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PUC DOCKET NO. 49421
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APPLICATION OF CENTERPOINT ENERGY HOUSTON ELECTRIC, LLC FOR AUTHORITY TO CHANGE RATES	§ § §	**BEFORE THE PUBLIC UTILITY COMMISSION OF TEXAS**

CENTERPOINT ENERGY HOUSTON ELECTRIC, LLC'S
REPLY TO EXCEPTIONS TO PROPOSAL FOR DECISION

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CenterPoint Energy Houston Electric, LLC ("CenterPoint Houston" or the "Company") respectfully submits its Reply to Exceptions to the Proposal for Decision ("PFD").

I. INTRODUCTION [PO Issues 1, 2, 3]

The decisions that the Public Utility Commission of Texas ("Commission") will make in this case have the potential to fundamentally change what has been a long-standing, constructive regulatory environment in Texas. As explained in CenterPoint Houston's Exceptions, the PFD recommendations, if approved by the Commission, will cause CenterPoint Houston to: (1) receive the lowest return on equity ("ROE") of any electric utility in the state of Texas; (2) face a credit downgrade; (3) receive materially lower Funds From Operations ("FFO"); and (4) forfeit $116.680 million in capital investment that has been made in the Company's transmission and distribution ("T&D") system since 2010 and will continue to be used and useful for years to come. Despite this result, Intervenors and Staff continue to argue for even deeper cuts in the Company's revenue requirement by encouraging the Commission to adopt:

- A capital structure and ROE that will further jeopardize CenterPoint Houston's credit metrics and require the Company to finance future capital investments at higher debt rates that will ultimately be borne by customers;[1]
- Capital disallowances for projects that have been in place for 30 years and undisputedly ensure reliable service at Houston's airports and the Houston Medical Center;[2]
- Additional operations and maintenance ("O&M") disallowances of over $50 million per year based on selectively chosen historical experiences that are not consistent with the actual test year expenses in the case;[3]

[1] Texas Coast Utilities Coalition ("TCUC") Exceptions at 1-10; Texas Industrial Energy Consumers ("TIEC") Exceptions at 6-15; Staff Exceptions at 5-7; H-E-B Exceptions at 4-8; Gulf Coast Coalition of Cities ("GCCC") Exceptions at 4-6.

[2] City of Houston and Houston Coalition of Cities ("COH/HCC") Exceptions at 8-14.

[3] COH/HCC Exceptions at 18-23; Staff Exceptions at 11-12.

- Additional payroll disallowances that would disregard the clear record evidence and send a signal that the Company should not structure its employee compensation in a manner consistent with the current labor market;[4] and
- Results that would overturn previously approved, final settlement agreements.[5]

Simultaneously, the Exceptions filed by Intervenors and Staff go out of their way to turn a blind eye to record evidence showing what constructive regulatory outcomes foster and what CenterPoint Houston has been able to achieve due, in large part, to the sound regulatory policy reflected in the Commission's decision in its last rate case in Docket No. 38339.[6] The evidence shows that the Commission's decision in that case has allowed CenterPoint Houston since 2010 to:

- invest over $6 billion in T&D infrastructure—equivalent to the installation of a new electric system capable of serving a customer base roughly twice the size of Corpus Christi and its unincorporated areas or, for the past four years, building a distribution line from Austin to Houston and back each year;[7]
- weather the impact of a generational storm event in 2017—Hurricane Harvey;[8]
- finish the installation of approximately 2.5 million Advanced Metering System ("AMS") meters, improving the intelligence and resiliency of its T&D system;[9] and
- prudently manage its cash flow so that the Company could take advantage of capital market conditions to lower the Company's overall cost of debt.[10]

In addition, the evidence in this case demonstrates that:

- CenterPoint Houston uses thorough budgetary and cost control processes on a daily, monthly and annual basis to ensure the prudence and reasonableness of costs;[11]

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[4] Staff Exceptions at 9-10.

[5] GCCC Exceptions at 7.

[6] *See Application of CenterPoint Electric Delivery Company, LLC, for Authority to Change Rates,* Docket No. 38339, Order on Rehearing (Jun. 23, 2011).

[7] In a Central Texas context, the magnitude of the Company's investment would equate to an electric system built to serve roughly half the size of the City of Austin or, alternatively, the cities of Round Rock, Pflugerville, Cedar Park and Georgetown, Texas combined.

[8] CEHE Ex. 6 at 46:8-47:8, 50:1-12 (Mercado Direct); CEHE Ex. 7 at 217:19-218:6 (Pryor Direct); CEHE Ex. 8 at 353:21-355:10 (Narendorf Direct).

[9] CEHE Ex. 1 at 13 (Application) (Bates Page).

[10] *Id.*

[11] CEHE Ex. 7 at 193:11–199:6 (Pryor Direct); CEHE Ex. 8 at 357:15–359:3 (Narendorf Direct); CEHE Ex. 9 at 589:13-607:20 (Bodden Direct); CEHE Ex. 10 at 687:10–13 (Sugarek Direct); CEHE Ex. 15 at 1090:10–1099:19 (Townsend Direct); CEHE Ex. 17 1593:10–1597:22 (James Direct); CEHE Ex. 19 at 1673:4–1678:8 (Kimzey Direct); CEHE Ex. 29 at 1703:1–1703:21 (Gauger Direct); CEHE Ex. 21 at 1716:1–1721:5 & 1736:9–1737:21 (Englet Direct).

- On average, CenterPoint Houston consistently builds transmission projects at amounts that are 8.5% *lower* than originally estimated;[12] and
- CenterPoint Houston provides and is consistently recognized for its outstanding customer service.[13]

Rather than acknowledging this evidence by seeking a result that will facilitate the continued financial integrity of the Company, the parties simply and often disingenuously suggest that CenterPoint Houston's revenue requirement should be reduced by hundreds of millions of dollars based on claims that the Company failed to meet its burden of proof—parties assert this position despite the fact that CenterPoint Houston's rate filing package ("RFP") fully complied with all statutory and Commission requirements and included thousands of pages of uncontroverted evidence that support a different conclusion. These parties also advocate disallowance arguments that are fundamentally inconsistent with one another and send very different signals regarding how the Company should prioritize its operations and investments. This is exemplified by COH's proposal to disallow $111.5 million in capital investment because the Company's T&D system is *too* reliable and the H-E-B ROE basis point penalty for not being reliable *enough*; a penalty that will cumulatively reduce the Company's earnings on its investment in the coming years by millions of dollars.

Fortunately, the final decision in this case, and the resulting regulatory policy decisions, rest with the Commission. In order to make these decisions, the Commission must necessarily be able to identify the actual revenue requirement based on its decisions, including flow-through adjustments for items like Accumulated Deferred Federal Income Tax ("ADFIT") and Accumulated Depreciation. In this regard, the Company, as detailed throughout its Exceptions, has provided the Commission with an evidentiary record that supports a fair and balanced result and allows the Commission to make constructive policy decisions that will influence what the Company can achieve in the coming years. These achievements can be significant and beneficial to the economic development of the Company's service territory and the State of Texas (as they have been for the past ten years) or they can be limited. CenterPoint Houston respectfully asks the Commission to consider the policy goals it has set for itself and the utilities that it regulates, and to let those goals and the evidence guide the decision making in this proceeding so that the

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[12] CEHE Ex. 32 at 18:4-18 & 81-82 (Exh. R-MWN-2) (Narendorf Rebuttal).

[13] CEHE Ex. 6 at 42:8–47:8 (Mercado Direct); CEHE Ex. 7 at 173:8–174:12 & 178:12–183:5 (Pryor Direct); CEHE Ex. 8 at 332:4–338:20 (Narendorf Direct); CEHE Ex. 9 at 581:1-589:12 (Bodden Direct): CEHE Ex. 10 at 665:15-669:14 & 670:15–676:21 (Sugarek Direct).

Company can maintain its financial integrity, continue to invest in its growing service territory, and ensure the provision of continuous and reliable service to the Greater Houston area at reasonable rates.

II. RATE BASE [PO Issues 4, 5, 10, 11, 12, 13, 15, 16, 17, 18, 19, 59]

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

1. Prudence Issues

b. CenterPoint Houston's prudent investment of $111.5 million in the URD CLEP and Major Underground Rehabilitation Programs should be fully recovered in its rates

In its Exceptions, COH continues to maintain that the entirety of the $111.5 million CenterPoint Houston invested in the Underground Residential Distribution Cable Life Extension Program ("URD CLEP Program") and the Major Underground Rehabilitation Program should be disallowed.[14] COH argues that CenterPoint Houston failed to demonstrate the need for these programs and it contends that these programs provide no affirmative benefit to customers.[15] This argument is, however, directly contradicted by other statements in COH's Exceptions, which evidence that these two programs have enabled CenterPoint Houston to achieve exceptional reliability performance.[16] For example, COH acknowledges that: (1) CenterPoint Houston has reported only 120 customer complaints per year over the last five years related to outages or adequacy of service;[17] (2) the Company's System Average Interruption Duration Index ("SAIDI") performance for eight of the last ten years was better than the Commission standard;[18] and (3) the Company consistently receives the lowest annual penalties among major utilities.[19] COH also notes that with 2.5 million customers, customer complaints represent less than 0.005% of CenterPoint Houston's customer base and that the Company's average customer service reliability is 99.98%.[20] The evidence proves that these reliability results are due, at least in part, to the URD CLEP and the Major Underground Rehabilitation Programs, which allow the Company to be

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[14] COH/HCC Exceptions at 8-14.

[15] *Id.* at 9-10.

[16] COH Exceptions at 12.

[17] *Id.* at 19.

[18] *Id.* at 11.

[19] *Id.* at 11-12.

[20] *Id.* at 19.

proactive rather than reactive in identifying underground cable failure issues[21]—a practice that directly benefits CenterPoint Houston's customers because it avoids the significant environmental, safety, and economic repercussions that can accompany electrical outages.[22]

In arguing that investment in the URD CLEP and Major Underground Rehabilitation Programs should be disallowed, it should not go unnoticed that COH offered no specific challenge to any specific cost incurred for either program. Rather, COH's complaint centers around a general dissatisfaction with the overall amount of investment that the Company has made to increase system reliability and respond to load growth.[23] This general dissatisfaction with costs, however, is not a legitimate challenge to the investment made in these programs. As explained in the PFD, "[i]f the utility's direct case makes a prima facie showing, the burden of production (also known as the burden of going forward with the evidence) shifts to other parties."[24] While COH implies that CenterPoint Houston did not meet its prima facie burden in this case, this is incorrect.[25]

CenterPoint Houston's Application and RFP included the direct testimony of four witnesses, who each testified in support of CenterPoint Houston's T&D system capital investment made between January 1, 2010 and December 31, 2018.[26] In addition, CenterPoint Houston provided detailed information regarding specific capital projects undertaken during this time period, including project descriptions, identification of the purposes of the capital project (i.e., load growth, restoration, system improvement, intelligent grid, etc.), the total project costs, including additions and net salvage, and the project category total.[27] In short, CenterPoint Houston met its prima facie burden. Thus, as the PFD further explains "[i]t is then incumbent on the challenging

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[21] CEHE Ex. 31 at 7:15-17 (Pryor Rebuttal).

[22] CEHE Ex. 32 at 10:6-18, 12:18-13:1 (Narendorf Rebuttal).

[23] COH/HCC Exceptions at 8-9.

[24] PFD at 10.

[25] COH/HCC Exceptions at 14.

[26] CenterPoint Houston witness Randal M. Pryor describes and supports the total capital investment that has been made in the Company's distribution system between January 1, 2010 and December 31, 2018. CenterPoint Houston witness Martin W. Narendorf Jr. similarly describes and supports the investment spent for transmission, substation and major underground work required to provide service to the distribution system. CenterPoint Houston witness Dale Bodden is responsible for the Engineering and Asset Optimization division and her testimony describes the engineering, planning, design and capital budgeting process for the distribution and transmission system. Finally, CenterPoint Houston Julienne P. Sugarek, who is responsible for the Power Delivery Solutions division, describes the customer interface, customer support and power quality solutions that directly impact CenterPoint Houston's customers. CEHE Ex. 7 at 166-325 (Pryor Direct); CEHE Ex. 8 at 326-573 (Narendorf Direct); CEHE Ex. 9 at 574-657 (Bodden Direct); CEHE Ex. 10 at 658-762 (Sugarek Direct).

[27] CEHE Ex. 7 at 183:6-193:10, 199:7-206:6, 248-325 & Voluminous WP RMP-2 2010 through WP RMP-2 2018 (Pryor Direct); CEHE Ex. 8 at 343:7-357:14 (Narendorf Direct).

party to produce credible evidence that its proposal is more reasonable than CenterPoint's."[28] Here, COH fails.

First, it is not credible for COH to argue that the investment made in the URD CLEP and Major Underground Rehabilitation Programs is "exorbitant"[29] when it fails to identify any single, specific investment made in those programs that was not reasonable or necessarily incurred. COH's challenge to the investment made in the URD CLEP and Major Underground Rehabilitation Programs can, at best, be characterized as conclusory. COH witness Scott Norwood asserted that the entire investment in these programs should be disallowed because they have not resulted in a discernible improvement in the Company's SAIDI over the 2010-2018 time period.[30] The evidence, however, showed that Mr. Norwood's position is premised on the incorrect assumption that the URD CLEP and Major Underground Rehabilitation Programs are reactive rather than proactive in nature. While reactive programs are driven by specific cable failures that are singularly addressed, CenterPoint Houston's URD CLEP and Major Underground Rehabilitation Programs are proactive programs that are designed to identify potential failures in aged underground cable and other components before they fail. As such, the programs better serve the Company's customers by preventing future outages and maintaining system reliability.[31] COH's desire to evaluate the benefit of these programs based on a shown improvement in the Company's SAIDI is misplaced because the programs are resolving reliability issues before they occur.[32]

COH also more generically argues that customers have not otherwise benefited from these programs.[33] Yet, there is no dispute that customers expect reliable electric service for their residences and businesses, and it is part of the Commission's stated mission to promote high quality infrastructure. CenterPoint Houston has shown that the benefits of a reliable system include fewer interruptions of service and faster response times and reduced outage time for

[28] PFD at 451(proposed Conclusion of Law No. 11 citing *Entergy Gulf States v. Pub. Util. Comm'n*, 112 S.W.3d 208, 214-215 (Tex. App.—Austin 2003, pet. denied)).

[29] COH/HCC Exceptions at 12.

[30] COH/HCC Ex. 1 at 17:12-17 (Norwood Direct).

[31] CEHE Ex. 7 at 203:9-14 (Pryor Direct); CEHE Ex. 32 at 9:3-13:17 (Narendorf Rebuttal).

[32] CEHE Ex. 32 at 12:16-13:1 (Narendorf Rebuttal).

[33] COH/HCC Ex. 1 at 15:4-18:3 (Norwood Direct).

customers in the event of an outage.[34] With regard to the URD CLEP Program, the evidence established that:

- by identifying the risk of potential failures, CenterPoint Houston better serves its customers by preventing future outages and maintaining system reliability;[35]
- the URD CLEP Program provides for the rehabilitation of the cable back to original manufacturer specifications, which improves the present condition of the cable and extends the expected life;[36]
- the URD CLEP Program has allowed CenterPoint Houston to assess and extend the life of more than 10 times as many loops as it had been replacing annually; and
- CenterPoint Houston's URD CLEP Program contractor, IMCORP, provides a 15-year life extension guarantee for the Company's cable system on all assessed loops.[37]

Further, as a result of the URD CLEP Program, the Company is systematically reducing the backlog of aging 35-year-old cable and related systems. This is a prudent utility practice and the capital costs associated with these efforts are reasonable and necessary to the provision of utility service.

Likewise, the evidence established that CenterPoint Houston's investment in the Major Underground Rehabilitation Program was reasonable, necessary, and prudently incurred. The evidence demonstrates that:

- CenterPoint Houston's Major Underground Rehabilitation Program has been in place for over 30 years and provides important safety and reliability benefits because it proactively identifies potential failures in aged underground cable and other components before those failures occur;[38]
- customers receive more reliable service because unscheduled equipment outages are often avoided, and the proactive replacements are often completed without the need for a scheduled customer outage;[39]
- the proactive inspection and replacement of CenterPoint Houston's Major Underground facilities is vital to the continuous supply of reliable power to customers served within downtown Houston, the Texas Medical Center, Bush Intercontinental Airport, and many other areas of critical importance;[40] and

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[34] CEHE Ex. 9 at 607:4-6 (Bodden Direct).

[35] CEHE Ex. 7 at 203:9-14 (Pryor Direct).

[36] *Id.* at 204:16-20.

[37] *Id.* at 204:10-15.

[38] *Id.* at 203:9-11; CEHE Ex. 32 at 9:5-9 (Narendorf Rebuttal).

[39] CEHE Ex. 32 at 10:4-12:10 (Narendorf Rebuttal).

[40] *Id.* at 10:6-8.

- failure in the Major Underground infrastructure would significantly impact hundreds, if not thousands, of individuals living, working or receiving medical treatment in those key areas, and result in significant environmental, safety, and economic repercussions.[41]

COH offered no evidence to dispute these facts.

Moreover, there can be no dispute that COH has been aware of these programs and their benefits for years. As noted above, the Major Underground Rehabilitation Program has been in place for 30 years. The URD CLEP Program was implemented in 2013 and was first presented for recovery in CenterPoint Houston's first Distribution Cost Recovery Factor ("DCRF") filing in Docket No. 44572.[42] COH intervened, filed testimony and conducted extensive discovery regarding the program in that case. Thus, COH has been aware of the URD CLEP Program and its benefits since at least 2015.

