

Staff Briefing Papers

Meeting Date October 25, 2018 Agenda Item 7**

Company Northern States Power Company d/b/a Xcel Energy (Xcel Gas)

Docket No. **G-002/M-18-184**

In the Matter of the Petition of Northern States Power Company for Approval of a Modification to its Natural Gas State Energy Policy (SEP) Tariff, 2018 SEP Rate Factor, and 2017 SEP Compliance Filing

Issues 1. Should the Commission accept Xcel Energy’s 2017 SEP compliance filing, approve the proposed 2018 SEP rate factor, and approve the Company’s proposed modification to its SEP tariff?

Staff	Ray Hetherington	raymond.hetherington@state.mn.us	(651) 201-2203
	Eric Bartusch	eric.bartusch@state.mn.us	(651) 201-2259

 **Relevant Documents**

Date

PUC - Order Continuing Recovery of Costs Through the State Energy Policy Rider and Other Action (Docket No. G-002/M-17-174)	August 24, 2017
Xcel Energy – Petition and Compliance Filing	March 1, 2018
Department of Commerce (Department) – Comments	April 2, 2018
Xcel Energy – Reply Comments	May 14, 2018
Xcel Energy – Supplemental Reply Comments	May 25, 2018

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The attached materials are work papers of the Commission Staff. They are intended for use by the Public Utilities Commission and are based upon information already in the record unless noted otherwise.

 **Relevant Documents**

Date

Department – Reply Comments

July 5, 2018

Xcel Energy – Second Supplement to Reply Comments

July 16, 2018

I. Statement of the Issues

Should the Commission accept Xcel Energy's 2017 SEP compliance filing, approve the proposed 2018 SEP rate factor, and approve the Company's proposed modification to its SEP tariff?

II. Introduction

On September 26, 2003, Northern States Power Company d/b/a Xcel Energy (Xcel, Xcel Energy, Xcel Gas or the Company) filed its first request for approval of a State Energy Policy Rate Rider in Docket No. E-002, G-002/M-03-1544. Since that time, the Commission has issued determinations twelve times. In its last order, issued August 24, 2017 in Docket No. G-002/M-17-174 *Order Continuing Recovery of Costs through the State Energy Policy Rider and Other Action* (August 24, 2017 Order), the Commission authorized Xcel to continue recovering certain costs through the SEP rider and conditioned the terms under which future cost recovery should occur.

The disputed issues revolve around the Company's request for a change in handling of Accumulated Deferred Income Taxes (ADIT), based on IRS private letter rulings and, accordingly, the time periods used in computing their new rate rider factor.

In its Second Supplement to Reply Comments, dated July 16, 2018, on p. 2, Xcel stated that:

Whether ADIT is prorated using the updated methodology or proration is removed entirely, with all else equal, the actual rate charged to customers would be the same. Further, we are not suggesting that any party agree that our proposal is the only appropriate methodology. Rather, we ask that parties agree to apply our proposed methodology for the currently pending Company rider filings, with no commitment from parties regarding future treatment. That is, should parties accept our proposed treatment in this proceeding, the Company commits here to refrain from using this outcome as an argument for acceptance in future proceedings. We believe this creates a win for customers: compliance with normalization rules, protection of customers and avoidance of precedent for resolution of this issue in future proceedings.

The Department recommends the Commission deny Xcel Gas' proposed 2018 SEP rate factor. The Department believes Xcel Gas' proposed SEP adjustment factor is effectively an inappropriate request for reconsideration of the Commission's 17-174 Order and, if implemented, would violate the Commission's August 24, 2017 Order. The Department recommends the Commission accept Xcel's petition as a compliance filing, updated to reflect Xcel's lower costs for 2017 and should be based on actual 2016 sales, which results in a SEP factor of \$0.001576 per therm¹ for implementation on or after July 1, 2018.

¹ See p. 9, Department, April 19, 2018 Comments

III. Background

On March 1, 2018, Xcel submitted its request for approval of its 2018 State Energy Policy (SEP) rider rate factor, proposed customer notice, updated tariff and its 2017 annual SEP rider compliance filing. The current SEP rider is recovering two types of costs: 1) Assessment for the Department of Commerce's Regional and National Duties (ADRND), and 2) the Cast Iron Pipe Replacement Project. ADRND costs are costs due to expenses incurred by the Department of Commerce for services to the Commission on reliability issues and other projects or analyses. The Cast Iron costs are costs incurred under Minn. Stat. § 216B.1637 as Recovery of Certain Greenhouse Gas Infrastructure Costs prior to its repeal in July 2013.

