

**COMMONWEALTH OF KENTUCKY**  
**BEFORE THE PUBLIC SERVICE COMMISSION**

In the Matter of:

Electronic Application Of Kentucky Power Company For )  
(1) A General Adjustment Of Its Rates For Electric )  
Service; (2) Approval Of Tariffs And Riders; (3) Approval )  
Of Accounting Practices To Establish Regulatory Assets )  
And Liabilities; (4) A Securitization Financing Order; And )  
(5) All Other Required Approvals And Relief )  
)

Case No. 2023-00159

**REBUTTAL TESTIMONY OF**  
**STEVEN M. FETTER**  
**ON BEHALF OF KENTUCKY POWER COMPANY**

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**I. INTRODUCTION**

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

2 A. My name is Steven M. Fetter. I am President of Regulation UnFettered. My  
3 business address is 1240 West Sims Way, Port Townsend, Washington 98368.

4 **Q. DID YOU FILE DIRECT TESTIMONY IN THIS CASE?**

5 A. Yes, I filed direct testimony on behalf of Kentucky Power Company on June 29,  
6 2023.

**II. PURPOSE OF REBUTTAL TESTIMONY**

8 **Q. WHAT IS THE PURPOSE OF YOUR REBUTTAL TESTIMONY?**

9 A. The purpose of my rebuttal testimony is to respond to several arguments raised by  
10 Mr. Tyler Comings on behalf of Joint Intervenors.

11 **Q. WOULD YOU PLEASE SUMMARIZE YOUR REBUTTAL TESTIMONY?**

12 A. Yes. My rebuttal testimony relates to comments made by Mr. Comings about the  
13 internal operations of credit rating agencies. To my knowledge, Mr. Comings has  
14 never worked at a rating agency, and his views are at odds with my understanding  
15 of the ratings process, gained during my eight-and-a-half years at Fitch Ratings,  
16 one of the three major US rating agencies, the latter half of which time involved  
17 leading Fitch's utilities ratings practice. Mr. Comings also provides his views as to  
18 how investors will react to Kentucky Power during and after this rate proceeding.  
19 As a former member of the financial community, and member (now emeritus) of

1 the Wall Street Utility Group for the past twenty-two years, I disagree with Mr.  
2 Comings' position.

3 **Q. DO YOU AGREE WITH MR. COMINGS' ARGUMENTS THAT THE**  
4 **COMPANY'S CREDIT RATINGS WILL IMPROVE IN THE NEAR**  
5 **TERM<sup>1</sup>, AND THAT THE COMPANY'S FUTURE CREDIT RATINGS**  
6 **COULD IMPROVE SINCE IT IS ADDRESSING ISSUES THAT WERE A**  
7 **DRAG ON ITS CREDIT RATING<sup>2</sup>?**

8 A. No, certainly not prior to the outcome of this and other pending regulatory  
9 proceedings concerning the Company that are under consideration at the  
10 Commission. It is unrealistic to expect positive movement of the Company's credit  
11 ratings absent sustained improvement of its credit metrics, which in turn are  
12 dependent on constructive results in the regulatory proceedings that the Company  
13 is subject to in the normal course of its business.

14 **Q. DO YOU AGREE WITH MR. COMINGS' RECOMMENDATION THAT**  
15 **THE COMMISSION SHOULD NOT TAKE INTO CONSIDERATION THE**  
16 **INFORMATION THAT CREDIT RATING AGENCIES PROVIDE<sup>3</sup>?**

17 A. No, not at all. It would be contrary to the public interest to heed Mr. Comings'  
18 recommendation that the Commission should ignore information from the rating  
19 agencies, due to his incorrect view that the agencies are biased toward utilities.<sup>4</sup>  
20 Rating agencies carry out their function through public dissemination of  
21 information and their independent judgments of utility credit strength, which are

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<sup>1</sup> Comings Direct at 10.

<sup>2</sup> *Id.* at 12.

<sup>3</sup> *Id.* at 10.

<sup>4</sup> *Id.*

1 broadly relied upon by the financial community. Moreover, Mr. Comings is wrong  
2 in his underlying argument that the credit metrics that rating agencies use in their  
3 analysis of the Company's financial condition are not "contingent upon the  
4 Commission's decision in this case."<sup>5</sup> To the contrary, the very reason the Company  
5 has requested the Commission's approval to increase its base rates and the other  
6 relief requested in this case is primarily driven by the Company's need to improve  
7 its credit metrics and financial strength, which in turn are indispensable in enabling  
8 the Company to continue to provide dependable and reliable electric service to its  
9 customers at just and reasonable rates.

