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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
BRIEF IN RESPONSE TO THE NOVEMBER 15, 2019 BRIEFING ORDER

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The first question posed by the Commission is whether replacing CenterPoint Energy Houston Electric, LLC's ("CenterPoint Houston" or the "Company") existing capital structure of 55% debt and 45% equity with a new, more debt-laden capital structure will necessitate noncompliance with a decision to impose dividend restrictions on the Company. The answer to this question is unequivocally, "Yes." This is because:

- the restrictions on dividends in excess of net income will prevent CenterPoint Houston from distributing equity to CenterPoint Energy, Inc. ("CNP") in order to move to a 60% debt and 40% equity ("60/40") capital structure because that distribution will exceed the Company's expected annual net income;[1]
- this means that equity will be trapped at CenterPoint Houston, but—because rates will have been set using a 60/40 capital structure—shareholders will have no chance to earn an equity return on these dollars;[2]
- trapping this equity would deny the Company the opportunity to earn its authorized return on all of its equity, which is contrary to *Bluefield* and *Hope*;[3]
- Consequently, while PURA and the Commission's rules do not expressly require CenterPoint Houston to make its actual capital structure match the capital structure the Commission uses to set rates, an order imposing both the dividend restrictions and a 40% equity ratio would necessarily violate PURA,[4] and both the United States Constitution

[1] By way of example, the Company's net income in 2018 was $336 million.

[2] *See* CEHE Ex. 43 at 43:12-17 (McRae Rebuttal) (explaining that CenterPoint Houston would recapitalize to a 60/40 capital structure, if approved by the Commission). Increasing the debt component of CenterPoint Houston's capital structure to 60% will require the Company to dividend approximately $900 million in equity to CNP to achieve the capital structure if ordered by the Commission by year end.

[3] Long-established principles of ratemaking require that the return to an equity owner should be reasonably sufficient to assure confidence in the financial soundness of the utility, to maintain and support the utility's credit, and to attract the capital necessary for the proper discharge of the utility's public duties. The return must also be commensurate with returns on investment in other enterprises having comparable risks. *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).

[4] PURA Section 36.003 ("Just and Reasonable Rates"); Section 36.051 ("Establishing Overall Revenues"); Section 36.052 ("Establishing Reasonable Return"); and Section 36.053 ("Components of Invested Capital").

(Fifth Amendment) and the Texas Constitution (Article I, Section 17) prohibitions against takings of property without just compensation.[5]

A second consequence of increasing the Company's debt leverage and restricting CenterPoint Houston's ability to issue dividends means that investors, who are funding this equity, face increased risk, which, in turn, increases the required return on equity ("ROE") well above 9.25%. This is evidenced by the fact that investors devalued CenterPoint Houston's implied market capitalization by 26% over a two-day period during and following the Commission's November 14th Open Meeting discussion of a capital structure and a ROE that is clearly out of line with the 9.68% national average ROE for electric utilities[6] and the average 49.91% equity ratio for delivery-only electric utilities for calendar year 2018, which is the test year in this case.[7] Moreover, just last week, Moody's recognized the additional risk associated with the Open Meeting discussion on capital structure and ROE when it placed the ratings of CenterPoint Houston on review for downgrade; an action that moves the Company ever closer to a credit rating downgrade irrespective of whether dividend restrictions are imposed and increases the cost of debt that customers will pay over the life of any future bond issuances.[8] It is also noteworthy that while parties often point to the Distribution Cost Recovery Factor ("DCRF") and Transmission Cost of Service ("TCOS") mechanisms as reducing utility risk, the existence of those mechanisms did not prevent Moody's from placing the ratings of CenterPoint Houston on review for a downgrade following the Commission's discussion of a 60/40 capital structure and 9.25% ROE.

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[5] U.S. Const. amend. V; "No person ... shall be deprived of life, liberty, or property, without due process of law; nor shall private property be taken for public use, without just compensation." Tex. Const. art. I, § 17; *Chicago, Burlington, & Quincy Railroad Co. v. City of Chicago,* 166 U.S. 226 (1897) (Holding that the takings clause of the Fifth Amendment is incorporated into the Due Process Clause of the Fourteenth Amendment and thus applicable to the states.); *Bluefield,* 262 U.S. at 683 (Holding that rate-setting by a utility commission is state action that must comply with the takings clause of the Fifth Amendment or the action is unconstitutional and void). Here, an order that sets a rate of return based on a 40% equity capital structure yet precludes CenterPoint Houston from issuing dividends to match its actual capital structure with the Commission-approved capital structure would be confiscatory because the trapped equity will only earn the cost of debt. Thus, if the Commission adopts such an order, it will deprive CenterPoint Houston of the ability to recover that cost of capital and just compensation required by the U.S. and Texas Constitutions.

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

[7] *See* CEHE Ex. 27 at 2854:10-2856:4 (McRae Direct), cited excerpt included as Attachment A to this brief; *See also* CEHE Ex. 42 at 16:7-8, 26:18-20 & Exh. R-RBH-7 (Hevert Rebuttal), which shows that the average equity ratio of the 24 holding companies in the proxy group was 53.25% over the last eight calendar quarters. Further, the capital structures of the utility operating companies encompassed within those 24 holding companies reflect an average equity ratio during that same time period of 53.13%. Both of those percentages are considerably higher than the 50% equity ratio requested by CenterPoint Houston in this case.

[8] *See* Ex. 48 at 53-57, Exh. R-EL-6 & CEHE Ex. 48a at Confidential Exh. R-EL-5 (Lapson Rebuttal).

Third, the evidence further shows that a 9.25% ROE for CenterPoint Houston does not satisfy the requisite legal standard and there is no compelling evidence in the record to support a conclusion that CenterPoint Houston should be considered dramatically less risky than other comparable utilities. This evidence establishes that a 9.25% ROE would be:

- materially lower than the ROEs approved by the Commission for every other electric utility in the State of Texas;[9]
- seventy-five basis points below the 10% ROE found reasonable by the Commission in the Company's last rate case;[10]
- far below the 9.68% national average ROE for electric utilities;[11] and
- at the lower end of the range the PFD found to be reasonable, which is between 9% and 10%.[12]

The evidence further shows that a 9.25% ROE, when paired with a 60/40 capital structure, would *increase* the risk of CenterPoint Houston.[13] As a result, a 9.25% ROE is woefully inadequate and does not satisfy the standard set forth in *Bluefield* and *Hope*. Moreover, it is irreconcilable to conclude that a capital structure and ROE that differ so materially from what is currently in place for CenterPoint Houston will preserve the Company's financial integrity, maintain its credit rating, and allow the utility to attract capital to support its operations and investment requirements as required under the law, particularly in light of the financial stress caused by the cash flow loss resulting from the Tax Cuts and Jobs Act of 2018 ("TCJA").

