Q3 2022 Earnings Call

Company Participants

- Darcy Reese, Vice President of Investor Relations
- Julie A. Sloat, Chief Financial Officer
- Nicholas K. Akins, Chief Executive Officer

Other Participants

- Durgesh Chopra, Analyst, Evercore ISI
- Jeremy Tonet, Analyst, JPMorgan
- Julien Dumoulin-Smith, Analyst, BofA Securities, Research Division
- Michael Lapides, Analyst, Goldman Sachs
- Ross Power, Analyst, UBS

Presentation

Operator

Welcome to the American Electric Power Third Quarter 2022 conference call. At this time, all participants are in a listen-only mode. Later we will conduct a question-and-answer session. (Operators Instructions) And as a reminder, your conference is being recorded. I would now like to turn the conference over to your host, Vice President of Investor Relations, Darcy Reese. Please go ahead.

Darcy Reese {BIO 20391516 <GO>}

Thank you, Louis. Good morning, everyone and welcome to the third quarter 2022 earnings call for American Electric Power. We appreciate your taking time today to join us. Our earnings release, presentation slides and related financial information are available on our website at aep.com.

Today, we will be making forward-looking statements during the call. There are many factors that may cause future results to differ materially from these statements. Please refer to our SEC filings for a discussion of these factors. Joining me this morning for opening remarks are Nick Akins, our Chair and Chief Executive Officer and Julie Sloat, our President and Chief Financial Officer. We will take your questions following their remarks.

I will now turn the call over to Nick.

Nicholas K. Akins {BIO 15090780 <GO>}

Okay. Thanks, Darcy. Welcome everyone to American Electric Power's third quarter 2022 earnings call. We continue to make significant progress on our commitments. We have leveraged our scale, our financial strength, portfolio management and transition to a pure-play regulated utility.

Over the past 10 years, we've had a great record of consistently exceeding our earnings projections and raising guidance, with this quarter being no exception. Today, I'll provide a brief recap of the key financial highlights for the quarter, followed by updates on our Kentucky sale process, our unregulated contracted renewables portfolio sale and the previously-announced strategic review of our retail business, all of which are part of our strategy to simplify and derisk our business profile. I will then spend time discussing our carbon emission reduction goals in addition to our continued emphasis on regulated renewables execution and generation fleet transformation.

I will conclude by providing insights into our other ongoing regulatory activities. All of this summarized information can be found on slide 6 and 7 of today's presentation with supporting details in the appendix. So, after the financials, we continue to build on our momentum delivering strong third quarter 2022 operating earnings of $1.62 per share or $831 million.

Today, we are reaffirming our 2022 narrowed full-your operating guidance range, as well as our newly introduced 2023 operating earnings guidance range, both of which we had announced at our recent Analyst Day. As a reminder, we are guiding to a 2022 range of $4.97 to $5.07, with an increase midpoint of $5.02 per share and our 2023 guidance range is $5.19 to $5.31 with a $5.29 per share at midpoint. Our long-term earnings growth rate guidance of 6% to 7% is underpinned by a robust $40 billion capital investment plan for 2023 to 2027, which includes $26 billion of wires and $9 billion in regulated renewables investments.

Moreover, our dividend growth is in line with our long-term growth rate and within our targeted payout ratio of 60% to 70%. We continue to derisk our platform and execute our strategy to ensure that we are best positioned for value creation in the face of global economic uncertainty and inflationary pressures. As part of this effort, we are continuing to work with states to drive reliability and resiliency in our service territory amidst customer bill considerations and other macroeconomic factors.

In order to lessen the impact on our capital investment plan, we have also diversified our mix of suppliers, which is to minimize customer and business supply-chain disruptions to date. Later in today's call, Julie will walk-through our third-quarter performance drivers and share our thoughts on the positive load outlook in our service territory as well as on our targeted 14% to 15% FFO-to-debt range.

So, now talking about some of the strategic reviews. True to our steadfast commitment to execution, we're in the final stretch to complete the sale of our Kentucky operations to Liberty. As we previously mentioned (inaudible) approval date to December 16th and we have therefore signed with Liberty to plan for a January 2023 closing date. This data is keyed off for this process and should give confidence to all stakeholders, including employees, customers, communities, and shareholders. It also enables our transition teams to adequately and efficiently plan for the closing.

While our sale time on this shifted over the past year, we are not revising our earnings guidance or any of our equity needs. We are pleased to reach this point and are confident in our ability to close the transaction shortly after the start of the New Year. Related to our unregulated contracted renewables portfolio, we launched the sale process for this 1,365 MW portfolio in late August 2022 with strong buyer interest from both financial and strategic investors. We recently accepted bids for phase 1 of the auction process and are proceeding into phase 2 due diligence with selected bidders.

We are on pace for a closing date in the second quarter of 2023. Selling the portfolio will allow AEP to shift focus and rotate capital towards regulated businesses, as we continue to transform our generation fleet and enhance transmission infrastructure. As we announced earlier this month on our Analyst Day, we are pursuing a strategic review of our retail business as we adjust to how our interest in the competitive markets has changed over time.

We'll keep you updated on our progress and expect to complete our review in the first half of 2023. We're always considering opportunities to enhance shareholder value and we'll continue to evaluate potential value-additive opportunities for our regulated businesses against the backdrop of our goal to further simplify and derisk the business. And regarding emission reduction goals as we mentioned on the Analyst Day, AEP remains firmly grounded in our principles of resiliency, reliability and affordability while recognizing the value of our diverse resource portfolio given today's world of energy-related volatility.

