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ARKANSAS PUBLIC SERVICE COMMISSION

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FILED

IN THE MATTER OF A SHOW CAUSE ORDER)
DIRECTED TO ENTERGY ARKANSAS, INC.)
REGARDING ITS CONTINUED MEMBERSHIP IN)
THE CURRENT ENTERGY SYSTEM AGREEMENT,)
OR ANY SUCCESSOR AGREEMENT THERETO,)
AND REGARDING THE FUTURE OPERATION AND)
CONTROL OF ITS TRANSMISSION ASSETS)

DOCKET NO. 10-011-U
ORDER NO. 76

ORDER

By this Order the Arkansas Public Service Commission (Commission) resolves the following outstanding issues in this proceeding:

1. Entergy Arkansas, Inc.'s (EAI) November 28, 2011 *Application to Transfer Functional Control of its Electric Transmission Facilities to the Midwest Independent Transmission System Operator Regional Transmission Organization (EAI's Application)*;
2. EAI's August 24, 2012 *Motion for Finding of Compliance with Conditions and for Approval of Application*;
3. Midwest Independent Transmission System Operator's (MISO) August 31, 2012 *Motion for Finding of Compliance with Conditions and Approval of Application*;
4. MISO's October 31, 2012 *Motion for Finding of Compliance with the Requirements of Order No. 72*;
5. MISO's January 7, 2013 *Motion for Finding of Compliance with the Requirements of Order No. 74*;
6. EAI's January 23, 2013 *Motion to Discontinue Activities Necessary to Operate as a True Stand-Alone Electric Utility*; and

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7. EAI's request for authorization to record and defer its MISO transition costs as a regulatory asset.

EAI's Application, the Motions identified above, and EAI's request to record and defer its MISO transition costs as a regulatory asset are conditionally granted by this Order.

Background

After the filing of multiple rounds of written testimony by witnesses for the parties to this proceeding and a public evidentiary hearing regarding EAI's Application, the Commission issued Order No. 68 in this Docket on August 3, 2012. In Order No. 68¹ the Commission listed nineteen separate conditions which would need to be satisfied by either EAI or MISO before the Commission could "reach a finding that EAI's Application is in the public interest." Specifically, the Commission ruled as follows:

... [T]he Commission is unable, at this time, to reach a finding that EAI's Application is in the public interest. However, assuming compliance by EAI and ... [MISO] of the [nineteen] conditions ..., and upon proper motion and proof of compliance ..., the Commission will make a determination whether EAI and MISO have, in fact, complied with the conditions. Upon a finding by the Commission that EAI and MISO have ... complied with the conditions, the Commission will grant conditional approval of EAI's Application, as being in the public interest, and will authorize EAI to sign the MISO Transmission Owners Agreement (TOA) and move forward with the MISO integration process. However, subsequent to the issuance of such conditional approval order, *if the Commission, after notice and hearing, finds that any condition enumerated herein has been materially modified or not fulfilled*, the Commission will withdraw its conditional approval and require EAI to exit MISO. Therefore, the Commission hereby defers further action on EAI's Application at this time.

Order No. 68 at 33, emphasis added.

¹ Order No. 68 is incorporated herein by reference as though set forth fully, word for word, as are Orders No. 72, 73, 74 and 75 of this Docket.

Compliance Filings of EAI and MISO

In response to Order No. 68, on August 24, 2012, EAI filed *Entergy Arkansas, Inc.'s Motion for Finding of Compliance with Conditions and for Approval of Application*. On the same date EAI also filed the Compliance Testimony (Document No. 919) of Mr. Hugh McDonald, EAI President and Chief Executive Officer, in support of EAI's Compliance Motion.

On August 31, 2012, MISO filed *Midwest Independent Transmission System Operator, Inc.'s Motion for Finding of Compliance with Conditions and Approval of Application*. On the same date MISO filed the Compliance Testimony (Document No. 926) of Mr. Clair J. Moeller, MISO Vice-President of Transmission Asset Management, in support of MISO's Compliance Motion.

