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DOCKET NO. 33734

APPLICATION OF ELECTRIC TRANSMISSION TEXAS, LLC FOR A CERTIFICATE OF CONVENIENCE AND NECESSITY, FOR REGULATORY APPROVALS, AND INTIAL RATES	§ § § § § §	**PUBLIC UTILITY COMMISSION** **OF TEXAS**

COMMISSION STAFF'S REPLY BRIEF

Respectfully submitted,

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NOW COMES the Staff of the Public Utility Commission of Texas (Staff), representing the public interest, and submits this reply brief and would show as follows:

I. INTRODUCTION

The application that Electric Transmission Texas, LLC (ETT) now asks the Commission to approve is almost unrecognizable compared with what the company originally filed in this Docket. In its Initial Brief, ETT:

- "Agrees" its Return on Equity (ROE) "should be the same" as AEP Texas Central Company (TCC) and AEP Texas North Company (TNC);[1]
- No longer requests an adder of 50 basis points to the ROE for each of its planned transmission projects, but still seeks one for the "initial facilities"[2] it seeks to transfer and others involving new technology;[3]
- No longer requests recovery of $721,738 in formation costs;[4]
- Accepts the dollar value of Staff witness Glenda Spence's proposed depreciation adjustment of $18,632 for the purposes of setting rates in this case, but for accounting purposes asks the Commission to prospectively apply the depreciation rates adopted by the Commission in TCC's pending rate case, Docket No. 33309;[5]
- Accepts the dollar value of Staff witness Ms. Spence's proposed lease and incentive compensation adjustments of $1,846 and $44,700, respectively, but for accounting purposes asks the Commission to prospectively apply the lease expense amount that results from the Commission's decision in TCC's pending rate case.[6]

Despite ETT's eleventh hour attempts to salvage its application, the Commission should deny ETT's application for a certificate of convenience and necessity (CCN) because ETT failed to prove there is a need for a CCN and that current electric service is inadequate. Furthermore, despite ETT's assurances that the proposed transactions are financially sound, it has failed to

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[1] Initial Brief of Electric Transmission Texas, LLC at 2 (Aug. 1, 2007).

[2] The "initial facilities" that ETT seeks to acquire and operate are located in the Laredo area. Staff Exh. No. 2, Direct Testimony of Mohammed Ally at 13 ln. 5-10 (June 18, 2007). They include a Variable Frequency Transformer (VFT), which provides bidirectional power flow between the Electric Reliability Council of Texas (ERCOT) and Mexico, as well as phase-shifting transformers that regulate power flow and Dynamic Reactive Compensation Systems that provide voltage support. *Id.*

[3] Initial Brief of Electric Transmission Texas, LLC at 2 and 35-36 (Aug. 1, 2007). ETT said, "In the future, the Commission should also consider incentives for other innovative transmission projects if: 1. there are demonstrated savings to customers; 2. the facility represents an innovative solution; and 3. the facility presents additional risk associated with new technology." Initial Brief of Electric Transmission Texas, LLC at 36 (Aug. 1, 2007).

[4] Initial Brief of Electric Transmission Texas, LLC at 2 (Aug. 1, 2007).

[5] Initial Brief of Electric Transmission Texas, LLC at 38 (Aug. 1, 2007).

[6] Initial Brief of Electric Transmission Texas, LLC at 38-39 (Aug. 1, 2007).

prove it has firm financing: at the close of evidence, its proposed co-owner, MidAmerican Energy Holdings Company (MidAmerican), had failed to fund its required $15 million equity commitment in ETT.

The Commission should also find that ETT's application for sale, transfer, or merger (STM) is not in the public interest. Contrary to ETT's claim that the Commission must use a "no harm" standard to determine if such transactions are in the public interest, the Commission in past cases has adopted what can be called a "net public benefits" standard. The Commission should find that ETT's STM transactions are not in the public interest because they would not result in net public benefits. Furthermore, even if a "no harm" standard were applied, ETT would fail that test as well, because at best approving its application would result in the same level of service being provided at a higher cost to ratepayers.

If the Commission is inclined to grant a CCN, it should not reach a final decision until the Federal Energy Regulatory Commission (FERC) decides whether it has jurisdiction over ETT.[7]

If the Commission grants a CCN, it should disallow the effect of the STM transactions by setting ETT's ROE no higher than that of TCC in its pending rate case and deny recovery of formation costs, rate case expenses, and make Staff's recommended adjustments for depreciation expenses, lease expenses, and incentive compensation expenses. If in the alternative the Commission approves rate case expenses, it should still deny as a matter of law the Cities' request for up to $202,325 in rate case expenses.

Finally, if the Commission grants ETT's CCN, it should approve a code of conduct and resolve other affiliate issues based on the agreed recommendation of ETT, the Office of Public Utility Council, and Staff.