COH also incorrectly claims that the only support that CenterPoint Houston provided to support the cost/benefits associated with the URD CLEP and Major Underground Rehabilitation Programs was a reference to the Asset Investment Strategy ("AIS") tool in response to discovery.[43] As evidenced above, this argument is disingenuous. It is also disingenuous for COH to try to rely on the AIS tool to justify the disallowance of the investment in these programs because CenterPoint Houston does not rely on the AIS tool to evaluate the prudence of undertaking a capital project.[44] Rather, CenterPoint Houston uses AIS to assist in the optimization of the Company's annual capital portfolio.[45] All of the capital projects entered into the AIS tool are developed, analyzed, and justified apart from the AIS process.[46] Further, as explained in the Company's Exceptions in Section II.A.1.b, COH's suggestion that CenterPoint Houston must fully meet its cost recovery burden of proof in its direct case or in response to discovery is not the legal standard.[47] Rather, as the party with the burden of proof, CenterPoint Houston is entitled to present rebuttal testimony and evidence responsive to arguments made by Intervenors and Staff. That is exactly what CenterPoint Houston did—CenterPoint Houston presented rebuttal evidence to further support the

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[41] *Id.* at 10:8-18, 12:2-10.

[42] CEHE Ex. 7 at 204:8-9 (Pryor Direct); CEHE Ex. 31 at 6:20-22 (Pryor Rebuttal).

[43] COH/HCC Exceptions at 10-11.

[44] *Id.* at 10-11; CEHE Ex. 32 at 5:20-21 (Narendorf Rebuttal).

[45] CEHE Ex. 32 at 6:12-13 (Narendorf Rebuttal).

[46] *Id.*

[47] COH/HCC Exceptions at 9-11. PURA § 36.006 ("In the *proceeding* involving a proposed rate change, the electric utility has the burden....") (emphasis added). Thus, it is the entire proceeding and not limited to direct and discovery.

prudence of the URD CLEP and Major Underground Rehabilitation Programs in response to the arguments raised by COH.

In expressing displeasure with what COH characterizes as an "extraordinary increase in Plant in Service" since 2010,[48] COH also distorts the load growth that CenterPoint Houston has experienced and the investment that has been required as a result. The evidence shows that CenterPoint Houston has experienced distribution growth of approximately 1,440 megawatts ("MW"), or an average load growth of 144 MW per year since 2009.[49] While COH emphasizes that this equates to approximately 1% per year, it misrepresents that this percentage demonstrates "little to nonexistent load growth" and fails to take into account the effect that this growth has had on CenterPoint Houston's distribution system.[50] CenterPoint Houston witness Dale Bodden put this load growth in perspective during the hearing, explaining that a distribution substation serves approximately 70 MW on average and, therefore, the Company added load equivalent to approximately two new substations per year.[51] Ms. Bodden further testified that this level of distribution load growth was substantial.[52] The evidence further shows that distribution load for the five years from 2018 through 2023 is projected to continue to grow by approximately 1,513 MW or an average load growth of 302.6 MW or 1.8% per year.[53] In short, it is a factual reality that an electric utility that serves more load will be required to make increased investments in its system.[54] The same is true for customer growth. This is particularly true where, as is the case for CenterPoint Houston, the customer and load growth is not geographically concentrated or limited to residential customers, but rather has required the deployment of new infrastructure capable of serving increased customer density within the City of Houston, within former pasture lands housing new suburban developments, and with new industrial loads along the Gulf Coast that are subject to flooding and high winds.[55]

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[48] COH/HCC Exceptions at 9.

[49] CEHE Ex. 9 at 592:12-14 (Bodden Direct).

[50] COH/HCC Exceptions at 9.

[51] Tr. at 220:7-17 (Bodden Redirect) (Jun. 24, 2019); *See also* CEHE Ex. 9 at 597:1-598:20 (Bodden Direct), wherein Ms. Bodden discusses some of the new substation construction that has resulted from load growth.

[52] Tr. at 220:7-17 (Bodden Redirect) (Jun. 24, 2019).

[53] CEHE Ex. 9 at 599:15-17 (Bodden Direct).

[54] CEHE Ex. 45 at 21:12-14 (Troxle Rebuttal).

[55] Tr. at 146:21-149:21 (Mercado Redirect) (Jun. 24, 2019).

Finally, as noted above, the crux of COH's argument is that CenterPoint Houston's service is *too* reliable, and thus, the cost of capital programs designed to proactively maintain the reliability of the Company's transmission and distribution system should be disallowed.[56] Effectively, COH suggests that CenterPoint Houston's quality of service should be lower and that two reliability-based, capital investment programs that have directly benefited CenterPoint Houston's customers by providing very high levels of reliability and the associated reduction in customer complaints should be discontinued. This is an unsound regulatory policy that should be rejected in its entirety.

B. Indirect Corporate Costs

The evidence soundly refutes COH's contention that CenterPoint Houston included indirect corporate costs in its prior DCRF filings.[57] First, in each of its DCRF filings, Docket Nos. 44572, 45747, 47032, and 48226, the Company attested to the fact that indirect corporate costs and capitalized O&M costs were excluded from its request as required by 16 Texas Administrative Code ("TAC") § 25.243(b)(3).[58] Second, indirect corporate costs are costs that cannot be directly assigned.[59] For this reason, the Company does not assign indirect corporate costs to capital projects.[60] Third, COH's statement in its Exceptions that CenterPoint Houston identified indirect corporate costs included in its DCRF filing as part of discovery is patently incorrect.[61] In response to discovery, CenterPoint Houston identified corporate costs associated with Accounts Payable, Property Accounting and the Call Center.[62] The Company established that the work performed by Property Accounting, Accounts Payable and the Call Center is all work performed based on capital activity and is not an activity or cost such as corporate aircraft or artwork, which the Commission provided as examples of indirect corporate costs in Project No. 39465.[63] Stated differently, the costs that COH seeks to disallow are costs *directly* assigned to capital work by those departments and are *not* indirect corporate costs as COH represents.[64] Because there are no indirect corporate costs assigned to capital projects either in this case or in the Company's prior DCRF filings, there

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[56] COH/HCC Exceptions at 9, 12-13.

[57] COH/HCC Ex. 1 at 18:18-22:2 (Norwood Direct).

[58] CEHE Ex. 37 at 6:12-7:11 & n.3 (Townsend Rebuttal).

[59] *Id.* at 7:3-6.

[60] *Id.*

[61] COH/HCC Exceptions at 15; *See* COH/HCC Initial Brief at Attachment 3 (Exhibit SN-13).

[62] CEHE Ex. 37 at 7:14-16 (Townsend Rebuttal).

[63] *Id.* at 5:10-6:2.

[64] *Id.* at 5:14-16.

is no need to make adjustments to exclude these costs and COH's Exceptions on this issue should be rejected.

E. Regulatory Assets and Liabilities [PO Issues 18, 19, 34, 41, 54, 59]

1. Amortization Period and Method of Recovery

Staff and the Office of Public Utility Counsel ("OPUC") challenge the PFD's recommendation that the Company should recover the following regulatory assets through base rates using a three-year amortization period: Hurricane Harvey restoration costs; Medicare Part D subsidy; Smart Meter Texas and REP Bad Debt.[65] Staff and OPUC instead support recovery of the costs over a five-year period and/or through riders instead of base rates.[66] The arguments Staff and OPUC put forth do not warrant rejection of the PFD. To the contrary, the position in the PFD should be approved because:

- The three-year amortization period is consistent with the amortization periods approved for regulatory assets in CenterPoint Houston's last rate case.[67]
- The three-year amortization period means that the costs to be recovered from customers are more closely aligned with the customers that existed at the time the costs were incurred—a ratemaking principle that OPUC witness June M. Dively supports.[68]
- The PFD reflects an approach that is consistent with the Commission's own RFP and related schedules, which specifically contemplate a utility including regulatory assets in base rates.[69]
- The position the PFD supports is also consistent with ASC 980, which allows utilities with cost-based rates to defer or capitalize certain costs (or regulatory assets) or obligations (regulatory liabilities) to be applied to future revenues.[70]

For these reasons, the Commission should adopt the PFD's recommendation to allow the Company to recover regulatory assets through rate base using a three-year amortization period.

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[65] PFD at 67, 108, 276.

[66] Staff Exceptions at 5 (Staff recommends recovery of the regulatory assets and liabilities over a five-year period through base rates. Staff's alternative position is recovery of these costs through riders.) OPUC Exceptions at 1-4. (OPUC supports recovery of the regulatory assets through riders with a five-year amortization period. OPUC's alternative request is recovery of the regulatory assets through base rates over a five-year period.)

[67] CEHE Ex. 35 at 42:18-20 (Colvin Rebuttal).

[68] *Id.* at 42:20-22.

[69] Transmission & Distribution (TDU) Investor-Owned Utilities RFP for Cost-Of-Service Determination Instruction for Schedule II-B-12 (Nov. 19, 2015) (TDU RFP).

[70] CEHE Ex. 12 at 868:19-869:1 (Colvin Direct). The ASC is the Financial Accounting Standards Board's ("FASB") Accounting Standards Codification ("ASC"), which is the source of authoritative generally accepted accounting principles ("GAAP") that are recognized by the FASB to be applied to nongovernmental entities.

2. Hurricane Harvey Regulatory Asset

GCCC also addresses this subject but does so only regarding recovery of Hurricane Harvey system restoration costs. The PFD appropriately recommends the Company should recover the Hurricane Harvey regulatory asset through base rates based on a three-year amortization period because:

- nothing about the Hurricane Harvey regulatory asset requires that it be recovered through a rider;
- the expenses were already booked and can be calculated as a lump sum; and
- the fixed amount of expenses for Hurricane Harvey restoration activities are amenable to recovery through base rates in contrast to variable expenses for which recovery through a rider might be appropriate.[71]

GCCC argues, however, that the Company ought to recover these costs through a rider over a five-year period.[72] GCCC insists that Hurricane Harvey costs should be recovered through a rider because the Company proposed a rider to return or refund unprotected excess deferred income taxes ("EDIT") to customers.[73] As the PFD correctly suggests, the use of a rider for a variable amount is reasonable, and unprotected EDIT is a good example of an item that is appropriately addressed through a rider. Specifically, the unprotected EDIT balance may change significantly over time.[74] For example, a change in the law or specific guidance from the Treasury or IRS could affect what amounts are properly characterized as protected EDIT or unprotected EDIT.[75] For these reasons, a rider is an appropriate way to separate items that may change over time from the cost of service used to calculate base rates. Using a rider for unprotected EDIT will allow CenterPoint Houston to track and record any over- or under-return of EDIT amounts.[76] That is not necessary for the costs in the Hurricane Harvey regulatory asset, which are known and will not change. In addition, there is no dispute the Company recorded a regulatory asset to defer Hurricane Harvey O&M expenses and did so based on prior treatment the Commission approved

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[71] PFD at 77.

[72] GCCC Exceptions at 4.

[73] *Id.*

[74] CEHE Ex. 12 at 909:21-910:5 (Colvin Direct).

[75] CEHE Ex. 13 at 1007:3-7 (Pringle Direct).

[76] CEHE Ex. 12 at 910:1-5 (Colvin Direct).

for the Company's Hurricane Rita costs.[77] GCCC's position on recovery of Hurricane Harvey costs through a rider should be rejected.

3. Medicare Part D Regulatory Asset

No party excepts to CenterPoint Houston's recovery of the Medicare Part D regulatory asset.[78] CenterPoint Houston explains in its Exceptions that, when properly calculated, the Medicare Part D regulatory asset totals $33.2 million, not the $5.572 recommended by the PFD. CenterPoint Houston further explains in its Exceptions that if the Commission adopts the PFD's proposal to calculate the Medicare Part D regulatory asset beginning January 1, 2013, the $5.572 million amount is still incorrect—a fact that the PFD itself recognizes.[79] To remedy this calculation error, CenterPoint Houston performed the calculation to give effect to the PFD's recommendation. This calculation results in a Medicare Part D regulatory asset in the amount of $16.176 million, or a $5.392 million amortization for three years.[80]

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

A. Return on Equity [PO Issue 8]

The 9.42% ROE recommended in the PFD is far too low for the reasons set forth in CenterPoint Houston's Exceptions to the PFD.[81] TIEC and TCUC, however, are not satisfied with a recommended ROE that would fall well below those authorized for other Texas electric utilities if it were approved by the Commission—they instead would have the Commission set CenterPoint Houston's ROE even lower.[82] As this Reply demonstrates, TIEC can support its ROE argument only by misstating facts and by relying on the deeply flawed analysis of its ROE witness, Michael P. Gorman. In contrast, TCUC's Exceptions on the ROE issue contain no analysis at all. TCUC merely cherry-picks some numbers from the ROE ranges recommended by the Staff and Intervenor witnesses (while ignoring CenterPoint Houston's ROE recommendations) and averages those numbers to arrive at an absurdly low ROE recommendation. The Commission should reject both sets of Exceptions.

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[77] *Id.* at 870:3-5.

[78] PFD at 81.

[79] *Id.* at 92 n.264

[80] CEHE Exceptions at 41.

[81] *Id.* at 45-59.

[82] It is also well below the average 9.64% ROE approved nationally for electric utilities since 2014. *See* CEHE Ex. 42 at 16:7-8 and Exh. R-RBH-8 (Hevert Rebuttal).

1. TIEC's Exceptions rely on Mr. Gorman's flawed ROE analysis and fail to appropriately consider CenterPoint Houston's risk factors

TIEC's Exceptions are remarkable, not for what they say, but for what they ignore. As CenterPoint Houston noted in its Exceptions, Mr. Gorman developed an analysis that purported to show CenterPoint Houston could maintain its current credit ratings with Mr. Gorman's proposed 9.25% ROE and 40.0% equity ratio, but Mr. Gorman actually performed the analysis using a 10.0% ROE.[83] When CenterPoint Houston pointed out his error, Mr. Gorman admitted the error and re-ran his analysis, which dropped the credit metrics below the level necessary to maintain CenterPoint Houston's current credit rating.[84] Remarkably, Mr. Gorman did not change his recommendation; he simply speculated that his recommendation might still allow CenterPoint Houston to maintain its current credit ratings under the Standard & Poor's ("S&P") metrics.[85]

Despite Mr. Gorman's analysis being discredited, TIEC continues to argue that the PFD's recommended ROE is high, because it is at the "very high end" of the ROE range developed by Mr. Gorman.[86] One might suppose that TIEC would address Mr. Gorman's errors in an effort to rehabilitate his analysis, but TIEC does not bother to do this. Instead, it presses forward as though the analysis retains some integrity. It does not. Moreover, it is axiomatic that a utility's allowed return must be commensurate with the return available on other enterprises of comparable risk.[87] TIEC, however, makes no effort to explain how CenterPoint Houston would be able to attract capital with an authorized ROE that is 43 basis points below the national average authorized ROE of 9.68%, and significantly below any authorized ROE in Texas.[88]

TIEC next argues that CenterPoint Houston benefits from low business risk, and that this should be reflected through a "much lower ROE."[89] TIEC attributes this low level of risk to CenterPoint Houston's operation as a transmission and distribution utility ("TDU"), and the availability of regulatory cost-recovery mechanisms.[90] TIEC ignores, however, that CenterPoint

[83] CEHE Ex. 43 at 21:20-22:14 (McRae Rebuttal).

[84] *Id.*

[85] *Id.*

[86] TIEC Exceptions at 2.

[87] *Federal Power Comm'n v. Hope Natural Gas Co.*, 320 U.S. 591, 603 (1944); *Bluefield Waterworks & Improvement Co. v. Pub. Serv. Comm'n of W. Va.*, 262 U.S. 679, 692-693 (1923).

[88] *See* CEHE Ex. 42 at 16:7-8 and Exh. R-RBH-8 (Hevert Rebuttal).

[89] TIEC Exceptions at 7.

[90] *Id.*

Houston faces a higher level of risk than any other TDU in the Electric Reliability Council of Texas ("ERCOT") due to the proximity of its service area to the Gulf Coast, which makes it susceptible to sudden, unexpected damage from hurricanes and other severe storms, and thus, to the associated liquidity risk.[91] TIEC's Exceptions also fail to address the risk associated with CenterPoint Houston's high degree of customer concentration. Unlike other companies in the proxy group, subsidiaries of which each serve thousands, if not millions, of customers, CenterPoint Houston's customers consist of approximately 65 retail electric providers.[92] This high degree of concentration equates to a high risk of CenterPoint Houston suffering an adverse financial effect following an event of default by one or more of those customers.[93] As further discussed below in regard to CenterPoint Houston's capital structure, regulatory cost-recovery mechanisms are common among the proxy group companies, and CenterPoint Houston's ability to utilize them makes the Company more comparable to, not less risky than, these other companies.[94]

Finally, TIEC argues that ring-fencing will substantially reduce CenterPoint Houston's financial risk by insulating it from its parent company and other affiliates, thereby meriting a further decrease in CenterPoint Houston's authorized ROE.[95] However, CenterPoint Houston has demonstrated that the financial protections it has in place are robust and provide the needed separation from its parent and affiliates, and that the ring-fencing measures proposed by TIEC and Staff would have no beneficial impact on its credit ratings or reduce the Company's risk.[96] While parties to this case may have their own views about utility risk, investors in utility debt look to the views of credit rating agencies—and the ratings they assign—in determining the riskiness of and appropriate interest rate for utility debt. In this case, Moody's has expressly stated that the proposed ring-fencing measures would be credit neutral, not credit positive.[97]

The single risk factor facing CenterPoint Houston that TIEC acknowledges is risk associated with the Tax Cuts and Jobs Act of 2017 ("TCJA").[98] However, TIEC attempts to

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[91] CEHE Ex. 26 at 2706:4-14 (Hevert Direct); CEHE Ex. 27 at 2846:7-8 (McRae Direct).

[92] CEHE Ex. 26 at 2703:15-17 (Hevert Direct).

[93] *Id.* at 2703:19-2704:3.

[94] *Id.* at 2710:1-11.

