EL PASO ELECTRIC CO

Moderator: Steven Busser
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9:30 am CT

Operator: Thank you for standing by. Good day and welcome to the El Paso Electric third quarter earnings conference call. Today's call is being recorded and at this time I'd like to turn the conference call over to the Treasurer, Steve Busser. Please go ahead, sir.

Steve Busser: Thank you, Matt and good morning everyone and thank you for joining the El Paso Electric Company third quarter 2011 earnings conference call. Also on the call with me today I have our CEO, David Stevens and our CFO, David Carpenter. Today we'll provide an update on our third quarter 2011 and year-to-date performance highlights and we will discuss key earnings drivers. We will also provide an update on regulatory matters, the revisions we have made to our 2011 earnings guidance and our capital allocation strategy in 2012.

Before we get started I would like to cover some items that will be pertinent to our call. You should have a copy of our press release. If you do not, you can obtain one from our website at www.epelectric.com on the Investor Relations page.

We currently anticipate that our third quarter 2011 Form 10-Q will be filed with the Securities and Exchange Commission (SEC) on or before November 9, 2011.

Please call our Investor Relations Department if you have any inquiries or require further information.

A replay of today's call will be made available shortly after our call ends and it will run through November 16, 2011. The details as it relates to the replay are disclosed in our press release.

Let me cover the Safe Harbor Provisions before I turn the call over to David Stevens.

On page 2 of our presentation you'll see our safe harbor statement. In summary, our comments and answers to your questions may include forward-looking statements made pursuant to the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. Such forward-looking statements involve known and unknown risks and other factors which may cause the Company's actual results in future periods to differ materially from those expressed here. Any such statement is qualified by reference to the risks and factors discussed in the Company's SEC Act filings. Our 10-K and other SEC filings contain our forward-looking statements and also lay out the risk factors that should be considered. These filings may be obtained upon request from the company, on our website, or from the SEC.

The Company cautions that the risk factors discussed in these filing are not exclusive and we do not undertake to update any forward-looking statement that may be made from time to time by or on behalf of the Company. These statements, especially those made during the question and answer section of the call, are subject to risks and uncertainties that are difficult to predict.

Now I'd like to turn the call over to our CEO, David Stevens.

David Stevens: Thank you, Steve. Good morning and thank you for joining our call. This is David Stevens, CEO of El Paso Electric.

If you'll now turn to page 3, I'd like to go over our third quarter 2011 highlights. I'm very pleased with our strong third quarter earnings of $1.41 per basic share which represents a $0.25 per share increase over the same period in 2010, excluding the 2010 extraordinary gain. Overall, we were significantly assisted by the hotter than normal summer weather we experienced in our service territory. During the third quarter of 2011, we estimate that almost half of the KWh increase was related to hotter than normal summer weather. We also continue to see strong growth in our customer base and increased usage per customer.

These increases translated into a new native peak load record of 1,711 megawatts on August 8, 2011, which was 95 megawatts or nearly six percent greater than the peak we achieved in 2010. The growth in our native peak load demand is driving our need to obtain new generation resources. To this end, we plan to add approximately 1,100 MW's of new generation in the next 10 years and over that same time frame will be retiring approximately 565 megawatts of older, natural gas-fired generation.

Our third quarter results also include a one-time benefit of $4.7 million for net transmission revenue and related interest income which we recorded after attaining final approval from the Federal Energy Regulatory Commission (FERC) for the settlement with Tucson Electric Power Company (TEP) to resolve the long-standing transmission service dispute.

Also of significance during the third quarter of 2011, in addition to our regular dividend, we repurchased approximately 1.6 million shares of stock at a total cost of $51 million. We remain focused on enhancing long-term shareholder value while managing our capital structure through a combination of share repurchases and cash dividends. Our cash dividend and share repurchases are both beneficial to our customers and investors, with share repurchases reducing the company's overall cost of capital. This, in turn, translates into lower costs for the company and lower costs for customers. The dividend and share repurchase programs also ensure that we have a properly balanced capital structure. During 2012, the Company expects to primarily utilize dividends to maintain a balanced capital structure, supplemented by share repurchases when appropriate. The company is expecting to move toward a 45 percent payout ratio for 2012.

In closing, before handing the call off to David Carpenter, I would like to personally thank the entire team of El Paso Electric employees for their strong work ethic and for their significant contributions they have made towards attaining our goals. I am very proud of our employees and they continue to be an integral part of the success of our company. Now, let me turn the call over to David Carpenter.

