system sales shall not reduce the Company's reconcilable fuel costs, and the Company shall not be required to calculate any incremental costs it incurs in connection with off-system sales.

20. As part of the overall settlement of this case, a reasonable sharing from July 1, 1995 and continuing during the Freeze Period of margins on off-system sales made by affiliates or subsidiaries of the Company will allow ratepayers to receive 25% of such margins.

Compliance Orders

21. The Company has satisfactorily complied with all outstanding Commission compliance orders.

Accounting Deferrals

22. It is appropriate to adjust Palo Verde Unit 3 accounting deferrals to remove the deferred lease payments and carrying charges on Palo Verde Unit 3 plant costs. Therefore, a balance of $4,308,000 Unit 3 accounting deferrals, less $1,457,000 of related ADFIT, as of June 30, 1993, will be included in rate base and amortized by the end of the Freeze Period.

23. ADFIT related to disallowed Unit 3 deferrals should not be reflected as a reduction to the Unit 3 deferral balance.

24. It is appropriate to include Palo Verde Units 1 and 2 accounting deferrals in rate base and to amortize these deferrals by the end of the Freeze Period.

Invested Capital

25. The Company's invested capital is properly calculated as presented on Schedule A of the Order.

26. One hundred percent of Palo Verde Unit 3 is deemed used and useful and included in rate base.

27. It is reasonable to recognize for rate purposes certain assets as a mechanism to implement the intent of the Signatories that the Company's base rates during the Freeze Period will not be changed regardless of future increases or decreases in the Company's cost of service. The assets so recognized are detailed in ordering paragraphs 11, 12 and 13.

Cost of Capital

28. The reasonable cost of equity for the Company is 12.0 percent.

29. The appropriate weighted overall cost of capital is 9.14 percent.

Decommissioning Expense

30. The reasonable decommissioning expense for the Palo Verde units is reflected in Schedule C to this Order.

31. State agencies are responsible for establishing an appropriate level of decommissioning funding and the mechanism for collecting and retaining funds above the NRC minimum required amount.

32. An escalation rate of 4.30 percent, as recommended by Staff, should be used to adjust decommissioning expense for inflation.

33. Decommissioning expense should be calculated using the existing inflation-adjusted method using a 3.90 percent inflation rate and using the following investment earnings rates:

Decommissioning Funds	
1/1/1995 - 1/1/1996	5.10 percent
1/1/1996 - 1/1/2000	5.11 percent
1/1/2000 - 1/1/2001	5.72 percent
1/1/2001 - thereafter	6.20 percent

Spent Fuel Fund	
1/1/1995	5.49 percent

34. The Company's beginning fund balances for Palo Verde Units 1, 2 and 3 decommissioning funds, as described in Schedule C, are appropriate and should be used. The Company's requested D-1 allocator, 0.6998166, is reasonable to determine the Texas jurisdictional portion of the approved expenses.

Depreciation and Amortization Expense

35. Staff's proposed (i) remaining life and (ii) depreciation rates for the Palo Verde plant are reasonable. The Company's proposed depreciation rates for non-nuclear plant are appropriate.

36. Amortization of the existing Mirror CWIP over 33 years is appropriate resulting in an amortization expense for the existing Mirror CWIP asset of $1,128,000 and for the existing Mirror CWIP liability of ($698,000).

Rate Moderation Plan and Mirror CWIP

37. It is in the public interest to terminate the Docket No. 7460 RMP as of June 30, 1993, include the balance of the deferrals in rate base, and amortize them by the end of the Freeze Period. Accordingly, the amount of the RMP deferrals and existing Mirror CWIP contained in Schedule A are appropriate.

Rate Case Expense

38. Pursuant to the Stipulation, the City's rate case expenses addressed in this docket are found to be reasonable, reimbursable to the City, and are deemed recovered by the Company. The Company's rate case expenses addressed in this docket are also deemed recovered by the Company.

Jurisdictional Cost Allocation

39. The Company's use of the 12-CP method for jurisdictional cost allocation is reasonable.

40. The Company's exclusion of CFE and IID-C sales from its jurisdictional cost study is reasonable.

41. It is reasonable to allocate Accounts 519 and 520 on the basis of the Company's energy allocator.

42. The Company's non-allocation of Accounts 907-910 to FERC customers is reasonable.

43. It is reasonable for the Company to exclude amortization expense when allocating its depreciation expense.

Class Cost Allocation

44. The Company's use of the A&E-4CP methodology to allocate demand-related costs to its various customer classes is reasonable.

45. The Company's exclusion of non-firm sales from its class cost allocation process is reasonable.

Assignment of Class Allocators

46. It is reasonable to make a corresponding adjustment to the Company's class allocator to reflect the jurisdictional assignment of Account 519 and Account 520.

47. It is reasonable to classify fuel inventory as energy-related.

48. The Company's allocation of its distribution plant accounts using a non-coincident peak demand allocator is reasonable.

Revenue Distribution

49. The Company's annualization method, used to adjust the test year billing determinants for the effects of customer growth or decline, is reasonable.

Rate Design

50. The tariffs approved in connection with the Second Interim Order entered in this docket on August 2, 1995 reflect the appropriate and reasonable resolution of all cost allocation, revenues distribution, and rate design issues.

51. The Company's proposed modifications to Rate 08 are reasonable.

52. The Company's proposed changes to the Off-Peak Rider in Rate 24, as modified by Staff's recommendation to increase the energy charge, are reasonable.

53. The Company's optional demand billing service for customers taking under Rate 02 is reasonable and beneficial to the Company's customers.

54. The Company's proposed hours-use rate, which is applicable to Rate 25 customers, is reasonable.

55. The Company's separately metered rate for thermal energy storage systems under a rider to Rate 24 and Rate 25, as modified by the stipulation between General Counsel and the Company, is reasonable.

56. The Company's proposal to offer interruptible power service under Rate 27 and Rate 38 is reasonable.

57. The changes recommended by the DOD to the Company's Rate 31 are reasonable because they move the demand and energy components of the rate closer to unit costs.

58. The Company's proposal to broaden the applicability clause in Rate 33 is reasonable. The proposed tariff adequately addresses the potential for a free rider taking under this rate.

59. A 2,000 kW minimum demand level for Rate 43, as stipulated to by the State and the Company, is reasonable.

60. The changes to the Company's cogeneration rates, Rate 45, Rate 46, and Rate 47, as modified by the stipulation between the State and the Company, are reasonable.

61. The Company's changes to the tariff language in Rate 99, as modified by Staff, are reasonable.

62. The Company's proposed changes to its service rules and regulations, as modified by the uncontested recommendations of the State, Staff, and the Company's rebuttal witness, are reasonable.

63. The Company filed a notice of intent to implement rates under bond in connection with its application in this docket to change rates. The bonded rates went into effect on July 16, 1994 upon approval of the bond by the Commission's Hearings Division.

64. It is reasonable to assign no base rate increase to Rate 30 because Border Steel is currently in Chapter 11 bankruptcy and any base rate increase in Rate 30 will likely cause it to go out of business.

65. With the exception of limiting the low income rider to persons age 65 or older, it is reasonable to adopt Staff's proposed changes to the Company's low income rider. Accordingly, the low income rider program will apply to all Company residential customers who have an active service account and meet the qualifications for income assistance, as defined by the Department of Human Services.

66. Until the Company submits additional testimony in its next rate filing package concerning the removal of non-school customers, the Company's proposal to limit the applicability of Rate 41 to current non-school customers and to public school accounts, grades kindergarten through 12, is reasonable. To the extent, however, that any City or County account, which was not in Rate 41 at the time of the Commission's Docket No. 9945 Order, receives service under Rate Class 41, it is reasonable that all state agency accounts become eligible for Rate 41.

Stipulation as Settlement

67. The Stipulation, as approved by the Commission, represents a fair, just and reasonable solution to the issues being resolved. Consistent with the Stipulation and the record in this proceeding, the ten year rate freeze agreed to by the signatories to the Stipulation is in the public interest and results in just and reasonable rates. Moreover, the Stipulation will serve the purpose of moderating the rates of the Company in the Texas jurisdiction during the Freeze Period. The Stipulation reflects settlement discussions. It is recognized and agreed by the Signatories that the Stipulation is made and filed solely in connection with the compromise and settlement of rate matters related to the Company and is subject to the specific approval of the Commission of the matters therein stipulated. By entering into the Stipulation, none of the Signatories is deemed to have approved or acquiesced in any ratemaking principle, valuation methodology, method of cost-of-service determination, method of revenue calculation, or cost allocation or rate design principle underlying any of the provisions and agreements contained therein. It is the result of a unique fact situation, and its resolution is specific to the circumstances presented. The Stipulation does not prejudice, bind, or affect any Signatory, or constitute an admission, except to the extent necessary to give effect to or enforce the terms of the Stipulation or unless otherwise specifically stated therein.

Conclusions of Law

1. The Company is a public utility as defined in the Public Utility Regulatory Act of 1995, S.B. 319, 74th Leg., R.S. 1995 ("PURA") § 2.001 (formerly § 3(c)) and is therefore subject to the Commission's jurisdiction and authority.

2. The Commission has jurisdiction over this docket pursuant to PURA §§ 1.101, 2.101, 2.108, 2.201, 2.212, 2.214, 2.216 and 1.251 (formerly §§ 16, 17, 26, 37, 43, 45, 47 and 63).

3. The Applicants provided notice of this proceeding as required by PURA § 2.212 (formerly § 43) and P.U.C. PROC. R. 22.51(a).

4. The Company is a debtor-in-possession under the Bankruptcy Code and is subject to the ongoing jurisdiction of the United States Bankruptcy Court for the Western District of Texas, Austin Division.

5. The Bankruptcy Code prohibits discrimination against the debtor based on the filing of the bankruptcy, and no action taken in this proceeding violates that prohibition. 11 U.S.C. § 525.

6. Pursuant to the Stipulation, the reacquisition of the leased Palo Verde Units 2 and 3 assets is in the public interest, and the decisions attendant to the reacquisition were reasonable and prudent when made.

7. The rate filing package filed by the Company meets the requirements of PURA § 2.212(a) (formerly § 43(a)) regarding the contents of a statement of intent.

8. The Company has complied with the requirements of P.U.C. SUBST. R. 23.22 regarding energy efficiency plans.

9. One hundred percent of Palo Verde Unit 3 is used and useful.

10. As required by PURA § 2.206 (formerly § 41(a)) the net plant component of the Company's invested capital as set forth in Schedule A of the Order, is based on the original cost of property used and useful to the Company in providing electric utility service.

