215 South Cascade Street
PO Box 496
Fergus Falls, Minnesota 56538-0496
218 739-8200
www.otpco.com (web site)

September 25, 2013

Dr. Burl Haar
Executive Secretary
Minnesota Public Utilities Commission
121 7th Place East, Suite 350
St. Paul, MN 55101-2147

Re: In the Matter of the Petition of Otter Tail Power Company for Approval of a Transmission Cost Recovery Rider Annual Adjustment
Docket No. E017/M-13-103
REPLY COMMENTS TO DOC RESPONSE COMMENTS

Dear Dr. Haar:

Enclosed for filing in the above-referenced matter are Otter Tail Power Company's ("Otter Tail") Reply Comments to Response Comments of the Department of Commerce, Division of Energy Resources ("DOC") filed August 30, 2013.

Otter Tail has electronically filed this document with the Commission which, in compliance with Minn. Rule 7829.1300, subp. 2, also constitutes service on the Department of Commerce, Division of Energy Resources and the Office of Attorney General-Residential Utilities Division. A Certificate of Service is also enclosed.

If you have any questions regarding this filing, please contact me at 218-739-8279 or at stommerdahl@otpco.com.

Sincerely,

/S/ STUART TOMMERDAHL
Stuart Tommerdahl
Manager, Regulatory Administration

dm
Enclosures
By electronic filing
c: Service List

STATE OF MINNESOTA
BEFORE THE
MINNESOTA PUBLIC UTILITIES COMMISSION

In the Matter of the Petition of Otter Tail Power Company for Approval of a Transmission Cost Recovery Rider Annual Adjustment

Docket No. E017/M-13-303

OTTER TAIL POWER COMPANY'S REPLY TO DEPARTMENT'S RESPONSE COMMENTS

Otter Tail Power Company ("OTP") is filing this Reply to The Department of Commerce's ("Department's") Response Comments to confirm that the issues in this matter appear to be resolved except for the following three issues:

1. Whether OTP's share of costs incurred to construct the Bemidji-Grand Rapids project, but not specifically quantified in planning estimates in the project's September 8, 2007 Application for a Certificate of Need[1], should be excluded from the rate base used to derive the Transmission Cost Recovery Rider ("TCRR") rates;

2. Whether capitalized internal labor costs incurred by OTP to construct the TCRR-eligible transmission projects should be excluded from the rate base used to derive TCRR rates;

3. If the answer to issue1 and/or 2 is yes, whether it would be appropriate to require that all of the revenues from OTP's investment in these transmission facilities should be included in the TCRR rate calculations, even the revenues that are attributable to the capital costs disallowed (per issue 1 and/or 2).

OTP has addressed issues 1 and 2 in its Original Reply Comments filed on June 27, 2013. OTP believes those Reply Comments explain its position on issues 1 and 2 and demonstrate that the costs should not be excluded from the rate base used to derive the TCRR rates.

Issue 3 was identified as a matter of dispute when the Department filed its August 30, 2013 Response Comments, in which it recommended "that the Commission require OTP to pass

[1] Docket No. E-017, E-015, ET-6/CN-07-1222.

through all MISO Schedule 26 revenues associated with the projects included in the TCRR that it receives from other utilities, including those revenues that are attributable to the Company's disallowed capital costs" (emphasis added). OTP addresses that issue in these Reply Comments.

OTP Response on Issue 3--It would not be appropriate to *include,* as a revenue credit to the Rider rate calculations, MISO revenues which are based on the full cost of construction, while at the same time *excluding* from the Rider rate calculations the costs of construction which are the basis for the revenues generated.

The Department's recommendation on issue 3 is for the Commission to create a mismatch between the rate base used to derive the revenue requirement for the TCRR and the rate base used to derive the revenue credits applied to the TCRR. The Department's recommendation to use two different rate bases in this way would be arbitrary and would violate fundamental regulatory and accounting principles. Accepting such a determination would result in substantial harm to OTP and it would serve as a serious disincentive for making such investments even though they are very beneficial to OTP's ratepayers.

A. The Department's recommendation to exclude some costs of constructing these projects but to include all revenues (even those derived from the excluded costs) would create an internal contradiction in the calculation of the TCRR rate.

The Department says in its Response Comments that it is "not appropriate to mix up federal and state rate making principles," but their recommendation does just that—it accepts a rate base at the full costs of construction for the revenue credits (based on the rate base used in the FERC-approved MISO tariff mechanism), but then it reduces the rate base for purposes of establishing the cost to be recovered (based on the Department's positions with respect to state recovery). To accept such a ruling, the Commission would have to make a ruling that:

1. Accepts the full costs of construction for purposes of the revenue crediting for the TCRR, but
2. Accepts something less than the full costs of construction for purposes of establishing the TCRR revenue requirement to which that revenue credit is applied.

