

BEFORE THE
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

REHEARING DIRECT TESTIMONY

OF

HUGH T. MCDONALD

PRESIDENT AND CHIEF EXECUTIVE OFFICER
ENTERGY ARKANSAS, INC.

ON BEHALF OF

ENTERGY ARKANSAS, INC.

MARCH 14, 2014

1 I. **BACKGROUND AND INTRODUCTION**

2 Q. PLEASE STATE YOUR NAME.

3 A. My name is Hugh T. McDonald.

4

5 Q. ARE YOU THE SAME HUGH T. MCDONALD WHO PREVIOUSLY
6 FILED TESTIMONY IN THIS DOCKET?

7 A. Yes, I am.

8

9 Q. ON WHOSE BEHALF ARE YOU TESTIFYING?

10 A. I am submitting this rehearing direct testimony to the Arkansas Public
11 Service Commission ("APSC" or the "Commission") on behalf of
12 Entergy Arkansas, Inc. ("EAI" or the "Company").

13

14 Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?

15 A. The APSC granted EAI's petition for rehearing in this docket and
16 allowed EAI to present new evidence related to the reaction of several
17 security analysts and a rating agency to Order No. 21 (the "Order") as
18 well as a report on Return on Equity ("ROE") decisions in other utility
19 rate cases. My testimony will underscore the importance of granting
20 the relief sought in EAI's petition for rehearing. The Company is at a
21 crossroads. It needs financial stability to meet the challenges of
22 operating independently of the Entergy System Agreement and the
23 significant capital investment planned in the next few years. Now is

1 not the time to test the Company's ability to meet these challenges if
2 hindered by a sub-standard return on equity ("ROE"), a formula for
3 calculating Allowance for Funds Used During Construction ("AFUDC")
4 that does not fully recover financing costs, and disallowed costs that
5 will prevent EAI from earning even the low allowed ROE.

6
7 Q. IS THE COMPANY SPONSORING OTHER WITNESSES?

8 A. Yes. EAI witness David Hunt, in his rehearing direct testimony,
9 presents reports from equity financial analysts and a rating agency in
10 response to the order. In addition, he provides a comparison of the
11 ROE determination in this case with other regulatory commission ROE
12 determinations in calendar year 2013 and historically, which
13 demonstrates that the 9.3 percent ROE allowed for EAI in this case
14 was the second lowest ROE awarded to a vertically integrated electric
15 utility in 2013, the lowest non-penalty ROE awarded to a vertically
16 integrated electric utility in 2013, and among the lowest ROEs ever
17 awarded to an investor-owned, vertically integrated electric utility. In
18 addition, former utility analyst Ellen Lapson of Lapson Consulting
19 explains how the significant disparity in EAI's allowed ROE and that of
20 other peer utilities has created a reaction among security analysts and
21 a rating agency that is negative to EAI and its customers.

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1 **II. SUPPORT FOR RELIEF ON REHEARING**

2 Q. WHY HAS EAI REQUESTED REHEARING OF THE ORDER?

3 A. EAI has just completed a decade-long transition out of the System
4 Agreement and into operation in the Midcontinent Independent System
5 Operator, Inc. ("MISO") Regional Transmission Organization. As a
6 result, for the first time since 1951, EAI is operating and transacting in
7 power markets on its own behalf rather than under the System
8 Agreement.

9 In addition to operating within the new framework, the Company
10 faces a number of other challenges in the near future. EAI must
11 continue to make investments required to serve customers in its
12 service territory. Plus, the industry is changing rapidly, and EAI plans
13 to investment approximately \$3.4 billion from 2012 through 2018¹ to
14 meet evolving environmental standards, infrastructure needs in
15 generation, transmission, and distribution, as well as, strategic
16 initiatives like smart grid development and recruitment of energy
17 intensive industries. Successfully addressing these initiatives will
18 require the Commission's support, and the Order does just the
19 opposite.

¹ Lewis Direct Testimony at 5 (March 1, 2013).

1 Q. WHY DO YOU SAY THAT?

2 A. The reality facing EAI as a result of the Order is that a 9.3 percent
3 allowed ROE will hinder the Company's ability to acquire capital and
4 the cost of that capital will be higher. Further, the Order disallowed
5 recovery of several categories of costs that do not go away because
6 they are not reflected in rates, which will reduce the actual return of the
7 Company even more. And finally, the cap on the AFUDC rate set in
8 the Order will erode EAI's earnings even further as investments are
9 completed and the cost of that investment, including AFUDC, is placed
10 into rates that do not fully reflect actual financing costs.²

11

12 Q. WHAT OTHER IMPACT WILL THE ORDER HAVE?

13 A. It could negatively affect economic development in the state. EAI has
14 a long history of active involvement in attracting industrial prospects to
15 the communities it serves. EAI is heavily involved with the Arkansas
16 Department of Economic Development and the Governor's office in
17 major industrial retention and recruitment efforts. This is a benefit to
18 the state because industrial growth brings more jobs and higher tax
19 revenues, a benefit to the Company because growth produces higher
20 revenues, and a benefit to customers because these higher revenues
21 offset future rate increases. The effects of the Order impair EAI in

² See *id.* at 7.

1 playing a major role in attracting new industry if that requires incentives
2 and significant capital investment to induce an industrial prospect to
3 locate in Arkansas.

4

5 Q. WHY SHOULD THE COMMISSION GRANT EAI ANY RELIEF ON
6 THE ISSUES IN ITS PETITION?

7 A. There are at least two bases for the Commission to reconsider its
8 decisions on issues in the Order that have come to light since it was
9 issued. First, Ms. Lapson explains her view that the consensus
10 reaction of financial analysts and a credit analysis firm is that the
11 collective impact of the Order -- including the 9.3 percent allowed ROE,
12 an AFUDC formula that does not fully compensate the Company for its
13 financing costs, and other cost disallowances -- will inhibit the
14 Company's ability to earn even this relatively low allowed ROE and will
15 weaken the Company financially. As a result, as Ms. Lapson explains,
16 the financial community will place a higher discount rate on Entergy
17 Corporation's equity because of the perception of greater regulatory
18 risk for EAI, which will increase the company's cost of capital. In
19 addition, Moody's Investors Service ("Moody's") recently completed a
20 review of the securities ratings of U.S. utilities by upgrading the
21 securities ratings of more than 90 percent of the utilities under
22 consideration. While Moody's upgraded the large majority of utilities
23 under consideration, including other Entergy Operating Companies,

1 Moody's did not upgrade EAI's securities ratings, citing the Order and
2 continuing concern about regulatory lag.³ As Ms. Lapson explains, the
3 effect is a downgrade in rating compared to most of the Company's
4 peers, which raises the cost for EAI to borrow money. This raises
5 customers' rates.

6 Second, Ms. Lapson explains that not recognizing the effect of
7 the Federal Reserve's monetary stimulus program and relying solely
8 on a quantitative analysis in setting the Company's allowed ROE
9 produced an unreasonable result that will hinder EAI's ability to secure
10 long-term debt on favorable terms and make it more costly for equity
11 investment in EAI. This raises customers' rates.

12 The Commission's granting of the Company's rehearing petition
13 provides the Commission an opportunity to review the new evidence
14 that EAI is submitting and to reconsider and revise its positions. By
15 doing so, the Commission would address those issues that create the
16 regulatory lag and weak operating cash flow ratios cited by Moody's in
17 explaining why it did not upgrade EAI's securities ratings and that
18 caused utility analysts to report the negative impact of the Order on
19 EAI's financial position, including: a 9.3 percent allowed ROE, an
20 AFUDC rate that does not fully compensate for construction cost

³ See Hunt Rehearing Direct Testimony, EAI Exhibit DEH-8 (March 14, 2014).

1 financing, and cost disallowances that hinder the Company's ability to
2 earn even the low allowed ROE.

3 The result of this rate case should be to position the Company
4 to serve its customers in the post-System Agreement world and to
5 support its communities in developing strong and vibrant economies.
6 By granting the requested relief, the public interest will be served, and
7 the Company will be spared the prospect of financial instability at this
8 critical time.

9

10 Q. DOES THIS CONCLUDE YOUR DIRECT TESTIMONY?

11 A. Yes.

CERTIFICATE OF SERVICE

I, Steven K. Strickland, do hereby certify that a copy of the foregoing has been served upon all parties of record by forwarding the same by electronic mail and/or first class mail, postage prepaid, this 14th day of March 2014.

/s/ Steven K. Strickland
Steven K. Strickland

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APPROVAL OF CHANGES IN RATES FOR)	DOCKET NO. 13-028-U
RETAIL ELECTRIC SERVICE)	

REHEARING DIRECT TESTIMONY

OF

DAVID E. HUNT

DIRECTOR, REGULATORY FILINGS
ENTERGY SERVICES, INC.

ON BEHALF OF

ENTERGY ARKANSAS, INC.

MARCH 14, 2014

1 **I. INTRODUCTION**

2 Q. PLEASE STATE YOUR NAME.

3 A. My name is David E. Hunt.

4

5 Q. ON WHOSE BEHALF ARE YOU TESTIFYING?

6 A. I am testifying on behalf of Entergy Arkansas, Inc. ("EAI or the
7 "Company").

8

9 Q. ARE YOU THE SAME DAVID E. HUNT WHO ADOPTED THE DIRECT
10 TESTIMONY OF PHILLIP B. GILLAM FILED IN THIS DOCKET ON
11 MARCH 1, 2013, AND WHO FILED REBUTTAL TESTIMONY ON
12 AUGUST 26, 2013, AND SUR-SURREBUTTAL TESTIMONY ON
13 SEPTEMBER 23, 2013?

14 A. Yes, but my position and job responsibilities have changed.

15

16 Q. WHAT CHANGES TO YOUR POSITION AND JOB RESPONSIBILITIES
17 HAVE OCCURRED SINCE YOU FILED SUR-SURREBUTTAL
18 TESTIMONY?

19 A. Effective January 19, 2014, my new position is Director, Regulatory Filings
20 for Entergy Services, Inc. ("ESI").¹ The Regulatory Filings Department is

¹ ESI is a subsidiary of Entergy Corporation that provides technical and administrative services to all the Entergy Operating Companies, which include EAI; Entergy Gulf States Louisiana, L.L.C. ("EGSL"); Entergy Louisiana, LLC ("ELL"); Entergy Mississippi, Inc. ("EMI"); Entergy New Orleans, Inc. ("ENOI"); and Entergy Texas, Inc. ("ETI").

1 responsible for the development, analysis, presentation, and support of
2 regulatory accounting data, revenue requirements, cost-of-service studies,
3 rate design data, and related regulatory filings for the Entergy Operating
4 Companies.

5

6 Q. ON WHOSE BEHALF ARE YOU TESTIFYING?

7 A. I am submitting this rehearing direct testimony to the Arkansas Public
8 Service Commission ("APSC" or the "Commission") on behalf of Entergy
9 Arkansas, Inc. ("EAI" or the "Company").

10

11 Q. WHAT IS THE PURPOSE OF YOUR REHEARING DIRECT
12 TESTIMONY?

13 A. The purpose of my rehearing direct testimony is to submit, explain, and
14 discuss certain additional evidence identified by EAI in support of its
15 Petition for Rehearing and Clarification filed on January 29, 2014, its
16 Supplement to Petition for Rehearing and Clarification filed on February 3,
17 2014, and its Reply to Responses to the Petition for Rehearing and
18 Clarification filed on February 14, 2014, as addressed by Amended Order
19 No. 25 issued February 26, 2014. EAI witness Hugh T. McDonald
20 provides a summary of the Company's rehearing direct testimony and EAI
21 witness Ellen Lapson provides analysis and comment with respect to the
22 new evidence being submitted.

23

1 **II. EQUITY FINANCIAL ANALYST AND RATING AGENCY DOCUMENTS**

2 Q. AFTER THE APSC ISSUED ORDER NO. 21 IN THIS CASE (THE
3 "ORDER"), DID SEVERAL EQUITY FINANCIAL ANALYSTS ISSUE
4 REPORTS EVALUATING THE DECISION?

5 A. Yes. Several utility equity analysts made specific reference to the Order in
6 reports, including Credit Suisse Securities Research & Analytics ("Credit
7 Suisse"), UBS, Deutsche Bank ("DB") Markets Research, and
8 International Strategy & Investment Group LLC ("ISI"). These well-
9 recognized equity analyst reports are attached to my testimony as EAI
10 Exhibit DEH-4 for the Credit Suisse report, EAI Exhibit DEH-5 for the UBS
11 report, EAI Exhibit DEH-6 for the DB report, and EAI Exhibit DEH-7 for the
12 ISI report. All four reports are available on a subscription-only basis and,
13 as such, are provided in their entirety as confidential documents pursuant
14 to the conditions of Interim Protective Order No. 2 in this docket.

15
16 Q. WAS THE ORDER A FACTOR IN ANY ACTIONS BY CREDIT RATING
17 AGENCIES?

18 A. Yes. In November 2013, Moody's Investors Service ("Moody's")
19 announced that it was reviewing a number of U.S. utilities for possible
20 upgrade. Moody's released the results of its review in a series of reports
21 in late January 2014, including a report focused on several Entergy
22 Corporation subsidiaries, including EAI, which was released on

1 January 31, 2014.² Moody's upgraded credit ratings for EGSL, ELL, EMI,
2 and ETI but maintained the ratings for EAI. The Moody's report is
3 attached to my testimony as EAI Exhibit DEH-8.

4
5 **III. ELECTRIC UTILITY ROE ANALYSIS**

6 Q. THE ANALYST REPORTS AND MOODY'S RATINGS REPORT
7 CHARACTERIZE THE 9.3 PERCENT ROE AS DISAPPOINTING OR
8 NEGATIVE. ACCORDING TO REGULATORY RESEARCH
9 ASSOCIATES, HOW DOES A 9.3 PERCENT ROE COMPARE TO
10 OTHER SIMILAR UTILITIES?

11 A. A 9.3 percent ROE compares unfavorably, according to the Major Rate
12 Case Decisions – Calendar 2013 report published by Regulatory
13 Research Associates ("RRA") on January 15, 2014, attached as EAI
14 Exhibit DEH-9. As with the equity analyst reports and the Moody's report,
15 Amended Order No. 25 authorized the Company to introduce this
16 document into evidence.

17
18 Q. CAN YOU BRIEFLY DESCRIBE THIS REPORT?

19 A. Yes. The Major Rate Case Decisions – Calendar 2013 report was
20 prepared by RRA after the end of 2013 to summarize the results of the
21 year's electric and gas rate case decisions. RRA updates this report on a

² Standard & Poor's is the other firm that issues credit ratings for Entergy Corporation and its affiliates. It has not issued any reports since the Order was issued.

1 quarterly basis throughout the year.³ The report includes several facts
2 from retail regulatory decisions in 2013, including overall rate of return on
3 rate base, allowed return on equity, common equity as a percent of the
4 utility's total capital structure, test year, rate base valuation method, and
5 dollar amount of approved rate increase or decrease. RRA also provides
6 significant information on a decision in footnotes to the report. For
7 example, footnote D indicates that a decision was for electric delivery
8 service only as compared to a decision for a vertically integrated utility
9 such as EAI. The report also contains historical annual and/or quarterly
10 rate of return and allowed ROE results since 1990. Access to RRA
11 reports and the RRA database is provided on a subscription-only basis,
12 and as such, the Major Rate Case Decisions – Calendar 2013 report is
13 being provided pursuant to the conditions of Interim Protective Order No. 2
14 in this docket.

15
16 Q. WHAT IS THE AVERAGE ALLOWED ROE FROM REGULATORY
17 PROCEEDINGS INVOLVING ELECTRIC UTILITIES IN 2013?

18 A. As tracked by RRA and stated in this report, the average ROE for electric
19 utilities based on 2013 regulatory decisions was 10.02 percent. This
20 average is based on 48 regulatory decisions in which an ROE was

³ The RRA Major Rate Cases report updated through the third quarter of 2013 was received by the APSC as a proffer during the evidentiary hearing and marked as EAI Proffered Exhibit 1. See Hearing Transcript at 619. It was discussed in camera during the oral examination of EAI witness Samuel C. Hadaway. See Hearing Transcript at 620-627.

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Table 1
Allowed ROEs By Quarter in 2013⁴

Quarter	Average Allowed ROE
1 ST	10.24%
2 ND	9.84%
3 RD	10.06%
4 TH	9.89%

Q. IS THE 10.02 PERCENT AVERAGE ALLOWED ROE FOR ALL ELECTRIC UTILITIES IN 2013 THE BEST COMPARISON FOR EAI'S ALLOWED ROE?

A. No. The 2013 RRA results reflect a variety of regulatory decisions, including ROEs for specific generating facilities and ROEs for utilities that only provide transmission or distribution service. These utilities are identified by the footnotes mentioned earlier.⁵ By excluding these results, the remaining decisions are for vertically integrated electric utilities, including EAI.

⁴ See EAI Exhibit DEH-9 at 3, which includes in its entirety the RRA Major Rate Case Decisions – Calendar 2013 report.

⁵ *Id.* at 8-9. Footnotes D, 1, 2, 3, 5, 6, 7, 9, 14, 16, and 22 contain information that indicates an ROE result for something other than a vertically integrated electric utility. The February 22, 2013 decision for Baltimore Gas and Electric in Maryland does not have a footnote but that regulatory jurisdiction has deregulated generation, and the decision is for distribution only. See the footnote for the Maryland decision for Baltimore Gas & Electric on December 13, 2013, that used a different test year.

1 Q. WHY IS IT MORE APPROPRIATE TO COMPARE EAI TO VERTICALLY
2 INTEGRATED ELECTRIC UTILITIES?

3 A. As RRA notes "...certain states unbundled electric rates and implemented
4 retail competition for generation,"⁶ which only allows the regulators in
5 those states to have jurisdiction over the transmission and/or distribution
6 service rates. A vertically integrated utility, with its additional responsibility
7 for providing generation service, has a higher risk profile than a service
8 provider with only transmission or distribution functions due to numerous
9 factors including environmental compliance costs and other long-term
10 generation planning requirements.

11
12 Q. WHAT ARE THE RESULTS ONCE YOU NARROW THE FOCUS TO
13 VERTICALLY INTEGRATED ELECTRIC UTILITIES?

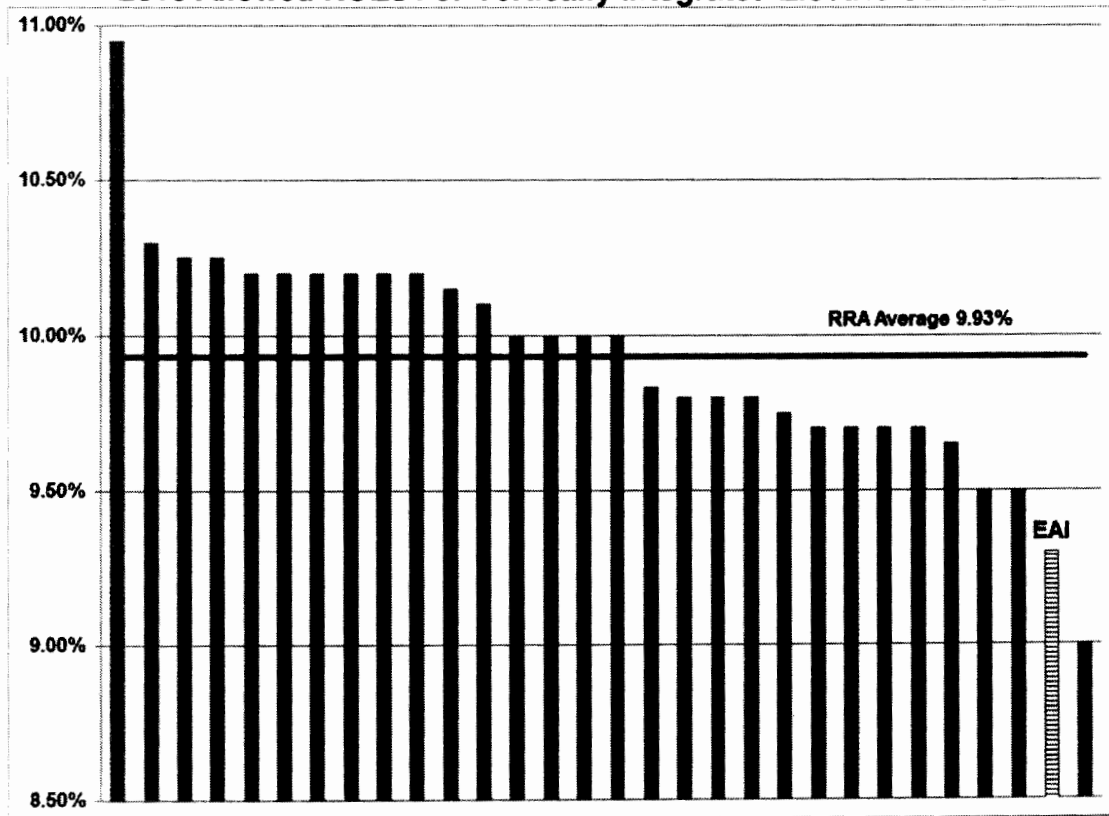
14 A. Of the 48 total ROE observations, 30 are for vertically integrated utilities.
15 The average allowed ROE drops slightly to 9.93 percent from 10.02
16 percent. Using the same format as Figure 1, the 30 results, new average,
17 and EAI's ROE set in the Order are presented in Figure 2.

18

⁶ *Id.* at 2.

1
2

Figure 2
2013 Allowed ROEs For Vertically Integrated Electric Utilities



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4

5 Q. OTHER THAN EAI'S ALLOWED ROE RESULT, ARE OTHER ENTERGY
 6 OPERATING COMPANY RESULTS INCLUDED IN THE RRA REPORT?

7 A. No other Entergy Operating Company allowed ROE is included in the
 8 RRA allowed ROE calculations or in Figures 1 or 2 above. EGSL and ELL
 9 are both listed on the RRA report as having December 2013 decisions, but
 10 no allowed ROE or other information is provided in the summary table of
 11 the report.⁷ Footnotes 20 and 21 of the RRA report explain that both
 12 companies received approval under settlements to operate under a

⁷ *Id.* at 6.

1 formula rate plan ("FRP") with a benchmark ROE of 9.95 percent in
2 December 2013.⁸

3

4 Q. DO THE MOODY'S AND EQUITY ANALYSTS' REPORTS REFERENCE
5 THE FRPS OR OTHER COST RECOVERY MECHANISMS IN PLACE AT
6 OTHER ENTERGY OPERATING COMPANIES?

7 A. Yes. The Moody's report discusses the FRPs in place for EGSL, ELL, and
8 EMI and notes that ETI operates in a regulatory jurisdiction where
9 transmission and distribution investment surcharges may be used.⁹ Credit
10 Suisse also noted an investment preference for utilities with "...supportive
11 regulation (ideally with formula rate plans)."¹⁰

12

13 Q. WHAT ARE THE ROES FOR THE ENTERGY OPERATING COMPANIES
14 NOTED IN THESE REPORTS?

15 A. The currently allowed ROEs for the Entergy Operating Companies
16 discussed above are summarized in Figure 3.

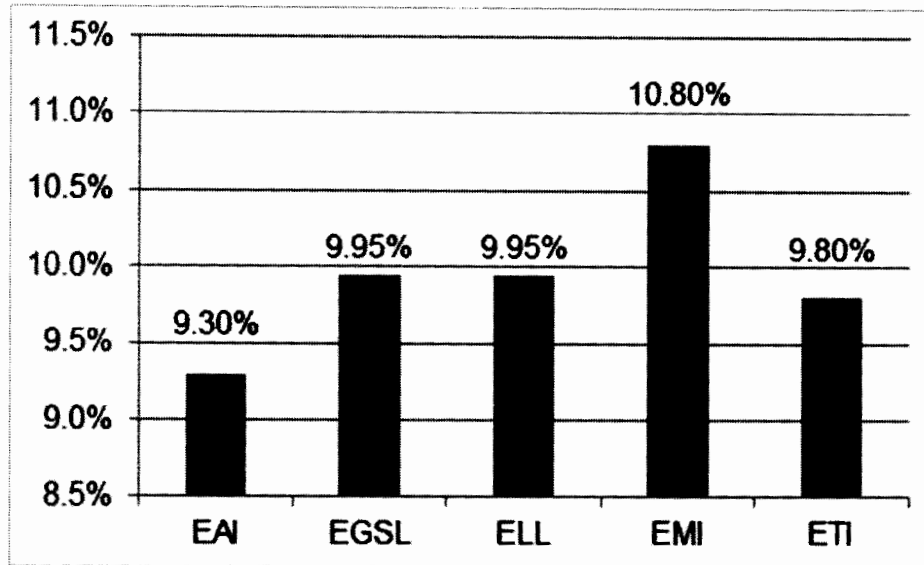
17

⁸ *Id.* at 9.

