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Filing Date - 2024-05-15 03:16:28 PM

Control Number - 56211

Item Number - 218

SOAH DOCKET NO. 473-24-13232
PUC DOCKET NO. 56211

APPLICATION OF CENTERPOINT ENERGY HOUSTON ELECTRIC, LLC FOR AUTHORITY TO CHANGE RATES	**§ § §**	**BEFORE THE STATE OFFICE OF ADMINISTRATIVE HEARINGS**

May 15, 2024

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- **Please note that the discovery responses were prepared under the direction of the sponsors.**

CENTERPOINT ENERGY HOUSTON ELECTRIC, LLC
PUC DOCKET NO. 56211
SOAH DOCKET NO. 473-24-13232

IBEW Local 66
REQUEST NO.: IBEW-RFI01-01

QUESTION:

Identify the name, address, and title of each witness you intend to sponsor at the hearing on the merits and summarize the testimony s/he will present.

ANSWER:

Please refer to the Direct Testimony of Lynnae Wilson for a list of witnesses CenterPoint Houston intends to present at the hearing on the merits and a summary of the testimony they will present. This list may be updated during the course of the proceeeding.

SPONSOR:
Lynnae Wilson

RESPONSIVE DOCUMENTS:
None

CENTERPOINT ENERGY HOUSTON ELECTRIC, LLC
PUC DOCKET NO. 56211
SOAH DOCKET NO. 473-24-13232

IBEW Local 66
REQUEST NO.: IBEW-RFI01-02

QUESTION:

Identify and provide any documents that your witnesses will introduce, sponsor, or rely on.

ANSWER:

Pursuant to Texas Rules of Civil Procedure 194.2(b)(3), CenterPoint Houston is not required to marshall the evidence it intends to offer at trial. However, please refer to the direct testimony of each of CenterPoint Houston's witnesses, which identify what materials they are currently sponsoring, including rate filing package schedules, attachments to testimony, and work papers. Please also refer to CenterPoint Houston's response to Question No. IBEW 1-03.

SPONSOR:
Lynnae Wilson

RESPONSIVE DOCUMENTS:
None

CENTERPOINT ENERGY HOUSTON ELECTRIC, LLC
PUC DOCKET NO. 56211
SOAH DOCKET NO. 473-24-13232

IBEW Local 66
REQUEST NO.: IBEW-RFI01-03

QUESTION:

Identify each expert you expect to call to testify at the hearing on the merits. For each testifying expert provide:

a. the expert's name, address, and telephone number;
b. the subject matter(s) on which the expert will testify;
c. the facts known by the expert that relate to or form the basis of the expert's mental impressions and opinions formed or made in connection with this case;
d. the expert's mental impressions and opinions formed or made in connection with the case, and any methods used to derive them;
e. any bias of the witness;
f. all documents, tangible things, reports, models, or data compilations provided to, reviewed by , or prepared by or for the expert in anticipation of the expert's testimony; and
g. the expert's current resume and bibliography.

ANSWER:

The outside expert witnesses that CenterPoint Houston intends to have testify at the hearing on the merits are as follows:

- Ann Bulkley
- Stuart McMenamin
- Myles Reynolds
- Dane Watson
- Greg Wilson

These witnesses can be contacted through counsel for CenterPoint Houston, and the additional information requsted can be found in each witness's direct testimony, or attached thereto. Please refer to the attachment for documents reviewed by the above referenced experts. In addition, please refer to CenterPoint Houston's response to Question No. IBEW 1-2.

The attachments are voluminous and will be provided in electronic format only.

The attachments are confidential highly sensitive protected material being provided pursuant to the Protective Order issued in Docket No. 56211.

Confidential	Title	Expert Witness	Number of Pages	Page No(s)
n/a	IBEW RFI01-03 Billing Rate Ranges AG Directive and Case Law- M Reynolds.pdf	Myles Reynolds	1387	1-1387
n/a	IBEW RFI-1-03 2022 Survey of Law Firm Economics Results M Reynolds.xlsx	Myles Reynolds	455	1-455
n/a	IBEW RFI01-03 Rate Survey- M Reynolds.pdf	Myles Reynolds	7	1-7

The attachments are confidential and being provided pursuant to the Protective Order issued in Docket No. 56211.	IBEW RFI01-03 Peer Monitor Rates Report Jan-Dec 2022 - M Reynolds Confidential HSPM.xlxs	Myles Reynolds	52	1-52
	IBEW RFI01-03 Peer Monitor Rates Report Jan-Nov 2023 - M Reynolds Confidential HSPM.xlxs	Myles Reynolds	60	1-60
	IBEW RFI01-03 Email From Myles Reynolds Inbox Confidential.pdf	Myles Reynolds	8	1-8
	IBEW RFI01-03 PCR-CP Engagement Letter - My Reynolds Confidential.pdf	Myles Reynolds	4	1-4

SPONSOR:
Lynnae Wilson

RESPONSIVE DOCUMENTS:
Myles Reynolds
IBEW RFI01-03 Billing Rate Ranges AG Directive and Case Law- M Reynolds.pdf
IBEW RFI-1-03 2022 Survey of Law Firm Economics Results M Reynolds.xlsx
IBEW RFI01-03 Rate Survey- M Reynolds.pdf
IBEW RFI01-03 Peer Monitor Rates Report Jan-Dec 2022 - M Reynolds Confidential HSPM.xlxs
IBEW RFI01-03 Peer Monitor Rates Report Jan-Nov 2023 - M Reynolds Confidential HSPM.xlxs
IBEW RFI01-03 Email From Myles Reynolds Inbox Confidential.pdf
IBEW RFI01-03 PCR-CP Engagement Letter - My Reynolds Confidential.pdf

ARTHUR ANDERSEN & CO., Petitioner,

v.

PERRY EQUIPMENT CORPORATION, Respondent.

No. 95-0444.

Supreme Court of Texas.

Argued March 19, 1997.

Decided May 16, 1997.

Purchasing corporation sued accounting firm, alleging violations of Deceptive Trade Practices Act (DTPA) in connection with firm's preparation of audited financial statements of acquired corporation. The 55th District Court, Harris County, Kathleen S. Stone, J., entered judgment for purchasing corporation, and the Houston Court of Appeals, First District, 898 S.W.2d 914, affirmed. On writ of error, the Supreme Court, Cornyn, J., held that: (1) purchasing corporation was "consumer" under DTPA although it did not pay for audit; (2) failure to instruct jury on proper measure of direct damages was reversible error; and (3) award of attorney fees under DTPA had to be dollar amount, not percentage of judgment.

Reversed and remanded.

1. Consumer Protection ⇐1

For purposes of Deceptive Trade Practices Act (DTPA) claim against accounting firm, purchasing corporation was a "consumer," although it did not pay for audit, where purchasing corporation insisted as condition of sale that acquired corporation provide audited financial statements, acquired corporation hired accounting firm for that purpose, purchasing corporation then relied on those statements in reaching its decision to purchase acquired corporation, and accounting firm was aware that purchasing corporation had required audit and would rely on its accuracy and knew specific purpose for which it was conducted. V.T.C.A., Bus. & C. § 17.45(4).

See publication Words and Phrases for other judicial constructions and definitions.

2. Consumer Protection ⇐1

In determining whether plaintiff is consumer under Deceptive Trade Practices Act (DTPA), focus is on plaintiff's relationship to transaction. V.T.C.A., Bus. & C. § 17.45(4).

3. Consumer Protection ⇐40

Under Deceptive Trade Practice Act (DTPA), amount of actual damages recoverable is total loss sustained as result of deceptive trade practice. V.T.C.A., Bus. & C. § 17.50(b)(1).

4. Consumer Protection ⇐40

Under Deceptive Trade Practices Act (DTPA), actual damages are those damages recoverable under common law, either direct or consequential. V.T.C.A., Bus. & C. § 17.50(b)(1).

5. Damages ⇐16

Direct damages are necessary and usual result of defendant's wrongful act; they flow naturally and necessarily from the wrong.

6. Damages ⇐16

Direct damages compensate plaintiff for loss that is conclusively presumed to have been foreseen by defendant from his wrongful act.

7. Damages ⇐18

Consequential damages result naturally, but not necessarily, from defendant's wrongful acts; under common law, they need not be usual result of the wrong, but they must be foreseeable, and must be directly traceable to wrongful act and result from it.

8. Consumer Protection ⇐36.1

Foreseeability is not an element of producing cause under Deceptive Trade Practices Act (DTPA). V.T.C.A., Bus. & C. § 17.50(b)(1).

9. Consumer Protection ⇐40

Under Deceptive Trade Practices Act, if damages are too remote, too uncertain, or purely conjectural, they cannot be recovered. V.T.C.A., Bus. & C. § 17.50(b)(1).

10. **Fraud** ⇐59(2, 3)

Under common law, direct damages for misrepresentation are measured either by out-of-pocket damages, which measure difference between value buyer has paid and value of what he has received, or by benefit-of-the-bargain damages, which measure difference between value as represented and value received.

11. **Consumer Protection** ⇐40

Under Deceptive Trade Practices Act (DTPA), plaintiff may recover under damage theory that provides greater recovery, either out-of-pocket damages or benefit-of-the-bargain damages. V.T.C.A., Bus. & C. § 17.50(b)(1).

12. **Consumer Protection** ⇐40

Under Deceptive Trade Practices Act(DTPA), both out-of-pocket and benefit-of-the-bargain measure of damages are determined at time of sale. V.T.C.A., Bus. & C. § 17.50(b)(1).

13. **Appeal and Error** ⇐1067
Consumer Protection ⇐36.1

Failure to instruct jury on proper measure of direct damages on purchasing corporation's claim under Deceptive Trade Practices Act (DTPA) regarding accounting firm's audit of acquired corporation was reversible error, where jury was not asked to find direct damages at time of sale as well as consequential damages attributable to accounting firm's misrepresentations, but was simply asked to consider purchase price as part of overall damages, and purchasing corporation did not establish how much of its loss was attributable to accounting firm. V.T.C.A., Bus. & C. § 17.50(b)(1).

14. **Consumer Protection** ⇐40

Under Deceptive Trade Practice Act, losses subsequent to time of sale are recoverable only if misrepresentation is producing cause of loss. V.T.C.A., Bus. & C. § 17.50(b)(1).

15. **Fraud** ⇐20

Basis of a misrepresentation claim is that defendant's false statement induced plaintiff to assume risk he would not have taken had truth been known.

16. **Consumer Protection** ⇐40

Plaintiff's recovery of damages under Deceptive Trade Practices Act (DTPA) is limited not only by his own evidence, but also by defendant's evidence of plaintiff's failure to reasonably mitigate losses or evidence of intervening causes.

17. **Attorney and Client** ⇐148(1)

Attorney contingency fee contracts allow plaintiffs who cannot afford to pay a lawyer up-front to pay lawyer out of any recovery, and, because they offer potential of greater fee than might be earned under hourly billing method, compensate attorney for risk that attorney will receive no fee whatsoever if case is lost.

18. **Consumer Protection** ⇐42

Party's contingent fee agreement should be considered by fact finder, and is therefore admissible in evidence, but that agreement cannot alone support award of attorney's fees under Deceptive Trade Practices Act (DTPA). V.T.C.A., Bus. & C. § 17.50(d); State Bar Rules, V.T.C.A., Government Code Title 2, Subtitle G App., Art. 10, § 9, Rules of Prof.Conduct, Rule 1.04(b)(8).

19. **Consumer Protection** ⇐42

To recover attorney's fees under Deceptive Trade Practices Act (DTPA), plaintiff must prove that amount of fees was both reasonably incurred and necessary to prosecution of case, and must ask jury to award fees in specific dollar amount, not as percentage of judgment. V.T.C.A., Bus. & C. § 17.50(d); State Bar Rules, V.T.C.A., Government Code Title 2, Subtitle G App., Art. 10, § 9, Rules of Prof.Conduct, Rule 1.04.

Ben Taylor, Dallas, Thomas C. Godbold, Houston, for Petitioner.

Christopher B. Allen, Michael P. Cash, James W. Paulsen, Houston, for Respondent.

CORNYN, Justice.

We withdraw our opinion of January 10, 1997, and substitute the following in its place. The parties' motions for rehearing are overruled.

In this accounting malpractice case, Perry Equipment Corporation (PECO) sued the accounting firm of Arthur Andersen for a faulty audit, which PECO relied on to purchase another company, Maloney Pipeline Systems. The audit favorably reported Maloney's financial condition when, in fact, the company was suffering substantial losses. Fourteen months after the sale, Maloney filed for bankruptcy. PECO sued for violations of the Deceptive Trade Practice Act, fraud, negligence, negligent misrepresentation, gross negligence, and breach of implied warranty. Based on the jury's verdict, the trial court rendered judgment for PECO. The court of appeals affirmed. 898 S.W.2d 914.

We address three issues presented by Arthur Anderson's application for writ of error. First, Arthur Andersen challenges PECO's consumer status because Maloney, rather than PECO, actually paid for the audit. Second, Arthur Andersen claims that the trial court failed to instruct the jury on the correct measure of damages. Third, Arthur Andersen contests the attorney's fees award, arguing that the percentage of recovery method is not a proper measure of attorney's fees under the DTPA, and that even if such fees were recoverable, no evidence supports the award. For the reasons discussed below, we reverse the judgment of the court of appeals and remand this case to the trial court for further proceedings.

I

When PECO, a successful manufacturer of oil filters used in compressors for gas pipelines, decided to expand its business into the gas metering field, it looked into acquiring Maloney Pipeline Systems, one of three United States companies in the liquid metering market. In the mid–1980s, PECO began negotiating with Maloney's owner, Ramteck II. As a condition of the sale, PECO required an audit of Maloney's financial statements. Maloney retained Arthur Andersen to conduct the audit. Maloney eventually provided PECO financial statements audited by Arthur Andersen. The statements showed Maloney to be a profitable business. Relying upon this information, on August 23, 1985, PECO purchased the Maloney stock from Ramteck II, Inc. for $4,088,237.

Soon after the purchase, Maloney began to show signs of serious financial decline. For example, three months after the sale, Maloney ran out of cash and required a $400,000 advance from PECO to continue operating. PECO also attempted other emergency financial measures, but to no avail. Fourteen months after the sale, Maloney filed bankruptcy. PECO presented uncontradicted evidence at trial that the purchase price for Maloney was a total loss from which PECO realized no return and which PECO wrote off.

PECO's experts testified that Arthur Andersen's audit contained serious errors and otherwise failed to follow acceptable auditing procedures. One of the most significant errors, the evidence showed, was the failure to verify that contracts Maloney reported as complete were in fact complete or that Maloney's estimates of costs and percentage of completion for ongoing contracts were accurate. Maloney later incurred substantial losses on these contracts. One expert testified that the audit was one of the worst he had ever seen. Another expert, an auditing professor, stated that if a student submitted the work, he would have given the student a failing grade.

The jury found Arthur Andersen 51 percent at fault and PECO 49 percent at fault. The jury also found that Arthur Andersen had committed fraud, DTPA violations, and breach of warranty, but that it was not liable for negligent misrepresentation or gross negligence. The jury assessed damages of $5,449,468, including the $4,088,237 PECO paid for Maloney and $1,361,231 for other expenses incurred by PECO in its attempt to salvage the company. PECO elected to recover under the DTPA. The trial court credited Arthur Andersen with the two million dollars that Ramteck II had already paid PECO in settlement, and then awarded PECO a total of $9,297,601.20, including damages, prejudgment interest, DTPA additional damages, attorney's fees, and costs.

II

[1, 2] Arthur Andersen first contends that PECO is not a "consumer," a prerequisite to recovery under the DTPA. The DTPA defines a consumer as one "who seeks or acquires by purchase or lease, any goods or services." TEX. BUS. & COM.CODE § 17.45(4). In determining whether a plaintiff is a consumer, our focus is on the plaintiff's relationship to the transaction. *Amstadt v. United States Brass Corp.*, 919 S.W.2d 644, 650 (Tex. 1996). As a condition of sale, PECO insisted that Maloney provide audited financial statements. Maloney hired Arthur Andersen for this specific purpose. PECO then relied on those statements in reaching its decision to purchase Maloney. Under these circumstances, we hold that PECO sought and acquired Arthur Andersen's services.

The next question is whether PECO sought and acquired these services *by purchase or lease*, inasmuch as it did not pay for the audit. Our decision in *Kennedy v. Sale*, 689 S.W.2d 890 (Tex.1985), controls this issue. There, we held that the DTPA does not require the consumer to be an actual purchaser or lessor of the goods or services, as long as the consumer is the beneficiary of those goods or services. *Id.*

The Texas Society of Certified Public Accountants, as amicus curiae, argues that a stock purchaser should not be considered a consumer simply because the corporation paid for an audit for the purchaser's benefit because virtually every external audit benefits third parties. Thus, any stock purchaser who reviews audited financial statements could bring a DTPA claim against the auditor.[1] Our holding is not so broad. In this case, the audit was rendered in connection with the sale of Maloney and was specifically required by PECO and intended to benefit PECO. Arthur Andersen was aware that PECO had required the audit and would rely on its accuracy and knew the specific purpose for which it was conducted. We accordingly hold that PECO is a consumer under the DTPA.

Arthur Andersen also urges us to reject PECO's consumer status based on the decision in *Hand v. Dean Witter Reynolds Inc.*, 889 S.W.2d 488 (Tex.App.—Houston [14th Dist.] 1994, writ denied). In *Hand*, the plaintiff alleged that her stock broker failed to purchase certain commodity option contracts after she requested that he do so. *Id.* at 487–88. After deciding that a commodity option contract is a right, not a "good," under the DTPA, *id.* at 498, the court next considered whether the plaintiff was a consumer by virtue of her purchase of "services." The DTPA defines services as including "services furnished in connection with the sale or repair of goods." TEX. BUS. & COM.CODE § 17.45(2). The court reasoned that the omission of any reference in the definition to services in connection with the sale of something other than a good indicated that services furnished in connection with the sale of intangibles did not fall within the definition of services under the DTPA. *Hand*, 889 S.W.2d at 498. The court then concluded: "The key to the [consumer status] determination is whether the purchased goods or services are an objective of the transaction or merely incidental to it." *Id.* at 500.

We believe that *Hand* confirms, rather than defeats, PECO's consumer status. Arthur Andersen's audit was not merely incidental to the sale of Maloney to PECO; it was required by PECO and was central to PECO's decision to consummate the purchase. Determining Maloney's financial condition was PECO's primary objective in acquiring Arthur Andersen's services. We therefore reject Arthur Andersen's contention that *Hand* defeats PECO's status as a consumer under the DTPA.

III

Arthur Andersen next complains that the jury charge allowed the jury to award PECO the entire purchase price of Maloney, without instructing the jury to subtract the value of Maloney stock at the time of the sale.[2] Ar-

1. After PECO brought this action, the Legislature amended the DTPA to preclude consumers from suing under the DTPA for professional negligence or for claims arising from transactions involving consideration of more than $500,000. TEX. BUS. & COM.CODE § 17.49(c) & (g).