II. CCN ISSUES

In its Initial Brief, ETT fails to show evidence that there is a need for a CCN, that current electric service is inadequate, or that transfer of "initial facilities" would result in probable

[7] On July 19, 2007, AEP and MidAmerican filed a petition with FERC requesting FERC to declare it would not assert jurisdiction over ETT. FERC Docket No. EL07-83-000 (July 19, 2007). If FERC has jurisdiction over ETT, then the Commission may have no jurisdiction over ETT's rates, because ETT would be a transmission-only utility. Although FERC has had a practice of setting the wholesale transmission rates of TCC, the Commission regulates TCC's transmission costs in its retail delivery rates. Such an erosion of the Commission's ability to regulate

improvement of service or lowering of costs. ETT acknowledges that it must address "whether ETT's requested CCN is necessary for the service, accommodation, convenience, or safety of the public under [PURA] § 37.056(a), taking into account the factors identified in [PURA] § 37.056(c)."[8] PURA § 37.056(c) provides:

> (c) The commission shall grant each certificate on a nondiscriminatory basis after considering:
> (1) the adequacy of existing service;
> (2) the need for additional service;
> (3) the effect of granting the certificate on the recipient of the certificate and any electric utility serving the proximate area;
> (4) other factors, such as:
>
> . . .
>
> (E) the probable improvement of service or lowering of cost to customers in the area if the certificate is granted; and
> (F) to the extent applicable, the effect of granting the certificate on the ability of the state to meet the goal established by Section 39.904(a) of this title.[9]

In its Initial Brief, ETT fails to cite to any evidence indicating that existing electric service is inadequate, and instead tries to recast the issue in terms of what will be needed in the future, stating: "the ERCOT transmission system is adequate to meet present requirements but the need for expansion over the next decade is significant and widely-recognized."[10]

The evidence shows that current electrical service through existing utilities is adequate and there is no need to grant a CCN to ETT.[11] TCC coordinated construction of the initial facilities and has placed them into operation.[12] TCC is operating and maintaining them using TCC staff and contractors, including AEP Service Company (AEPSC).[13] Like TCC, ETT would use TCC and AEPSC personnel to operate and maintain the initial facilities if the CCN is granted. Because TCC is already operating and maintaining the initial facilities and can continue to do so, it cannot be said that ETT's application for a CCN is needed to support a reliable and

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transmission costs in Texas is not in the public interest under PURA, and would be an additional basis for denying the application.

[8] Initial Brief of Electric Transmission Texas, LLC at 18 (Aug. 1, 2007).

[9] PURA § 37.056(c).

[10] Initial Brief of Electric Transmission Texas, LLC at 18 (Aug. 1, 2007).

[11] Staff Exh. No. 2, Direct Testimony of Mohammed Ally at 14 ln. 4-5 and 18-19 (June 18, 2007).

[12] *See* Staff Exh. No. 2, Direct Testimony of Mohammed Ally at 14 ln. 5-7, and at 15 ln. 9-11 (June 18, 2007).

[13] *Id.*

adequate network.[14] Furthermore, the evidence also shows that existing utilities such as TCC and TNC can meet future needs for transmission service.[15] In a deposition, AEP's Michael Heyeck testified that AEP could build the transmission infrastructure within AEP service areas, stating: "AEP will measure up to its obligations with respect to Texas Central and Texas North companies."[16]

In its Initial Brief, ETT also failed to cite any evidence indicating that the transfer of initial facilities would result in probable improvement of service or lowering of costs, as contemplated by PURA § 37.056(c)(4)(E). ETT generally speculated, without citation to the record, that "[e]nhancement of the transmission grid can lower cost and improve service in two ways – first, by relieving congestion and reducing associated costs and, second, by reducing the economic costs and service interruptions that can result from an overloaded grid."[17] These bare assertions should be rejected for three reasons. First, as previously stated, the existing utilities can already meet future needs for transmission service.[18] There will be no better service to existing customers for the first two years, because the services will be provided by AEPSC with or without the transfer of the facilities to ETT.[19] Second, ETT has done no cost-benefit studies,[20] and in its Initial Brief admits that the benefits claimed "do not lend themselves to immediate quantification in the form of short-term rate reductions . . ."[21] Third, rather than lower costs, the evidence shows ETT's costs for service will be higher than that of TCC, [22] and its ability to provide reliable service in the future may be compromised after two years if it loses its O&M contract with AEPSC.[23]

ETT has also failed to produce evidence that it has firm financing to provide continuous and adequate service. In *Application of Corpus Christi Power and Light For a Certificate Of*

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[14] *See* Staff Exh. No. 2, Direct Testimony of Mohammed Ally at 14 ln. 18-19 (June 18, 2007).
[15] *See* Staff Exh. No. 2, Direct Testimony of Mohammed Ally at 14 ln. 4-5 (June 18, 2007).
[16] *See* Staff Exh. No. 2, Attachment C, Workpapers of Mohammed Ally at bates 33 ln.15-19. (June 18, 2007).
[17] Initial Brief of Electric Transmission Texas, LLC at 19 (Aug. 1, 2007).
[18] *See* Staff Exh. No. 2, Direct Testimony of Mohammed Ally at 14 ln. 4-5 (June 18, 2007).
[19] Staff Exh. No. 2, Direct Testimony of Mohammed Ally at 17 lns. 16-18 (June 18, 2007).
[20] Tr. at 129 ln. 21-24 (July 16, 2007).
[21] Initial Brief of Electric Transmission Texas, LLC at 11 (Aug. 1, 2007).
[22] Staff Exh. No. 2, Direct Testimony of Mohammed Ally at 18 lns. 10-11 (June 18, 2007). Staff witness Ally testified that ". . . ETT would provide transmission service in a way that increases costs to customers."
[23] Staff Exh. No. 2, Direct Testimony of Mohammed Ally at 17 lns. 9-10 (June 18, 2007).

