

BEFORE THE  
ARKANSAS PUBLIC SERVICE COMMISSION

IN THE MATTER OF THE APPLICATION	)	
OF OKLAHOMA GAS AND ELECTRIC	)	
COMPANY FOR APPROVAL OF A GENERAL	)	DOCKET NO. 16-052-U
CHANGE IN RATES, CHARGES AND TARIFFS	)	

SURREBUTTAL TESTIMONY

OF

JEFF HILTON  
DIRECTOR OF REVENUE REQUIREMENTS

ON BEHALF OF THE GENERAL STAFF  
OF THE ARKANSAS PUBLIC SERVICE COMMISSION

MARCH 30, 2017

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DOCKET NO. 16-052-U  
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**INTRODUCTION**

**Q. Please state your name.**

A. My name is Jeff Hilton.

**Q. Are you the same Jeff Hilton who filed Direct Testimony on January 31, 2017, on behalf of the General Staff (Staff) of the Arkansas Public Service Commission (Commission)?**

A. Yes.

**PURPOSE OF TESTIMONY**

**Q. What is the purpose of your Surrebuttal Testimony in this docket?**

A. The purpose of my Surrebuttal Testimony is to present the results of Staff's Surrebuttal case. Specifically, I am sponsoring Staff Surrebuttal Exhibits JH-1 through JH-7. I will also discuss Staff's recommendation regarding the Storm Damage Recovery Rider (SDR), the Formula Rate Plan Rider (FRP Rider), the Revenue Conversion Factor (RCF), and Staff's treatment of revenues from expiring riders. In so doing, I will address the Rebuttal Testimony of Company witnesses Gwin Cash and Donald R. Rowlett, and the Direct Testimony of the Office of Arkansas Attorney General Leslie Rutledge (AG) witness David E. Dismukes.

**REVENUE REQUIREMENT**

**Q. What are the results of Staff's analysis?**

A. Staff's Arkansas retail non-fuel Revenue Requirement calculation is shown on my

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1 Surrebuttal Exhibit JH-1, Summary of Operations. Staff's recommendations  
2 result in an Arkansas retail Revenue Requirement of \$103,832,384 and a  
3 Revenue Deficiency of \$18,170,088. In contrast, OG&E includes in Rebuttal an  
4 Arkansas retail Revenue Requirement of \$110,345,373 resulting in a Revenue  
5 Deficiency of \$15,028,645, a difference of \$6,512,989 and \$3,141,443,  
6 respectively. The disparity in the differences between the Revenue Requirement  
7 and Revenue Deficiency is due to the treatment of certain rider revenues that are  
8 expiring and will be included in base rates as a result of this case. The Rider  
9 Revenue involved is \$9,741,043 based on Staff's case. I will address this in  
10 greater detail below.

11 **Q. Please describe the derivation of Staff's recommended Revenue**  
12 **Requirement.**

13 A. The development of Staff's case is shown on Surrebuttal Exhibits JH-2 through  
14 JH-6. Staff's recommended adjustments to Rate Base are shown on Surrebuttal  
15 Exhibit JH-3 and are summarized on Surrebuttal Exhibit JH-2. Staff's  
16 recommended adjustments to Revenues and Expense are shown on Surrebuttal  
17 Exhibit JH-5 and are summarized on Surrebuttal Exhibit JH-4. Surrebuttal  
18 Exhibit JH-6 illustrates the determination of Arkansas-jurisdictional income taxes.

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**RECONCILIATION**

**Q. What items differentiate Staff's recommended Arkansas retail non-fuel Revenue Requirement from the Company's requested Revenue Requirement?**

A. Surrebuttal Exhibit JH-7 summarizes and reconciles the differences between Staff's and the Company's Arkansas retail Revenue Requirement. It begins with the Company's Arkansas retail Revenue Requirement as filed in its Rebuttal MFRs and makes adjustments to arrive at Staff's recommended Arkansas non-fuel Revenue Requirement. It delineates the four areas affecting revenue requirement: Rate Base, Rate of Return, Income Taxes / Revenue Conversion Factor, and Operating Expenses. The underlying reasons for the differences in these four areas are discussed in the Surrebuttal Testimony of the respective sponsoring Staff witness. I discuss the noteworthy differences between OG&E's and Staff's recommended Revenue Requirement below.