Xcel discontinued use of the SEP Rider to recover electric costs. Recovery for these projects are now shifted into base rates in Xcel's multi-year electric rate plan, in docket E002/GR-15-826.

On April 2, 2018, the Department filed comments stating the Company's Petition fulfills the Commission's reporting requirements contained in orders from docket *E,G-002/M-03-1544 Order Approving State Energy Policy Rider, as Modified*; docket *E,G-002-M-08-261 Order Accepting and Modifying Petition Regarding State Energy Policy Rider*; and dockets *E,G-002/M-14-185 and E,G-002/M-17-174, Order Approving Modification of the Natural Gas State Energy Policy Tariff Rate*.

However, the Department concludes that the Company's proposed 2018 SEP adjustment factor based on future estimated sales with prorated accumulated deferred income taxes (ADIT) is in violation of the Commission's Order in docket 17-174. Because Xcel's petition does not agree with the Order, the Department recommends treating the Petition as a compliance filing and updating the proposed SEP adjustment factor so that it is based on the Company's lower, updated 2017 revenue requirement as included in this docket 18-184, while using 2016 actual sales.

On May 14, 2018, the Company filed its reply to the Department's April 2, 2018 comments stating that the only areas of disagreement with the Department are in the area of proration of ADIT and the natural gas sales period used to calculate the SEP rider rate factors. The Company stated that the ADIT treatment ordered by the Commission requires a permanent move to an historical test year and was not fully addressed in the written record of the 17-174 docket. The Company also proposed using forecasted sales as the best match in cost and recovery timeframes for calculating the rider adjustment factor.

On May 25, 2018, the Company filed supplementary comments. The Company engaged Deloitte Tax Services to evaluate their rider calculations and as a result Xcel proposed a new method that is intended to minimize ADIT proration. The new Deloitte calculation method reduces their originally proposed adjustment factor from \$0.001960 to \$0.001959 per kWh, a reduction of approximately \$0.01 per month for an average residential customer.

On July 5, 2018, the Department filed its reply to the Company's May 14th and May 25th comments refuting the new proposal as too complex and violating the requirement in the 17-174 order that Xcel exclude ADIT proration from the rider calculations. In addition, the Department states the Company materially under-estimated forecast sales and that using the

estimate as a basis for the calculation of the rider would result in an over-stated rider rate factor.

On July 16, 2018, the Company filed its Second Supplement to Reply Comments dated May 14th. The filing included Attachment A in response to the Department's request for a more granular breakdown of the ADIT proration impact on each project's revenue requirements. The Company stated that the impact on customers is de minimis and that the Company is asking for use of its proposed rate calculation for the current period only, with no commitment for use in future rate filings.

IV. Parties' Comments

A. Xcel Energy (Gas) – Initial Filing

The Company has requested for 2018 an increase to its 2016 SEP rate factor from \$0.001368 to \$0.001960 per therm. According to Xcel, an increase is warranted to allow the Company to recover a revenue requirement of approximately \$1.77 million over the 12 month period from July 2018 through June 2019 (see SEP Costs and Rate Factor table, below). As noted, the proposed rate incorporates the 2017 under-collected from customers in the 2017 period. The implementation of the proposed factor would result in an increase of about \$0.50 annually for the average natural gas residential customer using 70.33 therms per month. Currently, the average residential customer pays about \$1.15 a year for the recovery of approximately \$1.3 million in SEP costs. Under the proposed factor, the average customer would pay about \$1.65 per year.

SEP Costs and Rate Factor ²				
	2016	2017	2018	2018 vs 2016
Gas	Approved	Forecast**	Forecast	Difference
ADRND	\$31,557	\$27,030	\$31,645	\$88
Cast Iron	\$1,821,962	\$1,567,571	\$1,456,363	\$(365,599)
Cast Iron O&M Credit	\$(72,310)	\$(72,310)	\$(72,310)	\$0
Carryover	\$(466,208)	\$8,483	\$351,267	\$817,475
Revenue Requirement	\$1,315,002	\$1,530,774	\$1,766,965	\$451,963
Therm Sales*	961,310,996	N/A	901,480,683	(59,830,313)
Factor	\$0.001368	N/A	\$0.001960	\$0.000592

*The Sales Forecast information in Table 1 is annualized to provide a comparison of our projected factor and our approved factor.

** The 2017 Forecast amount includes 6 months of actuals and 6 months of forecast.

The Company proposes that if actual implementation does not happen until after July 1, 2018 the rate factor would need adjustment.