11. The Company must comply with P.U.C. SUBST. R. 23.21(b)(1)(F) and 23.59, which require all utilities to deposit monthly, in irrevocable trust funds external to the utility, the funds they collect from ratepayers for decommissioning.

12. The resolution of issues in this docket by the Stipulation is authorized by the Administrative Procedure Act, Tex. Gov't Code Ann. § 2001.056 (Vernon 1994) and is supported by evidence in the record. The Commission finds that the rates approved by this Order are just and reasonable and are in the public interest as specified in Conclusions of Law 13-15. Because this Order sets rates consistent with an unopposed settlement agreement among the parties, it is not necessary to resolve, and this Order does not resolve, issues that would have been presented for resolution on a contested basis. By entering this Order setting rates consistent with the Stipulation, the Commission does not approve or acquiesce in any specific ratemaking principle, valuation methodology, method of cost-of-service determination, method of revenue calculation, or cost allocation or rate design principle. This Order is the result of a unique fact situation, and the rates hereby approved are specific to the circumstances presented. This Order does not prejudice, bind, or affect the Commission in other pending or future cases except as may be appropriate to give effect to the terms of the Order.

13. The rates provided for in this Order, together with all the terms of the Stipulation, will result in overall revenue that will permit the Company a reasonable opportunity to earn a reasonable return over and above its reasonable and necessary operating expenses, within the intent of PURA § 2.203(a) (formerly § 39(a)).

14. The rates and rate design provided in this Order and the Commission's findings of fact are just and reasonable, not unreasonably preferential, prejudicial, or discriminatory, but sufficient, equitable, and consistent in application to each group of customers, as required by PURA § 2.202 (formerly § 38).

15. Rates and rate design provided in this Order and the Commission's findings of fact do not grant an unreasonable preference or advantage to any customer within a classification, subject any customer within a classification to any unreasonable prejudice or disadvantage, or establish unreasonable differences as to rates and services between localities or between classes of service within the meaning of PURA § 2.214 (formerly § 45).

16. The Company has met its burden of proof under PURA § 2.204 (formerly § 40) in demonstrating it is entitled to the level of revenue agreed to in the Stipulation.

APPLICATION OF EL PASO ELECTRIC COMPANY FOR AUTHORITY TO CHANGE RATES	**§ § §**	**PUBLIC UTILITY COMMISSION OF TEXAS**

STIPULATION AND SETTLEMENT AGREEMENT

WHEREAS, on January 10, 1994, El Paso Electric Company (the "Company") filed with the Public Utility Commission of Texas (the "Commission") (i) a petition to increase rates pursuant to Section 43 of the Public Utility Regulatory Act ("PURA"), Tex. Rev. Civ. Stat. Ann. art. 1446c (recodified as the Public Utility Regulatory Act of 1995, S.B. 319, 74th Leg., R.S. 1995), (ii) a petition to reconcile fuel and purchased power costs for the period April 1, 1989 through June 30, 1993, and to revise the Company's fixed fuel factors (the "fuel matters"), and (iii) applications pursuant to Section 63 of PURA for public interest determinations with respect to the Company's request to (a) reacquire the Palo Verde Nuclear Generating Station ("Palo Verde") leased assets and (b) merge with a utility holding company subject to certain regulatory and accounting conditions, which petitions and applications were assigned Docket No. 12700; and

WHEREAS, the Company also filed its PURA § 43 (recodified as PURA § 2.212) petition to increase rates within the City of El Paso (the "City") and other municipalities in the Company's service territory retaining original jurisdiction over the Company's rates; and

WHEREAS, the City and such municipalities have taken action concerning the Company's rates, the Company has appealed those actions to the Commission, and those appeals have been consolidated under Docket No. 12700; and

WHEREAS, on March 3, 1995, the Commission issued its Interim Order, Severance Order, and Order of Remand (the "Interim Order") in Docket No. 12700, wherein the Commission entered its Interim Order in the merger, reacquisition and rate cases and severed the fuel matters from Docket No. 12700 into a new docket, Docket No. 13966, for which the

Commission separately issued a final order, which several parties have now appealed to the Travis County District Court; and

WHEREAS, there are currently pending in the Texas courts several appeals of prior Commission dockets concerning the Company's rates, including Docket Nos. 8018, 8078, 8363, 9945 and 13966; and

WHEREAS, there are currently pending on remand at the Commission, following judicial review, two Commission dockets, Docket No. 8363 and Docket No. 8588, which have been assigned Docket Nos. 14000 and 14120, respectively; and

WHEREAS, the parties desire to resolve the above-described regulatory matters and appeals on a comprehensive basis; and

WHEREAS, the public interest will be served by the adoption of orders consistent with this Stipulation because it provides for the expeditious implementation of rates that are just and reasonable for the Company and its Texas customers, promotes the adequate and efficient provision of service, and is in accordance with applicable law; and

WHEREAS, resolution on a stipulated basis of the matters set forth herein would conserve resources, avoid the uncertainties inherent in future litigation, and reduce rate case expenses now and in the future;

NOW, THEREFORE, in consideration of the mutual agreements and covenants herein contained, the parties (the "Signatories") to this Stipulation and Settlement Agreement (the "Stipulation"), through their undersigned authorized representatives, stipulate and agree as follows:

1. (a) The Company will receive a $24.946 million annual base rate increase in this docket. Docket No. 12700 shall serve as the vehicle for implementing and obtaining approval of the base rate terms of this Stipulation.

(b) Pending a final order consistent with this Stipulation, the Signatories agree that the Company will implement interim rates consistent with this Stipulation, subject to

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refund and bond, upon entry of a second interim order (the "Second Interim Order") by the Commission, which order shall be issued as soon as possible after execution of this Stipulation. EPE agrees to use best efforts to obtain authority from the Bankruptcy Court to increase the existing bond by an amount equal to the annual base rate increase agreed to in this Stipulation.

(c) Except as described in this Paragraph, the Signatories agree that the rate design and cost allocation for such rate increase will be consistent with the Interim Order and the tariffs filed thereunder.

(i) To the extent any City or County account, which was not in Rate 41 at the time of the Commission's Order in Docket No. 9945, receives service under Rate Class 41, all state accounts become eligible for Rate 41.

(ii) Within 30 days after the Commission issues the Second Interim Order, the Company, OPC, General Counsel and the City agree to meet and discuss changes in implementation of the low income rider. The changes will be solely intended to improve and enhance the procedures that the Company will use to establish that persons qualify for the rider. Upon the agreement of the Company, OPC, General Counsel and the City, the Company will file a new residential tariff consistent with such process.

(d) Upon entry of a final order, the Company will retain all base rate revenues collected under its bonded rate increase through the date the Commission approves this Stipulation and the interim rates consistent with this Stipulation, with no refunds or surcharges.

(e) No order of the Commission will be final until the Company's Amended Plan of Reorganization becomes confirmed and effective. The Company agrees to grant sufficient hearing days to extend the jurisdictional deadline in Docket No. 12700 to a date subsequent to the confirmation order date and effective date. If the Company's Amended Plan of Reorganization should not become effective by

April 2, 1996 (which date shall be automatically extended to a date 30 days after the City gives notice that the effective date shall not be further extended), then this Stipulation is null and void *ab initio*; the Signatories are not bound by any of its terms; and the Signatories are free to seek appropriate remedies at the Commission and such other forums as may be appropriate.

2. (a) Subject to the terms of this Stipulation, during the first ten (10) years after implementation of interim rates consistent with this Stipulation (the "Freeze Period"), the Company's Texas base rates will be maintained in accordance with the final order in Docket No. 12700 except for customers taking service under the following tariffs: rate classes 15, 26, 27, 29, 30, 31 and 38, as to which this rate freeze does not apply and for whom rates may be decreased or increased in accordance with applicable contracts and law during the Freeze Period. Except for those rate classes discussed above, the Company agrees during the Freeze Period not to increase base rates for any reason save and except for an event of Force Majeure (as defined in Paragraph 2(c) hereof) or as provided in Paragraphs 2(e)(ii) and 2(d)(i).

(b) During the Freeze Period, and to the extent consistent with the freeze level, the Company may make filings that: (i) modify tariffs, riders and terms and conditions while not increasing Texas retail base rate revenues for any customer class subject to the rate freeze; provided, however, for any customer class subject to the rate freeze such modifications may neither exclude customers currently on the rate schedule nor force a customer to be moved to another rate class, (ii) add or modify tariffs, riders, and terms and conditions to address competitive conditions or secure additional load or (iii) change fixed fuel factors or otherwise provide for the recovery of fuel costs and the disposition of fuel over-recoveries and under-recoveries. Miscellaneous tariff filings, such as for incentive and load retention rates or special services, are not subject to the rate freeze, so long as there is no

increase to the Texas retail tariffs charged any rate class subject to the rate freeze. Nothing in this Paragraph shall be construed as a predetermination of the appropriate ratemaking treatment of any such changes.

(c) Except as otherwise provided in Paragraphs 2(e)(ii) and 2(d)(i), neither the Company nor any successor in interest or assignee may request from its Texas regulatory authorities nor support an increase in base rates above the freeze level with an effective date prior to the expiration of the Freeze Period, except to address an event of Force Majeure. The term "Force Majeure" as used in this Stipulation shall be limited to the effect of a natural disaster, act of war or act of God. The Company agrees to bind its successors or assignees to the terms of this Paragraph.

(d) (i) Subject to the provisions of Paragraph 2(f), the Signatories agree that if, during the Freeze Period, the fuel factor or fuel reconciliation process should be changed or eliminated in Texas, they will implement the fuel cost recovery mechanism as authorized by law or rule. In the absence of such a law or rule, the Signatories will devise a mechanism to allow the Company to recover reasonable and necessary fuel costs that it would otherwise have been allowed to recover through the fuel factor or fuel reconciliation process.

(ii) The Signatories recognize that the Federal Energy Regulatory Commission ("FERC"), or other regulatory authority with jurisdiction, may require the unbundling of utility services by utilities subject to its jurisdiction, including the Company. Subject to the provisions of Paragraphs 2(f), if such unbundling of services occurs by FERC order or otherwise, the components of the rates to the Company's customers covered by this Stipulation will be set at levels which will collect neither more nor less than the base rates established pursuant to this Stipulation notwithstanding the unbundling.

