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PUC DOCKET NO. 35665

COMMISSION STAFF'S PETITION	§	PUBLIC UTILITY COMMISSION
FOR SELECTION OF ENTITIES	§	
RESPONSIBLE FOR TRANSMISSION	§	
IMPROVEMENTS NECESSARY TO	§	
DELIVER RENEWABLE ENERGY	§	OF TEXAS
FROM COMPETITIVE RENEWABLE	§	
ENERGY ZONES	§	

FILED
 2008 DEC 19 PM 2:09
 PUBLIC UTILITY COMMISSION

POST HEARING BRIEF OF SHARYLAND UTILITIES, L.P.

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December 19, 2008

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PUBLIC VERSION

**HIGHLY SENSITIVE PROTECTED MATERIAL
HAS BEEN REDACTED PURSUANT TO THE
PROTECTIVE ORDER IN DOCKET NO. 35665**

In summary, Sharyland's financing plan provides ample assurance that Sharyland will be able to raise the necessary debt and equity capital to complete the CTP facilities it is requesting and more in an economical and timely manner.

VI. Comments on Other TSPs Seeking to Construct CTP Facilities

At present, there appear to be at least four entities in this proceeding seeking to construct portions of the specific facilities that Sharyland has asked to build. These include the City of Garland ("Garland"), which operates a municipally-owned utility that provides retail electric service to the citizens and businesses of that community; the Texas Municipal Power Agency ("TMPA"), a joint action agency formed by the Cities of Bryan, Garland, Denton, and Greenville in order to provide electric power to the four member cities; Tejas, a subsidiary of Babcock & Brown, Ltd. ("Babcock & Brown"), a specialized leveraged funds and asset management company based in Australia; and WETT, which, as described above, is a new company owned by Brookfield Asset Management and Isolux.

Garland and TMPA are seeking to construct a combined total of approximately \$415 million in interconnected CTP facilities that would be located at the top of the northwestern portion of the CREZ facilities, including the "horse's head." Tejas proposes to construct \$873 million in facilities, including a line that would extend into the South Plains area up to the beginning of the "horses's head" and would overlap with the facilities requested by Sharyland. Although WETT has not specifically focused on the Panhandle but instead has proposed to construct all of the CTP facilities in the Scenario 2 build-out, it did indicate an interest in its cross rebuttal testimony in constructing one of the collection stations that Sharyland seeks to build. Accordingly, Sharyland will also address WETT's proposal.

PUBLIC VERSION

A. Municipal Entities

Sharyland has not challenged the technical or financial qualifications of any of the municipal entities to finance, construct, and operate CTP facilities in ERCOT. Both Garland and TMPA hold existing CCNs and are familiar with ERCOT practices. In addition, both entities have strong credit ratings and access to tax exempt financing. However, Sharyland has several concerns with their CTP proposals in this proceeding. These concerns are discussed below.

I. Construction of CTP Facilities Outside Municipal Boundaries

Both Garland and TMPA are proposing to construct CTP facilities that are located far outside their municipal boundaries. In the case of Garland, the nearest CTP facility in the Panhandle that it proposes to build is 240 miles from its boundary; in the case of TMPA, the nearest CTP facility is 210 to 260 miles from the boundaries of its member cities.⁹⁰

Neither Garland nor TMPA was able to explain clearly at the hearing why it was seeking to construct facilities located so far from its municipal boundaries.⁹¹ The proposal to build CTP facilities in the Panhandle is especially puzzling for Garland, which actually opposed the construction of facilities to interconnect wind generators in the Panhandle to ERCOT in Docket No. 33672.⁹² Garland witness David Grubbs acknowledged that it would be necessary for Garland to enter into a joint maintenance agreement with other TSPs in the area in view of the fact that it would require a drive of several hours from the city to reach the facilities.⁹³ Both Garland and TMPA indicated that they were indifferent to what CTP facilities were assigned to them so long as the total investment was the same as they had requested in their CTP proposals.⁹⁴

Mr. Grubbs acknowledged that the principal motivation for Garland's request was to assure that it maintains its current position in the ERCOT Transmission Cost of Service

⁹⁰ Responsive Testimony of Pat Wood, III, Joint Parties Ex. 3 at Exhibit PW-1R.

⁹¹ See Tr. at 1037-39 (Garland) (Grubbs) (Dec. 3, 2008); Tr. at 260-61 (TMPA) (Dec. 1, 2008).

⁹² See Docket No. 33672, Phase 2 Post-Hearing Brief of the City of Garland and Denton Municipal Electric at 1, note 1 (June 26, 2008).

⁹³ Tr. at 1035 (Grubbs) (Dec. 3, 2008).