David Carpenter: Thank you, David. Now, turning to slide 4 of our presentation, we reported net income of $58.3 million or $1.41 per basic share for the third quarter of 2011, compared to our third quarter 2010 income of $49.9 million or $1.16 per basic share before an extraordinary item. For the nine months ended September 30, 2011, we posted net income of $98.1 million or $2.33 per basic share, compared to net income of $82.9 million or $1.90 per basic share before an extraordinary item for the nine months ended September 30, 2010.

Now if you turn to slide 5, I would like to discuss the main earnings drivers for both the third quarter of 2011 compared to the third quarter of 2010 and year-to-date earnings through September 30, 2011 compared to year-to-date earnings through September 30, 2010.

The primary earnings driver for both the quarter and year-to-date periods compared to the prior year was the significant increase in revenues that we have seen in 2011. Retail non-fuel base revenues increased $13.6 million in the third quarter of 2011 and increased $31.5 million in the year-to-date period ended September 30, 2011. The increase in retail non-fuel base revenue contributed$0.21 to earnings per share for the quarter and $0.47 to earnings per share year-to-date. I will provide additional information on the revenue increase later in the presentation.

Another positive earnings driver for both the third quarter of 2011 and the year-to-date period ended September 30 was the effect of a settlement with TEP regarding the provision of transmission wheeling that was approved by the FERC on August 31, 2011. As a result, we recognized $4.7 million in net transmission revenues and associated interest income in the third quarter of 2011 adding $0.07 per share. We will receive ongoing transmission revenues of approximately $1.1 million annually as a result of this settlement.

The reduction in our weighted average number of shares outstanding, as a result of our stock repurchase plan, contributed $0.05 in earnings per share in the third quarter of 2011 and $0.08 in earnings per share in the year-to-date period ended September 30, 2011.

In addition earnings increased in the year-to-date period ended September 30, 2011 compared to the same period in 2010 due to a one-time charge to income tax expense in 2010, to reflect the elimination of the Medicare Part D subsidy without any offsetting amount in the current year. This item positively impacted our current year-to-date earnings by $4.8 million or $0.11 per share.

Partially offsetting these positive earnings drivers in the quarter and year-to-date periods were decreases in allowance for funds used during construction due to lower construction work-in-progress balances resulting from the completion of Phase II of Newman Unit 5. Earnings declined $0.04 per share in both the third quarter of 2011 and the year-to-date period ended September 30, 2011 due to the decrease in allowance for funds used during construction.

For the nine months ended September 30, 2011, these positive factors were offset by lower retained off-system sales margins which declined by $6.1 million pre-tax or $0.09 per share. With the new rate agreements effective in July 2010, the Company now shares 90 percent of these margins with customers where it previously shared only 25 percent. Off-system sales margins were also affected by lower average market prices for power.

On slide 6, we show the percentage changes in retail megawatt-hour sales and non-fuel base revenue to residential and small commercial and industrial customers for both the third quarter of 2011 compared to the third quarter of 2010 and for the year-to-date periods ended September 30, 2011 and 2010. In the third quarter of 2011, our total retail megawatt-hour sales grew by 3.9 percent primarily reflecting hotter than normal summer weather as cooling degree days were 11.5 percent higher than the same period in 2010 and were 27 percent higher than the 30-year average. The hot summer weather also impacted megawatt-hour sales for the year-to-date period ended September 30, 2011 compared to the year-to-date period ended September 30, 2010. Cooling degree days for the year-to-date period ended September 2011 were 15 percent higher than the same period in 2010 and 29 percent higher than the 30-year average. As a result, total megawatt-hour sales for the nine months ended September 30, 2011 compared to the nine months ended September 30, 2010 increased by 3.2 percent.

The impact of weather is most significant on the megawatt-hour sales to residential and small commercial customers. Residential megawatt-hour sales grew by 9.8 percent in the third quarter of 2011 and 6.1 percent in the year-to-date period ended September 30, 2011. Small commercial and industrial megawatt-hour sales grew by 3.9 percent in the third quarter of 2011 and 3.1 percent in the year-to-date period ended September 30, 2011. The growth in megawatt-hour sales resulted in increases in non-fuel base revenues from residential and small commercial customers of 9.4 percent and 5 percent, respectively in the third quarter and 9.4 percent and 4.7 percent, respectively for the year-to-date period ended September 30, 2011. We also saw non-fuel base revenues increase from large commercial and industrial customers and from other public authorities in both the third quarter of 2011 and in the year-to-date period. Non-fuel base revenues from other public authority customers reflect increased sales to Fort Bliss at a higher rate per firm power. Currently, Fort Bliss represents about 70 megawatts of load and we expect the overall load at Fort Bliss to grow to over 90 megawatts by 2013 due to the additional soldiers and family members that are anticipated to be stationed at the Fort. As of October 30, 2011, Fort Bliss had an active duty soldier population of almost 28,000 soldiers and the soldier population is expected to grow to 30,000 soldiers by the end of 2012. At Fort Bliss, the $5 billion construction program is on-going and they broke ground in August 2011 on an additional $1 billion state-of-the-art hospital on the base which will be operational by 2016.