⁹ See EAI Exhibit DEH-8 at 1-2.

¹⁰ See EAI Exhibit DEH-4 at 1.

Figure 3
Currently Allowed ROEs For Entergy Operating Companies¹¹



Q. IN EAI'S REHEARING PETITION, THE 9.3 PERCENT ALLOWED ROE IS IDENTIFIED AS THE "LOWEST NON-PENALTY ROE AWARDED TO A VERTICALLY-INTEGRATED ELECTRIC UTILITY IN 2013."¹² PLEASE EXPLAIN THIS STATEMENT.

A. As reflected in Figure 2 above, there is one ROE result that was lower than EAI's 9.3 percent in 2013. This ROE result was based on a May 2013 decision involving Maui Electric Company, Limited ("MECO") before the Public Utilities Commission of the State of Hawaii ("Hawaii PUC"). In

¹¹ ETI's allowed ROE was granted in Public Utility Commission of Texas Docket No. D-39896, Order at 6 (September 14, 2012). ETI has appealed the ROE decision from that order. EMI's ROE noted by Credit Suisse was 10.59 percent, which reflects a rate adjustment limit in EMI's FRP. The 10.80 percent ROE is the allowed ROE used in EMI's FRP filing. For EMI's result, see Entergy's 4th Quarter 2013 Earnings Teleconference presentation at 20 (February 11, 2014). The presentation is available at <http://investor.shareholder.com/entergy/events.cfm>.

¹² EAI Petition for Rehearing and Clarification at 10 (January 29, 2014).

1 that proceeding, the Hawaii PUC modified a settlement agreement
2 between MECO and other parties that used a negotiated ROE of 10
3 percent. In modifying the settlement agreement, the Hawaii PUC
4 concluded, "Thus, a 9.50% ROE would have been acceptable but for
5 MECO's inability to address certain apparent system inefficiencies, which
6 are discussed in the section below."¹³ The Hawaii PUC further explained:

7 The commission finds it appropriate to adjust the Parties'
8 stipulated ROE another 50 basis points downward in light of
9 apparent system inefficiencies which negatively impact
10 MECO's customers. For example, MECO appears unable to
11 properly address known renewable energy curtailment
12 issues....MECO appears to have failed to adequately and
13 sufficiently plan for and implement the necessary
14 modifications to its existing operations to accept a more
15 appropriate level of the wind energy generation made
16 available to MECO, negatively impacting ratepayers through
17 higher electricity rates. Additionally, among other matters,
18 MECO appears unable to control operational costs such as
19 pension costs which are discussed above.¹⁴

20 Absent the 50 basis point (0.5 percent) penalty assessed by the
21 Hawaii PUC, MECO's allowed ROE would have been 9.5 percent leaving
22 EAI's 9.3 percent allowed ROE as the lowest allowed ROE for a vertically
23 integrated electric utility in 2013.

¹³ Hawaii PUC, Docket No. 2011-0092, Decision and Order No. 31288 at 107 (May 31, 2013).

¹⁴ *Id.* at 107-110.

1 Q. EAI'S REHEARING PETITION ALSO STATED THAT THE 9.3 PERCENT
2 ROE "IS THE SECOND LOWEST NON-PENALTY ROE GRANTED TO A
3 VERTICALLY INTEGRATED ELECTRIC UTILITY IN RECENT
4 DECADES."¹⁵ WHAT IS THE BASIS FOR THIS STATEMENT?

5 A. Along with issuing annual rate case reports discussed previously, RRA
6 maintains a database of regulatory decisions that extends back to 1980.
7 This database contains the summary information for approximately 1,700
8 electric utility rate cases, including over 1,400 where an allowed ROE is
9 identified. Of the 1,400 cases where an allowed ROE was identified, there
10 are only 13 decisions that have an ROE of 9.3 percent or lower. Of those
11 13 decisions, only three cases involve vertically integrated utilities, and all
12 three decisions were rendered in 2012 or 2013. The three utilities and
13 jurisdictions involved are MECO in Hawaii, EAI in Arkansas, and Northern
14 States Power ("NSP") in South Dakota.

15

16 Q. YOU HAVE ALREADY DISCUSSED THE MECO DECISION. PLEASE
17 PROVIDE SOME DETAILS OF THE NSP CASE IN SOUTH DAKOTA.

18 A. NSP received the lowest non-penalty, allowed ROE awarded to a
19 vertically integrated utility since 1980 as tracked by RRA. In June 2012,
20 the South Dakota Public Utilities Commission ("South Dakota PUC")
21 approved an NSP rate increase that included an allowed ROE of 9.25

¹⁵ EAI Petition for Rehearing and Clarification at 8-9 (January 29, 2014).

1 percent.¹⁶ In contrast to MECO, the order did not reference any specific
2 issues with NSP's operations that influenced the ROE decision.

3

4 Q. WHAT HAPPENED AFTER THE SOUTH DAKOTA PUC'S DECISION?

5 A. NSP filed a new rate case in South Dakota shortly after the 2012 decision.

6 Much like EAI, NSP planned to make significant capital expenditures and
7 needed a supportive ROE. In its filing, NSP explained its need for an
8 appropriate ROE in direct testimony:

9 Q. IS THE LEVEL OF ROE ESPECIALLY IMPORTANT
10 IN LIGHT OF THE COMPANY'S PLAN FOR
11 FUTURE INVESTMENTS?

12 A. Yes. An appropriate ROE and a supportive state
13 regulatory framework are key contributors to our
14 ability to raise significant capital at reasonable rates.
15 Our plan of investment in generation, transmission
16 and distribution will result in approximately \$5.9 billion
17 of expenditures between 2012 and 2016. We will
18 need to turn to the capital markets to support the level
19 of investment that is needed.

20 Given this magnitude of investment, we have a
21 common interest with our regulators and customers in
22 having the Commission set an appropriate ROE and
23 allowing us a reasonable opportunity to earn that
24 ROE. Absent these conditions, the cost of capital for
25 the investments we need to make to serve our
26 customers would be higher than otherwise necessary,
27 increasing the rate impact on our customers.¹⁷

28

¹⁶ South Dakota PUC, Docket No. EL11-019, South Dakota PUC Transcript of Proceedings at 10 – 11 (June 19, 2012); Final Decision and Order; Notice of Entry at 2 (July 2, 2012).

¹⁷ South Dakota PUC Docket No. EL12-046, Direct Testimony of Laura McCarten at 15 (June 29, 2012).

1 Q. WHAT WAS THE RESULT OF NSP'S SUBSEQUENT RATE CASE?

2 A. On April, 18, 2013, the South Dakota PUC approved a settlement between
3 NSP and the South Dakota PUC Staff for a rate increase that did not have
4 a specified allowed ROE.¹⁸ There was an agreed upon rate of return on
5 rate base of 7.78 percent but other elements – debt ratio, equity ratio, debt
6 rate, return on equity – were not specified. Based on this result, customer
7 rates reflecting the 9.25 percent ROE decision have been superseded and
8 are no longer in effect.

9

10 Q. DOES THIS CONCLUDE YOUR REHEARING DIRECT TESTIMONY?

11 A. Yes.

¹⁸ See EAI Exhibit DEH-9 at 5.

CERTIFICATE OF SERVICE

I, Steven K. Strickland, do hereby certify that a copy of the foregoing has been served upon all parties of record by forwarding the same by electronic mail and/or first class mail, postage prepaid, this 14th day of March, 2014.

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EAI EXHIBIT DEH-4

CREDIT SUISSE

UTILITY ROE TRENDS IN 2013

JANUARY 2, 2014

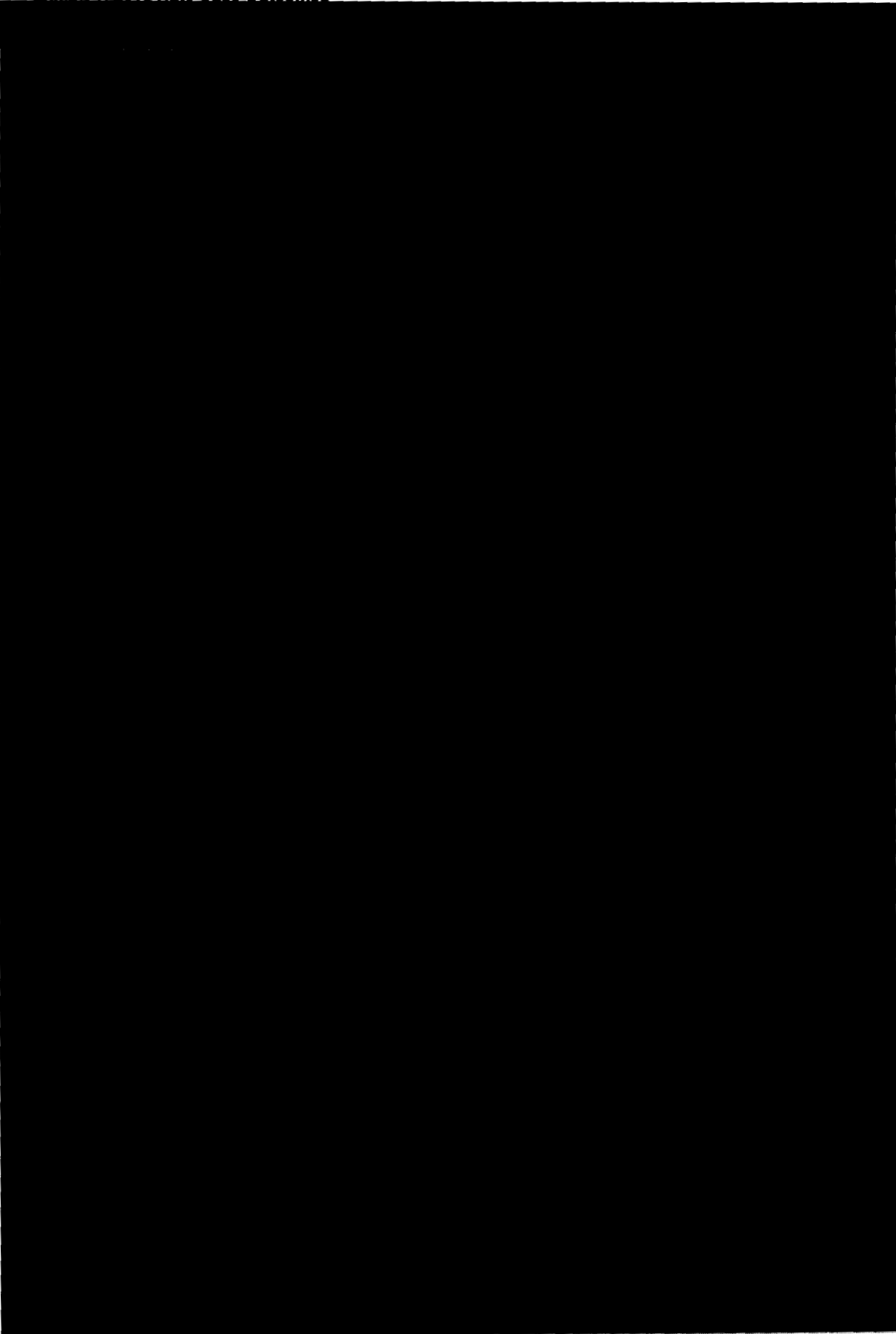
THIS EXHIBIT CONTAINS CONFIDENTIAL PROTECTED INFORMATION
PROVIDED PURSUANT TO THE COMMISSION'S INTERIM PROTECTIVE
ORDER NO. 2 ISSUED ON FEBRUARY 21, 2013 IN THIS DOCKET.

COMMENT

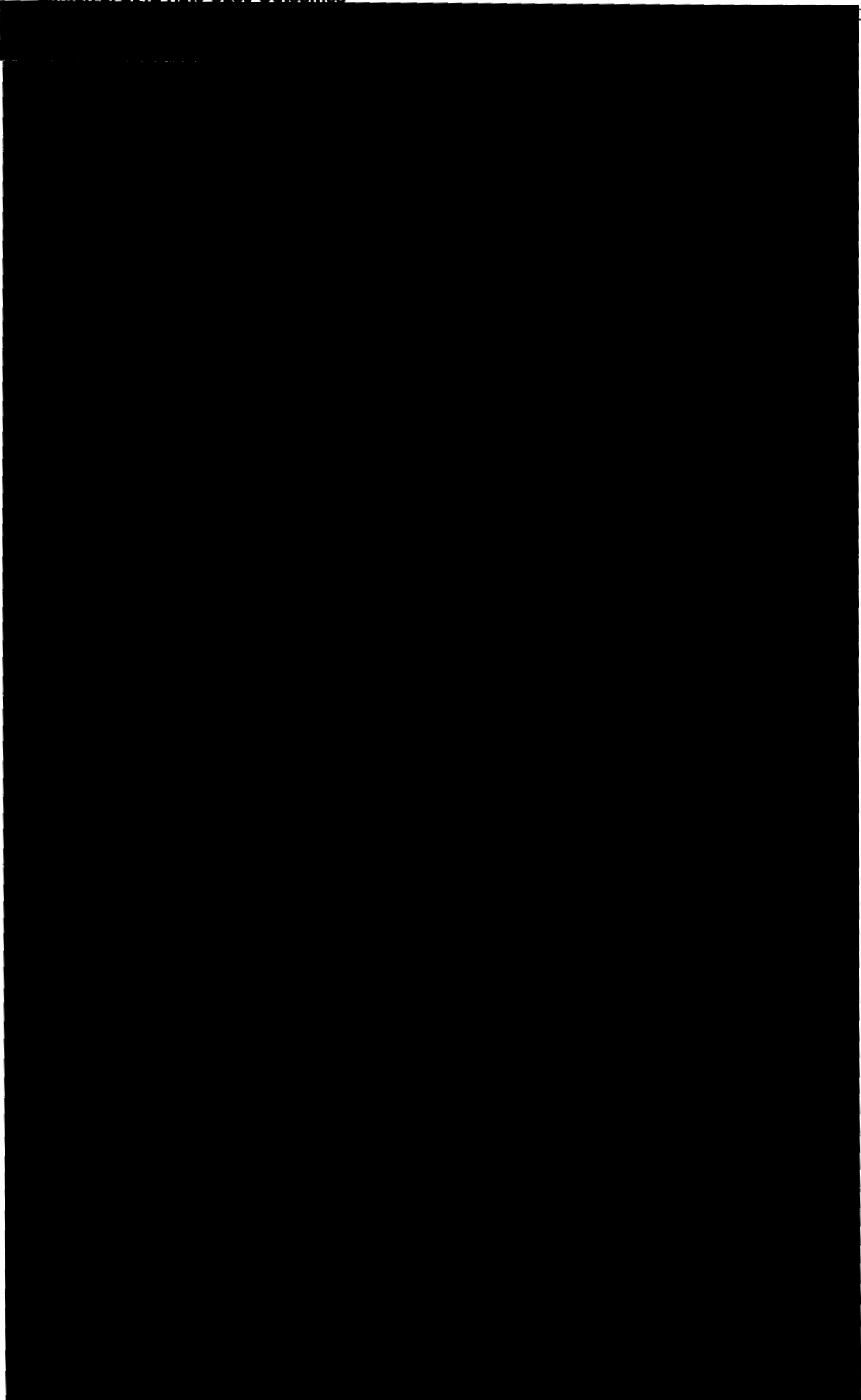
ETR and ED End Year On Soft Notes

_____ We think the low allowed ROE in Arkansas (where there is more risk than in NY at the same ROE) will sustain questions about the supportiveness of ETR's states and the ability for ETR to execute on the utility growth strategy.

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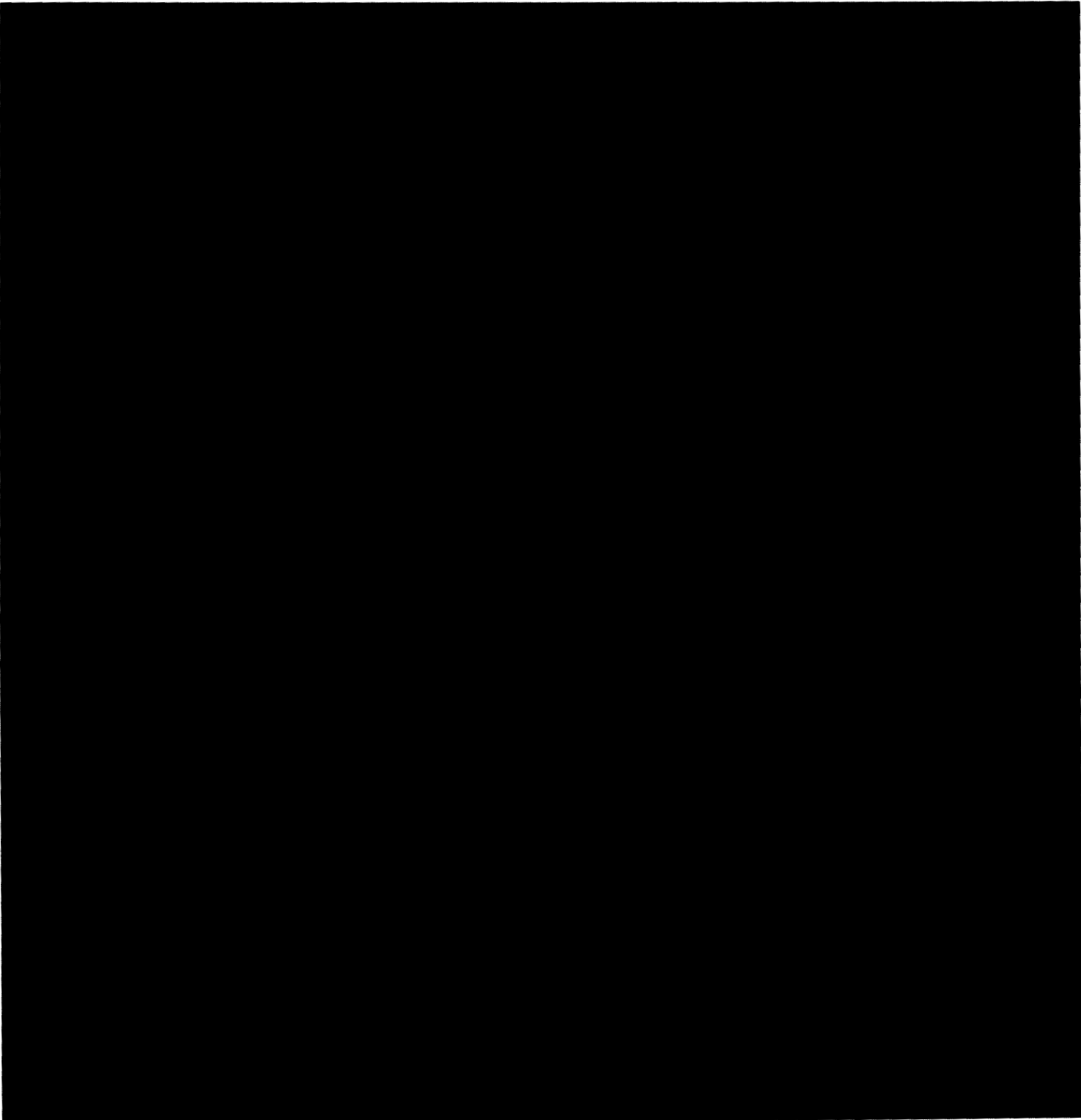


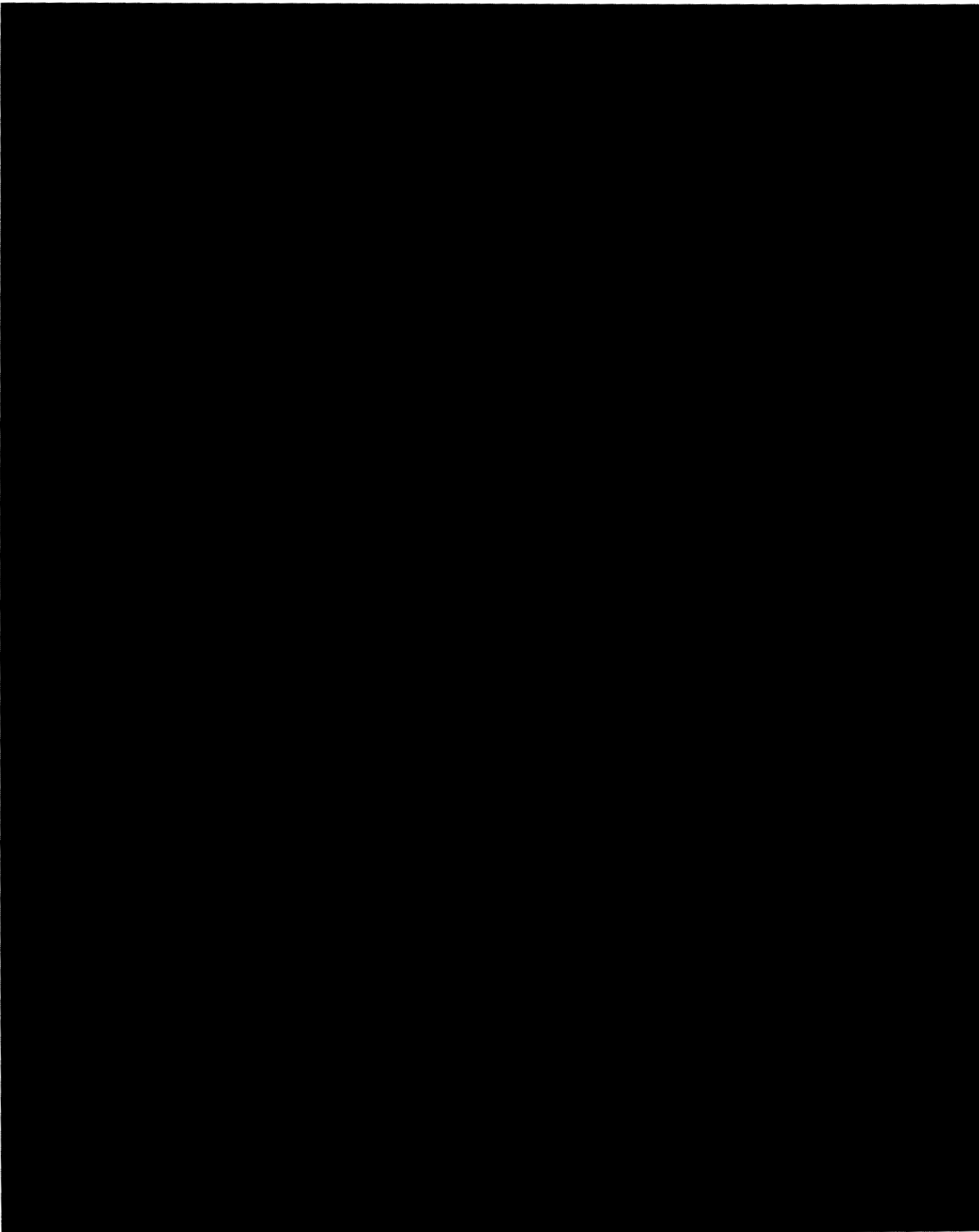
Source: Company data, Credit Suisse estimates