To be clear, CenterPoint Houston's cash flow will be reduced by approximately $100 million from current rates as a result of the Commission's tentative decisions in this case. Of this amount, a change in CenterPoint Houston's existing capital structure and ROE to a 60/40 capital structure and a 9.25% ROE alone will reduce CenterPoint Houston's annual cash flow by approximately $40 million (after tax). This makes the Company riskier because it increases debt and decreases the Funds from Operations ("FFO") available to finance CenterPoint Houston's operational and capital requirements.

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9 *See* CEHE Ex. 42 at Exh. R-RBH-8 (Hevert Rebuttal).

10 *Application of CenterPoint Electric Delivery Company, LLC for Authority to Change Rates,* Docket No. 38339, Order on Rehearing at Findings of Fact Nos. 70A–73A (Jun. 23, 2011).

11 *See* CEHE Ex. 42 at 16:7-8 (Hevert Rebuttal).

12 Proposal for Decision at 170 (PFD).

13 *See* CEHE Ex. 42 at 175:1-15 (Hevert Rebuttal) (showing that parties' lower equity ratios result in significantly lower interest coverage ratios).

For all these reasons, a 60/40 capital structure and 9.25% ROE is fundamentally at odds with an order that also imposes dividend restrictions. This conflict can only be resolved by: (1) increasing CenterPoint Houston's equity ratio, which will allow equity to be injected *into* the Company (or at least avoiding a withdrawal by staying with the currently authorized 45% equity ratio) and (2) adopting a ROE that does not materially differ from those approved for comparable utilities.

I. SOUND FINANCIAL METRICS ARE ESSENTIAL TO THE PROVISION OF ELECTRIC UTILITY SERVICE

Understanding the impact of the Commission's decisions on capital structure, ROE and a dividend restriction begins with the undisputed record evidence that CenterPoint Houston's business does not currently create enough income to fund the transmission and distribution ("T&D") system's capital investment needs.[14] This is not uncommon in the electric industry, but is particularly true of CenterPoint Houston because of its high customer growth and corresponding need for substantial capital investment.[15] Consequently, in order to fund its operational and capital needs, CenterPoint Houston must access the debt and equity markets, either taking out loans or issuing new shares of CNP stock (or a combination of the two).[16] This is evidenced by the fact that from January 2014 to March 2019, CNP has provided CenterPoint Houston with approximately $455 million in *net* equity to fund necessary capital investment.[17] Consequently, CNP has supplied more equity to CenterPoint Houston than CenterPoint Houston has paid to CNP in dividends.[18]

The cost to access the debt and equity markets is determined, in large part, by CenterPoint Houston's financial metrics and credit rating, which are primarily dictated by debt levels and FFO.[19] In this respect, it is essential to understand that a utility's financial metrics depend on both its ROE and its capital structure—they do not each exist in a vacuum.[20] As the Commission has previously found, there is a "close correlation" between ROE and capital structure that requires an upward adjustment to ROE to account for the "potential rating uncertainty due to higher debt based

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[14] CEHE Ex. 27 at 2836:15-18 (McRae Direct).

[15] *Id.* at 2835:19-2836:12 (Table 4) (McRae Direct).

[16] This example excludes any dividends that might have been paid by CenterPoint Houston to CNP.

[17] CenterPoint Houston's 10-Ks are filed in Project No. 18688 and reflect CNP's historic equity infusions into the Company. The Company's response to TCUC 1-7 also summarizes CNP's equity infusions through March 2019.

[18] *Id.*

[19] CEHE Ex. 48 at 41:20-42:12 & Exh. R-EL-3 (Lapson Rebuttal).

[20] *Id.* at 41:20-42:12 (Lapson Rebuttal).

on the adoption of 60% debt and 40% equity for capital structure."[21] Yet, in this case, the Commission is considering the exact opposite treatment by entertaining a ROE that is a 75 basis-point *downward* adjustment to the Company's current authorized ROE, while also considering a 500 basis-point *downward* adjustment in the amount of equity in its capital structure.

The record is clear that Moody's views increased leverage as less attractive to investors as evidenced by its statement that the absence of a supportive rate case outcome could lead to a downgrade in CenterPoint Houston's credit rating.[22] Moody's has also expressed concern with the increased risk associated with the cash flow decrease utilities are experiencing as a result of the TCJA, including the loss of bonus depreciation.[23] The rating agencies have explained that constructive regulatory decisions that approve increased equity ratios, ROEs, or depreciation expense are essential to restore lost cash flow and maintain utilities' current credit metrics.[24] In response to this guidance, CenterPoint Houston requested an increase in its existing 45% equity ratio to 50% to improve its post-TCJA cash flow metrics at the lowest cost to customers.[25] This higher equity ratio also moves CenterPoint Houston toward an equity ratio that is more consistent with those being approved by other regulatory agencies to offset the effect that the TCJA has had on utilities' cash flows.[26] In contrast, a capital structure that increases CenterPoint Houston's debt ratio above its currently authorized level of 55% and a ROE materially lower than 10% will cause CenterPoint Houston to fall below its current credit ratios at Moody's and Fitch.[27] This means increased risk for all investors, including equity investors.[28]

Equity investors have already begun to send a clear signal that affirms the negative impact that a 60/40 capital structure, 9.25% ROE, and dividend restrictions will have on CenterPoint

[21] *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*, Order No. 42 Interim Order Establishing Return on Equity and Capital Structure at 9-10 (Dec. 22, 2000).

[22] CEHE Ex. 48 at 55:9-12 & CEHE Ex. 48a at Confidential Exh. R-EL-5 (Lapson Rebuttal).

[23] CEHE Ex. 27 at 2839:3-10 (McRae Direct).

[24] *Id.* at 2837:1-2841:19 (McRae Direct).

[25] *Id.* at 2841:16-19 (McRae Direct).

[26] *Id.* at 2842:1-14 (McRae Direct)(explaining that the Alabama Public Service Commission has approved Alabama Power Company's request to move to a 55.0% equity ratio over time (from approximately 47%) because of the lost cash flows caused by the TCJA; the Georgia Public Service Commission has approved requests by Georgia Power Company and Atlanta Gas Light Company to move to a 55% equity ratio to mitigate the effects of the TCJA (from approximately 51%); and the Florida Public Service Commission approved a request by Florida City Gas to increase its equity ratio from 46.9% to 48.0% to mitigate the effects of the TCJA.).

[27] CEHE Ex. 43 at 24:1-25:17 (McRae Rebuttal).

[28] *See* CEHE Ex. 27 at 2858:10-2859:2 (McRae Direct) (relating to increased cost of debt).

Houston. During the Commission's November 14th discussion, CNP's stock fell sharply, closing that day down 5% and hitting a new 52-week low. This is notable because no other news was disclosed that day regarding CNP and the largest drops throughout the day occurred when the Commission discussed a 40% equity ratio and 9.25% ROE for CenterPoint Houston. The following day, November 15, 2019, CNP's stock suffered the biggest decline on the S&P 500, sinking to another 52-week low as various analyst downgrades were announced. As a result, over this two-day period, CNP experienced a total market cap loss of over $1.3 billion. Figure 1 illustrates the resulting 26% implied loss of CenterPoint Houston's value in the two days following the November 14th Commission Open Meeting. This is a direct reflection of how investors view CenterPoint Houston's value with a 60/40 capital structure and 9.25% ROE.