2. The charge asked the jury:

thur Andersen also contends that even if the court had properly instructed the jury, PECO failed to introduce any evidence that the stock was valueless at the time of sale, and thus failed to establish that it was entitled to the entire purchase price under either the "benefit-of-the-bargain" or the "out-of-pocket" measure of damages. PECO responds that in addition to direct damages, consequential damages are also recoverable under the DTPA. PECO thus argues that it is entitled to recover the purchase price as consequential damages.

[3] Under the version of the DTPA in effect at the time PECO brought this action, a consumer could recover "the amount of actual damages" caused by the defendant's false, misleading, or deceptive conduct. TEX. BUS. & COM.CODE § 17.50(b)(1).[3] The amount of actual damages recoverable is "the total loss sustained as a result of the deceptive trade practice." *Kish v. Van Note*, 692 S.W.2d 463, 466 (Tex.1985)(citing *Smith v. Baldwin*, 611 S.W.2d 611, 617 (Tex.1980)).

[4–6] Actual damages are those damages recoverable under common law. *Brown v. American Transfer & Storage Co.*, 601 S.W.2d 931, 939 (Tex.), *cert. denied*, 449 U.S. 1015, 101 S.Ct. 575, 66 L.Ed.2d 474 (1980). At common law, actual damages are either "direct" or "consequential." *Henry S. Miller Co. v. Bynum*, 836 S.W.2d 160, 163 (Tex. 1992) (Phillips, C.J., concurring); see RESTATEMENT (SECOND) OF TORTS § 549 (1977) (outlining measure of damages for fraudulent misrepresentation). Direct damages are the necessary and usual result of the defendant's wrongful act; they flow naturally and necessarily from the wrong. *See Southwind Aviation, Inc. v. Avendano*, 776 S.W.2d 734, 736 (Tex.App.—Corpus Christi 1989, writ denied); *Anderson Dev. Corp. v. Coastal States Crude Gathering Co.*, 543 S.W.2d 402, 405 (Tex.Civ.App.—Houston [14th Dist.] 1976, writ ref'd n.r.e.). Direct damages compensate the plaintiff for the loss that is conclusively presumed to have been foreseen by the defendant from his wrongful act. *See Bynum*, 836 S.W.2d at 163 (Phillips, C.J., concurring); *Coastal States*, 543 S.W.2d at 405; Anderson, *Incidental and Consequential Damages*, 7 J.L. & COM. 327, 328 (1987).

[7–9] Consequential damages, on the other hand, result naturally, but not necessarily, from the defendant's wrongful acts. *Haynes & Boone v. Bowser Bouldin, Ltd.*, 896 S.W.2d 179, 182 (Tex.1995); *Moore v. Anderson*, 30 Tex. 224, 230 (1867). Under the common law, consequential damages need not be the usual result of the wrong, but must be foreseeable, *see Mead v. Johnson Group, Inc.*, 615 S.W.2d 685, 687 (Tex.1981), and must be directly traceable to the wrongful act and result from it. *Airborne Freight Corp., Inc. v. C.R. Lee Enters., Inc.*, 847 S.W.2d 289, 295 (Tex.App.—El Paso 1992, writ denied); *El Paso Dev. Co. v. Ravel*, 339 S.W.2d 360, 363 (Tex.Civ.App.—El Paso 1960, writ ref'd n.r.e.). Of course, foreseeability is not an element of producing cause under the DTPA. *See Haynes & Boone*, 896 S.W.2d at 182; *Prudential Ins. v. Jefferson Assocs.*, 896 S.W.2d 156, 161 (Tex.1995). Still, if damages are too remote, too uncertain, or purely conjectural, they cannot be recovered. *See White v. Southwestern Bell Tel. Co., Inc.*, 651 S.W.2d 260, 262 (Tex.1983); *see also Bynum*, 836 S.W.2d at 164 (Phillips, C.J., concurring).

What sum of money, if any, if paid now in cash, would fairly and reasonably compensate PECO for its losses which resulted from such conduct?

Do not increase or reduce the amount in one answer because of your answer to any other question about damages.

....

....

Consider the elements of damages listed below and none other. Consider each element separately. Do not include damages for one element in any other element. Do not include interest on any amount of damages you find.

....

a. Purchase price of MPSI [Maloney]

b. Costs and expenses incurred by PECO as a result of its purchase and ownership of MPSI [listing 13 categories of costs and expenses]

3. In 1995, the Legislature amended § 17.50(b)(1) to permit recovery of "economic damages" and, if the defendant acted knowingly, "damages for mental anguish," instead of "actual damages." Act of May 17, 1995, 74th Leg., R.S., ch. 414, 1995 Tex.Gen. Laws 2992.

[10–12] Under Texas common law, direct damages for misrepresentation are measured in two ways. *W.O. Bankston Nissan, Inc. v. Walters*, 754 S.W.2d 127, 128 (Tex.1988); *Leyendecker & Assocs., Inc. v. Wechter*, 683 S.W.2d 369, 373 (Tex.1984). Out-of-pocket damages measure the difference between the value the buyer has paid and the value of what he has received; benefit-of-the-bargain damages measure the difference between the value as represented and the value received. *Leyendecker*, 683 S.W.2d at 373. Under the DTPA, a plaintiff may recover under the damage theory that provides the greater recovery. *Id.* Both measures of damages are determined at the time of sale. *See id.* at 373 (out-of-pocket damages are measured at the time of sale); *see also* Bullion, *An Understanding of Damages Recoverable Under the DTPA*, 20 ST. MARY'S L.J. 667, 670–72 (1989).

[13] In this case, the jury was not asked to find direct damages at the time of the sale as well as consequential damages attributable to Arthur Anderson's misrepresentations. Rather, the jury was simply asked to consider the purchase price as part of the overall damages. PECO did present evidence that the purchase price was eventually a total loss. There was also evidence that Maloney was losing money at the time of the sale and continued to do so until it declared bankruptcy. What PECO did not establish, however, was how much of its loss occurred at the time of the sale and how much was attributable to subsequent events for which Arthur Anderson should bear legal responsibility. If subsequent losses were caused by Arthur Andersen's wrongful conduct and were not simply part of the risk a buyer of the business would have assumed, they may be part of PECO's consequential damages.

[14, 15] Subsequent losses, however, are recoverable only if the misrepresentation is a producing cause of the loss. *See Haynes & Boone*, 896 S.W.2d at 182. Without this limitation, an investor could shift the entire risk of an investment to a defendant who made a misrepresentation, even if the loss were unrelated to the misrepresentation. The basis of a misrepresentation claim is that the defendant's false statement induced the plaintiff to assume a risk he would not have taken had the truth been known. But to allow the plaintiff to transfer the entire risk of loss associated with his investment, even risks that the plaintiff accepted knowingly or losses that occurred through no fault of the defendant, would unfairly transform the defendant into an insurer of the plaintiff's entire investment.

Because the charge failed to instruct the jury on the proper measure of direct damages, the submission was reversible error. But, because we find some evidence that Arthur Andersen's misrepresentation was a producing cause of PECO's loss, we remand this case for a new trial. *See Spencer v. Eagle Star Ins. Co.*, 876 S.W.2d 154, 157 (Tex.1994) (holding that remand is proper when defective liability question is submitted); *Jackson v. Fontaine's Clinics, Inc.*, 499 S.W.2d 87, 90 (Tex.1973) (remanding for new trial when defective damages question submitted); *Moulton v. Alamo Ambulance Serv., Inc.*, 414 S.W.2d 444, 449–50 (Tex.1967) (affirming remand for new trial when defective damages question submitted).

[16] We emphasize that a plaintiff's recovery of damages is limited not only by his own evidence, but also by the defendant's evidence of the plaintiff's failure to reasonably mitigate losses or evidence of intervening causes. *See Dubow v. Dragon*, 746 S.W.2d 857, 860 (Tex.App.—Dallas 1988, no writ); EDGAR & SALES, TEXAS TORTS & REMEDIES § 43.04[1][b]; Tschoepe et al., *Aspects of Defending A Texas Deceptive Trade Practices–Consumer Protection Act Claim*, 20 ST. MARY'S L.J. 527, 561 (1989). If a plaintiff's losses are attributable to his own mistakes or factors outside either of the parties' control, the defendant may be entitled to an appropriate limiting instruction to the jury.

IV.

Because we are remanding this case for a new trial, we turn now to Arthur Andersen's complaint that the trial court improperly awarded PECO attorney's fees calculated as a percentage of recovery.[4]

4. The jury charge requested the jury to calculate attorney's fees three ways: in dollars and cents,

[17] Attorney contingency fee contracts serve two main purposes. First, they allow plaintiffs who cannot afford to pay a lawyer up-front to pay the lawyer out of any recovery. *See* See, *An Alternative to the Contingent Fee*, 1984 UTAH L.REV. 485, 490 n. 14. Second, such contracts, because they offer the potential of a greater fee than might be earned under an hourly billing method, compensate the attorney for the risk that the attorney will receive no fee whatsoever if the case is lost. *Id.* The lawyer in effect lends the value of his services, which is secured by a share in the client's potential recovery. POSNER, ECONOMIC ANALYSIS OF LAW § 21.9 (4th ed.1992). Under some contingency fee contracts, the attorney also agrees to advance the out-of-pocket costs of the litigation. In such cases, the attorney not only risks loss of the fee, but also risks loss of actual expenditures.

Arthur Andersen complains that an award of contingency fees under a fee-shifting statute like the DTPA forces defendants to pay fees unrelated to the amount of work performed. While this is not always true, shifting these fees to the defendant presents two problems.

First, a contingent fee award based solely on evidence of a percentage fee agreement between a lawyer and client may be determined without regard to many of the factors that should be considered when determining reasonableness. The DTPA allows recovery of "reasonable and necessary attorneys' fees." TEX. BUS. & COM.CODE § 17.50(d). Factors that a factfinder should consider when determining the reasonableness of a fee include:

(1) the time and labor required, the novelty and difficulty of the questions involved, and the skill required to perform the legal service properly;

(2) the likelihood ... that the acceptance of the particular employment will preclude other employment by the lawyer;

(3) the fee customarily charged in the locality for similar legal services;

(4) the amount involved and the results obtained;

(5) the time limitations imposed by the client or by the circumstances;

(6) the nature and length of the professional relationship with the client;

(7) the experience, reputation, and ability of the lawyer or lawyers performing the services; and

(8) whether the fee is fixed or contingent on results obtained or uncertainty of collection before the legal services have been rendered.

TEX. DISCIPLINARY R. PROF. CONDUCT 1.04, *reprinted in* TEX. GOV'T CODE, tit. 2, subtit. G app. (STATE BAR RULES, art. X, § 9); *see also Ragsdale v. Progressive Voters League*, 801 S.W.2d 880, 881 (Tex.1990); *cf. General Motors Corp. v. Bloyed*, 916 S.W.2d 949, 960–961 (Tex.1996) (discussing the relative strengths and weaknesses of the contingent fee and lodestar methods of awarding attorneys fees in the context of a court-approved class action settlement). While we do not doubt that many plaintiffs must contract for a contingent fee to secure the services of a lawyer, we do not believe that the DTPA authorizes the shifting of the plaintiff's entire contingent fee to the defendant without consideration of the factors required by the Rules of Professional Conduct. A contingent fee may indeed be a reasonable fee from the standpoint of the parties to the contract. But, we cannot agree that the mere fact that a party and a lawyer have agreed to a contingent fee means that the fee arrangement is in and of itself reasonable for purposes of shifting that fee to the defendant.

[18] A party's contingent fee agreement should be considered by the factfinder, see TEX. DISCIPLINARY R. PROF. CONDUCT 1.04(b)(8), and is therefore admissible in evidence, but that agreement cannot alone support an award of attorney's fees under Texas Business and Commerce Code section 17.50(d). *See* Brister, *Proof of Attorney's Fees in Texas*, 24 ST. MARY'S L.J. 313, 324 (1993). In other words, the plaintiff cannot simply ask the jury to award a percentage of

as a percentage of PECO's recovery, and as a combination of dollars and cents and percentage of recovery.

the recovery as a fee because without evidence of the factors identified in Disciplinary Rule 1.04, the jury has no meaningful way to determine if the fees were in fact reasonable and necessary.

Second, because the jury is not informed what the total amount of the judgment will be, the jury can only speculate about whether a percentage of that unknown recovery will represent a reasonable and necessary fee in that particular case. Rather than leave this question to speculation, the jury must decide the question of attorney's fees specifically in light of the work performed in the very case for which the fee is sought.

[19] In light of these concerns, we hold that to recover attorney's fees under the DTPA, the plaintiff must prove that the amount of fees was both reasonably incurred and necessary to the prosecution of the case at bar, and must ask the jury to award the fees in a specific dollar amount, not as a percentage of the judgment.

For the foregoing reasons, we reverse the judgment of the court of appeals and remand this cause to the trial court for further proceedings consistent with this opinion.

TRINITY UNIVERSAL INSURANCE COMPANY and Trinity Lloyd's Insurance Company, Petitioners,

v.

Nicole COWAN, individually and as assignee of Gregory D. Gage, Respondent.

No. 95-1160.

Supreme Court of Texas.

May 16, 1997.

Subject of provocative photographs distributed by insured while employed as photo lab clerk brought action against homeowners' liability insurer to collect on judgment against insured. The 98th Judicial District Court, Travis County, Mike Lynch, J., granted subject's motion for partial summary judgment. Insurer appealed. The Court of Appeals, Carroll, C.J., 906 S.W.2d 124, affirmed. On application for writ of error, the Supreme Court, Cornyn, J., held that: (1) "bodily injury" covered by policy does not include purely emotional injuries, and (2) insured's intentional tort in copying photographs and showing them to friends was not "accident" and, therefore, was not covered.

Reversed and rendered.

1. **Insurance ⇐514.10(1)**

Under "complaint allegation rule," factual allegations in pleadings and policy language determine insurer's duty to defend.

See publication Words and Phrases for other judicial constructions and definitions.

2. **Insurance ⇐512(2)**

Liability insurer's duty to indemnify is triggered by actual facts establishing liability in underlying suit.

3. **Insurance ⇐514.9(1)**

Duty to defend and duty to indemnify by insurer are distinct and separate.

4. **Insurance ⇐435.35**

"Bodily injury" within liability coverage of homeowners' insurance policy does not include purely emotional injuries or pure mental anguish, but requires injury to physical structure of human body, even though tort law allows for recovery of mental anguish damages unaccompanied by physical manifestations in some circumstances.

See publication Words and Phrases for other judicial constructions and definitions.

5. **Insurance ⇐146**

Interpretation of insurance contracts is governed by same rules as interpretation of other contracts.

6. **Insurance ⇐146.5(1)**

When terms are defined in insurance policy, those definitions control.

PROJECT NO. 41622

RULEMAKING TO PROPOSE NEW SUBST. R. §25.245, RELATING TO RECOVERY OF EXPENSES FOR RATEMAKING PROCEEDINGS	**§ § § §**	**PUBLIC UTILITY COMMISSION OF TEXAS**

ORDER ADOPTING NEW §25.245
AS APPROVED AT THE JULY 10, 2014 OPEN MEETING

The Public Utility Commission of Texas (commission) adopts new §25.245, relating to Recovery of Expenses for Ratemaking Proceedings, with changes to the proposed text as published in the February 7, 2014 issue of the *Texas Register* (39 TexReg 571). The rule establishes criteria for review of utilities' and municipalities' requests for recovery of or reimbursement for rate-case expenses. Project Number 41622 is assigned to this proceeding.

The commission received written initial and/or reply comments on the new rule from the Alliance of Local Regulatory Authorities (the Alliance); AEP Texas Central Company, AEP Texas North Company, CenterPoint Energy Houston Electric LLC, Cross Texas Transmission LLC, El Paso Electric Company, Electric Transmission Texas LLC, Entergy Texas, Inc., Lone Star Transmission LLC, Oncor Electric Delivery Company, Sharyland Utilities LP, Southwestern Electric Power Company, Southwestern Public Service Company, Texas-New Mexico Power Company, and Wind Energy Transmission Texas LLC (collectively, Joint Utilities); Steve Baron; City of El Paso (El Paso); City of Houston (Houston); the Lower Colorado River Authority (LCRA); Office of Public Utility Counsel (OPUC); the REP Group; State of Texas' agencies and institutions of higher education (State Agencies); the Steering Committee of Cities Served by Oncor (Oncor Cities); Texas Industrial Energy Consumers

(TIEC); the Texas Municipal League (TML), and Aqua Texas, Canyon Lake Water Service Company, and SouthWest Water Company (collectively, Water IOUs).

Public Hearing

On April 3, 2014, at the request of OPUC and Water IOUs, commission staff conducted a public hearing in this proceeding. Parties' statements at the public hearing were generally similar to their filed written comments. Comments that were new or additional are noted below.

General Comments

State Agencies commented that although the commission's discretion to approve rate-case expenses is necessarily one that must be made on a case-by-case basis, and need not be justified by a rule, State Agencies appreciate the commissioners' proposal to outline some concepts and considerations that will guide their discretion. OPUC and TIEC similarly commended the commission's efforts to create a rule governing rate-case expense recovery, but opined that there may be policy issues to consider in determining which expenses to allow or disallow and that the rule as published unnecessarily restricts the commission's discretion, in contrast with the commission's broad authority in Public Utility Regulatory Act (PURA), Texas Utilities Code Annotated §36.061(b) (Vernon 2007 & Supp. 2013).

Steve Baron expressed similar comments by stating that the commission should adopt a rate-case expense rule that provides meaningful guidance without being overly prescriptive, and he noted that PURA §36.061(b)(2) articulates "reasonableness" as a single, general standard for recovery of rate-case expenses. Mr. Baron stated that this general "reasonableness" standard gives the

commission broad discretion to determine recovery of rate-case expenses, that the commission has exercised that discretion on a case-by-case basis, and that the courts have confirmed that the commission in doing so may consider a variety of factors. Mr. Baron commented that the rule should provide guidance regarding "reasonableness" without being overly prescriptive in a way that could constrain the commission's exercise of discretion and result in an arbitrary allowance or disallowance in a particular case.

