Before the Public Service Commission
of Kentucky

Rebuttal Testimony

of

Michael D. McCuen

on behalf of

Liberty Utilities Co.

TABLE OF CONTENTS
FOR THE REBUTTAL TESTIMONY OF MICHAEL D. MCCUEN
LIBERTY UTILITIES CO.
BEFORE THE PUBLIC SERVICE COMMISSION OF KENTUCKY

CASE NO. 2021-00481

SUBJECT **PAGE**

REBUTTAL TESTIMONY OF MICHAEL D. MCCUEN
ON BEHALF OF LIBERTY UTILITIES CO.
BEFORE THE PUBLIC SERVICE COMMISSION OF KENTUCKY

CASE NO. 2021-00481

I. INTRODUCTION

Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

A. My name is Michael D. McCuen. My business address is 602 S. Joplin Avenue, Joplin MO 64801.

Q. BY WHOM ARE YOU EMPLOYED AND IN WHAT CAPACITY?

A. I am the Director, U.S. Tax Planning and Strategy for Liberty Utilities Services Corp., a wholly owned subsidiary of Liberty Utilities Co.

Q. ON WHOSE BEHALF ARE YOU TESTIFYING?

A. I am testifying on behalf of Liberty Utilities Co. ("Liberty").

Q. PLEASE DESCRIBE YOUR EDUCATIONAL AND PROFESSIONAL BACKGROUND.

A. I received a Bachelor of Business Administration degree in Accounting from Franklin University in 1992. I received a Juris Doctor degree from Capital University Law School in 2000. I am a Certified Public Accountant in the State of Ohio; I am licensed to practice law in the State of Ohio. I held various accounting and tax positions through 2007. In 2007, I joined Mettler-Toledo as U.S. Tax Manager with responsibility for all income tax matters for their U.S. subsidiaries. In 2012, I was named Head of U.S. Taxation for Mettler-Toledo with responsibility for all tax matters within the U.S. I joined NiSource Corporate Services Company, a management and services subsidiary of NiSource, in May 2012 as Director of Income Taxes. I have worked at Liberty as both Senior Tax Manager since January 2021 and in my current position since September 2021.

Q. HAVE YOU PREVIOUSLY TESTIFIED BEFORE THE PUBLIC SERVICE COMMISSION OF KENTUCKY?

A. I have not. However, I have testified before the Indiana Utility Regulatory Commission, the Public Service Commission of Maryland, and the Public Utilities Commission of Ohio.

Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?

A. The purpose of my rebuttal testimony is to address certain positions taken by witness Lane Kollen on behalf of The Office of the Attorney General of the Commonwealth of Kentucky and the Kentucky Industrial Utility Customers, Inc. Specifically, I will address Mr. Kollen's assertion that there will be increased financing costs due to the loss of American Electric Power's ("AEP") reimbursement of tax effects to the AEP Tax Allocation Agreement.

II. MR. KOLLEN'S CONCLUSIONS REGARDING THE EFFECTS OF THE AEP TAX ALLOCATION AGREEMENT ARE INCORRECT.

Q. IS MR. KOLLEN CORRECT WHEN HE TESTIFIES THERE WILL BE INCREASED FINANCING COSTS DUE TO THE LOSS OF AEP'S REIMBURSEMENT TO KENTUCKY POWER OF TAX EFFECTS OF NET OPERATING LOSSES ("NOL") PURSUANT TO THE AEP TAX ALLOCATION AGREEMENT?

A. No. AEP expects to take a stand-alone net operating loss carryforward ("NOLC") position in Kentucky Power's next rate case. Second, Liberty would not use this exact reimbursement method because of consistency requirements of the normalization rules. I explain each of these reasons in more detail below.

Q. WHY MIGHT AEP NOT USE THIS METHOD ON A GO FORWARD BASIS?

A. AEP has filed applications over the last few years before regulatory bodies in Louisiana, Arkansas, Oklahoma, Texas, and Indiana to change its regulatory reporting of its NOL-Deferred Tax Asset ("DTA") because its past treatment of the NOLC for ratemaking purposes was not consistent with the normalization rules. As a result, AEP has contended that its GAAP books and records follow FERC guidance of a "company down" approach, which is appropriate for financial reporting purposes but not for ratemaking. Further, AEP has explained that FERC has established a precedent of a stand-alone method for income tax allowance within a utility's cost of service, which is the method Liberty intends on using. AEP witness Keaton's Rebuttal Testimony further addresses AEP's position on this topic.

Q. IS WITNESS KOLLEN AWARE THAT AEP HAS REQUESTED A CHANGE TO THE REGULATORY REPORTING OF ITS NOL-DTA IN THESE OTHER JURISDICTIONS?

A. Yes, at least as to the Louisiana filing. Mr. Kollen filed testimony on behalf of the Louisiana Public Service Commission Staff in the AEP Louisiana matter.