Also, contributing to our increased retail megawatt-hour sales was growth in the number of customers served as customers served in September 2011 were 1.5 percent higher than in September 2010 due to our expanding local economy.

Now turning to slide 7, I would like to update you on recent actions taken by the El Paso City Council. On October 4, 2011, the El Paso City Council adopted a resolution ordering the Company to show cause as to why its base rates for customers in the El Paso city limits should not be lowered and ordering the Company to file a rate filing package supporting its rates and initiating a rate case by February 1, 2012. The City of El Paso also adopted a resolution to conduct a temporary rate hearing on October 25, 2011. The City Staff notified the Company on October 20 that the temporary rate hearing was being postponed until November 15, 2011. The City Staff then notified us the day before the hearing that we might need to support our rates at the temporary rate hearing scheduled for October 25, 2011. At the temporary rate hearing on October 25, we made a presentation on the reasonableness of our rates and requested that temporary rates not be implemented. The City's outside regulatory attorney made a recommendation to set current rates as temporary rates. The City deferred a decision on temporary rates until November 15, 2011. At that time, the City could accept our recommendation to not implement temporary rates, vote to make our current rates temporary or vote to implement temporary rates at a reduced level. If temporary rates are implemented, they will be subject to refund or surcharge after a final decision by the PUCT.

On October 27, 2011, the Company filed an appeal of the City's Show Cause Order and requested that the PUCT vacate the City's resolution requiring the Company to Show Cause as to why rates should not be lowered. In alternative, the Company has requested that the PUCT require the City to establish a process whereby they would be required to objectively review the Company's cost of service and rates and stay the proceedings in this instance until the City completes a review consistent with the Public Utility Regulatory Act and PUCT standards and processes. The Company made this filing based on the premise that it believes that the City of El Paso has taken their actions absent any supporting factual support or analysis to demonstrate that the level of the EPE's investment or cost of providing utility services has materially changed during the fifteen months since the PUCT's Final Order in the Company's last rate case, or that EPE's base rates are no longer just and reasonable or in the public interest. In fact, investments in new plants have increased our net plant service by $260 million since our last rate case. In addition, we filed an earnings monitoring report with the PUCT showing that on a year ended June 30, 2011 basis our return on equity was slightly above 9 percent.

If the Show-Cause proceeding continues, in addition to filing for a rate increase within the City, we will file for a rate increase with the PUCT for rates outside the city limits and the other cities within our Texas service territory in order to maintain uniform rates notwithstanding the temporary rate issue. We plan to continue to vigorously defend ourselves against the efforts of the El Paso City Council to lower our rates which we believe are fair and reasonable and, in fact, should be raised if the show cause continues forward. If the rate case goes forward, a final decision is not likely before August 2012.

Now, turning to slide 8, I would like to discuss our capital requirements and our liquidity position. In terms of our capital requirements, we expended approximately $130 million for additions to utility plant in the first nine months of 2011. We currently expect to spend about $179 million for new construction in 2011. We also expect to pay approximately $27.6 million in dividends to our shareholders in 2011. During the first nine months of 2011, we repurchased 2.5 million shares of common stock at a cost of $77.3 million including $51 million in the third quarter of 2011. The repurchases in the third quarter of 2011 were primarily made from cash flow from operations. Approximately 674,000 shares remain available for repurchase under our current share authorization. We expect to continue to make additional share repurchases in excess of the dividends we pay to shareholders in the future to balance our capital structure.

At September 30, 2011 our liquidity was almost $190 million which consisted of a cash balance of $7.7 million and borrowing capability available to us on our credit facility of approximately $182 million.

On slide 9, you will see in October 2011, we received FERC and New Mexico Public Regulation Commission approval to amend and restate our $200 million revolving credit facility, which will lower our borrowing costs and extend the maturity of our revolving credit facility from September 2014 to September 2016. In addition, we also received approval to issue long-term debt up to $300 million to meet our expected need for long-term debt through 2014 which provides us with the flexibility to access the debt capital markets when needed and when conditions are favorable. While we believe that the available liquidity we have along with cash from operations will be sufficient to finance our capital requirements in 2012, it is likely that we will seek to issue long-term debt in the form of a fixed rate debt issuance in 2012. The timing and extent of such debt issuance is not yet known at this time.