We are undertaking one of the largest clean-energy transformations in the country through our regulated renewables strategy and we announced our enhanced and accelerated carbon emission reduction goals at our Analyst Day in early October as I mentioned earlier. First, we have rebased our near-term emission reduction target of 80% by 2030, now pegged to a 2005 baseline instead of 2000. Second, we upgraded our near-term reduction target and as such, all Scope 1 emissions are now included in our carbon emission reduction goals.

Lastly, we accelerated our net 0 goal by 5 years from 2050 to 2045. We are confident in our path forward and our ability to hit key milestones in a steady and timely manner. Importantly, these goals are aligned and supported by our latest integrated resource plans in the various states. We will continue our planned retirement and disposition of select fossil fuel units while adding renewables to our generation portfolio.

Our 1.5 gigawatt North Central Wind portfolio, which became fully operational in March of this year, represents only the beginning of our clean-energy fleet transition. In addition, we have 17 gigawatts of potential generation additions across different resource types within our Vertically Integrated utilities over the next 10 years. Combined, this represents 18.5 gigawatts of new generation, which will significantly contribute to AEP's reduce carbon emissions profile and put us on a path to achieve our net 0 goal by 2045. As an update on October 19th related to SWEPCo is 999 MW renewables totaling $2.2 billion of investment, the Arkansas staff while supported of these resources, subject to conditions.

Commission orders are expected in 2023. As we looked at the long term, we are committed to building a reliable and resilient grid to efficiently deliver clean energy to our customers and we will continue to monitor new technologies that can help us close the gap to net 0 while maintaining the highly reliable and affordable delivery of energy that our customers expect. Moreover, newly passed provisions in the Inflation Reduction Act, which is foundational to our clean energy investment strategy should help bolster advancement of new carbon-free energy sources.

The bill includes tax credits for technologies like clean hydrogen projection and energy storage in addition to the technology neutral tax credits for our carbon-free resources and we will continue to evaluate these resources through our integrated resource plans. With regard to our ongoing regulatory activities, our regulated ROE as of September 30, 2022 is 9.3% and continues to improve as we work through regulatory cases and continue to make strides in reducing our authorized versus actual ROE gap.

In fact, as an update on SWEPCo on September 29th, we filed notice to move the 88 MW of Turk plant in the rates in Arkansas. The full filing will occur within the November-December timeframe and we will seek a rider to place the 88 MW capacity in rates. With respect to our outstanding SWEPCo Louisiana rate case, we are expecting an order in the fourth quarter of 2022. We've also made notable progress on APCo's 2020 Virginia case. As many of you likely recall, we successfully appealed the triennial rate order the day following the issuance of the order in November 2020, giving confidence in our position that the order was inconsistent with Virginia statutes.

We are pleased that the Court recently ruled in AEP's favor preserving our right to seek a retroactive adjustment in addition to the ongoing rate adjustment. Interim rates were implemented in Virginia on October 1st of this year. We've also actively managed the implications of increased fuel cost as we focused on maintaining a balance between cost recovery and customer impacts. As part of this effort, our operating companies continue to work with commissions, regulators and other stakeholders to educate customers about price surges and put mechanisms in place to alleviate these pressures.

For example, we have six-month and two-month clauses in I&M and SWEPCo, Louisiana irrespectively to help ease the effect of longer-term fueled clauses. We were also able to lengthen the months of fuel recovery in Virginia and Oklahoma and are working with our customers and commissions to make sure we recover that over a longer period of time. As you all know, this will be my last earnings call as I will be transitioning from CEO to Executive Chair on January 1st and Julie will become CEO of AEP.

We're very excited to have an executive of Julie's caliber lead our company. I'm confident in her deep knowledge of AEP as well as the emphasis she places on consistency, quality of earnings and dividends, and shareholder and customer value-creation that will be instrumental to AEP's continued success. I'm also confident that she has the heart to be a strong leader. I'm reminded of the lyrics from Rush's Closer to the Heart that I have always related to as a CEO and it goes something like this, And the Men and Women Who Hold High Places Must be the Ones to Start to Mold the New Reality Closer to the Heart.

The role of a CEO in the company, our communities and our country has changed during my tenure. Julie is the embodiment of a new CEO and will lead this company to even greater success. After 44 earnings calls, my tenure will soon come to an end as CEO of this great company. So, I will end this call with lyrics from a great Led Zeppelin song, And So, Today My World It Smiles and a song title is merely, Thank You. Julie?

Julie A. Sloat {BIO 6462741 <GO>}

Oh, my goodness, Nick. Thank you, thank you. Well, yeah, all heart and all end, absolutely, absolutely. So, thanks everyone for joining us today. I know you have a really busy morning with multiple companies reporting, so we'll try to be as efficient as possible. I'm going to walk us through the third-quarter and year-to-date results, share some updates on our service territory load and economy and finish with commentary on credit metrics and liquidity as well as some thoughts on our guidance, financial targets, and recap our commitments to stakeholders.

So I'm going to start on slide 8, which shows the comparison of GAAP to operating earnings. GAAP earnings for the third-quarter were $1.33 per share compared to $1.59 per share in 2021. GAAP earnings through September were $3.76 per share compared to $3.90 per share in 2021. For the quarter, I'd like to mention two reconciling items. First, there is a write-off of a Virginia Regulatory Asset associated with previously closed coal plants. This is a result of the Virginia Supreme Court opinion that affirmed the Company's original write-down of those plants in 2019 and allowed APCo to increase its Virginia rates on a going-forward basis.

