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**SOAH DOCKET NO. 473-19-3864
PUC DOCKET NO. 49421**

**APPLICATION OF CENTERPOINT § BEFORE THE STATE OFFICE 11:24
ENERGY HOUSTON ELECTRIC, LLC § OF
FOR AUTHORITY TO CHANGE RATES § ADMINISTRATIVE HEARINGS**

CROSS-REBUTTAL TESTIMONY

AND

WORKPAPERS

OF

KARL NALEPA

ON BEHALF OF THE

OFFICE OF PUBLIC UTILITY COUNSEL

JUNE 19, 2019

583

**SOAH DOCKET NO. 473-19-3864
PUC DOCKET NO. 49421**

CROSS-REBUTTAL TESTIMONY OF KARL NALEPA

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1 **I. WITNESS IDENTIFICATION AND SCOPE OF TESTIMONY**

2 **Q. PLEASE STATE YOUR NAME, OCCUPATION, AND BUSINESS ADDRESS.**

3 A. My name is Karl J. Nalepa. I am President of ReSolved Energy Consulting, LLC
4 ("REC"), an independent utility consulting company. My business address is 11044
5 Research Boulevard, Suite A-420, Austin, Texas 78759.

6 **Q. HAVE YOU PREVIOUSLY PRESENTED DIRECT TESTIMONY IN THIS**
7 **DOCKET?**

8 A. Yes. I have presented direct testimony on behalf of the Office of Public Utility Counsel
9 ("OPUC") in this docket.

10 **Q. PLEASE PROVIDE YOUR QUALIFICATIONS.**

11 A. My qualifications are set forth in my direct testimony at Appendices A and B.

12 **Q. WHAT IS THE PURPOSE OF YOUR CROSS-REBUTTAL TESTIMONY?**

13 A. The purpose of my cross-rebuttal testimony is to address certain issues raised in the direct
14 testimonies of Public Utility Commission of Texas Staff ("PUC Staff") witnesses Jorge
15 Ordonez and Brian Murphy, and Texas Industrial Energy Consumers ("TIEC") witness
16 Jeffrey Pollock regarding proposals made by CenterPoint Energy Houston Electric, LLC
17 ("CenterPoint Houston" or the "Company").

18 **II. HURRICANE HARVEY CARRYING COSTS**

19 **Q. WHAT IS PUCT STAFF WITNESS JORGE ORDONEZ'S POSITION ON**
20 **CENTERPOINT HOUSTON'S REQUEST TO INCLUDE CARRYING COSTS**
21 **ON ITS HURRICANE HARVEY REGULATORY ASSET?**

1 A. Mr. Ordóñez supports CenterPoint Houston's request to include \$8.742 million in
2 carrying charges on its Hurricane Harvey regulatory asset.¹ Mr. Ordóñez states that he
3 reviewed the Company's calculation of the carrying costs and agrees with the Company's
4 calculation methodology.²

5 **Q. DO YOU AGREE WITH MR. ORDÓÑEZ'S POSITION?**

6 A. No. As I explained in my direct testimony, CenterPoint Houston incorrectly calculated
7 the carrying costs because it applied a monthly "compound interest" formula, rather than
8 an annual "simple interest" formula.³

9 **Q. DOES MR. ORDÓÑEZ'S TESTIMONY ADDRESS THIS ASPECT OF**
10 **CENTERPOINT HOUSTON'S CALCULATION?**

11 A. No. Mr. Ordóñez does not address CenterPoint Houston's use of a monthly compound
12 interest formula. As a result, it is not clear whether he considered this aspect of the
13 Company's calculation.

14 **Q. WHAT IS YOUR RECOMMENDATION?**

15 A. For the reasons discussed in my direct testimony, I recommend that if CenterPoint
16 Houston is permitted to recover carrying costs on its Hurricane Harvey regulatory asset,
17 then an annual "simple interest" formula should be applied to calculate the carrying costs.

¹ Direct Testimony of Jorge Ordóñez at 39.

² *Id.*

³ Direct Testimony of Karl Nalepa at 19-21.

