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

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

TEXAS COAST UTILITIES COALITION'S RESPONSES TO CENTERPOINT ENERGY HOUSTON ELECTRIC, LLC's THIRD REQUEST FOR INFORMATION TO TCUC, QUESTION NOS. 3-1 AND 3-6

Texas Coast Utilities Coalition ("TCUC") hereby files its responses to CenterPoint Energy Houston Electric, LLC ("CEHE") Third Set of Requests for Information ("RFIs") to TCUC.

I. Written Responses.

TCUC's written responses to CEHE' Third Set of RFIs are attached and incorporated by reference. Each response is stated on or attached to a separate page on which the request has been restated. TCUC's responses are made in the spirit of cooperation without waiving TCUC's right to contest the admissibility of any of these matters at hearing. Pursuant to 16 Tex. Admin. Code § 22.144(c)(2)(A), each response lists the preparer or person under whose direct supervision the response was prepared and any sponsoring witness. When TCUC provides certain information sought by the request while objecting to the provision of information, they do so without prejudice to their objection in the interests of narrowing discovery disputes pursuant to 16 Tex. Admin. Code § 22.144(d)(5). Pursuant to 16 Tex. Admin. Code § 22.144(c)(2)(F), TCUC stipulates that their responses may be treated by all parties as if they were made under oath.

II. Inspections.

If responsive documents are more than 100 pages but less than eight linear feet in length, the response will indicate that the attachment is VOLUMINOUS and, pursuant to 16 Tex. Admin. Code § 22.144(h)(2), the attachment will be made available for inspection at the offices of Herrera Law & Associates, PLLC, 816 Congress, Suite 950, Austin, Texas, 78701. If a response or the responsive documents are provided pursuant to the protective order in this

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docket, the response will indicate that it or the attachment is either CONFIDENTIAL or HIGHLY SENSITIVE as appropriate under the protective order. Highly sensitive responses will be made available for inspection at the offices of Herrera Law & Associates, PLLC, 816 Congress, Suite 950, Austin, Texas, 78701, unless they form a part of a response that exceeds eight linear feet in length; then they will be available at their usual repository in accordance with the following paragraph. Please call in advance for an appointment to ensure that there is sufficient space to accommodate your inspection.

If responsive documents exceed eight linear feet in length, the response will indicate that the attachment is subject to the FREIGHT CAR DOCTRINE, and, pursuant to 16 Tex. Admin. Code § 22.144(h)(3), the attachment will be available for inspection at the offices of Herrera Law & Associates, PLLC, 816 Congress, Suite 950, Austin, Texas, 78701, unless otherwise indicated. TCUC requests that parties wishing to inspect this material provide at least 48 hours' notice of their intent by contacting the offices of Herrera Law & Associates, PLLC, 816 Congress, Suite 950, Austin, Texas, 78701; telephone number (512) 474-1492; fax number (512) 474-2507. Inspections will be scheduled to accommodate all requests with as little inconvenience to the requesting party and TCUC's operations as possible.

Respectfully submitted,

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ATTORNEYS FOR TEXAS COAST UTILITIES COALITION

CERTIFICATE OF SERVICE

I certify that I have served a copy of ***TCUC's Responses to CEHE's Third Set of Requests for Information to TCUC*** upon all known parties of record by electronic mail in compliance with SOAH Order No. 2 on this the 24th day of June 2019.

Leslie Lindsey

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CEHE RFI 3-1:

Please refer to the Direct Testimony of J. Randall Woolridge. If not provided as part of Dr. Woolridge's workpapers, please produce the documents cited in the following footnotes:

a. 4
b. 5
c. 6
d. 7
e. 8
f. 12
g. 17
h. 18
i. 22
j. 23
k. 24
l. 26
m. 27
n. 28
o. 29
p. 30
q. 31
r. 32
s. 33
t. 34

u. 36

v. 37

w. 42

x. 43

y. 44

z. 47

aa. 48

bb. 49

cc. 50

dd. 51

ee. 52

ff. 53

gg. 54

hh. 55

ii. 56

jj. 57

kk. 58

ll. 59

mm. 60

nn. 62

RESPONSE:

The requested documents were provided in Dr. Woolridge's workpapers.

