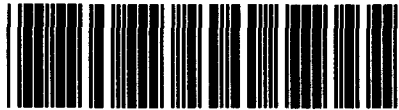


Control Number: 33309



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SOAH DOCKET NO. 473-07-0833  
PUC DOCKET NO. 33309

APPLICATION OF AEP TEXAS  
CENTRAL COMPANY FOR  
AUTHORITY TO CHANGE RATES

§  
§  
§

BEFORE THE  
STATE OFFICE OF  
ADMINISTRATIVE HEARINGS

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**AEP TEXAS CENTRAL COMPANY'S PROPOSED FINDINGS OF FACT,  
CONCLUSIONS OF LAW AND ORDERING PARAGRAPHS**

**PROPOSED FINDINGS OF FACT**

**I. Procedural History**

1. TCC filed its application for authority to increase its transmission and distribution (T&D) rates on November 9, 2007, requesting an overall increase of approximately \$62.7 million. As a result of the establishment of changed base rates in this proceeding, TCC is also entitled to terminate approximately \$20 million in credits to customers heretofore provided to customers via separate riders approved in connection with the Commission's approval of the AEP/CSW merger in Docket No. 19265.

2. The Commission referred this proceeding to SOAH on November 4, 2007. The Commission issued its Preliminary Order setting forth the issues to be addressed in this proceeding on December 19, 2006.

3. The following parties were granted intervention in Docket No. 33309: Alliance for Retail Markets (ARM); Cities served by TCC (Cities); City of Garland; Commercial Customer Group (CCG); CPL Retail Energy, L.P. (CPL); Efficiency Texas; Federal Executive Agencies (Department of the Navy); Occidental Power Marketing, L.P.; Office of Public Utility Counsel (OPC); Reliant Energy Retail Services, LLC; South Texas Electric Cooperative; Sharyland Utilities, L.P.; State of Texas; Texas Cotton Ginners' Association; Texas Industrial Energy Consumers (TIEC); Texas Legal Services Corporation (TLSC); Texas Ratepayers Organization to Save Energy (Texas ROSE); Texas State Association of Electrical Workers; Oncor Electric Delivery Company; TXU Energy, Wholesale and Power Companies; and Wal-Mart Stores Texas, L.P. and Texas Retail Energy LLC (Wal-Mart).

4. TCC timely filed appeals with the Commission of the rate ordinances of the municipalities exercising original jurisdiction within its service territory. All such appeals were consolidated for determination in this proceeding.

5. TCC's application is based on a test year ending June 30, 2006.
6. On January 26, 2007, TCC filed an update to its rate filing that reduced its overall rate increase request by approximately \$1.6 million.
7. When TCC filed its rebuttal case, it unilaterally decreased its total requested T&D base rate increase to approximately \$50 million, a reduction of approximately \$12 million from its initial request. This reduction included the impact of the January 26<sup>th</sup> update, as well as other reductions agreed to by the Company as a result of changed circumstances since its initial filing, or based on its review of staff and intervenor positions.
8. The hearing on the merits commenced on April 12, 2007 and lasted 17 days, concluding on May 4, 2007.
9. The notice provided in this case by TCC complies with P.U.C. PROC. R. 22.51.

## **II. Overview of the Case**

### **III. Rate Base**

10. TCC's used and useful total transmission plant in service is \$944,552,252 and its used and useful transmission plant in service net of accumulated depreciation is \$661,911,522.
11. TCC's used and useful total distribution plant in service is \$1,719,634,015 and its used and useful distribution plant in service net of accumulated depreciation is \$1,135,195,148.

#### **1. Prepaid Pensions**

12. TCC included in rate base a pension prepayment asset of \$112.4 million.
13. The pension prepayment asset arises under generally accepted accounting principles (GAAP) in accordance with Statement of Financial Accounting Standards No. 87 (SFAS 87) and represents the amount by which contributions to the pension fund exceed the accumulated pension obligations.
14. Investment income on the pension prepayment asset reduces pension cost calculated under SFAS 87. As a result of the pension prepayment asset, pension cost under SFAS 87 was \$12.5 million lower in 2006, and pension cost included in cost of service in this case is lower by that amount, than had the pension prepayment asset not been on TCC's books.
15. Accounting in accordance with GAAP requires that both the balance sheet and income statement effects be taken into account.

16. The pension prepayment asset of \$112.4 million benefits customers, represents funds provided by investors, was prudently incurred, and should be included in rate base.

## **2. ADFIT**

17. ADFIT should not be increased by the exclusion of certain items in Account 190 from the calculation of ADFIT as recommended by OPC witness Effron and Cities witness Kollen. All of TCC's operations and maintenance (O&M) and administrative and general (A&G) expenses are included in the cash working capital calculation. Therefore, the leads and lags in paying these items, which give rise to the amounts recorded in Account 190 identified by witnesses Effron and Kollen, have been appropriately included in the calculation of rate base through this process.

18. ADFIT of \$323.9 million should be included in rate base.

## **3. Reclassification of CWIP**

19. In arriving at its adjusted test-year-end rate base, TCC reclassified \$7.3 million in transmission projects that were classified as construction work in progress (CWIP) and that had not been closed out to plant-in-service as of June 30, 2006, but which were actually providing service to customers as of that date. TCC also removed from rate base allowance for funds used during construction (AFUDC) of \$368,625 related to the transmission projects that were reclassified.

20. The reasons given by Cities witness Kollen for recommending rejection of the \$7.3 million reclassification lack merit for the reasons discussed by TCC witness Hamlett.

21. The \$7.3 million reclassification of these projects to plant-in-service is reasonable and should be adopted.

22. The alternative recommendation of Cities witness Kollen that \$12.6 million in construction accounts payable should be applied to reduce rate base lacks merit and should not be adopted. The construction accounts payable are included in TCC's cash working capital calculation. Accordingly, the leads and lags associated with these construction accounts payable are appropriately included in the calculation of rate base.

## **4. Affiliate Capital Costs**

23. TCC's affiliate capital costs are reasonable, necessary, and are no higher than charges for the same or similar services to other affiliated companies or non-affiliated companies.

