis that it is contrary to FERC rate making principles.

JCG-2018-07 Incorrect Treatment of CIAC-related ADIT and Deficient ADIT in the Formula Rate Templates

Please refer to AEP's response to data request no. JI2-35 and other associated responses to data request nos. JI 1-91, 1-112, 1-133, 1-183, 1-200, 1-215, 1-237, JI2-46, 2-60, 2-90, 2-95, 2-96 and 2-98. The CIAC amount including gross-up is taxable for income tax purposes. All CIAC associated amounts (plant, accumulated depreciation, ADIT, etc.) are to be excluded from transmission formula rates since the CIAC agreements are not part of the formula rate and only apply to the individual contributor that the CIAC agreement relates. CIAC is not to be socialized for FERC rate making purposes. Specifically, Commission precedent[5] finds that

> consistent with our direction in the First Compliance Order, to the extent that Florida Parties propose to account for or recover tax effects of a CIAC, we require the associated tax effect be considered as part of the total project cost in the cost benefit analysis, and therefore include the calculation in their cost recovery provisions. We also remind Florida Parties that the opportunity for recovery of the tax effects of CIACs is at the time that the utility seeks the required Commission approval for that lump sum payment, and **may not be recovered at some later point outside of the transaction from entities other than the contributor** [bold added].

AEP's treatment of the CIAC-related ADIT is inconsistent with the FERC guidance referenced above. AEP's inclusion of the CIAC-related ADIT in rate base essentially recovers the tax effects of CIACs at a later point from entities that were not parties to the CIAC agreement (*i.e.*, socialized to all transmission customers), which is exactly the opposite of the cited FERC precedent. Therefore, the Joint Customer Group challenge the inclusion of CIAC-related ADIT in transmission rate base and any associated deficient CIAC-related ADIT resulting from the TCJA that has or will be amortized through the income tax allowance.

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[5] Tampa Electric Co., et al., 151 FERC ¶ 61,013, at P 65, n.115 (2015) (citing American Mun. Power-Ohio, Inc. v. Ohio Edison Co., 57 FERC ¶ 61,358 (1991), reh'g denied, 58 FERC ¶ 61,182 (1992) and Trailblazer Pipeline Co., 55 FERC ¶ 61,050 (1991)) (stating, "whether taxes are grossed-up or spread out over time, the contributor making the CIAC would pay the full cost of its contribution, including its tax effect, which would be determined as part of that transaction filed with the Commission for approval").

JCG-2018-08 Failure to Provide Revenue Credits Related to the Belmont Office Service Center

In reference to AEP's response to JI 1-50, AEP states that the $47,000 of revenue recorded in FERC Account No. 454, associated with the Belmont Office Service Center, is "non-transmission plant" related. In its response to data request no. JI2-16, however, AEP states that "[t]he assets for the Belmont Office Service Center are recorded in FERC accounts 35300 – Station Equipment, 38900 – Land, 39000 – Structures & Improvements, 39400 – Tools, 39700 – Communication Equipment, and 39800 – Miscellaneous Equipment." These Transmission and General Plant accounts were charged through the formula rate template, so the related revenues should be credited in the formula rate template in the same manner in which the assets were included in the template. The revenue portion associated with Transmission should be allocated using a "DA" allocator (as shown on the "TCOS" Tab, Line 2 – Revenue Credits allocated on "DA") and the General Plant revenue portion should be allocated using a "Wages and Salaries" allocator. "As a general rule, the equitable treatment of costs *vis-à-vis* revenue credits is as follows: if certain costs are included (or excluded) in the revenue requirement, then revenue credits associated with those costs should be included (or excluded) as well (and *vice versa*). If costs are included but related revenue credits are excluded, then the resulting rate results in double-recovery. If costs are excluded but related revenue credits are included, then the resulting rate is not fully compensatory to the utility" (*Constellation Mystic Power, LLC*, 165 FERC ¶ 61,267 at n. 303 (2018)).

