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# State Office of Administrative Hearings

Kristofer S. Monson
Chief Administrative Law Judge

December 28, 2022

Stephen Journeay, Commission Counsel
Commission Advising and Docket Management
William B. Travis State Office Building
1701 N. Congress, 7th Floor
Austin, Texas 78701

**VIA EFILE TEXAS**

**RE: SOAH Docket Number 473-22-2695; Public Utility Commission of Texas Docket No. 53601; *Application of Oncor Electric Delivery Company LLC for Authority to Change Rates***

Dear Mr. Journeay:

Please find attached a Proposal for Decision in this case. Enclosed is the Proposal for Decision (PFD) in the above-referenced case. By copy of this letter, the parties to this proceeding are being served with the PFD.

Please place this case on an open meeting agenda for the Commissioners' consideration. Please notify the undersigned Administrative Law Judges and the parties of the open meeting date, as well as the deadlines for filing exceptions to the PFD, replies to the exceptions, and requests for oral argument.

Enclosure

CC: Service List

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## LIST OF ACRONYMS AND DEFINED TERMS

| TERM | DEFINITION |
|---|---|
| 4CP | 4 Coincident Peak |
| ADFIT | Accumulated Deferred Federal Income Taxes |
| AEP Texas | AEP Texas, Inc. |
| AFUDC | Allowance for Funds Used During Construction |
| ALJ | Administrative Law Judge |
| AOC | Alliance of Oncor Cities |
| ARM | Alliance for Retail Markets |
| ASC | Accounting Standards Codification |
| CAPM | Capital Asset Pricing Model |
| CCN | Certificate of Convenience and Necessity |
| CCOSS | Class Cost of Service Study |
| CenterPoint | CenterPoint Energy Houston Electric, LLC |
| CI | Conformance Index |
| CIAC | Contribution in Aid of Construction |
| Cities | Steering Committee of Cities Served by Oncor |
| COL | Conclusion of Law |
| Commission | Public Utility Commission of Texas |
| Company | Oncor Electric Delivery Company LLC |
| CPI | Consumer Price Index |
| CRAs | Credit Rating Agencies |
| CREZ | Competitive Renewable Energy Zones |
| DCF | Discounted Cash Flow |
| DCRF | Distribution Cost Recovery Factor |
| DESR | Distribution Energy Storage Resource |
| DoD/FEA | United States Department of Defense and all other Federal Executive Agencies |
| DSC | Distribution System Charge |
| DSRP | Distribution Service Request Process |
| ECAPM | Empirical Capital Asset Pricing Model |
| ECOM | Investment that Exceeded Market |
| EOP | Emergency Operations Plan |
| ERCOT | Electric Reliability Council of Texas |

| TERM | DEFINITION |
|---|---|
| ETEC | East Texas Electric Cooperative, Inc. |
| EVgo | EVgo Services, LLC |
| FEA | Facilities Extension Agreement |
| FERC | Federal Energy Regulatory Commission |
| FOF | Finding of Fact |
| GAAP | Generally Accepted Accounting Principles |
| GDP | Gross Domestic Product |
| Google | Google LLC |
| GS | General Service |
| HB | House Bill |
| HEN | Hunt Energy Network L.L.C. |
| IAG | Inadvertent Gain |
| IRS | Internal Revenue Service |
| ISO | Independent System Operator |
| kV | Kilovolt |
| kVA | Kilovolt-Ampere |
| kVAr | Kilovolt-Ampere Reactive |
| kW | Kilowatt |
| kWh | Kilowatt-hour |
| Kroger | The Kroger Co. |
| LTI | Long Term Incentive |
| MW | Megawatt |
| NERC | North American Energy Reliability Corporation |
| NCP | Non-Coincident Peak |
| Nucor | Nucor Steel-Longview |
| O&M | Operations and Maintenance |
| OLT | Observed Life Table |
| Oncor | Oncor Electric Delivery Company LLC |
| OPEB | Other Post-Employment Benefits |
| OP | Ordering Paragraph |
| OPUC | Office of Public Utility Counsel |
| PFD | Proposal for Decision |
| PGC | Power Generation Company |
| Pioneer | Pioneer Natural Resources USA, Inc. |
| POD | Point of Delivery |

| TERM | DEFINITION |
|---|---|
| POI | Point of Interconnection |
| PRPM | Predictive Risk Premium Method |
| PUC | Public Utility Commission of Texas |
| PURA | Public Utility Regulatory Act |
| Rayburn | Rayburn Country Electric Cooperative, Inc. |
| RCE | Rate Case Expense |
| REP | Retail Electric Provider |
| REI | Retirement Experience Index |
| RFI | Request for Information |
| RFP | Request for Proposals |
| ROE | Return on Equity |
| RSU | Restricted Stock Units |
| S&P | Standard & Poor's |
| SAIDI | System Average Interruption Duration Index |
| SAIFI | System Average Interruption Frequency Index |
| SERP | Supplemental Executive Retirement Plan |
| Sharyland | Sharyland Utilities, L.P. |
| SDTS | Sharyland Distribution & Transmission Services, L.L.C. |
| SOAH | State Office of Administrative Hearings |
| SPS | Southwestern Public Service Company |
| Staff | Staff of the Public Utility Commission of Texas |
| STI | Short Term Incentive |
| T&D | Transmission and Distribution |
| TAC | Texas Administrative Code |
| Targa | Targa Pipeline Mid-Continent WestTex, LLC |
| TCGA | Texas Cotton Ginners' Association |
| TCJA | Tax Cuts and Jobs Act of 2017 |
| TCRF | Transmission Cost Recovery Factor |
| TDCS | Transmission and Distribution Utility Customer Service |
| TDU | Transmission and Distribution Utility |
| TEAM | Texas Energy Association for Marketers |
| TESR | Transmission Energy Storage Resource |
| TIEC | Texas Industrial Energy Consumers |
| TNMP | Texas-New Mexico Power Company |

| TERM | DEFINITION |
|---|---|
| USOA | FERC Uniform System of Accounts |
| U.S. | United States |
| UT System | The University of Texas System and its Agencies |
| Value Line | Value Line Investment Survey |
| WACC | Weighted Average Cost of Capital |
| Walmart | Walmart Inc. |

**SOAH Docket No. 473-22-2695 Suffix: PUC**
**PUC Docket No. 53601**

# BEFORE THE STATE OFFICE OF ADMINISTRATIVE HEARINGS

## APPLICATION OF ONCOR ELECTRIC DELIVERY COMPANY LLC FOR AUTHORITY TO CHANGE RATES

## PROPOSAL FOR DECISION

## I. INTRODUCTION

Oncor Electric Delivery Company LLC (Oncor or the Company) filed an application with the Public Utility Commission of Texas (Commission) on May 13, 2022, requesting authority to change its rates. Oncor is an investor-owned electric utility operating within the Electric Reliability Council of Texas (ERCOT) region. Oncor is the largest electric utility in Texas and the largest pure transmission and distribution utility (TDU) in the United States (U.S.).[1] The Company serves approximately 13 million customers in a service area that is over 54,000 square miles and covers 20% of Texas geographically and 48% of the electric meters in the ERCOT region.[2]

In its application, Oncor requests approval to increase its annual retail base rate revenue requirement to $5.811 billion—an increase of approximately $251 million, or 4.5%, over its adjusted test-year revenues of $5.560 billion.[3] Oncor calculated the revenue requirement increase using an overall proposed rate of return of 7.05%, which reflects a debt-to-equity ratio of 55% to 45% and a rate of return on equity (ROE) of 10.3%. Oncor states that its request reflects approximately $10.2 billion of capital investments made since December 31, 2016, the end of the test year in Oncor's last rate case. Oncor's application in this case uses a test year ending December 31, 2021.

## A. Executive Summary

The Administrative Law Judges (ALJs) find that Oncor met its burden of proof as to its proposals except where this Proposal for Decision (PFD) states otherwise or where necessary to recognize flow-through impacts of the ALJs' recommendations. In general, the PFD does not discuss uncontested issues, which are incorporated in the PFD's findings of fact (FOFs), conclusions of law (COLs),

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[1] Oncor Ex. 8 (Nye Dir.) at 4.

[2] Oncor Ex. 8 (Nye Dir.) at 4.

[3] Oncor Ex. 1 (Application) at 15.

and ordering paragraphs (OPs). As detailed in the schedules attached to this PFD as Appendix A, the ALJs recommend an overall revenue *decrease* of $60.6 million below the total adjusted revenue requirement for the test year, which represents a $397.2 million reduction to Oncor's requested annual retail base rate revenue requirement.

The ALJs' recommendations on some of the most significant issues are summarized below.

Rate Base

- The ALJs recommend disallowing $3.1 million attributable to the leasing costs of mobile generation units.
- The ALJs recommend disallowing $8.94 million attributable to Oncor's long-term accrued debt interest (this represents a $4.289 million reduction in the transmission revenue requirement and a $4.651 million reduction in the distribution revenue requirement).
- The ALJs recommend disallowing $13,115,158 million attributable to capitalized non-qualified pension expense.
- The ALJs recommend a 10-year amortization period for Oncor's $588.5 million self-insurance reserve (SIR) balance and an SIR annual accrual of $90 million.
- The ALJs recommend Oncor recover $13.65 million attributable to unrecovered expenses related to Covid-19 and $3.45 million of the related amortization expense (this represents recovery of $13.65 million for the asset and $3.45 million of the related amortization expense).
- The ALJs recommend disallowing the $851,000 annual amortization expense associated with a 2013 acquisition of utility plant assets by Sharyland Utilities, L.P. (Sharyland) from Southwestern Public Service Company (SPS).

- The ALJs recommend a 10-year amortization period for all non-tax regulatory assets and liabilities except for the Intangible Amortization Over-Recovery liability, for which the ALJs recommend a five-year amortization period.
- The ALJs recommend disallowing $34,607,629 attributable to capitalized financially based short-term and long-term incentive compensation costs.
- The ALJs recommend disallowing $16,861,782 attributable to the capitalized portion of non-financially based short-term and long-term incentive compensation that is predicated on a financial trigger (this represents one half of Oncor's request for non-financially based incentive compensation).
- The ALJs recommend disallowing $375,717 attributable to capitalized executive perquisites.

Rate of Return

- The ALJs recommend a ROE of 9.3%, a cost of debt of 4.39%, and a capital structure of 57.5% long-term debt and 42.5% common equity. Those recommendations result in an overall recommended rate of return of 6.48%.

Financial Integrity (Ring-Fencing Protections)

- The ALJs recommend that Oncor's existing ring-fencing provisions remain unchanged.

Operations and Maintenance (O&M) Expenses

- Regarding labor-related expenses, the ALJs recommend disallowing:
    - $7,953,307 million attributable to 100% of all financially based short-term incentive compensation and 50% of all non-financially based short-term incentive compensation that is predicated on a financial trigger.

- $14,430,262 million attributable to financially-based long-term incentive compensation.
- $2,938,132 million attributable to pension and other post-retirement benefits.
- $236,866 attributable to executive perquisites.

Depreciation

- The ALJs recommend approval of Oncor's proposed depreciation study and the resulting depreciation rates with the exception of the depreciation rates applicable to Accounts 353 (Transmission and Station Equipment) and 356 (Overhead Conductor).

Billing Determinants

- The ALJs recommend adopting Oncor's proposed customer growth adjustment to test-year billing determinants.
- The ALJs recommend an additional weather normalization adjustment to Oncor's billing determinants to exclude the entirety of February 2021 when determining class non-coincident peak (NCP) demand to account for the impact of Winter Storm Uri.
- The ALJs recommend rejecting Oncor's proposed power factor adjustment to test-year billing determinants.

Cost Allocation

- The ALJs recommend adopting Staff's proposal that Oncor update the four coincident peak (4CP) class allocation factors for the Transmission Cost Recovery Factor (TCRF) on an annual basis, and not update the TCRF rider in this proceeding.
- The ALJs recommend adopting Oncor's proposal to allocate costs to the wholesale rate classes on the basis of system average costs.

- The ALJs recommend that distribution energy storage resources (DESRs) continue to be subject to the rate schedules for the wholesale classes.
- The ALJs recommend that the Transmission and Primary Substation rate classes be excluded when allocating the cost of Federal Energy Regulatory Commission (FERC) Account 368 capacitors.
- The ALJs recommend that the Wholesale Substation (XFMR), Transmission, and Primary Substation rate classes be excluded when allocating mobile generation costs.
- The ALJs recommend allocating power factor revenues to all classes, both retail and wholesale.

<u>Revenue Distribution</u>

- The ALJs recommend that Oncor's rates be set at cost without rate moderation. Alternatively, if the Commission believes that rate moderation is warranted, the ALJs recommend adopting Staff witness Adrian Narvaez's proposal to phase in the change to the TCRF allocation factors.

<u>Rate Design</u>

- The ALJs recommend retaining the existing rate design for the Secondary Service > 10 kW class, including the 80% demand ratchet and annual load factor groupings.
- The ALJs recommend approving Oncor's proposal to continue charging an inadvertent gain (IAG) charge to retail electric providers (REPs), but that the amount of the charge should not increase.

<u>Baselines</u>

- The ALJs recommend adopting Staff's proposed methodology for calculating the Distribution Cost Recovery Factor (DCRF) baseline with two adjustments: (1) include FERC Account 391, but ensure that it does not include indirect corporate costs like office furniture; and (2) include in the DCRF baseline the excess ADFIT net regulatory liability created due to the Tax Cuts and Jobs Act.

Rate-Case Expenses

- The ALJs recommend adoption of the proposed settlement agreement approving $10 million in recoverable rate-case expenses and the reimbursement amounts for Cities and AOC.
- The ALJs recommend that Oncor be prohibited from earning a return on the unrecovered balance of rate-case expenses not recovered within the first year.

## B. Jurisdiction, Notice, and Procedural History

The Commission has jurisdiction over this proceeding under Public Utility Regulatory Act (PURA)[4] §§ 14.001, 32.001, 33.002, 33.051, 35.004, and 36.001. SOAH has jurisdiction over all matters relating to the conduct of the hearing in this proceeding under PURA § 14.053 and Texas Government Code § 2003.049.

On May 13, 2022, Oncor filed its application with the Commission and each municipality in Oncor's service territory that has not ceded its original jurisdiction as a regulatory authority to the Commission. Oncor appealed the municipalities' actions regarding the application, and the appeals were consolidated with this docket.[5]

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[4] Public Utility Regulatory Act, Tex. Util. Code §§ 11.001-66.016 (PURA).

[5] SOAH Order No. 2 (June 24, 2022); SOAH Order No. 3 (June 29, 2022); SOAH Order No. 5 (July 11, 2022); SOAH Order No. 7 (July 15, 2022); SOAH Order No. 9 (Aug. 5, 2022); SOAH

On May 16, 2022, the Commission referred this case to the State Office of Administrative Hearings (SOAH). The Commission issued its Preliminary Order on June 30, 2022, identifying 76 issues to be addressed in this proceeding.

On June 24, 2022, the SOAH ALJs found Oncor's application and notice sufficient.[6] The ALJs suspended Oncor's proposed effective date for the proposed rates for 150 days. To allow sufficient time for the ALJs and the Commission to process this case, Oncor agreed to further extend the effective date for its proposed rates such that the Commission's deadline to issue a final order is extended to March 3, 2023.[7]

The following entities intervened in this case and were admitted as parties: Alliance for Retail Markets (ARM); Alliance of Oncor Cities (AOC); Chevron U.S.A., Inc.; East Texas Electric Cooperative, Inc. (ETEC); EVgo Services, LLC (EVgo); Google LLC (Google); Hunt Energy Network L.L.C. (HEN); The Kroger Co. (Kroger); Nucor Steel – Texas (Nucor); Office of Public Utility Counsel (OPUC); Pioneer Natural Resources USA, Inc. (Pioneer); Rayburn Country Electric Cooperative, Inc. (Rayburn); Steering Committee of Cities Served by Oncor (Cities); Targa Pipeline Mid-Continent WestTex LLC (Targa); Texas Cotton Ginners' Association (TCGA); Texas Energy Association for Marketers (TEAM); Texas Industrial Energy Consumers (TIEC); University of Texas

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Order No. 21 (Oct. 31, 2022); SOAH Order No. 22 (Nov. 7, 2022); SOAH Order No. 23 (Nov. 10, 2022).

[6] SOAH Order No. 2 (June 24, 2022).

[7] SOAH Order No. 23 (Nov. 10, 2022).

System and its Agencies (collectively, UT System);[8] U.S. Department of Defense and all other Federal Executive Agencies (DoD/FEA); Walmart, Inc. (Walmart).[9] Commission staff (Staff) also participated as a party.

The hearing on the merits convened by videoconference on September 26, 2022, and concluded on October 4, 2022. On October 14, 2022, the parties filed initial post-hearing briefs, and on October 28, 2022, they filed reply briefs and proposed FOFs, COLs, and OPs. The record was kept open to provide additional time for the parties to submit information to facilitate the number-running process that is necessary to reflect the ALJs' recommended adjustments in the PFD.[10] On November 4, 2022, Staff filed a supplemental exhibit list identifying the parties' informational filings and requesting their admission into the record. Staff Exhibits 53 through 58, as identified on Staff's supplemental exhibit list, are hereby **ADMITTED**. The record closed on November 4, 2022, as to all issues except rate-case expenses (RCEs).