## **5. Debt Restructuring Costs**

24. TCC included in rate base \$10.2 million in debt restructuring costs related to business separation in accordance with PURA § 39.051. TCC also included in cost of service annual amortization expense of \$914,892 for amortization of these debt restructuring costs over a 15-year period.

25. TCC's treatment of these debt restructuring costs conforms to the determinations the Commission made regarding these costs in its orders in Docket Nos. 22352 and 28840.

26. Cities witness Kollen's challenges to the rate base treatment of these debt restructuring costs and to the amortization of these costs to cost of service over a 15-year period are precluded by the Commission's orders in Docket Nos. 22352 and 28840, and Mr. Kollen did not offer any changed circumstances that might justify reconsideration by the Commission of its prior determinations regarding these costs.

## **6. Cash Working Capital**

27. For the reasons set forth in the direct testimony of TCC witness Randall W. Hamlett and the rebuttal testimony of TCC witness Jay Joyce, TCC's proposed cash working capital of \$2,766,202 for distribution and (\$4,968,142) for transmission is reasonable and should be adopted.

## **7. SFAS 143 AROs**

28. Beginning with calendar year 2005, TCC was required to implement for financial reporting purposes accounting for legal asset retirement obligations (AROs) associated with the cost of removal of asbestos from buildings in accordance with Statement of Financial Reporting Standards No. 143 (SFAS 143).

29. In its filing, TCC incorporated appropriate accounting changes for ratemaking purposes to account for the AROs associated with the cost of removal of asbestos from buildings in accordance with SFAS 143. This involved the establishment of offsetting ARO assets and liabilities, the inclusion of SFAS 143 depreciation and accretion in cost of service, and the exclusion of the cost of removal of asbestos from buildings from the net salvage component of the calculation of depreciation rates for Account 390.

30. The reasons given by Cities witness Kollen for recommending rejection of accounting in accordance with SFAS 143 for the cost of removal of asbestos from buildings lack merit for the reasons discussed by TCC witness Hamlett.

31. Use of SFAS 143 accounting for ratemaking purposes for the cost of removal of asbestos from buildings aligns the regulatory treatment with GAAP, furthers the objectives of P.U.C. SUBST. R. 25.72(a) of uniform accounting by electric utilities, eliminates the potential for confusion or miscomprehension when regulatory accounting deviates from financial accounting over time, and will not hinder the Commission's ability to oversee TCC's legal obligations regarding costs of removal of asbestos from buildings or ability to determine how the cost of non-ARO items will be treated for ratemaking purposes.

#### **8. Uncontested Issues**

### **IV. Return**

#### **1. Rate of Return on Equity**

32. A return on equity of 10.75% will allow TCC a reasonable opportunity to earn a reasonable return on its capital investment.

33. TCC's energy conservation efforts, the quality of its services, the efficiency of its operations and the quality of its management are excellent and support the return on equity authorized by this order.

34. The ROE recommendations of the various witnesses to this case are as follows:

<u>Hadaway</u>	<u>Lain</u>	<u>Gorman</u>	<u>Szerszen</u>	<u>Hill</u>
10.75%	9.75%	9.7%	9.6%	9.0%

35. The return on equity proposed by TCC witness Dr. Hadaway is consistent with the benchmark range of returns on equity authorized by other regulatory agencies in 2005 and 2006.

36. The return on equity proposed by Dr. Hadaway is consistent with the level of financial risk associated with TCC's capital structure.

37. A reasonable application of the discounted cash flow, risk premium and capital asset pricing models provided by the witnesses in this case supports TCC's proposed return on equity of 10.75%.

38. The growth rates used by Dr. Hadaway in his discounted cash flow model are more reasonable than those of the other return on equity witnesses for purposes of producing the very long term growth parameter required by that model. The reasonableness of Dr. Hadaway's recommendation is further supported by his risk premium model.

39. The risk premium models and capital asset pricing models provided by Intervenor and Staff witnesses are more in line with the return on equity proposed by Dr. Hadaway, particularly after recognizing the errors in those models identified by Dr. Hadaway.

## **2. Cost of Debt**

40. On rebuttal testimony, TCC presented a revised pro forma cost of debt of 5.8586% based on updated information resulting from the retirement and refunding its debt using the proceeds of the securitization approved in Docket No. 32475.

41. The \$1.7 million in debt issuance costs sought to be excluded by OPC witness Szerszen were not incurred in connection with the issuance of transition bonds and, accordingly, do not qualify to be included in “qualified costs” of the securitization under PURA § 39.302(4). These debt issuance costs properly are included in the cost of debt calculation.

42. Inclusion of an additional year’s amortization of loss on reacquired debt in the cost of debt calculation, as proposed by OPC witness Szerszen, violates the test year concept, as it would attempt to reach out to September 2007 to make a single adjustment for one item reducing the cost of debt without considering other changes that would increase the return component, such as the substantial capital additions made by TCC since June 30, 2006.

43. Cities witness Kollen’s recommended modification to the level of debt used in calculating cost of debt is inconsistent with both P.U.C. SUBST. R. 25.231(c)(1)(C)(i) and the Commission’s rate filing package instructions that require the actual cost of debt to be used. Also, it is not unusual for there to be a deviation between a utility’s outstanding debt and its T&D rate base. In TCC’s case, this deviation can be explained by the fact that TCC is in the process of completing the transition to retail customer choice, including passing through to customers the \$315 million in ADFIT benefits quantified in Docket No. 32475 as part of the restructuring transition process.

44. TCC’s cost of debt for purpose of this docket is 5.8586%.

## **3. Capital Structure**

45. The appropriate capital structure for purposes of setting rates in this proceeding consists of 60% debt and 40% equity.