Convenience And Necessity In Nueces and San Patricio Counties,[24] Senior Administrative Law Judge Michael O'Malley found that in addition to statutory requirements, CCNs should be granted on a "case-by-case basis" only after considering the general financial strength of the applicant, the applicant's financial needs, and whether the applicant had the financial resources to adequately provide the proposed services. In its Initial Brief, ETT claims it is "well-qualified to provide continuous and adequate service, a standard that some previous utility applicants could not meet."[25] However, at the close of evidence, ETT had no formal business plan and had not adopted a formal capital spending plan outlining the approximately $1 billion investment in future projects that it contemplates.[26] More importantly, ETT lacks firm financing:[27] its proposed 50 percent partner, MidAmerican, has failed to fund its required $15 million equity commitment in ETT.[28]

Historically, the Commission has not approved CCN applications by applicants that failed to show a firm financial plan.[29] Staff witness Lain testified:

> Failing to require a firm financial commitment from a prospective CCN owner would put the public at risk and runs counter to the principle of fairness in the context of the financial investments made by other CCN holders in the state of Texas which are supported by significant equity commitments. . . . ETT has not provided any rationale for failing to have sufficient up-front equity investment from its proposed 50 percent owner, MidAmerican. While I understand that well-managed businesses should direct equity toward the most productive uses, the objective should be balanced with the goal of providing adequate liquidity and a financial cushion to support the construction of capital assets and the operations of the business, especially for a start-up business. Equity financing provides fundamental evidence to lenders, investors, employees, and customers – as well as the Commission

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[24] *Application of Corpus Christi Power and Light For a Certificate Of Convenience And Necessity In Nueces and San Patricio Counties*, Docket No. 19950, Interim Order (March 16, 1999).

[25] Initial Brief of Electric Transmission Texas, LLC at 20 (Aug. 1, 2007).

[26] Staff Exh. 1, Direct Testimony of Richard Lain at 14 ln. 11, 19-20 (June 18, 2007).

[27] Staff Exh. 1, Direct Testimony of Richard Lain at 17 ln. 15-17 (June 18, 2007).

[28] Tr. at 248 ln. 18 through 249 ln. 5 (July 16, 2007).

[29] *See, e.g., Application of Texland Electric Co. for a Certificate of Convenience and Necessity for Texland Generating Units 1, 2, and 3*, Docket No. 3896, Order at 1 (Sept. 23, 1982) (remanding a request for a CCN due to lack of a "firm" financial plan in which it failed to demonstrate an acceptable financial commitment); *Application of Cap Rock Electric Cooperative for a Certificate of Convenience and Necessity for a Proposed Transmission Line*, Docket No. 11248, Examiner's Report (May 6, 1993) (recommending denial or remand of application for a CCN to build new transmission facilities to interconnect with Southwestern Public Service because Cap Rock failed to demonstrate it had adequate capital resources to fund the project).

– that a business is financially sound and capable of meeting its obligations.[30]

ETT's request for a CCN should be rejected because the evidence shows there is no need for a CCN, service is adequate through existing utilities and would cost more under the proposal, and ETT has failed to demonstrate it has a firm financial plan.

III. SALE, TRANSFER, MERGER ISSUES

The Commission should find that the proposed PURA § 14.101 transactions to form, capitalize and transfer assets to ETT are not in the public interest because they result in no net public benefits, and at best would result in the same level of service being provided at a higher cost to ratepayers.

In its Initial Brief, ETT argues that the Commission should use a "no harm" standard when evaluating whether a PURA § 14.101 transaction is in the public interest.[31] ETT cites three LCRA cases as establishing "Commission precedent" that the commission uses a "no harm" standard.[32] None of the cases adopted a "no harm" standard, and in all three cases, the transfer of facilities to LCRA resulted in affirmative benefits to customers due to reduced financing costs, which outweighed any adjustments to O&M costs. Rather than supporting a "no harm," standard, these cases support the proposition that a transfer of facilities should not take place unless it results in net public benefits. ETT also incorrectly asserted that at the hearing on the merits, "many of the parties" in this case "appeared to accept this [no harm] standard."[33]

In *Application of Southwestern Public Service Company Regarding Proposed Business Combination with Public Service Company of Colorado* (hereinafter *Application of SPSC)*, the

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[30] Staff Exh. 1, Direct Testimony of Richard Lain at 17 ln. 17 through 18 ln. 7 (June 18, 2007).

[31] Initial Brief of Electric Transmission Texas, LLC at 7 (Aug. 1, 2007).

[32] Initial Brief of Electric Transmission Texas, LLC at 7 (Aug. 1, 2007), citing *Application for Sale, Transfer, or Merger of Oncor and LCRA Transmission Corp.*, Docket No. 25829, Order at 4 (FoF 22) (Dec. 20, 2002); *Joint Application of AEP Texas North Company and LCRA Transmission Services Corp. to Transfer Certificate Rights and for Approval of Transfer of Facilities*, Docket No. 30451, Order at 6 (FoF 21) (June 20, 2005); *Joint Application of AEP Texas Central Company and LCRA Transmission Services Corp. to Transfer Certificate Rights and for Approval of Transfer of Facilities in Cameron, Dimmit, Hidalgo, Maverick and Starr Counties*, Docket No. 32539, Order at 7 (FoF 23) (Aug. 28, 2006).

