DOCKET NO. 3250

RE: APPLICATION OF TEXAS ELECTRIC SERVICE COMPANY FOR A RATE INCREASE	§	PUBLIC UTILITY COMMISSION OF TEXAS

DIRECT TESTIMONY OF

CATHERINE P. JONES

ACCOUNTING DIVISION

PUBLIC UTILITY COMMISSION OF TEXAS

JULY 1980

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DOCKET NO. 3250

RE: APPLICATION OF TEXAS ELECTRIC SERVICE COMPANY FOR A RATE INCREASE	§	PUBLIC UTILITY COMMISSION OF TEXAS

<u>DIRECT TESTIMONY OF CATHERINE P. JONES</u>

Q. Please state your name and business address.

A. Catherine P. Jones, 7800 Shoal Creek Boulevard, Austin, Texas 78757.

Q. By whom are you employed and in what position?

A. I am employed by the Public Utility Commission of Texas as a Chief Accountant III.

Q. Please describe your responsibilities.

A. My responsibilities include reviewing rate increase applications filed with the Commission and preparing testimony and exhibits for the rate hearings on those applications. In addition, I have reviewed Annual Reports filed with this Commission for compliance with our reporting requirements and assisted those utilities having problems with the interpretation of those requirements. I have also conducted special investigations as a result of complaints filed with the Commission.

Q. Please state your educational background, business experience, and professional qualifications.

A. I received a Bachelor of Business Administration degree with a major in accounting from the University of Texas at Austin. After graduation, I spent about two years with the independent accounting firm of Haskins & Sells in Houston, Texas as a member of the audit staff. While with Haskins & Sells, I attended a utility seminar with emphasis on ratemaking. In addition, I was in charge of the audit of a large gas utility client. In October 1976, I began my employment with the Public Utility Commission of Texas. In August 1977, I attended the Annual Regulatory Studies Program sponsored by the National Association of Regulatory Utility Commissioners in Michigan. I also attended the Ninth Annual Conference of the Institute of Public Utilities held in December, 1977 and several other utility oriented conferences. I am a Certified Public Accountant and a member of the American Institute of Certified Public Accountants and the Texas Society of Certified Public Accountants.

Q. Have you previously testified before this Commission?

A. Yes, I have.

Q. Ms. Jones, in connection with the present case before this Commission, Docket No. 3250, have you performed an examination and review of the Rate Filing Package and supporting information filed by Texas Electric Service Company and Subsidiary (TESCO or Company) in support of its request to increase and change rates amounting to $122,904,361 annually?

A. Yes, I have. In addition, I have reviewed the audit workpapers of the independent accountant for TESCO and its affiliated companies. I have also performed an on-site examination of the Company's books and records and the books and records of Texas Utilities Services, Inc. (TUSI), Texas Utilities Fuel Company

(TUFCO) and Texas Utilities Generating Company (TUGCO).

Q. What exactly will be the purpose of your testimony?

A. The purpose of my testimony will be to present the Staff's recommendations as to the test period cost of service for the year ended March 31, 1980 and its rate base and invested capital at March 31, 1980 derived as a result of my review and examination of TESCO's rate increase application.

Q. I have before me your Exhibit I, pages 1 through 10, and Exhibit II, pages 1 through 3. Were these exhibits prepared by you or under your supervision as a result of your review and examination mentioned previously?

A. Yes, they were.

Q. Regarding Exhibit I, would you please describe its arrangement and the manner in which it has been presented?

A. Page 1 of my Exhibit I presents TESCO's test period cost of service and related adjustments to increase this test period cost of service for the Company's claimed revenue deficiency as shown on Schedule A, page 1 of the Rate Filing Package, rearranged to conform to this Commission's definition of cost of service.

The amounts presented in Column (4) represent the additional revenue requirement claimed by the Company in the amount of \$122,904,361. Column (5) is TESCO's total claimed cost of service which when compared to the Company's computed test period operating base rate revenue indicates a needed base rate revenue increase of $157,771,422. This amount, when combined with the decrease in fuel revenues, results in the total requested increase of $122,904,361.

Q. When you discuss revenue requirements, are you referring to test period cost of service?

A. Yes. The Commission's Substantive Rules specifically define "cost of service" as that amount of revenue required to cover all reasonable and necessary costs incurred by the utility in rendering service to the public which includes a fair and reasonable return on the adjusted value of invested capital used and useful in providing service. In determining this cost of service upon which to base rates, one must look at a representative twelve-month period. The period selected must be thoroughly examined to determine that no non-recurring expenditures are included in the cost of service and that, if known and reasonably measurable changes have occurred, adjustments are made to reflect those changes.

The Company has proposed such adjustments and it is the differences in interpretation of "known and measurable" and "fair and reasonable return" that give rise to the Staff's adjustments presented in Column (6) of page 1 of my Exhibit I. These adjustments amounting to $88,339,880 are a result of the Staff's detailed analysis, examination and recomputations of data included in the Rate Filing Package, responses to requests for information of the Staff and intervenors and data obtained from the Company during the Staff's on-site examination.

Column (7) represents the Staff's "as adjusted" test period cost of service for TESCO for the twelve months ended March 31, 1980 amounting to $755,868,357. In addition, the revenues generated from sources other than base rate revenues and base rate revenues of $271,437,310 and $414,999,505, respectively, are presented in order to arrive at the Staff recommended base rate revenue deficiency of $69,431,542.

Q. What is presented in the remaining pages of your Exhibit I?

A. The remaining pages show the detailed computations of the Staff's adjustments presented in Column (6) of page 1.

Q. Would you explain your adjustment to fuel as reflected on page 2 of Exhibit I?

A. I have made adjustments to fuel expense using the Company's methodology. TESCO's adjustment consisted of four components. The first part of the adjustment was to reflect the replacement of the gas from the Old Ocean fuel contract with the higher priced TUFCO gas. The second component was to restate other fuel sources at year-end prices. The third and fourth parts of the adjustment reflected the effect of Kwh sales on fuel costs.

