AMERICAN ELECTRIC POWER WEST 2019 ANNUAL UPDATE
FERC Docket No. ER18-195

Arkansas Electric Cooperative Corporation (AECC),
East Texas Electric Cooperative, Inc. (ETEC), and
Northeast Texas Electric Cooperatives (NTEC)
PRELIMINARY CHALLENGES

January 6, 2019

The Joint Customers[1] hereby notifies American Electric Power Service Corp. ("AEP") of Preliminary Challenges to certain components of (i) the AEP West Operating Companies' Annual Transmission Formula Rate True-up for 2018, which was filed with the Federal Energy Regulatory Commission ("FERC") on May 28, 2019 in Docket No. ER18-195 ("2018 OpCo Update"), and (ii) the AEP West Transmission Companies' Formula Rate Annual Update for 2018, which was filed with FERC on May 28, 2019 in Docket No. ER18-195 ("2018 Transco Update").

The list below outlines the issues that the Joint Customers consider to be unresolved and consequently are deemed to be Preliminary Challenges under the Protocols.

Unresolved Issues

PC-1. In reference to AEP's response to GDS 1-27, AEP indicates that "OKT incurred costs totaling $304,818 for the joint use of land and land rights during 2018 recorded in FERC Account 567 for payments made to PSO." However, in AEP's formula rate update file "21 2019 AEP FR Template.xlsx," tab "PSO WS H Rev Credits," Row 17 - PSO WS H Rev Credits, PSO shows a rent amount of $179,310. Therefore, it appears that PSO has not included the revenue for the payments OKT made to PSO related to the joint use of land and land rights. The Joint Customers challenge PSO's formula rate template for not including the $304,818 of revenues received from OKT.

PC-2. In reference to AEP's response to GDS 2-23, AEP states that "Tulsa Regional Chamber was invoiced as a sponsorship but inadvertently had miscoding to an outsider services cost component, rather than the appropriate cost component 955 for Contributions & Sponsorships. Had the appropriate cost component of 955 been entered, system restrictions would have required the use of the FERC 426x accounts. Per operation of the formula, the values shown above have been allocated to transmission based on the W/S allocator." AEP's response indicates that the amounts associated with the Tulsa Regional Chamber should have been recorded to a below the line 426 account, which are excluded from the formula rate template. The Joint Customers challenge the inclusion of these chamber of commerce expenses in accordance with AEP's response and FERC precedent.[2]

PC-3. In reference to AEP's response to GDS 2-23, AEP states that the "Public Affairs Council and the U.S. Chamber of Commerce are political and business related memberships. These amounts are the non-lobbying portion of these memberships, which are recorded to 930.2 as a deductible

[1] Arkansas Electric Cooperative Corporation (AECC), East Texas Electric Cooperative, Inc. (ETEC), and Northeast Texas Electric Cooperatives (NTEC).
[2] Docket Nos. ER09-1256-002 and ER12-2708-003 and FERC Docket No. ER17-1519-001, Exhibit No. S-0019, Page 78 and 79.

business expense. The lobbying portion are non-taxable and recorded below the line." AEP's response indicates that these expenses are memberships. FERC precedence[3] states that chamber of commerce memberships are to be included in Account 456.5. The U.S. Chamber of Commerce is the largest lobbying group in the U.S., spending more money than any other lobbying organization on a yearly basis. In reference to AEP's inclusion of Public Affairs Council memberships, AEP should record these amounts to Account 426.4 in accordance with American Electric Power Service Corporation in FERC Docket No. ER07-1069-007 filed on June 13, 2016, which states "For charges collected under the AEP Formula Rate from and after July 1, 2016, expenditures for lobbying and other civic, political, and related activities, and any expenditures that would not have been incurred but for such lobbying or other expenditures, shall be recorded in USofA Account 426.4 in accordance with the instructions to that account and excluded from recovery under the AEP Formula Rate.[4]" Based on the foregoing, the Joint Customers challenge the inclusion of the U.S. Chamber of Commerce and Public Affairs Counsel expenses.

