S. Morris Hadden
William C. Bovender
William C. Argabrite
Jimmie Carpenter Miller
Mark S. Dessauer
Gregory K. Haden
Michael L. Forrester
Stephen M. Darden
Edward J. Webb, Jr.
James N. L. Humphreys
Suzanne Sweet Cook
Michael S. Lattier
Scott T. Powers
Respond to:
Kingsport Office
William C. Bovender
423-378-8858
bovender@hsdlaw.com

HUNTER·SMITH·DAVIS LLP
SINCE 1916

Kingsport Office
1212 North Eastman Road
P.O. Box 3740
Kingsport, TN 37664
Phone (423) 378-8800
Fax (423) 378-8801

Johnson City Office
100 Med Tech Parkway
Suite 110
Johnson City, TN 37604
Phone (423) 283-6300
Fax (423) 283-6301

Leslie Tentler Ridings
Christopher D. Owens
Chad W. Whitfield
Jason A. Creech
Meredith Bates Humbert
Joseph B. Harvey
Rachel Ralston Mancl
Caroline Ross Williams
Marcy E. Walker
Matthew F. Bettis
Teresa Mahan Lesnak *
Michael A. Eastridge *
Jeannette Smith Tysinger*

**Of Counsel*

KPOW.95206

September 25, 2018

VIA EMAIL (Sharla.Dillon@tn.gov) & FEDEX
Mr. David Jones, Chairman
c/o Sharla Dillon, Dockets & Records Manager
Tennessee Public Utility Commission
502 Deaderick Street, 4th Floor
Nashville, TN 37243

RE: FILING OF KINGSPORT POWER COMPANY d/b/a AEP APPALACHIAN POWER ("KgPCo") IN RESPONSE TO TENNESSEE PUBLIC UTILITY COMMISSION INVESTIGATION OF IMPACT OF FEDERAL TAX REFORM ON THE REVENUE REQUIREMENTS OF KgPCo
DOCKET NO.: 18-00038

Dear Chairman Jones:

On behalf of Kingsport Power Company, we transmit herewith the following:

Direct Testimony of William K. Castle

The original and four (4) copies are being sent via Federal Express.

Very sincerely yours,

HUNTER, SMITH & DAVIS, LLP

Joseph B. Harvey

Enclosure: As stated

cc: Daniel P. Whitaker, III, Asst. Attorney General (w/enc.) ***Via U.S. Mail and Email: Daniel.Whitaker@ag.tn.gov***
Karen H. Stachowski, Esq. (w/enc.) ***Via U.S. Mail and Email: Karen.Stachowski@ag.tn.gov***
Kelly Grams, General Counsel (w/enc.) ***Via U.S. Mail and Email: Kelly.Grams@tn.gov***
Monica L. Smith-Ashford, Esq. (w/enc.) ***Via U.S. Mail and Email: monica.smith-ashford@tn.gov***
David Foster (w/enc.) ***Via U.S. Mail and Email: david.foster@tn.gov***
Michael J. Quinan, Esq. (w/enc.) ***Via U.S. Mail and Email: mquinan@cblaw.com***

KgPCo Exhibit No. ___
Witness: WKC

**DIRECT TESTIMONY OF
WILLIAM K. CASTLE
ON BEHALF OF KINGSPORT POWER COMPANY
D/B/A AEP APPALACHIAN POWER
BEFORE THE TENNESSEE PUBLIC UTILITY COMMISSION
DOCKET NO. 18-00038**

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

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

Q. PLEASE SUMMARIZE YOUR EDUCATIONAL BACKGROUND AND BUSINESS EXPERIENCE.

A. I earned a Bachelor of Science degree in Mechanical Engineering from Tulane University in 1988, and a Masters of Business Administration degree from the University of Texas – Austin in 1998. I hold the Chartered Financial Analyst (CFA) designation. I have worked in the utility industry since 1998, beginning with the Columbia Energy Group, Herndon, Virginia, where I held positions in financial planning and corporate finance. Subsequent to the acquisition of Columbia Energy Group by Merrillville, Indiana based NiSource in 2000, I performed financial planning and analysis functions. Since 2004, and prior to my current position, I was employed by American Electric Power Service Corporation (AEPSC) in the Corporate Planning and Budgeting department. Assignments included resource planning and demand-side management analysis, which encompasses Energy Efficiency and Demand Response. I have been in my current position since July, 2014.

