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

OFFICE OF PUBLIC UTILITY COUNSEL'S POST-HEARING REPLY BRIEF

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TO THE HONORABLE ADMINISTRATIVE LAW JUDGES:

The Office of Public Utility Counsel ("OPUC"), representing the interests of residential and small commercial consumers in Texas, respectfully submits this post-hearing reply brief. Pursuant to State Office of Administrative Hearings ("SOAH") Order No. 10, OPUC limits this brief to responding to the initial briefs of the other parties. In particular, OPUC responds to arguments presented by CenterPoint Energy Houston Electric, LLC ("CenterPoint Houston" or the "Company"), Texas Industrial Energy Consumers ("TIEC"), and Staff of the Public Utility Commission of Texas ("Commission Staff"). OPUC respectfully refers the Administrative Law Judges ("ALJs") to OPUC's initial brief for OPUC's positions on any issues not addressed in this reply brief and shows the following:[1]

II. RATE BASE [PO Issues 4, 5, 10, 11, 12, 15, 16, 17, 18, 19]

A. Transmission and Distribution Capital Investment [PO Issues 4, 5, 10, 11, 12]

1. Capital Project Prudence

a. Cost overruns due to construction errors

CenterPoint Houston's initial brief groups together OPUC's and Commission Staff's disallowances relating to the construction of the Alexander Island and La Marque Substations.[2] While witnesses for OPUC and Commission Staff each addressed cost overruns for these projects,

[1] The fact that OPUC does not address an issue, whether here in its reply brief, or in its initial brief, should not be interpreted as agreement with any particular position on the issue.

[2] CEHE Initial Brief at 15-18.

the bases for their disallowances differed. OPUC's recommendation is based on the Company's construction errors for the Alexander Island and La Marque Substations.[3] These construction errors led to substantial cost overruns for the substation projects, 104% and 92%, respectively, and thus, OPUC recommended disallowing the portion of the costs that exceeded the initial cost estimates. The disallowance is not based solely on the existence of cost overruns, but rather on the Company's imprudent actions that caused the overruns.

CenterPoint Houston does not dispute that construction errors contributed to the overruns, but instead, contends that the errors were not the only cause.[4] Even assuming that were the case, the Company does not identify an alternative method for calculating the costs that were incurred due to the construction errors. Construction errors are not prudent,[5] and therefore, the costs associated with the errors should not be recovered from customers. If imprudent costs cannot be separated from prudent costs, then the Company has failed to meet its burden of proof to show that all of the project costs it seeks to recover are prudent.

Yet rather than recommending the disallowance of the entire costs for the Alexander Island and La Marque Substations, OPUC proposes to disallow only the portions of the costs that exceeded the initial project cost estimates, even though the construction errors may have actually resulted in costs that are *higher* than OPUC's proposed disallowance. Construction estimates generally include a contingency amount that increases the project cost estimate to cover unexpected costs. It cannot be determined from the evidentiary record whether the substations would have been completed for less than the initial project cost estimates if there had not been construction errors. However, because there is evidence that the construction errors led to the cost overruns, OPUC believes that disallowing the cost overrun amount is a reasonable and balanced approach to approximate the portion of costs that were not prudently incurred by the Company. Accordingly, OPUC recommends that the Company's plant in service be reduced by $1,701,421, which is the amount of the project costs that exceeded the budgeted amount for both substation projects.[6]

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[3] OPUC Initial Brief at 3-4.

[4] CEHE Initial Brief at 17; CEHE Ex. 32 (Narendorf Rebuttal) at 17-18.

[5] *See* OPUC Initial Brief at 4.

[6] OPUC Ex. 5 (Nalepa Direct) at 39.

The Company notes that the disallowances proposed by OPUC witness Mr. Karl Nalepa and Commission Staff witness Mr. Tom Sweatman represent 0.12% and 0.68%, respectively, of the Company's High Voltage Operations capital investments.[7] The Company contends that these "statistics" prove it has a "very near perfect track record in managing its capital projects."[8] However, the intervenors' and Commission Staff's ability to review the prudence of the Company's $6 billion in capital investments incurred over the last nine years is limited by the compressed timeframe of this proceeding, and the errors identified are not an indication of the Company's overall track record. Moreover, the prudence of each project must be considered on its own merits. Therefore, even if the Company's actual error rate and track record for capital projects were known, it would not be relevant to determining the prudence of the costs the Company incurred for any particular project.

b. Foundation replacements

As discussed in OPUC's initial brief, OPUC recommends a total reduction to plant in service of $8,879,219 for the 2015 to 2017 project costs to replace certain concrete foundations due to Alkali-Silica Reaction ("ASR").[9] OPUC supports this disallowance in its initial brief, but addresses additional points made in CenterPoint Houston's initial brief.

CenterPoint Houston states that ASR exists due to the concrete materials rather than the method of installation.[10] However, there are steps that the Company can take during the installation stage to prevent ASR. As the Company acknowledges, ASR can be mitigated, such as by adding fly ash to the concrete mix.[11] The Company states that it took steps to mitigate ASR, but has not explained why its actions from 2015 to 2017 were ineffective. In that timeframe, the record shows that the cost of ASR foundation replacements more than quadrupled, increasing from $0 in 2014 to $1,190,140 in 2015, to $2,965,940 in 2016, and to $4,723,139 in 2017.[12] While

[7] CEHE Initial Brief at 16.

[8] *Id.*

[9] OPUC Initial Brief at 5-6.

[10] CEHE Ex. 32 (Narendorf Rebuttal) at 15.

[11] Tr. at 1180 (Narendorf Cross).

[12] CEHE Ex. 7 (Pryor Direct) at WP RMP-2, 2014 Capital Project List; WP RMP-2, 2015 Capital Project List (p. 8 of 10); WP RMP-2, 2016 Capital Project List (p. 7 of 8); and WP RMP-2, 2017 Capital Project List (p. 8 of 8); *see also* Tr. at 1175-77 (Narendorf Cross).

CenterPoint Houston witness Mr. Martin Narendorf noted that ASR is a growing problem, the Company did not have any ASR-related project costs in 2018,[13] so steady growth of such costs is not inevitable. The Company also did not incur ASR-related costs in 2010 to 2014,[14] so the issue appears to have been controlled until the 2015-to-2017 period. Thus, the Company's contention that "[t]he evidence shows that CEHE made no errors"[15] is incorrect. The Company did not explain why there were increasing costs from 2015 to 2017 or why its mitigation efforts were unsuccessful.

CenterPoint Houston states that it proactively replaced foundations that showed the effects of ASR.[16] However, the issue is not whether corrective action was taken, but rather, whether such action could have been avoided if the Company had been prudent in its selection of concrete materials for the foundations. The Company has failed to show that its selection of concrete materials was prudent, and thus, that the foundation replacements could not have been avoided. The Company has the burden of proof to demonstrate that its requested capital investments are reasonable, necessary, and prudent, and it has failed to meet this burden for the costs of the ASR-related foundation replacements. Therefore, the Company's plant in service should be reduced by $8,879,219 for the 2015 to 2017 ASR-related foundation replacements.

2. Capital Project Accounting/Capitalization Policy Changes

a. Costs that should have been expensed, not capitalized

As discussed in OPUC's initial brief, CenterPoint Houston should have expensed rather than capitalized its routine and corrective project costs, and corporate website redesign project costs. OPUC relies on its initial brief for a discussion of these issues.[17]

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[13] *See* CEHE Ex. 7 (Pryor Direct) at WP RMP-2, 2018 Capital Project List.

[14] *See id.* at WP RMP-2, 2010 – 2014 Capital Project Lists.

[15] CEHE Initial Brief at 15.

