**SOAH DOCKET NO. 473-00-1014**
**PUC DOCKET NO. 22349**

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| **APPLICATION OF TEXAS-NEW MEXICO POWER COMPANY FOR APPROVAL OF UNBUNDLED COST OF SERVICE RATE PURSUANT TO PURA § 39.201 AND PUBLIC UTILITY COMMISSION SUBSTANTIVE RULE § 25.344** | §<br>§<br>§<br>§<br>§<br>§ | **BEFORE THE STATE OFFICE**<br><br>**OF**<br><br>**ADMINISTRATIVE HEARINGS** |

# TEXAS-NEW MEXICO POWER COMPANY'S PROPOSED FINDINGS OF FACT AND CONCLUSIONS OF LAW

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## TEXAS-NEW MEXICO POWER COMPANY'S PROPOSED FINDINGS OF FACT AND CONCLUSIONS OF LAW

TNMP proposes the following findings of fact and conclusions of law with respect to its ECOM calculation. TNMP respectfully requests that these findings of fact and conclusions of law be adopted in this docket.

Respectfully submitted,

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**CERTIFICATE OF SERVICE**

Counsel for Texas-New Mexico Power Company certifies that a copy of this document was served on all parties of record in this proceeding on December ___, 2000 by hand delivery, facsimile, or United States mail, postage pre-paid.

____________________________________
Louis S. Zimmerman

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# TEXAS-NEW MEXICO POWER COMPANY'S PROPOSED FINDINGS OF FACT

## Procedural History

1. On March 31, 2000, TNMP filed with the Public Utility Commission of Texas ("Commission") an Unbundled Cost of Service Rate Filing Package ("UCOS-RFP"). The filing was assigned PUC Docket No. 22349.
2. On April 3, 2000, the Commission referred PUC Docket No. 22349 to the State Office of Administrative Hearings ("SOAH") for the assignment of an Administrative Law Judge to conduct a contested case hearing and issue a proposal for decision ("PFD"). The matter was assigned SOAH Docket No. 473-00-1014.
3. TNMP filed its Supplemental ECOM Filing ("Supplemental Filing") on August 28, 2000.
4. The hearing on the merits was conducted in phases. The hearing phase to determine TNMP's estimated stranded costs began on October 11, 2000 and concluded on October 17, 2000.
5. In addition to the Commission Staff, the following intervenors participated in the stranded cost phase of Docket No. 22349: Office of Public Utility Counsel ("OPC"); Texas Industrial Energy Consumers ("TIEC"); and Coalition of Cities ("Cities").
6. On September 5-6, 2000, OPC, Cities, and TIEC filed Motions to Strike Portions of TNMP's Supplemental ECOM filing. These motions were denied by Order No. 11.
7. On October 2, 2000, TNMP filed a Motion to Strike Portions of TIEC's, OPC's, Cities', and Staff's Testimony regarding accelerated depreciation and negative stranded cost. This motion was denied by Order No. 12.
8. On October 10, 2000, Staff filed a Motion to Strike TNMP Witness Kevin Buffington's testimony asserting it was improper rebuttal testimony. This motion was granted during the ECOM hearing. TNMP made an offer of proof of Mr. Buffington's testimony.

## The ECOM Model

9. TNMP utilized the ECOM Model described in PURA §39.262(i), that being the model described in the Commission's April 1998 Report To The Texas Senate Interim Committee on Electric Restructuring entitled "Potentially Strandable Investment (ECOM) Report: 1998 Update." ("1998 Report").

10. The historical test year used in the UCOS-RFP began on October 1, 1998 and concluded on September 30, 1999.

11. TNMP made no modifications to the ECOM Model from the 1998 Report.

12. In accordance with the requirements of Commission Orders No. 14 and 22, TNMP filed company-specific changes, updates, and corrections to its May 31, 2000 Initial Filing. Those updates and corrections were as follows:

    a. Updated market prices for gas, as provided in Order No. 22.
    b. Change in the A&G escalator (4.0% to 1.5%), as provided in Order No. 22.
    c. Inclusion of Investment Tax Credits, as provided in Order No. 14.
    d. Elimination of TNP One post-retirement years (2030-2035), a correction of error in the original filing.
    e. Change in Rate of Return to amount authorized (10.0% to 10.53%), as provided in Order No. 14.
    f. Correction/Change in the escalators for Taxes Other Than Income Taxes as provided in Order No. 14.
    g. Correction/Change in the heat rate for TNP One (a five year average consistent with the capacity factor), a correction to the original filing.
    h. Change in fuel costs reclassified in the base year but erroneously not forecasted ($1.6 million of Non Reconcilable Fuel), a correction to the original filing.
    i. Updated estimates for excess earnings for 2000 and 2001, as provided in Order No. 14.

