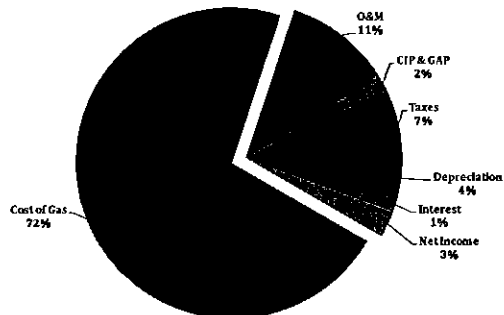


Legislative Energy Commission July 22, 2010

Net Income in Relation to Total Cost

- Net income represents a small part of a natural gas utility's total cost



What Drives Rate Cases



Depends upon circumstance:

- Declining use per customer (rate design)
- Capital additions –
 - 1997-2007
 - ◆ Invested over \$440 million (+61%)
 - ◆ Residential + small business customer growth – 142,000 (+22%)
 - ◆ Residential + small business gas use is flat (use per customer is declining)
- General Costs
- Higher Gas Costs
 - Bad Debt Expense
 - Cash Working Capital Requirements (Gas inventory, Accounts Receivable, etc.)
- Cost of Capital
- Efficiency Offsets:

	1982	1982 to 2009 Inflated	Act. 2009
▪ Residential Non-Gas Costs	\$206	\$460	\$250

Cost Recovery Mechanism (Riders)



- Variable, largely outside utility control
- Absent rider, great risk
 - PGA
- Policy Driven
 - Energy conservation
- Benefits:
 - Equitable – customers pay for the actual costs - no more, no less
 - Increased transparency/reoccurring review
 - Accurate price signals
 - Predictability and stability (reduced regulatory lag) - allows the company to attract capital with more favorable costs and terms.

Quality of State Regulation – The “Doorway” to Investment Decisions



- Many in the investment community indicate that the quality of state regulation is the first criteria that they evaluate when making investment decisions regarding utilities. For example, –

“In evaluating a utility’s regulatory framework, we consider such things as the regulatory body’s independence; its legislative or political environment; the extent of the regulatory framework’s development; its track record for predictable, stable decisions; the utility’s business model; and the openness of the regulators to alternative rate mechanisms that tend to provide additional assurance of timely cost recovery and the ability to earn a return on invested capital.” (Emphasis added)

Source: Moody’s Investor Services, Regulatory Frameworks – Ratings and Credit Quality for Investor-owned Utilities, June 18, 2010.

What is the Most Efficient Process For Setting Rates?



It depends/toolbox :

- Certain costs – variability/policy driven
- Alternative Ratemaking

Alternative Ratemaking



Objectives

- Reduce regulatory lag allowing all stakeholders to be more responsive to energy issues.
 - Streamline the time period required to review the utilities' costs of service and set rates.
- Reduce the cost of regulation (rate case expenses) through administrative efficiencies.
 - More interactive and efficient regulatory process.
 - Allow stakeholders to conduct interim review of financial information.

Alternative Ratemaking



One Model

- Utilities file to make periodic adjustments to distribution rates based on a comparison of actual to approved rates of return.
- Filings by utilities are staggered throughout the year to "even out" stakeholders' workload.
- Rate adjustment mechanisms are based on an earnings sharing approach - where the utility and its customers share any increase or decrease in achieved earnings relative to a banded earnings level.
- Narrows the issues that are considered in setting rates....typically:
 - Pro forma adjustments are limited.
 - Rates of return, depreciation rates, cost allocation and rate design based on prescribed formula or last rate case.
 - Other tariffs and services remain unchanged.



Jeff Daugherty
Director, Regulatory and Legislative Activities
(612) 321-5070
Jeffrey.Daugherty@CenterPointEnergy.com

