

May 18, 2015

Daniel P. Wolf
Executive Secretary
Minnesota Public Utilities Commission
121 7th Place East, Suite 350
St. Paul, Minnesota 55101-2147

RE: **Comments of the Minnesota Department of Commerce, Division of Energy Resources**
Docket No. E017/S-15-411

Dear Mr. Wolf:

Attached are the *Comments* of the Minnesota Department of Commerce, Division of Energy Resources in the following matter:

In the Matter of the Petition of Otter Tail Power Company for Approval of its 2015 Capital Structure and Permission to Issue Securities.

The petition was filed on May 1, 2015 by:

Brian Carlson
Vice President, Financial Planning
Otter Tail Corporation
44334 18th Avenue Southwest
Fargo, ND 58106-9156

The Department recommends that the Public Utilities Commission **approve the capital structure and the issuance of securities.**

Sincerely,

/s/ EILON AMIT
Statistical Analyst

EA/ja
Attachment

BEFORE THE MINNESOTA PUBLIC UTILITIES COMMISSION**COMMENTS OF THE
MINNESOTA DEPARTMENT OF COMMERCE
DIVISION OF ENERGY RESOURCES**

DOCKET No. E017/S-15-411

I. BACKGROUND

On May 1, 2015, Otter Tail Power Company (Otter Tail, OTP, or the Company) petitioned the Minnesota Public Utilities Commission (Commission) for approval of its proposed capital structure. The Company also requests that the Commission's approval of its capital structure remain in effect from the date of the Commission's Order in this matter until the Commission issues a subsequent capital structure Order for OTP.

The Company requests Commission approval of the following capital structure as of December 31, 2015.

	December 31, 2015	
	Thousand Dollars	%
Long-Term Debt	\$445,000	46.3%
Common Share Equity	\$500,064	52.1%
Short-Term Debt	\$15,209	1.6%
Total Capitalization	\$960,273	100.0%

The Company also requests approval of the following contingencies and securities issuances during the period for which the Commission's 2015 Capital Structure Order is in effect:

- a range of 10 percent around the 2015 common equity ratio of 52.1 percent (i.e., a range of 46.9 percent to 57.3 percent),¹
- any securities issuance that results in an equity ratio within this range, or that would not result in an equity ratio outside this range for more than 60 days,

¹ The Company miscalculated the range of $\pm 10\%$ to be 47.1% to 57.1%. The correct range is 46.9% to 57.3%.

- a cap of 10 percent over OTP’s total capitalization of \$960,273,000 (i.e., a total capitalization of \$1,056,300,000),
- any securities issuance that results in total capitalization below the cap (i.e., below \$1,056,300,000) or that would not result in total capitalization above the cap for more than 60 days, and
- short-term debt not to exceed 15 percent of total capitalization (about \$144 million) for more than 60 days. OTP shall ask for Commission approval as soon as it expects its short-term debt to exceed the approved cap for more than 60 days.

In addition, OTP states that it will seek approval from the Commission for any securities issuance as soon as the Company has reason to believe that any such issuance would cause the common equity ratio or total capitalization to fall outside the approved contingency ranges for more than 60 days.

II. DETAILS OF OTTER TAIL’S PROPOSAL

Otter Tail requests that its proposed capital structure be in force from the date of the Commission’s Order in this petition until the Commission issues a subsequent capital structure Order for OTP. Table 1 below provides OTP’s recent capital structures and OTP’s 2015 projected capital structure.

**Table 1: OTP’s Recent Capital Structures
(in Thousands of \$)**

	July 31, 2014 (Actual)		Dec. 31, 2014 (Actual)		Dec. 31, 2015 “Projected” (1)	
Short-Term Debt	\$0	0.0%	\$0	0.0%	\$15,209	1.6%
Current Maturities of LTD	\$0	0.0%	\$0	0.0%	\$0	0.0%
Long-Term Debt Net	\$455,000	51.6%	\$445,000	50.2%	\$445,000	46.3%
Preferred Shares	\$0	0.00%	\$0	0.0%	\$0	0.0%
Common Share Equity	\$415,612	48.4%	\$441,523	49.8%	\$500,064	52.1%
Total Capitalization	\$861,612	100.0%	\$886,523	100.0%	\$960,273	100.0%

(1) The “Projected” column reflects the Company’s best estimate of the proposed capital structure as of December 31, 2015.

