

**AUSTIN ENERGY 2016 RATE REVIEW**

**AUSTIN ENERGY'S TARIFF PACKAGE §  
UPDATE OF THE 2009 COST OF §  
SERVICE STUDY AND PROPOSAL TO §  
CHANGE BASE ELECTRIC RATES §**

**BEFORE THE CITY OF AUSTIN  
IMPARTIAL HEARING EXAMINER**

**AUSTIN CITY CLERK  
RECEIVED  
2016 MAY 27 PM 1 33**

**CORRECTED DIRECT TESTIMONY AND EXHIBITS OF**

**MARILYN J. FOX**

**ON BEHALF OF**

**NXP SEMICONDUCTOR, INC.**

**AND**

**SAMSUNG AUSTIN SEMICONDUCTOR, INC.**

**MAY 27, 2016**

**CORRECTED DIRECT TESTIMONY OF  
MARILYN J. FOX**

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**I. INTRODUCTION**

**Q. PLEASE STATE YOUR NAME, OCCUPATION AND ADDRESS.**

A. My name is Marilyn J. Fox. I am the President of Fox, Smolen & Associates, Inc. ("FSA")  
My business address is 1701 Nueces Street, Austin, Texas.

**Q. ON WHOSE BEHALF ARE YOU OFFERING TESTIMONY IN THIS PROCEEDING?**

A. On behalf of NXP Semiconductor, Inc. and Austin Samsung Semiconductors LLC  
("NXP/Samsung"). Gary Goble, of Management Applications Consulting, Inc. ("MAC"), is  
working with FSA in this proceeding.

**Q. WHAT TYPES OF ORGANIZATIONS ARE YOUR CLIENTS?**

A. Both organizations are manufacturers of electronic components with 24/7 continuous  
operations. Both are large customers of Austin Energy ("AE") with very high load profiles.

**Q. PLEASE DESCRIBE YOUR PROFESSIONAL EXPERIENCE AND EDUCATIONAL BACKGROUND.**

A. I am currently a principal and owner of FSA, a Texas corporation formed in 2001. FSA is a  
consulting firm and was a registered aggregator with the Public Utility Commission of  
Texas ("PUC") prior to 2014. FSA sold its customer base to NRG Energy in 2014, but the  
corporation survived the sale. In October 2015, the principals of FSA left NRG to resume  
the consulting practice.

Prior to forming FSA, I have worked in the area of rate regulation since the early  
1980's. I was the Assistant Director of the Accounting Division of the PUC and the

1 Director of Regulatory Affairs for the City of Houston from 1986 to 1989. The City of  
2 Houston exercised original jurisdiction over gas, electric, and water utilities operating in  
3 Houston. My responsibilities also covered both franchising cable and telecommunication  
4 providers. From 1990 through 1998, I worked as the Assistant Finance Director for the City  
5 of Austin, with my duties included regulation of investor-owned utilities serving Austin and  
6 the franchising of cable and telecommunication providers. While at the City of Austin I  
7 assisted the Director with budget and other financial duties, including assisting with the  
8 Utility Customer Service Office (now the office of Customer Care and Billing), the  
9 department responsible for billing all of Austin's utility and service bills. Exhibit MJF-1 is  
10 my complete resume.

11 **Q. HAVE YOU PREVIOUSLY TESTIFIED BEFORE THE PUBLIC UTILITY**  
12 **COMMISSION OF TEXAS (PUC)?**

13 A. Yes, Exhibit MJF-1 lists the most recent PUC dockets.

14 **Q. DID YOU PARTICIPATE IN THE LAST RATE REVIEW PROCESS AT THE**  
15 **CITY LEVEL?**

16 A. Yes, our firm represented a large commercial customer. During that process we participated  
17 in Austin Electric Utility Commission meetings and work sessions as well as public  
18 hearings before the Austin City Council.

19 **Q. WAS THIS TESTIMONY PREPARED BY YOU OR UNDER YOUR**  
20 **SUPERVISION?**

21 A. Yes.

**Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY IN THIS PROCEEDING?**

A. My testimony analyzes Austin Energy's ("AE") proposed revenue requirement and cost of service ("COS").

**Q. WHAT EXHIBITS ARE YOU SPONSORING?**

A. I am sponsoring the following Exhibits:

- Exhibit MJF-1 is my resume and list of relevant engagements and dockets; and,
- Exhibit MJF-2 is a summary of AE's requested revenue requirement compared to my proposed adjustments.
- Exhibit MJF-3 is a summary of dollar impact of the adjustments proposed by NXP/Samsung, including the changes recommended by Mr. Gary Goble.

**Q. WERE THESE EXHIBITS PREPARED BY YOU OR UNDER YOUR SUPERVISION?**

A. Yes

## **II. SUMMARY OF RECOMMENDATIONS**

**Q. PLEASE SUMMARIZE YOUR CONCLUSIONS AND RECOMMENDATIONS.**

A. Based on my analysis, I have determined AE's just and reasonable revenue requirement should be \$1,032,140,819 and AE's requested COS of \$1,217,227,311 is overstated by \$185,086,492.<sup>1</sup> AE's requested revenue requirement includes costs that are not necessary

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<sup>1</sup> This figure includes a \$70 million dollar reduction AE instituted as a reduction to the Power Supply Adjustment ("PSA"), which was approved after AE filed *Austin Energy's Tariff Package: 2015 Cost of Service Study and Proposal to Change Base Electric Rates* and therefore still included in their initial rate request.

1 and reasonable to provide electric service. Additionally, AE's Adjusted Test Year Revenue  
2 is understated due to adjustments made to Transmission revenue.

3 **Q. BRIEFLY OUTLINE YOUR RECOMMENDATIONS.**

4 A. Exhibits MJF-2 and MJF-3 illustrate my recommendations, which are outlined as follows:

- 5 (1) AE's requested Operations and Maintenance ("O&M") Expenses are overstated by  
6 \$113,465,039.
- 7 (2) AE's requested Margin (Return) is overstated by \$11,590,703.
- 8 (3) AE's current balance of reserves is in excess of required targeted reserves by  
9 \$37,435,998 and therefore, does not need any amount of increase through rates.

10 I am also recommending several changes to the process AE has used in rate reviews  
11 as well as changes to AE's financial policies.

12 **III. DETERMINING REVENUE REQUIREMENT – AUSTIN ENERGY'S PROPOSED USE OF THE**  
13 **CASH FLOW METHODOLOGY**

14 **Q. PLEASE DESCRIBE THE GENERAL STANDARDS YOU FOLLOWED IN YOUR**  
15 **ADJUSTMENTS TO AE'S REQUESTED REVENUE REQUIREMENT.**

16 A. There exists a set of generally accepted ratemaking principles followed in Texas and in  
17 many other parts of the United States. Rates are set using a test year concept that attempts  
18 to provide a proxy for the costs to be incurred and the revenue expected to be earned by the  
19 utility going forward. Under this principle, the test year costs are adjusted to eliminate any  
20 expenses that are not recurring in nature. Other adjustments are made to exclude abnormal  
21 costs as well as those costs that are neither reasonable nor necessary to provide electric  
22 service. Adjustments can also be included to reflect changes that are known and measurable

1 and will occur during the time the rates are in effect. For a cost to be included as a post-test  
2 year, known and measurable adjustment, *the event creating the cost must be certain* and the  
3 *amount must be quantifiable*. For example, a payroll increase that has been approved by a  
4 board of directors that will be implemented during the time the rates are in effect would  
5 constitute a known and measurable post test year adjustment; the amount of the increase and  
6 the number of employees eligible for the increase are both known. Therefore, the amount of  
7 increase in payroll cost can be calculated and is therefore measurable. Similarly, revenue is  
8 adjusted to remove any abnormal events like extreme weather, increases and decreases in  
9 customers, and any changes that will occur, such as interest, miscellaneous service charges,  
10 or wholesale revenue.

11 **Q. WHY ARE THESE ADJUSTMENTS MADE IN SETTING CUSTOMERS' RATES?**

12 A. The regulatory body attempts to insure that the rates charged to customers are just and  
13 reasonable in relation to the cost of providing utility service while providing the utility's  
14 owners the opportunity to realize a fair return on their investments made in providing that  
15 utility service.

16 **Q. WHAT IS INCLUDED IN A TYPICAL UTILITIES' REVENUE REQUIREMENT?**

17 A. Utility expenses are included in the revenue requirement, and usually include O&M of  
18 utility property, plant and equipment, customer service and general administrative costs.  
19 These are generally cash or accrued expenses. The revenue requirement also includes  
20 depreciation and amortization expenses, which are non-cash. There is also a provision for  
21 taxes such as payroll, property, and income. As with any business, revenue less expense  
22 results in net income. It is the net income before interest expense (return) that provides for a

1 utility's debt expense and compensation to shareholders for providing equity investments in  
2 the utility.

3 **Q. HOW DOES A REVENUE REQUIREMENT ANALYSIS FOR A MUNICIPALLY-**  
4 **OWNED UTILITY DIFFER FROM THAT OF AN INVESTOR OWNED**  
5 **REGULATED UTILITY?**

6 **A.** The major difference is in the determination of the utility's return because a municipally-  
7 owned electric utility's assets are generally financed using bonds and internally generated  
8 cash. An investor-owned electric utility's assets are financed with debt and stockholder  
9 investments (equity). Additionally, other differences exist because a municipally-owned  
10 utility will not have to pay federal income taxes or local property taxes within the city  
11 limits.

12 **Q. PLEASE IDENTIFY THE DIFFERENT COMMON METHODS OF**  
13 **DETERMINING RETURN AND EXPLAIN IF A SPECIFIC METHOD IS MORE**  
14 **REASONABLE TO USE WHEN DETERMINING RETURN FOR A**  
15 **MUNICIPALLY OWNED UTILITY VERSUS AN INVESTOR OWNED UTILITY?**

16 **A.** There are four common methods used to determine return (the amount of revenue  
17 requirement over and above the level of operating expenses that are reasonable and  
18 necessary): (1) Cash Flow Method; (2) the Rate of Return method; (3) the Debt Service  
19 Coverage method; and, (4) the Times Interest Earned Ratio (TIER) method. Each of these  
20 methods is provided for in the PUC's Commission approved rate filing package used by  
21 Transmission & Distribution Utilities within the state. While the choice of method to  
22 determine return by an investor owned utility and a municipally owned utility may be the



1 same, some methods are more applicable and preferable than others for determining a  
2 reasonable return due to characteristics unique to the type of ownership. For example, the  
3 Cash Flow method is not a reasonable method for determining return for a municipally  
4 owned utility.

5 **Q. HOW HAS AE DETERMINED ITS REQUESTED RETURN?**

6 **A.** AE has used the Cash Flow method to determine its return. The Cash Flow method  
7 considers all of a company's cash needs in excess of its O&M expense and debt service that  
8 is subject to recovery. The purpose of this approach is to provide for excess cash to fund  
9 established cash reserve requirements. For example, AE has proposed collecting through its  
10 revenue requirement an additional \$11,590,703 to fund its reserves over a three year period.  
11 AE is proposing this in order to fulfill the goals established by several decades' worth of  
12 Austin City Council Financial Policies.