Now turning to slide 10, we are revising our 2011 earnings guidance upward and tightening the range to $2.40 per share to $2.60 per share from a range of $2.20 per share to $2.50 per share. The primary driver for the revision was the above average sales and revenues we experienced in the third quarter resulting from the hotter than normal summer weather that we experienced this year.

Now, turning to slide 11, as David said at the beginning, El Paso Electric continues to utilize a combination of dividends and share repurchases to return capital to our shareholders, while maintaining a balanced capital structure. We will also continue to maintain a prudent level of liquidity as well as take market conditions for debt and equity securities into account. With the initiation of the dividend in early 2011, we were moving toward primarily utilizing the dividend to maintain a balanced capital structure, supplemented by share repurchases when appropriate.

Our current expectation is that our payout ratio will trend upward from its current level, with a payout ratio of approximately 45 percent being the anticipated target for 2012. As you know, our liquidity needs can fluctuate quickly based on fuel prices and other factors and we are continuing to make investments in new electric plants and other assets, in order to reliably server our customers. In light of these factors, we expect it will be a number of years before we achieve a dividend payout equivalent to the industry average. This concludes our third quarter 2011 earnings presentation and I will now hand the call back over to Steve to open up the call for questions.

Steve Busser: Thank you, David. Matt, at this time, we normally take questions.

Operator: Thank you, sir; for our phone audience, if you'd like to signal at this time please press the star or asterisk key followed by the digit one. Again, it is star one and please be sure that your mute function is off to allow that signal to reach our equipment. Again, that's star one.

We'll go first to Brian Russo with Ladenburg Thalmann.

Brian Russo: Hi, good morning.

Steve Busser: Good morning, Brian.

David Carpenter: Good morning, Brian.

David Stevens: Good morning, Brian.

Brian Russo: Just real quickly on the dividend payout target. It looks like your annualized dividend is $0.88 now and if we just assume, say, 2012 earnings are flat over 2011 on the low end that would imply a roughly 22 percent increase in the dividend in 2012 versus 2011 and is that how you get up to the 40 percent to 45 percent mark. Is that an accurate line of thinking?

David Stevens: Brian, this is David Stevens I think the line of thinking is appropriate. I would tell you that, you know obviously we haven't issued earnings guidance for 2012 and the other thing we're trying to signal is that we're going to move towards the 45 percent and as you're aware you know today if you look at our payout we're probably in the 35 percent range right now in light of what earnings are this year and if you annualize the dividend.

So what I would tell you is that the Board has not set the payout ratio firmly, but the Board has made a commitment that we are going to primarily utilize dividends to balance our capital structure as we move forward and only use share repurchases as needed and as opportunistically as we can. So I don't think your thought range is inappropriate, I don't think that we have signaled nor do I want to leave the message that we've signaled we're going to do that immediately or it's quite at that level. I won't know until we get to the first quarter.

Brian Russo: Right and when does the Board review the dividend? Each quarter or I know you initiated the dividend last year I think in March. Is that kind of the timing, maybe late first quarter or early second quarter is when we could expect a dividend increase?

David Stevens: I would say that we review it every quarter and we clearly go through it every quarter with the Board before we ever initiate or pay any dividend as to verifying liquidity, whether we still believe it's in the appropriate space. However, my expectation is we will try to get more on an annualized basis come next year and my suggestion right now is that we would probably look at the dividend before the first quarter dividend is paid out and make discussions at least about it then.

It could be that we wait for a year, so I don't want to commit to that, but I do expect that we will have the discussion because we have it every quarter before we pay it.

Brian Russo: Okay and it seems like you aggressively bought back stock in the third quarter. I would imagine, just based on your comments that you'll complete the 600,000 shares that are remaining and then focus on the dividend and so you'd need a Board authorization for a new buy-back, is that accurate?

David Stevens: That would be correct. Once we get close to the purchase of the balance of the shares we would more than likely go back to the Board and request a reauthorization of a certain amount of shares. But to your point, I think what we're expecting that we will continue to move more towards the dividend using it for balancing capital purposes and less share repurchases, but we would request an authorization from the Board, even though that has not been approved at this point we still do have to your point 674,000 shares give or take shares outstanding under our current authorization.

Brian Russo: Could you tell us what the quarter end total shares outstanding are?

David Carpenter: Yes.

David Stevens: We're going to look that up for you, Brian

David Carpenter: Yes, it was approximately 40,249,000 shares.

Brian Russo: Forty million two hundred and forty-nine thousand?

David Carpenter: Yes.

Brian Russo: Okay, great. And then can you just in terms of the 2011 updated guidance walk through some of the one-time or non-recurring gains and losses embedded in that? If you could quantify the weather impact as well.

David Carpenter: Brian, are you asking on an annual basis or on a quarterly basis?