10 **Q. DO YOU AGREE WITH MR. COMINGS' POSITION THAT THE**  
11 **COMPANY'S LEVEL OF FINANCIAL DISTRESS HAS BEEN**  
12 **EXAGGERATED?**<sup>6</sup>

13 A. No, I do not. Mr. Comings' argument has no factual support, and cannot be  
14 reconciled with the Company's weak credit profile during the past several years, as  
15 publicly analyzed and reported by the credit rating agencies. The actual return on  
16 equity recently earned by the Company has been alarmingly low as compared to  
17 US electric industry norms. The Company's dire financial condition is a reality,  
18 and it would be unreasonable to ignore that fact in assessing the degree to which  
19 the Company is able to access the capital markets upon reasonable terms. On that  
20 note, Mr. Comings' argument that Kentucky Power does not need to raise equity  
21 capital from investors is also fundamentally wrong. As Mr. Comings concedes, the  
22 Company does require debt and equity capital to operate, and regardless of who the

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<sup>5</sup> *Id.* at 12.

<sup>6</sup> *Id.* at 4-5.

1 investors are, basic principles apply: for the Company to maintain reasonable  
2 access to the capital markets, investor returns must be commensurate with the  
3 investment risk – and this applies even when it is parent AEP deciding whether to  
4 infuse equity into one of its regulated subsidiaries across the eleven states within  
5 which AEP operates. Company Witness McKenzie addresses those expected  
6 returns more in detail, but for the purposes of my testimony, it is sufficient to  
7 highlight that absent a sustained improvement in the Company’s credit metrics, its  
8 financial condition will continue to be perceived as dire, leading to higher debt  
9 capital costs associated with low credit ratings.

10 **Q. BASED ON YOUR HIGH-LEVEL RATINGS EXPERIENCE, CAN YOU**  
11 **DISCUSS THE INTERNAL OPERATIONS OF THE RATING AGENCIES?**

12 A. Rather than reiterate the discussion of the ratings process included in my Direct  
13 Testimony, I can sum it up in one sentence with a key word highlighted: “A credit  
14 rating reflects an *independent* judgment of the general creditworthiness of an  
15 obligor or of a specific debt instrument.”<sup>7</sup> Although rating agencies maintain paid  
16 ratings relationships with utilities, the ratings agencies’ true “clients” are the  
17 investors who rely on utility ratings to make their investment decisions. If an  
18 agency were to be viewed as “in the bag” on behalf of the utilities with whom it  
19 maintains relationships, its assigned ratings would be worthless to the financial  
20 community and such agency would soon be out of business. Thus, I do not believe  
21 anyone in the financial community would agree with Mr. Comings’ belief that  
22 “rating agencies ..., of course, will always favor more allowed earnings than less.”<sup>8</sup>

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<sup>7</sup> Fetter Direct at 12.

<sup>8</sup> Comings Direct at 10.

1           Indeed, the Commission, far from being “beholden to rating agencies”<sup>9</sup>,  
2           should carefully consider the analyses of ratings agencies in its evaluation of the  
3           financial condition of the Company. Rating agencies provide independent insight  
4           into the Company’s financial health, and importantly their opinions are relied upon  
5           not only by debt investors, but also by the entire financial community. What should  
6           not be lost in this high-level discussion is that a downgrade results in an increase in  
7           the Company’s borrowing costs, with negative effects ultimately flowing into  
8           customer rates. Mr. Comings’ views cannot be reconciled with the fact that rating  
9           agencies’ assessments and credit opinions have a direct effect on the Company’s  
10          cost to provide service, and therefore should appropriately be considered by the  
11          Commission in its regulation of the Company.

