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INDIANA UTILITY
REGULATORY COMMISSION

INDIANAPOLIS POWER & LIGHT COMPANY

IURC CAUSE NO. 45029

VERIFIED REBUTTAL TESTIMONY
OF

ALAN D. FELSENTHAL

SPONSORING IPL WITNESS ADF ATTACHMENTS 1R THROUGH 3R

VERIFIED REBUTTAL TESTIMONY OF ALAN D. FELSENTHAL
ON BEHALF OF
INDIANAPOLIS POWER & LIGHT COMPANY

Q1. Please state your name, address, occupation and employer.

A1. My name is Alan D. Felsenthal. My business address is One North Wacker Drive, Chicago, Illinois 60606. I am a Managing Director at PricewaterhouseCoopers LLP ("PwC").

Q2. Please describe your duties and responsibilities at PwC.

A2. I lead the Firm's regulatory support practice. Throughout my career, my focus has been on the regulated industry sector, primarily electric, gas, telecommunication and water utilities. I have focused on utility accounting, income tax and regulatory issues, primarily as a result of auditing regulated enterprises. The unique accounting standards applicable to regulated entities embodied in Accounting Standards Codification ("ASC") 980, Regulated Operations (formerly, Statement of Financial Accounting Standards ("SFAS") 71, FAS 90, FAS 92, FAS 101 and various Emerging Issues Task Force ("EITF") issues, all need to be understood so that auditors can determine whether a company's financial statements are fairly presented in accordance with generally accepted accounting principles. I have witnessed the issuance of these standards and have consulted with utilities as to how they should be applied. At both Arthur Andersen and PwC, I worked with the technical industry, accounting and auditing leadership to communicate and consult on utility accounting and audit matters. My curriculum vitae is attached as <u>IPL Witness ADF Attachment 1R</u>.

Q3. Please describe your educational background and business experience.

A3. I was graduated from the University of Illinois in 1971 and began my career at Arthur Andersen & Co ("Arthur Andersen"), where I was an auditor, and focused on audits of financial statements of regulated entities. In 2002, I joined PricewaterhouseCoopers and became a Managing Director in their Utilities Group and continued performing audits for regulated entities. I was hired by Huron Consulting Group ("Huron") in 2008 and returned to PwC in November of 2010. At both Arthur Andersen and PwC, I supervised audits of financial statements on which the firms issued audit opinions that were filed with the SEC, the Federal Communications Commission, the Federal Energy Regulatory Commission ("FERC") and various state commissions. At Arthur Andersen, PwC and Huron, I consulted on a significant number of utility rate cases and helped develop testimony for myself and others on a variety of issues, including construction work in progress in rate base, projected test years, lead-lag studies, cost allocation, several accounting issues (e.g., pension accounting, regulatory accounting, income tax accounting, cost of removal) and compliance with the income tax normalization requirements.

Q4. Have you previously testified before the Indiana Utility Regulatory Commission ("Commission")?

A4. Yes. I have testified or filed testimony before this Commission in three dockets. The first was in connection with Northern Indiana Public Service Company's rate case filing in Cause No. 43526 on the ratemaking treatment of cost of removal. I then testified in Indianapolis Power & Light Company's ("IPL" or "Company") rate case filing in Cause No. 44576, in which I testified on ratemaking treatment of the Company's net prepaid pension asset. I also provided rebuttal testimony in Northern Indiana Public Service Company's rate case filing in Cause No. 44688, on this subject.

Q5. Have you testified in other regulatory jurisdictions?

A5. Yes. I have testified before the Arizona Corporation Commission, the Florida Public Service Commission, the Illinois Commerce Commission, the Public Utility Commission of Ohio, the Public Utility Commission of Texas and the Washington Utilities and Transportation Commission.

Q6. Have you provided training on the application of Generally Accepted Accounting Principles ("GAAP") to regulated enterprises?

A6. Yes. At Arthur Andersen, Huron and PwC, I developed and taught utility accounting seminars focusing on the unique aspects of the regulatory process and the resulting accounting consequences of the application of GAAP. I have presented seminars, as well as delivered training on an in-house basis. Seminar participants have included utility company and regulatory commission staff accountants, utility rate departments and internal auditors, tax accountants and others. I have also conducted these seminars for the FERC and several state commissions, and I have presented at various Edison Electric Institute and American Gas Association ratemaking and accounting seminars.

Q7. As part of your work for the Company in this Cause, have you read the direct testimony of Edward J. Kunz, Margaret Stull and Michael Gorman?

A7. Yes, I have.

Q8. Please provide a summary of your rebuttal testimony.

A8. In its direct filing IPL included a net $158.2 million prepaid pension asset in the capital structure thereby permitting investors a return on this asset. The net prepaid pension asset consists of a prepaid pension asset of $170.6 million offset by an Other Post Employment Benefit ("OPEB") liability of $12.2 million. Margaret A. Stull submitted pre-filed testimony on behalf of the Indiana Office of Utility Consumer Counselor ("OUCC") rejecting this treatment and, instead, proposed a calculation to recover (but not earn a return on) the Employee Retirement Income Security Act of 1974 ("ERISA") minimum portion of the prepaid pension asset. Michael Gorman, on behalf of the IPL Industrial Group, also rejected the Company's treatment and proposes as an alternative that the "discretionary portion" of the prepaid pension asset potentially be included in rate base[1]. My rebuttal testimony will discuss (1) the GAAP accounting requirements for pension and OPEB costs which is different than the ERISA requirements for contributions to the pension trust. The net prepaid pension asset arises from cumulative contributions to the pension trust in excess of the cumulative pension and OPEB expense and, thus, is funded by investor capital; (2) why making a distinction between the "ERISA minimum" and "discretionary portion" of the prepaid pension asset is flawed and unnecessary as the source of the entire prepaid pension asset is funded by investors - thus requiring a return; (3) why the prepaid pension asset provides both quantifiable and other benefits to IPL's customers; (4) why the prepaid pension asset is essentially the mirror image of the Company's OPEB liability ($12.2 million) which in the ratemaking process has been treated in a manner which reduces return and revenue requirements, a treatment that the IURC has addressed and approved, and which neither Ms. Stull nor Mr. Gorman has challenged and why fairness and equity requires consistent treatment of the pension asset and OPEB liability.

Q9. What are the purposes of your rebuttal testimony in this proceeding?

[1] In his testimony, Mr. Gorman proposes rate base treatment up to the discretionary portion of the prepaid pension asset, net of the OPEB liability, whereas the Company proposes to include the entire investor supplied prepaid pension asset, net of the OPEB liability as capital structure components. In his schedules, however, Mr. Gorman's proposed revenue requirement does not include the net prepaid pension asset in rate base, nor does it include the OPEB liability in the capital structure (See Attachment MPG-3 and WP MPG-15).

A9. The purposes of my rebuttal testimony are to: discuss the accounting and regulatory treatment of the Company's prepaid pension asset and OPEB liability; discuss the ERISA requirements for contributions to the pension trust; demonstrate why the source of the entire prepaid pension asset is investor capital thus requiring a return; and, explain why the proposals by OUCC's witness Margaret Stull and the IPL Industrial Group's witness Michael Gorman on this matter which result in investors not receiving an adequate return on their capital comprising the prepaid pension asset be rejected.

Neither Ms. Stull nor Mr. Gorman objects to the Company's including pension expense as a recoverable cost, nor do they dispute the fact that pension expense is reduced as a result of IPL's prepaid pension asset. Yet, both are, in effect, requesting that the Company's actions to reduce cost of service (through a reduced pension expense) be permitted without customers paying rates that compensate investors for the cash they advanced to effectuate this cost of service reduction.

In addition to this quantifiable benefit that customers receive as a result of the investor-funded prepaid pension asset, I will show why such contributions to the pension trust which result in IPL's pension plan being funded, on an ERISA basis at around 100%, is a prudent decision benefitting IPL and its customers and why it is appropriate for investors to earn a return on their investment as the Company has proposed.

Pension Basics

Q10. Mr. Felsenthal, with respect to the prepaid pension asset Ms. Stull at pages 3 through 8 discusses U.S. GAAP, ASC 715, OPEB accounting, and ERISA. Before you get into the detailed accounting and funding rules for pensions, can you explain the prepaid pension issue at a high level?

