ARKANSAS PUBLIC SERVICE COMMISSION

IN THE MATTER OF THE APPLICATION) OF ENTERGY ARKANSAS, INC., FOR) APPROVAL OF CHANGES IN RATES FOR) RETAIL ELECTRIC SERVICE)	DOCKET NO. 13-028-U ORDER NO. 21

ORDER

I. Summary

On March 1, 2013, Entergy Arkansas, Inc. (EAI or the Company) filed in this Docket its Application seeking an increase in the rates it charges its Arkansas retail electric customers. EAI files this Application as the Company makes structural changes by leaving the Entergy System Agreement, which will eliminate the rough production cost equalization payments allocated among the Entergy Operating Companies (OpCos), and prepares to join the Midcontinent Independent System Operator, Inc. (MISO). Exit from the System Agreement will eliminate approximately $124 million dollars currently collected from ratepayers through EAI's Production Cost Allocation Rider (Rider PCA). *See* Figure 2, EAI Application at 22. EAI seeks a retail revenue requirement increase of $179,531,057, amended to $145,338,325 in its Sur-surrebuttal case. EAI also seeks a return on equity of 10.4% and an overall rate of return of 5.02%. EAI's rate request, if granted would, result in a 0.95 percent reduction for a typical customer using 1000 kWh a month. See EAI Application at ¶ 6.

As discussed herein, the Arkansas Public Service Commission (Commission) rejects EAI proposed retail revenue requirement increase, EAI's proposed return on equity and overall rate of return in favor of a lower retail revenue requirement to be computed based upon Staff's Revised Surrebuttal retail non-fuel Revenue Requirement

of $1,123,568,031 and a Revenue Deficiency of $109,968,597, with adjustments to Staff's Revised Surrebuttal Revenue Requirement and Revenue Deficiency in compliance with this Order for a return on equity of 9.3% and an overall rate of return of 4.29%; a disallowance of $8,087,877 in annual short-term incentive costs; a disallowance of $7,036,188 in long-term incentive costs; adoption of the methodology recommended by the Hospital and Higher Education Group (HHEG) witness Mark E. Garret regarding removal of the costs of EAI's supplemental executive retirement plans for benefits on salary levels exceeding $255,000; and all other adjustments necessary for full compliance with this Order.

Additionally, as discussed herein, the Commission rejects in this Docket the closure of EAI's Optional Interruptible Service Rider (Rider OIS) to new customers and rejects EAI's proposed Market Valued Load Modifying Rider (Rider MVLMR) and EAI's proposed Market Valued Demand Response Rider (MVDRR). The Commission directs EAI to file any proposed modifications of Rider OIS in a stand-alone tariff docket where the Commission may more fully consider whether and what changes may be necessary to Rider OIS for EAI's participation in MISO. As summarized above, and based upon the totality of evidence presented in this Docket, the Commission finds that EAI's retail revenue requirement increase request is excessive, and that EAI is entitled to a retail revenue requirement increase as recalculated pursuant to the Commission's findings herein. Among other adjustments to EAI's request, the Commission denies EAI's request for a 10.4% return on equity. Instead, the Commission finds that a return on equity of 9.3% is fair, reasonable and appropriate. The Commission adopts General Staff's (Staff) recommended capital structure of 53% to 47% total debt-to equity and

adopts Staff's recommendation that short-term debt should be included. Additionally, the Commission adopts Staff's adjustment to EAI's external sources of capital to reflect EAI's Money Pool lending to the other Entergy OpCos. The Commission denies EAI's requested method of calculating Accumulated Funds Used During Construction (AFUDC) and adopts the proposal of General Staff regarding AFUDC.

The Commission approves Staff's recommended 30-year period for weather normalization of billing determinants and rejects weather adjustments for industrial customer loads. The Commission finds no need to make an adjustment to billing determinants as a result of expanding EAI's vegetation management program and finds that Staff's billing determinants model and its results are reasonable and in the public interest.

Regarding Working Capital Assets (WCA), the Commission agrees with Staff's exclusion of clearing accounts and Staff's elimination of $5,323,940 from Wholesale Accounts Receivable. Additionally, the Commission agrees that a regulatory asset related to rate case expense should not be included in WCA.

The Commission agrees with Staff's inclusion in zero cost capital of accrued interest on the Accumulated Provision for Property Insurance, contingent liability accounts and prepaid contributions in aid of construction. The Commission finds Staff's method of calculating interest payable is reasonable and Staff's balance should be updated to reflect the Commission's findings as to the level and cost of debt. The Commission further finds Staff's four-year average of common stock dividends payable is more reflective of an ongoing level and should be included in Current Accrued and

Other Liabilities (CAOL). The Commission agrees that the balance in the nuclear fuel storage cost litigation should also be included in CAOL.

The Commission agrees that Staff's treatment of Accumulated Deferred Income Taxes (ADIT) is proper and also finds that the ADIT related to the Grand Gulf over/under recovery should reflect a normalized level based on a five-year annual year-end average. The Commission accepts the inclusion of the ADIT related to deferred MISO Transition Costs as a zero cost of capital and rejects EAI's removal of ADIT accounts and accepts Staff's proposed balances for any differences not specifically addressed herein.

The Commission accepts the inclusion of both the forfeited discounts revenues and the manufacturers' tax credit in the Revenue Conversion Factor. Further, the Commission adopts Staff's proposed adjusted *pro forma* payroll costs, as set out by Staff witness Bill Taylor in his Revised Surrebuttal Testimony, including the corrections outlined therein, as appropriately reflecting the normal, expected levels for payroll and payroll-related costs, including the use of the five-year average for ESI and EOI. The Commission approves Staff's payroll adjustment using Staff's test year data for EAI's payroll calculation taking into account the Human Capital Management (HCM) adjustment.

The Commission denies EAI's request to recover 100% of incentive pay and stock options for its employees from Arkansas ratepayers, and finds that EAI and Staff have failed to show that EAI's short-term, long-term, and stock-based incentive compensation provides ratepayer benefits justifying 100% inclusion in rates. The Commission recognizes that both shareholders and ratepayers benefit from the

structure of EAI's short-term incentive plans and therefore finds that $8,087,877 in annual short-term incentive costs should be removed from EAI's operating expenses. The Commission also agrees that EAI's long-term incentive compensation is based entirely on the financial performance of EAI and benefits shareholders. Therefore the Commission finds that $7,036,188 should be disallowed and removed from EAI's operating expenses.

Additionally, the Commission agrees with Hospital and Higher Education Group (HHEG) witness Mark Garrett that the shareholders, not ratepayers, should pay for the costs of EAI's supplemental executive retirement plans and adopts Mr. Garrett's methodology and disallows expenses on salary levels exceeding $255,000. Such expenses should be removed from EAI's operating expenses. The Commission further adopts Staff's adjustments regarding the Hot Spring Plant, Lake Catherine Unit 4, vegetation management, rate case expense, HCM costs and savings expense (and regulatory asset treatment), and potential System Planning and Operations (SPO) study expense. The Commission adopts Staff's recommendations regarding the expense adjustment for EEI and NEI dues and, heeding the recommendation of the Arkansas Attorney General (AG), agrees that in future rate cases, EAI should and will take additional steps to ensure verification of its EEI and NEI dues in order to insure that only appropriate expenses are passed on to EAI's ratepayers.

The Commission adopts Staff's depreciation rates and recommendations regarding plant life extensions, interim retirements and dismantlement reporting requirements. The Commission approves using the Average and Peak methodology to allocate capacity-related generation plant costs to the different customer classes and

concludes that Accounts 364-368 should be allocated to the customer classes using a 100% demand methodology. The Commission also orders EAI to begin maintaining load data sufficient for a Cost of Service Study that separates the current Large General Service (LGS), into the following four classes: LGS, LGS Time of Use (GST), Large Power Service (LPS) and LPS Time of use (PST).

Regarding Rate Design, the Commission approves the AG's recommended Residential rate design proposal which includes leaving the Residential customer charge at its current level of $6.96. The Commission also approves the AG's proposal regarding the Residential 1st and 2nd block differential. The Commission rejects increasing demand charges for GST and PST customers and rejects a re-alignment of the LGT and LPT rates. The Commission also rejects increasing the proportion of revenues recovered through demand charges of LGS customers. The Commission finds that Staff's mitigation is appropriate and in the public interest.

The Commission also denies EAI's request to close its Optional Interruptible Service Rider (Rider OIS) to new customers and denies EAI's proposed Rider OIS replacement tariffs, the MVLMR and MVDRR Riders. The Commission also directs EAI to work with its Rider OIS customers and those customers taking service under the Co-generation tariffs to address options available in the MISO market for such demand response resources. The Commission directs EAI to file any proposed modifications of Rider OIS in a stand-alone docket where the Commission may more fully consider whether and what changes may be necessary to Rider OIS for EAI's participation in MISO.

The Commission adopts the Capacity Cost Recovery Rider (Rider CCR) as amended pursuant to the recommendations outlined in the Revised Surrebuttal testimony of Staff witness Elana Davis. The Commission also approves EAI's proposed MISO Rider, but, finds that to allow carrying charges on the over/under-recovery balances is inconsistent with prior treatment and rejects such treatment here.

The Commission finds that the costs of activated carbon and calcium bromide should be included in costs for recovery through Rider ECR. Also, the Commission finds that the method for providing any refunds subsequently determined in Docket No. 05-116-U be set at the time of the Commission decision in that docket.

The Commission approves the requested changes in the Large and Small Cogeneration Riders until such time as Demand Response is appropriately addressed as required for Rider OIS. The Commission also adopts EAI's recommendations, as amended at the hearing, to the EOFP and the Commission approves EAI's request to close RTP Pilot Rider.

The Commission approves, as appropriate, EAI's proposal to collect Rider PCA true-up costs of less than $1 million dollars. The Commission also agrees that AEEC's proposed allocation method for such costs is appropriate and directs EAI to amend its ECR as needed to effect that allocation for these costs.

Regarding Rider ANOR, the Commission approves EAI's proposed transition plan for the treatment of costs recovered under Rider ANOR and finds there is no evidence that EAI has included any accident-related costs (from the March 2013 accident) and will address treatment of those costs upon EAI's request for recovery. The

Commission finds that the Commercial Space Heating Rider should remain open but approves the amendments recommended by Staff.

Regarding a formula rate plan, to the extent EAI should make such a filing outside the context of a rate case, the Commission will give that filing appropriate consideration given the concerns raised by the parties in this Docket.

The Commission agrees with EAI that Standby Service rates have been historically and consistently tied to the LGS rate class and, thus, the applicable rate increase to the LGS rate class is appropriately applied to these rates.

Regarding other tariffs and riders, the Commission finds that EAI's current deposit policies are reasonable and rejects changes. However the Commission adopts the AG's recommendation to limit the increase in customer charges to no more than the cost of inflation as measured by the Consumer Price Index.

II. Procedural History

The parties to this proceeding are: EAI, Wal-Mart Stores Arkansas, LLC and Sam's West, Inc. (collectively Wal-Mart), Kroger Company (Kroger), the Federal Executive Agencies (FEA), the Hospital and Higher Education Group[1] (HHEG), Evergreen Packaging (Evergreen), the Arkansas Electric Energy Consumers[2] (AEEC), the Attorney General of Arkansas (AG), and Staff.

On March 1, 2013, EAI filed in the above-styled Docket its Application for a general increase in the rates it charges for retail electric service. In support of its

[1]Members of HHEG are the Board of Trustees of the University of Arkansas acting for and on behalf of the University of Arkansas System; Baptist Health; and the Arkansas Children's Hospital.

[2]Members of AEEC are ACME Brick Company; Arkansas Steel Associates, A. Tenebaum Company, Inc., Bibler Brothers, Inc., Chemtura Corporation, Commercial Metals Companies, Lion Oil Company; Producers Rice Mill; Riceland Foods, Inc., Evraz Stratcor, Inc., Georgia-Pacific LLC, and Clearwater Paper Corporation.

Application, EAI filed the Direct Testimony and Exhibits of its witnesses, Hugh T. McDonald, Kurtis W. Castleberry, Jay A. Lewis, Phillip B. Gillam, S. Brady Aldy, Corey A. Pettett, Gregory R. Zakrzewski, Donald J. Clayton, William R. Crean, Eric Fox, Julie M. Cannell, Samuel C. Hadaway, Jay K. Thayer, Kevin G. Gardner, Crystal G. Clark, and Jay C. Hartzell.

The Commission entered Order No. 5 on March 28, 2013, suspending EAI's proposed rates and setting the procedural schedule. The procedural schedule directed Staff and Intervenors to file Direct Testimony by August 2, 2013; EAI to file Rebuttal Testimony by August 26, 2013, Staff and Intervenors to file Surrebuttal Testimony by September 16, 2013; and EAI to file Sur-Surrebuttal Testimony by September 23, 2013. The parties were directed to file a detailed Joint Issues List by October 11, 2013, and to file any settlement agreement and supporting testimonies by October 14, 2013. Further, Order No. 5 set the evidentiary hearing on EAI's Application to begin on October 22, 2013. Additional public comment hearings were set on October 29, 2013, and November 7, 2013. Order No. 10 rescheduled the public comment hearing set for October 29, 2013, to October 30, 2013, and announced the locations of the public comment hearings.

Pursuant to the procedural schedule established by Order No. 5, on August 2, 2013, Wal-Mart filed the Direct Testimony and Exhibits of Steve W. Chriss and Kenneth E. Baker; Kroger filed the Direct Testimony and Exhibits of Neal Townsend; FEA filed the Direct Testimonies and Exhibits of Michael P. Gorman and James T. Selecky; Evergreen filed the Direct Testimony and Exhibits of Mike Elmore; AEEC filed the Direct Testimonies and Exhibits of David C. Parcell and Randall J. Falkenberg; and the

AG filed the Direct Testimony and Exhibits of William B. Marcus. Additionally, on August 2, 2013, HHEG filed the Direct Testimonies and Exhibits of Steven A. Ward, Mark E. Garrett, Chet Howard, Charles Mathis, David L. Millay, William E. Tinsely, Mark A. Kenneday, Larry Blank and Jessica Jeffries. Also on that day, Staff filed the Direct Testimonies and Exhibits of LaToya Johnson, Matthew S. Klucher, Judy Kay Lindholm, Regina L. Butler, Clark D. Cotten, Robert Daniel, William L. Mathews, Claude Robertson, Robert H. Swaim, Bill Taylor, Elana Davis, Katrina Owoh, Rick Dunn, Ronald Garner, and Jeff Hilton.

On August 26, 2013, EAI filed the Rebuttal Testimonies and Exhibits of its witnesses McDonald, Lewis, Clayton, Crean, Cicio, Fox, Hadaway, Thayer, Gardner, Cannell, Pickles, Hartzell, Aldy, Castleberry, David E. Hunt, Pettett, Zakrzewski, and Cartwright. On September 13, 2013, HHEG submitted the Surrebuttal Testimonies and Exhibits of its witnesses Ward, Tinsley, Jeffries, Mathis, Howard, Millay, Garrett, Blank, and Kenneday. On the same day, AEEC submitted the Surrebuttal Testimonies and Exhibits of its witnesses Parcell and Falkenberg. Also on the same date, Staff filed the Surrebuttal Testimonies and Exhibits of its witnesses Holly Tubbs, Butler, Cotton, Swaim, Daniel, Davis, Dunn, Johnson, Garner, Hilton, Owoh, Matthews, Lindholm, Klucher, Taylor, and Robertson. The AG submitted, on the same day, the Surrebuttal Testimony and Exhibits of William Marcus and FEA submitted the Surrebuttal Testimonies and Exhibits of its witnesses Selecky and Gorman.

On September 23, 2013, EAI submitted the Sur-Surrebuttal Testimonies and Exhibits of its witnesses Lewis, Aldy, Clayton, Cicio, Gardner, Hartzell, Fox, Hadaway, Cannell, Pettett, Hunt, Castleberry, McDonald, and Zakrzewski. On October 11, 2013, a

Joint Issues list was submitted by the Parties and, on October 18, the Parties submitted a Revised Issues List.

Order Nos. 14, 15 and 16 entered in this Docket on October 18, 2013, excused Kroger witness Neal Townsend, Evergreen Packaging, Inc. witness Mike Elmore, and Wal-Mart's witnesses Steve Chriss and Kenneth Baker from attending the evidentiary hearing. On October 21, 2013, Staff filed the Revised Surrebuttal Testimonies and Exhibits of its witnesses Davis, Lindholm, Matthews, Klucher, and Hilton. An evidentiary hearing on EAI's Application commenced on October 22, 2013, at the offices of the Arkansas Public Service Commission in Little Rock, Arkansas. The hearing recessed on October 25, resuming and concluding on October 30, 2013. Pursuant to Ark. Code Ann. § 23-2-103(b), the Commission heard public comments during the evidentiary hearing in Little Rock, Arkansas, and during public comment hearings in El Dorado, Arkansas on October 30, 2013, and in Batesville, Arkansas, on November 7, 2013. During the Little Rock evidentiary hearing, one person commented in opposition to EAI's proposed rate increases, the closure of the Optional Interruptible Service Rider (OIS Rider) to new customers, and to the cost allocation methodology used by EAI. During the public comment hearing held in El Dorado, Arkansas, four persons spoke in opposition to EAI's Application, with all four speaking against EAI's request to close its interruptible service rider and two specifically opposing EAI's cost allocation methodology. During the Batesville, Arkansas public comment hearing, seven persons commented on EAI's Application. Of those seven, all seven opposed closure of Rider OIS, and three opposed EAI's rate increase. Additionally, the Commission received a

total of seven email or telephone comments on EAI's Application. All seven opposed EAI's Application.

Though highly valued by the Commission, the "public comments" of utility customers do not rise to the level of substantial evidence upon which the Commission is required by law to base its decision. The Commission cannot base its decisions upon the public comments of utility customers without violating the due process rights of the utility or other official parties to the rate case proceeding. The rate case decisions of the Commission must be based upon substantial evidence of record and must fall within the rate case boundaries or parameters prescribed by the Constitution of the United States as interpreted by federal and Arkansas courts. Although not substantial evidence of record, the Commission does take such public comments into consideration in its efforts to reach a balanced rate case decision that is lawful and fair to both the utility and its customers. Public comments can certainly be helpful to the Commission regarding quality of service issues, as well as cost allocation and rate design issues that can be decided within a "range of reasonableness." However, even these issues must be supported by substantial evidence of record.

On November 5, 2013, Order No. 18 was entered granting EAI's oral motion regarding the submission of post hearing briefs. On November 15, 2013, EAI, FEA, Evergreen, AEEC, HHEG, Kroger, the AG, and Staff filed Initial Briefs. On November 22, 2013, Reply Briefs were filed by EAI, Wal-Mart, FEA, Evergreen, HHEG, AEEC, the AG, and Staff.

III. EAI's Rate Request

By its Application, EAI initially requested an increase in its current retail rate schedule revenues of $179,531,057. EAI's current rate schedule revenues are $1,003,387,493. EAI initially requested a retail rate schedule revenue requirement of $1,182,918,550 for a revenue deficiency of $179,531,057, for an overall increase in its Arkansas retail rates of approximately 17.89%[3]. Subsequently, EAI amended its request in its Sur-Surrebuttal Testimony, adjusting its proposed test year rate schedule revenues to $988,501,648, its retail rate schedule revenue requirement to $1,133,839,935 and its projected retail rate schedule deficiency to $145,338,325[4] resulting in an increase in its current Arkansas retail rates of approximately 14.70%[5]. EAI proposes to use a different method than currently approved in Docket No. 09-084-U (EAI's last rate case), to determine the Allowance for Funds Used During Construction rate (AFUDC). EAI also proposes to implement new depreciation rates. EAI also asks for recovery of payments made to trade industry associations such as the Electric Power Research Institute (EPRI), Edison Electric Institute (EEI), and the Nuclear Energy Institute (NEI). *Id.* at 6. EAI requests an increase in the annual Storm Reserve Account of $5.8 million as well as the inclusion of $20.1 million associated with the 2013 winter storm and implementation of a $4.3 million *pro forma* adjustment to the vegetation management program. *Id.* EAI also asks for changes to the following Rate Schedules and Riders:

1. Rate Schedule No. 10, Municipal Street Lighting Service ;
2. Schedule No. 12, All Night Outdoor Lighting Service, in order to reflect

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[3] 179,531,057 requested increase divided by $1,003,387,493 current rate revenues.
[4] T. at E1310 (Exhibit DEH-3 at 1).
[5] $145,338,135 requested increase divided by $988,501,648.

lighting product line and other revisions;

3. Rate Schedule No. 20. Standby Service Rider;

4. Rate Schedule No. 26, Additional Facilities Charge Rider;

5. Rate Schedule No. 29, Charges Related to Customer Activity;

6. Rate Schedule No. 34. Small Cogeneration Rider;

7. Rate Schedule No. 35, Large Cogeneration Rider;

8. Rate Schedule No. 36, the Agricultural Irrigation Load Control Service Rider, in order to simplify the billing calculation for that Rider;

9. Rate Schedule No. 38, Entergy Cost Recovery Rider, to incorporate revisions to Rider ECR to accommodate MISO market energy charges instead of the Entergy Energy Exchange fuel and purchase expenses and including in Rider ECR the costs of activated carbon and calcium bromide acquired and consumed by EAI in its fossil-fired generating units necessary to comply with the Environmental Protection Agency's Mercury and Air Toxics Standards;

10. Rate Schedule No. 41, Optional Interruptible Service Rider, to close the rider to new customers but to continue to offer the Rider to customers currently talking service thereunder in order to align with the Company's transition to operation in MISO;

11. Rate Schedule No. 49, Capacity Acquisition Rider, to implement a transition mechanism for the ownership costs for the Hot Spring Energy Facility (Hot Spring Plant) that are currently being recovered in Rider CA and phase out Rider CA and reflect these costs in base rates;

12. Rate Schedule No. 60, Extension of Facilities Policy; and

13. Rate Schedule No. 61, Tariff Governing the Installation of Electric Underground Residential Distribution Systems and Underground Service Connections.

Id. at 8.

Additionally, as noted above, EAI requests approval of the following new tariffs: a MISO Rider to recover MISO-related costs including the costs of membership and revenues and costs of EAI's participation in the MISO energy market; the Market Valued

Load Modifying Rider (MVLMR) and the Market Valued Demand Response Rider (MVDRR); a Capacity Cost Recovery Rider; and the Additional Facilities Rider—Governmental. EAI asks to eliminate the Experimental Market Valued Energy Reduction Service and the Experimental Energy Reduction Service Riders and the Pilot Real Time Pricing Service Rider. *Id.* at 9. EAI asks to reflect in base rates the costs currently being recovered pursuant to the ANO Capacity Cost Recovery Rider and the Government Mandated Expenditure Surcharge Rider. *Id.*

General Staff initially recommended a retail non-fuel Revenue Requirement of $1,122,555,829 and a Revenue Deficiency of $93,722,904. In the Revised Surrebuttal Testimony of Staff witness Jeff Hilton, Staff revises its recommendations for the retail non-fuel Revenue Requirement to $1,123,568,031 and a Revenue Deficiency of $109,968,597, an increase of $16,245,693 from Staff's Direct Testimony recommendation. Hilton Revised Surrebuttal at 2. Mr. Hilton states that a significant component of the Revenue Deficiency is due to incorporating the Capacity Acquisition Rider (Rider CA), Arkansas Nuclear One Unit 1 Interim Capacity Cost Recovery Rider (Rider ANOR), and the Government Mandated Expenditure Surcharge Rider (Rider GMES) into base rates. According to Mr. Hilton, these riders have combined total *pro forma* revenues of $48,321,880. *Id.*

In reviewing EAI's rate application, the Commission has carefully and fully considered all written testimony and exhibits of all parties, all evidence and testimony presented at the evidentiary hearing held beginning on October 22, 2013, the post hearing briefs of parties, and public comments. Due to the large number of witnesses, voluminous testimony, and lengthy transcript of the hearing, it is not possible to recite

in or summarize herein all evidence before the Commission. However, the Commission has relied on all evidence presented before it in making its decision on EAI's Application. The following discussion is generally set out in the order the contested issues were presented in the Revised Issues List filed by the parties in this Docket on October 18, 2013[6].

IV. Revenues and Billing Determinants

EAI witness Corey Pettett explains that Base Rate Revenues (revenues excluding those from riders) are calculated using the billing determinants based on six months historical data and six months of projected data. Mr. Pettett notes that this is the same method with the same *pro forma* adjustments EAI used to calculate the allocation factors. He testifies he calculated EAI's test year base rate revenues by multiplying the test year billing determinants by EAI's current base rates. T. at P378. *Pro forma* adjustments included the known and measureable changes for Large Industrial demand and usage in the test year and *pro forma* year as well as the appropriate weather adjustment (to avoid either overstating or understating current revenues). EAI also used the most current customer count data available as of December 31, 2012. Mr. Pettett testifies that the Base Rate Revenue *pro forma* adjustments are consistent with the method used in making *pro forma* expense adjustments and produce a reasonable expected Base Rate Revenue level[7]. T. at P379-382.

Upon review of EAI's proposed billing determinants, Staff witness Robert Swaim testifies he found no material differences in those as traced to EAI's records and

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[6] References to the Transcript are made as follows: T. at *** for transcript references of the evidentiary hearing; T.at P*** for references to Parties' prefiled testimony; and T. at E*** for references to Parties' exhibits.

[7] The calculations made for billing determinants and Base Rate Revenues were used in EAI's rate case Dockets Nos. 06-101-U and 09-084-U. T. at P382.

budgeted data. Mr. Swaim states that the only differences between Staff and EAI were in the adjustments each made to the base amounts which included adjustments for weather, other known changes, growth, and demand adjustments. T. at P1205-1206. Staff and EAI also disagree on adjustments made for vegetation management and the determination of billing units by class and resulting allocation factors.

Weather Normalization

EAI retained Eric Fox of Itron to review and provide a report of EAI's weather normalization methodology and resulting normalized sales estimates used by EAI in this rate case.[8] T. at P52. Itron's report is filed as EAI Exhibit EF-2. T. at E353. Mr. Fox states that EAI used MetrixND software to perform their weather modeling, which was developed by Itron. To calculate normalized sales, EAI first came up with average monthly usage by plotting on a linear graph, Residential and Commercial classes' monthly billed sales from January 2004 to July 2011. T. at P54-55.

The model aligned this monthly average usage to billing-month weather conditions which was measured as cooling-degree days (CDD) or heating degree-days (HDD). T. at P56. This gave EAI its Actual HDD and CDD amounts, developing normal HDD and CDD using daily Little Rock temperature data for a 20-year period (January 1992 through December 2011). Mr. Fox states that in recent years, temperatures have gotten warmer. For this reason he believes a 20-year period better represents current temperature trends as compared to a 30-year period historically used by the Commission and used as the basis for the development of the billing determinants in EAI's last two rate cases, Docket Nos, 06-101-U and 09-084-U. T. at P58. Given the hotter summer and colder winter of the test year, EAI witness Fox adjusts the summer

[8] Mr. Fox provided similar testimony in EAI's last rate case, Docket No. 09-084-U.

month sales downward and adjusts the winter month sales upward to bring them to normal. T. at P59. EAI's weather normalization resulted in an upward adjustment of 0.24% to normal residential sales and a downward adjustment of 1.80% to normal commercial sales. T. at E374.

Staff witness Swaim recommends rejecting Mr. Fox's use of a 20-year average of HDDs and CDDs as the definition of normal weather, arguing that the Company has not provided sufficient evidence to justify using a shorter period. T. at P1210. Mr. Swaim points out that EAI, in Docket No. 09-084-U, used a 15-year period for weather normalization believing it was more reasonable given that average temperatures appear to be increasing. As in Docket No. 09-084-U, Mr. Swaim recommends using a 30-year average which he says has been accepted by the Commission since the early 1990's. Mr. Swaim also testifies that the National Oceanic and Atmospheric Administration (NOAA) and the World Meteorological Organization (WMO) continue to use the 30-year average as the appropriate long-term weather standard for measuring weather occurrences. T. at P1208-1209.

EAI witness Fox disagrees with Mr. Swaim's position that it is more appropriate to use 30-years of data to weather normalize sales, saying more recent analysis shows that a shorter time period, such as 20-years, provides a more accurate view of the impact of weather on customers' usage. T. at P79. Mr. Fox refers to surveys by Itron, which show a decline from 43 percent in 2006 to 27 percent in 2013 in the number of utility respondents using a 30-year period. T. at P69.

The Commission finds that the weather adjustment prepared by Staff witness Swaim is reasonable, reflects prior Commission-accepted practice, and the Commission hereby adopts Staff's recommended weather adjustment.

Weather Adjustment for Large General Service Customers

AEEC witness Falkenberg argues that EAI makes no weather normalization adjustment for industrial customers. He notes that the Company makes a *pro forma* adjustment to some individual accounts, increasing the allocation factors for the LGS class. He argues that the Company provides no sound basis for selecting to adjust these few customers and provides no documentation of the basis for the *pro forma* adjustment. (T. at P665).

EAI witness Fox refutes this assertion, stating "there is no evidence that the industrial class in EAI's territory is weather sensitive." T. at P64. Mr. Falkenberg argues that industrial customers "generally have large cooling loads and with a proper analysis of the data, weather sensitivity can be measured." As an example, Mr. Falkenberg provides an excerpt from Georgia Power Company's integrated resource plan (IRP) that included cooling degree-days data as a billing determinant for the industrial class energy sales model. T. at P688. Mr. Fox acknowledges that the model contained weather sensitivity data, but says the model did not contain enough information to know whether the CDD variable was statistically significant nor had any meaningful contribution to the variation in monthly industrial sales. T. at P66.

In his rebuttal testimony, EAI witness Fox provides a chart for large industrial and small industrial customers, which plotted industrial average use versus average temperature. Mr. Fox concluded that "there was no observable relationship between

industrial use and average monthly temperature in either scatter plot." T. at P65. AEEC witness Falkenberg argues that Mr. Fox did not perform a proper analysis of the data. In his Surrebuttal Testimony, Mr. Falkenberg presents Fox's charts but adds a regression line which he says shows a positive correlation between industrial sales and average temperature. T. at P751. Mr. Fox responds, saying Mr., Falkenberg's positive correlation is most likely seasonal load variation and not the impact of temperature. T. at P75.

Staff witness Swaim also disagrees with AEEC witness Falkenberg's argument that industrial customers are weather sensitive and he points out that none of the other parties in this docket have proposed weather adjusting industrial loads. T. at P1236.

The Commission concludes that there is not sufficient evidence demonstrating weather sensitivity on industrial customer loads, therefore, the Commission rejects AEEC's request to weather normalize the industrial class.

Vegetation Management

EAI witness Brady Aldy proposes expanding EAI's vegetation management program by increasing the frequency of vegetation trimming in order to reduce customer outages. T. at P119. HHEG witness Steven Ward agrees that expanding the vegetation management program should reduce outages, but points out that consequently, energy consumption should increase. Mr. Ward therefore proposes that EAI make an upward adjustment to billing determinants and base rate revenues to account for the increases in billing determinants that would result from fewer outages. Without the billing determinants adjustment, Mr. Ward recommends that the Commission reject EAI's proposed expansion of the vegetation program. T. at P629.

Staff witness Swaim disagrees with Mr. Ward's proposal to adjust billing determinants, stating Mr. Ward offered no calculation for determining the amount of the adjustment, much less any evidence to support his recommendation. Mr. Swaim therefore recommends the Commission reject Mr. Ward's proposal to adjust billing determinants for vegetation management. T. at P1235. EAI witness Pettett, in his Rebuttal Testimony, also responds to Mr. Ward's proposal. Mr. Pettett states the adjustment "would not be known and measurable." He argues that it is unclear what factors could be assumed to be relevant in making any projections about how an expanded vegetation program would result in additional energy consumption. Mr. Pettett agrees with Staff witness Swaim and states that Mr. Ward's proposal is speculative and the Commission should reject it. T. at P421.

The Commission agrees with Staff and EAI and rejects HHEG's proposal to adjust billing determinants associated with an expansion of EAI's vegetation management program.

Determination of Billing Units by Class and Resulting Allocation Factors

To project the customer count for the *pro forma* year 2013, EAI substituted the December 2012 actual customer count for each of the twelve pro forma months. Staff witness Swaim disagrees with this method, saying it "often results in projections that are less accurate than actual results." For example, Mr. Swaim notes that the December 2012 budgeted residential customer count was 584,459 while the actual December 2012 residential customer count was only 581,511. T. at P1210. Mr. Swaim explains that Staff used a different method, which takes the most recent test year counts and grows them at the five-year compound annual growth rate. He states that this method applies the

historical growth (or decline) rate to the most recently available data to forecast the conditions that can be expected to prevail in the *pro forma* year.[9] T. at 1211. AG witness Marcus believes Mr. Swaim's method is reasonable on a "policy level" and agrees that it is necessary to develop an estimated number of customers for the *pro forma* year. T. at P1083.

EAI witness Pettett argues that Staff's method utilizes assumptions that are not reasonably known and measurable and should therefore be rejected by the Commission. He goes on to state that "Staff's adjustment is not based on anything that could reasonably be expected, much less known, to occur in the 2013 *pro forma* year and is likewise not based on expected consequences that are reasonably measurable." T. at P428. In the event the Commission determines that using Staff's forecasts, based on 2012 calendar year data through the end of 2013, is a reasonable methodology, then Mr. Pettett recommends that the Commission make two adjustments to Staff's methodology, modifying it to "reflect updated and more accurate data and to correct certain flaws in the methodology...." T. at P429. In his Sur-Surrebuttal Testimony, Mr. Pettett acknowledged that Staff updated its billing determinants to incorporate his recommended adjustments, which produced billing determinants almost identical to those of EAI. T. at 481.

The Commission finds Staff witness Swaim's use of historic billing determinant data in determining appropriate *pro forma* adjustments to be an accepted method which is reasonable and produces reasonable results. The Commission also finds that the use of the growth factor calculated based on five years' of historical data and applied

[9] Swaim notes that this method of using historical data to forecast the pro forma billing determinants was approved in EAI's last two rate cases. T. at P1243.

to known and measurable billing determinants is an appropriate and accepted method for purposes of setting rates and differs little from Mr. Pettett's own use of a year-end annualization. Both methods are employed to estimate the expected level of billing determinants which will occur in the future. In this regard, the Commission finds that the five year measure of growth impacts, using Mr. Swaim's model, more reasonably measures and more accurately reflects expected growth than does EAI's method, which takes the customer count from one isolated month and simply multiplies it by twelve.

