

(iii) Account 354-Towers and Fixtures

Although there is limited experience available for this account, the five-year and ten-year moving averages for transaction year 2010 show a substantial level of negative net salvage (negative 299 percent and negative 233 percent, respectively). Taking into account the low level of retirement experience, Mr. Watson stated that he moderated the outcome by recommending moving to negative 20 percent net salvage.⁴⁵¹ Mr. Pous concurred in this recommendation.

Ms. Mathis recommended a net salvage rate of negative 5 percent for Account 354.⁴⁵² This recommendation is based on Commission precedent due to the absence of reliable historical salvage data.⁴⁵³ Although historical salvage data is available for the period of 1984 through 2010, this account had a low level of retirement during this period.⁴⁵⁴ Because of the limited retirement activity, Ms. Mathis stated that a reasonable net salvage rate cannot be calculated from the historical salvage data.⁴⁵⁵ For example, annual net salvage rates range from approximately negative 6,000 percent to approximately positive 31,253,400 percent.⁴⁵⁶ According to Ms. Mathis, such divergent numbers are indicative of the low retirement activity within this account.

The negative five percent net salvage value recommended by Ms. Mathis is the current Commission-approved number. The ALJs find it difficult to draw any conclusions from the paucity of historical data. Had there been additional historical data, it might have been possible to reach the conclusion urged by Mr. Watson; however, there was not. The ALJs recommend that the Commission adopt the negative five percent net salvage value recommended by Staff.

⁴⁵⁰ ETI Ex. 13A (Watson Direct) Workpaper on CD, “Entergy Net Salvage Transmission Distribution General” Spreadsheet, “Data Adjustments” Tab, Account 353.

⁴⁵¹ ETI Ex. 13 (Watson Direct) at Ex. DAW-1 at 66.

⁴⁵² Staff Ex. 2 (Mathis Direct) at 23.

⁴⁵³ *Id.* at 23.

⁴⁵⁴ ETI Ex. 13 (Watson Direct) at DAW-1 at 66.

⁴⁵⁵ Staff Ex. 2 (Mathis Direct) at 23.

⁴⁵⁶ *Id.* at Appendix C at 2.

(iv) Account 355-Poles and Fixtures

The Commission approved net salvage value for this account is a negative 25 percent.⁴⁵⁷ This account has shown negative salvage since the 1990s, and the most recent ten-year moving averages show negative 33.84 percent net salvage. Although years 2009-2010 reflect positive salvage values, Mr. Watson determined that these values were the product of differences in the timing of the recording of the various transactions associated with the asset retirement, rather than reflecting an actual positive salvage amount.⁴⁵⁸ For example, Mr. Watson's net salvage workpapers show a significant level of positive salvage only for the years 2009-2010 in Account 355.⁴⁵⁹ This is at odds with the remainder of the net salvage data shown in the workpapers, which is almost exclusively negative net salvage.⁴⁶⁰ Accordingly, Mr. Watson gave less weight to the 2009 and 2010 values, but moderated his recommendation compared to the ten-year moving averages, resulting in a recommended net salvage of negative 30 percent. Ms. Mathis concurred.

Cities witness Pous disagreed with Mr. Watson's analysis, claiming: (1) per book data from the five-year and ten-year moving averages show positive net salvage amounts; (2) authoritative depreciation treatises do not support Mr. Watson's decision to adjust relocation-related transactions out of the analysis;⁴⁶¹ (3) no portion of relocation-related costs can be treated as removal unless that treatment is prescribed by contract with the third-party; and (4) after the correction to his analysis, Mr. Watson changed his methodology to arrive at a negative net salvage recommendation. Mr. Pous recommended an increase in the net salvage values to a negative 15 percent based on the actual historical data of ETI. Cities contend that Mr. Pous was conservative in his recommendation given

⁴⁵⁷ Cities Ex. 5C (Pous Depreciation Study) at 23.

⁴⁵⁸ ETI Ex. 13 (Watson Direct) at Ex. DAW-1, p. 66.

⁴⁵⁹ ETI Ex. 13A (Watson Workpapers CD), Adjusted Data Net Salvage Tab, account 355, lines 130-131, columns I – S.

⁴⁶⁰ ETI Ex. 13A (Watson Workpapers CD), Adjusted Data Net Salvage Tab, account 355, at lines 105 – 129, columns I – AC. The 2005-2006 data in this workpaper show an obvious example of an accounting adjustment timing difference, wherein the year 2005 shows a \$1,867,532 removal cost (row 126, column G), while the immediately following year 2006 shows a large *negative* removal adjustment of (\$1,059,096), (row 127, column G).

⁴⁶¹ Relocations involve the situation where the Company is reimbursed by a third party who desires the relocation or replacement of the facilities in question.

the trend in the data. The most recent five-year band of actual data yields a positive two percent net salvage.⁴⁶²

The ALJs agree that the debate regarding this account essentially boils down to whether Mr. Watson's adjustment to remove relocation expense associated with third-party reimbursement from the analysis is appropriate. Although Mr. Pous claims that Mr. Watson's approach is contrary to authoritative guidance, ETI contends that he arrives at that conclusion only by disregarding the guidance in question, as well as Commission precedent. ETI argues that the depreciation text in question squarely supports Mr. Watson's approach:

A reimbursed retirement is one for which the company is fully compensated at the time of retirement Usually reimbursed retirements should not be included in analysis of property whose investment is recovered through depreciation accruals.⁴⁶³

Mr. Watson explained at hearing that, in his experience, adjustments to remove relocation expense are standard in depreciation analysis, and to do otherwise would result in a disproportionate impact on reasonably expected ongoing net salvage, caused by a transaction (the relocation) that constitutes a very small portion of the overall assets in question.⁴⁶⁴

Mr. Pous stated that all third-party reimbursements for facility relocation performed by the Company have to be deemed as salvage (thereby inflating the salvage portion of the net between removal costs and salvage proceeds) unless a contract between ETI and a third-party explicitly says otherwise. Mr. Watson's approach, however, is squarely supported the Commission's decision in the recent Oncor case, Docket No. 35717, where it was held that these third-party "reimbursements are prepayments for new property being installed."⁴⁶⁵ The ALJs find that Mr. Pous' argument is not credible in light of Mr. Watson's treatment of relocations in general. Since Mr. Watson properly removed such relocation expense from the depreciation analysis altogether, those amounts correctly

⁴⁶² Cities Ex. 5C (Pous Depreciation Study) at 22-25.

⁴⁶³ ETI Ex. 71 (Watson Rebuttal) at 63 (quoting *Depreciation Systems*, Iowa State Press, 1994, at 16-17).

⁴⁶⁴ Tr. at 405.

⁴⁶⁵ ETI Ex. 71 (Watson Rebuttal) at 63.

have no impact on depreciation rates, regardless of how they are allocated between gross salvage proceeds and the cost of installing new facilities.

ETI's evidence and argument support its request. Accordingly, the ALJs recommend that the Commission approve a net salvage of negative 30 percent as proposed by Mr. Watson.

(v) 356-Overhead Conductors and Devices

The Commission approved net salvage value for this account is a negative 20 percent.⁴⁶⁶ Much as was the case with Account 355, ETI argues that timing differences in reflecting accounting adjustments made the more recent shorter data bands less representative of reasonably expected future net salvage. Mr. Watson's study determined that the longer ten-year moving average for transaction year 2010 showed salvage of negative 33 percent, so Mr. Watson recommended moving to negative 30 percent net salvage for this account.⁴⁶⁷ Staff witness Mathis adopted the same negative net salvage value.

Cities' witness Pous recommended an increase to the net salvage value to a negative 10 percent based on a review of the actual historical data. The actual five-year and ten-year bands yield a positive one percent and a negative 31 percent. Mr. Pous argues that the trend in the data could justify even a less negative value.

As with Account 355, the ALJs find that ETI's evidence and arguments support its request. Accordingly, the ALJs recommend that the Commission approve a net salvage of negative 30 percent as proposed by Mr. Watson.

⁴⁶⁶ Cities Ex. 5C (Pous Depreciation Study) at 25.

⁴⁶⁷ ETI Ex. 13 (Watson Direct) at Ex. DAW-1 at 66-67.

4. Distribution Plant**(a) Lives**

An asset's useful life is used to determine the remaining life over which the cost will be spread for recovery through depreciation expense.⁴⁶⁸ The Company's depreciation study addresses 14 distribution accounts included between Accounts 360.2 and 373.2. According to ETI, the life parameters in Mr. Watson's study reflect standard depreciation analysis procedures, including comparison to standard Iowa curves and actuarial analysis, along with the exercise of informed judgment.⁴⁶⁹ Multiple bands and trends were reviewed and, in general, Mr. Watson's study explained that the dispersion curve chosen for each account is based on examination of the various "placement and experience bands"⁴⁷⁰ and the characteristics of the underlying asset in each account. The dispersion curve is then chosen that best matches the actual data.⁴⁷¹ Staff disagrees with Mr. Watson's life parameters for three accounts; Cities with five accounts. The parties' various recommendations on the accounts in dispute are shown below:

Depreciation Plant Lives				
Account	Approved Life	ETI Proposal	Staff Proposal	Cities Proposal
361	45 yrs. S2	65 yrs. R3	70 yrs. R3	65 yrs. R3
364	44 yrs. S1	38 yrs. R1.5	40 yrs. R1	44 yrs. L1
365	44 yrs. S1	39 yrs. R0.5	40 yrs. R0.5	42 yrs. S-0.5
367	40 yrs. S1	35 yrs. R1.5	35 yrs. R1.5	45 yrs. S-0.5
368	39 yrs. S0	29 yrs. L1	29 yrs. L1	33 yrs. L0.5
369.1	36 yrs. S4	26 yrs. L4	26 yrs. L4	33 yrs. R4

(i) Account 361 – Structures and Improvements

Mr. Watson's study depicts the fit between the actual data in the account and the 65 R3 life parameter that he proposed for this account.⁴⁷² Mr. Pous agreed with this recommendation.

⁴⁶⁸ *Id.* at 16.

⁴⁶⁹ *Id.* at Ex. DAW-1 at 37-54.

⁴⁷⁰ Placement bands look at assets installed in various years and reveal the types of assets in the account over time. Experience bands show accounting transactions associated with the assets over time and reveal trends associated with operational changes and other events.

⁴⁷¹ ETI Ex. 13 (Watson Direct) at Ex. DAW-1 at 37-54.

⁴⁷² *Id.* at Ex. DAW-1 at 37.

Ms. Mathis stated, however, that a life parameter of 70 R3 is a better visual fit for the 1960-2010 experience band.⁴⁷³

Considering all the historical mortality data available for this account (the overall experience band), the selected Iowa Curve produces a conformance index (CI) of 37.53.⁴⁷⁴ The CI is a measure of closeness of fit, and a higher CI value indicates a closer fit between the two sets of data that are being compared.⁴⁷⁵

Mr. Watson recommended a life parameter of 65 years based on comparing various slices (bands) of this account's mortality data to the 65 R3 Iowa Curve.⁴⁷⁶ However, Staff argues that Mr. Watson's recommended life parameter and Iowa Curve of 65-R3 produces a CI of only 23.61 when measured against the overall (1960 – 2010) experience band.⁴⁷⁷

ETI responds that the flaw in Ms. Mathis' position is that she only looks at one band. As the average age of the investment is only 19.22 years, it is inadequate to look at only one band that examines a 50-year period. When shorter bands are also factored in (1970-2010 and 1990-2010), the Company's proposal shows a significantly higher CI, which is indicative of a better fit to the actual data.⁴⁷⁸

The ALJs are persuaded that, in this instance, Ms. Mathis erred by limiting her review to a single band, especially when that band is significantly longer than the average age of the investment at issue. In this case, looking at multiple, shorter bands will give a clearer picture of the average life of the investment at issue. Therefore, the ALJs recommend the Commission approve the 65 R3 life parameter Mr. Watson proposes for this account.

⁴⁷³ Staff Ex. 2 (Mathis Direct) at 25-26.

⁴⁷⁴ *Id.* at 26, Table-5.

⁴⁷⁵ ETI Ex. 71 (Watson Rebuttal) at 24.

⁴⁷⁶ ETI Ex. 13 (Watson Direct) at 18, Figure 1.

⁴⁷⁷ Staff Ex. 2 (Mathis Direct) at 26, Table-5.

⁴⁷⁸ ETI Ex. 71 (Watson Rebuttal) at 24.

(ii) Account 364 – Poles, Towers, and Fixtures

Mr. Watson's study results in his proposing a life parameter of 38 R1.5.⁴⁷⁹ He stated that the current plant in service reflects a life (13.97 years on average) that is substantially shorter than his recommendation, and all the bands examined reflect a shorter life than the currently approved 44 years. Mr. Watson testified that his recommendation balances these facts with the additional fact that ETI is currently using Penta and CCA-treated poles (as opposed to creosote treated poles), for which a longer life is expected.

Ms. Mathis (40 R1) and Mr. Pous (44 L1) both proposed different life parameters than Mr. Watson. Ms. Mathis stated that her proposed life parameter is a better visual and mathematical fit for the single experience band (1959-2010) she considered.⁴⁸⁰ Mr. Watson responded to this argument, stating that the mathematical computer fitting emphasized by Ms. Mathis is too limited an approach, because there is too little information provided at the tail of the curve to rely on computer fitting in this instance. Mr. Watson indicated that his proposed life parameter shows a better fit over the full range of placement and experience bands applicable to this account.⁴⁸¹

Mr. Pous recommended that the expected service life remain at 44 years based on actuarial analysis and advances made by the industry and ETI in treating and preserving poles.⁴⁸² Mr. Pous also noted that "absent identifiable and supportable specific problems, the industry is not experiencing shorter lives for poles and neither should ETI."⁴⁸³ He stated that selection of different types of poles and different treatments by other utilities have their engineers expecting lives between 50 and 70 years.⁴⁸⁴ According to Mr. Pous, it is simply not realistic to believe or assume that ETI would operate now or in the future in a manner that its poles would only last two-thirds the life

⁴⁷⁹ ETI Ex. 13 (Watson Direct) at Ex. DAW-1 at 41.

⁴⁸⁰ Staff Ex. 2 (Mathis Direct) at 28-29.

⁴⁸¹ ETI Ex. 71 (Watson Rebuttal) at 29-31.

⁴⁸² Cities Ex. 5C (Pous Depreciation Study) at 35-36.

⁴⁸³ *Id.* at 37.

⁴⁸⁴ *Id.*

expectance being achieved by others.⁴⁸⁵ Mr. Watson responded that the increased life span urged by Mr. Pous based on his general discussion of varieties of poles with longer lives is not verifiable, not consistent with the Company-specific data or the specific experience of its distribution personnel, and is plainly exaggerated.⁴⁸⁶

The ALJs reviewed the evidence and arguments of the parties with respect to this issue and were most persuaded by the CIs that resulted from the recommendations of Staff and ETI. Considering all the historical mortality data available for this account (the overall experience band), Staff's selected Iowa Curve produces a CI of 41.44, while ETI's produces a CI of only 20.66 when measured against the overall (1958 – 2010) experience band.⁴⁸⁷ The ALJs recommend that the Commission adopt Staff's proposal of 40 R1.

(iii) Account 365 – Overhead Conductors and Devices

The Commission approved average service life is 44 years.⁴⁸⁸ All parties propose a change to this life parameter. Mr. Watson proposed a life parameter of 39 R0.5, Ms. Mathis proposes a life parameter of 40 R0.5, and Mr. Pous proposed a life parameter of 42 S.-5.

Mr. Watson noted that his analysis took into account the fact that the currently authorized life is longer than the history would support, and that the young average age of the current plant in service (12.15) points toward placing more weight on recent bands for life selection. He also noted that ETI's movement toward re-conductoring lines supports the conclusion that lives in this account will be shorter.

Ms. Mathis indicated that her recommendation is based on comparing the account's historical mortality data for the period of 1958 through 2010 to the 40 R0.5 Iowa Curve.⁴⁸⁹ Considering all the

⁴⁸⁵ *Id.* at 36.

⁴⁸⁶ ETI Ex. 71 (Watson Rebuttal) at 28-29.

⁴⁸⁷ Staff Ex. 2 (Mathis Direct) at 29, Table-6.

⁴⁸⁸ Cities Ex. 5C (Pous Depreciation Study) at 38.

⁴⁸⁹ Staff Ex. 2 (Mathis Direct) at 30.

historical mortality data available for this account (the overall experience band), the selected Iowa Curve produces a CI of 29.63.⁴⁹⁰ Mr. Watson countered that Ms. Mathis used the wrong curve to represent the Company's proposal in her calculations. He stated that when her analysis is corrected to make the proper comparison, ETI's proposal has a higher CI (and thus a better fit) across all experience bands save one.⁴⁹¹

Mr. Pous testified that his life parameter best matches the actuarial analysis taking into account the unusually high level of retirement activity recorded in the first 0.5 year of age. As Mr. Pous noted, "the highest retirement ratio for this investment in the first 23 years occurred at age 0.5 years, for brand new assets. While such events can and have occurred associated with utility plant, it is not the type of event that is reasonably expected to repeat itself in future periods as different equipment it purchases if it was an equipment problem, or different installation processes are employed if the early retirement were due to installation issues."⁴⁹² Mr. Pous criticized Mr. Watson's recommendation on several grounds: (1) it is not consistent with expected lives reported by ETI personnel; (2) it did not account for anomalies and/or unusual activity in the retirement data; (3) the major re-conductoring activity shown in the account should not be expected to continue; and (4) the life-curve combination chosen by Mr. Watson is not long enough to match the actual data.⁴⁹³

Mr. Watson took issue with Mr. Pous. He stated that Mr. Pous simply misread the data Mr. Watson argued that Exhibit DAW-R-1 to his rebuttal testimony shows that retirements are decreasing.⁴⁹⁴ Mr. Watson believes that his proposed life parameter is a better fit to the actual data. The very small amount of plant that may not last until the tail of the curve used by Mr. Watson does

⁴⁹⁰ *Id.* at 31, Table-7.

⁴⁹¹ ETI Ex. 71 (Watson Rebuttal) at 36.

⁴⁹² Cities Ex. 5C (Pous Depreciation Study) at 38-39.

⁴⁹³ *Id.* at 38-41.

⁴⁹⁴ ETI Ex. 71 (Watson Rebuttal) at 32-33.

not alter this conclusion.⁴⁹⁵ Finally, ETI argues that Mr. Pous provides no persuasive basis for second guessing the opinion of Company personnel regarding re-conductoring.

The ALJs are persuaded by ETI's evidence and argument. It does appear that Ms. Mathis used the wrong curve in her calculations. If corrected, Mr. Watson's proposal renders the higher CI. Mr. Pous' arguments fair no better. To the ALJs' eye, Mr. Pous did misread the data, and the conclusions drawn by Mr. Pous are simply inaccurate. The ALJs recommend that the Commission adopt ETI's proposed life parameter of 39 R0.5.

(iv) Account 367 – Underground Conductors and Devices

The Commission approved average service life is 40 years.⁴⁹⁶ Mr. Watson's life parameter for this account (35 R1.5) is based on his review of the various placement and experience bands, as well as the characteristics and longevity of the conductors in place in the ETI system and the retirement patterns that are unique to underground conductor performance and the locations where it is buried.⁴⁹⁷ Ms. Mathis agreed with Mr. Watson on this account. Cities propose a significantly longer life (45 S-0.5). Mr. Pous stated that Mr. Watson's and Ms. Mathis' recommendations do not account for the increased durability of newer types of conductor, and that the actuarial analysis should focus on more recent data that he believes is more consistent with the newer conductors.⁴⁹⁸

Mr. Watson testified that Mr. Pous' recommendation should be rejected for a variety of reasons. The Southern California Edison-based opinions regarding longer life for the conductor, relied on by Mr. Pous, relate to plant installed less than ten years ago. Therefore, based on his own theory, much of the investment in question in this account is still the older, shorter-lived variety, and his recommendations are premature. Moreover, Mr. Watson's plotting of the dispersion curves show that his is a better fit than that of Mr. Pous. In this instance, Mr. Pous' analysis, relying only on the

⁴⁹⁵ *Id.* at 32, 33-35.

⁴⁹⁶ Cities Ex. 5C (Pous Depreciation Study) at 41.

⁴⁹⁷ ETI Ex. 13 (Watson Direct) at Ex. DAW-1, p. 45.

⁴⁹⁸ Cities Ex. 5C (Pous Depreciation Study) at 41-44.

shortest band, failed to pick up the older investment that constitutes almost 80 percent of the surviving investment.⁴⁹⁹

It appears that Mr. Pous, in relying on the shortest band, did fail to take into account investment that comprises almost 80 percent of the surviving investment in this account. That is a significant flaw in his analysis. Similarly, his reliance on the Southern California Edison-based opinions relate to newer plant, which again calls his analysis into question in the present circumstances. The ALJs recommend that the Commission approve ETI's recommended service life of 35 R1.5.

(v) Account 368 – Line Transformers

The Commission approved anticipated service life is 39 years.⁵⁰⁰ Mr. Watson proposed a service life of 29 L1,⁵⁰¹ with which Ms. Mathis agreed. Mr. Watson stated that this is consistent with the data showing decreasing lives for these assets, the expected lives per Company personnel, and the fact that transformers are junked or sold rather than repaired.⁵⁰²

Mr. Pous recommended that the expected service life be decreased to 33 years, representing a 15 percent reduction in the anticipated service life. Mr. Pous stated that his analysis is based on actuarial analyses and the Company's addition of approximately \$80 million of pad mounted transformers since the last case, when the Commission approved a 39-year anticipated average service life. According to Mr. Pous, ETI personnel have stated that pole mounted transformers have a life of between 25 and 35 years. However, pad mounted transformers are expected to last up to 40 years by the same Company personnel. Given the sizable investment since the last case in the pad mounted transformers with a longer expected service life, a decrease in the anticipated service life of greater than 15 percent is not warranted, according to Mr. Pous. Moreover, Mr. Pous stated his analysis uncovered abnormally high retirement ratios in the 21.5 to 22.5 year age brackets

⁴⁹⁹ ETI Ex. 71 (Watson Rebuttal) at 40.

⁵⁰⁰ Cities Ex. 5C (Pous Depreciation Study) at 44.

⁵⁰¹ ETI Ex. 13 (Watson Direct) at Ex DAW-1 at 50.

⁵⁰² *Id.* at 47.

indicative of one-time events such as the ice storm or changes in accounting systems. As such, Mr. Pous performed his curve fitting analysis recognizing the unusually high retirement activity between years 21.5 and 22.5 rather than emphasizing such unusual activity as Mr. Watson did for his proposal to reduce service life by 26 percent.⁵⁰³

Mr. Watson recommended a decline in average service life from a 39-year anticipated service life to a 29-year anticipated service life citing the high occurrence of lightning in the ETI service area.⁵⁰⁴ However, Mr. Pous noted that the effects of lightning in ETI's service area would have been present in ETI's last base rate case when a 39-year anticipated service life was approved by the Commission. Both Mr. Watson and Mr. Pous recognized that the pad mounted transformers are not subject to the same forces of retirement like weather, lightning, and animal disturbances.⁵⁰⁵ However, Mr. Watson did not realistically factor ETI's relative increased investment in pad mounted transformers into his analysis. Moreover, when performing his curve fitting analysis, Mr. Watson neither analyzed nor adjusted for the abnormal unusual retirement ratios between years 21.5 and 22.5.⁵⁰⁶ Instead, Mr. Watson attempted to select a life analysis that anticipates a high level of retirement within that time period in the future.⁵⁰⁷ Cities argue that, by failing to recognize the sizable new investment in pad mounted transformers and failing to consider the unusual retirement ratios, Mr. Watson proposed an average service life that is lower than the bottom end of the range of life estimates of Company personnel for pad mounted transformers. Moreover, Mr. Watson's proposal does not even reach the midpoint of life estimates expected by Company personnel for pole mounted transformers.

The arguments and evidence advanced by Cities witness Pous are persuasive to the ALJs. Mr. Watson's contention regarding the occurrences of lightening in the ETI service area was equally applicable at the time the existing approved rate was set, and is, therefore, of little value in this proceeding. Further, Mr. Watson's failure to analyze the abnormal retirement ratios between years

⁵⁰³ Cities Ex. 5C (Pous Depreciation Study) at 45.

⁵⁰⁴ ETI Ex. 13 (Watson Direct) at Ex DAW-1 at 50.

⁵⁰⁵ *Id.*

⁵⁰⁶ Cities Ex. 5C (Pous Depreciation Study) at 47.

⁵⁰⁷ ETI Ex. 13 (Watson Direct) at Ex DAW-1 at 50-51.

21.5 and 22.5 also argues against his analysis. The ALJs recommend that the Commission adopt Mr. Pous' proposed life of 33 L0.5.