A10. Yes. Pensions are promised/contracted payments to retirees under a defined benefit plan. The prepaid pension asset issue involves different rules for expensing pensions (for GAAP and revenue requirement purposes) versus the contributions required under ERISA to fund pension payments through operation of a pension trust. The prepaid pension asset is the cumulative difference between 1) amounts expensed for GAAP (and recovery as a component of test year expenses) and 2) contributions to the pension trust.

Pension Expensing

For accounting purposes under GAAP, an employee's pension is "accrued" (recognized as an expense) over the employee's service life. In that manner, each year is charged a portion of the pension that is "earned" by the employee providing service for that year. Estimates of the amount that the employee will eventually receive as a pension payment are developed by actuaries considering how long the employee will live after retirement, the promised benefits, etc. The expense is recognized each year of the employee's service life, with a corresponding increase to the pension liability. Once the employee retires, his/her expense accrual stops and pension payments begin. Over time, pension expense plus investment returns will equal the pension benefits paid to retirees (less expenses of the plan, if any).

Pension Funding

Companies must be able to fund the future retiree payments. It is a prudent business decision to put away amounts prior to the time such retiree payments are to occur and most companies have established a pension trust to accomplish this. This is the "funding" part of the equation. Contributions to the pension trust are based on ERISA and deductibility of such amounts based on the Internal Revenue Service ("IRS") rules. The IRS sets minimum and maximum funding requirements and imposes penalties and other limitations for less well-funded pension plans. The Pension Benefit Guarantee Corporation requires participant notices for missed contributions and additional reporting for less well-funded plans.

Assets in the pension trust cannot be removed for any purpose other than retiree pension payments. Amounts in the fund can be invested in securities and other vehicles to earn a return—thus reducing the amount that eventually needs to be contributed to the fund in order to have enough cash accumulated to fund the retiree benefits once they begin. If, for example, $50,000 was needed to fund pension benefits for an employee that will retire in 10 years (the payments beginning in year 11), it is possible to contribute less than $50,000 to the pension trust as long as the earnings on the amounts invested produce the required $50,000 at the retirement date. Further, the sooner that contribution is made, the longer that contribution is available to earn within the plan, again requiring less that would be needed if the contribution is delayed. The sooner and greater the contribution, the less the company will be required to contribute over time to be able to make the pension payments. Further, and importantly from a ratemaking standpoint, pension trust earnings reduce ongoing annual pension expense. As pension expense is included as a recoverable cost in the ratemaking process, these trust earnings inure to the benefit of customers.

Different Calculations for Different Purposes

The calculation of pension expense and the determination of contributions to the pension trust are meant to accomplish different purposes. The pension expense calculation recognizes that a portion of an employee's pension benefits accrue (are earned) over each period of that employee's career.

The pension contribution is a separate calculation to fund the eventual pension benefits. The prepaid pension asset is the excess of the cumulative amounts contributed to the pension trust versus the cumulative amount of pension expense. Earnings on the trust assets as well as the impact of discounting liabilities and plan changes are also factors in determining the expense. Such accounting recognizes that less funding will be required when the pension trust has assets that can earn a return than if no such asset existed. Again, the greater the pension asset, the less the expense.

Summary of Pension Accounting/Ratemaking vs. Pension Contributions

In a regulated entity, revenue requirements often include recovery of pension expense as determined in accordance with GAAP, while contributions to the pension trust are determined to comply with ERISA with a different objective. The prepaid pension asset represents the cumulative amount of contributions to the pension trust in excess of the cumulative pension expense. Because the prepaid pension asset represents contributions *in excess* of the expense included in revenue requirements, investor capital is required to fund the entire net prepaid pension asset balance and such investor capital is entitled to a return.

Earnings on pension trust assets reduce pension expense, benefiting customers. In addition to the customer benefit of reduced annual and cumulative pension expense recognized for financial and ratemaking purposes, customers also benefit from the company's ability to attract and retain employees knowing their pension is adequately funded. Further, companies with a well-funded pension plan are viewed as having less risk to the investment community which, all else being equal, should reduce the required return.

OPEB

In addition to pensions, many employers provide other retiree benefits such as for medical costs and life insurance. The accounting rules for OPEB's are similar to those of pensions. However, the contributions for OPEB's are quite different than for pensions in that there are no specific requirements to pre-fund these obligations. Thus, no prepaid asset exists for OPEBs. Instead, there is an excess of cumulative OPEB expense compared to required contributions (close to zero), producing an OPEB liability. Because the OPEB expense is included in revenue requirements on an accrual basis, it is considered a customer supplied source of cost free capital (where there is no VEBA as is the case here with respect to IPL). In other words, it is viewed as an OPEB regulatory liability because rates paid by customers are the source of the funds for this ultimate expense. The OPEB accrual is treated as zero cost capital in the capital structure, the economic equivalent of reducing rate base.

The pension asset and OPEB liability are, therefore, mirror images of each other and should be reflected in ratemaking in a consistent manner, meaning the prepaid pension asset is ultimately funded entirely by investors requiring a return, while the ultimate source of the OPEB liability is customers, reducing the return.

Q11. Are there any material differences between you and Ms. Stull on the foundation matters you explained above?

A11. I don't believe so. While she takes issue with the term "prepaid pension asset" as not being a defined term in ASC 715 or ERISA, she uses that term in her testimony to effectively mean the "excess of contributions to the pension trust over recorded pension expense" which is the meaning I use as well. The primary differences relate to 1) the source of the prepaid pension asset, which I explain must be investors and 2) whether the investors who advanced the capital to fund the prepaid pension asset are entitled to a return on their investment.

IPL's Current Filing

Q12. Does Ms. Stull object to the Company's treatment of the OPEB liability, *i.e.* including the balance as zero cost capital in the capital structure?

A12. No. Even though the OPEB liability is essentially the mirror image of the prepaid pension asset, Ms. Stull's position is to reject the inclusion of the prepaid pension asset as a negative component in the capital structure (increasing return and revenue requirements), while at the same time she has reduced return and revenue requirements for the OPEB liability. Her position on the prepaid pension asset and OPEB liability is internally inconsistent. IPL has appropriately applied consistent treatment to these two items.

Q13. Ms. Stull states (pp. 18-19) that "IPL has no OPEB fund and therefore, there is no return on plan assets to adjust as I did with my pension expense adjustment." She proposes that the OPEB liability remain in the capital structure as a zero cost source of capital. Is this reasonable?

A13. No. The OPEB liability is the mirror image of the prepaid pension asset and consistency requires similar treatment. Netting the prepaid pension asset with the OPEB liability accomplishes this consistency. As I stated, her position on the OPEB liability is inconsistent with her position on the prepaid pension asset and inconsistent with the treatment approved in IPL's past rate case, which is to net the two.

Q14. IG witness Gorman (p. 33) contends that IPL has not demonstrated that the prepaid pension asset was funded by investor capital. Do you agree?

A14. No. Under GAAP, a prepaid pension asset results when contributions to the pension trust are in excess of the amounts recorded as pension expense under GAAP. If contributions to the pension trust equaled GAAP pension expense, there would be no prepaid pension asset. If contributions are less than GAAP pension expense, a pension liability results. Contributions in excess of GAAP expense are common and typically arise when contributions required under the federal ERISA rules (whether the ERISA minimum or greater to meet certain thresholds) are higher than GAAP expense. Such contributions and GAAP pension expense are calculated in completely different ways and will rarely, if ever, equal. For ratemaking purposes in most jurisdictions, including Indiana, only GAAP pension expense is generally included in the determination of the revenue requirement. As a result, in order to fund the required contributions in excess of GAAP expense, investor-supplied funds must be used.

As noted previously, a prepaid pension asset arises when contributions are in excess of GAAP expense; therefore, the prepaid pension asset is entirely funded by investors and investors alone. As a result, investors require a return on the prepaid pension asset as it represents funds provided by investors which are prudently invested in the delivery of utility service. In his direct testimony, Mr. Kunz explains both the Company's contribution strategy and the benefits such strategy provides.

Q15. Without going into the detailed calculations, can you briefly clarify the difference between the objectives of the GAAP determination of pension expense and the objectives of the ERISA requirements?