V. Modified Balance Sheet Approach, Working Capital Assets, Current Accrued and Other Liabilities and Accumulated Deferred Income Tax

Generally

EAI and Staff used the Modified Balance Sheet Approach (MBSA). In Order No. 7 of Docket No. 84-199-U, the Commission directed Staff to use the MBSA, either in the absence of a lead-lag study or as a check on a lead-lag study filed by the utility. Simply stated, the MBSA requires all non-interest bearing utility assets that are necessary in providing utility service, and that are not considered elsewhere in the cost of service, to be included in a utility's rate base as Working Capital Assets (WCA). Additionally, all Current Accrued and Other Liabilities (CAOL) which are a source of funds should be included in the Company's capital structure at their appropriate cost.

The MBSA recognizes three basic facts: (1) a utility has investments in assets other than plant, which are necessary to provide utility service and on which a return should be allowed; (2) a utility has sources of funds, other than equity and long-term debt, which should be included in the capital structure; and (3) all liabilities are fungible sources of funds that are used to fund each and every asset of the utility. A corollary of this third point is that zero-cost liabilities should be placed in the capital structure in

calculating the utility's cost of capital. The rationale for placing all liabilities in the capital structure with the MBSA is that all liabilities are sources of funds used to finance the assets of the Company. No distinction can be made as to which asset a liability is funding because the funds provided by liabilities are fungible. Therefore, to determine the total cost of funds for the Company, the MBSA posits that the Commission cannot ignore CAOL.

Working Capital Assets

Clearing Accounts

Staff recommends excluding certain assets from EAI Working Capital Assets (WCA), and thus from rate base. Significantly, Staff recommends exclusion of the Undistributed Stores Expense and Undistributed Fuel Stock Expense. Staff witness Rick Dunn testifies that he did not include FERC Account 163, Stores Expense Undistributed (Stores) as that account is a clearing account, temporarily accumulating cost to be distributed to maintenance or CWIP. Mr. Dunn states that plant-related costs accumulate AFUDC and when completed, these costs are then transferred to plant and included in rate base. Mr. Dunn further contends, and Staff argues in its Initial Brief, that Staff's exclusion of undistributed stores expense is consistent with Order 10 in Docket No. 06-101-U, which was affirmed in *Entergy Arkansas, Inc. v. Ark. Publ. Serv. Comm'n, 104 Ark. App. 147, 169-170, 289 S.W.3d 513, 530 (2008).* T. at P1327-1328 and Staff Initial Brief at 1.

Similarly, in comparing EAI's Adjustment RB-4, coal inventory, to Staff's Adjustment RB-4, Mr. Dunn states that FERC Account 152, Fuel Stock Expenses Undistributed (FSEU) operates in a similar manner to a clearing account, temporarily

accumulating costs which are then cleared to fuel expense subject to exact recovery riders with associated carrying charges. T. at P1328-1329.

In rebuttal to Staff, EAI witness Gregory R. Zakrzewski states that the Commission should reject Staff's recommendation to exclude these accounts from the Material and Supplies (M&S) inventory and Fuel Inventory because: (1) these investments are not temporary in nature; (2) these accounts are constantly cleared and restocked; and (3) the balances in these accounts meet all the requirements of the MBSA in that they are not interest bearing, are necessary in providing utility service, and are not considered elsewhere in the cost of service study. T. at P238-251. Mr. Zakrzewski explains that Mr. Dunn's characterization of these accounts as "temporarily accumulating costs" is not accurate because these accounts continuously accumulate costs which are to be charged or cleared to CWIP and Operation &Maintenance (O&M). T. at P241.

Mr. Zakrzewski further contends the Commission's exclusion of undistributed stores expense in Docket No. 06-101-U is contrary to and inconsistent with (1) the treatment of these costs in other rate case proceedings including Docket Nos. 81-144-U, 82-314-U, 84-199-U, 84-249-U, and 96-360-U; and (2) the accounting treatment prescribed by the FERC USOA and generally accepted accounting standards. T. at P249.

In his Surrebuttal Testimony, Mr. Dunn continues to support excluding undistributed stores and undistributed fuel stock expense from WCA for the same reasons he explained in his Direct Testimony. T. at P1342. Mr. Dunn explains that these temporary accounts are primarily used to collect labor costs that are eventually moved to either CWIP or expense and that EAI is already recovering a normal level of

expense in base rates and any change in that level will be reflected in whatever base rates are approved in this case, so there is no reason to include these accounts in WCA. Staff argues that to allow balances reflected in these accounts to remain in rate base and earn a return would result in recognizing them for ratemaking purposes twice. Staff Initial Brief at 2.

In his Sur-Surrebuttal Testimony, EAI witness Zakrzewski continues to disagree with Staff's exclusion of the undistributed stores and undistributed fuel stock expenses account balances from WCA. First, he argues that these accounts are not temporary in nature. Second, he states that Staff's argument fails to recognize the fact that EAI is normalizing the balance in the undistributed stores account and undistributed fuel stock accounts in its adjustments to the WCA balances to a 13-month average. The balances in these accounts meet all the requirements of the MBSA in setting working capital, *i.e.*, the accounts are not interest bearing, are necessary in providing utility service, and are not considered elsewhere in the cost-of-service study, and therefore should be included in WCA. T. at P236-239.

Staff witness Dunn also eliminates all the balances in Account 184 (Clearing Accounts) from Staff's WCA. T. at P1327. Mr. Zakrzewski disagrees and contends that Staff's adjustment is not appropriate because the costs in these accounts: (1) were incurred to provide utility services to customers; (2) meet the working capital asset requirements because they are not interest bearing; and (4) are not included elsewhere in rate base. T. at P232-235.

Mr. Dunn argues that clearing accounts are designed to be temporary accounts which hold costs that are cleared (moved) each month to a final expense or capital

account. Staff explains that temporary costs incurred through the *pro forma* year which are ultimately expensed are being recovered in current rates just like any other expense, with any differences in amount being comprehended in the normal level of expense included in this case. Finally, he notes that the Commission, in EAI's last rate case, found Staff's treatment of clearing accounts to be appropriate and consistent with recent Commission practice. T. at P1340-1341.

The Commission finds that Staff's exclusion of the undistributed stores expense and undistributed fuel stock accounts from WCA is appropriate and consistent with recent Commission practice and, therefore, the Commission adopts Staff's recommendation. Additionally, the Commission agrees with Staff's treatment of the clearing accounts. EAI has not presented compelling evidence to warrant inclusion of these amounts. It is clear that "...these costs which pass through such temporary accounts are fully and appropriately recognized either as part of rate base assigned to *pro forma* or in the *pro forma* expenses to which they are assigned." *See* Order No. 10, Docket No. 06-101-U, at 59. The Commission agrees with Staff that to allow these account balances to remain in rate base and earn a return would result in recognizing them for rate purposes twice.

Wholesale Accounts Receivable

Staff witness Dunn eliminates $5,323,940 in the Wholesale Accounts Receivable because he states these accounts are non-retail. T. at P1327. EAI witness Zakrzewski disagrees and states that Staff's adjustment is not appropriate because the balances in these accounts are related to revenues that EAI receives under the Entergy Open Access Transmission Tariff. T. at P231-232.

Staff witness Dunn states he removed non-retail accounts receivable of $5,323,940 which represented revenue collected from transmission service wholesale customers. He argues that the receivables should be excluded from rate base because retail ratepayers should not be required to furnish a return on a receivable from wholesale customers. T. at 1340.

In his Sur-Surrebuttal Testimony, EAI witness Zakrzewski continues to include in WCA the accounts receivable balance for wholesale customers that take transmission service. He argues that retail ratepayers receive credit for these revenues as an offset to its revenue requirement, therefore, it is appropriate to include the accounts receivable balance of $5.6 million associated with these revenues in the cost-of-service study. T. at P235-236.

The Commission adopts Staff witness Dunn's adjustment to remove non-retail accounts receivable from WCA. The Commission agrees with Staff witness Dunn that retail customers should not be required to furnish a return on these receivables from wholesale customers as part of EAI's WCA.

Rate Case Expense

Staff witness Dunn did not make an adjustment to include in WCA a regulatory asset related to deferred rate case expense. Mr. Dunn states that rate case expense should not be included as a regulatory asset because (1) once a normal level of expense is determined and included in base rates, EAI begins receiving recovery; and (2) expenses are included at a normal level in base rates which provides an opportunity to recover these costs. T. at P1326-1327 and P1341-1342. AG witness William Marcus testifies that deferred rate case expense should not be included in rate base and that

unamortized rate case expense in rate base was rejected by the Commission in its order in Docket No. 04-121-U. T. at P1024 and P1341-1342.

In his Rebuttal Testimony, EAI witness Zakrzewski states that it is reasonable to allow EAI to establish a regulatory asset for rate case expenses. He further states that EAI is undergoing major structural changes which benefit customers and which drove the need for this case and associated rate case expenses. T. at P234.

The Commission agrees with the Staff and the AG that EAI should not include in WCA a regulatory asset for deferred rate case expense. The Commission also agrees with Staff and the AG that the Commission's finding on this issue is consistent with the Commission's treatment of rate case expense in prior rate cases and EAI has not presented compelling evidence or arguments here to justify departing from such treatment.[10]

Edison Electric Institute (EEI) and Nuclear Energy Institute (NEI) Prepayments

Staff witness Dunn and AG witness Marcus recommend that prepaid dues to EEI and NEI should be removed from WCA in the same proportion as the related operating expenses eliminated by Staff and the AG in their respective calculations of expenses. AG witness Marcus states that, even if the Commission rejects the AG's recommendation to disallow a greater amount of EAI's EEI and NEI prepayments, EAI's disallowances for EEI and NEI should be removed. T. at P1327, P1025. EAI witness Zakrzewski agrees with Staff's adjustment to the prepayment accounts for EEI and NEI dues but disagrees with the AG's adjustment. T. at P231, P235. .

[10] AG witness Marcus and Staff witness Dunn cite the Commission's order in in Docket 04-121-U as a rate case in which the Commission rejected the inclusion of unamortized rate case expense in rate base.

The Commission agrees with EAI, Staff, and the AG that the EEI and NEI prepayment should be removed from the rate case based on the same percentage as used for the expense adjustments approved in this proceeding.

VI. Current Accrued and Other Liabilities

Staff witness Rick Dunn includes in CAOL the debit balance of accrued interest on the Accumulated Provision for Property Insurance in the amount of $244,331, contingent liability accounts in the amount of $1,364,561 for taxes other than income taxes and for penalties for violations of FERC, NERC, and SERC regulations, and prepaid contributions in aid of construction (CIAC) and associated income tax gross-ups totaling $1,992,355. T. at P1330.

EAI witness Zakrzewski submits that the accrued interest balance should not be included in CAOL because the account upon which interest is accrued, Accumulated Provision for Property Insurance, is not included in CAOL. T. at P252. Zakrzewski further objects to inclusion of the contingent liability accounts because the expenses related to these liabilities are not included for rate treatment. T. at P253. Finally, EAI witness Zakrzewski objects to the inclusion in CAOL of the funds available in the Prepaid CIAC accounts, asserting that that "[t]he Company receives no benefit from these funds as they are specifically used to pay for the construction of specific facilities." T. at P254.

Addressing the accrued interest on the Accumulated Provision for Property Insurance, he included in CAOL, Staff witness Dunn notes that this amount is appropriately considered in "the determination of the Company's zero cost capital, notwithstanding the ratemaking treatment of the underlying account on which the

interest is accrued." T. at P1345. Dunn continues to include the contingent liability accounts as appropriately included in CAOL, irrespective of the rate treatment of the underlying expenses. Finally, addressing Zakrzewski's arguments as to the treatment of Prepaid CIAC accounts, Dunn asserts that EAI does benefit from these accounts as sources of zero cost capital until EAI actually expends those funds on that construction. T. at P1345.

Staff witness Dunn concludes that, "[a]t the heart of the three issues discussed above is the concept of fungibility, which Mr. Zakrzewski fails to recognize." This underlying concept is that these sources of funds are "of such a nature that one part may be equally interchangeable with another part of the whole . . . and can no longer be tied to a particular asset, liability, or expense. The concept of fungibility has been repeatedly recognized by the Commission as reasonable and proper in ratemaking." T. at P1346.

The Commission finds Staff witness Dunn has appropriately included these accounts as part of his CAOL calculation. As witness Dunn notes, the Commission has consistently recognized that all sources of funds available to the utility should be included in the determination of the overall cost of capital to that utility. As such, the rate treatment of the underlying source of funds available is not germane in considering that source of funds in the cost of capital. The Commission, therefore, adopts Staff's inclusion of these accounts as zero cost funds within the cost of capital.

FIN 48[11]

Staff witness Dunn has recognized, as a debit to CAOL, cash deposits of $75,977,000 held by the IRS[12] related to certain income tax positions taken by EAI on

[11] *Financial Accounting Standards Board Interpretation No. 48, Accounting for Uncertainty in Income Taxes – an interpretation of Statement of Financial Accounting Standard No. 109, now Accounting Standards Codification No. 740,* i.e. FIN 48. T. at P1330-1331.

its filed tax returns. Staff's recognition of this deposit is directly related to the position it takes with regard to the inclusion of the Accumulated Deferred Income Taxes (ADIT) related to those tax positions. T. at P1330-1331.

In his Sur-Surrebuttal testimony, Mr. Zakrzewski advises that "this component of CAOL is no longer an issue as those deposits were used to satisfy a large tax obligation in June 2013." T. at P296.

Interest Payable

Staff witness Dunn has included in Staff's CAOL balances, interest payable which is based on the Staff's recommended *pro forma* debt and interest information "using the average daily balance and the average lag days between interest payment dates." T. at P1331. EAI witness Zakrzewski agrees with Staff's calculation and Staff's use of its currently recommended *pro forma* debt and interest information as reasonable. However, witness Zakrzewski further advises that interest payable "should be adjusted based on the debt and cost rates ultimately approved in this case." T. at P332.

The Commission finds Staff's method of calculation of interest payable is appropriate and reasonable and that Staff's balance should be updated to reflect the Commission's findings in this Order as to the level and cost of debt.

Dividends Payable

Staff witness Dunn included $1,179,187 in CAOL for dividends payable on common stock. Dunn testifies that he used the actual EAI lag days to calculate the payable balance which was based on a normalized level of dividends paid, using the average dividend payments from 2008 through 2011. Witness Dunn noted that the level

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[12] Internal Revenue Service.

of dividends paid on common stock for 2012 was only $10 million, while dividends paid in the prior four years ranged from $24.9 million to $173.4 million. T. at P1331.

Alternatively, EAI witness Zakrzewski included $273,973 for dividends payable in CAOL. Witness Zakrzewski based his calculation on EAI's lag days and on the $10 million of dividends actually paid in the 2012 test year. Mr. Zakrzewski asserted that his use of the actual test year dividends paid for his calculation is consistent with the methodology reflected in EAI Exhibit JDW-3 to the Rebuttal Testimony of J. David Wright in Docket No. 06-101-U, which the Commission adopted in its Order No. 22[13] in that Docket. T. at P 255.

In his Surrebuttal, Mr. Dunn continued to support using a normalized level of dividends paid on common stock, basing his calculation on the four year average of dividends paid for the years 2008 through 2011 as "more representative of ongoing conditions." Mr. Dunn reflected the following dividends paid for 2008 through 2013:

Year	Dividends Paid (in millions)
2008	$ 24.9
2009	$ 48.3
2010	$173.4
2011	$117.8
2012	$ 10.0
2013	$ 15.0

T. at P1346.

[13] Docket No. 06-101-U, Order No. 22 at 6-7. T. at P255. Footnote at 30.

The Commission notes that EAI witness Zakrzewski, as support for his use of actual, 2012 test year dividends, relied on Commission Order No. 22 in Docket No. 06-101-U in which, he asserts, the Commission adopted the amount of dividends payable as reflected in EAI Exhibit JDW-3 to the Rebuttal Testimony of J. David Wright. The Commission finds that Mr. Zakrzewski misapplies the Commission's ruling in that Order in concluding that such Order defines the use of test year dividends paid as the basis for the appropriate calculation of related payables.

Order No. 22 was issued in response to the Arkansas Court of Appeals' reversal and remand of the Commission finding in its Order No. 16 regarding only the lag days to be used in the calculation of dividends payable. In its Order No. 16, the Commission adopted Staff's position that the lag days for payment of dividends should reflect those of EAI's parent company, Entergy Corporation, rather than those of EAI. EAI, alternatively, had used its own payment lag days in its calculation. The Commission, in its Order No. 22, issued its *Ruling On Remand* as follows:

> The Arkansas Court of Appeals reversed and remanded the Commission's adoption of Staff's stock dividends payable calculation and instructed the Commission to recalculate common stock dividends payable using EAI-specific lag data as urged by EAI. The recalculated results[14] ... [used] the exact same methodology, including number of decimal places, as in Staff Surrebuttal Exhibit DG-30, with only the change in CAOL to reflect EAI's 3.2 days dividend lag for common stock dividends payable rather than Entergy Corp's 38 days dividend lag.[15]

The Commission's Order No. 22 did not address whether the test year dividends paid, which were used in the subsequent payable calculation, reflected a normal and

[14] The recalculated results were shown on page 6 of Order No. 22 and were adopted by the Commission in that Order.
[15] Arkansas Public Service Commission Docket No.06-101-U, Order No. 22 at 5-6.

representative level. The Court's reversal and remand and the Commission's subsequent Order addressed only the appropriate lag days and, with only that adjustment, the Commission adopted Staff's CAOL.

The Commission finds that both EAI and Staff have appropriately calculated the common stock dividends payable balance using the actual lag days of EAI payments. The Commission also finds the 2012 test year dividends paid are not representative of the normal and expected level of those dividends, as evidenced by the prior years' payments, which are significantly greater than the test year payments. The Commission further finds that Staff's four-year average based on the 2008 through 2011 payments is more reflective of that normal, ongoing level. The Commission, therefore, adopts Staff's proposed level of dividends payable to be included in CAOL.

Department of Energy (DOE) Regulatory Liability

Staff witness Dunn has included the proceeds from the nuclear fuel storage cost litigation in CAOL in the amount of $553,171, noting that EAI has not confirmed that this account is one which earns interest. T. at P1347.

EAI witness Zakrzewski testifies that this account should be excluded from CAOL, noting that "[t] he Commission will ultimately decide whether or not this account will bear interest ... [and] ... [u]ntil such time as the Commission makes this determination, this account should be excluded from CAOL." T. at P333.

Mr. Zakrzewski concedes that the balance in this account does not currently earn interest. As such, the Commission finds that Staff witness Dunn is correct in recognizing this account as a source of cost free funds and is properly included in CAOL.

VII. Accumulated Deferred Income Tax (ADIT)

EAI witness Zakrzewski testifies that EAI "has excluded certain ADIT balances related to uncertain tax positions accounted for in accordance with FIN 48 from the ADIT included in its capital structure...[, as]...consistent with the Settlement Agreement approved by the APSC resolving the issues in EAI's last general rate case in Docket No. 09-0844." T. at P193.

Staff witness Dunn included, as a source of zero cost capital, $332,331,557 of ADIT not included by EAI, which related to FIN 48. FIN 48 requires that EAI recognize a tax liability for any tax positions it takes on its returns for which there is uncertainty that such positions will be sustained. T. at P1334. The amount of such liabilities reflects the incremental income tax effect of those uncertain positions taken. Mr. Dunn testifies that his recommendation to include the FIN 48 ADIT here "is congruent with the FERC Accounting Guidance directive issued on May 25, 2007 in Docket No. A107-2-000 ... [in which] ... [t]he FERC requires utilities to treat FIN 48 amounts arising from temporary differences between book and tax treatment as deferred income taxes for purposes of determining the reduction to rate base, effectively treating FIN 48 liabilities as cost free capital." T. at P1333-1334. HHEG witness Garrett also recommends that the FIN 48 ADIT balance should be recognized by the Commission for ratemaking purposes. T. at P1251.

Witness Garrett cites findings of the Public Utilities Commission of Texas (PUCT) in rate case filings[16] of its jurisdictional utilities, Oncor and EAI's affiliate, Entergy Texas, Inc. (ETI), in which Garrett participated and in which these balances were recognized by the PUCT for ratemaking purposes. T. at P1251 -1252.

[16] PUCT Docket Nos. 35717 and 39896, Oncor and Entergy Texas, Inc. (ETI), respectively.

Mr. Garrett asserts that "the utility clearly has the use of these additional funds, cost free, up until the time the IRS rules against the utility, which may or may not ever happen." T. at P1252 – P1253. Mr. Garrett acknowledges that, in the settlement reached in Docket No. 09-084-U, the FIN 48 ADIT balances were not included in the cost of capital but were excluded, with EAI's promise of refunds should it ultimately prevail in its tax positions. However, Garrett asserts that the process approved in the settlement was the opposite of that which should occur, noting that EAI has the use of these funds, now, as a source of cost free capital and should be recognized now, rather than "at some time in the future when the IRS decides the Company doesn't have to give the money back." T. at P1252 – P1253.

EAI witness Zakrzewski, in his Rebuttal testimony, clarifies that EAI not only eliminated the FIN 48 ADIT credit balances from the ADIT included in the cost of capital, but also removed the ADIT related to the Net Operating Loss (NOL) which its uncertain tax position generated. T. at P295-P296. Witness Zakrzewski asserts that, because EAI has been in an NOL position, with not enough taxable income to "be able to seek a refund of prior tax payments to obtain a cash tax benefit...," it has not benefited from the FIN 48 tax positions it has taken and thus not benefited from the ADIT as a cost free source of capital. T. at P296. Further, although the length of time EAI will remain in a NOL position is subject to many factors, EAI has projected its ADIT through the end of the *pro forma* year, resulting in the debit balance of the ADIT related to the NOL exceeding its FIN 48 credit balance ADIT. Mr. Zakrzewski recommends the Commission adopt EAI's exclusion of both balances from ADIT, "which effectively has

little to no impact on the ADIT balances in the cost of capital and of which EAI has recognized no cash benefit." T. at P296-P297.

Staff witness Dunn clarifies that the projected *pro forma* NOL ADIT asset is $348,394,337 and the FIN 48 ADIT liability is $336,054,006, both of which EAI excluded from ADIT and Staff included. The difference between the parties is $12,340,331. Dunn testifies that EAI receives cash benefit from the NOL and could receive more in the future as it applies the NOL to future years' earnings, noting that EAI expects to apply some $73.69 million of the NOL in the *pro forma* year. Further, given that EAI files its taxes as part of the consolidated return of Entergy Corporation, such NOL could be used to offset consolidated taxable income, providing EAI, through inter-company allocations, a cash benefit from its contribution to reducing consolidated income taxes. T. at P1351-P1352.

The Commission finds Staff's inclusion of both the ADIT credit balance for the FIN 48 tax positions taken by EAI, as well as the ADIT debit balance for the resulting NOL, to be consistent with prior Commission recognition of ADIT balances as a source of cost free capital. Further, EAI's assertions that it fails to benefit from these sources of cost free capital because of its expected ongoing NOL position is without merit. As noted by Staff, EAI projects that, even within the *pro forma* year, it will apply some $73.69 million of the NOL to its taxable income and there is no evidence to indicate that such tax benefits will not be available in the future. Nor is there evidence that EAI will not "ultimately prevail," as addressed by HHEG witness Garrett, in the tax positions it has taken and from which the FIN 48 ADIT was generated.

As to EAI's contention that its proposed treatment is consistent with the Commission's approval of the Settlement in Docket No. 09-084-U, the Commission notes that, in its Order No. 15 in that Docket, the Commission specifically advised that, in its approval of a settlement, it "acknowledges that parties make concessions during settlement negotiations."[17] While the Commission accepted this concession within the context of that Settlement, it finds that, within this contested proceeding, the evidence supports, as appropriate rate treatment, Staff's proposal. The Commission, therefore, adopts Staff's inclusion of both the ADIT asset related to the NOL and the ADIT credit balance related to EAI's FIN 48 tax position.

ADIT Related to Over/Under Recovery Balances for the Grand Gulf Rider

EAI witness Zakrzewski recommends rejection of Staff's inclusion of the 2012 year-end ADIT credit balance related to under-recovery of the Grand Gulf Rider (GGR). Witness Zakrzewski asserts that such balance should be zero, as the GGR is designed such that, "[i]deally, each month's collections would exactly equal costs..." and would, therefore, generate no ADIT. Mr. Zakrzewski asserts that Staff's treatment assumes that the GGR will consistently under-recover Grand Gulf costs. T. P303-P304. In support of his recommended zero balance for this ADIT account, witness Zakrzewski provided, in his Figure 3, on page 80 of his Rebuttal Testimony, a graph reflecting the over/under recovery balances for the GGR from 1999 through 2013 which indicates wide variations from year to year in either over-recovery or under-recovery. T. at P304.

Witness Dunn rebuts EAI's contention that, because of the GGR design, the over/under-recovery balance should be assumed to be zero and noted that the GGR "recognizes that there will be over-/under-recovery and is designed to capture it in

[17] Order No. 15, Docket No. 09-084-U at 4.

future filings. A review of the actual year end balances bears this fact out." Staff witness Dunn continues to recommend that the year-end balance for this ADIT account be included in the capital structure as consistent with his treatment of all other ADIT accounts, whereby, he has included all such "point-in-time" year-end balances. T. at P1348-P1349.

The Commission finds Staff treatment of this account reflects the normal and appropriate method by which ADIT should be measured for inclusion as a zero cost of capital, i.e. that the most currently known and measurable balance be used. EAI, however, provides, in this specific instance, evidence of the wide variations in the actual annual balances in the GGR over/under-recovery. Based on such evidence, EAI seeks a "zero" balance in this specific ADIT account, asserting that the GGR design would "ideally" collect exactly what is charged each year. The Commission, however, notes that the actual levels of the over/under GGR balances are known and, thus, the actual annual ADIT for the years shown can be measured. The evidence reflects that this specific ADIT balance will vary from year to year. Therefore, consistent with the concept of normalization which the Commission applied to the treatment of common stock dividends payable, the Commission finds that the amount to include in ADIT should reflect a normalized level, based on the information available. The Commission therefore finds that an appropriate balance for the ADIT, related only to the over/under-recovery of the GGR, should be based on the five-year annual year-end average of that ADIT for the years 2008 through the test year 2012.

ADIT Related to Deferred MISO Transition Costs

EAI witness Zakrzewski proposes to eliminate the ADIT balances related to the Deferred MISO Transition Costs, arguing that, because the Commission explicitly allowed no return on these deferred costs[18], to include that ADIT as a source of zero cost capital effectively results in EAI experiencing a "negative" carrying charge on such deferred costs through an overall lower return on the remaining rate base. T. at P306-P307.

Staff witness Dunn includes this ADIT in the cost of capital and rebuts the assertion that such inclusion results in a "negative carrying charge." Mr. Dunn notes that EAI not only recovers the MISO Transition Costs, but benefits from the zero cost capital from deferral of income taxes. By including those deferred taxes in the cost of capital, Staff, thus, simply captures that benefit for the ratepayers. Witness Dunn also asserts that, by referring to the impact to the remaining rate base, "Mr. Zakrzewski implies that ADIT related to assets excluded from rate base should not be included in zero cost capital..." and again ignores the fundamental concept of fungibility. T. at P1349-P1350.

The Commission finds Staff's treatment appropriate and consistent with the concept of fungibility and, therefore, directs inclusion of the ADIT related to the deferred MISO Transition Costs as a zero cost of capital.

Staff witness Dunn also testifies that, in response to Staff Data Requests, EAI provided a list of ADIT accounts it removed "because the underlying asset/liability generating the ADIT was excluded from rate base/capital structure." T. at P1333. The

[18] In Order No. 76 in Docket No. 10-011, the Commission did not approve recovery of carrying costs on the deferred MISO Transition costs. T. at P306.

Commission finds any such treatment by EAI violative of this Commission's consistent determinations related to the concept of fungibility and appropriate rate treatment of ADIT balances. The Commission, therefore, rejects all such adjustments to ADIT made by EAI and adopts Staff's proposed balances for any differences not specifically addressed herein.

VIII. Revenue Conversion Factor

The revenue conversion factor is the multiplier applicable to revenue deficiency to assure recovery of both the deficiency and applicable taxes and applicable expenses the increase in revenues (deficiency) will generate. The issues still in contention among the parties are the appropriateness of including forfeited discount revenues and the manufacturers' tax credit in the conversion factor.

Forfeited discount revenues or late payment fees include the amount of discounts forfeited or the additional charges imposed due to the failure of customers to pay their electric bills on time. EAI recommended including the forfeited discount revenues in the revenue conversion factor. Staff witness Johnson, AG witness Marcus, and HHEG witness Blank support EAI's recommendation. AEEC witness Falkenberg recommends forfeited discount revenues not be included in the conversion factor. Mr. Falkenberg states that "[b]ecause Residential customers have a very large percentage of late payments they are given the largest credit in the revenue expansion factor. The only way in which the Company's treatment makes sense is if one were to assume that late payments have no cost (or that paying on time provides no benefit.)" T. at P685. AG witness Marcus testifies that late payment revenues, similar to uncollectible accounts, are tied to revenues. He also notes that adding it to the conversion factor recognizes

that, as rate revenue increases, customers who pay their bills late will increase; thus, revenues for late payment charges will increase. T. at P1084-P1085.

The Commission agrees with Mr. Marcus' testimony and finds that forfeited discounts and late payment fees are tied directly to the level of revenues generated and, with increases to revenues provided, will also increase. The Commission therefore finds including a factor to represent these expenses within the revenue conversion factor is appropriate.

The manufacturers' tax deduction (MTD) is a federal tax deduction allowed on the income attributable to domestic production activities which include the generation of electricity, but not transmission or distribution. EAI witnesses Gillam and Hunt recommend excluding the MTD from the revenue conversion factor. Mr. Hunt testifies that it is inappropriate to include the MTD due to EAI's current Net Operating Loss (NOL) position. T. at P1387, 1463. Staff witness Johnson agrees with EAI's position and testifies "it appears that the net operating loss for EAI will carry forward to the *pro forma* year and beyond." T. at P1484. However, during questioning by HHEG, Staff witness Johnson agreed that Commission precedent is that the applicability of the MTD is tied to the incremental revenue resulting from increased rates and not whether or not a NOL exists. T. at 341-342. AEEC witness Falkenberg recommends the Commission continue to include the MTD in the conversion factor calculation, which is supported by AG witness Marcus, who notes the calculation is the same he has used in multiple Arkansas cases. T. at P722,P1086.

Mr. Marcus testifies that the difference between his proposed revenue conversion factor of 1.6160 and Staff's 1.6435 results in $27,500 for every million dollars

of revenue deficiency. T. at P1086. HHEG witness Blank additionally recommends inclusion of the MTD in the conversion factor but proposes including additional components in the revenue conversion factor's calculation. In support of including the MTD in the conversion factor, Dr. Blank testifies that such factor is used to account for federal and state income tax expenses associated with the revenue deficiency and that, if the MTD is excluded from the revenue conversion factor, EAI will over-collect for federal income tax. T. at P591.

The Commission finds that it is appropriate to include the MTD in the calculation of the revenue conversion factor. The deduction is directly tied to taxable income resulting from the jurisdictional revenue requirement and would be treated similarly to that of the state income tax rate. In addition, the Commission finds that the methodology proposed for its calculation by both Mr. Falkenberg and Mr. Marcus is reasonable and consistent with prior Commission treatment. Therefore, the Commission directs EAI to incorporate the MTD in the calculation of the revenue conversion factor using the methodology proposed by Mr. Falkenberg and Mr. Marcus.

IX. Operating Revenues and Expenses

Payroll Adjustment IS-16

EAI witness Zakrzewski testifies that EAI's proposed payroll level is based on the annualized wages and benefits, adjusted for known and measurable changes due to wage increases and changes in employee levels. T. at P213. Staff witness Taylor testified to Staff's *pro forma* level of payroll expenses and noted the following major differences with those proposed by EAI: (1) Staff used actual test year data, rather than projected data as used by EAI; (2) Staff used a five-year average expense ratio for payroll expense

while EAI used the test year ratio; (3) Staff removed costs related to employees of the Hot Spring Plant; and (4) Staff updated its employee count through May 2013. T. at P2757- 2758.

HHEG witness Garrett states that HHEG does not agree with EAI's proposed payroll adjustment because: (1) the increase to payroll expense is based solely on the nominal amount of pay raises awarded well after the test year; and (2) it fails to show that net payroll expense levels actually increased by the amount of the pay raises. T. at P1286- 1287. Mr. Garrett testifies that, first, annualization of EAI payroll costs as of April 2013 indicates that the ongoing level of payroll costs is actually lower than the test year level and that, with EAI's announced workforce reduction, payroll levels will be even lower going forward. HHEG's payroll adjustment reduces EAI's total revenue requirement by $7,425,463. T. at P1291.

In response to Staff's proposed payroll calculation, EAI witness Zakrzewski's responses can be summarized as follows:

(1) Employee Count through May 2013 – Because of EAI's Human Capital Management (HCM) initiative[19] and the related adjustment, an update using the headcount changes which have occurred in 2013, is not appropriate; rather the December 31, 2012, headcount used for the HCM adjustment should be used. T. at P264;

(2) Removal of Employees at the Hot Spring Plant – Payroll costs associates with these employees are included in Staff adjustment IS-18 and while Staff appropriately removes the associated headcount from the adjustment; Staff inadvertently makes the same adjustment a second time. T. at P264-265; and

[19] T. at P2386-2387.

(3) O&M Expense Ratio – Staff's calculation of the five-year average for the ratio is incorrect because it did not use the information provided in the updated response to Staff Data Request No. 35-1. Mr. Zakrzewski notes also that Staff's use of a five-year average in its adjustment is inconsistent with the calculations made in the last two rate cases. T. at P265-267.