PC-4. In reference to AEP's response to GDS 2-24, AEP states that "The companies have not used a with and without test to determine if NOL - Fed should be protected or unprotected. The companies have not determined the extent to which the NOL is associated with bonus depreciation." In addition, AEP's response to GDS 1-38d. states that "All the amounts in accounts 190 and 283 are unprotected." Further in AEP's attachment "GDS 1-37_Attachment 2," AEP has included the following federal NOL in its EDIT calculations and amortized them in one year leaving a zero balance at 12/31/2018:

a. Row 19 – AEP Oklahoma Transmission Co, Inc. - Account 190 - Accum Deferred FIT-Other NOL - DEFERRED TAX ASSET RECLASS
b. Row 54 – AEP Southwestern Trans Co, Inc. - Account 190 - Accum Deferred FIT-Other NOL - DEFERRED TAX ASSET RECLASS
c. Row 119 – PSO Corp - Account 190 Accum Deferred FIT-Other NOL - DEFERRED TAX ASSET RECLASS
d. Row 281 - PSO Corp – Account 190 - Accum Deferred FIT-Other NOL - DEFERRED TAX ASSET RECLASS

The Joint Customers challenge AEP's decision to classify the federal NOL as unprotected without performing a "with or without" test in order to avoid being in violation of normalization rules, which would result in AEP losing its ability to use accelerated depreciation. In addition, Joint Customers challenge AEP's decision to amortize its federal NOL over one year, instead of based

[3] Id.
[4] Section II (D) at 6.

on ARAM for the portion associated with bonus depreciation and/or based on 5-years[5] for any portion that is not related to bonus depreciation and should be classified as unprotected.

PC-5. For each of AEP's OpCos and TransCos, AEP has not demonstrated that the amounts from company records on attachment "WS C-4 Excess FIT" reconciles to AEP's Attachment "GDS_1-37_Attachment_1.xlsx," Column D "Activity for TCJA Adjust." AEP's exhibit of its EDIT lacks transparency by not showing (i) the amounts that are deemed to be either protected or unprotected, (ii) appearing to only attempt to show the transmission only portion of the EDIT, (iii) failed to show the detail calculations behind its balances that show the functionalization of each EDIT item and how that detail supports AEP's balances (i.e. AEP's formula rate templates allocates ADIT based on "exclusions," "100% transmission," "PTD Plant," "T&D," and "Labor" and should use similar allocations to calculate the EDIT balances).

Further in relation to the Joint Customers' request in GDS 1-150, the Joint Customers requested that it provide an explanation and reconciliation to its formula rate, tab "SWEPCO WS C-1 ADIT EOY," Deferred Income Tax Balances – GL A/C 282, Row 50 and 51, as to why the components that total this account on Row 50 equal $(1,356,817,389) compared to the FERC Form 1 amounts shown on Row 51 of $(1,366,840,207). SWEPCO's response to GDS 1-150 states: To account for these differences between book values and ratemaking, Worksheet C-4 was used to determine beginning balances excess ADIT based upon AEP's final determination of the unprotected/protected split of the Excess as follows:

- The beginning transmission-functional balances of the Excess ADIT on Line 1 of WS C-4 represents the final balances of Excess ADIT as determined by the final TCJA entries in January 2019.
- The 2018 annual amortization for unprotected excess is equal to one fifth of the total unprotected beginning balance and the 2018 annual protected excess is the per books amortization.
- The 2018 ending transmission-functional balances are calculated by subtracting one year's amortization of from the beginning balances.
- All other Excess ADIT are considered excludable as they are not included in the transmission-functional balances.

The Joint Customers requested further information in GDS 2-63, which AEP responded with Attachment "GDS 2-63 Attachment 1." AEP's attachment did not provide an explanation of these changes and demonstrate what specifically changed by line item. AEP's response grouped or

[5] AEP's settlement agreement in FERC Docket No. ER18-195-001.

lumped everything together and did not provide an explanation as to what happened or what AEP was attempting to demonstrate.

For the foregoing reasons, the Joint Customers challenge AEP's treatment of its Excess ADIT balances until AEP can demonstrate that the balances included in each OpCos and TransCos' template have been properly functionalized and supported.

