



Control Number: 49421



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APPLICATION OF CENTERPOINT
ENERGY HOUSTON ELECTRIC, LLC
FOR AUTHORITY TO CHANGE
RATES

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BEFORE THE STATE OFFICE
OF
ADMINISTRATIVE HEARINGS

**OFFICE OF PUBLIC UTILITY COUNSEL'S
REPLY TO EXCEPTIONS TO THE PROPOSAL FOR DECISION**

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October 24, 2019

742

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**OFFICE OF PUBLIC UTILITY COUNSEL’S
REPLY TO EXCEPTIONS TO THE PROPOSAL FOR DECISION**

The Office of Public Utility Counsel (“OPUC”), representing the interests of residential and small commercial consumers in Texas, respectfully submits these replies to exceptions to the proposal for decision (“PFD”) issued by the Administrative Law Judges (“ALJs”) on September 16, 2019. OPUC replies to certain exceptions filed by CenterPoint Energy Houston Electric, LLC (“CenterPoint” or the “Company”) and Texas Industrial Energy Consumers (“TIEC”), and respectfully shows the following:¹

- 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**
 - d. Capital Project Oversight and Budget Estimation**
 - ii. La Marque Substation**

CenterPoint excepts to the PFD’s disallowance of a portion of the costs for the La Marque Substation.² However, the Company’s position is premised on the incorrect conclusion that the PFD’s decision was based solely on the difference between the estimated cost of the substation of \$1,446,000 and the actual cost of the substation of \$2,773,369.³ As discussed in OPUC’s initial brief, OPUC recommended disallowing a portion of the cost not based solely on the 92% cost

¹ The outline and headings of this reply to exceptions correspond to those in the PFD. OPUC’s silence on any issue addressed in the parties’ exceptions should not be construed as an agreement with those positions.

² CenterPoint Exceptions at 24-25.

³ *Id.* at 24.

overrun, but rather, on the Company's acknowledgment that the significant additional cost was due to construction errors.⁴ In particular, the Company's explanation for the cost overrun at the La Marque Substation was that "Tower design and location changed during detailed engineering phase which led to some material errors. One angle structure had to be removed and replaced."⁵ The existence of construction errors for the La Marque substation raises the issue of whether the costs incurred for the project were prudent.

CenterPoint has the burden of proof to demonstrate that its requested costs for capital investments, such as the La Marque Substation, are prudent.⁶ In its exceptions, the Company states that the substation is used and useful and that the scope of the project grew after the original estimate.⁷ However, the issue is not whether the substation is used and useful, but rather whether the entirety of its cost is prudent. The evidentiary record demonstrates that a portion of the cost overrun was due to construction errors. In discussing the evidence, the ALJs concluded that CenterPoint failed to prove that: (1) the construction errors were not caused by imprudence, and (2) the amount of the cost increase was due to the need to build seven structures instead of four, rather than imprudence.⁸ Thus, CenterPoint's exceptions on this issue are based on an incorrect premise, i.e., that the disallowance was based solely on the cost difference. For the reasons stated in the PFD, CenterPoint failed to meet its burden of proof as to the prudence of the entirety of the La Marque Substation costs. Accordingly, the Commission should reject CenterPoint's exceptions and adopt the ALJs' recommended disallowance.

3. Capital Project Accounting

d. Capital Project S/101318/CG/Tools

OPUC notes that CenterPoint's exceptions correctly state that OPUC withdrew its recommendation regarding the capitalization of substation tools identified as Capital Project S/101318/CG/Tools.⁹

⁴ OPUC Initial Brief at 3-4.

⁵ OPUC Ex. 5 (Nalepa Direct) at Att. KJN-3 at 36-37 (Response to PUC RFI No. 06-24).

⁶ PURA § 36.006.

⁷ CenterPoint Exceptions at 24.

⁸ PFD at 30.

⁹ CenterPoint Exceptions at 26; OPUC Initial Brief at 6 n.28.