Staff's recommended Required Rate of Return is 5.36% compared to the Company's proposed Required Rate of Return of 6.01%. The difference of 65 basis points along with the associated change in Weighted Cost of Debt results in a Revenue Requirement difference of \$5.9 million based upon Staff's Surrebuttal case. Please note that the \$3.4 million Rate of Return impact in my Reconciliation excludes the effect of grossing up the difference for income taxes. The primary reason for this difference is the Required Return on Equity of 9.5%

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recommended by Staff and 10.25% requested by OG&E, as discussed in the Surrebuttal Testimony of Staff witness Regis Powell. In addition, Staff's recommended Arkansas Rate Base differs from OG&E's by \$10.0 million, with the primary difference being *pro forma* plant additions. Staff witness William L. Matthews discusses the differences in plant between Staff and the Company.

**TREATMENT OF EXPIRING RIDERS INCLUDED IN BASE RATES**

**Q. Did the Company continue to include revenues from riders that will expire or otherwise be included in base rates coincident with the implementation of rates (Expiring Riders) resulting from this case?**

A. Yes. OG&E included both expenses and revenues from its Environmental Compliance Plan Rider, Smart Grid Recovery Rider, the Lost Contribution to Fixed Charges component of the Energy Efficiency Cost Recovery Rider, and the Crossroads Wind Farm amount recovered in the Energy Cost Recovery Rider in its Application, and the Company has updated its Rebuttal recommendation to include the Load Reduction Rider subscription payments that will be recovered in base rates as well. Company witness Cash addressed the additional amount requested for these subscription payments of \$2.974 million and referred to his updated *pro forma* Adjustment IS-11 of \$9.686 million to include the total amount of revenues associated with all of the Expiring Riders.<sup>1</sup>

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<sup>1</sup> Rebuttal Testimony of Gwin Cash, p. 5, line 21 – p.6, line 3.

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**Q. Did Staff include the revenues and expenses related to the Expiring Riders in its base rate revenues and expenses?**

A. Staff's recommendation has not changed since Direct Testimony. Staff included the expenses in its base rate calculation, but excluded the Expiring Rider revenues. As previously discussed in my Direct Testimony, Staff treated these items in this manner to reflect the change in base rates only, as reflected in the Revenue Deficiency. Therefore, Staff did not include its comparable amount of rider revenues of \$9,741,043, and Staff's Adjustment IS-11 is zero. I am including Table 1, below, which shows the effect of including the rider revenues in Staff's calculations, and Table 2, below, which compares Staff's Revenue Requirement components with those in the Company's Rebuttal case. Note that regardless of how the Expiring Rider revenues are treated, the Revenue Requirement is not affected.

**TABLE 1  
COMPARISON OF THE EFFECT OF EXPIRING RIDER REVENUES  
ON STAFF'S REVENUE REQUIREMENT**

<b>Revenue Requirement Component</b>	<b>Excluding Rider Revenues</b>	<b>Including Rider Revenues</b>	<b>Difference</b>
<b>Total Operating Revenues</b>	\$85,662,296	\$95,403,338	\$(9,741,043)
<b>Revenue Deficiency</b>	\$18,170,088	\$8,429,045	\$9,741,043
<b>Revenue Requirement</b>	\$103,832,384	\$103,832,384	\$0

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**TABLE 2**  
**COMPARISON OF STAFF'S AND OG&E'S REVENUE REQUIREMENT**

