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OFFICE OF PUBLIC UTILITY COUNSEL'S INITIAL COMMENTS ON COMMISSION'S PROPOSAL FOR PUBLICATION

The Office of Public Utility Counsel ("OPUC") respectfully submits these initial comments on the Proposal for Publication approved by the Public Utility Commission of Texas ("Commission") on February 14, 2020. The Commission's Proposal for Publication proposes new 16 Texas Administrative Code ("TAC") § 25.248, relating to the establishment of a generation cost recovery rider ("GCRR") for electric utilities operating outside of the Electric Reliability Council of Texas ("ERCOT") region in Texas. The proposed new rule implements House Bill 1397 ("HB 1397")¹ and corresponding Public Utility Regulatory Act ("PURA") § 36.213 (relating to Recovery of Generation Investment by Non-ERCOT Utilities). OPUC appreciates the Commission's efforts to create an efficient process to allow the Non-ERCOT utilities to recover their investment in generation facilities that provide service to the public, while ensuring that ratepayers pay just and reasonable rates for electric service. The Commission addressed many of OPUC's recommendations in its Proposal for Publication. In these initial comments, OPUC recommends that the Commission: (1) include a load growth adjustment in the proposed rule; (2) include additional offsets for accumulated deferred federal income taxes (ADFIT), accumulated depreciation, and avoided or displaced purchased power capacity costs in the definition of "power generation facility net invested capital"; (3) use certain class allocation factors for new generation facilities included in a GCRR; (4) add a "Commercial Operation Date" definition to serve as the effective date of a GCRR; and (5) add a reporting requirement to monitor the utility's earnings over the twelve-month period following the effective date of the GCRR.

¹ Tex. H.B. 1397, 86th Leg., R.S. (2019).

I. <u>COMMENTS ON THE PUBLISHED PROPOSAL</u>

A. <u>INCLUSION OF A LOAD GROWTH ADJUSTMENT (SUBSECTION (d) –</u> <u>CALCULATION OF GCRR)</u>

The proposed rule does not include an adjustment for load growth.² OPUC previously advocated for the inclusion of a load growth adjustment in its comments on Commission Staff's strawman rule and reiterates its position in the current filing.³ As discussed in OPUC's prior comments, without a load growth adjustment, the proposed GCRR formula would result in an over-recovery of generation capacity costs by the utility, because the GCRR formula would not fully account for load growth on the utility's system.⁴ The inclusion of a load growth adjustment in the GCRR rule would enable the Commission to consider the increase in base rate revenues resulting from an increase in load on the utility's system since the utility's last base rate case and would allow those increases to be offset by the cost of the new generation facility. Without a load growth adjustment, a utility would be allowed to over-recover costs in a GCRR, because the utility would be permitted to seek full recovery of its generation investment costs without a corresponding offset to recognize the increased base rate revenues from increased load on the utility's system. The GCRR is intended to reduce regulatory lag associated with the recovery of costs for new generation facilities, but not to allow for over-recovery of costs by the utility. Allowing a utility to simultaneously benefit from quicker recovery of generation investment, while the utility continues to collect higher base rate revenues due to higher load on its system, would serve to benefit the utility at the expense of its ratepayers.

In order to address this significant formulaic flaw in the proposed GCRR calculation, as discussed in OPUC's prior comments, the appropriate benchmark for evaluating the proposed GCRR formula is to evaluate whether the recovery of production capacity costs through the GCRR is equivalent to recognizing the new generation facility in a base rate case.⁵ The proposed GCRR

² Chairman DeAnn T. Walker's Memo at 3 (Feb. 13, 2020).

³ See Office of Public Utility Counsel's Reply Comments on Commission Staff's Strawman Rule at 5 (Nov. 15, 2019) (OPUC Reply Comments); See also Office of Public Utility Counsel's Comments on Commission Staff's Strawman Rule at 6 – 8 (Nov. 8, 2019) (OPUC Comments).

⁴ See Proposed Section 25.248(d)(4), 45 TexReg 1527, 1529 (Mar. 6, 2020).