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(e) (i) Subject to Paragraphs 2(f) and 24, the Signatories (except the Public Utility Commission of Texas General Counsel ("General Counsel"), the Office of Public Utility Counsel ("OPC") and the State of Texas ("State")) agree not to seek to institute or institute on their own motion during the Freeze Period an inquiry into the reasonableness of the Company's rates under PURA § 2.211 (formerly PURA § 42). If a complaint is filed with the Commission or any other Texas regulatory authority requesting an inquiry into the reasonableness of the Company's rates under PURA § 2.211, and the Commission and any other regulatory authority institutes such an inquiry, the Signatories (except General Counsel, OPC and State) commit to support the provisions of this Stipulation. In the course of any such PURA § 2.211 proceeding, the Company shall be entitled to defend against a rate reduction in any manner it deems appropriate.

(ii) All Signatories, including General Counsel, OPC, and the State, understand and agree that it is the Company's reasonable expectation that during the Freeze Period the Company's base rates for rate classes subject to the freeze will not be changed regardless of any circumstances that could increase or decrease the Company's cost of service. The Company has given valuable consideration, and assumed substantial business risks, in exchange for the expectation hereunder that its base rates for rate classes subject to the freeze will not be reduced during the Freeze Period. General Counsel, OPC and the State, accordingly, agree that if any of them should seek to institute, directly or indirectly, an inquiry into the reasonableness of the Company's rates under PURA § 2.211 (formerly PURA § 42) then in that event, the Company's rate base shall include, in addition to the assets otherwise contemplated hereunder, the following: (A) Palo Verde Unit 3 accounting deferrals in the amount of $66,654,000 as of June 30, 1993; and (B) additional Docket No. 7460 Rate Moderation Plan ("RMP") deferrals in the amount of $25,041,000 for the period from July 1, 1993 through December 31,

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1994. Such assets shall be amortized over a ten (10) year period beginning with the date of the Second Interim Order. Any change in rates from the freeze level as a result of a proceeding initiated by General Counsel or OPC will apply solely to ratepayers over which the Commission exercises original jurisdiction.

(f) During the Freeze Period the Company and its customers in Texas will be protected from the effects of transactions that shift costs between base rates and fuel or to other rates not subject to the freeze. During the Freeze Period, the only costs that may be recovered from Texas ratepayers other than through base rates are those costs recovered as reconcilable fuel costs according to the Commission's substantive rules in effect on July 1, 1995 (as applied to the Company) and in this Stipulation. The recovery of any other costs through the fuel factor, any other special factor, or surcharge, shall be considered a shift in costs between base rates and fuel. If any Signatory believes that the Company has engaged in a transaction that is inconsistent with the foregoing intent, the Signatory shall provide notice to the Company of the alleged violation of this Paragraph. If the Company does not cure the alleged violation within 30 days of the receipt of such notice, a Signatory may initiate a complaint with the appropriate regulatory authority to recover any and all additional costs charged or to be charged to customers on account of the violation. The Signatories agree that the Company's regulatory authorities have primary jurisdiction over such matters and that the appropriate forum for such a determination is a proceeding at the appropriate regulatory authority, subject to appeal, including as allowed by law *de novo* appeal to the Commission, for the limited purpose of adjusting the fuel factor, fuel balance and/or reducing base rates by the amount so shifted. If the regulatory authority does not have jurisdiction, the parties agree that venue lies in the state district court in El Paso County, Texas.

(g) Notwithstanding any other provision of this Stipulation, the Company understand that on September 1, 1995, Senate Bill 373, Public Utility Regulatory Act of 1995, S.B. 319, as amended by S.B. 373, §2.2141, 74th Leg., R. S. 1995 ("Senate Bill 373"), will become effective and, pursuant to Section 2.2141 of that bill, the Company will be required to provide discounted rates for certain state institutions of higher education. No later than October 1, 1995, the Company agrees to file tariffs to be effective October 1, 1995 necessary to implement the discount required by Senate Bill 373. Nothing in this Stipulation shall be construed as limiting any right of the State or the Company to seek to adjust base rates on account of a change in such law.

(h) Based on current projections, the Company may be entitled to a $17 million revenue increase at the end of the Freeze Period. In order to avoid such an increase, the Company agrees that in any proceeding instituted pursuant to PURA Sections 2.211 or 2.212, or their equivalent, for an effective date on or after August 2, 2005 but before August 1, 2006, the tariff or tariffs will be designed to collect $17 million less in base revenues ("Exclusion Factor") than the otherwise authorized revenue requirement. The Exclusion Factor for a proceeding instituted pursuant to PURA § 2.211 or 2.212, or their equivalent, for an effective date between August 2, 2006 and August 1, 2007 shall be $8 million. This Exclusion Factor will not be considered for financial integrity analysis or cash flow analysis in any proceeding before a Texas regulatory authority.

(i) Should the Company, contrary to the terms of this Stipulation, file for a rate increase in Texas during the Freeze Period, the Signatories agree that the value for the previously leased Palo Verde assets described in paragraph 7(a) of this Stipulation will not apply; and that instead the values for previously leased Palo Verde assets will be applied according to the table in Attachment "A" to this Stipulation for any determination of the Company's rate increase request.

(j) In the event the Company sells, transfers, leases or assigns any operating asset for a value of $10,000,000 or more during the Freeze Period, unless the City and Company otherwise agree, the Texas jurisdictional share of the net gain on such sale shall be paid to ratepayers as a credit to the base rates over what would have been the remaining life of the asset. Ratepayers will be credited with a "return" on the unamortized portion of such gain at the Company's last approved rate of return.

3. The Signatories agree to settle all base rate issues, including cost allocation and rate design issues, not specifically addressed herein in accordance with the Interim Order.

4. Except as otherwise provided in Paragraph 2(e)(ii), the Docket No. 7460 RMP will be terminated effective June 30, 1993, and the balance of RMP deferrals as of that date will be placed in rate base and fully amortized over the 10 year freeze period, so that there is no balance to be included in rates that may be effective on or after August 1, 2005. There will be no additional Mirror CWIP (Construction Work in Progress) approved, utilized or amortized for purposes of amortizing the RMP deferrals.

5. The Company shall not recover from its Texas retail ratepayers any bankruptcy reorganization costs in the pending Chapter 11 case in the Bankruptcy Court for the Western District of Texas, Austin Division, Case No. 92-10148-FM. For purposes of this Stipulation only, the Company agrees that such costs are not reasonable and necessary operating expenses within the meaning of PURA §2.203 (a). "Retail ratepayers" includes the industrial customers who are Signatories.

6. Deferred carrying charges and deferred lease payments will be eliminated from the accounting deferrals for Palo Verde Unit 3 according to the Interim Order resulting in a balance of $4,308,000 Unit 3 accounting deferrals, less $1,457,000 of related ADFIT, as of July 1, 1993, which will be amortized over the Freeze Period. The Company will otherwise recover all remaining Palo Verde Unit 1 and 2 accounting deferrals subject to the freeze limitations discussed in Paragraph 2(a) *supra*, with the unamortized balance

included in rate base according to the Interim Order and fully amortized over the Freeze Period such that all Palo Verde accounting deferrals will be eliminated from the Company's books at the end of the Freeze Period and there will be no balance to be included in rates that may be effective on or after August 1, 2005. For the purposes of this Stipulation only, the Signatories agree that they will not raise any future challenges to the Company's right to recover the Unit 1 and 2 accounting deferrals during the Freeze Period. ADFIT associated with disallowed Unit 3 deferrals will not be included as an offset to rate base.

7. Subject to the limitations in Paragraphs 2(a) through 2(j) *supra*:

(a) The previously leased Palo Verde assets will be valued in rate base at original cost, less accumulated depreciation, according to the Interim Order.

(b) Palo Verde Unit 3 will be deemed to be 100% used and useful as of a final order in this docket.

(c) The Company's rate base shall be as determined by the terms of the Interim Order, except that (i) the remaining 15% of Palo Verde Unit 3 will be included in rate base, (ii) rate base will not be reduced to reflect the tax benefits of the Palo Verde lease rejection damages, and (iii) rate base will include any other adjustments required by the terms of the Stipulation. Such adjusted rate base shall be used as the initial basis for purposes of any cost of service analysis for the Company, including any PURA § 2.211 rate inquiry which may be permitted by the terms of this Stipulation or any earnings monitoring report.

(d) Consistent with the Commission's order in Docket No. 8892, the performance standards in effect for the Company with respect to Palo Verde will be used as the mechanism for any future assessments of Palo Verde Unit 1, 2 and 3 operations and performance; provided, however, during the Freeze Period penalties and rewards for all three Units will be reported and evaluated on a calendar year basis using the three-year rolling average dictated by Docket No. 8892. The first such

reporting period shall run from January 1, 1993 to December 31, 1995. Any penalties or rewards accruing under the performance standards will be incorporated in the Company's fuel reconciliation proceedings during the Freeze Period. Further, during the Freeze Period, the Company's base rates will not be reduced below the freeze level on account of Palo Verde performance or operations, unless the capacity factor, as measured on a station basis for any consecutive 24 month period, shall fall below 35%. In the event that the foregoing should occur, the Signatories shall be free to urge whatever rate base adjustment they believe is appropriate.

8. Except for ADFIT associated with disallowed Palo Verde Unit 3 deferrals, which is addressed in Paragraph 6, there will be no findings with respect to federal income tax issues, and the parties can assert whatever positions they desire with respect to the calculation of the Company's federal income tax expense in future rate cases.

9. The revenues from the Company's providing wheeling service and from margins on off-system sales (other than those off-system sales allocated a full slice of system costs in Docket No. 12700 [i.e., Imperial Irrigation District firm, Texas New Mexico Power, and Rio Grande Electric Cooperative, Inc.]) made by the Company will be divided as follows during the Freeze Period:

   (a) For the first five (5) years of the Freeze Period, the Company will be entitled to retain 75% of the margins and wheeling revenues and 25% of the margins and wheeling revenues will be credited to ratepayers. Margins shall mean revenues from any capacity, demand or non-fuel energy charge included in an off-system sale net of any such charges as well as wheeling charges incurred by the Company in connection with making the off-system sale.

   (b) During the second five (5) years of the Freeze Period, the sharing will be 50% to the Company and 50% to the ratepayers.

(c) Incremental costs associated with off-system sales shall not reduce the Company's reconcilable fuel costs, and the Company will not be required to calculate any incremental costs it incurs in connection with off-system sales.

(d) During the Freeze Period, the Company will retain 75% of the margins on off-system sales made by affiliates or subsidiaries of the Company and 25% of the margins will be credited to ratepayers.