1 **III. ALLOCATION OF TRANSMISSION COSTS**

2 **Q. HOW DOES CENTERPOINT HOUSTON PROPOSE TO ALLOCATE**
3 **TRANSMISSION COSTS?**

4 A. CenterPoint Houston proposes to allocate transmission costs based on its own Company
5 4CP,⁴ which is the average of the four highest monthly coincident peak demands on its
6 system, corresponding to the months of June, July, August, and September.

7 **Q. HOW DO PUCT STAFF WITNESS BRIAN MURPHY AND TIEC WITNESS**
8 **JEFFRY POLLOCK PROPOSE TO ALLOCATE TRANSMISSION COSTS?**

9 A. PUCT Staff witness Brian Murphy⁵ and TIEC witness Jeffry Pollock⁶ both oppose
10 CenterPoint Houston's proposal to allocate transmission costs based on the Company's
11 4CP, and instead, they both propose to allocate transmission costs based on ERCOT's
12 4CP. ERCOT's 4CP is the average of the four highest monthly coincident peak demands
13 on the ERCOT system, corresponding to the months of June, July, August, and
14 September.⁷

15 **Q. DO YOU AGREE WITH MR. MURPHY'S AND MR. POLLOCK'S POSITION?**

16 A. No. Using CenterPoint Houston's 4CP to allocate transmission costs, as proposed by the
17 Company, is a more reasonable basis for transmission cost allocation than using
18 ERCOT's 4CP to allocate transmission costs to the Company's customers.

⁴ Direct Testimony of Matthew Troxle at 20.

⁵ Direct Testimony of Brian Murphy at 43.

⁶ Direct testimony of Jeffry Pollock at 2.

⁷ ERCOT Nodal Protocols, Sec. 9.17.1 *Billing Determinant Data Elements*.

1 Q. DO THE COMMISSION'S RULES SPECIFY HOW TO ALLOCATE
2 TRANSMISSION COSTS?

3 A. No.

4 Q. HOW DID THE COMMISSION ALLOCATE TRANSMISSION COSTS IN
5 CENTERPOINT HOUSTON'S MOST RECENT RATE CASE?

6 A. In the Company's most recent rate case in Docket No. 38339, the Commission approved
7 the use of ERCOT's 4CP for allocating the Company's transmission costs.

8 Q. DOES THE COMMISSION'S DECISION IN THE CENTERPOINT HOUSTON'S
9 LAST RATE CASE REQUIRE THE SAME TRANSMISSION COST
10 ALLOCATION IN THIS CASE?

11 A. No. The Commission typically relies on prior precedent unless there is a compelling
12 reason to change from its prior position. In this case, there is a compelling reason to
13 deviate from the Commission's prior precedent due to the availability of better customer
14 demand data from the Company's advanced meters.

15 Q. WHAT IS THE BASIS FOR YOUR CONCLUSION?

16 A. Using CenterPoint Houston's own advanced meter data provides a more accurate
17 measure of customer class peak demand. As noted by CenterPoint Houston witness J.
18 Stuart McMenamin:⁸

19 ...with advanced meters fully deployed, (the Company) can see actual
20 customer demand for every 15-minute interval in every day of every
21 month. These data support exact calculation of daily energy, daily peaks,
22 and daily coincident loads at the time of system peaks, eliminating the
23 statistical uncertainty from sample data. The availability of complete and

⁸ Direct Testimony of J. Stuart McMenamin at 5.

1 more granular interval data supports energy and peak adjustment models
2 that are more powerful and accurate than was possible in past rate cases.

3 Using 4CP data based on actual customer demand is more representative of the actual
4 demand on CenterPoint Houston's transmission system and will provide for a more
5 accurate allocation of transmission costs among the Company's customers. This more
6 accurate, granular customer demand data was not available for use in CenterPoint
7 Houston's prior rate case because the Company had not completed its deployment of
8 advanced meters in its service territory.