With regard to HHEG Witness Garrett's recommendation to reverse EAI's *pro forma* payroll adjustment, EAI witness Zakrzewski states that HHEG's recommendation is unreasonable because 1) it does not factor in any changes which occur during the test year or *pro forma* period, and 2) it does not consider EAI's HCM adjustment already made by EAI. T. at P267.

In Revised Surrebuttal testimony, Staff witness Taylor testifies that he agrees with several corrections to his payroll calculation made by EAI witness Zakrzewski and has incorporated those corrections into Staff's proposed payroll levels. However, Mr. Taylor also testifies that, for purposes of normalizing payroll, he continues to use a five-year average of the O&M expense ratios for ESI and EOI as more indicative of a normal level of expense, while alternatively, he continues to use the test year O&M ratio for EAI payroll costs in light of EAI's HCM adjustment made to that test year. T. at P2767.

In Surrebuttal Testimony, Mr. Garrett responds to EAI witness Zakrzewski by stating that: (1) HHEG's calculations did factor in the changes which occurred during the test year and the *pro forma* year; (2) HHEG's annualization of payroll costs during the *pro forma* period indicated that actual payroll cost levels were dropping, not increasing as asserted by EAI; (3) EAI's HCM adjustment would need to be made in addition to HHEG's adjustment; (4) EAI's proposed HCM adjustment accounts for

savings that accrue from actual cost levels, not for savings that accrue from its *pro forma* increased payroll levels; and (5) if the Commission accepts the HCM adjustment, it would need to accept either HHEG's adjustment or Staff's adjustment first, because the starting point for the adjustment needs to be actual payroll cost levels, not EAI's inflated *pro forma* payroll cost levels. T. at P1316-1317.

In his Sur-Surrebuttal Testimony, EAI witness Zakrzewski testifies that Staff's proposal to use a five-year average is not necessary and unsupported by Staff testimony and should be rejected. Mr. Zakrzewski further testifies, however, that should a five-year average be used, it should be applied to all components of the payroll adjustment and not just ESI and EOI. T. at P334- 337. Witness Zakrzewski also testifies that he does not agree with HHEG's recommendation to hold payroll costs at test year levels, nor does he agree with the contention that no payroll adjustment is warranted. T. at P337-338.

The Commission finds that Staff's proposed adjusted *pro forma* payroll costs, as addressed by Staff witness Taylor in his Revised Surrebuttal Testimony, including the corrections outlined therein, appropriately reflect the normal, expected levels for payroll and payroll-related costs. The Commission finds that use of the five-year average for ESI and EOI better reflects the normal, average level of payroll costs which will be incurred for those costs going forward.

The Commission also finds, given use of the December 31, 2012, headcount for payroll in conjunction with the HCM adjustment, that Staff's use of test year data for EAI's payroll calculation results in payroll costs more representative of expected normal

levels. The Commission, therefore, adopts Staff's payroll adjustment as contained in Staff witness Taylor's Revised Surrebuttal Testimony.

Short-Term and Long-Term Incentive Compensation

As it did in Docket No. 06-101-U, EAI has again requested recovery of 100% of short-term and long term incentive compensation. T. at P2579-2601. In Order No. 10 of Docket No. 06-101-U, the Commission rejected EAI's request and adopted Staff's recommendation to disallow 50% of the short-term incentive compensation tied to financial performance and 100% of long–term stock based incentive compensation. *See* Order No. 10; Docket No. 06-101-U at 65.

After the holding in 06-101-U, EAI made some changes to its incentives and the Entergy Achievement Multiplier (EAM). EAI witness Gardner states that "[t] he EAM is used as a funding mechanism to ensure adequate funds exist to pay the incentives, but not as a performance target." T. at P2599-2600. Mr. Gardner testifies that EAI's and the other Entergy Operating Companies' compensation program design is consistent with the industry and its total compensation is at the median of peer companies. He states that employee compensation consists of base pay, annual incentives and recognition programs, and equity-based long-term incentives. In January 1, 2008, the Entergy Companies replaced the Entergy Achievement Multiplier (EAM), a composite of Entergy Corporation's earnings per share and operating cash flow, with new measures aligned with meeting operational-based targets. T. at P2579-2601.

Staff witness Taylor testifies that the results of EAI's third-party compensation studies and survey show that EAI's compensation structure is consistent with industry practice and that its compensation levels are also consistent with industry practice. Mr.

Taylor states that attracting and retaining qualified and competent employees is beneficial to ratepayers because it improves the quality of service and reduces the cost of electric utility service. Staff witness Taylor concludes that EAI's overall compensation levels are reasonable and he states that Staff does not recommend an adjustment to reduce the level of incentive compensation or stock-based compensation plans in this proceeding. Mr. Taylor acknowledges that Staff's recommendation on these expenses is different from previous treatment of these expenses but that EAI's level of compensation is reasonable and that an adjustment consistent with previous treatment is not warranted. T. at P2760-2762.

In opposition to EAI's request, AG witness Marcus testifies that EAI requests ratepayer funding for long-term incentives, equity awards, restricted share award and restricted stock awards of $1,292,096 plus recovery of stock options valued at $5,744,091, for a total amount of $7,036,187. T. at P996. Witness Marcus recommends that the Commission disallow all of the stock-based compensation, in the amount of $7,036,018, noting that such long term incentives are not a cash expense, will fluctuate in value, are concentrated in a few top level executives, and do not provide material value to ratepayers or balance the interests between ratepayers and shareholders. T. at P996-1005.

Mr. Marcus states that EAI's continued payment of this type of compensation, despite Commission previous disallowance in rates, indicates that it must provide value to EAI's shareholders and "the Company believes that it stands to gain by an amount that is greater than the cost it is likely to absorb through the disallowance." T. at P1002-1003. With regard to other state Commissions' treatment of stock-based

compensation, Mr. Marcus states that, at a minimum, Arkansas, Texas, and California have all disallowed this type of compensation. T. at P1003-1005. As shown in EAI Hearing Exhibits 1 and 2, only two of the 53 individuals eligible to receive stock options or long-term incentive compensation live in Arkansas; the rest live in other Entergy jurisdictions. Only a small percentage of the stock-based compensation EAI seeks to charge to EAI ratepayers goes to employees in Arkansas. AG Initial Brief at 5.

Regarding short-term incentive compensation, Mr. Marcus testifies that EAI includes $20,961,000 of test year expense ($16,176,000 included in O&M) and that a significant portion of EAI's bonuses are tied to profitability (i.e. total corporate operating income).

Mr. Marcus notes that, for EAI, there are 5 plans for short term incentives: Executive Annual Incentive Plan (EAIP) for Entergy Corp's most senior management, Selected Management Incentive Plan (SMIP) for selected management and key employees, Exempt Incentive Plan (EXIP) for exempt employees not qualified for other plans, Team Sharing Incentive Plan (TSIP) for most of EAI's other non-exempt and non-bargaining employees not eligible for other plans, and Team Sharing Plan for Selected Bargaining Units (TPSBU) for non-exempt bargaining employees. T. at P1006.

Mr. Marcus states that these plans are based on five types of goals - which include cost control, operational, safety, and financial. He states the goals related to cost control are also at least in part financially-related, as the Commission has found previously. He points out that the total size of the pools of earnable short-term incentives is determined by the EAM, which is a composite of Entergy Corporation's earnings per share and operating cash flow. T. at P1007.

Mr. Marcus recommends a sharing between ratepayers and shareholders for incentives based on financial goals and he proposes a method to measure the appropriate disallowances due to incentives with some tie to financial goals. He proposes that the Commission allow 100% of Teams Share (TSIP and TPBU); (2) 50% of EXIP, EAIP & SMIP incentives between minimum and target; 50% of financial and cost control for Cost Control, estimated at 25% of payments; and a 50/50 sharing for Executive Compensation T. at P1007. In his Table 8, Mr. Marcus provides his overall recommended allowed and disallowed short-term incentives. T. at P1008.

HHEG witness Garrett states that EAI included $16,172,753 of short-term incentive compensation expenses in EAI's cost of service. T. at P1257. Mr. Garrett further states that the Commission should apply the general rule followed by most states that incentive payments related to the financial performance of the company are excluded for ratemaking purposes. According to Mr. Garrett, most states exclude incentive compensation costs based on one or more of the following reasons: the payment is uncertain; many of the factors that significantly impact earnings are outside the control of most company employees and have limited value to customers; earnings-based incentive plans can discourage conservation; the utility and its stockholders assume none of the financial risks associated with incentive payments; incentive payments based on financial performance measures should be made out of increased earnings; and incentive payments embedded in rates shelter the utility against the risk of earnings erosion through attrition. T. at P1258-1260.

Mr. Garrett provides the results of an incentive survey of 24 Western States which show how those jurisdictions treat incentive compensation. T. at P1261-1266.

Mr. Garrett contends that ratepayers should bear no more than 50% of the short-term incentive costs, or if the Commission rejects his recommendation, at a minimum, the Commission should disallow the $977,814 of short-term incentive costs identified by EAI as directly tied to financial performance. T. at P1271-1272.

Mr. Garrett states that EAI seeks to include $7,036,188 in the cost of service for long-term and stock-based incentive compensation expense. T. at P1273-1274. Mr. Garrett's proposed adjustment removes 100% of the cost of the long-term incentive plan, and 100% of the stock-based awards because these plans are based entirely upon the financial performance of the Company.

In Rebuttal Testimony, EAI witness Dr. Hartzell states that HHEG and the AG ignore the role of stock-based incentive compensation as part of an overall, balanced, and reasonable set of compensation tools that can be used to attract, motivate, and retain talented executives, thereby benefiting both shareholder and ratepayers and they ignore existing empirical evidence that suggests that financial incentives can benefit other stakeholders, even a regulated utility. T. at P2697-2698.

In his Surrebuttal Testimony, Staff witness Taylor states that his conclusion on EAI's level of compensation and its composition has not changed from his direct testimony position.

In response to the Rebuttal Testimony of EAI witness Gardner, Mr. Garrett states that the reasonableness of EAI's total compensation level has no bearing on whether the Commission should include incentive compensation costs in rates. He also states that EAI's response to the survey results from other states again attempts to shift the focus away from policy considerations and that the survey results reveal that regulators

routinely exclude the costs of financial-based incentive programs from rates. T. at P1298-1304. In response to the direct testimony of Staff witness Taylor, Mr. Garrett states the Commission's prior disallowance of financial-based incentive cost was not based on whether the costs were reasonable, but on whether the costs provided direct, material and measurable benefit to ratepayers. He also argues that the Commission should not change its policy on incentive compensation based on Staff's claim that the amounts paid during the test year were reasonable. T. at P1310-1314.

AEEC witness Falkenberg disagrees with the Staff policy shifts regarding inclusion of incentive compensation. T. at P771-773.

In responding to HHEG witness Garrett, EAI witness Hartzell states that Mr. Garrett mischaracterizes his testimony as contingent upon Dr. Hartzell's expertise in ratemaking, rather than the impact and role of incentive compensation in this setting. Also, Dr. Hartzell states that Mr. Garrett's discussion of six factors that Mr. Garrett claims support his position on compensation demonstrates a lack of understanding of incentive compensation, as well as key financial concepts such as risks and hedging. T. at P1301-1308.

In Sur-Surrebuttal testimony, EAI witness Gardner responds to HHEG witness Garrett and AG witness Marcus on EAI's proposed recovery of incentive compensation by stating that Mr. Garrett relies on a Commission decision in Docket No. 06-101-U. However, EAI's most recent rate case in Docket No. 09-084-U was resolved by settlement and in that proceeding the Commission did not have the opportunity to consider, weigh and accept or reject the testimony of EAI witness Hartzell. T. at P2639-2640.

Regarding Mr. Garrett's statement that Staff has changed its position on incentive compensation, Mr. Gardner states that evidence, circumstances and policies evolve over time. T. at P2640. Mr. Gardner states that other companies (including HHEG members, the University of Arkansas System and Arkansas Children's Hospital) routinely utilize market surveys to set reasonable compensation for their employees. T. at P2644. Mr. Gardner states that it is EAI's position that using incentive compensation to attract and retain qualified employees is an expense in the provision of utility service, and, if the cost is reasonable, it should be recovered in rates. T. at P2646-2647. Mr. Gardner further contends that EAI's long-term incentive plans are designed to align the interests of EAI's customers with the benefit of a financially strong company. T. at P2647.

The Commission finds that EAI and Staff have failed to show that EAI's short-term, long-term and stock based incentive compensation provide ratepayer benefits to justify 100% inclusion in rates. The Commission agrees with both the AG and HHEG witnesses that most, if not all, of the short-term incentive costs are indirectly tied to financial performance through the EAM funding mechanism and, therefore, the Commission finds that ratepayers should bear no more than 50% of the costs. The Commission finds that $8,087,877 in annual short-term incentive costs, and all other related payroll costs,[20] should be removed from EAI's operating expenses in this proceeding.

With regard to EAI's stock-based and long-term incentive costs, the Commission agrees that EAI's long-term incentives do not provide material ratepayer benefits, or align the interest of shareholders and ratepayers because the focus of the incentives is

[20] A reduction to applicable payroll taxes is also required. *See* T. at P1008.

on stock prices and earnings per share rather on the provision of utility service. In this regard, the Commission finds no reason to deviate from its past policy of disallowing all of long-term stock-based incentive compensation. In making this finding, the Commission agrees with both the AG and HHEG that EAI's long-term and stock-based incentive plans are based entirely on the financial performance of EAI and therefore entirely benefit shareholders, rather than ratepayers. Therefore, the Commission finds that $7,036,188, and any other related payroll costs,[21] should be disallowed and removed from EAI's operating expenses in this proceeding.

Supplement Executive Retirement Plan

HHEG witness Garrett states that EAI provides supplemental retirement benefits to highly compensated individuals of the Company which are subject to certain Internal Revenue Code limitations (non-qualified plans). According to Mr. Garrett, EAI has the following three non-qualified retirement plans for highly compensated employees: the Pension Equalization Plan; the System Executive Retirement Plan; and the System Executive Continuity Plan. Mr. Garrett states that EAI's portion of the total amount of non-qualified supplemental retirements plan costs of $4,360,588 is $463,561 with the remainder being allocated from ESI ($3,627,736) and EOI ($269,291). T. at P1281-1282

Mr. Garrett proposes that the total cost of the non-qualified retirement plans should be removed from the cost of service and paid for by the shareholders, because these costs are not necessary for the provision of utility service, but are instead discretionary costs of shareholders designed to attract, retain, and reward highly compensated executives. He points out that the plan's costs benefit highly paid

[21] (1) A reduction to applicable payroll taxes may also be required. *Id;* AG Hearing Exhibits 1 and 2 reflect an increase in the disallowance of $242,866. T. at 1507 and AG initial Brief at 7-9.

employees receiving salaries of $250,000 per year or more. Mr. Garrett states that similarly to incentive compensation, this plan is not necessary for the provision of utility service, but its costs "are instead discretionary costs of the shareholders designed to attract, retain, and reward highly compensated executives." T. at P1282-1283 and P1285.

In Rebuttal Testimony, EAI witness Gardner contends that HHEG witness Garrett's approach is not appropriate because Mr. Garrett's justification for disallowance of non-qualified pension plan costs is not consistent with accepted market practice. Mr. Gardner also contends that the salary threshold referenced by Mr. Garrett is simply the IRS Code limit on the level of retirement benefits and is not intended to convey a threshold for reasonable plan design. T. at P2613.

In his Surrebuttal Testimony, HHEG witness Garrett responds to EAI witness Gardner by stating Mr. Gardner's position centers on compensation practice and benefits design rather than appropriate ratemaking considerations and the question is whether the Commission should force captive customers to fund extra benefits for highly-compensated employees. T. at P1314-1315.

In Sur-Surrebuttal, Mr. Gardner testifies that HHEG witness Garrett confuses the issue by co-mingling non-qualified pension plans costs with incentive-based compensation and that non-qualified pension benefits have no direct alignment to the shareholder, but, rather, are designed to attract and retain the talent needed by EAI. T. at P2649-2650.

The Commission adopts HHEG witness Garrett's recommendation that shareholders, and not ratepayers, should pay for the costs of EAI's supplemental

executive retirement plans. The Commission agrees that the question before the Commission is whether the Commission should force captive customers to fund extra benefits for highly compensated employees. The Commission's answer to that question is no. The Commission finds that these costs are not necessary to provide utility service, rather these costs are discretionary costs implemented by EAI and adopts HHEG witness Garrett's methodology regarding these costs. Therefore such benefits shall be disallowed for salary levels which exceed $255,000.

Hot Spring Plant

EAI completed the acquisition of the Hot Spring plant on November 30, 2012, and began collecting the ownership cost of the plant through the Capacity Adjustment Rider (CA Rider). In this rate case, EAI proposes to recover the estimated costs associated with the operation of the plant through base rates. T. at P1562, P214. Staff witness Lindholm proposes that EAI use the June 11, 2013 budget rather than the amount used in EAI's Application and remove $469,190 in test year expense associated with the replacement of hydrogen seals that will not take place before the end of the *pro forma* year. She further recommends removal of a maintenance cost adjustment of $211,804 for projected expenses that are also beyond the *pro forma* year. T. at P2786. Ms. Lindholm testifies that EAI agrees with the methodology Staff used. T. at P2797, P340.

AG witness Marcus testifies that approximately one-half of EAI's requested adjustment of $19,508,056 is for a long-term service agreement (LTSA) and AG witness Marcus testifies that approximately one-half of EAI's requested adjustment of $19,508,056 is for a long-term service agreement (LTSA) and that an additional

$469,190 of those costs were incurred in 2012. T. at P1013. Mr. Marcus recommends an amount that is $1,484,036 less that EAI's requested amount because EAI's estimated run times for the plant are too high. Mr. Marcus further recommends an additional adjustment of $368,023 to reduce non-LTSA maintenance costs to a three-year average level. Mr. Marcus states that the net difference between his adjustment and EAI's is $286,494. T. at P1013-1014. With regard to the recommendations of the AG, the Staff found that there were issues with the AG's proposal which suggests that the AG's level of recovery was insufficient. Ms. Lindholm testifies that the AG's proposed $17,737,526 level of recovery was too low and that as of July 31, 2013, the annualized expense was already at $19,582,500. T. at P2796-2797

The Commission finds that Staff's adjustment for the Hot Spring O&M expense is reasonable. Even though Staff made some reductions to EAI's proposed adjustment, EAI agrees with Staff's recommendation. The Commission finds Staff's recommended level of expense more indicative of that to occur based on the levels already reflected in the *pro forma* year and that Staff's proposed levels should be adopted.

Lake Catherine Plant-Unit 4

EAI witness Castleberry testifies that Lake Catherine Unit 4 was refurbished and is now projected to have a 55-year operating life through 2024. EAI is requesting that a regulatory asset be established to accumulate the unit's O&M expense, estimated to be $17.5 million over the next 4 years, to be amortized over a 10-year period beginning in January 2014. According to Mr. Castleberry, the unit will have value in the MISO market, providing operational flexibility, hedging against purchased power costs, and

reliability to meet MISO resource adequacy requirements. It will also enable EAI to meet its capacity requirements in the future. T. at P1559-1562.

Staff witness Jeff Hilton agrees with EAI's request for recovery of related O&M expenses but not the full amount requested by EAI. Mr. Hilton found that, based on Staff's examination of the test year and previous three years O&M expense, an additional $1.1 million of recurring O&M expense requested is not necessary. Mr. Hilton testifies further that, with costs incurred outside the *pro forma* year, it is not appropriate to include any amortization of the regulatory asset in rates as part of the current case but the costs should be deferred for recovery within EAI's next rate case. Mr. Hilton also recommends that no carrying charges should be accrued on the deferred O&M expenses. T. at P2827-2830.

AG witness Marcus is concerned that EAI will use regulatory asset treatment to guarantee a dollar for dollar recovery and, therefore, Mr. Marcus recommends the Commission adopt the normalized amount to extend the life of this unit and approve the increase of $4,371,000. T. at P1014-1015. Mr. Marcus also recommends an adjustment to 2012 per book non-fuel expense to recognize the lower pre-2012 expenditures and the lower expenditures expected in the future. Using a 4-year average, Mr. Marcus recommends a reduction in EAI's requested Non-Fuel Expense of $1,188,000. T. at P1015-1016.

EAI witness Castleberry disagrees with the AG's proposed adjustments because Marcus's analysis is based on projected incremental costs and is not representative of total O&M cost projections. P. at P1640-1641.

In Surrebuttal Testimony, Staff witness Hilton testifies that Staff and EAI are in agreement on Staff's recommendations. With regard to the AG's recommendations, Mr. Hilton testifies that, while the Staff's adjustment addresses some of the same concerns expressed by the AG, Staff favors its adjustment over the AG's because it recognizes that the unit remains economically preferred over potential alternatives. T. at P2840-2841.

The Commission adopts the Staff recommendation for Lake Catherine Unit 4. The Commission finds that the adoption of Staff's recommendations addresses some of the same concerns expressed by the AG. First, under Staff's recommendations, through the establishment of a regulatory asset, there will be no recovery in base rates in this rate case because the expenses occur outside of the *pro forma* year. Second, Staff found that the additional $1.1 million of O&M expense requested by EAI is not necessary. Third, Staff recommended that no carrying charges be accrued on the deferred O&M expenses. Finally, as recommended by the AG, Staff has made substantial reductions in O&M expenses for other EAI power plants being retired in the *pro forma* year in this case. The Commission therefore finds that the Staff's adjustment is appropriate.

Ouachita Plant

For this adjustment, Staff witness Lindholm did not agree with EAI's normalization of maintenance costs because EAI included amounts outside the *pro forma* year. Staff included a normalized level of costs based on the years 2009 through 2012. T. at P2786. Staff witness Lindholm explains that FERC ordered EAI to reimburse Entergy Louisiana, LLC (ELL) and Entergy Mississippi, Inc. (EMI) upon EAI's withdrawal from the System Agreement on December 18, 2013. Staff witness Lindholm states that Staff's adjustment corrects an error discovered by EAI which

increases EAI's amount of $2,724,815 by $1,373,052. T. at P2786-2787. EAI witness Zakrzewski states that Staff correctly updated the cost in the adjustment to reflect the amount of expected expenses based on the latest available data. T. at P276.

Ms. Lindholm testifies that EAI did not oppose the methodology that Staff used for its adjustment and EAI states that it agrees with Staff's adjustment. T. at P2797-2798.

AG witness Marcus testifies that he did not oppose the concept of the adjustment. While EAI calculated 2009 maintenance for the entire plant (units 1-3) subtracting one-third for the sale of Unit 3 to ELL, Mr. Marcus proposes to use the maintenance costs for the two remaining units, which results in a reduction of the maintenance costs by $54,845. T. at P1012, P1090.

There appears to be no major differences between the parties on this proposed adjustment. EAI accepted Staff's proposed recommendation for this adjustment and the AG's proposal would not materially change Staff's recommended level. The Commission finds that Staff's proposed methodology for computing this adjustment is reasonable, as is the resultant level of costs included, and the Commission, therefore, adopts Staff's proposed adjustment.

Vegetation Management Adjustment

EAI witness Aldy proposes two adjustments to the amount of test year expense for vegetation management (VM) costs: a one-time upward adjustment of $2 million to reflect the difference in test year expense and the three-year historical average; and a $2.3 million increase to increase the cycle time by which EAI trims certain circuits that have a greater exposure to vegetation-related outages. The increased trim cycle would

allow for an average trim cycle of 3.5 years for high density circuits, 4.5 years for medium density circuits, and 5.5 years for low density circuits, which would bring the overall average cycle time to just over 5 years. T. at P115-121, P149-151, P173-176.

Staff witness Robertson's adjustment excludes the component of EAI's proposed increase in VM costs related to EAI's proposed revised trim cycle. Mr. Robertson testifies that, while EAI's proposed plan to reduce the trim cycle is reasonable, he has included only the adjustment for the use of the three-year historical average. Mr. Robertson contends that EAI has indicated that it will not implement it VM plan until 2014, making the proposed costs not known or measurable by the end of the *pro forma* year. T. at P2806-2808 and P2812-2814. EAI witness Aldy testifies that, although the 2014 trim plan will not be in effect until January 1, 2014, the contracts that govern the work were signed in 2012, and the actual circuits to be trimmed have already begun to be identified in 2013. T. at P173-176.

AG witness Marcus testifies that his calculated recommendation was lower than EAI's because he used: (1) lower unit costs and a more limited scope of work on low-density line; and (2) a lower calculated amount to take into account the potential that the higher unit costs in 2012 may have resulted from fewer trims in prior years. Further, his adjustment captures the fact that storm years, from time to time, cause tree trimming spending to be reduced relative to normal years. Mr. Marcus concludes that the Commission can: (1) agree with the Staff that the program is not known and measurable, or (2) adopt the AG's calculation of $17,000,000 and an adjustment of $2,601,000 to EAI's original amount based on recorded 2012 spending. The AG's calculation does not include EAI's increase in costs per mile of 3.5%, maintains the

status quo in the low-density areas, and ramps up trims as EAI proposes in high and medium density areas. T. at P1009-1012. EAI witness Aldy responds to the AG stating that EAI does not agree with the AG that the 2012 costs should be used as the baseline because the VM cost varies from year to year. T. at P1009-1012, P1075-1078.

HHEG witness Ward recommends adjusting billing determinants to reflect the impact of EAI's proposed VM program and disapproving trim cycle changes until the impact to revenue from fewer outages is determined. T. at P629. In responding to HHEG witness Ward, Mr. Aldy states that Mr. Ward offers no basis upon which to calculate Mr. Ward's proposal and cost impacts. T. at P629.

The Commission finds that Staff witness Robertson's recommendation to increase test-year VM expense based on a three-year average of known and measurable costs is reasonable and more reflective of expected costs within the *pro forma* year. The Commission agrees with Staff that EAI was unable to prove or provide compelling evidence that the new VM plan and revised contracts will begin before the end of the *pro forma* year and that the proposed costs are known and measurable. Also, Staff's use of a three-year average for its adjustment also addresses EAI's response to the AG that VM costs vary from year to year and EAI's statement that EAI supports Staff's recommendation to use the three-year average VM costs, consistent with the use of historical averages in prior rate cases. The Commission's finding in this docket does not preclude EAI from improving or changing its trim cycle and any costs associated with changes in EAI's trim cycle would be captured in future rate cases.

EEI and NEI Dues

EAI witness Aldy recommends recovery of EEI dues, adjusting out the percentage related to lobbying. After removing these costs, EAI seeks to recover $233,511 which represents 71.94% of the total amount paid during the test year. Mr. Aldy notes that his Direct Testimony complies with Order No. 10 in Docket No. 06-101-U in EAI's last rate case in which the Commission directed EAI to file, with any future rate case, a cost analyst reflecting all customer benefits of industry organization membership over the past two years.[22] T. at P97-104. Staff witness Johnson agrees with EAI's proposed adjustment with its exclusion of amounts related to lobbying by EEI. T. at P1478-1479.

AG witness Marcus states that EAI paid $324,590 to EEI for dues. Noting that EEI no longer provides a publicly available breakdown of its expenditures, Mr. Marcus has relied on previously obtained information related to the percentage of EEI spending which is made for activities for which ratepayers should not be charged (legislative advocacy – i.e. lobbying). Mr. Marcus states that EEI has stopped issuing detailed information on its budget, previously available under the auspices of the National Association of Regulatory Utility Commissioners (NARUC). Along with the $79,044 eliminated by EAI, Marcus proposes that an additional $84,652 be removed from O&M for EEI dues for a total EEI disallowance of $163,696. T. at P1018-1020.

According to EAI witness Aldy, AG witness Marcus agreed to inclusion of 100% of Southeastern Electric Exchange (SEE) dues but only 52.8% of EEI dues. The AG recommends additional reductions for advertising (2.3%) and public relations (2.9%) based on the 2009 EEI Budget (as addressed in Docket No. 10-067-U), a 16.5%

[22] Docket No. 06-101-U, Order No. 10 at 77.

reduction for "Regulatory Advocacy" based on the 2005 EEI Budget, and disallowance of 75% the of "Industry Issues" portion of the EEI Dues. T. at P153. Mr. Aldy testifies that the AG's 75% disallowance apparently was made based on updated information EEI provides to EAI regarding that portion of EEI activities which are related to lobbying and are, therefore, not deductible. However, according to Mr. Aldy, the AG did not update all the costs related to EEI's updated information. As to the AG's disallowance of advertising and public relations based on past years' data, Mr. Aldy notes that there is no way to know if the percentages applicable to past years has any relation to current costs and should not be used. EAI applied the EEI-supplied percentages to EAI's test year dues to determine the amount of EEI dues EAI excluded for lobbying. T. at P153-155.

Staff witness Johnson states that she does not agree with AG witness Marcus' recommendation regarding EEI dues. Ms. Johnson further states that the AG's adjustment for EEI is based in part on outdated information. Ms. Johnson contends that EAI has demonstrated that EEI provides net benefits to ratepayers and to EAI on evolving industry issues. Staff continues to recommend that EAI be allowed to recover the EEI dues, reduced only by the portion related to lobbying, or $79,044. (Johnson Surrebuttal 3). The AG continues to recommend its adjustment for EEI dues. Mr. Marcus states that EAI has not borne the burden of proof on EEI dues because, in all likelihood, EAI does not possess adequate information to do so because of EEI's lack of transparency. T. at P1078-1082.

Staff and EAI agree on including 100% of SEE dues and reducing EEI dues $79,044 for lobbying. EAI continues to disagree with the AG's $84,652 additional disallowance for EEI dues. T. at P178-180.

The Commission adopts EAI's and Staff witness Johnson's recommendation on EEI dues. While the Commission finds that EAI has substantially complied with the Commission's directives on EEI dues in in Docket No. 06-101-U, the Commission heeds the AG's concerns regarding the level of detail provided for expenses sought to be included in rate base. In future rate cases, the Commission expects EAI to take additional steps to validate its EEI dues, pertaining to lobbying and other "below the line" expenditures, if EAI seeks to pass these costs on to ratepayers.

With regard to NEI dues, EAI witness Thayer has excluded portions related to lobbying expenses and additionally cites multiple non-quantifiable benefits of NEI membership, including annual savings of $312,200 for EAI's "Risk Informed In-Service Inspection" program developed by NEI. T. at P2727-2733. Staff witness Johnson agrees with EAI's exclusion of amounts related to lobbying by NEI. T. at P1478-1479.

AG witness Marcus notes that NEI engages in significant additional lobbying activities[23] hidden in its support of multiple organizations. (Exhibit WBM-10). Marcus recommends that ratepayers only fund 50% of NEI dues (rather than the 75.4% requested by EAI), recognizing the technical role NEI plays but opposing the rampant promotional activities in which it engages. Mr. Marcus recommends an additional disallowance of $172,584 (total disallowance of $339,733). T. at P1020-1024.

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[23] Mr. Marcus cites NEI's six- month public opinion polls on nuclear power; its program to teach children living near Chernobyl not to fear nuclear energy; or promotional advertising on nuclear power.

EAI witness Thayer responds to AG witness Marcus' proposal to disallow an additional $172,584 in NEI dues on the basis that NEI's public relations activities should not be paid by EAI's customers. In stating his opposition to the AG's position, Mr. Thayer testifies that Mr. Marcus: (1) presents no basis for his proposed disallowance of one-half of NEI dues; (2) only identified a few publications and activities for which the AG believes EAI should not pay without any explanation of his proposed disallowance calculation; (3) fails to take into account the valid need for educational materials concerning nuclear power and the tangible benefit to ratepayers; and (4) recommends an adjustment which is arbitrary and unsupported by any analysis. EAI continues to support recovery of 75.4% of NEI dues, with 24.6 % not recovered in rates. EAI Exhibit JKT-3 is a copy of the 2012 lobbying expenditure percentages as calculated by NEI. T. at P2447-2455.

In Surrebuttal Testimony, Staff witness Johnson states that she does not agree with AG witness Marcus' recommendation regarding NEI dues. Ms. Johnson further states that the AG's adjustment for NEI is simply a sharing between ratepayers and shareholders and has no quantitative basis. Ms. Johnson contends that NEI provides net benefits to ratepayers and to EAI on evolving industry issues. Staff continues to recommend that EAI be allowed to recover NEI dues, reduced only by the portion related to lobbying. T. at P1485. The AG continues to recommend its adjustment for NEI dues. Mr. Marcus testifies that NEI is a policy-oriented organization that engages in all kinds of advocacy, public relations, and advertising and other activities. Mr. Marcus further testifies that a 50% allowance is generous, given NEI's flagrant political

advocacy. However, Mr. Marcus states that he recognizes that NEI's work has technical aspects that reduce the cost of existing nuclear plants. T. at P1078-1082.

As with EAI's EEI dues, the Commission adopts EAI's and Staff witness Johnson's recommendation on NEI dues. Like the Commission's finding on EEI dues, the Commission finds that EAI has substantially complied with the Commission's directives on NEI dues in the Commission's order in Docket No. 06-101-U. The Commission again notes the AG's concerns regarding the level of detail provided for expenses sought to be included in rate base. In future rate cases, it is incumbent upon EAI to take additional steps to calculate NEI's lobbying and "below the line" expenditures if it seeks to pass on these costs to ratepayers.

Rate Case Expense

Staff witness Johnson states that EAI used three years in determining annual rate case expense, but did not provide any support for its use of three years. T. at P1480. She recommends using a 3.5 year interval as representative of historical activity, which would result in a $386,286 annual level of rate case expense. EAI witness Zakrzewski contends that, if the Commission accepts Staff's recommendation regarding rate case expense, then additional expense must be added to Staff's adjustment to account for internal ESI support services and that rate case costs must be treated as a regulatory asset and amortized over a three-year period. T. at P237-238, P319-320.

In Surrebuttal Testimony, Staff witness Johnson states that Staff has revised its adjustment to include ESI costs in its estimate of rate case costs as addressed by EAI. However, Ms. Johnson continues to maintain that the rate case expense adjustment should be included an annual level of expense based on a 3.5 year normalization period

in revenue requirement as a normal, annual level of expense based on a 3.5 year normalization period. T. at P1479-1480, P1486.