4. Changes in Capitalization Policy

The PFD recommended a disallowance for certain items that were expensed in CenterPoint's last base rate case, but later capitalized by the Company. As stated in the PFD, the Company's capitalization policy changed for luminaires in 2014, microprocessor control devices in 2017, program assessment costs (underground cable life extension) in 2013, and certain overhead construction costs in 2014.¹⁰ In its exceptions, CenterPoint contends that the evidentiary record does not support the PFD's conclusion that the Company changed its capitalization policy regarding the Underground Residential Distribution ("URD") Cable Assessment and Life Extension Program ("CLEP").¹¹ In particular, CenterPoint states that because the URD CLEP was implemented in 2013, after the Company's rate case in Docket No. 38339 in 2009, the capitalization policy for that program did not change between its rate cases.¹² CenterPoint appears to be raising this issue for the first time in its exceptions, and thus, the parties have not previously had the opportunity to provide evidence or cross-examine the Company's witnesses on the issue. Nevertheless, for the reasons discussed below, the evidentiary record supports the PFD's recommended disallowance, and it should be adopted.

The URD CLEP is included in the category described as "program assessment costs (underground cable life extension)" by CenterPoint witness Ms. Kristie L. Colvin. In discussing the capitalization policy changes since the Company's last rate case, Ms. Colvin states in her direct testimony that "[a]s a result of the Company's annual review, **since Docket No. 38339**, the Company has made changes to its capitalization policy for luminaires, microprocessor control devices, **program assessment costs (underground cable life extension)** and certain construction overhead costs."¹³ Thus, as indicated in Ms. Colvin's testimony, the Company changed its capitalization policy for program assessment costs after its last rate case. In explaining the change, Ms. Colvin states that the Federal Energy Regulatory Commission ("FERC") issued guidance in 2009 clarifying that underground cable assessment costs may be capitalized if they meet certain

¹⁰ PFD at 50-51.

¹¹ CenterPoint Exceptions at 30.

¹² *Id.*

¹³ CenterPoint Ex. 12 (Colvin Direct) at 92-93 (emphasis added).

criteria.¹⁴ She states that the Company updated its capitalization policy in 2013 to be consistent with the FERC guidance.¹⁵ Ms. Colvin notes that, pursuant to the updated capitalization policy, CenterPoint implemented an underground cable assessment program in 2013 (i.e., the URD CLEP), but she does not address similar costs that would have been expensed prior to the capitalization policy change.

The evidentiary record also reflects that, prior to implementing the specific URD CLEP, the Company had practices for assessing and replacing its URD infrastructure. In particular, the direct testimony of CenterPoint witness Mr. Randal M. Pryor describes the Company's prior practice. Mr. Pryor states that "Historically, the Company replaced an average of 35 URD loops annually. The replacement criterion was based on: 1) the loop's age, 2) the loop's reliability performance, and 3) whether the loop was served by large step-down transformers."¹⁶ While the URD CLEP is a specific program to systematically address replacement of CenterPoint's URD infrastructure, it is clear from Mr. Pryor's testimony that the Company had measures in place prior to 2013 to assess and replace its URD infrastructure. Thus, contrary to CenterPoint's exceptions, the evidentiary record supports the ALJs' recommended disallowance due to CenterPoint's change in capitalization policy for its underground program assessment costs. Accordingly, for the reasons discussed in the PFD, the ALJs' recommended disallowance should be adopted.

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

2. Hurricane Harvey Regulatory Asset

CenterPoint excepts to the PFD's conclusion that the requested Hurricane Harvey regulatory asset should not include carrying costs.¹⁷ However, for the reasons discussed in the PFD, the ALJs reasonably concluded that there was a lack of evidence supporting the carrying costs and a lack of authority to recover those costs.¹⁸ Therefore, the ALJs recommended that the Company's request for carrying costs should be rejected. OPUC supports the PFD's discussion of this issue and advocates that the Commission adopt it. However, if the Commission does not adopt

¹⁴ *Id.* at 104.

¹⁵ *Id.*

¹⁶ CenterPoint Ex. 7 (Pryor Direct) at 36.

¹⁷ CenterPoint Exceptions at 36-38.

¹⁸ PFD at 76.

the PFD’s recommendation, CenterPoint’s calculation of the carrying costs must be corrected. As discussed in OPUC’s initial brief, CenterPoint incorrectly applied a monthly “compound interest” formula to determine the costs, which would result in an over-recovery of the costs.¹⁹ Thus, if CenterPoint is permitted to recover carrying costs on the Hurricane Harvey regulatory asset, an annual “simple interest” formula should be used to calculate the carrying costs as recommended by OPUC witness Mr. Karl Nalepa.²⁰ This correction would result in a reduction of \$0.126 million to the Company’s requested amount.²¹

4. Texas Margin Tax Regulatory Asset

In its exceptions, CenterPoint states that while it disagrees with the PFD’s proposal to disallow the Company’s requested \$19.6 million Texas Margin Tax (“TMT”) regulatory asset, the Company is not filing exceptions on the issue.²² Instead, the Company states that if the PFD is adopted on this issue, CenterPoint “should be allowed to revert to its former, uncontested methodology.”²³ The Company’s request should be denied. As an initial matter, the Company raised this proposal for the first time in its rebuttal testimony.²⁴ As a result, there has not been a thorough opportunity to vet the proposal in this rate case, and it is not clear that the evidentiary record supports CenterPoint’s requested findings of fact.