JCG-2018-09 Lack of Support for TCJA Remeasurement Balances (Including Lack of Support for (i) Excess and Deficient ADIT Items Being Allocated, and (ii) Classification of Protected and Unprotected Excess and Deficient ADIT)

Please refer to AEP's responses to data request nos. JI-62 and JI 2-18.

With reference to AEP's response to JI1-62(a), the Company's response included JI Set 1-62 Attachment, which includes multiple items that do not appear to fully reflect the remeasurements necessitated by the 2017 TCJA's 40% reduction in the FIT tax rate from 35% to 21%. It is logical to expect that the post-remeasurement balance for each item in FERC Accounts 190, 282 and 283 would be approximately 40% lower than the pre-remeasurement ADIT balances, and that the Excess/Deficient balance to be transferred to a regulatory liability or regulatory asset account would reflect approximately 40% of the pre-remeasurement balances. Insofar as the post-remeasurement balances are not in line with the expected balances, AEP should have explained the variances. Because it has not done so, the Joint Customer Group challenges this item.

With reference to AEP's response to JI-62(b), AEP's inclusion of the remeasured Excess/Deficient ADIT in FERC Accounts 190, 282 and 283 (rather than FERC Account Nos. 182.3 or 254) is inconsistent with the guidance provided in FERC Order No. 144 and, more recently, FERC Order No. 864[6].FERC Order 864 requires the classification of the Excess/Deficient ADIT to be recorded in FERC Accounts 254 and 182.3 and the inclusion of specific adjustments in the formulas account for the unamortized balances of the

[6] *Public Utility Transmission Rate Changes to Addrss Accumulated Deferred Income Taxes*, 169 FERC ¶ 61, 139 at P. 31 (November 21, 2019).

Excess/Deficient ADIT as reductions to rate base. AEP has not complied with the requirements of Order 864 as it relates to the recording of the Excess/Deficient ADIT.

With reference to AEP's response to JI1-62(d), AEP stated "Segregation of the excess ADFIT balances between protected and unprotected is determined by the Company's software related to depreciable property using the Average Rate Assumption Methodology ("ARAM"); once the software has determined the appropriate level of excess protected ADFIT based upon depreciable property, the remaining excess ADFIT is unprotected." AEP's statement that their software determines whether an item is protected or unprotected is incorrect. The PowerTax software does not and cannot determine whether an item is protected or unprotected for the (Excess)/Deficient ADIT (EADIT) balances for each property item. Whether an item is protected is determined based on whether the specific property item is subject to the IRC and IRS section 168, related to accelerated depreciation. All basis adjustments, repair deductions and non-section 168 related property are not "Protected." Only property subject to section 168, related to accelerated depreciation, is subject to ARAM amortization. All other property-related EADIT balances may be amortized over any reasonable period. AEP has not provided sufficient supporting documents or data to support either (i) AEP's position on the categorization of each ADIT item as "protected" or "unprotected," or (ii) the Excess/Deficient ADIT balance related to each. Also, there are various items (SFAS 109 items) which are balance sheet-related only and which therefore should be excluded from the rate calculations under the formula rate templates. It appears that AEP, however, has improperly included these items in the revenue requirement calculations.

In data request no. JI1-63, the Joint Customer Group requested copies of AEP's PowerTax Provision Report for each OpCo and TransCo to review the non-property Excess/Deficient ADIT related items before and after the remeasurement of the TCJA and to determine whether AEP has properly classified each as protected or unprotected. AEP's response to request JI1-63 simply refers back to its response to request no. JI1-62; as noted above, however, AEP's response to request no. JI1-62 does not provide sufficient explanation or justification for the inclusion/exclusion of each Account 190 and 283 item from calculations under the formula rates. This issue affects not only the normal ADIT items allocations but would also impact whether the associated Excess/Deficient ADIT balances are properly allocated to transmission customers. Also, there are various items (SFAS 109 items) which are balance sheet-related only and which therefore should be excluded from the rate calculations under the formula rate templates. It appears that AEP, however, has improperly included these items in the revenue requirement calculations.