(vi) Account 369.1 – Overhead Services

The Commission previously approved anticipated service life for this account is 36 years.⁵⁰⁸ Mr. Watson's analysis of this account shows that overhead assets have retired earlier and have been replaced more frequently than is consistent with the existing 36 S4 life. The average age of current investment is 10.12 years. Consistent with this data and his review of various curves and placement and experience bands, he recommended shortening the life to 26 L4. Ms. Mathis agrees with this proposal.⁵⁰⁹

Mr. Pous recommended that the expected service life be shortened to 33 years based on the lack of Company historical data and based on comparative utility experience including recent studies by Mr. Watson, where he proposed significantly longer average service lives. Mr. Pous testified that an evaluation of the actual data casts serious doubt about the reliability of the data for depreciation purposes. ETI does not have any records of services in this subaccount surviving past 1978. Mr. Pous stated that his recommended 33-year life expectancy for this sub-account is still far shorter than industry expectations, but is consistent with the depreciation study recently conducted for EGSL where the depreciation expert hired by EGSL recommended a 33-year life.⁵¹⁰

ETI argues that Mr. Pous apparently made no attempt to perform any curve fitting regarding this account, as none appears in his study; in the absence of performing this essential analysis, he settles for again casting doubt on the reliability of Company accounting data. ETI contends that, in reality, Mr. Pous appears to present no recommendation for this account based on evaluation of any of the accounting data that actually depicts the past and current characteristics of the assets.⁵¹¹

⁵⁰⁸ Cities Ex. 5C (Pous Depreciation Study) at 48.

⁵⁰⁹ ETI Ex. 13 (Watson Direct) at Ex. DAW-1 at 49.

⁵¹⁰ Cities Ex. 5C (Pous Depreciation Study) at 48-49.

⁵¹¹ *Id.* at 48-50.

ETI argues that its recommended life is clearly supported by the Company-specific data, graphically depicted in Mr. Watson's rebuttal testimony, while Mr. Pous' suggested life parameter is not even close, and is based on unsupported speculation.⁵¹²

Although the evidence on this issue is sparse, the ALJs ultimately are persuaded that ETI's (and Staff's) position is more reasonable. Accordingly, the ALJs recommend the Commission adopt ETI's proposed 26 L4 life span.

(b) Net Salvage Value

Staff disagrees with Mr. Watson's recommendations for five of the distribution accounts, and Mr. Pous disagrees regarding two of the accounts. The parties' positions on distribution net salvage values in dispute are set out immediately below:

Distribution Plant Net Salvage				
Account	Approved Rate	ETI Proposal	Staff Proposal	Cities Proposal
361	-5%	-10%	-5%	-10%
362	+15%	-20%	-10%	0%
365	+10%	-7%	-7%	0%
368	0%	0%	-5%	0%
369.1	-10%	-5%	-10%	-5%
369.2	-10%	-5%	-10%	-5%

(i) Account 361 – Structures and Improvements

The existing net salvage value for this account is negative five percent, which is the value proposed by Staff. Mr. Watson and Mr. Pous, on the other hand, proposed a salvage value of negative 10 percent.

Mr. Watson's recommendation is based on the most recent five-year and ten-year net salvage ratios, which are negative 9.70 percent and negative 36.70 percent, respectively. Ms. Mathis' recommendation is based on analysis of historical salvage data for the period of 1984 through 2010. Specifically, the two-year moving average median for the same period produces a net salvage rate of

⁵¹² ETI Ex. 71 (Watson Rebuttal) at 46-48.

negative 5.87 percent, which is very close to the currently approved net salvage rate for this account.⁵¹³ Moreover, the one-year, three-year, four-year, five-year, six-year, and seven-year moving average medians of negative 6.95 percent, negative 5.11 percent, negative 3.64 percent, negative 1.90 percent, negative 4.57 percent, and negative 7.24 percent, respectively, support this recommendation. Additionally, this account contains a few significant outliers, such as negative 655.91 percent in 2002 and negative 322.55 percent in 2005.⁵¹⁴ Ms. Mathis' use of the median average eliminates the skewing effect of these outlying values.

As discussed in Section VII.C.1, the use of the median is the most appropriate methodology. For this reason, the ALJs recommend the Commission approve Staff's proposed negative 5 percent net salvage value.

(ii) Account 362 – Station Equipment

The existing net salvage value of this account is positive 15 percent. Mr. Watson proposed that it be changed to negative 20 percent, Staff proposes it be changed to negative 10 percent, and Cities propose it be changed to zero.

Mr. Watson's study shows that the most recent five-year and ten-year net salvage ratios are negative 22.10 percent and negative 43.55 percent, respectively. He recommended negative 20 percent net salvage based on the Company's experience.⁵¹⁵

Ms. Mathis' recommendation is based on analysis of historical salvage data for the period of 1984 through 2010. Specifically, the recommendation is supported by the two-year moving average median for the same period of negative 12.23 percent.⁵¹⁶ Moreover, the one-year, three-year, five-year, six-year, seven-year, and eight-year moving average medians of negative 11.07 percent,

⁵¹³ Staff Ex. 2 (Mathis Direct) at 27.

⁵¹⁴ *Id.* at Appendix C at 4.

⁵¹⁵ ETI Ex. 13 (Watson Direct) at Ex. DAW-1 at 68.

⁵¹⁶ Staff Ex. 2 (Mathis Direct) at 27.

negative 14.16 percent, negative 7.62 percent, negative 8.19 percent, negative 11.75 percent, and negative 14.15 percent, respectively, support her recommendation.⁵¹⁷

Mr. Pous' recommendation is based on what he characterizes as the Company's actual, unadjusted, experience; recognition of the type of investment in the account; recognition of significant value of scrap copper; investigation of retirement mix compared to investment mix over the past ten years; and recognition of industry values.⁵¹⁸ According to Mr. Pous, given the significant increase in the value of copper, the retirement of a transformer could be expected to significantly influence the net salvage value for this account.

Mr. Pous' recommendation is the outlier among the three before the ALJs, and the ALJs are not convinced that the reasons put forth by Mr. Pous in support of his position are sufficient to carry the day. The real argument here is between ETI and Staff, which centers on the use of the median (Staff) and the mean (ETI). As discussed in Section VII.C.1, the use of the median is the most appropriate methodology. For this reason, the ALJs recommend the Commission approve Staff's proposed negative 10 percent net salvage value.

(iii) Account 365 – Overhead Conductors and Devices

The current net salvage value for this account is positive 10 percent.⁵¹⁹ ETI and Staff recommend changing it to negative seven percent, and Cities recommend changing it to zero.

Mr. Pous recommended a reduction in the current net salvage values to zero based on review of the actual historical data and the relative mix of the investment recorded in this account. Mr. Pous noted that \$40 million of investment recorded in this account is associated with clearing rights of way, which will not likely be retired or incur cost of removal or gross salvage. Another \$40 million

⁵¹⁷ *Id.* at Appendix C at 4-5.

⁵¹⁸ Cities Ex. 5C (Pous Depreciation Study) at 26.

⁵¹⁹ *Id.* at 28.

is associated with investment in copper conductors, which has escalated in demand in recent years and should result in positive net salvage.⁵²⁰

Mr. Watson corrected his analysis and recognized that timing differences between the recording of accounting adjustments related to net salvage (*i.e.*, salvage and removal costs for a particular transaction were not recorded at the same time) made one of the recent years less representative of reasonably expected ongoing net salvage levels. He focused, therefore, on longer period averages and recommends negative seven percent net salvage consistent with the most recent ten-year ratios.⁵²¹ Mr. Watson explained that his adjustments removed relocation activity altogether from this account because it is not characteristic of the vast majority of retirements and because, if the adjustment is not made, it will shorten and skew the life analysis. Further, Mr. Watson stated that Mr. Pous' claims regarding the impact of copper prices ignore those prices' future volatility and are not supported by any analysis or quantification specific to these accounts. Mr. Watson indicated that his recommendations are based on the most clear and reliable source – Company-specific accounting data – not “selective comparisons of industry norms,” as alleged by Mr. Pous.⁵²²

The ALJs find Mr. Watson's explanations of the rationale behind his analysis to be both credible and convincing. Accordingly, the ALJs recommend the Commission adopt ETI's requested negative 7 percent net salvage value.

(iv) Account 368 – Line Transformers

The existing net salvage value for this account is zero, which both Mr. Watson and Mr. Pous recommended be retained. Ms. Mathis, on the other hand, argued that the net salvage value should be changed to negative five percent.

The argument here is whether the median or the mean best represents the appropriate net salvage value. ETI argues for the mean, and Staff argues for the median. As discussed in

⁵²⁰ *Id.* at 28-29.

⁵²¹ ETI Ex. 13 (Watson Direct) at Ex. DAW-1 at 69.

⁵²² ETI Ex. 71 (Watson Rebuttal) at 68-69.

Section VII.C.1, the use of the median is the most appropriate methodology. For this reason, the ALJs recommend the Commission approve Staff's proposed negative five percent net salvage value.

(v) Account 369.1 – Overhead Services

The existing net salvage value for this account is negative 10 percent, which Staff recommends be retained. Mr. Watson and Mr. Pous argue in favor of a change to negative 5 percent net salvage value.

The argument here is whether the median or the mean best represents the appropriate net salvage value. ETI argues for the mean, and Staff argues for the median. As discussed in Section VII.C.1, the use of the median is the most appropriate methodology. For this reason, the ALJs recommend the Commission approve Staff's proposed negative 10 percent net salvage value.

(vi) Account 369.2 – Underground Services

ETI began specifically charging salvage and removal cost to this account just in the last two years, producing a five-year net salvage ratio of negative 15.75 percent. Mr. Watson recommended moving from the current negative 10 percent to negative five percent net salvage.⁵²³ Mr. Pous agreed. Because of the limited available data, Ms. Mathis recommended retaining the existing negative 10 percent net salvage.⁵²⁴

The ALJs agree with Staff that because of the limited retirement activity, a reasonable net salvage rate cannot be calculated from the historical salvage data. Accordingly, the ALJs recommend the Commission adopt the negative 10 percent net salvage value proposed by Staff.

5. General Plant

General plant includes some accounts that are subject to depreciation, and some that are subject to amortization. ETI proposes to adopt "Vintage Group Amortization," consistent with

⁵²³ ETI Ex. 13 (Watson Direct) at Ex. DAW-1 at 70.

⁵²⁴ Staff Ex. 2 (Mathis Direct) at 34.

FERC Rule AR-15 for Accounts 391-397.1 and Account 398. This approach, approved by both the FERC and the Commission (Docket No. 38339), does not affect the annual level of expense, but provides for timely retirement of assets and simplifies accounting for general property.⁵²⁵ Ms. Mathis concurred in the Company's proposal to adopt Vintage Group Amortization and with its recommendations for lives, amortization periods, and net salvage.⁵²⁶

The increase in expense for general plant proposed by ETI is due to the need to reduce the deficit in the general plant reserve caused by inadequate account level rates in the past.⁵²⁷ This is a matter of debate among the parties, as discussed in more detail below.

(a) Account 390 – Structures and Improvements (Life Parameter)

Based on his analysis of the data in comparison to various potential dispersion curves, Mr. Watson recommended an increase in the life of this account to 45 R2.⁵²⁸ Ms. Mathis agreed with this life. Mr. Pous proposed a significantly longer life (54 S0.5) and claimed that Mr. Watson did not adequately investigate the data and investments in this account. Mr. Pous concluded that “superstructures and roadways” are a significant element in the account which can be expected to have a long life.⁵²⁹

ETI contends that Mr. Pous' analysis is incorrect. First, as confirmed by his workpapers, Mr. Watson conducted an analysis of five bands, not a single band as alleged by Mr. Pous. Furthermore, Mr. Pous' argument regarding long lives, based on the idea that the investment dates back to 1927, is contrary to the actual data showing a minute amount of old investment (0.02 percent of the account) dating back only to 1939. The average age of investment in the account, however, is

⁵²⁵ ETI Ex. 13 (Watson Direct) at Ex. DAW-1 at 2-3.

⁵²⁶ Staff Ex. 2 (Mathis Direct) at 35-37.

⁵²⁷ ETI Ex. 13 (Watson Direct) at Ex. DAW-1 at 2-3.

⁵²⁸ *Id.* at Ex. DAW-1 at 56.

⁵²⁹ Cities Ex. 5C (Pous Depreciation Study) at 51.

only 15.87 years. Mr. Watson explained that the actual data shows no investment has achieved a life of 85 years, as alleged by Cities.⁵³⁰

The ALJs believe that the actuarial analysis and curve fitting shown in Mr. Watson's direct and rebuttal testimony demonstrate a more reasonable approach, as recognized by Staff witness Mathis. Therefore, the ALJs recommend the Commission adopt the 45 R2 life parameter recommended by ETI.

(b) Account 390 – Structures and Improvements (Net Salvage Value)

Account 390 is a depreciable account for structures and improvements. Though the current authorized net salvage is zero, Mr. Watson recommended a negative five percent net salvage value, and Staff agrees with this recommendation. Mr. Pous recommended a positive 15 percent net salvage value.

Mr. Watson based his recommendation on the most recent five-year and ten-year ratios, which are negative 1.51 percent and negative 34.27 percent.⁵³¹ Mr. Pous disagreed, arguing that: (1) Mr. Watson's data adjustments present an incorrect picture of the salvage history; and (2) Mr. Watson failed to account for the difference in net salvage values between the retirements of leaseholds, versus Company-owned facilities, which should not produce negative salvage.⁵³²

According to ETI, Mr. Pous' argument that retirement and sales of buildings will result in positive net salvage is not backed up by the Company-specific data for this account. Such data shows that negative net salvage has occurred in every period of the most recent ten-year moving average. Averages of six years or longer range from negative 4.56 percent to negative 34.27 percent.⁵³³ ETI also argues that Mr. Pous' attempt to use sales of facilities as an element of depreciation analysis is contrary to Commission precedent regarding building sales' and that his

⁵³⁰ ETI Ex. 71 (Watson Rebuttal) at 49.

⁵³¹ ETI Ex. 13 (Watson Direct) at Ex. DAW-1 at 73.

⁵³² Cities Ex. 5C (Pous Depreciation Study) at 31.

⁵³³ ETI Ex. 71 (Watson Rebuttal) at 73-74.

opinion is contrary to the facts that such sales are unique circumstances that do not reasonably represent the ongoing year-to-year retirement activity that should form the basis of depreciation analysis.

The ALJs find that Mr. Pous' arguments are not supported by the facts and that Mr. Watson's explanations are the more credible. Accordingly, the ALJs recommend the Commission adopt ETI's proposed negative five percent net salvage value for this account.

(c) General Plant Reserve Deficiency

A \$21.3 million deficit has developed over time in the reserve for the accounts that ETI proposes should be converted to General Plant Amortization. This deficit, or under-recovery, has occurred because assets have been retired more quickly than can be addressed by the existing amortization rate. ETI, therefore, proposes a \$2.1 million annual expense level to recover the deficit over ten years.⁵³⁴ Ms. Mathis recommended that the amortization of the reserve deficiency be rejected and that the deficit be recovered through application of the remaining life method to the individual accounts where the deficit occurred.⁵³⁵

ETI argues that although Ms. Mathis' recommendation could theoretically allow recovery, her calculation of the amortization for the accounts that created the deficit is erroneous and insufficient to carry out her proposed concept for recovery. During her cross examination, Ms. Mathis agreed that she had intended to take the elements of the remaining life calculation method exclusively from Mr. Watson's depreciation study.⁵³⁶ ETI contends that she failed to pull the correct values from Mr. Watson's study and her numbers did not match the corresponding entries from Mr. Watson's study.⁵³⁷ For example, Ms. Mathis affirmed that her remaining life calculations were intended to allow recovery of the remaining investment in general plant account 391.2. The

⁵³⁴ ETI Ex. 13 (Watson Direct) at Ex. DAW-2 at 2, App. A-2 at 1-2.

⁵³⁵ Staff Ex. 2 (Mathis Direct) at 38.

⁵³⁶ Tr. at 1752-1753.

⁵³⁷ Tr. at 1746-1759.

remaining investment she provided for was \$10.9 million of an original cost of \$21.7 million.⁵³⁸ The actual remaining investment in the account, however, as shown in the data she purported to rely on, was a *credit* balance of negative \$4.4 million, meaning that not only the original cost, but \$4.4 million *additional* investment remained unrecovered.⁵³⁹ Ms. Mathis had no explanation for the difference. In fact, it appears that she erroneously substituted the *theoretical* reserve for the account in Mr. Watson's study (\$10.789 million) as the actual book reserve, resulting in an erroneous calculation of the amount yet to be recovered.⁵⁴⁰ Mr. Watson's rebuttal points out the errors in the calculation and provides an exhibit to properly reflect the remaining life approach that Ms. Mathis intended.⁵⁴¹

However, Mr. Watson's rebuttal also explained the reasons that the Company's approach is better. By using a ten-year amortization period for the deficit, ETI lowers the annual amount of the expense in rates to \$2.1 million. Once Ms. Mathis' calculation is corrected, because the remaining lives through which the asset value is recovered are so short, her remaining life approach increases the annual expense of amortization to \$5.8 million. Given the significant level of expense involved, ETI personnel had asked Mr. Watson to moderate the remaining life approach in this instance by using a ten-year amortization period that was consistent with the approach used by another affiliate within the Entergy system. Moreover, although Ms. Mathis purports to rely on the Commission's decision in Docket No. 38339 in support of her proposal, that case includes no discussion of rejecting the proposal on general plant that Mr. Watson makes here.⁵⁴²

The ALJs have reviewed the evidence cited by both parties and the testimony offered in support of their respective positions. It is clear to the ALJs that Ms. Mathis inadvertently did exactly what ETI alleges – she got numbers confused and, in so doing, confused her analysis. The ALJs find that ETI's proposed \$2.1 million annual expense level to recover the deficit over ten years be approved by the Commission.

⁵³⁸ Tr. at 1754; Staff Ex. 2 (Mathis Direct) at Ex. JLM-2 at 4.

⁵³⁹ Tr. at 1755.

⁵⁴⁰ Tr. at 1759-1761.

⁵⁴¹ ETI Ex. 71 (Watson Rebuttal) at 84, Ex. DAW-R-5.

(d) Amortization Period for Account 391.2 – Computer Equipment

Mr. Pous challenged the amortization period for this account, contending, contrary to Staff and Mr. Watson, that the Company's proposal to amortize general plant using "Vintage Group Amortization" is not consistent with FERC pronouncement AR-15. ETI argues that Mr. Pous' critique is wrong because the five-year life of which Mr. Pous complains is based on standard life analysis. The life has nothing to do with AR-15, which does not determine such matters. Mr. Watson's study clearly explains that he based the life parameter on standard actuarial analysis.⁵⁴³

According to ETI, Mr. Pous' own recommendation points out the fallacy of his arguments about AR-15. He recommended a one-year increase in the amortization, which does not match the previous period of depreciation for this account, or the previous depreciation rate, despite that being the supposed flaw in Mr. Watson's approach.⁵⁴⁴ Mr. Watson explained that the use of AR-15 does not involve any independent tinkering with the life of the asset account because the AR-15 process "provides for the amortization of general plant over the same life as recommended," based on standard life analysis, which Mr. Watson's study recognized.⁵⁴⁵

The ALJs are persuaded by ETI's arguments on this point. FERC pronouncement AR-15 requires amortization over the same life as recommended based on standard life analysis. Mr. Watson's study employed standard life analysis to ascertain the recommended five-year life. The ALJs therefore recommend the Commission adopt the five-year life proposed by ETI.

6. Fully Accrued Depreciation

Mr. Pous claimed that the Company has failed to conform its Commission-authorized depreciation rates when it stops accruing depreciation on accounts and sub-accounts that are fully accrued. He testified that the Company must continue to depreciate such accounts, despite the fact

⁵⁴² *Id.* at 80-81.

⁵⁴³ ETI Ex. 13 (Watson Direct) at Ex. DAW-1 at 58.

⁵⁴⁴ Cities Ex. 5 (Pous Direct) at 36.

⁵⁴⁵ ETI Ex. 13 (Watson Direct) at Ex. DAW-1 at 2.

that this policy would mandate that the Company intentionally create negative depreciation amounts that do not relate to the existence of any depreciable asset still in existence. Mr. Pous testified that neither standard depreciation definitions nor GAAP or National Association of Regulatory Utility Commissioners (NARUC) depreciation guidance support the Company's action.⁵⁴⁶ The impact of Mr. Pous' recommendation is to impute an additional \$6,447,731 depreciation amount to reduce rate base and amortize that credit over four years, with an associated revenue requirement reduction of \$1,611,933.⁵⁴⁷

ETI argues that Mr. Pous pointed to no instance in which his theory has been adopted by the Commission, or any other regulatory body. Other regulators within the Entergy system have rejected his position.⁵⁴⁸ The RRC, which sets gas utility rates under essentially the same regulatory framework as PURA, has rejected Mr. Pous' position on three separate occasions.⁵⁴⁹ ETI contends that Mr. Pous' suggestion violates GAAP, which requires that once an asset's service value (original cost less net salvage) has been fully amortized through the application of the most recently approved depreciation rates, there is no further service value to be recognized. This has been ETI's practice as long as ETI regulatory accounting witness Considine has been aware. Furthermore, ETI suspends depreciation only so long as the account is fully amortized. Once additional activity hits the account, depreciation will begin again under the Company's automated systems.⁵⁵⁰

ETI also argues that Mr. Pous' retroactive approach is unreasonably selective. He would reach back into recoveries under existing rates to reclaim revenues associated with the depreciation expense that relates to the fully accrued accounts. According to ETI, Mr. Pous takes no notice of the depreciation taken on new assets that are not included in rate base or recovered through depreciation expense under existing rates. ETI witness Considine notes that Mr. Pous has essentially formulated

⁵⁴⁶ Cities Ex. 5 (Pous Direct) at 39-45.

⁵⁴⁷ *Id.* at 45.

⁵⁴⁸ ETI Ex. 46 (Considine Rebuttal) at 45-46.

⁵⁴⁹ ETI Ex. 71 (Watson Rebuttal) at 81, n. 61; ETI Ex. 46 (Considine Rebuttal) at Ex. MPC-R-11.

⁵⁵⁰ ETI Ex. 46 (Considine Rebuttal) at 44-45, 47.

a one-sided exact recovery mechanism for depreciation expense that is completely unique in the annals of base rates.⁵⁵¹

According to ETI, Mr. Pous also ignores that the remaining life depreciation method already addresses any over- or under-accrual of depreciation expense. As depreciation rates and the remaining life are adjusted over time, any over (under) recovery will be carried forward and the net (if any) of the original investment less any accumulated reserve will begin to be recovered under the new and future rate structures. This is the basic concept of remaining life depreciation rates. Thus, ETI contends that no further actions or adjustments are appropriate.⁵⁵²

The ALJs find that Mr. Pous' recommendation has previously been rejected, by other regulatory bodies. There is nothing in the arguments advanced by Cities that changes that fact. Accordingly, the ALJs recommend the Commission reject Cities' proposal.

7. Other Depreciation Issues – Accumulated Provision for Depreciation

ETI proposes to amortize the \$21 million general plant deficiency over ten years. Both the Cities and Staff agree with and use the accumulated depreciation reserve amounts per account from Mr. Watson's study.⁵⁵³ TIEC witness Pollock, in arguing against amortization of the amortized general plant reserve deficiency, testified that this reserve deficiency should instead be simply reallocated to other depreciable general plant accounts that have depreciation surplus.⁵⁵⁴

Mr. Pollock discussed transferring the depreciation reserve between the amortizable and depreciable general plant accounts. He failed to show, however, how the reserve reallocation would be computed and provided no workpapers to substantiate his analysis. ETI argues that without a verifiable basis for the computations, his recommendations to recompute general plant depreciation accruals should be rejected.

⁵⁵¹ *Id.* at 43, 45.

⁵⁵² ETI Ex. 71 (Watson Rebuttal) at 78.

⁵⁵³ *Id.* at 77.

⁵⁵⁴ TIEC Ex. 1 (Pollock Direct) at 38-39.

ETI also argues that Mr. Pollock's testimony shows that he has reallocated the amortizable general plant deficiency from the amortized general plant accounts to the depreciable general plant accounts. The depreciable plant accounts have shorter remaining lives than the ten-year amortization of the deficiency proposed by ETI.⁵⁵⁵ ETI contends that common sense dictates that transferring dollars from an account with a relatively longer remaining life to one with a shorter life will yield a higher annual depreciation or amortization expense, yet Mr. Pollock somehow takes this step and still arrives at a lower level of expense.

According to ETI, Mr. Pollock's methodology has the effect of "amortizing the difference between the book and theoretical reserve over a time period that is significantly shorter than the average remaining life of the assets within this function."⁵⁵⁶ ETI asserts that such an adjustment to depreciation and amortization expense was rejected by the Commission in the CenterPoint rate case, and it should be rejected here.⁵⁵⁷

TIEC argues that it does not propose any amortization of any accounts. Rather, TIEC states that it is proposing a more efficient method for ETI to cure its deficits. Because ETI retired equipment prior to the end of the assumed life of those assets, there is approximately a \$21,300,000 deficiency in general plant accounts. ETI seeks to amortize the deficiency over ten years so that the book reserve will "catch-up" with the theoretical depreciation reserve for the deficient reserve. TIEC contends that its position is that the catch-up adjustment is not necessary.⁵⁵⁸

The ALJs have reviewed the evidence and arguments advanced by the parties and find that those of ETI are more persuasive. Accordingly, the ALJs recommend the Commission reject TIEC's recommendation.

