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KPOW.93405

July 31, 2017

### **VIA EMAIL (Sharla.Dillon@tn.gov) & FEDEX**

Mr. David Price, Chairman  
c/o Sharla Dillon, Dockets & Records Manager  
Tennessee Public Utilities Commission  
502 Deaderick Street, 4th Floor  
Nashville, TN 37243

Re: Petition of Kingsport Power Company d/b/a AEP  
Appalachian Power for Approval of its Targeted  
Reliability Plan, and its TRP & MS Rider, an  
Alternative Rate Mechanism and Motion for  
Protective Order  
Docket No. 17-000032

Dear Chairman Price:

Enclosed herewith is Kingsport Power's REBUTTAL TESTIMONY OF WILLIAM K. CASTLE for filing in the captioned docket. We shall be shipping the original and four (4) copies via FED EX for Monday delivery.

If you have any questions, please contact the writer.

Very sincerely yours,

**HUNTER, SMITH & DAVIS, LLP**



William C. Bovender

### **Enclosures**

cc: Kelly Grams, General Counsel (w/enc.)  
David Foster (w/enc.)  
Monica L. Smith-Ashford, Esq. (w/enc.)  
Wayne M. Irvin, Esq. (w/enc.)  
Michael J. Quinan, Esq. (w/enc.)

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Michael J. Quinan, Esq. (w/enc.)

**REBUTTAL TESTIMONY OF  
WILLIAM K. CASTLE  
ON BEHALF OF KINGSPORT POWER COMPANY  
D/B/A AEP APPALACHIAN POWER  
BEFORE THE TENNESSEE REGULATORY AUTHORITY  
DOCKET NO. 17-00032**

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

2   A.   My name is William K. Castle. My business address is 1051 E. Cary St, Suite 1100,  
3       Richmond, VA. I am the Director of Regulatory Services VA/TN for Kingsport Power  
4       Company d/b/a AEP Appalachian Power (Kingsport, KgPCo or the Company).

5   **Q.   ARE YOU THE SAME WILLIAM K. CASTLE THAT SUBMITTED DIRECT**  
6       **TESTIMONY IN THIS DOCKET?**

7   A.   Yes.

8   **Q.   WHAT IS THE PURPOSE OF YOUR REBUTTAL TESTIMONY IN THIS**  
9       **PROCEEDING?**

10  A.   I respond to ETEC witness Baron's opinion that an ARM is not a reasonable ratemaking  
11       approach for the recovery of costs associated with the Company's proposed Targeted  
12       Reliability Plan (TRP) and Major Storm Rider (the TRP & MS Rider). Second, I address  
13       issues raised by Mr. Baron regarding the allocation of costs between rate classes. Finally,  
14       I clarify some aspects of the Company's Direct Testimony in response to issues raised by  
15       CPAD witness Novak.

16  **Q.   SUMMARIZE ETEC WITNESS BARON'S OBJECTION TO THE USE OF AN**  
17       **ARM FOR THE COSTS ASSOCIATED WITH MAJOR STORMS AND WITH**  
18       **THE COMPANY'S PROPOSED TRP PROGRAM.**

1 A. Mr. Baron objects to the use of an ARM because, unlike traditional rate making, only  
2 certain costs, those costs subject to the ARM, are subject to regulatory review.<sup>1</sup> Also,  
3 according to Mr. Baron, if the Company recovers the costs associated with the TRP  
4 Program and Major Storms that are incremental to those in base rates in an ARM, it will  
5 not be able to pass on any over-earning associated with its base rates in the form of a  
6 netting of all costs and revenues. He also posits that the Company could be put in an  
7 over-earnings position as a result of the proposed TRP and Major Storm cost recovery.

8 **Q. ARE ALL THE COMPANY'S COSTS AND REVENUES SUBJECT TO**  
9 **REVIEW?**

10 A. Of course. As this Commission is well aware, all of the Company's costs are subject to  
11 regulatory review. What seems to be at issue here is the periodicity of review for various  
12 costs. To avoid "single issue ratemaking," as Mr. Baron has described it, a utility should,  
13 in his opinion, include all costs, except those costs associated with fuel and purchased  
14 power, in base rates. In this way, all costs (except fuel and purchased power) can be  
15 reviewed at the same time.