Since the cast iron project is no longer incurring costs, the Company proposes moving the remaining depreciation expenses into rate base at the filing of its next rate case. The Company notes that there have been no carbon offsets or credits associated with the cast iron replacement program. The Cast Iron O&M Credit in the table reflects the portion of cast iron pipe replaced through the 2010 test year since that amount is already accounted for in base rates.

² Page 7, Xcel Gas' Initial Filing, Docket No. 18-184.

In compliance with docket 17-174, the Company used the capital structure authorized in its 2013 electric rate case (docket E002/GR-13-868) to calculate revenue requirements. Xcel used the Return on Equity of 9.04 percent as recommended by the Department and later approved in the Commission's Order in Gas Utility Infrastructure Cost (GUIC) Rider, docket G002/M-16-891.

The Commission's August 24, 2017 Order stated that the Company shall not prorate ADIT in its SEP rider and, since the effective date of the approved rider for the 2017-2018 period would not be effective before July 1, 2018, would make proration of ADIT unnecessary because historical actuals would be used to calculate the rate. The Company is proposing to eliminate a separate rate for the 2017-2018 period, and instead move to a 2018-2019 future SEP period revenue requirement which includes proration. Xcel states that Private Letter Ruling (PLR) #201717008, page 11, specifically disallows the combination of true-up forecasted costs using proration with actuals that do not have proration because the effect would reverse the economics of proration. Xcel has visualized the effects on timing in the chart below.

Xcel's Chart 1 (modified): ADIT Proration Timing³

In Current Filing (18-184)				True-up forecast with no proration to actuals	
ADIT Actuals, No Proration		Forecast ADIT, No Proration		Forecast ADIT, Proration	
2016 SEP Period (16-206)		2017 SEP Period (17-174)		2018 SEP Period (18-184)	
7/1/2016	6/30/2017	7/1/2017	6/30/2018	7/1/2018	6/30/2019

The Company argues that this method conforms to IRS normalization requirements and removes delay from the implementation of a new rate. Xcel's initial filing, in this docket, 18-184, incorporates this new approach.

B. Department of Commerce - Comments

The Minnesota Department of Commerce, Division of Energy Resources filed comments on April 2, 2018. The Department recommended that the Commission deny Xcel Energy's proposed SEP adjustment factor.

The Department concludes that this Petition contains most of the information required by the implementation process approved by the Commission in its 2003 order (Docket No. E,G-002/M-03-1544).

In compliance with the Commission's 2017 order (Docket No. E,G-002/M-17-174), the Department notes that the Company complied with the ordering point requesting a comparison between actual and budgeted monthly costs. However, the Department points out that the Company did not comply with the ordering points requiring it to not prorate ADIT in the SEP rider and to put the 2017 SEP rider into effect no later than July 1, 2018.

³ Page 10, Xcel Gas' Initial Filing, Docket No. 18-184.

The Department disputes the Company's new proposal for handling accumulated deferred income taxes (ADIT). The Department says that:

According to the Company, PLR #201717008 states that whenever a given rate is set, the months prior to that date can be treated as actuals, without proration, regardless of whether the data was based on actual or estimated figures. The Company stated that this PLR allows Xcel Gas to exclude proration for the 2017-2018 SEP period, even for months that are forecasted (January 1, 2018 – June 30, 2018).

The Department agreed that the IRS doesn't require proration due only to the use of estimated data but, rather, based on the date of rate implementation: if the test year [or test period] occurs before the rate implementation date, then proration of ADIT is not required.

The Department argues that there are several reason why the Company's proposal is not reasonable. The Commission already set the rate for July 1, 2018 in Docket 17-174, so it is not reasonable for the Company to propose setting a rate based on a different test period to be effective on that same date. Also, the Company is proposing to credit back to ratepayers a true-up amount equal to the difference between the forecast un-prorated ADIT and actuals. The Department concludes that waiting for actual data to be available before implementing the rate, as the Commission ordered, is a "clear and reasonable resolution of the issue".