Figure 1

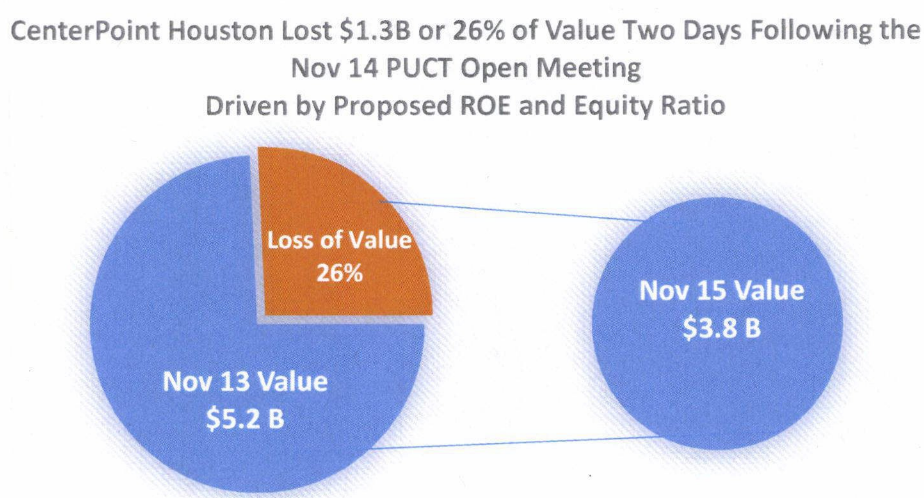

Figure 1 assumes CenterPoint Houston valuation equivalent to ~37% of total CNP market cap from Operating Income Contribution.

During this same two-day period, five separate analysts, Bank of America Merrill Lynch ("BAML"), Barclays, Credit Suisse, Guggenheim, and SunTrust Robinson also downgraded CNP's stock to Neutral or Hold from Buy. In taking this action, BAML, for example, explained that the "unconstructive outcome" of this rate case will likely be "much more punitive than expected" citing the Commission's discussion of a 60/40 capital structure, a 9.25% ROE, and ring-fencing provisions that would impose limits on the Company's ability to issue dividends.[29] All of these reports confirm the testimony and predictions of CenterPoint Houston's witnesses in this

[29] https://seekingalpha.com/news/3519856-centerpoint-energy-slammed-downgrades-four-wall-street-firms (retrieved on Nov. 24, 2019).

case and indicate that credit rating agency downgrades are likely in the near future.[30] They likewise directly contradict and prove incorrect the claims of Intervenor and Staff witnesses that suggested a ROE of 9.25% and capital structure ratio of 60% debt would not harm CenterPoint Houston or result in a credit rating downgrade, and that the ring-fencing provisions would be credit positive.[31]

In sum, it is important to recognize that ring-fencing measures designed to protect one utility may have unintended consequences and actually harm another utility. That is the case here. CenterPoint Houston's ratemaking capital structure dictates how it funds its capital needs. Cost of equity is the return investors expect in order to be willing to invest in the Company. Dividends are one component of the total return investors receive by investing in CenterPoint Houston. Investors who invest in utility equity, like investors in CNP stock, are especially sensitive to the need for consistent dividend payments over time. Utilities that are not able to maintain consistent dividend payments become less attractive to investors. The evidence and the market's reaction to the Commission's discussion make clear that dividend restrictions coupled with a 60% debt ratio and a 9.25% ROE will not be sufficient for CenterPoint Houston to attract equity as required under the law. For these reasons, CenterPoint Houston respectfully requests that the Commission reevaluate the record evidence in this case and issue a final order on ROE, capital structure and ring-fencing issues that will maintain its current level of financial integrity.

II. A 60/40 CAPITAL STRUCTURE, 9.25% ROE, AND DIVIDEND RESTRICTIONS UNDERMINE THE FINANCIAL INTEGRITY OF CENTERPOINT HOUSTON AND PRESENT IRRECONCILABLE CONFLICTS

Since 2011, CenterPoint Houston has managed and invested in its transmission and distribution system in accordance with a 55% debt/45% equity capital structure and a 10% ROE.[32] This capital structure and ROE in conjunction with sound management practices has allowed CenterPoint Houston to permanently finance more than $6 billion in long-term assets and respond to a generational storm event (Hurricane Harvey) while preserving its financial integrity. Recent events, such as the TCJA, including the loss of bonus depreciation, have required the Company to

[30] CEHE Ex. 48 at 42:13-44:13, Exh. R-EL-6, 46:16-47:7, 53:3-23, 55:4-12, 57:14-58:5 (Lapson Rebuttal); CEHE Ex. 27 at 2842:15-2843:11 (Table 5) (McRae Direct). CEHE Ex. 48, Exh. R-EL-6 is included for reference as Attachment B to this brief.

[31] TIEC Ex. 5 at 32:21-37:2 (Gorman Direct); Staff Ex. 1A at bates pages 12:38-13:11, 15:8-11 (Tietjen Direct).

[32] *See* Docket No. 38339, Order on Rehearing at Finding of Fact No. 67.

request in this case a higher ROE and equity ratio than those currently authorized in order to continue preserving its financial integrity.[33]

In this case, parties argue that an increase in the Company's debt ratio and in its ROE, such as TIEC's proposed 60% debt ratio and 9.25% ROE, will not impact CenterPoint Houston's financial metrics in a way that harms the Company or its customers. This was shown to be demonstrably false by the Company's rebuttal witness, Ms. Ellen Lapson, who analyzed this potential scenario and accurately predicted the market reaction discussed above; a market reaction that clearly undermines the Company's sound financial condition and access to long-term capital.[34] The evidence further shows that TIEC's proposed capital structure and ROE would cause CenterPoint Houston to be downgraded by both Moody's and Fitch.[35]

As a practical matter, capital structure rebalancing cannot occur if the dividend restriction based on net income is adopted. Legally, any dividend restrictions coupled with a 40% equity ratio or other equity ratio less than CenterPoint Houston's equity ratio of 45% at the end of the test year creates a takings issue.[36] This occurs because equity capital will be trapped within CenterPoint Houston and used on behalf of customers without adequate compensation. More specifically, the dividend restrictions necessarily compel CenterPoint Houston to hold some amount of trapped equity because it is not possible for the Company to manage its capital structure to precisely hit the authorized capital structure at all times. This, in turn, requires the Company to err on the side of having excess equity to avoid being in violation of a Commission order. Consequently, there is no potential resolution consistent with PURA and the United States and Texas Constitutions whereby both the dividend restrictions and a 60/40 capital structure or any capital structure below CenterPoint Houston's actual 45% equity ratio can be achieved.

