



City of League City, TX

300 West Walker
League City TX 77573

Text File

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Title

Consider and take action on a resolution denying the Texas-New Mexico Power Company's proposed rate increase in connection with its statement of intent submitted on or about May 30, 2018 (City Attorney)

..Background:

On May 30, 2018, Texas-New Mexico Power Company (TNMP) filed an application to increase its annual revenues by approximately \$33.3 million, which represents an increase in revenue of about 10.5%. This is TNMP's first comprehensive base rate case since 2010. Included in TNMP's requested increase is recovery of about \$4.1 million for rate case expenses; about \$4.6 million for vegetation management; and about \$7.2 million in extraordinary expenses related to Hurricane Harvey.

TNMP proposed an effective date of July 5, 2018 for its increase in rates. The City has previously taken action to suspend TNMP's proposed effective date to October 3, 2018. The City is participating in the proceedings as part of the Alliance of TNMP Company Municipalities ("ATM"), a coalition of similarly situated cities in which TNMP provides electric service. Through ATM, the City intervened in TNMP's current rate proceeding at the Public Utility Commission ("PUCT") and is represented by the law firm of Herrera Law & Associates, PLLC.

BASIS FOR TNMP's REQUEST:

The main factors TNMP asserts as the basis for its proposed increase in rates are the following:

- Accounting for the addition of distribution and non-transmission investment since TNMP's last rate case in 2010
- Updated depreciation and amortization expenses
- Moving TNMP's Advanced Metering System (AMS) costs into base rates and elimination of the AMS surcharge
- Reduction of TNMP's discretionary service fees which TNMP had been using to reduce base rates
- A requested cost of capital consisting of a 10.5% return on equity and 50% debt/50% equity capital structure.

TNMP's application also accounts for changes in federal income tax resulting from recent change in federal tax law in which the U.S. Congress reduced the federal corporate income tax rate from 35% to 21%.

TNMP proposes to allocate the increase of \$33.3 million, which includes revenue to recover rate-case expenses, vegetation management, and Hurricane Harvey restoration costs, in addition to base revenues, among the customer classes as follows:

Customer Class	Increase in Revenue	Percent Increase in Revenue
Residential Service	\$27,089,862	23.4%
Secondary <=5kW	\$278,205	9.6%
Secondary > 5 kW NIDR	\$4,974,260	6.7%
Primary > 5 kW IDR	\$902,209	8.8%
Primary NIDR	\$1,512,536	23.4%
Primary IDR (includes WDLS)	\$585,375	6.4%
Transmission	\$2,948,645	20.3%
Lighting	\$427,227	11.8%
Less Network Transmission Revenue	<\$5,390,047>	
Total	\$33,328,273	10.90%

The amounts in the “Increase Revenue” column include increases in base revenues, TNMP’s proposed amortization of rate case expenses, additional annual vegetation management expenses and amortization of Hurricane Harvey restoration costs.

BILL IMPACT:

Based on TNMP’s application, the estimated impact of TNMP’s proposed change on a typical residential customer’s bill at varying usage levels is as follows:

Usage	Current Bill (TNMP Charges Only)	Proposed Bill (TNMP Charges Only)	\$ Increase (TNMP Charges Only)	% Increase (TNMP Charges Only)
1000 kWh	\$41.43	\$53.86	\$12.43	30%
2000 kWh	\$74.21	\$99.28	\$25.07	34%
3000 kWh	\$106.99	\$144.70	\$37.71	35%

(REP) to account for generation and retail activity costs, in addition to the transmission and distribution service costs assessed by TNMP, the full effect on a customer’s bill, after accounting for these other charges, is shown in the table below. (The “All REP Charges” amounts include, for illustrative purposes, a \$0.067 per kWh energy charge and \$9.95 base charge.)

Usage	Current Bill (All REP Charges)	Proposed Bill (All REP Charges)	\$ Increase (All REP Charges)	\$ Increase (All REP Charges)
1000 kWh	\$118.38	\$130.81	\$12.43	11%
2000 kWh	\$218.16	\$243.23	\$25.07	11%
3000 kWh	\$317.94	\$355.65	\$37.71	11%

ATM'S CONSULTANTS' REVIEW OF TNMP'S RATE REQUEST:

In order to minimize the City's rate case expenses, ATM has coordinated its efforts with another group of cities in which TNMP provides service, known as the Cities Served by Texas New Mexico Power Company, and which also intervened in the pending TNMP rate proceeding at the PUCT. The consultants engaged by the cities reviewed TNMP's rate application and recommend a *decrease* to TNMP's current revenues of about \$8.0 million as compared to TNMP's requested increase of about \$33 million. While there are other expenditures in TNMP's rate application that the ATM/Cities' consultants found too high, the primary factors that comprise ATM/Cities' recommended decrease in annual revenue are:

- \$10 million reduction related to TNMP's requested depreciation expense
- \$5 million reduction related to TNMP's requested vegetation-management expense
- \$10 million reduction related to the combined effect of the ATM/Cities' proposed return on equity ("ROE") of 9.1% (as compared to TNMP's requested ROE of 10.5%), a capital structure of 45% equity and 55% debt (compared to TNMP's proposed capital structure of 50% equity and 50% long-term debt), including the cost of short-term debt, and the cost of long-term debt of 7.04% (compared to TNMP's request of 7.2%)
- \$4 related to a reduction in TNMP's federal income tax expense resulting from the passage of the Tax Cut and Jobs Act of 2017 ("TCJA") which reduced the corporate income tax rate from 35% to 21%.

The ATM/Cities' consultants also recommend an immediate refund of approximately \$4.5 million that TNMP over-collected from rate-payers since January 1, 2017, the effective date of the Tax Cut and Jobs Act.

In addition to ATM/Cities' adjustments noted above, the other parties in the proceeding before the PUCT (e.g., the PUC Staff, the Office of Public Utility Counsel, the Texas Industrial Energy Consumers) proposed additional reductions that combined with the ATM/Cities' adjustments, would produce a decrease of about \$37 million. We do not expect this to be the final outcome, but it is indicative of the disparity between TNMP's proposal and the view of the parties representing the ratepayers' interests.

SETTLEMENT EFFORTS:

As is typical, the parties in the rate case have met to evaluate whether it is possible to resolve TNMP's request without the need for a trial (in PUCT parlance, a "contested hearing"). Those efforts at the moment do not appear that they will be fruitful. ATM's Special Counsel expects that settlement efforts may resume, but because the hearing at the PUCT on TNMP's proposed increase in rates starts on September 7, 2018, and, given the statutory deadline of October 3, 2018, for the City to take final action on TNMP's application to increase rates, the City cannot await the outcome of any settlement discussions.

RECOMMENDATION:

Given the impending statutory deadline, ATM's Special Counsel recommends that the City deny TNMP's requested rate increase. The accompanying resolution if approved by the City Council, would deny TNMP's requested increase in rates. Following denial of TNMP's application to increase rates, TNMP will file an appeal to the PUCT, which is standard procedure. Nonetheless, if the

City denies TNMP's request, TNMP and ATM as well as other parties to the PUCT proceeding, can still attempt to engage in settlement negotiations in order to seek a mutually beneficially resolution without the need for a contested hearing.

The City must take action no later than October 3, 2018. Failure to take action by October 3, 2018 would result in TNMP's proposed increase in rates would take effect on that date by operation of law.

CONTRACT ORIGINATION: N/A

Attachments:

1. Data Sheet
2. Proposed Resolution

FUNDING

{x} NOT APPLICABLE

STRATEGIC PLANNING

{x} NOT APPLICABLE