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US IPP WEEKLY POWER POINTS

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[REDACTED]

Entergy's awarded 9.3% ROE by AR PSC

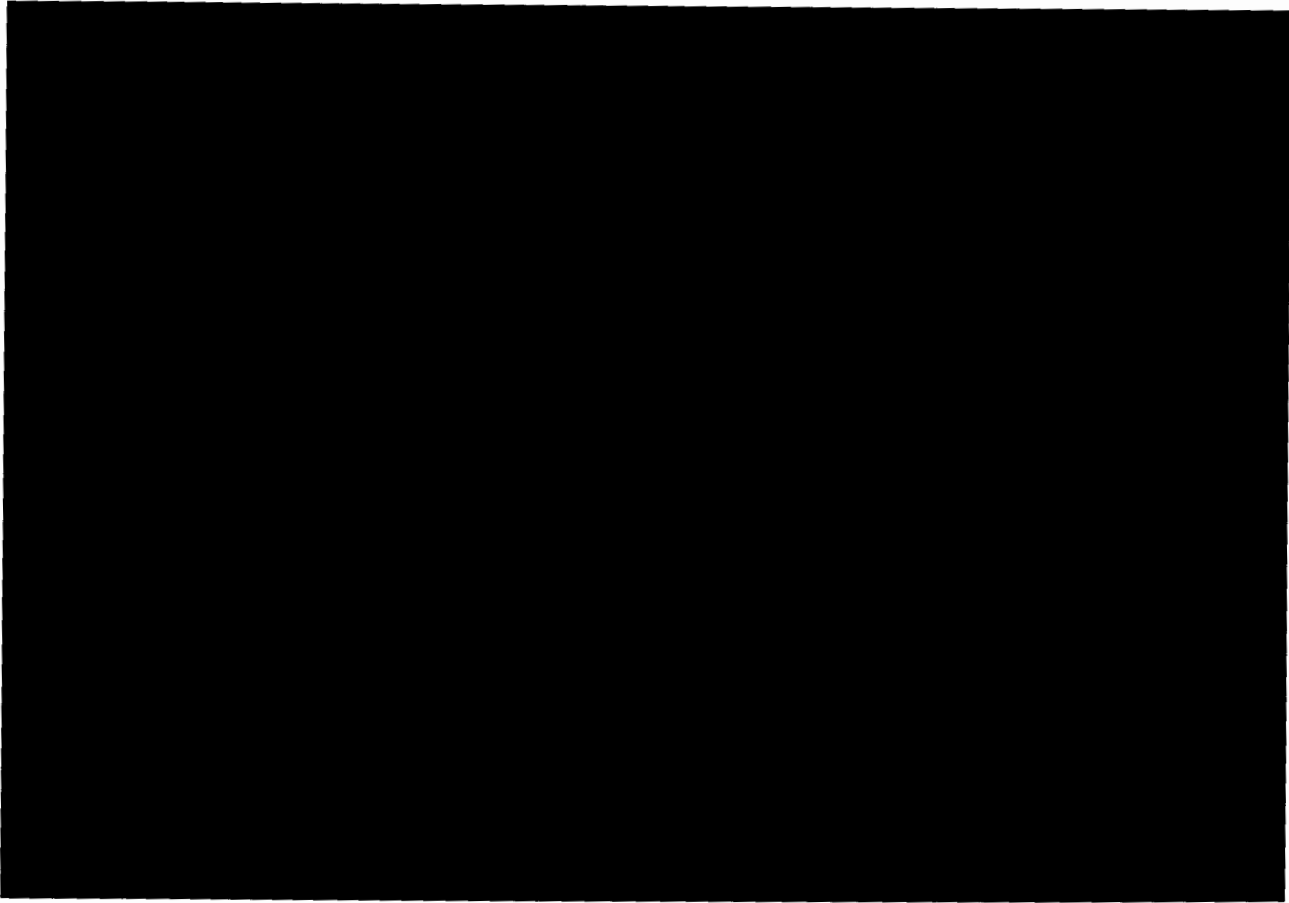
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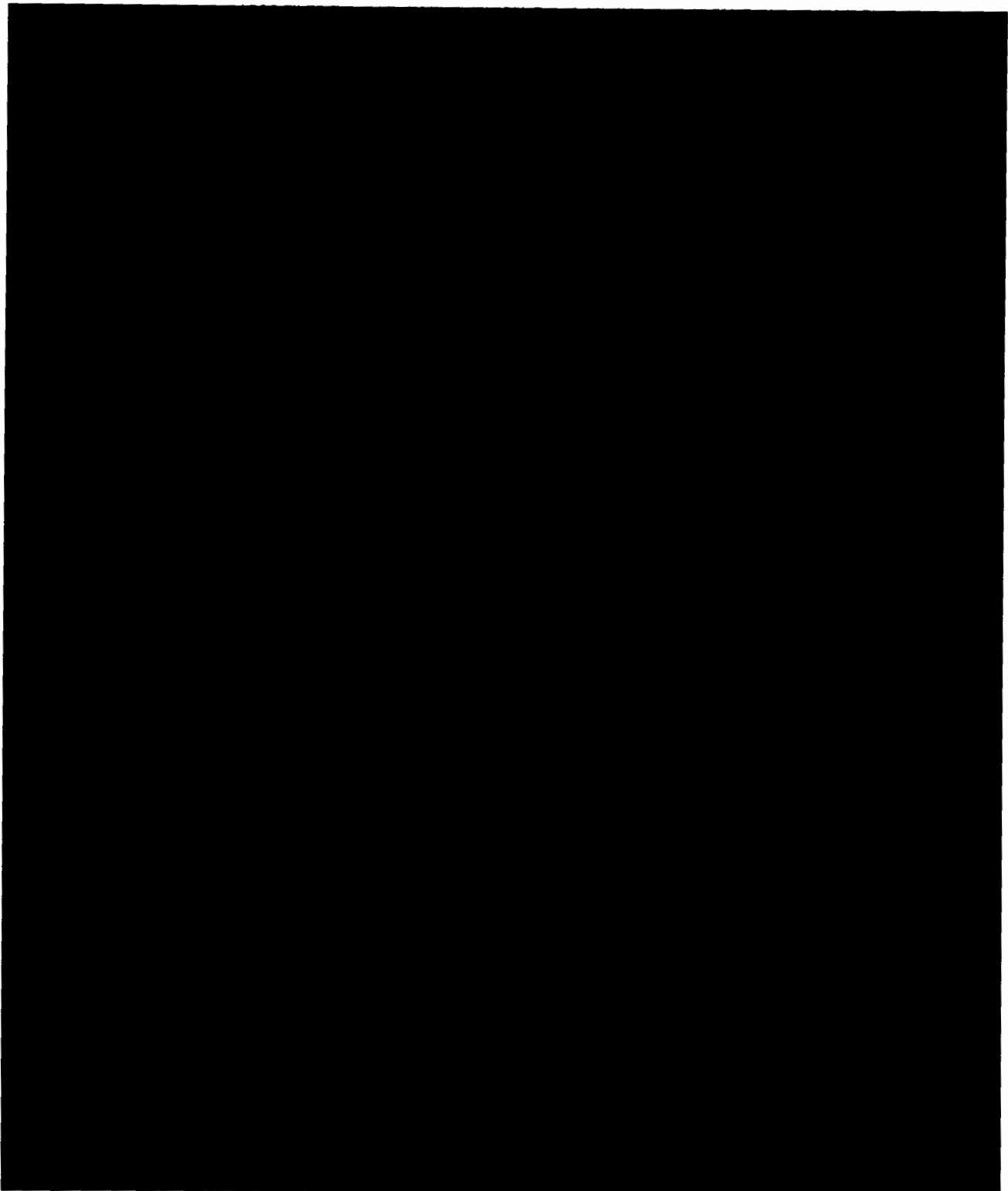
We read the decision negatively vs. our expectations. Vs. the 9.8% normalized ROE posted in 2012, we see the potential for a revenue reduction, or more importantly a relatively flat net income profile. [REDACTED]

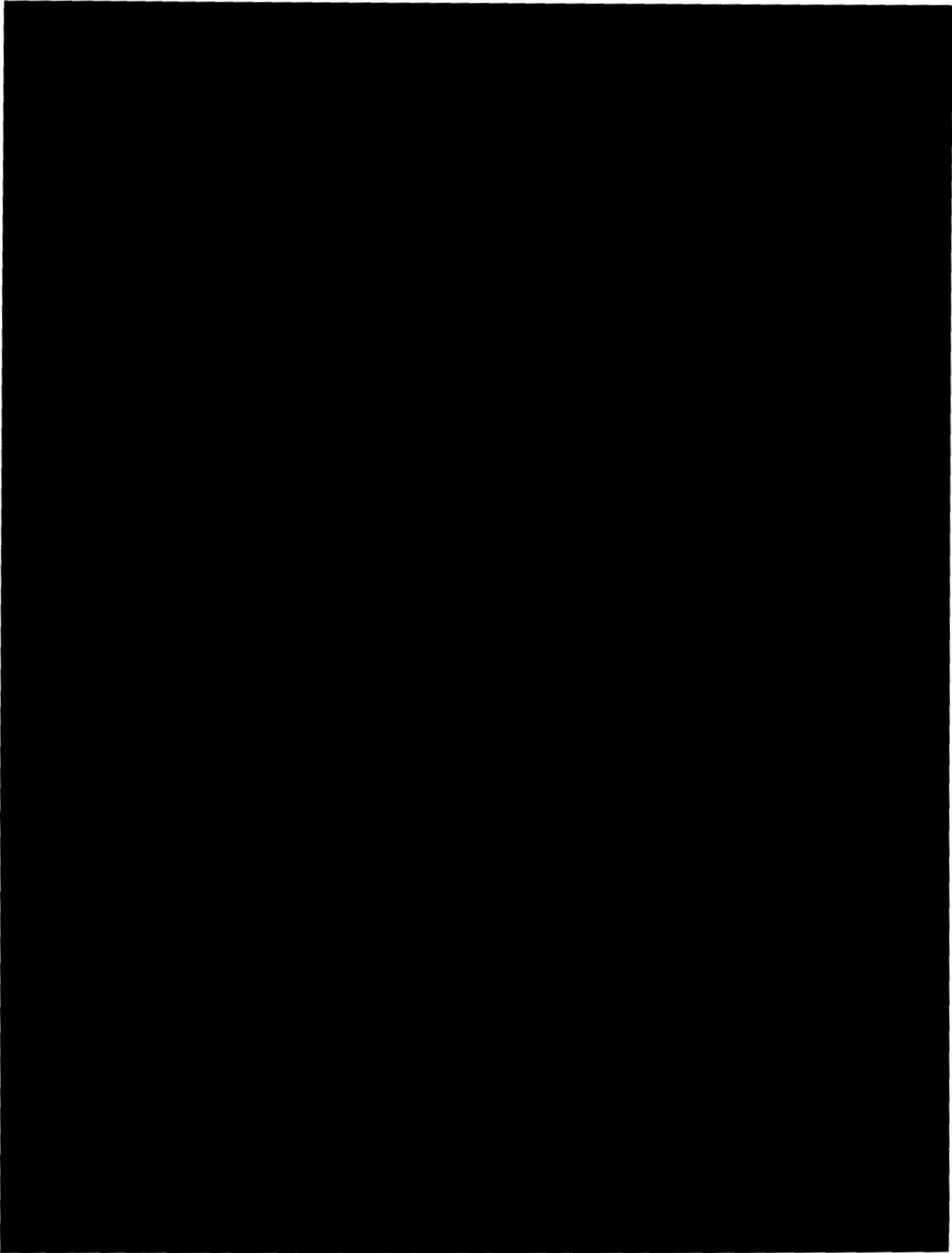
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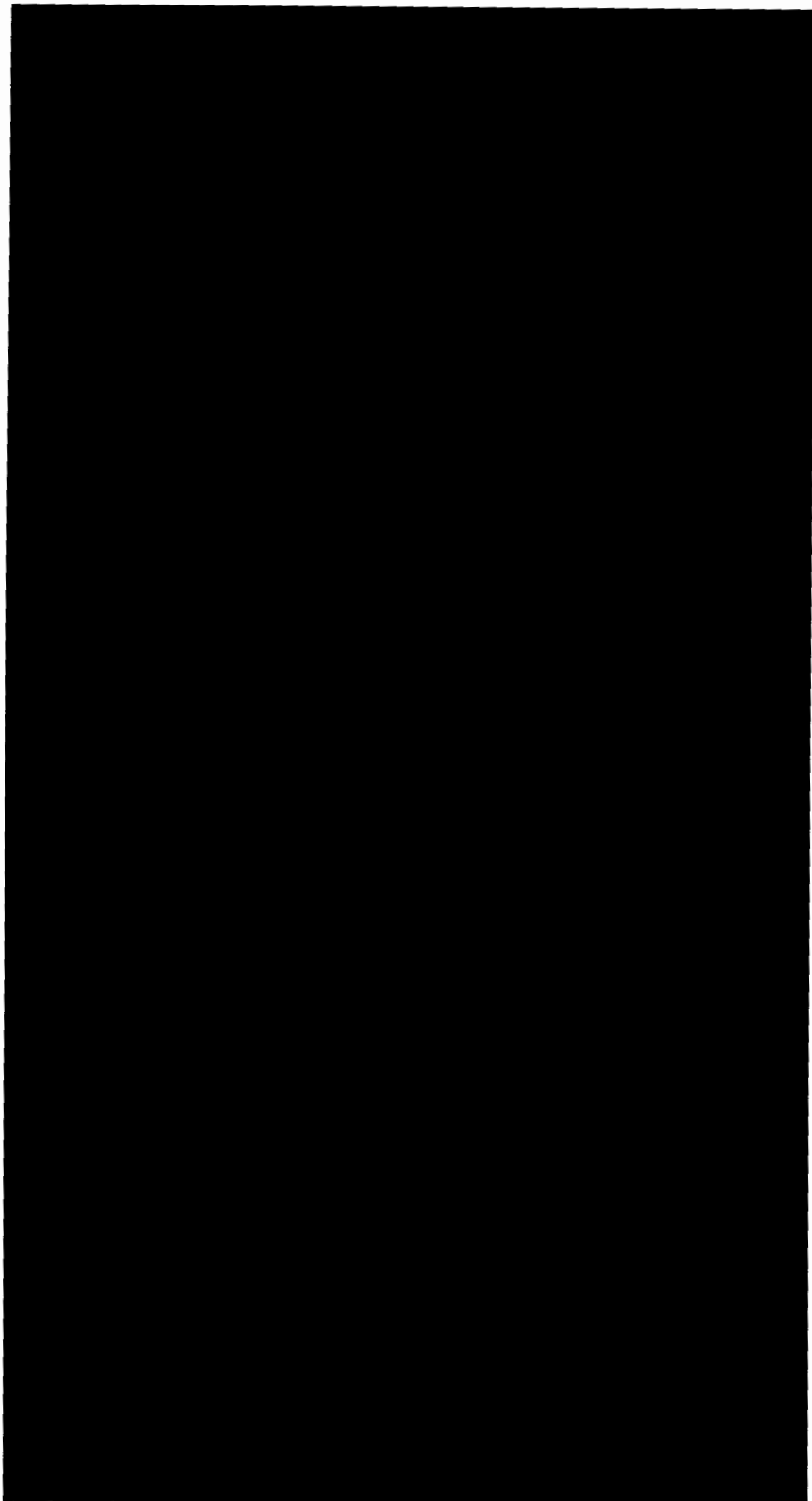
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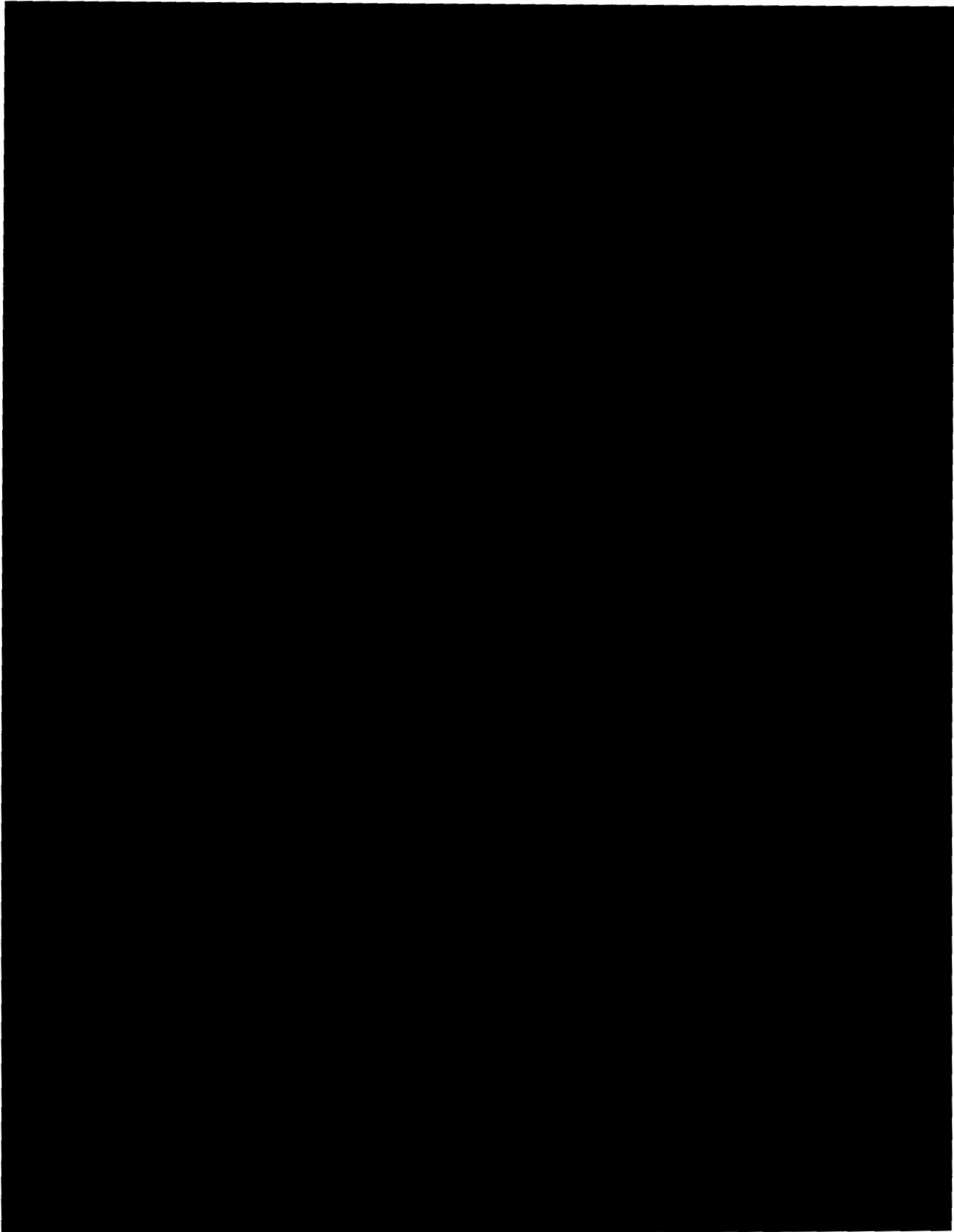


