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BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

JOINT APPLICATION OF MID-ATLANTIC INTERSTATE TRANSMISSION LLC (“MAIT”); METROPOLITAN EDISON COMPANY (“MET-ED”) AND PENNSYLVANIA ELECTRIC COMPANY (“PENELEC”) FOR: (1) A CERTIFICATE OF PUBLIC CONVENIENCE UNDER 66 PA.C.S. § 1102(A)(3) AUTHORIZING THE TRANSFER OF CERTAIN TRANSMISSION ASSETS FROM MET-ED AND PENELEC TO MAIT; (2) A CERTIFICATE OF PUBLIC CONVENIENCE CONFERRING UPON MAIT THE STATUS OF A PENNSYLVANIA PUBLIC UTILITY UNDER 66 PA.C.S. § 102; AND (3) APPROVAL OF CERTAIN AFFILIATE INTEREST AGREEMENTS UNDER 66 PA.C.S. § 2102

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Rebuttal Testimony
of
K. Jon Taylor

List of Topics Addressed

**Ground Leases, “Hold Harmless” Conditions,
Assignment And Allocation Of FirstEnergy Service Company Costs**

TABLE OF CONTENTS

| | Page |
|-------------------------------------|-------------|
| I. INTRODUCTION AND PURPOSE | 1 |
| II. RESPONSE TO MR. HAHN | 2 |
| A. Ground Leases | 2 |
| B. “Hold Harmless” Conditions | 6 |
| III. RESPONSE TO MS. GUMBY..... | 7 |
| IV. CONCLUSION..... | 8 |

**REBUTTAL TESTIMONY
OF
K. JON TAYLOR**

1 **I. INTRODUCTION AND PURPOSE**

2 **Q. Please state your name, title, and business address.**

3 A. My name is K. Jon Taylor. I am Vice President, Controller, and Chief Accounting
4 Officer of FirstEnergy Corp. (“FirstEnergy”) and a number of its subsidiaries, including
5 Metropolitan Edison Company (“Met-Ed”) and Pennsylvania Electric Company
6 (“Penelec”) (collectively, the “Companies”). My business address is 76 South Main
7 Street, Akron, OH 44308.

8 **Q. Have you previously presented testimony in this proceeding?**

9 A. Yes, on June 19, 2015, my Direct Testimony, Joint Applicants’ Statement No. 4 and the
10 accompanying Exhibits KJT-1 through KJT-8, were filed in this matter. On October 27,
11 2015, my Supplemental Direct Testimony, Joint Applicants’ Statement No. 4S and the
12 accompanying Exhibits KJT-9 and KJT-10, were served upon the parties and the
13 Administrative Law Judges.

14 **Q. What is the purpose of your Rebuttal Testimony?**

15 A. The purpose of my Rebuttal Testimony is to respond to portions of the Direct Testimony
16 of Richard D. Hahn, who submitted direct testimony on behalf of the Office of Consumer
17 Advocate (“OCA”) (OCA Statement No. 1) and Lisa A. Gumby, who submitted direct
18 testimony on behalf of the Bureau of Investigation and Enforcement (“I&E”) (I&E
19 Statement No. 1).

1 I will address issues raised by Mr. Hahn pertaining to the Ground Leases for transmission
2 land and land rights that will be entered into between Mid-Atlantic Interstate
3 Transmission, LLC (“MAIT”) and the Companies. I will also respond to Mr. Hahn’s
4 recommendations that the Pennsylvania Public Utility Commission (“PUC” or the
5 “Commission”) impose certain conditions if it approves the transaction for which
6 approval is sought in the Joint Application filed on June 19, 2015 (the “Transaction”).
7 Specifically, Mr. Hahn recommends conditions that customers be held “harmless” with
8 respect to: (1) the preservation of transmission-related accumulated deferred income tax
9 (“ADIT”) balances that will transfer to MAIT from the Companies pursuant to the terms
10 of the Transaction; and (2) costs incurred to complete the Transaction.

11 In response to Ms. Gumby, I will explain why the Transaction will not cause transmission
12 costs to be improperly allocated to the Companies.

13 **II. RESPONSE TO MR. HAHN**

14 **A. Ground Leases**

15 **Q. In his Direct Testimony, Mr. Hahn discusses the Ground Leases by which the**
16 **Companies will lease to MAIT transmission land and land rights on which the**
17 **transmission assets to be contributed to MAIT are located (OCA St. 1, p. 11, line 18**
18 **through p. 12, line 6). Mr. Hahn then states: “While it is not uncommon for utilities**
19 **to encounter logistical or other difficulties transferring rights-of-way and easements**
20 **that may have been acquired piecemeal over a great number of years, I am not fully**
21 **convinced that the Joint Applicants have demonstrated that the task is *not feasible***
22 **in this case” (OCA St. 1, p. 12, lines 10-13 (emphasis added)). Did the Joint**

1 **Applicants state that they propose to use Ground Leases because it is “not feasible”**
2 **to transfer title to land and land rights to MAIT?**

3 A. No, they did not. In fact, in the question and answer immediately preceding Mr. Hahn’s
4 statement that “the Joint Applicants have demonstrated that the task is not feasible,” he
5 summarized the Joint Applicants’ actual reasons for employing Ground Leases:

6 **Q. Why will the Operating Companies retain title to the**
7 **real property interests associated with the transmission**
8 **corridors?**

9 A. The Joint Applicants explain that the Transaction is
10 structured in this way to be more “efficient” and to avoid
11 the need for deeds, surveys, etc., that may otherwise be
12 associated with the transfer of real property.