⁵ OPUC Comments at 7.

formula does not recognize the impact of load growth on production capacity costs, and therefore, the GCRR would recover more production capacity costs than would be recovered in a traditional rate case. When a new generation facility is placed in service and recognized in a base rate case, the cost of the new generation facility is added to existing embedded generation costs, and the resulting generation rates are based on average costs that include the new generation facility. The average cost of generation is spread across the test year billing units, producing the new generation rates. This is the basic concept of average cost ratemaking. However, the proposed GCRR formula only recognizes current billing units for the new generation facility's cost. In doing so, the proposed GCRR formula ignores the impact on average production capacity costs, and in particular, the effect of load growth on average cost generation rates.

In order to implement a load growth adjustment in the proposed rule, OPUC recommends that the Commission use the same load growth adjustment methodology included in 16 TAC § 25.238 for the purchased power capacity cost recovery factor ("PCRF").⁶ In adopting the load growth adjustment in the PCRF rulemaking project, the Commission stated that it strikes an appropriate balance that considers "the potential for over-recovery, the fungibility of production sources, and the advantages of examining all of a utility's production-related expenses in toto."⁷ The Commission noted that it had previously approved load growth adjustments in Project No. 39465, Rulemaking Related to Periodic Rate Adjustments, and Project No. 39674, Rulemaking Proceeding to Amend Energy Efficiency Rules.⁸ The fact that the GCRR pertains to production facility costs, as opposed to purchased power, makes the load growth adjustment even more important and appropriate in the proposed GCRR formula. Moreover, the load growth adjustment in the Commission's PCRF rule in 16 TAC § 25.238 is based on the utility's production investment cost, which is directly comparable to production facility investment.

⁶ See 16 Tex. Admin. Code § 25.238 (TAC). (The key term in the PCRF formula is "LGI," which recognizes and deducts the load growth associated with production capacity costs. The LGI term is a percentage growth in billing units that is applied to total production investment cost, with the resulting load growth value deducted from the new capacity cost.)

⁷ Rulemaking Proceeding Concerning Recovery of Purchased Power Capacity Costs, Including Amendment of Subst. R. 05.238, Project No. 39246, Order Adopting Repeal of §25.238 and New §25.238 as Approved at the May 9, 2013 Open Meeting at 58 (May 28, 2013).

⁸ Id.

The simplified illustration in Attachment 1 demonstrates the over-recovery of production costs if load growth is not appropriately recognized in the proposed GCRR formula.⁹ The baseline for comparison is the generation rate that results from recognizing the new generation facility investment in a major base rate case (Line 3). The proposed GCRR formula over-recovers production capacity costs by 8.8% in this example (Line 6). However, if the load growth adjustment included in the Commission's PCRF rule is applied in the proposed GCRR formula, the over-recovery is eliminated (Line 13). This simple solution will ensure that ratepayers are not paying more than is necessary for a utility to recover costs of a new generation facility. For these reasons, OPUC requests that the Commission include a load growth adjustment in the proposed GCRR formula on a class-by-class basis to prevent over-recovery by a utility.

In their comments on Commission Staff's strawman rule, Entergy Texas, Inc. ("ETI") and Southwestern Public Service Company ("SPS") contend that the GCRR should not include a load growth adjustment.¹⁰ Both utilities note that HB 1397 does not expressly provide for a load growth adjustment. ETI states that while the Commission's Distribution Cost Recovery Factor ("DCRF") rule includes a load growth adjustment, the statutory authority for the DCRF provides for such an adjustment, whereas the GCRR statute (PURA § 36.213) is silent on the issue.¹¹ However, contrary to ETI's and SPS's assertions, the GCRR statute's silence regarding a load growth adjustment does not preclude the Commission from including one in the proposed rule. As discussed in Texas Industrial Energy Consumers' ("TIEC") initial comments on Commission Staff's strawman rule, the GCRR statute is intentionally silent on what adjustments the Commission can make to prevent over-recovery of costs by a utility.¹² As TIEC states, when Senator Nichols explained why HB 1397 did not include a load growth adjustment, he statute, therefore, is not intended to limit the Commission's authority to include a load growth adjustment, but rather gives the Commission the discretion to include

¹³ Id.

⁹ See Attachment 1, Simplified Illustration of Load Growth Adjustment, Project No. 50031, OPUC Comments.

¹⁰ See ETI's Informal Comments on the Strawman Rule, at 7; and Comments of SPS on Proposed New Texas Administrative Code ("TAC") §25.248 at 4.

¹¹ Id.