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PREPARED BY: **J. Randall Woolridge**

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CEHE RFI 3-2:

Please refer to page 4, lines 17-19 of the Direct Testimony of J. Randall Woolridge.

a. Is Dr. Woolridge aware of any prior base rate case in which Commission ordered that short-term debt be included in a utility's regulated capital structure?

b. If the answer to subpart (a) is yes, please provide citations to all such cases, including the docket number and the date of the order in which the Commission ordered that short-term be included in the utility's regulated capital structure.

RESPONSE:

a. No, Dr. Woolridge is not aware of any prior rate base case in Texas in which the Commission ordered that short-term debt be included in a utility's regulated capital structure.

b. N/A.

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CEHE RFI 3-3:

Please refer to page 4, lines 17-19 of the Direct Testimony of J. Randall Woolridge.

a. Does Dr. Woolridge contend that any of the assets contained in CenterPoint Houston's rate base are financed with short-term debt?

b. If the response to subpart (a) is yes, please describe all bases for Mr. Woolridge's contention and provide all documents that support that contention.

RESPONSE:

a. Because capital funds are fungible, whether the capital comes from short-term or long-term debt, or equity or cash flows, is immaterial. One dollar of capital is interchangeable with any other dollar of capital. As Dr. Woolridge notes on page 20 of his testimony, CEHE's financing requirements vary by the day, and the Company had short-term debt outstanding for 225 of the 365 days during the test year 2018. The average daily balance for the year was $52.1 million and a daily maximum of amount of $220 million on February 5th. Furthermore, financial risk is a function of total debt, which includes short-term debt and long-term debt. Fitch, S&P, and Moody's calculate their various financial metrics based on total debt, not just short-term debt. As such, the correct cost of the capital is the overall cost of capital for all the funds employed. This cost rate includes the weighted component costs of the alternative source of capital – short-term and long-term debt and common equity capital.

b. See response to a.

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CEHE RFI 3-4:

Please refer to page 4, lines 17-26 of the Direct Testimony of J. Randall Woolridge.

a. Why is Dr. Woolridge recommending an alternative capital structure?

b. Under what circumstances does Dr. Woolridge believe it would be appropriate for the Commission to adopt the alternative capital structure recommendation in lieu of Dr. Woolridge's primary capital structure recommendation?

c. Why is Dr. Woolridge recommending an alternative ROE?

d. Under what circumstances does Dr. Woolridge believe it would be appropriate for the Commission to adopt the alternative ROE recommendation in lieu of Dr. Woolridge's primary ROE recommendation?

RESPONSE:

a. Dr. Woolridge's recommendation of a 60% debt / 40% equity capital structure is a hypothetical capital structure, just as the capital structure that the Company has proposed. Dr. Woolridge notes that this 60/40 capital structure is consistent with the Commission's capital structures approved for Wind Energy Texas Transmission LLC and Cross Texas Transmission in 2015. Nonetheless, Dr. Woolridge has proposed the alternative capital structure to provide the Commission an option if it decides not to use a hypothetical capital structure and instead use the Company's actual capital structure.

b. Dr. Woolridge believes that if the Commission decides to employ a capital structure that reflects how the Company has financed its utility operations, then he believes that his alternative capital structure would be appropriate.

c. In his testimony, Dr. Woolridge concludes that the current market cost of capital for a low-risk electric delivery company is 8.65%. He highlights a number of factors on pages 49-50 of his testimony as to why capital costs for utilities remain low in today's economic environment. However, in his primary cost of capital, he recognizes that authorized ROEs for electric delivery companies were 9.38% in 2018. Therefore, in conjunction with his 60/40 debt/equity capital structure recommendation, he uses a 9.0% ROE. His alternative ROE recommendation is tied to his alternative capital structure. On pages 19-20 of his testimony, Dr. Woolridge discusses the trade-off between debt and equity financing and the level of financial risk. Consistent with this relationship, in his alternative cost-of-capital recommendation, Dr. Woolridge has proposed the lower 8.65% ROE recommendation because the alternative recommendation has a higher common equity (43.62%) and lower financial risk.

d. Dr, Woolridge believes that if the Commission decides to employ a capital structure that reflects how the Company has financed its utility operations, then he believes that his alternative capital structure and ROE would be appropriate.

