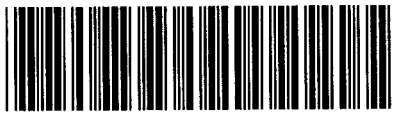

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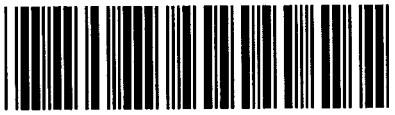

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SOAH DOCKET NO. 473-02-3473
PUC DOCKET NO. 26195

JOINT APPLICATION OF TEXAS GENCO, LP AND CENTERPOINT ENERGY HOUSTON ELECTRIC, LLC TO RECONCILE ELIGIBLE FUEL REVENUES AND EXPENSES PURSUANT TO SUBST. R. 25.236	§	**BEFORE THE STATE OFFICE OF ADMINISTRATIVE HEARINGS**

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March 25, 2004

Description **Page**

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JOINT APPLICATION OF TEXAS GENCO, LP AND CENTERPOINT ENERGY HOUSTON ELECTRIC, LLC TO RECONCILE ELIGIBLE FUEL REVENUES AND EXPENSES PURSUANT TO SUBST. R. 25.236	§ § § § § §	BEFORE THE STATE OFFICE OF ADMINISTRATIVE HEARINGS

CENTERPOINT'S REPLY TO EXCEPTIONS TO THE PROPOSAL FOR DECISION

I. INTRODUCTION

In their exceptions, Texas Industrial Energy Consumers ("TIEC") and the City of Houston ("COH") once again propose disallowances that are contrary to the Commission's rules and are inconsistent with past Commission practice and sound regulatory policy. They appear to be under the mistaken impression that because ratepayers pay these costs, as they always have, or because the proposed disallowance is small compared to HL&P's overall fuel and purchased power costs, this somehow justifies ***some*** level of disallowance.[1] *See, e.g., COH Exceptions at 1-2.* These have never been and could never be valid bases for disallowance.

Moreover, they make arguments that are not supported by the record, or worse, are refuted by the record. With respect to the Kerr-McGee costs, TIEC seeks an opportunity to re-litigate an issue they and other intervenors raised and lost in this proceeding. TIEC fails to mention that when it litigated and won an issue in the TNMP final fuel reconciliation proceeding, it subsequently opposed, as improper, TNMP's efforts to re-litigate that same issue in the TNMP true-up proceeding. To support the flawed heat rate assumptions used in the "imputed capacity"

[1] In judging the significance of the amounts at issue here, a more relevant comparison can be found in the SEC Form 8-K that CenterPoint Energy, Inc. was required to file upon receipt of the PFD. As a result of the disallowance recommended by the PFD, CenterPoint was required to establish a reserve and reduce its previously announced 2003 earnings for the entire company (not just the two CenterPoint entities in this proceeding) by nearly 15%.

calculations, TIEC floats a new illogical argument that has no factual basis, produces arbitrary and unreasonable results and contradicts the testimony of its own witness. COH, without citation to the record or legal authority, makes its own new argument regarding its proposed JOA disallowance and, in doing so, misstates the record created by its own witness.

In addition to these substantive flaws, TIEC and COH have failed to meet the evidentiary burden established in the Commission's rules. The Commission's procedural rules require exceptions to state with particularity "the evidence and law relied upon." P.U.C. PROC. R. 22.261(d)(2). COH and TIEC both failed to do this at various points in their exceptions. TIEC's exceptions are particularly troubling. In its exceptions, TIEC included exactly ***one*** citation to the record and no citations to any legal authority. TIEC's imputed capacity discussion contains no evidentiary or legal citations whatever, despite numerous assertions such as "[i]n view of the evidence in this case," *TIEC Exceptions at 3*, "[a]s the record demonstrates," *Id. at 4*, and "the evidence in the record demonstrates," *Id. at 5*. Similarly, COH makes new assertions regarding JOA payments without any citation to the record or legal authority. Exceptions without legal or evidentiary support violate the Commission's procedural rules and should be ignored.