The Commission adopts Staff's position on the rate case expense adjustment. EAI did not provide any support for its use of 3 years for the normalization period for rate case expense and therefore the Commission adopts Staff recommended 3.5 year normalization period. The Commission additionally rejects EAI's proposal to create a regulatory asset for these costs for future recovery, finding that prior Commission treatment more appropriately includes a normal level of these expenses in the revenue requirement.

Human Capital Management Initiative

HHEG witness Garrett testifies that EAI will eliminate approximately 800 positions as a result of its Human Capital Management (HCM) Initiative. He contends that payroll levels will be lower, not higher, when new rates go into effect. T. at P1290-1291. Staff contends that some level of estimated costs and savings should be included in base rates "because the HCM initiative is expected to produce net savings in 2013. Staff Initial Brief at 9.

EAI witness Zakrzewski states that EAI announced its HCM initiative after it filed its rate Application. He states that the HCM initiative will produce actual savings that will not be known until the organizational design is finalized and employees are designated to fill available positions. He states that EAI has estimated the net annual operations and maintenance savings it expects to achieve over the next three years and that the Company is requesting Regulatory Asset treatment of the costs associated with

achieving these savings. He states that EAI requests that it be allowed to amortize these costs over three years. T. at P229-230.

In his Surrebuttal Testimony, Staff witness Taylor states the HCM initiative is expected to produce net savings starting in 2013 and, therefore some level of estimated costs and savings should be included in base rates at this time. He agrees that a regulatory asset should be authorized to capture the actual costs related to the HMC initiative, subject to certain conditions. First, costs should be initially offset by the actual savings of the initiative and any remaining net difference between the actual costs and savings be addressed in EAI's next rate case. Next, EAI must provide to Staff a detailed report and supporting documentation of the Arkansas-specific costs, savings, and final payroll changes. Mr. Taylor also recommends that the regulatory asset should not accrue any carrying charges and that, consistent with Staff's recommendation for rate case expense, the HCM costs should be amortized over 3.5 years.

Finally, Staff witness Taylor agrees that the employee headcount as of December 31, 2012, is the proper starting point both for the payroll adjustment and for computing the HCM adjustment. Mr. Taylor testifies that it very important to note that the bottom line associated with the HCM initiative is the expected net annual savings that ratepayers will receive which is the difference between the gross annual O&M savings less the costs to achieve these savings. He recommends that EAI should provide Staff a detailed report with documentation for each year until all costs have been incurred and all changes in payroll have been finalized. Mr. Taylor reiterates his recommendation that the regulatory asset should not accrue any carrying charges and that the costs be amortized over 3.5 years. T. at P2769-2771.

AG witness Marcus agrees that the cost reductions should be captured as soon as possible. Mr. Marcus testifies that it is unclear if the HCM is a good deal for ratepayers. If the Commission approves the HCM, the AG recommends not including severance costs as a regulatory asset and, instead, that the costs should be normalized, with averaging over 3.5 years based the interval between this rate case and EAI's last rate case. T. at P1092-1094. AG witness Marcus recommends rejecting EAI's proposed HCM adjustment, or in the alternative, include an HCM-specific adjustment without establishing a regulatory asset. He also recommends averaging the projected severance costs over three and a half to four years. T. at P1052, P1092. HHEG witness Garrett recommends that, if the Commission intends to accept the HCM adjustment, the Commission should accept either HHEG's or Staff's payroll adjustment because the starting point for the adjustment needs to be actual payroll cost levels, not EAI's *pro forma* payroll cost levels. He also recommends that the starting point for the HCM adjustment should be the actual December 31, 2012, test year payroll. T. at P1317.

The Commission finds that ratepayers will benefit by recognizing the HCM adjustment as proposed by Staff and finds that a regulatory asset should be established subject to the following requirements:

1. That costs should be initially offset by actual savings and the remaining net difference will be addressed in EAI's next rate case;

2. That EAI will file in this Docket, upon conclusion of the HCM initiative, a detailed report and supporting documentation of the Arkansas-specific costs, savings, and final payroll changes; and

3. The regulatory asset will not accrue carrying charges and a 3.5 year amortization period will be used.

System Planning and Operations

AEEC witness Falkenberg addresses the services that EAI will obtain from Entergy Services, Inc.'s (ESI's) System Planning and Operations (SPO). Mr. Falkenberg recommends that, unless EAI can demonstrate that the sole source award to SPO was the least cost alternative, the Commission should reduce EAI's cost estimate by 20% or $2 million for the test year as an incentive to seek out bids from third party service providers. T. at P785-786. EAI witness Castleberry testifies that ESI is well experienced with EAI's electric system and this experience has already been shown to be vital as EAI moves toward integration with MISO. Mr. Castleberry further testifies that EAI will continue to evaluate the services provided by ESI and there is no need for the Commission to order EAI to analyze the impacts of changing or replacing the services provided by ESI. T. at P1686.

AG witness Marcus proposes no adjustment for the SPO costs but recommends that EAI be required to submit a study to the Commission on this issue within 18 months. T. at P1086-1087. Staff witness Robertson testifies that, while it may be prudent to pursue other options as recommended by AEEC, given EAI's near term transition to MISO, Staff continues to support EAI's adjustment for these costs. T. at P2815-2816.

The Commission supports Staff's position on this issue and agrees with Staff that this case is not the best time to consider alternatives to ESI's services especially with EAI's pending transition to MISO. The Commission further notes that, at the

Evidentiary Hearing, AEEC witness Falkenberg appeared to agree that this issue would be best addressed in EAI's next rate case.

X. Depreciation

As outlined in the Revised Issues List, depreciation issues still in contention among the parties include: the depreciation rates; proposals on the gain or loss from the future sales of land at dismantlement sites; plant life extensions for White Bluff and Ouachita; interim retirements related to ANO steam generators; inclusion of a contingency factor in the dismantlement costs; and dismantlement reporting requirements.

As addressed by EAI witness Clayton, EAI prepared a depreciation study and proposes new depreciation rates. The study "was prepared using the straight line method and the average service life (AL) procedure on a remaining life basis. The life span technique was used for the various production plant accounts. The calculations were based on the original cost and attained ages of the property as of December 31, 2011 and estimates of survivor curves, probable retirement dates and net salvage percentages applicable to each property group." T. at P1495. EAI's net salvage rates include the use of interim retirements and a dismantlement cost study for certain production plants. T. at P1498-1499. EAI also identified unrecorded retirements for certain production plant and general plant items, for which EAI witness Clayton proposes a ten year amortization period in order to minimize the impact on ratepayers. T. at P1501-1502. EAI's "existing depreciation rates result in $205.6 million of annual depreciation expense on depreciable plant as of December 31, 2011 of $7.861 billion or a

composite rate of 2.62 percent. The current study shows $203.5 million of annual depreciation expense or a composite rate of 2.59 percent." T. at P1503.

Staff witness Garner prepared a depreciation study using the remaining life technique and recommends depreciation rates as reflected in Direct Exhibit RG-1. Mr. Garner testifies that the Commission has "approved rates derived using the remaining life technique since the mid-1990's." T. at P1697. Applying Staff's proposed depreciation rates, EAI's proposed depreciation rates, and EAI's currently approved depreciation rates to EAI's *pro forma* plant balances resulted in composite rates of 2.56%, 2.57%, and 2.66%, respectively. T. at P1700.

EAI witness Zakrzewski testifies that "the Company has used the Staff's rates in computing depreciation expense." T. at P323. Mr. Garner states that Staff agrees with EAI's ten year amortization period for production plant and general plant unrecorded retirements. However, Staff's amortization adjustment for the regulatory assets differed from EAI's due to updates related to the production plant. Mr. Garner testifies he performed an extensive analysis of EAI's dismantlement cost study and determined the terminal net salvage values were reasonable. T. at P1710.

In addition, Mr. Garner proposes a list of reporting requirements for retiring plants that are being dismantled but agrees with modifications proposed by EAI witness Castleberry and amended Staff's recommended reporting requirements accordingly. At the hearing EAI witness Castleberry agreed to the one remaining contested reporting requirement proposed by Staff. T. at 365. Mr. Garner also recommends that any realized gain or loss from the future sale or disposition of the land at each retired generating unit be applied as an offset to the dismantlement cost of the generating unit,

given that "any gain in excess of the dismantlement costs or loss in excess of original cost would inure to the Company's shareholders." T. at P1732. Mr. Garner also testifies that EAI has sixteen fully-reserved or over-accrued accounts. Although he recommends these accounts be excluded from the depreciation expense calculation, he does recommend depreciation rates for possible future use. T. at P1713-1715.

FEA witness Selecky recommends changes to the parameters used by EAI to develop the Company's proposed production depreciation rates. Mr. Selecky proposes to extend the life span of the White Bluff units by two years based on a 2008 study conducted by Burns & McDonnell, which was provided to FEA by EAI pursuant to a data request. The change would result in an increase to the average remaining life of less than two years. T. at P1752-1753. Mr. Selecky also proposes to extend the average remaining life of the Ouachita combined cycle steam plant by eight years. Mr. Selecky' s recommendation was premised on data from the EIA that identified over seventy combined-cycle combustion turbines that have been in operation over thirty years. Mr. Selecky also testifies there does not appear to be any single component of the generating plant that would limit the life to EAI's projected thirty-two years. T. at P1761-1762.

Mr. Selecky also recommends that EAI's "depreciation rates for ANO Units 1 and 2 and Common investment be adjusted to remove the impact of the extraordinary retirements in 2000 and 2005." T. at P1754. The extraordinary retirements were associated with a $40.3 million steam generator replacement for ANO Unit 2 in 2000 and a $44.7 million steam generator replacement for ANO Unit 1 in 2005. T. at P1758. Mr. Selecky also has concerns with EAI's use of a "truncated Iowa curve to describe retirement activity associated with production investment." Mr. Selecky developed an

average remaining life for ANO that did not rely on Iowa curves. T. at P1754-1755. Mr. Selecky proposes changes to EAI's dismantlement cost study to exclude the contingency factor and include the market value of the land. Mr. Selecky testifies that EAI's contingency factor should be removed from the dismantlement cost study because it "does not reflect a real cost but provides a safeguard at the expense of current ratepayers in the event that the cost estimates are low." T. at P1765. Mr. Selecky proposes that the land appraisals performed by EAI witness Cartwright should be treated as salvage and used in the development of EAI's depreciation rates. T. at P1785-1786.

Both EAI and Staff disagree with Mr. Selecky's proposed increase to the life span of the White Bluff and Ouachita units. T. at P1510, P1514-1515, P1727-1728. Staff witness Garner testifies that the study relied upon by Mr. Selecky to extend the life of the White Bluff plant was "performed before the currently approved depreciation rates were set in Docket No. 09-084-U. In that docket, the life of White Bluff was extended by 20 years. With that extension, the life expectancy of White Bluff is currently 60 years and is consistent with the average life of coal plants in fleets of the electric utilities that serve customer in the Arkansas jurisdiction." T. at P1727.

EAI witness Clayton agrees with Mr. Selecky that there are combustion turbines which have been in service for more than thirty years. However, he testifies that "few are the newest generation of combined cycle generating units." Mr. Clayton also testifies that to extend the life of the Ouachita units beyond thirty years would require significant additional capital expenditures. T. at P1515. Mr. Garner testifies that it is premature to extend the life of the Ouachita units beyond thirty years. The "technology of this plant has only been in EAI's fleet for a relatively short time" and the current

thirty year life span for the Ouachita units is consistent with the life span used by Staff for "similar plants added in recent years to the fleet of Oklahoma Gas & Electric Company." T. at P1727.

Mr. Clayton and Mr. Garner both disagree with Mr. Selecky' s criticism regarding the use of Iowa curves for ANO and his exclusion of steam generators from interim retirements. Mr. Clayton testifies that it is not always possible to have homogeneous items of property in a depreciable group and "Iowa curves provide a better model than a constant retirement ratio because Iowa curves recognize that retirement ratios increase with age." Mr. Clayton also testifies that Mr. Selecky's method assumes both old and new items of plant are equally likely to be retired. T. at P1511. Mr. Garner testifies Staff's treatment of steam generator retirements is consistent with the treatment used in the currently approved rates set in Docket No. 09-084-U and that the replacement of the steam generators was a "factor in the 20 year life extension granted for those units by the NRC." T. at P1728.

EAI witness Crean and Mr. Garner both testify that contingency factors are typically used in preparation of dismantlement cost estimates. T. at P1540-1542, P1729. Mr. Crean testifies that a contingency factor recognizes there are events that could occur which cannot be estimated with precision, such as "weather changes, labor availability, equipment shortages, fluctuations in cost of consumables, and unforeseen obstacles." T. at P1541. Mr. Zakrzewski disagrees with Mr. Garner's recommendation to offset dismantlement costs by any realized gain or loss from the future sale or disposition of the land at each retired generating unit and also disagrees with Mr. Selecky' s recommendation to use the appraised value of the land in development of EAI's current

depreciation rates. Mr. Zakrzewski testifies that these recommendations by Mr. Garner and Mr. Selecky are premature and recommends that the Commission defer a decision on this issue until an actual sale has occurred which would allow the Commission to "make an informed decision based on facts and circumstances prevailing at the time." T. at P323-324.

The Commission finds Staff's proposed method is consistent with prior Commission findings and that Staff's resulting depreciation rates are reasonable and, therefore, approves Staff's depreciation rates as recommended in Direct Exhibit RG-1 T. at E1829-E1834. The Commission rejects FEA's recommendation to extend the life span of the White Bluff and Ouachita units and agrees with EAI and Staff that a 60 year life expectancy for White Bluff and 30 years for Ouachita is supported by the record and reasonable. The Commission also agrees that the use of Iowa curves for ANO and the inclusion of the steam generators in interim retirements is reasonable as recommended by EAI and Staff, and, therefore, rejects FEA's recommendation.

The Commission finds that inclusion of a contingency factor in the dismantlement cost estimate is reasonable and prudent and thereby rejects FEA's recommendation to exclude the contingency factor from EAI's dismantlement cost study. The Commission notes that EAI has agreed to Staff's recommended dismantlement reporting requirements and, therefore, orders EAI to comply with the reporting requirements as recommended in Mr. Garner's Surrebuttal testimony T. at P1731-P1732.

The Commission agrees with EAI to defer a decision on the treatment of future gains or losses on the disposition of land at retired generating sites until the sale of the

land has occurred and such costs are known. However, the Commission orders EAI, for each sale of land at a retired generating site, to maintain sufficient records for review and determination of any realized gains or losses.

XI. Capital Structure

As addressed by EAI witness Zakrzewski, EAI requests an actual capital structure based on a level of externally financed capital and ratemaking liabilities, adjusted for known and measurable changes through December 31, 2013. T. at P192. The capital components included in EAI's requested capital structure are long term debt, U.S. Department of Energy (DOE) obligations, preferred stock, common equity, customer deposits, accumulated deferred income taxes (ADIT), accumulated deferred investment tax credits and working capital liabilities based on a 13- month average. T. at P193. EAI does not include short-term debt. According to EAI witness Gregory Zakrzewski, EAI is requesting a debt to equity ratio of 49% to 51%. T. at E500.

The two primary issues with EAI's proposed capital structure are the inclusion of short-term debt in the capital structure, which EAI opposes, and the ratemaking treatment of EAI's Money Pool Lending (Money Pool). Staff, through its witness Robert Daniel, supports an overall debt to equity ratio of 53% to 47%. This recommendation is based on the inclusion of short-term debt. Except for his short-term debt recommendation, Mr. Daniel states his recommended capital structure is consistent with EAI's requested capital structure. T. at P1867-1873.

AG witness Marcus does not make a recommendation in Direct Testimony, but accepts EAI's capital structure with the exception of EAI's exclusion of short-term debt and EAI's treatment of the Money Pool. Mr. Marcus notes that Staff's common equity

percentage, which is based on the end of 2012, is 60 basis points higher than EAI's which is based on the end of 2013.

AEEC witness Parcell states that EAI's common equity/debt ratios are comparable to those of other Entergy OpCos, and slightly lower than those of investor-owned electric utilities in general. T. at P2531-2533. FEA witness Gorman has no issue with EAI's proposed capital structure. T. at P2415.

Mr. Zakrzewski testifies that EAI's cost of capital in EAI Exhibit GRZ-6 reflects known and measurable adjustments to most elements of the capital structure through December 31, 2013, while Staff's current cost of capital recommendation reflects a mix of dates with some as of December 31, 2012 and others as of December 31, 2013. T. at P309.

In his Surrebuttal Testimony, Staff witness Daniel updates his recommended capital structure and reflects updates from December 31, 2012, to June 30, 2013. T. at P1908 and E2092. He disagrees with EAI witness Zakrzewski's proposal to include two quarters of projected net income in the common equity balance as speculative. Daniel continues to support his total debt to equity ratio of 53% to 47%. T. at P1908-1910. As corroboration for his inclusion of short-term debt in the capital structure, Daniel states that the average levels of short-term debt for the four quarters ending June 30, 2013 for his risk comparable and industry samples are 2.7% and 3.4%, respectively. He recommends a short-term debt balance that is no less than 1% of EAI's total external capital. T. at P1911.

In his Sur-Surrebuttal testimony, EAI witness Zakrzewski states that he provides additional evidence that using December 31, 2013, balances are known, measurable, and

reasonable for the capital structure. The debt balances per EAI's cost of capital are actual and no activity is expected for preferred stock. In his Rebuttal Testimony, Mr. Zakrzewski shows that the December 31, 2013, common equity balance is reasonable based on the recent history of third and fourth quarter net income activity. T. at P350-352.

Short-Term Debt

Mr. Daniels includes two EAI short-term bank credit facilities with limits of $150 million and $20 million. He considers both long-term and short-term debt in the relative proportions of debt and equity. T. at P1868-1870. Based on his analysis of the short term debt bank borrowings, he calculated an average of $55.25 million from the outstanding amounts of bank short-term debt EAI had during the test year, which he recognized as reasonable and included in EAI's capital structure. As discussed below, he also includes an amount based on EAI's participation in the Money Pool as a component of the overall short-term debt amount. T. at P1871. In Direct Testimony Daniel recommends an over-all short-term debt balance of $70,562,407 and short-term debt proportion of 1.27%. T. at E2088.

The AG observes there is nothing theoretically wrong with including short-term debt in the cost of capital. The AG would recommend the following adjustments:

a. EAI's estimated average 2012 bank credit included in its cost of capital is $8,531,507. The AG would reduce this amount $1,095,890 for a non-recurring cost, leaving $7,435,616 at an interest rate of 1.71%

b. Include a $30 million adjustment for Money Pool lending, which is similar to adjustments made by Staff in previous rate cases (Direct Testimony of Donna Gray in Docket 06-161-U, pages 16-17).

The result of these adjustments would be a two basis-point reduction to cost of capital or $946,000 in revenue requirement based on Staff's rate base. T. at P1055-1056.

Responding to Staff's inclusion of short-term debt in the cost of capital, EAI witness Zakrzewski testifies that EAI does not use the available short-term debt as part of its permanent long-term financing. T. at P282. Mr. Zakrzewski testifies that, in the past, the purpose for which EAI obtained short term debt was to meet unique liquidity, working capital and short-term financing situations. T. at P283-284. He also testifies that EAI will be required to maintain a letter of credit as part of MISO, limiting its access to short-term credit. T. at P285. He states that Staff's inclusion of $55.25 million of EAI's credit facilities as a short term debt component in the capital structure is not appropriate. T. at P285. According to Mr. Zakrzewski, EAI anticipates using the $150 million Credit Facility as a part of joining MISO. EAI will have to maintain a $23 million dollar letter of credit for the foreseeable future and will always need to provide collateral to operate in MISO. This limits EAI to $127 million of the $150 million credit facility. If a portion of the credit facilities should be included as short term debt, that portion should be based on EAI's actual use of its credit facilities. He states that Staff witness Daniel does not take into account the number of days the loans were outstanding during the test year. T. at P283-286. Taking this into account, along with the updated cost rates and the limitation that the MISO letter of credit places on the

national credit facility, the amount of short term debt would be $8.5 million with a weighted average cost rate of 1.72% as opposed to Staff's $55,250,000. T. at P286.

Mr. Zakrzewski disagrees with both Staff witness Daniel and AG witness Marcus regarding the inclusion of EAI's credit facilities in the cost of capital calculation. He continues to recommend that the credit facility short-term debt be excluded from EAI's cost of capital calculation. Mr. Zakrzewski states that Mr. Daniel's recommendations do not reflect the purpose for which EAI secured its credit facilities nor the Company's actual use of the facilities during the *pro forma* year. He states that Staff's level of credit facility short term debt should not exceed $7.4 million. T. at P342-344.

Money Pool

EAI did not make a Money Pool adjustment to its cost of debt in its Direct case. However, Staff witness Daniel included EAI's Money Pool borrowings in his short-term debt because EAI has the ability to borrow funds from the Entergy System Money Pool. T. at P1870. Based on Daniel's review of the Company's participation in the Entergy System Money Pool, EAI is currently a net borrower and he included $15,312,407 in his recommended short-term debt balance. This is the mean of EAI's cumulative daily Money Pool balances for the twelve months ending December 31, 2012. T. at P1871.

Mr. Daniel testifies that he uses the same method used in EAI's two prior rate cases, Docket Nos. 06-101-U and 09-084-U. However, in those cases, the result was that EAI was a net lender to the Money Pool. It has been previously established that ratepayers do not benefit from EAI being a net lender to the Money Pool; primarily because ratepayers do not receive the benefit of the interest income EAI receives on loans made to the Entergy system. Here, EAI's net borrower position is not reflected in

the cost of capital by the low cost of borrowing through the Money Pool. Mr. Daniels states that his adjustment recognizes EAI's net borrowing position of $15,312,407 as short-term debt. T. at P1872.

Mr. Zakrzewski argues in Rebuttal that the Entergy Money Pool is a FERC-approved inter-company borrowing arrangement designed to reduce Entergy Corp.'s subsidiaries' dependence on external short-term borrowing subject to a cap on overall borrowings. T. at P287. Mr. Daniel's $15.3 million Money Pool borrowing recommendation is not representative of EAI's anticipated Money Pool participation. EAI's position as a lender or borrower cannot be predicted with any reasonable accuracy. T. at P291. Witness Zakrzewski testifies that Mr. Daniel's recommendation incorrectly assumes that $15.3 million will always be available for EAI to borrow from the Money Pool. Mr. Daniel's recommendation to include $15.3 million of Money Pool borrowing as part of the short-term debt component of the capital structure is not appropriate because:

1. There is evidence that EAI will remain a net borrower;
2. Net interest earned or paid is immaterial to EAI's cost-of service; and
3. There is no guarantee that EAI will have $15.3 million available to borrow on an ongoing basis. T. at P293.

According to Staff witness Daniel, since the last EAI rate case, from January 1, 2010 through March 31, 2013, EAI has primarily been a net lender to the Money Pool. Throughout the last half of 2011 and first half of 2012, EAI was a net borrower in the Money Pool. EAI has now reverted back to being a net lender, consistent with the Company's historical position. He calculated EAI's average daily balance over the

twelve months ending June 30, 2013. The result of that calculation showed that EAI is now a net lender, as opposed to being a net borrower, as was the case in his Direct Testimony. EAI lent on average $49,525,609 to the rest of the Entergy System. T. at P1912 and E2100-2105.

With regard to the Entergy System Money Pool, Daniel's Direct Testimony included EAI's net borrowings from the Money Pool for the 12 months ending December 31, 2012 as a source of short-term debt. However, by June 30, 2013, EAI was a net lender to the Pool, so Mr. Daniel removed that component from short-term debt in his Surrebuttal Testimony. However, Mr. Daniel made a downward adjustment to the common equity, long-term debt, preferred stock, and short-term debt balances on a pro-rata basis. Mr. Daniel makes this adjustment because the Commission has found in prior Dockets that it is unacceptable for EAI to pay higher outside capital costs to loan money to the other Entergy Companies through the Money Pool. T. at P1911-1914.

Mr. Daniel points out that in Order No. 10 in Docket No. 06-101-U, the Commission found that this type of adjustment is appropriate because ratepayers should not pay the high costs of outside capital in order to loan money to the other Entergy Operating Companies at lower interest rates, and because it is a direct subsidy of the other OpCos ratepayers by EAI ratepayers. This adjustment will reduce from the capital structure $49,525,609 in externally supplied funds. T. at P1913 and E2106.

In his Surrebuttal testimony, AG witness Marcus points out that Staff has previously made adjustments when EAI was in a Money Pool lending position. The AG estimates that an adjustment of $30 million for average Money Pool lending would be appropriate and consistent with Staff's previous adjustments and recommends that the

$30 million *pro forma* Money Pool lending be removed from financial capital. T. at P1051, P1054-1056.

In Sur-Surrebuttal Testimony, Mr. Zakrzewski repeats his arguments that the inclusion of the Money Pool effects in the cost of capital is inappropriate in that specific events caused EAI's net borrowing or lending position in the Money Pool. There are no facts or evidence that EAI is subsidizing other Operating Companies as they have access to short-term credit facilities similar to EAI's. He also testifies that the subsidy issue was not mentioned in Staff's Money Pool recommendation in its Direct Testimony. When EAI borrows from the Money Pool, Staff does not describe this Money Pool balance as a subsidy of EAI by the other Operating Companies. T. at P347-348. Staff could not describe in its answer to EAI Exhibit GRZ-9, a circumstance where EAI's Money Pool position would not result in a reduction in the proposed cost of capital. Additionally, if EAI is lending, an asset is reflected on EAI's books and under normal treatment this asset would be included in the working capital assets and then be excluded because the balance earns interest and does not impact rates. Staff's treatment is a rate impact that normal accounting would not produce. T. at P349.

The Commission determines that Staff's proposed capital structure of 53% to 47$ total debt-to equity is just and reasonable. It reflects EAI's actual capital structure as of June 30, 2013, adjusted for the repayment of a bond in August, 2013. In contrast, EAI's proposed capital structure is as of December 31, 2013, and does not reflect known and measurable changes. In particular, we note that EAI's projection of Third and Fourth Quarters, 2013 net income is not known and measurable.

The two primary issues concern the inclusion of short-term debt in the capital structure and the ratemaking treatment of EAI's Money Pool lending. Staff and the AG both support the inclusion of short-term debt in the capital structure, while EAI opposes that treatment. Staff proposes that the short-term debt component be 0.64% (T. at E2092) and the AG proposes that that component be 0.13% (T. at P1063, Table 3). We agree with Staff and the AG that short-term debt should be included in the capital structure. It is a normal source of capital used by EAI as well as other utilities to fund ongoing operations. Although short-term debt may fluctuate over time, it is a permanent source of funds used by the companies in the samples used by Staff witness Daniel. Further, this inclusion is consistent with Commission policy in prior rate cases.

With regard to EAI's Money Pool lending, we agree with Staff's adjustment to EAI's external sources of capital to reflect EAI's Money Pool lending to the other Entergy OpCos. T. at E2106. Consistent with Commission policy, it is inappropriate for EAI ratepayers to pay the relatively high costs associated with financing $50 million in outside capital in order to loan money to the other Entergy OpCos at lower interest rates, and it is a direct subsidy of those other Entergy OpCos' ratepayers by EAI ratepayers. This problem is particularly egregious since EAI's ratepayers have subsidized other Entergy OpCos' ratepayers by $4.5 billion through Grand Gulf payments and bandwidth payments during the last three decades. Any additional subsidies by EAI ratepayers are unreasonable.

XII. Cost of Capital

Overall Rate of Return

EAI witness Gregory Zakrzewski recommends an overall rate of return of 5.02%. This overall rate of return reflects the cost of equity, common equity/long-term debt ratios, zero-cost capital, among other issues. T. at E500. Staff witness Robert Daniel's overall rate of return recommendation in his Direct Testimony is 4.48%. T. at P1858, P1898. Because EAI is not market traded, he relies on a sample approach to assess the risk of an equity investment in EAI. T. at P1858-1859. AG witness William Marcus's overall rate of return recommendation in Direct testimony is 4.44%. T. at P957.

HHEG witness Mark Kenneday makes no overall rate of return recommendation, but did find that EAI deserves a 10.4% cost of equity. He also asks the Commission to consider the impact to the economy with increased rates. T. at P1980-1981. No further recommendations were made by HHEG on this issue. FEA witness Michael Gorman recommends a 4.56% overall cost of capital for EAI. T. at P2405.

In his Rebuttal Testimony, EAI witness Zakrzewski recommends a 4.71 % overall rate of return based on December 31, 2013, projected capital components. T. at E511. However, in his Surrebuttal Testimony, Staff witness Daniel recommends a 4.38% overall rate of return. This differs from EAI's Rebuttal Testimony recommendation of 4.71% because of differences in cost of equity; cost of long-term debt; inclusion of short-term debt (by Staff); Money Pool adjustment (by Staff); zero-cost capital structure components; and equity/debt ratio. Staff witness Daniel bases his capital structure on June 30, 2013, balances with an adjustment for an August, 2013, repayment of long-

term debt issuances. Daniel's balances for ADIT and Current, Accrued, and Other Liabilities are provided by other Staff witnesses. T. at P1908 and E2092.

AG witness Marcus recommends a 4.37% overall rate of return in his Surrebuttal Testimony. This differs from EAI's Rebuttal Testimony because of differences in the cost of equity, reduction in the cost of long-term debt to reflect recent refinancings, inclusion of short-term debt, and removal of Money Pool lending from financial capital. He accepts the Company's debt/equity ratio. T. at P1050-1051. In his Sur-Surrebuttal Testimony, EAI witness Zakrzewski recommends a 4.73 % overall rate of return based on December 31, 2013, projected capital components. T. at E567.

The Commission determines that the following capital structure and capital costs are just and reasonable:

Component	Proportion	Cost Rate	Weighted Cost
Long-Term Debt	29.03%	4.97%	1.44%
DOE Obligation	3.25%	0.08%	0.00%
Short-Term Debt	0.64%	1.72%	0.01%
Preferred Stock	2.03%	5.99%	0.12%
Common Equity	28.62%	9.30%	2.66%
Customer Deposits	1.54%	0.50%	0.01%
ADIT	31.29%	0.00%	0.00%
Post-70 ADITC-Long-Term	0.35%	4.97%	0.02%
Post-70 ADITC-Short-Term	0.01%	1.72%	0.00%
Post-70 ADITC-Preferred Stock	0.02%	5.99%	0.00%
Post-70 ADITC-Common Equity	0.34%	9.60%	0.03%

Current, Accrued, and Other Liabilities	2.87%	0.00%	0.00%

Overall Cost of Capital 4.29%

This cost of capital, **4.29%**, is based on Staff's Surrebuttal Testimony with one exception. The allowed return on equity (ROE) is set at 9.30%. This allowed ROE, as well as the other capital components and capital costs, is discussed later in this Section of the Order.

Return on Equity

EAI requests a 10.4% allowed return on equity (ROE). T. at P2367. EAI witness Dr. Samuel Hadaway points out that as of December 31, 2011, EAI had total assets of $7.2 billion, net utility plant of $4.6 billion, long-term debt of $1.9 billion, equity of $1.5 billion, deferred credits of $3.1 billion, total operating revenue of $2.1 billion, and net income of $165 million. EAI has bond ratings of Baa2 and BBB from Moody's and S&P, respectively. T. at P2118-2119.

Dr. Hadaway states that in the past 10 years, interest rates in the U.S. have generally declined, the average inflation rate was 2.4%, and the 2012 average utility interest rate is at its lowest level in more than 30 years. He states investors remain concerned about high unemployment, large federal deficits, the Mideast turmoil, sluggish growth in GDP, and European and domestic economic issues and there are substantial equity market concerns, which contribute to heightened investor risk aversion. T. at P2121-2125.

EAI witness Cannell states that the electric industry is now in a period of significant capital expenditures because of replacement of aging infrastructure,

environmental requirements, grid enhancements, smart grid technologies, and new generation resource requirements. T. at P2246-2249. EAI is projecting capital expenditures of nearly $3.4 billion ($2.7 billion excluding transmission) over the period 2012-2018. T. at P2249. She points out that recent allowed ROEs in the Southeast are in the 10.2 % to 10.5% range. T. at P2287.

EAI witness Cannell states that low U.S. Treasury bond rates do not imply a correspondingly lower level of expectations regarding authorized ROE levels. First, the Federal Reserve Bank (Fed) is keeping Treasury rates artificially low. Second, risks associated with the utility industry have risen. Third, the current low level of interest rates does not impact the Company's embedded cost of debt. Its credit metrics must be maintained regardless of the current level of interest rates. T. at P2291. Investors also have concerns about regulatory lag for EAI and future dividends for Entergy. T. at P2293-2295. She testifies that in this case a 10.4% allowed ROE within a 10.2 % - 10.4% range would help maintain the Company's financial health, and assist in maintaining access to capital markets. T. at P2297.

Dr. Hadaway testifies that in the current low interest rate environment investors have been attracted to dividend-oriented stocks, such as utility stocks. The result is that in the context of the Discounted Cash Flow (DCF) model, utility prices have been bid up, and dividend yields are down. Consequently, the DCF results are negatively skewed by income-seeking investor behavior. Similarly, in risk premium models, artificially low interest rates reduce ROE estimates. However, Dr. Hadaway testifies that the cost of equity has not declined as much as the drop in interest rates. T. at P2126-2127.

According to Dr. Hadaway, there are three general estimation methods for estimating the cost of equity: comparable earnings, DCF, and risk premium. The comparable earnings method is flawed because accounting-based methods do not generally provide reliable cost of equity estimates. In periods of reasonable capital market equilibrium, a combination of DCF and risk premium methods usually provides the most reliable approach for estimating the cost of equity. However, due to ongoing market turmoil and current government monetary policy (artificially low interest rates), cost of equity estimates from these methods should be discounted. T. at P2138-2140.

He sets out the basic constant growth DCF formula as:

$$k = D_1/P_0 + g$$

where "k" is the cost of equity, D_1 is the expected dividend, P_0 is the current market price, and g is the constant growth rate in dividends per share. Recent events and current market conditions challenge the constant growth rate assumption. Dividend growth rate expectations have fluctuated widely. Long-term growth rate estimates may be highly uncertain, and estimating a constant growth rate is often difficult. T. at P2141-2142. Another version of the DCF model uses a short-run transitional growth rate followed by a long-term growth rate. T. at P2142.