Final RCE updates were filed by Oncor on November 1, 2022, and by Cities and AOC on November 4, 2022. On November 10, 2022, Staff filed the supplemental testimony of Ruth Stark addressing RCEs. On November 15, 2022, Oncor filed a statement of position regarding Ms. Stark's supplemental testimony,

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[8] The University of Texas System Agencies participating in this docket are: The University of Texas at Arlington, The University of Texas at Dallas, The University of Texas Health Science Center at Tyler, The University of Texas at Tyler, The University of Texas Permian Basin, and The University of Texas Southwestern Medical Center.

[9] SOAH Order No. 2 (June 24, 2022); SOAH Order No. 3 (June 29, 2022); SOAH Order No. 4 (July 6, 2022); SOAH Order No. 5 (July 11, 2022).

[10] SOAH Order No. 21 (Oct. 31, 2022).

and AOC filed an affidavit in rebuttal to Ms. Stark's supplemental testimony. Thereafter, Oncor notified the ALJs that Oncor and Staff had reached a settlement agreement on RCEs, which was unopposed by Cities and AOC. On December 2, 2022, Oncor filed the settlement agreement and an associated agreed motion to admit evidence, and Staff filed a memorandum of Ms. Stark in support of the agreement. The following exhibits described in the agreed motion to admit evidence are hereby **ADMITTED**: Oncor Exhibits 110 and 111; Staff Exhibits 59 and 60; Cities Exhibit 18; and AOC Exhibits 38 and 39. The RCE settlement is discussed in Section XI below.

## II. INVESTED CAPITAL/RATE BASE

PURA provides that "[i]n a proceeding involving a proposed rate change, the electric utility has the burden of proving that . . . the rate change is just and reasonable."[11] PURA also requires the Commission to establish a utility's overall revenues at an amount that will permit it a reasonable opportunity to earn a reasonable return on its invested capital.[12] The rate base, also referred to as invested capital, includes "the original cost of plant, property, and equipment, less accumulated depreciation, used and useful in rendering service to the public."[13] Aside from a utility's invested capital being used and useful in providing service to

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[11] PURA § 36.006(1).

[12] PURA § 36.051.

[13] 16 Tex. Admin. Code (TAC) § 25.231(c)(2).

the public, the cost must also be prudently incurred.[14] The legal standard for determining prudence is well established:

> [P]rudence is the exercise of that judgment and the choosing of one of that select range of options which a reasonable utility manager would exercise or choose in the same or similar circumstances given the information or alternatives available at the point in time such judgment is exercised or option is chosen.[15]

"The 'prudence' standard explicitly incorporates a utility's reasonableness and, by speaking in terms of available alternatives, implicitly recognizes that an expense must be necessary."[16] This decision of reasonableness "must be judged in light of the circumstances, information, and available options existing at the time, without benefit of hindsight."[17] A utility can establish that its investments were prudent by presenting historical facts and testimony from employees or other experts.[18] Furthermore, "[w]hat is prudent, reasonable, and necessary depends on circumstances. The prudence standard does not require perfection."[19] Although the utility has the initial burden to prove its capital investments were prudent, if it establishes a *prima facie* case of prudence, prudence is presumed, and the burden shifts to others to rebut that presumption.[20]

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[14] PURA §§ 36.051, .053; 16 TAC § 25.231(c)(2).

[15] *Pub. Util. Comm'n of Tex. v. Tex. Indus. Energy Consumers*, 620 S.W.3d 418, 428 (Tex. 2021).

[16] *Nucor Steel v. Pub. Util. Comm'n*, 26 S.W.3d 742, 748 (Tex. App.—Austin 2000, pet. denied).

[17] *Tex. Indus. Energy Consumers*, 620 S.W.3d at 428.

[18] *Tex. Indus. Energy Consumers*, 620 S.W.3d at 429-30.

[19] *Nucor Steel*, 26 S.W.3d at 749.

[20] *Entergy Gulf States v. Pub. Util. Comm'n of Tex.*, 112 S.W.3d 208, 214 (Tex. App.—Austin 2003, pet. denied).

Here, Oncor has the burden of proving that any cost incurred for capital investment since the test year ended in Oncor's last rate case was prudently incurred and used and useful.

## A. T&D Capital Investment

Oncor's transmission and distribution (T&D) capital investments through test year ending December 31, 2021, reflect a net plant in service of $21.1 billion, which produces a net rate base of $18.8 billion.[21]

### 1. Capital Investments Acquired from Sharyland and SDTS

#### a. Sharyland CCN Projects

Oncor seeks recovery of approximately $12.1 billion in additional capital investments not previously reviewed for prudence, which includes the following:[22]

- $4.13 billion invested in Oncor's distribution system;[23]
- $5.37 billion invested in Oncor's legacy transmission systems;[24]

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[21] *See* Oncor Ex. 2 (Non-Voluminous Schedules) at Schedule II-B; Oncor Ex. 4 (45-day Update); Oncor Ex. 17 (Ledbetter Dir.) at 32.

[22] Oncor Initial Brief at 13.

[23] Oncor Ex. 11 (Hull Dir.) at 18. Throughout the PFD the ALJs will reference the native page numbers, not Bates, for the direct testimonies filed with Oncor's application.

[24] Oncor Ex. 10 (Speed Dir.) at 8.

- $1.62 billion for capital investments Oncor acquired from Sharyland and Sharyland Distribution & Transmission Services, L.L.C. (SDTS);[25] and
- $959 million in technology-related capital investments.[26]

Staff recommends disallowance of two capital investments acquired from Sharyland and SDTS. No other party recommends disallowance, and Oncor contends that Staff's recommended disallowances are meritless.[27]

To establish the prudence of its capital investments, Oncor provided detailed explanations of the various cost drivers for more than 1,600 transmission projects, along with its decision-making processes, and any cost variances.[28]

### i. Staff's Recommendation

Staff witness John Poole testified that Oncor submitted 1,645 capital projects for prudence review for a total cost of $6.29 billion, broken down as follows:[29]

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[25] Oncor Ex. 10 (Speed Dir.) at 8-9. These assets previously held by Sharyland and SDTS were obtained through Oncor's acquisition of InfraREIT, Inc. and are now owed by Oncor Electric Delivery Company, NTU LLC. *Id.*

[26] Oncor Ex. 4 (45-day Update) at 15.

[27] Oncor Initial Brief at 14.

[28] *See* Oncor Ex. 10 (Speed Dir.) at 8-35; Oncor Ex. 40 (Speed Reb.) at 7-60; Oncor Ex. 11 (Hull Dir.) at 18-24; Oncor Ex. 12 (Nichols Dir.) at 3-10; Oncor Ex. 12A; Oncor Exs. 19 (Austin Dir.) and 19A (Austin Workpapers); Oncor Exs. 20 (Hodges Dir.) and 20A (Hodges Workpapers); Oncor Exs. 2I & 2L.

[29] Staff Ex. 3 (Poole Dir.) at 6.

| Number of Projects | Project Description | Total Cost |
|---|---|---|
| 34 | Commission ordered as a result of applications for Certificates of Convenience and Necessity (CCN) | $1.78 billion |
| 1,015 | Projects that did not require a CCN and had initial estimates | $3.45 billion |
| 596 | Additional projects that did not have estimates | $1.06 billion |

As displayed in the table below, Staff recommends the disallowance of two projects—CCN Docket No. 38829 (White Deer-to-Silverton Competitive Renewable Energy Zones (CREZ) transmission line) and CCN Docket No. 40484 (Colorado City-to-Barber Lake transmission line)—for a total recommended disallowance of $5.0 million.[30] These proposed disallowances relate to cost overruns on projects Oncor acquired from Sharyland and SDTS.[31] Specifically, the final costs for the projects exceeded the cost approved by the Commission by more than 10%.[32] Staff, therefore, recommends only granting the originally approved amount plus 10% to cover reasonable contingencies.[33]

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[30] Staff Initial Brief at 10. Mr. Poole initially challenged the prudence of certain Oncor capital investments. Staff Ex. 3 (Poole Dir.) at 3. After reviewing the rebuttal testimony of Oncor witness Wesley Speed and other Oncor exhibits, Mr. Poole withdrew this testimony and filed supplemental direct testimony indicating that all the capital investments originally constructed by Oncor were prudent, while retaining disallowances for the two projects identified above. Staff Ex. 52 (Poole Suppl.) at 4. Thus, Mr. Poole's proposed disallowance was reduced by approximately $223 million (from $228 million to $5 million). *Compare* Staff Ex. 3 (Poole Dir.) at 17, 22, 26 *with* Staff Ex. 52 (Poole Suppl.) at 4.

[31] Staff Initial Brief at 10; *see* Staff. Ex. 3 (Poole Dir.) at 18-19.

[32] Staff Ex. 3 (Poole Dir.) at 21; Staff Ex. 53 (Staff Cross Exhibit) at 4.

[33] Staff Ex. 52 (Poole Suppl.) at 5.

| CCN Docket No. | Disallowance |
|---|---|
| 38829 | $3,547,074.37 |
| 40484 | $1,470,090.49 |
| **Total** | **$5,017,164.86** |

The basis for Staff's disallowance is that the projects exceeded the Commission-ordered amount by 32% in the White Deer-to-Silverton CREZ transmission line, and by 53% in the Colorado City-to-Barber Lake transmission line.[34] Staff notes that, under PURA § 36.053, the rates approved in a proceeding are based on original cost, less depreciation, of property used and useful in providing service.[35] While the Commission previously held a contingency of over 14% to be recoverable, Staff argues there is no standard percentage for a permissible contingency and the Commission must make the decision in each case based on that case's unique facts.[36] Staff asserts that disallowances for overruns are appropriate here because PURA § 36.053 does not permit a project to overrun the Commission-approved cost by an unlimited amount.[37]

Regarding the Colorado City-to-Barber Lake transmission line, Staff did not provide specific arguments, aside from the overage, supporting its disallowance.

Regarding the White Deer-to-Silverton CREZ transmission line, Mr. Poole did not dispute that the facilities constructed are used and useful, that the facilities can be included in rate base, or that the updated estimated cost provided by

[34] Staff Ex. 3 (Poole Dir.) at 18-19.

[35] PURA § 36.053(a).

[36] Staff Reply Brief at 9.

[37] Staff Reply Brief at 9.

Sharyland in compliance with Docket No. 37858 is prudent.[38] However, he referenced Staff witness Joe Luna's recommended disallowance in Sharyland's rate case in Docket No. 45414 of $42.8 million for Sharyland's CREZ projects and highlighted Mr. Luna's concerns about the "poor management controls" and "poor project record keeping practices" for those projects.[39] Although Mr. Luna did not specifically mention the White Deer-to-Silverton project, Mr. Poole emphasized that Mr. Luna also did not exclude the project.[40]

### ii. Oncor's Position

Oncor insists it is entitled to recover all capital investments associated with the Colorado City-to-Barber Lake and White Deer-to-Silverton CREZ transmission lines, because: (1) the capital investment in the White Deer-to-Silverton CREZ transmission line has been subject to extensive review without recommendations for disallowance, (2) Staff improperly applies the prudence standard, and (3) the Commission has previously held a contingency of more than 14% to be recoverable through rates.

First, Oncor argues the capital investment in the White Deer-to-Silverton CREZ transmission line is recoverable pursuant to PURA § 36.053(d), as it requires CREZ facilities be found used and useful, prudent, and includable in rate base. The project was also subject to extensive Commission oversight through an

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38 Staff Ex. 52 (Poole Suppl.) at 5.

39 Staff Ex. 52 (Poole Suppl.) at 5.

40 Staff Ex. 52 (Poole Suppl.) at 5-6.

independent CREZ monitor that tracked the cost associated with this investment in compliance Docket No. 37858, as well as an extensive review by Staff in Docket No. 45414, in which Staff made no specific disallowance recommendations for the White Deer-to-Silverton CREZ transmission line.[41]

Second, Oncor argues Staff's recommendations are inconsistent with the standard for evaluating prudence. Oncor describes Mr. Poole's approach to prudence—looking solely at final project costs—as a "mathematical exercise" that can only be employed in retrospect and with the benefit of hindsight.[42] In contrast, Oncor states that it approaches prudence with evidence on the circumstances, information, and options available at the time such investments were made.[43]

Finally, Oncor argues Commission precedent weighs in favor of including more than a 10% contingency in rate base.[44] Staff, Oncor notes, does "not necessarily" claim that the costs in excess of that amount are imprudent,[45] and no party, including Staff, has produced any specific evidence refuting the prudence of any capital investment Oncor seeks to recover.[46] Oncor notes that the Commission previously held a contingency of more than 14% to be recoverable through rates on

[41] Oncor Ex. 40 (Speed Reb.) at 29.

[42] Oncor Initial Brief at 15.

[43] Oncor Initial Brief at 15; *see Tex. Indus. Energy Consumers*, 620 S.W.3d at 428.

[44] *See Entergy Gulf States, Inc. v. Pub. Util. Comm'n of Tex.*, 112 S.W.3d 208, 215-16 (Tex. App.—Austin 2003, pet. denied) (approving the Commission's decision to include in rate base approximately $243 million in contingency costs associated with construction of the River Bend Nuclear Station).

[45] Staff Ex. 52 (Poole Suppl.) at 6; Oncor Reply Brief at 13.

[46] Oncor Reply Brief at 13.

a capital investment that was far greater than those being challenged here.[47] For the aforementioned reasons, Oncor urges the Commission to include both Sharyland CCN projects, along with the rest of Oncor's capital investment, in rate base.

### iii. ALJs' Analysis

The ALJs find Oncor met its burden of proof on this issue. Staff did not recommend a disallowance *specifically associated* with the Sharyland CREZ project when Staff previously reviewed it in Docket No. 45414. More compelling is Oncor's evidence detailing how the Sharyland CREZ project was subjected to extensive oversight by the Commission's independent CREZ monitor. Furthermore, despite Staff's argument that PURA § 36.053 does not inherently permit a project to overrun the cost approved by the Commission by an unlimited amount, Mr. Poole focused his testimony on Oncor's cost estimates and total costs without considering a utility's reasonableness: whether Oncor's actions were reasonable under the circumstances known at that time or why cost variances occurred. Staff's evidence does not rise to a level that rebuts the presumption that Oncor's Sharyland and SDTS capital investments were prudent. Thus, the ALJs find Oncor's capital investments not previously reviewed for prudence, including Oncor's capital investments acquired from Sharyland and SDTS, should be included in rate base as they are prudent, used and useful, and reasonable and necessary.

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[47] *See Entergy Gulf States, Inc.*, 112 S.W.3d at 215-16.

### b. Sharyland's Acquisition of SPS Transmission Line

Oncor seeks to include $23.5 million in rate base for the acquisition of SPS utility plant assets originally acquired by Sharyland and to recover approximately $851,000 through rates for annual amortization associated with the acquisition.[48] Sharyland acquired the assets in question from SPS in 2013 (the Sharyland acquisition), and Oncor subsequently acquired the assets from Sharyland in 2019 through the InfraREIT transaction. Oncor was not a party to the Sharyland acquisition.

In its initial brief, OPUC recommends disallowing the $851,000 annual amortization from Oncor's revenue requirement recovery associated with the $23.5 million Sharyland acquisition premium.[49] Acquisition premiums may be recovered through rates if: (1) the purchase price was not excessive; and (2) specific and offsetting benefits have accrued to ratepayers.[50] OPUC argues it is inappropriate for Oncor to recover the Sharyland acquisition premium through rates because Oncor was not a party to the original 2013 acquisition, Oncor did not prove that the benefits expected to accrue to SPS ratepayers may also accrue to Oncor ratepayers and its system, and the acquisition occurred too long ago—approximately 10 years ago.

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48 OPUC Ex. 8 (Hunt Dir.) at 25.

49 OPUC Initial Brief at 14.

50 *Application of Electra Telephone Company, Inc. for the Transfer of a Certificate of Public Convenience and Necessity from Electra Telephone Company*, Docket No. 8374, Examiner's Report on Remand at 6 (Aug. 1, 1990).

Oncor witness Wesley Speed relied on language from the Commission's final order in Docket No. 41430 to argue that, because the Commission found the purchase price for the Sharyland acquisition reasonable under PURA § 14.101, it should also find it reasonable in this proceeding.[51] He testified that ERCOT customers realized multiple benefits from the acquisition, including a net $98 million in overall transmission cost savings and mitigated environmental impacts through the use of existing facilities rather than new construction.[52]

OPUC witness Steven Hunt disagreed that the Commission had already approved the reasonableness of the Sharyland acquisition in Docket No. 41430, and asserted that Oncor had not justified the recovery of the Sharyland acquisition premium in this proceeding. According to Mr. Hunt, Oncor did not provide evidence of any clear, quantifiable, or substantial net benefits that were realized by ratepayers that would not have been realized had the transaction not occurred.[53] Additionally, he testified that the Commission's determination in Docket No. 41430, concerning the purchase price under PURA § 14.101, was not dispositive of any issue in subsequent rate proceedings before the Commission, such as this one.[54]

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[51] Oncor Ex. 10 (Speed Dir.) at 24.

[52] Oncor Ex. 10 (Speed Dir.) at 24.