⁵⁵⁵ ETI Ex. 13 (Watson Rebuttal) at Ex. DAW-1, App. A-1 at 4.

⁵⁵⁶ ETI Ex. 71 (Watson Rebuttal) at 75.

⁵⁵⁷ *Id.* at 75-76.

⁵⁵⁸ TIEC Ex. 1 (Pollock Direct) at 37.

D. Labor Costs**1. Payroll and Related Adjustments**

A number of parties suggest various adjustments to ETI's proposed payroll and related costs. In the application, ETI's Test Year payroll costs were adjusted downward by \$957,695 to reflect a decrease in the employee headcount levels at ETI during the Test Year. At the same time, payroll costs were increased in the amount of \$1,105,871 to account for employee pay raises. The net result was that ETI's Test Year payroll expense was adjusted upward by \$148,176. Similar calculations were made for ESI employees, resulting in a net upward adjustment for ESI payroll expenses of \$852,493. Thus, ETI requested an upward adjustment of \$1,000,669 (\$148,176 plus \$852,493) for ETI and ESI payroll expenses.⁵⁵⁹

Cities oppose one part of these proposed adjustments. As noted above, ETI is proposing an upward adjustment to account for pay raises given to ETI and ESI employees. One set of those raises was given to employees in early August 2011, one month after the end of the Test Year. Another set of raises was given to employees in April 2012, roughly nine months after the end of the Test Year. Cities witness Garrett testified that it is acceptable to make an adjustment for the raises made in August 2011 because they occurred shortly after the end of the Test Year. However, he stated that it is unreasonable to include an adjustment for the raises given in April 2012. He believes that any increase in costs due to the April 2012 pay raises might be offset by changes in productivity and the overall workforce that may occur during the same time period, such as the replacement of higher-paid workers who retire with new, lower paid employees.⁵⁶⁰ Thus, Cities propose an adjustment that would reverse ETI's proposed increase for the April 2012 pay raises thereby reducing payroll expense by \$1,185,811.⁵⁶¹ No other party makes a similar challenge to the April 2012 pay raise.

⁵⁵⁹ ETI Ex. 8 (Considine Direct) at 24-25; 3 at Sched. A-3 and WP/P AJ22.

⁵⁶⁰ Cities Ex. 2 (Garrett Direct) at 13-15.

⁵⁶¹ *Id.* at 19.

With regard to the adjustments proposed by ETI, Staff witness Givens accepted the adjustments for headcount changes and the pay raises, but recommended a further downward adjustment of \$778,034 to account for a further decrease in ETI employee headcount levels from 678 at Test Year-end to 660 as of February 2012. She also recommended an upward adjustment of \$158,589 to account for an increase in ESI employee headcount levels from 3,055 to 3,089 as of December 2011.⁵⁶² Ms. Givens also recommended that, in addition to adjusting payroll expense levels, the more recent headcount numbers should be used to adjust the level of payroll tax expenses, benefits expenses, and savings plan expenses.⁵⁶³ As an alternative to its primary line of attack (discussed above), Cities agree with the adjustments recommended by Staff.

ETI also agrees, in concept, with the adjustments recommended by Staff, but contends that Ms. Givens made some errors in her calculations. First, according to ETI, Ms. Givens used erroneous headcounts for the end of the Test Year for ETI and ESI. According to the Company, ETI's headcount at Test Year-end was 675 and ESI's was 3,054. Ms. Givens wrongly used headcounts of 678 and 3,055, respectively, which caused a double counting of three ETI employees and one ESI employee.⁵⁶⁴ Second, Ms. Givens made an error in the calculation of benefits costs associated with the updated ESI headcount. Ms. Givens inadvertently used the ETI percentage in the calculation rather than the ESI percentage shown on her exhibit.⁵⁶⁵ Third, Ms. Givens' adjustment for savings plan expense was not necessary and is thus inappropriate. According to ETI witness Considine, savings plan expense is already included in benefits expense levels so it would be double counting to adjust for both benefits expense and savings plan expense.⁵⁶⁶ Fourth, Ms. Givens' full-time equivalent calculations need to be corrected. She included an incorrect assumption regarding part time employee salaries. Ms. Givens assumed that a part time employee's average salary is 50 percent of the full time average salary. In his rebuttal testimony, Mr. Considine provided the correct calculation of full time equivalents, thereby making it unnecessary to rely upon

⁵⁶² Staff Ex. 1 (Givens Direct) at 10-12.

⁵⁶³ *Id.* at 13-15.

⁵⁶⁴ ETI Ex. 46 (Considine Rebuttal) at 32-33.

⁵⁶⁵ *Id.* at 33.

⁵⁶⁶ *Id.*

an assumed average.⁵⁶⁷ According to Mr. Considine, the combined impacts of these errors is that Ms. Givens' ETI headcount adjustment overstated her O&M payroll reduction by \$224,217, and her ESI headcount adjustment understated her O&M payroll increase by \$37,531.⁵⁶⁸ No party challenged these corrected numbers.

The ALJs are unpersuaded by Cities' attempt to exclude the April 2012 pay raises. There can be no real dispute about the fact that the pay raises are known and measurable. Moreover, there is an obvious logical inconsistency in the Cities' position – on the one hand they oppose consideration of certain pay raises because they fall outside the Test Year, and on the other hand they support consideration of headcount reductions even though they also fall well outside the Test Year.

The ALJs are also persuaded that, conceptually, the adjustments suggested by Staff are reasonable and appropriate. Indeed, all parties agree on this point. Moreover, no party challenged the corrections to Staff's adjustments that were suggested by ETI, and the ALJs can find no basis for challenging those corrections. Thus, the ALJs recommend that the Commission: (1) accept the payroll adjustments proposed in the ETI application; and (2) accept the further payroll adjustments proposed by Staff, corrected by ETI.

2. Incentive Compensation

One of the hotly contested issues concerns the extent to which ETI should be allowed to recover, through its rates, the incentive compensation it pays to its employees. All parties agree that Commission precedent generally identifies two types of incentive compensation, only one of which is recoverable. Specifically, pursuant to Commission precedent, incentive compensation that is tied to operational goals is recoverable, while incentive compensation that is tied to financial goals is not.⁵⁶⁹ In its application, however, ETI requests that it be allowed to recover its Test Year costs of

⁵⁶⁷ *Id.* at 34.

⁵⁶⁸ *Id.* at MPC-R-5, and MPC-R-6.

⁵⁶⁹ See, e.g., TIEC Initial Brief at 51-52; see also AEP Application of AEP Texas Central Company for Authority to Change Rates, See Docket No. 33309, Order on Rehearing at FoF 82 (Mar. 4, 2007); Application of AEP Texas Central Company for Authority to Change Rates, Docket No. 28840, Order at FoF 164-170 (Aug. 15, 2005).

all of its incentive compensation costs, regardless of whether those costs are tied to operational goals or to financial goals.

(a) Financially Based Incentive Compensation Should Not Be Recoverable

ETI acknowledges that costs of incentive compensation tied to financial goals have typically been disallowed by the Commission. However, ETI asks for the Commission to reconsider its precedents on this issue.⁵⁷⁰ ETI argues that the Commission precedent is not, and should not be, a hard and fast rule. ETI contends that the reason why cost recovery has been denied for incentive compensation in prior rates cases is that, in those prior cases, there was “a lack of evidence showing sufficient customer benefits.”⁵⁷¹ ETI asserts that, in this case, it has assembled evidence not previously considered by the Commission that shows the benefits to customers of using financial measures in incentive compensation programs. For example, ETI argues that incentive compensation that encourages the financial health of a company also benefits customers because:

- (1) if a company maintains a financially healthy position, it will tend to have a lower cost of capital that will in turn benefit customers through lower rates;
- (2) a financially healthy company will be more prepared for emergency events such as storms (which is particularly important in the Gulf Coast areas served by ETI, which are subject to experiencing hurricanes); and
- (3) with financial health, the costs of doing business with suppliers (of both goods and services, including labor) will remain lower because, for example, if a company was not in a financially stable condition, suppliers would tend to demand higher prices or more onerous credit terms, resulting in higher costs that would lead to higher rates than would otherwise occur.

ETI witness Kevin Gardner, Vice President of Human Resources for ESI, testified that customers receive benefits from those portions of the incentive compensation plans that are tied to financial goals and measures. He explained that incentive compensation based on financial metrics is a reasonable, necessary, and common component of compensation for companies like ETI. He also opined that such incentives are a market necessity that ETI must include in its compensation package so that it can hire and retain talented employees. He contended that customers benefit from

⁵⁷⁰ Tr. at 1726.

⁵⁷¹ ETI Initial Brief at 129.

the incentives because they attract and keep qualified people.⁵⁷² Mr. Gardner further testified that disallowing financially-based incentives would only encourage utilities to eliminate them, thus weakening the alignment of employees' financial interests with the interest of the ratepayers in having an efficiently run and financially healthy utility. He opined that having only operational incentives could encourage utilities to overspend in some areas resulting in an incomplete, unbalanced incentive program that would be atypical when compared with American industry in general.⁵⁷³

A second ETI witness, Dr. Jay Hartzell, also testified in favor of the concept of allowing ETI to recover its costs associated with its financially-based incentive compensation. He is a professor of finance in the business school at the University of Texas at Austin. Dr. Hartzell acknowledged the historical distinction that has been made by the Commission between compensation tied to financial measures and compensation tied to operational measures. However, he argues that this distinction is based upon a "false dichotomy" and that the more appropriate focus should be on whether customers benefit from the incentive in question, regardless of whether it is a financial or operational incentive.⁵⁷⁴ Dr. Hartzell summarized his key opinion as follows:

In my opinion, a well-designed compensation plan that includes incentive compensation tied to cost controls, profitability, and stock prices would tend to provide greater benefits to customers than an otherwise similar compensation plan that did not include any such incentive compensation.⁵⁷⁵

Dr. Hartzell argues that compensation linked to stock prices (provided it is part of a reasonable, well-designed compensation plan) has four advantages for customers, :

- helps ensure that managers will consider the financial health of the company when they make decisions, and it is in customers' interests for the company be financially healthy;
- provides an incentive for managers and employees to ensure that the company operates efficiently, resulting in lower rates than would otherwise occur;

⁵⁷² ETI Ex. 36 (Gardner Direct) at 31.

⁵⁷³ *Id.* at 32.

⁵⁷⁴ ETI Ex. 15 (Hartzell Direct) at 3-4, 6, and 9-10.

⁵⁷⁵ *Id.* at 7.

- provides a monitoring mechanism for managerial decision-making and the overall quality of management; and
- results in lower customer costs because capital markets will tend to reward efficient long-term investments or capital expenditures.⁵⁷⁶

Dr. Hartzell cited a number of studies which support the theory that the benefits of incentive compensation linked to stock price and profitability measures extend to customers of the company, such as by lowering the company's cost of capital, increasing the company's ability to respond to external shocks, improving customer satisfaction, and increasing oversight on managerial decisions.⁵⁷⁷

Conversely, Dr. Hartzell opined that if the use of incentive compensation linked to profitability and stock prices is discouraged, via Commission policy disallowing recovery of the costs of such compensation, then utility customers would be adversely affected. For example, if employees did not receive any incentive compensation, salaries would have to be higher to attract and retain the same quality of talent. Dr. Hartzell also testified that a compensation plan solely consisting of salary and incentives based on operational performance could likely lead to "horizon problems," meaning that, absent incentives to focus on the long run health of the company, managers might maximize their immediate compensation at the expense of longer-run benefits that the customer could have enjoyed.⁵⁷⁸

All of the other parties oppose ETI's efforts to recover the costs of its incentive compensation tied to financial goals. The parties uniformly agree that the Commission has a well-established and straightforward policy regarding the recoverability of incentive compensation through rates: incentive compensation that is tied to operational goals is recoverable; incentive compensation tied to financial goals is not.⁵⁷⁹ They contend that ETI's position in this case flies directly in the face of

⁵⁷⁶ *Id.* at 13-14.

⁵⁷⁷ ETI Ex. 15 (Hartzell Direct) at 15-21.

⁵⁷⁸ *Id.* at 22-25.

⁵⁷⁹ TIEC Reply Brief at 35; State Agencies Initial Brief at 14; OPC Reply Brief at 12; Staff Initial Brief at 56; Cities Initial Brief at 67; *see also, Application of AEP Texas Central Company for Authority to Change Rates*, Docket No. 33309, Order on Rehearing at FoF 82 (Mar. 4, 2007); *Application of AEP Texas Central Company for Authority to Change Rates*, Docket No. 28840, Order at FoF 164-170 (Aug. 15, 2005).

that policy. TIEC points out that ETI has offered no legal authority, such as a statute or rule, which would justify its desire to have the Commission reverse its policy and allow the recovery of incentive compensation tied to financial goals. State Agencies similarly argue that ETI failed to establish a reason why the Commission should deviate from its long-standing policy. The parties also support the reasoning behind the Commission's policy: that financially-based incentives are of more immediate benefit to shareholders, not ratepayers, and therefore are not necessary and reasonable for the provision of service.

State Agencies point out that, in support of his theory that financially-based incentives provide benefits to ratepayers, Dr. Hartzell relied upon studies of utilities in competitive markets. Thus, State Agencies contend, the studies are of little to no benefit in evaluating the effects of financially-based incentives upon ETI customers because ETI is a monopoly that is not subject to competitive pressures. Moreover, State Agencies examine at length the underlying studies relied upon by Dr. Hartzell and assert, essentially, that the studies do not fully support the findings that Dr. Hartzell ascribes to them.

Staff refutes ETI's contention that the only reason why cost recovery has historically been denied for financially-based incentive compensation is that there has been a lack of evidence showing customer benefits. For example, Staff points out that, in one of the prior dockets cited by ETI, the Commission disallowed recovery for financially-based incentive costs after stating, "Incentive compensation based on financial measures or goals is of *more immediate benefit* to shareholders."⁵⁸⁰ This suggests that the question is not, as ETI contends, whether the incentives provide *any* benefit to ratepayers. Rather, the question is whether the incentives are primarily intended to provide benefits to shareholders.

Mark Garrett, an attorney and certified public accountant who works as a consultant in the area of public utility regulation, testified on behalf of the Cities in opposition to cost recovery for financially-based incentive compensation. He stated there are a number of reasons why it makes sense to exclude financially based incentive costs from rates: (1) there is no certainty from year to

⁵⁸⁰ Staff Reply Brief at 44, quoting *Application of Oncor Electric Delivery Company for Authority to Change Rates*, Docket No. 35717, Order on Rehearing at FoF 92 (Nov. 30, 2009).

year what the level of incentive payments will be (because incentive payments are conditioned upon future events and triggers that might not occur), thereby making it difficult to set rates and recover a level of expense; (2) many of the types of factors that increase earnings per share—such as an unusually hot summer or customer growth—are outside the control of employees and have no value to customers; and (3) earnings-based incentives can discourage energy conservation.⁵⁸¹ Mr. Garrett also discussed the results of a survey of 24 other states, which revealed that 17 states closely follow Texas’ approach, and none allow full recovery of incentive compensation.⁵⁸²

Mr. Garrett testified that ETI will not be placed at a competitive disadvantage in its ability to obtain and retain qualified employees if its financially-based incentives are disallowed. He stated that the Company’s total payroll costs for 2011 were 10 percent above the market price, and that most of the above-market payroll costs derived from the incentive program.⁵⁸³

The ALJs conclude that ETI should not be entitled to recover its financially based incentive compensation costs. Based upon prior Commission precedents, the ALJs conclude that the issue is not, as ETI contends, whether such incentives might provide any benefits to customers. The proper question to be asked is whether they provide benefits most immediately or predominantly to shareholders. Without a doubt, the primary purpose of financially based incentives, such as incentives tied to earnings per share or stock price, is to benefit shareholders, not ratepayers. Even construing Dr. Harzell’s testimony in the most generous light, any benefits that might accrue to ratepayers would be merely tangential to that primary purpose.

Moreover, even if the ALJs were to completely accept as true the opinions offered by Dr. Hartzell, it would be of limited benefit to ETI because his opinions were almost completely theoretical. The premise of his testimony was that “a well-designed compensation plan” that includes incentive compensation tied to financial goals would “*tend to* provide greater benefits to customers” than a plan that did not include such compensation.⁵⁸⁴ He stressed that the customer

⁵⁸¹ Cities Ex. 2 (Garrett Direct) at 29-30

⁵⁸² *Id.* at 32-38.

⁵⁸³ *Id.* at 45-46.

⁵⁸⁴ ETI Ex. 15 (Hartzell Direct) at 7 (emphasis added).

benefits of incentive compensation tied to financial goals can only exist if such compensation is part of a larger, reasonable, and well-designed overall compensation plan.⁵⁸⁵ However, he did not meaningfully apply this abstract theory to ETI's compensation plan. For example, Dr. Harzell did not offer an evaluation of ETI's compensation plan and conclude that it is "well designed," nor did he testify that ETI's incentives tied to financial goals *actually* provide benefits to its customers. He admitted that he did not study the details of ETI's incentive plans, nor did he do any type of analysis to see if the costs of ETI's incentive programs outweighed their benefits.⁵⁸⁶ He did not know the amounts of incentive compensation that was paid by ETI.⁵⁸⁷ One of his major premises was that financially-based incentives can benefit customers by lowering their costs, but he did not know how ETI customer's costs compared with customer costs in the other Entergy operating companies.⁵⁸⁸ Another of his major premises was that financially-based incentives can benefit customers by ensuring the financial health of the Company, but he made no attempt to determine whether ETI was, in fact, a financially healthy company.⁵⁸⁹ By confining his testimony to the abstract, it is impossible to know whether Dr. Hartzell believes that ETI's incentive compensation tied to financial goals achieves the customer benefits that he believes such compensation can theoretically achieve. It is true that Mr. Gardner described some of the specifics of ETI's incentive plans. However, because Dr. Hartzell did not explain the metrics of what he would consider "a well-designed compensation plan," it is impossible to know if ETI's plan meets those metrics.

Simply put, the ALJs conclude that ETI has failed to establish a sufficient justification for overturning the well-established Commission policy that financially based incentive compensation is not recoverable.

⁵⁸⁵ See, e.g., ETI Ex. 15 (Hartzell Direct) at 13.

⁵⁸⁶ Tr. at 484.

⁵⁸⁷ Tr. at 478.

⁵⁸⁸ Tr. at 480.

⁵⁸⁹ Tr. at 481-82.

(b) The Adjustment for Financially-Based Incentive Compensation Costs

Having concluded that ETI is not entitled to recover the costs of its financially based incentive programs, it is necessary to determine the amount of those costs so that they may be removed from consideration in this rate case. The parties disagree on the correct amount. Staff argues that \$5.3 million of ETI's incentive compensation is financially based.⁵⁹⁰ TIEC contends the correct number is \$6.2 million.⁵⁹¹ Cities contend it is \$8.4 million.⁵⁹²

Broadly speaking, ETI has two categories of incentive compensation programs – annual programs and long-term programs. ETI witness Gardner testified that 100 percent of ETI's long-term programs are financially based, whereas an average, representing a far lower percentage, of the Company's annual programs are financially based.⁵⁹³ Staff witness Givens applied those percentages to determine her estimate of the amount spent by ETI in the Test Year on financially based incentives. As to the Company's long-term programs, she recommended removing the entire costs of those programs (*i.e.* 100 percent) from the cost of service. As to the Company's annual programs, she recommended removing average percentage of the costs of those programs. Ms. Givens then applied the FICA tax rate to the total amount she identified as financially based costs to account for direct taxes that ETI would have paid as a result of those costs. By her estimate, the FICA taxes associated with ETI's financially based incentives paid in the Test Year totaled \$429,096. In total, Ms. Givens recommended removing \$5,609,093 (representing ETI's financially based incentives paid in the Test Year, plus FICA taxes associated with those payments) from ETI's requested O&M expenses. However, based upon subsequent additional information supplied by ETI⁵⁹⁴ relative to the actual payroll taxes paid by the Company for its financially based incentive compensation, Staff has agreed to lower its estimate of FICA taxes from \$429,096 to \$143,801. Thus, Staff now recommends removing \$5,323,798 (representing ETI's financially based incentives

⁵⁹⁰ Staff Initial Brief at 56. (As discussed more below, Staff's original estimate was roughly \$5.6 million. The estimate was reduced, however, in response to supplemental payroll tax information supplied to Staff by ETI.)

⁵⁹¹ TIEC Initial Brief at 53-54.

⁵⁹² Cities Initial Brief at 70.

⁵⁹³ ETI Ex. 36 (Gardner Direct) at 30.

⁵⁹⁴ ETI Ex. 46 (Considine Rebuttal).

paid in the Test Year, plus FICA taxes associated with those payments) from ETI's requested O&M expenses.⁵⁹⁵

Like Ms. Givens for Staff, TIEC witness Pollock relied on the numbers and percentages concerning ETI's incentive programs that were provided by Mr. Gardner. However, Mr. Pollock calculated those numbers and percentages in a slightly different manner, leading to a different recommended reduction amount. Just as Ms. Givens did, as to the Company's long-term programs, he recommended removing the entire costs of those programs from the cost of service. ETI witness Gardner testified that actual percentages of each annual program were quite different than the average percentages for all programs used by Ms. Givens.⁵⁹⁶ Thus, as to the Company's annual programs, while Ms. Givens applied the average percentage reduction to all of the annual programs, Mr. Pollock applied the actual percentage reductions applicable to each of the annual programs. Based on Mr. Pollock's calculations, TIEC recommends removing \$6,196,037 (representing ETI's financially based incentives paid in the Test Year) from ETI's requested O&M expenses.⁵⁹⁷ TIEC appears not to have taken into account any payroll taxes associated with ETI's financially based incentives.

Cities witness Garrett took a substantially different approach when he calculated his estimate of ETI's financially based incentive costs. He agreed with Ms. Givens and Mr. Pollock that 100 percent of the Company's long-term program costs should be removed from the cost of service. As to the annual programs, however, Mr. Garrett defined what qualifies as "financially based" much more broadly than ETI, Staff, and TIEC. ETI witness Gardner testified that, when the Company's five annual programs were averaged together, specific percentages of those programs were financially based, aimed at "cost control," and aimed at "cost control, operational, safety."⁵⁹⁸ Mr. Garrett added together the percentages representing the financially-based costs, the cost-control costs, and roughly one-third of the cost-control, operational safety costs to arrive at the figure he identified as the amount of ETI's costs for its annual programs that is "related to financial

⁵⁹⁵ Staff Ex. 1 (Givens Direct) at 15-22; Staff Initial Brief at 56-63.

⁵⁹⁶ ETI Ex. 36 (Gardner Direct) at 30 and KGG-4.

⁵⁹⁷ TIEC Ex. 1 (Pollock Direct) at 41-45 and JP-7; TIEC Initial Brief at 51-54.

⁵⁹⁸ ETI Ex. 36 (Gardner Direct) at 30 and KGG-4.

performance measures.”⁵⁹⁹ Cities contend this approach is supported by the decision in a prior docket.⁶⁰⁰ Based on Mr. Garrett’s calculations, Cities recommend removing \$8,397,232 (representing ETI’s incentives “related to financial performance measures” paid in the Test Year) from ETI’s requested O&M expenses.⁶⁰¹ Mr. Garrett also agreed with Ms. Givens that an additional reduction should be made to account for the FICA taxes that ETI would have paid as a result of those costs.⁶⁰²

The ALJs reject Cities’ attempt to broadly expand the definition of what qualifies as a financially based incentive to include items such as cost control measures. Cities’ primary justification for doing so is that the Commission has done so previously in the *AEP Texas* case. As pointed out by ETI, however, the Commission did so in that case merely because AEP Texas lumped its cost control measures in with its financially based incentive costs. The evidence in this case demonstrates that ratepayers benefit when a utility incentivizes its employee to control costs. Even TIEC witness Pollock testified that “incentives that encourage employees to minimize costs are probably more or less in the best interest of ratepayers.”⁶⁰³ ETI further provided evidence establishing that cost control incentives that result in lower costs for the Company likewise result in lower rates for customers.⁶⁰⁴

As to the approaches advocated by TIEC and Staff, the ALJs conclude that TIEC’s approach more accurately captures the true cost of ETI’s financially based incentive programs. Rather than averaging across all of ETI’s annual programs (as was done by Staff), TIEC used the percentage applicable to the single annual program that included a component of financially based costs. Thus, the ALJs recommend removing \$6,196,037 (representing ETI’s financially based incentives paid in the Test Year) from ETI’s requested O&M expenses. Additionally, the ALJs agree with Staff and

⁵⁹⁹ Cities Ex. 2 (Garrett Direct) at 39-40, 46-50, MG2.10.

⁶⁰⁰ Cities Initial Brief at 68, *Application of AEP Texas Central Company for Authority to Change Rates*, Docket No. 28840, Final Order (August 15, 2005).

⁶⁰¹ Cities Ex. 1 (Garrett Direct) at 51-52 and MG2.10; Cities Initial Brief at 70.

⁶⁰² Cities Ex. 1 (Garrett Direct) at 53.

⁶⁰³ Tr. at 1528.

⁶⁰⁴ ETI Ex. 50 (Gardner Rebuttal) at 6-7, ETI Initial Brief at 137-38.