13. These company-specific changes, updates, and corrections to inputs were properly made by TNMP and must be taken into account in the ECOM Model.

14. TNMP used inputs that are relevant to the operation of TNP One as if it were to be operated in a regulated environment in accord with the 1998 Report and Commission Order No. 14.

15. There were challenges made to certain inputs in TNMP's Supplemental Filing, as described below.

16. All other inputs made by TNMP in the ECOM Model in its Initial and Supplemental Filings were supported by TNMP, were unchallenged, are reasonable, and are consistent with Commission Orders No. 14 and 22.

17. TNMP was a utility with positive ECOM in the "base case" in the 1998 Report.

**Challenged Inputs**

18. Capacity Factor/Heat Rate. A capacity factor of 81.5% and a heat rate of 11,500 btu/kwh is reasonable.

    a. The capacity factor/heat rate must be evaluated in the context of TNP One operations in a regulated environment.

    b. As a regulated entity, TNMP must:

        i) Satisfy its obligation to serve and

        ii) Supply ancillary services.

c. TNMP must make provision for ancillary services in a regulated environment. TNMP has been unable to contract for future delivery of adequate ancillary services in ERCOT today. It is not reasonable to assume that ancillary services will be available in the market in the future, particularly when assuming a continued regulated environment. Thus in calculating TNP One's capacity factor, TNMP's obligation to provide ancillary services must be taken into account.

d. The estimated 81.5% capacity factor is consistent with TNP One's five-year historical average capacity factor.

e. The estimated 81.5% capacity factor is higher than the capacity factor would be if TNMP accounted for all ancillary services provided by TNP One.

f. The heat rate is a function of plant operation. The higher the capacity factor, the lower the heat rate. Based on TNP One's historic operations, a heat rate of 11,500 btu/kwh is appropriate for a capacity factor of 81.5%.

19. Changes in Escalators for Taxes other than Income Taxes.

a. Property Taxes.

i) A 3.0% property tax escalator was included in the preliminary ECOM runs TNMP presented to the Commission. The "base case" in the 1998 Report prepared by the Commission includes a 3.0% escalator. TNMP erred in not including this escalator in its Initial ECOM Filing. TNMP properly corrected the error in its Supplemental Filing.

ii) TNMP property tax expense is a function of the tax rate ($ per $100 of appraised value) and the appraised value.

iii) The tax rate applicable to TNP One has increased at an annual rate of 7.1% over the five (5) year period commencing with 1994.

iv) The appraised value for TNP One has fallen since 1996. The appraised value is not anticipated to fall further.

v) While the tax rate has increased, the declining assessed value has caused TNMP's tax expense to decline.

vi) TNMP has reasonably projected that the assessed value will not continue to fall.

vii) Since the appraised value of TNP One has reached its approximate market value, the property tax expense will increase due to changes in the tax rate and/or assessed value.

viii) TNMP has reasonably projected that the TNP One tax expense will increase by 3%.

b. Other Taxes.

i) "Other taxes" include ad valorem taxes, Texas Franchise taxes, Texas gross receipts taxes, Texas street rental fee expenses, Texas PUC assessment, payroll taxes, and Texas Use taxes.

ii) TNMP included a 3.0% escalator in its report to the Commission underlying the Commission's 1998 Report. The "base case" in the 1998 Report prepared by the

Commission includes a 3.0% escalator. TNMP included a 2.8% escalator in its Initial Filing and made a company-specific change to 3.0% in its Supplemental Filing.

iii) Intervenors assume in the calculation of revenues upon which "other taxes" that TNMP would not replace its purchased power contracts in a regulated environment. In a regulated environment, which must be assumed here, TNMP will have a continuing obligation to serve, and thus must have sufficient purchased power resources to meet existing and future demands for service.

iv) TNMP has reasonably projected that these tax expenses will continue to increase by 3%.