[95] TIEC Exceptions at 8-9.

[96] CEHE Ex. 48 at 25:20-26:14 and CEHE Ex. 48a Confidential Exh. R-EL-5 (Lapson Rebuttal); CEHE Ex. 43 at 19:17-18, 20:8-10 (McRae Rebuttal).

[97] CEHE Ex. 48a Confidential Exh. R-EL-5 (Lapson Rebuttal).

[98] TIEC Exceptions at 7.

discount this risk by citing to a March 2018 CenterPoint Energy, Inc. ("CNP") presentation—which TIEC now attempts to characterize as CenterPoint Houston's "own words"—that describes the TCJA as a "manageable event."[99] As noted in CenterPoint Houston's reply brief, TIEC's reliance on this particular portion of the CNP presentation ignores the following important facts:

- The same March 2018 document forecasts a drop in CenterPoint Houston's ratio of FFO to Debt ("FFO/Debt") of more than 650 basis points from 2017 to 2019 as a result of the TCJA;[100]
- TIEC is proposing a reduction in CenterPoint Houston's equity ratio by 500 basis points in this case,[101] a factor that could not have been considered in the March 2018 presentation;
- The March 2018 presentation assumes a "constructive regulatory environment" in Texas,[102] which would not exist if the Commission were to accept TIEC's ROE and capital structure recommendations; and
- Since the issuance of the March 2018 presentation, Moody's Investor Service ("Moody's") June 16, 2019 comment noted that CenterPoint Houston's cash flow metrics will be under strain going forward because of the effects of the TCJA, as well as CenterPoint Houston's capital expenditure forecast.[103]

Moreover, CNP's messaging that the TCJA is a win for customers and other stakeholders and a positive driver for 2019[104] does not minimize the impacts of the TCJA. TIEC's arguments to the contrary are based on the erroneous assumption that certain concepts are mutually exclusive (i.e., the TCJA cannot be both a positive benefit to stakeholders and customers *and* weaken CenterPoint Houston's credit quality in the absence of any mitigation measures).[105]

TIEC also argues that regulated utility ROEs have been trending downward over the last several years, and that during that same period, utilities have maintained or improved their credit quality, access to capital, and stock valuations.[106] However, the evidence in this proceeding shows that there is no downward trend in authorized ROEs.[107] And the enactment of the TCJA in 2017

[99] *Id.*; *compare* TIEC Initial Brief at 38.

[100] TIEC Ex. 4a at Highly Sensitive Exh. CSG-2 (Griffey Direct) at bates page 345 (CenterPoint Houston's Response to TCUC 1-02, SP 2018 CenterPoint Energy Annual Presentation) (HSPM).

[101] *See* TIEC Ex. 5 at 7:13 (Gorman Direct).

[102] TIEC Ex. 4a at Highly Sensitive Exh. CSG-2 (Griffey Direct) at bates pages 228, 322 (CenterPoint Houston's Response to TCUC 1-02, SP 2018 CenterPoint Energy Annual Presentation) (HSPM).

[103] CEHE Ex. 43a, Confidential Exh. R-RBM-3 at 1 (McRae Rebuttal).

[104] Tr. at 84:9-16 (Mercado Cross) (Jun. 24, 2019); TIEC Ex. 12 at 5 (1st Quarter 2019 Earnings Presentation on May 9, 2019).

[105] *See* CEHE Reply Brief at 72.

[106] TIEC's Exceptions at 9.

[107] CEHE Ex. 42 at 7:8-10, 73:2-74:2 (Hevert Rebuttal).

has significantly changed utilities' key cash flow metrics such that pre-TCJA comparisons are of limited value.[108] As shown in CenterPoint Houston witness Robert B. McRae's Exhibit R-RBM-2, there have been twice as many downgrades as upgrades in 2019 because of the effects of the TCJA.[109]

TIEC also portrays a misleading picture of the authorized ROEs in other jurisdictions to support this supposed downward trend. TIEC asserts that the national average ROE for delivery-only utilities was 9.38% in 2018,[110] while ignoring the evidence that the average so far in 2019 is 9.42%.[111] TIEC argues that the 9.38% average is "potentially misleading and inflated" because it includes averaged data from all delivery-only utilities, many of which are riskier than CenterPoint Houston.[112] However, the opposite is true. Both the 9.38% (2018 average) and 9.42% (2019 average) are actually artificially low because they include extremely low formula rates from Illinois that are based on a premium over bond rates, not on actual investor requirements.[113]

2. TCUC's Exceptions ignore CenterPoint Houston witness Robert B. Hevert's ROE analyses and should be rejected

Besides TIEC, the only other Intervenor to take exception to the PFD's ROE recommendation is TCUC, who urges the Commission to adopt a ROE of 9.0%.[114] TCUC's Exceptions, however, contain nothing more than a recitation of the ROE ranges recommended by the Staff and Intervenor ROE witnesses. TCUC picks two numbers that it claims are within the "credible range" of ROEs and averages them to arrive at "an average ROE."[115] That is TCUC's entire argument.

TCUC makes no effort to explain why the bookends of its selected range establish the "credible range." Indeed, the lower end of TCUC's so-called "credible range" is 7.30%, which TCUC's own witness admitted was below any ROE that he was aware of anywhere in the United States.[116] In addition, the low end of the range is more than 200 basis points below the average

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[108] CEHE Reply Brief at 63-64.

[109] *See* CEHE Ex. 43a, Confidential Exh. R-RBM-2 (McRae Rebuttal).

[110] TIEC Exceptions at 9.

[111] Tr. at 526:13-16 (Woolridge Cross) (Jun. 26, 2019).

[112] TIEC Exceptions at 9.

[113] Tr. at 527:7-18 (Woolridge Cross) (Jun. 26, 2019).

[114] TCUC Exceptions at 3.

[115] *Id.* at 2-3.

[116] Tr. at 545:5-13 (Woolridge Cross) (Jun. 26, 2019).

authorized ROE for electric utilities. TCUC does not bother to explain how CenterPoint Houston could attract capital on reasonable terms with a ROE that is more than 200 basis points below the authorized ROEs of comparable utilities.

TCUC's proposed range completely excludes the range recommended by Mr. Hevert. Perhaps TCUC believes that even the low end of Mr. Hevert's recommended range is outside the "credible range," but TCUC makes no effort whatsoever to support such a position.

3. Conclusion

For the foregoing reasons, TIEC's and TCUC's attempts to further reduce the already insupportably low ROE recommended by the PFD are without merit. As set forth in CenterPoint Houston's Exceptions, the PFD's recommended ROE fails the *Hope* and *Bluefield* standards, and does not adequately reflect the significant capital investment CenterPoint Houston is making and will be making to serve customers.[117] Furthermore, Moody's has stated that a ROE materially below 10% will be considered credit-negative.[118] CenterPoint Houston respectfully requests that the Commission reject TIEC's and TCUC's Exceptions, and instead authorize a ROE for the Company that, at a minimum, is consistent with the recent ROEs authorized by the Commission for TDUs operating in ERCOT and with the national average ROE for electric utilities.

B. Cost of Debt [PO Issue 8]

No party has taken issue with the PFD's recommendation that CenterPoint Houston's current embedded cost of long-term debt be set at 4.38%.[119] However, TCUC excepts to the PFD's rejection of TCUC's alternate capital structure recommendation (0.90% short-term debt, 55.48% long-term debt, and 43.62% equity), based on the ALJs' conclusion that it is not appropriate to include short-term debt in determining CenterPoint Houston's overall cost of capital.[120]

TCUC first takes issue with the PFD's statement that "Commission precedent and long-standing practice has been to exclude the cost of short-term debt from the rate of return calculation and capital structure."[121] TCUC argues that the PFD's citation to a single docket, Docket No. 43695, is not sufficient to support this characterization of the Commission's "long-standing

[117] CEHE Exceptions at 45-59.

[118] CEHE Ex. 43a, Confidential Exh. R-RBM-3 at 1 (McRae Rebuttal).

[119] *See* PFD at 171.

[120] TCUC Exceptions at 3-6, 8-10.

[121] *Id.* at 4 (addressing PFD at 173).

practice."[122] The ALJs, however, are not required to cite every case in which the Commission has decided to establish a utility's capital structure based on common equity and long-term debt. It is enough that they cite to a prior case in which the Commission expressly noted its long-standing practice of excluding short-term debt from a utility's capital structure.[123] If the ALJs had wished to do so, they could have cited all of the prior cases in which the Commission has excluded short-term debt from the utility's capital structure, and that list would have included every rate case decided by the Commission in the last 20 years, including CenterPoint Houston's most recent base rate case.[124] Indeed, the list probably would have included every electric rate case decided in the entire history of the Commission.

In contrast, TCUC does not cite to a single case in which the Commission approved the use of short-term debt in a utility's capital structure,[125] and its own witness, J. Randall Woolridge, could not name a single case in which the Commission authorized the inclusion of short-term debt in a utility's capital structure.[126] It is troubling, to say the least, that TCUC argues the precedent on short-term debt is unclear or undeveloped when: (1) short-term debt was excluded from the utility's capital structure in literally every rate case decided by the Commission in at least the last two decades, and (2) TCUC does not identify a single case in which the Commission has authorized the inclusion of short-term debt in a Texas utility's capital structure.

TCUC next argues that it has presented sufficient evidence to support inclusion of short-term debt in CenterPoint Houston's capital structure.[127] As explained in CenterPoint Houston's evidence and in the PFD, however, the Company initially funds its capital investments with a combination of internally-generated funds, short-term debt, long-term debt, and common equity investments from CNP, but that short-term debt is converted to long-term debt when a utility asset is removed from Construction Work in Progress("CWIP") and placed in service.[128] TCUC does not contest this explanation, but argues that it ignores the fungibility of CenterPoint Houston's

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[122] *Id.*

[123] CEHE Ex. 69 at Tab 6 (CEHE's Cross Book of Mr. Woolridge) (emphasis added).

[124] *See* Docket No. 38339.

[125] *See* TCUC Exceptions at 3-6.

[126] Tr. at 522:4-10 (Woolridge Cross) (Jun. 26, 2019).

[127] TCUC Exceptions at 4-5.

[128] *See* CEHE Ex. 27 at 2836:13-18 (McRae Direct); CEHE Ex. 43 at 16:7-8 (McRae Rebuttal); CEHE Reply Brief at 70; PFD at 172-173.

sources of cash.[129] According to TCUC, because CenterPoint Houston acquires each asset through "a mix of indistinguishable dollars," the cost of short-term debt plays a key role in establishing CenterPoint Houston's cost of capital.[130] However, this argument is a red herring. The classification of dollars used to acquire an asset is not determinative, because all of CenterPoint Houston's long-term investments that are placed in service are financed with long-term debt and equity.[131] CenterPoint Houston earns a return on the investment only after it has been placed in service; therefore, only the long-term debt used to finance that investment should be included in the capital structure.

Moreover, TCUC overlooks the fundamental ratemaking principle that the capital on which a utility earns a return is the capital in rate base. CenterPoint Houston uses short-term debt primarily to finance CWIP and to fund day-to-day operating expense. Unless TCUC is willing to stipulate that CenterPoint Houston's CWIP and daily operating funds should be included in rate base, TCUC is arguing for an inappropriate and inequitable mismatch between CenterPoint Houston's capital structure and rate base.

Finally, TCUC faults the PFD for "simply ignor[ing]" that Mr. McRae has previously filed testimony before the Minnesota Public Utilities Commission requesting the inclusion of short-term debt in the capital structure of a different CNP subsidiary.[132] Minnesota, however, allows CWIP to be included in rate base.[133] Moreover, Minnesota has a long history of including short-term debt in rate base.[134] TCUC cannot demonstrate that short-term debt is appropriate for Texas merely by pointing to its treatment in a different jurisdiction with a different regulatory framework and different precedent.

For the above reasons, as well as those set forth in CenterPoint Houston's testimony and briefing,[135] the Commission should reject TCUC's Exceptions and find that it is not appropriate to include short-term debt in a utility's regulated capital structure.

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[129] TCUC Exceptions at 5.

[130] *Id.*

[131] *See* CEHE Ex. 43 at 14:9-10, 16:7-8 (McRae Rebuttal).

[132] TCUC Exceptions at 6.

[133] *E.g.*, Minnesota Public Utilities Comm'n, *In the Matter of the Application of Northern States Power Company for Authority to Increase Rates for Electric Service in the State of Minnesota,* Docket No. E-002/GR-13-868 at 44 (May 8, 2015).

[134] *Id.* at 61-62.

[135] *See* CEHE Initial Brief at 63; CEHE Reply Brief at 70-71.

C. Capital Structure [PO Issue 7]

The PFD recommends that the Commission approve a capital structure composed of 55% long-term debt and 45% equity.[136] CenterPoint Houston excepted to that recommendation because an equity ratio of 45% will not produce financial metrics that are sufficient to maintain the Company's current credit ratings.[137] Instead, the evidence has demonstrated that a 50/50 capital structure reasonably reflects the business and regulatory risks CenterPoint Houston faces; will support a credit rating that will help ensure that CenterPoint Houston will be able to access capital in nearly all economic climates; and more closely reflects the capital structures of utilities with whom CenterPoint Houston competes for capital.[138]

Despite the evidence demonstrating CenterPoint Houston's need for an increased equity ratio in this case, several Intervenors and Staff ask the Commission to reject the PFD's recommended capital structure of 55% debt and 45% equity and to adopt a 60% debt and 40% equity capital structure.[139] However, Intervenors and Staff misread the Commission's order in Docket No. 22344, give undue credence to a misleading statement in Staff witness Jorge Ordonez's direct testimony, and rely on erroneous assumptions about CenterPoint Houston's current business risks. As a result, their arguments should be rejected.

1. A capital structure composed of 60% debt and 40% equity is not an established standard for TDUs in ERCOT, nor does it justify Staff's and Intervenors' disregard for CenterPoint Houston's specific risks and more recent Commission precedent

Staff and Intervenors argue that CenterPoint Houston's capital structure should be composed of 60% debt and 40% equity, based on their assertion that precedent and current practice have established that this is the Commission's "preferred"[140] or "standard"[141] capital structure for TDUs operating in ERCOT.[142] GCCC even goes so far as to criticize the PFD for "disregarding

[136] PFD at 191.

[137] CEHE Ex. 27 at 2843:1-10 (McRae Direct); CEHE Ex. 48 at 42:13-21 (Lapson Rebuttal).

[138] CEHE Initial Brief at 60 (citing CEHE Ex. 27 at 2834:8-18 (McRae Direct)).

[139] H-E-B Exceptions at 8; Staff Exceptions at 6; GCCC Exceptions at 6; TCUC Exceptions at 8; TIEC Exceptions at 16.

[140] H-E-B Exceptions at 8.

[141] *Id.* at 4.

[142] *See* TIEC Exceptions at 12; GCCC Exceptions at 5.

the articulated, reconsidered, and affirmed policy of the Commission."[143] Their arguments have no merit for numerous reasons.

First, both Staff and TCUC contend that in Docket No. 22344, the Commission established a "precedent" that Texas TDUs should have a capital structure with 40% equity.[144] In fact, the Commission made it quite clear in Order No. 42 in Docket No. 22344 that its capital structure analysis was based on conditions the Commission foresaw *during the transition* to a competitive retail market:

> In approaching the issues of the appropriate ROE and capital structure, the Commission notes two underlying considerations that served as a starting point in the decision-making process. First, these decisions are made for ratemaking purposes for the newly unbundled TDUs *during the transition period*; and second, the decisions are based on the close correlation between the ROE and capital structure.[145]

At the hearing on the merits, Mr. Ordonez admitted that CenterPoint Houston is not "recently unbundled" but is an established utility, that the transition period is now over, and that nothing in the order in Docket No. 22344 indicated that it was intended to continue in effect in perpetuity.[146] Thus, it is clear that the Commission's reasoning in Docket No. 22344 no longer applies to the circumstances in this case. Instead, the Commission should focus on the business risks that CenterPoint Houston currently encounters and its need for access to capital in nearly all market conditions.

Staff and TCUC also ignore the fact that the Commission stated in the Docket No. 22344 order that its decision was based on a "close correlation" between ROE and capital structure.[147] Because it was adopting a capital structure with a lower percentage of equity than the industry norm, the Commission determined it was appropriate to add 50 basis points to the ROE that it otherwise would have considered reasonable.[148] Notably, Staff and Intervenors have not proposed making any upward adjustment to ROE to compensate for the higher percentage of debt that they

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[143] GCCC Exceptions at 5.

[144] Staff Exceptions at 5-6; TCUC Exceptions at 7.

[145] *Generic Issues Associated with Applications for Approval of Unbundled Cost of Service Rate 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) (emphasis added).

[146] CEHE Initial Brief at 65 (citing Tr. at 685:21-686:18 (Ordonez Cross) (Jun. 26, 2019)).

[147] Docket No. 22344, Order No. 42 at 9.

[148] CEHE Ex. 43 at 34:17-35:1 (McRae Rebuttal) (citing Docket No. 22344, Order No. 42 at 10).

propose.[149] Thus, they implicitly admit that it is no longer necessary to follow the approach set forth in the Commission's order on capital structure in Docket No. 22344, and their "precedent" argument has no merit.