The Department notes that Xcel provided updated cost recovery data that would be "more appropriate" in setting the 2017 SEP factor in last year's SEP rider docket (17-174). The Department prepared the table below summarizing this data:

Based on 2017 Figures ⁴

Gas	18-184	17-174	Difference
RA/SBG	\$27,030	\$10,565	\$16,465
Cast Iron	\$1,567,571	\$1,754,251	(\$186,680)
Cast Iron O&M Credit	(\$72,310)	(\$72,310)	\$0
Carryover	\$8,483	\$139,726	(\$131,243)
Revenue Requirement	\$1,530,774	\$1,832,232	(\$301,458)
Xcel's Est. Therms (2018 & 2017)	901,480,683	871,444,973	30,035,710
2016 Actual Therms *	971,043,548	971,043,548	0
Factor	\$0.001576	\$0.001887	\$(0.000310)

The Department recommends that the Commission accept Xcel's petition as a compliance filing, but deny its proposed 2018 SEP rate factor, instead using the lower 18-184 revenue

⁴ Page 9, Comments of the Minnesota Department of Commerce, Division of Energy Resources, April 2, 2018.

requirement amount of \$1,530,774 and 2016 Actual Therms of 971,043,548 to set a factor of \$0.001576 per therm, effective July 1, 2018.

C. Xcel Energy – Reply to Department Comments

Xcel Gas submitted its reply to the Department's April 2nd comments on May 14, 2018. The Company stated that its proposed rate combined the 2017 tracker balance with the 2018 forecasted rate, as the Company has done in past SEP Rider petitions. The Company and the Department agree on the reasonableness of the costs being recovered in the SEP Rider. There are two issues of disagreement with the Department: 1) the proration of accumulated deferred income taxes (ADIT) and 2) the natural gas sales period used in calculating the rider rate.

The Company does not agree with the Department's assertion that the Company is seeking an improper rehearing of the 17-174 Order, contending that the Commission's Order was issued because the Company had not yet received the Private Letter Ruling that it sought from the IRS on handling ADIT. Further, the Company says that it does not "believe the Commission decided to permanently change the SEP Rider into a historical recovery mechanism".

The Company concedes that IRS ADIT Proration requirements are cumbersome, but Xcel Energy has taken steps to evaluate the topic across its companies and its various rider filings. Responding to the Department's argument that PLRs are unique to the company requesting them, the Company notes that PLRs are published publicly in order to show the IRS's view of the application of law to a specific set of facts. Finally, the Company states that tax normalization is required by the IRS in order for any company to use accelerated depreciation and that §1.167(l)(h)(6) requires proration of forecasted ADIT. The Company sees no way to avoid this.

Xcel states that it engaged Deloitte Tax Services (Deloitte) to review the Company's rider calculations and to suggest ways to optimize its approach to normalizing ADIT through proration. Deloitte suggests Xcel treat each forecast month as a separate test period. This would allow proration of each month's activity. This treatment would embed the proration calculation in the rate base calculation, but Xcel would provide a supplementary schedule to identify the revenue requirement impacts. Xcel believes this small modification to be preferable over moving to a purely historical method. The Company points out that the prorate is small, but postponing rate implementation past the test year would result in a large carryover balance to be recovered in the next rate case, thus leading to greater volatility in rates to the customers.

The Company disagrees with the Department position on using 2016 actual sales instead of Xcel's forecasted 2018 sales. The Company notes that the use of forecasted sales is well established in the rider process and that forecasted sales will be more accurate since they are the result of past actuals adjusted by the Company for its expected sales based on current plans.

D. Xcel Energy – First Supplement to Reply Comments

On May 25, 2018, Xcel Gas submitted its first supplement to its reply comments. The Company states that Deloitte, along with Xcel's tax experts identified the following 3 possible modifications to Xcel's process for handling ADIT proration:

- 1) Treat each forecast month as a test period using the revenue requirements in these riders which are calculated monthly. This allows the monthly ADIT balance to be reset to its un-prorated beginning balance and only the monthly activity receives the proration.
- 2) Then apply a mid-month convention for the proration factors in each month.
- 3) Remove ADIT from the beginning-of-month and end-of-month rate base average, since the proration is itself a form of averaging.

Incorporating these modifications to the ADIT proration changed Xcel's calculated 2018 SEP Rider adjustment factor from \$0.001960 per [therm] to \$0.001959 per [therm].⁵

E. Department of Commerce – Reply Comments

On July 5, 2018, the Department filed its reply to the Company's May 14th and May 25th reply comments.