16 **Q. PLEASE DISCUSS MR. BARON'S ARGUMENT THAT FUEL AND**  
17 **PURCHASED POWER COSTS SHOULD BE RECOVERED IN A RIDER**  
18 **BECAUSE THEY ARE "SIGNIFICANT AND VOLATILE,"<sup>2</sup> WHILE ALL**  
19 **OTHER COSTS SHOULD BE RECOVERED IN BASE RATES.**

20 A. Mr. Baron is correct that fuel and purchased power costs can be volatile and significant,  
21 but the actual reason why fuel and purchased power costs are typically recovered with a  
22 rider mechanism with periodic reviews and resets between rate cases is to avoid the

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<sup>1</sup> Baron, page 10, line 5.

<sup>2</sup> Baron footnote page 10.

1 potential construction of large deferred fuel balances that, if left to be dealt with only  
2 during rate cases, can grow unwieldy and have enormous rate consequences when  
3 eventually reset. Riders allow for the monitoring and more frequent adjustment of these  
4 type of costs. Purposefully deferring the known TRP and Major Storm costs for future  
5 recovery, as Mr. Baron proposes, could have the same effect on customers' rates as  
6 would deferring fuel and purchased power costs.

7 **Q. CAN THE USE OF AN ARM TO RECOVER COSTS ASSOCIATED WITH THE**  
8 **TRP AND MAJOR STORMS BE THE CAUSE OF OVER-EARNINGS AS MR.**  
9 **BARON CLAIMS<sup>3</sup>?**

10 A. No. Both the costs and revenues of the TRP and costs associated with Major Storms that  
11 are incremental to base rates are completely independent of the costs and revenues  
12 associated with base rates. This is the whole idea and purpose of an ARM. An ARM is  
13 trued-up so that only the actual and specific costs of the program are recovered, and there  
14 can be no permanent over- (or under-) collection of revenues from customers for those  
15 specific costs. Further, the presence of the ARM does not change or impact base rates,  
16 the revenues collected, or the costs associated with base rates, and thus cannot contribute  
17 to any over- (or under-) earnings that may occur.

18 **Q. CAN THE COMPANY OVER-EARN ON ITS TRP INVESTMENT AND MAJOR**  
19 **STORM COSTS AS MR. BARON CLAIMS?<sup>4</sup>**

20 A. No. The TRP & MS Rider is designed to recover only the costs incurred. If revenues are  
21 over-collected in a period, they will be deferred and used to reduce revenue requirements

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<sup>3</sup> Baron page 11, lines 5-7.

<sup>4</sup> Baron page 10, lines 11-12.

1 in subsequent periods. The Company cannot over- (or under-) earn on its TRP  
2 investments and Major Storm costs.

3 **Q. MR BARON'S SOLUTION IS TO HAVE A BASE RATE CASE WHERE ALL**  
4 **COSTS CAN BE LOOKED AT IN TOTAL. PLEASE COMMENT.**

5 A. Setting aside the fact that the Company very recently completed a base rate case in which  
6 ETEC was an active participant, it seems that a base rate case is not, in fact, what ETEC  
7 wants at all. Instead, Mr. Baron advocates for the deferral of all costs associated with the  
8 proposed TRP and Major Storms until the Company files another rate case. He goes on  
9 to state that the Company would then have the opportunity to recover in its rates its  
10 reasonable deferred costs on a prospective basis.<sup>5</sup>

11 **Q. WILL MR. BARON'S PROPOSED APPROACH RETURN ANY OVER-**  
12 **EARNINGS ASSOCIATED WITH BASE RATES, SHOULD THEY OCCUR, TO**  
13 **CUSTOMERS?**

14 A. No. Under Mr. Baron's proposal to defer all costs associated with the TRP and Major  
15 Storms until the Company's next base case, the Company would continue to over- (or  
16 under)-earn during that interim period.