<b>Revenue Requirement Component</b>	<b>Staff Surrebuttal</b>	<b>OG&amp;E Rebuttal</b>	<b>Difference</b>
<b>Excluding Rider Revenues (Staff's Case Only):</b>			
<b>Operating Revenues</b>	\$85,662,296	\$95,316,728	\$(9,654,432)
<b>Revenue Deficiency</b>	\$18,170,088	\$15,028,645	\$3,141,443
<b>Revenue Requirement</b>	\$103,832,384	\$110,345,373	\$(6,512,989)
<b>Including Rider Revenues:</b>			
<b>Operating Revenues</b>	\$95,403,338	\$95,316,728	\$(86,610)
<b>Revenue Deficiency</b>	\$8,429,045	\$15,028,645	\$(6,599,600)
<b>Revenue Requirement</b>	\$103,832,384	\$110,345,373	\$(6,512,989)

**REVENUE CONVERSION FACTOR**

**Q. Did your determination of the RCF for each rate class change since Direct Testimony?**

A. No. I continue to include the Uncollectible Accounts ratio and the composite income tax percentage, which reflects the Manufacturing Tax Deduction, in the determination of each class's RCF. The composite RCF, shown on Surrebuttal Exhibit JH-1, reflects the weighted average as determined in the Class Cost of Service Study presented by Staff witness Matthew S. Klucher. Therefore, the total Arkansas retail RCF is 1.6272, which is .0002 less than that used in Staff's Direct case.

**Q. Did OG&E address the RCF?**

A. No. The RCF was not addressed in OG&E's Rebuttal Testimony. The Company included language regarding the Manufacturing Tax Deduction in its FRP Rider,

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1 but its Rebuttal MFR Schedule A-1 did not include the Manufacturing Tax  
2 Deduction.

3 **STORM DAMAGE RECOVERY RIDER**

4 **Q. Did OG&E address its proposal or your Direct Testimony regarding SDR?**

5 A. No. In his Rebuttal Testimony, OG&E witness Rowlett only noted the SDR in  
6 regard to the FRP Rider included with its Application, stating that “[i]n the event  
7 that the Company’s proposed Large Capital Additions (“LCA”) Rider and Storm  
8 Damage Recovery (“SDR”) Rider are not approved, the Company will need to  
9 amend Attachment A-1 of the FRP Rider to remove these riders from the  
10 proposed FRP Rider.”<sup>2</sup> However, Attachment A-1 of the Company’s revised FRP  
11 Rider, Sheet Nos. 80.0 – 80.3, included as Rebuttal Exhibit GC-1 to OG&E  
12 witness Cash’s Rebuttal Testimony,<sup>3</sup> does not refer to the SDR. If the SDR is  
13 approved for use, it will need to be added to the excluded Schedules in  
14 Attachment A-1.

15 **Q. Do you continue to recommend the Commission reject the Company’s**  
16 **proposed SDR at this time?**

17 A. Yes. As I discuss in my Direct Testimony, Staff recommends approval of the  
18 FRP Rider and, because it is specifically designed to capture these types of  
19 costs on a timely basis, the SDR is unnecessary. Therefore, I recommend that

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<sup>2</sup> Rebuttal Testimony of Donald Rowlett, p. 8, line 15 – p. 9, line 2.

<sup>3</sup> Rebuttal Exhibit of Gwin Cash, p. 5.

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1 the SDR be reserved for use when storm costs are atypical and that both the  
2 need for and the terms of recovery via the SDR be addressed on a case-by-case  
3 basis.

4 **FORMULA RATE PLAN**

5 **Q. Did OG&E address Staff's proposed FRP Rider?**

6 A. Yes. OG&E witness Cash agreed with Staff's recommendations regarding the  
7 FRP Rider and the timing of the Evaluation Report and effective date, with one  
8 exception.<sup>4</sup> He disagreed with Staff's inclusion of a fixed Debt-to-Equity (DTE)  
9 ratio and short-term debt proportion in favor of its actual capital structure.<sup>5</sup>  
10 OG&E's proposed FRP Rider provided a range of DTE, including short-term debt  
11 of 44/56 to 50/50. Mr. Cash did not address this issue further but referred to  
12 Company witnesses Donald R. Rowlett and Robert B. Hevert, both of whom  
13 address OG&E's use of the Company's actual capital structure rather than a  
14 hypothetical capital structure proposed by Staff and the intervenors.