The credit-rating-based dividend restriction also presents additional complications. Specifically, this measure prohibits CenterPoint Houston from issuing dividends if it falls below a credit rating of BBB+ for senior secured debt. As an initial matter, the requirement to maintain a BBB+ rating for CenterPoint Houston's senior secured debt is inconsistent with the requirements imposed on other utilities with similar ring fencing requirements as evidenced by the fact that

[33] CEHE Ex. 26 at 2677:6-2680:19 (Hevert Direct); CEHE Ex. 27 at 2837:2-2846:2 (McRae Direct).

[34] CEHE Ex. 48 at 100-103 (Exh. R-EL-6) (Lapson Rebuttal).

[35] CEHE Ex. 43 at 24:1-25:17 (McRae Rebuttal).

[36] See footnote 5 of this brief.

Oncor Electric Delivery Company is required only to maintain a BBB rating.[37] Moreover, the evidence in this case demonstrates that credit rating agencies have made clear that a 9.25% ROE in this case will not be sufficient to maintain CenterPoint Houston's credit metrics.[38] In a comment issued on June 17, 2019, Moody's noted that a ROE "materially below [CEHE's] current 10% . . . would be credit negative."[39] Likewise, the evidence shows that an equity layer below 45% is credit negative.[40]

As a result, this dividend restriction coupled with a 60/40 capital structure and 9.25% ROE will trigger the exact result that the restriction purports to protect against. In this regard, language requiring CenterPoint Houston to "work to ensure" the maintenance of its credit ratings cannot be reconciled with a cost of capital result that does not allow the Company to maintain and support its credit metrics.[41] It is also not realistic given that the only way for CenterPoint Houston to ensure that its credit ratings remain at or above the current rating is for the Company to improve its FFO/Debt ratio, which is largely influenced by factors outside the Company's control, such as authorized capital structure.[42] For example, CenterPoint Houston's cash flow will decrease under a 60/40 debt to equity ratio and 9.25% ROE. This, in turn, would cause a significant reduction in FFO and a corresponding increase in debt, which leads to a more negative FFO/Debt ratio that is not supportive of the Company's current credit metrics.[43]

Finally, the impact of the Commission's decisions on these issues is also not limited to CNP's shareholders or CenterPoint Houston. Weakened financial metrics for CNP and CenterPoint Houston would necessarily affect CNP's ability to support CenterPoint Houston during periods of financial distress—such as the period immediately following a major storm event when the utility may need immediate access to capital for restoration expenses, which was the case with Hurricane Ike in late 2008, a period of economic recession. It likewise may make it more difficult for CenterPoint Houston to continue spending discretionary capital in response to customer preferences, like the ongoing capital project to convert streetlights to LED lamps upon a

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[37] *See Joint Report and Application of Oncor Electric Delivery Company LLC and Sempra Energy for Regulatory Approvals Pursuant to PURA §§ 14.101.39 262 and 39.915*, Docket No. 47675, Final Order at Finding of Fact No. 51 (Mar. 8, 2018).

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

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

[40] CEHE Ex. 48 at 57:14-21 & CEHE Ex. 48a at Confidential Exh. EL-R-5 (Lapson Rebuttal).

[41] *See* Sections III.A.4 and III.C.1 of CenterPoint Houston's Exceptions to the PFD.

[42] CEHE Ex. 48 at 53:18-23 & Exh. R-EL-6 (Lapson Rebuttal).

[43] *Id.* at 41:9-17 (Lapson Rebuttal); CEHE Ex. 27 at 2842:15-2844:9 (McRae Direct).

customer request. In short, the Commission's decision on these issues has wide ranging impacts not only on CenterPoint Houston, but its customers.

III. MITIGATION OPTIONS

A. The most straightforward, reasonable and long-lasting means of reconciling the conflict created by the dividend restriction language is to increase CenterPoint Houston's equity ratio because this will cause equity to be injected into the Company, not withdrawn.

Increasing CenterPoint Houston's equity ratio up to 50% will eliminate the conflict created by a dividend restriction because it will result in an injection of equity that supports the Company's credit metrics and current financial stability.

1. A 60/40 capital structure is not the current standard for transmission and distribution utilities in Texas.

During the November 14th Open Meeting, it was suggested that a 60/40 capital structure was the "traditional method" of the Commission.[44] This has not been true for nearly a decade. In 2000, the Commission adopted a generic ROE of 11.25% and a generic 60/40 capital structure as a basis for setting initial rates for the newly unbundled transmission and distribution utilities ("TDUs") in Texas.[45] A decade later, in CenterPoint Houston's last rate case, the Commission recognized that the 60/40 structure created by Docket No. 22344 was intended to be in place during the transition period and be re-evaluated as the market matured.[46] Since 2011, CenterPoint Houston has managed its operations based on an authorized capital structure of 45% equity/55% debt.[47]

Moreover, CenterPoint Houston is one of six TDUs in Texas.[48] Of those TDUs, only American Electric Power Company ("AEP") has a 60/40 capital structure and the PFD in AEP's pending rate case recommends that AEP's capital structure be revised to 55% debt/45% equity—the same capital structure currently approved for CenterPoint Houston and also recommended by

[44] Open Meeting Tr. at 104:13 (Nov. 14, 2019).

[45] Docket No. 22344, Order No. 42 at 1.

[46] Docket No. 38339, PFD at 36 (Dec. 3, 2010).

[47] CEHE Ex. 27 at 2832:4-6 (McRae Direct); Docket No. 38339, Order on Rehearing at Findings of Fact 67-69..

[48] Sharyland Utilities no longer provides distribution service. However, the Commission's last approved capital structure for Sharyland as a TDU was comprised of 55% debt/45% equity and a ROE of 9.7%. *See Application of Sharyland Utilities, L.P. to Establish Retail Delivery Rates, Approve Tariff for Retail Delivery Service and Adjust Wholesale Transmission Rate,* Docket No. 41474 (Jan. 23. 2014).

the PFD in this case.[49] All of the other TDUs in Texas, as well as four fully integrated utilities in the state, have capital structures with equity ratios in excess of 40%:

Company	Docket No.	Final Order Date	ROE	Equity Ratio
Oncor	46957	Oct. 2017	9.8%	42.50%
TNMP	48401	Dec. 2018	9.65%	45%
AEP	49494	PFD Issued Nov. 2019	Recommended 9.4%	Recommended 45.0%
El Paso (integrated)	46831	Dec. 2017	9.65%	48.348%
SPS (integrated)	43695	Dec. 2015	9.7%	51%
SWEPCO (integrated)	46449	March 2018 (Order on Rehearing)	9.60%	48.46%
ETI (integrated)	48371	Dec. 2018	9.65%	50.90%