[16] *Id.*

[17] OPUC Initial Brief at 7-8 (routine and corrective projects), 8-10 (corporate website redesign).

b. Change in capitalization policy

CenterPoint Houston's initial brief does not address the changes to its capitalization policy since its last rate case. OPUC relies on its initial brief for a discussion of this issue.[18]

F. Other Prepayments

As discussed in OPUC's initial brief, OPUC recommends a disallowance of $5,308,505 for the full amount of CenterPoint Houston's prepayments of other taxes.[19] OPUC's recommendation is based on the Company's response to OPUC RFI No. 05-03, which indicates that these prepayments are not traditional prepayments (such as those that are made on a quarterly basis) and that the Company had no meaningful opportunity to use these funds as working capital.[20] As a result, CenterPoint Houston should not be allowed to earn a return on the 13-month average of the prepayments of other taxes.

G. Regulatory Assets and Liabilities [PO Issues 18, 19, 59]

CenterPoint Houston is seeking to include certain regulatory assets and liabilities in rate base, where they will earn a return, and to recover the amounts using a three-year amortization period.[21] However, for the reasons discussed in OPUC's initial brief, CenterPoint Houston should recover its Hurricane Harvey, Medicare Part D, and Smart Meter Texas ("SMT") regulatory assets through separate riders using a five-year amortization period, rather than through rate base with an earned return.[22] The Company also should not be authorized to recover its requested regulatory asset for Texas gross margin taxes ("TGMT"). Further, the Company should recover its requested retail electric provider ("REP") bad debt costs as an operations and maintenance ("O&M") expense, rather than as a regulatory asset. OPUC supported these recommendations in its initial brief, but responds to additional arguments included in the Company's initial brief.

CenterPoint Houston states that OPUC witness Ms. June Dively's recommendation is one-sided because it places regulatory assets, but not regulatory liabilities, into riders. The Company's

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[18] OPUC Initial Brief at 10-12.

[19] OPUC Initial Brief at 12-14.

[20] OPUC Ex. 9 (CEHE Response to OPUC RFI No. 05-03).

[21] CEHE Initial Brief at 30.

[22] OPUC Initial Brief at 14-20.

criticism is unwarranted. As stated in OPUC's initial brief, OPUC is not opposed to treating regulatory assets and liabilities the same, so long as the amortization period is five years, with the exception of the refund provided for unprotected excess deferred income taxes ("Rider UEDIT"), which should be returned to customers more quickly.[23]

It is CenterPoint Houston's approach that is, in fact, one-sided because it places all of the risk of over-recovering the assets on its customers. Placing the regulatory assets in rate base using a three-year amortization period is likely to result in over-recovery because the Company is not required to file another rate case for four years.[24] The Company does not bear a corresponding risk of under-recovery if it requests a rate change sooner, because it can seek to recover any remaining unamortized amount at that time. The Company states that a three-year amortization period is consistent with the treatment in its last rate case in Docket No. 38339,[25] but that case illustrates the risk of including the assets in rate base with such a short amortization period. As shown in OPUC's initial brief, the Company actually recovered more than double the amount of its regulatory asset for expedited switching because the rates set in its last rate case were in effect for far longer than three years.[26] Thus, the use of a three-year amortization period unreasonably places all of the risk on the Company's customers.

The Company's approach is also one-sided because it considers intergenerational equity but does not balance that interest with a consideration of the impact on customer rates. The requested regulatory assets are sizable, and thus, it is important to use an appropriate amortization period to moderate how much is recovered from customers each year. A five-year amortization period has been used to recover similar assets,[27] and provides a reasonable balance of these interests.[28] The Company also seeks to recover a return on its regulatory assets from its customers. However, the Company has already benefited by being able to book the regulatory assets and avoid

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[23] *Id.* at 19.

[24] 16 TAC § 25.247(b)(1).

[25] CEHE Initial Brief at 30 (citing *Application of CenterPoint Electric Delivery Company, LLC for Authority to Change Rates*, Docket No. 38339, Order on Rehearing at Finding of Fact ("FOF") No. 159A (June 23, 2011)).

[26] OPUC Initial Brief at 16-17.

[27] *See id.* at 21 (Hurricane Harvey restoration costs), 31 (SMT expenses).

[28] OPUC Ex. 1 (Dively Direct) at 12.

an impact on its earnings per share. Furthermore, the assets contain deferred O&M expenses, which typically are not eligible to earn a return.

In contrast, OPUC's recommendation to use riders to recover the assets is more balanced and equitable because it ensures that the Company recovers the full amount of its regulatory assets, but no more and no less. Using a rider removes the risk of over-recovery that the Company's proposal would place on customers, without adding any risk for the Company. In addition, OPUC's use of a five-year amortization period balances the need for intergenerational equity with moderating the impact on customer rates. Accordingly, OPUC's proposed approach is more reasonable and should be adopted in this case.

OPUC responds to the Company's arguments regarding the specific regulatory assets in the subsections below.

2. Hurricane Harvey

a. Deferred Storm Restoration Costs[29]

CenterPoint Houston's initial brief confirms that it is appropriate to remove $96,696 and any associated carrying costs from the Hurricane Harvey regulatory asset, and thus, this reduction is undisputed.[30] However, as discussed in OPUC's initial brief, the regulatory asset should be further reduced based on the results of the Company's internal audit for Hurricane Harvey expenses.[31] The Company contends that OPUC witness Mr. Nalepa's proposed disallowance was based on a "misrepresentation" of the results of the audit.[32] However, as the Company acknowledges in its initial brief, the audit "identified some opportunities for improvement in documentation and the control process."[33] Mr. Nalepa's recommended disallowances are based on the specific documentation and control process issues raised in the audit. The Company bears the burden of proof to demonstrate that its requested storm restoration costs are reasonable and necessary. As discussed in OPUC's initial brief, the Company has failed to meet this burden for

[29] For consistency with Company's initial brief, OPUC addresses the O&M costs included in the Hurricane Harvey regulatory asset in this section, rather than Section IV.F. below.

[30] CEHE Initial Brief at 33.

[31] OPUC Initial Brief at 58-60.

[32] CEHE Initial Brief at 33.

[33] *Id.*

the items identified in the audit, and the Hurricane Harvey regulatory asset should be further reduced base on the audit findings.

b. Carrying Costs

As discussed in OPUC's initial brief, the Company's Hurricane Harvey carrying costs should be addressed in a separate compliance docket.[34] This approach was used to address Hurricane Harvey carrying costs in the settlement of Texas-New Mexico Power Company's ("TNMP") recent rate case in Docket No. 48401.[35] However, if carrying costs are addressed in this proceeding, the amount should be corrected to calculate the carrying costs using an annual "simple interest" formula, rather than a monthly compound interest formula.[36]

CenterPoint Houston disagrees with making this correction to the calculation.[37] The Company contends that the monthly compounding method reflects its "actual carrying costs," but the evidentiary record demonstrates that this statement is incorrect. The Company admitted that it had not previously booked the carrying costs;[38] thus, there are not actual carrying costs on its books. Further, the *actual* amount of carrying costs that is recoverable under the Public Utility Regulatory Act ("PURA") and the Commission's rules is yet to be determined and is at issue in this proceeding. In fact, CenterPoint Houston witness Ms. Kristie Colvin noted that under generally accepted accounting principles ("GAAP"), the Company does not record carrying costs until after it receives a Commission order.[39] Thus, the amount of carrying costs that CenterPoint Houston has requested cannot be considered its *actual* carrying costs.

The Company also states that a monthly compounding method is "consistent with Commission practice," but the Company's only support for this statement is a citation to TNMP's settled rate case.[40] Even if a non-precedential settlement agreement can indicate prior Commission practice, the TNMP settlement agreement does not support the Company's carrying cost

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[34] OPUC Initial Brief at 22.

[35] *Id.* (citing *Application of Texas-New Mexico Power Company to Change Rates*, Docket No. 48401, Order at FOF No. 64 (Dec. 20, 2018)).

[36] OPUC Initial Brief at 23.

[37] CEHE Initial Brief at 36.

[38] Tr. at 1286-89 (Colvin Cross).