The other reconciling item that I'd like to mention is related to the sale of Kentucky Power. You'll recall that we announced on September 30th that we'd entered into an amendment to the stock purchase agreement with Liberty that among other items resulted in a reduced purchase price. We've reflected the additional loss on the expected sale of Kentucky Power and Kentucky Transco as a non-operating costs. There is a detailed reconciliation of GAAP to operating earnings on pages 16 and 17 of the presentation today.

Let's walk through our quarterly operating earnings performance by segment on slide 9. Operating earnings for the third quarter totaled $1.62 per share compared to $1.43 per share in 2021. Operating earnings for the Vertically Integrated Utilities were $0.97 per share, up $0.10. Favorable drivers included rate changes across multiple jurisdictions, the impact of the Virginia Supreme Court ruling related to our APCo triennial review which you'll see on the waterfall today as a 6% catch-up of the 2017 through 2019 under earnings, positive weather on our Western jurisdictions and increased transmission revenue.

These items were somewhat offset by an increase in depreciation, lower normalized load and increased income taxes. Just as a reminder on O&M and depreciation as I mentioned on last quarter's call and included in our 2022 guidance details because of a change in accounting related to the Rockport Unit 2 lease at I&M, we're seeing approximately $0.05 of favorable O&M offset by $0.05 of unfavorable depreciation in each quarter of 2022, but no consequential earnings impact.

I'll talk a little bit more on load performance but I'll get to that here in a minute, so bear with me. The transmission and distribution utilities segment earned $0.32 per share, up a penny compared to last year. Favorable drivers in this segment included rate changes and positive weather in Texas and Ohio, an increased transmission revenue. Offsetting these favorable items were unfavorable O&M, depreciation and income taxes.

The AEP Transmission Holdco segment contributed $0.33 per share flat compared to last year, favorable investment growth of $0.02 was somewhat offset by unfavorable income taxes. Generation and marketing produced $0.14 per share, up $0.10 from last year. The positive variance is primarily due to higher retail margins, increased renewable wind production, higher market prices impacting generation margins and favorable income taxes.

Finally, corporate and other was down $0.02 per share driven by unfavorable interest expense, mainly as a result of the increase in short-term debt rates and increased O&M partially offset by reduced investment losses. The reduced investment losses are largely related to charge point losses that we had in the third quarter of 2021 that have reversed this year. I'll note that we exited our position in charge point during the third quarter, so aside from the year-over-year comparison, we will not have any new volatility in this particular aspect of corporate and other segment relating to our direct ownership of charge points share since the position has been liquidated.

So let's go to slide 10 and I'll talk about our year-to-date operating earnings performance. Year-to-date operating earnings totaled $4.04 per share compared to $3.76 per share in 2021. Operating earnings for Vertically Integrated Utilities were $2.15 per share, up $0.28, similar to the quarter favorable drivers included rate changes across multiple jurisdictions, the resolution of the APCo triennial, positive weather in our Western jurisdictions, increased transmission revenue and favorable normalized retail load.

These items were somewhat offset by increased depreciation and lower off-system sales. Once again, the change in accounting around the Rockport Unit 2 lease results in $0.17 of favorable O&M, offset by $0.17 of unfavorable depreciation. The Transmission and Distribution Utilities segment earned $0.95 per share, up $0.10 compared to last year. Favorable drivers in this segment included rate changes in Texas and Ohio, favorable weather and increased normalized retail load and transmission revenue. Offsetting these favorable items were unfavorable O&M, property taxes and depreciation.

The AEP Transmission Holdco segment contributed $0.95 per share, down $0.07 per share compared to last year. Favorable investment growth of $0.06 was more than offset by an unfavorable true-up of $0.07 and increased income taxes. As I mentioned last quarter, this is entirely consistent with our guidance. Our 2022 guidance had this segment down by $0.08 year-over-year as a result of the investment growth being more than offset by the annual true-up that occurred last quarter and some unfavorable comparisons on the tax and financing side.

Generation and Marketing produced $0.34 per share, up $0.14 from last year. The positive variance is primarily due to the sale of renewable development sites, improved retail margins, increased wholesale margins and land sales in the generation segment. Finally, corporate and other was down $0.17 per share, driven by lower investment gains, unfavorable interest and increased O&M. The lower investment gains are largely related to charge point gains that we had in 2021 that reversed this year.

Turning to slide 11, let me provide an update on our normalized load performance for the quarter. Overall, AEP service territory has maintained significant momentum through the first three quarters of the year despite increasing headwinds impacting the macroeconomy. Starting in the lower right corner, normalized retail sales increased by 2.6% in the third quarter compared to last year. Once again, every operating company experienced positive year-over-year growth for the quarter. Furthermore, the growth in the commercial and industrial sales this quarter more than offset the modest decline in residential sales.

For the year-to-date comparison, AEP's normalized retail sales increased by 3.1% with growth spread across all major retail classes and operating companies. In fact, we're on pace to experience the strongest year for load growth since the mid 1990s and that's on top of the recovery year we had last year when the load increased by 2.1%.