Q. HAVE YOU PREVIOUSLY SUBMITTED TESTIMONY AS A WITNESS BEFORE ANY REGULATORY COMMISSION?

A. Yes. I presented testimony on behalf of Kingsport Power in Docket Nos. 16-0001 and 17-00032 and on behalf of APCo before the Virginia State Corporation Commission, most recently in Case Nos. PUR-2018-00051, and PUR-2018-00153. I have also presented testimony in the states of Ohio, Oklahoma, Indiana, West Virginia, and Arkansas.

Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY IN THIS PROCEEDING?

A. I support the Company's proposal to credit customers with the tax savings that have arisen from the Tax Cuts and Jobs Act of 2017.

Q. ARE YOU SPONSORING ANY EXHIBITS?

A. Yes. I am sponsoring the following exhibits:

- KgPCo Exhibit No. 1 (WKC): Company's Response to the Commission's Order in Docket No. 18-00001.
- KgPCo Exhibit No. 2 (WKC): Proposed Federal Tax Rate Adjustment Rider

Q. BRIEFLY SUMMARIZE THE COMPANY'S PROPOSAL.

A. As described in Exhibit 1, the Company proposes to credit customers with tax savings by reducing or eliminating uncollected regulatory asset balances and via a credit rider that effectively reduces the base rates established in its last base rate case (Docket No. 16-0001). The Company includes in this filing (Exhibit 2), its proposed Federal Tax Rate Adjustment Rider which has been provided to the parties in discovery (ETEC 1-3).

Q. ARE THERE ANY CHANGES OR CORRECTIONS TO THE COMPANY'S RESPONSE TO THE COMMISSION IN DOCKET NO. 18-00001?

A. Yes. The Company used a "Revenue Basis Factor" of 1.266 in its response. In subsequent discovery, the Company acknowledged the revenue basis factor of 1.3528, which reflects state tax treatment, is appropriate in this case. This has the effect of increasing the Company's proposed annual credit amount from $1,348,650 to $1,441,344.

Q. IN THE COMPANY'S PROPOSAL, THE COMPANY SEEKS TO ELIMINATE OR REDUCE REGULATORY ASSET BALANCES WITH UNPROTECTED EXCESS ADFIT. IF THE COMMISSION DOES NOT ADOPT THIS TREATMENT FOR SOME OR ALL OF THE EXCESS UNPROTECTED ADFIT, WHAT AMORTIZATION PERIOD DOES THE COMPANY PROPOSE FOR THE OUTSTANDING BALANCE?

A. The Company proposes to credit customers with any remaining unprotected excess unprotected ADFIT balance over a period of 10 years.

Q. DOES THIS CONCLUDE YOUR DIRECT TESTIMONY?

A. Yes, it does.

BEFORE THE TENNESSEE PUBLIC UTILTY COMMISSION

NASHVILLE, TENNESSEE

IN RE: FILING OF KINGSPORT POWER COMPANY d/b/a AEP APPALACHIAN POWER ("KgPCo") IN RESPONSE TO TENNESSEE PUBLIC UTILITY COMMISSION INVESTIGATION OF IMPACT OF FEDERAL TAX REFORM ON THE REVENUE REQUIREMENTS OF KgPCo	))))))))	DOCKET NO.: 18-______

FILING OF KINGSPORT POWER COMPANY D/B/A AEP APPALACHIAN POWER ("KgPCo") IN RESPONSE TO TENNESSEE PUBLIC UTILITY COMMISSION INVESTIGATION OF IMPACT OF FEDERAL TAX REFORM ON THE REVENUE REQUIREMENTS OF KgPCo