For purposes of my computation, I have combined the restatement of fuel due to the expiration of the Old Ocean contract and year-end price levels. As shown on page 3 of my Exhibit I, I have adjusted the year-end price level for lignite fuel. The Company used the weighted average lignite price for the month of March

1980 in their computation. The use of this price would be proper if the costs and operations at all the lignite plants in March were representative. In my opinion, March 1980 was not a representative month of operations. The capacity factors for the lignite units for the test year were approximately of 63.7 percent at Big Brown (BBSES), 60.8 percent at Monticello (MOSES), and 66 percent of Martin Lake (MLSES). During March, the capacity factors were 48.8 percent, 76 percent, 50 percent, respectively. By using a weighted average cost for March 1980, a greater weighting is given to MOSES (76 percent). Big Brown was given the least weighting and has the lowest priced fuel. I recomputed the weighted average cost of lignite using the total test year mmBtus at the respective plants at the average cost for March, April, and May 1980. Based on a review of the lignite costs for the year and the two subsequent months, the average of these months is more representative than March. The resulting lignite price is 70.95 cents per mmBtu compared with the 72 cents used by the Company.

Q. What other adjustments have you made to fuel expense?

A. I have reclassified $215,855 from operations and maintenance expenses as shown on page 2. In February and March 1980 these expenses were improperly charged to power operations by TUGCO. These amounts were reclassified to fuel expense in April and May 1980. As a result, test year operations and maintenance expenses were overstated and fuel expense was understated. I have also removed social club dues allocated from TUFCO and TUGCO. The Commission's Substantive Rules disallows inclusion of such dues in the cost of service whether directly incurred by the utility or included within billings from affiliates.

My two remaining adjustments to fuel expense are detailed on page 3. I have recomputed the effect of a change in Kwh sales on fuel expense. Mr. Ted Vogel of the Economic Research Division will testify to the Kwh sales changes.

Q. Are these two adjustments similiar to those made by the Company?

A. Yes. The only differences are Kwh sales and the heat rate used to compute the reduction in mmBtus. I have used the test year average heat rate at the gas plants which burn TUFCO gas. This heat rate is consistent with the use of the TUFCO gas price to determine the dollar impact on fuel expense. The Company used the average heat rate for all units, including lignite, which is inconsistent with the pricing.

Q. Page 4 of Exhibit I presents the Staff adjustments to operation and maintenance expenses. Would you explain these adjustments?

A. I have made an adjustment to payroll expense. The Company has proposed an adjustment to increase payroll expenses by $6,511,238 to recognize both the number of employees at March 31, 1980 and wage rates which will be in effect in October 1980. The Staff has reviewed the Company's computation and agrees with their methodology. However, the Company inadvertently included in their computation the wages of several employees added to the payroll subsequent to March 31, 1980. The Staff recomputed the payroll adjustment excluding the employees added after the test year. The result of the recomputation is to reduce the proposed payroll adjustment by $29,904. I have also adjusted payroll related costs to reflect the effect of the adjustment to payroll expense.

Q. Referring to page 6, please explain your adjustment to payroll expense at the Monticello plant.

A. The lignite plants are operated by TUGCO using TUGCO employees. The Company adjusted TUGCO payroll expense using the last pay period in March 1980 to develop a percentage increase of the year ended base salaries over the average year base salaries. I have also used this methodology in computing my adjustment to the Monticello (MOSES) payroll. In developing the percentage increase, I included salaries for the administrative and supervisory and accounting and technical employees located at the mining facility in Hopkins County. The inclusion of these salaries had a minimal impact on my adjustment. The majority of my adjustment is the result of a difference in the allocation of this payroll expense to TESCO.

TESCO owns an average of 37.895 percent of all three units at MOSES. All costs are allocated to TESCO on this basis with the exception of special projects and fuel. These expenses are allocated using the ownership percentage in the individual units. The Company allocated the increased total payroll using

37.895 percent. In computing the actual test year payroll to TESCO of $3,674,290 the Company used the percentage of cost charged to TESCO to the total costs for the test year of all three units. This resulting percentage of 36.89 reflects the impact of the allocation of special projects. The Company, in using this percentage, understated test year actual payroll allocated to TESCO and overstated the necessary adjustment to expense. I have used the ownership percentage of 37.895 to arrive at my adjustment to MOSES payroll of $554,901 which is $111,874 less than the adjustment proposed by the Company.

Q. Have you made any other adjustments on page 4 which relate to allocations from TUGCO?

A. Yes. My next adjustment on page 4 is the reclassification of fuel expenses improperly charged to operation and maintenance expenses during the test year. This reclassification was discussed previously.

I have also removed social club dues from TUGCO which I will discuss later in my testimony.

Q. Please explain the remaining adjustments on page 4.

A. The Company has proposed an adjustment to increase postal expense to reflect the year end level of customers and an anticipated postal rate increase. While the increase in postal expense due to an increase in customers represents a known and measurable change, the proposed postal rate increase is neither known nor measurable at this time. The process of raising postal rates is similar to the process a utility must go through to raise its rates. The process lasts about ten months and involves a hearing with intervenors. The likelihood that the requested rates will be those that are granted cannot be measured. Because of the uncertainty of the ultimate level and effective date of the postal increase, the Staff has eliminated the portion of the adjustment that relates to the postal rate increase.