II. KERR-MCGEE COSTS

A. The Evidence In This Proceeding Shows That the Kerr-McGee Costs Have Not Been Recovered.

Having litigated and lost the issue of whether CenterPoint has recovered certain costs under its coal supply contract with Kerr-McGee, TIEC now excepts to Finding of Fact No. 37 and 38, and seeks a second bite at this apple in the 2004 true-up proceeding. No less than 5 of

the 8 witnesses who testified in the present proceeding substantively addressed this issue.[2] All were cross-examined on their opinions. After considering the entire record, the ALJ found that CenterPoint is entitled to recover these costs in the true-up proceeding. Rather than disputing the ALJ's finding, TIEC would have the Commission call a King's-X and re-litigate this dispute in the true-up proceeding. TIEC's exceptions are particularly disingenuous given that TIEC and the other intervenors are the parties that raised the substantive issue in the first place. *TIEC Ex. 1 at 6:20-21 (Pollock Dir.) (claiming recovery through ECOM in the UCOS proceeding (Docket No. 22355)); OPC Ex. 1 at 21:23-22:3 (Falkenberg Dir.) (raising the issue of recovery in the UCOS proceeding (Docket No. 22355) and in the 2004 True-Up proceeding).* CenterPoint responded to these unfounded accusations in rebuttal testimony, and the parties spent considerable time at hearing exploring these issues. In fact, the ALJ required each party to address the following issues in its initial and reply briefs:

> C. Are these [Kerr-McGee] costs properly recoverable, or in fact already recovered, through any other mechanism?
>
> 1. Price to Beat
> 2. ECOM
> 3. UCOS
> 4. 2004 True-Up Proceeding.

See Order No. 35 at 2 (November 24, 2003). The PFD properly concluded that the evidence in this proceeding supports a finding that the Kerr-McGee costs have not been recovered. In fact, no party argued for a dollar amount different than the $46.2 million sought by CenterPoint. For TIEC to now argue that the Company did not prove that the Kerr-McGee costs had not been recovered quite simply ignores the substantial evidentiary record and post-hearing argument on this issue.

[2] These include OPC witness Mr. Falkenberg, COH witness Mr. Daniel, TIEC witness Mr. Pollock, and CNP witnesses Ms. Thomas and Ms. Mitcham.

TIEC's claim that these costs have not been proven "stranded" is equally without merit. *TIEC Exceptions at 2.* No party contested the evidence presented by CenterPoint that the $46.2 million in Kerr-McGee costs were on the Company's books in an Electric Plant in Service ("EPIS") account as of December 31, 2001. *CNP Ex. 4 at Figure CDT-13 (Thomas Dir.).* Indeed, the very parties opposing inclusion of the Kerr-McGee costs in fuel expenses used ***the fact*** that these are "stranded costs" to support their arguments. *TIEC Ex. 1 at 7:7 (Pollock Dir.) (stating that these costs should be considered "among the other stranded costs in the True-Up proceedings"); TIEC Reply Brief at 6 ("the Kerr-McGee deferred contract costs have already been recovered, and/or will be recovered in CenterPoint's stranded cost case"); OPC Ex. 1 at 21:9-10 (Falkenberg Dir.) (stating "these [Kerr-McGee] costs have effectively become stranded costs").*

TIEC's requested re-litigation of this issue is also contrary to the policy TIEC claimed to support in TNMP's true-up proceeding (Docket No. 29206). There, TIEC argued that the Commission should not reconsider an issue that had been adjudicated in TNMP's final fuel reconciliation (Docket No. 27576) stating, "[t]he ALJ should reject TNMP's improper attempt to gain reconsideration of an issue that the Commission has already decided. . . ."[3]

Having properly reviewed evidence on this matter in this proceeding and having reached a conclusion based on that evidence, it makes no sense now to defer this decision to the true-up proceeding. Doing so would be a waste of Commission, SOAH and party resources. TIEC simply wants a second bite at an issue it tried and lost in this proceeding.

[3] *Application of Texas-New Mexico Power Company, First Choice Power, Inc., and Texas Generating Company, L.P., to Finalize Stranded Costs Under PURA §39.262*, PUC Docket No. 29206, TIEC's Response to Texas New-Mexico Power Company's Motion for Clarification and/or Reconsideration of the Commission's Preliminary Order at 5 (February 27, 2004).