A15. Yes. US GAAP accounting is included in ASC 715 and is described in the direct testimony of Mr. Kunz. The components of the calculation include service costs, interest costs, earnings on fund assets and certain amortizations. The GAAP objective is to attribute pension costs earned by eligible employees to each fiscal year they are employed in a smooth, systematic, and rational manner.

In contrast, the purpose of ERISA minimum funding is to require contributions by the employer in order to maintain a well-funded plan, which in turn provides benefit security for employees. While ERISA does not require a plan to fund 100% of pension liabilities each year, that is the target for minimum funding. Each year the minimum contribution is the sum of normal cost (the cost of benefits accruing during the year) plus a 7-year amortization of any shortfall (i.e., the difference between plan assets and 100% of plan liabilities). Absent any actuarial gains or losses, the result of making minimum required contributions would be a plan that is 100% funded after 7 years.

These two concepts have different objectives. But even if a company made only the ERISA minimum required contributions to their plan, there can be a prepaid pension asset generated because the US GAAP expense is calculated independently of required contributions. Ms. Stull (p. 11) describes this contrast as a "disconnect" between GAAP accounting and required contributions.

Q16. In the long-run, will the cumulative pension expense recorded under GAAP equal the contributions to the pension trust plus investment returns on such trust contributions?

A16. Yes. During the entire lifetime of the pension plan, total cumulative employer contributions plus investment earnings on such trust assets must necessarily equal total cumulative GAAP expense (*i.e.*, in the long run, once the last participant has been paid their final benefit, the prepaid pension asset or liability will be $0).

Q17. What are the implications of the above question and answer?

A17. Because, in the long-run, contributions to the pension trust plus investment earnings on trust assets will equal the long-run pension expense, it follows that by making pension trust contributions earlier in the lifetime of the plan, total pension expense will be reduced. Mr. Gorman (p. 35) states that he does not dispute that increased pension contributions can reduce annual pension expense which can be a benefit to customers. He identifies the issues as "Who paid for the benefit"? Here it is clear that this "benefit" was not produced by including FAS 87/ASC 715 based pension expense in the ratemaking process as further explained below.

Response to Mr. Gorman

Q18. Mr. Gorman's alternative position (p. 38) is essentially the same as the IURC decision in IPL's last Cause, that is, permitting a return on the portion of the prepaid pension asset as a result of IPL investors making additional discretionary contributions to the pension trust. His position assumes the portion of the prepaid pension asset representing ERISA minimum contributions results from contributions from ratepayers. Do you agree?

A18. No. The entire prepaid pension asset was funded by investors. To separate the prepaid pension asset into "ERISA minimum" and "discretionary" components and suggest that one was paid by customers and one was paid by investors is a flawed position.

Minimum funding contributions under ERISA and pension expense under GAAP (including the amount of any prepaid pension asset) are separate and distinct calculations. The purpose of ERISA minimum funding is to require contributions by the employer in order to maintain a well-funded plan. The required contribution amount for any given year is a function of the plan's relative funded status that year, which is dependent on the level of contributions (required or discretionary) made in prior years.

In contrast, the purpose of GAAP accounting is to try and attribute pension costs to each fiscal year in a smooth, systematic, and rational manner. The GAAP calculation of pension expense does not include ERISA minimum funding. Even if a company made only the ERISA minimum required contributions to their plan, there can be a prepaid pension asset generated because the GAAP pension expense is calculated independently of required contributions.

In the ratemaking process customers pay for service, not individual expenses. The test period is used to determine the revenue requirement. One element of that cost is pension expense determined under GAAP. The prepaid pension asset, by definition, is the amount (at any given point in time) by which total cumulative contributions have exceeded total cumulative GAAP pension expense, which is in no way a function of ERISA minimum funding.

The source of the entire prepaid pension asset is investor capital requiring a return.

Q19. Why do you say that the entire prepaid pension asset is funded by investors?

A19. The short answer is "it had to have been." While Mr. Gorman rejected Mr. Kunz's response to this question, it is correct. By definition, the prepaid pension asset represents the excess of cumulative contributions to the pension trust over the cumulative recorded pension expense. In previous rate cases, the pension expense amount has been included in IPL's rate case filings and customers could not have paid rates calculated to recover ***more*** than this pension expense amount. Thus, the entire amount of contributions to the pension trust must have come from another source. That source is investors.

Q20. Can it be demonstrated definitively that customer rates were not the source of any portion of IPL's prepaid pension asset?

A20. Yes. The point that customers could not have paid rates to fund any of the prepaid pension asset can also be shown by looking back at the Company's rate case filings from the time FAS 87 was effective. I can calculate a high level "proof" that customer rates could not have funded any of the prepaid pension asset.

Q21. How can you calculate this?

A21. Information to perform this calculation includes GAAP pension expense, the pension expense included in revenue requirements as determined in rate case filings and contributions to the pension trust. Unfortunately, IPL does not have all this information going back before 2000, but they do have the GAAP pension expense going back. Also, IPL has filed only two rate cases since 1995, one in 1995 and the other in 2014. The 1995 rate case was settled, with rates effective in 1996 and the 2014 rate case was fully litigated, with new rates effective in 2016. Even though the settlement in the 1995 rate case was a "black box," surely the Commission could not and would not have approved a settlement providing rate recovery of *more* than actual pension expense in 1995. It is therefore reasonable to conclude that this 1995 actual level of pension expense was reflected in rates in 2000 up until the next rate case filing in 2014, where an updated GAAP pension expense was presented.

With the foregoing reasonable assumptions, an assumed pension expense recovered in rates from 1995 to 2017 can be calculated, the 2000 through 2015 recovery of the GAAP pension expense in the first filing and the 2016 through 2017 recovery of GAAP pension expense resulting from the second filing. That cumulative pension expense recovery is approximately $220 million less than the recorded GAAP expense for the respective years 2000 through 2017. As the prepaid pension asset in this Cause is based on the excess of contributions to the pension trust in excess of GAAP pension expense and

GAAP pension expense is significantly above the assumed pension expense recovered in rates, it is apparent that the source of the prepaid pension asset must have been investor's in its entirety.

Q22. Do you have an attachment which provides this calculation?

A22. Yes. <u>IPL Witness ADF Attachment 2R</u> shows this calculation, which demonstrates that customer rates cannot be the source of funding for any of IPL's prepaid pension asset.

Q23. Mr. Gorman (p. 33) says the Order in Cause No. 44576 used the ERISA minimum funding as the "representative amount of the customer funded portion of the prepaid pension asset." Are you disagreeing with this determination?

A23. Yes. The distinction between the ERISA minimum portion and the discretionary portion of the prepaid pension asset was made based on my rebuttal testimony in response to Ms. Stull's position in the last rate case that customers should not be required to pay rates reflecting a return on discretionary contributions to the fund. In response to this claim, I provided rebuttal testimony showing that even if the funding had been made at the ERISA minimum level, a prepaid pension asset would still exist. The calculation of the pension expense amount is not based on ERISA funding, it is based on GAAP, which is a separate calculation that does not consider ERISA. Because ratemaking has recognized pension expenses based on GAAP, the "source" of the prepaid pension asset could not be the pension expense component of the revenue requirement used to establish customer rates.

Q24. Are you saying that the GAAP calculation of pension expense included in the test period does not consider the minimum ERISA contribution level?

A24. Exactly. I think it is possible that there was a misunderstanding in IPL's prior Cause that the calculated pension expense was based or partially based on ERISA minimum funding levels. That is not the case. Pension expense is based on GAAP considering service costs, interest costs, return on pension assets and amortizations. Contributions are based on separate determinations to comply with ERISA and IRS requirements. Any amounts, regardless if due to ERISA rules or the discretion of the Company, contributed to the pension trust above GAAP pension expense, included in the revenue requirement, are funded by investors and should not receive different regulatory treatment.

Q25. Ms. Stull proposes to not directly allow a return on any portion of IPL's prepaid pension asset, whether including the prepaid pension asset in rate base or as a component of the capital structure. Is her position contrary to previous decisions approved by the IURC?