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Comes Kingsport Power Company, d/b/a AEP Appalachian Power (herein "KgPCo" or "Company"), and respectfully submits its response to the Tennessee Public Utility Commission's February 6, 2018 Order Opening an Investigation and Requiring Deferred Accounting Treatment as set forth in Docket No. 18-00001. This filing, opening a separate Docket, is made pursuant to Page 6, Paragraph 3 of the Commission's Order in said Docket No. 18-00001. In that Order, the Commission required certain public utilities, including the Company, to immediately apply deferred accounting treatment described therein with respect to the impact of the lowering of the federal corporate income tax rate; to provide the amounts deferred and submit certain calculations to the Commission by no later than March 31, 2018; and to submit ratemaking proposals to account for the tax benefits resulting from the 2017 Tax Cuts and Jobs Act ("Tax Act") by that same date. KgPCo would show the Commission as follows:

1. Upon receipt of the Commission's Order, KgPCo began to track and accumulate monthly in a deferred account the portion of its revenue representing the difference between the

cost of service approved by the Commission in its most recent rate case (Docket No. 16-00001) and the cost of service that would have resulted had the provision for federal income taxes ("FIT") been based on 21% rather than 35%. The amount deferred monthly is designed to equate to $904,383 annually. The derivation of this amount is shown on the accompanying Schedule, Section A. As of March 31, 2018, KgPCo's books reflect a deferred liability in the amount of $232,699 associated with this excess FIT expense. The journal entries associated with accounting for the difference in corporate FIT rates, on an annual basis, is shown in the accompanying Schedule, Section B.

2. KgPCo also calculated the excess accumulated deferred income tax ("ADIT") reserve caused by the reduction in the corporate FIT rate and recognized as a deferred liability, as of December 31, 2017, the estimated reduction of the utility's revenue requirement. Kingsport estimated these amounts, which are subject to change until such time that the Company files its tax return, to be $13,591,820, on a revenue basis. This amount is comprised of $9,329,605 in "protected" ADIT, and $4,262,215 of "unprotected" ADIT, both on a revenue basis. The journal entries associated with this accounting are shown in the accompanying Schedule, Section C.

3. As reported to the Commission, Kingsport earned its authorized rate of return on common equity in 2017. It also expects to prospectively earn its allowed return over the near term. As a result, the Company is able to propose to return the tax savings associated with the Tax Act to its customers.

4. Unprotected ADIT balances can be used to offset regulatory asset balances that have not yet been collected from customers, and are not part of base rates. The Company currently has before the Commission in Docket No. 17-00143, a request to recover $1,505,354 in

deferred costs (primarily associated with the 2013 winter storm) over two years or $752,677 annually. The Company proposes to offset this regulatory asset with a corresponding portion of the unprotected excess ADIT liability, eliminating the need to recover the winter storm costs through the rider proposed in that Docket. If approved, the unprotected excess ADIT balance would be reduced to an estimated $2,756,861.

5. The Company further proposes to use the remainder of its unprotected excess ADIT balance to offset a portion of the uncollected fuel and purchased power balances, which as of February 28, 2018, total $7,418,359. The cold winter of 2017-2018 has contributed to that balance, which exceeds the remaining excess unprotected ADIT.

6. Offsetting deferred winter storm costs and a portion of the uncollected fuel and purchased power balances with the excess unprotected ADIT balance is an efficient way to return this balance to customers, as it offsets expenses that the Company would otherwise recover from customers over a relatively short time horizon.

7. As indicated in numbered paragraph 1, the difference between the cost of service approved by the Commission in KgPCo's most recent case (Docket No. 16-0001), and the cost of service that would have resulted had the provision for FIT been based upon 21% rather than 35%, equates to an annual revenue reduction of $904,383. As indicated in numbered paragraph 2, KgPCo currently has deferred on its books $9,329,605 of protected excess ADIT. Protected excess ADIT balances must be amortized over periods prescribed in the tax code to avoid a "normalization" violation. The Company has estimated the effective amortization period of its

protected balances to be 21 years[1]. Returning the deferred excess balance to its customers over this period would result in an additional annual revenue reduction of $444,267.