46. A 60/40 capital structure is consistent with existing Commission precedent for T&D utilities.

47. A 60/40 capital structure is consistent with current rating agency expectations for TCC.

#### 4. Overall Rate of Return

48. TCC's overall rate of return is as follows:

	<u>% of Total Capitalization</u>	<u>Cost of Capital Rate</u>	<u>WACC (%)</u>
Long Term Debt (includes Preferred Stock)	60.00%	5.8401%	3.5040%
Common Equity	40.00%	10.7500%	<u>4.3000%</u>
Total	100.00%		7.8040%

#### V. Cost of Service

##### 1. Affiliate Costs

49. TCC is a wholly owned subsidiary of American Electric Power Company.

50. AEPSC is a service company that provides a wide variety of operations and support services to TCC.

51. During the test year, TCC engaged in transactions with AEPSC and other affiliates.

52. TCC's affiliate costs for the following classes of service are reasonable, necessary, and are no higher than charges for the same or similar services to affiliate companies or non-affiliated companies.

Customer Service	\$15,957,265
Distribution	5,959,207
Transmission	4,071,691
External Affairs	1,155,186
Regulatory	2,673,374
Texas Administrative Services	877,284
Information Technology	5,236,279
Business Logistics	1,893,020
Human Resources	2,337,687
Finance, Accounting, Strategic Planning	8,660,387
Internal Support	1,681,122
Pro-Forma Adjustments	(3,033,049)
Safety, Environmental, Internal Audit	2,757,612



Legal	2,355,147
Corporate Communications	764,721
Non-AEPSC Billings	<u>1,186,588</u>
Total	<u>\$54,533,521</u>

53. The application of the Total Asset allocation factor to TCC by AEPSC, which includes TCC's securitized regulatory assets, is reasonable and results in charges to TCC which are no higher than charges for the same or similar charges to other affiliated companies or non-affiliate companies.

54. For the reasons set forth in the rebuttal testimony of TCC witness Sandra S. Bennett, the adjustment proposed by Staff witness Candace Romines regarding the bill review process utilized by TCC is unreasonable and should not be adopted.

**2. Labor Expenses** The compensation packages that the Company offers its employees include a base payroll amount as well as annual and long term incentive compensation portions. All portions are part of an overall compensation package that is designed to be competitive in the marketplace and allow the Company to attract and retain qualified individuals as employees.

55. The Company's request to include the test year target level of annual and long term incentive compensation expense in cost of service is reasonable and should be approved.

56. TCC annualized base labor expense by using the actual employees on the payroll in the last pay period of June 2006 and applying the capital/O&M ratio for the test year to the resulting annualized amount.

57. The adjustment recommended by Cities witness Cannady to direct regular base labor expense, based on the premise that the increase in wages and salaries should not exceed the average merit increase in wages and salaries, lacks merit for the reasons provided by TCC witness Hamlett.

58. TCC's method of determining regular base labor expense is reasonable and appropriate. The fact that it produces a higher overall average increase in base pay than the average merit pay increase is attributable to promotions and craft step progressions granted certain employees, which incorporate higher increases than the average merit increase.

59. TCC based its requested overtime component of labor expense on the test-year amount actually incurred and the capital/O&M ratio for the test year.

60. The adjustments to TCC's overtime expense recommended by Staff witness Jacobs and Cities witness Cannady lack merit for the reasons provided by TCC witnesses Hamlett, Gordon, and Pasternack. These adjustments were based on the erroneous assumption that the test-year level of overtime expense is excessive and incorporated, among other methodological flaws, a mismatch of the time period used to calculate the overtime expense with the O&M/capital ratio applied to such period.

61. The amount of overtime expense requested by TCC is reasonable, necessary, and not excessive. The record establishes that the test-year overtime expense is representative of an ongoing amount.

62. TCC annualized AEPSC base payroll by using actual employees on the payroll in the last pay period of June 2006 and allocating the annualized amount to TCC based on the allocation of the AEPSC payroll to TCC for the first six months of 2006.

63. Cities witness Cannady's recommended adjustment to TCC's annualized AEPSC base payroll lacks merit for the reasons provided by TCC witness Hamlett.

64. TCC's method of annualizing AEPSC base payroll properly accounts for the transfers as of January 1, 2006, of certain employees from AEPSC to the operating companies, including TCC, and is reasonable and appropriate. This method properly captures not only the transfer of employees, but also other changes in AEPSC employment during the first six months of 2006.

### **3. Group Insurance Expense**

65. TCC annualized group insurance expense using the June 2006 amount. TCC's adjustment took into account the portion of such expenses capitalized and adjusted cost of service only for the portion expensed.

66. The adjustments to group insurance expense recommended by Cities witness Cannady lack merit for the reasons discussed by TCC witness Hamlett. Ms. Cannady used selective periods as the basis for her proposed adjustments and mismatched the capital/O&M ratio to these periods.

67. TCC's method for annualizing group insurance expense is reasonable and appropriate.

### **4. Savings Plan Expense**

68. TCC annualized savings plan expense using the amount for June 2006. The objective of TCC's adjustment was to take into account the portion of such expenses capitalized and to adjust cost of service only for the portion expensed. On rebuttal, TCC stated that it had found an error

in the calculation of its savings plan expense and that the correct amount is \$1,807,781, instead of \$1,361,320 as included in its initial filing.

69. The adjustment to savings plan expense that Cities witness Cannady recommended lacks merit for the reasons discussed by TCC witness Hamlett. Witness Cannady eliminated September from the periods she selected as the basis for her adjustment, but did not account for the fact September has three pay periods, which means that her annualized amount lacked two pay periods.

70. TCC's method for annualizing savings plan expense is reasonable and appropriate. The corrected annualized adjusted test year amount for savings plan expense of \$1,807,781 should be included in cost of service.

#### **5. Pension Expense**

71. Pension expense of \$1,627,376, which reflects a reduction of \$456,000 for negative pension expense under SFAS 87 related to former generation employees, is reasonable and necessary and is in accordance with PURA § 36.065.

#### **6. OPEB Expense**

72. In its application, TCC included an adjusted test-year amount of \$5,953,937 for postretirement benefits under Statement of Financial Accounting Standards No. 106 (SFAS 106), which included \$886,264 in SFAS 106 transition adjustment amortization related to former generation employees in accordance with PURA § 36.065.

73. Cities witness Kollen recommended that the \$886,264 in SFAS 106 transition adjustment amortization related to the former generation employees be disallowed. This recommendation lacks merit for the reasons discussed by TCC witness McCoy.