Creating such an internal contradiction in the calculations for the TCRR rates would be arbitrary, and made only to create a false arbitrage between the revenue requirements and the credits.

B. OTP would be substantially harmed by the Department's recommendation.

The Department goes on to say that OTP will not be harmed by its recommendation. That is simply not accurate. A calculation of the harm is provided below (see Table 1 and the analysis that follows)—and that analysis shows that if the Department's recommendation were accepted, OTP would recover less than 25 percent of what an outside entity, such as an independent transmission company, would recover for these investments.

The Department's Response Comments include an incorrect statement that reflects the principle that a harm occurs (either for ratepayers or for shareholders) when an arbitrary mismatch is created between the costs of the investment and the revenues derived from the investment. The Department's Response Comments incorrectly say:

> "However, OTP's ratepayers would be harmed if OTP's shareholders were allowed to retain a portion of the revenues that the Company would not be receiving but for investments in infrastructure used to provide service to ratepayers."

The Department's statement would only make sense if OTP were asking to create a mismatch (i.e. to include all the costs of the investments, but less than all of the revenues); but that's not what OTP is requesting. OTP is asking that the investment upon which the revenue credits are based is the same investment upon which the cost recovery is based. In other words, if ratepayers are paying for all of the investments they should be credited with all of the revenues derived from the investments; if they are paying for some portion of the investments, they should be credited with a corresponding portion of the revenues derived from the investments. As the mistaken statement in the Department's Response Comments illustrates, it is the Department's recommendation, not OTP's, that recommends such an arbitrary mismatch.

The Department Comments also characterize the TCRR mechanism and the transmission investments in a way that ignores the substantial benefit conferred on OTP's ratepayers by OTP making investments in these projects and including them in the TCRR. The statute authorizing TCRRs was enacted for the purpose of incentivizing investments in such projects. The Department even suggests that by requesting that all costs be included in the Rider (or a proportional amount of revenues be excluded along with any excluded costs) OTP has a "reluctance to be held financially responsible." That is simply not true. OTP has remained consistent to the Commission's Order from the last TCRR proceeding (including and matching all costs with all revenues) and has reflected the corresponding impact (reduced costs = corresponding reduction in revenue credits should certain costs be disallowed from the Rider), following standard ratemaking principles. OTP's financial responsibility and the significant benefit conferred on OTP ratepayers by OTP's transmission investment is demonstrated in Table 1 of its June 27, 2013 Comments in this proceeding, which is repeated below.

Table 1

(Repeated from OTP's Reply Comments)

	Bemidji–Grand Rapids Project Revenue Requirements 2013	
	With OTP Investment	**No OTP Investment**
Schedule 26 Expense[2]	1,228,463	1,228,463
MN Revenue Requirements[3]	1,447,707	0
Schedule 26 Revenue[4]	(1,879,798)	0
Total	796,372	1,228,463

The information in Table 1 shows that by OTP investing in the Bemidji-Grand Rapids Project (including all costs and revenues), OTP has saved its ratepayers significantly—OTP's ratepayers will pay approximately one-third less for that project in 2013 than they would have if OTP had not invested in it.[5] And it should be remembered that these investments have also been

[2] Minnesota's share of MISO's allocation of costs to OTP for Bemidji-Grand Rapids based on OTP's retail load requirements.

[3] The Minnesota revenue requirement for Bemidji-Grand Rapids is based on OTP's total investment in the project.

[4] Minnesota's share of MISO's allocation of revenues to OTP for Bemidji-Grand Rapids is based upon OTP's total investment in the project.

[5] The Department's claim that there has been no regulatory constraint on the costs OTP has incurred for Bemidji-Grand Rapids is also not accurate. The MISO tariff includes FERC-approved provisions for review and disallowance of costs that cannot be demonstrated as prudently incurred—therefore there are federally authorized mechanisms that provide such oversight. And, it appears that the Minnesota Commission has also approved full recovery of Bemidji-Grand Rapids costs for Xcel Energy--OTP could not identify any costs for the Bemidji-Grand Rapids project that were disallowed for Xcel in its recently concluded rate case. OTP and Xcel and other utilities constructed the Bemidji-Grand Rapids project jointly and each pays its proportional share of project costs. Therefore, to the extent the Department is requesting disallowance of Bemidji-Grand Rapids project costs, it is

recognized as beneficial for reliability and market performance. Because of these benefits, the Minnesota TCRR legislation and the federal mechanisms were established to incentivize utility investments in these projects. The Department's recommendations would result in a significant disincentive from OTP making such investments as it would not allow OTP to recover its revenue requirements for the projects, even while they are generating such substantial benefits for OTP ratepayers.