Dr. Hadaway states that the risk premium methods are based on the assumption that equity securities are riskier than debt and, therefore, equity investors require a higher rate of return. However, there is no consensus on the estimate of the specific risk premium associated with the difference in investors' expected returns between debt and equity. Some analysts use long-term data, while others focus on more recent data. T. at P2145-2146.

Dr. Hardaway's DCF analysis uses three variants: constant growth based on analysts' estimates of 5- year earnings per share (EPS) growth, constant growth based on the long-term estimated Gross Domestic Product (GDP) growth rate, and a two-stage growth approach with transitional EPS growth rates and long-term growth rates. T. at P2148-2149.

Dr. Hadaway testifies that growth in nominal GDP (real GDP growth plus the inflation rate) is the most general measure of economic growth in the U.S. economy. Long-term growth in dividends is more closely predicted by broader measures of economic growth, such as nominal GDP, than by short-term analysts' estimates. Dividends for mature firms are often expected to grow about the same rate as nominal GDP. Competitive pressures ultimately work to correct excessively high or excessively low profitability growth. For the period 1952-2012 the overall average growth rate per year in nominal GDP was 6.5%. However, after the early 1980's, lower inflation has resulted in lower nominal GDP growth. In his analysis, witness Hadaway gave more weight to more recent years, which results in a long-term average nominal GDP growth rate of 5.6%. T. at P2149-2152.

Dr. Hadaway testifies that some currently lower growth rate forecasts understate long-term growth in nominal GDP because they are based on the assumption of permanently low inflation rates around 2%. The average long-term inflation rate has been higher at 3%. T. at P2152.

Dr. Hadaway testifies that government agency forecasts have been wrong in the past. Essentially all government agency forecasts currently use a 2% inflation forecast. In conjunction with a real GDP growth forecast of 2.4% to 2.8%, projected nominal GDP

growth rates by those agencies are in the range of 4.5%. Dr. Hadaway claims that his forecast of 5.6% for nominal GDP growth represents a much more realistic view of what longer term inflation will be. T. at P2152-2154.

Dr. Hadaway's DCF cost of equity estimates are as follows:

Constant growth with 5-year analyst-projected EPS growth rates – 9.6% to 9.8%;

Constant growth with nominal GDP growth rate – 9.9% to 10.0%;

Two-stage with 5-year analyst-projected growth and nominal GDP growth – 9.8%. T. at 2154.

Dr. Hadaway states that his DCF analysis indicates an equity range of 9.60% - 10.0%. T. at P2158. Dr. Hadaway's risk premium analysis yields estimates in the range of 9.7% to 10.0%.

Based on his DCF and risk premium analyses his resulting overall cost of equity range is 9.6% to 10.0%. However, he discounts the lower end of his ranges because he feels the DCF range is negatively skewed by the Federal Reserve's efforts to hold interest rates low and that the risk premium understates the required rate of return because of the historically low interest rates. T. at P2154-2158.

He concludes that, based on EAI witness Cannell's conclusion that a 10.2% - 10.4% range is consistent with investor expectation and EAI witnesses McDonald's and Lewis's concerns with EAI's substantial capital expenditures in the future, an allowed ROE range of 10.2% to 10.4% is reasonable. T. at P2159-2160.

Staff witness Daniel uses the DCF method as the primary methodology to determine EAI's ROE, as the Commission has embraced the DCF method for nearly two decades. T. at P1876. He bases his cost of equity analyses upon a risk-comparable

sample of 19 companies. He disagrees with EAI witness Hadaway's sample selection because Dr. Hadaway uses a criterion that includes revenues related to natural gas operations. This results in the inclusion of companies with different risk profiles than EAI's. T. at P1880-1883.

Staff witness Daniel's DCF estimate of the cost of equity using his risk-comparable sample ranges from 9.0% to 9.6% with a mean and midpoint of 9.3%. T. at P1887-1888. Using a broader "industry sample of electric utilities," his DCF analysis results in an estimated range from 8.8% to 9.8% with a mean and midpoint of 9.3%. T. at P1888-1889. Mr. Daniel also updates EAI witness Hadaway's DCF analysis using Dr. Hadaway's sample companies with more recent inputs which results in a range of 9.3% to 9.6%, down from Dr. Hadaway's initial range of 9.6% to 10%. T. at P1888-1889. Finally, he applies his recommended DCF approach to Dr. Hadaway's sample group of firms and obtained a range of 8.8% to 9.5% with a mean of 9.2% and a midpoint of 9.1%.

Mr. Daniel notes that recent Fed actions have kept interest rates at a low level, which has increased utility stock prices. Utility stocks are considered a safe alternative to interest-bearing securities and are havens for income-oriented investors. These higher utility stock prices have depressed dividend yields in the context of the DCF model. Additionally, current economic and market conditions have depressed analysts' growth rate projections in the context of usage in the DCF model. Given all of this, Mr. Daniel recommends a cost of equity range of 9.0% to 9.6%, with a point recommendation of 9.6%. Mr. Daniel testifies that, absent these unique economic and financial conditions, his recommendation would be 9.3%, which is the midpoint of his recommended range. T. at P1890-1893.

Staff witness Daniel testifies that EAI witness Hadaway's growth rate in Hadaway's DCF analysis is upwardly biased by the historical time-frames witness Hadaway used to estimate that growth rate. Dr. Hadaway calculates a 5.6% GDP growth rate but, if he had used more recent periods, the average GDP growth rate would be below his 5.6% figure. T. at P1885-1886.

Mr. Daniel states that Dr. Hadaway's risk premium approach is not reliable since risk premiums fluctuate over time. He also recommends the Commission continue to rely upon the DCF model as the primary method. T. at P1894- 1895. Further, he testifies that Dr. Hadaway's specific risk-premium analysis using allowed returns on equity is inherently circular, and based on cost of equity decisions in other jurisdictions. T. at P1895-1896.

Staff witness Daniel states that EAI witness Cannell performs no quantitative analysis for a cost of equity. Further, her recommendation of 10.2% to 10.4% is beyond the top of Hadaway's cost of equity range of 9.6% to 10.0% produced by Dr. Hadaway's DCF and risk premium analysis. T. at P1896-1897.

In his Direct Testimony, AG witness Marcus notes Dr. Hadaway admits that market uncertainty drives more investors to the less-risky utility stocks and, thus, will depress expected returns, as reflected in witness Hadaway's DCF analysis (pp. 18-20 of Hadaway Direct). However, to support his "adjustment" to his equity return, AG witness Marcus points out that Dr. Hadaway argues the opposite. Addressing the "artificially low" interest rates, Marcus quotes the Fed which indicates that interest rates are not expected to rise significantly. T. at P969-970. AG witness Marcus also rebuts Dr. Hadaway's concerns as to "analyst produced" growth rates used in the DCF, noting that

in EAI's last rate case Dr. Hadaway filed testimony in support of those rates. T. at P970-971.

AG witness Marcus states that Dr. Hadaway has created his own "Risk Premium" method, using unnamed utility data on "commission - approved" returns and Moody's cited utility debt costs to measure the "premium." He finds Dr. Hadaway's use of other commission approved returns, rather than "expected market," circular and testifies that Dr. Hadaway would have this Commission abdicate its responsibility by deferring to those other commission determinations. Mr. Marcus also notes that, once completed, Dr. Hadaway then discards the 10% return results of his own analysis. T. at P971-973.

AG witness Marcus proposes to look at other measures of investor equity return expectations including utility pension fund and decommissioning fund managers. The result of Mr. Marcus' pension fund analysis, using Dr. Hadaway's sample companies, is an expected equity return of 9.16% (with the related risk premium of 4.44% over bond yield). T. at P973-977.

AG witness Marcus also develops a Capital Asset Pricing Method (CAPM) analysis using the sample companies of Hadaway as a check against EAI's requested 10.4% ROE. The analysis reflects an ROE range between 6.46% to 7.61%. Even adding an additional 100 basis points to the risk free rate does not bring Dr. Hadaway anywhere near his requested ROE of 10.4%. T. at P992-993. Based on his analysis, and with the type of analysis prepared by Staff in normal cases, AG witness Marcus recommend an allowed ROE of 9.25%.

In Direct Testimony, AEEC Witness Parcell recommends, a cost of equity range of 9.0% to 9.5% with a point recommendation of 9.25%. Mr. Parcell notes that EAI

witness Cannell's testimony in support of a 10.4% cost of equity is based upon the risks of restructuring in the industry, a new construction cycle, and regulatory risks. However, Mr. Parcell's analysis indicates that the risk factors for the proxy group companies are largely unchanged from 2003. This indicates no increase in the relative risks for the electric utilities over the past several years. T. at P2559.

In his cost of equity analyses, AEEC witness Parcell uses two risk-comparable groups: witness Parcell's group of 12 companies (Parcell Group) and EAI witness Hadaway's group of companies (Hadaway Group). T. at P2533-2534. In his DCF analysis, Mr. Parcell calculates the dividend yield based on the average of high and low stock prices from April-June, 2013, and the current annualized dividend. T. at P2536.

For his DCF growth rates, AEEC witness Parcell uses *Value Line*'s projected and historical growth rates in dividends per share, earnings per share, book value per share, and earnings retention growth rate based on *Value Line* projections. Parcell Direct at 23-4. Witness Parcell's DCF estimate of the cost of equity using his risk-comparable sample is in a range of 8.4% to 9.1% with a midpoint estimate of 8.75%. T. at P2538.

AEEC witness Parcell's CAPM analysis uses the equation:

$$K = R_f + \beta(R_m - R_f)$$

where K is the cost of equity, R_m is the market return, R_f is the risk-free rate, "Rm - R_f" is the risk premium, and β is the Beta Coefficient. The Beta Coefficient reflects the relative volatility of a particular stock in relation to the overall market. For the risk-free rate, witness Parcell uses a recent 3-month average of 20-year U. S. Treasury yields, or 2.78%. For the Beta Coefficients, he uses the *Value Line* betas for his risk-comparable group. His estimated risk premium is about 5.47%. His CAPM estimate of EAI's cost of

equity is 6.3% to 6.7% for both the Parcell Group and Hadaway Group. T. at P2539-2942.

AEEC witness Parcell's Comparable Earnings (CE) Method uses historical returns on equity (1992-2012) for the two groups of proxy companies, as well as for unregulated companies. He compares these results with market price-to-book value ratios for the same time period. Based on the earned returns and the market-to-book ratios, Mr. Parcell's CE analysis indicates that the cost of equity for the proxy group is no more than 9.0% to 10.0%. T. at P2543-2547.

Witness Parcell disagrees with Dr. Hadaway's sole reliance on a single measure of DCF growth rate expectations – analysts' forecasts, noting that Dr. Hadaway's DCF model does not even consider dividend growth rates. T. at P2551. He disagrees with Dr. Hadaway's use of a GDP growth rate of 5.63% in his DCF analysis. Mr. Parcell states that it is more appropriate to use projections of GDP growth from the Social Security Administration and the Energy Information Administration (EIA) of 4.6% and 4.5 %, respectively. Correction for Dr. Hadaway's growth rate results in a DCF estimate of 8.93%. T. at P2552-2556.

Witness Parcell also does not agree with Dr. Hadaway's upward adjustment to his cost of equity analysis. He states that Dr. Hadaway's DCF results are in a range of 9.6% to 10.0% and his risk premium results are in a range of 9.7% to 10.0%. According to witness Parcell, Dr. Hadaway's 10.4% cost of equity recommendation significantly exceeds the results of his own analysis. He points out that Dr. Hadaway states he makes this upward adjustment because of current market turmoil and capital market

conditions. However, DCF results already reflect these conditions; thus, there is no need to inflate the DCF results. T. at P2557-2558.

FEA witness Gorman bases his cost of equity analyses upon the same risk-comparable sample that EAI witness Hadaway used, except he excluded TECO Energy because of a planned acquisition by TECO. T. at P2418. For his DCF analysis Mr. Gorman calculates weekly high and low stock prices for the sample companies over the 13-week period ending on July 12, 2013. For the dividend term in the DCF, he uses the annualized dividend levels reported in *Value Line*. The dividend yield is then adjusted for next year's growth rate. T. at P2420-2421. For his constant growth DCF analyses, he uses Reuters, Zack's, and SNL's projected growth rates in EPS which results in an average growth rate of 5.13%. The average and median constant growth DCF cost of equity estimates for his proxy group are 9.15% and 9.02%, respectively. T. at P2422.

Witness Gorman also uses a multi-stage growth DCF model. His analysis indicates that the long-term sustainable growth in stock investments will not exceed the growth in GDP. His long-term growth rate of 4.9% is corroborated by projections from the EIA and the Congressional Budget Office. T. at P2428-2430. Based on all of his DCF analysis, witness Gorman's DCF cost of equity range is 8.96% to 9.15%, and he concludes that a reasonable DCF cost of equity estimate is 9.15%, which is primarily based on his constant growth DCF model. T. at P2431.

The results of witness Gorman's risk premium method yields an overall risk premium cost of equity result of 9.60%. T. at P2436. Witness Gorman's CAPM analysis yields a cost of equity for EAI of 8.80%. T. at P2436-2441. Based on his DCF, risk premium, and CAPM analyses, witness Gorman's recommended cost of equity for EAI is

9.40%. He places minimal weight on his CAPM result because of concerns about the risk-free rate and risk premium. T. at P2441-2442. At his recommended return on equity of 9.4% and the Company's proposed capital structure, EAI's financial metrics are supportive of its current investment utility bond rating. T. at P2442-2445.

Witness Gorman points out that Dr. Hadaway's own analyses would support a return on equity in the range of 9.2% to 9.8% if that analysis is adjusted to reflect current market data and if Dr. Hadaway's models are properly applied. These adjustments to Dr. Hadaway's analysis support Gorman's proposed recommendation of 9.4%. T. at P2445.

In his Rebuttal Testimony, EAI witness Hadaway continues to recommend a 10.4% allowed ROE. He believes that mechanistic application of traditional cost of equity models do not capture the expectation of higher interest rates in the future. They are not consistent with basic economic theory or common sense. He states that his updated analysis confirms that the recommendations of the other parties are unreasonably low. T. at P2166-2167 and P2205-2207.

Dr. Hadaway states that the abnormally low interest rate policy of the Fed does not adequately represent utility capital cost conditions and reliance on such leads to under-estimated electric utility cost of equity estimates. Further he states that other parties have not incorporated the very recent increase in interest rates into their analyses. The Baa Average Utility bond yield has increased by 72 basis points since April 2013. Interest rates on 10-year and 30-year Treasuries are projected to increase by 80 and 60 basis points, respectively, by December 2014. T. at P2164-2173 and P2177.

Dr. Hadaway also testifies that the other parties' ROE recommendations (9.25%-9.60%) are substantially lower than average allowed returns for electric utilities of 9.8% to 10.6% over the period 2009-2013. T. at P2173-2174. He also states that the time period used in Staff witness Daniel's DCF model happens to correspond to the peak in utility prices. This decreases the dividend yield component in the DCF model, and consequently understates Mr. Daniel's DCF cost of equity. T. at P2181-2182. AG witness Marcus's use of actuarial rate of return assumptions for pension and nuclear decommissioning trust funds have little direct connection with the cost of equity for utilities. T. at P2186.

EAI witness Hadaway updated his ROE analysis in Rebuttal Testimony. His DCF updates have dropped by 30 to 70 basis points to a range of 8.9% to 9.7%. T. at P2166, fn. 1. He states these results are inconsistent with economic theory and common sense since interest rates have increased in the same period of time. His updated risk premium results are in the range of 10.0% to 10.4%. T. at P2206.

In her Rebuttal Testimony, EAI witness Cannell states that adoption of Staff or Intervenors' ROE recommendations would have a detrimental impact on investor perceptions regarding EAI's earnings and dividends prospects. T. at P2305. In the 155 rate case decisions since 2009 for integrated electric utilities in which an ROE was established, only one was below 9.25% (as recommended by the AG and AEEC), and only two were below 9.4% (as recommended by FEA). T. at P2306. She also testifies that it is necessary to look beyond quantitative models with their temporal influences (low interest rates) and to fully encompass risks (large capital programs, environmental

mandates, regulatory challenges) that investors are undertaking with their investments in electric utilities. T. at P2311.

Ms. Cannell disagrees with Mr. Marcus's use of pension returns as an additional means for reaching an appropriate ROE for EAI. She testifies that in Docket No. 04-021-U, the Commission stated that expected returns, as used in pension plans, cannot be used as a proxy for required returns, which is the type of ROE sought in rate cases. T. at P2313-2314.

In his Surrebuttal testimony, Staff witness Daniel updated his DCF cost of equity analysis. His updated DCF results are in a range of 8.4% to 9.5%. T. at P1917. He testifies that based on his review of other parties' recommendations, as well as his updated DCF results, he continues to recommend a cost of equity range of 9.0% to 9.6%, with a point recommendation of 9.6%. He also testifies that, because of uncertain economic conditions, his recommendation is at the top end of his range. Otherwise, he would recommend the midpoint, 9.30%. T. at P1915-1919. He also makes similar rebuttal arguments to EAI witnesses Hadaway and Cannell, as was made in his Direct Testimony. T. at P1919-1921.

In his Surrebuttal testimony, AG witness Marcus agrees that interest rates have risen, but not as drastically as suggested by EAI. Witness Marcus discusses the changes in interest rates and risk premiums for 30-year U.S. Treasury bonds and Baa bonds. Marcus concludes there has been some fluctuation, but little fundamental change in financial markets' assessments of financial risk in the last two years. The AG also notes that the near-term inflation outlook is stable. T. at P1057.

AG witness Marcus notes that Staff witness Daniel chose the absolute high end of his 9.0% to 9.6% range, which can only be supported because of the inclusion of four questionable companies in Staff's Risk Comparable and utility samples and Mr. Marcus recommends excluding these companies. T. at P1059. The four companies that Marcus recommends excluding are:

a. NV Energy – The company is the subject of a merger, which was announced after Staff started its work on this case.
b. Northeast Utilities – Marcus could not replicate *ValueLine*'s claim of the 18% historical growth rate over the last five years. In addition, Northeast Utilities acquired NStar in the middle of the historical period.
c. Public Service Enterprise Group – Even though *ValueLine* considers the company a regulated electric utility, it does not meet the appropriate screening criteria.
d. Edison International – Marcus believes the company's slow future growth is influenced by the bankruptcy of non-regulated affiliates in December 2012.

By re-running Staff's sample with the four companies excluded, the DCF-based cost of capital figures are between 8.9% and 9.3%, with a midpoint of 9.15% as shown in Table 2 on page 17 of witness Marcus' Surrebuttal testimony. Given the increase in interest rates in recent months, witness Marcus states he would add 10 basis points to the dividend yield. He still believes that a 9.25% allowed ROE is reasonable. T. at P1061-1063.

In response to EAI witness Cannell, AEEC witness Parcell notes in his Surrebuttal Testimony that average authorized ROEs have been trending down the past few years. The 2013 average allowed ROE is 9.80%. T. at P2573. Also, in response to Ms. Cannell, he notes that his ROE recommendation is consistent with ROEs expected by investors. T. at P2574. Parcell notes that witness Cannell is inconsistent on the levels of interest rates in the same way that Hadaway is inconsistent. T. at P2575.

Witness Parcell also notes that EAI witness Hadaway's DCF estimates of 8.9% to 9.7% are consistent with the DCF estimates of the other parties. However, Dr. Hadaway ignores his own DCF results because Dr. Hadaway claims that they do not pass basic tests of reasonableness. Further, Dr. Hadaway's 10.4% ROE recommendation is not supported by Dr. Hadaway's own analysis. T. at P2566.

In his Surrebuttal Testimony, FEA witness Gorman disputes EAI witness Hadaway's use of historical GDP growth rates in a DCF analysis. T. at P2462. He disagrees with Dr. Hadaway's assertion that there is an inverse relationship between interest rates and risk premiums. Witness Gorman's updated risk premium results are in the range of 9.10% to 9.56%. T. at P2463-2467. Witness Gorman still supports his recommended allowed ROE, which is still approximately the midpoint of his range of 9.15% to 9.60%. T. at P2467.

In rebuttal of EAI witness Cannell, witness Gorman notes that authorized ROEs have declined since 2009. The average allowed ROE in the 3rd Quarter, 2013 was 9.80%. The APSC has also reduced allowed ROEs recently. T. at P2468-24-69.

In Sur-Surrebuttal, EAI witness Hadaway continues to emphasize that interest rates have risen recently, which increases utility equity costs. EAI witness Cannell

doubts that utility stocks' dividend yields will likely continue to hold appeal relative to bonds as interest rates rise. T. at P2319-2320. She states that the central tendency in 2013 for allowed ROEs for integrated electric utilities in the Southeast U.S. has been 10.10%. T. at P2321-2322.

A summary of the Parties' recommended allowed ROEs is provided in the Table below:

Recommendations for EAI's Allowed Return on Equity

Party	Recommended ROE
EAI	**10.4%** (10.2% - 10.4%)
Staff	**9.60%** (9.0% - 9.6%)
Attorney General	**9.25%**
AEEC	**9.25%** (9.0% - 9.5%)
FEA	**9.4%** (9.15% - 9.50%)

Note: Recommended ROE ranges are shown in parentheses.

Of the five ROE recommendations made by the Parties, including EAI, four of the recommendations are clustered in the range of 9.25% to 9.6%, while the outlier is the Company's recommendation of 10.4%. If the Staff's recommendation were the midpoint of its range, or 9.3%, the four non-EAI Parties' recommendations would be clustered in the range 9.25% - 9.4% with a midpoint of approximately 9.3%.

Generally, estimates of the cost of equity are used as a basis for determining the allowed ROE. The cost of equity is the return required by investors in the common equity of the Company. In this case, the methods generally used for estimating EAI's

cost of equity are the Discounted Cash Flow, or DCF method, the Risk Premium method, and the Capital Asset Pricing Method, or CAPM. The Commission does not rely upon the Comparable Earnings Method because that method relies upon earned returns, rather than required returns, and is circular in nature. The Commission primarily relies upon the DCF method because it is more directly market-based than the other methods. A key component of the DCF formula is the price term. The price term, if properly calculated, is *forward-looking*, and directly embodies the market consensus of a utility's risk, the time value of money, and expected dividends. As can be easily seen from the DCF formula, $k = D/P + g$, if risk or the time value of money increases, k increases and P decreases. None of the other cost of equity methods employ such a simple and direct market-based measure. In sharp contrast, other methods such as the Risk Premium method and CAPM are *backward-looking*, relying upon an array of historical data, which may or may not be applicable in the future.

EAI witnesses Hadaway and Cannell argue that current interest rates and DCF results are anomalously low because of the Federal Reserve's efforts to maintain low interest rates during the past few years. According to EAI, the Fed's actions have artificially inflated utility stock prices and led to lower dividend yields and lower DCF results. Consequently, EAI recommends an allowed ROE at the very top of Hadaway's risk premium range, and totally ignores its own witness's DCF results of 8.9% to 9.7%. However, that risk premium upper estimate utilizes a projected Triple-B bond yield of 5.78%, which is 35 basis points greater than the current bond yield. If that risk premium is eliminated, Hadaway's risk premium results are in the range of 10.0% -

10.2%. T. at E2208-2211. Staff makes a similar "anomaly" argument in support of the upper end of its cost of equity range.

The Commission does not find EAI's and Staff's "anomaly" arguments persuasive. Similar arguments can be made for any time period in recent U.S. economic and financial history. It is unclear what exactly constitutes "normal" economic and financial conditions, and, in particular, what constitutes a normal level of interest rates. As shown in Exhibit DCP-2, T. at E 2369, the interest rates on U.S. 10-year Treasury bonds has varied between 1.80% and 13.93% since 1981. The country is currently in a low interest rate environment. In the past, including the early 1980's, this Commission allowed higher ROEs, which corresponded with extremely high interest rates during that period. It would be inconsistent to now adjust allowed ROEs upward because of currently low interest rates. Further, the Fed has been pursuing those low interest rate policies for a number of years, a period which corresponds closely to the period of time new rates are effective for a typical utility.

The allowed ROE should reflect current economic and financial conditions, not ignore those conditions. The DCF method reflects current economic and financial conditions through the price term in the DCF equation. EAI has not presented any evidence that any of the parties' DCF price terms, or the price terms used by its own witness Hadaway, are flawed or erroneous. As noted by AG witness Marcus:

> Dr. Hadaway's statement acknowledges that investors favor utilities so much that they are driving dividends yields down [and DCF results down]. The lower yield may be in part a result of more purchasing by income-seeking investors, but the proof of the pudding is in the eating: income-seeking investors...are investing in utilities despite the lower yields. The conclusion from this observation is not that utilities should be rewarded with high returns in a low-return economy. T. at P967-968

This Commission has always relied upon and afforded significant weight to the DCF method. Further the Commission notes the that 9.3% is the mid-point of Staff's recommended ROE range, without an upward adjustment for "anomalous" economic and financial conditions. Staff's application of its recommended DCF approach to Dr. Hadaway's sample group of firms results in a mean ROE of 9.2%. T. at P1889-1890. The Commission also notes that EAI witness Hadaway updated his DCF analysis in Rebuttal Testimony resulting in a range of 8.9% to 9.7% with a midpoint of 9.3%. *See* T. at P2166, footnote 1.

As noted in Order No. 7, Docket No. 05-006-U, historically, Staff has recommended, and the Commission has adopted, a return on equity which falls approximately in at the mid-point of the Commission-approved equity range. The Commission has deviated from this historical practice based on a utility's poor customer service and failure to comply with Commission Rules or in recognition of the reduced risk associated with the adoption of a decoupling rate mechanism.[24] Here, as in Docket No. 05-006-U, the Commission finds no compelling evidence to justify a return on equity above the approximate mid-point of Staff's range. The Commission finds that a return on equity of 9.3 is reasonable.

Costs of Long-Term Debt, Short-Term Debt, Department of Energy Debt, Customer Deposits, and Preferred Stock

In Direct Testimony, EAI Witness Gregory Zakrzewski recommends cost rates of 5.41%, 0.09%, 0.50%, and 5.99% for long-term debt, DOE debt, customer deposits, and preferred stock, respectively, based on December 31, 2013 projections. He made no

[24] Docket No. 04-121-U, Order No. 16 and Docket No. 07-026-U, Order No. 7, footnote 7

recommendation on the cost of short-term debt since he did not include that capital component in his capital structure. T. at E500.

In Direct Testimony Staff witness Robert Daniel recommends cost rates of 5.52%, 1.68%, 0.09%, 0.50%, and 5.99% for long-term debt, short-term debt, DOE debt, customer deposits, and preferred stock, respectively, based on December 31, 2012 balances. T. at E2088. His cost of long-term debt is different from the Company's since his is based on actual information as of December 31, 2012. T. at P1874. Mr. Daniel's cost of short-term debt is based on weighted average bank short-term debt and Money Pool borrowings during the test year. T. at P1875. He does not disagree with the Company's costs of DOE debt, customer deposits, and preferred stock.

AG witness Marcus disagrees with the Company's cost of long-term debt. He has updated it to 4.97% based on debt refinancings in January, 2013, and August, 2013, as well as new issuances in June, 2013. T. at P962.

FEA witness Michael Gorman adjusted EAI's cost of long-term debt for two debt issues that are currently callable without a premium and restated these securities at current market rates. He also adjusted EAI's projected 2013 debt issuance interest rate to reflect the actual interest rates on these debt issues rather than EAI's projected interest rates. His recommendation for the cost of long-term debt is 4.90%. T. at P2405 and E2251-2253.

AEEC witness David Parcell disagrees with the Company's cost of long-term debt, noting that EAI's actual debt costs for the May, 2013, and June, 2013, issuances were less than the 5.5% cost rate in EAI's application. Updating for that will decrease EAI's cost of long-term debt. Further, EAI could reduce its cost of long-term debt by

calling certain bonds at par. AEEC witness Parcell does not recommend a specific cost of long-term debt. T. at P2548-2549.

In Rebuttal Testimony EAI Witness Gregory Zakrzewski recommends cost rates of 4.82%, 0.06%, 0.50%, and 5.99% for long-term debt, DOE debt, customer deposits, and preferred stock, respectively, based on December 31, 2013 projections. If short-term debt is included in the capital structure, which he does not recommend, the calculated cost of short-term debt is 1.72%. T. at P286 and E511.

In Revised Surrebuttal Testimony. Staff witness Daniel recommends cost rates of 4.97%, 1.72%, 0.08%, 0.50%, and 5.99% for long-term debt, short-term debt, DOE debt, customer deposits, and preferred stock, respectively, based on June 30, 2013, balances. T. at 32092. His cost of long-term debt is adjusted to reflect EAI's repayment of a bond in August, 2013. T. at P1909. His updated cost of short-term debt is 1.72%, based on information provided in EAI witness Zakrzewski's Rebuttal Testimony. He also updated his cost of DOE debt to 0.08%. T. at P1914.

AG witness Marcus agrees with the Company's updated cost of long-term debt of 4.82%. T. at P1056. He made numerous adjustments to EAI's calculated cost of short-term debt and recommends a 1.71% cost of short-term debt. T. at P1054-1055 and P1063.

In Sur-Surrebuttal Testimony EAI Witness Gregory Zakrzewski recommends cost rates of 4.82%, 0.06%, 0.50%, and 5.99% for long-term debt, DOE debt, customer deposits, and preferred stock, respectively, based on December 31, 2013, projections. If short-term debt is included in the capital structure, which he does not recommend, his calculated cost of short-term debt is 1.72%. T. at P286 and E511.

The Commission notes there is no disagreement among all of the parties regarding the costs of the DOE obligation, customer deposits, and preferred stock. The Commission agrees with the parties' recommendations on those capital components.

With regard to the cost of long-term debt, Staff and HHEG recommend 4.97%, FEA recommends 4.90%, EAI and the AG recommend 4.82%, and AEEC recommends a cost of long-term debt less than that in EAI's application. The Staff's recommendation is based upon data as of June 30, 2013, with one known and measurable change. The Commission determines that Staff's cost of long-term debt reflects the most current cost levels and is reasonable.

With regard to the cost of short-term debt, Staff recommends 1.72%, based on EAI's calculation. EAI makes no recommendation given that it does not include short-term debt in the capital structure, HHEG recommends 1.68%, and the AG recommends 1.71%. We determine that Staff's recommendation is reasonable, and practically the same as the AG's. HHEG's recommendation is based on Staff's Direct Testimony and does not reflect Staff's updates.

XIII. Accumulated Funds Used During Construction

EAI witness Jay Lewis testifies that as part of the overall settlement in Docket No. 09-084-U, the Company agreed to limitations on the level of Allowance for Funds Used During Construction (AFUDC) to be accrued as recommended by Staff in that Docket. Specifically EAI agreed in that Docket that the AFUDC rate would be no higher than the overall rate of return; compounding would be on an annual basis; AFUDC accrual would not begin until the project has been approved by the Commission; and accrual of AFUDC would be suspended where there is an interruption in construction that has

exceeded four consecutive months. EAI witness Lewis points out that the parties in that prior Docket agreed that the Settlement Agreement on this matter shall not be used or argued as establishing precedent for any methodology or rate treatment in any future proceeding. T. at P1808-1810.

EAI witness Lewis proposes that the AFUDC rate be calculated consistently with the FERC Uniform System of Accounts; compounding would be on a semi-annual basis; AFUDC accrual would begin at the time construction begins; and accrual of AFUDC will not be discontinued on a project, unless certain criteria are met. T. at P1811.

Mr. Lewis testifies that the FERC AFUDC formula proposed by the Company recognizes the difference between financing during construction and the financing of rate base considered in a rate case. The FERC formula establishes that the first source of funds for construction is short-term debt, with long-term debt and equity supplementing that source when the amount of short-term debt it is not sufficient to finance the construction activity. The FERC formula updates both the balances and cost rates to the most current values. In addition, the FERC formula does not include zero-cost capital sources, such as ADIT. T. at P1815-1816. He states that the Company should be allowed AFUDC accrual from the time construction begins because that is when construction funds begin to be expended. T. at P1819-1820.

Staff witness Daniel disagrees with the Company's recommendation to use the FERC formula for calculating the AFUDC rate. He also disagrees with the Company's request to compound semi-annually instead of annually. He testifies that ADIT should be used in the calculation of the AFUDC rate since it is a source of funds for construction activity and all sources of funds are fungible. Witness Daniel testifies that ratepayers

should not pay any higher return than is allowed in establishing base rates. An annual compounding of AFUDC better aligns the Company's accrual with the determination of annual revenue requirement and with the frequency of general rate cases allowed under Arkansas law. He recommends that the AFUDC rate be no higher than the overall rate of return determined in this Docket. T. at P1900-1903.

Staff witness Matthews' recommendation regarding AFUDC is that: 1) the accrual of AFUDC for projects requiring Commission approval should not begin until the project has been approved; 2) AFUDC should not begin prior to construction costs being continuously incurred on a planned, progressive basis whether Commission approval is required or not; and 3) the accrual of AFUDC should not be made if work on the construction project has been interrupted for more than four consecutive months. T. at P1254-1255. Staff witness Matthews states that Staff is attempting to prevent ratepayers from paying AFUDC cost above a reasonable level and to suspend AFUDC accrual if there is an interruption exceeding four consecutive months. As the Company has control of the timing of its request and expenditures prior to approval, the ratepayers should not bear the burden of delays, lengthy periods of interruption, or inclusion of costs of projects not approved. T. at P1938-1940.

Witness Matthews testifies that in the current Docket there were only three instances in which there were interruptions of more than four months. During his review of AFUDC calculations in Docket No. 09-084-U, there were several projects with periods of interruption from 1 month to 23 months during which EAI accrued AFUDC. Subsequent to the conclusion of EAI's last rate case, EAI implemented a new policy which suspends the accrual of AFUDC if there is an interruption exceeding four

consecutive months. The four-month interruption policy should be continued. T. at P1938-1940.

Kroger witness Townsend recommends continuation of the APSC policy of using the overall rate of return on rate base for the AFUDC rate, rather than using the FERC formula. Mr. Townsend's recommendation is based on the fact that all sources of capital are fungible and comingled, which is a methodology approved by the Commission in the following cases: Arkansas Western Gas Company in Docket No. 06-124-U, United Water Arkansas, Inc. in Docket No. 06-160-U, Center Point Energy Arkansas Gas in Docket No. 06-161-U, Arkansas Oklahoma Gas Corporation in Docket No. 07-026-U, and Oklahoma Gas and Electric Company in Docket No. 08-103-U. T. at P35-38.

