ORDINANCE NO. 2007-03

AN ORDINANCE OF THE CITY OF INGLEISDE ON THE BAY, TEXAS FINDING, AFTER REASONABLE NOTICE AND HEARING, THAT AEP TEXAS CENTRAL COMPANY'S EXISTING RATES ARE UNREASONABLE; FINDING THAT AEP TEXAS CENTRAL COMPANY'S REQUESTED REVENUES RESULTING FROM ELECTRIC TRANSMISSION AND DISTRIBUTION RATES AND CHARGES WITHIN THE CITY SHOULD BE REDUCED; DETERMINING JUST AND REASONABLE RATES; ADOPTING RECOMMENDATIONS OF CONSULTANTS; PROVIDING FOR RECOVERY OF RATE CASE EXPENSES; PRESERVING REGULATORY RIGHTS OF THE CITY; ORDAINING OTHER PROVISIONS RELATED TO THE SUBJECT MATTER HEREOF.

WHEREAS, pursuant to § 33.001 of the Public Utility Regulatory Act, the City has exclusive original jurisdiction over the electric rates, operations, and services provided within city limits;

WHEREAS, on or about November 9, 2006, AEP Texas Central Company ("TCC" or "Company") filed with the City an application seeking to increase electric transmission and distribution rates by 13% on a system-wide basis;

WHEREAS, the Company proposed an effective date of December 14, 2006, that was suspended by resolution to provide time to study the reasonableness of the application;

WHEREAS, the City, in a reasonably noticed public hearing, considered the Company's application and a recommendation from the City's consultants who were retained to evaluate the merits of the Company's application;

WHEREAS, the City has determined that the Company's existing rates are unreasonable, that the Company's requested increase in revenues for its transmission and distribution systems within the City should be reduced, and that rates should be set at levels required to recover the revenue requirements set forth herein, pursuant to the recommendations of its consultants;

NOW, THEREFORE, BE IT ORDAINED BY THE CITY COUNCIL OF THE CITY OF INGLESIDE ON THE BAY, TEXAS:

SECTION 1. That the existing rates of AEP Texas Central Company are hereby found to be unreasonable. The rates proposed by AEP Texas Central Company, to be recovered through its electric transmission and distribution rates charged to customers located within the City limits, are hereby found, after reasonable notice and hearing, to be unreasonable and shall be changed as hereinafter ordered.

SECTION 2. The Company shall reduce its requested transmission base rate revenue requirement by $13.9 million, so that rates shall increase by the amount of $6,729,000.

SECTION 3. The Company shall reduce its distribution base rate revenue requirement by $7.1 million, so that its present rates shall be reduced by this amount.

SECTION 4. The electric rates charged within City limits shall reflect a 9% return on equity and a capital structure comprised of 59% debt, 40% common equity, and 1% preferred stock in order to reflect the historic low cost of capital and to prevent financial subsidization of TCC's parent company.

SECTION 5. Cities' rate case expenses are found to be reasonable and shall be reimbursed by the Company.

SECTION 6. The Company's rates shall be revised on a system-wide equal percentage basis to all customer classes. The changed rates resulting from this Ordinance are hereby determined to be just and reasonable rates to be observed and in force within the City.

SECTION 7. The electric rate revisions herein approved shall be effective for bills rendered on or after approval of this Ordinance. TCC shall file tariffs reflecting the change of rates herein ordered within 10 days of passage of this Ordinance.

SECTION 8. The rates set forth in this Ordinance may be changed and amended by either the City or Company only as provided by law.

SECTION 9. It is hereby found and determined that said meeting at which this ordinance was passed was open to the public, as required by Texas law, and that advance public notice of the time, place and purpose of said meeting was given.

SECTION 10. This Ordinance shall be served on AEP Texas Central Company by U.S. Mail to the Company's authorized representative, Nancy Napolitano, 400 West 15th Street, Suite 1520, Austin, Texas 78701.

SECTION 11. Nothing contained in this Ordinance shall be construed now or hereafter in limiting or modifying, in any manner, the right and power of the City under law to regulate the rates and charges of AEP Texas Central Company.

SECTION 12. All ordinances, resolutions, or parts thereof, in conflict with this Ordinance are repealed to the extent of such conflict.