[33] Initial Brief of Electric Transmission Texas, LLC at 2 (Aug. 1, 2007). ETT's citations on this point are misleading. For example, ETT cites transcript comments by Mr. Lain on page 417 of the transcript in support of this proposition. Nowhere on the cited page nor in any evidence produced does Mr. Lain or any other Staff witness testify that a "no harm" standard should be applied to this case.

Commission adopted what can be described as a net public benefits standard to determine if a transaction was consistent with the public interest.[34] Rather than merely consider only whether a transaction "would not unduly harm or act as a detriment to the public," the Commission adopted "a more comprehensive public interest standard than articulated in past dockets."[35] The case involved the merger of two companies. To "satisfy the public interest standard" of PURA95, the Commission said:

> a. The merging parties must *do more than promise cost savings*;
> b. The merger should result in *improvement of service* to Texas ratepayers;
> c. The merger should not result in Texas ratepayers bearing merger costs that do not result in corresponding benefits to Texas Ratepayers;
> d. The merger should not be used as a means to evade regulation, but should facilitate regulatory oversight;
> e. The merger should not result in the concentration of market power; and
> f. The merger should not impede on competition.[36]

Thus, to satisfy the public interest standard, an applicant is required to prove the transaction produced net public benefits, such as resulting in improvements of service and doing more than promising savings. Since adopting the "comprehensive public interest standard" in Docket No. 14980, the Commission has consistently considered whether transactions involving the sale or transfer of stock resulted in net public benefits. *See, e.g. Application of Central and South West Corporation and American Electric Power Company, Inc. Regarding Proposed Business Combination,* Docket No. 19265, Order at 1 (Nov. 18, 1999) (finding that the merger of Central and South West Corporation and American Electric Power Company, Inc. met the "comprehensive public interest standard" articulated in *Application of SPSC*).

ETT argues that a "net public benefits" standard should not be applied to this case because that standard was developed for merger cases.[37] ETT argues that this case is not a merger, and "there are no merger synergies that can be quantified or shared."[38] In *Application of Central and South West Corporation and American Electric Power Company, Inc. Regarding*

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[34] *Application of Southwestern Public Service Company Regarding Proposed Business Combination with Public Service Company of Colorado,* Docket No. 14980, Order at 4 (Feb. 14, 1997)(emphasis added).
[35] *Id.*
[36] *Id.*
[37] Initial Brief of Electric Transmission Texas, LLC at 7 (Aug. 1, 2007).
[38] Initial Brief of Electric Transmission Texas, LLC at 7 (Aug. 1, 2007).

Proposed Business Combination, the Commission did not limit the net public benefits standard to merger cases and specifically applied such a "comprehensive public interest standard" to a case involving a "business combination."[39] The case at bar involves two PURA § 14.101 transactions: the transfer of initial facilities, and the sale and transfer of 50 percent of ETT stock to a subsidiary of MidAmerican. The sale of 50 percent of ETT's stock is a "business combination": subsidiaries of AEP and MidAmerican are combining assets to create a new company. Furthermore, there is no reason not to apply the comprehensive public interest standard to this case. As with the stock transactions at issue in prior dockets, the transactions in this docket would involve the change of ownership and control of both stock and facilities to new owners of a utility. Furthermore, unlike the stock transactions at issue in prior dockets, the transactions as proposed in this docket would have immediate, adverse effects on rates.

The proposed transactions meet neither the "net public benefits" standard nor a "no harm" standard. Staff witnesses Mr. Ally testified that the proposed transactions to form, capitalize, and transfer assets to ETT is not in the public interest because they result in no new public benefits and at best will result in the same level of service being provided at higher costs to ratepayers.[40] The initial facilities near Laredo are being completed and operated by TCC.[41] ETT's service is not expected to be better than TCC's because both would primarily rely on AEPSC to operate and maintain the equipment.[42] On cross examination, ETT witness Mr. Crowder admitted that he expected AEPSC to provide the same level of service operating and maintaining the initial facilities whether they are owned by ETT or TCC.[43] Furthermore, Mr. Ally testified that because ETT's Service Agreement with AEPSC could be cancelled after two years, there is "uncertainty in the continuity or adequacy of service with ETT owning the facilities."[44]

Mr. Ally also testified that any benefits which could be derived from ETT's future plans to build transmission projects "are speculative, will require future filings for Commission approvals, and can be achieved without the transfer of the initial facilities requested in this

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[39] Docket No. 19265, Order at 1 (Nov. 18, 1999).
[40] Staff Exh. 2, Direct Examination of Mohammed Ally at 8 ln. 10-15 (June 18, 2007).
[41] *See* Staff Exh. 2, Direct Examination of Mohammed Ally at 8 ln. 16-18 (June 18, 2007).
[42] Staff Exh. 2, Direct Examination of Mohammed Ally at 8 ln. 10-15 (June 18, 2007).
[43] Tr. at 252 ln. 5-8.
[44] Staff Exh. No. 2, Direct Testimony of Mohammed Ally at 17 ln. 9-10 (June 18, 2007).

case."[45] Furthermore, as previously stated, the evidence shows that existing utilities such as TCC and TNC can meet future needs for transmission service.[46]