Second, H-E-B,[150] GCCC,[151] TCUC, and TIEC[152] continue to support their capital structure arguments by citing to Mr. Ordonez's direct testimony that a 60% debt and 40% equity capital structure is consistent with the authorized capital structure of the "majority of TDUs operating in Texas"[153] based on his supposed identification of five TDUs in ERCOT with this capital structure.[154] However, as Mr. Ordonez admitted at the hearing, his testimony is inaccurate.[155] As the below chart illustrates, only *one* of five utilities[156] identified by Mr. Ordonez is actually a TDU operating in ERCOT with a 60% debt and 40% equity capital structure.[157] Moreover, that one utility, AEP Texas, has a pending rate case before the Commission in which it is requesting an increase in its currently authorized 40% equity ratio.[158]

Utility[159]	**Description**
Cross Texas Transmission, LLC	This utility is a transmission-only utility, not a TDU[160]
Electric Transmission Texas, LLC	This utility is a transmission-only utility, not a TDU[161]
AEP Texas Central Company	This utility no longer exists independently—it was merged into a single utility, AEP Texas[162]
AEP Texas North Company	This utility no longer exists independently—it was merged into a single utility, AEP Texas[163]
Wind Energy Transmission Texas, LLC	This utility is a transmission-only utility, not a TDU[164]

[149] *See id.* at 35:1-3.

[150] H-E-B Exceptions at 7, n.19.

[151] GCCC Exceptions at 5.

[152] TIEC Exceptions at 12, n.68.

[153] Staff Ex. 39 at 37:18-20 (Ordonez Direct).

[154] *Id.* at 37, n.41.

[155] Tr. at 691:3-12 (Ordonez Cross) (Jun. 26, 2019).

[156] The list represents a double counting of the former utilities that now make up AEP Texas. CEHE Ex. 43 at 37:18-20 (McRae Rebuttal).

[157] *Id.* at 37:18-38:2 (McRae Rebuttal).

[158] *Id.* at 37:21 (citing Docket 22344, Order No. 42 at 10).

[159] Staff Ex. 39 at 37, n.41 (Ordonez Direct).

[160] Tr. at 691:3-7 (Ordonez Cross) (Jun. 26, 2019).

[161] *Id.* at 691:8-12.

[162] *Id.* at 691:13-19.

[163] *Id.* at 691:20-24.

[164] *Id.* at 691:8-12.

Notably, Staff does not rely on this portion of Mr. Ordonez's testimony in its post-hearing briefing or in its Exceptions. H-E-B, GCCC, TCUC, and TIEC are either unaware of Mr. Ordonez's cross-examination testimony at the hearing on the merits, and CenterPoint Houston's briefing on this issue,[165] or they are intentionally continuing to mischaracterize the authorized equity ratios of other TDUs. Accordingly, their attempt to paint a capital structure consisting of 60% debt and 40% equity as the prevailing practice of TDUs in ERCOT based on the capital structures of the above-listed utilities is misleading, at best.

Finally, it is important to note that in 2011, the Commission considered the appropriate capital structure for CenterPoint Houston, a TDU operating in ERCOT, and did not simply award the Company a 60% debt and 40% equity capital structure based on some established "policy." Instead, the Commission considered CenterPoint Houston's specific business risks and determined that a 45% equity ratio was appropriate.[166] Similarly, the Commission has approved equity ratios higher than 40% for other TDUs such as Oncor and Texas New Mexico Power Company.[167] It is therefore bizarre that TCUC accuses the ALJs of "jettison[ing] the Commission's long-standing precedent from Docket No. 22344."[168] There is no such "long-standing precedent."

For these reasons, the Commission should reject Staff's and Intervenors' attempt to limit the Commission to a no longer applicable "standard" capital structure and should instead act consistently with its practice and precedent of reviewing the individual facts and circumstances in establishing CenterPoint Houston's capital structure.[169]

2. CenterPoint Houston's business and regulatory risks support a 50/50 capital structure

A common theme in Staff's and Intervenors' Exceptions is their assertion that their recommended capital structure is appropriate given CenterPoint Houston's low business risk as a TDU,[170] the existence of a constructive regulatory environment in Texas,[171] and the availability of

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[165] *See* CEHE Ex. 43 at 37:22-38:2 (McRae Rebuttal); Tr. at 691:3-24 (Ordonez Cross) (Jun. 26, 2019); CEHE Initial Brief at 66; CEHE Reply Brief at 68.

[166] CEHE Ex. 43 at 35:4-11 (McRae Rebuttal).

[167] *See Application of Oncor Electric Delivery Company LLC for Authority to Change Rates*, Docket No. 46957, Order at Findings of Fact Nos. 32 & 35 (Oct. 13, 2017); *Application of Texas-New Mexico Power Company to Change Rates*, Docket No. 48401, Order at Finding of Fact No. 48 (Dec. 20, 2018).

[168] TCUC Exceptions at 7.

[169] *See* CEHE Ex. 43 at 36:10-13 (McRae Rebuttal).

[170] H-E-B Exceptions at 6; Staff Exceptions at 5; TIEC Exceptions at 7; GCCC Exceptions at 5.

[171] H-E-B Exceptions at 5; Staff Exceptions at 6.

various cost-recovery mechanisms.[172] In considering these arguments, it is important to keep in mind that while Staff and Intervenors argue that CenterPoint Houston does not face any additional business risks that justify increasing its equity ratio, they are not recommending that CenterPoint Houston's capital structure remain at its current level (and the level recommended by the PFD)—they are recommending that it be *decreased* by 500 basis points.

As the evidence in this case shows, CenterPoint Houston faces numerous business and regulatory risks that merit a 50/50 capital structure:[173]

- Elevated capital expenditures over the next five years. It is undisputed that CenterPoint Houston will invest approximately $5.14 billion from 2019-2023 in order to serve its rapidly expanding service area;[174]
- Risks caused by the TCJA. Due to a combination of lower tax rates and the elimination of bonus depreciation, CenterPoint Houston will experience significant declines in cash flows and credit quality as a result of the TCJA;[175]
- Risk of catastrophic damage from hurricanes. CenterPoint Houston is exposed to high risk of hurricane damage because all of its service territory is within 100 miles of the Gulf Coast;[176] and
- Regulatory risk. Unfavorable policies and outcomes in regulatory and legislative decisions are a large risk for regulated utilities, and investors and rating agencies will continue to focus on CenterPoint Houston's regulatory risk especially in light of the TCJA's impacts.[177]

Staff and certain Intervenors also make much of the regulatory cost-recovery mechanisms available to CenterPoint Houston in their attempt to discount the Company's business and regulatory risk.[178] However, these mechanisms were available in 2011 when the Commission determined that CenterPoint Houston's risks merited a 45% equity ratio,[179] and there was no evidence that CenterPoint Houston has become less risky since that time. Indeed, Hurricane

[172] H-E-B Exceptions at 6; Staff Exceptions at 6; TIEC Exceptions at 7.

[173] CEHE Ex. 27 at 2835:12-17 (McRae Direct).

[174] CEHE Ex. 26 at 2680:5-12 (Hevert Direct).

[175] CEHE Ex. 27 at 2837:16-17 (McRae Direct).

[176] *Id.* at 2846:7-8; CEHE Ex. 26 at 2706:4-5 (Hevert Direct).

[177] CEHE Ex. 27 at 2849:5-15 (McRae Direct).

[178] H-E-B Exceptions at 6; Staff Exceptions at 6; TIEC Exceptions at 7.

[179] Tr. at 663:24-665:10 (Ordonez Cross) (Jun. 26, 2019); Tr. at 625:10-626:16 (Gorman Cross) (Jun. 26, 2019).

Harvey drove home the undeniable fact that CenterPoint Houston continues to have significant hurricane risk.[180] Staff and Intervenors somehow overlook that fact.

Moreover, recovery mechanisms are common among the proxy companies.[181] To the extent the proxy companies have mechanisms in place to address revenue shortfalls or cost recovery, CenterPoint Houston's use of transmission cost of service and DCRF mechanisms make it more comparable to its peers,[182] who have equity ratios more in line with CenterPoint Houston's requested 50% than with Staff and Intervenors' recommended 40%.[183] Furthermore, Moody's June 17, 2019, issuer comment acknowledges that CenterPoint Houston "benefits from transmission and distribution cost riders that reduce regulatory lag," but states that even considering those mechanisms, the Company's credit metrics will weaken in light of the TCJA and its capital expenditure forecast absent a positive rate case outcome.[184] And this has in fact come to bear, as evidenced by Moody's updated report issued June 26, 2019, changing CenterPoint Houston's outlook from Stable to Negative.[185]

Finally, while Staff and TIEC both assert that CenterPoint Houston's financial risk will further decrease if the Commission adopts the PFD's proposed ring-fencing measures,[186] the actual evidence proves that these measures would have no appreciable effect on CenterPoint Houston's credit ratings.[187]

3. Increasing CenterPoint Houston's equity ratio will help preserve the Company's financial metrics while balancing the interests of both customers and investors

TIEC argues that increasing the equity in CenterPoint Houston's capital structure will increase costs to customers, and that even if applying Mr. Gorman's recommendations resulted in a downgrade for the Company, the resulting increased debt costs would still be less expensive for

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[180] *See* CEHE Ex. 26 at 2706:5-9 (Hevert Direct) (noting that CenterPoint Houston incurred approximately $117 million in storm recovery in connection with Hurricane Harvey in 2017).

[181] CEHE Ex. 26 at 2710:5-6 (Hevert Direct).

[182] *Id.* at 2710:8-11.

[183] *Id.* at 2714:18-23.

[184] CEHE Ex. 43a, Confidential Exh. R-RBM-3 at 1 (McRae Rebuttal); *see* Tr. at 662:9-25 (Ordonez Cross) (Jun. 26, 2019).

[185] CEHE Exceptions at Attachment D. For the reasons set forth in CenterPoint Houston's Exceptions, the Company respectfully requests that the Commission reverse the ALJs' decision to exclude the Moody's June 26th report. CEHE Exceptions at 50-53.

[186] Staff Exceptions at 6; TIEC Exceptions at 13.

[187] *See* CEHE Ex. 43 at 20:6-10 (McRae Rebuttal).

customers than the pre-tax revenue needed to support equity.[188] Yet, TIEC and Staff acknowledge that the Commission has a duty to balance the interests of customers as well as investors when setting CenterPoint Houston's capital structure.[189] In this regard, the evidence shows that allowing CenterPoint Houston to include additional equity in its capital structure serves the interests of both consumers and investors because it helps to ensure that the Company will have access to capital in nearly all economic climates, which, in turn, helps ensure that CenterPoint Houston can continue to provide reliable service and respond to customer and load growth.

In the short-term, Staff and Intervenors' proposed capital structure may appear favorable to customers in the form of lower prices.[190] However, those savings become much more speculative when viewed over the life of the bonds that CenterPoint Houston will be issuing over the next several years. If the outcome of this case is not sufficient to preserve CenterPoint Houston's financial metrics, and it is downgraded, this would increase the cost of long-term debt at a time when CenterPoint Houston will be incurring a significant amount of additional long-term debt due to its capital expenditure forecast.[191] The trade-off must be measured over decades, because even though customers may pay less upfront under Staff's and Intervenors' recommended capital structures, if CenterPoint Houston is downgraded, customers will suffer from the overall higher interest rates on that debt for the entire life of the newly issued bonds.[192] The ultimate beneficiaries of lower bond coupon rates are customers, not CenterPoint Houston, because the cost of debt is passed through in rates on a dollar-for-dollar basis.[193] Additionally, a downgrade would cause CenterPoint Houston's cost of equity to rise as well, which will also affect customers.[194] While TIEC states it is "obvious" that for customers the more desirable choice is to bear increased costs resulting from a downgrade rather than the cost of increasing CenterPoint Houston's equity ratio,[195] this narrow and short-sighted view should be rejected by the Commission. As CenterPoint Houston witness Ellen Lapson testified, maintaining a utility's viability and ability to attract capital

[188] TIEC Exceptions at 11.

[189] *Id.* at 13; *see* Staff Exceptions at 6 (citing Tr. at 624:3-6 (Gorman Redirect) (Jun. 26, 2019)).

[190] CEHE Ex. 48 at 46:7-9 (Lapson Rebuttal).

[191] CEHE Exceptions at 60.

[192] *Id.*

[193] CEHE Ex. 43 at 40:20-41:1 (McRae Rebuttal).

[194] *Id.* at 41:1-3.

[195] TIEC Exceptions at 11.

provides a benefit to its customers that goes beyond the trade-off of lower revenue requirements in the near-term.[196]

4. Contrary to TIEC's arguments, CenterPoint Houston cannot maintain adequate credit metrics with a 40% equity ratio

In addition to the issues addressed above, TIEC's Exceptions raise additional arguments that are addressed in this section. First, TIEC contends that "in their rebuttal testimony, [CenterPoint Houston's] witnesses confirmed that [CenterPoint Houston] will maintain solid investment grade credit ratings on a standalone basis if the Commission adopts Mr. Gorman's recommended 9.25% ROE and 40% equity ratio."[197] However, "investment grade" credit ratings do not equate to financial integrity.[198] TIEC's repeated emphasis that CenterPoint Houston could maintain "solid investment grade credit ratings"[199] is an attempt to distract from the fact that a 9.25% ROE and a 40% equity ratio will not support CenterPoint Houston's *existing* credit metrics. Moreover, maintaining "investment grade" credit ratings is an unusually low hurdle because, as Mr. Gorman himself admits, in 2016-2018, there were *no other utilities* below investment grade.[200] While Mr. Gorman's recommendation may keep CenterPoint Houston's credit metrics from falling below every other utility, it does not in any way assure CenterPoint Houston's financial integrity or enable it to compete with other utilities for capital. While TIEC accuses CenterPoint Houston of using "scare tactics" in this case,[201] TIEC has failed to offer any credible analysis showing that its recommended capital structure will allow CenterPoint Houston to maintain credit metrics such that it can continue to access capital at reasonable rates.

TIEC is also incorrect that CenterPoint Houston witnesses Mr. McRae and Ms. Lapson agree that adopting Mr. Gorman's recommendations would decrease CenterPoint Houston's credit rating "by one notch *at most* for any of the rating agencies."[202] What CenterPoint Houston's testimony actually shows is that Mr. Gorman's recommendation results in financial ratios that are materially lower than the threshold for CenterPoint Houston's current ratings, signaling a potential

[196] CEHE Ex. 48 at 46:11-13 (Lapson Rebuttal).

[197] TIEC Exceptions at 14.

[198] CEHE Reply Brief at 72; *see* Tr. at 605:7-13 (Gorman Cross) (Jun. 26, 2019).

[199] TIEC Exceptions at 9, 14-16.

[200] *See* Tr. at 605:22-25 (Gorman Cross) (Jun. 26, 2019).

[201] TIEC Exceptions at 15.

[202] *Id.* at 14-15.

downgrade by Moody's and Fitch of *two notches*.[203] In addition, CenterPoint Houston's SACP (a component in S&P's rating approach) would be downgraded to a- under Mr. Gorman's recommendation, a *two notch* downgrade from the Company's current a+ SACP.[204] Under these projections, Ms. Lapson testified that CenterPoint Houston would essentially revert to the unfavorable financial status that it held prior to the Commission's decision in Docket No. 38339.[205] Notably, while TIEC points to CenterPoint Houston's projections of credit metrics under Mr. Gorman's recommendations, Mr. Gorman himself based his evaluation entirely on S&P's rating system, and did no analysis with respect to Moody's or Fitch Ratings ("Fitch").[206]

In addition, as CenterPoint Houston discussed in briefing and its Exceptions,[207] TIEC continues to disregard the obvious issues in Mr. Gorman's analysis with respect to CenterPoint Houston's financial metrics. In attempting to quantify CenterPoint Houston's S&P credit metrics under his recommendation, Mr. Gorman assumed a 10% ROE instead of the 9.25% he recommends.[208] CenterPoint Houston noted the error and explained that applying Mr. Gorman's 9.25% ROE would result in credit metrics below the level needed to maintain the standalone credit rating assigned by S&P for CenterPoint Houston. Incredibly, Mr. Gorman admitted that he had made the error and that it would reduce the CFO/Debt ratio below 13.0%,[209] the level needed to maintain CenterPoint Houston's standalone credit rating, but he did not change his recommendation or his testimony alleging that his recommendation would support CenterPoint Houston's credit rating. At no point has TIEC acknowledged this key flaw in Mr. Gorman's recommendation. Instead, it attempts to shift the focus to the "investment grade" credit ratings and lower short-term costs for customers it argues would result from its recommended capital structure, even if CenterPoint Houston is downgraded.

TIEC further maintains that CenterPoint Houston can attract capital on reasonable terms, even if subjected to the downgrade assumed under Mr. Gorman's recommendation.[210] However, the evidence in this case has established that the average equity ratio of the utilities that CenterPoint

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[203] CEHE Ex. 48 at 53:18-21, 55:1-9 (Lapson Rebuttal); *see* CEHE Ex. 43 at 24:1-25:17 (McRae Rebuttal).

[204] CEHE Ex. 48 at 54:13-15 (Lapson Rebuttal); CEHE Ex. 43 at 23:12-14 (McRae Rebuttal).

[205] CEHE Ex. 48 at 53:21-23 (Lapson Rebuttal).

[206] Tr. at 580:7-581:3, 608:7-609:23 (Gorman Cross) (Jun. 26, 2019).

[207] CEHE Exceptions at 50; CEHE Reply Brief at 62.

[208] CEHE Exceptions at 50 (citing CEHE Ex. 43 at 21:20-22:14 (McRae Rebuttal)).

[209] Tr. at 574:4-10 (Gorman Cross) (Jun. 26, 2019).

[210] TIEC Exceptions at 15-16.

Houston competes with for capital is closer to 50%, not 40%.[211] If CenterPoint Houston's capital structure reflects a lower level of equity than the companies with which it competes for capital, CenterPoint Houston will have more trouble attracting capital because lenders and investors will perceive the Company as having greater risk.[212]

5. Conclusion

The Commission's decision in this case is critically important to CenterPoint Houston and its customers. The combined impacts of the TCJA and CenterPoint Houston's capital expansion program will not allow the Company to maintain its current credit rating, absent a supportive rate case outcome. In practical terms, this would require either reducing the Company's planned level of capital investment or maintaining that level of investment but financing it at a higher cost of debt. Neither result would be good for CenterPoint Houston's customers or the communities it serves. The credible evidence establishes that even the PFD's recommended equity ratio of 45% will not be sufficient to provide that necessary support—therefore, the Commission should reject Staff and Intervenors' attempt to further lower this equity ratio and should instead grant CenterPoint Houston's Exceptions.