Brian Russo: The 2011 guidance.

David Carpenter: Are you talking about the one-time items on an annual or for the fourth quarter?

Brian Russo: Annual.

David Carpenter: Annual, okay.

Brian Russo: Meaning there was a $0.07 gain in the third quarter, but what other gains and losses did you incur throughout the year that's embedded in that guidance?

David Carpenter: You know obviously one of the items that we had it's not really affecting guidance, but you had the one-time expense in 2010 for the Medicare Part D, so that doesn't really come into play, and I did want to point that out.

You had the $4.7 million of TEP income that we had in the third quarter on an ongoing basis and we expect to receive about $1.1 million per year for providing ongoing transmission both includes money for a new facility that just went into service, Macho Springs Wind Farm, then they're selling the power to Tucson and we're providing, part of the agreement was to provide transmission for that facility too.

Then you also had the weather that, on a normalized basis our estimate is around $10 million of pre-tax revenue was the impact of weather year-to-date and so we would certainly expect that our guidance in 2012 will reflect normalized weather and that will have an impact when you look at guidance in 2012.

Other than that I'm trying to see if you had the impact of the life extension at Palo Verde, which lowered depreciation expense, but then on the other hand you had the impact of the depreciation on Newman 5 both of those kind of went into effect in the second quarter of this year and the impact on 2012 will be pretty minimal they tend to balance out. And so other than that, it will just be normal changes in O&M and those types of things. I don’t think there’s anything real significant. Do you see anything else, Steve?

Steve Busser: I think you covered it, David.

Brian Russo: Another question if I could. Could you give us what the updated rate base or net plant is in your New Mexico jurisdiction, maybe as of the June 30, 2011 kind of test year to coincide with what you presented to the City Council last week?

David Carpenter: Yes. I can tell you kind of what we estimated Texas as it’s going to be on a different basis than New Mexico.

Steven Busser: Brian, are you asking for Texas because you talked about that at City Council in El Paso, correct?

Brian Russo: No, I just wanted to add up what you presented in Texas with what you know, is in an accurate kind of up-to-date New Mexico rate base

David Carpenter: Right. In Texas we presented about a million two and on a total company basis you remember that in New Mexico you don't have Palo Verde 3 in the rate base so I think it would probably be between $400 and $500 million, say $450 million.

Brian Russo: Okay, great, thank you.

Steve Busser: Thanks, Brian.

Operator: We go next to Anthony Crowdell with Jefferies.

Anthony Crowdell: Good morning. I want to follow up on Brian's question, I guess with the slide you presented to the city council, one of them you showed an adjusted return on equity (ROE) of 9.92 percent. What was the equity ratio involved in that calculation?

David Carpenter: Yes it was about a 53 percent equity ratio in that calculation, but you should also remember Anthony, that that was just taking a few major selected items and making adjustments.

When we go into the rate case we will only reflect Newman 5 in rate base, but all of the other plants that we've constructed will also have adjustments to expenses that weren't reflected in that calculation, and so we calculated a 9, slightly over 9 percent in our earnings monitoring report. And I think that's probably a little bit closer number and I think in the presentation we showed about $18.4 million rate increase and that's probably on the low side because it really had very minimal adjustments for changes in expenses and so I don't want you to think those are final numbers they're very preliminary numbers and we tried to use very conservative assumptions in putting those together.

Anthony Crowdell: Okay, so I guess just to summarize what you said when the numbers that you presented at the City Council and the rate base you used there does not include Newman 5 in service or the additional plant that you've added since that last rate filing.

David Carpenter: It did reflect Newman 5.

Anthony Crowdell: Okay.

David Carpenter: It didn't reflect other plant additions. It was just reconciliation between GAAP earnings and what you would be looking at on a Texas basis and really the more accurate calculation is to go to the earnings monitoring report that we filed with PUCT.

Anthony Crowdell: Great, thank you for your help.

Operator: And we go next to Ashar Khan with Visium.

Ashar Khan: So could I just go back to the dividend if I heard correctly your objective is to be at a 45 percent payout next year and then if I'm right, utilities are more like a 60 to 65 percent payout and the objective is to reach the industry average over the next 3 or 4 years. Am I reading that correctly?

David Stevens: No, I think you'd be reading too much into that, first off the 45 percent is what we're saying we are going to move to that from our current 35 percent and the Board hadn't said it, but we will be doing the calculations and presenting to the Board what dividend level we need to be at and we'll then announce that to everybody. But we're giving you an indication that it's going to be moving toward that range for 2012 in order for us to utilize, primarily dividends to maintain the capital structure.