Cities that an additional reduction should be made to account for the FICA taxes that ETI would have paid as a result of those costs. That amount is not specifically known at this time.

3. Compensation and Benefits Levels

In the application, ETI included, as part of its labor costs, \$54,965,005 in base payroll paid by ETI and ESI in the Test Year. It also included \$20,428,817 in costs associated with various benefits (such as medical/dental, and life insurance) that ETI and ESI provided to their employees.⁶⁰⁵

Cities contend that the amounts for base pay and the benefits package should be reduced by \$989,370 and \$2,860,034, respectively, because the amounts paid were above the market price.⁶⁰⁶ No other party challenges the reasonableness of the base payroll and benefits package.

As to base payroll, Cities contends that the amount paid by ETI and ESI was 1.8 percent above the prevailing market price (above market).⁶⁰⁷ Cities witness Garrett acknowledges that ETI and ESI are free to pay their employees at above market wages, but he contends that ratepayers should only be asked to pay the market rate for wages, which he contends constitute the only “necessary” costs of providing utility service. Thus, Mr. Garrett and Cities recommend a 1.8 percent downward adjustment to base payroll expense (or \$989,370) “to bring the company’s base payroll down to a market-based level.”⁶⁰⁸

As to the Company’s benefits package, Cities points out that the amount paid by ETI and ESI was 14 percent above market when compared to a peer group of Fortune 500 companies.⁶⁰⁹ Cities witness Garrett again contends that ratepayers should only be asked to pay the market rate for benefits, which he contends constitute the only “necessary” costs of providing utility service. Thus,

⁶⁰⁵ Cities Ex. 2 (Garrett Direct) at 25, MG2.8, and MG2.9.

⁶⁰⁶ *Id.*

⁶⁰⁷ *Id.* at 25 and MG2.8.

⁶⁰⁸ *Id.* at 26-27 and MG2.8.

⁶⁰⁹ *Id.* at 58 and MG2.9; ETI Ex. 36 (Gardner Direct) at 41-42.

Mr. Garrett and Cities recommend a 14 percent downward adjustment to benefits expenses (or \$2,860,034).⁶¹⁰

ETI concedes that its Test Year base pay was 1.8 percent “above the market median,” but argues that this is not the same thing as being “above market.” As ETI witness Gardner explained, “being ‘at market’ means being within a reasonable range, such as +/-10 percent, of the market median; therefore, the Company’s base pay levels are at market.”⁶¹¹ According to Mr. Gardner, some compensation consultants use an even broader range, such as a +/- 15 percent range, for determining whether compensation levels are at market.⁶¹² Mr. Gardner testified that, because no two jobs are likely to be identical, attempting to benchmark jobs to a “market price” is an inexact science, involving inherent imprecision. Thus, Mr. Gardner testified that, when using a benchmark analysis to compare companies’ levels of compensation, it is advisable to view the market level of compensation as a range (*e.g.*, +/- 10 percent of a mid-point) rather than a precise, single point.⁶¹³

ETI also disputes Cities’ contention that the Test Year costs of the Company’s benefits package were 14 percent “above market.” Mr. Gardner acknowledged that the costs were 14 percent higher than those of Fortune 500 companies, but he pointed out the costs were only 1 percent above the market median of a peer group of utility companies.⁶¹⁴ ETI contends that the comparison against the peer group of utility companies provides a more appropriate comparison for ETI than Fortune 500 companies. ETI also points out that, even if equal weight were given to the comparisons against the Fortune 500 companies and the peer utilities group, the value of the Company’s benefit plans would average within a +/- 10 percent range and, therefore, be at market. Thus, ETI argues that its benefit plan levels are within a reasonable range, and no disallowance should be required.⁶¹⁵

⁶¹⁰ Cities Ex. 2 (Garrett Direct) at 58-59 and MG2.9.

⁶¹¹ ETI Ex. 50 (Gardner Rebuttal) at 11.

⁶¹² ETI Ex. 36 (Gardner Direct) at 23, and ETI Ex. 50 (Gardner Rebuttal) at 11 n. 1.

⁶¹³ ETI Ex. 50 (Gardner Rebuttal) at 11-12.

⁶¹⁴ ETI Ex. 36 (Gardner Direct) at 42.

⁶¹⁵ ETI Ex. 50 (Gardner Rebuttal) at 13-14; ETI Initial Brief at 139-142.

The ALJs conclude that ETI has met its burden to prove the reasonableness of its base pay and incentive package costs. The ALJs agree that it is reasonable to view market price for these categories of costs as lying within a range of +/- 10 percent of median, rather than being a single point along a spectrum. As to both base pay and the incentive package, ETI has proven that its costs fall within such an acceptable range. Accordingly, the ALJs recommend rejecting the adjustments sought by Cities.

4. Non-Qualified Executive Retirement Benefits

ETI provides three types of supplemental executive retirement plans: the Pension Equalization Plan, the Supplemental Retirement Plan, and the System Executive Retirement Plan.⁶¹⁶ In the application, ETI included, as part of its labor costs, \$2,114,931 in costs associated with its executive retirement plans. The expenses represent non-qualifying retirement plan expenses designed to provide retirement benefits to key managerial employees and executives who are invited to participate in the plans. They are generally available only to employees and executives earning more than \$245,000 per year.⁶¹⁷

On behalf of the Staff, Ms. Givens recommended a complete disallowance of the costs for these programs, on the grounds that they are offered to only select, highly compensated employees and are excessive. Ms. Givens offered the opinion that the expenses were not reasonable and necessary for the provision of electric utility service and were not in the public interest.⁶¹⁸ On behalf of Cities, Mr. Garrett agreed with Ms. Givens' recommendation, arguing that it is fair to have ratepayers pay for benefits included in regular pension plans, but that shareholders ought to pay for any additional benefits included in supplemental plans, "since these costs are not necessary for the provision of utility service, but are instead discretionary costs of the shareholders."⁶¹⁹ Mr. Garrett also testified that costs associated with supplemental executive retirement plans are typically

⁶¹⁶ ETI Ex. 50 (Gardner Rebuttal) at 14.

⁶¹⁷ Staff Ex. 1 (Givens Direct) at 22-23; Cities Ex. 2 (Garrett Direct) at 54.

⁶¹⁸ Staff Ex. 1 (Givens Direct) at 23; Staff Initial Brief at 64.

⁶¹⁹ Cities Ex. 2 (Garrett Direct) at 55; Cities Initial Brief at 71-72.

excluded by utility commissions in Oklahoma, Oregon, Idaho, Arizona, and Nevada.⁶²⁰ On behalf of OPC, Dr. Szerszen also recommended a complete disallowance of the portion of these costs allocated from ESI to ETI.⁶²¹ She stated that ETI has not shown that ratepayers benefit from the expenses, the costs are not necessary to provide utility service, and that the ESI allocation method is unjustified.⁶²²

ETI disagrees with all of these criticisms and maintains that the costs of the plans should be recoverable. ETI witness Gardner testified that the supplemental executive retirement plans are needed for attracting, retaining, and motivating highly competent and qualified leaders. He explained that the Pension Equalization Plan provides supplemental retirement benefits to account for the fact that Internal Revenue Code regulations limit the level of retirement benefits that qualify for tax treatment favorable to ETI and Entergy. The existence of this supplemental benefit program allows the Company to pay retirement benefits to highly-compensated employees that are proportionate to the compensation they receive while active in their employment. The Supplemental Retirement Plan and the System Executive Retirement Plan provide supplemental benefits beyond the amounts restricted in the qualified plan to some participants to attract, retain, and motivate employees.⁶²³ According to Mr. Gardner, these types of retirement benefits are widely provided by companies within the utility business sector.⁶²⁴ Accordingly, ETI argues that it needs to offer them in order to be competitive in the employment market with peer companies, and thereby to retain and adequately compensate these employees in terms of future retirement benefits.

The ALJs conclude that the supplemental executive retirement plans are not reasonable and necessary for the provision of electric utility service and are not in the public interest. They are non-qualifying retirement plan available only to employees and executives earning more than \$245,000 per year, and they constitute benefits over and above the Company's standard retirement

⁶²⁰ Cities Ex. 2 (Garrett Direct) at 56-57.

⁶²¹ OPC Ex. 1 (Szerzen Direct) at 68. Dr. Szerzen quantifies the costs of the plans as \$1,391,861 (a much lower estimate than those of Ms. Givens and Mr. Garrett).

⁶²² *Id.* at 68-69.

⁶²³ ETI Ex. 50 (Gardner Rebuttal) at 15-16.

⁶²⁴ *Id.* at 16.

benefits package. Because these costs are not necessary for the provision of utility service, but are instead discretionary costs, they should be paid by the shareholders. Accordingly, the ALJs recommend an adjustment to remove \$2,114,931, representing the full costs associated with ETI's non-qualified executive retirement benefits.

5. Employee Relocation Costs

In the application, ETI included, as part of its labor costs, \$436,723 in employee relocation costs.⁶²⁵ ETI contends that, in order to be competitive in the employment market, it must provide relocation assistance to certain of its employees. ETI witness Gardner testified that ETI's relocation policies and costs are reasonable and consistent with general industry practice. He also testified that the Company's average relocation costs are in line with the relocation costs for the companies surveyed by the Employee Relocation Council.⁶²⁶

Staff recommends an adjustment to remove the entire \$436,723 of ETI's relocation expenses.⁶²⁷ No other party challenged the legitimacy of relocation expenses. Staff points out that ETI pays 110 percent of the market median for total annual compensation.⁶²⁸ Staff contends that the fact that ETI pays more than the average market wage demonstrates that employees should be sufficiently enticed to join and move around within its organization without the need for ETI to pay relocation expenses to attract employees. Therefore, Staff argues that the relocation expenses do not meet the reasonable and necessary standard required for inclusion in cost of service, nor are the expenses in the public interest.⁶²⁹ Staff also points out that similar types of payments were removed from cost of service in recent proceedings, such as in Docket No. 28906, where payments for moving expenses or signing bonuses were removed from cost of service.⁶³⁰

⁶²⁵ Staff Ex. 1 (Givens Direct) at 25.

⁶²⁶ ETI Ex. 36 (Gardner Direct) at 45-46.

⁶²⁷ Staff Initial Brief at 64; Staff Ex. 1 (Givens Direct) at 24.

⁶²⁸ Staff Ex. 1 (Givens Direct) at 24 (*citing* ETI Ex. 36 (Gardner Direct) at 26).

⁶²⁹ Staff Initial Brief at 64; Staff Ex. 1 (Givens Direct) at 24.

⁶³⁰ Staff Initial Brief at 64; Staff Ex. 1 (Givens Direct) at 24, *citing Application of LCRA Transmission Services Corporation to Change Rates*, Docket No. 28906, Final Order (Apr. 5, 2005).

ETI responds by pointing out that Staff does not challenge the reasonableness of the amount spent on relocations by ETI. It also contends that most of its peers offer moving assistance. Thus, it would be competitively disadvantaged if it did not offer it as well. ETI reiterates that its relocation costs are reasonable and necessary and should be authorized.⁶³¹

The ALJs conclude that ETI has the better argument. There is no allegation that ETI was too lavish in its relocation expenditures. The only complaint offered by Staff is that ETI's overall compensation costs are 110 percent of the market median. It does not necessarily follow that the relocation program is unnecessary. ETI provided substantial evidence that, without a relocation program, it would be at a competitive disadvantage with its peers. Accordingly, the ALJs reject Staff's request to disallow the Company's relocation expenses.

6. Executive Perquisites

In the application, ETI included, as part of its labor costs, \$40,620 in costs associated with its executive perquisites. Those perquisites consist of financial counseling and tax gross-ups for system officers and executives. Specifically, the financial counseling program promotes maximizing investment growth opportunities for eligible officers and executives, and allows reimbursement for certain expenses incurred for personal financial counseling services.⁶³² Staff recommends an adjustment to remove the full cost of the executive perquisites (\$40,620), reasoning that the costs are not reasonable and necessary for the provision of electric utility service.⁶³³ ETI does not oppose that adjustment.⁶³⁴ The ALJs agree that the adjustment is warranted. Therefore, the ALJs recommend an adjustment to remove \$40,620, representing the full cost of ETI's executive perquisite costs.

⁶³¹ ETI Initial Brief at 143.

⁶³² Staff Ex. 1 (Givens Direct) at 23.

⁶³³ Staff Initial Brief at 65; Staff Ex. 1 (Givens Direct) at 23.

⁶³⁴ ETI Initial Brief at 144.

E. Interest on Customer Deposits

Staff witness Givens adjusted ETI's requested interest expense of \$68,985 by removing \$(25,938) from FERC account 431.⁶³⁵ This decrease is a result of applying the interest rate of 0.12 percent for calendar year 2012 on deposits held by utilities.⁶³⁶ Using the active customer deposits amount of \$35,872,476 and the 2012 interest rate, Ms. Givens calculated a recommended interest expense of \$43,047 (\$35,872,476 multiplied by .12 percent).⁶³⁷

This change, which reflects Commission-approved interest rates for 2012 as set in December 2011, complies with Project No. 39008 and ETI agreed with this amount. Accordingly, the ALJs recommend that the Commission approve this amount.

F. Property (Ad Valorem) Tax Expense

During the Test Year, ETI's property tax expense equaled \$23,708,829.⁶³⁸ Patricia Galbraith, ETI's Tax Officer, testified that a *pro forma* adjustment should be made to this level of expense for a known and measurable change that reflects the level of property tax expense ETI will experience in the Rate Year. Specifically, her proposed adjustment would increase the Test Year level of expense by \$2,592,420 to \$26,301,249.⁶³⁹ As Ms. Galbraith testified, ETI's property tax expense for the calendar year 2012 will be paid in January of 2013 and be based on 2011 calendar year-end values for both net operating income and net plant amounts.⁶⁴⁰ Her proposed adjustment is based on an expected ad valorem rate increase of 1 percent and expected increases in both net plant values and ETI net operating income that will equal 9.81 percent.⁶⁴¹

⁶³⁵ Staff Ex. 1 (Givens Direct) at 24.

⁶³⁶ *Setting Interest Rates for Calendar Year 2012*, Project No. 39008, Order (Dec. 8, 2011).

⁶³⁷ Staff Ex. 1 (Givens Direct) at 24-25.

⁶³⁸ ETI Ex. 26 (Galbraith Direct) at 5; ETI Ex. 3 at Sched. G-9.

⁶³⁹ ETI Ex. 26 (Galbraith Direct) at 5 and PAG-1; ETI Ex. 3 at Sched. G-9.

⁶⁴⁰ Tr. at 1235.

⁶⁴¹ ETI Ex. 26 (Galbraith Direct) at PAG-1.

TIEC, Cities, and Staff oppose the property tax adjustment proposed by ETI. TIEC argues that ETI's proposed adjustment should be rejected entirely, on the grounds that it is not a known and measurable change from ETI's Test Year property tax costs. Ms. Galbraith admitted that she does not know, with certainty, what the relevant property tax rate will be in 2012, nor has ETI received any tax bills advising that tax rates will rise.⁶⁴² Thus, TIEC witness Pollock testified that ETI's proposed adjustment is not known and measurable and recommended that the Commission reject the adjustment and include only the Test Year level of expense in cost of service.⁶⁴³ TIEC further points out that the Commission has twice rejected requests to include projected property tax expense in rates.⁶⁴⁴ For example, in Docket No. 28813, Cap Rock prepared an independent analysis indicating that property taxes were expected to increase to \$2,700,000 per year from its test year tax level of approximately \$900,000 per year. The analysis used an estimated tax assessment of \$110,000 with an estimated tax rate of \$2.47 per \$100 of value. The ALJs in that case concluded that the property tax increases were estimates at the time of the hearing, and thus they were not known and measurable and should not be allowed.⁶⁴⁵ Subsequently, the Commission adopted the ALJs' finding.⁶⁴⁶ The Commission rejected a similar request from ETI's predecessor Gulf States Utilities (GSU).⁶⁴⁷ In consolidated Docket No. 8702, the Commission rejected GSU's request for projected 1989 property taxes and instead only allowed the actual calendar year property tax expenses.⁶⁴⁸ In both cases the Commission found that projected tax expense is not a known and measurable

⁶⁴² Tr. at 1221, 1238.

⁶⁴³ TIEC Ex. 1 (Pollock Direct) at 40–41.

⁶⁴⁴ *In re Cap Rock Corp., Petition of PUC (Staff) to Inquire into the Reasonableness of the Rates and Services of Cap Rock Energy Corporation*, Docket No. 28813, Order on Rehearing at FoF 137 (Nov. 9, 2005) (“Cap Rock failed to prove any increase in property taxes above those in the test year-\$899,597-was known and measurable.”); *Application of Gulf States Utilities Company for Authority to Change Rates, Application of Sam Rayburn G&T Electric Coop., Inc. for Sale Transfer or Merger, Appeal of Gulf States Utilities Company from Rate Proceedings of Various Municipalities*, Docket Nos. 8702, 8922, 8939, 8940, 8946, 8233, 8944, 8945, 8947, 8948 and 8949, Order at FoF 111 (May 2, 1991) (“The 1988 calendar year level of actual property taxes paid should be used in determining rate year taxes because it is a known and measurable change.”).

⁶⁴⁵ Docket No. 28813, PFD at 99 (Mar. 17, 2005).

⁶⁴⁶ Docket No. 28813, Order on Rehearing at FoF 137 (Nov. 9, 2005).

⁶⁴⁷ Docket No. 8702, Order at FoF 111 (May 2, 1991).

⁶⁴⁸ Docket No. 8702, Order at 52.

change.⁶⁴⁹ Accordingly, TIEC contends that ETI's request for a forecasted tax expense increase should be rejected.⁶⁵⁰

Staff concedes that some level of increase is warranted but argues that the increase should be smaller than ETI is asking for. Rather than an increase of \$2,592,420, Staff contends that ETI's Test Year property tax expenses should be adjusted upward by only \$1,214,688.⁶⁵¹ Staff witness Givens arrived at this increase by applying the effective tax rate for the calendar year 2011 to the Staff's Test Year end plant in service recommendation. She testified that both of these inputs to her calculation are known and measurable and thus may be used to determine the increase.⁶⁵²

Cities also concede that some level of increase is warranted, but argue that the increase should be smaller than ETI is asking for, and smaller than Staff proposes. Cities contend that ETI's Test Year property tax expenses should be adjusted upward by only 1,134,442.⁶⁵³ Cities witness Garrett offered the opinion that ETI's proposed adjustment was based on estimates that were unreasonably high when compared to the actual tax valuation increases experienced since 2008. Mr. Garrett arrived at his projected increase in tax expense by applying the average annual valuation increase experienced over the period of 2009-11 to net plant value for 2011. Cities argue that both of these inputs to the calculation are known and measurable and thus may be used to determine the increase.⁶⁵⁴

ETI responds to its opponents by pointing out that the Commission has, in the past, recognized that the adjustment proposed by Staff, which was obtained by applying a historical effective tax rate to the level of test year end plant in service, is known, measurable, and

⁶⁴⁹ Docket No. 28813, Order on Rehearing at FoF 137 (Nov. 9, 2005); Docket No. 8702, Order at 52, FoF 111 (May 2, 1991).

⁶⁵⁰ TIEC Initial Brief at 54-56.

⁶⁵¹ Staff Ex. 1 (Givens Direct) at 25.

⁶⁵² *Id.* at 25-26.

⁶⁵³ Cities Ex. 2 (Garrett Direct) at 61.

⁶⁵⁴ *Id.*

appropriate.⁶⁵⁵ ETI also notes that, although it had not done so at the time Ms. Galbraith filed her testimony, ETI has since filed its 2011 year end FERC Form 1 data and now knows both the final net income amounts and net plant values for year end 2011 that will be used to determine the Company's 2012 tax expense (that will be paid in January of 2013).⁶⁵⁶ ETI contends that those known values are substantially larger than the estimates used by Ms. Galbraith when she calculated the proposed adjustment, such that the known increases in 2011 net operating income and net plant amounts over 2010 are so large that, even without the 1 percent increase in tax rate assumed in the property tax adjustment, Rate Year property tax expenses will be larger than the \$26,301,249 amount requested by the Company.⁶⁵⁷

The issue with regard to property taxes is whether a level of increase is known and measurable. The ALJs conclude that the approach taken by Staff does the best job of generating a known and measurable value for ETI's property tax burden in the Rate Year. As explained above, Staff's approach is supported by prior Commission precedent. Moreover, unlike the approaches advocated by ETI and Cities, Staff's approach requires no guesswork about future tax rates. Accordingly, the ALJs recommend that ETI's property tax burden should be adjusted upward by applying the effective tax rate for the calendar year 2011 to the final, adopted Test Year-end plant in service value for ETI.

G. Advertising, Dues, and Contributions

In the application, ETI included, as part of its operating expenses, \$2,046,214 in costs associated with advertising, dues, and contributions.⁶⁵⁸ Staff recommended an adjustment to remove \$12,800, representing contributions to organizations primarily focused on influencing legislative

⁶⁵⁵ ETI Initial Brief at 145; see also, *Application of AEP Texas Central Company for Authority to Change Rates*, Docket No. 28840, Final Order at FOF 189-191 (Aug. 15, 2005); *Petition of General Counsel to Inquire Into the Reasonableness of the Rates and Services of Central Telephone Company of Texas*, Docket No. 9981, 19 Tex. P.U.C. BULL. 936, 1080-82, 1217 (Sept. 8, 1993); *Application of Central Power and Light Company for Rate Changes and Inquiry Into the Company's Prudence with Respect to South Texas Project Unit 2*, Docket No. 9561, 17 Tex. P.U.C. BULL. 157, 231-232 (Dec. 19, 1990).

⁶⁵⁶ Tr. at 1236-37.

⁶⁵⁷ ETI Initial Brief at 146-47.

⁶⁵⁸ ETI Ex. 3, Sched. G-4.

activities. Staff reasons that these costs are not reasonable and necessary for the provision of electric utility service.⁶⁵⁹ ETI makes no response to the suggested adjustment.⁶⁶⁰ The ALJs agree that the adjustment is warranted. Therefore, the ALJs recommend an adjustment to remove \$12,800 from ETI's costs of advertising, dues and contributions.

H. Other Revenue-Related Adjustments

Several items within the Company's revenue requirement are interrelated. This means that changes to one area or item will impact one or more additional items, such as the Texas state gross receipts tax, the PUC Assessment tax, and Uncollectible Expenses.⁶⁶¹ From the discussions in briefs, it does not appear that there are any substantive differences among the parties regarding these amounts, which will ultimately be determined during number running.

I. Federal Income Tax

As explained by ETI witness Rory Roberts, the Company calculated its income tax expense in the cost of service by taking into account only the revenues and expenses included in the cost of service.⁶⁶² To the extent the Commission makes changes to the revenues and expenses that are ultimately included in the cost of service, the income tax expense amount included in the cost of service will change accordingly. This represents a proper matching of income tax effects to the expenses and revenues that produced those tax effects.⁶⁶³

Mr. Roberts contended that the Commission's past practice of reducing tax expense for a consolidated tax adjustment based on some measure of the tax "savings" the utility realized by joining in a consolidated group federal income tax return was inappropriate. He testified that it is improper to reduce tax expense for deductions or losses that are not also included in the cost of service. In the case of the Commission's consolidated tax adjustment, tax expense is reduced to the

⁶⁵⁹ Staff Initial Brief at 66; Staff Ex. 1 (Givens Direct) at 26.

⁶⁶⁰ ETI Initial Brief at 147.

⁶⁶¹ Staff Ex. 1 (Givens Direct) at 28-29.

⁶⁶² ETI Ex. 21 (Roberts Direct) at 10; Ex. 3 Sched. G-7.

⁶⁶³ ETI Ex. 21 (Roberts Direct) at 10.

extent that utility income is used to offset non-utility affiliate losses, even though those losses are not included in cost of service or borne in any manner by the utility's customers.⁶⁶⁴

Despite his disagreement with the approach, Mr. Roberts performed a calculation of the adjustment using the interest credit methodology adopted by the Commission. He concluded that, instead of positive taxable income, ETI had net tax losses over the 15-year calculation period and thus provided no taxable income that could be used to offset affiliate losses.⁶⁶⁵ In fact, over the 15-year period, ETI's tax losses were offset by taxable income produced by other affiliates. Thus, ETI contends that, were the Commission to be consistent in applying its interest credit methodology, it should increase ETI tax expense included in cost of service due to the fact that its affiliates' taxable income had to be used to offset ETI's tax losses. Nevertheless, in its application, ETI rejected the interest credit methodology and has not requested that ETI's tax expense be increased as a result of the consolidated tax adjustment calculation. No other party to the proceeding challenged the Company's position on federal income tax expense in testimony or at the hearing. The ALJs find no reason to do so either.

J. River Bend Decommissioning Expense

ETI has an ownership interest in River Bend. In the application, ETI requested that \$2,019,000 be included in its cost of service to account for the Company's annual decommissioning expenses associated with River Bend.⁶⁶⁶ This is the same amount that was requested and approved on December 13, 2010, in Docket No. 37744.⁶⁶⁷ The amount of \$2,019,000 was derived from an ETI decommissioning study that was completed in 2009. In this case, ETI chose not to propose any change to its 2009 estimate. ETI contends that this decision is supported by an August 9, 2011, letter from the Nuclear Regulatory Commission.⁶⁶⁸

⁶⁶⁴ *Id.* at 10-11.