D. Overall Rate of Return [PO Issue 8]

For the reasons set forth above, the Commission should reject Staff's and Intervenors' Exceptions, and instead award CenterPoint Houston an overall rate of return that will allow the Company to maintain its financial metrics and continue providing safe and reliable service to its customers.

E. Financial Integrity [PO Issue 9]

The PFD properly rejected two of Staff's proposed ring-fencing measures. In its Exceptions, Staff argues that the PFD should not have rejected the language that would prohibit CenterPoint Houston from using below investment grade credit ratings as an argument in favor of a higher ROE.[213] While Staff claims that the ALJs overlooked the possibility that CNP's and

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[211] CEHE Ex. 27 at 2854:1-19 (McRae Direct) (stating that for the last eight calendar quarters, the average equity ratio was 53.28% for the holding companies in Mr. Hevert's proxy group, and 53.13% for the utility operating companies encompassed within those holding companies, and the average equity ratio of electric delivery-only utilities for calendar year 2018 was 49.91%.).

[212] *See* CEHE Ex. 48 at 52:17-20 (Lapson Rebuttal) ("If the Commission orders a capital structure that is excessively leveraged and may result in low credit ratings, utilities in Texas would have a harder time to access sources of funding and to fulfill the needs of customers.").

[213] Staff Exceptions at 7.

CenterPoint Houston's actions can affect CenterPoint Houston's credit ratings,[214] Staff ignores the possibility that actions or events totally outside of CNP's or CenterPoint Houston's control could also affect CenterPoint Houston's credit ratings. This could include a macroeconomic event, a change of law, or, as clearly demonstrated through the testimony of CenterPoint Houston's witnesses, the outcome of this rate case, if the proposals of the Intervenors and/or Staff, or the recommendations in the PFD are followed. As Ms. Lapson explained, CenterPoint Houston should not be prevented from making arguments that protect its financial integrity, particularly if it receives a credit rating downgrade because of a negative outcome in a rate case.[215] And, Staff offers no statutory authority to support its assumption that the Commission has authority to prohibit CenterPoint Houston from requesting and presenting evidence that an increase to its ROE is warranted.

Staff also claims that CenterPoint Houston should be precluded from arguing for an increased ROE in the event that it has taken some action that has caused a downgrade in its credit rating and to avoid ratepayers bearing the burden of any costs associated with a downgrade.[216] The language of this ring-fencing measure, however, goes far beyond what Staff claims is the purpose of the measure. As proposed, this ring-fencing measure does not distinguish between reasons (which, again, could be due to factors totally outside the control of CNP or CenterPoint Houston) for a credit downgrade or limit recovery of costs associated with a downgrade. In addition, the fact that CenterPoint Houston may raise an argument does not guarantee that it will prevail on the issue. Any ROE decision remains squarely in the hands of the Commission. CenterPoint Houston should, however, have the right to advance any argument that it determines is in its interest and the Commission may then decide whether to accept or reject those arguments. Further, prohibiting CenterPoint Houston from making these arguments arguably constitutes prior restraint of CenterPoint Houston's right to free speech without justification.[217] Therefore, the PFD properly rejected this measure.

[214] *Id.* at 7-8.

[215] CEHE Ex. 48 at 33:23-24:4 (Lapson Rebuttal).

[216] Staff Exceptions at 7-8.

[217] *See generally Kinney v. Barnes*, 443 S.W.3d 87 (Tex. 2014) (finding that while a permanent injunction to remove language from a website that was adjudicated as defamatory was acceptable, prohibiting the future use of language that was the same or similar to that found to be defamatory was an unconstitutional prior restraint).

Staff also excepts to the PFD's rejection of language that would prohibit CenterPoint Houston from seeking to recover costs associated with a CNP bankruptcy.[218] This language similarly prohibits CenterPoint Houston from making a request that the Commission would have the ability to accept or reject based on the arguments presented. Staff again incorrectly conflates CenterPoint Houston's ability to put forth an argument with the Commission's adoption of the argument and approving the recovery of costs. Further, this issue is not relevant to the costs under review and rates to be determined in this rate case proceeding. To be clear, the evidence establishes that there is no current bankruptcy at any of the CNP companies, CenterPoint Houston is not at risk of being drawn into the very unlikely prospect of a bankruptcy of its parent or sister companies,[219] and CenterPoint Houston has not asked to recover any bankruptcy costs in this proceeding. Finally, as with the prohibition of arguments regarding CenterPoint Houston's ROE based on its credit rating, this measure would also be an unconstitutional prior restraint on CenterPoint Houston's free speech and the PFD's rejection of it was proper.[220]

Staff's use of the history of Oncor to help justify the imposition of ring-fencing measures is also misplaced, even if well-intentioned. First, Staff's reference to the Oncor cases in Docket Nos. 34077 and 45188 as evidence that the Commission has adopted versions of this ring-fencing provision in prior cases ignores the fact that Oncor and its parent company *voluntarily* agreed to a version of this ring-fencing commitment in those dockets.[221] That is not the case here. Second, the use of the Oncor example must be viewed in the context of the history of the acquisition of Oncor's parent. As previously noted, almost all of the financing for the acquisition of Oncor's parent was debt, and investors in the acquisition financing for Oncor's parent (who accepted the risk of default in return for the possibility of a higher rate of return) knew that there was a high likelihood of default when that debt was issued.[222] In contrast, the majority of the financing used to acquire the stock of Vectren was in the form of equity issued by CNP, and both the remaining debt issued by CNP to acquire Vectren as well as CNP itself after the merger received solid

[218] Staff Exceptions at 8.

[219] CEHE Ex. 48 at 59:10-12 (Lapson Rebuttal).

[220] *See generally Kinney v. Barnes*, 443 S.W.3d 87 (Tex. 2014).

[221] *See* Staff Exceptions at 8 and n.25.

[222] CEHE Exceptions at 71.

investment grade credit ratings.[223] As a result, the Oncor example does not justify the imposition of ring-fencing measures on CenterPoint Houston.

Finally, TIEC makes several unfounded claims with respect to purported benefits of ring-fencing. First, TIEC claims that the "single largest threat" to CenterPoint Houston's financial stability is its credit linkage to CNP and that the PFD's recommendations on ring-fencing neutralize this threat.[224] To be clear, as fully described in CenterPoint Houston's Exceptions, the single greatest threat to CenterPoint Houston's financial stability are TIEC's, Staff's and other Intervenors' proposals in this proceeding. In particular, their proposals on capital structure, return on equity, and overall rate of return will do more harm to CenterPoint Houston's financial stability as revealed through the projected degradation of credit metrics and resulting multiple notch downgrades at each of the three major credit rating agencies than the Vectren merger, which resulted in a single notch downgrade at one credit rating agency and no change at the other two. And, the PFD's proposed ring-fencing measures do nothing to protect CenterPoint Houston from this serious threat to its financial stability.

Furthermore, TIEC makes the unfounded assertion that CenterPoint Houston borrows at BBB+ due to its affiliation with CNP.[225] As described in the testimony of Ms. Lapson, investors would typically either use the preponderance of the three rating agencies or the middle of the three; in either case, this would result in borrowings from debt investors at a rating that is unchanged from before the Vectren merger and otherwise based on CenterPoint Houston's standalone credit rating (as both Moody's and Fitch rate CenterPoint Houston on a standalone basis).[226] As such, the implication by TIEC that the proposed ring-fencing measures would result in a three notch upgrade to CenterPoint Houston's ratings is wrong for two clear reasons: 1) the investment community already generally disregards the S&P rating as it would look to Moody's and Fitch's ratings, and 2) Moody's has expressly stated that the proposed ring fencing measures would be credit neutral, not credit positive.[227]

In conclusion, both TIEC's analysis of the Company's current credit ratings and its claim that CenterPoint Houston's credit rating will improve with the imposition of the proposed ring-

[223] CEHE Ex. 48 at 12:11-16 (Lapson Rebuttal).

[224] TIEC Exceptions at 2.

[225] TIEC Exceptions at 14.

[226] CEHE Ex. 48 at 18:6-15 (Lapson Rebuttal).

[227] CEHE Ex. 48a Confidential Exh. R-EL-5 (Lapson Rebuttal).

fencing measures are wrong. As a result, TIEC's conclusion that the proposed ring-fencing will neutralize CenterPoint Houston's existing financial risk is also wrong. Instead, the facts show that the proposed ring-fencing will do nothing to mitigate the potential damage caused by TIEC's, Staff's and other Intervenors' proposals on capital structure, return on equity, and cost of capital.

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

A. Total O&M Expense

The PFD properly rejects COH's proposed $44.3 million adjustment to O&M because it violates PURA and 16 TAC § 25.231.[228] COH fails to disclose in its Exceptions that its proposed adjustment is based on the use of outdated 2017 O&M expenses, escalated by 2.6%.[229] In rejecting COH's position, the PFD correctly summarizes the legal standard regarding allowable O&M expenses.[230] The PFD also correctly recognizes that "future rates are made on the basis of past costs" where "changes occurring *after* the test period, if known, may be taken into consideration" by the Commission "to make the test year data as representative as possible of the cost situation that is apt to prevail in the future."[231] COH's approach violates these requirements[232] and thus, must be rejected to avoid legal error.

The PFD also rightfully rejects COH's position because COH offered no specific challenge to any specific O&M expense incurred by CenterPoint Houston during the test year and the evidence does not show that COH's proposal would establish a level of O&M expenses representative of CenterPoint Houston's costs to operate and maintain its T&D system.[233]

The evidence proves that CenterPoint Houston effectively controls its operating costs while continuing to provide safe and reliable service at reasonable rates and has a number of processes and procedures in place to ensure the Company's costs are properly managed and remain at reasonable levels.[234] Despite continuous cost control efforts, operating expenses associated with

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[228] PFD at 226.

[229] COH/HCC Exceptions at 18-23. The PFD, however, accurately identifies the basis for COH's proposed adjustment. PFD at 222.

[230] PFD at 219-220.

[231] *Id.* at 220 (citing *Suburban Util. Corp. v. Public Util. Comm'n*, 652 S.W.2d 358, 366 (Tex. 1983)) (emphasis added).

[232] *Id.* at 226.

[233] *Id.*

[234] CEHE Ex. 7 at 193:13-199:6 (Pryor Direct); CEHE Ex. 8 at 357:18-359:3 (Narendorf Direct); CEHE Ex. 9 at 589:14-607:20 (Bodden Direct).

new installations, regulatory compliance, and maintenance activities are rising as the Company responds to customer and load growth in its service territory.[235] While COH makes every effort to dismiss the impact that customer and load growth have had on the Company's test year O&M expense, COH cannot escape the facts showing that:

- CenterPoint Houston now serves 359,525 more residential customers and 41,991 more commercial customers than it did on December 31, 2009;[236]
- Customer growth has occurred not only in areas with existing infrastructure, but also in undeveloped locations, which require the deployment of all new infrastructure;[237]
- Over the past four years, overhead distribution pole miles (feeder-main and laterals) have increased an average of 171 miles per year, while URD circuit miles have increased an average of 257 miles per year;[238] and
- To support economic growth within the City of Houston and surrounding areas, CenterPoint Houston had to build or install approximately 221 new substation feeder positions to accommodate new distribution feeders, 55 new substation transformers, size upgrades for 12 substation transformers, and 6 new distribution substations.[239]

Further, for the same reasons discussed above in Section II.A regarding the impact that customer and load growth have on capital costs, there is a corresponding upward pressure placed on the Company's O&M expense. The actual effect these drivers have and will continue to have on CenterPoint Houston's ongoing expenses are not hypothetical, and they are reflected in CenterPoint Houston's test year costs. It is simply unrealistic to think that COH's proposal to rely on 2017 O&M expense levels as the baseline from which to establish rates in this case will be sufficient to operate and maintain CenterPoint Houston's T&D system in 2020 and beyond.

Finally, while COH proposed no specific disallowance to CenterPoint Houston's test year expense amounts in any specific O&M FERC account, it does generally point to seven FERC accounts that COH contends have unjustifiably increased over the average.[240] While COH contends these costs were not adequately explained,[241] the evidence proves otherwise. In rebuttal, CenterPoint Houston presented detailed evidence identifying the factors driving these costs as well as evidence showing that the test year costs in each of those accounts were representative of current

[235] CEHE Ex. 6 at 22:4-7 (Mercado Direct).

[236] CEHE Ex. 9 at 593:2-3 (Bodden Direct); CEHE Ex. 7 at 175:9-11 (Pryor Direct).

[237] Tr. at 147:1-149:21 (Mercado Redirect) (Jun. 24, 2019).

[238] CEHE Ex. 7 at 210:23-211:1 (Pryor Direct).

[239] CEHE Ex. 9 at 596:10-15 (Bodden Direct).

[240] COH/HCC Exceptions at 19, 22.

[241] *Id.* at 22.

O&M conditions as well as costs that will continue to be incurred in the future.[242] As these explanations make clear, the increase in CenterPoint Houston's O&M expenses is not simply due to the need to "address reliability concerns" as COH states in its Exceptions.[243] Rather, CenterPoint Houston's O&M costs are being driven not only by system improvements to replace aging infrastructure, but also by new infrastructure that has been constructed and must be operated and maintained to serve the approximately 400,000 new customers that CenterPoint Houston added to its system between 2010 and 2018.[244] Other O&M cost drivers were shown to include: (1) engineering and technology costs, including costs related to improvements, upgrades and maintenance of system equipment and software, as well as cyber security enhancements;[245] (2) the increased cost associated with the environmental disposal and clean-up of transformers;[246] (3) increased maintenance and repair costs, as well as corrective and preventative maintenance costs;[247] and (4) increased contractor labor costs.[248] And, all of these costs were shown to be expected to continue into the future as CenterPoint Houston's technology systems are updated and maintained, CenterPoint Houston's electric system ages, and labor costs continue to escalate.[249]

In sum, the test year in this case serves as the most appropriate and reasonable measure of the Company's O&M expenses. For these reasons, COH's proposed O&M adjustment was properly rejected in the PFD.

B. Labor Expenses

2. Incentive Compensation

a. Short-Term Incentive Compensation

The PFD correctly reflects that the total short-term incentive compensation ("STI") expense CenterPoint Houston requested to recover through rates is $16,879,888.[250] This amount is shown in CenterPoint Houston witness Kristie L. Colvin's rebuttal testimony and on

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[242] CEHE Ex. 31 at 20:7-21:24 (Pryor Rebuttal) addressing FERC Accounts 580, 588, 593, and 594; CEHE Ex. 32 at 29:1-32:3 (Narendorf Rebuttal) addressing FERC Accounts 560 and 570; CEHE Ex. 37 at 8:6-12:6 (Townsend Rebuttal) addressing FERC Account 930.2.

[243] COH/HCC Exceptions at 19-20.

[244] CEHE Ex. 32 at 29:18-30:2 (Narendorf Rebuttal).

[245] CEHE Ex. 31 at 20:7-22:9 (Pryor Rebuttal).

[246] *Id.*

[247] *Id.*; CEHE Ex. 32 at 30:3-31:20 (Narendorf Rebuttal).

[248] CEHE Ex. 31 at 20:7-22:9 (Pryor Rebuttal).

[249] *Id.*

[250] PFD at 231.

WP R-KLC-02, which is in the record.[251] Ms. Colvin also confirmed during the hearing in response to cross-examination questions on this issue that the $16,879,888 is the right amount.[252] Nevertheless, rather than accept the overwhelming evidence that identifies the right STI amount, Staff insists that the STI amount provided in the original response to Staff RFI 03-01 should be used to calculate STI recovery.[253] Staff's position should not be adopted. The PFD clearly and correctly states the total STI expense the Company requested is $16,879,888, and there is no reason to rely on amounts that do not reflect the Company's actual STI request.

b. Long-Term Incentive Compensation

TIEC, COH, OPUC and Staff urge the Commission to also disallow $3.8 million in time-based long-term incentive ("LTI") costs awarded in the form of restricted stock units ("RSUs").[254] In doing so, those parties take positions that are contrary to Commission precedent and distort the meaning of what constitutes financially-based LTI costs. In contrast, the PFD correctly notes that CenterPoint Houston's recovery of time-based LTI in the form of RSUs is consistent with the Commission's recent decisions on this issue.[255] The PFD also reflects the right perspective on time-based LTI: financial measures are not what trigger the RSU payments to employees.[256] Instead, RSUs require an eligible employee to remain with CNP for a three-year period to earn the incentive compensation.[257] Thus, the $3.8 million for RSUs are not tied to the achievement of financial goals and should be recovered through rates.[258]

Nevertheless, TIEC, COH, OPUC and Staff insist the time-based LTI costs should be disallowed as "financially based" because the value of the RSU award changes as the financial achievements of CNP change or because the incentive award is in the form of stock.[259] OPUC and TIEC, for example, ask the Commission to focus on the behavior or incentives the compensation is designed to promote.[260] Yet, the behavior that time-based RSUs are designed to encourage is

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[251] *See* CEHE Ex. 35 at 17:1-9 & 23 (WP R-KLC-02 - STI Expense Calculation Summary) (Colvin Rebuttal).

[252] Tr. at 1275:1-5 (Colvin Cross) (Jun. 28, 2019).

[253] Staff Exceptions at 9-10.

[254] TIEC Exceptions at 16-18; COH/HCC Exceptions at 23-25; OPUC Exceptions at 4-6; Staff Exceptions at 10.

[255] PFD at 248 (citing to Docket No. 40443, Order at 13, FoF No. 202 & Docket No. 46449, Order at FoF No. 199).

[256] *Id.*

[257] CEHE Ex. 39 at 23 (Harkel-Rumford Rebuttal).