[53] OPUC Ex. 8 (Hunt Dir.) at 28.

[54] OPUC Ex. 8 (Hunt Dir.) at 27; *see also Joint Report and Application of Sharyland Utilities, LP, Sharyland Distribution & Transmission Services, LLC and Southwestern Public Service Company for Approval of Purchase and Sale of Facilities, for Regulatory Accounting Treatment of Gain on Sale, and for Transfer of Certificate Rights*, Docket No. 41430, Order at 19, COL No. 8a (Dec. 20, 2013).

The ALJs find OPUC's testimony and arguments compelling. Oncor was not a party to the Sharyland acquisition, which occurred almost 10 years ago, and did not invest the capital to generate the acquisition premium. Further, Oncor failed to provide sufficient evidence to show that the benefits expected to accrue to SPS ratepayers also benefited Oncor's system and ratepayers. Accordingly, the ALJs conclude Oncor has not demonstrated it is eligible to recover the Sharyland acquisition premium in this proceeding, and recommend the Commission exclude the $851,000 annual amortization costs from Oncor's revenue requirement.

### 2. Mobile Generation

#### a. PURA § 39.918 Utility Facilities for Power Restoration After Widespread Power Outage

In 2021, Winter Storm Uri highlighted the need for additional tools to minimize the duration of widespread power outages and aid in the restoration of service after them. During the 87th legislative session, the Texas Legislature passed House Bill (HB) 2438, which enacted PURA § 39.918, Utility Facilities for Power Restoration After Widespread Power Outage. This new statute, in part, authorizes TDUs to:

> lease and operate facilities that provide temporary emergency electric energy to aid in restoring power to the utility's distribution customers during a widespread power outage in which:

(A) the independent system operator has ordered the utility to shed load; or

(B) the utility's distribution facilities are not being fully served by the bulk power system under normal operations.[55]

At issue in this proceeding is whether Oncor's leased mobile generation units permitted under PURA § 39.918 should be included in rate base.

### i. Oncor's Position

Oncor seeks recovery of approximately $3.1 million in invested capital for mobile generation units that it leased under PURA § 39.918(b). As of April 14, 2022, Oncor is leasing 15 mobile generation units with a total capacity equivalent to approximately 11 megawatts (MW) for use as an electrical backup in the event of a widespread outage.[56] Oncor witness Keith Hull testified that the primary use for these mobile generation units is to provide backup power to government agencies, fire departments, police departments, 911 call centers, hospitals, emergency shelters/warming facilities, and water treatment facilities.[57]

Oncor claims it provided extensive support for its mobile generation investment, including: (1) explanations of the bidding process and the factors that

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[55] PURA § 39.918(b)(1).

[56] Oncor Ex. 11 (Hull Dir.) at 26.

[57] Oncor Ex. 11 (Hull Dir.) at 26.

led Oncor to lease the units from Citizens Bank, and why that benefits taxpayers, as well as (2) the lease schedules and acquisition costs for the mobile generation units from Citizens Bank. By securing the mobile generation units through Citizens Bank, Oncor was able to have them in place before the winter season and within months after the legislature passed HB 2438.

### ii. Intervenors' Arguments

A TDU may recover only the reasonable and necessary cost of leasing and operating mobile generation facilities and may only earn a return on invested capital that is used and useful in providing service.[58] Cities, DoD/FEA, and TEAM/ARM argue that Oncor must therefore show that it leased its mobile generators within the narrow permissible parameters of PURA § 39.918. They assert Oncor did not meet its burden because it failed to support the underlying costs; therefore, they seek removal of the costs associated with the mobile generation leases from Oncor's cost of service. Cities and TEAM/ARM also contend Oncor did not use a competitive bidding process in leasing its mobile generation units.

TEAM/ARM recommends deferment of Oncor's recovery until the Commission develops a rule for PURA § 39.918 and Oncor can demonstrate compliance with both the statute and rule.[59]

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[58] PURA § 39.918(h); 16 TAC § 25.231(c)(2).

[59] TEAM/ARM Initial Brief at 6-8.

OPUC, DoD/FEA, and TIEC, however, have more limited requests. OPUC recommends Oncor remove from rate base its leased mobile generation facilities that have not been prepaid or represent invested capital. DoD/FEA recommends an adjustment to include the corresponding liability of $3.1 million, as a rate base offset, because Oncor is only entitled to incur reasonable and necessary costs, which DoD/FEA considers to be the actual costs incurred by Oncor. TIEC raises an issue regarding the appropriate allocation of the costs of mobile generators to customers. This issue is addressed in the cost allocation section of this PFD (see Section VII.B).

#### (a) TEAM/ARM's Arguments Regarding Compliance with PURA § 39.918

TEAM/ARM witness Chris Hendrix explained the roles of the three categories of market participants under PURA: retail electric providers (REPs), power generation companies (PGCs), and TDUs.[60] He identified REPs as being only able to sell electricity to retail customers, not own or operate generation assets; PGCs being only able to own generation and not T&D facilities; and TDUs, like Oncor, being specifically prohibited from owning generation.[61] However, TEAM/ARM recognizes that PURA § 39.918 allows TDUs to lease mobile generation for deployment to protect public safety in the event of widespread power outages caused by load shed or by an outage on the bulk power system. TEAM/ARM emphasizes that Oncor's proposal to recover costs for mobile

[60] TEAM/ARM Ex. 1 (Hendrix Dir.) at 7.

[61] TEAM/ARM Ex. 1 (Hendrix Dir.) at 7-8.

generation is a case of first impression for the Commission.[62] Since TEAM/ARM contends that Oncor's plan addressing deployment and use of its mobile generators does not conform to the limited statutory purpose of PURA § 39.918, it proposes denial of Oncor's requested recovery without prejudice and recommends deferment of Oncor's recovery to a future rate proceeding.[63]

Mr. Hendrix testified that the Commission has opened a rulemaking to implement PURA § 39.918 in Project No. 53404, but a final rule has yet to be adopted.[64] In the interim, TEAM/ARM interprets PURA § 39.918 to have a limited scope as it construes the authority granted to a TDU to lease and operate mobile generation for the purposes of and during the specific emergency grid conditions provided for in subsection (b)(1) of the statute.[65] TEAM/ARM notes that a widespread power outage alone, or a widespread outage that is attributable only to issues with a TDU's distribution facilities, does not fall within the exception allowing a TDU to lease generation equipment.[66]

TEAM/ARM asserts that Oncor incorrectly interprets PURA § 39.918 as a blanket authorization to recover costs to lease and operate mobile generation to be deployed during any and all widespread power outages, including outages caused by a localized failure of its distribution system.[67] Such interpretation is reflected in

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62 TEAM/ARM Initial Brief at 6; *see* TEAM/ARM Ex. 1 (Hendrix Dir.) at 14; PURA § 39.051.

63 TEAM/ARM Initial Brief at 6.

64 TEAM/ARM Ex. 1 (Hendrix Dir.) at 10; *Restoration of Electric Service After a Widespread Power Outage*, Project No. 53404 (pending).

65 PURA § 39.918(b)(1).

66 *See* PURA § 39.918(b)(1); TEAM-ARM Ex 1 (Hendrix Dir.) at 8.

Oncor's policies that omit any consideration of the conditions in subsection (b)(1) yet reference widespread power outage but not load shed or the bulk power system.[68] TEAM/ARM finds this interpretation is fundamentally flawed and reflects Oncor's intent to recover costs for mobile generators that are designed to be used to serve individual customers in the event of any widespread power outage regardless of the cause of the outage.[69]

The definitions of "load shed" and "bulk power system" are important to understanding PURA § 39.918(b)(1). TEAM/ARM witness Hendrix defined "load shed" as an emergency measure used by ERCOT when the demand for electricity on the grid exceeds the supply of available electricity.[70] Mr. Hendrix noted that a load shed order pertains to load on the distribution system.[71]

Regarding the term "bulk power system," TEAM/ARM contends that Oncor improperly disregards this statutory term entirely. Oncor witness Hull testified that a definition of "bulk power system" is not included in PURA § 39.918

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67 Oncor Ex. 41 (Hull Reb.) at 5 ("I am not a lawyer, but a plain reading of that section shows that there is no specific or implied limitation that the damaged facilities that caused the outage must be on the transmission system, or mobile generation cannot be deployed to distribution customers."); *see* TEAM/ARM Ex. 1 (Hendrix Dir.) at 12 (referencing Oncor's response to TEAM Request for Information (RFI) No. 2-6 wherein Oncor "cherry picked aspects of a widespread power outage—lasting/expected to last more than eight hours, affecting a significant number of distribution customers, and posing a risk to public safety").

68 TEAM/ARM Ex. 1 (Hendrix Dir.) at Attach. CH-3; TEAM/ARM Ex. 4 (Public Emergency Plan); Tr. at 315-16.

69 TEAM/ARM Initial Brief at 10.

70 TEAM/ARM Ex. 1 (Hendrix Dir.) at 5.

71 TEAM/ARM Ex. 1 (Hendrix Dir.) at 5.

or any other PURA provision or Commission rule.[72] Using the plain meaning of the term and interpreting it within the context of the statute, TEAM/ARM defined "bulk power system" as "the electrical network comprised of generation facilities and transmission facilities."[73] Mr. Hull acknowledged and agreed with the North American Energy Reliability Corporation's (NERC's) definition of bulk power system: "(A) facilities and control systems necessary for operating an interconnected electric energy transmission network (or any portion thereof); and (B) electric energy from generation facilities needed to maintain transmission system reliability. *The term does not include facilities used in the local distribution of electric energy*."[74]

Finally, TEAM/ARM argues that Oncor's "bare assertions" and "simple references" to portions of PURA § 39.918 on how it plans to operate its mobile generation facilities are conclusory and insufficient to show it will operate them within the confines of PURA § 39.918. TEAM/ARM presents the following as evidence of how Oncor treats mobile generation outside the scope of PURA § 39.918:

- Oncor used its mobile generation unit when neither of the conditions enumerated in PURA § 39.918(b)(1) were present. The incident occurred when Oncor used a mobile generator to restore power at the Faith Community Hospital in Jacksboro, Texas (Jacksboro Hospital), which was served by a single distribution feeder. Jacksboro Hospital was hit by a tornado that caused damage to 34 poles, 32 crossarms, and four transformers on the distribution feeder serving the hospital.[75] Oncor did

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[72] Tr. at 337.

[73] TEAM/ARM Ex. 1 (Hendrix Dir.) at 6.

[74] TEAM/ARM Ex. 1 (Hendrix Dir.) at 6 (emphasis added).

not provide any information that it had received a load shed order from ERCOT, and Oncor admitted the tornado did not damage any portion of its transmission system.[76]

- Oncor is attempting to socialize the costs for that service to all ratepayers.[77] A customer can seek backup generation by purchasing such service from the competitive market (e.g., small gas-powered generators, battery devices).[78] PURA § 39.918 prohibits a TDU from leasing generators as a substitute for this customer-specific back-up generation service.[79] However, Oncor failed to develop policies for the deployment of mobile generation within the limited scope of PURA § 39.918.

- Oncor's policies omit any consideration of the conditions in subsection (b)(1) yet reference widespread power outage but not load shed or the bulk power system.[80] TEAM/ARM contends Oncor's policies show it is only applying the criteria used to define "widespread power outage" but not the criteria to describe the limited circumstances a TDU is permitted to deploy mobile generation.[81] And, to determine there is an outage sufficient to support mobile generation, Oncor only proposes to dispatch Distribution Operations field personnel to confirm a reported outage or interruption of electrical service to Oncor's distribution facilities.[82]

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[75] Oncor Ex. 41 (Hull Reb.) at 3, Exh. KH-R-1.

[76] Oncor Ex. 41 (Hull Reb.) at 3, Exh. KH-R-1.

[77] TEAM/ARM Ex. 1 (Hendrix Dir.) at 8.

[78] TEAM/ARM Ex. 1 (Hendrix Dir.) at 8.

[79] TEAM/ARM Ex. 1 (Hendrix Dir.) at 8.

[80] TEAM/ARM Ex. 1 (Hendrix Dir.) at Attachment CH-3; TEAM/ARM Ex. 4 (Public Emergency Plan); Tr. at 315-16.

[81] TEAM/ARM Ex. 1 (Hendrix Dir.) at Attachment CH-3; TEAM/ARM Ex. 4 (Public Emergency Plan); Tr. at 315-16.

[82] TEAM/ARM Ex. 1 (Hendrix Dir.) at Attachment CH-2.

TEAM/ARM offers two proposals: (1) Oncor defer approval of its cost recovery for mobile generation until Oncor satisfies certain conditions in a future proceeding; and (2) Oncor be required to file a plan detailing how the mobile generation facilities leased now or in the future will be operated only when ERCOT has directed Oncor to shed load or the bulk power system is not serving Oncor's distribution facilities under normal circumstances and in a manner that satisfies all other requirements of PURA § 39.918.[83]

TEAM/ARM believes deferral is reasonable for three reasons. First, Oncor's requested recovery is relatively modest from a pure dollar-and-cents standpoint. Oncor seeks to recover a total rate base of approximately $3.1 million to lease seven mobile generation units, which equates to an annual revenue requirement of $769,171, which, while not insignificant, is just a small part of the $5.8 million per year Oncor seeks to recover through the rates proposed in this proceeding.[84] Second, Oncor has stated its intention to seek recovery of additional costs incurred to lease and operate mobile generation in a future proceeding.[85] The incremental costs for the eight additional units Oncor leased since the end of the test year and the actual costs to deploy and operate mobile generation facilities during a widespread power outage are included in the revenue requirement requested by Oncor.[86] Finally, Oncor has not carried its burden that it is in compliance with PURA § 39.918.

[83] TEAM/ARM Ex. 1 (Hendrix Dir.) at 3, 14.

[84] TEAM/ARM Ex. 1 (Hendrix Dir.) at Attachment CH-4; Oncor Ex. 1 (Application) at Exh. 1.

[85] T EAM/ARM Ex. 1 (Hendrix Dir.) at Attachment CH-4.

[86] TEAM/ARM Ex. 1 (Hendrix Dir.) at Attachment CH-5; Oncor Ex. 11 (Hull Dir.) at 26.

### (b) Cities' and TEAM/ARM's Arguments Regarding Competitive Bidding Process

Cities and TEAM/ARM both argue that Oncor failed to show it used a competitive bidding process or that it was impracticable to do so. Cities' recommendation to remove Oncor's costs related to the mobile generation facilities from its cost of service results in a $257,000 decrease in distribution revenues.[87]

Although Cities supports Oncor's effort to acquire mobile generation units and provide backup power to critical facilities during a widespread outage, it asserts that Oncor failed to establish that the mobile generation facilities lease it ultimately entered into was the most cost-effective and, therefore, that its associated costs were reasonable and necessary. Cities contends that because Oncor acquired the mobile generation facilities under a non-competitive lease, it circumvented the competitive bidding process required.[88] Citing to PURA § 39.918, Cities notes that subsection (j) states that a TDU may only recover "reasonable and necessary" costs associated with facilities that provide temporary emergency electric energy (i.e., mobile generation facilities) in a ratemaking proceeding and subsection (f) requires a utility to "use a competitive bidding process to lease" mobile generation facilities "when reasonably practicable."[89]

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[87] Cities Ex. 3 (Nalepa Dir.) at 15.

[88] Cities Initial Brief at 4.

[89] PURA § 39.918(j), (f).

TEAM/ARM and Cities agree that Oncor provided the following three facts showing it used a competitive bidding process to lease mobile generation: (1) Oncor developed a request for proposals (RFP); (2) Oncor sent the RFP to nine vendors and received eight responses; and (3) the nine vendors were either existing Oncor suppliers or identified through research.[90] In addition, Cities witness Karl Nalepa testified that Oncor selected two suppliers, PowerSecure, Inc. and Darr Equipment Company as a result of its RFP process.[91] However, Cities stresses that Oncor requested one-year leases under its RFP and ultimately entered into an 84-month lease with Citizens Bank. Thus, contrary to Oncor's insistence, Cities maintains it is impractical and misleading to directly compare those leases. Even Oncor concedes it "cannot know what pricing would have been for terms after the one-year rental terms proposed by the suppliers."[92] Cities claims it is probable that the request for pricing leases, if extrapolated to terms similar to the Citizens Bank lease, would be more cost-effective.[93]

Cities argues that Oncor's position that its initiation of the RFP satisfies the competitive bidding process requirement is specious.[94] Cities notes Oncor never executed a lease with the two bidders it selected but instead acquired the facilities under a previously existing non-competitive lease with Citizens Bank, which was not a direct result of the competitive bidding process.[95] Furthermore, in order to

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[90] Oncor Ex. 43 (Buck. Reb) at 4.

[91] Cities Ex. 3 (Nalepa Dir.) at Attachment KJN-5, Attachment KJ.

[92] Oncor Ex. 51 (Fease Reb.) at 22.

[93] Cities Initial Brief at 5.

[94] Oncor Ex. 51 (Fease Reb.) at 21.