The other thing we said was that it would be a number of years, we weren't implying 2 to 3 or anything like that we're implying longer than that because of that fact that we have the 1,100 megawatts or 1.1 giga-watts of power we have to install over the next 9 years.

We're going to have significant capital programs going forward and so we're going to have to balance our liquidity need with our dividend strategy and with our capital structure balancing and so I would tell you that, right now we don't really have a projected timeframe. What we're trying to send as a direction to the market is that we can't tell you right now when we will get to the industry average, but it's going to be a number of years out, is what we're trying to explain.

Ashar Khan: Okay. Then could you just go over what should we expect at the next council meeting? You kind of mentioned what could be the three outcomes on the council meetings could you just go over that?

David Stevens: Sure, I think right now the expectation is at least it was laid out by the City Council's outside regulatory attorney that he expects to come back and make a presentation either he or his consultant to the city council that will in effect take the presentation that Mr. Carpenter made on October 25 and they will make statements and/or judgments based upon their review of the same information that we presented on October 25, 2011. Then the council will make a decision at that meeting or they could postpone that decision, we don't know, but they will make a decision on temporary rates.

And what we we're saying is we have asked them and we believe temporary rates are not justifiable, nor appropriate. They could go with what the City Council's outside regulatory attorney has recommended which is to continue our current rates as temporary rates and, in effect, what that says is if the outcome of the ultimate rate case of the PUCT is an increase, then we get to back bill plus interest all the way back to the dates that they set. Or if it's a decrease then we would have to refund plus interest back to this date. Or the third option is they could actually vote to decrease our rates on a temporary basis.

We unfortunately don't know any more than that at this point in time and it's totally subject to the City Council's actions and then we'll have to react accordingly depending upon what they do.

Ashar Khan: Okay and can I ask you, what is the interest rate that is usually computed in these proceedings?

David Carpenter: I don't remember the exact interest rates, but it's very low, less than 4 percent now. There are two interest rates they use and it's between 1 percent and 4 percent, but it's very low.

Ashar Khan: Okay, so wouldn't it be rational for the City Council to leave them temporary rather than if they were to lose the case and then have to give you interest payments from the City Council or consumers to the company. Wouldn't that be the more rational outcome?

David Stevens: I guess the way I would word it is that, if you take the position that there's a City Council member, and you took the position that you had to balance the risk of having to your point pay interest plus get the surcharge bills and by the way, there's an expense to doing temporary rates because we have to go back and reprogram our customer system and it's a fairly significant expense if you have to go backwards with it and so by virtue of that, you would argue that it probably makes more sense to keep them where they are saying that, I don't know that that will occur. And then secondly the other point that I think is critical, that people understand is that, ultimately the PUCT has final authority over all of these matters and if the PUCT throws out temporary rates, for example even if they were set, then that could potentially negate those, so this is really kind of a first step in a process depending upon what they do.

Ashar Khan: Okay. When is the PUCT expected to vote, you know, on your petitions?

David Stevens: There is no statutory requirement for them to vote. The only thing that they have set to date has been an order which requires the staff to issue certain information, timelines, some recommendations on November 8 and then for the city to respond to our appeal by November 17, 2011. But the PUCT on an appeal like this to my knowledge does not have a statutory obligation to hear it and therefore, they'll do it based upon when they feel they have adequate and appropriate information.

Ashar Khan: Okay, I appreciate it. Thank you.

Operator: We go next to Michael Lapides with Goldman Sachs.

Neil Mehta: It's Neil Mehta.

Steve Busser: Hi Neil.

David Carpenter: Hello Neil.

David Stevens: Hi Neil.

Neil Mehta: So how are you thinking about the decision to go with the dividend over the share repurchases? Can you walk us through that are you taking a view on importance of liquidity or taking advantage of the low ten-year yield environment? What's driving the decision?

David Stevens: Neil we went through as you noted to just reinstitute the dividend we went through a variety of reviews not to mention the fact that we had to look at what the market looks at relative to a dividend versus a share repurchase. And as you're well aware and I believe we heard from a lot of the analysts and our shareholders on this, was that the predictability of a dividend was valued higher than a share repurchase program that may not be as predictable and by virtue of that, when you look at that, the fact that we believe that we need to obviously maintain the capital structure in light of the fact that we're making significant investments and will likely be in for more rate cases over time. Our view was, let's go ahead and balance the capital structure utilizing the methodology that the market actually appreciates the most and to our knowledge at least that would be one of the major factors, not to mention we would've looked at all of the others as well.

Neil Mehta: Got it and as of the last quarter, where's the regulatory cap structure versus what's been authorized?

David Carpenter: Yes, I think the regulatory cap structure is about 52 percent at the end of the last quarter. Within a percent or so, but I believe its right at 52 percent.