By Order No. 72, issued on October 26, 2012, the Commission found that "EAI and MISO have either complied or substantially complied with the Order No. 68 conditions with the exception of Condition No. 13 with which MISO has sufficiently complied for the EAI/MISO integration process to move forward at this time." Order No. 72 at 29. Accordingly, the Commission ordered, in part, as follows:

1. EAI is hereby authorized to sign the MISO Transmission Owners Agreement and move forward with the EAI/MISO integration process;
2. Final approval of EAI's Application will be held in abeyance pending satisfaction of the following directive;
3. MISO is directed to expeditiously file in this Docket proof that MISO's governance Proposals A and B have each been officially approved and adopted by OMS, MISO and the MISO TOs; and
4. Upon satisfactory compliance by MISO with the immediately preceding directive, the Commission will issue an order granting conditional approval of EAI's Application subject to EAI's and

MISO's ongoing compliance with the Order No. 68 Conditions as clarified by the Commission hereinabove.

Id. at 29-30.

EAI signed the MISO Transmission Owners Agreement on October 31, 2012. EAI President Hugh McDonald Supplemental Direct Testimony at 4, Document No. 960, November 1, 2012. Thereafter, on December 13, 2012, MISO approved EAI as a new MISO Transmission Owner (TO) member. McDonald Supplemental Direct Testimony at 4, Document No. 984, January 23, 2013.

On October 31, 2012, MISO filed its *Motion for Finding of Compliance with the Requirements of Order No. 72* and the supporting Compliance Testimony (Document No. 959) of MISO Vice-President Moeller. By Order No. 74, issued on November 21, 2012, the Commission directed MISO to provide additional proof that the MISO TOs have "officially approved and adopted" MISO's "Governance Proposal B" which provides the Organization of MISO States (OMS) with enhanced authority for determining and filing alternative cost allocation methodologies with the Federal Energy Regulatory Commission (FERC) pursuant to Section 205 of the Federal Power Act. Order No. 74 at 3-4. In response to Order No. 74, MISO filed on January 7, 2013, its *Motion for Finding of Compliance with the Requirements of Order No. 74* and the supporting Compliance Testimony (Document No. 978) of MISO Vice-President Moeller.

By Order No. 75, issued on March 18, 2013, the Commission requested clarification and assurance from EAI that EAI "does not intend to discard the 'bundled load exemption' with regard to EAI's retail transmission rates as required by [Order No. 68] Condition No. 8." Order No. 75 at 5. On March 27, 2013, EAI President McDonald filed Supplemental Compliance Testimony in response to Order No. 75. Therein, Mr. McDonald explained EAI's compliance with Condition No. 8 and reaffirmed "without

hesitation” EAI’s “commitment to comply with Condition No. 8” McDonald Supplemental Compliance Testimony at 15, Document No. 997, March 27, 2013. On March 29, 2013, MISO filed the Compliance Testimony of Mr. Richard Doying, MISO Executive Vice-President, in response to Order No. 75. Mr. Doying testifies that, “[a]s long as EAI is a MISO Transmission Owner and uses Network Integration Transmission Service on those [transmission] assets to serve its Bundled Load (or services under other rate schedules to which the Bundled Load Exemption applies) it may use the Bundled Load Exemption.” Doying Compliance Testimony at 4, Document No. 998, March 29, 2013.

EAI’s Motion to Discontinue Stand-Alone Option

On January 23, 2013, EAI filed in this Docket its *Motion to Discontinue Activities Necessary to Operate as a True Stand-Alone Electric Utility* along with the supporting Supplemental Testimonies of EAI President McDonald, and Mr. Kurtis Castleberry, EAI Director of Resource Planning. Mr. McDonald testifies that continuing to develop a stand-alone option “would be an unnecessary expense for our customers and would require a diversion of resources that would jeopardize the successful integration with MISO on December 19, 2013.” McDonald Supplemental Testimony at 3, Document No. 984, January 23, 2013. Mr. Castleberry testifies that the continued allocation of resources for the dual paths, i.e. MISO integration and the stand-alone option, “will not only be wasteful, but it also will increasingly jeopardize EAI’s ability to successfully integrate with MISO on December 19, 2013.” Castleberry Supplemental Testimony at 10, Document No. 985, January 23, 2013. Mr. Castleberry also testifies that the following “positive effects” will be realized if EAI is allowed to discontinue development of the stand-alone option:

1. Reduce cost, and conserve time and valuable resources;
2. Reduce risk to the primary goal of MISO integration;
3. Avoid confusion for Embedded Entities who may be reluctant to plan for their MISO integration while EAI pursues multiple scenarios, but who are on a tight schedule if they are to be ready for MISO market operations by December 2013;
4. Avoid potential concerns with NERC, which must certify and approve EAI's new operating model, but will be reluctant to go through the extensive time and expense of certifying additional operating scenarios; and
5. Mitigate the increasing risk of implementing multiple, fully-operable solutions beyond approximately March 1, 2013, that eventually would become an infeasible project burden.