[95] Cities Ex. 3 (Nalepa Dir.) at Bates 189.

determine whether the procurement process was sufficiently competitive, TEAM/ARM submits that one must evaluate the entire RFP process, such as criteria that needed to be met to bid on the RFP, the amount of each bid received, and the system used to compare bids.[96]

Cities also argues Oncor did not offer any substantive evidence regarding the reasonableness of the mobile generation facilities' purchase price. This information would enable the Commission to comprehensively assess the reasonableness of Oncor's lease cost because Citizens Bank's mobile generation facility purchase price dictated the facilities' subsequent leasing price. It would also provide transparency in this proceeding of first impression.[97]

Oncor states that it instructed Citizens Bank to purchase the facilities because "each supplier preferred to sell the assets, rather than lease them."[98] Cities challenges this assertion, because a bidder's preference is irrelevant. Cities cites to PURA § 39.918, which provides that the utility must lease the mobile generation facilities through a competitive bidding process. In a competitive bidding process, of import is the terms of the RFP, not a bidder's preference. Thus, another reflection of Oncor's failure to comply with the competitive bidding process.

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[96] TEAM/ARM Initial Brief at 19; TEAM/ARM Reply Brief at 6-7.

[97] Cities Initial Brief at 6.

[98] Oncor Ex. 51 at 21.

For these reasons, Cities and TEAM/ARM contend that Oncor failed to acquire the facilities as required by PURA § 39.918(f).

### (c) DoD/FEA's Arguments Regarding Accounting

DoD/FEA witnesses Lafayette Morgan and Jennifer Rogers explained that, according to U.S. Generally Accepted Accounting Principles (GAAP), Oncor's lease associated with the mobile generation units is properly classified and reported as an operating lease; however, Oncor attempts to reclassify the costs related to the lease to mimic the accounting for a finance lease pursuant to the provisions in PURA § 39.918(j).[99] And that, under GAAP directives, when a finance lease is recorded, the liability section of a utility's balance sheet includes an amount equal to the present value of the future lease payments to recognize the lessee's obligation under the lease.[100] Furthermore, the effect on the financial statements is very different: operating leases recognize only the lease payment expense while finance leases recognize an asset, a liability, depreciation, property taxes, and interest expense.[101]

Oncor included the present value of future lease payments required under the terms of the lease, totaling $3.1 million, in its rate base as plant in service and also included $3.1 million (representing those future lease payments) in the long-term debt component of its capital structure and weighted average cost of

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[99] Oncor Ex. 17 (Ledbetter Dir.) at 22.

[100] DoD/FEA Ex. 2 (Morgan and Rogers Dir.) at 14.

[101] DoD/FEA Ex. 2 (Morgan and Rogers Dir.) at 13.

capital.[102] In doing this, according to DoD/FEA, Oncor attempts to reclassify the costs related to the operating lease to mimic the accounting for a finance lease.[103]

DoD/FEA asserts that PURA § 39.918 allows a utility to recover its actual cost. Here, DoD/FEA maintains that the reasonable and necessary costs are actual costs incurred by Oncor, and they do not include the present value of future payments because Oncor's lease is an operating lease, not a finance lease. Thus, DoD/FEA recommends an adjustment to include the corresponding liability of $3.1 million in Oncor's long-term debt component of its capital structure as a rate-base offset.[104] According to DoD/FEA witnesses Morgan and Rogers, this adjustment is necessary to reflect the true cost Oncor will incur relative to leasing the mobile generation units because under GAAP directives, when a finance lease is recorded, the liability section of the balance sheet also includes an amount equal to the present value of the future lease payments to recognize the lessee's obligation under the lease.[105] The effect of recording this liability has a $0 effect on the balance sheet, and, without the adjustment, Oncor will receive a windfall of $210,000.[106]

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[102] Oncor Ex. 17 (Ledbetter Dir.) at 22.

[103] Oncor Ex. 17 (Ledbetter Dir.) at 101.

[104] DoD/FEA Ex. 2 (Morgan and Rogers Dir.) at 14.

[105] DoD/FEA Ex. 2 (Morgan and Rogers Dir.) at 14.

[106] DoD/FEA Ex. 2 (Morgan and Rogers Dir.) at 14.

### (d) OPUC's Arguments Regarding Recovery

OPUC recommends (1) removing from rate base Oncor's leased generating facilities that have not been prepaid or represent invested capital, and (2) excluding incremental costs associated with mobile generation operations that Oncor proposed to include in a regulatory asset. OPUC also recommends those incremental costs be defined.[107]

Oncor proposes to include $3.1 million of operating lease payments for mobile generation units in rate base.[108] As discussed above, Oncor reclassified these operating leases as finance leases to reflect the present value of future payments required under the lease in Oncor's rate base and the long-term debt components on Oncor's capitalization and weighted average cost of capital calculation.[109] OPUC argues that Oncor's proposal to include the operating lease in rate base is not consistent with the intent of PURA § 39.918, because subsection (j) does not guarantee rate recovery—the costs of capital finance leases may be presented for rate recovery—and qualifies the rate recovery of capital finance leases to those costs that are reasonable and necessary.[110] Thus, the practical implementation of this provision, according to OPUC witness Hunt, is to allow rate base treatment for capital finance leases that have been prepaid.[111] Mr. Hunt testified it would be unreasonable to provide rate base treatment on the present value of future

107 OPUC Initial Brief at 18, 20.

108 OPUC Initial Brief at 18.

109 OPUC Ex. 33 (Evans Cross-Reb.) at 14; Oncor Ex. 45 (Ledbetter Dir.) at 22.

110 OPUC Ex. 8 (Hunt Dir.) at 36.

111 OPUC Ex. 8 (Hunt Dir.) at 36.

payments, which do not represent current or previously invested capital.[112] Therefore, to the extent the leases are not prepaid or represent actual capital, OPUC recommends capital lease costs be excluded from rate base and determined to be unreasonable for a return.[113]

Because Oncor expects to incur incremental costs above the amounts in its requested rates due to having leased an additional eight mobile generation units and to not include in its requested rate the costs to deploy and operate those additional units, Oncor seeks to defer them.[114] Although Oncor stated that incremental costs includes several categories, Oncor does not demonstrate that its definition of "incremental costs" will be limited to costs that are not already incurred.[115] OPUC asserts that Oncor must provide more clarity on what its incremental costs will be and how those costs will be distinguished from costs already included in this rate proceeding.[116] Thus, OPUC recommends that costs includable in Oncor's proposed regulatory asset for incremental costs associated with mobile generation operations be clearly defined and that the costs included in rate base be excluded.[117]

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[112] OPUC Ex. 8 (Hunt Dir.) at 37.

[113] OPUC Ex. 8 (Hunt Dir.) at 37-38.

[114] OPUC Ex. 8 (Hunt Dir.) at 38, Attach. SDH-21.

[115] OPUC Ex. 8 (Hunt Dir.) at 39 (providing the example that incremental costs should not include any project costs for the deployment of mobile generation in an event where the technicians employed are existing Oncor staff).

[116] OPUC Ex. 8 (Hunt Dir.) at 39.

[117] OPUC Initial Brief at 20; OPUC Ex. 8 (Hunt Dir.) at 39.

### iii. Oncor's Response

Oncor disputes each of the intervenors' challenges to its right to recover costs associated with leasing mobile generation units pursuant to PURA § 39.918. Compliance with PURA § 39.918

According to Oncor, TEAM/ARM's proposal for Oncor to develop a plan demonstrating how it will comply with PURA § 39.918 has no statutory basis. Oncor argues TEAM/ARM cites no authority requiring Oncor to develop such a plan ***before*** it may recover its mobile generation costs, and the statute contains no such requirement.[118] Instead, Oncor cites to the plan it is required to develop, and has developed, under the statute which is "a detailed plan on the utility's use of [mobile generation] facilities" for inclusion in Oncor's Emergency Operations Plan (EOP).[119]

Oncor insists that it is also irrelevant that Oncor's EOP does not specifically use the terms "load shed" or "bulk power system" since the statute simply requires a plan detailing that "the utility will use its mobile generation facilities" and not the depth of explanation TEAM/ARM seek. Oncor asserts its EOP demonstrates how Oncor complies with the statute without using the specific terms.[120]

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[118] Oncor Reply Brief at 16.

[119] PURA § 39.918(g).

[120] Oncor Reply Brief at 17.

Oncor challenges TEAM/ARM's interpretation of the statute that an issue with the transmission system is a requirement for the use of mobile generation. Initially, TEAM/ARM raises concerns that Oncor has not and will not comply with PURA § 39.918, specifically, subsection (b)(1), which outlines when a mobile generator may be deployed. Oncor disagrees and argues that, because PURA § 39.918 focuses on issues with the distribution system, it permits deployment of mobile generation when Oncor's "distribution facilities are not being fully served by the bulk power system."[121] This scenario occurred with the Jacksboro Hospital, which did not receive power from the bulk power system for 18 hours.[122]

Oncor witness Hull testified that for 18 hours, Jacksboro Hospital was without grid power after a tornado damaged Oncor's distribution system and was not "being fully served by the bulk power system."[123] According to Oncor, TEAM/ARM's interpretation of the statute would prohibit Oncor from providing emergency backup power to critical facilities simply because there was no damage to Oncor's transmission system, which Oncor insists is not what the Texas Legislature intended.[124] Instead, Mr. Hull testified that a plain reading of the statute does not provide a specific or implied limitation that the damaged facilities causing the outage must be on the transmission system or Oncor is prohibited from

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[121] PURA § 39.918(b)(1)(B) (emphasis added). *See* PURA §§ 39.918(a)(1) (defining "widespread power outage" as an event that affects a significant number of ***distribution*** customers); 39.918(b)(1) (allowing TDUs to lease mobile generation to restore power to its ***distribution*** customers); and 39.918(b)(1)(B) (allowing mobile generation when the utility's ***distribution*** facilities are not being fully served by the bulk power system).

[122] Oncor Ex. 41 (Hull Reb.) at 3-4.

[123] Oncor Ex. 41 (Hull Reb.) at 3.

[124] Oncor Ex. 41 (Hull Reb.) at 3.

deploying mobile generation to distribution customers.[125] As an example, Mr. Hull explained that a number of customers still suffered widespread power outages after the load shedding events during Winter Storm Uri.[126] Under TEAM/ARM's interpretation, Mr. Hull testified that these customers would have to do without electrical service and no mobile generation units could have been provided to them after the load shed event was over because the transmission was not damaged during the storm.[127] Oncor asserts adoption of TEAM/ARM's interpretation would cause an absurd result by prohibiting Oncor from deploying mobile generation to customers in situations similar to the Jacksboro Hospital's 18-hour power outage.[128]

Finally, Oncor disputes TEAM/ARM's claims that Oncor has not demonstrated that its mobile generation units are reasonable and necessary and that Oncor will not operate or deploy the mobile generation in accordance with PURA § 39.918, specifically subsections (c), (d)(1), (d)(2), and (e). Oncor maintains these assertions are merely speculative and have no basis in fact because Oncor witnesses Mr. Hull and Daniel Hall fully addressed those issues, as detailed below.[129]

First, PURA § 39.918(c) prohibits a TDU from selling electric energy or ancillary services from its leased mobile generation facilities. Mr. Hull testified that

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[125] Oncor Ex. 41 (Hull Reb.) at 5.

[126] Oncor Ex. 41 (Hull Reb.) at 5.

[127] Oncor Ex. 41 (Hull Reb.) at 5.

[128] Oncor Ex. 41 (Hull Reb.) at 3-4; TEAM/ARM Initial Brief at 14-15.

[129] TEAM/ARM Ex. 1 (Hendrix Dir.) at 12-14; *see* Oncor Ex. 41 (Hull Reb.) at 4-7; Oncor Ex. 44 (Hall Reb.) at 2-3.

Oncor has no plans to sell electric energy or ancillary services from mobile generation facilities.[130]

Second, Mr. Hull testified that Oncor will ensure its mobile generation facilities are operated in isolation from the bulk power system pursuant to PURA § 39.918(d)(1).[131] Oncor will: (1) look at each deployment on a case-by-case basis; (2) have field personnel who will work with Oncor's Distribution Operation Centers to ensure devices are isolated with no possibility of back feed onto the Oncor system; and (3) have field personnel visually inspect the generators to verify that they are operating in isolation.[132]

Third, regarding PURA § 39.918(d)(2), Mr. Hull explained Oncor does not send cost information to ERCOT, only usage and system information; thus, Oncor will not submit any information concerning the cost of mobile generator leases to ERCOT.[133] Consequently, ERCOT cannot include the usage information or the costs of mobile generation in its pricing calculations or its realizability models.[134]

Lastly, regarding PURA § 39.918(e), Mr. Hall addressed Oncor's process for ensuring the retail customers' usage during operation of a mobile generator will not be included in the usage reports to REPs for billing purposes.[135] Essentially, when a

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130 Oncor Ex. 41 (Hull Reb.) at 5-6, Exh-R-4 (responding to a TEAM RFI on PURA § 39.918(c) that Oncor "has not sold" nor "will not sell").

131 Oncor Ex. 41 (Hull Reb.) at 6, Exh. KH-R-5.

132 Oncor Ex. 41 (Hull Reb.) at Exh. KH-R-5.

133 Oncor Ex. 41 (Hull Reb.) at 6.

134 Oncor Ex. 41 (Hull Reb.) at 6-7.

mobile generation facility is connected to a customer's premises, Oncor will remove the customer's billing meter, replace it with a temporary meter so that no consumption is measured, and issue a temporary disconnect order. After the event is complete, Oncor will remove the temporary meter, reinstall the customer's original meter, and remove the temporary disconnect order.[136] Then, to ensure no usage is posted against the customer's account while the mobile generation facility is connected to the customer's premise, Oncor will analyze the usage information.[137]

Through a multi-level review process, Oncor will carefully consider the entirety of PURA § 39.918 when it determines how and when to deploy the mobile generation units based on the particular set of circumstances before it.[138] Oncor asserts that not only has it deployed its mobile generator in accordance with the statute, but it will continue to comply with the statute and other PURA provisions, the Commission's rules, and Oncor's Commission-approved tariff in any deployment of mobile generation units.[139]

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[135] Oncor Ex. 41 (Hull Reb.) at 7; Oncor Ex. 44 (Hall Reb) at 2-3.

[136] Oncor Ex. 44 (Hall Reb.) at 2-3, Exh. DEH-R-1.

[137] Oncor Ex. 44 (Hall Reb.) at 2-3, Exh. DEH-R-1.

[138] Oncor Ex. 41 (Hull Reb.) at 4-5.

[139] Oncor Ex. 41 (Hull Reb.) at 3-7; Oncor Ex. 44 (Hall Reb.) at 2-3.

### (a) Competitive Bidding Process

Oncor witness Ellen Buck noted that a competitive bidding process is not mandatory for a utility to recover its costs; rather, a competitive bidding process is only required by PURA § 39.918(f) when "reasonably practicable."[140] Nonetheless, Oncor used a RFP process to secure two different supplies for its leased mobile generation facilities.[141] Oncor sent an RFP to nine suppliers—three were existing suppliers for Oncor and the remaining six were determined, through Oncor's market knowledge and research, to have the capability to meet the requirements of the RFP.[142] Oncor received eight responses and selected two suppliers for further evaluation—one for larger size mobile generation facilities (625 kilowatt (kW) capacity and above) and one for smaller size facilities (under 625 kW capacity).[143]

After Oncor conducted a financial review of the lease/rental agreements from the supplier of the larger size facilities, Oncor determined it would be more cost-effective to lease the units through one of its existing fleet lease vendors: Citizens Bank.[144] Citizens Bank had leased Oncor vehicles and equipment since 2008. Citizens Bank offered leasing financial terms that, according to Oncor witness Kevin Fease, were significantly more favorable to Oncor than those proposed by the two other suppliers. In addition to better pricing, Oncor was able to secure a seven-year contract with Citizens Bank—a longer term than the

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[140] Oncor Ex. 43 (Buck Reb.) at 3-4.

[141] Oncor Ex. 43 (Buck Reb.) at 3.

[142] Oncor Ex. 43 (Buck Reb.) at 4.

[143] Oncor Ex. 43 (Buck Reb.) at 4; Oncor Ex. 51 (Fease Reb.) at 21.

[144] Oncor Ex. 51 (Fease Reb.) at 22.

one-year term offered by the respondents to Oncor's RFP process. Mr. Fease testified that Oncor's RFP process indicated that monthly rents across the board from suppliers were consistently higher than the terms offered by Citizens Bank. Oncor had contacted the supplier of the smaller size facilities about using a similar lease arrangement through Citizens Bank; Citizens Bank's pricing terms were more favorable.[145]

Through its RFP process and market research, Oncor found that there was high demand for mobile generation facilities in the marketplace and that agreements with suppliers would need to be entered into in a relatively short timeframe to secure assets meeting its needs and to have them in place before the winter season.[146] Considering the high demand, Mr. Fease testified it was prudent to secure them for longer terms to ensure their availability to help restore power to customers in the event of a widespread power outage.[147] Furthermore, Oncor did not know whether the rental fees would increase after the proposed one-year rental terms or even if the relationship would be terminated.[148] Leasing the assets with Citizens Bank, as opposed to entering into annual leases with suppliers, gave Oncor the needed certainty regarding continued availability and pricing of the assets.[149]

Mr. Fease testified that under PURA § 39.918, Oncor is only permitted to lease, not own, the mobile generation units; thus, there was no reason for Oncor to

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[145] Oncor Ex. 51 (Fease Reb.) at 22.