With reference to AEP's response to data request no. JI1-64, AEP's 2018 amortizations for Protected Property do not appear to be properly based on ARAM, but appear to be based instead on the Average Remaining Life ("ARL") method or the Reverse South Georgia Method ("RSGM") in Attachments 5 - 9. Furthermore, the inclusion of SFAS 109 ADIT balances for various items (see list of items in JCG-2018-14) that should not be included in transmission rates are also impacting the TCJA related amortizations.

Other potential items include the following:

a. ACCRD PARTNERSHIP WITH OH-NONCURRENT
b. ACCRD PARTNERSHIP WITH OH-CURRENT
c. ACCRD OH GROWTH FUND-NONCURRENT

d. ACCRD OH GROWTH FUND-CURRENT
e. SECURITIZATION DEFD EQUITY INCOME - LONG-TERM
f. AMORT - GOODWILL PER BOOKS
g. ACCRD BOOK ARO EXPENSE - SFAS 143
h. IRS AUDIT SETTLEMENT
i. Various Regulatory Assets and Regulatory Liabilities that were approved by state commissions and not FERC
j. Any other items determined to be not includable pursuant to Order Nos. 144 and 864.

With reference to AEP's responses to data request nos. JI1-84 and JI2-31, Attachment 1 to the JI1-84 response does not provide sufficient detail regarding the Excess ADFIT reversals (e.g., by identifying the individual protected and unprotected ADIT items) for the Joint Customer Group to determine whether the amortizations are appropriately related to transmission rates.

JCG-2018-10 Failure to Remove Battery Storage Facility from Plant in Service Since 2012

In data request no. JI 1-68, the Joint Customer Group requested information related to the Chemical Station project, located at N. Charleston, WV classified as Transmission on APCo's 2018 FERC Form 1, page 123.78. AEP's response to data request no. JI-68a states that "[t]he retired facility is part of a transmission substation. The retired facility served the purpose of housing the energy storage battery during the time it was used and useful." AEP further explains in subpart b. that "[t]he facility was retired in 2012. The facility was retired due to a failure on the battery and a subsequent distribution circuit obviated the need to fix/replace the asset." Further, AEP's response to JI2-19 states that "[t]he battery was connected to the Chemical/West Washington Street Feeder via a 12 kV underground riser and 1500 KVA, 12 kV-480 V transformer. No meter was used as this battery was being utilized as a system asset."

In the Joint Customer Group's data request no. JI 2-20, AEP was asked to provide the justification for not writing off this asset. AEP's response to JI 2-20 states that "The Company follows FERC's Electric Plant Instructions, Item 10 "Additions and Retirements of Electric Plant" when accounting for retirements of plant and the associated cost of removal." and that "The Company has identified an oversight in following these instructions in the case of the Chemical Station project. The Company is working to correct this oversight." Based on AEP's responses to data requests, it appears this Battery Storage Facility has remained in rate base since 2012 despite the facility not being used and useful since 2012. FERC precedent is clear that only assets being used to provide service to customers may be included in rate base.[7] The Joint Customer Group challenges the inclusion of this asset in rate base and requests a refund of all charges arising from AEP's inclusion of this facility in rate base (including depreciation, return, taxes, associated ADIT, and any other items affected by the inclusion of the facility in rate base).

JCG-2018-11 Classification of Cloverdale 500/345/138KV Substation

In AEP's response to specific data request no. JI2-23 and an associated response to data request no. JI 1-72, particularly JI 1-72 Attachment), AEP states that the T0190035 - Cloverdale

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7 In general, the used and useful standard provides that an asset may be included in a utility's rate base only when the item is used and useful in providing service, and that current ratepayers should bear only the costs incurred in providing service to them" (*New England Power Co.*, 42 FERC ¶ 61,016 (1988)).