⁶⁶⁵ *Id.* at 10, and RLR-5.

⁶⁶⁶ ETI Ex. 3 Schedules. M-1 and M-2; ETI Ex. 8 (Considine Direct) at 57-58.

⁶⁶⁷ ETI Ex. 8 (Considine Direct) at 58.

⁶⁶⁸ *Id.* at 58 and MPC-2.

Cities argue that the decommissioning expense should be reduced to \$1,126,000.⁶⁶⁹ Cities point out that the larger amount sought by ETI was merely the amount agreed to by the parties, as opposed to being substantively considered and approved by the Commission in Docket No. 37744.⁶⁷⁰ In the current case, ETI was asked through discovery to provide an updated estimate of the annual decommissioning expense responsibility for Texas retail customers calculated using the most current Texas jurisdictional decommissioning fund balance. ETI responded that the current annual decommissioning revenue requirement is \$1,126,000.⁶⁷¹

Under P.U.C. SUBST. R. 25.231(b)(1)(F)(i), the annual cost of decommissioning for ratemaking purposes must “be determined in *each* rate case based on . . . *the most current information reasonably available* regarding the cost of decommissioning, the balance of funds in the decommissioning trust, anticipated escalation rates, the anticipated return on the funds in the decommissioning trust, and other relevant factors.” The cost determined must then be expressly included in the cost of service established by the Commission’s order.

The parties agree that \$1,126,000 is the best estimate of the current annual revenue requirement to meet ETI’s estimated decommissioning cost. However, ETI relies on P.U.C. SUBST. R. 25.231(b)(1)(F)(iv) and Staff witness Cutter’s testimony to contend that it need not adjust the current amount being charged.⁶⁷² Pursuant to subpart (iv), ETI is required to periodically study its decommissioning costs, and such a study must be done “at least every five years.” Because its last study was done in 2009, ETI contends that it need not do a new study now, but may simply rely of the outcome of its last study, which showed that its annual revenue requirement is \$2,019,000.⁶⁷³

Cities agree that ETI is not required to conduct a new decommissioning study at this time. However, the most current information reasonably available clearly shows that the annual amount

⁶⁶⁹ Cities Ex. 2 (Garrett Direct) at 64-65.

⁶⁷⁰ *Application of Entergy Texas, Inc. for Authority to Change Rates and Reconcile Fuel Costs*, Final Order at FoF 32 (Dec. 13, 2010); Cities Initial Brief at 73.

⁶⁷¹ Tr. at 348-49.

⁶⁷² ETI Ex. 46 (Considine Rebuttal) at 38-39.

⁶⁷³ *Id.*

required to meet the total cost determined in the Company's last decommissioning study has decreased. Cities argue that to ignore the most current information available disposal would unreasonably shift future costs to current customers and would be a violation of P.U.C. SUBST. R. 25.231(b)(1)(F)(i). The ALJs agree. ETI's annual decommissioning revenue requirement should reflect the most current calculation of \$1,126,000. Therefore, an adjustment of \$893,000 to the *pro forma* cost of service is needed to reflect the difference between the requested level for decommissioning costs of \$2,019,000 and recommended level of \$1,126,000.

K. Self-Insurance Storm Reserve Expense [Germane to Preliminary Order Issue No. 5]

In prior dockets, the Commission authorized ETI to recover \$3,650,000 annually for storm damage expenses and to maintain a reasonable and necessary storm damage reserve account of \$15,572,000.⁶⁷⁴ ETI requests to increase the authorized storm damage reserve account to \$17,595,000 (an increase of \$2,023,000) and to increase the annual accrual to \$8,760,000 (an increase of \$5,110,000). ETI's proposed annual accrual is composed of two elements: (1) an annual accrual of \$4,890,000 to provide for average annual expected losses from all storms that do not exceed \$100 million; and (2) a 20-year annual accrual of \$3,870,000 to bring the reserve up from its current deficit of \$59,799,744 to ETI's target reserve of \$17,595,000.

No party disputes that ETI's proposal to self-insure for catastrophic property loss is appropriate under PURA § 36.064 and P.U.C. SUBST. R. 25.231(b)(1)(G). However, Cities, OPC, and Staff oppose the amount of ETI's proposed annual accrual, and Cities and OPC also oppose ETI's proposed target reserve. The parties' recommendations are:

	Annual Accrual	Target Reserve
Current	\$3,650,000	\$15,572,000
ETI	\$8,760,000	\$17,595,000
Cities	\$6,150,339	\$15,572,000
OPC-1	\$2,335,047	\$15,572,000
OPC-2	\$3,650,000	\$15,572,000
Staff	\$8,270,000	\$17,595,000

⁶⁷⁴ Staff Ex. 4 (Roelse Direct) at 8.

The first component of ETI's requested annual accrual is \$4,890,000 for expected annual losses. ETI explains that this is the amount of annual losses projected to be incurred by ETI from all storm damage, except those over \$100 million (the minimum amount likely to be securitized),⁶⁷⁵ adjusted to reflect current conditions and current cost levels.⁶⁷⁶ This recommended accrual was calculated by ETI witness Gregory Wilson using a Monte Carlo simulation of ETI's loss history.⁶⁷⁷ A statistical distribution was estimated from ETI's trended loss experience, and the model indicated an average annual loss of \$4,890,000. Mr. Wilson excluded losses from Hurricanes Rita, Gustav, and Ike from the model because those losses were securitized and not recovered through the insurance reserve.⁶⁷⁸ ETI adds that results from the model simulation were also adjusted by removing any simulated year in which the total storm loss exceeded \$100 million, which would likely be securitized.

The second component of the proposed annual accrual is \$3,870,000 per year for 20 years to restore the reserve from the current deficit of \$59,799,744 up to the \$17,595,000 requested target level. In ETI's opinion, a 20-year period balances the interests of future and past ratepayers. It added that Mr. Wilson's calculations were prepared in accordance with generally accepted actuarial procedures, with certain adjustments to reflect the nature of ratemaking for public utilities.⁶⁷⁹

ETI also requests a target reserve of \$17,595,000. It argues that this would be an actuarially sound provision to cover self-insured losses. ETI noted that the target reserve was also developed by Mr. Wilson through the Monte Carlo simulation based upon the ETI's loss history.⁶⁸⁰

Cities recommend maintaining the current target reserve of \$15,572,000 and adopting an annual storm damage accrual of \$6,150,399. Cities' proposed annual accrual is comprised of two

⁶⁷⁵ ETI Ex. 19 (McNeal Direct) at 32.

⁶⁷⁶ ETI Ex. 14 (Wilson Direct) at 5.

⁶⁷⁷ *Id.* at Ex. GSW-3.

⁶⁷⁸ *Id.* at 9.

⁶⁷⁹ ETI Ex. 14 (Wilson Direct) at 11-12.

⁶⁸⁰ *Id.* at 9.

parts: (1) keeping the current accrual of \$3,650,000 for projected annual storm expense; and (2) adding \$2,500,399 annually to bring ETI's reserve deficit amount, as adjusted by Cities, up to a target reserve of \$15,572,000. Cities' witness Jacob Pous testified that the current target reserve of \$15,572,000 should be maintained given ETI's plan to divest itself of the transmission system, which would reduce storm damage expenses.⁶⁸¹ For the same reason, Mr. Pous also stated that the Commission should maintain the current annual accrual amount that was approved most recently in Docket No. 37744.⁶⁸²

According to Cities, ETI witness Wilson acknowledged that his calculations assumed that the current transmission system would be owned by ETI, and if the transmission system were sold, his analysis would need to be adjusted.⁶⁸³ Cities also note that Mr. Wilson included ETI's 1997 ice storm expenses within the historical storm data used for his calculations.⁶⁸⁴ As discussed in Section V.F., Cities challenge these expenses. If the Commission determines that those costs should be excluded, Mr. Wilson agreed that it would be inappropriate to include them in his analysis.⁶⁸⁵ In addition, Cities stated, Mr. Wilson's Monte Carlo model analysis has been rejected in several cases by the Commission, as noted by Staff witness Chris Roelse.⁶⁸⁶ Cities noted that Mr. Wilson limited the storm reserve expense in his model to \$100 million, as anything over that amount might be securitized.⁶⁸⁷ But, Cities contend, Mr. Wilson did not consider that the storm loss history provided to him by ETI included only storm damage *expenses* and not *capital costs*, which are also included when determining the amount capable of being securitized. Thus, in Cities opinion, Mr. Wilson's cap of \$100 million was overstated, and for all these reasons Cities argues that Mr. Wilson's analysis should not be considered reliable.

⁶⁸¹ Cities Ex. 5 (Pous Direct) at 65-66.

⁶⁸² *Id.* at 66; *see also* Docket No. 37744, Final Order at FoF 31 (Dec. 13, 2010).

⁶⁸³ Tr. at 1247.

⁶⁸⁴ Tr. at 1244-1246.

⁶⁸⁵ Tr. at 1246-1247.

⁶⁸⁶ Staff Ex. 4 (Roelse Direct) at 12.

⁶⁸⁷ ETI Ex. 14 (Wilson Direct) at 9.

Finally, Cities note that ETI requested that the annual storm reserve accrual “would be made . . . only until it reaches the recommended target level, at which point contributions to the reserve would reduce to the lower of annual expected losses or actual losses.”⁶⁸⁸ In Cities view, this request should be rejected and the accrual should only be modified through a future rate case.

OPC also recommends adjustments to the storm damage reserve and the annual accrual. As discussed in Section V.F., OPC argues that ETI failed to prove that its storm damage expenses booked since 1996 were reasonable and prudently incurred. Consequently, OPC recommends disallowing all of those charges. Removing those charges would leave ETI with a positive storm reserve balance of \$41,871,059, which exceeds the currently approved storm reserve balance of \$15,572,000 by \$26,299,059. OPC witness Benedict proposed that this surplus be refunded to rate payers at a rate of \$1,314,953 per year for 20 years. He also recommended that current annual storm damage accrual of \$3,650,000 be maintained, less his proposed customer refund of \$1,134,953 per year, leaving a net annual storm damage accrual of \$2,335,047 per year. Mr. Benedict acknowledged that some storm damage expenses incurred by ETI since 1996 likely were reasonable and necessary. Therefore, as an alternative proposal, Mr. Benedict suggested that ETI’s current storm balance reserve be set at the last approved amount of \$15,572,000 (*i.e.*, without any surplus or deficit) and that the currently approved total annual accrual of \$3,650,000 be maintained. In addition, OPC argues that Mr. Wilson’s Monte Carlo model analysis was flawed because it included expenses that ETI did not establish were reasonable and prudently incurred.⁶⁸⁹

Staff witness Chris Roelse agreed that ETI’s proposed target reserve of \$17,595,000 is reasonable. However, he recommended an annual accrual of \$8,270,000, which is \$490,000 less than ETI’s request. Mr. Roelse pointed out that ETI’s witness calculated the proposed annual accrual based on a Monte Carlo simulation, which projects a loss experience over a longer time than the period captured in the available loss history. However, Mr. Roelse stated, the Commission has not approved the use of these models in prior dockets; instead, it has relied on averaging known insurance losses over a period of time to compute the annual accrual. Using historical loss data,

⁶⁸⁸ ETI Initial Brief at 151.

⁶⁸⁹ OPC Ex. 6 (Benedict Direct) at 6-16; OPC Initial Brief at 14-20; OPC Reply Brief at 13-15.

Mr. Roelse calculated an annual expected storm loss of approximately \$4,400,000. When this amount is added to the proposed annual accrual of \$3,870,000 to restore the reserve balance from its current deficit, it produces a total annual accrual of \$8,270,000, which Staff recommends.⁶⁹⁰

In response, ETI agreed that if portions of the underlying costs upon which the Monte Carlo analysis was performed are removed from the reserve, then the outcome of Mr. Wilson's analysis would be different. However, ETI stressed that questions about the underlying expenses are not an attack on the Monte Carlo analysis itself. Rather, Mr. Wilson provided an analysis based upon information supplied by ETI, and he did not claim to support the expenses themselves. But ETI disagreed with the challenges to the underlying costs, as discussed in Section V.F.⁶⁹¹

Most of Cities' and OPC's objections to ETI's requested storm damage annual accrual and target reserve relate to their objections to the underlying expenses, as discussed in Section V.F. For the reasons stated in that section, the ALJs denied those objections, and they do not support rejecting ETI's request for the annual accrual or target reserve. Likewise, the ALJs find that Cities' concerns about ETI selling its transmission system are too uncertain to justify altering the storm damage reserve at this time.

Cities also raised a question about whether Mr. Wilson properly calculated the cap he used to exclude from his analysis storms that would likely result in securitized costs. Staff pointed out that the Commission has not approved the use of the Monte Carlo simulation model in prior dockets. Rather, the Commission has traditionally used known insurance losses over a period of time. The ALJs note that neither PURA nor the Commission's rules either require or prohibit the use of actuarial models, such as the Monte Carlo simulation. The prior dockets cited by Staff did not adopt the recommendations developed by actuarial models, but the Commission also did not expressly reject the models in those cases. Likewise, however, ETI has not cited any Commission decisions that expressly adopted or used such models.

⁶⁹⁰ Staff Ex. 4 (Roelse Direct) at 10-15; Staff Initial Brief at 13-14.

⁶⁹¹ ETI Reply Brief at 81.

Staff witness Chris Roelse explained that the Commission has traditionally averaged known insurance losses over a period of time to compute the annual accrual. He made such a calculation that produced an annual accrual for storm damage loss of \$4,400,000. When added to the proposed annual accrual of \$3,870,000 to restore the reserve balance from its current deficit, the total annual accrual equals \$8,270,000. No party challenged that calculation. Because a question remains as to whether Mr. Wilson properly calculated his cap to exclude storm damage expenses that would likely be securitized, the ALJs find it is more reasonable to adopt the annual accrual proposed by Staff. Therefore, the ALJs recommend that the Commission approve a total annual accrual of \$8,270,000, comprised of an annual accrual of \$4,400,000 to provide for average annual expected storm losses, plus an annual accrual of \$3,870,000 for 20 years to restore the reserve from its current deficit. The ALJs also recommend approval of ETI's proposed target reserve of \$17,595,000. Finally, the ALJs recommend that the Commission require ETI to continue recording its annual accrual until modified by an order in a future rate case, as requested by Cities. Otherwise, ETI could continue to receive rates based on the total accrual amount, but not record the receipts in the storm damage reserve. The ALJs find that such circumstances would not result in just and reasonable rates.

L. Spindletop Gas Storage Facility

Cities challenged ETI's use of the Spindletop Facility, arguing that the costs of operating it outweigh the benefits gained from it. In Section V.H., the ALJs rejected Cities' contention that a substantial portion of ETI's annual costs to operate the Spindletop Facility should be removed from ETI's rate base. For the same reason he challenged the Spindletop Facility costs associated with rate base, Cities witness Nalepa also challenges a portion of ETI's costs derived from the Spindletop Facility that are associated with operating expenses. Specifically, Mr. Nalepa and Cities argue that \$2,090,116 (consisting of \$309,751 in depreciation expense and \$1,780,365 associated with the Spindletop Facility) ought to be removed from ETI's operating expenses.⁶⁹² For the same reason that they rejected Cities' Spindletop Facility arguments relevant to rate base, the ALJs also reject Cities' Spindletop Facility arguments relevant to operating expenses.

⁶⁹² Cities Ex. 6 (Nalepa Direct) at 19; Cities Initial Brief at 76.

VIII. AFFILIATE TRANSACTIONS [Germane to Preliminary Order Issue No. 3]

PURA requires that more stringent standards be applied to affiliate expenses than are applied to other utility company expenses. Section 36.058 begins by stating “except as provided by Subsection (b),” the PUC may not allow as capital cost or as expense a payment to an affiliate for the cost of a service, property, right, or other item or interest expense. Subsection 36.058(b) provides that the Commission may allow an affiliate payment “only to the extent” that the PUC finds the payment is reasonable and necessary for each item or class of item as determined by the Commission.

The seminal case interpreting PURA’s affiliate transaction standard under Section 36.058 is *Railroad Commission v. Rio Grande Valley Gas Company*.⁶⁹³ In that case, the court recognized that PURA’s affiliate transaction statute created a presumption that a payment to an affiliate is unreasonable. The court explained:

Rio’s entire approach has been that the Commission is required to allow the residual affiliate charges unless they are shown to be imprudent, unreasonable, or out of line. Although this may be true with respect to arms length transactions, it is not true with respect to affiliates about which the Legislature has its suspicion and which to any reasonable mind are clearly tainted with the possibility of self-dealing.

The court went on to state that the burden was upon Rio to show that its affiliate charges were just and reasonable. The court interpreted the PURA affiliate transaction statute and explained four major areas in which Rio had failed to meet its burden of proof:

- Plaintiff had the burden of showing that the prices it was charged by its affiliate were no higher than the prices charged by the supplying affiliate to its other affiliates. . . .
- Plaintiff had the burden of showing that expenses which may not be allowed for rate making purposes for any reason . . . were not included in the “allocated expenses.” . . .
- Plaintiff had the burden of proving that each item of allocated expense was reasonable and necessary. . . .

⁶⁹³ 683 S.W. 2d 783 (Tex. App.—Austin 1985, no writ).

- Plaintiff had the burden of proving that the allocated amounts reasonably approximated the actual cost of services to it. . . .

In 2000, the Third Court of Appeals once again spoke on the issue of affiliate transactions in the utility setting. In *Central Power and Light Company/Cities of Alice v. Public Utility Commission*, the court cited to *Rio Grande Valley Gas Company* and stated:

Because of the possibility for self-dealing between affiliated companies, however, expenses paid to an affiliated entity are presumptively not included in the rate base. A utility can overcome this presumption against affiliate expenses only if it demonstrates that its payments are ‘reasonable and necessary for each item or class of items as determined by the commission.’⁶⁹⁴

PURA Section 36.058 places a greater burden of proof on the utility to prove the reasonableness and necessity of its affiliate transactions because of the nature of the relationship between the utility and its affiliates. These transactions are not considered to be arms-length, and there is a potential for self-dealing. The transactions must be disallowed for regulatory purposes, unless the utility presents sufficient evidence that it has met each of the affiliate transaction statutory requirements. If the regulatory tests for affiliate transactions are not properly enforced, the regulated utility may become a vehicle for cross-subsidization by ratepayers of other regulated or unregulated affiliates.

OPC witness Szerszen was the only witness to challenge ETI’s affiliate transactions,⁶⁹⁵ recommending a total affiliate disallowance (after erratas) of \$8,945,221.⁶⁹⁶ Dr. Szerszen reviewed a select subset of ETI’s affiliate expenses using the PURA affiliate transaction standards. She reviewed the Company’s affiliate transactions on a project by project basis, noting that such a review was more efficient and easier to understand.⁶⁹⁷ Dr. Szerszen testified that a review by the

⁶⁹⁴ 36 S.W.3d 547 at 564 (Tex. App.—Austin 2000, pet. denied) (citations omitted).

⁶⁹⁵ Cities witness Mark Garrett recommended disallowance of certain short-term incentive compensation affiliate costs, but those disallowances are largely also recommended by Dr. Szerszen. See ETI Ex. 69 (Tumminello Rebuttal) at 17. ETI contends that the duplicated disallowances by Dr. Szerszen and Mr. Garrett would result in double counting \$217,520 of the requested affiliate charges and requests that if the ALJs rule in OPC’s and Cities’ favor regarding these short-term incentive compensation costs, that disallowance should be reduced by \$217,520. ETI Initial Brief at 157, n. 898.

⁶⁹⁶ Tr. at 1607.

⁶⁹⁷ OPC Exhibit No. 1 (Szerszen Direct) at 42-43.

Company's 25 classes of service presents a far too macro view of affiliate transactions that does not allow an adequate review of ETI's affiliate transactions according to PURA mandates and takes the focus away from the important issues.⁶⁹⁸

OPC notes that PURA Subsection 36.058(f) requires that if the Commission finds an affiliate expense for the test period to be unreasonable, then the Commission is to make a determination of what level of the expense is reasonable. By analyzing ETI's affiliate transactions on a project basis, OPC contends that it has facilitated the Commission's ability to make such a determination for each of ETI's classes of service; instead of an "up or down" decision on the macro level of expense for the class, the Commission can disallow the portion not shown to be reasonable and approve the remainder as reasonable.

ETI disagrees with OPC's contentions and argues that Dr. Szerszen's approach to addressing the Company's affiliate case is inappropriate for a number of reasons and should be rejected.

- First, her approach is directly contrary to the Commission's Guiding Principles included as part of the Commission's Transmission and Distribution Cost of Service Rate Filing Package that was issued on April 2, 2003.⁶⁹⁹ Item 2 of the Guiding Principles clearly states that a class of service approach is required for purposes of complying with the provisions of Section 36.058 of PURA.⁷⁰⁰ Dr. Szerszen ignores the class of service approach required by Section 36.058 of PURA as detailed in the Guiding Principles, and instead states OPC's case on a project code-by-project code basis.
- Second, Dr. Szerszen's approach is directly contrary to the Commission's directives in Docket No. 16705. In that docket, the Commission disallowed a substantial amount of affiliate expense because Entergy Gulf States, Inc. had done then what Dr. Szerszen proposes here – based the affiliate analysis solely on project codes, rather than affiliate classes of service. Because the Commission found that a scope statement/project code-based affiliate analysis is "impossible," the Company, in its subsequent base rate cases, including its filing in this docket, changed to a class-based presentation, as directed by the Commission.

⁶⁹⁸ OPC Exhibit No. 1 (Szerszen Direct) at 42-43; Tr., at 1671-72.

⁶⁹⁹ See ETI Ex. 69 (Tumminello Rebuttal) at Ex. SBT-R-1.

⁷⁰⁰ Dr. Szerszen conceded that the Guiding Principles require that a utility's affiliate case be presented in a sufficient number of class or other logical groupings. Tr. at 1632.

- Third, by refusing to consider a class-based analysis, Dr. Szerszen has ignored the Company's testimony, presented by 19 affiliate witnesses, which explains in detail why the Company's affiliate-incurred costs meet the Section 36.058 of PURA and *Rio Grande* standards.⁷⁰¹ According to ETI, the Company's affiliate class witnesses, who are knowledgeable about the activities that are encompassed in each of their classes, have each shown why the services provided through those classes are necessary. They have each also addressed numerous Commission-recommended metrics to measure the reasonableness of costs, including cost trends, staffing trends, the budgeting process, and, if applicable, benchmarking and outsourcing comparisons.⁷⁰² Their testimony and exhibits, according to ETI, show numerous different "views" of the costs in their classes, including the project codes that comprise their classes. Each affiliate witness also addressed the "not higher than" and "reasonably approximates cost" standards applicable to affiliate costs. ETI contends that the evidence provided by its witnesses meets the requirements of these Guiding Principles and supports the Company's burden of proof for the recovery of affiliate costs. ETI also contends that Dr. Szerszen ignores this overwhelming evidence and the careful attention paid to presenting it in an organized manner. In addition, she presents no evidence in accordance with the Guiding Principles that supports her proposed disallowances.
- Fourth, the Company's case is much less cumbersome and less complex than the approach suggested by OPC, which would require a showing on the necessity, reasonableness, "not higher than," and "reasonably approximates cost" standards for *each* of almost 1,300 project codes subject to this docket. Even if the Company were to do that, Dr. Szerszen's "cherry picking" approach among the project codes ignores any savings in other project codes that would comprise a class of affiliate costs, thereby resulting in an overall reasonable level of costs within the class even assuming that any of her complaints about individual project codes had merit.
- Fifth, ETI contends that Dr. Szerszen fails to mention Section 36.058(f) of PURA, which requires that the Commission determine the reasonable level of "an affiliate expense" if it first finds that the expense presented is unreasonable. But rather than offering an alternative "reasonable" level of an expense, she either categorically disallows all costs in that project; or, in some instances, substitutes an arbitrary sharing or allocation of costs between ETI and its regulated affiliates, or ETI and its non-regulated affiliates. In doing so, Dr. Szerszen does not make any evidence-based attempt to ground her alternative allocation (and associated disallowance of ETI affiliate costs) on any objective basis reflecting cost causation principles. ETI contends that the effect of her approach is to presume that the Company needs zero dollars in its cost of service to perform a variety of essential utility support activities.

⁷⁰¹ Dr. Szerszen claimed that, instead of considering the narrative class testimony, she instead "looked at more of the detail," presumably meaning the exhibits. Tr. at 1629.

⁷⁰² ETI Ex. 69 (Tumminello Rebuttal) at Ex. SBT-R-1. Dr. Szerszen conceded that the Company's testimony included proof items such as benchmarking data, outsourcing, staffing trends, and cost trends. Tr. at 1631.

- Sixth, Dr. Szerszen's positions in the 2009 Oncor rate case,⁷⁰³ which she agrees are similar to her positions in this ETI base rate case,⁷⁰⁴ were rejected by the two SOAH ALJs and the Commission in that docket. "Many of the allegations and arguments made by Dr. Szerszen in this case are very similar, if not identical, to the points she asserted in the *Oncor* case.