HHEG witness Garrett does not agree with EAI's recommendations concerning AFUDC and testifies that the FERC formula is only instructive for state regulatory commissions and the APSC is free to set AFUDC rates in Arkansas. Nor has EAI provided evidence to show it should be treated differently than other companies. Mr. Garrett also testifies that sole discretion regarding accrual during periods of inactivity should not lie with the Company.

In his Rebuttal Testimony, EAI witness Lewis disagrees with Staff witness Daniel and Kroger witness Townsend that all sources of capital are fungible. In particular, ADIT, and other zero-cost sources of capital are only being used to fund rate base and cannot be used for CWIP. The calculation of AFUDC relates solely to the relatively small portion of the Company's assets that are under construction at any given point in time. T. at P1829-1832. The FERC approach, which is recommended by EAI, recognizes these

distinctions. Setting AFUDC lower than the actual cost of financing construction discourages a utility from making investment and is particularly counterproductive at this time of large expected investment outlays by EAI. T. at P1833.

Lewis disagrees with Staff witness Matthews' recommendation that AFUDC accrual should not begin until the project has been approved by the APSC. Lewis states that EAI already provides customer protection in its policy to reverse AFUDC accrual if a construction project is either cancelled or not approved by the APSC. T. at P1833-1834. He further testifies that construction delays can occur because of a customer's delay in completing its portion of the work, or due to securing permits, or other regulatory approvals. He states that it is in the best interest of the customers to maintain flexibility in construction scheduling such that the highest priority work can be performed, even if this results in delays in completing other work. T. at P1834-1835.

Mr. Lewis disagrees with Staff witness Daniel regarding the frequency of compounding of AFUDC. He states that the timing of rate cases has little to do with the financing of construction costs. The determining factor in EAI's recommendation that AFUDC be compounded on a semi-annual basis is that EAI typically makes interest payments on long-term debt quarterly or semi-annually, and common dividend payments as often as monthly. T. at P1835-1836. Mr. Lewis argues that the previous dockets cited were settlements and should not be used as precedent. T. at P1837.

Staff witnesses Daniel and Matthews maintain their positions in Surrebuttal testimony. Staff witness Matthews states that under EAI witness Lewis' reasoning, the Company could accrue AFUDC for preliminary survey costs for months, or even years in advance of its decision to apply for approval of the project. Allowing the Company to

accrue AFUDC for extended periods of inactivity results in the Company earning a return for inactivity, the costs of which are ultimately capitalized and included in rates. T. at P1946-1947.

In his Surrebuttal testimony, Staff witness Daniel states that EAI witness Lewis ignores the fact that AFUDC captures funds from all available sources used during construction (fungibility principle) and so AFUDC should be determined in the same manner as overall rate of return. He states the Company has multiple options to finance construction projects in any combination of liability and capital sources, including ADIT, as well as sources of zero-cost funds. He testifies that although FERC does allow compounding more frequently than annually, annual compounding is reasonable and consistent with the application of the overall rate of return since an AFUDC rate set at the overall rate of return will encompass different capital components with different rates and required payments. T. at P1923-1926.

HHEG witness Garrett states in his Surrebuttal Testimony that even though the cases cited in Direct were settled cases, the Staff has stated a policy on AFUDC and the other Arkansas regulated utilities are following it. According to Garrett, EAI has shown no evidence demonstrating why the Commission should treat it differently than the other regulated utilities in the state. T. at P1927-1298.

In his Sur-Surrebuttal Testimony, EAI witness Lewis testifies that the calculation of AFUDC is a policy issue that should be consistent across all public utilities in Arkansas. The appropriate approach is for the Commission to initiate a generic docket to collect facts and make a policy determination and apply it consistently for all industry participants. EAI will support this effort. T. at P1843-1845.

In response to Staff witness Matthew's concerns that EAI could accrue AFUDC for months or even years in advance of applying for approval of a project, Mr. Lewis testifies that, during the period from design to completion, the Company would incur financing costs on the project until it is closed to plant and included in rates. T. at P1846. Mr. Lewis asserts that not accruing during inactivity amounts to a zero interest loan during construction and that four months is not sufficient to resolve issues related to delays. T. at P1847-1848.

The Commission finds that the AFUDC should be set at the overall rate of return, as recommended by Staff, Kroger, and HHEG, and is consistent with AFUDC treatment by this Commission since Docket No. 09-084-U. The Commission has long accepted that all sources of funds are fungible, and are equally used to finance CWIP as well as rate base. Given the fungibility of the funds available to EAI, it is impossible to determine which specific source is financing any particular asset. All of the sources are commingled together to fund all of the assets and specific funding sources cannot be assigned to AFUDC rate determinations only. Consequently it is reasonable to apply the overall rate of return to rate base and to AFUDC.

The Commission also agrees with Staff that annual compounding of AFUDC better aligns the Company's accrual with the determination of annual revenue requirement and with the frequency of general rate cases allowed under Arkansas law. This represents a reasonable balancing of ratepayer and shareholder interests and is adopted.

Finally, the Commission agrees with Staff witness Matthews' and HHEG witness Garrett's recommendations regarding AFUDC that: 1) the accrual of AFUDC for

projects requiring Commission approval should not begin until the project has been approved and 2) the accrual of AFUDC should not be made if work on the construction project has been interrupted for more than four consecutive months. The Commission finds that, as the Company has control of the timing of its request and expenditures prior to approval, the ratepayers should not bear the burden of delays, lengthy periods of interruption, or inclusion of costs of projects not approved. Allowing the Company to accrue AFUDC for extended periods of inactivity results in the Company earning a return for inactivity- the costs of which are ultimately capitalized and included in rates. Further, under EAI's approach, the Company could accrue AFUDC for preliminary survey costs for months, or even years in advance of its decision to apply for approval of the project.

XIV. Cost Allocation

Production Demand Cost Allocation Methodology

The appropriate methodology for allocation of demand-related production costs to retail rate classes remains an outstanding issue among the Parties as reflected in the Revised Issues List. In this regard, EAI, Staff, and the AG all support a method referred to as the Energy and Peak methodology, which is more commonly known as the Average and Peak (A&P) methodology. AEEC witness Falkenberg and HHEG witness Blank recommend the Commission reject the A&P methodology and instead adopt the 12 Monthly Coincident Peak (12CP) Method for both production and transmission.

Staff witness Klucher testifies that the A&P methodology appropriately recognizes that the system must have adequate capacity to satisfy demand at the time of the peak and also that the utility tries to satisfy the energy supply over the course of the

year with the most economical supply available. T. at P2078. Mr. Klucher describes the A&P method as having two components: an energy component (with a percentage weight of the system load factor[25]) and a peak demand component (with a percentage weight of one minus the system load factor). Thus, the A&P method recognizes that classes of customers should receive some allocation of costs reflecting both a contribution to peak and an energy usage component to recognize that different types of capacity – base load, intermediate, and peaking capacity – are installed depending on energy use and the duration of load. The use of the A&P methodology is also consistent with the Commission's treatment of demand-related production costs in EAI's last two rate cases. T. at P2079. EAI witness Pettett says the A&P method recognizes that the system serves customer demand throughout the year and not just "on-peak" and provides a reasonable balance between customer demand and annual use. T. at P367-368.

Mr. Falkenberg criticizes the A&P method as being one of the most adverse methodologies for high load factor and interruptible consumers. T. at P669. Mr. Falkenberg also testifies the A&P method fails to produce reasonable results, and does not reflect cost causation, particularly now with EAI's entry into MISO. He points out that the load serving Market Participants in MISO estimate their load coincident with the (estimated) four MISO system peaks, from June through September, (4CP method) to determine planning reserve requirements which Falkenberg believes is a method more compatible with the 12CP method. T. at P672. Mr. Falkenberg promotes the 12

[25] "Load factor is the relationship of average demand to peak demand. Load factor is calculated by: 1) dividing the total annual energy consumption by the number of hours in the year (this calculation produces an average demand (kW); 2) this average demand is then divided by the peak annual kW demand to determine an annual load factor." T. at P368.

CP Method as being widely used and generally seen as a compromise method (as compared with 1CP, 4CP, and A&P). From a pure cost causation viewpoint, he believes that the Average and Excess 4CP method used in Texas is probably the most superior of all the competing methods if the APSC desires to use a method that recognizes both peak demands and energy usage. T. at P671-675.

HHEG witness Blank says he is troubled with EAI's use of the A&P method to determine the energy related portion of capacity related costs. He argues that this method of determining the energy allocation portion contradicts the NARUC Manual (see the footnote on p. 57 of the Manual), and places excessive weight on the energy allocation ratios, and effectively double-counts energy (or average demand) because the average demand level is also embedded in the coincident peak allocation ratios. T. at P539.

Mr. Blank testifies that, given the long-term application of the A&P method in Arkansas and the suppression of rates for certain rate classes, the Commission should transition away from this allocator carefully to avoid excessive rate shock on any customers. Therefore, to mitigate possible rate shock as Arkansas moves toward cost-based rates, he recommends the use of the 12CP allocation ratios for the allocation of production capacity costs. Effectively, the 12CP methodology recognizes both the class average demands and the class excess demands for each month with the average and the excess weighted evenly. Because the calculation includes all 12 months, he argues this method allocates less cost to the relatively low load factor rate classes. T. at P544.

Wal-Mart witness Chriss asserts that the A&P method, which allocates significant demand cost on energy, unfairly penalizes high load factor customers by allocating a

larger percentage of production demand costs to large users. He argues that this method fails to capture high-load factor customers' increased off-peak (more efficient) use and this fact, along with EAI's failure to incorporate a customer class level time variant factor, to recognize the off-peak lower fuel cost, results in a double penalty to those customers. Therefore, Mr. Chriss recommends the Commission consider whether the A&P method is appropriate in the rate case, but does not offer a specific alternative. T. at P23-24.

In rebuttal, EAI witness Pettett points out that production demand allocation has been thoroughly debated in past rate cases, with each party advocating an interest in the allocation of costs that aligns with its client's direct interests. As an example, he says AEEC and HHEG witnesses both recommend methods that rely more on the four summer months, such as the Average and Excess 4 Coincident Peak (A&E4CP), because those methods would most likely shift costs away from higher load factor customers, such as industrial customers, and onto the residential rate class as compared to the Energy and Peak. Mr. Pettett goes on to state that, if public policy or other appropriate consideration causes any change away from the A&P method, as suggested by AEEC and HHEG, it should be a gradual and thoughtful process to minimize abrupt customer impacts. T. at P450-451.

AG witness Marcus supports EAI's use of the A&P methodology, but states if changes are made, the Commission should move toward classifying more generating plant as energy-related. Mr. Marcus disagrees with Mr. Falkenberg's belief that the Average and Excess 4CP method "alone can provide the cost causation for a utility to build a nuclear power plant or a modern coal plant." Mr. Marcus says "peak" causes

megawatts to be acquired, while "sustained energy use" causes the type of plant that is built. T. at P1098.

In his Surrebuttal testimony, Staff witness Klucher says he continues to recommend the A&P methodology for allocating capacity related production costs. He argues that the A&P methodology recognizes each class's contribution to system peak as well as average energy used throughout the year, consistent with EAI's production plant investment decisions. T. at P2088. Mr. Klucher states that the A&P method is more appropriate than the 12CP method because it recognizes that system operations, fuel costs, and fuel diversity are major determinants of production planning, and, as such, considers energy consumption as well as demand in the development of the allocation factor. He says the 12CP method does not assign cost responsibility to users of production capacity at times other than the 12 monthly system peaks and, therefore, does not properly incorporate energy weighting into the treatment of production plant costs. T. at P2088. Mr. Klucher believes the appropriate way to incorporate an energy weighting is to classify part of the utility's production plant costs as energy-related and to allocate those costs to the classes on the basis of energy consumption. He believes using a coincident peak, such as 1CP or 12CP, to allocate costs will result in apportioning too much capacity to customers whose load factors are below the system average, and too little capacity to customers whose load factors are above the system average. Mr. Klucher says the opposite is true when using an allocator that only considers energy consumption. He argues that A&P methodology provides the correct balance, because the A&P capacity allocator falls between the coincident peak and energy allocators when using a weighted average based on the system's load factor. T. at P2089.

Regarding the NARUC Manual, EAI witness Pettett pointed out during the hearing that the NARUC Manual "recognizes that no single costing methodology will be superior to any other, and the choice of methodology will depend on the unique circumstances of each utility. Individual costing methodologies are complex and have inspired numerous debates on application, assumptions and data. Further, the role of cost and ratemaking is itself not without controversy." T at 506.

The Commission continues to agree with EAI, Staff and the AG and finds that the A&P method appropriately reflects the procurement and use of production capacity and is a balanced and reasonable allocation methodology. The Commission, therefore, adopts the use of the Average and Peak methodology to allocate capacity-related plant costs to the different customer classes.

Accounts 364-368 Demand Customer Split

In preparing its cost of service study, EAI allocated the following accounts using a 100% demand factor: 364-Poles, Towers & Fixtures; 365-overhead Conductors & Devices; 366-Underground Conduit; 367-Underground Conductors & Devices; 368-Line Transformers. AEEC and HHEG disagree with this method and instead propose to classify larger portions of the system as customer-related. AEEC witness Falkenberg proposes to include a customer component for all distribution plant below the substation, arguing that accounts 364-368 should be classified as partially customer-related because the investment is related to the number of customers and their geographic dispersion and should be reflected in a minimum system. T. at P1101.

Mr. Falkenberg says industry standard practice as well as the 1992 NARUC Cost Allocation Manual call for treating these accounts as being both demand and customer

related. T. at P675-676. He also says the current allocation method penalizes industrial customers by making them subsidize residential customers and recommends that the Commission direct EAI to perform a study to determine the proper allocation between demand and customer costs for accounts 364-368. T. at P681.

HHEG witness Blank disagrees with EAI's allocation method as it relates to line transformers and secondary lines. For line transformer costs, Mr. Blank recommends the Commission classify these costs as 30% customer-related and 70% demand-related. For secondary distribution costs, he recommends the Commission classify the costs as 37% customer-related and 63% demand-related. For both line transformer and secondary line costs, Mr. Blank also recommends that the Commission modify EAI's allocation methodology by applying EAI's weighted customer allocation ratios to the customer-related secondary distribution costs and EAI's non-coincidental maximum demand allocation ratios ("NCP at Meter") to the demand-related costs. T. at P550-553.

AG witness Marcus agrees with EAI's method and points out that this method for allocating the cost of accounts 364-368 has been adopted by the Commission in a number of general rate cases for the investor-owned electric utilities including EAI's last general rate case. T. at P1101. Mr. Marcus testifies that AEEC's minimum system method is flawed because it relies on the notion that there is a cost correlation between area and the number of customers. Mr. Marcus argues that most utilities will only extend their lines and provide service (at the utility's expense), if the utility believes it can recover an adequate revenue stream. Mr. Marcus says a policy such as this means the expansion of the distribution system is driven by demand and "not the mere existence of customers." T. at P1102.

Staff also opposes AEEC's proposed minimum system method saying AEEC and HHEG did not present a convincing argument that some portion of accounts 364-368 should be allocated based on the number of customers by class. Brief at 17.

The Commission agrees with EAI, Staff and AG that accounts 364-368 should be allocated to the customer classes using a 100% demand methodology and find that AEEC and HHEG do not provide sufficient evidence to warrant a determination that these accounts reflect a customer component necessary for allocation purposes. The Commission, therefore, rejects AEEC and HHEG's recommendation to allocate a portion of the costs of these accounts based on a customer demand factor and direct allocation of these accounts as recommended by Staff.

Separate Rate Classes for LGS Service

EAI's cost of service study aggregates the following four different rate schedules into a single rate class: (a) Large General Service (LGS), (b) LGS Time of Use (GST) - (Demand 100-1000 kW), (c) Large Power Service (LPS), and (d) LPS Time of Use (PST) – (Demand Over 1000 kW). HHEG witness Blank argues these are very different rate schedules with distinct rates and should not be bundled into one rate class. T. at P555-556. Mr. Blank says there are two problems with combining these four rate schedules into one. First, the Commission has no way of knowing whether the overall EAI-proposed percentage increase for these individual rate schedules is reasonable as would be assessed on a cost of service basis. Second, he says the Commission has no way of knowing whether the magnitude of the individual rate elements in the rate design are reasonable as would be assessed on a cost of service basis. T. at P559.

Mr. Blank recommends that the Commission order EAI to prepare a new cost of service study that separates these four rate classes in a fashion that would provide a revenue requirement specific to each schedule and the ability to identify customer-related, demand-related, and energy-related costs for each schedule. If the Commission is unable to direct EAI to do this now, then Mr. Blank recommends requiring EAI to do so in the next general rate case. T. at P560.

Mr. Blank notes that EAI proposes to apply a fixed 29.82% increase to each component of the rates of each of the four rate schedules without a cost of service to measure rate impact on each individual schedule. Mr. Blank argues that by combining these four schedules, the Commission cannot determine whether the proposed rates are just and reasonable at current costs. Mr. Blank gives two examples of cost of service data he says are important but not included in EAI's cost of service. First, he says that EAI's cost of service results do not provide specific revenue requirement targets for these individual rate schedules (LGS, GST, LPS, and PST) and, therefore, the Commission and the parties cannot know how much the proposed rates deviate from cost of service for each rate schedule. Second, Mr. Blank points out that EAI's cost of service does not provide the functionalized and classified costs for each rate schedule so as to distinguish between customer-related costs, demand-related costs, and energy-related costs, which are obviously important for rate design considerations. T. at P557-558.

EAI witness Pettett disagrees with Mr. Blank's recommendation to separate the LGS rate class into four rate schedules; LGS, LPS, GST and PST. Mr. Pettett says the customers under the four individual rate schedules within the LGS rate class are not so

different in load characteristics to warrant the creation of four separate rate classes. T. at P460. He also states that aggregating the LGS rate class is consistent with the creation of other rate classes that have multiple rate schedules within a rate class. For example, the Small General Service (SGS) rate class contains the following rate schedules: Small General Service, General Farm Service, Community Antenna TV Amplifier Service, Municipal Pumping Service, Agricultural Water Pumping Service, Cotton Ginning Service and Traffic Signal Service. T. at P461.

Mr. Pettett also points out that no other party in this docket or in past rate cases has suggested that EAI's cost of service has been incomplete because it did not file separate minimum filing requirement schedules for each rate schedule within the LGS rate class as proposed by Mr. Blank. T. at P460. Because EAI did not prepare detailed information on each of the four rate schedules, Mr. Pettett says he has no way of knowing if the four rate schedules should in fact be separated. He does make a commitment in his Sur-Surrebuttal that EAI will evaluate in its next general rate proceeding whether any or all of the LGS rate schedules should become a separate rate class based on diversity of load characteristics. T. at P482.

The Commission finds that the data necessary to separate these four rate schedules within the Large General Service class within this case is not sufficient. However, the Commission also agrees with HHEG that, given the size and complexity of the four rate schedules which make up this class, data related to each schedule should be maintained by EAI sufficient for it to prepare, in its next rate filing, a Cost of Service Study (COSS) that separates the current LGS rate schedule into the four following classes; LGS, LPS, GST, and PST.

Adjustment for Wholesale Base Load (WBL)Production Demand Allocation Factor

EAI witness Castleberry testifies that EAI wholesale service essentially has no load. In its current cost of service model, EAI allocates 99.987% of production costs to retail. Currently, 100% of the capacity costs for the Ouachita and Hot Spring plants have been assigned to retail. In Docket No. 12-038-U, the APSC approved EAI's request to assign the 154 MW of available ANO Wholesale Baseload capacity to retail. All of EAI's other generating costs are currently allocated 86.13% to retail. EAI proposes to update the production cost allocation factor to 99.987% to retail. This will also have an impact on Rider ECR. Castleberry Direct at 18-19.

According to Staff witness Butler, in order to recognize use of its generation by wholesale customers, EAI proposes to credit its retail revenue requirement for its wholesale sales ($35,234,925) then adjust its proposed retail PDAF to 99.9987%.[26] Staff witness Butler notes that, by using this PDAF, EAI assigns virtually all costs related to certain capacity sold (WBL[27]) to retail and also increases the retail allocation of costs for gas and hydro units. Butler Direct at 5-10. She states that EAI's method is inconsistent with the Commission's findings in Order No. 9 in Docket No.03-028-U and Order No. 7 in Docket No. 12-038-U that certain Wholesale Baseload Capacity be sold and not retained to serve retail load. Butler Direct at 7.

Rather than using EAI's wholesale revenues as an offset to revenue requirement, Staff witness Butler recommends that the investment in and expenses of the WBL sales be removed from rate base and expenses, respectively, for the calculation of revenue

[26] EAI retains one small wholesale customer, i.e. AECI.
[27] EAI sold to the other OpCos 572 MW of WBL capacity (portions of ANO, ISES, White Bluff & Grand Gulf) previously used by EAI to serve wholesale.

requirement.[28] As detailed below, the revenue requirement difference between Staff and EAI is an increase to revenue requirement under Staff's method of $0.8 million :

Adjustment	Staff	EAI	RevReq
EAI AJ26 Credit Wholesale Revs	-0-	(35,234,925)	(35.2 mil)
EAI Total RevReq			(35.2 mil)
Staff RB-26 Remove	(107,027,123	-0-	(7.4 Mil)
WBL Investment from Rate base		-0-	
Staff IS-26 Remove	(26,917,502)	-0-	(27.0 mil)
WBL Expenses		-0-	
		-	
Staff Total RevReq			(34.4 mil)
EAI Minus Staff			+ .8 mil

Butler Direct at 4.

Based on information available, Ms. Butler concludes that the increase in allocation of the Lake Catherine, Remmel, and Carpenter Units to retail is economically justified. Butler Direct at 8; *See RLB-1*. However, Ms. Butler does not have enough data to justify the increased allocation to retail for the Mabelvale Units and recommends EAI provide such data in Rebuttal. Butler Direct at 9-10.

AEEC witness Falkenberg is concerned that the Company not include costs from the surplus Grand Gulf, White Bluff and ISES Wholesale Base Load Capacity in retail rates. Mr. Falkenberg testifies that the treatment appears to be correctly done currently, but the Commission should make sure that the costs are properly excluded, or offset,

[28] This would be done via allocation between wholesale and retail use of the generation.

rather than offset by actual revenues from sales from those resources, if any, in future cases. Falkenberg Direct at 61-2.

EAI witness Hunt explains that EAI sells portions of its capacity of ANO, White Bluff, and Independence plants to its other OpCos. As such, EAI ratepayers should be insulated from those costs, which can be accomplished by either crediting revenues from wholesale sales to retail, or by allocating the plants' costs to wholesale and out of retail. EAI proposes to credit the revenues to the retail cost of service which Mr. Hunt maintains is reasonable. He states that the primary difference in results from this method, as opposed to allocation/assignment of generation costs, relates to the equity return included in the WBL FERC tariff which generates those wholesale revenues. Mr. Hunt testifies that EAI uses the revenue crediting method because it is simple. Hunt Rebuttal at 7-9.

Mr. Hunt testifies that Staff witness Butler uses a cost allocation method different from EAI's based on Staff's interpretation of Order No. 9 in Docket No. 03-028-U (wherein the Commission directed EAI to address ratepayer protections for certain riders - Hunt Rebuttal at 9, footnote 7) and Order No. 7 in Docket No. 12-038-U (WBL Orders), Hunt Rebuttal at 9. Mr. Hunt, states however, that the WBL Orders do not specifically address this cost treatment issue. Nor, he notes, does EAI find its revenue crediting method inconsistent with those Orders, noting the Commission has demonstrated an interest in a variety of methods. Hunt Rebuttal at 9-10.

EAI, however, does not object to Staff's method. Staff's method would reduce revenue requirement by $34,319,948, while EAI's method would reduce revenue requirement by $35,831,703. Hunt Rebuttal at 9.

EAI agreed to Staff's methodology to address Wholesale Base Load capacity sales. Staff updated its adjustments to reflect Staff's Surrebuttal case. Staff agrees with EAI's proposal to allocate additional capacity for Mabelvale Units 1 and 3 to retail. Butler Surrebuttal at 2-5.

AEEC witness Falkenberg testifies that the retail/wholesale allocation of capacity differences between Staff and EAI should be reconciled. Falkenberg Surrebuttal at 59-60.

The Commission determines that Staff's method for allocating production demand costs between retail and wholesale appropriately assigns the costs incurred by retail customers for their use of production rather than the alternative method which simply credits revenues back to retail customers wholesale sales. Staff's method is consistent with prior Commission's findings in Order No. 9 in Docket No.03-028-U and Order No. 7 in Docket No. 12-038-U that certain Wholesale Baseload Capacity be sold and not retained to serve retail load. Staff provided further detail of its method in its response to the Commission's October 30, 2013 instructions, and submitted late-filed Staff Hearing Exhibit 9 on November 6, 2013. The assignments and allocations of generating units are shown in Attachment 1 to that response and are consistent with the Commission Orders in Docket Nos. 96-360-U, 03-028-U, and 12-038-U. As part of this determination, the Commission agrees with Staff concerning the additional allocations of Lake Catherine 4, Carpenter Units 1 and 2, Mabelvale Units 1 and 3, and Remmel Units 1, 2, and 3 to retail. The Commission also notes that the calculations in Rider ECR should reflect these retail assignments/allocations which the Commission will discuss later this Order.

Cost Allocation Mitigation

EAI and Staff each developed a cost of service study that resulted in an overall system increase in the revenue requirement. A revenue requirement increase was allocated to the Residential and Small General Service (SGS) classes, while the largest increase was allocated to the Large General Service (LGS) class. Finally, the Lighting class was allocated a revenue requirement surplus. In reviewing the overall impact of the allocation of the revenue requirement, Staff witness Klucher states that Staff first considers the total increase in base rates and the total bill impact for each customer class and then makes mitigation recommendations that will achieve a just and reasonable result for all classes.

Consistent with prior rate cases, Mr. Klucher proposes that no individual customer class receive a rate decrease in the context of an overall system increase. To mitigate the adverse rate increase, Mr. Klucher recommends distributing the revenue surplus from the Lighting class to the LGS class, since the LGS class was the only class allocated a larger-than-system-average increase. T. at P2081. Mr. Klucher points out that even after the redistribution from the Lighting class, the LGS class remains significantly higher than the system average. He believes additional mitigation is needed and recommends adjusting the SGS class up to the system average and adjusting the Residential class up to three-quarters (75%) of the system average.

Mr. Klucher proposes using the resulting surplus to reduce the revenue deficiency of the LGS class. T. at P2099-2100. Mr. Klucher summarizes his mitigated cost of service results in Table 8 of his revised Surrebuttal Testimony. Mr. Klucher believes the results of his proposed rate mitigation achieve a just and reasonable result

by tempering the rate increase to the LGS class while keeping the base rate increase to all other classes virtually at or below the system average. T. at P2100.

EAI witness Pettett points out that Staff's recommendation does not follow the cost causation principle, but it may have merit from a public policy perspective of gradually moving the LGS rate class to its full cost-of-service. T. at P453.

AG witness Marcus recommends rejecting Staff's mitigation proposal and instead recommends two alternatives, which he presented during the hearing. T. at E3170-3176. Mr. Marcus recommends a mitigation plan that would set the Residential class rates at between 50%-60% of the system average. Mr. Marcus says his plan sets rates that are much closer to "cost to serve" rates and which follow the principles in the settlement that was approved in EAI's last rate case, Docket No. 09-084-U. Brief at 4.

The Commission finds that Staff's rate mitigation plan achieves a just and reasonable result. The Commission therefore directs Staff to distribute the approved revenue requirement in such manner that any allocated revenue surplus be redistributed to the LGS class. In addition, the SGS class shall be allocated a revenue requirement equal to the system average and the Residential class shall be allocated a revenue requirement equal to 75% of the system average. While other mitigation plans could also be reasonable, the Commission finds that Staff's mitigation plan results in a more balanced outcome.

XV. Rate Design

Residential Customer Charge and Rate Blocks

Based on its cost-of-service study, EAI has proposed to increase the residential customer charge to $9.00 from the existing $6.96 per month, a 29.3% increase. EAI

witness Pettett testifies the proposed increase reflects cost based rates and moves the customer charge closer to the cost of providing service. T. at P489. Mr. Pettett says the proposed energy charges for these rate schedules will be reduced from those otherwise required by the overall residential increase to offset the additional revenue from the additional customer charge increase. T. at P383.

Staff witness Swaim initially appeared to agree with EAI's proposed increase, stating in his Direct testimony that "it may be reasonable" to increase the residential customer charge to $9.00 per month. T. at P1202. In his Surrebuttal testimony, Mr. Swaim continued to support his original position that a $9.00 customer charge "may be reasonable," saying an increase to the customer charge would more closely approximate the results of the cost of service study. He also compared EAI's proposed customer charge to the other three jurisdictional investor-owned electric utilities' customer charges, which are $7.75 for Southwestern Electric Power Company, $7.94 for Oklahoma Gas and Electric Company, and $10.00 for The Empire District Electric Company. T. at P1222. As for the block rates, Mr. Swaim recommends maintaining the current energy rate structure by increasing the rates for each block by the same percentage as proposed by EAI. He says an equal percentage increase in each block's rate will increase the differential in the summer inclining blocks and reduce the differential in the winter's declining blocks, both of which will promote energy efficiency. T. at P1222-1223.

During cross-examination in the hearing, Mr. Swaim was asked to clarify his position. He stated that he was now "recommending something like 8.24 percent" as an increase to the monthly residential customer charge. T. at 1183. During the hearing, Mr.

Swaim also agreed with Mr. Marcus' position to keep the customer charge unchanged, but only if the Commission decides there is an overall decrease in rates. T. at 1185.

AG witness Marcus recommends that the Commission reject EAI's proposed increase and instead recommends the Commission accept the AG's proposal to freeze the monthly customer charge at $6.96. Marcus also believes that Staff's recommended increase of 8%, which he calculates would raise the customer charge to about $7.52 is too great and will discourage conservation. Reply Brief at 11. Mr. Marcus argues that Staff's 8% increase is merely based upon the percentage increase in base rates and ignores the undisputed fact that the total bill impact resulting from this case (after Rider PCA goes away), will be a decrease in the bills for all classes. With this in mind, Mr. Marcus says that freezing the customer charge when residential customers will see an effective decrease (or only a nominal increase) in bills is the only reasonable rate design. Mr. Marcus also believes Staff's approach contradicts the Commission's directive in Order No. 19 in Docket No. 08-137-U, which encourages customer charges to be set at a level low enough to encourage conservation. Reply Brief at 12.

As part of his proposal to freeze the customer charge, Mr. Marcus also recommends that the Commission not lower the summer inverted block second tier rates or the winter declining block second tier rates. Specifically, he proposes that base rates be increased in the second incremental tier in an amount that would at least recover the decreases in riders in that tier in both summer and winter. This will effectively hold the second tier rates constant. Secondly, he proposes that all decreases (base plus rider rates) be applied to first tier energy charges. These two changes will

have the effect of increasing the summer tier differential and reducing the steepness of the winter declining block rate, which will encourage energy conservation. T. at P1039.

The Commission finds the AG's recommendations in this case appropriately assign costs to those components of the rates which will provide incentives for conservation. The Commission, therefore, approves the AG's residential rate design proposal, which includes leaving the residential customer charge at its current amount of $6.96. The Commission also approves the AG's proposal to increase only the second block rates (summer and winter) if there is a net increase to rates (base rate plus riders). If there is a net decrease to rates, the Commission adopts the AG proposal to lower the first summer block rate which would increase the differential. The first winter block rate would also be reduced which will decrease the differential, since it is declining.

Excess Demand Charges on GST and PST

HHEG witness Blank states that there are significant differences in the rates between Large Power Service - Time-of-Use (LPSTOU) and Large General Service – Time-of-Use (LGSTOU) for customer and demand charges and both schedules have the same energy charge. He says that because LPSTOU, having demand over 1,000 kW, would likely have less excess demand at peak than would LGSTOU (100-1000 kW), less cost should have been allocated to LPSTOU (which is not reflected in the demand rates.) Blank says that absent a cost of service study, there is no way to tell how much these rates deviate from cost. Thus, Mr. Blank concludes, given that EAI's proposed rates were determined applying a flat 29.82% against all components of the schedules it is likely that the Time-of-Use (TOU) rate design was flawed. T. at P561-562. Mr. Blank proposes that the LPSTOU and LGSTOU, therefore, be designed using the LPS and LGS

differentials. Using EAI's initially filed revenue requirement and cost of service, Mr. Blank designs and recommends increases to rates to LPSTOU of 28.33% and to LGSTOU of 33.10%. T. at P564.

EAI witness Pettett says EAI is willing to propose a new rate design that combines LGSTOU AND LPSTOU rate schedules. T. at P456-460. Staff states the rate designs HHEG opposes have been in existence for more than twenty years. Absent a customer impact study, Staff recommends the rejection of HHEG's proposal. T. at P1227.

The Commission rejects HHEG's proposal at this time, absent data to support the increases proposed, and directs EAI to keep data sufficient to appropriately design the components of the rates for GST and PST customers to be used in EAI's next rate case. The Commission adopts increases to the components of these rate schedules based on the overall increase for the rate class to which they are assigned.

LGS Minimum Billing Demand

HHEG witness Blank asserts that the LGS, GLSTOU, LPS, and LPSTOU customers' minimum payment of demand (at either 100 KW or 1000 KW) is unduly discriminatory against customers whose demand hovers around the qualifying minimum, given that customers with higher demand will only pay for their actual demand. He argues that EAI already has a minimum bill based on a demand ratchet (which requires the payment of the highest demand from the past 12 months at reduced demand rate). He also points out that EAI provided no cost basis for this treatment. Mr. Blank recommends the Commission consider a demand ratchet at actual demand charges, but because of current lack of data, recommends the Commission simply

abolish this provision and have customers under these rate schedules pay only for actual demand. T. at P564-566.