500/345/138KV Substation: APCo: 7113 project should have been classified as distribution; however, AEP did not indicate that it would be reclassifying this asset as part of this review. To the extent AEP does not remove the $10,988.66 of plant and associated depreciation, return, taxes, ADIT and other affected items from the revenue requirement calculation, the Joint Customer Group challenges the inclusion of this asset in transmission rates.

JCG-2018-12 Recovery of General Plant Depreciation Expense Related to Unapproved AROs

a. AEP's response to data request no. JI2-26 indicates that APCo has included the depreciation expense associated with General Plant ARO in the transmission formula rate. The associated general plant ARO and accumulated depreciation is correctly being removed from the template on the "TCOS" tab, Lines 26 and 37. However, there is no corresponding adjustment for the removal of the associated depreciation expense. The Joint Customer Group challenges the inclusion of unapproved ARO General Plant depreciation expense in its formula rate.

b. Similarly, I&M Power has included ARO depreciation expense in its formula rate template on TCOS Line 101. (See AEP's response to data request no. JI 2-41). Joint Customer Group challenges this item for the reason noted in part a of this challenge.

JCG-2018-13 Omission of Rental Revenue Credits Associated with General Plant Assets Included in the TRR

With reference to AEP's responses to specific data request nos. JI 2-29, 2-40, 2-55, 2-65, 2-75, 2-85 (and associated responses to data request nos. JI 1-80 (specifically, JI_Set_1-80_Attachment 1), 1-105, 1-124, 1-138, 1-156, 1-176), the Joint Customer Group questioned why numerous rental revenue payments were not being included as revenue credits in AEP's formula rate templates. AEP indicates that the assets and presumably the expenses associated with these revenues have been recorded to various general plant accounts. AEP states in its response to data request no. JI 2-29 that "the assets are recorded in FERC accounts 38900 – Land, 38910 - Land and Rights, 39000 – Structures & Improvements, and 39700 – Communication Equipment. The rental payment is associated with one business unit owning a facility and another business unit utilizing space in that facility and is considered revenue received from an affiliate." The remaining requests related to this challenge produced similar responses. Since these assets are included in General Plant accounts and included in the formula rate template, the associated revenues should also be included based on a wages and salaries allocator. The Joint Customer Group challenges AEP's decision not to include the rental revenue credits associated with these assets in the transmission formula rates. "As a general rule, the equitable treatment of costs *vis-à-vis* revenue credits is as follows: if certain costs are included (or excluded) in the revenue requirement, then revenue credits associated with those costs should be included (or excluded) as well (and *vice versa*). If costs are included but related revenue credits are excluded, then the resulting rate results in double-recovery. If costs are excluded but related revenue credits are included, then the resulting rate is not fully compensatory to the utility" (*Constellation Mystic Power, LLC*, 165 FERC ¶ 61,267 at n. 303 (2018)).

JCG-2018-14 Failure to Comply with FERC Order No. 144 in Allocating ADIT

With reference to data request no. JI2-32, the Joint Customer Group questioned AEP as to how its allocation of ADIT in the formula rate templates is in compliance with Order 144. AEP's response to request no. JI 2-32 stated that "[t]he inclusion of ADIT in the companies' filing is made pursuant to the formula rate as documented in the protocols and template formulas found in Attachments H-14 and H-20 in the PJM Open Access Transmission Tariff." However, the settlement does enable AEP to disregard FERC Order No. 144 and include ADIT items where the associated expenses or revenues are not included in the formula rate templates. The Joint Customer Group challenges AEP's decision to include ADIT items that are not a result of expenses or revenues included in the OpCos' and TransCos' formula rate templates, since doing so is contrary to FERC Order No. 144. The Joint Customer Group challenges the following ADIT items, and, to the extent the inclusion of any other ADIT items in the revenue requirement does not comport with Order No. 144, the Joint Customer Group reserves their right to challenge those items as well.