13 Mr. Hahn cited my Direct Testimony (Joint Applicants’ St. 4, pp. 6-7) as the source of
14 the information in his answer, which explains the reasons for entering into Ground Leases
15 instead of transferring title to the transmission land and land rights to MAIT, as follows.

16 **Q. Why will the Operating Companies be entering into a**
17 **Ground Lease, rather than contributing a fee interest in**
18 **land and other real estate to MAIT?**

19 A. It is an administratively more efficient way to effect the
20 transfer. It is also consistent with the way transmission
21 facilities located in western Pennsylvania and Ohio were
22 transferred to American Transmission Systems,
23 Incorporated (“ATSI”) in 1999 and 2000, which
24 experience has shown provided ATSI all of the interests in
25 real property it needs to safely, reliably and efficiently
26 furnish transmission service. In summary, the use of a
27 ground lease to provide MAIT the interests in real property
28 it needs to operate and maintain the transmission facilities
29 enables a quicker transfer of property rights by avoiding the

1 need for surveys, deed recordings, and easement
2 negotiations.¹

3 While it may be “feasible” for the Companies to transfer title to the transmission land and
4 land rights to MAIT, doing so would entail a lengthy and expensive process requiring
5 land surveys, the preparation of metes and bounds descriptions for all applicable deeds,
6 recording of deeds in each county where any of the land and land rights are located, and
7 careful review of the easement agreements to assure that a transfer of title is consistent
8 with the terms of those agreements. The time, expense and expenditure of other
9 resources that process would require are avoided by using the Ground Leases.
10 Additionally, as I explained in my Direct Testimony, the Ground Leases provide MAIT
11 all of the rights and entitlements it needs to own, operate, maintain, rebuild, replace and
12 add to the transmission assets being transferred. As I also explained, a Ground Lease was
13 used in the ATSI/Penn Power transaction, which the Commission previously approved
14 and which experience has shown provides ATSI all of the real property interests it needs
15 to furnish safe, reliable and efficient transmission service. Furthermore, it is important to
16 note that Met-Ed’s and Penelec’s distribution and transmission facilities sometimes
17 utilize shared rights-of-way for lines running in parallel with, or due to distribution lines
18 being under-built on the transmission structures located on, the transmission rights-of-
19 way. Mr. Hahn fails to recognize that, if the land and land rights were transferred to
20 MAIT, Met-Ed and Penelec would, in turn, pay MAIT to use the right-of-way.

¹ Pennsylvania Power Company (“Penn Power”) transferred its transmission assets to ATSI pursuant to a certificate of public convenience evidencing the approval granted by the Commission in *Application Of Pennsylvania Power Co. For (1) A Certificate Of Public Convenience Authorizing The Transfer Of Certain Transmission Assets To American Transmission Systems, Inc., And (2) Approval Of Certain Affiliated Interest Agreements Necessary To Effect The Transfer*, Docket No. A-110450F0016 (July 14, 2000) (hereafter, “ATSI/Penn Power”). Penn Power is a subsidiary of Ohio Edison Company (which, in turn, is a subsidiary of FirstEnergy) that provides electric distribution service in western Pennsylvania.

1 Essentially, Mr. Hahn’s proposal would harm Met-Ed and Penelec’s distribution
2 customers rather than benefit them.

3 In summary, the Joint Applicants are not proposing to enter into the Ground Leases
4 because it is not “feasible” to transfer title to the transmission land and land rights but,
5 rather, because it is an administratively more efficient way to effect the transfer and using
6 the Ground Leases provides affirmative benefits as compared to a title transfer, which has
7 been demonstrated through the Ground Lease previously approved by the Commission
8 under similar circumstances in the ATSI/Penn Power case.

9 **Q. Mr. Hahn recommends that the “formula” set forth in the Ground Lease to**
10 **calculate the rental payments on the transmission land and land rights as well as the**
11 **“input variables” for that formula “should be defined with greater specificity”**
12 **(OCA St. 1, p. 16, lines 7-9). How do you respond?**

13 A. I disagree. The methodology for calculating “base rent” is set forth in Schedule A to the
14 Ground Leases (Joint Applicants’ Exhibit KJT-2, Schedule A) and is reproduced at page
15 13 of Mr. Hahn’s Direct Testimony. The methodology is detailed and contains all of the
16 elements necessary to calculate base rent to the Companies that reasonably corresponds
17 to the revenue requirement that MAIT would receive if the underlying land and land
18 rights were included in its rate base for purposes of calculating transmission rates subject
19 to the jurisdiction of the Federal Energy Regulatory Commission (“FERC”). Mr. Hahn
20 has not offered evidence or any explanation that would suggest the base rent
21 methodology set forth in the Ground Leases would produce rental payments that are
22 materially different from the revenue requirement that would be computed if MAIT or