13 **Q. HOW HAVE THE RESERVES ESTABLISHED IN THE FINANCIAL POLICIES**  
14 **BEEN FUNDED?**

15 **A.** From 1994 through 2012 the reserves were funded using excess net revenue, which is  
16 comprised of revenue less expense before any transfers. Practically speaking net revenue  
17 occurs when a utility recovered more revenue than expense. For AE this excess was placed  
18 into the reserves. Between 1994 and 2012 AE did not have a rate increase; it was only in  
19 relation to the 2012 rate case that AE sought to replenish their reserves through rates  
20 because they had been depleted during the previous years.

1 **Q. DO YOU THINK THE CASH FLOW METHOD IS PREFERABLE TO OTHER**  
2 **METHODS TO DETERMINE RETURN FOR A MUNICIPALLY-OWNED**  
3 **UTILITY?**

4 **A.** No. I agree with the concerns stated by the PUC's Director of the Rate Regulation Division,  
5 Darryl Tietjen, who stated during the appeal of AE's last rate case to the PUC,

6 [a]lthough the Cash Flow approach is listed in the Commission's rate filing  
7 package as one of a number of return-dollar methodologies on which a utility  
8 may rely in developing its request, I believe that its use—more than the use of  
9 the other methods specifically included in the rate filing package—can be  
10 fraught with questions about its underlying assumptions. The basic reason for  
11 this opinion is that the return determined using the Cash Flow method is  
12 ultimately a “plug –in” number; that is, the Cash Flow method allows a utility to  
13 assert the total amount of return necessary to pay for all its cash needs, and that  
14 resulting amount is—*ipso facto*—the amount that the utility claims as the return  
15 that it “requires” in its revenue requirement. The bottom- line result is that a  
16 utility's demonstration and justification of its desired return amount is a  
17 foregone conclusion because it is a mathematical inevitability.<sup>2</sup>

18 As Mr. Tietjen stated, this method is based on inherently circular logic;

19 [a] utility asserts that it has a given level of costs that must be paid, and it uses  
20 the Cash Flow method to demonstrate this alleged necessity. When the Cash  
21 Flow method then invariably produces the asserted revenue requirement  
22 (because, by its inherent nature, it always will), that result is declared by the  
23 utility to constitute the required evidence that its claimed needs are reasonable  
24 and “necessary.”<sup>3</sup>

25 Mr. Tietjen went even further to state:

26 [t]he use of a method to achieve such an effectively predetermined outcome  
27 could conceivably lead to inconsistency with PURA §11.002(b), which states, in  
28 part: “Public agencies regulate utility rates, operations and services as a  
29 substitute for competition.” Unlike the other three options for determining the  
30 return component of a utility's revenue requirement, the Cash Flow method, as  
31 applied by Austin Energy, has no obvious comparison point to the dynamics of

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<sup>2</sup> *Petition by Homeowners United for Rate Fairness to Review Austin Rate Ordinance No. 20120607-055*, Docket No. 40627, Direct Testimony of Darryl Tietjen at 8 (Feb. 14, 2013).

<sup>3</sup> *Id.* at 8-9.

1 competitive markets by which non-competitive performance would be  
2 apparent.<sup>4</sup>

3 Under the Cash Flow method utilized by AE, the General Fund Transfer, Internally  
4 Generated Funds for Construction and other transfers to reserves are taken as a given,  
5 regardless of their prudence or reasonableness. This methodology does not incentivize  
6 prudent financial practices or cost savings because rates will be set based on these transfers,  
7 which are presumed to be a given.

8 **Q. DO YOU CONTINUE TO AGREE WITH MR. TIETJEN'S ASSESSMENTS**  
9 **PROVIDED ABOVE?**

10 **A.** Yes, I believe the above assessments highlight the unreasonable nature of a municipally-  
11 owned utility using a Cash Flow method when determining revenue.

12 **Q. WHAT ALTERNATIVE METHOD SHOULD AE HAVE USED TO DETERMINE**  
13 **THEIR REVENUE?**

14 **A.** The Debt Service Coverage methodology would have been more appropriate as this  
15 methodology is more economically justifiable as a starting point to determine return  
16 requirements. The Debt Service Coverage methodology is similar to the Rate of Return  
17 method used by many Investor-Owned Utilities in that rates are set to allow the utility the  
18 "opportunity" to earn its rate of return, not a "guarantee." If reviewed periodically, in a  
19 consistent manner, the Debt Service Coverage methodology can serve as a check on the  
20 utility's spending by placing a transparent metric on amounts that are included in the return  
21 calculation. Under this methodology, the burden is on the managers of the utility to control

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<sup>4</sup> *Id.* at 9.

costs and insure that coverage is sufficient, resulting in benefits to ratepayers through prudent expenditures.

**Q. HAVE YOU CALCULATED YOUR RECOMMENDATIONS USING THE DEBT SERVICE COVERAGE METHOD?**

A. No. The Impartial Hearings Examiner determined that the issue of what methodology should be used to determine return was not within the scope of this proceeding, despite the fact that PUC Staff testimony in Docket 40627 went against the use of the Cash Flow Method and recommended the use of a method based on Debt Service Coverage.<sup>5</sup> However, it is my recommendation that the use of a Cash Flow method to determine return should be fully vetted by the Austin City Council based on the arguments above. The determination as to which method should be used should be determined by the Austin City Council in this rate proceeding. AE customers should not be bound by faulty logic which was squarely not supported by PUC Staff during the last rate case, but was inevitably adopted in order to achieve settlement in the aforementioned case. This is a new proceeding and therefore this issue should be addressed and the faulty logic that results in a return over and above what is required by AE should be fully considered and reevaluated based on the facts in this proceeding.

**IV. PIECEMEAL RATEMAKING AND PASS-THROUGH CHARGES**

**Q. WHAT OTHER CONCERNS DO YOU HAVE WITH AE'S CURRENT RATE MAKING PROCESS?**

A. I am concerned that AE is currently practicing "piecemeal ratemaking."

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<sup>5</sup> *Id.* at 14.

1 **Q. WHAT IS PIECEMEAL RATEMAKING?**

2 A. Piecemeal ratemaking allows certain individual utility costs to be considered outside a full  
3 review of all of the utility's costs. The PUC has pointed out problems with piecemeal  
4 ratemaking. In Docket 28840, *Application of AEP Texas Central Company for Authority to*  
5 *Change Rates*, the PUC found in connection with Piecemeal Ratemaking that "[a] utility  
6 cannot increase its rates unless it demonstrates that its **total revenues are insufficient to**  
7 **recover the totality of its reasonable costs**, plus a reasonable rate of return. **Singling out**  
8 **certain expenses in order to guarantee dollar-for dollar cost recovery is piecemeal**  
9 **ratemaking**" (emphasis added).<sup>6</sup>

10 **Q. WHAT IS AE'S JUSTIFICATION FOR EXCLUDING CERTAIN RATES OR**  
11 **CHARGES FROM REVIEW IN THIS PROCEEDING AND THEREFORE**  
12 **CONDUCTING PIECEMEAL RATEMAKING?**

13 A. AE has excluded certain pass-through charges from this ratemaking process. A pass-  
14 through charge is a charge that a utility merely passes along to customers without any kind  
15 of manipulation of the charge. Examples of pass-through charges are power production and  
16 fuel costs, sales taxes, Electric Reliability Council of Texas ("ERCOT") fees, as well as  
17 transition charges.<sup>7</sup> Pass-through charges are typically charges that are assessed against a

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<sup>6</sup> *Application of AEP Texas Central Company for Authority to Change Rates*, Docket No. 28840, Finding of Fact No. 257 (Aug. 15, 2005).

<sup>7</sup> Utilities are allowed to securitize or refinance their regulatory assets and/or stranded costs (assets that become uneconomical as a result of deregulation) as long as it benefits ratepayers. Securitizing debt provides funding at a lower cost than traditional utility funding. Utilities are also allowed to recover the transaction costs of securitization through this fee. Public Utility Commission of Texas, *Electricity Options – Charges on your Electric Bill*, [https://www.puc.texas.gov/consumer/electricity/bill\\_e.aspx](https://www.puc.texas.gov/consumer/electricity/bill_e.aspx) (last visited Apr. 29, 2016).

1 utility over which the utility has no control. AE has included in its pass-through charges,  
2 expenses for internal programs such as energy efficiency and street lighting. AE has  
3 maintained that Austin City Council should only consider pass-through charges during the  
4 Austin City budget process (“budget process”) as they have in the past. This is despite the  
5 fact that pass-through charges were considered in PUC Docket No. 40627 and that since  
6 that time there has been no other full rate proceeding. Though over the past five years,  
7 pass-through charges have been considered during the budget process, there is no reason  
8 these charges cannot and should not be reviewed during a full ratemaking proceeding, a  
9 proceeding in which the rates will be evaluated in conjunction with the reasonableness of all  
10 rates and charges to customers for electric service. It is imperative that the manner of  
11 calculating the pass-through charges should be examined in this review considering that at  
12 this time, pass-through charges make up approximately 50% of a customer’s bill.

13 Despite the importance of conducting a thorough review of all customer charges, AE  
14 has avoided having to provide the full cost of these pass-through charges by claiming that a  
15 majority of the costs associated with the pass-through charges were protected competitive  
16 material because they are related to fuel expenses. Since AE refused to allow a Protective  
17 Order to be implemented in this proceeding, as is customary at the PUC, any information  
18 regarding competitively sensitive material was not provided. Therefore, unlike a PUC rate  
19 case where parties review confidential information under a protective order, a full analysis  
20 of AE’s rates was impossible to conduct here. **Understanding the pass-through charges**  
21 **is also critical to the complete understanding of the impacts that a change in the base**  
22 **rate would have on any particular rate class because there may be an offset due to**

1 **pass-through revenues associated with that particular class.** By not providing for a full  
2 analysis of ALL rates and charges, AE is requiring parties as well as the Austin City  
3 Council to conduct piecemeal ratemaking because a full review of all rates and charges and  
4 how they interact with each other can never be fully achieved through AE's current method  
5 of evaluation.

6 **Q. ARE ADJUSTMENTS DUE TO CHANGES IN PASS-THROUGH CHARGES**  
7 **COMMON IN RATEMAKING?**

8 **A.** Yes. The riders included in rates schedules approved for transmission and distribution  
9 utilities by the PUC, like the transmission cost recover factor ("TCRF") and energy  
10 efficiency cost recovery factor ("EECRF"), allow an investor-owned utility to adjust for  
11 changes to pass-through charges. Specifically, the PUC allows adjustments to be made to  
12 changes in transmission costs (done in a TCRF), changes in costs to administer Energy  
13 Efficiency programs (done in an EECRF), and changes in fuel costs for non-ERCOT  
14 utilities (all pass-through charges). This is allowed for in PUC SUBST. R. §25.193(b)(1) (16  
15 TEX. ADMIN. CODE §25.193(b)(1) (TAC)), which authorizes an adjustment clause to a  
16 utility's tariff "to charge or credit its customers for the amount of wholesale transmission  
17 cost changes approved or allowed by the commission to the extent that such costs vary from  
18 the transmission service cost utilized to fix the base rates of the [Distribution Service  
19 Provider]." Fuel factors may also be established in the utility's base rate case or in a  
20 separate proceeding dealing specifically with fuel costs. The types of fuel expense eligible  
21 and not eligible for recovery through the fuel factor are specific and outlined by FERC  
22 System of Accounts, PUC SUBST. R. §25.236 (16 TAC §25.236).