a. ACCRUED INTEREST-SHORT-TERM – FIN 48 (see responses to data request nos. JI1-94, JI1-115, JI1-135, JI1-146, JI1-172, and JI1-185, as well as JCG-2018-17)
b. DEFD BK CONTRACT REVENUE (see responses to data request nos. JI 1-94 and 1-172) – no separate contracts are included under the formula rate template
c. ACCRD SIT TX RESERVE-SHRT-TERM-FIN 48 (see responses to data request nos. JI1-94, JI1-135, JI1-172, and JI1-185, as well as JCG-2018-17)
d. CIAC – BOOK RECEIPTS (see responses to data request no. JI 1-112, Line 2.06, 1-143, and 2-67, as well as **Error! Reference source not found.**)
e. PROV FOR RATE REFUND – TAX REFORM and PROVS POSS REV REFDS (see responses to data request nos. JI 1-86, 1-113, 1-134, 1-144, 1-170, 1-184, 1-201, 1-218, 1-240, 1-252, and 1-265)

   Prov for Rate Refund – Tax Reform and Provs Poss Rev Refds should not be included in ADIT to be allocated to transmission customers. There should not be a timing difference for what is recorded on the books and records and what is recorded on the tax returns. This item should be excluded with other SFAS 109 amounts which are balance sheet only and not included in the formula rate template per Order 144.
f. Prov For Rate Refund Excess Protected
g. SFAS 106 PST RETIRE EXP – NON-DEDUCT CONT (see responses for data request nos. JI1-94, JI1-110, JI1-135, JI1-146, JI1-166, and JI1-185)
h. BK PROV UNCOLL ACCTS (see responses to data request nos. JI 1-114 and JI1-171, as well as JCG-2018-18)
i. Line 2.72 DEFD REV-BONUS LEASE SHORT-TERM and Line 2.73 DEFD REV-BONUS LEASE LONG-TERM (see response to data request no. JI 1-172)

   In AEP's response to data request no. JI 1-172c. and d., AEP states "Line 2.72 and 2.73 relates to the current portion of oil and gas bonus payments (deferred revenue) which is amortized over the length of the lease. The payments and amortization are recoded to accounts 2530177 and 2530178. The ADIT is not measured on the expense account but measured on the balance sheet account." These amounts are related to the oil and gas bonus payment revenue where the underlying revenues are not included in the formula rate template; therefore, the associated ADIT should not be included.

j. AMT CREDIT – DEFERRED (see responses to data request nos. JI1-135, JI1-146, JI1-172, JI1-185, JI1-219, JI1-241, JI1-253, and JI1-266)

AMT (Alternate Minimum Tax) Credit is a tax position, but should not impact transmission rates which reflect the income tax rate allowance excluding all schedule M adjustments including AMT. The ADIT related to the AMT Credit should not be included in ADIT to be allocated to transmission customers. There should not be a timing difference for what is recorded on the books and records and what is recorded on the tax returns. This item should be excluded with other SFAS 109 amounts which are balance sheet only.

See also associated responses to data request nos. JI1-86, 1-94, 1-112, 1-113, 1-114, 1-134, 1-144, 1-170, 1-172, 1-184, 1-201, 1-218, 1-219, 1-240, 1-241, 1-252, 1-253, 1-265, 1-266, 2-32 and 2-45.

JCG-2018-15 Allocation of Accrued Book Pension Expense ADIT in FERC Account No. 190 for KPCo

In its response to data request no. JI 2-58, AEP states that "[t]he ADIT for Prepaid Pension Benefits is on WS B-2 line 2.14, which is the detail of account 190. The amount for this ADIT item is shown as a deduct to the total balance of account 190.1. Therefore, the ADIT amount is being properly reported as a reduction in rate base in the formula." The Joint Customer Group agrees that these are reductions in the formula rate; however, AEP has not adequately explained the ADIT amounts allocated to Transmission. KPCo appears to have only allocated 0.7635% of the total amount to Transmission in 2017 and 0.0067% of the total amount to Transmission in 2018. AEP should allocate the ADIT to transmission on the same basis as the prepaid pension benefits that give rise to the ADIT, or provide documentation supporting the amount of the allocation.