20. Consolidated Tax Adjustment. TNMP's calculation of federal income tax expense on a stand-alone basis was appropriate.

a. TNMP calculated its federal income tax liability for regulatory purposes on a stand-alone basis.

b. TNMP calculates its income tax liability on a consolidated basis at the holding company level, offsetting losses incurred by non-utility affiliates with earnings of TNMP. The resulting federal income tax liability at the holding company level is reduced.

c. The Commission has repeatedly approved TNMP's stand-alone methodology, which does not take consolidated tax savings into account.

d. It is not reasonable to overturn years of Commission precedent as to TNMP for purposes of calculating ECOM.

e. There is no provision (*i.e.* input variable) for inclusion of consolidated tax savings in the ECOM Model and no Commission order requires that they be taken into account.

21. Lignite Escalation Factor. TNMP's use of a 2.5% escalator for lignite fuel cost was reasonable.

a. TNP One lignite is supplied under a contract with the Walnut Creek Mining Company ("WCMC"). The term of this contract extends until 2022.

b. The Commission-approved 1.3% generic escalator for natural gas does not provide a proper basis upon which to determine escalation under the WCMC contract, which is governed by its own terms.

c. It is necessary to develop escalation factors for lignite using the contract terms.

d. Price indicators developed using the terms of the WCMC contract support an estimated 2.5% escalator.

22. Accelerated Depreciation Under S.B. 7/TNMP Commitments. TNMP has appropriately not included accelerated depreciation in its calculation of ECOM.

a. The Transition Plan approved by the Commission in Docket No. 17551 provides that TNMP shall take $15 million in accelerated depreciation in 1999, 2000, 2001, and 2002. The Transition Plan also provides that obligations under its terms will expire on the date that competition under any legislation permitting retail competition commences. Under S.B. 7, the competition date is January 1, 2002.

b. The Transition Plan also provides that TNMP must conform its terms to the terms of any legislation permitting retail competition in Texas. S.B. 7 was that legislation.

c. The Commission has ordered that it will review how TNMP has conformed the Transition Plan to S.B. 7 in a proceeding in 2001 and the Commission will take such action as it deems necessary at that time. Therefore, this issue should not be considered in this docket.

d. TNMP did not record $15 million accelerated depreciation in 1999 and has not projected doing so in 2000 or 2001.

e. TNMP has estimated its excess earnings for purposes of the ECOM Model in accordance with the methodology specified in S.B. 7.

f. If TNMP were to record $15 million in accelerated depreciation, its estimates of excess earnings would decline.

g. Reducing ECOM for accelerated depreciation and not reducing excess earnings "double counts" the accelerated depreciation.

23. <u>Excess Earnings Calculation</u>. For purposes of ECOM, TNMP properly estimated excess earnings of $21,938,000 for 1999, $18,028,000 for 2000, and $11,145,000 for 2001.

a. TNMP's estimates of revenue and federal income taxes used in the estimation of excess earnings were consistent with normal estimation methodologies, taking into account weather adjustments, customer growth, and Commission-mandated rate reductions.

b. The cost of capital used by TNMP in the calculation of excess earnings was that approved by the Commission in Docket No. 10200. Docket No. 10200 was the last docket in which a cost of capital was specifically approved.

c. TNMP's reported excess earnings for 1999 were $21,949,819, which is very close to its estimated excess earnings of $21,938,000, which supports the accuracy of TNMP's methodology.

24. <u>Depreciation Redirection</u>. TNMP's actions in not redirecting depreciation were reasonable.

a. TNMP has not yet used depreciation redirection as an ECOM mitigation tool.

b. There are significant advantages to both TNMP and its ratepayers if TNMP can use securitization rather than depreciation redirection to mitigate ECOM.

c. TNMP will not be able to determine whether it can reasonably securitize until the Commission determines its ECOM.

d. Given TNMP's size and its estimated ECOM, TNMP cannot get the advantage of securitization if the Commission mandates depreciation redirection at this time.

e. If TNMP is unable to take advantage of securitization, it will be able to redirect depreciation at a later date and the CTC charge would be adjusted.

25. Rate of Return/Capital Structure With Alternative Recommendation. TNMP was reasonable in using a 10.53% cost of capital in the ECOM Model.

    a. The UCOS-RFP Guidelines provided a 10% rate of return.

    b. Order No. 14 stated that company-specific inputs from a utility's last rate case should be used.

    c. TNMP's rate of return in its last rate case in which a rate of return was approved was 10.53%.