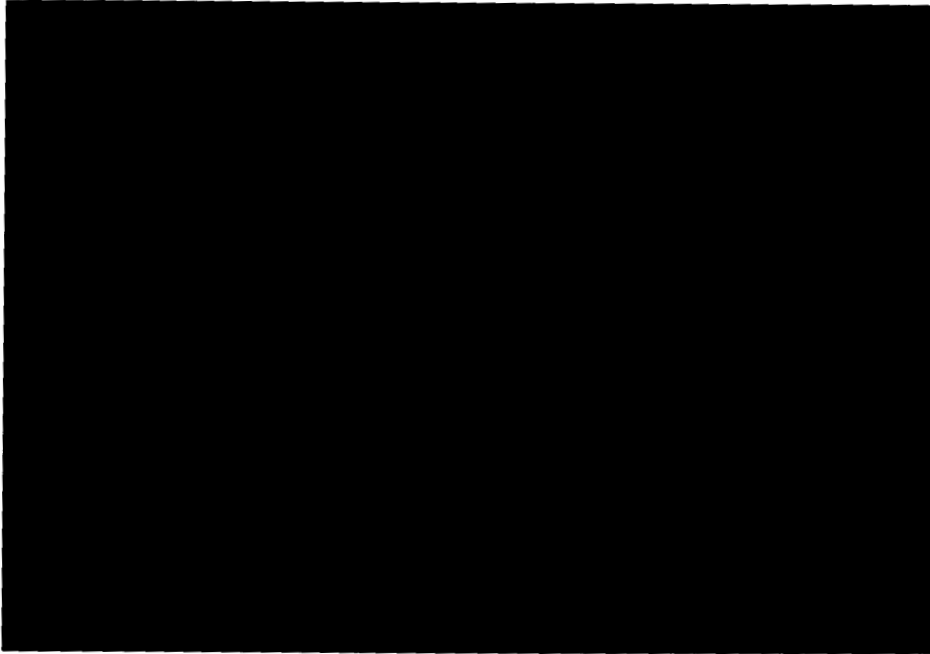


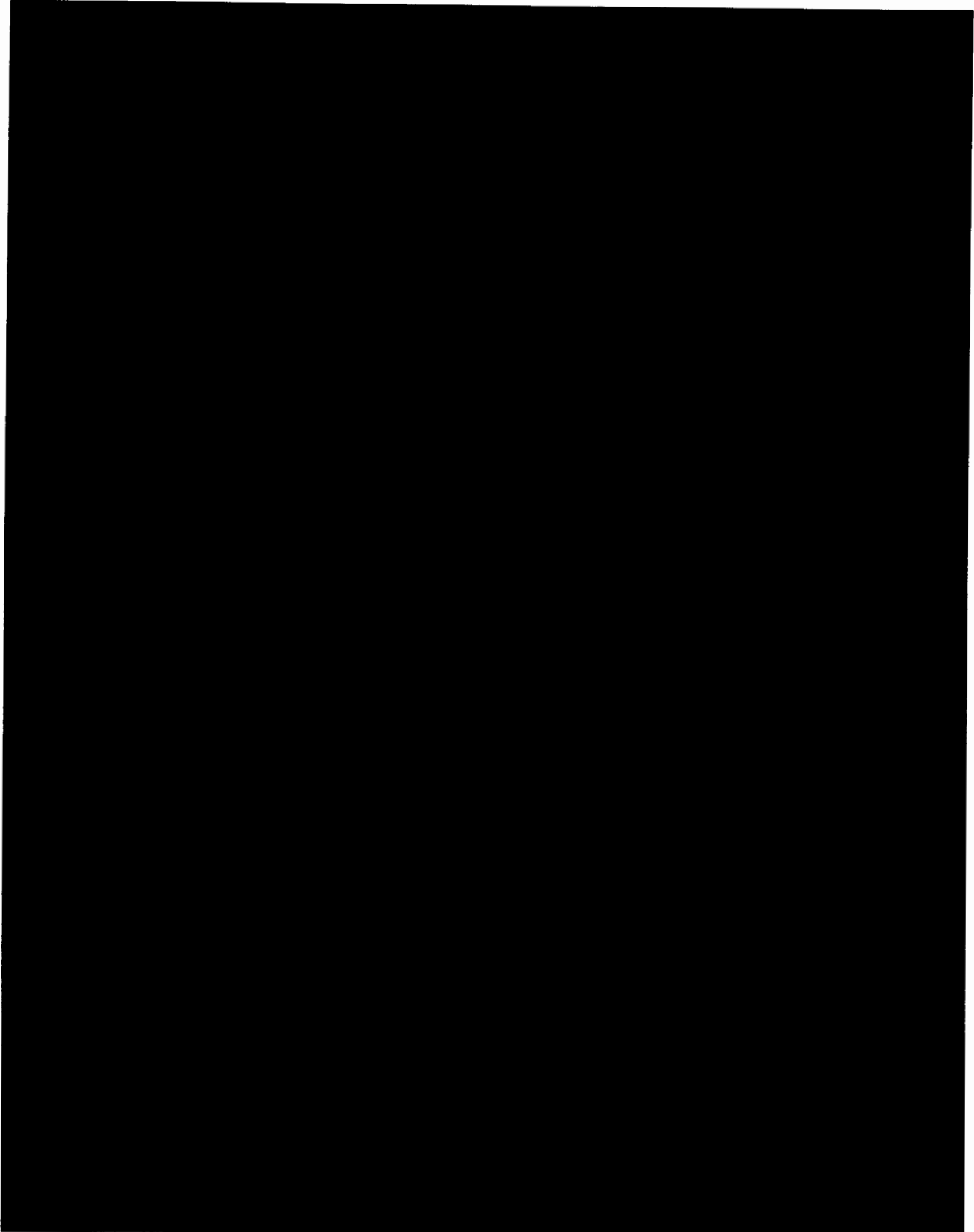


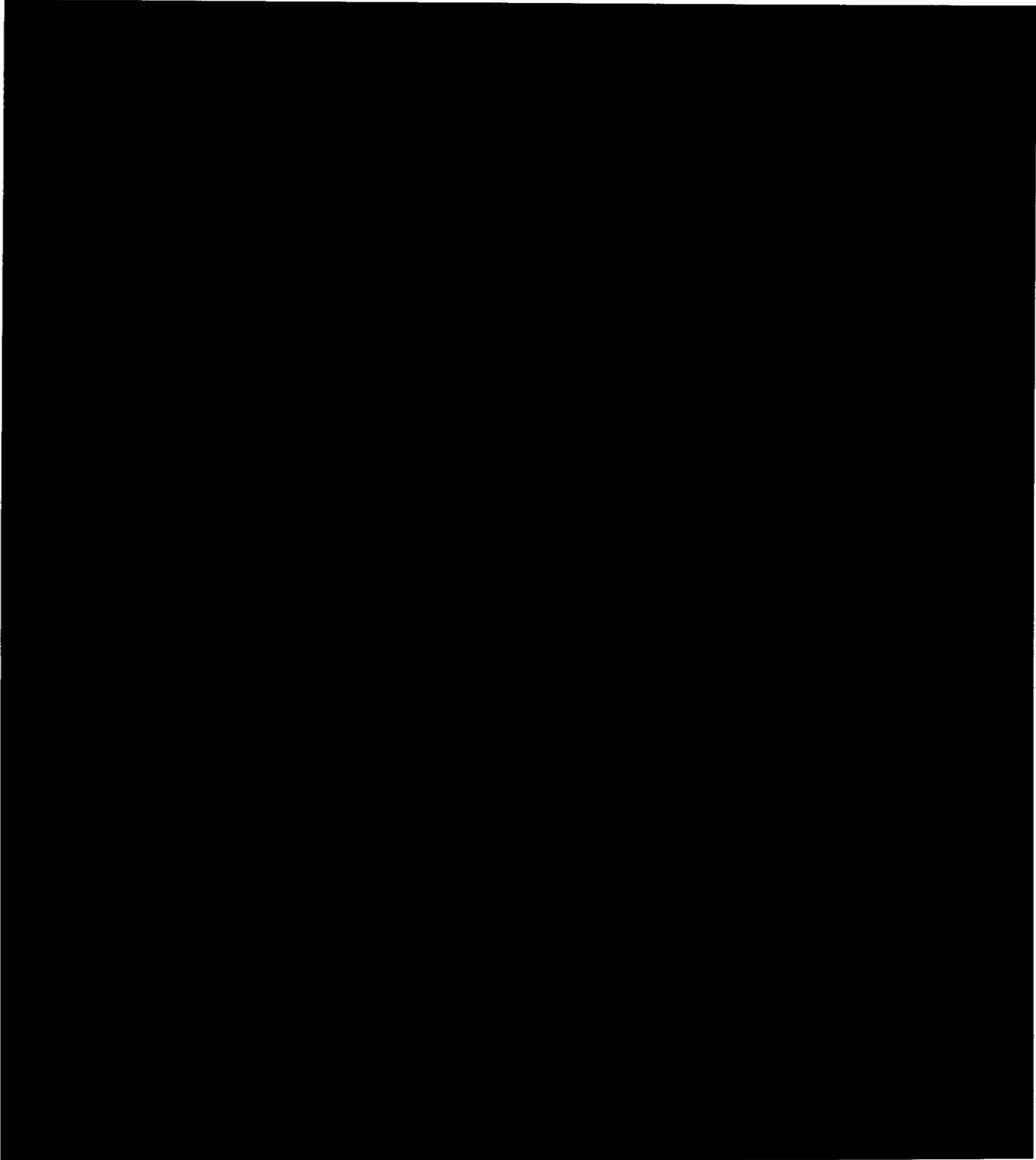












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Date

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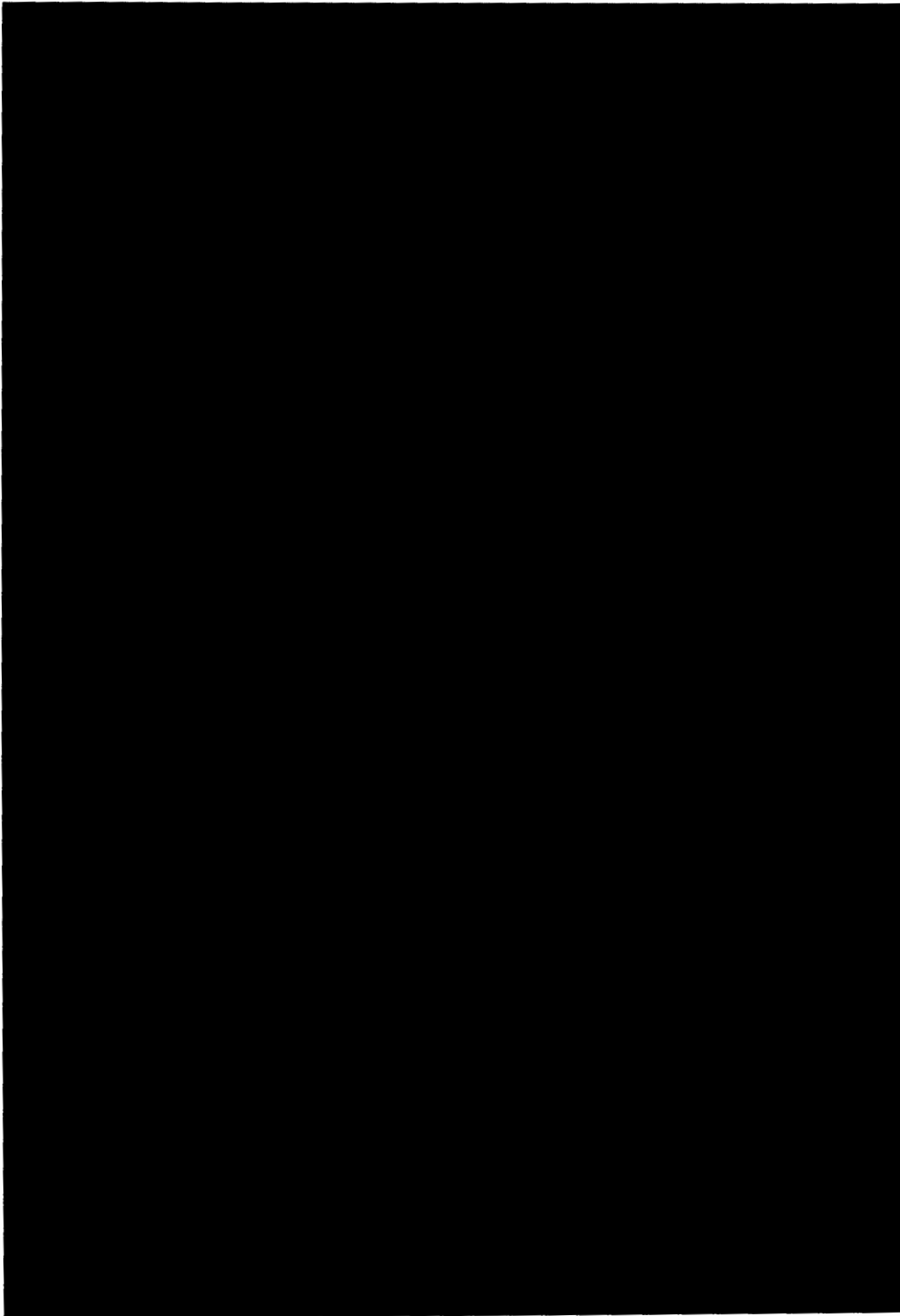


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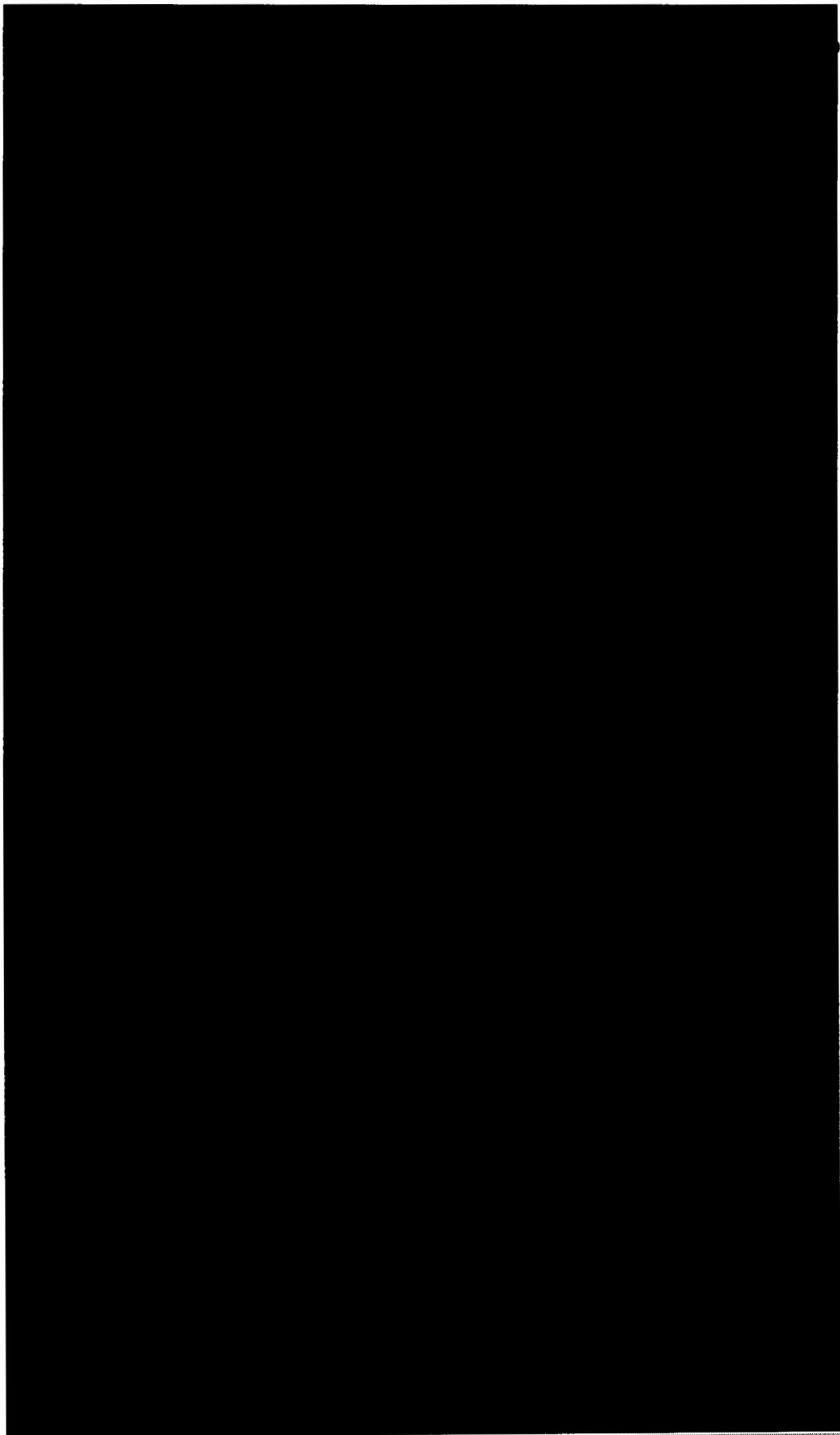


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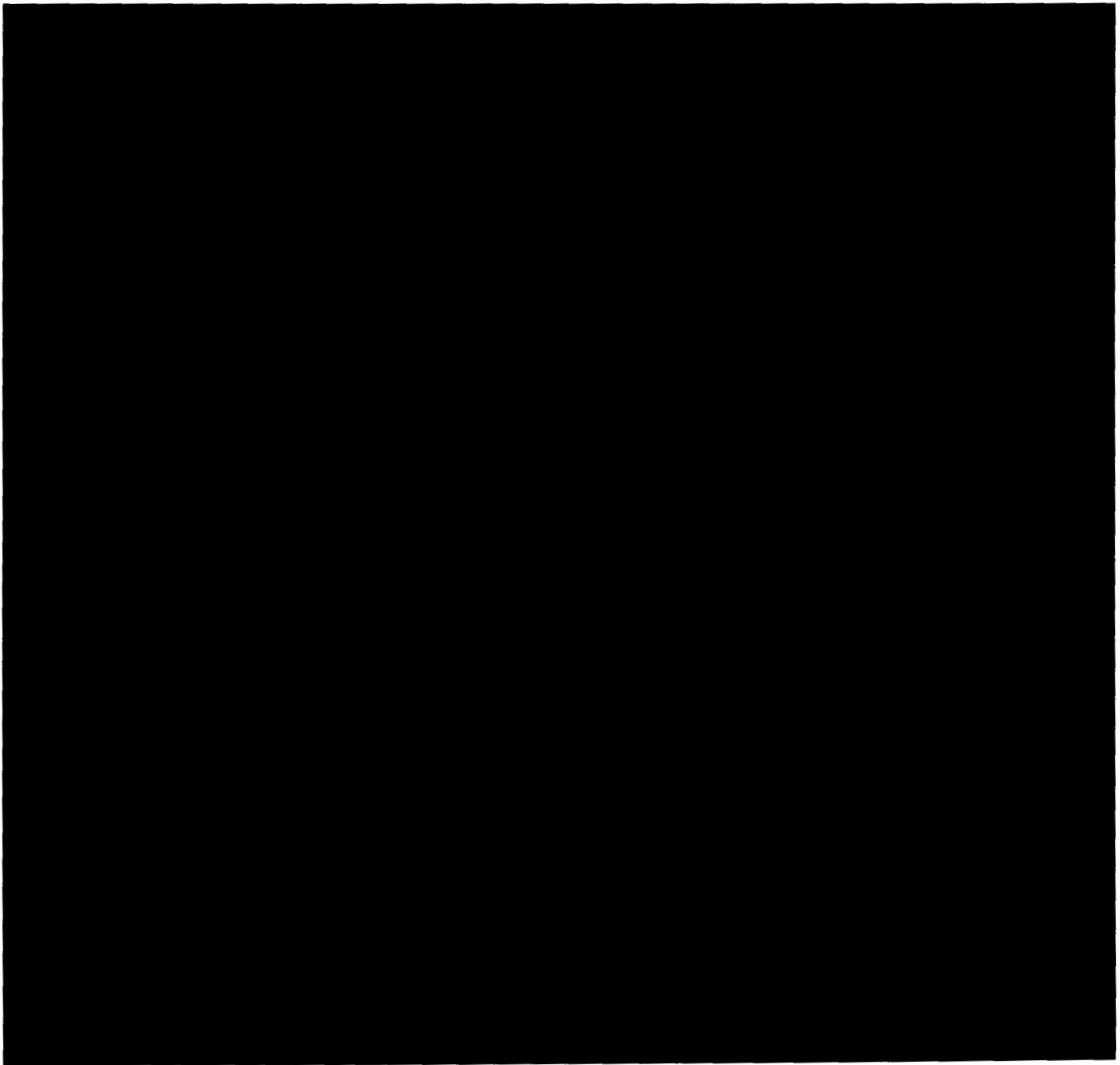


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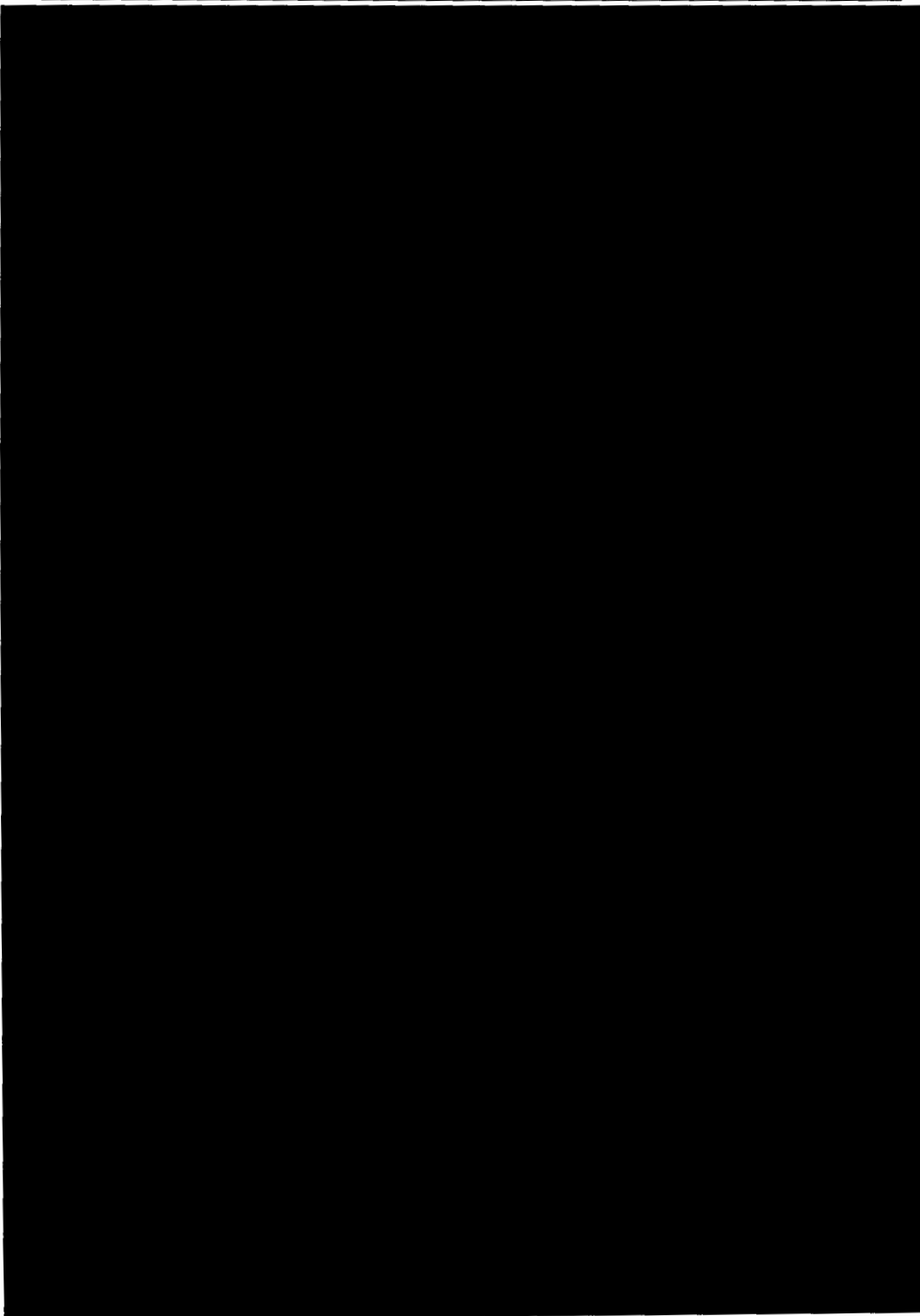
Utility events – next week

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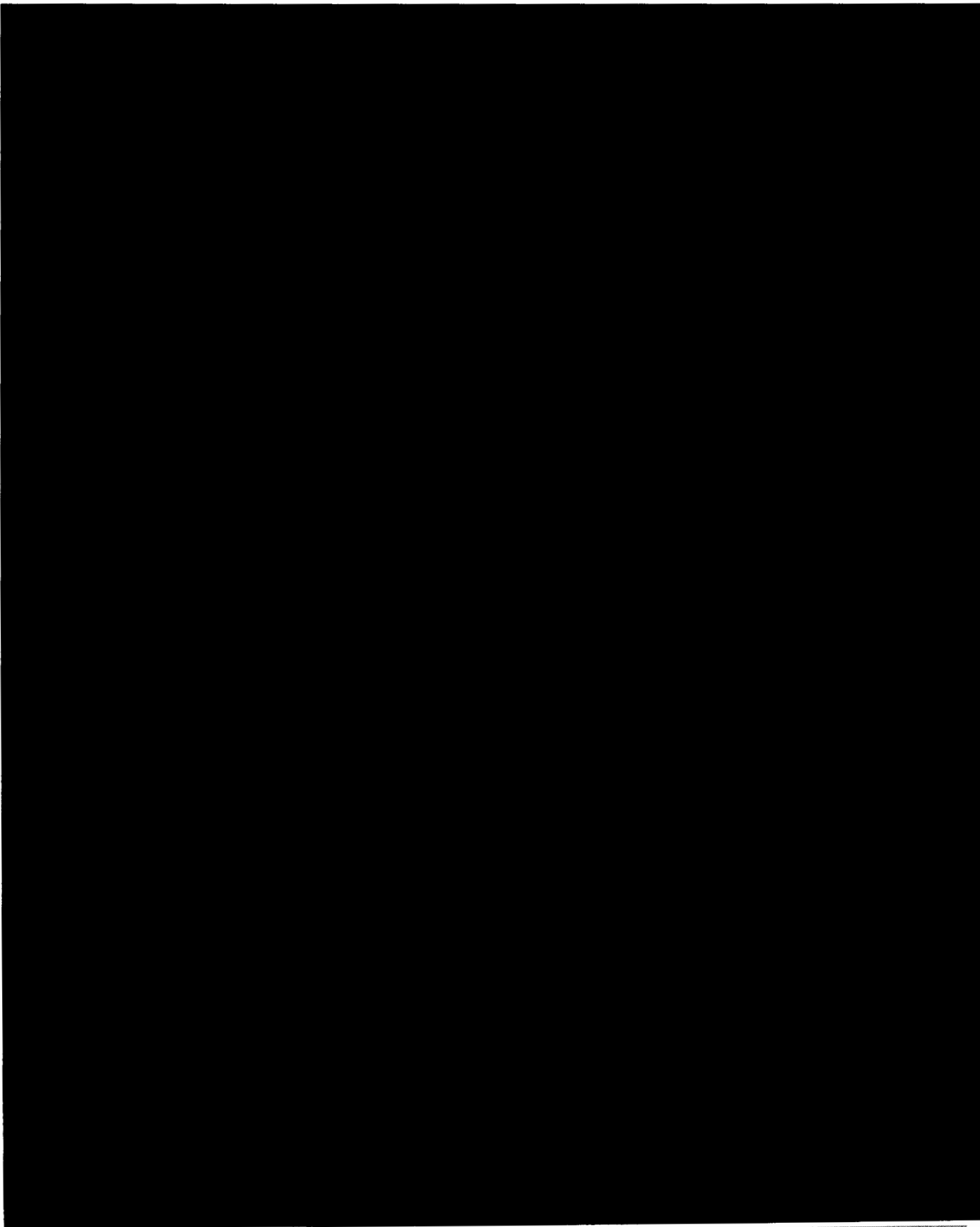