Id. at 10-11.

EAI's Request to Defer MISO Transition Costs as a Regulatory Asset

EAI witness Castleberry estimates that the cost for EAI, along with all of the other Entergy Operating Companies, to transition to membership in MISO by December 2013 is "roughly \$105 million" and that EAI's share of these costs "is approximately \$22 million" based upon EAI's "responsibility ratio share" of the total estimated \$105 million. Castleberry Direct Testimony at 29, Document No. 369, May 12, 2011. Further, Mr. Castleberry testifies that EAI will incur additional costs, roughly \$35 million, to maintain the Commission directed alternatives to MISO membership through December 2013. *Id.* at 29-30. In addition, Mr. Castleberry testifies that EAI has incurred approximately \$1.9 million in costs through March 2011 associated with EAI's

“evaluation of its post-[Entergy] System Agreement options to arrive at ... [EAI’s] recommended Transition Plan to join MISO...” According to Mr. Castleberry, “[a]pproximately \$0.3 million of these costs are currently deferred as a regulatory asset pursuant to ... [Commission] Order Nos. 6 and 15 in which the Commission allowed regulatory asset treatment of specific [Transition Plan] study costs.” *Id.* at 30-31. The “remaining costs reflect additional costs incurred by EAI to evaluate options not specifically addressed in those orders.” *Id.*

EAI witness Jay Lewis, Vice-President of Finance for Entergy Services, Inc., explains that a regulatory asset is an accounting mechanism that is unique to the cost-based ratemaking environment of the utilities industry and involves the “deferral of an incurred cost which would normally be recorded as an expense as an asset on the balance sheet because it is probable that such cost will be included in a future period for ratemaking purposes.” Lewis Supplemental Direct Testimony at 4-5, Document No. 371, May 12, 2011. Mr. Lewis testifies that EAI’s request for regulatory asset treatment “is limited to the MISO ... implementation costs that would otherwise be recorded as expenses in the periods in which the costs are incurred.” *Id.* at 7. Based upon EAI witness Castleberry’s preliminary estimate, described above, Mr. Lewis testifies that “approximately \$15 million of EAI’s \$22 million of total implementation costs would be deferred as a regulatory asset, assuming all Entergy Operating Companies joined ... MISO ... in December 2013.” *Id.* at 8. Also, Mr. Lewis testifies that if EAI continues to pursue multiple “implementation paths ... through December 2013, EAI would record an estimated \$21 million of additional deferrals out of the roughly \$35 million in additional costs” identified by Mr. Castleberry. *Id.* In addition, Mr. Lewis testifies that EAI is requesting deferral of the remaining \$1.6 million out of the \$1.9 million as

identified above by Mr. Castleberry. *Id.* Finally, EAI is requesting a carrying cost rate of 7.0% on the balance of any allowed deferred costs. *Id.* at 9.

Staff witness Jeff Hilton, Staff Director of Revenue Requirements, testifies that he agrees “that deferral of the implementation costs is reasonable at this time.” Hilton Supplemental Initial Testimony at 6, Document No. 516, July 12, 2011. He explains that a “reservation at this time of these types of one-time costs for future review and consideration for rate recovery is certainly reasonable in principle.” *Id.* However, Mr. Hilton testifies that the Commission should require adequate ratepayer protections to ensure ratepayers pay no more than is required and reasonable for the provision of utility service.” *Id.* To that end, Mr. Hilton recommends that the Commission impose the following five ratepayer protection provisions:

1. The deferred costs should be specific to EAI’s implementation plan, as authorized by the Commission;
2. Only incremental expenses should be deferred for future recovery; and expenses which are already being recovered through base rates, *e.g.* EAI payroll and related expenses, should specifically be excluded;
3. Costs that are routinely disallowed or any ratemaking adjustments of the types of expense in establishing base rates, either entirely or in part, in EAI’s most recent rate case should likewise be excluded, *e.g.* costs that are not necessary in providing electric service or not appropriate for rate recovery, such as charitable contributions or incentive pay;
4. All deferred costs should be subject to audit, analysis, examination and adjustment to ensure that only reasonable and prudent costs are included and recoverable; and

5. EAI's request for a carrying charge should be denied consistent with the Commission's past treatment of similar unamortized expenses balances.