[146] Oncor Ex. 43 (Buck Reb.) at 4.

[147] Oncor Ex. 51 (Fease Reb.) at 22.

[148] Oncor Ex. 51 (Fease Reb.) at 22.

[149] Oncor Ex. 51 (Fease Reb.) at 22.

request purchase prices in its RFP.[150] Citizens Bank negotiated the purchase prices directly with the suppliers, and Oncor was not a party to those negotiations.[151]

Oncor, therefore, insists it provided ample evidence that it used a competitive bidding process in leasing its mobile generation units, including information regarding: (1) its RFP to nine suppliers and further evaluation of two of those suppliers; (2) the market conditions that led Oncor to explore options beyond just those two bidders; (3) how Oncor leveraged an existing master lease agreement to secure the desired units from the competitive bidders indirectly through a third party and for a lower monthly lease cost; (4) its entry into a long-term agreement to ensure the units are available when needed for the next seven years; (5) the lease schedules showing the units' acquisition costs and the monthly cost to Oncor under the lease; and (6) testimony from Ms. Buck, whose organization was responsible for procurement.[152] Oncor also noted neither PURA nor the Commission's prudence standard necessarily require utilities to choose the "most cost-effective" option; instead, they allow utilities to choose from a "range of reasonable options."[153] Oncor explains that it chose the most reasonable option available at the time, which ultimately cost less than other options. Thus, Oncor argues its evidence demonstrates that it used a competitive bidding process to lease the mobile generation units, that the resulting costs are reasonable and necessary,

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150 Oncor Ex. 51 (Fease Reb.) at 23.

151 Oncor Ex. 51 (Fease Reb.) at 22.

152 Oncor Ex. 43 (Buck Reb.) at 3-4; Oncor Ex. 51 (Fease Reb.) at 21-22; Oncor Ex. 15 (Buck Dir.) at 4-8.

153 *Tex. Indus. Energy Consumers*, 620 S.W.3d at 428.

and that it is entitled to recover those costs in this proceeding under PURA § 39.918(h).

### (b) Appropriate Costs for Mobile Generation Leases are included

Oncor disagrees with both of OPUC's recommendations. First, PURA § 39.918 does not require lease payments be prepaid and even FERC USOA general instructions consider leasing to involve periodic payments, not prepayments.[154] More importantly, according to Oncor, OPUC's argument contradicts the plain statutory language expressly stating that the Commission "shall permit" recovery of "the ***present value of future payments*** required under the lease."[155]

Second, Oncor addresses OPUC's recommendation that Oncor clearly define the costs included in the regulatory asset for the incremental operating costs and the return, not otherwise recovered in this case, associated with leasing or procurement, ownership, and operation of the mobile generation facilities and to exclude any costs included in rate base. Oncor contends this recommendation is unfounded because the record reflects that Oncor clearly identified amounts relating to mobile generation that it has requested be included in base rates.[156] And,

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[154] Oncor Ex. 45 (Ledbetter Reb.) at 46-47 (referencing FERC USOA General Instructions No. 19-Criteria for Classifying Leases and No. 20-Accounting for Leases).

[155] Oncor Ex. 45 (Ledbetter Reb.) at 47 (citing PURA § 39.918(h)(1)).

[156] Staff Ex. 33 (Staff RFI 10-01).

consistent with PURA § 39.918(i), Oncor will defer any other mobile generation-related costs that are not included in base rates.[157]

Finally, Oncor postulates that it and other TDUs will be disincentivized from investing in and using mobile generating units if recovery of their investment is deferred until the Commission develops a rule implementing PURA § 39.918.[158] Oncor contends TEAM/ARM's suggestion is flawed. HB 2483 identified a "need for additional tools to help [TDUs] reduce the duration or impact of [widespread electricity] outages."[159] As codified in PURA § 39.918, it provides that the Commission ***shall*** permit recovery of reasonable and necessary costs for mobile generation but makes no mention of the need for a rulemaking or a requirement that the Commission develop a rule before allowing cost recovery.[160]

Oncor, therefore, seeks recovery of its mobile generation costs.

#### iv. ALJs' Analysis

Under PURA § 39.918(b)(1), a TDU may "lease and operate facilities that provide temporary emergency electric energy to aid in restoring power to the utility's distribution customers during [certain] widespread power outages."[161] The

157 Oncor Reply Brief at 20.

158 Oncor Reply Brief at 20-22.

159 Bill Analysis, Tex. H.B. 2483, 87th Leg., R.S. (May 14, 2021).

160 PURA § 39.918.

161 PURA § 39.918(b)(1).

TDU may recover "the reasonable and necessary costs of leasing and operating the facilities, including the present value of future payments required under the lease, using the rate of return on investment established in the commission's final order in the utility's most recent base rate proceeding."[162] Furthermore, a TDU may request recovery of the reasonable and necessary costs of leasing and operating facilities that provide temporary emergency electric energy, including any deferred expenses, "through a proceeding under Section 36.210 or in another ratemaking proceeding."[163]

For the reasons discussed below, the ALJs find that Oncor's use of the mobile generation units did not comply with PURA § 39.918 and therefore Oncor did not meet its burden to prove its costs were prudently incurred and reasonable and necessary.

PURA § 39.918(f) states that a TDU "shall, when reasonably practicable, use a competitive bidding process to lease facilities under subsection (b)(1)." The Code Construction Act, in chapter 311 of the Texas Government Code, instructs reading words and phrases in context and construing them according to the rules of grammar and common sense.[164] Here, subsection (f) imposes a duty.[165] The American Heritage Dictionary defines "practicable" as "capable of being effected, done, or put into practice."[166] And, a competitive bidding process is designed to be

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[162] PURA § 39.918(h)(1).

[163] PURA § 39.918(j).

[164] Tex. Gov't Code § 311.011(a).

[165] *See* Tex. Gov't Code § 311.016(2) (declaring that "shall" imposes a duty).

fair and open. Considering this context, the ALJs agree with Cities and TEAM/ARM that subsection (f) requires a utility to use a competitive bidding process when reasonably practicable.

The ALJs find Cities and TEAM/ARM presented compelling evidence that Oncor did not use a competitive bidding process and that Oncor failed to show that it was not reasonably practicable to do so. Although Oncor initiated the RFP process, Oncor did not complete the process: Oncor stopped the competitive bidding process once a more favorable, in its estimation, offer appeared outside of its RFP process.

The ALJs also agree it is impracticable and misleading to compare the terms of the one-year lease under the RFP, which Oncor set, with the terms of the seven-year lease offered by Citizens Bank. Furthermore, Oncor assumes Citizens Bank's lease is more cost-effective despite not comparing offers from its other vendors or knowing how the terms of a one-year lease would change upon renewal.

The ALJs are also persuaded by TEAM/ARM's evidence that Oncor's plan addressing deployment and use of its mobile generators does not conform to the limited statutory purpose of PURA § 39.918. The ALJs are not convinced by Oncor's primarily blanket claims that it will deploy mobile generation in accordance with PURA § 39.918, specifically subsections (c), (d)(1), (d)(2), and (e).

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[166] American Heritage Dictionary, https://www.ahdictionary.com/word/search.html?q=practicable (last visited Dec. 4, 2022).

The ALJs agree with TEAM/ARM's interpretation of the statute that PURA § 39.918 creates an exception for TDUs in PURA to lease and operate mobile generation only under the specific conditions listed in the statute: during a widespread power outage when ERCOT has ordered the utility to shed load or when the TDU's distribution facilities are not being fully served by the bulk power system under normal operations.[167]

As TEAM/ARM explained, "load shed" pertains to load on the distribution system while the "bulk power system," as defined by NERC, applies to the transmission system and does not include facilities used in the local distribution of electric energy. Therefore, when ERCOT orders a TDU to shed load pursuant to PURA § 39.918 (b)(1)(A), a TDU's distribution system applies. However, PURA § 39.918 (b)(1)(B) allows a TDU to lease temporary generators to deal with a situation in which the transmission system, not its own distribution system, goes down. TEAM/ARM credibly argued that when Oncor used a mobile generator to restore power at Jacksboro Hospital, when Oncor did not receive a load shed order from ERCOT and the tornado did not damage any portion of the transmission system, Oncor failed to comply with the requirements of PURA § 39.918(b)(1).

Therefore, the ALJs find Oncor did not comply with the competitive bidding requirements under PURA § 39.918(f) and that Oncor's use of the mobile generating units exceeded the explicitly limited purposes set out in PURA § 39.918(b)(1). Accordingly, the ALJs recommend the Commission deny Oncor's

[167] PURA § 39.918(b)(1).

request for recovery of its invested capital associated with mobile generation units leased under PURA § 39.918(b).

The ALJs reject TEAM/ARM's suggestion that Oncor must file a plan with the details TEAM/ARM outlined. Only subsection (g) requires TDUs to file a plan, which Oncor already has. The ALJs recommend the Commission not adopt TEAM/ARM's recommendation for Oncor to file a detailed plan separate from the plan required under PURA § 39.918(g).

Alternatively, due to the Commission's pending Project No. 53404, the ALJs find TEAM/ARM's recommendation to defer the requested costs until the Commission develops a rule for PURA § 39.918, and, at which point Oncor can demonstrate compliance with both the statute and rule, a reasonable approach. However, due to the uncertainty of when or if a rule may be adopted, the ALJs conclude it is prudent to defer the issue to a future rate proceeding instead of hinging the deferment on the development or adoption of a rule. Accordingly, if the Commission wishes to defer ruling on this issue, the ALJs recommend the Commission defer Oncor's request for recovery of its invested capital associated with mobile generation units leased under PURA § 39.918(b) until a future rate proceeding. Additionally, if the Commission defers this issue, the ALJs also recommend the Commission require Oncor to create a regulatory asset to track its costs associated with leasing 15 mobile generation units along with the associated incremental costs.

Because the ALJs recommend denial, or, in the alternative, deferral, of Oncor's costs associated with mobile generating units, the ALJs did not address the remaining issues regarding DoD/FEA's and OPUC's recommendations that are applicable only if Oncor's requested costs were approved.

### 3. AFUDC Being Transferred to Invested Capital

Allowance for Funds Used During Construction (AFUDC) accrues on construction work in progress (CWIP) while construction is continuing. AFUDC is an entry in a utility's books to indicate the cost of capital used during construction and does not represent a transfer of funds. Once construction is complete and the facility operational, CWIP and AFUDC are transferred to the utility's rate base and the utility begins to earn a return on its investment in both.[168]

Oncor's policy defines "AFUDC" as "a cost accounting procedure whereby amounts based upon interest charges on borrowed funds and a return on equity capital used to finance construction are charged to electric plant."[169] Mr. Ledbetter testified that Oncor capitalizes AFUDC on all active work projects involving construction periods lasting greater than 30 days.[170] Oncor's AFUDC accruals, which begin the month after construction commences, are calculated based on Oncor's consolidated capital structure, which results in each business function having the same AFUDC accrual rate each month.[171] In Schedule II-B-15A, Oncor

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[168] *Cities for Fair Util. Rates v. Public Util. Comm'n of Tex.*, 924 S.W.2d 933, 935-36 (Tex. 1996).

[169] Oncor Ex. 17 (Ledbetter Dir.) at 29.

[170] Oncor Ex. 17 (Ledbetter Dir.) at 29.

provides information concerning the accrual of AFUDC. Oncor calculated and transferred to plant in service AFUDC in the amount of $139.2 million from 2017 through 2021.[172]

### a. OPUC's Position

Here, only OPUC challenges Oncor's AFUDC accruals applied to CWIP projects in the years 2017 through 2021 by asserting the 2019 accrual level is overstated by $4.9 million as a result of an accounting discrepancy.[173] Thus, OPUC proposes to remove $0.571 million from the revenue requirement.[174] However, Mr. Ledbetter explained that no accounting discrepancy exists, that OPUC's claim is a misstatement of the record and an overstatement of the alleged discrepancy, and that OPUC relied on Federal Power Commission (FPC) Order 561 issued circa 1977 and failed to apply more recent interpretive guidance of FPC Order 561.[175] FPC Order 561 established the FERC accounting regulations on AFUDC.[176] Specifically, FPC Order 561 requires an adjustment to the AFUDC rate if the AFUDC rate used throughout the year is more than 25 basis points higher than the rate determined based on the inclusion of year-end actuals for short-term debt and CWIP.

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[171] Oncor Ex. 17 (Ledbetter Dir.) at 29.

[172] Oncor Ex. 2 (Non-Voluminous Schedules) at Schedule II-B-15A.

[173] OPUC Ex. 8 (Hunt Dir.) at 33.

[174] OPUC Ex. 8 (Hunt Dir.) at 8.

[175] Oncor Ex. 45 (Ledbetter Reb.) at 42-45. FPC is the predecessor of FERC. *Id.*

[176] OPUC Ex. 8 (Hunt Dir.) at 31.

OPUC argues that Oncor did not properly follow the AFUDC requirements for year-end adjustments stated in FPC Order 561 and 561-A.[177] Based on Mr. Hunt's review of Oncor's AFUDC capitalization, OPUC determined that in 2019, the AFUDC rate used during the year was 91.6 basis points lower than the year-end AFUDC rate, which resulted in Oncor recording additional AFUDC amounts of $4.9 million.[178] Mr. Hunt believed these AFUDC amounts were capitalized to construction projects in 2019 and are now included in Oncor's proposed rate base and relevant revenue requirement.[179]

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177 OPUC Ex. 8 (Hunt Dir.) at 31-32. As it pertains to year-end adjustment, FPC Order 561 states, in part:

> We are modifying the proposed rule to provide that the balances of long-term debt, preferred stock, and common equity for use in the formula for the current year will be the balances in such accounts at the end of the prior year; the cost rates for long-term debt and preferred stock will be the effective weighted average cost of such capital. The average short-term debt balances and related cost and the average construction work in progress balance will be estimated for the current year. We shall require, however, that public utilities and natural gas companies monitor their actual experience and adjust to actual at year-end if a significant deviation from the *estimate should occur. For this purpose we shall consider a significant deviation to exist if the gross AFUDC rate exceeds by more than one-quarter Of a percentage point (25 basis points) the rate that is derived from the formula by use of actual 13 monthly balances of construction work in progress and the actual weighted average cost and balances for short-term debt outstanding during* the year. [Emphasis added].

*Id.*

178 OPUC Ex. 8 (Hunt Dir.) at 32.

179 OPUC Ex. 8 (Hunt Dir.) at 32.

OPUC also contends that Oncor, without Commission authorization, deviated from the FERC accounting regulations by computing AFUDC on a monthly basis.[180] Furthermore, OPUC witness Hunt testified that FPC Order 561's provision for year-end adjustments should only be used to lower the AFUDC rate and related AFUDC capitalized.[181] This provision for year-end adjustments should also only adjust short-term debt and CWIP estimated balances with year-end actuals.[182] Mr. Hunt explained that the driver of Oncor's significant deviation in 2019 related to equity, rather than differences caused by actuals for short-term debt and CWIP.[183]

Finally, in response to Oncor's assertion that OPUC did not consider the guidance on FPC Order 561, OPUC argues the audit reports, which are generally issued to a specific entity under delegated authority, are not precedent. Therefore, OPUC argues, these reports cannot override or clarify an FPC or FERC order. Doing so would not afford the due process to parties who were not involved in the audit.[184] OPUC argues the interpretation document Oncor cites is not a FERC-issued document but merely a survey sponsored by industry. According to OPUC, this survey neither supports Oncor's position nor does it clarify or broaden FPC

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180 OPUC Ex. 8 (Hunt Dir.) at 8; *see also* OPUC Ex. 8 (Hunt Dir.) at Attach. SHD-14 (FERC order granting an Illinois utility's request for a waiver of certain requirements of FPC Order 561 to allow for the monthly calculation of AFUDC rates based on the utility's representation its monthly AFUDC rate computations will not result in AFUDC amounts recoded in excess of that prescribed on FPC Order 561).

181 OPUC Ex. 8 (Hunt Dir.) at 33.

182 OPUC Ex. 8 (Hunt Dir.) at 33.

183 OPUC Ex. 8 (Hunt Dir.) at 33.

184 OPUC Reply Brief at 7-8.

Order 561. Rather, OPUC contends it reinforces the fact pattern articulated in FPC Order 561.

### b. Oncor's Position

Oncor insists that its accounting practice is consistent with FPC Order 561 and subsequent guidance and that OPUC ignores the 1992 FERC Biennial Report of Major Utilities. The report, which addressed "Compliance Audit Issues," noted that "Order No. 561 requires that the actual AFUDC rate be used when it *differs* from the estimated rate by 25 or more basis points."[185] Oncor acknowledges that the examples in the report addressed excess rather than under-accruals, as with Oncor's 2019 under-accrual, but Oncor claims FERC audits of under-accruals would not have been aggressively pursued.[186] Furthermore, Mr. Ledbetter testified that FERC guidance on the application of FPC Order 561 provides for period-end true-up of AFUDC accruals that differ from the estimate by 25 or more basis points.[187] And Oncor posits that if AFUDC accruals are only subject to downward adjustments, as OPUC argues, there would be an incentive to over-accrue AFUDC calculations, rather than updating the monthly accruals "for the current year with appropriate adjustments as actual data becomes available," because Oncor would

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[185] Oncor Ex. 45 (Ledbetter Reb.) at 43-45, Exh. WAL-R-5; Oncor Reply Brief at 22; *see* OPUC Initial Brief at 6-7.