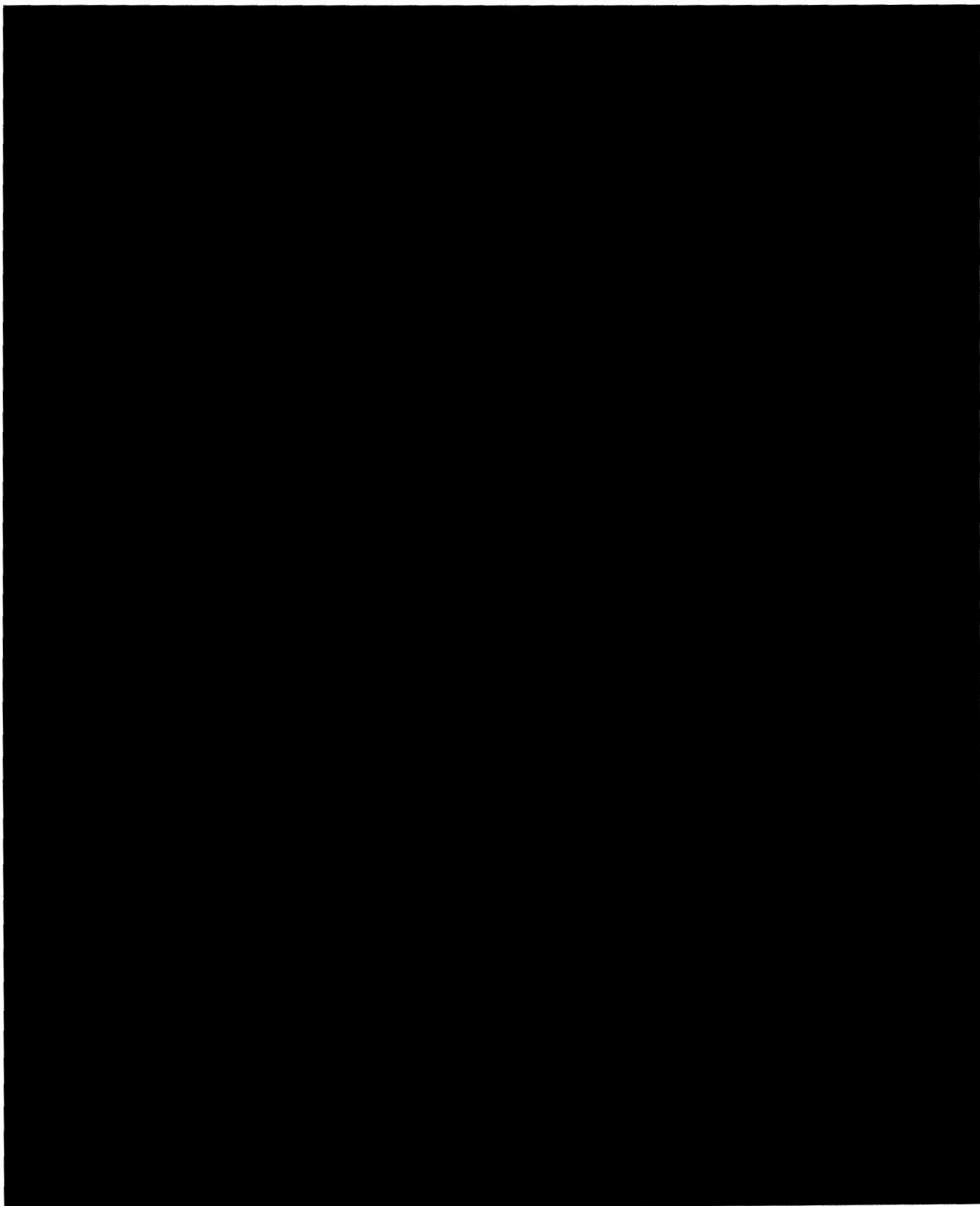
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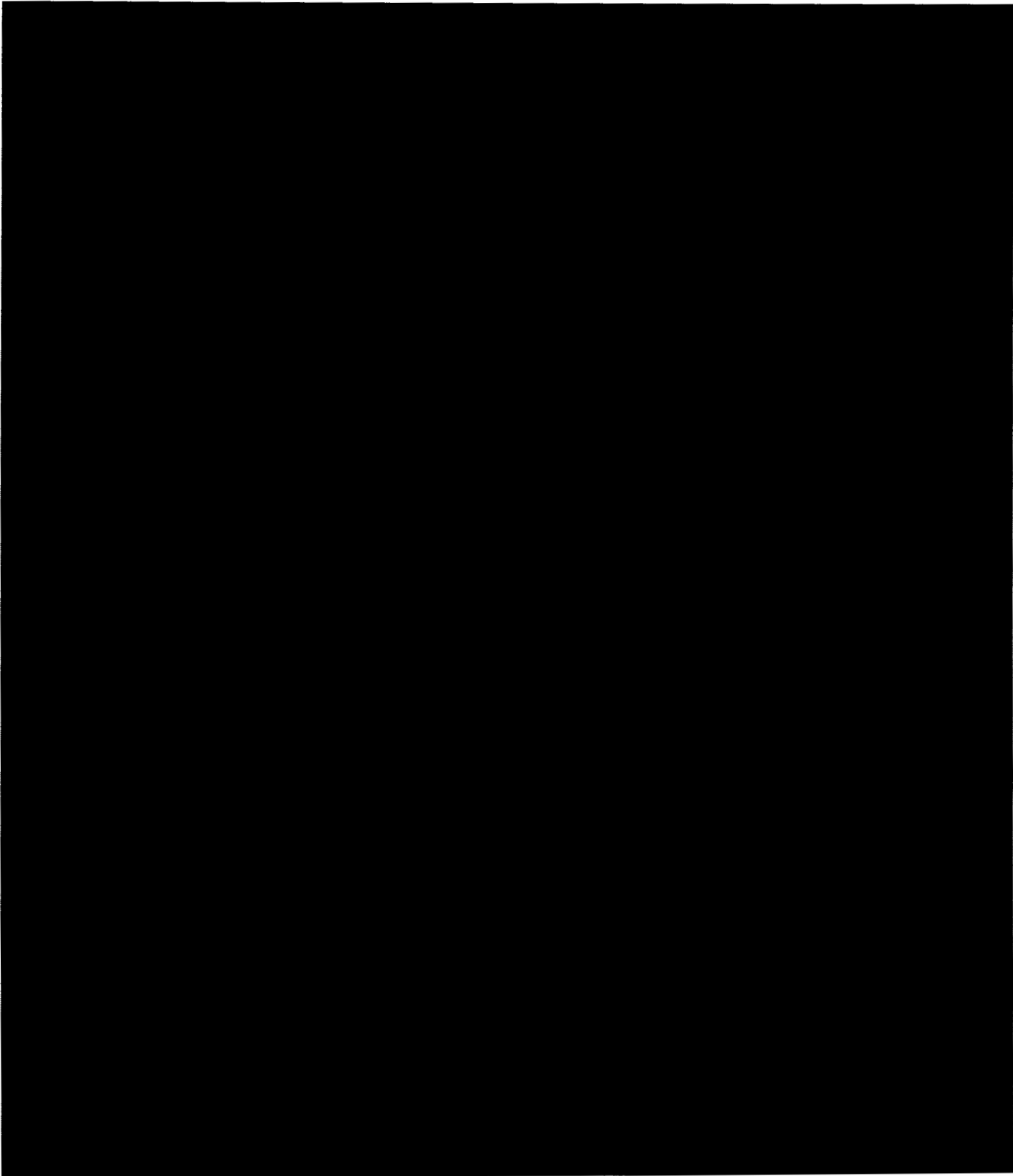
_____ We viewed the order negatively for ETR, particularly since the commission has recommended additional cost disallowances versus Staff's recommendation and a lower ROE. In the order, the PSC has directed Staff to file an updated revenue deficiency as compared to Staff's most recent \$110M recommendation based on an ROE of 9.3% vs. the 9.6% ROE recommended by Staff and cost disallowances totaling about \$15M related to incentive compensation.

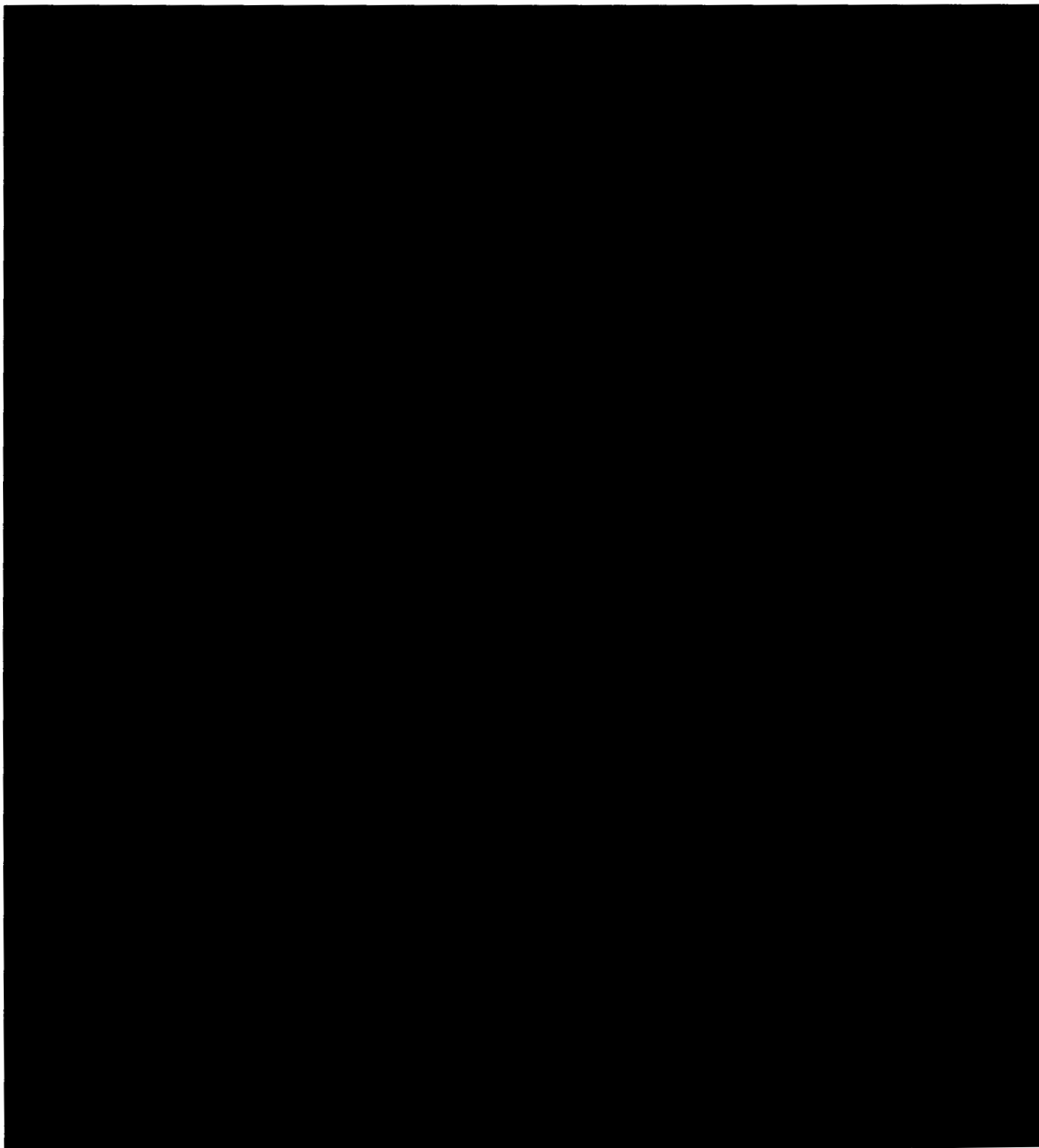


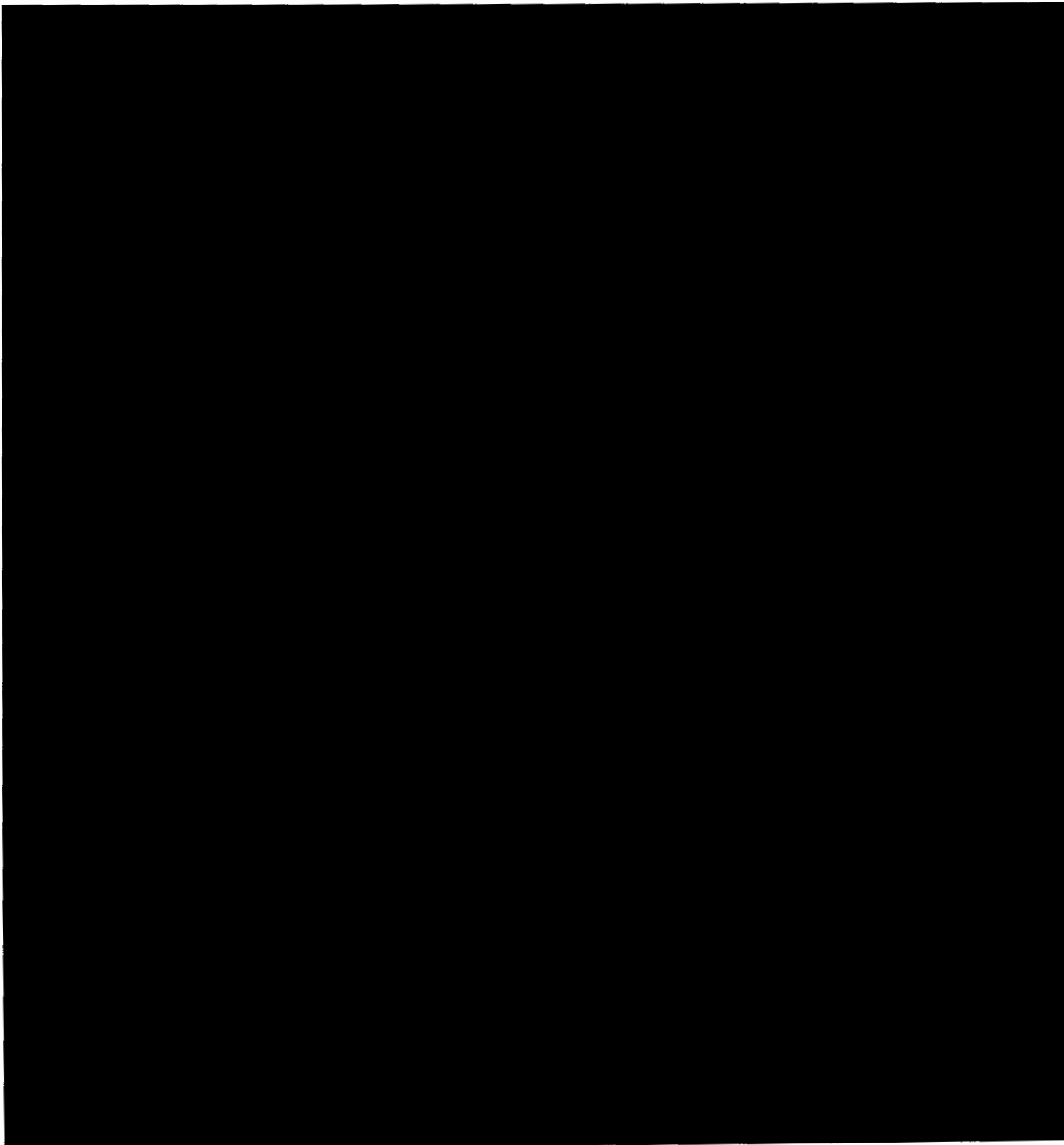
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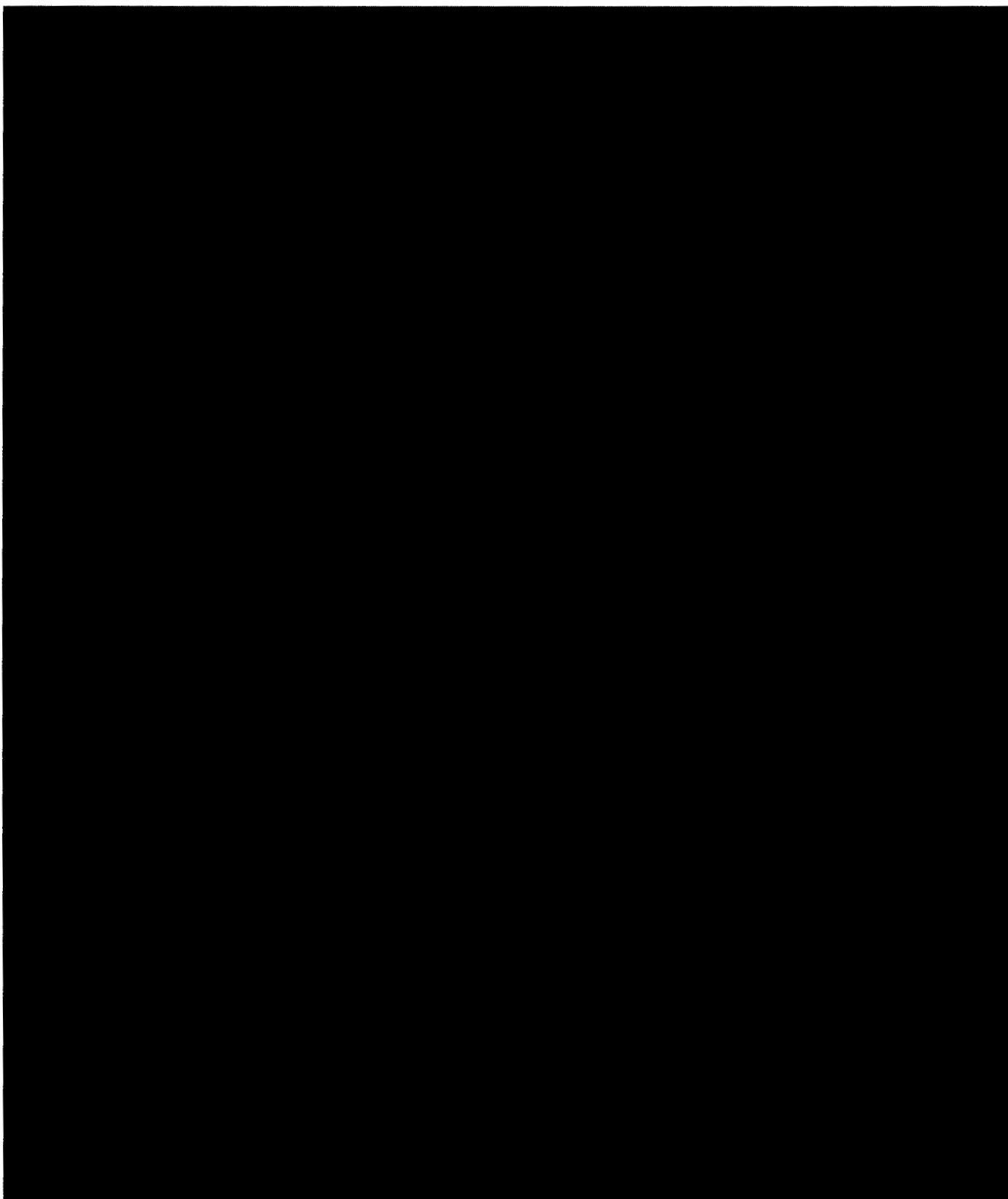