Neil Mehta: 100 to 200 basis points

David Carpenter: Still a little higher than our target.

David Stevens: Correct and Neil so you'll know the PUCT doesn't necessarily in our last case it was black box settlement there could've been imputed, people could have imputed certain cap structures, but we would say that the most logical scenario for us to be at is approximately 50/50.

Neil Mehta: And if you do go ahead with the rate case, are you going to likely file with the second quarter rate base in mind or third quarter rate base?

David Carpenter: Yes, our thought is that we would use the third quarter rate base. We made some pretty significant capital additions in the third quarter so we just think it makes more sense to use as current a numbers as possible.

Neil Mehta: And when the City Council makes its decision on interim and temporary rates, will they be premising that on second quarter results or third quarter results?

David Stevens: You know, Neil, unfortunately we have no idea. At this point in time, there have been no results that the City Council has utilized anything, I'm being direct, I mean, there's really been no information that we're aware of it doesn't mean that they haven't discussed it in executive sessions. However, to our knowledge, the City Council, the only information they've seen that we're aware of is that information that Mr. Carpenter presented at the last hearing which shows that we are not over-earning and that neither the show cause nor the temporary rates make any sense.

Neil Mehta: All right, well, thank you very much, guys, always a pleasure.

David Stevens: Thank you.

Operator: As a quick reminder, it is star 1 to signal for questions. We go next to Michael Klein with Sidoti & Company.

Michael Klein: Hey, guys.

Steve Busser: Morning Michael.

David Carpenter: Morning.

David Stevens: Morning.

Michael Klein: Just to follow up on that last question for a second, what exactly was included in the spend that you're looking to get included in the increase rates? I believe it was $260 million you said?

David Carpenter: Right, that was through June and that included about $160 million of that was for our Newman 5 phase II, which went into service in April, at the end of April.

And then we've also had a significant amount of expenditures for transmission and distribution plant, and that, to a lesser extent, you know, just your normal purchases for general plant would be (fleet) and things like that, but primarily it's the T&D plant and the generation additions.

Michael Klein: Sure, and its $260 million, thereabout?

David Carpenter: That was through June and then we would've spent and added probably another $30 million net in September.

Michael Klein: Okay and is there anything that you could pull forward to include in, I guess, this rate case if you go forward with that or is that not allowed in Texas because you can't have a over-test year?

David Carpenter: Right, you can make certain pro forma adjustments although we may, because this a little bit different proceeding, we may seek to try to bring some plant in.

Generally, you're limited on bringing plant in Texas to the extent it has to be 10 percent of your rate base, but we will make a number of other adjustments to things like expenses. For example, we just had our union contract just provided for a 3 percent pay increase to union employees, and so we'll reflect the full and annualized amount for that. And there are a number of things like that that we'll be reflecting, kind of, the latest data. It's more on the expense side than on the plant side.

Michael Klein: Okay, and do you have any more clarity around the level of O&M at Palo Verde as we move forward. I remember on the last call you said that it was, kind of, a clouded view whether or not there was the increased regulation or oversight of the nuclear plants in the U.S.

David Stevens: Mike, this is David Stevens. Based on my discussions with them and we've got another meeting coming up in this quarter, but based on my last discussions I think their belief is they'll continue to be able to decrease O&M expenses. However, it's going to be on a slightly less aggressive of a decrease I guess, if you can use that word, then what we had expected about a year and half ago or a year ago and therefore, the last I've been told is that, even with the additional regulation and things, unless something changes dramatically, their belief was they could still decrease expenses, but it may not be quite as fast as what we originally anticipated. Other than that, unfortunately, I don't have much more color.

Michael Klein: Sure, okay, and lastly, I missed the part in the prepared comments on debt. Did you say that you're going to possibly raise debt next year? Is that correct?

David Carpenter: Yes, we expect, probably in the second half of the year, that we would likely go out and replace any borrowings under our revolving credit facility with a longer term debt issuance and you know we'll take a look at the market when timing might be right. But we probably won't really have a significant need until the second half of the year and so we, our goal is to, on a periodic basis, bring our revolving credit facility back down to zero except for the borrowings for nuclear fuel.

Michael Klein: Sure, okay, that's all. Great, thanks, guys.

David Carpenter: You're welcome, thank you.

Operator: And that's star one to signal. We go next to Scott Carroll with Goldman Sachs.

Scott Carroll: Hi, Goldman Sachs Asset Management. Thanks for taking my call. David, I think, mentioned earlier some of the monetary costs associated with potentially adjusting rates, such as, I guess, reprogramming cost and, you know, the interest expense, but is anyone on the council or anywhere else thinking about the non-monetary costs associated with pursuing, you know, this action so quickly after, you know, a rate case was filed?