Rather than provide new public benefits, such as lowering of costs or improvement of service, the evidence shows that the formation of ETT would result in a public detriment: higher costs to ratepayers. In its Initial Brief, ETT appears to be backing away from its request for a 10.75 percent base ROE by stating its ROE "should be the same" as AEP Texas Central Company (TCC) and AEP Texas North Company (TNC).[47] Staff and intervenors have recommended ROEs of 9.75 percent or less in the TCC case.[48] In addition, ETT no longer requests recovery of $721,738 in formation costs.[49] ETT accepts the dollar value of Staff witness Glenda Spence's proposed depreciation adjustment of $18,632 for the purposes of setting rates in this case, but for accounting purposes asks the Commission to prospectively apply the depreciation rates adopted by the Commission in TCC's pending rate case, Docket No. 33309.[50] ETT also accepts the dollar value of Staff witness Ms. Spence's proposed lease and incentive compensation adjustments of $1,846 and $44,700, respectively, but for accounting purposes asks the Commission to prospectively apply the lease expense amount that results from the Commission's decision in TCC's pending rate case.[51] Finally, ETT says it no longer requests an adder of 50 basis points to the ROE for each of its planned transmission projects, but still seeks one for the "initial facilities"[52] and others involving new technology.[53] However, even with these concessions, ratepayers would still pay more to ETT for the initial facilities if ETT's request for a 50 basis point adder for initial facilities is approved, and if ETT is allowed to recover rate case expenses.

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[45] Staff Exh. No. 2, Direct Testimony of Mohammed Ally at 8 ln. 10-15 (June 18, 2007).
[46] *See* Staff Exh. No. 2, Direct Testimony of Mohammed Ally at 14 ln. 4-5 (June 18, 2007).
[47] Initial Brief of Electric Transmission Texas, LLC at 2 (Aug. 1, 2007).
[48] Tr. at 256 ln. 24 through 257 ln. 2 (July 16, 2007).
[49] Initial Brief of Electric Transmission Texas, LLC at 2 (Aug. 1, 2007).
[50] Initial Brief of Electric Transmission Texas, LLC at 38 (Aug. 1, 2007).
[51] Initial Brief of Electric Transmission Texas, LLC at 38-39 (Aug. 1, 2007).
[52] The "initial facilities" that ETT seeks to acquire and operate are located in the Laredo area. Staff Exh. No. 2, Direct Testimony of Mohammed Ally at 13 ln. 5-10 (June 18, 2007). They include a Variable Frequency Transformer (VFT), which provides bidirectional power flow between the Electric Reliability Council of Texas (ERCOT) and Mexico, as well as phase-shifting transformers that regulate power flow and Dynamic Reactive Compensation Systems that provide voltage support. *Id.*
[53] Initial Brief of Electric Transmission Texas, LLC at 2 and 35-36 (Aug. 1, 2007). ETT said, "In the future, the Commission should also consider incentives for other innovative transmission projects if: 1. there are demonstrated savings to customers; 2. the facility represents an innovative solution; and 3. the facility presents additional risk associated with new technology." Initial Brief of Electric Transmission Texas, LLC at 36 (Aug. 1, 2007).

Ratepayers also risk paying more in Operation and Maintenance (O&M) costs if ETT takes over the initial facilities.[54] ETT has a two-year contract with AEPSC to provide O&M services.[55] AEPSC and ETT are all affiliates of AEP. Pursuant to PURA § 36.058, when one affiliate provides services to another, it must do so "at cost."[56] Staff witness Mr. Ally testified that because ETT's O&M service agreement with AEPSC can be cancelled after two years, "there is uncertainty in the continuity and adequacy of service" that ETT would provide.[57] In its Initial Brief, ETT discounts this possibility, stating that "logic suggests termination would not occur unless better services could be acquired for lower cost."[58] However, this fails to recognize that AEPSC itself could cancel the contract after two years, with no guarantee that ETT could find a comparable provider. Mr. Ally testified that ETT's O&M costs could increase if ETT or AEPSC cancel their O&M service agreement and ETT must hire another O&M contractor.[59]

Staff witness Mr. Lain testified that the proposal to purchase some of TCC's facilities but charge customers more to finance and operate them is not in the public interest.[60] Because ETT's rates and costs would be higher than existing utilities which can and are already providing similar services, the transactions to form, capitalize, and transfer assets to ETT are not in the public interest.

IV. RATE CASE ISSUES

The Commission should deny ETT's CCN and find that the proposed transactions to form, capitalize, and transfer assets to ETT are not in the public interest because they would not result in net public benefits, and at best would result in the same level of service being provided at a higher cost to ratepayers. If the Commission denies the CCN, there is no need to set an initial rate for ETT in this case.

If the Commission grants a CCN, pursuant to PURA § 14.101(c), it should disallow the effect of the sale, transfer, or merger transactions because the transactions are not in the public

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[54] Staff Exh. No. 2, Direct Testimony of Mohammed Ally at 18 lns. 10-11 (June 18, 2007).
[55] Tr. at 252 ln. 17-22 (July 16, 2007).
[56] *See also Railroad Commission of Texas v. Rio Grande Valley Gas Co.*, 683 S.W.2d 783 (Tex. Civ. App.-Austin, no writ).
[57] Staff Exh. No. 2, Direct Testimony of Mohammed Ally at 17 lns. 9-10 (June 18, 2007).
[58] Initial Brief of Electric Transmission Texas, LLC at 9 (Aug. 1, 2007).
[59] Staff Exh. No. 2, Direct Testimony of Mohammed Ally at 19 lns. 12-13 (June 18, 2007).

interest. To accomplish this, the Commission should set ETT's ROE no higher than that of TCC in its pending rate case and deny ETT recovery of formation costs and rate case expenses. ETT has withdrawn its request for formation costs.[61] The Commission should also make adjustments for depreciation expenses, lease expenses, and incentive compensation amounts consistent with Staff's recommendations.