9 **Q. WHAT WOULD BE THE IMPACT OF MR. MURPHY'S AND MR. POLLOCK'S**
10 **PROPOSAL?**

11 A. As shown in Mr. Pollock's Table 3, the Transmission class benefits the most from their
12 proposal to use ERCOT's 4CP, with a 10% reduction in the allocation of transmission
13 costs. This change would shift recovery of \$13.8 million from the Transmission class to
14 other classes. The Residential class would experience a 2% increase, or \$9.0 million
15 more in allocated costs, relative to the Company's proposal.

16 **IV. ALLOCATION OF MUNICIPAL FRANCHISE FEES**

17 **Q. HOW DOES CENTERPOINT HOUSTON PROPOSE TO ALLOCATE**
18 **MUNICIPAL FRANCHISE FEES?**

19 A. CenterPoint Houston proposes to allocate municipal franchise fees to retail delivery
20 classes using in-city kilowatt-hour (kWh) sales.⁹

⁹ See WP-Franchise and II-I-Total.

1 **Q. WHAT IS TIEC WITNESS JEFFRY POLLOCK’S POSITION ON**
2 **ALLOCATING MUNICIPAL FRANCHISE FEES?**

3 A. Mr. Pollock proposes that municipal franchise fees be allocated to retail delivery classes
4 using in-city kilowatt-hour (kWh) sales, but weighted to reflect the different municipal
5 franchise fee rates charged by the various cities in CenterPoint Houston’s service area.¹⁰

6 **Q. WHAT WOULD BE THE IMPACT OF MR. POLLOCK’S POSITION?**

7 A. Under Mr. Pollock’s proposal, as seen in his Table 6, every class except the Transmission
8 class would be allocated a greater share of municipal franchise fees.¹¹ The allocation of
9 municipal franchise fees to the Transmission class would decrease by \$4.1 million, or
10 23%.

11 **Q. WHAT IS MR. POLLOCK’S JUSTIFICATION FOR ALLOCATING**
12 **MUNICIPAL FRANCHISE FEES ON A CITY-BY-CITY BASIS?**

13 A. Mr. Pollock contends that his proposal is more consistent with cost causation because
14 different cities levy different rates of municipal franchise fees and the proportion of kWh
15 sales by delivery rate class is not uniform by city.¹²

16 **Q. DO YOU AGREE WITH MR. POLLOCK’S POSITION?**

17 A. No. CenterPoint Houston’s methodology has been consistently approved by the
18 Commission in past rate case proceedings, and Mr. Pollock provides no compelling
19 reason to deviate from the Commission’s precedent. In fact, Mr. Pollock made this exact
20 same proposal regarding allocation of municipal franchise fees in CenterPoint Houston’s

¹⁰ Direct Testimony of Jeffry Pollock at 3.

¹¹ *Id.* at 16.

¹² *Id.* at 14.

1 last rate case proceeding in Docket No. 38339, and his proposal was rejected by the
2 Commission. In that case, the Commission concluded that the collection of the municipal
3 franchise fees from all customers within the customer class was reasonable and consistent
4 with Commission precedent.¹³

5 **Q. HAS MR. POLLOCK PROPOSED A DIFFERENT ALLOCATION METHOD**
6 **FOR MUNICIPAL FRANCHISE FEES IN OTHER CASES?**

7 A. Yes. For example, in Entergy Texas, Inc.'s ("ETI") 2011 rate case in Docket No. 39896,
8 Mr. Pollock proposed allocating municipal franchise fees to, and collecting them only
9 from, customers within the cities that levy such taxes.¹⁴ The Commission also rejected
10 Mr. Pollock's proposal in that case. In addressing the issue, the Commission made the
11 following findings of fact:

12 178. Municipal Franchise Fees (MFF) is a rental expense paid by utilities for
13 the right to use public rights-of-way to locate its facilities within
14 municipal limits.

15 179. ETI is an integrated utility system. ETI's facilities located within
16 municipal limits benefit all customers, whether the customers are located
17 inside or outside of the municipal limits.

18 180. Because all customers benefit from ETI's rental of municipal right-of-
19 way, municipal franchise fees should be charged to all customers in ETI's
20 service area, regardless of geographic location.