⁹⁴ Tr. at 260-61 (TMPA) (Dec. 1, 2008); Tr. at 1037-38 (Garland) (Dec. 3, 2008).

PUBLIC VERSION

("TCOS") payment matrix.⁹⁵ According to Mr. Grubbs, "[i]f the ERCOT transmission grid grows by \$5 billion worth of additions and GP&L is not able to increase its rate base proportionally, its relative transmission expense will increase and its citizens will be harmed."⁹⁶ However, this is not an adequate basis for a decision to award CTP facilities to an applicant under PURA § 39.904(g) or the Commission's TSP selection rule.⁹⁷ The purpose of this proceeding is to develop the most beneficial and cost-effective transmission plan for customers, not to maintain the same relationships between utilities in the TCOS transmission matrix that currently exist. In fact, those relationships are constantly changing as new transmission is added, and no one argues that the basis for assigning transmission projects should be to assure that no utility's proportionate share of TCOS changes.⁹⁸ Under Mr. Grubb's logic, all transmission facilities would be assigned to TSPs on a proportional basis, regardless of where those facilities were located or which TSP was most suited to construct the facilities, an obviously absurd result.

As the hearing in this proceeding made clear, both Garland and TMPA intend to construct the CTP Facilities they have requested without seeking CCNs from the Commission, even though those facilities would be located far outside their municipal boundaries. At first blush, this might suggest that the municipal entities could complete construction of the CTP projects more rapidly than other TSPs that are required to go through the CCN process at the Commission. However, the evidence indicates that the opposite would likely be the case.

The municipal entities' proposal to bypass the CCN process would effectively strip the Commission's regulatory oversight over the routing or construction of the CTP facilities they would build. Moreover, it would deprive landowners of an independent objective adjudication of their concerns by a body with statewide authority; instead, decisions as to routing would be made by the municipal entity itself or by the applicable city council. As pointed out by Joint Parties' witness Pat Wood, this is of particular concern with entities that seek to construct CTP

⁹⁵ Rebuttal Testimony of David Grubbs, Garland Ex. 8 at 14; Tr. at 1037-39 (Grubbs) (Dec. 3, 2008).

⁹⁶ Rebuttal Testimony of David Grubbs, Garland Ex. 8 at 14; Tr. at 1037-39 (Grubbs) (Dec. 3, 2008).

⁹⁷ See Tr. at 578-86 (Dec. 2, 2008).

⁹⁸ Tr. at 578-86 (Dec. 2, 2008).

PUBLIC VERSION

facilities well outside their traditional footprints (as would be the case with Garland and TMPA).⁹⁹

Municipal entities have a special status under PURA because of the fact that they are political bodies that are accountable to their constituents.¹⁰⁰ To the extent that municipal entities construct transmission lines within their boundaries, the lack of Commission oversight of routing decisions is not of great concern because citizens affected by the lines have a remedy at the ballot box. However, when municipal entities seek to construct transmission facilities outside their traditional boundaries and claim the right to utilize eminent domain in such areas, they significantly increase the likelihood of litigation by affected landowners, who may legitimately question why cities located hundreds of miles away are seeking to condemn their property. As Mr. Wood stated, an award of transmission facilities to municipalities with no connection to the areas in which they seek to build and that do not intend to obtain CCNs will likely result in legal disputes and delays in completing the facilities.¹⁰¹

In addition, PURA § 39.904(g)(2) requires the Commission to “develop a plan to construct transmission capacity” for the CREZ build-out. It is difficult to see how the Commission can fulfill its statutory obligations when significant parts of the plan are outside its regulatory approval and oversight. Awarding the transmission responsibilities in this proceeding is a discretionary act on the part of the Commission, and it has wide latitude to determine the best plan. Its lack of authority over construction of transmission facilities by municipal entities is a compelling reason for not awarding any CTP facilities to Garland and TMPA.

2. TMPA’s Ability to Finance and Construct CTP Facilities.

A separate concern relates to TMPA’s ability to finance and complete construction of the CTP facilities it proposes to build. Sharyland witness Ralph Goodlet submitted testimony detailing the long history of litigation among the member cities of TMPA and noting questions as to whether the CTP proposal filed by TMPA was consistent with TMPA’s enabling legislation

⁹⁹ Responsive Testimony of Pat Wood, III, Joint Parties Ex. 3 at 14.

¹⁰⁰ Responsive Testimony of Pat Wood, III, Joint Parties Ex. 3 at 15.

¹⁰¹ Responsive Testimony of Pat Wood, III, Joint Parties Ex. 3 at 11-12.