The PFD references a claim made by Staff witness Jorge Ordonez that a 60/40 capital structure is "consistent with the prevailing capital structure of many ERCOT TDUs." However, three of the five referenced companies are transmission-only utilities (Cross Texas, ETT, and WETT),[50] and the two genuine TDUs are the two AEP TDUs[51] for whom ALJs have recently recommended a 55/45 capital structure.[52] In addition, in comparison to the 9.25% ROE discussed at the November 14th Open Meeting, the Commission has approved a higher ROE for each of the transmission only utilities (Cross Texas – 9.6%, ETT – 9.96%, WETT – 9.6%, and Lone Star Transmission – 9.6%), which the Commission generally considers to have a lower risk profile than TDUs.[53]

Further, an examination of the Commission's rate of return analysis in the unbundling dockets, where the 60/40 capital structure was first imposed, demonstrates that the Commission was aware that its 2000 decision on capital structure in that case required the approval of a higher ROE. In fact, in Docket No. 22344, the Commission noted the "close correlation" between ROE and capital structure and approved a ROE for all TDUs that was 50 basis points higher than the

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[49] *Application of AEP Texas Inc for Authority to Change Rates*, Docket No. 49494, PFD at 139-140 (Nov. 12, 2019) ("AEP PFD").

[50] PFD at 180-181, n.718, citing Staff Ex. 39 at 37, n.41. And, not even the TSP-only utilities are at 60/40 as evidenced by Lone Star Transmission, LLC's approved 55/45 capital structure. *Application of Lone Star Transmission for Authority to Change Rates*, Docket No. 42469, Order at 4, Finding of Fact 25 (Sept. 11, 2014).

[51] *Id.*

[52] Docket No. 49494, AEP PFD at 139-140.

[53] *Application of Cross Texas Transmission LLC for Authority to Change Rates and Tariffs*, Docket No. 43950, Order at 5 (May 1, 2015); *Application of Electric Transmission Texas LLC for a Certificate of Convenience and Necessity, for Regulatory Approvals, and Initial Rates*, Docket No. 33734, Order on Rehearing at 17, Finding of Fact 57 (Dec. 21, 2007); *Application of Wind Energy Transmission Texas, LLC for Authority to Change Rates and Tariffs*, Order at 3 (Sept. 25, 2015); Docket No. 42469, Order at 4, Finding of Fact 25 (Sept. 11, 2014).

ROE the Commission had found to be "a reasonable starting point."[54] This reflected an upward adjustment of 50 basis points that accounted for, among other things, the "potential rating uncertainty due to higher debt based on the adoption of 60% debt and 40% equity for capital structure" in that proceeding.[55] As acknowledged by the recent PFD issued in AEP's pending rate case, Docket No. 49494, reliance on the 60/40 capital structure approved in the unbundling dockets, more than 19 years ago at the outset of competition, is simply not appropriate any longer.[56] The market and its participants have changed since the introduction of competition in 2001, and since 2011 the Commission, as demonstrated above, has changed the capital structures awarded to similarly situated utilities by moving *toward* (not away from) the 55/45 capital structure currently in place for CenterPoint Houston.[57]

2. The Commission has authority to adopt a capital structure that is within the range proposed by expert witnesses and is supported by substantial evidence.

It is well-settled law that the Commission may satisfy the substantial evidence standard of review by selecting a capital structure anywhere within the range of those proposed by expert witnesses in the case.[58] The evidence is undisputed that the Company's current capital structure is comprised of 55% debt and 45% equity.[59] The record evidence also reflects recommended capital structures ranging as follows:

Capital Structure Recommendations[60]

Party	Witness	Long-term Debt %	Equity %
CenterPoint Houston	McRae/Hevert	50.0	50.0
OPUC	Winker	54.5	45.5
TIEC	Gorman	60.0	40.0
TCUC	Woolridge*	60.0	40.0
Staff	Ordonez	60.0	40.0

* Mr. Woolridge's alternate recommendation is 55.48% long- term debt, 0.9% short-term debt, and 43.62% common equity.

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[54] Docket No. 22344, Order No. 42 at 8-9.

[55] *Id* at 10.

[56] Docket No. 49494, AEP PFD at 139-140 ("The market and its participants have changed since then. The Commission has changed the capital structures awarded to similarly situated utilities, moving toward the [55/45] capital structure advocated by AEP Texas.").

[57] *Id.*

[58] *See e.g. City of El Paso v. Pub. Util. Comm'n*, 883 S.W.2d 179, 186 (Tex. 1994) (allowing the "Commission to, in its discretion, select an amount within the range of figures provided by expert testimony of the parties."); *Cent. Power & Light Co. v. Pub Util. Comm'n*, 36 S.W.3d 547, 561 (Tex. App.–Austin 2000, pet. denied.).

[59] CEHE Ex. 27 at 2832:4-6 (McRae Direct); Docket No. 38339, Order on Rehearing at Findings of Fact 67-69.

[60] PFD at 173-174.

And, the evidence demonstrates that a 50/50 capital structure is consistent with the level of equity authorized for comparable utilities in other jurisdictions.[61] For example, the average equity ratio of electric delivery-only utilities for calendar year 2018 was 49.91%,[62] and it has been trending upward in recent years.[63] For the last eight calendar quarters, the average equity ratio was 53.28% for the holding companies in the Company's proxy group, and 53.13% for the utility operating companies encompassed within those holding companies.[64]

Therefore, the Commission has all the record evidence it needs to adopt: (1) the 50% equity ratio requested by CenterPoint Houston and thus, more closely align the Company's capital structure with the equity ratios approved for comparable utilities or (2) adopt an equity ratio falling between CenterPoint Houston's equity ratio request of 50% and its approved existing 45% equity ratio.

B. Moving to a 60/40 capital structure will prevent the Company's recovery of its 2019 distribution capital investment unless a transition period is adopted.

Even if the dividend restriction is eliminated, the adoption of a 60/40 capital structure in this case will create another unintended consequence of preventing timely recovery of the Company's 2019 distribution capital. During 2019, the Company has operated under the current Commission-approved 55/45 capital structure and 10% ROE. Some parties may, however, argue that the Earnings Monitoring Report ("EMR") due in a few months should compare 2019 to any new equity ratio and ROE approved in this case, which may be materially lower. Perversely, that comparison could show CenterPoint Houston over-earning and ineligible to make a DCRF filing to recover its 2019 distribution capital investment. Indeed, that could be the case for multiple years following such a dramatic downward shift in the Company's equity ratio and ROE given that the Commission has not, since unbundling occurred in 2001, reduced a TDU's equity ratio. Debt and equity investors expect that CenterPoint Houston will use the DCRF and TCOS mechanisms to recover incremental capital, and a decision in this case that prevents CenterPoint Houston from doing so would further degrade the Company's financial integrity. As a result, the Company would need the Commission to reject an interpretation of the EMR and DCRF rules that causes this punitive result. To address this, the Company's capital structure and ROE for, at least

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[61] CEHE Ex. 27 at 2854:1-9 (McRae Direct); CEHE Ex. 26 at Exh. RBH-9 (Hevert Direct).