15 AG witness Dismukes discusses this issue in his Direct Testimony.<sup>6</sup> Dr.  
16 Dismukes compares OG&E's proposal to the Commission-approved FRP Riders  
17 of Entergy Arkansas, Inc. (EAI) and CenterPoint Energy Arkansas Gas (CEA).  
18 Dr. Dismukes notes that CEA's FRP Rider utilizes a fixed capital structure  
19 consistent with that approved in its last rate case; and that EAI's FRP Rider

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<sup>4</sup> Rebuttal Testimony of Gwin Cash, p. 2, line 24 – p. 3, line 8.

<sup>5</sup> *Id.* at 3, lines 10-20.

<sup>6</sup> Direct Testimony of David E. Dismukes, p. 20, line 11 - p. 22, line 21.

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1 includes a range, but that the equity range is from 44 to 50 percent, while  
2 OG&E's proposal includes an equity range from 50 to 56 percent. Dr. Dismukes  
3 summarizes the basis for his recommendation to include a fixed capital structure  
4 as providing incentives to utilities to increase cost efficiencies, rather than  
5 receiving earnings by simply changing the capital structure.<sup>7</sup>

6 Staff continues to recommend a fixed capital structure including short-term  
7 debt. Staff witness Regis Powell addresses Staff's reliance on a hypothetical  
8 capital structure and the use of a fixed capital structure in the FRP Rider.<sup>8</sup>

9 **Q. Did AG witness Dismukes address any other FRP Rider issues?**

10 A. Yes. He discussed two other concerns. First, he asserted that there was  
11 ambiguity in regard to the Company's proposed FRP Rider Test Period, which  
12 resulted in his recommendation that the Commission direct the Company to  
13 clarify the definition of its Projected Year in Attachment C of its FRP Rider.  
14 Additionally, Dr. Dismukes recommended that the Company should be required  
15 to clearly indicate which type of Test Period it is using, with the definition of this  
16 Test Period being directly tied to the statutory language.<sup>9</sup>

17 **Q. How did OG&E respond to AG witness Dismukes' recommendation**  
18 **regarding the Test Period?**

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<sup>7</sup> *Id.* at 21, lines 7-12.

<sup>8</sup> Surrebuttal Testimony of Regis Powell, p. 21, line 18 - p. 22, line 8.

<sup>9</sup> Direct Testimony of David E. Dismukes, p. 20, lines 6-10.

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1 A. Company witness Cash addressed this concern by stating that the Company's  
2 intent is to utilize a Projected Year as its Test Period. Also, the Company made a  
3 change to Attachment C in its FRP Rider to state how the Projected Year will be  
4 developed; illustrating that it is not based on an Official Company Budget.<sup>10</sup>

5 **Q. Has AG witness Dismukes' concern regarding OG&E's designation of a**  
6 **Test Period been resolved?**

7 A. Yes. Section 80.3(B) of OG&E's proposed tariff, presented on page 1 of OG&E  
8 witness Cash's Rebuttal Exhibit GC-1, defines the Formula Rate Review Test  
9 Period as being based upon a Projected Year. I agree with Mr. Cash that the  
10 Attachment C usage of the term "Historical Year" simply refers to the 12 months  
11 ending March 31 preceding the filing of an Evaluation Report, as defined in  
12 section 80.3(C) of the tariff, and is not to be confused with the election of the Test  
13 Period. Therefore, no specific directive from the Commission is needed  
14 regarding this issue.

15 **Q. What was AG witness Dismukes' second concern relating to the FRP**  
16 **Rider?**

17 A. Dr. Dismukes expressed concern about difficulties that could arise in comparing  
18 the first year FRP Rider annual review information with historic trends,  
19 particularly in the area of the Company's jurisdictional allocations.<sup>11</sup> This

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<sup>10</sup> Rebuttal Testimony of Gwin Cash, p. 3, line 22 – p. 4, line 12.