The mechanism for such sharing (margins and wheeling revenues) will be in the fuel factor and fuel reconciliation process. If, during the course of the Freeze Period or any time prior to a reconciliation of margins through the end of the Freeze Period, the fuel factor or fuel reconciliation process should be eliminated, the Company agrees to devise a mechanism to reduce rates by the appropriate customer share of such margins.

10. The Signatories agree that the amounts of decommissioning expense allowed on an annual basis in the Company's cost of service shall be described in a schedule to be attached to the Second Interim Order. Such amounts shall be adjusted in any future rate proceeding or earnings monitoring report as necessary to reflect the cost estimate of the most recent official decommissioning study prepared for the Palo Verde participants and to enable the Company to secure an exemption pursuant to § 468A of the Internal Revenue Code of 1986 from federal income tax liability in connection with its nuclear decommissioning trust. The Company agrees to fund such amounts pursuant to its contractual obligations under the Arizona Nuclear Power Project Participation Agreement. Such decommissioning expense shall be recognized as a reasonable and necessary expense in any rate proceeding or earnings monitoring report initiated during the Freeze Period and, during such period, no Signatory shall contest the inclusion of such amounts in the Company's cost of service. After the Freeze Period, Ratepayers are to be in no worse position as to decommissioning expense than they would have been had rates not been frozen.

11. The Company will reimburse the City for all its outstanding rate case expenses billed and unreimbursed as of July 17, 1995 of $1,081,229.14 within ten (10) days following issuance of the final order consistent with this Stipulation. Additional expenses of the City incurred in Docket No. 12700 as well as any proceedings resolved by this Stipulation will be paid by the Company to the City within thirty (30) days of the submittal of a bill or ten (10) days following the issuance of a final order consistent with this Stipulation, whichever is later. The Company agrees to indemnify the City against any claims made pursuant to the City's agreement dated May 3, 1994 relating to reimbursement of rate case expenses. There shall be no surcharge to ratepayers in any class whatsoever as a result of such payments.

12. (a) With respect to the fuel matters initially presented in Docket No. 12700, the Signatories agree to settle all fuel reconciliation issues and fuel factor issues in accordance with the Commission's final order in Docket No. 13966, subject to the provisions of Paragraph 9 above.

(b) The Signatories further agree that the Company's fuel and purchased power costs for the period July 1, 1993 through June 30, 1995 will be deemed reconciled and that, taken in conjunction with the purchased power capacity charges at issue in the remand of Docket No. 8588 (Docket No. 14120), discussed below, there shall be no net refund or surcharge to ratepayers as a result of such fuel reconciliation. The Company's over/under recovery fuel balance shall be $0 as of June 30, 1995. The Signatories agree to implement their agreement in this Paragraph with a fuel reconciliation filing, to be made by the Company within thirty (30) days following the effective date of the Company's Amended Plan of Reorganization. The Signatories will urge that such reconciliation be processed administratively, by agreement, without the need for the Company to develop and file the fuel reconciliation schedules and supporting testimony otherwise required by Commission rules.

(c) The Company will make filings during and after the Freeze Period to reconcile its fuel and purchased power costs incurred during the Freeze Period in accordance with PURA and Commission rules and procedures, subject to Paragraph 9 above.

(d) The Company will initiate a proceeding to implement a revised composite fixed fuel factor as appropriately adjusted for voltage levels, effective as soon as practicable following the entry of the Second Interim Order by the Commission.

13. The Signatories agree that the Company shall withdraw its application filed in Docket No. 12700 for a determination by the Commission that the proposed acquisition of the common stock of the Company is in the public interest.

14. The Signatories agree that reacquisition of the Palo Verde leased assets is in the public interest as that term is defined by PURA § 63 (recodified as PURA § 1.251), and each Signatory agrees to support a determination by the Commission that such reacquisition is in the public interest and that the previously leased assets be included in rate base at their original cost less depreciation, consistent with the Interim Order and further subject to the provisions of Paragraph 2(i) above.

15. The Signatories agree to use their best efforts to finalize the PURA § 43 (recodified as PURA § 2.212) rate order in this docket in accordance with this Stipulation.

16. Upon the date the City signs this Stipulation, the City agrees to have its staff begin the process of presenting to the City Council a new franchise for the Company in substantially the same form as the current franchise (granted by ordinance dated March 25, 1971 for a 30 year period), except for a provision recognizing the City's option to decline to purchase the Company's property under certain circumstances. If the City Council does not grant the Company a franchise consistent with this Paragraph within 45 days of inception of the process, then the Company may declare this Stipulation null and void. If a new franchise is granted , it will become effective upon the termination of the current franchise and extend through August 1, 2005. The new franchise will be

null and void if the Amended Plan of Reorganization does not become effective consistent with this Stipulation.

17. The Company agrees to dismiss without prejudice its Adversary Proceeding No. 94-1148-FM in the Bankruptcy Court for the Western District of Texas, Austin Division against the Commission, the City, the New Mexico Public Utility Commission and the OPC within 10 days of the Commission's entry of the Second Interim Order.

18. (a) As further detailed below, the Signatories agree to dismiss their pending appeals of the Commission's orders in Docket Nos. 8018, 8078, 8363, and 9945, and the Company agrees to dismiss the pending remand of Docket No. 8363 (Docket No. 14000) (the "Resolved Appeals"). Within ten (10) days after the date of execution of this Stipulation, all Signatories who are parties to any of the Resolved Appeals shall file a motion jointly notifying the court or Commission in which the matter is now pending that it is likely that the issues in the cases will be resolved. Such notice shall request that action be delayed pending further motion by the parties.

(b) Subject to the qualifications set out below, within ten (10) days after the effective date of the Company's Amended Plan of Reorganization, the Signatories who are parties to the Resolved Appeals shall file appropriate motions with each applicable court, or the Commission, to dismiss with prejudice each of the Resolved Appeals brought by any one of the Signatories. The precise form of the motions shall be tailored to each case, but will be substantially as described below with respect to each Signatory and proceeding:

(1) With respect to the appeal of Docket No. 8018, now pending in the Austin Court of Appeals, the City agrees to move to dismiss with prejudice its appeal. If the Austin Court of Appeals has already issued its decision in this appeal prior to the filing of the City's motion to dismiss, the Signatories who are parties to the appeal will jointly move the Austin

Court of Appeals, or the Texas Supreme Court, as appropriate, to vacate the court judgments and opinions issued in this case and dismiss the appeal.

(2) With respect to the appeal of Docket No. 8078, now pending in the Austin Court of Appeals, the City agrees to move to dismiss with prejudice its appeal. If the Austin Court of Appeals has already issued its decision in this appeal prior to the filing of the City's motion to dismiss, the Signatories who are parties to the appeal will jointly move the Austin Court of Appeals, or the Texas Supreme Court, as appropriate, to vacate the court judgments and opinions issued in this case and dismiss the appeal.

(3) With respect to the appeal of Docket No. 8363, now pending in the Travis County District Court, the Company, the City and OPC agree to dismiss with prejudice their appeals. The Company further agrees to move for dismissal of Commission Docket No. 14000, which is pending on limited remand from the appeal of Docket No. 8363.

(4) With respect to the appeal of Docket No. 9945, now pending in the Austin Court of Appeals, the Company, the City, the State of Texas and OPC agree to jointly file a motion requesting that the Court of Appeals, or the Texas Supreme Court, as appropriate, (i) vacate all court opinions and judgments issued in the case, (ii) dismiss all appeals of the Commission's order and (iii) refrain from publishing any opinions. The Signatories (except General Counsel) agree to use their best efforts to prevail on the Commission to concur in this motion and to likewise dismiss its appeal concerning Docket No. 9945.

(5) With respect to the appeal of Docket No. 13966, now pending in the Travis County District Court, the Signatories who are parties to these

appeals agree to jointly request a remand to the Commission of such appeal, so that the Commission may delete any language inconsistent with the intent of the Signatories with respect to the treatment of off-system sales revenues and wheeling revenues as provided in Paragraph 9 above.

The Signatories (except General Counsel) will exercise best efforts to obtain the Commission's concurrence in all the foregoing motions.

(c) The Signatories agree to finalize the pending remand of Docket No. 8588 (Docket No. 14120). The resolution will take the form of a request by the Signatories that the proceeding be stayed, and that the Commission take no further action on such docket pending a final order in Docket No. 12700. In the event the order in Docket No. 12700 becomes final as contemplated by this Stipulation, the Signatories who are parties to Docket No. 14120 agree to file notification in that docket that they have stipulated that the purchased power capacity charges at issue in the remand of Docket No. 8588 shall be credited to the Company's July 1, 1993 to June 30, 1995 over/under recovery fuel balance, and to request that the Commission enter a final order in Docket No. 14120 consistent therewith. As discussed above in Paragraph 12, the charges at issue in Docket No. 14120 will be treated consistent with the reconciliation of the Company's fuel and purchased power costs for the period July 1, 1993 through June 30, 1995.

19. Any recovery from the Company's pending lawsuit No. 95-7153, or causes of action that accrued to the Company as a result of the failure of its proposed merger or arising out of the Company's bankruptcy shall be retained wholly and exclusively by the Company and not passed through to ratepayers. Any costs incurred by the Company in connection with such litigation shall not be considered reasonable and necessary operating expenses for ratemaking purposes in accordance with PURA §2.203(a). Any liabilities incurred by the Company in connection with such litigation shall be borne by the Company shareholders and shall not be recovered from ratepayers.

20. This Stipulation is the result of an extended and highly complex course of negotiations among the Signatories. It necessarily represents many compromises made by the Signatories on all of the issues involved. The Stipulation covers several separate Company proceedings pending before the Commission and the courts, each of which involves a number of discrete issues. The entire Stipulation should be viewed as a unitary, whole agreement, and not separate agreements on discrete issues or phases of any particular case. The resolution of each issue is interrelated to the resolution of all other issues. The Signatories understand and agree that each term of this Stipulation is in consideration and support of every other term. As a result, the Stipulation is indivisible because of the comprehensive nature of the compromises made.

21. This Stipulation, if approved by the Commission, represents a fair, just and reasonable solution to the issues being resolved. Moreover, this Stipulation will serve the purpose of moderating the rates of the Company in the Texas jurisdiction during the Freeze Period. This Stipulation reflects settlement discussions. It is recognized and agreed by the Signatories that this Stipulation is made and filed solely in connection with the compromise and settlement of rate matters related to the Company and is subject to the specific approval of the Commission of the matters herein stipulated. By entering into this Stipulation, none of the Signatories shall be deemed to have approved or acquiesced in any ratemaking principle, valuation methodology, method of cost-of-service determination, method of revenue calculation, or cost allocation or rate design principle underlying any of the provisions and agreements contained herein. It is the result of a unique fact situation, and its resolution is specific to the circumstances presented. This Stipulation shall not prejudice, bind, or affect any Signatory, or be viewed as an admission, except to the extent necessary to give effect to or enforce the terms of this Stipulation or unless otherwise specifically stated herein.