[39] *Id.*

[40] CEHE Initial Brief at 36.

calculation. As noted above, the final amount of carrying costs that TNMP was authorized to recover was determined in a separate compliance docket.[41] As part of that separate proceeding, TNMP agreed to reduce its requested carrying costs.[42] While the basis for this disallowance is not specified in the settlement agreement, it shows that the Company did not recover the full amount of carrying costs that it requested using a monthly compound formula. Thus, the TNMP settlement agreement cannot be relied on to support using a monthly compound formula, and the Company has not provided any other support for its contention that its calculation is consistent with Commission precedent.

The Company also states that its requested amount of carrying costs is supported by Commission Staff.[43] However, Commission Staff witness Mr. Jorge Ordonez did not address CenterPoint Houston's use of a monthly compound interest formula, so it is not clear whether he considered this aspect of the Company's calculation.[44] Further, Commission Staff's initial brief does not cite to any support for using a monthly compound interest formula.[45] As a result, the Company's contention that Commission Staff supports its calculation should not be given any weight.

3. Medicare Part D

CenterPoint Houston argues that it should earn a return on its Medicare Part D regulatory asset because it pre-funded the regulatory asset over multiple years and has yet to recover the amount.[46] However, a utility is not guaranteed an opportunity to earn a return on all of its regulatory assets.[47] When the Commission authorized the Company to accrue a regulatory asset for Medicare Part D in its last rate case, the Commission stated that the Company could book "the difference between what its rates assume the Medicare Part D subsidy tax expense will be and

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[41] *Compliance Filing of Texas New Mexico Power Company in Accordance with the Final Order in Docket No. 48401 Regarding Hurricane Harvey Rider*, Docket No. 49122, Order at FOFs 5 & 11 (June 27, 2019).

[42] OPUC Ex. 8 at 19, line 22 (showing a "Settlement Adjustment" reducing the amount of interest on TNMP's Hurricane Harvey carrying costs by $34,000); *see also* Tr. at 1300-02 (Colvin Cross) (June 28, 2019).

[43] CEHE Initial Brief at 36.

[44] *See* Staff Ex. 3A (Ordonez Direct) at 39.

[45] Commission Staff Initial Brief at 18, 49.

[46] CEHE Initial Brief at 43.

[47] OPUC Ex. 1 (Dively Direct) at 10-11.

what CenterPoint Houston is required to pay."[48] The Commission's order was silent as to how the Company should recover the Medicare Part D regulatory asset. Further, the costs included within the regulatory asset are expenses, and expenses are not typically eligible to earn a return.[49] Finally, while the Company states that the regulatory asset accrued over multiple years, the length of time is a function of the Company's choice not to file a rate case sooner. Given these factors, the Company should not earn a return on its Medicare Part D regulatory asset.

4. Texas Margin Tax

CenterPoint Houston contends that intervenors and Commission Staff "misunderstand" its request for a regulatory asset for Texas gross margin taxes ("TGMT").[50] However, CenterPoint Houston witness Ms. Colvin specifically noted in her rebuttal testimony that OPUC witness Ms. Dively understood the Company's request.[51] Further, the intervenors' and Commission Staff's initial briefs explain why the Company's proposed TGMT regulatory asset should not be recovered.[52] As discussed in OPUC's initial brief, the Company has not received approval to record a regulatory asset for its TGMT expense.[53] While CenterPoint Houston cites to Docket No. 29526 as authority, the Commission's order in that case did not authorize the Company's current TGMT regulatory asset.[54] Because the Company did not have authority to book the TGMT as a regulatory asset, it is not recoverable. Despite the Company's assertions to the contrary,[55] its request is essentially a "true up" of the historical accrued amount for TGMT and the historical actual amount paid for TGMT, and therefore, recovery of this true-up amount would be retroactive ratemaking, which is strictly prohibited.

The Company's current proposal to change its accounting method for TGMT does not change this result. The Company's current rates already include an annual expense for TGMT. If

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[48] Docket No. 38339 Order on Rehearing at 159A.

[49] *See* 16 TAC § 25.231(c) (allowing a utility a reasonable opportunity to earn a reasonable rate of return on its *invested capital*).

[50] CEHE Initial Brief at 45-47.

[51] CEHE Ex. 35 (Colvin Rebuttal) at 30.

[52] *See* OPUC Initial Brief at 25-30; GCCC Initial Brief at 17-19; Commission Staff Initial Brief at 19-21.

[53] OPUC Initial Brief at 26-27.

[54] *Id.*

[55] CEHE Initial Brief at 46.

the Company is authorized to recover an additional year of TGMT expense through a regulatory asset, it would result in recovering the same expense twice. Thus, ratepayers would be harmed if the Company recovers the TGMT regulatory asset. The intervenor and Commission Staff witnesses understand that this is the effect of the Company's proposal, and therefore, appropriately recommend the denial of the TGMT regulatory asset.

5. Smart Meter Texas ("SMT")

OPUC relies on its initial brief for a discussion of CenterPoint Houston's request for an SMT regulatory asset.[56] The Company's arguments related to its ongoing SMT expenses are addressed in Section IV.I. below.

6. REP Bad Debt

CenterPoint Houston's initial brief incorrectly asserts that OPUC agrees that the Company is following Section 25.107(f)(3)(B) of the Commission's rules.[57] OPUC agrees that the rule authorizes the creation of a regulatory asset for REP bad debt expenses, but does not agree that the Company is following the rule. As discussed in OPUC's initial brief, the portion of CenterPoint Houston's regulatory asset for REP bad debt that is derived from the credit approved in Docket No. 38339 does not qualify for recovery as a regulatory asset. The rule contemplates recovery of a bad debt *expense*, but a credit is not an expense. This conclusion is further supported by the plain language of the rule, which only permits a transmission and distribution utility ("TDU") to create a regulatory asset for bad debt *expenses*, "net of collateral posted…and bad debt already included in its rates"[58] In other words, the regulatory asset may only contain any expense that remains after netting out any bad debt included in rates. The Company does not cite to any authority for its assertion that the rule allows the recovery of a credit for bad debt so long as the credit was included in the Company's rates. Accordingly, for the reasons stated here and in OPUC's initial brief, the Company should not be allowed to recover a REP bad debt regulatory asset, but instead, should be allowed to recover REP bad debt as an expense in the amount stated in OPUC's initial brief.

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[56] OPUC Initial Brief at 30-31.

[57] *See* CEHE Initial Brief at 48.

[58] 16 TAC § 25.107(f)(3)(B).

III. RATE OF RETURN [PO Issues 4, 5, 7, 8, 9]

A. Return on Equity [PO Issue 8]

In its initial brief, CenterPoint Houston seeks approval of its witness Mr. Robert Hevert's recommended return on equity ("ROE") of 10.4%, while asserting that the ROE recommendations of the intervenors and Commission Staff are unreasonably low.[59] In establishing their recommended ROEs, OPUC, Texas Coast Utilities Coalition ("TCUC"), TIEC, and Commission Staff appropriately considered the current low interest rate environment, the effects of the Tax Cuts and Jobs Act of 2017 ("TCJA"), and the lower risk that the Company experiences as a TDU with the availability of several rate recovery mechanisms like the transmission cost of service ("TCOS") and distribution cost recovery factor ("DCRF"). As a result, OPUC, TCUC, TIEC, and Commission Staff each have ROE recommendations that fall within a relatively narrow range of 9.0% to 9.45%. In contrast, CenterPoint Houston witness Mr. Hevert's proposed ROE of 10.4% is unreasonably high because it is based on excessive and unsustainable growth rate assumptions.

