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

REBUTTAL TESTIMONY
OF
ROBERT B. McRAE
ON BEHALF OF
CENTERPOINT ENERGY HOUSTON ELECTRIC, LLC

June 2019

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589

TABLE OF CONTENTS

I. INTRODUCTION3

II. PURPOSE OF REBUTTAL TESTIMONY AND RECOMMENDATIONS3

III. CAPITAL STRUCTURE5

 A. Response to Dr. Woolridge’s Capital Structure Arguments 11

 B. Response to Mr. Gorman’s Capital Structure Arguments 18

 C. Response to Ms. Winker’s Capital Structure Arguments 30

 D. Response to Mr. Ordonez’s Capital Structure Arguments..... 33

IV. WEIGHTED AVERAGE COST OF CAPITAL41

V. EFFECT OF CITIES’ RECOMMENDATIONS ON CREDIT METRICS42

VI. LONG-TERM INCENTIVE COMPENSATION45

LIST OF EXHIBITS

Exhibit R-RBM-1	Moody’s June 3, 2019 Presentation (Confidential)
Exhibit R-RBM-2	S&P June 3, 2019 Presentation (Confidential)
Exhibit R-RBM-3	Moody’s June 16, 2019 Issuer Comment (Confidential)
Exhibit R-RBM-4	S&P Report on CEHE March 22, 2019 (Confidential)
Exhibit R-RBM-5	Errors Uncovered in Gorman’s MPG-5
Exhibit R-RBM-6	Proforma Correction of MPG-5
Exhibit R-RBM-7	Adjustment of Proforma Corrections of MPG-5 to 9.25% ROE
Exhibit R-RBM-8	Effect of Cities’ Recommendations on Credit Metrics

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REBUTTAL TESTIMONY OF ROBERT B. MCRAE

I. INTRODUCTION

Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

A. My name is Robert B. McRae. My business address is 1111 Louisiana Street, Houston, Texas 77022.

Q. BY WHOM ARE YOU EMPLOYED AND IN WHAT POSITION?

A. I am employed by CenterPoint Energy Service Company, LLC as Assistant Treasurer.

Q. ON WHOSE BEHALF ARE YOU TESTIFYING IN THIS PROCEEDING?

A. I am filing testimony on behalf of CenterPoint Energy Houston Electric, LLC (“CenterPoint Houston” or the “Company”).

Q. ARE YOU THE SAME ROBERT B. MCRAE WHO FILED DIRECT TESTIMONY ON BEHALF OF CENTERPOINT HOUSTON IN THIS DOCKET?

A. Yes.

II. PURPOSE OF REBUTTAL TESTIMONY AND RECOMMENDATIONS

Q. WHAT IS THE PURPOSE OF YOUR REBUTTAL TESTIMONY?

A. The purpose of my rebuttal testimony is to respond to the direct testimony and recommendations by Intervenor and Staff witnesses regarding the Company’s capital structure and weighted average cost of capital (“WACC”). In particular, I respond to the cost-of-capital testimony filed by:

- Michael P. Gorman and Charles S. Griffey on behalf of Texas Industrial Energy Consumers (“TIEC”);
- J. Randall Woolridge on behalf of Texas Coast Utilities Coalition (“TCUC”);

- 1 • Anjuli Winker on behalf of the Office of Public Utility Counsel (“OPUC”);
- 2 and
- 3 • Jorge Ordonez on behalf of the Public Utility Commission of Texas
- 4 (“Commission”) Staff.

5 **Q. PLEASE SUMMARIZE YOUR REBUTTAL TESTIMONY AND**
6 **RECOMMENDATIONS REGARDING THE COMPANY’S COST OF**
7 **CAPITAL.**

8 A. I recommend that the Commission approve a capital structure composed of 50%
9 debt and 50% equity. Contrary to the assertions by Intervenor and Staff witnesses,
10 CenterPoint Houston needs a 50% equity ratio to maintain its credit metrics at a
11 level that will support the Company’s current credit ratings. In contrast, the
12 Intervenor and Staff witnesses’ capital structure recommendations would likely
13 lead to a ratings downgrade and higher capital costs for customers.

14 I also recommend that the Commission approve the Company’s proposed
15 4.38% cost of long-term debt. That is CenterPoint Houston’s actual embedded cost
16 of long-term debt, and no party has requested that the Commission approve a
17 different cost of long-term debt.

18 I also recommend that the Commission approve the Company’s proposed
19 7.39% WACC, which is calculated using the Company’s proposed 50/50 capital
20 structure, the 4.38% cost of long-term debt, and the 10.40% return on equity
21 (“ROE”) supported by Company witness Robert B. Hevert.

22 In addition, I explain that the disallowance recommendations by the city
23 groups would cause CenterPoint Houston’s credit metrics to fall far below the level
24 needed to sustain the Company’s current credit ratings.

1 Finally, I address the effect of the Intervenor and Staff recommendations
2 regarding Long-Term Incentive (“LTI”) compensation.

3 **Q. ARE YOU THE ONLY CENTERPOINT HOUSTON WITNESS FILING**
4 **REBUTTAL TESTIMONY ON COST-OF-CAPITAL ISSUES?**

5 A. No. As noted in the previous answer, Mr. Hevert is also filing rebuttal testimony
6 regarding the Company’s required ROE, and he addresses capital structure as well.
7 In addition, Company witness Ellen Lapson addresses capital structure issues.

8 **III. CAPITAL STRUCTURE**

9 **Q. WHAT CAPITAL STRUCTURE IS CENTERPOINT HOUSTON ASKING**
10 **THE COMMISSION TO APPROVE?**

11 A. I explained in my direct testimony that CenterPoint Houston is asking the
12 Commission to approve a capital structure composed of 50% equity and 50% debt.¹
13 That capital structure is necessary for a number of reasons, including the
14 Company’s high level of forecasted capital expenditures, the risk of losses from
15 hurricanes, and the reduced cash flow attributable to the Tax Cuts and Jobs Act of
16 2017 (“TCJA”).²

¹ Dr. Woolridge mistakenly asserts that Company witness Charles W. Pringle is the Company witness that supports CenterPoint Houston’s proposed capital structure. Woolridge Dir. at 17:6-8. In fact, I am the Company witness supporting CenterPoint Houston’s proposed capital structure.

² McRae Dir. at 15:12-17.

1 **Q. WHAT CAPITAL STRUCTURES ARE THE INTERVENOR AND STAFF**
2 **WITNESSES ASKING THE COMMISSION TO APPROVE FOR**
3 **PURPOSES OF SETTING CENTERPOINT HOUSTON’S RATES?**

4 A. Dr. Woolridge, Mr. Gorman, and Mr. Ordonez propose a capital structure
5 composed of 60% long-term debt and 40% common equity.³ Ms. Winker proposes
6 a capital structure composed of 54.5% long-term debt and 45.5% common equity.⁴
7 I address those witnesses’ capital structure arguments in the following subsections.

8 **Q. BEFORE PROCEEDING TO THE SPECIFIC ARGUMENTS ADVANCED**
9 **BY THE INTERVENOR AND STAFF WITNESSES, DO YOU HAVE ANY**
10 **THRESHOLD OBSERVATIONS REGARDING THEIR TESTIMONY?**

11 A. Yes, I have three. First, it appears that all of the Intervenor and Staff witnesses fail
12 to recognize the detrimental effects that the TCJA has had on utilities’ cash flows.
13 As I mentioned in my direct testimony, Moody’s Investors Service (“Moody’s”)
14 placed the entire regulated utility sector on negative outlook in mid-2018 because
15 of the effects of the TCJA on cash flows.⁵ Moreover, in a recent presentation,
16 Moody’s confirmed that the tax reform legislation continues to weigh upon the
17 utility sector. In Exhibit R-RBM-1, which is a PowerPoint presentation by
18 Moody’s on June 3, 2019 at the 2019 Power and Gas Issuers’ Conference, Moody’s
19 noted that [REDACTED]

20 [REDACTED]

³ Gorman Dir. at 37, Table 7; Woolridge Dir. at 20:1-3. Dr. Woolridge also presents an alternative capital structure composed of 55.48% long-term debt, 0.90% short-term debt, and 43.62% common equity. Woolridge Dir. at 20:17-22.

⁴ Winker Dir. at 43:5.

⁵ McRae Dir. at 19:13-19 (citing to Moody’s Investors Service, *Regulated Utilities – US: 2019 Outlook Shifts to Negative Due to Weaker Cash Flows, Continued High Leverage* (June 18, 2018)).

1 [REDACTED].”⁶ Moody’s further noted that [REDACTED]

2 [REDACTED]

3 [REDACTED].⁷

4 **Q. IS ANY OTHER RATING AGENCY TAKING ACTION TO ADDRESS**
5 **THE EFFECTS OF THE TCJA ON UTILITY CREDIT METRICS?**

6 A. Yes. My Exhibit R-RBM-2 is a recent Standard & Poor’s (“S&P”) presentation.
7 As that presentation shows, S&P currently has nearly four times as many utilities
8 on negative outlook as it did in 2014.⁸ In contrast, the number of utilities on
9 positive outlook has fallen by 80% since 2014. And in 2019 alone, S&P has
10 downgraded 18 utilities, as compared to upgrades for only nine utilities.⁹

11 **Q. HAVE THE RATING AGENCIES IDENTIFIED STEPS THAT UTILITIES**
12 **CAN TAKE TO MITIGATE THE RISK PRODUCED BY THE TCJA?**

13 A. Yes. As I explained in my direct testimony, the rating agencies have focused on
14 several tools to mitigate the risk, including an increase in the authorized equity
15 ratio, an increase in the authorized ROE, and an increase in depreciation expense.¹⁰
16 CenterPoint Houston is requesting an increase in the equity ratio because it
17 mitigates the effects on cash flow at the lowest cost to customers.¹¹

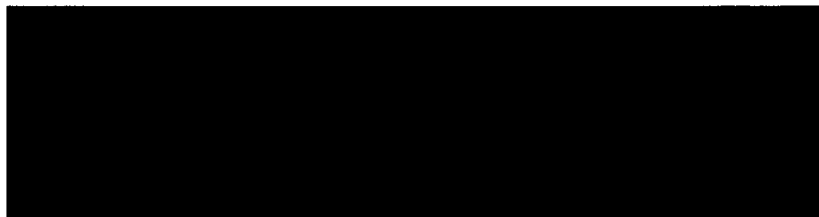
⁶ Exhibit R-RBM-1 at 4.
⁷ *Id.* at 4.
⁸ Exhibit R-RBM-2 at 9.
⁹ *Id.* at 10.
¹⁰ McRae Dir. at 21:7-13.
¹¹ *Id.* at 21:16-19.

1 Q. SOME OF THE INTERVENOR WITNESSES ASSERT THAT THE
2 EFFECTS OF THE TCJA ARE TEMPORARY, AND THEREFORE THE
3 COMMISSION NEED NOT CONCERN ITSELF WITH THOSE
4 EFFECTS.¹² WHAT IS YOUR RESPONSE?

5 A. I believe that those witnesses have misconstrued the word “temporary.” The rating
6 agencies have stated that over the “longer term,” the TCJA could be mildly credit-
7 positive for utilities because lower deferred tax balances will increase rate base and
8 because utilities retained the deductibility of interest expense.¹³ But over the next
9 several years, the TCJA will continue to erode key ratios used by the rating
10 agencies. For example, in the June 2018 report placing the entire utility sector on
11 negative outlook as a result of the TCJA, Moody’s noted that the ratio of Cash from
12 Operations to Debt (“CFO/Debt”) is projected to continue declining through at least
13 2022, and perhaps longer.¹⁴

14 It is also important to note that the rating agencies have said they will view
15 the effects of the TCJA on a utility-by-utility basis, with regulatory actions playing
16 a key role in the rating agencies’ evaluation of how the TCJA will affect a particular
17 utility’s credit rating.

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¹² *E.g.*, Winker Dir. at 43:8-10.

¹³ Fitch Ratings, *Tax Reform Impacts on the U.S. Utilities, Power & Gas Sector* at 1 (Jan. 24, 2018).

¹⁴ Moody’s Investors Service, *Regulated Utilities – US: 2019 Outlook Shifts to Negative Due to Weaker Cash Flows, Continued High Leverage* at 2 (June 18, 2018).

2 [REDACTED]¹⁵

3 Thus, the Commission’s capital structure decision in this case will help determine
4 how the TCJA ultimately affects CenterPoint Houston’s credit ratings. It will also
5 influence the rating agencies’ perceptions of whether the Texas regulatory
6 environment remains constructive.

7 **Q. YOU STATED EARLIER THAT YOU HAVE THREE THRESHOLD**
8 **OBSERVATIONS REGARDING THE INTERVENOR AND STAFF**
9 **CAPITAL STRUCTURE TESTIMONY. WHAT IS YOUR SECOND**
10 **OBSERVATION?**

11 A. My second observation relates to the effect of the Intervenor and Staff witnesses’
12 capital structure recommendations on CenterPoint Houston’s credit metrics. On
13 June 17, 2019, Moody’s issued a comment on CenterPoint Houston’s rate case, so
14 we have empirical evidence of how at least one of the rating agencies views the
15 Intervenor and Staff witnesses’ cost-of-capital recommendations. In that comment,
16 Moody’s expressly stated [REDACTED]

17 [REDACTED]

18 [REDACTED]”¹⁶

¹⁵ S&P Global Ratings, *U.S. Tax Reform: For Utilities’ Credit Quality, Challenges Abound* at 5 (Jan. 24, 2018) (emphasis added); see also Fitch Ratings, *Tax Reform Impacts on the U.S. Utilities, Power & Gas Sector* at 4 (Jan. 24, 2018) (“Fitch’s rating actions will be guided by both the regulatory and management responses.”).

¹⁶ Exhibit R-RBM-3 at 1.

1 **Q. DID MOODY'S MAKE ANY OTHER STATEMENTS RELEVANT TO**
2 **THE INTERVENOR AND STAFF WITNESSES' CAPITAL STRUCTURE**
3 **RECOMMENDATIONS?**

4 A. Yes. Moody's noted [REDACTED]
5 [REDACTED]
6 [REDACTED]
7 [REDACTED]

8 [REDACTED]¹⁷ As I will demonstrate, the Intervenor and Staff
9 witnesses' capital structure recommendations would force CenterPoint Houston's
10 credit ratios to fall even lower than the reduced levels that Moody's is predicting.

11 **Q. WHAT IS YOUR THIRD OBSERVATION?**

12 A. My third observation is that, although the Staff and Intervenor witnesses make
13 capital structure recommendations, three of the four witnesses make no attempt to
14 determine how their recommendations would affect CenterPoint Houston's credit
15 metrics and credit ratings. The only effort who makes any effort to quantify the
16 effect of this capital structure recommendation is Mr. Gorman, and his analysis is
17 riddled with errors that render it useless. I describe those errors later in my
18 testimony.

¹⁷ Exhibit R-RBM-3 at 1.

1 **A. Response to Dr. Woolridge’s Capital Structure Arguments**

2 **Q. PLEASE EXPLAIN YOUR UNDERSTANDING OF DR. WOOLRIDGE’S**
3 **RECOMMENDATION ON CAPITAL STRUCTURE.**

4 A. As I understand Dr. Woolridge’s capital structure testimony, he is making a primary
5 recommendation and a secondary recommendation. His primary recommendation
6 is that the Commission authorize a capital structure composed of 60% debt and
7 40% equity.¹⁸ In the alternative, Dr. Woolridge recommends that the Commission
8 authorize a capital structure composed of 0.90% short-term debt, 55.48% long-term
9 debt, and 43.62% common equity.¹⁹

10 **Q. HAS DR. WOOLRIDGE PROVIDED ANY QUANTITATIVE ANALYSIS**
11 **TO SUPPORT HIS CONTENTION THAT HIS CAPITAL STRUCTURE**
12 **RECOMMENDATIONS WILL ALLOW CENTERPOINT HOUSTON TO**
13 **MAINTAIN ITS FINANCIAL INTEGRITY?**

14 A. No. As far as I can tell, he has made no effort to establish that CenterPoint Houston
15 could maintain its current credit rating with a 40% equity ratio and his proposed
16 ROE.