17 **Q. WOULD ANY OVER- (OR UNDER-) EARNINGS ASSOCIATED WITH BASE**  
18 **RATES OCCURING DURING THE INTERIM PERIOD BE APPLIED TO THE**  
19 **DEFERRED TRP & MAJOR STORM COSTS UNDER THIS APPROACH?**

20 A. No. His proposed remedy does nothing to address his concern.

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<sup>5</sup> Baron page 12, lines 11-15.

1 **Q. MR BARON STATES THAT AN ARM SHOULD ONLY BE REQUIRED IF THE**  
2 **COMPANY DEMONSTRATES A FINANCIAL NEED TO RECOVER COSTS**  
3 **CONCURRENTLY.<sup>6</sup> IS THERE ANY BASIS FOR THIS STATEMENT?**

4 A. Nowhere in the Tennessee code does such a requirement exist. Further, no utility in  
5 Tennessee that has been granted an ARM has had that requirement imposed upon it, that I  
6 am aware of.

7 **Q. ASIDE FROM THE FALLACIES IN MR. BARON'S ARGUMENTS, ARE**  
8 **THERE REASONS WHY THE USE OF AN ARM IS PREFERABLE TO**  
9 **DEFERRING COSTS UNTIL THE NEXT BASE RATE CASE?**

10 A. Yes, there are several reasons. First, the use of an ARM ensures that only the exact costs  
11 of the programs are recovered through the periodic true-ups and resetting of ARM rates.  
12 Deferring costs, then setting a base rate designed to recover those costs at some point in  
13 the future merely constructs the opportunity to over- (or under)-earn on that deferred  
14 asset in the future. The second reason concurrent recovery of costs through an ARM is  
15 preferable to deferring costs for future recovery is that current customers, who will  
16 benefit from the program, will pay for the program. There is no justification to have  
17 future customers pay for current customers to benefit from improved reliability or storm  
18 restoration efforts when concurrent recovery mechanisms are available. In addition, the  
19 cost of conducting an annual review, limited to the issues in this ARM filing, pales in  
20 comparison to the cost to conduct a full base rate case. Finally, the deferral of costs  
21 accumulating at the Company's weighted average cost of capital will serve to increase  
22 revenue requirements well above what would be if recovered from customers

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<sup>6</sup> Baron page 13, lines 3-5.

1 concurrently, further exacerbating the cost-shifting to future customers in favor of current  
2 customers.

3 **Q. DOES THE TENNESSEE CODE ALLOW FOR THE IMPLEMENTATION OF**  
4 **AN ARM TO ALLOW FOR PUBLIC UTILITY RATE REVIEWS AND COST**  
5 **RECOVER IN LIEU OF A GENERAL RATE CASE PROCEEDING?**

6 A. Yes. Tennessee Code § 65-5-103 allows a public utility to request a mechanism to  
7 recover both the operational expenses and capital costs for investments that ensure the  
8 reliability of the public utility plant in service or for weather-related disasters. The  
9 Company's proposed TRP & MS Rider meet these criteria.

10 **Q. MR BARON DISCUSSES, AT GREAT LENGTH, THE ALLOCATION OF**  
11 **VEGETATION MANAGEMENT COSTS IN OTHER JURISDICTIONS IN**  
12 **WHICH APCO OPERATES. PLEASE DISCUSS.**

13 A. The statutes and Commission practices in Virginia and West Virginia are not in dispute in  
14 this case. The Company originally proposed in Docket No. 16-00001 to allocate costs  
15 associated with vegetation management and major storms on a cost-of-service basis,  
16 which if it had been adopted by parties in that case, would have resulted in a significantly  
17 lower proposed allocation to ETEC customers than what is proposed by the Company in  
18 this Docket. That also would have been more consistent with how costs are allocated in  
19 the other states in which APCo operates. However, the Company understands that  
20 Commissions have latitude to determine how costs are allocated and this Commission  
21 approved a settlement less than one year ago that allocated costs identical to those in the  
22 TRP & MS Rider among customer classes in the manner consistent with the Company's  
23 proposal in this Docket. It is for this reason that the Company's proposed allocation of



costs in this Docket is different from what the Company proposed in Docket No. 16-00001 and similar dockets in other states.