EAI witness Pettett opposes HHEG's request to eliminate the minimum demand provisions for LGS, LGSTOU, LPS, and LPSTOU. T. at P456-460. Mr. Pettett argues that if the demand definition provision where eliminated as suggested by Mr. Blank, EAI would have to find another way to recover an estimated $1 million in lost revenue. T. at P490-491.

The Commission finds that the current revenue requirement recovery is based on the billing determinants under the current schedules, including the minimum demand levels and therefore rejects HHEG's proposal. EAI is directed to keep appropriate data for purposes of exploring alternatives to the minimum demand billing in its next filed rate request.

Demand Charge Allocation/LGS Class

Wal-Mart witness Chriss notes that EAI proposes to use the percent of increase to each class as applied to each component of current rates to set new rates. The result for LGS customers is that only 51.3% of its revenue requirement is in the demand rate, with 46.43% in energy charges. As for LGS-Time-Of-Use Customers (LGSTOU), EAI's proposed rate structure will collect 65.66% of revenue requirement through the demand charge and 33.01% through energy charges. Wal-Mart witness Chriss argues that EAI's proposed rate structure for the LGS customers is inconsistent with the unit cost results from EAI's cost of service study, which shows that almost 88% of revenue for the LGS class, as a whole, should be classified as demand related. He explains that increasing the energy related factor will result in shifting demand cost responsibility from lower

load factor customers to higher load factor customers. Mr. Chriss says this will result in a misallocation of cost responsibility to customers as higher load factor customers overpay for the demand related costs incurred by EAI to serve those customers. T. at P19-20. Mr. Chriss recommends that the demand related factor for LGS customers be increased to 65.66% which is equal to the demand related factor for LGSTOU customers. T. at P23.

Staff witness Swaim recommends rejecting Wal-Mart's proposed adjustment to the LGS rate structure. Mr. Swaim says the LGS-Time-of-Use rate was developed to encourage high load factor customers to avoid the consumption of energy and demands during EAI's system expected peak load hours.

The Commission finds that the demand rates are based on the cost of service and allocation methods which it has already found to be reasonable, reflective of cost causation, and, therefore, in the public interest. The Commission also finds that the rates for LGS-Time-of-Use rates are designed to discourage both demand and consumption by those TOU customers during high demand peak periods and, therefore, reflect appropriate design. Alternatively, the rates designed for non-TOU customers, based on the Commission-approved methodology, have been designed to reflect the usage and demand of those customers. The Commission, therefore, rejects Wal-Mart's proposal to increase the proportion of revenues recovered through demand charges of LGS customers from the 51.12% proposed by EAI to the 65.39% proposed for the LGS – Time-of-Use (GST) customers.

XVI. Rider OIS Rider

EAI proposes to close the Optional Interruptible Service Rider, Rate Schedule 41, (Rider OIS) to new customers and also proposes significant changes to Rider OIS for current customers. Currently under Rider OIS, customers[29] may contract with EAI to use interruptible service during on-peak hours. Under Rider OIS, on-peak hours are 1:00 p.m. through 8:00 p.m., Monday through Friday during summer months and 7:00 a.m. through 6:00 p.m. Monday through Friday for other months of the year. Currently EAI will notify the Customer by 4:30 p.m. that, on the following day, EAI may call for an interruption. This is called "Day-Ahead Notice." This notice provides an estimated starting time for the interruption. Under Rider OIS, interruptions may currently be called, if EAI is expecting a Peak Load Condition as defined in the tariff or is experiencing a Capacity Shortage Condition as defined in the tariff or is experiencing an emergency condition. Customers are subject to a maximum of one interruption per day for no more than 4 hours during the summer months and 3 hours in non-summer months. A customer may only be subject to interruption during summer months no more than 10 days per month and no more than 35 hours per month. There are certain pricing penalties if the customer does not reduce demand if called upon to do so.

Customers taking service under Rider OIS pay the currently effective firm demand charge under the applicable standard rate schedule only for the amount of kW demand the customer designates as "firm." The customer is not charged for any kW demand it takes in excess of that designated firm level. However, the Rider OIS customer must reduce its kW demand to its designated firm demand level when an

[29]Small General Service, Large General Service, Large General Service Time-of-Use, Large Power Service, or Large Power Service Time-of-Use who are willing to contract with EAI for interruptible power during on-peak hours.

interruption is called. Thus, the "pricing" or "compensation value" for the interruptible service or the "credit" applicable to that service is the current effective firm demand rate which the customer does not pay. *See* EAI Rate Schedule 41. This mechanism by which that interruptible "credit" to EAI's Rider OIS customers is set is the mechanism approved pursuant to Order Nos. 35 and 38 in Docket No. 96-360-U and has been in effect for approximately fifteen years. *See* Staff Initial Brief at 19.

In support of its proposal that Rider OIS should be closed and in support of the proposed changes to Rider OIS, EAI states that Rider OIS is obsolete and currently reflects the utilization of interruptible load under the Entergy System Agreement (ESA) and does not reflect EAI's participation in MISO. EAI argues that Rider OIS does not contemplate EAI's access to the MISO market for capacity and does not reflect MISO's procedures for utilizing interruptible demand. *See* EAI Initial Brief at 18. EAI witness Pettett argues that the current Rider OIS does not align with EAI's transition to MISO and, therefore, changes to Rider OIS are needed. EAI, thus, proposes to close Rider OIS to new customers and to make several changes to the tariff. EAI proposes changes to the notice provisions (to give no more than twelve hours' notice for interruption); to the duration of interruptions (EAI proposes to change the non-summer months' interruption duration, which is currently 3 hours, to 4 hours) T at P1615-1616; and to the penalty provisions. EAI asserts such changes will mimic MISO's current Load Modifying Resource (LMR) market product requirements. Additionally, EAI has added a requirement that Rider OIS customers must register with MISO through EAI and be verified as an LMR and has added provisions which would terminate a customer's

participation in Rider OIS if the customer fails to meet eligibility requirement for two consecutive years. T. at P389-391 and T. 499-500.

EAI witness Castleberry concludes that "[b]ecause the MISO market provides the mechanisms for, and sets the compensation value for participation by an interruptible customer, EAI no longer needs its Optional Interruptible Service Rider ("Rider OIS") ..." and will seek, at a later time, to phase out that tariff. In the interim, witness Castleberry testifies that changes are needed to the existing Rider OIS to make it consistent with MISO's LMR – Demand Response Product. T. at P1590. Once qualified as an LMR, Rider OIS customer interruptible load will be used to meet EAI's MISO resource adequacy requirements. T. at P1614.

Additionally, in conjunction with the changes to Rider OIS, EAI witness Pettett proposes two new tariffs, the Market Valued Load Modifying Rider (Rider MVLMR) and the Market Valued Demand Response Rider (Rider MVDRR), which EAI will offer to new customers wishing to offer interruptible load and which will replace Rider OIS. T. at P391-392. These are two experimental tariffs which EAI states will provide its commercial and industrial customers, including existing Rider OIS customers, access through the Company to MISO's capacity and energy markets. EAI Initial Post-Hearing Brief at 22.

Staff witness Butler states that Staff recommends approval of the changes to Rider OIS, with "the appropriate long-term disposition of Rider OIS ... [to be] evaluated when EAI gains experience in MISO." T. at P3007. Staff also recommends approval of the MVLMR and MVDRR, with the further recommendation that EAI keep the pertinent

cost data on its activities "to more fully justify the charges and penalties proposed in the riders." T. at P3008, P3027-3029.

As addressed by its witness Marcus, the AG does not oppose changes to Rider OIS, but recommends any changes be the minimum needed to reflect MISO's LMR qualification. T. at P1053-1054.

AEEC recommends Rider OIS remain open and, as addressed by witness Falkenberg, objects to both closure of Rider OIS to new customers and its future phase-out, citing the adverse rate impact to Rider OIS customers and the benefits they provide, including the use of interruptible service in the stead of EAI's other generation capacity options and reductions to distribution and transmission capacity needs. T. at P716, P745-746, P706-710, P733. AEEC asserts that EAI fails to show that current Rider OIS pricing does not reflect the "value" of interruptible load and, therefore, EAI fails to show that the tariff's closure is necessary. According to AEEC, pursuant to Commission findings in its Order No. 35 in Docket No. 96-360-U, rates, including the rates or "credits" for interruptible service, are based on cost and not the "value" to other customers and to set interruptible rates on "value" rather than cost would discriminate against non-firm service. T. at P 737-738.

AEEC also offers alternatives both to EAI's proposed 12-hour notification provisions and to the changes to hours of interruption, noting such changes are not required by MISO, nor is MISO registration. T. at P717. T. at P739-743. AEEC, in addition, recommends that Rider OIS credits be effectively increased by eliminating the "excess" demand charge for Time-of-Use customers, which is applied to the non-firm

demand,[30] contending large customers already pay substantial demand costs within the kWh charges and, thus, the excess demand charge is not appropriate. To avoid any undue discrimination against non-TOU customers, AEEC suggests a reduction in the kWh charge for non-TOU customers as a means to address any disparity. T. at P716, P736-737.

With regard to the MVLMR and MVDRR, AEEC objects to EAI's proposed pricing under these tariffs, which AEEC claims EAI has incorrectly tied to MISO's capacity auction and which violates the Commission's findings regarding the pricing for interruptible service as reached in its Order No. 35 in Docket No. 96-360-U. T. at P710-711.

HHEG opposes EAI's proposed changes to Rider OIS, including its closure to new customers. HHEG witnesses Kenneday, Mathis, Howard, Millay and Jeffries identify the negative impact such changes would have to customers and recommend the Commission reject these changes, including any future phase-out of the tariff. T. at P1990 to 1994, P3042-3044, P2900-2914, P2887-2889, P2923-2926. HHEG witnesses Blank and Howard, respectively, note the harm in closing the tariff to new customers who "may want to expand interruptible load at other service locations or move existing service locations to new locations..." and who will be unable to use EAI's proposed MVLMR and MVDRR. T. at P608-609, P2915.

Opposing closure of Rider OIS to new customers, HHEG witness Kenneday rebuts EAI's contentions: (1) that such closure is necessary because Rider OIS no longer appropriately values interruptible service and (2) that the MISO markets more

[30] Excess Demand is charged for non-peak kW demand for Large General Service Time-of-Use (TOU) customers and Large Power Service Time-of-Use (TOU) customers. Application, Schedule H-10, RS7 and RS9.

appropriately reflect that value. T. at P2027. Objecting to EAI's valuation of interruptible service at incremental or marginal cost of generation in MISO markets rather than embedded cost, Mr. Kenneday outlines the Commission's findings in Order No. 35 of Docket No. 09-360-U in which the Commission rejected the use of incremental savings to other customers for pricing interruptible service and set that pricing based on fully embedded cost of the firm service no longer provided. T. at P2027, P2034, P2042. Mr. Kenneday further rebuts EAI's contention that, with EAI's exit from the ESA, interruptible service must align with MISO markets and testifies that the pricing of interruptible service under the current Rider OIS "aligns with the pricing for firm service and not the ESA...[and that, because Rider OIS]... never aligned with the ESA, it need not align with MISO." T. at P2043-2044.

HHEG witness Jeffries also recommends rejection of EAI's proposal to close Rider OIS and to value interruptible service based only as a MISO planning resource, citing multiple studies and papers which address the appropriate valuation of that service. She testifies that EAI's proposed valuation reflects "only one limited aspect of the beneficial impact of demand response ..." and lists other benefits and conclusions cited by the studies which support her recommendation. T. at P. 2931-2935.

HHEG objects to the other multiple EAI proposed changes to Rider OIS which witness Blank asserts are not required for EAI's integration into MISO and recommends the Commission make no such changes, noting also the tariffs of other MISO-member utilities which contain no such provisions. T. at P529- 531, P536. E604, E609, P615. Specifically, Mr. Blank objects to changes made (1) to penalty provisions, noting that Rider OIS penalties are likely greater than those imposed by MISO, (2) to the 12-hour

notice provisions, asserting that EAI incorrectly incorporates MISO's LMR eligibility requirement into the tariff, (3) requiring MISO registration, which is not required by MISO and that given EAI as LSE would be the responsible market participant, and (4) to interruption duration for non-summer months from 3 hours to 4 hours, which is not required for LRM qualification. T. at P531,.P534-536 ,P609-611, P613, P615. Mr. Kenneday recommends EAI's changes to the termination provisions be rejected as unsupported and vague, because they allow EAI to unilaterally terminate service and, are inconsistent with Commission findings in Docket No. 96-360-U. T. at P2053-2055.

HHEG also recommends that the MVLMR and MVDRR be disapproved, with HHEG witness Ward citing, as support for that recommendation, the ambiguity of MVLMR and its unnecessary MISO registration provisions, and the pricing risk under the MVDRR in an untested market as well the MVDRR's 10% administrative fee tied to settlement costs, which is not known and measurable, which EAI fails to support, and which has no correlation to settlement costs. T. at P634, P631-633, P654-656. HHEG witness Millay further testifies to these tariffs' uncertainties, insufficient information, and experimental nature, and concludes that "[t]he proposed riders increase risk for stranded cost and increase volatility in utility cost for participants." T. at P2889- 2890.

HHEG witness Blank also supports AEEC's proposed elimination of the excess demand charge on large Time-of-Use (TOU) customers as appropriate, asserting the charge penalizes large customers who can shift demand. Mr. Blank, however, proposes elimination of the charge for all TOU customers, not just Rider OIS customers. Mr. Blank further recommends that, because data is not available and for purposes of this

rate case, the resulting reduction in revenues, which was not addressed by AEEC, be offset by an increase to the seasonal on-peak demand charge. T. at P600-601.

Mr. Baker, on behalf of Wal-Mart, recommends the Commission approve the "grandfathering" provision of EAI's proposed Rider OIS to ensure customers will recoup their Rider OIS investments and has further concerns that the MVLMR and MVDRR do not clearly set out options under these demand response tariffs concurrent with those available under the Commission's energy efficiency programs. T. at P6-11.

Evergreen witness Elmore testifies that, pursuant to MISO tariffs and business practices, retail customers are not required to participate in MISO through a MISO member, nor is there any such provisions which require a MISO utility member to change its retail interruptible tariff terms. T. at P41-42, 43. Mr. Elmore further testifies to the flaws in both the MVLMR and MVDRR. T. at P43-44.

EAI continues to recommend closing Rider OIS to new customers because the MISO markets, not the ESA, will set the mechanisms and pricing for interruptible service. T. at P1612-P1613. Mr. Castleberry addresses AEEC's and HHEG's rebuttal of his testimony that Rider OIS's current pricing for load interruption is no longer valid. Mr. Castleberry asserts that these parties argue for maintenance of a tariff approved some 15 years ago which was designed to reflect value within the ESA and ignores the new MISO structures. T. at P1620, P1658-1659. Mr. Castleberry states that Rider OIS current fixed prices, which are based on embedded generation costs and are significantly higher than the prices for one-year capacity available in MISO, are no longer appropriate and their use would negate expected benefits MISO integration would bring. T. at 1659-1660.

Mr. Castleberry rebuts HHEG's reference to other MISO-member utilities' tariffs as evidence no changes are needed. Mr. Castleberry notes that credits provided under these tariffs are much lower than under Rider OIS and further AEEC's comparison of interruptible load to other EAI capacity resources, given the short-term nature of interruptible load in comparison to the long-term nature of those other resources. T. at P1662-1664 , P1661.

Mr. Castleberry also rejects contentions that the Commission, in Docket No. 96-360, directed pricing for Rider OIS be set by the costs to EAI and not the "value" of the service and notes that the Commission directed, in that Docket, the parties

> '. . . to work together to develop an interruptible tariff which (1) will be operationally useful to customers and EAI, (2) will be economically justified, and (3) will not result in cost shifting or cross-subsidization among classes.'

Thus, Mr. Castleberry states the Commission was concerned, not only with pricing, but with whether the tariff was "economically justified" and "not result in cost shifting...among classes." In that regard, Rider OIS, providing short-term capacity, is currently priced significantly higher than similar resources in the MISO market. T. at P1668 and P1668 footnote 19, P1669. Mr. Castleberry further rejects AEEC's comparisons of interruptible load to other capacity EAI has recently acquired and reiterates that the value of Rider OIS in MISO is "more akin" to the value found in MISO's capacity auction and not those referenced by AEEC. T. at 1621.

EAI continues to support its MISO LMR registration provision. Mr. Castleberry agrees that, while not required for EAI membership in MISO, in order for interruptible load to meet MISO's resource adequacy requirements and to provide value to EAI and

its customers as a MISO planning resource, i.e. as an LMR, registration is required. T. at P1614.

EAI also continues to support the change in the interruption duration for non-summer months. Mr. Castleberry testifies that, to qualify as an LMR, the customer must demonstrate a capability to sustain demand reduction for a minimum of 4 hours. T. at P1615-1616. Mr. Castleberry further testifies that "MISO does not state that LMRs will not be deployed during non-summer months..." and therefore these provisions are appropriate, with these additional interruptions further supporting the value of the credits currently provided to Rider OIS customers. T. at P1616-1617.

EAI, in its Sur-Surrebuttal, amended its originally proposed changes to the notice provisions of Rider OIS. EAI now proposes a change to those provisions such that EAI will provide minimum notice of 8 hours, instead of in "12 hours or less," as originally requested. T. at P1619-1620, T. at 1455 – 1458, EAI Initial Brief at 20.

EAI also addresses the concerns of the parties related to its originally proposed service termination provisions, which would have terminated service upon a customer's failure to meet eligibility requirements. As addressed by Mr. Pettett, EAI has amended these provisions such that a customer's failure to meet the requirements would have to occur in two consecutive years prior to termination. T. at P1670, P470-471, 499-500.

EAI recommends rejection of AEEC's proposed elimination of the "excess demand" charge and rejects HHEG's contention that the charge penalizes large customers who can shift load to off-peak. EAI witness Pettett testifies that there is no penalty and explains that elimination of the charge is not necessary to provide incentive

for customers to shift to off-peak, given the tariff's on-peak/off-peak rate differentials. T. at P492-493.

EAI continues to recommend approval of the MVLMR and MVDRR and urges the Commission reject HHEG's recommendation to disapprove these tariffs and have EAI collect data on such programs for future tariff consideration. Parties may not wish to take service under these tariffs but the tariffs should be available to those parties who do. T. at P498. EAI also continues to support implementation of the 10% administrative fee under the MVDRR. Mr. Pettett identifies other MISO utilities' tariffs with similar charges within the same range as proposed by EAI. EAI also agrees that it will maintain data to justify fees under its market tariffs in the future. T. at P498-499.

Although the AG and Staff are in agreement with EAI's proposal to close Rider OIS to new customers and with certain EAI-proposed Rider OIS changes which will affect current customers, the other parties vehemently disagree with EAI's proposals regarding the changes to Rider OIS, including its closure to new customers, and the approval of Rider MVLMR and Rider MVDRR as Rider OIS replacements. The evidence before the Commission in this Docket on these issues from all parties is contradictory with a number of factual disputes. There is disagreement among the parties as to what MISO will require regarding Rider OIS or whether EAI's proposal to require the registration of customers as LMR's is a MISO requirement. There is significant disagreement related to the "value" or "pricing" appropriate for interruptible service in future MISO markets. Notably absent is any testimony or participation from MISO on these issues. Therefore the Commission is unable to rule on EAI's request to close Rider

OIS to new customers, approve EAI's requested revisions to Rider OIS, or approve EAI's proposed Rider MVLMR or Rider MVDRR.

However, the Commission is aware that, with the demise of the Entergy System Agreement and with EAI's integration into MISO, some changes to Rider OIS may indeed be warranted. However, within the limits of this rate case, and upon the unclear and conflicting testimony presented, the Commission finds that it is inappropriate to rule on EAI's request to amend Rider OIS or to implement Riders MVLMR and MVDRR. Those questions will be taken up by the Commission in a stand-alone docket where the Commission and the parties can focus on the question of Rider OIS and the appropriate actions to be taken regarding the Rider. Therefore the Commission orders EAI to work with its current interruptible and cogeneration customers regarding any changes to Rider OIS along with any new riders to address MISO demand resource markets and for EAI to file such changes or tariffs in a new tariff Docket.

The Commission, however, notes that the current Rate Schedule 41, or Rider OIS, includes provisions which are tied to the Entergy System. Under Section 41.3, *Notification Provisions*, of Schedule 41, the tariff provides that:

> On the day following the Day-Ahead Notice, if the Company is expecting a <u>*Peak Load Condition*</u>, is experiencing a Capacity Shortage Condition, or is experiencing an emergency condition, the Company may call for an interruption... (Emphasis added).

See Section 41.3, Schedule 41, approved June 23, 2010 by Order No. 20 Docket No. 09-084-U. A *Peak Load Condition* is defined in Section 41.2.5, under Section 41.2, *Definitions*, as:

> those conditions on any day that could result in the <u>*Entergy System*</u> establishing a monthly peak. (Emphasis added.)

Such definition is no longer applicable and the Commission, therefore, directs EAI to refile Schedule 41 with its compliance tariffs and, under the Definition for *Peak Load Condition,* substitute "Company" for "Entergy System." Given the Commission's directive to EAI to file proposed changes to Rider OIS within ninety (90) days of this order, the Commission anticipates little impact with this minor provision change in the interim and anticipates that EAI and its customers will provide alternatives to these provisions in that filing.

The Commission, therefore, rejects EAI's proposed changes to Rider OIS and directs EAI to incorporate the change to Rider OIS as addressed above. The Commission also rejects EAI's proposed riders MVLMR and MVDRR.

XVII. Capacity Cost Recovery Rider

EAI witness Castleberry proposes a Capacity Cost Recovery Rider (Rider CCR) to provide for recovery of the costs of limited-term purchases, including bilateral contracts with other power producers and purchases from the MISO Planning Reserve Auction (Auction). EAI may also sell excess capacity in the Auction if it is beneficial to customers. Castleberry testifies that the need for the new rider is a result of EAI's exit from the Entergy System Agreement (ESA), through which it shared capacity and purchases, and its subsequent integration into MISO. As support for the recommendation, Mr. Castleberry also asserts that Rider CCR would lead to greater participation in EAI's Request for Proposal (RFP) process for purchases, resulting in lower cost. Absent Rider CCR, EAI would have to rely more on owned generation and long-term capacity purchases, which would provide less flexibility in matching generation with projected load. T. at P 1581-1585.

Staff witness Davis explains the provisions of EAI's proposed Rider CCR. Rider CCR would recover capacity purchases and non-fuel capacity portions of purchased power agreements (PPAs). Effective upon EAI's exit from the ESA in December 2013, EAI would annually file its 12-month projected purchases, subject to true-up to actual cost, with any remaining balance subject to a carrying charge. Should the true-up accumulated balance exceed $10 million, interim recovery would be allowed. The charge applied under Rider CCR would be designed based on a percentage of capacity costs to final approved revenue requirement applied to each component of all base rates (e.g. kWhs, kW demand, customer charges). T at P 3065-3066.

In her Direct Testimony, Staff witness Davis recommends rejection of Rider CCR, noting that there was no evidence that such mechanism would result in lower cost offers under the RFP process or that EAI had insufficient capacity. Further, EAI was not eligible to participate in MISO's capacity market. Given other current regulatory options available to EAI, Ms. Davis concluded that Rider CCR was unnecessary. T at P 3067-3070.

Witness Davis, however, also alternatively recommends, should the Commission approve Rider CCR, that the rider be amended such that:

1. EAI be required to provide certain information, as outlined in her Direct Testimony, to support the transactions and costs before they are included in the Rider CCR;
2. No carrying charge on the over/under-recovery balances be allowed; and

3. The trigger point for interim recovery be set at 10%, rather than $10 million, which coincides with the materiality of the cost level. T. at P 3070-3073.

AG witness Marcus recommends that no contracts which exceed a year be allowed to pass through Rider CCR, without prior Commission approval, and also recommends that the residential charge under the rider by designed on a cents-per-kWh basis rather than as a percent of the residential rate components. T. at P 1028-1029.

AEEC witness Falkenberg recommends disapproval of Rider CCR as: (1) single issue ratemaking; (2) a diminishment in EAI's incentive to control cost; and (3) providing a perverse incentive to purchase in the Auction, given costs which might improve generation outage rates would not be subject to recovery. Mr. Falkenberg additionally asserts that Rider CCR lacks sufficient review provisions. Should Rider CCR be approved, witness Falkenberg alternatively proposes that its charges be designed on demand for classes with demand metering and on energy for other customer classes. Additionally, if approved, Rider CCR should be amended to allow for, not only true-up to actual costs from the prior year projected cost, but also a true up of any over/under-recovery to avoid any incentive for "gaming." T. at P 703-705.

In Rebuttal, EAI witness Castleberry advises that EAI had filed for Commission approval to participate in the Auction and that Rider CCR will provide a mechanism through which EAI is best positioned to take advantage of economic opportunities to purchase or sell capacity and provide the benefits and costs to its customers at the same time. T. at P 1627-1630.

Castleberry also recommends that the Commission direct EAI and Staff to work towards jointly developing reporting requirements for Rider CCR. These reporting requirements should also address concerns about "gaming." T. at P 1630-1631.

EAI witness Pettett advises in his Rebuttal testimony that EAI is not opposed to AEEC's and the AG's recommendations related to the design of the charge under Rider CCR. T. at P 461-463.

Mr. Hunt, on behalf of EAI, testifies that EAI continues to support the $10 million "dollar" threshold rather than Staff's proposed 10% change in current contract costs. Staff asserted its proposed treatment is consistent with operation of the Rider ECR, which is tied to the expected amount of costs. Hunt notes, however, that the dollars in the ECR are significantly greater than those generated in Rider CCR and that interim adjustments should only be made if the actual dollar impact is significant. Witness Hunt also argues, as he does with regard to the MISO Rider, that, as with other approved riders, it is appropriate to allow carrying charges on the rider's true-up balances. T. at P 1450-1452.

Staff witness Davis, in her Revised Surrebuttal, notes the Commission's approval of EAI's participation in the Auction by Commission Order No. 77 issued on September 18, 2013, in Docket No. 10-011-U, and that, as a result, EAI anticipates making capacity sales in the market, with the revenues for those sales credited to ratepayers. In order to allow those benefits to flow to ratepayers, Ms. Davis changes her recommendation and proposed that the Commission approve Rider CCR, "with the additional protections recommended by the AG that would allow pass through of capacity transactions of one year or less and pre-approval of longer term capacity purchases." Ms. Davis also

continues to recommend: (1) approval of the reporting requirements outlined in her Direct testimony, which would allow review of the transactions and costs prior to recovery; (2) that no carrying charge be allowed on the difference between EAI's actual costs and those estimated in the prior year; and (3) that the threshold trigger be set at 10% and not $10 million. T. at P3028.

Ms. Davis further testifies that she agrees with Intervenors that Rider CCR charges be recovered on the basis of demand charges for classes with demand metering and energy charges for other customer classes. She addresses AEEC witness Falkenberg's concerns related to the review period and noted her proposed reporting requirements will assist in expediting the process. Ms. Davis also testifies that she now supports Mr. Falkenberg's recommendation that Rider CCR be trued up for the difference in collections and not just changes in the revenue requirement. T. at P3082-3083.

Mr. Castleberry further clarifies in his Sur-Surrebuttal testimony that the Auction purchases and sales are limited to one-year terms and thus the term for Rider CCR should consequently be one year or less. T at P 1674.

In Sur-Surrebuttal, Mr. Pettett testifies that EAI would agree to the AG's and AEEC's suggestion to bill Rider CCR and the MISO Rider on an energy (kWh) basis for all rate classes except for the LGS rate class, which would be billed using demand (kW). T. at P 496.

EAI witness Hunt, in his Sur-Surrebuttal, continues to recommend the interim recovery threshold be set at $10 million rather than 10%. Mr. Hunt also continues to support EAI's proposed method for true-up, rejecting the method proposed by AEEC

and Staff. Mr. Hunt testifies that neither AEEC nor Staff provided definitive evidence for the Commission to reject EAI's proposal to use the actual versus the estimated revenue requirement true-up calculation for this rider, noting that EAI's currently approved Capacity Acquisition Rider uses that method. Additionally, Mr. Hunt testifies that EAI continues to support applicable carrying charges be applied to the true-up balance. T. at P 1461-1462.

The Commission finds that the design of the charges under Rider CCR as recommended by AEEC and the AG and as supported by Staff and with which EAI agrees are appropriate and, therefore, charges under Rider CCR will be billed on an energy (kWh) basis for all rate classes except for the LGS rate class, which would be billed using demand (kW).

The Commission finds that, as addressed by the AG, long-term capacity transactions should require pre-approval of the Commission, therefore, capacity transactions considered under the Rider CCR should be one year or less or have been pre-approved for recovery by the Commission.

In setting a threshold for interim recovery, the Commission finds Staff's recommendation to set that threshold at 10% more appropriate than EAI's set dollar limit of $10 million in that a percentage level correctly ties the threshold to the overall recovery amount. The Commission therefore adopts Staff's proposed percentage.

The Commission also finds that Staff's and AEEC's recommendations related to the true-up provisions under Rider CCR are appropriate and reject EAI's proposal. The Commission notes that Staff's and AEEC's true-up provisions reflect a method consistent with numerous currently approved EAI riders in which costs are trued up

both for over/under-collections as well as for the difference in any estimated costs versus actual costs, effectively making Rider CCR an exact-recovery rider. The Commission finds further that the reporting requirements as proposed by Staff are appropriate, providing needed information in which pre-recovery review can be more timely effected.

As recommended by Staff and consistent with the treatment approved herein for the MISO Rider, carrying charges on unrecovered true-up or over/under-recovery balances are not appropriate under this rider.

Rider CCR, as amended pursuant to Staff's Revised Surrebuttal testimony, is an appropriate mechanism by which to effect recovery of costs from or flow-through of revenues to ratepayers resulting from EAI's purchases or sales of short term capacity.

Having made these findings, the Commission, therefore, adopts Rider CCR as amended pursuant to the recommendations outlined in the Revised Surrebuttal testimony of Staff witness Davis.

XVIII. MISO Rider

EAI witness Castleberry proposes a MISO Rider to recover the costs EAI pays to MISO for wholesale transmission service, certain other MISO charges, and EAI's deferred MISO Implementation Costs. T. at P 1575. EAI's originally proposed MISO Rider called for recovery of MISO regional transmission charges net of EAI's MISO Point to Point Wholesale revenues plus MISO administrative charges plus the deferred MISO Implementation Costs. EAI's proposed MISO Rider would be subject to a carrying charge using the most currently Commission approved return; would allow for interim adjustments should the balance exceed $10 million; and would be designed by

applying to each element of base rates the percentage of total MISO Rider charges to base rate revenues determined in this docket. T. at P 3061-3063.

Staff witness Davis recommends approval of the MISO Rider subject to elimination of the over/under carrying charges as unreasonable and unjustified and inconsistent with prior Commission orders approving similar riders in Docket Nos. 10-052-U and 10-067-U for Empire District Electric Company and Oklahoma Gas & Electric Company, respectively. Davis also asserts that such treatment would be inconsistent with the Commission's Order No. 76 in Docket No. 10-011-U. Witness Davis also recommends that EAI be subject to certain reporting requirements during operation of the Rider. T. at P 3063-3064, P3063, footnote 7, and P3064 footnote 8.

Addressing the design of the Rider, AG witness Marcus recommends that, for residential customers, recovery be made on a cents-per-kWh basis rather than as a percent of the residential rate components. P. at 1029. Both AEEC witness Falkenberg[31] and HHEG witness Blank recommend that the MISO Rider provide for a per kW[32] charge for customers paying demand. T. at 732 and P570.

AEEC witness Falkenberg recommends that the MISO Implementation Costs be recovered through base rates and not through the Rider. He also recommends that the MISO Rider be subject to a three-year sunset provision, at the end of which the Commission can determine the appropriate rate recovery mechanism. P. at 702. HHEG witness Blank also recommends that the MISO Implementation Costs not be recovered through the MISO Rider but be subject to audit and that any recovery method be addressed in next rate case. T. at P 571-572.

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[31] AEEC witness Falkenberg Surrebuttal (incorrectly headed as "Direct Testimony").
[32] Kilowatt (kW)

Staff witness Hilton testifies in support of including the MISO Implementation Costs for recovery in the MISO Rider, reiterating the ratepayer safeguards instituted by the Commission in its Order No. 76 in Docket No. 10-011-U when it approved the deferral of the MISO Implementation Costs. Those provisions are:

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 expense balances.

Hilton testifies that he "has reviewed the detailed cost information provided in support of EAI's requested deferrals for May 2013 and similar previous reports as they have been provided in Docket No. 10-011-U." He notes that he has found no "instances of non-compliance" with these ratepayer protections in the costs provided and that he

will continue to monitor any subsequent costs prior to inclusion in the MISO Rider. T. at P2830-2832.

Witness Hilton addresses the concerns of AEEC and HHEG, noting that, although these costs could be addressed in a subsequent rate case, "given the timing of the instant rate case, including accrual of these costs throughout the pro forma year, ... and the Commission's order that no carrying charges related to these costs be allowed," he continues to recommend recovery through the MISO Rider and reiterates his ongoing review of such costs. T. at P 2839-2840.

In his Rebuttal testimony, EAI witness Hunt agrees to Staff's proposed reporting requirements and also agrees with Staff that no carrying charges should be allowed on the deferred MISO Implementation Costs. P. at 1448. EAI witness Pettett, in his Sur-Surrebuttal testimony, further agrees to bill the MISO Rider on an energy (kWh) basis for all rate classes except for the Large General Service (LGS) rate class, which would be billed using demand (kW). T. at P 496.

With these amendments to the Rider and agreement to Staff's reporting recommendations, EAI witness Hunt continues to seek approval of the MISO Rider, with recovery of the deferred MISO Implementation Costs and a carrying charge applicable only to the over/under-recovery balances generated by the operation of the rider. As support for application of a carrying charge to the over/under-recovery balances, Mr. Hunt testifies that such treatment has been approved by the Commission for both EAI's Energy Cost Recovery Rider (Rider ECR) and its Production Cost Allocation Rider (Rider PCA) and represents a reasonable balancing of interests between customers and EAI. T. at P. 1449, 1461.