[62] CEHE Ex. 43 at 38:9-11 (McRae Rebuttal).

[63] Staff Ex. 3A at 36:1-2, Chart (Ordonez Direct); CEHE Ex. 43 at 38:9-11 (McRae Rebuttal); CEHE Ex. 48 at 50:9-12 (Lapson Rebuttal).

[64] CEHE Ex. 27 at 2854:4-9 (McRae Direct); CEHE Ex. 26 at Exh. RBH-9 (Hevert Direct).

the 2019 EMR and the 2020 interim period before new rates are implemented, should continue to be evaluated based on a 45% equity ratio and a 10% ROE.

C. The language of the dividend restriction provisions should, at a minimum, also be revised to provide additional clarity.

If the Commission moves forward with dividend restriction ring-fencing measures, CenterPoint Houston urges the Commission to make revisions to afford the Company the opportunity to more gradually adjust its capital structure to any changes resulting from this docket, to provide further clarity regarding the requirements of the dividend restriction provisions, and to mitigate the possibility that any dividend restrictions will compound the problems of decreased access to external funding caused by the proposals on capital structure and ROE.[65] These necessary language revisions are shown in Attachment C to this Brief.

D. Proposals to require CenterPoint Houston to return equity in excess of the Commission-approved equity ratio through the inter-company money pool or to utilize excess equity to fund system investment are not workable.

CenterPoint Houston appreciates the Commission's decision to reject the ring-fencing provisions that would have precluded the Company from continuing to utilize the inter-company money pool. In this regard, CenterPoint Houston understands that the Commission intends to adopt the following measure with regard to this issue:

- Except for its participation in an affiliate money pool, CenterPoint Houston shall not commingle its assets with those of other CNP affiliates.
- Except for its participation in an affiliate money pool, CenterPoint Houston shall not lend money to or borrow money from CNP affiliates.

At the Open Meeting, however, H-E-B's counsel suggested that excess equity resulting from a change in CenterPoint Houston's existing capital structure could be returned to CNP through the inter-company money pool. This suggestion is not workable because CenterPoint Houston investing in the money pool does not reduce its equity. Transferring cash to a money pool is similar to investing in a money market account; the funds are still the property of the investor. Therefore, no equity is transferred out.

Commission Staff's suggestion at the Open Meeting that CenterPoint Houston can utilize excess equity resulting from any change in the Company's current equity ratio is also not workable

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[65] These language revisions should not be construed as a change in CenterPoint Houston's stance opposing the ring-fencing measures, including the imposition of dividend restrictions, or a waiver of CenterPoint Houston's legal arguments regarding the Commission's jurisdictional authority or the evidence demonstrating that additional ring-fencing measures are not necessary to protect CenterPoint Houston's financial integrity or the other arguments raised in the Company's Exceptions to the PFD at Sections III.E.1 through 6.

as it would cause CenterPoint Houston to continue to exceed its authorized equity ratio and would result in the situation where retained excess equity would only receive a cost of debt return on that equity.

IV. CONCLUSION

A fiscally strong utility is in the interest of customers, regulators, and shareholders. Three issues are critical to CenterPoint Houston's financial integrity and its ability to comply with regulatory measures that the Commission may impose in this case: (1) capital structure; (2) cost of capital, including a record low ROE; and (3) measures that would preclude CenterPoint Houston from issuing dividends. The Company thanks the Commission for its consideration of these issues and the others discussed in its Exceptions and asks the Commission to render a decision in this case that will allow CenterPoint Houston to comply with the regulatory directives of the Commission while allowing the Company to recover its reasonable and necessary costs, giving the Company a reasonable opportunity to earn a fair return on its investment, and maintaining the financial strength of the Company so that it can continue providing safe and reliable service.

Respectfully submitted,

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COUNSEL FOR CENTERPOINT ENERGY HOUSTON ELECTRIC, LLC

CERTIFICATE OF SERVICE

I hereby certify that on this 25th day of November 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.

Patrick H. Peters III

Q. IS A CAPITAL STRUCTURE WITH 50.0% COMMON EQUITY REASONABLE WHEN COMPARED TO CAPITAL STRUCTURES OF THE COMPANIES IN MR. HEVERT'S PROXY GROUP?

A. Yes. As shown on Mr. Hevert's Exhibit RBH-9, the average equity ratio of the 24 holding companies in the proxy group was 53.28% over the last eight calendar quarters. If one reviews the capital structures of the utility operating companies encompassed within those 24 holding companies, the average equity ratio during that same time period was 53.13%. Both of those percentages are considerably higher than the 50% equity ratio requested by CenterPoint Houston in this case.

Q. SOME OF THE OPERATING COMPANIES LISTED ON EXHIBIT RBH-9 ARE VERTICALLY INTEGRATED UTILITIES. ARE YOU AWARE OF ANY EVIDENCE SHOWING THAT A 50% EQUITY RATIO IS REASONABLE WHEN THE COMPARISON IS LIMITED TO ELECTRIC DELIVERY-ONLY UTILITIES?

A. Yes. RRA periodically publishes a report showing the authorized ROEs and equity ratios authorized by state regulatory commissions. Pages 11-12 of my Exhibit RBM-5, which is the RRA publication issued on January 31, 2109, shows that the average authorized equity ratio for delivery-only electric utilities was 49.91% for calendar year 2018.

Q. HOW DID YOU DETERMINE WHICH OF THE UTILITIES LISTED ON PAGE 10 WERE ELECTRIC DELIVERY-ONLY UTILITIES?

A. The "Footnotes" column at the right-hand side of Page 10 contains various numbers and letters, one of which is the letter "D." Page 15 of Exhibit RBM-5 explains that the letter "D" denotes electric delivery-only utilities. Table 8 lists the utilities with the letter "D" beside them and the authorized equity ratios for those electric delivery-only utilities:

Table 8. Authorized Equity Ratios for Delivery-Only Utilities[24]

Date of Final Order	Utility	Authorized Equity Ratio
3/15/18	Niagara Mohawk Power Corporation	48.0%
4/18/18	Connecticut Light and Power Company	53.0%
5/31/18	Potomac Electric Power Company	50.44%
6/14/18	Central Hudson Gas & Electric Corp.	48.0%
6/28/18	Emera Maine	49.0%
8/8/18	Potomac Electric Power Company	50.44%
8/21/18	Delmarva Power & Light Company	50.52%
8/24/18	Narragansett Electric Company	50.95%
9/26/18	Dayton Power and Light Company	47.52%
10/04/18	UGI Utilities, Inc.	54.02
10/29/18	Public Service Electric and Gas Company	54.0%
11/1/18	Ameren Illinois Company	50.0%
12/4/18	Commonwealth Edison Company	47.11%
12/19/18	Duke Energy Ohio, Inc.	50.75%
12/20/18	Texas-New Mexico Power Company	45.0%
12/21/18	Green Mountain Power Corporation	49.85%
Average		49.91%

[24] Exhibit RBM-5 at 11-12.