[258] CEHE Ex. 35 at 18 (Colvin Rebuttal).

[259] TIEC Exceptions at 16-18; COH/HCC Exceptions at 24; OPUC Exceptions at 4-6; Staff Exceptions at 10.

[260] OPUC Exceptions at 4; TIEC Exceptions at 17.

for employees to stay with CNP for the long-term.[261] In addition, the fact that the award for this time-based LTI is in the form of stock does not make RSUs a financially-based component of LTI.[262]

To support its Exceptions, COH specifically disputes evidence showing that CNP must offer LTI to compete for employees. COH claims CNP does not need to provide LTI because "much of the electricity in this country" is provided by municipal electric providers, state-run electric systems, or federally owned utilities "virtually none of which pay" LTI.[263] This opinion, however, ignores a fundamental premise—CNP is not competing with municipal, state-run or federal utility providers for employees. In fact, the market compensation studies attached to CenterPoint Houston witness Lynne Harkel-Rumford's direct testimony show that those types of entities are not considered peers of CNP for determining compensation design or for pay purposes.[264] With approximately 2.5 million metered customers, 2,800 full-time employees, and over $3 billion in revenues, neither CNP nor CenterPoint Houston are comparable to the vast majority of those types of non-investor-owned entities.[265] Thus, COH's position is not grounded in the reality of the market in which CNP must attract and retain employees who are eligible to earn LTI.[266]

To the extent the Commission retains the customer-versus-shareholder benefit test that has previously been applied to incentive compensation recovery, the PFD already recommends a disallowance of the financially-based LTI the Company requested, which constitutes 70% of the LTI plan.[267] It is inappropriate to stretch the meaning of financially-based LTI to also disallow $3.8 million in purely time-based LTI. Moreover, disallowing time-based LTI costs is inconsistent with the evidence and prior Commission decisions. For these reasons, the PFD should be adopted on this issue and the related Exceptions of TIEC, COH, OPUC and Staff should be rejected.

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[261] CEHE Ex. 39 at 20:9-17 (Harkel-Rumford Rebuttal).

[262] *Id.* at 25:4-6.

[263] COH/HCC Exceptions at 25 (citing COH/HCC Ex. 2 at 39:24-40:16).

[264] CEHE Ex. 39 at 10:9-11 (Harkel-Rumford Rebuttal); CEHE Ex. 22a at Confidential Exhs. LHR-3 and LHR-6 (Harkel-Rumford Direct).

[265] CEHE Ex. 39 at 10:11-16 (Harkel-Rumford Rebuttal).

[266] CEHE Ex. 23 at 1903:11-1906:13 (Reed Direct) & CEHE Ex. 40 at 22:7-20 (Reed Rebuttal).

[267] PFD at 248. CenterPoint Houston takes exception to the PFD's position on those LTI costs. *See* CEHE Exceptions at 79-85. For a description of financially-based LTI, refer to CEHE Ex. 39 at 20:13-15 (Harkel-Rumford Rebuttal).

C. Depreciation [PO Issue 25]

TCUC's depreciation recommendations represent a significant departure from well-established depreciation practices and the depreciation methodologies consistently relied upon by experts and previously this Commission. The PFD rightly rejects TCUC's arguments as lacking credibility.[268]

1. Study methodology

TCUC's Exceptions challenged the recommended service lives for nine accounts, eight of which were calculated based on the Simulated Plant Record ("SPR") methodology and one based on actuarial analysis. TCUC's argument is essentially that (1) SPR analysis is less robust than actuarial analysis because it relies on unaged data; (2) all Company-specific data—operational changes, updated materials, and other retirement forces known to affect these assets—must be *disregarded entirely* because Company personnel cannot be relied on to provide accurate plant data;[269] and, accordingly, (3) the approved service lives of three other utilities are more reliable for setting CenterPoint Houston's depreciation rates. All three of these arguments were thoroughly rebutted by the record evidence, as recognized in the PFD. The evidence established that:

- The SPR methodology is regularly utilized by depreciation experts and produces results that can be as accurate and reliable as those produced using actuarial analysis;[270]
- The Company has used the SPR analyses to set depreciation rates since as far back as 1985,[271] including the existing rates that were adopted by the Commission in Docket No. 38339;[272]
- Staff testified the SPR method used by the Company is appropriate and commonly relied on by utilities and this Commission to determine reasonable life and survivor characteristics of property accounts;[273] and
- Staff conducted its own SPR analysis and arrived at the exact same results as the Company's witness.[274]

Moreover, sound depreciation theory and long-standing Commission precedent requires that depreciation rates be established on a utility-specific basis using the utility's own historical

[268] PFD at 265.

[269] CEHE Ex. 41 at 15:3-25:17 (Watson Rebuttal).

[270] Tr. at 325:8-17, 328:3-6, 328:25-329:23 & 349:4-350:6 (Watson Cross) (Jun. 25, 2019); Tr. at 838:5-839:22 (Tuvilla Cross) (Jun. 26, 2019).

[271] CEHE Ex. 41 at 4:3-5 (Watson Rebuttal) (citing Docket Nos. 6765, 12065, 22355, 32093, and 38339).

[272] *Id.* at 4:5-9.

[273] Staff Ex. 9 at 4:10-9:2 (Tuvilla Direct).

[274] Tr. at 827:7-10 (Tuvilla Cross) (Jun. 26, 2019); Staff Ex. 9 at 6:2-8:2 (Tuvilla Direct).

data and experience[275] and only suggests relying on other utilities in extraordinary circumstances, such as when a utility lacks *any* plant data for its assets.[276] Notably, TCUC presented no actual evidence to support its position that CenterPoint Houston's historical data and experience were unreliable nor did TCUC offer any evidence to demonstrate that these other utilities are comparable or similarly situated to the Company in any way.

There is also no merit to TCUC's contention that the entirety of the Company's recent experience should be disregarded based on the dubious premise that a utility's employees are "by definition" incapable of being objective and could fabricate information about its plant assets to enhance the Company's financial performance.[277] Sound depreciation practice dictates that depreciation experts rely on utility personnel for this type of information to better understand the assets being analyzed.[278] And, Mr. Watson thoroughly rebutted TCUC argument at hearing, explaining that he validates the integrity of all information he includes in his study.[279]

2. Specific Accounts

TCUC challenged the service lives for eight SPR-based accounts (Accounts 353, 354, 362, 364, 365, 366, 367, and 368) and one actuarial-based account (Account 390). Regarding all of these accounts, the ALJs rightly dismiss TCUC's concerns regarding the reliability of Company data and recognize that plant characteristics and actual Company experience are determinative factors in setting service lives for these accounts. In the interest of brevity, the Company summarizes below its response to TCUC's Exceptions regarding these accounts and directs the Commission to Pages 26-55 of Mr. Watson's rebuttal testimony for a detailed explanation of the flaws in TCUC witness David J. Garrett's analysis.

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[275] CEHE Ex. 41 at 4:14-5:2 (Watson Rebuttal).

[276] CEHE Ex. 41 at 10:12-16 & 16:16-17:15 (Watson Rebuttal); *see* Tr. at 841:9-16 (Tuvilla Cross) (Jun. 26, 2019) (explaining that using other utilities' approved service lives would be more appropriate "if a company has never had that type of plant before, like a wind facility or a battery. . ."); *See, e.g., Application of AEP Texas Central Company for Authority to Change Rates*, Docket No. 28840, PFD on Remand at 58 (Nov. 16, 2004) (indicating a preference for using a utility's own data to establish depreciation rates over that of other utilities); CEHE Ex. 41 at 15:5-14 (Watson Rebuttal) (citing *City of Amarillo v. Railroad Commission of Texas*, 894 S.W.2d 491, 501 (Tex. App.—Austin 1995, writ denied) (". . . depreciation rates are company and account specific.").

[277] Despite recognizing the lack of evidence to support its claims, TCUC asserts that this "does not prove that these things do not happen." To be clear, there is *no* evidence to support this claim. TCUC Exceptions at 17.

[278] CEHE Ex. 41 at 4:14-5:2 (Watson Rebuttal).

[279] Tr. at 342:16-347:6 & 349:4-353:16 (Watson Cross) (Jun. 25, 2019).

Account	CenterPoint Houston	TCUC	
353 (SPR)	53 R0.5	56 R0.5	• The ALJs properly recognized that the property in this account is changing.[280] • Mr. Garrett failed to provide operational justification for his life expectations, instead relying on lives approved for SWEPCO and OG&E, without evidence to support those comparisons.[281] • Mr. Garrett fails to reconcile his recommendation for these assets with his proposal in Docket No. 48401, where he proposed 45 years.[282]
354 (SPR)	59 R2.5	66 R2	• The ALJs recognized[283] that Mr. Garrett ignored Company-specific plant characteristics and experience that indicate a shorter service life for this account, specifically the impacts of electrical capacity upgrades, chemical reactions, higher loading on foundations, and a Company practice to replace structures when having to replace the foundations.[284] • The evidence does not support Mr. Garrett's unsupported reliance on the service life of a single Oklahoma utility to support his proposal.[285] • Mr. Garrett fails to reconcile his recommendation for these assets with his proposal in Docket No. 48401, where he proposed 54 years.[286]
362 (SPR)	48 R1	55 R0.5	• Mr. Garrett fails to account for the Company's plans to replace switchboard panels and use of more electronics.[287] • Mr. Garrett's proposal is inconsistent with his recommendation for Account 353 because distribution substations have a shorter life (53 vs. 48 years).[288]
364 (SPR)	35 R0.5	45 R0.5	• The PFD properly recognizes that changing conditions are affecting the assets in this account,

280 PFD at 267-268.

281 CEHE Ex. 41 at 28:10-29:4 (Watson Rebuttal).

282 *Id.* at 28:10-29:8 (citing Docket No. 48401, Direct Testimony and Exhibits of David Garrett at Exhibit DJG–4).

283 PFD at 268-269.

284 CEHE Ex. 41 at 31:1-20 (Watson Rebuttal); CEHE Ex. 25 at 2491, Exh. DAW-1 (Watson Direct).

285 TCUC Ex. 2 at 24:1-6 (Garrett Direct).

286 CEHE Ex. 41 at 21:4-9 (Watson Rebuttal) (citing Docket No. 48401, Direct Testimony and Exhibits of David Garrett at Exhibit DJG–4).

287 *Id.* at 33:1-17; CEHE Ex. 25 at 2503, Exh. DAW-1 (Watson Direct).

288 CEHE Ex. 41 at 33:1-17 (Watson Rebuttal). For example, distribution-level assets see more fault current than transmission and will, consequently, have a shorter life. CEHE Ex. 25 at 2503, Exh. DAW-1 (Watson Direct).

Account	CenterPoint Houston	TCUC	
			which Mr. Garrett ignores.[289] Specifically, the Company uses wood poles, which are being impacted by high water tables, high soil acidity levels, other coastal conditions and high humidity. Materials used for newer poles are shortening lives, and more pole contacts and inspections result in more replacements, also shortening lives.[290] There is no operational reason the life should increase by 10 years (or 30%) as Mr. Garrett proposes.
365 (SPR)	38 R0.5	40 R0.5	• The PFD recognizes that while the use of more modern equipment extends the service lives in this account, other impacts shorten the life,[291] such as increasing lightning strikes, wind, automobile strikes to poles, and environmental conditions.[292] • Increasing use of electronic equipment (such as sensors, motors and sectionalizing equipment with a much shorter life) is also shortening the service life.[293] • TCUC presents no evidence as to why the service lives of other utilities better represent Company assets.[294]
366 (SPR)	62 R2.5	65 S1	• As with Account 365, the Company is using more modern equipment in this account, but other retirement forces are shortening service lives. • Mr. Garrett's dispersion curve anticipates assets in this account surviving to nearly age 130, which is unreasonable.[295] Mr. Watson's dispersions curve assumes more realistic expectations.[296] • Mr. Garrett fails to reconcile his recommendation for these assets with his proposal in Docket No. 48401, where he proposed 52 years.[297]
367 (SPR)	38 R0.5	42 L0	• The PFD properly recognizes that underground conductor life is increasing due to newer conduit

[289] PFD at 270-271.

[290] CEHE Ex. 41 at 36:1-15 (Watson Rebuttal).

[291] PFD at 272.

[292] CEHE Ex. 41 at 39:10-21 (Watson Rebuttal).

[293] *Id.*; CEHE Ex. 25 at 2506 (Exh. DAW-1) (Watson Direct).

[294] TCUC Exceptions at 22-23.

[295] CEHE Ex. 41 at 41:10-42:10 (Watson Rebuttal).

[296] PFD at 273.

[297] CEHE Ex. 41 at 21:18-22:23 (Watson Rebuttal) (citing Docket No. 48401, Direct Testimony and Exhibits of David Garrett at Exhibit DJG–4).

Account	CenterPoint Houston	TCUC	
			technology but a recent shift to direct burying cable will shorten the cable life going forward.[298] Mr. Watson's recommendation reconciles these retirement forces.[299] Mr. Garrett dismisses them entirely. • Mr. Garrett does not address whether his "peer group" is subject to the impacts of direct burying.[300] • Mr. Garrett's dispersion curve anticipates assets surviving to nearly age 160, which is unreasonable.[301] Mr. Watson's dispersions curve anticipates more realistic expectations.
368 (SPR)	28 R1	32 L0	• Company engineers indicate that overload, lightning surge, cars hitting poles, growth and ants shorten the life of transformers[302] along with the fact that the Company is currently replacing rather than repairing outdated transformers.[303]
390 (Actuarial)	50 R4	58 R2	• This account includes building structures and improvements, both large and small, but Mr. Garrett essentially ignores life expectations for smaller shorter-lived assets like HVAC, chillers, roofs, fencing, water systems, lighting systems, elevators, fire protection systems, and other capitalized assets that will be replaced prior to the building shell.[304] Mr. Garrett fails to explain how his increase in life is operationally justified. • As explained in the PFD, Mr. Watson's analysis is more "realistic" because it recognizes that many building components fail at 50 years,[305] and Mr. Watson's analysis provides the "best fit"[306] Mr. Garrett disregards this experience, ignoring the fact that many building components frequently fail at 50 years.[307]

[298] PFD at 273-274.

[299] CEHE Ex. 41 at 45:4-46:12 (Watson Rebuttal).

[300] *Id.* at 46:1-12.

[301] *Id.* at 44:5-45:9.

[302] CEHE Ex. 25 at 2512 (Exhibit DAW-1) (Watson Direct).

[303] *Id.*

[304] *Id.* at 2522 (Exhibit DAW-1) & CEHE Ex. 41 at 54:22-55:4 (Watson Rebuttal).

[305] PFD at 267; CEHE Ex. 41 at 54:22-55:4 (Watson Rebuttal).

[306] PFD at 267.

[307] CEHE Ex. 41 at 54:22-55:4 (Watson Rebuttal).

Account	CenterPoint Houston	TCUC	
			• Mr. Garrett limited his analysis to a single band.[308]

Finally, Mr. Garrett's study contains a critical error because he failed to properly reallocate the depreciation reserve based on the changed service lives he recommends.[309] Accordingly, in addition to the errors in his methodology, his resulting depreciation rates are incorrect and cannot be relied on for purposes of making adjustments to the Company's rates.

H. Vegetation Management

The PFD properly recommends approval of CenterPoint Houston's test year expenses in the amount of $35.02 million for proactive tree trimming, hazard tree removal and reactive tree trimming (collectively, "vegetation management").[310] Only OPUC and Staff filed Exceptions to the PFD's recommendation. Rejection of OPUC's and Staff's proposals is supported by both the law and the record evidence in this case. From a legal perspective, OPUC's proposal to rely on a historical 2015-2017 average O&M to establish CenterPoint Houston's vegetation management expense as well as Staff's proposed use of a 2016-2018 average for vegetation management expense conflicts with the statutory and Commission requirement that a utility's expenses (1) be based on a historic test year and (2) that expenses be as representative as possible of the cost situation that is apt to prevail in the future.[311] The PFD correctly applies the Court's directive by recognizing that the costs CenterPoint Houston has already spent during the first six months since the end of the test year are comparable to those incurred during the test year[312] and thus, the test year costs are the most accurate representation of future costs. This is especially true given that both OPUC's and Staff's proposals rely on the use of historical period costs that are outdated by as much as three or four years.

Both OPUC's and Staff's proposals were further shown to be understated and unrepresentative of CenterPoint Houston's ongoing vegetation management expenditures due to their inclusion of 2017 expenses, which the PFD explains "does not accurately reflect normal annual vegetation management costs because it is not based on CenterPoint's normal operations

[308] *Id.* at 51:3-55:4.

[309] *Id.* at 55:5-20.

[310] PFD at 298.

[311] PURA § 36.051 and 16 TAC § 25.231; *Suburban*, 652 S.W.2d 358 at 366.

[312] PFD at 299.

over a 12-month period."[313] This is due to the disruption caused to these activities by Hurricane Harvey in 2017, which caused the Company to forgo 1.5 months of vegetation management activities.[314] Further, as the PFD explains, there is *no factual evidence* to support Staff's suggestion that reduced vegetation management activity in 2017 impacted CenterPoint Houston's vegetation management activities in 2018.[315] Rather, contrary to Staff's argument in its Exceptions,[316] the evidence shows that CenterPoint Houston *did not* increase its test year vegetation management activities in response to 2017's Hurricane Harvey. As the PFD concludes, this is evidenced by the fact that the 5,357 circuit miles trimmed in 2018 are comparable to the miles trimmed in three prior years: 2011 – 5,606 miles, 2013 – 5,074 miles, and 2014 – 5,139 miles.[317] The evidence further establishes that if Hurricane Harvey had not occurred, the expected level of distribution vegetation management expense would have been $31.89 million for 2017, which is more in line with the upward trend in vegetation costs CenterPoint Houston has experienced in recent years.