A25. Yes. The IURC has consistently and appropriately allowed a return on the prepaid pension asset, either through including the prepaid pension asset in rate base or as a component of the capital structure. Ms. Stull lists those outcomes in her rebuttal testimony on Page 9. (Cause Nos. 44075 and 44967 for Indiana-Michigan, Cause 44450 for Indiana-American Water Company, Cause Nos. 44576 for IPL and Cause Nos. 44688 and 44988 for Northern Indiana Public Service Company). Even in IPL's Cause No. 44576, a return on the prepaid pension asset was permitted, albeit only on a portion of the prepaid pension asset based on a mistaken belief as to the source of the prepaid pension asset.

Whether the prepaid pension asset is included in rate base or included as a component of capital structure produces results that are effectively economic equivalents. Either approach permits a return to the investor.[2] The IURC has permitted rate base inclusion of the prepaid pension asset in Orders issued for Indiana and Michigan Electric (Cause 44075) and in IPL's last rate case (Cause 44576). In several other cases the prepaid pension asset has been included as a component of the capital structure. While those cases were settled, the IURC approved the settlements.

Q26. Ms. Stull (p. 14) contends that it is "unreasonable to burden ratepayers with higher rates to provide a ratemaking benefit to the utility for unnecessary contributions." Please respond.

A26. The prepaid pension asset provides a benefit to customers by reducing the pension expense as there is a "return on pension assets" component in the GAAP pension expense calculation which can be estimated by multiplying the prepaid pension asset by the expected return on pension assets. This was explained in the Company's response to IG DR 2-10, a copy of which is included with my testimony as <u>IPL Witness ADF Attachment 3R</u>.

Q27. Please explain what is shown by the analysis set forth in <u>IPL Witness ADF Attachment 3R.</u>

A27. This analysis shows the benefit to customers by showing that the reduction in pension expense for the return on plan assets is greater than the increased return to investors that customers will be charged on the prepaid pension asset. The customers will receive a direct reduction in pension expense of approximately $12.4 million (prepaid pension asset of $170.6 million time the 6.75% expected return on plan assets and the $.9 reduction in PBGC premium). This customer benefit can be compared to the requested

[2] The OUCC has challenged the inclusion of the prepaid pension asset in rate base "under the strictures of I.C. § 8-1-2-6." Stull at 9-10. While I disagree with Ms. Stull's testimony on this issue, including the prepaid pension asset in the capital structure as zero cost capital avoids this legal concern as recognized by Ms. Stull at page 11.

rate of return by including the prepaid pension asset and the related ADIT impact in the capital structure, which increases the rate of return to 6.82% from 6.61%. Applied to the requested original cost rate base of $3,397 million with gross-up a revenue requirement increase of $9.4 million results. Therefore, a net customer benefit exists and it is only equitable for customers who are receiving the benefit of the reduced pension expense proved a return to the investors who are providing this benefit.

Response to Ms. Stull

Q28. Turning to the direct testimony of Ms. Stull, beginning on the bottom of Page 2, she begins a discussion on whether the term "prepaid pension asset" is, in fact, a defined term from an accounting or ratemaking perspective, although she acknowledges the meaning of such term as "excess pension contributions" or as "the difference between cumulative pension contributions and cumulative pension expense" throughout her testimony. Should the terminology matter?

A28. Terminology matters only to the extent that all parties have an understanding as to what is meant by the term in question. While the concept of a prepaid pension asset first existed under superseded accounting guidance, Accounting Standards Board Opinion No. 87, Employers' Accounting for Pensions ("FAS 87"), this item is currently referred to as "accumulated contributions in excess of net periodic benefit cost" which is a component of funded status under current authoritative guidance contained in Topic 715, Compensation-Retirement Benefits, of the Accounting Standards Codification ("ASC 715"). This name change did not remove the concept of the prepaid pension asset from GAAP. Under ASC 715, "accumulated contributions in excess of net period benefit costs" is one component of what makes up funded status and is what was formerly referred to in the accounting literature as the prepaid pension asset. The difference is simply one of word choice, not substance.

The Company records the GAAP pension components in its books and records and the same components exist to enable the determination of the prepaid pension asset considered and permitted by the IURC in previous rate cases.

And, while Ms. Stull cannot find that term mentioned in the Federal Energy Regulatory Commission's ("FERC") Uniform System of Accounts ("USOA"), it is clear that the FERC has used this term as recently as last year in connection with Delmarva Power & Light Company's inclusion of the prepaid pension asset in rate base (ER 09-1158-0000), using the meaning described above.

If it were necessary to only consider terms defined in GAAP or the FERC USOA, "cash working capital" or "lead-lag" studies would never be permitted.

Q29. Ms. Stull (Page 24) testifies that permitting a return on the prepaid pension asset "could result in ratepayers paying more than the actual cost of the plan." Is that really possible?

A29. No. Ultimately, the amount of pension cost recovery through rates, the GAAP pension expense, will equal the amount of pension benefits paid to retirees. Said another way, GAAP pension expense equals cash in the long run. Further, including a return on the prepaid pension asset is simply compensating investors for the use of their capital to fund the pension trust above the amount of GAAP pension expense. The use of this investor capital provides a benefit to customers through lower pension expense and other factors discussed in my testimony. Therefore, allowing a return on the prepaid pension asset simply allows customers to pay for the benefits they receive.

Q30. On Page 13 of her testimony, Ms. Stull says that the 'disconnect between contributions and pension expense will increase over time." And, the prepaid pension asset "could eventually become the largest asset in a utility's rate base." Do you agree?

A30. No. As a pension fund gets closer to being 100% funded, defined as projected benefit obligation net of plan assets equaling zero, the required ERISA contributions naturally decrease. As such, GAAP pension expense may exceed required ERISA contributions. In addition, a company making discretionary contributions in excess of ERISA required amounts would also not be expected to continue to do so in this scenario. When this time comes, GAAP pension expense will be greater than pension contributions and thus the prepaid pension asset will go down and may even become a liability that would be used to reduce the revenue requirement similar to the OPEB liability discussed previously. This fact further reinforces that the OPEB liability and prepaid pension asset are simply mirror images of each other and should receive similar treatment.

Q31. Ms. Stull states on page 14 of her testimony that "either proposal incents utilities to make potentially imprudent contributions to a pension plan rather than invest in utility infrastructure." Are IPL's contributions to the pension trust at 100% of that required by ERISA imprudent?

A31. No. And this is a significant point. IPL has an obligation to pay promised pension benefits to covered retirees. To assure that funds are available in the pension trust to make such payments, their goal is to make contributions to the pension trust to achieve ERISA funding at 100%. Not only does funding at this level increase the likelihood that funds will be available to pay the promised benefits, earnings on the prepaid pension asset reduces the ultimate pension expense.

Contributions at this level help reduce or eliminate PBGC variable rate premiums which are additional premiums owed to the PBGC at a current rate of approximately 4% of any unfunded obligations. This level of contributions positions the plan to be able to absorb adverse plan experience (negative asset return, interest rate decreases, etc.) without significant spikes in required contributions, helps the plan avoid benefit restrictions that may apply to underfunded plans and provides a greater guarantee of benefits to employees, and allows for more predictable, level annual contribution amounts. In the event of higher interest rates, contributions at lesser amounts may increase the required levels of contributions in the future as these low interest rates wear away. The prudence of this policy affects the entire prepaid pension asset, not just the contributions above the ERISA minimum. The inability of various state governments to pay pension obligations shows what could happen without such contributions.

In the IURC's decision in IPL's last rate case and decisions prior to and subsequent to that Cause, the Commission effectively agrees with this position. The IURC permitted IPL to include the discretionary portion of the prepaid pension asset in rate base (and to earn a return) concluding that funding the pension trust above the ERISA minimum was prudent. But in that cause, the IURC did not permit allowing inclusion of the ERISA minimum portion of the prepaid pension asset on the apparent mistaken belief that this portion was not funded by investors. Now knowing that the entire prepaid pension asset was funded by investors, the IURC should permit a return on such amount, consistent with the positions taken in the other cited causes.

Q32. On Pages 14-17 of her testimony, Ms. Stull proposes to allow recovery of (but not return on) of a portion contributions in excess of GAAP expense through an

adjustment to pension expense. Is this position consistent with prior OUCC positions on the prepaid pension asset issue?