1   **Q    BECAUSE THESE PASS-THROUGH CHARGES ARE ANALYZED DURING THE**  
2   **AUSTIN CITY BUDGET PROCESS, WHY IS THERE STILL A CONCERN WITH**  
3   **PIECEMEAL RATEMAKING IF THEY ARE NOT INCLUDED WITHIN THIS**  
4   **RATEMAKING PROCESS?**

5   A.   While the budget process provides the opportunity for customer input, it does not allow for  
6   discovery. Discovery, under a Protective Order, is necessary to allow a full evaluation of all  
7   inputs into the pass-through charges. Though the budget process might be a stopgap review  
8   when a full rate proceeding is not conducted, it is imperative that, at least every five years, a  
9   full analysis of all costs and revenues related to pass-through charges is conducted. This is  
10   the best way to prevent piecemeal ratemaking.

11           The best way to conduct a full analysis of pass-through charges, and conduct a full  
12   rate analysis, instead of participating in piecemeal ratemaking is to allow pass-through  
13   charges to be vetted in a full ratemaking proceeding, like the one currently being conducted.  
14   A full ratemaking proceeding allows citizens and members of the Austin City Council to  
15   question AE's analysis and inputs into their pass-through charges to make sure AE is not  
16   double dipping by including in base rates charges that are also included as part of a pass-  
17   through. By not including a complete analysis of pass-through charges in this ratemaking  
18   proceeding, the Austin City Council is endorsing piecemeal ratemaking. The best way to  
19   prevent piecemeal ratemaking is to allow all rates that will affect a customer's bill to be  
20   fully and completely analyzed during a review process that allows discovery and analysis of  
21   the relationship of all inputs with one another.



1 **Q. WHAT IS YOUR RECOMMENDATION IN ORDER TO AVOID PIECEMEAL**  
2 **RATEMAKING BY AUSTIN CITY COUNCIL?**

3 A. By allowing for a full review of all AE rates at least every five years, as contemplated by  
4 Austin City Ordinance No. 20120607-055, piecemeal ratemaking could be avoided. This  
5 Ordinance states that “[t]he Council adopts as policy that Austin Energy’s rates should be  
6 reviewed at least once every five years” and there is nothing in the ordinance limiting the  
7 scope of that review. There is nothing preventing the Austin City Council from instructing  
8 AE to perform a full analysis of ALL rates and charges every five years. A process that  
9 would allow for review of all of AE’s cost when a cost of service study is performed could  
10 eliminate piecemeal ratemaking and result in a more efficient and accurate result because  
11 the interaction of all rates will be fully analyzed in one proceeding. As a result, a  
12 comprehensive recommendation could be presented to the Austin City Council for review.  
13 The review should allow for discovery, under a protective order, and a vetting of all of AE’s  
14 costs not just half of the costs that are charged to customers. The pass-through charges,  
15 which normally appear as riders, could then be adjusted every year, or more often as needed  
16 to conform to the language of the approved tariffs like Austin City Council has done  
17 between current ratemaking proceedings. If this procedure was adopted, the transmission  
18 costs and revenue could be reflected in base rates with interim adjustments for changes as  
19 they occur in between full rate cases with new cost of service studies. Additionally, Austin  
20 City Council could adjust charges associated with the collection of the Community Benefit  
21 Charge on an interim basis with a full vetting occurring during a full rate case. This  
22 approach will lessen the occurrence of over/under recovery by AE and provide more

1 certainty to the ratepayers as well as more trust that revenues/costs are properly aligned and  
2 allocated. Customer confidence in AE's rates should be a priority with the Austin City  
3 Council and the best way to instill confidence is with a transparent process that includes the  
4 analysis of all rates and charges and a demonstration that all rates and charges are just and  
5 reasonable.

6 **V. ADJUSTMENTS TO AE'S REVENUE REQUIREMENT**

7 **Q. WHAT IS YOUR RECOMMENDED REVENUE REQUIREMENT FOR AE?**

8 **A.** I recommend a total revenue requirement for AE of \$1,032,140,819, this represents a  
9 decrease in AE's request of \$185,086,492.

10 **Q. WHY ARE YOU RECOMMENDING THAT SOME OF AE'S EXPENSES BE**  
11 **DISALLOWED FROM RECOVERY?**

12 **A.** After reviewing *Austin Energy's Tariff Package: 2015 Cost of Service Study and Proposal*  
13 *to Change Base Electric Rates* (Jan. 25, 2016) and accompanying spreadsheets and files, as  
14 well as AE's responses to Requests for Information (RFI) I have found that AE is requesting  
15 recovery for items that are not necessary and reasonable to provide electric service and  
16 should therefore not be charged to customers. In following the general principles of  
17 ratemaking followed by the PUC, my recommendations ensure that all costs included in  
18 rates are necessary and reasonable to provide electricity service and that the test year does  
19 not include any expenses that are non-recurring and therefore do not need to be recovered  
20 on a recurring basis.

21 Through my analysis, I have found that AE has expended funds for activities that are  
22 not necessary and reasonable to provide electricity service to AE's ratepayers. Additionally,

1 I have identified other costs that should have been shared with other City of Austin  
2 departments or paid for through other City of Austin funds, like the General Fund. Finally,  
3 some of AE's requested levels of expense were not known and measurable, which is the  
4 standard for inclusion of cost beyond the test year under PUC precedent. Based on my  
5 analysis, I am recommending the following specific adjustments:<sup>8</sup>

- 6 • Reducing the amount of Capital Improvement Program ("CIP") transfer,  
7 resulting in an adjustment of \$38,341,454.
- 8 • Increasing the amount of Transmission Revenue and expense, resulting in a net  
9 adjustment of \$4,510,436.
- 10 • Removing the Non-Nuclear Decommissioning expense from miscellaneous  
11 power production expense, resulting in an adjustment of \$19,442,308.
- 12 • Removing test year expenses for funding the City of Austin's Economic  
13 Development Department, resulting in an adjustment of \$9,090,429.
- 14 • Reallocating Customer Care and Billing Expenses to other City Departments,  
15 resulting in an adjustment of \$10,371,210.
- 16 • Eliminating the loss on the disposal of assets, resulting in an adjustment of  
17 \$7,170,039.
- 18 • Reducing AE's requested amount for Outside Services, resulting in an  
19 adjustment of \$6,762,767.
- 20 • Decrease in uncollectible expense, resulting in an adjustment of \$7,591,813
- 21 • Increasing the number of years to amortize the rate case expenses, resulting in an  
22 adjustment of \$215,333.

23 **Q. BRIEFLY DISCUSS AE'S REQUESTED AMOUNT FOR CIP TRANSFER?**

24 A. AE requested \$88,341,454 of internally generated cash to transfer for CIP expenditures,  
25 based on AE's total construction spending for fiscal year ("FY") 2015 for electric utility  
26 related projects. AE maintains a CIP Fund which is used to pay for construction projects.  
27 In total, during FY 2015, AE incurred \$158,169,688 in total costs for power production,  
28 transmission, distribution, and customer service support. AE funded \$88,341,454 of this

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<sup>8</sup> As previously stated, \$70 million of my recommended \$185 million represents AE's PSA adjustment made after the filing of the Tariff Package and instituted in April. These recommendations represent an additional \$115 million in reductions I recommend be made and will be discussing in this testimony.

1 with cash and the remaining \$69,828,233 with debt, which translates into a 56% cash / 44%  
2 debt funding ratio. These calculations are reflected on AE Tariff Package WP C-3.4.1.  
3 However, also reflected on WP C-3.4.1, AE appears to be recommending a 50% cash/debt  
4 funding ratio.<sup>9</sup> This is despite the fact that the amount requested of approximately \$88  
5 million is based on 56% cash funding of total construction expenditures. A 50% cash  
6 funding policy would have resulted in a requested amount of \$79,084,844, or \$9,256,610  
7 less than AE's request. At this time it is unclear what funding ratio AE is requesting.

8 **Q. WHAT HAS AE'S HISTORY BEEN WITH RESPECT TO THE RATIO OF CASH**  
9 **AND DEBT FUNDING FOR CONSTRUCTION OF UTILITY (NON-NEPA)**  
10 **ASSETS?**

11 **A.** Based on numbers provided by AE, as shown on WP C-3.4.1 of the Tariff Package, over the  
12 last four fiscal years, AE has funded \$280 million (46%) of construction with debt and \$329  
13 million (54%) of construction with cash. In addition, AE has funded its power production  
14 construction with 21% debt funding and 79% cash funding. As shown on WP C-3.4.1 the  
15 total actual expenditures for power production for the years 2012-2015 was \$85,878,146, of  
16 which \$68,083,362 was funded by cash.

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<sup>9</sup> *Austin Energy's Tariff Package: 2015 Cost of Service Study and Proposal to Change Base Electric Rates* at WP C-3.4.1, ln 63 ("Tariff Package").

1 **Q. BASED ON THE DISCUSSION ABOVE, DO YOU AGREE WITH AE'S**  
2 **PROPOSED TEST YEAR AMOUNT FOR INTERNALLY GENERATED CASH**  
3 **FOR THE CIP TRANSFER?**

4 **A.** No, I do not believe a one year snapshot of construction expenditures is representative of  
5 what AE will incur for construction in the future. As recent as FY 2013, AE had actual  
6 construction expenditures that were approximately \$15 million less than proposed here.  
7 Specifically, in FY 2013, AE spent a total of approximately \$143 million on construction  
8 projects, which represents an amount approximately \$15 million less than AE's current  
9 request of \$158,169,688. I propose that AE look back several years in order to assess what  
10 AE's "normal" level of construction expenditures is. In addition, I recommend the level of  
11 power production construction be excluded from consideration for internally generated cash  
12 for the transfer to the CIP Fund for reasons I will describe in more detail below.

13 Based on this strategy and after reviewing AE's historical funding (FY 2012-2015)  
14 for transmission, distribution, distribution substation, customer service (metering and  
15 billing) and support services, I recommend AE be allowed \$125,000,000 in total per year  
16 for construction. I also recommend that 40% of this total be funded with cash for this case  
17 to correct for AE's use of cash at 546% funding in the prior 4 years. This represents the  
18 average amount AE has spent on construction between FY 2012 and 2015. In reviewing  
19 AE's future construction plans, I reviewed AE's most recent five year capital plan as shown  
20 in AE's Official Statement ("OS") associated with AE's 2015 Bond Refunding. The five  
21 year plan as noted in that OS, indicates that the five year average for transmission,  
22 distribution, distribution substation, customer service (metering and billing) and a three year

average of facilities, technology and support services, indicate a reasonable amount for total construction of approximately \$125 million per year as well. The difference in my recommended \$125,000,000 in total expenditures at a 40% cash ratio results in \$50,000,000, which is a decrease of \$38,341,454 from AE's request of \$88,341,454 for cash to transfer to the CIP Fund. I am therefore recommending that AE's cost of service include only \$50 million per year for internally generated cash to transfer to the CIP Fund in setting AE's base rates. The calculation of my adjustment is shown below.