The Commission finds that EAI's proposed MISO Rider is an appropriate mechanism with which to collect those charges to be billed by MISO to EAI in service of its retail customers. The Commission additionally finds that such rider is also the appropriate mechanism by which recovery of the deferred MISO Implementation Costs should be effected, with the proviso that, consistent with prior Commission Order,[33] no carrying charges will be applicable to those balances. The Commission finds that the concerns of both AEEC and HHEG, regarding the timeliness of MISO Implementation Costs recovery through the MISO Rider as well as the prudence of those costs recovered, have been addressed, as Staff will continue to review all such costs pursuant to the Commission's ratepayer safeguards.[34]

The Commission finds no need to implement a sunset date for this tariff, given that the provisions of the MISO Rider may be addressed at any time. The Commission also finds that, consistent with similar cost recovery mechanisms approved for Empire and for OG&E, no carrying charges will be allowed on the over/under-recovery balances generated under the MISO Rider. The Commission further finds that the design of the rates collected under the MISO Rider should comport with the recommendations of the AG and AEEC, with which EAI has agreed. Finally, the Commission adopts Staff's recommended reporting requirements under the MISO Rider to which EAI has also agreed.

XIX. Rider ECR

Proposed modifications to Rider ECR which remain outstanding, as addressed below, include implementation of either the average, set-price fuel mechanism or a

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[33] Order No. 76, Docket No. 10-011-U.
[34] *Id.*

varying fuel cost mechanism, recovery of activated carbon and calcium bromide through Rider ECR, and refund of damages determined in Docket No. 05-116-U through the tariff."

Average Fuel Cost Method/Varying Fuel Cost Method

EAI witness Castleberry proposes to eliminate the retail allocation mechanism currently employed to allocate fuel costs and to adopt the average fuel cost method. Witness Castleberry testifies that, with "essentially ... no full or partial requirements wholesale load, the capacity allocation for retail is 99.987 percent. Thus, when this allocation factor is applied, customers will pay essentially the same energy rate whether using the revised mechanism or the proposed average rate methodology...." T. at P1573-1574. Mr. Castleberry explains that, additionally, such allocation is no longer necessary because, pursuant to Order No. 7 in Docket No. 12-038-U, EAI is required "to seek approval prior to making any capacity sales from units that are allocated to retail...." T. at P1574, and P1574 footnote 17.

HHEG witness Kenneday recommends that the Commission reject EAI's proposed recovery of the average, fixed rate cost for fuel and purchased power from all customers and that the Commission require recovery "using a time varying method." T. at P1988. Mr. Kenneday testifies that fuel and purchased energy costs will vary based on the demand on the system and that "[u]sing the same ECR charge for all customers fails to consider that low load factor customers use a disproportionately higher share of electricity produced by higher cost peakers than high load factor customers." T. at P1986-1987. Witness Kenneday proposes implementation of a "time-varying" rate, changed each hour or half hour, to match the actual costs incurred and more

appropriately providing price signals, with resultant reduced consumption and fuel cost savings. T. at P1987-1988.

HHEG witness Tinsley testifies that he has done an analysis to measure the interclass subsidy caused using the same Rider ECR charge for all classes. T. at P2501. Mr. Tinsley did his analysis using the hourly data EAI used in 2012 to make its wholesale/retail allocation under the current Rider ECR. T. at P2501-2502. Based on that analysis, witness Tinsley concludes, under the current method to charge fuel and purchased power costs through Rider ECR, substantial inter-class subsidies occur. His analysis indicates that LGS and Lighting rate classes subsidize retail customs by approximately $6.6 million annually. T. at P2505. Mr. Tinsley recommends "the Commission require allocation of fuel and purchased energy costs to rate classes using an hour by hour method similar to the current method approved by the Commission [by Order No. 19 at 15] in Docket No. 03-028-U for the allocation of fuel and purchased energy costs between retail and wholesale customers based on rate class consumption at the plant (inclusive of line losses)." T. at P2505-2506, and P2506, footnote 12.

Wal-Mart witness Chriss testifies that EAI does not incorporate a class level time variant rate for variable costs, including fuel, which results in an inequitable assignment of additional costs to high load factor customers during off-peak hours. T. at P24.

Staff witness Regina Butler recommends approval of EAI's changes to Rider ECR to effect use of the average rate method subject to certain Staff proposed amendments and reporting requirements to which EAI agrees. T. at P3003, P3005-3006, P3023-3024, P1452, and P1677. Ms. Butler addresses HHEG's proposed time-varying rate, stating that such method may not be appropriate for all customers and that no analysis

had been performed to measure the possible customer impact such change to Rider ECR would have. T. at P3025.

EAI witness Castleberry testifies that he does not recommend incorporation within Rider ECR of an hourly method for fuel and purchased power cost allocation to rate classes, which he states is consistent with Staff's recommendation. He asserts that the fact that no customers have "signed up for the real-time pricing pilot that was approved in 09-084-U" supports there is no need for this change. T. at P1678.

The Commission finds that, as noted by Staff, the impact to each rate class of an hourly or half-hourly measure of fuel and purchased power costs for recovery under Rider ECR has not been clearly demonstrated. Given this lack of sufficient information, the Commission rejects the method recommended by HHEG at this time. The Commission, however, directs EAI to maintain the hourly fuel and purchased power cost data. The Commission further directs EAI to work with its customers to develop a workable Real Time Pricing tariff or to explore the use of hourly fuel and purchase power cost within Rider ECR, including analysis which shows rate class impacts, and to report to the Commission within 180 days.

Environmental Protection Agency (EPA) Regulation Costs

Mr. Castleberry recommends Rider ECR be amended to include the costs of activated carbon and calcium bromide that will be used in its White Bluff and ISIS coal fired units to comply with the EPA Mercury Air Toxics Standards (MATS) regulation. T. at P1595. Witness Castleberry asserts such costs are appropriate for recovery under Rider ECR rather than base rates, because these costs are not known at this time, will be incurred as a function of the operation of the units, are expected to be volatile, and are

similar to costs previously approved by the Commission for recovery under Rider ECR. T. at P1597-1598. He also testifies that changing Rider ECR to accommodate these future costs is not premature and rebutted the contention that including these costs would present additional complication to the tariff's review process. T. at P1633-1635.

Staff witness Butler recommends approval of including these costs for recovery in Rider ECR. Ms. Butler testifies that she bases her recommendation on EAI's demonstration that it will install the equipment which uses these chemicals, that the level of the chemicals' use will vary directly with generation, and that the Commission has approved similar costs for recovery through Rider ECR T. at P3023.

AG witness Marcus testifies that inclusion of these chemical costs for recovery under Rider ECR is premature but, if such cost recovery is approved, it should be made clear that such recovery does not constitute pre-approval of the costs which flow through the tariff. T. at P. 1095-1096.

AEEC witness Falkenberg recommends that these costs be recovered through base rates and that including such costs in Rider ECR will reduce incentives for cost control and will complicate the review process. T. at P719-720.

HHEG witness Kenneday recommends that these costs should be included in base rates, testifying that EAI had not provided evidence which would indicate that these costs meet all the Commission's criteria for automatic flow through of costs, which are: 1) the cost is a significant portion of the utility's operational costs; 2) the cost is extremely volatile and unpredictable; and 3) the cost is outside the utility's control. He states that EAI has not demonstrated the volatility of these costs. T. at P1989.

The Commission finds that the costs of activated carbon and calcium bromide, to be used in EAI's White Bluff and ISIS coal fired units to comply with the EPA MATS regulation, are, similar to fuel, tied directly to the generation function of these plants and will vary with that function, are similar to other costs approved for recovery through Rider ECR, and are therefore appropriately recovered through Rider ECR. The Commission, therefore, approves the inclusion of the costs for recovery through Rider ECR.

Rider ECR Recovery of Damages from Docket No. 05-116-U

AEEC witness Falkenberg recommends that, concurrent with the Commission order in this instant case, the Commission render its finding in Docket No. 05-116-U, regarding the damages incurred related to coal inventory shortages and generator outages and that the Commission require the damages, with interest, be refunded to customers through Rider ECR. Mr. Falkenberg also recommends, because the damages were incurred in 2005 and many of the 2005 customers are no longer on the system, that the Commission further order EAI to directly refund the determined damages to those customers. T. at P720.

The Commission has not made its final ruling regarding damages in the cited Docket and AEEC's proposal for application to and recovery from ratepayers is premature.

XX. Large and Small Cogeneration Rider

EAI proposes changes to the calculation of avoided costs under the Large Cogeneration Rider (LCR) and the Small Cogeneration Rider (SCR). The Commission

notes that it has approved a temporary LCR Rider pursuant to Orders No. 17 and 20 issued in this Docket.

EAI witness Castleberry proposes changes to the payment provisions of the Large Cogeneration Rider (LCR) and the Small Cogeneration Rider (SCR) for payments made to customers, with behind the meter generation facilities and who are Qualifying Facilities (QFs). QFs consist of electric generating facilities that are 'qualifying cogeneration facilities or qualifying small power production facilities' as defined under Federal Energy Regulatory Commission (FERC) regulations- 18 C.F.R. Section 292.101 (2012)." T. at P2845, footnote 2. Mr. Castleberry explains that, pursuant to the Commission's Cogeneration Rules, the compensation level to be paid QFs for the energy provided " 'shall be at avoided costs, defined as the cost to the purchasing utility of electric energy which, but for the purchase from the QF, such utility would generate itself or purchase from another source.'" T. at P1591and P1591- footnote 22. Mr. Castleberry explains that these changes are necessary, first, because, for purposes of determining avoided cost, the LCR and SCR currently reference the ESA, from which EAI will exit, and, second, because EAI will now be participating in MISO's Day 2 Market, EAI will use this market to set the avoided cost payments under the tariffs. T. at P1591-1592.

Mr. Castleberry explains that "QFs in MISO will be able to elect one of two structures.... The first structure is referred to as the 'Hybrid Option[,]' [u]nder [which] ..., QFs will be able to offer their uncommitted generation into the MISO market while reserving the generation that is needed to serve their host load. Alternatively, QFs that elect the Hybrid Option also may put energy to the host utility. The second structure is

the 'Behind-the-Meter Option[,]' [u]nder [which] ..., QFs will not transact in the MISO market but will, instead, put energy to the host utility. Under both structures, avoided cost will be determined from the MISO settlement statements based on MISO Locational Marginal Prices (LMP) data. T. at P1592.

EAI witness Cicio further explains the two QF options available in and eligibility requirements of the MISO markets, including how payments are made in those markets. T. at P2850-2857. Mr. Cicio outlines the mechanisms which would be used to measure the avoided costs for both the LCR and SCR, which will be based on MISO settlement data, as well from what entity payments will be made under the tariffs. T. at P 2859-2863. He further testifies that both the LCR and SCR tariff language will be appropriately amended to reflect EAI's proposed methods for avoided cost determination and to reflect the appropriate eligibility requirements. T. at P2873-2876.

Staff witness Cotten clarifies EAI's proposed method and testifies that, "[f]or large QFs, the avoided cost will differ with respect to QFs registered as separate Load Zones in MISO and QFs embedded within the EAI Load Zone. For small QFs, defined as QFs that are 100 kW or below in size, avoided cost will continue to be based upon a projected avoided cost rate, however the projections will be based on MISO market operations." T. at P2968-2969. Witness Cotten recommends approval of EAI's proposed methods for determining avoided costs under the LCR and SCR, finding such methods reasonable because:

1. The methods are consistent with the Commission definition of avoided cost;

2. The pricing is location specific and hourly and based on actual MISO locational Marginal Prices for larger QFs;
3. The rates will be based on settlement statements prepared by MISO, which is an independent entity; and
4. The projected avoided cost for QFs that are 100 kW and below in size will be determined using the AURORA model of the MISO system . AURORA is a software package containing data for all the reliability regions in North America to forecast wholesale electricity market prices..

T. at P2969 and P2969, footnote 7.

HHEG witness Tinsley recommends the Commission reject the changes proposed to set avoided cost under Rider LCR and SCR. T. at P2509.

The Commission finds that the record supports EAI's proposed changes to the calculations under Rider LCR and Rider SCR and that, given EAI's exit from the ESA and integration into MISO, MISO's market prices reflect easily identified avoided prices. However, as addressed by the Commission in its findings related to Rider OIS, the Commission directs EAI to work with its Rider LCR and Rider SCR customers to further address the use of demand resources, including the pricing for QFs, in the MISO market.

XXI. Rate Schedule No. 60. Extension of Facilities Policy (EOFP)

EAI witness Aldy recommends several changes to Rate Schedule No. 60, Extension of Facilities Policy (EOFP) to clarify the provisions in that schedule. T. P130-136. Only one issue regarding these changes remained outstanding at the time of the

filing of the Revised Issues List. That issue relates to changes to Section 60.2.8 regarding easements, clarifying year round access. T. at P162. AEEC witness Falkenberg recommends alternative and additional changes to EAI's amendments to this section, to which EAI objects. T. at P162-164.

EAI witness Aldy testified that EAI withdrew its proposed changes to Section 60.2.8 and clarified that, with that withdrawal no further outstanding issues remained with regard to EAI"s recommended EOFP. T. at 952-953. AEEC witness Falkenberg confirms that his concerns regarding EAI's changes have been addressed by that withdrawal. T. at 1048.

The Commission finds that no issues remain outstanding with regard to EOFP which require a Commission determination.

XXII. Real Time Pricing Service Rider Pilot

EAI witness Pettett recommends the Commission close the Real Time Pricing Service Rider (Rider RTP), which allows customers to tie rates to real time pricing. Mr. Pettett testifies that Rider RTP has no current customers, is slated to expire on December 21, 2013, and is no longer necessary given EAI integration into MISO, with its available markets. T. at P392.

HHEG witness Kenneday testifies to the origins of the pilot Rider RTP program and explains that, in Docket No. 09-084-U, he had proposed that a real time program be instituted to "mitigate subsidization issues caused by the use of a constant ECR charge to recover fuel and purchased power costs." Mr. Kenneday testifies that the tariff, subsequently submitted by EAI after Commission approval of the "Late Filed Revised Settlement Agreement" in that Docket, only addressed base rates and still required

payment of a constant ECR charge and failed to address his concerns regarding use of a constant ECR rate. He testifies that UAMS did evaluate that subsequently approved Rider RTP but rejected participation in the program because it was not cost effective, a conclusion supported by the fact that there were no participants. T. at P1956 and P1989-1990.

HHEG witness Kenneday recommends that, should the Commission adopt his recommendation to institute time varying rates under the ECR, Rider RTP should be closed. Alternatively, Kenneday recommends that, should the Commission not adopt that recommendation for the ECR, EAI's proposal to withdraw Rider RTP should be rejected and the Commission approve a revised Rider RTP program which includes fuel and purchased power costs. T. at P1956-P1957 and P1989-1990.

Staff witness Butler recommends the Commission close Rider RTP. T. at P3009. Ms. Butler explains that the tariff was originally designed to allow customers to increase or decrease load in response to real-time fluctuating fuel prices within the ESA. Witness Butler testifies that "[n]o analysis has been presented in this docket on the appropriate design of a revised Rider RTP which considers EAI's participation in MISO..." and that she continues to agree that Rider RTP should be withdrawn and HHEG's recommendation be rejected. T. at P3030.

The Commission finds that the current Rider RTP, which will expire in December 2013, should be withdrawn. As directed by the Commission with regard to Rider ECR, the Commission directs EAI to work with its customers to develop a workable Real Time Pricing tariff within the MISO markets or to explore the use of hourly fuel and purchase

power cost within Rider ECR, including analysis which shows rate class impacts, and to report to the Commission no later than noon on July 1, 2014.

XXIII. Rider PCA

EAI witness Gillam outlines EAI's proposal for closing out recoveries under the Production Cost Allocation Rider (Rider PCA) which includes EAI's proposal to true-up the unrecovered balances from the final December 31. 2013, billing cycle which are less than $1 million. Mr. Gillam testifies that EAI proposes to collect any true-up amount which is less than $1 million through Rider ECR, with that collection to be effected in the March 2014 Rider ECR filing. T. at P1408.

AEEC witness Falkenberg makes an additional recommendation related to any true-up of PCA costs which would be collected through the Rider ECR. For any such true-ups collected through Rider ECR, Mr. Falkenberg recommends that "class specific amounts should reflect the PCA allocation method, not the method used for energy costs in the ECR." T. at P698.

Staff witness Butler recommends the Commission approve EAI's proposed recovery through Rider ECR of any Rider PCA true-up amounts which remained as of the December 31, 2013 billing cycle and which were less than $1 million. She testifies that the proposed method of recovery was reasonable and fairly considered the customer impact of that true-up. T. at P3011. Ms. Butler also addresses AEEC's recommendation regarding the appropriate method to allocate any Rider PCA true-up through Rider ECR and testified that any true-up amount of less than $1 million would not result in significant rate differences under either method and, thus, EAI's proposal should be approved without modification. T. at P3032.

The Commission finds EAI's proposal to collect Rider PCA true-up costs which would be less than $1 million through Rider ECR appropriate. The Commission also finds that AEEC's proposed allocation method for such costs reflects consistent rate allocation treatment as originally found under Rider PCA and is also appropriate and directs EAI to amend its ECR as needed to effect that allocation for these costs.

XXIV. Rider ANO

EAI witness Gillam testifies to EAI's proposed transition for the ANO Recovery Rider (Rider ANOR) in which EAI will transfer the ANO Wholesale Baseload (WBL) cost to base rates and it will file, as of April 1, 2014, its Rider ANOR update which will reflect only the unrecovered true-up costs allowed under the tariff. T. at P1406.

AEEC witness Falkenberg recommends the Commission open an investigation into the accident which occurred at ANO on March 31, 2013, and proposes that the Commission disallow from recovery any costs found to have been incurred due to imprudence or negligence and that EAI refund any such costs it has collected through Rider ANOR. He recommends such refund be effected through the Rider ANOR true-up. T. at P666. Witness Falkenberg recommends that Rider ANOR remain open until the next general rate case to allow completion of that full investigation and subsequent refund of any disallowed costs through the tariff. T. at P701.

Mr. Falkenberg testifies that the accident resulted in an extended shut-down of ANO-Unit 2 and the continued shut-down of ANO Unit 1, with early estimates for repair cost ranging between $130 million to $215 million and additional expected costs to result from replacement power purchases made during the unscheduled outage periods for both units. T. at P699, P700.

Witness Falkenberg asserts that the provisions of Rider ANOR provide the opportunity and necessity for an investigation into the prudence of the ANO outage and the Company's repair costs." T. at P700. Witness Falkenberg testifies in support of not closing Rider ANO at this time, that "[r]etroactive ratemaking arguably precludes making any adjustment to refund ANO costs already recovered via base rates, however because Rider ANO is subject to a true-up, the opportunity for refunds does exist for costs recovered pursuant to the rider." T. at P700.

Staff witness Butler recommends approval of EAI's transition plan as meeting the provisions of Section 55.4 of Rider ANOR. T. at P3010 and P3032. Responding to AEEC, witness Butler states that "[t]he terms for recovery and true-up of Rider ANOR costs were approved in Docket No. 12-038-U...[and that k]eeping Rider ANOR open for the purposes stated in Mr. Falkenberg's testimony is not appropriate or necessary..." and she continues to recommend approval of EAI's proposal. T. at P3031-3032.

The Commission finds that EAI's proposed transition plan for treatment of costs recovered under Rider ANOR is appropriate and should be approved. With regard to AEEC's proposed investigation of the March 2013 ANO accident, the Commission finds that finalization of repairs are not expected to be concluded until the end of 2013 and issues related to insurance reimbursement appear to remain outstanding, with EAI to seek any reimbursement at a later date. T. at P699. The Commission, therefore, finds it premature to institute an investigation at this time and additionally finds no evidence to indicate that EAI has included any accident-related costs in its current base rate request. At the appropriate time, the Commission will review, for prudence, all repair and other costs for which EAI may request recovery and make its determination as to

disallowance. The Commission will also review for prudence any costs of replacement purchased power which EAI has recovered through its Rider ECR and make its determination as to any appropriate refund which may be due.

XXV. Commercial Space Heating Rider

EAI proposes to close the Commercial Space Heating Rider (CSHR) to new customers. The CSHR is available to customers that have permanently installed and regularly use qualifying space heating equipment. EAI witness Pettett testifies that in Docket No. 06-101-U, the Commission closed the Separately Metered Commercial Space and Water Heating Rider Schedule M14 (SMWHR). Mr. Pettett testifies that consistent with the Commission's finding on SMWHR, EAI "proposes to close the CSHR to new customers and to include a similar grandfathering proviso for existing customers." T. at P393.

HHEG witness Ward testifies that the closing of SMWHR was related to the testimony and evidence presented in Docket No. 06-101-U. The issue of closing CSHR was addressed in Docket 09-084-U and the parties agreed to revised language which closed CSHR to new customers "except where the electric heating system has a coefficient of performance greater than 1.5." T. at P700. Mr. Ward recommends not changing CSHR and testifies that EAI has not provided sufficient justification for closing CSHR when evidence in Docket 09-084-U supported continued availability. T. at P700.

EAI witness Pettett testifies that the concept behind SMWHR and CSHR is the same, providing a reduced billing for heating load. Mr. Pettett testifies that it would be "inequitable and inconsistent" to close SMWHR and have CSHR open to new customers. T. at P464.

HHEG witness Ward testifies that historical precedent should not be the sole justification for closing CSHR. Mr. Ward testifies that electric heating technology has improved in recent years and using this technology "promotes better utilization of Company assets and energy efficiency." T. at P657. Mr. Ward continues to recommend that CSHR remain unchanged and open to new customers. T. at P658.

Staff witness Swaim testifies that in Docket No. 09-084-U's settlement, CSHR was modified to require new customers to have electric space heating systems with a coefficient of performance (COP) greater than 1.5. Mr. Swaim testifies that because of efficiency gains in electric space heating systems, the 1.5 COP appears too low. "As of January 2012, the Arkansas Technical Reference Manual (TRM) requires ENERGY STAR standards as the minimum (baseline) efficiencies allowable for ground source heat pumps replacing any electric heating and air-to-air cooling system. Those COPs are 3.6 for a Closed Loop Water-to-Air system and 4.1 for an Open Loop Water-to-Air system." (T. at P1225) Mr. Swaim recommends "the Commission reject Mr. Ward's rate design proposal and impose the TRM baseline COP for electric space heating systems installed after January 1, 2012." T. at P1225. EAI does not oppose Staff's recommendation.

The Commission finds CSHR should remain open to new customers with higher efficiency electric space heating systems. Therefore, the Commission orders CSHR remain open and amended as recommended by Staff witness Swaim.

XXVI. Formula Rate Plan

EAI witness McDonald testifies that EAI did not file in this Docket any proposals in response to the Commission's Order No. 19 in Docket No. 08-137-U, which invited

innovative rate case proposals and that EAI's filing in this docket concentrated on the structural changes that its integration into MISO would cause. T. at P2374. He testifies that, should EAI file any proposed mechanism, it would do so in a timely manner, shortly after rates are set within this rate case which would provide the Commission several months for review and result in the mechanism's first update the same as that which would have occurred had the mechanism been approved in this docket. T. at P2375.

HHEG witness Kenneday testifies that, should any EAI-proposed Formula Rate Plan (FRP) reflect that which EAI proposed in Docket No. 09-084-U, approval of such an RFP outside of a rate case would be inappropriate, given that the reduction in risk such an RFP provides would reduce the level of return allowed within the cost of service. Mr. Kenneday recommends that the Commission not approve automatic adjustment clauses of this kind outside of a rate case. T. at P1998-1999.

Wal-Mart witness Chriss also recommends the Commission not approve a formula rate plan outside the context of a rate case. Mr. Chriss further testifies that the traditional rate making "paradigm" is more appropriate because it more systematically considers the "costs, benefits, and risks" and EAI has provided no evidence that it is unable to earn its return on and of its investments using traditional rate making. T. at P29. Mr. Chriss testifies that implementation of such an FRP will reduce the risk of cost recovery and, if approved outside of a rate case, parties will not be able to address the corresponding reduction in return which should be allowed the utility and there exists the possibility that overlaying an FRP onto currently effective rates may result in overpayment by ratepayers. T. at P26. In support of his position, Mr. Chriss provides

examples of other state commissions who recognized the need for a lower return to match the reduced risk such mechanisms provide. T. at P26-28.

The Commission, in its Order No. 19 in Docket No. 08-137-U, invited electric utilities to propose any mechanism, *within the context of any rate case they may file*, "that would ensure that the utility recovers all utility costs approved by the Commission independently of the utility's volume of sales, thereby further aligning utility and ratepayer interests in both utility and non-utility energy efficiency efforts and promoting utility pursuit of least-cost service over the long term." In this case, EAI chose not to make any such proposal for Commission determination.

To the extent EAI should make such a filing outside the context of a rate case, the Commission will give that filing appropriate consideration given the concerns raised by the parties in this Docket.

XXVII. Standby Service Rider Rate Increase

EAI witness Pettett testifies that EAI proposes increases to the Standby Service Rider (the SSR) rates to reflect the same percentage increase as applicable to Large General Service (LGS) customers. T. at P494-495. "Supplemental service is the power that a [Combined Heat and Power] CHP customer takes in addition to its self-generation." T. at P496.

Mr. Pettett explains that the SSR "provides for various power and energy supply products for cogenerating customers' use during planned maintenance periods or unplanned outages of on-site generating equipment. The prices for these energy products are taken from the Large Power Service (LPS) tariff, which ensures that energy consumption for cogenerating customers is priced equivalent to similar service to firm

power customers." T. at P467. Mr. Pettett testifies that these rates have been historically treated consistent with treatment of LGS rates, with the SSR energy charges the same as those for LPS and daily demand charges "roughly equivalent to the LPS demand charges, if service were taken for a full month." T. at P494. Therefore, increases to these rates have been set at the same level as increases to the LGS class, reflecting that cost of service increase. T. at P495.

HHEG witness Tinsley recommends the Commission reject EAI's proposed increases to the various components of the SSR, asserting such increases are not based on a cost of service for the service provided under the tariff and that the increases requested will reduce the economies of CHP and will significantly discourage its use on EAI's system. T. at P2481-2482 and P2487. Mr. Tinsley testifies that promotion of CHP offers significant benefits to EAI and its customers, including reduced energy costs, reduced environmental emissions, improved reliability, reduced transmission costs and is a source of short- and limited-term capacity. T. at P2481-2482.

Staff witness Swaim addresses EAI's proposal to set the increase for SSR rates at the same percentage as that for LGS customers. Mr. Swaim testifies that [b]ecause the billing determinants for the ... SSR customers are difficult to predict, those rate codes have been excluded from the traditional rate design. Instead, the ... SSR rates have been increased in past cases by the same percentage as the increase for LGS. Although these rates are not determined by the COS [cost of service] study, the revenues they produce are netted against the revenue requirement. T. at P1226. Mr. Swaim concludes, based on his review of the resultant rates under the SSR, that the level of increases is not such that investment in CHP would be discouraged. T. at P1226-1227.

The Commission finds that the rates charged under the SSR have been historically and appropriately based on the firm service offered to large customers which EAI stands ready to provide its SSR customers. The Commission finds that, therefore, increases to the SSR rates have also historically and appropriately replicated the increases to that same firm service. T. at P494 and P1226. In this Docket, EAI's proposed method to increase SSR rates is consistent with that previously used and approved and results in reasonable rates. The Commission directs that the SSR rates be increased by the same mitigated percentage applicable to the LGS class.

XXVIII. Other Tariffs and Riders

Non-Residential Customer Deposits (CAC Charge)

AEEC witness Falkenberg testifies EAI's non-residential customer deposit policies are unfair. Mr. Falkenberg testifies EAI refunds residential customer deposits after twelve months, but only provides refunds to non-residential customers when their accounts are closed. Mr. Falkenberg states that this policy is unfair because non-residential customers have a better payment history than residential customers. T. at P682-683.

In addition, Mr. Falkenberg takes issue with an exemption to General Service Rule (GSR) 4.02.A granted by the Commission whereby EAI can demand an additional deposit from a non-residential customer based on the customer's bond rating. Mr. Falkenberg testifies "residential customers with high credit scores may not be required to provide a deposit at all." T. at P683-684. Mr. Falkenberg recommends EAI be granted a waiver to allow for refunding of non-residential customer deposits after twelve months of on time payment and elimination of EAI's exemption to GSR 4.02.A. T. at

P695-696. HHEG witness Kenneday testifies that EAI's treatment is discriminatory and agrees with Mr. Falkenberg's recommendations. T. at P2057.

EAI witness Aldy testifies that different deposit policies for residential and non-residential customers are warranted. Mr. Aldy testifies that the exposure from a delinquent non-residential customer is greater than with a residential customer. Mr. Aldy also testifies many non-residential customers that file bankruptcy have never paid a late bill. T. at P165.

Staff witness Holly Tubbs testifies there have been "numerous situations where non-residential customers, who have historically paid their bill on time, suddenly file bankruptcy or close their business leaving EAI with a large unpaid bill, with little or no deposit to cover that bill, which increases the exposure for other ratepayers." T. at P2942. The lowering of a credit rating is an indication of financial issues that warrant a review and possible increase to a customer's deposit amount to "adequately secure the account and prevent the absorption of potential losses by other ratepayers." T. at P2942. Ms. Tubbs testifies that the same argument to protect ratepayers from unsecured losses can be made regarding the refunding of non-residential deposits. Ms. Tubbs clarifies that a waiver from GSR 4.06. is not required to allow for non-residential deposit refunds. GSR 4.06. does not require or prevent utilities from refunding non-residential deposits. Ms. Tubbs testifies "in order to protect the general body of ratepayers, it is not in the public interest to eliminate EAI's exemption from GSR 4.02.A. or require utilities to refund non-residential deposits after twelve months of good payment." T. at P2943.

The Commission agrees with EAI and Staff that a non-residential customer's failure to pay has a greater impact and a greater risk for subsequent recovery than residential customers. The Commission also notes that interest is paid on deposits pursuant to GSR 4.05. and Ark. Code Ann. §23-4-206. Therefore, the Commission finds that EAI's current deposit policies are reasonable and in the public interest and rejects the changes proposed by AEEC and HHEG.

Meter Test, Reconnect, and Trip Fees in CAC

EAI proposes to increase miscellaneous customer activity charges (CAC) related to Meter Test, Reconnect, and Trip fees. EAI witness Aldy testifies the proposed fees are cost based and are based on an analysis that includes "the average time required to provide the service, labor cost for the employees involved in these services, any appropriate payroll overheads, any related vehicle costs; and in the case of reconnection fee, the cost of a locking band." T. at P128. EAI's proposed increases in fees are shown below:

Customer Activity	Current Fee	Proposed Fee
Meter Test Fee	$52	$79
Trip Fee	$14	$20
Reconnect Fee-At Meter During Normal Working Hours	$35	$49
Reconnect Fee-Not At Meter During Normal Working Hours	$72	$100
Reconnect Fee-At Meter After Normal Working Hours	$54	$62

Reconnect Fee-Not At Meter After Normal Working Hours	$96	$110

T. at P125-P127.

Mr. Aldy testifies that it is impossible to know the number of customers impacted by these increases because the fees are only charged at customers' request or as the result of customers' actions. T. at P128.

Staff witness Owoh testifies that she reviewed EAI's cost analyses and supporting documentation and determined EAI's "proposed fees are within their respective average costs and are reasonable." T. at P2978. Ms. Owoh recommends approval of EAI's proposed fees. T. at P2981.

AG witness Marcus testifies that these charges are "applied to customers who cannot pay their bills, who are likely to be lower income customers." T. at 1027. Mr. Marcus proposes to limit the increases in these fees to no more than the cost of inflation as measured by the Consumer Price Index (CPI). He recommends fees of $62.40 for Meter Test, $16.80 for Trip, and $42.00 for Reconnection during Normal Working Hours. Mr. Marcus does not propose a change in the Reconnection after Normal Working Hours because EAI's proposed increase is less than the increase derived using the CPI. Mr. Marcus testifies that his recommendation would increase EAI's revenue requirement $517,000. T. at P1027-1028.

EAI witness Aldy and Staff witness Owoh disagree with AG witness Marcus and continue to recommend approval of EAI's proposed cost based CAC fees. AG witness Marcus testifies that there is little explanation as to why the costs associated with these charges have increased at greater than 5% per year. Mr. Marcus also testifies that increasing these fees could result in greater bad debt costs. Mr. Marcus continues to

support moderating these fees based on the CPI. T. at P1094-1095. HHEG witness Kenneday supported the AG's position. T. at P2060.

The Commission agrees with AG witness Marcus and adopts the AG's recommendation to limit the increase in these fees to no more than the CPI, as a form of mitigation similar to that which both EAI and Staff recommend for the LGS for base rates. The result of this mitigation is an increase of $517,000 to EAI's revenue requirement.

XXIX. Uncontested Issues

The Commission finds that the Revised Issues List also delineates those issues upon which the parties have reached agreement. The Commission has considered the record on the issues for which agreement has been reached and finds substantial evidence within the record for the final positions taken. Therefore, for those issues upon which the parties agree, the Commission approves those positions and the rate treatments as outlined in the testimony of the Parties.

XXX. Conclusion

Accordingly, the Commission orders as follows:

1. The rates and tariffs filed by EAI on March 1, 2013, are hereby denied.

2. Revised retail rates and tariffs in compliance with the Order shall be effective for all bills rendered on or after the date of this Order;

3. Within ten (10) days of the date of this Order, General Staff is directed to prepare and file in this Docket a revenue requirement summary reflecting the changes to Staff's Revised Surrebuttal Revenue Requirement,

adjusted in compliance with the findings of this Order. Further, Staff is directed to show a reconciliation of Staff's Revised Surrebuttal Revenue Requirement to the Revenue Requirement resulting from the findings of this Order. Contemporaneously with the recalculated Revenue Requirement, Staff is directed to file a cost of service to rate class resulting from the Commission's Order herein, and a mitigated cost of service showing the mitigation method approved herein.

4. EAI shall file with the Commission revised retail rates and compliance tariffs in accordance with this Order for review and approval of the Commission as expeditiously as possible; and

5. EAI shall otherwise fully comply with the directives set forth in this Order.

BY ORDER OF THE COMMISSION,

This 30th day of December, 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
Part 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

Dallas W. Heltz, Secretary of the Commission