¹⁸ Woolridge Dir. at 20:1-5.

¹⁹ Woolridge Dir. at 20:10-16.

1 **Q. DR. WOOLRIDGE NEVERTHELESS ASSERTS THAT “THE MEDIAN**
 2 **COMMON EQUITY RATIOS OF THE ELECTRIC AND HEVERT PROXY**
 3 **GROUPS ARE 45.2% AND 45.8%, RESPECTIVELY,” AND FROM THAT**
 4 **PREMISE HE CONCLUDES THAT CENTERPOINT HOUSTON’S**
 5 **PROPOSED CAPITAL STRUCTURE CONTAINS MORE EQUITY THAN**
 6 **THE TWO PROXY GROUPS.²⁰ DO YOU AGREE WITH THAT**
 7 **ARGUMENT?**

8 **A.** No. In direct testimony, Mr. Hevert demonstrated that the average equity ratio for
 9 the companies in his proxy group was 53.28% through the third quarter of 2018,
 10 based on data from S&P Global Market Intelligence.²¹ And even if one relies on
 11 the Value Line data that Dr. Woolridge claims his Exhibit JRW-2 is based on, the
 12 equity ratios in that exhibit cannot be reconciled with the equity ratios listed for
 13 those utilities in the most recent versions of the Value Line reports:

14 **Table 1**

Utility	Equity Ratio Listed in Exhibit JRW-2	Equity Ratio Listed in Most Recent Value Line Report
ALLETE, Inc.	59.2%	59.0%
Alliant Energy Corporation	44.6%	48.0%
Ameren Corporation	46.2%	49.5%
American Electric Power Company, Inc.	42.7%	48.5%
AVANGRID, Inc.	70.8%	62.0%
Black Hills Corporation	42.1%	51.5%

²⁰ Woolridge Dir. at 17:11-14.

²¹ Hevert Dir., Exhibit RBH-9 at 1.

Utility	Equity Ratio Listed in Exhibit JRW-2	Equity Ratio Listed in Most Recent Value Line Report
CMS Energy Corporation	28.9%	36.5%
Consolidated Edison, Inc.	44.8%	49.0%
DTE Energy Company	42.9%	46.5%
Duke Energy Corporation	43.1%	43.5%
El Paso Electric Company	44.8%	47.5%
Evergy	54.2%	47.0%
Eversource Energy	46.7%	47.5%
Hawaiian Electric Industries	51.2%	55.0%
NextEra Energy, Inc.	49.8%	54.0%
NorthWestern Corporation	47.8%	51.5%
OGE Energy Corp.	56.0%	54.5%
Otter Tail Corporation	54.5%	49.5%
Pinnacle West Capital Corp.	50.6%	57.0%
PNM Resources, Inc.	37.6%	42.0%
Portland General Electric Company	50.3%	53.0%
Southern Company	38.3%	41.5%
WEC Energy Group	45.3%	50.0%
Xcel Energy Inc.	41.5%	42.0%
Average	47.2%	49.4%

1 As the foregoing table shows, the average equity ratio reported by *Value Line* for
2 the Hevert proxy group companies is much closer to my proposed 50% equity ratio

1 than it is to Dr. Woolridge's proposed 40% equity ratio. Indeed, even if one
2 assumes the equity ratios listed in Exhibit JRW-2 are accurate, the 47.2% average
3 is far closer to my proposed equity ratio than it is to Dr. Woolridge's proposed
4 equity ratio.

5 **Q. DR. WOOLRIDGE SUGGESTS THAT THE CAPITAL STRUCTURES HE**
6 **REPORTS FOR THE PROXY GROUP COMPANIES INCLUDE SHORT-**
7 **TERM DEBT.²² SHOULD SHORT-TERM DEBT BE USED TO**
8 **CALCULATE THE EQUITY RATIOS?**

9 A. No. The utility assets included in CenterPoint Houston's rate base are financed
10 with long-term debt and common equity, not with short-term debt. Moreover, this
11 Commission's long-standing precedent is to exclude short-term debt from utilities'
12 authorized capital structures.²³ Therefore, including short-term debt in the proxy
13 group capital structures skews the comparison in a way that makes it misleading.

14 **Q. DR. WOOLRIDGE ALSO ARGUES THAT CENTERPOINT HOUSTON IS**
15 **PROPOSING A HIGHER EQUITY RATIO THAN IT AND CENTERPOINT**
16 **ENERGY INC. HAVE MAINTAINED IN THE PAST.²⁴ WHAT IS YOUR**
17 **RESPONSE?**

18 A. I have several responses. First, Exhibit JRW-3 shows that Dr. Woolridge is
19 including short-term debt in his calculation of CenterPoint Houston's capital
20 structure, which is incorrect for the reasons I discussed above. Second, Exhibit

²² Woolridge Dir. at 17:14-18.

²³ See, e.g., *Application of Southwestern Public Service Company for Authority to Change Rates*, Docket No. 43695, Order on Rehearing at 25, Finding of Fact No. 71 (Feb. 23, 2016) ("It is unreasonable and inconsistent with Commission precedent to include short-term debt in SPS's capital structure.").

²⁴ Woolridge Dir. at 17:22-26.

1 JRW-3 shows that the most recent equity ratios for CenterPoint Energy, Inc. and
2 CenterPoint Houston are 47.0% and 45.5%, respectively, which are considerably
3 higher than those reported by Dr. Woolridge. Finally, if Dr. Woolridge is
4 suggesting that CenterPoint Houston needs to maintain an actual 50.0% equity ratio
5 in order to obtain an authorized 50% equity ratio, I strongly disagree with his
6 reasoning. CenterPoint Houston currently has an authorized equity ratio of 45.0%,
7 which means that it receives an equity return on 45.0% of its rate base investment.
8 Under Dr. Woolridge's suggestion that CenterPoint Houston should be maintaining
9 an actual 50.0% equity ratio if it wants the Commission to approve a 50.0% equity
10 ratio, CenterPoint's shareholders would earn a debt return on part of their equity
11 investment. And if equity investors believe that they will receive a debt return on
12 part of their equity investment, they will require a much higher equity return on the
13 remaining investment to compensate them for that debt return.

14 **Q. IF THE COMMISSION AUTHORIZES AN EQUITY RATIO OF 50.0%,**
15 **WILL CENTERPOINT ENERGY, INC. INFUSE SUFFICIENT EQUITY**
16 **TO BRING THE ACTUAL EQUITY RATIO IN LINE WITH THE**
17 **AUTHORIZED EQUITY RATIO?**

18 A. Yes. Within a reasonable time after the Commission's final decision in this docket,
19 CenterPoint Energy, Inc. will ensure that CenterPoint Houston's equity ratio is
20 generally consistent with the authorized equity ratio.

1 **Q. IN ADDITION TO HIS PRIMARY RECOMMENDATION OF 60% DEBT**
2 **AND 40% EQUITY, DR. WOOLRIDGE ALSO PROPOSES AN**
3 **ALTERNATIVE CAPITAL STRUCTURE COMPOSED OF 55.48% LONG-**
4 **TERM DEBT, 0.90% SHORT-TERM DEBT, AND 43.62% COMMON**
5 **EQUITY.²⁵ SHOULD THE COMMISSION ADOPT THAT PROPOSED**
6 **ALTERNATIVE CAPITAL STRUCTURE?**

7 A. No. As I explained earlier, CenterPoint Houston finances its rate base investment
8 with long-term debt and common equity, not short-term debt. Moreover, including
9 short-term debt in CenterPoint Houston's capital structure would be contrary to
10 long-standing Commission precedent. Therefore, the Commission should reject
11 Dr. Woolridge's alternative proposal as well.

12 **Q. DR. WOOLRIDGE ALSO TAKES ISSUE WITH YOUR TESTIMONY**
13 **THAT A 50% EQUITY RATIO IS NECESSARY TO MITIGATE THE**
14 **LOWER CASH FLOW CAUSED BY THE TCJA.²⁶ DO YOU AGREE**
15 **WITH HIS ARGUMENT?**

16 A. No. Dr. Woolridge argues that the TCJA does not warrant a higher equity ratio
17 because CenterPoint Houston has been able to raise cash, as evidenced by its higher
18 equity ratio, and because CenterPoint Houston's credit ratings are comparable to
19 the average credit ratings of his proxy group and Mr. Hevert's proxy group. His
20 argument is misguided for several reasons.

²⁵ Woolridge Dir. at 20:17-22.

²⁶ Woolridge Dir. at 21:5-14. In this question, Dr. Woolridge again mistakenly attributes my testimony to Mr. Pringle.

1 First, as I explained in my direct testimony, CenterPoint Houston's
2 projected credit metrics in the coming years will not support its current credit rating,
3 even with a 45.0% equity ratio. Though Dr. Woolridge did not provide any
4 quantitative analysis in his testimony, it is safe to assume that increasing the
5 Company's leverage as a result of his recommended equity ratios would further
6 lower credit metrics and accelerate their degradation.

7 Second, Dr. Woolridge ignores the impact TCJA has had on the utility
8 companies he includes in his peer set. For example:

- 9 • On March 26, 2019, Moody's downgraded ALLETE, Inc.'s issuer
10 rating to Baa1 from A3 as the result of an adverse general rate case
11 outcome at its primary subsidiary, Minnesota Power, and the negative
12 cash flow impact of TCJA.
- 13 • On May 23, 2018, Moody's placed Alliant Energy Corporation's Baa1
14 long term rating on negative outlook due to weakening financial ratios,
15 sizeable capital expenditure program, and negative cash flow impacts
16 associated with federal tax reform.
- 17 • On October 30, 2018, Moody's downgraded the long-term ratings of
18 Consolidated Edison Inc. and its subsidiaries due to a weaker financial
19 profile.
- 20 • On May 31, 2019, Moody's downgraded Oklahoma Gas & Electric
21 Company from A2 to A3, due to higher debt levels and lagging cash
22 flow from tax reform.
- 23 • On March 28, 2019, Moody's downgraded Xcel Energy Inc.'s long-
24 term rating from A3 to Baa1 due to the negative impact of tax reform,
25 an elevated capital program and limited plans to issue equity.
- 26 • On July 12, 2018, Moody's downgraded WEC Energy Group from A3
27 to Baa1 due to negative cash flow impact of tax reform and incremental
28 debt to fund capital expenditures.

29 My direct testimony provides solutions to avoid the downgrades that several
30 utilities in Dr. Woolridge's utility peer group have experienced, and to ensure that
31 CenterPoint Houston continues to have access to capital on reasonable terms.

1 Third, Dr. Woolridge's argument is directly contradicted by the June 17,
2 2019 Moody's issuer comment I discussed earlier. In that comment, Moody's
3 expressly states that [REDACTED]

4 [REDACTED].²⁷

5 Finally, Dr. Woolridge's argument that CenterPoint Houston has been able
6 to maintain adequate credit ratings with its current 45.0% equity ratio is
7 disingenuous, because Dr. Woolridge is not asking the Commission to maintain
8 CenterPoint Houston's current equity ratio. As I noted earlier, he is asking the
9 Commission to reduce CenterPoint Houston's authorized equity ratio to 40.0%, a
10 500 basis-point reduction.

11 **B. Response to Mr. Gorman's Capital Structure Arguments**

12 **Q. WHAT CAPITAL STRUCTURE IS MR. GORMAN RECOMMENDING**
13 **THAT THE COMMISSION APPROVE?**

14 A. Like Dr. Woolridge, Mr. Gorman is proposing that the Commission adopt a capital
15 structure composed of 40% equity and 60% debt.²⁸

16 **Q. DO YOU HAVE ANY OVERARCHING COMMENTS ABOUT MR.**
17 **GORMAN'S CAPITAL STRUCTURE ANALYSIS?**

18 A. Yes. It appears that Mr. Gorman has developed a four-step argument to support his
19 proposed 40% equity ratio and the ring-fencing protections advocated by TIEC:

- 20 1. CenterPoint Houston enjoys a supportive regulatory environment
21 and low business risk, and therefore it would be rated higher by the
22 rating agencies but for its association with CenterPoint Energy,
23 Inc.²⁹

²⁷ Exhibit R-RBM-3 at 1.

²⁸ Gorman Dir. at 37, Table 7.

²⁹ Gorman Dir. at 27:9-26.

- 1 2. The Commission should impose the financial ring-fencing measures
2 proposed by Mr. Griffey, which would sever the link between
3 CenterPoint Houston’s rating and CenterPoint Energy, Inc.’s
4 rating.³⁰
- 5 3. After severing that link, CenterPoint Houston would be measured
6 under the “low volatility” table used by S&P, rather than the “medial
7 volatility” table that S&P currently uses for CenterPoint Houston.³¹
- 8 4. If S&P’s “low volatility” table were used, CenterPoint Houston
9 could maintain its current credit rating with a 40.0% equity ratio and
10 a 9.25% ROE.³²

11 Mr. Gorman’s reasoning is flawed in numerous respects.

12 **Q. WHY DO YOU ASSERT THAT MR. GORMAN’S REASONING IS**
13 **FLAWED?**

14 A. First, Mr. Gorman is wrong to the extent he assumes that S&P evaluates
15 CenterPoint Houston in accordance with the medial volatility table. S&P has
16 expressly stated that it evaluates CenterPoint Houston under the low volatility
17 table.³³ Thus, the ring-fencing protections that Messrs. Griffey and Gorman
18 advocate would make no difference to S&P’s rating of CenterPoint Houston.

19 The actual reason that S&P rates CenterPoint Houston lower than Moody’s
20 and Fitch do is that S&P uses a “group rating” methodology in which a holding
21 company and its subsidiaries are typically rated the same. Notably, however, S&P
22 is revising its “group rating” methodology criteria and expects to publish its new
23 criteria in mid-July 2019.³⁴ As I interpret S&P’s guidance on this issue,

³⁰ Gorman Dir. at 32:21-33:2.

³¹ Gorman Dir. at 36:7-14.

³² Gorman Dir. at 36:20-37:2.

³³ Exhibit R-RBM-4 at 4 (S&P stating about CenterPoint Houston, [REDACTED]

[REDACTED]”)

³⁴ S&P Global Ratings, *Group Rating Methodology Guidance* at 2 (June 3, 2019).

1 CenterPoint Houston could experience an upgrade of at least one notch with its
2 existing operations and protections, provided that increased financial risk resulting
3 from the TCJA is mitigated. Thus, Mr. Gorman's conclusion that CenterPoint
4 Houston needs financial ring-fencing protections to enhance its S&P credit rating
5 is based on stale information.

6 Moreover, S&P is just one of the three major rating agencies, and the other
7 two rating agencies—Moody's and Fitch—view operating company subsidiaries
8 such as CenterPoint Houston on a more standalone basis. Thus, the ring-fencing
9 provisions proposed by Mr. Griffey would not necessarily have any appreciable
10 effect on the ratings from those rating agencies.³⁵ Moody's considers [REDACTED]

11 [REDACTED]
12 [REDACTED].

13 Finally, Mr. Gorman's assertion that CenterPoint Houston could maintain
14 its current credit rating with a 40.0% equity ratio and a 9.25% ROE is based upon
15 an erroneous analysis.

16 **Q. WHY DO YOU STATE THAT MR. GORMAN'S ASSERTION THAT**
17 **CENTERPOINT HOUSTON COULD MAINTAIN ITS CURRENT CREDIT**
18 **RATING WITH A 40.0% EQUITY RATIO AND A 9.25% ROE IS BASED**
19 **UPON AN ERRONEOUS ANALYSIS?**

20 **A.** For his assertion that CenterPoint Houston could maintain its current credit metrics
21 with a 40.0% equity ratio and 9.25% ROE, Mr. Gorman points to his Exhibit

³⁵ As Company witness Ellen Lapson states in her rebuttal testimony, CenterPoint Houston already has numerous financial protections in place, so even if Mr. Griffey's proposals were adopted, it is not clear that they would have any significant effect on the rating agencies' evaluations of CenterPoint Houston's financial risk.