The ALJs agree that the Commission's Guiding Principles set forth the minimum that a utility must present to establish a *prima facie* case, and it is clear that ETI met that burden. That, however, is not the end of the question. Permitting a utility to escape further scrutiny of its affiliate transactions by resting on its *prima facie* presentation imposes too many limits and, as suggested by OPC, presents too macro a view to be a legitimate review for rate case purposes.

OPC performed essentially a sample review of ETI's affiliate transactions. The review was not exceptionally large, and (as evidenced by ETI's concurrence in the removal of some of the costs) it represented an additional layer of review to ensure that improper costs would not inadvertently be charged to ratepayers. That, of course, is not the sole focus of OPC's review, but it is important for purposes of determining whether the review itself is appropriate. If intervenors and Staff were limited to the macro level of review urged by ETI, such matters would never be revealed and there would exist a possibility that ratepayers would be charged for matters not their responsibility. The ALJs do not characterize OPC's review as "cherry picking." It is more a reasonable sample for examination that gives ETI a reasonable opportunity to explain the reasons for the charges to ratepayers. Accordingly, the ALJs find that the Commission's Guiding Principles do not limit the review performed by OPC, and the review performed by OPC is not contrary to the Commission's holdings in Docket No. 16705.

A. Large Industrial & Commercial Sales Reallocation

OPC contends that ETI incurs considerable amounts of sales and marketing expenses that are exclusively for the benefit of the larger commercial and industrial customers. However, most of ESI's sales, marketing, and customer service expenses are allocated to residential and small business

⁷⁰³ *Application of Oncor Electric Delivery Company, LLC for Authority to Change Rates*, Docket No. 35717 (PFD issued on Jun. 2, 2009; Order on Rehearing issued on Nov. 30, 2009) (*Oncor*).

⁷⁰⁴ Tr. at 1656.

customers.⁷⁰⁵ The vast majority of the sales, marketing and customer service expenses are allocated to the operating companies based on customer counts, the majority of these expenses are consequently allocated to residential and small business customers. In the test year, residential and small general service customers made up 94.8 percent of the ETI total customer count. ETI's General Service, Large General Service, and Large Industrial Power Service, and Lighting classes combined comprise only 5.2 percent of ETI's customers. For the test year, OPC argues that ETI is requesting the recovery of \$2.086 million of sales, marketing, billing and load research expenses that benefitted only the large customer service classes. OPC contends that it is inappropriate for residential and small customers to pay for these expenses, when cost causation is so readily identifiable, particularly since a disproportionately small portion of larger customer sales and marketing expenses is allocated to ETI's largest customers.⁷⁰⁶ The total recommended reallocated large customer expense is \$2,086,145.

ETI and TIEC oppose OPC's recommendation, arguing that it is "cherry-picking" and that the evidence does not demonstrate that the \$2.086 million of affiliate expense should be directly assigned to the large commercial and industrial classes.⁷⁰⁷

With respect to the first argument, ETI and TIEC contend that Dr. Szerszen developed her adjustment by examining a limited sample of affiliate project code summaries and making the call, based on project code descriptions, that certain affiliate costs for marketing, sales and customer service expense should be directly assigned to large commercial and industrial customers.⁷⁰⁸ Both TIEC and ETI contend that the bias and results-oriented nature of her recommendation became apparent when Dr. Szerszen admitted on cross examination that she made no effort to examine whether certain affiliate costs should be directly assigned to residential and small customers.⁷⁰⁹ Both ETI and TIEC contend that it is inappropriate to take a "limited sample of costs" and directly assign them to a particular class.

⁷⁰⁵ OPC Ex. 1 (Szerszen Direct) at 45.

⁷⁰⁶ OPC Ex. 1 (Szerszen Direct) at 45.

⁷⁰⁷ ETI Ex. 55 (LeBlanc Rebuttal) at 5; TIEC Ex. 3 (Pollock Cross Rebuttal) at 36.

⁷⁰⁸ Tr. at 1609.

According to TIEC, Dr. Szerszen admitted that it could have been appropriate to make an adjustment for direct assignment of costs to small commercial and residential customers based on principles of cost causation.⁷¹⁰ However, she made no effort to do that herself, nor did she ask ETI to conduct such an analysis.⁷¹¹ The parties argue that the evidence shows that Dr. Szerszen's recommendation rests on an incomplete analysis of ETI's affiliate costs and her recommendation should be rejected because direct assignment of costs is only appropriate if there has been a thorough and complete cost study analysis to determine what costs are or are not appropriate for direct assignment to *all* of the classes.

TIEC further argues that the evidence did not demonstrate that the \$2.086 million of affiliate expense that Dr. Szerszen proposes for direct assignment to large commercial and industrial customers is solely attributable to costs caused by those customers. Mr. Pollock testified that the project codes Dr. Szerszen selected include load research expenses that benefit residential and small commercial customers.⁷¹² TIEC pointed out that ETI witness Stokes testified that the billing methods used for the affiliate expenses for customer service operations and retail operations were fair and reasonable.⁷¹³ According to TIEC, Dr. Szerszen's proposal should be rejected because her assertion that these expenses exclusively benefit large commercial and industrial customers is incorrect.

The ALJs have reviewed the arguments of the parties and find that Dr. Szerszen's analysis is far from complete. It appears to be result-oriented, ignoring critical aspects (such as failing to make an adjustment for direct assignment of costs to small commercial and residential customers based on principles of cost causation). The ALJs believe that Dr. Szerszen's analysis with respect to this issue should not be adopted.

⁷⁰⁹ Tr. at 1609-10.

⁷¹⁰ Tr. at 1685.

⁷¹¹ Tr. at 1613-1624.

⁷¹² TIEC Ex. 3 (Pollock Cross Rebuttal) at 35.

⁷¹³ ETI Ex. 66 (Stokes Rebuttal) at 3.

B. Administration Costs

Dr. Szerszen recommended disallowance of \$94,709 (25 percent) of the charges in Project F3PCFACALL, contending that ESI failed to directly charge any of the costs in this project code to ETI. She claimed that the billing method applied to this project code by ESI (that is, Billing Method “SQFALLC”), which is based on square footage, is not appropriate for these types of costs.⁷¹⁴

ETI witness Plauche explained that the costs captured in this project code are primarily for the oversight of administrative functions, such as facilities, real estate, and security.⁷¹⁵ This project code applies to the administration of these types of functions. These services benefit all companies that receive facility services and are not attributable to any one specific Entergy affiliate. Therefore, it is appropriate to bill these costs to all companies based on their pro rata share of square footage occupied.⁷¹⁶

The ALJs concur that this is the appropriate method to employ and, therefore, recommend that the Commission approve the inclusion of these costs as requested by ETI.

C. Customer Service Operations Class

Dr. Szerszen recommended disallowances in seven project codes covered primarily by ETI’s Customer Service Operations Class: (1) F3PCR29324 (Revenue Assurance - Adm.) for a disallowance of \$70,849; (2) F3PCR53095 (Headquarter’s Credit & Collect) for a disallowance of \$110,338; (3) F3PCR73380 (Credit Systems) for a disallowance of \$73,562; (4) F3PCR73458 (Credit Call Outsourcing) for a disallowance of \$197; (5) F3PCR73381 (Customer Svc Cntr Credit Desk) for a disallowance of \$43,378; (6) F3PCR73390 (Customer Svs Ctl - Entergy Bus) for a

⁷¹⁴ OPC Ex. 1 (Szerszen Direct) at 80-82.

⁷¹⁵ ETI Ex. 20 (Plauche Direct) at 15-26.

⁷¹⁶ ETI Ex. 69 (Tumminello Rebuttal) at Ex. SBT-R-2 at 10.

disallowance of \$60,926; and (7) F3PCR73403 (Customer Issue Resolution – ES) for a disallowance of \$1,869.⁷¹⁷

1. Projects F3PCR29324 (Revenue Assurance - Adm.), F3PCR53095 (Headquarter's Credit & Collect), F3PCR73380 (Credit Systems), and F3PCR73458 (Credit Call Outsourcing)

For the costs captured by these project codes, Dr. Szerszen recommended that the costs be reallocated based on the Company's 10 percent "bad debt" expense percentage.

ETI witness Stokes responded that the costs captured by these project codes are for management and supervision of credit, collection, and revenue assurance activities for all of the Operating Companies. These functions ensure the most efficient processes are used in managing write-offs for all the Operating Companies and have contributed to Entergy's first quartile ranking in benchmarking of credit and collection operations. These managerial and supervisory costs, which include bankruptcy administration, surety administration, arrears management, collection agency administration, skip tracing, and final bill collections, remain consistent whether ETI's bad debt percentage is 10 percent, 30 percent, or any other percent and are appropriately allocated using the CUSTEGOP billing method, which is based on the number of electric and gas customers for each Operating Company.⁷¹⁸

ETI has provided credible evidence that it has chosen the correct billing methodology. Therefore, the ALJs recommend the Commission approve inclusion of these costs as requested by ETI.

2. Projects F3PCR73381 (Customer Svc Cntr Credit Desk), F3PCR73390 (Customer Svs Ctl - Entergy Bus), and F3PCR73403 (Customer Issue Resolution – ES)

Dr. Szerszen recommended that these costs be reallocated using the CUSTCALL billing method. Given ESI's demonstrated tracking capabilities, Dr. Szerszen reallocated the costs of this

⁷¹⁷ OPC Ex. 1 (Szerszen Direct) at 76-78.

⁷¹⁸ ETI Ex. 66 (Stokes Rebuttal) at 15-16.

project using a 10.8 percent customer call allocator, which is on the low end of the 10.70 percent-11.04 percent Test-Year CUSTCALL allocators.⁷¹⁹

ETI witness Stokes believes that Dr. Szerszen's proposed reallocation is arbitrary and fails to consider the cost causation associated with the actual project code at issue. These costs are not driven by a specific proportion of calls from each Operating Company (that is, by the CUSTCALL allocator). The costs captured by Project F3PCR73345 reflect the costs of overseeing the Quick Payment Center vendors in each of the Entergy Operating Companies, regardless of the number of calls by customers to the Company.

The ALJs are persuaded that the allocation methodology chosen by ETI is the superior method and that the CUSTCALL allocator would not be appropriate given the cost causation associated with the project. Accordingly, the ALJs recommend the Commission approve the costs proposed by ETI.

D. Distribution Operations Class

Dr. Szerszen addressed three project codes that are within the Distribution Operations Class: (1) F5PCDW0200 (Lineman's Rodeo Expenses) for a disallowance of \$7; (2) F3PCTJGUSE (Joint Use With Third Party – E) for a disallowance of \$6,405; and (3) F3PCTJTUSE (Joint Use With 3rd Parties – A) for a disallowance of \$36,293.⁷²⁰

1. Project F5PCDW0200 (Lineman's Rodeo Expenses)

Dr. Szerszen claimed that the expenses captured by this project should be disallowed because ETI is a monopoly and Texas ratepayers should not have to pay for corporate image costs.

ETI witness Tumminello responds, stating that this minimal amount is related to a safety competition known as the "Lineman's Rodeo," it is not a corporate "image" expense. The cost,

⁷¹⁹ OPC Exhibit No. 1 (Szerszen Direct) at 77 and 118; OPC Exhibit No. 27 (ETI's Ex. SBT-15, Attachment 6) at 2; Tr., at 838-839.

⁷²⁰ OPC Ex. 1 (Szerszen Direct) at 66, 75.

according to Ms. Tumminello, is driven by Entergy employee safety in the Distribution business units.⁷²¹

The ALJs agree that the Lineman's Rodeo competition is not a corporate image expense, rather it is designed to promote employee safety. The ALJs recommend the Commission approve inclusion of the costs captured by this project as requested by ETI.

2. Projects F3PCTJGUSE (Joint Use With Third Party – E) and F3PCTJTUSE (Joint Use With Third Parties – A)

Dr. Szerszen recommends exclusion of these two projects, which she claims represent the difference between the costs incurred for ETI for pole rental costs and the revenues received from pole space rentals.

With respect to this proposed disallowance, ETI witness McCulla states that Dr. Szerszen has confused the rental of space on transmission poles and the rental of space on distribution poles. She has essentially performed a cost-benefit analysis that erroneously compares the cost of providing rental space on distribution poles with the income received solely from rental of space on transmission poles. Mr. McCulla explained that data for the distribution poles show that the more than \$2.5 million in revenues from distribution pole rentals far exceeds the \$67,174 in costs billed to ETI under these two project codes and, therefore, Dr. Szerszen's misassumption that the revenues were less than the costs incurred is unfounded.⁷²²

The ALJs find that Dr. Szerszen erred. Making the correct comparison, as demonstrated by Mr. McCulla, shows there is no basis for the disallowance claimed by Dr. Szerszen. The ALJs, therefore, recommend the Commission deny the requested disallowance.

⁷²¹ ETI Ex. 41 (Tumminello Direct) at Ex. SBT-E at 1234.

⁷²² ETI Ex. 59 (McCulla Rebuttal) at 8-12.

E. Energy and Fuel Management Class

Dr. Szerszen addresses seven project codes that are within the Energy and Fuel Management Class: (1) F3PCCSPSYS (System Planning And Strategic) for a disallowance of \$29,304; (2) F3PCWE0140 (EMO Regulatory Affairs) for a disallowance of \$114,468; (3) F3PPSPE002 (SPO 2009 Renewable RFP Expense) for a disallowance of \$3,014; (4) F3PPSPE003 (SPO Summer 2009 RFP Expense) for a disallowance of \$56,672; (5) F3PPSPE004 (SPO Summer09RFP IM&Propslsubmt) for a disallowance of \$42,018; (6) F3PPWET300 (SPO 2008 Western Region RFP-Te) for a disallowance of \$645; and (7) F3PPWET303 (SPO2008WinterWestnRegionRFP-IM) for a disallowance of \$4,200.⁷²³

1. Project F3PCWE0140 (EMO Regulatory Affairs)

Dr. Szerszen testified that Texas ratepayers do not receive benefits as a result of the costs captured by this project code and should therefore not be charged those costs.⁷²⁴

ETI witness Cicio explained that Dr. Szerszen misinterpreted an RFI response to conclude that Texas ratepayers did not receive benefits from the activities whose costs were booked through this project code. That project code is not intended to capture costs for docketed or large System Planning and Operations projects. Mr. Cicio states that it is not possible to assign a specific project code for every discrete activity performed by each employee, nor would it be appropriate to attempt to do so. Regardless of the number of activities specifically identified through project codes, there will remain the need to have generic project codes that capture time spent on more general, undocketed matters and activities that are no less beneficial to ratepayers.⁷²⁵

The ALJs agree that Texas ratepayers receive benefits as a result of the costs charged to this account. Accordingly, the ALJs recommend the Commission approve inclusion of the costs as requested by ETI.

2. Projects F3PPSPE003 (SPO Summer 2009 RFP Expense), F3PPSPE003 (SPO

⁷²³ OPC Ex. 1 (Szerszen Direct) at 55, 60, and 65-66.

⁷²⁴ *Id.* at 55.

⁷²⁵ ETI Ex. 45 (Cicio Rebuttal) at 8-9.

Summer 2009 RFP Expense), F3PPSPE004 (SPO Summer09RFP IM & Propslsubmt), and F3PPWET303 (SPO2008 Winter Westn RegionRFP-IM)

Dr. Szerszen testified that the costs captured by these projects should be disregarded because they were incurred during the 2008-2009 period, which is outside of the Test Year, and are nonrecurring.⁷²⁶

ETI witness Cicio explained that although these projects were initiated prior to the Test Year, the costs that the Company seeks to recover through these project codes were expenses incurred during the Test Year, including development activities, request for proposal issuance, bidders conferences, written and posted questions and answers from market participants and other interested parties, submission of proposals, screening of proposals, proposal evaluation, follow-up questions and clarifications, recommendations and awards, contract negotiations, Independent Monitor reports, and regulatory approvals, if necessary. These routinely encompass a multi-year time frame, and the costs required to perform those activities, although associated with a project that may have been initiated several years previously, are properly incurred over the life span of the project. He also states that they are recurring because they reflect the kinds and levels of charges that would be expected to be incurred on an ongoing basis in association with requests for proposals managed by ESI on behalf of the Entergy Operating Companies, and the Company has been involved in these types of solicitations since 2002.⁷²⁷

The ALJs find that the costs captured by these projects were incurred during the Test Year and represent the kinds and levels of costs routinely incurred on a recurring basis. Accordingly, the ALJs recommend that the Commission approve their inclusion as requested by ETI.

3. Project F3PCCSPSYS (System Planning and Strategic)

Dr. Szerszen recommended total disallowance of the costs captured by this project code because they are allocated based on the total assets of the Entergy affiliates.⁷²⁸ Dr. Szerszen's

⁷²⁶ OPC Ex. 1 (Szerszen Direct) at 65.

⁷²⁷ ETI Ex. 45 (Cicio Rebuttal) at 13-14.

⁷²⁸ OPC Ex. 1 (Szerszen Direct) at 60-61.

conclusion appears to be that no such corporate-level costs should be allocated to ETI because there are other project codes that allocate corporate planning and analysis-type costs only to the regulated utilities, such as ETI; thus, any corporate-level costs that are allocated to all subsidiaries, whether regulated or non-regulated, should not be charged to ETI.

ETI witness Tumminello testified that Dr. Szerszen's theory neither considers the Entergy organization as a family of companies and ETI's place in that family, nor the fact that these services are not only relevant to ETI as part of the Entergy family, but are reasonable, necessary and meet the Commission's affiliate cost recovery standard. ESI's corporate oversight services are provided to both individual companies and groups of companies within the Entergy 'corporate structure. As a member of the corporate group, ETI receives the benefit of corporate-level planning, reporting, and forecasting activities provided by ESI.⁷²⁹

The ALJs find that ETI (and, therefore, its ratepayers) does receive benefits as a member of the Entergy family of companies and that it is appropriate for it to receive charges for those services. Therefore, the ALJs recommend the Commission approve the inclusion of costs as requested by ETI.

F. Environmental Service Class

Dr. Szerszen recommended disallowance of \$301,879 in six project codes primarily within ETI's Environmental Services Class: (1) F3PCCE0129 (Corporate Sustainability Strat) for a disallowance of \$6,781; (2) F3PCCE0193 (Corp Environmental Special Pro) for a disallowance of \$1,203; (3) F3PCCEIE01 (Corp Environmental Initiatives) for a disallowance of \$2,413; (4) F3PCCEII01 (Corp Environmental Initiatives) for a disallowance of \$2,413; (5) F3PCCEP001 (Corporate Environmental Policy) for a disallowance of \$269,248; and (6) F5PPBCNAVF (Avian Flu Contingency Planning) for a disallowance of \$47.⁷³⁰

Dr. Szerszen's reasoning for this disallowance was that these six project codes, which all deal with corporate environmental policy, initiatives, strategy, and consulting services, were allocated

⁷²⁹ ETI Ex. 69 (Tumminello Rebuttal) at 10-11.

⁷³⁰ OPC Ex. 1 (Szerszen Direct) at 62-63.

based on Billing Method CAPAOPCO, which is based on the fossil plant capacity of the regulated utility operating companies, even though “non-regulated entities clearly benefit from the corporate level expenses.”⁷³¹ Dr. Szerszen recommended a \$47 disallowance for Project F5PPCCNAVF (Avian Flu Contingency Planning), asserting that this charge is a “corporate imaging expense that should not be borne by Texas ratepayers.”⁷³²

According to ETI, Dr. Szerszen has a fundamental misunderstanding of how the affiliate billing system works and, as a result, she incorrectly assumed that ESI charges are not being properly allocated. ETI argues that the non-regulated Entergy affiliates do receive the proper and appropriate allocation of costs. The two service companies for non-regulated affiliates also provide services to their non-regulated affiliates directly. There simply is no subsidization or improper allocation.⁷³³

Dr. Szerszen noted that Entergy’s website indicates that nuclear-related environmental issues are being pursued.⁷³⁴ She argued that this shows that the non-regulated affiliates are under-allocated environmental-related costs. Ms. Stokes explained that the project codes at issue “deal with services provided to the operating companies. . . . and just looking at the website there are other things . . . that are not covered or paid for by Texas ratepayers in these project codes that are in this testimony.”⁷³⁵ Therefore, according to Ms. Stokes, these project codes are not allocated in such a way that under-recovers costs from the non-regulated affiliates; they pay their own way.

Finally, the Project Summary for the Avian Flu Contingency Planning project shows that these costs involve developing and communicating Avian Flu business continuity plans and then

⁷³¹ *Id.*

⁷³² *Id.* at 66.

⁷³³ *See, e.g.*, ETI Ex. 41 (Tumminello Direct) at 10-15. Moreover, while ESI bills the regulated utility affiliates such as ETI at cost, it bills the non-regulated affiliates at cost plus a 5 percent mark-up pursuant to a June 1999 Securities and Exchange Commission order. ETI Ex. 41 (Tumminello Direct) at 15. This 5 percent mark-up is then flowed back to entities that receive service from ESI. Therefore, the regulated affiliates are, by federal order, receiving essentially a rebate from the non-regulated affiliates.

⁷³⁴ OPC Ex. 1 (Szerszen Direct) at 62.

⁷³⁵ Tr. at 884.

maintaining, checking, and adjusting those plans once established.⁷³⁶ These are not “corporate imaging expenses” as characterized by Dr. Szerszen.

The ALJs agree that ETI’s evidence demonstrates the recoverability of the costs captured by these project codes. Therefore, the ALJs recommend the Commission approve their recovery.

G. Federal PRG Affairs Class

Dr. Szerszen recommended disallowances for three project codes primarily in the Federal PRG Affairs Class: (1) F5PPSPE044 (PMO Support Initiative-System) for a disallowance of \$344; (2) F3PPUTLDER (Utility Derivatives Compliance) for a disallowance of \$20,447; and (3) F3PCSYSRAF (System Regulatory Affairs-Federal) for a disallowance of \$352,084.⁷³⁷

1. Project F5PPSPE044 (PMO Support Initiative-System)

Dr. Szerszen recommended disallowance of \$344.29 from Project F5PPSPE044 (PMO Support Initiative System). ETI responds, however, that a review of the Project Summary for that project code in Ex. SBT-E reveals that ETI already removed those costs before even filing its direct case. Therefore, according to ETI, Dr. Szerszen is recommending disallowance of a cost that is not in this case.⁷³⁸

The ALJs agree that examination of the exhibit referenced by ETI appears to reveal that the costs challenged by Dr. Szerszen have been removed from this case through a *pro forma* adjustment. Accordingly, the ALJs recommend the Commission reject OPC’s challenge.

⁷³⁶ ETI Ex. 41 (Tumminello Direct) at SBT-E at 1342-43.

⁷³⁷ OPC Ex. 1 (Szerszen Direct) at 46-47, 66-67.

⁷³⁸ ETI Initial Brief at 174-175.

2. Project F3PPUTLDER (Utility Derivatives Compliance)

Dr. Szerszen recommended disallowance of \$20,447 of derivatives expenses because ETI did not use derivative instruments and therefore should not be charged these costs and because ratepayers do not benefit from derivatives.⁷³⁹

ETI witness Tumminello responded that Project F3PPUTLDER was charged by a group developing compliance mechanisms to protect Entergy's regulated utility interests in observance of the Dodd-Frank Act. Although ETI does not currently use any derivative activities, understanding the impacts of that Act is necessary to ensure current and future compliance through Entergy. The definitions under the legislation have not been finalized, and there remain issues that ETI must be aware of to fully comply. These costs, therefore, are necessary and reasonable charges that should not be disallowed.⁷⁴⁰

The explanation offered by ETI for the inclusion of these charges appears reasonable to the ALJs. Even though ETI does not now use derivatives, it is possible that it will in the future and it is important that it be aware of the regulatory framework associated with such actions to avoid problems. The ALJs therefore recommend the Commission approve inclusion of these costs as requested by ETI.

3. Project F3PCSYSRAF (System Regulatory Affairs-Federal)

In the regulatory affairs category, ETI requests the recovery of various legal, testimony-related, communications, and filing costs associated with both Texas-specific regulatory activities, FERC-related regulatory activities, and non-Texas specific regulatory activities. OPC witness Szerszen did not recommend a disallowance of the \$1,442,223 in adjusted Test Year expenses for regulatory affairs that ETI has shown to be specific to the Texas jurisdiction.⁷⁴¹ Rather,

⁷³⁹ ETI stated that it assumes that Dr. Szerszen must be referring to Project Code F3PPUTLDER (Utility Derivatives Compliance) because her recommended disallowance is the same total ETI adjusted amount shown on the Project Summary for that project code. *See* SBT-E at 1113. The ALJs make the same assumption as it appears reasonable.

⁷⁴⁰ ETI Ex. 69 (Tuminello Rebuttal) at Ex. SBT-R-2 at 3.

⁷⁴¹ *See* OPC Ex. 3 (Szerszen Workpapers) at 368-371.