I guess I noted that, 1,100 new megawatts of generation have to be invested in over the next 10 years and since all of this has happened I think El Paso's one of the most highly shorted small cap utility stocks out there right now. So it seems like given the amount of investment and you know the level of concern demonstrated by the market, I'm just wondering how people are thinking about non-monetary costs of the uncertainty that's been put into the story now.

David Stevens: Scott, this is David Stevens. It's a great question. I would tell you that we are to the extent allowed we are educating everybody that is in a legislative or regulatory position associated with that. The fact that there are a lot of, if you will non-monetary costs and some of those actually translate into direct costs also because regulatory uncertainty creates additional risk. Additional risk creates a higher needed premium on return of equity. It also puts the Company at least the risk related to the debt cost and the associated ratings, et cetera and that's why we're trying to maintain this the best we can in a reasonable basis, but saying that we feel that, at this point in time, based upon a lot of the rhetoric that has occurred in El Paso, that, unfortunately, our view is we will likely have to be at the PUCT in Austin, ultimately on the decision on this for it to come out and for all of those things to be considered to your point. And I do know that, at least historically, I do not want to speak for anybody that's in one of those positions, but at least historically the PUCT put a premium on what I call regulatory certainty and this is obviously not regulatory certainty, so to the extent that they continue down that path, I'm hopeful that they will take into account all of those factors that you just mentioned.

Scott Carroll: All right, well thanks, because I think the PUCT has always been pretty rational and I mean, capital can flow across many states and you know, we can invest in a lot of different utilities and you know, we put a premium on the regulatory certainty and I hope this all gets resolved soon.

David Stevens: Thank you, Scott, I appreciate that, we agree.

Operator: Next we'll take a follow up from Anthony Crowdell with Jefferies.

Anthony Crowdell: Hey, just a quick follow up. I'm referring again to the slides at the council meeting and the one I think on page 21 where you gave an ROE of 9.92 percent. When I use that 53 percent equity ratio I come up with a net plant that's slightly different than on page 44.

Is that an apples-to-apples comparison? When I do the $81.1 million net income in at 9.92 percent return and 53 percent equity. The rate base I get there, do I compare that to the rate base on page 44?

David Stevens: Anthony, the simple answer is no. I'm going to let David answer, this is David Stevens, I'm going to let Carpenter answer this more directly, but let me kind of explain that 9.9 percent slide that you’re referring to. Where that slide came from, and we need to explain this to everybody, is that slide came from a very early request in August before the city council made any actual public announcements or anything, and they asked us to provide to them a back of the envelope, if you will, or a quick calculation as to where we though our return was, and so this is a very cursory, quick return. The reason that slide was put in the presentation is because it was a slide that we presented to the outside council, the city of El Paso, on August 16, well in advance of any hearings or anything else that occurred, and so we didn’t want to have apples and oranges from that standpoint. I think the challenge that, right now, is utilizing that slide is difficult because of the way it was presented, and for the purpose it was presented, was not meant nor is it indented still to be any kind of true regulatory filing, if you will, and then, David, if you want to clarify.

David Carpenter: Yes. David did a good job there. Anthony, just to put it basically, we were trying to show two things there, one, they were using the GAAP earnings and saying that the GAAP earnings justified a rate decrease. And what we were trying to point out to them was that a very cursory and simple reconciliation of GAAP earnings showed when you make Texas jurisdictional adjustments it does not show that at all. And then the follow-up information was okay, let's go into a little bit more detail and actually do a Texas jurisdictional calculation of what we think we could ask for in a rate case, and that's why the two really aren't comparable.

Anthony Crowdell: Okay, great and just, hopefully, a last quick one. Do you know if Occupy El Paso is scheduled for the agenda on November 15?

David Stevens: Because you would like to watch that for a long time before they get to us or...

Anthony Crowdell: Yes, I was there five hours, I was just curious if you knew if they were on the agenda?

David Stevens: I have no idea, but we will - the agenda will be posted on the Thursday prior, so you can look at it and see. I have no idea.

Anthony Crowdell: Great, thank you.

David Stevens: Thank you, Anthony.

Operator: Gentlemen, we have no other questions at this time. I'd like to turn the call back to you for any additional or closing comments.

David Stevens: Again, this is David Stevens, we sure appreciate everybody's time and great questions today and we will keep you up to date as we move forward and we look forward to having a good fourth quarter and obviously a good 2012. And thanks for following us and being with us today. Thank you.

David Carpenter: Thanks.

Operator: And, again, that does conclude today's call. Thank you for your participation. Have a good day.

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