PASSED AND APPROVED, this the 20th day of Feb, 2007.

APPROVED:

Cynthia B Foster

CYNTHIA B FOSTER, MAYOR

ATTEST:

Diane Hosea

DIANE HOSEA, CITY SECRETARY

PUC DOCKET NO. 33309
AEP TEXAS CENTRAL COMPANY RATE CASE
CITIES' PRELIMINARY ASSESSMENT OF ISSUES

A. RATE BASE ISSUES

1. Reclassification of CWIP at June 30, 2006 to plant in service and related accumulated depreciation and accumulated deferred income taxes.

The Company has included in electric plant in service amounts that were in construction work in progress ("CWIP") at June 30, 2006 for accounting purposes, but which it argues actually were in service and used and useful. The Company's proposed adjustment is unreasonable.

2. ARO 143 in lieu of ratemaking net salvage in accumulated depreciation (and depreciation expense).

The Company has proposed using Statement of Financial Accounting Standards (SFAS) No. 143 to determine the amount of net salvage included in accumulated depreciation and in depreciation expense for buildings (account 390, but separately reflected in account 399) in lieu of the PUC's historic practice of including net salvage on a ratemaking basis in the depreciation rate. This treatment is unreasonable and Cities will oppose this change.

3. Prepaid pension benefits (funding in excess of ERISA requirements).

The Company substantially overfunded its pension plan in 2005 and has included the overfunding as a prepaid pension asset in rate base. Cities oppose this treatment of the pension benefits. Additionally, Cities will reduce the prepaid pension asset for the generation portion.

4. Regulatory assets: debt refinancing – restructuring costs.

The Company included debt refinancing – restructuring costs in rate base rather than in the cost of debt. Other debt refinancing costs are included in cost of debt, which has been the historical precedent. Cities will oppose this treatment of debt refinancing-restructuring costs.

5. Other adjustments.

Cities' testimony at the PUC will make adjustments to Materials and Supplies, accumulated deferred income taxes, cash working capital, and affiliated transactions. These adjustment have not yet been finally quantified.

B. COST OF CAPITAL ISSUES

6. Return on common equity.

TCC has requested an ROE of 11.25%; Cities will be recommending an ROE in the range of 9%.

7. Capital structure.

Cities plan to support a capital structure consisting of approximately 59% debt and 40% common equity and 1% preferred stock.

8. Cost of debt.

Cities will be addressing the need for separate debt rates for the CTC and T&D components of TCC's proposed rates.

9. Debt refinancing - restructuring costs.

Cities plan to remove this amortization expense from operating expenses and include it in the cost of debt, consistent with the Commission's historic treatment of such refinancing costs. This cost will be allocated to T&D through the rate of return (the Company allocated the amortization expense only to distribution).

C. OPERATING EXPENSE ISSUES

10. Payroll and benefits expense.

Cities will be addressing the reasonableness of TCC's proposed payroll expense, including straight time and overtime labor costs, group insurance benefits expense, and incentive compensation expense.

11. Pension and OPEB expense.

The Company has excluded generation pension expense, which is a negative expense, although it has included the generation portion of the prepaid pension asset in rate base. Cities plan to propose including the generation pension expense, which is required pursuant to PURA. In addition, the Company has included an amortization of the generation net transition obligation for ratemaking purposes, although there is not amortization for per books expense. PURA requires only that the Commission recognize the pension and OPEB expense for generation computed in accordance with generally accepted accounting principles; it does not require that the Commission impute an additional amount for the generation net transition obligation. Accordingly, Cities plan to argue against this adjustment.

12. Bad debt expense.

The Company has included bad debt expense based on 5 year average of actual experience due to REPs and other miscellaneous revenues. Cities plan to reject 5 year average because this would be retroactive ratemaking. Instead, Cities will recommend either the test year amount or zero (for the REPs) and the test year amount for other miscellaneous revenues.

13. Affiliate transaction expenses incurred from AEP Service Corp.

Cities will be addressing the reasonableness of expenses associated with TCC's proposed affiliate transactions with AEPSC.