1 MPG-5. That exhibit, however, contains several errors, which I have identified on
2 my Exhibit R-RBM-5. One error, in particular, inflates Mr. Gorman's credit
3 metrics, thereby rendering them unreliable.

4 **Q. WHICH ERROR IN EXHIBIT MPG-5 INFLATES MR. GORMAN'S**
5 **CREDIT METRICS?**

6 A. On page 2 of Exhibit MPG-5, Mr. Gorman attempts to recreate CenterPoint
7 Houston's income statement based on an equity ratio of 40.0% and an ROE of
8 9.25%. In calculating the tax expense, however, Mr. Gorman erroneously increased
9 the amount of the tax expense by the amount of the tax adjustment on line 18 rather
10 than reducing it by that amount, as he should have. If he had offset them properly,
11 as I have done in my Exhibit R-RBM-6, the amount on line 22 would have been
12 \$289.6 million in 2019, instead of the \$267.9 million shown on Mr. Gorman's
13 Exhibit MPG-5.

14 **Q. HOW DOES THAT ERROR AFFECT MR. GORMAN'S ANALYSIS?**

15 A. The balance sheet reflected in Exhibit MPG-5 shows an equity balance of \$2.9
16 billion dollars for CenterPoint Houston. When the \$289.6 million of corrected net
17 income is divided by the \$2.9 billion, it becomes clear that Mr. Gorman is actually
18 assuming an ROE of approximately 10.0% for 2019, not the 9.25% he claims to be
19 using.

20 **Q. HOW SHOULD MR. GORMAN'S EXHIBIT MPG-5 BE ADJUSTED TO**
21 **ACHIEVE A 9.25% ROE?**

22 A. The "Revenues Adjustment" on line 2 of page 2 of Exhibit MPG-5 must be changed
23 from -\$35 million to -\$62 million, which reduces the net income used to calculate

1 the ROE and reduces the EBITDA used in calculating CenterPoint Houston's S&P
2 credit metrics.

3 **Q. DOES THAT SAME ERROR OCCUR IN YEARS AFTER 2019?**

4 A. Yes. Mr. Gorman repeats the mistake in every year from 2019 through 2023. As
5 shown in my Exhibit R-RBM-6, Mr. Gorman's credit metric analysis implicitly
6 assumes ROEs over 10.0% in 2021, 2022, and 2023.

7 **Q. HAVE YOU RECALCULATED MR. GORMAN'S CREDIT METRICS
8 USING HIS RECOMMENDED 9.25% ROE AND A 40.0% EQUITY
9 RATIO?**

10 A. Yes. In my Exhibit R-RBM-7, I recreated Mr. Gorman's Exhibit MPG-5, except
11 that I increased the revenue adjustment in line 2 to a level that is needed to bring
12 the ROE down to 9.25%. As noted above, that results in a revenue adjustment of
13 \$62 million, rather than the \$35 million that Mr. Gorman shows in his Exhibit
14 MPG-5. I have made the same adjustment for the remaining years.

15 **Q. IF MR. GORMAN HAD ADJUSTED THE REVENUES PROPERLY, HOW
16 WOULD THAT AFFECT CENTERPOINT HOUSTON'S CREDIT
17 METRICS?**

18 A. Correcting Mr. Gorman's error produces significantly lower ratios of Funds From
19 Operations to Debt ("FFO/Debt") and Debt to Earnings Before Interest, Taxes,
20 Depreciation, and Amortization ("Debt/EBITDA") than Mr. Gorman shows. For
21 example, in Exhibit MPG-5 Mr. Gorman represents that CenterPoint Houston's
22 FFO/Debt ratio would be 13.2% and that its Debt/EBITDA ratio would be 4.93x in
23 2019. But as shown in my Exhibit R-RBM-7, the actual FFO/Debt in 2019 would

1 be 12.7% if Mr. Gorman had calculated the ratios correctly, and the Debt/EBIDTA
2 ratio would be 5.08x.

3 **Q. IN HIS TABLE 6, MR. GORMAN SUGGESTS THAT EVEN THOSE**
4 **LOWER RATIOS WOULD BE SUFFICIENT TO MAINTAIN OR**
5 **IMPROVE CENTERPOINT HOUSTON'S CREDIT RATINGS. IS HE**
6 **CORRECT?**

7 A. No. First, Mr. Gorman mistakenly uses the ratios for CenterPoint Energy, Inc. As
8 shown on Exhibit R-RBM-4, S&P's targeted FFO/Debt ratio for CenterPoint
9 Houston is 18%-20%, and its targeted Debt/EBITDA ratio is roughly 3.5x. Thus,
10 the credit metrics produced by Mr. Gorman's ROE and capital structure
11 recommendations are far below the S&P benchmarks.

12 Second, S&P's currently stand-alone rating for CenterPoint Houston is a+.
13 Mr. Gorman's target of 13% FFO to Debt would actually represent a two-notch
14 downgrade from its current position down to a-.

15 Third, 13% is at the bottom of the range for a company deemed to have
16 "intermediate" financial risk. Targeting the low end of a credit metric range is
17 imprudent as it provides little cushion against unexpected events, such as a
18 hurricane or other extreme weather.

1 **Q. HAS CENTERPOINT HOUSTON PERFORMED AN ANALYSIS OF HOW**
 2 **MR. GORMAN'S CAPITAL STRUCTURE AND ROE**
 3 **RECOMMENDATIONS WOULD AFFECT CENTERPOINT HOUSTON'S**
 4 **CREDIT METRICS UNDER THE METHODOLOGY USED BY**
 5 **MOODY'S?**

6 A. Yes. Table 2 displays what CenterPoint Houston's ratios would be based on the
 7 Moody's methodology under Mr. Gorman's ROE and capital structure
 8 recommendations.

9 **Table 2**

	2019	2020	2021	2022	2023
CFO pre-WC + Interest / Interest	4.21x	4.28 x	4.08x	4.03x	4.08x
CFO pre-WC / Debt	13.0%	13.2%	12.5%	12.6%	12.5%
CFO pre-WC – Dividends / Debt	12.0%	11.9%	9.4%	10.7%	9.3%
Debt / Capitalization	54.3%	55.0%	55.7%	56.6%	57.9%

10 **Q. WOULD THE RESULTING METRICS BE CONSISTENT WITH AN "A"**
 11 **RATING UNDER THE MOODY'S METHODOLOGY?**

12 A. No. As shown in Table 3, the resulting metrics for 2019 would map to a Baa rating
 13 under the Moody's methodology.

14 **Table 3**

Financial Strength Metric	Pro-forma 2019*	A	Baa	Ba
CFO pre-WC + Interest / Interest	4.21x	4.5x – 6.0x	3.0x – 4.5x	2.0x – 3.0x
CFO pre-WC / Debt	13.0%	19% - 27%	11% –19%	5% - 11%
CFO pre-WC – Dividends / Debt	12.0%	15% - 23%	7% - 15%	0% - 7%
Debt / Capitalization	54.3%	40% - 50%	50% - 59%	59% - 67%

15 * Source: Exhibit R-RBM-7

1 **Q. HAS CENTERPOINT HOUSTON PERFORMED AN ANALYSIS OF HOW**
 2 **MR. GORMAN'S CAPITAL STRUCTURE AND ROE**
 3 **RECOMMENDATIONS WOULD AFFECT CENTERPOINT HOUSTON'S**
 4 **CREDIT METRICS UNDER THE METHODOLOGY USED BY FITCH?**

5 A. Yes. Table 4 displays what CenterPoint Houston's ratios would be based on the
 6 Fitch methodology under Mr. Gorman's ROE and capital structure
 7 recommendations.

8 **Table 4**

	2019	2020	2021	2022	2023
Fitch FFO-adjusted leverage (x)	5.60	5.53	5.53	5.50	5.57
Total Adjusted Debt / Operating EBITDAR (x)	4.99	5.04	5.04	5.03	5.12
FFO Fixed-Charge Cover (x)	4.18	4.25	4.20	4.17	4.26

9 **Q. WOULD THE METRICS RESULTING FROM MR. GORMAN'S**
 10 **RECOMMENDATIONS BE CONSISTENT WITH AN "A" RATING**
 11 **UNDER THE FITCH METHODOLOGY?**

12 A. No. As shown in Table 5, the resulting metrics for 2019 would map to a bbb rating
 13 under the Fitch methodology.

14 **Table 5**

	Pro-forma 2019*	a	bbb	bb
Fitch FFO-adjusted leverage (x)	5.60	3.5	5.0	6.5
Total Adjusted Debt / Operating EBITDAR (x)	4.99	3.25	3.75	4.75
FFO Fixed-Charge Cover (x)	4.18	5.0	4.5	3.5

15 * Source: Exhibit R-RBM-7

16 Again, Gorman's proposed capital structure and ROE do not support CenterPoint
 17 Houston's current a- rating.

1 **Q. ON PAGE 29 OF HIS DIRECT TESTIMONY, MR. GORMAN SETS**
2 **FORTH FIVE REASONS WHY HE BELIEVES CENTERPOINT**
3 **HOUSTON'S PROPOSED CAPITAL STRUCTURE IS UNREASONABLE.**
4 **DO YOU HAVE ANY THRESHOLD RESPONSE TO HIS LIST OF**
5 **REASONS?**

6 A. Yes. Several of Mr. Gorman's reasons for opposing CenterPoint Houston's
7 proposed 50.0% equity ratio are rooted in the proposition that CenterPoint
8 Houston's currently authorized 45.0% equity ratio has served CenterPoint Houston
9 and its customers well. Mr. Gorman, however, is not proposing to maintain the
10 currently approved regulatory capital structure; instead, he is proposing to reduce
11 it by 500 basis points. It is unclear why he touts the benefits of the currently
12 approved capital structure at the same time he is proposing to reduce it so
13 dramatically.

14 **Q. TURNING TO THE INDIVIDUAL REASONS, MR. GORMAN'S FIRST**
15 **ARGUES THAT CENTERPOINT HOUSTON'S PROPOSED CAPITAL**
16 **STRUCTURE IS UNREASONABLE BECAUSE CENTERPOINT**
17 **HOUSTON HAS NOT DEMONSTRATED A NEED TO INCREASE THE**
18 **CURRENT EQUITY RATIO.³⁶ DO YOU AGREE?**

19 A. No. I explained in my direct testimony that an increase in the equity ratio to 50.0%,
20 along with a 10.4% ROE, would increase the ratio of FFO/Debt by roughly 200
21 basis points, which may be sufficient to maintain CenterPoint Houston's current
22 credit ratings.³⁷ In contrast, a 45.0% equity ratio would drop CenterPoint Houston

³⁶ Gorman Dir. at 29:3-4.

³⁷ McRae Dir. at 25:3-4.

1 below the threshold for a downgrade,³⁸ and the 40.0% equity ratio recommended
2 by Mr. Gorman would undoubtedly drive CenterPoint Houston's credit metrics
3 below the level needed to maintain its current credit ratings.

4 **Q. MR. GORMAN NEXT ASSERTS THAT CENTERPOINT HOUSTON'S**
5 **CURRENTLY APPROVED REGULATORY CAPITAL STRUCTURE HAS**
6 **SUPPORTED THE COMPANY'S CREDIT RATING AND FINANCIAL**
7 **INTEGRITY FOR MANY YEARS.³⁹ WHAT IS YOUR RESPONSE?**

8 A. I agree that the capital structure approved in Docket No. 38339 helped support
9 CenterPoint Houston's credit rating and financial integrity for several years, but
10 most of that time occurred prior to the enactment of the TCJA. As I demonstrated
11 in my direct testimony, the 45.0% equity ratio is no longer adequate in light of the
12 reduced cash flow produced by the TCJA. Moreover, it bears repeating that Mr.
13 Gorman is not proposing to maintain that currently approved regulatory capital
14 structure.

³⁸ McRae Dir. at 25:Table 6.

³⁹ Gorman Dir. at 29:5-6.

1 **Q. NEXT, MR. GORMAN ARGUES THAT CENTERPOINT HOUSTON’S**
2 **“RATEMAKING CAPITAL STRUCTURE IS IN LINE WITH**
3 **PREDICTABLE AND CONSISTENT RATEMAKING PRACTICES USED**
4 **BY THE COMMISSION IN SETTING OVERALL RATES OF RETURN**
5 **FOR LOW-RISK ELECTRIC TDUs THAT OPERATE WITHIN ERCOT.”⁴⁰**
6 **HOW DO YOU RESPOND?**

7 A. As I understand the argument, Mr. Gorman is asserting that the 45.0% equity ratio
8 currently authorized for CenterPoint Houston is consistent with the equity ratios
9 authorized for other transmission and distribution utilities operating in the Electric
10 Reliability Council of Texas (“ERCOT”). I have several responses. First, a number
11 of the equity ratios currently authorized for ERCOT utilities were established
12 before the enactment of the TCJA. Moreover, Mr. Gorman has not established that
13 other utilities in ERCOT are forecasting the high levels of capital expenditures that
14 CenterPoint Houston expects to incur. Thus, Mr. Gorman’s reliance on the
15 authorized capital structures of other utilities within ERCOT is misplaced.

16 Second, it is my understanding that the recently authorized capital structures
17 for Oncor Electric Delivery Company, LLC and Texas New Mexico Power
18 Company were based on non-precedential settlements. Thus, they shed little light
19 on the appropriate capital structure for CenterPoint Houston.

20 Third, as I noted earlier, Mr. Gorman is not asking the Commission to
21 approve a 45.0% equity ratio. He is asking the Commission to approve a 40.0%
22 equity ratio, which would be a decrease of 500 basis points from CenterPoint

⁴⁰ Gorman Dir. at 29:7-9.

1 Houston's currently authorized equity ratio. Moreover, Mr. Gorman has identified
2 no material change in CenterPoint Houston's business and financial risk since the
3 Commission established that 45.0% equity ratio for CenterPoint Houston.
4 Therefore, if Mr. Gorman wants to foster "predictable and consistent" ratemaking
5 practices in Texas, he should be supporting an equity ratio of no less than 45.0%.

6 **Q. MR. GORMAN ALSO STATES THAT CENTERPOINT HOUSTON'S**
7 **"APPROVED CAPITAL STRUCTURE HAS ALLOWED CEHE TO**
8 **SUPPORT ITS CAPITAL INVESTMENT PROJECTS WHILE**
9 **PROVIDING RELIABLE SERVICE."**⁴¹ **DO YOU AGREE?**

10 A. I agree that CenterPoint Houston has been able to support its capital investment
11 projects, and I agree that CenterPoint Houston has provided reliable service. But
12 again, much of that occurred prior to the enactment of the TCJA. As noted earlier,
13 my direct testimony presented quantitative evidence showing CenterPoint Houston
14 will not be able to do that in the future and maintain its existing credit metrics
15 without an increase in its equity ratio.

16 **Q. MR. GORMAN'S FINAL REASON FOR ASSERTING THAT**
17 **CENTERPOINT HOUSTON'S PROPOSED CAPITAL STRUCTURE IS**
18 **UNREASONABLE IS THAT A "CAPITAL STRUCTURE WITH A**
19 **HIGHER COMMON EQUITY RATIO COMPONENT PLACES AN**
20 **UNREASONABLE BURDEN ON RATEPAYERS."**⁴² **DO YOU AGREE?**

21 A. No. That is simply a conclusory statement with no support. In contrast, my direct
22 testimony contains a quote from Dr. Roger Morin, a noted regulatory finance

⁴¹ Gorman Dir. at 29:10-11.

⁴² Gorman Dir. at 29:12-13.

1 expert, that both utilities and customers are best served by a utility with an A rating,
2 which is what CenterPoint Houston is seeking to maintain by virtue of a 50.0%
3 equity ratio. My capital structure recommendation will increase the chance of
4 CenterPoint Houston maintaining an A rating, whereas Mr. Gorman's
5 recommendation will not.