12   **Q.   ALSO, CONCERNING RATING AGENCY OPERATIONS, CAN YOU**  
13   **EXPLAIN THE IMPORT OF THE “STABLE” OUTLOOK THAT ALL**  
14   **THREE MAJOR RATINGS AGENCIES HAVE ASSIGNED TO**  
15   **KENTUCKY POWER’S RATINGS?**

16   A.   Yes. All three agencies are relatively consistent with their treatment of outlooks.  
17   S&P recently republished its Global Ratings Definitions with the following  
18   language:

19                   **Ratings Outlooks:**

20                   An S&P Global Ratings outlook assesses the potential direction of  
21                   a long-term credit rating over the intermediate term, which is  
22                   generally up to two years for investment grade.... In determining a  
23                   rating outlook, consideration is given to any changes in economic  
24                   and/or fundamental business conditions. An outlook can be one of  
25                   the following:

- 26                   • Positive: a rating may be raised.
- 27                   • Negative: a rating may be lowered.

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<sup>9</sup> *Id.* at 10.

- Stable: a rating is not likely to change.
- Developing: a rating may be raised, lowered, or affirmed.<sup>10</sup>

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2  
3  
4 Moody's states that a "stable outlook indicates a low likelihood of a rating change over  
5 the medium term. ...After the initial assignment of a stable outlook, about 90% of ratings  
6 experience no change in rating during the following year."<sup>11</sup>

7 Fitch "Outlooks indicate the direction a rating is likely to move over a one-to-two-year  
8 period."<sup>12</sup>

9 **Q. DOES MR. COMINGS' TESTIMONY LINE UP WITH THESE**  
10 **CONCEPTS?**

11 A. No, it does not. Kentucky Power now holds credit ratings just above the  
12 investment-grade/non-investment grade dividing line, and actual equity returns  
13 among the lowest if not the lowest of any regulated US utility over the past four  
14 years. Under these circumstances, no member of the financial community would  
15 agree with Mr. Comings that Kentucky Power "has exaggerated its level of  
16 financial distress ... [painting] a dire picture of its credit rating and finances."<sup>13</sup>  
17 And coupled with the Stable outlooks at all three rating agencies, the financial  
18 community would not agree that "the Company's credit ratings will improve in the  
19 near term."<sup>14</sup> Mr. Comings' conjecture that the Company's ratings could improve  
20 prior to the Commission's decision in this rate case is unrealistic, and certainly is  
21 at odds with the Company's Stable outlooks. Indeed, it would be contrary to rating

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<sup>10</sup> S&P Report: "S&P Global Ratings Definitions," June 9, 2023.

<sup>11</sup> Moody's Report: "Rating Symbols and Definitions," January 2020.

<sup>12</sup> Fitch Report: "Rating Definitions," April 24, 2023.

<sup>13</sup> Comings Direct at 4-5.

<sup>14</sup> *Id.* at 10.



1 agencies' practices and basic analytical processes for the rating agencies to act prior  
2 to conclusion of a rate proceeding that will have a significant impact on the  
3 Company's financial future.

4 **Q. FINALLY, CAN YOU COMMENT ON MR. COMINGS' POSITION THAT**  
5 **KENTUCKY POWER HAS NO WORRIES VIS-À-VIS INVESTORS,**  
6 **BECAUSE THERE IS PARENT AEP ALWAYS THERE TO PROVIDE**  
7 **EQUITY SUPPORT?**

8 A. There is an inherent contradiction in Mr. Comings' comment that Kentucky Power  
9 has no need to attract outside investment because investors need only look to parent  
10 AEP. As Mr. Comings concedes, "Kentucky Power will need **debt and equity**  
11 **funds** available in order to operate in a safe, reliable manner[.]" [Emphasis added]  
12 It appears that Mr. Comings has not factored in that, as of June 30, 2023, Kentucky  
13 Power has over one billion dollars in outstanding debt<sup>15</sup> to investors who would  
14 have no recourse to AEP if Kentucky Power were to default on any of that debt –  
15 or the financial problems the Company would face if it could not refinance that debt  
16 upon reasonable terms. At this point, we can benefit from the guidance provided  
17 by Attorney General Witness Richard Baudino with regard to equity investment,  
18 but it applies equally to debt investment, as I will annotate with *italics*: "The key  
19 determinant in deciding whether to invest ... is based on comparative levels of risk.  
20 Our hypothetical [*equity or debt*] investor would not invest in a particular regulated

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<sup>15</sup> S&P recently quantified Kentucky Power's outstanding debt: "Debt maturities – Through 2023: \$275; 2024: \$215 million; 2025: --; 2026: \$265 million; 2027: \$40 million; and Thereafter: \$450 million." S&P Report: "Kentucky Power Co.," September 14, 2023.