PC-6. PSO has included $3,075,790 of ADIT associated with non-deductible contribution as shown on PSO WS C-1 ADIT EOY, Row 90 - 906D SFAS 106 PST RETIRE EXP - NON-DEDUCT CONT. The Joint Customers requested further justification for including this ADIT in PSO's formula rate template. AEP's response to GDS 2-34 states that "Accrued SFAS 106 Postretirement Benefits represents contributions that were made to an Other Post Employment Benefit (OPEB) trust. These contributions are recorded to the balance sheet. PSO's deduction for the contributions are temporary disallowed." Based on PSO's response to GDS 2-34, the Joint Customers challenge the inclusion of this ADIT in its formula rate template and AEP's lack of providing the requested FERC Account information, PSO's deduction for contributions are temporarily disallowed (tax purposes implied), therefore the ADIT should not be allocated to transmission customers, until the contributions are allowed for tax purposes. Furthermore, PSO's response indicates this ADIT is associated with balance sheet accounts, which are not included in the formula rate template. Therefore, AEP should not include the associated ADIT in compliance with Order 144.

The Joint Customers requested similar information in GDS 1-137 and 2-59 to which AEP's response referenced back to "See Response to GDS 2-34." Likewise, the Joint Customers challenge this ADIT item in SWEPCO's formula rate template.

PC-7. In relation to PSO's formula rate template, tab "WS C-1 ADIT EOY," Deferred Income Tax Balances – GL A/C 283, Line # 960F-XS, Excess ADFIT 283 Unprotected (Excel rows 93 & 94). The Joint Customers requested in GDS 2-35 for AEP to (i) provide a detailed explanation as to why the transmission portion of $6,534,881 is a positive amount and why the excluded portion is a negative $(3,962,053) and (ii) provide the detailed supporting calculations for both balances, including the tax reports for these amounts. AEP's response stated "The $6,534,881 amount is a positive amount (debit balance) on the Transmission functional ledger because the net result of all of underlying activity to record unprotected ADIT in that account is a debit. Detail for that amount was provided in GDS 1-68 Attachment 1 cell I53. The combined balance of the unprotected ADIT in 283 for all three functions is a $2,572,828 debit. This is the combination of the two unprotected line items on excel rows 93 and 94 of PSO's WS C-1. The $(3,962,053) excluded amount is the generation and distribution functional component of those two unprotected line items which was shown in the excluded column on WS C-1." Based on AEP's response to GDS 2-35, and AEP's total lack of providing detailed information demonstrating why the generation and distribution functional components resulted in a "negative" $3,962,053 balance (*i.e.*, excess ADIT) and the transmission balance a "positive" $6,534,881 balance (*i.e.*, deficient ADIT), AEP has not demonstrated that the transmission function is not subsidizing both the generation and distribution functions for this underlying activity. For the foregoing reasons, the Joint Customers challenge the treatment of this ADIT.

The Joint Customers requested similar information in GDS 1-98 and 2-45 to which AEP's response referenced back to "See Response to GDS 2-35." Likewise, the Joint Customers challenge this ADIT item in OKT's formula rate template.

PC-8. In relation to PSO's formula rate template, tab "WS C-1 ADIT EOY," Deferred Income Tax Balances – GL A/C 190, Line # 520A, Provs Poss Rev Refds-A/L (Excel row 111), PSO has allocated this ADIT in the amount of $1,702,155. The Joint Customers requested further information on what this ADIT was related to in GDS 1-71. AEP responded that "a. The Line # 520A, Provs Poss Rev Refds-A/l (Provisions for Possible Revenue Refunds) represents the timing differences related to provisions for revenue overcollections which are not deductible for tax at the time the book provision is recorded. b. The underlying impact of this flows through the formula rates when revenue over collections are returned to customers as prescribed in the formula rate. c. This is applicable to all three functions." AEP further justified the inclusion of this ADIT in its response to GDS 2-36 by stating "The Company disagrees with the premise that the ADIT underlying these revenues should not be included in rates. The Company must book the provisions referenced in 1-71 when there is a known over-collection of wholesale transmission revenues collected through this formula rate. The ADIT associated with the provisions is directly-related to the administration of the formula rate and should therefore be included."