TIEC noted that its members pay for both the utilities' and municipalities' rate-case expenses, in addition to their own legal and consulting fees. TIEC noted that, given this fact, it is in a unique position to offer comments regarding the appropriate framework for considering utility and municipalities' rate-case expenses, and TIEC expressed support for rule revisions that would incentivize municipalities and utilities to act more like self-funded litigants. TIEC commented that although many of the positions articulated by the utilities and the municipalities presume that recovery of rate-case expenses is a right, PURA §36.061 provides only that the commission "may allow" a utility's "reasonable costs of participating in a proceeding under this title not to exceed the amount approved by the regulatory authority." TIEC stated that, similarly, PURA §33.023(b) states that an electric utility shall reimburse the governing body of the municipality for the "reasonable cost of the services" of persons engaged in rate case proceedings "to the extent the applicable regulatory authority determines is reasonable." TIEC submitted that existing law, therefore, gives the commission broad discretion to determine the reasonableness of rate-case expenses and whether they should be recovered; consistent with this existing legal principle, and regardless of whether the proposed rule is adopted, the commission has broad authority to determine whether rate-case expenses are unrecoverable for a variety of reasons,

including litigation of well-settled issues, frivolous positions, flawed analysis, over-lawyering, or other policy considerations. TIEC submitted that the commission does not need a new rule to carry out its statutory duties regarding rate-case expenses, and nothing in the proposed rule should be applied in a way that would limit this existing discretion and authority.

State Agencies noted that in proceedings prior to publication of the proposed rule, commission staff was urged to draw on the collective wisdom of other state agencies in Texas as well as surrounding states, and gave the example of how the Texas Railroad Commission has a rate-case expense rule (16 Texas Administrative Code §7.5530) that provides guidelines for the commission's exercise of discretion without curtailing its power to react to specific circumstances. State Agencies noted that Rule 1.04 of the Texas Disciplinary Rules of Professional Conduct (TDRPC) also offers parameters for measuring the reasonableness of attorney fees that are worthy of consideration by the commission. State Agencies stated that the commission's proposed new §25.245 commendably incorporates guidelines similar to the Railroad Commission's rule, but State Agencies expressed its belief that other concepts from that rule should be included in the commission's proposed rule—specifically, the criterion allowing comparison of the rate relief that was requested to that which was ultimately awarded.

State Agencies further commented that the rule should remove the qualifier that would restrict the commission's consideration of methods for evaluating rate-case expense that go beyond "bean counting" individual invoices. State Agencies submitted that for those cases where individual invoices must be scrutinized, the proposed rule lacks an essential standard for evaluating costs incurred for travel, lodging and meals, and therefore proposed the use of an

existing objective standard: the ceiling on expenses that state employees and officials must observe when on official business.

El Paso commented that in any discussion about municipal rate-case expenses, the commission must consider that pursuant to Chapter 33 of PURA, the municipalities have original jurisdiction over the rates, operations, and services of electric utilities in areas in the municipality. El Paso noted that a rate case must be filed with the municipality, which has the obligation to evaluate the rate increase request, and therefore, it is improper to characterize the statutory role of the municipality as challenging or opposing portions of the request, and it is similarly inappropriate to provide guidance on the reasonableness of municipal expenses on the basis of either issues or amounts successfully or unsuccessfully challenged. El Paso commented that because the commission has the authority to disallow expenses that it does not find reasonable, portions of the rule other than those that codify prior commission practices and precedents are unnecessary. Houston and the Alliance expressed similar comments, with Houston stating that it does not believe that reductions in rate-case expense should equate to a reduction in the level of proper and necessary review performed by the municipal regulator. Houston stated that if the proposed rule limits a city's ability to perform a comprehensive review in any rate proceeding, whether directly or indirectly, the rule ultimately interferes with that city's ability to effectively perform its legislatively mandated obligations as municipal regulator. The Alliance commented that municipalities have a statutory right to participate in rate cases and noted that no other party has that right. The Alliance also commented that its members fully recognize that it is its citizens and businesses that ultimately bear the costs of rate cases, and that the City Attorney offices, the City Manager offices, the Financial Directors, the members of the Alliance's city councils and

city commissions are ever vigilant over fees and expenses incurred for the cities' active participation in rate-making proceedings. The Alliance commented that its participation has achieved savings for its citizens and business that far outweigh the total municipal rate-case expenses.

Oncor Cities commented that the language of PURA §33.023 makes clear that it is both a grant and a limitation, as it affords municipal intervenors the authority to recover their reasonable costs of participating in a ratemaking proceeding, but not expenses in excess of that amount. Oncor Cities stated that while the commission's proposed rule appropriately focuses on ensuring that only reasonable rate-case expenses are approved and recovered, the statute also requires that the rule not hinder or even prevent the quantification and recovery of reasonable expenses.

Houston stated that at this time, it does not believe the proposed rule is necessary, as it believes the current long-standing process for reviewing and determining the amount of reasonable and necessary rate-case expenses has proven sufficient and effective. Houston commented that it is not aware of any instance in which comments by other parties suggested that the current process was ineffective or defective in a material manner. Houston further opined that the current two-tier process provides for an extensive and transparent review, and includes the State Office of Administrative Hearing (SOAH) and the commission; the process also allows for the intervention of interested and affected parties, and while rate-case expenses may have increased over the past few decades, the complexity of filings and number of issues presented have also increased. Houston stated that the regulatory process is not immune to standard inflation-related increases, and it is concerned that a rule focused on reducing overall rate-case expenses without a

more thorough review, inclusive of a cost/benefit analysis, could have a significant and negative impact on the overall ratemaking process and could hinder the municipal regulator's effective participation in rate proceedings.

Joint Utilities commented that under PURA and the Third Court of Appeals' decision in *Oncor Electric Delivery Company LLC v. Public Utility Commission of Texas*, 406 S.W.3d 253 (Tex. App.—Austin 2013, no pet.) (*Oncor*), all reasonable and necessary rate-case expenses incurred by utilities or municipalities are recoverable. Joint Utilities stated that to give effect to PURA and the court's decision, the proposed rule should (1) establish the criteria that utilities and municipalities must meet in order to establish the reasonableness of their expenses, (2) apply those criteria equally to both utilities and municipalities, (3) ensure utilities and municipalities have an opportunity to seek recovery of their reasonable and necessary expenses, and (4) ensure that, if the utility or municipality meets its burden of proof, all reasonable costs are recoverable. Joint Utilities opined that subsections (a) - (c) of the proposed rule include language that appropriately addresses these standards, but for reasons discussed below, Joint Utilities urged the commission to modify subsection (c) and (d).

Similar to Houston, LCRA stated that it believes the existing method of determining the reasonableness of rate-case expenses has worked well to date and the proposed rule's subsections (a) - (c) effectively describe those steps. LCRA averred, however, that proposed subsection (d) introduces new mechanical approaches that purport to measure the reasonableness of rate-case expenses by application of formulaic methodologies rather than a reasoned review of the pertinent facts in any given case, and LCRA believes these proposed new approaches are

therefore incompatible with PURA. LCRA also stated that it believes the comments filed by Joint Utilities constitute a comprehensive and correct assessment of the proposed rule as a whole and offer the best roadmap for the commission to follow as it decides what parts, if any, of the proposed rule should be adopted. LCRA commented that the commission already has authority and discretion to disallow expenses (including rate-case expenses) that are not just and reasonable, or on which a party has not carried its burden of proof, and that therefore this rule is largely unnecessary. LCRA commented that to the extent the proposed rule was prompted by the facts of any given rate case it may be more reasonable to deal with the specific facts of that case rather than establish a general rule whose applicability to many utilities is questionable, particularly when many of the proposed subsections of the rule simply add complexity and possible confusion rather than clarity. LCRA submitted that to the extent that a rate-case expenses rule adds more requirements to describe, segregate, or account for certain expenses in a particular fashion, it virtually invites additional litigation from parties who claim utilities did not present rate-case expenses correctly, or from utilities that assert they did and are entitled to full recovery of all rate-case expenses. LCRA stated that, given the foregoing considerations, it respectfully questions the necessity for this rule, but at the very least believes subsection (d) of the proposed rule should be rejected in its entirety if the commission believes any new rule is necessary at all.

State Agencies commented that contrary to the assertions of Joint Utilities and Mr. Baron, the *Oncor* decision did not establish a mandate for approval of a utility's incurred rate-case expenses. State Agencies submitted that the rate-case expenses at issue in that case were from 2004 and 2005 rate cases, not previously recovered, and had been stipulated by the parties to be

both reasonable and necessary, but that the commission held that it had no jurisdiction in a later 2009 rate case to consider those costs from earlier proceedings because Oncor failed to obtain approval to seek them in a later proceeding. State Agencies commented that the commission determined that it had no jurisdiction to consider earlier rate-case expenses because the right to seek them had not been preserved; thus, the principal issue before the Court of Appeals was not the reasonableness of the 2004 and 2005 rate-case expenses, given that that had been stipulated, but whether the commission acted arbitrarily and capriciously by imposing on Oncor the requirement for "prior authorization" to seek earlier rate-case expenses in its later rate case. State Agencies commented that the court discussed the evidence showing that this prior authorization requirement was a departure from the commission's prior practice and focused specifically on the violation of Oncor's due process rights inherent in the commission's decision, and that there is nothing in the *Oncor* case holding that PURA §36.051 somehow removes the commission's discretion under PURA §36.061(b)(2) to approve or disapprove rate-case expenses, and nothing that changed the requirement that these costs cannot be recovered unless they were proven to be reasonable and necessary.

Water IOUs expressed concern that the proposed rule creates a possibility that the commission may see fit to adopt a similar rule for water/wastewater rate cases after the September 1, 2014 jurisdictional transfer. Water IOUs commented that if a rate-case expense rule is adopted, it should follow well-established Texas law for determining reasonableness and necessity of attorney's fees and apply similar criteria for other types of rate-case expenses, and Water IOUs opined that proposed §25.245 does not accomplish this, but instead proposes various levels of criteria that are at best problematic and at worst will pave the way for arbitrary disallowance of

rate-case expenses that should be recoverable. Water IOUs cited the test laid out by TDRPC §1.04(b) in conjunction with the precedent from *Arthur Andersen & Co. v. Perry Equipment Corp.*, 945 S.W.2d 812 (Tex. 1997) (*Andersen*) as relatively simple criteria that are universally accepted in the Texas courts for determining reasonable and necessary attorneys' costs. OPUC responded that while some of these factors may be instructive in determining the extent of reasonable fees, they are too narrow to apply generally to utility rate proceedings; further, some of these factors are simply not relevant to determining whether the ratepayers should be responsible for paying the utility's rate-case expenses. OPUC stated that, for instance, the "nature and length of the professional relationship with the client" may be relevant to the client, *i.e.*, the utility, but it does not go to whether the expenses are reasonable and in the public interest, and thus, appropriate for recovery from the rate payers.

Water IOUs also expressed concern about the possibility of any version of the specific provisions in proposed §25.245(d) being applied to them in future rate cases. Water IOUs pointed out that water customer counts are relatively small when compared to electric utilities and have a smaller denominator for rate-case expense surcharge calculations, and that there is a potential for unnecessarily inflating the resulting rate-case-expense surcharge because of increased litigation costs directly resulting from rate-case expense disallowance efforts under the proposed rule. Water IOUs stated that PURA has a similar statutory requirement to Texas Water Code §13.183(a), which specifies that the return on a utility's invested capital used and useful in rendering service to the public must be (1) over and above its reasonable and necessary operating expenses and (2) sufficient to preserve the financial integrity of the utility. Water IOUs noted that PURA §36.051 contains similar language, and that in the recent Court of Appeals opinion in

the *Oncor* case, the court found that disallowance of reasonable and necessary rate-case expenses violates this requirement. Water IOUs commented that the effect of disallowing reasonable and necessary expenses is to charge those expenses to the utility's stockholders instead of to its ratepayers, thus reducing the return the utility earns on its rate base. Water IOUs submitted that the requirement for a reasonable return is only satisfied if the utility's return on capital is sufficient to ensure confidence in the financial integrity of the utility to enable it to maintain its credit and attract capital, and that therefore, regulatory agencies cannot arbitrarily disallow reasonable and necessary expenditures, or confiscation will result.

Commission response

The commission agrees with the several parties who commented that the rule should not hinder or limit the commission's broad discretion under PURA §36.061(b) and §33.023(b) with respect to rate-case expenses. The adopted rule maintains the commission's discretion in this regard while also articulating more specific criteria by which the commission may determine disallowances. While recognizing that the commission retains broad discretion to review and evaluate rate-case expenses under PURA's "reasonableness" standard, the commission also agrees with the comments of Mr. Baron that the rate-case expense rule should provide meaningful guidance to the parties regarding specific rate-case expense requests, including the evidence parties must submit to meet their burden to establish the reasonableness of any requested rate-case expenses. In light of the comments from the parties, the commission has made several changes to the published rule in order to further clarify the evidence necessary to establish reasonable rate-case expenses and the criteria the commission will utilize in reviewing and determining the reasonableness of particular

expenses. As discussed more fully in the responses to the comments on particular subsections below, the commission finds that subsections (a) - (c) of the rule, as adopted, now provide adequate guidance to the parties regarding the commission's process for evaluating rate-case expenses.

The commission notes that several parties, including LCRA, asserted that subsection (d) of the proposed rule introduced mechanical approaches and/or formulistic methodologies that were inconsistent with the commission's broad discretion to review the reasonableness of rate-case expenses. The commission emphasizes that the methodologies in subsection (d) of the proposed rule only apply in circumstances in which the requesting party submitted insufficient evidence to quantify rate-case expenses and are not exhaustive or mandatory. Nevertheless, as discussed in the responses to the comments on subsection (b) below, the commission has now further clarified the requirements for claiming recovery of or reimbursement for rate-case expenses in the adopted rule. In light of these revisions to the evidentiary requirements in the adopted rule, the commission is persuaded by the comments of various parties that in most circumstances, the calculation of the disallowance of particular rate-case expense amounts should be based directly upon the amount of rate-case expenses found to be unreasonably incurred. The commission is persuaded that sufficient evidence will be presented in most circumstances, in part, because, if a utility company or municipality fails to provide evidence supporting the reasonableness of its rate-case expenses as required under subsection (b)(6) of the adopted rule, the adopted rule provides reasonable alternatives to the presiding officer in order to allow for efficient processing of the application. If the evidence provided is insufficient to meet the

requirements of the rule, the commission anticipates that such an application would likely need to be supplemented or be rejected as insufficient and the applicant would be required to file the information required under the rule. In addition, the commission would retain the authority to disallow a portion of the party's rate-case expenses pursuant to subsection (d)(3) of the adopted rule as discussed below.

As discussed in greater detail below, the commission has revised subsection (d) of the rule to provide that, in most circumstances, the presiding officer will disallow or recommend disallowance of recovery of rate-case expenses equal to the amount shown to have not been reasonably incurred using the criteria in subsection (c). The remaining methodologies in subsection (d) will now only apply in two specific circumstances: (1) the methodology stated in subsection (d)(3) of the adopted rule (the Issue Specific Method) may be applied when the applicant has not specified the amount of rate-case expenses reasonably associated with a particular issue under subsection (b)(6) of the rule as adopted; or (2) the methodology stated in subsection (d)(2) of the adopted rule (the Results Oriented Method) may be applied when the commission finds that the rate-case expenses as a whole were disproportionate, excessive, or unwarranted in relation to the nature and scope of the rate case under subsection (c)(5) of the rule as adopted.

Consistent with comments by TIEC regarding PURA §36.061, the commission concludes that adopting clear evidentiary standards and specific criteria for the review and determination of the reasonableness of rate-case expenses will incentivize utilities and municipalities to act more like self-funded litigants, while still providing for recovery of

reasonable rate-case expenses. The commission emphasizes that it retains broad discretion and flexibility when reviewing requests for recovery of or reimbursement for rate-case expenses. The commission further anticipates that in evaluating specific rate-case expense requests, the presiding officer will apply the specific criteria established in the adopted rule in light of the overall "reasonableness" standard for rate-case expense recovery.

Regarding the concerns expressed by Water IOUs about the possibility of any version of the specific provisions in proposed subsection (d) being applied to them in future rate cases, the commission notes that §25.245 will only apply to electric utility companies. The commission will begin regulation of water utility companies on September 1, 2014, and currently has open a rulemaking proceeding in Project No. 42191 that transfers the existing Texas Commission on Environmental Quality (TCEQ) rules to the commission with only minimal substantive revisions. Included in the transferred rules is 30 Texas Administrative Code §291.28(7) - (9), which will continue to address water utilities' recovery of rate-case expenses after the commission assumes jurisdiction over water utilities on September 1, 2014. The commission notes, however, that it may in the future consider additional rulemaking proceedings for water utilities, including a possible rulemaking that specifically addresses the criteria for recovery of rate-case expenses, but that is beyond the scope of this proceeding.

With regard to parties' comments on specific subsections of the rule—such as, for example, State Agencies' comments regarding the proposed rule's similarities to guidelines in the Railroad Commission's rules—the commission responds in greater detail below. Also

below, the commission addresses Mr. Baron's and Joint Utilities' assertions on the court decision in the *Oncor* case.

Response to Commission Questions

In addition to the published proposal, the commission requested that parties submit responses to the following questions:

1. *Should the proposed rule, if adopted, explicitly allow for allocation of rate-case expenses to a utility's shareholders?*

The Alliance, OPUC, State Agencies, TIEC, and TML responded that, yes, explicitly allowing for allocation of rate-cases expenses to a utility's shareholders is appropriate. OPUC and State Agencies commented that, as a practical matter, the effect of disallowing any requested cost is that the utility and its shareholders are responsible for those costs, not the ratepayers. OPUC and State Agencies noted, however, that if the commission chooses for policy reasons to assign a portion of rate-case expenses under certain circumstances to a utility's shareholders, expressly stating this in the rule serves as additional notice to the utilities of the commission's intent.

OPUC further commented that if a utility knew that it would be responsible for some portion of its rate-case expenses, it might give more consideration to the costs and benefits of raising certain issues. OPUC stated that this could include decisions to challenge established commission precedent, whether to bring multiple lawyers to a proceeding, or whether to pursue certain procedural or discovery disputes that have a low probability of success. OPUC stated that requiring utilities and their shareholders to be at least partially accountable for the costs of

these activities would increase the incentive to employ a more reasonable and cost-effective litigation strategy.

State Agencies commented that approval or disapproval of rate-case expenses is necessarily dependent upon the facts of a case and the overall history of a utility's filing at the commission, and that well-managed utilities that control their costs and run efficient operations—which obviate the need for frequent, repetitive rate-case filings—can make a more persuasive case that a greater portion of their requested rate-case expenses is necessary.

The Alliance commented that in the vast majority of cases, the utility is the entity that initiates a case to seek a rate increase. The Alliance stated that while the utility and its board of directors owe a fiduciary duty to the utility's shareholders to maximize profits, it is only fair that the shareholders pay for some or all of the utility's rate-case expenses.

TIEC similarly commented that utility shareholders benefit from rate increases and should therefore share in the cost of obtaining a rate increase. TIEC opined that giving utility shareholders "skin in the game" for rate-case expenses would limit over-lawyering, encourage negotiation during the litigation process, and discourage utilities from incurring excessive and imprudent rate-case expenses to litigate well-settled issues or frivolous positions. TIEC submitted that PURA §36.061 provides that the commission "may allow" a utility's "reasonable costs of participating in a proceeding under this title not to exceed the amount approved by the regulatory authority," and that this provision plainly gives the commission authority to allocate a portion of rate-case expenses to the utility's shareholders. TIEC also stated that a rule that

explicitly allows rate-case expenses to be allocated to a utility's shareholders would give utilities an incentive to better manage their rate-case expenses and act more like private litigants. TIEC commented that the proposed rule would offer a useful framework and guidelines in the consideration of rate-case expenses, but the rule should not be misconstrued as limiting the commission's existing authority and discretion in any way.