1 electric utility stock [*or debt instrument*] if it offered a return [*or yield*] lower than  
2 other investments of similar risk.<sup>16</sup>

### III. CONCLUSION

3 **Q. DO YOU HAVE CONCLUDING THOUGHTS?**

4 A. Yes, the financial health of utilities and the environment of commissions when  
5 faced with that concern is a serious issue. My testimony is based on that serious  
6 issue and the impact it could have on customers. Mr. Comings mischaracterizes  
7 my Direct Testimony, which of course requires no paraphrasing. For example, Mr.  
8 Comings' paraphrase argues that:

9 [Mr. Fetter] warns that 'a less than constructive decision by the Commission  
10 in this case could lead to further negative credit rating actions' and foretells  
11 of potential 'junk bond status' *if the Commission does not grant the*  
12 *Company its request.*<sup>17</sup>

13 This is a mischaracterization of the language from my Direct Testimony, which  
14 instead states:

15 [A] less than constructive decision by the Commission in this case could lead  
16 to further negative credit rating actions, potentially moving the Company  
17 into below investment-grade territory. Such junk bond status would increase  
18 the Company's costs for capital, including its normal day-to-day capital  
19 investment for reliability during a time of increasing inflationary pressure,  
20 ultimately leading to higher rates for customers.<sup>18</sup>

21 And further states that:

22 I encourage the Commission to reduce any uncertainty as to this body's  
23 future regulatory direction that may exist by providing an ongoing  
24 constructive regulatory environment that respects the interests of all  
25 stakeholders within the regulatory process, including the consumers that pay  
26 the bills and the investors that fund the Company's operations.<sup>19</sup>

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<sup>16</sup> Baudino Direct at 4.

<sup>17</sup> Comings Direct at 10 (*Italics added*).

<sup>18</sup> Fetter Direct at 5.

<sup>19</sup> *Id.* at 18-19.

1           Contrary to Mr. Comings' argument and paraphrasing, my recommendations and  
2           observations are intended to be informative and descriptive of real-life  
3           considerations that have real-life effects on Kentucky Power's customers.

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

5   **A.    Yes.**



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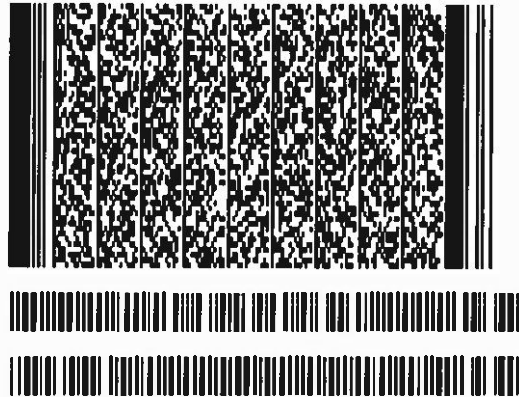
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### E-Signature Summary

**E-Signature 1: Steven M Fetter (SMF)**  
November 03, 2023 11:06:20 -8:00 [06652B6A5D20] [73.221.181.100]  
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November 03, 2023 11:06:20 -8:00 [8CADBF5B721A] [167.239.221.103]  
mmcaldwell@aep.com  
I, Marilyn Michelle Caldwell, did witness the participants named above electronically sign this document.



# VERIFICATION

The undersigned, Steven M. Fetter, being duly sworn, deposes and says he is the President, of Regulation Unfettered, that he has personal knowledge of the matters set forth in the foregoing testimony and the information contained therein is true and correct to the best of his information, knowledge, and belief after reasonable inquiry.

Steven M Fetter

Steven M. Fetter

Commonwealth of Kentucky )  
)  
County of Boyd )

Case No. 2023-00159

Subscribed and sworn to before me, a Notary Public in and before said County and State, by Steven M. Fetter, on November 3, 2023.

Notary Public

Marilyn Caldwell

MARILYN MICHELLE CALDWELL  
ONLINE NOTARY PUBLIC  
STATE AT LARGE KENTUCKY  
Commission # KYNP71841  
My Commission Expires May 05, 2027

Notarial act performed by audio-visual communication

My Commission Expires May 5, 2027

Notary ID Number KYNP71841