22. The Signatories agree that they will use their best efforts to obtain expeditious implementation of this Stipulation by the entry of appropriate final orders in Docket

Nos. 12700, 14000 and 14120 and in the judicial appeals of Docket Nos. 8018, 8078, 8363, 9945 and 13966. This Stipulation assumes the legality of the treatments and methodologies set out herein. Should any such treatment or methodology be rejected or declared illegal by either the Commission or a court, any Signatory shall have the right to withdraw from this Stipulation; however, the Signatories agree to negotiate in good faith to substitute a treatment or methodology with the same economic effect as that rejected or declared illegal.

23. The Signatories further agree that, upon the Commission's entry of the Second Interim Order, they will engage in good faith efforts to obtain approval of a consensual plan of reorganization that will allow the Company to emerge from bankruptcy on a stand-alone basis, consistent with the matters agreed to herein. This undertaking includes, but is not limited to, the exercise of reasonable efforts by the Signatories to obtain the support and cooperation of the Bankruptcy Court, the Commission, the Company's creditors and other parties-in-interest in the Company's bankruptcy case.

24. This Stipulation shall be unaffected by and shall not be changed or invalidated based upon the creditor and equity holder distributions or capital structure ultimately provided by the new plan of reorganization unless (i) the Plan does not comply with and implement this Stipulation, (ii) prior to confirmation the City is not satisfied that the reorganized company will be financially sound (a preliminary credit rating issued by one of the four (4) major rating agencies, that the credit quality of the first mortgage bonds to be issued by the reorganized company will be not less than BB- (as defined by Standard & Poor's) or its equivalent will establish that the reorganized company is financially sound); or (iii) debt of the reorganized company exceeds $1.3 billion. In any of such events, the City has the right to withdraw from the terms of this Stipulation and terminate it. The Signatories recognize that the Company will emerge from bankruptcy on a stand-alone basis and that the Company will be free to engage in a merger or other business combination with a third party after emerging from bankruptcy. In the event of such a

merger, the Signatories retain all the rights provided in this Stipulation, their rights as a party in a proceeding pursuant to PURA §1.251 (formerly §63) as well as the right to pursue a reduction in rates below the freeze level. However, such right shall be limited to urging rate reductions based on post-merger synergy savings. In the event the Company seeks a merger or other business combination, General Counsel retains all authority consistent with PURA, § 1.251. Nothing in this paragraph shall be construed as a pre-determination of the appropriate ratemaking treatment of any such synergy-based reductions in cost.

25. Where this Stipulation requires a Signatory to "participate," "support" or "urge" regulatory or judicial action, and where the Signatory is not a governmental body or agency, then such obligation shall be limited to no more than reasonable efforts involving minimal expense.

26. Unless the context otherwise indicates, references to ratemaking items including, but not limited to, rate base, expense, margin and gain, shall mean the Texas jurisdictional share of such items.

27. Each person executing this Stipulation represents that (s)he is authorized to sign this Stipulation on behalf of the party represented. Facsimile copies of signatures are valid for purposes of evidencing this Stipulation. This Stipulation may be executed in multiple counterparts.

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EXECUTED this 27th day of July, 1995.

EL PASO ELECTRIC COMPANY

By:_____
Name:_____
Title:_____

PUBLIC UTILITY COMMISSION OF TEXAS GENERAL COUNSEL

By:_____
Name:_____
Title:_____

OFFICE OF PUBLIC UTILITY COUNSEL

By:_____
Name:_____
Title:_____

CITY OF EL PASO

By:_____
Name:_____
Title:_____

Approved as to form:

_____

ASARCO INCORPORATED

By:_____
Name:_____
Title:_____

PHELPS-DODGE REFINING CORPORATION & CHEVRON U.S.A., INC.

By:_____
Name:_____
Title:_____

BORDER STEEL ROLLING MILLS, INC. AND EL PASO IRON & METAL COMPANY

By:_____
Name:_____
Title:_____

The execution of this Stipulation by Border Steel Rolling Mills, Inc. and El Paso Iron & Metal Company is subject to the approval of the U.S. Bankruptcy Court for the Western District of Texas, El Paso Division.

DEPARTMENT OF DEFENSE

By: David A. McCormick
Name: David A. McCormick
Title: General Attorney

INTERNATIONAL BROTHERHOOD OF ELECTRICAL WORKERS

By:_____
Name:_____
Title:_____

TEXAS STATE AGENCIES

By:_____
Name:_____
Title:_____

EXECUTED this 27TH day of JULY, 1995.

EL PASO ELECTRIC COMPANY

By: [signature]
Name: DAVID H. WIGGS JR
Title: CHAIRMAN & C.E.C.

PUBLIC UTILITY COMMISSION OF TEXAS GENERAL COUNSEL

By: [signature]
Name: Charles E. Johnson
Title: Assistant General Counsel

OFFICE OF PUBLIC UTILITY COUNSEL**

By: [signature]
Name: MARION TAYLOR DREW
Title: ASSISTANT PUBLIC COUNSEL

CITY OF EL PASO

By: [signature]
Name: [illegible]
Title: [illegible]

Approved as to form:

_____

ASARCO INCORPORATED

By: _____
Name: _____
Title: _____

PHELPS-DODGE REFINING CORPORATION & CHEVRON U.S.A., INC.

By: _____
Name: _____
Title: _____

BORDER STEEL ROLLING MILLS, INC. AND EL PASO IRON & METAL COMPANY

By: _____
Name: _____
Title: _____

The execution of this Stipulation by Border Steel Rolling Mills, Inc. and El Paso Iron & Metal Company is subject to the approval of the U.S. Bankruptcy Court for the Western District of Texas, El Paso Division.

DEPARTMENT OF DEFENSE

By: _____
Name: _____
Title: _____

INTERNATIONAL BROTHERHOOD OF ELECTRICAL WORKERS

By: _____
Name: _____
Title: _____

THE STATE OF TEXAS

By: _____
Name: _____
Title: _____

**OPC's signature is contingent upon there being no opposition to this Stipulation and Settlement Agreement by other parties in this Docket. If by August 16, 1995 no such opposition becomes known, OPC's signature is unconditional.


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necessity for generation facilities, a utility shall include the following:

(1) the most recent energy efficiency plan;

(2) testimony which shall specifically indicate the extent to which the goals of the utility's energy efficiency plan have been reached as of the date of filing. This testimony shall indicate the status of all programs and studies which are being undertaken pursuant to the energy efficiency goals laid out in subsection (b)(1) of this section and all costs expended and benefits achieved to date; and

(3) testimony which shall indicate to what extent the utility's achievements through its energy efficiency plan have offset the need for new generating facilities, or permitted the utility to reduce reliance on less efficient generation facilities, as required by the Public Utility Regulatory Act, §54(d)(1) and §54(e)(2).

(d) The following treatment may be applied to appropriate utility-controlled options or conservation programs:

(1) recovery of part of the expenses as part of cost of service;

(2) recovery of all of the expenses as part of cost of service;

(3) adjustment in the rate of return or return on equity; or

(4) capitalization or other treatment allowing a return on conservation expenditures.

(e) A utility may amend or modify its energy efficiency plan as needed.

Source: The provisions of this §23.22 adopted to be effective August 2, 1984, 9 TexReg 3929; amended to be effective July 13, 1989, 14 TexReg 3201; amended to be effective December 27, 1993, 18 TexReg 9305.

§ 23.23. Rate Design

(a) Guidelines for certifying long-term fuel contracts. The commission will certify long-term fuel contracts in accordance with the guidelines in this subsection for determining the reasonableness of the terms and conditions of such contracts. This subsection does not require long-term fuel contracts to be submitted for certification, and no adverse inference will result from a utility's decision not to seek certification.

(1) Definition. A long-term fuel contract is a contract, or an amendment to a contract, with a specified term of at least five years for the supply, transportation, processing, and/or storage of fuel for the generation of electricity.

(2) Initiation of review. Upon the petition of a utility, the commission will review the reasonableness of the terms and conditions of one, or more if entered within a 60-day period, long-term fuel contracts as of the time of execution. A petition for certification may be filed separately, with a petition to reconcile fuel expenses, or with a statement of intent to change rates; however, a utility may not have more than one separately filed petition for certification pending before the commission at one time. The commission may consolidate a certification proceeding with, or sever it from, another proceeding.

(3) Criteria. The commission will consider the following factors in determining whether to certify a long-term fuel contract:

(A) the pricing provisions and other terms, in light of, among other factors, identified contracts, offers, or proposals, if any, that the utility could reasonably have obtained for comparable supply, transportation, processing, and/or storage of fuel when the contract was executed;

(B) the quantity deliverable under the contract, in light of the utility's long-term load forecast, mix of fuel purchases, and the most recent commission approved integrated resource plan, if any;

(C) current and projected fuel prices when the contract was executed;

(D) the reliability of the supply;

(E) provisions allowing for variation in the purchase and receipt or supply and delivery of fuel; and

(F) any other appropriate factors, which may include, but are not limited to, environmental, health, and safety protection, and economic impacts.

(4) Additional considerations. Other matters relating to long-term fuel contracts will be handled as follows.

(A) A price-adjustment clause, if any, in a long-term fuel contract must either provide for specified or determinable adjustments or tie the price adjustments to appropriate market indexes.

(B) A long-term fuel contract may be contingent on certification, approval by other appropriate regulatory authorities, and other reasonable contingencies, but otherwise must be fully executed.

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(C) A long-term fuel contract may provide for prepayments by the utility in return for dedicated long-term fuel supply.

(D) The reasonableness of any price premiums in a long-term fuel contract over short-term prices will be determined in light of all the benefits obtained under the contract as a whole.

(5) Procedural matters. Matters relating to procedural schedules and notice will be handled as follows.

(A) Upon motion by a utility for an expedited certification in a proceeding in which certification is the sole issue, the presiding officer shall determine within 35 days whether the utility has complied with the requirements of subparagraph (B) of this paragraph, and if so, set a procedural schedule that will enable the commission to issue a final order in the proceeding as follows:

(i) within 120 days after the contract is submitted to the commission, if no hearing is requested within 60 days after the contract is submitted; and

(ii) within 180 days after the contract is submitted to the commission, if a hearing is requested within 60 days after the contract is submitted, except that this deadline is extended two days for each day in excess of five days on which the commission conducts a hearing on the merits of the case.