**Transfer to Capital Improvement Projects**

	<b>AE Requested</b>	<b>Adjustment</b>	<b>NXP/Samsung Recommended</b>
Total Annual Expenditures	\$ 158,169,688	(\$33,169,688)	\$125,000,000
Percent Cash	56%		40%
Cash in Base Rates	\$ 88,341,455	\$ (38,341,455)	\$ 50,000,000

**Q. AS YOU MENTIONED EARLIER, YOU HAVE EXCLUDED ALL CONSTRUCTION EXPENDITURES FOR POWER PRODUCTION FROM CONSIDERATION FOR CASH FUNDING IN THIS CASE. PLEASE EXPLAIN THE RATIONALE FOR THIS EXCLUSION.**

A. I am not suggesting that AE will not incur construction expenditures for power production. Instead, I am suggesting that the Austin City Council has not determined AE's next power supply incremental or the level of construction expenditure needed to support it. If AE pursues plans to construct a gas fired plant, then at that time it would be reasonable to include those costs. However, we do not know that AE will pursue these plans and incur those expenditures, instead AE could decide to contract for power supply, as it has done for

1 wind and solar and other power sources. If AE contracts for power supply, then those  
2 charges would be passed through to customers as power supply contract costs through  
3 power supply and fuel adjustment clause. If this is done, then the cash funding required  
4 through rates would be minimal. Because the Austin City Council has not made a decision  
5 with respect to near term power supply, it is not prudent to include construction  
6 expenditures for power production in this proceeding. These costs should not be included  
7 until they are known and certain to be incurred.

8 **Q. IF AUSTIN CITY COUNCIL MAKES A FINAL DETERMINATION WITH**  
9 **REGARDS TO A POWER SUPPLY SOURCE THAT WOULD REQUIRE**  
10 **FUNDING BY AE, HOW WOULD YOU PROPOSE IT BE FINANCED?**

11 **A.** I would recommend that AE finance the power supply source with debt funding. AE's  
12 history with power supply funding has been to rely significantly on cash funding of power  
13 supply, as evidenced by the 79% cash funding AE utilized over the last four years. It  
14 doesn't seem reasonable or prudent to me for AE to expect customers to provide cash  
15 funding at such a high level for power production plant that may have a useful life of up to  
16 40 years. The source of funding should match the time period that the asset is used and  
17 useful in providing service. To do otherwise results in today's ratepayers funding with cash  
18 the assets that serve future ratepayers, which would be better funded through debt for a term  
19 that matches the life of the asset.

20 **Q. BASED ON YOUR RECOMMENDATIONS REGARDING THE CIP TRANSFER**  
21 **AND THE POWER SUPPLY SOURCE FUNDING, ARE YOU RECOMMENDING**

**A 40% CASH FUNDING AND A 60% DEBT FUNDING RATIO IN THIS CASE  
FOR ALL ASSET FUNDING?**

**A.** No, I am not recommending a 40% cash / 60% debt funding ratio in the long term, just for this rate case. I have no problem with a 50% cash and 50% debt funding strategy over the long term with respect to rate setting, if that is Austin City Council's desires. I believe a 50/50 debt/equity ratio target for balance sheet capital asset funding is reasonable and is also in compliance with Council Ordinance No. 20120607-055.<sup>10</sup> However, in recent years AE has relied more heavily on cash funding of capital assets despite the low cost of capital in the market over the same period. This has led in part to AE's balance sheet ratio of debt/equity funding of 45% debt and 55% equity and a greater reliance on cash revenue from ratepayers. Because of this, I think using a 60% debt strategy in the near term for certain assets would not unreasonably change the long term goal of equal funding from both debt and equity.

**Q. PLEASE EXPLAIN YOUR ADJUSTMENT TO AE'S REQUESTED  
"TRANSMISSION OF ELECTRICITY BY OTHERS" INCLUDED IN THE COST  
OF SERVICE ("COS").**

**A.** Transmission service (and rates) within ERCOT are regulated by the PUC. Each year, the PUC establishes an updated ERCOT statewide postage stamp rate, which is the consolidation of all PUC approved individual postage stamp rates for all ERCOT

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<sup>10</sup> Austin, Tex., Ordinance No. 201220607-055, *An Ordinance Prescribing and Levying Rates and Charges for Sales Made and Services Rendered in Connection with the Electric Light and Power System of the City of Austin for Residential, Commercial, Public, and Other Uses of Electric Light and Power Sold and Served by the City of Austin* at Part 7 (2012) ("[t]he Council adopts a policy of targeting a debt-to-equity ratio of 60/40 for financing electric utility capital projects until October 1, 2014, and reaffirms the current long-term policy of maintaining a 50/50 ratio").



1 transmission owning entities. Each load serving entity in ERCOT is then assessed ERCOT  
2 transmission charges based on that entity's previous years' average four coincident peaks (4  
3 CP) and the updated ERCOT statewide postage stamp rate. AE's proposed known and  
4 measurable change to ERCOT transmission expense is based on the 2015 statewide postage  
5 stamp rate of \$46.403634 multiplied times AE's normalized 4 CP of 2,518,250 kW to  
6 derive its test year ERCOT transmission expense of \$116,855,952.

7 **Q. WHERE IS THIS CHARGE REFLECTED IN THE COS AND BY WHAT**  
8 **MECHANISM IS THIS CHARGE RECOVERED?**

9 A. AE's proposed ERCOT transmission expense is properly recorded in FERC account 565 -  
10 TRANSMISSION OF ELECTRICITY BY OTHERS. AE is proposing to recover the  
11 proposed ERCOT transmission expense of \$116,855,952 through the regulatory adjustment  
12 clause as shown on AE Schedule G-7 line 23.

13 **Q. DO YOU AGREE WITH AE'S PROPOSED ADJUSTMENT?**

14 A. No. AE should use the most recent PUC approved ERCOT statewide postage stamp rate  
15 and that this rate should be assessed against AE's most recent 4 CP.

16 **Q. PLEASE EXPLAIN YOUR RECOMMENDATION AND HOW IT DIFFERS FROM**  
17 **AE'S PROPOSED RECOVERY.**

18 A. AE did not use the most recent ERCOT statewide postage stamp rate approved by the PUC.  
19 AE used the 2015 ERCOT statewide postage stamp rate approved March 2015 in PUC  
20 Docket No. 43881, *Commission Staff's Application to Set 2015 Wholesale Transmission*  
21 *Service Charges for the Electric Reliability Council of Texas* (associated with the 2015

transmission expense matrix). Subsequently, the PUC has approved an updated ERCOT statewide postage stamp rate for 2016 in PUC Docket No. 45382, *Commission Staff's Application to Set 2016 Wholesale Transmission Service Charges for the Electric Reliability Council of Texas* (2016 transmission matrix, approved March 25, 2016). The spreadsheet (matrix) attached to the PUC order clearly identifies AE's ERCOT transmission expense responsibility to be \$126,825,202, based on the updated ERCOT statewide postage stamp rate of \$50.48097 and AE's previous summer 4 CP of 2,512,336 kW. Thus AE's known and measurable ERCOT transmission expense should be \$126,825,202 rather than \$116,855,952. I am therefore recommending that an adjustment of \$9,969,250 be approved. Further, I am recommending that AE's regulatory adjustment charge be increased by \$9,969,250 to assure proper recovery of AE's increased expense for this cost of service item.

**Q. WHAT IS YOUR PROPOSED ADJUSTMENT TO AE'S TRANSMISSION SERVICE REVENUE?**

A. I am recommending that AE's transmission service revenue be increased by \$14,479,686 to reflect an amount for transmission revenue of \$76,609,559, as stated in Texas PUC Docket No. 45382, *Commission Staff's Application to Set 2016 Wholesale Transmission Service Charges for the Electric Reliability Council of Texas* (2016 transmission matrix). The worksheet (matrix) attached to the Order in that docket identified that ERCOT load serving entities are responsible for reimbursing AE for transmission service provided by AE to such load serving entities at a rate requested by AE and approved by the Texas PUC in June 2014. On April 11, 2014, AE filed PUC Docket 42385, *Application of City of Austin dba*

1 *Austin Energy for Interim Update of Wholesale Transmission Rates Pursuant to PUC Subst.*  
2 *R. §25.192(h)(1)*, in which AE requested an increase in its transmission service rate. On  
3 June 3, 2014, the PUC approved AE's 15.7% requested transmission rate increase; and AE's  
4 transmission rate was increased from \$1.002466 to \$1.160111.<sup>11</sup> The Order also approved  
5 AE's requested total transmission cost of service of \$75,697,440.<sup>12</sup> Based on an increase in  
6 the ERCOT 4 CP, the PUC in Docket 45382 identified that AE was entitled to collect  
7 \$76,609,599 in revenue for transmission service provided by AE to ERCOT load serving  
8 entities.

9 **Q. WHAT IS THE AMOUNT OF TRANSMISSION SERVICE REVENUE INCLUDED**  
10 **BY AE IN ITS REVENUE REQUIREMENT?**

11 **A.** Referring to AE Tariff Package WP E-5.1.1, AE has reduced its FY 2014 transmission  
12 revenue of \$68,974,261 by \$6,844,343 to a test year amount of \$62,129,919. The WP  
13 explanation is that the approximately \$6.8 million reduction is "an adjustment to set  
14 Wholesale Transmission Revenue equal to Wholesale Transmission COS."<sup>13</sup> The WP sets  
15 forth a calculation of transmission cost of service of \$62,129,919. In NXP and Samsung's  
16 Fourth Request for Information to Austin Energy, RFI 4-17, NXP and Samsung asked AE  
17 why it was stating that its transmission revenue was \$62,129,919 despite the fact that in FY  
18 2014 AE's recorded transmission revenue was \$68,974,261 and reported in its FY 2014-15  
19 Fourth Quarter Report that it expected to receive \$74.3 million from this revenue source in

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<sup>11</sup> *Application of City of Austin dba Austin Energy for Interim Update of Wholesale Transmission Rates Pursuant to PUC Subst. R. §25.192(h)(1)*, Docket No. 42385, Ordering Paragraph 1 (Jun. 3, 2014),

<sup>12</sup> *Id.*

<sup>13</sup> Tariff Package at WP E-5.1.1.