OPUC first addresses the Company's allegation that OPUC witness Ms. Anjuli Winker incorrectly assumed that the Federal Open Market Committee ("FOMC") would put a hold on interest rate increases over the next few years. However, the Company's statement that there is "no indication that the FOMC...has any such plan"[60] is simply incorrect. As discussed in Ms. Winker's testimony, the FOMC issued a statement on May 1, 2019 announcing its decision to maintain the target range for the federal funds rate at 2-1/4 to 2-1/2%.[61] Moreover, the FOMC recently indicated that it expects to *decrease* the federal funds rate next year. An FOMC press release issued on June 19, 2019 shows that interest rates will remain at 2.4% for the rest of 2019, decrease to 2.1% in 2020, and finally increase back to 2.4% in 2021.[62] Thus, the evidentiary record supports Ms. Winker's consideration of the current low interest rate environment in her ROE

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[59] CEHE Initial Brief at 52-60.

[60] *Id.* at 56.

[61] *Id.*

[62] TIEC Ex. 21.

analysis. Other intervenor and Commission Staff witnesses also appropriately considered this factor as part of their analyses.[63]

With respect to the ROE recommendations, the Company contends that intervenor and Commission Staff witnesses wrongly insist that their model results are reasonable because the models and inputs to the models are reasonable.[64] CenterPoint Houston states that the *Hope Natural Gas* case "teaches that it is the result reached, not the method employed, that is evaluated for reasonableness."[65] However, the models relied on by the intervenors and Commission Staff are well-established and commonly used in Commission proceedings to determine ROEs for electric utilities. In fact, OPUC witness Ms. Winker and CenterPoint Houston witness Mr. Hevert used the same models for their ROE analyses—the constant-growth Discounted Cash Flow ("DCF") model, the Bond Yield Plus Risk Premium model, and the Capital Asset Pricing Model ("CAPM"). The ROE ranges obtained from running these well-established and commonly used models with reasonable inputs should not be discarded simply because the Company does not like the resulting ROE ranges.

Despite using the same models, the OPUC and CenterPoint Houston witnesses that provided testimony on cost of capital reached divergent results. The primary difference lies in the witnesses' inputs to the models. For the DCF model, CenterPoint Houston criticizes OPUC witness Ms. Winker for relying on a sustainable retained earnings growth rate (also referred to as the "BR" growth rate),[66] but this criticism is unwarranted. The Commission has previously adopted an ROE for a TDU that incorporated results from a DCF model using sustainable retained earnings growth.[67] Moreover, Ms. Winker did not rely solely on the BR growth rate for her recommended growth rate range of 3.43% to 6.47%.[68] Ms. Winker also considered historical and projected dividend, book value, and earnings growth for a more balanced approach to her DCF

[63] TCUC Ex. 1 (Woolridge Direct) at 11-17; TIEC Ex. 5 (Gorman Direct) at 16-20; Staff Ex. 3A (Ordonez Direct) at 29.

[64] CEHE Initial Brief at 55.

[65] *Id.* (citing *Federal Power Comm'n v. Hope Natural Gas Co.*, 320 U.S. 591, 603 (1944)).

[66] *Id.* at 56.

[67] *Application of AEP Texas Central Company for Authority to Change Rates*, Docket No. 33309, Order on Rehearing at 26 and FOF No. 55 (Mar. 4, 2008); *see also* Docket No. 33309, Proposal for Decision ("PFD") at 53.

[68] OPUC Ex. 3 (Winker Direct) at 30.

analysis.[69] In contrast, Mr. Hevert relied solely on investment analyst earnings growth projections, which fails to take into account that investors consider multiple growth rate indicators like the indicators used by Ms. Winker in her DCF analysis.[70] Because individual investors have different expectations of growth, it is important to use a range of indicators to estimate growth. Mr. Hevert's sole reliance on one growth rate indicator in his DCF model limits the reliability of his results.

The Company also criticizes Ms. Winker's bond yield plus risk premium analysis for using a shorter data set of 18 years, rather than Mr. Hevert's 39 years.[71] OPUC believes the shorter time period is appropriate because it effectively captures the trend in authorized ROEs while remaining long enough to encompass the last two recessions and the last two periods of economic growth.[72] In addition, monetary policy changes over time, and Ms. Winker's shorter time period is more reflective of current monetary policy. Nevertheless, the time period used to calculate the risk premium does not result in a significant difference. OPUC's and the Company's calculated risk premiums were 4.64% and 4.66%, respectively. Thus, the time period is not the primary driver of the difference between OPUC's and the Company's bond yield plus risk premium results.

Instead, the primary difference in the bond yield plus risk premium ranges calculated by OPUC (8.98% to 9.04%) and CenterPoint Houston (9.93% to 10.17%) is due to Mr. Hevert's use of an adder to inflate his results. Mr. Hevert concluded that because interest rates are at historical low levels, the actual observed risk premiums from his study needed to be increased based on his regression analysis.[73] However, as discussed in Ms. Winker's testimony, this adjustment is unnecessary because of the 39-year time period that Mr. Hevert used to determine his risk premium. The 39-year time period includes various periods of very high, medium, and very low interest rates, and therefore, already incorporates the inverse relationship between interest rates and risk premiums that Mr. Hevert's adder is intended to capture.[74] As a result, an adder is

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[69] *Id.* at 29-31.

[70] *Id.* at 29.

[71] CEHE Initial Brief at 57.

[72] OPUC Ex. 3 (Winker Direct) at 34.

[73] *Id.* at 36.

[74] *Id.*

unnecessary. Without the adder, Mr. Hevert's bond yield plus risk premium range is 7.69% to 8.71%, which falls below the low end of Ms. Winker's range of 8.98% to 9.04%.[75]

The Company also states that Ms. Winker's CAPM result of 8.2% is "too low."[76] However, as discussed in her testimony, Ms. Winker did not incorporate her CAPM results into her recommended ROE range because there is not sufficient Commission precedent to support a finding that an ROE of 8.20% will allow CenterPoint Houston a reasonable opportunity to earn a reasonable return on its investment.[77] Instead, Ms. Winker used her CAPM analysis as a qualitative check on the results of the other two models that she used in her ROE analysis.[78] The CAPM results show that a reduced ROE for CenterPoint Houston is appropriate given the continued low interest rate environment.[79]

Accordingly, the Company's criticisms of Ms. Winker's ROE recommendation are without merit and should be rejected. Ms. Winker's analyses appropriately considered the current low interest rate environment and used well-established models with reasonable inputs. Therefore, Ms. Winker's recommended ROE of 9.15% should be adopted in this case.

C. Capital Structure [PO Issue 7]

The Company contends that OPUC witness Ms. Winker's recommended capital structure is based on a conclusory statement that CenterPoint Houston will continue to be able to attract financial capital on reasonable terms since it has been able to do so after the enactment of the TCJA.[80] However, this statement is just one basis for Ms. Winker's conclusion. Ms. Winker's recommended capital structure of 54.5% debt and 45.5% equity reflects the Company's current book values and differs only slightly from the Company's current Commission-approved capital structure.[81] As discussed in Ms. Winker's testimony, the Company's current capital structure has

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[75] *Id.* at 35.

[76] CEHE Initial Brief at 57.

[77] OPUC Ex. 3 (Winker Direct) at 39.

[78] *Id.* at 39-40.

[79] *Id.*

[80] CEHE Initial Brief at 64.

[81] OPUC Ex. 3 (Winker Direct) at 43.

supported the issuance of long-term debt totaling approximately $2.4 billion since 2012.[82] While the TCJA has had a temporary impact on electric utility cash flows, Ms. Winker noted that credit rating agencies have indicated that the TCJA is a short-term negative, but a longer-term positive for electric utilities.[83] Despite the passage of the TCJA, the Company was able to issue $400 million in long-term debt at a 3.95% interest rate after the TCJA became effective.[84] Given these circumstances, the Company has failed to demonstrate that moving to a 50% debt and 50% equity capital structure is warranted. Furthermore, as discussed by other intervenor and Commission Staff witnesses who recommend a 60% debt and 40% equity capital structure,[85] there is also support for using a capital structure with a higher concentration of debt.