Base Return on Equity. In its Initial Brief, ETT appears to be backing away from its request for a 10.75 percent base ROE by stating its ROE "should be the same" as that of TCC and TNC.[62] Staff and intervenors have recommended ROEs of 9.75 percent or less in the TCC case.[63] ETT's requested 10.75 percent base ROE should be rejected because it was based on a set of data that is not comparable.

Staff witness Richard Lain testified about how the data set that ETT witness Dr. Hadaway developed to justify a 10.75 percent base ROE is flawed.[64] Mr. Lain testified that Dr. Hadaway used companies in his comparison that had lower debt-ratio averages and higher credit-rating averages.[65] Dr. Hadaway also discarded the traditional constant-growth version of the discounted cash flow (DCF) model that uses the actual three-to-five year growth rate projections of professional industry analysts.[66] Instead, Dr. Hadaway replaced the analysts' growth rate estimates for each company in his DCF model with a generic growth rate estimate, based on his forecasted long-term growth rate of 6.6 percent for the U.S. Gross Domestic Product (GDP).[67] Mr. Lain testified that Dr. Hadaway's use of a 6.6 percent generic growth rate in his DCF model analysis leads to almost a full percentage point higher growth rate than the amount in Mr. Lain's estimate of 5.62 percent. Mr. Lane testified that this adjustment led to a jump in Dr. Hadaway's estimated ROE for his comparable electric companies to 10.8 percent.[68] Dr. Hadaway also used his long-term growth rate in a two-stage version of the DCF model, resulting in an estimated average ROE for his comparable electric companies of 10.4 percent.[69]

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[60] Staff Exh. No. 1, Direct Testimony of Richard Lain at 38 ln. 8-9 (June 18, 2007).
[61] Initial Brief of Electric Transmission Texas, LLC at 2 (Aug. 1, 2007).
[62] Initial Brief of Electric Transmission Texas, LLC at 2 (Aug. 1, 2007).
[63] Tr. at 256 ln. 24 through 257 ln. 2 (July 16, 2007).
[64] Staff Exh. No. 1, Direct Testimony of Richard Lain at 65 ln. 1 through 69 ln 10 (June 18, 2007).
[65] Staff Exh. No. 1, Direct Testimony of Richard Lain at 65 ln. 5-8 (June 18, 2007).
[66] Staff Exh. No. 1, Direct Testimony of Richard Lain at 65 ln. 11-13 (June 18, 2007).
[67] Staff Exh. No. 1, Direct Testimony of Richard Lain at 65 ln. 16-19 (June 18, 2007).
[68] Staff Exh. No. 1, Direct Testimony of Richard Lain at 65 ln. 16-19 (June 18, 2007).
[69] Staff Exh. No. 1, Direct Testimony of Richard Lain at 65 ln. 19 through 66 ln. 1 (June 18, 2007).

Mr. Lain concluded:

> A generic growth rate should not be used when there is already an acceptable amount of available data from the specific circumstances of the individual companies whose growth is being estimated. Dr. Hadaway never provides sufficient justification in the form of independent studies, analyses, reports or information to warrant a change from a historic and appropriate source of growth rates – growth forecasts made by security analysts that theoretically already incorporate the variable.[70]

Because Dr. Hadaway's ROE recommendations are based on a set of data that is not comparable, ETT's request for a 10.75 percent base ROE should be rejected. In its Initial Brief, ETT acknowledges that its base ROE should be the same as TNC and TCC.[71]

Incentive for Advanced Technology. ETT says it is no longer seeking an adder of 50 basis points for its ROE for each of its planned transmission projects, but still seeks one for the "initial facilities" and others involving new technology.[72] ETT originally claimed it should receive a 50 basis point adder due to innovative transmission technology, its ambitious construction plan, as well as ERCOT's need to successfully compete with other jurisdictions for transmission investment.[73] In its Initial Brief, ETT limits the situations where it says it will request an adder:

> In the future, the Commission should also consider incentives for other innovative transmission projects if: 1. there are demonstrated savings to customers; 2. the facility represents an innovative solution; and 3. the facility presents additional risk associated with new technology.[74]

ETT's request for an adder for the initial facilities should be rejected because ETT has not met even its own suggested criteria. Although ETT witnesses say the initial facilities will result in savings to customers, ETT has conducted no cost-benefit study supporting such an assertion.[75] Furthermore, the initial facilities near Laredo are already being completed and operated by TCC,[76] which has not requested and does not receive a 50 basis point advanced technology

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[70] Staff Exh. No. 1, Direct Testimony of Richard Lain at 66 ln 6-12 (June 18, 2007).
[71] Initial Brief of Electric Transmission Texas, LLC at 2 (Aug. 1, 2007).
[72] Initial Brief of Electric Transmission Texas, LLC at 2 and 35-36 (Aug. 1, 2007).
[73] ETT Exh. No. 6, Direct Testimony of Samuel C. Hadaway at 4 ln. 11-17 (January 22, 2007).
[74] Initial Brief of Electric Transmission Texas, LLC at 36 (Aug. 1, 2007).
[75] Tr. at 129 ln. 21-24 (July 16, 2007).
[76] *See* Staff Exh. 2, Direct Examination of Mohammed Ally at 8 ln. 16-18 (June 18, 2007).