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CEHE RFI 3-5:

Please refer to page 20, lines 1-5 of the Direct Testimony of J. Randall Woolridge.

a. Has Dr. Woolridge performed any quantitative analysis to determine what CenterPoint Houston's ratio of Cash Flow from Operations pre-Working Capital to Debt would be under Dr. Woolridge's capital structure recommendation? If so, please provide that analysis.

b. Has Dr. Woolridge performed any quantitative analysis to determine what CenterPoint Houston's ratio of Debt to Earnings Before Interest, Taxes, Depreciation, and Amortization would be under Dr. Woolridge's capital structure recommendation? If so, please provide that analysis.

c. Has Dr. Woolridge performed any quantitative analysis to determine what CenterPoint Houston's ratio of Funds from Operations to Debt would be under Dr. Woolridge's capital structure recommendation? If so, please provide that analysis.

RESPONSE:

a. No. However, as Dr. Woolridge notes in his testimony, the 60% debt / 40% equity capital structure is similar to the capital structure that the Company has maintained over the past three years. On page 2 of Exhibit JRW-3, Dr. Woolridge provides the average quarterly capitalization ratios for CEHE. The data shows that CEHE's common equity ratio has been in the 38% to 45% range over the three-year time period. This is the capitalization the Company has used to maintain its credit ratings and raise capital. It is significant to note that over this time period, CEHE maintained an 'A' S&P credit rating. On page 16 of his testimony, Dr. Woolridge also notes that CEHE was downgraded from 'A' to 'BBB+' in February of 2019. However, this downgrade is unrelated to CEHE and its capitalization. The downgrade is related to the risks associated with CenterPoint Energy's, CEHE's parent, acquisition of Vectren.

b. See response to a.

c. See response to a.

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CEHE RFI 3-6:

Please refer to page 35, lines 12-13 of the Direct Testimony of J. Randall Woolridge.

a. Please describe all bases for Dr. Woolridge's contention that "I do believe that investors are well aware of the bias in analysts' EPS growth-rate forecasts, and therefore stock prices reflect the upward bias."

b. Please produce all documents on which Dr. Woolridge relies for his contention that "I do believe that investors are well aware of the bias in analysts' EPS growth-rate forecasts, and therefore stock prices reflect the upward bias."

RESPONSE:

a. As Dr. Woolridge discusses on pages 34 and 35 of his testimony, numerous studies have demonstrated the analysts' 3-5 year EPS growth rate forecasts are overly optimistic and upwardly biased. This is a well-known concept, as the first such study was published over thirty years ago. Many of the studies that support this observation are listed in footnote no. 23 on page 35 and were provided as part of Dr. Woolridge's work papers. One such study, by the international consulting firm McKinsey & Co., was entitled "Equity Analysts: Still Too Bullish." The authors concluded that after a decade of stricter regulation, analysts' long-term earnings forecasts continue to be excessively optimistic. They made the following observation:[1]

> Alas, a recently completed update of our work only reinforces this view—despite a series of rules and regulations, dating to the last decade, that

[1] Marc H. Goedhart, Rishi Raj, and Abhishek Saxena, "Equity Analysts, Still Too Bullish," *McKinsey on Finance*, pp. 14-17, (Spring 2010) (emphasis added).

were intended to improve the quality of the analysts' long-term earnings forecasts, restore investor confidence in them, and prevent conflicts of interest. For executives, many of whom go to great lengths to satisfy Wall Street's expectations in their financial reporting and long-term strategic moves, this is a cautionary tale worth remembering. This pattern confirms our earlier findings that analysts typically lag behind events in revising their forecasts to reflect new economic conditions. When economic growth accelerates, the size of the forecast error declines; when economic growth slows, it increases. So as economic growth cycles up and down, the actual earnings S&P 500 companies report occasionally coincide with the analysts' forecasts, as they did, for example, in 1988, from 1994 to 1997, and from 2003 to 2006. Moreover, analysts have been persistently overoptimistic for the past 25 years, with estimates ranging from 10 to 12 percent a year, compared with actual earnings growth of 6 percent. Over this time frame, actual earnings growth surpassed forecasts in only two instances, both during the earnings recovery following a recession. On average, analysts' forecasts have been almost 100 percent too high.

This is the same observation made in a *Bloomberg Businessweek* article.[2] The author concluded:

> ***The bottom line:*** *Despite reforms intended to improve Wall Street research, stock analysts seem to be promoting an overly rosy view of profit prospects.*

b. The requested documents, including the two cited above, were provided with Dr. Woolridge's work papers.

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[2] Roben Farzad, "For Analysts, Things Are Always Looking Up," *Bloomberg Businessweek* (June 10, 2010).