Dr. Szerszen recommended that all regulatory affairs expenses not specific to Texas be disallowed.⁷⁴² These expenses total \$759,868.⁷⁴³

Project F3PCSYSRAS (System Regulatory Affairs – State) was incurred for administrative activities for senior management, project work associated with system-wide regulatory matters, system-wide regulatory strategies and emerging regulatory issues, and it relates to multiple regulated jurisdictions.⁷⁴⁴ Project No. F3PCSYSRAF (System Regulatory Affairs – Federal) was incurred for regulatory oversight and coordination of FERC matters.⁷⁴⁵ OPC contends that ETI provided no evidence that Texas ratepayers receive any tangible benefits from “system” regulatory affairs costs in proportion to the costs being allocated to Texas.

Project F3PCSYSRAS costs are allocated to the subsidiaries based on electric customer counts, and OPC states that it is questionable whether Entergy’s positions on “emerging” state or national regulatory issues or “system-wide regulatory strategies” are conveying any benefits to its electric customers beyond those already captured in the Texas-specific regulatory affairs project codes.⁷⁴⁶ In fact, according to OPC, the Company’s shareholders are the primary beneficiaries of these system-wide regulatory strategies.⁷⁴⁷ The federal regulatory affairs costs captured under Project F3PCSYSRAF are allocated to the regulated subsidiaries based on each company’s load responsibility ratio; this ratio assumes that every FERC docket and/or FERC issue is related to ETI’s peak demand. According to OPC, this is not reality, nor is it consistent with FERC’s primary responsibility to ensure that electric wholesale buyers and sellers are provided open access transmission across utility systems.

ETI witness May offered the following as rebuttal of Dr. Szerszen’s contentions regarding these two project codes:

⁷⁴² OPC Ex. 1 (Szerszen Direct) at 46-47.

⁷⁴³ *Id.* at 46.

⁷⁴⁴ OPC Ex. 3 (Szerszen Workpapers) at 365.

⁷⁴⁵ OPC Ex. 1 (Szerszen Direct) at 46-47; OPC Ex. 3 (Szerszen Workpapers) at 367.

⁷⁴⁶ OPC Ex. 3 (Szerszen Workpapers) at 368-371.

The affiliate charges to Project Codes F3PCSYSRAS and F3PCSYSRAF are directly associated with the issues and matters within the federal jurisdiction of the Federal Energy Regulatory Commission (“FERC”) including but not limited to the Open Access Transmission Tariff (“OATT”) as well as any other federal statutes, rules and regulations. These are the result of issues and matters raised concerning the OATT, operations of the transmission system, requests for transmission service and interpretation of applicable provisions under the jurisdiction of FERC. They are costs incurred on an Entergy System-wide basis that cannot be directly assigned to any one Operating Company, such as ETI.⁷⁴⁸

He then went on to state that the affiliate Test Year issues and costs related to these project codes are reflective of typical issues and costs that the Company experiences on an ongoing basis.⁷⁴⁹ With respect to the benefits derived by Texas ratepayers as a result of activities conducted under these project codes, Mr. May stated that:

the benefit to ETI involves a multitude of issues that are directly related to the jurisdiction of the FERC, including but not limited to any revisions to Service Schedules under the System Agreement that applies to all operating companies including ETI, power purchase agreements for cost-based, short-term power sales, and compliance with FERC by each Operating Company to the market-based rate tariff and cost-based rate tariff. The Entergy Operating Companies’ market-based rate tariff and cost-based rate tariff are joint tariffs containing terms and conditions of service.⁷⁵⁰

Mr. May also explained why the billing methods applied to these two project codes are appropriate. The cost drivers for Project F3PCSYSRAF are labor, employee expenses, consultant expenses, and other general operating expenses incurred for the benefit of the Entergy Operating Companies and their regulated customers. Therefore, a billing method based on load responsibility – “LOADOPCO” – is appropriate for this type of project code. Project F3PCSYSRAS captures costs associated with general regulatory support work that is applicable across all of the jurisdictions. The primary activities associated in this project code include but are not limited to: special project work associated with system-wide regulatory matters, analysis of emerging state or national regulatory and

⁷⁴⁷ OPC Ex. 1 (Szerszen Direct) at 47.

⁷⁴⁸ ETI Ex. 57 (May Rebuttal) at 25.

⁷⁴⁹ ETI Ex. 57 (May Rebuttal) at 25.

⁷⁵⁰ ETI Ex. 57 (May Rebuttal) at 27-28; *see also*, Tr. at 370-371.

accounting issues affecting the Entergy System, and internal process improvement work. What drives the cost of this project code is the average number of both electric and gas customers served – CUSTEGOP – because all such customers benefit from these services provided by ESI to ETI.⁷⁵¹ In short, according to ETI, the activities undertaken under both of these project codes benefit Texas ratepayers, and they are properly allocated to the regulated operating companies using the billing methods employed.

The ALJs believe that resolution of this question is a close call. Although ETI provided an adequate explanation of the reasons underlying the allocation of costs to Texas ratepayers and the appropriateness of the allocation methodologies used, the one troubling aspect, as noted by OPC, was that Mr. May’s testimony regarding Projects F3PCSYSRAF and FP3PCSYSRAS contradicted the fact that ESI has a specific project dedicated to open access transmission issues entitled “FERC-Open Access Transmission” (Project F3PCE01601).⁷⁵² As OPC notes, if Mr. May was correct that OATT issues have been included in Projects F3PCSYSRAF and FP3PCSYSRAS the project pages should arguably be more specific about the purpose of the expenditure. Nevertheless, the ALJs find ETI’s testimony credible and recommend that the costs of Projects F3PCSYSRAF and FP3PCSYSRAS not be disregarded.

H. Financial Services Class

Dr. Szerszen recommended disallowances in nine project codes that are primarily captured within ETI’s Financial Services Class of affiliate costs: (1) F3PCF05700 (Corporate Planning & Analysis) for a disallowance of \$4,254; (2) F3PCF21600 (Corp Rptg Analysis & Policy) for a disallowance of \$320,157; (3) F3PCFF1000 (Financial Forecasting) for a disallowance of \$96,734; (4) F3PPADSENT (Analytic/Decision Support-Entergy) for a disallowance of \$93,544; (5) F3PPSPSENT (Strategic Planning Svcs-Entergy) for a disallowance of \$45,265; (6) F3PCR73345 (Quick Payment Center, Adm) for a disallowance of \$14,484; (7) F3PCF20990

⁷⁵¹ ETI Ex. 57 (May Rebuttal) at 28-29.

⁷⁵² OPC Ex. 11; *also found in* OPC Exhibit No. 3 (Szerszen Workpapers) at 363-364.

(Operations Exec VP & CFO) for a disallowance of \$146,267; (8) F3PCFF1001 (OCE Support) for a disallowance of \$1,923; and (9) F3PCF23936 (Manage Cash) for a disallowance of \$15,677.⁷⁵³

1. Projects F3PCF05700 (Corporate Planning & Analysis), F3PCF21600 (Corp Rptg Analysis & Policy), F3PCFF1000 (Financial Forecasting), F3PPADSENT (Analytic/Decision Support-Entergy), and F3PPSPSENT (Strategic Planning Svcs-Entergy)

Dr. Szerszen proposed to disallow all costs related to these five project codes, which she collectively describes as addressing Corporate Planning, Reporting, and Forecasting issues because she contends that an assets-based allocator should not be used to allocate these costs and, regardless of the allocator used, these types of services do not benefit Texas ratepayers because ESI has, in other instances, directly billed corporate-level services to ETI.

ETI witness Tumminello responded, stating that Dr. Szerszen failed to consider the Entergy organization as a family of companies and ETI's place in that family. The services provided under these project codes are not only relevant to ETI as part of the Entergy family, but are reasonable and necessary. ESI's corporate oversight services are provided to both individual companies and groups of companies within the Entergy Companies' corporate structure. As a member of the corporate group, ETI receives the benefit of corporate-level planning, reporting, and forecasting activities provided by ESI. Ms. Tumminello contested that the use of an asset-based allocator is appropriate because this is an example of the stewardship of the company-wide assets and such an allocator is, therefore, appropriate.⁷⁵⁴ The ALJs agree.

The ALJs find that ETI's proposed allocator is appropriate and that the costs benefit Texas ratepayers. Accordingly, the ALJs recommend the Commission approve the costs proposed by ETI.

⁷⁵³ OPC Ex. 1 (Szerszen Direct) at 56, 60-62, and 74, and Schedules CAS-9, CAS-10, and CAS-15.

⁷⁵⁴ ETI Ex. 69 (Tumminello Rebuttal) at 10-11.

2. Projects F3PCF20990 (Operations Exec VP & CFO) and F3PCFF1001 (OCE Support)

Dr. Szerszen recommended disallowance of all costs captured by these project codes because, in her opinion: (1) there are “no perceivable benefits to ETI’s ratepayers”; (2) they should be paid for by the parent entity (presumably meaning Entergy’s shareholders); and (3) an assets-based allocator is not appropriate.⁷⁵⁵

As to Dr. Szerszen’s assertion that Texas ratepayers do not benefit from the costs captured by these project codes, ETI witness Domino, President of Entergy, provided anecdotal evidence that that Entergy was vital to ETI’s restoration efforts on two fronts. First, the parent provided cash to ETI for its hurricane restoration efforts; second, ETI was not required to pay dividends to the parent while it was strapped for funds due to hurricane restoration efforts.⁷⁵⁶ With respect to the argument that an asset-based allocator is not appropriate, Ms. Tumminello testified that the functions covered by this project code relate to the oversight of all system operations and the stewardship of corporate assets and that because ETI is part of a corporate group, the allocated charges associated with these services are relevant to ETI as part of that group. Furthermore, ETI argues, the asset-based allocator is appropriate because it reflects the cause of the costs incurred, in that services provided relate to the stewardship of all the corporation’s assets.⁷⁵⁷

Dr. Szerszen took too narrow a view and, without justification, argued that these costs provide no benefit to Texas ratepayers. There are innumerable benefits provided by the corporate structure adopted; those mentioned by Mr. Domino are just a few. Ms. Tumminello’s testimony explained why an asset-based allocator is appropriate. Accordingly, the ALJs recommend the Commission approve the inclusion of these costs as requested by ETI.

⁷⁵⁵ OPC Ex. 1 (Szerszen Direct) at 56-57.

⁷⁵⁶ Tr. at 141.

⁷⁵⁷ ETI Ex. 69 (Tumminello Rebuttal) at 9-11.

3. Project F3PCR73345 (Quick Payment Center, Adm)

Dr. Szerszen recommended that these costs be reallocated using the CUSTCALL billing method. Given ESI's demonstrated tracking capabilities, Dr. Szerszen reallocated the costs of this project using a 10.8 percent customer call allocator, which is on the low end of the 10.70 percent-11.04 percent Test-Year CUSTCALL allocators.⁷⁵⁸ As a result of Dr. Szerszen's reallocation, \$14,484 associated with this project should, according to Dr. Szerszen, be disallowed.⁷⁵⁹

ETI witness Stokes responded, stating that Dr. Szerszen's proposed reallocation is arbitrary and fails to consider the cost causation associated with the actual project code at issue. These costs are not driven by a specific proportion of calls from each Operating Company (that is, by the CUSTCALL allocator). The costs captured by Project F3PCR73345 reflect the costs of overseeing the Quick Payment Center vendors in each of the Entergy Operating Companies, regardless of the number of calls by customers to the Company.⁷⁶⁰

The ALJs are persuaded that the allocation methodology chosen by ETI is the superior method and that the CUSTCALL allocator would not be appropriate given the cost causation associated with the project. Accordingly, the ALJs recommend the Commission approve the costs proposed by ETI.

4. Project F3PCF23936 (Manage Cash)

Dr. Szerszen recommended disallowance of \$15,677 from Project F3PCF23936 (Manage Cash), arguing that this project: (1) is duplicative of ETI-specific financing and cash management activities; (2) the allocator is wrong; and (3) Entergy, not ETI ratepayers, should pay for this activity.⁷⁶¹

⁷⁵⁸ OPC Exhibit No. 27 (ETI's Ex. SBT-15, Attachment 6) at 2; Tr. at 838-839.

⁷⁵⁹ OPC Exhibit No. 1 (Szerszen Direct) at 77 and 118.

⁷⁶⁰ ETI Ex. 66 (Stokes Rebuttal) at 11.

⁷⁶¹ OPC Ex. 1 (Szerszen Direct) at 74 and Schedule CAS-15.

ETI witness McNeal testified that the services are not duplicative of the cash management services performed by the Cash Management department in the Treasury Class. The services provided under Project F3PCF23936 are associated with daily cash management responsibilities, such as loading bank balances, setting daily cash position for all the Entergy Companies, transmitting wire/ACH files to Entergy Company banks for vendor payments, and maintaining proper cash controls over these cash functions. These services are necessary for the daily operation of all the Entergy Companies, including ETI, and are thus not directly associated with any one specific legal entity. The costs are driven by the time spent on the daily cash management activities, which is directly related to the number of bank accounts that the Entergy Companies have open. Since the services provided under this project code cannot be identified to a particular Entergy Company, the billing method based on the number of open bank accounts is the best allocation. Billing method BNKACCTA does that and, according to Mr. McNeal, is therefore appropriate for allocating costs for this project code.⁷⁶²

The evidence demonstrates that the activities captured by this project code are not directly associated with any one specific entity; rather, they benefit all the entities under the Entergy umbrella. It also appears that a billing method based on the number of open bank accounts is the appropriate allocation methodology. Accordingly, the ALJs recommend the Commission approve inclusion of costs as requested by ETI.

I. Human Resources Class

Dr. Szerszen recommended disallowances for three project codes that are primarily within the Human Resources Class of affiliate costs: (1) F3PCHRCCSM (HR Competitive Compensation) for a disallowance of \$20,146; (2) F5PCZUBENQ (Non-Qualified Post-Retirement) for a disallowance of \$115,078; and (3) F5PPZNQBUDU (Non-Qual Pension/Benf-Dom Utl) for a disallowance of \$241,073.⁷⁶³

⁷⁶² ETI Ex. 61 (McNeal Rebuttal) at 4, 6; Tr. at 546-547.

⁷⁶³ OPC Ex. 1 (Szerszen Direct) at 56, 68.

1. Project F3PCHRCCSM (HR Competitive Compensation)

Dr. Szerszen testified that an asset-based allocator is not appropriate for a project, such as Project F3PCHRCCSM, that captures overall executive management-related costs.⁷⁶⁴

ETI contends that the functions covered by this project code relate to the oversight of all system operations and the stewardship of corporate assets and that because ETI is part of a corporate group, the allocated charges associated with these services are relevant to ETI as part of that group of companies. Furthermore, ETI argues, the asset-based allocator is appropriate because it reflects the cause of the costs incurred, in that services provided relate to the stewardship of all the corporation's assets.⁷⁶⁵

A corporation cannot function without executives, who are charged with the responsibility of overseeing, among other things, the assets of the corporation. This is an important function that Dr. Szerszen did not acknowledge in her testimony. The utility and executive management class costs that she challenged are reasonable and necessary costs that are allocated to ETI based on a logical allocator – the assets the executives are charged with overseeing. The ALJs recommend that OPC's challenge be rejected.

2. Projects F5PCZUBENQ (Non-Qualified Post-Retirement) and F5PPZNQBUDU (Non-Qual Pension/Benf-Dom Utl)

With respect to Projects F5PCZUBENQ and F5PPZNQBUDU, Dr. Szerszen testified that: (1) there is no evidence that Texas ratepayers benefit from the pension-related benefits in these codes; and (2) the LBRBILAL allocator (Labor Billings to All) is not appropriate because the benefits are unrelated to ESI labor costs.⁷⁶⁶

⁷⁶⁴ OPC Ex. 1 (Szerszen Direct) at 56.

⁷⁶⁵ ETI Ex. 4 (Domino Direct) at 18-38; ETI Ex. 69 (Tumminello Rebuttal) at 9-11.

⁷⁶⁶ OPC Ex. 1 (Szerszen Direct) at 68.

Initially, ETI agrees that \$112,531 of the costs in total for both of these project codes should be excluded because that amount is attributable to nuclear and non-regulated employees.⁷⁶⁷

With respect to the remaining costs, ETI disagrees. The ALJs, however, have already resolved this issue in their discussions related to Section VII.D.4, above, where they concluded that that the supplemental executive retirement plans are not reasonable and necessary for the provision of electric utility service and are not in the public interest. Accordingly, the ALJs recommend the Commission accept OPC's proposed disallowance of \$356,151 (which includes the \$112,531 agreed to by ETI).

J. Information Technology Class

Dr. Szerszen recommended disallowances in two project codes that are primarily within ETI's Information Technology Class: (1) F3PPFXERSP (Evaluated Receipts Settlement) for a disallowance of \$10,279; and (2) F3PCFX3555 (BOD/Executive Support) for a disallowance of \$3,148.⁷⁶⁸

1. F3PPFXERSP (Evaluated Receipts Settlement)

Dr. Szerszen testified that Project F3PPFXERSP is not moving forward due to tax and freight implications and, as such, the cost is not recurring.⁷⁶⁹ Ms. Tumminello testified in response that the "Evaluated Receipt Settlement" program was originally being capitalized in a capital project. But when it was decided that the program would be cancelled, the capital project was closed and the charges to the project were expensed. Although the costs for this particular project do not recur every year, they are part of normal utility operations, and this type of project does recur as necessary.⁷⁷⁰

⁷⁶⁷ ETI Initial Brief at 179.

⁷⁶⁸ OPC Ex. 1 (Szerszen Direct) at 56, 71.

⁷⁶⁹ OPC Ex. 1 (Szerszen Direct) at 71.

⁷⁷⁰ ETI Ex. 69 (Tumminello Rebuttal) at SBT-R-2 at 4.

Although the ALJs understand the concept of normally recurring cost types, they do not believe that the costs captured by this project code fall within that category. Those costs related to a project that was cancelled and sufficient explanation of how similar projects in the future might occur was not provided. Accordingly, the ALJs recommend the Commission reject inclusion, as proposed by OPC.

2. Project F3PCFX3555 (BOD/Executive Support)

Dr. Szerszen argued that Project F3PCFX3555 is an executive-related project that does not provide perceivable benefits to ETI ratepayers, the Entergy shareholders should bear this cost, and an assets-based allocator is not appropriate.⁷⁷¹

ETI argues that the functions covered by this project code relate to the oversight of all system operations and the stewardship of corporate assets and that because ETI is part of a corporate group, the allocated charges associated with these services are relevant to ETI as part of that group of companies. Furthermore, ETI argues, the asset-based allocator is appropriate because it reflects the cause of the costs incurred, in that services provided relate to the stewardship of all the corporation's assets.⁷⁷²

A corporation cannot function without executives who are charged with the responsibility of overseeing, among other things, the assets of the corporation. This is an important function that Dr. Szerszen did not acknowledge in her arguments. The utility and executive management class costs that she challenged are reasonable and necessary costs that are allocated to ETI based on a logical allocator – the assets the executives are charged with overseeing. The ALJs recommend that OPC's challenge be rejected.

K. Internal and External Communications Class

Dr. Szerszen recommended disallowances in four project codes that are primarily within ETI's Internal and External Communications Class: (1) F3PCR40118 (Utility Communications for a

⁷⁷¹ OPC Ex. 1 (Szerszen Direct) at 56.

⁷⁷² ETI Ex. 4 (Domino Direct) at 18-38; ETI Ex. 69 (Tumminello Rebuttal) at 9-11.

\$6 disallowance; (2) F5PCZPDEPT (Supervision and Support – Public) for a \$138 disallowance; (3) F5PPICC000 (Integrated Customer Communications) for a \$199 disallowance; and (4) F5PPICCEMP (ICC - Employee Education Initiative) for a \$3 disallowance.⁷⁷³

ETI witness Tumminello responded to Dr. Szerszen's claim that the costs captured by these project codes are corporate image costs by stating that the costs are for advertising activities that are of a good will or institutional nature, which is primarily designed to improve the image of the utility or the industry, including advertisement which inform the public concerning matters affecting the Company's operations, such as, the costs of providing service, the Company's efforts to improve the quality of service, the Company's efforts to improve and protect the environment. According to FERC, such costs are properly includable in FERC Account 930.1 and are recoverable. According to Ms. Tumminello, as contemplated by FERC, the fact that ETI is a monopoly has no bearing on the recoverability of these costs.⁷⁷⁴

OPC provided little support for its claim that costs covered by these project codes should not be recoverable, essentially limiting the basis to the contention that ETI is a monopoly and ratepayers should not be charged with such costs. ETI did little better, but it did provide the testimony of Ms. Tumminello, which confirms that the costs are properly includable in FERC Account 930.1 and are, therefore, recoverable. In the end, the ALJs must go with the weight of the evidence, which is in ETI's favor. The ALJs recommend the Commission reject OPC's contention that costs covered by these project codes are not recoverable.

L. Legal Services Class

Dr. Szerszen recommended disallowances in 13 project codes that are primarily within the Legal Services Class: (1) F3PPCASHCT (Contractual Alternative/Cashpo) for a disallowance of \$2,553; (2) F3PCF99180 (CORP. COMPLIANCE TRACKING SYS) for a disallowance of \$9; (3) F3PPINVDOJ (DOJ Anti Trust Investigation) for a disallowance of \$1,039,664;⁷⁷⁵

⁷⁷³ OPC Ex. 1 (Szerszen Direct) at 66.

⁷⁷⁴ ETI Ex. 69 (Tumminello Rebuttal) at SBT-R-2 at 4-6.

⁷⁷⁵ Dr. Szerszen also proposed disallowance of \$765 in charges for related Project Code F3PPTDHY19

(4) F3PCE01601 (Ferc - Open Access Transmission) for a disallowance of \$84,183; (5) F3PCERAKTL (RAKTL Patent Matter) for a disallowance of \$75; (6) F3PPEASTIN (Willard Eastin et al) for a disallowance of \$19,714; (7) F3PPTCGS11 (TX Docket Competitive Generation) for a disallowance of \$310,746; (8) F5PCE13759 (Jenkins Class Action Suit) for a disallowance of \$205,107; (9) F5PCZLDEPT (Supervision & Support – Legal) for a disallowance of \$225,794; (10) F3PCCDV DAT (Corporate Development Data Room) for a disallowance of \$6,147; (11) F3PCSYSAGR (System Agreement-2001) for a disallowance of \$880,841; (12) F3PPWET302 (SPO 2008 Winter Western Region) for a disallowance of \$13,919; and (13) F3PPWET308 (SPO Calpine PPA/Project Houston) for a disallowance of \$435,963.

1. Project F3PPCASHCT (Contractual Alternative/Cashpo)

With respect to Project F3PPCASHCT (\$2,553 disallowance), ETI agrees that these costs are non-recurring and should be disallowed. Accordingly, the ALJs recommend the Commission exclude those costs.

2. Project F5PCZLDEPT (Supervision & Support – Legal)

As to Project F5PCZLDEPT (\$225,794), OPC, through its Second Errata, removed that proposed disallowance, and it is no longer contested by Dr. Szerszen. Accordingly, the ALJs recommend the Commission approve inclusion of those costs.

3. Project F3PCF99180 (Corp. Compliance Tracking Sys)

F3PCF99180 (Corp. Compliance Tracking Sys) is one of the project codes that Dr. Szerszen claimed should be disallowed because ETI is a monopoly and Texas ratepayers should not have to pay for corporate image costs.⁷⁷⁶

(Dept. of Justice Investigation), which is actually primarily attributable to the Transmission Operations Class, rather than the Legal Services Class. Because the issues are intertwined, that project will be discussed here, rather than in the Transmission Operations Class.

⁷⁷⁶ OPC Ex. 1 (Szerszen Direct) at 66.

ETI witness Tumminello testified that these costs are for advertising activities that are of a good will or institutional nature, which is primarily designed to improve the image of the utility or the industry, including advertisement which inform the public concerning matters affecting the Company's operations, such as, the costs of providing service, the Company's efforts to improve the quality of service, the Company's efforts to improve and protect the environment. According to FERC, such costs are properly includable in FERC Account 930.1 and are recoverable. According to Ms. Tumminello, as contemplated by FERC, the fact that ETI is a monopoly has no bearing on the recoverability of these costs.⁷⁷⁷

OPC provided little support for its claim that costs covered by these project codes should not be recoverable, essentially limiting the basis to the contention that ETI is a monopoly and ratepayers should not be charged with such costs. ETI did little better, but it did provide the testimony of Ms. Tumminello, which confirms that the costs are properly includable in FERC Account 930.1 and are, therefore, recoverable. The weight of the evidence is in ETI's favor. The ALJs recommend the Commission reject OPC's contention that costs covered by these project codes are not recoverable.

4. Projects F3PPINVDOJ (DOJ Anti Trust Investigation) and F3PPTDHY19 (Dept. of Justice Investigation)

Entergy is currently under investigation by the Department of Justice (DOJ) for certain business practices of the Operating Companies, including the procurement of generating assets and power, dispatch of generation within the Entergy system, and transmission capacity expansion. This is a civil investigation under Section 2 of the Sherman Act and Section 7 of the Clayton Act. The investigation has been ongoing since 2010, and Entergy does not know when the investigation will conclude.⁷⁷⁸

Dr. Szerszen testified that there are two reasons why ratepayers should not pay for the DOJ expenses. First, ETI does not have the ability to make its own power procurement, generation dispatch, or transmission capacity decisions. These decisions are made by ESI and Entergy's

⁷⁷⁷ ETI Ex. 69 (Tumminello Rebuttal) at SBT-R-2 at 4-6.