Id. at 6-7.

Arkansas Attorney General (AG) witness William Marcus testifies that EAI's deferral request "is generally reasonable" so long as the deferred costs are "incremental ... and reflect other regulatory decisions of the Commission." Mr. Marcus recommends that the Commission define incremental costs as it did in Docket No. 01-041-U. Mr. Marcus states that the Commission, in that case, adopted Staff's recommendation that "payroll costs for employees whose costs were included in current rates – those on 1995 payrolls who were included in Docket No. 96-360-U, as well as other employees for which EAI allegedly provided inadequate documentation" be removed from the deferral account. Marcus Supplemental Direct Testimony at 3, Document No. 510, July 12, 2011, citing Commission Order No. 8 in Docket No. 01-041-U at 8-12.

In his Rebuttal Testimony, EAI witness Lewis disagrees with Staff witness Hilton's recommendation that EAI not be allowed carrying costs on the deferral amounts. Lewis Rebuttal Testimony at 5-6, Document No. 568, August 4, 2011. Mr. Lewis states that the deferred costs "represent actual cash expenditures that will be incurred by the Company over a multi-year period and deferred for future recovery, likely also over a multi-year period." Accordingly, Mr. Lewis asserts that "there will in fact be an economic cost of funds incurred by EAI as a result of the incurrence of these costs, and [therefore] it is appropriate that this economic cost be included in the deferred costs." Otherwise, Mr. Lewis argues, the Company "will incur a de facto disallowance without any finding of imprudence." *Id.*

Responding to the testimony of AG witness Marcus, Mr. Lewis states that he disagrees with Mr. Marcus' comments on incremental costs and recommendation that the Commission use a similar definition to that used in Docket No. 01-041-U to determine incremental costs. *Id.* at 8. More specifically, Mr. Lewis argues that the issues in Docket No. 01-041-U "were very specific to transition to competition activities and costs and tied to the legislation that allowed them." *Id.* The determination of incremental costs, asserts Mr. Lewis, "should be, as described by [Staff witness] Mr. Hilton, based on whether the costs are already being recovered in base rates." Further, Mr. Lewis argues that this issue "is more appropriately addressed in a future rate case coincident with EAI's joining ... [MISO] in which recovery of these deferred costs will be requested." *Id.*

In his Surrebuttal Testimony Staff witness Hilton states his disagreement with EAI witness Lewis on the issue of the application of carrying costs to the deferred costs. Specifically, Mr. Hilton testifies as follows:

In establishing utility revenue requirements, the Commission establishes a rate of return that is applied to assets that are devoted to providing utility service. The Commission also authorizes the recovery of expenses associated with the provision of utility service, but does not authorize a rate of return on those expenses. Historically, when the Commission has permitted the deferral of expenses for recovery in a future period, it has not authorized a return on those expenses. Mr. Lewis advocates a departure from the Commission's established treatment of deferred expenses. While I agree that it is reasonable to defer the expenses associated with the Company's transition to post-2013 operations subject to the conditions addressed in my Supplemental Initial Testimony ..., I do not support the application of a carrying charge [As] I noted in my Supplemental Initial Testimony, the inclusion of carrying charges ... suggests will result in ratepayers paying more than is required or reasonable for utility service. The Commission should not deviate from its established treatment of expenses that are deferred for recovery in future periods and should not include any carrying charges.

Hilton Surrebuttal Testimony at 2, Document No. 597, August 18, 2011.

In his Sur-Surrebuttal Testimony, EAI witness Lewis continues to argue for the application of carrying costs to the deferred costs. Mr. Lewis asserts that the requested MISO implementation costs “will be deferred over a four-year period and the subsequent recovery of those deferred costs likely would cover several additional years, the longer term carrying costs proposed by the Company is reasonable.” Lewis Sur-Surrebuttal Testimony at 7-8, Document No. 622, August 25, 2011. In an effort to address some of Mr. Hilton’s concerns, Mr. Lewis suggests that the carrying cost calculation “could be specified to be a simple interest calculation ... [which] would accrue monthly based on the ... [MISO] implementation deferral balance but there would be no compounding of interest.²” Mr. Lewis states that this treatment “would be similar to the carrying cost calculation contained in the storm reserve accounting legislation.” *Id.* at 8.