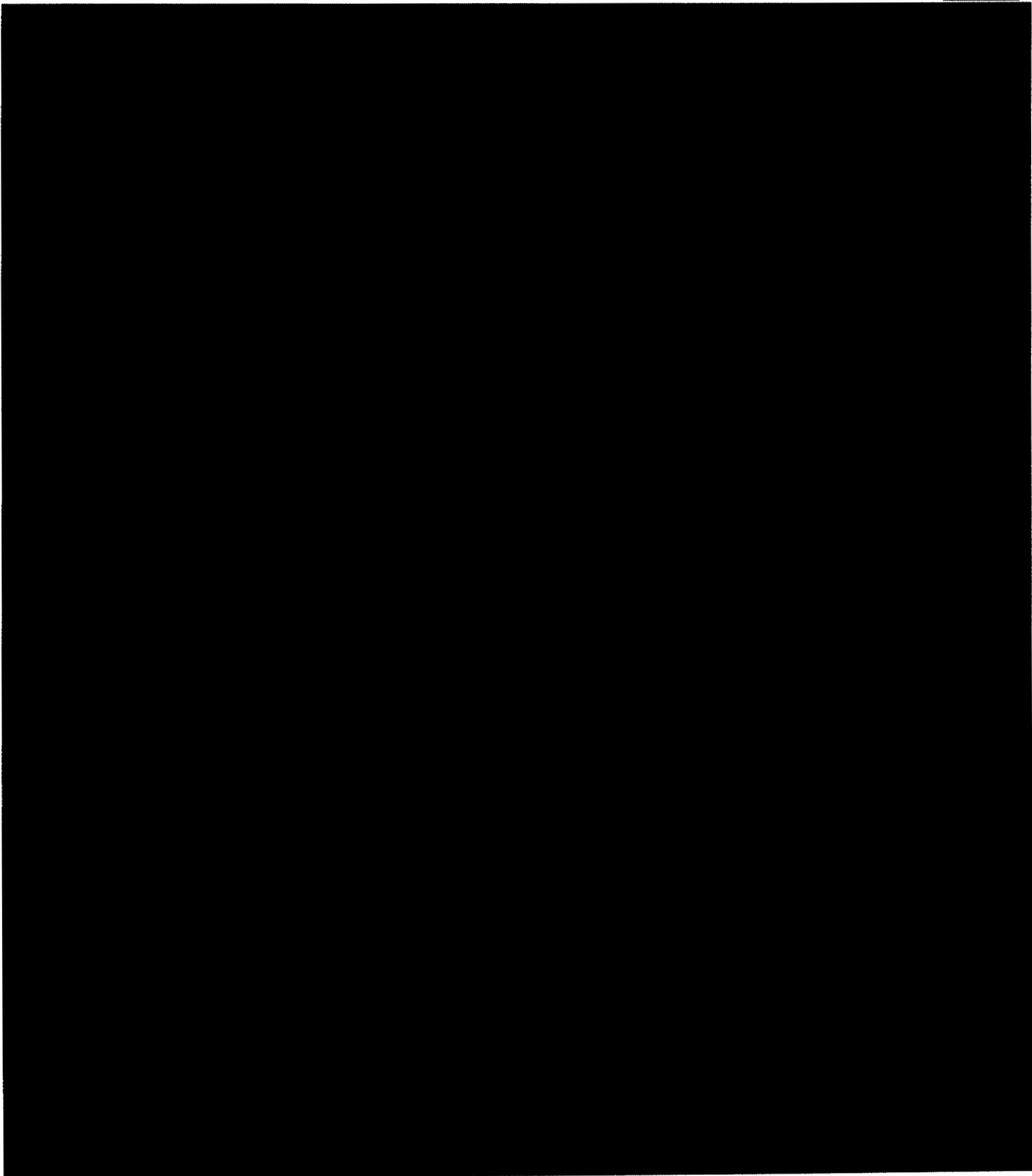






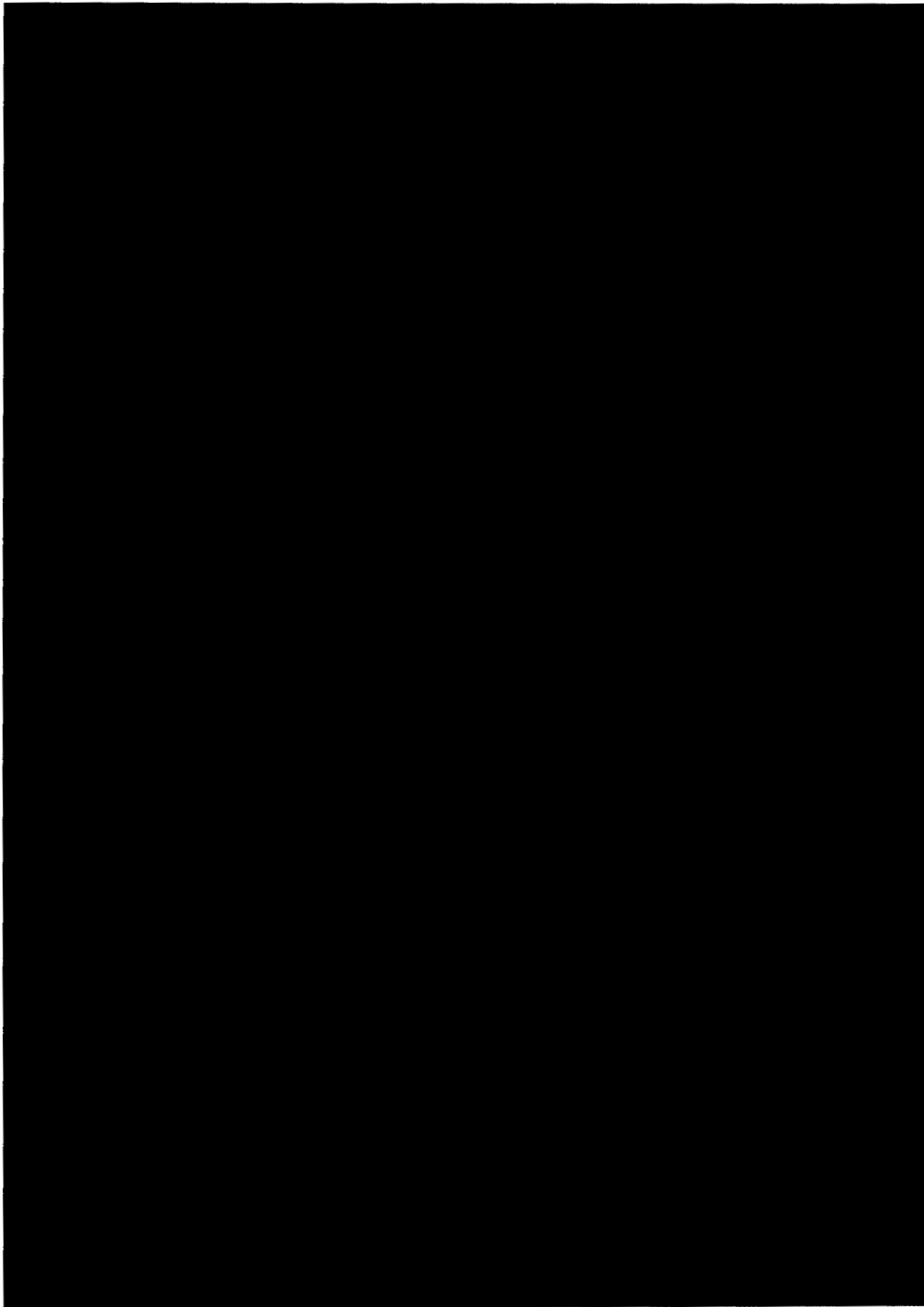






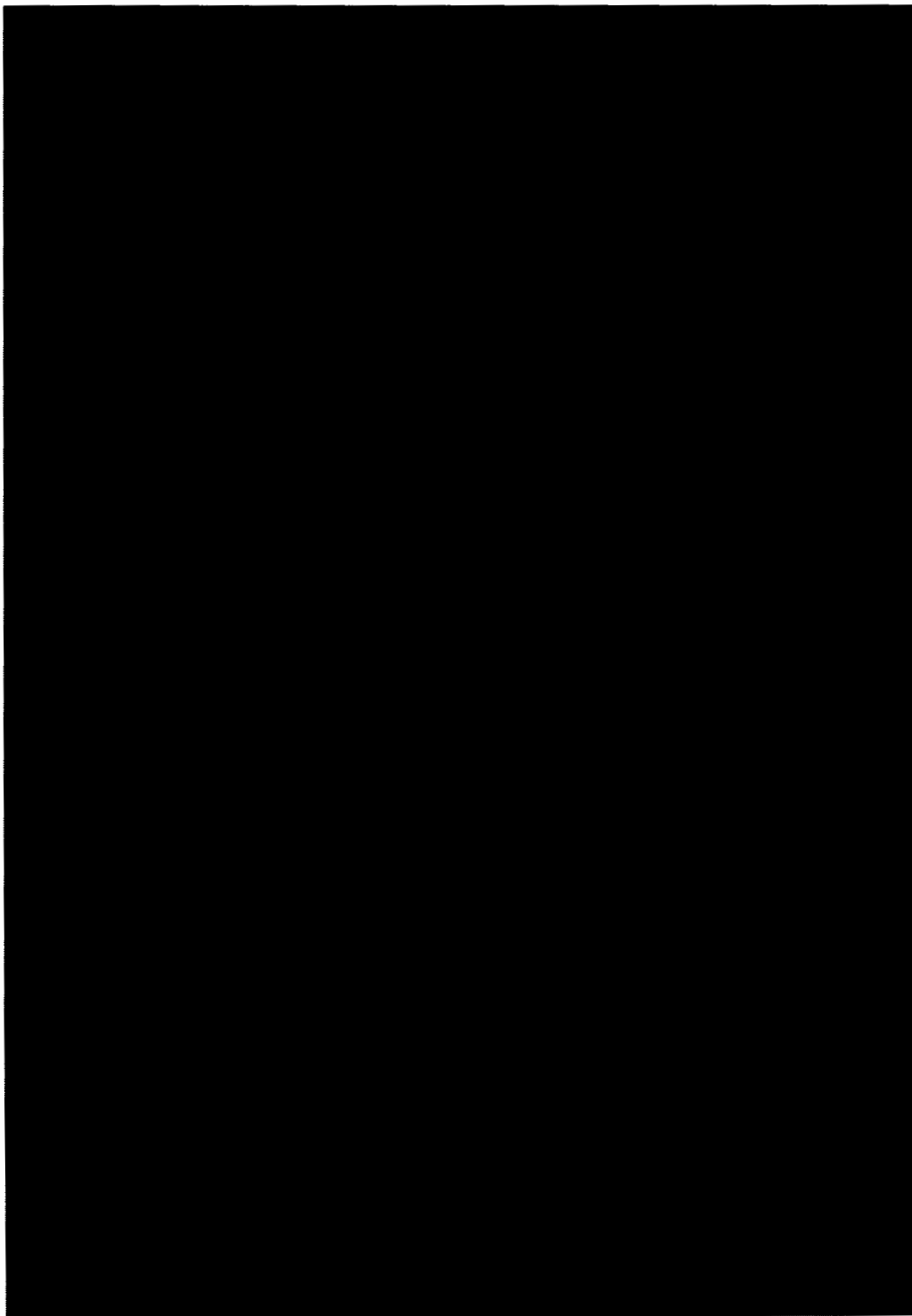


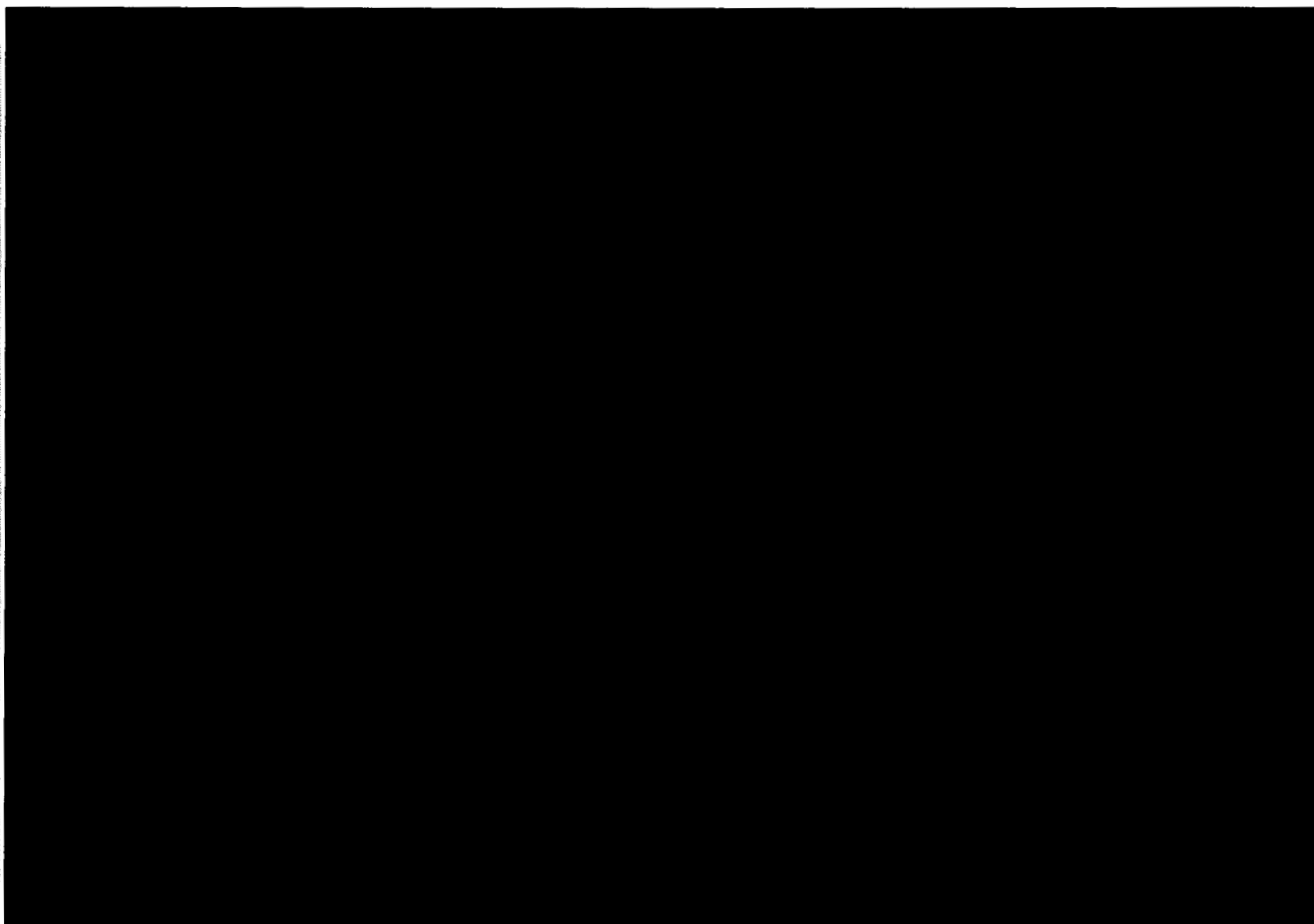
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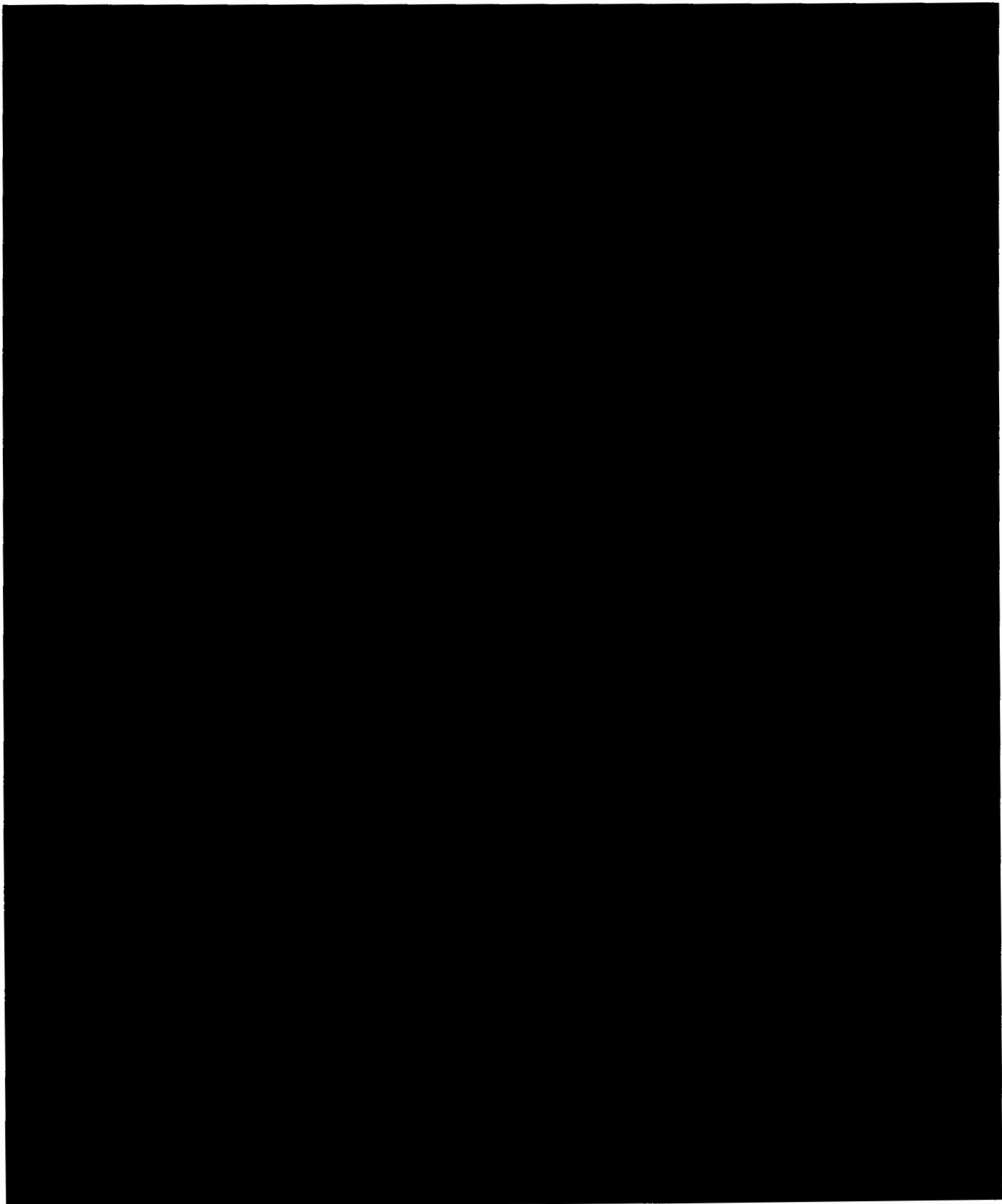


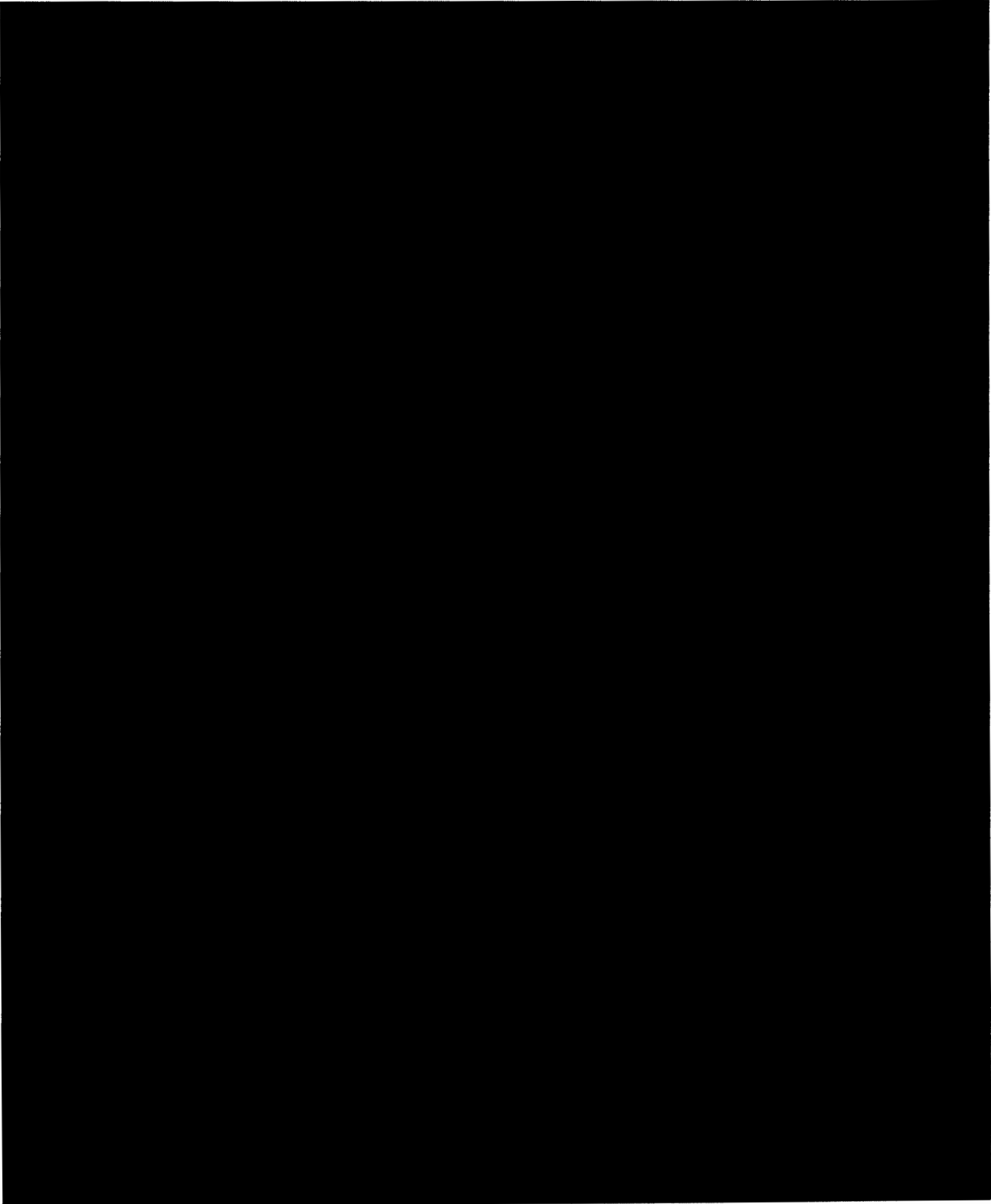
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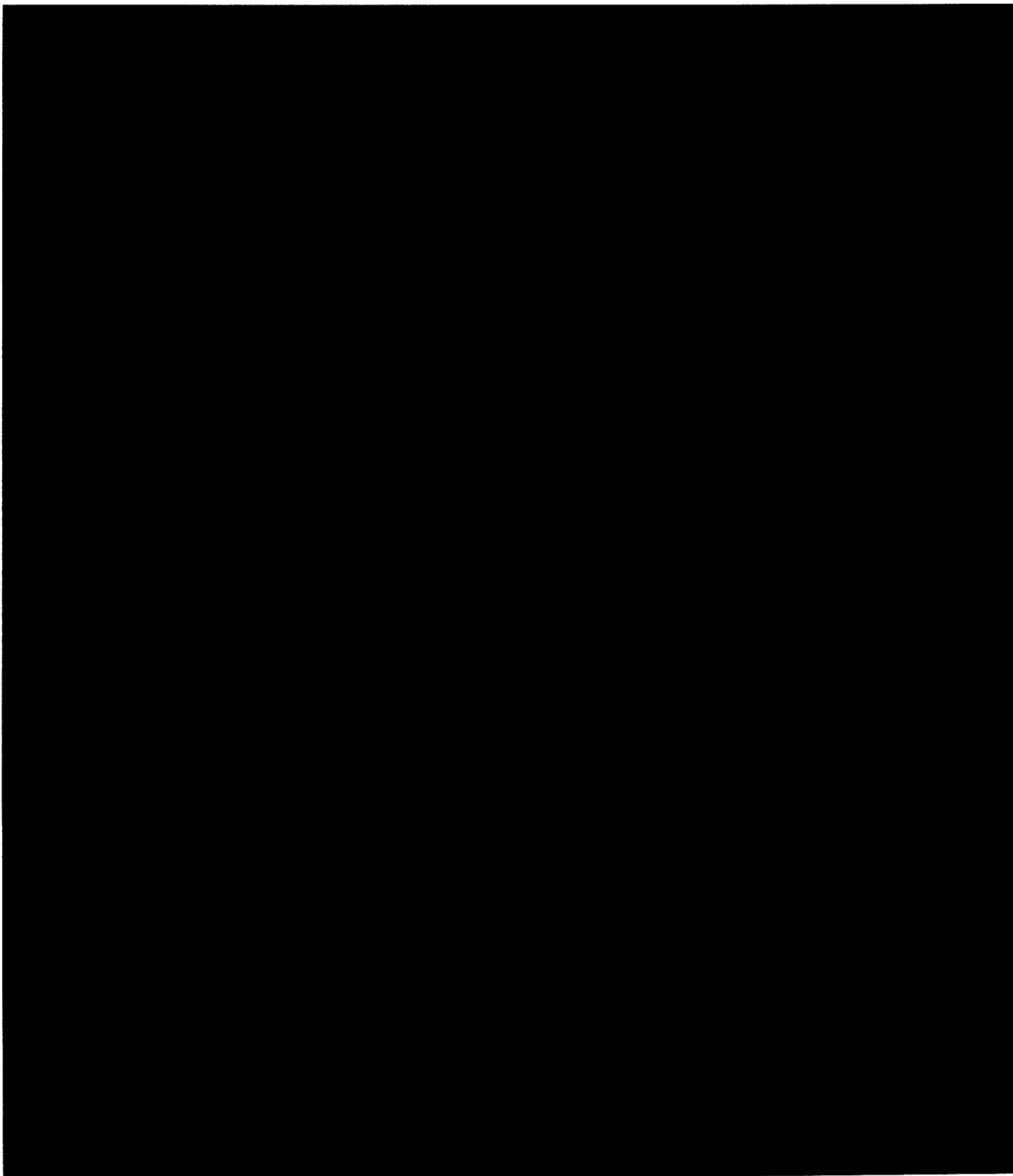