(B) Commission approval of a request for expedited certification is contingent on the utility's filing its entire direct case at the time it submits its contract to the commission. The direct case must include:

(i) testimony addressing each factor listed in paragraph (3)(A)-(E) of this subsection;

(ii) a sensitivity analysis showing the utility's economic dispatch of its generating units, and incorporating the corollary energy requirements over a reasonable range of load growth scenarios and a reasonable range of fuel price variations;

(iii) documentation of the comparative analyses performed on the alternative fuel supplies, initially and throughout the life of the contract; and

(iv) a narrative explanation of the utility's strategy for long-term versus short-term fuel purchases.

(C) A utility may file a petition for certification without submitting a contract if at the time of filing it requests entry of a protective order making the contract available while protecting its confidentiality. The presiding officer shall promptly issue a protective order subject to any party's right to challenge the confidential designation of information in a contract. Issues involving the confidentiality of information will be resolved under subsection (b)(5) of this section.

(D) In any proceeding in which certification of a long-term fuel contract is requested, the utility shall provide a copy of the filing to the Office of Public Utility Counsel and the General Counsel and provide written individual notice of the proceeding to all other parties to the contract and each of the utility's customers.

(6) Certification. After considering the factors set forth in paragraph (3) of this subsection, the commission shall certify a long-term fuel contract if it determines that the terms and conditions of the contract are reasonable as a whole; otherwise, the commission shall deny certification.

(7) Effect of certification. Certification of a long-term fuel contract establishes that the original prices, terms, and conditions of the contract were reasonable at the time the contract was entered and that it was reasonable to enter the contract and does not preclude commission review of the reasonableness of the utility's actions with respect to the contract. Denial of certification establishes that the contract is not eligible for certification, and precludes relitigation of the reasonableness of the contract as a whole. To the extent other ultimate issues of fact are actually litigated and are essential to the commission's decision not to certify the contract, relitigation of such issues is also precluded.

(b) Recovery of fuel and purchased-power costs.

(1) Purpose. The commission will set an electric utility's rates at a level that will permit the utility a reasonable opportunity to earn a reasonable return on its invested capital and to recover its reasonable and necessary expenses, including the cost of fuel and purchased power. The commission recognizes in this connection that it is in the interests of both utilities and their ratepayers to adjust customer charges in a timely manner to account for changes in certain fuel and purchased-power costs. Pursuant to the Public Utility Regulatory Act (the Act), §43(g)(2), this sub-

section establishes a procedure for setting and revising fuel factors and purchased-power cost recovery factors and a procedure for regularly reviewing the reasonableness of the fuel expenses recovered through fuel factors.

(2) Fuel factors.

(A) Use and calculation of fuel factors. A utility's fuel costs will be recovered from the utility's customers by the use of a fuel factor that will be charged for each kilowatt-hour (kwh) consumed by the customer.

(i) Fuel factors are determined by dividing the utility's projected net eligible fuel expenses, as defined in subparagraph (B) of this paragraph, by the corresponding projected kilowatt-hour sales for the period in which the fuel factors are expected to be in effect. Fuel factors must account for system losses and for the difference in line losses corresponding to the type of voltage at which the electric service is provided. A utility may have different fuel factors for different times of the year to account for seasonal variations. A different method of calculation may be allowed upon a showing of good cause by the utility.

(ii) A utility may initiate a change to its fuel factor as follows.

(I) A utility may petition to adjust its fuel factor as often as once every six months according to the schedule set out in subparagraph (E) of this paragraph.

(II) A utility may petition to change its fuel factor at times other than provided in the schedule if an emergency exists as described in subparagraph (G) of this paragraph.

(III) A utility's fuel factor may be changed in any general rate proceeding.

(iii) Fuel factors are in the nature of temporary rates, and the utility's collection of revenues by fuel factors is subject to the following adjustments.

(I) The reasonableness of the fuel costs that a utility has incurred will be periodically reviewed in a reconciliation proceeding, as described in paragraph (3) of this subsection, and any unreasonable costs incurred will be refunded to the utility's customers.

(II) To the extent that there are variations between the fuel costs incurred and the revenues collected, it may be necessary or convenient to refund overcollections or surcharge undercollections. Refunds or surcharges may be made without changing a utility's fuel factor, but requests by the utility to make refunds or surcharges may only be made at the times allowed by this paragraph. A utility may petition to make refunds or surcharges at the specified times that these rules allow a utility to change its fuel factor irrespective of whether the utility actually petitions to change its fuel factor at that time. A utility shall petition for a surcharge at the next date allowed for setting a fuel factor by the schedule set out in subparagraph (E) of this paragraph when it has materially undercollected its fuel costs and projects that it will continue to be in a state of material undercollection. A utility shall petition to make a refund at any time that it has materially overcollected its fuel costs and projects that it will continue to be in a state of material overcollection. "Materially" or "material," as used in this paragraph, shall mean that the cumulative amount of over- or under-recovery, including interest, is 4.0% of the annual estimated fuel cost figure most recently adopted by the commission, as shown by the utility's fuel filings with the commission.

(B) Eligible fuel expenses. Eligible fuel expenses include expenses properly recorded in the Federal Energy Regulatory Commission Uniform System of Accounts, Numbers 501, 503, 518, 536, 547, 555, and 565, as modified in this subparagraph, as of September 30, 1992, and the items specified in clause (vi) of this subparagraph. Any later amendments to the system of accounts are not incorporated into this subparagraph. Subject to the commission finding special circumstances under clause (v) of this subparagraph, eligible fuel expenses are limited to:

(i) For any account, the utility may not recover, as part of eligible fuel expense, costs incurred after fuel is delivered to the generating plant site, for example, but not limited to, operation and maintenance expenses at generating plants, costs of maintaining and storing inventories of fuel at the generating plant site, unloading and fuel handling costs at the generating plant, and expenses associated with the disposal of fuel combustion

residuals. Further, the utility may not recover maintenance expenses and taxes on rail cars owned or leased by the utility, regardless of whether the expenses and taxes are incurred or charged before or after the fuel is delivered to the generating plant site. The utility may not recover an equity return or profit for an affiliate of the utility, regardless of whether the affiliate incurs or charges the equity return or profit before or after the fuel is delivered to the generating plant site. In addition, all affiliate payments must satisfy the Act, §41(c)(1).

(ii) For Accounts 501 and 547, the only eligible fuel expenses are the delivered cost of fuel to the generating plant site excluding fuel brokerage fees. For Account 501, revenues associated with the disposal of fuel combustion residuals will also be excluded.

(iii) For Accounts 518 and 536, the only eligible fuel expenses are the expenses properly recorded in the account, excluding brokerage fees. For Account 503, the only eligible fuel expenses are the expenses properly recorded in the account, excluding brokerage fees, return, non-fuel operation and maintenance expenses, depreciation costs, and taxes.

(iv) For Account 555, the utility may not recover demand or capacity costs.

(v) Upon demonstration that such treatment is justified by special circumstances, a utility may recover as eligible fuel expenses fuel or fuel related expenses otherwise excluded in clauses (i)-(iv) of this subparagraph. In determining whether special circumstances exists, the commission shall consider, in addition to other factors developed in the record of the reconciliation proceeding, whether the fuel expense or transaction giving rise to the ineligible fuel expense resulted in, or is reasonably expected to result in, increased reliability of supply or lower fuel expenses than would otherwise be the case, and that such benefits received or expected to be received by ratepayers exceed the costs that ratepayers otherwise would have paid or otherwise would reasonably expect to pay.

(vi) In addition to the expenses designated above, unless otherwise specified by the commission, eligible fuel expenses shall include:

(I) revenues from steam sales included in Accounts 504 and 456 to the extent expenses incurred to produce that steam are included in Account 503; and

(II) revenues from wheeling transactions; and

(III) revenues from off-system sales in their entirety.

(C) Petitions to revise fuel factors. On the first business day of the months specified in subparagraph (E) of this paragraph, each utility using one or more fuel factors may file a petition requesting revised fuel factors. A copy of the filing shall also be delivered to the general counsel and the Office of Public Utility Counsel. Each petition must be accompanied by the commission prescribed fuel factor application and supporting testimony that includes the following information:

(i) for each month of the period in which the fuel-factor has been in effect up to the most recent month for which information is available:

(I) eligible fuel expenses incurred, listed by the types of fuel used;

(II) purchased power and energy delivered to the utility, listed by source and showing the demand component and energy and/or fuel-expense component associated with the purchases;

(III) kilowatt-hour sales to system utility customer classes;

(IV) generation by plant, and if available, by unit;

(V) off-system kilowatt-hour sales, and associated fuel costs and revenues;