74. Both the legislative bill analysis of PURA § 36.065 and the record of the accounting profession's consideration of "pensions and other postemployment benefits" establish that this term is intended to include pensions under SFAS 87, postretirement benefits under SFAS 106, and postemployment benefits under Statement of Financial Standards No. 112 (SFAS 112). The legislative bill analysis for PURA § 36.065 specifically refers to "retiree health care costs" as being included in the costs intended to be covered by that statutory provision. Postretirement health care costs are the principal component of SFAS 106 postretirement benefits.

75. In the event the negative pension costs of \$456,000 for the former generation employees are included in cost of service in accordance with PURA § 36.065, Mr. McCoy identified

additional SFAS 106 postretirement benefit costs of \$564,736 related to the former generation employees that should be included in cost of service.

76. Postretirement benefits under SFAS 106 of \$6,518,673, which include \$1,451,000 in postretirement benefits under SFAS 106 related to the former generation employees, are reasonable and necessary and should be included in cost of service. Such inclusion is in accordance with PURA § 36.065.

#### **7. Catastrophe Reserve**

77. TCC proposed a catastrophic property damage loss self-insurance program with an annual accrual of \$3,913,342 and a target reserve of \$22 million based on a catastrophe model that modeled TCC's risk of property loss from hurricane damage.

78. TCC witness Wilson, a qualified independent insurance consultant, presented a cost/benefit analysis of TCC's proposed self-insurance plan. The preponderance of the evidence demonstrates that TCC's proposed self-insurance program is a lower-cost alternative than commercial insurance and the customers receive the savings of the self-insurance plan.

79. TCC's requested catastrophic property damage loss self-insurance program which involves an annual accrual of \$3,913,342 and a target reserve amount of \$22 million is in the public interest and in accordance with PURA § 36.064 and P.U.C. SUBST. R. 25.231(b)(1)(G).

#### **8. Distribution O&M Expenses**

80. It is inappropriate to single out a particular activity within maintenance expense and focus on whether there will be continued spending on that particular activity because costs will vary from year to year between activities while the overall maintenance costs remain the same or increase.

81. With the removal of the payment to the Public Utilities Board of Brownsville, TCC's test year amount of Distribution Station Maintenance expense is reasonable and necessary and should not be further adjusted.

82. For the reasons set forth in the rebuttal testimony of TCC witness Harry Gordon, the adjustment to TCC's requested distribution O&M expenses regarding miscellaneous distribution operations expense proposed by OPC witness David Effron should not be adopted.

83. For the reasons set forth in the rebuttal testimony of TCC witness Harry Gordon, the adjustment to TCC's requested distribution O&M expenses regarding its vegetation management expense proposed by OPC witness David Effron should not be adopted.

84. TCC's proposed level of distribution O&M expense is reasonable and necessary.

#### **9. Transmission O&M Expenses**

85. The benchmarking studies presented by TCC, as well as its evidence of budget and cost controls, support the reasonableness and necessity of its transmission O&M expenses.

86. It is inappropriate to single out a particular activity within maintenance expense and focus on whether there will be continued spending on that particular activity because costs will vary from year to year between activities while the overall maintenance costs remain the same or increase.

87. There are a number of reasons that explain the increasing maintenance expense TCC is incurring: increased national focus on maintenance arising from the August 2003 Northeast blackout and the Energy Policy Act of 2005; the increasing size of the transmission system; significant increases in the cost of materials and labor; and the overall aging of the system.

88. TCC's proposed level of transmission O&M expense is reasonable and necessary and should not be adjusted.

#### **10. Energy Efficiency Costs**

89. **[assuming a cost recovery factor is rejected]** TCC's cost of service should include \$6,334,949 in energy efficiency costs, equal to the costs TCC incurred in calendar year 2006.

90. TCC's test year energy efficiency costs were not representative of its ongoing costs, and it is inappropriate to reach back to its calendar year 2005 costs or to impose a penalty in proportion to TCC's achievement of its energy efficiency goal

#### **11. Depreciation Expense**

91. In its application, TCC submitted a depreciation study based on plant-in-service as of December 31, 2005. This study reduced TCC's depreciation rates relative to the rates adopted by the Commission in Docket No. 28840.

92. Based on the testimony filed by Staff and Cities, TCC witness Henderson accepted Cities' recommended service life and survivor curve for two FERC accounts and net salvage for one FERC account. Mr. Henderson also accepted Staff's recommendation with respect to service life and survivor curve for one FERC account. This left differences between TCC and Cities and/or Staff with respect to service life and survivor curve as to seven FERC accounts and with respect to net salvage as to 20 FERC accounts.

93. Where TCC differs with Cities and/or Staff on service life and survivor curve, TCC's recommendation should be adopted. Cities' and Staff's recommendations are primarily based on mathematical goodness of fit. Their recommendations failed to consider the extent to which the curves matched the earlier data where most of the retirement units were exposed to retirements, a factor taken into consideration by TCC witness Henderson.

94. Staff witness Srinivasa's proposed net salvage rates for FERC Accounts 351-357, 361-373, 390, and 397-398 are not reasonable. Mr. Srinivasa recommended a methodology that represents a drastic departure from the Commission's traditional method of determining net salvage, which was followed by both TCC witness Henderson and Cities witness Hughes. Staff witness Srinivasa never has previously recommended the approach he proposed in this docket, the Commission had never adopted it, and, to the best of Mr. Srinivasa's knowledge, no other regulatory authority has done so.

95. Staff witness Srinivasa's approach to net salvage is based on the premise that the inflation embedded in TCC's historical information is too high and not representative of future escalation in cost of removal. However, there is no reason to believe that the inflation embedded in TCC's historical information will not be experienced in the future.

96. Mr. Srinivasa's approach to net salvage is not consistent with the Commission's straight-line concept contemplated by P.U.C. SUBST. R. 25.231(b)(1)(B) and would improperly shift to future customers costs of serving current customers. It is precisely to avoid endless debates on what future inflation will be that the Commission relies on the utility's historical data in the net salvage calculation.