[186] *See* Oncor Ex. 45 (Ledbetter Reb.) at 44.

[187] Oncor Ex. 45 (Ledbetter Dir.) at 45; *see* Oncor Ex. 45 (Ledbetter Dir.) at Exh. WAL-R-5, page 2.

have made no adjustment despite the fact that an even greater amount of AFUDC would have been recorded than the actual level.[188]

Finally, Oncor argues that, even if OPUC's reasoning is appropriate, its request should be denied because it is improperly quantified based on an over-estimation of the effects of the under-accrual: the electric plant investment that Mr. Hunt claims to be overvalued has been subject to depreciation through the entire period since Oncor placed those construction projects into service.[189] According to Oncor, OPUC fails to account for this in its recommendation.

Oncor argues Mr. Hunt's suggestion that Oncor must have a waiver or modification from FERC or the Commission to adjust its AFUDC estimates monthly is unsupported. In fact, Mr. Ledbetter noted FERC's criticism of a utility for failing to exercise the practice of monthly adjustments that Oncor utilized.[190] Thus, according to Oncor, OPUC's proposed AFUDC-related adjustment should be disregarded.

### c. ALJs' Analysis

At issue is whether the calculation of AFUDC in 2019 should be adjusted. OPUC credibly argued that Oncor may not rely on a survey of audits to provide

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[188] Oncor Ex. 45 (Ledbetter Reb.) at 44 (citing FERC USOA Electric Plant Instruction No. 17(b)).

[189] Oncor Ex. 45 (Ledbetter Reb.) at 45.

[190] Oncor Ex. 45 (Ledbetter Reb.) at 44-45.

guidance on FPC Order 561. But OPUC also relied on a specific and inapplicable order from FERC to support its contention that a waiver is required for Oncor to adjust its AFUDC estimates on a monthly basis. That FERC order involves an Illinois utility and did not refer to the final disposition in that case as the order itself notified the party of its right to appeal the FERC decision. Neither OPUC nor Oncor may rely on FERC orders that hold no precedence. Hence, the ALJs were not persuaded by Oncor's survey of audits or OPUC's FERC order.

However, the ALJs are persuaded by Oncor's arguments that AFUDC accruals are not only subject to downward adjustments, and any over-estimation of the effects of OPUC's alleged under-accrual in 2019 are alleviated as those investments have been subject to depreciation. Furthermore, the ALJs find Oncor appropriately calculated and transferred to plant in service AFUDC in the amount of $139.2 million from 2017 to 2021, and supported the requirements for complete statement for the methods, procedures, and calculations followed in capitalizing the AFUDC.

The ALJs recommend Oncor's AFUDC amount be included in rate base.

### 4. Electric Plant Held for Future Use

Electric plant held for future use (EPHFU) represents tracts of land acquired for future construction of T&D facilities. Oncor identified $26.7 million in

EPHFU.[191] Oncor requests that $23.2 million of EPHFU be included in rate base.[192] Oncor notes that the EPHFU investments it seeks to include in rate base are included within its 10-year planning horizon as they were acquired for the future construction of necessary switching stations, substations, and transmission line right-of-way.[193] Oncor does not seek recovery for other properties in this account that it does not expect to place in service in the next 10 years.[194]

Only DoD/FEA challenged Oncor's right to recover the return on its EPHFU investments. DoD/FEA claims that Oncor's right to recover the return on its EPHFU investment provides an opportunity for potential over-recovery. And, regardless of whether it will be in service within 10 years, DoD/FEA posits Oncor's EPHFU is not used and useful until facilities are constructed on the land.

Oncor argues it is entitled to recover the cost of those properties as prudently incurred and reasonable and necessary costs for three reasons:

- DoD/FEA's arguments directly contradict controlling precedent set by *Cities for Fair Utility Rates v. Public Utility Commission of Texas*, 924 S.W.2d 933 (Tex. 1996).[195] Pursuant to the Texas Supreme Court's holding in *Cities for Fair Utility Rates,* Oncor only seeks recovery for EPHFU properties that are held for use "in the reasonably near future;"

[191] Oncor Ex. 17 (Ledbetter Dir.) at 48.

[192] Oncor Ex. 2 (Non-Voluminous Schedules) at Schedule II-B-6; Oncor Ex. 40 (Speed Reb.) at Exh. WRS-R-3.

[193] Oncor Ex. 45 (Ledbetter Reb.) at 32; Oncor Ex. 10 (Speed Dir.) at 41-42.

[194] Oncor Ex. 40 (Speed Reb) at Exh. WRS-R-3.

[195] *Cities for Fair Util. Rates v. Pub. Util. Comm'n of Tex.,* 924 S.W.2d 933, 935-38 (Tex. 1996).

Oncor has definitive, "specific plans" for placing these properties in service in less than 10 years.[196]

- Long-range planning and timely acquisition of property resources benefit Oncor's customers by providing them the assurance that properties will be available when they are needed for service.[197]
- DoD/FEA's potential over-recovery argument also fails because Oncor does not accrue AFUDC on land and land rights.[198]

### d. DoD/FEA's Position

DoD/FEA recommends Oncor's $23.2 million for EPHFU be removed from rate base because 16 TAC § 25.231(c)(2) excludes those costs in rate base.[199] DoD/FEA argues that the land is not being used to provide electric service to customers.[200] Furthermore, DoD/FEA witnesses Morgan and Rogers assert it does not matter that the tracts of land will be in service in 10 years, because Section 25.231(c)(2) has "no exceptions provided for rate base inclusion, such as property being owned a certain period of time before being placed in service."[201] DoD/FEA further argues inclusion is also not automatic because FERC has accounts separating plant currently in service and plant not in service (i.e., Electric Plant in Service (FERC Account 101) and EPHFU (FERC Account 105)) with only

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196 *See* Oncor Ex. 3 (Non-Voluminous Schedule) at WP/II-B-6/01; Oncor Ex. 40 (Speed Reb.) at Exh.WRS-R-3 (detailing Oncor's plans for its EPHFU properties).

197 Oncor Ex. 10 (Speed Dir.) at 42-53.

198 Oncor Ex. 45 (Ledbetter Reb.) at 32.

199 DoD/FEA Ex. 2 (Morgan and Rogers Dir.) at 12.

200 DoD/FEA Initial Brief at 22.

201 DoD/FEA Ex. 2 (Morgan and Rogers Dir.) at 13.

the former allowed in rate base and cost of service.[202] Thus, DoD/FEA maintains this accounting distinction as well as the timing distinction between *when* plant is placed in service—within 10 years or after 10 years—would not exist if EPHFU costs were considered plant in service when acquired.[203]

Finally, DoD/FEA argues that even if the Commission has previously allowed the inclusion of EPHFU in rate base, Oncor still has the burden to demonstrate why it is reasonable and necessary to include these costs in rate base here.[204] DoD/FEA submits Oncor has not done so, nor has Oncor provided evidence the land will be included in rate base within the 10-year period after this rate case.[205]

#### e. Oncor's Position

Oncor insists the plain language of PURA and Commission rules, as well as Commission precedent, allow for the inclusion of EPHFU where there is a plan to place such properties in service within a 10-year period.

First, Oncor asserts these properties satisfy the "used-and-useful" requirement, which it explains "refers to such property as has been acquired in good faith and *held for use in the reasonably near future* in order to enable a utility to

[202] DoD/FEA Ex. 2 (Morgan and Rogers Dir.) at 14.

[203] DoD/FEA Initial Brief at 22.

[204] DoD/FEA Initial Brief at 23.

[205] DoD/FEA Initial Brief at 23.

supply and furnish adequate and uninterrupted service."[206] Although Oncor has not yet constructed facilities on all of its EPHFU properties, it contends the properties still satisfy the "used-and-useful" requirement because they will be used in the "reasonably near future," enabling Oncor to provide adequate and uninterrupted electric service.

Second, Oncor explains that, contrary to DoD/FEA's claims, the Commission has a long-standing policy to include prudent EPHFU investments that will be operational within 10 years in rate base.[207] And unlike CWIP, *"[e]xpenditures may be posted to [EPHFU] absent ongoing construction*. All that is required for [EPHFU] is that there be a *specific plan* for using the expenditure in providing service within [10] years."[208]

Finally, Oncor witness Speed provided "specific plans" for each EPHFU property that Oncor seeks to include in rate base.[209] Each plan explains (1) the electrical need that led Oncor to purchase the property, (2) how the property will be used to meet that need, (3) what facilities Oncor will construct on the property, and (4) when Oncor expects those facilities to be operational.[210] Oncor argues no

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206 *Cities for Fair Util. Rates*, 924 S.W.2d at 935 (quoting *Lone Star Gas Co. v. State*, 153 S.W.2d 681, 698 (Tex. 1941)) (ellipses omitted) (emphasis added); *see also City of Corpus Christi v. Pub. Util. Comm'n of Tex.*, 51 S.W.3d 231, 245 (Tex. 2001) (reaffirming the standard employed in *Cities for Fair Utility Rates* and observing that plant held for future use "expenses are used and useful because they are a necessary part of planned investments.").

207 *See Cities for Fair Util. Rates*, 924 S.W.2d at 937.

208 *Cities for Fair Util. Rates*, 924 S.W.2d at 938 (emphasis added).

209 Oncor Ex. 40 (Speed Reb.) at Exh. WRS-R-3.

210 Oncor Ex. 40 (Speed Reb.) at Exh. WRS-R-3.

party has attempted to rebut this evidence. Therefore, Oncor maintains the entire $23.2 million of EPHFU should be included in rate base.

### f. ALJs' Analysis

The ALJs agree with Oncor's arguments. DoD/FEA essentially argues that Oncor is only entitled to have the prudently incurred costs of used and useful property included in its rate base when providing service to customers in its service area. As such, DoD/FEA argues that EPHFU, whether or not it comes into service within 10 years, is not providing electric service to customers, and is therefore not allowed in rate base. However, DoD/FEA fails to consider the Texas Supreme Court's holding in *Cities for Fair Utility Rates,* where the court held that expenditures for EPHFU could be included in a utility's rate base before the plant went into service if there are specific plans that the EPHFU will be placed in service in the reasonably near future.[211] As Oncor also argues, the Commission includes EPHFU when the utility demonstrates specific plans to use each EPHFU property within 10 years. Here, the ALJs find Oncor has provided sufficient evidence in the form of specific plans that the identified EPHFU will be placed in service within 10 years. The ALJs, therefore, recommend the Commission adopt Oncor's request to include $23.2 million of EPHFU in rate base.

[211] *Cities for Fair Util. Rates*, 924 S.W.2d at 936-37.

## B. Working Capital

Under 16 TAC § 25.231(c)(2)(B), Oncor's total working capital allowance is to be composed of, but not limited to, the following rate base items: (i) reasonable inventories of materials and supplies (M&S); (ii) reasonable prepayments for operating expenses; and (iii) a reasonable allowance for cash working capital (CWC), based on a lead-lag study. Here, Oncor requests inclusion of $152.0 million of M&S inventories, $115.1 million in prepaid operating expenses, and negative $82.2 million in CWC based on a lead-lag study for the period of October 14, 2020, to September 30, 2021.[212]

### 1. Materials and Supplies

Oncor requests the inclusion of $152.0 million in M&S inventories based on an adjusted 13-month average. Cities, however, requests deduction of sources of cost-free capital secured by vendor financing of M&S and non-cash expenses from CWC.[213]

Schedule II-B-8 requires a utility to calculate its 13-month M&S average and use that average when determining the balance in rate base.[214] Oncor's 13-month average of $152.0 million was adjusted to remove select duplicate accounting

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[212] Oncor Ex. 4 (45-day Update) at Schedule II-B-8 (reflecting Oncor's requested M&S inventories), Schedule II-B-10 (reflecting Oncor's requested prepayments); Oncor Ex. 24 (Thenmadathil Dir.) at 4, Exh. AT-3 (reflecting Oncor's requested CWC).

[213] Cities Initial Brief at 15.

[214] Oncor Ex. 2 (Non-Voluminous Schedules) at Schedule II-B-8; Oncor Ex. 26 (Thenmadathil Dir.) at 8-9.

entries, specifically certain December 2021 inventory items that were erroneously miscoded and mistakenly booked into two separate inventory accounts.[215]

### g. Vendor financing of M&S

Cities explains that Oncor did not explicitly recognize vendor supplied financing for M&S as a cost-free source of capital.[216] A portion of Oncor's M&S is initially financed by vendors in the form of a delayed payment recorded by Oncor in accounts payable: the vendors finance Oncor's M&S from the date Oncor purchases and records the M&S assets until it actually pays for those assets.[217] Cities witness Lane Kollen testified that on an average monthly basis, Oncor's vendors, not Oncor's investors, finance $2.304 million of the transmission M&S reflected in rate base and $5.948 million in distribution M&S reflected in rate base.[218]

In response to Cities' vendor-financing allegation, Oncor insists no adjustment is warranted or appropriate as Oncor's requested M&S amount is more reasonable than Mr. Kollen's recommended revenue requirement reduction, which totals approximately $0.684 million.[219] Oncor believes Cities ignores the following four critical aspects of M&S funding:

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[215] Oncor Ex. 26 (Thenmadathil Dir.) at 9.

[216] Cities Ex. 1 (Kollen Dir.) at 12-13.

[217] Cities Ex. 1 (Kollen Dir.) at 12.

[218] Cities Ex. 1 (Kollen Dir.) at 12.

[219] Oncor Initial Brief at 20.

First, accruals and payables represent a customary and accepted part of M&S accounting and Oncor must follow GAAP for accrual-method accounting.[220] Oncor witness Ashley Thenmadathil testified that Oncor has never removed accruals from its M&S assets in any prior rate case and is unaware of any Commission precedent supporting such removal.[221] However, Cities notes that Commission rules explicitly require a utility to subtract from its rate base "other sources of cost-free capital," so GAAP and other rate cases are irrelevant since Oncor's vendor-financed M&S are sources of cost-free capital that should be subtracted from rate base.[222]

Second, the rate filing package instructions require use of a 13-month average, which is used in Schedule II-B-8, rather than a single point-in-time calculation as used by Mr. Kollen.[223] Oncor argues that by its very structure, the 13-month averaging applied to these M&S accounts negates any vendor financing concerns as the 13-month average smooths and averages out both the variable level of total M&S and any accruals/payables timing.[224] Thus, any instances of vendor financing concerns involved in any given month and any short-term timing aberrations are alleviated.[225] Cities, however, states Oncor has no basis for claiming its witness Mr. Kollen used a single-point-in-time calculation to calculate Oncor's

[220] Oncor Ex. 50 (Thenmadathil Reb.) at 15.

[221] Oncor Ex. 50 (Thenmadathil Reb.) at 15.

[222] 16 TAC § 25.231(c)(2)(C)(v); Cities Ex. 1 (Kollen Dir.) at 13.

[223] Oncor Ex. 50 (Thenmadathil Reb.) at 14-15.

[224] Oncor Ex. 50 (Thenmadathil Reb.) at 14.

[225] Oncor Ex. 50 (Thenmadathil Reb.) at 14-15.

M&S inventories, because Mr. Kollen's workpapers illustrate his calculations used a 13-month average.[226]

Third, Oncor's 45-Day Update for Schedule II-B-8 shows higher M&S account levels for the first three months of 2022 than at any point during the 13 months being averaged in this case.[227] Thus, Oncor's requested M&S amount, not Mr. Kollen's reduced amount, represents the more reasonable level of expected M&S inventories during the rate-effective period.[228] In response, Cities reiterates that the rules explicitly require a utility to subtract from its rate base "other sources of cost free capital," such as the vendor financing.[229] Cities explains that this vendor financing displaces Oncor's need to finance a portion of the M&S balance sheet asset through equity or debt.[230] Oncor did not recognize this in its rate base calculation, and, according to Cities, this arbitrarily inflated its revenue requirement.[231]

Finally, Oncor explained that any alleged cost-free, vendor-financed capital for M&S purchases has already been incorporated in Oncor's lead-lag study, which used a reasonable sampling methodology measuring the leads and lags associated with cash expenses involving *all* third-party transactions, regardless of whether they involved capital costs or O&M expenses (including M&S-related expenses).[232]

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226 Cities Ex. 2 (Kollen Errata) at Workpaper LK-1, Tab: M&S.

227 *See* Oncor Ex. 4 (45-day Update) at Schedule II-B-8.

228 Oncor Initial Brief at 21.

229 Cities Ex. 1 (Kollen Dir.) at 13.

230 Cities Ex. 1 (Kollen Dir.) at 12-13.

231 Cities Ex. 1 (Kollen Dir.) at 12-13.

Oncor's lead-lag study incorporates vendor-financing concepts, and Cities' recommended adjustment would double-count this reduction: once through Oncor's lead-lag study and again through Cities' proposed adjustment.[233] Therefore, according to Oncor, Cities' recommendations should be rejected.