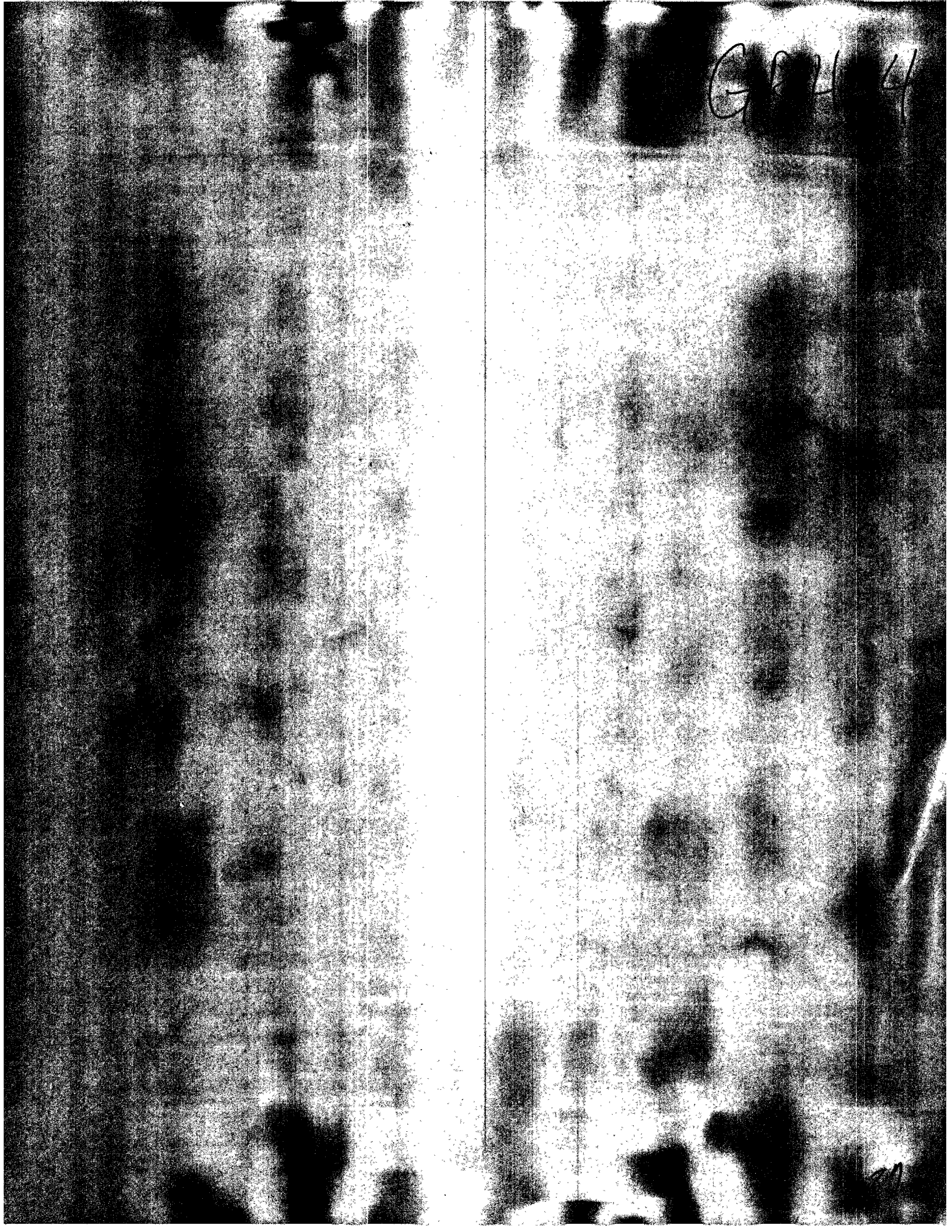
(VI) the revenues collected pursuant to fuel factors by customer class;

(VII) any other items that to the knowledge of the utility have affected fuel factor revenues and eligible fuel expenses; and

(VIII) the difference, by customer class, between the revenues collected pursuant to fuel factors and the eligible fuel expenses incurred;

(ii) for each month of the period for which the revised fuel factors are expected to be in effect:

(I) estimated eligible fuel expenses, listed by the types of fuel expected to be used;



NAVIGANT CONSULTING

ASSESSMENT OF THE EL PASO ELECTRIC COMPANY'S OPERATING EXPENSES

Prepared for

The City of El Paso, Texas

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June 2, 2006

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ASSESSMENT OF THE EL PASO ELECTRIC COMPANY'S OPERATING EXPENSES

This Report summarizes the assessment prepared by Navigant Consulting, Inc. ("Navigant Consulting") of whether the operating expenses of El Paso Electric Company (the "Company" or "EPE") were within a reasonable range as compared to the utility industry. This Report offers a high level summary of Navigant Consulting's assessment process and the resulting findings and recommendations. Attached to this document is a PowerPoint slide presentation offering additional detailed explanation regarding the findings from this assessment.

I. BACKGROUND

The City of El Paso (the "City") entered into a Rate Agreement (the "Rate Agreement") with the Company, effective July 1, 2005. By its terms, the Rate Agreement states it is intended to provide:

- Future rate stability;
- Fair cost-based rates;
- Reduced fuel costs with the sharing of profits from off-system sales;
- Continued improvement in the Company's financial health;
- Expanded participation by the Company in local civic and charitable activities;
- Additional investment by the Company in its delivery systems so that it can maintain a high quality of service;
- Replacement of old local generation with new, more efficient facilities;
- The opportunity to work together for the betterment of the community;
- Recognition of the inevitable interdependence that exists between the economic health of the community and one of its largest companies; and
- Coordination with El Paso Water Utilities to improve water conservation efforts in the City.

The Rate Agreement allowed the City to select a qualified consultant to determine whether the Company's operating expenses are within a reasonable range as compared to the utility industry. The term "operating expenses" for this assessment was assumed to exclude the cost of fuel and purchased power as well as not include taxes, capital expenditures, depreciation, return on investment and profit. If the operating expenses are deemed unreasonable, then the Company and the City will agree upon a remedy, or the Rate Agreement will expire at the end of the twelve-month period. If the operating expenses are deemed to be reasonable, the Agreement shall continue in full force and effect.

Navigant Consulting was retained to prepare the assessment to determine whether the Company's operating expenses are within a reasonable range as compared to the utility industry. The assessment focused on addressing the following questions:

- Are El Paso Electric's costs reasonable given its business structure?
- Are El Paso Electric's operating and maintenance expenses ("O&M") appropriate given its operating environment?
- Are there specific opportunities that emerge from the above analysis that El Paso Electric should pursue?

II. GLOSSARY OF INDUSTRY TERMS

The following is a glossary of electric industry terms used in this Report.

A&G: administrative and general expense; typically including corporate administration (salaries and benefits), accounting, insurance, rents and facility costs for corporate administration

Customer Care: the function of a utility company that supports the direct relationship with customers; typically includes customer call center, sales and marketing, customer accounting and billing, and customer information systems

FERC: The Federal Energy Regulatory Commission has jurisdiction over electric wholesale power and transmission rates and establishes detailed reporting requirements for regulated (investor-owned) utilities.

FERC Form 1: complex annual operational and financial report required to be filed by all regulated electric utilities.

Generation: the production of electric energy by electric generators.

GIS: Geographic Information System; technology equipment and data combined to display actual utility operating conditions to support utility real-time operations and planning.

kWh: kilowatt hour; a unit of energy equal to the consumption of 1,000 watts for the period of an hour.

MWh: megawatt hour; a unit of energy that is equal to 1,000 kWh.

Net Plant in Service: total book value of investment in facilities less accumulated depreciation.

O&M / Operating Expenses: Operations and maintenance expenses as required to operate and maintain a utility; for purposes of this assessment, the cost of fuel and

purchased power have been excluded from operating (O&M) expenses; operating expenses do not include taxes, capital expenditures, depreciation, and return on investment.

SAIDI: an electric utility operations performance measure; SAIDI stands for System Average Interruption Duration Index and presents the average time (in minutes) that customers experience interruptions in the supply of power; for example, the Company's 2005 SAIDI was 31.9 which states that the average length of time for a power interruption in 2005 was 31.9 minutes.

SAIFI: an electric utility operations performance measure; SAIFI stands for System Average Interruption Frequency Index and presents the average number of times all the utility's customers had their power interrupted within a year period.

T&D: Transmission and Distribution

> **Transmission:** the function of transmitting electric power over high voltage lines; typically transmission systems are used to transmit large quantities of power over extended distances from power plants to regional delivery points on a utility's system.
>
> **Distribution:** the function of transmitting electric power over medium voltage lines; typically distribution systems receive power from transmission systems and after reduction in voltage levels through substations, transmit power to the customer.

III. SCOPE OF ASSESSMENT

Navigant Consulting reviewed all operating costs of the Company's regulated utility business. These O&M costs were separated into four main components:

1) Generation
2) Transmission and Distribution ("T&D")
3) Customer Care
4) Corporate/support functions

For the four main components of O& M costs outlined above, Navigant Consulting examined the reasonableness of the Company's:

- Overall O&M expenses
- Capitalization versus expense policies
- Depreciation expenses
- Expenses related to service quality
- Existing workforce
- Projected changes to the workforce
- Routine maintenance programs
- Recent cost-cutting initiatives

In accordance with the recommendation from Navigant Consulting, and acceptance by the City and the Company, Navigant Consulting did not review fuel and purchased power expenses. Fuel and purchased power expenses are formally reviewed in the Company's fuel reconcilliation filings at the Texas Public Utility Commission. In addition, Pensions and Benefits (Account 926); Franchise Requirements (Account 927); and Regulatory Commission Expenses (Account 928) were excluded from the review due to the company-specific uniqueness and high variability of the expenses.

Navigant Consulting relied upon data provided by the Company, publicly available data (primarily FERC Form 1 filings), and its internal databases to assess the reasonableness of the Company's operating costs. Navigant Consulting reviewed the costs in aggregate, by FERC account, as well as on a unitized basis. Examples of unitized costs reviewed were:

- Cost per customer
- Cost per employee
- Cost per line mile
- Cost per meter
- Cost per MWh

A. Peer Group Benchmarking

The overall objective of the review was to determine the reasonableness of the Company's operating expenses as compared to those of similarly situated regulated utilities. It was important to compare the Company with other utilities of similar size and organizational structure to afford a reasonable comparison. The group of comparative companies ("Peer Group") against which the Company's operating expenses were benchmarked was determined after consultation with the City and the Company. The selection of the companies that were included in the Peer Group was based on five selection criteria:

1. *Company Type* - Electric operating utilities required by FERC to file an annual Form 1 (i.e., IOUs)

2. *Company Organization* - Holding companies with many operating utility subsidiaries were generally excluded

3. *Business Composition* - Integrated utilities with both generation and delivery operations

4. *Company Location* - Primarily located in the Midwest or Southwest

5. *Company Size* - Between 100,000 and 1,000,000 customers, annual retail revenues of $200 million -$2 billion, and under $10 billion in net plant

Based on the above selection criteria, the following Peer Group was identified:

» Arizona Public Service Co. (APS)	» Madison Gas & Electric Co. (MGE)
» CLECO (CNL)	» MidAmerican Energy Co. (MA)
» Dayton Power & Light (DPL)	» Northern Indiana PSC (NI)
» Duquesne Light Co. (DQE)	» Oklahoma Gas & Electric Co. (OGE)
» The Empire District Electric Co. (EDE)	» Otter Tail Power Co. (OTTR)
	» Public Service Co. of New Mexico (PNM)
» Indianapolis Power & Light (IPL)	
» Kansas City Power & Light (KCPL)	» Tampa Electric Co. (TECO)
» Kansas Gas & Electric Co. (KGE)	» Tucson Electric Power Co. (UNS)
» Kentucky Utilities (KU)	» Westar Energy (WR)
» Louisville Gas & Electric (LGE)	» Wisconsin Public Service Corp. (WPS)

B. Benchmarking Metrics

The Peer Group was compared to the Company using the following measures:

- » Size indicators
  - — Customers
  - — Revenues
  - — Net plant in service
  - — Employees
- » Asset metrics
  - — Net plant/ MWh
  - — Net plant/employee
- » Financial metrics
  - — Revenues/customer
  - — Revenues/employee

C. Assessment Process

The process deployed by Navigant Consulting involved the following key steps:

- » Confirm the City's objectives for the O&M cost reasonableness review,
- » Meet with City and Company representatives to establish schedule and communication processes to obtain key Company data and discuss findings,
- » Prepare requests for financial and performance data from the Company,
- » Obtain industry data for utilities in the Peer Group,
- » Tabulate Company and Peer Group data and prepare comparisons; for each area, identify the nature of the operating expense, the range of reasonableness based on the Peer Group, and how the Company performed compared to the Peer Group

» Meet with the City and the Company to discuss initial comparisons,
» Obtain supplemental information for the Company and finalize assessment
» Present findings from the assessment to the City and the Company, and
» Finalize Report on O&M cost assessment following receipt of comments from the City and the Company

IV. SUMMARY FINDINGS

Overall, Navigant Consulting found that EPE's O&M costs were reasonable.