Ruling of the Commission

Based upon the assurances contained in EAI’s and MISO’s compliance filings, as identified hereinabove, the Commission finds that EAI and MISO have either complied or substantially complied with each of the Order No. 68 conditions. Therefore, the Commission finds that EAI’s *Application to Transfer Functional Control of its Electric Transmission Facilities to the Midwest Independent Transmission System Operator Regional Transmission Organization* is supported by substantial evidence of record and is in the public interest, conditioned upon full and continued compliance by EAI and MISO with each of the Order No. 68 Conditions. Failure by EAI or MISO to comply fully with each of the Order No. 68 Conditions will trigger action by the Commission pursuant to Order No. 68 Condition No. 5 which provides as follows:

² “The monthly rate as proposed by the Company would be 0.5833 percent – 7 percent divided by 12.” *Id.*

5. Should EAI become a member of MISO, EAI shall agree that the Commission, *sua sponte* or upon the motion of any party, after notice and hearing, may direct EAI to exit MISO under the terms of the [EAI/MISO] Memorandum of Understanding or the ... [EAI/MISO Transmission Owners Agreement.] EAI will otherwise retain all of its rights, state and federal, to appeal or seek review of or relief from the decision of the Commission.

Order No. 68 at 27.

To ensure continued compliance with each of the Order No. 68 Conditions, the Commission will closely monitor the integration of EAI into MISO, including but not limited to, all filings made by EAI and MISO in the relevant proceedings pending before the FERC and before the Entergy retail regulators in Louisiana, Mississippi and Texas.

Based upon the above findings, the Commission also finds that EAI's *Motion to Discontinue Activities Necessary to Operate as a True Stand-Alone Electric Utility* will save unnecessary additional costs and, therefore, is in the public interest.

Based upon the testimony of EAI witness Lewis and Staff witness Hilton, as set forth above, the Commission also finds that EAI's request to defer its MISO Transition Costs as a Regulatory Asset is reasonable and in the public interest. However, for the reasons cited by Staff witness Hilton, the Commission finds that the addition of carrying cost to the deferred cost balances is unreasonable and unjustified and, therefore, is not in the public interest.

Accordingly, the Commission orders and directs as follows:

1. EAI's *Application to Transfer Functional Control of its Electric Transmission Facilities to the Midwest Independent Transmission System Operator Regional Transmission Organization* is granted conditioned upon full and continued compliance by EAI and MISO with each of the Order No. 68 Conditions;

2. Failure by EAI or MISO to comply fully with each of the Order No. 68 Conditions will trigger action by the Commission pursuant to Condition No. 5;

3. EAI's *Motion to Discontinue Activities Necessary to Operate as a true Stand-Alone Electric Utility* is granted;

4. EAI's request for approval to defer its MISO transition costs, without the addition of carrying costs, is granted subject to EAI compliance with the five ratepayer protection provisions as recommended by Staff witness Hilton and as set forth above. However, a prudence finding regarding such transition costs is specifically reserved to be addressed and considered in a later proceeding in which EAI seeks to incorporate such costs into its retail rates. Also, nothing in this Order shall constitute a finding that such costs are approved for recovery through EAI's retail rates;

5. EAI and MISO are directed to file in this Docket on the first business day of each month, beginning on May 1, 2013, Supplemental Testimony providing monthly updates regarding the progress of the integration of EAI into MISO process; critical developments in the various Entergy/MISO related proceedings pending before the FERC and before Entergy's other retail regulators; and ongoing compliance with the Order No. 68 Conditions;

6. By subsequent Order the Commission will establish a procedural schedule for the consideration of MISO's *Application for a Certificate of Convenience and Necessity* (CCN) (MISO's Application) pending before the Commission in Docket No. 11-165-U. By its Application MISO seeks an Arkansas CCN "to transact the business of an electric public utility in the State of Arkansas for the limited purpose of asserting functional control over transmission facilities of MISO transmission owning members subject to this Commission's jurisdiction." MISO Application at 9. Upon the issuance of

a procedural schedule by the Commission, Docket No. 11-165-U will proceed toward conclusion and a final ruling.

BY ORDER OF THE COMMISSION,

This 5th day of April, 2013.

I hereby certify that this order, issued by the Arkansas Public Service Commission, has been served on all parties of record on this date by the following method:

U.S. mail with postage prepaid using the mailing address of each party as indicated in the official docket file, or
 Electronic mail using the email address of each party as indicated in the official docket file.

Colette D. Honorable, Chairman

Olan W. Reeves, Commissioner

Elana C. Wills, Commissioner

Kristi Rhude, Secretary of the Commission