¹² TIEC's Initial Comments on Strawman at 6.

such an adjustment in its GCRR rule. For comparison purposes, the statute authorizing the PCRF rule is similarly silent on whether the Commission should include a load growth adjustment,¹⁴ but the Commission nevertheless included a load growth adjustment in the PCRF rule. Therefore, the Commission has the discretion to include a similar load growth adjustment in the GCRR rule and should include such an adjustment to prevent a utility from over-recovering generation capacity costs.¹⁵

B. <u>ADDITIONAL OFFSETS TO DEFINITION OF POWER GENERATION</u> FACILITY NET INVESTED CAPITAL (SUBSECTION (b)(5)

As discussed in OPUC's comments on Commission Staff's strawman rule, in order to avoid over-recovery of costs by the utility, OPUC supports additional offsets to the proposed definition of power generation facility net invested capital, including offsets for ADFIT, accumulated depreciation associated with a utility's embedded net production plant investment, and avoided or displaced purchased power capacity costs.¹⁶

The proposed rule limits recognition of ADFIT and accumulated depreciation to the amounts associated with the power generation facility net invested capital included in the GCRR. However, this proposed offset is minimal, relative to the recognition of ADFIT and accumulated depreciation associated with a utility's aggregate production net plant investment. ADFIT and accumulated depreciation are known and measurable adjustments to the amount of production net plant investment currently included in a utility's rates and should be reflected as an offset to the utility's power generation facility net invested capital in the GCRR. The changes in production net plant investment ADFIT and accumulated depreciation are known and measurable accounting measures that fluctuate with the passage of time. If power generation facility net invested capital offsets are limited to the specific new generation facility associated with the GCRR, the GCRR will result in customers paying an inflated production rate base, because rates will include both the GCRR net invested capital and generation assets in base rates which are not reduced for the current level of ADFIT and accumulated depreciation. OPUC, therefore, recommends that the Commission not limit the power generation facility net invested capital offsets to the specific new generation.

¹⁴ See PURA §§ 36.204-.205.

¹⁵ OPUC Reply Comments at 5.

¹⁶ OPUC Comments at 5.

generation facility, because the failure to recognize offsets outside of the new r generation facility will result in an over-recovery of costs by the utility.

The proposed rule does not include offsets for displaced or avoided purchased power capacity costs to the power generation facility net invested capital in the GCRR. Since the addition of a new generation facility may allow a utility to forego some level of purchased power capacity already embedded in costs, those avoided costs should be deducted from the costs that are recoverable through the GCRR. Failure to account for displaced or avoided purchased power capacity costs will result in an over-recovery of costs directly attributable to the addition of the new generation facility. OPUC, therefore, recommends that the Commission include the following language in the definition of power generation facility net invested capital in subsection(b)(5):

(5) **Power generation facility net invested capital** – Power generation facility invested capital that is adjusted for accumulated depreciation and any changes in accumulated deferred federal income taxes, including changes to excess accumulated deferred federal income taxes, associated with all power generation facilities included in the electric utility's GCRR. <u>This value shall include offsets related to the change in generation-related accumulated depreciation (AD) and accumulated deferred federal income taxes (ADFIT). The following shall be deducted from the facility invested capital:</u>

i. Change in AD for a pre-existing generation resource generation accumulated depreciation approved in the most recent base rate case minus the balance of generation related accumulated depreciation for the most recent 12-month period prior to the GCRR effective date.

<u>ii. Change in ADFIT - generation accumulated deferred</u> federal income taxes approved in the most recent base rate case minus the balance of generation related accumulated deferred income taxes for the most recent 12 month period prior to the GCRR effective date, based on the utility's accounting records. OPUC believes it is necessary to require offsets for avoided or displaced purchased power capacity costs to the power generation facility net invested capital in the GCRR to avoid over-recovery of costs by the utility.

C. CLASS ALLOCATION FACTORS (SUBSECTION (f))

As discussed in OPUC's comments on Commission Staff's strawman rule, relying upon class allocation factors from a utility's last base rate case, in certain circumstances, may create interclass inequities.¹⁷ If the purpose of the new generation facility is primarily energy-related, rather than demand-related, the use of demand allocation derived from four coincident peak hours will be inconsistent with cost causation. For example, non-dispatchable generation resources, such as solar generation and wind generation, may not provide any, or in some cases limited, contributions to a utility's generation reserve margin requirement. The output of wind generation may be effectively non-existent during the four coincident peak hours. Commission Staff's strawman rule recognized this issue by requiring the allocation of non-firm generation facilities in the GCRR on the basis of class energy use.