The Joint Customers disagree with AEP's statements above. The formula rate does not take into account AEP's "known over-collection." The revenues charged in AEP's projected transmission revenue requirement ("PTRR") are the revenues generated due to the various billing cycles and the only unbilled revenues would be associated with those billing cycles during the calendar/fiscal tax year; therefore, there would not be a book tax timing difference. Any true-up amounts performed in May would be included in the amounts received in the following year for both taxes and books and records. These revenues would not be included on AEP's tax return as they are not earned until the true-up occurs in May 2019 for which AEP receives during the following billing cycles in the next rate year (June – May 2020). AEP's treatment of including this associated ADIT on the Provs Poss Rev Refds-A/L essentially allows AEP to earn interest on the revenues billed for the true-up amounts through the PTRR and also a return on the associated ADIT for the Provs Poss Rev Refds-A/L, which results in a double recovery. For the foregoing reasons, the Joint Customers challenge the inclusion of the Provs Poss Rev Refds-A/L ADIT in any of AEP's OpCo or TransCo formula rate templates. (Also, a similar issue associated with AEP data responses to GDS 2-36, 2-46, and 2-60)

PC-9. In reference to AEP's response to GDS 2-58, AEP states "The OPEB[sic] accounting is recorded to 165 and 129 accounts that offset the 228.3 account." To the extent AEP is including the Account 165 balances for OPEB in rate base there should be ADIT associated with these OPEB balances. For the foregoing reasons, Joint Customers challenge AEP's decision to not include the ADIT related to those OPEB balances which would be a "credit" or a reduction in rate base.

PC-10. In reference to AEP's response to GDS 2-17 (also associated with GDS 1-31), AEP states "The transmission facilities listed are not required to be excluded from rates as they include interconnection points with other networked assets on the SPP system. However, as contemplated in Docket ER09-12, the Companies determined that certain feeders (a, c, e, i and k) in the list included some radial facilities. As such, the Companies have excluded a percent of the additions associated with those feeders based on the method approved in ER09-12. The remaining items were not excluded from the rates." AEP's response does not provide supporting documentation that the facilities identified in GDS 2-17b., d., f. through h., j., l., and m. should not be considered interconnection or radial facilities in the formula rate template. The Joint Customers challenge the inclusion of these facilities until AEP can provide supporting documentation to support their assertion.

PC-11. In reference to AEP's response to GDS 2-19 (also associated with GDS 1-31), AEP states "The transmission facilities listed are not required to be excluded from rates as they include interconnection points with other networked assets on the SPP system." AEP's response does not provide supporting documentation that the facilities identified in GDS 2-19a. through f. should not be considered interconnection or radial facilities in the formula rate template. The Joint Customers challenge the inclusion of these facilities until AEP can provide supporting documentation to support their assertion.

Unfunded Reserve Preliminary Challenges

In reference to the Preliminary Challenges PC-12 through PC-16 below, the Joint Customers provide 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 identified accrued items. 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 that:

> …we 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.[6]

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 2-30, 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.

AEP has interpreted the item 15. Contingent Assets and Liabilities to include "all" possibilities, but the statement AEP underlines states "Contingent liabilities include items which **may** [bold added]…" Furthermore, AEP's definition states that these assets and liabilities must be "uncertain." The items in question are by no means "uncertain," but rather known that these amounts will be paid out at a future date.

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[6] Xcel Energy Southwest Transmission, 149 FERC ¶ 61,182, at P 97 (2014) ("Xcel Order")

For the foregoing reasons, the Joint Customers challenge AEP's decision to not include the associated unfunded reserves with PC-10 through PC-14.

PC-12. In reference to AEP's response to GDS 2-28 (also associated with GDS_1-49_Attachment 1), AEP's "GDS_2-28_Attachment 1.xlsx" indicates there are multiple items included in Account 228.3 where expenses are included in rates and AEP uses the description as "known direct liability." These 'known direct liabilities' are estimates and various factors may affect their final amounts. For example, Accumulated Provision for Pensions and Benefits are based on actuarial reports for PBOPs (OPEBs) and pensions. These reports include many assumptions that are uncertain or inherently risky by being based off of inflation, mortality rates and employment status. AEP has no way of knowing the true balances in which it will pay out in the future; therefore, they should be considered uncertain until they are transferred into an external trust. Similarly, the other items identified in AEP's response are also uncertain because they may be based off a final tax return, employment status and performance of the company. In addition, AEP appears to state that "SFAS 112 Postemployment Benef," "FAS 158 SERP Payable Long Term" and "FAS 158 Qual Payable Long Term" are only associated with balance sheet accounts. There should be some portion of these items which have been included in expenses flowing through rates; therefore, some portion of these items should also be included as an unfunded reserve. For the foregoing reasons, these unfunded reserves meet the definition of contingent liabilities and should be included as an offset to rates for all OpCos and TransCos.