26. Excess Accumulated Deferred Federal Income Tax. TNMP has no excess ADITs related to TNP One.

27. Inclusion of Investment Tax Credits. TNMP has complied with Order No. 14 by offsetting ITC against the income tax expense in the ECOM Model.

28. ECOM Amount. The proper ECOM amount for TNMP is estimated at $194.4 million.

**Development Of Competition Transition Charge (CTC).**

29. It is reasonable to find that the Legislature intended for ECOM resulting from the ECOM Model to be the estimate of stranded costs for purposes of calculating a CTC charge.

30. Conversion of PVRR to Rate Base Amount. This proposed adjustment is rejected because it is not provided for in the statute or the ECOM Model.

31. Discount Rate/Carrying Charge on CTC Revenue Stream. TNMP's proposed carrying charge of 9.11% is reasonable.

    a. TNMP sought a 9.11% cost of capital in its UCOS Filing.

    b. TNMP's rate of return of 9.11% was based in part on a debt/equity ratio of 60%/40% and a return on equity of 11.50%. [Recently, the Commission has approved a capital structure of 60%/40% and a return on equity of 11.25%.]

    c. There are collection and recovery risks related to collecting the CTC charge and recovering stranded costs. The cost of equity must exceed the cost of debt because debt holders have priority over equity owners to the assets of the company. Therefore, setting the cost of capital at a level equivalent to the cost of debt as proposed by Intervenors is unreasonable.

32. CTC Structure/Negative CTC. TNMP has mitigated ECOM by applying excess earnings to reduce stranded costs. TNMP has positive ECOM after accounting for the above mitigation.

33. CTC Structure/CTC Recovery Period and Pattern. TNMP's use of ten (10) year straight line amortization period is reasonable.

## TEXAS-NEW MEXICO POWER COMPANY'S PROPOSED CONCLUSIONS OF LAW

1. The Commission has authority to determine rates for TNMP's transmission and distribution utility pursuant to PURA §39.201.

2. The ECOM Model.

   a. PURA §39.261 requires an electric utility to use the ECOM administrative model referenced in PURA §39.262 to determine estimated stranded costs.

   b. TNMP has complied with the ECOM modeling process as provided in the UCOS Filing package.

   c. TNMP has complied with Commission Orders 14, 22, and 24 from Docket No. 22344.

   d. In calculating ECOM, the parties are required to assume a continued regulated environment.

3. Capacity Factor

   a. As a regulated entity, TNMP must both satisfy its obligation to serve and supply ancillary services

4. Consolidated Taxes Adjustment.

   a. The use of a stand-alone tax savings methodology, as approved by the Commission in TNMP Docket Nos. 10200 and 12900, is consistent with S.B. 7.

   b. No provision in the ECOM Model nor any Commission Order requires consideration of consolidated tax savings.

5. Accelerated Depreciation.

   a. Consideration of the application of the accelerated depreciation provision in the Transition Plan, approved in Docket No. 17551, should be deferred to the Commission mandated proceeding in 2001.

6. Excess Earnings.

   a. The method for calculating excess earnings is mandated by PURA §39.258.

   b. "Cost of Capital," as defined by PURA §39.258(7), refers to the cost of capital determined in a utility's last rate case in which the cost of capital was specifically adopted.

   c. Under PURA, a company must use the above cost of capital to calculate excess earnings.

   d. TNMP's last rate case in which a cost of capital was determined was Docket 10200.

7. Depreciation Redirection.

   a. PURA allows a utility to redirect depreciation at any time until the True-Up date.

   b. Under PURA, TNMP cannot be required to redirect depreciation for purposes of determining ECOM.

8. Inclusion of Investment Tax Credits. TNMP has included ITC as required by Order No. 14.

9. Conversion of PVRR to Rate Base Amount.

a. Under PURA, the 1998 Report to the Legislature, and the ECOM Rate Filing Package, the ECOM Model calculation is an administrative estimate for stranded costs.

b. Under PURA, the 1998 Report to the Legislature, and the ECOM Rate Filing Package, a conversion of the ECOM Model calculation to a "rate base amount" is inappropriate.

10. Negative CTC. The Commission is not authorized under the statute to apply a negative CTC. There has been no excessive mitigation to support application of a negative CTC.

11. ECOM Amount. TNMP ECOM is estimated at $194.4 million.

12. CTC Charge. TNMP's Competition Transition Charge shall be determined in a later phase based on the Stipulation of the Parties.