In the Petition, OTP states that its capital expenditure plans for 2015 primarily consist of maintenance of its generation, transmission and distribution facilities, along with expenditures for the Company’s share of the CapX 2020 transmission project and its share of Big Stone Area Transmission projects and OTP’s share of an Air Quality Control System at

Big Stone Plant (AQCS). In Attachment No. 10B, the Company identifies generation (energy supply), transmission, distribution and general projects totaling about \$147.7 million for the year ending December 31, 2015. The three largest expected project expenditures are Big Stone AQCS at about \$53.025 million, Big Stone area Transmission at about \$31.007 million and Distribution at about \$16.15 million.

Otter Tail plans to use internally generated cash flows, short-term debt, and equity contributions from its parent company to meet its financing needs for its 2015 capital expenditure plan. For its short-term borrowing, OTP plans to draw on its \$170 million credit facility to support its working-capital needs and capital expenditure program until such time as it makes sense to convert these short-term borrowings into a long-term financial arrangement. Regarding equity, OTP is a wholly-owned subsidiary of Otter Tail Corporation (OTC) and, therefore, does not issue its own equity. Instead, OTP estimates equity contributions from Otter Tail Corporation during the authorized period to be \$46,500,000.

III. DEPARTMENT ANALYSIS

A. CAPITAL STRUCTURE

To check the reasonableness of OTP's proposed 2015 capital structure, the Department compared the equity ratio in the Company's capital structure with the average equity ratio of electric utilities that are risk-comparable to OTP. The 2014 average equity ratio for publicly traded electric utilities with bond ratings from BBB- to BBB+ (Otter Tail's bond rating is BBB) was 47.41 percent.² The 2014 average debt ratio for the group was 50.27 percent. The DOC notes that the Company's proposed equity ratio of 52.1 percent is slightly higher than the group's average equity ratio, and its proposed debt ratio is lower than the group's average debt ratio. Therefore, OTP's capital structure does not raise concerns about any equity ratio that is too low to ensure the financial health of the Company.

Based on the above discussion, the DOC concludes that OTP's proposed 2015 capital structure is reasonable for the purpose of this Petition.

B. CONTINGENCIES

1. Common Equity Ratio

OTP requests a ± 10 percent contingency range around its requested equity ratio. This range is as follows:

² Source: Compustat Data from Standard & Poor's Research Insight, March 31, 2015. (See Attachment No. 1).

Contingency Range for OTP's Equity Ratio

	<u>Low</u>	<u>Requested</u>	<u>High</u>
Common Equity	46.9%	52.1%	57.3%

The DOC concludes that this range is reasonable because it provides the Company with adequate financial flexibility, keeps OTP on sound financial footing and allows the Commission sufficient oversight.

2. *Short-Term Debt*

OTP requests a contingency to issue short-term debt not to exceed 15 percent of total capitalization (about \$144 million) at any time while the 2015 capital structure is in effect.³ This request for flexibility is consistent with the flexibility allowed by the Commission for OTP's 2014 capital structure. The DOC concludes that the 15 percent cap would allow the Company needed and reasonable flexibility given the expected short-term fluctuations in the Company's revenues and expenditures.

3. *Total Capitalization*

The Company proposes total capitalization of \$1,056,300,000 including a contingency amount of \$96,027,000 or 10 percent of the total capitalization. This proposed contingency would allow flexibility in the Company's funding of utility construction and unforeseen business or financial conditions that might develop during the year. In addition, the contingency is needed because, during a refinancing, both the new and old debt issues may be outstanding temporarily beyond the requested 60-day window. Based on the above discussion, the DOC concludes that OTP's request for a contingency of \$96,027,000 for total capitalization is reasonable.

C. *FLEXIBILITY TO ISSUE SECURITIES*

OTP plans to use internally generated cash flows, short-term debt and equity from its parent company during 2015 to meet any future operational and financial needs. However, to be able to react to changing market conditions, the Company may need to issue long-term debt as well. Therefore, the Company requests authority to issue, as need, any of the following securities: long-term debt, common equity and short-term debt. Such issuances would be for the purpose of financing the Company's capital expenditure program, meeting current maturities and sinking fund requirements and for other corporate financial requirements. Any such issuance that would cause the total capitalization or the equity ratio to exceed the 10 percent contingencies for periods exceeding 60 days would first have to be approved by the Commission. The DOC notes that OTP does not issue common equity. However, it may

³ The Company miscalculated the 15 percent cap as \$158 million. The correct number is \$144 million.

receive equity contribution from OTC. Attachment No. 10A of the Company's filing shows that the parent company, OTC, expects to contribute \$44 million of equity to OTP in 2015. As shown in the Company's Attachment No. 10, the Company plans to finance its 2015 capital expenditures and other corporate expenditures using mostly internally generated funds, common equity and short-term debt.