1 FY 2015. In response, AE once again stated that the approximately \$62 million is the  
2 amount required to offset test year transmission revenue requirements appropriately  
3 recovered from load entities within ERCOT.<sup>14</sup> This response is baffling given that AE itself  
4 recognizes that it expects to receive \$74.3 million in FY 2015 and the 2016 PUC Order  
5 identifies that AE is entitled to collect \$76.6 million from the date of that Order. Finally,  
6 AE staff member Russell H. Maenius filed testimony in AE Docket No. 42385, *Application*  
7 *of City of Austin dba Austin Energy for Interim Update of Wholesale Transmission Rates*  
8 *Pursuant to PUC Subst. R. §25.192(h)(1)*, before the PUC supporting a requested  
9 transmission revenue requirement of \$75,697,440.<sup>15</sup> The PUC approved AE's request  
10 setting a transmission revenue requirement of \$75,697,440 and AE's proposed transmission  
11 rate of \$1.160111.

12 **Q. IS IT POSSIBLE THAT AE IS OFFSETTING ITS ERCOT TRANSMISSION**  
13 **EXPENSE, RECOVERED THROUGH THE REGULATORY ADJUSTMENT**  
14 **CLAUSE, WITH A PORTION OF THE TRANSMISSION REVENUE IT**  
15 **RECEIVES?**

16 A. This is possible, however, if that were the case, it would be fairly easy to provide that  
17 explanation in response to NXP/Samsung's' RFI 4-17. Further, I believe if this were the

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<sup>14</sup> See, *Austin Energy's Tariff Package: 2015 Cost of Service Study and Proposal to Change Base Electric Rates*, Austin Energy's Response to NXP Semiconductors' and Samsung Austin Semiconductor, LLC's Fourth Request for Information at 4-17 (Mar. 28, 2016).

<sup>15</sup> *Application of City of Austin dba Austin Energy for Interim Update of Wholesale Transmission Rates Pursuant to PUC Subst. R. §25.192(h)(1)*, Direct Testimony of Russell H. Maenius at 7, ln 5 (Apr. 11, 2014).

1 case, AE would have identified an offsetting revenue credit to its proposed recovery of  
2 transmission expense on Schedule G-7 line 23. This appears to be a transparency problem.

3 **Q. PLEASE SUMMARIZE YOUR ADJUSTMENT TO AE'S TRANSMISSION**  
4 **SERVICE REVENUE.**

5 **A.** I am recommending that AE's transmission service revenue be increased by \$14,479,686 to  
6 reflect an amount for transmission revenue of \$76,609,559 as approved in PUC Docket No.  
7 45382, *Application of City of Austin dba Austin Energy for Interim Update of Wholesale*  
8 *Transmission Rates Pursuant to PUC Subst. R. §25.192(h)(1)* (2016 transmission matrix).

9 **Q. WHAT ARE YOUR RECOMMENDED ADJUSTMENTS TO NON-NUCLEAR**  
10 **DECOMMISSIONING?**

11 **A.** Austin Energy included \$19,442,308 in O&M for decommissioning costs for Decker Creek,  
12 Fayette Power Plant, and Sandhill Energy Center. Previously, funds for non-nuclear  
13 decommissioning were treated as a reserve. However, AE has relied upon a report produced  
14 by NewGen Strategies & Solutions ("NewGen"), but recommends the maximum amounts  
15 identified by NewGen, which could potentially result in higher than necessary  
16 decommissioning costs.<sup>16</sup> The total costs established by AE based on the NewGen report  
17 are: \$28 million for Decker Creek; \$30 million for Fayette Power Plant; and, \$22 million for  
18 Sand Hill Energy Center.

19 The NewGen report surveyed the various decommissioning costs per kW allowed by  
20 the selected PUCs and determined the mean for gas-fired steam plants to be \$17.40 per kW.

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<sup>16</sup> Tariff Package at Appendices, Bates No. 527 (*NewGen Strategies & Solutions Decommissioning Report*).

1 Despite this mean, AE is requesting \$38.57 per kW for the Decker Creek Units 1 & 2,  
2 which is even higher than the inflated amount included in the report. This \$21.17 per kW  
3 difference, as in comparison to the mean, is unreasonable and unnecessarily high. Using the  
4 mean of \$17.40 per kW, I am recommending a total non-nuclear decommissioning for  
5 Decker Creek Units 1 and 2 of \$12,~~632~~545,400 million. I only recommend  
6 decommissioning costs associated with Decker Creek Units 1 & 2 be allowed into rates at  
7 this time because, though not authorized for decommissioning at this time, these are the  
8 only units that the Austin City Council has stated they are considering retiring within the  
9 next 4 years. Currently, the Austin City Council has not affirmatively approved  
10 decommissioning by 2018. Neither the Fayette Power Plant nor the Sandhill Energy Center  
11 have been formally designated for decommissioning and no timeline exists at all.<sup>17</sup>

12 **Q. DID THE NEWGEN REPORT RECOMMEND INCLUDING THE NON-NUCLEAR**  
13 **EXPENSE AS AN O&M EXPENSE?**

14 A. No, NewGen recommended the amount be included as a reserve as specified in AE's  
15 current Financial Policies.

16 **Q. DO YOU AGREE WITH AE'S RECOMMENDATION TO COLLECT THESE**  
17 **EXPENSES THROUGH O&M AND NOT THROUGH RESERVES AS NEWGEN**  
18 **RECOMMENDED?**

19 A. No. AE has classified decommissioning expenses as O&M expenses. It appears AE has  
20 done this because they find decommissioning expenses best resemble O&M expenses.

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<sup>17</sup> *Austin Energy's Tariff Package: 2015 Cost of Service Study and Proposal to Change Base Electric Rates*, Austin Energy's Response to NXP Semiconductors' and Samsung Austin Semiconductor, LLC's Fourth Request for Information at 4-3 and 4-4 (Mar. 28, 2016).

1 According to AE, O&M expense “represents funds to be spent for specific purposes, as  
2 opposed to the reserve funds general cash balances which can be used to mitigate  
3 unpredictable, risky events.”<sup>18</sup> I disagree with this statement because O&M expense should  
4 be paid when the expense is incurred. Therefore, because these expenses will not occur  
5 until the Units are decommissioned, they are not properly classified as O&M expenses. The  
6 amount included in O&M collected through rates will be included in AE’s operating  
7 balance because they did not incur or pay the expense.

8 **Q. WHAT ARE YOU RECOMMENDING?**

9 A. As previously stated, I recommend that the reserve amount included in rates for non-nuclear  
10 decommissioning be limited to \$12,545,632,400 for Decker Units 1 & 2 based on the median  
11 of the survey of PUCs in the NewGen report. Further, this amount should be included as a  
12 reserve, not O&M, and funded from the excess reserves already collected by AE.

13 **Q. PLEASE EXPLAIN YOUR ADJUSTMENT TO AE’S TRANSFER TO THE CITY**  
14 **OF AUSTIN’S ECONOMIC DEVELOPMENT DEPARTMENT (“EDD”).**

15 A. AE has included \$9,090,429 as O&M for the transfer into the City’s EDD. I am  
16 recommending that this transfer not be allowed. I am recommending this because these  
17 costs are not associated with the provision of electric service and therefore should not be  
18 included in AE’s budget. EDD has been described as having a FY 2015-16 budget of  
19 ...\$47.9 million. Of this amount, \$14.8 million is for day-to-day operations and  
20 includes incremental increases for employee wages and benefits, administrative  
21 support, rental adjustments, and removes onetime funding for the Austin Tech

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<sup>18</sup> *Austin Energy’s Tariff Package Update of the 2009 Cost of Service Study and Proposal to Change Base Electric Rates*, Austin Energy’s Response to NXP Semiconductors’ and Samsung Austin Semiconductor, LLC’s Second Request for Information at 2-9 (Feb. 29, 2016).

1 Partnership.... Historically, Austin's Economic Development was budgeted in  
2 Austin Energy. This is the final year of the Council approved four-year  
3 transition to a cost-share allocation model between other City Departments....  
4 The remaining \$33.1 million of funding in EDD's FY 2015-16 Budget is for  
5 cultural arts contracts, Economic Incentive Payments, small business loans, and  
6 for business retention and music venue assistance.<sup>19</sup>

7 The expenditures for these programs, while worthy, are not necessary and reasonable to  
8 provide electric service and should therefore not be paid for by AE ratepayers. If the City  
9 Council continues to fund these programs, it should do so out of the proper budget, the  
10 General Fund.

11 **Q. IS IT YOUR OPINION THAT THESE ACTIVITIES ARE NOT BENEFICIAL TO**  
12 **THE CITY OF AUSTIN?**

13 **A.** No. As stated above, these programs, while worthy of the City of Austin, are not necessary  
14 and reasonable to provide electric service and should therefore not be paid for by AE  
15 ratepayers. Economic growth activities do benefit the community; however, they have little  
16 to no association with the provision of electricity. I do not think it is appropriate to use  
17 ratepayer money to encourage growth and energy consumption, while charging ratepayers  
18 for programs to reduce electricity consumption. The City Council initiated a transition plan  
19 to allocate economic development funding to the General Fund or other City departments,  
20 which is more appropriate, however, at this time the 2016-17 budget is not approved and  
21 therefore the amount of the transition is unknown. The amount included in the COS  
22 represents the amount allocated to AE for 2015-2016 Budget<sup>20</sup> and because those services

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<sup>19</sup> City of Austin 2015-2016 Approved Budget, Austin, TX, Volume I, pg. 263.

<sup>20</sup> AE Tariff Package, WP D-1.2.8.1, Line 22, Column I.



1 are not necessary and reasonable to provide electric service, they should not be included as  
2 an AE expense.

3 **Q. HAS AE PERFORMED A COST BENEFIT ANALYSIS THAT QUANTIFIES**  
4 **BENEFITS TO THE AUSTIN RATEPAYER?**

5 **A.** No. AE's response to NXP/Samsung Request for Information 4-12 states that it did not  
6 perform a cost benefit analysis but cites redevelopment projects in downtown, Mueller, the  
7 Domain, Seaholm, and Colony Park as benefits.<sup>21</sup> However, I do not see this as a benefit as  
8 the air conditioning load of many of the customers in these redevelopment projects are  
9 served by On-Site Energy Resources ("OSER"), which is deemed as non-utility by AE. AE  
10 should be required to substantiate its claimed benefits before the cost is passed on to utility  
11 ratepayers to ensure that it is a reasonable and prudent expense.

12 **Q. HOW HAS AE ALLOCATED ITS CUSTOMER CENTER EXPENSES?**

13 **A.** AE uses an allocation methodology to share the expenses associated with its Utility  
14 Customer Center ("UCC"), which was developed in 2002, and provides services to various  
15 departments within the City of Austin. AE operates UCC and the 311 Call Center. UCC is  
16 responsible for customer billing and service for AE, Water, Waste Water, Solid Waste  
17 Services (now called Austin Resource Recovery), Drainage, and Transportation. AE  
18 included \$20,179,737, as reimbursements from other departments and funds.

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<sup>21</sup> *Austin Energy's Tariff Package: 2015 Cost of Service Study and Proposal to Change Base Electric Rates*, Austin Energy's Response to NXP Semiconductors' and Samsung Austin Semiconductor, LLC's Fourth Request for Information at 4-12 & 4-14 (Mar. 28, 2016).