Moving to the upper left corner, normalized residential sales decreased by 0.8% in the third quarter, but remained up 0.3% through September compared to last year. For the quarter, residential accounts increased by 0.4% but this was offset by a 1.2% decline in weather-normalized usage. This is not surprising when you consider that last year, many of our customers were receiving extra income from the fiscal stimulus, it is not happening in 2022. While the results were mixed by operating company, the strongest residential growth for the quarter was at SWEPCo.

Moving right, weather-normalized commercial sales increased by 3.4% for the quarter and were up 3.8% for the year-to-date comparison. The growth in commercial sales was spread across nearly every operating company and eight of our top 10 commercial sectors. The fastest growing commercial sector is data centers where load was up 33% compared to last year for the quarter and for the year-to-date comparisons.

Finally, focusing on the lower left corner, you'll see that the industrial sales posted another strong quarter, up 6% for the quarter and up 5.5% for the year-to-date comparison to last year. Industrial sales were up in nearly every operating company and most of our largest sectors. We continued to experience double-digit growth in number of key industries this quarter including chemicals manufacturing and oil and gas extraction. We also saw robust growth in primary metals manufacturing, pipeline transportation, paper manufacturing and coal mining.

To summarize, the AEP service territory has maintained significant momentum through the first nine months of the year despite the challenging headwinds of inflation, higher interest rates, supply-chain disruptions and the labor shortage. We know the Federal Reserve's approach to address inflation is designed to slow down the economy, which will eventually work its way through our footprint. However, I'd like to remind you that there are things that we've done and we'll continue to do to help mitigate the impact of slowing economic conditions in our service territory. Specifically, we're talking about our economic development efforts.

So turning to slide 12, I want to highlight how our commitment to economic development is helping to sustain load growth even in the face of challenging economic conditions. The chart on this slide illustrates why this strategy is so important to us. The blue bars on this chart show the growth in gross regional product or GRP for the AEP service territory over the past year. So, you can see that has been slowing over the period, in fact for the third quarter, growth in AEP's GRP was essentially flat; however, the green bars here show that our industrial sales growth over the same period. You will notice that they've maintained their strength, even improving 6%

without the help from GRP. How does this happen, that's because of our consistent and disciplined approach to economic development over the years.

A lot of the growth in industrial load that we're seeing today is a consequence of economic development projects from previous years that are coming online this year. Examples include a large steel plant and an LNG processing facility that are now online in the AEP Texas service territory, a new chemicals plant that is now operating in Tennessee or paper plant that is now producing in Oklahoma and these are just a few of the many examples that we could mention, but the key takeaway here is that AEP's commitment to economic development is what is allowing us to be on track to push our strongest year for load growth in decade despite an economy that is beginning to slow down.

Another key point to remember is that you cannot turn it on or off like a light switch. Economic development projects take time to materialize and the results that we see here today are largely the result of activities that occurred years ago. By making this a key component of our strategy, AEP is helping to mitigate the impact of economic downturns on our customers, our communities, and our investors. In AEP's economic development team, has a proven track record of helping bring these new customers to our service territory with an emphasis on jobs and load. In fact, the AEP service territory has added over 106,000 jobs this year.

So, let's move on to slide 13 to discuss the Company's capitalization and liquidity position. We're doing well in this regard. On a GAAP basis, our debt-to-capital ratio held constant from the prior quarter at 61.4%. Taking a look at the left upper quadrant on this page, you'll see our FFO-to-debt metric stands at 14.5% on both the Moody's and GAAP basis, which is an increase of 1.1% and 1.2% respectively from the prior quarter.

The primary reason for the increase is attributed to the completion of the PSO securitization efforts which increased cash from operations. As we stated on our last earnings call, we anticipated trending toward our FFO-to-debt targeted range of 14% to 15% as the year progressed and we currently sit comfortably within that range. You can see our liquidity summer in the lower left quarter on the slide. Our five-year $4 billion bank revolver and our two-year $1 billion revolving credit facility support our liquidity position, which remains strong at $3.6 billion.

On the qualified pension front, while our funding status decreased 0.3% during the quarter, it remains comfortably strong at 105.3%. Negative returns on the risk-seeking and fixed-income assets during the quarter were primary drivers of the funded status decrease; however, rising interest rates caused plan liabilities to decrease, which provided a favorable offset to the negative asset returns, so we're in a good place in terms of funding.

Let's go to slide 14, so I can do a quick recap of today's message. The third quarter continues to provide a solid foundation for the rest of 2022 and allowed us at our recent Analyst Day to narrow and raise our operating earnings guidance range to $4.97 to $5.07 with a midpoint of $5.02. As you know, AEP offers steady and predictable growth driven by our low-risk regulated business, robust electric infrastructure investment pipeline and our proven track record of managing cost pressures over time while growing our rate base.

This along with the updated 2022 load forecast we provided at our October 4th Analyst Day and the Virginia Supreme Court ruling related to APCo's 2017 to 2019 triennial review position us to navigate headwinds remaining this year that you would expect such as continued inflation, interest rates, weather risks, etc., which is why we maintain (inaudible) range when we recently lifted and tightened our 2022 guidance range. We continue to be committed to our long-term growth rate of 6% to 7%, continued dividend growth and a strong balance sheet while we are derisking the company, focusing on the customer and actively managing the portfolio.

So, we really do appreciate your time and attention today. I know you guys are super busy with all the earnings calls. So with that, I'm going to kick it over to the operator, so we can hear what's on your mind and take your questions.