A32. No. This is new. In prior cases, Ms. Stull took the position that the prepaid pension asset should not be included in rate base. However, in those settled cases, the OUCC did not object to including the prepaid pension asset in the capital structure as IPL has proposed in this case. For instance, in the Indiana American Water Company case, OUCC witness Heather Poole recommended including the prepaid pension asset in the capital structure. The relevant question and answer appears on page 8 of her prefiled testimony filed on May 12, 2014, in *Indiana-American* (Cause No. 44450) (emphasis added):

> Q. What is your recommendation regarding Petitioner's other employee benefit plans?
>
> A. Because Petitioner's prepaid pension asset should not be included in rate base, **the OUCC recommends Petitioner include the prepaid pension asset in the capital structure as a zero cost of capital**, similar to the OPEB liability.

In that same case, OUCC witness Ms. Stull calculated the revenue requirement by including the prepaid pension asset as a zero cost debit in the capital structure. On page 41 of Ms. Stull's testimony in *Indiana-American*, the following Question and Answer is presented (emphasis added):

> Q. Is the OUCC proposing any adjustments to Petitioner's projected November 30, 2014 capital structure?
>
> A. Yes. **Petitioner's prepaid pension asset should be included as a reduction to the zero cost source of capital.** OUCC Witness Heather Poole discusses the OUCC's proposal to include the prepaid pension asset in the capital structure rather than as a component of rate base, as proposed by Petitioner.

Q33. Are you aware of other instances where the OUCC supported inclusion of the prepaid pension asset as a component of the calculated return?

A33. Yes. The *Indiana-American* case was not the first time that an OUCC witness supported a return on the prepaid pension asset. In a NIPSCO rate case (Cause No. 41746), OUCC witness Michael Brosch agreed to permit the prepaid pension asset in rate base. On page 17 of his rebuttal testimony in that investigation he concluded (emphasis added):

> Q. HAS THE TESTIMONY OF MR. MCKNIGHT CONVINCED YOU THAT THE COMPANY'S RATE BASE INCLUSION OF THE PREPAID PENSION AMOUNT IS NOW REASONABLE?
>
> A. Yes. **Inclusion of the amounts NIPSCO elected to prepay into the pension fund appear to generate significant financial benefits in the test period in amounts sufficient to justify rate base inclusion of such investments**. This may not always be the case in the future and the inclusion of prepaid pensions will require analysis in future rates cases. However, at this time and under the circumstances of this proceeding, the OUCC revenue requirement has been revised to include the prepaid pension balance in the Company's rate base.

Q34. In those prior cases, did OUCC distinguish between the portion of the prepaid pension asset representing the ERISA minimum and the discretionary contribution?

A34. No. The entire prepaid pension asset was permitted. That distinction only arose in IPL's last rate case and ignores the fact that the source of the entire prepaid pension asset is contributions made by investors. Customers did not pay any amount above the GAAP pension expense.

Q35. Ms. Stull (pp. 10-11) suggests that the prepaid pension asset is not "working capital" or "used and useful" property. Do you agree with this characterization?

A35. No. Even though the Company is not proposing to include the prepaid pension asset in rate base in this Cause, they certainly could. The prepaid pension asset would qualify as "working capital" and be entitled to a return. As it applies to a regulated utility, working capital includes the average amount of capital in excess of that used to finance net utility plant, (and other separately identified rate base components) necessary to operate the utility business and including working capital in rate base is an appropriate method of compensating investors for the cost of capital which they have provided.

In addition to such items as materials and supplies inventory and fuel inventory (typical components of working capital), the rate base of Indiana utilities has included other investor supplied investment such as regulatory assets. E.g., *Re Southern Indiana Gas & Electric*, Cause No. 43839, p. 16 (IURC 4/27/2011) (including allowance inventory, stores expense, DSM Regulatory Asset and MISO Regulatory Asset as well as Fuel Stock and Materials and Supplies in the rate base).

Importantly, the IURC's Minimum Standard Filing Requirement Schedules provide for a utility to request rate base treatment of regulatory assets in addition to net plant and working capital (170 IAC 1-5-9(a)(2)).

The purpose of including non-plant assets in rate base is to permit a return to investors who have contributed the amounts funding the investment. That is why regulatory assets and the net prepaid pension asset have been included in various rate base determinations. Such amounts have been funded by investors to support utility operations. Shareholders are entitled to a return on their funding of the prepaid pension asset, whether in rate base or as a component of the capital structure as it is investors who have funded such balances.

Q36. Ms. Stull proposes (p. 13) to increase operating expense as an alternative to address the prepaid pension asset issue. Would such an adjustment resolve this matter?

A36. No. It is important to recognize she is proposing an entirely new calculation that produces a hypothetical pension expense and, at page 16, she appears to acknowledge that this hypothetical expense calculation would continue indefinitely into future cases. And I am not sure if her proposal is even workable from a GAAP accounting standpoint. Ms. Stull has calculated a hypothetical pension expense above the GAAP pension expense amount which she suggests should be added to IPL's operating expenses and revenue requirement. This amount in not recorded on IPL's books and records, nor is it the amount contributed to the pension trust. She appears to be proposing that rates reflect a portion of the decrease in pension expense resulting from the expected return on a portion of the prepaid pension asset.

It is a calculation based on fiction. So if revenue were increased to permit recovery of this fictitious cost, such revenues would need to be reduced with a regulatory liability recorded, negating the purpose of this amount. Further, the Company would be required to keep track of this pretend cost so that in future rate case filings, it would not be recovered again and to be able to increase or reduce the regulatory liability. Also, such an action would not address the amounts historically contributed to the pension trust which were supplied by investors, i.e. the amounts historically contributed in excess of GAAP pension expense. Even if operating expenses were increased, the fact would remain that the prepaid pension asset being requested in this case would have still been funded by investors who require a return on that investment and would continue to be required until amounts included in the revenue requirement exceed the cumulative pension expense.

Her position is both contrary to all IURC decisions addressing the prepaid pension asset as well as the OUCC positions in prior cases which correctly includes a return on the entire prepaid pension asset.

Q37. Ms. Stull expresses concerns about IPL's strategy of funding at 100% of the ERISA requirement. She states (p. 20):

> **However, there are also risks to this funding strategy. The market crashes in 2000, with the dot.com bust, and in 2008, during the Great Recession, had a sizeable, negative effect on pension plans. These types of events cannot be forecasted and losses will occur. If a pension fund is fully funded, these losses will be even greater. In the case of regulated utilities, it is the ratepayers who will be expected to pick up the tab to replace lost pension funds despite the fact that ratepayers have no say in the utility's pension funding goals.**

Can you comment?

A37. Yes. Ms. Stull states that there are risks to having a well-funded plan, but really only lists one – that a market crash would result in greater losses because there are more assets in the plan. While the nominal dollar amount of such an asset loss may be larger, the well-funded plan will still be better positioned than the non-well-funded plan after such a market event. Having a well-funded plan also allows employers to adjust their investment strategies to reduce risk in their portfolios such that they can be immunized (at least partially) to such market events. Most notably, it is typical that employers will shift their investment mix to less risky investments the more funded the plan.

In addition, the use of a prudent funding policy to maintain a well-funded plan allows employers to have more predictable and steady contribution levels. Plans that are not well-funded are not positioned to absorb adverse experience, and as a result minimum ERISA required contribution levels can fluctuate greatly from year to year.

However, to help avoid the negative consequences of a "market event", IPL has changed its pension trust investment guidelines so that the vast majority (over 90%) of the pension trust assets are invested in fixed income securities. That is the primary reason for the lowering of the "expected return on plan assets" to 5.45%.

Ms. Stull goes on to state (p. 20) that a better use of funds might be in the investment in utility infrastructure or maintenance costs. However, she does not acknowledge that the current funding strategy for the plan saved IPL $901,000 in 2017 alone (per Mr. Kunz direct testimony, p.13) on PBGC premium costs.

Q38. At page 17, Ms. Stull includes a table purporting to present the revenue requirement effects of the three proposals presented for the prepaid pension asset. Has she correctly calculated this?