6 **Q. MR. GORMAN ALSO SUGGESTS THAT CUSTOMERS WOULD BE**
7 **BETTER OFF IF CENTERPOINT HOUSTON HAD A LOWER CREDIT**
8 **RATING THAN THEY WOULD BE WITH A HIGHER EQUITY RATIO.⁴³**
9 **WHAT IS YOUR RESPONSE?**

10 A. I disagree. Mr. Gorman takes a very short-term view involving only one debt
11 issuance. When a utility's credit rating is downgraded, however, that rating
12 typically does not rebound quickly, even in the face of improved financial metrics.
13 Therefore, if CenterPoint Houston's credit ratings fall, they may remain at the lower
14 level through many debt issuances, and customers will pay the higher costs
15 associated with those debt issuances for the entire lives of the bonds, which may be
16 two or three decades.

17 **C. Response to Ms. Winker's Capital Structure Arguments**

18 **Q. WHAT CAPITAL STRUCTURE IS MS. WINKER RECOMMENDING ON**
19 **BEHALF OF OPUC?**

20 A. As I noted earlier, Ms. Winker is recommending that the Commission adopt a
21 capital structure composed of 45.5% equity and 54.5% long-term debt.⁴⁴

⁴³ Gorman Dir. at 31:5-19.

⁴⁴ Winker Dir. at 43:5.

1 **Q. MS. WINKER ARGUES THAT CENTERPOINT HOUSTON HAS BEEN**
2 **ABLE TO IMPROVE ITS CREDIT RATINGS WITH ITS CURRENT**
3 **AUTHORIZED CAPITAL STRUCTURE, WHICH IS COMPOSED OF 55%**
4 **DEBT AND 45% EQUITY.⁴⁵ IS THAT A VALID REASON FOR THE**
5 **COMMISSION TO APPROVE A SIMILAR CAPITAL STRUCTURE IN**
6 **THIS CASE?**

7 A. No. It is true that the Company has been able to improve its credit ratings since the
8 2010 rate case, but that is hardly surprising given that the Company had a capital
9 structure composed of 60.0% debt and 40.0% equity before that time. The real
10 question is whether CenterPoint Houston will be able to maintain its current credit
11 metrics going forward with the large capital expenditure program and the reduced
12 cash flow attributable to the TCJA. For the reasons I have set forth, it likely will
13 not maintain those metrics absent measures such as an increase in its authorized
14 equity ratio.

15 **Q. MS. WINKER ALSO ASSERTS THAT CENTERPOINT HOUSTON'S**
16 **CURRENT CREDIT RATING HAS ALLOWED IT TO ISSUE LONG-**
17 **TERM DEBT AT REASONABLE RATES.⁴⁶ WHAT IS YOUR RESPONSE?**

18 A. I agree, and that is why CenterPoint Houston is asking the Commission for an
19 equity ratio that will support the Company's effort to maintain its current credit
20 ratings. The mere fact that CenterPoint Houston has not yet been downgraded
21 because of the TCJA's effects does not mean it is immune from such a downgrade.
22 The rating agencies made it very clear in publications after the enactment of the

⁴⁵ Winker Dir. at 42:8-16.

⁴⁶ Winker Dir. at 42:16-43:2.

1 TCJA that they were awaiting the regulatory agencies' responses in individual
2 utility cases before deciding whether to downgrade utilities.

3 **Q. MS. WINKER STATES, "CENTERPOINT HOUSTON WILL CONTINUE**
4 **TO BE ABLE TO ATTRACT FINANCIAL CAPITAL ON REASONABLE**
5 **TERMS USING" HER RECOMMENDED CAPITAL STRUCTURE.⁴⁷ HAS**
6 **SHE SUPPORTED THAT ASSERTION WITH ANY EVIDENCE?**

7 A. No. As far as I can tell, her only justification for that statement is that CenterPoint
8 Houston has been able to attract capital on reasonable terms since the enactment of
9 the TCJA. But as I explained earlier, rating agencies are awaiting the outcomes of
10 regulatory proceedings such as this one to determine how to rate utilities like
11 CenterPoint Houston on a going-forward basis. Therefore, the Commission should
12 not take any comfort from the fact that CenterPoint Houston has not been
13 downgraded thus far because of the effects of the TCJA.

14 **Q. DID MS. WINKER PERFORM ANY QUANTITATIVE ANALYSES TO**
15 **DETERMINE WHAT CENTERPOINT HOUSTON'S CREDIT METRICS**
16 **WOULD BE UNDER HER PROPOSED CAPITAL STRUCTURE?**

17 A. No. She admitted in response to discovery that she did not.⁴⁸

⁴⁷ Winker Dir. at 14-16.

⁴⁸ OPUC's Response to CenterPoint Energy Houston Electric LLC's Third Request for Information, request 3-10.

1 **D. Response to Mr. Ordonez’s Capital Structure Arguments**

2 **Q. WHAT CAPITAL STRUCTURE IS MR. ORDONEZ RECOMMENDING**
3 **ON BEHALF OF STAFF?**

4 A. As I noted earlier, Mr. Ordonez is recommending that the Commission adopt a
5 capital structure composed of 40.0% equity and 60.0% long-term debt.⁴⁹

6 **Q. WHAT IS MR. ORDONEZ’S RATIONALE FOR PROPOSING A CAPITAL**
7 **STRUCTURE COMPOSED OF 40.0% EQUITY AND 60.0% DEBT?**

8 A. His primary rationale appears to be that his capital structure recommendation is
9 consistent with the Commission’s ruling in Docket No. 22344, in which the
10 Commission found that a capital structure with 60.0% debt and 40.0% equity was
11 appropriate for the newly unbundled transmission and distribution utilities in
12 ERCOT.

13 **Q. IS MR. ORDONEZ’S RELIANCE ON THE DOCKET NO. 22344 ORDER**
14 **REASONABLE?**

15 A. No. His reliance on the Commission’s order in Docket No. 22344 is misplaced for
16 numerous reasons. First, in Docket No. 22344 the Commission established a
17 generic capital structure that was intended to apply to all of the transmission and
18 distribution utilities (“TDU”) that would operate within ERCOT. The Commission
19 did not consider any TDU’s individual circumstances in setting that capital
20 structure, in large part because the TDUs did not exist at that time in any real sense.
21 The Docket No. 22344 order was issued on December 22, 2000, over a year before
22 the then-integrated utilities were unbundled into TDUs, retail electric providers,

⁴⁹ Ordonez Dir. at 36:5-12.

1 and power generation companies. Thus, the generic capital structure established in
2 that case was intended to be a placeholder until the TDUs came into existence and
3 established their own standalone credit profiles. Indeed, the very order that Mr.
4 Ordonez relies on states that the Commission’s decision on capital structure and
5 ROE “are made for ratemaking purposes for the newly unbundled TDUs during the
6 transition period.”⁵⁰ CenterPoint Houston and other TDUs within ERCOT now
7 have their own standalone credit ratings and risk factors, and we are far beyond the
8 transition period, so it is no longer necessary or reasonable to rely on the generic
9 capital structure established in Docket No. 22344.

10 Second, Mr. Ordonez’s reliance on the Docket No. 22344 order is highly
11 selective. His analysis ignores the Commission’s statement in the Docket No.
12 22344 order that its decision was based “on the close correlation between the ROE
13 and capital structure.”⁵¹ As Mr. Ordonez correctly notes, the Commission
14 concluded in Docket No. 22344 that TDUs would be less risky than vertically
15 integrated utilities, but Mr. Ordonez overlooks the Commission’s statement in that
16 same order that the higher financial risk associated with greater leverage gave rise
17 to the need for a higher ROE. Accordingly, the Commission approved an ROE of
18 11.25% for the TDUs, which reflected an upward adjustment of 50 basis points to
19 account for, among other things, the “potential rating uncertainty due to higher debt,
20 based on the adoption of 60% debt and 40% equity for capital structure in this

⁵⁰ *Generic Issues Associated with Applications for Approval of Unbundled Cost of Service Rates Pursuant to PURA § 39.201 and Public Utility Commission Substantive Rule § 25.344*, Docket No. 22344, Order No. 42, Interim Order Establishing Return on Equity and Capital Structure at 8-9 (Dec. 22, 2000).

⁵¹ *Id.* at 9.

1 proceeding.”⁵² In contrast to the Commission’s action in Docket No. 22344, Mr.
2 Ordonez has not adjusted his ROE upward in this case to increase for the increased
3 financial risk that his recommended capital structure would produce.

4 Third, Mr. Ordonez ignores a more recent precedent—the Commission’s
5 2010 decision in Docket No. 38339 to authorize a capital structure composed of
6 55.0% debt and 45.0% equity for CenterPoint Houston. In that docket, the
7 Commission expressly found that a “capital structure of 55% debt and 45% equity
8 is reasonable in light of CenterPoint’s business and regulatory risks.”⁵³ Mr.
9 Ordonez makes no effort to explain how CenterPoint Houston’s business and
10 regulatory risks have changed enough since 2010 to justify reducing the equity ratio
11 by 500 basis points.

12 **Q. IN HIS TESTIMONY, MR. ORDONEZ SETS FORTH TWO REASONS**
13 **WHY HE BELIEVES THAT THE COMMISSION’S CONCLUSION IN**
14 **DOCKET NO. 22344 “REMAINS RELEVANT.”⁵⁴ DO YOU AGREE WITH**
15 **HIS REASONS?**

16 A. No. Mr. Ordonez’s first reason for maintaining that the Docket No. 22344 order
17 remains relevant is that the rating agencies have characterized the Texas regulatory
18 environment as being “constructive” or “credit positive.”⁵⁵ His second reason is
19 that the Commission stated in Project No. 46046 that the ratemaking mechanisms

⁵² *Id.* at 10.

⁵³ *Application of CenterPoint Electric Delivery Company, LLC for Authority to Change Rates*, Docket No. 38339, Order on Rehearing at 21, Finding of Fact No. 68 (June 23, 2011).

⁵⁴ Ordonez Dir. at 37:1-2.

⁵⁵ Ordonez Dir. at 37:4-5.

1 for TDUs in ERCOT are serving their intended purpose.⁵⁶ From those premises,
2 he concludes that TDUs in ERCOT operate in a “low risk environment.”

3 **Q. DO THOSE REASONS JUSTIFY AUTHORIZING A CAPITAL**
4 **STRUCTURE THAT THE COMMISSION ESTABLISHED 19 YEARS AGO**
5 **FOR THE PERIOD IN WHICH TDUs WERE TRANSITIONING TO**
6 **COMPETITION?**

7 A. No. Under Mr. Ordonez’s rationale, there would be no need to consider an
8 individual utility’s circumstances in establishing that utility’s capital structure. The
9 Commission could just set a generic capital structure for all utilities based on the
10 existing regulatory framework. But that is not what the Commission has chosen to
11 do. It instead reviews the facts and circumstances in each case. Thus, Mr.
12 Ordonez’s recommendation is directly contrary to Commission practice and
13 precedent.

14 Moreover, it is ironic that Mr. Ordonez cites to the rating agencies’
15 characterization of the Texas regulatory framework as being constructive and
16 credit-positive to support his capital structure recommendation. The rating
17 agencies would undoubtedly view it as non-constructive and credit-negative if the
18 Commission were to lower CenterPoint Houston’s authorized equity ratio by 500
19 basis points based on the rationale that the Commission established a generic debt
20 ratio of 60% in a proceeding that occurred almost 20 years ago. Indeed, the
21 Moody’s report that I discussed earlier expressly states that [REDACTED]

22 [REDACTED].⁵⁷

⁵⁶ Ordonez Dir. at 37:5-12.

⁵⁷ Exhibit R-RBM-3 at 1.

1 **Q. MR. ORDONEZ ALSO ASSERTS THAT HIS RECOMMENDED CAPITAL**
2 **STRUCTURE IS CONSISTENT WITH THE CAPITAL STRUCTURES**
3 **AUTHORIZED BY THE COMMISSION FOR THE MAJORITY OF TDUs**
4 **OPERATING IN ERCOT.⁵⁸ WHAT IS YOUR RESPONSE?**

5 A. I have several responses. First, the capital structure analysis should be focused
6 primarily on whether an individual utility's capital structure is set at a level that is
7 appropriate for its business and financial risks and whether the capital structure
8 would allow the utility to maintain access to the capital markets on reasonable
9 terms. As I noted earlier, the Commission found in CenterPoint Houston's last rate
10 case that the Company's business and regulatory risks justified a capital structure
11 composed of 55.0% debt and 45.0% equity, and Mr. Ordonez has made no showing
12 of changed circumstances that would justify a 500-basis-point reduction in the
13 capital structure. On the other hand, I have presented a quantitative analysis
14 showing that CenterPoint Houston needs an increase in its authorized equity ratio
15 just to maintain its current credit metrics.

16 Second, even if it were appropriate to ignore business and financial risk and
17 focus instead on a headcount of utilities in ERCOT with a particular capital
18 structure, Mr. Ordonez's analysis would not stand up to scrutiny. His list of five
19 utilities with a 40.0% equity ratio double-counts AEP Texas, which is no longer
20 divided into AEP Texas North Company and AEP Texas Central Company.
21 Moreover, Mr. Ordonez fails to note that AEP Texas has a currently pending rate
22 case in which it is requesting an equity ratio of 45.0%. Mr. Ordonez's list of utilities

⁵⁸ Ordonez Dir. at 37:18-20.

1 with a 40.0% equity ratio also includes three transmission-only utilities, which have
2 lower risk than a TDU. In contrast, his list of four utilities with an equity ratio
3 higher than 40.0% includes three TDUs and only one transmission-only utility.
4 More to the point, it includes CenterPoint Houston, which is the utility whose
5 capital structure is at issue in this case.

6 Third, if CenterPoint Houston's capital structure is to be based on a
7 comparison to other utilities' authorized capital structure, that comparison should
8 extend beyond the TDUs in ERCOT, because CenterPoint Houston competes for
9 capital with utilities across the country, not just in ERCOT. Mr. Ordonez's own
10 testimony demonstrates that the national average authorized equity ratio for
11 delivery-only utilities such as CenterPoint Houston was 49.91% in 2018.⁵⁹

12 **Q. MR. ORDONEZ ATTEMPTS TO MINIMIZE THAT COMPARISON TO**
13 **THE NATIONAL AVERAGE BY ARGUING THAT MOST OTHER**
14 **DELIVERY COMPANIES PURCHASE AND SELL ELECTRICITY,**
15 **WHEREAS CENTERPOINT HOUSTON DOES NOT.⁶⁰ IS THAT A VALID**
16 **DISTINCTION?**

17 **A.** No. That is simply one risk factor out of many for utilities, and Mr. Ordonez does
18 not appear to have performed any analysis to determine areas in which CenterPoint
19 Houston might have more risk than other utilities. For example, CenterPoint
20 Houston has significant hurricane risk, whereas many of the other delivery-only
21 companies do not. And as S&P has recognized, CenterPoint Houston has limited

⁵⁹ Ordonez Dir. at 36:2.

⁶⁰ Ordonez Dir. At 35:4-14.

1 geographic and regulatory diversity, given that its service area is limited to the Gulf
2 Coast area around Houston.⁶¹

3 **Q. MR. ORDONEZ DISCOUNTS CENTERPOINT HOUSTON'S**
4 **HURRICANE RISK BY ARGUING THAT TEXAS LAW ALLOWS**
5 **UTILITIES TO RECOVER STORM RESTORATION COSTS AND TO**
6 **OBTAIN SECURITIZATION FINANCING FOR THOSE COSTS.⁶² DO**
7 **YOU AGREE THAT ADEQUATELY MITIGATES CENTERPOINT**
8 **HOUSTON'S HURRICANE RISK?**

9 A. No. Texas law does allow recovery of storm restoration costs and provides a
10 securitization vehicle to do so, but as I pointed out in my direct testimony, the
11 damage must exceed \$100 million net of insurance proceeds in order to obtain
12 securitization, and the delay in obtaining the securitization funds can be lengthy.
13 Perhaps more importantly, the ability to recover storm restoration costs does
14 nothing to compensate CenterPoint Houston for the lost energy sales during the
15 time it takes to restore service after a hurricane. After Hurricane Harvey, for
16 example, it took several weeks to restore service in parts of the CenterPoint
17 Houston service area because those areas were simply underwater. CenterPoint
18 Houston was not supplying electricity to those areas during that time, and therefore
19 it was forgoing revenue as a result of the hurricane. Mr. Ordonez overlooks that
20 risk completely.