21 181. It is reasonable and consistent with the Public Utility Regulatory Act
22 (PURA) § 33.008(b) that MFF be allocated to each customer class on the
23 basis of in-city kilowatt hour (kWh) sales, without an adjustment for the
24 MFF rate in the municipality in which a given kWh sale occurred.¹⁵

¹³ Docket No. 38339, Order on Rehearing at FOF 179.

¹⁴ Docket No. 39896, Direct Testimony of Jeffry Pollock at 52-58.

¹⁵ Docket No. 39896, Order on Rehearing at FOFs 178-181.

1 **Q. IS CENTERPOINT HOUSTON'S PROPOSAL FOR ALLOCATING MUNICIPAL**
2 **FRANCHISE FEES CONSISTENT WITH COMMISSION PRECEDENT?**

3 A. Yes. CenterPoint Houston is proposing to use the same method for allocating municipal
4 franchise fees that the Commission approved in its prior rate case.

5 **Q. IS THE COMPANY'S PROPOSAL CONSISTENT WITH THE PRINCIPLE OF**
6 **COST CAUSATION?**

7 A. Yes. The principle of cost causation suggests that customers pay for the costs that they
8 incur or the benefits that they receive. Consistent with that principle, the Commission
9 concluded in ETI's rate case in Docket No. 39896 that all customers benefit from the
10 rental of municipal rights-of-way, so municipal franchise fees should be charged to all
11 customers in ETI's service area.

12 **Q. ARE THERE OTHER POLICY REASONS THAT SUPPORT CENTERPOINT**
13 **HOUSTON'S TREATMENT OF MUNICIPAL FRANCHISE FEES?**

14 A. Yes. In considering rate design, it is also important to consider simplicity and
15 consistency. The Company's proposal serves both of these goals because it applies a
16 uniform policy to all customers and maintains the Commission's historical practice.
17 Notably, Mr. Pollock's proposal would not promote the goal of simplicity. As shown in
18 Exhibits JP-3, JP-5 and JP-6 to his testimony, there are 93 separate municipal franchise
19 fee rates that Mr. Pollock weights for each of the Company's seven customer classes to
20 develop his proposed allocation factors. Deriving a city-by-city allocation in this manner
21 introduces unnecessary complexity in setting the Company's rates. Further, as I

discussed above, the Company's proposal is consistent with the Commission's longstanding treatment of municipal franchise fees.

Q. WHAT DO YOU RECOMMEND FOR THE ALLOCATION OF MUNICIPAL FRANCHISE FEES?

A. Consistent with Commission precedent and sound ratemaking policy, I recommend that the Commission adopt the Company's allocation of municipal franchise fees.

V. RATE MODERATION

Q. WHAT IS TIEC WITNESS JEFFRY POLLOCK'S POSITION ON RESETTling THE TRANSMISSION COST RECOVERY FACTOR ("TCRF") ALLOCATION FACTORS?

A. Mr. Pollock compared the relative allocation of transmission costs under current allocation factors and the allocation factors proposed by the Company in this case. Based on this comparison, Mr. Pollock observed that the Transmission class would experience a 22% increase in transmission costs while all other classes would receive a decrease in allocated costs. He concluded that this purported cost shift would result in rate shock for the Transmission class.¹⁶

Q. WHAT DOES MR. POLLOCK BELIEVE CAUSED THE COST SHIFTING?

A. Mr. Pollock believes that the cost-shifting resulting in rate shock can be attributed to (1) the almost nine years that have passed since CenterPoint Houston's last rate case, and (2) the Commission's TCRF rule,¹⁷ which updates the billing determinants used for

¹⁶ Direct Testimony of Jeffry Pollock at 31.

¹⁷ 16 TAC § 25.193.

