



Control Number: 28813



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State Office of Administrative Hearings



Shelia Bailey Taylor
Chief Administrative Law Judge

May 6, 2005

Mr. Stephen Journeay
Director, Office of Policy Development
Public Utility Commission of Texas
William B. Travis State Office Building
1701 N. Congress, 7th Floor
Austin, Texas 78701

Courier Pick-up

RE: SOAH Docket No. 473-04-3554
PUC Docket No. 28813

Petition to Inquire into the Reasonableness of the Rates and Services of Cap Rock Energy Corporation

Dear Mr. Journeay:

We have read and considered the exceptions and replies filed in the above-referenced case. Most of the exceptions are similar to the arguments raised at the hearing and in the parties' closing briefing and, thus, do not require a response from us. However, we do find it appropriate to address certain items to clarify both the evidentiary record and our recommendations. Therefore, we are providing this limited response. Generally, we address the exceptions by specific category below. However, there are two matters deserving of attention at the outset of this letter.

First, in their exceptions, a number of intervenors have challenged our conclusion that NewCorp Resources Electric Cooperative, Inc. (NewCorp) is not considered an affiliate of Cap Rock Energy Corporation (Cap Rock) under PURA or the Commission's rules. These intervenors cite to a Final Order from last year in which the Commission found that NewCorp is an electric utility under PURA § 31.002.¹ Because the definition of electric utility under PURA § 31.002 excludes electric cooperatives, the intervenors contend that our conclusion that NewCorp is an electric cooperative, and thus not an affiliate

¹ *Application of NewCorp Resources Electric Cooperative, Inc. To Transfer Certificate of Convenience and Necessity from NewCorp Resources, Inc.*, Docket No. 29370, Final Order at 3 (June 15, 2004).

of Cap Rock, is erroneous. **We wish to stress that the first time the intervenors raised this argument was in their exceptions to the PFD. At no time prior to issuance of the PFD did any party cite to that prior Final Order contending that it was dispositive of the affiliate issue, nor did any party raise this argument during the hearing or in their closing briefing.** Accordingly, the ALJs were never given the opportunity to address and consider this argument.

Further, Cap Rock contends the language from the prior Commission order was simply a mistake, resulting from the use of form language, and was not a determination made on a contested issue. Cap Rock's explanation appears reasonable. Ultimately, we decline to rely on that sole conclusion of law to revise our recommendation in this case. However, the Commission can choose to give the conclusion of law whatever weight it deems appropriate. If the Commission determines that its prior finding that NewCorp is an electric utility under PURA § 31.002 means that NewCorp is not an electric cooperative, then it may properly conclude that NewCorp is an affiliate of Cap Rock.

As a second initial matter, we note that Cap Rock has excepted to the number-running process and, more specifically, to alleged discrepancies between the Proposal for Decision (PFD) and the number-running calculations prepared by Staff. If possible, we address those exceptions in this letter. However, in most instances, we are unable to address the exceptions because the matters were not contested issues at the hearing, and they require technical or regulatory accounting knowledge or experience. For example, in many instances the parties argue over the "attendant" effects of a specific recommendation we make in the PFD. Often, the first time these attendant effects have been discussed is through exceptions to the PFD. Without the assistance of a regulatory accounting expert or additional evidence in the record, we are not in a position to offer a recommendation on such attendant effects.

This scenario highlights one of the difficulties of the number-running process. Because we lack the technical expertise necessary to conduct number-running, we rely on Staff to make all attendant adjustments that might clearly and ordinarily flow from our specific recommendations. On the other hand, number-running Staff feel constrained in making adjustments that are not clearly delineated by us. This results in the present situation where there are a number of additional adjustments that will need to properly be made to final numbers, but where we are not in a position to make a recommendation on those numbers because they were not specifically contested before us and the parties did not present evidence and arguments on them. Therefore, our response to exceptions should be understood in that context.

Invested Capital and Rate Base

Working Cash Allowance

Cap Rock argues in its exceptions that working cash allowance is impacted by the reclassification of work orders from plant to operating and maintenance expenses. The ALJs agree that the reclassification of work orders may have an impact on working cash allowance and, accordingly, adjustments to working cash allowance would be appropriate. Staff can appropriately make this adjustment in revised number-running conducted for the Commission to implement final rates.