⁶¹ Exhibit R-RBM-4 at 4.

⁶² Ordonez Dir. at 32:1-8.

1 **Q. MR. ORDONEZ ALSO TAKES ISSUE WITH YOUR OTHER REASONS**
2 **FOR REQUESTING A CAPITAL STRUCTURE COMPOSED OF 50.0%**
3 **EQUITY AND 50.0% DEBT – THE COMPANY’S LARGE CAPITAL**
4 **EXPENDITURE PROGRAM AND THE TCJA EFFECTS.⁶³ WHAT IS**
5 **YOUR RESPONSE?**

6 A. Mr. Ordonez is essentially quarreling with the rating agencies, which have
7 identified those as risks for CenterPoint Houston. In its most recent report on
8 CenterPoint Houston, S&P listed [REDACTED]
9 [REDACTED].⁶⁴
10 And as I noted earlier, the June 2019 Moody’s report expressly cites [REDACTED]
11 [REDACTED]
12 [REDACTED].

13 **Q. MR. ORDONEZ FURTHER CONTENDS THAT CENTERPOINT**
14 **HOUSTON IS ASKING THE COMMISSION TO “PROVIDE**
15 **EXTRAORDINARY RELIEF IN HELPING CEHE MAINTAIN AN A-**
16 **ISSUER RATING.”⁶⁵ DO YOU AGREE WITH THAT**
17 **CHARACTERIZATION?**

18 A. No. CenterPoint Houston is simply asking the Commission to authorize a capital
19 structure that will allow the Company to continue having access to capital on
20 reasonable terms. Ultimately, the beneficiaries of lower bond coupon rates are
21 customers, not CenterPoint Houston, because the costs of debt are passed through

⁶³ Ordonez Dir. at 31:8-21.

⁶⁴ Exhibit R-RBM-4 at 2.

⁶⁵ Ordonez Dir. at 12-13.

1 in rates on a dollar-for-dollar basis. Moreover, if CenterPoint Houston experiences
2 a downgrade, its cost of equity will rise as well, which will also affect customers.

3 I do not view a request to control capital costs as a form of “extraordinary relief.”

4 **Q. DO YOU HAVE ANY CONCLUDING REMARKS REGARDING MR.**
5 **ORDONEZ’S CAPITAL STRUCTURE RECOMMENDATION?**

6 A. Yes. Mr. Ordonez has provided no cogent rationale for the Commission to reject
7 CenterPoint Houston’s proposed capital structure, and he certainly has provided no
8 reason to reduce CenterPoint Houston’s existing equity ratio by 500 basis points.
9 Notably, he has not even attempted to determine how his capital structure
10 recommendation would affect CenterPoint Houston’s credit metrics, nor has he
11 taken issue with my quantitative analysis showing that CenterPoint Houston needs
12 an equity ratio containing 50.0% equity to maintain its current credit metrics.
13 Therefore, the Commission should reject his capital structure recommendation.

14 **IV. WEIGHTED AVERAGE COST OF CAPITAL**

15 **Q. WHAT WACC ARE YOU RECOMMENDING FOR CENTERPOINT**
16 **HOUSTON IN THIS CASE?**

17 A. I recommend that the Commission approve a WACC of 7.39%. That WACC is
18 calculated using my recommended capital structure composed of 50.0% equity and
19 50.0% debt, the 4.38% cost of long-term debt, and the 10.40% ROE supported by
20 Mr. Hevert.

1 **Q. WILL A 7.39% WACC BE SUFFICIENT TO SUPPORT CENTERPOINT**
2 **HOUSTON'S FINANCIAL INTEGRITY AND TO PRESERVE ITS**
3 **CREDIT METRICS AT A LEVEL THAT WILL SUPPORT THE**
4 **CURRENT CREDIT RATINGS?**

5 A. I cannot say definitively how the rating agencies will react to a decision from the
6 Commission, of course, but the 7.39% that CenterPoint Houston is requesting in
7 this case will certainly increase the chances that CenterPoint Houston is able to
8 maintain its current credit ratings.

9 **Q. DO CUSTOMERS BENEFIT FROM A UTILITY THAT PERFORMS**
10 **WELL FINANCIALLY?**

11 A. Yes. A utility that performs well financially will attract capital more easily and at
12 a lower cost, which can then be invested in the infrastructure needed to provide safe
13 and reliable service, all to the benefit of customers.

14 **V. EFFECT OF CITIES' RECOMMENDATIONS ON CREDIT METRICS**

15 **Q. HAVE YOU REVIEWED THE RECOMMENDATIONS OF LANE**
16 **KOLLEN ON BEHALF OF GULF COAST COALITION OF CITIES?**

17 A. Yes. In Table 1 of his direct testimony, Mr. Kollen provides a list of the cities'
18 proposed revenue requirement adjustments, the amount of each adjustment, the
19 sponsoring city group, and the witness proposing the adjustment. Taken together,
20 those adjustments would result in a -\$210.041 million change in rates.

1 **Q. HAVE YOU CONDUCTED AN ANALYSIS TO DETERMINE THE**
 2 **IMPACT OF MR. KOLLEN'S ADJUSTMENTS ON THE CREDIT**
 3 **QUALITY OF CENTERPOINT HOUSTON?**

4 A. Yes. The proposed changes would result in a material weakening of CenterPoint
 5 Houston's credit quality.

6 **Q. WHAT ARE THE KEY ASSUMPTIONS OF YOUR ANALYSIS?**

7 A. The key assumptions include the following:

- 8 • The \$158 million of securitization excess accumulated deferred income tax
 9 liability is accrued by year-end 2019, with an offsetting equity infusion to
 10 maintain capital structure at 55% debt / 45% equity, and with no other
 11 changes to 2019.
- 12 • New rates are effective in 2020, and CenterPoint Houston is recapitalized
 13 to 60% debt / 40% equity by year-end 2020, consistent with other forecasts
 14 provided.
- 15 • CenterPoint issues an additional \$500 million of long-term debt over the
 16 plan period, primarily as a result of the change to capital structure. The
 17 increase is assumed to begin in 2021.
- 18 • All other adjustments to the plan are derived from Mr. Kollen's testimony.

19 **Q. WHAT IS THE RESULTING CREDIT METRICS?**

20 A. As shown in Exhibit R-RBM-8, the assumptions produce a range of FFO/Debt of
 21 10.0% to 11.6% in 2020-2023 under S&P's metrics.

22

Table 6

S&P Credit Metrics	2019	2020	2021	2022	2023
FFO/Debt	15.3%	10.3%	10.0%	10.6%	11.6%
Debt/EBITDA	4.36	6.46	6.59	6.35	5.99
Operating Cash Flow/Total Debt	14.5%	10.2%	9.1%	9.7%	10.8%

1 **Q. DO THESE CREDIT METRICS SUPPORT CENTERPOINT HOUSTON'S**
2 **CURRENT CREDIT RATINGS?**

3 A. No. S&P's recent CenterPoint Houston credit update stated that S&P's base case
4 assumption for FFO/Debt was 18%-20%, and the base case assumption for
5 Operating Cash Flow to Debt is 18%-19%. The percentages in Table 6 are far
6 below that expectation.

7 **Q. HOW DOES S&P CURRENTLY DEFINE CENTERPOINT HOUSTON'S**
8 **FINANCIAL RISK?**

9 A. In that same report, S&P states that CenterPoint Houston has "Intermediate"
10 financial risk.

11 **Q. DO THE RESULTING CREDIT METRICS PROVIDED IN TABLE 6**
12 **SUPPORT CENTERPOINT HOUSTON'S INTERMEDIATE FINANCIAL**
13 **RISK, AS DEFINED BY S&P?**

14 A. No. S&P's corporate methodology provides the following ranges for financial risk
15 for a utility on the low volatility table, which S&P currently uses to evaluate
16 CenterPoint Houston.

17 **Table 7**

Financial Risk	FFO/Debt	Debt/EBITDA	CFO/Debt
Minimal	35%+	Less than 2x	30%+
Modest	23-35%	2-3x	20-30%
Intermediate	13-23%	3-4x	12-20%
Significant	9-13%	4-5x	8-12%
Aggressive	6-9%	5-6x	5-8%
Highly Leveraged	Less than 6%	Greater than 6x	Less than 5%

1 The FFO/Debt ratio of 10.0%-11.6% produced by Mr. Kollen's recommendations
2 would fall below the Intermediate range into Significant financial risk; the
3 Debt/EBITDA range of 6.46x in 2020 to 5.99x in 2023 would be considered Highly
4 Leveraged; and the OCF/Debt range would be considered Significant. All three of
5 these financial risk measures are below CenterPoint Houston's current Intermediate
6 financial risk.

7 **VI. LONG-TERM INCENTIVE COMPENSATION**

8 **Q. DO YOU HAVE A RESPONSE TO THE INTERVENORS' PROPOSALS TO**
9 **REMOVE ALL LTI COSTS?**

10 A. Yes. Company witness Lynne Harkel-Rumford explains that the portion of LTI
11 related to restricted stock awards is purely time-based and not tied to the
12 achievement of financial goals. The Company's requested LTI expenses related to
13 restricted stock awards is \$3.8 million. Therefore, even if the Commission were to
14 adopt the Intervenor's recommendations to disallow LTI costs based on financial
15 goals, it would not be appropriate to disallow costs related to the restricted stock
16 awards. The mere fact that the LTI related restricted stock awards are not held on a
17 cash basis should not determine whether the Company should be reimbursed for
18 the cost of restricted stock awards. First, the Company is required to accrue expense
19 for stock-based incentive awards under Generally Accepted Accounting Principles
20 ("GAAP") because it's considered the most appropriate method to capture the costs
21 associated with paying an employee with shares instead of cash. While it is a non-
22 cash expense (due to the way the expense is calculated), it is meant to represent our
23 costs under the accounting rules. Second, if CenterPoint Energy Inc. were to issue
24 those shares in the public market, it would receive cash consideration. Since these

1 shares are issued as a form of compensation without a cash inflow associated with
2 them, CenterPoint Energy Inc. allocates a portion of that compensation expense to
3 the Company in order to make itself whole. This expense is settled during
4 intercompany settlement, thereby effecting a cash outflow by the Company.
5 Without the ability for the Company to include these LTI costs in its cost of service,
6 the Company will not be made whole for expenses it incurred.

7 **Q. DOES THIS CONCLUDE YOUR REBUTTAL TESTIMONY?**

8 **A. Yes.**

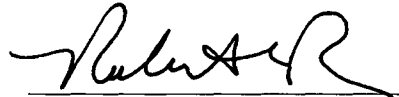
STATE OF TEXAS §
 §
COUNTY OF HARRIS §

AFFIDAVIT OF ROBERT B. McRAE

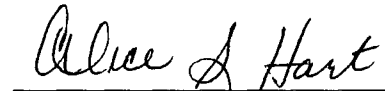
BEFORE ME, the undersigned authority, on this day personally appeared Robert B. McRae, who having been placed under oath by me did depose as follows:

1. “My name is Robert B. McRae. I am of sound mind and capable of making this affidavit. The facts stated herein are true and correct based upon my personal knowledge.
2. I have prepared the foregoing Rebuttal Testimony and the information contained in this document is true and correct to the best of my knowledge.”

Further affiant sayeth not.


Robert B. McRae

SUBSCRIBED AND SWORN TO BEFORE ME on this 17th day of June, 2019.


Notary Public in and for the State of Texas



My commission expires: 07/17/2019

Exhibits R-RBM-1 through R-RBM-4 are Confidential and will be provided pursuant to the terms of the Protective Order issued in Docket No. 49421.

CenterPoint Energy Houston Electric

Financials (2019-2023)

(For the Year Ended or As of December 31, Dollars in Millions)

Line	Income Statement	2018	2019	2020	2021	2022	2023
1	Revenues	\$ 3,004.0	\$ 2,984.9	\$ 3,135.4	\$ 3,275.6	\$ 3,441.7	
2	Revenues Adjusted	(\$35)	(\$24)	(\$44)	(\$46)	(\$51)	
3	Total Revenues	\$ 2,969.1	\$ 2,961.2	\$ 3,091.9	\$ 3,229.1	\$ 3,390.9	
4	Operating and Administrative	1,503.4	1,532.3	1,599.5	1,662.6	1,770.5	
5	Taxes Other Than Income	252.0	261.8	269.3	277.0	284.5	
6	Depreciation and Amortization	650.9	592.3	622.7	640.0	652.3	
7	Operating Income	562.7	574.8	600.4	649.6	683.5	
8	Interest Income (intercompany)	20.5	14.5	7.7	2.6	0.1	
9	Other Income	(9.9)	(9.2)	(5.8)	(6.6)	(8.5)	
10	EBIT	573.2	580.0	602.4	645.6	675.2	
11	Securitization Interest	39.7	28.0	20.8	13.4	7.6	
12	Int External	163.5	174.4	185.2	203.0	211.2	
13	Additional						
14	Other Interest (external)	163.5	174.4	185.2	203.0	211.2	
15	Additional Long-term Debt Interest	16.6	18.2	18.9	20.3	21.4	
16	Other Interest (intercompany)	-	-	0.1	2.2	5.3	
17	EBT	353.5	359.5	377.4	406.8	429.7	
18	Tax Adjustment	(10.8)	(8.8)	(13.1)	(14.0)	(15.2)	
19	Tax Expense	74.7	60.7	61.2	70.1	77.9	
20	Net Income before Non-Recurring Items	267.9	290.0	303.0	322.8	336.7	
21	Non-Recurring Items	-	-	-	-	-	
22	Net Income	\$ 267.9	\$ 290.0	\$ 303.0	\$ 322.8	\$ 336.7	
23	Credit Metrics						
24	S&P						
25	Funds From Operations / Total Debt	13.2%	13.0%	13.3%	13.6%	13.6%	
26	Total Debt / EBITDA	4.93	5.01	4.98	4.97	5.04	
27	Operating Cash Flow / Total Debt	13.3%	13.8%	13.4%	13.4%	13.3%	
28	ROE	9.23%	9.27%	9.26%	9.24%	9.23%	
29	CEHE Model ROE	10.1%	9.6%	10.2%	10.2%	10.3%	
30	ROE Change	-0.9%	-0.4%	-1.0%	-1.0%	-1.1%	

Error #1:
subtracts
negative tax
adjustment
from EBT not
tax
adjustment
IE for 2019 NI:
353.5-(74.7-
10.8) = 289.5

Error #2: Net
Income on
Income
Statement does
not match Net
Income on the
Cash Flow

Line	Cash Flows	2018	2019	2020	2021	2022	2023
31	Net Income	\$ 330.2	\$ 340.8	\$ 378.6	\$ 403.5	\$ 424.0	
32	Non-Recurring Items, net of tax	-	-	-	-	-	
33	Net Income before Non-Recurring Items	330.2	340.8	378.6	403.5	424.0	
34	Depreciation and Amortization	650.9	592.3	622.7	640.0	652.3	
35	Amortization of Deferred Financing Costs	10.5	10.2	9.9	8.6	6.9	
36	Deferred Taxes	(69.2)	(61.3)	(65.3)	(54.2)	(43.8)	
37	Funds From Operations	922.5	882.0	945.8	997.8	1,039.4	
38	Changes in Working Capital	(48.7)	(23.5)	(68.9)	(74.4)	(84.6)	
39	Operating Cash Flow	873.8	858.5	876.9	923.4	954.8	
40	Capital Expenditures	(979.1)	(1,027.9)	(1,177.9)	(978.8)	(980.0)	
41	Other Investing Activities	-	-	-	-	-	
42	Investing Cash Flow	(979.1)	(1,027.9)	(1,177.9)	(978.8)	(980.0)	
43	Increase (decrease) in Intercompany Notes Payable	(589.8)	123.8	503.7	77.2	220.3	
44	Increase (decrease) in Securitization Debt	(264.3)	(176.4)	(181.6)	(169.3)	(148.7)	
45	Increase (decrease) in Other Long Term Debt	700.0	300.0	197.6	300.0	200.0	
46	Dividends	259.4	(77.9)	(218.7)	(152.5)	(246.4)	
47	Other Financing Activities	-	-	-	-	-	
48	Financing Cash Flow	105.3	169.4	301.0	55.4	25.1	
49	Total Cash Flow	\$ -	\$ -	\$ -	\$ 0.0	\$ 0.0	