The Department states that it appreciates Xcel Gas' efforts to minimize the harm to ratepayers from ADIT proration, but the Department still recommends the Commission deny Xcel's proposed 2018 SEP rate factor for the following reasons:

- 1) The 17-174 Order says "Xcel Gas shall not prorate its accumulated deferred income taxes in the SEP rider".
- 2) The proposed new, optimized method is "needlessly complex", particularly when the IRS has provided a simple method to avoid proration: apply the rate after the test period has become historical.
- 3) The Company "clearly stands to financially benefit from charging higher rates to ratepayers when ADIT is prorated" and the Company is not "required to prorate ADIT to preserve tax benefits".
- 4) The Company's statement that "without changing the law or regulation, the Company sees no way to avoid this circumstance" ignores the fact that the IRS provides a method without need for proration.
- 5) Xcel Gas chose not to provide actual sales data for 2017, but their annual jurisdictional report shows that the Company underestimated its 2017 natural gas

⁵ May 25, 2018 Xcel Gas Supplemental Reply Comments SEP Rider Docket No. G002/M-18-184 Page 2

sales by 6.4 percent. Although this is subject to true-up in the future, since there are no carrying charges applied to over-recovery, the Company would keep any interest earned and so, has an incentive to under-forecast sales. The Department concludes that Xcel has not demonstrated that it is reasonable for Xcel to use its sales forecast in setting rates.

- 6) Xcel is ignoring the fact that recovery under a rider is, in itself, extraordinary ratemaking, allowing recovery in advance of a rate case. So, even using historical data would result in cost recovery earlier than under a rate case.
- 7) Xcel Gas is ignoring the small benefit that ratepayers would receive as a result of this minor delay in cost recovery.

The Department believes the IRS solution which would entail waiting until the end of the test period to implement rider rates is a reasonable and accurate fix for the problems of ADIT proration.

F. Xcel Energy – Second Supplement to Reply Comments

On July 16, 2018, the Company filed its Second Supplement to its Reply Comments providing a more granular breakdown of its modified ADIT proration methodology, as requested by the Department. Additionally, the Company reaffirmed its position that the overall impact on customers is de minimis; the difference between Xcel's and the Department's proposals results in a \$5 overall revenue requirement impact.

Finally, the Company continues to request the Commission allow it to use its new ADIT proration methodology, as noted in Deloitte's recommendations, for the currently pending rate filings, with no commitment regarding future treatment. The Company will refrain from treating this outcome as an argument for acceptance in future proceedings.

V. Staff Analysis

A. Does Xcel's proposed SEP Rider filing comply with the Commission's August 24, 2017 Order?

1. Are Costs Appropriately Recovered Through the SEP Rider?

a. ADRND Assessment Costs

The 2017 legislature, under Minn. Stat. § 216B.62, subd. 3b, authorized an assessment for ADRND costs (which replaced the Reliability Administrator statute) to be extended through June 30, 2018. The Commission ordered the Company to seek cost recovery under the SEP Rider.⁶ The Company is seeking approval for 2018 forecast costs of \$31,645 (an \$88 increase over the 2016 approved costs of \$31,557).

⁶ Docket No. G-002/M-17-174 issued August 24, 2017

b. Natural Gas Iron Pipe Replacement Project

Originally, these costs were authorized for recovery by the Commission under Minn. Stat. § 216B.1637 as Recovery of Certain Greenhouse Gas Infrastructure Costs. However, after all of the costs were incurred, authorization for rider recovery was received, and the project was placed in-service, the statute was repealed in July, 2013. The costs presented here are for all costs incurred before the repeal date. Since the project is no longer incurring costs, the Company proposes moving remaining depreciation costs into base rates in its next rate case. The total Minnesota revenue requirement associated with these costs are forecast at \$1,456,363 for 2018 (a reduction of \$365,599 over 2016 approved costs).

c. O&M Credit Calculation

The O&M Credit calculation is adjusted to reflect the outcome of the Company's last natural gas rate case in Docket No. G002/GR-09-1153. The 2018 forecast amount is a credit of \$72,310 – no change from the 2016 approved amount.

d. Gas Tracker Carryover

The Gas Tracker Carryover represents continuing balances from previous periods. For 2018, it is forecast at \$351,267. It was at a credit balance of (\$466,208) for 2016. This is an overall increase of \$817,475. The Company also notes that the November 25, 2008 Order requires that they credit any carbon offsets or credits through the SEP rider, but there have been no such revenues to date.

e. Rate of Return

Ordering point number 5 in the Commission's August 24, 2017 Order approved use of the capital structure from Xcel Electric's 2013 rate case and also approved a 9.04 return on equity from Xcel's Gas Utility Infrastructure Cost (GUIC) rider in Docket No. G-002/M-16-891. The Company notes it has complied by using both the stated capital structure and the 9.04 return on equity in their SEP calculations.

2. Is the proposed timing and method of SEP-related cost recovery in Xcel's petition consistent with the Commission's August 24, 2017 Order?