Accumulated Deferred Income Taxes

Cap Rock argues in its exceptions that its accumulated deferred income taxes also are impacted by the reclassification of work orders from plant to operating and maintenance expenses. The ALJs agree that the reclassification of work orders may have an impact on taxes and, accordingly, adjustments to accumulated deferred income taxes would be appropriate. Staff can appropriately make this adjustment in revised number-running conducted for the Commission to implement final rates.

Operating and Maintenance Expenses - Compensation and Benefits

Cap Rock argues in its exceptions that the \$174,000 annual payment to its general counsel, Ronnie Lyon, includes not just his salary but also his office expenses and his legal assistant's salary. The ALJs agree with Cap Rock's exception. Therefore, Finding of Fact No. 126 should be revised to read: The base salary of \$174,000 paid to Cap Rock's General Counsel, Ronnie Lyon, is reasonable and necessary and is properly included in the cost of service because it covers his salary, office expenses, and the salary of his legal assistant.

Cap Rock also excepts to the ALJs' recommendations regarding executive compensation. Cap Rock contends that the ALJs should not have reduced the total amount of executive compensation. Further, Cap Rock contends that, if the ALJs' recommendation is adopted, then 30 percent of the compensation should be allocated to NewCorp. The ALJs decline to amend the PFD to adjust the recommended amount of executive compensation. Moreover, the ALJs note that the record evidence does not support Cap Rock's assertion for allocating 30 percent of compensation to NewCorp. The evidence in the record indicates the total amount in issue was for Cap Rock's executive compensation, and did not include any portion for NewCorp. However, as Pioneer suggests in its reply to exceptions, this is a relatively straightforward matter. Because the ALJs recommend total executive compensation at no more than \$200,000, Staff may utilize this figure in conducting number-running. Accordingly, instead of reducing existing amounts by some calculation, Staff may entirely delete Cap Rock's existing executive compensation figure and replace it with the \$200,000 amount for number-running purposes.

Purchased Power

The City of Greenville (Greenville) excepts to Finding of Fact No. 34 because it uses the term "purchased power contract" to refer to the agreement between NewCorp and Cap Rock. Although Cap Rock previously purchased power from NewCorp, we have made clear in the PFD that Cap Rock currently obtains only transmission service from NewCorp. To avoid any confusion, the words "purchased power" may be deleted from Finding of Fact No. 134.

Rate Design - Commercial service at Primary Voltage

Cap Rock disagrees with the ALJs' recommendation that a discount be given to customers in the commercial class taking service at primary voltage. Cap Rock contends that no customers in the commercial class are entitled to take service at primary voltage and, instead of offering such customers a discount, Cap Rock should be allowed to move them to the proper customer class. The ALJs'

recommendation is based on the evidence in the record that Cap Rock has been providing service to commercial customers taking service at primary voltage. If Cap Rock has improperly classified and billed customers in the past, it may be entitled to properly categorize them based on its lawfully-approved tariffs and that is not a matter the ALJs address in this proceeding. Rather, the ALJs simply recommend that any commercial customers that are taking service at primary voltage should be entitled to a discount. This determination is not a specific recommendation that Cap Rock be prohibited from properly classifying customers according to its tariffs or that Cap Rock be prohibited from changing the existing classification of customers.

Rate Case Expenses

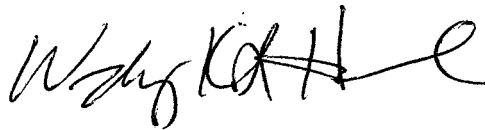
In the PFD, the ALJs found that all expenses incurred with respect to rate design should be disallowed. Staff and Pioneer indicated in their exceptions that the ALJs indicated the incorrect amount of rate case expenses spent on rate design. After reviewing the record, the ALJs agree with Staff and Pioneer that the total disallowance for rate design rate case expenses should be \$689,374. Thus, Finding of Fact No. 154a. should read: \$689,374 in expenses associated with rate design are properly disallowed, because the rate design is so flawed and unreliable as to be useless.

Any additional rate case expenses incurred for rate design as this case proceeds through the appeals process should also be denied. The ALJs are not, however, including the amount of those expenses in the total because at the close of the record in this case, those expenses were estimated.

Sincerely,



Craig R. Bennett
Administrative Law Judge



Wendy K. L. Harvel
Administrative Law Judge

cc: All Parties of Record