Error #3: Gorman
did not update
Financing section
to reflect
rebalancing the
capital structure
or to reflect lower
revenue or lower
net income

CenterPoint Energy Houston Electric

Financials (2019-2023)

(For the Year Ended or As of December 31, Dollars in Millions)

Line	Balance Sheet	2018	2019	2020	2021	2022	2023
50	ASSETS						
51	Cash/Temporary Investments	\$ (0.2)	\$ 588.4	\$ 464.6	\$ (0.2)	\$ (0.2)	\$ (0.2)
52	Current Assets	949.5	998.1	1,021.3	1,045.2	1,070.4	1,096.8
53	PP&E, net	8,401.7	8,993.4	9,604.9	10,341.4	10,849.4	11,325.6
54	Other Assets	1,156.1	928.5	771.4	625.4	493.2	388.5
55	Total Assets	<u>\$ 10,507.1</u>	<u>\$ 11,508.4</u>	<u>\$ 11,862.2</u>	<u>\$ 12,011.8</u>	<u>\$ 12,412.8</u>	<u>\$ 12,810.8</u>
56	LIABILITIES AND EQUITY						
57	Facility/Intercompany Debt	\$ 1.2	\$ -	\$ -	\$ 38.9	\$ 116.1	\$ 336.4
58	Other Current Liabilities	630.3	655.6	679.8	696.2	715.6	731.4
59	Total Current Liabilities	631.5	655.6	679.8	735.1	831.7	1,067.8
60	Non-Recourse Securitization Debt	1,435.4	1,171.8	995.9	814.7	645.6	497.0
61	Other Long Term Debt (external)	3,577.8	4,353.5	4,693.2	4,909.7	5,242.3	5,470.8
62	Other Long-Term Debt	3,281.5	3,984.7	4,288.0	4,489.0	4,792.2	4,995.6
63	Additional LTD	296.3	368.8	405.2	420.8	450.1	475.3
64	Deferred Income Taxes	1,022.9	953.7	892.4	827.1	772.9	729.1
65	Other Liabilities	1,454.4	1,471.5	1,472.1	1,452.1	1,425.5	1,398.8
66	Total Liabilities	8,121.9	8,606.1	8,733.4	8,738.7	8,918.0	9,163.5
67	Common Equity Adjustment	(296.3)	(368.8)	(405.2)	(420.8)	(450.1)	(475.3)
68	Common Equity	2,681.5	3,271.1	3,534.0	3,693.9	3,944.9	4,122.5
69	Common Equity, Adjusted	2,385.2	2,902.3	3,128.8	3,273.1	3,494.9	3,647.2
70	Total Equity	2,385.2	2,902.3	3,128.8	3,273.1	3,494.9	3,647.2
71	Total Liabilities and Equity	<u>\$ 10,507.1</u>	<u>\$ 11,508.4</u>	<u>\$ 11,862.2</u>	<u>\$ 12,011.8</u>	<u>\$ 12,412.8</u>	<u>\$ 12,810.8</u>
72	Balance check	(0.0)	(0.0)	(0.0)	(0.0)	(0.0)	(0.0)
73	Equity	2,385.2	2,902.3	3,128.8	3,273.1	3,494.9	3,647.2
74	Long-Term Debt	3,577.8	4,353.5	4,693.2	4,909.7	5,242.3	5,470.8
75	Total	5,963.00	7,255.76	7,821.98	8,182.85	8,737.17	9,118.06
76	Debt Ratio	60%	60%	60%	60%	60%	60%

CenterPoint Energy Houston Electric

S&P Methodology

(For the Year Ended or As of December 31, Dollars in Millions)

Line	Description	2019	2020	2021	2022	2023
DEBT:						
1	Balance Sheet Debt	5,525.3	5,689.1	5,763.3	6,004.0	6,304.2
2	Less Securitization Debt	(1,171.8)	(995.9)	(814.7)	(645.6)	(497.0)
3	Adjusted Debt (GAAP)	4,353.5	4,693.2	4,948.6	5,358.4	5,807.2
4	Plus Pension & Postretirement Underfunded Amount (After Tax)	45.2	42.5	39.9	37.5	35.2
5	Plus Asset Retirement Obligations (After Tax)	27.7	27.7	27.7	27.7	27.7
6	Plus Interest Accrued	77.3	81.4	86.4	92.1	92.2
7	Plus Unamortized Issuance Cost (Excluding Securitization)	15.6	13.7	12.2	10.9	9.9
8	Adjusted Debt (S&P)	4,519.3	4,858.5	5,114.7	5,526.6	5,972.1
INTEREST EXPENSE:						
9	Income Statement Interest	219.7	220.6	225.0	236.6	240.2
11	Less Securitization Interest (Cash and Non-Cash)	(39.7)	(28.0)	(20.8)	(13.4)	(7.6)
12	Adjusted Interest Expense (GAAP)	180.1	192.6	204.1	223.2	232.6
13	Plus Capitalized Interest	6.1	7.0	8.7	8.2	7.2
14	Plus Interest on Pension & Postretirement Underfunded Amounts	2.7	2.6	2.4	2.3	2.1
15	Plus Asset Retirement Obligations	1.0	1.0	1.0	1.0	1.0
16	Adjusted Interest Expense (S&P)	189.9	203.2	216.3	234.7	243.0
EBITDA:						
17	Unadjusted EBITDA	1,213.6	1,167.1	1,223.1	1,289.6	1,335.9
19	Less Securitization EBITDA	(303.2)	(203.9)	(202.1)	(182.4)	(156.2)
20	Adjusted EBITDA	910.4	963.2	1,021.0	1,107.1	1,179.7
21	Plus Interest on Pension & Postretirement Underfunded Amounts	5.7	5.4	5.1	4.8	4.5
22	Plus Asset Retirement Obligations	1.0	1.0	1.0	1.0	1.0
23	Adjusted EBITDA	917.2	969.6	1,027.1	1,112.9	1,185.2
FUNDS FROM OPERATIONS:						
24	Adjusted EBITDA (S&P)	917.2	969.6	1,027.1	1,112.9	1,185.2
26	Less Adjusted Interest Expense, net (S&P)	(189.9)	(203.2)	(216.3)	(234.7)	(243.0)
27	Less Current Taxes	(133.1)	(135.1)	(130.8)	(129.9)	(128.8)
28	Plus Pension & Postretirement Adjustment	1.4	1.3	1.2	1.1	1.1
29	Plus Asset Retirement Obligations	0.2	0.2	0.2	0.2	0.2
30	Adjusted Funds from Operations (S&P)	595.8	632.8	681.5	749.6	814.7
OCF, FOCF & DCF:						
31	Operating Cash Flow	873.8	858.5	876.9	923.4	954.8
33	Less Securitization OCF	(264.3)	(176.4)	(181.6)	(169.3)	(148.7)
34	Adjusted Operating Cash Flow	609.5	682.0	695.3	754.1	806.1
35	Plus Pension & Postretirement Adjustment	(2.5)	(2.3)	(2.2)	(2.1)	(1.9)
36	Less Capitalized Interest	(6.1)	(7.0)	(8.7)	(8.2)	(7.2)
37	Plus Asset Retirement Obligations	(0.8)	(0.8)	(0.8)	(0.8)	(0.8)
38	Adjusted Operating Cash Flow (S&P)	600.2	671.9	683.6	743.0	796.2
39	Less Capital Expenditures	(979.1)	(1,027.9)	(1,177.9)	(978.8)	(980.0)
40	Plus Capitalized Interest	6.1	7.0	8.7	8.2	7.2
41	Free Operating Cash Flow (S&P)	(372.9)	(349.0)	(485.6)	(227.6)	(176.6)
42	Less Dividends	259.4	(77.9)	(218.7)	(152.5)	(246.4)
43	Discretionary Operating Cash Flow (S&P)	(113.5)	(426.9)	(704.3)	(380.0)	(423.0)
Core Ratios						
45	FFO / Total Debt	13.2%	13.0%	13.3%	13.6%	13.6%
46	Total Debt / EBITDA	4.93	5.01	4.98	4.97	5.04
Supplemental Ratios						
48	OCF / Total Debt	13.3%	13.8%	13.4%	13.4%	13.3%
49	FOCF / Total Debt	-8.3%	-7.2%	-9.5%	-4.1%	-3.0%
50	DCF / Total Debt	-2.5%	-8.8%	-13.8%	-6.9%	-7.1%
51	EBITDA Interest Coverage	4.83	4.77	4.75	4.74	4.88
52	FFO Interest Coverage	4.14	4.11	4.15	4.19	4.35

Source
TIEC03-13 Financial Metrics - Excel

CenterPoint Energy Houston Electric
 FYE or As of December 31, Dollars in Millions)

SOAH DOCKET NO. 473-19-3864
 PUC Docket No. 49421
 Exhibit R-RBM-6
 1 of 8

Red Text = Gorman Edits to CEHE Financials Blue Text = CNP adjustments to MPG-5

Line	Income Statement	2019	2020	2021	2022	2023
		2018	2019	2020	2021	2022
1	Revenues	\$ 3,004.0	\$ 2,984.9	\$ 3,135.4	\$ 3,275.6	\$ 3,441.7
2	Revenues Adjusted	(\$35)	(\$24)	(\$44)	(\$46)	(\$51)
3	Total Revenues	\$ 2,969.1	\$ 2,961.2	\$ 3,091.9	\$ 3,229.1	\$ 3,390.9
4	Operating and Administrative	1,503.4	1,532.3	1,599.5	1,662.6	1,770.5
5	Taxes Other Than Income	252.0	261.8	269.3	277.0	284.5
6	Depreciation and Amortization	650.9	592.3	622.7	640.0	652.3
7	Operating Income	562.7	574.8	600.4	649.6	683.5
8	Interest Income (intercompany)	20.5	14.5	7.7	2.6	0.1
9	Other Income	(9.9)	(9.2)	(5.8)	(6.6)	(8.5)
10	EBIT	573.2	580.0	602.4	645.6	675.2
11	Securitization Interest	39.7	28.0	20.8	13.4	7.6
12	Int External	163.5	174.4	185.2	203.0	211.2
13	Additional					
14	Other Interest (external)	163.5	174.4	185.2	203.0	211.2
15	Additional Long-term Debt Interest	16.6	18.2	18.9	20.2	21.4
16	Other Interest (intercompany)	-	-	0.1	2.2	5.3
17	EBT	353.4	359.5	377.4	406.9	429.8
18	Tax Adjustment	(10.8)	(8.8)	(13.1)	(14.0)	(15.2)
19	Tax Expense	74.7	60.7	61.2	70.1	77.9
20	Net Income before Non-Recurring Items	289.5	307.6	329.3	350.8	367.0
21	Non-Recurring Items	-	-	-	-	-
22	Net Income	\$ 289.5	\$ 307.6	\$ 329.3	\$ 350.8	\$ 367.0

Error #1:
 subtracts negative tax adjustment from EBT not tax adjustment. IE for 2019 NI: 353.5-(74.7-10.8) = 289.5 not 267.9
Adjustment #1:
 Corrected formula to EBT-(Tax Expense+Tax Adjustment)

Error #2:
 Mismatch of Net Income numbers between income statement and cashflow

Red Text = Gorman Edits to CEHE Financials Blue Text = CNP adjustments to MPG-5

	2019	2020	2021	2022	2023
23 <u>Credit Metrics</u>					
24 <u>S&P</u>					
25 Funds From Operations / Total Debt	13.2%	13.0%	13.3%	13.6%	13.6%
26 Total Debt / EBITDA	4.93	5.01	4.98	4.97	5.04
27 Operating Cash Flow / Total Debt	12.4%	13.1%	12.4%	12.5%	12.4%
28 ROE	9.98%	9.83%	10.06%	10.04%	10.06%
29 CEHE Model ROE	10.10%	9.64%	10.25%	10.23%	10.29%
30 ROE Change	-0.1%	0.2%	-0.2%	-0.2%	-0.2%

Comment #1:
 ROE exceeds
 Gormans
 proposed ROE;
 Gorman uses
 GAAP ROE in this
 calculation

Error #2:
 Mismatch of Net
 Income numbers
 between Income
 statement and
 Cash Flow
 statement

Line	Cash Flows	2018	2019	2020	2021	2022	2023
	prior Gorman	\$ 330.2	\$ 340.8	\$ 378.6	\$ 403.5	\$ 424.0	X
	delta	\$ (40.7)	\$ (33.2)	\$ (49.3)	\$ (52.7)	\$ (57.0)	X
31	Net Income From I/S	\$ 289.5	\$ 307.6	\$ 329.3	\$ 350.8	\$ 367.0	X
32	Non-Recurring Items, net of tax	-	-	-	-	-	
33	Net Income before Non-Recurring Items	289.5	307.6	329.3	350.8	367.0	
34	Depreciation and Amortization	650.9	592.3	622.7	640.0	652.3	
35	Amortization of Deferred Financing Costs	10.5	10.2	9.9	8.6	6.9	
36	Deferred Taxes	(69.2)	(61.3)	(65.3)	(54.2)	(43.8)	
37	Funds From Operations	881.8	848.8	896.5	945.1	982.4	
38	Changes in Working Capital	(48.7)	(23.5)	(68.9)	(74.4)	(84.6)	
39	Operating Cash Flow	833.1	825.3	827.6	870.7	897.8	

Adjustment #2:
 Linked Net
 Income on C/F
 statement to Net
 Income on I/S.
 Displayed prior NI
 from MPG-5 and
 the delta
 between it and
 the corrected NI
 for clarity

CenterPoint Energy Houston Electric
 FYE or As of December 31, Dollars in Millions)

SOAH DOCKET NO. 473-19-3864
 PUC Docket No. 49421
 Exhibit R-RBM-6
 3 of 8

Red Text = Gorman Edits to CEHE Financials Blue Text = CNP adjustments to MPG-5

	2019	2020	2021	2022	2023
40 Capital Expenditures	(979.1)	(1,027.9)	(1,177.9)	(978.8)	(980.0)
41 Other Investing Activities	-	-	-	-	-
42 Investing Cash Flow	(979.1)	(1,027.9)	(1,177.9)	(978.8)	(980.0)
43 Increase (decrease) in Intercompany Notes Payable	(589.8)	123.8	503.7	77.2	220.3
44 Increase (decrease) in Securitization Debt	(264.3)	(176.4)	(181.6)	(169.3)	(148.7)
45 Increase (decrease) in Other Long Term Debt	700.0	300.0	197.6	300.0	200.0
Additions to long term debt	369.1	36.2	15.1	29.1	25.2
Total Long Term Debt	1,069.1	336.2	212.6	329.1	225.2
46 Dividends	259.4	(77.9)	(218.7)	(152.5)	(246.4)
Additions to dividends	(328.4)	(3.0)	34.2	23.6	31.5
Total Dividends	(69.0)	(80.9)	(184.4)	(128.8)	(214.6)
47 Other Financing Activities	-	-	-	-	-
48 Financing Cash Flow	146.0	202.6	350.3	103.1	82.1
49 Total Cash Flow	\$ -	\$ -	\$ -	\$ 0.0	\$ -
	(1,000.1)	(255.3)	(28.2)	(200.2)	(10.6)

Error #3:
 Gorman did not update Financing section to reflect rebalancing capital structure or lower income
Adjustment 3#:
 Added rows for "Additions to Long Term Debt" and "Additions to Dividend" as well as totals for clarity.