97. Cities witness Hughes' primary recommendation with respect to salvage value for FERC Account 390 was based on Cities witness Kollen's recommendation that for ratemaking purposes, the cost of removal of asbestos from buildings not be accounted for in accordance with SFAS 143 for ratemaking purposes, but continue to be included in net salvage for purposes of calculating the depreciation rate for Account 390. Because TCC's proposal to account for the legal obligations (AROs) related to the cost of removal of asbestos from buildings in accordance with SFAS 143 is reasonable, Cities witness Hughes' primary recommendation for net salvage for FERC Account 390 should be rejected. Cities witness Hughes' alternative recommendation for net salvage for FERC Account 390 is addressed in connection with Cities' recommended treatment of gain from the sale of buildings.

98. The depreciation rates requested by TCC as set forth in TCC Exhibit 66 are reasonable and should be approved. These depreciation rates should be applied to the adjusted plant-in-service as of June 30, 2006, to calculate the reasonable and necessary depreciation accrual expense for cost of service.

## **12. Amortization of Gain from Sale of Buildings**

99. TCC received proceeds of \$2,256,793 from the sale of the buildings and incurred associated costs of removal of \$162,806. TCC included the net amount of \$2,093,987 in the depreciation reserve.

100. TCC removed the proceeds from the sale of the buildings, the associated costs of removal, and the original costs of the buildings from its depreciation study.

101. The approach TCC used is reasonable, comports with the applicable accounting requirements, and provides the full benefit of the sale, including the gain, to customers, through reduction of rate base and associated reduction of the depreciation accrual.

102. Cities witness Kollen recommended an alternative treatment. Under his recommendation, the gain would be removed from the depreciation reserve and would be amortized to cost of service over three years. Mr. Kollen's proposal is not reasonable and should be rejected because it would reduce current rates for a three-year period, by imposing on future customers higher rates than under TCC's treatment.

103. Cities witness Hughes proposed an alternative net salvage rate for FERC Account 390 of 53% in the event Mr. Kollen's recommended amortization of the gain from the sale of the buildings were rejected.

104. Cities witness Hughes' alternative recommended net salvage rate for Account 390 is not reasonable. TCC is not in the business of selling buildings. TCC witness Henderson removed the items related to the sale of the buildings, because such sales are not anticipated to reoccur and leaving the items in the depreciation calculation would inappropriately skew the resulting depreciation rates.

105. A net salvage rate of 53% is not a reasonable alternative to Cities witness Kollen's proposed amortization of \$2 million in gain from the buildings. It would increase the net salvage amount by \$24 million, as an alternative to a proposed treatment of \$2 million, which treatment only alters the pattern of recovery of costs and does not change the costs recovered.

### **13. SFAS 143 Accretion**

106. As part of its implementation for ratemaking purposes of SFAS 143 ARO accounting for the legal obligations related to costs of removal of asbestos from buildings, TCC included an accretion expense which substitutes for the cost of removal of asbestos previously included in the cost of removal for depreciation purposes.

107. Since it is reasonable to implement for ratemaking purposes SFAS 143 ARO accounting for the legal obligations related to costs of removal of asbestos from buildings, the related accretion amount is reasonable and necessary.

### **14. Late Payment Penalties**

108. TCC's application of late payment penalties to its retail electric provider customers was consistently applied during the test year in a manner designed to recover all available late payment penalties. For the reasons set forth in the rebuttal testimony of TCC witness David Hooper, the revenue credit related to late payment penalties proposed by Cities witness Gerald Tucker should not be adopted.

### **15. Third-Party Construction Margins**

109. TCC is exiting the third party construction business, and as a consequence, future revenues will be far below the test year amount.

110. The only active third party construction projects are two projects under the Joint Development Agreement with the Lower Colorado River Authority.

111. The LCRA JDA and ETT are completely separate ventures.

112. It is appropriate to make a known and measurable adjustment to the test year amount of third party construction margins by reducing TCC's test year margin of \$3.3 million down to \$789,714 to more accurately reflect the actual situation that will exist in the future.

113. The remaining margins of \$789,714 should be used to reduce TCC's revenue requirement in this case.

### **16. Federal Tax Issues**

114. TCC is a member of an affiliated group eligible to file a consolidated tax return.

115. The amount of the "fair share" of consolidate federal income tax savings allocated to the Company in accordance with PURA §36.060(a) is zero.

### **17. Ad Valorem Property Taxes**

116. Ad valorem taxes in the amount of \$27,853,898 are reasonable and necessary expenses.



### **18. TCOS Synchronization**

117. The transmission cost of service (TCOS) included in the final distribution cost of service should be synchronized with the transmission rates applied to the TCC distribution function based on the TCOS established for the TCC transmission function as a result of this case.

### **19. Bad Debt Expenses**

118. TCC's historical actual bad debt cost for the test year of \$138,776 should be included in cost of service.

### **20. Rate Case Expenses**

119. No party has raised any contested issue concerning the reasonableness of or recovery of Cities' and TCC's rate case expenses. All issues concerning rate case expense recovery shall be severed and included in Docket No. 34301.

### **21. Uncontested Issues**

## **VI. Energy Efficiency Funding**

120. The recommendation of TLSC/Texas ROSE that TCC be required to implement a five-fold increase in the funding of the TDHCA weatherization program and the Hard to Reach Standard Offer Program considered together is unreasonable and not adopted. This recommendation would severely distort the allocation of energy efficiency funding between low income customers and the other customer classes.

121. The Commission declines to order TCC to implement a five-fold increase in its overall energy efficiency goal and funding. TCC's overall program funding has not been shown to be inadequate, and an increase of this magnitude raises profound cost recovery and related issues that are better addressed in a rulemaking or by the Legislature.

## **VII. Load Research**

122. In Docket No. 28840, TCC was ordered to file TCC-specific load research data in its next rate case, and TCC has complied with that order in this case.

123. TCC employed industry-accepted standard load research practices in developing the load research samples and demand estimates, which accurately represent the TCC rate class populations.

124. The overall result of TCC's load research study is a reasonable estimate of class demands for use in allocating costs in this case

125. The changed load characteristics are a result of actual class usage changes and not a result of issues with the load research study.