Yet, Cities finds Oncor's position unfounded and contradictory to basic accounting principles and posits Oncor conflates the two components because Oncor must incorporate the related vendor-financed capital in a lead-lag study *and* its balanced sheet.[234] As Mr. Kollen testified, there are two separate M&S components: (1) M&S cash expense for purposes of cash working capital, and (2) M&S in inventory for purposes of balance sheets.[235]

Cities argues that the accounts payable representing the amount of this cost-free vendor financing should be subtracted from rate base.[236] Thus, Cities proposes the M&S included in rate base be offset by the related accounts payable to reflect the portion financed by vendors at zero cost, which effectively reduces $0.191 million in the transmission revenue requirement and $0.493 million in the distribution revenue requirement.[237]

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232 Oncor Ex. 50 (Thenmadathil Reb.) at 15; *see also* Oncor Ex. 26 (Thenmadathil Dir.), Exh. AT-2 at 9-11.

233 Oncor Ex. 50 (Thenmadathil Reb.) at 15-16.

234 *See* Cities Ex. 1 (Kollen Dir.) at 18.

235 Cities Ex. 1 (Kollen Dir.) at 19.

236 Cities Ex. 1 (Kollen Dir.) at 13.

237 Cities Initial Brief at 16; Cities Ex. 1 (Kollen Dir.) at 14.

Finding Cities' arguments convincing, the ALJs determine Oncor's M&S rate base component is unreasonable and should be denied. The ALJs recommend offsetting Oncor's M&S rate base component by the portion financed by vendors at zero cost. The weight of the evidence supports Cities' contention that Oncor's vendor-financed M&S are sources of cost-free capital, which should be excluded. Thus, the ALJs recommend adopting Cities' adjustment to the revenue requirement.

#### h. Non-Cash Expense from CWC

Investor-owned electric utilities are allowed a reasonable allowance for CWC to be included in rate base.[238] This reasonable allowance for CWC is determined through a lead-lag study conducted in accordance with the Commission's rules. Here, Oncor requests a negative CWC allowance of $82.1 million, which reduces Oncor's rate base. Cities argues that non-cash M&S expense should be excluded from CWC, which reduces the transmission revenue requirement by $0.003 million and the distribution revenue requirement by $0.035 million.

#### v. Cities' Position

Cities argues that Oncor's CWC calculations incorrectly recorded M&S expense as if it is a cash expense. Commission rules require the lead-lag study to use the cash method: "all non-cash items, including but not limited to depreciation,

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[238] 16 TAC §25.231(c)(2)(B)(iii)(IV).

amortization, deferred taxes, prepaid items, and return (including interest on long-term debt and dividends on preferred stock), will not be considered."[239] According to Mr. Kollen, Oncor adhered to this Commission rule by excluding all non-cash regulatory asset amortization expenses from its operating expenses, but it failed to exclude the M&S expense—an expense that should be classified as a non-cash expense in several instances.[240]

These instances Mr. Kollen referred to as non-cash expenses occurred when there was an initial disbursement of cash and record of the expense in the M&S inventory balance sheet asset account. When inventory is used and charged to expenses in CWIP, Mr. Kollen explained that Oncor does not reimburse cash a second time.[241]

Mr. Kollen testified that the non-cash M&S expense is similar to the non-cash amortization expense that Oncor excluded from CWC: both represent balance sheet assets that are expenses as they are used or amortize and both represent non-cash expenses.[242] Yet, Oncor included the non-cash M&S expense as if it were a cash expense in CWC calculations.[243] Therefore, Cities recommends exclusion of the non-cash M&S expense from CWC, as required under 16 TAC § 25.231(c)(2)(B)(iii)(IV)(-a-), which effectively reduces $0.003 million in the

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[239] 16 TAC § 25.231(c)(2)(B)(iii)(IV)(-a-).

[240] Cities Ex. 1 (Kollen Dir.) at 18-19.

[241] Cities Ex. 1 (Kollen Dir.) at 18.

[242] Cities Ex. 1 (Kollen Dir.) at 18-19.

[243] Cities Ex. 1 (Kollen Dir.) at 18-19.

transmission revenue requirement and $0.035 million in the distribution revenue requirement.[244]

### vi. Oncor's Position.

Oncor asserts Cities misconstrues the nature of these expenses and their inclusion in the lead-lag study. Oncor explains M&S supplies used for O&M expenses will routinely need replacing to keep sufficient inventory on hand to serve customers.[245] When replacing M&S, a cash transaction occurs to replenish those items, and Oncor generally expenses them when purchased.[246] This same process should apply for untracked M&S items for which no specific lead or lag days can be calculated with exact certainty. Oncor contends that, contrary to Cities' argument, this does not represent a "non-cash" method of analyzing these expenses, and they are not akin to non-cash items such as depreciation, amortization, deferred taxes, prepaid items, and return elements that must be excluded from the lead-lag study under 16 TAC § 25.231(c)(2)(B)(iii)(IV)(-a-).

### vii. ALJs' Analysis

Oncor did not provide sufficient evidence to overcome Mr. Kollen's testimony that M&S expense is a non-cash expense that should be excluded from the CWC calculation. Accordingly, the ALJs find the evidence weighs in favor of Cities' allegation that Oncor included non-cash M&S expense in the lead-lag study.

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244 Cities Ex. 1 (Kollen Dir.) at 20; Cities Reply Brief at 7.

245 Oncor Ex. 50 (Thenmadathil Reb.) at 16.

246 Oncor Ex. 50 (Thenmadathil Reb.) at 16; Cities Ex. 1 (Kollen Dir.), Exh. LK-8 at 1 (Oncor response to Cities RFI 3-05).

The ALJs recommend adopting Cities' adjustment to the revenue requirement removing the non-cash M&S expense from CWC.

### 2. Prepayments

Oncor requested inclusion of $115,153,396 of prepayments in calculating its rate base based on a 13-month average after removal of non-recoverable costs, consistent with the RFP instructions.[247] No party objected to the reasonableness of Oncor's prepayments or contested the addition of this amount to the rate base. Therefore, the ALJs recommend the Commission approve Oncor's prepayments in the amount of $115,153,396.

### 3. Cash Working Capital / Lead-Lag Study

CWC represents the component of working capital that is not specifically addressed in other rate base items, such as M&S inventories and prepayments.[248] Capital investments, such as prepayments and inventories, are included separately in rate base, whereas governmental-supplied capital, such as deferred federal income taxes, and customer-supplied capital, such as customer deposits, are deducted from rate base.[249] The remainder is CWC—net funds required by Oncor to pay for goods and services between the time they are paid for by Oncor and the

[247] Oncor Ex. 2 (Non-Voluminous Schedules) at Schedule II-B-10; Oncor Ex. 26 (Thenmadathil Dir.) at 9-12.

[248] Oncor Ex. 26 (Thenmadathil Dir.) at 5.

[249] *See* 16 TAC § 25.231(c)(2)(B) (listing items included in rate base); 16 TAC § 25.231(c)(2)(C) (listing items deducted from rate base).

time revenues are recovered from customers.[250] Oncor's CWC amount was determined by a lead-lag study that, according to Oncor, used methodologies that have been traditionally used in rate cases before the Commission and are consistent with Commission rules.[251]

Oncor requests the inclusion of negative $82,163,866 of CWC.[252] Mr. Thenmadathil testified that the lead-lag study quantifies the net working capital necessary for ongoing operations.[253] A negative CWC means that Oncor received revenue faster than it paid out expenses during the test year, and the CWC amount is a reduction to rate base, which results in a lower revenue requirement than if the CWC were zero.

Cities, however, recommends an adjustment due to an uncorrected error. On June 27, 2022, Oncor filed an errata, which reduced the CWC in its T&D rate base.[254] This reduction was based on a reallocation of expenses between payroll expense and incentive compensation expense in Oncor's lead-lag study.[255]

Mr. Kollen testified that Oncor's errata reduced the transmission CWC included in rate base by $0.754 million and the distribution CWC included in rate

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250 Oncor Ex. 26 (Thenmadathil Dir.) at 5.

251 Oncor Ex. 26 (Thenmadathil Dir.) at 6-8.

252 Oncor Ex. 4 at (45-day Update) at Schedule II-B-9; Oncor Ex. 26 (Thenmadathil Dir.) at 5.

253 Oncor Ex. 26 (Thenmadathil Dir.) at 5.

254 Oncor Ex. 4 (45-day Update); Cities Ex. 1 (Kollen Dir.) at 17-18. Pages referenced in Cities Exhibit 1 will refer to native, not bates, page numbers.

255 Cities Ex. 1 (Kollen Dir.) at 17.

base by $7.926 million, but Oncor did not correct the distribution revenue increase in its errata filing.[256] Therefore, Cities recommends Oncor be required to correct this error, which will result in a $0.062 million reduction in the transmission revenue requirement and a $0.657 million reduction in the distribution revenue requirement.[257]

Commission rules permit a utility a reasonable allowance for CWC, as determined by a sound lead-lag study. If the lead-lag is unreliable, the utility is allowed a working capital allowance equal to negative one-eighth of the utility's O&M expense.[258] No party contested Oncor's requested CWC allowance of negative $82.2 million, which operates as a deduction to rate base, as calculated in Oncor's lead-lag study. However, Cities recommended an adjustment to the CWC because Oncor's errata failed to correct the requested distribution revenue increase that was based on a reallocation of expenses in its lead-lag study. The purpose of a lead-lag study is to net the revenue lag and expense leads associated with expenses not included in rate base; thus, revenues and expenses must match. Here, Oncor's CWC amounts were not synchronized with its filed errata, and therefore were not just and reasonable. The ALJs, therefore, adopt Cities' recommendation that Oncor's error be corrected. The ALJs recommend the CWC calculation be updated and synchronized.

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[256] Cities Ex. 1 (Kollen Dir.) at 17-18.

[257] Cities Ex. 1 (Kollen Dir.) at 8.

[258] 16 TAC § 25.231(c)(2)(B)(iii).

## C. Additions or Deductions to Rate Base

### 1. Accumulated Reserve for Deferred Federal Income Taxes (ADFIT)

ADFIT represents the cumulative tax cash flow differences for items treated differently for book and tax purposes.[259] 16 TAC § 25.231(c)(2)(C)(i) provides that ADFIT can reduce rate base.

Oncor seeks to include an ADFIT level of $2,347,893,771 in rate base.[260] Cities argues that multiple accounting errors related to ADFIT must be rectified to ensure just and reasonable rates. The disputed ADFIT issues include: (1) Performance Enhancement Plan (PEP), Supplemental Executive Retirement Plan (SERP), and Long-Term Incentive Plan (LTIP); (2) the pension plan, other postemployment benefits (OPEB), and FAS 112 assets; and (3) the TCRF, Advanced Metering System (AMS), and Energy Efficiency Cost Recovery Factor (EECRF) unbilled revenue assets.

#### a. Cities' Position

Cities explains that three interrelated components affect the calculation of rate base: (1) the temporary difference; (2) ADFIT; and (3) the related excess asset ADFIT.[261] Cities argues that ADFIT assets and liabilities must match—that the

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[259] Oncor Ex. 25 (Clutter Dir.) at 34.

[260] Oncor Ex. 2 (Non-Voluminous Schedules) at Schedule II-E-3.5.

temporary differences on the balance sheet must be matched with the corresponding ADFIT.[262] Since ADFIT is always recorded on the opposite side of the balance sheet from the temporary differences, both the temporary difference and the ADFIT are either both included or excluded from rate base.[263]

Cities asserts that, unless the matching temporary differences are subtracted from rate base, Oncor should not be permitted to add the ADFIT of certain employee compensation categories (PEP, SERP, and LTIP) and certain ADFIT assets (the pension plan, OPEB, and FAS 112) to rate base.[264] Cities argues that Oncor added the tax effects of these liabilities to rate base but failed to subtract the liabilities themselves (the temporary differences).[265] In both Oncor's treatment of the employee compensation categories and the asset ADFIT of those employee-related retirement costs, Oncor fails to subtract the related temporary differences. As a result, Cities maintain that Oncor's books do not reflect accurate accounting treatment between key components of rate base.

Furthermore, according to Cities, Oncor does not fully fund its pension and OPEB trust funds, which results in savings in financing costs.[266] Oncor relies on its CWC calculation to justify its treatment of these employment-related costs.

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[261] Cities Ex. 1 (Kollen Dir.) at 25.

[262] Cities Ex. 1 (Kollen Dir.) at 30, 32-33.

[263] Cities Ex. 1 (Kollen Dir.) at 29-30. If ADFIT is recorded as a negative, it is recorded on the same side of the balance sheet as the temporary differences. *Id.*

[264] Cities Ex. 1 (Kollen Dir.) at 25-26.

[265] Cities Ex. 1 (Kollen Dir.) at 32-33.

[266] Cities Initial Brief at 11-12.

However, Cities contends that the amounts included in CWC for pension and OPEB are entirely different from the temporary differences. Cities notes Oncor admitted in its last rate case, Docket No. 46957, that pension and OPEB CWC additions to rate base are not the same as the temporary differences and cannot be used as substitute.

Finally, Cities notes Oncor also fails to subtract the corresponding temporary difference for TCRF: Oncor subtracted approximately $65.3 million from rate base but failed to add approximately $14 million in related asset ADFIT to rate base. Cities believes this action to be in error, because, unlike TCRF, Oncor treated similar liabilities—the AMS and EECRF unbilled revenues regulatory liabilities and their related asset ADFIT—correctly. By treating these other similar assets consistently in calculation of rate base, Oncor demonstrates that its treatment of the comparable TCRF line item is an error.

Cities recommends that any ADFIT additions to rate base be rejected if the related temporary difference is not subtracted from rate base. If the asset ADFIT additions are allowed, the related temporary differences should be required to be subtracted from rate base. The specific monetary effects of this adjustment are:

- **PEP, SERP and LTIP:** A reduction of $0.591 million to the transmission revenue requirement and a reduction of $1.656 million to the distribution revenue requirement.
- **Pension, OPEB, and FAS 112 Costs:** A $4.791 million reduction to the transmission revenue requirement and an $11.899 million reduction to the distribution revenue requirement.
- **TCRF, EECRF, and AMS Unbilled Revenue ADFIT Assets:** Since all TCRF amounts apply only to the distribution function, Cities'

adjustment on this issue will result in a reduction of $1.162 million to the distribution revenue requirement.[267]

### b. Oncor's Position

Oncor disputes Mr. Kollen's matching requirement, which is met if an expense related to the temporary difference is included in CWC. First, Oncor notes that the Commission has repeatedly rejected Mr. Kollen's argument—excluding certain ADFIT assets because the related liability is not included in rate base—in prior rate cases.[268] In those cases, the Commission determined that it is a sufficient recognition of the liability in rate base if the corresponding liability is included in the utility's CWC analysis.[269]

Second, Oncor argues its CWC analysis takes into account each liability Mr. Kollen addresses; therefore, there is no basis to "double count" them by adding them to rate base a second time. Even if the CWC study did not take the corresponding liabilities into consideration, Mr. Kollen has cited no authority to support his theory that ADFIT assets cannot be included in rate base unless a corresponding liability is also included.[270]

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[267] Cities Ex. 1 (Kollen Dir.) at 38.

[268] *See Application of AEP Texas Central Company for Authority to Change Rates* (AEP rate case*),* Docket No. 33309 (Aug. 30, 2007); *Application of* Oncor Electric Delivery Company, LLC for Authority to Change Rates (Oncor's last rate case), Docket No. 35717, Order on Rehearing (Nov. 30, 2009). Mr. Kollen made his matching arguments in these two dockets.

[269] Application of AEP Texas Central Company for Authority to Change Rates, Docket No. 33309, PFD at 26-27 (Aug. 30, 2007).

[270] Oncor Ex. 49 (Clutter Reb.) at 5-6.

Next, addressing Cities' argument about Oncor's treatment of AMS and EECRF unbilled revenues, Oncor points to its witness Bonnie Clutter's testimony that Oncor did not include the unbilled revenue impact based upon a prior agreement—now expired—that all EECRF impacts would be removed from base rates and recovered through the EECRF.[271]

Oncor admits it erred by not including the EECRF unbilled revenue ADFIT in rate base, but it argues that this lends no support to Mr. Kollen's position, because Oncor will correct this error in its next base-rate case.[272]

### c. ALJs' Analysis

Cities argues that any ADFIT additions to rate base should be rejected if the related temporary differences are not subtracted from rate base. The ALJs decline to adopt the adjustments proposed by Cities. Oncor established that it included in CWC all of the items disputed by Cities, which resulted in corresponding adjustments to rate base.

The ALJs find Oncor properly included ADFIT of certain employee compensation categories (PEP, SERP, and LTIP) and certain ADFIT assets (the pension plan, OPEB, and FAS 112) and unbilled revenues to rate base. The ALJs also find Oncor's ADFIT adjustments are consistent with PURA § 36.059 and 16

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[271] Oncor Ex. 49 (Clutter Reb.) at 12.

[272] Oncor Ex. 49 (Clutter Reb.) at 12.

TAC § 25.231(c)(2)(C)(i), and Oncor's pension plan, OPEB, and FAS 112 are properly included in rate base in accordance with PURA § 36.065. Accordingly, the ALJs recommend the Commission deny the ADFIT adjustments proposed by Cities and approve the ADFIT adjustments Oncor requested. The ALJs also recommend Oncor correct its error of not including the EECRF unbilled revenues ADFIT in rate base in its next rate case, as Oncor witness Clutter said it would do.