Moreover, CenterPoint’s statement that its current methodology is uncontested is not accurate. In this proceeding, the Company asserted that its current practice of booking a TMT regulatory asset was approved in Docket No. 29526.²⁵ However, as discussed by OPUC, Gulf Coast Coalition of Cities (“GCCC”), and Commission Staff, Docket No. 29526 does not apply because it dealt with stranded costs and other true-up balances under PURA § 39.262 related to the transition to competition, and the Commission’s order was limited to those circumstances.²⁶ The ALJs agreed, concluding that Docket No. 29526 did not approve CenterPoint’s proposed TMT

¹⁹ OPUC Initial Brief at 23 (citing OPUC Ex. 5 (Nalepa Direct) at 21).

²⁰ *Id.*

²¹ *Id.*

²² CenterPoint Exceptions at 41.

²³ *Id.*

²⁴ *See* CenterPoint Ex. 35 (Colvin Rebuttal) at 33-34.

²⁵ CEHE Ex. 12 (Colvin Direct) at 39-40.

²⁶ OPUC Initial Brief at 26-27; GCCC Ex. 1 (Kollen Direct) at 32; Commission Staff Initial Brief at 19-21.

regulatory asset and was “readily distinguishable from the issue here.”²⁷ In addition, as noted by OPUC, GCCC, and Commission Staff, CenterPoint did not request a TMT regulatory asset in rate base in its last rate case in Docket No. 38339.²⁸ Thus, CenterPoint is seeking approval for the first time in this case to approve the establishment of a TMT regulatory asset. Contrary to its exceptions, the Company’s authority to do so was contested in this proceeding, and the evidentiary record does not support its request to continue this practice. Accordingly, CenterPoint’s request should be denied, and the PFD’s recommendation should be adopted.

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

B. Labor Expenses

2. Incentive Compensation

CenterPoint excepts to the PFD’s recommendation to disallow recovery of financially based incentive compensation.²⁹ CenterPoint’s primary position is that the Commission should reverse course and change its longstanding precedent that financially based incentive compensation is not recoverable from ratepayers. However, the Company’s exceptions simply repeat the same arguments that were thoroughly discussed and properly rejected by the ALJs in the PFD. Accordingly, OPUC relies on its prior briefing and testimony on this issue, as well as the ALJs’ analysis in the PFD. As the PFD states, the Commission’s precedent on incentive compensation is “well-established and unambiguous.”³⁰ The ALJs specifically “recognize[d] the Commission’s long-standing precedent to disallow financially-based incentive compensation costs because: (1) those costs are not considered to be reasonable and necessary to provide service to the public, and (2) they provide more immediate benefits to shareholders, rather than ratepayers.”³¹ For the reasons discussed in the PFD, the basis for this precedent has not changed. Accordingly, CenterPoint’s exceptions are without merit and should be rejected.

²⁷ PFD at 100.

²⁸ OPUC Initial Brief at 26-27; GCCC Initial Brief at 17-18; Commission Staff Initial Brief at 20-21.

²⁹ CenterPoint Exceptions at 79-85.

³⁰ PFD at 243.

³¹ *Id.* at 243-44.

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

B. Class Allocation

2. Municipal Franchise Fees [PO Issue 27]

TIEC excepts to the PFD's rejection of its proposal to change how the Commission allocates municipal franchise fees ("MFFs").³² In particular, TIEC proposes that in-city kilowatt-hour ("kWh") sales be weighted to reflect the different MFF rates charged by the various cities in CenterPoint's service area. However, for the reasons discussed in the PFD and below, TIEC's exceptions should be rejected and the PFD's recommendation should be adopted.