III. IMPUTED CAPACITY

A. The Heat Rates Proposed By TIEC and OPC Are Significantly Understated.

TIEC and OPC have a serious problem. The proxy-price methodologies they presented in this case were rejected by the Commission in the *El Paso* case.[4] Now TIEC tries to recast its theory by claiming that the heat rate and methodology that it used was intended to represent the heat rate of the ***supplier*** and not the heat rate of HL&P's own units. *TIEC Exceptions at 4.* TIEC provides no citation to ***any*** evidence in the record to support this assertion, which by itself dictates that the assertion should be rejected. In addition, TIEC's new rationale is illogical, contradicts the statements of its own witness and leads to untenable results.

In calculating their proxy prices, OPC and TIEC respectively claimed to use the heat rate of the Company's "least efficient combustion turbine" and "most expensive peaking units." *OPC Ex. 1 at 15:5 (Falkenberg Dir.); TIEC Ex. 1 at 17:20 (Pollock Dir.).* As noted in the PFD, the evidence in this proceeding clearly showed that neither OPC nor TIEC followed their own rationale. *PFD at 28.* TIEC seeks to expand the universe of "most expensive peaking units" to the average for ***all*** 23 of HL&P's peaking units over the entire 53 months of the reconciliation period. *TIEC Exceptions at 4; Tr. at 305:16-20 (Pollock).* That is plainly unreasonable given the record evidence, noted by the PFD, that the heat rates of HL&P's least efficient (i.e., "most expensive") units averaged ***over*** 20,000 Btu/kWh[5] during the reconciliation period, *Tr. at 307:6-10 (Pollock) (noting that several units had average heat rates above 20,000)*, and HL&P had one unit with an average heat rate over 30,000 Btu/kWh. *Tr. at 306:18-22 (Pollock).* The PFD appropriately adjusted both the OPC and TIEC methodologies using a

[4] *Petition of El Paso Electric Company to Reconcile Fuel Costs*, PUC Docket No. 26194, Memorandum from Chairman Hudson (March 10, 2004) (adopted to modify the PFD at the March 10, 2004, open meeting).

[5] CenterPoint inadvertently used the wrong units (i.e., MMBtu/kWh) in describing the heat rate issues in its Exceptions to the Proposal for Decision. As reflected in this document and in the record, the correct units are Btu/kWh.

heat rate that more reasonably reflects the Company's "most expensive peaking units." *PFD at 26 (noting the effect of the adjustment on both methodologies) and 28 (stating that both methodologies used an understated heat rate).*

In its exceptions, TIEC claims that the heat rate and prices it used were a proxy for heat rates and production costs of the entities that sold electricity to HL&P at the time the electricity actually flowed. *TIEC Exceptions at 4.* Simple logic dictates that the heat rate and costs of any supplier are not governed by or related to the heat rate or other operating characteristics of HL&P's units. TIEC offers no citations to the record supporting its arguments, and for good reason. Neither TIEC nor any other party presented ***any*** evidence establishing a relationship between HL&P's average peaking heat rates and any supplier's heat rates. No party presented evidence regarding, for instance, the market price of energy or capacity at any time during the reconciliation period, or the actual fuel price or heat rate for any particular supplier or for any particular transaction. In fact, both OPC and TIEC candidly admitted at hearing that they made no effort whatever to estimate the actual price of energy in the market. *Tr. at 252:5-14 (Pollock); Tr. at 395:10-12 (Falkenberg).* The parties cannot even state whether the seller in a given transaction was even generating the energy itself, or reselling power it purchased from another source. *Tr. at 411:20-23 (Falkenberg).* In short, TIEC's assertion is utterly unsupported by the record. Under no circumstances can TIEC's proposed heat rate be said to reasonably estimate the energy or capacity costs of any entity that supplied electricity to HL&P during the fuel reconciliation period.