In short, CenterPoint Houston met its burden to demonstrate that its test year vegetation management costs were reasonable, necessary, and are reflective of the Company's ongoing operations. CenterPoint Houston's vegetation management activities are competitively bid with approximately 90% of the Company's proactive vegetation management work being based on a fixed price.[318] CenterPoint Houston performs inspections to ensure that vegetation management work is completed satisfactorily and reviews invoices to ensure accuracy.[319] The evidence further established that the costs associated with vegetation management activities continue to rise. For example, from 2011 to 2013, hazard tree expenditures increased due to drought conditions and the impact of pine bark beetles.[320] Likewise, proactive tree trimming expenditures increased from

[313] PFD at 298. Moreover, OPUC admits that in 2017 CenterPoint Houston necessarily halted its vegetation management activities "for a significant period of time due to Hurricane Harvey." OPUC Initial Brief at 63-64.

[314] CEHE Ex. 31 at 26:2-6 (Pryor Rebuttal).

[315] PFD at 298; While Staff makes this assertion in its Initial Brief, it offers no supporting evidentiary citation for this claim other than the unsubstantiated opinion of its witness and a misrepresentation of Mr. Pryor's rebuttal testimony; Staff Initial Brief at 50 and 51, n.207.

[316] Staff's Exceptions at 11-12.

[317] PFD at 299; CEHE Ex. 31 at 26:7-27:14 & 30 (Exh. R-RMP-02) (Pryor Rebuttal).

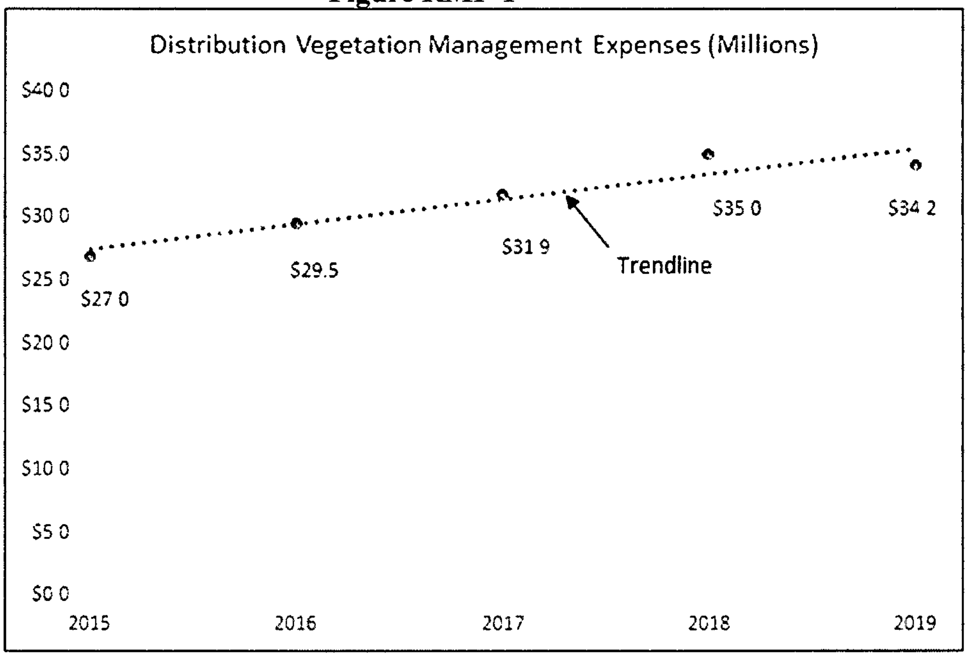
[318] CEHE Ex. 7 at 207:1-19 (Pryor Direct).

[319] *Id.* at 207:20-24.

[320] *Id.* at 212:1-18.

2014 to 2017 due to rising contractor labor rates.[321] The growing cost trend shown below further substantiates the fact that vegetation management costs and expenditures are continuing to go up as the Company's service territory grows, not down as the adoption of a three-year historical average would suggest.[322]

Figure RMP-1[323]



While OPUC argues that CenterPoint Houston was able to trim comparable miles at lower expense in prior years,[324] there is no dispute that the trend in vegetation management costs is largely being driven by:

- A 50% increase in contractor bid prices on a per mile basis from 2014 to 2017 for proactive tree trimming;[325]
- Over the past four years, the miles of overhead distribution line (feeder-main and laterals) that CenterPoint Houston must maintain with tree trimming activities has increased by an average of 171 miles per year;[326]

[321] *Id.* at 212:13-14.

[322] CEHE Ex. 31. at 25:11-26:1 (Pryor Rebuttal).

[323] *Id.* at 26:1.

[324] OPUC Exceptions at 8.

[325] CEHE Ex. 31 at 24:3-4 (Pryor Rebuttal).

[326] *Id* at 24:4-6.

- CenterPoint Houston has increased the spend every year for the past four years on reactive tree trimming to address customer outages by spot tree trimming between proactive cycles;[327] and
- Vegetation growth driven by an increase in rainfall for the past several years has increased the Company's required tree trimming activities.[328]

With more miles of distribution line to maintain, heavier rainfall, and ever-increasing contractor prices, the Company's costs associated with tree trimming have increased and will continue to trend upward.[329]

OPUC also misrepresents the 2019 cost data confirming the continuing upward trend in vegetation management expenses that CenterPoint Houston is experiencing. Specifically, OPUC attempts to discredit the PFD's findings by arguing that CenterPoint Houston's projected 2019 total vegetation management expenses for distribution system management is lower ($34.033 million) than the Company's actual 2018 test year costs of $35.022 million and thus, the test year costs are abnormal.[330] To the contrary, this information illustrates that the vegetation management expense CenterPoint Houston incurred in 2018 and expects to incur in the future is significantly higher than the amounts incurred in each of the three years that OPUC seeks to include in its three-year average (2015-2017) and is well above the three-year average proposed by Staff.[331]

In sum, the PFD properly concludes that CenterPoint Houston's test year vegetation management expense is reasonable and in line with the costs expected to be incurred in the future. For these reasons, the Commission should adopt the PFD's recommendation and approve CenterPoint Houston's test year O&M expense of $35.022 million for vegetation management activities.

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

A. Weather Normalization

CenterPoint Houston explained in its Exceptions why the Commission should adopt a policy of using a 20-year period to determine normal weather and will not reargue that point here. However, regardless of whether the Commission uses a 10-year or 20-year period to determine

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[327] *Id.* at 24:10-12.

[328] *Id.* at 24:12-13.

[329] *Id.* at 23:20-23 & 25:11-26:6.

[330] OPUC Exceptions at 8.

[331] *See* OPUC Initial Brief at 63; Staff Initial Brief at 50.

normal weather, it should adopt CenterPoint Houston witness J. Stuart McMenamin's methodology for applying weather normalization adjustments, not Staff witness Alicia Maloy's methodology. The PFD correctly found "that Dr. McMenamin sufficiently and credibly rebutted Ms. Maloy's specific allegations of error and demonstrated that his models incorporate strong AMS data and are based on sound weather normalization methodologies."[332]

Dr. McMenamin used four years of detailed AMS data to determine customers' likely response to changes in weather. Those four years of daily AMS data provided 1,400 data points compared to just 120 points provided by Ms. Maloy's 10 years of monthly data. The four years of AMS data used by Dr. McMenamin to determine the effect of abnormal weather on electricity demand produce a "strong stable picture of how weather works in recent years."[333] The only other weather normalization witness, Karl Nalepa for OPUC, testified that Dr. McMenamin's regression models (using the four years of AMS data) "are quite detailed and rely on data obtained from [the Company's] fully deployed advanced meter systems that have provided actual customer demand for every 15-minute interval in every day of every month."[334] In contrast, the 10 years of billing cycle data used by Ms. Maloy produce results that make it hard to see much of a relationship at all between abnormal temperature and electricity sales.[335] For example, Ms. Maloy's 10 data points for the month of May (one point per year) suggest that the two years with the least number of cooling degrees have the largest level of electricity use—a result that does not make sense.[336]

Staff also criticizes Dr. McMenamin for including test year data in his regression analysis.[337] Once again, however, determining normal weather is a distinct and independent step from estimating weather effects on the test year—the purpose of the regression analysis.[338] Ms. Maloy concedes that the entire point of the regression analysis is that "you're trying to remove the impacts of weather *from the test year*."[339] No data could be more relevant regarding customer reaction to abnormal weather *in the test year* than data regarding electric demand *in the test year*. Ms. Maloy eventually acknowledged that more recent years (the test year being the most recent of

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332 PFD at 320.

333 CEHE Ex. 44 at 6:14 (Figure SM-R2) & 23:10-11 (McMenamin Rebuttal).

334 OPUC Ex. 5 at 41:12-14 (Nalepa Direct).

335 CEHE Ex. 44 at 17:7–18:15 (McMenamin Rebuttal).

336 *See id.*

337 Staff Exceptions at 13-14; Staff Initial Brief at 57; Staff Ex. 5A at 22:13-18 (Maloy Direct).

338 CEHE Ex. 44 at 23:1-24:18 (McMenamin Rebuttal).

339 Staff Initial Brief at 57; Tr. at 887:15-16 (Maloy Cross) (Jun. 26, 2019).

all) provide a more accurate read on how customers react to weather changes.[340] Dr. McMenamin properly *excluded* the test year in determining normal weather, but properly *included* it to determine how customers *in the test year* reacted to variances from normal weather *in the test year*.[341]

Finally, Staff criticizes Dr. McMenamin for including in his regression analysis some variables that Ms. Maloy argues are not statistically significant at the 95% confidence level.[342] However, Ms. Maloy has previously testified that the inclusion of variables with a confidence level below 95% may still be valid to include in regression models if the variable makes theoretical sense.[343] Dr. McMenamin testified that his variables do make theoretical sense (day of week effects, holidays) and would not have changed his results significantly if removed.[344] Ms. Maloy offered no such analysis, and the PFD found that Dr. McMenamin's more specific testimony sufficiently overcame Ms. Maloy's "blanket" criticism.[345]

The Commission should uphold the PFD's recommendation to use Dr. McMenamin's weather normalization adjustments regardless of whether it adopts a 10-year or 20-year period to determine normal weather.

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

A. Functionalization

1. Texas Margin Tax Expense and Associated Accounts

The PFD properly adopts Staff's proposed functionalization and allocation of Texas Margin Tax ("TMT") expense as agreed to in rebuttal by CenterPoint Houston.[346] COH alleges that the PFD accepts without explanation an inflated TMT expense number and that the PFD ignores binding precedent.[347] Neither allegation is correct.

The PFD notes testimony by Staff witness Brian T. Murphy, during cross examination by counsel for COH regarding the alleged double counting, that "the $942.4 million he assigned to

[340] Tr. at 891:19-21 (Maloy Cross) (Jun. 26, 2019).

[341] CEHE Ex. 44 at 23:1–24:18 (McMenamin Rebuttal).

[342] Staff Exceptions at 14; Staff Ex. 5A at 23:13–24:18 (Maloy Direct).

[343] Tr. at 876:13-878:25 (Maloy Cross) (Jun. 26, 2019).

[344] CEHE Ex. 44 at 24:19–26:10 (McMenamin Rebuttal).

[345] PFD at 321.

[346] *Id.* at 327-330 & 442 (Finding of Fact Nos. 346 and 347).

[347] COH/HCC Exceptions at 29-30.

retail does not reflect a miscalculation, but rather the correct amount of ERCOT transmission payments CenterPoint Houston seeks to include in its retail rates."[348] Mr. Murphy's direct testimony supports his testimony on cross examination, comparing "the Company's approach, which does not tie to its request, and Staff's approach, which ties to the CEHE's request as shown on page 12 of the Company's Application."[349] The PFD specifically acknowledges and discusses the correctness of Mr. Murphy's math.[350]

The PFD also acknowledges that Mr. Murphy's proposed treatment differs from the treatment in CenterPoint Houston's last rate case, Docket No. 38339.[351] The PFD does not simply ignore that precedent. Instead, the PFD correctly notes that the functionalization and allocation of TMT expense was not a contested issue in Docket No. 38339 and acknowledges Mr. Murphy's explanation in this proceeding that CenterPoint Houston's initial treatment of TMT expenses "conflicted with cost causation principles" and "uplifted a portion of the TMT expense attributable specifically to its provision of retail service to all customers on the ERCOT transmission grid through its TCOS."[352] Accordingly, while acknowledging the different outcome in Docket No. 38339, the PFD properly concludes that the prior outcome "should not control in this case, especially in light of the evidence presented" in this case.[353] The Commission should adopt the PFD's findings of fact on the functionalization and allocation of TMT expense.

B. Class Allocation

1. Class Allocation of Transmission Costs and Distribution Costs

a. CEHE 4CP Allocation versus ERCOT 4CP Allocation

In its Exceptions, TIEC argues that the PFD erred in recommending that CenterPoint Houston bill its transmission customers for distribution costs based on their usage at CenterPoint Houston's system demand peak ("CEHE 4CP").[354] The ALJs also recommended that CenterPoint Houston allocate distribution costs to transmission customers based on the CEHE 4CP, but TIEC did not address the PFD's recommendation on this issue in its Exceptions. The PFD's

[348] PFD at 329.

[349] Staff Ex. 2A at 29:9-11 (Murphy Direct).

[350] PFD at 329-330.

[351] *Id.* at 329.

[352] *Id.* at 330.

[353] *Id.* at 329.

[354] TIEC Exceptions at 18-20.

recommended approach to both bill and allocate distribution costs based on transmission customers usage using the CEHE 4CP is reasonable and should be adopted. TIEC's claims that using the CEHE 4CP will over-complicate billing is not based on any record evidence. To the extent the Commission determines that CenterPoint Houston should bill transmission customers for distribution costs based on usage at the ERCOT 4CP, as TIEC urges, it should still adopt the ALJs' recommendation to allocate these costs based on the CEHE 4CP.

b. 4CP Allocation versus NCP Allocation

In their Exceptions, Texas Competitive Power Advocates argues that the Commission should require the use of the non-coincident peak ("NCP") method to allocate transmission costs to the classes.[355] The PFD appropriately recognizes that the Company's transmission system is designed to serve the maximum load requirement of each individual retail customer at the same time—during the months of June, July, August, and September[356]—not each individual class' maximum load throughout the year.[357] It is reasonable to utilize the 4CP method instead of the NCP method because costs should be allocated to the classes based on their contribution to the Company's summer peak loads.[358] The 4CP component of the Company's proposed allocator accomplishes this goal by isolating class contributions to system peak load during those four months.[359]

2. Municipal Franchise Fees [PO Issue 27]

The Commission should adopt CenterPoint Houston's allocation of municipal franchise fees among customer classes, which is expressly supported by COH as "consistent with cost causation principles."[360] As noted in the Company's initial brief, "[n]o party contests the reasonableness of the *amount* of CenterPoint Houston's municipal franchise fee expenses,"[361] rather TIEC, and TIEC alone, contests the *allocation* of such fees.[362] TIEC witness Jeffry Pollock recommends that municipal franchise fees be allocated among customer classes based not only on

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[355] Texas Competitive Power Advocates Exceptions at 1-3.

[356] PFD at 347 & CEHE Ex. 30 at 3012:14-3013:22 (Troxle Direct).

[357] CEHE Ex. 30 at 3013:7-22 (Troxle Direct).

[358] *Id.*

[359] *Id.*

[360] COH/HCC Initial Brief at 35.

[361] CEHE Initial Brief at 127.

[362] *See* TIEC Exceptions at 20-24; *see also,* Docket No. 38339, TIEC's Initial Post-Hearing Brief at 37-40 (Oct. 22, 2010).

in-city kWh sales, but also based on differences in per kWh franchise fee amounts among those cities.[363] TIEC acknowledges that its witness "made a similar proposal in [CenterPoint Houston's last rate case]" and the Commission adopted CenterPoint Houston's proposal instead.[364] Nevertheless, TIEC asserts that its proposal "is not at odds with the Commission's actual findings in Docket No. 38339."[365] TIEC relies on the absence of any explicit rejection of its proposal in the single finding of fact that addressed the allocation of municipal franchise fees in Docket No. 38339.[366] However, the PFD in that proceeding explicitly rejected TIEC's position,[367] and the Commission's Order on Rehearing adopted not just the ALJs' findings of fact, but also the proposal for decision.[368] More recently, in an Entergy case, both the PFD and Order on Rehearing expressly rejected Mr. Pollock's methodology.[369] Thus, the Commission *has* previously considered and rejected TIEC's proposal and should do so again for the same reasons.

5. Other Cost Allocation Issues

b. Allocation of FERC Account 907-10 Costs

In its Exceptions, COH argues that the PFD errs in allocating FERC Account 907-10 Customer Service Administration and Community Relations costs to the lighting class based on lamp count instead of customer count.[370] Contrary to COH's unsupported assertions, there is nothing "conclusory" about this finding or "extreme" or potentially "harmful" about the result.[371] In fact, the evidence shows, and the PFD recognizes,[372] that some customers, like COH, have a

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363 TIEC Ex. 1 at 20:21-21:9 (Pollock Direct).

364 TIEC Exceptions at 22.

365 *Id.*

366 *Id.* and *see* Docket No. 38339, Order on Rehearing at Finding of Fact 179.

367 Docket No. 38339, PFD at 156-157.

368 Docket No. 38339, Order on Rehearing at Ordering Paragraph No 1.

369 *Application of Entergy Texas, Inc. for Authority to Change Rates, Reconcile Fuel Costs, and Obtain Deferred Accounting Treatment*, Docket No. 39896, PFD at 296 (Jul. 6, 2012) and Order on Rehearing at 30 (Finding of Fact No. 181) (Nov. 1, 2012) ("It is reasonable and consistent with [PURA] that MFF be allocated . . . *without an adjustment for the MFF rate in the municipality in which a given kWh sale occurred.*") (Emphasis added.).