126. The final numbers produced by the load research study consistently represent the customers that moved from the non-IDR class to the IDR class as if they were members of the IDR class for the entire test year.

### **VIII. Cost-of-Service Study**

127. In Docket No. 28840, the Commission's Order required TCC to perform a new distribution field study. That study has been completed and its results were used to allocate demand-related distribution costs in the cost-of-service study used in this docket.

128. The cost-of-service studies performed by TCC were performed in a manner that is consistent with that used in TCC's most recent rate case, are reasonable, and should be approved.

#### **1. Accounts 364-368 (Distribution Plant)**

129. It is appropriate to use a 100% demand allocator for distribution accounts 364 through 368 because these costs do not vary directly with the number of customers.

130. There are serious flaws in the minimum-system and minimum-intercept (or zero-intercept) methods for determining a customer component.

131. Wal-Mart's recommended allocation percentages, 30% on customer and 70% on demand, are unsupported estimates and do not reflect the TCC system.

132. Wal-Mart's proposed allocations would cause over a 51% revenue requirement increase to the Secondary  $\leq 10$  kW class and over a 13% increase to the Residential class, based only on an unsupported 30% customer and 70% demand split.

#### **2. Staff's Cost-of-Service Study**

133. Concerns about the accuracy of the Staff's cost-of-service study have been satisfied by the errata filed by Staff witness Christine Wright.

#### **3. IDR Issues**

134. The data in the cost-of-service study supporting the development of charges for IDR-metered customers, the schedules, and workpapers collectively support the changes proposed by TCC for IDR-metered customers.

135. The higher costs of IDR meters as well as the costs of standard Watt-hour meters are "socialized" so that all customers within a class pay the same metering charge, regardless of the type of meter they use.

136. IDR-metered customers receive a higher Customer Charge than non-IDR-metered customers in the same class, primarily due to the complexity of preparing and handling the data from those meters for the IDR-metered customer's bill.

#### **IX. Rate Design**

137. TCC's rate design uses the same customer classes ordered by the Commission in Docket No. 22344, Order No. 40.

138. TCC's proposed textual changes and changes to the standard allowance values in the Facilities Extension Schedule are unopposed and are reasonable.

139. TCC's proposed pilot program for front-of-the-lot subdivisions, as modified by Staff, is reasonable.

140. TCC's request to continue to provide facilities rental services under the Distribution Voltage Facilities Rental Service and System Integral Facilities Rental Service tariff schedules, as updated in this proceeding, until January 1, 2011, is unopposed and is reasonable.

##### **1. Gradualism**

141. The increases assigned to each of the generic rate classes are the result of moving each rate class to unity (*i.e.*, an equalized rate of return or full recovery of allocated costs).

142. The amount of actual data for the Secondary >10 kW class is much greater than before.

143. Since the UCOS cases in 2002, where generic rates were set in accordance with Order No. 40 in Docket No. 22344 (which held that rates should be based on cost), the transmission and distribution utilities in Texas have designed rates on the basis of an equalized cost of service.

144. Applying an across-the-board increase when actual cost data is available is contrary to Commission precedent, unjustified, and should be rejected.

145. An adjustment to the revenue allocation for the intra-class functions is neither necessary nor appropriate.

146. Modification of the customer service, metering, and distribution function revenue requirements unjustifiably strays from the equalized cost-of-service study.

147. TCC's proposed changes to the Customer Charges are based on cost, are consistent with Commission precedent, and should be approved.

## **2. Riders**

148. An energy efficiency cost recovery factor would ensure that TCC recovers only its actual energy efficiency costs, and no double-recovery of costs will occur if all such costs are removed from base rates.

149. TCC's energy efficiency obligations and costs are unique because TCC is a funding conduit for third-party energy efficiency providers, TCC's energy efficiency goal is driven by its growth in demand, over which it has no control, and the purpose of the energy efficiency regime is to promote the public policy goals of conserving energy and reducing energy bills, which are not an intrinsic function of a transmission and distribution utility.

150. TCC's proposal to include in the Transmission Cost Recovery Factor (TCRF) any changes in Transmission Service Provider (TSP) access fees approved after the date the application in this docket was filed and any TSP access fees not approved to be included in TCC's Transmission System Charge is reasonable.

151. It is reasonable to update TCC's base rate charge for transmission system service to include the changes in the wholesale transmission rate that are currently included in the TCRF Rider.

152. TCC's proposed adjustments to its rates to recover specified cost changes outside of a general rate review through the proposed riders are not automatic adjustments to its rates.

153. There are specific instances where riders further certain goals of the Commission or permit the adherence to Commission rules.

154. Collecting costs beyond the utility's control through a rider may allow base rate cases to become more infrequent because general rate cases would not be required as a result of changes in these costs, giving the Company continued incentive to manage and control costs within its control that are not included in riders.

155. Riders provide the REPs with more information regarding the entirety of TDU charges for transmission and distribution service.

156. More information would provide better transparency in TDU charges and allow the REPs more flexibility to form specific retail rate offerings crafted for specific market segments.

157. The proposed MFFA-C Rider will be used to reflect a change to a specific municipality's franchise fee.

158. A municipal franchise fee adjustment that applies to a specific municipality will be applied to bills of retail customers who are located within the specific city's municipal limits.
159. TCC's proposed Rider MFFA-C is reasonable, is consistent with statutory authority, and should be approved.
160. TCC's proposed EECR Rider is modeled after Southwestern Electric Power Company's (SWEPCO's) similar tariff.
161. TCC would recover only its actual energy efficiency costs, no more and no less.
162. Any funds collected in rates must be used for energy efficiency and cannot be diverted to another purpose.
163. The EECR Rider is clearly and specifically authorized by PURA § 36.204(1).
164. TCC has very little control over these costs, because they are ultimately driven by TCC's growth in demand.
165. TCC does not provide the energy efficiency measures itself but instead supplies funding for third parties that provide the measures.
166. Circumstances have changed since Docket No. 28840 given the increased public interest in energy efficiency as a tool to meet rising demand for power.
167. TCC should be allowed to recover its energy efficiency costs through a cost recovery factor, with the annual factor filings and three-year reconciliations that TCC proposes and are currently in place for the similar tariff that SWEPCO has.
168. The amount to include in the initial energy efficiency cost recovery factor is \$6,334,949, which represents both the costs TCC incurred in calendar year 2006 and the amount budgeted for calendar year 2007.
169. TCC's proposed EECR Rider is reasonable, is consistent with statutory authority, and should be approved.
170. The quantification and surcharge of rate case expenses should be severed from this docket.