On August 24, 2017 the Commission issued its "Order Continuing Recovery of Costs through the State Energy Policy Rider and Other Action", Docket No. G-002/M-17-174. The Department found Xcel to be in compliance with ordering points 1, 2, 4, 5, 7, 8 and 10. However, the Department identified compliance issues with ordering points 3, 6 and 9.

[OP 3] Xcel Gas shall not prorate its accumulated deferred income taxes in the SEP rider.

[OP 6] Xcel Gas shall submit an annual compliance filing by each March 1 containing the actual and forecasted information needed to determine any true-up amount to be recovered from or returned to ratepayers as a result of the operation of the SEP rider. Xcel shall submit a miscellaneous filing to establish new SEP rider rates

for the subsequent fiscal year, incorporating amounts anticipated to be incurred and including any true-up amounts for the operation of the SEP rider during the current year.

- [OP 9] Xcel Gas shall recalculate the 2017 SEP rider revenue requirements and factor, to incorporate all of the Commission's decisions herein and shall submit revised schedules and factors reflecting these modifications, highlighting the values that differ from the initial filing's schedules.

<i>Issue</i>	<i>Xcel Gas</i>	<i>The Department of Commerce</i>
<i>2017 SEP Proceeding (for 7/17 – 6/18 time period)</i>	Combine rate with 2018 rider rate (for 7/18 – 6/19).	Implement a 2017 rider rate not before July 1, 2018.
<i>Historically based rate implementation</i>	Xcel Gas “does not believe the Commission decided to permanently change the SEP Rider into a historical recovery mechanism”. Xcel notes that such a change would require notice and a full record to be developed	The Department states that “the IRS has been clear that, if rates are implemented subsequent to the end of the test year used to set rates, no proration is needed, and ratepayers thus receive full credit for their prepayment of the utility’s income taxes”.
<i>ADIT Proration</i>	Proposes new ADIT proration treatment through review of IRS PLR’s and Deloitte Tax methodology review. Result is to prorate ADIT for forward looking period (7/1/2018-6/30/2019 for 2017 and 2018 SEP proceedings). Proration methodology treats each month as a separate test period where the month’s ADIT increase/decrease is separately prorated. Results: in keeping with recent IRS guidance, eliminate risk of losing use of accelerated depreciation methods for shareholders, faster collections with less variability due to carryovers.	No ADIT proration. Not needed due to shift to historical basis on implementation date. Results: simpler calculation method, improved accuracy. Increased regulatory lag.
<i>Sales used in rate calculation</i>	Use of Xcel’s estimated sales of 901,480,683 to update 2017-2018 SEP proceedings resulting in a factor of \$0.001959. Results: Company estimated sales should be reflective of future business results. Xcel believes their estimates to be accurate.	Use of 2016 actual sales of 971,043,548 to update the 2017-2018 SEP proceedings resulting in a factor of \$0.001576. Results: historical rate based on actual sales, no estimation error, however actuals may not be reflective of future. Department believes Company has incentive to underestimate sales, resulting in overestimated rate.

B. Xcel's 2018 SEP Rider Factor

One of the Commission's key decisions is whether Xcel Gas should be allowed to forego complying with the previously issued order which required the Company to use an historical rate implementation with no proration of accumulated deferred income taxes. If so, should Xcel Gas be allowed to use its proposed method of embedded proration?

1. Accumulated Deferred Income Taxes (ADIT) Treatment

a. Background

On June 21, 2018, FERC instituted proceedings to examine the methodology for public utilities to calculate Accumulated Deferred Income Tax (ADIT) balances in their projected test years and annual true-up calculations for transmission formula rates.

In the background section of its June 21, 2018 Order,⁷ FERC stated the following:

“Under Commission ratemaking policies, income taxes included in rates are determined based on the return on net rate base that is calculated using straight-line depreciation. However, in calculating the actual amount of income taxes due to the Internal Revenue Service (IRS), companies generally are able to take advantage of accelerated depreciation. Accelerated depreciation will usually lower income taxes payable by companies during the early years of an asset's life followed by corresponding increases in income taxes payable during the later years of an asset's life when the depreciation is lower. This means that a company's income taxes owed to the IRS during a period will differ from its income tax expenses used for Commission ratemaking purposes during the same period. The difference between the income taxes received by a company in its rate based on straight-line depreciation and the actual income taxes owed to the IRS by the company are reflected in an ADIT account. Because the resulting balance in an ADIT account effectively provides the company with cost-free capital, the Commission generally requires a company to subtract the ADIT from rate base, thereby reducing customer charges. The reduction to rate base is diminished as the ADIT reverses due to actual taxes owed to the IRS subsequently exceeding the income taxes calculated based on straight-line depreciation. ***This method of passing the time value of benefits from accelerated depreciation on to ratepayers throughout the asset's life is referred to as tax normalization.***”⁸ (emphasis added.)