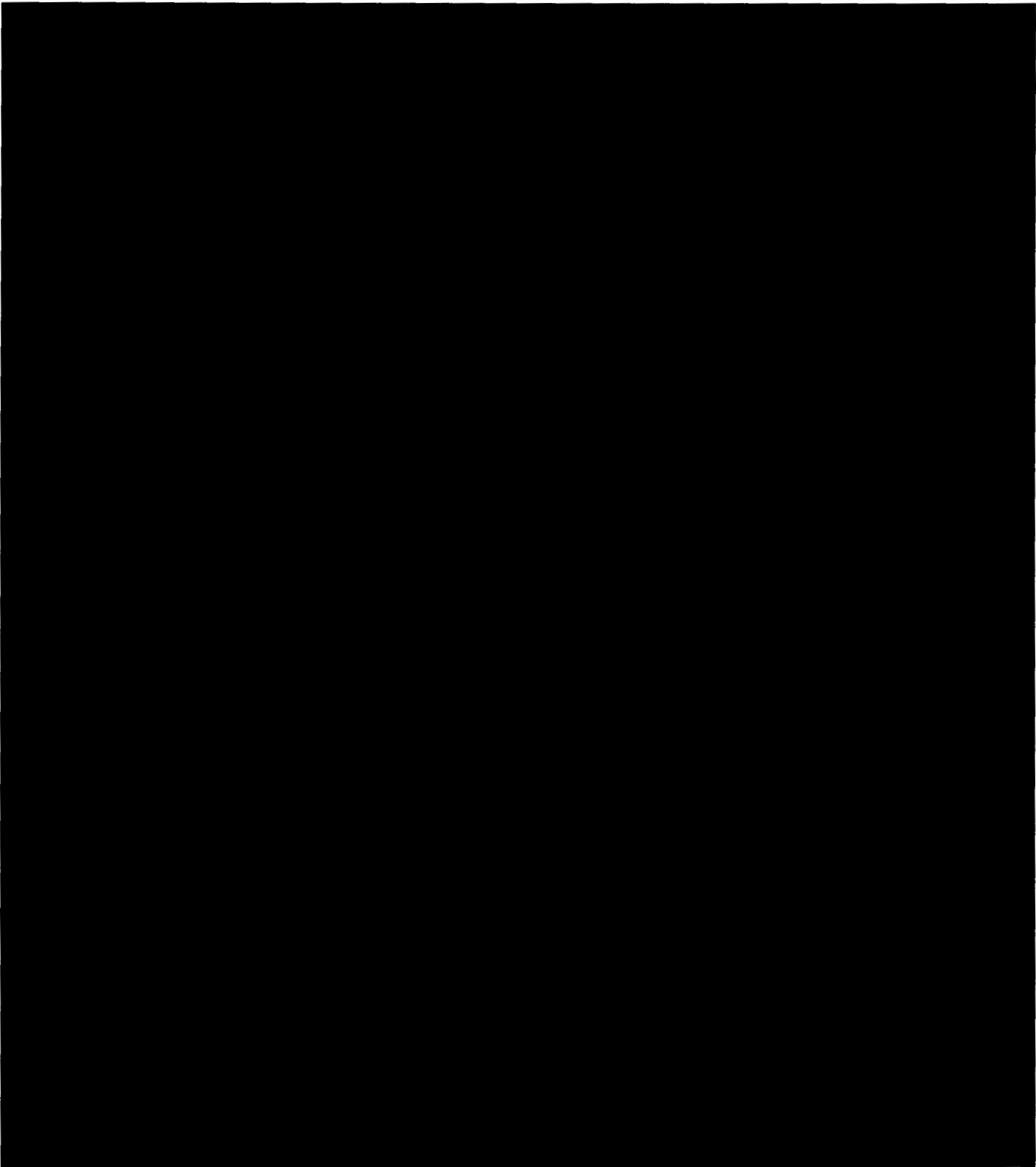


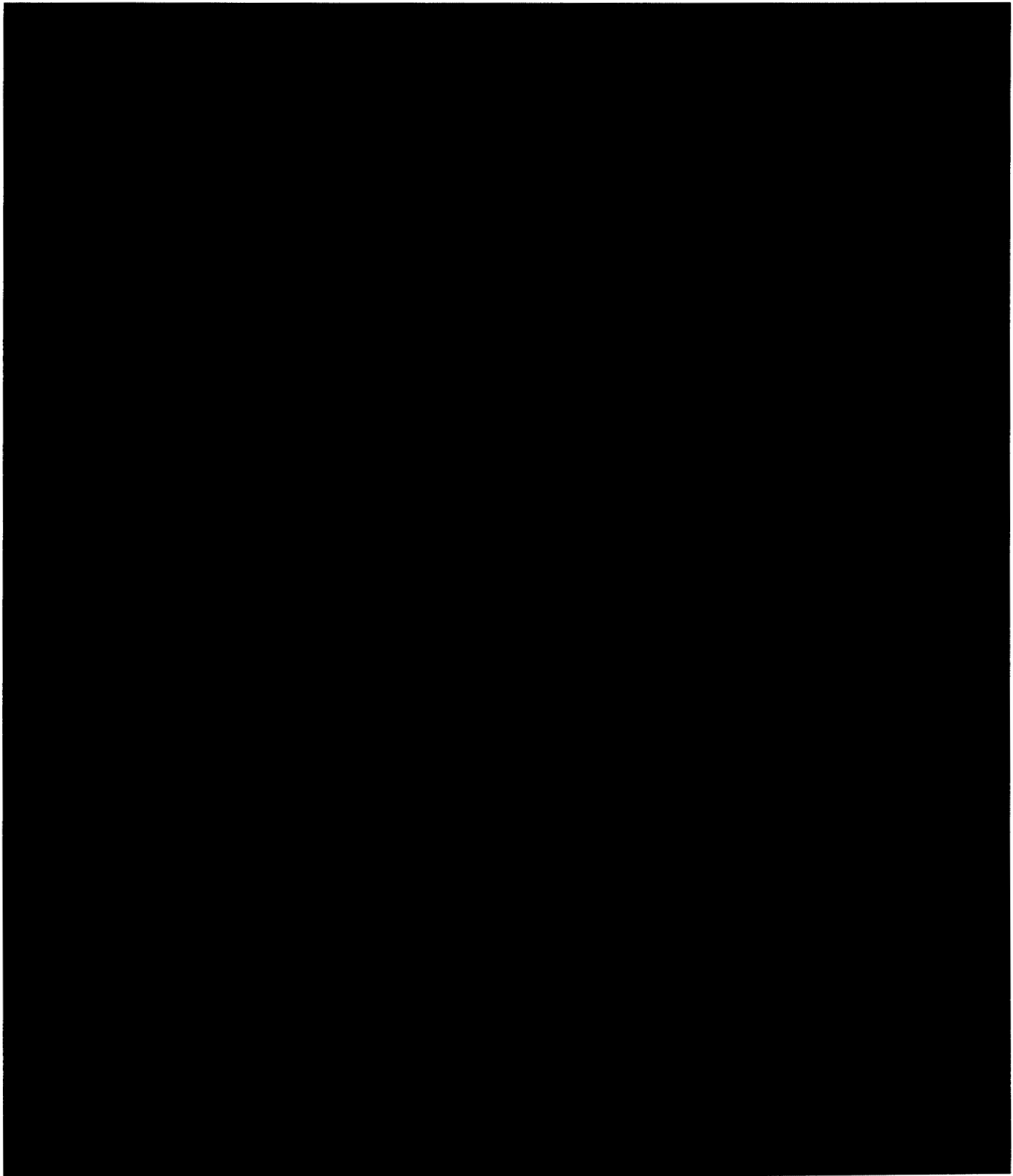


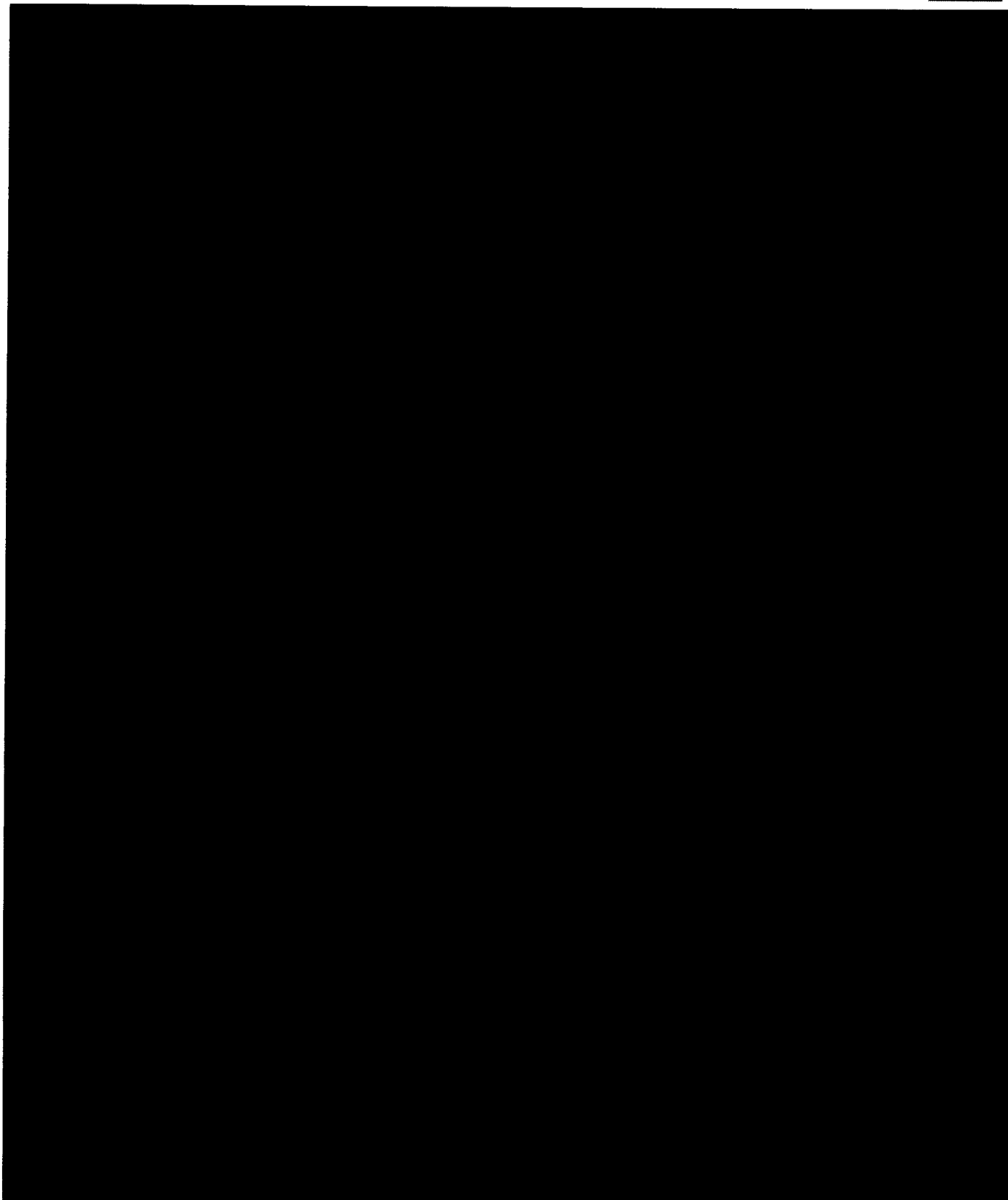


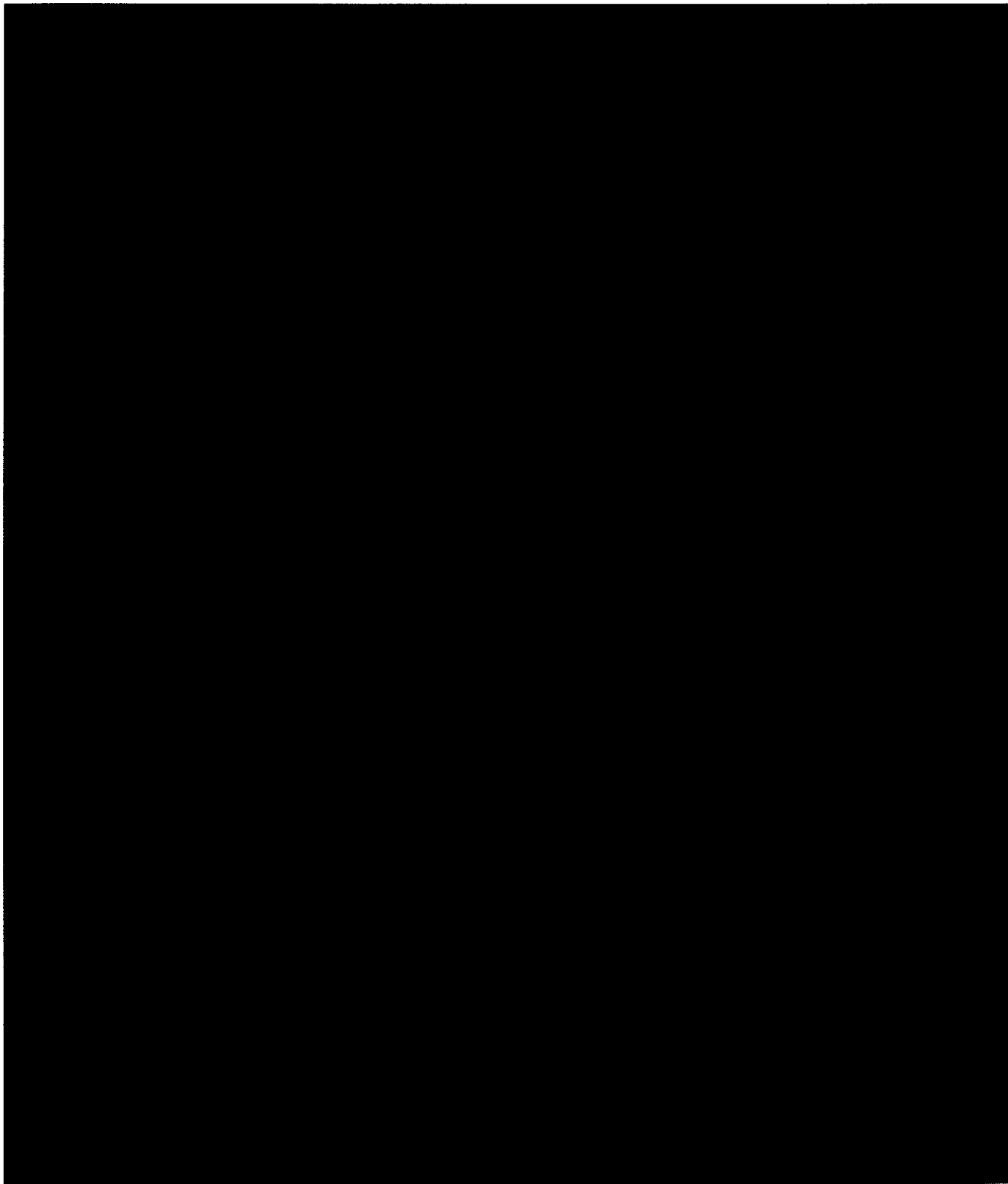






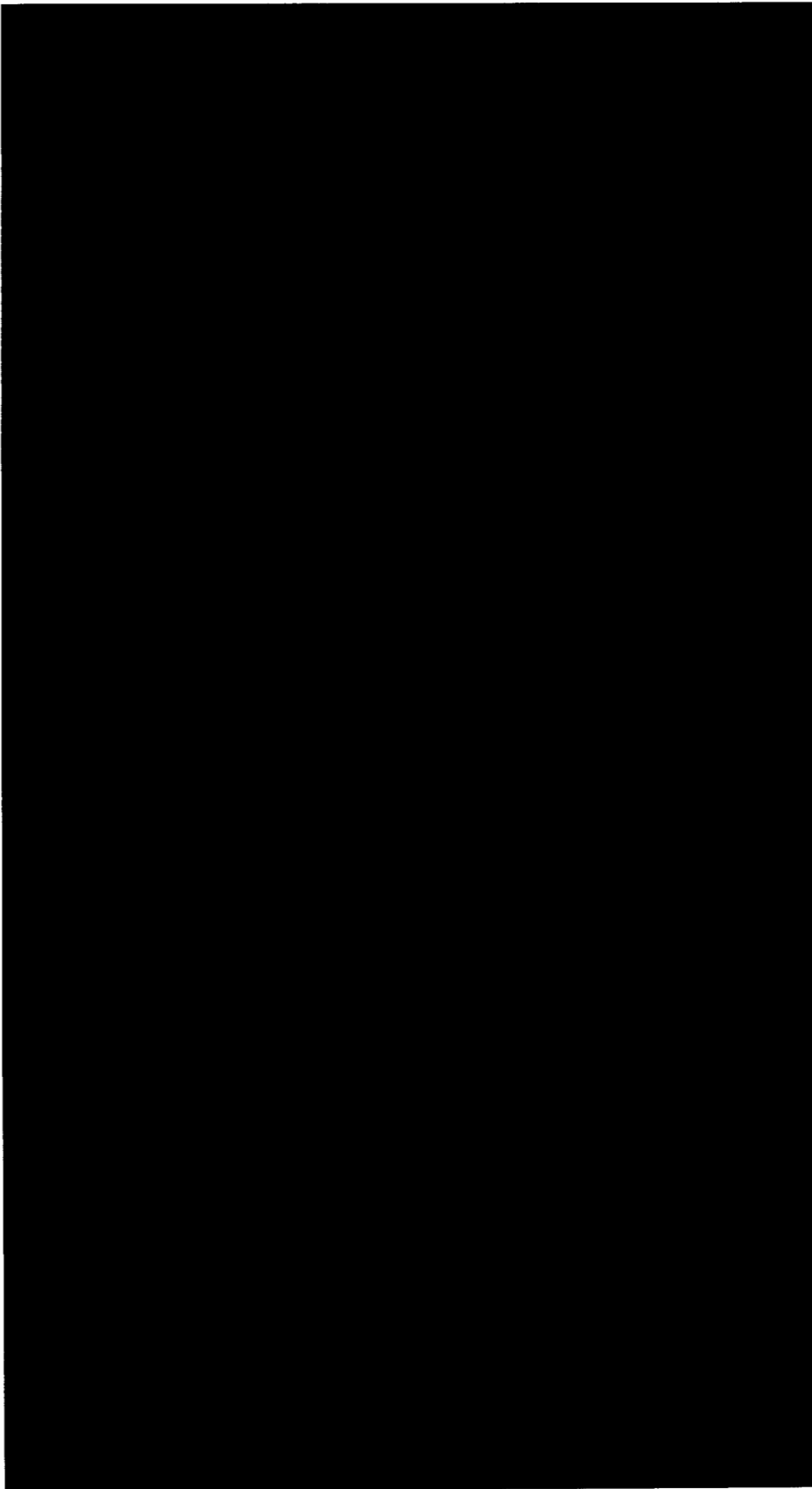






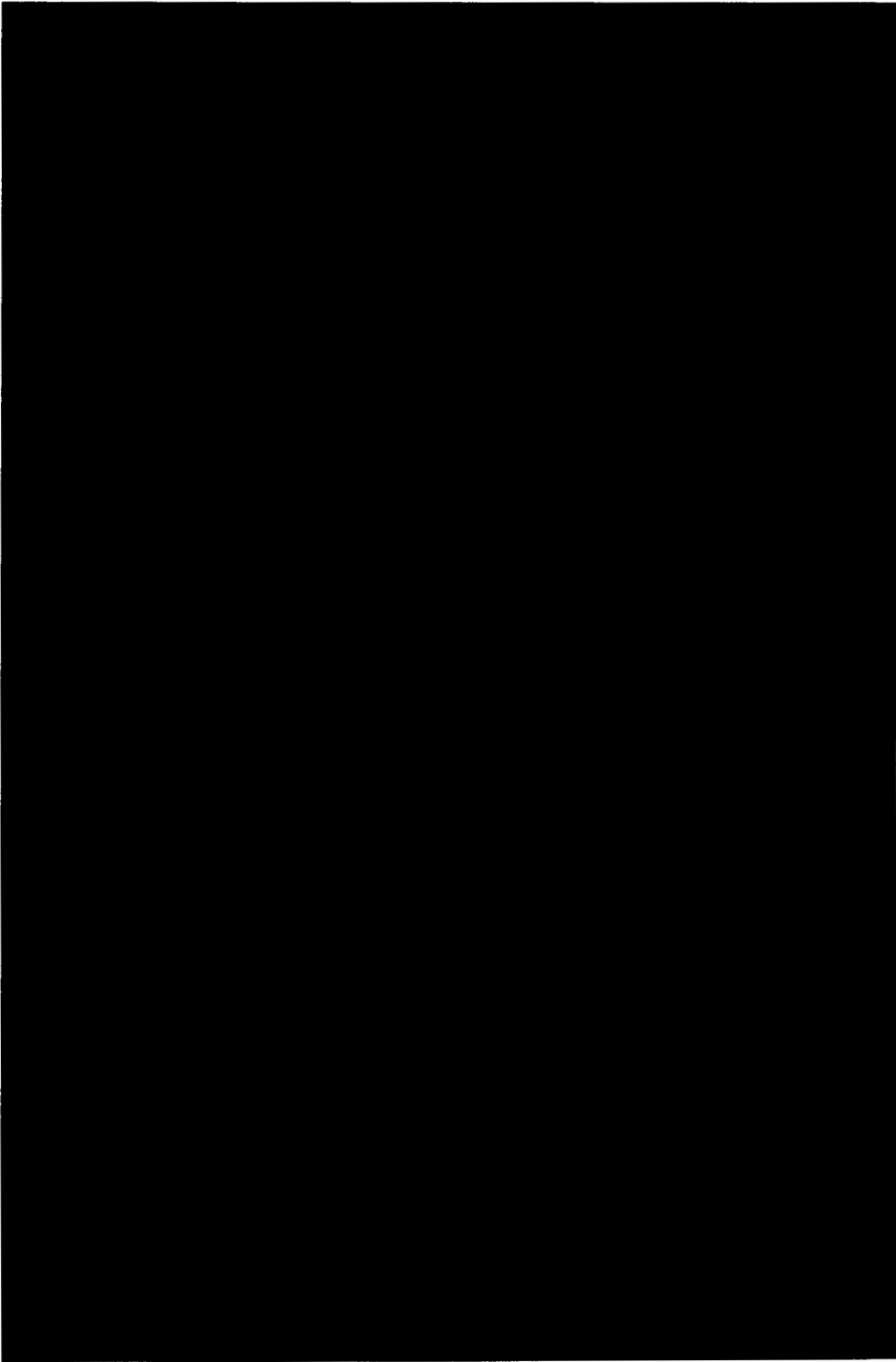


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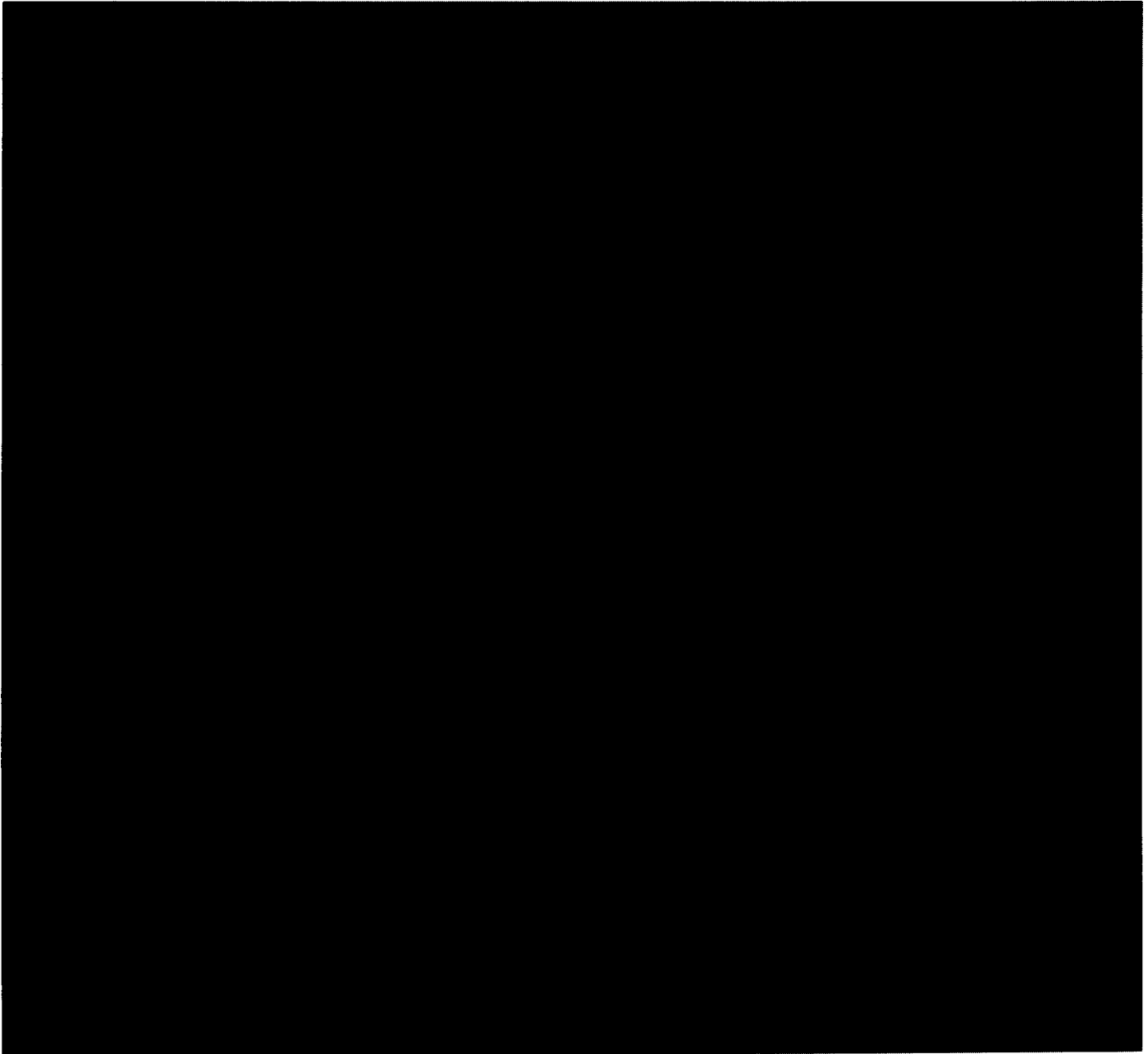
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Appendix 1

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BEFORE THE
ARKANSAS PUBLIC SERVICE COMMISSION

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

EAI EXHIBIT DEH-7

INTERNATIONAL STRATEGY & INVESTMENT GROUP LLC
POWER & UTILITIES RESEARCH
DIVERSIFIED UTILITIES

ENTERGY CORP (ETR)

JANUARY 3, 2014

THIS EXHIBIT CONTAINS CONFIDENTIAL PROTECTED INFORMATION
PROVIDED PURSUANT TO THE COMMISSION'S INTERIM PROTECTIVE
ORDER NO. 2 ISSUED ON FEBRUARY 21, 2013 IN THIS DOCKET

BEFORE THE
ARKANSAS PUBLIC SERVICE COMMISSION

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

EAI EXHIBIT DEH-8

MOODY'S INVESTORS SERVICE

"RATING ACTION: MOODY'S UPGRADES CERTAIN ENTERGY
SUBSIDIARIES, OUTLOOKS STABLE"

JANUARY 31, 2014

MOODY'S

INVESTORS SERVICE

Rating Action: Moody's upgrades certain Entergy subsidiaries, outlooks stable

Global Credit Research - 31 Jan 2014

Approximately \$11 Billion of Debt Securities Upgraded

New York, January 31, 2014 -- Moody's Investors Service upgraded the long-term ratings of Entergy Gulf States Louisiana, LLC (Issuer Rating to Baa1 from Baa2, Senior Secured to A2 from A3, Preferred Stock to Baa3 from Ba1); Entergy Louisiana, LLC (Issuer Rating and Senior Unsecured to Baa1 from Baa2, Senior Secured to A2 from A3, Preferred Stock to Baa3 from Ba1); Entergy Mississippi, Inc. (Issuer Rating to Baa2 from Baa3, Senior Secured to A3 from Baa1, Preferred Stock to Ba1 from Ba2); and Entergy Texas, Inc. (Issuer Rating to Baa3 from Ba1, Senior Secured to Baa1 from Baa2, and Senior Secured Shelf to (P)Baa1 from (P)Baa2).