IV. OPERATING AND MAINTENANCE EXPENSES [PO Issues 4, 5, 21, 22, 25, 26, 28, 29, 33, 35, 36, 38, 39, 54, 55]

B. Labor Expenses

1. Incentive Compensation

OPUC's recommended disallowances for CenterPoint Houston's short-term and long-term incentive compensation plans ("STI Plan" and "LTI Plan," respectively) are addressed in OPUC's initial brief, but OPUC responds here to additional points raised in the Company's initial brief.

a. Short-Term Incentive Compensation

In its initial brief, CenterPoint Houston discusses House Bill ("HB") 1767, which creates a presumption for natural gas utilities that: "When establishing a gas utility's rates, the regulatory authority shall presume that employee compensation and benefits expenses are reasonable and necessary if the expenses are consistent with market compensation studies issued not earlier than three years before the initiation of the proceeding to establish the rates."[86] The Company contends

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[82] *Id.* at 42.

[83] *Id.* at 17-18, 43.

[84] *Id.* at 42-43.

[85] TCUC Ex. 1 (Woolridge Direct) at 17-21; TIEC Ex. 5 (Gorman Direct) at 27-38; Staff Ex. 3A (Ordonez Direct) at 30-37.

[86] TIEC Ex. 36 (HB 1767).

that newly enacted HB 1767 is a "triggering event" that gives the Commission the opportunity to evaluate and potentially reconsider the way it addresses incentive compensation.[87]

However, the Company's reliance on HB 1767 is misplaced for several reasons. First, as the Company acknowledges, the legislation applies only to ratemaking proceedings for gas utilities, not electric utilities.[88] As the Texas Supreme Court has stated, "A statute's silence can be significant. When the Legislature includes a right or remedy in one part of a code but omits it in another, that may be precisely what the Legislature intended."[89] This insight is particularly relevant here because during the same legislative session that the Legislature adopted HB 1767, it also considered, but did not adopt, two bills that would have created a similar presumption for electric utilities.[90] Thus, if the Legislature had intended to create a presumption for electric utilities, it could have done so, but did not.

Moreover, given its recent enactment, the regulatory authority charged with interpreting and applying HB 1767 (which is the Texas Railroad Commission ("RRC"), not the Public Utility Commission of Texas) has not had an opportunity to implement the legislation. CenterPoint Houston appears to assume that the existence of the presumption of reasonableness necessarily leads to the conclusion that the costs of the Company's incentive compensation program are reasonable and recoverable. However, a presumption is merely a procedural device relating to the burden of proof for establishing a particular fact. Specifically, "[a] legal presumption is a rule of law, statutory or judicial, by which the finding of a basic fact gives rise to the existence of the presumed fact, until the presumption is rebutted."[91] If this were a gas rate case (which it is not), the Company could assert that the presumption applies, but even so, the presumption is rebuttable. While the Company states that there is overlap between the employees who serve its electric utility and CenterPoint Energy, Inc.'s ("CNP") gas utility divisions,[92] the RRC has not considered this incentive compensation issue under the new law.

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[87] CEHE Initial Brief at 78.

[88] *Id.* at 79.

[89] *PPG Indus., Inc. v. JMB/Houston Centers Partners Ltd. P'ship*, 146 S.W.3d 79, 84 (Tex. 2004).

[90] TIEC Ex. 37 (HB 1766); TIEC Ex. 38 (HB 1768).

[91] *Hunter v. Palmer*, 988 S.W.2d 471, 473 (Tex. App.—Houston [1st Dist.] 1999, no pet.).

[92] CEHE Initial Brief at 79.

Further, a presumption of reasonableness does not necessarily lead to recoverability of the costs. Under the Commission's rules, allowable expenses include only those expenses that are "reasonable and necessary to provide service to the public."[93] While it may be reasonable for a utility to make financially based incentive compensation available to its employees, the Commission has consistently concluded that such compensation is not recoverable from ratepayers because it is not reasonable and necessary to provide service to the public. For instance, as the Commission concluded in a prior Entergy Texas, Inc. ("ETI") rate case, "[i]ncentives to achieve operational measures are necessary and reasonable to provide utility services but those to achieve financial measures are not."[94] As discussed in OPUC's initial brief, OPUC's recommended disallowances are based on this long-standing Commission precedent, which is not impacted by the presumption of reasonableness for gas utilities in HB 1767.

This same concept applies to CenterPoint Houston's argument that its STI costs for union employees are presumed reasonable under PURA § 14.006,[95] which states that:

> The commission may not interfere with employee wages and benefits, working conditions, or other terms or conditions of employment that are the product of a collective bargaining agreement recognized under federal law. An employee wage rate or benefit that is the product of the collective bargaining is presumed to be reasonable.

This proceeding is not addressing the reasonableness of an employee wage rate or benefit that is the product of a collective bargaining agreement. Instead, the issue is whether the cost of such wages or benefits are recoverable from ratepayers. PURA § 14.006 only creates a presumption of reasonableness. Even assuming the presumption applies to a portion of the Company's STI costs, it is not a guarantee that the Company can recover the costs in rates. As discussed above, such a presumption does not affect the Commission's precedent that financially based incentive compensation is not an allowable expense because it is not "reasonable and necessary to provide service to the public."

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[93] 16 TAC § 25.231(b).

[94] *Application of Entergy Texas, Inc. for Authority to Change Rates, Reconcile Fuel Costs, and Obtain Deferred Accounting Treatment*, Docket No. 39896, Order on Rehearing at FOF 130 (Nov. 1, 2012).

[95] CEHE Initial Brief at 83.

Despite the Commission's long line of decisions prohibiting recovery of financially based incentive compensation, CenterPoint Houston contends that the Commission should consider whether to apply its long-standing precedent given the facts of this case.[96] In the prior cases, the Commission has determined that *legally* financially based incentive compensation is not recoverable. Thus, the only *factual* issue in this case is whether the Company's incentive compensation programs are based on achieving financial measures or operational measures. In making this determination, the Company is incorrect that intervenors "pit the interests of customers and shareholders against one another" and have advanced an "either/or" issue for customers and shareholders.[97] While a particular metric may have incidental benefits for customers, the Commission considers whether the metric more immediately and predominantly benefits customers or shareholders.[98] The Company admits that its core operating income and earnings per share metrics are financial goals, and for the reasons discussed in OPUC's initial brief, the Company's metric for O&M expenditures is also a financial goal.[99] Thus, based on the Commission's long-standing precedent, the costs for these incentive compensation programs are not recoverable from ratepayers.

CenterPoint Houston also takes issue with disallowances proposed by intervenor and Commission Staff witnesses for a portion of the Company's operational metrics that are tied to financially based funding triggers.[100] The Commission's precedent again is clear that such a disallowance is appropriate when the funding of the operational metrics is tied to a financially based trigger.[101] CenterPoint Houston's STI plan, including the portion related to operational metrics, is only funded if the Company achieves a specific overall core operating income. As stated above, the Company acknowledges that core operating income is a financial metric. Therefore, the funding of the STI plan is dependent on a financial trigger. As a result, the proposed

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[96] *Id.* at 83-84.

[97] *Id.* at 80.

[98] *See, e.g.*, Docket No. 39896, Order on Rehearing at FOF 129.

[99] OPUC Initial Brief at 48-50.

[100] CEHE Initial Brief at 87-88.

[101] *See Application of Southwestern Electric Power Company for Authority to Change Rates*, Docket No. 46449, Order on Rehearing at FOF Nos. 194-98 (Mar. 19, 2018); *Application of Southwestern Public Service Company for Authority to Change Rates*, Docket No. 43695, Order on Rehearing at 5-6 & FOF Nos. 83A-85A (Feb. 23, 2016).

disallowances to remove the impact of the financial trigger are appropriate based on long-standing Commission precedent and should be adopted in this case.

b. Long-Term Incentive Compensation

As discussed above regarding STI compensation, the Commission's long-standing precedent is clear that financially based incentive compensation is not recoverable. As to its LTI plan, the Company contends that the portion of the LTI plan related to restricted stock units ("RSUs") is not financially based, but instead is "time-based."[102] However, the factual issue that must be decided in this case is whether the incentive compensation is based on achieving financial measures or operational measures. As discussed in OPUC's initial brief, the evidence in this case indicates that the RSUs are at least partly based on achieving financial measures.[103] In addition, the Company has not demonstrated that the RSUs are of more immediate and predominant benefit to ratepayers rather than shareholders.[104] As a result, the Company has failed to meet its burden of proof to show that the costs of the LTI plan are "reasonable and necessary to provide service to the public,"[105] and therefore, the costs of the LTI plan should be disallowed.