adder. Approval of the adder would result in customers paying more for the same service,[77] which fails to meet ETT's own suggested criteria of demonstrating savings to customers. Furthermore, ETT also has not proven that the initial facilities will be any riskier to maintain or operate. To the contrary, the evidence suggests that the initial projects are working well. If operation and maintenance costs rise higher than expected in the future, ETT can request a rate adjustment. The commission should also reject ETT's request for a bifurcated rate because it could create an arbitrage situation, where TCC and TNC would have incentive to move any "new technology" projects to ETT in order to charge customers a higher rate for such projects. Absent strong, countervailing benefits that are not present in this case, the Commission should not grant a CCN that creates arbitrage opportunities that provide disincentives for low-rate providers to build transmission and incentives for the high-rate providers to build them. Mr. Lain also testified that an incremental approach of setting ROEs higher on a case-by-case basis rather than industry-wide would allow some transmission providers higher returns on equity before others, and that would be an uncompetitive influence, and would therefore not be in the public interest.[78]

Rate Case Expenses. As a matter of law, the Commission should disallow the Cities' rate case expenses of up to $202,325.[79] This amount includes $71,178 in incurred legal and consultant expenses and an additional $131,147 in estimated fees for completing this proceeding through the appeals process.[80] In this docket, ETT seeks approval for rates for wholesale transmission service. The Commission is specifically authorized to set a utility's rates for wholesale transmission service pursuant to PURA § 35.004. PURA § 35.004(d) requires that the Commission price wholesale transmission service within ERCOT based on the postage stamp method of pricing, whereby the cost of the service is charged only to utilities, based on the utilities' peak loads.[81]

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[77] *See* Staff Exh. No. 2, Direct Testimony of Mohammed Ally at 16 ln. 3-13 (June 18, 2007)

[78] Staff Exh. No. 1, Direct Testimony of Richard Lain at 49 ln 1-4 (June 18, 2007).

[79] Cities Initial Brief at 30 (Aug. 1, 2007).

[80] *Id.*

[81] P.U.C. SUBST. R. 25.192(b)(1). *See also, e.g.,* Docket No. 33550, *Commission Staff's Application to Set 2007 Wholesale Transmission Service Charges for the Electric Reliability Council of Texas (ERCOT)*, Order (March 30, 2007) and Order Nunc Pro Tunc (May 1, 2007).

In its Initial Brief, Cities claims that PURA § 33.023 gives it the right to recover rate case expenses in a wholesale transmission rate case.[82] However, PURA § 33.023 cannot be reasonably interpreted to permit reimbursement of a city's rate case expenses in a docket in which only wholesale transmission rates are set.[83] Instead, it applies only to a rate proceeding in which rates for retail service within the city are set. This is evident from the other provisions of Chapter 33, which generally address the jurisdiction and powers of cities to regulate electric utilities. PURA § 33.001(a) provides that a city has "exclusive original jurisdiction over the rates, operations, and services of an electric utility in areas in the municipality, subject to the limitations imposed by this title." PURA § 33.004(a) clarifies that a city's jurisdiction to regulate electric utility service is limited to local service.

PURA § 33.023 is within Subchapter B of Chapter 33. The first sentence in this subchapter begins: "A municipality regulating an electric utility under this subtitle ...." The first sentence of PURA § 33.023 begins: "The governing body of a municipality participating in or conducting a ratemaking proceeding ...." PURA § 33.025(a) makes clear that § 33.023 applies only to "an electric utility providing service in the municipality."

That § 33.023 does not apply to wholesale-only transmission rate cases is further supported by the fact that the Commission has exclusive jurisdiction under PURA § 35.004 to set wholesale transmission rates.[84] Cities have no jurisdiction to set wholesale transmission rates. In addition, "electric utility" as used in Chapter 33 includes utilities that are investor-owned or river authorities but excludes electric cooperatives and municipally owned utilities, whereas pursuant to PURA § 35.004 the Commission sets the wholesale transmission rates for all of these type of utilities.[85]

In its Initial Brief, Cities argues that "[i]n essence, the Staff's view is that cities' right to reimbursement is contingent upon cities having original jurisdiction over the matter."[86] That is not Staff's argument. Rather, Staff's argument is that PURA § 33.023 applies only to a rate proceeding for retail electric service in the city seeking reimbursement. Cities have not provided

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[82] Cities Initial Brief at 30-31 (Aug. 1, 2007).
[83] In this pleading, "city" is used interchangeably with "municipality" and "the governing body of a municipality".
[84] The Federal Energy Regulatory Commission sets wholesale transmission rates outside of ERCOT and for AEP Texas Central Company and AEP Texas North Company in ERCOT.
[85] PURA §§ 31.002(6) and 35.001.
[86] Cities Initial Brief at 31 (Aug. 1, 2007).

any statutory provision that would give them the right to recover rate case expenses from a remote wholesale transmission provider.

PURA § 33.023 cannot be read in a vacuum. If read literally, this section would permit reimbursement of rate cases expenses for any city in the world that participated in an electric utility rate case at the Commission. More practically, it would mean that any city in ERCOT could be reimbursed for participation in any ERCOT wholesale transmission rate case, or at least one for an investor-owned utility or river authority. Although Cities claim that 30 years of experience shows this has not happened,[87] it is because the law does not allow for it, not because cities would not seek such recoveries if allowed. In this docket, the transmission facilities that ETT proposes to acquire are not even located in or near the cities seeking reimbursement.