Houston similarly stated that it is not opposed to allowing for allocation of rate-case expenses to a utility's shareholders.

Water IOUs and Mr. Baron responded that the rule should not explicitly allow for allocation of rate-case expenses to a utility's shareholders. Mr. Baron commented that rate-case expenses should be disallowed not on a "shareholders benefit" theory, but on the evidentiary record applied to the factors and criteria for reasonableness. Mr. Baron stated that, by statute, a utility must follow all applicable rate-case procedures and thereby unavoidably incur rate-case expenses, and that under this framework, it is reasonable and appropriate to deny recovery of expenses shown by the facts to be excessive and unnecessary, but difficult to justify disallowances on a "shareholders benefit" theory that disregards the evidentiary record.

LCRA commented that none of the arguments made by the Alliance, State Agencies, OPUC, and TIEC are valid bases for denying recovery of legitimate expenses such as rate-case expenses, and more to the point, none of those arguments square with the applicable sections of PURA that state that a utility that carries its burden of proof is entitled to its reasonable and necessary

expenses and a reasonable return on investment. Like Joint Utilities, LCRA submitted that the Austin Court of Appeals recently decided these principles in the *Oncor* case.

Joint Utilities and Water IOUs similarly commented that if rate-case expenses are reasonable and necessary, the commission should allow recovery. These parties stated that regulated utilities must apply to increase rates when needed to maintain their legal right to recover reasonable and necessary O&M costs, plus return on invested capital, and that rate-case expenses are required by regulatory processes imposed upon utilities and not by shareholder interests. Joint Utilities commented that the commission has discretion under PURA—and under subsections (b) and (c) of the published rule—to determine whether a party has met its burden of proof that its requested rate-case expenses are reasonable. Joint Utilities stated that to the extent the commission determines rate-case expenses are not reasonable or necessary, those disallowed expenses are effectively assigned to the shareholders; however, under the *Oncor* decision, the commission cannot presume that rate-case expenses are unreasonable just for the sake of requiring shareholders to "pay" for the presumed benefit of filing a rate case. Similarly, Water IOUs submitted that there should not be allocation to shareholders of such expenses by making reasonable and necessary rate-case expenses partially unrecoverable through retail rates in the manner this question suggests.

Joint Utilities additionally commented that assigning reasonable rate-case expenses to a utility's shareholders essentially punishes the utility and its shareholders for requesting their reasonable and necessary operating expenses, thereby reducing their commission-approved return by the cost of requesting their expenses. Joint Utilities further stated that this fails to account for the

fact that a utility does not always determine whether or when it files a statement of intent, given that a municipality or the commission can initiate a rate-case proceeding as well and thus requiring a utility to expend funds to defend its existing cost of service. Joint Utilities submitted that requiring shareholders to pay to litigate a utility's cost of service also incents other parties to inflate litigation costs as a tactic to discourage utilities from changing rates or encourage utilities to settle for less than their actual cost of service to avoid litigation expense. Joint Utilities stated that the commission must reject certain commenters' proposal to systematically disallow utility rate-case expenses for "policy" reasons without regard to their reasonableness. Joint Utilities submitted that both PURA and the Third Court of Appeals ruling in *Oncor* dictate that a utility's reasonable rate-case expenses are recoverable, and any rule adopted in this proceeding must comply with the *Oncor* analysis. Joint Utilities stated that, notably, none of these commenters even address *Oncor* and its clear requirements, but that instead, commenters point to the broad discretion granted the regulatory agency in *City of Port Neches v. Railroad Commission of Texas*, 212 S.W.3d 565 (Tex. App.—Austin 2006, no pet.) *(City of Port Neches)*, which addresses post-test year adjustments, and *City of El Paso v. Public Utility Commission of Texas*, 916 S.W.2d 515 (Tex. App.—Austin 1995, writ dism'd by agr.), which expressly requires that a utility be reimbursed for its reasonable rate-case expenses, consistent with *Oncor*.

OPUC commented that Joint Utilities advance a far too narrow interpretation of the commission's authority by asserting that the recent decision in the *Oncor* case requires that all reasonable and necessary rate-case expenses be recoverable. OPUC contended that the commission has broad discretion to determine recovery of expenses in a ratemaking proceeding, and cited *City of Port Neches*. OPUC stated that PURA §36.061 reflects this authority and states

that the regulatory authority may allow as a cost or expense the "reasonable costs of participating in a proceeding under this title not to exceed the amount approved by the regulatory authority." OPUC stated that this language indicates that the commission can approve some amount that is less than reasonable costs and can take into account other considerations, and without this discretion, rate-case expense proceedings would be rendered mere accounting exercises. OPUC further stated that the courts have made clear that the commission's authority is not limited to line item disallowances or charges related to underlying unreasonable costs, and cited the case of *City of Amarillo v. Railroad Commission of Texas*, 894 S.W.2d 491, 496-97 (Tex. App.-Austin 1995, writ denied), in which the court upheld the Railroad Commission's decision to reduce the uncontested rate-case expenses related to one analyst's charges by 20% due to insufficiency of support. OPUC noted that the Third Court of Appeals also confirmed that it is within the agency's discretion to find rate-case expenses to be unreasonable even if the underlying cost item in the rate case is found to be reasonable. The court stated in *City of Port Neches* that:

> It is true that, in order to include . . . costs as an "expense or cost of service" in TGS's rate calculation, TGS was required to demonstrate that those costs were reasonable and necessary. But the leap cannot be made from this fact to TGS's conclusion that any fee incurred by TGS in presenting its "cost of service" argument is automatically recoverable as a rate-case expense. This is where the Commission's discretion . . . plays an integral role. 212 S.W.3d 565, 581.

OPUC contended that the commission therefore has significant discretion in determining recovery of rate-case expenses.

OPUC also stated that contrary to Joint Utilities' comments, the acknowledgment that certain rate-case expenses may be assigned to a utility's shareholders does not serve as a punishment of the utility and its shareholders. Rather, it recognizes the reality that a utility's shareholders reap

benefits from implementing rate increases and that the utility's board of directors owes a fiduciary duty to the utility's shareholders to maximize profits. OPUC agreed with TIEC's comments that a rule that explicitly allows rate-case expenses to be allocated to a utility's shareholders provides to utilities an incentive to better manage their rate-case expenses and act more like private litigants, and this incentive is essential given that the utilities in large part control the expenses incurred for a rate case. OPUC submitted that a utility, properly acting as a prudent gatekeeper of rate-case expenses, should make decisions about whether to incur certain rate-case expenses as if it were ultimately the party responsible for paying them.

Commission response

The commission agrees with comments filed by OPUC, the Alliance, State Agencies, TIEC, TML, and Houston that the commission can explicitly provide in the rule for allocation of rate-case expenses to a utility's shareholders. However, the commission also agrees with the comments of Mr. Baron and others that the disallowance of rate-case expenses should be based, to the extent practicable, on the evidentiary record as applied to the factors and criteria for reasonableness. As discussed in greater detail below, the commission has now further clarified the requirements for claiming recovery of or reimbursement for rate-case expenses in the adopted rule, as well as the criteria for evaluating rate-case expense requests. In light of these revisions to the evidentiary requirements in the adopted rule, the commission is persuaded by the comments of various parties that in most circumstances, the calculation of the disallowance of specific rate-case expense amounts should now be based directly upon the amount of rate-case expenses found to be unreasonably incurred. As discussed in greater detail below, the commission has revised subsection (d) of the rule

to provide that in most circumstances, the presiding officer will disallow or recommend disallowance of recovery of rate-case expenses equal to the amount shown to have not been reasonably incurred under the criteria in subsection (c). In light of these changes, and as discussed more fully below, the commission concludes that it is not necessary to adopt subsection (d)(1) of the proposed rule (the 50/50 Method) at this time, but the commission maintains that adoption of that methodology is within the commission's discretion.

The commission agrees with TIEC's comments that the possibility that a utility and its shareholders may be held accountable for rate-case expenses increases the utility's incentive to undertake cost-effective and efficient litigation strategies, and encourages the utility to act more like a private litigant. As discussed more fully below, the commission has added subsection (c)(5) to the criteria for evaluating the reasonableness of rate-case expenses in the adopted rule to permit the commission to disallow rate-case expenses that are, as a whole, disproportionate, excessive, or unwarranted to the nature and scope of the rate case at issue. The commission finds that this provision, along with the other criteria in subsection (c) of the adopted rule, provides the proper incentives for utilities to monitor their costs and avoid unreasonable expenditures.

The commission agrees with Joint Utilities' comments that any rule adopted in this proceeding must comply with the *Oncor* precedent and concludes that the adopted rule is consistent with that precedent. The commission further agrees with Joint Utilities that the commission cannot presume that rate-case expenses are unreasonable just for the sake of requiring shareholders to pay for the presumed benefit of filing a rate case. However,

without stating a definitive interpretation of the *Oncor* precedent, the commission finds that it continues to retain substantial discretion under PURA §36.061 to disallow utility rate-case expenses even after the *Oncor* decision. At a minimum, the commission finds that the *Oncor* decision does not, even if interpreted in the broadest possible fashion, mandate that utilities be permitted to recover unreasonably incurred rate-case expenses.

As noted by TIEC, PURA §36.061 provides that the commission "may" allow a utility's reasonable rate-case expenses. Consistent with the commission's authority to permit recovery of "reasonable" rate-case expenses, subsections (b) and (c) of the adopted rule set forth the general requirements for establishing and evaluating the reasonableness of rate-case expense requests. Subsection (d) then provides that the presiding officer shall disallow or recommend the disallowance of only those rate-case expenses that the commission has found to be not reasonably incurred. Subsection (d) then provides two specific methodologies to quantify such a disallowance in circumstances in which either the overall rate-case expenses were disproportionate, unwarranted or excessive, or when the presiding officer cannot reasonably determine the appropriate disallowance of unreasonable rate-case expenses associated with a particular issue. The commission finds that this approach is entirely consistent with the *Oncor* decision, and the commission declines to make any changes to the published rule on this basis.

2. *Should rate-case expenses incurred for purposes of reducing a utility's commission-authorized Texas jurisdictional retail revenue requirement be allocated to and collected from ratepayers in a manner different from the allocation and collection of rate-cases expenses incurred for the purpose of shifting costs among Texas jurisdictional retail customer groups? If so, how should the commission determine the amount and recovery method of the costs associated with these categories of expenses?*

Water IOUs, State Agencies, the Alliance, OPUC, El Paso, TML, and Oncor Cities responded "no" to this question. State Agencies commented that there is no advantage to allocating rate-case expenses any differently among the classes on a functional basis and, additionally, doing so would add unnecessary complications and disputes to a review of rate-case expenses. The Alliance commented that the great majority of the municipal rate-case expenses are on revenue-requirement issues, which benefit all ratepayers, and trying to segregate rate design expenses from revenue-requirement expenses is inefficient and could increase the overall costs. The Alliance also noted that its participation in rate-making proceedings is not limited to a particular class of customers; rather, members of the Alliance participate in ratemaking proceedings with the interests of all ratepayers. OPUC commented that with regard to the way this question applies to a utility company, rate-case expenses related to shifting costs among customer groups should be paid by all classes. OPUC stated that utilities typically bring each class to cost in the cost-of-service study, only rarely applying other ratemaking principals such as gradualism. OPUC stated that the utility's interest is in recovering its costs, not in ensuring that a certain class is allocated costs in a certain way, and that carving out costs related to the allocation of expenses among the Texas retail rate classes would only add to the costs of the rate case and to its litigiousness, and where the line would be drawn is equally ambiguous.

With regard to these issues, OPUC raised the following points: Would one class be assigned more rate-case-expense costs because it has more intra-class issues at stake? If a class has more sub-classes, would that warrant a greater proportion of the costs because testimony would have to cover more topics? Would more costs be assigned to the class with the biggest rate increase?

Would the calculation be based on the actual dollars or would it be based on who was furthest from unity? What if the utility proposed an intra-class allocation issue that was controversial and resulted in significant discovery, testimony, and briefing? OPUC stated that such issues vary from case to case, and that there is not a sufficient policy reason to justify treating these rate-case expenses differently from any other expense. OPUC submitted that the cost allocation derived in the rate case and approved by the commission is based upon the cost to serve each of the classes, and that no further delving down is necessary or appropriate. OPUC opined that applying the allocation from the rate case to the rate-case expenses is sufficient to ensure an equitable allocation of costs among the classes.

OPUC further stated that applying such a standard could also have a chilling effect on settlement negotiations if some parties feel hamstrung regarding their ability to negotiate without penalty. OPUC commented that a prudent attorney would have to consider whether to risk having rate-case expenses allocated more heavily to her class before asking the utility questions or engaging in negotiations with them.

OPUC also commented that the question also arises as to how it would be decided in any given case which class or classes would share these costs, as no set standard could reasonably be set forth in a rule because the focus may shift from case to case. OPUC stated that adding a new requirement of a different allocation of rate-case expenses for the portion related to cost allocation among classes would inevitably lead to a more adversarial litigation process, both in the rate case itself and in any rate-case expense docket.

Oncor Cities and the Alliance echoed these points, noting that as part of litigating rate-case expense amounts, parties would then need to propose (and respond to) possible allocation of those expenses within the classes. The Alliance also noted that tracking rate-case expenses related to specific issues would likely result in the expenditure of added expenses for little or no gain. Oncor Cities submitted that the current approach—allocation of the expenses to all retail customer classes in proportion to each class's share of the total revenue requirement—is straightforward, reasonable, and should continue.

El Paso commented that the question is predicated on two incorrect assumptions. The first incorrect unstated basis of this question assumes that a municipality represents an interest or interest of particular classes over other classes, rather than a fair allocation of costs among all customer classes. El Paso commented that the only statutory party charged with representing the interest of a particular class is OPUC, which is charged with representing the interest of residential and small commercial customers. Municipalities, particularly when considered with the statutory function of the regulator with original jurisdiction, do not specifically represent one class or group of customer classes. El Paso stated that the second incorrect unstated basis assumes that a party that disagrees with the position put forward by the company is attempting to shift costs among customer classes or groups, and that the utility is itself not attempting to shift costs. The assumption that one party or another is attempting to "shift costs" rather than recommend or pursue an allocation of costs that results in just and reasonable rates is never explicit in any evidentiary proceeding. El Paso stated that, moreover, it is probable that no witness on allocation of costs ever testifies that the proposed allocation results in anything other than just and reasonable rates.

Oncor Cities stated that rate-case expenses should be allocated and collected system-wide, regardless of whether the expenses were directed toward the utility's revenue requirement or toward cost allocation or rate design issues. Oncor Cities commented that, currently, municipal rate-case expenses are treated as a regulatory expense and are allocated to all retail customer classes in proportion to each class's share of the total revenue requirement, and that it is not clear how allocation of rate-case expenses to particular classes might work in some other manner, particularly given the fact that most participants in rate cases have accounts in several different rate classes.

Oncor Cities also commented that this question could be premised on the notion that municipal rate-case expenses in the cost-allocation and rate design phase of a case should be assigned to the classes in which municipal accounts are found, and that if so, that understanding of the issues fails to account for the complexity of the rate design issues in a rate case. Cities stated that municipal intervenors typically have delivery points in the lighting, small and large secondary, and even primary and transmission classes; but at the same time, Oncor Cities participate in rate cases to protect the interests of the residential, commercial, and even industrial customers within city limits. Oncor Cities additionally stated that municipal accounts are usually not the only accounts within a particular class, meaning that a city's efforts and success will also benefit non-city customers, and for these reasons, it makes little sense to allocate municipal rate-case expenses to particular classes based on a purported benefit to cities.

Oncor Cities further commented that if this question contemplates directly assigning cost-allocation and rate design rate-case expenses only to customers in participating municipalities, the case for such an allocation is even weaker. Oncor Cities stated that a city position that benefits a particular rate class benefits all customers in the class, not just the city accounts within that class, and that it would be inequitable to require customers within participating cities' boundaries to bear the expense of litigating that position alone. Oncor Cities noted that multiple other customers are usually found within all of a utility's rate classes, not just city accounts, and that this can even be the case in the lighting class, where other institutions or governmental bodies have accounts for different kinds of lighting. Oncor Cities submitted that a direct assignment of rate-case expenses only to customers in participating cities would be a punitive deterrent against city participation in ratemaking proceedings; also, allocating city rate-case expenses only to customers within the participating municipalities' boundaries would create a free rider problem because a city declining to participate in the case would exempt that city's ratepayers from the cost of participation, while all ratepayers within the rate class would still benefit from the work of any cities who do participate.

Oncor Cities also commented that collecting municipal rate-case expenses only from customers found within city limits would impair and needlessly complicate the retail electric market. Oncor Cities noted that in the Energy Efficiency Cost Recovery Factor cases processed in 2012, the commission considered whether to directly assign municipal intervenors' rate-case expenses to customers within the participating cities. Oncor Cities pointed out that the commission ultimately declined to allocate rate-case expenses in this manner, and in the course of that deliberation, Retail Electric Providers (REPs) filed a brief outlining their concerns. Oncor Cities

stated that, according to the REPs, direct assignment of municipal rate-case expenses would "increase costs to all customers . . . by creating complexity and new administrative costs that all customers will pay," and that same dynamic would exist with respect to direct assignment of the cost of litigating cost- allocation and rate design issues, as doing so would create a patchwork of different city-by-city rate-case expense surcharges that would be costly and difficult for the retail electric market to navigate.

Oncor Cities also responded by noting that the question may be suggesting that the cost of pursuing cost allocation/rate design issues that are lost should only be recovered from the rate classes of the party pursuing such issues. Oncor Cities stated that the commission's current practice approximates the kind of allocation to which this question appears to be directed, and as noted above, the commission's current practice is to allocate rate-case expenses to the classes in proportion to their share of the revenue requirement. Oncor Cities commented that when a party litigates and loses a cost allocation/rate design issue, the relevant rate class bears a larger portion of the revenue requirement than if that party won the issue; accordingly, losing a cost allocation/rate design issue leads to the relevant class bearing a larger portion of the rate-case expense reimbursement. Oncor Cities submitted that much of what this question could portend is therefore already part of the commission's current practice on the allocation and collection of rate-case expenses.