The next adjustment on page 4 relates to the first year estimated cost of the Residential Conservation Service Program. The Residential Conservation Service Program (RCSP) was initiated as a result of the National Energy Conservation Policy Act (NECPA) of 1978. The general purpose of the RCSP is to reduce the residential consumption of energy by providing conservation information to each residential customer and conducting, at the request of the customer, an on-site inspection of the customer's residence for the purpose of advising the customer of estimated energy savings if he were to implement recommended energy conservation measures for his residence. TESCO will be offering these energy audits to their residential customers in 1981.

The Company has proposed an adjustment of $675,000 to cover the costs of the program announcement, the offering of the audit, and the hiring of auditors. The Company based its adjustment for the RCSP on the assumption that the program announcement would cost 10¢ per customer plus postage, that the offering of the audit would cost 5¢ per customer contacted plus postage, and that with a 5% response rate, 20 additional employees would be required to perform the 19,992 estimated annual audits. While an adjustment to recognize the costs of the RCSP is necessary, the Staff does not completely agree with the cost estimates the Company has utilized in computing the adjustment. From information obtained from the Texas Energy and Natural Resources Advisory Council (TENRAC) and Paul Smolen, the Commission representative to the State advisory committee, the Staff has recomputed the adjustment for the RCSP on page 7. The Staff utilized the most recent available cost estimates in computing the adjustment. I have estimated that the program announcement will cost 5¢ per residential customer with no postal expense required. The offering of the audit is estimated to cost 15¢ per residential customer contacted plus 15¢ postage. The response rate is estimated to be 3% of the residential customers who are actually offered the audit. These differences result in a substantial decrease in the estimated costs of the RCSP, the majority of which is attributable to the auditors' wages. TESCO, in assuming a 5% response rate of all residential customers contacted, estimated it would require 45 auditors to perform the anticipated audits. Of the 45 auditors required, 25 would be employees currently on the payroll and 20 additional employees would be required. At the 3% response rate, the Staff has estimated that 6,585 audits will be performed each year and that only 15 auditors will be required thereby eliminating the need for additional employees. The

Staff is recommending $87,800 for the estimated cost of the first year of the RCSP rather than the $675,000 requested by the Company.

Q. Your next adjustment is to the provision for insurance and casualties. What does this provision represent?

A. This is an accrual made to expenses for which there is no current cash out flow. The accrual is necessary because of the difficulty in obtaining insurance for catastrophic losses such as boiler explosions, wind storm damage and fire without a significant amount being designated as deductible from coverage. In some cases, the deductible can be as high as two million dollars. Even if a Company could obtain coverage with a lower deductible, the premium costs could be prohibitive. By allowing the Company to accrue for losses over an extended period of time, the impact on the ratepayer or the stockholder is reduced. In addition, it allows the management of a Company to apply its expertise in risk management and thereby seek the most economic type of coverage to the benefit of the ratepayer. The Commission has recognized this need and allowed this Company to accrue for such losses in previous cases.

The history of losses experienced by TESCO in recent years justifies the continued need for such accrual. However, because the level of the provision is at the discretion of management, it needs to be closely evaluated.

TESCO has requested to increase the provision to $1,740,000.

This provision is based on the need to achieve a target reserve balance of $5,000,000 in three years. Also included in the computation is the anticipated cost to be incurred over the next two years related to a rotor repair at the Eagle Mountain plant. I do not agree with the method used by TESCO in determining the requested provision. By including the anticipated cost of the rotor repair, TESCO is requesting recovery of this loss over a three year period. In my opinion, this anticipated cost should not have any effect on the current provision. I have recomputed the needed provision using the Company's methodology excluding the cost of the Eagle Mountain repair. Based on this computation, the provision granted in Docket #2606, $1,320,000, is a reasonable level to be included in the cost of service.

Q. Are you recommending the amortization of the cost of the Eagle Mountain repair over a future period?

A. No. An alternative to the insurance reserve provision is the amortization over a future time period after the loss has occurred. The Staff has rejected this alternative in previous cases and I feel the reserve is the preferable method. The effects of the Eagle Mountain loss would need to be considered only if the reserve was insufficient. To consider this loss in the current provision defeats the purpose of the reserve set out previously in my testimony.

Q. Will your recommended provision achieve a $5,000,000 reserve by 1982?

A. No. In 1982 the reserve balance will be approximately $3,700,000 after considering the anticipated costs of the rotor repair. The $5,000,000 reserve will be reached in the next year, 1983, if no further losses occur.

Q. Has 1982 always been the target date set by the Company?

A. No. In each of the previous cases, Docket #1903 and Docket #2606, the date has changed. In Docket #1903, it was 1980; in Docket #2606, 1981. Although these date changes are the apparent result of building the reserve over three years, I have seen no justification or support for the three year period.

Q. Please continue explaining the adjustments shown on page 4.

A. The next adjustment is to other operation and maintenance expenses. I have adjusted the Company's adjustment to the level recommended by Mr. Vogel of the Economic Research Division. I have removed contributions and dues which are specifically disallowed by this Commission. These expenditures include contributions to the United Methodist Women, Blundell Creek Baptist Church, Antioch Missionary Baptist Church, Ministerial Alliances of Greater Fort Worth, Church of God in Christ, County Judges and Commissioners Association of Texas and Southwestern Baptist Theological Seminary, which are expenditures in support of religious and political causes. Additional expenditures include contributions to Rotary Clubs, Jaycees, Lions Clubs, Kiwanis Clubs, and Optimist Clubs, which are expentitures in support of or membership in social and fraternal organizations. I have also excluded social club dues allocated to TESCO from TUGCO and TUSI in the monthly billings for power operations and services provided, respectively.

I have recomputed uncollectibles using the Staff recommended cost of service. Uncollectibles vary in relation to revenues as do other expense items. One of these is the Public Utility Commission (PUC) assessment. I have reclassified the Public Utility Commission assessment to Taxes Other Than Income for this computation. This reclassification was based on the opinion of the General Counsel's division that this assessment is a tax.