D. Affiliate Expenses [PO Issue 35, 36]

1. Vectren Issues

OPUC relies on its initial brief for a discussion of this issue.[106]

2. Compensation for Use of Capital

OPUC relies on its initial brief for a discussion of this issue.[107]

F. Hurricane Harvey Restoration Costs [PO Issues 54, 55]

Please see Section II.G.2. for a discussion of the Hurricane Harvey restoration costs included in the Company's proposed Hurricane Harvey regulatory asset.

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[102] CEHE Initial Brief at 88-90.

[103] OPUC Initial Brief at 51-52.

[104] *See* Docket No. 39896, Order on Rehearing at FOF 129.

[105] *See* 16 TAC § 25.231(b).

[106] OPUC Initial Brief at 53-55.

[107] *Id.* at 55-58.

G. Self-Insurance Reserve [PO Issues 16, 33]

OPUC relies on its initial brief for a discussion of this issue.[108]

H. Vegetation Management

CenterPoint Houston contends that OPUC witness Mr. Nalepa's recommendation to normalize the Company's test-year vegetation management expenses results in understating the costs that the Company must incur to support its vegetation management program.[109] However, as discussed in OPUC's initial brief, the Company's test-year level of vegetation management expenses appears to be unusually high. In such circumstances, normalization of the costs is common practice and reasonable.

The Company lists several factors that it contends explain the increased vegetation management costs, but each of these factors assume a steady increase of the costs over time.[110] However, a review of the actual vegetation management expenses incurred each year indicate that the Company's test-year level of vegetation management expenses is an outlier, rather than the product of a year-over-year increase in costs. From 2011 to 2017, the amount for vegetation management expenses remained under $30 million, fluctuating up and down between $22.94 million and $29.45 million. In contrast, in 2018, the Company incurred $35.02 million in vegetation management expenses. Therefore, including this amount in rates would likely *overstate* the vegetation management expenses that the Company will incur in the future and would be unreasonable. In contrast, Mr. Nalepa's proposal to normalize vegetation management expenses using a three-year average for 2015 to 2017, which results in $28.16 million for vegetation management expenses, is reasonable.

The Company's initial brief contends that using a three-year average is understated and unrepresentative, "especially in light of the disruption caused to the activities by Hurricane Harvey in 2017." However, this statement appears to be an acknowledgement that the 2018 test-year vegetation management expenses are inflated due to "catch up" work from Hurricane Harvey in 2017. Any catch-up work for this one-time event does not justify a permanent increase in annual

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[108] OPUC Initial Brief at 61-62.

[109] CEHE Initial Brief at 111.

[110] *Id.* at 110-11.

vegetation management expense.[111] The likelihood that the 2018 test year includes such catch-up work is another indication that it is not representative of the Company's ongoing level of vegetation management expense and that the test-year level should be normalized to more appropriately reflect these costs.

I. Smart Meter Texas Expense

CenterPoint Houston contends that its test-year level of SMT expense must be adjusted because the SMT expenses it incurred for the 2018 test year were based on a previous contract.[112] While it is uncontested that the Company has entered into new contracts related to its participation in SMT, the Company's proposed level of SMT expenses does not reflect a known and measurable change and should be rejected.

To depart from using test-year data, a utility's proposed change must be both known and measurable.[113] To satisfy this standard, the expenses included in the utility's cost of service are "limited to amounts actually realized or which can be anticipated with reasonable certainty."[114] As discussed in OPUC's initial brief, OPUC has reflected the portion of the changed costs that are known and measurable, specifically the 2020 contract costs.[115] There is no dispute that these costs are known and measurable with reasonable certainty. However, the record demonstrates that the remaining amounts that the Company seeks to recover, such as costs for professional and legal services, travel expenses, and meal and entertainment expenses, are not known and measurable with reasonable certainty.[116] The Company used estimates of the various costs based on its judgment, rather than evidence of actual costs, and then added a 10% contingency factor.[117] Yet the Company has not explained why these categories of costs would increase under the new contracts, and using a contingency factor as the basis for a known and measurable change is

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[111] OPUC Ex. 5 (Nalepa Direct) at 9.

[112] CEHE Initial Brief at 111-12.

[113] 16 TAC § 25.231(a)

[114] *Oncor Elec. Delivery Co. LLC v. Pub. Util. Comm'n of Texas*, 406 S.W.3d 253, 263 (Tex. App.—Austin 2013, no pet.) (citing *Suburban Util. Corp. v. Public Util. Comm'n*, 652 S.W.2d 358, 362 (Tex.1983)).

[115] OPUC Initial Brief at 65-67.

[116] *Id.*

[117] *Id.*; Tr. at 256-58 (Hudson Redirect).

unreasonable. The Company notes that the new SMT contracts allow for change requests,[118] but the Company experienced change requests prior to the contract amendments,[119] and thus, this factor does not appear to be a basis from diverging from test-year expense levels. Moreover, the amounts of any future change requests are not known and measurable with reasonable certainty.[120] As a result, except for the updated contract amounts, the information provided by the Company is not sufficiently certain to support a change from the test-year levels of SMT expenses and should not be used to set rates in this case.

J. Loss on Sale of Land

CenterPoint Houston's initial brief provides information about how the loss on the sale of land occurred and states that OPUC witness Mr. Nalepa did not question the prudence of these actions.[121] However, none of the information provided in the Company's initial brief was available prior to the date that Mr. Nalepa's testimony was filed in this case. The Company's direct testimony did not provide any description of the sales transactions or explain why there was a loss on the sale of the tracts.[122] The only information provided in the Company's application regarding the loss on the sale of land was contained in a workpaper to Schedule II-B-13, which identified the tracts of land, their book values, and sales prices.[123] Notably, all of the Company's citations in its initial brief are to CenterPoint Houston witness Mr. Narendorf's *rebuttal* testimony, which was filed after Mr. Nalepa's testimony. However, even with the additional information provided by Mr. Narendorf in rebuttal, there is insufficient information in the evidentiary record to support the reasonableness of the loss on the sale of land. OPUC addresses this lack of information in more detail in its initial brief.[124] OPUC's initial brief also discusses why the Company's loss on the sale of land should be treated differently than the gain on the sale of land in its prior rate case in Docket No. 38339.[125]

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[118] CEHE Initial Brief at 112.

[119] Tr. at 258-59 (Hudson Re-Cross).

[120] *Id.*

[121] CEHE Initial Brief at 114.

[122] OPUC Ex. 5 (Nalepa Direct) at 24-25.

[123] *Id.*

[124] OPUC Initial Brief at 67-70.

[125] *Id.*

VI. BILLING DETERMINANTS [PO Issue 4, 5, 45]

A. Weather Normalization

OPUC relies on its initial brief for a discussion of this issue.[126]

B. Energy Efficiency Plan ("EEP") Adjustment

CenterPoint Houston's initial brief acknowledged that Commission Staff recommended rejecting the Company's proposed EEP adjustment, but failed to note that OPUC made the same recommendation for the same reasons articulated by Commission Staff.[127] As discussed by both OPUC witness Mr. Nalepa and Commission Staff witness Mr. William Abbott, the EEP adjustment is not appropriate because it is not a known and measurable change and is an impermissible lost revenue adjustment mechanism ("LRAM").[128] OPUC addresses its recommendation in detail in its initial brief, but responds here to additional points in the Company's initial brief.