TIEC expressed its position that all municipality rate-case expenses should be allocated and collected from customers solely within the corporate boundaries of the intervening cities. TIEC stated that customers outside cities have no ability to influence either the positions taken by

intervening municipalities or the expenses incurred in advocating them, and while there may be benefits to other customers from revenue requirement adjustments identified by cities, there are many issues that industrial customers identify and litigate that also benefit other customers, but the costs of litigating these issues are not collected from other customers that are not TIEC members. TIEC stated that the commission should align the costs and benefits of each litigant's participation by assigning the costs of participation for cities to the customers that reside within those cities that have control over the participation; otherwise, municipality rate-case expenses act as an indirect tax for customers located outside the municipality's jurisdiction. TIEC commented that if the commission continues, however, to allocate municipalities' rate-case expenses to customers that are not within the municipality, this should apply only to revenue requirement issues, and not issues that shift costs from one class to another. TIEC noted that Oncor Cities primarily represent the interests of residential and commercial customers, who are often at odds with industrial customers on cost allocation issues; nonetheless, large customers pay municipality rate-case expenses for litigation and settlement of cost allocation and rate design issues. TIEC contended that to determine the amount of rate-case expenses associated with revenue requirement issues versus cost allocation issues, the commission should require municipalities to submit time records that track litigation costs by category, with sufficient detail for effective review. TIEC stated that as long as consultants and counsel are on notice of this requirement up front, it should not be difficult for municipalities to identify which litigation costs relate to revenue requirement disallowances, and which related to cost allocation and rate design.

TIEC further stated that, contrary to the statements of some municipalities in their initial comments, it is not accurate that municipalities represent the interests of all customer classes.

TIEC pointed out that for various reasons related to siting, municipal fees and ordinances, and other issues, most industrial facilities are located outside municipal limits, and as a result, municipalities' interests have historically been biased in favor of residential and small commercial customers, and municipal cost allocation and rate design proposals have historically disadvantaged large, energy-intensive industrial customers. TIEC expressed its belief that while municipalities' rate-case expenses should all be borne by customers within the city limits, as discussed above, municipalities' disparate representation of smaller customers makes it particularly appropriate for any rate-case expenses related to cost allocation and rate design to be borne by municipal customers, rather than shifted to other customer classes to whom the municipalities' interests are adverse.

Houston and OPUC stated strong disagreement with TIEC on these points, with Houston stating that allocating municipal rate-case expenses solely to customers in intervening cities is unjust, discriminatory, and would harm all ratepayers. OPUC noted that TIEC's position ignores the benefits that customers outside municipal boundaries receive when municipalities participate in rate cases. Houston and El Paso additionally commented that if a rate case is filed with a city exercising its regulatory authority, the city is obligated to evaluate the rate-change request. Houston also pointed out that if a rate application is filed in which the utility seeks system-wide rates, municipal regulators have no option but to consider and review the rate filing package inclusive of both environs and municipal customers, and Houston stated it is not aware of any claims that the overall worth of municipal actions in rate proceedings does not provide benefits to all ratepayers.

Joint Utilities stated that to the extent utilities or municipalities unreasonably incur rate-case expenses in the rate design portion of a proceeding, those unreasonable costs can be disallowed based on the factors provided in subsection (c) of the proposed rule. Joint Utilities stated, however, that the commission should retain the discretion to allocate reasonable rate-case expenses to particular customers if there are compelling reasons to do so. Joint Utilities argued that, for example, if a municipality participates in a commission proceeding for the sole purpose of pursuing a theory of allocation of costs that would benefit only its citizens, the commission should retain the discretion to allocate that municipality's rate-case expenses to the citizenry of that municipality; similarly, if a non-municipal intervenor pursues frivolous arguments causing the utility or municipalities to incur additional rate-case expenses, the commission should have the discretion to assign the utility's or municipality's rate-case expenses incurred to defend against such claims to the customer classes represented by the party causing such expense. Joint Utilities commented that the commission may retain its discretion to make such allocation decisions by either addressing that issue in each case as needed and not addressing it in the rule, or by adding appropriate language to the rule.

Oncor Cities commented in reply that Joint Utilities cannot have it both ways by expressing a willingness to have cities' rate-case expenses directly assigned in a manner to which Joint Utilities object when it comes to their own rate-case expenses.

Commission response

The commission agrees with the comments of TIEC that municipal participants often favor the interests of certain customers or customer classes over others, and may incur

significant rate-case expenses litigating positions that do not benefit all ratepayers. Requiring the collection of municipal rate-case expenses related to revenue allocation and rate design issues from all customers may, in some cases, introduce significant inequities. Accordingly, in some cases, it may be preferable to assign the cost of litigating certain issues to in-city customers.

However, the commission finds that these issues should be assessed on a case-by-case basis. Accordingly, the commission declines to mandate a specific treatment for the allocation and collection of rate-case expenses based upon a division between revenue requirement-related expenses and allocation-related expenses in the adopted rule. The commission agrees with Joint Utilities that the commission should retain the discretion to allocate reasonable rate-case expenses to particular customers if there are compelling reasons to do so. The commission finds that it continues to possess the broad discretion to allocate rate-case expenses to particular customer groups in individual proceedings in which such treatment may be appropriate under the rule as adopted.

The commission disagrees with the comments of OPUC, Oncor Cities, and the Alliance that it would be unduly burdensome to require the segregation of and accounting for rate-case expenses based upon a division between revenue requirement issues and allocation issues in all proceedings. As discussed below, the commission has determined that it is appropriate to incorporate a new subsection (b)(6) into the adopted rule, that requires the parties to specify those rate-case expenses reasonably associated with each issue in a proceeding.

3. *Should the commission require that rate-case expenses be evaluated in the proceeding in which they are incurred unless the commission authorizes their consideration in a future proceeding?*

OPUC, State Agencies, El Paso, and Houston generally responded affirmatively to this question. OPUC and Houston commented that in some proceedings, especially those that end in settlement, inclusion of rate-case expenses is appropriate; in other cases in which the rate-case expenses would be better evaluated in a separate docket, commission authorization is appropriate. OPUC stated that, depending on the facts of a particular case, there can be appropriate circumstances for either considering the rate-case expenses in the same proceeding in which they occurred or in a future proceeding, and it is appropriate for the commission to adopt a rule that retains the flexibility to handle either situation.

OPUC, El Paso, and Houston stated that requiring commission authorization to defer consideration of rate-case expenses until a future proceeding reduces uncertainty and is appropriate because of the inequities at risk in deferring expenses to the future. El Paso and Houston opined that it should be less costly to determine the expenses in the context of the proceeding for which they are incurred, rather than an additional proceeding convened expressly for that purpose.

State Agencies commented that because the commission has determined that it will not allow rate-case expense based upon estimates of future costs, and costs continue to accrue through the hearing and post-hearing proceedings, the commission generally authorizes the severance of rate-case expenses into a separate proceeding. State Agencies commented that while this allows costs

to be fully explored through the ordinary discovery process, parties can and should retain the ability to settle rate-case expenses as part of a total rate-case resolution.

The Alliance stated that it believes that the current process, where the commission defers the review of rate expenses to a later proceeding, has worked well. The Alliance commented that the current process allows the parties and the fact finder to focus on completing the rate case, rather than simultaneously reviewing the rate-case expenses as well; furthermore, the final tally of the rate-case expenses for the proceeding before the commission is not available until well after the record is closed, given that parties file briefs, exceptions, and motions for rehearing. The Alliance suggested that should the commission move to a process where rate-case expenses are evaluated in the proceeding in which they are incurred, the commission should revisit its current practice of not allowing recovery of estimated rate-case expenses. TML agreed with this point.

Oncor Cities commented that the commission's current practice is to consider parties' rate-case expense requests in a severed proceeding, separate from the underlying rate case, and that since 2011, municipalities are not permitted to recover amounts that are estimated to be necessary to complete a case or to participate in the appellate process. Oncor Cities commented that under the prior practice, rate-case expenses were an issue in the actual rate case, with the commission quantifying an estimate for municipal intervenors to complete the case (and participate in any appeals) subsequent to a specified quantification date. Oncor Cities commented that intervenors in such cases did not receive any of the estimated reimbursement amounts until the associated work was performed and the invoices were submitted to the utility; instead, the estimate represented a budget for that work that was found to be reasonable in the underlying rate case.

Oncor Cities expressed its continued support for this pre-2011 approach to quantifying rate-case expenses, and stated that, provided that municipal intervenors may quantify a cost estimate for work completed after the rate-case expense quantification date, this approach results in no further litigation of parties' rate-case expenses and resolves all related issues in one proceeding. Oncor Cities submitted that the current practice of severing expenses into a separate proceeding conducted after the underlying rate case prolongs litigation and increases parties' expenses, and it provides no feasible means of recovery of the cost of municipal intervenors' participation in the appellate process, a cost which is recoverable pursuant to PURA §33.023(a)(2). Oncor Cities stated that without quantification of a reasonable estimate for such work, municipal intervenors must wait until the utility's next rate case to seek recovery of their appellate expenses related to the utility's last case, and in the current era of the commission, the time between rate cases can be significant, leaving municipal intervenors no means to recover the cost of appealing those cases in the intervening time. Oncor Cities noted that instances of municipalities initiating a rate case via a show cause proceeding are relatively rare, consisting of approximately four such cases, and if municipal intervenors would otherwise be required to wait a number of years between rate cases filed by the utility that serves them, those municipalities might be compelled to initiate rate cases simply to recover their reasonable rate-case expenses from the utility's prior case. Oncor Cities stated that quantification of reasonable rate-case expenses during the underlying rate case, and allowance of an estimate, is preferable to this costly and involved route.

LCRA and Water IOUs stated that while they believe the better practice is to require that rate-case expenses be evaluated in the proceeding in which they are incurred, it is not necessarily always the best approach. Water IOUs recommended that the commission refrain from making

this a requirement in the rule. LCRA stated that this general approach has been followed in its three most recent rate cases and has worked efficiently, but noted that in two of these three cases, the commission also authorized consideration of certain rate case related expenses in a future rate proceeding to the extent these rate-case-related expenses were incurred after a specific date established by the commission. LCRA and Water IOUs commented that despite what may be considered a better practice, unforeseen circumstances may require the consideration of rate-case expenses not previously authorized and a utility should be given the opportunity to demonstrate in a separate proceeding—however difficult that may be—that its rate-case expenses are reasonable. LCRA stated that the commission should not enact a hard and fast rule that precludes consideration of post-hearing rate-case expenses.

Mr. Baron commented that the commission should consider the converse of the approach indicated in the question—that is, the commission should direct that rate-case expenses be evaluated in a follow-up proceeding unless the commission authorizes otherwise. TML agreed with this point, and the Alliance commented that the commission should retain the option of reviewing rate-case expenses in a separate proceeding once all the rate-case expenses are quantifiable.

Joint Utilities responded "no" to the question, stating that rate-case expenses can be incurred in proceedings before municipal regulators, in cases before the commission, or in courts on appeal of rate decisions. Joint Utilities noted that, as discussed in *Oncor*, PURA provides for recovery of reasonable rate-case expenses in each of these scenarios, and while some rate-case expenses incurred at the commission can be evaluated in the proceeding in which they are incurred

(although sometimes even those expenses are intentionally severed for consideration at a later time), some rate-case expenses are not available for review by the commission until they are presented in a later proceeding—as is the case in municipal proceedings that do not get appealed to the commission (which was the subject of the *Oncor* case), or in appeals of rate decisions to the courts (that may or may not result in a remand proceeding where those expenses can be reviewed).

Joint Utilities submitted that the simplest solution to address the various scenarios in which reasonable rate-case expenses can be incurred is for the commission to include language in the proposed rule that allows a utility to either seek recovery of rate-case expenses in the proceeding in which they were incurred or create a regulatory asset for those expenses and defer cost recovery until the next general rate case or a proceeding brought solely to review rate-case expenses. Joint Utilities opined that this approach would allow utilities the opportunity to recover their reasonable rate-case expenses regardless of the scenario in which they were incurred, consistent with *Oncor* and PURA.

El Paso commented that the commission should reject Joint Utilities' proposal for a regulatory asset, and argued that if the utility takes the position that it will not reimburse the municipality until a finding of reasonableness by the commission, that municipality can be left waiting years for a proceeding to finish and get reimbursed. El Paso stated that under Joint Utilities proposal, the utility earns a return on the time value of its funds, but the municipalities are left waiting, with no compensation for the wait.

The REP Group did not take a position on whether the commission should evaluate rate-case expenses in the original proceeding or authorize a future docket for their consideration, but stated that if the commission chooses to authorize the consideration of such expenses in a future proceeding, the filing utility should be required to provide adequate notice of the resulting rate-case expenses. The REP Group recommended that the affected utility provide notice to REPs of the approved rates not later than the 45th day before the date the rates take effect, as a 45-day notice requirement will allow REPs to incorporate the new rate-case expense amount into their invoices to end-use customers. The REP Group noted that 45 days has been generally recognized in commission rules as providing a sufficient amount of time for to REPs to adjust business processes and prices to incorporate rate revisions. The REP Group additionally commented that the time periods in which changes in rates for rate-case expense can take effect should be limited, and that any approved rate-case expenses should be implemented on a semi-annual basis at most. The REP Group stated that a limitation of rate-case expense implementation to a semi-annual basis would help limit the number of times that a REP may revise its rates as a result of changes to the rate schedule of a utility, and suggested that the appropriate schedule for any rate-case expense adjustments would be March 1 and September 1, consistent with the regularly scheduled semi-annual Transmission Cost Recovery Factor (TCRF) updates.

Commission response

The commission declines at this time to mandate that rate-case expenses be evaluated in the proceeding in which they are incurred. Conversely, the commission also declines to adopt the comment by Mr. Baron that the commission direct recovery of rate-case expenses in a

follow-up proceeding unless the commission otherwise authorizes. The commission agrees with the comments of a number of parties that the issue of whether rate-case expenses should properly be considered in the same proceeding or in a separate, future proceeding depends on the specific circumstances of the request. Accordingly, the commission declines to adopt any changes to the published rule that would limit its general flexibility in addressing the appropriate process of reviewing and awarding rate-case expenses.

The commission also declines to adopt Joint Utilities' proposal to amend the published rule to authorize the creation of a regulatory asset for those expenses and defer cost recovery until the next general rate case or a proceeding brought solely to review rate-case expenses. The commission agrees with El Paso that such a mechanism could potentially allow utilities to earn a return on the time value of its funds while potentially delaying municipalities from recovering their own reasonable rate-case expenses with similar interest. The commission also reiterates that it retains the authority to authorize the creation of these types of regulatory assets if the circumstances warrant, but does not conclude that a general rule is appropriate at this time.

4. *Is it appropriate for intervening municipalities to be subject to P.U.C. SUBST. R. §25.245(d)(3)(B) as proposed?*

El Paso, State Agencies, Oncor Cities, the Alliance, and Houston responded "no" to this question. El Paso, Houston, and the Alliance noted that because the municipality has the obligation to evaluate all the issues in a proceeding, such a rule would controvert the statutory responsibility of the municipalities. El Paso additionally commented that the complexity of the

case as well as the determination of rate-case expenses will actually cause more expenses that must be tracked issue-by-issue. State Agencies and Oncor Cities commented that tying municipal rate-case expenses to success in achieving a specific outcome runs counter to PURA, and that the legislature has determined that municipal regulatory authorities should be provided with resources to review a rate filing and *shall* be entitled to have their reasonable expenses reimbursed. State Agencies, Houston, and Oncor Cities noted that restricting a municipality's ability to be reimbursed for its costs of reviewing and litigating its position would put it at a disadvantage that the legislature did not intend, with Oncor Cities further noting that the rule would penalize cities merely for losing issues in a case. Houston further noted that the rate-case expenses borne by ratepayers are typically minimal compared to the benefits achieved through municipal intervention.

The Alliance commented that municipalities do not control the issues raised by a utility, but respond to the proposed increases, and that penalizing the municipalities for trying to minimize increased costs for ratepayers is unfair. The Alliance stated that a more equitable approach is to maintain the status quo, where the finder of fact decides on a fact-specific basis whether the municipalities' rate-case expenses are reasonable.

Mr. Baron responded that the proposed subsection (d)(3)(B) is not needed and should be omitted if the rule requires utilities and municipalities to track their actual rate-case expenditures by issue. Mr. Baron stated that if a municipality unreasonably litigates an issue with no reasonable basis in law, policy, or fact, the municipality's litigation expenses can and should be disallowed.

El Paso expressed general agreement with these points, and stated that a municipality's expenses should not be subject to the formulaic concepts in proposed subsection (d).

Joint Utilities, LCRA, and Water IOUs responded "yes" to this question, although these commenters expressed the position that subsection (d) should not be adopted. These commenters stated that if the commission adopts subsection (d), it and all other provisions in the rule should be applied equally to utilities and municipalities. Joint Utilities noted that, consistent with PURA, the *Oncor* decision establishes that both utilities and municipalities are entitled to recover their reasonable rate-case expenses. Joint Utilities further commented that although PURA provides that utilities "may" recover their reasonable expenses, the court in *Oncor* interprets PURA as *requiring* that utilities be allowed to recover those expenses pursuant to the mandate in PURA §36.051 that utilities *shall* recover their overall revenues necessary to earn a return over their reasonable and necessary expenses. Joint Utilities stated that there is therefore no distinction between utilities and municipalities under PURA once reasonableness is established, and there should be no distinction under the commission's rules in determining the reasonableness of those expenses.

Commission response

As discussed in the commission's response to comments on subsection (b) below, the commission concludes that it is appropriate for utilities and municipalities to track their rate-case expenses by issue and provide, as part of their application to recover rate-case expenses, the specific issue or issues in the rate case and the amount of rate-case expenses reasonably associated with each issue. The commission further agrees with the comments

of Mr. Baron that the proposed subsection (d)(3)(B) is generally not needed in such circumstances. The commission disagrees, however, that such a provision is not needed altogether. Instead, as discussed more fully below, the commission revises the rule such that the Issue Specific Method, as set forth in subsection (d)(3)(B), may be applied to a municipality only in those circumstances in which the commission finds a disallowance of certain municipal rate-case expenses is appropriate and the municipality has failed to specify the amount of rate-case expenses reasonably associated with that particular issue or issues.

The commission disagrees with those commenters that suggest that applying the Issue Specific Method to municipalities would controvert the statutory responsibility of municipalities in rate proceedings. The commission again notes that the Issue Specific Method may only be applied in circumstances in which a municipality has both unreasonable expenses and has failed to specify the amount of rate-case expenses reasonably associated with the particular issue or issues for which the commission has determined a disallowance is appropriate. Further, in evaluating the reasonableness of a party's rate-case expenses, the rule, as revised, explicitly directs the presiding officer to consider the relevant factors listed in subsection (b) and any other factor shown to be relevant in a proceeding. As such, municipalities remain free under the commission's rule to argue in each proceeding that their expenses were reasonable given their statutory obligations or the nature of the utility's particular filing. Finally, the commission notes that the Issue Specific Method is discretionary, and the commission anticipates that it will

be applied solely in circumstances in which the application of this methodology will result in the disallowance of unreasonable municipal rate-case expenses.