TIEC makes an additional unfounded leap in logic by asserting that ***any*** market energy price above the supplier's actual cost of production is a capacity cost. *PFD at 3-4.* That is inconsistent with evidence in the record. While sellers may attempt to price their products

above their cost of production, any energy premiums they are able to achieve are simply a normal part of price formation in deregulated energy markets. *CNP Ex. 5 at 9:15-16 (Graves Reb.).* ***Such energy premiums do not represent capacity.*** *CNP Ex. 5 at 6:8-10 (Graves Reb.) ("[t]he [excess values above production cost] have no relationship to either the presence or absence, or cost or value, of capacity").* TIEC again provides no citations to the record supporting its assertion. The assumption that any amount in excess of production costs constitutes a capacity payment is utterly antithetical to the realities of a competitive wholesale market as envisioned by PURA. It also contradicts TIEC's own witness, who asserted that characteristics such as the reason for the purchase and the nature of the delivery (i.e., firm and on-peak) were important characteristics of a capacity purchase. *TIEC Ex. 3 at 3:18-4:6 (Pollock Supp. Dir.).*

TIEC's attempt to use the buyer's heat rates to compute the supplier's costs leads to arbitrary and unreasonable results. In the deregulated market, any given seller will make sales to a number of different buyers at the same market price and at the same time. Under TIEC's approach, the seller's production costs for each of these sales would be deemed to be different because in each case the deemed production cost would be dependent on the historical operating costs of the ***buyer*** and not on the actual production costs of the ***seller***. TIEC's method would impute such differing production costs to a single seller even if all of the electricity was produced from the same source and the same time and thus had identical actual production costs.

It is clear why TIEC does not want the Commission to accept the 20,000 Btu/kWh heat rate that is consistent with their original proxy price theories. Doing so eliminates almost two-thirds of TIEC's proposed "imputed capacity" disallowance, reducing it to approximately $8 million. *PFD at 26; CNP Ex. 13 at 13:3-5 (Mitcham Supp. Reb.).* However, the higher heat rate

more accurately reflects the true marginal energy cost of the purchasing utility's least efficient units and is, therefore, the only option supported by the record that is consistent with TIEC's and OPC's underlying theories.

The TIEC and OPC methodologies are simply mathematical contrivances for disallowing a substantial part of the prices paid by utilities to obtain necessary supplies whenever ***market*** prices (the appropriate bench mark in a competitive market) increase above the level TIEC or OPC views as an appropriate ***average*** price (the benchmark in the old, regulated wholesale market). Indeed, using the assertions in TIEC's exceptions, they amount to a method of disallowing buyer's costs of needed supplies to the extent that the seller made any profit above the seller's theoretical fuel cost. The two methodologies use the same formula, they differ only in the contracts to which they are applied (TIEC limited the number of contracts) and the proxy price used (TIEC used a lower proxy price than OPC because it assumed a much lower heat rate). Using the same heat rate under both the OPC and TIEC methodologies illustrates the problem with OPC's decision to focus exclusively on price. *See CNP Exceptions at 22-23.* At the more reasonable 20,000 heat rate, OPC's methodology - based on price alone without regard to the purpose or nature of the purchase - results in a proposed disallowance that is more than double the proposal of TIEC – applied only to firm, on-peak transactions. Neither methodology, however, produces an "imputed capacity" amount that bears any relation to the actual cost of capacity.

IV. OUT OF MERIT REPLACEMENT CAPACITY (OOMC)

CenterPoint agrees with Staff's exceptions on this issue.

V. JOINT OPERATING AGREEMENT (JOA)

Under the Joint Operating Agreement (JOA) between HL&P and City Public Service Board of San Antonio (CPS), HL&P customers received and consumed over 13 million MWhs of electricity generated by CPS. *PFD FOF No. 62.* Even accepting (for the sake of argument) the adjusted benefits proposed by COH and the PFD, the JOA saved HL&P ratepayers nearly $14 million. *COH Ex. 18 at DSN-17 (Norwood Dir.) ($139 million x 10%).* Through sleight of hand, the City of Houston attempts to draw the Commission's attention away from the benefits obtained by HL&P for its customers through the JOA and, by means of this misdirection, to finagle a wholly unjustified $34.3 million disallowance. The ploy begins with COH's assertion that marginal variable cost (MVC) payments by HL&P to CPS under the Production Cost Adjustment (PCA) provision of the JOA "have little to do with actual incurred costs and are merely negotiated amounts." *COH Exceptions at 2.* In fact, COH has always acknowledged that HL&P actually made the MVC payments to CPS and thereby ***actually incurred*** the cost.