14. Amortization of regulatory assets: debt refinancing – restructuring costs.

See discussion under Rate Base Issues. In addition, the Company failed to allocate any portion of this amortization expense to transmission. Cities will propose that a portion of this amortization expense be allocated to transmission if PUC does not put it in the cost of debt, which inherently ensures that a portion of the cost is allocated to transmission by applying the rate of return to the T and D rate base amounts, respectively.

15. Storm damage expense accrual.

The Company has proposed an increase in the storm damage expense accrual to $3.2 million from Docket 28840 $0.9 million level. This increase is based on projected losses rather than historic losses. TCC refers to this storm damage expense as "funding for its catastrophe reserve account." Cities plan to oppose this because it is unnecessary and excessive.

16. Amortization of gains from sale of buildings.

The Company excluded the gains from the 2005 sales of buildings. Ratepayers are entitled to these gains. Cities plan to propose a deferral of the gains and amortization over 3 years on a levelized basis (the combination return of and on are levelized so that the revenue requirement effect is the same in each of the 3 years).

17. Depreciation on CWIP reclassified to plant in service at June 30, 2006.

The depreciation expense on this CWIP should be removed from the revenue requirement for the same reasons as the CWIP should not be included in rate base (see Rate Base Issues).

18. Depreciation rates and resulting depreciation expense.

Cities will be proposing adjustments to address the plant service lives and survivor curves underlying TCC's proposed depreciation rates.

19. Depreciation and interest expense on SFAS 143 ARO.

Cities will propose removing all effects of SFAS 143 from rate base and operating expense (see Rate Base Issues).

20. Income tax expense: investment tax credit amortization (ITC).

Cities will propose to incorporate effect of changes in depreciation rates on ITC (effect is the opposite sign from effect on depreciation expense).

21. Income tax expense: consolidated tax savings adjustment (CTSA).

The Companies have not included consolidated tax savings adjustments ("CTSA") in their filed revenue requirements, but they have quantified the amounts. Cities will argue for the CTSA in accordance with Commission precedent, among other reasons.

D. MISCELLANEOUS REVENUE ISSUE

22. ABD (transmission construction services) revenues.

The Company removed the margins (revenues less expenses) resulting from its transmission construction services provided to third parties, including LCRA. Cities plan to argue that these revenues should continue to be imputed to the Company for the benefit of the ratepayers.

E. COST ALLOCATION, RATE DESIGN AND NEW TARIFFS

23. Class cost allocation and rate design.

Cities are evaluating TCC's proposed rate design and allocation of revenues among rate classes and will recommend appropriate adjustments as needed.

24. New Riders and effect on base revenue requirement.

Cities will be addressing TCC's proposals to implement new riders to allow for future pass through of costs, including:

- Energy Efficiency Cost Recovery Rider
- Municipal Franchise Fee Adjustment Rider
- Rate Case Expense Rider
- Ad Valorem Tax Adjustment Rider

F. FINANCIAL IMPACT OF ADJUSTMENTS

The above-described adjustments, with the additional adjustments that may be necessary based upon the consultants' continuing review of the rate application, will include the following impacts:

Distribution Rate Base:

Removal of Generation prepaid pension	$1,654,000
Removal of capital prepaid pension	$2,023,000
Removal of debt restructuring costs	$ 690,000
Reduce plant in service for affiliate adjustments	$ 256,000
Reduce cash working capital lead lag	$ 739,000
Correct ADIT errors	$ 983,000

Transmission Rate Base:

Removal of Construction Work in Progress	$ 717,000
Removal of generation prepaid pension	$ 207,000
Removal of capital prepaid pension	$ 357,000
Removal of debt restructuring costs	$ 377,000
Correct ADIT errors	$ 198,000

Distribution Rate of Return:

Return on equity at 9.0%	$13,175,000

Transmission Rate of Return:

Return on equity at 9.0%	$ 7,893,000

Distribution Expenses:

Reduce expense for consolidated tax savings	$1,225,000
Modify depreciation rates	$5,000,000
Remove catastrophic loss adjustment	$2,875,000
Reduce affiliate charges	$8,044,000
Adjust payroll annualization	$2,552,000
Adjust incentive compensation	$2,132,000
Remove generation OPEBs	$ 786,000
Removal amortization of debt reacquisition costs	$ 915,000

Transmission Expenses:

Reduce expense for consolidated tax savings	$1,699,000
Remove depreciation expense on CWIP	$ 103,000
Adjust payroll annualization	$ 621,000
Remove catastrophic loss adjustment	$ 315,000
Adjust incentive compensation	$ 301,000

These above adjustments, as described in more detail above, achieve a reasonable response to the Company's filing. However, these adjustments are preliminary, and could increase if the Cities' actions are appealed to the PUC where the consultants will undertake more aggressive efforts to identify additional adjustments.