JCG-2018-16 Failure to Include Unfunded Reserves to Reduce to Rate Base

Please refer to AEP's response to specific data request no. JI2-34,.as well as other associated responses to data request nos. JI1-90, 1-111, 1-131, 1-142, 1-167, 1-181, 1-199, 1-217, 1-239, 1-251, 1-264, JI2-44, 2-59, 2-66, 2-79, 2-89, 2-93, 2-97, 2-99, 2-100, and 2-101.

With reference to this preliminary challenge, the Joint Customers Group provides the following explanation as it relates to unfunded reserves. AEP has failed to provide the customers with a reduction in rate base for the "Unfunded Reserves" associated with each of the accrued items identified in the foregoing data responses. AEP should have recorded each unfunded reserve as a reduction to rate base to reflect the fact that customers fund these accrued "expenses" that have not yet been incurred, and thus are providing a source of cost-free capital to the utility. FERC stated in an order in Docket No. ER14-2751-000 as follows:

> [W]e find that XEST's formula rate template should recognize unfunded operations and maintenance costs reserves as a form of cost-free financial capital to XEST. Utilities **may accrue monies through charges to operation and maintenance expense to fund contingent liabilities**, and such accrued reserves should be deducted from rate base until they are used to fund the liabilities because such reserves represent a cost-free form of financial capital from customers to utilities, not unlike accumulated deferred income taxes (ADIT) which are deducted from

> rate base. Accordingly, we direct XEST, in a compliance filing, to propose revisions to its formula rate template **to credit any unfunded reserves** against rate base.[8]

XEST does not differentiate between long-term contingent liabilities and short-term contingent liabilities. FERC only stated that the unfunded O&M reserves should be recognized as a form of cost-free capital.

Moreover, FERC broadly defines a contingent liability as any liability related to accruing monies from customers through charges to fund "accrued O&M expenses" prior to the Company having to actually pay the costs. Contingent liabilities may be classified as: (1) a current or short-term liability which is to be paid in 12 months or less; (2) a long-term liability that the Company will pay in more than a year; or (3) both a current and a long-term liability because they have both components. All accrued O&M expenses are essentially contingent liabilities.

In AEP's response to data request no. 2-34, AEP defines "contingent liabilities" as:

Contingent liabilities are defined by FERC in General Instruction 15 to the Uniform System of Accounts, which states the following:

> 15. Contingent Assets and Liabilities (Major Utility).
>
> Contingent assets represent a possible source of value to the utility contingent upon the fulfillment of conditions regarded as uncertain. <u>Contingent liabilities include items which may under certain conditions become obligations of the utility but which are neither direct nor assumed liabilities at the date of the balance sheet.</u> The utility shall be prepared to give a complete statement of significant contingent assets and liabilities (including cumulative dividends on preference stock) in its annual report and at such other times as may be requested by the Commission. [Emphasis added]

AEP has interpreted General Instruction 15 as allowing inclusion of "all" possibilities, but the statement AEP underlines states that "Contingent liabilities include items which **may** [bold added] <u>under certain conditions become obligations of the utility but which are neither direct nor assumed liabilities at the date of the balance sheet</u> " The fact that they may become obligations of the utility does not change the fact that they were contingent. Therefore, AEP's statement that "Common accruals recorded as of any balance sheet date for items like accounts payable, salaries and wages, incentive plans, and vacation pay do not fall under this definition." is flawed because(i) all employee related and injuries and damages liabilities whether current, long-term or uncertain have components, attributes or conditions that have to be fulfilled before the payments of the liabilities are made; and(ii) all employment benefits are contingent to the employees being either employed, retired, meeting a combination of age and year of service at the time the benefits are paid or that the employees have met certain conditions. For example, Accumulated Provision for Pensions and Benefits are based on actuarial reports for PBOPs (OPEBs) and pensions, which are dependent on age and years of service. These reports