> During the reconciliation period, the Company ***made payments*** of $320 million to CPSB . . . under the Production Cost Adjustment provision of the JOA. The City recommended that $34.3 million of these ***expenses*** be disallowed.

COH Exceptions at 2 (emphasis added).

The real basis for COH's proposed disallowance of $19.3 million in MVC payments is that they represent ***negotiated*** payments to CPS for *CPS's* non-fuel costs of providing electricity to HL&P's customers. Well, of course they do. The fact that a price is ***negotiated***, however, has nothing to do with whether it is ***reasonable*** – the standard for recovery in this proceeding. All purchased power prices are the result of negotiation between the seller

and buyer. The only difference is that under the JOA, Mr. Norwood and the Commission have far more information regarding the basis for the negotiated price than is usually available.

Mr. Norwood repeatedly and incorrectly states that HL&P could have achieved benefits similar to those under the JOA by simply purchasing block power from third parties. *COH Ex. 18 at 33-34 (Norwood Dir.).* Had HL&P followed Mr. Norwood's recommended course, HL&P still would have paid those third parties a ***negotiated*** price for power. Any seller of purchased power would price its product to recover the non-fuel variable costs of generating that energy, yet Mr. Norwood was unable under cross examination to point to a single case in which the Commission had removed from eligible fuel purchase power costs associated with a ***seller's*** underlying costs. *Tr. at 192:23-193:3 (Norwood); and see Tr. at 411:16-19 (Falkenberg) (stating that the fixed costs of a* ***supplier*** *are "not really relevant") (emphasis added).*

COH wants so badly to shift the Commission's attention away from the reasonable payments HL&P actually made to CPS to secure the undisputed benefits of the JOA and toward an irrelevant debate over what CPS's actual costs might have been that it distorts the Commission's own rules to do so. COH argues that MVC payments are not eligible because P.U.C. SUBST. R. 25.236(a)(1) prohibits a utility from recovering in eligible fuel "costs incurred after fuel is delivered to the generating plant site, for example, but not limited to, operation and maintenance expenses." *COH Exceptions at 2-3.* Rule 25.236(a)(1), however, applies to a company's ***own*** non-fuel O&M costs, and does not preclude the utility from fully recovering the cost of purchased energy that has been priced by the seller to recover non-fuel O&M costs incurred ***by the seller***. *PFD at 37.* Mr. Norwood admitted on cross-examination that the fuel rule does not require the Commission to look behind a purchased power price and attempt to

discover whether some portion of the price was for non-fuel O&M. *See Tr. at 192:23-193:3 (Norwood).*

As the PFD correctly notes, CenterPoint provided as evidence HL&P's own NEP tariff, which included a $1.20/MWh charge for variable costs incurred by qualifying facilities (QFs) supplying non-firm energy to HL&P; and the Commission not only approved the tariff, but also routinely allowed HL&P to recover the associated expense through eligible fuel. *CNP Ex. 12 at 23:15-18 (Mitcham Reb.); and see, Tr. at 178:6-24 (Mr. Norwood stating he doesn't know whether O&M portion of NEP tariff recovered in eligible fuel) and 187:25-188:3 (Mr. Norwood admitting that in Docket No. 8425, NEP expenses appear to be included in fuel expense used to set fuel factor); and see, CNP Ex. 10 at 17:8-16 (Thomas Supp. Reb.) (both the "fuel payment" and "firm energy payment" under HL&P's FEP Tariff for QFs have been included in reconcilable fuel since at least 1987).* The Commission should accept the PFD's analysis of this issue and reject COH's sleight of hand.