### **3. Discretionary Service Fees**

171. Discretionary services are services that relate to electric distribution service.
172. The fees for discretionary services are billed to the REPs or distribution end-use retail customers for the cost of performing a specific distribution service requested by the REP or end-use retail customer.

173. The discretionary service fees serve to charge the party that causes the cost to be incurred so that other parties that do not require the service do not have to pay for it through base rates.

174. All TDUs must offer the discretionary services defined in the Standardized Discretionary Services Section of the Tariff.

175. The fees are based on the Company-specific cost to perform each discretionary service.

176. For all categories of discretionary services, the costs were developed by a core discretionary service fee team that performed extensive interviews with the field personnel and other Company personnel responsible for performing and supervising the various distribution services defined by all of the discretionary service fees.

177. The most current salary, labor and materials overheads, transportation cost and materials cost data were used in determining the total average cost to perform each discretionary service.

178. TCC's proposed discretionary fees, including its disconnect and reconnect fees, are reasonable and should be approved.

#### **X. Tariff Formatting and Language**

179. Several areas in the filed Standardized Discretionary Services portion of the Tariff do not conform to the pro forma tariff approved in Project No. 29637.

180. The formatting changes recommended by Staff should be made in order to comply with the Commission's rule.

181. Staff's recommended changes to the proposed Broken Meter Seal and After Hours Temporary Removal fees should be made.

182. Staff's recommended language changes to Section 6.2.3.3.7, Meter Enclosure Seal Breakage, should be approved.

#### **XI. Termination of the ISA Riders**

183. The merger savings and rate reduction riders related to the merger of AEP and CSW terminate with a change in TCC's rates, whether that change is bonded or permanent.

### **PROPOSED CONCLUSIONS OF LAW**

1. TCC is an electric utility as defined by § 31.002 of the Public Utility Regulatory Act (PURA), TEX. UTIL. CODE ANN., and therefore it is subject to the Commission's jurisdiction under PURA §§ 32.001, 33.051, and 36.102.

2. TCC is a T&D utility as defined in PURA § 31.002(19).

3. SOAH has jurisdiction over all matters relating to the conduct of the hearing in this case, including the preparation of a Proposal for Decision pursuant to PURA § 14.053 and TEX. GOV'T CODE ANN. § 2003.049(b).
4. Each municipality in TCC's service area that has not ceded jurisdiction to the Commission has jurisdiction over the application to the extent that the application seeks to change rates for distribution services within each municipality pursuant to PURA § 33.001.
5. TCC provided adequate notice of this proceeding in compliance with P.U.C. PROC. R. 22.51.
6. The effective date of the change in rates approved in this case was extended consistent with P.U.C. SUBST. R. 25.241(i) and by agreement of TCC, consistent with P.U.C. PROC. R. 22.33(c).
7. The return on equity and overall return authorized in this proceeding are consistent with the requirements of PURA §§ 36.051 and 36.052.
8. The rates approved in this proceeding are based on the original cost, less depreciation, of property used by and useful to TCC, consistent with PURA § 36.053.
9. The affiliate expenses included in TCC's rates are consistent with the requirements of PURA § 36.058.
10. PURA § 36.065(a) provides that electric utility rates shall include "expenses for pensions and other postemployment benefits, as determined by actuarial or other similar studies in accordance with generally accepted accounting principles, in an amount the regulatory authority finds reasonable."
11. Generally accepted accounting principles (GAAP) with respect to pension cost are determined in accordance with Statement of Financial Accounting Standards Nos. 87 and 88 (SFAS 87 and SFAS 88).
12. In accordance with GAAP both the income statement and balance sheet effects under SFAS 87 must be recognized.
13. Inclusion in rate base of TCC's pension prepayment asset of \$112.4 million and offsetting accumulated deferred income taxes of \$40.6 million comports with GAAP and PURA § 36.065.
14. The last sentence of PURA § 36.065(a) provides that an electric utility's rates shall include expenses "for pension and other postemployment benefits," "in an amount found

reasonable by the regulatory authority” that are “attributable to the service of employees who were employed by the predecessor integrated electric utility of an electric utility before the utility’s unbundling under Chapter 39 irrespective of the business activity performed by the employee or the affiliate to which the employee was transferred on or after unbundling.”

15. The purpose of the last sentence of PURA § 36.065(a) is to permit an unbundled transmission and distribution utility to include in rates the “pension and other postemployment benefits” related to the employees of its predecessor’s generation function.

16. As used in PURA § 36.065(a) the term “pension and other postemployment benefits” includes pension costs under SFAS 87, postretirement benefits under Statement of Financial Standards No. 106 (SFAS 106), and postemployment benefits under Statement of Financial Standards No. 112 (SFAS 112). The bill analysis for PURA § 36.056 specifically states that it applies to “retiree health care costs,” which are the subject of SFAS 106.

17. No modification would be proper to the rate base treatment or to the 15-year amortization to cost of service of the debt restructuring costs TCC incurred in connection with business separation ordered in Docket Nos. 22352 and 28840.

18. P.U.C. SUBST. R. 25.72(a) requires each electric utility to maintain its accounts in a uniform manner.

19. PURA § 39.302(4) allows “the costs of issuing, supporting, and servicing transition bonds and any costs of retiring and refunding the electric utility’s debt and equity securities in connection with the issuance of transition bonds” to be included in qualified up-front costs of securitization. The costs in the amount of \$1,669,612 initially incurred in issuing Matagorda Navigation District No. 1 Pollution Control Bonds Series 2005 and B in 2005 were not incurred in “retiring and refunding . . . [TCC’s] debt and equity securities in connection with the issuance of transition bonds,” which occurred in late 2006. These costs are properly included in TCC’s cost of debt calculation under P.U.C. SUBST. R. 25.231(c)(1)(C)(i).