1 **Q. DO YOU AGREE WITH THE ALLOCATION METHODS USED BY AE?**

2 **A.** No. I reviewed the allocation and am proposing that costs be distinguished as being solely  
3 belonging to AE from those belonging to Water and Waste Water utilities, and that these  
4 costs be allocated to all users either on the basis of revenue or number of bills, depending on  
5 which allocation is more appropriate. Though the fees and charges are billed by the  
6 combined billing system, and complaints and billing inquiries are directed to the Customer  
7 Care Service Center, there is no reason AE should be responsible for all costs; there is little  
8 justification for allocating 100% of a customer complaint expense to AE when there is  
9 evidence that a number of customer complaints regarding water are received<sup>22</sup> and it is odd  
10 to think that in 2016 there is no way to track that type of data. Recent reports to Council  
11 concerning the number of water related complaints would indicate that someone is able to  
12 track complaints by type.

13 AE's method makes distinctions between the three types of bills to customers, each  
14 of which is associated with a different expense: Customer Billing, Customer Billing – CIS,  
15 and Customer Billing - Postage. Since the bills are generated by the Customer Information  
16 System and mailed, the same allocation method should be used – each area should be  
17 allocated based on the total number of bills for all users. The Table 1 below compares my  
18 recommended allocations to AE's allocations.

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<sup>22</sup> *Austin Energy's Tariff Package: 2015 Cost of Service Study and Proposal to Change Base Electric Rates*, Austin Energy's Response to the First Request for Information from NXP Semiconductors and Samsung Austin Semiconductor, LLC's at 1-96, Attachment 1, at 66 of 81 (Feb 28, 2016).

1

**Table 1: Recommended Allocations of Customer Care Costs**

Org name	AE	NXP/Samsung
Customer Complaint	100 % E	Service Revenue by Utility
Payment Processing	Service Revenue by Utility	Service Revenue by Utility
System Management	Service Revenue by Utility	Service Revenue by Utility
Customer Billing	Bills by E, W, WW Only	Bills by Utility
Customer Billing - CIS	Service Revenue by Utility	Bills by Utility
Customer Billing - Postage	Bills by Utility	Bills by Utility
Rev Measurement - Field Services	Service Orders by Utility	Service Orders by Utility
Contact Compliance (Meter Reading)	Meters Read	Meters Read
Revenue Measure & Control	Bills by E, W, WW Only	Bills by Utility
Revenue Measurement - Dispatch	Service Orders by Utility	Service Orders by Utility
Call Center	Bills by E, W, WW Only	Bills by Utility
Call Center - Base Telephone	100 % E	Bills by Utility
Credit Management	Service Revenue by Utility	Service Revenue by Utility
Consumer Services	100 % E	Bills by Utility
RMGT Service Orders	No Activity	No Activity
Quality Management	Bills by E, W, WW Only	Bills by Utility
Current Diversion	Total Meters by Utility	Total Meters by Utility
Small commercial	Service Revenue E, W, WW	Service Revenue E, W, WW
East Branch Walk-In	Service Revenue by Utility	Service Revenue by Utility
MULTIFAMILY PARTNERSHIP PRGM	Bills by E, W, WW Only	Bills by E, W, WW Only
North Branch Office	Service Revenue by Utility	Service Revenue by Utility
Customer Services MGMT Admin	Service Revenue by Utility	Service Revenue by Utility
CIS Accounting Services	Service Revenue by Utility	Service Revenue by Utility
AE IT CIS Projects	Overall Percentage average	Overall Percentage average
CTM Allocation	Service Revenue by Utility	Service Revenue by Utility

2

3 **Q. WHAT AMOUNT DO YOU RECOMMEND BE REIMBURSED BY THE OTHER**  
4 **USER DEPARTMENTS?**

5 **A.** I am recommending that an additional \$10,371,602 be allocated to other user departments,  
6 thus reducing AE's requested revenue requirement.

7 **Q. WHAT IS YOUR RECOMMENDATION CONCERNING THE ADJUSTED TEST**  
8 **YEAR AMOUNT FOR LOSSES ON ASSET DISPOSAL?**

9 **A.** AE recorded a Test Year Loss for asset disposal of \$9,113,497, as Other Expense and

1 removed \$1,943,458 as a Non-Electric Adjustment/Transfer.<sup>23</sup> I am recommending that the  
2 remaining test year amount of \$7,170,039 be excluded in AE's revenue requirement because  
3 it is not known and measurable. This loss is also a book loss that is measured by removing  
4 the net book value of the asset after deducting any salvage value received from disposing of  
5 the asset. Since AE is using the cash flow method to determine return, this book loss should  
6 not be included.

7 AE's response to NXP/Samsung's Third Request for Information, RFI 3-4, states  
8 that the Test Year Loss for asset disposal is from the retirement of assets and is a recurring  
9 cost because it "generally" happens yearly. According to AE's response to NXP/Samsung  
10 Request for Information 4.10, the losses on the disposition of utility assets since 2010 were:  
11 \$10,213,180 in 2011; \$8,108,821 in 2012; and, \$67,256 in 2013.<sup>24</sup> While there are losses  
12 in each of the years, including the test year, the amounts vary greatly and therefore cannot  
13 be deemed as a known and measurable cost. Because the amounts vary from year to year,  
14 the amount in any particular year is not measurable. Additionally, AE did not provide any  
15 type of asset retirement plan to support the amount that may occur during the time rates  
16 from this review are in place.

17 **Q. WHAT ADJUSTMENT ARE YOU RECOMMENDING TO OUTSIDE SERVICES?**

18 A. AE's total charges (expensed and capitalized) for Outside Service contracts in the test year  
19 were \$54 million. The proposed cost of service includes \$27 million for Outside Services

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<sup>23</sup> Tariff Package, WP E-4.3, ln 6.

<sup>24</sup> *Austin Energy's Tariff Package: 2015 Cost of Service Study and Proposal to Change Base Electric Rates*, Austin Energy's Response to NXP Semiconductors' and Samsung Austin Semiconductor, LLC's Fourth Request for Information at 4-10 (Mar. 28, 2016).

Employed in the test year and AE recommends an additional increase of \$7.2 million resulting in a total cost for Outside Services of \$33 million in revenue requirement. Of the \$33 million, \$18.4 relates to IT and Technology, including a transfer of \$6.5 million to the City of Austin's Communications and Technology Management ("CTM"). I am recommending a decrease of \$6,762,767 associated with the employment of outside programmers to augment AE's information technology staff of 148 approved in the FY 2015-2016 Budget.<sup>25</sup> My adjustment removes the amount for Supplement Technology Operations. AE identified a total of \$8,925,683 for Outside Services – Employment in the test year for Federal Compliance Initiatives, Maintenance Activities, Security and Supplement Technology Operations.

The following table shows the amount included in each category referred to as Employment.

**Table 2: Outside Services**

Scope Descriptions	Number of Charges	Amount	NXP/Samsung Adjustment	NXP/Samsung Recommendation
Federal Compliance Initiatives	72	\$ 845,265.97		\$ 845,265.97
Maintenance Activities	71	\$ 863,844.76		\$ 863,844.76
Security	28	\$ 276,247.05		\$ 276,247.05
Supplement Technology Operations	457	\$ 6,762,767.05	\$ (6,762,767.05)	\$ -
(blank)	5	\$ 177,558.55		\$ 177,558.55
Grand Total	633	\$ 8,925,683.38	\$ (6,762,767.05)	\$ 2,162,916.33

Supplement Technology Operations is also referred to as Staff Augmentation. According to AE's response to NXP/Samsung Request for Information 2-1 these costs are for "activities required to support on-going operations" and "will continue as an on-going

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<sup>25</sup> *Austin Energy's Tariff Package Update of the 2009 Cost of Service Study and Proposal to Change Base Electric Rates*, Austin Energy's Response to NXP Semiconductors' and Samsung Austin Semiconductor, LLC's Second Request for Information at 6-12 at 14 (Apr. 18, 2016).

1 practice to support Austin Energy technology initiatives.”<sup>26</sup> When asked to provide the  
2 estimated cost of Staff Augmentation during the timeframe that rates from this review will  
3 be in effect, AE responded that they have not estimated future cost.<sup>27</sup> Based on these  
4 responses, AE has not demonstrated that this is a known and measurable cost that will recur  
5 in the future. Therefore, I recommend these costs be disallowed.

6 **Q. DO YOU HAVE ANY OTHER CONCERNS ABOUT THE COST ASSOCIATED**  
7 **WITH IT FUNCTIONS?**

8 A. Yes, I would recommend that the Austin City Council take a serious look at the total cost  
9 that is incurred by AE for outside contractors, whether expensed or capitalized, to assess  
10 whether more FTEs would be justified, if indeed, all of these projects and initiatives are  
11 “on-going” in nature. It also appears that many of the functions that are supported by the  
12 City of Austin’s CTM overlap with the functions of the Outside Contractors, such as  
13 licensing and training and therefore might not be prudent expenditures.

14 **Q. ARE YOU RECOMMENDING A CHANGE TO AE’S REQUESTED AMOUNT FOR**  
15 **UNCOLLECTIBLE EXPENSE?**

16 A. Yes. Uncollectible expense is usually a variable expense to revenue and is commonly  
17 adjusted in rate cases by calculating an expense factor (dividing expense by test year  
18 revenue). However, AE experienced a usually high uncollectible expense in FYs 2013 and

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<sup>26</sup> *Austin Energy’s Tariff Package Update of the 2009 Cost of Service Study and Proposal to Change Base Electric Rates*, Austin Energy’s Response to NXP Semiconductors’ and Samsung Austin Semiconductor, LLC’s Second Request for Information at 2-1 (Feb. 29, 2016).

<sup>27</sup> *Austin Energy’s Tariff Package: 2015 Cost of Service Study and Proposal to Change Base Electric Rates*, Austin Energy’s Response to NXP Semiconductors’ and Samsung Austin Semiconductor, LLC’s Fourth Request for Information at 4-29 (Mar. 28, 2016).

1 2014. Therefore, AE made a known and measurable adjustment that reduced its 2014  
2 uncollectible expense by \$4,813,622, resulting in a test year adjusted uncollectible expense  
3 of \$16,054,751.<sup>28</sup> The actual unaudited amount for 2015 was \$8,462,938.<sup>29</sup> I am  
4 recommending the use of 2015 actual, which is a \$7,591,813 reduction to the amount  
5 requested by AE. In my opinion this actual 2015 amount accurately reflects the downward  
6 trend AE has been experiencing since 2014, which is expected to continue during the time  
7 the rates from this review will be in effect.

8 **Q. PLEASE DISCUSS YOUR ADJUSTMENT TO RATE CASE EXPENSE.**

9 A. AE has requested that \$1,615,000 be included in rates as an estimate of rate case expenses  
10 for consulting services, including the rate consultants, Independent Consumer Advocate,  
11 Impartial Hearings Examiner, and Outside Attorneys. AE proposes to amortize this expense  
12 over a three year period. In addition, AE included \$47,644 of actual rate case expense from  
13 2014. Therefore, the total requested in rates by AE is \$585,977.