A38. No. IPL has reduced its calculated return by including the Accumulated Deferred Income Tax ("ADIT") on the net prepaid pension asset as zero cost capital in the rate of return computation. To the extent that net prepaid pension asset is not permitted to earn a return, an adjustment to reduce this ADIT would be required. When the ADIT impacts are not included, the revenue requirement of permitting a return on the prepaid pension asset is overstated,

Q39. Have other jurisdictions included a return on the prepaid pension asset?

A39. Yes. In addition to the IURC, the FERC and the FCC and a number of state jurisdictions have permitted a return on the prepaid pension asset.

Q40. What are the potential consequences of not providing investors a return on their contributions comprising the prepaid pension asset which they have funded in its entirety?

A40. Under Ms. Stull's or Mr. Gorman's approach, shareholders are not fairly compensated for their investments which have been contributed to the pension trust and bear the cost (no return on any of their investment under Ms. Stull's approach or no return on the portion of their investment making up the ERISA minimum under Mr. Gorman's alternative proposal) while customers receive all of the benefit. This approach is unfair because it fails to recognize the cost incurred to achieve the benefit (reduction in pension expense) in the ratemaking process. This approach may also prevent a utility from making good decisions for the benefit of customers as, to the extent contributions to the pension trust are reduced (because investors will not receive a return on the funds contributing to the prepaid pension asset), pension expense will increase, unfunded pension liabilities will increase and employees will likely become more concerned about the ability of the Company to make promised pension payments.

Summary

Q41. Can you please summarize your rebuttal testimony?

A41. Yes. Funding pension benefits is a necessary and responsible action on the part of IPL in the provision of electric service. IPL's net prepaid pension asset is the result of cumulative contributions to the pension trust in excess of GAAP pension expense. In the ratemaking process, revenue requirements include recovery of GAAP pension expense; however, all contributions to the pension trust in excess of this amount, whether due to ERISA rules or discretionary contributions, are funded by investors. As such, and consistent with virtually all of the previous decisions approved by the IURC, the entire prepaid asset should be allowed to earn a return, which is the position taken by IPL in this proceeding.

Q42. Does this conclude your rebuttal testimony?

A42. Yes.

VERIFICATION

I, Alan D. Felsenthal, Managing Director at PricewaterhouseCoopers LLP, affirm under penalties of perjury that the foregoing representations are true and correct to the best of my knowledge, information and belief.

Alan D. Felsenthal

Dated: June 21, 2018

CURRICULUM VITAE

ALAN D. FELSENTHAL

EDUCATIONAL BACKGROUND

June, 1971	B.S. in Accounting University of Illinois Champaign, Illinois
May, 1972	Certified Public Accountant

EMPLOYMENT

2010-	Managing Director, Power and Utilities PricewaterhouseCoopers LLP
2008-2010	Managing Director-Utilities Industry Huron Consulting Group
2002-2007	Managing Director—Utilities Industry PricewaterhouseCoopers LLP
1985-2002	Principal in Utilities and Telecommunications Practice, Arthur Andersen LLP, Chicago
1976-1985	Manager in Utilities and Telecommunications Practice, Arthur Andersen LLP, Chicago
1971-1976	Staff and Senior Accountant, Arthur Andersen LLP, Utilities and Telecommunications Division, Chicago

TESTIMONY EXPERIENCE

Testified before the Illinois Commerce Commission on behalf of Town Gas Company of Illinois, 1985. Accounting witness covering cost of service issues.

Testified before the Illinois Commerce Commission on behalf of Town Gas Company of Illinois, 1986. Generic hearing regarding high gas costs.

Testified before the Florida Public Service Commission on behalf of Central Telephone Company of Florida (1991). Testimony addressed projected test year, a computer model we developed to simplify forecast procedures and propriety of including pension asset in rate base.

Submitted an expert report and testified in an appeal by Yellow Cab Company versus the City of Chicago, (2000). Topic dealt with the adequacy of taxicab lease rates. Yellow Cab was appealing the lease rates they were permitted to charge lessees. The model developed by the City of Chicago to set lease rates was based on traditional utility ratemaking principles. Was hired by the City of Chicago to review Yellow Cab's appeal compared to traditional ratemaking principles and submit a report. Yellow Cab appealed the decision and a hearing before a judge resulted.

Testified before the Arizona Corporation Commission on behalf of Tucson Electric Power Company, 2008. Rebuttal testimony addressed application of FAS 71 when a portion of the business was opened to competition and appropriate treatment of the FAS 143 cost of removal regulatory liability.

Testified before the Florida Public Service Commission on behalf of Tampa Electric Company and Peoples Gas, (2008). Direct testimony on income taxes, including the appropriate accumulated deferred income tax calculation when a projected test period is used.

Testified before the Washington Utilities and Transportation Commission on behalf of Avista Corporation, (2008).

Testified before the Illinois Commerce Commission on behalf of The Peoples Gas, Light and Coke Company/North Shore Gas Company (2009). Rebuttal and Surrebuttal testimony on the appropriate treatment of prepaid pension asset in rate base.

Testified before the Indiana Utility Regulatory Commission on behalf of Northern Indiana Public Service Company (2009). Rebuttal testimony on the appropriate treatment of cost of removal vis a vis FAS 143.

Submitted an expert report and a reply expert report to a Seattle-based arbitration panel in a dispute involving Grays Harbor Energy LLC vs. Energy Northwest, 2009. Subject involved the appropriate determination of fixed costs and cost of capital pursuant to a purchase and sale agreement.

Testified before the Public Utility Commission of Texas on behalf of Centerpoint Energy (2010). Direct and Rebuttal testimony on a number of income tax issues including consolidated income tax adjustments and FIN 48.

Testified before the Indiana Utility Regulatory Commission on behalf of Indianapolis Power & Light Company (2015). Rebuttal testimony on including prepaid pension asset in rate base.

Testified before the Public Utility Commission of Ohio on behalf of Dayton Power & Light Company (2015). Direct testimony on the results of a lead-lag study.

Submitted rebuttal testimony to the Indiana Utility Regulatory Commission on behalf of Northern Indiana Public Service Company (2016) on the appropriateness of including the prepaid pension asset in rate base.

Submitted an expert report to the Virginia State Corporation Commission regarding the allocation of Dominion Resources Inc. shared service costs to Virginia Electric Power Company (2016).

Submitted an expert report to the Oregon Public Service Commission regarding the capitalization of administrative and general overhead costs. (2017).

Testified before the Florida Public Service Commission on behalf of Tampa Electric Company and Peoples Gas on the subject of the appropriate treatment of excess Accumulated Deferred Income Taxes resulting from the Tax Cuts and Jobs Act (2018).

REGULATORY CONSULTING EXPERIENCE

Synopsis—Throughout the late 1970's, the 1980's, 1990's, 2000's and 2010's assisted Andersen and PwC partners in the preparation of regulatory testimony covering a variety of accounting issues. Much of this testimony involved income tax accounting issues related to flow-through versus normalization or investment tax credit. Also developed testimony on CWIP in rate base and working capital (lead-lag technique), appropriateness of allocation of service company costs to regulated entities and capital structure issues.

In 2015, assisted with the preparation of an Expert Report for EverSource Energy subsidiary Connecticut Light & Power which was submitted to the Connecticut regulator. The issue concerned reopening a rate order to address the treatment of accumulated deferred income taxes which was incorrectly decided in the rate order.

Provided assistance on rate case testimony for the following companies:

- Indianapolis Power & Light Company
- Dayton Power & Light Company
- Pacific Gas & Electric Company
- Iowa-Illinois Gas and Electric Company
- The Peoples Gas Light and Coke Company
- Northern Indiana Public Service Company
- PPL Montana (contract dispute)
- Southern Bell Telephone Company
- Indiana Bell Telephone Company

- Iowa Power Company
- El Paso Electric
- Ameritech Corporation
- Central Illinois Light Company
- Central Illinois Public Service Company
- Tampa Electric Company
- Public Service Company of New Mexico
- EverSource Energy
- Tampa Electric Company
- Central Telephone Company of Florida
- Central Telephone Company of Texas
- Central Telephone Company of Nevada
- Integrys Energy Group, Inc.

Provided regulatory consulting for the Panama Canal Company. Tariffs charged to transit the Panama Canal were based on a cost of service approach. Assisted the Panama Canal Company in determining test year costs. Tariffs were established based on these costs.