First, as the PFD notes, the Company's proposed allocation of MFFs is reasonable and consistent with Commission precedent.³³ In CenterPoint's last rate case in Docket No. 38339, the Commission found that "CenterPoint's allocation of municipal franchise fees to the customer classes based upon in-city kilowatt-hour (kWh) sales and collection of the fees from all customers within the customer class is reasonable and consistent with Commission precedent."³⁴ No party disputes that CenterPoint followed this precedent in the current proceeding. In its exceptions, TIEC contends that its proposal "is consistent with, but improves upon, the allocation methodology adopted in Docket No. 38339."³⁵ However, TIEC witness Mr. Jeffrey Pollock made the same proposal regarding allocation of MFFs in that case, and the Commission rejected his proposal.³⁶ Thus, TIEC's proposal is not consistent with Commission precedent.

Additionally, in its exceptions, TIEC continues to inaccurately contend that "no party has disputed that Mr. Pollock's allocation better reflects each class's contribution to [CenterPoint's] MFF expense."³⁷ However, as OPUC previously noted in its reply brief, OPUC does dispute this point.³⁸ Mr. Pollock made a similar MFF allocation proposal in Entergy Texas Inc.'s ("ETI") rate

³² TIEC Exceptions at 20.

³³ PFD at 350.

³⁴ *Application of CenterPoint Energy Houston Electric, LLC for Authority to Change Rates*, Docket No. 38339, Order on Rehearing at Finding of Fact ("FOF") 179 (June 23, 2011).

³⁵ TIEC Exceptions at 21.

³⁶ OPUC Ex. 7 (Nalepa Cross-Rebuttal) at 8-9.

³⁷ TIEC Exceptions at 22.

³⁸ OPUC Reply Brief at 29.

case in Docket No. 39896 that was also rejected by the Commission.³⁹ In that case, the Commission's order included specific findings reflecting that MFFs should be charged to all customers in ETI's service area, regardless of geographic location. In particular, the Commission made the following findings of fact:

179. ETI is an integrated utility system. ETI's facilities located within municipal limits benefit all customers, whether the customers are located inside or outside of the municipal limits.
180. Because all customers benefit from ETI's rental of municipal right-of-way, municipal franchise fees should be charged to all customers in ETI's service area, regardless of geographic location.
181. It is reasonable and consistent with the Public Utility Regulatory Act (PURA) § 33.008(b) that MFF be allocated to each customer class on the basis of in-city kilowatt hour (kWh) sales, without an adjustment for the MFF rate in the municipality in which a given kWh sale occurred.⁴⁰

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

There are also other policy reasons that support the PFD's recommendation to adopt CenterPoint's treatment of MFFs. In considering rate design, it is also important to consider simplicity and consistency.⁴¹ The Company's proposal serves both of these goals because it applies a uniform policy to all customers and maintains the Commission's historical practice. Notably, TIEC's proposal would not promote the goal of simplicity. As shown in Exhibits JP-3, JP-5 and JP-6 to Mr. Pollock's direct testimony, there are 93 separate MFF rates that he weights for each of the Company's seven customer classes to develop his proposed allocation factors.⁴² Deriving a city-by-city allocation in this manner introduces unnecessary complexity in setting the

³⁹ *Id.* at 33 (citing OPUC Ex. 7 (Nalepa Cross-Rebuttal) at 9-10, 14; *Application of Entergy Texas, Inc. for Authority to Change Rates, Reconcile Fuel Costs, and Obtain Deferred Accounting Treatment*, Docket No. 39896, Order on Rehearing at FOFs 178-81 (Nov. 2, 2012)).

⁴⁰ Docket No. 39896, Order on Rehearing at FOFs 178-81.

⁴¹ OPUC Ex. 7 (Nalepa Cross-Rebuttal) at 10-11.

⁴² TIEC Ex. 1 (Pollock Direct) at JP-3, JP-5 & JP-6.

Company's rates. Further, as discussed above, the Company's proposal follows the Commission's longstanding treatment of MFFs, which promotes consistency. Accordingly, the ALJs' recommendation to adopt the Company's proposed allocation of MFFs is reasonable, consistent with Commission precedent, and should be adopted in this case.

CONCLUSION

For the reasons stated herein and in its post-hearing briefing and the testimonies of its witnesses, OPUC respectfully requests that the Commission adopt OPUC's recommendations on the issues presented in this case, including those addressed in OPUC's exceptions to the PFD and in these replies to exceptions, and incorporate them into the final order. OPUC further asks to be granted any other relief to which it may be entitled.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing document was served on all parties of record in this proceeding on this 24th day of October 2019 by facsimile, electronic mail, and/or first class, U.S. Mail.



Cassandra Quinn