The commission also disagrees with State Agencies and Oncor Cities that the application of subsection (d)(3)(B) to a municipality would violate PURA §33.023(b), which states that municipalities shall be entitled to have their reasonable rate-case expenses reimbursed. As discussed above, the Issue Specific Method would only be applied to a municipality in the quantification of unreasonably incurred rate-case expenses in situations in which the municipality failed to specify the issue or issues with which those rate-case expenses were reasonably associated. Conversely, subsection (d)(3)(B) would not be used to disallow any reasonable rate-case expenses. Accordingly, the commission finds that subsection (d)(3)(B), as adopted by the commission, is consistent with PURA §33.023(b).

The commission further agrees with other commenters such as the Alliance that the commission's rule should require the determination on a fact-specific basis whether a municipality's rate-case expenses are reasonable. Again, the rule as adopted retains the commission's flexibility in evaluating the reasonableness of a municipality's rate-case expenses in each proceeding. At the same time, however, the rule as adopted also puts those municipalities on notice that municipal rate-case expenses could potentially be subject to reductions based on the value of specific issues in a proceeding if the municipalities fail to present sufficient evidence under the adopted subsection (b)(6) for the commission to determine the issue or issues with which their unreasonable rate-case expenses were reasonably associated. The commission agrees with Joint Utilities, LCRA,

and Water IOUs that it is appropriate for the commission to retain the discretion to apply the Issue Specific Method to requests filed by municipalities, as well as utilities, in these circumstances.

Comments on Specific Sections of the Rule

Section (a) **Application.**
This section applies to municipalities and utilities requesting recovery of or reimbursement for rate-case expenses pursuant to Public Utility Regulatory Act (PURA) §33.023 or 36.061(b)(2).

Mr. Baron suggested the reference in subsection (a) of the proposed rule to PURA §33.023 should specifically reference subsection (b) of that section of PURA and suggested restating the first sentence of the subsection to read as follows: "This section applies to electric utilities requesting recovery of expenses for ratemaking proceedings (rate-case expenses) pursuant to Public Utility Regulatory Act (PURA) §36.041(b)(2) and to municipalities requesting reimbursement for rate-case expenses pursuant to PURA §33.023(b)." Mr. Baron further commented that his proposal to provide "rate-case expenses" as a defined term would clarify that the term "rate-case expenses" refers specifically to expenses incurred in ratemaking proceedings, a term that is defined in PURA §11.003(17). Mr. Baron also commented that subsection (a) should be modified to clarify that the new rule will apply to rate-case expenses incurred in rate cases initiated on or after 90 days following the date on which the rule is adopted in order to provide parties with adequate advance notice of the rule's requirements.

State Agencies responded that Mr. Baron's suggested 90-day delay for applying the rule is unwarranted. State Agencies commented that the commission's order in *Application of Entergy Texas, Inc. for Rate Case Expenses Pertaining to Docket No. 39896*, Docket No. 40295 (Docket

No. 40295) and the rulemaking process leading up to publication of this proposed rule indicate that utilities and municipalities have already been on notice regarding the proposed rule.

Commission response

The commission agrees with Mr. Baron that the reference in subsection (a) of the proposed rule to PURA §33.023 should properly reference subsection (b) of that section of PURA. The commission also adopts Mr. Baron's more precise statement of the entities affected by the new rule and the applicable provisions of PURA by striking the sentence in the published version of subsection (a) and replacing it with the following sentence: "This section applies to utilities requesting recovery of expenses for ratemaking proceedings (rate-case expenses) pursuant to Public Utility Regulatory Act (PURA) §36.061(b)(2) and to municipalities requesting reimbursement for rate-case expenses pursuant to PURA §33.023(b)." As recommended by Mr. Baron, the commission finds that this change clarifies that the term "rate-case expenses" refers specifically to expenses incurred in ratemaking proceedings, a term that is defined in PURA §11.003(17).

The commission declines to adopt any other proposed changes to this section. The commission agrees with State Agencies that an additional 90-day delay after the effective date of this rule is unnecessary to put parties on notice regarding the new rule's requirements. Additionally, the commission notes that the proposed rule will only apply to applications filed after the effective date of the rule and will not be applied retroactively.

Section (b) **Requirements for claiming recovery of or reimbursement for rate-case expenses.**

In any rate proceeding, a utility or municipality requesting recovery of or reimbursement for its rate-case expenses pursuant to PURA §33.023 or §36.061(b)(2) shall have the burden to prove the reasonableness of such rate-case expenses by a preponderance of the evidence. In order to establish its rate-case expenses, each utility or municipality shall detail and itemize all rate-case expenses and shall provide evidence, verified by testimony or affidavit, showing the reasonableness of the cost of all professional services, including but not limited to:

Mr. Baron recommended changes to subsection (b) that would define how a utility or municipality would establish its prima facie case. Mr. Baron also proposed deleting "In any rate proceeding" and "pursuant to PURA §33.023 or 36.061(b)(2)" from the first sentence of subsection (b) as published and to restate the second sentence as follows: "To establish its prima facie case, each utility or municipality shall detail and itemize all rate-case expenses for which recovery or reimbursement is requested, including but not limited to costs for attorney and other professional services, lodging, meals and beverages, and transportation." Mr. Baron proposed further changes to the third sentence of this paragraph to delete "including but not limited to" and replace it with the following language: "The evidence shall address" Mr. Baron commented that these changes would clarify that a utility or municipality must present evidence addressing, at a minimum, the issues listed in subsection (b).

Mr. Baron further commented that a more complete list of the evidence that must be provided to determine reasonableness and allowed expenses should be consolidated from subsections (b) and (c) into one subsection. Mr. Baron commented that some references to relevant evidence appear in subsection (b) while some appear in subsection (c). Mr. Baron proposed to better specify in subsection (b) the list of issues that an application must address. Specifically, Mr. Baron's proposed subsection would instruct the municipality or utility to provide evidence addressing (1) the extent of responsibilities assumed by the attorney or other professional in the rate case; (2)

the time and labor required and expended by the attorney or other professional; (3) the rates or other consideration paid to the attorney or other professional for the services rendered; (4) the benefits to the client from the services rendered; and (5) the nature and scope of the rate case, including the size of the utility and number and type of customers served, the amount of money or value of property at stake, the novelty and complexity of the issues addressed, the amount of discovery, and the occurrence and length of a hearing. As discussed below, Mr. Baron proposed retaining subsection (c) as a list of bases for the presiding officer to recommend a disallowance.

Joint Utilities replied that they are not opposed to Mr. Baron's revisions that clarify the rule by appropriately focusing on the evidence presented, the parameters of the reasonableness inquiry, and the calculation of disallowances based strictly on the amount of expenses actually incurred and shown to be reasonable and necessary by the record evidence as applied to the factors and criteria in subsections (b) and (c) with changes to certain provisions of his proposed rule language.

OPUC also replied that by revising the language to state that the utility or municipality establishes its prima facie case by submitting certain evidence, Mr. Baron's proposal essentially shifts the burden of proof from the utility or municipality to the other parties to show that certain rate-case expenses should not be recovered. OPUC argued that this momentous shift is poor public policy in that it removes part of the incentive for the utility or municipality to submit thorough, comprehensive evidence of its expenses; instead the utility or municipality could merely show that it has met the minimum requirements to submit *some* evidence on each factor, regardless of its adequacy, and the burden would then be on the other parties to point out the

deficiencies. OPUC pointed out that Mr. Baron's proposed change is contrary to the direction taken in recent commission cases where it has requested more information from the parties on expenses, indicating that sufficient information is not initially being submitted.

State Agencies replied that Mr. Baron's significant changes to the commission's proposed rule would effectively neutralize the meaningful review that the proposed rule was designed to effectuate and that his revisions, taken as whole, would detrimentally restrict the discretion of the commission to review rate-case expenses that will ultimately be borne by ratepayers. State Agencies argued that Mr. Baron's suggested revisions to subsection (b) first act to shift the burden of proof by establishing (without explanation) what amounts to a presumption that rate-case expenses are reasonable, a "prima facie" case achievable simply through filing a laundry list of information along with an affidavit, with no presiding officer determining whether the preponderance-of-evidence standard has been met. State Agencies pointed out that having set up a "prima facie case" presumption, Mr. Baron's subsequent revisions narrow the reasons that a presiding officer may rely upon to review and disallow any of the costs included in the "prima facie case" and that these revisions simultaneously raise the ratepayers' burden of proof.

State Agencies noted that as an example, under Mr. Baron's proposal, travel-related expense can be disallowed only if "extreme or excessive," notwithstanding any evidence that it was unnecessary to use higher cost alternatives because lower cost alternatives were readily available. State Agencies commented that none of Mr. Baron's proposals, limited only to reviewing the reasonableness of costs, incorporate the essential analysis of whether claimed rate-case expenses were also *necessary* for participation in a rate case and that in any event,

customers' responsibilities for costs should generally be far below that which rises to the level of "extreme or excessive." State Agencies argued that substitution of Mr. Baron's proposal for the commission's would not be in the public interest, because his revisions create a presumption that costs are reasonable and heighten the standard of evidence required for disallowance while also infringing on the commission's discretion to assess whether rate-case expenses are both reasonable and necessary, and the flexibility to address disallowances as the facts of a particular case may warrant.

With respect to subsection (b), the Joint Utilities recommended deleting Mr. Baron's proposed subsection (b)(5)(A), which lists "the size of the utility and number and type of customers," on the basis that a utility's size or customer count has no bearing on the reasonableness or necessity of the expenses incurred.

Mr. Baron further proposed that subsection (b) would include an additional sentence requiring that documents and other evidence be organized and detailed to enable a determination of the amount of expenses incurred for each major issue litigated in the rate case. Mr. Baron noted that such a requirement would provide accuracy in the event the commission were to disallow litigation costs related to a specific issue. Mr. Baron noted that, for example, if this information had been presented in Docket No. 40295, it would not have been necessary for the commission to resort to the application of the Issue Specific Method.

Joint Utilities requested that, if the commission chooses to require that documents and other evidence be organized and detailed to enable a determination of the amount of expenses incurred

for each major issue litigated in the rate case, that the commission limit this provision by inserting the phrase "to the extent practical."

Houston replied that it recognizes and appreciates the concerns Mr. Baron's proposed record-keeping requirement attempts to address, but that the recommendation presents a concern because requiring such a level of detail in each instance would be extremely burdensome and is not practical. Houston expressed concern that the proposed record keeping-requirement would potentially increase rate-case expenses and that due to the often abbreviated time-frame for review, requiring the allocation of additional time to record keeping, above and beyond the current level, would potentially interfere with the municipality's ability to conduct a comprehensive review of the rate filing package. Houston argued that the proposal does not consider that many activities are not related to a specific issue (*e.g.*, reading the filing), and that some efforts do not always result in an issue being raised for litigation purposes (*e.g.*, an issue turns out to be cost ineffective to pursue further or there is insufficient time available to adequately develop the issue). Houston further noted that the time to retain attorneys and consultants, review the filing, identify potential issues, develop information requests, review responses, perform analyses and develop written testimony is very limited due to the schedules mandated by state law and if attorneys and consultants are required to allocate time for each major issue during the review and analysis of a rate filing package, the potential result is a less comprehensive review and an increase in overall rate-case expenses. Houston pointed out that Mr. Baron's comments do not identify, nor is Houston aware of, any meaningful historical problem in this area applicable to the municipal regulator.

Oncor Cities replied that Mr. Baron's proposal is unnecessary, costly, and nearly impossible to accurately implement because not all time is spent by attorneys or even experts working on discrete issues in isolation and that large amounts of time are required to perform work not directly linked to a specific, major issue. Oncor Cities cited examples like an expert reviewing a utility's rate filing package in its entirety before issues are even fully developed or an expert preparing basic discovery requests to ask for clarification or supporting documentation for portions of the rate filing package. Oncor Cities pointed out similar examples for attorneys performing work not associated with particular substantive issues like preparation of lists of issues, negotiating procedural schedules, attending prehearing conferences, conducting settlement negotiations, and counseling intervenor cities on their exercise of original jurisdiction prior to consolidation of the city-level case with the associated commission appeal. Oncor Cities argued that even in other more issue-oriented tasks, parceling out total time spent into specific issue categories would be burdensome, such as attempting to track time spent on a wide-ranging, day-long deposition of an expert that addresses a number of issues. Oncor Cities noted that many ratemaking issues are complex and interconnected, and it would be difficult if not impossible to determine how to divide up the associated time spent. For those reasons, Oncor Cities recommended against the adoption of Mr. Baron's proposal on this point.

El Paso replied that Mr. Baron seeks to impose a requirement that is inconsistent with the type of review that must be accomplished by municipalities, or for that matter, the process by which a utility assembles a case. El Paso noted that the municipality is presented with a rate case filing that includes the testimony of many witnesses, a large number of schedules and many volumes of material that must be reviewed as a part of its analysis of the case. El Paso argued that the

matters that may need to be more carefully evaluated, and perhaps disallowed, are often not evident until such time as the discovery process is far along and that Mr. Baron's proposal does not limit expenses, but instead it makes the process of record keeping more difficult and will add to the expense if adopted. El Paso stated that the reasonableness question has arisen in potential detail in instances in which an argument or position may have been brought in violation of SOAH Rule §155.303, should that occur and that for the same reasons that proposed subsection (d) should not be adopted, Mr. Baron's proposed amendment to subsection (c) should not be adopted.

LCRA opposed Mr. Baron's proposal for several reasons, the first of which was that while some issues can be considered "major" from the beginning of a rate case, others become "major issues" when other parties choose to litigate them later in the course of the proceeding, and so a utility may not be able to organize its rate-case expenses at the beginning of a case in a manner that is consistent with the issues that ultimately become "major" issues only after litigation begins. LCRA also replied that requiring that every person who works on a rate case to record his or her time by issue would affect the number of time records that would need to be kept and increase the chances that a legitimate expense could be waived or forfeited simply because it was misfiled in the wrong category or given a more general description. LCRA argued that not only is it unreasonable to require the amount of effort necessary to describe activities by "major issue," but mandating such detailed information on invoices, and then requiring that those invoices be filed or produced in discovery during a case could provide a roadmap to counsel's litigation strategy by providing a window into the time and effort a party's outside counsel or experts are spending on certain issues while the those issues are still being adjudicated. LCRA

stated that this is inappropriate and the commission should reject recommendations that documents and evidence related to rate-case expenses be kept by issue.

Water IOUs replied that Mr. Baron's proposal is impractical, unwieldy, and unworkable since multiple issues are often worked on simultaneously.

State Agencies replied that Mr. Baron inaccurately perceives that the utility's problem in Docket No. 40295 was simply the failure to document specific costs for specific issues "because the utility lacked notice of any requirement to segregate costs by issue." State Agencies argued that this issue-allocation becoming part of the "prima facie case" that Mr. Baron proposed has a surface appeal. State Agencies noted that the primary objective of such record-keeping is expressly stated by Mr. Baron: to "obviate the need" for the commission to use an important tool in the exercise of its discretion, the "Issue Specific" method in subsection (d) of the proposed rule. However, State Agencies stated that, leaving aside the practical problems of whether and how that could be done, this record-keeping exercise plainly would increase rate-case expenses.

OPUC recommended deleting or limiting the provision allowing expenses to be proven or verified by affidavit. OPUC pointed out that if the costs supported by affidavit become an issue, allowing affidavits to suffice as support impairs the other parties' ability to question the sponsor of the evidence through discovery and cross-examination and that under the Texas Rules of Evidence, affidavits are hearsay. OPUC recognized that there may be circumstances in which affidavits might prove useful, for instance if the commission wishes to allow the use of affidavits in order to increase the efficiency of the process and reduce costs. OPUC commented that the

rule should include a provision allowing parties who contest the evidence verified by affidavit to have discovery answered by the affiant or an expert witness and be allowed to cross-examine the affiant or an expert witness who can adopt the statements made by the affiant. OPUC suggested that in the alternative, the rule could include a provision allowing for verification by affidavit when the rate-case expense request is unopposed.

Joint Utilities commented that they support language in the rule that allows a utility or municipality to support its evidence by affidavit but that they do not oppose a requirement that the affiant be made available for cross-examination.

Commission response

Comments relating to the burden of proof in rate-case expense proceedings

The commission declines to adopt the additional language proposed by Mr. Baron that relates to the establishment of a prima facie case for the recovery of rate-case expenses. The commission agrees with OPUC and State Agencies, which stated that Mr. Baron's proposed language shifts the burden of proof from the utility or municipality to the other parties to show that certain rate-case expenses should not be recovered. The commission agrees with OPUC and State Agencies that Mr. Baron's proposed changes could unduly restrict the commission's discretion to consider the full range of evidence necessary to evaluate the reasonableness of a particular request for the recovery of rate-case expenses by in essence establishing a limited list of evidence necessary to present a "prima facie"

case. The result would be to shift the burden to parties challenging the reasonableness of particular expenses and potentially preclude the commission from disallowing certain items that have met the threshold test but would be unreasonable upon full consideration of all relevant evidence.

The commission instead adopts the following sentence in place of the second sentence of subsection (b) of the published rule: "A utility or municipality seeking recovery of or reimbursement for rate-case expenses shall file sufficient information that details and itemizes all rate-case expenses, including, but not limited to, evidence verified by testimony or affidavit, showing," which, as discussed below, will be followed by a list of evidence that must be presented in order for an application to be considered to be sufficient for further processing. The commission finds that this change specifies clearly that the burden of proof to establish the reasonableness of particular rate-case expenses is not shifted away from the party requesting recovery of or reimbursement for its rate-case expenses and better notifies parties of the evidence necessary to constitute a sufficient application. While recognizing the comments provided by parties who indicated that some of the language proposed by Mr. Baron was unduly restrictive, the commission finds that adoption of this provision does not restrict the commission's discretion. The commission notes that subsection (b) as adopted now merely lists the evidence that must be presented in a complete application, but subsection (c) states that the presiding officer shall consider all relevant factors, including those not listed in subsection (b).

New criteria adopted in subsections (b)(1)-(5)

The commission finds that many of Mr. Baron's proposed changes to the list of evidentiary requirements in subsection (b) are meritorious. Mr. Baron proposed deletion of the list present in the published version of subsection (b) and adoption of his proposed list of evidentiary requirements. Mr. Baron's proposed list would instruct the municipality or utility to provide evidence addressing (1) the extent of responsibilities assumed by the attorney or other professional in the rate case; (2) the time and labor required and expended by the attorney or other professional; (3) the rates or other consideration paid to the attorney or other professional for the services rendered; (4) the benefits to the client from the services rendered; and (5) the nature and scope of the rate case, including: (A) the size of the utility and number and type of customers served, (B) the amount of money or value of property at stake, (C) the novelty and complexity of the issues addressed, (D) the amount of discovery, and (E) the occurrence and length of a hearing.