2012-1017. Led several projects to evaluate a rate case filing prior to filing validating the completeness, accuracy, consistency and support of the filing. As a result, adjustments and edits were made to the filing to increase the credibility of the utility's filing. Provided a similar role with respect to date request responses and rebuttal testimony.

FINANCIAL CONSULTING EXPERIENCE

Assisted two Chinese utility companies in registration filings to have their shares traded on the New York Stock Exchange. Huaneng Power International and Shandong Huaneng Power Company were the first two Chinese utilities to list on the NYSE. Process involved working with attorneys, company personnel and the Securities and Exchange Commission to file the equivalent of a Form S-1.

Assisted a number of companies in the preparation, review and filing of Registration Statements with the SEC to raise debt and equity capital.

Consulted with an electric transmission company on whether costs charged to generation companies based on specific costs are in accordance with the costs permitted by the Federal Energy Regulatory Commission.

Consulted with Ameritech Corporation on a number of projects involving cost allocations and compliance with the Federal Communications Commission separations rules.

Consulted with several entities in the preparation of a private letter ruling request to determine whether certain regulatory/ratemaking approaches would violate the Internal Revenue Service ("IRS") normalization rules. Provided the ratemaking aspect of the request when, combined with income tax consulting assistance formed the basis for a complete request, accepted by the IRS.

FINANCIAL AUDIT EXPERIENCE

- Allegheny Energy
- Ameritech Corporation
- Ameritech Cellular
- Ameritech New Media
- Louisville Gas and Electric Company
- Iowa-Illinois Gas and Electric Company
- Centel Corporation
- Constellation Energy
- Nicor, Inc.
- Peoples Energy
- Nisource
- Focal Communications
- Utilities, Inc.
- Chicago Skyway
- United Airlines

LECTURES AND SEMINARS

Speaker at Edison Electric Institute/American Gas Association Introductory, Intermediate and Advanced Accounting Seminar 1996-2017.

Speaker at SNL (Regulatory Research Associates) Utility Foundations Seminar 2013-2017

Speaker at Power Plan Associates annual conference (2012, 2010, 2008, 2006, 2004, 2002) on recent accounting, regulatory and SEC matters affecting utilities.

Developed and conducted Utilities Industry Basic Accounting and Ratemaking Seminar. This two-day seminar is conducted each year for Andersen, Huron and PwC personnel assigned to utility audits or projects. In addition, the seminar is periodically offered on an open-registration basis for utility company personnel as well as offered and conducted for specific utility companies at their training sites.

Developed and conducted Utility Income Taxes-Accounting and Ratemaking Issues. This two-and-a-half day seminar is conducted each year for Andersen, PwC and Huron personnel assigned to utility audits or income tax projects. In addition, the seminar is conducted annually on an open-registration basis for utility company personnel as well as offered and conducted for specific utility companies at their training sites.

Developed and conducted Rate Case Experience Seminar. This week long seminar is conducted each year on an open-registration basis for utility company personnel as well as offered and conducted for specific utility companies at their training sites.

Specific examples of special training conducts for utility companies/regulators are as follows:

- Nicor
- Entergy
- Peoples Energy
- Sempra Energy
- Centerpoint
- Nisource, Inc.
- Cleco Corporation

- Consolidated Edison
- Duke Energy
- National Grid
- Tucson Electric Power
- Portland General
- Pepco Holdings, Inc.
- Ameritech Corporation
- Louisville Gas and Electric
- American Water Works
- Tampa Electric
- Natural Gas Pipeline Company of America
- Transco Pipeline
- Federal Energy Regulatory Commission
- Oklahoma Commission
- Arkansas Commission
- Illinois Commerce Commission
- Sprint Corporation
- American Electric Power
- Consumers Power Company
- Arizona Public Service Company
- Qwest
- Northwest Pipeline
- SBC
- Alaska Regulatory Commission
- Xcel Energy
- Exelon Corporation
- PG&E Corporation

PROFESSIONAL ASSOCIATIONS

American Institute of Certified Public Accountants

Illinois CPA Society

	OUCC 25-3 Employer Contributions	OUCC 25-3 (NPPBC + Curtailment + Settlement - Adjustment + Cost) FAS Cost	OUCC 25-3 Total Prepaid Pension Asset (Liability)	OUCC 25-3 Employer Contributions	Maximum Pension Expense That Could Have Been in Rates	Total Prepaid Pension Asset (Liability)
1/1/2000			$ (28,750)			$ (28,750)
2000	$ 642	$ 59,238	$ (87,346)	$ 642	$ 5,693	$ (33,801)
2001	$ 11,639	$ 28,924	$ (104,631)	$ 11,639	$ 5,693	$ (27,855)
2002	$ 15,171	$ 6,766	$ (96,226)	$ 15,171	$ 5,693	$ (18,377)
2003	$ 96,074	$ 10,792	$ (10,944)	$ 96,074	$ 5,693	$ 72,004
2004	$ 6,148	$ 6,254	$ (11,050)	$ 6,148	$ 5,693	$ 72,459
2005	$ 17,604	$ 7,248	$ (694)	$ 17,604	$ 5,693	$ 84,370
2006	$ 37,202	$ 13,487	$ 23,021	$ 37,202	$ 5,693	$ 115,879
2007	$ -	$ 12,066	$ 10,955	$ -	$ 5,693	$ 110,186
2008	$ 56,660	$ 9,570	$ 58,045	$ 56,660	$ 5,693	$ 161,153
2009	$ 20,127	$ 34,293	$ 43,879	$ 20,127	$ 5,693	$ 175,587
2010	$ 28,701	$ 24,435	$ 48,145	$ 28,701	$ 5,693	$ 198,595
2011	$ 37,345	$ 24,546	$ 60,944	$ 37,345	$ 5,693	$ 230,247
2012	$ 48,312	$ 29,381	$ 79,875	$ 48,312	$ 5,693	$ 272,866
2013	$ 49,702	$ 26,922	$ 102,655	$ 49,702	$ 5,693	$ 316,875
2014	$ 54,109	$ 11,055	$ 145,709	$ 54,109	$ 5,693	$ 365,291
2015	$ 25,166	$ 12,096	$ 158,779	$ 25,166	$ 5,693	$ 384,764
2016	$ 15,950	$ 8,420	$ 166,309	$ 15,950	$ 12,096	$ 388,618
2017	$ 7,212	$ 5,558	$ 167,963	$ 7,212	$ 12,096	$ 383,734

Notes: There were no ERISA contributions for qualified plan from the inception of FAS 87 through 1996
Certain information needed rollforward Prepaid Pension Asset prior to 2000 is not available
Adjustment for Change in Plan Year is deduct of negative

Data Request IG DR 2 - 10

Concerning the Company's prepaid pension asset included in its proposed ratemaking capital structure, please provide the following:
a. All workpapers used to develop the prepaid pension asset as proposed for the test year.
b. An estimate of the annual contributions IPL has made to the pension trust its employees participate in since FAS 87 was implemented, the actual pension annual contribution and ERISA minimum contribution required each year since FAS 87 was implemented.
c. Please identify the amount of pension cost recovered from all ratepayers that contribute to the pension trust that IPL participates in, over the same period as referenced in b. above.
d. Please provide a study that shows the existence of the prepaid pension asset results in a net decrease in IPL's cost of service in this proceeding, compared to a scenario where the prepayment had not been made.

Objection:

IPL objects to the request on the grounds and to the extent it mischaracterizes the ratemaking process. IPL further objects to the request on the grounds and to the extent it solicits a compilation, calculation or analysis that IPL has not performed and objects to performing. Subject to and without waiver of the foregoing objections, IPL provides the following response.

Response:

a. The prepaid pension asset is reflected on IPL's books in accordance with Generally Accepted Accounting Principles. Please see IPL Witness EJK Attachment 2, IPL Workpaper 2 – IPL Witness EJK Attachment 2, and MFSR 1-5-8 (a) 15 and 16.

b. Please see attachment IG DR 2-10 Attachment 1.

c. Unable to determine as a result of one or more previous rate adjustment filings being settled.

d. If IPL had not made contributions to the pension fund beyond the pension cost that has been expensed by IPL, the pension fund would be lower in amount and the return on the pension fund trust would also be lower. If the pension fund amount is lower, then IPL's ongoing level of annual pension cost would be higher.