As Table 8 shows, the average authorized equity ratio for electric delivery-only utilities in 2018 was 491 basis points higher than CenterPoint Houston's current authorized equity ratio, but only 9 basis points lower than the 50% equity ratio that CenterPoint Houston asks the Commission to approve in this case.

D. Summary of Capital Structure Recommendation

Q. HOW WOULD YOU SUMMARIZE THE DATA THAT YOU HAVE REVIEWED AND PRESENTED IN THIS TESTIMONY ON THE MATTER OF CAPITAL STRUCTURE?

A. The impacts of the TCJA on cash flow and incremental debt necessary to finance CenterPoint Houston's capital investment will create downward pressure of its credit metrics and may lead to a ratings downgrade. The most efficient way to maintain CenterPoint Houston's A3/BBB+/A- issuer credit rating is to increase the equity content in its capital structure. This will finance more of CenterPoint Houston's capital investment with equity and improve metrics. The data and testimony I have presented demonstrate the reasonableness of using a 50/50 capital structure. As I have stated previously, I think that it is in the best interest of electric consumers and the communities we serve for the local transmission and distribution utility to have a single-A credit rating because such rating is expected to allow the utility to raise funds as needed, on reasonable terms, to finance the ongoing capital investment and improvements in our electric system even in the face of adverse conditions (whether that be a hurricane that affects the utility or developments in the bank or capital markets that affect all companies in the industry).

CenterPoint Energy Houston Electric, LLC

Scenario: 55% Long-Term Debt; 45% Equity. Authorized ROE 10%

Pro Forma using Moody's methodologies

Current Rating: A3	Predicted Rating 2020-22			Baa1 or Baa2
				Indicative Rating
Moody's (including Securitization) (a)	**2020**	**2021**	**2022**	2020-2022
Funds From Operations Interest Coverage	5.23	5.29	5.26	
Moody's Benchmarks	*4.5 -6 x = A*			A mid
	3 - 4.5x = Baa			
Total Debt / Capital	55.4%	55.1%	55.0%	
Moody's Benchmarks	*50-59% = Baa*			Baa2 mid
	59% - 67% = Ba			
Funds From Operations / Total Debt	16.0%	16.3%	16.5%	
Moody's Benchmarks	*11% - 19%= Baa*			Baa1
(FFO - Dividends) / Total Debt	12.7%	12.3%	13.8%	
Moody's Benchmarks	*7% - 15%= Baa*			Baa2 to Baa1
Total Debt / EBITDA	4.58	4.34	4.27	n.a.
(FFO - Dividends) / Capital Expenditures	67.1%	56.9%	80.2%	n.a.
Moody's (excluding Securitization) (a)	**2020**	**2021**	**2022**	
Funds From Operations Interest Coverage	4.90	4.80	4.71	
Moody's Benchmarks	*4.5 -6 x = A*			A low
	3 - 4.5x = Baa			
Total Debt / Capital	50.4%	51.1%	52.0%	
Moody's Benchmarks	*50-59% = Baa*			Baa1
	59% - 67% = Ba			
Funds From Operations / Total Debt	15.6%	10.5%	12.3%	
Moody's Benchmarks	*11% - 19%= Baa*			Baa2 to Baa3
(FFO - Dividends) / Total Debt	11.6%	10.5%	12.3%	
Moody's Benchmarks	*7% - 15%= Baa*			Baa2
Total Debt / EBITDA	4.52	4.40	4.38	n.a.
(FFO - Dividends) / Capital Expenditures	49.9%	41.5%	62.9%	n.a.

(a) Primary ratios are those that include securitization debt and related cash flows.

n.a. There is no applicable Moody's benchmark.

Scenario: 65% Debt,

Pro Forma using Fitch Ratings methodologies

Current Rating: A-	**Predicted Rating 2020-22:**			**BBB to BBB-**
				Indicative Rating
Fitch Ratings Ratio Method (b)	**2020**	**2021**	**2022**	2020-2022
FFO Interest Coverage (times)	4.86	4.90	4.85	A-
Fitch Benchmarks	*5x = Median A*			
	4.5x=Median BBB			
	3.5x = Median BB			
Debt / EBITDA (times)	4.39	4.28	4.28	BBB- to BB+
Fitch Benchmarks	*3.75x= Median BBB*			
	4.75x = Median BB			
Debt / FFO (times)	4.86	4.76	4.74	BBB mid
Fitch Benchmarks	*5x = Median BBB*			
	6.5x = Median BB			
Debt as % of Total Capitalization	60.0%	60.2%	60.5%	n.a.
Common Equity as % of Total Capitalization	40.0%	39.8%	39.5%	n.a.
FFO / Debt %	13.8%	13.8%	13.8%	n.a.
EBITDA Interest Coverage (times)	4.78	4.77	4.71	n.a.
% Internal Cash Generation [(FFO less Dividends) / Capital Expenditures]	78.3%	74.6%	91.0%	n.a.

(b) Ratios are computed by eliminating securitization debt and all related cash flows.
n.a. - There is no applicable Fitch benchmark.

Pro Forma using S&P rating methodologies (SACP).

Current SACP: a+	**Predicted SACP 2020-22:**			**a**
Current formal Rating: A-				
				Indicative Financial
S&P Rating Method (b)(c)				Risk Category
Core Ratios	**2020**	**2021**	**2022**	2020-2022
FFO/Total Debt	15.4%	15.9%	16.1%	Intermediate
Total Debt/EBITDA	4.48	4.38	4.38	Significant
Supplemental Ratios				
OCF/Total Debt	15.1%	14.6%	14.6%	Intermediate
FOCF/ Total Debt	-7.8%	-10.3%	-4.5%	Aggressive
EBITDA Interest Coverage	5.37%	5.42%	5.35%	Intermediate
FFO Interest Coverage	4.72%	4.79%	4.78%	Intermediate

Financial Risk Category: Significant

Business Risk Category	**Interme-diate**	**Signi-ficant**	**Aggres-sive**	**Highly Leveraged**
Excellent	$\boxed{\text{a+/a}}$	a-	bbb	bbb-/bb+
Storng	a-/bbb+	bbb	bb+	bb
Satisfactory	bbb/bbb-	bbb-/bb+	bb	b+

(b) Ratios are computed by eliminating securitization debt and all related cash flows.
(c) Low Volatility Matrix; Assuming Business Risk Category is Excellent
OCF = Operating Cash Flow; FOCF= Free Operating Cash Flow
SACP = Standalone Credit Profile (a component used to develop the formal rating)

CenterPoint Energy Houston Electric, LLC

Scenario: 60% Long-Term Debt; 40% Equity. Authorized ROE 9.25%

Pro Forma using Moody's methodologies

Current Rating: A3	**Predicted Rating 2020-22**			**Baa3 or Baa2** Indicative Rating 2020-2022
Moody's (including Securitization) (a)	**2020**	**2021**	**2022**	
Funds From Operations Interest Coverage	3.66	3.60	3.56	
Moody's Benchmarks	*4.5 -6 x = A*			Baa3
	3 - 4.5x = Baa			
Total Debt / Capital	59.6%	59.4%	59.3%	
Moody's Benchmarks	*50-59% = Baa*			Baa3 low
	59% - 67% = Ba			
Funds From Operations / Total Debt	14.0%	13.9%	14.0%	
Moody's Benchmarks				Baa2
(FFO - Dividends) / Total Debt	11.3%	10.5%	11.5%	
Moody's Benchmarks	*7% - 15%= Baa*			Baa2
Total Debt / EBITDA	5.01	4.83	4.79	n.a.
(FFO - Dividends) / Capital Expenditures	94.5%	86.2%	103.2%	n.a.