» EPE's total O&M costs per customer were slightly lower (i.e., less money is spent per customer) than the Peer Group average.

» EPE's gas and coal steam generation O&M costs per MWh generated were higher (i.e., more money was spent per MWh generated) than the Peer Group average.
  — EPE's steam generation portfolio included a number of old units which require a greater level of maintenance.

» Transmission O&M costs per line mile were lower than average; but not as low as the Peer Group top quartile.

» Distribution O&M per customer were lower than average and within the Peer Group top quartile.
  — Reliability indicators (e.g., SAIFI, SAIDI) were low (i.e., good) compared to the Peer Group.

» Customer Care O&M per customer were lower than average and within the Peer Group top quartile.
  — Customer satisfaction scores were relatively high (i.e., good) along most indicators...although in 2005 they dropped.
  — EPE was in the 2nd quartile (out of about 100 utilities) in customer satisfaction.

» EPE's administrative and general ("A&G") O&M costs were higher than the Peer Group average but this appeared to be attributable to past allocation problems between A&G accounts and distribution and customer care accounts.
  — Too much was allocated to A&G and too little was allocated to customer care and distribution.
  — One of the purposes of the new Oracle accounting system, installed and operating as of mid-2005, was to address this problem.

» EPE's plant was highly depreciated (compared to Peer Group companies) due to the acceleration of the amortization of nuclear production plant and nuclear plant write-offs.

» EPE's capitalization and expense policies (as written) were standard, and no concerns were identified regarding these policies.

» EPE did not have an explicit, targeted cost-cutting program.
  — EPE reported that it had not targeted specific cost cutting initiatives aimed at reducing operating expenses but instead managed and controlled expenses through its budgeting process.
  — In certain key areas (T&D and customer care), EPE's costs were already low, reducing the potential need for any major cost cutting initiatives.

» EPE's employee-to-customer ratio was among the lowest in the Peer Group.
  — Like most utilities, EPE faces an aging workforce...but does not currently have in place explicit succession planning programs to address this issue. The Company reported that it has plans to launch a Workforce Risk Assessment to evaluate these challenges.

» EPE is considering many new systems which have been in place at other utilities for years which could lower costs in the longer term, including:
  — GIS
  — Outage Management System
  — Customer Accounting/Information System
  — Outsourcing of payroll

V. BASIS FOR SUMMARY FINDINGS

Table 1 offers a high level perspective of the Company's O&M cost and proficiency metrics for calendar year 2005.

Table 1

	EPE	Peer Group Average	Peer Group Top Quartile	Gap between EPE and Average (%)*	Gap between EPE and Top Quartile* (%)
O&M/Customer	$512	$526	$451	None	12%
O&M/Employee ($000)	$173	$150	$104	13%	40%
O&M/MWh	$26	$19	$14	26%	47%
Employees/ Thousand Customers	3.0	3.8	2.7	None	9%
O&M/ Utility Revenue	22%	23%	18%	None	19%

» Gaps have been calculated as the percentage of cost reduction needed by EPE to make it to the average or top quartile. Thus, EPE would have to reduce total O&M costs/customer by 12 percent to make it from the current $512 per customer to $451 per customer to be in the top quartile.

» EPE's O&M/MWh average is impacted as a result of EPE having a smaller average level of MWh sales per customer.

Table 2

Key EPE Statistics for 2002-2005

	2002	2003	2004	2005	CAGR*
Retail Revenues ($M)	$580	$576	$617	$710	7%
Retail Customers	313,953	320,180	328,779	337,621	3%
Capital Expenditures ($M)	$71.3	$83.4	$76	$94.2	10%
Operating Expenses**	$208.7	$210.2	$211.1	$219.5	3%
Employees	993	977	990	998	0%
Miles of Transmission Lines	1,984	1,985	1,761	1,738	-4%

» EPE's annual operating expenses increased at about the rate of inflation since 1997, or at about a 3 percent compound annual growth rate ("CAGR").

» A&G represents a relatively high proportion of EPE's total O&M costs but when compared against EPE's relatively low distribution and customer care costs they balance out.
- — A&G plus Customer Care plus Distribution equals 48 percent of total O&M for EPE and 48 percent of total O&M for the Peer Group average.
- — EPE's new Oracle-based accounting system, installed in mid-2005, appears to be allocating costs more appropriately.
- — A decline in A&G and increase in customer care and distribution suggest a trend towards more accurate accounting but the accounting system had been installed too recently to make a full assessment.

» EPE's annual capital expenditures have increased substantially since 1997, driven by equipment replacements at Palo Verde and growth of the distribution system to serve new customers.
- — EPE's capital expenses have increased at a compound annual rate of about 8 percent since 1997.

» EPE's capital expenditures, as a portion of total expenditures, has generally been lower than the Peer Group average for the years 2002-2005.

A. *Generation Metrics*

As shown in Table 3, EPE's Generation O&M costs were more expensive per MWh than the Peer Group in 2005.

Table 3

	EPE	Peer Group Average	Peer Group Top Quartile	Gap between EPE and Average (%)	Gap between EPE and Top Quartile (%)
Steam O&M/ Steam MWh	$8.4	$6.4	$4.7	24%	44%
Nuclear O&M/ Nuclear MWh	$11.2	$27	$12.9	None	None
Total O&M/ Total MWh	$10	$7.2	$4.8	28%	52%

» Gas and coal steam generation costs per MWh were higher than average; whereas nuclear generating costs per MWh were lower than average.

» Steam generating O&M costs per MWh increased at about 7 percent compounded annually since 1997.
  — EPE steam generation O&M costs were heavily impacted by maintaining the old Rio Grande and Newman gas-fired units.

» EPE nuclear O&M per MWh increased at a 6 percent compound annual growth rate for the period 1997 to 2005.
  — Despite this level of cost increase, EPE nuclear O&M costs per MWh were lower than the Peer Group average and within the top quartile.

B. *Transmission System Metrics*

As shown in Table 4, EPE's transmission O&M costs were lower than the Peer Group average for 2005.

Table 4

	EPE	Peer Group Average	Peer Group Top Quartile	Gap between EPE and Average (%)	Gap between EPE and Top Quartile (%)
Trans. Operation Cost/Line Mile	$5,049	$6,893	$3,349	None	34%
Trans. Maintenance Cost/Line Mile	$992	$1,990	$1,069	None	None
Total Trans. O&M Cost/ Line Mile	$6,041	$8,883	$4,418	None	27%

» EPE had a high reliance on its transmission system for the import of power.

» EPE benefits from having more moderate weather conditions than other Peer Group companies (limited ice, limited destructive winds, etc.).

» EPE must maintain many miles of remote transmission lines.

C. *Distribution System Metrics*

As shown in Table 5, EPE's distribution O&M costs were lower than the Peer Group average and within the top quartile for 2005.

Table 5

	EPE	Peer Group Average	Peer Group Top Quartile	Gap between EPE and Average (%)	Gap between EPE and Top Quartile (%)
Distribution Operation Cost/ Customer	$33.9	$34.8	$28.8	None	15%
Distribution Maintenance Cost/ Customer	$18.8	$40.3	$28.4	None	None
Total Distribution O&M Cost/Customer	$52.7	$75.1	$57.2	None	None

» Since 2002, EPE's distribution O&M costs per customer had risen only at a 2 percent compound average growth rate.

» EPE's distribution reliability statistics reflect system performance well above most of the Peer Group companies.

D. *Customer Care Metrics*

As shown in Table 6, EPE's Customer Care O&M cost benchmarks were in the top quartile of the Peer Group in 2005.

Table 6

	EPE	Peer Group Average	Peer Group Top Quartile	Gap between EPE and Average (%)	Gap between EPE and Top Quartile (%)
Cust. Account Expenses/ Customer	$32.5	$41.8	$33.7	None	None
Cust. Svc and Info Expenses/ Customer	$1.4	$13.5	$2.1	None	None
Sales Expenses/ Customer	$0.1	$4.0	$0.1	None	None
Total Customer Care Expenses/ Customer	$34.0	$59.3	$35.9	None	None

» Customer Care O&M costs per customer had generally declined over the last 10 years.

» EPE ranked high in most metrics in the annual Market Strategies, Inc. customer satisfaction survey of about 100 utilities annually.

E. Administrative and General Metrics

As shown in Table 7, EPE's A&G O&M cost benchmarks were higher (i.e., worse) than the average of the Peer Group in 2005.

Table 7

	EPE	Peer Group Average	Peer Group Top Quartile	Gap between EPE and Average (%)	Gap between EPE and Top Quartile (%)
A&G Salaries/ Customer (920)	$57.7	$49.0	$28.9	15%	50%
A&G Outside Services/ Customer (923)	$28.9	$19.7	$11.2	32%	61%
Total A&G Expenses/ Customer**	$172.6	$121.6	$85.3	36%	51%

» The high A&G costs were largely balanced out by EPE's low Customer Care and Distribution costs; the new Oracle System is expected to address the allocation of costs by more appropriately tracking the source of each cost item.

» A&G costs had been driven both by increases in consulting and legal fees, as well as by historical accounting practices.

F. Plant in Service

» EPE's plant in service had the highest proportion of depreciated assets in the Peer Group.
- About 60 percent of EPE's total plant was depreciated, higher than all companies in the Peer Group.
- Over the last ten years, EPE accelerated the amortization of nuclear production plant and wrote off nuclear plant costs
- As a result, EPE's nuclear plant was approximately 70 percent depreciated even though it is less than 50 percent through its expected service life
- The last major new non-nuclear generating plant construction was nearly 30 years ago

» EPE's capitalization versus expense policies were standard for the industry.