   The funds in the pension trust are invested and thus earn a return (for the trust and its beneficiaries, not IPL). The expected return on assets represents the long-term rate of return on plan assets. For IPL's pension fund, the "expected" return on the pension fund reflected in the actuarial analysis is 6.75%. The amount of the Prepaid Pension Asset is $170.6 million. This amount reflects IPL's excess employer contributions.

The prepaid pension asset directly reduces pension expense as calculated pursuant to SFAS 87 (also known as ASC 715), by approximately $11.5 million (the "direct SFAS 87 reduction") million per year. This is computed by multiplying the prepaid pension asset ($170.6 million) by the 6.75% long-term expected return assumed in the actuarial report which computes annual pension expense. This is a direct reduction to SFAS 87 pension expense. Because the ASC 715 cost is the cost recognized for ratemaking purposes, the prepaid pension asset has reduced the annual cost of providing service recognized in the revenue requirement. The reduction in annual pension cost will occur as long as the prepaid pension asset exists. Put another way, if the prepaid pension asset did not exist, pension expense that would be recognized in the revenue requirement would be $11.5 million higher than reflected in the Company's proposal. While the earnings on the pension trust reduce future pension contributions and net periodic pension expense to the benefit of IPL's customers, IPL's investors do not receive a benefit through the earnings accruing on the investments in the pension trust.

There are other tangible benefits from the prepaid pension asset in that it will reduce pension cost every year, it will protect employees by funding benefits they have already earned, and it will increase IPL's perceived financial strength by reducing unfunded obligations. These other benefits have not been quantified, but they nonetheless exist. Simply put, the prepaid pension asset reduces pension cost every year, protects employees by funding benefits they have already earned, and reduces IPL's unfunded obligations.

In addition to the savings to pension expense pursuant to SFAS 87, the prepaid pension asset reduces expenditures to the Pension Benefit Guaranty Corporation ("PBGC"). The PBGC was created by the Employee Retirement Income Security Act of 1974. It is a governmental agency that serves as the "insurer" for private-sector defined benefit pension plans. In the event a plan sponsor becomes insolvent, the PBGC steps in to continue plan payments to retirees and beneficiaries. The PBGC is not funded by general tax revenues; instead, it collects insurance premiums from employers that sponsor insured pension plans, earns money from investments, and receives funds from pension plans it takes over.

Without the prepaid pension asset, the pension plan would have a larger unfunded status, would be deemed riskier by the PBGC, and a larger premium would be owed to the PBGC for it to provide its guarantee. The total reduction in premium due to the prepaid pension asset is an estimated $0.9 million for 2017. This calculation is set forth on IPL Witness EJK Attachment 3.

Payments to the PBGC can either be paid out of the trust fund or paid directly by employers. If they are paid directly by employers, they are unquestionably charged to current expense. Even if they are paid out of the fund, the avoided payment would ultimately be paid by IPL and would be reflected as pension expense. Since this payment would relate to the current period, intergenerational equities would require that this increased PBGC payment, if required to be made, be reflected as a component of current pension expense for ratemaking purposes. Otherwise, customers in future periods would be paying higher rates to recover costs that are incurred currently. Effectively, this would be the result under SFAS 87 as well. The additional fee would be deferred and amortized to pension expenses over approximately ten years,[1] but an equivalent fee would be owed every year, thus producing an annual amortization equal to one-tenth of ten years' fee - or one year. Adding the avoided PBGC obligation to the direct SFAS 87 expense reduction produces a total pension expense savings of approximately $12.4 million per year.

To quantify the monetary benefit as the question requests, the annual expense savings may be compared to the impact on the revenue requirement of the gross prepaid pension asset of $170.6 million.[2] As shown on the first page of IG DR 2-10 Attachment 2, the impact to the revenue requirement from removing the gross prepaid pension asset and related deferred income taxes from the capital structure is $9.4 million. This shows that the existence of the prepaid pension asset in the revenue requirement results in a net decrease in IPL's cost of service in this proceeding,

This analysis was computed using IPL's proposed fair return on fair value rate base and also includes the utilization of an original cost ratemaking methodology using IPL's proposed common equity of 10.32%. To the extent the Commission finds a lower fair rate of return and/or cost of common equity than that proposed by IPL, the revenue requirement impact of including the prepaid pension asset in the capital structure would be reduced.

[1] The amortization period is the average remaining service lives of the employees expected to benefit.

[2] IPL Financial Exhibit IPL-CC, Schedule CC3-T shows the prepaid pension asset reflected in the capital structure is net of the offsetting OPEB liability.

Indianapolis Power & Light Company
Employer Contributions
Total & Minimum Funding Requirements

Contributions During Fiscal Year	Actual Contributions Made			Estimated Contributions Assuming Only Minimum Funding Requirements Met*		
	Qualified Pension Plan	SERP	Total	Qualified Pension Plan	SERP	Total
		(thousands)			(thousands)	
Prior to 1997	-	-	-	-	-	-
1997	-	559	559	-	559	559
1998	-	3,324	3,324	-	-	-
1999	-	3,324	3,324	-	-	-
2000	-	642	642	-	642	642
2001	4,000	7,639	11,639	4,000	7,639	11,639
2002	14,300	871	15,171	14,300	871	15,171
2003	96,000	74	96,074	96,000	74	96,074
2004	6,000	148	6,148	6,000	148	6,148
2005	17,525	79	17,604	17,525	79	17,604
2006	37,000	202	37,202	37,000	202	37,202
2007	-	-	-	-	-	-
2008	55,300	1,360	56,660	55,300	1,360	56,660
2009	20,000	127	20,127	13,500	127	13,627
2010	28,531	170	28,701	20,831	170	21,001
2011	37,345	-	37,345	32,945	-	32,945
2012	48,300	12	48,312	42,000	12	42,012
2013	49,600	102	49,702	38,900	102	39,002
2014	54,100	8	54,108	23,000	9	23,009
2015	25,000	166	25,166	19,400	166	19,566
2016	15,900	50	15,950	12,300	50	12,350
2017	7,100	112	7,212	5,200	112	5,312
2018	30,000	26	30,026	6,000	26	6,026
Total	**546,001**	**18,995**	**564,996**	**444,201**	**12,348**	**456,549**

* Assumes same contributions made to meet Gateway funding thresholds during 2001-2006 plan years and meet minimum requirement for 2007 plan year. Contributions from 2008 plan year on were designed to meet minimum requirements / avoid benefit restrictions.

** Before reflecting impact of curtailment / settlement accounting for Q1/Q2 2018.

***Assumes final SERP contribution for the 2016-2017 plan year is made before June 30, 2018

Indianapolis Power & Light Company
Cause No 45029

Impact on Revenue Increase Due to Removing Gross Prepaid Pension Asset
Based on Fair Value, using Company Return on Equity Proposal
(Thousands of Dollars)

Line No.			Per Supplemental Filing	Remove Gross Prepaid Pension Asset	Impact of Removal
1	Fair Value Rate Base		$4,040,037	$4,040,037	$0
2	x Rate of Return	McKenzie Attach 15-T	5.93%	5.76%	-0.17%
3	Allowable Operating Income		$239,574	$232,706	($6,868)
4	Less : Net Operating Income - Present Rates		$169,064	$169,064	$0
5	(Excess) / Deficiency in Net Operating Income		$70,510	$63,642	($6,868)
6	/ Revenue Conversion Factor		0.728928	0.728928	
7	(Excess) / Deficiency in Operating Revenue		$96,731	$87,309	($9,422)

NOTE: Removed $170,555 Gross Prepaid Pension Asset and $65,199 Accumulated Deferred Income Taxes from Capital Structure

Calculation of allowable operating income using original cost rate base:

8	Original Cost Rate Base		$3,397,648	$3,397,648	$0
9	x Cost of Capital	CC3-T	6.82%	6.61%	-0.21%
10	Allowable Operating Income Before Fair Value		$231,720	$224,585	($7,135)
11	Fair Value Increment		$7,854	$8,121	$267
12	Allowable Operating Income		$239,574	$232,706	($6,868)