8. Because the change in the corporate tax rate is ongoing, and protected deferred taxes must be amortized over a period specified by the IRS, estimated to be 21 years, the Company proposes to return to customers the current excess FIT expense, and the excess protected ADIT balance, in the form of a credit rider to their respective rate schedules. Given current information, the ongoing annual amount is estimated to be $1,348,650 ($904,383 plus $444,267), as shown in Section A, line 5 of the accompanying Schedule. The allocation of the credits will follow the allocation of base rates approved by the Commission in the Company's most recent base rate case (Docket No. 16-00001). The Company proposes to implement the rider October 1, 2018, with annual true-up filings and adjustments as necessary until the Company's next base rate case. Truing up the actual credits to the excess protected ADIT schedule is necessary to avoid a normalization violation.

9. In addition, the Company proposes to return the excess FIT expense deferred in accordance with paragraph 1 of this Response, for the period of January 1, 2018- September 30, 2018 (expected to be approximately $678,287), over the period October 1, 2018-September 30, 2019.

10. Under the Company's proposal, the customer credit rider for the period October 1, 2018 – September 30, 2019 will reflect the on-going annual credit amount of $1,348,650, and the

[1] The Average Rate Assumption Method ("ARAM") will be utilized to amortize the excess deferred income tax ("EXDFIT") balance over the remaining useful life of the associated assets as prescribed by the Internal Revenue Service ("IRS"). The Company's tax software will, by the closing of the quarterly financial statements in mid-April, determine the amortization over the remaining life of the assets in accordance with the ARAM. The amortization period of 21 years used in this filing is therefore an indicative estimate.

deferred FIT from the period January 1, 2018 – September 30, 2018 of $678,287, for a total of $2,026,937.

11. The Company proposes to change the customer credit rider October 1, 2019, and each year thereafter until the Commission sets new base rates, to reflect only the on-going annual credit of $1,348,650, plus or minus any under-or over-returned balances (the true-up balances). The Company proposes to amortize the true-up balances over each subsequent 12 month period.

WHEREFORE, the Company respectfully requests that the Commission issue an order:

1. Finding that KgPCo has complied with the Commission's February 6, 2018 Order in Docket No. 18-0001; and

2. Approving KgPCo's ratemaking proposals to account for the tax benefits of the Tax Act.

Respectfully submitted this the 29th day of March, 2018.

KINGSPORT POWER COMPANY d/b/a AEP APPALACHIAN POWER

By: ______________________
William C. Bovender, Esq.
Joseph B. Harvey, Esq.
HUNTER, SMITH & DAVIS, LLP
PO Box 3740
Kingsport, TN 37665
Ph: (423) 378-8858

James R. Bacha, Esq.
American Electric Power Service Corporation
1 Riverside Plaza
Columbus, OH 43215
Ph: (615) 716-1615; Fax: (614) 716-2950
Email: jrbacha@aep.com

Noelle J. Coates, Senior Counsel
American Electric Power Service
Corporation
Three James Center
Suite 1100 1051 E. Cary Street
Richmond, VA 23219-4029
Ph: (804) 698-5541
Email: njcoates@aep.com

CERTIFICATE OF SERVICE

The undersigned hereby certifies that the foregoing **RESPONSE OF RESPONDENT KINGSPORT POWER COMPANY d/b/a AEP APPALACHIAN POWER** has been served by mailing a copy of same by United States mail, postage prepaid, and Email, to below on this the 29th day of March, 2018, as follows:

Kelly Grams, General Counsel
Tennessee Public Utility Commission
502 Deaderick Street, 4th Floor
Nashville, TN 37243
Email: kelly.grams@tn.gov

David Foster, Chief-Utilities Division
Tennessee Public Utility Commission
502 Deaderick Street, 4th Floor
Nashville, TN 37243
Email: David.Foster@tn.gov

Monica L. Smith-Ashford
Tennessee Public Utility Commission
502 Deaderick Street, 4th Floor
Nashville, TN 37243
Email: monica.smith-ashford@tn.gov

Daniel P Whitaker, III, Assistant Attorney General
Karen H. Stachowski
Office of the Tennessee Attorney General
Public Protection Section
Consumer Protection and Advocate Division
P.O. Box 20207
Nashville, Tennessee 37202-0207
Daniel.Whitaker@ag.tn.gov
Karen.Stachowski@ag.tn.gov