OPUC strongly recommends that the Commission reinsert the language from subsection (f) in Commission Staff's strawman rule which maintains the difference between firm and nonfirm generation capacity, allocates firm generation capacity based on demand allocation factors from the utility's previous rate case, and allocates non-firm generation capacity based on energy allocation factors from the utility's previous rate case.¹⁸ Failure to recognize the difference between firm and non-firm generation capacity in the proposed rule will result in the application of allocation factors to generation facilities for which those factors were not designed to apply. Wind generation, for example, primarily peaks in production in non-summer and non-peak usage hours, meaning it does not align with the four coincident peak summer hours used for demand allocation. Non-firm generation resources, like wind generation, are more appropriately allocated on a demand basis. This distinction is important and should be recognized in subsection (f).

¹⁷ See OPUC Comments at 8 – 9; See also OPUC Reply Comments at 5 - 6.

¹⁸ Staff Revised Draft Rule Language at 5 (Oct. 28, 2019).

In the alternative, in order to avoid cost allocation disputes in a GCRR proceeding, OPUC would support the proposed rule's use of default class allocation factors from the utility's last base rate case, but only with certain limitations on the precedential value of the allocation factors utilized and guarantees of reconsideration in the utility's next base rate proceeding that includes the new generation facility.¹⁹ The class allocation factors set in the GCRR should not be precedential, and as necessary, the Commission should be able to alter the class allocation factors in the utility's next base rate case that includes the new generation facility. OPUC acknowledges that a new generation facility may use a new source of power generation that does not have a pre-existing class allocation factor from a previous base rate case. For example, if a utility has never included a wind generation facility in rate base, the utility will not have a class allocation factor for a wind generation facility from a previous base rate case.²⁰ The use of pre-existing class allocation factors for other generation facilities in the utility's previous base rate case should not set precedent for a new generation facility on a going forward basis, and therefore, the pre-existing class allocation factors should be considered both temporary and reconcilable in the utility's next base rate case that includes the new generation facility.

If the Commission chooses not to recognize firm versus non-firm generation capacity in the proposed rule, OPUC recommends that the Commission specifically state in subsection (e) that the use of pre-existing default class allocation factors for a new generation facility that utilizes a new power resource for the utility is non-precedential and the class allocation factors will be subject to reconsideration in the utility's next base rate proceeding. OPUC suggests that the Commission add the following language to subsection (e):

(e) Jurisdictional and class allocation factors. For calculating GCRR rates, the baseline jurisdictional and rate-class allocation factors used to allocate generation invested capital in the last base-rate proceeding will be used. <u>These allocation factors do not set</u> precedent for a facility that utilizes a generation resource not already

¹⁹ OPUC Comments at 8 - 9.

²⁰ In some instances, previous renewable generation projects were contractually procured and included as an operating expense, and generally recovered through reconcilable fuel rates (energy allocation). However, the GCRR applies to utility constructed facilities which will be recovered as invested capital through base rates.

used by the utility and are subject to reconciliation in the next baserate proceeding.

If the Commission determines in the utility's next base rate proceeding that the class allocation factors for the new generation facility should be different than the pre-existing default class allocation factors that were used in the GCRR, the difference in the GCRR's cost allocation can be corrected in the reconciliation of the GCRR. This approach would temporarily address cost allocation to help avoid cost allocation disputes in the GCRR process and would help prevent ratepayers from carrying the burden of inequitable cost allocation on a more permanent basis.

D. EFFECTIVE DATE OF GCRR (SUBSECTION (b))

As discussed in OPUC's comments on Commission Staff's strawman rule, Section 36.213(d) of PURA states that the GCRR "shall take effect on the date the power generation facility begins providing service to the electric utility's customers."²¹ However, PURA does not provide further guidance as to what actually constitutes providing service to an electric utility's customers. For example, if the utility is building a wind generation facility with 100 wind turbines, can the utility claim that the effective date of the GCRR is the date that it installed the first wind turbine? OPUC believes that such an effective date scenario should be expressly addressed by the Commission with the adoption of a "Commercial Operation Date" definition. The "Commercial Operation Date" should serve as the date when service was first provided to a utility's customers.²² OPUC, therefore, recommends that the Commission add the following definition to the proposed rule in subsection (b):

Commercial Operation Date – the date on which a new power generation facility begins commercial operation.