PUBLIC VERSION

or the Power Sales Contract between TMPA and each of the member cities.¹⁰² Joint Parties' witness Pat Wood also expressed concerns with TMPA's ability to finance and construct the CTP Facilities and observed that the City of Bryan had already stated its opposition to the CTP proposal.¹⁰³ Given the history of litigation between Bryan and TMPA, Mr. Wood concluded that an award of facilities to TMPA "would likely be the subject of additional lawsuits" and noted that additional litigation was already underway arising out of the TMPA Board of Directors' approval of the bond resolution that was attached to TMPA's CTP proposal.¹⁰⁴

On December 3, the City of Bryan filed a letter with the Commission raising a number of procedural and substantive concerns related to TMPA's CTP proposal as well as a special TMPA Board meeting scheduled on December 4 to ratify and confirm TMPA's actions in this proceeding. In particular, the letter expressed opposition to any further participation by TMPA in the CREZ proposal. This letter was introduced in evidence as Commissioners Exhibit No. 2. On the following day, December 4, TMPA submitted a resolution of the TMPA Board of Directors that had been adopted at the special meeting held that day by six of the eight Board members (City of Bryan members were not present).¹⁰⁵ The resolution purported to confirm TMPA's commitment to construct the CTP facilities. However, Paragraph 5 of the resolution explicitly conditioned its commitment on the occurrence of subsequent events, including a decision by the Board to budget the necessary funds.¹⁰⁶ In response to a question, Staff witness Slade Cutter stated that he was not aware of any other TSP that had included a disclaimer in its proposal as broad as TMPA's disclaimer.¹⁰⁷

Sharyland takes no position on the issues concerning TMPA's authority to finance and construct the CTP facilities under either its enabling legislation or the Power Sales Contract, nor does Sharyland believe that it is necessary for the Commission to resolve these issues in reaching

¹⁰² Responsive Testimony of Ralph G. Goodlet, Sharyland Ex. 7 at 10-12.

¹⁰³ Cross-Rebuttal Testimony of Pat Wood, III, Joint Parties Ex. 6 at 15; Tr. at 726-27 (Wood) (Dec. 2, 2008).

¹⁰⁴ Cross-Rebuttal Testimony of Pat Wood, III, Joint Parties Ex. 6 at 15.

¹⁰⁵ TMPA Ex. 10.

¹⁰⁶ TMPA Ex. 10.

¹⁰⁷ Tr. at 1308-09 (Cutter) (Dec. 4, 2008).

PUBLIC VERSION

a decision in this proceeding. What is clear, however, is that there is a significant degree of uncertainty regarding TMPA's ability to complete any CTP projects assigned to it in a timely fashion. As noted during the hearing, there is also a question whether TMPA has the ability to finance the CTP project through revenues collected by TMPA under the Power Sales Contract.¹⁰⁸ To the extent that TMPA does not have such authority, it would need to find another means of financing the CTP Facilities.¹⁰⁹ However, TMPA provided no evidence of how it would raise the necessary capital if it was unable to finance the facilities under the Power Sales Contract because of legal challenges.

Obviously, the mere threat of litigation should not deter the Commission from taking actions that it believes are lawful and appropriate. However, Sharyland submits that questions concerning TMPA's commitment to finance and construct the CTP facilities it proposes to build, when combined with concerns with respect to its plan to build facilities hundreds of miles from the boundaries of its member cities, provides ample basis for concluding that award of facilities to TMPA will not achieve the Commission's goal of a timely build-out of the CREZ facilities.

3. Cost of Service Issues

Municipal entities would have access to tax-advantaged debt for financing any CTP Facilities that may be awarded to them. However, as the testimony of Sharyland witness Ellen Blumenthal made clear, access to lower cost debt does not mean that the transmission cost of service for Garland and TMPA will be lower than the cost of service of investor-owned utilities or that a decision not to award CTP facilities to Garland and TMPA will result in a higher cost to ratepayers. The reason for this is the specific methodology that Garland and TMPA plan to use for determining the return they will seek in the rate cases filed to recover the costs of their CTP facilities.

Municipal utilities have the option to utilize several different methodologies for calculating their return under the Commission's Transmission Cost of Service Rate Filing

¹⁰⁸ Tr. at 1311-13 (Dec. 4, 2008).

¹⁰⁹ Tr. at 1311-13 (Dec. 4, 2008).

PUBLIC VERSION

Package for Non-Investor Owned Utilities.¹¹⁰ Although Garland initially proposed using the “Utility” method, it subsequently filed supplemental testimony changing to the “Debt Service Coverage” (“DSC”) methodology.¹¹¹ Under this methodology, the utility’s annual debt service payment is multiplied by its DSC rate (in the case of Garland and TMPA, 1.5). The resulting figure is then divided by the utility’s rate base to determine its effective rate of return.