Q. Page 8 details your adjustment of $1,068,985 to Taxes Other Than Income. Please explain these adjustments.

A. All of my adjustments are recomputations of revenue related taxes using the Staff recommended cost of service. In computing these taxes, the Staff has used rates which are slightly different from those proposed by the Company. In computing the adjustment to street rental and State gross receipts taxes, the Company attempted to compute a rate which properly matches the revenue with the corresponding tax expense. The Company compared test year revenue related taxes to calendar year 1979 revenues excluding intersystem sales. The Staff agrees that a proper matching occurs when test year tax expenses are utilized in conjunction with 1979 revenues. However, the Staff used total 1979 revenues to compute the tax rates for street rental and

State gross receipts taxes. Total test year revenues were used to compute the rate for the PUC assessment. These recomputations were necessary as the rates were applied to total cost of service.

Q. Ms. Jones, your computation of Federal income taxes as shown on your Exhibit I, page 9 starts with the return dollars as determined by the Staff. Would you explain your approach as presented on this Exhibit?

A. It is my opinion that the method that should be used pursuant to sound ratemaking practices for computing test period income taxes is to determine such taxes as a derivation of the test period return amount. The test period return amount is the amount of dollars which will allow the Company to recoup its debt and preferred stock capital costs and provide a fair return to its equity holders. This return to equity holders is an after income tax amount. Therefore, it is necessary to start with the return dollars less amounts for debt interest plus any other items on which deferred taxes have not been previously provided or which are direct offsets to taxes payable. The resulting taxable income after income taxes of $104,946,209 must then be grossed up to arrive at net taxable income before income taxes. This number, multiplied by the Federal income tax rate of 46 percent less tax credits and the consolidated tax savings, provides the actual test period income taxes. My computation results in a $32,281,180 reduction of the Company's claimed test period Federal income taxes.

Q. The Company has requested that their cost of service include full normalization of timing differences. Does your computation of Federal income taxes take this into consideration?

A. Yes. Because my computation starts with the return amount after income taxes, the tax timing differences that are normalized (i.e., accelerated depreciation, capitalized taxes, pension and thrift plan costs,) have no effect on my total tax calculation. Those tax liabilities are either current or deferred, but remain the same in total. Only those non-normalized tax differences, such as taxes and other costs capitalized and those previously flowed through to the ratepayer, need to be taken into consideration. Book depreciation now includes these certain costs that are no longer deductible for tax purposes.

This increases the Company's actual tax liability (present and future) above the amount that would have been determined if a flat 46 percent were applied to income before Federal income taxes. For this reason, I have added back depreciation in the amount of $3,938,930 which represents depreciation on these differences in the basis for tax depreciation versus book depreciation.

Q. The amount that you have deducted for interest in your tax calculation differs from that shown on Schedule H-1 of the Rate Filing Package, does it not?

A. Yes, it does. In determining my interest amount, I have taken the weighted average interest cost in percent, as presented by Mr. Child, and applied it to the Staff "as adjusted" invested capital. The purpose of this calculation is to allocate to the invested capital only that portion of the total interest costs that would reduce operating income before taxes and accordingly have an effect on the amount of Federal income taxes included in the cost of service. This treatment recognizes that the additional interest cost will act as deductions against any non-operating income that may arise "below the line" or from non-utility operations.

Q. Have you made any other adjustments in arriving at your test period Federal income taxes?

A. Yes, I have recomputed the Company's amortization of deferred investment tax credits. Prior to 1977, the investment tax credits generated by TUFCO and TUGCO were allocated to the operating companies and carried on their books. Consistent with the change to straight line depreciation by TUFCO and TUGCO it is necessary to adjust the ratable amortization of these investment tax credits. My resulting amortization of deferred investment tax credits is $2,273,480.

Q. How did you calculate the Staff's return amount?

A. Using the weighted average capital cost of TESCO at March 31, 1980, as presented by Mr. Child, on the Staff's "as adjusted" original cost of invested capital shown on page 2 of my Exhibit II, I have recomputed a fair and reasonable return on the adjusted value of invested capital of $155,405,463.

Q. Have you reviewed the Company's proposed adjusted value of invested capital at March 31, 1980?

A. Yes. Page 1 of my Exhibit II presents the recommended adjusted value of invested capital pursuant to this review.

Q. Would you briefly explain page 1 of your Exhibit II?

A. This Exhibit presents the major components of the proposed adjusted value of invested capital of $1,683,081,418 at March 31, 1980. I have used the mix percentages presented by Mr. Child in his testimony and the current cost of plant in service, net of adjustment for age and condition, proposed by Mr. Saathoff in his testimony. Original cost of net plant and other elements of invested capital are shown on pages 2 through 3 of my Exhibit II.

Q. On page 3, a Staff adjustment to the Company's end of period accumulated provision for depreciation was made. Would you explain the nature of this adjustment and its effect on the net original cost of plant in service?

A. The Company has increased its test year depreciation expense by $516,868. This adjustment reflects the increase in depreciable plant at March 31, 1980 over depreciable plant in service during the test year. By making this adjustment, the Company has attempted to reflect a cost of service consistent with the balance of year-end net plant in service. However, to be completely consistent, there should be a corresponding increase in the end-of-period accumulated provision for depreciation. My adjustment to increase the accumulated provision for depreciation, and thereby decrease net original cost of plant, recognizes that there will be continued diminution in plant investment through the recovery of this investment via the depreciation provision. Therefore, in order to reflect a representative test period for prospective ratesetting, I have increased the accumulated provision for depreciation by one-half of the adjustment, \$258,434.

Q. The Company has proposed to include all construction work in progress (CWIP) in the rate base. The Staff, however, does not agree with the inclusion of 100% of CWIP. Would you explain the reason for this?