Questions And Answers

Operator

Thank you. Our first question is from Jeremy Tonet from JPMorgan. Please go ahead.

A - Nicholas K. Akins {BIO 15090780 <GO>}

Good morning, Jeremy.

Q - Jeremy Tonet {BIO 15946844 <GO>}

Good morning, good morning. I just wanted to pick up on one of the key themes at the Analyst Day talking about the transmission within AEP and a significant growth. The potential there as you see it and what appears to be a valuation disconnect with AEP stock relative to public comps in transactions, I'm just wondering if that conversation invited any reverse inquiries on your assets. I know you said these are core to you, but just kind of curious how that's developed and any other thoughts on that side you might share?

A - Nicholas K. Akins {BIO 15090780 <GO>}

Yeah, I'll just follow up with that I mentioned transmission, so I'll turn it over to Julie and respond to that.

A - Julie A. Sloat {BIO 6462741 <GO>}

Thank you, Nick. Thanks, Jeremy. Thanks for the question. Let me tell you, we certainly got a lot of attention from our investor base and so I'll answer it that way. We appreciate that because that means we're doing our jobs. I think we still need to do a lot of work here and make sure that it may make it easy for you all to understand what the earnings stream is and the earnings potential of that particular business and so as we were getting ready for this call today, I'm looking at the waterfalls on pages 9 and 10 of the presentation today.

And so, let me go to page 10, just real quickly so that AEP Transmission Holdco, which is our pure-play transmission component, contributed $0.95 of the $4.04 year-to-date and as you know, we've got more transmission in play across this waterfall to that shows up in the Vertically Integrated Utilities and the T&D segment. So as a swag and will do better with this as we go into 2023 to give you a more granular view of the transmission component in the aggregate from AEP.

But assume that roughly 50% of the earnings on the Vertically Integrated Utilities and T&D Utilities is essentially the part of adding the $0.95 to another -- let me say it in another way, I'm totally tripping over myself here, $0.95 from the AEP Transmission Holdco essentially doubled that, so that's about half. So half of our earnings are coming from that particular segment, the other half is coming from the Vertically Integrated Utilities and T&D Utilities.

So not insignificant when you compare that just under two bucks to the $4.04, so we'll do better and I'll do better explaining the stuff as we go forward in 2023 but wanted to have that number kind of back in my pocket here in case you ask the question, so I'm glad you did.

A - Nicholas K. Akins {BIO 15090780 <GO>}

But the overarching theme around transmission is certainly with the movement to clean-energy economy and the focus we have on renewables is being put in place. You cannot put these renewables in place without additional transmission. Transmission is becoming more constrained, so it turns out to be very positive from an AEP perspective, from an opportunities to really focus on not only the development transmission which we're the largest in the country, but also in terms of the renewables build-out and in fact distribution with distributed energy resources that will drive different resource needs as well. So, all in good shape from that perspective, so we feel very, very bullish about our transmission.

Q - Jeremy Tonet {BIO 15946844 <GO>}

Got it, that's helpful and then just shifting gears a little bit, rates. Rates moving up here and so just wondering what you can say about that with regards to short-term rate moving higher and long-term debt issuance is being more expensive, just think about historic test years and lag in jurisdictions, wondering what can be done or how do you see that unfolding?

A - Nicholas K. Akins {BIO 15090780 <GO>}

Yeah. Julie?

A - Julie A. Sloat {BIO 6462741 <GO>}

Yeah. No, thanks again for the question. We are keeping a watchful eye on that. You're absolutely right. So, let me kind of compare and contrast the short-term debt rate that we were realizing last year through the first nine months was about 27 basis points to date through the first nine months that was about at 1.46%. So, a significant uptick and so what we'll be doing is continuing to manage across the different buckets of tenure and using kind of barbell strategies to do our financings going forward.

We still have a little bit of work we have yet to do this year and that's at parent, I mentioned that at our Analyst Day back on October 4th and we're assuming that rates would adjust to on a longer-term basis to about 5% to 6% for us that compares to through the year-to-date, a rate of about 3.34%. We will and do have that embedded in our 2023 guidance but we'll continue to work with that.

Let me give you another finer point to what I pay attention to is how much of our debt is floating rate, we generally target somewhere between 15% and 20% of our total portfolio being floating rate. As of the end of the third quarter, we were at about 14.8% that equates to about the parent, about $5.7 billion, $1.95 billion of that being CP, so we've got a fair amount of fluctuation there, but that's already getting picked up in rates and this absolutely embedded in 2023 guidance. We'll have more for you to share and for your modeling efforts at the EEI Conference when you get all the assumptions that we have behind the waterfall in details that you're typically used to seeing from us.

Q - Jeremy Tonet {BIO 15946844 <GO>}

That's very helpful. I'll leave it there. Thank you.

A - Julie A. Sloat {BIO 6462741 <GO>}

Yeah.

A - Nicholas K. Akins {BIO 15090780 <GO>}

Thank you.

Operator

Thank you, and the next question will come from the line of Durgesh Chopra from Evercore ISI. Please go ahead.

A - Nicholas K. Akins {BIO 15090780 <GO>}

Good morning, Durgesh.

Q - Durgesh Chopra {BIO 20053859 <GO>}

Hey, hey. Hey, good morning.

A - Nicholas K. Akins {BIO 15090780 <GO>}

Good morning.