Another way to look at the information included in Table 1 is to consider whether the Commission would prefer to have local utilities or outside transmission investment entities making these investments. If an outside transmission investment entity had invested in the Bemidji-Grand Rapids project instead of OTP, OTP's customers would have paid $1,228,463 and the outside entity would have recovered $1,228,463 as its revenue requirement on the project. In contrast, as OTP has proposed to recover costs through its TCRR in this proceeding, OTP's customers will pay and OTP will recover $796,372. This is because of the crediting of the revenues associated with OTP's investment in the project. The Department's proposal to create a mismatch between the rate base used for recovery (approximately 65% of total investment) and the rate base used for revenue credits (100% of total investment) would reduce OTP's recovery by an estimated $505,000 to $291,000 [6] (as compared to the $1,228,463 that would be recovered by an outside transmission entity). <u>There is no rational basis that would justify OTP recovering less than 25 percent of what an outside entity would recover for this investment</u>. While OTP believes that there are significant benefits that can be conferred on Minnesota retail ratepayers when local utilities invest in these projects (such as the substantial reduction in rates reflected in Table 1, above), the Department's recommendation in this matter goes too far. Creating such a large disadvantage for a local utility would serve as a strong disincentive weighing against local utilities making investments in these kinds of projects. This would not be in the public interest or in the interest of OTP's ratepayers.

doing so on procedural grounds and not based on any reasonable substantive concern that the costs of that project were not prudently incurred.

[6] This reduction takes into consideration the Department's position with respect to capping recovery at the CON cost estimate amount, as adjusted for inflation, of $74 million, as stated in their Response Comments, (Issue 1).

C. The beneficial effect of increasing the rate base (and thus increasing the revenues) for the TCRR rate calculation was recognized in last year's TCRR proceeding, in which the Commission made the determination that the "All-in" method should be used for OTP's investments in regional transmission projects. To now reduce the rate base (but not the revenues) would be a significant contradiction of that prior ruling.

Creating such a mismatch as the Department has recommended would ignore the decision made by the Commission in OTP's last annual TCRR rate proceeding. In that proceeding, the Commission Ordered that OTP's TCRR will use the "all-in" method for projects with a regional cost allocation (and specifically for the Bemidji-Grand Rapids and Fargo-Monticello projects). The Commission explained how its decision should be applied by stating, "All Minnesota-jurisdictional costs [of the Bemidji-Grand Rapids and Fargo-Monticello lines] will be included in the rider and all revenues attributable to the Minnesota-jurisdictional portions of the lines will be credited to ratepayers."[7] The effect of this ruling was to increase the amount of the investment included in the TCRR rate base over the costs allocated to OTP based on its retail load-serving obligations; an outcome that would typically have been opposed by the Department and not likely approved by the Commission (because typically increasing rate base increases rates to customers). But in the instance of these regional projects that generate MISO revenues, the Commission agreed that OTP's rate base should include all of the costs incurred for these investments--not just the portion associated with retail service--because doing so increases the corresponding revenues derived from that larger investment. For the Department to now propose to disallow certain costs (to decrease the investment included in the rate base) but to continue to include all revenues is a recommendation for a reversal of that "all-in" determination—but a reversal on only half of the "all-in" equation. For all the reasons explained above, the Department's recommendation should not be accepted. Instead, OTP should be authorized to continue calculating its TCRR rate for eligible projects as the Commission articulated in the last TCRR rate proceeding:

All Minnesota-jurisdictional costs of eligible projects should be included in the rider and all revenues attributable to the Minnesota-jurisdictional portions of the lines should be credited to ratepayers.[8]

[7] Commission Order (March 26, 2012) in Docket E-017/M-10-1061, Page 5, B. Commission Action, Paragraph 1 (emphasis added).
[8] *Id*.

CONCLUSION

For these reasons, OTP requests that its TCRR rate be calculated reflecting all costs incurred for its TCRR eligible transmission projects and all revenues derived from those project investments. Alternatively, if the Commission determines that certain costs should be excluded from the TCRR rate base, then the revenues that are derived from that disallowed investment should similarly be excluded.