A. The inclusion of CWIP within the invested capital of the Company is, by law, dependent on the maintaining of that Company's "financial integrity." Within my analysis, I asked Mr. Child to provide me with certain financial indicators and the levels which, in his professional opinion, would have to be attained by TESCO for it to maintain its "financial integrity." These indicators were the interest coverages excluding and including allowance for funds used during construction (AFUDC) before taxes, the percentage of internal cash generation and the percentage of income available for common generated from AFUDC. Mr. Child reviewed the results of the inclusion of various levels of CWIP on the financial indicators and selected the level which, in his opinion, provided the most satisfactory results. The level of CWIP chosen represents fifty percent of CWIP, or $269,039,980, as shown on page 3.

Q. Why have you adjusted the Company's amount for electric plant held for future use?

A. There are many factors to be considered in analyzing plant held for future use. Most of these are difficult to quantify and represent reasons other Commissions have decided to disallow plant held for future use entirely. In certain instances, a company might not even be able to find a substation site in a rapidly growing area if the site had not been purchased in prior years. This factor may cause some utilities to gamble on the growth in certain areas by purchasing sites ahead of time. If the projected growth does not take place as anticipated, ratepayers have paid the carrying cost of property that may be delayed in use for many years or cancelled altogether. This is a risk that should be borne by the ratepayers only when it can be shown that the Company has a definite plan for the property's use within a reasonable time period. I have excluded the Titus County Water Rights as there is no specific plan to use these prior to 1990. In my opinion, inclusion of property which will not be placed in service for ten or more years places an unreasonable burden on the ratepayers.

Q. You have adjusted working capital downward by $14,352,628. Could you please discuss this adjustment?

A. Page 3 of Exhibit II shows the detailed amounts of working capital allowed by the Staff. I have agreed with the Company concerning the requirements for materials and supplies, working funds and fuel gas inventories. I do not, however, agree with the Company's proposal for prepayments, fuel oil inventories, and working cash.

The Company as proposed to include in invested capital an average of prepayments. In March 1979, the Company prepaid approximately $744,000 in retirement plan costs. This prepayment was also included in April 1979. In the usual course of business, the Company does not prepay these costs. In determining a reasonable level of prepayments to include in working capital, I have eliminated this amount and recalculated the average of the remaining prepayments. I have allowed the year end level of fuel oil inventory as recommended by Mr. Saathoff of the Engineering Division.

I have recomputed the working cash allowance requested by the Company using the Company's methodology and Staff adjusted operation and maintenance expenses excluding fuel expense.

A. Would you please explain your adjustment for Other Cost-Free Capital?

A. Yes. The Company changed its method of calculating depletion for tax purposes in 1977. However, the method used to calculate the depletion allowance for book purposes did not change. Because the method used for tax purposes resulted in a greater deduction for depletion than that reflected on TESCO's books, the Company has had the use of additional dollars at no cost. I have also removed the 1979 and first quarter of 1980 contribution to the Edison Electric Institute. These contributions are for the delayed Liquid Breeder Reactor project and are not payable until 1982 at the earliest.

Q. Ms. Jones, would you please summarize your conclusion pertaining to Texas Electric Service Company's claimed test period cost of service and revenues?

A. I am recommending a reduction in the Company's claimed test period cost of service of $60,428,656 which results in a fair and reasonable test period cost of service of $755,868,357. After excluding revenues from sources other than base rates, there remains a base rate revenue deficiency of $69,431,542.

Q. What do the revenues from other sources represent?

A. As shown on page 10 of Exhibit I, the $271,437,310 that I have deducted from cost of service is comprised of two major sources. One source is miscellaneous operating revenues as detailed on Schedule N-4 of the Rate Filing Package adjusted for the estimated number of audits that will be conducted as part of the RCSP discussed previously. The other represents fuel adjustment clause revenues in the amount of $267,060,659.

Q. Why have you adjusted test period base rate revenues?

A. The Company computed test period base rate revenues using the adjusted Kwh sales for customers, weather, and elasticity. Conrates, it is necessary to recompute test period base rate revenues in determining the deficiency.

Q. Is there anything else you wish to discuss?

A. Yes. During the course of my review, two items came to my attention which do not affect this case, but will affect subsequent cases. The first item involves the Company's investment in some of their lignite leases. The Company entered into an option in February to sell some of their lignite leases to a third party. These leases were transferred from plant held for future use to non-utility plant in March 1980. If this option is exercised, the sale will take place later this summer. Due to the accounting complexities of recording this transaction and the resulting ratemaking treatment of the gain on the sale, I recommend the Company be ordered to file an application for sale with the Commission and allow the Staff to review the accounting treatment at the time of sale.

The second item relates to social club dues charged to TESCO by affiliates. Included in the cost of the Commanche Peak project are social club dues. Although these costs are minor, I would recommend TESCO identify and remove the total amount along with the related AFUDC from Account 107.