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8 See Xcel Energy Southwest Transmission Co., LLC, 149 FERC ¶ 61,182, at P 97 (2014) ("XEST"); Transource Wisconsin, LLC, 149 FERC ¶ 61,180, at P 43 (2014); see also NextEra Energy Transmission West, LLC, 154 FERC ¶ 61,009, at P 125 (2016) ("[I]n the past the Commission has directed entities to revise their formula rate templates to 'credit any unfunded reserves against rate base.'"). Working capital includes capital supplied by investors (i.e., cash working capital, prepayments, and materials and supplies) and capital supplied by customers (i.e., unfunded reserves).

include many assumptions that are uncertain or inherently risky such as those premised on inflation, mortality rates and employment status. AEP has no way of knowing the actual amounts it will pay out in the future; therefore, the amounts should be considered uncertain until funds to meet an obligation actually are transferred into an external trust. Similarly, the other items identified in AEP's response are also uncertain because the factors that ultimately establish the amount of the obligation (such as a final tax return, employment status and performance of the company) may not be known with certainty. For these reasons, the Joint Customer Group challenges AEP's decision to exclude the associated unfunded reserves as FERC has a policy that such reserves are a source of cost-free capital, notwithstanding items which are in a trust, an escrow or a restricted account. Those items that are in a trust, an escrow or a restricted account are funded reserves and the associated ADIT would also be excluded from being allocated to transmission customers.

JCG-2018-17 Inclusion of ADIT Related to Uncertain Tax Positions That Are Not Included In the TRR

In reference to AEP's response to specific data request no. JI 2-36 and other associated responses to data request nos. JI 1-94a., JI 1- 94d., 1-115a., 1-135a., 1-135d., 1-146a., 1-172a., 1-172e., 1-185a., 1-185c, JI 2-48a, 2-50, 2-61, 2-68, 2-82, and 2-91, AEP states that "[t]he two items requested are not short-term debt. ACCRUED INTEREST-SHORT-Term - FIN 48 is related to the book vs tax timing difference around the accrual of interest expense associated with uncertain tax positions. It represents the estimate of interest expense that would be owed to a taxing authority if an uncertain tax position is not maintained as filed. ACCRD SIT TX RESERVE-SHRT-TERM-FIN 48 is related to the book versus tax timing difference around the accrual of state tax expense for uncertain tax positions. It represents the amount of state income taxes that would be owed to a taxing authority if an uncertain tax position is not maintained as filed. Both of these items impact the total company, thus an allocation to Transmission is warranted." Unless AEP can show that the interest on uncertain tax positions and the uncertain tax positions themselves are included in the cost of service or customers do benefit from short term interest received, the ADIT associated with these items should be excluded from rate base.

JCG-2018-18 Treatment of ADIT Related to BK PROV UNCOLL ACCTS That Are Distribution Related Service

a. In AEP's response to specific data request no. JI 2-47 and an associated response to data request no. JI 1-114, AEP indicated that the expenses associated with the BK PROV UNCOLL ACCTS are included in FERC Account "904 related to the Distribution portion of I&M." In addition, AEP states "the associated ADIT, are not included in the formula." I&M has included $715 of ADIT associated with uncollectible accounts as shown in I&M's template on the tab "WS B-2 - Actual Stmt. AG," Line 2.30 - BK PROV UNCOLL ACCTS, Column S - Transmission, which is contrary to AEP's statements. The Joint Customer Group challenges the inclusion of this ADIT associated with expenses related to the distribution function as the expenses are not included in the formula rate template, which would be in compliance with Order 144.

b. Similarly, AEP's response to specific data request no. JI 2-81 (and an associated response to data request no. JI 1-171) indicates that this ADIT is related to the distribution function and not included in OPCo's formula rate template. Contrary to AEP's statements, OPCo's formula rate template on the tab "WS B-2 - Actual Stmt. AG," Line 2.23 - BK PROV UNCOLL ACCTS - Column N - Transmission includes $1,050 of ADIT associated with the BK PROV UNCOLL ACCTS. The Joint Customer Group challenges the inclusion of this ADIT associated with expenses related to the distribution function as the expenses are not included in the formula rate template, which would be in compliance with Order 144.