D. ADDITIONAL FILING REQUIREMENTS

The Commission's August 1, 2014 Order in OTP's 2014 capital structure petition (Docket No. E017/S-14-381) included the following order points:

6. Required OTP to provide, within 20 days after each non-recurring issuance of securities, the following information:
 - a. the specific purposes for individual issuances;
 - b. the type of issuances;
 - c. the timing of issuances;
 - d. the amounts of issuances;
 - e. issuance cost (for common equity issuances, including price per share), and
7. Required OTP to provide, in its next capital structure filing, an exhibit showing a general projection of capital needs, projected expenditures, anticipated sources, and anticipated iteming, with the understanding that such exhibit is not intended to require dollar-for-dollar on the uses identified in the exhibit or to limit issuances to project-specific financing. The exhibit need not list short-term, recurring security issuances.
8. Required OTP to provide in its next annual capital structure filing, a schedule comparing its actual capital investments in the past year with the capital investments projected by OTP in its previous capital structure filing.
9. Required OTP to provide in its next annual capital structure filing, the Company's investment plan not only for the next year, but also for at least the next five years.

The Department discusses these reporting requirements below.

a. Information Regarding Non-Recurring Issuance of Securities

ON November 20, 2014, OTP submitted a compliance filing in Docket No. E017/S-14-381 containing the required information regarding a November 3, 2014 amendment to an existing credit agreement. The Department concludes that OTP has complied with order point 6 noted above.

b. Projected Capital Needs and Anticipated Resources

Attachments 10A and 10B of the Company's filing provide the information required by the Commission Order. Attachment 10A, pages 1 and 2, show the sources of financing OTP's various expenditures and OTP's expenditures by general category for the years 2014 and 2015. Attachment 10B of the Company's filing provides OTP's projected expenditures for the period 2015-2019 by four categories: Energy Supply, Transmission, Distribution and General.

Based on its review of Attachments 10A and 10B, the Department concludes that OTP's Petition complies with Requirement No. 7 above.

c. Comparison of Actual and Projected Capital Investments

Attachment 10C of the Company's filing provides the required information. It shows that OTP's actual capital expenditures were \$14,769,000 less than its expected 2014 capital expenditures. This deviation represents about 9.1 percent of the expected 2014 capital expenditures. The most significant deviations are in transmission (2.6 million), CapX 2020 (\$3.97 million) and Big Stone AQCS (about 4.9 million). The footnotes to Attachment No. 10C provide explanation for the discrepancy. For all the three categories above, the projected expenses were deferred for a later period than expected. The Department concludes that the lower expenditures were reasonable.

d. The Company's Investment Plans

The Company projected investment for each of the years 2015 through 2019 is provided in the Company's Attachment 10B. Based on its review of the Company's Attachment 10B, the Department concludes that the Company complied with the Commission's Requirement No. 3 above.

Order Point 3 of the Commission's May 12, 2009 Order in Docket No. E, G999/Ci-08-1416 states:

3. Starting with the utilities' next annual capital structure filings, the utilities shall include a report of actual issuances and uses of the funds from the prior year. The report will be for information purposes only and need not cover short-term, recurring security issuances.

Attachment No. 10C of the Company's filing provides the information regarding uses of funds. Uses totaled \$146,961,000 allocated to transmission, distribution, general, CapX 2020, Big Stone area transmission and Big Stone AQCS. The funds are shown on page 2 of the Company's Attachment No. 10. The total cash requirement for 2014 was

\$147,201,000 and the total cash flow for 2014 was \$146,591,000. The shortfall of \$610,000 was financed by reducing the cash balance of \$3,539,000 at the end of 2013 to \$2,928,000 at the end of 2014. Based on its review of the Company's Attachments 10C and 10, the Department concludes that OTP's petition complies with order point 3 above.