Q. Does this conclude your testimony?

A. Yes, it does.

PUBLIC UTILITY COMMISSION OF TEXAS

TEXAS ELECTRIC SERVICE COMPANY AND SUBSIDIARY
COST OF SERVICE

TWELVE MONTHS ENDED MARCH 31,1980

Line No.	Description (1)	Exhibit Reference (2)	Company: Test Period Amount (a) (3)	Company: Claimed Income Deficiency (4)	Company: Total (a) (5)	Staff: Adjustments (6)	Staff: As Adjusted (7)
1	Fuel	I(Jones) p. 2	$ 275,730,493	$ (35,302,290)	$ 240,428,203	$ 26,632,456	$ 267,060,659
2	Operations and Maintenance	I(Jones) p. 4	151,463,486	651,393	152,114,879	(6,082,912)	146,031,967
3	Depreciation		50,986,049		50,986,049		50,986,049
4	Taxes Other Than Income	I(Jones) p. 8	46,268,793	4,243,888	50,512,681	(1,068,985)	49,443,696
5	Federal Income Taxes	I(Jones) p. 9	48,415,637	70,523,230	118,938,867	(32,281,180)	86,657,687
6	Interest on Customers' Deposits		282,836		282,836		282,836
7	Return	II(Jones) p. 1	120,245,358	82,788,140	203,033,498	(47,628,035)	155,405,463
8	Total Cost of Service		$ 693,392,652	$ 122,904,361	$ 816,297,013	$(60,428,656)	$ 755,868,357
9	Fuel and Other Revenues	I(Jones) p. 10	(279,805,985)	34,866,061	(244,938,924)	(26,498,386)	(271,437,310)
10	Base Rate Revenue		$ 413,586,667	$ 157,771,422	$ 571,358,089	$(86,927,042)	$ 484,431,047
11	Test Period Base Rate Revenue				(413,586,667)	(4,412,838)	(414,999,505)(b)
12	Base Rate Revenue Deficiency (Excess)				$ 147,771,422 $ 157,771,422	$(88,339,880)	$ 69,431,542

(a) Schedule A, page 1 (Rate Filing Package).
(b) Obtained from Ted Vogel, Economic Research Division

PUBLIC UTILITY COMMISSION OF TEXAS

TEXAS ELECTRIC SERVICE COMPANY AND SUBSIDIARY

FUEL EXPENSE

TWELVE MONTHS ENDED MARCH 31, 1980

Description	Amount
Consolidated fuel expense	$155,402,321 (a)
Fuel component of purchased power	5,138,793 (a)
Adjustments to reflect price changes	123,136,930 (b)
Reclassification from operation and maintenance	215,855 (c)
Removal of social club dues	(830)(d)
Less:	
Fuel component of intersystem sales	(5,754,234)(a)
Exploration and development	(102,150)(a)
Transportation and storage	(263,544)(a)
Adjusted recoverable fuel costs for test year sales	$277,773,141
Adjustment to reflect Kwh sales adjusted for customers, weather, and price elasticity	(235,256)(b)
Recoverable fuel costs for test year at present rates	$277,537,885
Adjustment to reflect Kwh sales adjusted for price elasticity at proposed rates	(10,477,226)(b)
Fuel - Staff	$267,060,659
Fuel - Company	(240,428,203)(a)
Staff adjustment	$ 26,632,456

(a) Schedule A, page 34 (Rate Filing Package) and Company response to Commission request C-1.
(b) Exhibit I (Jones) page 3.
(c) Exhibit I (Jones) page 4.
(d) Determined from review of books and records of TUFCO and TUGCO.

PUBLIC UTILITY COMMISSION OF TEXAS

TEXAS ELECTRIC SERVICE COMPANY AND SUBSIDIARY

FUEL EXPENSE

TWELVE MONTHS ENDED MARCH 31, 1980

Description			Amount
Adjustment to reflect price changes			
Lignite consumed (mmBtu)		108,532,714 (a)	
Lignite price - Staff	$.7095 (c)		
Lignite price - Company	(.7200)(a)	X (.0105)	
Adjustment due to lignite price		$ (1,139,593)	
Adjustment for price changes-Company		124,276,523 (b)	$123,136,930
Adjustment to reflect Kwh sales for customers, weather and price elasticity			
Staff adjustment to test year Kwh sales		(10,164,869)(d)	
Heat rate		X 11127 (e)	
Reduction in mmBtus		(113,104)	
Price		X $2.08 (b)	$ (235,256)
Adjustment to reflect Kwh sales for price elasticity at proposed rates			
Staff adjustment to Kwh sales		(452,694,125)(d)	
Heat rate		X 11127 (e)	
Reduction in mmBtus		(5,037,128)	
Price		X $2.08 (b)	$(10,477,226)

(a) Company's response to Commission request C-1.
(b) Schedule A, page 34 (Rate Filing Package).
(c) Computed from Company response to Commission request C-1 and informal request for information.
(d) Ted Vogel, Economic Research Division.
(e) Computed from power reports for gas fired units contained in March, 1980 Financial and Operating Report.

PUBLIC UTILITY COMMISSION OF TEXAS

TEXAS ELECTRIC SE../ICE COMPANY AND SUBSIDIARY
OPERATION AND MAINTENANCE EXPENSES
STAFF ADJUSTMENTS

TWELVE MONTHS ENDED MARCH 31, 1980

Description		Adjustment
Payroll		
Staff payroll adjustment	$ 6,481,334 (b)	
Company payroll adjustment	(6,511,238)(a)	$ (29,904)
Payroll Related Costs		
Staff adjustment to payroll	$ (29,904)	
Percent payroll related costs	X 15.905%(a)	(4,756)
Payroll Changes at Monticello		
Staff payroll adjustment	554,901 (c)	
Company payroll adjustment	(666,775)(a)	(111,874)
Reclassification		
Reclassification to fuel expense		(215,855) (d)
Postage Expense		
Staff postage expense adjustment	$ 23,631 (e)	
Company postage expense adjustment	(292,874)(a)	(269,243)
Residential Conservation Service Program		
Staff amount	$ 87,800 (f)	
Company amount	(675,000)(a)	(587,200)
Provision for Insurance		
Staff amount	$ 1,320,000 (g)	
Company amount	(1,740,000)(a)	(420,000)
Other Operation and Maintenance		
Staff adjustment	$ 1,519,350 (h)	
Company adjustment	(4,407,655)(a)	(2,888,305)
Disallowed Expenses		
Elimination of dues and contributions in accordance with Substantive Rule 052.02.03.032		(16,536) (i)
Uncollectibles		
Staff cost of service	$755,868,357 (j)	
Rate	X .0036156 (k)	
Staff uncollectibles	$ 2,732,916	
Company uncollectibles	(2,982,449)(a)	(249,531)
Public Utility Commission Assessment		
Reclassification to Taxes Other Than Income		(1,289,708) (a)
Total staff adjustments		$(6,082,912)

See Exhibit I (Jones) page 5 for Footnote explanations.