1 the Companies sought to include the underlying transmission land and land rights in a
2 FERC-approved transmission rate. Moreover, while Mr. Hahn recommends that the base
3 rent methodology and its “input variables” “should be defined with greater specificity,”
4 he identified only one term that he alleged is “inconsistent with Commission ratemaking”
5 (OCA St. 1, p. 15, line 25 through p. 16, line 3). As to that term, Mr. Hahn’s claim of an
6 alleged inconsistency is wrong, as explained by Mr. Fullem in his Rebuttal Testimony
7 (Joint Applicants’ St. 1-R).²

8 **B. “Hold Harmless” Conditions**

9 **Q. Mr. Hahn recommends that the Commission impose a condition on its approval of**
10 **the Transaction that “customers should be held harmless for the loss of the ADIT**
11 **credit if the Joint Applicants are required to pay ADIT” (OCA St. 1, p. 34, lines 4-**
12 **6). How do you respond?**

13 A. Such a condition is not necessary. Mr. Hahn offers as the alleged basis for his proposed
14 condition that, while the Joint Applicants claim the transaction will not trigger the
15 payment of ADIT,” they “have not submitted a private letter ruling to confirm” that such
16 will be the case.

17 The Transaction has been structured as a non-taxable contribution of property by the
18 Companies to MAIT, which preserves the ADIT balances. Based on research, including
19 review of previous similarly-structured transactions, as well as through consultations with

² Mr. Hahn asserts that the base rent methodology is inconsistent with “Commission ratemaking” because depreciation cannot be recovered on “land.” As Mr. Fullem explains, the base rent methodology does not provide for depreciation on “land” as such, but on “land rights,” which is entirely consistent with the FERC’s Uniform System of Accounts and FERC and PUC ratemaking principles and practices.

1 a recognized international accounting firm, the Transaction will have the tax
2 consequences I described in my direct testimony.

3 **Q. Mr. Hahn also recommends that the Commission impose a condition on its approval**
4 **of the Transaction that “[a]ll costs to achieve the Transaction will be excluded from**
5 **distribution and transmission rates and the FirstEnergy companies will not seek, at**
6 **any point in the future, to recover those costs from customers” (OCA St. 1, p. 34,**
7 **lines 9-11). Do you agree?**

8 A. All Transaction-related costs, including costs incurred to discuss, gather information and
9 investigate the feasibility of creating MAIT, and continuing through the completion of
10 the Transaction, will be incurred by FirstEnergy Transmission, LLC (“FET”) and charged
11 to FERC Account 426.5 – Other Deductions on FET’s books of account. As I explained
12 in my Direct Testimony (Joint Applicants’ St. 1, p. 15, lines 11-14), the Joint Applicants
13 commit to exclude all Transaction-related costs from MAIT’s transmission rates and, in
14 fact, have made that commitment in their application to the FERC for approval of the
15 Transaction. No Transaction-related costs will be recorded by, or allocated to, the
16 Companies, which also will not seek to recover any costs to achieve the Transaction in
17 distribution rates.

18 **III. RESPONSE TO MS. GUMBY**

19 **Q. Ms. Gumby proposes that the Commission approve the Transaction, but expresses**
20 **concern that the Transaction may cause an unjustified increase in the costs charged**
21 **to the distribution function of the Companies for service performed by FirstEnergy**

1 **Service Company (“FESC”) (I&E St. 1, p. 7, lines 3-5). Please address Ms. Gumby’s**
2 **concern.**

3 A. Ms. Gumby’s concern is not warranted. The manner in which FESC directly assigns and,
4 as to costs not directly assigned, allocates costs to the companies it serves assures that
5 FESC costs will be properly charged to MAIT and the Companies. FESC establishes and
6 maintains a “cost collector” for each type of capital and maintenance project, including
7 specific transmission or specific distribution projects. This “cost collector” captures and
8 tracks all costs for a specific project and records the costs to the company for which the
9 specific work was performed. Costs that are not directly assigned to cost collectors, such
10 as, for example, corporate support costs, are allocated in compliance with FirstEnergy’s
11 detailed Cost Allocation Manual, which is incorporated in the FirstEnergy Service
12 Agreement (Exhibit KJT-5). Under the FirstEnergy Service Agreement, FESC allocates
13 costs to the operating companies it serves using one (or various combinations, as
14 applicable) of eighteen cost allocation factors. The FirstEnergy Service Agreement has
15 been filed with, and approved by, this Commission. FirstEnergy’s process for assigning
16 and allocating costs as discussed above will be consistently applied post-Transaction and
17 will ensure that the appropriate amount of costs are recorded on the books of each of the
18 FirstEnergy operating companies.

19 **IV. CONCLUSION**

20 **Q. Does this conclude your rebuttal testimony at this time?**

21 A. Yes, it does.