The commission adopts item (1) from Mr. Baron's proposed list but rewords it to state "the nature, extent, and difficulty of the work done by the attorney or other professional in the rate case" in order to better reflect the range of factors regarding which evidence should be submitted. The commission adopts item (2) from Mr. Baron's proposed list. The commission also adopts item (3), but, for the same reasons discussed regarding subsection (c)(1) of the proposed rule, the word "rates" is changed to "fees." Additionally, the commission adopts item (5) as proposed by Mr. Baron but changes "the amount of discovery" to "the amount and complexity of discovery" in order to better clarify that both

the amount and complexity of discovery are both relevant factors for the presiding officer's consideration.

The commission agrees with Mr. Baron, who stated that that these changes consolidate into one subsection a more complete list of the evidence that must be provided relating to the factors that will be considered. The commission finds that the revised evidentiary requirements require the presentation of all of the factors listed in the rule as published, except for the issue of the benefits to clients from the services rendered, but explains in better detail and with more clarity precisely which issues a complete application will address.

Additionally, the commission declines to include in the first two sentences of subsection (b) Mr. Baron's proposed language referring to costs for attorney and other professional services, lodging, meals and beverages, and transportation. Instead, the commission inserts the requirement to present evidence regarding costs for attorney and other professional services, lodging, meals and beverages, and transportation as subsection (b)(4) in order to more clearly communicate to parties that each of these categories of expenses is an issue that must be addressed in a party's application. This clarification aids in the achievement of the commission's goal of providing clear evidentiary standards and specific criteria for the review and determination of the reasonableness of rate-case expenses.

State Agencies commented that none of Mr. Baron's proposals, limited only to reviewing the reasonableness of costs, incorporate the essential analysis of whether claimed rate-case

expenses were also necessary for participation in a rate case. As discussed above, PURA provides an overall "reasonableness" standard for rate-case expense recovery. The rule as adopted complies with the "reasonableness" standard required by PURA. The commission expects that nearly all unnecessary expenses will be found to have been unreasonably incurred using the criteria provided by the rule and will be appropriately disallowed. Accordingly, the commission disagrees with State Agencies' contention that those proposed evidentiary criteria, as adopted by the commission, are not in the public interest.

Requirement that rate-case expenses be reasonably segregated by issue

The commission has determined that it is appropriate to adopt the requirement that the rate-case expenses are tracked and identified according to each litigated issue from the underlying rate case with which they are reasonably associated, as proposed in Mr. Baron's comments. The commission finds that adoption of this requirement will aid in the efficient processing of rate-case expense proceedings and will decrease the likelihood that a methodology, such as those found in subsection (d) of the adopted rule, will be required. The commission finds that, in most cases, the calculation of the disallowance of specific rate-case expenses should be based directly upon the amount of rate-case expenses found to be unreasonably incurred. This goal is more likely achieved following the adoption of this provision. Although Mr. Baron proposed a new sentence following the list of factors in subsection (b) that would state this requirement, the commission opts to insert this provision as subsection (b)(6) of the adopted rule. The commission finds that inclusion of this provision as part of the list of evidence that must be provided by a utility or

municipality further clarifies that a sufficient application must include evidence necessary to associate rate-case expenses with each litigated issue from the underlying rate case. The commission finds that including all of the evidentiary requirements for a complete application in a single list aids in the efficiency of administration of the rule. Accordingly, the commission adopts a new subsection (b)(6), which states that the evidence presented with a request for rate-case expenses must show the specific issue or issues in the rate case and the amount of rate-case expenses reasonably associated with each issue.

The commission disagrees with parties, such as Houston, Oncor Cities, El Paso, LCRA, Water IOUs, and State Agencies, who stated that the requirement to comply with subsection (b)(6) is unduly burdensome or that adoption of this provision would increase litigation costs by imposing more burdensome requirements for tracking rate-case expenses. The commission disagrees that this requirement imposes an undue burden and emphasizes the flexibility that should be used when determining which issues in an underlying rate case merit having their associated rate-case expense amounts specified. For example, clearly some issues contain sub-issues that are not significant enough to warrant requiring a party to further subdivide its rate-case expense request. The commission expects that the presiding officer will require a reasonable but not burdensome level of detail when conducting a proceeding. The commission also emphasizes the broad discretion granted to the presiding officer when conducting a proceeding in which recovery of or reimbursement for rate-case expenses may be awarded. The commission notes that the rule should be interpreted to provide the presiding officer all necessary flexibility when determining whether a failure to provide sufficient evidence pursuant to subsection (b)(6)

of the adopted rule should result in a finding that the application is not sufficient for further processing. In addition, the presiding officer is authorized to recommend a disallowance calculated pursuant to subsection (d)(3) of the adopted rule. The commission also notes that other courts in Texas have imposed a similar obligation on litigants. For example in *Tony Gullo Motors I, L.P. v. Chapa*, 212 S.W.3d 299 (Tex. 2006), because litigation costs may be recoverable for one issue but not another issue within the same proceeding, the Supreme Court of Texas stated that "claimants have always been required to segregate fees between claims for which they are recoverable and claims for which they are not." *Id.* at 311. Accordingly, the commission finds that adoption of subsection (b)(6) will provide for better efficiency in the processing of rate-case expense proceedings while allowing the presiding officer the flexibility necessary to avoid unduly burdening any party.

Joint Utilities also requested that, if the commission chooses to require that documents and other evidence be organized and detailed to enable a determination of the amount of expenses incurred for each major issue litigated in the rate case, that the commission limit this provision by inserting the phrase "to the extent practical." The commission declines to adopt this change, as the commission wishes to avoid unnecessary litigation regarding a party's claimed excuses for failing to comply with subsection (b)(6) as adopted. As discussed above, the commission rejects the argument that the adoption of subsection (b)(6) imposes an undue burden on any party or that Joint Utilities' change is necessary to avoid such a burden. The commission notes that the presiding officer is granted the discretion and flexibility to provide for the efficient processing of each rate-case expense proceeding.

Other proposed changes to this paragraph

The commission agrees with Mr. Baron's clarifying changes to the first sentence of subsection (b), which entails deleting "In any rate proceeding" and "pursuant to PURA §33.023 or 36.061(b)." The commission finds that these changes more clearly state the requirements of subsection (b).

Additionally, the commission disagrees with OPUC and declines to delete or limit the provision in the published rule permitting the verification of rate-case expenses by affidavit. Parties have supported rate-case expense amounts through affidavit on a number of occasions in contested proceedings before the commission. The commission finds that this process has contributed to the efficient handling of rate-case expense proceedings, particularly in situations where the requested amounts are small or not in dispute. Accordingly, the commission retains this option in the rule. However, the inclusion of an affidavit option in the new rule should not be interpreted to prevent a party from requesting discovery regarding an affiant's statement or to prevent a party from objecting to the admissibility of an affidavit when the affiant is not made available for examination as provided by the Texas Rules of Evidence.

Additionally, the commission adopts further changes to subsection (b) which are discussed in further detail below.

With respect to subsection (b), the Joint Utilities recommended deleting Mr. Baron's proposed subsection (b)(5)(A), which lists "the size of the utility and number and type of customers," based on the contention that a utility's size or customer count has no bearing on the reasonableness or necessity of the expenses incurred. The commission notes that the utility's size and number of customers can be relevant in determining whether the magnitude of rate-case expenses is reasonable. The commission finds that the size of a utility is frequently correlated with the amount of rate-case expenses it incurs. As discussed in more detail regarding subsection (c)(5) as adopted, the commission finds that the presiding officer should consider in each case whether a party's rate-case expenses as a whole are disproportionate, excessive, or unwarranted in relation to the size of the utility, among other factors.

Section (b)
(1) time and labor required;

As discussed above, Mr. Baron's comments proposed incorporation into his proposed subsection (b)(2) of language similar to subsection (b)(1) as published. Specifically, Mr. Baron's proposal would require the submission of evidence regarding the time and labor required and expended by the attorney or other professional.

Commission r esponse

For the reasons discussed above, the commission has adopted Mr. Baron's proposal to incorporate into subsection (b)(2) this modified version of subsection (b)(1) as published. The commission finds that this organizational change improves the clarity of the requirements of the adopted rule.

Section (b)
(2) nature and complexities of the case;

As discussed above, Mr. Baron's comments proposed incorporating similar language to subsection (b)(2) as proposed into subsection (b)(5)(C) of the adopted rule. Mr. Baron's proposed subsection (b)(5)(C) would require the submission of evidence regarding the novelty or complexity of the issues addressed.

Commission response

For the reasons discussed above, the commission has adopted Mr. Baron's proposal to incorporate into subsection (b)(5)(C) this modified version of subsection (b)(2) as published. The commission finds that this organizational change improves the clarity of the requirements of the adopted rule.

Section (b)
(3) amount of money or value of property or interest at stake;

As discussed above, Mr. Baron's comments proposed incorporating this language as subsection (b)(5)(B) of the adopted rule.

Commission response

For the reasons discussed above, the commission has adopted Mr. Baron's proposal to incorporate into subsection (b)(5)(B) the language found in subsection (b)(3) of the published rule. The commission finds that this organizational change improves the clarity of the requirements of the adopted rule.

Section (b)
(4) extent of responsibilities the attorney or professional assumes; and

OPUC commented that the phrase "extent of responsibilities the attorney or professional assumes" is ambiguous and not sufficiently tied to the rate-case expenses for which recovery is sought. OPUC suggested that if the intent is to take into consideration the nature, extent, and difficulty of the work done by the attorney or professional, the rule should clearly state so and that similar language can be found in the Railroad Commission's rule on rate-case expenses.

As discussed above, Mr. Baron proposed incorporating the following language as subsection (b)(1): "the extent of responsibilities assumed by the attorney or other professional in the rate case." Mr. Barron indicated that adoption of his proposal would replace subsection (b)(4) as published.

Commission response

The commission agrees that the change proposed by OPUC clarifies the commission's intent to focus on the nature, extent, and difficulty of the work done by the attorney or professional in evaluating the overall reasonableness of rate-case expenses in a particular proceeding. Accordingly, the commission adopts as subsection (b)(1) a modified version of the language proposed by Mr. Baron, which is reworded to state "the nature, extent, and difficulty of the work done by the attorney or other professional in the rate case." This change more accurately states the range of topics upon which parties seeking recovery of or reimbursement for rate-case expenses should submit evidence. This language is substantially similar to the language found in the Railroad Commission rule referenced by

OPUC, 16 Texas Administrative Code §7.5530(a)(3) and better reflects the potential nexus between the complexity or number of issues in a proceeding and the reasonableness of a particular amount of rate-case expenses.

Section (b)
(5) benefits to the client from the services.

City of Houston proposed striking subsection (b)(5) from the rule as published arguing that it is unclear or not necessary. Houston argued that as applied to a utility, it is presumed that the "client" is the utility's shareholder and that since the utility has a fiduciary responsibility to its shareholders, it is expected that the utility would not file testimony that breaches that responsibility. Houston commented that as the proposed rule might apply to a municipality, it must be noted that a municipality's "client" is the public interest and that it is expected that a municipality would not file testimony that would breach the public interest. Houston noted that under any situation, the trier of facts would already be expected to recognize and address any unusual circumstances.

OPUC commented that the commission should omit this subsection of the rule because it is irrelevant to the statutory standards required for recovery of rate-case expenses, including the public interest and the reasonable and necessary standards. OPUC agreed that if something did not benefit the client, it should not be recovered, but OPUC disagreed that the reverse is true. OPUC pointed out that the commission, in proposing to expressly state that certain expenses should be borne by shareholders, has acknowledged that not all expenses are appropriate for recovery from ratepayers and that the question as to whether it benefitted the client, *i.e.*, the

utility, does not answer the question regarding how inclusion of the expense is reasonable and necessary or in the public interest. OPUC suggested that if the commission wishes to consider a factor regarding the benefits inured due to the service provided, the beneficiary in question should not be the client, it should instead be the rate case proceeding or the commission's ability to consider all relevant facts when making its decision. OPUC commented that the Railroad Commission includes a similar consideration in subsection (b) of its rule, stating that a factor to be considered is "whether the work was relevant and reasonably necessary to the proceeding."

TIEC recommended that subsection (b)(5) either be removed or modified to include a cost-effectiveness standard and to consider the likelihood of success on a given issue, rather than simply referencing "benefits to the client" irrespective of the costs incurred or the likelihood of success on a particular issue. TIEC argued that whether an expenditure provides "benefits to the client" is a very broad standard that almost all rate-case expenses would meet and that not all costs of professional services that provide "benefits to the client" are necessarily reasonable costs. TIEC commented that the costs expended in pursuit of such "benefits" may far exceed the potential savings to be obtained, or may not be justified based on the probability of winning the issue. TIEC noted that, for example, it may "benefit" a utility to engage in long-shot discovery objections or judicial appeals of well-settled commission precedent, but those are not necessarily reasonable rate-case expenses. TIEC urged that subsection (b)(5) is overly broad and should either be deleted from the proposed rule or substantially revised to incorporate a "cost-effectiveness" standard and to account for the likelihood of success. TIEC suggested that, at a minimum, this section be revised to require proof of "benefits to the client from the services sufficient to justify the costs expended considering the likelihood of success."

Joint Utilities replied that one of the rate-case expense review criteria listed by the Third Court of Appeals in *City of El Paso v. Public Utility Comm'n of Texas*, 916 S.W.2d 515 (Tex. App.—Austin 1995, writ dism'd by agr.) was "benefits to the client from the services" and that this criterion should be retained, as a basic evaluation of whether the work performed needed to be performed for that particular client. Joint Utilities provided as an example the instance where an attorney bills the client for reading a beginner's book on utility ratemaking because the attorney is not familiar with the ratemaking process, that that may or may not have been beneficial to the client and that if the "benefits to the client from the services" criterion is deleted, it is not clear what criterion would be used to address these types of billings.

Commission response

Houston, OPUC, and TIEC urged deletion of subsection (b)(5) as published, stating that the wording of this subsection is overly broad and not necessary or relevant. In particular, the commission agrees with TIEC, which stated that the concept of benefit to the client is a broad standard that almost all rate-case expenses could be argued to satisfy. Accordingly, the commission finds that it does not need to require examination of this criterion in all cases, but instead parties should raise this issue on a case-by-case basis as appropriate.

Joint Utilities commented that the commission should retain this criterion in order to direct the presiding officer to consider whether the work performed needed to be performed for that particular client. However, the commission notes that subsection (b) merely lists the minimum amount of evidence that must be filed for a request to be sufficient for the

purpose of substantive review. Although the commission has decided that this criterion should not be required in all cases, a utility or municipality is permitted to provide any additional evidence supporting the reasonableness of its rate-case expenses, and other parties are likewise permitted to challenge any evidence or argue that such expenses are unreasonable given the circumstances of a particular request. The commission finds that it is most efficient to decline to require consideration of this issue in each proceeding, but instead permit parties to raise this issue as needed on a case-by-case basis.

Other comments related to subsection (b):

State Agencies agreed with the proposed rule that utilities and municipalities have the burden of proof and suggested three additional requirements that should be provided at inception in order to avoid additional time and expense in discovery: a justification for the need and cost of outside consultants who have not given testimony in the rate case, copies of any contracts or agreements that include charges for services that underlie rate-case expenses, and an explanation for the presence of attorneys at a hearing at a time when they did not actively participate. State agencies explained that the first two items are typically requested by Staff and intervenors. OPUC supported State Agencies' suggestions.

LCRA replied that normally, non-testifying consulting experts and their work product are not discoverable and that a party's attorneys may acquire the services of non-testifying consulting experts to help prepare for hearing, to assist with cross examination, to assist with briefing, or all of the above. LCRA argued that State Agencies' proposed rule requiring justification of non-testifying consulting experts would require the production of privileged information and is

impermissible. LCRA also replied that requiring an explanation for the presence of attorneys at a hearing who did not "actively participate" in the hearing is inappropriate because conceivably, in any given situation, one attorney may be charged with drafting the brief and would benefit from observing the hearing or an aspect of the hearing, another attorney may be preparing to cross examine a different witness on the same topic and would have a need to observe the answers of a witness on the stand, and yet another attorney may be in charge of the overall presentation of the case. LCRA pointed out that all of those lawyers are involved in the litigation though they may not be "actively participating" in the hearing to the satisfaction of State Agencies, and it should not be State Agencies' concern to know why there are multiple attorneys present at any one time. LCRA argued that requiring an explanation for the number of attorneys who attend a hearing at any given time is a matter of trial strategy, and should generally be regarded as privileged.

Joint Utilities opposed State Agencies' proposal to include language in the rule that requires utilities and municipalities to specifically justify costs related to non-testifying consultants and non-participating attorneys who attend hearings because it suggests the imposition of a higher standard on these rate-case participants. Joint Utilities pointed out that it is not only reasonable and necessary but common for utilities and municipalities to employ non-testifying consultants during rate-case proceedings and that it is also reasonable, necessary, and common for attorneys to attend a hearing without actually putting on a witness. Joint Utilities commented that this is made necessary by not only the number of contested issues and the depth and complexity of the subject matter, but also by the uncertainty as to how issues will be addressed at the hearing and to what extent other issues will arise that must be addressed by other witnesses. Joint Utilities

also noted that the witness schedule at the hearing can be unpredictable and that the next witness on the schedule (and his or her attorney) may wait in the hearing room for hours before that witness is called to testify. Joint Utilities pointed out that oftentimes a witness incurs the expense to travel to the hearing and waits at the hearing to testify, but is then passed at the last moment without any cross-examination at all. Joint Utilities commented that utilities and municipalities already have a burden under subsection (b) to present evidence of the reasonableness of their rate-case expenses, and the commission can determine the reasonableness of those costs pursuant to the factors listed in proposed subsection (c). Joint Utilities noted that information about non-testifying consultants is typically not discoverable, and to the extent State Agencies is challenging the long-standing consulting expert privilege, that would not only be unprecedented but would lead to more discovery and more expense.

LCRA commented that the categories listed on the proposed rule appear to be reasonable items for inspection, but that the commission should provide for appropriate redaction of attorney and consultant invoices particularly during the pendency of the proceeding given that invoices might be specific enough that a review of un-redacted invoices could reveal case strategy or violate client confidentiality.

Mr. Baron proposed insertion of a new subsection, "Purpose," which would establish the burden of proof, filing requirements, criteria, and procedures for determining the reasonableness of rate-case expenses. Mr. Baron noted that numerous substantive rules include a short statement of purpose and that inclusion of this new subsection would conform to that practice.

Water IOUs urged the commission to adopt the test laid out by TDRPC §1.04(b) in conjunction with the precedent from the *Andersen* case to determine the reasonableness and necessity of rate-case expenses as that standard was adopted by the Texas Supreme Court and has been time tested in numerous types of cases and contexts. Water IOUs commented that the least problematic part of the proposed rule is subsection (b) as this portion of the rule captures some of the *Andersen* criteria, but should be modified to adopt all of the *Andersen* considerations in line with Texas law. Water IOUs noted that *Andersen* is a simple standard so there is no need to adopt a more complicated set of rules like the ones proposed. Water IOUs noted that rate-case expense recovery should be simplified - not complicated - and that any time a complicated set of rules is adopted, that alone will increase the cost to litigate rate-case expenses.