Q - Durgesh Chopra {BIO 20053859 <GO>}

Congrats on a solid quarter here. I have two questions. The first one just maybe can you elaborate to the extent you can, you mentioned phase 1 of the unregulated renewable cell, just who are the interested parties here or the strategics, are these privates or any additional color you can share there?

A - Nicholas K. Akins {BIO 15090780 <GO>}

I would certainly say that the list was robust, and all the usual suspects that you would think of and beyond, but there were a lot. And I'd say, it was still generally half-and-half, 60:40, whatever it was of strategics and others financials. And actually the Phase 2, we're going into a list with strategics and financials. And that's a well-balanced group. One that I'm sure will hold each other accountable. They are in the process but we are very happy with the responses we received.

Q - Durgesh Chopra {BIO 20053859 <GO>}

Excellent. It sounds like you're making very good progress though.

A - Nicholas K. Akins {BIO 15090780 <GO>}

Yeah. I'll go into the confidential rooms and all that kind of stuff and more due diligence will be done and then we'll go through the process with them, just for this is what the process is.

A - Julie A. Sloat {BIO 6462741 <GO>}

And Durgesh, this is Julie. We have a two-step bid process and we would expect to be in a position to have a PSA signed in early 2023 with a closing in the first half of next year. I think we shared that with you on October 4th, and we get the question around who is the primary regulatory authority or body that will govern this and that's FERC as you know.

Q - Durgesh Chopra {BIO 20053859 <GO>}

Got it, thanks for that Julie. And then maybe just to pivot on to the second subpoena from SEC, just how to read into that, what are the implications for you. I mean does it --

A - Nicholas K. Akins {BIO 15090780 <GO>}

Yeah.

Q - Durgesh Chopra {BIO 20053859 <GO>}

-- increased the risk, sort of potential (Multiple Speakers).

A - Nicholas K. Akins {BIO 15090780 <GO>}

Yeah. We view this as a continuing part of the process and we said we would be transparent. And we have been transparent and we'll continue to work in a positive fashion with the SEC during their investigation and certainly the issuance of a second subpoena is really, they just need more information, so and we're going to supply.

So we're going to work with them and we'll continue doing so. So our response is essentially the same as from the first one. We recognize there were governance issues needed to change relative to 501(c)(4) and we made those changes and certainly from our perspective, we will continue to work with them to get this thing resolved.

Q - Durgesh Chopra {BIO 20053859 <GO>}

Excellent guys. Thank you so much. I appreciate the time.

A - Nicholas K. Akins {BIO 15090780 <GO>}

Yeah.

Operator

Thank you. The next question is from Julien Dumoulin-Smith from Bank of America. Please go ahead.

A - Nicholas K. Akins {BIO 15090780 <GO>}

Hey, Julien.

Q - Julien Dumoulin-Smith {BIO 15955666 <GO>}

Hey, excellent. Hey, good morning and congrats, Nick.

A - Nicholas K. Akins {BIO 15090780 <GO>}

Yeah, sure. Thank you.

Q - Julien Dumoulin-Smith {BIO 15955666 <GO>}

Absolutely. If I can pivot still on this, if I can continue with the last question a little bit and can ask again about this second subpoena, just what's your understanding of the process from here on out again. I get that they continue to inquire here, just can you elaborate a little bit further here? Again, obviously you're complying, you're submitting documentation, but just a little bit of a sense of what you get from (Multiple Speakers).

A - Nicholas K. Akins {BIO 15090780 <GO>}

Yeah, I mean, there's not much else we can say about obviously because it is a process with the SEC and it's really up to the SEC, what -- how they want to continue to analyze information and ask for new information and typically I guess, whenever they need new information, they'll issue a new subpoena. So, it's just part of the process and it's really up to the SEC and the only control we have is to continue to cooperate very positively and respond and we'll continue to do that.

Q - Julien Dumoulin-Smith {BIO 15955666 <GO>}

Excellent, okay, perfect. And then if I can just with respect to West Virginia, can you guys talk a little bit about the fuel situation there? And is there an ability to leverage securitization here to address the balance there and just to what extent can that sort of fully address the balance?

A - Nicholas K. Akins {BIO 15090780 <GO>}

Yeah. Julie?

A - Julie A. Sloat {BIO 6462741 <GO>}

Yeah, no, thanks for the question, Julien, and no, actually as a matter of fact that's exactly what we're contemplating. As you know, we've got a fair amount of exposure in excess of $400 million as of the end-of-the third-quarter of deferred fuel in West Virginia in particular. We want to be very sensitive to customer bills, so the plan is to see what we can do around securitization of the outstanding balance and manage rates for customers.

Right now, the current mechanism is we have a 12-month fuel clause to reset in account for the prior year, we're currently in hearing there but we want to be extremely sensitive to our customer base as it relates to that particular area. So standby, we'll have more to tell you and more to share as we make some progress but securitization is absolutely contemplated.

A - Nicholas K. Akins {BIO 15090780 <GO>}

Yeah.

Q - Julien Dumoulin-Smith {BIO 15955666 <GO>}

Got it, so there is no qualification issues or needing any clarification legislation, right? That it should be directly applicable?

A - Nicholas K. Akins {BIO 15090780 <GO>}

That's right.

A - Julie A. Sloat {BIO 6462741 <GO>}

Yeah.

Q - Julien Dumoulin-Smith {BIO 15955666 <GO>}

All right.