Line	Balance Sheet	2018	2019	2020	2021	2022	2023
50	ASSETS						
51	Cash/Temporary Investments	\$ (0.2)	\$ 588.4	\$ 464.6	\$ (0.2)	\$ (0.2)	\$ (0.2)
52	Current Assets	949.5	998.1	1,021.3	1,045.2	1,070.4	1,096.8
53	PP&E, net	8,401.7	8,993.4	9,604.9	10,341.4	10,849.4	11,325.6
54	Other Assets	1,156.1	928.5	771.4	625.4	493.2	388.5

CenterPoint Energy Houston Electric
 FYE or As of December 31, Dollars in Millions)

SOAH DOCKET NO. 473-19-3864
 PUC Docket No. 49421
 Exhibit R-RBM-6
 4 of 8

Red Text = Gorman Edits to CEHE Financials Blue Text = CNP adjustments to MPG-5

	2019	2020	2021	2022	2023
55 Total Assets	\$ 10,507.1	\$ 11,508.4	\$ 11,862.2	\$ 12,011.8	\$ 12,412.8
LIABILITIES AND EQUITY					
57 Facility/Intercompany Debt	\$ 1.2	\$ -	\$ -	\$ 38.9	\$ 116.1
58 Other Current Liabilities	630.3	655.6	679.8	696.2	715.6
59 Total Current Liabilities	631.5	655.6	679.8	735.1	831.7
60 Non-Recourse Securitization Debt	1,435.4	1,171.8	995.9	814.7	645.6
61 Other Long Term Debt (external)	3,577.8	4,353.8	4,693.3	4,909.3	5,241.7
62 Other Long-Term Debt	3,281.5	3,984.7	4,288.0	4,489.0	4,792.2
63 Additional LTD	296.3	369.1	405.3	420.4	449.4
64 Deferred Income Taxes	1,022.9	953.7	892.4	827.1	772.9
65 Other Liabilities	1,454.4	1,471.5	1,472.1	1,452.1	1,425.5
66 Total Liabilities	8,121.9	8,606.4	8,733.5	8,738.3	8,917.3
67 Common Equity Adjustment	(296.3)	(328.4)	(331.4)	(297.2)	(273.6)
68 Common Equity	2,681.5	3,230.4	3,460.1	3,570.7	3,769.1
69 Common Equity, Adjusted	2,385.2	2,902.0	3,128.7	3,273.5	3,495.5
70 Total Equity	2,385.2	2,902.0	3,128.7	3,273.5	3,495.5
71 Total Liabilities and Equity	\$ 10,507.1	\$ 11,508.4	\$ 11,862.2	\$ 12,011.8	\$ 12,412.8
72 Balance check	(0.0)	(0.0)	(0.0)	(0.0)	(0.0)
73 Equity	2,385.2	2,902.0	3,128.7	3,273.5	3,495.5
74 Long-Term Debt	3,577.8	4,353.8	4,693.3	4,909.3	5,241.7

Adjustment 4#:
 1. Modified Common Equity to equal "Prior common equity" + Net Income (line 31) - Dividends (line 46).
 2. Modified Common Equity Adjustment to adjust for the change in revenue and to balance to 60/40 debt/equity cap structure

X
 X

CenterPoint Energy Houston Electric
 FYE or As of December 31, Dollars in Millions)

SOAH DOCKET NO. 473-19-3864
 PUC Docket No. 49421
 Exhibit R-RBM-6
 5 of 8

Red Text = Gorman Edits to CEHE Financials Blue Text = CNP adjustments to MPG-5

		2019	2020	2021	2022	2023	
75	Total	5,963.00	7,255.76	7,821.98	8,182.85	8,737.17	9,118.06
76	Debt Ratio	60.00%	60.00%	60.00%	60.00%	59.99%	59.99%
		3,578	4,353	4,693	4,910	5,242	5,471
		296	345	16	(15)	(3)	(9)

Red Text = Gorman Edits to CEHE Financials Blue Text = CNP adjustments to MPG-5

	2019	2020	2021	2022	2023
S&P					
Core Ratios					
FFO / Total Debt	13.2%	13.0%	13.3%	13.6%	13.6%
Total Debt / EBITDA	4.93	5.01	4.98	4.97	5.04
Supplemental Ratios					
OCF / Total Debt	12.4%	13.1%	12.4%	12.5%	12.4%
FOCF / Total Debt	-9.1%	-7.9%	-10.5%	-5.1%	-3.9%
DCF / Total Debt	-3.4%	-9.5%	-14.7%	-7.8%	-8.0%
EBITDA Interest Coverage	4.83	4.77	4.75	4.74	4.88
FFO Interest Coverage	4.14	4.11	4.15	4.19	4.35

Red Text = Gorman Edits to CEHE Financials Blue Text = CNP adjustments to MPG-5

	2019	2020	2021	2022	2023
Moody's (excluding Securitization)					
CFO pre-WC + Interest / Interest	4.32	4.37	4.21	4.15	4.21
Debt / Capitalization	54.3%	55.0%	55.7%	56.6%	57.9%
CFO pre-WC / Debt	13.5%	13.6%	13.0%	13.1%	13.0%
Total Debt / EBITDA	4.99	5.06	5.00	4.98	5.05
(FFO - Dividends) / Total Debt	12.0%	11.9%	9.4%	10.7%	9.4%
(FFO - Dividends) / Capital Expenditures	54.9%	56.0%	40.6%	60.0%	56.5%
Moody's (including Securitization)					
Funds From Operations Interest Coverage	4.92	4.74	4.72	4.68	4.71
Total Debt / Capital	59.9%	59.6%	59.4%	59.3%	59.8%
Funds From Operations / Total Debt	15.4%	14.3%	14.3%	14.5%	14.3%
Total Debt / EBITDA	4.71	5.03	4.84	4.77	4.83
(FFO - Dividends) / Total Debt	14.2%	12.9%	11.2%	12.4%	10.9%
(FFO - Dividends) / Capital Expenditures	115.4%	73.5%	53.1%	74.8%	68.4%

Red Text = Gorman Edits to CEHE Financials Blue Text = CNP adjustments to MPG-5

	2019	2020	2021	2022	2023
<u>Fitch</u>					
FFO Fixed-Charge Cover (x)	4.29	4.34	4.33	4.29	4.38
Debt as % of Total Capitalization	60.0%	60.0%	60.2%	60.5%	61.4%
FFO / Debt	14.1%	14.2%	14.3%	14.4%	14.3%
Total Adjusted Debt / Operating EBITDAR (x)	4.84	4.92	4.87	4.87	4.96
EBIT Interest Coverage	2.76	2.69	2.70	2.70	2.72
EBITDA Interest Coverage	4.83	4.78	4.77	4.71	4.78
Fitch FFO-adjusted leverage	5.45	5.42	5.37	5.34	5.41
Common Equity as % of Total Capitalization	44.5%	44.2%	43.4%	42.6%	41.1%
<u>Covenant Calculation</u>					
Covenant Debt / Capital	60.0%	60.0%	60.2%	60.5%	61.4%

CenterPoint Energy Houston Electric
 FYE or As of December 31, Dollars in Millions)

SOAH DOCKET NO. 473-19-3864
 PUC Docket No. 49421
 Exhibit R-RBM-7

1 of 8

Red Text = Gorman Edits to CEHE Financials Blue Text = CNP adjustments to MPG-5

Line	Income Statement	2019					2020					2021					2022					2023				
		2018	2019	2020	2021	2022	2023	2018	2019	2020	2021	2022	2023	2018	2019	2020	2021	2022	2023	2018	2019	2020	2021	2022	2023	
1	Revenues		\$ 3,004.0	\$ 2,984.9	\$ 3,135.4	\$ 3,275.6	\$ 3,441.7																			
2	Revenues Adjusted			(\$62)	(\$47)	(\$77)	(\$82)	(\$88)																		
3	Total Revenues		\$ 2,942.2	\$ 2,938.1	\$ 3,058.4	\$ 3,193.8	\$ 3,353.3																			
4	Operating and Administrative		1,503.4	1,532.3	1,599.5	1,662.6	1,770.5																			
5	Taxes Other Than Income		252.0	261.8	269.3	277.0	284.5																			
6	Depreciation and Amortization		650.9	592.3	622.7	640.0	652.3																			
7	Operating Income		535.8	551.7	567.0	614.3	646.0																			
8	Interest Income (intercompany)		20.5	14.5	7.7	2.6	0.1																			
9	Other Income		(9.9)	(9.2)	(5.8)	(6.6)	(8.5)																			
10	EBIT		546.3	557.0	568.9	610.3	637.7																			
11	Securitization Interest		39.7	28.0	20.8	13.4	7.6																			
12	Int External		163.5	174.4	185.2	203.0	211.2																			
13	Additional																									
14	Other Interest (external)		163.5	174.4	185.2	203.0	211.2																			
15	Additional Long-term Debt Interest		16.6	18.2	19.0	20.3	21.5																			
16	Other Interest (intercompany)		-	-	0.1	2.2	5.3																			
17	EBT		326.6	336.4	343.8	371.5	392.1																			
18	Tax Adjustment		(16.5)	(13.7)	(20.1)	(21.4)	(23.1)																			
19	Tax Expense		74.7	60.7	61.2	70.1	77.9																			
20	Net Income before Non-Recurring Items		268.3	289.4	302.8	322.9	337.3	X																		
21	Non-Recurring Items		-	-	-	-	-																			
22	Net Income		\$ 268.3	\$ 289.4	\$ 302.8	\$ 322.9	\$ 337.3	1																		

Comment #1:
 "Revenues Adjusted"
 lowered to adjust to ROE of 9.25% on line 28

CenterPoint Energy Houston Electric
 FYE or As of December 31, Dollars in Millions)

SOAH DOCKET NO. 473-19-3864
 PUC Docket No. 49421
 Exhibit R-RBM-7
 2 of 8

Red Text = Gorman Edits to CEHE Financials Blue Text = CNP adjustments to MPG-5

	2019	2020	2021	2022	2023		
23	<u>Credit Metrics</u>						
24	<u>S&P</u>						
25	Funds From Operations / Total Debt	12.7%	12.6%	12.7%	12.9%	13.0%	Comment #2: GAAP ROE now at Gorman's proposed limit
26	Total Debt / EBITDA	5.08	5.13	5.15	5.13	5.21	
27	Operating Cash Flow / Total Debt	11.9%	12.8%	11.9%	12.0%	11.9%	
28	ROE	9.25%	9.25%	9.25%	9.24%	9.25%	
29	CEHE Model ROE	10.10%	9.64%	10.25%	10.23%	10.29%	
30	ROE Change	-0.8%	-0.4%	-1.0%	-1.0%	-1.0%	

Line	Cash Flows	2018	2019	2020	2021	2022	2023
	prior Gorman	\$ 330.2	\$ 340.8	\$ 378.6	\$ 403.5	\$ 424.0	
	delta	\$ (61.9)	\$ (61.4)	\$ (75.8)	\$ (80.6)	\$ (86.7)	
31	Net Income	From I/S	\$ 268.3	\$ 289.4	\$ 302.8	\$ 322.9	\$ 337.3
32	Non-Recurring Items, net of tax		-	-	-	-	-
33	Net Income before Non-Recurring Items		268.3	289.4	302.8	322.9	337.3
34	Depreciation and Amortization		650.9	592.3	622.7	640.0	652.3
35	Amortization of Deferred Financing Costs		10.5	10.2	9.9	8.6	6.9
36	Deferred Taxes		(69.2)	(61.3)	(65.3)	(54.2)	(43.8)
37	Funds From Operations		860.6	830.6	870.0	917.2	952.7
38	Changes in Working Capital		(48.7)	(23.5)	(68.9)	(74.4)	(84.6)
39	Operating Cash Flow		811.9	807.1	801.1	842.8	868.1

CenterPoint Energy Houston Electric
 FYE or As of December 31, Dollars in Millions)

SOAH DOCKET NO. 473-19-3864
 PUC Docket No. 49421
 Exhibit R-RBM-7
 3 of 8

Red Text = Gorman Edits to CEHE Financials Blue Text = CNP adjustments to MPG-5

	2019	2020	2021	2022	2023
40 Capital Expenditures	(979.1)	(1,027.9)	(1,177.9)	(978.8)	(980.0)
41 Other Investing Activities	-	-	-	-	-
42 Investing Cash Flow	(979.1)	(1,027.9)	(1,177.9)	(978.8)	(980.0)
43 Increase (decrease) in Intercompany Notes Payable	(589.8)	123.8	503.7	77.2	220.3
44 Increase (decrease) in Securitization Debt	(264.3)	(176.4)	(181.6)	(169.3)	(148.7)
45 Increase (decrease) in Other Long Term Debt	700.0	300.0	197.6	300.0	200.0
Additions to long term debt	369.2	35.8	16.5	29.4	26.0
Total Long Term Debt	1,069.2	335.8	214.0	329.4	226.0
46 Dividends	259.4	(77.9)	(218.7)	(152.5)	(246.4)
Additions to dividends	(307.2)	15.6	59.3	51.2	60.7
Total Dividends	(47.9)	(62.4)	(159.3)	(101.2)	(185.7)
47 Other Financing Activities	-	-	-	-	-
48 Financing Cash Flow	167.2	220.8	376.8	136.0	111.8
49 Total Cash Flow	\$ (0.0)	\$ -	\$ -	\$ 0.0	\$ 0.0
	(1,021.3)	(273.5)	(54.7)	(228.1)	(40.3)

Line	Balance Sheet	2018	2019	2020	2021	2022	2023
50	ASSETS						
51	Cash/Temporary Investments	\$ (0.2)	\$ 588.4	\$ 464.6	\$ (0.2)	\$ (0.2)	\$ (0.2)
52	Current Assets	949.5	998.1	1,021.3	1,045.2	1,070.4	1,096.8
53	PP&E, net	8,401.7	8,993.4	9,604.9	10,341.4	10,849.4	11,325.6
54	Other Assets	1,156.1	928.5	771.4	625.4	493.2	388.5

CenterPoint Energy Houston Electric
 FYE or As of December 31, Dollars in Millions)

SOAH DOCKET NO. 473-19-3864
 PUC Docket No. 49421
 Exhibit R-RBM-7
 4 of 8

		Red Text = Gorman Edits to CEHE Financials Blue Text = CNP adjustments to MPG-5					
		2019	2020	2021	2022	2023	
55	Total Assets	\$ 10,507.1	\$ 11,508.4	\$ 11,862.2	\$ 12,011.8	\$ 12,412.8	\$ 12,810.8
56	LIABILITIES AND EQUITY						
57	Facility/Intercompany Debt	\$ 1.2	\$ -	\$ -	\$ 38.9	\$ 116.1	\$ 336.4
58	Other Current Liabilities	630.3	655.6	679.8	696.2	715.6	731.4
59	Total Current Liabilities	631.5	655.6	679.8	735.1	831.7	1,067.8
60	Non-Recourse Securitization Debt	1,435.4	1,171.8	995.9	814.7	645.6	497.0
61	Other Long Term Debt (external)	3,577.8	4,353.8	4,693.0	4,910.4	5,243.1	5,472.4
62	Other Long-Term Debt	3,281.5	3,984.7	4,288.0	4,489.0	4,792.2	4,995.6
63	Additional LTD	296.3	369.2	405.0	421.5	450.8	476.9 X
64	Deferred Income Taxes	1,022.9	953.7	892.4	827.1	772.9	729.1
65	Other Liabilities	1,454.4	1,471.5	1,472.1	1,452.1	1,425.5	1,398.8
66	Total Liabilities	8,121.9	8,606.5	8,733.2	8,739.4	8,918.7	9,165.1
67	Common Equity Adjustment	(296.3)	(307.2)	(291.7)	(232.4)	(181.1)	(120.4) X
68	Common Equity	2,681.5	3,209.2	3,420.6	3,504.8	3,675.2	3,766.1
69	Common Equity, Adjusted	2,385.2	2,901.9	3,129.0	3,272.4	3,494.1	3,645.6
70	Total Equity	2,385.2	2,901.9	3,129.0	3,272.4	3,494.1	3,645.6
71	Total Liabilities and Equity	\$ 10,507.1	\$ 11,508.4	\$ 11,862.2	\$ 12,011.8	\$ 12,412.8	\$ 12,810.8
72	Balance check	(0.0)	(0.0)	(0.0)	(0.0)	(0.0)	(0.0)
73	Equity	2,385.2	2,901.9	3,129.0	3,272.4	3,494.1	3,645.6
74	Long-Term Debt	3,577.8	4,353.8	4,693.0	4,910.4	5,243.1	5,472.4