As a matter of due diligence to further protect ratepayers, an electric utility should also be required to provide proof of commercial operation of the new generation facility before the GCRR goes into effect. For instance, an electric utility should be required to show that all tests and inspections for the manufacturer warranties have been successfully passed by the new generation facility, the new generation facility has achieved operation at full power for a set number of hours,

²¹ PURA § 36.213(d).

²² OPUC Comments at 5 and 10.

and the new generation facility is able to provide reliable power to the utility's customers.²³ OPUC believes that requiring proof of commercial operation of the new generation facility and setting the effective date at the date of commercial operation would provide additional certainty regarding the effective date of the GCRR and would prevent a GCRR from becoming effective before service is actually provided to the electric utility's customers.

II. <u>GCRR TERM LIMITATION DUE TO UTILITY'S EARNINGS (NEW</u> SUBSECTION (k))

As a matter of due diligence to further protect ratepayers from potential over-recovery of costs by the utility, similar to the existing DCRF process, OPUC recommends that the Commission require a utility that obtains approval of a GCRR to file an earnings monitoring report that contains the utility's earnings for the twelve-month period immediately preceding the GCRR's effective date. If the annual GCRR earnings report shows that the utility is exceeding its authorized rate of return using weather normalized data, the utility's GCRR should be limited to a twelve-month period. This proposed reporting mechanism would help prevent over-recovery of costs by the utility, would provide additional ratepayer protection, and would provide a utility with a sufficient amount of time to prepare a base rate case that incorporates the new generation facility associated with the GCRR in base rates.

OPUC recommends that the Commission add the following language in new subsection (k) of the proposed rule:

(k) Term limitation due to earnings – An electric utility shall submit an earnings monitoring report for the calendar year immediately preceding the effective date of the commissionapproved GCRR. The commission shall limit an electric utility's GCRR to a term of 12 months after the effective date of the GCRR if the earnings monitoring report shows that the electric utility is earning more than its authorized rate of return using weather-normalized data.

²³ OPUC Comments at 5.

If the Commission does not incorporate OPUC's recommended offsets to generation plant facility net invested capital for ADFIT, accumulated deferred depreciation, and avoided or displaced purchased power capacity costs, the utility may receive a return on its investment in base rates, while it receives excess earnings through a GCRR. Without the additional protections provided by OPUC's recommended offsets to generation plant facility net invested capital or the proposed GCRR earnings monitoring report mechanism, ratepayers will face an elevated risk of being overcharged by the utility. OPUC believes that the suggested language strikes the proper balance between protecting ratepayers, while giving a utility the ability to recover power generation facility invested capital.

III. CONCLUSION

OPUC appreciates the opportunity to provide comments on the Commission's proposed rule and looks forward to working with the Commission and other stakeholders in this project.

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Respectfully submitted,

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Simplified Illustration of Load Growth Adjustment

	Production Demand Cost				
Rate Case Recognition	Rev	Req Rate (e (kW)	
1. Initial Embedded Cost	\$	4,500,000	\$	4.50	
2. Add Generation	\$	600,000			
3. New Test Year Level (1+2)	\$	5,100,000	\$	4.64	
4. GCRF as Proposed (2/Current BU)			\$	0.55	
5. Total Rate Recovery (4+1)			\$	5.05	
6. Over recovery (% of 3)				8.8%	
Load Growth Adjustment Per Subst. R. 25.328					
7. LGI Term in Formula		10%			
8. Times Initial Embedded Cost (7X1)	\$	450,000			
9. Deduct from Added Gen (2-8)	\$	150,000			
10. GCRF Rate (8/Current BU)			\$	0.14	
11.Existing Production Rate (1)			\$	4.50	
12. Total (10+11)			\$	4.64	
13. Over recovery			\$	-	

Assumptions:				
	С	ost/kW	MW	Billing Units
New Generation		40	100	
Existing Generation		30	1000	
Fixed Charge Rate		0.15	0.15	
Average Cost	\$	30.91	1100	
Prior Demand			1000	1,000,000
Demand Growth			100	100,000
Current Demand			1100	1,100,000