<sup>11</sup> Direct Testimony of David E. Dismukes, p. 23, lines 2-19.

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1 concern resulted in his recommendation for OG&E to provide comparative  
2 information that examines the major costs and drivers between its projected and  
3 current rate case test year for the first two years of the FRP Rider.<sup>12</sup> He notes  
4 that the information would not be used for any type of reconciliation.

5 **Q. What was OG&E witness Cash's response to AG witness Dismukes'**  
6 **second concern about the FRP Rider?**

7 A. Mr. Cash discussed the statutory requirement for "netting", and also cited to my  
8 Direct Testimony, in support of his position "[t]hat this netting will occur with the  
9 third Evaluation Report filing and is the earliest that it can be included."<sup>13</sup>

10 **Q. Do you agree with OG&E that AG witness Dismukes' requested information**  
11 **cannot be provided until the third Evaluation Report?**

12 A. No. I agree with the Company that Attachment D Schedules containing Historical  
13 Year information are not required in the first two years and any information that  
14 was provided could not be used as a basis for any type of netting. However, the  
15 information requested by Dr. Dismukes could be useful in analyzing OG&E's  
16 request. To be clear, Dr. Dismukes specifically mentioned EAI's Attachment E  
17 Filing Requirements, Item 24, which is the validation analysis required by EAI.<sup>14</sup>  
18 OG&E's Attachment E Filing Requirements do not require a validation analysis  
19 because all of its adjustments to the Historical Year data will be supported and

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<sup>12</sup> *Id.* at 25, lines 5-14.

<sup>13</sup> Rebuttal Testimony of Gwin Cash, p. 4, Lines 14-27.

<sup>14</sup> Direct Testimony of David E. Dismukes, p. 24, lines 1-12.

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1 no such threshold before an explanation is required or will be needed. The  
2 information required of EAI in item 24 include: the adjusted historical year, the  
3 adjusted projected year and a comparison of the difference of those years'  
4 amounts with a trended average by account. However, in EAI's initial filing, it  
5 also provided the final compliance account balances from the recent rate case.  
6 In addition, EAI witness Myra L. Talkington provided an exhibit (Direct Exhibit  
7 MLT-2)<sup>15</sup> with the significant drivers since the conclusion of its rate case. As Dr.  
8 Dismukes noted, this type of information will assist in evaluating the  
9 reasonableness of certain costs and the accuracy of the Company's projections  
10 in a more timely manner.<sup>16</sup> Because the Filing Requirements only include a  
11 reconciliation of the Historical Year with the Projected Year in the third year and  
12 do not specifically require a reconciliation of the Projected Year with the results of  
13 the instant rate case, I agree with Dr. Dismukes that this information could be  
14 helpful in analyzing OG&E's requested increase. Therefore, I recommend that  
15 OG&E provide this information in its initial and second Evaluation Report filings.

16 **Q. What modification do you recommend to the FRP Rider, included in**  
17 **Rebuttal Exhibit GC-1?**

18 A. I recommend restoring the language regarding the use of the fixed DTE,  
19 including the short-term debt proportion, from my Direct Exhibit JH-9, in

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<sup>15</sup> Docket No. 16-036-FR, EAI Direct Exhibit MLT-2 to Direct Testimony of Myra L. Talkington, pp. 25-26.

<sup>16</sup> Direct Testimony of David E. Dismukes, p. 23, lines 9-19.

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1 Attachments B-5, D-5, and Attachment C, Section II, paragraph E.4.

2 **Q. Does this conclude your testimony?**

3 A. Yes, it does.

**CERTIFICATE OF SERVICE**

I hereby certify that a copy of the foregoing has been served on all parties of record by electronic means via the Commission's Electronic Filing System this 30<sup>th</sup> day of March, 2017.

/s/ Justin A. Hinton  
Justin A. Hinton