### 2. Excess Deferred Federal Income Taxes

The Tax Cuts and Jobs Act (TCJA) created excess ADFIT assets when, upon its passage in December 2017, the ADFIT asset balances were reduced and the differences reclassified to an "excess" ADFIT regulatory asset account.[273] More specifically, excess ADFIT is created when ADFIT is reduced and when there is a reduction in the corporate tax rate (e.g., the TCJA decreased the tax rate from 35% to 21%).[274] Oncor witness Clutter testified that excess ADFIT, which is amortized as a reduction to income tax expense, should be returned to customers because it is no longer a federal tax liability.[275] And, similar to ADFIT, excess ADFIT is comprised of both assets and liabilities.[276] Ms. Clutter explained that the excess ADFIT assets represent taxes Oncor has pre-paid to the federal government, which it will not recover unless included in rates.[277] In this rate

[273] Oncor Ex. 49 (Clutter Reb.) at 13, 14-15.

[274] Oncor Ex. 49 (Clutter Reb.) at 13, 14.

[275] Oncor Ex. 49 (Clutter Reb.) at 13.

[276] Oncor Ex. 49 (Clutter Reb.) at 13.

[277] Oncor Ex. 49 (Clutter Reb.) at 14.

proceeding, Oncor included $108.3 million of excess ADFIT assets in its tax-related regulatory asset balance.

Again, Cities argues that the three interrelated components that impact calculation of rate base must receive consistent accounting treatment. According to Cities, Oncor should not be permitted to add excess asset ADFIT to rate base or to amortize it to expense if the related asset ADFIT is not also added to rate base. Ms. Clutter contrasted the treatment of excess liability ADFIT with excess asset ADFIT: the former is subtracted from rate base and amortized and refunded in the revenue requirement while the latter is *added* to rate base and amortized and *recovered* in the revenue requirement.[278]

Cities recommends excess asset ADFIT also be excluded in all instances where the asset ADFIT and the temporary differences are excluded from rate base.[279] The effect of Cities' recommendation is: (1) a $7.155 million reduction in the transmission revenue requirement, which includes a $1.764 million reduction in the return on rate base and a $5.391 million reduction of amortization expense; and (2) a $19.544 million reduction in the distribution revenue requirement, which includes a $4.818 million reduction in the return on rate base and a $14.726 million reduction of amortization expense.[280]

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278 Oncor Ex. 49 (Clutter Reb.) at 13.

279 Cities Ex. 1 (Kollen Dir.) at 41.

280 Cities Ex. 1 (Kollen Dir.) at 41.

In response, Oncor presents two grounds for disregarding Cities' proposal: (1) the Commission has not accepted Cities' matching argument (i.e., excess ADFIT should not be included in rate base unless there is a consistency with the three accounting components) nor has Cities provided any support for its contention; and (2) Cities' proposal is inconsistent with prior Commission orders to exclude excess ADFIT assets from rate base. Oncor specifically references the Commission's Order in Docket No. 48325, which authorized Oncor to amortize the excess ADFIT assets over a 10-year period. Thus, the unamortized balance of excess ADFIT assets at the test-year end is $108.3 million.[281] By not allowing amortization, Oncor would not have the ability to recover the unamortized balance of $108 million it has already pre-paid to the federal government in taxes, contrary to the requirement that Oncor be allowed to recover all reasonable operating expenses, including taxes.

The ALJs are not persuaded by Cities' proposal to exclude all instances of excess asset ADFIT when the asset ADFIT and the temporary differences are excluded from rate base. For the same reasons discussed above in the ADFIT section, the ALJs are not compelled by Cities' matching argument. The ALJs find it most reasonable to include $108,278,694 of excess ADFIT assets in Oncor's tax-related regulatory asset balance, as Oncor requested.

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281 Oncor Ex. 49 (Clutter Reb.) at 14.

#### a. Oncor NTU Excess ADFIT for Net Operating Loss

As of May 2019, when Oncor acquired Oncor Electric Delivery Company NTU, LLC's (Oncor NTU's) predecessor, SDTS, Oncor NTU had $56 million of net excess ADFIT liabilities recorded on its books as the result of the TCJA.[282] Included in the $56 million balance is an excess ADFIT asset related to a net operating loss (NOL) carryforward that existed upon the enactment of the TCJA.[283] Oncor included $7.539 million in Oncor NTU's excess ADFIT for NOL in rate base, which includes $1.508 million in related amortization expense.[284] The NOL carryforward was generated by SDTS and can be carried forward to offset future taxes payable in years when taxable income is positive.[285] Under the commitment reflected in the Docket No. 48929 final order, none of the excess ADFIT recorded for Oncor NTU as a result of the TCJA has been amortized or otherwise reduced because current rates do not reflect any such amortization.[286] As agreed by the parties and ordered by the Commission in Docket No. 48929, the amortization of Oncor NTU's excess ADFIT is included in this rate proceeding.[287]

Contrary to Cities' contention, Oncor asserts SDTS could ***not*** have amortized the excess ADFIT asset for NOL before Oncor's acquisition, because: (1) SDTS had not filed a request with the Commission to adjust its rates to return

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[282] Oncor Ex. 49 (Clutter Reb.) at 15.

[283] Oncor Ex. 49 (Clutter Reb.) at 15.

[284] Cities Ex. 1 (Kollen Dir.) at 41.

[285] Oncor Ex. 49 (Clutter Reb.) at 15-16.

[286] Oncor Ex. 25 (Clutter Dir.) at 26, 39.

[287] Oncor Ex. 25 (Clutter Dir.) at 26-27.

the net excess ADFIT liability to ratepayers;[288] and (2) the ADFIT asset for NOL, which was generated from SDTS taking accelerated tax depreciation, is protected under the Internal Revenue Service normalization rules and cannot be reversed faster than the Average Rate Assumption Method.[289]

Cities suggests SDTS reversed the excess ADFIT asset for NOL as the NOL was utilized and recommends excluding the excess ADFIT asset for NOL from Oncor's rate base.[290] However, Oncor argues it would have resulted in a normalization violation for which the penalty is quite severe, and costly to the utility and the ratepayer as the utility can no longer claim accelerated tax depreciation on its federal tax return.[291] Ms. Clutter testified that only the excess ADFIT liability for accelerated tax depreciation remains if the excess ADFIT for NOL is excluded from rate base, which results in too large of a rate base reduction for protected excess ADFIT and too large of a reduction to cost of service as the excess ADFIT liability is amortized.[292] She asserted this is a normalization violation.[293] Ms. Clutter testified that the excess ADFIT asset for NOL and the excess ADFIT liability for accelerated tax depreciation are connected and must be treated the same, because the NOL was generated as a result of taking accelerated

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[288] Oncor Ex. 49 (Clutter Reb.) at 16.

[289] Oncor Ex. 49 (Clutter Reb.) at 16.

[290] Oncor Ex. 49 (Clutter Reb.) at 16.

[291] Oncor Ex. 49 (Clutter Reb.) at 17.

[292] Oncor Ex. 49 (Clutter Reb.) at 16-17.

[293] Oncor Ex. 49 (Clutter Reb.) at 17.

tax depreciation.[294] Thus, Oncor concludes it is appropriate to include the excess ADFIT for NOL in rate base and amortize it to federal tax expenses.

Cities contends the excess ADFIT for NOL should have been fully amortized prior to Oncor's acquisition of Sharyland. Mr. Kollen testified that the excess ADFIT for NOL was due solely to the SDTS NOL carryforward on December 31, 2017, which was fully utilized before Oncor's acquisition of SDTS in May 2019.[295] Thus, Mr. Kollen recommended excluding from rate base the excess ADFIT for NOL. The effects of his recommendation include: (1) a reduction of $1.850 million to the transmission revenue requirement, which includes a $0.456 million reduction in the return on rate base and a $1.394 million reduction of amortization expense, and (2) a reduction of $0.151 million to the distribution revenue requirement, which includes a $0.037 million reduction in the return on rate base and a $0.114 million reduction of amortization expense.[296]

The ALJs recommend the Commission approve Oncor's request to include the excess ADFIT for NOL in rate base and amortize it to federal tax expenses. As Oncor points out, the Commission ordered that none of the excess ADFIT recorded for Oncor NTU be amortized. FOF No. 92 in Docket No. 48929 provides that direction: "Oncor…and Sharyland Utilities, L.L.C. must not amortize or reduce the regulatory liabilities for excess accumulated deferred income taxes recorded as a result of the TCJA until the amortization is reflected in rates."[297]

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294 Oncor Ex. 49 (Clutter Reb.) at 16.

295 Cities Ex. 1 (Kollen Dir.) at 42.

296 Cities Ex. 1 (Kollen Dir.) at 43.

Contrary to Cities' assertions, Oncor presented evidence to make a prima facie showing that the excess ADFIT for NOL should be included in rate base.

### b. Excess ADFIT on Sale of Assets to AEP Texas

In November 2019, Oncor transferred to AEP Texas Inc. (AEP Texas) certain assets, including the non-protected excess ADFIT regulatory liability related to the specific distribution assets transferred.[298] Ms. Clutter testified that the unamortized balance of the non-protected excess ADFIT regulatory liability related to the assets sold was $1.1 million.[299] Since Oncor transferred the liability to AEP Texas and ceased amortization, Oncor had no means of returning the excess ADFIT to the customers served by the assets, and FOF No. 49 in the Docket No. 49402 final order states "[i]t is appropriate, as the signatories agreed, for AEP Texas to record a regulatory liability related to [ADFIT], including excess ADFIT resulting from the [TCJA], attributable to the assets to be transferred."[300]

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[297] *Joint Report and Application of Oncor Electric Delivery Company LLC, Sharyland Distribution & Transmission Services L.L.C., Sharyland Utilities, L.P., and Sempra Energy for Regulatory Approvals Under PURA §§ 14.101, 37.154, 39.262, and 39.915*, Docket No. 48929, Order at 35 (May 9, 2019). The Commission found in FOF No. 92: "Oncor and Sharyland Utilities, L.P. commit that … Sharyland Utilities, L.L.C. will [not] amortize or reduce the regulatory liabilities for excess accumulated deferred income taxes recorded as the result of the Tax Cuts and Jobs Act of 2017 until the amortization is reflected in rates, and they agreed that the disposition of these amounts will be addressed in the next base-rate case proceedings for Oncor and Sharyland Utilities, L.L.C. Additionally, the signatories agreed for all issues related to net operating loss accumulated deferred income tax to be reserved for disposition in future base-rate proceedings." *Id.* at 20.

[298] Oncor Ex. 49 (Clutter Reb.) at 17-18.

[299] Oncor Ex. 49 (Clutter Reb.) at 18.

[300] Oncor Ex. 49 (Clutter Reb.) at 18.

OPUC witness Hunt recommends that Oncor re-establish the $1,116,261 of non-protected excess ADFIT that was removed from Oncor's books due to the asset sale to AEP Texas. OPUC initially contested, in its initial briefing, the amount of excess ADFIT that Oncor did not refund to its customers following the sale of assets to AEP Texas in 2019; however, OPUC withdrew, in its reply brief, its proposal that Oncor remove $1.1 million of excess ADFIT from its books.[301] Accordingly, the ALJs find that this issue is moot and Oncor's removal of the non-protected excess ADFIT is appropriate.

### 3. Contributions In Aid of Construction

As set forth in 16 TAC § 25.231(c)(2)(C)(iv), certain items, such as contributions in aid of construction (CIACs), are deducted from rate base. Oncor explains that CIACs reflect amounts requested by customers for "facilities in excess of a standard installation…based on their own economic principles all the time" and should not be confused with "temporary facilities" expected to be in place "less than 12 months."[302] Consistent with the FERC USOA, Oncor credits CIACs in the form of money or its equivalent toward the construction of electric plant charged with the cost of such construction.[303]

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[301] OPUC Initial Brief at 2, 5-6; OPUC Reply Brief at 2.

[302] Tr. at 940-41, 944.

[303] Oncor Initial Brief at 29.

No party contests Oncor's treatment of crediting CIACs toward the construction of electric plant charged with the cost of construction. The ALJs find Oncor's treatment of CIACs and the resulting impact on rate base reasonable.

### 4. Sources of Cost-Free Capital

#### a. Customer Deposits

Oncor's balance sheet reflects $43.0 million of customer deposits at the end of the test year. From that, Oncor identified $162,100 of customer deposits for inclusion as a reduction in rate base. According to Mr. Thenmadathil, the $162,100 in customer deposits represent a predictable, long-term source of financing Oncor's working capital needs. These customer deposits were received from third-parties to long-term joint pole use agreements.

No party or briefing contested Oncor's deduction of $162,100 from distribution rate base for customer deposits arising from joint pole use agreements. The ALJs find that the funds Oncor subtracted from rate base are reasonable as prescribed by 16 TAC § 25.231(c)(2)(C)(v), which states customer deposits and other sources of cost-free capital are deducted from rate base.

#### b. Customer Advances for Construction

At the end of test year ending December 31, 2021, Oncor held $42.9 million in fully refundable customer advances for construction activities that, according to

Mr. Thenmaddathil, are primarily short-lived. These deposited amounts are not contributions in aid of construction and are excluded from Oncor's operating cash. Oncor deposited these customer advances in an interest-bearing restricted escrow account ("construction collateral") and are not available as a source to Oncor's working capital needs. Oncor, therefore, proposed a known and measurable adjustment to remove these short-lived, unpredictable, non-recurring construction collateral funds, which Cities opposes as a claimed source of cost-free capital.

Oncor advances the following arguments to support its adjustment to remove these construction collateral from the calculation of its rate base: (1) Oncor's proposal represents a reasonable, middle-ground position unlike Cities' least favorable treatment; (2) these short-lived construction collateral funds should not serve as a fixed, long-term reduction to transmission rate base; (3) these funds are not "cost-free capital" as a matter of law; and (4) construction collateral amounts are erratic and non-recurring.

In addition to claiming that its proposal, unlike Cities', represents a reasonable, middle-ground position because it neither serves as an addition to, nor a subtraction from, rate base, Oncor also asserts that Cities' recommendation ignores the construction collateral asset and includes a permanent rate base deduction for the attendant liability. Mr. Ledbetter testified that, for Oncor, the most favorable treatment of these funds would be to add them to a non-interest-bearing bank account, which would operate as an addition to Oncor's rate base under 16 TAC § 25.231(c)(2)(B)(iii)(IV)(-e-). Cities disagree, stating that Oncor's use of a restricted cash account to deposit these funds rather than using them for general corporate purposes is merely a self-imposed restriction. Cities note that Oncor's use of this account is not required by contract requirement or mandated by law and add that this account is not an escrow account subject to the supervision of a third party. Even Mr. Ledbetter admitted there are no regulatory requirement that require customer advances be held in a restricted account. Cities also note that a middle ground treatment does not increase transmission revenue requirements by $3.552 million.

And, despite Oncor's argument that this restriction complies with the Securities and Exchange Commission (SEC) financial reporting "disclosure requirements" regarding restricted accounts, Cities contends the SEC reporting disclosure requirement is not the same, as it only addresses disclosure as to amounts that are "restricted to withdrawal or usage." Further undermining Oncor's SEC argument, Cities presents that (1) the SEC reporting disclosure requirement does not address the appropriate ratemaking for customer advances regardless of whether they are deposited into a restricted account or not; and (2) the SEC financial reporting disclosure requirements do not compel the use of a restricted cash account. Finally, Cities notes that there is no GAAP mandate requiring Oncor to deposit customer advances in a restricted account, and, prior to December 2021, when Oncor established the restricted account, the cash was available for general corporate purposes.

Oncor, in turn, points out that Cities fails to cite any statute, rule, or case law to support its proposed adjustment to these funds. Additionally, an interest-bearing restricted escrow account has been funded with the same exact cash amounts that customers have posted as collateral for construction-related activities, not Oncor's debt and equity capital as suggested by Cities.

Oncor's second argument is that its short-lived construction collateral funds should not serve as a fixed, long-term reduction to transmission rate base. Unlike the long-term stable customer/joint use deposits, the availability of these construction collateral funds is fleeting and they are not reasonably expected to last throughout the rate-effective period. The three types of construction collateral include cash, a letter of credit, and corporate guaranty, often with cash posted to enable quick execution of the relevant construction agreement. However, that cash collateral is then replaced with a letter of credit or guaranty. Nonetheless, Cities argue that placing these customer advances in restricted account allows Oncor to finance these discretionary deposits, which unnecessarily increases the transmission revenue requirement and reduces Oncor's proposed transmission rate reduction. Cities reiterates that the cash was available for operating cash before December 2021 and allowed Oncor to avoid other equity and long-term debt financing of an equivalent amount. Instead of issuing equity and debt to finance the deposit of these advances into a restricted account, Mr. Kollen insisted Oncor should use these customer advances to displace equity and debt financing.

Oncor's third argument is that these funds are not "cost-free capital" as a matter of law because Oncor must refund construction collateral with interest, as required by statute and Commission rule. Oncor explains that Commission-mandated interest rates that attach to customer reimbursement exceed the actual interest rates earned on these funds, even when placed into an interest-bearing