Moody's (excluding Securitization) (a)	**2020**	**2021**	**2022**	
Funds From Operations Interest Coverage	3.28	3.08	3.03	
Moody's Benchmarks	*4.5 -6 x = A*			Baa3 low
	3 - 4.5x = Baa			
Total Debt / Capital	55.0%	55.7%	56.6%	
Moody's Benchmarks	*50-59% = Baa*			Baa2
	59% - 67% = Ba			
Funds From Operations / Total Debt	13.2%	12.5%	12.6%	
Moody's Benchmarks	*11% - 19%= Baa*			Baa3
(FFO - Dividends) / Total Debt	10.0%	8.6%	9.8%	
Moody's Benchmarks	*7% - 15%= Baa*			Baa3
Total Debt / EBITDA	5.03	4.99	4.99	n.a.
(FFO - Dividends) / Capital Expenditures	77.3%	70.7%	85.9%	n.a.

(a) Primary ratios are those that include securitization debt and related cash flows.

n.a. There is no applicable Moody's benchmark.

Scenario: 60% Debt, 40%

Pro Forma using Fitch Ratings methodologies

Current Rating: A-

Fitch Ratings Ratio Method (b)		**2020**	**2021**	**2022**	**BBB mid** Indicative Rating 2020-2022
FFO Interest Coverage (times)		4.25	4.20	4.17	BBB mid
	Fitch Benchmarks	*5x = Median A*			
		4.5x=Median BBB			
		3.5x = Median BB			
Debt / EBITDA (times)		4.92	4.88	4.87	BB mid
	Fitch Benchmarks	*3.75x= Median BBB*			
		4.75x = Median BB			
Debt / FFO (times)		5.53	5.53	5.49	BBB low
	Fitch Benchmarks	*5x = Median BBB*			
		6.5x = Median BB			
Debt as % of Total Capitalization		60.0%	60.2%	60.5%	n.a.
Common Equity as % of Total Capitalization		40.0%	39.8%	39.5%	n.a.
FFO / Debt %		13.8%	13.8%	13.8%	n.a.
EBITDA Interest Coverage (times)		4.78	4.77	4.71	n.a.
% Internal Cash Generation [(FFO less Dividends) / Capital Expenditures]		78.3%	74.6%	91.0%	n.a.

(b) Ratios are computed by eliminating securitization debt and all related cash flows.
n.a. - There is no applicable Fitch benchmark.

Pro Forma using S&P rating methodologies (SACP)

Current SACP: a+ **Predicted SACP 2020-22:** **a-**
Current formal Rating: A-

S&P Rating Method (b)(c)				Indicative Financial Risk Category
Core Ratios	**2020**	**2021**	**2022**	2020-2022
FFO/Total Debt	13.1%	13.4%	13.5%	Intermediate
Total Debt/EBITDA	4.99	4.97	4.98	Significant
Supplemental Ratios				
OCF/Total Debt	12.8%	11.9%	12.0%	Signficant
FOCF/ Total Debt	-8.2%	-11.0%	-5.6%	Aggressive
EBITDA Interest Coverage	4.80%	4.76%	4.68%	Intermediate
FFO Interest Coverage	4.19%	4.16%	4.14%	Intermediate

Financial Risk Category: Significant

Business Risk Category	**Interme-diate**	**Signi-ficant**	**Aggres-sive**	**Highly Leverage**
Excellent	**a+/a**	$\boxed{\text{a-}}$	bbb	bbb-/bb+
Storng	a-/bbb+	bbb	bb+	bb
Satisfactory	bbb/bbb-	bbb-/bb+	bb	b+

(b) Ratios are computed by eliminating securitization debt and all related cash flows.
(c) Low Volatility Matrix; Assuming Business Risk Category is Excellent
OCF = Operating Cash Flow; FOCF= Free Operating Cash Flow
SACP = Standalone Credit Profile (a component used to develop the formal rating)

Dividend Restriction Language Changes

Dividend Restriction Commitment. Effective January 1, 2021, CenterPoint Houston shall limit the payment of dividends by CenterPoint to an amount not to exceed CenterPoint Houston's ~~its~~ net income (as determined in accordance with GAAP). As of the date the Commission's Order in Docket No. 49421 becomes final through December 31, 2020, CenterPoint Houston shall make an informational filing with the Commission no less than 30 days prior to issuing any dividend. Furthermore, this restriction shall not apply to dividends at the end of the year made to true-up CenterPoint Houston's capital structure.

CenterPoint Houston Credit Ratings and Suspension of Dividends. ~~CenterPoint Houston shall work to ensure that its credit ratings at all three major ratings agencies (S&P, Moody's, and Fitch) remain at or above CenterPoint Houston's current credit ratings.~~ If CenterPoint Houston's credit rating at any one of the three major ratings agencies falls below BBB-~~BBB+ (or its equivalent)~~ for CenterPoint Houston's senior secured debt, then CenterPoint Houston shall suspend payment of dividends or other distributions, except for contractual tax payments, until otherwise allowed by the Commission. CenterPoint Houston must notify the Commission if its credit issuer rating or corporate rating as rated by any of the three major rating agencies falls below investment-grade level.

Debt-to-Equity Ratio. CenterPoint Houston's debt shall be limited so that its debt-to-equity ratio, as shown in its Earnings Monitor Report, at December 31st of each year is at or below the debt-to-equity ratio established from time to time by the Commission for ratemaking purposes in CenterPoint Houston rate proceedings. The Commission has authority to determine what types of debt and equity are included in a utility's debt to-equity ratio. CenterPoint Houston shall not make any payment of dividends or other distributions, except for contractual tax payments, where such dividends or other distributions would cause CenterPoint Houston to be out of compliance with the Commission-approved debt-to-equity ratio. ~~Additionally, neither CNP nor any of its affiliates may issue a stock or ownership interest that supersedes the foregoing obligations of CenterPoint Houston.~~