OPUC replied that while some of the *Andersen* factors may be instructive in determining the extent of reasonable fees, they are too narrow to apply generally to utility rate proceedings and some of the factors are simply not relevant to determine whether rate payers should be responsible for paying the utility's rate-case expenses. OPUC noted that some factors may be relevant to the client, *i.e.*, the utility, but do not go to whether the expenses are reasonable and in the public interest and appropriate for recovery. OPUC urged the commission to reject the proposal of the Water IOUs.

Commission response

The commission finds that the utility or municipality has the burden of proof to establish that its rate-case expenses are reasonable and necessary. The commission has broad discretion to consider the totality of the circumstances and evidence submitted. The

commission expects that the utility or municipality will provide sufficiently detailed evidence that meets its burden of proof and that will allow the commission to make a determination of reasonableness and necessity.

The commission declines to adopt State Agencies' proposal to include in subsection (b) the requirement that utilities submit evidence specifically relating to a justification for the need and cost of outside consultants who have not given testimony in the rate case, copies of any contracts or agreements that include charges for services that underlie rate-case expenses, and an explanation for the presence of attorneys at a hearing at a time when they did not actively participate. The commission agrees with Joint Utilities that consulting experts are commonly used by parties. Additionally, due to the unpredictable nature of live hearings, as well as the interconnected nature of many issues, it is common for attorneys to be present at a hearing even when they are not actively participating. The commission does not believe that evidence relating to these three issues necessarily must be provided in order for the presiding officer to conduct a full review of a party's rate-case expenses. However, no provision of this rule shall be construed to prevent a party from conducting discovery regarding these issues or from challenging the reasonableness of certain rate-case expenses using evidence relating to these issues based on the specific factual circumstances in a particular proceeding.

The commission further declines to adopt LCRA's proposal that the proposed rule be amended to explicitly authorize the redaction of attorney and consultant invoices. The commission notes that any party may request the entry of a protective order and that, to

the extent that the invoices in question contain confidential information, parties may assert that documents are subject to a claim of confidentiality pursuant to the commission's rules. Accordingly, the commission finds that it would be redundant to provide for treatment of confidential documents in subsection (b) of the proposed rule.

The commission declines to adopt the *Andersen* criteria proposed by Water IOUs in lieu of the proposed criteria in the commission's published rule. The commission agrees with OPUC that the *Andersen* factors, while perhaps informing the commission's analysis of the reasonableness of rate-case expenses in certain circumstances, are too narrow to apply to rate-case expense proceedings generally. The commission has determined that the factors listed in the rule as adopted are appropriate given the nature of commission proceedings addressing the recovery of rate-case expenses.

Furthermore, the commission declines to adopt the "Purpose" subsection proposed by Mr. Baron. The commission finds that adoption of this new subsection is unnecessary because it does not aid in the understanding or interpretation of the rule. While Mr. Baron notes that numerous substantive rules include a purpose subsection, the commission notes that numerous substantive rules do not include such a subsection. Accordingly, the commission finds that it is not necessary or mandatory in this case to include such a subsection.

Section (c) **Criteria for review.**
In determining the reasonableness of the rate-case expenses, the presiding officer shall consider all relevant factors, including but not limited to those set out previously, and shall also consider:

State Agencies suggested that the introductory paragraph should be clarified by replacing the phrase "including but not limited to those set out previously" with "including but not limited to those set out in subsection (b)."

Mr. Baron proposed several changes to subsection (c). Mr. Baron proposed a change to the first sentence of subsection (c) to clarify that the list of factors for the presiding officer's consideration are listed in subsection (b) of the rule and any factor shown to be relevant to the specific case. Mr. Barron stated that this change to the first sentence in subsection (c) is intended to make it clear that the factors the presiding officer is required to consider are found in subsection (b) without precluding the possibility that the parties will raise other relevant issues in the proceeding. Mr. Baron also proposed a new second sentence to be inserted, which would state: "The presiding officer shall disallow or recommend disallowance of recovery of rate-case expenses as unreasonable if and to the extent the evidence shows that . . . ." Mr. Baron stated that these changes would state that the list found in subsection (c) are the bases upon which the presiding officer may recommend or impose disallowances.

Mr. Baron also commented that, for completeness, it should be made clear that all types of rate-case expenses, including expenses for travel and not just expenses for attorney and other professional services, are subject to disallowance if and to the extent found unreasonable. Mr. Baron proposed inserting a new item in the list of factors that would state that expenses incurred for lodging, meals and beverages, transportation, or other services or materials that are extreme or excessive may be disallowed. Mr. Baron proposed inserting this requirement as a new subsection (c)(2) while renumbering the succeeding list items accordingly.

Water IOUs urged the commission not to adopt subsection (c) and argued that it should instead apply the tests in *Andersen*/TDRPC. Water IOUs commented that subsection (c) is objectionable and unnecessary if the *Andersen*/TDRPC criteria are used to determine recoverable rate-case expenses based on reasonableness and necessity. Water IOUs noted that several parts of proposed subsection (c) are already covered by *Andersen*/TDRPC factors or, in some instances, proposed subsection (b) and proceeded to list several examples where they perceived overlap between them. Water IOUs commented that allowing consideration of "all relevant factors" eviscerates the establishment of any prescribed set of criteria and will lead to arbitrarily reduced recovery of reasonable and necessary rate-case expenses.

Commission response

The commission agrees with State Agencies and Mr. Baron, who both stated that subsection (c) as published should be clarified to better state the commission's intent. Both commenters stated that the commission should explicitly refer to subsection (b) instead of instructing the presiding officer to consider factors that were set out previously. The commission modifies the first sentence of subsection (c) to be consistent with Mr. Baron's proposed language, which would read "In determining the reasonableness of the rate-case expenses, the presiding officer shall consider the relevant factors listed in subsection (b) of this section and any other factor shown to be relevant to the specific case." The commission concludes that this change more specifically states what criteria will be considered by the presiding officer while also stating that no party is precluded from asserting that some other factor is relevant to a particular proceeding.

The commission declines to adopt the second sentence as proposed by Mr. Baron, which states: "The presiding officer shall disallow or recommend disallowance of recovery of rate-case expenses as unreasonable if and to the extent the evidence shows that" before the list of criteria provided in subsection (c). Mr. Baron's proposed language implies that the factors found in subsection (c) are the only grounds for the disallowance of a party's rate-case expenses. The commission intends to conduct a comprehensive review with reasonableness as the standard for allowances and disallowances and adopts subsection (c) as a list of factors that guide that inquiry. As subsection (d)(1) as adopted states, whether the rate-case expenses were actually and reasonably incurred is the ultimate question. Accordingly, the commission adopts a less restrictive version of the second sentence of subsection (c), which now reads as follows: "The presiding officer shall decide whether and the extent to which the evidence shows that" before the list of criteria provided in subsection (c). The commission finds that this change better communicates to the parties that subsection (c) lists criteria that guide the presiding officer's inquiry and that, while some disallowances may be said to be recommended pursuant to a particular paragraph in subsection (c), the ultimate inquiry in a rate-case expense proceeding is whether the rate-case expenses are reasonably incurred.

Mr. Baron proposed changes to subsection (c) of the proposed rule in an attempt to clarify that all types of rate-case expenses, including expenses for travel and not just expenses for attorney and other professional services, are subject to disallowance if and to the extent that they are found unreasonable. Mr. Baron proposed inserting a new item in the list of

factors that would instruct the presiding officer to consider whether expenses incurred for lodging, meals and beverages, transportation, or other services or materials that are extreme or excessive. The commission has incorporated Mr. Baron's recommendations in subsection (c) of the rule. Specifically, the commission adopts a new subsection (c)(2) and renumbers the succeeding paragraphs accordingly. These changes provide an increased degree of specificity with respect to the information necessary for a determination of reasonableness while retaining the presiding officer's flexibility to consider all relevant factors and while putting parties on notice regarding certain factors that will be considered in the evaluation of all requests for recovery of or reimbursement for rate-case expenses.

The commission rejects Water IOUs' proposal to delete subsection (c) and adopt the *Andersen* criteria instead. As stated above, the commission has determined that the *Andersen* criteria are too narrow to apply to rate-case expense proceedings generally. Accordingly, the commission retains subsection (c), which is appropriate given the nature and complexity of issues decided before the commission. The commission emphasizes that the presiding officer shall consider all relevant factors when determining the reasonableness of rate-case expenses.

Section (c)

(1) whether the rates paid to, tasks performed by, and time spent on each task by an entity were extreme or excessive;

OPUC commented that in order to prevent confusion of the term "rates," as it is intended to be used in this section, with the "rates" charged by the utility, this provision should be clarified by

changing "rates" to "fees," "billing rates," or another similar term if the intent is to look at whether what the expert or attorney charged was extreme or excessive.

Houston commented that the proposed reference to "each" task is unclear and potentially unfeasible, noting that if the term "each" is taken literally, it would place an impractical and costly requirement on all parties without generating a compensating benefit to ratepayers. Houston argued that trying to keep track of "each" task, rather than the general task performed imposes an impractical constraint on all involved. Houston noted that if the witness were required to keep track of "each" such task, not only would it be extremely disruptive to the process, it would greatly increase the cost incurred to perform an analysis and diminish the investigation of that and other issues in the case. Houston recommended changing the word "each" to "a" in this subsection.

Mr. Baron provided several changes to add clarity when interpreting subsection (c)(1). Specifically, Mr. Baron proposed inserting "attorney or other professional or" before the word "entity," replacing the word "and" with "or," and deleing the phrase "on each task."

Commission response

OPUC, Mr. Baron, and Houston each proposed clarifying changes to subsection (c)(1) as published. The commission agrees that OPUC's proposal to change the word "rates" in subsection (c)(1) to "fees" would prevent confusion and better clarify the effect of the rule. Accordingly, OPUC's proposed change is adopted.

The commission also agrees with Houston's proposal to change "each task" to "a task" in the proposed rule. The commission finds that this change clarifies that the presiding officer is not expected to review evidence regarding each and every task performed by any entity, but does direct the presiding officer to consider whether unreasonable or excessive rate-case expenses are associated with any task..

The commission further agrees with Mr. Baron regarding his proposals to change "and" to "or" and modify subsection (c)(1) to make reference to attorneys as well as other professionals. The commission finds that these clarifying changes aid in the understanding of the new rule. However, the commission disagrees with Mr. Baron's suggested deletion of "on each task." The commission finds that this change would decrease the level of review required by subsection (c)(1) by expanding the focus from whether the fees or time spent on any single task is excessive to whether the fees or time spent by the professional overall is excessive. As discussed above, the commission has changed "each task" to "a task" in order to address Houston's concerns. Accordingly, the commission finds that it is appropriate to retain this phrase as modified.

After incorporating the changes described above, subsection (c)(1) now reads as follows: "the fees paid to, tasks performed by, or time spent on a task by an attorney or other professional were extreme or excessive."

Section (c)
(2) whether there was duplication of services or testimony;

Water IOUs stated that the language in proposed (c)(2), "whether there was duplication of services or testimony," invites substitution of subjective opinions in lieu of sound professional judgments, but is arguably also subsumed by the "time and labor required" component of proposed subsection (b) and the *Andersen*/TDRPC factors.

Commission response

The commission rejects Water IOUs' suggestion to delete subsection (c)(2) as published. Water IOUs stated that the proposed subsection invites substitution of subjective opinions in lieu of sound professional judgments and is redundant if the commission adopts the *Andersen* criteria or the "time and labor required" component of subsection (b). For the reasons stated above, the commission declines to adopt the *Andersen* criteria. Accordingly, this subsection is not made redundant by the *Andersen* criteria.

Additionally, whether there was duplication of services or testimony is one of many criteria that the commission has considered in the evaluation of rate-case expenses in the past. The commission determines that unreasonable duplication of services or testimony is a valid consideration when considering the reasonableness and necessity of such expenses. The commission further finds that it is entirely appropriate for the presiding officer to determine whether particular expenses are "unreasonable" because they were unnecessarily duplicative. Parties remain free to present any evidence they deem necessary to establish the reasonableness of any testimony or service, including detailed evidence of how such testimony or services reflect the exercise of a particular parties' sound

professional judgment. Accordingly, the commission retains the instruction that the presiding officer shall consider this factor.

Consistent with the reorganization of subsection (c), this paragraph has been renumbered as subsection (c)(3), and the word "whether" is removed.

Section (c)
(3) the novelty of the issues addressed, including, but not limited to,
(A) whether a legal or factual contention advanced in a rate proceeding is warranted by existing law or policy or by a nonfrivolous argument for the extension, modification, or reversal of existing law or policy or the establishment of a new law or policy; or

Mr. Baron urged that the standard for disallowing expenses related to litigating a specific issue should be sharpened by stating a single basis for disallowance that combines parts (A) and (B) in proposed rule subsection (c)(3). Mr. Baron commented that the commission must balance two competing interests. He argued that the rule should discourage utilities and municipalities from raising issues that are plainly without merit on the hope that litigating might nonetheless yield some financial or strategic benefit. Mr. Baron stated that the rule must also not cast a chill on good-faith arguments, having a legitimate basis in law or policy, that seek to change established precedent based on the specific facts of a case or reconsideration of prior policies. Mr. Baron argued that his proposed language strikes this balance by stating a single basis for disallowance that borrows in part from the definition of "groundless" in Chapter 9 of the Texas Civil Practice and Remedies Code which governs frivolous pleadings and claims, and Rule 13 of the Texas Rules of Civil Procedure, which governs the filing of court pleadings by attorneys and parties. Mr. Baron stated that subsection (c)(3) as published is not preferable because it would invite dispute regarding which commission precedents are clearly established and it fails to adequately

strike the necessary balance between discouraging meritless arguments and between not chilling meritorious arguments.

State Agencies commented that the reference to "existing law" in subsection (c)(3)(A) is troublesome because the commission cannot reverse or modify a statute or court decision and to the extent a statute or court decision constitutes "existing law" any position that urged them to do so is frivolous *per se*. State Agencies contended that adoption of the rule as proposed would result in additional costly disputes to determine what constitutes a "non-frivolous argument" and that the absence or presence of frivolity is not relevant to determining whether an entity should be allowed to recover costs associated with re-litigating issues that have already been decided by the commission. State Agencies commented that the proposed language would create more problems that it would solve because it will create additional litigation over what it means.

Joint Utilities proposed that to avoid the possibility that some may interpret subsection (c)(3) as conflating two discrete criteria for reasonableness, the rule should be separated into two subsections that separately address the litigation of "novel" issues and the engagement in "frivolous" litigation tactics. Joint Utilities argued that there is an important distinction between novel issues and frivolous arguments and that when an issue is truly "novel" in that it presents as an issue of first impression or addresses new facets of an existing issue, parties should be encouraged to bring those issues before the commission in order to obtain a decision on them. Joint Utilities commented that parties should not be penalized if they choose to raise novel issues so long as they have a reasonable basis in law and fact. Joint Utilities urged the commission to modify subsection (c)(3) to just address novel issues and add a new (c)(4) to separately address

frivolous arguments. Joint Utilities' proposed replacing subsection (c)(3) with "the novelty of the issues address;" and inserting a new subsection (c)(4) stating whether the claim, defense or other legal contention is warranted by existing law or policy or by a nonfrivolous argument for the extension, modification, or reversal of existing law or policy or the establishment of a new law or policy." Joint Utilities stated that their proposal incorporated language taken from section 10.001 of the Civil Practice & Remedies Code concerning frivolous arguments since the courts have already interpreted this language and that would reduce litigation over its meaning. TIEC replied that it does not oppose this proposed change.

El Paso replied that the provision may not be required as the parties are already under a similar duty imposed by SOAH Procedural Rule §155.303 which states "The signatures of parties or authorized representatives constitute certification that they have read the pleading and that, to the best of their knowledge, information, and belief formed after reasonable inquiry, the pleading is neither groundless nor brought in bad faith." El Paso argued that given the certification implied in the pleadings, the commission currently has the ability to find expenses incurred in connection with a position brought in bad faith unreasonable.

Water IOUs concurred with Joint Utilities that care should be taken not to conflate novel arguments with frivolous ones and noted that novel legal arguments are expressly contemplated under the *Andersen* standard.

Commission response

The commission agrees with Mr. Baron that the commission's review of the reasonableness of expenses related to the litigation of specific issues should strike a balance by discouraging parties from litigating issues without merit while not discouraging litigation of arguments made in good faith. The commission finds that the language proposed by Mr. Baron appropriately distinguishes between meritorious and unreasonable claims. Accordingly, the commission deletes subsection (c)(3) as published and adopts Mr. Baron's proposed replacement, which states "the utility's or municipality's proposal on an issue in the rate case had no reasonable basis in law, policy, or fact and was not warranted by any reasonable argument for the extension, modification, or reversal of commission precedent." The commission agrees with Mr. Baron that this paragraph as adopted sharpens the standard for reviewing expenses related to litigating a specific issue. The new language is simpler while enhancing the focus of the commission's review on the essential reasonableness of the party's positions. The rule discourages utilities and municipalities from raising issues that are plainly without merit on the hope that litigating might nonetheless yield some financial or strategic benefit. The commission equally expects that the adopted rule will not cast a chill on good-faith arguments that have a legitimate basis in law or policy or that seek to change established precedent based on the specific facts of a case or reconsideration of prior policies.

State Agencies stated that the reference to "non-frivolous" in subsection (c)(3)(A) as proposed is troublesome because it could result in additional costly disputes to determine what constitutes a "non-frivolous argument." The commission notes that this paragraph,

as proposed by Mr. Baron and as adopted by the commission, makes no reference to the word "non-frivolous," and, therefore, addresses State Agencies' concerns. However, the commission does not intend for the new rule to be interpreted in a way that will permit the recovery of rate-case expenses that are associated with the presentation of frivolous arguments. Parties remain free to raise this issue in each proceeding on a case-by-case basis.

Joint Utilities recommend splitting subsection (c)(3) into two paragraphs in order to avoid the possibility that some may interpret subsection (c)(3) as conflating two discrete criteria for evaluating the reasonableness of rate-case expenses: novelty and frivolity. The proposed subsection (c)(3)(A) states clearly that the presiding officer shall consider whether arguments that seek extension, modification, or reversal of existing law or policy are frivolous when evaluating the novelty of the issues addressed in a proceeding and ultimately, the reasonableness of a particular request for rate-case expenses. The commission declines to adopt Joint Utilities' proposed language. The commission finds that the language proposed by Mr. Baron more explicitly expresses the commission's intent in adopting subsection (c). As discussed above, the commission has deleted the reference in the rule to the word "non-frivolous," which is present in the Joint Utilities' proposed language. The commission finds that the language proposed by Mr. Baron better puts parties on notice regarding the review that will be conducted by the presiding officer, and, accordingly, that language is adopted instead of the Joint Utilities' proposal.