Diane Hosea

From:	Gail Johle [gjohle@lglawfirm.com] on behalf of Kristi Gotcher [kgotcher@lglawfirm.com]
Sent:	Thursday, February 08, 2007 12:44 PM
To:	city@georgewest.org; Devine CM (Dora V. Rodriquez); Dilley (Felix Arambula); Dilley Mayor (Russell J. Foster); Donna Mayor (Ricardo L. Morales); Eagle Lake (Ronald Holland); Eagle Pass (Marga Lopez); Eagle Pass (Mary Velasquez); Edna (Becky Miska); El Campo (John Steelman); Freer (Cindy Lackey); George West Mayor (August E. Caron, Jr.); Goliad CM (Ken Bays); Goliad Mayor (William J. Schaefer); Harlingen (Brendan Hall); Harlingen Mayor (Richard R. Rodriguez); Hidalgo (Joe Vera); Ingleside (Kimberly Drysdale); Ingleside (Stan Bryum); Ingleside on the Bay CS (Diane Hosea); Kenedy (Sandra Lundquist); Kenedy (Walter Hill); Kingsville (Edna Lopez); Kingsville CM (Carlos Yerena); cityofkc@sbcglobal.net
Cc:	Thomas Brocato; Kristi Gotcher
Subject:	Corrections to TCC Rate Case Ordinance.
Attachments:	Page 2 only from ordinance sent 2.7.07.doc; TCC Intervening Cities.doc

Yesterday we forwarded to each of you a cover memo, consultant report, rate ordinance and model staff report for you to use in setting electric rates within your city. Since that time I have noticed three minor errors in those documents. First, on page 2 at section 3 of the ordinance the word "requested" should be deleted. While I don't think that inclusion of the word is a fatal flaw, we request that you either strike the word from yesterday's version or use the corrected page that I am attaching to this email (removal of the word will not impact the remaining formatting on the document so it can simply be inserted). Second, the heading of my cover memo was incorrectly titled "Passing of Resolutions." Of course, it is actually an ordinance that needs to be adopted. Lastly, on the first page of the model staff report it states that a list of intervening cities was attached however it was not provided. I am attaching the list of cities to this email. I apologize for this inconvenience. If you have any questions please contact me by email or phone. My number is 512-322-5857. Thomas Brocato

Kristi Gotcher
Paralegal
Lloyd Gosselink Blevins Rochelle & Townsend, P.C.
816 Congress Avenue, Suite 1900
Austin, Texas 78701
(512) 322-5800 phone
(512) 322-5883 direct
(512) 472-0532 fax
kgotcher@lglawfirm.com

Intervening Cities
Texas Central Company – Dkt 33309

Alamo
Alice
Alton
Asherton
Bay City
Bayview
Beeville
Big Wells
Bishop
Bracketville
Brownsville
Carrizo Springs
Charlotte
Combes
Corpus Christi
Del Rio
Devine
Dilley
Donna
Edinburg
Edna
El Campo
Eagle Lake
Eagle Pass
Freer
Ganado
George West
Goliad
Harlingen
Hidalgo
Ingleside
Ingleside on the Bay
Karnes City
Kenedy
Kingsville
La Feria
La Joya
Laguna Vista
Laredo
Los Fresnos
Los Indios
Lyford
Lytle
Mathis
McAllen
Mercedes
Mission
Nordheim
Odem
Orange Grove
Palm Valley
Penitas
Pharr
Pleasanton
Point Comfort
Port Aransas
Port Isabel
Portland
Port Lavaca
Poteet
Primera
Rancho Viejo
Raymondville
Refugio
Rio Grande City
Rio Hondo
Rockport
Roma
Runge
Sabinal
San Benito
San Juan
Santa Rosa
Sinton
Smiley
South Padre Island
Sullivan City
Taft
Uvalde
Victoria
Weslaco
Woodsboro