Moody's also confirmed the rating of Entergy Arkansas, Inc. This rating action concludes the review of these companies' ratings Moody's initiated on November 8, 2013. The rating outlooks of Entergy Corporation and all of its subsidiaries are stable.

RATINGS RATIONALE

Moody's had placed the ratings on review for upgrade in response to Moody's more favorable view of the relative credit supportiveness of the US regulatory environment, as detailed in the September 2013 Request for Comment titled "Proposed Refinements to the Regulated Utilities Rating Methodology and our Evolving View of US Utility Regulation." Among the critical factors supporting this view include better cost recovery provisions, reduced regulatory lag, and generally fair and open relationships between utilities and regulators. The US utility sector's low number of defaults, high recovery rates, and generally strong financial metrics from a global perspective provide additional corroboration for these upgrades.

Entergy Gulf States Louisiana (EGSL) is regulated by the Louisiana Public Service Commission (LPSC), which has provided a relatively stable and credit supportive regulatory environment. Like other major utilities in the state, EGSL operates with earnings-sharing mechanisms and Formula Rate Plan (FRP). Moody's generally views FRPs as a credit positive, since they reduce regulatory lag and provide transparency on cost recoveries. EGSL has been operating under an FRP established in 2009 with an ROE mid-point of 10.65% and a +/- 75 basis point bandwidth. Earnings outside the bandwidth are allocated 60% to customers and 40% to the company. The company has recently over-earned under the FRP. LTM third-quarter 2013 metrics further justify the rationale, with Cash Flow Interest Coverage of 6.9x and CFO pre-WC to debt of 29%.

Entergy Louisiana (EL) is also regulated by the LPSC and benefits from a similar earnings-sharing mechanism and FRP structure. EL's FRP through 2012 incorporated a ROE mid-point of 10.25% and a +/- 80 basis point bandwidth, which included a recovery mechanism for LPSC-approved capacity additions. Similar to EGSL's FRP, earnings outside EL's bandwidth are allocated 60% to customers and 40% to the company. In December 2013, the LPSC and EL filed a settlement for its pending rate case, under which EL's base rates were to remain unchanged and the company was allowed to operate under a FRP through the 2016 test-year. The updated FRP incorporated a ROE of 9.95% and +/- 80 basis point bandwidth. In addition, the settlement included several riders outside of the FRP formula, including a capacity rider and the ability to recover costs associated with EL's MISO integration. EL is also permitted to implement a \$10 million base rate increase in December 2014. Certain other costs, including MISO related costs, capacity and purchase costs, environmental-related costs, efficiency-related costs, storm costs, and certain depreciation and decommissioning costs would be recover outside of the FRP mechanism. LTM third-quarter 2013 metrics further justify the rationale, with Cash Flow Interest Coverage of 5.5x and CFO pre-WC to debt of 20%.

Mississippi has traditionally fostered a fairly supportive regulatory environment for investor owned utilities. Entergy Mississippi (EM) has benefited from an ability to recover fuel costs in rates on a timely basis by filing for small but relatively frequent adjustments in rates. The company operates under a FRP that was modified in March 2010 to align it more with FRPs of other utilities in Mississippi. The modification replaced the old revenue change limit (2% with a \$14.5 million cap) with a 4% limit (no dollar cap), with any adjustment over 2% requiring a hearing. These changes were slightly positive from a credit standpoint. In August 2013, the MPSC approved \$22.3 rate increase, which would reset EM's ROE to 10.59%, which compares to an 8.96% earned ROE for 2012, with the increase

effective as of September 2013. LTM third-quarter 2013 metrics further justify the rationale, with Cash Flow Interest Coverage of 4.6x and CFO pre-WC to debt of 19%.

Moody's generally views the regulatory climate in Texas as credit positive for transmission and distribution utilities operating within ERCOT but somehow challenging for vertically integrated utilities operating outside of ERCOT. The PUC generally has not permitted the utilities to include construction work in progress (CWIP) in rate base, with the exception of certain environmental compliance costs. However, the companies are permitted to adjust rates through surcharge mechanisms to reflect certain types of new transmission and distribution investment, fuel and purchased power costs are recovered through a separate fuel factor, the level of which is established in base rate cases.

On September 2013, ET filed a rate case with the PUCT requesting a \$38.6 million base rate increase, reflecting a 10.4% ROE based on a test year ending March 31, 2013. ET also sought to implement several riders, including a rough production cost equalization adjustment rider (Rider RPCEA), a rate case expense rider (Rider RCE), deferred tax accounting rider (Rider DTA), and a transmission cost recovery rider (Rider TCRF). On January 17, the PUCT's staff filed testimony regarding the pending case recommending that the PUCT approve a \$3.4 million base rate increase based on 9.2% ROE, the settlement decision is expected by March 5, after rebuttal testimony, hearing, and briefs. The resolution of this case will be an important indicator of the trend in long-term credit supportiveness of Texas's regulatory environment. Despite being on a quarterly basis, LTM third-quarter 2013 metrics were stronger than initially projected, with Cash Flow Interest Coverage of 5.4x and CFO pre-WC to debt of 25%. Fiscal year end 2012 metrics were 4.5x Cash Flow Interest Coverage and 20% CFO pre-WC to debt.

Moody's confirmed the ratings of Entergy Arkansas based on the less than favorable rate case outcomes in May 2010 and December 2013. Arkansas operates under traditional rate of return regulation rather than the more credit supportive formula rate plans in place in Louisiana and Mississippi, where Entergy's other large subsidiaries operate. The rate of return regulation contributes to regulatory lag at Entergy Arkansas (EA). Under Arkansas regulation, the test year is either fully historical or 6 months historical and 6 months projected. However, there are fuel and certain other riders that help offset some aspects of the lag.

Historically, EA has experienced a relatively challenging regulatory environment. In March 2013, EA filed for a rate increase with the Arkansas Public Service Commission (APSC) that included MISO and capacity costs riders, receiving a decision in December 2013. The outcome was disappointing as EA received a base rate increase of \$81 million (without specifying the amounts to be recovered through MISO and Capacity Costs riders) based on a 9.3% ROE, significantly below its requested base rate increase of \$145 million based on 10.4% ROE. Resolution of EA's May 2010 rate case also yielded an increase below that expected of \$63.7 million (10.3% ROE) against the expected \$168 million (10.6% ROE). LTM third-quarter 2013 metrics are consistent with that of fiscal year end 2012, with Cash Flow Interest Coverage of 4.5x and CFO pre-WC to debt of 13%. According to Moody's adjusted projections, EA will be able to maintain appropriate metrics for the rating, including CFO pre-WC to debt, and CFO pre-WC -- Div to debt of around 16% and 14% respectively.

Rating Outlook

Entergy Gulf States Louisiana, Entergy Louisiana, and Entergy Mississippi outlooks are stable, reflecting that Moody's expects the companies will continue to exhibit financial metrics that are appropriate for their current ratings, that in Louisiana formula rate plan will continue to provide regulatory transparency and certainty, and that Mississippi's regulation will remain reasonably long-term credit supportive and allow the recovery of prudently incurred costs.

Entergy Texas' rating outlook is stable, reflecting Moody's view that the company will continue to generate adequate metrics for its rating. Although the regulatory lag for vertically integrated utilities will remain less credit supportive over the medium term in Texas, Moody's does not expect the regulatory environment to deteriorate. According to Moody's adjusted projections, ET will likely be able to maintain appropriate metrics for the rating, including CFO pre-WC to debt, and CFO pre-WC -- Div to debt of around 15% and 12% respectively.

Entergy Arkansas' rating outlook is stable, reflecting Moody's expectation that the utility's financial metrics will maintain levels that are appropriate for its rating despite the company's disappointing rate case outcomes. The outlook also assumes that regulatory lag will remain manageable and that the issues surrounding the company's exit from the Entergy System Agreement will be resolved in a manner not detrimental to credit quality. According to Moody's adjusted projections, EA will likely be able to maintain appropriate metrics for the rating, including CFO pre-WC to debt, and CFO pre-WC -- Div to debt of around 16% and 14% respectively.

What Could Change the Rating - Up

Entergy Gulf States Louisiana and Entergy Louisiana ratings could be upgraded if material long-term credit improvements were to happen in Louisiana regulation that set the state far above other jurisdictions in the US, if economic conditions in its service territory continued to improve, and if recently improved financial metrics were sustained in the absence of bonus depreciation, including consistent CFO pre-WC plus interest to interest above 5.5x and CFO pre-WC to debt nearing the mid-20% range.

The ratings for Entergy Mississippi could be further upgraded if there were an improvement in the regulatory and political environment in the state, or if there were a sustained increase in EM's cash flow coverage metrics, including CFO pre-WC to debt above 19%.

The rating of Entergy Texas is unlikely to be upgraded in the near term; however an upgrade could come under consideration if there is a material and sustained improvement in the regulatory environment in Texas for vertically integrated utilities --outside ERCOT- including the implementation of long-term credit-supportive rate design and cost recovery mechanisms, and continued strong financial metrics, including CFO pre-WC to Debt above 16% on a sustained basis.

The ratings of Entergy Arkansas could be upgraded if there were an improvement in the credit supportiveness of the regulatory environment in Arkansas, along with a sustainable increase in cash flow coverage metrics, including CFO pre-WC to debt above 22%.

What Could Change the Rating - Down

The ratings for Entergy Gulf States Louisiana, Entergy Louisiana, and Entergy Mississippi could be downgraded if there were a deterioration in the regulatory environment for utilities in Louisiana, and Mississippi, if there were significant additional storm costs that were not recovered on a timely basis through the regulatory process, or if financial metrics excluding bonus depreciation exhibited a sustained decline.

The ratings of Entergy Texas could be downgraded if the business and regulatory environment in which it operates were to deteriorate, if pending or future rate case outcomes are detrimental to its credit profile, or if there were a significant decline in financial metrics, including CFO pre-WC to debt below 13% on a sustained basis.

The ratings of Entergy Arkansas could be downgraded if there were continuous adverse regulatory developments, if there were a termination or any changes to the utility's rate riders that would prevent full and timely recovery of prudently incurred costs, or if there is not an improvement in cash flow coverage metrics from unusually low 2012 and 2013 levels, including CFO pre-WC to debt below 15% for an extended period.

The principal methodology used in these ratings was Regulated Electric and Gas Utilities published in December 2013. Please see the Credit Policy page on www.moodys.com for a copy of this methodology.

The following ratings of Entergy Gulf States Louisiana are upgraded:

Issuer Rating to Baa1 from Baa2

Preference Stock to Baa3 from Ba1

Pref. Shelf to (P)Baa3 from (P)Ba1

First Mortgage Bonds to A2 from A3

The outlook of Entergy Gulf States Louisiana is stable from RUR-UP

The following ratings of Entergy Louisiana are upgraded:

Issuer Rating to Baa1 from Baa2

Senior Unsecured to Baa1 from Baa2

Pref. Stock to Baa3 from Ba1

Backed First Mortgage Bonds to A2 from A3

Underlying First Mortgage Bonds to A2 from A3

First Mortgage Bonds to A2 from A3

The outlook of Entergy Louisiana is stable from RUR-UP

The following rating of W3A Funding Corporation has been upgraded:

BACKED Senior Secured Shelf to (P)Baa1 from (P)Baa2

The outlook of W3A Funding Corporation is stable from RUR-UP

The following ratings of Entergy Mississippi are upgraded:

Issuer Rating to Baa2 from Baa3

Senior Secured Shelf to (P)A3 from (P)Baa1

Pref. Stock to Ba1 from Ba2

Underlying First Mortgage Bonds to A3 from Baa1

First Mortgage Bonds to A3 from Baa1

Backed First Mortgage Bonds to A3 from Baa1

The outlook of Entergy Mississippi is stable from RUR-UP

The following ratings of Entergy Texas are upgraded:

Issuer Rating to Baa3 from Ba1

Senior Secured Shelf to (P)Baa1 from (P)Baa2

First Mortgage Bonds to Baa1 from Baa2

The outlook of Entergy Texas is stable from RUR-UP

The following ratings of Entergy Arkansas, Inc. are confirmed:

Issuer Rating, Confirmed at Baa2

Pref. Stock Preferred Stock, Confirmed at Ba1

Pref. Stock Shelf, Confirmed at (P)Ba1

Senior Secured First Mortgage Bonds, Confirmed at A3

The outlook of Entergy Arkansas, Inc. is stable from RUR-UP

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BEFORE THE
ARKANSAS PUBLIC SERVICE COMMISSION

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

EAI EXHIBIT DEH-9

REGULATORY RESEARCH ASSOCIATES

MAJOR RATE CASE DECISIONS – CALENDAR 2013

JANUARY 15, 2014

THIS EXHIBIT CONTAINS CONFIDENTIAL PROTECTED INFORMATION
PROVIDED PURSUANT TO THE COMMISSION'S INTERIM PROTECTIVE
ORDER NO. 2 ISSUED ON FEBRUARY 21, 2013 IN THIS DOCKET

BEFORE THE
ARKANSAS PUBLIC SERVICE COMMISSION

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

REHEARING DIRECT TESTIMONY

OF

HUGH T. MCDONALD

PRESIDENT AND CHIEF EXECUTIVE OFFICER
ENTERGY ARKANSAS, INC.

ON BEHALF OF

ENTERGY ARKANSAS, INC.

MARCH 14, 2014

1 **I. BACKGROUND AND INTRODUCTION**

2 Q. PLEASE STATE YOUR NAME.

3 A. My name is Hugh T. McDonald.

4

5 Q. ARE YOU THE SAME HUGH T. MCDONALD WHO PREVIOUSLY
6 FILED TESTIMONY IN THIS DOCKET?

7 A. Yes, I am.

8

9 Q. ON WHOSE BEHALF ARE YOU TESTIFYING?

10 A. I am submitting this rehearing direct testimony to the Arkansas Public
11 Service Commission ("APSC" or the "Commission") on behalf of
12 Entergy Arkansas, Inc. ("EAI" or the "Company").

13

14 Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?

15 A. The APSC granted EAI's petition for rehearing in this docket and
16 allowed EAI to present new evidence related to the reaction of several
17 security analysts and a rating agency to Order No. 21 (the "Order") as
18 well as a report on Return on Equity ("ROE") decisions in other utility
19 rate cases. My testimony will underscore the importance of granting
20 the relief sought in EAI's petition for rehearing. The Company is at a
21 crossroads. It needs financial stability to meet the challenges of
22 operating independently of the Entergy System Agreement and the
23 significant capital investment planned in the next few years. Now is

1 not the time to test the Company's ability to meet these challenges if
2 hindered by a sub-standard return on equity ("ROE"), a formula for
3 calculating Allowance for Funds Used During Construction ("AFUDC")
4 that does not fully recover financing costs, and disallowed costs that
5 will prevent EAI from earning even the low allowed ROE.

6
7 Q. IS THE COMPANY SPONSORING OTHER WITNESSES?

8 A. Yes. EAI witness David Hunt, in his rehearing direct testimony,
9 presents reports from equity financial analysts and a rating agency in
10 response to the order. In addition, he provides a comparison of the
11 ROE determination in this case with other regulatory commission ROE
12 determinations in calendar year 2013 and historically, which
13 demonstrates that the 9.3 percent ROE allowed for EAI in this case
14 was the second lowest ROE awarded to a vertically integrated electric
15 utility in 2013, the lowest non-penalty ROE awarded to a vertically
16 integrated electric utility in 2013, and among the lowest ROEs ever
17 awarded to an investor-owned, vertically integrated electric utility. In
18 addition, former utility analyst Ellen Lapson of Lapson Consulting
19 explains how the significant disparity in EAI's allowed ROE and that of
20 other peer utilities has created a reaction among security analysts and
21 a rating agency that is negative to EAI and its customers.

1 **II. SUPPORT FOR RELIEF ON REHEARING**

2 Q. WHY HAS EAI REQUESTED REHEARING OF THE ORDER?

3 A. EAI has just completed a decade-long transition out of the System
4 Agreement and into operation in the Midcontinent Independent System
5 Operator, Inc. ("MISO") Regional Transmission Organization. As a
6 result, for the first time since 1951, EAI is operating and transacting in
7 power markets on its own behalf rather than under the System
8 Agreement.

9 In addition to operating within the new framework, the Company
10 faces a number of other challenges in the near future. EAI must
11 continue to make investments required to serve customers in its
12 service territory. Plus, the industry is changing rapidly, and EAI plans
13 to investment approximately \$3.4 billion from 2012 through 2018¹ to
14 meet evolving environmental standards, infrastructure needs in
15 generation, transmission, and distribution, as well as, strategic
16 initiatives like smart grid development and recruitment of energy
17 intensive industries. Successfully addressing these initiatives will
18 require the Commission's support, and the Order does just the
19 opposite.

¹ Lewis Direct Testimony at 5 (March 1, 2013).

1 Q. WHY DO YOU SAY THAT?

2 A. The reality facing EAI as a result of the Order is that a 9.3 percent
3 allowed ROE will hinder the Company's ability to acquire capital and
4 the cost of that capital will be higher. Further, the Order disallowed
5 recovery of several categories of costs that do not go away because
6 they are not reflected in rates, which will reduce the actual return of the
7 Company even more. And finally, the cap on the AFUDC rate set in
8 the Order will erode EAI's earnings even further as investments are
9 completed and the cost of that investment, including AFUDC, is placed
10 into rates that do not fully reflect actual financing costs.²

11

12 Q. WHAT OTHER IMPACT WILL THE ORDER HAVE?

13 A. It could negatively affect economic development in the state. EAI has
14 a long history of active involvement in attracting industrial prospects to
15 the communities it serves. EAI is heavily involved with the Arkansas
16 Department of Economic Development and the Governor's office in
17 major industrial retention and recruitment efforts. This is a benefit to
18 the state because industrial growth brings more jobs and higher tax
19 revenues, a benefit to the Company because growth produces higher
20 revenues, and a benefit to customers because these higher revenues
21 offset future rate increases. The effects of the Order impair EAI in

² See *id.* at 7.

1 playing a major role in attracting new industry if that requires incentives
2 and significant capital investment to induce an industrial prospect to
3 locate in Arkansas.

4

5 Q. WHY SHOULD THE COMMISSION GRANT EAI ANY RELIEF ON
6 THE ISSUES IN ITS PETITION?

7 A. There are at least two bases for the Commission to reconsider its
8 decisions on issues in the Order that have come to light since it was
9 issued. First, Ms. Lapson explains her view that the consensus
10 reaction of financial analysts and a credit analysis firm is that the
11 collective impact of the Order -- including the 9.3 percent allowed ROE,
12 an AFUDC formula that does not fully compensate the Company for its
13 financing costs, and other cost disallowances -- will inhibit the
14 Company's ability to earn even this relatively low allowed ROE and will
15 weaken the Company financially. As a result, as Ms. Lapson explains,
16 the financial community will place a higher discount rate on Entergy
17 Corporation's equity because of the perception of greater regulatory
18 risk for EAI, which will increase the company's cost of capital. In
19 addition, Moody's Investors Service ("Moody's") recently completed a
20 review of the securities ratings of U.S. utilities by upgrading the
21 securities ratings of more than 90 percent of the utilities under
22 consideration. While Moody's upgraded the large majority of utilities
23 under consideration, including other Entergy Operating Companies,

1 Moody's did not upgrade EAI's securities ratings, citing the Order and
2 continuing concern about regulatory lag.³ As Ms. Lapson explains, the
3 effect is a downgrade in rating compared to most of the Company's
4 peers, which raises the cost for EAI to borrow money. This raises
5 customers' rates.

6 Second, Ms. Lapson explains that not recognizing the effect of
7 the Federal Reserve's monetary stimulus program and relying solely
8 on a quantitative analysis in setting the Company's allowed ROE
9 produced an unreasonable result that will hinder EAI's ability to secure
10 long-term debt on favorable terms and make it more costly for equity
11 investment in EAI. This raises customers' rates.

12 The Commission's granting of the Company's rehearing petition
13 provides the Commission an opportunity to review the new evidence
14 that EAI is submitting and to reconsider and revise its positions. By
15 doing so, the Commission would address those issues that create the
16 regulatory lag and weak operating cash flow ratios cited by Moody's in
17 explaining why it did not upgrade EAI's securities ratings and that
18 caused utility analysts to report the negative impact of the Order on
19 EAI's financial position, including: a 9.3 percent allowed ROE, an
20 AFUDC rate that does not fully compensate for construction cost

³ See Hunt Rehearing Direct Testimony, EAI Exhibit DEH-8 (March 14, 2014).

1 financing, and cost disallowances that hinder the Company's ability to
2 earn even the low allowed ROE.

3 The result of this rate case should be to position the Company
4 to serve its customers in the post-System Agreement world and to
5 support its communities in developing strong and vibrant economies.
6 By granting the requested relief, the public interest will be served, and
7 the Company will be spared the prospect of financial instability at this
8 critical time.

9

10 Q. DOES THIS CONCLUDE YOUR DIRECT TESTIMONY?

11 A. Yes.

CERTIFICATE OF SERVICE

I, Steven K. Strickland, do hereby certify that a copy of the foregoing has been served upon all parties of record by forwarding the same by electronic mail and/or first class mail, postage prepaid, this 14th day of March 2014.

/s/ Steven K. Strickland
Steven K. Strickland