In its Initial Brief, Cities also incorrectly imply that Staff's position on this matter was raised late.[88] Because this is a matter of law, it was properly addressed in a Statement of Position filed with the Commission on July 10, 2007, pursuant to Order No. 12.[89] If Cities wanted an early ruling on this issue, they should have included it in their list of issues as a threshold legal issue for the Commission to address in the Preliminary Order.

Cities cite a Texas-New Mexico Power true-up case[90] and a Reliant environmental clean-up case[91] for the proposition that cities should be allowed to recover for participation in ratemaking proceedings where cities do not have original jurisdiction. However, both of the cited cases involved retail delivery service in the cities that were reimbursed. Neither of the cited cases involved the Commission's exclusive jurisdiction under PURA § 35.004 to set wholesale transmission rates.

The presiding officer correctly granted the Cities' motion to intervene in this docket, because retail customers such as Cities and their residents will ultimately pay ETT's costs if its application in this docket is granted.[92] The Commission has previously granted the opposed motion to intervene of a retail customer in a wholesale-only transmission rate proceeding.[93]

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[87] Cities Initial Brief at 33 (Aug. 1, 2007).
[88] Cities Initial Brief at 31 fn 84 (Aug. 1, 2007).
[89] Docket No. 33734, Order No. 12 at 2 (June 25, 2005).
[90] Docket No. 29206.
[91] *Petition of Reliant Energy, Inc. for Approval of Environmental Cleanup Costs Plan*, Docket No. 24835, Order at 10 (April 12, 2002).
[92] *See* Order No. 3.
[93] *Commission Staff's Application to Set 2003 Wholesale Transmission Service Charges for the Electric Reliability Council of Texas*, Docket No. 26950, *Nucor Steel's Response to Oncor Electric Delivery Company's Objection to*

However, in such a rate proceeding, retail customers, including Cities, must pay their own expenses and cannot impose them on every customer in ERCOT.

Depreciation expenses, lease expenses, and incentive compensation amounts. Staff witness Glenda Spence recommended adjustments in each of these categories. In its Initial Brief, ETT said it would accept the dollar amount of Ms. Spence's recommended depreciation adjustment of $18,632 for the purposes of setting rates in this case, but for accounting purposes asks the Commission to prospectively apply the depreciation rates adopted by the Commission in TCC's pending rate case, Docket No. 33309.[94] ETT also said it would accept the dollar amounts of Ms. Spence's recommended lease and incentive compensation adjustments of $1,846 and $44,700, respectively, but for accounting purposes asks the Commission to prospectively apply the lease expense amount that results from the Commission's decision in TCC's pending rate case.[95] Staff agrees that the Commission should make these adjustments consistent with its decisions in TCC's pending rate case.

V. CODE OF CONDUCT AND AFFILIATE RULE EXEMPTIONS

If the Commission grants ETT's CCN, it should approve a Code of Conduct and resolve ETT's requests for exemptions from certain transaction and reporting rules based on the agreed recommendations of ETT, the Office of Public Utility Council and Staff. The recommendation is detailed in Staff Exhibit 6, Supplemental Direct Testimony of Candice J. Romines, and in the findings of fact and conclusions of law regarding these issues, filed by ETT and agreed to by Staff and OPC.

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and Motion to Strike the Motion to Intervene of Nucor Steel – Texas (Dec. 30, 2002) and Order No. 4 (Jan. 2, 2003). *See also Application of Lone Star Transmission, LLC's for a Certificate of Convenience and Necessity and Certain Regulatory Clarifications*, Docket No. 34362, *Commission Staff's Response to Lone Star Transmission, LLC's Objection to TIEC's Motion to Intervene* (July 10, 2007) (end-use customers should be permitted to intervene in docket for entity seeking to become a transmission utility throughout the state).

[94] Initial Brief of Electric Transmission Texas, LLC at 38 (Aug. 1, 2007).

[95] Initial Brief of Electric Transmission Texas, LLC at 38-39 (Aug. 1, 2007).

VI. CONCLUSION

The Commission should deny ETT's application for a CCN because ETT has failed to demonstrate that there is a need for a CCN or that current electric service is inadequate. The Commission should also deny the CCN because by the close of the evidentiary record, MidAmerican failed to make its required $15 million equity investment in the new venture.

The Commission should find that ETT's application for transfer of the initial facilities and stock is not in the public interest because it would not result in net public benefits, and at best it would result in the same level of service being provided at a higher cost to ratepayers. Because the proposed transfer of initial facilities and stock is not in the public interest, if the Commission approves a CCN, it should disallow the effect of the transaction on ratepayers pursuant to PURA § 14.101(c) by disallowing formation costs, rate case expenses, and setting ETT's ROE no higher than what it sets in the pending rate case of TCC. Furthermore, the Commission should not approve ETT's request for a 50 basis point advanced technology adder for initial facilities because it would result in customers paying more for the same service they would otherwise have received from TCC at a lower cost.

Respectfully Submitted,

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DOCKET NO. 33734

CERTIFICATE OF SERVICE

I certify that a copy of this document will be served on all parties of record on this the 15th day of August, 2007, in accordance with P.U.C. Procedural Rule 22.74.

Paul A. Curtis

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