PC-13. In reference to AEP's response to GDS 1-56, AEP states that the increase to Account 923 – Outside Services Employed is a "$2M increase in expense is primarily due to an increase in the Umbrellas Trust." In AEP's response to GDS 2-32, AEP provides a description of the "Umbrellas Trust," which stated "The purpose of the umbrella trust is to provide a contingent source of funding for certain previously unfunded employee benefit obligations of AEPSC. These benefits include deferred compensation agreements and pension benefits. These plans are currently funded by the company, as a general obligation, separate from the Trust. While these future obligations are currently funded by the company, they lack the level of protection available to other post-employment benefits covered by the Employee Retirement Income Security Act. As such, the Trust was created to provide a level of protection in regard to the referenced benefits. If the company becomes unable to pay these benefits, the Trust funds would be used as a funding source for the benefits. If the company continues to fund and pay these benefits as a general obligation, as is expected, the Trust would never be used and the value of the Trust funds would be available to the company once the final benefit has been paid. This change in cash surrender value is recorded to FERC account 923."

To the extent AEP retains cost free-capital provided by the customers related to the "Umbrellas Trust," AEP should record an unfunded reserve from the time period the monies are included in a general account until the general account is transferred to the trust or a restricted account (for the time period from which monies are accrued in a general account to which AEP has access to the date in which those monies are put into the "Umbrella Trust"). AEP has not demonstrated which FERC accounts these unfunded reserves are recorded for the cost-free financial capital being provided by the transmission customers.

PC-14. In reference to the Joint Customers' request in GDS 2-38, the customers requested that PSO identify where "the associated ADIT with severance payable has been recorded in the template." AEP's response states that "The ADIT is recorded in the template in worksheets C-1 and C-2." PSO's template exhibits the severance ADIT as being reflected on attachment C1, Excel row 126, in the amount of $136,811 and attachment C2, Excel row 125, in the amount of $0 BOY balance based on labor, therefore the unfunded reserves related to this severance payable should be included as an offset to rates. These are severance accruals associated with amounts from customer contributed capital through the transmission rate prior to it being paid by AEP.

PC-15. In relation to OKT's formula rate template, tab "OKT WS C-1 ADIT EOY, Deferred Income Tax Balances – GL A/C 190, Line # 612Y, Accrd Companywide Incentv Plan (Excel row 48)," AEP states in its response to GDS 1-100 (also associated with GDS 2-47) that "Schedule M line 612Y relates to the book/tax timing difference associated with the accrual and payments for the AEP companywide incentive compensation plan (ICP). The underlying costs associated with the ADIT balance are charges from AEP Service Corporation (AEPSC) for an accrual for this ICP and recorded in account 9230003." Given that there are expenses included in Account 923, an unfunded reserve would be established and should be included as an offset to rates. AEP's responses to GDS 1-100b. and c. were non-responsive as to where the unfunded reserve accruals are recorded, but rather referenced Account 236 – Taxes Accrued.

Similarly, the Joint Customers asked requests in SWT's formula rate related to the incentive compensation plant in GDS 2-67(also associated with GDS 1-100 and 1-165), therefore unfunded reserves associated with the ICP should be included as an offset to rates.

PC-16. In reference to AEP's response to GDS 2-51 related to Account 228.3 – Accumulated Provision for Pensions and Benefits, AEP provided GDS Set 2-51 – Qa-41020 – Attachment 1.xlsx, the "OPENING" beginning balance in column (B) of $10,499,971.12 ties to SWEPCO's 2018 FERC Form 1, page 112, line 29, column (d) and the "2018 Total" balance of $17,129,792.06 ties to SWEPCO's 2018 FERC Form 1, page 112, line 20, column (c); therefore all of the amounts in this attachment are included in Account 228.3. AEP did not provide enough data to determine what was included in the beginning balance and the FERC Accounts in Excel column (f) are the second half of the transaction. AEP has should include the unfunded reserves for the beginning and ending balances of Account 228.3.