“The depreciation normalization rules of the Internal Revenue Code and the IRS regulations (Normalization Rules) mandate the use of a very specific proration procedure in measuring the amount of ***future test period ADIT*** that can reduce rate base. Section 1.167(l)-1(h)(6)(ii) of the IRS regulations requires that, ***if a utility***

⁷ June 21, 2018; 163 FERC 61,200; ORDER INSTITUTING SECTION 206 PROCEEDINGS, COMMENCING PAPER HEARING PROCEDURES, AND ESTABLISHING REFUND EFFECTIVE DATE

⁸ Ibid. Pages 2-3.

uses solely a future period (projected test year) to determine depreciation, ‘the amount of the reserve account for the period is the amount of the reserve at the beginning of the period and a pro rata portion of the amount of any projected increase to be credited or decrease to be charged to the account during such period.’ The pro rata amount of any increase during the future portion of the period is determined by multiplying the increase by a fraction, the numerator of which is the number of days remaining in the period at the time the increase is to accrue, and the denominator of which is the total number of days in the future portion of the period.”⁹ (emphasis added.)

The timing of test periods is critical in determining the need for normalization through proration adjustments.

b. Rate Implementation Timing

If the implementation date of the rider rate is after the test period used in determining the rate, then the rate is historical and calculations for ADIT proration are *not* required. However, if the rate is implemented before the end of the test period, then ADIT proration is required to prevent ratepayers from gaining the value of accelerated depreciation and its tax impacts. Violation of IRS ADIT proration rules on tax normalization could result in the utility being barred from using accelerated depreciation methods for income tax reporting purposes.

c. Test Period Timing

Often, test period timing will include both actual and projected numbers. In its current filing, Xcel Gas used actual data (without ADIT proration) for 7/1/2017-6/30/2018 and forecast data from 7/1/2018 through 6/30/2019. Since 7/2018-6/2019 is projected data, and the rate was planned to be implemented on a future basis, Xcel Gas has applied ADIT proration to this projected period.

If Xcel Gas is not authorized to implement its 2018 SEP rate (for the 7/18 through 6/19 time period) until 7/1/2019, then everything would be historically based. ADIT proration would be unnecessary. Note, however, that Xcel’s regulatory lag would be increased by one full year. Because Xcel’s last rate case was filed in 2009 with a 2010 test year, this rider has already significantly relieved Xcel from regulatory lag. A one year lag between July 2018 and July 2019 is a much smaller and less significant period of time than 2010 to 2018.

C. Actual Implementation Date of Rate Factor Adjustment

Xcel Gas calculated its proposed natural gas SEP rate factor assuming all components are approved for eligibility, and are effective July 1, 2018 to June 30, 2019. If actual implementation occurs after July 1, 2018, Xcel proposed that the 2018 SEP Rider rate factor be adjusted to recover the approved program costs over the remaining months of the period, through June 30, 2019. This approach ensures that the cost recovery matches the approved eligible costs.

⁹ Ibid., Pages 2-3.

Below is a table illustrating the impact of a December, 2018 implementation date. This recalculates the Gas Rate/therm using Xcel Gas' December, 2018 through June, 2019 forecasted therms (see middle column).¹⁰

Gas Rate Factor - Effect of Implementation Dates			
	2018 Fcst with July 2018 Implementation (1)	2018 Fcst with Dec 2018 Implementation (2)	2019 Fcst with July 2019 Implementation (3)
Revenue Requirement	1,766,059	1,766,059	1,377,227
Number of Months Fcstd	12	7	12
Forecasted Therms	901,480,683	639,714,146	892,773,230
Gas Rate/therm	0.001959	0.002761	0.001543
Residential bill impact/Month	0.14	0.19	0.11
Residential bill impact/Year	1.65	2.33	1.30

(1) and (3) Xcel Gas data from Supplemental Reply Comments, Revised Attachment A2, May 14, 2018

(2) Calculated by Staff based on (1) with a 7 month recovery period

The numbers in this table were provided by Xcel and include its projection for the SEP rate factor that could be in effect in July 1, 2019 after it files its next SEP rider petition.

D. Forecasted or Historical Test Periods in Future SEP Rider Filings

The main issue with respect to the 2018 SEP factor is timing: historical data versus forward-looking data.