COH points to the recent decision in TNMP's fuel reconciliation case (Docket No. 27576) to support its proposed disallowance of HL&P's MVC payments to CPS. The two disallowances in that case, however, were made on different grounds. Indeed, the analysis in the Docket No. 27576 PFD ***supports*** recovery of HL&P's MVC payments to CPS. The TNMP PFD reviewed O&M charges in two contracts: a Power Supply and Services Agreement with Constellation and a purchased power contract with Panda. *TNMP PFD at 53-59 (Constellation contract) and 68-70 (Panda contract).*

Under the Constellation contract, TNMP paid Constellation a $1.88/MWh O&M charge as part of the agreements. *Id. at 53.* Cities, using Mr. Norwood as their witness, challenged the costs on two grounds: (1) that Rule 25.236(a)(1) precluded such costs and (2) that

the costs were already being recovered in TNMP's base rates. *Id. at 53.* On the first ground, the PFD found that energy prices generally recover variable costs and that, because the O&M charge in question was a variable O&M rate, it could be properly included in fuel expenses.

> . . . [C]apacity prices traditionally recover the capital and fixed operational costs and the energy price recovers variable costs, including fuel. In the Constellation contract, TNMP is paying a variable O&M rate: ***the variable nature of the rate preponderates in favor of finding that it is properly included in fuel expenses.*** This conclusion, however, does not solve the double-recovery problem Cities allege.

Id. at 57 (emphasis added and footnotes omitted). Nevertheless, the PFD went on to find that the O&M charge should be disallowed on the second ground, because it covered services previously provided by TNMP's own in-house Power Resources Department, for which TNMP was already compensated in base rates. *Id. at 58.* The MVC component of the PCA payments by HL&P to CPS is for CPS's ***variable*** costs of providing power and, therefore, eligible for inclusion in fuel expense under the rationale of the TNMP PFD. Unlike the TNMP contract, the JOA does not farm out a service previously performed in-house and compensated by base rates, so the double recovery issue presented by the TNMP Constellation contract does not exist with the JOA. Moreover, as COH's inability to cite the record makes clear, there is ***no evidence*** in this docket to support a contrary position.

Under the Panda contract, the PFD found that the $2.60/MWh O&M adder was for ***fixed*** costs and therefore not appropriate for inclusion in fuel. *Id. at 69-70 and 91 (FOF No. 105 stating that the adder "recovers fixed operations and maintenance charges").* That holding is not applicable to the ***variable*** cost adder in the JOA, which covers "recognizable but difficult-to-quantify variable costs." *See, COH Ex. 18 at 00503 (DSN-1, JOA section 1.20) (Norwood Dir.).* Indeed, the TNMP PFD again ***supports*** inclusion of variable cost components in eligible fuel. *Id.*

Indeed, COH's entire "double recovery" argument is specious. CenterPoint is not seeking to recover HL&P's ***own*** O&M costs in this proceeding. Rather it seeks to include in eligible fuel payments made to CPS that covered CPS's ***variable*** costs of providing energy. It is very important to remember, moreover, that the CPS power was dispatched to HL&P only because (even with the MVC payments) doing so was less expensive than relying on HL&P's own generation. To deny CenterPoint recovery of these costs, which lowered costs for HL&P's customers, would be very poor public policy. Moreover, as discussed in CenterPoint's Exceptions to the PFD at 14-18, the annual report process protects ratepayers against any possible double recovery.

COH next proposes to disallow $15 million in PCA payments on the grounds that CenterPoint "did not provide or have access to CPSB fuel invoices, fuel audits or other evidence to support payments it made to CPSB for estimated fuel expenses it incurred under the JOA." *COH Exceptions at 4.* Note first that COH again chooses to ignore the fact that the JOA – even using Mr. Norwood's own figures – saved HL&P's customers nearly $14 million. Instead, COH again tries to draw the Commission's attention away to ***CPS's*** costs. Even so, COH is wrong. The PCA payments were based on CPS's actual fuel costs. Ms. Mitcham testified that HL&P reviewed and summarized all of CPS's fuel contracts to determine CPS's fuel prices and used the same fuel prices to calculate the PCA payments that it used in the joint dispatch system. *CNP Ex. 12 at 19:16-18 (Mitcham Reb.).* Moreover, as part of the JOA cost reconstruction process, the calculated fuel costs were periodically trued-up against CPS's actual fuel costs. *Id. at 19:18-20.* Copies of CPS's fuel contracts and/or HL&P's summaries of those contracts, as well as fuel cost true-up documents, were all included in the material made available for review in this docket. *Id. at 19:18-22.* No witness for any party has testified that HL&P incorrectly interpreted

the pricing under CPS's contracts, that the fuel prices in those contracts were unreasonable, or that HL&P failed to use the correct prices. The PFD correctly concluded that the fuel portion of the PCA payments was adequately supported by the record.