20. TCC’s decisions to retire and refund debt using the proceeds of the securitization were prudent under the prudence standard articulated in *Application of Gulf States Utilities Company to Change Rates*, Docket No. 7195, 14 P.U.C. BULL. 1943, 1969-1970, 2429 (CoL 14) (May 16, 1998).



21. P.U.C. SUBST. R. 25.231(c)(1)(C)(i) requires the cost of debt to be “the actual cost of debt at the time of issuance, plus adjustments for premiums, discounts, and refinancing and issuance costs.”
22. PURA § 36.064 permits a utility to self-insure “potential liability or catastrophic property loss, including windstorm, fire, and explosion losses, that could not have been reasonably anticipated and included under operating and maintenance expenses.” The Commission shall approve a self-insurance plan under that section if it finds the coverage in the public interest, the plan, considering all of its costs, is a lower cost alternative to purchasing commercial insurance, and ratepayers receive the benefits of the savings.
23. TCC’s proposed self insurance accrual and reserve comply with PURA § 36.064.
24. Although PURA § 36.201 expressly prohibits an automatic change in rates, this is subject to the exception in PURA § 36.204 that permits the Commission to allow for the timely recovery of conservation and load management costs, or energy efficiency costs.
25. Under PURA § 36.204, TCC’s energy efficiency costs should be timely recovered through a separate cost recovery rider.
26. P.U.C. SUBST. R. 25.342(f)(1)(D)(ii)(III) requires the utility to “credit all revenues received...during the test year after known and measurable adjustments are made to lower the revenue requirement of the transmission and distribution utility...”
27. TCC’s proposal to make a known and measurable change to its test year margin of \$3.3 million and then reduce its revenue requirement by the adjusted margin of \$789,714 complies with the requirements of P.U.C. SUBST. R. 25.342(f)(1)(D)(ii)(III).
28. TCC’s proposed rate design, cost allocation, and its proposed EECR and MFFA-C riders, are consistent with the requirements of PURA §§ 36.003 and 36.004.
29. Termination of the rider credits associated with the Commission’s order in Docket No. 19265, contemporaneous with implementation of bonded rates in this proceeding, is consistent with the provisions of PURA § 36.110 and with the express language of the Integrated Stipulation and Agreement approved by the Commission in Docket No. 19265.

#### **PROPOSED ORDERING PARAGRAPHS**

In accordance with the above findings of fact and conclusions of law, the Commission issues the following:

1. The Proposal for Decision prepared by the Administrative law Judges of the State Office of Administrative Hearings is adopted to the extent consistent with this Order.
2. TCC's application is granted to the extent provided in this Order.
3. TCC shall file tariff sheets consistent with this Order (compliance tariff) no later than 20 days after receipt of this Order. The compliance tariff, and all filings related to it, shall be filed in Tariff Control Number \_\_\_\_\_, and shall be styled: *Compliance Tariff Pursuant to Final Order in P.U.C. Docket No. 33309 (Application of AEP Texas Central Company for Authority to Change Rates)*. The filing shall include a transmittal letter stating that the tariffs attached are in compliance with the order, giving the docket number, date of the order, a list of tariff sheets filed, and any other necessary information. The timetable for review of the compliance tariff shall be established by the P.U.C. ALJ assigned to the tariff. In the event any sheets are modified or rejected, the applicant shall file proposed revisions to those sheets in accordance with the P.U.C. ALJ's notice. The effective date of the tariff shall be as determined in the written notice of approval by the P.U.C. ALJ. All subsequent filings in connection with the compliance tariff (i.e., requests for extensions, textual corrections, revisions) shall be filed in the same Tariff Control Number provided above, and styled as set forth above. After issuance of the final order, no further filings other than those pertaining to a motion for rehearing shall be made in this Docket.
4. The determination of the reasonableness and recovery of rate case expenses and the implementation of the surcharge for recovery of rate case expenses is severed into Docket No. 34301, *Proceeding to Consider Rate Case Expenses Severed From Docket No. 33310 (Application of AEP Texas North Company for Authority to Change Rates)*.
5. All other motions, request for entry of specific findings of fact and conclusions of law, and any other requests for general or specific relief, if not expressly granted herein, are denied.

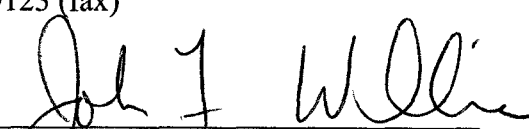
Respectfully submitted,

Larry W. Brewer  
State Bar No. 02965550  
Rhonda Colbert Ryan  
State Bar No. 17478800  
Jerry N. Huerta  
State Bar No. 24004709  
AMERICAN ELECTRIC POWER  
COMPANY, INC.  
400 West 15<sup>th</sup> Street, Suite 1500  
Austin, Texas 78701  
512.481.3321  
512.481.4591 (fax)

John F. Williams  
State Bar No. 21554100  
CLARK, THOMAS & WINTERS,  
A Professional Corporation  
Post Office Box 1148  
Austin, Texas 78767  
512.472.8800  
512.474.1129 (fax)

Philip F. Ricketts  
BRACEWELL & GIULIANI LLP  
111 Congress Avenue, Suite 2300  
Austin, Texas 78701  
512.472.7800  
512.472.9123 (fax)

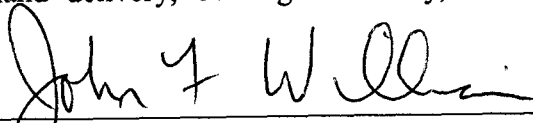
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John F. Williams  
State Bar No. 21554100

ATTORNEYS FOR  
AEP TEXAS CENTRAL COMPANY

**CERTIFICATE OF SERVICE**

I hereby certify that a true and correct copy of the foregoing document was served on all parties of record via U.S. first-class mail, hand delivery, overnight delivery, or facsimile transmission on the 31<sup>st</sup> day of May, 2007.

  
\_\_\_\_\_  
John F. Williams