A - Julie A. Sloat {BIO 6462741 <GO>}

Though we do need some clarification on the legislation because it's very specific to what you're trying to securitize, so that will be a critical path for us.

Q - Julien Dumoulin-Smith {BIO 15955666 <GO>}

Okay. So we should look for that next --

A - Julie A. Sloat {BIO 6462741 <GO>}

Yes.

Q - Julien Dumoulin-Smith {BIO 15955666 <GO>}

-- in terms of getting it done.

A - Julie A. Sloat {BIO 6462741 <GO>}

Yes.

Q - Julien Dumoulin-Smith {BIO 15955666 <GO>}

Okay. Wonderful.

A - Julie A. Sloat {BIO 6462741 <GO>}

Yes. Yes.

Q - Julien Dumoulin-Smith {BIO 15955666 <GO>}

Thank you. I appreciate it and, Julie, I wish you all the best. Good luck.

A - Julie A. Sloat {BIO 6462741 <GO>}

Oh hey, thank you so much. Thank you, thank you.

Operator

Thank you. Our next question is from Ross Power from UBS. Please go ahead.

A - Nicholas K. Akins {BIO 15090780 <GO>}

Good morning, Ross.

Q - Ross Power

Good morning, Nick. Good morning, Julie. How are you?

A - Julie A. Sloat {BIO 6462741 <GO>}

Good morning.

Q - Ross Power

Nick, thank you for the Rush quote. I very much appreciate that. I understand that (inaudible).

A - Nicholas K. Akins {BIO 15090780 <GO>}

Good for you.

Q - Ross Power

So I just had a couple of questions here. I was going to ask about the subpoena, but we've kind of beaten that to death but the (inaudible) strategic computing that's going to happen within sort of the first half of next year. Are there other businesses that sort of fit into that same sort of potential strategic review category? I'm thinking about wholesale services or distributed resources. Are they core to you or is that something we could see in the future?

A - Nicholas K. Akins {BIO 15090780 <GO>}

Yeah, so obviously we have three -- I guess three of the normal four burners already loaded. One is Kentucky, one is the contracted renewables, and then the retail after that and we have to do a really a strategic review around retail because it includes some of Ohio and that kind of things we need to fully understand that. And we said that we would look at other parts of the business if it fuels the growth that we're focused on relative to transmission and the movement to a clean-energy economy, and so we'll continue to do that.

I really don't want to position one business versus another at this point, but we'll continue to look at all of our business to make sure that we are being as efficient as possible to, as Julie always says, actively manage the portfolio to ensure that we are moving forward from a growth perspective but also from a derisking perspective to ensure that we are spending our capital on the right things and O&M as well. So that's probably all I will say at this point. I'll leave it to Julie in the future to answer those questions. Julie?

A - Julie A. Sloat {BIO 6462741 <GO>}

Yeah, yeah, but I would leave you with this thought, as it relates to OnSite Partners which is our distributed energy solutions organization and we have wholesale services as well when you look at the quadrants of our unregulated components of our total AEP business. I would submit to you that you should assume that they operate business as usual. Those are closer to customer, those are things that we need to engage in to manage our day-to-day operations and we want to make sure that we're extracting all the intelligence we possibly can and taking care of the customer at the same time but if there are things we can leverage to help us in the regulated envelope, we'll be doing that as well.

So, distributed energy solutions seems to scratch that itch, and we've gotten a lot of success in one way out of that, so business as usual and we'll keep you apprised, anything else that we put on deck like Nick said, we got all of our burners busy, you know what's on deck but the point here is to get as efficient as we possibly can so that we can deliver the goods, take care of you, take care of our customer and then when we're good to go.

Q - Ross Power

That's great (inaudible), thank you. And then just maybe one more around sort of the flexibility of your capital strength. As you kind of iterated at the Analyst Day many times, Julie, a lot of the capital is in transmission. We've seen some other companies maybe struggle to get transmission projects on schedule given the siting and permitting issues. Is that just a large-scale transmission project issue? And do you have sort of just a lot of smaller scale stuff you can move around in that transmission and even in the distribution bucket?

A - Nicholas K. Akins {BIO 15090780 <GO>}

Yeah, so obviously we've had the same conversations (Technical Difficulty) Congress. A large block of our transmission is transmission within our service territory and actually, basically the nuts and bolts of making sure that we have rehabilitation of the grid, replacement of old resources, we have some transmission lines and just every time we have our sub-company Board meeting always comment about these 100-year-old lines that come up for replacement and we're still in the process of doing that.

We've talked a lot about the amount, just this sheer magnitude of AEP's transmission system and the average age being 57 years old or some number like that and in the spend that we have ongoing now just increases it by a year. Every year it goes by like (inaudible) $3 billion. So you see really we have not had issues with the construction of our transmission. Now, if you do a new transmission with new large-scale transmission that's where you really get into permitting and right-of-way issues and that's really part of the permit legislation.

And then when you crossover states, obviously the cost allocation issues occur, so but by and large almost all of our transmission is really related to transmission that either already exists or within our territory that we certainly have the ability to move forward with and we also have and this is probably more than you asked for but from a transmission perspective, we've increased our planning associated with that. We used to do 120% of the capital plan. Now, we do 130%. We're also looking at distribution actually to do the same thing around the 120%.

So, those are mechanisms where we continue to be able to use throttles, we continue to be able to adjust based upon different projects being either slowed down, sped up or whatever and we continually adjust to that because we have thousands of projects to be able to work that through, so that really drives that element of consistency around our ability to provide capital for transmission and in fact distribution.