In its initial brief, the Company compares the EEP adjustment to its customer count adjustment, which was unopposed.[129] However, the proposed EEP adjustment is not akin to a customer count adjustment. A customer count adjustment uses actual customer data to account for customer growth during the test year so that energy consumption can be determined using the most recent (test-year-end) customer counts. In contrast, the Company's proposed EEP adjustment is a novel attempt to recover lost revenues by annualizing the assumed impact of certain energy efficiency programs that cannot otherwise be directly measured. The EEP and customer count adjustments also differ because the Commission has twice rejected similar attempts by the Company to impute an energy efficiency lost revenue adjustment, which no other electric utility in Texas employs. Conversely, electric utilities typically apply a customer count adjustment in developing rates, and the Commission generally requires electric utilities to adjust for customer growth in rate-making proceedings.

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[126] OPUC Initial Brief at 70-74.

[127] CEHE Initial Brief at 120-21.

[128] OPUC Ex. 5 (Nalepa Direct) at 46-49; Staff Ex. 7 (Abbott Direct) at 6-25.

[129] CEHE Initial Brief at 120.

The Company tries to distinguish its proposed EEP adjustment from other LRAMs by stating that the EEP adjustment is a billing determinant adjustment based on historical test-year data rather than a forward-looking mechanism to recover incremental lost revenues between rate cases.[130] However, as with the Company's past LRAM proposals, the EEP adjustment seeks to increase rates based on estimates of energy efficiency savings that are not known and measurable. Further, from a rate impact perspective, a reduction to billing determinants has the same effect as increasing the revenue requirement.[131] Therefore, the Company's proposed EEP adjustment is not substantively different from its prior LRAM proposals, which have previously been rejected by the Commission, and should similarly be rejected in this case.

VII. FUNCTIONALIZATION AND COST ALLOCATION [PO Issues 4, 5, 43, 44, 46]

B. Class Allocation

1. Class Allocation of Transmission Costs

a. "CenterPoint 4CP" versus "ERCOT 4CP" Class Allocation (separately for both transmission and for distribution)

The primary issue related to allocation of transmission costs in this case is whether such costs should be allocated based on ERCOT 4CP or CenterPoint Houston's 4CP.[132] The 4CP method allocates costs to a utility's customer classes based on each class's contribution to the system peak demands in each of the four months of highest use: June, July, August, and September.[133] In this case, CenterPoint Houston proposes to allocate transmission costs based on CenterPoint Houston's 4CP, which is the peak demand on *CenterPoint Houston's* system for June through September.[134] In contrast, TIEC and Commission Staff propose to allocate the transmission costs based on ERCOT 4CP, which is the peak demand on *ERCOT's* system for the same four months.[135] OPUC supports the Company's proposal in this case.

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[130] *Id.* at 121.

[131] Staff Ex. 7 (Abbott Direct) at 17.

[132] "4CP" refers to four coincident peaks.

[133] OPUC Ex. 7 (Nalepa Cross-Rebuttal) at 5.

[134] CEHE Initial Brief at 124-25; *see also* CEHE Ex. 30 (Troxle Direct) at 20.

[135] TIEC Initial Brief at 58-61; Commission Staff Initial Brief at 69-70.

TIEC and Commission Staff note that using CenterPoint Houston's 4CP would be a departure from the cost allocation approved in the Company's last rate case, which used ERCOT 4CP.[136] OPUC acknowledges that the use of CenterPoint Houston's 4CP would be a change. However, OPUC believes it is appropriate in this case because CenterPoint Houston's system is built primarily to serve the Company's peak demand,[137] and detailed customer demand data from the Company's system is now available from advanced meters.[138] Using 4CP data based on actual customer demand is more representative of the actual demand on CenterPoint Houston's transmission system and will provide for a more accurate allocation of transmission costs among the Company's customers.[139] This more accurate, granular customer demand data from the Company's advanced meters was not available for use in CenterPoint Houston's prior rate case because the Company had not completed its advanced meter deployment.[140]

TIEC and Commission Staff contend that using CenterPoint Houston's 4CP is inconsistent with Section 25.192 of the Commission's rules.[141] However, Section 25.192 does not dictate how transmission costs are allocated to customer classes in a rate case. Rather, the rule addresses how transmission service providers ("TSPs") charge distribution service providers ("DSPs") for transmission service.[142] The rule does not address how DSPs allocate those costs to retail customers. CenterPoint Houston is both a TSP and a DSP in ERCOT.[143] As a TSP, the Company's transmission system costs are pooled with the transmission system costs of other ERCOT TSPs, and then the total transmission system costs are charged to DSPs (including CenterPoint Houston) based on their contribution to ERCOT 4CP. However, the use of ERCOT 4CP for this purpose does not compel its use for allocating transmission costs in this rate case.

In determining the appropriate way to allocate transmission costs, it is helpful to consider the purpose of cost allocation in a rate case. As Commission Staff witness Mr. Brian Murphy

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[136] TIEC Initial Brief at 58; Commission Staff Initial Brief at 69-70.

[137] CEHE Initial Brief at 124 (citing CEHE Ex. 45 (Troxle Rebuttal) at 6).

[138] OPUC Ex. 7 (Nalepa Cross-Rebuttal) at 5.

[139] *Id.* at 7.

[140] *Id.*

[141] TIEC Initial Brief at 58; Staff Initial Brief at 69-70.

[142] CEHE Ex. 45 (Troxle Rebuttal) at 8.

[143] Commission Staff Ex. 2A (Murphy Direct) at 12-13, 15.

stated, cost causation is important in the class cost allocation step of ratemaking.[144] Cost causation is the ratemaking principle that costs are to be assigned to those customers who cause the costs to be incurred by the utility.[145] TIEC and Commission Staff assert that, because the TSP transmission costs are charged to CenterPoint Houston based on ERCOT's 4CP, the use of ERCOT 4CP is consistent with cost causation.[146] However, CenterPoint Houston's transmission system is built primarily to serve the Company's peak demand, not ERCOT's peak demand, so the use of CenterPoint Houston's 4CP is more relevant in determining the cause of the transmission system costs. In other words, because the transmission facilities in the Company's service area are built to meet the demands of CenterPoint Houston's customers, it is the demand that these customers place on CenterPoint Houston's transmission system that drive the costs of the system. While these costs are "uplifted" to the ERCOT system, the costs are incurred to meet the demand of CenterPoint Houston's customers. As a result, using CenterPoint Houston's 4CP is more reflective of cost causation and should be adopted in this case.

d. Moderating the Update to the 4CP Class Allocation Factor

TIEC contends that rate moderation is warranted if the Commission allocates transmission costs using the CenterPoint Houston 4CP as proposed by the Company.[147] TIEC does not request rate moderation if the ERCOT 4CP is used as proposed by TIEC and Commission Staff.[148] TIEC asserts that rate moderation is necessary because the Transmission class's allocation would increase from 12.22% to 14.92%, which is a change of 22.1%.[149] However, TIEC has failed to demonstrate that rate moderation is appropriate in this case. As an initial matter, TIEC has not provided any specific proposal for how rate moderation should be implemented in this case.[150] Moreover, the Commission has established a strong preference to move classes to cost of service,

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[144] Staff Ex. 2A (Murphy Direct) at 18.

[145] *Id.*

[146] TIEC Initial Brief at 59-60; Staff Initial Brief at 69-70.

[147] TIEC Initial Brief at 63.

[148] *Id.*

[149] *Id.* at 63-64.

[150] TIEC Initial Brief at 63-65. Similarly, TIEC witness Mr. Pollock's direct testimony addressing rate moderation also does not provide a specific rate moderation proposal. *See* TIEC Ex. 1 (Pollock Direct) at 28-35.

and has approved rate moderation plans on only rare occasions.[151] In addition, when considering whether to implement rate moderation, the Commission should consider the total bill impact, not the effect of a single cost allocator. TIEC has not established that an isolated increase in this single allocation factor will lead to overall rate shock for the Transmission class or any other class.[152] Accordingly, TIEC's proposal for rate moderation is not supported and should be rejected in this case.