JCG-2018-19 Treatment of Joint License Revenues Associated with Affiliate Agreements

With reference to JI 2-69 Attachment 1 provided in AEP's response to data request no. JI 2-69, "WPCO" tab, Excel Cell J14 in the amount of $18,619.08, the note in Column I states "less joint license expense recorded in account 567." This comment indicates that AEP is removing the expense from the revenue credit; thereby decreasing the overall credit. If AEP has already included the expense in FERC Account No. 567, the manual removal of this expense on this attachment would result in a double adjustment for the expense. The Joint Customer Group challenges such treatment. See also other associated files JI-148_Attachment_1.xlsx and JI_Set_1-80_Attachment 1.xlsx provided in response to data request nos. JI 1-148 and 1-80.

JCG-2018-20 Treatment of Prepaid Pension Benefits in Working Capital Compared to the Treatment of the Associated ADIT

In the files "APCo - 2018 ATRR Template.xlsx," "KgPCo – 2018 ATRR True-Up Template.xlsx," "KPCo -2018 ATRR True-Up Template.xlsx," "OPCo -2018 ATRR True-up V.2.xlsx," and "WPCo – 2018 ATRR True-Up Template.xlsx," on the respective "WS C – Working Capital" tabs, the AEP companies shows Prepaid Pension Benefits as being Transmission Labor Related, but the FAS 158 Qual Contra Asset in equal and offsetting amounts are excluded entirely from rate base. However, it appears that the related average ADIT to both the Prepaid Pension Benefits asset and the contra asset shown on the respective "WS B-1 – Actual Stmt. AF" tabs are included in rate base, which result in a net zero effect in each of the templates. Either the FAS 158 Qual Contra Asset should also be included in rate base as a transmission labor-related item on "WS C – Working Capital," or the ADIT associated with the FAS 158 Qual Contra Asset should be excluded from rate base on the "WS B-1 – Actual Stmt. AF." Below are the relevant Excel rows in "WS B-1 – Actual Stmt. AF" associated with the FAS158 Contra Asset that should be excluded for each company:

i. APCo – Excel row 97 – Line 9.16
ii. KgPCo – Excel row 54 – Line 9.02
iii. KPCo – Excel row 78 – Line 9.11
iv. OPCo – Excel row 92 – Line 9.20
v. WPCo – Excel row 59 – Line 9.02

Furthermore, in AEP's response to specific data request no. JI 2-77 and an associated response to data request no. JI 1-165, AEP indicated that for OPCo, Line 16 - Prepaid Pension Benefit in WS C – Working Capital has its ADIT offset "on WS B-1 line 9.19." However, AEP shows the contra asset being related to FAS158, so it remains unclear whether this item is truly the offset or if the offset should be line 9.41 - REG ASSET-SFAS 158 – PENSIONS. It also appears this description may have been inadvertently switched with line 9.20 - ACCRUED BK PENSION COSTS - SFAS 158. In addition, it appears that AEP's response to JI 2-88 for WPCo (Other associated responses JI 1-180) may have a similar issue. The Joint Customer Group requests further clarification of this issue.

Please acknowledge your receipt of this letter and notification by "Reply All" e-mail. In addition, feel free to contact me directly if you have any questions concerning the above-described Preliminary Challenges. Finally, I would be grateful if you would include the persons copied on this letter (as copied on the email correspondence and listed in footnote 1) as recipients of all future correspondence concerning this matter.

Very truly yours,

Chris Norton

Chris Norton
Director of Market Regulatory Affairs

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