Q - Ross Power

That's fantastic, Nick. Thank you. Julie, best of luck.

A - Julie A. Sloat {BIO 6462741 <GO>}

Hey, thank you so much. Thank you, thank you.

Operator

(Operators Instructions) We will go to the line of Michael Lapides from Goldman Sachs. Please go ahead.

Q - Michael Lapides {BIO 6317499 <GO>}

Hey guys.

A - Nicholas K. Akins {BIO 15090780 <GO>}

Hey Michael.

Q - Michael Lapides {BIO 6317499 <GO>}

Hey Nick, big --

A - Nicholas K. Akins {BIO 15090780 <GO>}

We're looking for something from you, but go ahead.

Q - Michael Lapides {BIO 6317499 <GO>}

Big weekend coming up, Alabama and LSU, we got 10 days. I hope that's not like you're looking for me from (inaudible). Hey, couple of questions. First of all, I loved slide 41. When I'm looking at slide 41, Nick, it's trailing 12 month earned ROE chart. Just curious, when I think about what's embedded in 2023 guidance, which of those get materially better in '23, which of those face even a little bit more lag in '23 than they do right now?

A - Nicholas K. Akins {BIO 15090780 <GO>}

Yeah. Julie?

A - Julie A. Sloat {BIO 6462741 <GO>}

Yeah, yeah, so Michael what you should anticipate is movement on the PSO front. I mean we've got a little bit of momentum there, we've got the securitization taken care of now. We'll be making an application soon for a rate case, so anticipate that. We do expect over time that APCo is going to improve too, particularly now that we've got the Virginia triennial behind us and you're starting to see the fruits of that effort already showing up in our waterfall slides.

And then we've got activity regulatory activity underway at SWEPCo too, but we will give you more granular detail at the EEI Conference on a company-by-company basis across the board, so stay tuned for that, but as you know the entire objective is to move the needle and closing the gap and I would submit to you that that's how we describe another aspect of our active management. So we should be in good shape and moving in the right direction. Obviously, we're comfortable with the guidance we already put out there.

A - Nicholas K. Akins {BIO 15090780 <GO>}

Yeah.

Q - Michael Lapides {BIO 6317499 <GO>}

Got it and then speaking of APCo and the court case in Virginia and the $37 million pre-tax benefit you took this quarter, how should we think about that for 2023? I mean is that just a nonrecurring one time or should be smooth that out over '23's quarters? I'm just trying to think about how to actually model that?

A - Julie A. Sloat {BIO 6462741 <GO>}

Yeah. Yeah. No, I love that question because (inaudible) with that myself as we've got the good news. So yeah, $0.06 that you saw in the third quarter which is essentially like a catch-up from the under earnings from 2017 to 2019, so that's unique, so $0.06 this quarter and I'll take it a step further. Let's go to the fourth quarter because you'll probably ask me about that too. We should have about a penny of earnings associated with this particular outcome in the fourth quarter of 2022, so think about that when you're calibrating your model.

And then for 2023, we'll have about $37 million of additional revenues from rate increases that effectively covers January of 2021 to September 2022 that in terms of what we should have been able to recognize but we're spreading it over 16 months plus we have that going forward a benefit that starts October 2022. So what all does that mean, that means $0.06 spread across 2023 and that will be included in the waterfall guidance that we gave to you at EEI. So I hope that helps kind of (Multiple Speakers) for you.

Q - Michael Lapides {BIO 6317499 <GO>}

That does help and then finally one last thing, can you remind us what's your cash tax position will be in the coming years?

A - Julie A. Sloat {BIO 6462741 <GO>}

Yeah, cash tax gets really goofy with the BMT, so those numbers kind of float all around and we can always help you behind the scenes with modeling but for cash tax in 2022, I want to say that the rate is something like 10.8% then go out to 2023 the way we're modeling, it is just a little bit over 4% but I would just direct you back to the GAAP annual effective tax rate and so we're looking at the traditional 5.2% in 2022 and it pumps up a little bit to about 8.4% in 2023 but we'll be able to give you more granular there too when we roll out all the backup to the 2023 guidance.

But yeah the BMT, it almost looks theological and we're looking at some of the modeling. I mean it works and it's accurate but it's just the rate kind of bounces all over the place from a cash perspective because you're using those tax credits.

Q - Michael Lapides {BIO 6317499 <GO>}

Got it. Thank you, Julie and once again, congratulations.

A - Julie A. Sloat {BIO 6462741 <GO>}

Yep. Thank you, thank you.

A - Nicholas K. Akins {BIO 15090780 <GO>}

Thanks Michael.

Operator

And at this time, there are no further questions in queue. Please continue.

A - Darcy Reese {BIO 20391516 <GO>}

Thank you for joining us on today's call. As always, the IR team will be available to answer any additional questions you may have. Louis, please go ahead and give the replay information.

Operator

Thank you. And ladies and gentlemen, this conference will be available for replay beginning at 11:30 AM today and running through November 4th at midnight. You may access the AT&T replay system at any time by dialing 866-207-1041 and entering the access code 7723525. International callers can dial 402-970-0847. Again, the numbers are 1-866-207-1041 and 402-970-0847, access code of 7723525 and that does conclude our conference for today. Thank you for your participation and for using AT&T conferencing service. You may now disconnect.