1 transmission cost recovery, but does not update class allocation factors between base rate
2 cases.¹⁸

3 **Q. DOES MR. POLLOCK PROPOSE A REMEDY TO AVOID RATE SHOCK?**

4 A. Mr. Pollock suggests that rate shock can be avoided by moderating the changes in the
5 4CP allocation factors.¹⁹

6 **Q. DOES MR. POLLOCK EXPLAIN HOW SUCH A MODERATION IN THE 4CP**
7 **ALLOCATION FACTORS SHOULD BE ACCOMPLISHED?**

8 A. No. It is not clear how Mr. Pollock proposes to moderate the impact of changing the 4CP
9 allocation factors.

10 **Q. IS IT REASONABLE TO IMPLEMENT A 4CP ALLOCATION FACTOR**
11 **MODERATION PLAN AS SUGGESTED BY MR. POLLOCK?**

12 A. No. The Commission has established its strong preference to move classes to cost of
13 service, and has approved rate moderation plans on only rare occasions. Mr. Pollock has
14 not established that an isolated increase in this single allocation factor will lead to overall
15 rate shock for the Transmission class or any other class. Thus, Mr. Pollock's proposal
16 should be rejected.

17 **Q. DOES THIS CONCLUDE YOUR CROSS-REBUTTAL TESTIMONY?**

18 A. Yes.

¹⁸ Direct Testimony of Jeffry Pollock at 31-32.

¹⁹ *Id.* at 32.

WORKPAPERS

SOAH DOCKET NO. 473-19-3864
PUC DOCKET NO. 49421

APPLICATION OF CENTERPOINT § BEFORE THE STATE OFFICE
ENERGY HOUSTON ELECTRIC, LLC §
FOR AUTHORITY TO CHANGE § OF
RATES § ADMINISTRATIVE HEARINGS

TEXAS INDUSTRIAL ENERGY CONSUMERS' RESPONSE TO
CENTERPOINT ENERGY HOUSTON ELECTRIC, LLC'S
THIRD REQUEST FOR INFORMATION

- 3-3 Regarding the Direct Testimony of Jeffry Pollock, identify each proceeding before this Commission in which TIEC or Mr. Pollock has recommended the same or a similar municipal franchise fee allocation methodology as Mr. Pollock recommends in this proceeding and whether the Commission adopted Mr. Pollock's approach.

RESPONSE:

Mr. Pollock recommended the same municipal franchise fee allocation methodology in Docket Nos. 38339 and 39896. Mr. Pollock's methodology was not adopted in Docket Nos. 38339 and 39896.

Preparer: Jeffry Pollock
Sponsor: Jeffry Pollock

**SOAH DOCKET NO. 473-19-3864
PUC DOCKET NO. 49421**

APPLICATION OF CENTERPOINT ENERGY HOUSTON ELECTRIC, LLC FOR AUTHORITY TO CHANGE RATES	§ § § §	BEFORE THE STATE OFFICE OF ADMINISTRATIVE HEARINGS
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**TEXAS INDUSTRIAL ENERGY CONSUMERS' RESPONSE TO
CENTERPOINT ENERGY HOUSTON ELECTRIC, LLC'S
THIRD REQUEST FOR INFORMATION**

- 3-4** Is it Mr. Pollock's testimony that the Company's proposed allocation method in this case is inconsistent with the Commission-approved method in Docket No. 38339? If so, identify all ways in which it is inconsistent.

RESPONSE:

Counsel for CEHE clarified that the "proposed allocation method" in this question refers to the allocation of municipal franchise fees. With that clarification, Mr. Pollock answers as follows:

No. In Docket No. 38339, the Commission approved an allocation of municipal franchise fees based on each class's proportion of in-city kilowatt-hours (i.e., the Direct method). This is the same approach that CenterPoint is proposing in this proceeding.