14 **Q. DO YOU AGREE WITH THE THREE YEAR PERIOD AE IS REQUESTING TO**  
15 **AMORTIZE THESE EXPENSES THROUGH RATES?**

16 A. No. City Ordinance No. 20120607-055 requires a cost of service study every five years,  
17 therefore I believe it is more reasonable to use an amortization period of 5 years.

18 **Q. WHAT IS YOUR NET ADJUSTMENT FOR RATE CASE EXPENSES?**

19 A. My adjustment results in a decrease of \$215,333 from AE's request.

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<sup>28</sup> Tariff Package at WP D-1.2.9, Col. F, ln 10.

<sup>29</sup> *Austin Energy's Tariff Package Update of the 2009 Cost of Service Study and Proposal to Change Base Electric Rates*, Austin Energy's Response to the Independent Consumer Advocate's Second Request for Information at 2-30, at 395 (Mar. 25, 2016).

1                                    **VI.     RESERVE FUNDS AND FINANCIAL POLICIES**

2     **Q.     WHAT IS AE REQUESTING IN TERMS OF RESERVE FUNDS?**

3     **A.**     Through use of the Cash Flow method of calculating return, AE has calculated a requested  
4             return of \$11,590,703. To come to this figure, AE has used the *existing* Financial Policies  
5             and the balances of the reserves as of September 30, 2015. Based on the existing Financial  
6             Policies, AE is requesting \$34,772,108 be added to reserves and collected through rates over  
7             a three-year period, representing the total amount requested of \$11,590,703. As further  
8             explained below, I believe AE's current reserves are too high and therefore any  
9             replenishment is unnecessary.

10    **Q.     DID NEWGEN CONDUCT AN ANALYSIS OF AE'S CURRENT RESERVES AND**  
11             **FINANCIAL POLICIES?**

12    **A.**     Yes, AE contracted NewGen to perform a review of the existing Financial Policies.  
13             Additionally, NewGen recommended changes to the existing Financial Policies for Austin  
14             City Council to consider. Based on NewGen's assessment, AE is requesting that Council  
15             approve some, but not all, of NewGen's recommendations. A summary of the NewGen  
16             recommendations can be found in AE's Tariff Package, Appendices (Bates number 437). In  
17             its report, NewGen recommended an increase in reserves of \$10,194,385 to be collected  
18             over a three year period, translating into \$3,398,128 in revenue requirement. AE did not  
19             incorporate this adjustment in its filing because, as stated above, the Council has not  
20             approved the policy changes. I do not accept NewGen's recommendation because AE's  
21             requested revenue requirement is overstated and NewGen's recommendation is based on  
22             this overstated revenue requirement.



1           Though AE has incorporated most of NewGen's recommendation, as discussed  
2           above, AE did not include NewGen's recommendation to include Non-Nuclear  
3           Decommissioning cost as a reserve, instead of as part of O&M expense as requested by AE.  
4           I reaffirm my agreement with NewGen's classification of Non-Decommissioning cost as  
5           reserve.

6   **Q.   DO YOU AGREE WITH NEWGEN'S RECOMMENDATIONS?**

7   **A.**   I agree, for the most part with the NewGen study and NewGen's recommendations. I find  
8           NewGen's recommendations to be more transparent than what is currently in place through  
9           the numerous reserves adopted by City Councils since 1989. Though it might have been  
10          reasonable to establish various reserves in the past, at this point in time, as noted in the City  
11          of Austin Internal Audit Report on Reserves (presented in the last rate review) and now by  
12          NewGen's Report, AE has far more reserves than its peers.<sup>30</sup> I also agree with NewGen's  
13          assessment that AE's calculation of cash on hand should conform to the calculation used by  
14          Moody's which is:

15               (Available unrestricted cash and investments +Eligible unused bank lines and  
16               capacity under commercial paper programs) X 365 days / Utility's annual  
17               operating and maintenance expenses exclusive of depreciation and amortization  
18               expenses)<sup>31</sup>

19          To determine the amount of reserves to be included in rates to meet the cash on hand metric,  
20          the formula used by AE and NewGen is the total O&M (including fuel) divided by 365 days

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<sup>30</sup> NewGen Strategies & Solutions, Summary of Austin Energy's Reserve Funds, July 27, 2015, Table 7.6 (Tariff Package Bates No. 478).

<sup>31</sup> Moody's Investor Service, US Public Power Electric Utility with Generation Ownership Exposure, Factor 5 (Tariff Package Bates Number 403).

1 times 150 days. This should set the target which can then be measured on a three-year  
2 average.

3 Based on my review, I recommend that the reserves that should be used to calculate  
4 the of number of days on hands are the Working Capital, Contingency, and Capital Reserve,  
5 as these are not restricted funds. As previously stated, the Nuclear Decommissioning  
6 expense should be treated as a reserve and included in the 150 day calculation.

7 NewGen also recommends that any future over-recoveries of the PSA be transferred  
8 to the Rate Stabilization Reserve, instead of refunding the over-recovery to ratepayers. I  
9 disagree with this recommendation by NewGen; I continue to recommend that AE not be  
10 allowed to collect funds from current ratepayers for future events. In addition, I recommend  
11 that AE should not be allowed to use the Rate Stabilization Funds to avoid future  
12 compliance with the Affordability requirement established by Council, which directs Austin  
13 Energy to keep rates among the 50% lowest of Texas utilities and limits any annual rate  
14 increase to no more than two percent for all customer classes.<sup>32</sup>

15 **Q. HAVE YOU MADE ADJUSTMENT TO AE'S REQUESTED RESERVE FUNDING?**

16 A. Yes, I recommend that AE's request to increase rates by \$11,590,703, to allow for the  
17 replenishment of reserve funds, be denied. I also recommend that the Rate Stabilization  
18 Reserve be eliminated. I see little justification to charge today's ratepayers for something  
19 that may or may not happen in the future, which appears to be the goal of the Rate

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<sup>32</sup> Tex., Austin, Resolution No. 20140828-157 (Aug. 28, 2014) (reaffirming the City Councils February 17, 2011 directive where "the City Council recognized the importance of economic considerations in the generation resource planning process and adopted an affordability goal calling for Austin Energy to operate so as to control all-in (base, fuel, riders, etc.) rate increases to residential, commercial, and industrial customers to 2% or less per year, and to maintain AE's current all-in competitive rates in the lower 50 percent of Texas rates overall ('Affordability Goal').").

Stabilization Reserve. Ratepayers should only be responsible for those utility costs which are known to occur, and not possible costs that might occur at some point in the future, if at all. The Rate Stabilization Reserve is especially unreasonable considering the fact that almost half of AE's total revenue requirement will be recovered from pass-through rates, effectively guaranteeing that more than half of AE's costs will be recovered as they are not subject to a full review.

**Q. PLEASE DEMONSTRATE HOW YOUR RECOMMENDATION DIFFERS FROM AE'S REQUEST.**

A. The following table shows AE's request compared to my recommendation.

**Table 3: Recommended Reserves**

	Existing Policies Days	Existing Policies with Adjusted Test Year	Reserve Study Days	Per Reserve Requirement Study	NXP/Samsung Days	NXP/Samsung Adjustments to AE Adjusted Test Year	NXP/Samsung Recommended
Working Capital							
O&M Excluding Power Supply	45	\$ 70,080,491	60	\$ 93,440,655	45	\$ (28,723,746)	\$ 64,716,909
Contingency							
O&M Excluding Power Supply	60	93,440,655	60	93,440,655	60	\$ (7,151,443)	86,289,212
Rate Stabilization							
Power Supply	90	107,412,480	105	125,314,560	-	\$ (125,314,560)	0
Capital Reserve							50%
50 % of Depreciation Expense	50%	72,825,880	50%	72,825,880	50%	-	72,825,880
Excess from Elimination of Emergency Fund						\$ 125,314,560	125,314,560
Subtotal		\$ 343,759,506		\$ 385,021,750		\$ (35,875,189)	\$ 349,146,562
Additional to meet 150 days Cash on Hand		\$ 68,862,932		\$ 27,600,688		\$ (10,770,542)	\$ 16,830,146
Total Reserves per Reserve Requirement Study		\$ 412,622,438		\$ 412,622,438		\$ (46,645,731)	\$ 365,976,708
Rating Agency Standard - 150 days cash on h	150	\$ 412,622,438	150	\$ 412,622,438	150	\$ (46,645,730)	\$ 365,976,708

As can be seen from the above table, NXP and Samsung's recommendations drops the need for the quantity of cash reserves AE has proposed. As can be seen by the drop, it is

imperative to include AE's change in the Power Supply Adjustment ("PSA") charge and non-fuel O&M to determine the proper level of reserves. AE implemented a change to its PSA with the April billing cycle. As this chart demonstrates, all AE rates can work together, proving that a full rate analysis needs to be conducted in order to fully understand and verify AE's rates.

**Q. HAVE YOU MADE ANY OTHER ADJUSTMENTS?**

A. Yes, I have also changed the recommended number of days associated with the working capital reserve; I adjusted it from 60 days of O&M, as requested by AE, to 45 days of O&M to comply with PUC SUBST. R. §25.231(c)(2)(B)(iii) (16 TAC §25.231(c)(2)(B)(iii)). The adjustments I have made, when compared to the existing balance of the reserves as of September 30, 2015, result in \$37,435,998 of *excess* cash in the reserves. The following table shows the adjustments. Based on my analysis, no additional return is justified.

**Table 4: Excess Reserve Balance**

	Reserve Balances as of September 2015 (Unaudited)		
Working Capital	\$ 251,115,560	\$ 251,115,560	\$ 251,115,560
Strategic Reserve	152,233,075	152,233,075	152,233,075
Repair & Replacement Reserve	64,071	64,071	64,071
Mark to Market Adjustment	(984,653)	(984,653)	
Total Reserves	\$ 402,428,053	\$ 402,428,053	\$ 403,412,706
	<b>AE</b>	<b>NewGen</b>	<b>NXP/Samsung</b>
Per Financial Policy Existing and Study	\$ 437,200,161	\$ 412,622,438	\$ 365,976,708
Deficiency (Excess) per Financial Policy	\$ 34,772,108	\$ 10,194,385	\$ (37,435,998)
	3	3	
Adjustments	\$ 11,590,703.00	\$ 3,398,128.27	\$ -

1 **Q. DO YOU HAVE ANY OTHER RECOMMENDATION REGARDING AE'S**  
2 **FINANCIAL POLICIES OR PROCESSES?**

3 A. Yes, I recommend that AE's financial policies incorporate more direct language that will  
4 govern the use of the reserves. For example, the financial policies should make clear that  
5 AE and Austin City Council cannot pay for long lived assets entirely from reserves. These  
6 assets should be funded through debt which as closely as possible relates to the asset's  
7 useful life to provide service. To do otherwise results in today's ratepayers paying too  
8 much of the cost of the asset and does not result in intergenerational equity. Additionally,  
9 as indicated above, the financial policies should be revised to explicitly require AE to use  
10 the Debt Service Coverage method to determine return in rate reviews, and explicitly  
11 disallow AE from using a Cash Flow method of analysis. All of the policies should also be  
12 revised to incorporate all of the metrics used by rating agencies for financial strength. In  
13 addition to the number of days of cash on hand, the other components that should be  
14 considered is the debt ratio on a three-year average and the debt service coverage.