COH also argues that "the level of energy 'purchased' by the Company from CPSB, which establishes the level of the non-fuel PCA charges at issue, is improperly calculated and greatly overstated." *COH Exceptions at 4-5.* According to COH, this overstating of CPSB power consumed by HL&P customers is the result of not including short-term transactions in the stand-alone case (Study S). *Id. at 5.* COH provides ***no citations*** to the record to support this argument, because neither COH nor any other party raised this argument in testimony or in briefs. On that basis alone, it should be disregarded at this stage of the proceedings.[6] Moreover, COH gets things ***exactly backward***, because the new allegation is premised on an erroneous assumption about how the inclusion of short-term transactions in Study S would affect the PCA calculations under the JOA. COH proposed, and the PFD erroneously adopted, a $46.8 million disallowance based on the hindsight claim that short-term transactions should have been included in Study S. *PFD at 43-44.* If, as COH witness Mr. Norwood originally testified, including short-term transactions in Study S would have ***decreased*** the calculated ***benefits*** under the JOA, then it would have ***increased*** the calculated PCA ***payments*** from HL&P to CPS.

JOA benefits are the difference between the higher combined costs of stand-alone operations (CPS Study S costs and HL&P Study S costs) and the lower combined costs of joint operations (total costs under Study J). *CNP Ex. 1 at 130:3-10 (Mitcham Dir.); COH Ex. 18 at 00061 (Norwood Dir.) (JOA Section 5.1).* A benefit only exists, therefore, when the combined Study J is ***lower*** than the combined Study S. If one modifies Study S to include some assumed

[6] CenterPoint has already explained that, regardless of its hindsight effects, HL&P's decision to agree to JOA pricing that did not account for short-term, third-party transactions was reasonable at the time. *CNP Exceptions at 31-34.*

level of savings from stand-alone, third-party transactions, then the Study S costs decrease, and the difference between Study S and Study J (the JOA benefit) also decreases.

On the other hand, the additional costs to CPS of supplying power to HL&P are calculated based on the difference between CPS's stand alone costs operating by itself (CPS Study S) and the amount CPS spent under joint operations (CPS Study J). *See, COH Ex. 18 at 00061 (Norwood Dir.) (JOA Section 5.1.1).* CPS receives PCA payments for its fuel and other marginal variable costs only when the CPS Study J costs are ***higher*** than the CPS Study S costs. *See, COH Ex. 18 at 00053 and 00061 (Norwood Dir.) (JOA Section 1.26, defining "PCA" and JOA Section 5.1.2 stating, "If CPS's Study J costs exceed its Study S costs, Houston will compensate CPS by the amount of the increase through a Production Cost Adjustment").* Therefore, if stand-alone, third-party transactions (purchases and/or sales) are assumed in Study S to lower CPS's overall stand-alone costs (as COH advocates), then the CPS Study S costs move further away from the CPS Study J costs and the Production Cost Adjustment paid to CPS as a result of joint operations increases, not decreases as suggested by COH.

HL&P negotiated a joint dispatch agreement that obtained over 13 million MWhs of electricity for HL&P's customers and saved those customers, even according to the analysis provided by COH's own witness, nearly $14 million in the process. Those are the facts upon which the Commission should focus. To allow COH to create an irrelevant debate regarding the costs of HL&P's ***supplier*** will lead to a result inconsistent with the Commission's own rules and inconsistent with sound policy.

VI. CONCLUSIONS

For the reasons listed above, the Commission should disregard the exceptions filed by TIEC and COH.

VII. FINDINGS OF FACT AND CONCLUSIONS OF LAW

Please see CenterPoint's initial exceptions.

March 25, 2004

Respectfully submitted,

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CERTIFICATE OF SERVICE
SOAH Docket No. 473-02-3473
PUC Docket 26195

I hereby certify that a true and correct copy of the foregoing document was hand delivered, electronic mail or sent by overnight delivery or United States first class mail to all parties this 25th of March 2004.