J.W. Luna, Esq.
Luna Law Group, PLLC
Attorney of Record for Chattanooga Gas Company
333 Union Street, Suite 300
Nashville, TN 37201
jwluna@lunalawnashvile.co

A. Scott Ross, Esq.
Neal & Harwell, PLC
Attorney of Record for Atmos Energy Corporation
1201 Demonbreun Street, Suite 1000
Nashville, TN 37203
sross@nealharwell.com

Melvin J. Malone
Butler Snow LLP
Attorney of Record for Tennessee-American Water Company
The Pinnacle at Symphony Place
150 3rd Avenue South, Suite 1600
Nashville, TN 37201
melvin.malone@butlersnow.com

HUNTER, SMITH & DAVIS, LLP

By:______________________________
William C. Bovender

Kingsport Tax Reform Impacts Schedule

Section A

line #	Federal Income Tax Expense	TN Retail [A]	Revenue Basis Factor [B]	Revenue Basis [C] = [A] x [B]	Amortization Period [D]	Annual Revenue Reduction [E] = [C] x [D]
1	(Docket No. 160001, Attachment A, Schedule 9 of the Stipulation and Settlement Agreement)	$ (1,786,157)				
2	Tax Savings (1-[21%/35%]) x FIT	$ (714,463)	1.266	$ (904,383)	1	$ (904,383)
3	Distribution Excess ADIT Protected (12/31/2017)	$ (7,370,388)	1.266	$ (9,329,605)	21	$ (444,267)
4	Distribution Excess ADIT Unprotected (12/31//2017)	$ (3,367,150)	1.266	$ (4,262,215)	N/A	
5	Estimated Annual Ongoing Credit Rider					$ (1,348,650)
	*Revenue Gross-up Factor		1/[1-21%] = 1.266			

Section B

Journal Entry (on an annual basis) for the excess tax until current rates change (i.e., proposed credit rider starts):

	Reduction in FIT Expense	
Debit Account 449	$ 904,385	
Credit Account 229		$ 904,385

Section C

Journal Entries for the excess tax on distribution property as of December 31, 2017:

	Protected	
Debit Account 282	$ 7,370,388	
Debit Account 190	$ 1,959,217	
Credit Account 254		$ 9,329,605

	UnProtected	
Debit Account 282/283	$ 3,367,150	
Debit Account 190	$ 895,065	
Credit Account 254		$ 4,262,215

KgPCo Exhibit No. 1 (WKC)

FEDERAL TAX RATE ADJUSTMENT RIDER

Kingsport Power is authorized under the terms of this rider to apply a credit or charge to all customer bills rendered by the Company to reflect the impacts of changes to the Federal Corporate Income Tax Rate not included in base rate or other tariff schedules.

1. Applicability

Credits or charges resulting from changes in the Federal Income Tax Rate not otherwise incorporated in rate schedules in this tariff shall be applied to all Distribution function base rates in the form of a percentage credit or charge to those rates. The credit or charge will apply to the Service, Energy, Demand, and Lamp charge components of the distribution portion of the schedules. The credit or charge is not applicable to Rider schedules in this tariff.

2. Determination of Credit or Charge Percentage

The aggregate credit or charge amounts shall be determined by the Tennessee Public Utility Commission. The percentage credit or charge will remain in place until modified or discontinued by the Tennessee Public Utility Commission.

3. Notification of Change in Charge by the Company

The Company will provide no less than a 30-day notice of the proposed effective date in any change in the federal tax rate adjustment to its customers. The Company will also provide the calculations and other information supporting the proposed purchased power charges to the Staff of the Tennessee Regulatory Authority 30 days prior to the effective date of such charge.

4. Credit or Charge

Pursuant to the provisions of this Rider, a Federal Tax Rate Adjustment Rider credit or charge will be applied to each kilowatt-hour, kilowatt or lamp rate as billed under the Company's filed tariff non-rider schedules.

The Federal Tax Rate Adjustment Rider percentage credit or charge applicable to each schedule for the period Month 01, 201X to Month XX, 201X, is a credit or reduction to rates of 5.045%: