

**BEFORE THE
ARKANSAS PUBLIC SERVICE COMMISSION**

**IN THE MATTER OF AN APPLICATION OF)
ENTERGY ARKANSAS, INC., MID SOUTH)
TRANSCO LLC, ITC MIDSOUTH LLC,)
TRANSMISSION COMPANY ARKANSAS, LLC,)
AND ITC HOLDINGS CORP. TO ENTER)
TRANSACTIONS RESULTING IN A)
CERTIFICATE OF PUBLIC CONVENIENCE)
AND NECESSITY FOR A NEW ARKANSAS)
UTILITY TO OWN EAP'S ELECTRIC)
TRANSMISSION FACILITIES)**

DOCKET NO. 12-069-U

**DIRECT TESTIMONY
OF
DANIEL E. PEACO
ON BEHALF OF THE GENERAL STAFF OF THE
ARKANSAS PUBLIC SERVICE COMMISSION**

PUBLIC VERSION

APRIL 19, 2013

DOCKET NO. 12-069-U

DIRECT TESTIMONY OF DANIEL PEACO

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DOCKET NO. 12-069-U

DIRECT TESTIMONY

OF

DANIEL PEACO

I. QUALIFICATIONS

Q. Please state your name, position, and business address.

A. My name is Daniel Peaco. I am President of La Capra Associates, Inc. My business address is One Washington Mall, 9th Floor, Boston, Massachusetts 02108.

Q. Please summarize your professional experience and qualifications.

A. I am an electric power industry planning specialist with over 30 years of experience in power markets and marketing, strategic planning, pricing and price forecasting, power procurement and contracts, and power systems planning. My consulting practice has included a range of engagements relating to integrated resource planning, transmission planning, renewable energy planning and policy, competitive electric markets and industry restructuring, generation asset valuation, strategic planning, competitive market formation and pricing, market analysis of prices and supply requirements, power contract analysis, and power procurement practices.

I am currently President of La Capra Associates and have served in that capacity since 2001. Prior to joining La Capra Associates, I held power supply planning positions with

1 Central Maine Power Company (1986-96), Pacific Gas & Electric Company (1981-86),
2 and the Massachusetts Energy Facilities Siting Council (1978–79).

3 I hold a master’s degree in Engineering Sciences from the Thayer School of Engineering
4 at Dartmouth College (1981) and a bachelor’s degree in Civil Engineering from the
5 Massachusetts Institute of Technology (1977). A copy of my resume is attached hereto
6 as Exhibit DEP-1.

7 **Q. Please summarize La Capra Associates and its business.**

8 A. La Capra Associates provides consulting services in energy planning, market analysis,
9 and regulatory policy in the electricity and natural gas industries. We serve a national
10 and international clientele from our offices in Boston, Massachusetts; Portland, Maine;
11 and Williston, Vermont providing consulting services to a broad range of organizations
12 involved with energy markets, including renewable energy producers, private and public
13 utilities, energy producers and traders, energy consumers and consumer advocates,
14 regulatory agencies, and public policy and energy research organizations. Our technical
15 skills include power market forecasting models and methods, economics, management,
16 planning, rates and pricing, and energy procurement, and contracting. Our experience
17 includes detailed analyses of energy and environmental performance of the electric
18 systems, economic planning for transmission, and market analytics.

19 **Q. Have you previously testified before this or other Commissions?**

20 A. Yes. I appeared before the Arkansas Public Service Commission (“Commission”) on
21 behalf of General Staff in Docket No. 10-011-U regarding EAI’s exit from the Entergy
22 system agreement and EAI’s proposal to join the Midwest Independent System Operator
23 (“MISO”) regional transmission organization (“RTO”) and in several proceedings on
24 behalf of the General Staff in 2000 and 2001. In addition to my appearances before the

1 Commission, I have testified on numerous occasions before state commissions in Maine,
2 Oklahoma, Connecticut, Georgia and Nevada and have testified before siting agencies in
3 Massachusetts, Connecticut, and Rhode Island. A listing of my expert witness
4 appearances is included in Exhibit DEP-1.

5 **II. PURPOSE OF TESTIMONY**

6 **Q. On whose behalf are you appearing in these proceedings?**

7 A. I am testifying on behalf of the General Staff of the Arkansas Public Service Commission
8 (“Staff”). Staff retained La Capra Associates to assist in its review of the Application of
9 Entergy Arkansas, Inc. (“EAI”), Mid South TransCo LLC (“Mid South TransCo”), ITC
10 Midsouth LLC (“ITC Midsouth”), Transmission Company Arkansas, LLC (“TCA”), and
11 ITC Holdings Corp (“ITC”) (collectively, “Applicants”) pertaining to the proposed
12 transfer of EAI’s transmission assets to ITC.

13 **Q. Please describe the purpose of your testimony.**

14 A. The purpose of my Direct Testimony and the Technical Report attached as Staff Exhibit
15 DEP-2 (“Report”) is to provide Staff’s response to the Application. The Report explains
16 Staff’s assessment of the Application and discusses a number of issues that are important
17 to the decisions pending in this proceeding. In this testimony, I summarize the key
18 findings in that Report and provide Staff’s position on the merits of the Application.

19 **Q. Please provide a brief overview of the Commission actions requested in the**
20 **Application.**

21 A. Entergy and ITC proposed a Transaction that would transfer ownership of the
22 transmission assets owned by Entergy’s Operating Companies (“Entergy OpCos”) to
23 ITC, removing EAI and all Entergy OpCos from the transmission business. Within the

1 context of that Transaction, the Commission has been asked to authorize those aspects of
2 the Transaction that pertain to EAI, and TCA/ITC Arkansas.

3 In the Transaction, EAI will separate its transmission assets and operations into TCA and
4 TCA will become a public utility subject to Commission jurisdiction for the transmission
5 business that it receives from EAI. Following formation of TCA, EAI will transfer
6 ownership of TCA to Mid South TransCo (an Entergy subsidiary created in the
7 Transaction to hold TCA and the newly formed wires companies from each of the
8 Entergy OpCos). TCA will be included in the spinoff of Mid South TransCo to Entergy
9 shareholders and the subsequent merger of Mid South TransCo with ITC. Upon
10 completion of the merger, TCA will be renamed ITC Arkansas and will be an operating
11 subsidiary of ITC Midsouth. ITC Arkansas will retain TCA's status as the public utility
12 in Arkansas subject to Commission jurisdiction. EAI and ITC Arkansas will be
13 completely separate and unaffiliated companies. ITC Arkansas will remain affiliated
14 with the wires companies formed by each of the Entergy OpCo in the Transaction, each
15 as operating subsidiaries of ITC Midsouth.

16 The Application includes a number of requests for Commission action to authorize the
17 EAI and TCA aspects of the Transaction, including:¹

- 18 1) Authorization for EAI to transfer all of its transmission assets to TCA,
19 including all authorizations previously granted to EAI to allow TCA to
20 operate as a transmission utility in Arkansas;
- 21 2) Recognition of TCA as a public utility subject to the jurisdiction of the
22 Commission;

¹ Application, pages 6 – 9.

- 1 3) Exempting TCA from certain statutory requirements related to TCA providing
- 2 exclusively wholesale services and not requiring setting of retail rates;
- 3 4) An accounting order for deferral of EAI transmission costs resulting from the
- 4 Transaction pending the establishment of new base rates; and
- 5 5) Authorization for EAI to be restructured as a limited liability company,
- 6 transferring EAI to Entergy Arkansas LLC.

7 The Application also asks for any other approvals necessary from the Commission to
8 complete the Transaction. Other steps of the Transaction that may require Commission
9 action include:

- 10 1) EAI's transfer of its 100% ownership rights of TCA, once formed, to Entergy;
- 11 2) Entergy's transfer of its 100% ownership rights of TCA, once acquired, to Mid
- 12 South TransCo;
- 13 3) Entergy's transfer of its 100% ownership rights of TCA, as part of Mid South
- 14 TransCo, to the Entergy Shareholders;
- 15 4) Entergy shareholders transfer of their 100% ownership rights of TCA to ITC,
- 16 once acquired, as part of the merger of Mid South TransCo and ITC; and
- 17 5) The transformation of TCA to ITC Arkansas, following completion of the
- 18 merger.

19 The Application also requests that the Commission make a finding that the
20 Transaction is in the public interest.

1 **III. SCOPE OF STAFF REVIEW**

2 **Q. Please describe Staff's approach to the preparation of this Direct Testimony.**

3 A. Staff, with the support of me and others at La Capra Associates Inc., has reviewed the
4 materials filed by the Applicants in September 2012. In addition, Staff² has conducted
5 discovery with EAI and ITC on the filed materials and participated in informal technical
6 sessions. The technical evaluation of the materials in this effort was conducted by me or
7 by La Capra Associates personnel working under my direction. Members of the Staff
8 and I have collaborated on the development of the conclusions and recommendations
9 included in this testimony.

10 **Q. What information have you reviewed in preparing this testimony?**

11 A. Staff has reviewed the following documents in preparation of this testimony:

- 12 • The Application and the Direct Testimony of the seventeen witnesses for EAI
13 and ITC offered with the Application.
- 14 • The materials provided by EAI and ITC in response to discovery requests
15 issued in this Docket.
- 16 • FERC Dockets EC12-145, EC12-2681, and EL12-107 regarding the joint
17 filing by ITC, Entergy, and MISO: *Joint application for authorization of*
18 *acquisition and disposition of jurisdictional transmission facilities, approval*
19 *of transmission service formula rate and certain jurisdictional agreements,*
20 *and petition for declaratory order on application of section 305(a) of the*
21 *Federal Power Act.*

² "Staff" is used in this testimony to refer to the collective effort of members of the Staff and members of the La Capra Associates project team assisting Staff with this work embodied in this testimony.

- ITC's filings with the U.S. Securities and Exchange Commission related to the Transaction including ITC's S-4 filing on September 25, 2012, S-4 Amendment No. 1 filed on December 2, 2012, S-4 Amendment No. 2 filed on January 29, 2013, S-4 Amendment No. 3 filed on February 20, 2013, and ITC's filing pursuant to SEC rule 424(b)(3) filed on February 27, 2013.
- Testimony, exhibits, hearing transcripts, and Commission Orders in Docket No. 10-011-U related to EAI's application to join MISO.
- The Commission's Order No. 6 in Docket No. 11-050-U regarding the joint application of SWEPCO and AEP Southwestern Transmission Company (SW Transco) for transfer transmission related authorities from SWEPCO to SW Transco.
- The Settlement Agreement and Commission Orders in Docket No. 09-084-U related to EAI's general rate case.

Q. What criteria did you use in your review?

A. During the review, Staff considered the Commission's recent ruling regarding the public interest criteria in the SWEPCO-SW Transco case³ and the Commission's decisions regarding EAI's application to join MISO.⁴

In its August 31, 2012 Order, the Commission articulated a standard of substantial evidence of concrete benefits for ratepayers (in this case, SWEPCO ratepayers).⁵ Staff considered the similarities of that case to the Application in this proceeding in concluding that Staff's review should examine this Application relative to that same standard.

³ Order No. 6, Docket 11-050-U, August 31, 2012.

⁴ Docket No. 10-011-U.

⁵ Order No. 6, Docket 11-050-U, August 31, 2012, at 18-21.

Staff also reviewed the Application to assess the degree of compliance with the conditions established by the Commission regarding EAI's membership in MISO, as set forth in Order Nos. 68, 72, 74, 75 and 76 in Docket No. 10-011-U. In this context, Staff reviewed the proposed structure of TCA/ITC Arkansas and the degree to which ITC ownership would depart from the conditions placed on EAI's membership in MISO.

IV. CONCLUSIONS AND RECOMMENDATIONS

Q. Please summarize Staff's conclusions.

A. The following is a summary of the Staff conclusions:

1. Application as filed does not meet public benefits standard the Commission articulated in the SWEPCO Order

In APSC Docket No. 11-050-U, the Commission articulated that it "is not opposed to independent transmission companies or independent transmission construction and, in fact, it strongly supports the improvement of the transmission system in this state and region as a means to lower energy costs for Arkansas ratepayers."⁶ However, in that same Order the Commission stated that a determination of public interest requires that the applicants provide evidence that the benefits are concrete and "significant enough to outweigh the potential for increased retail rates."⁷

Based on the standard articulated in the SWEPCO docket, the Applicants in this Docket have not demonstrated concrete benefits that outweigh the significant quantitative costs.

⁶ Order No. 6, APSC Docket No. 11-050-U at 21.

⁷ Id.

1 **2. The Transaction imposes significant additional costs to ratepayers**

2 The shift from transmission charges utilizing the Bundled Load exemption to
3 rates under the MISO tariff is expected to result in a significant increase in
4 transmission revenue requirement for Arkansas ratepayers. The shift to ITC
5 ownership adds additional costs based on its capital structure, a higher return on
6 equity, and use of a forward looking test year with an annual true-up provision.
7 In addition, the costs may be even higher if ITC obtains incentive ROE approval
8 and adds transmission investment beyond those known additions included in
9 ITC's cost estimates.

10 The Applicants have provided evidence demonstrating that the Transaction will
11 result in significant increases in transmission charges for both retail ratepayers
12 and wholesale customers in Arkansas. Overall, the change in ownership will
13 result in an increase in annual transmission revenue requirement of between
14 [REDACTED] each year for the first five years. Even if the impact
15 of the forward test year and annual true-up provisions for FERC ratemaking is
16 excluded, as the Applicants propose, the transmission revenue requirement still
17 increases by [REDACTED] over the status quo each year from 2014-2018. This
18 estimate includes offsetting quantitative benefits derived from a purportedly
19 lower cost of debt under ITC and the preservation of the current ADIT and tax
20 basis.

21 The increase will likely be higher, but there is currently insufficient evidence to
22 determine the actual figures because ITC has not provided information on capital
23 expenditures that will accompany additional transmission projects beyond
24 Entergy's current forecast. It is also possible that ITC will seek a higher ROE
25 from FERC in the future, and ITC has expressly stated that it believes it is

1 eligible for an incentive ROE adder. Each of these uncertainties could result in
2 significantly higher rates for Arkansas ratepayers.

3 **3. The Transaction does not yield significant benefits incremental to EAI**
4 **membership in MISO**

5 The benefits of the Transaction identified by the Applicants are primarily
6 qualitative in nature. Many of these benefits, such as ITC's independence and
7 broad regional view, are substantially similar to benefits of EAI joining MISO, or
8 provide only a small incremental benefit over benefits of EAI as a transmission
9 owning member of MISO.

10 Additional benefits claimed by the Applicants, such as the increased financial
11 flexibility, could be achieved through other means that do not impose such a high
12 quantitative cost on ratepayers. The Applicants have not sufficiently
13 demonstrated that other benefits are tangible, such as ITC's singular focus on
14 transmission. While the Applicants also claim that customers will benefit from
15 the independence and broad regional view of ITC, the opportunities for economic
16 transmission upgrades to reduce congestion lay primarily in areas other than
17 Arkansas. Additionally, while this provides for the possibility that costs would
18 be shared beyond the region, it also indicates that EAI could be required to pay
19 for projects in excess of the benefits received.

20 **4. The Transaction will render the Commission's evaluation and conditional**
21 **order in Docket No. 10-011-U obsolete and the APSC will lose jurisdiction**

22 The Commission issued orders in Docket No. 10-011-U to ensure that EAI's
23 transition to MISO was in the public interest. As a result of the Transaction,
24 many of the conditions of MISO membership identified by the Commission in

1 APSC Docket No. 10-011-U that were deemed critical will be voided.
2 Accordingly, the value and impact of the conditions will be altered. As ITC will
3 be primarily operating under FERC jurisdiction, the Commission will lose
4 significant jurisdiction over transmission operations and, most notably,
5 transmission rates charged to Arkansas customers. The loss of the Bundled
6 Load exemption shifts transmission rates out of Commission control, to the
7 benefit of the transmission owner and the detriment of the retail ratepayers.

8 **5. Other issues support Commission rejection of the Transaction**

9 The RMT structure of the Transaction preserves the current ADIT and tax basis
10 of the transmission assets, which simply preserves the status quo with respect to
11 this aspect of the transmission rates, rather than providing a true benefit to
12 ratepayers. The RMT structure also requires the transmission assets of all
13 Entergy Operating Companies be included in the Transaction, putting the
14 Transaction and its purported benefits at risk if any one of the retail regulatory
15 commissions does not approve the Transaction.

16 The safe and reliable delivery of energy to Arkansas customers requires a capable
17 transmission system owner and operator. The Applicants have not provided
18 sufficient evidence to demonstrate that their due diligence concluded that ITC is
19 a qualified and capable transmission system operator.

20 **Q. What is Staff's recommendation?**

21 A. The Application is not in the public interest and should not be approved.

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

23 A. Yes.

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ENTERGY ARKANSAS, INC., MID SOUTH)
TRANSCO LLC, ITC MIDSOUTH LLC,)
TRANSMISSION COMPANY ARKANSAS, LLC,)
AND ITC HOLDINGS CORP. TO ENTER)
TRANSACTIONS RESULTING IN A)
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UTILITY TO OWN EAP'S ELECTRIC)
TRANSMISSION FACILITIES)**

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**DIRECT EXHIBITS
OF
DANIEL E. PEACO
ON BEHALF OF THE GENERAL STAFF OF THE
ARKANSAS PUBLIC SERVICE COMMISSION**

PUBLIC VERSION

APRIL 19, 2013

**EXHIBIT DEP-1****DANIEL E. PEACO****La Capra Associates***President*

Daniel Peaco is an electric industry planning specialist with more than 30 years of experience in power markets and marketing, strategic planning, pricing and price forecasting, power procurement and contracts, and power systems planning. Mr. Peaco has significant experience as an expert witness and as an advisor to senior utility managers and public policy officials. His consulting practice has included a range of engagements relating to integrated resource planning, competitive electric markets and industry restructuring, including generation asset valuation, strategic planning, competitive market formation and pricing, stranded cost assessment and mitigation, power market analysis of prices and supply requirements, power contract analysis, and power procurement practices. In addition to his tenure at La Capra Associates, he has held management and planning positions in power supply planning at Central Maine Power, CMP International Consultants, Pacific Gas & Electric, and the Massachusetts Energy Facilities Siting Council.

EMPLOYMENT HISTORY

La Capra Associates	Boston, MA
<i>President</i>	<i>2002-current</i>
<i>Managing Director</i>	<i>1996-2002</i>
 Central Maine Power Company	 Augusta, ME
<i>Manager, Industrial Marketing and Economic Development</i>	<i>1995-96</i>
<i>Principal, CMP International Consultants</i>	<i>1993-95</i>
<i>Director, Power Supply Planning</i>	<i>1987-93</i>
<i>Power Supply Planning Analyst</i>	<i>1986-87</i>
 Pacific Gas & Electric Company	 San Francisco, CA
<i>Power Supply Planning Analyst</i>	<i>1985-86</i>
<i>Hydropower Planning Analyst</i>	<i>1983-84</i>
<i>Cogeneration Contracts Analyst</i>	<i>1981-82</i>
 Massachusetts Energy Facilities Siting Council	 Boston, MA
<i>Planning Engineer</i>	<i>1978-79</i>

EDUCATION

Thayer School of Engineering, Dartmouth College	Hanover, NH
<i>M.S. in Engineering Sciences, Resource Systems and Policy Design</i>	<i>1981</i>
 Massachusetts Institute of Technology	 Cambridge, MA
<i>B.S. in Civil Engineering, Water Resource Systems</i>	<i>1977</i>

REPORTS AND PRESENTATIONS

Regarding Tri-State G&T's Cost to Serve Its Nebraska Loads and the Nebraska Power Supply Issues Group Loads, prepared for the Nebraska Power Supply Issues Group, two public power districts and two member-owned electric utilities in Western Nebraska. December 2012. Lead Consultant and Principal Author.

Independent Valuation Opinion for the Vernon Station in the Town of Hinsdale, NH, prepared for the Transcanada Hydro regarding the value of a 32 MW hydropower asset. November 2012. Lead Consultant and Principal Author.

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Independent Opinion Regarding the Market Value of Brassua Hydro LP Assets, prepared for the Owners of Brassua Dam regarding the value of a 4 MW hydropower asset. November 2012. Lead Consultant and Principal Author.

Independent Opinion Regarding Amortization Reserve of Brassua Hydro LP, prepared for the Owners of Brassua Dam regarding the amortization reserve value of a 4 MW hydropower asset. November 2012. Lead Consultant and Principal Author.

Regional Framework for Non-Transmission Alternatives, Report prepared for the New England States Committee on Electricity. October 2012. Lead Consultant and Principal Author.

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EXHIBIT DEP-1

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Non-Transmission Alternatives Assessment for the Lewiston-Auburn Area, Report for Central Maine Power. August 27, 2010. Co-Author.

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2010 Comprehensive Plan for the Procurement of Energy Resources, Report prepared for the Connecticut Energy Advisory Board. April 27, 2010. Lead Consultant and Principal Author.

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2008 Comprehensive Plan for the Procurement of Energy Resources, Report prepared for the Connecticut Energy Advisory Board. August 1, 2008. Lead Consultant and Principal Author.

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Technical Audit: Purchased Power Budget April 2005 – March 2006, prepared for the New Brunswick Power Distribution and Customer Service Corp., May 18, 2005. Lead Consultant and Principal Author.

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Preliminary Market Value Assessment of PP&L Maine Hydroelectric Plants, August 2001. Proprietary report prepared for American Rivers, the Atlantic Salmon Federation, the Natural Resources Council of Maine, the Penobscot Indian Nation, and Trout Unlimited. Principal Author.

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Wholesale Market Development: Timing and Issues Survey of Activity in Other Regions, FERC Initiatives, In The Matter of a Progress Report to the Arkansas General Assembly on the Development of Competition in Electric Markets and the Impact, if any, on Retail Consumers, Docket No. 00-190-U, September 29, 2000. Principal Author.

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EXPERT TESTIMONY AND APPEARANCES

<u>Forum</u>	<u>Client</u>	<u>Topic</u>
US District Court Colorado Civil Action No. 10-CV-02349-WJM-KMT	Nebraska Power Supply Issues Group	Expert testimony regarding Tri-State G&T cost to serve five Nebraska members. Deposition Testimony February 27, 2013
Arbitration AAA Case No. 11 153 Y 02133 11	Owners of Brassua Dam FPL Hydro Maine LLP Madison Paper Industries Merimil Ltd Partnership	Expert testimony regarding the valuation of a 4 MW hydropower facility and the determination of amortization reserve obligations under FERC license provisions. Valuation Report November 1, 2012 Amortization Reserve Report November 1, 2012 Amortization Reserve Rebuttal November 15, 2012 Oral Testimony December 5, 2012
Burrillville Board of Review	Transcanada; Ocean States Power Holdings, Ltd..	Expert testimony regarding the valuation of a 540 MW combined cycle power plant in appeal of an appraisal conducted for the Town of Burrillville, RI. Valuation Report January 4, 2012 Oral Testimony March 1, 2012
Arkansas Public Service Commission Docket No. 10-011-U	General Staff of the AK Public Service Comm.	Testimony regarding the evaluation of Entergy Arkansas's strategic reorganization options and request for authorization to transfer control of its transmission asset to the Midwest ISO. Oral Testimony May 31, 2012 Surrebuttal Testimony April 27, 2012 Direct Testimony March 16, 2012
Burrillville Board of Review	Transcanada; Ocean States Power Holdings, Ltd..	Expert testimony regarding the valuation of a 540 MW combined cycle power plant in appeal of an appraisal conducted for the Town of Burrillville, RI. Valuation Report January 4, 2012 Oral Testimony March 1, 2012
Oklahoma Corporation Commission Cause No. PUD 201100186	OK Corporation Commission OK Attorney General	Testimony regarding a 60 MW Wind Energy Purchase Agreement and Cogeneration deferral Agreement proposed by Oklahoma Gas & Electric Company, addressing cost pre-approval, and a requested waiver from competitive procurement. requirements. Prefiled Testimony February 8, 2012
Arkansas Public Service Commission Docket No. 10-011-U	General Staff of the AK Public Service Comm.	Testimony regarding the evaluation of Entergy Arkansas's strategic reorganization options upon its exit from the Entergy System Agreement. Oral Testimony September 9, 2011 Surrebuttal Testimony August 18, 2011 Supplemental Initial Testimony July 12, 2011 Initial Testimony February 11, 2011

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State Corporation Commission of the State of Kansas	The Landowner Group	Testimony regarding the application of ITC Great Plains for a siting permit for a 345-kV Transmission Line addressing project need and route selection methodology. Initial Testimony April 18, 2011
Federal Energy Regulatory Commission (FERC) RM10-23-000	Maine Public Utilities Commission, et. al.	Expert Affidavit regarding economic analysis methodology for transmission project evaluation. Provided in reply comments on the FERC Transmission Planning and Cost Allocation NOPR. Affidavit November 12, 2010
Maine Public Utilities Commission Docket No. 2008-255	Central Maine Power	Testimony regarding CMP's application for approval the Lewiston Loop 115kV Transmission Project. Testimony addressed non-transmission alternatives. Oral Testimony November 16, 2008 December 14, 2010 Rebuttal Testimony November 8, 2010 August 27, 2010
Oklahoma Corporation Commission Cause No. PUD 201000092	OK Corporation Commission OK Attorney General	Testimony regarding a 99.2 MW wind farm power purchase agreement and green energy choice tariff proposed by Public Service Company of Oklahoma, addressing cost pre-approval, resource need, and competitive procurement. requirements.. Prefiled Testimony October 5, 2010 Oral Testimony November 3, 2010
Oklahoma Corporation Commission Cause No. PUD 201000037	Oklahoma Attorney General	Testimony regarding a 198 MW wind farm proposed by Oklahoma Gas & Electric, addressing cost pre-approval, resource need, and competitive procurement. requirements. Prefiled Testimony June 11, 2010
Connecticut Dept. of Public Utilities Control (DPUC) Docket No. 10-02-07	Connecticut Energy Advisory Board (CEAB)	Lead witness sponsoring the CEAB's 2010 <i>Comprehensive Plan for the Procurement of Energy Resources</i> . Oral Testimony June 2 & 3, 2010
Georgia Public Service Commission Docket No. 31081	Georgia Public Service Commission Public Interest Advocacy Staff	Witness sponsoring testimony regarding integrated resource planning methods, renewable energy, solar PV demonstration projects, and uncertainty analysis. Written Testimony May 7, 2010 Oral Testimony May 18, 2010

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Maine Public Utilities Commission Docket No. 2008-255	Central Maine Power	Testimony regarding CMP's application for approval \$1.5 B Maine Power Reliability Transmission Project. Testimony addressed non-transmission alternatives and economic benefits, economics of proposed solar alternative, wind energy development benefits. Oral Testimony October 10, 2008 November 19, 2008 December 21, 2009 February 4, 2010 Rebuttal Testimony December 4, 2009 April 3, 2009
Oklahoma Corporation Commission Cause No. PUD 200900167	Oklahoma Attorney General	Testimony regarding a 102 MW wind farm proposed by Oklahoma Gas & Electric, addressing cost pre-approval, resource need, and competitive procurement. requirements. Prefiled Testimony Sept 29, 2009
Oklahoma Corporation Commission Cause No. PUD 200900099	Oklahoma Industrial Energy Consumers (OIEC)	Testimony regarding a power contract pre-approval and recovery of Independent Evaluator costs of Public Service Company of Oklahoma. Prefiled Testimony July 14, 2009
Connecticut Dept. of Public Utilities Control (DPUC) Docket No. 09-05-02	Connecticut Energy Advisory Board (CEAB)	Lead witness sponsoring the CEAB's <i>2009 Comprehensive Plan for the Procurement of Energy Resources</i>. Oral Testimony June 30, 2009
Connecticut Dept. of Public Utilities Control (DPUC) Docket No. 08-07-01	Connecticut Energy Advisory Board (CEAB)	Lead witness sponsoring the CEAB's <i>2008 Comprehensive Plan for the Procurement of Energy Resources</i>. This Plan is the first prepared under the State's new integrated resource planning statute. Oral Testimony August 28, 2008 September 22, 2008 October 3, 2008
Maine Superior Court Civil Action Docket No. cv-06-705	Worcester Energy Co., Inc.	Expert opinion regarding renewable energy and power procurement services. Prefiled Report January 30, 2008 Oral Testimony March 18, 2009
Massachusetts Dept. Of Telecommunications And Energy Docket No. DTE/DPU-06-60	Russell Biomass	Testimony regarding economic, reliability and environmental need for renewable power in the Massachusetts and New England in support of Russell Biomass petition for a zoning exemption. Prefiled Testimony June 2007 Oral Testimony October 30, 2007

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Hawaii Public Utilities Commission Docket No. 04-0046	Hawaii Division of Consumer Advocacy	Testimony regarding Hawaii Electric Light Company's integrated resource plan. Prefiled Testimony September 28, 2007 Oral Testimony November 26, 2007
Nevada Public Utilities Commission Docket No. 06-12002	Nevada Attorney General Bureau of Consumer Protection	Testimony regarding the prudence of Sierra Pacific Power Company in its purchased power expenses for the period December 2001 through November 2002. Prefiled Testimony September 14, 2007
Oklahoma Corporation Commission Cause No. PUD 2005516 Cause No. PUD 2006030 Cause No. PUD 2007012	Oklahoma Attorney General	Testimony regarding a 950 MW coal-fired generation facility proposed by Public Service of Oklahoma and Oklahoma Gas & Electric, including IRP, competitive procurement, and construction financing issues. Prefiled Testimony May 21, 2007 Rebuttal Testimony June 18, 2007 Oral Testimony July 26, 2007
Oklahoma Corporation Commission Cause No. PUD 2002-038 REMAND	Oklahoma Industrial Energy Consumers (OIEC)	Testimony regarding a power contract proposal of Lawton Cogeneration and the pricing analysis of Public Service Company of Oklahoma. Prefiled Testimony October 28, 2005 Rebuttal Testimony March 17, 2006 Oral Testimony May 9, 2006
New Brunswick Board of Commissioners of Public Utilities (PUB) Ref: 2005-002	New Brunswick Power Distribution Company	Testimony regarding La Capra Associates' three technical audits of the NBP-Disco purchased power budget and variance analyses for FY 2004 – 2006. Oral Testimony February 14-22, 2006
Connecticut Department of Public Utility Control Docket No. 05-07-14 Phases I and II	Connecticut Energy Advisory Board	Testimony regarding Connecticut's need for electric capacity to meet reliability requirements and to mitigate congestion charges in the wholesale markets. Oral Testimony February 14-22, 2006 May 1, 2006 June 15, 2006 September 26, 2005
Hawaii Public Utilities Commission Docket No. 03-0372	Hawaii Division of Consumer Advocacy	Testimony regarding competitive bidding rules and integrated resource planning. Oral Testimony December 12-16, 2005
Oklahoma Corporation Commission Cause No. PUD 2005-151	Oklahoma Industrial Energy Consumers (OIEC)	Testimony regarding resource planning, prudence of generation investment of Oklahoma Gas & Electric Company. Prefiled Testimony September 12, 2005 Rebuttal Testimony September 29, 2005 Oral Testimony October 18, 2005

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Oklahoma Corporation Commission Cause No. PUD 2003-076	Oklahoma Industrial Energy Consumers (OIEC)	Testimony regarding resource planning, prudence of generation investment and fuel and purchased power expenses of Public Service Company of Oklahoma. Prefiled Testimony January 4, 2005
Oklahoma Corporation Commission Cause No. PUD 2003-633/4	Oklahoma Industrial Energy Consumers (OIEC)	Testimony regarding power contract proposal for Blue Canyon wind development and avoided costs of Public Service Company of Oklahoma. Prefiled Testimony August 16, 2004
Civil Litigation Maine Superior Court Docket No. CV-01-24	Central Maine Power Co.	Factual and expert witness in litigation regarding pricing provisions of a purchased power agreement between Central Maine Power and Benton Falls Associates. Deposition Testimony April 28, 2004
Oklahoma Corporation Commission	Oklahoma Attorney General	Testimony regarding power contract proposal for PowerSmith Cogeneration and avoided cost analysis of Oklahoma Gas & Electric Company. Prefiled Testimony February 18, 2004 Rebuttal Testimony March 16, 2004 Oral Testimony August 4, 2004
Nevada Public Utilities Commission	Nevada Attorney General Bureau of Consumer Protection	Testimony regarding the Nevada Power Company's Integrated Resource Plan and associated financial plan. Prefiled Testimony September 19, 2003 Oral Testimony October 15, 2003
Massachusetts Energy Facilities Siting Council Docket No. EFSB-02-2	Cape Wind	Testimony regarding economic, reliability and environmental need for power in the Massachusetts and New England power markets regarding the need for new wind power facility. Prefiled Testimony February 14, 2003 Oral Testimony August 6&7, 2003
Maine State Board of Property Tax Review	United American Hydro	Testimony regarding the Maine and New England power market prices pertaining to the valuation of a hydro-electric power facility in Winslow, Maine. Oral Testimony June 18, 2003
Nevada Public Utilities Commission Docket No. 03-1014	Nevada Attorney General Bureau of Consumer Protection	Testimony regarding the prudence of Sierra Pacific Power Company in its purchased power expenses for the period December 2001 through November 2002. Prefiled Testimony April 25, 2003
Oklahoma Corporation Commission Cause No. PUD 2002-038	Oklahoma Attorney General	Testimony regarding a power contract proposal of Lawton Cogeneration and the pricing analysis of Public Service Company of Oklahoma. Prefiled Testimony December 16, 2002 Oral Testimony May 22, 2003
Arkansas Public Service Commission	General Staff of the AK Public Service Comm.	Testimony regarding the Development of Competition in Electric Markets and the Impact on Retail Consumers in Arkansas. Prefiled Testimony September 4, 2001

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Arkansas Public Service Commission	General Staff of the AK Public Service Comm.	Testimony regarding the Development of Competition in Electric Markets and the Impact on Retail Consumers in Arkansas. Prefiled Testimony September 29, 2000
Arkansas Public Service Commission	General Staff of the AK Public Service Comm.	Testimony regarding the establishment of uniform Policies and guidelines for a Standard Service Package. Staff Proposal and Comments June 13, 2000 Reply Comments July 21, 2000 Sur reply Comments August 2, 2000 Oral Testimony August 8, 2000 Petition for Rehearing Rebuttal Testimony November 15, 2000 Oral Testimony November 29, 2000
Arkansas Public Service Commission	General Staff of the AK Public Service Comm.	Testimony regarding the determination of the merits of declaring retail billing services competitive effective At the start of retail open access. Oral Testimony June 27, 2000 Prefiled Rebuttal Testimony June 23, 2000 Prefiled Testimony June 16, 2000 Oral Testimony May 10, 2000
Arkansas Public Service Commission	General Staff of the AK Public Service Comm.	Testimony regarding the minimum filing requirements for market power studies to be filed by the Arkansas Electric utilities and affiliated retail companies. Oral Testimony June 1, 2000
Amer. Arb. Assoc. No. 50T 198 00197-98	Vermont Joint Owners	Testimony regarding economic damages resulting from alleged breach of a long-term purchase power agreement between Hydro-Quebec and Vermont utilities (VJO). Oral Testimony May 25, 2000 Prefiled Rebuttal Testimony February 10, 2000 Prefiled Testimony August 13, 1999
Rhode Island Energy Facilities Siting Board	Indeck-North Smithfield, L.L.C.	Testimony regarding economic, reliability and environmental need for power in the Rhode Island and New England power markets regarding the need for new, merchant power facility. Prefiled Testimony August 16, 1999 Oral Testimony August 17, 2000 Prefiled Testimony January 26, 2001 Oral Testimony March 23, 2001
Civil Litigation Maine Superior Court Docket No. CV-98-212	Central Maine Power Co.	Factual and expert witness in litigation regarding pricing provisions of a purchased power agreement between Central Maine Power and Regional Waste Systems. Deposition Testimony May 5, 1999
Connecticut Energy Facilities Siting Council Docket No. 190	PDC – El Paso Meriden LLC	Testimony regarding economic, reliability and environmental need for power in the Connecticut and New England power markets regarding the need for new, merchant power facility. Prefiled Testimony January 25, 1999

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Rhode Island Energy Facilities Siting Council Docket No. SB-98-1	R. I. Hope Energy, L. P.	Testimony regarding economic, reliability and environmental need for power in the Massachusetts and New England power markets regarding the need for new, merchant power facility. Oral Testimony November 4, 1998 Prefiled Testimony October 30, 1998
Massachusetts Energy Facilities Siting Council Docket No. EFSB-91-101A	Cabot Power Corp.	Testimony regarding economic, reliability and environmental need for power in the Massachusetts and New England power markets regarding the need for new, merchant power facility. Oral Testimony May 27, 1998 Prefiled Testimony August 15, 1997
Massachusetts Energy Facilities Siting Council Docket No. EFSB-97-2	ANP Blackstone Energy	Testimony regarding economic, reliability and environmental need for power in the Massachusetts and New England power markets regarding the need for new, merchant power facility. Oral Testimony April 6, 1998 Prefiled Testimony January 23, 1998
Massachusetts Energy Facilities Siting Council Docket No. EFSB-97-1	ANP Bellingham	Testimony regarding economic, reliability and environmental need for power in the Massachusetts and New England power markets regarding the need for new, merchant power facility. Oral Testimony February 3, 1998 January 28, 1998
Rhode Island Energy Facilities Siting Board Docket No. SB-97-1	Tiverton Power Associates LP	Testimony regarding economic, reliability and environmental need for power in the Rhode Island and New England power markets regarding the need for new, merchant power facility. Oral Testimony October 15, 1997 Prefiled Testimony October 1, 1997
Maine Public Utilities Commission Docket No. 92-102	Central Maine Power	Testimony regarding CMP's avoided cost methods and practices pertaining to the prudence of power purchase contract decisions with regard to contract awards and contract management. Oral Testimony July 1993 Deposition Testimony February 25, 1993 March 1, 1993 Prefiled Rebuttal Testimony June 7, 1993 Prefiled Testimony June 15, 1992
Maine Public Utilities Commission Docket No. 92-315	Central Maine Power	Testimony regarding CMP's avoided cost methods and practices pertaining to the setting of long-term avoided costs, CMP's Energy Resource Plan, and the relationship of marginal costs of generation to embedded costs. Supplemental Prefiled Testimony April 20, 1993 Prefiled Testimony February 17, 1993
Maine Public Utilities Commission Docket No. 87-261 Docket No. 88-111	Central Maine Power	Testimony regarding CMP's avoided cost methods and practices pertaining to the setting of long-term avoided costs, CMP's Energy Resource Plan, and the proposal for a 900 MW power Contract with Hydro Quebec. Oral Testimony Summer 1988 Prefiled Testimony October 31, 1987

**BEFORE THE
ARKANSAS PUBLIC SERVICE COMMISSION**

**IN THE MATTER OF AN APPLICATION OF)
ENTERGY ARKANSAS, INC., MID SOUTH)
TRANSCO LLC, ITC MIDSOUTH LLC,)
TRANSMISSION COMPANY ARKANSAS, LLC,)
AND ITC HOLDINGS CORP. TO ENTER)
TRANSACTIONS RESULTING IN A)
CERTIFICATE OF PUBLIC CONVENIENCE)
AND NECESSITY FOR A NEW ARKANSAS)
UTILITY TO OWN EAP'S ELECTRIC)
TRANSMISSION FACILITIES)**

DOCKET NO. 12-069-U

EXHIBIT DEP-2

TECHNICAL REPORT

**EVALUATION OF THE TRANSACTION TO
TRANSFER THE ENTERGY CORP. TRANSMISSION BUSINESS
TO ITC HOLDINGS, INC.**

PUBLIC VERSION

**EVALUATION OF THE
TRANSACTION TO TRANSFER
THE ENTERGY CORP.
TRANSMISSION BUSINESS TO
ITC HOLDINGS, INC.**

La Capra Associates

Docket No. 12-069-U

PUBLIC VERSION

PREPARED FOR

General Staff of the Arkansas
Public Service Commission

PREPARED BY

La Capra Associates, Inc.
One Washington Mall, 9th Floor
Boston, MA 02108

Technical Report

April 19, 2013

TECHNICAL REPORT

Evaluation of the Transaction to Transfer the Entergy Corp. Transmission Business to ITC Holdings, Inc.

Docket No. 12-069-U

In The Matter Of An Application Of Entergy Arkansas, Inc., Mid South TransCo LLC,
ITC Midsouth LLC, Transmission Company Arkansas, LLC, and ITC Holdings Corp.
To Enter Transactions Resulting In A Certificate Of Public Convenience And Necessity
For A New Arkansas Utility To Own EAI's Electric Transmission Facilities

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- ATTACHMENT 2: ITC'S PUBLIC RESPONSES TO DATA REQUESTS
- ATTACHMENT 3: EAI'S PROTECTED RESPONSES TO DATA REQUESTS
- ATTACHMENT 4: ITC'S PROTECTED RESPONSES TO DATA REQUESTS

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ACRONYMS/ABBREVIATIONS

ACRONYMS/ABBREVIATIONS	
APSC	Arkansas Public Service Commission
CAOL	Current, Accrued, and Other Liabilities
ESI	Entergy Services, Inc.
FERC	Federal Energy Regulatory Commission
ICT	Independent Coordinator of Transmission
LSE	Load-Serving Entity
METC	Michigan Electric Transmission Company
MISO	Midwest Independent Transmission System Operator
MTEP	MISO Transmission Expansion Plan/Planning
MVP	Multi-Value Project
NPV	Net Present Value
OATT	Open Access Transmission Tariff
OpCo	Entergy Operating Company
RMT	Reverse Morris Trust
ROE	Return on Equity
RTO	Regional Transmission Organization
SPP	Southwest Power Pool
TCA	Transmission Company Arkansas
TO	Transmission Owner
TOA	Transmission Owner's Agreement
WACC	Weighted Average Cost of Capital

1. INTRODUCTION

On September 28, 2012, Entergy Arkansas, Inc. (“EAI”) and ITC Holdings Corp. (“ITC”) submitted an Application containing their proposal to enter into a series of transactions (collectively, the “Transaction”), calling for the transfer of EAI’s transmission assets and associated transmission operations to Transmission Company Arkansas (“TCA”), a spin-off of TCA to Mid South TransCo, and subsequently a merger of Mid South TransCo with ITC Midsouth LLC (“ITC Midsouth”), a subsidiary of ITC.¹ As a result of the Transaction, TCA will be an operating subsidiary of ITC Midsouth and ITC, providing transmission services in Arkansas with no affiliation to EAI or Entergy.

The Transaction also includes a transfer of the generation and distribution functions of EAI to Entergy Arkansas LLC, which will remain an operating subsidiary of Entergy. Energy Arkansas LLC will be an operating subsidiary of a new holding company which will operate as a first-tier subsidiary of Entergy. Collectively herein, EAI, ITC, ITC Midsouth, Mid South TransCo and TCA will be referred to as “Applicants.”

The Transaction includes similar actions by all Entergy Operating Companies (“OpCos”). All Entergy transmission operations will become affiliated operating subsidiaries of ITC Midsouth. The remaining generation and distribution functions of all Entergy Operating Companies (including EAI) will be operating subsidiaries of a new holding company that will be a direct subsidiary of Entergy Corp.

The Applicants seek (1) a number of approvals from the Commission² regarding the transfer of ownership of the EAI transmission assets to TCA, (2) the transfer of TCA ownership to Mid South TransCo and then to ITC Midsouth, and (3) the authority for TCA to operate as a public utility in Arkansas. In addition to these requested actions by the Commission, the Transaction requires similar approvals from other jurisdictions for the transfer of transmission assets from the other Entergy Operating Companies, which are proposed to occur in parallel with the EAI and TCA transfers.

This report presents the results of Staff’s review of the Application and materials supplied by the Applicants in responses to discovery, as well as Staff’s findings regarding the Applicants’ evidence supporting its request for approval of the Transaction. Staff conducted its review of the Application focusing on the specific implications for EAI and EAI’s retail and wholesale customers in Arkansas and the extent to which the Transaction offers

¹ The Application was filed on behalf of EAI, ITC, ITC Midsouth, and two other entities: Mid South Transco LLC (“Mid South Transco”), which is a temporary entity created by Entergy and would later be merged into ITC Midsouth as a result of the proposed Transaction. Transmission Company Arkansas, LLC (“TCA”) is an entity created by EAI to receive the spun-off EAI transmission assets. TCA is proposed to be renamed ITC Arkansas subsequent to completion of the Transaction.

² Application pp. 6-9, 50-55, 63-64.

concrete benefits to EAI ratepayers such that a finding that the transaction is in the public interest could be supported and justified.³ Based on this review, Staff finds that:

1. The Transaction would result in significant and tangible added costs to retail and wholesale ratepayers in Arkansas.
2. The Transaction would not provide significant or tangible benefits to Arkansas beyond the benefits that are expected to derive from EAI's membership in Midwest Independent Transmission System Operator ("MISO").
3. The Transaction would reduce the Commission's jurisdiction over the transmission system that is currently owned and operated by EAI and would obviate many of the conditions on MISO membership established by the Commission in Docket No. 10-011-U.
4. The other benefits claimed by the Applicants are not quantified or concrete, and could be attained through other mechanisms.
5. The Reverse Morris Trust ("RMT") structure of the Transaction preserves the current ADIT and tax basis of the transmission assets, which simply preserves the status quo with respect to this aspect of the transmission rates, rather than providing a true benefit to ratepayers. The RMT structure also requires the transmission assets of all Entergy Operating Companies be included in the Transaction, putting the Transaction and its purported benefits at risk if any one of the retail regulatory commissions does not approve the Transaction.
6. The Applicants have not provided evidence necessary to establish ITC's competency to operate the EAI transmission system in Arkansas, specifically, or the new entity that combines all the Entergy transmission system with the current ITC.

This report discusses each of these findings in the sections that follow.

Given that Staff's review concludes that the Application is not in the public interest, Staff has not developed a detailed review of the issues pertaining to the manner of implementing the transition to ITC ownership and structuring of the new entities (i.e., Entergy Arkansas LLC and ITC Arkansas), including:

- EAI employees transferring to ITC
- the implementation of the integration to MISO
- the status of ITC/ITC Arkansas as public utility in Arkansas
- the applicability of Commission imposed conditions to ITC Arkansas,
- the reorganization of EAI to Entergy Arkansas LLC, and
- ITC's approach to planning and cost allocation.

³ In SWEPCO's application regarding SW Transco, the Commission discussed the need for substantial evidence that the benefits outweigh the costs of that proposal and that the evidence demonstrated that the benefits to ratepayers are concrete. Order No. 6 at 18-19, August 31, 2012, Docket No. 11-050-U (August 31, 2012).

2. PROPOSED CHANGES TO ARKANSAS TRANSMISSION SERVICE

The proposed Entergy-ITC Transaction would transfer the Entergy transmission business to ITC. As part of this Transaction, EAI and each of the other Entergy Operating Companies would be restructured as generation and distribution subsidiaries of Entergy. The transmission business of EAI and each of the other Entergy Operating Companies would be restructured to operate as separate transmission subsidiaries of ITC. This section of the report addresses the overall goals and process for the proposed Transaction and describes the elements of the Transaction that are specific to EAI and Arkansas.

A. Overall Entergy-ITC Transaction Objectives and Process

The Transaction is actually a complex series of transactions within the Entergy organization and ultimately with ITC. The Entergy organizational transactions culminate with all current Entergy transmission assets being spun off as a separate transmission company (Mid South TransCo) to the Entergy shareholders. Entergy shareholders merge Mid South TransCo with ITC Midsouth and receive ITC common stock. Upon completion of this transaction, the former Entergy transmission business would become an ITC subsidiary completely independent and separate from the Entergy organization. The Entergy shareholders remain owners of Entergy and also hold ownership positions in ITC.

Discussion of the Transaction with ITC was initiated by Entergy in June 2011 and ITC provided a non-binding indication of interest letter to Entergy on July 1, 2011.^{4,5} Entergy and ITC publicly announced their plans for the Transaction on November 21, 2011⁶ and entered into a formal agreement to transfer ownership of Entergy's transmission assets on December 4, 2011.⁷ [REDACTED]

⁴ Amendment No. 1 to Form S-4 filed with the U.S. Securities and Exchange Commission by ITC Holdings Corp. (December 3, 2012), p. 118. Produced by ITC in response to Staff Data Request APSC 15-7.

⁵ [REDACTED] See HSPI Attachment to EAI's Response to Staff Data Request APSC 11-1, Addendum 2. "HSPM Dec 2 2011 Entergy Corp Board Presentation Materials", p. 4/408. See also HSPI Attachment to EAI's Response to Staff Data Request APSC 17-1, Addendum 1. "Attachment 17-2e Addendum1_HSPI_ITC_10 14 10_v1_HSPI.PDF."

⁶ Entergy-ITC Press Release, "Entergy to Divest and Merge Electric Transmission Business Into ITC Holdings, Creating Industry-Leading Electric Transmission Company," November 21, 2011, <http://www.itc-holdings.com/itc-entergy/news/breaking-news/press-release.html>.

⁷ Application, p. 2.

[REDACTED]

In the Application, Entergy describes this Transaction as the culmination of more than a decade of effort to form an effective Transco for the Entergy system, including various Transco proposals and the operation of its transmission system under the Independent Coordinator of Transmission ("ICT") structure as administered by the Southwest Power Pool ("SPP").⁹ Entergy determined that separation of its transmission business was the best way to realize the full value of its businesses.¹⁰ The strategic rationale presented to Entergy's Board when the Transaction was approved included:¹¹

[REDACTED]

With respect to the benefits to customers, the Application stresses the benefits of a robust transmission system, including greater confidence in wholesale markets derived from an independent transmission owner, enhanced financial strength for the transmission system and the Entergy Operating Companies, improved transmission service derived from ITC's singular focus on transmission, ITC's regional view of transmission planning, and the elimination of EAI's transmission planning, which would have to be performed in conjunction with the other Entergy Operating Companies.¹²

The Transaction is structured as a RMT transaction, defined as:

A Reverse Morris Trust transaction is a business combination involving the spin- or split-off of a business (here, Entergy's Transmission Business), by a company (here, Entergy), and its subsequent merger with another company (here, ITC). Entergy's proposal would be structured on a tax free basis where shareholders of the company effecting the spin-

⁸ EAI's Response to Staff Data Request APSC 17-2, "Attachment 17-2.2_HSPI_110725 Process Update_HSPI.PDF" pp. 4-10.

⁹ Application at 22-25; Direct Testimony of Hugh T. McDonald (September 28, 2012) at 27-30.

¹⁰ Amendment No. 1 to Form S-4 filed with the U.S. Securities and Exchange Commission by ITC Holdings Corp. (December 3, 2012), p. 147. Produced by ITC in response to Staff Data Request APSC 15-7.

¹¹ HSPI Attachment to EAI's Response to Staff Data Request APSC 11-1, Addendum 2. "HSPM Dec 2 2011 Entergy Corp Board Presentation Materials", p. 5/408.

¹² Application at 26.

or split-off (here, the Entergy shareholders) receive more of the equity in the combined company than the shareholders of the other company (here, the ITC shareholders).¹³

Entergy proposed that the Transaction be structured as a RMT Transaction to accomplish the Transaction on a tax-free basis for its shareholders, electing this structure rather than a straight asset sale.¹⁴ However, the RMT Transaction results in a complete separation of the transmission business from Entergy and its Operating Companies just as would be the case in a straight asset sale to ITC. At the conclusion of the RMT, Entergy shareholders would have ownership in ITC and ITC would own the Mid South TransCo assets outright and independent from Entergy and its operating companies. ITC has estimated that the total net consideration transferred from ITC to Entergy shareholders will be approximately \$3.56 billion at the time of execution, including 50.1% of ITC common shares. In return, ITC will receive the entire Entergy transmission business enterprise valued by ITC at \$3.56 billion. This includes \$2.40 billion in excess of the net book value of the enterprise, which will be booked by ITC as goodwill.¹⁵

The individual steps of the Transaction are detailed in the testimony of EAI witness Theodore Bunting.¹⁶ In general, the Transaction steps are:

1. Entergy forms Mid South TransCo, a new subsidiary which will become the holding company for individual wires subsidiaries created by each Entergy OpCo.
2. Each OpCo creates a wires subsidiary which will eventually hold the transmission assets of that OpCo. For EAI, this wires subsidiary is TCA.
3. Entergy Corp. borrows \$575 million from capital markets. This money will be used to provide capital infusions to the OpCos to retire OpCo debt and outstanding preferred shares.
4. The wires subsidiaries, still owned by the OpCos, collectively borrow \$1.2 billion from capital markets. TCA's share of the total is \$400 million.
5. The wires subsidiaries will distribute the cash borrowed in the previous step to their respective OpCos, and the OpCos will contribute the transmission assets to the wires subsidiaries. The assets will be transferred to the wires subsidiaries at book value and the cash will be used by the OpCos to pay down debt related to the transmission assets.

¹³ Amendment No. 1 to Form S-4 filed with the U.S. Securities and Exchange Commission by ITC Holdings Corp. (December 3, 2012), p. 120. Produced by ITC in response to Staff Data Request APSC 15-7.

¹⁴ Id. at 118-120. See also EAI's Response to Staff Data Request APSC 16-13.

¹⁵ ITC's filing pursuant to SEC Rule 424(b)(3), February 28, 2013, pp. 46, 49. This document revises portions of ITC's S-4 filing cited above. The revised filing has not been produced by the Applicants in this matter, but is publicly available at: www.sec.gov/Archives/edgar/data/1317630/000119312513078606/d389849d424b3.htm

¹⁶ Direct Testimony of Theodore H. Bunting, Jr. (September 28, 2012) pp. 34-37, Exhibit THB-2.

The preceding overview is a high-level description of the key steps of the Transaction. There are additional steps related to the treatment of stock, the establishment of a trust to receive some of the shares, and other issues which are relevant for the tax accounting of the Transaction.

B. EAI Restructuring in the Transaction

As part of the Transaction outlined above, EAI would be restructured into a generation and distribution company, with its current transmission assets and operations being spun off into a separate transmission company, TCA. This section of the report describes the proposed changes in EAI, the creation of TCA, and the exchange of assets between EAI and Entergy proposed in the Transaction.

Currently, EAI is a vertically integrated utility owning generation, transmission and distribution assets which it uses to serve its retail load and its wholesale customers. EAI's total assets have a net book value of [REDACTED], with its transmission assets being approximately [REDACTED] of that value.¹⁷ EAI holds [REDACTED] in debt and has approximately [REDACTED] in equity, including approximately [REDACTED] in preferred stock outstanding, for an overall debt/equity ratio of [REDACTED].¹⁸

The Transaction would remove the [REDACTED] in transmission assets from EAI and provide \$585 million in capital to EAI from Entergy (\$185 million in two parts) and TCA (\$400 million). At the end of the Transaction, EAI would have assets with a total net book value of [REDACTED], holding [REDACTED] in debt and [REDACTED] in equity, with a debt/equity ratio similar to the pre-Transaction amounts.¹⁹

17 The net book value of the assets is distinct and separate from the tax basis of the assets, which includes an adjustment for accumulated deferred income taxes (ADIT).

¹⁸ Attachment to EAI's Response to Staff Data Request APSC 34-2.

19 *Id.*

TCA is proposed to initially be established as an EAI subsidiary and, once formed, ownership of TCA is to be transferred to Entergy, effectively as a dividend. As an EAI subsidiary, EAI is proposed to transfer its transmission assets to TCA. TCA borrows \$400 million and transfers the proceeds from that loan to EAI. The resulting structure of TCA includes assets with net book value of [REDACTED] and debt of \$400 million, with a net book value of [REDACTED].²⁰

The Transaction calls for EAI to retire debt totaling approximately [REDACTED] and to purchase and retire all outstanding preferred shares of EAI totaling [REDACTED]. The Transaction is designed to maintain the pre-Transaction proportion of debt to total equity of EAI, as well as those of the other OpCos. At the conclusion, EAI will have [REDACTED] in debt and [REDACTED] in equity, a [REDACTED] debt/equity ratio.²¹

The impact of the Transaction on the capitalization of EAI and TCA is addressed in Table 1 below.

TABLE 1. IMPACT OF TRANSACTION ON EAI CAPITALIZATION, ASSETS²²

TRANSACTION STEP	EAI		
	Debt	Equity	Preferred
Beginning capital structure	[REDACTED]	[REDACTED]	[REDACTED]
EAI redeems all preferred shares	-	-	[REDACTED]
TCA borrows \$400m from capital markets	-	-	-
EAI exchanges T assets for cash from TCA	-	-	-
EAI receives cash from Entergy's debt issuance	-	[REDACTED]	-
EAI receives additional cash infusion from Entergy	-	[REDACTED]	-
EAI retires historical debt	[REDACTED]	-	-
EAI gives ownership of TCA (\$0.43B, net of \$0.40B debt and \$0.83B T assets) to Entergy	-	[REDACTED]	-
Final capital structure	[REDACTED]	[REDACTED]	-

As proposed, EAI will continue to be the load serving entity for its Arkansas load. According to the Applicants, the change in ownership of the transmission assets will have little, if any,

²⁰ Id.

²¹ Id.

²² Id.

impact on the day-to-day experience of EAI's retail customers, and with the exception of certain large industrial customers, the retail customers of EAI will have no direct involvement with ITC.²³

C. TCA Transfer from Entergy to ITC Arkansas

As discussed in the Transaction overview above, TCA will initially be created as a wholly-owned subsidiary of EAI. After TCA issues \$400 million of debt, the proceeds of that loan will be distributed to EAI. The EAI transmission assets will be transferred to TCA. At this point in the restructuring, EAI will have received \$400 million in cash and will have sole ownership of TCA, which will have \$400 million in debt and will have direct ownership of the EAI transmission business.

Following the restructuring of TCA as a Transco subsidiary of EAI, EAI is to distribute all membership units of TCA to Entergy Corp., transferring ownership of the transmission business to the parent company.

Entergy then contributes all membership units to Mid South TransCo, which at this point in the restructuring is a direct subsidiary of Entergy, holding the transmission assets received from EAI and the other Entergy Operating Companies as separate subsidiaries.

Once Entergy declares a dividend and distributes all membership units of Mid South TransCo to its shareholders, TCA will effectively be owned by the Entergy shareholders.

Immediately after this spin-off to the Entergy shareholders, the merger of Midsouth TransCo with ITC Mid South will occur. As a result of the merger, Mid South will become a direct subsidiary of ITC, under the new name ITC Midsouth. TCA will be renamed ITC Arkansas and will be a direct subsidiary of ITC Midsouth. As ITC Arkansas, the subsidiary will continue to own the transmission business currently operated by EAI.

D. ITC Arkansas Planning and Ratemaking Proposal

Once the Transaction is complete, ITC Arkansas will be a subsidiary of ITC Midsouth, providing transmission service to EAI and other wholesale customers.

According to ITC's Application at FERC, ITC Arkansas and the five other wires subsidiaries will each sign the MISO Transmission Owners Agreement ("TOA") and become transmission-owning members of MISO, and as such, will be participants in the MISO planning processes.²⁴ The Applicants have not provided a comprehensive organizational

²³ Direct Testimony of S. Brady Aldy (September 28, 2012), p. 5.

²⁴ ITC Holdings Corp., Entergy Corporation, Midwest Independent Transmission System Operator, Inc. *Joint application for authorization of acquisition and disposition of jurisdictional transmission facilities, approval of*

description of who will plan ITC Arkansas's system (i.e., whether it will be ITC Arkansas personnel, ITC Midsouth personnel, or ITC personnel). In fact, ITC has stated that it has not yet determined the post-transaction organization for the planning function.²⁵ The testimony supporting the Application states that initially, the organization for the new ITC Midsouth employees brought over from Entergy will be similar to the existing structure.²⁶ This indicates that the system will be planned similarly to how Entergy Services, Inc. ("ESI") plans the system for EAI today, with a central planning group at ITC Midsouth that performs services for the subsidiaries and assigns or allocates planning expenses to each subsidiary.^{27, 28}

ITC has applied to FERC for approval of formula-based rate tariffs for each of the new ITC operating companies, including ITC Arkansas, based on the mechanism contained in Attachment O to the MISO Open Access Transmission Tariff ("OATT").²⁹ If approved, ITC will implement the Attachment O formula rate for Arkansas customers by populating the inputs of the Attachment O formula and using the resulting ITC Arkansas revenue requirement forecast.

There are three key components of ITC Arkansas's formula rate. First, the rate employs a forward-looking test year which requires customers to pay rates based on forecasted spending. In a given rate year, if the actual spending is either higher or lower than the forecast upon which rates have been based, there will be a true-up mechanism the following year to reconcile the difference.³⁰

The second major component of the formula rate is the return on equity ("ROE") rate. ITC is requesting an ROE of 12.38% and claims that this rate is "available to all TOs belonging to MISO and comparable to that of the ITC operating subsidiaries that are members of MISO."³¹

Lastly, ITC's rate filing with FERC requests approval to utilize a capital structure of 60% equity and 40% debt. ITC states that this level is "consistent with both ITC's existing

transmission service formula rate and certain jurisdictional agreements, and petition for declaratory order on application of section 305(a) of the Federal Power Act. FERC Dockets EC 12-145, 12-2681, EL12-107. September 24, 2012. P. 60.

²⁵ Direct Testimony of Thomas W. Vitez (September 28, 2012), p. 33:1-17.

²⁶ See Direct Testimony of Jon E. Jipping (September 28, 2012), pp. 72:11-76:18

²⁷ Id. at 76:9-12, stating that "ITC employees dedicated to the ITC Midsouth Operating Companies' activities will perform the Planning function for the ITC Midsouth Operating Companies. However, the standards and planning criteria to which they perform this work will be set by ITC's corporate Planning organization."

²⁸ See, e.g., Direct Testimony of Kurtis W. Castleberry (September 28, 2012) at 17:9-19; Direct Testimony of Thomas W. Vitez (September 28, 2012) at 33:1-17; ITC's Response to Staff Data Request APSC 27-2.

²⁹ ITC Holdings Corp., et al. *Joint application*. FERC Dockets EC 12-145, 12-2681, EL12-107. September 24, 2012.

³⁰ Direct Testimony of Thomas H. Wrenbeck (September 28, 2012), pp. 5-8.

³¹ Direct Testimony of Cameron H. Bready (September 28, 2012), p. 35:2-9.

operating subsidiaries and with capital structure levels approved by FERC for other transmission entities.”³²

The impact of these components of ITC’s rate application is addressed in the following section.

³² Id.

3. THE TRANSACTION WOULD IMPOSE SIGNIFICANT COSTS ON ARKANSAS RATEPAYERS

As proposed, the Transaction would result in significant additional costs to all Arkansas ratepayers utilizing the Entergy transmission system. The following section describes the components of the net rate increase, including the quantitative costs and offsetting quantitative benefits described by the Applicants in testimony and supported by filed workpapers and responses to data requests.

In general, the Application presents an argument that the benefits of the Transaction, which are primarily qualitative, outweigh the net quantitative cost. In this section, Staff presents its review of the quantitative costs of the Transaction to customers. The qualitative benefits to customers will be discussed in Sections 4 and 6 below. Staff's analysis of the Transaction concludes that the alleged qualitative benefits do not outweigh the identified quantitative costs.

A. Loss of Bundled Load exemption for EAI retail ratepayers

Under the status quo, with EAI's continued ownership of the transmission assets and its anticipated membership in MISO, the Commission will continue to have ratemaking authority for EAI retail ratepayers. The Commission is able to retain this authority under EAI's membership in MISO due to the MISO's Bundled Load exemption, which establishes alternate revenue collection for transmission owners ("TOs") that are also load-serving entities ("LSEs"). In APSC Docket No. 10-011-U, the filings, technical conference, and hearings related to Entergy's Application to transfer control of its transmission assets to MISO included discussion of the Bundled Load exemption for EAI retail customers, under which, "MISO does not collect or distribute any revenues from or to a member TO's Bundled Load."³³

If the Transaction is executed, EAI will no longer be a TO in MISO. EAI retail load will therefore no longer qualify as Bundled Load. As a result of the loss of the Bundled Load exemption, transmission charges will be levied on Arkansas ratepayers (passed through EAI as the LSE) based on rates calculated through the MISO tariff, rather than APSC proceedings.

The shift from transmission charges utilizing the Bundled Load exemption to rates under the MISO tariff is expected to result in a significant increase in transmission revenue

³³ EAI's Response to Staff Data Request APSC 18-11.

requirement for Arkansas ratepayers. The components of this increase are detailed in the following section.

As will be discussed in the following section, the loss of the Bundled Load exemption shifts transmission rates out of Commission control, to the benefit of the transmission owner and the detriment of the retail ratepayers.

B. Increase in transmission rates under ITC ownership

The increase in transmission revenue requirement is based on three primary changes to the method of revenue recovery under ITC asset ownership, as compared to the current method under EAI ownership or the anticipated method under EAI ownership as a transmission owning member of MISO. These three components are: increased ROE, change in capital structure, and implementation of a forward looking test year for ratemaking purposes.

In addition to the increase in revenue requirement recovered from Arkansas ratepayers for these three changes, there are other potential changes that will increase rates, such as potential ROE adders and additional transmission system expansion beyond the upgrades currently planned by Entergy.

1. INCREASED RETURN ON EQUITY

A significant portion of the increase in revenue requirement results from the increase in allowed ROE as a result of the Transaction.

Currently, the Commission sets the recoverable ROE through the regular ratemaking process, which is now set at 10.2%.³⁴ As discussed in the previous section, this process would continue for EAI as a transmission-owning member of MISO due to the Bundled Load exemption.

Under ITC ownership, however, the ROE will be set during a proceeding at FERC whereby the transmission-owning member of MISO requests approval of an Attachment O template to be used to establish formula rates for transmission service. It is in that proceeding that the ROE will be set for ITC's transmission service to EAI. That proceeding is currently under way at FERC.³⁵ In their Application in that proceeding, ITC is requesting a 12.38% ROE, stating: "Consistent with Commission precedent, because they will be Transmission Owner members of MISO, the New ITC Operating Companies are entitled to use the 12.38% MISO ROE."³⁶ The 218 basis point increase in ROE will directly increase the transmission revenue requirement to be recovered from

³⁴ Commission Order No. 20, Docket No. 09-084-U.

³⁵ FERC Dockets EC 12-145, 12-2681, EL12-107.

³⁶ ITC Holdings Corp., et al. *Joint application*. FERC Dockets EC 12-145, 12-2681, EL12-107. September 24, 2012, p. 65.

Arkansas ratepayers. See Table 3 below for details on the increase in revenue requirement.

2. CHANGE IN CAPITAL STRUCTURE

During the ratemaking process, the applicable ROE is applied to the approved equity portion of the company capital structure to determine the revenue requirement approved for equity investors.

Currently, the APSC has approved a capital structure for EAI consisting of 54.5% debt and 45.5% equity (including preferred shares).³⁷ ITC has applied to FERC for approval of a target capital structure consisting of 40% debt and 60% equity.³⁸

The Applicants have not provided a direct justification for the proposed capital structure in their Application. ITC's response to a Staff Data Request on the issue refers to testimony in the FERC matter stating that the capital structure is appropriate for a non-diversified company because they are "less able to withstand disruptions in their revenue stream."³⁹ Additionally, ITC claims that the capital structure will permit lower interest payments, "preserve investor confidence," and provide access to lower cost capital.⁴⁰

Since the ROE is significantly higher than the cost of debt, a capital structure with a high equity portion produces a higher transmission revenue requirement, significantly increasing costs to ratepayers. This effect is compounded by the higher ROE under ITC ownership, as discussed above.

The Applicants prepared an exhibit demonstrating how the change in ROE and capital structure increase the weighted average cost of capital ("WACC").⁴¹ A summary of the overall impact is provided in Table 2 below.

TABLE 2. MODELED IMPACT OF TRANSACTION ON WACC

	2014	2015	2016	2017	2018
EAI Pre-Tax WACC	10.31%	10.41%	10.45%	10.51%	10.56%
ITC Arkansas, LLC WACC	13.62%	13.65%	13.67%	13.70%	13.72%

³⁷ Derived from EAI workpapers filed in support of its Application (HSPI_Lewis-Rate_Effects_Workpaper_2.xlsx).

³⁸ ITC Holdings Corp., et al. *Joint application*. FERC Dockets EC 12-145, 12-2681, EL12-107. September 24, 2012. P. 51.

³⁹ ITC's Response to Staff Data Request 35-1.

⁴⁰ Id.

⁴¹ Exhibit CMB-7 to the Direct Testimony of Cameron M. Bready (September 28, 2012).

This calculation of EAI's WACC does not incorporate several zero cost components that were included in EAI's last general rate case, such as Current, Accrued, and Other Liabilities ("CAOL") and ADIT. When these and other components were included in the calculation, EAI's WACC was 5.04%.⁴² The Applicants have not addressed how these elements would be incorporated in the FERC ratemaking process.

See Table 3 below for details on the increase in revenue requirement due to the modified capital structure.

3. FORWARD TEST YEAR

Under Arkansas law, EAI's general rate case applications, including its transmission rates, are based on a test year adjusted for known and measurable changes.⁴³ That test year may be comprised of historical twelve calendar months or comprised of six months of historical data and six months of projected data. In either case, the test year information may be adjusted for known and measurable changes in circumstances that occur during the twelve months following the end of the test year.

In its rate application at FERC, ITC is proposing the use of a forward looking test year in which rates are based on the forecast of costs and capital expenditures, rather than an accounting of actual past expenditures.⁴⁴ The rate includes a true-up mechanism to reconcile any differences between actual costs and revenues recovered from ratepayers.

The FERC forward looking test year and true-up provisions provide more frequent adjustments to the transmission revenue requirement and rates than do the procedures implemented by the Commission pursuant to Arkansas law. The transmission revenue requirement will be set each year based on the forecast of the following year's expenditures, as determined in the formula rate implementation protocols.⁴⁵ According to the Applicants, this is important to reduce "regulatory lag" related to cost recovery.⁴⁶ EAI has argued that the impact of the forward looking test year should be excluded from the analysis of rate impact because it is a "timing effect" of revenue recovery rather than an actual increase.⁴⁷ However, EAI's analysis shows an actual impact on year-to-year revenue requirement recovered from customers. Between 2014 and 2018, the use of

⁴² Commission Order No. 20, Docket 09-084-U.

⁴³ Ark. Code Ann. §23-4-406

⁴⁴ ITC Holdings Corp., et al. *Joint application*. FERC Dockets EC 12-145, 12-2681, EL12-107. September 24, 2012. pp. 52-53.

⁴⁵ Direct Testimony of Thomas H. Wrenbeck (September 28, 2012), pp. 9-12.

⁴⁶ Direct Testimony of Cameron M. Bready (September 28, 2012), pp. 36:11-37:1.

⁴⁷ EAI's Response to Staff Data Request APSC 11-11.

Direct Testimony of Jay A. Lewis, (September 28, 2011) pp. 34-38.

the forward test year [REDACTED]
[REDACTED] (see Table 3 below).⁴⁸

4. COMBINED IMPACT OF CHANGES

The Application presents an estimate of the impact of the Transaction on the retail rates of EAI customers, claiming that the average retail customer will pay only \$1.22 more per month, a 1.3% increase in the overall bill.⁴⁹ Given that this Transaction affects EAI's transmission assets and ultimately the resultant transmission rates, Staff has analyzed data provided in support of the Application to evaluate the increase in transmission revenue requirement recovered from ratepayers in total.

Overall, the increase in ROE, revised capital structure, and implementation of a forward looking test year account for significant increases over the status quo (continued Entergy ownership). A summary of the increase in the transmission revenue requirement is provided in Table 3 below. Note that this analysis does not include offsetting Transaction benefits claimed by the Applicants. The quantitative benefits are addressed below.

TABLE 3. INCREASE IN ARKANSAS RETAIL TRANSMISSION REVENUE REQUIREMENT UNDER ITC, 2014-2018⁵⁰

	2014	2015	2016	2017	2018
Status Quo	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
ROE/Capital Structure	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
Forward looking test year	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
Increase due to Transaction	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
Increase (%)	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]

Based on the Applicants' analysis, the 2014 transmission revenue requirement will increase by [REDACTED] due to revenue recovery changes stemming from the Transaction and ITC ownership.

The Applicants' rate impact analysis only forecasted the revenue requirement through 2018, but the impact of the higher ROE, change in capital structure, and forward looking test year will persist and the transmission revenue requirement under ITC will continue to be higher than it would under continued EAI ownership.

⁴⁸ Derived from EAI workpapers filed in support of its Application (HSPI_Lewis-Rate_Effects_Workpaper_2.xlsx)

⁴⁹ Application, pp. 38-39.

⁵⁰ Derived from EAI workpapers filed in support of its Application (HSPI_Lewis-Rate_Effects_Workpaper_2.xlsx)

5. ADDITIONAL INCREASES POSSIBLE

As discussed above, The Applicants' analysis shows that the Transaction will cause a significant increase in transmission revenue requirement. There are at least two ways in which the rate impact analysis performed by the Applicants and summarized above may underestimate the increase in transmission rates resulting from the Transaction.

Potential ROE Adders

First, the analysis assumes an increase in the ROE from current APSC approved rates to the standard MISO rate of 12.38%. However, ITC has acknowledged multiple times that, despite its Application at FERC for the standard 12.38% ROE, it may be eligible for incentive rates as high as 13.38%.

ITC's July 1, 2011 non-binding indication of interest in the Entergy transmission business states:

[REDACTED]

51

The parties' joint application at FERC, in which ITC requests the "default" 12.38% ROE, states:

*At this time, ITC Holdings is not requesting any transmission rate incentives for the New ITC Operating Companies, including an incentive adder for independence, even though ITC believes that such an incentive adder would be appropriate and fully in line with Commission precedent... **ITC, however, reserves the right to request in the future transmission rate incentives for the New ITC Operating Companies, including an incentive adder for independent ownership of transmission facilities.** Because of the constraints imposed by the independent transmission company model, and its demonstrated track record of supporting cost effective transmission investment, such ROE incentives continue to be important and may become necessary for the New ITC Operating Companies. (Emphasis added.)*⁵²

ITC has previously requested and received from FERC incentive adders for independent ownership of 100 basis points for other operating subsidiaries. In fact, of the five ITC subsidiaries, four have received the independence incentive ROE adder: ITC Transmission (13.88%),⁵³ Michigan Electric Transmission Company (13.38%),⁵⁴ ITC

⁵¹ ITC's Response to Staff Data Request APSC 17-1, Attachment p. TH41.

⁵² ITC Holdings Corp., et al. *Joint application*. FERC Dockets EC 12-145, 12-2681, EL12-107. September 24, 2012. P. 51.

⁵³ *ITC Holdings Corp.*, 113 FERC ¶ 61,343 (2003) (Order authorizing disposition of jurisdictional facilities, accepting for filing proposed agreements, requiring compliance filing, and accepting in part and rejecting in part proposed transmission rates).

Great Plains (12.16%),⁵⁵ and ITC Green Power Express (12.38%).⁵⁶ ITC requested the incentive adder for ITC Midwest, but was denied due to insufficient supporting analysis in the application.⁵⁷

It is important to note that if the Transaction receives all necessary approvals and is executed as scheduled, this future application for an increase in ROE will be made at FERC only, and will not be subject to Commission jurisdiction.

Potential additional investment in capital expenditures

The Applicants' analysis calculates the transmission revenue requirement based on Entergy's current assumptions on transmission expansion and capital expenditures. However, it is likely that ITC will develop a more aggressive transmission system upgrade plan with additional capital expenditures for two reasons.

First, EAI and ITC have acknowledged that the capital spending assumptions used in their analysis are lower than the likely actual spending levels. In discussing the assumptions for modeling the increase in transmission revenue requirement under ITC ownership, witness Cameron Bready noted that ITC only assumed that it would build projects currently identified in Entergy's 5-year base capital plan.⁵⁸

In addition, EAI witness Jay Lewis testified that the Entergy base capital plan is most likely a conservative estimate and that particularly in the latter years, spending will most likely be higher than the forecast:

The taper effect reflects that the base capital plan does not include potential incremental, unidentified or unknown projects that could occur depending on future events and variables, such as catastrophic storm activity, new regulations or acquisition opportunities. A recent example of capital requirements that arose but were not included in the planned capital investments is the investment needed to meet updated transmission planning standards (over \$500 million)... I believe the latter year estimates are less

⁵⁴ *Michigan Electric Transmission Company, LLC*, 113 FERC ¶ 61,343 (2005) (Order conditionally accepting proposed tariff revisions for filing and establishing hearing and settlement judge procedures). ITC acquired METC in 2006.

⁵⁵ *ITC Great Plains, LLC*, 126 FERC ¶ 61,223 (2009) (Order granting in part and denying in part rate incentives, conditionally accepting tariff revisions, and establishing hearing and settlement procedures).

⁵⁶ *Green Power Express LP*, 127 FERC ¶ 61,031 (2009) (Order on transmission rate incentives and formula rate proposal and establishing hearing and settlement judge procedures).

⁵⁷ *ITC Holdings Corp.*, 121 FERC ¶ 61,229 (2007) (Order authorizing disposition of jurisdictional facilities, accepting proposed rates and jurisdictional agreements subject to conditions, and dismissing complaint).

⁵⁸ Direct Testimony of Cameron M. Bready (September 28, 2012), p. 43:14-17.

*than what will actually occur because it is not possible to accurately predict the latter years of a forecast.*⁵⁹

The second reason why the assumptions on capital expenditures are too low is that ITC intends to identify additional projects to reduce system-wide congestion. In fact, according to the Applicants, ITC's ability to identify more transmission projects is one of the primary benefits of the Transaction [See Section 4C below].

To illustrate the potential impact of additional investment, the suite of "illustrative projects" developed by ITC witness Johannes Pfeifenberger carried a net increase in Entergy system-wide revenue requirement of \$2.1 billion. According to the analysis, this increase was largely offset by production cost savings occurring primarily in Louisiana and Texas (see Table 6 below).⁶⁰

C. Quantified benefits do not offset additional costs

The Applicants have represented in the Application and testimony that one of the benefits of the Transaction derives from the lower cost of debt available to ITC. ITC witness Cameron Bready notes that the debt cost savings are a "direct result of the difference in credit quality between what is anticipated for the New ITC Operating Companies and the current Entergy Operating Companies."⁶¹

Table 4 below contains the Applicants' assumptions regarding the pre-tax cost of debt for EAI and ITC.

TABLE 4. PRE-TAX COST OF DEBT, 2014-2018⁶²

	2014	2015	2016	2017	2018
EAI	5.29%	5.46%	5.58%	5.69%	5.78%
ITC	3.50%	3.57%	3.63%	3.69%	3.75%

ITC has based its assumed cost of debt on JP Morgan estimates subject to change.⁶³ EAI has not provided support for the cost of debt assumed in the rate impact, which contradicts EAI's statement in response to a data request that its current cost of debt is 4.88%.⁶⁴

⁵⁹ Direct Testimony of Jay A. Lewis (September 28, 2012), p. 8:7-19.

⁶⁰ Direct Testimony of Johannes Pfeifenberger (September 28, 2012), pp. 23:22-24:7.
ITC's Response to Staff Data Request APSC 10-17.

⁶¹ Direct Testimony of Cameron M. Bready (September 28, 2012), p. 20:16-17.

⁶² Id. at Exhibit CMB-7

⁶³ Direct Testimony of Cameron M. Bready (September 28, 2012), p. 22.

⁶⁴ EAI's Response to Staff Data Request APSC 21-5.

According to the Applicants' analysis, the assumed reduction in debt cost reduces the overall revenue requirement modeled in the Application. Table 5 below provides the offsetting change in revenue requirement impact due to the modeled change in cost of debt.

TABLE 5. IMPACT OF LOWER COST OF DEBT ON RETAIL TRANSMISSION REVENUE REQUIREMENT, 2014-2018

	2014	2015	2016	2017	2018
Status Quo					
ROE/Capital Structure					
Forward looking test year					
Savings from lower cost of debt					
Increase due to Transaction					
Net Increase (%)					

The evidence suggests that the offsetting savings from a lower cost of debt are overstated. Even if the claimed reduction does materialize, the revenue requirement benefits still do not nearly offset the additional costs from the changes in ROE, capital structure, and forward test year discussed above.

D. Rate impact on wholesale customers

In addition to the impact on retail rates, the Transaction would also impose additional quantitative costs on wholesale customers. Upon EAI's transition to MISO, wholesale customers will already have to pay the increased ROE because wholesale load does not qualify for the Bundled Load exemption. However, wholesale customers will be impacted by the change in capital structure, the implementation of the forward test year, and any additional future impacts of the ROE adder and additional capital expenditures under ITC ownership discussed above.

To the extent that the Transaction yields benefits claimed in the Application (as discussed in the following sections), wholesale customers will similarly share in those benefits with retail customers.

E. No impact mitigations have been proposed

The Applicants have not proposed any measures which would directly mitigate the impact of the higher transmission revenue requirement to ratepayers.

ITC's July 1, 2011 non-binding indication of interest in the Entergy transmission business states:

[REDACTED]

ITC has provided no further information on [REDACTED] considered.⁶⁶

Similarly, EAI has not provided any information regarding ██████████ in the development of the Transaction.⁶⁷

A Board of Directors presentation from December 2, 2011

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED] 68

F. Conclusion

The Applicants acknowledge that the Transaction will result in quantifiable net costs to Arkansas wholesale and retail ratepayers. The increase in ROE, increased equity portion of the capital structure, implementation of a forward looking test year and annual true-up

⁶⁵ ITC's Response to Staff Data Request APSC 17-1, Attachment p. TH43.

66 In response to a data request seeking information on the [REDACTED] considered, ITC withheld all applicable information as attorney work product or protected under attorney-client privilege. See ITC's Response to Staff Data Request APSC 24-2.

67 [REDACTED]
[REDACTED]
[REDACTED]
[REDACTED]
[REDACTED] See EAI's Response to Staff Data Request APSC 23-5.

68 EAI's Response to Staff Data Request APSC 23-9.

provisions for FERC ratemaking all impose significant additional increases in the transmission revenue requirement. The Applicants have argued that quantitative benefits due to ITC's purported lower cost of debt offset this increase. Even if these savings materialize, they will only offset the costs to a small degree.

Overall, the change in ownership will result in an increase in annual retail transmission revenue requirement of between [REDACTED] each year for the first five years. Even if the impact of the forward test year and annual true-up provisions for FERC ratemaking is excluded, as the Applicants propose, the transmission revenue requirement still increases by [REDACTED] over the status quo each year from 2014-2018.⁶⁹

Perhaps of greater concern is the potential for additional increases that have not been modeled by the Applicants. If ITC seeks, and is granted, an additional incentive ROE adder from FERC, the ROE could increase by 100 basis points, based on previous ITC subsidiary experience. As noted above, ITC has acknowledged to FERC that it believes this incentive would be appropriate, and has stated that [REDACTED]

[REDACTED]
[REDACTED]
[REDACTED]
[REDACTED]

In addition to the higher ROE, there is a strong indication that ITC will make transmission investments in excess of the upgrades currently planned by Entergy, and included in the rate impact analysis. Additional capital expenditures will increase the rate base upon which the ROE and capital structure impacts are applied, increasing the transmission revenue requirement further.

The known impact of the Transaction on the transmission revenue requirement is large and would impose significant costs on ratepayers, and the impacts still unknown could increase this impact even further.

⁶⁹ Derived from EAI workpapers filed in support of its Application (HSPI_Lewis-Rate_Effects_Workpaper_2.xlsx)

4. THE TRANSACTION DOES NOT YIELD SIGNIFICANT BENEFITS INCREMENTAL TO EAI MEMBERSHIP IN MISO

Throughout the Application and testimony, Applicants argue that the Transaction will yield substantial benefits. Several of the primary benefits identified are substantively similar to the benefits of Regional Transmission Organization (“RTO”) membership identified by EAI in APSC Docket No. 10-011-U. The Applicants have not provided compelling evidence that the Transaction will yield material benefits beyond those that will accrue from RTO membership.

A. Independence

The Applicants argue throughout the Application and testimony that independence created by the Transaction drives a significant portion of the overall benefits. There are two primary types of independence identified by the Application as creating benefits. The first is the independent ownership, planning and operation of the transmission system independent from generation or distribution operations, which this report will refer to as “functional independence.” The second is the independence of the transmission system ownership from the other Entergy OpCos, which this report will refer to as “organizational independence.”

1. FUNCTIONAL INDEPENDENCE

The Applicants argue that functional independence creates benefits by instilling confidence in the wholesale markets and removing any lingering perception of bias in transmission planning and operation deriving from EAI’s operation as a vertically integrated entity.

The Applicants argue that independent ownership of the Entergy transmission system from Entergy generation and retail operations provides the optimal structure to derive benefits from the wholesale market. As described in the Bunting Testimony:

This transaction, in combination with the proposal to join MISO, assures all transmission customers that they are on equal footing to compete in a regional Day 2 Market (and bilaterally) using a transmission system that is owned by an entity that is completely independent from that market. That combined effect should instill the highest level of confidence in merchant generators that they will be able to compete in a larger market and to their fullest capability,

which should translate to benefits for retail customers by providing those customers access to lower cost energy sources.⁷⁰

The Applicants provided no evidence or support demonstrating that the Transaction will accomplish any independence benefits beyond those accomplished through Entergy's transfer of operational control of those assets to MISO. In fact, the Application notes that participation in MISO as a transmission owning member will already constitute progress towards functional independence: "MISO membership will mitigate any lingering perceptions of bias, but only full independence will completely eliminate such perceptions."⁷¹ EAI has not provided any arguments or evidence demonstrating that there is any incremental benefit to ratepayers from this distinction.

The Applicants have not provided any additional support or documentation demonstrating benefits beyond the arguments provided in testimony. EAI has referred simply to the "perception of bias" argument:

The ITC Transaction will enhance independence in two primary ways that are not achievable under Entergy Operating Company ownership. There will be greater independence in transmission planning and MISO governance... While a utility would be obligated to undertake its participation in MISO planning processes in a non-discriminatory manner, and MISO rules ultimately must be approved by FERC as not unduly discriminatory, that situation does not eliminate the perception by other asset owners or market participants that a transmission owner may act in a biased manner in favor of its own generation or load served.⁷² (Emphasis added.)

EAI's explanation indicates that the vertically-integrated nature of its business inherently creates bias, or the perception of bias, and consequently hinders the operation of the wholesale market. EAI has proposed to join MISO, in part, to address these concerns of bias. MISO operates an open, competitive market including many vertically-integrated utilities. Given that divestiture of transmission assets is not required to participate in, and benefit from, MISO's open market, EAI has not provided any evidence demonstrating that the distinction created by independent ownership will create tangible benefits.

ITC's response to a similar data request also does not provide any evidence or documentation supporting the existence or magnitude of any incremental benefit.⁷³

In general, the Applicants argue that despite independent operation of the transmission system by MISO and formal planning processes under MISO designed to ensure non-

⁷⁰ Direct Testimony of Theodore H. Bunting, Jr. (September 28, 2012), pp. 12-13.

⁷¹ Application, p. 27.

⁷² EAI's Response to Staff Data Request APSC 21-2.

⁷³ ITC's Response to Staff Data Request APSC 22-1.

discriminatory planning, there may still be a “lingering perception” by some market participants that Entergy could engage in planning that unfairly advantages its own generators. The Applicants have provided no evidence supporting this argument beyond statements in testimony, nor any analysis demonstrating how this benefit outweighs the additional costs of the Transaction discussed above.

2. ORGANIZATIONAL INDEPENDENCE

The Applicants also argue that the Transaction will achieve a goal set by the Commission for independence from the other Entergy OpCos. Their argument for the value of this independence misconstrues the Commission’s directive, and omits other Commission goals expressed in Docket No. 10-011-U.

The Application states that: “The Transaction fulfills the APSC’s directive for EAI to conduct its transmission planning and operations separate from that of the other Entergy Operating Companies.”⁷⁴ In support of this statement, the Application cites Commission Order No. 54 in Docket No. 10-011-U, which directs EAI to “[e]ngage in transmission planning or operations separately from the other OpCos, Entergy affiliates, or any future Entergy Transco except through the RTO process as a separate RTO member.”⁷⁵

Furthermore, EAI witness McDonald’s testimony discusses how the Transaction will advance this objective, claiming that after the Transaction, EAI will not have to participate with the other Entergy OpCos in joint planning:

*Absent the ITC Transaction, EAI will be required to continue to participate in joint transmission planning for the Entergy Transmission System with the other Entergy Operating Companies, whether as a MISO member or if EAI operates its electrical facilities on a stand-alone basis... After the closing of the Transaction, ITC would independently own all the Entergy Operating Companies’ transmission assets, eliminating that remaining obligation for EAI to participate with the other Entergy Operating Companies in joint planning for the former Entergy Transmission System, consistent with the Commission’s objective of EAI’s minimizing its interaction with the other Operating Companies.*⁷⁶

The Applicants’ representation of the Commission’s directive is focused too narrowly and omits other priorities expressed elsewhere in Order No. 54 and other orders in Docket No. 10-011-U. The Commission was looking to end cost-sharing and litigation among the Entergy OpCos and shield Arkansas ratepayers from the negative consequences of EAI’s association with the other OpCos. The conditions agreed upon by

⁷⁴ Application, p. 2.

⁷⁵ Docket No. 10-011-U, Order No. 54 at 109.

⁷⁶ Direct Testimony of Hugh T. McDonald (September 28, 2012), pp. 14-15.

the parties in that docket help achieve the Commission's objectives, but under ITC ownership, there will be fewer protections against cost-sharing among the ITC Midsouth transmission subsidiaries that were formerly held by Entergy OpCos.

Under EAI's continued ownership and membership in MISO, EAI will conduct transmission planning with the assistance of ESI. EAI will procure ESI's services under a cost-based contract that is subject to approval by the Commission.⁷⁷ There will be no allocation to EAI of costs incurred by ESI for Entergy system-wide planning, or cost-sharing for projects that do not benefit EAI customers. This structure achieves the primary goals expressed by the Commission and described above.

Under the proposed Transaction, the transmission operating companies under ITC are similar to the transmission portion of the current Entergy OpCos (i.e., ITC Arkansas would own the same assets and serve the same territory as the transmission portion of EAI currently does). The Applicants are correct that there will be no association with the remaining *Entergy* OpCos. However, there will be a strong association between ITC Arkansas and the other ITC subsidiaries. The difference is largely in name only, and will not actually address the concerns and priorities expressed by the Commission.

In fact, under ITC ownership, there could actually be less independence and more cost-sharing between the transmission operating companies than there would be under continued Entergy ownership under MISO operational control. Regarding planning, under the status quo, EAI would be responsible for transmission planning duties, supplemented by ESI personnel under a cost-based contract subject to Commission approval.⁷⁸ Under ITC structure, planning and operation will be done at the holding company level, and costs will be directly assigned to affiliates "where it is rational and reasonably clear to do so."⁷⁹ Where this is not possible, "those costs will be allocated to the ITC Midsouth Operating Companies in accordance with ITC's FERC approved methodology for the allocation of such costs."⁸⁰

The Applicants have not provided any evidence to support their statements in testimony that ITC ownership of the Entergy transmission assets will provide meaningful independence beyond Entergy's participation as a transmission-owning member of MISO. Additionally, it appears that the Applicants erred in their interpretation of Commission directives in assuming that changing ownership while maintaining largely the same relationship between the transmission operating companies achieves the Commission's directives regarding desired independence.

⁷⁷ Commission Order No. 72 (Docket No. 10-011-U) pp. 10-11.

⁷⁸ *Id.*

⁷⁹ ITC's Response to Staff Data Request APSC 27-2.

⁸⁰ *Id.*

B. Broad regional view

The Applicants have argued that ITC's business model gives it a more broad regional view of transmission planning which will yield additional benefits. The Application states: "An independent transmission company also offers a broader regional view of the MISO market with respect to identifying opportunities to improve the efficiency of the transmission system to the benefit of the market as a whole."⁸¹ The Welch Testimony elaborates on this argument.⁸²

Additionally, the Pfeifenger Testimony argues that due to ITC's experience in multiple markets, it will be better suited for interregional planning:

*In fact, as an independent transmission company operating in the SPP and MISO regions, ITC will have the expertise to facilitate transmission planning across the MISO-SPP boundaries. As an independent transmission company, ITC may also be in better position to facilitate coordination with AECI and TVA.*⁸³

This benefit apparently relies on the assumption that ITC is better at planning and identifying beneficial projects than Entergy operating within the MISO planning processes. The Applicants have not provided any evidence why ITC's experience or business model will enable it to identify regional transmission projects better than Entergy, which currently plans and operates a transmission system covering four states with interconnections with SPP, MISO, and TVA.

In response to Staff data requests, neither EAI nor ITC were able to provide an estimate of the magnitude of the benefits of the broad regional view.^{84, 85} In addition, EAI's past testimony in Docket No. 10-011-U indicates that it is primarily MISO's responsibility to do regional planning. For instance, Mr. Riley states:

[T]he MISO planning staff is responsible for conducting the regional planning process. MISO staff integrates the planning processes used by each Transmission Owner member for that owner's own transmission system and the advice and guidance of stakeholders into a coordinated regional transmission plan (the MTEP) and identifies additional expansions as needed to provide for an efficient and reliable transmission system. Among other things, the MISO staff is responsible for developing regional transmission planning models, testing regional models to identify performance of the models against national reliability standards, evaluating alternative solutions to identified needs, developing (through a collaborative process) possible solutions to identified issues, selecting

⁸¹ Application, p. 34.

⁸² Direct Testimony of Joseph L. Welch (September 28, 2012), p. 27.

⁸³ Direct Testimony of Johannes Pfeifenger (September 28, 2012), p. 12:9-13.

⁸⁴ EAI's Response to Staff Data Request APSC 9-2.

⁸⁵ ITC's Response to Staff Data Request APSC 12-6.

*preferred solutions, identifying opportunities for economic expansions, determining funding and cost responsibility, and monitoring the progress of solution implementation.*⁸⁶

Moreover, Mr. Riley states that “MISO will have primary authority for planning economic transmission upgrades, providing an independent view across a broader region than today.”⁸⁷

C. Economic upgrades

The Applicants also claim that, due to the independence and broad regional view of ITC, it will be better suited to identify transmission projects that will increase the economic efficiency of the grid, generating benefits for customers. ITC Witness Joseph Welch testifies that “... it is both in our best interest and the best interest of customers to ensure that the transmission system is robust, to pursue the economic reduction of congestion and lower the overall cost of delivered energy, and provide access to all generators.”⁸⁸

Additional testimony from ITC witness Thomas Vitez argues that ITC’s planning process is better capable of identifying projects that will reduce congestion⁸⁹ Mr. Vitez claims that ITC will yield planning benefits above and beyond those that EAI would achieve as a MISO member is due to MISO’s bottoms up approach.⁹⁰

Mr. Vitez claims that ITC’s singular focus allows it to plan and construct better transmission solutions under this structure, and specifically addresses the advantages regarding economic upgrades.⁹¹

ITC’s claims on the advantages of its planning process are not consistent with the characterization of the benefits of the MISO planning process offered by EAI and MISO in Docket No. 10-011-U (as discussed above).

Even if ITC is better able to find economic transmission projects, it is not certain that the projects will benefit Arkansas ratepayers. As part of the Application, ITC contracted Johannes Pfeifenberger to perform analysis and modeling of illustrative transmission projects that would, among other things, reduce congestion in the Entergy region and provide access to lower cost energy sources. According to the modeling results, the illustrative projects studied by Mr. Pfeifenberger indeed reduced congestion and yielded production cost benefits, but these benefits primarily accrued in southern Louisiana and

⁸⁶ Direct Testimony of Richard C. Riley (November 28, 2011), Docket No. 10-011-U, pp. 29:20-30:11.

⁸⁷ Id., p. 36:20-22.

⁸⁸ Direct Testimony of Joseph L. Welch (September 28, 2012), p. 49.

⁸⁹ Direct Testimony of Thomas W. Vitez (September 28, 2012), p. 8:11-13.

⁹⁰ Id., p. 31:22-32:2.

⁹¹ Id., p. 32:15-20.

Texas where congestion is high.⁹² Table 6 below provides a breakdown of the production cost savings by service territory (negative numbers indicate increases in production cost [REDACTED]).

TABLE 6. PRODUCTION COST SAVINGS FROM SELECT "ILLUSTRATIVE PROJECTS"⁹³

ENTERGY OPCO	NPV OF ADJUSTED PRODUCTION COST (2017 \$MILLION)
[REDACTED]	[REDACTED]
[REDACTED]	[REDACTED]
[REDACTED]	[REDACTED]
[REDACTED]	[REDACTED]
[REDACTED]	[REDACTED]
[REDACTED]	[REDACTED]
[REDACTED]	[REDACTED]
System-wide savings	\$1,406.3

The Applicants' argument that the Transaction will yield benefits from improved identification and planning of economic transmission projects relies on the assumption that ITC is inherently better at identifying such projects. In addition, it generally disregards the MISO planning processes already in place to identify transmission solutions to congestion. Part of the MISO Transmission Expansion Plan ("MTEP") planning process includes the "Market Efficiency Planning Study," which "considers local flowgate specific congestion mitigation solutions (bottom-up) and larger scale projects/portfolios (top-down) on a regional basis to produce more efficient and cost effective projects and portfolios."⁹⁴ And Mr. Pfiefenberger's evaluation of the illustrative ITC upgrades admits that many of the projects would already be identified by the MISO process:

While it is likely that the Congestion Relief projects would also be identified through MISO's planning process, I included these projects as part of the illustrative portfolio of strategic projects as examples of the type of additional cost-effective projects that will tend to be found through this type of broad-based independent planning process.⁹⁵

⁹² Direct Testimony of Johannes Pfeifenberger (September 28, 2012), pp. 23-25.

⁹³ Attachment to ITC's Response to Staff Data Request APSC 10-17, "HSPI_ITC-AR-008364.XLS"

⁹⁴ MISO MTEP Studies, <https://www.midwestiso.org/Planning/TransmissionExpansionPlanning/Pages/MTEPStudies.aspx>

⁹⁵ Direct Testimony of Johannes Pfeifenberger (September 28, 2012), p. 16.

Moreover, in Docket No. 10-011-U, Mr. Riley states that “The identification of economic upgrades is part of MISO’s top down planning process, such as the evaluation of MVPs and Market Efficiency Projects.”⁹⁶

While the Applicants’ analysis is only for illustrative purposes, it does reinforce the conclusion that the opportunities for economic transmission upgrades to reduce congestion lay primarily in areas other than Arkansas. The analysis did not evaluate potential allocation of project costs, and ITC only notes that allocation would follow MISO procedures whereby “cost allocation would generally align the costs of projects with the benefits received.”⁹⁷ While this provides for the possibility that costs would be shared beyond the region, it also indicates that EAI could be required to pay for projects in excess of the benefits received.

D. Conclusion

Many of the primary benefits of the Transaction claimed in the Application derive from ITC’s independence, broad regional planning view, and ability to identify economic transmission upgrades. The argument that the planning benefits should be ascribed to the Transaction relies on the assumption that ITC is inherently better at identifying potential upgrades than Entergy operating within MISO, and that the MISO planning processes in place will not identify these projects without ITC participation.

These are important attributes in the operation of a transmission system, but the Applicants have not provided sufficient evidence to support their assertions in testimony to demonstrate that operation and planning of the Entergy transmission system by ITC in MISO will yield substantial, if any, additional benefits over Entergy operation and planning as a transmission owning member of MISO. In addition, the Applicants have not been able to quantify the magnitude of any benefits.

⁹⁶ Direct Testimony of Richard C. Riley (November 28, 2011), Docket No. 10-011-U, p. 36:1-3.

⁹⁷ ITC’s Response to Staff Data Request APSC 10-20.

5. THE TRANSACTION MAY REDUCE COMMISSION JURISDICTION AND RENDER THE CONDITIONAL ORDERS IN DOCKET NO. 10-011-U OBSOLETE

The Commission issued Orders in Docket No. 10-011-U to ensure EAI's transition to MISO was in the public interest. If EAI successfully transfers control of its transmission assets to MISO and then sells its transmission assets to ITC, EAI would no longer be a transmission-owning member of MISO. This section of the report explains how the Transaction would impact EAI's planned MISO membership and change the meaning of the conditions the Commission placed in its conditional Orders approving EAI's petition to transfer control of its transmission assets to MISO.

A. Certain conditions may not apply if this Transaction is approved

EAI has indicated in response to data requests that several conditions in Order No. 68, which it had originally agreed to, may no longer apply or at least have reduced relevance if the Transaction is completed. For instance:

- For Condition 4, EAI would still be bound by the condition to seek Commission approval to terminate its MISO membership. However, it would be a transmission customer of ITC but not a transmission owner in MISO, and could no longer request authority to transfer control of transmission assets it no longer owns.⁹⁸
- For Condition 5, EAI would still be bound by the condition that the Commission could direct EAI to exit MISO, but as with Condition 4, EAI would still be a transmission customer of ITC.⁹⁹
- For Condition 8, transmission service would no longer be bundled with other service.¹⁰⁰
- For Condition 14, EAI could still provide the Commission with information on the net benefits of MISO membership and changes in FERC policies regarding RTOs, but the usefulness of such information if EAI no longer has the authority to transfer control of transmission assets is questionable.¹⁰¹

⁹⁸ EAI's Response to Staff Data Request ASPC 21-8.

⁹⁹ EAI's Response to Staff Data Request ASPC 21-9.

¹⁰⁰ EAI's Response to Staff Data Request ASPC 21-11.

¹⁰¹ EAI's Response to Staff Data Request ASPC 21-13.

B. ITC is not subject to conditions of Order No. 68

Unlike EAI, ITC was not a party to Docket No. 10-011-U. Joseph Welch filed an affidavit related to Condition 2 of Order No. 68 stating that ITC agreed to assume a separate Arkansas transmission pricing zone and stating ITC would not oppose Arkansas being in all zones in MISO separate from the other OpCos.¹⁰² Aside from this affidavit, ITC has not agreed to any MISO membership conditions. In responses to data requests, ITC has indicated that if the proposed Transaction is completed, it may not be able to meet many conditions of Order No. 68, or the Commission may lack jurisdiction to enforce the conditions. These conditions include:

- For Condition 4, ITC states that based on its review of applicable statutes and regulations, ITC Arkansas “would not need permission from the Commission to withdraw from MISO” and that exiting MISO would be FERC jurisdictional.¹⁰³
- For Condition 5, ITC states that the Commission could request ITC Arkansas withdraw from MISO, but that ITC Arkansas “would have to agree to the withdrawal and such an exit would have to be approved by FERC and would be subject to the processes and requirements of the MISO tariff and the MISO TOA” and that “FERC would be the appropriate authority to address ITC Arkansas’ membership or withdrawal from MISO.”¹⁰⁴
- For Condition 6, although ITC confirms that the Commission would have authority over siting of transmission facilities, assuming ITC Arkansas is a regulated public utility in Arkansas,¹⁰⁵ and that it would have the contractual obligation to provide reliable service to Entergy, it states that:¹⁰⁶
 - FERC would determine the rates for transmission service for ITC Arkansas facilities;
 - FERC would have exclusive jurisdiction of transmission facility operations;
 - FERC has jurisdiction over the reliability of the bulk power system; and
 - Section 204 of the Federal Power Act regulates the issuance of securities by FERC-jurisdictional utilities.
- For Condition 7, similar to Condition 5, ITC states that the Commission could not “unilaterally reverse the transfer of control to MISO of the transmission assets that would then be owned by ITC Arkansas.”¹⁰⁷

¹⁰² Compliance Testimony of Hugh T. McDonald, Exhibit HTM-9, Docket No. 10-011-U, August 24, 2012.

103 ITC's Response to Staff Data Request APSC 22-7.

104 ITC's Response to Staff Data Request APSC 22-8.

105 The Application asks that TCA be recognized as a public utility in Arkansas subject to Commission jurisdiction, which presumably remains with TCA as it is moved to ITC and renamed as ITC Arkansas. Application at page 7.

106 ITC's Response to Staff Data Request APSC 22-9.

107 ITC's Response to Staff Data Request APSC 22-10.

- For Condition 8, ITC would not have any agreement with MISO to ensure that the Commission sets the transmission component of rates to serve EAI's bundled load, as the transmission service would be unbundled after the Transaction is completed.¹⁰⁸
- For Condition 14, ITC states that as an independent transmission owner, it would lack the information to estimate the net benefits of MISO membership or the potential exit costs from MISO, but it would be willing to provide the Commission information regarding FERC and MISO policy changes and is willing to collaborate with EAI to produce the requested information to the extent allowed under FERC's Standards of Conduct for Transmission Providers.¹⁰⁹

C. Conclusion

The Transaction terms could significantly alter the value and impact of the Commission's conditions specified in Order Nos. 68 and 72 in Docket No. 10-011-U—conditions that were deemed critical to ensure EAI's transition to MISO is in the public interest. These conditions were reiterated in Order No. 76 approving EAI's membership in MISO, stating that approval is "conditioned upon full and continued compliance by EAI and MISO with each of the Order No. 68 Conditions."¹¹⁰ Moreover, the Transaction may result in a considerable loss of Commission jurisdiction over both EAI and ITC Arkansas's participation in RTO markets.

¹⁰⁸ ITC Response to Staff Data Request APSC 22-11.

¹⁰⁹ ITC Response to Staff Data Request APSC 22-13.

¹¹⁰ Order No. 76, Docket No. 10-011-U (April 8, 2013), p. 11.

6. OTHER BENEFITS CLAIMED BY APPLICANTS ARE NOT COMPELLING OR COULD BE ACHIEVED WITHOUT THE ADDED COSTS OF THE TRANSACTION

In addition to the claimed benefits of the Transaction discussed in Section 4 above, the Application and testimony discusses several other benefits purportedly achieved by the Transaction. These benefits, which can be summarized under the categories of “financial strength” and “singular focus on transmission,” are discussed below.

A. Financial Strength

The Application and testimony make several arguments that the Transaction will yield benefits by taking advantage of ITC’s financial strength and will improve Entergy’s financial position. Many of the benefits cited are not quantified or quantifiable, and others are likely achievable without the costs associated with the Transaction.

1. CAPITAL EXPENDITURE REQUIREMENTS

One of the primary benefits of the Transaction, as stated in the Application, is ITC’s ability to better address upcoming capital requirements:

The ITC Transaction offers the financial strength of ITC and improves that of EAI and the other Entergy Operating Companies to support the escalating capital expenditure requirements facing the electric industry over the next decade and beyond due to challenges and opportunities associated with increasing regulatory requirements and modernization of the U.S. electric grid.¹¹¹

These escalating requirements are discussed by several witnesses for the Applicants.¹¹² Mr. McDonald claims that “[t]he ITC Transaction eliminates the amount of capital that EAI would be expected to incur to fund future transmission investment and therefore alleviates a significant financing burden.”¹¹³ He continues, noting that “EAI’s projected

¹¹¹ Application, p. 26.

¹¹² See, e.g., Direct Testimony of Theodore H. Bunting, Jr. (September 28, 2012) at 20:9-22:8; Direct Testimony of Jay A. Lewis (September 28, 2012) at 5:17-10:21; Direct Testimony of Hugh T. McDonald (September 28, 2012) at 21:15-24:3.

¹¹³ Direct Testimony of Hugh T. McDonald (September 28, 2012), pp. 21:18-22:1.

capital spending for transmission is expected to exceed \$960 million through 2018, which is 143 percent of EAI's 2011 transmission rate base."¹¹⁴

Challenges posed by capital expenditures are common in the electricity industry and are not unique to Entergy. In fact, testimony filed by Michael Tennican on behalf of EAI explains in detail that the industry as a whole is facing escalating capital expenditure requirements and many other utilities are largely in the same position as EAI.¹¹⁵

Utilities across the country are facing similar pressures, yet few are divesting their transmission assets. There are many options to manage the capital requirements for the various elements of utility operations, such as:

- Short- or long-term energy market purchases can allow a delay in generation investment.
- Merchant transmission projects can reduce transmission capital requirements.

EAI has not provided evidence that it has evaluated any other options to address the capital challenges other than the proposed Transaction with ITC.

2. FINANCIAL FLEXIBILITY

Related to the purported benefit related to capital expenditure challenges is the claim by Applicants that the Transaction will yield benefits from increased financial flexibility. The Application summarizes this benefit, stating:

[T]he ITC Transaction will provide enhanced flexibility for EAI to focus its capital on generation and distribution. The separate balance sheets of ITC and EAI will more effectively deal with rising capital investment requirements facing the industry and provide a greater ability to respond to the financial challenges of storm restoration and other unforeseen events.¹¹⁶

The benefits of financial flexibility are also discussed in testimony of various witnesses.¹¹⁷

Overall, the Applicants claim that the Transaction benefits EAI by providing financial flexibility due to reduced debt burden and a reduction in future capital spending obligation. Additionally, they claim that since the transmission business is cash flow negative, the removal of this obligation will put EAI in a stronger position to make generation and distribution investments.

114 *Id.* at p. 22:9-11

¹¹⁵ Direct Testimony of Michael L. Tennican (September 28, 2012), pp. 8-35.

¹¹⁶ Application, p. 33.

¹¹⁷ See, e.g., Direct Testimony of Jay A. Lewis (September 28, 2012) at 10:23-14:8, 17:7-21:13; Direct Testimony of Joseph L. Welch (September 28, 2012) at 50:15-51:6; Direct Testimony of Theodore H. Bunting, Jr. (September 28, 2012) at 21:10-23:15.

The benefits of financial flexibility are not quantified, nor have the Applicants adequately provided analysis demonstrating how changing ownership will address the negative cash flow which characterizes the transmission business.¹¹⁸ The only explanation provided in response to data requests was that ITC would achieve stronger cash flow through its proposed ROE, capital structure, and forward-looking formula rates.¹¹⁹ This response essentially refers to increasing the revenue requirement recovered from ratepayers.

The Application does not present any evidence that EAI has evaluated alternative options to achieving these benefits without the increased ratepayer costs associated with ITC ownership.

3. CREDIT STRENGTH

Due to the increased capital expenditures and negative cash flow discussed above, the Applicants argue that ITC's superior credit quality will yield benefits for ratepayers and that relieving the capital spending burden from EAI will help protect it from a potential credit downgrade.

ITC witness Cameron Bready analyzed the potential savings from a lower cost of debt. He assumed that ITC will be able to borrow capital at an interest rate of 3.5%, compared to a forecasted average Entergy rate of 6% and EAI rate of 5.29%. His analysis found that from 2014-2018, the cost of debt for the transmission business under ITC ownership would be between \$99 million to \$123 million less than under Entergy ownership on a net present value (NPV) basis. For Arkansas assets, this figure is \$20 million to \$23 million.¹²⁰

The vast majority of these benefits derive from the recapitalization of Entergy's existing debt related to the transmission business under ITC's cost of debt.¹²¹ The Applicants have not explained why, absent the Transaction, EAI would not refinance its existing debt to take advantage of lower borrowing rates currently available.

Despite the magnitude of the benefit from debt cost savings the Applicants have calculated, it does not nearly begin to offset the additional cost to ratepayers imposed by the Transaction. In fact, the impact on transmission revenue requirement presented in Table 5 above is a net impact already incorporating the offsetting benefits of a lower cost of debt.

¹¹⁸ EAI's Response to Staff Data Request APSC 28-6.

ITC's Response to Staff Data Request APSC 27-1.

¹¹⁹ ITC's Response to Staff Data Request APSC 27-1(a).

¹²⁰ Direct Testimony of Cameron M. Bready (September 28, 2012), pp. 18:21-22:19.

¹²¹ Id. at 21:7-22:9.

C. Conclusion

The Application relies on a detailed accounting of several characteristics of ITC operation to support the claimed benefits of the Transaction. Of the benefits discussed above, only debt cost savings are quantifiable. In addition to being somewhat speculative, the magnitude of benefits has not been estimated by Applicants.

In many instances, the claimed benefits of ITC ownership are accessible to EAI, for example, through alternative ratemaking or third party coordination (e.g., with merchant transmission operators). EAI has not provided any evidence that it has evaluated these options to compare the costs and benefits with the proposed Transaction.

Despite requests, EAI and ITC have been unable to quantify or estimate the magnitude of a majority of the claimed benefits of the Transaction. Given the high cost of the Transaction to EAI ratepayers estimated by the Applicants and discussed previously in this report, the lack of consideration of alternatives is concerning.

7. OTHER ISSUES

A. RMT Transaction Structure

The only benefits of the RMT structure to ratepayers identified by the Applicants relate to the ADIT balances and tax basis of the assets. The Applicants have stated that the structure of the Transaction preserves the current ADIT and tax basis in the transfer of the assets to ITC. However, despite the purported benefits of the RMT structure, the rates paid by retail ratepayers and wholesale customers will increase.

In addition, the RMT structure involves regulatory risk. Entergy has included all of the transmission businesses owned by its OpCos in the Transaction. Entergy is seeking regulatory approvals in Arkansas and each of the other state jurisdictions where Entergy operates transmission. EAI has stated that all regulatory approvals are necessary as conditions of consummation of the Transaction and that it will not speculate on what other OpCos will do if the APSC does not approve the request.¹²⁹ Conversely, APSC approval alone is not sufficient to allow the Transaction to proceed. Given the integrated nature of the Transaction, however, the exclusion of one jurisdiction's assets would alter the value exchanged and conflict with the contractual requirements established for the Transaction.

B. ITC as Transmission Operator

The transmission system is a critical element of ensuring safe and reliable energy delivery to Arkansas customers. As such, ensuring the capability of the company operating and planning the transmission system is a key component of determining whether or not the Transaction is in the public interest.

The Applicants have represented that ITC would be a capable operator and planner of what is currently the Entergy transmission system. The record in this docket, however, provides some conflicting evidence regarding ITC's capabilities.

[REDACTED]

[REDACTED]

[REDACTED]¹³⁰ The presentation slides are heavily redacted and considerable portions of the due diligence assessment were withheld as privileged. [REDACTED]

[REDACTED]

¹²⁹ EAI's Response to Staff Data Request APSC 11-14.

¹³⁰ HSPI attachment to EAI's Response to Staff Data Request APSC 11-1, Addendum 2. "HSPM Dec 2 2011 Entergy Corp Board Presentation Materials"

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

Notwithstanding these concerns, the Transaction was approved by the Entergy Board of Directors.

Staff has requested due diligence reports from both Entergy and ITC. Both parties have withheld the reports as privileged.^{131, 132} Through its attorneys, Staff formally requested from Entergy a selective waiver of privilege on the due diligence materials to aid the evaluation of ITC as a potential transmission owner in Arkansas, and consequently the assessment of whether or not the Transaction is in the public interest. EAI declined to waive privilege.

[REDACTED]

[REDACTED] the Application and supporting testimony claim that improved storm response and maintenance are benefits of the Transaction.

While ITC has substantial experience with transmission planning and operations, there are still some serious outstanding concerns identified by Entergy, and Entergy has withheld substantial information related to its reservations about ITC's capabilities. Since the Transaction would result in a doubling of ITC's transmission assets and operations, it is important to ensure its preparedness and competency to ensure continued reliable service to Arkansas customers.

¹³¹ EAI's Response to Staff Data Request APSC 18-1.

¹³² ITC's Response to Staff Data Request APSC 19-1.

The Applicants have not established ITC's competency to operate the EAI transmission system in Arkansas. Moreover, without access to Entergy's due diligence reports, ITC's competency cannot be assessed by the Parties or the Commission.

8. CONCLUSIONS

The foregoing report represents Staff's review and analysis of the record as it currently stands. Based on Staff's review of the Application, supporting testimony, and evidence on the record in this matter, Staff offers the following conclusions.

A. Application as filed does not meet public benefits standard the Commission articulated in the SWEPCO Order

In APSC Docket No. 11-050-U, the Commission articulated that it "is not opposed to independent transmission companies or independent transmission construction and, in fact, it strongly supports the improvement of the transmission system in this state and region as a means to lower energy costs for Arkansas ratepayers."¹³³ However, in that same Order the Commission stated that a determination of public interest requires that the applicants provide evidence that the benefits are concrete and "significant enough to outweigh the potential for increased retail rates."¹³⁴

Based on the standard articulated in the SWEPCO docket, the Applicants in this Docket have not demonstrated concrete benefits that outweigh the significant quantitative costs.

B. The Transaction imposes significant additional costs to ratepayers

The shift from transmission charges utilizing the Bundled Load exemption to rates under the MISO tariff is expected to result in a significant increase in transmission revenue requirement for Arkansas ratepayers. The shift to ITC ownership adds additional costs based on its capital structure, a higher return on equity, and use of a forward looking test year with an annual true-up provision. In addition, the costs may be higher if ITC obtains incentive ROE approval and adds transmission investment beyond those known additions included in ITC's cost estimates.

The Applicants have provided evidence demonstrating that the Transaction will result in significant increases in transmission charges for both retail ratepayers and wholesale customers in Arkansas. Overall, the change in ownership will result in an increase in annual transmission revenue requirement of [REDACTED] each year for the first five years. Even if the impact of the forward test year and annual true-up provisions for FERC ratemaking is excluded, as the Applicants propose, the transmission revenue requirement still increases by [REDACTED] over the status quo each year from 2014-

¹³³ Order No. 6, APSC Docket No. 11-050-U at 21.

¹³⁴ Id.

2018. This estimate includes offsetting quantitative benefits derived from a purportedly lower cost of debt under ITC and the preservation of the current ADIT and tax basis.

The increase will likely be higher, but there is currently insufficient evidence to determine the actual figures because ITC has not provided information on capital expenditures that will accompany additional transmission projects beyond Entergy's current forecast. It is also possible that ITC will seek a higher ROE from FERC in the future, and ITC has expressly stated that it believes it is eligible for an incentive ROE adder. Each of these uncertainties could result in significantly higher rates for Arkansas ratepayers.

C. The Transaction does not yield significant benefits incremental to EAI membership in MISO

The benefits of the Transaction identified by the Applicants are primarily qualitative in nature. Many of these benefits, such as ITC's independence and broad regional view, are substantially similar to benefits of EAI joining MISO, or provide only a small incremental benefit over benefits of EAI as a transmission owning member of MISO.

Additional benefits claimed by the Applicants, such as the increased financial flexibility, could be achieved through other means that do not impose such a high quantitative cost on ratepayers. The Applicants have not sufficiently demonstrated that other benefits are tangible, such as ITC's singular focus on transmission. While the Applicants also claim that customers will benefit from the independence and broad regional view of ITC, the opportunities for economic transmission upgrades to reduce congestion lay primarily in areas other than Arkansas. Additionally, while this provides for the possibility that costs would be shared beyond the region, it also indicates that EAI could be required to pay for projects in excess of the benefits received.

D. The Transaction will render the Commission's evaluation and conditional order in Docket No. 10-011-U obsolete and the APSC will lose jurisdiction

The Commission issued orders in Docket No. 10-011-U to ensure that EAI's transition to MISO was in the public interest. As a result of the Transaction, many of the conditions of MISO membership identified by the Commission in APSC Docket No. 10-011-U that were deemed critical will be voided. Accordingly, the value and impact of the conditions will be altered. As ITC will be primarily operating under FERC jurisdiction, the Commission will lose significant jurisdiction over transmission operations and, most notably, transmission rates charged to Arkansas customers. The loss of the Bundled Load exemption shifts transmission rates out of Commission control, to the benefit of the transmission owner and the detriment of the retail ratepayers.

E. Other issues support Commission rejection of the Transaction

The RMT structure of the Transaction preserves the current ADIT and tax basis of the transmission assets, which simply preserves the status quo with respect to this aspect of the transmission rates, rather than providing a true benefit to ratepayers. The RMT structure also requires the transmission assets of all Entergy Operating Companies be included in the Transaction, putting the Transaction and its purported benefits at risk if any one of the retail regulatory commissions does not approve the Transaction.

The safe and reliable delivery of energy to Arkansas customers requires a capable transmission system owner and operator. The Applicants have not provided sufficient evidence to demonstrate that their due diligence concluded that ITC is a qualified and capable transmission system operator.

**EVALUATION OF THE
TRANSACTION TO TRANSFER
THE ENTERGY CORP.
TRANSMISSION BUSINESS TO
ITC HOLDINGS, INC.**

Docket No. 12-069-U

CONFIDENTIAL VERSION

PREPARED FOR

General Staff of the Arkansas
Public Service Commission

PREPARED BY

La Capra Associates, Inc.
One Washington Mall, 9th Floor
Boston, MA 02108
Boston, MA 02108Boston, MA 02108

La Capra Associates

Technical Report – Attachments

April 19, 2013

TECHNICAL REPORT – ATTACHMENTS

**Evaluation of the Transaction to Transfer the Entergy Corp.
Transmission Business to ITC Holdings, Inc.**

Docket No. 12-069-U

In The Matter Of An Application Of Entergy Arkansas, Inc., Mid South TransCo LLC,
ITC Midsouth LLC, Transmission Company Arkansas, LLC, and ITC Holdings Corp.
To Enter Transactions Resulting In A Certificate Of Public Convenience And Necessity
For A New Arkansas Utility To Own EAI's Electric Transmission Facilities

**ATTACHMENT 1:
EAI'S PUBLIC RESPONSES TO DATA REQUESTS**

**ATTACHMENT 2:
ITC'S PUBLIC RESPONSES TO DATA REQUESTS**

**ATTACHMENT 3:
EAI'S PROTECTED RESPONSES TO DATA
REQUESTS**

**ATTACHMENT 4:
ITC'S PROTECTED RESPONSES TO DATA
REQUESTS**

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Attachment 1

EAI's Public Responses to Data Requests

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4. APSC 18-11
5. APSC 21-2
6. APSC 21-5
7. APSC 21-8
8. APSC 21-9
9. APSC 21-11
10. APSC 21-13
11. APSC 28-6

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ENTERGY ARKANSAS, INC.
ARKANSAS PUBLIC SERVICE COMMISSION
Docket No. 12-069-U
Proposed Divestiture of the Transmission Assets Investigation

Response of: Entergy Arkansas, Inc.
to the Ninth Set of Data Requests
of Requesting Party: Arkansas Public Service
Commission Staff

Filed: 11/6/12

Question No.: APSC 9-2

Part No.:

Addendum:

Question:

Please provide all memoranda, research, assessments, or estimates created by or for EAI or Entergy relating to the magnitude of the following benefits for EAI's ratepayers, as defined by Richard C. Riley in his Direct Testimony, along with supporting workpapers in electronic format with formulas intact and readable.

- a. The ability to attract and retain highly-qualified personnel;
 - b. Better pricing for equipment from increased leverage of purchasing power;
 - c. Efficiencies in supply chain management;
 - d. Storm response enhancement;
 - e. ITC's systematic approach to outage reduction; and
 - f. ITC's broader regional perspective for transmission planning.
-

Response:

- a. As Mr. Riley explained in his Direct Testimony, EAI believes that by combining the Entergy Operating Companies' and ITC's transmission businesses, there will be a broader base and a more competitive environment for employees who wish to specialize in transmission services. There will also be a greater opportunity for career progression in a larger organization, which should enhance the ability to attract and retain the best available prospects in the industry. EAI has no additional memoranda, research, assessments, or estimates created by or for EAI or the other Entergy Operating Companies relating to the magnitude of the benefits to EAI's ratepayers.

- b. As Mr. Welch testified on pages 35 and 36 of his direct testimony, ITC's large size has allowed ITC to leverage its purchasing power into good pricing for transmission related equipment. EAI believes that an even larger transmission organization could reasonably expect to have more opportunities for leverage with suppliers in transmission related equipment procurement. EAI has no additional memoranda, research, assessments, or estimates created by or for EAI or the other Entergy Operating Companies relating to the magnitude of the benefits to EAI's ratepayers.
- c. Mr. Jipping described on pages 56 – 62 of his direct testimony about ITC's efficiencies and successes in supply chain management. EAI believes this will provide opportunities for cost savings with the Entergy Operating Companies' current suppliers and/or with ITC's existing suppliers. EAI has no additional memoranda, research, assessments, or estimates created by or for EAI or the other Entergy Operating Companies relating to the magnitude of the benefits to EAI's ratepayers.
- d. Mr. Jipping explains ITC's Storm Restoration methods, as well as how ITC plans to coordinate with EAI on pages 50 – 56 of his direct testimony. EAI witness Brady Aldy also discusses this in his direct testimony. EAI has no additional memoranda, research, assessments, or estimates created by or for EAI or the other Entergy Operating Companies relating to the magnitude of the benefits to EAI's ratepayers.
- e. As stated on page 17 of Mr. Riley's direct testimony, ITC has a systematic approach to outage reduction, which includes a cross-functional committee comprised of operations, engineering, and technical areas that meets monthly to review every transmission line outage, outage causes and remediation. EAI believes that implementing this practice in its region will drive improved reliability performance. Mr. Jipping explains the practice in his testimony. EAI has no additional memoranda, research, assessments, or estimates created by or for EAI or the other Entergy Operating Companies relating to the magnitude of the benefits to EAI's ratepayers.
- f. EAI has not prepared any memoranda, research, assessments, or estimates related to subpart f. ITC has provided information regarding its planning perspective and provides support for its analysis in the direct testimonies of Pfeifenberger, Welch and Vitez.

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ENTERGY ARKANSAS, INC.
ARKANSAS PUBLIC SERVICE COMMISSION
Docket No. 12-069-U
Proposed Divestiture of the Transmission Assets Investigation

Response of: Entergy Arkansas, Inc.
to the Eleventh Set of Data Requests
of Requesting Party: Arkansas Public Service
Commission Staff

Filed: 11/8/12

Question No.: APSC 11-11

Part No.:

Addendum:

Question:

Reference Section III of the Lewis Direct Testimony, pages 32-44.

- a. Provide all workpapers used to calculate the estimated impact on retail customer bills (34:16-20). Workpapers should be provided in electronic spreadsheet format with formulas intact.
 - b. Provide an analysis calculating the total percent increase in the amount a typical residential customer will pay specifically for transmission service in 2014. Provide all workpapers used to support this analysis in electronic spreadsheet format with formulas intact.
-

Response:

- a. See the Highly Sensitive workpapers previously provided by EAI witness Jay Lewis entitled:

HSPI_Lewis-Rate_Effects_Workpaper_1.xlsx
HSPI_Lewis-Rate_Effects_Workpaper_2.xlsx
- b. Retail customers do not pay for transmission service. They pay for bundled electric service. The revenue requirement for the transmission component of electric service makes up a small portion of a customer's bill for electric service. As indicated in Mr. Lewis' testimony, when operating expenses and other components of revenue requirements are taken into account, the transmission revenue requirement constitutes only approximately 4.3 percent of a typical EAI residential customer total bill based on 2011 average billing data. The WACC-related and other effects of the ITC Transaction discussed in Mr. Lewis' testimony increase that small transmission component by 23%, excluding the timing effect of

use of a forward test year. Accordingly, applying this change to the small, transmission component of the bill produces an estimated, overall typical bill effect of approximately \$1.22, or 1.3%.

See the Highly Sensitive workpaper previously provided by EAI witness Jay Lewis entitled:

HSPI_Lewis-Rate_Effects_Workpaper_2.xlsx

The above-cited calculation was performed by performing the following sequence of operations:

1. Summing cells AP58 and AH83 from tab 'TPZ by State (Retail)' and then subtracting cell AX14 from tab 'TPZ by State (Retail)' in order to calculate the transaction-driven total change in transmission revenue requirement.
2. Dividing that number by cell AH47 from tab 'TPZ by State (Retail)' in order to translate the transaction-driven total change in transmission revenue requirement into a percentage basis.

In Excel formula terms, this sequence of operations can be expressed as:

$$=('TPZ \text{ by State (Retail)}!AP58+'TPZ \text{ by State (Retail)}!AH83-'TPZ \text{ by State (Retail)}!AX14)/'TPZ \text{ by State (Retail)}!AH47$$

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ENTERGY ARKANSAS, INC.
ARKANSAS PUBLIC SERVICE COMMISSION
Docket No. 12-069-U
Proposed Divestiture of the Transmission Assets Investigation

Response of: Entergy Arkansas, Inc.
to the Eighteenth Set of Data Requests
of Requesting Party: Arkansas Public Service
Commission Staff

Filed: 1/11/13

Question No.: STAFF 18-1

Part No.:

Addendum:

Question:

Provide all due diligence reports on ITC's financial and technical capabilities produced by or for EAI or Entergy related to this transaction.

Response:

The requested due diligence reports are protected by the attorney-client privilege and/or the work product doctrine.

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ENTERGY ARKANSAS, INC.
ARKANSAS PUBLIC SERVICE COMMISSION
Docket No. 12-069-U
Proposed Divestiture of the Transmission Assets Investigation

Response of: Entergy Arkansas, Inc.
to the Eighteenth Set of Data Requests
of Requesting Party: Arkansas Public Service
Commission Staff

Filed: 1/11/13

Question No.: STAFF 18-11

Part No.:

Addendum:

Question:

Please provide the specific MISO tariffs that address the Bundled Rate Exemption for retail load. Explain the specific services or service schedules that would not be applicable to bundled retail load. Explain the specific services or service schedules that would be applicable to bundled retail load. Please list and explain any revenues that MISO would collect from or distribute to bundled retail load.

Response:

The MISO Transmission Owner Agreement ("TOA") addresses the Bundled Load exemption. A copy of the MISO TOA is attached. Appendix C, Section II.A.3.a of the TOA states: "Owners taking Network Transmission Service to serve their Bundled Load shall not pay charges pursuant to Schedules 1 through 6 and Schedule 9 and also shall not be responsible for losses from network resources located within their Local Balancing Authority Areas or pricing zone pursuant to Attachment M. The Owner, however, shall be responsible for losses under Attachment M for network resources located outside of its Local Balancing Authority Area or pricing zone that are within or attached to the Transmission System." Transmission Owners that are Load Serving Entities are responsible for all other schedules (not listed above) under the MISO Tariff for service to Bundled Load. MISO does not collect or distribute any revenues from or to Bundled Load. All collections and distributions relating to Bundled Load are done through Transmission Owners that are Load Serving Entities.

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ENTERGY ARKANSAS, INC.
ARKANSAS PUBLIC SERVICE COMMISSION
Docket No. 12-069-U
Proposed Divestiture of the Transmission Assets Investigation

Response of: Entergy Arkansas, Inc.
to the Twenty-First Set of Data Requests
of Requesting Party: Arkansas Public Service
Commission Staff

Filed: 2/12/13

Question No.: STAFF 21-2

Part No.:

Addendum:

Question:

Reference the Application, page 25, paragraph 35 (*"The Transaction is the final step to be taken by the Entergy Operating Companies in their continuing evolution toward greater transparency and independence in the operation and management of the Entergy Transmission System."*) as well as EAI's Evaluation Report filed on 5/12/2011 in APSC Docket 10-011-U, page 49 (*"RTOs will provide greater independence in the areas of transmission planning and the development and operation of markets."*). Please identify all ways in which the transaction will enhance independence of Entergy's transmission system that are not achievable under Entergy ownership as a transmission-owning member of MISO. Provide all documentation supporting your response.

Response:

The ITC Transaction will enhance independence in two primary ways that are not achievable under Entergy Operating Company ownership. There will be greater independence in transmission planning and MISO governance.

Absent the ITC transaction, the Entergy Operating Companies would participate in MISO as asset owners, market participants, and transmission owners. A utility that participates in MISO in such capacities must develop and submit transmission plans to MISO for consideration in the MISO MTEP process because MISO's transmission planning process originates with transmission owners. Such a utility would also (a) participate in MISO governance as a transmission owner, including voting on items such as the membership of the MISO Board of Directors and changes to the Transmission Owners Agreement, and (b) have FPA Section 205 filing rights related to, among other things, transmission upgrades and cost allocation. While a utility would be obligated to undertake its participation in MISO planning processes in a non-discriminatory manner, and MISO rules ultimately must be approved by FERC as not unduly discriminatory, that situation does not eliminate the perception by other asset owners or market participants that a transmission owner may act in a biased manner in favor of its own generation or load served. See the direct testimony of Theodore Bunting at pp. 12-13 discussing the

existence of such perceptions in the current structure. MISO offers a different structure, but that structure contemplates that transmission owners who also own generation and serve load will have substantial input in transmission planning and RTO governance. See, e.g., MISO TOA, Article II, Section IX; MISO Tariff, Attachment FF.

In contrast, if ITC were the independent owner of the Entergy Transmission System, there would be no basis for perception of bias in transmission planning and MISO governance because ITC is independent of market participants and asset owners. Messrs. Welch and Vitez discuss in their direct testimonies how that model instills greater confidence in the market and leads to more robust transmission planning for the benefit of all market participants (e.g., ITC is better able to coordinate with generators in transmission planning because ITC is not perceived as a competitor).

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ENTERGY ARKANSAS, INC.
ARKANSAS PUBLIC SERVICE COMMISSION
Docket No. 12-069-U
Proposed Divestiture of the Transmission Assets Investigation

Response of: Entergy Arkansas, Inc.
to the Twenty-First Set of Data Requests
of Requesting Party: Arkansas Public Service
Commission Staff

Filed: 2/12/13

Question No.: STAFF 21-5

Part No.:

Addendum:

Question:

Reference Exhibit THB-2 to the testimony of Theodore Bunting. After Step 7 the retirement of historic debt using the proceeds of the new debt issued by the Wires Subs, how will EAI's overall cost of debt change? Provide EAI's current average cost of debt, EAI's expected cost of debt after the transaction, and all documentation and workpapers used to support your response. Workpapers should be provided in electronic spreadsheet format with formulas intact.

Response:

EAI's current weighted average pre-tax coupon is 4.88%. Assuming a June 30, 2013 closing date, EAI's weighted average pre-tax coupon post-transaction should be approximately 4.62% assuming the total amount of debt and particular series of debt targeted to be retired do not change from the current assumptions. This analysis does not take into account the cost of new debt issued at EAI between now and the Transaction date, nor does it take into account securitization debt or debt related to financing nuclear fuel. The foregoing amounts are estimates based on a forecast. The final amounts may vary to the extent forecast assumptions differ from the circumstances that exist at the time of closing. The requested workpaper is attached.

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ENTERGY ARKANSAS, INC.
ARKANSAS PUBLIC SERVICE COMMISSION
Docket No. 12-069-U
Proposed Divestiture of the Transmission Assets Investigation

Response of: Entergy Arkansas, Inc.
to the Twenty-First Set of Data Requests
of Requesting Party: Arkansas Public Service
Commission Staff

Filed: 2/12/13

Question No.: STAFF 21-8

Part No.:

Addendum:

Question:

Condition 4 in Order No. 68 issued by the Commission in Docket 10-011-U
states:

"Should EAI become a member of MISO, EAI shall agree that it will not exit MISO without first filing an application with the Commission seeking its approval for a change of control of its transmission assets. EAI will otherwise retain all of its rights, state and federal, to appeal or seek review of or relief from the decision of the Commission."

Should Entergy and ITC complete the proposed transaction:

- a. Please describe how this condition still applies to EAI, if at all.
- b. If the condition is still relevant when EAI is no longer a transmission-owning member of MISO, how does EAI intend to comply with this condition?
- c. Will this condition apply to ITC after the execution of the transaction? If so, how will EAI ensure that ITC will comply with this condition? Provide any and all documentation supporting this response.

Response:

- a. The question of whether and how a MISO condition would continue to apply to EAI after divestiture of EAI's transmission assets, as well as whether such condition would be relevant at all, calls for speculation and legal conclusions and is a matter for the Commission. Similarly, whether any of the conditions in Order No. 68, as clarified by Order No. 72 should

EAI responds generally that this condition (as with the various conditions of Order No. 68, as clarified by Order No. 72) would continue to apply to EAI, in accordance with the terms of the applicable Commission orders and applicable law (and subject to the applicable reservations of rights reflected in the Commission's Orders), until and unless the Commission modifies or terminates the condition. However, as explained in more detail below, the condition would have less relevance post-ITC Transaction.

Assuming closing of the proposed ITC Transaction, EAI would become a transmission dependent utility ("TDU") and ITC would become the transmission owner of the assets. Post-closing, EAI would still be bound by the condition. While EAI, however, as a TDU technically could terminate its MISO membership, such termination would not affect EAI's status as a transmission customer of ITC, and EAI would not have the authority to transfer control of transmission assets that it no longer owns.

- b. See EAI's response to subpart (a).
- c. Absent some action from the Commission in this docket, this condition would not apply to ITC, which was not a party to Docket 10-011-U, in which this condition was adopted. Because the condition does not apply to ITC, the portion of the request asking how EAI would "ensure compliance" with the condition is not applicable.

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ENTERGY ARKANSAS, INC.
ARKANSAS PUBLIC SERVICE COMMISSION
Docket No. 12-069-U
Proposed Divestiture of the Transmission Assets Investigation

Response of: Entergy Arkansas, Inc.
to the Twenty-First Set of Data Requests
of Requesting Party: Arkansas Public Service
Commission Staff

Filed: 2/12/13

Question No.: STAFF 21-9

Part No.:

Addendum:

Question:

Condition 5 in Order No. 68 issued by the Commission in Docket 10-011-U
states:

"Should EAI become a member of MISO, EAI shall agree that the Commission, sua sponte or upon the motion of any party, after notice and hearing, may direct EAI to exit MISO under the terms of the Memorandum of Understanding or the TOA. EAI will otherwise retain all of its rights, state and federal, to appeal or seek review of or relief from the decision of the Commission."

Should Entergy and ITC complete the proposed transaction:

- a. Please describe how this condition still applies to EAI, if at all.
- b. If the condition is still relevant when EAI is no longer a transmission-owning member of MISO, how does EAI intend to comply with this condition?
- c. Will this condition apply to ITC after the execution of the transaction? If so, how will EAI ensure that ITC will comply with this condition? Provide any and all documentation supporting this response.

Response:

- a-c. See EAI's response to APSC 21-8. EAI would still be bound by the condition. While EAI, however, as a TDU technically could terminate its MISO membership, such termination would not affect EAI's status as a transmission customer of ITC, and EAI would not have the authority to transfer control of transmission assets that it no longer owns.

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ENTERGY ARKANSAS, INC.
ARKANSAS PUBLIC SERVICE COMMISSION
Docket No. 12-069-U
Proposed Divestiture of the Transmission Assets Investigation

Response of: Entergy Arkansas, Inc.
to the Twenty-First Set of Data Requests
of Requesting Party: Arkansas Public Service
Commission Staff

Filed: 2/12/13

Question No.: STAFF 21-11

Part No.:

Addendum:

Question:

Condition 8 in Order No. 68 issued by the Commission in Docket 10-011-U
states:

"Should EAI become a member of MISO, EAI shall not unbundle transmission or seek to make basic changes to transmission service for retail ratemaking without prior APSC approval. EAI shall negotiate a transmission service agreement with MISO that ensures that the APSC continues to determine the transmission component of the rates to serve EAI's bundled retail load."

Should Entergy and ITC complete the proposed transaction:

- a. Please describe how this condition still applies to EAI, if at all.
- b. If the condition is still relevant when EAI is no longer a transmission-owning member of MISO, how does EAI intend to comply with this condition?
- c. Is EAI requesting the Commission unbundle transmission service because of the proposed transaction?
- d. Will this condition apply to ITC after the execution of the transaction? If so, how will EAI ensure that ITC will comply with this condition? Provide any and all documentation supporting this response.

Response:

- a-d. See EAI's response to APSC 21-08. Further responding to subpart (c), the proposed ITC Transaction contemplates EAI's becoming a transmission

dependent utility ("TDU"), and under the terms of the Transaction, ITC would become the transmission owner of EAI's former transmission assets. Accordingly, upon the closing of the ITC Transaction, transmission would become unbundled and the Commission would no longer have jurisdiction with respect to setting retail rates for transmission assets previously owned by EAI. As such, as part of this proceeding, it would be necessary for the Commission to give its approval for the unbundling of transmission as contemplated by Condition No. 8.

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ENTERGY ARKANSAS, INC.
ARKANSAS PUBLIC SERVICE COMMISSION
Docket No. 12-069-U
Proposed Divestiture of the Transmission Assets Investigation

Response of: Entergy Arkansas, Inc.
to the Twenty-First Set of Data Requests
of Requesting Party: Arkansas Public Service
Commission Staff

Filed: 2/12/13

Question No.: STAFF 21-13

Part No.:

Addendum:

Question:

Condition 14 in Order No. 68 issued by the Commission in Docket 10-011-U
states:

"Should EAI become a member of MISO, no later than three years after joining MISO and every two years thereafter, assuming EAI continues as a MISO member, EAI shall file with the Commission a detailed report providing the following information:

- a. The quantified historical net benefits of MISO membership for EAI, as compared to the stand-alone option, as of the date of each of the reports described above;*
- b. The projected net benefits of MISO membership for EAI, as compared to the stand-alone option, for the post-transition period on a bi-annual basis beginning one year after the end of the transition period;*
- c. Any significant changes in FERC RTO policies, rules or regulations, MISO requirements, Day 2 market conditions, or other regulatory or market structure components; and*
- d. An estimate of the costs to exit MISO after the end of the five-year transition period or a specified time thereafter and to transition to a new operating environment such as a different RTO."*

Should Entergy and ITC complete the proposed transaction:

- a. Please describe how this condition still applies to EAI, if at all.

- b. If the condition is still relevant when EAI is no longer a transmission-owning member of MISO, how does EAI intend to comply with this condition?
 - c. Please explain how, if at all, EAI would collaborate with ITC to produce such information.
 - d. Will this condition apply to ITC after the execution of the transaction? If so, how will EAI ensure that ITC will comply with this condition? Provide any and all documentation supporting this response.
-

Response:

- a,b,d. See EAI's response to APSC 21-8. EAI would remain in a position, after the ITC Transaction closes, to provide the Commission with the estimated net benefits and information on changes in FERC policy or MISO rules as called for by Condition No. 14(a), (b), (c), and (d), although the Commission may wish to consider as part of this proceeding whether the information called for by Condition No. 14 remains useful in light of the limitations on EAI's authority to transfer control of the subject assets described in EAI's response to APSC 21-8.
- c. EAI objects to the extent that this question calls for speculation. Without waiving the objection, EAI states that it is willing to coordinate with ITC regarding compiling non-privileged information that may be requested by the Commission to the extent such information exists and is within EAI's possession and control. Such coordination would also be subject to the limits of the FERC Standards of Conduct. EAI further states that it anticipates relying in part on the prior filings of the SPP-member utilities with respect to the similarly-worded requirement imposed upon them in Order No. 1, issued in APSC Docket 04-137-U.

11

ENTERGY ARKANSAS, INC.
ARKANSAS PUBLIC SERVICE COMMISSION
Docket No. 12-069-U
Proposed Divestiture of the Transmission Assets Investigation

Response of: Entergy Arkansas, Inc.
to the Twenty-Eighth Set of Data Requests
of Requesting Party: Arkansas Public Service
Commission Staff

Filed: 3/11/13

Question No.: STAFF 28-6

Part No.:

Addendum:

Question:

Reference the Direct Testimony of Jay Lewis, pages 17-23, discussing the negative cash flow nature of Entergy's transmission business.

- a. Provide any documentation and work papers supporting Figures 1, 2, and 3. Work papers should be provided in electronic spreadsheet format with formulas intact.
 - b. Please explain how the change in ownership will address the conditions leading to the negative cash flow described in the Lewis Testimony
 - c. Provide any documentation and work papers demonstrating the impact that the change in ownership to ITC will have on the cash flow of the transmission business. Work papers should be provided in electronic spreadsheet format with formulas intact.
-

Response:

- a. Please see the Highly Sensitive workpaper provided by EAI witness Jay Lewis titled:

HSPI_Lewis_Bunting_Testimony_Capital_Workpaper.xlsx

Support for Figures 1, 2, and 3 in Mr. Lewis's testimony can be found in the tab titled "Testimony #s".

Support for the significantly higher forecasted transmission capital spending versus transmission depreciation through 2018 for both the Entergy Operating Companies and EAI, as presented in Figure 1, can be found in cells J54 and J57 for the Entergy Operating Companies and cells C54 and C57 for EAI in particular.

Support for Figure 2 showing that transmission is forecasted to be the largest functional contributor to the shortfall between total investment needs and internally generated funds for the period 2012 – 2018 can be found in cells J60:J67 and J70:J72 for the Entergy Operating Companies, and cells C60:C67 and C70:C72 for EAI in particular.

Support for the pronounced positive effect of the ITC Transaction on EAI's and the other Entergy Operating Companies' projected cash flow, as shown in Figure 3, can be found in cells J78:J81 for the Entergy Operating Companies and cells C78:C81 for EAI in particular.

- b. The negative cash flow discussed by Mr. Lewis is a result of transmission capital exceeding the operating cash flows produced by the transmission business. Accordingly, the transaction relieves the Entergy Operating Companies of this negative cash flow by removing the capital expenditures associated with transmission.

Mr. Lewis notes in his testimony that "the net effect of the ITC transaction is a 20 percent improvement (57 percent improvement for EAI) in cash flow, with projected cash flow increasing by over \$860 million (approximately \$350 million for EAI) over 2014-2018 if [the Entergy Operating Companies] no longer own transmission assets." Further, he goes on to state that "[t]he positive cash flow effect of the ITC Transaction means there is more cash available to pay down debt or invest back into the business. As such, there is greater potential to accelerate capital projects of local interest, such as economic development."

- c. Questions pertaining to the cash flow of the transmission business under ITC ownership should be directed to ITC.

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Attachment 2

ITC's Public Responses to Data Requests

1. APSC 10-20
2. APSC 12-6
3. APSC 14-2
4. APSC 15-7
5. APSC 19-1
6. APSC 22-1
7. APSC 22-7
8. APSC 22-8
9. APSC 22-9
10. APSC 22-10
11. APSC 22-11
12. APSC 22-13
13. APSC 24-2
14. APSC 27-1
15. APSC 27-2

1

Data Request No. APSC 010-20

Data Request: Reference the Pfeifenberger Direct Testimony. Provide an estimate of the cost allocation to Arkansas ratepayers for the illustrative projects considered under MISO's cost allocation policies.

Response: The propose of Mr. Pfeifenberger's testimony was to present an indicative analysis of the potential benefits of a portfolio of "strategic" transmission projects that are illustrative of the types of projects that ITC would be uniquely positioned to plan, develop, and implement through its broad-based independent planning process. This did not require the determination of how project costs would be allocated to transmission and retail customers within and outside the Entergy Region. However, as also noted in Mr. Pfeifenberger's testimony, the allocation of project costs would follow MISO's cost allocation process, as modified for the transitional period immediately following MISO obtaining functional control of the transmission system now owned by the Entergy Operating Companies, which aligns the costs of projects with the benefits received. In some instances, projects might also be supported through interregional cost-sharing with neighboring systems. Thus, the costs and wide range of potential benefits of this illustrative portfolio of strategic projects might be shared by the Entergy Operating Companies' customers and other market participants in the Entergy Region as well as customers in adjoining systems and regions. In other words, cost allocation would generally align the costs of projects with the benefits received.

While the share of strategic project costs allocated to Arkansas might be as low as zero if these projects were to be pursued further, Mr. Pfeifenberger did not estimate total Arkansas-specific benefits provided by the strategic set of projects.

For some information on how benefits are allocated between the Entergy Region and non-Entergy Regions, please see Highly Sensitive Protected Information document Bates-stamped ITC-AR-008364 provided in response to APSC 010-17. Rows 48 through 68 of the 'Figure 1' tab of ITC-AR-008364 are a summary of benefits to inform cost allocation. Also, the 'ProMod results' tab of the same spreadsheet shows only the adjusted production cost savings (a subset of total benefits) by Entergy Operating Company.

2

Data Request No. APSC 012-6

Data Request: Please provide all estimates in ITC's possession of the magnitude of the following benefits as defined by Richard C. Riley in his Direct Testimony along with supporting workpapers in electronic format with formulas intact and readable.

- a. The ability to attract and retain highly-qualified personnel;
- b. Better pricing for equipment from increased leverage of purchasing power;
- c. Efficiencies in supply chain management;
- d. Storm response enhancement;
- e. ITC's systematic approach to outage reduction; and
- f. ITC's broader regional perspective for transmission planning.

Response: a. ITC is not aware of any documents responsive to Request 12-6(a). However, ITC believes that by becoming a larger organization after approval of the transaction, it will be able to offer more opportunities for employee growth and development. ITC also believes that organizations with more growth opportunities enjoy higher retention rates and an increased ability to attract talented and highly-qualified personnel. Additional non-privileged, non-confidential information responsive to this request is contained in the pre-filed, direct testimony of Richard C. Riley, filed with the APSC as Document 17 in Docket no. 12-069-U. There, Mr. Riley explains that, by combining the Entergy Operating Companies' and ITC's transmission businesses, there will be greater opportunity for career progression in a larger organization, which should enhance the ability to attract and retain the best available prospects in the industry.

b. Non-privileged, non-confidential, responsive documents can be found on ITC's Online Data Room, Bates-stamped ITC-AR-009064 and ITC-AR-009066. Additional non-privileged, non-confidential information responsive to this request is contained in the pre-filed, direct testimony of Joseph Welch, filed with the APSC as Document 21 in Docket no. 12-069-U at pages 35-36. Pursuant to Mr. Welch's testimony, ITC has developed strategic alliance relationships with its vendors. Those relationships, coupled with large volume purchases of transmission equipment, allows ITC to leverage its purchasing power into better pricing for equipment. ITC anticipates

that, post-transaction approval, the increased company size will permit ITC to successfully pursue further efficiencies.

c. Non-privileged, non-confidential, responsive documents can be found on ITC's Online Data Room, Bates-stamped ITC-AR-008953 to ITC-AR-009005 and ITC-AR-009064. Additional non-privileged, non-confidential information responsive to this request is contained in the pre-filed, direct testimony of Jon E. Jipping, filed with the APSC as Document 24 in Docket no. 12-069-U at pages 56-62. Specifically, and as set forth in Mr. Jipping's testimony, ITC has successfully leveraged numerous supply chain relationships to obtain competitively priced goods and services in a timely manner. Post-transaction approval, and as an organization with a larger footprint, ITC believes that it will be able to further leverage its supply chain relationships to ensure continued supply chain efficiencies and competitive pricing.

d. Non-privileged, non-confidential information regarding ITC's storm restoration methods and its plans to coordinate with Entergy is contained in the pre-filed, direct testimony of Jon E. Jipping, filed with the APSC as Document 24 in Docket no. 12-069-U at pages 50-56. Entergy Witness S. Brady Aldy confirms that these plans will not impede the speed or efficiency of power restoration efforts, and that ITC's plan will be seamless to Entergy's customers and stakeholders. See the pre-filed, direct testimony of S. Brady Aldy, filed with the APSC as Document 14 in Docket no. 12-069-U at page 18.

Additional non-privileged, non-confidential, responsive documents can be found on ITC's Online Data Room, Bates-stamped ITC-AR-008932 to ITC-AR-009005 and ITC-AR-009064.

e. In his pre-filed, direct testimony filed with the APSC as Document 24 in Docket no. 12-069-U, Jon E. Jipping describes ITC's systematic approach to outage reduction. Entergy Witness Richard C. Riley also describes this approach in his pre-filed, direct testimony, filed with the APSC as Document 17 in Docket no. 12-069-U at page 17. ITC believes that implementing its systematic approach to outage reduction will result in improved reliability performance in the region. In his testimony, Mr. Jipping discusses

the value that improved reliability brings to the transmission system. See the pre-filed, direct testimony of Jon E. Jipping filed with the APSC as Document 24 in Docket no. 12-069-U at pages 43-45 and supporting exhibits.

Additional non-privileged, non-confidential, responsive documents can be found on ITC's Online Data Room, Bates-stamped ITC-AR-008932 to ITC-AR-009005. The responsive document, SGS Benchmarking Study, was attached to the Direct Testimony of Mr. Jon E. Jipping as confidential Exhibit JEJ-6. Additional responsive documents Bates-stamped ITC-AR-009075 to ITC-AR-009076 constitute Confidential Information and are being provided on disc with this response to those Reviewing Representatives of Staff and the other official parties to this Docket who have executed an Affidavit of Non-Disclosure pursuant to the Interim Protective Order in this Docket.

f. Non-privileged, non-confidential information responsive to this request is contained in the pre-filed, direct testimony of Johannes P. Pfeifenberger, filed with the APSC as Document 25 in Docket no. 12-069-U.

Additional non-privileged, non-confidential, responsive documents can be found on ITC's Online Data Room, Bates-stamped ITC-AR-009044 to ITC-AR-009045 and ITC-AR-009067 to ITC-AR-009074.

3

Data Request No. APSC-014-2

Data Request: Reference the Direct Testimony of Joseph Welch, pages 30-45, related to ITC's "Second Beneficial Attribute." Provide all reports, memoranda, or other documentation demonstrating that:

- a. ITC's structure as a non-vertically integrated utility yields benefits to EAI customers
- b. These benefits are not achievable under EAI ownership of the transmission assets

Response: The testimony of Joseph Welch and other witnesses supporting the joint application submitted by ITC and EAI demonstrates that ITC's structure will yield benefits to EAI's customers that are not achievable under EAI ownership of transmission assets. ITC does not have additional reports, memoranda, or other documentation to add to Mr. Welch's direct testimony.

4

Data Request No. APSC-015-7

Data Request: Does ITC have any plan or intention to issue more common shares prior to exchanging ITC stock for ownership units with Entergy Corporation shareholders as part of the transaction? If so, explain why more shares may be issued, how many shares and the impact on the transaction.

Response: ITC does not have any plan or intention to publicly issue more common shares prior to exchanging ITC stock for ownership units with Entergy Corporation shareholders as part of the transaction. ITC does, however, have employee equity compensation programs through which common shares are issued, and ITC plans to continue to utilize those programs in the normal course of business. ITC is specifically authorized to continue to utilize those programs, in the ordinary course and consistent with past practice, under the transaction agreements. Such programs are as follows:

New Hire Grants: Currently, newly hired employees are granted shares of restricted stock on their hire date. These restricted shares have a 5 year cliff vest and are forfeited if the employee terminates employment prior to the 5 year anniversary under most circumstances.

Annual Long Term Incentive Awards: Currently, all employees are eligible to participate in the ITC Long-Term Incentive Plan (LTIP) and to be awarded annual grants of restricted stock and/or stock options under the LTIP. These awards are generally made in May of each year, subject to approval of the Compensation Committee of the Board of Directors. ITC anticipates making these awards in May 2013.

Employee Stock Purchase Plan: ITC offers an employee stock purchase plan through which eligible employees can purchase ITC stock at a 15% discount, with purchases being made four times a year.

Exercising of Stock Options: As mentioned above, ITC issues stock options as a form of employee compensation. It is anticipated that employees will exercise stock options which would result in issuance of shares.

The number of common shares that might be issued prior to exchanging ITC stock for ownership units with Entergy Corporation shareholders as part of the transaction under the foregoing programs has been estimated as disclosed on page 46 (Note 4 of the Unaudited Pro Forma Condensed Combined Consolidated Financial Statements) in ITC's Amendment No. 1 to Form S-4 filed with the Securities and Exchange Commission ("SEC") on or about December 3, 2012. The Amendment No. 1 to Form S-4 referenced above is publicly available through the SEC website. Furthermore, the Amendment No. 1 to Form S-4 can be found on ITC's Online Data Room, Bates-stamped ITC-AR-010712 to ITC-AR-011263. As set forth in the Amendment No. 1 to Form S-4, Entergy shareholders are to receive approximately 50.1% of ITC's common stock on a "fully diluted basis" in connection with the merger calculated as 52,772,253 shares. The share amount was computed using the number of shares of ITC common stock outstanding as of September 30, 2012, adjusted for the 50.1% ownership of Entergy. In addition, based on current knowledge, it is anticipated that ITC will issue approximately 140,430 shares of ITC common stock as replacement awards for Entergy equity-based awards held by employees of Entergy's Transmission Business. The impact on the transaction from the foregoing employee equity compensation programs is that the more ITC common shares that are outstanding as a result of these programs at the time that the closing of the transaction occurs, the higher the amount of ITC's common stock that will have to be issued to Entergy shareholders to meet the 50.1% threshold.

SELECTED FINANCIAL STATEMENT DATA

Selected Historical Combined Financial Data of Entergy's Transmission Business

Entergy's Transmission Business' selected combined statement of income data for the three years ended December 31, 2011, 2010 and 2009 and combined balance sheet data as of December 31, 2011 and 2010 have been derived from Entergy's Transmission Business' audited combined financial statements, included elsewhere in this proxy statement/prospectus. Entergy's Transmission Business' selected combined balance sheet data as of December 31, 2009, 2008, and 2007 and its selected statements of income data presented below for the years ended December 31, 2008 and 2007 have been derived from Entergy's Transmission Business' historical accounting records, which are unaudited and are not included in this proxy statement/prospectus. Entergy's Transmission Business' selected combined statement of income data for the nine months ended September 30, 2012 and 2011 and selected combined balance sheet data as of September 30, 2012 have been derived from Entergy's Transmission Business' unaudited condensed combined financial statements, included elsewhere in this proxy statement/prospectus. The selected historical combined financial data below is not necessarily indicative of the results that may be expected for any future period. This information should be read in conjunction with "Management's Discussion and Analysis of Financial Condition and Results of Operations for Entergy's Transmission Business" and the financial statements of Entergy's Transmission Business and the notes thereto included elsewhere in this proxy statement/prospectus.

The financial information of Entergy's Transmission Business included in this proxy statement/prospectus has been derived from the financial statements and accounting records of Entergy and reflects assumptions and allocations made by Entergy. The financial position, results of operations and cash flows of Entergy's Transmission Business presented may be different from those that would have resulted had Entergy's Transmission Business been operated as a stand-alone company. Additionally, the financial position, results of operations and cash flows of Entergy's Transmission Business presented reflect its existing state and local jurisdictional rate regulation as a component of the Utility Operating Companies, as compared to the FERC rate regulation expected for Entergy's Transmission Business under ITC's ownership. As a result, the historical financial information of Entergy's Transmission Business is not a reliable indicator of future results. See "Risk Factors."

	Entergy's Transmission Business						
	Nine Months Ended September 30,		Year Ended December 31,				
	2012	2011	2011	2010	2009	2008	2007
(In thousands)	(unaudited)					(unaudited)	(unaudited)
Statement of Income Data:							
Operating revenues	\$ 498,942	\$ 505,721	\$ 652,792	\$ 631,742	\$ 582,847	\$ 569,507	\$ 569,998
Operating expenses							
Operation and maintenance	167,226	159,727	218,929	212,113	186,734	189,959	168,151
Depreciation and amortization	108,286	97,966	132,302	127,738	110,294	97,287	94,908
Taxes other than income taxes	37,670	34,148	45,751	42,052	38,346	36,473	33,668
Total operating expenses	313,182	291,841	396,982	381,903	335,374	323,719	296,727
Operating income	185,760	213,880	255,810	249,839	247,473	245,788	273,271
Other expenses (income)							
Interest expense	59,959	47,003	63,247	79,041	79,734	70,782	59,415
Allowance for equity funds used during construction	(8,112)	(7,714)	(15,122)	(8,388)	(6,195)	(8,439)	(11,894)
Other expense (income)	(1,069)	(1,907)	(1,599)	1,459	(4,697)	(12,921)	(2,608)
Total other expenses (income)	50,778	37,382	46,526	72,112	68,842	49,422	44,913
Income before income taxes	134,982	176,498	209,284	177,727	178,631	196,366	228,358
Income taxes	41,007	65,593	74,460	67,166	68,205	72,265	84,362
Net income	<u>\$ 93,975</u>	<u>\$ 110,905</u>	<u>\$ 134,824</u>	<u>\$ 110,561</u>	<u>\$ 110,426</u>	<u>\$ 124,101</u>	<u>\$ 143,996</u>

	Entergy's Transmission Business					
	As of September 30,		As of December 31,			
	2012	2011	2010	2009	2008	2007
(In thousands)	(unaudited)			(unaudited)	(unaudited)	(unaudited)
Balance Sheet Data:						
Property, plant and equipment—net	\$3,885,501	\$3,666,387	\$3,369,025	\$3,134,123	\$2,981,331	\$2,825,203
Total assets	\$4,250,604	\$4,015,404	\$3,669,588	\$3,450,333	\$3,308,492	\$3,160,214
Long-term debt	—	—	—	—	—	—

Selected Consolidated Historical Financial Data of ITC

The selected consolidated financial data presented below have been derived from, and should be read together with, ITC's consolidated financial statements and the accompanying notes and the related "Management's Discussion and Analysis of Financial Condition and Results of Operations" and "Selected Financial Data" sections included in ITC's Annual Report on Form 10-K, as amended by the Annual Report on Form 10-K/A, for the year ended December 31, 2011 and in ITC's Quarterly Report on Form 10-Q for the nine months ended September 30, 2012, which are incorporated by reference into this proxy statement/prospectus. The summary consolidated financial data below is not necessarily indicative of the results that may be expected for any future period. To find out where you can obtain copies of ITC's documents that have been incorporated by reference, see "Where You Can Find More Information; Incorporation By Reference."

	ITC (a)						
	Nine Months Ended September 30,		Year Ended December 31,				
	2012	2011	2011	2010	2009	2008	2007
(In thousands)	(unaudited)						
Statement of Operations Data:							
Operating revenues	\$608,889	\$555,787	\$757,397	\$696,843	\$621,015	\$617,877	\$426,249
Operating expenses							
Operation and maintenance (b)	90,314	92,486	129,288	126,528	95,730	113,818	81,406
General and administrative (b) (c) (d)	78,791	54,915	82,790	78,120	69,231	81,296	62,089
Depreciation and amortization (e)	78,453	70,338	94,981	86,976	85,949	94,769	67,928
Taxes other than income taxes (f)	44,186	39,620	53,430	48,195	43,905	41,180	33,340
Other operating income and expense—net	(586)	(611)	(844)	(297)	(667)	(809)	(688)
Total operating expenses	291,158	256,748	359,645	339,522	294,148	330,254	244,075
Operating income	317,731	299,039	397,752	357,321	326,867	287,623	182,174
Other expenses (income)							
Interest expense	116,918	110,002	146,936	142,553	130,209	122,234	81,863
Allowance for equity funds used during construction	(15,800)	(12,078)	(16,699)	(13,412)	(13,203)	(11,610)	(8,145)
Loss on extinguishment of debt	—	—	—	—	1,263	—	349
Other income	(2,171)	(2,136)	(2,881)	(2,340)	(2,792)	(3,415)	(3,457)
Other expense	2,473	3,063	3,962	2,588	2,918	3,944	1,618
Total other expenses (income)	101,420	98,851	131,318	129,389	118,395	111,153	72,228
Income before income taxes	216,311	200,188	266,434	227,932	208,472	176,470	109,946
Income tax provision (f)	76,691	71,166	94,749	82,254	77,572	67,262	36,650
Net income	\$139,620	\$129,022	\$171,685	\$145,678	\$130,900	\$109,208	\$ 73,296

ITC (a)							
	Nine Months Ended September 30,		Year Ended December 31,				
	2012	2011	2011	2010	2009	2008	2007
	(unaudited)						
Basic earnings per share	\$ 2.72	\$ 2.52	\$ 3.36	\$ 2.89	\$ 2.62	\$ 2.22	1.72
Diluted earnings per share	\$ 2.68	\$ 2.49	\$ 3.31	\$ 2.84	\$ 2.58	\$ 2.18	1.68
Weighted-average basic shares	50,748,257	50,192,675	50,289,905	49,526,580	49,196,470	48,592,534	42,298,478
Weighted-average diluted shares	51,502,694	50,974,142	51,078,823	50,398,039	50,077,433	49,627,887	43,454,115
Dividends declared per share	\$ 1.0825	\$ 1.0225	\$ 1.3750	\$ 1.3100	\$ 1.2500	\$ 1.1900	1.1300

	ITC (a)						
	As of September 30,		As of December 31,				
	2012	2011	2011	2010	2009	2008	2007
(In thousands)	(unaudited)						
Balance Sheet Data:							
Cash and cash equivalents	\$ 30,026	\$ 48,327	\$ 58,344	\$ 95,109	\$ 74,853	\$ 58,110	\$ 2,616
Working capital (deficit)	(785,818)	(2,413)	(113,939)	69,338	147,335	1,095	(30,370)
Property, plant and equipment—net	3,967,190	3,221,523	3,415,823	2,872,277	2,542,064	2,304,386	1,960,433
Total assets	5,381,172	4,632,859	4,823,366	4,307,873	4,029,716	3,714,565	3,213,297
Long-term debt:							
ITC Holdings	1,193,008	1,459,493	1,459,599	1,459,178	1,458,757	1,327,741	1,687,193
Regulated Operating Subsidiaries	1,213,666	1,117,912	1,185,423	1,037,718	975,641	920,512	556,231
Total long-term debt	2,406,674	2,577,405	2,645,022	2,496,896	2,434,398	2,248,253	2,243,424
Total stockholders' equity	1,349,209	1,206,002	1,258,892	1,117,433	1,011,523	929,063	563,075

	ITC (a)						
	Nine Months Ended September 30,		Year Ended December 31,				
	2012	2011	2011	2010	2009	2008	2007
(In thousands)	(unaudited)						
Other Data:							
Expenditures for property, plant and equipment	\$637,386	\$388,402	\$556,931	\$388,401	\$404,514	\$401,840	\$287,170
Interest paid (net of interest capitalized)	112,040	126,481	142,101	135,771	125,254	102,149	73,489
Income taxes paid	26,024	23,010	34,127	8,844	1,971	2,012	2,058

- (a) ITC Midwest's results of operations, cash flows and balances are included for the periods presented subsequent to its acquisition of the electric transmission assets of Interstate Power and Light on December 20, 2007.
- (b) The reduction in expenses for 2009 compared to 2008 was due in part to efforts to achieve short-term reductions in operation and maintenance expenses and general and administrative expenses to offset the impact of lower network load on cash flows and any potential revenue accrual relating to 2009.

- (c) During 2011 and 2009, we recognized \$2.0 million and \$10.0 million, respectively, of regulatory assets associated with the development activities of ITC Great Plains as well as certain pre-construction costs for the Kansas V-Plan and Kansas Electric Transmission Authority ("KETA") projects. Upon initial establishment of these regulatory assets in 2011 and 2009, \$1.9 million and \$8.0 million, respectively, of general and administrative expenses were reversed of which \$1.4 million and \$5.9 million were incurred in periods prior to 2011 and 2009, respectively. No initial establishment of regulatory assets occurred in 2010 that resulted in a reversal of expenses.
- (d) During 2011 and the nine months ended September 30, 2012, we expensed external legal, advisory and financial services fees of \$7.0 million and \$12.1 million, respectively, relating to the Entergy transaction recorded primarily within general and administrative expenses of which certain amounts are not expected to be deductible for income tax purposes.
- (e) In 2009, the FERC accepted the depreciation studies filed by ITC Transmission and METC that revised their depreciation rates. In 2010, the FERC accepted a depreciation study filed by ITC Midwest which revised its depreciation rates. These changes in accounting estimates resulted in lower composite depreciation rates for ITC Transmission, METC and ITC Midwest primarily due to the revision of asset service lives and cost of removal values. The revised estimate of annual depreciation expense was reflected in 2009 for ITC Transmission and METC and in 2010 for ITC Midwest.
- (f) The increase in the income tax provision for 2008 compared to 2007 was due in part to the implementation of the Michigan Business Tax, which was in effect from 2008 through 2011 and was accounted for as an income tax, compared to the Michigan Single Business Tax in effect prior to 2008 that was accounted for as a tax other than income tax.

Selected Unaudited Pro Forma Condensed Combined Consolidated Information

The unaudited pro forma condensed combined consolidated financial statements (which we refer to as the pro forma financial statements) combine the historical consolidated financial statements of ITC and the historical combined financial statements of Entergy's Transmission Business to illustrate the effect of the merger. The pro forma financial statements were based on and should be read in conjunction with:

- accompanying notes to the unaudited pro forma financial statements;
- ITC's consolidated financial statements for the year ended December 31, 2011 and as of and for the nine months ended September 30, 2012 and the notes relating thereto, incorporated herein by reference; and
- Entergy's Transmission Business's combined financial statements for the year ended December 31, 2011 and as of and for the nine months ended September 30, 2012 and the notes relating thereto included in this proxy statement/prospectus.

The unaudited pro forma condensed consolidated statement of operations (which we refer to as the pro forma statement of operations) for the year ended December 31, 2011 and for the nine months ended September 30, 2012, give effect to the merger as if it occurred on January 1, 2011. The unaudited pro forma condensed consolidated balance sheet (which we refer to as the pro forma balance sheet) as of September 30, 2012, gives effect to the merger as if it occurred on September 30, 2012.

The pro forma financial statements have been presented for informational purposes only and are not indicative of the operating results or financial position that would have occurred if the merger had been consummated on the dates indicated, nor are indicative of any future operating results or financial position of the combined business. The results of operations and cash flows of the acquired business reflect its existing state and local jurisdictional rate regulation as a component of the Utility Operating Companies, as compared to the FERC rate regulation expected for Entergy's Transmission Business under ITC's ownership. The pro forma financial statements do not reflect the impact of transitioning Entergy's Transmission Business to FERC rate regulation under ITC ownership.

The merger has not been consummated as of the date of the preparation of these pro forma financial statements and there can be no assurances that the merger will be consummated. See "Risk Factors" for additional discussion of risk factors associated with the pro forma financial statements.

ITC AND ENTERGY'S TRANSMISSION BUSINESS
UNAUDITED PRO FORMA CONDENSED COMBINED CONSOLIDATED BALANCE SHEET

As of September 30, 2012

(In thousands)	ITC (Historical) (a)	Entergy's Transmission Business (Historical) (a)	Adjustments to Entergy's Transmission Business (b)	As Adjusted Entergy's Transmission Business	Acquisition and Related Pro Forma Adjustments (c)	Pro Forma Combined (d)
Assets						
Current assets:						
Cash and cash equivalents	\$ 30,026	\$ 1,319	\$ (1,319)(e)	—	40,000 (f)	\$ 70,026
Accounts receivable	94,863	28,163	(28,163)(e)	—	60,848 (g)	155,711
Inventory	33,876	36,267	—	36,267	—	70,143
Deferred income taxes	21,045	—	—	—	—	21,045
Regulatory assets—revenue accruals, including accrued interest	7,267	—	—	—	—	7,267
Prepaid and other current assets	9,935	—	—	—	—	9,935
Total current assets	197,012	65,749	(29,482)	36,267	100,848	334,127
Property, plant and equipment (net)	3,967,190	3,885,501	(54,459)(e)	3,831,042	—	7,798,232
Other assets						
Goodwill	950,163	38,494	(38,494)(g)	—	2,120,481 (g)	3,070,644
Intangible assets (net)	45,334	—	—	—	—	45,334
Other regulatory assets	171,057	254,986	(47,333)(d)	207,653	—	378,710
Deferred financing fees (net)	19,593	—	13,500 (e)	13,500	7,058 (f)	40,151
Other	30,823	5,874	—	5,874	—	36,697
Total other assets	1,216,970	299,354	(72,327)	227,027	2,127,539	3,571,536
Total assets	\$5,381,172	\$4,250,604	\$ (156,268)	\$4,094,336	\$ 2,228,387	\$11,703,895
Liabilities and stockholders' equity						
Current liabilities						
Accounts payable	\$ 102,530	\$ 54,105	\$ (6,553)(e)	47,552	—	\$ 150,082
Accrued payroll	15,721	10,905	—	10,905	—	26,626
Accrued interest	43,395	—	—	—	—	43,395
Accrued taxes	18,370	35,869	(35,869)(e)	—	—	18,370
Regulatory liabilities—revenue deferrals, including accrued interest	51,836	—	—	—	—	51,836
Refundable deposits from generators for transmission network upgrades	48,041	—	—	—	—	48,041
Debt maturing within one year	651,897	—	—	—	—	651,897
Other	51,040	7,877	—	7,877	7,058 (f)	96,886
Total current liabilities	982,830	108,756	(42,422)	66,334	37,969	1,087,133
Accrued pension and other postretirement liabilities	44,299	99,244	(29,979)(e)	69,265	—	113,564
Deferred income taxes	432,677	949,287	(31,821)(e)	917,466	(12,658)(i)	1,337,485
Regulatory liabilities—revenue deferrals, including accrued interest	68,324	—	—	—	—	68,324
Regulatory liabilities—accrued asset removal costs	79,492	66,213	—	66,213	—	145,705
Refundable deposits from generators for transmission network upgrades	5,241	—	—	—	—	5,241
Other	12,426	39,396	—	39,396	—	51,822
Long-term debt	2,406,674	—	1,775,000 (f)	1,775,000	740,000 (f)	4,921,674
Stockholders' equity						
Common stock	955,258	—	—	—	3,347,246 (j)	3,993,755
Net parent investment	—	2,990,141	(1,829,479)(n)	1,160,662	(308,749)(m)	—
Retained earnings	414,759	—	—	—	(1,160,662)(n)	—
Accumulated other comprehensive loss	(20,808)	(2,433)	2,433 (k)	—	(23,508)(l)	—
Total stockholders' equity	1,349,209	2,987,708	(1,827,046)	1,160,662	(391,251)(m)	3,972,947
Total liabilities and stockholders' equity	\$5,381,172	\$4,250,604	\$ (156,268)	\$4,094,336	\$ 2,228,387	\$11,703,895

See notes to the unaudited pro forma condensed combined consolidated financial statements.

ITC AND ENTERGY'S TRANSMISSION BUSINESS
UNAUDITED PRO FORMA CONDENSED COMBINED CONSOLIDATED
STATEMENTS OF OPERATIONS

For the Nine Months Ended September 30, 2012

	ITC (Historical) (a)	Entergy's Transmission Business (Historical) (a)	Adjustments to Entergy's Transmission Business (b)	As Adjusted Entergy's Transmission Business	Acquisition and Related Pro Forma Adjustments (c)	Pro Forma Combined (d)
(In thousands, except share and per share data)						
Operating revenues	\$ 608,889	\$498,942	\$ 6,067 (i)	\$505,009		\$ 1,113,898
Operating expenses						
Operation and maintenance	90,314	95,188		95,188		185,502
General and administrative	78,791	72,038	(7,072)(e)	64,966	(12,089)(h)	131,668
Depreciation and amortization	78,453	108,286	(8,824)(e)	99,462		177,915
Taxes other than income taxes	44,186	37,670		37,670		81,856
Other operating income and expense—net	(586)	—		—		(586)
Total operating expenses	291,158	313,182	(15,896)	297,286	(12,089)	576,355
Operating income	317,731	185,760	21,963	207,723	12,089	537,543
Other expenses (income)						
Interest expense	116,918	59,959	(5,668)(f)	54,291	28,557 (f)	199,766
Allowance for equity funds used during construction	(15,800)	(8,112)		(8,112)		(23,912)
Other income	(2,171)	(2,164)		(2,164)		(4,335)
Other expense	2,473	1,095		1,095		3,568
Total other expenses (income)	101,420	50,778	(5,668)	45,110	28,557	175,087
Income before income taxes	216,311	134,982	27,631	162,613	(16,468)	362,456
Income tax provision	76,691	41,007	19,066(i)	60,073	(5,764)(i)	131,000
Net income	<u>\$ 139,620</u>	<u>\$ 93,975</u>	<u>\$ 8,565</u>	<u>\$102,540</u>	<u>\$(10,704)</u>	<u>\$ 231,456</u>
Weighted-average shares of common stock outstanding (Note 6):						
Basic	50,748,257					103,983,366
Diluted	51,502,694					104,750,094
Basic earnings per common share (Note 6)	\$ 2.72					\$ 2.23
Diluted earnings per common share (Note 6)	\$ 2.68					\$ 2.21

See notes to the unaudited pro forma condensed combined consolidated financial statements.

ITC AND ENTERGY'S TRANSMISSION BUSINESS
UNAUDITED PRO FORMA CONDENSED COMBINED CONSOLIDATED
STATEMENTS OF OPERATIONS

For the Year Ended December 31, 2011

	ITC (Historical) (a)	Entergy's Transmission Business (Historical) (a)	Adjustments to Entergy's Transmission Business (b)	As Adjusted Entergy's Transmission Business	Acquisition and Related Pro Forma Adjustments (c)	Pro Forma Combined (d)
(In thousands, except share and per share data)						
Operating revenues	\$ 757,397	\$652,792		\$652,792	\$	\$ 1,410,189
Operating expenses						
Operation and maintenance	129,288	133,949		133,949		263,237
General and administrative	82,790	84,980	(5,152)(e)	79,828	(7,000)(h)	155,618
Depreciation and amortization	94,981	132,302	(11,449)(c)	120,853		215,834
Taxes other than income taxes	53,430	45,751		45,751		99,181
Other operating income and expense—net	(844)	—		—		(844)
Total operating expenses	<u>359,645</u>	<u>396,982</u>	<u>(16,601)</u>	<u>380,381</u>	<u>(7,000)</u>	<u>733,026</u>
Operating income	<u>397,752</u>	<u>255,810</u>	<u>16,601</u>	<u>272,411</u>	<u>7,000</u>	<u>677,163</u>
Other expenses (income)						
Interest expense	146,936	63,247	9,141 (f)	72,388	38,076 (f)	257,400
Allowance for equity funds used during construction	(16,699)	(15,122)		(15,122)		(31,821)
Other income	(2,881)	(2,741)		(2,741)		(5,622)
Other expense	3,962	1,142		1,142		5,104
Total other expenses (income)	<u>131,318</u>	<u>46,526</u>	<u>9,141</u>	<u>55,667</u>	<u>38,076</u>	<u>225,061</u>
Income before income taxes	<u>266,434</u>	<u>209,284</u>	<u>7,460</u>	<u>216,744</u>	<u>(31,076)</u>	<u>452,102</u>
Income tax provision	<u>94,749</u>	<u>74,460</u>	<u>2,611 (i)</u>	<u>77,071</u>	<u>(10,876)(i)</u>	<u>160,944</u>
Net income	<u>\$ 171,685</u>	<u>\$134,824</u>	<u>\$ 4,849</u>	<u>\$139,673</u>	<u>\$ (20,200)</u>	<u>\$ 291,158</u>
Weighted-average shares of common stock outstanding (Note 6):						
Basic	50,289,905					103,525,014
Diluted	51,078,823					104,320,730
Basic earnings per common share (Note 6)	\$ 3.36					\$ 2.81
Diluted earnings per common share (Note 6)	\$ 3.31					\$ 2.79

See notes to the unaudited pro forma condensed combined consolidated financial statements.

ITC AND ENTERGY'S TRANSMISSION BUSINESS NOTES TO THE UNAUDITED PRO FORMA CONDENSED COMBINED CONSOLIDATED FINANCIAL STATEMENTS

Note 1. Description of the Merger

As of December 4, 2011, Entergy and ITC executed definitive agreements under which Entergy will separate and then merge its electric transmission business with a wholly-owned subsidiary of ITC.

Entergy's Transmission Business consists of the Entergy transmission system, which comprises over 15,800 circuit miles of 69kV to 500kV transmission lines and 1,500 substations over a 114,000-square mile service territory. The Entergy transmission system spans portions of Arkansas, Louisiana, Mississippi, Missouri and Texas.

The terms of the transaction agreements call for Entergy to separate its electric transmission business into a newly-formed entity, TransCo, and TransCo's subsidiaries, and distribute the equity interests in TransCo (excluding any equity interests in TransCo to be contributed to an exchange trust in the event Entergy makes the exchange trust election) to Entergy's shareholders in the form of a tax-free spin-off or split-off exchange offer or a combination of both. TransCo will then merge with a newly-created merger subsidiary of ITC in an all-stock, Reverse Morris Trust transaction, and will survive the merger as a wholly owned subsidiary of ITC. Prior to the merger, under the terms of the merger agreement, ITC may, in ITC's sole discretion, elect to (i) pay a \$700 million one-time special dividend to its pre-merger shareholders, (ii) repurchase \$700 million of ITC common stock or (iii) undertake a combination of both (not to exceed \$700 million in the aggregate). Such election is referred to as the ITC recapitalization. The ITC recapitalization is expected to be funded by approximately \$740 million of debt securities issued by ITC prior to the merger with the remaining \$40 million to be used for general corporate purposes and payment of transaction-related costs. As a result of and immediately following the merger, Entergy shareholders (and, if applicable, the exchange trust) will collectively own approximately 50.1% of ITC common stock on a "fully diluted basis," and existing ITC shareholders will collectively own approximately 49.9% of ITC common stock on a "fully diluted basis" (subject to adjustment in limited circumstances as provided in the merger agreement and excluding any ITC equity awards issued to employees of Entergy's Transmission Business who become employees of TransCo). In no event will Entergy shareholders (and, if applicable, the exchange trust) hold less than 50.1% of the outstanding common stock of ITC immediately after the merger. In addition, Entergy will receive senior securities of TransCo and gross cash proceeds from indebtedness that will be incurred by TransCo and its subsidiaries prior to the merger in an aggregate amount of \$1.775 billion. This indebtedness will be assumed by ITC. Entergy expects that these proceeds will be used to reduce outstanding Entergy or Utility Operating Company debt or for other corporate purposes.

Upon completion of the merger, Entergy equity-based awards held by employees of Entergy's Transmission Business will generally convert to equivalent ITC equity-based awards, after giving effect to an equity exchange ratio. As defined in the employee matters agreement, the equity exchange ratio is defined as the quotient of (i) the per share closing trading price of Entergy common stock trading in the "Regular Way" trading market on the NYSE on the day before the distribution date and (ii) the per share closing trading price of ITC common stock trading on the NYSE on the closing date of the merger. For purposes of the per share trading prices for the pro forma financial statements, November 23, 2012⁴ has been used as both the distribution and closing date.

Completion of the merger is expected in 2013 subject to the satisfaction of specified closing conditions, including the necessary approvals of Entergy's retail regulators, the FERC and ITC's shareholders. There can be no assurance the merger will be consummated. See "Risk Factors."

⁴ November 23, 2012 share price was used as a reasonable date prior to the filing of the Form S-4 Registration Statement. The share price will be updated with each subsequent Form S-4 amendment based on a reasonable recent date prior to the filing.

Note 2. Basis of Pro Forma Presentation

The pro forma financial statements were derived from historical consolidated financial statements of ITC and the historical combined financial statements of Entergy's Transmission Business. Certain reclassifications have been made to Entergy's Transmission Business' financial statements to conform to ITC's historical presentation.

The historical consolidated financial statements have been adjusted in the pro forma financial statements to give effect to pro forma events that are (1) directly attributable to the merger, (2) factually supportable, and (3) with respect to the pro forma statement of operations, expected to have a continuing impact on the combined results. The pro forma financial statements reflect the impact of:

- the assets and liabilities of Entergy's Transmission Business that will not be transferred to ITC pursuant to the separation agreement;
- the issuance of 52,772,253 shares of ITC common stock to the shareholders of Entergy in connection with the merger and the issuance of 140,430 shares of ITC common stock as replacement awards for Entergy equity-based awards held by employees of Entergy's Transmission Business;
- the additional indebtedness to be incurred with the related financing transactions;
- the recapitalization which will take the form of one of the following: (i) a one-time special dividend payable to pre-merger ITC shareholders or (ii) a share repurchase of ITC common stock, or (iii) a combination of a one-time special dividend and share repurchase of ITC common stock; and
- other adjustments described in the notes to this section.

The following matters have not been reflected in the pro forma financial statements as they do not meet the aforementioned criteria:

- Fair value adjustments for assets or liabilities subject to rate-setting provisions for Entergy's regulated entities operating Entergy's Transmission Business. These operations are subject to the rate-setting authority of the FERC and other local regulators. The rate-setting and cost recovery provisions currently in place for Entergy's Transmission Business regulated operations provide revenues derived from costs including a return on investment of assets and liabilities included in rate base. The fair values of Entergy's Transmission Business assets and liabilities subject to these rate-setting provisions approximate their carrying values and therefore the pro forma financial statements do not reflect any net adjustments related to these amounts.
- Cost savings (or associated costs to achieve such savings) from operating efficiencies, synergies or other restructuring that could result from the merger. The timing and effect of actions associated with integration are currently uncertain.
- Adjustments to the operating expenses recorded in Entergy's Transmission Business' historical financial statements associated with Entergy's MISO integration of \$4.8 million and \$7.0 million for the nine months ended September 30, 2012 and the year ended December 31, 2011, respectively.
- The \$75.0 million aggregate principal amount of 3.98% Senior Secured Notes due 2042 issued by METC on October 26, 2012, the proceeds of which were used to repay borrowings under its revolving credit agreement, partially fund capital expenditures and for general corporate purposes and was unrelated to the transaction financings.

The transaction is being accounted for using the acquisition method of accounting for business combinations with ITC as the acquirer for accounting purposes. Accordingly, ITC's cost to acquire Entergy's Transmission Business will be allocated to the assets acquired and the liabilities assumed based upon their respective fair values on the date the merger is completed. Under the acquisition method of accounting, the total estimated

consideration transferred is allocated to Entergy's 'Transmission Business' net tangible and intangible assets and liabilities based on their estimated fair values as of the date of consummation of the merger. The pro forma adjustments included herein may be revised as additional information becomes available and as additional analyses are performed. See Note 4 "Estimated Consideration Transferred and Preliminary Allocation of Consideration Transferred" below for the estimate of the consideration transferred allocation.

Note 3. Significant Accounting Policies

Based upon ITC's initial review of the summary of significant accounting policies for Entergy's Transmission Business, as disclosed in the notes to the combined financial statements included in this proxy statement/prospectus, as well as preliminary discussions with the management of Entergy's Transmission Business, the pro forma combined consolidated financial statements assume there will be no significant adjustments necessary to conform Entergy's Transmission Business' accounting policies to ITC's accounting policies. Upon completion of the merger and a more comprehensive comparison and assessment, differences may be identified that would necessitate changes to Entergy's Transmission Business' future accounting policies and such changes could result in material differences in future reported results of operations and financial position for Entergy's Transmission Business' operations as compared to historically reported amounts.

Note 4. Estimated Consideration Transferred and Preliminary Allocation of Consideration Transferred

Entergy shareholders (and, if applicable, the exchange trust) are to receive approximately 50.1% of ITC's common stock on a "fully diluted basis" in connection with the merger. In no event will Entergy shareholders (and, if applicable, the exchange trust) hold less than 50.1% of the outstanding common stock of ITC immediately after the merger. The preliminary consideration transferred was computed using the number of shares of ITC common stock outstanding as of September 30, 2012, adjusted for the 50.1% ownership of Entergy as follows (dollars in thousands):

	Number of Shares/Awards Issued	Total Estimated Fair Value
Issuance of ITC common stock to Entergy's shareholders	52,772,253	\$3,340,706
Issuance of ITC equity awards to replace existing earned equity awards of Entergy's Transmission Business	140,430	1,285
Transactional cash (Note 5(g))		(60,848)
Total estimated consideration transferred		\$3,281,143
	Preliminary Allocation of Consideration Transferred	
Current assets	\$ 36,267	
Property, plant and equipment	3,831,042	
Goodwill	2,120,481	
Other long-term assets, excluding goodwill	227,027	
Total assets	6,214,817	
Current liabilities	66,334	
Deferred credits and other liabilities	1,092,340	
Long-term debt (assumed by ITC—Note 5(f))	1,775,000	
Total liabilities	2,933,674	
Total estimated consideration transferred	\$ 3,281,143	

The estimated fair value of the shares of ITC common stock issued to Entergy shareholders of \$63.30 per share was based on the number of shares issued multiplied by the closing price of ITC common stock (\$76.89 on November 23, 2012), adjusted by \$13.59 per share for the effects of the \$700 million one-time special dividend as described in Note 1, "Description of the Merger", as if that dividend were paid on ITC's outstanding shares of common stock at September 30, 2012 that were eligible for dividends. For purposes of these pro forma financial statements, it has been assumed that the ITC recapitalization will take the form of a one-time special dividend. Additionally, the preliminary consideration transferred reflects the total estimated fair value of Entergy's Transmission Business' share-based compensation awards outstanding as of September 30, 2012, converted to ITC common shares based on the equity exchange ratio (described in Note 5(j), *Common Stock* below). If ITC were to effectuate its recapitalization in the form of a repurchase of ITC common stock outstanding prior to the closing date instead of the one-time special dividend as described above, the total estimated consideration transferred would be the same amount, \$3,281.1 million, assuming the share repurchase was effectuated at the closing price of ITC common stock of \$76.89 on November 23, 2012 multiplied by the number of shares expected to be issued after the \$700 million repurchase.

The final allocation of the consideration transferred will be determined after the merger is completed and after completion of a final analysis to determine the fair values of Entergy's Transmission Business' assets and liabilities as of the date of consummation of the merger. Accordingly, the final acquisition accounting adjustments may be materially different from the pro forma adjustments presented in this document.

The consideration transferred will fluctuate with the market price of ITC's common stock until it is reflected on an actual basis when the merger is completed. An increase or decrease of 17% in ITC's common share price from the price used above would increase or decrease the consideration transferred by approximately \$575.6 million. Assessing sensitivity at 17% rate of change is consistent with the differential between the most recent 52-week high and low closing prices of ITC's common stock.

Note 5. Pro Forma Adjustments to Financial Statements

The pro forma adjustments included in the pro forma financial statements are as follows:

(a) *ITC and Entergy's Transmission Business historical presentation*—Certain financial statement line items or components of financial statement line items included in Entergy's Transmission Business historical presentation have been reclassified to conform to ITC's historical presentation. These reclassifications had no impact on the historical operating income, net income or total equity reported by Entergy's Transmission Business. The adjustments to total assets and liabilities were not material to Entergy's Transmission Business' balance sheet.

(b) *Adjustments to Entergy's Transmission Business*—Pursuant to the separation agreement, certain adjustments are required to accurately reflect the assets acquired and liabilities assumed of Entergy's Transmission Business, including the issuance of long-term debt by Entergy's Transmission Business to be assumed. These adjustments to Entergy's Transmission Business financial information are described in Note 5(c) *Assets and Liabilities Not Transferred* and Note 5(f) *Debt* below.

(c) *Acquisition and Related Pro Forma Adjustments*—Adjustments were made to ITC's historical financial information in addition to the "As Adjusted Entergy's Transmission Business" financial information. These adjustments reflect the effects of the acquisition, including the one-time special dividend and the issuance of common stock.

(d) *Pro Forma Combined*—Represents the total of the "ITC (Historical)" column, the "As Adjusted Entergy's Transmission Business" column and the "Acquisition and Related Pro Forma Adjustments" column.

(c) *Assets and Liabilities Not Transferred*—Pursuant to the separation agreement, certain assets and liabilities of Entergy's Transmission Business will not be transferred to ITC and will be retained by Entergy. The pro forma balance sheet includes the following pro forma adjustments to reflect assets, liabilities and associated deferred taxes not transferred to ITC pursuant to the separation agreement (in thousands):

	As of September 30, 2012
Cash and cash equivalents	\$ (1,319)
Accounts receivable (net)	(28,163)
Property, plant and equipment (net) (1)	(54,459)
Other regulatory assets (2)	(47,333)
Total assets	<u>\$(131,274)</u>
Accounts payable	\$ (6,553)
Accrued taxes	(35,869)
Accrued pension and other postretirement liabilities (2)	(29,979)
Deferred income taxes	(31,821)
Total liabilities	<u>\$(104,222)</u>
Net Assets Not Transferred	<u>\$ (27,052)</u>

- (1) The pro forma statements of operations include pro forma adjustments to depreciation and amortization expense of \$8.8 million and \$11.4 million for the nine months ended September 30, 2012 and the year ended December 31, 2011, respectively, to reflect a decrease in ongoing depreciation expense for the assets not transferred.
- (2) As the combined company will not have responsibility for the inactive and retired employees under the previous Entergy pension plan pursuant to the employee matters agreement, the pro forma statements of operations include pro forma adjustments to general and administrative expenses of \$7.1 million and \$5.2 million for the nine months ended September 30, 2012 and the year ended December 31, 2011, respectively, to reflect a decrease in the ongoing expense relating to these employees.

(f) *Debt*—As described in Note 1, "Description of the Merger", the pro forma balance sheet includes a \$1.775 billion and a \$740 million adjustment made to the "As Adjusted Entergy's Transmission Business" and the "Pro Forma Combined," respectively, that are described below.

Prior to the closing of the merger, Entergy's Transmission Business is expected to obtain an additional \$1.775 billion in debt financing that will be assumed by ITC, consisting of \$1.2 billion of TransCo Subs Financing and \$575 million of TransCo debt securities. The \$1.775 billion is a liability to be assumed by ITC in the transaction. The pro forma balance sheet includes a pro forma adjustment to record deferred financing fees of \$13.5 million related to the TransCo Subs Financing of \$1.2 billion, which will be paid by Entergy's Transmission Business.

Additionally, \$740 million of new ITC debt is expected to be issued, with \$40 million recorded as an increase to cash to be used for general corporate purposes and payment of transaction-related costs and \$700 million to be used to finance the recapitalization of ITC, described below in Note 5(m), *Recapitalization*. The \$7.1 million of deferred financing fees to be paid by ITC is included as an increase to deferred financing fees and other current liabilities.

The pro forma statements of operations include a pro forma adjustment of \$5.7 million and \$9.1 million to interest expense related to Entergy's Transmission Business for the \$1.775 billion in debt financing for a total interest expense of \$54.3 million and \$72.4 million for the nine months ended September 30, 2012 and the year

ended December 31, 2011, respectively. Additionally, the pro forma statements of operations include a pro forma adjustment of \$28.6 million and \$38.1 million to interest expense related to the \$740 million of new ITC debt for the nine months ended September 30, 2012 and the year ended December 31, 2011, respectively. An interest rate of 5.05% was used to calculate the pro forma interest expense on the new ITC debt of \$740 million as well as the TransCo debt securities to be assumed by ITC of \$575 million and an interest rate of 3.50% was used to calculate the pro forma interest expense on the TransCo Subs Financing of \$1.2 billion to be assumed by ITC. The interest rates are based on a 10-year forward U.S. Treasury Bond estimate for July 2013 plus an applicable credit spread for both senior secured and unsecured notes for ITC and its subsidiaries. The effect of a 0.125% change in interest rates would result in an annual change in the interest expense adjustment of approximately \$3.1 million.

(g) *Goodwill*—The pro forma balance sheet includes a preliminary estimate of goodwill. Goodwill represents the excess of consideration transferred over the estimated fair value of the identifiable assets acquired and liabilities assumed in addition to an adjustment to remove Entergy's Transmission Business' existing goodwill balance of \$38.5 million. The consideration transferred of \$3,281.1 million includes: (1) ITC common stock issued to Entergy; (2) ITC equity awards issued to replace existing earned awards of Entergy's Transmission Business; and (3) a reduction for transactional cash (recorded as an increase to accounts receivable of \$60.8 million). The amount of transactional cash paid to ITC from Entergy is equal to the balance of Entergy's Transmission Business' customer deposits and accounts payable related to capital assets. The transactional cash is expected to be paid at or shortly after the closing of the transaction and is recorded in accounts receivable on the pro forma balance sheet.

Total estimated consideration transferred (Note 4)	\$ 3,281,143
Less: Fair value of net assets assumed by ITC	(1,160,662)
Estimated goodwill from acquisition	<u>\$ 2,120,481</u>

(h) *Merger Transaction Costs*—The pro forma balance sheet includes a pro forma adjustment to reflect ITC's estimated merger transaction costs for periods subsequent to September 30, 2012 of \$30.9 million. Merger transaction costs primarily include costs related to investment banking, legal, accounting, and consulting services.

The pro forma statements of operations include the pro forma adjustments to eliminate the merger transaction costs incurred by ITC of \$12.1 million for the nine months ended September 30, 2012 and \$7.0 million for the year ended December 31, 2011. Entergy's Transmission Business has not recorded any merger transaction costs in its historical financial statements. ITC's estimated merger transaction costs have been excluded from the pro forma statements of operations as they reflect non-recurring charges not expected to have a continuing impact on the combined results.

(i) *Income Taxes*—The pro forma balance sheet includes a pro forma adjustment to reflect the estimated deferred income tax impact of \$10.8 million for merger transaction costs (as described in Note 5(h), *Merger Transaction Costs*) and \$1.8 million for accelerated vesting of share-based awards (as described below in Note 5(j), *Common Stock*), based on the federal statutory rate of 35%.

The total pro forma adjustments for income taxes in the pro forma statements of operations are \$13.3 million for the nine months ended September 30, 2012 and \$8.3 million for the year ended December 31, 2011. The pro forma adjustments are tax-effected at the federal statutory rate of 35%.

Included in the pro forma income statement for the nine months ended September 30, 2012 is an adjustment to Entergy's Transmission Business to increase the income tax provision by \$9.4 million and to increase revenues by \$6.1 million. As described in Note 8 in the condensed combined financial statements of Entergy's

Transmission Business for the nine months ended September 30, 2012 and 2011 included elsewhere in this proxy statement/prospectus, in June 2012 Entergy settled an uncertain tax position that was recorded as an income tax benefit and a reduction to operating revenues for the nine months ended September 30, 2012. These items were adjusted from the pro forma income statement as the items are not expected to have a continuing impact.

(j) *Common Stock*—The total adjustments to common stock of \$3,347.2 million consist of the following items:

- An adjustment to common stock of \$3,340.7 million related to the issuance of 52,772,253 shares of ITC common stock to the shareholders of Entergy (and, if applicable, the exchange trust) in order to receive approximately 50.1% of the shares of pro forma ITC as described in Note 4.
- An adjustment to common stock of \$1.3 million for 140,430 shares related to the issuance of ITC equity awards (as authorized by the proposed amendment to the Amended and Restated Articles of Incorporation as noted above under “Notice of Special Meeting of Shareholders” and described in Note 4) to replace existing awards, held by employees of Entergy’s Transmission Business as described in Note 1, “Description of the Merger.” For the replacement awards, each Entergy share award held by an employee of Entergy’s Transmission Business will be converted to an ITC equity award. The fair value of the replacement awards which are considered vested under Entergy’s share-based compensation plans at the effective time of the merger has been attributed to pre-combination service and reflected in the consideration transferred. Unvested share-based awards are considered post-combination service. These estimates are preliminary, subject to change and could vary materially from the actual adjustments at the time the merger is completed, driven by various factors including changes in ITC and Entergy share prices as compared to November 23, 2012 share prices that were used for purposes of determining these pro forma adjustments.
- An adjustment to common stock of \$5.2 million related to the impact of the accelerated vesting of certain share based awards. In accordance with our Second Amended and Restated 2006 Long-Term Incentive Plan, the vesting period for certain grants issued to ITC employees prior to September 30, 2012 will be accelerated upon the transfer of shares in connection with the merger transaction.

(k) *Accumulated Other Comprehensive Loss*—The pro forma balance sheet reflects the elimination of the historical accumulated other comprehensive loss of Entergy’s Transmission Business.

(l) *Retained Earnings*—The pro forma balance sheet adjustment to retained earnings of \$23.5 million consists of \$20.1 million related to the estimated merger transaction costs (net of tax) (as described in Note 5(h), *Merger Transaction Costs*) and \$3.4 million related to the accelerated vesting of ITC common stock (net of tax) (as described in Note 5(j), *Common Stock*).

(m) *Recapitalization*—ITC’s \$700 million recapitalization described in Note 1, “Description of the Merger,” may take the form of a one-time special dividend to ITC’s pre-merger shareholders, a repurchase of ITC common stock from its shareholders, or a combination of a one-time special dividend and share repurchase. For purposes of these pro forma financial statements, we have assumed that the recapitalization will take the form of a one-time special dividend of \$700 million, which is reflected as a reduction to common stock and retained earnings of \$308.7 million and \$391.3 million, respectively. If ITC’s \$700 million recapitalization were to take the form of a share repurchase, the pro forma financial statements would reflect a reduction in common stock of \$700 million. The impact of effectuating a share repurchase instead of a one-time special dividend on pro forma basic and diluted earnings per share is described in Note 6, “Common Stock Shares Outstanding.”

(n) *Net Parent Investment*—The pro forma balance sheet reflects the adjustment to eliminate Entergy's Transmission Business' net parent investment. The elimination of the net parent investment was performed as a two-step process as described below.

- In determining the net assets of the "As Adjusted Entergy's Transmission Business", \$1,829.5 million of Entergy's Transmission Business' net parent investment was eliminated. This amount was calculated as the offsetting entry to all of the adjustments to the historical financial information of Entergy's Transmission Business (as described in Note 5(c), *Adjustments to Entergy's Transmission Business*). Included in this adjustment is the \$1.775 billion of debt being issued by Entergy's Transmission Business for which Entergy will retain the proceeds (as described in Note 5(f), *Debt*).
- In determining the "Pro Forma Combined Balance Sheet", \$1,160.7 million of Entergy's Transmission Business' net parent investment was eliminated. This amount was calculated as the net assets of the "As Adjusted Entergy's Transmission Business" and used in the calculation of Goodwill (as calculated in Note 5(g), *Goodwill*).

Note 6. Common Stock Shares Outstanding

The pro forma weighted-average number of basic shares outstanding is calculated by adding (i) the shares issued in connection with the transaction; (ii) ITC's weighted average number of basic shares of common stock outstanding for the nine months ended September 30, 2012 and the year ended December 31, 2011; and (iii) the shares to be issued for accelerated vesting of restricted stock awards (as described above in Note 5(j), *Common Stock*). The pro forma weighted-average number of diluted shares outstanding is calculated by adding (i) the pro forma weighted-average basic shares, (ii) ITC's incremental shares for stock options and the employee stock purchase plan for the nine months ended September 30, 2012 and the year ended December 31, 2011 and (iii) the shares for stock options and restricted shares held by employees of Entergy's Transmission Business, which was converted to equivalent ITC incremental shares based on the equity exchange ratio of 1.016 that is pursuant to the employees matters agreement. The following table illustrates these computations:

	Nine Months Ended September 30, 2012	Year Ended December 31, 2011
Basic:		
ITC common shares issued in the transaction	52,772,253	52,772,253
ITC weighted-average basic common shares	50,748,257	50,289,905
Accelerated vesting of restricted stock	462,856	462,856
Pro forma weighted-average basic common shares	<u>103,983,366</u>	<u>103,525,014</u>
Diluted:		
ITC incremental shares for stock options and employee stock purchase plan	754,437	788,918
Shares for stock options and restricted shares held by employees of Entergy's Transmission Business	12,103	6,694
Equity Exchange ratio	1.016	1.016
Equivalent ITC incremental shares	<u>12,291</u>	<u>6,798</u>
Pro forma weighted-average diluted common shares	<u>104,750,094</u>	<u>104,320,730</u>

ITC's historical earnings per share were calculated based on the two-class method due to our restricted stock containing rights to receive nonforfeitable dividends. As a result of the accelerated vesting of the restricted stock awards at the merger date, the use of the two class method did not have a material impact on pro forma earnings per share.

If the \$700 million recapitalization took the form of a share repurchase instead of a one-time special dividend, the pro forma weighted average basic and diluted common shares would decrease by 9,103,915 shares for the nine months ended September 30, 2012 and the year ended December 31, 2011. For the nine months ended September 30, 2012, pro forma basic and diluted earnings per share would increase by \$0.21. For the year ended December 31, 2011, pro forma basic and diluted earnings per share would increase by \$0.27.

ITC common stock that are held in the exchange trust. See “Additional Material Agreements—Agreements Related to the Exchange Trust and Exchange Offer—Exchange Trust Agreement” and “Additional Material Agreements—Agreements Related to the Exchange Trust and Exchange Offer—Registration Rights Agreement.”

Background of the Merger

In the ordinary course of business, ITC periodically reviews and evaluates industry developments and strategic alternatives to enhance shareholder value, including assessing transmission systems that would be potential acquisition candidates and considering various transaction partners that would be able to provide ITC with an ability to expand ITC's transmission business. Entergy's board of directors and management frequently review Entergy's portfolio of assets to evaluate its current structure and composition to determine whether changes might be advisable, and to look for attractive ways to add value for its shareholders. ITC determined to pursue this transaction with Entergy to expand its transmission business, rather than other available transactions or no transaction, for a variety of reasons, including the expectation that such transaction will be value accretive to ITC's financial results (after giving effect to the ITC recapitalization), increase ITC's revenues and earnings and enhance cash flow generation, the enhanced growth prospects available through ITC's increased size and geographic reach, the expectation that such transaction will enhance ITC's overall credit quality and significantly enhance ITC's balance sheet, the structure of such transaction as a tax-free reorganization for federal income tax purposes and for other reasons described below under “—ITC's Reasons for the Merger; Recommendation of ITC's Board of Directors.”

On June 6, 2011, Mr. Eddie Peebles, Vice President of Corporate Development for Entergy, initiated a call with Dr. Terry Harvill, Vice President of Grid Development for ITC. During this call Mr. Peebles inquired about ITC's interest in submitting a proposal related to Entergy's Transmission Business.

After ITC expressed interest in submitting a proposal, on June 10, 2011, ITC and ESI executed a non-disclosure agreement.

Following the execution of the non-disclosure agreement, Entergy provided ITC with preliminary non-public information regarding Entergy's Transmission Business. Such information included (i) a summary of Entergy's Transmission Business, (ii) information on the historical rate base and deferred taxes of Entergy's Transmission Business and (iii) projections for capital expenditures. Also included with such information were instructions for submitting a non-binding indication of interest.

From June 13, 2011 through June 17, 2011, Dr. Harvill and Mr. Peebles had several calls to discuss matters regarding Entergy's request for a non-binding indication of interest for Entergy's Transmission Business and the preliminary non-public information previously provided to ITC.

On June 21, 2011, Mr. Peebles provided Dr. Harvill with updated non-public information regarding Entergy's Transmission Business' projections for capital expenditures.

On July 1, 2011, at Entergy's request, ITC submitted to Entergy a confidential and non-binding indication of interest letter for the acquisition of Entergy's Transmission Business. The letter proposed an acquisition of Entergy's Transmission Business for all-cash consideration, but in its letter ITC also indicated that it would be willing to explore various alternative structures to facilitate a potential transaction, including a pre-paid lease, a leveraged partnership and the Reverse Morris Trust structure described below that was ultimately adopted for the transaction. ITC's proposal also included its preliminary indication of the enterprise value of Entergy's Transmission Business between \$6.75 billion and \$7.25 billion. This preliminary valuation reflected a taxable asset acquisition for all-cash consideration and was based on transmission rate base values and capital investment forecasts provided by Entergy, among other assumptions. In particular, consistent with Entergy's instructions, the preliminary valuation assumed a January 1, 2014 valuation date, utilized a projected 2014 rate base, did not estimate any potential effects of accelerated federal tax bonus depreciation, and, due to the taxable nature of an

all-cash consideration transaction, assumed that there would be a resetting of tax basis of the assets acquired and a corresponding remeasurement of accumulated deferred income taxes on the assets acquired. These assumptions implied significantly higher rate base and earnings power (and a correspondingly higher value) for Entergy's Transmission Business relative to those implied by the Reverse Morris Trust transaction structure ultimately agreed upon by the parties. In addition, during the course of negotiating the transaction with Entergy, certain other assumptions for Entergy's Transmission Business were refined by Entergy, including transmission rate base values, capital investment projections and the applicability of accelerated federal tax bonus depreciation, which had a material impact on the valuation of Entergy's Transmission Business relative to what ITC presented in July 1, 2011 non-binding indication of interest.

On July 6, 2011, representatives from Entergy and ITC met at Entergy's New Orleans, Louisiana headquarters to discuss ITC's preliminary indication of interest to acquire Entergy's Transmission Business. Participants from ITC included Mr. Cameron Bready, Executive Vice President and Chief Financial Officer, and Dr. Harvill, and participants from Entergy included Mr. Leo Denault, Chief Financial Officer, and Mr. Peebles. The group discussed various preliminary issues and concerns, including structuring alternatives and the potential benefits to ITC and Entergy of a transaction involving Entergy's Transmission Business, ITC's ability to successfully integrate and operate the larger business that would result from the acquisition and the regulatory approvals that would be required to consummate the transaction. At the conclusion of the meeting, the parties agreed that they would continue to evaluate the feasibility of a potential transaction. Mr. Denault informed Mr. Bready that he would contact Mr. Bready with the plan for next steps, if any, after Mr. Denault had briefed the Entergy board of directors at its regular July meeting.

On July 29, 2011, at a regularly scheduled meeting of Entergy's board of directors, Mr. Denault presented Entergy's board of directors with information on a potential transaction involving Entergy's Transmission Business. The presentation included information on (i) a summary of the actions taken to date, (ii) the internal valuation of Entergy's Transmission Business, (iii) a potential transaction structure for consideration and (iv) a potential transaction timeline if the proposed transaction were to proceed. The Entergy board of directors instructed management to proceed with further discussions with ITC to determine whether a transaction could be achieved.

On August 17, 2011, the ITC board of directors held its regularly scheduled quarterly board meeting during which Mr. Bready provided a brief overview of the potential opportunity with Entergy.

On August 23, 2011, Mr. Denault called Mr. Bready to discuss the possibility of advancing discussions to determine if ITC and Entergy could reach a mutually agreeable transaction. Mr. Denault and Mr. Bready agreed to establish a process to exchange non-public information, perform due diligence and enter into further discussions regarding a potential transaction.

On August 26, 2011, ITC retained Simpson Thacher & Bartlett LLP, referred to as Simpson Thacher, as outside legal counsel.

On August 31, 2011, Entergy and ITC entered into a mutual non-disclosure agreement which superseded the non-disclosure agreement entered into between ESI and ITC on June 10, 2011. Also on August 31, 2011, Entergy retained Skadden, Arps, Slate, Meagher & Flom LLP, referred to as Skadden, Arps, as outside legal counsel.

On September 2, 2011, Entergy and ITC exchanged, through their respective financial advisors, additional financial information regarding Entergy's Transmission Business and ITC, respectively.

On September 7, 2011, at the Chicago, Illinois offices of Goldman Sachs & Co., referred to as Goldman Sachs, senior management from ITC and Entergy and other representatives for Entergy and ITC held a transaction kick-off meeting. Attendees at this meeting from ITC included Mr. Bready, Dr. Harvill, and Mr. Jon Jipping, Executive Vice President and Chief Operating Officer, representatives from Deloitte & Touche, tax

advisors to ITC, referred to as Deloitte; representatives from J.P. Morgan, financial advisor to ITC, referred to as J.P. Morgan; and representatives from Simpson Thacher, ITC's legal counsel. Attendees at this meeting from Entergy included Mr. Denault, Mr. Peebles, and Mr. Mark Savoff, Executive Vice President and Chief Operating Officer; representatives from Skadden, Arps and representatives from Goldman Sachs. At the meeting, Entergy and ITC representatives discussed the potential terms and structure of a transaction involving Entergy's Transmission Business. Representatives of ITC and Entergy also presented information about their respective transmission businesses and financial forecasts and assumptions.

At this meeting, Entergy proposed that the transaction be structured as a Reverse Morris Trust transaction. A Reverse Morris Trust transaction is a business combination involving the spin- or split-off of a business (here, Entergy's Transmission Business), by a company (here, Entergy), and its subsequent merger with another company (here, ITC). Entergy's proposal would be structured on a tax free basis where shareholders of the company effecting the spin- or split-off (here, the Entergy shareholders) receive more of the equity in the combined company than the shareholders of the other company (here, the ITC shareholders). In addition to facilitating a tax-free transaction for Entergy shareholders, the Reverse Morris Trust structure also results in a lower rate base for Entergy's Transmission Business under ITC ownership relative to that which would result from a taxable, all-cash transaction, which results in lower expected transmission rates for ITC's new customers upon closing the transaction relative to what they would have experienced in a taxable, all-cash transaction. The Reverse Morris Trust structure was ultimately selected by the parties for the foregoing reasons and for the other reasons described below under "—ITC's Reasons for the Merger; Recommendation of ITC's Board of Directors" and "—Entergy's Reasons for the Separation, Distribution and the Merger". The attendees also discussed the due diligence protocol and the due diligence process.

On September 8, 2011, there was a conference call among representatives of ITC, Entergy, J.P. Morgan and Goldman Sachs to discuss the details of ITC's and Entergy's financial forecasts.

From September 8, 2011 through October 18, 2011, Mr. Bready, Dr. Harvill and representatives of J.P. Morgan had preliminary communications with representatives of Entergy, including Mr. Peebles, and Goldman Sachs regarding a working framework for the valuation terms of the potential transaction, including the pro forma ownership of ITC between Entergy and ITC shareholders after the merger, the amount of indebtedness Entergy's Transmission Business could incur, and the value that ITC would distribute to its pre-merger shareholders in the form of a one-time special dividend, share repurchase or combination thereof, referred to as the ITC recapitalization.

On September 13, 2011, Entergy formally engaged Goldman Sachs as its financial advisor in connection with the proposed transaction.

Beginning on September 16, 2011, weekly calls between Mr. Denault and Mr. Bready were implemented in order to discuss issues related to the proposed transaction.

From September 14, 2011 to September 23, 2011, representatives from ITC and Entergy and their respective advisors held numerous calls to discuss (i) outstanding issues regarding the potential transaction, including the transaction structure, (ii) what assets and operations would constitute Entergy's Transmission Business, (iii) due diligence issues of primary concern related to environmental, information technology, transmission operations, treasury, federal regulatory, accounting, real estate, state/local regulatory, human resource/employee, tax and legal and (iv) the progress of the proposed transaction.

On September 26, 2011, each of Entergy and ITC provided to the other party and their respective legal and financial advisors access to electronic data rooms containing non-public information related to ITC and Entergy's Transmission Business in order to continue to conduct due diligence. Due diligence continued until shortly before the merger agreement, the separation agreement and the employee matters agreement were executed.

From September 27, 2011 until shortly before the execution of the merger agreement, the separation agreement and the employee matters agreement, representatives of Entergy and ITC and their respective advisors had regular meetings and ongoing discussions related to regulatory strategy matters regarding the proposed transaction.

On September 30, 2011, representatives from ITC, Entergy, J.P. Morgan and Goldman Sachs participated in a conference call to discuss Entergy's Transmission Business's and ITC's capital expenditures forecasts, respectively. Also on September 30, 2011, Dr. Harvill and Mr. Peebles had a call to discuss outstanding valuation and other transaction matters and a general update of the progress of the proposed transaction.

On October 3, 2011, Entergy through Goldman Sachs also provided ITC with updated financial forecasts to supplement the information provided to ITC on September 2, 2011.

On October 11, 2011, there was a conference call among Mr. Bready, Dr. Harvill and other representatives of ITC, Mr. Peebles and other representatives from Entergy, and representatives from Deloitte, J.P. Morgan, Goldman Sachs, Simpson Thacher and Skadden, Arps to discuss transaction structuring matters. Also on October 11, 2011, Dr. Harvill and Mr. Peebles had a call to discuss outstanding issues related to valuation and other transaction terms, including a general update on the progress of the proposed transaction.

On October 11, 2011, Mr. Joseph Welch, Chairman, President and Chief Executive Officer of ITC, and Mr. Bready met in Atlanta, Georgia with Mr. J. Wayne Leonard, Chairman and Chief Executive Officer of Entergy, and Mr. Denault to discuss certain aspects of a potential transaction, including the strategic rationale for the transaction for both parties, the regulatory considerations to effectuate the transaction and certain operational matters for Entergy's Transmission Business. At the meeting, each party's representatives expressed their mutual desire to proceed and further negotiate a proposed transaction.

On October 13, 2011, Entergy provided ITC with an updated capital expenditure forecast and financial model, supplementing the information provided on October 3, 2011.

On October 14, 2011, representatives from ITC, including Dr. Harvill, representatives from Entergy, including Mr. Rick Riley, Vice President of Energy Delivery, and Mr. Peebles, and representatives from J.P. Morgan and Goldman Sachs participated in a conference call to discuss the capital expenditure forecasts provided the day before.

On October 18, 2011, J.P. Morgan delivered a preliminary proposal to Entergy on behalf of ITC, which included: (i) that the post-merger pro forma ownership of ITC between Entergy shareholders and ITC shareholders would be approximately 50.1% and 49.9%, respectively, (ii) that Entergy's Transmission Business could incur up to \$1.8 billion in indebtedness prior to the distribution and merger, the proceeds of which would be retained by Entergy and Entergy's Utility Operating Companies and (iii) that the ITC recapitalization would not exceed \$700 million.

On October 19, 2011, Mr. Denault and Mr. Bready spoke by telephone about the proposed transaction. On the telephone call, Mr. Denault asked Mr. Bready follow up questions regarding the proposal delivered by ITC the previous day.

At a special meeting of the Entergy board of directors held on October 20, 2011, Entergy management briefed the Entergy board of directors on the status of the proposed divestiture of Entergy's Transmission Business.

On October 20, 2011, Skadden, Arps, distributed initial drafts of the merger agreement and separation agreement to Simpson Thacher.

Also on October 20, 2011, the ITC board of directors held a special meeting, during which Mr. Bready provided the ITC board of directors with a comprehensive review of the proposed transaction, including an overview of Entergy's Transmission Business, strategic rationale for the proposed transaction, regulatory approvals required to close the transaction, an update on the status of ITC's due diligence review of Entergy's Transmission Business and proposed next steps to advance the transaction. Mr. Bready also presented preliminary valuation and combination analytics, as well as an overview of the key elements of the structure of the proposed transaction. In addition, representatives of Simpson Thacher and Dykema, ITC's Michigan outside counsel, provided an overview of applicable legal standards and fiduciary duties of directors in the context of considering the potential transaction and other strategic alternatives available to ITC. After extensive consideration, the ITC board of directors directed senior management to continue to pursue discussions with Entergy regarding a potential transaction. In addition, due to the expected timing associated with advancing the transaction and its complexity, the board of directors of ITC designated a sub-committee of board members, referred to as the ITC board sub-committee, to be accessible to management for more regular updates and to provide guidance on significant issues associated with the transaction arising between meetings of the full board of directors.

On October 25, 2011, Mr. Denault and Mr. Bready met in Chicago, Illinois. At this meeting, Mr. Denault and Mr. Bready discussed matters related to the transaction, including the terms of ITC's preliminary proposal delivered by J.P. Morgan on October 18, 2011. Mr. Denault and Mr. Bready preliminarily agreed that the post-merger pro forma ownership of ITC between Entergy shareholders and ITC shareholders would be 50.1% and 49.9%, respectively, (ii) that Entergy's Transmission Business could incur up to \$1.95 billion in indebtedness prior to the distribution and the merger, the net proceeds of which would be retained by Entergy and Entergy's Utility Operating Companies and (iii) that the ITC recapitalization would not exceed \$600 million.

On October 27, 2011, representatives from Simpson Thacher and Skadden, Arps held a call to discuss ITC's preliminary issues arising out of the drafts of the merger agreement and separation agreement distributed by Skadden, Arps.

On October 28, 2011, at a regularly scheduled meeting of the Entergy board of directors, Mr. Denault and Mr. Peebles presented an update to the Entergy board of directors regarding the proposed transaction. The presentation included information on (i) strategic rationale, (ii) background on ITC, (iii) Entergy's internal valuation of Entergy's Transmission Business and combination analysis of Entergy's Transmission Business with ITC, (iv) proposed transaction structure, (v) social factors, (vi) transaction timing and (vii) next steps.

Also on October 28, 2011, Mr. Denault and Mr. Bready spoke by telephone about the proposed transaction. Mr. Denault informed Mr. Bready that at the meeting of the Entergy board of directors that day, the Entergy board of directors continued to be interested in the proposed transaction provided satisfactory financial and other terms and conditions could be reached.

On October 29, 2011, there was a conference call to discuss issues in the draft merger agreement and separation agreement provided to ITC. Participants included Mr. Peebles from Entergy, Dr. Harvill from ITC, and representatives from Deloitte, Simpson Thacher, J.P. Morgan, Goldman Sachs, and Skadden, Arps. The discussions included issues related to (i) the financings to be conducted prior to the closing of the merger, (ii) the ability of Entergy to modify aspects of the transaction concerning Entergy's internal reorganization without the consent of ITC, (iii) the circumstances in which each party could terminate the agreement, (iv) the obligations of the parties to close the transaction based on certain events, (v) the required efforts of each party necessary to close the transaction, (vi) the allocation of assets and liabilities between ITC and Entergy related to Entergy's Transmission Business, (vii) whether the amount of debt and Entergy shareholders' post-merger ownership of ITC would be adjusted upon certain events and (viii) other contract provisions.

Between November 1, 2011 and November 10, 2011, Dr. Harvill and Mr. Peebles had several calls to discuss outstanding valuation matters, issues in the transaction agreements and a general update of the progress of the proposed transaction.

On November 3, 2011, ITC formally engaged J.P. Morgan as its financial advisor in connection with the proposed transaction.

Also on November 3, 2011, the ITC board sub-committee held a telephonic meeting to receive an update from management and their legal and financial advisors with respect to progress on the proposed transaction.

On November 4, 2011, Simpson Thacher distributed to Skadden, Arps a mark-up of the separation agreement.

On November 6, 2011, Simpson Thacher distributed to Skadden, Arps a mark-up of the merger agreement. On the same day, Skadden, Arps distributed a draft of the employee matters agreement to Simpson Thacher.

On November 7, 2011, Mr. Mark McCulla, Vice President of Transmission Regulatory Compliance, and Mr. Riley, each from Entergy and Mr. Jipping from ITC, met in Jackson, Mississippi to review business operations and answer questions related to specific groups within the transmission organization. The group also discussed information technology related matters.

On November 9, 2011, representatives from Entergy, ITC, Simpson Thacher and Skadden, Arps participated in meetings at Entergy's New Orleans, Louisiana headquarters to discuss outstanding employee matters related to the proposed transaction, including the draft employee matters agreement delivered to ITC on November 6, 2011. Participants included Dr. Harvill, Mr. Bready, Ms. Linda Blair, Executive Vice President and Chief Business Officer, and Mr. Jipping of ITC; Ms. Renae Conley, Executive Vice President of Human Resources and Administration, Mr. Peebles, Mr. Denault, and Mr. Savoff of Entergy; and representatives from Simpson Thacher. A representative of Skadden, Arps participated by phone.

On November 11, 2011, representatives of Entergy and ITC and their legal advisors met in New Orleans, Louisiana to further discuss outstanding issues with the revised drafts of the transaction agreements raised on the October 29, 2011 teleconference between the parties. Participants included Dr. Harvill from ITC; Mr. Peebles from Entergy; and representatives from Simpson Thacher and Skadden, Arps.

Also on November 11, 2011, ITC formally engaged Barclays Capital Inc., also referred to as Barclays, as its financial advisor in connection with the proposed transaction.

On November 14, 2011, Mr. Welch and Mr. Bready from ITC met with Mr. Leonard and Mr. Denault from Entergy in Atlanta, Georgia to discuss the proposed transaction. At this meeting, the participants discussed the progress of the proposed transaction, including the board and management composition of ITC following the potential transaction, key terms and conditions of the merger agreement, and other social issues.

On November 16, 2011, the ITC board of directors held its regularly scheduled quarterly board meeting during which senior management provided the ITC board of directors with an update regarding progress on the proposed transaction with Entergy. At this meeting, Mr. Bready also provided additional financial analysis regarding the potential transaction and a status update with respect to due diligence efforts and negotiation of the transaction agreements. Mr. Bready also presented an expected timeline for advancing the potential transaction assuming that agreement could be reached on remaining issues subject to negotiation.

Also on November 16, 2011, Skadden, Arps distributed a revised draft of the merger agreement to Simpson Thacher.

On November 16, 2011 and November 17, 2011, there were calls between Dr. Harvill and Mr. Peebles to discuss outstanding issues related to transaction representations and warranties, status of the employee matters agreement and the progress of other outstanding matters related to the proposed transaction.

On November 18, 2011, the Entergy board of directors held a telephonic special meeting to discuss the transaction. Mr. Denault and Mr. Peebles presented an update to the Entergy board of directors regarding the proposed transaction. The presentation included information on (i) strategic rationale, (ii) Entergy's internal valuation of Entergy's Transmission Business and combination analysis of Entergy's Transmission Business with ITC, (iii) proposed transaction structure, (iv) social issues, (v) transaction timing and (vi) next steps.

On November 19, 2011, there was a conference call among Mr. Bready, Dr. Harvill, Mr. Peebles, and Mr. Denault and other representatives of ITC, Entergy, Deloitte, Simpson Thacher, Skadden, Arps, J.P. Morgan and Goldman Sachs to discuss financing matters relating to the proposed transaction.

On November 19, 2011, Skadden, Arps distributed a revised draft of the separation agreement to Simpson Thacher.

On November 20, 2011, Dr. Harvill and Ms. Blair from ITC and Mr. Peebles from Entergy had a conference call to discuss outstanding employee related matters about the proposed transaction.

On November 21, 2011, representatives of ITC, Entergy, Simpson Thacher and Deloitte had a conference call to discuss and negotiate certain tax provisions of the merger agreement and separation agreement.

On November 22, 2011, representatives from ITC, including Dr. Harvill, representatives from Entergy, including Mr. Peebles, and other representatives from Entergy, ITC, Simpson Thacher, Skadden, Arps, J.P. Morgan and Goldman Sachs met at J.P. Morgan's offices in Chicago, Illinois. Issues discussed at the meeting included (i) the circumstances in which each party could terminate the merger agreement, (ii) the obligations of the parties to close the proposed transaction based on certain events, (iii) the required efforts of each party necessary to close the proposed transaction, (iv) the allocation of assets and liabilities between ITC and Entergy related to Entergy's Transmission Business, (v) whether the amount of debt and shares to be issued to Entergy shareholders would be adjusted upon certain events and (vi) other contract provisions. Representatives of the parties also agreed to negotiate after the proposed transaction was announced the form of certain ancillary agreements related to the separation agreement and the merger agreement. There were also calls between Dr. Harvill and Mr. Bready of ITC and Mr. Peebles and Mr. Denault of Entergy to discuss Entergy's plans to elect accelerated tax depreciation and the impacts of such election on Entergy's Transmission Business.

Also on November 22, 2011, representatives of Entergy and ITC met in New Orleans to discuss bargaining unit employees, assumption by ITC of collective bargaining agreements and general employee issues and due diligence meetings related to business operations of ITC and Entergy's Transmission Business were held in Novi, Michigan and attended by representatives of Entergy and ITC.

Also on November 22, 2011, the ITC board sub-committee held a telephonic meeting to receive an update from management and their legal and financial advisors with respect to progress on the proposed transaction.

On November 24, 2011 and November 27, 2011, there were calls between Dr. Harvill and Mr. Peebles to discuss outstanding issues related to the representations and warranties contained in the merger agreement, status of the employee matters agreement, and the progress of other outstanding matters related to the proposed transaction.

On November 25, 2011, Simpson Thacher distributed a revised draft of the employee matters agreement to Skadden, Arps.

Between November 26, 2011 and December 4, 2011, representatives of Entergy, ITC, Skadden, Arps and Simpson Thacher negotiated and exchanged multiple drafts of the employee matters agreement.

On November 27, 2011, Simpson Thacher distributed revised drafts of the merger agreement and the separation agreement to Skadden, Arps. Between November 28, 2011 and December 4, 2011, representatives of Entergy, ITC, Skadden and Simpson Thacher negotiated and exchanged multiple drafts of the merger agreement and the separation agreement.

On November 29, 2011, Mr. Bready met with Mr. Denault in Atlanta, Georgia to discuss the proposed transaction. The discussions included matters regarding Entergy's plans to take accelerated tax depreciation and the impacts of such election on Entergy's Transmission Business; the amount of debt to be incurred by Entergy's Transmission Business; whether the number of shares of ITC common stock to be received by Entergy shareholders in the proposed transaction would be adjusted in certain events; the obligations of the parties to close the proposed transaction under specified circumstances; representations and warranties made by Entergy regarding Entergy's Transmission Business in the merger agreement; social and employee benefit issues; and other open issues. As a result of Entergy's plans to take accelerated tax depreciation, as well as the other matters discussed, Mr. Bready and Mr. Denault negotiated changes to the terms of the proposed transaction to reflect a reduction in the amount of indebtedness that Entergy's Transmission Business would incur prior to the distribution and the merger to \$1.775 billion and an increase in the ITC recapitalization to an amount not to exceed \$700 million.

From November 30, 2011 through December 4, 2011, there were multiple conference calls between representatives from Entergy, ITC, Simpson Thacher, Cooley LLP, Entergy's tax counsel, and Deloitte to discuss and negotiate the tax provisions of the merger agreement and the separation agreement, as well as other outstanding issues, including with respect to the allocation of assets and liabilities between TransCo and Entergy and the standard of efforts required of the parties to obtain certain regulatory approvals, and finalized the merger agreement, the separation agreement and the employee matters agreement.

On December 1, 2011, the ITC board of directors held a special meeting at the offices of ITC in Novi, Michigan. At the meeting, Mr. Bready updated the ITC board of directors on the status of the negotiations with Entergy. Prior to the meeting, the ITC board of directors was provided with substantially complete drafts of the merger agreement, the separation agreement and employee matters agreement and summaries of such agreements. A representative of Dykema reviewed and discussed with the ITC board of directors the fiduciary duties of the directors in the context of considering ITC's strategic alternatives (including the proposed transaction), and senior management and a representative of Simpson Thacher reviewed with the ITC board of directors the principal terms of the merger agreement, the separation agreement and the employee matters agreement. Mr. Bready, together with representatives of J.P. Morgan and Barclays, also reviewed and discussed with the ITC board of directors financial analyses relating to the terms of the proposed transaction. After extensive discussion regarding the proposed transaction, the ITC board of directors instructed management to proceed with final negotiations and work to finalize the merger agreement, the separation agreement and the employee matters agreement.

On December 2, 2011, the Entergy board of directors discussed the proposed transaction at a regularly scheduled meeting at Entergy's New Orleans headquarters. Prior to the meeting, the Entergy board of directors was provided with substantially complete drafts of the merger agreement, the separation agreement and employee matters agreement. All board members were present. Mr. Denault, Mr. Robert D. Sloan, then the Executive Vice President, General Counsel and Secretary of Entergy, Mr. Peebles, Ms. Conley and other representatives from Entergy and representatives from Skadden, Arps and Goldman Sachs presented an update to the Entergy board of directors regarding the proposed transaction. The presentation and discussion included information regarding the proposed transaction on (i) strategic rationale and benefits to Entergy's shareholders, (ii) Entergy's internal valuation of Entergy's Transmission Business and combination analysis of Entergy's Transmission Business with ITC, (iii) Goldman Sachs financial analysis of the proposed transaction, (iv) proposed transaction structure, (v) transaction timing, (vi) employee matters, (vii) other commercial terms, (viii) due diligence results and (ix) next steps. Representatives from Skadden, Arps reviewed with the board the terms of the merger agreement, the separation agreement, the employee matters agreement and the open issues in each agreement. Following this board meeting, the presidents of Entergy Arkansas, Entergy Gulf States Louisiana, Entergy Louisiana, Entergy Mississippi, Entergy New Orleans, Entergy Texas and ESI were given an update on the proposed transaction and a summary of the proposed transaction terms and conditions, including substantially the same information presented to the Entergy board of directors earlier in the day.

From December 2, 2011 through December 4, 2011, final negotiations related to the merger agreement, the separation agreement and the employee matters agreement took place between Entergy and ITC representatives.

On December 3, 2011, the Entergy board of directors held a telephonic special meeting to consider the proposed transaction with ITC. All board members other than Mr. Tauzin were in attendance. Mr. Leonard updated the Entergy board of directors on the status of negotiations with ITC, including the remaining open issues on the transaction agreements. Also present were various representatives from management, including Mr. Denault, Mr. Peebles and Mr. Sloan, and representatives from Skadden, Arps and Goldman Sachs. After considering the foregoing, the presentations and discussions made at prior meetings of the Entergy board of directors, the merger agreement, the separation agreement and the employee matters agreement, and taking into consideration the factors described under the section "—Entergy's Reasons for the Separation, Distribution and the Merger," the Entergy directors present at the meeting unanimously determined that the transaction agreements and the transactions contemplated by the transaction agreements were advisable and in the best interest of Entergy and its shareholders and approved the transaction.

Also on December 3, 2011, the respective governing bodies of Entergy Arkansas, Entergy Gulf States Louisiana, Entergy Louisiana, Entergy Mississippi, Entergy New Orleans, Entergy Texas and ESI considered and approved entering into the separation agreement and related transactions.

On the morning of December 4, 2011, the ITC board of directors held a special telephonic meeting to review the proposed transaction. At the meeting, senior management apprised the ITC board of directors of the status of negotiations and reviewed the terms of the transaction as reflected in the final forms of the merger agreement, the separation agreement and the employee matters agreement. J.P. Morgan delivered its oral opinion to the ITC board of directors (subsequently confirmed by a written opinion dated December 4, 2011) to the effect that, as of such date, and subject to the limitations and assumptions set forth in its written opinion, the aggregate merger consideration is fair to ITC from a financial point of view. Barclays also delivered its oral opinion, (subsequently confirmed by delivery of a written opinion, dated December 4, 2011), to the effect that, as of that date and based upon and subject to the qualifications, limitations and assumptions described in the opinion, the exchange ratio in the merger was fair, from a financial point of view, to ITC. After further discussion, the ITC board of directors determined that the merger agreement, the separation agreement and the employee matters agreement and proposed transactions with Entergy were advisable, fair to and in the best interests of ITC and its shareholders, approved the merger agreement, the separation agreement and the employee matters agreement and the proposed transactions with Entergy in accordance with Michigan law and recommended that the ITC shareholders approve the merger, an amendment to the ITC articles of incorporation to increase the number of authorized shares of ITC common stock and the issuance of ITC common stock pursuant to the merger agreement. The ITC board also authorized senior management to finalize, execute and deliver the merger agreement, the separation agreement and the employee matters agreement.

On December 3 and 4, 2011, internal and external representatives from ITC and Entergy participated in numerous phone calls and other meetings regarding the remaining open issues related to the transaction agreements. On December 4, 2011, representatives of Cooley, LLP met with Mr. Bready, and representatives from Simpson Thacher in New York City to conclude Entergy's due diligence with respect to tax matters.

The merger agreement, the separation agreement and the employee matters agreement were finalized and executed on December 4, 2011.

On December 5, 2011, Entergy and ITC issued a joint press release announcing the execution of the merger agreement, the separation agreement and the employee matters agreement before the opening of trading on the New York Stock Exchange.

Since December 6, 2011, Entergy, ITC and their respective advisors have continued to negotiate and finalize the generator interconnection agreement, the distribution-transmission interconnection agreement, the transition

services agreement, the software/IP license agreement, the pole attachment agreement for electric distribution facilities, the transmission structure attachment agreement for telecommunications facilities, the exchange trust agreement and the registration rights agreement.

On September 21, 2012, the respective parties to the merger agreement entered into Amendment No. 1 to the merger agreement and on September 24, 2012, the respective parties to the separation agreement entered into Amendment No. 1 to the separation agreement.

ITC's Reasons for the Merger; Recommendation of ITC's Board of Directors

ITC's board of directors has approved the merger agreement and the consummation of the transactions contemplated thereby and determined that the terms of the merger agreement and the transactions contemplated thereby, including the issuance of ITC common stock in the merger, are advisable, fair to and in the best interests of ITC and its shareholders. ITC's board of directors recommends that shareholders vote FOR the proposals to approve the merger agreement, to amend the amended and restated articles of incorporation of ITC to increase the number of authorized shares of ITC common stock, to issue ITC common stock in the merger and to approve adjournments or postponements of the special meeting for the purpose of soliciting additional proxies, if necessary.

In reaching its decision to approve the merger agreement and the consummation of the transactions contemplated thereby, the ITC board of directors consulted with its financial and legal advisors and carefully considered a variety of factors, including the following:

- the expectation that the merger will be value accretive to ITC's financial results (after giving effect to the ITC recapitalization), increase ITC's revenues and earnings and enhance cash flow generation;
- the potential that the merger will further enhance ITC's ability to achieve its long-term strategic objectives and position ITC as the preeminent transmission company in the United States, while further strengthening ITC's business model as an independent transmission company;
- the opportunity to significantly expand the scope and scale of ITC's operations by creating one of the largest transmission companies in the United States based on net property, plant and equipment and by load served and expanding ITC's geographic reach through the introduction of new markets in the Gulf States and Mid-South regions;
- the enhanced growth prospects available through ITC's increased size and geographic reach and the shifting of growth to more predictable base capital investments;
- the expectation that the merger will enhance ITC's overall credit quality and significantly enhance ITC's balance sheet strength;
- the expectation that the introduction of sizeable new markets will provide ITC with a stronger operational platform and strengthened financial resources from which to pursue additional development initiatives, which should significantly broaden and de-risk ITC's capital investment opportunities and enhance ITC's ability to pursue new acquisition and investment opportunities;
- the potential that the merger will generate increased visibility and greater access to the capital markets for ITC, which could enhance the market valuation of ITC's common stock and facilitate ITC's ability to access the capital markets going forward;
- information concerning the business, assets, liabilities, financial performance and results of operations, and condition and prospects of ITC and Entergy's Transmission Business;
- the structure of the merger as a tax-free reorganization for federal income tax purposes;
- the experience and prior success of ITC's management in integrating acquisitions into ITC's existing business, and effectively merging corporate cultures;

ITC. J.P. Morgan calculated a range of terminal values of ITC at the end of the projection period by applying a perpetuity growth rate to projected 2021 unlevered free cash flows of \$632 million, which were adjusted for normalized capital expenditures, deferred taxes, depreciation, amortization and changes in net working capital. The perpetuity growth rate range used was 0.5% to 1.0%. The present value of the estimated unlevered free cash flows and terminal values were then calculated using discount rates ranging from 5.75% to 6.25%. This analysis indicated an implied range of enterprise values for ITC of \$7.084 billion to \$8.829 billion, and an implied range of equity values of \$3.184 billion to \$4.929 billion.

Entergy's Transmission Business. J.P. Morgan calculated a range of terminal values of Entergy's Transmission Business at the end of the projection period by applying a perpetuity growth rate to projected 2021 unlevered free cash flows of \$471 million, which were adjusted for normalized capital expenditures, deferred taxes, depreciation, amortization and changes in net working capital. The perpetuity growth rate range used was 0.5% to 1.0%. The present value of the estimated unlevered free cash flows and terminal values for Entergy's Transmission Business pursuant to the management case was calculated using discount rates ranging from 5.75% to 6.25%. Free cash flows of Entergy's Transmission Business did not account for potential cost or other operating synergies or potential concessions, as the extent of these were not known at the time of J.P. Morgan's opinion. These analyses indicated an implied range of enterprise values for Entergy's Transmission Business of \$5.400 billion to \$6.719 billion and an implied range of equity values of \$3.625 billion to \$4.944 billion.

Relative Financial Analysis

J.P. Morgan considered the implied equity values of ITC and Entergy's Transmission Business that were derived from the trading comparables and discounted cash flow analyses to calculate the implied equity ownership percentage on a fully diluted basis for Entergy shareholders in a combination of ITC and Entergy's Transmission Business.

J.P. Morgan compared the high end of the respective ranges for Entergy's Transmission Business to the low end of the respective ranges for ITC to derive the highest relative ownership percentage for Entergy shareholders implied by each of the methodologies. J.P. Morgan also compared the low end of the respective ranges for Entergy's Transmission Business to the high end of the respective ranges for ITC to derive the lowest relative ownership percentage for Entergy shareholders implied by each of the methodologies.

J.P. Morgan compared the implied range of ownership percentages to the approximately 50.1% of the outstanding ITC common stock that Entergy shareholders will own following the effective time of the merger, and noted that the 50.1% ownership level was within the range of implied equity ownership percentages derived using this analysis.

The following table reflects the results of the analysis:

	<u>Implied Entergy shareholder equity ownership % range</u>
Trading comparables	
Price to 2013 projected net income	41.1% – 58.8%
EV to 2013 projected EBITDA	42.5% – 73.7%
Discounted cash flow	
ITC + Transco management case	42.4% – 60.8%

Other Analyses

Value Creation Analysis. J.P. Morgan reviewed for informational purposes the potential value creation of the transactions for ITC shareholders. J.P. Morgan reviewed the discounted cash flow value creation by comparing the equity value per share implied for ITC on a standalone basis and the potential pro forma equity value per share implied for ITC after the transactions. For illustrative purposes, J.P. Morgan calculated a

standalone pro forma equity value for ITC utilizing the midpoint of the enterprise value reference range implied from the discounted cash flow analysis of ITC described above, less ITC's projected net debt as of December 31, 2012 as well as the \$740 million in debt expected to be incurred by ITC in the transactions. J.P. Morgan then added to such implied equity value the midpoint of the equity value reference range implied from the discounted cash flow analysis of Entergy's Transmission Business described above. J.P. Morgan then calculated the value attributable to each share of ITC common stock in the resulting implied equity value of the pro forma combined company plus the amount to be paid with respect to each share of ITC common stock in the ITC recapitalization. This analysis indicated potential pro forma value creation for ITC shareholders of approximately 1.6%.

J.P. Morgan also reviewed for informational purposes the market value creation by comparing the equity value per share implied for ITC, using a multiple of 18.6x ITC management estimates of 2013 net income for ITC, and the pro forma equity value per share implied for ITC after the transactions, utilizing a range of multiples of 17.6x to 20.9x ITC management estimates of 2013 net income for ITC and including the amount to be paid with respect to each share of ITC common stock in the ITC recapitalization. This analysis indicated potential pro forma value creation for ITC shareholders ranging from (0.2)% to 15.5%.

Relative Contribution Analysis. J.P. Morgan calculated for information purposes the relative contributions of ITC and Entergy's Transmission Business to the estimated total rate base of the combined company for 2012 and 2013 as well as the combined company's estimated EBITDA and net income for 2013 and 2014, respectively, based on ITC management estimates, in the case of ITC, and ITC management's view on estimates provided by Entergy, in the case of Entergy's Transmission Business. J.P. Morgan also calculated the relative contributions of ITC and Entergy's Transmission Business to the pro forma equity value of the combined company implied by the discounted cash flows as discussed above. This analysis indicated a range of implied ownership percentages for ITC's current shareholders immediately after the transactions as set forth in the below table as compared to the implied 49.9% ownership percentage set forth in the merger agreement.

	<u>Implied ITC shareholder equity ownership %</u>
Rate Base	
Estimated 2012 ¹	47.1%
Estimated 2013 ¹	51.2%
Estimated 2012 (equity rate base) ²	55.6%
EBITDA	
Estimated 2013 ¹	46.4%
Estimated 2014 ¹	47.6%
Net income	
Estimated 2013	50.0%
Estimated 2014	50.6%
DCF	
ITC DCF vs. Entergy's Transmission Business DCF ³	48.5%
Entergy's Transmission Business DCF vs. ITC Market Cap ⁴	51.3%

- 1 Percentages represent leverage adjusted contribution using estimated net debt as of December 31, 2012 of \$3.900 billion for ITC and \$1.775 billion for Entergy's Transmission Business and management case mid-point DCF enterprise values.
- 2 Represents unadjusted relative contribution of equity portion of rate base.
- 3 Represents ITC and Entergy's Transmission Business equity values as of December 31, 2012.
- 4 Represents ITC market cap as of November 30, 2011 and Entergy's Transmission Business DCF equity value with a valuation date of November 30, 2011.

Other. J.P. Morgan did not conduct a comparable transaction analysis because other business combination and acquisition transactions involving companies in similar industries as ITC and Entergy's Transmission Business generally included control premiums, whereas the proposed transaction did not include a premium.

5

Data Request No. APSC-019-1

Data Request: Provide all due diligence reports on Entergy transmission assets and operations produced by or for ITC related to the transaction.

Response: All documents responsive to this request prepared in connection with this transaction are privileged attorney work product and contain privileged attorney-client communication.

6

Data Request No. APSC-022-1

Data Request: Reference the Application, page 25, paragraph 35 (*"The Transaction is the final step to be taken by the Entergy Operating Companies in their continuing evolution toward greater transparency and independence in the operation and management of the Entergy Transmission System."*) as well as EAI's Evaluation Report filed on 5/12/2011 in APSC Docket 10-011-U, page 49 (*"RTOs will provide greater independence in the areas of transmission planning and the development and operation of markets."*). Please identify all ways in which the transaction will enhance independence of Entergy's transmission system that are not achievable under Entergy ownership and MISO operation and planning. Provide all documentation supporting your response.

Response: Independence will be enhanced because the transmission system will be owned by an independent entity that does not also own generation or distribution assets which would not be the case under Entergy's ownership or MISO operation and planning. As addressed in great detail in the direct testimony of Joseph Welch, ITC's independent business model is structured with a singular focus on transmission, which means that all financial and other company resources are utilized to build, operate, and maintain best in class transmission that provides access to the lowest cost generation available. All of ITC's decisions are made based on the needs of customers and the system. ITC's track record of making investments to improve reliability and provide greater access to wholesale energy markets is outlined throughout the case filing.

MISO membership alone does not lead to the same results, because the individual transmission owner continues to play a critical role in the RTO planning process which is largely derived from projects submitted by the transmission owner. Therefore, the owner's approach to transmission development affects what will ultimately be built. ITC's broader, regional approach to transmission development provides more robust and effective regional transmission projects than might otherwise be considered. In addition, as stated on page 54 of Mr. Welch's Direct Testimony, the RTO "does not perform local operations, fund or perform maintenance on the system, fund or build capital projects or generator interconnections, or respond to customer needs or

concerns on the ground.” As such, independent ownership is the best model to provide the focus and financial capability to achieve the most effective transmission system.

7

Data Request No. APSC-022-7

Data Request: Condition 4 in Order No. 68 issued by the Commission in Docket 10-011-U states:

"Should EAI become a member of MISO, EAI shall agree that it will not exit MISO without first filing an application with the Commission seeking its approval for a change of control of its transmission assets. EAI will otherwise retain all of its rights, state and federal, to appeal or seek review of or relief from the decision of the Commission."

Should Entergy and ITC complete the proposed transaction:

- a. Should ITC choose to exit MISO, does ITC intend to file an application with the Commission seeking approval for a change of control of transmission assets before it exits MISO?
- b. If not, please explain ITC's view of why such an action would not be appropriate.

Response: ITC objects to this request on the grounds that it seeks legal conclusions. Subject to, and without waiving the foregoing, ITC responds as follows:

The preamble to this request assumes that ITC and Entergy "complete the proposed transaction." ITC interprets this request as asking it to assume that ITC and Entergy have obtained all necessary regulatory approvals for closing, including the approval of the Arkansas Public Service Commission, that all other conditions to closing have occurred and that the parties have closed the Transaction transferring ownership of the transmission assets to ITC Arkansas.

- a. Based on the above assumption, and based upon ITC's review of the applicable statutes and regulations, ITC Arkansas would not need permission from the Commission to withdraw from MISO. Upon completion of the Transaction, ITC Arkansas will own these transmission assets and will be an Appendix I Member of MISO. The Federal Energy Regulatory Commission (FERC) has exclusive authority over transmission in interstate commerce under Section 201(b) of the Federal Power Act. Thus, the FERC would be the

appropriate authority to address ITC Arkansas' membership or withdrawal from a regional transmission organization. However, ITC Arkansas will have robust stakeholder outreach and ongoing communication with the APSC about its plans and operations impacting Arkansas.

- b. See the response to a.

8

Data Request No. APSC-022-8

Data Request: Condition 5 in Order No. 68 issued by the Commission in Docket 10-011-U states:

"Should EAI become a member of MISO, EAI shall agree that the Commission, sua sponte or upon the motion of any party, after notice and hearing, may direct EAI to exit MISO under the terms of the Memorandum of Understanding or the TOA. EAI will otherwise retain all of its rights, state and federal, to appeal or seek review of or relief from the decision of the Commission."

Should Entergy and ITC complete the proposed transaction:

- a. Could the Commission direct ITC to exit MISO after notice and hearing?
- b. If not, please explain ITC's view of why the Commission would not have this authority.

Response: ITC objects to this request on the grounds that it seeks a legal conclusion. Subject to, and without waiving the foregoing, ITC responds as follows:

The preamble to this request assumes that ITC and Entergy "complete the proposed transaction." ITC interprets this request as asking it to assume that ITC and Entergy have obtained all necessary regulatory approvals for closing, including the approval of the Arkansas Public Service Commission, that all other conditions to closing have occurred and that the parties have closed the Transaction transferring ownership of the transmission assets to ITC Arkansas.

- a. The Commission could request ITC Arkansas to withdraw its transmission assets from MISO, but ITC Arkansas would have to agree to the withdrawal and such an exit would have to be approved by FERC and would be subject to the processes and requirements of the MISO tariff and the MISO TOA, with possible assessment of exit fees and costs.
- b. As discussed in response to APSC 22-7, as a transmission-only public utility, ITC Arkansas' rates will be exclusively under the

authority of the Federal Energy Regulatory Commission (FERC). As such, the FERC would be the appropriate authority to address ITC Arkansas' membership or withdrawal from MISO.

9

Data Request No. APSC-022-9

Data Request: Condition 6 in Order No. 68 issued by the Commission in Docket 10-011-U states:

"Should EAI become a member of MISO, EAI shall remain under the Commission's jurisdiction, to the extent not otherwise preempted by FERC, with respect to retail electric rates and all related electric facility operations, facility siting, financing, and reliability."

Should Entergy and ITC complete the proposed transaction:

- a. What is ITC's view regarding whether FERC or the APSC have jurisdiction over the following transmission issues:
 - i. Retail rates for transmission service
 - ii. Electric facility operations
 - iii. Reliability
 - iv. Financing
 - v. Facility siting

Response: ITC objects to this request on the grounds that it seeks legal conclusions. Subject to, and without waiving the foregoing, ITC responds as follows:

The preamble to this request assumes that ITC and Entergy "complete the proposed transaction." ITC interprets this request as asking it to assume that ITC and Entergy have obtained all necessary regulatory approvals for closing, including the approval of the Arkansas Public Service Commission, that all other conditions to closing have occurred and that the parties have closed the Transaction transferring ownership of the transmission assets to ITC Arkansas.

- i. In *New York v. FERC*, No. 00-568, decided March 4, 2002, the Supreme Court determined that FERC properly exercised its transmission rate jurisdiction over transmission service "unbundled" from the retail sale of electric energy. As a result of the Transaction, transmission service would be provided by ITC Arkansas separate and "unbundled" from the sale of electricity by EAI. Therefore,

FERC would determine the rate for transmission service over ITC Arkansas' facilities, not the APSC.

- ii. FERC has exclusive jurisdiction over transmission in interstate commerce, including facilities used to provide that transmission.
- iii. Under Section 215 of the Federal Power Act, FERC has jurisdiction over reliability of the Bulk Power System, including transmission in interstate commerce. In accordance with that provision of the Federal Power Act, FERC has designated NERC as the National Electric Reliability Organization and approves reliability standards developed by NERC. ITC Arkansas will have a contractual obligation under the Distribution-Transmission Interconnection Agreement with Entergy to provide it with reliable service so that it can meet the APSC's requirements for service to customers.
- iv. Section 204 of the Federal Power Act regulates the issuance of securities by FERC-jurisdictional public utilities. In construing similar language in the Natural Gas Act, the Supreme Court has determined that this language pre-empts state regulation of the same transactions. *See Schneidewind v. ANR Pipeline Company*, 485 U.S. 293 (1988).
- v. The APSC has authority over siting of transmission facilities in Arkansas. See Ark. Code Ann. §§ 23-18-501 et seq and 23-3-201 et seq.

10

Data Request No. APSC-022-10

Data Request: Condition 7 in Order No. 68 issued by the Commission in Docket 10-011-U states:

"Should EAI become a member of MISO, EAI shall agree that the Commission, sua sponte or upon the motion of any party to this proceeding, may, after notice and hearing, reconsider and, if necessary, reverse any approval of the transfer of control if:

a) The terms of FERC's approval of the modifications to the MISO Tariff to transition EAI into MISO are materially changed such that the revised terms will have a material adverse impact on EAI's retail ratepayers; or

b) Any of the foregoing conditions are not fully adopted, incorporated or realized."

Should Entergy and ITC complete the proposed transaction:

- a. Could the Commission reverse its approval of the transfer of control of assets currently owned by EAI to MISO?
- b. Could the Commission direct ITC to exit MISO for the reasons specified in the condition?
- c. If the answer to either part a or part b is no, please explain ITC's view of why the Commission would not have this authority.

Response: ITC objects to this request on the grounds that it seeks legal conclusions. Subject to, and without waiving the foregoing, ITC responds as follows:

The preamble to this request assumes that ITC and Entergy "complete the proposed transaction." ITC interprets this request as asking it to assume that ITC and Entergy have obtained all necessary regulatory approvals for closing, including the approval of the Arkansas Public Service Commission, that all other conditions to closing have occurred and that the parties have closed the Transaction transferring ownership of the transmission assets to ITC Arkansas.

- a. Based on the above assumption, no, the Commission could not unilaterally reverse the transfer of control to MISO of the transmission assets which by then would be owned by ITC Arkansas. Upon completion of the Transaction, ITC Arkansas will own these transmission assets and will be an Appendix I Member of MISO. While the Commission may ask ITC Arkansas to withdraw, ITC Arkansas withdrawal from MISO would be subject to FERC approval and would have to be accomplished pursuant to the processes and requirements of the MISO Tariff and TOA, including possible assessment of exit fees and costs.
- b. The Commission could request ITC Arkansas to withdraw its transmission assets from MISO, but under the assumptions set forth above, any such exit would have to be approved by FERC and could be subject to substantial fees and costs. See ITC Response to APSC 22-7.
- c. Please see the answers to a and b above.

11

Data Request No. APSC-022-11

Data Request: Condition 8 in Order No. 68 issued by the Commission in Docket 10-011-U states:

"Should EAI become a member of MISO, EAI shall not unbundle transmission or seek to make basic changes to transmission service for retail ratemaking without prior APSC approval. EAI shall negotiate a transmission service agreement with MISO that ensures that the APSC continues to determine the transmission component of the rates to serve EAI's bundled retail load."

Should Entergy and ITC complete the proposed transaction:

- a. Will ITC have a transmission service agreement with MISO that ensures that the APSC continues to determine the transmission component of the rates to serve EAI's bundled retail load? Why or why not?

Response: ITC objects to this request on the grounds that it seeks legal conclusions. Subject to, and without waiving the foregoing, ITC responds as follows:

The preamble to this request assumes that ITC and Entergy "complete the proposed transaction." ITC interprets this request as asking it to assume that ITC and Entergy have obtained all necessary regulatory approvals for closing, including the approval of the Arkansas Public Service Commission, that all other conditions to closing have occurred and that the parties have closed the Transaction transferring ownership of the transmission assets to ITC Arkansas.

- a. Based on the above assumption, no. As per the Response to APSC 22-7, the Transaction will have already resulted in the "unbundling" of transmission from generation and distribution service. The Federal Energy Regulatory Commission will set the rate for transmission services provided over ITC Arkansas' facilities.

12

Data Request No. APSC-022-13

Data Request: Condition 14 in Order No. 68 issued by the Commission in Docket 10-011-U states:

"Should EAI become a member of MISO, no later than three years after joining MISO and every two years thereafter, assuming EAI continues as a MISO member, EAI shall file with the Commission a detailed report providing the following information:

- a. The quantified historical net benefits of MISO membership for EAI, as compared to the stand-alone option, as of the date of each of the reports described above;*
- b. The projected net benefits of MISO membership for EAI, as compared to the stand-alone option, for the post-transition period on a bi-annual basis beginning one year after the end of the transition period;*
- c. Any significant changes in FERC RTO policies, rules or regulations, MISO requirements, Day 2 market conditions, or other regulatory or market structure components; and*
- d. An estimate of the costs to exit MISO after the end of the five-year transition period or a specified time thereafter and to transition to a new operating environment such as a different RTO."*

Should Entergy and ITC complete the proposed transaction:

- a. Will ITC provide the above information to the Commission?
- b. If not, please describe why such action would be inappropriate.
- c. If so, please explain how, if at all, ITC would collaborate with EAI to produce such information.

Response: ITC objects to this request on the grounds that it seeks legal conclusions. Subject to, and without waiving the foregoing, ITC responds as follows:

The preamble to this request assumes that ITC and Entergy "complete the proposed transaction." ITC interprets this request as

asking it to assume that ITC and Entergy have obtained all necessary regulatory approvals for closing, including the approval of the Arkansas Public Service Commission, that all other conditions to closing have occurred and that the parties have closed the Transaction transferring ownership of the transmission assets to ITC Arkansas.

- a. With respect to the information described in subparts a, b, and d, above, ITC Arkansas as a transmission-owner only will not have the necessary information to respond to these requests. With respect to subpart c, ITC Arkansas is willing to provide information to the Commission as to FERC or MISO significant transmission policy changes and will do so if requested by the Commission.
- b. See response to a. above.
- c. ITC is willing to collaborate with EAI to produce the information requested, to the extent the sharing of information is allowed by FERC's Standards of Conduct for Transmission Providers.

13

Data Request No. APSC-024-2

Data Request: Reference ITC's July 1, 2011 non-binding indication of interest in acquiring Entergy's transmission business. The section under the header "Requisite State and Local Jurisdictional Approvals" contains the quote: "[t]he Acquiring Company has considered and analyzed several additional qualitative and quantitative mitigation options that could be employed as elements of an overall transaction. As noted in the 'Valuation and Conforming Assumptions' section above, our indicative value is premised on the inclusion of specific and substantial financial concessions relative to the regulatory approval process. These options include provisions to maintain transmission rates at their current levels for a specified period of time; a phase-in of any transmission rate increases associated with the transactions over a specified period of time; and, substantial rebates to customers of the Company."

- c. Provide a detailed description of the concessions included in ITC's bid as well as any workpapers used to calculate the value or impact of the concessions. Workpapers should be provided in electronic spreadsheet format with formulas intact.
- d. Provide a detailed description of all other concessions considered by the parties during the negotiations as well as any workpapers used to calculate the value or impact of the concessions. Workpapers should be provided in electronic spreadsheet format with formulas intact.
- e. Provide references to all points in testimony and workpapers filed by either Entergy or ITC reflecting these concessions.

Response:

- c. ITC objects to this request on the grounds that it seeks confidential information and documents protected by the attorney work product doctrine and attorney-client privilege.

- d. ITC objects to this request on the grounds that it seeks confidential information and documents protected by the attorney work product doctrine and attorney-client privilege.
- e. No testimony or workpapers filed by ITC or EAI reflect concessions referenced in ITC's July 1, 2011 non-binding indication of interest in acquiring the Entergy Operating Companies' transmission business.

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Data Request No. APSC-027-1

Data Request: Reference the Direct Testimony of Jay Lewis, pages 17-23, discussing the negative cash flow nature of Entergy's transmission business.

- a. Please explain how the change in ownership will address the conditions leading to the negative cash flow described in the Lewis Testimony
- b. Provide any documentation and workpapers demonstrating the impact that the change in ownership to ITC will have on the cash flow of the transmission business. Workpapers should be provided in electronic spreadsheet format with formulas intact.

Response:

- a. As indicated in the previously filed Direct Testimony of Jay A. Lewis, Vice President, Regulatory Strategy Entergy Services, Inc. on Behalf of Entergy Arkansas, Inc., under Entergy ownership, internally generated cash flows attributable to the transmission business will not be adequate to fund transmission capital requirements. Therefore, the transmission function is placing greater pressure on cash flow than the generation and distribution functions at Entergy. As explained in the previously filed Direct Testimony and Exhibits of Cameron M. Bready on Behalf of ITC Holdings Corp. and ITC Midsouth, LLC, ITC's regulatory construct, including its requested return on equity, capital structure and forward-looking formula rates, ensures 1) steady and predictable cash flow generation and 2) deep access to cost-effective capital to absorb the sustained and significant capital investment requirements of Entergy's transmission business. Moreover, given ITC's singular focus on transmission, ITC is void of any internal competition for capital unlike vertically integrated utilities. As such, ITC is well equipped to support cash-heavy transmission investments.
- b. ITC is not in the possession of workpapers or other documentation responsive to this request.

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Data Request No. APSC-027-2

Data Request: Reference the Commission Order No. 54 in Docket No. 10-011-U, page 86: "Similarly, EAI should not be involved in any allocation processes associated with services received from ESI. Currently, ESI provides a variety of legal, engineering, and regulatory services to the OpCos with a variety of allocation methodologies associated with bills that the OpCos receive from ESI." Reference also the Commission Order No. 68 in Docket No. 10-011-U, page 11: "In light of the above, the Commission reiterates that EAI should negotiate cost-based contracts with ESI and any other Entergy service company, separate and apart from the other OpCos and with no cost allocations with the other OpCos."

- c. Please explain whether the planning and operation of the transmission system under ITC ownership will require the types of cost allocation among the wires subsidiaries contemplated by the Commission's orders. Provide any documentation supporting your response.
- d. If so, provide a detailed explanation of how such costs will be allocated to the various wires subsidiaries and how this would impact transmission rates in each planned transmission pricing zone in the Entergy region.

Response:

- c. ITC Holdings Corp. directly assigns costs to its affiliates where it is rational and reasonably clear to do so. It is anticipated that the majority of the costs for planning and operating the transmission system, including facilities and labor related costs, will be directly assigned to a specific operating company. With respect to costs that cannot be assigned directly, those costs will be allocated to the ITC Midsouth Operating Companies in accordance with ITC's FERC approved methodology for the allocation of such costs.
- d. For the allocation of costs that cannot be directly assigned, ITC Holdings Corp. uses a FERC-approved formula, based on the Massachusetts formula. This formula is described in Exhibit No. ITC-505 to the testimony of ITC Witness Fred Stibor, Exhibit No. ITC-500, in the Joint Application pending before FERC in Docket No. EC12-145 et al. ITC does not include any markups, premiums, or similar items on any costs assigned or allocated to its operating companies.

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Attachment 3

EAI's Non-Public Responses to Data Requests

1. APSC 11-1, Addendum 2
2. APSC 17-1, Response Letter
3. APSC 17-2, Transmission Update and Attachment 2e
4. APSC 23-5
5. APSC 23-9
6. APSC 34-2, Attachment (partial)

THESE RESPONSES ARE REDACTED PURSUANT TO ORDER NO. 2

Table of Contents Attachment 4

ITC's Non-Public Responses to Data Requests

1. APSC 10-17 (partial)

THIS RESPONSE IS REDACTED PURSUANT TO ORDER NO. 2

CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing has been served on all parties of record by forwarding the same by electronic mail and/or first class mail, postage prepaid, this 19th day of April, 2013.

/s/ Valerie F. Boyce
Valerie F. Boyce