Preparer: Jeffrey Pollock / Counsel
Sponsor: Jeffrey Pollock

SOAH DOCKET NO. 473-12-2979
PUC DOCKET NO. 39896

APPLICATION OF ENTERGY
TEXAS, INC. FOR AUTHORITY TO
CHANGE RATES, RECONCILE FUEL
COSTS, AND OBTAIN DEFERRED
ACCOUNTING TREATMENT

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§
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§

PUBLIC UTILITY
COMMISSION OF TEXAS

Direct Testimony and Exhibits

of

JEFFRY POLLOCK

On Behalf of

Texas Industrial Energy Consumers

REDACTED

March, 2012



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SOAH DOCKET NO. 473-12-2979
PUC DOCKET NO. 39896

APPLICATION OF ENTERGY TEXAS, INC. FOR AUTHORITY TO CHANGE RATES, RECONCILE FUEL COSTS, AND OBTAIN DEFERRED ACCOUNTING TREATMENT	PUBLIC UTILITY COMMISSION OF TEXAS
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1 improperly allocated miscellaneous gross receipts taxes (MGRT) to customer
2 classes. These expenses were allocated on total revenues. This is not consistent
3 with cost causation because MFF are caused by kWh sales within cities that levy
4 MFF, and MGRT are caused by revenues collected by ETI from within cities. They
5 are not caused by total revenues.³⁰

6 **Q SHOULD ETI'S CLASS COST-OF-SERVICE STUDY BE REVISED TO REFLECT**
7 **THE FLAWS NOTED ABOVE?**

8 **A Yes. The allocations of MFF and MGRT should also be revised to reflect cost**
9 **causation. I suggest changes to the class cost-of-service to address the appropriate**
10 **allocation of MFF and MGRT.**

11 **Municipal Franchise Fees**

12 **Q WHAT ARE MUNICIPAL FRANCHISE FEES?**

13 **A MFF are taxes levied by municipalities based on the amount of electricity sold within**
14 **the municipal boundaries. They are also referred to as street rental taxes. The MFF**
15 **charged to ETI are based on ordinances passed by the elected representatives of**
16 **the cities in which ETI makes retail sales. Different cities have enacted different**
17 **levels of MFF on in-city kWh sales ranging from 0.0956¢ to as much as 0.2644¢ per**
18 **kWh as shown in Exhibit JP-9, pages 1-2.**

³⁰ I am not addressing a third flaw: the failure to classify any distribution network investment as customer-related. The reasons for doing so are discussed in Appendix C.

1 Q DO THE RATES SHOWN IN EXHIBIT JP-9 REFLECT THE ENTIRETY OF THE
2 MUNICIPAL FRANCHISE FEES CHARGED BY CITIES IN ETI'S SERVICE AREA
3 FOR ?

4 A No. The rates shown in Exhibit JP-9, pages 1-2 are those MFF collected in base
5 rates. Nineteen cities also charge MFF through separate "Incremental Franchise
6 Fee Recovery" Riders. These incremental MFF are not included in ETI's proposed
7 revenue requirements in this case.

8 Q HOW IS ETI PROPOSING TO ALLOCATE MUNICIPAL FRANCHISE FEES
9 RECOVERED IN BASE RATES?

10 A ETI is proposing to allocate that portion of MFF to be collected in base rates relative
11 to revenues.³¹

12 Q IS ETI'S APPROACH CONSISTENT WITH COST CAUSATION?

13 A No. MFF are not caused by total revenues. MFF are caused by the kWh delivered
14 within incorporated municipalities that levy MFF costs, pursuant to PURA § 33.008.

15 Q DO CUSTOMERS LOCATED OUTSIDE OF A CITY HAVE ANY CONTROL OVER
16 THE AMOUNT OF MUNICIPAL FRANCHISE FEES THAT A CITY MAY CHARGE?

17 A No. Unlike in-city customers who can vote on the representatives who set the MFF
18 rates, customers located outside a city have no control over the level of the tax.

³¹ Schedule P-13, page 10, lines 32-33; the allocation factor "RSRRTOA-Total" is rate schedule revenue.

1 Q DO ELECTRICITY SALES OR REVENUES TO CUSTOMERS LOCATED
2 OUTSIDE OF A CITY AFFECT THE AMOUNT OF MUNICIPAL FRANCHISE FEES
3 THAT ETI IS OBLIGATED TO PAY?

4 A No. Electricity sales to and revenues from customers located outside of a city do not
5 have any effect on how much ETI must pay to the city. Rather, the MFF incurred by
6 ETI is directly caused by in-city kWh sales.