**Q. CPAD WITNESS NOVAK RECOMMENDED APPROVAL OF THE TRP PROGRAM AND TRP & MS RIDER. ARE THERE ANY PARTS OF HIS TESTIMONY THAT THE COMPANY WISHES TO ADDRESS?**

**A.** Yes. The Company wishes to reiterate that the MS portion of the proposed TRP & MS Rider is for the recovery of major storm costs that are above the amount in base rates or to return to customers the difference in actual storm costs and the amount of storm costs in base rates. If there are no major storm costs in the review period, the amount in base rates, \$392,381, will be returned to customers in the form of a credit to the TRP & MS Rider. In Mr. Novak's testimony discussion of Major Storms, he only mentioned the possibility of storm costs above the amount in base rates. However, it is also probable, in any year, that actual Major Storm costs will be below the amount in base rates, which will result in a credit to the rider.

**Q. DOES THE COMPANY HAVE ANY OBJECTIONS TO MR. NOVAK'S RECOMMENDATION THAT THE COMPANY MAKE AN ANNUAL REPORT OF MULTIPLE METRICS TO INFORM PARTIES AS TO THE EFFICACY OF THE PROGRAM<sup>7</sup>?**

**A.** No. The Company agrees to provide the information as requested.

**Q. MR. NOVAK ALSO RECOMMENDS ANNUAL TRUE-UP FILINGS BE ACCOMPANIED BY AN ATTESTATION THAT THE COSTS AND EXPENSES INCLUDED IN THE TRP & MS RIDER ARE COMPLETE AND ACCURATE**

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<sup>7</sup> Novak page 14, lines 1-16.

1           **AND REFLECT THE AMOUNTS INCLUDED ON KINGSFORT'S BOOKS**  
2           **AND RECORDS. IS THE COMPANY WILLING TO PROVIDE SUCH AN**  
3           **ATTESTATION<sup>8</sup>?**

4    A.     Yes.

5    **Q.     DO YOU HAVE ANY ADDITIONAL COMMENTS REGARDING MR.**  
6           **NOVAK'S TESTIMONY?**

7    A.     Yes. The Company wishes to reiterate the importance of looking at multiple years of  
8           data to establish trends in reliability statistics. Mr. Novak accurately represented  
9           statistics for Kingsport's Tennessee peers in his testimony using three years of data.<sup>9</sup>  
10          While those data show Kingsport near the bottom of the peer group in reliability, they  
11          do not clearly show the deterioration of Kingsport's reliability statistics over time. This  
12          trend is apparent in Figure 1 and Figure 2 of Company witness Wright's direct  
13          testimony which uses seven years of data.

14   **Q.     DOES THIS CONCLUDE YOUR REBUTTAL TESTIMONY?**

15   A.     Yes, it does.

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<sup>8</sup> Novak page 25, lines 4-7.

<sup>9</sup> See Novak's Table 1 and Table 2, pages 8 and 9.

**CERTIFICATE OF SERVICE**

The undersigned hereby certifies that the foregoing Rebuttal Testimony of William K. Castle has been served upon the following by Email and mailing a copy of same by United States mail, postage prepaid, as follows, on this the 31<sup>st</sup> day of July, 2017.

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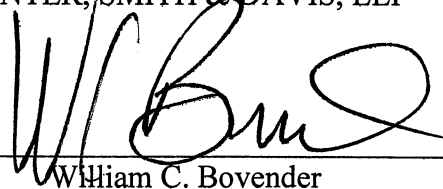
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HUNTER, SMITH & DAVIS, LLP

By



William C. Bovender