370 COH/HCC Exceptions at 31-32.

371 COH cites no evidence that this allocation causes a safety concern, and CenterPoint Houston is not aware of what harm could be caused by this allocation.

372 PFD at 356.

significant number of lamps[373] and Account 907-10 costs vary depending on the number of lamps a customer uses.[374] The Company's proposed allocation for this account is reasonable.

VIII. REVENUE DISTRIBUTION AND RATE DESIGN [PO Issues 4, 5, 43, 49, 50]

C. Transmission Service Facility Extensions

The PFD rightly rejected TIEC's proposal to require CenterPoint Houston to "refund a portion of a transmission customer's contribution in aid of construction ("CIAC") if the facilities constructed with that CIAC are later used to serve other customers." As noted in its prior briefing, CenterPoint Houston has reviewed TIEC's proposed changes to the Transmission Facility Extension Agreement ("FEA") submitted with its initial brief and has no objection to some of TIEC's proposals, which were adopted in the PFD. But, CenterPoint Houston objects to TIEC's proposal that CenterPoint Houston be required to issue refunds to a customer if that customer later determines to use its facility to serve another separate customer.[375] The Company is unaware of such a situation arising in the past with respect to a CenterPoint Houston-owned transmission facility paid for by a customer through a CIAC except perhaps in a subtractive metering arrangement, where the original customer that paid the CIAC negotiates with the second customer to convey part of its customer premises to that customer. Rather than requiring CenterPoint Houston and a second customer to execute a second transmission FEA for a new facility extension to serve the portion of the premises conveyed to it, a more appropriate solution is for the Company to enter into a subtractive metering arrangement with both customers so that any refund occurs between customers. In short, if a customer has built and owns a facility, any customer that wants to use that facility should negotiate with the customer that built and paid for the facility regarding its use, not CenterPoint Houston.

D. Street Lighting Service

As an initial matter, COH's new claim is that the ALJs "misunderstood" COH's position relating to street lighting service O&M and that COH was merely seeking a different "allocation" of street lighting costs, is demonstrably false. In both COH's initial and reply briefs, COH argued

[373] CEHE Ex. 45 at 17:9-18 (Troxle Rebuttal).

[374] Tr. at 1048:1-19 (Troxle Cross) (Jun. 27, 2019).

[375] TIEC Exceptions at 29-30.

for a $2.73 million disallowance or "exclusion" of street lighting expense from the Company's request.[376] The PFD thus correctly summarizes and analyzes COH's position.

More importantly, the PFD reaches the correct result based on the evidence. The undisputed evidence demonstrates:

- the Company incurred approximately $7.6 million in test-year O&M costs for street lighting;[377]
- CenterPoint Houston has standing work orders for all O&M costs associated with all streetlights in its territory;[378]
- CenterPoint Houston has a warranty on its bulbs, but it only covers luminaire *replacement* not ongoing O&M;[379] and
- ongoing O&M costs associated with LED streetlights include fuse replacement, maintaining the post, conduit replacement, and clamp/connector replacement over its used and useful life to maintain standard performance.[380]

To this end, COH's contention that COH witness Kit Pevoto's testimony was "uncontroverted"[381] is likewise demonstrably false. The Company's case thoroughly rebutted Ms. Pevoto's position, proving that CenterPoint Houston prepared a study for this proceeding to demonstrate the level of street lighting costs associated with all of the different types of lamps in the Company's system.[382] The study assigned to LED street lighting approximately $2.73 million of the Company's total $7.6 million in street lighting O&M costs.[383] However, regardless of what amount of costs were assigned to LED, that does not affect the fact that the Company incurred $7.6 million in street light related O&M during the test year and has requested this amount as part of its cost of service.

In the same way, the Company also rebutted Ms. Pevoto's claim that the Company would have no street lighting O&M at all for 10 years because of a warranty on the bulbs. Company

[376] COH/HCC Initial Brief at 40 ("Therefore, COH/HCC recommends that the Company's O&M expenses related to street lighting be excluded, thereby reducing the Company's street lighting rates by $2.73 million."); COH/HCC Reply Brief at 33 ("Therefore, COH/HCC recommends that the Company's O&M expenses related to street lighting be excluded, thereby reducing the Company's street lighting rates by $2.73 million.").

[377] CEHE Ex. 2 at 2104 (H-I-J and CA Errata – 1, WP – Lighting revenue); CEHE Ex. 45 at 40:16-17 (Troxle Rebuttal); CEHE Ex. 33 at 18:1-20:20 (Sugarek Rebuttal).

[378] CEHE Ex. 33 at 18:18-19 (Sugarek Rebuttal).

[379] Tr. at 232:5-233:6 (Sugarek Cross) (Jun. 24, 2019).

[380] CEHE Ex. 33 at 18:8-12 (Sugarek Rebuttal).

[381] COH/HCC Exceptions at 26.

[382] CEHE Ex. 2, Schedule H-I-J and CA Errata-1, WP-Streetlight Rate Design.

[383] *Id.*

witness Julienne P. Sugarek explained at the hearing that the warranty covers luminaire replacement; it does not cover on-going O&M—including fuse replacement, maintaining the post, conduit replacement, and clamp/conductor replacement.[384]

Finally, COH's suggestion that projected LED savings should offset future LED costs, was also shown to be without merit.[385] The record is clear that savings related to LED lighting took place in the test year and were captured in the Company's cost of service;[386] the test year costs are the *actual* O&M costs the Company incurred during the test year to operate its street lighting system, which currently includes both LED and high pressure sodium bulbs. The costs do not offset one another. The Company's $7.6 million in actual test year street lighting O&M costs should be approved.

IX. RIDERS [PO Issues 4, 5, 43, 51, 52]

A. Rider UEDIT [PO Issue 51]

3. Structure of Rider UEDIT

GCCC's Exceptions demonstrate that GCCC continues to misunderstand the straight-forward structure of the Company's proposal to return unprotected EDIT through Rider UEDIT.[387] The evidence demonstrates that the Company calculated its proposed annual Rider UEDIT refund amount by taking its total unprotected EDIT refund amount, adding interest, and then amortizing that total amount (principal and interest) over a three-year period.[388] Despite GCCC's confusing assertions otherwise, no second year was used. To support its confusing assertions, GCCC relies solely on a CenterPoint Houston discovery response. Yet the response does not say what GCCC purports it says and is entirely irrelevant to Rider UEDIT.

Specifically, GCCC cites the Company's response to COH RFI No. 3-6 (attached both to GCCC witness Lane Kollen's testimony at Attachment N and to this reply for ease of reference). However, neither the RFI nor CenterPoint Houston's response reference *unprotected* EDIT, let alone Rider UEDIT or the Company's proposed amortization period for Rider UEDIT. Rather, COH RFI No. 3-6 asks, and the Company answers, a question related only to *protected* (not

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[384] Tr. at 232:5-233:2 (Sugarek Cross) (Jun. 24, 2019).

[385] COH/HCC Exceptions at 27-28.

[386] Tr. at 237:12-19 (Sugarek Redirect) (Jun. 24, 2019).

[387] GCCC Exceptions at 6.

[388] CEHE Ex. 12 at 74:3-75:7 (Colvin Direct); CEHE Ex. 45 at 44:7-14 (Troxle Rebuttal).

unprotected) EDIT.[389] Protected EDIT must be refunded through the Company's base rates no faster than permitted using the average rate assumption method—it has no connection to Rider UEDIT or its calculation.

In short, the PFD did not need to analyze the Company's response to COH RFI No. 3-6 in the context of this issue because the contents of that discovery response have no relevance to Rider UEDIT, its computation, or its refund period.

4. Amount to Return through Rider UEDIT

GCCC also continues to argue that the Commission should "disallow" $158 million (approximately $200 million when properly grossed up) in EDIT associated solely with transition bonds and system restoration bonds[390] and that the Company failed to meet its burden of proof on this issue. None of GCCC's arguments are correct or appropriate. The settlement agreements at the heart of this issue, to which GCCC is a signatory, are in evidence and fully demonstrate that acceptance of GCCC's position would result in the overturning of prior Commission securitization orders and findings.[391] The evidence is also undisputed that CenterPoint Houston agreed to over $800 million in adjustments in those transition cost and system restoration cost proceedings—all to the benefit of ratepayers—so as to *forever* resolve all future potential ADFIT benefit issues.[392]

GCCC's briefing, however, (including its Exceptions) fails to address or acknowledge these facts.[393] For the sake of brevity in this Reply, the Company notes that CenterPoint Houston's Exceptions and briefing throughout this proceeding thoroughly address the legal error and poor policy that would result if GCCC's position is accepted, and CenterPoint Houston incorporates those arguments herein by reference.[394] GCCC's arguments that the Company failed to meet its burden of proof and that EDIT associated solely with the securitized bonds should be flowed through to ratepayers have no merit.

[389] *See* Attachment A & GCCC Ex. 1 at bates pages 134-135, Attachment N (CenterPoint Houston's Response to COH 03-06).

[390] GCCC Exceptions at 7.

[391] CEHE Ex. 65 (Docket No. 39504, CEHE's Submission of Unopposed Stipulation, Draft Final Order and Testimony Supporting Stipulation); CEHE Ex. 66 (Docket No. 37200, Settlement Agreement).

[392] CEHE Ex. 65 (Docket No. 39504, CEHE's Submission of Unopposed Stipulation, Draft Final Order and Testimony Supporting Stipulation); CEHE Ex. 66, Docket No. 37200, Settlement Agreement at 2-3; Tr. at 802:20-806:3 (Tietjen Cross) (Jun. 26, 2019).

[393] GCCC Exceptions at 7.

[394] CEHE Exceptions at 98-102; CEHE Initial Brief at 136-140; CEHE Reply Brief at 143-146.

B. Merger Savings Rider

GCCC's Exceptions ignore the fact that it is not known for certain what savings or costs to achieve will be realized as a result of the Vectren transaction.[395] Integration activities cost money and take time.[396] The evidence is also clear that CNP's costs to achieve any savings are substantial, currently exceed any near-term estimated savings, and are ongoing.[397] CenterPoint Houston witness Jeffrey S. Myerson's rebuttal testimony sets forth the confidential estimate of CNP's costs to achieve[398] and demonstrates that if the actual costs to achieve the savings attributable to the Vectren acquisition were included in the proposed "Merger Savings Rider," the result for 2019 would be a *surcharge* to customer bills—not a refund.[399] Thus, in recommending that GCCC's suggestion be denied, the PFD properly recognizes both the uncertainty associated with future savings and the inequity of GCCC's proposal because it fails to properly reflect *all* of the impacts of the Vectren acquisition, both cost savings *and* costs necessary to achieve those savings that must be captured and considered.[400]

The PFD also properly recognizes that GCCC asks for a rider that returns "expectations"[401] of savings and not an actual accounting of savings that can be offset by corresponding costs. In other words, GCCC asks the Commission to set up a rider that does not use actual known and measurable data. GCCC then posits an alternative that would reduce the Company's cost of service by a similar "expectation" rather than known and measurable savings. In short, GCCC asks the Commission to ignore traditional ratemaking principles with both its "Merger Savings Rider" and alternative. The PFD correctly rejected those suggestions.

Moreover, the evidence demonstrates that any savings associated with the Vectren acquisition are properly addressed through the protections already in place through the annual Earnings Monitoring Report ("EMR") filing process. Per 16 TAC § 25.73, the Commission uses the EMR as the way to properly monitor a utility's earnings; in fact, the Commission's order approving the EMR filing package in Project No. 39040 states that the "report has been used as a

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[395] CEHE Ex. 47 at 13:14-15, 18:14 (Myerson Rebuttal).

[396] *Id.* at 19:1.

[397] *Id.* at 6:13-17, 19:5-6, 8:20-22.

[398] *Id.* at 13:12-16.

[399] *Id.* at 19:1-9.

[400] CEHE Ex. 35 at 63:4-10 (Colvin Rebuttal).

[401] GCCC Exceptions at 7-8.

tool to review a utility's actual earnings for an historical period."[402] The EMR provides information necessary to determine if a utility is earning above its authorized return, which means at *any* point in time the Company can be compelled to file a base rate case if the Commission believes it is over-earning.[403] It also means that, if the Company is earning above its authorized return, it will be prohibited from filing a DCRF during the following year.[404] Finally, under the recently implemented 16 TAC § 25.246, CenterPoint Houston will be required to file a base rate case approximately four years following the implementation of rates in this case, at which point any potential costs and savings will be captured through a comprehensive rate case filing.[405] GCCC's proposed "Merger Savings Rider" and alternative should be rejected.

X. BASELINES FOR COST-RECOVERY FACTORS [PO Issues 4, 5, 43, 53]

A. TIEC's Support for Exclusive Cost Recovery Through the TCRF

In its Exceptions, TIEC attacks the PFD's finding that the Company's Rider TCRF is intended to capture incremental differences in transmission costs, arguing that *all* transmission costs should be recovered through the TCRF and that no costs should be recovered through base rates. This proposal defies the clear language of 16 TAC § 25.193[406] and was not supported by any party to this proceeding other than TIEC.

The record clearly shows that the TCRF is intended to capture the "the amount of wholesale transmission cost changes approved or allowed by the commission to the extent that such costs vary from the transmission service cost utilized to fix the base rates of the DSP"—i.e., the incremental differences in costs.[407] It was never intended to capture all transmission costs.[408] As the ALJs explain, CenterPoint Houston's approach is entirely consistent with TIEC's own expert's definition of the TCRF mechanism:[409]

> The TCRF mechanism was designed pursuant to 16 T.A.C. § 25.193 that allows CenterPoint to recover changes in wholesale transmission costs above the level of such costs that are already being recovered in the [Transmission Service charge].

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402 *Project to Revise Earnings Monitoring Report Forms for Electric Utilities,* Docket No. 39040, Order at 31 (Jan. 7, 2012).

403 CEHE Ex. 35 at 63:1-3 (Colvin Rebuttal).

404 CEHE Ex. 47 at 19:10-14 (Myerson Rebuttal).

405 *Id.*

406 TIEC Exceptions at 24-26 & TIEC Initial Brief at 71-74.

407 CEHE Ex. 45 at 20:2-4 (quoting 16 TAC § 25.193(b)) (Troxle Rebuttal).

408 *Id.* at 20:5-6.

409 PFD at 403; TIEC Ex. 1 at 22:17-21 (Pollock Direct).

> Thus, the combination of the Transmission Service charge and TCRF provides the revenues necessary to recover all wholesale transmission costs allocated to CenterPoint.

The Company's approach is also consistent with the requirements in the Commission's TDU RFP instructions[410] and the RFP sample forms, which are clearly designed to reflect a transmission charge in base rates.[411] Regardless, this is clearly not the appropriate venue for TIEC to re-litigate arguments regarding the TCRF rule that this Commission already rejected in the TCRF rulemaking project.[412] TIEC's attempts to re-characterize and re-interpret Staff witness William B. Abbott's testimony and Staff's prior positions on this issue for the Commission are unconvincing. Staff explicitly rejected TIEC's approach in this proceeding.[413] TIEC does not cite a single litigated proceeding in which its proposed treatment of the TCRF mechanism was applied.

Furthermore, while TIEC complains about the *potential* impacts of load growth associated with the current TCRF rule that could result in over-recovery of these costs, it does not even acknowledge the *other* impacts of load growth that drive *down* recovery of these costs,[414] like increased O&M, increased investments in its system, changes in weather, economic conditions, or tax rates, increased customer attribution, or energy efficiency.[415] This is in fact precisely why the TCRF rule is constructed the way it is. There is no guarantee CenterPoint Houston will experience year-after-year load growth, and CenterPoint Houston bears the risk of both under-and over-recovery under the TCRF incremental cost recovery method. And regardless, TIEC's concerns are mitigated by 16 TAC § 25.246, which requires all investor-owned electric utilities to file a rate case every four years,[416] at which point the Company's entire cost of service will be subject to review.[417] Alternatively, the Commission retains the authority to require a rate case at any time.[418]

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[410] CEHE Ex. 45 at 20:6-13 (Troxle Rebuttal) (citing page 59 of the Instructions, which refers to the allocation of the functional requirements, and on page 63, which refers to the revenue requirements by the function (Transmission is one of the functions)).

[411] *Id.* at 20:14-21:3.

[412] *See, e.g., Rulemaking Proceeding to Amend PUC Subst. Rule §25.193, Relating to Distribution Service Provider Transmission Cost Recovery Factors (TCRF),* Project No. 37909, Order Adopting Amendment to § 25.193 as Approved at the September 29, 2010 Open Meeting at 18 (Oct. 4, 2010).

[413] *See, e.g.,* Staff Ex. 7B at 27:11-19 (Abbott Cross Rebuttal).

[414] CEHE Ex. 45 at 21:10-14 (Troxle Rebuttal).

[415] *Id.* at 21:14-16.

[416] *Id.* at 22:3-5.

[417] *Id.* at 22:5-7.

[418] *Id.* at 22:8-9.

The PFD appropriately recognizes that there is no justification to deviate from this Commission's rules.[419]

XI. CONCLUSION

The exceptions by Staff and Intervenors addressed above are each without merit and should be rejected in their entirety. CenterPoint Houston respectfully requests that the Commission grant the Company's Exceptions and enter an Order consistent therewith. In this regard, CenterPoint Houston further requests that it be allowed to work with Staff to align the Commission's final decision with the approved schedules to ensure that the final revenue requirement is accurate and gives full effect to the Commission's decision. Finally, CenterPoint Houston requests that the Commission grant the Company such further legal, equitable, and necessary relief to which it may be entitled.

[419] *Id.* at 22:10-12 & PFD at 402-403.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that on this 24th day of October 2019, a true and correct copy of the foregoing document was served on all parties of record in accordance with 16 Tex. Admin. Code § 22.74.

Andrea Moore Stover

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