PUBLIC UTILITY COMMISSION OF TEXAS

TEXAS ELECTRIC SERVICE COMPANY AND SUBSIDIARY

OPERATION AND MAINTENANCE EXPENSES

FOOTNOTES

(a) Schedule A (Rate Filing Package).

(b) Determined from information obtained in review of books and records and Company response to Commission request C-1.

(c) Exhibit I (Jones) page 6.

(d) Determined from on-site review of books and records of TUGCO.

(e) Computed using Company response to Commission request C-1 and Schedule N-3 (Rate Filing Package).

(f) Exhibit I (Jones) page 7.

(g) Docket No. 2606 final order.

(h) Testimony of Ted Vogel, Economic Research Division.

(i) Determined from Company response to Commission request C-20 and on-site review of books and records.

(j) Exhibit I (Jones) page 1.

(k) Computed using Company response to Commission request C-1.

PUBLIC UTILITY COMMISSION OF TEXAS

TEXAS ELECTRIC SERVICE COMPANY AND SUBSIDIARY
PAYROLL EXPENSE AT MONTICELLO SES
STAFF ADJUSTMENT

TWELVE MONTHS ENDED MARCH 31, 1980

Description	Amount
Annualized base salaries	$8,957,270 (a)
Actual test year base salaries	(7,808,976)(a)
Increase in base salaries	$1,148,294
Percent increase	14.7%
Total payroll to operation and maintenance expense	X 9,961,312 (b)
Increase in total payroll	$1,464,313
Percent to TESCO	X 37.895%(b)
Adjustment to MOSES payroll - Staff	$ 554,901

(a) Computed using Company response to Commission request C-1 and response to informal request.
(b) Schedule A, page 7 (Rate Filing Package).

PUBLIC UTILITY COMMISSION OF TEXAS

TEXAS ELECTRIC SERVICE COMPANY AND SUBSIDIARY
RESIDENTIAL CONSERVATION SERVICE PROGRAM
STAFF ADJUSTMENT

TWELVE MONTHS ENDED MARCH 31, 1980

Description		Amount
Program Announcement		
End of test year residential customers	438,994 (a)	
Printing cost per customer	X $.05 (b)	
		$21,950
Offering of Audit		
Residential customers offered the audit each year	219,497 (c)	
Printing and postal cost per customer	X $.30 (b)	
		65,850
Adjustment for Residential Conservation Service Program - Staff		$87,800

(a) Schedule N-3 (Rate Filing Package).
(b) Computed using information obtained from Texas Energy and Natural Resource Advisory Council.
(c) Computed as one-half of year end customers per Schedule N-3 (Rate Filing Package).

PUBLIC UTILITY COMMISSION OF TEXAS

TEXAS ELECTRIC SERVICE COMPANY AND SUBSIDIARY
TAXES OTHER THAN INCOME
STAFF ADJUSTMENT

TWELVE MONTHS ENDED MARCH 31, 1980

Description		Staff Adjustment
Public Utility Commission Assessment		
Cost of service - Staff	$755,868,357 (a)	
Rate	X .001573 (b)	
PUC assessment - Staff	$ 1,188,973	
PUC assessment - Company	-0-	$1,188,973
Street Rental taxes		
Cost of service - Staff	$755,868,357 (a)	
Rate	X .020968 (d)	
Street rental taxes - Staff	$ 15,849,047	
Street rental taxes - Company	(17,249,850)(c)	(1,400,803)
State Gross Receipts Taxes		
Cost of service - Staff	$755,868,357 (a)	
Rate	X .012868 (d)	
Gross receipts taxes - Staff	$ 9,726,514	
Gross receipts taxes - Company	(10,583,669)(c)	(857,155)
Total Staff adjustment		$(1,068,985)

(a) Exhibit I (Jones) page 1.
(b) Computed using Company response to Commission request C-1.
(c) Schedule I.8 and A (Rate Filing Package).
(d) Computed using Company response to Commmission request C-1 and December, 1979 Financial and Operating Report.

PUBLIC UTILITY COMMISSION OF TEXAS

TEXAS ELECTRIC SERVICE COMPANY AND SUBSIDIARY
FEDERAL INCOME TAXES

TWELVE MONTHS ENDED MARCH 31, 1980

Description		Amount	
Return per Exhibit II (Jones) page 1		$155,405,463	
Interest		(47,822,349)	(a)
Non-normalized timing differences and other credits:			
Amortization of investment tax credit	$(2,273,480)		
Depreciation	3,938,930		
Consolidated tax savings	(461,457)		
Other	(3,840,898)	(2,636,905)	
Taxable income after income taxes		$104,946,209	
Factor for Federal income taxes before amortization of tax credits and other		X .851851852	
Federal income taxes before amortization of tax credits and other		$ 89,398,622	
Amortization of investment tax credits		(2,273,480)	(c)
Consolidated tax savings and surtax exemption		(467,455)	(b)
Staff Federal income taxes		$ 86,657,687	
Company Federal income taxes		(118,938,867)	(b)
Staff adjustment		$(32,281,180)	

(a) Weighted average cost of debt applied to Staff invested capital.
(b) Schedule A (Rate Filing Package).
(c) Recomputed using response to Commission request C-1 and Docket 2606 workpapers.