Red Text = Gorman Edits to CEHE Financials Blue Text = CNP adjustments to MPG-5

		2019	2020	2021	2022	2023	
75	Total	5,963.00	7,255.76	7,821.98	8,182.85	8,737.17	9,118.06
76	Debt Ratio	60.00%	60.01%	60.00%	60.01%	60.01%	60.02%
		3,578	4,353	4,693	4,910	5,242	5,471
		296	330	5	(29)	(19)	(26)

Red Text = Gorman Edits to CEHE Financials Blue Text = CNP adjustments to MPG-5

	2019	2020	2021	2022	2023
S&P					
<u>Core Ratios</u>					
FFO / Total Debt	12.7%	12.6%	12.7%	12.9%	13.0%
Total Debt / EBITDA	5.08	5.13	5.15	5.13	5.21
<u>Supplemental Ratios</u>					
OCF / Total Debt	11.9%	12.8%	11.9%	12.0%	11.9%
FOCF / Total Debt	-9.6%	-8.2%	-11.0%	-5.6%	-4.4%
DCF / Total Debt	-3.9%	-9.8%	-15.2%	-8.3%	-8.5%
EBITDA Interest Coverage	4.69	4.66	4.59	4.59	4.72
FFO Interest Coverage	4.03	4.00	4.00	4.04	4.20

Red Text = Gorman Edits to CEHE Financials Blue Text = CNP adjustments to MPG-5

	2019	2020	2021	2022	2023
Moody's (excluding Securitization)					
CFO pre-WC + Interest / Interest	4.21	4.28	4.08	4.03	4.08
Debt / Capitalization	54.3%	55.0%	55.7%	56.6%	57.9%
CFO pre-WC / Debt	13.0%	13.2%	12.5%	12.6%	12.5%
Total Debt / EBITDA	5.15	5.18	5.17	5.14	5.22
CFO pre-WC – Dividends / Debt	12.0%	11.9%	9.4%	10.7%	9.3%
(FFO - Dividends) / Capital Expenditures	54.9%	56.0%	40.4%	59.9%	56.4%
Moody's (including Securitization)					
Funds From Operations Interest Coverage	4.82	4.66	4.60	4.56	4.59
Total Debt / Capital	59.9%	59.6%	59.4%	59.3%	59.8%
Funds From Operations / Total Debt	15.0%	14.0%	13.9%	14.0%	13.8%
Total Debt / EBITDA	4.82	5.13	4.98	4.91	4.98
(FFO - Dividends) / Total Debt	14.2%	12.9%	11.2%	12.3%	10.9%
(FFO - Dividends) / Capital Expenditures	81.9%	73.2%	55.9%	77.2%	71.6%

Red Text = Gorman Edits to CEHE Financials Blue Text = CNP adjustments to MPG-5

	2019	2020	2021	2022	2023
Fitch					
FFO Fixed-Charge Cover (x)	4.18	4.25	4.20	4.17	4.26
Debt as % of Total Capitalization	60.0%	60.0%	60.2%	60.5%	61.4%
FFO / Debt	13.6%	13.8%	13.8%	13.8%	13.7%
Total Adjusted Debt / Operating EBITDAR (x)	4.99	5.04	5.04	5.03	5.12
EBIT Interest Coverage	2.61	2.58	2.54	2.54	2.57
EBITDA Interest Coverage	4.69	4.66	4.61	4.56	4.62
Fitch FFO-adjusted leverage	5.60	5.53	5.53	5.50	5.57
Common Equity as % of Total Capitalization	44.2%	43.7%	42.6%	41.5%	39.8%
Covenant Calculation					
Covenant Debt / Capital	60.0%	60.0%	60.2%	60.5%	61.4%

CenterPoint Energy Houston Electric, LLC

Transmission and Distribution Utility

(For the Year Ended or As of December 31, Dollars in Millions)

	2018	2019	2020	2021	2022	2023
Income Statement						
Total Revenues	\$ 3,004.0	\$ 2,717.4	\$ 2,854.6	\$ 3,002.8	\$ 3,169.9	
Operating and Administrative	1,503.4	1,545.6	1,613.5	1,677.4	1,736.8	
Taxes Other Than Income	252.0	261.8	269.3	277.0	284.5	
Depreciation and Amortization	650.9	566.8	597.1	614.4	617.1	
Operating Income	597.6	343.2	374.7	434.0	531.4	
Interest Income (intercompany)	20.7	16.7	2.2	3.2	0.2	
Other Income	(9.9)	(12.6)	(6.4)	(6.6)	(8.5)	
EBIT	608.3	347.3	370.4	430.6	523.2	
Securitization Interest	39.7	28.0	20.8	13.4	7.6	
Other Interest (external)	163.5	174.1	199.3	223.5	232.5	
Other Interest (intercompany)	-	-	3.7	2.2	4.5	
EBT	405.1	145.3	146.6	191.5	278.6	
Tax Expense	233.0	(55.3)	(63.9)	(52.3)	22.8	
Net Income before Non-Recurring Items	172.1	200.6	210.5	243.8	255.8	
Non-Recurring Items	-	-	-	-	-	
Net Income	\$ 172.1	\$ 200.6	\$ 210.5	\$ 243.8	\$ 255.8	

Credit Metrics

S&P

Funds From Operations / Total Debt	15.3%	10.3%	10.0%	10.6%	11.6%
Total Debt / EBITDA	4.36	6.46	6.59	6.35	5.99
Operating Cash Flow / Total Debt	14.5%	10.2%	9.1%	9.7%	10.8%

CenterPoint Energy Houston Electric, LLC

Transmission and Distribution Utility

(For the Year Ended or As of December 31, Dollars in Millions)

	2018	2019	2020	2021	2022	2023
Cash Flows						
Net Income	\$ 172.1	\$ 200.6	\$ 210.5	\$ 243.8	\$ 255.8	
Non-Recurring Items, net of tax	-	-	-	-	-	-
Net Income before Non-Recurring Items	172.1	200.6	210.5	243.8	255.8	
Depreciation and Amortization	650.9	566.8	597.1	614.4	617.1	
Amortization of Deferred Financing Costs	10.5	10.2	9.9	8.6	6.9	
Deferred Taxes	89.1	(109.7)	(112.7)	(101.6)	(38.0)	
Funds From Operations	922.6	668.0	704.8	765.2	841.8	
Changes in Working Capital	(48.8)	(9.9)	(45.7)	(47.8)	(37.8)	
Operating Cash Flow	873.8	658.1	659.1	717.5	804.0	
Capital Expenditures	(979.1)	(1,024.8)	(1,177.3)	(978.8)	(980.0)	
Other Investing Activities	-	-	-	-	-	
Investing Cash Flow	(979.1)	(1,024.8)	(1,177.3)	(978.8)	(980.0)	
Increase (decrease) in Intercompany Notes Payable	(748.0)	896.5	(95.2)	10.9	244.8	
Increase (decrease) in Securitization Debt	(264.3)	(176.4)	(181.6)	(169.3)	(148.7)	
Increase (decrease) in Other Long Term Debt	700.0	300.0	597.6	400.0	200.0	
Dividends	417.7	(653.3)	197.4	19.8	(120.1)	
Other Financing Activities	-	-	-	-	-	
Financing Cash Flow	105.3	366.8	518.2	261.4	176.0	
Total Cash Flow	\$ -	\$ -	\$ -	\$ (0.0)	\$ 0.0	

CenterPoint Energy Houston Electric, LLC

Transmission and Distribution Utility

(For the Year Ended or As of December 31, Dollars in Millions)

	2018	2019	2020	2021	2022	2023
Balance Sheet						
ASSETS						
Cash/Temporary Investments	\$ (0.2)	\$ 746.7	\$ (0.2)	\$ (0.2)	\$ (0.2)	\$ (0.2)
Current Assets	949.5	998.3	998.1	1,022.6	1,048.4	1,072.2
PP&E, net	8,401.7	8,993.4	9,636.9	10,408.0	10,951.2	11,462.7
Other Assets	1,156.1	928.5	764.5	611.6	469.2	349.3
Total Assets	<u>\$ 10,507.1</u>	<u>\$ 11,666.8</u>	<u>\$ 11,399.4</u>	<u>\$ 12,042.2</u>	<u>\$ 12,468.6</u>	<u>\$ 12,884.0</u>
LIABILITIES AND EQUITY						
Facility/Intercompany Debt	\$ 1.2	\$ -	\$ 149.7	\$ 54.5	\$ 65.4	\$ 310.2
Other Current Liabilities	630.3	655.6	672.9	695.9	715.2	733.5
Total Current Liabilities	<u>631.5</u>	<u>655.6</u>	<u>822.6</u>	<u>750.4</u>	<u>780.6</u>	<u>1,043.7</u>
Non-Recourse Securitization Debt	1,435.4	1,171.8	995.9	814.7	645.6	497.0
Other Long Term Debt (external)	3,281.5	3,984.7	4,288.0	4,889.0	5,292.2	5,495.6
Deferred Income Taxes	1,022.9	1,111.9	1,002.3	889.6	787.9	749.9
Other Liabilities	1,454.4	1,471.5	1,472.1	1,472.1	1,472.1	1,472.1
Total Liabilities	<u>7,825.7</u>	<u>8,395.6</u>	<u>8,580.9</u>	<u>8,815.7</u>	<u>8,978.5</u>	<u>9,258.3</u>
Common Equity	2,681.5	3,271.2	2,818.5	3,226.5	3,490.1	3,625.8
Total Equity	<u>2,681.5</u>	<u>3,271.2</u>	<u>2,818.5</u>	<u>3,226.5</u>	<u>3,490.1</u>	<u>3,625.8</u>
Total Liabilities and Equity	<u>\$ 10,507.1</u>	<u>\$ 11,666.8</u>	<u>\$ 11,399.4</u>	<u>\$ 12,042.2</u>	<u>\$ 12,468.6</u>	<u>\$ 12,884.0</u>
Balance check	(0.0)	(0.0)	(0.0)	(0.0)	(0.0)	(0.0)

CenterPoint Energy Houston Electric, LLC

Transmission and Distribution Utility

(For the Year Ended or As of December 31, Dollars in Millions)

	S&P Methodology				
	2019	2020	2021	2022	2023
DEBT:					
Balance Sheet Debt	5,156.5	5,433.6	5,758.1	6,003.3	6,302.8
Less: Securitization Debt	(1,171.8)	(995.9)	(814.7)	(645.6)	(497.0)
Adjusted Debt (GAAP)	3,984.7	4,437.7	4,943.5	5,357.7	5,805.7
Plus: Pension & Postretirement Underfunded Amount (After Tax)	45.2	42.5	39.9	37.5	35.2
Plus: Asset Retirement Obligations (After Tax)	27.7	27.7	27.7	27.7	27.7
Plus: Interest Accrued	77.3	81.3	92.2	98.8	98.9
Plus: Unamortized Issuance Cost (Excluding Securitization)	15.6	13.7	12.2	10.9	9.9
Adjusted Debt (S&P)	4,150.5	4,602.9	5,115.4	5,532.5	5,977.3
INTEREST EXPENSE:					
Income Statement Interest	203.1	202.0	223.8	239.1	244.6
Less: Securitization Interest (Cash and Non-Cash)	(39.7)	(28.0)	(20.8)	(13.4)	(7.6)
Adjusted Interest Expense (GAAP)	163.5	174.1	203.0	225.7	237.0
Plus: Capitalized Interest	6.1	7.3	8.7	8.2	7.2
Plus: Interest on Pension & Postretirement Underfunded Amounts	2.7	2.6	2.4	2.3	2.1
Plus: Asset Retirement Obligations	1.0	1.0	1.0	1.0	1.0
Adjusted Interest Expense (S&P)	173.3	185.0	215.2	237.2	247.4
EBITDA:					
Unadjusted EBITDA	1,248.5	910.1	971.8	1,048.4	1,148.5
Less: Securitization EBITDA	(303.2)	(203.9)	(202.1)	(182.4)	(156.2)
Adjusted EBITDA	945.3	706.2	769.8	866.0	992.3
Plus: Interest on Pension & Postretirement Underfunded Amounts	5.7	5.4	5.1	4.8	4.5
Plus: Asset Retirement Obligations	1.0	1.0	1.0	1.0	1.0
Adjusted EBITDA	952.1	712.6	775.8	871.8	997.8
FUNDS FROM OPERATIONS:					
Adjusted EBITDA (S&P)	952.1	712.6	775.8	871.8	997.8
Less: Adjusted Interest Expense, net (S&P)	(173.3)	(185.0)	(215.2)	(237.2)	(247.4)
Less: Current Taxes	(144.0)	(54.4)	(48.8)	(49.3)	(60.8)
Plus: Pension & Postretirement Adjustment	1.4	1.3	1.2	1.1	1.1
Plus: Asset Retirement Obligations	0.2	0.2	0.2	0.2	0.2
Adjusted Funds from Operations (S&P)	636.4	474.7	513.3	586.6	690.9
OCF, FOCF & DCF:					
Operating Cash Flow	873.8	658.1	659.1	717.5	804.0
Less: Securitization OCF	(264.3)	(176.4)	(181.6)	(169.3)	(148.7)
Adjusted Operating Cash Flow	609.5	481.6	477.5	548.1	655.3
Plus: Pension & Postretirement Adjustment	(2.5)	(2.3)	(2.2)	(2.1)	(1.9)
Less: Capitalized Interest	(6.1)	(7.3)	(8.7)	(8.2)	(7.2)
Plus: Asset Retirement Obligations	(0.8)	(0.8)	(0.8)	(0.8)	(0.8)
Adjusted Operating Cash Flow (S&P)	600.1	471.2	465.8	537.1	645.3
Less: Capital Expenditures	(979.1)	(1,024.8)	(1,177.3)	(978.8)	(980.0)
Plus: Capitalized Interest	6.1	7.3	8.7	8.2	7.2
Free Operating Cash Flow (S&P)	(372.9)	(546.3)	(702.8)	(433.6)	(327.4)
Less: Dividends	417.7	(653.3)	197.4	19.8	(120.1)
Discretionary Operating Cash Flow (S&P)	44.7	(1,199.6)	(505.4)	(413.8)	(447.5)

CenterPoint Energy Houston Electric, LLC

Transmission and Distribution Utility

(For the Year Ended or As of December 31, Dollars in Millions)

	S&P Methodology				
	2019	2020	2021	2022	2023
<u>Core Ratios</u>					
FFO / Total Debt	15.3%	10.3%	10.0%	10.6%	11.6%
Total Debt / EBITDA	4.36	6.46	6.59	6.35	5.99
<u>Supplemental Ratios</u>					
OCF / Total Debt	14.5%	10.2%	9.1%	9.7%	10.8%
FOCF / Total Debt	-9.0%	-11.9%	-13.7%	-7.8%	-5.5%
DCF / Total Debt	1.1%	-26.1%	-9.9%	-7.5%	-7.5%
EBITDA Interest Coverage	5.49	3.85	3.61	3.67	4.03
FFO Interest Coverage	4.67	3.57	3.39	3.47	3.79