Dated: September 25, 2013

Respectfully Submitted,

OTTER TAIL POWER COMPANY

By: */s/ STUART TOMMERDAHL*
Stuart Tommerdahl
Manager, Regulatory Administration
Otter Tail Power Company
215 S. Cascade Street
Fergus Falls, MN 56537
(218) 739-8279
stommerdahl@otpco.com

OTTER TAIL POWER COMPANY

By: */s/ BRUCE GERHARDSON*
Bruce Gerhardson
Associate General Counsel
Otter Tail Power Company
215 S. Cascade Street
Fergus Falls, MN 56537
(218) 739-8475
bgerhardson@otpco.com

CERTIFICATE OF SERVICE

Re: **In the Matter of the Petition of Otter Tail Power Company for Approval of a Transmission Cost Recovery Rider Annual Adjustment**
Docket No. E017/M-13-103

I, Diane Merz, hereby certify that I have this day served a copy of the following on Dr. Burl W. Haar and Sharon Ferguson by e-filing, and to all other persons on the attached official service list by electronic service or by first class mail.

Otter Tail Power Company
Reply Comments to DOC Response Comments

Dated this **25th** day of **September 2013**.

/s/ DIANE MERZ

Diane Merz
Regulatory Filing Coordinator
Otter Tail Power Company
215 South Cascade Street
Fergus Falls MN 56537
(218) 739-8608

First Name	Last Name	Email	Company Name	Address	Delivery Method	View Trade Secret	Service List Name
Julia	Anderson	Julia.Anderson@ag.state.mn.us	Office of the Attorney General-DOC	1800 BRM Tower 445 Minnesota St St. Paul, MN 551012134	Electronic Service	Yes	OFF_SL_13-103_13-103
Christopher	Anderson	canderson@allete.com	Minnesota Power	30 W Superior St Duluth, MN 558022191	Electronic Service	No	OFF_SL_13-103_13-103
Michael	Bradley	bradleym@moss-barnett.com	Moss & Barnett	4800 Wells Fargo Ctr 90 S 7th St Minneapolis, MN 55402-4129	Electronic Service	No	OFF_SL_13-103_13-103
Gary	Chesnut	gchesnut@agp.com	AG Processing Inc. a cooperative	12700 West Dodge Road PO Box 2047 Omaha, NE 681032047	Electronic Service	No	OFF_SL_13-103_13-103
James C.	Erickson	jericksonkbc@gmail.com	Kelly Bay Consulting	17 Quechee St Superior, WI 54880-4421	Electronic Service	No	OFF_SL_13-103_13-103
Sharon	Ferguson	sharon.ferguson@state.mn.us	Department of Commerce	85 7th Place E Ste 500 Saint Paul, MN 551012198	Electronic Service	No	OFF_SL_13-103_13-103
Bruce	Gerhardson	bgerhardson@otpco.com	Otter Tail Power Company	PO Box 496 215 S Cascade St Fergus Falls, MN 565380496	Electronic Service	No	OFF_SL_13-103_13-103
Burl W.	Haar	burl.haar@state.mn.us	Public Utilities Commission	Suite 350 121 7th Place East St. Paul, MN 551012147	Electronic Service	Yes	OFF_SL_13-103_13-103
Shane	Henriksen	shane.henriksen@enbridge.com	Enbridge Energy Company, Inc.	1409 Hammond Ave FL 2 Superior, WI 54880	Electronic Service	No	OFF_SL_13-103_13-103
James D.	Larson	james.larson@avantenergy.com	Avant Energy Services	220 S 6th St Ste 1300 Minneapolis, MN 55402	Electronic Service	No	OFF_SL_13-103_13-103
Douglas	Larson	dlarson@dakotaelectric.com	Dakota Electric Association	4300 220th St W Farmington, MN 55024	Electronic Service	No	OFF_SL_13-103_13-103

First Name	Last Name	Email	Company Name	Address	Delivery Method	View Trade Secret	Service List Name
John	Lindell	agorud.ecf@ag.state.mn.us	Office of the Attorney General-RUD	1400 BRM Tower 445 Minnesota St St. Paul, MN 551012130	Electronic Service	Yes	OFF_SL_13-103_13-103
Kavita	Maini	kmaini@wi.rr.com	KM Energy Consulting LLC	961 N Lost Woods Rd Oconomowoc, WI 53066	Electronic Service	No	OFF_SL_13-103_13-103
Andrew	Moratzka	apmoratzka@stoel.com	Stoel Rives LLP	33 South Sixth Street Suite 4200 Minneapolis, MN 55402	Electronic Service	No	OFF_SL_13-103_13-103
Larry L.	Schedin	Larry@LLSResources.com	LLS Resources, LLC	12 S 6th St Ste 1137 Minneapolis, MN 55402	Electronic Service	No	OFF_SL_13-103_13-103
Stuart	Tommerdahl	stommerdahl@otpco.com	Otter Tail Power Company	215 S Cascade St PO Box 496 Fergus Falls, MN 56537	Electronic Service	No	OFF_SL_13-103_13-103