2. Municipal Franchise Fees [PO Issue 27]

Municipal franchise fees (MFFs) are fees, similar to rent, paid by a utility to various municipalities for the use of their rights-of-way. Consistent with Commission precedent, CenterPoint Houston allocated MFFs to retail delivery classes using in-city kilowatt-hour (kWh) sales.[153] TIEC opposes the Company's allocation methodology, and instead, proposes that the in-city kWh sales be weighted to reflect the different MFF rates charged by the various cities in CenterPoint Houston's service area.[154] As discussed below, TIEC's proposal is not consistent with Commission precedent, has been rejected by the Commission in prior proceedings, and should be rejected in this case.

First, this issue has already been litigated and resolved in CenterPoint Houston's last rate case. In that case, the Commission found that "CenterPoint's allocation of municipal franchise fees to the customer classes based upon in-city kilowatt-hour (kWh) sales and collection of the fees from all customers within the customer class is reasonable and consistent with Commission precedent."[155] CenterPoint Houston has followed this precedent in the current proceeding. Nevertheless, even though its recommendation differs from the currently approved MFF allocation methodology, TIEC states that its proposal is consistent with Commission precedent. However, Mr. Pollock made this same proposal regarding allocation of MFFs in CenterPoint Houston's last rate case, and his proposal was rejected by the Commission.[156] As a result, the proposal is not

[151] OPUC Ex. 7 (Nalepa Cross-Rebuttal) at 12.

[152] *Id.*

[153] OPUC Ex. 7 (Nalepa Cross-Rebuttal) at 7 (citing WP-Franchise and WP II-I-Total).

[154] TIEC Initial Brief at 65.

[155] Docket No. 38339 Order on Rehearing at FOF 179.

[156] OPUC Ex. 7 (Nalepa Cross-Rebuttal) at 8-9.

consistent with Commission precedent. In its initial brief, TIEC acknowledges that it made a similar proposal in the Company's last rate case, but states that "Mr. Pollock's approach is not at odds with the Commission's actual findings in Docket No. 38339."[157] However, the Commission considered Mr. Pollock's same proposal for this same utility and did not adopt it. Thus, TIEC's proposal is not consistent with the Commission's decision in that case.

The Commission also rejected a similar proposal by Mr. Pollock in ETI's rate case in Docket No. 39896.[158] TIEC contends that OPUC witness Mr. Nalepa claimed that in ETI's rate case the Commission "rejected weighting MFF expense by class usage within each city,"[159] but this is a mischaracterization of Mr. Nalepa's testimony. In fact, Mr. Nalepa's testimony states that the Commission rejected Mr. Pollock's proposal in that case and then recites the Commission's findings of fact from that case.[160] Nevertheless, TIEC attempts to rebut a position that Mr. Nalepa did not take in his testimony. Citing to a schedule from ETI's tariff, TIEC states that ETI collects all incremental MFF expenses that are not in base rates through a rider charged directly to in-city customers.[161] However, an isolated tariff sheet does not demonstrate the Commission's practice for collecting all incremental MFF expenses. In contrast, the Commission made specific findings in its order in Docket No. 39896 reflecting that MFFs should be charged to all customers in ETI's service area, regardless of geographic location.[162]

TIEC also contends that "[n]o party disputed that Mr. Pollock's allocation better reflects each class's contribution to CEHE's MFF expense."[163] However, OPUC does dispute this point. In the ETI rate case, the Commission made the following findings of fact:

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

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[157] TIEC Initial Brief at 66, 68-69.

[158] OPUC Ex. 7 (Nalepa Cross-Rebuttal) at 9-10, 14 (citing Docket No. 39896, Order on Rehearing at FOFs 178-81).

[159] TIEC Initial Brief at 69.

[160] OPUC Ex. 7 (Nalepa Cross-Rebuttal) at 9.

[161] TIEC Initial Brief at 69.

[162] Docket No. 39896, Order on Rehearing at FOF 180.

[163] TIEC Initial Brief at 66.

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

181. It is reasonable and consistent with the Public Utility Regulatory Act (PURA) § 33.008(b) that MFF be allocated to each customer class on the basis of in-city kilowatt hour (kWh) sales, without an adjustment for the MFF rate in the municipality in which a given kWh sale occurred.[164]

As the Commission noted, *all* customers benefit from the utility's integrated system and use of municipal rights-of-way regardless of geographic location. Therefore, attempting to allocate costs based on geographic location is not a better reflection of cost causation because it ignores the benefit that all customers receive from the utility's integrated system and use of municipal rights-of-way.

There are also other policy reasons that support CenterPoint Houston's treatment of MFFs. In considering rate design, it is also important to consider simplicity and consistency.[165] The Company's proposal serves both of these goals because it applies a uniform policy to all customers and maintains the Commission's historical practice. Notably, TIEC's proposal would not promote the goal of simplicity. As shown in Exhibits JP-3, JP-5 and JP-6 to Mr. Pollock's direct testimony, there are 93 separate MFF rates that he weights for each of the Company's seven customer classes to develop his proposed allocation factors. Deriving a city-by-city allocation in this manner introduces unnecessary complexity in setting the Company's rates. Further, as discussed above, the Company's proposal follows the Commission's longstanding treatment of MFFs, which promotes consistency. Accordingly, the Company's proposed allocation of MFFs is reasonable and should be adopted in this case.

3. Transmission and Key Accounts

In its initial brief, TIEC criticizes the amount OPUC witness Mr. Nalepa initially proposed to directly assign to the transmission class for the Transmission and Key Accounts Department.[166] However, as discussed in OPUC's initial brief, OPUC updated the amount based on additional information obtained at the hearing regarding the annual cost of the Transmission Accounts and

[164] Docket No. 39896, Order on Rehearing at FOFs 178-181.

[165] OPUC Ex. 7 (Nalepa Cross-Rebuttal) at 10-11.

[166] TIEC Initial Brief at 69-70.

Support group.[167] Based on that information, OPUC recommends that $1.3 million be directly assigned to transmission.

TIEC also contends that since transmission voltage retail customers already pay contributions in aid of construction ("CIAC") to interconnect, the direct assignment of the costs for the Transmission Accounts and Support group to transmission customers would result in those customers paying twice for the same service.[168] However, the basis for OPUC's proposed direct assignment of these costs is that only transmission customers benefit from the services provided by the Transmission Accounts and Support group.[169] Non-transmission customers are not served by this group, and therefore, these customers should not be responsible for paying the costs based on cost-causation principles. Further, it is not clear from the evidentiary record that transmission customers would be paying twice for the same service. It is also possible that the CIAC represent an incremental cost of interconnecting transmission customers, not a duplication of costs.

TIEC further states that OPUC has singled out the transmission class for direct assignment of costs.[170] However, as discussed in OPUC's initial brief, OPUC's recommendation is based on the Commission's treatment of major account representatives for other electric utilities.[171] OPUC is proposing a similar adjustment in this case. OPUC acknowledges that direct assignment of other costs may be appropriate depending on the specific facts surrounding those costs.

4. Allocation of Hurricane Harvey Restoration Costs [PO Issue 56]

OPUC relies on its initial brief for a discussion of this issue.[172]

XII. CONCLUSION

For the reasons stated in its initial brief, this reply brief, and the testimonies of its witnesses, OPUC respectfully requests that the SOAH ALJs adopt and incorporate OPUC's recommendations

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[167] Tr. at 235 (Sugarek Cross).

[168] TIEC Initial Brief at 70.

[169] OPUC Initial Brief at 78-79.

[170] TIEC Initial Brief at 70.

[171] OPUC Initial Brief at 78-79.

[172] *Id.* at 79-80.

into the PFD in this proceeding. OPUC further asks to be granted any other relief to which it may be entitled.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing document was served on all parties of record in this proceeding on this 16th day of July 2019 by facsimile, electronic mail, and/or first class, U.S. Mail.

Cassandra Quinn