PUBLIC UTILITY COMMISSION OF TEXAS

TEXAS ELECTRIC SERVICE COMPANY AND SUBSIDIARY
FUEL AND OTHER REVENUES

TWELVE MONTHS ENDED MARCH 31, 1980

	Company			Staff	
Description	Test Period Amount (a)	Adjustments	Total (a)	Adjustments	As Adjusted
Recoverable Fuel Costs	$275,730,493	$(35,302,290)	$240,428,203	$26,632,456	$267,060,659 (c)
Other Revenues	4,075,492	435,229	4,510,721	(134,070)(b)	4,376,651
Total	$279,805,985	$(34,867,061)	$244,938,924	$26,498,386	$271,437,310

(a) Schedule N-2 (Rate Filing Package).
(b) Computed using Staff adjustment to residential conservation program and Schedule N-4 (Rate Filing Package).
(c) Exhibit I (Jones) page 1.

PUBLIC UTILITY COMMISSION OF TEXAS

TEXAS ELECTRIC SERVICE COMPANY AND SUBSIDIARY
ADJUSTED VALUE OF INVESTED CAPITAL AND RETURN

TWELVE MONTHS ENDED MARCH 31, 1980

Description	Exhibit Reference	Mix Computation	Amount
Net Plant - Original Cost Percentage Mix	II (Jones) p.2 Child	\$1,100,955,464 X 63.875%	\$ 703,235,303
Net Plant Current Cost Percentage Mix	Saathoff Child	\$1,957,068,261 X 36.125%	706,990,909
Construction Work in Progress	II (Jones) p.2		269,039,980
Plant Held for Future Use	II (Jones) p.2		3,694,185
Nuclear Fuel in Process	II (Jones) p.2		25,581,796
Working Capital	II (Jones) p.2		57,196,106
Customer's Deposits	II (Jones) p.2		(3,920,772)
Accumulated Deferred Federal Income Taxes	II (Jones) p.2		(69,758,408)
Reserve for Insurance and Casualties	II (Jones) p.2		(1,802,321)
Other Cost Free Capital	II (Jones) p.2		(7,175,360)
Adjusted Value of Invested Capital			\$1,683,081,418
Return @ 9.23%			\$ 155,405,463 (a)

(a) Exhibit II (Jones) page 2.

PUBLIC UTILITY COMMISSION OF TEXAS

TEXAS ELECTRIC SERVICE COMPANY AND SUBSIDIARY
INVESTED CAPITAL AND RETURN

TWELVE MONTHS ENDED MARCH 31, 1980

Description	Exhibit Reference	Company Amount (a)	Staff Adjustments	Staff As Adjusted
Original Cost of Plant in Service		$1,483,200,358		$1,483,200,358
Accumulated Depreciation	II (Jones) p.3	(381,986,460)	$ (258,434)	(382,244,894)
Net Plant in Service		$1,101,213,898	$ (258,434)	$1,100,955,464
Construction Work in Progress	II (Jones) p.3	538,079,959	(269,039,979)	269,039,980
Electric Plant Held for Future Use	II (Jones) p.3	3,948,445	(254,260)	3,694,185
Nuclear Fuel in Process		25,581,796		25,581,796
Working Capital	II (Jones) p.3	71,548,734	(14,352,628)	57,196,106
Customers' Deposits		(3,920,772)		(3,920,772)
Accumulated Deferred Federal Income Taxes		(69,758,408)		(69,758,408)
Reserve for Insurance and Casualties	II (Jones) p.3	(1,802,321)		(1,802,321)
Other Cost Free Capital	II (Jones) p.3		(7,175,360)	(7,175,360)
Total Invested Capital		$1,664,891,331	$(291,080,661)	$1,373,810,670
Return @ 12.2% Company @ 11.312% - Staff (b)		$ 203,033,498		$ 155,405,463

(a) Determined from Schedule B (Rate Filing Package).
(b) Testimony of Chris Child, Economic Research Division.

PUBLIC UTILITY COMMISSION OF TEXAS

TEXAS ELECTRIC SERVICE COMPANY AND SUBSIDIARY
INVESTED CAPITAL AND RETURN
STAFF ADJUSTMENTS

MARCH 31, 1980

Description		Staff Adjustment
Accumulated Depreciation		
Adjustment to reflect one-half of adjustment to expense		$ (258,434)(a)
Construction Work in Progress		
Construction Work in Progress - Staff	$ 269,039,980 (b)	
Construction Work in Progress - Company	(538,079,959)(g)	$(269,039,979)
Plant Held for Future Use		
Exclusion of Titus County water rights		$ (254,260)(c)
Working Capital		
Thirteen month average of materials and supplies	$ 9,284,803(d)	
Thirteen month average of prepayments	4,688,502(f)	
Thirteen month average of fuel gas inventory	4,627,205(d)	
Year end fuel oil inventory	21,407,491(d)	
Average working funds	4,241,098(d)	
Working cash allowance	12,947,007(e)	
Staff working capital	$ 57,196,106	
Company working capital	$ (71,548,734)(d)	$ (14,352,628)
Other Cost Free Capital		
Taxes accrued not yet payable	$ (6,837,593)(h)	
Payable to Edison Electric Institute	(337,767)(h)	$ (7,175,360)

(a) Computed using Schedule A (Rate Filing Package).
(b) Represents fifty percent of adjusted construction work in progress.
(c) Exhibit WMT-5, Taylor testimony.
(d) Schedule G (Rate Filing Package).
(e) Computed as one-eighth of Staff operation and maintenance expenses adjusted for items charged to expense per Schedule G-3 (Rate Filing Package).
(f) Determined from Schedule G (Rate Filing Package) and Company response to Commission request C-15.
(g) Schedule B (Rate Filing Package).
(h) Determined from information obtained during review of books and records.