7 Q IS ETI'S PROPOSED ALLOCATION OF BASE RATE MUNICIPAL FRANCHISE
8 FEES CONSISTENT WITH THE INCREMENTAL FRANCHISE FEE RECOVERY
9 RIDERS?

10 A No. For example, a typical Incremental Franchise Fee Recovery Rider states:

11 The rate associated with this Surcharge Tariff shall be \$0.0010137 *for*
12 *every kilowatt-hour billed by the Company to its retail customers*
13 *inside the city limits of Beaumont.*³² (emphasis added)

14 Thus, incremental franchise fees are allocated and collected solely from retail
15 customers within city limits. This is clearly different from how ETI allocates the
16 portion of MFF that it recovers in base rates, which is based on revenue.

17 Q DOES THIS COMMISSION HAVE A CONSISTENT POLICY REGARDING THE
18 ALLOCATION OF MUNICIPAL FRANCHISE FEES?

19 A Yes. The Commission's current policy was adopted in the unbundled cost-of-service
20 (UCOS) cases in 2001 and affirmed in all delivery rate cases since. Under this
21 policy, MFF costs are allocated based on the classes within the assessing

³² Entergy Texas, Inc., Section III Rate Schedule, *Incremental Beaumont Franchise Fee Recovery Rider*, Sheet No. 64, Revision 1 at 101.

1 municipality's boundaries. This approach is referred to as the "Direct" method of
2 allocation.

3 Although Commission policy varied widely prior to the UCOS cases (some
4 utilities were allowed to recover MFF separately from in-city customers and others
5 allocated MFF relative to total revenues), the Commission has consistently approved
6 the Direct method of allocation in cases over the past eleven years. This issue was
7 litigated in both the Reliant Energy (now CenterPoint Energy) and TXU (now Oncor)
8 cases. Specifically, the Commission's Orders in the two cases included the following
9 identical findings:

10 The LGRT legislation requires the tax be based on the number of
11 kWh delivered within the municipal boundaries in order to maintain
12 sufficient revenue levels for the cities. To meet this revenue
13 requirement, LGRT should be allocated using a direct allocation
14 and employing the energy allocator.³³

15 This same Direct method of allocating MFF was also adopted in Docket Nos. 28840
16 and 33309.

17 **Q HOW SHOULD MFF EXPENSE BE ALLOCATED?**

18 **A** Consistent with the ratemaking principle of cost causation and Commission
19 precedent, MFF should be allocated using the Direct method, while also recognizing
20 the widely varying MFF rates and class sales by city. The results of this allocation
21 are shown in Exhibit JP-9.

³³ Application of TXU Electric Company for Approval of Unbundled Cost of Service Rate Pursuant to PURA § 39.201 and Public Utility Commission Substantive Rule § 25.344, Docket No. 22350, Order at FOF 156 (Oct. 4, 2001); Application of Reliant Energy HL&P for Approval of Unbundled Cost of Service Rate Pursuant to PURA § 39.201 and Public Utility Commission Substantive Rule § 25.344, Docket No. 22355, Order at FOF 222A (Oct. 4, 2001). Note: the term LGRT, or local gross receipts tax, was used synonymously with MFF.

3. Class Cost-of-Service Study

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1 Q PLEASE EXPLAIN EXHIBIT JP-9.

2 A The starting point for applying the Direct method is the current base rate MFF rates
3 shown in pages 1-2 and the kWh sales by customer class by city shown on pages 3-
4 4. As can be seen, there is no uniformity in both the MFF rates (pages 1-2) and the
5 proportion of kWh sales by class (pages 3-4) by city. In general, those cities
6 charging the lowest MFF rates also have a larger amount of kWh sales from
7 Schedule LIPS customers. Cities with higher MFF rates generally have a larger
8 proportion of kWh sales from residential customers.

9 The allocated MFF expense is the product of the MFF rates and the
10 corresponding kWh sales by class by city. This calculation is shown in Exhibit JP-9,
11 pages 5-6. The MFF allocation factor is shown on page 6, line 70. It is the result of
12 summing the allocated MFF expenses (line 69) and expressing the total by class
13 (columns 1-6) as a percent of total retail (column 7).