⁷⁷⁸ OPC Ex. 1 (Szerszen Direct) at 51-52.

corporate management, which has traditionally planned and managed the electric operating companies' generation and transmission functions on a system-wide basis. Second, ETI is not responsible for the development and administration of the system agreement, and should not be held responsible for these antitrust investigation expenses. Furthermore, according to Dr. Szerszen, if the DOJ finds that Entergy has acted illegally, it is even more inappropriate to charge ETI ratepayers for corporate-level illegal actions. These expenses should be borne by Entergy's corporate parent and/or the corporation's shareholders, and not the ratepayers.⁷⁷⁹

ETI contends that Dr. Szerszen fundamentally misunderstands the nature of the System Agreement and the benefits that ETI derives from that agreement. All of the Entergy Operating Companies voluntarily entered into the System Agreement so that the Entergy system can be planned and operated on a total system basis, in order to maximize economic benefit and reliability of service. All of the Operating Companies benefit from integrated planning and operations in this manner. This does not mean that ETI has no decision-making role in these activities. ETI notes that under Section 5.01 of the System Agreement, the agreement is administered through an Operating Committee, which includes an ETI representative, as well as representatives of the other Operating Companies and Entergy. ETI's representative is one of the voting members of the Committee, and all decisions of the Operating Committee must be approved by a majority vote. As a voting member of the Operating Committee, ETI is responsible for administering the System Agreement and does participate in decision-making on generation and transmission matters.⁷⁸⁰

ETI acknowledges that ESI is tasked with providing services and making decisions related to generation dispatch, power procurement, and transmission operations on behalf of the Entergy Operating Companies and at the direction of the Operating Committee, but these activities are for the benefit of the Operating Companies and their ratepayers. ETI receives the benefits of these services and integrated planning and operations under the System Agreement and, according to ETI, should also be responsible for its portion of costs related to those services and operations.⁷⁸¹

⁷⁷⁹ *Id.* at 52.

⁷⁸⁰ ETI Ex. 65 (Sloan Rebuttal) at 8.

⁷⁸¹ *Id.*

As to Dr. Szerszen's contention that the costs should be disallowed because DOJ might find that Entergy acted illegally, ETI notes that the DOJ is not an adjudicatory body or regulatory agency and, thus, it does not make "findings of fact." If DOJ believes the civil antitrust laws have been violated, it can file a complaint in federal district court. To date, no complaint has been filed. ETI points out that ESI routinely incurs legal costs in responding to regulatory audits and investigations on behalf of ETI and the other Operating Companies in the same manner in which other operating costs are incurred. ESI is authorized to retain legal counsel on behalf of, and for the benefit of, ETI and the other Entergy Operating Companies. ESI is authorized to allocate the respective costs to the Operating Companies under a service agreement with the Entergy Operating Companies designated as Rate Schedule FERC No. 435. This service agreement is on file with, and was approved by, FERC under FERC Docket No. ER07-38-000.⁷⁸² Thus, according to ETI, it is appropriate that ETI is allocated its share of the costs of legal services related to the DOJ investigation.⁷⁸³

The DOJ antitrust investigation is a massive undertaking. Unfortunately, it is a part of the ordinary course of modern business life. OPC's arguments that ESI is solely responsible for decision-making under the System Agreement miss the mark, as pointed out by ETI. It is clear that ETI and the other Operating Companies play an active role in the decision-making. As to OPC's arguments about what would happen if Entergy were found to have violated the antitrust laws, those arguments are little more than speculation. As ETI noted, the DOJ is not an adjudicatory body and its investigation can only result in the filing of a complaint in Federal court (if the DOJ believes that such an action is justified). Until that time, it is imperative for the company to fully respond to the DOJ investigation. The ALJs find that ETI has met its burden of proving that Texas ratepayers should be charged the costs of the DOJ investigation allocated to them by ETI.

5. Project F3PCE01601 (Ferc - Open Access Transmission)

Project F3PCE01601 costs are incurred to manage costs associated with regulatory oversight and coordination of the Entergy System Open Access Transmission Service before FERC. OPC contends that not only are most of the FERC dockets accruing costs under Project F3PPEO1601 no

⁷⁸² *Entergy Serv. Inc.*, 117 FERC ¶ 61,288 (2006).

⁷⁸³ ETI Ex. 65 (Sloan Rebuttal) at 8-9.

longer open as of December 31, 2011,⁷⁸⁴ most of the closed dockets have absolutely nothing to do with Texas operations.⁷⁸⁵ Furthermore, according to OPC, ETI witness Sloan agreed that only three of the dockets shown in OPC Exhibit No. 12 were open at the end of the test year, and one of the open dockets involves a transmission service agreement involving the Missouri Joint Municipal Electric Utility Commission and various cities in Missouri and Arkansas.⁷⁸⁶

ETI responds that the activities in this project relate to oversight and coordination of the OATT proceedings before the FERC. Costs billed to this project code are related to ESI's representation of the Operating Companies, including ETI, before the FERC on OATT issues. Revenues derived from provision of service under the OATT are credited to all of the Operating Companies on a load responsibility ratio basis. ETI's retail share of these revenues was \$168,366 during the test period, demonstrating the benefits derived by Texas ratepayers as a result of the activities undertaken through this project code.⁷⁸⁷

Activities relating to a company's OATT are not one-time activities; they will continue from year to year. OPC's contention that because most of the dockets listed as having taken place during the Test Year were completed by the end of the Test Year they should be disregarded is not well-founded. It is clear that the activities covered by this project code not only benefit ETI's Texas ratepayers, but will continue (albeit under new docket numbers) into future years. The ALJs recommend that costs under this project code be allowed.

⁷⁸⁴ OPC Ex. 12 (OPC RFI No. 7-3); OPC Ex. 3 (Szerszen Workpapers) at 363.

⁷⁸⁵ OPC Ex. 12 (OPC RFI No. 7-3); OPC Ex. 1 (Szerszen Direct) at 54.

⁷⁸⁶ Tr. at 280.

⁷⁸⁷ ETI Ex. 65 (Sloan Rebuttal) at 10.

6. Project F3PCERAKTL (RAKTL Patent Matter)

The costs under this project code involve the RAKTL patent, which relates to call center operations. RAKTL is a patent infringement claim lodged against several Entergy companies. The alleged patents are for voice prompting technology used in call centers.⁷⁸⁸

Dr. Szerszen testified that it is not appropriate to charge ETI for the costs associated with this litigation because ETI did not purchase the call center telephone equipment at issue, and therefore should not be required to pay any legal costs associated with patent infringement investigation or settlement costs. ESI is totally responsible for system-wide technology purchases and operations, and, according to Dr. Szerszen, it is not reasonable to require the operating companies to pay legal costs associated with ESI technology acquisition or technology application errors.⁷⁸⁹

ETI contends that ESI incurred the legal expenses on this patent matter on behalf of the Entergy Operating Companies, whose residential and small commercial customers call into the call centers to obtain customer service for issues related to connection and disconnection of electric service, billing issues, and other customer transactions. The call centers provide an interface between ETI customers and the Entergy Operating Companies and, as such, are valuable in providing quality service to customers. Consequently, according to ETI, costs related to the call centers, including the costs of defending lawsuits involving technologies used at those call centers, is a reasonable and necessary expense that is appropriately allocated to ETI.⁷⁹⁰

OPC tends to ignore the purpose and benefits of a centralized service company such as ESI. If ETI were to fund stand-alone call centers, it is likely that the costs to Texas ratepayers would be higher than those proposed by ETI in this case. Part of the costs that ESI incurs is the cost of patent claims. Those are legitimate costs that should be borne by all who receive service from ESI. Accordingly, the ALJs recommend the Commission reject OPC's challenge.

⁷⁸⁸ *Id.* at 4; OPC Ex. 1 (Szerszen Direct) at 49-50.

⁷⁸⁹ OPC Ex. 1 (Szerszen Direct) at 50.

⁷⁹⁰ ETI Ex. 65 (Sloan Rebuttal) at 4.

7. Project F3PPEASTIN (Willard Eastin *et al.*)

This project code, which contains costs in the amount of \$19,714, collects costs related to an age discrimination law suit filed by Willard Eastin, *et al.* against Entergy. The defendants to the lawsuit were Entergy, ESI, Entergy Louisiana, Inc. (ELL), and Entergy New Orleans, Inc. (ENOI). The plaintiffs to the lawsuit were employees of ESI, ELL, and ENOI.⁷⁹¹

OPC witness Szerszen testified that ETI should not be required to pay any of the costs of this litigation. Although ESI provides services to the Operating Companies, this does not imply that the Operating Companies should be charged costs associated with the service company's employment practice problems or errors according to Dr. Szerszen.⁷⁹²

ETI argues that costs are driven by ESI having the need for legal services to defend itself. As shown on the Project Code Summary for this project, since all ESI functions are in service to the various affiliates and arise as a consequence of providing such services, it is appropriate to relate these legal costs to the total ESI billings to the affiliates.⁷⁹³

ETI has provided little in the way of explanation regarding these costs or the litigation that generated them. What is troubling to the ALJs is that the only named defendants are Entergy, ESI, ELL, and ENOI; ETI is not included among the named defendants. If this were simply a cost of doing business for ESI, as claimed by ETI, why were ELL and ENOI named? No explanation was offered. It appears to the ALJs that although this litigation is related to ESI's operations, it is more immediately related to ELL and ENOI. The ALJs do not believe that ETI's Texas ratepayers should be charged for these costs; therefore the ALJs recommend that \$19,714 not be included.

⁷⁹¹ ETI Ex. 65 (Sloan Rebuttal) at 2; OPC Ex. 1 (Szerszen Direct) at 49-50.

⁷⁹² OPC Ex. 1 (Szerszen Direct) at 50.

⁷⁹³ ETI Ex. 65 (Sloan Rebuttal) at 2.

8. Project F3PPTCGS11 (TX Docket Competitive Generation)

The costs billed through this project code all pertain to ETI's CGS matter currently pending before the Commission in Docket No. 38951.⁷⁹⁴

OPC witness Szerszen testified that because no decision has been made yet as to the disposition of the expenses associated with the CGS tariff, ETI should not be expensing the costs associated with that docket. Dr. Szerszen disallowed \$310,746 in Test-Year expenses, and recommended that ETI be allowed to defer the expenses until the Commission determines the appropriate regulatory treatment.⁷⁹⁵

ETI argues that these costs were incurred during the Test Year in a pending Commission docket, and ETI continues to incur costs related to this matter. As such, according to ETI, these costs are appropriately included in ETI's cost of service and should neither be disallowed nor deferred.⁷⁹⁶

OPC's arguments with respect to these costs are not well-founded. It appears to be likening these regulatory costs to rate case expense, which would be subject to Commission review and approval in the proceeding to which they relate. But that is not the nature of these expenses. They are simply regulatory expenses incurred in the course of ongoing regulatory proceedings. They are ordinary and necessary expenses, the reasonableness of which OPC did not challenge. Accordingly, the ALJs find that it is appropriate for ETI to charge these expenses to its Texas ratepayers.

9. Project F5PCE13759 (Jenkins Class Action Suit)

The project code relates to a class action lawsuit filed in Texas District Court in 2003 on behalf of all Texas retail customers served by ETI's predecessor-in-interest, EGSi (Jenkins Class Action). The Jenkins Class Action plaintiffs allege that they have been damaged due to manipulation of the dispatch and pricing of the Entergy system's generating units and electricity

⁷⁹⁴ *Id.* at 5; OPC Ex. 1 (Szerszen Direct) at 50.

⁷⁹⁵ OPC Ex. 1 (Szerszen Direct) at 50.

⁷⁹⁶ ETI Ex. 65 (Sloan Rebuttal) at 5.

purchases. As a result of this alleged manipulation, they contend that ETI's Texas retail customers were charged more than they should have been for purchased power.⁷⁹⁷ Dr. Szerszen asserted there are three reasons why these legal expenses should not be borne by ETI:

- ESI charges 100 percent of the legal expenses to ETI, even though ETI is only one of several defendants;
- ETI claims that it is defending practices relating to system operations, but fails to acknowledge that Entergy's system operations are comprised of many generation and transmission components other than those of ETI; and
- ETI does not have any authority to administer the System Agreement, that being a function solely within the purview of ESI.⁷⁹⁸

Dr. Szerszen testified that "[i]t would be more appropriate for the Entergy parent to be charged for these lawsuit expenses, particularly since ETI cannot make unilateral power purchases and power sales decisions."⁷⁹⁹

ETI responds that the plaintiffs in this lawsuit are challenging the reasonableness of ETI's Commission-set rates and that the Commission has filed an *amicus* brief in support of ETI's position in the case. ETI further argues that retail ratepayers are benefitting from ETI's pursuit of the litigation because ETI is defending practices that are in place to ensure the lowest reasonable cost consistent with system reliability. Finally, ETI states that the costs are reasonable and necessary expenses because the plaintiffs purport to represent only ETI's ratepayers and seek to recover damages inconsistent with ETI's filed rates approved by the Commission.⁸⁰⁰

The ALJs understand Dr. Szerszen's concerns that there are multiple defendants involved in this litigation, there are many aspects to Entergy's system operations, and ETI does not have power to unilaterally make decisions under the System Agreement. The crucial point, however, is that

⁷⁹⁷ OPC Ex. 1 (Szerszen Direct) at 49; ETI Ex. 65 (Sloan Rebuttal) at 2-3.

⁷⁹⁸ OPC Ex. 1 (Szerszen Direct) at 49.

⁷⁹⁹ *Id.*

⁸⁰⁰ ETI Ex. 65 (Sloan Rebuttal) at 3.

these are Texas ratepayers pursuing a challenge to ETI's Texas rates. The matter centers around Texas, and the costs of the litigation should be borne by Texas ratepayers.

10. Project F3PCSYSAGR (System Agreement-2001)

OPC witness Szerszen disallowed \$880,841 in legal expenses regarding the 2001 complaint filed by the Louisiana Public Service Commission and the City of New Orleans seeking revisions to the Entergy System Agreement.⁸⁰¹ OPC states that it generally agrees with ETI witness Sloan that the complaint challenges the equalization of costs between all Entergy Operating Company jurisdictions.⁸⁰² However, OPC does not agree that the inquiry "will" affect all Entergy jurisdictions.

Texas has benefitted from the complaint primarily through the past receipt of equalization payments pursuant to FERC's decision in this complaint matter. However, Entergy's SEC Form 10-K shows that for 2012 and 2013, ETI will receive no equalization payments, and further shows that ETI received no rough production cost equalization payments in 2010.⁸⁰³ Thus, according to OPC, the legal expenses sought to be recovered under Project F3PCSYSAGR are non-recurring for ETI and therefore not representative of future costs and should be removed from ETI's cost of service.⁸⁰⁴

ETI established that this litigation involved the System Agreement, which governs the equalization of costs between all of the Entergy Operating Company jurisdictions, it provides benefits to ETI's Texas ratepayers as well as those of the other Entergy Operating Companies. OPC's argument that ETI did not receive equalization payments in 2010 and is non-recurring for ETI does not overcome the benefits received by ETI's Texas ratepayers. The ALJs recommend that OPC's disallowance be denied.

11. Project F3PCCDVDAT (Corporate Development Data Room)

ETI requests the recovery of \$6,147 in ESI allocated costs for the corporate development data room. The stated purpose of the data room is for due diligence reviews associated with Entergy

⁸⁰¹ OPC Ex. 1 (Szerszen Direct) at 53.

⁸⁰² ETI Ex. 65 (Sloan Rebuttal) at 9.

⁸⁰³ ETI Ex. 98 (Entergy's SEC Form 10-K) at 79-80.

⁸⁰⁴ OPC Ex. 1 (Szerszen Direct) at 52-53.

merger, acquisition, or diversification activities. The expenses associated with the corporate development data room are for the gathering, collating, indexing, manning, and storage of data during the due diligence reviews.⁸⁰⁵ OPC contends that the costs incurred for the corporation's analysis of merger, acquisition, and diversification opportunities should not be charged to ETI's ratepayers. Entergy has not acquired any utilities or utility operations that might produce system-wide benefits to utility customers.⁸⁰⁶ The \$6,147 of expenses for the corporate development room are not reasonable and necessary expenses that ratepayers should shoulder and therefore, according to OPC, recovery of these expenses should be disallowed.

ETI responds that these costs are driven by each company's need for corporate services and the costs, therefore, are appropriately allocated based on the level of service provided by ESI, which is a reasonable proxy of each company's need for corporate services.⁸⁰⁷ Further, just because Entergy has not acquired any utility or utility operations in the recent past does not mean that these are not reasonable and necessary costs. Entergy points out that as Dr. Szerszen noted in her description of this project, it is not only for the acquisition of other operating units, but also used to analyze diversification activities, which is a legitimate and reasonable undertaking by an integrated utility and its parent company.

The ALJs believe that there are legitimate costs that may not on their face appear to be properly allocable to entities such as ETI, but on closer examination they merit such an allocation. These fall into that class. As Ms. Tumminello testified, the Corporate Development Data Room includes costs not only related to mergers and acquisitions, but also diversification activities that could benefit ETI ratepayers. Accordingly, they are properly allocated to ETI ratepayers.

⁸⁰⁵ OPC Ex. 3 (Szerszen Workpapers) at 394.

⁸⁰⁶ OPC Ex. 1 (Szerszen Direct) at 45-46.

⁸⁰⁷ ETI Ex. 69 (Tumminello Rebuttal) Ex. SBT-R-2 at 1.

12. Project F3PPWET302 (SPO 2008 Winter Western Region)

Dr. Szerszen argued that Project F3PPWET302 costs should be disregarded because they were incurred during the 2008-2009 period, which is outside of the Test Year, and they are nonrecurring.⁸⁰⁸

ETI witness Cicio explained that although this project was initiated prior to the Test Year, the costs that the Company seeks to recover through this project code were expenses incurred during the Test Year. These costs included development activities, requests for proposal issuance, bidders' conferences, written and posted questions and answers from market participants and other interested parties, submission of proposals, screening of proposals, proposal evaluation, follow-up questions and clarifications, recommendations and awards, contract negotiations, Independent Monitor reports, and regulatory approvals, if necessary. He stated that these types of costs routinely encompass a multi-year time frame, and the costs required to perform those activities, although associated with a project that may have been initiated several years previously, are properly incurred over the life span of the project. He also stated that they are recurring because they reflect the kinds and levels of charges that would be expected to be incurred on an ongoing basis in association with request for proposals managed by ESI on behalf of the Entergy Operating Companies, and the Company has been involved in these types of solicitations since 2002.⁸⁰⁹

The ALJs find that the costs captured by Project F3PPWET302 were incurred during the Test Year and represent the kinds and levels of costs routinely incurred on a recurring basis. Accordingly, the ALJs recommend the Commission approve their inclusion as requested by ETI.

⁸⁰⁸ OPC Ex. 1 (Szerzen Direct) at 65.

⁸⁰⁹ ETI Ex. 45 (Cicio Rebuttal) at 13-14.

13. Project F3PPWET308 (SPO Calpine PPA/Project Houston)

With respect to Project F3PPWET308, which deals with the Calpine-Carville purchased power agreement, Dr. Szerszen testified that the costs were either non-recurring, or rate case expenses, or expenses that should have been charged to Louisiana ratepayers.⁸¹⁰

ETI witness Cicio explained that these are recurring costs because they reflect the kinds and levels of charges that the Company expects to incur on an ongoing basis in association with RFPs managed by ESI on behalf of the Entergy Operating Companies; they were not incurred as part of some rate case preparation and, therefore, are not a rate case expense that is otherwise sought for recovery by ETI; and the costs in the matter are costs that were billed only to Texas and should not have been billed to Louisiana because there is a separate project code that captures the Louisiana costs that are billed to Louisiana.⁸¹¹

The ALJs find that these costs, like those captured by Project F3PPWET302, are recurring in that they represent the kinds and levels of costs routinely incurred on a year-in and year-out basis. Further, the ALJs find that the costs should not have been charged to Louisiana and that there existed a separate project code to capture costs attributable to Louisiana. Accordingly, the ALJs recommend the Commission approve the inclusion of these costs as requested by ETI.

M. Other Expenses Class

Dr. Szerszen recommended disallowances in 11 project codes that are primarily within the Other Expenses Class of affiliate costs: (1) F3PCSPETEI (Entergy-Tulane Energy Institute) for a disallowance of \$14,288; (2) F3PCC08500 (Executive VP, Operations) for a disallowance of \$4,117; (3) F3PPBFMESI (ESI Function Migration Relocation) for a disallowance of \$4,187; (4) F3PPBFRESI (ESI Business Function Relocation) for a disallowance of \$11,444; (5) F3PPDRPESI (ESI Disaster Recovery Plan Charge) for a disallowance of \$761; (6) F5PPBFMREL (Business Function Migration Employee) for a disallowance of \$33,624;

⁸¹⁰ OPC Ex. 1 (Szerszen Direct) at 65-66.

⁸¹¹ ETI Ex. 45 (Cicio Rebuttal) at 14-17.

(7) F5PPBFRREL (Business Function Relocation) for a disallowance of \$15,624; (8) F5PPBFRSEV (Business Function Relocation Severance) for a disallowance of \$3,066; (9) F5PPDRPREL (Disaster Recovery Plan Relocation) for a disallowance of \$31,006; (10) F5PPETXRFI (2009 Texas Ike Recovery Filing) for a disallowance of \$441; and (11) F5PPKATRPT (Storm Cost Processing & Review) for a disallowance of \$929.⁸¹²

1. Projects F3PCSPETEI (Entergy-Tulane Energy Institute) and F5PPKATRPT (Storm Cost Processing & Review)

ETI agrees with Dr. Szerszen that the \$14,288 amount she proposed to disallow for Project F3PCSPETEI (Entergy-Tulane Energy Institute) can be treated as a donation, and so should be removed from ETI's cost of service. ETI also agrees with Dr. Szerszen to remove the \$929 billed to ETI under Project F5PPKATRPT (Storm Cost Processing & Review). The charges for the remaining nine project codes, however, are contested.

2. Project F3PCC08500 (Executive VP, Operations)

As to Project F3PCC08500 (Executive VP Operations), Dr. Szerszen testified that an asset-based allocator is not appropriate for these types of executive management costs, and there is "no perceivable benefit" to ETI ratepayers for these types of allocated costs.⁸¹³

Ms. Tumminello disagreed, stating that asset-based allocation methods are selected for projects where the costs are driven by the oversight and stewardship of corporate assets of the Entergy Companies including, but not limited to, services provided by financial management and certain finance functions, among others. Each Entergy affiliate with assets on Entergy's consolidated balance sheet will be billed their proportionate share of the costs. The use of the Total Assets allocation method is, in fact, an appropriate method to allocate corporate-level corporate governance type services.⁸¹⁴

⁸¹² OPC Ex. 1 (Szerszen Direct) at 56, 67, and 72.

⁸¹³ *Id.* at 56-57.

⁸¹⁴ ETI Ex. 69 (Tumminello Rebuttal) at 9-10.

The ALJs find credible ETI's assertion that the costs captured by this project code are for oversight and stewardship of the corporate assets of Entergy and, therefore, an asset-based allocator is appropriate. Accordingly, the ALJs recommend the Commission reject OPC's challenge to the inclusion of these costs.

3. Projects F3PPBFMESI (ESI Function Migration Relocation), F3PPBFRESI (ESI Business Function Relocation), F3PPDRPESI (ESI Disaster Recovery Plan Charge), F5PPBFMREL (Business Function Migration Employee), F5PPBFRREL (Business Function Relocation), F5PPBFRSEV (Business Function Relocation Severance), F5PPDRPREL (Disaster Recovery Plan Relocation), and F5PPETXRFI (2009 Texas Ike Recovery Filing)

The remaining eight of the project codes attributable to the Other Expenses Class all deal with system restoration and business continuity resulting from Hurricane Katrina, with one applying to Hurricane Ike. Dr. Szerszen testified that these costs should be disallowed because they should not be considered to be system restoration costs or, if they are, citing to PURA § 36.405, ETI should have requested recovery of these costs in its first base rate following Hurricane Katrina (Docket No. 34800). She also testified that ETI has not shown that Texas ratepayers benefited from these costs.⁸¹⁵

Ms. Tumminello testified that because of the magnitude of Hurricane Katrina, these expenses were necessary so that activities in connection with the restoration of service and infrastructure associated with electric power outages affecting customers could continue. These expenses relate to critical functions needed to support storm restoration, such as business function relocation, and provided a direct benefit to ratepayers. Ms. Tumminello stated that the costs in seven of these project codes (F3PPBFMESI, F3PPBFRESI, F3PPDRPESI, F5PPBFMREL, F5PPBFRREL, F5PPBFRSEV, and F5PPDRPREL) are being amortized over five years. Though these particular costs do not recur every year, they are a part of ETI's normal utility operations given the service area served by ETI, and do recur as necessary.⁸¹⁶

⁸¹⁵ OPC Ex. 1 (Szertrzen Direct) at 72, Schedule CAS-14.

⁸¹⁶ ETI Ex. 69 (Tumminello Rebuttal) at 16.