IV. DEPARTMENT RECOMMENDATIONS

Based on its review and analysis of OTP's 2015 capital structure petition, the Department recommends that the Commission:

1. Approve OTP's requested 2015 capital structure; this approval to be in effect until the 2016 capital structure Order is issued. OTP shall file its next securities issuance petition no later than May 2016.
2. Approve OTP's equity ratio of 52.1 percent and a contingency range of minus/plus 10 percent around the approved equity ratio (46.9% to 57.3%). Equity ratios outside this range may not exceed a period of 60 days without prior Commission approval.
3. Approve OTP's proposed total capitalization of \$960,273,000 with a contingency cap of 10 percent (or \$1,056,300,000). The Company may not exceed its total capitalization, including the requested contingency amount, for a period exceeding 60 days without prior Commission approval.
4. Approve OTP's request to issue short-term debt not to exceed 15 percent of OTP's total capitalization (i.e., \$144,040,950). OTP's short-term debt may not exceed 15 percent of its total capitalization for a period exceeding 60 days without prior Commission approval.
5. Approve any securities issuance during this period in which this Order is in place that would not result in an equity ratio outside the approved range. Securities issuances resulting in an equity ratio outside this range may not exceed a period of 60 days without prior Commission approval.
6. Require OTP to provide, within 20 days after each non-recurring issuance of securities, the following information:
 - a. the specific purposes for individual issuances;
 - b. the type of issuances;
 - c. the timing of issuances;
 - d. the amounts of issuances;

- e. issuance costs (for common equity issuances, including price per share); and
 - f. interest rates.
7. Require OTP to provide, in its next capital structure filing, an exhibit showing a general projection of capital needs, projected expenditures, anticipated sources, and anticipated timing, with the understanding that such exhibit is not intended to require dollar-for-dollar on the uses identified in the exhibit or to limit issuances to project specific financing. The exhibit need not list short-term, recurring security issuances.
 8. Require OTP to provide in its next annual structure filing, a schedule comparing its actual capital investments in the past year with the capital investments projected by OTP in its previous capital structure filing.
 9. Require OTP to provide in its next annual capital structure filing, the Company's investment plan not only for the next year, but for at least the next five years.

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OTTER TAIL COMPARISON GROUP

RISK REPORT

SIC Code	Stock Ticker Symbol	Most Recent BETA	Standard Deviation	S&P Debt Rating	2014 Long Term Debt	2014 Equity Ratio
4911	AEP	0.337	0.044	BBB	49.70	50.30
4911	BKH	0.801	0.056	BBB	47.95	52.05
4911	BIP	0.771	0.048	BBB+	51.62	34.38
4911	CNL	0.497	0.046	BBB+	45.34	54.66
4931	DTE	0.242	0.038	BBB+	50.00	49.95
4911	EIX	0.389	0.048	BBB+	44.55	46.79
4911	EE	0.351	0.048	BBB	53.54	46.46
4911	EDE	0.350	0.052	BBB	50.63	49.37
4911	ETR	0.282	0.050	BBB	54.85	43.81
4911	EXC	0.447	0.057	BBB	45.33	52.81
4911	FE	0.215	0.060	BBB-	60.69	39.31
4911	GXP	0.496	0.048	BBB+	49.04	50.42
4911	HE	0.130	0.047	BBB-	49.61	49.45
4911	IDA	0.542	0.046	BBB	45.20	54.75
4911	OTTR	1.007	0.063	BBB	46.53	53.47
4911	POM	0.248	0.051	BBB+	51.20	47.39
4911	PNM	0.489	0.054	BBB	47.61	51.01
4911	POR	0.412	0.040	BBB	52.66	47.34
4911	PPL	0.224	0.040	BBB	58.05	41.95
4911	TAC	0.459	0.050	BBB-	46.01	35.54
4911	UIL	0.578	0.048	BBB	55.57	44.43

Average 50.27
 Minimum 44.55
 Maximum 60.69
 St. Deviation 4.42
 Source: Copustat Data Base March 31,2015

CERTIFICATE OF SERVICE

I, Linda Chavez, hereby certify that I have this day served copies of the following document on the attached list of persons by electronic filing, e-mail, or by depositing a true and correct copy thereof properly enveloped with postage paid in the United States Mail at St. Paul, Minnesota.

MINNESOTA DEPARTMENT OF COMMERCE – COMMENTS

Docket Nos. **E017/S-15-411**

Dated this **18th** day of **May, 2015**.

/s/Linda Chavez

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