In the case of TMPA, which is already using the DSC methodology, its currently approved rate of return is 12.54 percent.¹¹² Ms. Blumenthal calculated the equivalent return for Garland for the CREZ facilities using the same DSC methodology and concluded that it would be 14.7 percent. Both rates of return are significantly higher than the equivalent rates of return for all of the investor-owned TSPs as shown on Staff witness Slade Cutter’s Exhibit SC-R-A, which ranged from 10.04 percent to 11.21 percent.¹¹³ Although Garland and TMPA challenged the specific figures used by Ms. Blumenthal at the hearing, even the revised figures developed by TMPA in its own Exhibit 7 showed that TMPA would have a higher rate of return than Sharyland, and Garland’s would be about the same.¹¹⁴

As Ms. Blumenthal testified, it is premature to attempt to determine the effect of the various CTP proposals on TCOS at this early stage of the process.¹¹⁵ It will be several years before TSPs seek to recover costs associated with the facilities and it is not possible to predict what the cost of capital will be then, let alone what a TSP’s TCOS will be. As a result, the various TCOS analyses that have been submitted¹¹⁶ provide little guidance in deciding how to

¹¹⁰ Responsive Testimony of Ellen Blumenthal, Sharyland Ex. 10 at 3; Direct Testimony of Daniel Lanning, Garland Ex. 4 at 7.

¹¹¹ Supplemental Direct Testimony of Daniel Lanning, Garland Ex. 5 at 1-2.

¹¹² See Tr. at 332 (Graves) (Dec. 1, 2008) (referring to Schedule B to TMPA’s Application for Update of Wholesale Transmission Rates, currently pending in Docket No. 36392); Cross-Rebuttal Testimony of Ellen Blumenthal, Sharyland Ex. 17 at 4.

¹¹³ Rebuttal Testimony of Slade Cutter, Staff Ex. 5 at Exhibit SC-R-A. (This Exhibit was misidentified in Mr. Cutter’s testimony as Exhibit SC-3.)

¹¹⁴ TMPA Ex. 7 showed a return of 7.26 percent for Garland, 9.52 percent for TMPA, and 7.86 percent for Sharyland. Tr. at 433-34 (Blumenthal) (Dec. 2, 2008).

¹¹⁵ Cross-Rebuttal Testimony of Ellen Blumenthal, Sharyland Ex. 17 at 11.

¹¹⁶ See Responsive Testimony of Chris Parker, WETT Ex. 5 at Bates Nos. 11-15 and Exhibit 5 (Bates No. 54); WETT Ex. 5A (Revised TCOS Analysis).

PUBLIC VERSION

assign CTP facilities. What is clear is that it cannot be assumed that municipal utilities will have a lower TCOS than investor-owned utilities. While municipal entities have a lower cost of debt due to their ability to use tax exempt financing, their TCOS – and hence the impact on ratepayers – may actually be higher than investor-owned entities that do not have access to such financing.

B. Tejas Transmission

I. Financial Qualifications

The obvious concern with Tejas is whether it is financially qualified to build CTP facilities. The TSP Selection Rule, P.U.C. SUBST. R. 25.216(e)(2), requires that an Interested TSP “must establish that it has adequate financial resources as described in subparagraphs (A) – (G) of this paragraph.” The remainder of the paragraph sets forth several different ways that an Interested TSP can make such a demonstration, including holding an investment grade credit rating (either itself or through its parent company), meeting certain financial ratios, or otherwise providing evidence that it has the capability to finance the CTP Facilities it proposes to construct. In its CTP proposal, Tejas relied heavily on the financial resources of its parent company, Babcock & Brown, to show its financial qualifications. Among other things, Tejas claimed that it has “the corporate backing of its corporate parent;”¹¹⁷ that “Babcock & Brown will stand behind the financial requirements of the Guarantee;”¹¹⁸ that “Babcock & Brown expects to have the financial resources outlined for Babcock & Brown in the financial plan;”¹¹⁹ and that “Babcock & Brown is a financially strong and profitable company.”¹²⁰ Tejas also asserted that Babcock’s “credit rating remains strong,” citing a Standard & Poor’s rating issued in August 2008.¹²¹ Thus, Tejas’ contention that it is capable of financing and constructing the CTP facilities it seeks to construct is squarely based on its affiliation with Babcock & Brown.

¹¹⁷ Tejas CTP Proposal, Tejas Ex. 1 at Bates No. 0007.

¹¹⁸ Tejas CTP Proposal, Tejas Ex. 1 at Bates No. 0104.

¹¹⁹ Tejas CTP Proposal, Tejas Ex. 1 at Bates No. 0104.

¹²⁰ Tejas CTP Proposal, Tejas Ex. 1 at Bates No. 0104.

¹²¹ Tejas CTP Proposal, Tejas Ex. 1 at Bates No. 0102.