Xcel has requested the Commission to authorize its proposed methodology for the currently pending Company rider filings. It does not commit to adapting its proposal in future SEP rider filings or other rider dockets to what it was ordered to do in the 17-174 Docket and Xcel requests no commitment from the Commission regarding future treatment. That is, Xcel would agree to not use this authorization as an argument for acceptance of the methodology authorized in this proceeding in future proceedings.

Almost all rider filings, including GUIC riders, involve some degree of forecasting to balance the desire to be accurate while reducing the amount of regulatory lag. The Commission may wish to consider the overall impacts of ordering Xcel to use purely historical data while allowing Xcel (and other utilities) to use forecasting in other rider filings. While no party disputes that every docket is considered on its own merits, the Commission may consider providing additional guidance as to its expectations for future rider filings.

The treatment of ADIT and the use of a historical or forecasted time period is a disputed issue between the utility and the Department (and in some cases the OAG) in almost every pending petition that involves a rider with a forecasted time period. This is a list of some of those

¹⁰ Xcel Gas Supplemental Reply Comments on May 25, Revised Attachment A2.

dockets. Most of these involve larger dollar amounts than is at issue in this proceeding and in the Minnesota Power RES rider, in docket 18-375, which is also on the agenda for this meeting.

Partial List of Pending Dockets in which the Treatment of ADIT is a Disputed Issue

Company	Docket No.	Rider
Great Plains Natural Gas Co.	G-004/M-18-282	Gas Utility Infrastructure Charge (GUIC)
Minnesota Energy Resources Corp.	G-011/M-18-281	GUIC
Xcel Energy	G-002/M-17-787	GUIC
Xcel Energy	E-002/M-17-797	Transmission Cost Recovery (TCR)
Xcel Energy	E-002/M-17-818	Renewable Energy Standard (RES)
MP	E-015/M-18-375	Renewable Resource Rider (RRR)

VI. Decision Alternatives

2017 SEP Compliance filing

1. Accept the compliance-related sections of Xcel's petition as being in compliance with the Commission's August 24, 2017 Order, in docket 17-174. (Xcel)
2. Accept Xcel's entire petition as a compliance filing only. (DOC)

2018 SEP Rate Factor

3. Authorize Xcel to implement its initially proposed 2018 SEP Rider adjustment factor of \$0.001960 per therm to be effective as of the first of the month following the issuance of the Commission's order in this docket. (Xcel, initial alternative)
4. Authorize Xcel to implement its proposal for a revised 2018 SEP Rider adjustment factor of \$0.001959 per therm to be effective as of the first of the month following the issuance of the Commission's order in this docket. (Xcel, preferred alternative)
5. Deny Xcel's proposed 2018 SEP rate factor[s],¹¹ instead require Xcel to use the lower docket 18-184 revenue requirement amount of \$1,530,774 to set a factor of \$0.001576 per therm to be effective as of the first of the month following the issuance of the Commission's order in this docket. (DOC)

¹¹ The Department concludes that Xcel Gas' proposed SEP adjustment factor is effectively an inappropriate request for reconsideration of the Commission's 17-174 Order and would violate the Commission's 17-174 Order if implemented.

Actual Implementation Date Rate Factor Adjustment

6. If the Commission adopts decision alternative 4 or 5, then authorize Xcel Gas to adjust the rate charged based on the implementation date: dividing the revenue requirements by the remaining months of forecasted sales for the period the rate factor is implemented. (Xcel)
7. If the Commission adopts decision alternative 4 or 5, do not authorize Xcel Gas to adjust the rate charged based on the implementation date to shorten the number of months of forecasted sales on which the SEP rate factor is based.

Compliance Filing

8. Require Xcel to make a compliance filing within 10 days of the Commission's order in this docket with its revised SEP rider tariff language.

Modification to SEP Natural Gas Tariff & Forecasted or Historical Test Periods in Future SEP Rider Filings

9. Authorize future SEP rider filings to be based on: a) a future test period, b) the proration of accumulated deferred income taxes (ADIT) and c) the natural gas sales period used in calculating the rider rates. (Xcel, initial filing).
10. Condition authorization of Xcel's use of its proposed methodology for the currently pending Company rider filings, with no commitment from the Commission regarding future treatment. (Xcel, second supplemental reply comments)
11. Condition authorization of Xcel's use of its proposed methodology in this SEP rider filing only, with no commitment from the Commission regarding future treatment.
12. Prohibit Xcel from using this outcome as an argument for acceptance of the methodology authorized in this proceeding in future proceedings. (Xcel, second supplemental reply comments)
13. Require future Xcel SEP rider filings to be based on a historical test period. (DOC)