Q. MR. KOLLEN IS ADVOCATING THAT LIBERTY USE THE SAME APPROACH AS AEP CURRENTLY HAS IN PLACE IN KENTUCKY. IS THIS PRUDENT?

A. Not in my opinion. The current form of tax allocation agreement that AEP has in place in Kentucky is the very form of agreement that AEP is seeking to change in other regulatory jurisdictions because of the potential normalization violations. It would not make sense for Liberty to apply a method that AEP itself has sought to change in other jurisdictions. I understand that AEP expects to take a stand-alone NOLC position in Kentucky Power's next rate case in the event that Kentucky Power continues to be owned by AEP.

Q. IS THERE ANY HARM THAT COULD OCCUR AS A RESULT OF A NORMALIZATION VIOLATION?

A. A normalization violation could result in Kentucky Power not being allowed to use accelerated depreciation for income taxes purposes. Accelerated depreciation creates a timing difference resulting in a deferred tax liability which is included in rate base as a reduction, partially offsetting the associated property that is included in rate base that created the timing difference. If Kentucky Power was not permitted to use accelerated depreciation, this would result in an increase to the Company's rate base as there would not be a timing difference from the associated property.

Q. WHAT APPROACH TO TAX ALLOCATION DOES LIBERTY INTEND TO USE IN KENTUCKY?

A. Liberty would use the stand-alone approach based on FERC guidance from Opinion No. 173.[1] This approach looks to the books and records of Kentucky Power and does not bring in any other consolidated or affiliated utility attributes into the equation. This means Kentucky Power would generate and utilize its attributes independently of the consolidated group.

Q. CAN YOU EXPLAIN FURTHER YOUR REGULATORY STAND-ALONE APPROACH AS IT RELATES TO NOLS?

A. Yes. For regulatory tax matters, Kentucky Power will follow Internal Revenue Service (IRS) normalization rules when determining rate base and cost of service models, except for any Kentucky approved flow through items. These normalization rules also require that there be consistency with the assumptions used in the revenue requirement for

[1] Columbia Gulf Transmission Company; Docket No. RP75-105-002.

depreciation expense, tax expense, rate base, and the reserve for deferred taxes.[2] It is important to note that NOL-related deferred tax assets arising from accelerated depreciation must offset the related deferred tax liabilities for rate making purposes to avoid a potential normalization violation. IRC § 1.167(1)-1(h)(1)(iii) makes clear that the effects of a net operating loss carryforward must be considered for normalization purposes. Further, while that section provides no specific mandate on methods, it does provide that the IRS has discretion to determine whether a particular method satisfies the normalization requirements. IRC §1.167(1)-(h)(6)(i) provides that a taxpayer does not use a normalization method of regulated accounting if, for ratemaking purposes, the amount of the reserve for deferred taxes, which is either excluded from the base to which the taxpayer's rate of return is applied or treated as no-cost capital in those rate cases in which the rate of return is based upon the cost of capital, exceeds the amount of such reserve for deferred taxes for the period used in determining the taxpayer's expense in computing cost of service in such ratemaking. Because the ADIT account, the reserve account for deferred taxes, reduces rate base, the portion of a NOLC that is attributable to accelerated depreciation must be considered in calculating the amount of the reserve for deferred taxes (ADIT).[3]

Q. DO YOU BELIEVE THE APPROACH THAT LIBERTY INTENDS TO ADOPT IS REASONABLE?

A. Yes. As referenced above, FERC Opinion No. 173 set a precedent for the stand-alone method for ratemaking purposes. Under this approach, the stand-alone books and records of Kentucky Power are relied upon without consideration of any other consolidated or

---

[2] §26 U.S.C. §168 (i)(9)(B)
[3] PLR-116998-15 August 19, 2015

affiliated utility attributes into the equation. This is consistent with the rest of the rate making process. There should be no cross-subsidization, expenses, or benefits, between regulated or non-regulated businesses within a consolidated group.

Q. DOES THIS CONCLUDE YOUR TESTIMONY?

A. It does.

VERIFICATION

The undersigned, Michael D. McCuen, being duly sworn, deposes and says he is Director, U.S. Tax Planning and Strategy at Liberty Algonquin Business Services, that he has personal knowledge of the matters set forth in the foregoing Rebuttal Testimony and the information contained therein is true and correct to the best of his information, knowledge, and belief after reasonable inquiry.

Michael D. McCuen 3/18/22

Michael ~~D.~~ McCuen, ~~Affiant~~

COMMONWEALTH OF KENTUCKY)
)
COUNTY OF FAYETTE)

Sworn to, acknowledged and subscribed before me via video communications technology by Michael D. McCuen on this 18 day of March, 2022.

Janet Gross

Notary Public, State at Large - Kentucky
I.D. No. KYNP6586
My Commission Expires: 6-27-24