15 I also recommend Austin City Council revise the recovery method for the  
16 transmission costs/revenue and costs for energy efficiency, and include their review in a full  
17 rate case proceeding like the one currently being conducted. The PUC has authorized  
18 recovery mechanisms for other utilities that include these costs in base rates and allow for  
19 adjustments for changes that occur outside of a base rate review. Reducing the amount of  
20 charges collected through riders will reduce AE's potential of under/over recoveries and  
21 lessen the impact of large, anticipated adjustments to customers. This is true because AE  
22 currently collects almost half of its test year cost through riders. By reducing the amount

1 AE collects through riders, AE will have more certainty in long term rates. I therefore  
2 recommend that the Austin City Council consider revising the current tariffs to allow the  
3 review of all costs in the 5 year rate review process and only authorize adjustments for  
4 incremental changes to base rates in the interim.

5 **VII. CONCLUSION**

6 **Q. PLEASE SUMMARIZE YOUR RECOMMENDED REVENUE REQUIREMENT.**

7 A. I am recommending a total COS of \$1,032,140,819. This represents a reduction of  
8 \$185,086,492 to AE's requested COS, and translates into a base rate decrease of  
9 \$132,546,001. The resulting debt service coverage of this recommendation is 2.28, which is  
10 above the minimum required by AE's current financial policies. However, this is lower  
11 than AE's request 2.77 debt service coverage. I have also included changes to the cost of  
12 Transmission in the Regulatory Charge to comply with PUC precedent. Additionally, I  
13 have included Mr. Goble's adjustment to restate the Municipal Street Lighting tariff, where  
14 the City of Austin is billed rather than the ratepayers, which results in a reduction to the  
15 Community Benefit Charge. Finally, I have incorporated Mr. Goble's adjustments to AE's  
16 allocations, resulting in an overall revenue reduction of \$202,560,790. The details of all  
17 adjustments are shown on MJF Exhibit-3.

18 **Q. DOES THIS CONCLUDE YOUR TESTIMONY?**

19 A. Yes.

**Marilyn J. Fox**  
**President**

Marilyn is a professional accountant, specializing in rate regulation, financial analysis and policy issues. She has served as an expert witness in local, state and federal proceedings. Marilyn is the President of Fox, Smolen & Associates, Inc., a certified Historically Underutilized Business.

Marilyn was employed by the City of Austin (1989-1998) as Austin's Assistant Director of the Finance and Administrative Department (1986-1989) and the City of Houston's Director of Regulatory Affairs. Her responsibilities included regulating providers of telecommunication, cable, gas and electric services, including Houston Lighting & Power (CenterPoint Energy), Southwestern Bell (AT&T), and Time Warner Cable. She processed rate filings by utilities at the city level and on appeal and monitored filings and rulemakings at the PUC.

From 1981 to 1986, Marilyn was the Assistant Director of the Accounting Division and the Manager of the Fuels Section of the Utility Evaluation Division of the PUC. Her responsibilities included reviewing rate requests and fuel reconciliation applications filed with the Commission. She filed expert testimony in administrative hearings before the PUC and supervised division staff. Prior to 1981, Marilyn worked for El Paso Electric Company as a tax accountant.

Marilyn holds a Bachelor of Arts from Texas Tech University with a History Major with Political Science and English minors. She completed Post-graduate work in Accounting and Business at The University of Texas at El Paso.

She has been a Certified Public Accountant since 1980 and is a member of the Texas Society of CPAs and the American Institute of Certified Public Accountants.

***Relevant Consulting Projects***

Commercial and Industrial Electric Market Information developed for a large municipally-owned utility

Review of Joint Natural Gas Procurement developed for a large municipally-owned utility

Legislative and Regulatory Advocacy for Energy Efficiency Legislation for environmental coalition

Review Revenue Transactions Relating to the Sale of Excess Energy for the owner of a Large Cogeneration Facility owner

Participation at the PUC in formal complaint procedure concerning disputed contracts terms and amounts charged to customers

Review of billing data from ERCOT attorneys in dispute between customer and provider.

Development of an Exemption from the Demand Ratchets of the Transmission and Distribution Utilities

Developed pole attachment agreements and rates for members of a statewide association

Assisted privately owned cable operator in negotiating pole attachment rate with large TDU

Competitive assessment for a large municipally-owned utility

Participation in TDU tariff-related complaint at PUC related to a Texas utility

Participation in City of Austin Public Involvement Committee and other proceedings related to the Austin Energy Rate Filing. Data Foundry, 2011-12.

Reviewed and Analysis of Texas Gas Service Rate Filing, City of Austin, 2009.

Review and Analysis of Texas Gas Service Gas Reliability Infrastructure Program Rate Filing, City of Austin, 2011.

Review and Analysis of Texas Gas Service Gas Reliability Infrastructure Program Rate Filing, City of Austin, 2012.

Review and Analysis of Texas Gas Service Gas Reliability Infrastructure Program Rate Filing, City of Austin, 2013.

Review and Analysis of Texas Gas Service Gas Reliability Infrastructure Program Rate Filing, City of Austin, 2014.

Review and Analysis of Texas Gas Service Gas Reliability Infrastructure Program Rate Filing, City of Austin, 2015.

***PUC Dockets Since 1998***

*Docket 21527 – Application of TXU Electric Company for Financing Order to Securitize Regulatory Assets and Other Qualified Costs*

*Docket 20290 – Application of Central Power and Light Company to Reconcile Fuel Costs*

*Docket 33967 – Complaint of Greater Houston Retailers Association Against Tara Energy LP*

*Docket 34800 – Application of Entergy Gulf States, Inc. for Authority to Change Rates and to Reconcile Fuel Costs*



Docket 38448 – *Petition of Just Energy Texas, LP for the Commission to Resolve a Billing Dispute and Brief in Support of Petition*

Docket 40627 – *Petition by Homeowners United for Rate Fairness to Review Austin Rate Ordinance No. 20120607-055*

Docket 41474 – *Application of Sharyland Utilities, L.P. to Establish Retail Delivery Rates, Approve Tariff for Retail Delivery Service, and Adjust Wholesale Transmission Rate*

Docket 41987 – *Complaint of Multiple RV Tenants of Live Oak Resort, Inc. Against Live Oak Resort, Inc.*

Docket 42252 – *Application of Southwestern Electric Power Company for Authority to Revise its Qualified Facility Non-Firm Power Purchase Schedule and Purchase Power Service Tariffs*

### Revenue Requirement Comparison

<b>Cost of Service</b>	<b>AE Proposed Test Year</b>	<b>NXP/Samsung Proposed Adjustments</b>	<b>NXP/Samsung Proposed Test Year</b>
Recoverable Fuel Cost	\$ 412,844,601	\$ (70,000,000)	\$ 342,844,601
Non-Recoverable Fuel Costs	37,959,112	-	37,959,112
Non-Fuel O&M	553,244,219	(43,504,610)	509,739,609
Total O&M	1,004,047,932	(113,504,610)	890,543,322
Taxes Other Than Income Taxes	1,407,353	-	1,407,353
Other Expense	9,035,408	(7,170,039)	1,865,369
Debt Service	102,653,421	-	102,653,421
Required Reserve Contribution	11,590,703	(11,590,703)	-
General Fund Transfer	105,000,000	-	105,000,000
Internally Generated Funds for Construction	88,341,454	(38,341,454)	50,000,000
Interest and Dividend Income	(4,633,152)	-	(4,633,152)
Contribution in Aid of Construction	(18,513,220)	-	(18,513,220)
Total Cost of Service	\$ 1,298,929,899	\$ (170,606,806)	\$ 1,128,323,093
Less Other Income	(81,702,588)	(14,479,686)	(96,182,274)
<b>Cost of Service</b>	<b>\$ 1,217,227,311</b>	<b>\$ (185,086,492)</b>	<b>\$ 1,032,140,819</b>

#### Debt Service Coverage

**2.77**

**2.28**

#### **AE Revenues at Present Rates**

Recoverable Fuel and Purchased Power	\$ 411,649,196	\$ (68,804,595)	\$ 342,844,601
Green Choice	22,772,679	-	22,772,679
Regulatory Charge	123,670,242	9,992,960	133,663,202
Community Benefit Charge	44,731,029	(11,203,154)	33,527,875
Base Rate Revenues	631,878,463	(132,546,001)	499,332,462
<b>Total Revenues</b>	<b>\$ 1,234,701,609</b>	<b>\$ (202,560,790)</b>	<b>\$ 1,032,140,819</b>
AE Base Rate Reduction/NXP/Samsung	\$ (17,474,298)		\$ (185,086,492)

### Recommended Adjustments

Description	Amount	Amount with Street Light Transfer
<b><u>AE Base Revenue</u></b>	\$ 631,878,463	\$ 631,878,463
Non- Nuclear Decommissioning	(19,442,308)	(19,442,308)
Transmission Revenue	(14,479,686)	(14,479,686)
Economic Development Transfer	(9,090,429)	(9,090,429)
Outside Services	(6,762,767)	(6,762,767)
Loss on Disposal of Assets	(7,170,039)	(7,170,039)
Rate Case Expense	(215,333)	(215,333)
Uncollectible Accounts	(7,591,813)	(7,591,813)
Customer Call Center	(10,371,210)	(10,371,210)
Capital Improvements Transfer	(38,341,454)	(38,341,454)
Reserves (Margin)	(11,590,703)	(11,590,703)
CBC and Reg Allocation Changes	2,441,632	2,441,632
AE Base Rate Reduction	(17,474,298)	(17,474,298)
NXP/Samsung Base Revenue	\$ 491,790,055	\$ 491,790,055
Transfer Street Lights to Base Rates		7,542,407
NXP/Samsung Base Revenue and SL		\$ 499,332,462
Difference	\$ (140,088,408)	\$ (132,546,001)

### Pass Through Adjustments

#### Fuel

Decrease test year fuel	\$ (70,000,000)	
Street Light Fuel Adjustment	1,195,405	
Net Adjustment		\$ (68,804,595)

#### Regulatory Charge

Increase to ERCOT Transmission Expense	\$ 9,969,250	
Goble Allocation Adjustments	23,710	
Net Regulatory Charge		\$ 9,992,960

#### Community Benefit Charge

Transfer Street Fuel to recoverable Fuel	\$ (1,195,405)	
Transfer Street Base Rates to New Street Light Class	(7,257,421)	
Goble Transfer Adjustments	(24,097)	
Goble Allocation Adjustments	(2,726,231)	
		\$ (11,203,154)

Total NXP/Samsung Revenue Requirement Reduction	\$ (202,560,790)
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