14 Q IS THE ALLOCATION METHODOLOGY SHOWN IN EXHIBIT JP-9 CONSISTENT
15 WITH COST CAUSATION?

16 A Yes. The methodology recognizes that the level of MFF costs ETI incurs is a
17 function of only two things: (1) the tax level set by the city, and (2) the usage of
18 customers inside the city limits. There is nothing that an outside-city customer can
19 do to influence either element. In-city customers, however, determine the tax rate
20 through their elected representatives, and their usage determines the amount that
21 ETI must pay the cities. It also recognizes that MFF rates and the proportion of kWh
22 sales by class are not uniform by city. Customers should only be charged for the

3. Class Cost-of-Service Study

J. POLLOCK
INCORPORATED

1 MFF they cause. For this reason, it would not be appropriate to charge all customers
2 the same average MFF rate when the rates for many cities (that also happen to
3 serve more Schedule LIPS kWh sales) are below average.

4 **Q HOW SHOULD MFF BE COLLECTED?**

5 **A** Consistent with cost causation, MFF expense should be recovered from customers
6 located within the municipalities that levy these taxes. This is referred to as the
7 "Direct" method of collection. The Direct method would continue the link between the
8 usage of a group of customers and the costs incurred. Allocating MFF to and
9 collecting MFF from customers within the cities that levy such taxes is the only way
10 to remain consistent with the principle of cost causation. Thus, customers located
11 outside of tax-levying municipalities should pay zero MFF.

12 **Q IS THERE ANY PRECEDENT FOR THE DIRECT METHOD OF COLLECTING**
13 **MFF?**

14 **A** Yes. As previously stated, several cities in ETI's service area have implemented
15 Incremental Franchise Fee Recovery Riders that collect MFF only from retail
16 customers in the city limits. Further, both Southwestern Public Service Company
17 and Texas New Mexico Power Company use the Direct method in collecting MFF
18 from transmission level customers.³⁴

³⁴ Southwestern Public Service, Electric Tariff, *Large General Service - Transmission*, Section No. IV, Sheet No. IV-108, Revision No. 7 at 1; Texas-New Mexico Power Company, Tariff for Retail Delivery Service, 6.1.1.1.5 *Transmission Service*, Revision 5 at 100.

1 Q WOULD IT BE EQUITABLE TO CHARGE MUNICIPAL FRANCHISE FEES TO
2 CUSTOMERS WHO TAKE SERVICE OUTSIDE CITY LIMITS?

3 A No. This would be tantamount to "taxation without representation." Outside-city
4 customers have no voice in determining either the level of MFF, or how the money is
5 to be spent. By spreading MFF to all customers, cities that elect to raise the MFF
6 rate would be able to force outside-city customers to pay for local expenses from
7 which the customers receive no direct benefit. And by cushioning the impact on in-
8 city residents, there would be little to prevent a city from raising its fees. Thus,
9 charging MFF to outside-city customers is not only inequitable, it would weaken the
10 incentive for cities (and city voters) to exercise appropriate fiscal discipline.

11 Q HAS THIS ISSUE ALSO BEEN ADDRESSED IN OTHER STATES?

12 A Yes. Regulators in several other states where municipalities levy such taxes have
13 addressed this issue in contested cases and have ordered that MFF be allocated to,
14 and collected from, the customers located inside the levying cities. These states
15 include: Alaska, Arkansas, Colorado, Florida, Idaho, Illinois, Indiana, Iowa, Kansas,
16 Missouri, Nevada, New Mexico, Pennsylvania, Virginia, Washington and West
17 Virginia. Thus, this approach has gained wide acceptance.

18 Q HOW DO YOU RECOMMEND THAT MFF BE ALLOCATED AND COLLECTED?

19 A I recommend the Direct method of allocation and the Direct method of collection (i.e.,
20 Direct/Direct) because this method is more consistent with cost causation.

3. Class Cost-of-Service Study

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